

Stronger Connections. Better New Zealand.

ANNUAL INTEGRATED REPORT 2018



Welcome – Tēnā koutou

Rail's proud 155-year history of enabling growth in New Zealand has been revitalised over the past year with a new coalition Government signalling its strong support for expanding rail's role in the economy.

For KiwiRail, this revival of rail is the culmination of four years of reform, with our plan to standardise our assets, simplify our business and invest in our people to deliver improved productivity and lay the groundwork for an exciting future of growth.

Our history is one of adapting to meet customers' needs and evolving as global supply chains develop.

KiwiRail's purpose, developed this year, of 'Stronger Connections. Better New Zealand' evokes this plan for a bigger, bolder role for rail.

In the 1800s engineers designed a rail network that could operate in New Zealand's uncompromising landscape, building wooden infrastructure to carry the steel tracks that ran across swamps, rugged mountains, dense forests and rivers, connecting otherwise isolated communities and industries to the market.

That mission has not changed, though the way we service those customers has. That change will continue in

the decades to come. Technological disruption, changing demographics, the future of work and new skills, a surge in rail commuters, a burgeoning tourism market and the advent of big ships in our ports will guide much of our strategy over the next few years.

Driving economic growth across New Zealand's cities and regions is part of KiwiRail's DNA. It is where we come from, it is who we are now, and it is what we will strive to be in the decades and generations to come.

Contents

| | | |
|---|--|---------------------------------------|
| Overview of our business | Capitals review | Governance review |
| At a glance..... 4 | Financial 28 | The KiwiRail Board 54 |
| Awards..... 5 | <i>Case study - Record season for Interislander tourism</i> 30 | The KiwiRail Executive Team 56 |
| Our purpose..... 6 | People 31 | How we are governed..... 58 |
| Management review | <i>Case study - Revitalising health and safety action teams</i> 34 | Statutory review |
| Our reporting approach 9 | Assets..... 35 | Key Performance Indicators 62 |
| How KiwiRail creates value 10 | <i>Case study - Supporting regional development</i> 37 | Vote Transport 64 |
| Chair's message..... 12 | Skills and know-how 38 | Financial statements..... 66 |
| After the earthquake 13 | <i>Case study - Safety technology</i> 40 | Independent Auditor's Report 96 |
| Milestones 14 | Relationships 41 | Directory 99 |
| Chief Executive's report..... 16 | <i>Case study - Toi Toi</i> 45 | |
| Our progress 2014-2018 19 | Environment 46 | |
| The Value of Rail in New Zealand 20 | United Nations Sustainable Development Goals 49 | |
| Business review | Strategic outlook..... 51 | |
| Performance of our business units 22 | | |
| <i>Case study - Our integrated business</i> .. 26 | | |

Front cover photo: KiwiRail commissioned local artist Ben Foster to create a sculpture of rail recovered during our rebuild efforts etched with the names of the many impacted communities, to mark the rebuild of the rail line and the challenges faced by the local communities following the Kaikoura earthquake. See page 13 for more details.



KiwiRail haka Te Iho Matua being performed at Toi Toi Maori Leaders Programme 2018 graduation.

At a glance

Highlights from FY18



Financial

- \$49 million operating surplus¹
- \$94 million underlying operating surplus² excluding \$45 million impact from Kaikoura, exceeding FY17 underlying result
- \$7 million of efficiency and waste savings were delivered, building on the \$45 million achieved in previous years
- Forestry revenue up 12% with strong export demand
- Bulk freight revenue up 6% with strong milk and coal volumes



People

- Staff engagement hits record high with Employee Net Promoter Score reaching +1 in 2018, from a low of -21 in 2016 and -7 in 2017
- Total Recordable Injury Frequency Rate decreases by 10% over previous year
- 6,700 Safe Work Conversations recorded over the year
- Toi Toi Maori Leadership programme launched
- High Performance High Engagement (HPHE) project at Hutt Workshops traction motor maintenance facility leads to improved safety and efficiency



Assets

- Two major projects underway to consider long term strategy for interisland ferries and future rolling stock fleet
- \$171 million (including contributions from other parties) capital expenditure targeted on key freight lines and improving resilience and operational capacity to meet increasing freight volumes
- On Time Performance (OTP) of 91% for all freight trains
- Napier to Wairoa line sees first work train in six years preparing the line for resuming log trains
- Final testing of 15 new locomotives underway



Skills and know-how

- Main North Line reopened to restricted freight services just 10 months after the Kaikoura earthquake, and work continues to enable daytime running of trains
- Workforce management system introduced in nine weeks using agile principles



Relationship

- Project Wā heke launches to help develop a customer-focused 10-year growth strategy
- Customer satisfaction ratings for Interislander at 90%
- KiwiRail wins Supreme Award at AUT Business Support Awards for work with Fonterra and Port of Tauranga to boost export growth
- Social media video "Rail Safety Week 2017" is viewed more than 300,000 times



Environment

- Rail freight reduces heavy vehicle impact on New Zealand roads by 1.1 million truck trips, saving 66.3 million litres of fuel and 180,212 tonnes of CO₂ emissions
- Reached EECA energy saving target in just eight months

1. Operating surplus represents earnings before depreciation & amortisation, interest, impairment, capital grants and fair value changes.
 2. Underlying operating surplus is a non-GAAP measure used by management to assess the performance of the business. It is derived from KiwiRail's group financial statements for the year ended 30 June 2018 and excludes Kaikoura impact.

Awards



July

KiwiRail wins the Australasian Rail Industry Award for Freight Rail Excellence in recognition of its efforts to keep customers' freight moving around New Zealand following the Kaikoura earthquake

August

Great Journeys of New Zealand's TranzAlpine, Coastal Pacific and Northern Explorer scenic rail services, and the Interislander, are awarded Qualmark Gold Status

KiwiRail's Back to Basics programme is a finalist in the Diversity Works New Zealand 2017 Skills Highway Award

September

The Southdown 35/36 Roads project is awarded Public Sector Project of the Year at the Project Management Institute Awards. KiwiRail's Makatote Viaduct project is a finalist in the same category

October

KiwiRail wins the Supreme Award at the AUT Business Support Awards in recognition of its partnership with the Port of Tauranga and Fonterra, which has improved productivity, supported regional development and reduced CO₂ emissions and costs

At the AUT Business Support Awards, KiwiRail wins the International Business Export Support and Advanced Security Group Government categories

December

Video "Rail Safety Week 2017" wins the Security and Safety category at the CINERAIL International Railway Corporate Film Competition in Portugal; a second KiwiRail safety video "Trackstoppers" receives a commendation in the same category

The Institution of Structural Engineers awards the Makatote Rail Viaduct project a Structural Engineering Award for Structural Heritage

March

KiwiRail is a finalist at the 2018 New Zealand CFO Awards for Finance Team of the Year

May

KiwiRail and its partners in the North Canterbury Transport Infrastructure Recovery (NCTIR) alliance are awarded the Railway Technical Society of Australasia's Biennial Railway Project Award 2018 for the rebuild of the Main North Line following the Kaikoura earthquake

June

KiwiRail receives the 2018 Rail Heritage Trust Restoration Award for its efforts in restoring the Parnell Railway Station building

KiwiRail wins the Australasian Reporting Awards Special Award for Communication, Public Sector, for the second year running for its 2017 Integrated Report

Our purpose

Stronger Connections.
Better New Zealand.

We connect people and communities

34 million

We help commuters make more than 34 million low-carbon journeys each year

One million

We carry more than one million tourist passengers each year

20%

We enable passenger growth of 20% in Auckland over the last two years

We keep freight moving

18 million

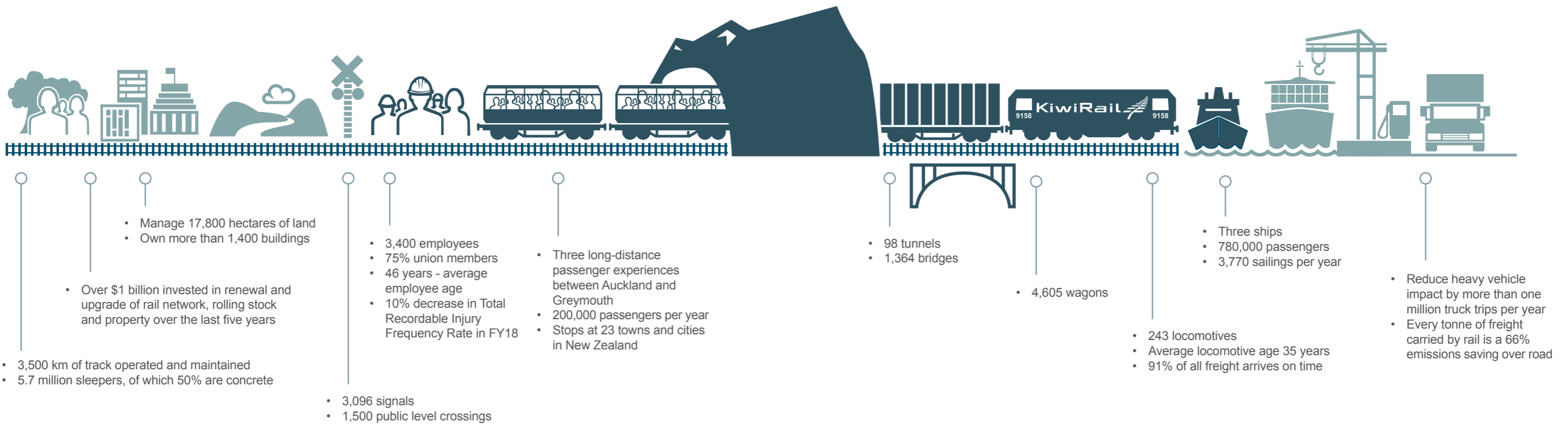
We move 18 million tonnes of freight each year

16%

We carry around 16% of New Zealand's total freight task (tonnes-km)

25%

We transport around 25% of New Zealand's exports





Phillip Lewis, Mechanical Engineer. Dunedin.

Our reporting approach

This is KiwiRail's third Integrated Report, which uses the International Integrated Reporting Council's (IIRC) framework to detail KiwiRail's business performance.

Its aim is to provide in-depth information about our relationship with stakeholders, what we do in our business and our role as a driver of sustainable and inclusive economic growth for the year to 30 June 2018.

Within the report we demonstrate how we create value for New Zealand, our stakeholders, our customers, and our business in the short, medium and long term. The report also covers key material issues, the issues that are most important to KiwiRail and its stakeholders: customer relationships, workplace health and safety, public safety, operational efficiency, energy and carbon emissions, transport resilience, commercial focus, and employee relations.

In FY18 we engaged an external agency to review the material issues

we had identified in 2016, refreshing their meaning and comparing the list for comprehensiveness against international frameworks. That work is influencing KiwiRail's evaluation of the UN Sustainable Development Goals (SDG) as we identify our priorities for the year ahead. See page 49 for more detail on our SDG work.

This report's title, "Stronger Connections. Better New Zealand", reflects KiwiRail's evolution over the past four years as we have set ourselves up for growth. The \$1.5 billion of external benefits rail delivers each year from reduced congestion and emissions, road maintenance savings and safety, are now being recognised by the public and have resulted in increased support for rail in our cities and regions.

This report is also designed to provide an overview of KiwiRail activities, to describe how each capital contributes to our strategy and to provide a transparent assessment of overall performance, future prospects and risks

in relation to finance, people, assets, knowledge, relationships and the environment.

This year there is a strong focus on the reporting capital areas of People and Environment, to reflect the work that we have undertaken over the past 12 months. The organisation has recognised the need for increased diversity and inclusiveness, and that work is paying off through increased staff engagement and Māori leadership. KiwiRail's sustainability story is still evolving, but much has been achieved in this area over the 12 months.

Regional development is a newer focus for our teams as the Government rolls out its priorities for the Provincial Growth Fund. This has increased our focus on social and environmental outcomes for New Zealanders, much of which is highlighted in the following pages.

More information on the Integrated Reporting framework can be found at: <http://integratedreporting.org>

Statement of Responsibility

We, the Board of KiwiRail, acknowledge our responsibility to ensure the integrity of this Integrated Report. In preparing and approving the content of the report, we are confident that it aligns with the principles of the International Integrated Reporting Framework.







Audit New Zealand has provided a statement of assurance for the financial statements in this report, but we have not sought external assurance of the contents of this Integrated Report.

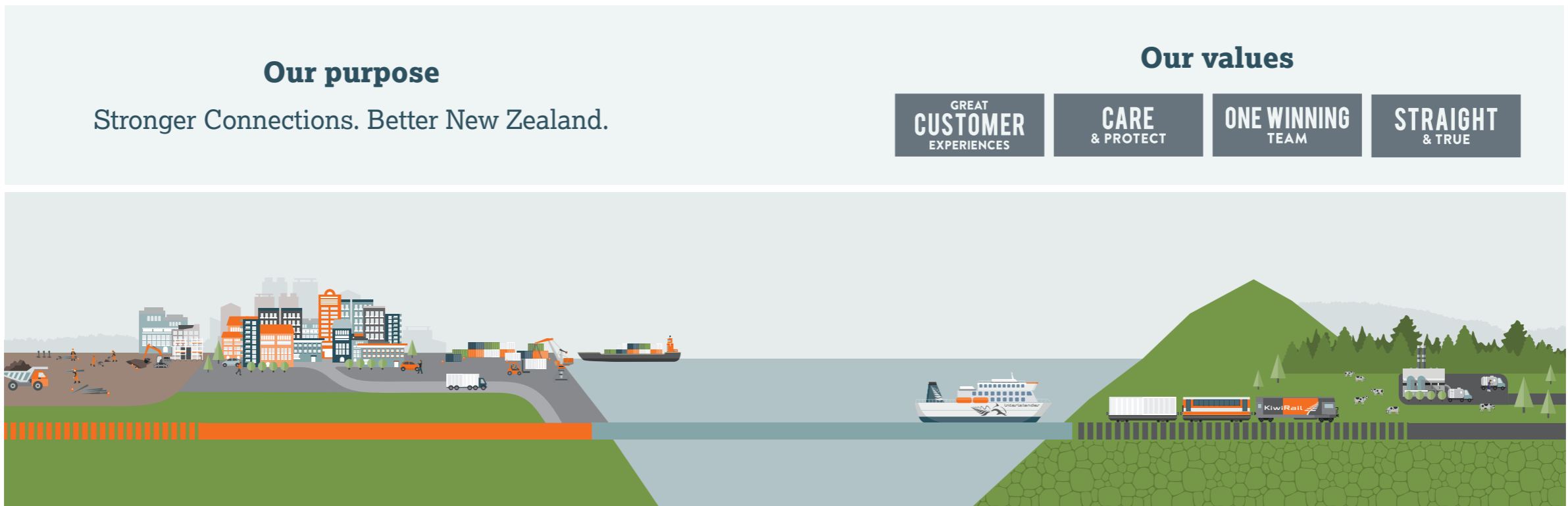
Brian Corban
Acting Chair

Mike Pohio
Director

How KiwiRail creates value

Our inputs

-  Financial
-  People
-  Assets
-  Skills and know-how
-  Relationships
-  Environment



Our purpose

Stronger Connections. Better New Zealand.

Our values

- GREAT
CUSTOMER
EXPERIENCES
- CARE
& PROTECT
- ONE WINNING
TEAM
- STRAIGHT
& TRUE

Our outcomes

-  Reliable
-  Sustainable
-  Valuable

Growing a highly-engaged, safe and productive workforce

Supporting customers to grow New Zealand's economy

Providing resilience to the New Zealand transport network

Facilitating efficient flows to/from ports

Delivering world class tourism experiences

Providing a sustainable transport alternative and reducing emissions

Connecting people and places by enabling commuter journeys

We move people

and freight

Chair's message



It is just over a decade since I joined the establishment Board of KiwiRail, serving as Deputy Chair of the new integrated rail and ferry business which marked the end of private ownership of rail operations in New Zealand.

It was July 2008. The Board was formed by then-Finance Minister Michael Cullen, was led by former Prime Minister Jim Bolger and was lauded by then-Prime Minister, Helen Clark. Re-forming an above and below rail business led by a single Board with a commercial mandate and the ability to deliver public good was a remarkable vision of what a unified KiwiRail could deliver for New Zealand. It was met with some doubt and much delight.

"New Zealand's rail network is now back in New Zealand's hands," Dr Cullen said.

"By bringing our rail system back into public ownership - following the buyback of the tracks four years ago - we will spare future generations from subsidising a private rail operator and will be able to create an integrated, sustainable transport system.

"We will now be able to make the investments necessary to develop a world-class 21st century rail system for New Zealanders."

The KiwiRail I have seen since re-joining the Board in July this year has fulfilled much of that vision. Yes, there have been tough times since formation. Not all of the necessary investments were made by successive Governments, nature

has provided many challenges, some lines have closed, our locomotives are ageing and the world-class rail system is still in development.

But what is remarkable to those of us who were there at its beginning is the culture, character and strength of the KiwiRail we see today and of what it is delivering for New Zealand. In safety, reliability and sustainability more has been achieved than many of us predicted. Rail now delivers \$1.5 billion in benefit to New Zealand each year, far exceeding the investment made by Government.

This report highlights that, for the third year running, KiwiRail has met its commitment to Government in its financial result, bar the on-going impact of 2016's Kaikoura earthquake. Twenty-five per cent of the nation's exports are carried by KiwiRail. More than 34 million commuter journeys are made on its network each year. And its Interislander fleet has on-time performance at over 90% with customer ratings that rival Air New Zealand's.

I have joined the Board again at an exciting juncture for the organisation. The Coalition Government has signalled its strong support for rail and its ability to drive regional economic growth, ease congestion in our cities and help New Zealand transition to a low-carbon economy.

The organisation has spent the past few years readying itself for the growth that is now on offer with strong tourism services, integrated relationships with the country's ports, a thriving

and engaged workforce and new strategies to grow its freight task.

Later this year a new Chair will join the Board. Former Toll Managing Director Greg Miller, like me, saw KiwiRail before and during its formation and has strong logistics and freight experience that will be invaluable.

What is critical now is achieving an integrated national transport strategy that places KiwiRail firmly where it can deliver best, through partnerships with customers, connecting communities and moving large numbers of people and goods sustainably, efficiently and at speed.

Finally, may I thank outgoing Chief Executive Peter Reidy for his leadership over the past four years. He has left the organisation in great heart and confidence, ready for the next decade ahead.

Brian Corban CNZM, QSO
Acting Chair
KiwiRail

After the earthquake

“This sculpture reminds us ... of how resilient we all are as it reaches upward”

Ben Foster, Artist

A sculpture now stands at the Kaikoura Railway Station to recognise both the immense impact of the Kaikoura earthquake on the local community, and the efforts of those rebuilding the rail line in the region.

KiwiRail commissioned internationally acclaimed Kaikoura artist Ben Foster created the sculpture, which features pieces of twisted track salvaged from IronGate, north of Kaikoura. It incorporates place names which sit along the railway line in the area.

"This sculpture reminds us that change is very much a constant, the twisted rail communicating the raw power of Mother Nature, and may stand as a constant reminder of how resilient we all are as it reaches upward," says Mr Foster.

As well as recognising the impact of the earthquake on the wider community, the sculpture also commemorates the rebuild efforts put in by KiwiRail and its partners in the North Canterbury Transport Infrastructure Recovery (NCTIR) alliance.

It was unveiled by Kaikoura Mayor Winston Gray in September 2017 at an event marking the resumption of rail freight services on the Main North Line.

The sculpture created for Kaikoura, above, is by local, internationally-acclaimed artist Ben Foster, below.



Milestones



Chief Executive's report



Tēnā koutou

There is real meaning behind the title of this year's Integrated Report: "Stronger Connections. Better New Zealand."

Last year KiwiRail published the results of the EY Study "The Value of Rail in New Zealand", a ground-breaking analysis which highlighted the \$1.5 billion in often unseen benefits that rail delivers each year. That value includes the reduced congestion in our cities, the carbon emissions savings from using rail, road maintenance costs and the fewer road fatalities and injuries on our roads.

The study quantified for the first time what taxpayers really receive for the annual investment they make in rail. And it concluded that this funding is far outweighed by the benefits. Those of us who work in rail have known this to be a fact for decades.

If rail was switched off at midnight tonight, the country would pay. We saw this first hand when the Kaikoura earthquake hit in 2016, devastating transport links in the South Island and sending thousands of trucks onto often unsuitable roads. Rail is essential for connecting the country and for making a New Zealand better place to live and do business.

Establishing those, admittedly conservative, facts about rail's value has been part of a four-year programme at KiwiRail to set the organisation on a new path for growth.

When I joined the company as Chief Executive in March 2014, I could see the immense passion our people have for KiwiRail and for what we deliver for New Zealand. Together we embarked initially on a 'back to basics' plan to drive commercial results in the business, improve service reliability, reduce safety incidents, optimise our

rail freight, ferry, tourism and property businesses and build a 'One KiwiRail' culture for our 3,400 people, with a common language and values.

It has been a significant piece of work and all our people are proud of the results. This year, as in the previous two years, we have exceeded our financial commitment to Government with an underlying EBITDA of \$94 million, up 2% on the previous year once the effects of the on-going disruption from the Kaikoura earthquake are taken into account.

That result includes sizeable gains in forestry (up 12% on the previous year), bulk freight (up 6%) and Interislander recording a record summer on its ferries. Customer satisfaction on those services has risen to a remarkable 90%. Our strong relationships with ports over the last 12 months saw most ports committing to grow volumes on rail.

The lingering effects of the 2016 earthquake are still impacting our business. We have been running only overnight freight trains on the line between Picton and Christchurch for the past year, allowing the rebuild of the road and rail to continue during the day. That has hurt our domestic freight volume which is primarily responsible for the \$45 million impact to our operating surplus. I want to personally thank our domestic freight customers for their patience and support during the recommissioning of the line.

Despite the on-going disruption to services, our safety results and culture continue to improve. KiwiRail's Total Recordable Injury Frequency Rate (TRIFR) has reduced again, building on safety improvements in previous years. This year we saw the rate of injuries again reduce by 10% on FY17. A focus on our leading indicators for safety has seen a remarkable 150% increase in the reporting of near-misses over the year and a commitment to safe work conversations in the workplace by all our people.

Our 'One KiwiRail' culture, led by our High Performance, High Engagement programme with our union partners, has been described by the Government as the 'future of industrial relations' and has had a real impact on the organisation. Employee engagement has soared from -21 in 2016 to +1 this year with an 8% increase in participation. We are evolving a 'bottom-up' culture that is driving business results and emphasises the purpose beyond profit philosophy that motivates our teams.

“ We are now primed for growth with a strong integrated platform, engaged employees and a supportive shareholder recognising the value KiwiRail drives for New Zealand.”

Diversity has been a big focus of the past four years – women in leadership roles have risen and our Toi Toi leadership programme is growing a new generation Maori leaders in the organisation. Combined, these results show the platform that KiwiRail has built over the past few years through a strategy of simplifying our business, standardising our assets and investing in our people. We are now primed for growth with a supportive shareholder recognising the value KiwiRail drives for New Zealand, and the potential for more development in regional New Zealand.

The Coalition Government has signalled their support through the new

Provincial Growth Fund (PGF), initially this year funding the reinstatement of the Napier to Wairoa line to take logging trucks off the road and reduce carbon emissions; an upgrade of the freight line in Whanganui and feasibility studies into rail opportunities in Taranaki, Southland and Kawerau. In July the first of a series of tourism proposals under the fund was announced. This is a study into the potential for a new rail service between Hokitika and Westport, which would build on the award-winning TranzAlpine Great Journey of New Zealand.

These are all important initiatives for New Zealand and will be followed by larger proposals seeking support from the fund to support new forestry and dairy projects which could take tens of thousands of trucks off New Zealand's roads improving safety further reducing carbon emissions. This will help New Zealand reach its Paris Accord targets as every tonne of freight carried by rail has 66% fewer carbon emissions than heavy road freight. We have plans to expand our tourism services to bring more high value visitors into hard to reach towns and cities, creating jobs and supporting new tourism businesses.

Alongside the PGF proposals, our people have been working on a 10-year growth strategy for KiwiRail, deep diving into the businesses of our current and potential customers for insight into how disruption is changing their industries.

From this work we have set a path for growth based on three key strategies: enabling customer success; growing through agility, initiative and collaboration; and delivering with smart assets and connected networks. Our 10-year plan will focus on finding sustainable solutions to customers' needs, diversifying and growing market share, opening up new partnering opportunities and planning a network for the future. That includes our ferry fleet, which will need to be replaced by 2025.



Matt Hermann and Justin Anderson at work in Palmerston North.

We have reorganised our teams to drive our customer focus, combining operations, network services and rolling stock under a Chief Operations Officer, Todd Moyle. With enabling technology and smaller agile work teams, we will prototype innovations to make it easier for our customers to connect to the rail and ferry network and reduce our unit costs.

We have set a new course also on sustainability, signing up to the Climate Leaders' Coalition to reduce our environmental footprint and to help other New Zealand businesses reach their carbon emission reduction targets. Transport accounts for 19% of New Zealand's overall emissions but KiwiRail is just 1% of that and driving modal shift from road onto rail is a key enabler for change.

Central to these growth strategies is a new purpose for KiwiRail, unveiled to our people just a few weeks ago, "Stronger Connections. Better New Zealand". It speaks to the critical role we play in connecting our communities, in taking New Zealand's

goods to the world, in showcasing our country to visitors and of the enviable environmental benefits rail offers. It is, like KiwiRail, aspirational for the future of New Zealand.

But this purpose and our growth strategies will require longer-term funding. KiwiRail is still dealing with the legacy of decades of underinvestment, particularly in our locomotives and wagons. Over the past 12 months we have had to unexpectedly pull dozens of ageing locomotives into our workshops for repair and we are constrained by the age and size of our fleet. We cannot grow without a commitment to our core funding for tracks, infrastructure, and rolling stock. While the Government has signalled there will be longer-term funding to come and from new sources including the National Land Transport Fund, there is still uncertainty as to how this will evolve.

Sadly, I will be leaving KiwiRail in a few weeks for a new challenge, but I will be watching the organisation's

next stage with great interest. I would like to thank the 3,400 passionate people, our Board and our union partners who make up the KiwiRail team for their contribution and wish them continued success. They have, I believe, comprehensively demonstrated the value of KiwiRail to New Zealand in the work they do every day and that the case for growth is now indisputable.

Ngā mihi
Peter Reidy
Chief Executive
KiwiRail

Our progress 2014-2018

| | | |
|---|--|--|
| <p>Safety</p> <p>LTIs have reduced by 55% since 2014</p> <p>WINNER of Safeguard New Zealand Workplace Safety Awards 2017 'Engagement' category</p> | <p>People</p> <p>Employee NPS Engagement score up from -21 (2016) to +1</p> <p>Employee NPS Participation up from 47% (2016) to 81%</p> | <p>Customer</p> <p>Interislander Passenger NPS Increase by 20% since 2016</p> <p>Interislander Customer Satisfaction up 8% since 2015</p> |
| <p>Operational</p> <p>All Freight trains OTP up from 83% (2014) to 91%</p> | <p>Relationships</p> <p>Collective agreement negotiations 4 HOURS (2018) down from 6 months (2016)</p> | <p>Commercial</p> <p>Operating margin up from +10% (2014) to +14% (excluding earthquake impacts)</p> |

The launch of the Toi Toi Maori Leaders Programme in 2017



Northern Explorer crew, Fiona Stevenson, Justin Gallagher and Lea Chinnery.

The Value of Rail in New Zealand

For more than a century rail has connected New Zealand's communities, taken our goods around the country and to the world and showcased our landscapes to locals and visitors. But the total value that rail delivers to New Zealand can sometimes be overlooked while the costs are much debated.

Last year KiwiRail released a groundbreaking report by EY which, for the first time, quantified the unseen benefits of rail and what the costs of rail not existing would be to New Zealand if it was stopped tomorrow.

The results, though admittedly conservative, were remarkable. EY identified and quantified the economic, social and environmental contributions rail makes to the economy each year through the 34 million commuter journeys on our network; the tourist journeys; and the 18 million tonnes of freight moved by rail. EY calculated the benefits of the reduced congestion in our cities, the carbon emission savings made, the road maintenance costs avoided and – most importantly – the injuries and fatalities prevented on our roads through the use of rail

totalled \$1.5 billion each year, far exceeding the investment made by Government.

The EY Report, which was commissioned by NZTA in conjunction with KiwiRail and other agencies, followed similar work completed in Scotland, Australia and the wider United Kingdom. There are additional benefits also not yet quantified, including resilience for New Zealand's transport network, connectivity and the uplift in land values.

The total economic value of rail is:

**\$1.47B-
\$1.54B**
EVERY YEAR



Total value is derived from:

\$1.3B
reduced congestion

\$8.5M
reduced emissions

\$60M
improved safety outcomes

\$63M
reduced road maintenance

This value far exceeds the Government's annual investment in rail

RAIL REDUCES ROAD CONGESTION BY

76M

LIGHT VEHICLE HOURS PER ANNUM (SAVING \$1.1B) 75% IN AUCKLAND

THAT'S THE EQUIVALENT OF 100,000 DAILY CAR TRIPS OR REMOVING ALL THE CAR JOURNEYS IN PALMERSTON NORTH, EVERY DAY (SAVING \$1.1B)

RAIL REMOVES

11M

HEAVY VEHICLE HOURS PER YEAR (SAVING \$200M)

THE EQUIVALENT OF TAKING 30,000 TRUCKS OFF THE ROAD FOR AN HOUR, EVERY DAY (SAVING \$200M).

HELPING THE ENVIRONMENT BY **REDUCING**



EMISSIONS BY **488,000** TONNES PER YEAR (SAVING \$8.5M)

THAT'S THE EQUIVALENT EMISSIONS OF 87,000 CARS EVERY YEAR, OR A 747 FLYING NON-STOP ALL YEAR, EVERY DAY!

RAIL ELIMINATES

AT LEAST 271

SAFETY INCIDENTS A YEAR COMPARED WITH ROADS

THAT'S THE EQUIVALENT OF, ACTUALLY, WHO NEEDS AN EQUIVALENT? THAT'S 271 PEOPLE WHO WON'T DIE OR BE INJURED.

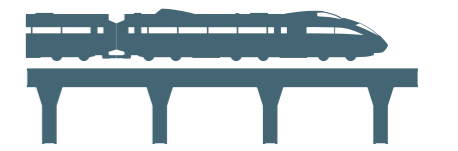
SAVING TAXPAYERS

\$63M

IN ANNUAL ROAD MAINTENANCE COSTS

THE AVERAGE COST TO OPERATE, MAINTAIN AND RENEW AN URBAN ROAD IS \$60,000 /KM /YR. THAT'S A ROAD NEARLY THE LENGTH OF THE SOUTH ISLAND.

RAIL PROVIDES A RANGE OF BENEFITS

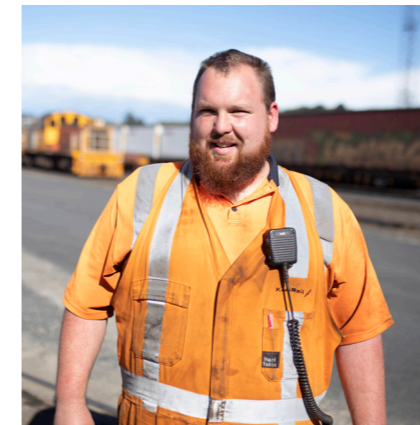


- THESE BENEFITS:
- HELP PEOPLE IN OUR COMMUNITIES TO CONNECT
 - RESULT IN MORE PRODUCTIVE USE OF LAND
 - KEEP US MOVING IN TIMES OF TROUBLE

Performance of our business units



Siobhan Russel, part of the KiwiRail Graduate programme.



Freight

Freight remains the biggest revenue earner for KiwiRail and contributes 57% of total operating revenue.

In FY18, the impacts of the 2016 Kaikoura earthquake continued to be felt, but KiwiRail has been pleased with the support received from customers since the Main North Line reopened to restricted freight services in September 2017.

Rebuilding domestic volumes remains a focus as further repairs are completed on the line, allowing additional services to be added as we return to unrestricted operations.

The earthquake's impact has been offset by strong performances in our forestry and bulk freight volumes, with increases in sales of 12% and 6% respectively. In response to the increased demand in these areas we have added coal trains and converted additional wagons to carry logs.

This year KiwiRail has worked with regional leaders, forestry owners and ports to explore options so the high volumes of logs now coming on stream can be moved by rail rather than road.

We have also continued to work with our port partners and other stakeholders at a strategic level to progress initiatives which will see more customers using rail as an integral part of their supply chains, benefitting not only our key import and export sector partners, but New Zealand as a whole.

Delivering a reliable service remains a core strategic focus for our business.

Our on-going work to improve network reliability and invest in new rolling stock over the past year has seen KiwiRail services maintain an On-Time Performance average for all freight trains at 91%.



Interislander

Interislander is an extension of State Highway 1, linking road and rail networks between Auckland and Christchurch. In 2017/18 the ferries carried nearly 800,000 passengers, 250,000 cars, 1.2 million lane metres of trucks and 500,000 lane metres of rail freight. This was reflected in a 5% growth in Interislander sales.

This year more than 99% of scheduled services operated as planned and 93% of these sailings were on or ahead of their scheduled arrival times. This has resulted in continued improvement of Interislander's customer satisfaction ratings, which were at a remarkable 90% as at June 2018.

The Kaikoura earthquake continued to have a significant effect on rail freight volumes on our ferries, as customers

shifted from rail to trucks or coastal shipping services. During this period, Interislander saw an increase of 11% in commercial vehicle activity and an increase in passengers travelling with cars of 8%. Conversely foot passenger numbers reduced by 2% as the Coastal Pacific train service from Picton to Christchurch remained unavailable for use.

KiwiRail continues to plan for the future of its ferry fleet through Project iRex. The Inter-Island Resilient Connection project is looking at future market demands, trends and customer requirements for replacing at least two of its ferries, which are reaching the end of their useful lives. That includes assessing how many ships should be in the fleet, how big they should be and whether they should be rail-enabled.



Tourism

KiwiRail's tourism services, collectively branded the Great Journeys of New Zealand, set new records this year as visitor numbers to New Zealand continue to grow.

February and March were the biggest months ever on the South Island's TranzAlpine and the North Island's Northern Explorer, with business up more than 10% on any previous year. Overall, TranzAlpine passenger business has grown by 90% over the past five years, while the Northern Explorer is up 71%.

Interislander had one of its busiest summers, with record vehicle numbers crossing the Cook Strait. At the same time, on-time performance and customer satisfaction scores reached new heights, and all services moved from Qualmark Silver to Gold status.

The New Zealand public welcomed the news that we are planning for the return of our much-loved Coastal Pacific service at the end of this year, following two years out of service as a result of the Kaikoura earthquake.

KiwiRail's tourism services are well-placed to help drive New Zealand's regional growth aspirations. Our scenic train services bring thousands of tourists each year to regions including Waikato, Ruapehu, Manawatu, Marlborough, Kaikoura and the West Coast, and there are plans to double that number in the years to come.

Rail also decreases the impact of visitors on the environment. This year has seen KiwiRail boost its focus on sustainability and waste management, including Great Journeys signing up to the New Zealand Tourism Sustainability Commitment.



Infrastructure

KiwiRail works hard to align its infrastructure investment priorities with customer needs and freight demand. However the underinvestment of past decades continues to have an impact on our business and that of our customers. We are working closely with Government to address this issue and identify appropriate long-term funding mechanisms to ensure KiwiRail can continue its vital role in growing New Zealand.

Over the past 12 months more than \$171 million was invested in the renewal and upgrade of the network (including contributions from other parties). Work continues on restoring and upgrading key infrastructure, including track, structures and container terminals.

Major projects include upgrading fibre communications alongside the North Island Main Trunk line, on-going improvements to the Kaimai and Otira tunnels, and improved access to the Southdown container terminal.

KiwiRail continues to focus its investment on growth corridors including the freight critical Auckland-Hamilton-Tauranga route with targeted

infrastructure investments that will support growing volumes at New Zealand ports. Substantial resources are being directed to reinstating the Main North Line between Picton and Christchurch.

Burgeoning commuter populations in Auckland and Wellington mean maintaining and upgrading urban metro rail networks remains a key area of focus for KiwiRail.

In 2018 work will continue upgrading the Wellington Metro network, with particular emphasis on renewals on the Hutt Valley line. This will deliver increasing network resilience and reliability for passenger and freight customers.

In Auckland, the key focus will be on delivering capacity improvements for freight and passenger, and preparing the network for the opening of the City Rail Link, which is expected to lead to substantial patronage growth. Key projects include extending electrification to Pukekohe, and a Third Main line between Westfield and Wiri, which has the key aims of segregating freight from the busiest part of the network and delivering improved network resilience.



Property

As one of New Zealand's largest landowners, KiwiRail's property focus in recent years has been on commercialising its holdings and the property portfolio it manages which includes more than 1,400 buildings and 8,000 third party interests spread over more than 17,800 hectares of land.

We have partnered with a number of key freight customers who lease land next to rail yards for rail-served operations. These initiatives enable KiwiRail to improve the efficiency of customers' supply chains and to generate income growth through long-term, sustainable, leasing arrangements.

KiwiRail continues to review its property portfolio to ensure its lease and licence arrangements are managed in a fair and commercial manner.

Protecting the active rail portfolio is key to KiwiRail safeguarding the corridor for future generations. In FY18 this strategy was broadened to include securing land for future use while disposing of land to improve the network. The strategy also increases revenue from KiwiRail's land by streamlining processes, optimising yard and terminal assets and releasing the maximum capital from non-active rail land. Surplus cash is used to invest in the network.



Rolling stock

KiwiRail is investing in new rolling stock as we renew our asset base and transition our fleet in line with our rolling 10-year plan.

The plan addresses decades of underinvestment which have left us with a locomotive and wagon fleet that is increasingly showing the signs of ageing.

We have critical rolling stock capital requirements which cannot be further deferred as the assets are at their end of life.

Legacy issues relating to our ageing rolling stock in the South Island last year caused an unexpected and costly locomotive refurbishment programme which affected reliability for our customers.

The average age of a locomotive in the South Island is 42 years, while the useful life of a locomotive is typically 30 years.

Production of 235 new wagons has been completed in Dalian, China, and they arrived in New Zealand for commissioning in July 2018. In addition, 15 new DL Locomotives (Generation 2.3) purchased in 2016

are nearing completion, and will enter a staged commissioning programme from October 2018.

Investment in our facilities to support the 10-year fleet plan continued through FY18, with a major programme of works at the Hutt Workshops traction motor maintenance facility. This High Performance High Engagement (HPHE) project also resulted in a large jump in employee engagement, improved workplace safety through a reduction in crane movements, and a 40% reduction in the average number of labour hours per traction motor overhaul.

Our organisational capability continues to grow, with new members joining the team in asset management and asset-performance focused roles. In Palmerston North we also saw improvements in our wagon servicing through an HPHE project.

In FY18 our diesel locomotive reliability programme made progress. There was also a focus on wagon availability and reducing the number of wagons out of service for long-term repairs or maintenance.

Our integrated business



Adam Matete, Terminal Manager Night Operations, KiwiRail and Alan Jefferson, Operations Manager Coda at the Coda Depot, Saville Road.



Coda brings together import, export and domestic freight, to increase the total volume on rail and balance rail flows around the country.

KiwiRail's customer-led strategy to shape the organisation's future has well-founded roots, as shown by the on-going collaboration with logistics company Coda.

At the heart of the strategy is engagement with existing and potential customers across the country, in order to understand what they need from us – both now and in the future.

A recent outcome has been the shift to a vertically integrated operating model that will be customer-centric, service-led and primed for growth.

Led by the new role of Chief Operations Officer, the new structure brings together into one team, our rail network, operations, rolling stock and container transfer sites.

"We've changed so everyone's role in KiwiRail has a customer outcome," says Chief Executive Peter Reidy.

"This enables a customer-centric approach to both day-to-day

operations and longer term thinking and planning."

“KiwiRail is firmly committed to putting customers at the centre of all we do, to build Stronger Connections and a Better New Zealand. And it is our people who will make this happen.”

Chief Operations Officer, Todd Moyle

For Coda, this means closer collaboration to develop even more efficient intermodal supply chain solutions that benefit their customers

and more widely New Zealand, says KiwiRail Chief Operations Officer Todd Moyle.

"Our new structure enables us to work more effectively with Coda, particularly around demand planning to meet seasonal peaks and to help remove the empty return journeys in the country's supply chains."

The empty return trip is an issue faced by all long-haul freight transport operators and one that has been addressed by Coda with real success.

Coda, a joint venture between Kotahi and Port of Tauranga, moves almost 30% of containerised export cargo to ports around New Zealand and is one of the largest movers of imported goods in the North Island. Coda has been working closely with KiwiRail on an intermodal strategy since 2015 and now Coda is also one of the largest movers of domestic freight on rail.

By partnering with KiwiRail and developing strategically located intermodal freight hubs, Coda is

successfully bringing together the import, export and domestic freight flows into a single supply chain, to increase the total volume on rail and balance rail flows around the country.

As an example, Coda rails export-bound product from the lower North Island to its intermodal freight hub in Auckland and from there it is delivered to port via rail. Then, given most of New Zealand's imported goods arrive into ports in the upper North Island, Coda is able to backload the intermodal units with imports and other domestic cargo. The full intermodal units are then railed back down to a lower North Island hub, from where the freight is further distributed.

This strategy has achieved close to 100% utilisation of the round-trip rail leg between Auckland and Palmerston North and has eliminated the need to move empty shipping containers around the North Island.

A similar intermodal operation will shortly open at Rolleston near

Christchurch, to allow the more efficient movement of goods around the South Island.

“We recognise that in order to create new and innovative solutions more easily and quickly we must work collaboratively with our logistics partners.”

Coda Chief Executive Scott Brownlee

"Our collaborative approach with Coda delivers cohesive asset planning, demand management, reliability and operational safety, which means we can more effectively develop the right equipment and services and deliver better demand planning," says Todd Moyle.

The two companies are also exploring joint digital solutions to develop more seamless freight booking channels, which will enable both organisations to further improve two-way loading for all journeys.

Coda Chief Executive Scott Brownlee says working closely with KiwiRail can deliver real value for its customers and for New Zealand.

"New Zealand exporters need to maintain effective connections to global markets, but to support this we need to ensure our domestic transport networks are cost effective and sustainable.

"We recognise that in order to create new and innovative solutions more easily and quickly we must work collaboratively with our logistics partners.

"Working more closely with KiwiRail has allowed us to open up very reliable and cost effective intermodal solutions and provides the opportunity for more customers to share in the value that rail can offer," says Mr Brownlee.

Financial

KiwiRail met the full year operating surplus commitment of \$30-50 million by delivering a strong operating surplus of \$49 million despite the many challenges FY18 brought. Revenue was impacted as work on rebuilding the Main North Line continued.

Our Financial Capital

Operational Revenue

Government Investment

Grant Funding

Asset Sale Proceeds

Debt Funding

The underlying operating surplus was \$94 million, excluding Kaikoura earthquake impacts of \$45 million, \$38 million of which was attributable to domestic freight revenue loss.

Despite the challenges, there were areas of growth, bulk freight revenue up 6% through strong milk and coal volumes, and forestry revenue up 12% with strong export demand. Tourism revenue was strong, up 10% with a record summer season, high customer satisfaction and consistently high operational performance. Property revenue was also up 5%, a rise attributable to commercial leases.

KiwiRail has continued to focus on achieving underlying targets and managing costs with reduced available cash flow. In FY18 \$7 million of efficiency and waste savings were delivered, building on the \$45 million achieved in previous years.

Future of Rail

Future of Rail is a Government initiative led by the Ministry of Transport. It will formally set out the purpose of rail within New Zealand's wider transport system, the benefits that rail provides, and the optimal structure and funding for rail. The initiative will put rail on a longer-term sustainable footing.

In Budget 2018 KiwiRail was allocated \$230 million for FY19 to finance capital expenditure on the national freight network, \$164 million to roll over an existing loan from the Crown, and \$145 million to fund reinstatement of the Main North Line while KiwiRail awaits the outcome of its insurance claim. Given the transition under Future of Rail, and the continuing revenue impacts arising from the Kaikoura earthquake, KiwiRail has taken a conservative approach to spending for the coming year and will invest in core business improvement areas.

Provincial Growth Fund

The Provincial Growth Fund (PGF) has been established by the Government to support regional economic development and lift productivity potential in the regions.

On 23 February the Government announced the first five KiwiRail projects to be funded from the PGF, including the reinstatement of the Napier to Wairoa line, upgrade of Whanganui line and three feasibility studies looking at areas of future investment. These announcements are a strong signal of the Government's confidence in rail's ability to drive regional economic growth for New Zealand. A case study on the Napier to Wairoa initiative is included on page 37.



Highlights

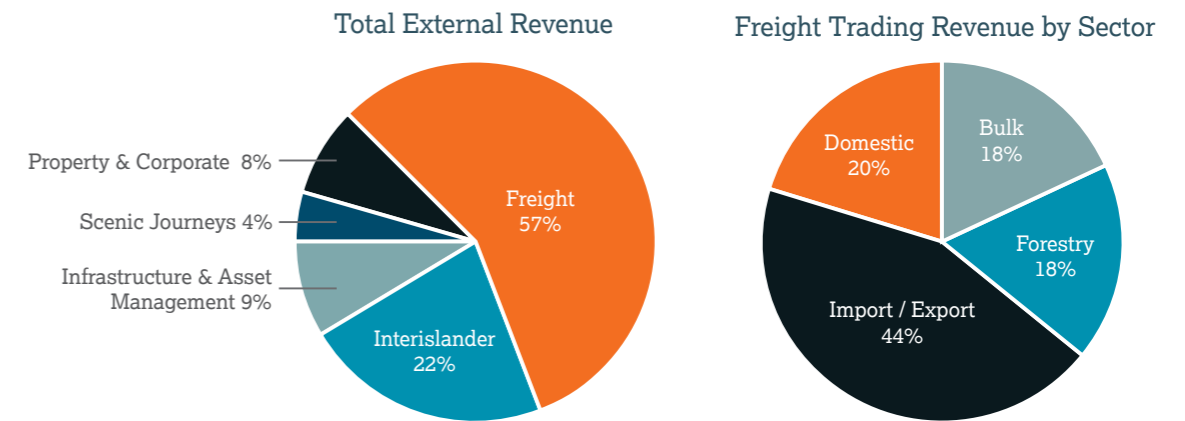
\$49m
Operating surplus

\$94m
Underlying operating surplus excluding \$45 million impact from Kaikoura, exceeding FY17 underlying result

\$7m
of efficiency and waste savings were delivered, building on the \$45m achieved in previous years

12%
Forestry revenue up 12% with strong export demand

6%
Bulk freight revenue up 6% with strong milk and coal volumes



The charts above show the source of KiwiRail's revenue, and a breakdown of KiwiRail's freight revenue by sector. In terms of freight revenue, it is worth noting that the non-commodity driven activities are where we can have the greatest degree of influence on our market share as these activities are less susceptible to price movements caused by external factors.

KiwiRail has identified a number of further initiatives that will help to enable regional growth and also have flow-on benefits for core passenger and freight transport networks and services. We will be working with the Provincial Development Unit to progress these opportunities over coming months.

Government Policy Statement on land transport

In June 2018 the Minister of Transport Phil Twyford, Associate Minister of Transport Julie Anne Genter and Minister of Finance Grant Robertson visited KiwiRail's Southdown container hub terminal in Auckland to launch the Government Policy Statement (GPS) on land transport 2018. The GPS outlines the Government's strategic priorities and provides guidance on how the National Land Transport Fund (NLTF) will be spent. The four strategic

Financial statements

The financial statements are included from pages 66 onwards and detail the financial performance for the year and the financial position at 30 June 2018.

Notes which may be of particular interest to our readers are:

Note 2 – Operating Revenues – provides the split of revenue between business units

Note 3 – Operating Expenses – shows KiwiRail's key operating costs

Note 8 (c) – Impairment of Non-Financial Assets – explains why KiwiRail impairs \$249 million of railway infrastructure assets

Note 25 – Financial Risk Management Policies and Objectives – explains the financial risks KiwiRail faces, how these risks impact the financial statements and how KiwiRail manages these risks

Note 26 – Impact of Kaikoura Earthquake – outlines the Kaikoura Earthquake impacts on the financial statements

priorities in GPS are safety, access, environment and value for money.

In addition, the GPS signals a shift to a mode neutral approach to ensure that all transport modes are considered when planning and funding land transport activity. A new transitional rail funding class has been created

to ensure that priority passenger rail projects can be advanced while the Future of Rail project is in progress. GPS notes that a second stage GPS will consider the role and funding of rail further and will be informed by the Future of Rail.

GPS took effect on 1 July 2018.



Tini Tilitua, Remote Control Operator.

Record season for Interislander tourism



“My wife and I have used ferries around the world (Andros, Gozo, Mekong and Ireland to name a few) and found the Interislander superior in all aspects. Congratulations and well done!”

Continuing growth in visitor numbers and the reopening of the road between Picton and Christchurch helped Interislander to one of its best tourism seasons over the 2017/18 summer.

The number of vehicles using the Interislander to cross Cook Strait was at an all-time high between December 2017 and February 2018. Passenger revenue for summer also reached a new record.

Importantly, as those numbers increased, Interislander’s on-time performance and customer satisfaction scores also continued to climb.

More than 99% of scheduled services operated as planned and 93% arrived on or ahead of schedule. Our customer satisfaction ratings are sitting at 90%, and we are ahead of target for our Net Promoter Score, which asks if customers would recommend our service to others.

These ratings are reflected in the feedback received from passengers.

A common thread is the extra mile staff go to keep customers comfortable and make their journeys memorable.

An example was when a passenger asked for help to make the trip special for his two grandsons, who have a condition that will cause blindness. The Interislander team responded with VIP treatment, tours, ice creams, and special signage to welcome them on-board.

Other passengers have written to thank staff for looking after them in rough seas, taking special care of pets, ensuring the safe delivery of a classic car, and even rustling up a bacon buttie with brown sauce for English passengers keen for a taste of home.

The re-opening of the highway between Picton and Christchurch, a key route for self-drive visitors to New Zealand, is believed to have contributed to the growth in vehicle traffic across the Strait.

Motorhome enthusiasts remain a key market for Interislander, and

KiwiRail’s long-running relationship with the New Zealand Motor Caravan Association (NZCMA) was further deepened in 2017 with the NZCMA making Interislander its preferred partner.

Sustainability is an increased focus for our tourism services, and this year Great Journeys of New Zealand (including Interislander) signed up to the New Zealand Tourism Sustainability Commitment.

Interislander has also improved from Qualmark Silver to Gold status.

Initiatives to manage and reduce waste are being introduced, including removing plastic straws from Interislander services.

Given Interislander’s close connection to the ocean, these moves have resonated well with its increasingly environmentally-aware customers.

As we plan for our future ferry fleet, we will continue to offer the great customer experiences that make Interislander a treasured part of New Zealand’s tourism history.

People

KiwiRail has transformed its people culture over the past three years, as our frontline-led High Performance, High Engagement programme and a focus on purpose beyond profit has engaged our 3,400 people.

We are one of New Zealand’s largest employers with proud KiwiRail staff operating in more than 50 towns and cities across the country. History means a lot to our people – many are the third or fourth generation in their family to work in rail – but it is the promise of rail’s future that is exciting our business.

KiwiRail teams have had to tackle significant hurdles recently – from rebuilding our network after the devastating Kaikoura earthquake, to bush fires, devastating weather events and working with ageing infrastructure and rolling stock. However, our people never give up on a problem and are united by challenge.

But over the past year we have focused our people strategy on a deeper purpose and will roll this out to our team towards the end of the year. “Stronger Connections. Better New

Zealand”, speaks to the role KiwiRail plays in growing communities and the economy through our passenger and freight services.

“For me the key change has been around communication, we now communicate better with each other, with teams from across the business, and with our customers.”

Logan Rusling, Rail Operator, Palmerston North



Highlights

+1

Staff engagement hits record high with Employee Net Promoter Score reaching +1 in 2018, from a low of -21 in 2016 and -7 in 2017

10%

Total Recordable Injury Frequency Rate decreases by 10% over previous year

6,700

Safe Work Conversations recorded over the year

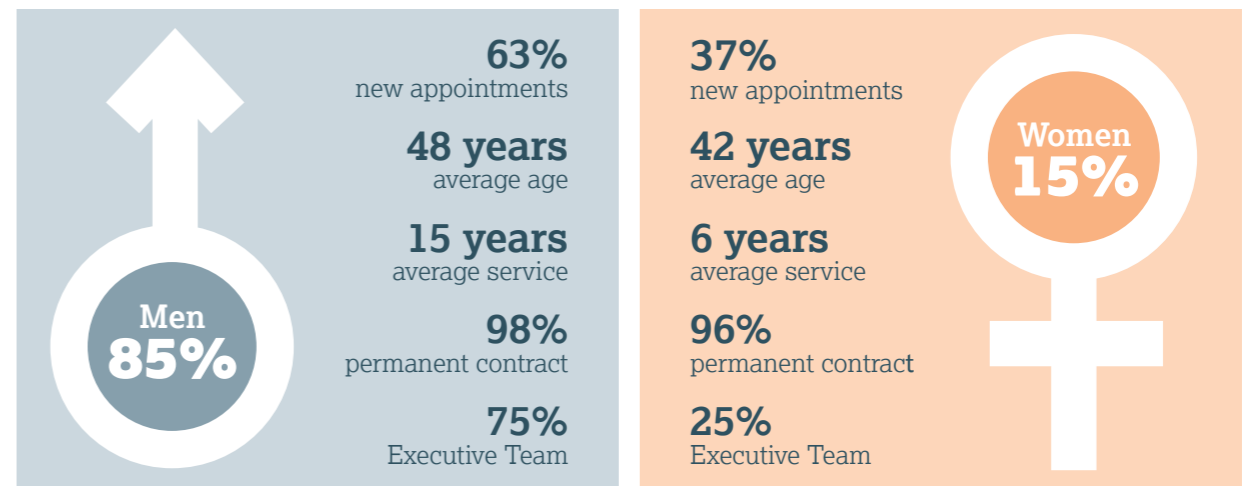
Toi Toi

Toi Toi Maori Leadership programme launched

HPHE

High Performance High Engagement (HPHE) project at Hutt Workshops traction motor maintenance facility leads to improved safety and efficiency

Our workforce statistics





Nick McCleery, Operations Manager Invercargill.

We have reorganised ourselves around our customers, uniting our operational teams of network, rolling stock and operations into a single unit focused on exceeding our promise.

At the heart of this work is the significant lift we have seen in employee engagement. Our Employee Net Promoter Score has lifted from -21 in 2016 and -7 in 2017 to +1 in April 2018. This means that more of our people would actively promote working at KiwiRail, and sits us well above industry benchmarks.

Zero Harm

Critical to our business is our core value of 'Care and Protect'. Our Zero Harm vision is to become the leading safety and health organisation in New Zealand. That means KiwiRail's employees and contractors need to believe that every accident is preventable. As part of achieving this, we have increased the focus on learning from critical risk incidents and near miss events - situations where outcomes could have resulted in serious harm or fatal injuries.

In April, we launched the first phase of our Safety, Health and Environment management system. This will consolidate safe working practices from all business units and provide a single, consistent framework for managing Zero Harm right across

“
Staff engagement is now an on-going process. At our sites at the morning Toolbox meetings we have conversations covering staff health and safety issues and the overall running of the yard.”

Ebin Schofield,
Christchurch CT Team Leader

the business. This will support our continuous improvement practices, particularly in relation to our risks.

KiwiRail is improving safety capabilities of its people through a deeper understanding of the safety skills training and non-technical skills each role requires. Programmes such as Just and Fair Culture, and our local Health and Safety Action Team, are supporting our cultural change and Zero Harm engagement by encouraging a proactive approach to personal safety and people understand how their choices impact on the safety of others.

Safe Work Conversations are a key activity in safety culture development, designed to create engagement opportunities between KiwiRail's frontline team members and leaders. In FY18, Safe Work Conversations with staff about mitigating risk and identifying areas for improvement have increased by more than 160% which is supporting improvements in our safety performance, with reduced injury rates and incident severity.

People Development

The High Performance High Engagement programme (HPHE),

is a joint project with KiwiRail's union partners, which empowers frontline staff to find solutions to the challenges facing the business while raising productivity, improving safety and enhancing performance. The programme continued to deliver excellent results during FY18, with Workplace Safety Minister Iain Lees-Galloway describing it as “the future of industrial relations”, and praising KiwiRail for working towards ‘enduring results that make lasting change in the workplace’, after a site visit to our Palmerston North Depot.

KiwiRail also explored new learning and development opportunities for its people in FY18. We gave KiwiRail's digital Learning Management System a makeover to make it more user-friendly and responsive to all devices. Our people can now see their competencies, which allow them to carry out certain tasks, complete eLearning, view information about our courses and request access to attend training, even when working off-site.

Ahurea (Culture)

KiwiRail has embarked on a significant programme of cultural change in recent years, driving bottom-up leadership in our frontline teams, developing diversity and inclusiveness programmes and investing in a unique Te Ao Māori environment to grow inspiring Māori leaders.

Our Māori network, Te Kupenga Mahi (TKM), helps our people to connect with their whakapapa and advises the business of appropriate ways to incorporate Māori culture into our day-to-day activities. TKM regularly performs karakia (blessings), pōwhiri (welcoming ceremonies) and te pure (ritual cleansings of sites and machinery) at our events.

KiwiRail's Toi Toi Māori Leadership Programme gives young Māori exposure to a Te Ao Māori learning environment using Kaitohutohu (mentors) to aid the personal and professional development of the

programme's Taura (cadets). The programme inspires our people to become influential and successful across business, community and family contexts. Its vision is to 'create inspirational Māori leaders who grow other leaders'.

KiwiRail Values Awards

A strong culture will help KiwiRail grow, and in October we celebrated the winners of our inaugural KiwiRail Values Awards. Nineteen staff from across the business were recognised for their commitment to living our core values.

Diversity

Only 15% of KiwiRail's workforce are women, and the average age of our workforce is 46. KiwiRail remains committed to being inclusive and diverse, and a number of initiatives are underway to achieve that.

The Diversity and Workforce Planning Committee continues to work on lifting the profile and number of women in the workplace. There was a strong turnout on International Women's Day for a company-wide panel discussion on opportunities and challenges for women in the business. In May, Pink Shirt Day was embraced throughout the company as KiwiRail made a strong statement that bullying and harassment are not part of our culture.

In FY18 KiwiRail established a mentoring programme for younger members of its workforce and also commenced a Graduate Programme aimed at attracting and retaining a diverse group of young talent for future operational, technical and leadership roles. Graduates are provided with a supportive environment, formal rotations through a number of different business areas, on-the-job training and mentoring. The Programme will continue into FY19, with a second intake scheduled for July 2018.

“
Getting a programme like this underway requires real leadership, commitment and patience and this has been demonstrated at all levels of both KiwiRail and the RMTU...”

Ross Wilson,
WorkSafe Deputy Chair

Case study

Revitalising health and safety action teams



Kasia Kurene, Locomotive Maintainer.

KiwiRail has strengthened its commitment to Zero Harm during the year by reinvigorating our Health and Safety Action Teams (HSATs).

Our 350 HSAT members are our people on the ground when it comes to safety. They connect our managers and Zero Harm team with frontline staff, and help to raise awareness of the people who see potential safety issues first hand.

KiwiRail has 39 HSAT teams across the business.

National Zero Harm Manager Sacha Montgomery says while HSATs have been in place for a number of years, they have been revitalised over the past six months. This refocus is designed to support their activities, provide additional education on hazard and risk identification and create opportunities for raising their profile within the business.

"HSATs are the voice of our people and we want them to be proactive, identifying potential issues and driving solutions. It's about building the skills and culture to get ahead of potential problems - and the approach is paying real dividends."

The improved focus has seen an increase of more than 150% in hazard and near miss reporting,

which strengthens our ability to identify and address issues and risks before incidents can occur. This reduces the severity of health and safety incidents and injuries over time.

Dunedin HSAT Chair, mechanical engineer Mike Beaufort, says it's crucial to have safety people on the ground.

"HSAT reps are available and approachable all the time. We're right there and staff know who to go to.

"I'm known as the local HSAT guy and staff come straight to me with any health and safety concerns. Working together, and with the team leader, we get it sorted quickly, and it makes it easy for our staff to take action, which empowers them."

Local HSAT teams now have stronger connections with other HSATs around the country as well as with senior management.

One of KiwiRail's core values, and the one most often repeated by staff, is 'Care and Protect'. By fostering a thriving HSAT community, we ensure that all parts of our business are contributing to a safer work environment for all of our people and our customers.

Assets

KiwiRail moves around 25% of New Zealand's exports, transports more than one million tourists on its Great Journeys passenger services and helps enable 34 million commuter journeys a year in Auckland and Wellington.

To do that, we work our assets hard.

We keep our customers satisfied by ensuring our services are reliable and that they can be trusted to deliver on time.

That means making sure our assets are up to standard, and to achieve that KiwiRail regularly inspects its track, upgrades its assets and carries out preventative maintenance and repairs over the rail network. In FY18 we spent \$171 million on network capital expenditure (including contributions from other parties), targeted on key freight lines and improving line, resilience and operational capacity to meet increasing freight volumes.

This includes two projects funded through the Government's Provincial

Growth Fund - the re-opening of the Napier-Wairoa line for forestry trains, and an upgrade of the Whanganui line.

It also includes continued work on the Main North Line to improve its resilience and reliability after the Kaikoura earthquake, work on the Kaimai Tunnel and an upgrade to the CT site at Southdown, both key assets supporting our Golden Triangle freight business.

Ferry replacement

Interislander serves three main customer segments: freight by rail, freight by commercial vehicles and passengers/tourists. To remain viable, relevant and competitive, KiwiRail offers reliable, efficient and



Highlights

Two

Two major projects underway to consider long term strategy for Interislander ferries and future rolling stock fleet

\$171m

(including contributions from other parties) capital expenditure targeted on key freight lines and improving resilience and operational capacity to meet increasing freight volumes

91%

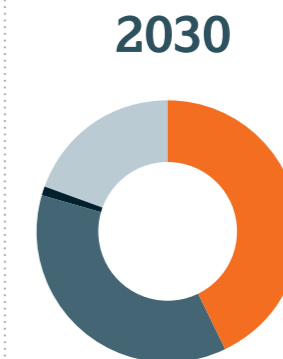
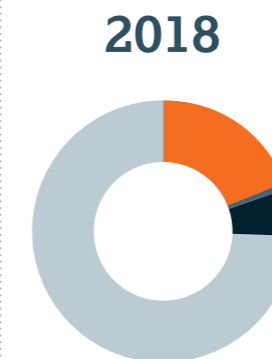
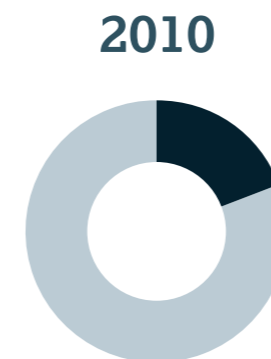
On Time Performance (OTP) of 91% for all freight trains

Napier to Wairoa line sees first work train in six years preparing the line for resuming log trains

15

Final testing of 15 new locomotives underway

Age profile of the locomotive fleet



By 2030 the majority of the fleet will be under 30 years of age. A significant change from 2010 when 80% were over 30 years old.

- 1-10 yrs old
- 11-20 yrs old
- 21-30 yrs old
- +31 yrs old

resilient services to ensure we meet customers' needs now and in the future.

KiwiRail's Cook Strait business will soon face challenges related to the capacity and age of the existing fleet, and the age and resilience of the terminals in Picton and Wellington.

Within the next five years, Interislander will be expected to replace at least two of its three ferries, Aratere and Kaitaki, before they become uneconomic to operate and maintain.

Project iReX has been assessing future market demands, trends and customer requirements. The current phase of the project is looking at the number of ships KiwiRail should operate, the size of those ships and what sort of ships they should be – rail-enabled or road vehicle only, with rail containers transhipped by truck.

At the same time, the project is also considering terminal options, including whether KiwiRail could share facilities with other operators.

Project iReX will deliver the best solution for KiwiRail to provide improved services for customers and grow its business. Another major aim of the project is to build resilience into the operation to ensure services can continue to operate in the event of disaster such as earthquake.

Rolling stock upgrade

This year saw the launch of Project Nexus, a strategy to deliver future rolling stock, facilities and asset management practices ensuring reliability as we grow our customer base.

KiwiRail has had decades of underinvestment in its assets, and many of its trains and wagons are at the end of their useful lives. The average age of a locomotive in the South Island fleet is 42 years, against a typical useful life of 30 years.

The initial focus of Nexus is specification and procurement of the next generation of super shunt locomotives (large shunting locomotives capable of mainline running) and mainline locomotives for the South Island.

The first phase of the process - preliminary market research - was completed in FY18 and it is expected that tendering will begin in FY19, to be followed by contract development.

Nexus also includes redevelopment of our maintenance facilities and provision of next-generation technology on our rolling stock fleets to enable preventive and predictive maintenance.

Manufacture of 15 new DL Class locomotives was largely completed during FY18. The locomotives are

currently being tested, before being shipped to New Zealand to arrive in late 2018. They will undergo commissioning at the Te Rapa maintenance depot before being introduced to service during FY19.

KiwiRail has continued to implement a strategy of standardising its wagon fleet by reducing wagon types. This strategy either retires obsolete fleet classes and wagons which are uneconomic to repair, or upgrades existing models into wagons that are able to support increased sector demand. An example of that is converting 236 ageing container wagons to be capable of carrying logs to meet demand for New Zealand's 'wall of wood' coming on stream. Investments were also made in multi-use wagons, to ensure operational flexibility across the bulk freight sector.

In FY18 KiwiRail acquired 150 new wagons, made up of what is now our standard heavy wagon, the IH 50 foot wagon. Progress was also made on 235 heavy wagons to be delivered in FY19, 135 of which will be 50 foot while the other 100 will be 60 foot wagons, IBB class.

We have continued our transition to an intermodal asset base which enables freight to move easily between ships, trains and trucks. With 59% of our wagon fleet now intermodal, it is easier for customers to carry freight on our rail and ferry services and transition between networks.



Gavin Baillie, Third Officer Engineer.

Supporting regional development



Regional Economic Minister Shane Jones in the cab of the first work train to run on the Napier-Wairoa line.

When the coalition Government took office in October 2017, it signalled its recognition of KiwiRail's contribution to New Zealand and its commitment to using rail to drive regional economic growth.

As part of that, the Government announced in February it was allocating \$8 million towards 'rebooting regional rail' through a number of projects funded by the Provincial Growth Fund.

Reopening the Napier to Wairoa line for log trains topped that list and just three days later KiwiRail began work on the task of reinstating the line.

The road between Napier and Wairoa was not designed to cope with the rising number of trucks needed to transport the wall of wood expected to be harvested over coming years. Reopening this line could take more than 5,500 trucks off the road between Napier and Wairoa, reducing carbon emissions, improving safety for motorists, avoiding road maintenance costs and providing an efficient supply chain to port for forestry owners.

Despite an early setback - intense rain in the region caused a large amount of damage - our teams have made good progress and in June a work train made the journey from Napier

to Eskdale delivering ballast. It was the first train on the line for six years and many locals turned out to watch its progress.

KiwiRail marked the occasion with a special event at Ahuriri, with local iwi in attendance to bless the line, the work train and our people working on it. Later in the month work trains began travelling between Napier and Wairoa.

The line is expected to be ready for logging trains by early next year.

Other projects already funded by the Provincial Growth Fund include upgrading the Whanganui line, and feasibility studies for regional rail projects in Kawerau, Southland and New Plymouth. KiwiRail is working on a number of other proposals for the fund, aimed at bringing tourists to the regions, exports to port and connecting communities through a revival of rail.

Our growth strategy recognises KiwiRail's critical role as an enabler of sustainable economic development in regional New Zealand. We are working with key stakeholders, including existing customers, local councils, tourism operators, forestry interests and other businesses, to explore the myriad of opportunities for rail.

Skills and know-how

KiwiRail's people draw on their deep rail and ferry knowledge to develop solutions that perform in New Zealand's unique and challenging rail environment.

Their world-class engineering skills and innovative approach to meeting challenges are applied across the business, but over the past year have been most apparent in the continuing response to the November 2016 Kaikoura earthquake and the damage it did to the Main North Line (MNL) connecting Christchurch to Picton.

KiwiRail had challenged itself from the outset to restore the line and resume restricted rail services as quickly as possible, to provide critical freight transport services for customers and take pressure off the vulnerable road network.

Moving mountains to reconnect communities

The scale of the recovery work required was unprecedented but despite the overwhelming task, KiwiRail reopened the line to night freight services within 10 months of the earthquake.

KiwiRail developed a suite of safety measures to enable this to happen while repairs continued.

The measures included the installation of remote monitoring technology along areas of potential further instability designed to alert KiwiRail's National Train Control Centre to potential events before trains passed through.

Technology was also put in place on damaged bridges and tunnels to monitor their performance under load and ensure safe operations.

Initial safety thresholds were conservative, which meant trains did not operate during wet weather as a precaution. Close analysis of incidences of instability during and after wet weather, and the completion

of further works, has seen these thresholds revised, allowing a more reliable service for customers.

This impressive feat on the MNL saw KiwiRail and its project partners awarded the Rail Technical Society of Australasia's Biennial Project Award.

Their work was described as an "inspiring example of how railway people respond energetically and successfully to the most severe of challenges".

Managing the infrastructure

Ensuring network infrastructure, rolling stock and other assets are maintained or upgraded appropriately and in a cost-effective way while keeping the impact on our operations to a minimum is a key focus of our asset management programme.

KiwiRail uses Structural Health Monitoring (SHM) to ensure the right level of repair at the right time for its many bridges and viaducts. This approach uses modern technology to better understand how a bridge or viaduct behaves under load and builds an accurate picture of which parts of the structure need strengthening and which parts do not.

During testing, engineers calculate the weight of a work train, and then move it across the bridge at various speeds, stopping at different locations. Sensors mounted to the bridge measure how the spans and towers react to the train's movement and position.

Digital

With KiwiRail people spread across the country and a 24/7 operation, considerable planning is needed for staff rostering.



Highlights

10 months

Main North Line reopened to restricted freight services just 10 months after the Kaikoura earthquake, and work continues to enable daytime running of trains

Nine weeks

Workforce management system introduced in nine weeks using agile principles



KiwiRail has leveraged technology to develop automated integrated financial and Zero Harm reporting, simplifying and standardising the reporting framework, and allowing management to access key KPIs remotely using the reporting app.

In 2017 KiwiRail implemented the Quintiq workforce management system, which optimises staff rosters to not only provide cost-effective operational outcomes, but also consider non-financial metrics such as sociability for the staff involved.

Using the agile implementation framework, KiwiRail introduced Quintiq to a pilot group in just nine weeks. That project is being used as a global case study in rapid digital implementation.

KiwiRail has also leveraged technology to develop automated integrated financial and Zero Harm reporting, simplifying and standardising the reporting framework, and allowing management to access key KPIs remotely using the reporting app.

We have also developed a new 'system to system' service that automates the booking process and allows our customers to have seamless interactions with us. Deep customer engagement over the last 12 months

has also revealed opportunities for new digital services for specific customer segments, which will be further explored over the coming year.

Safety initiatives

KiwiRail closely monitors rail and ferry trends to find solutions to operational challenges and to improve safety systems' performance. In one innovation, KiwiRail has adopted a system overlay approach to technology intended to ensure the safety of operations at worksites and in non-signalled 'dark territory'.

Project Interceptor employs GPS data from the locomotive to monitor the approach of a train to the limit of where it has authority to run, and applies the brakes if the train does not slow sufficiently, then stop as required.

A series of final trials of the system were carried out over the past year and the technology is to be rolled out across KiwiRail from later this year.

KiwiRail has also begun a 12-month trial at Paraparaumu, in conjunction with Victoria University and engineering consultancy WPS Opus, to use a new GPS monitoring system giving advanced warning of land instability along the rail network. Monitors are arranged on a hillside and their status is tracked, with any movement signalling a potential landslide.



KiwiRail is looking to new technologies to help keep people safe.

KiwiRail is trialling new safety technology in New Plymouth as it responds to the growing number of pedestrian and cyclist fatalities at New Zealand level crossings.

Pedestrian and cyclist fatalities have been trending upwards since 2000. That year there was one fatality, four in 2004, and seven in 2016. Thirty-seven pedestrians and cyclists died at rail crossings around New Zealand between January 2000 and December 2017.

Crossing users often fail to check for approaching trains before stepping on to the tracks. Modern technology has been identified as a leading cause of distraction, particularly mobile devices and headphones.

KiwiRail is committed to turning these statistics around and making rail as safe as possible for everyone. Part of the solution may be technology, and New Plymouth - a district with a number of level crossings which require pedestrians to actively check before walking was the right environment for a trial of new safety technology.

The concept is simple: a voice messaging system is being installed to advise

approaching users that a level crossing is ahead and they should check for trains.

To reinforce that message, and for people with impaired hearing, LED tiles are installed on the crossing's footpath approach to visually alert users that they should look for trains in both directions before crossing.

KiwiRail Engineering Services Delivery Manager, Eddie Cook, has led the trial.

"We had used LED lights at level crossings in Tawa, Feilding and Napier to warn pedestrians trains were approaching," he says. "In New Plymouth, I took that technology and used the lights to warn people they were approaching a level crossing. The voice message was used for the first time and reinforces the need for care," he says.

Both the New Plymouth District Council and the Australasian Centre for Rail Innovation (ACRI) are evaluating the system. If using technology to improve level crossing safety is successful, it could be installed at other suitable locations throughout New Zealand.

Relationships

The strength of KiwiRail's relationships is central to our business and critical for our ability to create Stronger Connections for a Better New Zealand.

We engage with customers, the Government and its agencies and a diverse range of regional stakeholders to help drive development of our cities and regions through an integrated transport network, with a focus on economic, environmental and social sustainability outcomes for New Zealand.

As one of New Zealand's largest landowners, and with a rail network that extends the length and breadth of the country, KiwiRail is involved with communities across New Zealand every day.

We understand the importance of rail to these communities through our shared histories, the future economic potential we can help unlock, and our day to day interactions as part of a freight and passenger transport system.

Customer partnerships

In 2017 we embarked on a customer-led strategy to shape the organisation's future.

As its Māori name suggests, Project Wā heke looks into the future through the eyes of key players and influencers in the transport and tourism markets. At its heart has been deep engagement with existing and potential customers across New Zealand. The dominant themes emerging from this work were customer-centricity, collaboration, connection, communication and certainty.

From this we have gained insights into how disruption is affecting supply chains, how New Zealand industries are changing and what our customers need from us – both now and in the future. This will allow us to determine

the partnerships we can develop to deliver sustainable growth for both our customers and our business, and for New Zealand.

An early outcome of this work is a transition into a vertically integrated operating model that is truly customer-centric, service-led, and primed for growth.

A new role of Chief Operations Officer has been established to lead all teams working in network services, rolling stock, operations and container terminal businesses. This structure provides a single approach to our asset planning, availability, reliability, operational safety and people development across the organisation, all pointing towards the outcomes we want for customers.

This change to our organisational structure forms the cornerstone of a fundamental shift in our business which will enable us to better develop strategic partnerships with customers, and provide innovative logistics solutions and enhanced passenger travel experiences.

Since September, when the Main North Line reopened with a restricted level of night-time freight services, our teams have maintained close contact with customers moving goods between Auckland and Christchurch, providing on-going updates on the status of the line to support their logistics planning. Each week the resilience and reliability of the line improved as teams worked during the day to continue the rebuilding of road and rail. These improvements have seen significant increases in reliability and resilience of the line, with 24/7 operations due to resume in time for the 2018 freight peak.



Highlights

10-year
Project Wā heke launches to help develop a customer-focused 10-year growth strategy

90%
Customer satisfaction ratings for Interislander at 90%

First
KiwiRail wins Supreme Award at AUT Business Support Awards for work with Fonterra and Port of Tauranga to boost export growth

300,000
Social media video "Rail Safety Week 2017" is viewed more than 300,000 times

“Congratulations KiwiRail on the dedication put in by all the people involved.”

Social media message during the rebuild of the Main North Line.



Nathan Cole, Kākano Youth Arts Collective.

Partnerships with ports are delivering new rail-served operations around the country. Further intermodal hubs being developed near Hamilton and Christchurch will see more customers and ports using rail as an integral part of their supply chains.

We are also working closely with forestry owners, ports and regional leaders to identify ways to ensure the best locations for the development of log hubs for the expected large volume of logs as the 'Wall of Wood' comes on stream.

KiwiRail's innovative solutions and ability to adapt to disruption were recognised when it was presented with the supreme award at the 2017 AUT Business School Excellence in Business Support Awards. The Awards recognise and celebrate organisations and individuals that deliver quality products and services to help small, medium and large businesses maximise their potential. KiwiRail was acknowledged for our partnership with Port of Tauranga and Fonterra, aimed at boosting export growth. The three-way alliance has resulted in an improved supply chain, productivity, regional development, reduced carbon emissions and lower costs.

Tourism partnerships

KiwiRail works with regional government, economic development agencies, businesses and tourism operators to develop opportunities to support tourism growth and drive economic and social benefits in the regions.

In the central North Island our work with Tourism Ruapehu, regional leaders, businesses, tourism operators, and MBIE has led to the development of a strategy and regional action plan that will boost tourism growth with the support of rail.

The Northern Explorer stops in Ruapehu six times a week, delivering strong economic benefits through increased tourism spend and higher employment rates.

The region is famed for its outstanding natural beauty and range of outdoor activities and is one of New Zealand's favourite skiing destinations, but like many other regions its growth potential is restricted by limited resources.

The strategy encourages tourists to explore out-of-the way destinations through partnerships with local tourism operators and the provision

“What a fantastic sound to hear and see the trains coming through Rangiora and Belfast yesterday. The sound was like the song ‘You lift me up’ such music to our ears.”

Social media message during the rebuild of the Main North Line.

of premium experiences that are designed to attract visitors to Taupo and Ruapehu all year round.

In June this year the Government announced a \$10 million loan to Ruapehu Alpine Lifts for a new gondola that will provide access to the upper reaches of the mountain at Whakapapa and allow it to become a year-round destination.

Early projections indicate this new premium attraction could bring an additional 800 tourists to the region each day, many of whom will travel to and from the region by rail.

Communities

Our people are mindful of the impact of our operations on our neighbours and work hard to ensure KiwiRail is an active and collaborative participant in what matters most to the community. This has resulted in a number of activities over the past year.

- In April 2018 we joined with the Wahine 50 Charitable Trust to hold commemorative events in Wellington to honour the 53 lives lost when

the Union Steam Ship Company's passenger ferry Wahine sank off the coast of the city in 1968. The event provided opportunities for the friends and families of those who were lost, the rescuers - including those from the rail ferry Aramoana - and survivors to share their experiences.

- Te Papa, with the support of KiwiRail and Steam Incorporated, commemorated the 100th Anniversary of the Battle of Passchendaele with a vintage steam train return trip from Wellington to Trentham in October 2017.
- KiwiRail works to create enduring relationships with local councils and community partners to keep the rail corridor free from rubbish. Last year we facilitated community clean-ups of the rail tracks at a number of locations around the country. We also use these events as opportunities to promote rail safety.
- We collaborated with the Kākano Youth Arts Collective in West Auckland as part of an initiative to manage graffiti vandalism. Murals were painted on rail bridge

abutments by some of the at-risk young people supported by the trust. After this success Kākano was also commissioned to paint further murals on signalling equipment in the wider Auckland area to discourage taggers from putting themselves in danger by trespassing on the rail corridor. Kākano is a participant in a graffiti prevention and eradication focus group KiwiRail has established.

Safety

KiwiRail actively engages with communities, schools, and New Zealand Police to promote rail safety awareness and address incidences of risky behaviour and trespass on the rail corridor.

To further strengthen its activities in this important area, KiwiRail is establishing a nation-wide network of safety ambassadors to visit schools and attend community events to speak about rail safety. Ambassadors will be equipped with the resources needed to provide consistent and appropriate key messaging regarding rail safety including a rail safety awareness video aimed at primary school children.



A Rātana band helped welcome trains back to the Napier-Wairoa line.

KiwiRail has a strong relationship with local iwi and police, the Waikato District Council, and other community leaders in Ngaruawahia to address longstanding trespass issues in the Waikato township.

Following the death of an 11-year-old girl who was struck by a freight train travelling over the Ngaruawahia rail bridge in March this year, KiwiRail was able to quickly work with its community partners to arrange a public workshop on rail safety.

This event allowed residents to offer their opinions, ideas and solutions on local rail safety issues, and was attended by more than 100 people.

This year, KiwiRail delivered a series of level crossing seminars across the country, bringing together stakeholders from local government and the transport sector. The seminars aimed to increase awareness and to foster greater collaboration between stakeholders.

KiwiRail is a key sponsor of TrackSAFE NZ, a charitable trust that raises awareness about rail safety and ways to keep safe around tracks and trains. Rail Safety Week is an annual campaign run by the trust, KiwiRail and AT involving key stakeholders New Zealand Police, NZTA, Transdev and Greater Wellington Regional Council.

Te Kupenga Mahi

KiwiRail's Māori network, Te Kupenga Mahi (TKM) helps our people to connect with their whakapapa and advises the business of appropriate ways to implement Māori culture into our day-to-day activities. TKM also supports our business by facilitating interactions with local iwi regarding our activities, and at our public events.

Just one example of this work took place in May as we began some track repair work on the Main North Line along the Kaikoura coast, in an area with great cultural sensitivity and many sacred sites for local iwi.

A TKM South Island representative and KiwiRail track staff met a local kaumātua who briefed them on the history of the coastal area, in particular

the many urupa (burial sites) and wahi tapu (sacred sites) along the line.

Our team were in turn able to outline their planned activities through these areas and reinforce their commitment to ensuring the correct process was followed in the event any historical artefacts were uncovered as part of the maintenance programme. The session closed with a blessing to safeguard KiwiRail staff while they worked in the sacred areas.

Social media channels

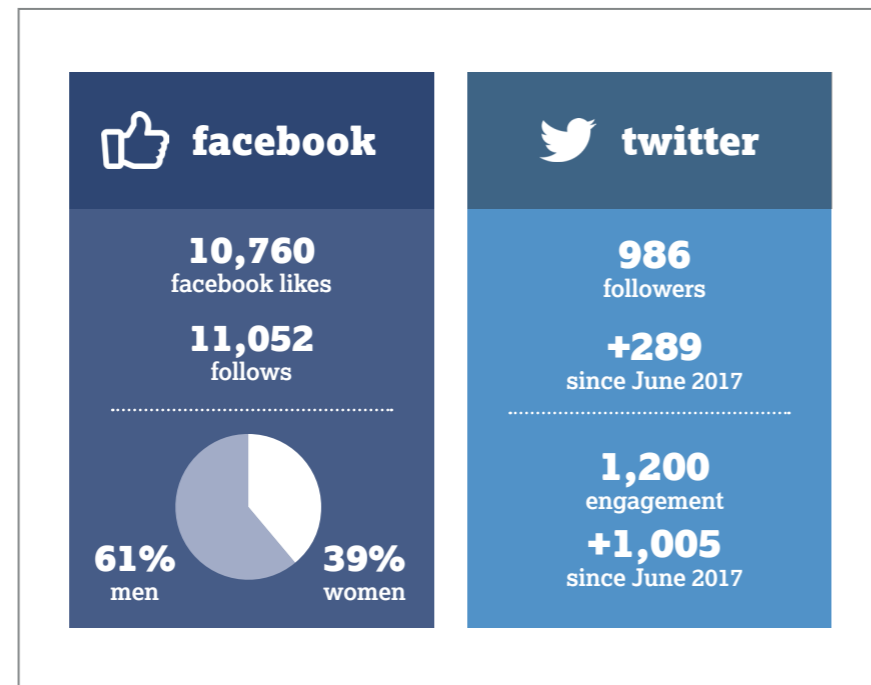
In December 2016 KiwiRail launched external Facebook and Twitter profiles, and this was followed with an Instagram profile last year. Over the past year we have seen huge growth in our social media following, particularly on Facebook, which now has more than 11,000 highly active followers.

Our social media channels enable us to inform and engage with our stakeholders, using videos and images to promote safety messages, celebrate our history and to provide updates on projects we are working on, such as the re-opening of the Napier–Wairoa line. In the past year, we have reached hundreds of thousands of New Zealanders using social media.

Social media also gives the public a convenient and transparent method to communicate with us. A highlight has been the messages of support and encouragement we regularly receive from the public, both in New Zealand and overseas. Having a channel where we can hear directly from the public about the difference rail is making in people's lives is a major morale boost for our people. During the rebuild of the Main North Line we received thousands of messages like these:

"What a fantastic sound to hear and see the trains coming through Rangiora and Belfast yesterday. The sound was like the song "You lift me up" such music to our ears."

"Congratulations KiwiRail on the dedication put in by all the people involved. The impact of this great achievement will benefit KiwiRail, the track and structures staff, the communities that are neighbours to the rail corridor. This achievement will make a huge impact on people getting their lives back to normal."



The first graduating class of our Toi Toi Māori Leaders programme.

Leadership development is about more than just developing leaders. In the case of KiwiRail's Toi Toi Māori Leaders Programme, it is about developing people, families and community.

Led by KiwiRail Leadership Capability Manager, Reuben Araroa, the programme involves formal and informal learning opportunities over a 12-month period, delivered in both marae and classroom settings. The curriculum includes behavioural competencies to accelerate learning and achievement, as well as an exploration of leadership theory using principles of Te Ao Māori.

Three two-day marae noho (workshops) allow participants to connect with their culture, and newly-acquired skills are put into action through completing practical assignments. To support their personal growth, participants are encouraged to seek out a mentor to provide guidance as they pursue their goals.

The results have been outstanding. Participants have gained confidence in

their ability as leaders to share their Toi Toi journey and learnings with the wider KiwiRail whanau and their communities. Equipped with tools for success, participants are now giving back to the organisation by actively driving culture shifts within their circles of influence and contributing to KiwiRail's diversity strategy.

Inspirational stories of personal and career growth were shared by participants at the Toi Toi graduation celebration in July, an event attended by participants' families along with Board members, KiwiRail Executive, and community leaders. Chief Executive Peter Reidy addressed the event attendees in te reo Māori, having devoted time over the past year to growing his own understanding of Te Ao Māori.

KiwiRail's growth in regional New Zealand is also enhanced by the Toi Toi leaders who engage with iwi. Historically, KiwiRail has relied on local kaumātua to guide and support our actions on marae. Toi Toi has enabled KiwiRail to engage with iwi, confident that it is growing capable Māori leaders within the organisation.

Environment

KiwiRail plays a critical role in New Zealand's transport system and in the health of the economy, our communities and the natural environment.

KiwiRail plays a critical role in New Zealand's transport system and in the health of the economy, our communities and the natural environment.

EY's The Value of Rail in New Zealand report, released in 2017 calculated the often hidden benefits of rail as being worth \$1.5 billion per year to New Zealand. That includes

the cost savings from reduced congestion in our cities; avoided road maintenance costs; fewer injuries and fatalities on our roads; and the significant carbon emission savings through moving people and freight by rail.

For every tonne of freight carried by rail there is a 66% carbon emissions saving over heavy road freight.



Highlights

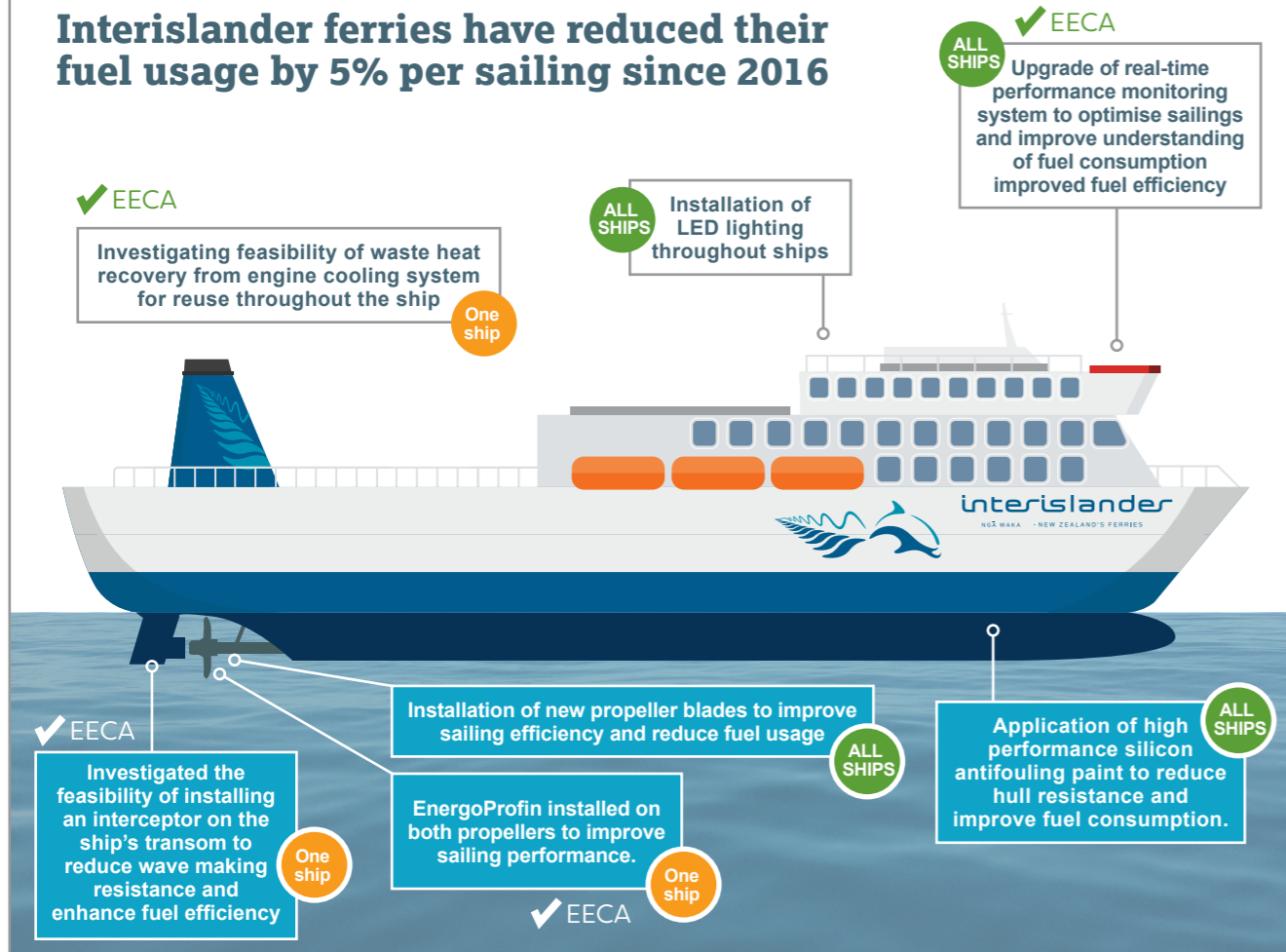
1.1m

Rail freight reduces heavy vehicle impact on New Zealand roads by 1.1 million truck trips, saving 66.3 million litres of fuel and 180,212 tonnes of CO₂ emissions

Eight months

Reached EECA energy saving target in just eight months

Interislander ferries have reduced their fuel usage by 5% per sailing since 2016



Dodie Joseph, Train Examiner Maintenance.

This year the Coalition Government signalled its support for modal shift to rail. In the Government Policy Statement on Land Transport (GPS), a mode-neutral approach to transport planning and investment was introduced, and carbon emission reduction was highlighted as a priority. A measure of the contribution that KiwiRail can make is that while transport accounts for 19% of New Zealand's carbon emissions, rail generates less than 1% of that total.

EY found that New Zealand's rail services reduce carbon emissions by 488,000 tonnes a year - the equivalent of taking 87,000 cars off the road.

A significant part of that saving comes from the commuter rail services in Auckland and Wellington, services which KiwiRail, as owner and maintainer of the network, enables. Last year 34 million commuter trips were made on our network, with numbers in Auckland rising by 20% over the last two years.

The GPS looks to increase the numbers of commuters on rail, with funding for maintaining and improving rail infrastructure on key passenger services in major metropolitan areas, including inter-regional rail services.

Driving economic growth in the regions is a key strategy for KiwiRail with projects funded through the Government's Provincial Growth Fund. In 2018, \$5 million was committed to rebuild the Napier to Wairoa line which, when fully utilised, could avoid 5,714 trucks on Hawke's Bay roads, reducing carbon emissions and providing a seamless supply chain to port.

This is one of the initiatives KiwiRail is pursuing to increase the role rail plays in moving logs from New Zealand's "Wall of Wood".

Energy efficiency

Building on rail's competitive advantage as an energy efficient mode of transport, KiwiRail is also committed to cutting its own fuel use.

A key component of our energy saving programme is a close collaboration with the Energy Efficiency and

Conservation Authority (EECA) to progress programmes and set targets across our rail and ferry operations.

All areas of the organisation are working to meet KiwiRail's 73.5 gigawatt hours (GWh) energy saving target by 2020, a target that was raised after the initial 20 GWh target was reached just eight months after the agreement was established in November 2016.

EY found that New Zealand's rail services reduce carbon emissions by 488,000 tonnes a year - the equivalent of taking 87,000 cars off the road.

With fuel for trains and ferries making up the overwhelming bulk of KiwiRail's energy consumption, that is the area of greatest focus, with a number of initiatives underway that will deliver large gains over the next two years.

The Locomotive Fuel Savings project has already shown significant success, delivering fuel savings of 17 million litres, or \$12 million, since 2015 through the ground-breaking Driver Advisory System (DAS), and other energy initiatives on our rail freight services.

The ferry initiatives being undertaken in collaboration with EECA aim to deliver substantial energy savings through a number of projects, including propeller caps on the Aratere designed to reduce resistance, a new fuel monitoring system which - as DAS does for locomotives - can provide vital information on how to sail the ship safely with improved fuel efficiency, and studies on the feasibility of heat recovery in the ships.

Waste management

Another area of focus over the past year has been the reinvigoration of KiwiRail's waste management programme with a focus on exploring new ways to reduce industrial and passenger waste.

KiwiRail's Great Journeys of New Zealand tourism services have signed the New Zealand Tourism Sustainability Commitment, with one early initiative reducing the use of plastic packaging and straws.

Rail is a material-intensive industry and over the past few years KiwiRail has developed a recycling programme for used rail infrastructure materials which still have life left in them.

In 2018, the programme has seen sleepers and rail previously installed at Raurimu, on the North Island Main Trunk line, used in the rebuild of the Napier-Wairoa Line.

United Nations Sustainable Development Goals

KiwiRail is committed to playing its part in an international drive towards sustainable development. This year we have pledged to support New Zealand's involvement in the UN's Sustainable Development Goals.

In September 2015, leaders from the 193 member states of the United Nations adopted the 17 Sustainable Development Goals (SDGs), covering social and economic development issues including poverty, hunger, health, education, climate change, gender equality, water, sanitation, energy, urbanisation, environment and social justice. Each goal has a number of specific targets associated with it, totalling 169 targets in all.

As a key enabler of social, environmental and economic growth in New Zealand, KiwiRail is committed to playing its part in supporting progress towards the goals which aim to leave the planet in a better place for future generations.

The UN sees the goals as a call to action for Government, the private sector, society and citizens to address the world's most urgent challenges.

In 2018, KiwiRail undertook an assessment to identify where the business can have the most meaningful impact over the short to medium term. The assessment involved mapping the SDGs to KiwiRail's material issues. As a result, we have identified three SDGs which strongly align with our organisational strategy and activities, and in which we have the ability to influence.

These three goals are:



- SDG 8 Decent Work and Economic Growth

- SDG 9 Industry, Innovation and Infrastructure
- SDG 13 Climate Action

Over the next 12 months KiwiRail will further analyse our response to these goals and their associated targets, and explore how our activities can align to support the outcomes they seek. We will measure our outputs in line with the goals.

Several programmes of work are already underway which will assist KiwiRail's ambition. Here we have listed some of the specific targets and how our work programmes can influence outcomes.

| Sustainable Development Goal | KiwiRail's Response | SDG target | KiwiRail's Work Programme |
|---|--|--|---|
| <p>8 – Decent Work and Economic Growth</p>  | <p>While KiwiRail has a number of diversity and inclusiveness programmes which contribute to decent work for New Zealanders, our primary contribution to this goal is through sustainable tourism. KiwiRail is a signatory to the NZ Tourism Sustainability Commitment and has big plans for growth.</p> | <p>Target 8.9 - By 2030, devise and implement policies to promote sustainable tourism that creates jobs and promotes local culture and products.</p> | <p>The Great Journeys of NZ</p> <p>KiwiRail has plans to significantly increase its economic contribution to New Zealand's regions through new services and additional capacity on our scenic rail journeys. This will lead to job creation and opportunities for new tourism businesses in the regions.</p> <p>Interislander</p> <p>KiwiRail is planning for the future of its ferry fleet across Cook Strait which is a major contributor to New Zealand tourism and economic growth in the regions. By 2025 new ships may be in use which will be optimised for passengers and provide greater capacity to meet the growth of visitors. Interislander is also a signatory to the NZ Tourism Sustainability Commitment.</p> |

| Sustainable Development Goal | KiwiRail's Response | SDG target | KiwiRail's Work Programme |
|---|---|--|---|
| <p>9 – Industry, Innovation and Infrastructure</p>  | <p>KiwiRail is committed to a resilient and integrated transport system for New Zealand and the contribution this makes towards a sustainable future. KiwiRail enables the significant growth in commuters on rail in our biggest cities and is working closely with Government on new connections for freight and people in the regions.</p> | <p>Targets 9.1 - Develop quality, reliable, sustainable and resilient infrastructure, including regional and trans-border infrastructure, to support economic development and human well-being, with a focus on affordable and equitable access for all.</p> | <p>Napier to Wairoa line In 2018, KiwiRail began work on the reinstatement of the Napier to Wairoa line to take logging trucks off the road and reduce carbon emissions.</p> <p>Hamilton to Auckland passenger service KiwiRail is working closely with local and central Government on a proposal for a daily commuter service between Hamilton and Auckland which will reduce congestion and connect communities along the route.</p> <p>Main North Line rebuild Following the Kaikoura earthquake in 2016, KiwiRail has worked to rebuild transport connections in the South Island. Freight services are now running at night to allow the rebuild of the road and rail to continue through the day. It is anticipated that work may be complete by the end of 2018.</p> |
| <p>13 – Climate Action</p>  | <p>KiwiRail's strategic focus is on future emissions reduction across the transport sector. Its energy savings and carbon emissions reduction programme provides tangible evidence of our commitment to climate action. This includes fuel reduction programmes and reduced carbon intensity of freight operations.</p> | <p>Target 13.2 - Integrate climate change measures into national policies, strategies and planning.</p> | <p>Modal shift In 2017 KiwiRail published EY's "The Value of Rail in New Zealand" analysis which showed \$1.5 billion in unseen benefits from rail such as emissions reduction, congestion easing and safety on roads. KiwiRail is working closely with Government and customers on how business can account for these benefits when they shift to rail.</p> <p>Energy Efficiency Programme KiwiRail is continuing to build on its Locomotive Fuel Savings project with the Driver Advisory System (DAS) and other energy initiatives. Similar initiatives are also underway with our ferries to reduce fuel consumption, including propeller caps on the Aratere designed to reduce resistance, and a new fuel monitoring system which will work as DAS does for locomotives</p> <p>Glidepath to Electrification KiwiRail is investigating energy options for its busiest freight routes between Auckland, Hamilton and Tauranga including extension of Auckland's rail electrification. New fuel options such as hydrogen are also in the early stages of investigation.</p> |

Strategic outlook

Changes in New Zealand's transport outlook, coupled with major shifts toward environmental sustainability, urban growth, and new technology, present exciting opportunities and some challenges for KiwiRail.

We are addressing these by leveraging rail's natural advantages, following our strategy to ensure a customer-centric focus across all aspects of our business, and proactively engaging with Government around its priorities for transport and regional development.

New Zealand's transport outlook

The Government's Policy Statement on Land Transport, issued in June 2018, represents a significant change

in focus. It prioritises safety, access and mobility, reducing emissions and delivering value for money, with a mode neutral approach that better integrates land use and transport planning.

That mode neutral approach opens new funding mechanisms for KiwiRail, including through the National Land Transport Fund administered by NZTA. Under the Future of Rail review, options for long-term funding for KiwiRail will be investigated offering certainty for customers and

the ability to procure long-term assets efficiently.

The statement also establishes funding for maintenance and improvement of heavy rail infrastructure for key passenger rail services in major metropolitan areas, including existing and new inter-regional commuter rail services to support housing and employment opportunities.

To support this Government focus, KiwiRail is working closely with



The iRex team are engaging with Interislander staff on options for future ferries and terminals.

Hamilton City Council, Waikato District Council and Auckland City Council to develop a proposal for a preliminary Hamilton to Auckland commuter service that will test demand for a frequent return service between the two cities.

KiwiRail, Greater Wellington and Horizons Regional Councils, will also be submitting a business case for funding the Capital Connection, linking Palmerston North and Wellington, which has operated at a loss for a number of years.

Sustainability

The Government is committed to the Paris Accord, which aims to reduce emissions below 2005 levels by 30% by 2030, and has announced its intention to introduce legislation to further reduce New Zealand's greenhouse gas emissions by 2050.

At the same time consumers are increasingly looking to business to lead initiatives to tackle environmental and sustainability issues.

With 66% fewer carbon emissions per tonne of freight carried by rail over heavy road transport, KiwiRail is building on its natural advantage as an energy efficient mode of transport to support environmental outcomes. We are actively working with the Government and businesses to facilitate modal shift from road to rail to achieve safer and more efficient transport for New Zealand.

In July KiwiRail Chief Executive Peter Reidy was one of 60 CEOs to sign up to a CEO Climate Change Statement, committing the organisation to public emissions reduction targets, measuring emissions and working with suppliers to reduce their emissions.

KiwiRail is internally focused on identifying and prioritising further fuel efficiency opportunities through our partnership with Energy Efficiency and Conservation Authority (EECA) and the implementation of our Energy Management Plan. Over time, this will make the organisation even more carbon efficient, ensuring we give value to our customers and meet sustainability targets.

KiwiRail is also in the early stages of investigating the potential of zero-carbon hydrogen-fuelled locomotives, following growing interest in Europe and trials in the UK and Germany.

Increasing demand for metropolitan rail

The Upper North Island is experiencing a period of sustained population growth with increases concentrated in large cities, such as Auckland, Tauranga and Hamilton.

In Auckland, KiwiRail continues its role as an Access Provider for the City Rail Link (CRL) which, once complete, will reduce journey times, enable higher service frequencies and improve capacity across the Auckland Metro.

KiwiRail is working collaboratively with Auckland Council as the Council determines the transport requirements of the region through its Auckland Transport Alignment Programme (ATAP). In April 2018, ATAP announced a series of rail network upgrades, including investment for the electrification of the Auckland Metro to Pukekohe. The Pukekohe section will support the benefits of the CRL once the project reaches completion.

ATAP has also announced a Third Main Line between Westfield and Wiri to ease rail congestion. The line will improve operational efficiency for freight and passenger trains operating on the Auckland Metro by allowing more frequent trains and reducing conflicts between passenger and freight services.

In Wellington, KiwiRail and Greater Wellington Regional Council are working together on a \$49 million contract to replace the overhead line system that supplies power to Metlink's commuter trains on the Hutt Line. The project is part of a \$98 million four-year project to replace the overhead power system between Wellington Station, Melling and Upper Hutt, as well as Ngaio and Johnsonville. This work is vital for the resilience of KiwiRail's network and will improve commuter travel times upon completion.

Regional development

Rail is a key driver of economic growth in the regions through linking exporters to ports, bringing tourists and passengers to cities and reducing road maintenance costs while improving safety.

KiwiRail continues to work closely with its customers, local government and other stakeholders to plan an optimal freight transport system that

will support export and domestic markets in key areas.

The Government has funded a number of rail projects through its \$1 billion a year Provincial Growth Fund (PGF) such as the reopening of the Napier to Wairoa line for forestry freight, upgrade in Whanganui to support customers and investigations into rail growth in Taranaki, Southland and Kawerau.

With 66% fewer carbon emissions per tonne of freight carried by rail over heavy road freight, KiwiRail is building on its natural advantage as an energy efficient mode of transport to support environmental outcomes.

Future proposals are being developed to significantly grow tourism in the regions, to open up new routes for forestry and to take more dairy freight by rail to ports. The PGF offers a once-in-a-generation opportunity to revive rail in the regions, supporting regional development and reducing emissions by taking heavy trucks off the roads.

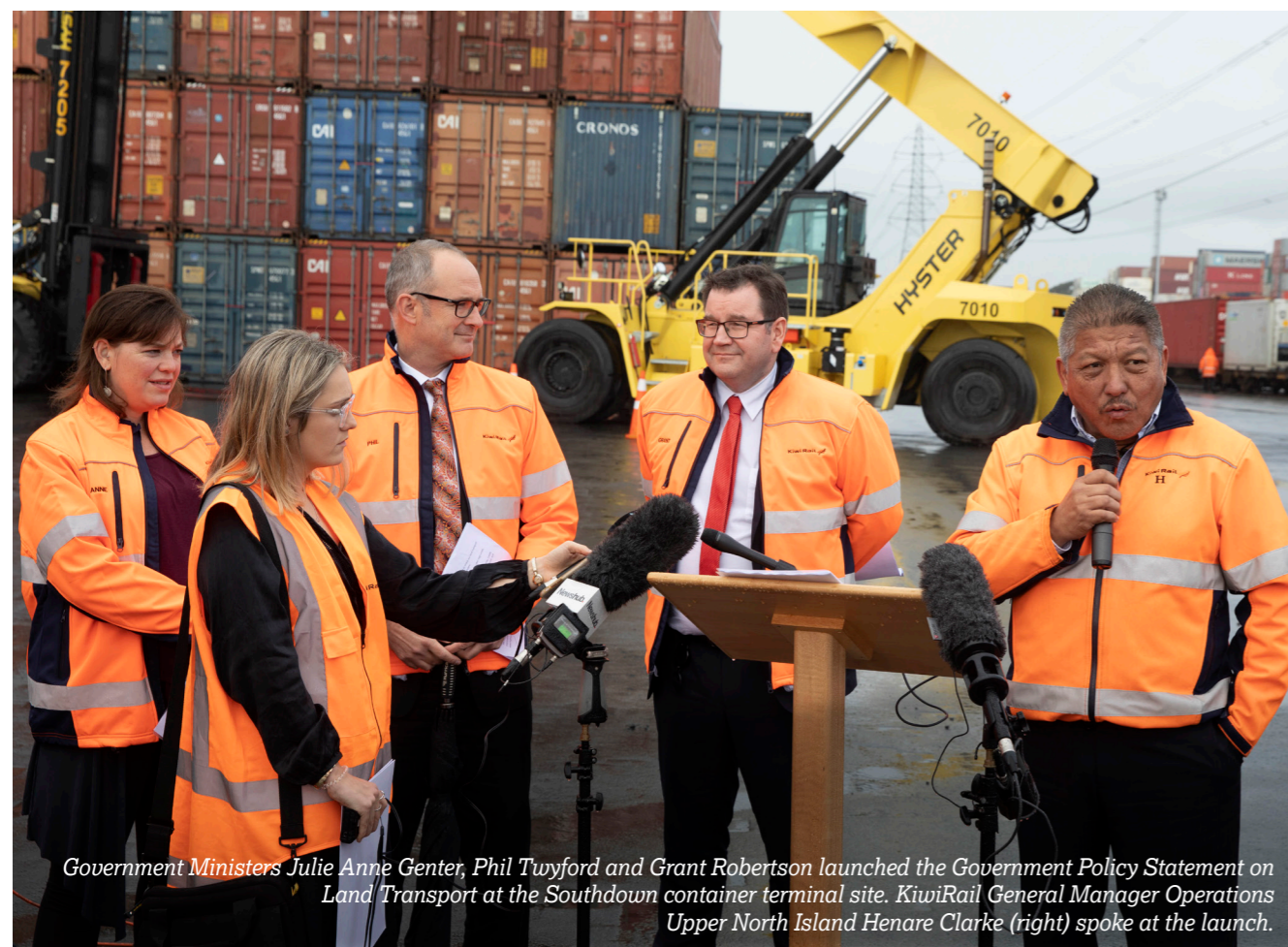
Digitalisation and smart data

Internationally, new technologies and new business models are changing the traditional approach to logistics. The industry is facing digital disruption along its entire value chain, from freight forwarding, brokerage, and long-distance transportation to warehousing, contract logistics, and last-mile delivery.

KiwiRail recognises that to compete and be relevant to our customers, we need to increasingly interact

on a digital basis. Our customer insight project Wā heke this year highlighted where we can extend our use of digital technology and offer more services to customers. A number of initiatives are underway, including enabling customers to book and manage freight orders on a purely digital basis (system to system), and the extension of operational technology platforms beyond workforce management to timetabling and fleet management. In the long term it will also enable deeper integration with partners and customers as part of the digital transport ecosystem.

Innovations include smart data options for new rolling stock to allow for the capture and sharing of detailed information on freight performance while monitoring the condition and service requirements of trains and tracks. The future use of this technology will enable the roll-out of fully integrated and intelligent transport networks which can provide deeper insights into our customers' needs and KiwiRail's operations. For instance the implementation of live-tracking systems would enhance user experience, and would enable the business to make faster and more informed business decisions.



Government Ministers Julie Anne Genter, Phil Tuiyford and Grant Robertson launched the Government Policy Statement on Land Transport at the Southdown container terminal site. KiwiRail General Manager Operations Upper North Island Henare Clarke (right) spoke at the launch.

The KiwiRail Board



Brian Corban CNZM, QSO
Acting Chair/Deputy Chair appointed July 2018



Trevor D Janes
Chairman ended 30 June 2018



Dame Paula Rebstock
Deputy Chair ended 30 April 2018



John Leuchars
Director



Guy Royal
Director



Paul Harper
Director



Mike Pohio
Director



John Dennehy
Director



Bob Major
Director



Susan McCormack
Director

Brian Corban CNZM, QSO
Acting Chair/Deputy Chair

Brian Corban was appointed to the KiwiRail Board as Deputy Chair in July 2018, and will act as Chair of KiwiRail until such time as a new Chair is appointed.

Brian is an Auckland-based company director and lawyer. His experience includes Chair of Genesis for 10 years, Chair of Radio New Zealand Ltd, and the Foundation Chair of Television New Zealand Ltd. He has previously served as Deputy Chair of NZ Railways Corporation/KiwiRail in 2008.

He is also Chair of the Melanesian Trust Board, a Board member of Auckland War Memorial Museum, a director of Ngatarawa Wines and a number of private companies and a trustee of various community trusts. He is a former Chair of Auckland City Mission and member of the Waitangi Tribunal.

Trevor D Janes
Chairman

Trevor Janes joined the Board in November 2016 as Chairman and retired from the Board effective 30 June 2018.

Trevor has an extensive background in investment banking and finance. He is currently Chairman of Abano Healthcare, the Tokelau International Trust Fund and Transport Investments Ltd. He is also Deputy Chair and Investment Committee Chair of the Accident Compensation Corporation (ACC). Trevor is a member of the NZ Markets Disciplinary Tribunal and the Postal Network Access Committee. He is a Chartered Fellow for the Institute of Directors, and a Fellow of both the NZ Institute of Financial Professionals and Chartered Accountants of Australia and New Zealand.

Dame Paula Rebstock
Deputy Chair

Dame Paula Rebstock joined the Board in 2009 and completed her term on 30 April 2018.

Dame Paula is an Auckland-based economist and company director and brings an extensive governance background to KiwiRail. She is Chair of the Board of the Accident Compensation Corporation. Dame Paula is also Chair of the Insurance and Financial Services Commission, and a Director of Auckland Transport. She is a member of the University of Auckland Business School Advisory Board, and Chair of the Vulnerable Children's Board.

John Leuchars
Director

John Leuchars joined the Board in 2010. John is a professional company director and civil engineer. He brings significant experience in senior management and governance of international consulting engineering companies. John has experience as a Board member of

professional institutions, private and public companies and not-for-profit organisations. John is a Board member of the Wellington Gateway Project (Transmission Gully Motorway). He is a member of the Auckland City Council Value for Money review panel. He was a member of the Board of Genesis Energy until April 2018, and is a Fellow of the Institute of Professional Engineers New Zealand.

Guy Royal
Director

Guy Royal joined the Board in 2013.

Guy has more than 20 years' experience in private equity and commercial and corporate law in New Zealand, Hong Kong, Vietnam and the United Kingdom. He is Managing Director of Tuia Group, a professional advisory firm with offices in New Zealand, Papua New Guinea and Samoa. Guy has sat on the Boards of a number of private and public-sector businesses including Crown Forest Rental Trust, Film and Literature Review Board and New Zealand Fast Forward Fund Limited.

Paul Harper
Director

Paul Harper joined the KiwiRail Board in May 2016.

He brings experience in directorships and senior management roles across the transport and infrastructure sectors. Paul was the foundation Chairman of Netlogix Ltd and is a Director of SeaLink Group and Health Alliance Ltd. His varied roles have included marine engineer, shore-based shipping company management in Norway, Scotland, Brazil and Australia, Group General Manager of the Interisland Line, and establishment CEO of Carter Holt Harvey Lodestar. He is also a Chartered Member of the Institute of Directors and a member of the Chartered Institute of Logistics and Transport.

Mike Pohio
Director

Mike Pohio joined the Board in May 2016.

Mike is a Hamilton-based director. Mike currently holds directorships on the Boards of Panuku Development Auckland, NIWA, OSPRI and Te Atiawa Iwi Holdings. He is also Chairman of BNZ Partners, Waikato Region. His executive career includes CEO of Tainui Group Holdings (TGH) for eight years and senior executive roles for companies including Port of Tauranga, Fonterra, NZ Dairy Group and Elders Pastoral. His governance background includes six years as a shareholder and director of NZL Group, seven years on the Transpower Board and a Ministerial appointment to the University of Waikato Council. Mike holds an MBA from IMD, Lausanne and an FCA from the Chartered Accountants Australia and New Zealand.

John Dennehy
Director

John Dennehy joined the KiwiRail Board in May 2017.

John brings with him a valuable background in financial services focusing on international transport and infrastructure, including rail, shipping, road and aviation in the private and state-owned sectors.

John has served on a number of Boards in New Zealand and in the United Kingdom, and is currently Chair of the Mercer Group Ltd.

Bob Major
Director

Bob Major joined the KiwiRail Board in May 2017.

Bob brings valuable governance experience to the Board. He has spent many years working in the dairy industry, including Fonterra where he was a member of the Senior Leadership Team, the New Zealand Dairy Board and the New Zealand Dairy Research Institute. He is a current director of Westland Milk Products, BioVittoria Ltd and Chair of Gibb Holdings (Nelson) Ltd. He is a former Chair of Mud House Wines and director of a number of companies including Sealord Group and Barker Fruit Processors.

Susan McCormack
Director

Susan McCormack joined the KiwiRail Board in May 2017.

A partner at Mortlock McCormack Law, Sue specialises in corporate and commercial law. She is the Pro-Chancellor of the University of Canterbury and has previously been a director of the Lyttelton Port Company Limited, the New Zealand Symphony Orchestra and the Public Trust.

Where a date for appointment to the Board precedes 1 January 2013, it is a reference to the date that the Director was appointed to the Board of the New Zealand Railways Corporation (NZRC), the former parent of the Group. Following a restructure of the Crown's rail interests in 2012/13 in which the majority of NZRC's rail assets and liabilities were vested in KiwiRail Holdings Limited, the then Directors of NZRC were appointed to the Board of KiwiRail Holdings Limited as the new parent company for the Group.

The KiwiRail Executive Team



Peter Reidy
Chief Executive



Kate Jorgensen
Chief Financial Officer



Todd Moyle
Chief Operations Officer



Alan Piper
Group General Manager Sales and Commercial



David Gordon
Group General Manager Investment, Planning and Risk



Andrew Norton
Group General Manager Human Resources



Katie McMahon
Group General Manager Zero Harm



Mark Thompson
Group General Manager Interislander

Peter Reidy
Chief Executive

Peter joined KiwiRail as Chief Executive in March 2014.

He brings to KiwiRail a successful track record of building and leading service and infrastructure-based businesses in the logistics, energy, building products and asset management sectors in New Zealand, Australia, Asia and the United Kingdom. Prior to KiwiRail, Peter held a number of senior leadership roles with Downer Group, Fletcher Building, Todd Energy and Freightways.

Kate Jorgensen
Chief Financial Officer

Kate joined KiwiRail in March 2015.

She is a strategic CFO who partners with the business to drive results. Prior to KiwiRail, Kate worked for Fletcher Building for six years, where she held several senior commercial roles, including Divisional CFO for Heavy Building Products and Divisional CFO for the Infrastructure Products Division.

Todd Moyle
Chief Operations Officer

Todd joined KiwiRail in February 2007.

Todd leads the operational areas of KiwiRail covering Network Services, Rolling Stock Asset Services, Rail Operations and Train Control. Before moving into his current role, Todd was Group General Manager Network Services, overseeing KiwiRail's 'below rail' network of track, bridges and tunnels along with the Engineering function. Todd has more than 15 years in the construction and operation of rail networks across New Zealand and the United Kingdom. Prior to that, Todd worked in roles across the pulp and paper sector in New Zealand.

Alan Piper
Group General Manager Sales and Commercial

Alan joined KiwiRail in September 2013.

He is responsible for the freight, tourism, commercial vehicles and passenger revenue portfolios. This includes marketing, pricing and sales planning to improve margin and revenue. He previously worked in freight and logistics sales and general management roles with CourierPost and Pace Couriers and had a successful 23-year career with the Bank of New Zealand in retail banking and branch strategy.

David Gordon
Group General Manager Investment, Planning and Risk

David joined KiwiRail in 2007.

He oversees the strategic capital projects and property portfolio and leads KiwiRail's collaboration with Government, agencies and local government on transport policy and investment issues. Previously, David held the roles of General Group Manager Asset Management and Investment, and General Manager Network Performance. Before joining KiwiRail, he worked as a consultant in the transport infrastructure business, was Planning and Development head for Wellington International Airport and a Senior Manager in the strategy consulting team of Ernst and Young.

Andrew Norton
Group General Manager Human Resources

Andrew joined KiwiRail in June 2014.

He brings extensive experience in Human Resources and Industrial Relations, in both large public and commercial organisations. Andrew has an in-depth understanding of Industrial Relations, strong engagement skills with front line engineering and customer service teams, and experience in developing Executive leadership in large organisations. He previously held high level roles with Public Service Association (PSA) NZ, Auckland District Health Board and worked as Downer Australia's Executive General Manager Human Resources.

Katie McMahon
Group General Manager Zero Harm

Katie joined KiwiRail in June 2017.

She is responsible for leading KiwiRail's health and safety strategy programme. Katie has worked in the rail industry for more than 10 years and has experience in leading risk management and health and safety practices for large rail businesses. Katie began her career in the Australian Army and prior to joining KiwiRail, was Manager Safety, Health and Environment for Aurizon's Queensland operations.

Mark Thompson
General Manager Interislander

Mark joined KiwiRail in 2014.

He oversees the Interislander operations. Mark has spent 30 years at senior leadership roles in the service industry, primarily the courier and express freight segment but with various roles in total supply chain management, M&A and Board Chair, and recently in the software industry. Mark has held leadership roles on both sides of the Tasman with companies such as NZ Couriers, CourierPost, Star Track Express, Convergia in the United States and the Philippines and NetSuite.

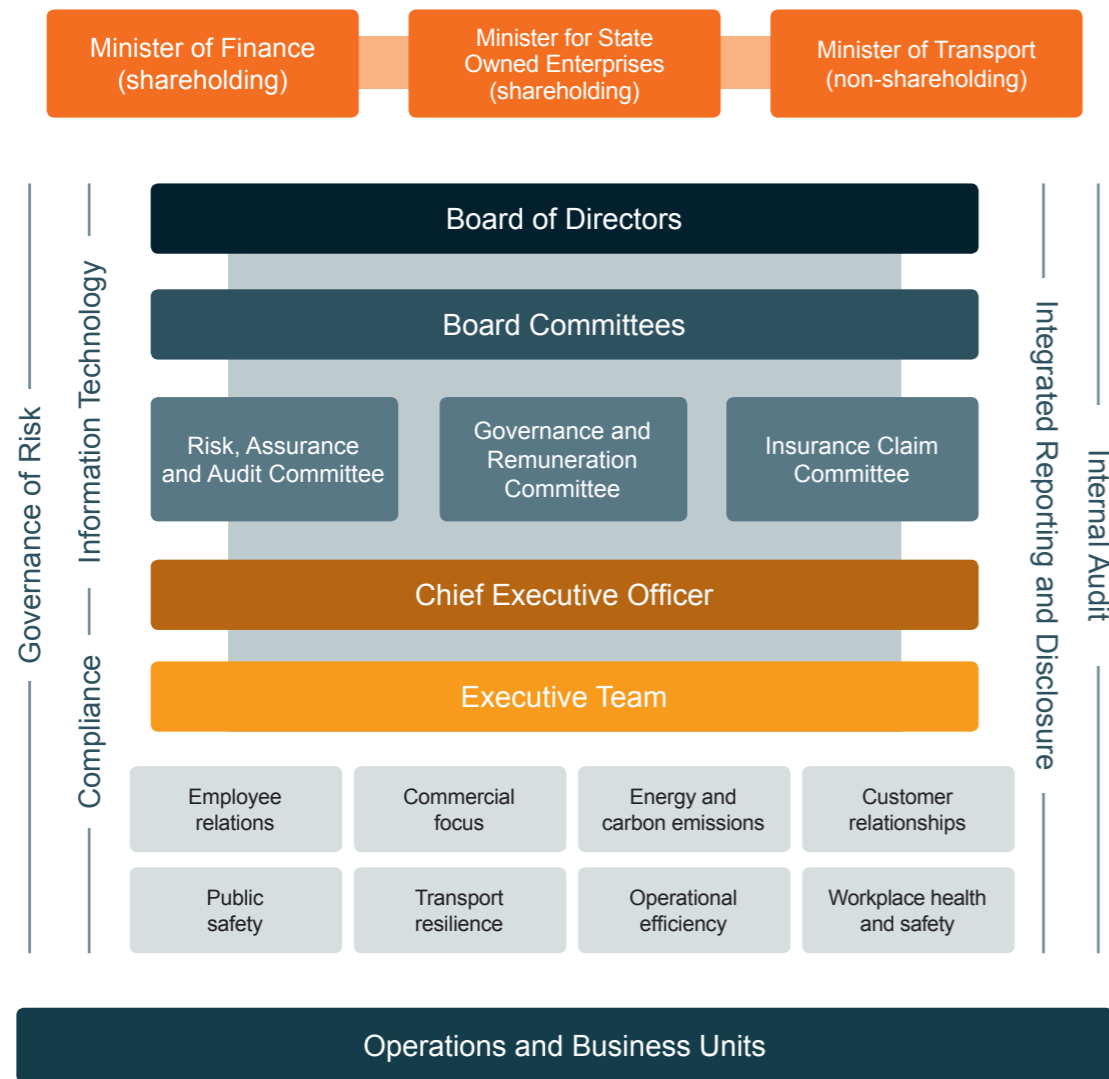
How we are governed

Our commercial mandate

KiwiRail Holdings Limited is a limited liability company incorporated under the Companies Act 1993 and a state owned enterprise (SOE) under the State Owned Enterprises Act 1986.

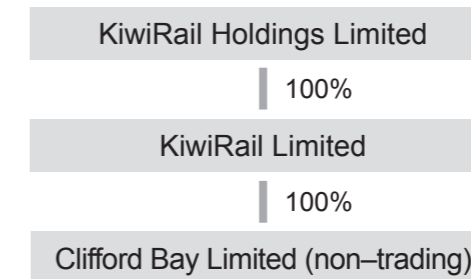
As an SOE, all of KiwiRail's shares are held by Shareholding Ministers of the Crown. They are held in equal proportions by the Minister of Finance and the Minister for State Owned Enterprises.

The diagram below shows our governance structure:



The principal objective of every SOE is to operate as a successful business and, to this end, to be as profitable and efficient as comparable businesses that are not owned by the Crown. SOEs are also required to be good employers and to exhibit a sense of social responsibility.

During the financial year ended 30 June 2018 the Group comprised KiwiRail Holdings Limited and its subsidiaries as detailed in the below diagram:



Governance functions

The Board of Directors of KiwiRail is appointed by the Shareholding Ministers and is accountable to the Shareholding Ministers for the performance of KiwiRail. The Shareholding Ministers may jointly remove directors at any time and entirely at their discretion.

The role of the Board is to guide the strategic direction of KiwiRail and to direct and oversee management.

The Board establishes objectives and sets strategies to achieve those objectives. The Board, in the context of the approved policy, risk and compliance framework within which the Group operates, monitors the performance of management and the Group against those strategies. The Board has delegated the day-to-day management of the Group to the Chief Executive.

Typically the Board meets 11 times during the year as part of the regular

meeting agenda. In addition, there are three committees of the Board which meet four times a year. These committees are described further below.

The Board is committed to ensuring that the Shareholding Ministers are informed of all major issues and developments affecting the company. Such information is communicated in various ways including Annual/Integrated reports, half yearly reports and continuous disclosure statements.

| Risk, Assurance and Audit Committee (RAAC) | Governance and Remuneration Committee (GREM) | Insurance Claim Committee (ICC) |
|--|---|---|
| Four meetings per year | Four meetings per year | Four meetings per year |
| Mike Pohio (Committee Chair) Guy Royal John Dennehy John Leuchars | Dame Paula Rebstock (Committee Chair to 30 April 2018) Bob Major (Committee Chair from 1 May 2018) Sue McCormack Paul Harper John Dennehy Brian Corban | Sue McCormack (Committee Chair) Trevor Janes (to 30 June 2018) Mike Pohio John Leuchars |
| Assists the Board with the discharge of its responsibilities in relation to audit, finance and risk management. The committee monitors the roles, responsibilities and performance of management and the auditors in financial reporting, business risk management systems and internal control systems. | Assists the Board in establishing remuneration strategies and policies for the Chief Executive and his direct reports that support an increase in productivity and the retention of staff. Also assists the Chairperson and the Board to consider performance and skill set of the Board. | As a result of the magnitude 7.8 (M _w) Kaikoura Earthquake on 14 November 2016, KiwiRail has a material insurance claim in respect of property damage and consequential losses suffered. The role of the Committee is to assist the Board in discharging its responsibility to exercise due care and diligence in the governance and oversight of KiwiRail's insurance claim, with a view to obtaining what is properly payable to KiwiRail under its insurance policies. |

Executive committees

There are five committees which the Board have issued the Executive team responsibility for. These are the Health, Safety and Environment Committee (HSEC), the Operational Safety, Health and Environment Committee (SHE), the Asset and Infrastructure Management Committee (AIMC), the Risk Committee, and the Property Committee.

The HSEC meets quarterly to gain assurance against the Enterprise Risk Management controls, compliance with Safety, Health and Environment obligations including licencing and code requirements. This committee also checks progress against strategy, Enterprise SHE risk reviews and deep dives where required. The Chief Executive is the Executive owner of this committee.

The SHE is a monthly meeting of the Executive that enables oversight of the operational performance of the business over the past month and considers incident learning, hazard and near miss reporting and other operational performance measures. This performance is considered against the relevant Safety, Health and Environment risk profiles and Zero Harm strategic initiatives to determine impact. The Chief Executive is the executive owner of this committee.

The AIMC is responsible for the performance and management of,

and risks associated with, KiwiRail's material assets. The Group General Manager Investment, Planning and Risk is the Executive owner of this committee.

The Risk Committee is responsible for monitoring the development of KiwiRail's Enterprise Risk Management Strategy throughout KiwiRail's business units. The Group General Manager Investment, Planning and Risk is the Executive owner of this committee.

The Property Committee is an advisory committee of senior external consultants to advise on KiwiRail's property strategy and planning. The Chief Executive is the Executive owner of this committee.

Each of the committees is comprised of Executive team members, and meets four times each year, with the exception of SHE which meets monthly. The Executive team provide updates to the Board as required.

Approach to risk management

KiwiRail is committed to ensuring that risk management is an important element and integral part of the way we undertake our operations. We take an enterprise-wide approach to risk management, and consider the potential impact of risks on our processes, activities, stakeholders, products and services. An Enterprise Risk Management Strategy has been developed and implemented across the

organisation. This Strategy is based on principles that are industry best practice and the National Rail Systems Standard 4 (NRSS), which is aligned to the international standard for Risk Management: AS/NZS ISO31000:2009.

At a strategic level, effective governance of risk is achieved through the Risk, Assurance and Audit Committee of the Board. At an operational level, a risk champion network is in place, and risk is actively managed and reported through an enterprise risk register.

Insurance and indemnity

In accordance with the Companies Act 1993 and the terms of its constitution, KiwiRail indemnifies the members of the Board in respect of liability for conduct that comprises acts or omissions by the Directors in good faith and in the performance or intended performance of KiwiRail's functions and for any costs incurred in defending or settling any claim or proceeding related to liability for such conduct.

KiwiRail has insured the Directors and employees of the Group against any costs or liabilities of the type referred to in section 162(5) of the Companies Act.

In addition, KiwiRail indemnifies Directors of its wholly-owned subsidiaries against any costs or liabilities of the type referred to in section 162(5) of the Companies Act.

Directors Attendance and Remuneration

The following Directors attended Board and Committee meetings during the 2018 financial year:

| | Board meeting | RAAC meeting | GREM meeting | ICC meeting |
|---------------------|---------------|--------------|--------------|-------------|
| Trevor Janes | 11/11 | - | - | 3/3 |
| Dame Paula Rebstock | 10/10 | - | 4/4 | - |
| Guy Royal | 10/11 | 4/4 | - | - |
| Mike Pohio | 10/11 | 4/4 | - | 2/3 |
| John Leuchars | 11/11 | 3/4 | - | 2/3 |
| Paul Harper | 10/11 | - | 5/5 | - |
| John Dennehy | 10/11 | 4/4 | 2/2 | - |
| Bob Major | 10/11 | - | 4/5 | - |
| Susan McCormack | 11/11 | - | 5/5 | 3/3 |

Board Committees are open to any Director to attend. Directors who are not Committee members regularly attend Committee meetings. Those additional attendances are not recorded in the table above.

There were five GREM meetings held in FY18 as there was an off-cycle meeting in October 2017. There were three ICC meetings held in FY18 as the committee was first established in November 2017.

Note 22 of the financial statements sets out what fees Directors earned during FY18. Trevor Janes retired from the Board effective 30 June 2018. Dame Paula Rebstock's term as director ended on 30 April 2018.

Employee remuneration

There were 908 KiwiRail employees (or former employees) who received remuneration and benefits in excess of \$100,000 (not including Directors) in their capacity as employees during the year ended 30 June 2018, as set out below

| | | | |
|-------------|---|---------|-----|
| 1,190-1,200 | 1 | 240-250 | 6 |
| 760-780 | 1 | 230-240 | 3 |
| 570-580 | 2 | 220-230 | 4 |
| 560-570 | 1 | 210-220 | 4 |
| 500-510 | 1 | 200-210 | 18 |
| 480-490 | 1 | 190-200 | 15 |
| 390-400 | 2 | 180-190 | 16 |
| 340-350 | 1 | 170-180 | 20 |
| 320-330 | 2 | 160-170 | 24 |
| 300-310 | 3 | 150-160 | 29 |
| 290-300 | 2 | 140-150 | 58 |
| 280-290 | 1 | 130-140 | 83 |
| 270-280 | 1 | 120-130 | 123 |
| 260-270 | 2 | 110-120 | 195 |
| 250-260 | 3 | 100-110 | 285 |

| | |
|--|-----|
| Total employees earning in excess of \$100,000 | 908 |
| Employees who are included but who are no longer at KiwiRail as at 30 June 2018 | 48 |
| Net total employees earning in excess of \$100,000 and employed at KiwiRail as at 30 June 2018 | 860 |

This includes fixed remuneration, employee KiwiSaver contributions, settlement payments and redundancy payments for all permanent employees. It also includes short term incentive payments made to eligible staff in accordance with KiwiRail's remuneration policies.

Key Performance Indicators

KiwiRail Holdings Limited
Statement of Corporate Intent comparisons

| | 2018 Actual | 2018 Plan |
|---|----------------|--------------|
| Sustaining a Zero Harm Environment | | |
| Total Recordable Injuries | 177 | 131 |
| SPAD As | 18 | 18 |
| Safe working irregularities | 327 | 228 |
| Derailments – mainline | 4 | 5 |
| Derailments – terminal | 82 | 82 |
| GHG emissions per NTK | 27.76gms | 26.19gms |
| Truck avoidance | 1.1 | 1.1 |
| Meeting our financial targets | | |
| Operating Surplus | \$49m | \$30-50m |
| Operating Surplus – excluding earthquake impacts | \$94m | \$92m |
| Operating Margin | 8% | 5-8% |
| Operating Margin – excluding earthquake impacts | 14% | 14% |
| Capital Expenditure - net of grants | \$261m | \$271m |
| Property | | |
| - Reduce Operational Footprint | 6% | 5% |
| - Reduce Inward Lease Liability | 0% | 5% |
| - Reduce Vacant Land | 8% | 2% |
| Empowering our people | | |
| Employee Net Promoter Score | +1 | 0 |
| Engaging our customers and stakeholders | | |
| Revenue | \$616m | \$603-623m |
| Revenue – excluding earthquake impacts | \$663m | \$662m |
| Freight trading growth | 0% | (2)-3% |
| Freight trading growth – excluding earthquake impacts | 2% | 5% |
| Passenger trading growth | 8% | 17% |
| Passenger trading growth – excluding earthquake impacts | 7% | 8% |

Key Performance Indicators

KiwiRail Holdings Limited
Statement of Corporate Intent comparisons

| | 2018 Actual | 2018 Plan |
|--|----------------|--------------|
| Delivering Operational Performance | | |
| On Time Performance | | |
| - Freight Trains – Premium | 87% | 90% |
| - % Interislander services to advertised sailings | 99% | 99% |
| Operating costs as a percentage of revenue | 92% | 92-95% |
| Operating costs as a percentage of revenue – excluding earthquake impacts | 86% | 86% |
| Network Renewals | | |
| - New Sleepers Laid | 76,000 | 64,000 |
| - New Rail Laid | 22km | 20km |
| - New Turnouts | 44 | 37 |
| Availability of all locomotives | 92% | 89% |
| Wagon availability | 91% | 91% |
| Shareholder Return Measures | | |
| Total Shareholder Return | n/a | n/a |
| Dividend Yield | 0 | 0 |
| Dividend Pay-out | 0 | 0 |
| Return on Average Equity | (35%) | (43%) |
| Profitability/Efficiency Measures | | |
| Return on Average Capital Employed | (25%) | (28%) |
| Operating Margin | 8% | 6% |
| Leverage/Solvency Measures | | |
| Shareholder's Funds to Total Assets | 61% | 52% |
| Gearing Ratio (net) | 21% | 37% |
| Interest Cover | 4.4 | 3.0 |
| Solvency (current assets/current liabilities) | 0.74 | 1.04 |

Vote Transport

Vote Transport: Non-Departmental Capital and Other Expenditure

Activities undertaken by KiwiRail that are funded through Vote Transport Non-Departmental Capital and Other Expenditure are detailed below.

Rail – Public Policy Projects (M72)

This appropriation is limited to public policy rail initiatives.

| | 2018 Actual | 2018 Budget |
|---|-------------|-------------|
| Amount of Appropriation (\$000) | 3,270 | 3,270 |
| Performance Measure: | | |
| The public policy projects are carried out in line with the programme | 100% | 100% |

Rail – Public Policy Projects (M72)

This appropriation is limited to public safety works.

| | 2018 Actual | 2018 Budget |
|---------------------------------|-------------|-------------|
| Amount of Appropriation (\$000) | 500 | 500 |
| Performance Measure: | | |
| A safer railway system | Achieved | Achieved |

Rail – KiwiRail Equity Injection (M72)

This appropriation is limited to equity injections to KiwiRail Holdings Limited offset by property transactions in New Zealand Railways Corporation.

| | 2018 Actual | 2018 Target |
|---------------------------------|-------------|-------------|
| Amount of Appropriation (\$000) | 3,026 | 12,100 |

Rail – KiwiRail Holdings Limited (M72)

This appropriation is limited to a capital injection to KiwiRail Holdings Limited to finance approved capital expenditure on the New Zealand rail system.

| | 2018 Actual | 2018 Target |
|--|-------------|-------------|
| Amount of Appropriation (\$000) | 220,000 | 220,000 |
| Performance Measure: | | |
| Capital is invested in the New Zealand rail system as approved by shareholding Ministers | 100% | 100% |

Rail – KiwiRail Holdings Limited (M72)

This appropriation is limited to loans to KiwiRail Holdings Limited to fund capital projects and provide working capital.

| | 2018 Actual | 2018 Target |
|--|-------------|-------------|
| Amount of Appropriation (\$000) | 163,500 | 163,500 |
| Performance Measure: | | |
| All documentation and transactional requirements are met | 100% | 100% |

Rail – Wellington Metro Rail Network Upgrade (M72)

This appropriation is limited to catch up investment in the Wellington metro rail network which will enable sustainable operation of the network through the Metro Rail Operating model.

| | 2018 Actual | 2018 Target |
|--|---|-------------|
| Amount of Appropriation (\$000) | 11,665 | 25,900 |
| Performance Measure: | | |
| Work is carried out per the agreed programme | 45% completed with remainder carried forward to 2018/19 | 100% |

The above tables do not include activities funded through the Appropriation (2017/18 Supplementary Estimates) Bill.



Brad Claridge, Track Group.

Financial statements

KiwiRail Holdings Limited

Statement of Comprehensive Income

For the financial year ended 30 June 2018

| | Note | GROUP 2018 | GROUP 2017 |
|--|------------|----------------|----------------|
| | | \$m | \$m |
| Operating revenues | 2 | 615.8 | 594.7 |
| Operating expenses | 3 | (567.3) | (542.5) |
| Operating surplus | | 48.5 | 52.2 |
| Capital grants | 4 | 39.8 | 27.6 |
| Depreciation and amortisation expenses | 8(a), 8(b) | (86.2) | (77.1) |
| Foreign exchange and commodity gains/(losses) | 5 | 9.3 | (3.6) |
| Impairment | 8(c) | (27.0) | (218.3) |
| Impairment – earthquake | 8(c) | (221.6) | (77.5) |
| Insurance proceeds | 26 | 8.0 | 100.0 |
| Movement in value of investment properties | 13 | 4.0 | 6.1 |
| Net finance expenses | 6 | (7.9) | (7.6) |
| Other costs – earthquake | | (2.8) | - |
| Other income | | - | 0.5 |
| Share in profit of joint venture | 15 | - | 0.4 |
| Net deficit before taxation | | (235.9) | (197.3) |
| Income tax expense | 7 | - | - |
| Net deficit after taxation | | (235.9) | (197.3) |
| Other comprehensive income/(loss) | | | |
| <i>Items that can be reclassified into net surplus/deficit:</i> | | | |
| Gains from cash flow hedges | | - | 0.6 |
| <i>Items that cannot be reclassified into net surplus/deficit:</i> | | | |
| Building revaluation | 8(c) | - | (0.3) |
| Total comprehensive loss | | (235.9) | (197.0) |

The accompanying notes form part of these financial statements.

KiwiRail Holdings Limited

Statement of Financial Position

For the financial year ended 30 June 2018

| | Note | GROUP 2018 | GROUP 2017 |
|-------------------------------------|------|----------------|----------------|
| | | \$m | \$m |
| Current assets | | | |
| Cash and cash equivalents | 9 | 87.0 | 83.4 |
| Trade and other receivables | 10 | 91.0 | 138.0 |
| Inventories | 11 | 71.6 | 65.0 |
| Financial assets | 12 | 8.4 | 0.3 |
| Assets held for sale | 15 | - | 1.9 |
| | | 258.0 | 288.6 |
| Non-current assets | | | |
| Property, plant and equipment | 8(a) | 898.2 | 748.1 |
| Investment property | 13 | 82.8 | 76.5 |
| Intangible assets | 8(b) | 0.3 | 0.4 |
| Financial assets | 12 | 1.0 | 0.2 |
| Trade and other receivables | 10 | 0.4 | 0.4 |
| | | 982.7 | 825.6 |
| Total assets | | 1,240.7 | 1,114.2 |
| Current liabilities | | | |
| Trade and other liabilities | 16 | 103.8 | 132.5 |
| Employee entitlements | 17 | 58.5 | 55.1 |
| Financial liabilities | 12 | 181.3 | 180.4 |
| Income taxes payable | 7 | - | - |
| Provisions | 18 | 6.0 | 5.0 |
| | | 349.6 | 373.0 |
| Non-current liabilities | | | |
| Employee entitlements | 17 | 39.3 | 36.9 |
| Financial liabilities | 12 | 86.6 | 106.2 |
| Provisions | 18 | 6.0 | 6.0 |
| | | 131.9 | 149.1 |
| Total liabilities | | 481.5 | 522.1 |
| Equity | | | |
| Share capital | 23 | 1,233.8 | 833.8 |
| Retained earnings | | (494.9) | (264.0) |
| Asset revaluation reserve | | 20.3 | 22.3 |
| | | 759.2 | 592.1 |
| Total liabilities and equity | | 1,240.7 | 1,114.2 |


Brian Corban, Acting Chair
23 August 2018

Mike Pohio, Director
23 August 2018

The accompanying notes form part of these financial statements.

Kiwirail Holdings Limited

Statement of Movements in Equity

For the financial year ended 30 June 2018

| GROUP | Note | Share Capital | Retained Earnings | Asset Revaluation Reserve | Cash Flow Hedge Reserve | Total |
|--|------|----------------|-------------------|---------------------------|-------------------------|----------------|
| | | \$m | \$m | \$m | \$m | \$m |
| As at 30 June 2016 | | 613.6 | (81.7) | 22.6 | (0.6) | 553.9 |
| Net deficit for the period | | - | (197.3) | - | - | (197.3) |
| Other comprehensive income/(loss) | | | | | | |
| Gains from cash flow hedges | | - | - | - | 0.6 | 0.6 |
| Buildings revaluation reserve | | - | - | (0.3) | - | (0.3) |
| Total comprehensive income/(loss) | | - | (197.3) | (0.3) | 0.6 | (197.0) |
| Transactions with owners | | | | | | |
| Capital Investment | | 220.2 | - | - | - | 220.2 |
| Crown appropriation - land transactions | 19 | - | 15.0 | - | - | 15.0 |
| As at 30 June 2017 | | 833.8 | (264.0) | 22.3 | - | 592.1 |
| Net deficit for the period | | - | (235.9) | - | - | (235.9) |
| Other comprehensive income/(loss) | | | | | | |
| Revaluation reserve of transferred buildings | | - | 2.0 | (2.0) | - | - |
| Total comprehensive (loss) | | - | (233.9) | (2.0) | - | (235.9) |
| Transactions with owners | | | | | | |
| Capital Investment | | 400.0 | - | - | - | 400.0 |
| Crown appropriation - land transactions | 19 | - | 3.0 | - | - | 3.0 |
| As at 30 June 2018 | | 1,233.8 | (494.9) | 20.3 | - | 759.2 |

The accompanying notes form part of these financial statements.

Kiwirail Holdings Limited

Statement of Cash Flows

For the financial year ended 30 June 2018

| | Note | GROUP 2018 | GROUP 2017 |
|---|------|----------------|----------------|
| | | \$m | \$m |
| Cash flows from operating activities | | | |
| Receipts from customers | | 620.0 | 597.9 |
| Interest received | | 2.7 | 2.8 |
| Payments to suppliers and employees | | (590.9) | (541.5) |
| Interest expense | | (13.1) | (13.3) |
| Net cash from operating activities | 21 | 18.7 | 45.9 |
| Cash flows from investing activities | | | |
| Sale of property, plant and equipment | | 1.1 | 1.0 |
| Capital grant receipts | | 33.7 | 27.6 |
| Insurance proceeds | | 29.9 | 72.1 |
| Sale of investment in joint venture | | 2.7 | - |
| Purchase of property, plant and equipment and investment properties | | (491.8) | (416.4) |
| Purchase of intangibles | | (6.7) | (4.8) |
| Net cash used in investing activities | | (431.1) | (320.5) |
| Cash flows from financing activities | | | |
| Crown capital investment | | 430.0 | 190.2 |
| Proceeds from NZRC land sales | | - | 15.7 |
| Loans | | - | 62.2 |
| Repayment of borrowings | | (12.5) | (5.3) |
| Repayment of finance lease liability | | (1.5) | (1.3) |
| Net cash from financing activities | | 416.0 | 261.5 |
| Net increase/(decrease) in cash and cash equivalents | | 3.6 | (13.1) |
| Cash and cash equivalents at the beginning of the year | | 83.4 | 96.5 |
| Cash and cash equivalents at the end of the year | 9 | 87.0 | 83.4 |

The accompanying notes form part of these financial statements.

KiwiRail Holdings Limited

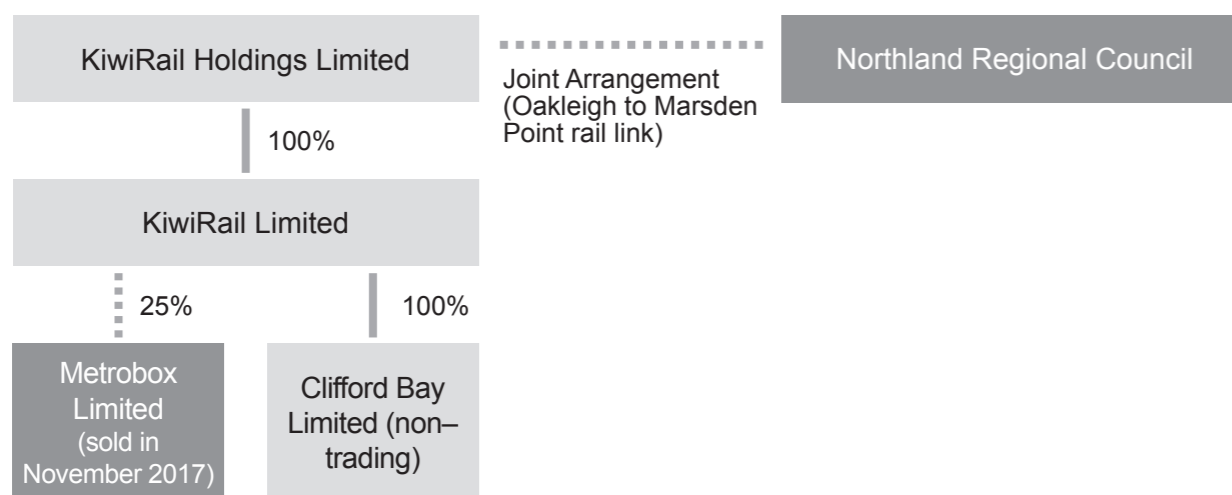
Notes to the Financial Statements

For the financial year ended 30 June 2018

1. GROUP INFORMATION

(a) Reporting entity

KiwiRail Holdings Limited ("KHL", "the Parent") is a company domiciled in New Zealand, registered under the Companies Act 1993 and is included within the First Schedule of the State-Owned Enterprises Act 1986. The beneficial shareholder of the Parent is the Crown. The Group comprises KiwiRail Holdings Limited and its subsidiaries as detailed in the diagram below:



The following activities are required to be carried out by the Group:

- Provide end-to-end transport supply chain services and connect customers with global markets
- Own and operate a national rail network which meets the needs of our customers
- Provide for the transport of bulk and consolidated freight
- Provide ferry services (forming the 'bridge' between the North and South Islands) for rail and road freight and for passengers and their vehicles
- Support rail passenger services in metropolitan areas and long distance services for both domestic and tourist markets
- Manage and develop property holdings for rail operations and appropriate third-party land use

The financial statements of the Group are for the year ended 30 June 2018 and were authorised for issue by the Board of Directors on 23 August 2018.

(b) Basis of preparation

The financial statements have been prepared 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 for-profit entities and other applicable Financial Reporting Standards. They comply with the State-Owned Enterprises Act of 1986, the requirements of the Companies Act 1993 and the Financial Reporting Act 2013. The financial statements have been prepared on the basis of historical cost, except for certain non-financial assets and derivative financial instruments, which have been valued at fair value.

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

Unless otherwise specified, all dollar amounts in these financial statements and accompanying notes are stated in New Zealand dollars and all values are expressed in millions of dollars (\$m). The functional and presentation currency is New Zealand dollars.

(c) Consolidated financial statements

The consolidated financial statements of the Parent and its subsidiaries include the financial statements of subsidiary companies using the acquisition method of consolidation. The acquisition method of consolidation involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree.

Subsidiary companies are those entities that are controlled directly or indirectly by the Parent.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

(d) Standards and interpretations

The Group applied for the first time certain amendments to the NZ IFRS standards, which are effective for the Group as at 1 July 2017. The nature and the effect of these changes are described below:

- Amendments to NZ IAS 7 *Statement of Cash Flows* – requires the disclosure of changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. This information is provided in note 12(c). As permitted on initial application, comparatives have not been provided.

NZ IFRS standards and interpretations that have recently been issued or amended but are not yet effective have not been adopted by the Group for the annual reporting period ended 30 June 2018. Significant changes are outlined below:

- IFRS 15 *Revenue from Contracts with Customers* is effective for periods on or after 1 January 2018. The core principle of IFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The Group is currently assessing the impact of this standard.
- IFRS 16 *Leases* requires lessees to account for all leases under a single on-balance sheet model in a similar way to finance leases under NZ IAS 17. These changes are effective for periods on or after 1 January 2019. The Group is currently assessing the impact of this standard.

(e) Comparatives

The presentation of some information has changed from the previous period with prior period balances re-classified to be comparable with current year figures.

(f) Significant accounting judgements, estimates and assumptions

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, revenues and expenses. These estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates.

Management's significant judgements, estimates and assumptions are outlined in the relevant notes to the financial statements.

(g) Rail review and going concern

A Rail Review, led by the Ministry of Transport, is currently underway. The review is working towards:

- defining the purpose of rail in a multi modal transport system, including the outcomes and objectives for rail that the Shareholder seeks; and
- determining the appropriate structure, capital requirements and funding mechanisms of the Group to reflect that purpose, and the outcomes and objectives.

As at 30 June 2018, this review is still in progress.

Decisions following the completion of the rail review may affect the mix of assets and operations, the extent of the rail network, and which of the entities within the Crown might own those assets and/or perform those operations.

While the outcome of the review is unknown, decisions that are made following the completion of the review may have an impact on the future carrying value of assets in the Group. The Group currently values most of its rail network assets on a cash generating basis. Were this to change to a non-cash generating basis using optimised depreciated replacement cost, the carrying value of the rail network assets would increase. Based on current year figures, the assets would increase from \$206m (2017: \$105m) to \$6,202m (2017: \$5,210m). In addition to this, the amount by which the Group's rail network assets are annually impaired would reduce and the depreciation charge would increase. The amount impaired in the current year was \$249m (2017: \$296m) while the depreciation amount would increase by \$292m (2017: \$210m).

KiwiRail continues to operate on a commercial basis. KiwiRail remains dependent on shareholder support to meet capital expenditure requirements for its integrated rail network. Existing commitments from the shareholder for equity funding is \$415m for the 2018/19 and 2019/20 financial years. Based on KiwiRail's current cashflow forecast the shareholders committed equity funding enables KiwiRail to meet its current and forecast financial obligations through to late 2019.

Should any unexpected events occur, KiwiRail will either need to seek additional equity contributions from the shareholder and/or significantly reduce its capital expenditure programme or dispose of assets to maintain a positive cashflow position.

KiwiRail's business planning is dependent on additional equity funding for a number of years, with future equity funding still to be confirmed. With the support of its shareholder KiwiRail is also investigating other funding options, for example, the Provincial Growth Fund, the National Land Transport Fund and Central Government. We have completed these financial statements on a going concern basis on the assumption that shareholder support will continue in line with their announced election manifestos.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

2. OPERATING REVENUES

| | GROUP 2018 | GROUP 2017 |
|---------------------------------|---------------|---------------|
| | \$m | \$m |
| Freight | 350.7 | 345.6 |
| Interislander | 137.0 | 130.2 |
| Infrastructure | 52.5 | 49.6 |
| Property | 45.1 | 42.9 |
| Scenic | 27.8 | 22.8 |
| Other | 2.7 | 3.5 |
| Tranz Metro | - | 0.1 |
| Total operating revenues | 615.8 | 594.7 |

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable by the Group to the extent it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue represents amounts receivable for goods and services provided in the normal course of business once significant risks and rewards of ownership have been transferred to the buyer.

3. OPERATING EXPENSES

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Salaries and wages | 312.0 | 303.0 |
| Restructuring | 1.9 | 1.5 |
| Defined contribution plan employer contributions | 11.2 | 10.8 |
| Other employee expenses | 8.2 | 2.7 |
| Total staff expenses | 333.3 | 318.0 |
| Amount capitalised | (55.5) | (51.6) |
| Total employee expenses | 277.8 | 266.4 |
| Materials and supplies | 109.2 | 103.7 |
| Fuel and traction electricity | 70.1 | 62.1 |
| Lease and rental costs | 44.6 | 48.2 |
| Incidents and insurance | 15.3 | 8.1 |
| Contractors' expenses | 8.2 | 8.4 |
| Audit fees | 0.4 | 0.3 |
| (Recovery from)/impairment of receivables | (0.5) | 0.9 |
| Directors' fees | 0.4 | 0.4 |
| Gain on disposal of property, plant and equipment | (0.9) | (0.4) |
| Other expenses | 42.7 | 44.4 |
| Total operating expenses | 567.3 | 542.5 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

4. CAPITAL GRANTS

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Capital grants (Ministry of Transport funded) | 15.0 | 6.2 |
| Other capital grants | 24.8 | 21.4 |
| Total capital grant income | 39.8 | 27.6 |

The Group receives grants from Government entities for the purpose of maintaining the railway networks and infrastructure.

Where the asset being funded is depreciated over its useful life, the funding is recognised as income on a straight line basis over the same life. Grants received for services provided are recognised when the requirements of the relevant grant agreement are met. Funding received as reimbursements for capital projects are recognised in the same period as the expenditure to which it relates.

5. FOREIGN EXCHANGE AND COMMODITY GAINS AND LOSSES

| | GROUP 2018 | GROUP 2017 |
|--|---------------|---------------|
| | \$m | \$m |
| Net realised foreign exchange and commodity (losses) | (1.3) | (3.6) |
| Net change in the fair value of derivatives | 10.6 | - |
| Total foreign exchange and commodity gains/(losses) | 9.3 | (3.6) |

The table above excludes foreign exchange and commodity gains on fuel related contracts of \$1.7m (2017: \$0.4m loss) which are reported within 'Fuel and Traction Electricity Expenses' in note 3.

Foreign currency translation

Foreign currency transactions are translated to New Zealand currency at the exchange rates ruling at the transaction date.

Monetary assets and liabilities in foreign currencies at balance date are translated at exchange rates ruling at balance date. All exchange differences arising on the translation of monetary assets and liabilities in foreign currencies, whether realised or unrealised, are recognised in net surplus or deficit, except when deferred in equity as qualifying cash flow hedges.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items in a foreign currency that are measured based on historical costs are translated using the exchange rate at the date of the transaction.

6. NET FINANCE EXPENSES

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Finance income | | |
| Interest income on bank deposits | 3.2 | 2.3 |
| | 3.2 | 2.3 |
| Less Finance expenses | | |
| Interest expense on borrowings | (13.7) | (13.0) |
| Interest expense on finance lease | (0.4) | (0.4) |
| Net change in fair value of interest rate swaps | 3.0 | 3.5 |
| | (11.1) | (9.9) |
| Net finance expenses | (7.9) | (7.6) |

Finance income and expenses

Interest income from call and term deposits and interest expense on borrowings are recognised in net surplus or deficit using the effective interest rate method. Interest income is recognised as it accrues.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

7. TAXATION**Income tax**

All members of the Group are subject to income tax. The accounting policies applied are as follows:

Income tax expense comprises both current and deferred tax. Income tax expense is charged or credited to net surplus or deficit, except when it relates to items charged or credited directly to equity, in which case the tax is charged to equity.

(a) Current tax

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at reporting date and any adjustments to tax in respect of previous years.

(b) Deferred tax

Deferred tax is provided for temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the carrying amounts used for taxation purposes. No deferred tax asset is recognised in the financial statements as it is not probable that future taxable surpluses will be available against which the asset can be utilised.

(c) Tax benefit/(expense)

| | GROUP 2018 | GROUP 2017 |
|--|---------------|---------------|
| | \$m | \$m |
| Components of tax expense | | |
| Current tax expense | - | - |
| Deferred tax expense | - | - |
| Tax benefit/(expense) | - | - |
| Reconciliation between tax expense and accounting surplus | | |
| Deficit before tax | (235.9) | (197.3) |
| Tax at 28% | (66.1) | (55.2) |
| Tax effect of: | | |
| Non-deductible expenditure | 6.5 | (25.5) |
| Other temporary differences | 59.6 | 80.7 |
| Tax benefit/(expense) | - | - |

The Group has an unrecognised deferred tax asset of \$964.9m (2017: \$905.9m) arising from deductible temporary differences of \$2,399.3m (2017: \$2,298.5m) and unused tax losses of \$1,144.3m (2017: \$936.9m).

Imputation credits

The Group has formed an imputation group. The Group has access to \$1.2m imputation credits (2017: \$1.2m imputation credits).

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

8. NON-FINANCIAL ASSETS**(a) PROPERTY, PLANT AND EQUIPMENT**

| 2018 | Land | Buildings | Railway Infrastructure | Rolling Stock | Ships | Plant & Equipment | Assets Under Construction | Total |
|---------------------------------|------|-----------|---------------------------|---------------|-------|----------------------|------------------------------|---------|
| Cost/Valuation | \$m | \$m | \$m | \$m | \$m | \$m | \$m | \$m |
| Balance at 1 July 2017 | 3.1 | 40.7 | 105.6 | 330.6 | 232.3 | 229.9 | 71.7 | 1,013.9 |
| Additions | - | 5.3 | 145.4 | 49.9 | 3.5 | 28.5 | 247.1 | 479.8 |
| Disposals | - | (0.1) | - | (2.2) | - | (1.2) | - | (3.5) |
| Category Transfers | - | (1.4) | - | - | - | (0.4) | 0.9 | (0.9) |
| Revaluation | - | - | - | - | - | - | - | - |
| Impairment | - | (0.3) | (137.0) | (39.0) | - | (0.6) | (216.5) | (393.4) |
| Impairment Reversal | - | - | 92.0 | (31.0) | - | - | - | 61.0 |
| Balance at 30 June 2018 | 3.1 | 44.2 | 206.0 | 308.3 | 235.8 | 256.2 | 103.2 | 1,156.8 |
| Accumulated depreciation | | | | | | | | |
| Balance at 1 July 2017 | - | 0.2 | 0.5 | 94.1 | 64.3 | 106.7 | - | 265.8 |
| Depreciation expense | - | 3.1 | 7.3 | 31.6 | 25.2 | 18.7 | - | 85.9 |
| Disposals | - | - | - | (1.6) | - | (1.2) | - | (2.8) |
| Category Transfers | - | - | - | - | - | - | - | - |
| Revaluation | - | - | - | - | - | - | - | - |
| Impairment | - | - | (5.9) | (10.1) | - | (0.1) | - | (16.1) |
| Impairment Reversal | - | - | (1.9) | (72.3) | - | - | - | (74.2) |
| Balance at 30 June 2018 | - | 3.3 | - | 41.7 | 89.5 | 124.1 | - | 258.6 |
| Net book value | | | | | | | | |
| At 1 July 2017 | 3.1 | 40.5 | 105.1 | 236.5 | 168.0 | 123.2 | 71.7 | 748.1 |
| At 30 June 2018 | 3.1 | 40.9 | 206.0 | 266.6 | 146.3 | 132.1 | 103.2 | 898.2 |

| 2017 | Land | Buildings | Railway Infrastructure | Rolling Stock | Ships | Plant & Equipment | Assets Under Construction | Total |
|---------------------------------|------|-----------|---------------------------|---------------|-------|----------------------|------------------------------|---------|
| Cost/Valuation | \$m | \$m | \$m | \$m | \$m | \$m | \$m | \$m |
| Balance at 1 July 2016 | 3.1 | 55.5 | 109.0 | 338.4 | 138.7 | 211.1 | 39.2 | 895.0 |
| Additions | - | 5.4 | 106.7 | 29.3 | 93.6 | 21.6 | 181.2 | 437.8 |
| Disposals | - | - | - | (2.3) | - | (2.8) | - | (5.1) |
| Revaluation | - | (6.9) | - | - | - | - | - | (6.9) |
| Impairment | - | (13.3) | (110.1) | (34.8) | - | - | (148.7) | (306.9) |
| Balance at 30 June 2017 | 3.1 | 40.7 | 105.6 | 330.6 | 232.3 | 229.9 | 71.7 | 1,013.9 |
| Accumulated depreciation | | | | | | | | |
| Balance at 1 July 2016 | - | 6.1 | - | 74.7 | 43.5 | 94.4 | - | 218.7 |
| Depreciation expense | - | 3.4 | 4.4 | 33.1 | 20.8 | 14.9 | - | 76.6 |
| Disposals | - | - | - | (1.9) | - | (2.6) | - | (4.5) |
| Revaluation | - | (6.6) | - | - | - | - | - | (6.6) |
| Impairment | - | (2.7) | (3.9) | (11.8) | - | - | - | (18.4) |
| Balance at 30 June 2017 | - | 0.2 | 0.5 | 94.1 | 64.3 | 106.7 | - | 265.8 |
| Net book value | | | | | | | | |
| At 1 July 2016 | 3.1 | 49.4 | 109.0 | 263.7 | 95.2 | 116.7 | 39.2 | 676.3 |
| At 30 June 2017 | 3.1 | 40.5 | 105.1 | 236.5 | 168.0 | 123.2 | 71.7 | 748.1 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

8. NON-FINANCIAL ASSETS (continued)**(a) PROPERTY, PLANT AND EQUIPMENT (continued)****(i) Recognition and Measurement**

Property, plant and equipment is shown at cost or valuation, less any accumulated depreciation and accumulated impairment losses. Items of property, plant and equipment under construction are classified as assets under construction. Cost includes expenditure that is directly attributable to the acquisition or construction of the asset.

Where an asset is acquired for nil or nominal consideration the asset is recognised initially at fair value, where fair value can be reliably determined; and the fair value of the asset received less costs incurred to acquire the asset is also recognised as income in net surplus or deficit.

(ii) Revaluation

Buildings are revalued with sufficient regularity to ensure that the carrying amount does not differ materially from fair value. Refer to note 24(b)(ii) for the methodology used in the determination of fair value. Any revaluation increase arising on the revaluation of buildings is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in net surplus or deficit, in which case the increase is credited to net surplus or deficit to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of land or buildings is charged as an expense to net surplus or deficit to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset.

If buildings were stated on the historical cost basis, the amounts would be as follows:

| | GROUP 2018 | GROUP 2017 |
|---------------------------|---------------|---------------|
| | \$m | \$m |
| Cost | 135.9 | 133.2 |
| Accumulated depreciation | (44.5) | (41.0) |
| Net carrying value | 91.4 | 92.2 |

(iii) Derecognition

Realised gains and losses arising from the derecognition of property, plant and equipment are recognised in net surplus or deficit in the period in which the transaction occurs. The gain or loss is calculated as the difference between the carrying amount of the asset and the net disposal proceeds received (if any). Any credit balance attributable to the disposed asset in the asset revaluation reserve is transferred to retained earnings.

(iv) Depreciation

Depreciation is charged on a straight line basis at rates that will allocate the cost or valuation of the asset over its expected useful life to its estimated residual value. Leasehold improvements are depreciated over the period of the lease or estimated useful life, whichever is the shorter. In determining an asset's useful life, consideration is given to its expected usage, its expected wear and tear, technical or commercial obsolescence, and legal or similar limits on its use.

The average depreciable lives for major categories of property, plant and equipment are as follows:

| Category | Useful life |
|--------------------------------|----------------|
| Railway Infrastructure | |
| Tunnels and bridges | 75 - 200 years |
| Track and ballast | 40 – 50 years |
| Overhead traction | 20 – 80 years |
| Signals and communications | 15 – 50 years |
| Buildings | 35 – 80 years |
| Rolling Stock and Ships | |
| Wagons and carriages | 5 - 30 years |
| Locomotives | 5 - 25 years |
| Ships | 20 years |
| Containers | 10 years |
| Plant and Equipment | |
| Plant and equipment | 5 – 35 years |
| Motor vehicles | 5 – 12 years |
| Furniture and fittings | 5 – 12 years |
| Office equipment | 3 – 5 years |

Land is not depreciated.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

8. NON-FINANCIAL ASSETS (continued)**(a) PROPERTY, PLANT AND EQUIPMENT (continued)***Estimation of useful lives of assets*

The Group reviews the useful lives and residual values of its property, plant and equipment annually. Assessing the appropriateness of useful life and residual value estimates of property, plant and equipment requires the Group to consider a number of factors such as the physical condition of the asset, expected period of use and expected disposal proceeds from the future sale of the asset.

(v) Finance leases

Leases in which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Included within plant and equipment are assets acquired by way of a finance lease with a net book value of \$12.9m (2017: \$14.0m).

Assets held under finance leases are stated at cost less accumulated depreciation and impairment. Finance charges are recognised as finance expenses in net surplus or deficit. Further details of the lease term are provided in note 20(a).

(vi) Property, plant and equipment pledged to secure borrowing

Details of property, plant and equipment pledged as security is provided in note 12(b)(i).

(b) INTANGIBLE ASSETS

| | Note | GROUP 2018 | GROUP 2017 |
|---------------------------|------|---------------|---------------|
| | | \$m | \$m |
| Opening balance | | 0.4 | 0.8 |
| Additions | | 6.7 | 4.8 |
| Amortisation | | (0.3) | (0.5) |
| Impairment | 8(c) | (6.5) | (4.7) |
| Balance at 30 June | | 0.3 | 0.4 |

Intangible assets comprise software applications which have a finite useful life and are recorded at cost less accumulated amortisation and impairment losses. Intangible assets with a finite useful life are amortised on a straight-line basis over their estimated useful lives of 3 to 5 years.

(c) IMPAIRMENT OF NON-FINANCIAL ASSETS**Reconciliation of Impairment Movements to Net Surplus or Deficit**

| | GROUP 2018 | GROUP 2017 |
|--|---------------|---------------|
| | \$m | \$m |
| Impairment of Cash Generating Units (below) | 27.0 | 215.7 |
| Impairment of earthquake damaged assets | 26 | 77.5 |
| Impairment of asset transferred to asset held for sale | 15 | 2.6 |
| Impairment in net surplus or deficit | 248.6 | 295.8 |

(i) Impairment of Cash Generating Units ("CGUs")

The Group has two CGUs and management consider that the assets within them form the individual CGU:

- Rail CGU – non-leased buildings, railway infrastructure, rolling stock, plant and equipment and intangible assets; and
- Interislander - ships and related plant and equipment and intangible assets that relate to the Interislander business unit.

The two CGUs are assessed for impairment at each reporting date.

The value in use for each CGU is the present value of expected future cash flows. The recoverable amount of a CGU is the higher of its value in use and its fair value less costs to sell. If the carrying amount exceeds the recoverable amount the asset is impaired and the carrying amount is written down to the recoverable amount. For revalued assets the impairment is treated as a revaluation decrease (see note 8(a)(ii) above). For assets not carried at a revalued amount, the total impairment is recognised in net surplus or deficit.

As at 30 June 2018 the Interislander CGU recoverable amount exceeds the carrying amount and no impairment is recognised. As at 30 June 2018 the recoverable amount of the Rail CGU does not exceed the carrying amount and impairment has been recognised. We have determined the recoverable amount of the Rail CGU to be fair value less costs to sell. The impairment is allocated across each asset class within the CGU, including intangible assets.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

8. NON-FINANCIAL ASSETS (continued)**(c) IMPAIRMENT OF NON-FINANCIAL ASSETS (continued)**

- In determining the fair value less cost to sell of the railway infrastructure assets and rolling stock within the Rail CGU, the Group adopted a market approach assuming an orderly liquidation of the assets to arrive at a net realisable or scrap value.
- The higher of the scrap value or the net realisable value is adopted to determine the individual asset's fair value less cost to sell.
- Market values such as steel prices and scrap metal rates are taken into account in determining the asset's fair value.
- For assets where scrap value is lower than the cost of removal the assigned fair value less cost to sell was set to nil.
- Where assets have a readily determinable market value they have been impaired to this value. Where a market value is not able to be determined the assets have been impaired to their share of the calculated value in use for the CGU.
- Market values have been provided by an independent valuer for buildings based on the most recent valuation.
- Market values for all railway infrastructure and rolling stock were calculated with reference to external index data as at 30 June 2018.

The following impairments and revaluation movements have been recorded in relation to the Rail CGU:

| GROUP 2018 | 2018 Carrying amount before revaluation and impairment | Impairment recognised in net surplus or deficit | Movement recognised in Asset Revaluation Reserve | Carrying amount after impairment |
|-------------------------------------|--|---|--|----------------------------------|
| | \$m | \$m | \$m | \$m |
| Rail CGU | | | | |
| Buildings | 41.2 | (0.3) | - | 40.9 |
| Railway infrastructure | 243.2 | (37.2) | - | 206.0 |
| Rolling stock | 254.2 | 12.4 | - | 266.6 |
| Plant and equipment | 124.7 | (0.5) | - | 124.2 |
| Assets under construction | 306.3 | (216.5) | - | 89.8 |
| Total property, plant and equipment | 969.6 | (242.1) | - | 727.5 |
| Intangible assets | 6.5 | (6.5) | - | - |
| Total Rail CGU | 976.1 | (248.6) | - | 727.5 |

| GROUP 2017 | 2017 Carrying amount before revaluation and impairment | Impairment recognised in net surplus or deficit | Movement recognised in Asset Revaluation Reserve | Carrying amount after impairment |
|-------------------------------------|--|---|--|----------------------------------|
| | \$m | \$m | \$m | \$m |
| Rail CGU | | | | |
| Buildings | 51.4 | (10.6) | (0.3) | 40.5 |
| Railway infrastructure | 211.3 | (106.2) | - | 105.1 |
| Rolling stock | 259.5 | (23.0) | - | 236.5 |
| Plant and equipment | 116.7 | - | - | 116.7 |
| Assets under construction | 217.8 | (148.7) | - | 69.1 |
| Total property, plant and equipment | 856.7 | (288.5) | (0.3) | 567.9 |
| Intangible assets | 4.7 | (4.7) | - | - |
| Total Rail CGU | 861.4 | (293.2) | (0.3) | 567.9 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

9. CASH AND CASH EQUIVALENTS

| | GROUP 2018 | GROUP 2017 |
|------------------------------------|-------------|-------------|
| | \$m | \$m |
| Current accounts and call deposits | 87.0 | 83.4 |
| | 87.0 | 83.4 |

Cash and cash equivalents comprises cash on hand, call deposits and other investments with an initial term of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

10. TRADE AND OTHER RECEIVABLES

| | GROUP 2018 | GROUP 2017 |
|--------------------------------|-------------|--------------|
| | \$m | \$m |
| Trade receivables | 56.4 | 52.4 |
| GST receivable | 2.3 | 4.6 |
| Accrued and other receivables: | | |
| Prepayments | 12.4 | 9.2 |
| Related party receivables | 3.5 | 36.3 |
| Other | 17.2 | 37.7 |
| Gross receivables | 91.8 | 140.2 |
| Less provision for impairment | (0.4) | (1.8) |
| | 91.4 | 138.4 |
| Current assets | 91.0 | 138.0 |
| Non-current assets | 0.4 | 0.4 |
| | 91.4 | 138.4 |

Receivables (excluding prepayments) are financial assets classified as loans and receivables. Short-term receivables are recorded at their face value, less any provision for impairment.

Impairment

Receivables are assessed for indicators of impairment at each balance date. Receivables are impaired where there is objective evidence that, as a result of one or more events that have occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial asset have been impacted. The amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the receivables is reduced through the use of a doubtful debt provision. When a trade receivable is uncollectible, it is written off against the doubtful debt provision. Subsequent recoveries of amounts previously written off are credited to net surplus or deficit. Changes in the carrying amount of the doubtful debt provision are recognised in net surplus or deficit.

All overdue receivables have been assessed for impairment at balance date and appropriate provisions applied, as detailed below:

| | 2018 | | | 2017 | | |
|-----------------------|-------------|--------------|-------------|-------------|--------------|-------------|
| | Gross | Impairment | Net | Gross | Impairment | Net |
| | \$m | \$m | \$m | \$m | \$m | \$m |
| Not past due | 42.3 | - | 42.3 | 35.0 | - | 35.0 |
| Past due 1 – 30 days | 7.4 | - | 7.4 | 8.7 | - | 8.7 |
| Past due 31 – 60 days | 1.0 | - | 1.0 | 2.4 | - | 2.4 |
| Past due 61 - 90 days | 1.3 | - | 1.3 | 1.5 | (0.1) | 1.4 |
| Past due > 91 days | 4.4 | (0.4) | 4.0 | 4.8 | (1.7) | 3.1 |
| Total | 56.4 | (0.4) | 56.0 | 52.4 | (1.8) | 50.6 |

The average credit period on sales of goods and services is 32.1 days (2017: 30 days).

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

11. INVENTORIES

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Operational Activities | | |
| Fuel | 2.0 | 1.6 |
| Inventory held to maintain rail network | 37.8 | 35.0 |
| Inventory held to maintain rolling stock | 34.0 | 31.6 |
| Inventory held to maintain ships | 8.1 | 6.2 |
| Inventory held for resale | 0.6 | 0.2 |
| Contracting Activities – work in progress | 1.0 | 1.5 |
| Gross inventory | 83.5 | 76.1 |
| Less provision for stock obsolescence | (11.9) | (11.1) |
| Net inventory | 71.6 | 65.0 |

Inventory is recorded at the lower of cost and net realisable value. Costs comprise direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventory to its present condition and location. Cost is calculated using the weighted average method.

Write-downs or reversals of write-downs of inventories are recognised in operating expenses in net surplus or deficit, in the period the loss or reversal occurs. During the year, the Group has recognised write-downs in inventory of \$0.2m (2017: write-down of \$0.1m).

12. FINANCIAL ASSETS AND LIABILITIES

| | GROUP 2018 | | | GROUP 2017 | | |
|------------------------------------|--------------|-------------|--------------|--------------|--------------|--------------|
| | Current | Non-current | Total | Current | Non-current | Total |
| | \$m | \$m | \$m | \$m | \$m | \$m |
| Financial assets | | | | | | |
| Commodity forward contracts | 3.2 | 0.4 | 3.6 | 0.1 | 0.1 | 0.2 |
| Foreign currency forward contracts | 5.2 | 0.6 | 5.8 | 0.2 | 0.1 | 0.3 |
| Total financial assets | 8.4 | 1.0 | 9.4 | 0.3 | 0.2 | 0.5 |
| Financial liabilities | | | | | | |
| Commodity forward contracts | 1.5 | 0.1 | 1.6 | 0.1 | 0.1 | 0.2 |
| Loans | 174.2 | 74.8 | 249.0 | 176.0 | 85.5 | 261.5 |
| Finance leases | 1.2 | 6.3 | 7.5 | 1.5 | 7.5 | 9.0 |
| Foreign currency forward contracts | 0.7 | 1.0 | 1.7 | 2.8 | 1.9 | 4.7 |
| Interest rate swaps | 3.7 | 4.4 | 8.1 | - | 11.2 | 11.2 |
| Total financial liabilities | 181.3 | 86.6 | 267.9 | 180.4 | 106.2 | 286.6 |

(a) Financial assets

The Group's financial assets designated at fair value are those derivative financial instruments within predetermined policies and limits in order to manage exposure to fluctuations in foreign exchange, commodity and interest rate risks. The relevant accounting policy for these types of financial assets is set out under 'Derivative financial instruments' in note 24(b)(i). Financial assets are classified as non-current when the maturity of the hedged item exceeds 12 months.

(b) Financial liabilities

Financial liabilities are designated at amortised cost or at fair value through net surplus or deficit unless these are designated as hedged items and therefore hedge accounted for. Financial liabilities are classified as non-current when the maturity exceeds 12 months.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

12. FINANCIAL ASSETS AND LIABILITIES (continued)**(i) Amortised cost**

Amortised cost is the amount at which the financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount and the maturity amount.

Interest-bearing liabilities

Interest-bearing liabilities comprise of loans and finance leases. They are initially measured at fair value, plus directly attributable transaction costs. Interest-bearing liabilities are subsequently measured at amortised cost using the effective interest method.

Unsecured loans

The notional principal amounts of the outstanding loans for the Group were \$174.2m (2017: \$174.2m).

Secured loans

Loans from Bank of New Zealand are secured against MV Aratere and hoists. A loan from Westpac Banking Corporation is secured against MV Kaitaki. There are no restrictions on title. The amount outstanding for all secured loans as at the reporting date is \$74.8m (2017: \$87.3m).

The average term to maturity and weighted average interest rates for external unsecured and secured loans and finance leases are shown in the table below:

| | Unit | GROUP 2018 | GROUP 2017 |
|--------------------------|-------|---------------|---------------|
| Notional principal | \$m | 256.5 | 270.5 |
| Average interest rate | % | 2.78 | 4.12 |
| Average term to maturity | years | 1.23 | 1.55 |

Committed standby facility

The Group has a committed standby facility with Bank of New Zealand for \$15.0m as at 30 June 2018 (2017: \$15.0m) with an expiry date of 1 July 2019. As at 30 June 2018, the facility is undrawn.

Letter of credit facilities

The Group had no letter of credit facilities at 30 June 2018 (2017: nil).

Standby letter of credit

The Group had no standby letters of credit at 30 June 2018 (2017: nil).

(c) Changes in liabilities arising from financing activities

| | GROUP 2017 | Cash Flows | Non-cash changes | | GROUP 2018 |
|--|---------------|---------------|---------------------------|----------|---------------|
| | \$m | \$m | Changes in Fair values | Others | \$m |
| Loans | 261.5 | (12.5) | - | - | 249.0 |
| Finance leases | 9.0 | (1.5) | - | - | 7.5 |
| Total liabilities from financing activities | 270.5 | 14.0 | - | - | 256.5 |

13. INVESTMENT PROPERTY

| | GROUP 2018 | GROUP 2017 |
|-------------------------------|---------------|---------------|
| | \$m | \$m |
| Opening balance | 76.5 | 68.7 |
| Additions | 0.5 | 1.7 |
| Disposals | (0.1) | - |
| Transfers | 1.9 | - |
| Fair value gains on valuation | 4.0 | 6.1 |
| Balance at 30 June | 82.8 | 76.5 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

13. INVESTMENT PROPERTY (continued)

Investment properties are measured initially at cost, including transaction costs. Investment properties include land and buildings held to earn rental income or capital gains through the future resale of the property.

Subsequent to initial recognition, investment properties are measured at fair value. Gains or losses from changes in the fair values of investment properties are recognised in net surplus or deficit in the year in which they arise. Valuation of leased buildings is undertaken with sufficient regularity to ensure carrying value does not materially differ from fair value. See note 24(b)(ii) for the methodology used in the determination of fair value.

Investment properties are derecognised 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 net surplus or deficit in the year of retirement or disposal.

Included within investment property is land (excluding the rail corridor) acquired as part of the joint arrangement with Northland Regional Council. The total carrying amount of investment properties relating to this joint arrangement is \$3.0m (2017: \$2.8m). See note 14 for further information on this joint arrangement.

The total rental income generated from investment properties for the year ended 30 June 2018 was \$5.9m (2017: \$5.9m). The direct operating expenses (including maintenance) arising from the use of investment properties during the year was \$1.3m (2017: \$1.0m).

14. JOINT ARRANGEMENTS WITH NORTHLAND REGIONAL COUNCIL

In January 2009 the New Zealand Railways Corporation ("NZRC") entered into an agreement with Northland Regional Council, which was vested from NZRC to KHL on 31 December 2012, to create a joint arrangement in order to advance the proposed Oakleigh to Marsden Point rail link. This arrangement is considered as a joint operation under NZ IFRS 11 Joint Arrangements. As a party to a joint operation, the Group has recognised the related assets and liabilities in relation to its interest in the proposed Oakleigh to Marsden Point rail link.

The Council entered into voluntary negotiations with landowners who owned land along the existing corridor and to date have acquired nine properties with a total acquisition cost of \$11.5m (the Group's share is \$5.8m).

At 30 June 2018 the Group has a liability of \$5.6m (2017: \$5.5m) to the Council for its share of the cost of land purchased by the Council as well as other Council expenditure relating to the joint operation. This is included in Trade and Other Liabilities in note 16.

15. INVESTMENT IN JOINT VENTURE

In November 2017, the Group sold its 25% interest in MetroBox Limited, a joint venture involved in container repair and storage operating from a facility at Southdown, Auckland.

The Group classified its investment in Metrobox Limited as held for sale at \$1.9m as at 30 June 2017 and recognised an impairment charge of \$2.6m in the Statement of Comprehensive Income. The Group's share of profit for the year was \$nil (2017: \$0.4m).

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

16. TRADE AND OTHER LIABILITIES

| | Note | GROUP 2018 | GROUP 2017 |
|-----------------------------|------|---------------|---------------|
| | | \$m | \$m |
| Trade payables | | 52.3 | 50.4 |
| Unearned revenue | | 12.7 | 12.6 |
| Accrued interest | | 1.9 | 1.2 |
| Payable to joint operator | 14 | 5.6 | 5.5 |
| Other payables and accruals | | 31.3 | 62.8 |
| Total payables | | 103.8 | 132.5 |
| Current liabilities | | 103.8 | 132.5 |
| Non-current liabilities | | - | - |
| | | 103.8 | 132.5 |

Payables are recognised when the Group becomes obliged to make future payments resulting from the purchase of goods and services. Payables are initially measured at fair value and subsequently measured at amortised cost using the effective interest rate method.

Trade payables are settled on normal commercial terms and the carrying value approximates fair value. No interest is incurred on trade payables unless the amounts fall overdue. Interest is charged at the discretion of the vendor.

Goods and services tax (GST)

All items in the financial statements are presented exclusive of GST, except for receivables and payables, which are presented on a GST inclusive basis. Where GST is not recoverable as an input tax it is recognised as part of the related asset or expense.

The net amount of GST payable to Inland Revenue ('IR') is included as part of trade and other liabilities. The amount of GST receivable from IR is included as part of Trade and Other Receivables (note 10).

17. EMPLOYEE ENTITLEMENTS

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Current portion | | |
| Short-term employee benefits | 12.2 | 10.9 |
| Annual leave entitlement accruals | 40.6 | 39.1 |
| Retirement and long service leave liability | 5.7 | 5.1 |
| Total current portion | 58.5 | 55.1 |
| Non-Current portion | | |
| Retirement and long service leave | 39.3 | 36.9 |
| Total non-current portion | 39.3 | 36.9 |
| Total employee entitlements | 97.8 | 92.0 |

Provisions are made for benefits accruing to employees in respect of annual leave, retiring leave (including involuntary retirement as medically unfit) and long service leave when it is probable that settlement will be required and they are capable of being measured reliably. Employee entitlements are accounted for based on NZ IAS 19 *Employee Benefits*.

Provisions made in respect of employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Provisions made in respect of employee benefits which are not expected to be settled within twelve months are measured on an actuarial basis by independent actuaries Melville Jessup Weaver ("MJW") at the present value of the estimated future cash outflows to be made by the Group in respect of services provided by employees up to the reporting date.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

17. EMPLOYEE ENTITLEMENTS (continued)

The present value of the retirement and long service leave obligations depend on a number of factors. Two key assumptions used in calculating this liability include the discount rate and the salary inflation factor. The assumptions used by the actuaries in arriving at the retirement and long service leave liabilities were a salary increase rate from 2.2% to 2.5% per annum (2017: from 2.17% to 2.5% per annum) and a term specific risk-free discount rate of between 1.78% and 4.75% per annum (2017: between 1.97% and 4.75% per annum). The discount rate is derived from the yields on Government bonds as at the respective reporting dates, which have terms to maturity that match, as closely as possible, the estimated future cash outflows. The salary inflation factor has been determined after considering historical salary inflation patterns.

Contributions to superannuation plans

Certain employees are members of defined contribution schemes and the Group contributes to those schemes. The contributions are recognised as labour and related costs in net surplus or deficit when they are due.

18. PROVISIONS

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and the amount can be reliably estimated.

| GROUP 2018 | ACC AEP | Leased vessel costs | Reorganisation costs | Other provisions | Total |
|---|------------|---------------------|----------------------|------------------|-------------|
| | \$m | \$m | \$m | \$m | \$m |
| Balance at 1 July 2017 | 3.7 | 6.0 | 0.2 | 1.1 | 11.0 |
| Provisions made during the year | - | - | 0.9 | 1.2 | 2.1 |
| Provisions utilised or released during the year | (0.2) | - | - | (0.9) | (1.1) |
| Balance at 30 June 2018 | 3.5 | 6.0 | 1.1 | 1.4 | 12.0 |
| Current | 3.5 | - | 1.1 | 1.4 | 6.0 |
| Non-current | - | 6.0 | - | - | 6.0 |
| | 3.5 | 6.0 | 1.1 | 1.4 | 12.0 |

ACC Accredited Employer Programme

KHL and its subsidiary KiwiRail Limited ("KRL") belong to the ACC Accredited Employer Programme ("ACC AEP") whereby each company accepts the management and financial responsibility for employee work-related accidents.

The liability for the ACC AEP is measured annually by MJW, an external independent actuarial valuer, using actuarial techniques at the present value of expected future payments to be made in respect of the employee injuries and claims up to the reporting date. Any changes in assumptions will not have a material impact on the financial statements.

Leased vessel cost

The Group has charter agreements in place for the MV Kaiarahi. Redelivery costs are accrued in accordance with NZ IAS 37.

19. SALE AND PURCHASE OF LAND

On 31 December 2012 there was a restructure of the Crown's investment in rail operations. In accordance with the KiwiRail Holdings Vesting Order 2012 which took effect from 31 December 2012, the KiwiRail business was transferred from the NZRC into KHL. All land previously held by KiwiRail was retained by NZRC.

From time to time NZRC may sell parcels of railway land. Under the Group's lease agreement with NZRC entered into on 31 December 2012, the Group may identify railway land that should be sold and request NZRC to sell it or surrender it from the lease. The sale proceeds are provided to the Group to support its business as the State Owned Enterprise responsible for the financial performance of the Crown's investment in rail operations.

Similarly, the Group can identify new parcels of land that are required for rail purposes. The Group will fund the acquisition of the land and can transfer it to NZRC to be included within the lease.

The sale and purchase of land are treated as common control transactions as the Crown is their ultimate parent. The sale of NZRC's land is regarded as an increase in equity of the Crown to the Group whilst the Group's acquisition of land for NZRC is treated as a reduction from the Crown's equity to the Group.

The total net proceeds from land sold/land swaps during the year was \$4.8m (2017: \$15.0m). The total net land acquisitions during the year was \$1.8m (2017: nil). They were treated as transactions with owners in the Statement of Movements in Equity.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

20. LEASES AND COMMITMENTS**(a) Finance lease**

The Group has a lease agreement with Westpac Banking Corporation. Refer to note 8(a)(v) for details. The lease terms range between four to ten years and there are no terms of renewal, escalation clauses or purchase options contained within the agreement. The approved limit of this facility is \$13.1m (2017: \$13.1m).

At 30 June 2018 the Group had the following liability under this lease agreement:

| | GROUP 2018 | GROUP 2017 |
|---|------------|------------|
| | \$m | \$m |
| Total minimum lease payments due | | |
| Not later than one year | 1.5 | 1.8 |
| Later than one year but not later than five years | 4.5 | 5.0 |
| Later than five years | 2.9 | 3.9 |
| Total minimum lease payments | 8.9 | 10.7 |
| Future lease finance charges | (1.4) | (1.7) |
| Present value of minimum lease payments | 7.5 | 9.0 |
| Represented by: | | |
| Current | 1.2 | 1.5 |
| Non-current | 6.3 | 7.5 |
| Total finance leases | 7.5 | 9.0 |

(b) Operating lease commitments as lessee

NZRC has, along with the Crown, granted a long-term lease to KRL for nominal consideration, under which KRL can enjoy the commercial benefit of the rail corridor land. KRL has primary responsibility for administering the land. Under the lease it can undertake many activities in relation to the land without requiring the consent or involvement of NZRC. It is also able to sub-lease railway land for periods of time within the term of the lease. The total minimum future sublease payments expected to be received under non-cancellable subleases at balance date is \$nil.

Operating lease payments are recognised as an operating expense in net surplus or deficit on a straight-line basis over the lease term. Operating lease incentives are recognised as a liability when received and subsequently reduced by allocating lease payments between rental expense and reduction of the liability.

The Group leases vessels and plant and equipment in the normal course of its business. Included in these lease commitments is the Group's charter for the MV Kaiarahi. The lease for the MV Kaiarahi is non-cancellable for five years expiring on 17 July 2020.

Motor vehicle leases generally have a non-cancellable term of three years.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

20. LEASES AND COMMITMENTS (continued)**(b) Operating lease commitments as lessee (continued)**

The future aggregate minimum lease payments payable under non-cancellable operating leases are as follows:

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Total minimum lease payments due: | | |
| Not later than one year | 25.3 | 19.9 |
| Later than one year but not later than five years | 52.4 | 44.5 |
| Later than five years | 38.7 | 7.3 |
| | 116.4 | 71.7 |

(c) Operating lease commitments as lessor

The Group has certain non-cancellable property leases. The property lease portfolio is made up of a large number of leases with varying terms.

The future aggregate minimum lease payments to be collected under non-cancellable operating leases are as follows:

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Total minimum lease payments receivable: | | |
| Not later than one year | 35.3 | 30.9 |
| Later than one year but not later than five years | 86.3 | 83.3 |
| Later than five years | 93.1 | 89.2 |
| | 214.7 | 203.4 |

For the year ended 30 June 2018, \$40.3m was recognised as revenue in net surplus or deficit (2017: \$36.9m).

(d) Capital and other commitments

The Group has capital commitments for network upgrades, infrastructure renewal materials, manufacturing of new rolling stock, refurbishment costs relating to rolling stock and purchases of plant and equipment.

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Capital expenditure commitments: | | |
| Not later than one year | 89.2 | 87.6 |
| Later than one year but not later than five years | 21.4 | 22.7 |
| | 110.6 | 110.3 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

21. RECONCILIATION OF NET (DEFICIT) TO NET CASH FLOWS FROM OPERATING ACTIVITIES

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| | \$m | \$m |
| Net deficit after taxation | (235.9) | (197.3) |
| Add/(deduct) items classified as investing or financing activities | | |
| Gain on sale of assets | (0.9) | (0.4) |
| Fair value movement in derivatives | (13.6) | (3.7) |
| Capital grant receipts | (33.7) | (27.6) |
| Insurance proceeds | (29.9) | (72.1) |
| Share in profit of joint venture | - | (0.4) |
| | (314.0) | (301.5) |
| Add/(deduct) non-cash items | | |
| Depreciation and amortisation expense | 86.2 | 77.1 |
| Movements in provisions | 3.5 | (2.5) |
| Impairment of non-financial assets | 248.6 | 295.8 |
| Movement in fair value of investment properties | (4.0) | (6.1) |
| | 20.3 | 62.8 |
| Add/(deduct) movements in working capital | | |
| (Increase)/decrease in trade receivables | (4.0) | 4.8 |
| Decrease/(increase) in other receivables | 20.1 | (31.2) |
| (Increase) in inventories | (6.6) | (1.9) |
| Increase in trade payables | 1.9 | 14.4 |
| (Decrease) in other payables | (13.0) | (3.0) |
| Net cash flows from operating activities | 18.7 | 45.9 |

22. RELATED PARTY TRANSACTIONS

The Group enters into transactions with related parties all of which are carried out on normal commercial terms. Transactions that occur within a normal supplier or client / recipient relationship, on terms and conditions no more or less favourable than those which it is reasonable to expect the Parent or its subsidiaries and associates would have adopted if dealing with that entity at arm's length in the same circumstance, are not disclosed.

Significant transactions with Government-related entities

The Group has been provided with equity from the Crown and capital grant funding from Government entities. Equity funding of \$430.0m (2017: \$190.2m) has been received together with capital grant funding of \$15.0m (2017:\$6.2m).

The Group paid \$195.8m (2017: \$34.7m) to New Zealand Transport Agency for the Main North Line reinstatement.

The Group receives operating revenue for providing rail freight services to Solid Energy New Zealand, New Zealand Transport Agency and Genesis Energy.

The Group also purchases goods and services from entities controlled, significantly influenced, or jointly controlled by the Crown.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

22. RELATED PARTY TRANSACTIONS (Continued)

As these transactions are material in nature they have been disclosed in thousands rather than expressed in millions.

| | GROUP 2018 | GROUP 2017 |
|-------------------------------------|-----------------------|-----------------------|
| REVENUE | \$000 | \$000 |
| Solid Energy | 9,133 | 27,742 |
| New Zealand Transport Agency | 4,352 | 8,451 |
| New Zealand Post | 3,642 | 3,074 |
| Genesis Energy | 25 | 989 |
| | 17,152 | 40,256 |
| | | |
| | GROUP 2018 | GROUP 2017 |
| EXPENSES | \$000 | \$000 |
| Meridian Energy | 11,852 | 12,462 |
| Transpower | 3,684 | 3,415 |
| Air New Zealand | 3,211 | 2,375 |
| New Zealand Transport Agency | 852 | 707 |
| Kordia | 683 | 1,563 |
| New Zealand Fire Service Commission | 640 | - |
| New Zealand Post | 240 | 368 |
| Other | 725 | 382 |
| | 21,887 | 21,272 |

Collectively but not individually significant transactions with Government-related entities

The Group is required to pay various taxes and levies (such as GST, FBT, PAYE, ACC levies and Customs duties) to the Crown and entities related to the Crown. The payment of these taxes and levies is based on the standard terms and conditions that apply to all tax and levy payers.

Transactions with key management personnel

Key management personnel is defined as Directors, the Chief Executive and all executive level direct reports of the Chief Executive. Key management personnel of the Group may be directors or officers of other companies or organisations with whom the Group may transact. Such transactions are all carried out independently on normal commercial terms.

The compensation of the key management personnel of the Group was as follows:

| | GROUP 2018 | GROUP 2017 |
|--|---------------|---------------|
| | \$000 | \$000 |
| Key management personnel compensation | | |
| Short-term employee benefits | 5,898 | 5,212 |
| Termination benefits | 214 | - |
| Total key management personnel compensation | 6,112 | 5,212 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

22. RELATED PARTY TRANSACTIONS (continued)

The following Directors earned fees during the period:

| | 2018 | 2017 |
|----------------------|--------------|--------------|
| KHL Directors | \$000 | \$000 |
| Trevor Janes | 87 | 61 |
| Paula Rebstock | 48 | 53 |
| Mike Pohio | 47 | 42 |
| John Leuchars | 43 | 42 |
| Guy Royal | 43 | 42 |
| Paul Harper | 43 | 42 |
| John Dennehy | 43 | 7 |
| Bob Major | 43 | 7 |
| Susan McCormack | 43 | 5 |
| John Spencer | - | 27 |
| Kevin Thompson | - | 23 |
| | 440 | 351 |

Trevor Janes retired from the Board effective 30 June 2018. Paula Rebstock completed her term on 30 April 2018.

23. SHARE CAPITAL

At 30 June 2018, the Group had issued 1,233,800,000 ordinary shares with no par value (2017: 833,800,000), each fully paid. The following rights attach to the ordinary shares issued by the Group:

- the right to one vote on a poll at a meeting of the Group on any resolution, including any resolution to appoint or remove a Director or auditor, alter the Group's constitution, approve a major transaction, approve an amalgamation, and put the Group into liquidation;
- the right to an equal share of dividends approved by the Board; and
- the right to an equal share in the distribution of the surplus assets of the Group.

| Reconciliation of number of shares | GROUP 2018 | GROUP 2017 |
|------------------------------------|----------------|---------------|
| | (m) | (m) |
| Opening balance | 833.8 | 613.6 |
| Shares issued | 400.0 | 220.2 |
| Balance at 30 June | 1,233.8 | 833.8 |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

24. FAIR VALUE**(a) Classification of Financial Instruments**

The classification of each category of financial instruments is set out below:

| | GROUP 2018 | GROUP 2017 |
|---|---------------|---------------|
| FINANCIAL ASSETS | \$m | \$m |
| Loans and receivables | | |
| Cash and cash equivalents | 87.0 | 83.4 |
| Trade and other receivables (excluding prepayments) | 77.1 | 124.6 |
| | 164.1 | 208.0 |
| Fair value through net surplus or deficit | | |
| Derivative financial assets | 9.4 | 0.5 |
| FINANCIAL LIABILITIES | | |
| Amortised cost | | |
| Trade and other liabilities | 91.1 | 119.9 |
| Interest-bearing liabilities | 256.5 | 270.5 |
| | 347.6 | 390.4 |
| Fair value through net surplus or deficit | | |
| Derivative financial liabilities | 11.4 | 16.1 |

The carrying amounts of the financial assets and financial liabilities approximate their fair value.

(b) Fair Value Hierarchy

Fair values are allocated to a fair value hierarchy based on the following:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2- Inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – Inputs for the asset or liability that are not based on observable market data.

The Group does not have any Level 1 and/or Level 3 financial instruments (2017: nil).

For financial assets not quoted in active markets, the Group uses valuation techniques such as present value techniques, comparison to similar instruments for which market observable prices exist and other relevant models used by market participants.

i. Derivative financial instruments

The fair value of the financial assets and financial liabilities as well as the methods used to estimate the fair value is summarised below:

| | Level 2 | |
|--|---------------|---------------|
| Financial instruments (Net Liability)/Net Asset | GROUP 2018 | GROUP 2017 |
| | \$m | \$m |
| Commodity forward contracts | 2.0 | - |
| Foreign currency forward contracts | 4.1 | (4.4) |
| Interest rate swaps | (8.1) | (11.2) |
| | (2.0) | (15.6) |

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

24. FAIR VALUE (continued)**(b) Fair Value Hierarchy (continued)**

Derivative financial instruments are initially recognised at fair value on the date a derivative contract is entered into (the trade date). Any transaction costs are expensed immediately. The derivative financial instruments are subsequently re-measured to fair value. Derivative financial instruments are designated at fair value through net surplus or deficit and, if they are in a hedge relationship, at fair value through other comprehensive income. The Group uses discounted cash flow techniques. In estimating the fair value of an asset or liability, the Group uses market-observable data to the extent it is available. Where observable inputs are not available, the Group engages banking counterparties to support the establishment of appropriate valuation inputs. A Credit Value Adjustment is made to the underlying interest rate swap curve to adjust for counterparty credit risk.

ii. Non-financial assets

The fair value of the non-financial assets which are required to be reflected at fair value during the year was:

| | Level 2 | |
|----------------------|---------------|---------------|
| Non-financial assets | GROUP 2018 | GROUP 2017 |
| | \$m | \$m |
| Investment property | 82.8 | 76.5 |
| Buildings | 40.9 | 40.5 |
| | 123.7 | 117.0 |

NZ IFRS 13 requires that the fair value measurement of non-financial assets take into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

Highest and best use of a non-financial asset takes into account the use of the asset that is physically possible, legally permissible and financially feasible. It is determined from the perspective of market participants, even if the Group intends a different use.

The valuation techniques used in determining the fair value of non-financial assets are as follows:

- *Investment property*
Valuation of investment property is carried out with sufficient regularity to ensure the carrying value does not materially differ from fair value. The most recent valuation was carried out by an independent valuer who holds a recognised and relevant professional qualification.

Investment properties are valued accounting for market derived assumptions using comparable rental and sales evidence. When the fair value is determined, the independent valuer has utilised valuers located nationwide that are familiar with the local property market in which the property is situated. They have factored local inputs into the valuation such as rentals, capitalisation rates and land values. The market valuation methodology used for investment properties was the capitalisation of net income and direct comparison approaches. The capitalisation rates used in the valuation generally range from 5% to 15%.

- *Buildings*
Buildings are properties held to carry-out the Group's entity-specific operations. They are revalued with sufficient regularity to ensure the carrying value does not materially differ from fair value. The most recent valuation of buildings that form part of the rail CGU was carried out by an independent valuer who has recognised and relevant qualifications.

In carrying out the valuation, the valuers take into account the likely sale price of the property but also assumed that the highest and best use is the properties' current use. Valuations are undertaken in accordance with the standards issued by the New Zealand Property Institute, NZ IAS 16 Property, Plant and Equipment and NZ IFRS 13 with the following bases of valuation adopted:

- *Specialised buildings* which are those assets identified as having no readily available market and exist strictly to carry out KiwiRail's unique operations are valued using optimised depreciated replacement cost.
- *Non-specialised buildings* which could be sold with relative ease are valued at market value.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

24. FAIR VALUE (continued)**(b) Fair Value Hierarchy (continued)***Sensitivity analysis*

The following represents the financial impact of changes in fair value of non-financial assets:

| Non-financial assets | Increase in fair value by 5% | | Decrease in fair value by 5% | |
|-----------------------|------------------------------|------------|------------------------------|------------|
| | GROUP 2018 | GROUP 2017 | GROUP 2018 | GROUP 2017 |
| | \$m | \$m | \$m | \$m |
| Buildings | 0.9 | 0.5 | 0.5 | 0.6 |
| Investment properties | 3.9 | 3.7 | 3.9 | 3.7 |

25. FINANCIAL RISK MANAGEMENT POLICIES AND OBJECTIVES

The Group's principal financial instruments comprise cash and cash equivalents, receivables, interest-bearing liabilities, trade and other liabilities and derivatives.

The Group manages its exposure to key financial risks, including market risk, credit risk and liquidity risk in accordance with the Group's financial risk management policies. The objective of the policy is to support the delivery of the Group's financial targets whilst protecting future financial security.

(a) Market Risk

Market risk refers to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market price. Market risk comprises three types of risk; currency risk, interest rate risk and other price risk.

i. Foreign Exchange Risk or Currency Risk

Foreign exchange risk is the risk of cash flow volatility arising from the movement in foreign exchange rates to which the Group may be exposed. The Group is exposed to foreign exchange risk from normal operating activities and capital purchases.

The Group's Treasury Policy requires it to manage foreign currency risks arising from future transactions and liabilities by using Board approved foreign exchange hedging instruments.

The New Zealand Dollar notional principal amounts of outstanding forward foreign exchange contracts were \$122.9m (2017: \$152.7m).

The Group has hedged 100% (2017: 100%) of committed foreign currency capital purchases.

Foreign currency sensitivity on financial instruments

The following table demonstrates the sensitivity of the Group's equity and profit to a 10% strengthening or weakening in the value of the New Zealand Dollar.

| In NZ \$m | GROUP 2018 | | GROUP 2017 | |
|--|------------|--------|------------|--------|
| | Equity | Profit | Equity | Profit |
| Foreign currency sensitivity analysis | | | | |
| Impact of a 10% strengthening of the NZD | (10.5) | (10.5) | (13.2) | (13.2) |
| Impact of a 10% weakening of the NZD | 12.8 | 12.8 | 16.1 | 16.1 |

ii. Interest Rate Risk

Interest rate risk is the risk that cost of funds increase due to adverse movements in the interest rates that KiwiRail pays on its borrowings.

The Group borrows a mixture of fixed and floating rate debt in New Zealand Dollars. The Group hedges its re-pricing profile using interest rate swaps in accordance with its Treasury Policy in order to minimise and provide certainty over funding costs.

The notional principal amounts of the outstanding interest rate swaps for the Group were \$198.0m (2017: \$198.0m), with average term to maturity of 1.63 years (2017: 3.98 years) and weighted average fixed interest rate of 5.24% (2017: 5.24%). As at 30 June 2018, after taking into account the effect of the interest rate swaps, approximately 57.0% of the Group's borrowings are at a fixed rate of interest (2017: 54.0%).

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

25. FINANCIAL RISK MANAGEMENT POLICIES AND OBJECTIVES (continued)**(a) Market Risk (continued)****Interest sensitivity analysis**

A change in the interest rates would also have an impact on interest payments and receipts on the Group's floating rate debt and investment instruments (including the floating rate leg of any interest rate derivatives). The sensitivity to a 100 basis point (bp) movement in interest rates (based on financial assets and liabilities held at the reporting date) is as follows:

| In NZ \$m | GROUP 2018 Profit | GROUP 2017 Profit |
|---|-------------------|-------------------|
| Impact of a 100 bp interest rate increase | (0.6) | 1.1 |
| Impact of a 100 bp interest rate decrease | 0.5 | (1.3) |

iii. Price Risk

Price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market prices.

Fuel Price risk

The Group seeks to recover increased costs caused by increased fuel prices from its customers in the form of a fuel surcharge or fuel adjustment factor. Since the Group purchases its fuel at floating market rates, the Group is exposed to fuel price risk to the extent that it is unable to fully recover fuel price increases from its customers in the form of fuel surcharges. Accordingly, the Group's Treasury Policy allows Board approved hedging instruments to be entered into to manage this exposure.

The Group is party to a number of commodity forward contracts for Singapore intermediate fuel oil and gas oil. The total notional principal amount of outstanding commodity forward contracts is \$13.0m (2017: \$16.9m).

(b) Credit Risk

Credit risk is the potential loss from a transaction in the event of default by a counterparty during the term of the transaction or on settlement of the transaction. Financial instruments which potentially subject the Group to credit risk consist primarily of cash and cash equivalents, trade and other receivables and commodity and foreign currency forward contracts.

Whilst the Group may be subjected to losses up to the contract value of the instruments in the event of default by its counterparties, it does not expect such losses to occur. On-going credit evaluation is performed on the financial condition of accounts receivable and customers' compliance with credit terms.

The Group's Treasury Policy does not require collateral support for financial instruments subject to credit risk, although personal guarantees may be obtained in support of the financial performance of certain customers.

Concentration of credit risk

The Group does not have any significant credit risk exposure to a single counterparty or any group of counterparties having similar characteristics due to the large number of customers included in the Group's customer base. The credit risk on cash and cash equivalents and foreign exchange dealings is limited as the Group spreads its business amongst a number of Standard & Poors AA- rated counterparties.

Credit quality of assets not impaired or not yet due

The Group does not rate its individual debtors as it has a large number of customers. The incident of default on financial assets not impaired or not yet due is minimal. The Group has no other significant exposure to credit risk from financial assets not impaired or not yet due, nor has there been any renegotiation of terms on any of these assets.

Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure.

(c) Liquidity Risk

Liquidity risk is the risk that the Group will not be able to meet financial commitments as they fall due. The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and financial liabilities. The Group accesses funds via Crown appropriations for specified capital projects.

Exposure to liquidity risk

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period at the balance date to the contractual maturity date. Future interest payments on floating rate debt are based on the floating rate on the instrument at the balance date. The amounts disclosed are the contractual undiscounted cash flows.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

25. FINANCIAL RISK MANAGEMENT POLICIES AND OBJECTIVES (continued)**(c) Liquidity Risk (continued)**

| GROUP 2018 | Carrying amount | Contractual cash flows | Less than 1 year | 1 – 2 years | 2 – 5 years | More than 5 years |
|------------------------------------|-----------------|------------------------|------------------|-------------|-------------|-------------------|
| | \$m | \$m | \$m | \$m | \$m | \$m |
| Financial Liabilities | | | | | | |
| Trade and other payables | 91.1 | 91.1 | 91.1 | - | - | - |
| Net settled derivative liabilities | 11.4 | 11.2 | 6.0 | 2.5 | 2.7 | - |
| Finance leases | 7.5 | 8.9 | 1.5 | 1.5 | 3.0 | 2.9 |
| Borrowings | 249.0 | 259.6 | 179.1 | 23.5 | 57.0 | - |
| Total | 359.0 | 370.8 | 277.7 | 27.5 | 62.7 | 2.9 |

| GROUP 2017 | Carrying amount | Contractual cash flows | Less than 1 year | 1 – 2 years | 2 – 5 years | More than 5 years |
|------------------------------------|-----------------|------------------------|------------------|-------------|-------------|-------------------|
| | \$m | \$m | \$m | \$m | \$m | \$m |
| Financial Liabilities | | | | | | |
| Trade and other payables | 119.9 | 119.9 | 119.9 | - | - | - |
| Net settled derivative liabilities | 16.1 | 16.1 | 2.9 | 6.9 | 3.7 | 2.6 |
| Finance leases | 9.0 | 10.7 | 1.8 | 1.5 | 3.5 | 3.9 |
| Borrowings | 261.5 | 278.1 | 182.7 | 13.9 | 81.5 | - |
| Total | 406.5 | 424.8 | 307.3 | 22.3 | 88.7 | 6.5 |

(d) Derivative Financial Instruments and Hedging Activities

The Group uses derivative financial instruments within predetermined policies and limits in order to manage its exposure to fluctuations in foreign exchange, commodity and interest rate risks. The Group does not engage in speculative transactions or hold derivative financial instruments for trading purposes.

The risk management objectives and strategy for undertaking various hedge transactions is covered by the Group Treasury Policy. The Group documents, at the inception of the transaction, the hedging relationship between hedging financial instruments and the hedged items. The Group also documents its assessment, both at hedge inception and on an on-going basis, of whether the derivatives used in the hedging transaction are highly effective in offsetting changes in fair values or cash flows of hedged items.

Cash flow hedges

Changes in the fair value of derivative financial instruments designated as cash flow hedges are recognised in other comprehensive income and the cash flow hedge reserve within other comprehensive income to the extent that the hedges are deemed effective. To the extent that the hedges are ineffective for accounting, changes in fair value are recognised in net surplus or deficit in foreign exchange and commodity net gains and losses.

In any of the following circumstances, the Group shall discontinue hedge accounting:

- If a derivative financial instrument expires or is sold, terminated or exercised
- It no longer meets the criteria for hedge accounting
- The forecast transaction is no longer expected to occur
- The designation of the hedge relationship is revoked or changed

In cases where hedge accounting is discontinued, the cumulative, unrealised gain or loss recognised in the cash flow hedge reserve in other comprehensive income with respect to the derivative instrument is recognised immediately in net surplus or deficit.

Where the hedge relationship continues throughout its designated term, the amount in the cash flow hedge reserve is transferred to the carrying value of the asset when it is recognised.

KiwiRail Holdings Limited

Notes to the Financial Statements (continued)

For the financial year ended 30 June 2018

25. FINANCIAL RISK MANAGEMENT POLICIES AND OBJECTIVES (CONTINUED)**(e) Capital Risk Management**

The Group manages its capital structure to ensure it is able to continue as a going concern whilst maximising its investment into rail infrastructure and rolling stock assets. The State-Owned Enterprises Act 1986 requires the Board to manage the Group as a profitable and efficient organisation that is comparable to businesses that are not owned by the Crown.

The capital structure of the Group consists of borrowings, cash and cash equivalents and equity. Equity comprises a capital contribution from the Crown, retained earnings and reserves.

The Board reviews the capital structure of the Group as part of the Group's planning cycle and regular on-going reviews. As part of this review, the Board considers the level of capital invested in the business and the amounts retained to ensure it effectively achieves its objectives and purpose.

26. IMPACT OF KAIKOURA EARTHQUAKE

A 7.8 magnitude earthquake hit the Kaikoura region on 14 November 2016 followed by a number of aftershocks. This caused significant damage to the Group's infrastructure assets along the Main North Line ("MNL").

Impact on assets

KiwiRail has continued to work on the rebuild for the financial year ended 30 June 2018 and an additional impairment charge of \$221.6m has been recognised for the capital cost of reinstatement incurred as at 30 June 2018 (2017: \$77.5m).

Insurance

The Group has insurance coverage in place under an operational infrastructure and consequential loss policy. Cover is provided for loss and damage up to a sum insured of \$350m. While a claim has been submitted as at 30 June 2018, it is not practicable to estimate the full extent of the overall insurance recovery. Only the portion that can be measured reliably has been recognised as a receivable. In the year ended 30 June 2018 we have recognised an insurance receivable of \$6.0m for the estimated recoverable costs incurred to date (2017: \$28.3m).

Crown support

The Crown has agreed to fund the uninsured cost of the rebuild. \$180m was received through equity funding in the year ended 30 June 2018 (2017: \$30.0m).

Cash

The cash balance at 30 June 2018 reflects the insurance proceeds received of \$27.9m (30 June 2017: \$72.1m) and Crown injection received of \$210.0m.

27. CONTINGENT LIABILITIES**Marsden Point rail corridor designation**

The Group has confirmed its designation of the rail corridor from the North Auckland Line to Marsden Point. The Northland Regional Council will purchase any land that may be required. The Group has an agreement with the Northland Regional Council that it will have a half share in the acquisition and holding costs of land purchases with the Council.

Holidays Act 2003

A number of New Zealand's public and private organisations have identified issues with the calculation of leave entitlements under the Holidays Act 2003 ("the Act"). During the year, KiwiRail completed its own review of payroll processes which identified instances of non-compliance with the Act. In addition, the Labour Inspectorate completed a payroll audit of KiwiRail. This audit resulted in KiwiRail entering an Enforceable Undertaking to become compliant and remediate historical payroll liabilities for current and former employees. The remediation project is a significant undertaking and work to assess all non-compliance will continue through the 2018/19 financial year.

The final outcome of the remediation project cannot be determined with any certainty at this time and therefore no provision has been recognised at 30 June 2018.

Notwithstanding, KiwiRail has carried out some limited work to determine an indicative amount of any potential liability. The Board is of the view that the indicative potential liability could be in the range of \$15 million to \$30 million. This is based on selecting a small, non-statistical sample of current and former employees, making a number of early assumptions, calculating an indicative liability for those current and former employees, extrapolating the result, and considering the degree of uncertainty to determine a range. Given the high level of uncertainty, the final outcome could fall outside of this range.

28. EVENTS SUBSEQUENT TO BALANCE DATE

There were no material events subsequent to balance date.



Independent Auditor's Report

To the readers of KiwiRail Holdings Limited's Group financial statements for the year ended 30 June 2018

The Auditor-General is the auditor of KiwiRail Holdings Limited Group (the Group). The Auditor-General has appointed me, Clint Ramoo, using the staff and resources of Audit New Zealand, to carry out the audit of the financial statements of the Group on his behalf.

Opinion

We have audited the financial statements of the Group on pages 66 to 95, that comprise the statement of financial position as at 30 June 2018, the statement of comprehensive income, statement of movements in equity and statement of cash flows 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 on pages 66 to 95:

- present fairly, in all material respects:
 - its financial position as at 30 June 2018; and
 - its financial performance and cash flows for the year then ended; and
- comply with generally accepted accounting practice in New Zealand in accordance with the New Zealand equivalents to International Financial Reporting Standards.

Our audit was completed on 23 August 2018. This is the date at which our opinion is expressed.

The basis for our opinion is explained below and draws your attention to the uncertainties relating to the outcome of the rail review on the structure of the Group and carrying value of assets in future years and the contingency for entitlements under the Holidays Act 2003. In addition, we outline the responsibilities of the Board of Directors and our responsibilities relating to the financial statements, and we explain our independence.

Uncertainties relating to the outcome of the rail review on the structure of the Group and carrying value of assets in future years

Without modifying our opinion, we draw your attention to the disclosure in note 1(g) on page 71 relating to the rail review, which is working towards defining the purpose of rail, and determining the appropriate structure, capital requirements and funding mechanisms for the Group in future years. The disclosure also explains that decisions arising from the review may have an impact on how the Group's assets are valued and presented in the financial statements.

Contingency for entitlements under the Holidays Act 2003

Also, without modifying our opinion, we draw your attention to the disclosures in note 27 on page 95 relating to the Group's contingent liability to remediate issues associated with the calculation of entitlements under the Holidays Act 2003, which could be significant. The range of \$15m to \$30m is indicative, with a high level of uncertainty, and the final outcome could fall outside of this range.

Basis for our opinion

We carried out our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the Professional and Ethical Standards and the International Standards on Auditing (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board. Our responsibilities under those standards are further described in the Responsibilities of the auditor section of our report.

We have fulfilled our responsibilities in accordance with the Auditor-General's Auditing Standards.

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

Responsibilities of the Board of Directors for the financial statements

The Board of Directors is responsible on behalf of the Group for preparing financial statements that are fairly presented and that comply with generally accepted accounting practice in New Zealand.

The Board of Directors is responsible for such internal control as it determines is necessary to enable it to prepare financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Board of Directors is responsible on behalf of the Group for assessing the Group's ability to continue as a going concern. The Board of Directors is also responsible for disclosing, as applicable, matters related to going concern and using the going concern basis of accounting, unless there is an intention to liquidate the Group or to cease operations, or there is no realistic alternative but to do so.

The Board of Directors' responsibilities arise from the State Owned Enterprises Act 1986.

Responsibilities of the auditor for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit carried out in accordance with the Auditor-General's Auditing Standards will always detect a material misstatement when it exists. Misstatements are differences or omissions of amounts or disclosures, and can arise from fraud or error. Misstatements are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decisions of readers taken on the basis of these financial statements.

We did not evaluate the security and controls over the electronic publication of the financial statements.

As part of an audit in accordance with the Auditor-General's Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. Also:

- We identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of the internal control.
- We obtain an understanding of internal control relevant to the audit 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.

- We evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors.
- We conclude on the appropriateness of the use of the going concern basis of accounting by the Board of Directors and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- We evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Board of Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify in our audit.

Our responsibilities arise from the Public Audit Act 2001.

Other Information

The Board of Directors is responsible for the other information. The other information comprises the information included on pages 2 to 65, but does not include the financial statements, and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of audit opinion or assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information. In doing so, we consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on our work, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Independence

We are independent of the Group in accordance with the independence requirements of the Auditor-General's Auditing Standards, which incorporate the independence requirements of Professional and Ethical Standard 1 (Revised): Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board.

Other than the audit, we have no relationship with, or interests in, the Group.



Clint Ramoo
Audit New Zealand
On behalf of the Auditor-General
Wellington, New Zealand

Directory

Bankers

Bank of New Zealand
North End Branch, 100 Lambton Quay, Wellington
P.O. Box 1596, Wellington 6140

Auditors

Clint Ramoo, Audit New Zealand
On behalf of the Auditor-General
Level 2, 100 Molesworth Street, Wellington
Private Bag 99, Wellington 614

Registered office

Level 3, 8–14 Stanley Street, Auckland 1010

Further information

For assistance, publications or information concerning KiwiRail please visit our website at www.kiwirail.co.nz or contact:

KiwiRail Communications
PO Box 593, Wellington, 6140
Telephone: 0800 801 070
Email: kiwirail@kiwirail.co.nz

