



ERM Power Limited
Annual Report 2011



Vision Statement

ERM Power aspires to be the electricity supplier of choice to Australia's large business customers.

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About ERM Power

ERM Power is an integrated energy company which operates electricity sales, generation and gas procurement businesses.

Founded in 1980 as a specialist energy advisory firm, the Company grew through deregulation and privatisation to become one of Australia's largest private energy sector companies before listing on the Australian Securities Exchange (ASX) on 10 December 2010.

ERM Power has four key business units – ERM Sales, ERM Generation Assets, ERM Generation Development and Operations, and ERM Gas.

ERM Power aspires to be the electricity supplier of choice to Australia's large business customers through a differentiated service offering tailored to the specific needs of the customer.

ERM Sales

ERM Power's electricity sales business, ERM Sales, was established in 2007.

ERM Sales sells electricity to large business customers which typically spend more than \$75,000 per annum on electricity and, on average, spend about \$1.5 million per annum.

The business provides large corporate and industrial energy users with tailored energy solutions.

ERM Sales' customers operate in a wide range of industries including manufacturing, mining, education, healthcare, infrastructure, retailing, government and consumer staples.

ERM Sales is one of the largest electricity providers (by load) to business customers in Queensland and has a growing business in New South Wales, the Australian Capital Territory, Victoria, Tasmania, South Australia and Western Australia.

ERM Generation Assets

The ERM Generation Assets business consists of ERM Power's interests in low emission gas-fired peaking power stations at Oakey in Queensland and Neerabup in Western Australia.

These power stations are strategically located close to energy resources and infrastructure in regions that are forecast to experience high growth in electricity demand.

ERM Power owns a 62.5% effective interest in the Oakey power station and a 50% interest in the Neerabup power station. The power stations are fully contracted through

long-term off-take contracts, have long-term, limited-recourse project debt facilities in place and are expected to have a significant useful operating life after current off-take arrangements end.

Oakey power station

Oakey is a 332 MW two unit peaking power station with dual fuel capability (gas and distillate) that is located at Oakey, about 150 km west of Brisbane.

ERM Power led the development of Oakey, which was commissioned in December 1999.

Oakey has a long-term power purchase agreement (PPA) with AGL that runs until the end of 2014 when the current project debt is scheduled to have been repaid. Most of the power station's operation has been fuelled by natural gas supplied by AGL under an agreement that expires at the same time as the PPA.

The off-take contract has been structured such that the plant is usually dispatched at times of peak electricity demand and high prices, such as on the hottest days of summer.

Neerabup power station

Neerabup is a 330 MW two unit peaking power station at Neerabup, about 40 km north of Perth and incorporates a 30 km high-pressure gas pipeline and gas compressor station that provides a connection to the Dampier to Bunbury Natural Gas Pipeline and linepack storage of gas to allow for generation at peak price periods.

Neerabup was commissioned in October 2009 with a long-term, 20 year off-take contract with Synergy, a Western Australian State Government-owned corporation.

The off-take contract is structured so that the plant is mostly dispatched in times of peak electricity demand and high prices.

ERM Generation Development and Operations

ERM Generation Development and Operations is responsible for delivering power generation solutions, from the initial concept stage through to development and operations.

ERM Power has managed the development of six power stations with a capacity of 2,669 MW since 1999.

During that time, the Company has raised almost \$1 billion in limited-recourse project finance and brought into operation more than 290 km of high pressure gas pipelines, 18 km of high voltage power transmission lines, a major electrical sub-station and two gas compression plants.

In the six years to 30 June 2011, ERM Power led the development of five major gas-fired power stations in three states (Braemar 1 and 2 in Queensland, Uranquinty in New South Wales and Kwinana and Neerabup in Western Australia) and in two different electricity markets (National Electricity Market in the eastern states and the Wholesale Electricity Market in Western Australia).

ERM Generation Development and Operations partners with industry-leading companies to implement its development strategy. The business provides services to partnerships where ERM Power is a partner, and also to third parties where ERM Power has divested its interest for strategic reasons.

The business is also responsible for the management and operation of electricity generation and gas pipelines for the Neerabup and Kwinana power stations.

ERM Power has a land bank around key energy hubs in Australia's high-growth regions and is targeting development of more than 4,500 MW of additional generation capacity and more than 1,300 km of gas pipelines.

The business has development approval for 1,210 MW of generation in the proposed Braemar 3 and Wellington 1 power station projects in Queensland and New South Wales, along with environmental approval for the 330 MW Three Springs Project in Western Australia. ERM Power is ready to commit to a development when it is required by the electricity sales market.

ERM Gas

ERM Gas was established in 2007 and focuses on procuring long-term gas supplies for future ERM Power projects through commercial gas supply contracts and exploration.

More than \$3 billion of gas has been procured across all of ERM Power's generation developments.

ERM Gas has joint venture equity interests in more than 10,400 km² of gas exploration acreage in Western Australia's on-shore Perth Basin. It has evolved from a small, complementary and developing business into an emerging business with the potential to deliver profits in its own right over the next few years following two consecutive exploration successes.

The Red Gully-1 gas and condensate discovery in exploration permit EP 389 in the on-shore Perth Basin of Western Australia in March 2011 followed the success of the nearby Gingin West-1 well in the same permit in April 2010.



Neerabup power station

Chairman's and Managing Director's Report

Almost 12 months ago new investors were invited to join us, our fellow directors, senior management and other employees as shareholders of ERM Power Limited, a company with 30 years of operating history, through an initial public offer (IPO) and listing on the ASX.

Our new investors gained direct exposure to the forecast growth of the Australian electricity industry through ERM Power's businesses spanning electricity sales, generation and gas procurement.

Over the past year, our management and employees have worked hard through turbulent times to achieve and exceed the goals and forecasts we set for ourselves.

Outlook

ERM Power is tracking well for FY2012 and increased its forecasts for FY2012 by 34% for EBITDAIF¹ and 7% for Underlying NPAT².

The EBITDAIF¹ forecast for FY2012 is \$83.5 million, compared with the prospectus forecast of \$62.4 million.

Underlying NPAT² for FY2012 is forecast to be \$27 million, compared with the prospectus forecast of \$25.2 million.

Highlights since the start of FY2012 include:

- Upgraded FY2012 Revenue forecast;
- acquiring an additional 50% of the Oakey power station, which settled on 1 July 2011;
- starting the electricity supply contract with the Commonwealth Government in New South Wales and the Australian Capital Territory.
- signing a Gas Sale Agreement with Alcoa in Western Australia for gas supply from the EP 389 discoveries; and
- receiving promising seismic results from the Charger and Garibaldi oil and gas prospects in Western Australia.

As major shareholders in the Company we understand if other shareholders have been disappointed with the share price, which has not tracked the strong operational improvement in the business since listing on the ASX.

Fortunately ERM Power is on track to exceed its prospectus forecasts and remains focused on value creation for shareholders. We are confident this value will be recognised in the market in time as the Company pursues its vision of being the electricity supplier of choice to Australia's large business customers.

FY2011 results

We are pleased to report that ERM Power exceeded prospectus forecasts for revenue, EBITDAIF¹ and Underlying Net Profit After Tax (Underlying NPAT²) for the financial year ending 30 June 2011 (FY2011).

Revenue of \$549.8 million, including other income and asset sales, was 15% higher than the prospectus forecast of \$478.9 million and 32% higher than revenue of \$418.4 million in FY2010.

EBITDAIF¹ of \$46.4 million was 2% higher than the prospectus forecast of \$45.7 million and 32% lower than EBITDAIF¹ of \$68.7 million in FY2010, which included a profit of \$36.4 million from an asset sale.

Underlying NPAT² was \$6.3 million, 80% higher than the prospectus forecast of \$3.5 million (FY2010: \$10.3 million).

Financial Highlights (\$ million)	FY2011 Actual	FY2011 Prospectus Forecast	Change
Revenue	549.8	478.9	15%
EBITDAIF ¹	46.4	45.7	2%
Underlying NPAT ²	6.3	3.5	80%
Statutory NPAT	16.2	26.5	-39%
Underlying EPS ³	4.5	2.2	106%
Dividend per share	3.5	3.5	-

These results were achieved despite extreme weather including floods and cyclones in Queensland and heatwaves in the southern states, which affected the Company's electricity sales business, ERM Sales.

This strong result demonstrates the robustness of ERM Power's business model and risk management and is a testimony to the skills and dedication of our people and the ongoing spirit and culture of the Company.

¹ EBITDAIF – earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts, and including profit of associate and non-controlling interests.

² Underlying NPAT – excludes marked-to-market changes recognised on financial instruments and onerous contracts from NPAT and includes profit of associate and non-controlling interests.

³ Underlying EPS – calculation of underlying EPS is based on Underlying NPAT.

ERM Sales, which sells electricity to large commercial and industrial customers, achieved 70% growth in sales and 138% growth in earnings compared with the previous year.

ERM Sales has most of its forecast FY2012 electricity sales volumes covered by existing sales contracts and is forecast to achieve 56% growth in revenue to \$759 million in the FY2012 financial year, which is well above the prospectus forecast.

The ERM Sales business has also achieved significant geographic diversification with the percentage of sales from Queensland falling from 86% to 59% in 12 months.

ERM Power's gas-fired power stations, Oakey in Queensland and Neerabup in Western Australia, performed reliably and above expectations, and exceeded prospectus earnings forecast by 10%.

Operational performance and asset utilisation were also above expectations.

The generation operations business produced higher profits than forecast from services to the Braemar 2, Neerabup and Kwinana power stations, largely as a result of bonus payments.

The generation development business had a productive year, advancing future projects including Braemar 3 in Queensland, Wellington 1 in New South Wales and Three Springs in Western Australia, which will allow ERM Power to remain a leader in the Australian electricity development market.


The gas procurement business, ERM Gas, exceeded expectations with its second consecutive oil and gas discovery in Western Australia along with an increasing interest in prospective exploration acreage.

Other highlights included:

- the signing of major Commonwealth and State Government electricity sales contracts in Queensland, New South Wales and Tasmania;
- the acquisition of a controlling interest in the 332 MW gas-fired Oakey power station (after year end); and
- securing additional strategic development sites in New South Wales and Western Australia.

A fully franked dividend of 3.5 cents per share was declared for the FY2011 period as proposed in the prospectus.

 revenue **15%**
higher than
forecast

 **70%**
growth in
electricity sales

power stations
exceeded forecasts by
10%

 **25%**
geographical
sales diversification

FY2012
forecast revenue
\$853 million

Chairman's and Managing Director's Report continued...

IPO

In December 2010, ERM Power brought to market a company that had grown organically over 30 years to become one of Australia's largest private sector energy companies, with expansion opportunities that were beyond its capital limitations.

The purpose of the IPO was to raise funds for immediate growth and provide access to capital markets for additional growth.

ERM Power's existing shareholders did not sell any shares in the IPO and the funds raised were deployed in accordance with the prospectus.

The ability of ERM Power as a publicly-listed company to use its capital to take up a controlling interest in Oakey power station in July 2011 affirmed the benefits of the IPO.

The increase in revenue and profit forecasts for FY2012 represents a significant return to the new shareholders who showed faith by investing in the Company.

Industry overview

ERM Power operates in an energy industry which is experiencing an unprecedented level of change.

The Federal Government's carbon policy is a significant 'x-factor' which is hard to predict. However, ERM Power is favourably positioned with low-emission gas and gas generation assets.

Privatisation of government-owned electricity assets and businesses is expected to continue.

Mining and liquefied natural gas (LNG) industries are expected to drive significant electricity demand growth in Queensland and Western Australia.

An industry-wide reluctance to commit to new electricity generation leaves ERM Power well positioned with approved short lead-time projects ready to meet market shortfalls in electricity supply when they arise.

Subsidised intermittent and unscheduled wind and solar is another 'x-factor' that is hard to predict but ERM Power's planned low-emission peaking gas projects are likely to be needed in any scenario.

Export LNG has driven large increases in gas prices on the west coast of Australia and this is expected to occur on the east coast as LNG trains come on line. These LNG driven gas price increases will affect Australia's electricity markets going forward.

Looking further ahead we expect to see significantly more demand-side response to higher electricity prices and potentially a significant electric vehicle presence.

ERM Power has evolved because of, and thrives on, a dynamic market.

We believe ERM Power is well positioned to anticipate, prepare for and respond to these changes as they arise.

People and community

ERM Power's achievements also reflect its focus on all stakeholders, including customers, shareholders, employees, suppliers, governments and, importantly, members of the communities in which it operates.

The Company maintained its life-time record of no permanent injuries over more than 30 years of business.

Community sponsorship activities included regional tours by the Queensland Symphony Orchestra, Camerata of St John's Chamber Orchestra and Queensland Ballet performances in Toowoomba, and other community activities at Wellington in New South Wales.

ERM Power sponsors indigenous education through the Trevor St Baker and Richard Wilkes Indigenous Scholarship Foundation with the first two scholars successfully completing their five-year secondary education at Guildford Grammar School in Perth in 2010.

Finally, we would like to thank our staff, fellow directors, partners, customers and investors, and the communities in which we operate, who have all helped to make our first year as a publicly listed company, a positive and successful one.



Trevor St Baker
Non-Executive Chairman



Philip St Baker
Managing Director



ERM Sales employee with a customer

ERM Sales

ERM Sales exceeded its prospectus forecasts for FY2011 as it continued to grow strongly in its fourth year of operation as an electricity retailer focused on large commercial and industrial customers across Australia.

In the last financial year, ERM Sales entered the South Australian and Western Australian markets to complement its increasing presence in Queensland, New South Wales (NSW), the Australian Capital Territory (ACT), Victoria and Tasmania.

The new markets and existing markets represent excellent growth potential for ERM Sales.

Growth was particularly strong in NSW and well above historical levels and expectations.

Key customers signed in the financial year were the Commonwealth of Australia, Tasmanian Government agencies, Westfield (Queensland), Myer, Woolworths (Queensland and Tasmania), Bunnings (Victoria), Hungry Jacks (Victoria), Regal Cream Products (Bulla Dairy Foods), Tassal Operations, Hellyer Mill Operations and Norton Gold Fields Limited (Paddington Operations).

The four-year \$300 million contract with the Commonwealth of Australia covers 82 departments and agencies, including the Department of Defence, at 406 sites in the ACT and a further 83 Department of Defence sites in NSW.

Outlook

Despite its exceptional growth, the business has a relatively small share of its target market and offers strong growth potential as it taps a range of opportunities.

Financial performance

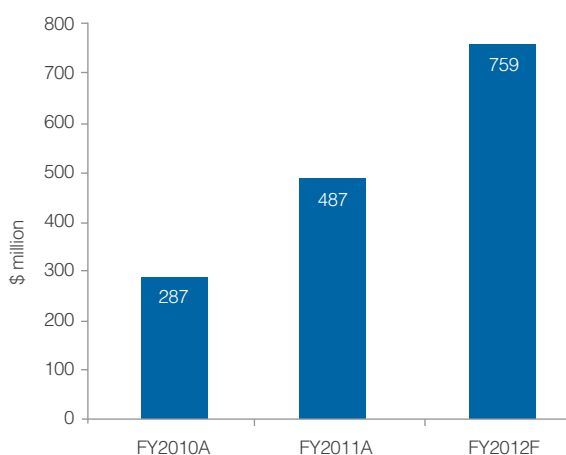
Revenue was \$486.7 million in FY2011, which was 13% ahead of the prospectus forecast of \$429.3 million and 70% more than FY2010 of \$286.7 million.

Sales volumes were 5,646 gigawatt hours (GWh), which was 39% more than the previous year due to growth in customer numbers in all segments of the target market across Australia.

Volumes were 6% below the prospectus forecast of 6,010 GWh because severe flooding in central Queensland in December 2010 and January 2011 affected customer loads, particularly in the mining and rail sectors.

EBITDAIF¹, which excludes the impact of unrealised marked-to-market changes to the values of financial instruments, increased by 138% to \$22.5 million (FY2010: \$9.5 million), which was 3% higher than the prospectus forecast of \$21.9 million.

Revenue Growth



“ERM Power has a thorough understanding of our business so they can provide the expert advice we need, allowing us to save money on our energy costs and valuable time when dealing with energy related matters for our day-to-day business.

ERM Power provides QAL with excellent account management and customer service and we rely on them to offer us more than just a retail product. We trust ERM Power for their advice and their service.”

Peter Mouna, Principal Buyer Raw Materials and Energy, Queensland Alumina Limited (QAL)

¹ EBITDAIF – earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts, and including profit of associate and non-controlling interests.

National growth

ERM Sales continued to diversify its customer base by sector and geographically, further strengthening the business.

ERM Sales has been working to diversify its retail customer portfolio in terms of both industry classification and geographic region (State). The charts below show the progress made in both of these areas over the last year.

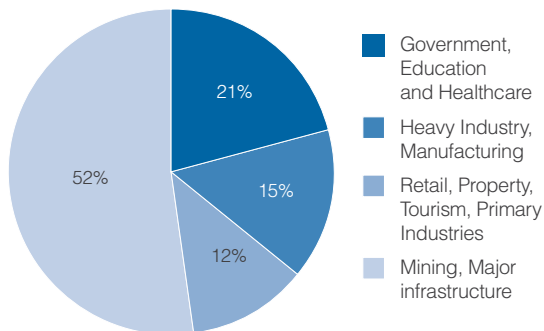
In terms of industry, customers have been aggregated into four major industry classifications:

- government, education and healthcare;
- heavy industry and manufacturing;
- retail, wholesale, tourism, property and primary industries (agriculture); and
- mining and major infrastructure (such as pipelines and airports).

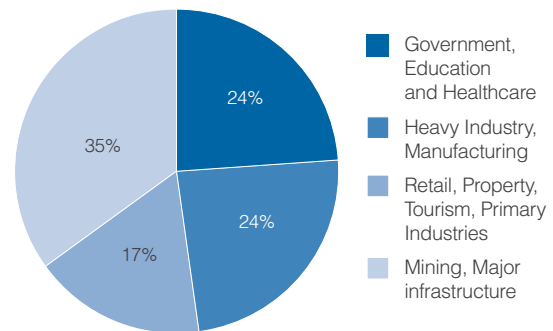
The customer portfolio in July 2011 (compared to July 2010) illustrates how the dependency on the mining and major infrastructure industry has been reduced relative to the other three industry classifications. The focus is on balancing industry representation as this provides improved load stability.

In terms of sales volume by State, 2011 represented an increased presence in the other states and hence a reducing reliance on Queensland. New South Wales as a percentage of the total sales portfolio has increased from 4% to 17% and Victoria has increased from 6% to 8%. In addition, an increasing presence in South Australia and Western Australia will further reduce the concentration, and therefore the reliance on Queensland market.

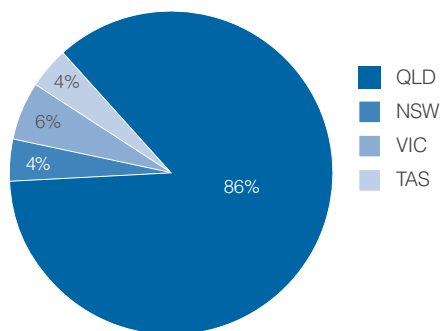
Sales by Industry in July 2010



Sales by Industry in July 2011

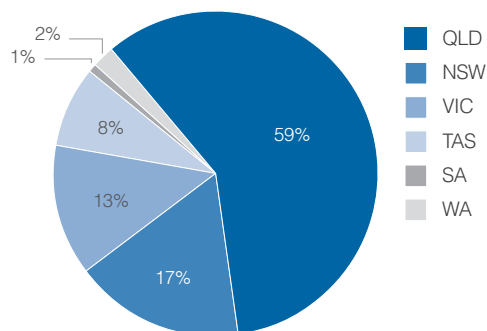


Sales (GWh) by State in July 2010



FY2010: 4,065 GWh

Sales (GWh) by State in July 2011



FY2011: 5,646 GWh



ERM Sales employees

ERM Generation Assets

The ERM Generation Assets business, consisting of a 12.5% effective interest (62.5% from 1 July 2011) in the 332 MW Oakey power station in Queensland and a 50% interest in the 330 MW Neerabup power station in Western Australia, performed reliably, safely and better than forecast in the prospectus. ERM Power sold its 30% interest in the 320 MW Kwinana power station in Western Australia in October 2010.

Financial performance

Revenue², based on the Group's proportionate interests in the Neerabup and Kwinana power stations, was \$47.1 million (FY2010: \$83.7 million), which was higher than the prospectus forecast of \$37.4 million because the interest in Kwinana was held for a month longer than expected and Neerabup was called to operate by the system operator more than forecast.

EBITDAIF¹ (including share of associates) was also higher at \$28.9 million (FY2010: \$36.4 million) compared with the forecast of \$26.2 million.

The FY2011 results include a contribution from ERM Power's 30% interest in Kwinana until it was sold in October 2010. The previous year's results included a contribution from the Company's 25.05% interest in the Braemar 2 power station in Queensland, which has been sold.

The Group has maintained its interest in Neerabup and increased its interest in Oakey. These power stations are high-quality, low-risk generation assets that deliver solid and predictable returns while steadily appreciating in value and positioning ERM Power for future strategic value-adding opportunities through expansion, recontracting, redevelopment and optimisation.

Oakey results

Revenue, based on ERM Power's 12.5% interest in FY2011, was \$4.3 million (FY2010: \$4.1 million), which was higher than the prospectus forecast of \$4.0 million for the same period.

The proportionate share of EBITDAIF¹ of \$3.1 million (FY2010: \$3.1 million) was below the forecast of \$3.3 million.

ERM Power's share of Oakey's NPAT was \$1.4 million (FY2010: \$1.3 million), which was also lower than the forecast of \$1.6 million.

Distributions to ERM Power were \$0.6 million (FY2010: \$0.5 million), which were above the forecast of \$0.5 million.

The power station's record of no lost time injuries over its 11 year life was maintained in the last year.

Oakey acquisition

On 1 July 2011 ERM Power lifted its effective interest in the Oakey power station to 62.5% when it acquired a 50% interest from Redbank Energy Ltd (formerly Alinta Energy Ltd) for \$61.7 million.

The acquisition of the additional 50% interest was consistent with ERM Power's strategy of building a portfolio of high-quality, low-emission power generation assets in high-growth regions.

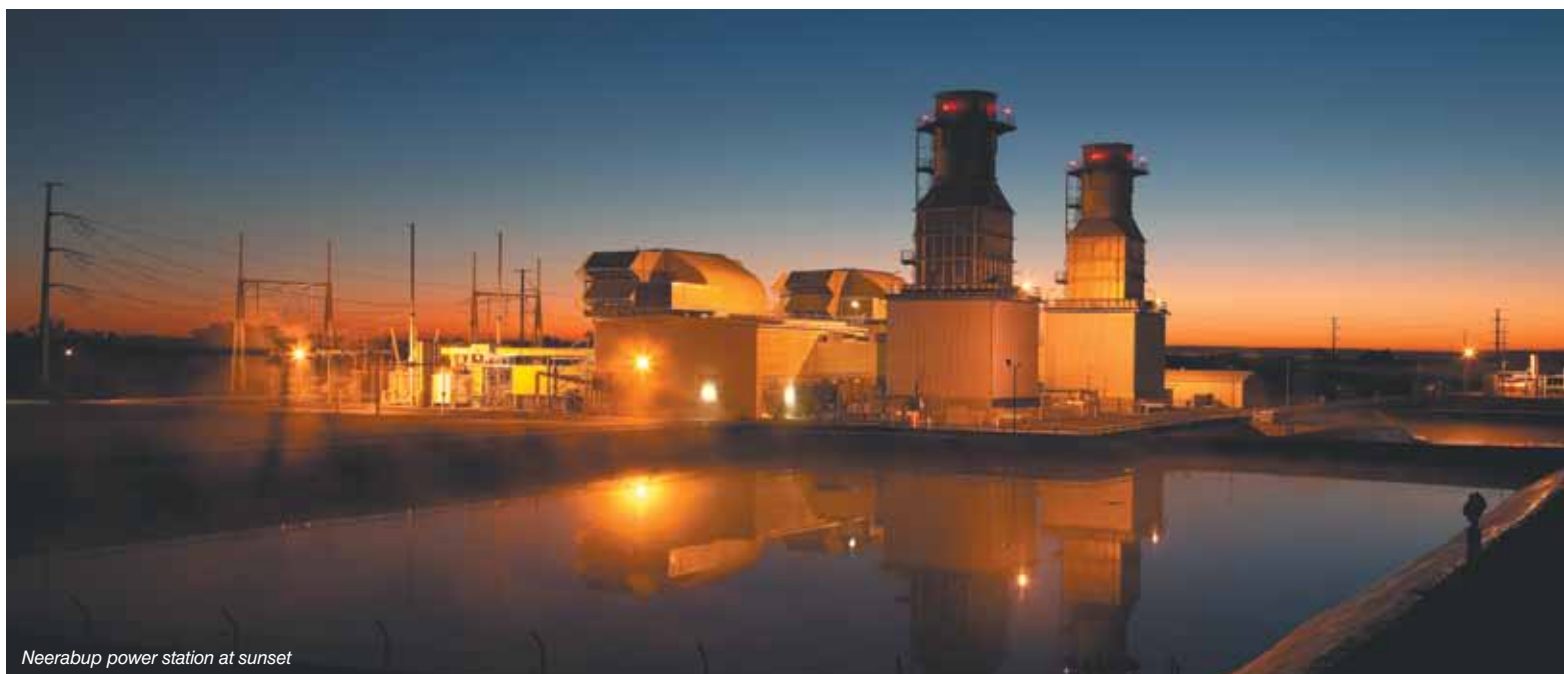
The purchase price was less than 50% of the estimated replacement cost and the asset is in near-new condition because it is a peaking power station that has operated less than 5% of the time over its 11 years of operation.

In addition to these benefits, ERM Power has the skills, experience and complementary businesses to exploit substantial potential upside from this asset.

¹ EBITDAIF – earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts, and including profit of associate and non-controlling interests.

² Revenue does not include Oakey power station, which was equity accounted in FY2011.

ERM Generation Assets continued...



Neerabup power station at sunset

Neerabup results

Revenue in FY2011 was \$26.3 million (FY2010: \$13.6 million), based on ERM Power's 50% interest, compared with the prospectus forecast of \$24.0 million. Neerabup's results in FY2010 were for a part year only as the power station was commissioned in October 2009.

The Company's share of EBITDAIF¹ of \$21.8 million (FY2010: \$11.6 million) was higher than the forecast of \$20.5 million because the station was called to operate by the system operator more than forecast.

Net cash flow after project debt service was \$3.3 million (FY2010: \$1.7 million), compared with \$2.8 million in the prospectus.

Neerabup power station performed reliably and safely with no lost time injuries.

Given its highly contracted nature, the business produces predictable revenues and cashflows.

Braemar 2 divestment

On 30 September 2010, ERM Power exercised a put option to sell its remaining 25.05% interest in the 519 MW Braemar 2 power station in Queensland to Arrow Energy for \$66.1 million.

ERM Power led the development of Braemar 2, an open cycle gas peaking power station and a 110 km high-pressure gas pipeline about 30 km west of Dalby which began commercial operations in July 2009.

The sale of the 25.05% interest was completed on 30 June 2011 when Arrow Energy took over operations of the power station following the sale of a 24.95% interest to Arrow Energy in September 2009 for \$45 million. The total profit of \$36.4 million on the sale of the combined 50% interest was recognised in FY2010.

Kwinana divestment

ERM Power sold its 30% interest in the 320 MW Kwinana power station to ANZ Specialist Asset Management Limited for a \$4.7 million profit in October 2010.

ERM Power led the development of Kwinana, a combined cycle gas turbine power plant which is located about 30 km south of Perth in the Kwinana Industrial Estate. It was commissioned in October 2008.

The consideration was \$39.9 million in gross terms, before the redemption of the notes used to fund the initial equity investment.

The Company continues to operate the Kwinana power station on behalf of its new owners.

¹EBITDAIF – earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts, and including profit of associate and non-controlling interests.

ERM Generation Development and Operations

Overview

As the dominant form of new generation in Australia over the last decade, gas-fired electricity has proven itself as the most affordable, low-emission power solution in Australia.

ERM Generation and Operations is at the forefront of gas-fired electricity development, having built more than one quarter of Australia's scheduled new power projects since 2005.

ERM Power's strategic thinking and wealth of industry knowledge allows it to identify, design, build and operate low-emission power stations in locations with great potential. A key competitive advantage is a bank of land assets at key energy hubs in high-growth regions, close to gas and infrastructure.

ERM Power is targeting the development of more than 4,500 MW of additional generation capacity and more than 1,300 km of gas pipelines.

In the past year, the Wellington 1 power project in New South Wales received approval for a modification of its original development approval and the development application for the Braemar 4 project in Queensland was submitted.

The business has developed an effective community engagement process for ensuring people living around ERM Power projects are fully informed of the process that goes into developing gas-fired power stations and the benefits for the economy and the environment.

Projects

Critical to ERM Generation and Operations' development strategy is long-term electricity supply and demand planning. The business identifies deficiencies in the electricity supply-demand mix, new generation requirements and optimal plant types to fulfil these needs.

Power generation opportunities are identified up to 10 years into the future, positioning the business to deliver generation projects to meet growth in electricity demand.

Three Springs

ERM Generation and Operations secured an option over a strategic land parcel at Three Springs in Western Australia in September 2010. This land has space for two generation sites which will be ideally positioned next to Western Power's future 330kV substation.



Kwinana power station employee

ERM Generation and Operations continued...

This substation will be a major distribution point for electricity to the region's growing mining community, and ERM Power's site will be at the epicentre of the transmission network.

ERM Generation and Operations has been communicating with local land owners, indigenous groups and regional councils, ensuring full disclosure and transparency of development plans. The development has received a positive reception from the local community with local councils providing support.

ERM Power received environmental approval for the project from the Western Australian Government in September 2011.

ERM Power is the lead developer, project manager, construction manager and financial arranger for Three Springs and owns 100% of the project. The Company plans to retain at least 50% after introducing an equity partner prior to financial close and expects to be the power station's operator.

Wellington 1

Wellington 1 is a proposed open-cycle gas-fired power station of up to 660 MW capacity combined with an integrated high-pressure gas pipeline. The proposed power station is strategically located with access to conventional gas and emerging gas reserves and is close to the largest load growth region in New South Wales.

In September 2010 the New South Wales Government approved a modification of the original development approval to enable Wellington 1 to be developed as a peaking or intermediate power station.

In March 2011 the New South Wales Planning Assessment Commission granted environmental approval for the 203 km Young to Wellington pipeline which will transport gas to the power station.

ERM Generation and Operations has undertaken extensive community engagement to ensure land owners and members of the community are aware and informed about ERM Power's proposals to reinvigorate the region.

ERM Power is the lead developer, project manager, construction manager and financial arranger for Wellington 1 and owns 100% of the project. The Company plans to retain at least 50% after introducing an equity partner prior to financial close and expects to be the operator of the power station.

Demand for new generation has softened in New South Wales and, in response, ERM Power has reforecast the financial close of Wellington 1 to the 2014 calendar year from FY2013 previously, with commissioning expected to occur in the 2016 calendar year.

Braemar 3

The Braemar 3 power station development is a proposed open-cycle gas-fired power station of up to 550 MW capacity at ERM Power's Braemar land hub in Queensland.

ERM Power has executed an engineering procurement and construction contract with a Siemens-John Holland joint venture and a long-term maintenance agreement with Siemens.

In addition, ERM Power has executed a connection and access agreement with PowerLink Queensland's Braemar sub-station located adjacent to ERM Power's land holdings, which will provide a high degree of transmission security, being on the main interconnector between Queensland and New South Wales.

ERM Power is the lead developer, project manager, construction manager and financial arranger for Braemar 3 and owns 100% of the project. The Company plans to retain at least 50% after introducing an equity partner prior to financial close and expects to be the operator of the power station.

ERM Power has also reforecast the financial close of Braemar 3 from FY2012 to FY2013 because of softer demand for new generation in Queensland, with commissioning expected to occur in FY2015.

Braemar 4

ERM Generation and Operations also acquired additional land near the Braemar power stations and submitted a development application for a 500 MW power station on the site.

Wollar

ERM Generation and Operations secured an option over a strategic 2000-acre parcel of land at Wollar in New South Wales in November 2010.

This site will provide future base load power when coal-fired power stations across the National Electricity Market (NEM) retire and electricity supply falls short of demand.

The Wollar site is near the 500,000 volt (500kV) transmission system.



Kwinana power station employee

Operating performance

ERM Generation and Operations has service agreements with the Neerabup and Kwinana power stations in Western Australia for the comprehensive management of those respective businesses and had a service agreement with Braemar 2 until 30 June 2011.

Management services to Braemar 2 concluded with the sale of the remaining ERM Power interest in this power station.

All power stations performed reliably and safely with no lost time injuries.

Financial performance

ERM Generation and Operations generated revenue before asset sales of \$8.7 million in FY2011 which was higher than the prospectus forecast of \$3.4 million because of an operator bonus from Kwinana and additional operating fees from the Braemar 2 power station.

As forecast, no development fees were received in FY2011.

EBITDAIF¹ was \$0.1 million, compared with the prospectus forecast of a \$1.7 million loss.

Asset sales generated a gain of \$4.7 million (FY2010: \$36.4 million), which differs from the prospectus forecast of \$6.6 million because of a balance sheet tax credit related to the Kwinana power station sale which is included in tax expense.

¹EBITDAIF – earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts, and including profit of associate and non-controlling interests.

ERM Gas

The evolution of ERM Gas from a small, complementary and developing business into an emerging business with the potential to deliver profits in its own right continued with a second exploration success.

The Red Gully-1 gas and condensate discovery in exploration permit EP 389 in the onshore Perth Basin of Western Australia in March 2011 followed the success of the nearby Gingin West-1 well in the same permit in April 2010.

The discoveries reinforced ERM Power's decision to expand across the electricity supply chain by creating a separate gas business to procure long-term gas supplies for future generation projects in 2007.

ERM Gas owns 21.25% of EP 389, which covers 1,500 km², and has various interests in approximately another 8,900 km² of exploration acreage in the on-shore Perth Basin. The acreage is ideally positioned near markets, transmission pipelines, power stations, compression stations and linepack facilities.

The ERM Gas strategy is to increase the value of its acreage through technical analysis, exploration, commercialisation and farm-out activities.

Financial performance

ERM Gas spent \$4.9 million on exploration in FY2011 compared with the forecast for capital expenditure of \$5.4 million.

Red Gully-1 well

The success of the ERM Gas strategy was demonstrated in March 2011 when the Red Gully-1 well recorded the largest gas and condensate flow from a Jurassic reservoir in onshore Western Australia. ERM Gas actively contributed to the technical assessment of the prospects in co-operation with the operator of EP 389, Empire Oil Company (WA) Limited (Empire), using ERM Gas staff's deep upstream petroleum expertise across a wide range of Australia's petroleum provinces in reservoir engineering, geophysics, engineering and production.

The production test of the 'D' Sand Cattamarra Formation achieved a gas flow rate of 11.748 million cubic feet per day (mmcf) on a 38/64 inch choke with associated condensate production of 888 barrels per day (bbl/d).

The Red Gully-1 discovery followed the successful Gingin West-1 well completed in an adjacent structure in April 2010.

Gingin West-1 delivered a maximum gas flow rate of 8.04 mmcf on a 40/64 inch choke during clean up with a peak condensate rate of 376 bbl/d recorded in an extended test.

The Red Gully-1 discovery significantly enhanced the prospects of the combined development of both fields. Empire has estimated the combined fields could contain 20 billion to 30 billion cubic feet of recoverable gas plus associated condensate.

The wells are ideally located, about 80 km north of Perth, less than 3 km from the Dampier to Bunbury and Parmelia gas pipelines, and about 45 km north of the Neerabup power station.

The joint venture parties are advancing the development of gas and condensate production facilities through engineering design work and sub-surface reservoir modelling.

On 4 October 2011, Empire and the EP 389 Joint Venture announced they had negotiated an agreement with Alcoa of Australia Limited for the supply of gas from the Red Gully and Gingin West fields.

The proposed production facility for Gingin West and Red Gully is also well located for condensate sales, being only two hours by road tanker from the BP Kwinana Refinery.

EP 454

In April 2011, about 90 line km of 2D seismic over the large Garibaldi gas prospect in exploration permit EP 454 was acquired and processed. Interpretation and mapping is now being progressed with a view to identifying drilling targets.

ERM Gas has a 50% interest in the permit, which is operated by the other 50% joint venture partner, Empire. ERM Gas lifted its interest in the permit from an initial 12.5% by funding the seismic approval process and program.

The prospect has a large gas trap potential. The Garibaldi prospect is delineated as being 12 square kilometres. The top Permian reservoir objectives have been estimated at 2,000 metres.

The permit is about 220 km north of Perth, 40 km from the Dampier to Bunbury and Parmelia gas pipelines, and 50 km south of the Three Springs development site.



2D seismic interpretation and mapping Garibaldi gas prospect

Other acreage

ERM Gas continues to review other opportunities in existing acreage in Western Australia and new acreage in Western Australia, Queensland, New South Wales and Victoria.

An extension of the ERM Gas strategy to the east coast is a mid-term focus. ERM Gas plans to build an expanded portfolio of gas interests and to de-risk those interests through the application of rigorous technical and geological work.

ERM Power's generation development business is expected to benefit from the ERM Gas business as a result of more informed site identification and improved fuel supply negotiations.

Shale gas

Some of the ERM Gas exploration permits are prospective for shale gas, a fuel which is the focus of increasing global interest because of recent discoveries, acquisitions and other corporate activity.

This activity has increased the attractiveness and potential value of the onshore Perth Basin.

Eastern Star Gas MOU

Negotiations continued with Eastern Star Gas over a gas supply agreement for the proposed Wellington power station development in New South Wales.

In 2010, ERM Power signed a non-binding memorandum of understanding with Eastern Star Gas, operator of the Narrabri Coal Seam Gas Project in New South Wales, for the supply of 20 petajoules (PJ) of gas per year over 20 years.

Carbon Tax

On 10 June 2011 the Australian Government released its climate change plan, *Securing a Clean Energy Future*, under which around 500 of the highest carbon emitters in Australia will need to buy and surrender a permit for every tonne of carbon emitted to the Government.

The carbon price will be fixed for the first three years, starting at \$23 per tonne on 1 July 2012, and escalating at the consumer price index (CPI) rate plus 2.5% for the following two years.

After 1 July 2015, the price will be set by the market under an emissions trading scheme (ETS).

A price floor (\$15 per tonne) and price ceiling (\$20 per tonne above the expected international price at 1 July 2015) will apply in the first three years of the ETS. The price floor will escalate at CPI + 4% and the price ceiling will escalate at CPI + 5%.

Preliminary analysis has been undertaken on the likely impact of the Government's proposals on the current ERM Power business. This analysis and the resulting conclusions are based on a fairly broad set of assumptions and are therefore subject to further detailed assessment.

In general, gas generation is considered a beneficiary of any carbon pricing scheme as it has a lower emissions intensity than both coal and the electricity 'pool' average.

Gas generation incremental costs (for carbon permits) are therefore expected to be less than incremental revenues (higher pool and contract revenues), resulting in higher operating margins and increased demand for gas generation capacity and energy.

The major impacts on ERM Power will be through the direct cost of carbon permits, the indirect cost of permits through higher input costs such as gas, and higher prudential, credit and working capital costs.

However, these costs will be potentially offset by pass-through of direct and indirect carbon and credit costs, and higher revenue from an increase in electricity pool and financial product prices.

ERM Sales contracts are structured to pass on the cost of carbon policies.

The Oakey power station in Queensland and the Neerabup power station in Western Australia are likely to be modest beneficiaries of the tax given they are low emission gas-fired power stations.

The carbon package is considered to be marginally beneficial to the Braemar 3 and Wellington 1 projects but it is not expected to materially impact on the supply-demand balance in the short to medium term. It is not expected to have a material impact on ERM Power's gas exploration or construction businesses.

Future opportunities

The potential closure of 2,000 MW of brown coal plants in Victoria and South Australia by 2020 would create additional new development opportunities.

Replacement plants are expected to be a mix of closed cycle gas turbine (CCGT) and open cycle gas turbine.

The combination of a carbon price and higher black coal prices could accelerate the retirement of some New South Wales and Queensland coal plants and create opportunities for replacement CCGT plant.

The full benefit of a carbon price will flow directly through to renewables projects, although a price of \$23 per tonne is unlikely to have a substantial impact on the commercial viability of these technologies.

The proposal also includes funding assistance for energy consumers to reduce their energy consumption (through activities such as co-generation), which may prove beneficial to ERM Power's demand-side response capability.

Environment

ERM Power is proud to be a leader in producing cleaner electricity for Australia and strives to perform in a safe and environmentally responsible manner which is consistent with its core values of people, planet and performance.

The Company develops power stations fuelled by natural gas, which is a cleaner fossil fuel than oil or coal.

Gas produces about half of the greenhouse gas emissions of coal when burned and, unlike most renewable energy options, can be available 24 hours a day to generate electricity when required.

Low emissions

ERM Power has estimated that the power stations it has developed will produce about 100 million fewer tonnes of greenhouse gas than their coal counterparts over their working lives.

ERM Power developed the Neerabup power station in Western Australia, which began commercial operations in October 2009.

Neerabup is an open cycle power station which boasts significantly lower CO₂ emissions per MWh of power than the average in Western Australia, as the table below demonstrates.

State average CO ₂ production rate	0.82t/MWh
Neerabup CO ₂ production rate	0.61t/MWh

Neerabup emitted about 20,000 tonnes less CO₂ last year than an equivalent coal-fired power station would have emitted to produce the same amount of energy.

ERM Power has a Health, Safety, Environment and Sustainability Committee that assists it to operate safely, responsibly and sustainably and is committed to playing a major role in reducing Australia's carbon footprint.

Water efficiency

Power stations developed by ERM Power are cooled by air or sea water and use little domestic fresh water for cooling. This is in contrast to many of Australia's coal-fired power stations, which use significant amounts of fresh water for cooling.

ERM Power has estimated the power stations it has developed will use approximately 9 billion litres less water over their working lives than the average of the Australian electricity generation sector.



Native flora (Oakey Power Station in background)

People and Safety

ERM Power has an un-compromising approach to safety.

Employees identify risks and take action to prevent loss or harm to people, communities and environment.

The Company has a life time record of no permanent injuries covering more than 30 years of business, more than five million exposure hours and the construction of six major gas-fired power stations and three high pressure gas pipelines.

The Company's safety record is a testament to the effectiveness of its hazard reporting systems, positive safety culture and management commitment to safety. Managers promote a safe culture by encouraging open incident reporting and discussion of safety issues and hazards in leadership meetings.

Senior managers regularly visit work sites and participate in condition inspections and planned job observations, further demonstrating the Company's commitment to safe work.

ERM Power safety initiatives

- Hazard and near-miss reporting to help identify risks.
- Active investigation of hazards.
- Safety training across the business.
- Staff rewarded for showing safety initiative.
- Dedicated on-site safety officers for projects.
- Mandatory on-site alcohol testing.
- Monitoring of industry incident reports.

Results

- 73 improvement actions implemented across three sites.
- More than 4,000 alcohol tests conducted.
- 336 staff safety briefings.
- Zero lost-time injuries.



Neerabup power station employee



Kwinana power station employees

Case study

ERM Power's commitment to safety is demonstrated by its practice of alcohol testing all people entering its industrial sites every day to ensure they are fit for work. This applies to the Neerabup and Kwinana power stations and the Neerabup compressor facility and pipeline right-of-way. This screening regime covers everyone including employees, contractors and visitors.

Anyone who tests positive is re-tested shortly after the first test and if the second test is positive, they are escorted from the site and cannot return for 24 hours. If they return a positive test within three months, they are refused entry until ERM Power is satisfied they are fit for work.

Community

ERM Power is committed to playing a part in building strong and vibrant communities in the regions where it operates.

The Company's partnership and community sponsorship programs are aimed at forming active and mutually beneficial relationships, not merely through financial support, but also through contributing and transferring skills, expertise and knowledge.

In the past 12 months, ERM Power has supported gifted students in Toowoomba by sponsoring academic events such as the Opti-MINDS Challenge, a creative problem-solving competition among students.

In allocating sponsorship funding, ERM strives to achieve a balance among projects that complement its corporate values of people, performance and planet.

It has also assisted the Surat Basin Work Placement Program in south east Queensland by offering work experience opportunities to young Australians starting out in the gas, mining and energy sectors.

ERM Power is dedicated to giving everyone the opportunity to experience the arts and continues to work with partners to bring music to the people of Queensland.

It brought the Queensland Symphony Orchestra to students of the Darling Downs in March and sponsored the Queensland Ballet to perform at the Empire Theatre in Toowoomba in June.

A highlight of the year was sponsorship of the Queensland Music Festival's Opera at Jimbour, and Paul Kelly and Randy Newman performances, which saw 14,000 people gather in Brisbane and Jimbour to enjoy unforgettable shows.

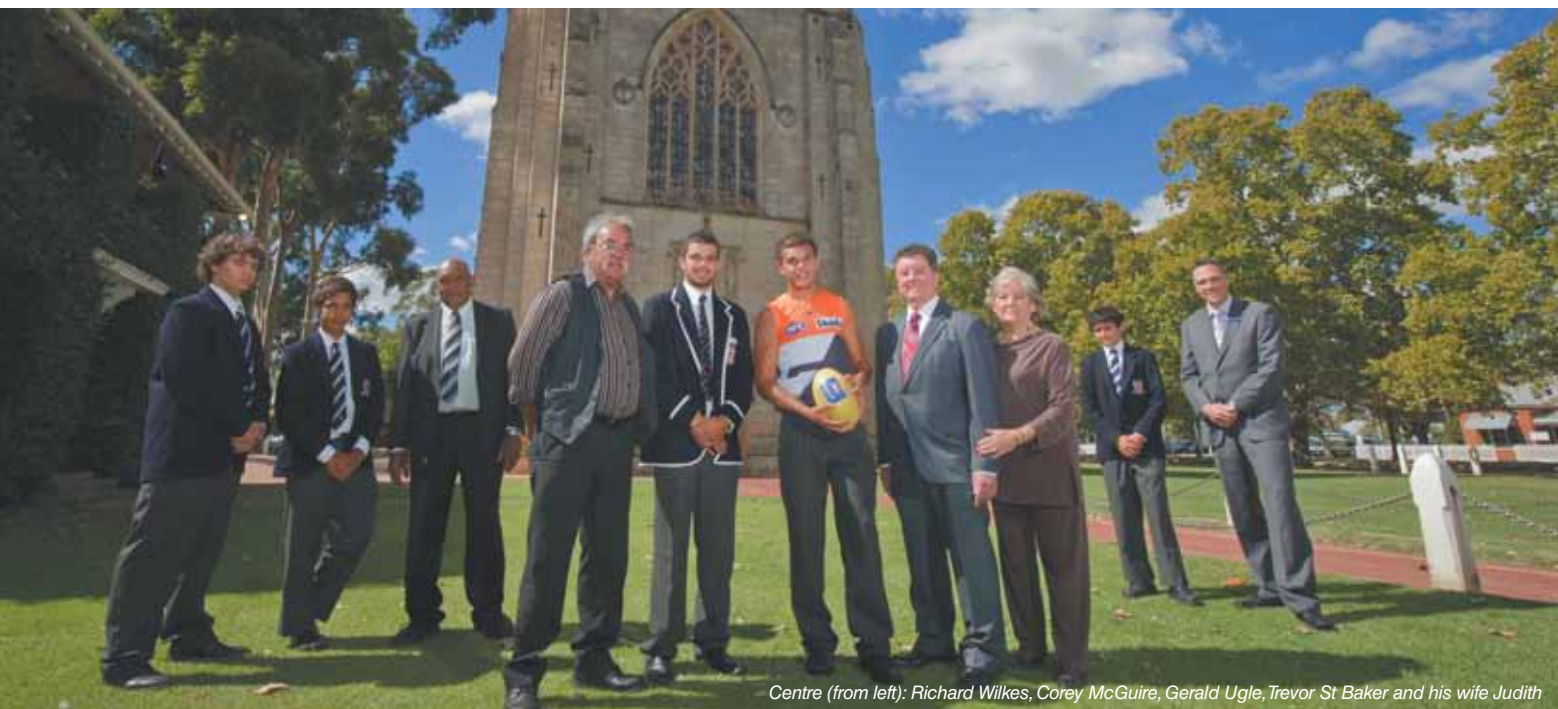
ERM Power is also heavily invested in the Wellington region and often undertakes local sponsorships. The Company was a major supporter of the Wellington Golf Club Pro Am Championships in 2011, sponsored the Wellington Eisteddfod and was heavily involved in Wellington Council's 'Building Our Future Together' community initiative.

Trevor St Baker and Richard Wilkes Indigenous Scholarship Foundation

ERM Power sponsors indigenous education through the Trevor St Baker and Richard Wilkes Indigenous Scholarship Foundation, which was established by ERM Power Chairman Trevor St Baker and the senior Elder of the Nyoongar people of southern Western Australia, Richard Wilkes.

The Foundation provides secondary and tertiary educational support for indigenous students in communities near ERM Power's projects in Western Australia, as well as offering them ongoing career support to enhance their futures.

The recipients of the first scholarships, Gerald Ugle and Corey McGuire, graduated from secondary college Guildford Grammar School in Perth in 2010 and were each awarded \$10,000 for their ongoing career development.



Centre (from left): Richard Wilkes, Corey McGuire, Gerald Ugle, Trevor St Baker and his wife Judith

Directors' Report for the year ended 30 June 2011

In accordance with the *Corporations Act 2001*, the directors of ERM Power Limited ("Company") report on the Company and the consolidated entity ERM Power Group ("Group"), being the Company and its controlled entities for the year ended 30 June 2011.

1. PRINCIPAL ACTIVITIES

The principal activities of the Group during the financial year were:

- its electricity sales;
- electricity generation development;
- generation asset ownership and operation; and
- gas exploration and development.

2. OPERATING RESULTS FOR THE YEAR

2.1. Revenue

Total revenue in FY2011 was \$550 million, which was 15% above the prospectus forecast of \$479 million and 32% above FY2010. Additional revenue was earned from holding the interest in the Kwinana power station for a month longer than forecast together with higher revenue earned in the rest of the Group.

Electricity sales business, ERM Sales, continued its strong growth with revenue 70% above the previous year at \$487 million, which was 13% above the prospectus forecast of \$429 million. This was despite the impact of severe flooding in Queensland, which left electricity sales volumes 6% below the forecast. Forward electricity sales are tracking to expectations and, as of 12 August 2011, 93% of the FY2012 electricity sales forecast of 8,499 gigawatt hours (GWh) was covered by existing sales contracts. This compares with 94% at the end of September 2010 in respect of the FY2011 sales forecast of 6,010 GWh, as reported in the prospectus.

Revenue from the Generation Assets business was \$47 million, which was 26% above the prospectus forecast of \$37 million. However it was 32% below the previous year because of the sale of the Group's interests in the Braemar 2 power station ("Braemar 2") in Queensland, and the Kwinana power station ("Kwinana") in Western Australia.

2.2. Profit

ERM Power's statutory profit after tax includes both gains from the sale of assets and the impact of unrealised changes in values of financial instruments, in both years.

The FY2011 year includes \$4.7 million made from the sale of the interest in Kwinana and the FY2010 year, \$36.4 million from the sale of the interest in Braemar 2.

The Group is required to value its forward electricity purchase contracts at market prices at each reporting date with changes between reporting dates recognised as unrealised gains or losses in the particular reporting period. The market value of corresponding sales contracts to which these purchase contracts relate are not permitted to be recognised, unless those contracts are regarded as onerous.

Accordingly, the directors of ERM Power believe that both EBITDAIF (earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments) and Underlying Net Profit after tax (statutory profit after tax adjusted for the impact of unrealised changes in fair values of financial instruments) provide the most meaningful indicators of its underlying business performance. EBITDAIF is one of the principal metrics used in the ERM Power prospectus dated 17 November 2010.

2.2.1. Statutory profit after tax for the year was \$16.2 million (FY2010: \$15.8 million loss).

These figures include net unrealised fair value gains on financial instruments of \$9.9 million in FY2011 and net unrealised fair value losses of \$26.1 million in the previous year, net of tax.

Note: The prospectus forecasts for statutory profit (NPAT) do not assume that there are any fair value adjustments during the forecast period.

The analysis of the major components of EBITDAIF below provides details of the underlying performance of ERM Power's businesses.

2.2.2 EBITDAIF for the full year (including profit of associate) was \$46.4 million (FY2010: \$68.7 million), which was 2% above the prospectus forecast of \$45.7 million.

The comparison with FY2010 is distorted by a net gain of \$36.4 million on the sale of the interest in Braemar 2 in the previous year.

ERM Sales' EBITDAIF increased by 138% to \$22.5 million (FY2010: \$9.5 million), which was 3% above the forecast of \$21.9 million despite reduced electricity load due to flooding in Central Queensland.

Generation Assets' EBITDAIF (including profit of associate) was \$28.9 million (FY2010: \$36.4 million), which was 10% above the forecast of \$26.2 million. The comparative period had some differences in the generation assets with commissioning of new power stations and disposals of others, as disclosed in the prospectus.

Group EBITDAIF was also affected by \$0.9 million of IPO costs that could not be deducted from equity as planned and have been expensed.

The EBITDAIF gain on the sale of the Kwinana interest differs from the prospectus (\$4.7 million against prospectus of \$6.6 million) due to a balance sheet tax credit which reported directly to the tax line.

2.2.3. Reconciliation of EBITDAIF and Underlying Profit with Statutory Profit

Underlying Profit is Statutory Profit after tax adjusted for the impact of unrealised changes in fair values of financial instruments and reflects the ongoing performance of the business. The following table reconciles EBITDAIF to Statutory Profit and then shows the impact of adjustments for financial instruments to arrive at Underlying Profit.

The reconciling items shown below are the unrealised changes in market values of financial instruments that the Group routinely enters into as part of risk management.

The Group enters into hedging arrangements that provide protection from electricity spot price risk, and also interest rate exposure. In respect of the financial instruments that provide the electricity price hedges, a Group subsidiary routinely enters into forward sales contracts ("Contracts") related to the provision of electricity in the Australian National Electricity Market ("NEM"). The Contracts are exclusively entered into with large industrial, commercial and government entities under term contracts. All of the electricity provided under these Contracts is traded in the NEM spot market. The subsidiary also enters into a variety of electricity derivative transactions ("Derivatives"), the objective of which is to create an economic hedge for the Contracts. Accounting standards have been interpreted to preclude recognition of the marked to market value of the Contracts in the financial statements and, as a result, only the unrealised after tax effect of the Derivatives is reflected in profit and loss.

\$ million	Actual FY2011A	Prospectus FY2011F	Actual FY2010A
EBITDAIF (incl. profit of associate)	46.4	45.7	68.7
Other Statutory Items			
Interest	(29.8)	(30.6)	(39.8)
Tax	(4.6)	(10.6)	5.3
Depreciation and amortisation	(10.0)	(10.8)	(12.7)
Financial instruments	14.2	32.8	(37.3)
	(30.2)	(19.2)	(84.4)
Statutory Profit after tax	16.2	26.5	(15.8)
Reconciling items			
Increase / (decrease) in fair value of financial instruments:			
ERM Sales	20.6	32.8	(30.8)
Disposal of Kwinana	(6.4)	-	-
Other	-	-	(6.5)
Total (before tax)	14.2	32.8	(37.3)
Tax effect on reconciling items	(4.3)	(9.9)	11.2
Less total reconciling items	9.9	23.0	(26.1)
Underlying Profit after tax	6.3	3.5	10.3

Directors' Report for the year ended 30 June 2011 continued...

2.3. Depreciation and amortisation

Total depreciation and amortisation charges for the year were slightly lower than forecast. Depreciation charges for the Neerabup power station ("Neerabup") are dictated by running time which varies depending on the extent to which the power station is called into operation. The current period charges were for Neerabup and Kwinana (part period) whilst the previous corresponding period charges were for Neerabup (part period), Kwinana and Braemar 2.

2.4. Net borrowing costs

Net finance charges for the year were slightly lower than forecast. The current and previous corresponding period charges reflect the different asset ownership referred to in the depreciation comment above and redemption costs on the Kwinana equity notes.

2.5. Cash flow

The following table compares actual cash flows for the year with those forecast in the prospectus.

\$ million	Actual FY2011A	Prospectus FY2011F
EBITDAIF (before profit of associate)	46.7	44.0
Change in working capital	0.4	(2.9)
Disposal profit on Kwinana	(4.7)	(6.6)
Distributions from Oakey	0.5	0.5
Tax paid	-	(1.1)
Net operating cash flows	42.9	33.9
Proceeds from issue of shares	93.9	93.9
Borrowing received in advance (Oakey)	4.4	-
Capital expenditure - projects	(13.1)	(25.4)
Capital expenditure - exploration	(4.9)	(5.4)
Net capital expenditure cash flows	80.3	63.1
Repayment of project borrowings	(3.3)	(3.4)
Repayment of corporate borrowings	(8.0)	(8.0)
Net project cash flows	69.0	51.7
Net proceeds from assets sales - Braemar 2	41.0	40.8
Net proceeds from assets sales - Kwinana	8.9	9.9
Kwinana cash reserve accounts	(10.2)	(8.8)
Net cash acquired on acquisition	0.4	-
Net interest paid	(28.2)	(28.3)
Financing and investing cash flows	11.9	13.6
Net increase in cash	123.8	99.2
Closing cash balances		
Free cash held in ERM Power	105.1	69.2
Free cash held in projects	5.1	8.1
Total free cash	110.2	77.3
Restricted cash	76.2	84.5
Total closing cash balances	186.4	161.8

\$ million	Actual FY2011A	Prospectus FY2011F
Operating cash flow on a statutory basis	109.3	100.4
Arrow Energy receivable included in receipts from customers	(66.4)	(66.4)
Operating cash flows above	42.9	33.9

The Group's cash balances increased by \$123.8 million to \$186.4 million over the financial year.

Net surplus operating cash flows show a \$9.0 million improvement in the prospectus forecast. The difference is largely due to higher earnings, the use of tax losses and changes in working capital. The statutory cash flow contained in the Annual Financial Statements shows the \$66.4 million received from Arrow Energy as revenue as it was received during the year. A reconciliation of operating cash flows on a statutory basis to the operating cash flows presented above is contained in the preceding table.

Capital expenditure was \$12.8 million below prospectus forecast principally due to development costs being incurred at a slower rate. In addition, \$4.4 million of a \$15.6 million facility arranged for the purchase of a further 50% interest in the Oakey power station ("Oakey") in FY2012 was received in advance on the last day of the current year.

2.6. Assets

During the year the Group disposed of its 30% interest in Kwinana. The sale contributed \$4.7 million to EBITDAIF.

The Group also received cash of \$66.4 million in respect of the sale of its interest in Braemar 2, the profit from which was accounted for in FY2010.

The Group acquired a further 50% interest in Oakey for \$61.7 million subsequent to balance date, increasing its interest to 62.5%. The results from Oakey will be consolidated in FY2012, having been equity accounted to date.

2.7. Debt

The Group's total debt reduced by 51% to \$211.7 million at 30 June 2011. \$207.3 million of this is the Neerabup project debt that has recourse only to Neerabup. \$4.4 million is part of a new facility arranged for part financing of the Oakey acquisition.

Corporate loans of \$33.1 million were repaid during the year and Neerabup repaid a total of \$5.3 million of its project debt. The Kwinana project debt was eliminated on the sale of that asset.

3. BUSINESS STRATEGIES AND PROSPECTS

The Group's business activities, strategies, underlying performance, balance sheet and growth prospects are consistent with the prospectus dated 17 November 2010.

During the last five years the Group has diversified and strengthened its business model across the value chain. The Group is now actively involved in gas exploration and development, electricity generation development, ownership and operation, and the sale of electricity to commercial, industrial and government customers. It is expected that the Group's growth, diversification and vertical integration will continue at a steady pace for the foreseeable future. In FY2011 the Group's gas business had its second successive commercial gas discovery in as many years; its electricity sales business grew by more than [50%] as forecast, as it expands Australia wide; our generation assets performed to expectation; the Group's generation development business continued to position itself to maintain its leadership in Australia as the leading developer of low emission gas fired power generation. In FY2012, the Group expects to maintain growth rates in electricity sales, advance major power generation projects, increase ownership of generation assets and associated earnings and profits, and advance commercialisation of the two gas discoveries ready for gas sales to major customers.

The Group's strategic intent over the next five years, as we strengthen the business model through vertical integration, is to continue to deliver growth, profits and long term value creation for shareholders. The Group aims to emerge in this time as one of Australia's top five integrated energy businesses and a preferred supplier to Australia's large commercial, industrial and government customers.

Directors' Report for the year ended 30 June 2011 continued...

4. SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

The Company was admitted to the Official List of the Australian Securities Exchange in December 2010 as the result of an initial public offering that raised \$100 million in new capital.

The Group sold its interests in the Kwinana and Braemar 2 power stations during the year, but continues to operate Kwinana on behalf of its owners.

5. EVENTS AFTER BALANCE DATE

On 1 July 2011, the Company completed the purchase of an additional 50% interest in the 332 megawatt Oakey Power Station ("Oakey"). With the completion of this transaction, the Company's beneficial interest in Oakey has increased from 12.5% to 62.5%. A corporate facility of \$16 million was arranged to partly fund the acquisition.

6. LIKELY DEVELOPMENTS AND EXPECTED RESULTS

The Federal Government announced their intention to introduce a Carbon Tax from July 2012. As one of Australia's leading developers of low emission electricity solutions and a successful gas explorer, the Group is favourably positioned for a carbon signal:

- Our gas and gas generation businesses will get a natural benefit from a carbon price as gas-fired; and generation has approximately half the emissions of coal
- The electricity sales business is not expected to be adversely affected due to our purchase and sales contracts allowing for pass through of carbon policy impacts.

In summary ERM Power's business plan does not rely on the introduction of a carbon signal but the Company is well placed if one is introduced.

Apart from that provided above, information as to likely developments in the operations of the Group and the expected results of those operations in subsequent financial years has not been included in this report because the directors believe this could result in unreasonable prejudice to the Group.

7. PROCEEDINGS ON BEHALF OF THE COMPANY

No person has brought, or intervened in, on behalf of the Company with, an application for leave under section 237 of the *Corporations Act (2001)*.

8. DIVIDENDS

No dividends were declared or paid during the year (2010: nil).

Subsequent to year end, the directors have declared a final dividend in respect of the 2011 financial year as follows:

Amount:	3.5 cents per share
Franking:	Fully franked
Date payable:	19 October 2011

9. SHARE OPTIONS

9.1. Unissued shares

As at the date of this report, there were 11,444,518 options to acquire fully paid ordinary shares on issue. The options do not carry any entitlement to participate in any share issue of the Company. All options expire on the earlier of their expiry date, or for those showing a 2017 expiry date, termination of the holder's employment, or as otherwise determined by the Board.

Expiry Date	Issue price of shares	Number of option
6 June 2013	80.6 cents	9,655,412
30 June 2013	80.6 cents	250,000
1 November 2017	275.0 cents	1,296,400
8 November 2017	275.0 cents	242,706

9.2. Shares issued on the exercise of options

209,203 ordinary shares were issued during the financial year on the exercise of options which had been granted in June 2008, with consideration of \$0.806 per share.

No amounts are unpaid on any of the shares.

10. Directors and company secretaries

DIRECTORS

The directors of the Company during the financial year and up to the date of this report are:

Trevor St Baker	Non-Executive Chairman
Anthony (Tony) Bellas	Independent Non-Executive Director
Martin Greenberg	Independent Non-Executive Director
Brett Heading	Independent Non-Executive Director (appointed 12 October 2010)
Antonino (Tony) Iannello	Independent Non-Executive Director (appointed 19 July 2010)
Philip St Baker	Managing Director

INFORMATION ON DIRECTORS AND COMPANY SECRETARIES

Trevor St Baker

BEng, BA, MAICD, FAusIMM, FIEAust, FAIE

Trevor founded the Group in 1980. He was Executive Chairman from July 2006 and was appointed Non-Executive Chairman in June 2009. He has more than 50 years of experience in the electricity industry. He is the ERM Power representative on the Electricity Supply Association of Australia, Chairman of the Board of the National Generators' Forum in Australia and is on the Board of the Queensland Resources Council.

Trevor has been a Director of Oakey Power Holdings Pty Ltd since 2000 and Chairman of the operating committees of each of NewGen Neerabup since 2007, NewGen Braemar 2 since 2008 (until its divestment in June 2011) and NewGen Power Kwinana since 2005 (until its divestment in October 2010). In June 2010, Trevor accepted the position of Non-Executive Chairman of Master Electricians Australia, and in September 2010 co-founded the Trevor St Baker & Richard Wilkes Indigenous Scholarship Foundation, of which he is the Managing Director.

Anthony (Tony) Bellas

MBA, BEc, DipEd, CPA, FAIM, MAICD.

Tony was appointed as a Non-Executive Director in December 2009, bringing to the business almost 25 years of policy and operational experience in the energy industry. Tony was previously CEO of the Seymour Group, one of Queensland's largest private investment and development

companies. Prior to joining the Seymour Group, Tony held the position of CEO of Ergon Energy, a Queensland Government-owned corporation involved in electricity distribution and retailing in Queensland. Before that, was CEO of CS energy, also a Queensland Government-owned corporation and the State's largest electricity generation company, operating over 3,500 MW of gas-fired and coal-fired plant at four locations.

He is a director of the listed companies shown below and is also a director of Australian Water Queensland Pty Ltd, Gasfields Water Management Pty Ltd and QIP Coal Pty Ltd.

Other listed company directorships in the last three years

Corporate Travel Management Limited	Since June 2010
Guilford Coal Limited	Since December 2010
Watpac Limited	(December 2007 – October 2010)

Special Responsibilities

Chairman of the Audit and Risk Committee, and a member of the Remuneration Committee and the Nomination Committee.

Martin Greenberg

BBus, DipCom, FCPA, JP

Martin was appointed as a Non-Executive Director in July 2007, bringing finance credentials and business experience spanning 35 years. Martin has been a director of several public companies in Australia and New Zealand and has an extensive range of national and international contacts and experience, accumulated over the past 35 years.

Martin is currently the Managing Director of Apollan Investments Group, a Sydney based company specialising in venture capital, corporate finance, securities, and general investment. He is also the current Chairman of Selector Funds Management Ltd, Aimedics Pty Ltd and Liquid Capital Management (Australasia) Pty Ltd.

Special Responsibilities

Member of the Audit and Risk Committee, the Remuneration Committee and the Nomination Committee.

Antonino (Tony) Iannello

BCom, FCPA, FAICD, SFFSIA, Harvard Business School Advanced Management Program

Tony was appointed as a Non-Executive Director in July 2010, bringing to the business more than 30 years of banking and energy experience.

Directors' Report for the year ended 30 June 2011 continued...

He is a director of the listed companies shown below, a director of HBF Health Ltd and MG Kailis Group Intium Energy Ltd, Harrier Resourcing People Pty Ltd and a member of The Murdoch University Senate. Prior to embarking on a career as a non-executive director, Tony was the Managing Director of Western Power Corporation until its separation into four separate businesses. Previously he held a number of senior executive positions at BankWest.

Other listed company directorships in the last three years

Energia Minerals Limited	Since March 2010
SP Ausnet*	Since June 2006
Aviva Corporation Limited	(February 2008 – November 2010)

*The SP Ausnet "stapled group" of companies comprises SP Australia Networks (Distribution) Ltd, SP Australia Networks (Transmission) Ltd & SP Australia Networks (Finance) Trust.

Special Responsibilities

Chairman of the Nominations Committee and the Remuneration Committee and member of the Audit and Risk Committee.

Brett Heading

BCom, LLB (Hons), FAICD

Brett was appointed as a Non-Executive Director in October 2010. He has specialized in corporate law for 25 years, including mergers and acquisitions, capital raising, ASX listings and advising boards of listed and unlisted public companies and government-owned corporations. He has been a partner of McCullough Robertson Lawyers since 1985 and was appointed Chairman of Partners in 2004.

Brett has been a director of the listed companies shown below and a number of unlisted companies. He has also held roles on Federal Government boards, having been a longstanding member of the Takeovers Panel (1998 to 2009) and the Board of Taxation (2000 to 2009).

Other listed company directorships in the last three years:

ChemGenex Pharmaceuticals Limited	Since June 2002
Trinity Limited	Since August 2009
Diversa Limited (previously Ambri Limited)	(November 2006 – July 2008)
Capilano Honey Limited	(July 2008 – October 2008)
Australian Agricultural Company Limited	(June 2008 – June 2009)

Special Responsibilities

Member of the Nominations Committee and the Remuneration Committee

Philip St Baker

BEng, MAICD

Phil was appointed as Managing Director and CEO in July 2006 and is focused on the long term growth and prosperity of the Group. Phil has over 20 years of diversified international experience in the resources and energy industry including exploration, mining, processing, smelting, refining, power and gas. Over the last five years, Phil has utilized his extensive experience in transforming the Group from an emerging power development business into one of Australia's leading diversified energy businesses. Previously, Phil had a 15 year career with BHP, where he progressed to the role of Global Maintenance Manager, supporting BHP's 100+ businesses worldwide. For five years, Phil led an international team tasked with facilitating operating business improvement across the entire group. Prior roles also include Vice President of Queensland Nickel QNI and CEO of NewGen Power.

Special Responsibilities

Chairman of the ERM Sales and ERM Gas subsidiary Boards and chairman of the Health, Safety, Environment and Sustainability Committee of the ERM Power Board.

COMPANY SECRETARIES

Peter Jans

LLB (Hons), MA

Peter joined the Group in July 2007 and was appointed as Company Secretary in March 2008. He is an affiliate of the Institute of Chartered Secretaries, a member of the Queensland Law Society, Barrister and a Solicitor of the Supreme Court of Victoria and a Solicitor of the Supreme Court of Queensland and the High Court of Australia. He has practised as a lawyer for over 30 years in the corporate, property, international investment, energy and resource sectors. After an active career in private practice, Peter became General Counsel of CS Energy in the late 1990s and was involved in major electricity generation projects, including Callide C, Swanbank E and Kogan Creek. Peter was General Counsel and Company Secretary of Queensland Gas Company Limited from April 2005 until July 2007, during which period the company transformed from junior explorer to a major gas producer.

Special Responsibilities

Peter's role and responsibility covers the whole of ERM Power's broader business plans and portfolios, including business development, construction and operations, sales and gas activities. Peter is responsible for all aspects of ERM Power's legal dealings, and for compliance and corporate governance.

Graeme Walker

BCom, CA, CA (SA), FAICD

Graeme joined the Group in April 2009 and was appointed as joint Company Secretary in December 2009. As Chief Financial Officer, Graeme is also responsible for the financial management and control of ERM Power.

Graeme has served as CFO of a number of major ASX-listed companies in the resources sector, including Normandy Mining Limited and Ampolex Limited, where he was involved in significant business growth and corporate activity. He subsequently provided consulting services to a number of companies, advising on financial and commercial services, as well as interim management. During this time he was also involved in the listing of a number of resource companies, as a non-executive director.

11. MEETINGS OF DIRECTORS

The number of meetings of the Board of directors and each Board committee held during the financial year, and the numbers of meetings attended by each director are as follows:

Director	Board Meetings		Audit & Risk Committee		Nominations Committee		Remuneration Committee	
	A	B	A	B	A	B	A	B
Trevor St Baker	18	20	**	**	**	**	**	**
Tony Bellas	19	20	5	5	0	0	2	2
Martin Greenberg	19	20	4	5	0	0	2	2
Brett Heading	13	16	**	**	0	0	1	2
Tony Iannello	19	20	5	5	0	0	2	2
Philip St Baker	19	20	**	**	**	**	**	**

A = number of meetings attended

B = number of meetings held during the time the director held office during the year

** = not a member of the relevant committee

The Group has a Health, Safety, Environment & Sustainability Committee. Committee members include the Managing Director and other senior management. This committee met four times during the financial year.

12. DIRECTORS' INTERESTS

The relevant interest of each director in the share capital of the Company at the date of this report, as notified by directors to the ASX in accordance with Section 205G of the *Corporations Act*, is as follows:

Director	Ordinary shares	Options to acquire ordinary shares
Trevor St Baker	84,704,918	-
Tony Bellas	100,000	-
Martin Greenberg	571,794	354,726
Brett Heading	14,285	-
Tony Iannello	114,285	-
Philip St Baker	4,013,734	1,076,576

Directors' Report for the year ended 30 June 2011 continued...

13. ENVIRONMENTAL REGULATION AND PERFORMANCE

The Group's environmental obligations are regulated by relevant federal, state and local government ordinances. The Group's policy is to comply with, but in most cases exceed its environmental performance obligations. No environmental breaches have been notified by any governmental agency or local council authority during the year ended 30 June 2011.

The Group is subject to the reporting requirements of the *Energy Efficiency Opportunities Act 2006* and shortly expects to be subject to the *National Greenhouse and Energy Reporting Act 2007*. The *Energy Efficiency Opportunities Act 2006* requires the Group to assess its energy usage, including the identification, investigation and evaluation of energy saving opportunities, and to report publicly on the assessments undertaken, including what action the Group intends to take as a result. The Group continues to meet its obligations under this Act.

The *National Greenhouse and Energy Reporting Act 2007* would require the Group to report its annual greenhouse gas emissions and energy use. The Group has implemented systems and processes for the collection and calculation of the data required.

14. INDEMNIFICATION AND INSURANCE OF OFFICERS

Insurance and indemnity arrangements are in place for directors and officers of the Group. Disclosure of premiums and coverage is not permitted by the contract of insurance.

To the extent permitted by law, the Group indemnifies every person who is or has been an officer against:

- any liability to any person (other than the Company, related entities or a major shareholder) incurred whilst acting in that capacity and in good faith; and
- costs and expenses incurred by that person in that capacity in successfully defending legal proceedings and ancillary matters.

For this purpose, "officer" means any company secretary or any person who makes, participates in making decisions that affect the whole, or a substantial part of the business of the Company or Group.

15. AUDITOR'S INDEPENDENCE DECLARATION

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 45.

16. NON-AUDIT SERVICES

Non-audit services provided by the Group's auditors PricewaterhouseCoopers were in relation to advice and certain agreed-upon procedures. The directors are satisfied that the provision of non-audit services is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*.

Amounts received or due and receivable by PricewaterhouseCoopers Australia for non-audit services:	2011 \$	2010 \$
Investigating accounts report	630,000	-
Due diligence services	60,000	-
Other agreed-upon procedures in relation to the entity and any other entity in the consolidated Group	115,002	-
	805,002	-

17. CHANGE IN COMPANY NAME

On 17 September 2010, ERM Power Pty Ltd changed its name to ERM Power Limited.

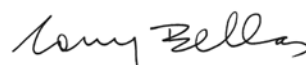
18. ROUNDING OF AMOUNTS

The amounts contained in this report and in the financial report have been rounded to the nearest thousand dollars (where rounding is applicable) under the option available to the Group and the Company under ASIC Class Order 98/0100. The Group and the Company are entities to which the class order applies.

19. REMUNERATION REPORT

The Remuneration Report is attached and forms part of this report.

This report is made in accordance with a resolution of directors.



Tony Bellas
Director

Brisbane

25 August 2011

Remuneration Report

for the year ended 30 June 2011

The directors present the Remuneration Report for ERM Power Limited (“Company”) and its consolidated entities (“Group”) for the year ended 30 June 2011.

1. REMUNERATION FRAMEWORK

1.1. Role of the Remuneration Committee

The Remuneration Committee ensures that the remuneration of directors and senior executives is consistent with market practice and sufficient to ensure that the Company can attract, develop and retain the best individuals. The committee reviews directors’ fees, and remuneration of the Managing Director and senior executives against the market and against Group and individual performance.

The committee oversees governance procedures and policy on remuneration including:

- General remuneration practices;
- Performance management;
- Equity plans and incentive schemes, and
- Recruitment and termination.

Through the committee, the Board ensures the company’s remuneration philosophy and strategy continues to be designed to:

- attract, develop and retain top class Board and executive talent,
- create a high performance culture by driving and rewarding executives for achievement of the Company’s strategy and business objectives, and
- link incentives to the creation of shareholder value.

In undertaking its work, the committee seeks the advice of external remuneration consultants.

1.2. Key Management Personnel

Key Management Personnel (“KMP”) are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director of that entity. The term KMP refers to the following persons who were KMPs during the financial year, and who were also the five highest remunerated executives. Unless otherwise indicated, they were KMPs for the entire year.

1.2.1. Non-Executive directors

Trevor St Baker	Chairman
Tony Bellas	Independent
Martin Greenberg	Independent
Brett Heading	Independent (appointed 12 October 2010)
Tony Iannello	Independent (appointed 19 July 2010)

1.2.2. Executive director

Philip St Baker	Managing Director and Chief Executive Officer
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1.2.3. Senior executives

William (Mitch) Anderson	Chief Executive Officer – ERM Sales
Peter Jans	Group General Counsel & Company Secretary
Derek McKay	Chief Executive Officer – Generation Operations
Graeme Walker	Chief Financial Officer

2. REMUNERATION

2.1. Fees payable to Non-Executive Directors

Fees paid to non-executive directors reflect the demands which are made on, and the responsibilities of, directors. Directors’ fees are reviewed annually by the Board. Directors who chair or are members of a committee receive additional fees for these services.

The Board considers the advice of independent remuneration consultants to ensure directors’ fees are appropriate and in line with the market. The Chairman’s fees are determined independently to the fees of directors and are based on comparative roles in the market. The Chairman is not present at any discussions relating to the determination of his remuneration.

The current fees were reviewed prior to the IPO. During the year, the responsibilities of the ERM Power Retail Pty Ltd Board were assumed by the full Board – the fees of \$10,000 per annum previously paid to each non-executive director of the ERM Power Retail Pty Ltd Board were eliminated, and base fees to directors of the ERM Power Board increased by \$5,000 per annum. Directors’ fees are determined within an aggregate fee pool limit approved by shareholders. This is currently set at \$800,000 per annum and was approved by shareholders at the annual general meeting held on 7 June 2010.

Remuneration Report for the year ended 30 June 2011 continued...

The annual fee structure for non-executive directors, excluding superannuation, is as follows:

Base fee		\$
Chairman	205,000	
Non-executive directors	105,000	
Additional fees		\$
Audit Committee - Chairman	20,000	
Audit Committee - Member	10,000	
Remuneration Committee - Chairman	10,000	
Remuneration Committee - Member	5,000	
Chairman of Partnership Committee or subsidiary	10,000	

The tables at the end of this report provide details of fees paid during the financial year to each non-executive director.

2.2. Managing Director and Senior Executives

The objective of the Company's executive remuneration framework is to ensure that reward for performance is competitive and appropriate for the results delivered. The framework aligns executive remuneration with the achievement of strategic objectives and the creation of the value for shareholders, and conforms with market practice. The Board ensures that executive reward satisfies the following key criteria for good reward governance practices:

- Competitiveness and reasonableness;
- Acceptability to shareholders;
- Performance linkage/alignment of executive remuneration; and
- Transparency.

Senior executives are remunerated by way of a mix of fixed and variable remuneration in a manner that motivates them to pursue the long term growth and success of the Group. The components of remuneration are:

- Base pay and benefits, including superannuation;
- Short-term performance incentives;
- Long-term incentives; and
- Other cash or equity based discretionary incentives.

As detailed in the remuneration table, incentives were awarded in the current financial year in respect of financial results and the delivery of key outcomes in the 2010 financial year. Additional incentives were also awarded containing continuity of service vesting conditions, targeting employee retention beyond the IPO period. Future long term incentives to be offered will incorporate performance conditions to be set by the Board to reflect the competitive market and business conditions when it is in the interest of

the company and shareholders to do so. As the Company's shares were listed for the first time on the ASX in December 2010, no incentive award has yet been made that contain performance conditions linked to share price.

2.3. Base Pay and benefits

External remuneration consultants provide analysis and advice to ensure executive remuneration is set to reflect the market for comparable roles. Remuneration is reviewed annually to ensure that it is competitive with the market. Remuneration is also reviewed on promotion or change of role. There are no guaranteed base pay increases included in executive contracts. Executive remuneration includes salary continuance insurance.

The tables at the end of this report provide details of remuneration paid during the financial year to the Managing Director and each of the named executives.

2.4. Incentive schemes

Variable remuneration is in the form of short ("STI") and long term ("LTI") incentives which represent "at risk" remuneration. STI remuneration is paid annually against agreed and objective KPIs which are designed to align the interests of the Company and its shareholders. LTI remuneration will be accrued over a number of years and earned through satisfaction of performance and service conditions. Achievements are assessed annually using the ERM Performance Appraisal and Development Review process.

STI payments are in the form of cash or equity, or a combination of these. LTI payments are in the form of equity.

The trading of equities which vest under STI or LTI are required to comply with the Company's Securities Trading Policy. This policy also prohibits any employees or directors from entering into any scheme, arrangement or agreement under which the economic benefit derived by the employee or director, in relation to an equity-based incentive award or grant made by the Company is altered, irrespective of the outcome under that incentive award or grant, other than as permitted in any approved share or option plan, or as authorized by the Board.

For employees, benefits associated with the incentive scheme include:

- Provision of clear targets, stretch targets and structures for achieving rewards;
- Recognition and reward for achievement, capability and experience; and
- Delivery of reward for contribution to growth in shareholder wealth.

For shareholders, benefits associated with the incentive scheme include:

- A clear focus on performance improvement at all levels of the Group, with year-on-year profit growth a core component;
- A focus on sustained growth in shareholder wealth, consisting of dividends and share price growth and delivering the greatest returns on assets; and
- The ability to attract and retain high calibre executives.

Key performance indicators (“KPI”) for both short and long term incentives are annually assessed and approved by the Board. The KPIs include both financial and non-financial conditions under a balanced scorecard approach, and reflect the key measures of success as determined by the Board. These may include, but are not limited to, a range of measures such as:

- Zero Harm – safety and environment performance measures, including lost time and medically treated injury frequency rates;
- Financial Measures – including earnings before interest, tax, depreciation, amortisation and net fair value changes in financial instruments (EBITDAF), cash flow management etc.; and
- Market based – shareholder returns, earnings per share, share price improvement, etc.

2.4.1. Short term incentives

Short term incentives (“STI”) are provided to Senior Executives and most employees.

At the beginning of each year, the remuneration committee determines the Group key performance indicators (“KPI”), and sets target and stretch target levels. KPIs and target and stretch targets are also set at this time for business units and individuals.

A weighting is applied to each of the target components (Group, business unit and individual performance) with the average performance against target and stretch target measured at the end of the year to provide a target achievement score. The target achievement score is applied to an STI opportunity level. STI opportunity levels are predetermined percentages of average fixed remuneration set by the remuneration committee with the levels determined by employees’ roles and relative influence on the Group’s performance.

STI opportunity levels are currently set in range of 10% to 40% of average fixed remuneration, with the stretch target potential to achieve up to 150% of these levels (i.e. 15% to 60%).

STIs are assessed annually using the ERM Performance and Development Review process. They are paid following completion of the Group’s audited accounts, and may be offered by way of cash or equity (through an equity incentive plan), or a combination of the two. They are only payable to individuals who are employees at the time that the STI is payable. Employees whose employment is terminated during the financial year due to retrenchment, retirement on the grounds of age or invalidity, or death may be paid on a pro-rata basis, and in other circumstances, at the discretion of the Board.

In respect of the FY10 incentives, paid in the 2011 financial year, KPIs were set and paid prior to listing on the ASX. They were focused on aligning employees with the strategic goals and performance of the Group. The Group KPIs were in the following categories:

- Safety;
- Profit;
- Value (based on movement in annual independent valuations); and
- Cash levels.

The performance categories established post listing have continued to focus on the achievement of strategic objectives and the creation of value for shareholders. The weighting given to each performance objective category will vary for each executive depending upon their role within the Group. For the FY11 incentives to be paid in the 2012 financial year, KPIs were established within the following categories:

- Operational (safety and compliance);
- Financial and prospectus forecasts;
- Growth;
- People; and
- Strategic.

All executives had as an objective, the achievement by the Group of the forecast strategies and results as outlined in the Prospectus. The ERM P&DR is used to measure the actual level of achievement of each objective in the financial year.

2.4.2. Other incentives

Prior to listing, the Company awarded a discretionary incentive award to certain employees for achieving the successful Initial Public Offering (“IPO”). The vesting conditions are targeted at the retention of those employees through to at least September 2012, being the prospectus forecast period.

Remuneration Report for the year ended 30 June 2011 continued...

Also prior to listing, the Company awarded a discretionary incentive to key staff, to encourage retention beyond the IPO forecast period.

Neither of the above awards included performance conditions and were awarded by way of participation in the long term equity plans (the LTIST and LTIOT).

2.4.3. Long-term incentives

The Company may issue long-term incentives to certain employees to provide incentives to focus on long term shareholder returns.

These incentives will be in the form of equity which will only vest if certain performance measures, yet to be established are met and the employees are still employed at the end of the vesting period.

The first issue under the long term incentive scheme is anticipated to occur in the 2012 financial year with vesting to be subject to the achievement of appropriate performance measures to be set by the Board, and time.

3. Service agreements

On appointment, all non-executive directors are issued with a letter of appointment which summarises board policies and terms.

Remuneration and other terms of employment for the Managing Director and the other key management personnel are formalized in service agreements. Each of these agreements specify the components of remuneration to which they are entitled and outline base salary, the provision of incentives, and other benefits including superannuation and salary continuance insurance.

Service terms for the Managing Director and senior executives are as follows:

Name	Term of agreement	Base salary excluding superannuation @ 9%*	Termination benefits **
Philip St Baker (Managing Director & CEO)	On-going (no fixed term)	\$494,400	12 months base salary
Mitch Anderson (CEO - ERM Sales)	On-going (no fixed term)	\$325,000	6 months base salary
Peter Jans (Group General Counsel and Company Secretary)	On-going (no fixed term)	\$325,686	6 months base salary
Derek McKay (CEO – Generation Operations)	On-going (no fixed term)	\$325,000	6 months base salary
Graeme Walker (Chief Financial Officer)	On-going (no fixed term)	\$283,250	6 months base salary

* Base salaries quoted are for the year ended 30 June 2011; they are reviewed annually by the remuneration committee.

** Termination benefits are payable at the option of the company in lieu of notice, other than termination for cause.

4. Share price and consequences of performance on shareholder wealth

ERM's executive remuneration is directly linked to the performance of the Company across a range of measures. The STI is focused on achieving annual profit and operational targets, while the LTI is focused on achieving long term growth and retention of talented executives. The Board considers this combination an effective way to align incentives to shareholder value.

The Company's shares were listed on the ASX in December 2010 at a listing price of \$1.75. The table below shows ERM's operating revenue, EBITDAIF, and NPAT for the current reporting year vs prospectus, and the effect of ERM's performance on shareholder value.

		2011 Actual	2011 Prospectus Forecast
Revenue and other income	(\$'000)	549,814	478,916
EBITDAIF ¹	(\$'000)	46,407	45,665
Net Profit After Tax (NPAT)	(\$'000)	16,219	26,474
Underlying Net Profit After Tax	(\$'000)	6,288	3,488
Basic Earnings per Share		11.72 cents	16.6 cents
Dividends in respect of financial year		3.5c per share	3.5c per share
Closing share price as at 30 June 2011		\$1.57	

¹ EBITDAIF (after profit of associate) includes profits from ERM Power's ownership interest in the Oakey power station.

5. Remuneration and other tables

5.1 Remuneration table for year ended 30 June 2011

Details of the remuneration of directors and key management personnel of the Group for the financial year, which include the five highest remunerated executives, are set out in the following table:

	Cash salary and fees \$	Short term benefits			Post-employment benefits	Long term benefits	Long term equity based benefits		Total \$
		Additional fees ¹ \$	Cash bonus ² \$	Non monetary benefits ³ \$	Super-annuation \$	Termination Benefits \$	Shares ⁴ \$	Options ⁵ \$	
Non-executive directors									
Trevor St Baker	229,792	-	-	-	20,681	-	-	-	250,473
Tony Bellas	127,292	27,523	-	-	13,933	-	-	-	168,748
Martin Greenberg	121,875	9,174	-	-	11,794	-	-	5,301	148,145
Brett Heading (appointed 12 October 2010)	78,905	-	-	-	-	-	-	-	78,905
Tony Iannello (appointed 19 July 2010)	123,541	9,174	-	-	11,944	-	-	-	144,660
Total	681,405	45,872	-	-	54,225	-	-	-	790,931
Executives									
Philip St Baker (Managing Director & CEO)	494,400	-	80,005	1,444	44,496	-	150,926	21,346	792,617
Mitch Anderson	325,000	-	-	5,372	29,250	-	143,623	13,956	517,201
Peter Jans	325,686	-	-	2,221	29,312	-	161,103	10,828	529,150
Derek McKay	325,000	-	-	2,221	29,250	-	123,809	7,726	488,006
Graeme Walker	283,250	-	-	1,966	25,493	-	124,867	3,478	439,054

¹ Fees paid for additional roles undertaken in the initial public offering.

² The FY10 bonus paid to the Managing Director in the current year consisted of both cash and share based payments for which a general provision had been provided for in the FY10 accounts. (Although a general provision has been made for incentive payments for FY11, to be paid in FY12, the allocation for payments to specific individuals and the form, whether to be taken in cash or equity, has not yet been determined.)

³ Non monetary benefits include salary continuance insurance premiums and FBT.

⁴ Issue of shares as the result of awards under equity incentive schemes, in addition to a bonus awarded in connection with the initial public offering. A general provision was made in the FY10 accounts, but the allocation to individuals was only calculated at the time of grant in the current FY.

⁵ Issue of options under equity incentive schemes based on the value of options expensed during the year (Non-executive director options granted FY08, executive options granted in FY08 and the current year).

Remuneration Report for the year ended 30 June 2011 continued...

5.2 Remuneration table for year ended 30 June 2010

Details of the remuneration of directors and key management personnel of the Group for the prior financial year, which include the five highest remunerated executives, are set out in the following table:

	Cash salary and fees \$	Short term benefits		Post-employment benefits	Long term benefits	Long term equity based benefits		Total \$
		Cash bonus ¹ \$	Non monetary benefits ² \$	Super-annuation \$	Termination Benefits \$	Shares \$	Options ³ \$	
Non-executive directors								
Trevor St Baker	269,006	-	-	5,310	-	-	-	274,316
Tony Bellas	73,333	-	-	6,600	-	-	-	79,933
Martin Greenberg	137,500	-	-	-	-	-	5,301	142,801
Brett Heading (appointed 12 October 2010)	-	-	-	-	-	-	-	-
Tony Iannello (appointed 19 July 2010)	-	-	-	-	-	-	-	-
Wayne St Baker (ceased 30 June 2010)	120,000	-	-	-	20,000	-	2,242	142,242
Total	599,839	-	-	11,910	20,000	-	7,543	639,292
Executives								
Philip St Baker (Managing Director & CEO)	480,000	-	1,444	43,200	-	-	12,461	537,105
Mitch Anderson	277,900	-	4,719	25,011	-	-	9,966	317,596
Peter Jans	310,000	-	1,444	27,506	-	-	6,829	341,406
Derek McKay	261,187	-	1,444	23,507	-	-	3,736	289,874
Graeme Walker	275,000	-	1,909	24,750	-	-	-	301,659

¹ No cash bonus paid in FY10.

² Non monetary benefits include salary continuance insurance premiums and FBT.

³ Issue of options under equity incentive schemes based on the value of options expensed during the year which were granted in FY08.

5.3 Relative Proportion of Remuneration

The relative proportion of remuneration that was linked to performance and those that were fixed are as follows:

Name	Fixed Remuneration		At Risk – Cash Bonus and Shares Issued		At Risk – Options	
	2011 %	2010 %	2011 %	2010 %	2011 %	2010 %
Non-executives directors						
Trevor St Baker	100	100	-	-	-	-
Tony Bellas	100	100	-	-	-	-
Martin Greenberg	96	96	-	-	4	4
Brett Heading (appointed 12 October 2010)	100	-	-	-	-	-
Tony Iannello (appointed 19 July 2010)	100	-	-	-	-	-
Wayne St Baker (ceased 30 June 2010)	-	98	-	-	-	2
Executives						
Philip St Baker	68	98	29	-	3	2
Mitch Anderson	70	97	27	-	3	3
Peter Jans	68	98	30	-	2	2
Derek McKay	73	99	25	-	2	1
Graeme Walker	71	100	28	-	1	-

5.4 Share-based compensation

The terms and conditions of each grant of options affecting remuneration in the current or a future reporting period are as follow:

Grant date	Number of Options granted ¹	Number exercisable as at 30 June 2011	Vesting and exercise date	Expiry date	Exercise price ²	Value per option at grant date	Performance achieved	% Vested
1 Jun 2008	10,524,962	9,819,209	Vested 3 Nov 2010	6 Jun 2013	\$0.806	\$0.0448	N/A, service condition	100%
30 Jun 2008	400,000	250,000	Vested 3 Nov 2010	30 Jun 2013	\$0.806	\$0.0448	N/A, service condition	100%
1 Nov 2010	1,296,400	1,296,400	3 business days after 2012 Financial Statements are signed	1 Nov 2017	\$2.75	\$0.1043	N/A, service condition	N/A
8 Nov 2010	242,706	242,706	3 business days after 2012 Financial Statements are signed	8 Nov 2017	\$2.75	\$0.1043	N/A, service condition	N/A

¹ Options granted restated for 2 for 1 share split during FY2011.

² Options convertible into one ordinary share and carry no dividend or voting rights.

Remuneration Report for the year ended 30 June 2011 continued...

5.5 Details of option grants

Details of options to acquire ordinary shares in the Company provided as remuneration to each of the key management personnel are set out below. Further information on the options is set out in note 28 to the financial statements. No options were granted to any non-executive director of the Company in the current year.

Name	Number of options granted during the year	Value of options at grant date \$	Number of options vested during the year ¹	Number of options lapsed during the year	Value at lapse date
Non-Executive Directors of the Group					
Trevor St Baker	Nil	-	Nil	Nil	N/A
Tony Bellas	Nil	-	Nil	Nil	N/A
Martin Greenberg	Nil	-	354,726	Nil	N/A
Brett Heading	Nil	-	Nil	Nil	N/A
Tony Iannello	Nil	-	Nil	Nil	N/A
Key management personnel of the Group					
Philip St Baker (Managing Director & CEO)	242,706	25,314	833,870	Nil	N/A
Mitch Anderson	106,364	11,094	666,872	Nil	N/A
Peter Jans	106,590	11,117	457,010	Nil	N/A
Derek McKay	106,364	11,094	250,000	Nil	N/A
Graeme Walker	92,700	9,669	Nil	Nil	N/A

¹ Options issued in June 2008 vested on 3 November 2010.

5.6 Shares issued on the exercise of remuneration options

No ordinary shares were issued as a result of the exercise of remuneration options to any director or key management personnel during the financial year.

5.7 Details of remuneration: Bonuses and share-based compensation benefits

Name	Bonus		Share-based compensation benefits				
	Paid %	Forfeited %	Year Granted	Vested %	Forfeited %	Financial years in which options may vest	Maximum total value of grant yet to vest \$
Tony Bellas	100%	-	-	-	-	-	-
Martin Greenberg	100%	-	2008	100%	-	-	-
Tony Iannello (appointed 19 July 2010)	100%	-	-	-	-	-	-
Philip St Baker (Managing Director & CEO)	100%	-	2011	100%	-	-	-
			2011	-	-	2013	47,059
			2011	-	-	2014	73,045
			2008	100%	-	-	-
Mitch Anderson	100%	-	2011	100%	-	-	-
			2011	-	-	2013	20,348
			2011	-	-	2014	31,734
			2008	100%	-	-	-
Peter Jans	100%	-	2011	100%	-	-	-
			2011	-	-	2013	20,390
			2011	-	-	2014	31,801
			2008	100%	-	-	-
Derek McKay	100%	-	2011	100%	-	-	-
			2011	-	-	2013	20,348
			2011	-	-	2014	31,734
			2008	100%	-	-	-
Graeme Walker	100%	-	2011	100%	-	-	-
			2011	-	-	2013	17,732
			2011	-	-	2014	27,656

5.8 Loans to directors, employees and contractors

Information on loans to directors, employees and contractors including amounts, interest rates and repayment terms are set out in note 32 to the financial statements.

Corporate Governance Statement

Compliance with ASX Corporate Governance Principles and Recommendations

The ASX document, *'Corporate Governance Principles and Recommendations'* ('Guidelines') was published by the ASX Corporate Governance Council ("Council") with the aim of enhancing the credibility and transparency of Australia's capital markets. In August 2007 the Council released a revised version, featuring eight principles to apply to the first financial year starting on or after 1 January 2008.

In June 2010, the Council released further amendments to apply to listed entities in respect of their first financial year starting on or after 1 January 2011. Those amendments, relating to diversity, remuneration, trading policies and briefings, although not required disclosure for ERM Power Limited ('Company') in the 2011 Annual Report, have been adopted early by the Company as encouraged by the Council.

This statement summarises the Company's Corporate Governance practices which have been in place since the Company listed in December 2010. The Company is pleased to report that, with the exception of Principle 2.2 in relation to an independent director as Chairman, it complied with all of the ASX Guidelines.

The Board has assessed the Company's current practice against the Guidelines and outlines its assessment below.

Principle 1 – Lay solid foundations for management and oversight

The role of the Board and ability to delegate to management has been formalised in ERM Power's Board charter. The Board charter, along with other charters and policies, can be found on the Company's website. The charter is reviewed and amended from time to time taking into consideration practical experience gained in operating as an ASX listed company. The Company complies with this Principle of the Guidelines.

The Managing Director has made delegations to senior executives related to the Company's day to day affairs, within set limits and which delegations may be withdrawn or amended by the Managing Director at any time, within the following areas: Legal, Financial, ERM Sales matters, Operational matters, ERM Gas matters, Project Development, Asset Optimisation and Project Delivery.

At the time of joining the Company, directors and senior executives are provided with letters of appointment, together with key Company documents and information setting out

their term of office, duties, rights and responsibilities, and entitlements on termination.

The performance of all senior executives, including the Managing Director, is reviewed annually against:

- a) a set of personal, financial and non-financial goals;
- b) company goals; and
- c) adherence to the Company's policies, commitments, values and principles.

The Remuneration Committee reviews and recommends the Managing Director's package and incentive payments. The Remuneration Committee also approves the fixed remuneration and incentive packages for all senior executives (the "Executive Management Team") with reference to external benchmarking indicators. Further information on senior executive remuneration is contained in the Remuneration Report.

Principle 2 – Structure the Board to add value

ERM Power has a six-member Board comprising a Non-Executive Chairman, four independent Non-Executive Directors and a Managing Director. The Company seeks to have directors with a broad range of experience, expertise, skills, qualifications and an understanding of, and competence to deal with, current and emerging issues of the business. The Company's succession plans are designed to maintain an appropriate balance of skills, experience and expertise on the Board. The director's profiles, period in office, and details of their skills, experience, and special expertise are set in the Directors' Report.

Principle 2.1 of the Guidelines states that the majority of the Board should be independent directors. The Board considers each director's independence on a regular basis and formed the view that for the FY11 reporting period, Tony Bellas, Martin Greenberg, Brett Heading and Tony Iannello were independent. In defining the characteristics of an independent director, the Board uses the Guidelines, together with its own consideration of the Company's operations and businesses and appropriate materiality thresholds in any relationship that could materially interfere, or be perceived as interfering with the exercise of an unfettered independent judgement in relation to matters concerning the Company. Despite being a partner of a law firm that provides professional advice to ERM Power and its related entities, the Board nevertheless considers Brett Heading to be independent as he has not been directly involved in the provision of any legal advice, or the management of any legal matters (as this responsibility rests with executive management).

Principle 2.2 of the Guidelines recommends that the Company's chairman should be independent. Trevor St Baker, the Non-Executive Chairman, is not independent (by virtue of his major shareholding interest in the Company) and accordingly, the Company is unable to comply with Principle 2.2. The Board believes that it is in the best interests of the Company to have Trevor St Baker as its Chairman, acknowledging Trevor's standing and experience in the Australian electricity industry and his contributions to the Company's development over the past 30 years.

The Board schedules a minimum of six meetings a year. If required, additional unscheduled meetings are held to deal with urgent matters. An agenda is prepared for each Board meeting by the Company Secretary to ensure operational, financial, strategic, regulatory and major risk areas are addressed. Executive management also provide the Board each month with an operations report, a health, safety, environment and sustainability report, financial reports and reports on all major projects under construction and, as appropriate, on other company and operational matters. All directors have unfettered access to any of the Company's records and information they consider necessary to fulfil their responsibilities, and the Board may invite external advisers to attend Board meetings where necessary or desirable.

The Audit & Risk Committee, Remuneration Committee, Health, Safety, Environment & Sustainability Committee and Nomination Committee each has a charter which sets out its roles and responsibilities, composition, structure, membership requirements and operation. These are available on the Company's website. Committee meeting minutes are tabled at the following Board meeting.

A list of the members of each Committee and their attendance at Committee meetings is set out in the Directors' Report.

The Nomination Committee provides advice and makes recommendations to the Board to ensure that it is comprised of individuals who are best able to discharge the responsibilities of directors, having regard to the law and the highest standards of governance by:

- assessing the skills required by the Board and the extent to which the required skills are represented on the Board;
- establishing processes for the review of the individual directors and the Chairman specifically, and the Board as a whole;
- establishing processes for the identification of suitable candidates for appointment to the Board as additional members or to succeed existing members and reviewing Board succession plans;

- reviewing and reporting, at least annually, on the relative proportion of women and men on the Board; and
- making recommendations to the Board on directors appointments or Board and Committee structure.

Each year, one-third of the Board, other than the Managing Director, retires in accordance with the constitution, and is eligible for re-election by shareholders at the annual general meeting (AGM). At the Company's AGM, on 23 November 2011, Trevor St Baker and Martin Greenberg, as the longest standing directors, will be retiring and standing for re-election. The Board unanimously supports their re-election.

Prior to the AGM each year the Nomination Committee evaluates any new directorship nominations, and evaluates the performance of those directors retiring by rotation; the results of which form the basis of the Boards' recommendation to shareholders. The Board's recommendation on the re-election of Trevor St Baker and Martin Greenberg will be included in the Notice convening the AGM.

Every year, through the Nomination Committee, the directors review the performance of the whole Board and Board Committees. The review considers a director's expertise, skill and experience, along with his/her understanding of the Company's business, preparation for meetings, relationships with other directors and management, awareness of ethical and governance issues, and overall contribution. This year a full review was undertaken covering the Board's activities and work program, time commitments, meeting efficiency and Board contribution to Company strategy, monitoring, compliance and governance.

Principle 3 – Promote ethical and responsible decision making

The Board strongly encourages ethical and responsible decision making and has implemented policies to achieve this while in pursuit of the Company's objectives.

A Code of Business Conduct, Securities Trading Policy and Whistleblower Policy apply to the Company's directors and employees and are available on the Company's website.

The purpose of these documents is to guide directors and employees in the performance of their duties, set appropriate restrictions on the trading of securities by directors, employees and their associates, and to the Company's employees who wish to report in good faith inappropriate behaviour or wrongful acts without fear of retaliation or punishment.

Corporate Governance Report for the year ended 30 June 2011 continued...

The Guidelines were amended on 30 June 2010 to include, amongst other things, a recommendation that companies establish a policy concerning diversity. The Board has adopted a Diversity Policy which is available on the Company's website with the following measurable objectives proposed for the forthcoming reporting period (FY2012):

- ensure diversity programs reflect the Company's policy and approach to diversity and ensure they are communicated to all employees:
- review all recruitment and remuneration practices to ensure they are free from gender bias and encourage greater female participation and opportunity:
- identify high talent women at low to middle management level and implement specific strategies to enhance the skills and experience of these people to prepare them for advancement: and
- encourage female applicants for all roles, but specifically technical roles where representation is low, and seek at least one female candidate for the shortlist for each technical role.

As at the end of the FY11 reporting period, there was no female participation on the Board or in senior executive positions (out of approximately 10). The percentage of women employed by the Company as a whole organisation was 21.5%.

Principle 4 – Safeguard integrity in financial reporting

The Company has an Audit and Risk Committee compliant with Principle 4 which consists of three independent directors, Tony Bellas (Chairman), Martin Greenberg and Tony Iannello. The charter is available on the Company's website and contains information on the procedures for the selection and appointment of external auditors and for the rotation of external audit engagement partners.

The Audit and Risk Committee reviews and discusses with management and the external auditors the half-yearly and annual financial reports including notes to the financial accounts and other disclosures and recommends to the Board whether the financial reports should be approved.

The Audit and Risk Committee monitors the adequacy of, integrity of, and the effectiveness of, management processes that support financial reporting. It also maintains

and oversees a sound system of internal controls based on the adoption by the Board of a risk-based approach to the identification, assessment, monitoring and management of risks that are significant to the fulfilment of the Company's business objectives.

The qualifications of the members of the Audit and Risk Committee and their attendance at meetings of the committee are set out in the Directors' Report.

Principle 5 – Make timely and balanced disclosure

The Company's current practice on disclosure is consistent with the Guidelines. The Board has adopted a Continuous Disclosure Policy and procedures are in place to ensure compliance with ASX Listing Rule disclosure requirements.

The Continuous Disclosure Policy and the Shareholder Communication Policy are available on the Company's website.

All material presentations by the Company are released to the ASX and posted on the Company's website.

Principle 6 – Respect the rights of shareholders

The Company is committed to providing regular communication to shareholders about the financial performance of ERM Power and its business and operations. Annual reports are able to be accessed by shareholders via the Company's website, with a hardcopy able to be mailed out on request.

The Board will communicate with shareholders regularly and clearly by electronic means as well as by traditional methods. Shareholders are encouraged to attend and participate at general meetings. The Company's auditor will attend the annual general meeting and will be available to answer shareholders' questions. The Company's policies comply with the Guidelines in relation to the rights of shareholders.

All announcements to the ASX are posted on the Company's website. The Company attempts to keep its website as current and informative as possible for shareholders and other stakeholders, including any update on its current projects.

The Shareholder Communication Policy is available on the Company's website.

Principle 7 – Recognise and manage risks

The Board, through the Audit and Risk Committee, has an overarching policy governing the Company's approach to risk oversight and management and internal control systems, the Risk Management Framework Policy which is available on the Company's website. The Board is also responsible for ensuring that there are other appropriate policies in relation to risk management and internal control systems.

The Company's policies are designed to identify, assess, address and monitor strategic, operational, legal, reputational, commodity and financial risks to enable it to achieve its business objectives. Where appropriate, certain risks are covered by insurance or by Board-approved policies for hedging of interest rates, foreign exchange rates and commodities. In this respect, the Company complies with Principle 7.1.

Board, executive and business unit level controls are designed to safeguard company and stakeholders' interests in respect of those risks mentioned above. Each Executive Team member is responsible for communicating to their team the risk framework and structure required by the ERM Power Board and the Audit and Risk Committee. The Chief Financial Officer is responsible for reporting to the Board and the Audit and Risk Committee about the management of the Company's material business risks, and the Board has received a report from the Chief Financial Officer that as at 30 June 2011 its material business risks are being managed effectively.

The Company undertakes reviews of projects and business units for major risks and seeks to maintain strong controls across all corporate and operational activities in compliance with Principle 7.2.

When presenting financial statements for Board approval, the Managing Director and Chief Financial Officer provide a formal statement in accordance with section 295A of the *Corporations Act 2001* (Cth) with an assurance that the statement is founded upon a sound system of risk management and internal control that is operating effectively in all material respects in relation to financial reporting risks.

Principle 8 – Remunerate fairly and responsibly

The Remuneration Committee ensures that remuneration is consistent with current market practices and that the Company can attract, retain and develop valued employees. In this regard, the Company complies with Principle 8.1. The Remuneration Committee charter can be found on the Company's website.

The Remuneration Committee charter was updated during the FY11 reporting period to ensure the Committee reviews and reports, at least annually, on the relative proportion of women and men in the workforce at all levels of the ERM Power group, excluding the ERM Power Board (which is the responsibility of the Nomination Committee). These proportions are contained in Principle 3 above.

In compliance with Principle 8.2, the Remuneration Committee is comprised of ERM Power's four independent Non-Executive Directors (Tony Bellas, Martin Greenberg, Brett Heading and Tony Iannello) with Tony Iannello as Chairman. Their attendance at meetings of the committee is set out in the Directors' Report.

The remuneration of non-executive directors is structured separately from that of the Managing Director and senior executives. The Managing Director and senior executives are remunerated by way of a mix of fixed and variable remuneration in a manner that motivates them to pursue the long term growth and success of the Group.

The Securities Trading Policy contains a prohibition against directors and employees altering the economic benefit derived by the director or employee in relation to an equity-based incentive award or grant made by the Company.

Information on remuneration of directors and senior executives is contained in the Remuneration Report.

All information referred to in this Corporate Governance Statement as being on the Company's website can be found at the web address: www.ermpower.com.au within the "Shareholders" tab, under either "Corporate governance" or "ASX Announcements". More information on ERM Power's Corporate Governance is also located here.



ERM Power Limited Annual Financial Statements for the year ended 30 June 2011

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The financial statements were authorised for issue by the Directors on 25 August 2011. The Directors have the power to amend and reissue the financial statements.

This financial report covers ERM Power Limited, formerly known as ERM Power Pty Ltd, ("ERM") as a consolidated entity comprising ERM Power Limited and its controlled entities. ERM was converted to a public company on 17 September 2010. The Group's functional and presentation currency is Australian dollars (AUD).

ERM Power Limited is a company limited by shares, incorporated and domiciled in Australia. Its registered office and principal place of business is as set out on page 52.

A description of the Group's operations and of its principal activities is included in the review of operations and activities in the Directors' report on pages 22 to 30. The Directors' report does not form part of the financial report.

ABN 28 122 259 223



Auditor's Independence Declaration

As lead auditor for the audit of ERM Power Limited for the year ended 30 June 2011, I declare that to the best of my knowledge and belief, there have been:

- a) no contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
- b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of ERM Power Limited and the entities it controlled during the period.

A handwritten signature in blue ink, appearing to read 'Timothy J Allman'.

Timothy J Allman
Partner
PricewaterhouseCoopers

Brisbane
25 August 2011

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CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 30 JUNE 2011

	Note	2011 \$'000	2010 \$'000
CONTINUING OPERATIONS			
Revenue	5	544,563	378,612
Other income		513	3,412
Net gain on disposal of interests in assets	35	4,738	36,379
Expenses	6	(504,843)	(351,041)
Results from operating activities before finance costs, depreciation, amortisation and fair value gains/losses on financial instruments		44,971	67,362
Depreciation and amortisation		(9,977)	(12,722)
Net fair value losses on financial instruments designated at fair value through profit or loss	7	14,187	(37,262)
Results from operating activities		49,181	17,378
Finance expense	8	(29,793)	(39,770)
Share of profit of associates, net of income tax	17	1,436	1,321
Profit / (loss) before income tax		20,824	(21,071)
Income tax (expense) / benefit	9	(4,605)	5,318
Profit / (loss) for the year		16,219	(15,753)
Attributable to:			
Equity holders of the Company		16,176	(16,867)
Non-controlling interest		43	1,114
Profit / (loss) for the year		16,219	(15,753)
Earnings per share based on earnings attributable to the ordinary equity holders of the Company		Cents	Cents
Basic earnings per share	37	11.72	(16.72)
Diluted earnings per share	37	11.35	(16.72)

The above Consolidated Income Statement should be read in conjunction with the accompanying notes.

Operational business segment performance and underlying profit of the consolidated entity is presented in note 2 together with a reconciliation between statutory profit attributable to members of the parent entity and underlying profit.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2011

	2011 \$'000	2010 \$'000
Profit / (loss) for the year	16,219	(15,753)
Other comprehensive income		
Cash flow hedges net of tax	3,393	7,083
Other comprehensive income for the year, net of tax	3,393	7,083
Total comprehensive income	19,612	(8,670)
Other comprehensive income for the year attributable to:		
Equity holders of the Company	3,063	8,749
Non-controlling interest	330	(1,666)
Other comprehensive income	3,393	7,083
Total comprehensive income for the year attributable to:		
Equity holders of the Company	19,239	(8,118)
Non-controlling interest	373	(552)
Total comprehensive income	19,612	(8,670)

The above Consolidated Statement of Comprehensive Income should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2011

	Note	2011 \$'000	2010 \$'000
ASSETS			
Current Assets			
Cash and cash equivalents	11	184,264	59,478
Trade and other receivables	13	45,181	103,747
Inventories	14	3,139	800
Other assets	15	4,486	8,286
Derivative financial instruments	16	499	409
Total Current Assets		237,569	172,720
Non-Current Assets			
Cash and cash equivalents	11	2,091	3,032
Trade and other receivables	13	2,556	2,607
Derivative financial instruments	16	43	-
Investment in associates accounted for using the equity method	17	18,541	17,675
Property, plant and equipment	19	206,456	392,607
Exploration and evaluation costs	20	11,435	6,569
Deferred tax assets	9	33,455	61,066
Intangible assets	21	1,882	5,815
Total Non-Current Assets		276,459	489,371
TOTAL ASSETS		514,028	662,091
LIABILITIES			
Current Liabilities			
Trade and other payables	22	63,035	51,310
Current tax liabilities	9	-	46
Borrowings	23	-	7,973
Borrowings – limited recourse	23	4,719	5,001
Derivative financial instruments	24	27,091	39,601
Provisions	25	1,079	1,122
Total Current Liabilities		95,924	105,053
Non-Current Liabilities			
Borrowings	23	4,400	25,140
Borrowings – limited recourse	23	202,575	393,208
Derivative financial instruments	24	29,954	47,260
Deferred tax liabilities	9	23,426	46,149
Provisions	25	50	36
Total Non-Current Liabilities		260,405	511,793
TOTAL LIABILITIES		356,329	616,846
NET ASSETS		157,699	45,245
EQUITY			
Contributed equity	26	160,239	60,573
Reserves	27	(11,555)	(21,412)
Retained earnings		9,015	(7,161)
Capital and reserves attributable to owners of ERM Power Limited		157,699	32,000
Non-controlling interest		-	13,245
TOTAL EQUITY		157,699	45,245

The above Consolidated Statement of Financial Position should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2011

Note	Contributed equity \$'000	Reserves \$'000	Retained earnings \$'000	Total \$'000	Non- controlling interests \$'000	Total equity \$'000
Balance at 1 July 2009	60,012	(30,488)	9,706	39,230	13,797	53,027
Loss for the period	-	-	(16,867)	(16,867)	1,114	(15,753)
Other comprehensive income	-	8,749	-	8,749	(1,666)	7,083
Total comprehensive income for the year	-	8,749	(16,867)	(8,118)	(552)	(8,670)
Transactions with owners in their capacity as owners:						
Issue of shares and share options pursuant to employee incentive scheme	561	327	-	888	-	888
Balance at 30 June 2010	60,573	(21,412)	(7,161)	32,000	13,245	45,245
Profit for the period	-	-	16,176	16,176	43	16,219
Other comprehensive income	-	3,063	-	3,063	330	3,393
Total comprehensive income for the year	-	3,063	16,176	19,239	373	19,612
Transactions with owners in their capacity as owners:						
Disposal of interest in partnership net of tax ⁽ⁱ⁾	-	6,517	-	6,517	(13,618)	(7,101)
Issue of shares and share options pursuant to employee incentive scheme	26	4,470	-	4,470	-	4,470
Contribution of equity from IPO net of transactions costs	26	93,760	-	93,760	-	93,760
Issue of shares on acquisition of SAGE	26	2,334	-	2,334	-	2,334
Purchase of treasury shares	26	(898)	-	(898)	-	(898)
Share based payment expense	28	-	277	277	-	277
Balance at 30 June 2011	160,239	(11,555)	9,015	157,699	-	157,699

⁽ⁱ⁾ Kwinana Power Station sold during year. Refer note 35 for further details

The above Consolidated Statement of Changes in Equity should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2011

	Note	2011 \$'000	2010 \$'000
Cash flows from operating activities			
Receipts from customers (inclusive of applicable goods and services tax)		644,967	424,663
Payments to suppliers and employees (inclusive of goods and services tax)		(536,434)	(409,269)
Dividends received		570	1,230
Income tax paid		-	(9,112)
Net cash flows used in operating activities	12a	109,103	7,512
Cash flows from investing activities			
Payments for exploration and evaluation		(4,866)	(3,378)
Payments for plant and equipment		(13,143)	(41,070)
Cash loss on disposal of joint interests	35	(1,264)	18,863
Net cash acquired as part of business combination	36	417	-
Net cash flows used in investing activities		(18,856)	(25,585)
Cash flows from financing activities			
Proceeds from borrowings		4,400	26,640
Repayments of borrowings		(33,086)	(78,561)
Proceeds from borrowings – limited recourse		-	168,061
Repayments of borrowings – limited recourse		(3,438)	(144,011)
Finance costs		(32,696)	(39,025)
Interest received		4,488	2,759
Issue of shares on initial public offering	26	100,000	-
Transaction costs on initial public offering share issue	26	(6,240)	-
Cash received on exercise of share options	26	170	-
Net cash flows from financing activities		33,598	(64,137)
Net increase / (decrease) in cash and cash equivalents		123,845	(82,210)
Cash and cash equivalents at the beginning of the year		62,510	144,720
Cash and cash equivalents at the end of the year	11	186,355	62,510
Non-cash investing and financing activities	12b	2,334	-

The above Consolidated Statement of Financial Position should be read in conjunction with the accompanying notes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

These financial statements cover ERM Power Limited the consolidated entity ('Group' or 'consolidated entity') consisting of ERM Power Limited and its subsidiaries. The report is presented in Australian dollars.

ERM Power Limited is incorporated and domiciled in Australia. Its registered office and place of business is Level 5, Riverside Centre, 123 Eagle Street, Brisbane, Queensland, 4000.

A description of the nature of the Group's operations and of its principal activities is included in the review of operations and activities in the Directors' report on pages 22 to 30.

This report was authorised for issue by the Directors on 25 August 2011.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

(a) Basis of preparation

This general purpose financial report has been prepared in accordance with Australian Accounting Standards, other authoritative pronouncements of the Australian Accounting Standards Board and the *Corporations Act 2001*.

Compliance with IFRS

The consolidated financial statements of the Group comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

Early adoption of Australian Accounting Standards

The Group has elected to apply the following pronouncements to the annual reporting period commencing 1 July 2010:

Revised AASB 124 Related Party Disclosures and AASB 2009-12 Amendments to Australian Accounting Standards.

This includes applying the revised pronouncement to the comparatives in accordance with AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors. None of the items in the financial statements had to be restated as the result of applying this standard.

Historical cost convention

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and liabilities (including derivative instruments) at fair value through profit and loss.

Critical accounting estimates

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. Information regarding critical accounting estimates is provided in note 4.

(b) Principles of consolidation

Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of ERM Power Limited as at 30 June 2011 and the results of all its subsidiaries for the year then ended.

Subsidiaries are all those entities (including special purpose entities) over which the Group has the power to govern their financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group that were not previously under common control.

On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets. Non-controlling interests in the results and equity of subsidiaries are shown separately in the consolidated income statement, statement of comprehensive income, statement of changes in equity and balance sheet respectively.

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

Intercompany balances, transactions and unrealised gains resulting from intra-Group transactions have been eliminated in full. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred.

Investments in subsidiaries are accounted for at cost less any impairment in the individual financial statements of ERM Power Limited.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(b) Principles of consolidation continued

Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for in the consolidated financial statements using the equity method of accounting.

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. Dividends receivable from associates are recognised in the consolidated financial statements by reducing the carrying amount of the investment.

When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the investment.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Jointly controlled entities

Jointly controlled entities are those entities over whose activities the entity has joint control, established by a contractual agreement. In the consolidated financial statements, investments in jointly controlled entities, including partnerships, are accounted for using the proportionate consolidation method of accounting.

The proportionate interests in the assets, liabilities, income and expenses of a jointly controlled entity are incorporated in the financial statements under the appropriate headings. Transactions and balances between the Group and jointly controlled entities are eliminated to the extent of the Group's proportionate interests.

Employee share trusts

The Group has formed trusts to administer the Group's employee share schemes. The trusts are consolidated, as the substance of the relationship is that the trusts

are controlled by the Group. Shares held by the trusts are disclosed as treasury shares and deducted from contributed equity.

(c) Parent entity financial information

The financial information for the parent entity, ERM Power Limited, disclosed in note 29 has been prepared on the same basis as the consolidated financial statements, except as set out below:

(i) Investments in subsidiaries, associates and joint venture entities

Investments in subsidiaries, associates and joint venture entities are accounted for at cost in the financial statements of ERM Power Limited. Dividends received from associates are recognised in the parent entity's profit or loss, rather than being deducted from the carrying amount of these investments.

(ii) Financial guarantees

Where the parent entity provides financial guarantees in relation to loans and payables of subsidiaries for no compensation, the fair values of these guarantees are accounted for as contributions and recognised as part of the cost of the investments.

(iii) Share-based payments

The grant by the company of options over its equity instruments to the employees of subsidiary undertakings in the Group is treated as a capital contribution to that subsidiary undertaking. The fair value of employee services received, measured by reference to the grant date fair value, is recognised over the vesting period as an increase to investment in subsidiary undertakings, with a corresponding credit to equity.

(iv) Tax consolidation legislation

ERM Power Limited and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation.

The head entity ERM Power Limited, and the controlled entities in the tax consolidated Group, account for their own current and deferred tax amounts. These tax amounts are measured as if each entity in the tax consolidated Group continues to be a standalone taxpayer in its own right.

In addition to its own current and deferred tax amounts, ERM Power Limited also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(c) Parent entity financial information continued

(iv) Tax consolidation legislation continued

Assets or liabilities arising under tax funding agreements with the tax consolidated entities are recognised as amounts receivable from or payable to other entities in the Group.

Any difference between the amounts assumed and amounts receivable or payable under the tax funding agreement are recognised as a contribution to (or distribution from) wholly-owned tax consolidated entities.

(d) Segment reporting

The consolidated entity determines and presents operating segments based on the information that is internally provided to the Managing Director who is the chief operating decision maker. The Managing Director regularly receives financial information on the underlying profit of each operating segment and the statutory profit.

An operating segment is a distinguishable component of an entity that engages in business activity from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity), and whose operating results are regularly reviewed by the chief operating decision maker to make decisions about resources to be allocated to the segment.

(e) Foreign currency translation

Functional and presentation currency

The consolidated financial statements are presented in Australian dollars, which is the functional and presentation currency of each of the Group companies.

Transactions and balances

Foreign currency transactions are translated into the functional currency at the rate of exchange at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges.

(f) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, deposits held at call with financial institutions, and other short-term highly liquid investments with original maturities of three months or less that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, net of any bank overdrafts. These assets are stated at nominal values.

Cash that is reserved and its use specifically restricted for maintenance and/or debt servicing under the Group's borrowing agreements is defined as restricted cash.

Restricted cash is shown at the balance date according to the timing of its release. Accordingly, cash that cannot be applied or used within the next 12 months is shown as a non-current asset. All other cash and cash equivalents are shown as current assets.

(g) Trade and other receivables

All trade and other debtors are recognised initially at fair value and subsequently measured at amortised cost using the original effective interest method less allowances for doubtful debts. Collectability is reviewed on an ongoing basis. An allowance for doubtful debts is made when there is objective evidence that the Group will not be able to collect any amounts due according to original terms. The amount of the allowance is the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the effective interest rate. The amount of the impairment loss is recognised in the income statement.

Trade receivables are those due for settlement no more than 30 days from the date of invoice.

(h) Inventories

Renewable energy certificates

Renewable energy certificates held by the Group are accounted for as commodity inventories. The Group participates in the purchase and sale of a range of renewable energy certificates, including both mandatory and voluntary schemes.

Purchased renewable energy certificates are initially recognised at cost within inventories. Subsequent measurement is at fair value less costs to sell, with unrealised gains and losses arising from changes in fair value being recognised in the income statement in the period of the change.

(i) Financial assets

Investments are recognised and derecognised on trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value.

Subsequent to initial recognition, investments in associates are accounted for under the equity method in the consolidated financial statements. Further information regarding equity accounted investments is detailed in note 1 (b).

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(i) Financial assets continued

Other financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss', 'held-to-maturity investments', 'available-for-sale' financial assets, and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. Further information on the categories of financial assets held by the Group during the financial year is provided below.

Financial assets at fair value through profit or loss

Financial assets are classified as financial assets at fair value through profit or loss where the financial asset:

- has been acquired principally for the purpose of selling in the near future; and
- is a derivative that is not designated and effective as a hedging instrument.

Loans and receivables

Trade receivables, loans and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method less impairment. Interest income is recognised by applying the effective interest rate.

De-recognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Impairment of financial assets

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at each balance date. Financial assets are impaired where there is objective evidence that as a result of one or more events that occurred after the initial recognition of the financial asset the estimated future cash flows of the investment have been impacted.

For financial assets carried at amortised cost, 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 financial assets including uncollectable trade receivables is reduced by the impairment loss through the use of an allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

With the exception of available-for-sale equity instruments, if in a subsequent period the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest rate basis for debt instruments other than those financial assets 'at fair value through profit or loss'.

(j) Capitalised work in progress

Costs incurred in relation to the development of a project, including the cost of construction, are recorded as capitalised work in progress when these costs are incurred prior to the establishment of a development vehicle. Development expenditure is recorded as capitalised work in progress only if development costs can be measured reliably, the project is technically and commercially feasible, future economic benefits are probable, and the Group intends to and has sufficient resources to complete development and to use or sell the asset. Development costs relating to project costs incurred may include legal fees, insurance costs, independent engineer costs, borrowing costs, environmental impact study fees, and direct labour and overhead costs.

Capitalised work in progress is measured at cost less accumulated impairment losses.

The recovery of these costs usually occurs at financial close of a project at which time these costs are transferred to a development vehicle.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(k) Derivative financial instruments

ERM Power Retail Pty Limited ("ERM Sales"), one of the subsidiaries in the Group, routinely enters into forward sales contracts ("Contracts") related to the provision of electricity in the Australian National Electricity Market ("NEM"). The Contracts are exclusively entered into with large industrial, commercial and government entities under term contracts. All of the electricity provided under these contracts is traded in the NEM spot market.

ERM Sales also enters into a variety of electricity derivative transactions ("Derivatives") as part of an overall strategy to hedge the exposure to contract prices. ERM Sales manages all of its Contracts and Derivatives as part of an overall commodity trading strategy.

Revenue from the Contracts is recognised in accordance with the revenue recognition policy in note 1(x). Derivatives are initially recognised at fair value on the date the derivative contract is entered into, and are subsequently remeasured to their fair value at each balance date. Derivatives are carried in the statement of financial position as assets when the fair value is positive and as liabilities when the fair value is negative. The resulting gain or loss arising from the revaluation is recognised in the income statement in the period it arises.

Hedge accounting

The Group designates interest rate swaps and forward foreign exchange contracts as cash flow hedges.

At the inception of the hedge relationship the entity documents the relationship between the hedging instrument and hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in cash flows of the hedged item.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are deferred in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss. Amounts deferred in equity are recycled in profit or loss in the periods when the hedged item is recognised in profit or loss in the same line as the recognised hedged item. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-

financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

Hedge accounting is discontinued when the Group revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss deferred in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was deferred in equity is recognised immediately in profit or loss.

(l) Fair value estimation

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes.

The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the balance date. The quoted market price used for financial assets held by the Group is the current bid price; the appropriate quoted market price for financial liabilities is the current ask price.

The fair value of financial instruments that are not traded in an active market is determined using a variety of valuation techniques and assumptions that are based on market conditions existing at each balance date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt instruments held. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of forward exchange contracts is determined using market exchange rates and published forward margins at balance date.

The nominal value less estimated credit adjustments of trade receivables and payables is assumed to approximate their fair value. For disclosure purposes the fair value of financial liabilities is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

(m) Property, plant and equipment

Items of property, plant and equipment are initially measured at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(m) Property, plant and equipment continued

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All repairs and maintenance expenses are charged to the income statement during the financial period in which they are incurred.

Subsequent impairment losses are recognised in accordance with note 1(o).

Depreciation

Land and capital work in progress are not depreciated. Depreciation on the other assets is calculated using the straight-line method to allocate their cost, net of their residual values, over their estimated useful lives, as follows:

- Leasehold improvements the lesser of the remaining lease term and the life of the asset
- Motor vehicles 3 – 10 years;
- Plant and equipment 20 – 33 years;
- IT equipment 3 – 5 years; and
- Furniture and equipment 5 years.

Capital work in progress comprises costs incurred to date on construction of power generation plants.

Asset residual values and useful lives are reviewed and adjusted if appropriate at each balance date.

Gains and losses on disposals are determined by comparing the proceeds to the carrying amount. These are included in the income statement.

Exploration and evaluation costs

Exploration and evaluation expenditure incurred is accumulated in respect of each identifiable area of interest. Such expenditure comprises net direct costs and an appropriate portion of related overhead expenditure but does not include overheads or administration expenditure not having a specific nexus with a particular area of interest. Exploration and evaluation expenditure is only capitalised from the point when the rights to tenure of the area are granted. All exploration and evaluation costs are capitalised to the extent that they are expected to be recouped through the successful development of the area or where activities in the area have not yet reached a stage which permits reasonable assessment of the existence of economically recoverable reserves and active or significant operations in relation to the area are continuing.

The probability of expected future economic benefits is assessed using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset. In this assessment, greater weighting is given to available external evidence. Exploration and evaluation assets will be reclassified as development assets at the point in which technical feasibility and commercial viability of extraction gas are demonstrated or a petroleum lease is granted. Exploration and evaluation assets are assessed for impairment and any impairment loss is recognised before reclassification. Accumulated costs in relation to an abandoned area are written off in full against profit in the year in which the decision to abandon is made.

Software

Computer software is either purchased or developed within the organisation and is recorded at cost less accumulated amortisation and impairment losses. Amortisation is calculated using the straight line method over the estimated useful lives. Depending on the individual software, the estimated useful life ranges between 3 and 5 years.

(n) Intangible assets

Goodwill

Goodwill is measured as described in note 1(p). Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of associates is included in investments in associates.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose, identified according to operating segments.

(o) Impairment of assets

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows.

Intangible assets, including exploration and evaluation assets, are assessed for impairment when facts and circumstances suggest that the carrying amount may exceed its recoverable amount.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(o) Impairment of assets continued

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired.

(p) Business combinations

The acquisition method of accounting is used to account for all business combinations, regardless of whether equity instruments or other assets are acquired. The consideration transferred for the acquisition of a subsidiary comprises the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred also includes the fair value of any asset or liability resulting from a contingent consideration arrangement and the fair value of any pre-existing equity interest in the subsidiary. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are, with limited exceptions, measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the group's share of the net identifiable assets acquired is recorded as goodwill. If those amounts are less than the fair value of the net identifiable assets of the subsidiary acquired and the measurement of all amounts has been reviewed, the difference is recognised directly in profit or loss as a bargain purchase.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value as at the date of exchange. The discount rate used is the entity's incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

Contingent consideration is classified either as equity or a financial liability. Amounts classified as a financial liability are subsequently remeasured to fair value with changes in fair value recognised in profit or loss.

(q) Trade and other payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of the financial period and which are unpaid. The amounts are unsecured and are usually paid within 60 days of recognition.

(r) Provisions

Onerous contracts

Obligations arising under onerous contracts are recognised and measured as a provision. An onerous contract is considered to exist where the Group has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be derived from it.

(s) Other financial liabilities

Other financial liabilities, including borrowings, are initially recognised at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

(t) Employee benefits

Wages and salaries, annual leave and sick leave

Liabilities arising in respect of wages and salaries, annual leave and any other employee entitlements expected to be settled within 12 months of balance date are measured at the amounts expected to be paid when the liabilities are settled.

Long service leave

Long service leave liabilities are measured at the present value of the estimated future cash outflow to be made in respect of services provided by employees up to balance date. Consideration is given to expected future wage and salary levels, projected employee movements and periods of service. Expected future payments are discounted using market yields at balance date on government bonds with terms to maturity that match, as closely as possible, the estimated future cash flows.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(t) Employee benefits continued

Bonus plans

Liabilities for employee benefits in the form of bonus plans are recognised in liabilities when it is probable that the liability will be settled and there are formal terms in place to determine the amount of the benefit.

Liabilities for bonus plans are expected to be settled within 12 months and are measured at the amounts expected to be paid when they are settled.

Equity-based compensation benefits

Equity-based compensation benefits are provided to employees via employee and executive equity plans.

The fair value of options or shares issued to employees is recognised as an employee benefit expense with a corresponding increase in equity. The fair value is measured at grant date and recognised in the option reserve or share-based payment reserve over the period during which the employees become unconditionally entitled to the equity. When the shares are issued, or the options exercised, the value is transferred to contributed equity.

The fair value of options at grant date is determined using the Black Scholes method that takes into account the value of the underlying share at grant date, the term of the vesting period, exercise price and expiry date.

The assessed fair value of shares granted to employees is allocated equally over the period from issue to the actual or expected vesting date.

Refer to note 28 for further details.

(u) Assets available for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition.

Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification. Non-current assets (and disposal groups) classified as held for sale are measured at the lower of their previous carrying amount and fair value less costs to sell.

(v) Earnings per share

Basic earnings per share are calculated by dividing:

- The profit attributable to owners of the Company, excluding any cost of servicing equity other than ordinary shares;
- By the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements ordinary shares issued during the year and excluding treasury shares.

Diluted earnings per share

Diluted earnings per share adjust the figures used in the determination of basic earnings per share to take into account:

- The after income tax effect of interest and other financing cost associated with dilutive potential ordinary shares; and
- The weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

(w) Contributed equity

Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

Preference share capital

Preference share capital is classified as equity if it is non-redeemable, or redeemable only at the entity's option, and any dividends are discretionary. Dividends thereon are recognised as distributions within equity upon declaration by the directors.

Preference share capital is classified as a liability if it is redeemable on a specific date or at the option of the shareholders, or if dividend payments are not discretionary. Dividends thereon are recognised as interest expense in profit or loss.

(x) Revenue recognition

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as outlined below.

Revenue is measured at the fair value of the consideration received or receivable. Amounts disclosed as revenue are net of trade allowances and duties and taxes paid. Electricity sales revenue from sales contracts is recognised on measurement of electrical consumption at the metering

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(x) Revenue recognition continued

point, as specified in each contractual agreement, and is billed monthly in arrears. At each balance sheet date, sales and receivables include an amount of sales delivered to customers but not yet billed and recognised as accrued income.

Interest revenue is recognised on a time proportional basis taking into account the interest rates applicable to the financial assets. All revenue is stated net of goods and services tax.

Project management fees are calculated based on current contractual guidelines and include project success fees earned at financial close. The Group's share of capitalised project management fees is eliminated on consolidation.

(y) Cost of sales

Cost of sales is recognised as those costs directly attributable to the goods sold and includes the costs of electricity, materials and associated distribution expenses.

Electricity

Electricity costs are based upon spot prices for electricity as established by the Australian Energy Market Operator (AEMO) and the outcomes of derivative financial instruments entered into for the purpose of risk management (refer to note 1(k)).

(z) Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in profit or loss over the period of the borrowings using the effective interest method. Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalised as a prepayment for liquidity services and amortised over the period of the facility to which it relates.

Preference shares, which are mandatorily redeemable on a specific date, are classified as liabilities. The dividends on these preference shares are recognised in profit or loss as finance costs.

The fair value of the liability portion of a convertible bond is determined using a market interest rate for an equivalent non-convertible bond. This amount is recorded as a liability on an amortised cost basis using the effective interest rate method until extinguished on conversion or maturity of the bonds. The remainder of the proceeds is allocated to the conversion option. This is recognised and included in shareholders' equity, net of income tax effects.

Borrowings are removed from the balance sheets when the obligation specified in the contract is discharged, cancelled or expired. The difference between the carrying amount of a financial liability that has been extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in profit or loss as other income or finance costs. Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the reporting period.

(aa) Borrowing costs

Borrowing costs incurred for the construction of any qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use or sale. Other borrowing costs are expensed.

The capitalisation rate used to determine the amount of borrowing costs to be capitalised to each project is the effective interest rate applicable to the specific borrowings at a project level during the year.

(bb) Leases

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments.

Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(cc) Income tax

Income tax expense or revenue for the period is the tax payable on the current period's taxable income based on the prevailing income tax rate adjusted by changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Company's subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax liabilities and assets are not recognised for temporary differences between the carrying amount and tax bases of investments in controlled entities where the entity is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

(dd) Goods and services tax (GST)

Revenues, expenses and assets are recognised net of the amount of associated GST, unless the GST incurred is not recoverable from the taxation authority. In this case it is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included with other receivables or payables at the balance date.

Cash flows are presented on a gross basis. The GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to the taxation authority, are presented as operating cash flows.

(ee) Dividends

Provision is made for the amount of any dividend declared, appropriately authorised, no longer at the discretion of the entity and not distributed during the reporting period.

(ff) Rounding of amounts

The Group is of a kind referred to in Class Order 98/100, issued by the Australian Securities and Investments Commission, relating to the "rounding off" of amounts in the financial statements. Amounts in the financial statements have been rounded off in accordance with that class order to the nearest thousand dollars, or in certain cases, the nearest dollar.

(gg) New accounting standards and interpretations

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2011 reporting periods.

AASB 9 Financial Instruments, AASB 2009-11

Amendments to Australian Accounting Standards

arising from AASB 9 and AASB 2010-7 Amendments to Australian Accounting Standards arising from AASB 9

(December 2010) (effective for annual reporting periods beginning on or after 1 January 2013). AASB 9 Financial Instruments addresses the classification, measurement and derecognition of financial assets and financial liabilities. The standard is not applicable until 1 January 2013 but is available for early adoption.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(gg) New accounting standards and interpretations continued

AASB 1053 Application of Tiers of Australian Accounting Standards and AASB 2010-2 Amendments to Australian Accounting Standards arising from Reduced Disclosure Requirements (effective 1 July 2013). On 30 June 2010 the AASB officially introduced a revised differential reporting framework in Australia. Under this framework, a two-tier differential reporting regime applies to all entities that prepare general purpose financial statements. ERM Power Limited is listed on the ASX and is therefore not eligible to adopt the new Australian Accounting Standards – Reduced Disclosure Requirements. As a consequence, the two standards will have no impact on the financial statements of the entity.

IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interests in other Entities and revised IAS 27 Separate Financial Statements and IAS 28 Investments in Associates and Joint Ventures (effective 1 January 2013). In May 2011, the IASB issued a suite of five new and amended standards which address the accounting for joint arrangements, consolidated financial statements and associated disclosures. The AASB is expected to issue equivalent Australian standards shortly.

IFRS 10 replaces all of the guidance on control and consolidation in IAS 27 Consolidated and separate financial statements, and SIC-12 Consolidation – special purpose entities. The core principle that a consolidated entity presents a parent and its subsidiaries as if they are a single economic entity remains unchanged, as do the mechanics of consolidation. However, the standard introduces a single definition of control that applies to all entities. It focuses on the need to have both power and rights or exposure to variable returns before control is present. Power is the current ability to direct the activities that significantly influence returns. Returns must vary and can be positive, negative or both. There is also new guidance on participating and protective rights and on agent/principal relationships.

IFRS 11 introduces a principles based approach to accounting for joint arrangements. The focus is no longer on the legal structure of joint arrangements, but rather on how rights and obligations are shared by the parties to the joint arrangement. Based on the assessment of rights and obligations, a joint arrangement will be classified as either a joint operation or joint venture. Joint ventures are accounted for using the equity method, and the choice to proportionately consolidate will no longer be permitted. Parties to a joint operation will account their share of revenues, expenses, assets and liabilities in much the same way as under the previous standard. IFRS 11 also provides guidance for parties that participate in joint arrangements but do not share joint control.

IFRS 12 sets out the required disclosures for entities reporting under the two new standards, IFRS 10 and IFRS 11, and replaces the disclosure requirements currently found in IAS 28.

Amendments to IAS 28 provide clarification that an entity continues to apply the equity method and does not remeasure its retained interest as part of ownership changes where a joint venture becomes an associate, and vice versa. The amendments also introduce a “partial disposal” concept.

IFRS 13 Fair value measurement (effective 1 January 2013). IFRS 13 was released in May 2011. The AASB is expected to issue an equivalent Australian standard shortly. IFRS 13 explains how to measure fair value and aims to enhance fair value disclosures.

Revised IAS 1 Presentation of Financial Statements (effective 1 July 2012). In June 2011, the IASB made an amendment to IAS 1 Presentation of Financial Statements. The AASB is expected to make equivalent changes to AASB 101 shortly. The amendment requires entities to separate items presented in other comprehensive income into two groups, based on whether they may be recycled to profit or loss in the future. It will not affect the measurement of any of the items recognised in the balance sheet or the profit or loss in the current period.

The Group is currently in the process of assessing the impact of these standards and amendments and is yet to decide whether to early adopt any of the new and amended standards.

2. SEGMENT REPORT

	ERM Sales		Generation Assets		Generation & Development & Operations		Other		Total	
	2011	2010	2011	2010	2011	2010	2011	2010	2011	2010
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Non-statutory revenue										
Non-statutory revenue	486,715	286,692	46,650	80,274	12,780	7,027	1,890	9,650	548,035	383,643
Other income	-	-	450	3,397	-	-	2,077	20	2,527	3,417
Net gain on disposal of interests in assets	-	-	-	-	-	-	4,738	36,379	4,738	36,379
Intersegment sales elimination	-	808	-	-	(4,096)	(2,574)	(1,390)	(3,270)	(5,486)	(5,036)
Total segment revenue	486,715	287,500	47,100	83,671	8,684	4,453	7,315	42,779	549,814	418,403
Less Expenses	(464,257)	(278,045)	(19,628)	(48,582)	(8,545)	(6,869)	(12,413)	(17,545)	(504,843)	(351,041)
Underlying earnings before interest, tax, depreciation and amortisation, (EBITDAIF), and share of profits of associates	22,458	9,455	27,472	35,089	139	(2,416)	(5,098)	25,234	44,971	67,362
Share of profit of associates, net of income tax	-	-	1,436	1,321	-	-	-	-	1,436	1,321
Depreciation and amortisation	(266)	(361)	(8,799)	(11,835)	(101)	-	(811)	(526)	(9,977)	(12,722)
Finance expenses	(715)	(564)	(23,924)	(30,471)	(2)	(5)	(5,152)	(8,730)	(29,793)	(39,770)
Underlying profit before income tax	21,477	8,530	(3,815)	(5,897)	36	(2,421)	(11,061)	15,978	6,637	16,191
Income tax expense attributed to underlying profit	-	-	-	-	-	-	-	-	(349)	(5,861)
Underlying profit after tax	-	-	-	-	-	-	-	-	6,288	10,330
<i>Impact of items excluded from underlying profit:</i>										
Net fair value gains / (losses) on financial instruments designated as fair value through profit or loss									14,187	(37,262)
Tax credit on items excluded from underlying profit									(4,256)	11,179
Statutory profit / (loss) after tax									16,219	(15,753)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

2. SEGMENT REPORT (continued)

	ERM Sales		Generation Assets		Generation Development & Operations		Other		Total	
	2011	2010	2011	2010	2011	2010	2011	2010	2011	2010
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Assets										
Segment assets	104,035	61,382	199,463	413,699	5,511	3,405	153,023 ⁽¹⁾	104,864	462,032	583,350
Investments accounted for using the equity method	-	-	18,541	17,675	-	-	-	-	18,541	17,675
Total segment assets	104,035	61,382	218,004	431,374	5,511	3,405	153,023	104,864	480,573	601,025
Current and deferred tax assets									33,455	61,066
Total assets									514,028	662,091
Liabilities										
Segment liabilities	94,918	61,312	226,670	424,206	1,527	484	9,788	84,695	332,903	570,697
Current and deferred tax liabilities									23,426	46,149
Total liabilities									356,329	616,846

Management has determined the operating segments based on reports reviewed by the Managing Director who is the chief operating decision maker for the consolidated entity. The Managing Director regularly receives financial information on the underlying profit of each operating segment so as to assess the ongoing performance of each segment and to enable a relevant comparison to budget and forecast underlying profit.

Business segments:

ERM Sales

Generation Assets

Generation, Development and Operations

Other

All segment activity takes place in Australia.

Products and services:

Electricity sales to large commercial, industrial and government customers

Gas-fired power generation assets

Delivery of power generation solutions, from the initial concept through to development and operations

ERM Gas, Corporate

⁽¹⁾ Goodwill in relation to the acquisition of Sage Utility Systems Pty Ltd is provisional only at 30 June 2011 and has not been allocated to a business segment. The balance of goodwill is included in the "other" segment at 30 June 2011. Further details are contained within Note 36.

3. FINANCIAL RISK MANAGEMENT

A. Financial risk management objectives

The Group's activities are exposed to a variety of financial risks, including market risk (commodity price, interest rate and foreign currency rate), credit risk and liquidity risk. The Group's overall risk management strategy focuses on the unpredictability of markets and seeks to minimise potential adverse effects on the financial performance of the Group. The Group uses a variety of derivative financial instruments such as electricity derivatives, interest rate swaps and foreign exchange contracts, to hedge against certain risk exposures.

The Group uses different methods to measure the different types of risk to which it is exposed. These methods include sensitivity analysis in the case of interest rate, foreign exchange and other price risks, and ageing analysis for credit risk.

The Group holds the following financial instruments:

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Financial assets	542	409
Derivative financial instruments	3,688	76,723
Loans and receivables	186,355	62,510
Cash and cash equivalents	190,585	139,642
Financial liabilities	57,045	86,861
Derivative financial instruments	274,729	482,632
Other financial liabilities at amortised cost	331,774	569,493

(a) Market risk

Electricity pool price risk

The Group is exposed to fluctuations in wholesale market electricity prices as a result of electricity generation and sales.

Group policies prescribe active management of exposures arising from forecast electricity sales within prescribed limits. In doing so, various hedging contracts have been entered into with individual market participants. Any unhedged position has the potential for variation in revenue from fluctuations in electricity pool prices.

ERM Power Retail Pty Limited ("ERM Sales"), one of the subsidiaries of the Group, routinely enters into forward sales contracts for the provision of electricity. The Group is exposed to a market risk of price fluctuations between the fixed price of these contracts and the relevant spot price of the electricity pool at the time of usage. The majority of this exposure to fluctuations in wholesale market electricity prices is managed through the use of various types of hedging contracts. The hedge portfolio consists predominantly of swaps, caps, futures and sales contracts. Electricity derivatives are either entered into in separate agreements or arise as embedded derivatives. Whilst the Group recognises the fair value of electricity derivative contracts for accounting purposes, the Group does not similarly recognise the fair value of the sales contracts that form the other side of the economic hedging relationship.

The following table summarises the impact of a 10% change in the relevant forward prices for wholesale market electricity prices for the Group at the balance date, while all other variables were held constant.

The impact disclosed below summarises the sensitivity on the mark to market of electricity derivatives contracts only and does not include any corresponding movement in the value of customer contracts.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

3. FINANCIAL RISK MANAGEMENT continued

A. Financial risk management objectives continued

(a) Market risk continued

Retail sales sensitivity

	Increase by 10% \$'000	decrease by 10% \$'000
2011		
Net profit / (loss)	35,191	(35,420)
Equity increase / (decrease)	-	-
2010		
Net profit / (loss)	27,556	(28,157)
Equity increase / (decrease)	-	-

Sensitivity of 10% has been selected as this is considered reasonably possible based on industry standard benchmarks and historical volatilities.

Electricity generation sensitivity

	Increase by 10% \$'000	decrease by 10% \$'000
2011		
Net profit / (loss)	77	(77)
Equity increase / (decrease)	-	-
2010		
Net profit / (loss)	2,206	(2,206)
Equity increase / (decrease)	-	-

Sensitivity of 10% has been selected as this is considered reasonably possible based on industry standard benchmarks and historical volatilities.

Interest rate risk

The Group is exposed to interest rate risk on the funds it borrows at floating interest rates and cash deposits. The risk is managed by entering into interest rate swap contracts. The sensitivity analysis to net profit (being profit before tax) and equity has been determined based on the exposure to interest rates at the balance date and assumes that there are concurrent movements in interest rates and parallel shifts in the yield curves. A sensitivity of 100 basis points has been selected as this is considered reasonable given the current level of short term and long term interest rates.

3. FINANCIAL RISK MANAGEMENT continued

A. Financial risk management objectives continued

(a) Market risk continued

At balance date, if interest rates had been 100 basis points higher/lower and all other variables were held constant, the impact of the Group would be:

	Increase by 1% \$'000	decrease by 1% \$'000
2011		
Net profit / (loss)	632	(632)
Other equity increase / (decrease)	-	-
2010		
Net profit / (loss)	(337)	337
Other equity increase / (decrease)	-	-

The impact on net profit is largely due to the Group's exposure to interest rates on its non-hedged variable rate limited recourse borrowings and cash assets.

Foreign exchange risk

The Group undertakes certain transactions denominated in foreign currencies, related to capital expenditure, which result in exposure to exchange rate fluctuations. Exchange rate exposures are managed utilising forward foreign exchange contracts. For unhedged foreign exchange exposures, there would be no material impact on the Group net profit or equity as a result of a 10% change in the Australian dollar against the USD or EURO with all other variables held constant as at balance date.

(b) Credit risk

Credit risk refers to the loss that would occur if a debtor or other counterparty fails to perform under its contractual obligations. The carrying amounts of financial assets recognised at balance date best represents the Group's maximum exposure to credit risk at balance date. The Group seeks to limit its exposure to credit risks as follows:

- conducting appropriate due diligence on counterparties before entering into arrangements with them;
- depending on the outcome of the credit assessment, obtaining collateral with a value in excess of counterparties' obligations to the Group – providing a 'margin of safety' against loss; and,
- for derivative counterparties, using primarily high credit quality counterparties, in addition to utilising ISDA master agreements with derivative counterparties in order to limit the exposure to credit risk.

The Group has no significant concentrations of credit risk. The credit qualities of all financial assets are consistently monitored in order to identify any potential adverse changes in the credit quality.

Concentrations of credit risk

The Group minimises concentrations of credit risk in relation to debtors by undertaking transactions with a large number of customers from across a broad range of industries within the business segments in which the Group operates, such that there are no significant concentrations of credit risk within the Group at balance date. Credit risk to trade debtors is managed through setting normal payment terms of up to 30 days and through continual risk assessment of debtors with material balances. Credit risk to electricity debtors is managed through system driven credit management processes. The process commences after due date. For some debtors the Group may also obtain security in the form of guarantees, deeds of undertaking, or letters of credit which can be called upon if the counterparty is in default under the terms of the agreement.

The Group minimises concentrations of credit risk in relation to other receivables by entering into partnership arrangements with appropriately qualified partners in order to secure project financing for completion of the project.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

3. FINANCIAL RISK MANAGEMENT continued

A. Financial risk management objectives continued

(b) Credit risk continued

The ageing of receivables as at balance date was as follows:

	Total \$'000	< 30 days \$'000	31-60 days \$'000	> 60 days \$'000		
			Impaired (i)	PDNI ^(a) (ii)	Impaired (i)	>1 year
2011						
Consolidated						
Trade receivables	479	479	8	-	-	-
Other receivables	3,209	-	-	-	-	3,209
	3,688	479	8	-	-	3,209
2010						
Consolidated						
Trade receivables	6,923	6,923	-	-	266	-
Other receivables	69,800	67,193	-	-	-	2,607
	76,723	74,116	-	-	266	2,607

^(a) Past due not impaired

The majority of year end debtors relate to electricity. All of these trade receivables have been paid subsequent to year end.

Other receivables are neither past due or impaired and relate principally to employee shareholder loans, which are subject to loan deeds:

- (i) Impaired balance represents account balances deemed to be irrecoverable by the Group at balance date. A provision for doubtful debts has been provided for.
- (ii) Past due not impaired (PDNI) represents account balances deemed to be outstanding for greater than 30 days but are still considered to be recoverable in the ordinary course of business. Included in the Group's trade receivable balance are debtors with a carrying amount of \$Nil (2010: \$Nil) which are past due at balance date for which the Group has not provided as there has not been a significant change in credit quality and the amounts are still considered recoverable. The Group does not have any collateral over these balances.

(c) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities. Surplus funds are generally only invested in instruments that are tradeable in highly liquid markets.

Information regarding undrawn finance facilities available as at 30 June 2011 is contained in Note 23.

Maturities of financial liabilities

The tables below analyse the Group's financial liabilities, including net and gross settled derivative financial instruments, into relevant maturity groupings based on the remaining period at balance date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. For interest rate swaps the cash flows have been estimated using forward interest rates applicable at balance date. For electricity derivatives the cash flows have been estimated using forward electricity prices at balance date. For foreign exchange contracts, the cash flows have been estimated using forward foreign exchange rates at the balance date.

3. FINANCIAL RISK MANAGEMENT continued

A. Financial risk management objectives continued

(c) Liquidity risk continued

	≤1 year \$'000	1 to 5 years \$'000	>5 years \$'000	Discount \$'000	Total \$'000
Financial liabilities					
Consolidated					
2011					
Trade payables	41,777	-	-	-	41,777
Other payables	21,258	-	-	-	21,258
Interest bearing liabilities	5,900	-	-	-	5,900
Interest bearing liabilities –limited recourse	3,219	23,996	197,547	(18,968)	205,794
Derivatives	27,091	29,954	-	-	57,045
	99,245	53,950	197,547	(18,968)	331,774
2010					
Trade payables	34,414	-	-	-	34,414
Other payables	16,896	-	-	-	16,896
Interest bearing liabilities	12,956	28,605	-	(3,463)	38,098
Interest bearing liabilities – limited recourse	4,420	33,220	393,549	(37,982)	393,207
Finance leases	17	-	-	-	17
Derivatives	39,601	47,260	-	-	86,861
	108,304	109,085	393,549	(41,445)	569,493

B. Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 1 to the financial statements.

C. Financial instruments used by the Group

The Group is party to derivative financial instruments in the normal course of business acquired in order to hedge exposure to fluctuations in electricity prices and interest and foreign exchange rates in accordance with the Group's financial risk management policies.

Interest rate swap contracts-cash flow hedges

The Neerabup partnership has limited recourse, variable interest rate project finance in place. This variable interest has been swapped into fixed.

Swaps currently in place for the Neerabup partnership cover approximately 96% (2010:97%) of the variable loan principal outstanding and are timed to expire as each loan repayment falls due. The fixed interest rate is 7.189% (2010:7.189%) and the variable rate is 1.2% above the BBSY rate which at the end of the reporting period was 5.0% (2010:4.92%).

The contracts require settlement of net interest receivable or payable each 90 days. The settlement dates coincide with the dates on which interest is payable on the underlying debt. The contracts are settled on a net basis.

The gain or loss from remeasuring the hedging instruments at fair values is recognised in other comprehensive income and deferred in equity in the hedging reserve, to the extent that the hedge is effective. It is reclassified into profit or loss when the hedged interest expense is recognised. There was no hedge ineffectiveness in the current or prior year.

Electricity derivative contracts held for trading

The maximum exposure to credit risk at the end of the reporting period is the carrying amount of each class of derivative financial asset mentioned in notes 16 and 24.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

3. FINANCIAL RISK MANAGEMENT continued

D. Fair value of financial instruments

The directors are of the opinion that the carrying amount of financial assets and financial liabilities recorded in the financial statements approximates their fair values.

The fair values of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions, and traded on active liquid markets, is determined with reference to quoted market prices;
- the fair value of other financial assets and financial liabilities is determined in accordance with generally accepted pricing models based on discounted cash flow analyses; and
- the fair value of derivative instruments included in hedging assets and liabilities is calculated using quoted prices. The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives and sales contracts) is determined using valuation techniques. The Group uses a variety of methods, such as estimated discounted cash flows, and makes assumptions that are based on market conditions existing at each balance date. These amounts reflect the estimated amount which the Group would be required to pay or receive to terminate (or replace) the contracts at their current market rates at balance date.

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes.

The following table presents the Group's assets and liabilities measured and recognised at fair value at 30 June 2011.

	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
As at 30 June 2011				
Assets				
Financial assets at fair value through profit or loss				
Electricity derivatives contracts	-	542	-	542
Total assets	-	542	-	542
Liabilities				
Financial assets at fair value through profit or loss				
Electricity derivatives contracts	1,061	38,615	-	39,676
Derivatives used for hedging	-	17,369	-	17,369
Total liabilities	1,061	55,984	-	57,045
As at 30 June 2010				
Assets				
Financial assets at fair value through profit or loss				
Electricity derivatives contracts	-	409	-	409
Total assets	-	409	-	409
Liabilities				
Financial assets at fair value through profit or loss				
Electricity derivatives contracts	-	60,860	-	60,860
Derivatives used for hedging	-	26,001	-	26,001
Total liabilities	-	86,861	-	86,861

3. FINANCIAL RISK MANAGEMENT continued

D. Fair value of financial instruments continued

Level 1

The fair value of financial instruments traded in active markets is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Group is the current bid price.

Level 2

The fair values of financial instruments that are not traded in an active market are determined using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at the end of each reporting period. Quoted market prices or dealer quotes for similar instruments are used to estimate fair value for long-term debt for disclosure purposes. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward exchange contracts is determined using forward exchange market rates at the end of the reporting period.

Level 3

A valuation technique for these instruments is based on significant unobservable inputs.

E. Capital risk management

The Group manages its capital so that it will be able to continue as a going concern while maximising the return to stakeholders through an appropriate mix of debt and equity. The capital structure of the Group as at balance date consists of total corporate facilities, as listed in note 23, total limited recourse facilities as listed in note 23 and equity, comprising issued capital, reserves and retained earnings as listed in notes 26 and 27. The Group does not hold recourse corporate debt. All debt at balance date is limited recourse and unsecured debt.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group is required to provide prudential credit support to various parties which it does through provision of bank guarantees or cash collateral. It also has a working capital facility in place which is settled each month. Virtually all of the Group debt is in the form of limited recourse project finance provided directly to power stations in which the Group has an interest.

The quantitative analysis of each of these categories of capital is provided in their respective notes to the accounts.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that may have a financial impact on the Group and that are believed to be reasonable under the circumstances.

(a) Critical accounting estimates and assumptions

The Group makes estimates and assumptions concerning variables. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Estimated impairment of goodwill

The Group tests annually whether goodwill has suffered any impairment in accordance with the accounting policy stated in note 1 (o). The recoverable amounts of cash-generating units have been determined based on value-in-use calculations, where applicable. These calculations require the use of assumptions. Provisional goodwill in relation to the acquisition of SAGE has not been tested for impairment as this goodwill has not been allocated to a cash generating unit at 30 June 2011. Refer to note 21 for details.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS continued

(a) Critical accounting estimates and assumptions continued

Impact of Carbon Tax on carrying value of assets

Directors are of the view that the Carbon Tax Plan introduced on 10 July 2011 will not have any negative impact on the recoverability of any assets of the Group.

Share-based payment transactions

The Company measures the cost of shares and options issued to employees and third parties by reference to the fair value of the equity instruments at the date at which they are granted. The fair value of unlisted options is determined using the Black-Scholes method taking into account the terms and conditions upon which the instruments were granted.

Deferred tax assets

The Group has recognised deferred tax assets relating to carried forward tax losses to the extent there are sufficient taxable temporary differences (deferred tax liabilities) relating to the same taxation authority against which the unused tax losses can be utilised. However, utilisation of the tax losses also depends on the ability of the entity to satisfy certain tests at the time the losses are recouped.

(b) Critical judgements in applying the entity's accounting policies

Recoverability of exploration costs

All exploration, evaluation and development costs are capitalised to the extent that they are expected to be recouped through the successful development of the area or where activities in the area have not yet reached a stage which permits reasonable assessment of the existence of economically recoverable reserves and active or significant operations in relation to the area are continuing. The probability of expected future economic benefits is assessed using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset. In this assessment, greater weighting is given to available external evidence.

Exploration and evaluation assets are reclassified as development assets at the point in which technical feasibility and commercial viability of extracting gas are demonstrated or a petroleum lease is granted. Exploration and evaluation assets are assessed for impairment and any impairment loss recognised before reclassification.

Fair value of financial instruments

The fair value of financial assets and financial liabilities are estimated for recognition and measurement and for disclosure purposes. Management uses its judgement in selecting appropriate valuation techniques for financial instruments not quoted in active markets. Valuation techniques commonly used by market practitioners are applied. For derivative financial instruments, assumptions are made based on quoted market rates adjusted for specific features of the instrument. Other financial instruments are valued using a discounted cash flow analysis based on assumptions supported, where possible, by observable market prices and rates. Refer to note 3 for further details of valuation methods used by the Group to determine fair value.

Purchase price allocation

AASB 3 Business Combinations requires the recognition of fair value estimates of assets and liabilities acquired. By the nature of these estimates, judgements are made on the allocation of the purchase consideration.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

5. REVENUE

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
<i>Revenue from Continuing Operations</i>		
Sale of electricity	483,631	285,509
Electricity generation revenue	47,055	80,090
Project fees	9,200	9,737
Sale of Gas	30	517
Interest income	4,647	2,759
	544,563	378,612

Refer to note 2 for further information regarding transactions between entities within the Group that have been eliminated on consolidation.

6. EXPENSES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Cost of electricity sales	473,492	314,167
Employee benefits expense	20,158	23,055
Other expenses	11,193	13,819
	504,843	351,041
Included in the above are:		
Rental expenses relating to operating leases	1,309	1,546
Foreign exchange (gains) and losses	8	291
Defined contribution superannuation expense	1,723	1,351
Equity settled share based payment compensation	277	327

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

7. NET FAIR VALUE GAIN / (LOSS) ON FINANCIAL INSTRUMENTS DESIGNATED AT FAIR VALUE THROUGH PROFIT AND LOSS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Unrealised		
Electricity derivative contracts	20,602	(49,868)
Option contract	-	(6,498)
	20,602	(56,366)
Realised		
Electricity derivative contracts	-	19,104
Interest rate swaps	(6,415)	-
	(6,415)	19,104
	14,187	(37,262)

In the absence of hedge accounting, the Group's electricity derivatives and foreign exchange contracts are designated at fair value through profit or loss.

8. FINANCE COSTS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Borrowing costs – bank loans	18,447	44,886
Borrowing costs – convertible notes	8,953	7,799
Other borrowing costs	2,393	8,667
Less: Amounts included in qualifying assets	-	(21,582)
	29,793	39,770

9. INCOME TAX

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
(a) Income tax expense / (benefit)		
Income tax comprises:		
Current tax expense / (benefit)	(231)	(11,664)
Deferred tax expense / (benefit)	3,738	6,346
Under / (over) provided in prior years	1,098	-
Income tax expense / (benefit)	4,605	(5,318)
Deferred income tax included in income tax expense / (benefit) comprises:		
Decrease / (increase) in deferred tax asset	26,509	(18,721)
(Decrease) / increase in deferred tax liabilities	(21,491)	14,749
Prior period acquired deferred tax asset de-recognised in current period on consolidation	-	13,325
Prior period acquired deferred tax liability de-recognised in current period on consolidation	-	(4,785)
Prior year under / (over) provision of deferred tax expense	(1,280)	1,778
Deferred income tax expense / (benefit)	3,738	6,346
(b) Numerical reconciliation of prima facie tax benefit to prima facie tax		
Profit / (loss) from continuing operations	20,824	(21,071)
Income tax expense calculated at 30%	6,247	(6,321)
Differences between Braemar 2 accounting and tax deconsolidation	-	481
Effect of permanent differences on Kwinana disposal	398	-
Effect of expenses that are not deductible in determining taxable profit	119	598
Other permanent differences	(3,257)	(76)
Under / (over) provided in prior year	1,098	-
Income tax expense / (benefit)	4,605	(5,318)
(c) Amounts recognised directly in other comprehensive income		
(Increase) / decrease in equity due to current and deferred amounts charged directly to equity during the period:	-	-
Net tax effect of amounts charged to hedge reserve	1,607	(3,023)
	1,607	(3,023)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

9. INCOME TAX (continued)

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
(d) Tax losses		
Tax losses for which deferred tax asset is recognised in the current period	771	38,881
Potential tax benefit at 30%	231	11,664
(e) Current tax liabilities		
Current tax payables:	-	-
Income tax payable	-	46
(f) Recognised deferred tax assets and deferred tax liabilities		
Deferred tax assets		
Carried forward tax losses	10,979	28,787
Capitalised borrowing costs	210	1,050
Derivative financial instruments	17,189	26,434
Employee provisions	1,519	382
Project development costs	-	893
Other miscellaneous	42	3
Fixed assets	3,516	3,516
	33,455	61,065
Deferred tax liabilities		
Trade and other receivables	-	(14,540)
Property, plant and equipment	(18,695)	(29,704)
Capitalised exploration expenditure (Gas)	(3,660)	(1,905)
Other	(1,071)	-
	(23,426)	(46,149)

Tax consolidation

The Company and its wholly-owned Australian controlled entities, has implemented the tax consolidation legislation.

The entities in the tax consolidated Group have entered into tax sharing agreements which, in the opinion of the directors, limits the joint and several liability of the wholly-owned entities in the case of a default by the head entity being ERM Power Limited.

The entities in the tax consolidated Group have also entered into tax funding agreements under which the wholly-owned entities fully compensate the head entity for any current tax payable assumed and are compensated by the head entity for any current tax receivable and deferred tax assets relating to unused tax losses or unused tax credits that are transferred to the head entity under the tax consolidation legislation. The funding amounts are determined by reference to the amounts recognised in the wholly-owned entities' financial statements. The amounts receivable/payable under the tax funding agreement are due upon receipt of the funding advice from the head entity, which is issued as soon as practicable after the end of each financial year. The head entity may also require payment of interim funding amounts to assist with its obligations to pay tax instalments. The funding amounts are recognised as current intercompany receivables or payables.

9. INCOME TAX (continued)

Deferred Tax Assets: Movements – Consolidated	Carried forward tax losses \$'000	Capitalised borrowing costs \$'000	Derivative financial liabilities \$'000	Employee provisions \$'000	Project development costs \$'000	Fixed cost adjustments \$'000	Other \$'000	Total \$'000	Held for sale \$'000	Total \$'000
At 1 July 2009	16,400	214	22,127	1,187	1,115	5,130	133	46,306	(13,325)	32,981
(Charged) / credited to profit or loss	12,387	836	7,330	(805)	(222)	(1,614)	(130)	17,782	13,325	31,107
to other comprehensive income	-	-	(3,023)	-	-	-	-	(3,023)	-	(3,023)
At 30 June 2010	28,787	1,050	26,434	382	893	3,516	3	61,065	-	61,065
(Charged) / credited to profit or loss	(17,808)	(840)	(8,144)	1,137	(893)	-	39	(26,509)	-	(26,509)
to other comprehensive income	-	-	(1,101)	-	-	-	-	(1,101)	-	(1,101)
At 30 June 2011	10,979	210	17,189	1,519	-	3,516	42	33,455	-	33,455

Deferred Tax Liabilities: Movements - Consolidated	Derivative financial assets \$'000	Receivables and accrued income \$'000	Capitalised exploration costs \$'000	Capitalised construction costs \$'000	Prepayments \$'000	Other \$'000	Total \$'000	Held for sale \$'000	Total \$'000
At 1 July 2009	(1,949)	(6,050)	(957)	(26,907)	(145)	(177)	(36,185)	4,785	(31,400)
Charged / (credited) to profit or loss	1,949	(8,490)	(948)	(2,797)	145	177	(9,964)	(4,785)	(14,749)
to other comprehensive income	-	-	-	-	-	-	-	-	-
At 30 June 2010	-	(14,540)	(1,905)	(29,704)	-	-	(46,149)	-	(46,149)
(Charged) / (credited) to profit or loss	-	14,540	(1,755)	9,777	-	(1,071)	21,491	-	21,491
to other comprehensive income	-	-	-	1,232	-	-	1,232	-	1,232
At 30 June 2011	-	-	(3,660)	(18,695)	-	(1,071)	(23,426)	-	(23,426)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

10. DIVIDENDS PAID AND PROPOSED

During the year ended 30 June 2011, no dividend was paid by the Company (2010: Nil).

After 30 June 2011 the following dividends were proposed by the directors. The dividends have not been provided for and there are no income tax consequences.

	Cents per share	Total amount \$'000	Franked / Unfranked	Date of payment
Final ordinary	3.5	5,674	Franked	19 October 2011

	2011 \$'000	2010 \$'000
Franking credits available to shareholders in subsequent years	13,595	13,211

The franking account balance is adjusted for:

- franking credits that will arise from the payment of income tax;
- franking debits that will arise from the payment of dividends recognised as a liability at the reporting date; and
- franking credits that will arise from the receipt of dividends recognised as receivables at the reporting date.

The consolidated amounts include franking credits that would be available to the parent entity if distributable profits of subsidiaries were paid as dividends. The impact on the franking account of the dividend recommended by the directors since the end of the reporting period, but not recognised as a liability at the reporting date, will be a reduction in the franking account of \$2,431,714.

11. CASH AND CASH EQUIVALENTS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Current		
Non-restricted cash at bank and cash on hand	110,153	20,046
Restricted cash	74,111	39,432
	184,264	59,478
Non-current		
Restricted cash	2,091	3,032
	2,091	3,032
Total cash and cash equivalents	186,355	62,510
Restricted cash	76,202	42,464
Non-restricted cash	110,153	20,046
	186,355	62,510

The cash and cash equivalents are bearing interest at rates between nil and 5%.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

11. CASH AND CASH EQUIVALENTS continued

Restricted cash

Restricted cash deposits are held as cash-backed guarantees in respect of coupon payments due for the convertible notes issued and to provide credit support for the Group's electricity derivative contracts. The restricted cash deposits, held on term deposit, are bearing interest at rates between 4% and 5%.

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Term deposits	68,072	26,531
Other restricted cash deposits	8,130	15,933
	76,202	42,464

12. (a) RECONCILIATION OF CASH FLOWS USED IN OPERATING ACTIVITIES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Net profit / (loss) after tax	16,219	(15,753)
<i>Adjustments for:</i>		
Depreciation and amortisation of non-current assets	9,977	12,722
Interest income	(4,647)	(2,759)
Share based payment expense	277	-
Share of associate's net profit	(1,436)	(1,321)
Net fair value (gains) / losses on financial instruments	(14,187)	37,262
Finance costs	29,793	39,025
Gain on disposal of assets	(4,738)	(36,379)
<i>Transfers to/(from) provisions:</i>		
Employee entitlements	(12)	380
<i>Changes in assets and liabilities net of purchase of subsidiary and divestment of Kwinana:</i>		
(Increase) / decrease in trade and other receivables	51,612	(60,203)
(Increase) / decrease in other assets	(1,159)	(6,416)
(Increase) / decrease in inventories	(1,667)	(650)
(Increase) / decrease in deferred tax assets	18,631	(28,085)
Net movement in derivatives	-	73,776
(Decrease) / increase in deferred tax liabilities	(9,913)	14,749
(Decrease) / increase in current tax liability	(46)	(9,112)
(Decrease) / increase in trade and other payables	20,399	(9,724)
Net cash provided (used in)/by operating activities	109,103	7,512

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

12. (b) NON-CASH INVESTING AND FINANCING ACTIVITIES

	Note	CONSOLIDATED	
		2011 \$'000	2010 \$'000
Issue of shares – SAGE acquisition	26	2,334	-
		2,334	-

Disclosure of financing facilities

Refer to note 23 for information regarding financing facilities.

13. TRADE AND OTHER RECEIVABLES

	Note	CONSOLIDATED	
		2011 \$'000	2010 \$'000
Current			
Trade receivables	(i)	479	6,923
Amount receivable from third party	(ii)	-	62,960
Amounts receivable from jointly controlled entities	(iii)	-	4,034
Other receivables		199	199
Amounts receivable from employee shareholders	(v)	454	-
		1,132	74,116
Accrued income	(iv)	44,049	29,631
		45,181	103,747
Non-current			
Amounts receivable from employee shareholders	(v)	2,101	2,052
Amount receivable from external party		455	555
		2,556	2,607

(i) Trade receivables are non-interest bearing and are generally on 30-day terms. An allowance for doubtful debts is made when there is objective evidence that a trade receivable is impaired. An allowance of \$7,857 (2010: \$266,000) has been recognised as an expense for the current year for specific debtors for which such evidence exists. The amount of the allowance / impairment loss is measured as the difference between the carrying amount of the trade receivables and the estimated future cash flows expected to be received from the relevant debtors.

(ii) Amount receivable from Arrow relating to the sale of the interest in the Braemar 2 power station. This amount was received on 30 June 2011.

(iii) Loans to jointly controlled entities are interest-free and are subject to loan deeds.

(iv) Accrued income represents electricity amounts due to be invoiced on 1 July 2011.

(v) Employee shareholder loans are subject to loan deeds and interest is charged at the FBT benchmark rate.

Details regarding the effective interest rate and credit risk of current receivables are disclosed in Note 3.

Impaired receivables and receivables past due

None of the non-current receivables are impaired or past due but not impaired. The carrying amounts of non-current receivables are equal to the fair values.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

14. INVENTORIES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Renewable energy certificates	3,081	759
Gas in storage	58	41
	3,139	800

15. OTHER ASSETS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Current		
Prepayments ⁽¹⁾	1,337	4,455
Security deposits ⁽²⁾	3,149	3,831
	4,486	8,286

⁽¹⁾ Prepayments predominantly consist of amounts for prepaid gas.

⁽²⁾ Refer to Note 30 for further details regarding security deposits.

16. DERIVATIVE FINANCIAL INSTRUMENTS – ASSETS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Current		
Electricity derivatives	499	409
	499	409
Non-current		
Electricity derivatives	43	-
	43	-

Refer to note 3 for further information regarding financial instruments used by the Group.

Refer to note 24 for Derivative Financial Instruments - Liabilities.

17. INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

Investment in Associates

Name of the entity	Principal activity	Place of incorporation	Reporting date	Ownership interest	
				2011 %	2010 %
Oakey Power Holdings Pty Ltd ("Oakey")	Power generation	NSW	30 June	12.5	12.5

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

17. INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD continued

The Group accounts for its investment in Oakey as an associate because the Group has the ability to exercise significant influence over the investment due to its voting power via representation on the Oakey Board of directors and key decision making committees.

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Movements in carrying amounts		
Carrying amount at the beginning of the financial year	17,675	17,584
Dividend received/receivable	(570)	(1,230)
Share of profit after tax	1,436	1,321
Carrying amount at the end of the financial year	18,541	17,675
Share of associate's profit or losses		
Revenue	4,296	4,131
Profit before income tax	2,052	1,876
Income tax expense	(616)	(555)
Profit after income tax	1,436	1,321
Summarised financial information of associate not adjusted for percentage ownership		
Current assets	7,524	7,307
Non-current assets	105,080	111,234
Total assets	112,604	118,541
Current liabilities	14,775	14,225
Non-current liabilities	62,998	76,416
Total liabilities	77,773	90,641
Net assets	34,831	27,900
Share of associate's expenditure commitments		
Capital commitments	-	-
Lease commitments	-	-
	-	-

Restriction on funds distributed to shareholders

Oakey may make a distribution to its shareholders in the form of cash dividends and repayment of shareholder loans when the required levels have been met in the Debt Service Reserve Account (DSRA) and the Major Maintenance Reserve Account (MMRA), as required by the terms of its Credit Facility Agreement. The DSRA is an amount necessary to ensure there is a balance equal to the sum of the principal and interest amounts and the Bank Guarantee fees scheduled to be paid during the next six months. The MMRA is required to be maintained from financial close until the first major overhaul of the plant. As at 30 June 2011, the DSRA was \$8.5 million (2010: \$8.6 million), and the MMRA was \$2.5 million (2010: \$2.2 million). There are no other restrictions on distribution to shareholders.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

18. INVESTMENT IN CONTROLLED ENTITIES

Name	Place of incorporation	Percentage of equity interest held by the Company	
		2011 %	2010 %
DIRECT HOLDINGS			
ACN 139 091 866 Pty Ltd	QLD	-	100
EIT Kwinana Genco Pty Ltd	VIC	-	100
Arrow Braemar 2 Holdings Pty Ltd	VIC	-	100
ERM Braemar 3 Power Pty Ltd	QLD	100	100
Arrow Braemar Power Pty Ltd	QLD	-	50.1
ERM Financial Services Pty Ltd	QLD	100	100
ERM Gas Pty Ltd	QLD	100	100
ERM Holdings Pty Ltd	QLD	100	100
ERM Neerabup Holdings Pty Ltd	QLD	100	100
ERM Neerabup Power Pty Ltd	VIC	100	100
ERM Power Developments Pty Ltd	VIC	100	100
ERM Power Executive Option Plan Manager Pty Ltd	NSW	100	100
ERM Power Generation Pty Ltd	VIC	50	50
ERM Power Retail Pty Ltd	VIC	100	100
ERM Power Services Pty Ltd	VIC	100	100
ERM Power Utility Systems Pty Ltd	VIC	100	-
INDIRECT HOLDINGS			
Braemar 3 Holdings Pty Ltd	QLD	100	100
Arrow Braemar 2 Power Pty Limited	VIC	-	50.1
Arrow Braemar 2 Pty Ltd	QLD	-	50.1
ERM Braemar 3 Pty Ltd	QLD	100	100
ERM Gas WA01 Pty Ltd	VIC	100	100
NewGen Kwinana Holdings Pty Ltd	VIC	-	30
EIT Kwinana Partner Pty Ltd	VIC	-	30
ERM Land Holdings Pty Ltd	QLD	100	100
ERM Neerabup Pty Ltd	VIC	100	100
EIT Kwinana Genco 1 Pty Ltd	QLD	-	100
ERM Power Generation Pty Ltd	VIC	100	100
EIT Power Investments Pty Ltd	QLD	-	60
MetroWest Convenience Store Pty Ltd	QLD	100	100
SAGE Utility Systems Pty Ltd	VIC	100	-
Summit Kwinana Holdings Pty Ltd	VIC	-	30
Summit Kwinana Power Pty Limited	VIC	-	30

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

19. PROPERTY, PLANT AND EQUIPMENT

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
<i>Plant and equipment</i>		
Cost	190,136	389,140
Accumulated depreciation and impairment	(10,554)	(13,507)
Net carrying amount	179,582	375,633
<i>Land</i>		
Carrying amount at cost	9,830	3,776
<i>Furniture and equipment</i>		
Cost	2,498	2,420
Accumulated depreciation and impairment	(2,035)	(1,520)
Net carrying amount	463	900
<i>Motor vehicles</i>		
Cost	87	87
Accumulated depreciation and impairment	(87)	(67)
Net carrying amount	-	20
<i>Software</i>		
Cost (gross carrying amount)	2,139	2,010
Accumulated amortisation and impairment	(1,434)	(812)
Net carrying amount	705	1,198
<i>Capital work in progress ⁽ⁱ⁾</i>	15,876	11,080
Total property, plant and equipment – net carrying	206,456	392,607

⁽ⁱ⁾ Capital work in progress relates to capitalised costs for power station projects.

Each of the Group's current generation assets, the Oakey and Neerabup power stations, are project financed by limited recourse debt, meaning the security of project lenders does not extend beyond the Group's interest in the particular generation asset. The Group also raised funds for its equity investment in the Neerabup power station by issuing notes. Those notes are limited-recourse to the Group's interest in the Neerabup power station.

Refer note 23 for details regarding recourse and limited recourse borrowings of the Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

19. PROPERTY, PLANT AND EQUIPMENT (continued)

	Note	CONSOLIDATED	
		2011 \$'000	2010 \$'000
Reconciliations			
<i>Plant and equipment</i>			
Net of accumulated depreciation and impairment at start of year		375,633	196,315
Transfers from capital work in progress		-	185,110
Additions		2,009	4,205
Disposals		(189,266)	-
Depreciation		(8,794)	(9,997)
Net of accumulated depreciation and impairment at end of year		179,582	375,633
 <i>Land</i>			
At start of year		3,776	253
Additions		6,054	2,199
Transfers from capital work in progress		-	1,324
At end of year		9,830	3,776
 <i>Furniture and equipment</i>			
Net of accumulated depreciation and impairment at start of year		900	1,576
Additions		97	43
Acquired through business combination	36	4	-
Disposals		-	(45)
Depreciation		(538)	(674)
Net of accumulated depreciation and impairment at end of year		463	900
 <i>Motor vehicles</i>			
Net of accumulated depreciation and impairment at start of year		20	43
Depreciation		(20)	(23)
Net of accumulated depreciation and impairment at end of year		-	20
 <i>Software</i>			
Net of accumulated depreciation and impairment at start of year		1,198	933
Additions		129	822
Disposals		-	(19)
Amortisation		(622)	(538)
Net of accumulated depreciation and impairment at end of year		705	1,198

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

20. EXPLORATION AND EVALUATION COSTS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
<i>Exploration and evaluation costs</i>		
Cost (gross carrying amount)	11,435	6,569
Accumulated amortisation and impairment	-	-
Net carrying amount	11,435	6,569
Reconciliation		
Net of accumulated amortisation and impairment at start of year	6,569	3,191
Additions	4,866	3,378
Net of accumulated amortisation and impairment at end of year	11,435	6,569

21. INTANGIBLE ASSETS

	Note	CONSOLIDATED	
		2011 \$'000	2010 \$'000
<i>Goodwill</i>			
Cost (gross carrying amount)		1,882	9,740
Accumulated impairment		-	(3,925)
Net carrying amount		1,882	5,815
Reconciliation			
Net of accumulated amortisation and impairment at start of year		5,815	5,815
Disposals		(5,815)	-
Acquired through business combination	36	1,882	-
Net of accumulated amortisation and impairment at end of year		1,882	5,815

Impairment test for goodwill

As the SAGE acquisition accounting is provisional the Group has not finalised the allocation or amount of goodwill. Refer note 2 and note 36.

22. TRADE AND OTHER PAYABLES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Current		
Trade creditors and accruals	41,777	34,414
Other creditors	21,258	16,896
	63,035	51,310

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

23. BORROWINGS

	Note	CONSOLIDATED	
		2011 \$'000	2010 \$'000
Current			
<i>Unsecured</i>			
Other loans – related parties	(i)	-	7,956
<i>Secured</i>			
Obligations under finance leases		-	17
Total borrowings		-	7,973
<i>Secured limited recourse</i>			
Bank loan – Kwinana working capital facility	(ii)	-	3,501
Bank loan – Neerabup working capital facility	(iii)	1,500	1,500
Bank loans – Neerabup term facility (current portion)	(iv)	3,219	-
Total limited recourse borrowings		4,719	5,001
		4,719	12,974
Non-current			
<i>Unsecured</i>			
Other loans – related parties	(v)	4,400	-
<i>Secured</i>			
Loans – other parties	(vi)	-	25,140
Total borrowings		4,400	25,140
<i>Secured limited recourse</i>			
Bank loans – Kwinana term facility	(vii)	-	155,857
Bank loans – Neerabup term facility	(iv)	159,552	168,061
Convertible notes	(viii)	43,023	69,290
Total limited recourse borrowings		202,575	393,208
		206,975	418,348

Information on credit risk, fair value and interest rate risk exposure of the Group is provided at note 3.

- (i) Loans of \$8.0 million from a director related entity bearing interest at BBSY plus 4% were repaid during the period.
- (ii) Amounts drawn down on a limited recourse bank working capital facility by NewGen Power Kwinana partnership. These borrowings were part of the Group's interest in the Kwinana power station which was disposed of in October 2010.
- (iii) Amounts drawn down on a limited recourse bank working capital facility by the Neerabup partnership. This facility has recourse to the assets of the Neerabup partnership only which is proportionately consolidated into the Group.
- (iv) Amounts drawn down on a limited recourse term debt facility in respect of the Neerabup partnership. This facility has recourse to the assets of the Neerabup partnership only which is proportionately consolidated into the Group.
- (v) Loan of \$4.4 million from director related entity drawn down on 30 June 2011 in relation to funding of additional 50% interest in Oakey acquisition. Refer notes 32 and 38 for further details. Loan is interest bearing at 12% per annum.
- (vi) Loan from third party repaid in December 2010.
- (vii) Amounts drawn down on a limited recourse term debt facility in respect of the Kwinana Partnership. The interest in which was disposed of in October 2010.
- (viii) Convertible notes are redeemable by the issuer from 30 September 2010 until maturity in February 2023. Notes have a coupon rate fixed at 4% p.a. until 30 September 2009, 11% until 11 February 2010, and then the rate is variable based on BBSY plus 4%. The notes are accounted for using the effective interest method at 10.5% (2010: 10.55%). The notes can only be converted to shares in the issuing subsidiary upon failure to redeem them at maturity or other named event of default. The notes have recourse to the Group's 50% interest in the Neerabup partnership only.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

23. BORROWINGS continued

Financing facilities available

The Group's financing facilities predominantly relate to limited recourse power station development activities. Funding is drawn down progressively according to project time lines. At balance date, the following financing facilities had been negotiated and were available:

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Total facilities – bank loans	187,578	430,434
Facilities used at balance date – bank loans	166,234	383,482
Facilities unused at balance date – bank loans	21,344	46,952

24. DERIVATIVE FINANCIAL INSTRUMENTS – LIABILITIES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Current		
Electricity derivatives	27,091	39,601
	27,091	39,601
Non-current		
Electricity derivatives	12,585	21,259
Interest rate swaps	17,369	26,001
	29,954	47,260

Refer to note 3 for further information regarding financial instruments used by the Group

25. PROVISIONS

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Current		
Employee benefits – annual leave	1,079	1,122
	1,079	1,122
Non-current		
Employee benefits – long service leave	50	36
	50	36

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

26. CONTRIBUTED EQUITY

	Note	CONSOLIDATED		CONSOLIDATED	
		2011 Number of shares	2010 Number of shares	2011 \$'000	2010 \$'000
Issued ordinary shares – fully paid	26(a)	162,140,656	50,454,354	161,137	60,573
Treasury shares	26(b)	(513,072)	-	(898)	-
		161,627,584	50,454,354	160,239	60,573
(a) Movement in ordinary share capital					
At the beginning of the period		50,454,354	50,199,463	60,573	60,012
Issue of shares – employee incentive scheme		1,656,786	254,891	4,300	561
Exercise of options		202,999	-	170	-
Issue of shares – SAGE acquisition		1,368,854	-	2,334	-
Share split 2:1		51,314,805	-	-	-
Issue of shares – initial public offering (net of transaction costs)		57,142,858	-	93,760	-
At the end of the period		162,140,656	50,454,354	161,137	60,573

(b) Terms and conditions of contributed equity

Ordinary shares

During the year, the Company conducted an initial public offering raising \$100 million from the issue of 57,142,858 ordinary fully paid shares at \$1.75 per share.

Ordinary shares have the right to receive dividends as declared and, in the event of winding up the Company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of shares held.

Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the Company.

Ordinary shares have no par value and the company does not have a limited amount of authorised capital.

Treasury shares

Treasury shares are shares that are held in trust for the purpose of issuing shares under employee share incentive schemes. Details of shares and options issued under employee share schemes (see note 28).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

27. RESERVES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Cash flow hedge reserve	(12,158)	(24,615)
Asset revaluation reserve	-	2,876
Share option reserve	603	327
	(11,555)	(21,412)
Movements		
<i>Cash flow hedge reserve</i>		
Balance at the beginning of the year	(24,615)	(33,364)
Revaluation – gross	4,165	(9,597)
Revaluation – deferred tax	(1,249)	2,778
Sale of interest in jointly controlled entity – net of tax (note 35)	9,541	15,568
Balance at the end of the year	(12,158)	(24,615)
<i>Asset revaluation reserve</i>		
Balance at the beginning of the year	2,876	2,876
Disposal of subsidiary	(2,876)	-
Balance at the end of the year	-	2,876
<i>Share option reserve</i>		
Balance 1 July	327	-
Options expense	276	327
Balance 30 June	603	327

(a) Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

(b) Asset revaluation reserve

The revaluation reserve related to the revaluation of property, plant and equipment acquired via a stepped acquisition of a subsidiary. The purchase of a controlling interest in the Kwinana Power Station on 11 October 2007 resulted in an asset revaluation in respect of the initial acquisition of \$2.9 million after tax. Upon review of the carrying amount of the Kwinana Power Station asset when it was available for sale during the current year, the valuation of the asset was decreased by the amount of the existing revaluation surplus.

(c) Share option reserve

As at the date of this report, there were 10,069,209 options on issue to acquire fully paid ordinary shares. The options do not carry any entitlement to participate in any share issue. All options expire on the earlier of their expiry date or termination of the holder's employment, or as otherwise determined by the Board. Refer to note 28 for details of the employee share and option incentive schemes.

28. SHARE BASED PAYMENTS

(a) Short term incentives

During the year eligible employees received ordinary shares as a short term incentive bonus by way of an offer to participate in the Short Term Incentive Share Trust. The number of shares issued to participants during the year was 1,997,761 (inclusive of effect of 2 for 1 share split). The shares vested immediately on issue with the cost provided for in the 2010 financial year.

(b) Long term incentives

The objective of the Long Term Incentive Scheme is to provide incentives to focus on long term shareholder returns. Participation in the scheme is open to senior employees (including Executive Directors) who are invited by the Board.

Although a performance based award was not made during the year, the Company did award an incentive to certain employees for achieving the successful Initial Public Offering ("IPO"). The vesting conditions were targeted at the retention of those employees through to at least September 2012, being the prospectus forecast period, as well as twelve months beyond the forecast period.

These incentive awards were granted by way of offers to participate in both the Long Term Incentive Share Trust (LTIST) and the Long Term Incentive Option Trust (LTIOT).

i. LTIST

Shares will be acquired by a trustee who will hold those Shares on behalf of participants. The Shares will be acquired by the trustee either subscribing for new Shares or purchasing Shares on market. Vesting conditions may be a combination of service and performance hurdles, as determined by the Directors.

Participants hold their interest in the Long Term Incentive Share Trust ("LTIST") by holdings units, where one unit represents one Share. Participants are issued units at the prevailing market value of the Shares. A participant may instruct the trustee how to exercise its vote in the case of a poll at a meeting of ERM Power. If the participant's employment ceases prior to the Shares vesting, the participant's units in the LTIST will be forfeited.

Early vesting may occur in the following circumstances, subject to the participant achieving any relevant performance hurdles, as set out below:

- On a change of control of ERM Power, being a material change in the composition of the Board initiated as a result of a change of ownership of Shares and the purchaser of the Shares requiring (or agreeing with other Shareholders to require) that change in Board composition, or in other circumstances that the Board determines appropriate.
- On termination of employment due to redundancy, death or permanent disability, or in circumstances that the Board determines appropriate.

The number of shares issued under the plan to employees during the year was 513,072 (2010 – not applicable). Subject to continuation of employment of the participants, 33% of those shares will vest in September 2012 with the balance to vest in September 2013. The value of the shares at grant date was \$1.75 per share with the expense to be allocated over the vesting periods.

ii. LTIOT

Participants are issued units at the prevailing market value of the Options. If the participant's employment ceases prior to the Options vesting, the participant's options will be forfeited.

Early vesting may occur in the same circumstances as the Long Term employee share scheme, subject to achieving any relevant performance hurdles.

Set out below are summaries of options granted under the plan during the current financial year with vesting conditions subject to continuation of employment in September 2012:

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

28. SHARE BASED PAYMENTS continued

(b) Long term incentives continued

Grant Date	Expiry date	Exercise price	Balance at start of the year Number	Granted during the year Number	Forfeited during the year Number	Options exercised during the year Number	Balance at end of the year Number	Vested and exercisable at end of the year Number
1/11/2010	1/11/2017	2.75	-	1,296,400	-	-	1,296,400	-
8/11/2010	8/11/2017	2.75	-	242,706	-	-	242,706	-
Total			-	1,539,106	-	-	1,539,106	-

The weighted average remaining contractual life of share options outstanding at the end of the period was 6 years (2010 – not applicable).

Fair value of options granted

The assessed fair value at grant date of options granted during the year ended 30 June 2011 was 10.43 cents. The fair value at grant date is determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk free interest rate for the term of the option.

The model inputs for options granted during the year ended 30 June 2011 included:

- Share price at grant date: \$1.75;
- Exercise price: \$2.75;
- Expected price volatility of the Company's shares: 28.1%;
- Risk free interest rate: 5.69%; and
- Expected vesting date: 3 years after issue.

Employee Option Plan 2008

In June 2008, the Company made offers to certain employees to participate in the Employee Option Plan ("EOP") and granted Options with a five year exercise period and an exercise price of \$0.806. There are no performance conditions attached to the Options issued under the EOP.

Details of the 2008 option plan, the options in which vested in the financial year, are summarised below:

Grant Date	Expiry date	Exercise price	Balance at start of the year Number	Granted during the year Number	Forfeited during the year Number	Options exercised during the year Number	Balance at end of the year Number	Vested and exercisable at end of the year Number
6/06/2008	6/06/2013	0.806	10,524,962	-	496,550	209,203	9,819,209	9,819,209
30/06/2008	30/06/2013	0.806	400,000	-	150,000	-	250,000	250,000
Total			10,924,962	-	646,550	209,203	10,069,209	10,069,209

The weighted average share price from the date of listing on 10 December 2010 to 30 June 2011 was \$1.8388 (2010 – not applicable).

28. SHARE BASED PAYMENTS continued

(c) Amounts expensed in respect of share-based payment transactions

Expenses recognised in respect of share-based payment transactions during the period as part of employee benefit expense:

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Options issued under employee option plans	167	327
Shares issued under long term employee share scheme	110	-
	277	327

29. PARENT ENTITY FINANCIAL INFORMATION

(a) Summary financial information

The individual financial statements for the parent entity show the following aggregate amounts:

	2011 \$'000	2010 \$'000
Statement of financial position		
Current Assets	212,917	134,279
Total Assets	286,467	214,908
Current Liabilities	71,848	65,785
Total liabilities	78,270	104,717
<i>Shareholders' equity</i>		
Contributed equity	161,136	60,573
Treasury shares	(898)	-
Reserves		
Share option reserve	603	327
Retained earnings	47,356	49,291
	208,197	110,191
(Loss) / profit for the year	(1,937)	10,398
Total comprehensive (loss) / income	(1,937)	10,398

(b) Guarantees entered into by the parent entity

The Company has provided bank guarantees in relation to its lease arrangements for premises in Brisbane totalling \$522,000 (2010: \$418,600).

(c) Contingent liabilities of the parent entity

The Company does not have any contingent liabilities at 30 June 2011.

(d) Contractual commitments for acquisition of property, plant and equipment

There are no contractual commitments for the acquisition of property, plant and equipment at 30 June 2011.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

30. COMMITMENTS AND CONTINGENCIES

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
(a) Capital expenditure commitments		
Estimated capital expenditure contracted for at balance date, not provided for but payable (including share of associates and joint ventures):		
– not later than one year	4,076	23,224
– later than one year and not later than five years	-	-
– later than five years	-	-
	4,076	23,224
(b) Lease expenditure commitments		
<i>(i) Operating leases (non-cancellable):</i>		
Minimum lease payments		
– not later than one year	1,272	1,131
– later than one year and not later than five years	1,649	2,826
– later than five years	-	286
Aggregate lease expenditure contracted for at balance date	2,921	4,243
<i>(ii) Finance leases:</i>		
Minimum lease payments		
– not later than one year	-	18
– later than one year and not later than two years	-	-
Total minimum lease payments	-	18
Future finance charges	-	(1)
Net liability	-	17
Classified as follows:		
Current liability	-	17
Non-current liability	-	-
	-	17

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

30. COMMITMENTS AND CONTINGENCIES continued

Details of contingent liabilities are set out below. The directors are of the opinion that provisions are not required in respect of these items as it is not probable that a future sacrifice of economic benefits will be required or the amount is not capable of reliable measurement.

	Note	CONSOLIDATED	
		2011 \$'000	2010 \$'000
Bank guarantees – Australian Energy Market Operator	(i)	38,000	12,800
Bank guarantees – Lease arrangements	(ii)	522	419
Financial bond	(iii)	-	4,900
Third party guarantee	(iv)	25,000	25,000
Futures margin deposits	(v)	2,732	-
Security deposits	(vi)	3,145	-
Bank guarantees – Western Power	(vii)	300	-
Bank guarantees - Powerlink	(viii)	2,200	-
		71,899	43,119

- (i) The Group has provided bank guarantees in favour of the Australian Energy Market Operator (formerly National Electricity Market Management Company) to support its obligations to purchase electricity from the national electricity market. Bank guarantees have also been provided to various counterparties in relation to electricity derivatives. These guarantees are supported by term deposits as detailed in note 11.
- (ii) The Group has provided bank guarantees in relation to lease arrangements for premises in Brisbane. The guarantee is secured by a registered charge over all assets and undertakings of the Company (being ERM Power Limited).
- (iii) The Group had drawn down on a financial bond with a financial institution in order to provide reserve capacity security to the independent market operator in Western Australia.
- (iv) The Company and one of its subsidiaries had issued a guarantee to a third party under a credit support facility agreement. The third party has provided credit support in favour of the Group in relation to electricity derivatives. The guarantee is secured by assets held in a director related entity.
- (v) Futures margin deposits represent interest bearing cash lodged with the Group's futures clearing brokers. The deposits are in relation to various futures contracts on the Australian Stock Exchange and may be retained by the clearing brokers in the event that the Group does not meet its contractual obligations.
- (vi) Security deposits represent interest bearing cash lodged as eligible credit support with various counterparties to the Group's electricity derivative contracts and may be retained by those counterparties in the event that the Group does not meet its contractual obligations.
- (vii) The Group has provided a bank guarantee in favour of Western Power. This can be called upon if the Neerabup partnership fails to pay its monthly transmission invoices.
- (viii) The Group has provided a bank guarantee in favour of Powerlink for \$2.2 million under the B3 Connection Agreement.

The NewGen Neerabup Partnership is currently in dispute with a contractor responsible for the design and construct of the balance of plant works for the NewGen Neerabup Power Station. The dispute is currently being progressed through the dispute resolution provisions contained within the contract.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

31. INTERESTS IN JOINTLY CONTROLLED ENTITIES

	Interest Held	
	2011 %	2010 %
As at 30 June 2011, the Group has the following interests in power station projects with other external parties:		
Name		
NewGen Power Neerabup Pty Ltd	50	50
NewGen Neerabup Pty Ltd	50	50
NewGen Neerabup Partnership	50	50
NewGen Braemar 2 Pty Ltd	-	25.05
ERM Power Trust	50	50
Queensland Electricity Investors Pty Ltd	50	50
NewGen Power Kwinana Pty Ltd	-	30
NewGen Kwinana Holdings Pty Ltd	-	30
Summit Kwinana Holdings Pty Ltd	-	30
Summit Kwinana Power Pty Limited	-	30
ERM Kwinana Power Pty Ltd	-	30
NewGen Kwinana Partnership	-	30

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

31. INTERESTS IN JOINTLY CONTROLLED ENTITIES continued

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Net assets employed in the jointly controlled entities, including assets held for sale, are included in the financial statements as follows:		
CURRENT ASSETS		
Cash and cash equivalents	9,717	27,347
Trade and other receivables	3,471	11,754
Inventories	58	41
Prepayments	226	3,758
TOTAL CURRENT ASSETS	13,472	42,900
NON-CURRENT ASSETS		
Investment in associates accounted for using the equity method	12,914	12,914
Property, plant and equipment	199,733	381,090
TOTAL NON-CURRENT ASSETS	212,647	394,004
TOTAL ASSETS	226,119	436,904
CURRENT LIABILITIES		
Trade and other payables	764	6,830
Borrowings	4,719	5,001
Provisions	20	5
TOTAL CURRENT LIABILITIES	5,503	11,836
NON-CURRENT LIABILITIES		
Borrowings	159,552	321,793
Derivative financial instruments	17,369	26,001
TOTAL NON-CURRENT LIABILITIES	176,921	347,794
TOTAL LIABILITIES	182,424	359,630
NET ASSETS	43,695	77,274

Capital expenditure commitments

Estimated capital expenditure contracted for at balance date, not provided for but payable:

– not later than one year	4,076	8,242
– later than one year and not later than five years	-	-
– later than five years	-	-
	4,076	8,242

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

32. RELATED PARTY DISCLOSURES

Parent Company

ERM Power Limited is the parent entity of the consolidated entity. Balances and transactions between the parent entity and its wholly owned subsidiaries (which are related parties) have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the consolidated entity and other related parties are disclosed below.

Trevor St Baker and his related parties have a controlling shareholding in the Company at 30 June 2011.

Equity interests in subsidiaries

Details of interests in subsidiaries are set out in note 18.

Equity interests in associates

Details of interests in associates are set out in note 17.

Equity interests in jointly controlled entities

Details of interests in jointly controlled entities are set out in note 31.

Key management personnel

Disclosures relating to key management personnel are set out in note 33 and the Directors' Report.

Transactions with related parties

Transaction type	CONSOLIDATED		
	2011 \$'000	2010 \$'000	
<i>Loans from Directors</i>			
Loans received	i	4,400,000	250,889
Loan repayments	ii	7,955,955	4,119,807
Interest paid on director loans		-	676,713
<i>Director related entity transactions</i>			
Consulting fees	iii	304,447	475,150

- (i) Loan of \$4.4 million from a related entity of Trevor St Baker drawn down on 30 June 2011 in relation to funding of additional 50% interest in Oakey acquisition. Loan is interest bearing at 12% per annum.
- (ii) Loans of \$8.0 million from a director related entity bearing interest at BBSY plus 4% were repaid during the period.
- (iii) ERM Power has entered into a consulting agreement with Sunset Power Pty Ltd (a related party of Trevor St Baker) for Trevor St Baker to provide mentoring services and advice to ERM Power's planning group on a range of planning functions until 30 June 2011. Under this agreement ERM Power pays Sunset Power Pty Ltd a fee of \$3,500 per day for services provided (up to a maximum of 70 days per annum). Sunset Power Pty Ltd is also entitled to be reimbursed for all reasonable expenses incurred in providing these services. The consulting agreement may be terminated by giving 30 days written notice or immediately if Sunset Power breaches the agreement.

Other related party transactions

During the year, Stephen St Baker and Andrew St Baker were employed by the Company, either directly or on a contractor basis, on terms and conditions no more favourable than those that would have been adopted if dealing at arm's length with an unrelated person. Total payments excluding GST for the year ended 30 June 2011 were \$524,807 (2010: \$421,900).

There is no allowance account for impaired receivables in relation to any outstanding balances, and no expense has been recognised in respect of impaired receivables due from related parties.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

32. RELATED PARTY DISCLOSURES continued

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Transactions with jointly controlled entities:		
Net loans advanced/(repaid)	(4,582,604)	52,075,989
Current trade receivables	183,484	1,155,257
Current trade payables	(140,135)	-
Project fees	1,040,981	2,573,388
Operations management fees	5,548,633	3,269,684

33. KEY MANAGEMENT PERSONNEL DISCLOSURES

(a) Key management personnel compensation

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
Short-term employee benefits	2,573,842	2,214,886
Post-employment benefits	212,026	155,884
Termination benefits	-	20,000
Share-based payments	761,662	40,535
	3,547,530	2,431,305

Detailed remuneration disclosures are provided in the Remuneration Report on pages 31 to 39.

(b) Equity instruments disclosures relating to key management personnel

The number of shares and options held during the financial year by each director and other Key management personnel of the Group are disclosed in the Directors' Report.

(c) Loans to key management personnel

Details of loans made to directors and other key management personnel of the Group, including their related parties, are set out below:

Total individual loans

	Balance at the start of the year	Interest paid and payable for the year	Interest not charged	Balance at the end of the year	Number in Group at the end of the year
2011	1,163,642	83,354	-	1,246,996	4
2010	1,313,680	74,596	-	1,163,642	4

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

33. KEY MANAGEMENT PERSONNEL DISCLOSURES continued

Total Individuals with loans above \$100,000 during the financial year

	Balance at the start of the year	Interest paid and payable for the year	Interest not charged	Balance at the end of the year	Number in Group at the end of the year
2011	1,088,089	74,481	-	1,166,570	3
2010	1,242,377	74,845	-	1,088,089	3

The above loans to key management personnel include employee shareholder loans. In 2007 and 2008, ERM Power made offers to certain senior executives to participate in a share loan incentive plan. ERM Power provided loans to participants to enable them to subscribe for shares. The loans subject to loan deeds and are interest bearing at the FBT benchmark rate with recourse limited to the value of the shares. The loans are repayable in the event of termination of employment or otherwise between seven and 10 years from the date of advance.

Key management personnel and their related parties with loans greater than \$100,000 at 30 June 2011 and 30 June 2010 include Philip St Baker, Mitch Anderson and Andrew St Baker.

Further details regarding Director loans and other Director transactions are included in Note 32 and the Directors' Report.

34. AUDITORS' REMUNERATION

	CONSOLIDATED	
	2011 \$'000	2010 \$'000
<i>Amounts received or due and receivable by PricewaterhouseCoopers Australia for:</i>		
An audit or review of the financial report of the entity and any other entity in the Group	525,000	442,500
	525,000	442,500
<i>Amounts received or due and receivable by PricewaterhouseCoopers Australia for non-audit services:</i>		
Investigating accounts report	630,000	-
Due diligence services	60,000	-
Other agreed-upon procedures in relation to the entity and any other entity in the consolidated Group	115,002	-
	805,002	-

35. SALE OF INTERESTS IN POWER STATION

Braemar 2 Power Station

In the prior year, the Group disposed its interest in the Braemar 2 Power Station for a consideration of \$113.7 million and recognised a gain on disposal of \$36.4 million.

Kwinana Power Station

On 28 October 2010, the Group sold its 30% interest in the Kwinana power station. The Group sold all the shares of ERM BK Power Pty Ltd and ERM Oakey Power II Pty Ltd which were the holding companies for Kwinana group subsidiaries.

The consideration received by the Group for its interest in Kwinana was \$39.9 million less the convertible note liability outstanding at the date of sale of \$31.0 million.

Deferred interest of \$6.0 million, payable on redemption of the notes, is included in finance expense. A loss of \$6.4 million in relation to the interest rate swaps entered into by the Kwinana partnership is included in net fair value losses.

	2011 \$'000
Consideration received	
Consideration received in cash and cash equivalents	8,917
Total consideration received	8,917
Assets and liabilities over which control was lost	
Cash and cash equivalents	10,181
Trade & other receivables	6,818
Prepayments	4,102
Property, plant & equipment	185,222
Goodwill	5,815
Deferred tax assets	10,115
Trade & other payables	(5,375)
Deferred tax liabilities	(11,577)
Borrowings – limited recourse	(187,504)
Minority interest share of relevant assets and liabilities disposed of	(13,618)
Net assets and liabilities disposed of	4,179
Gain on sale	
Consideration received	8,917
Net assets disposed of	(4,179)
Gain on disposal	4,738
Net cash inflow on disposal	
Consideration received in cash or cash equivalents	8,917
Less cash and cash equivalents disposed of	(10,181)
Net cash outflow on disposal	(1,264)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

36. BUSINESS COMBINATION

There were no acquisitions in the year ended 30 June 2010.

Current year acquisition – SAGE Utility Systems Pty Ltd

On 31 March 2011, the Group purchased all of the share capital of SAGE Utility Systems Pty Ltd. At 30 June 2011 the fair values of the assets and liabilities acquired as well as any goodwill on acquisition, is provisional. Provisional fair values may be used for a period of 12 months from acquisition. During the 12 month period from acquisition date the Group will continue to assess the fair value of identifiable assets and liabilities acquired as well as any goodwill on acquisition.

Details of the purchase consideration and the provisional fair values of net assets acquired are as follows:

	2011 \$'000
Purchase consideration	
Cash paid	50
Shares	1,950
Working capital adjustment	384
Total purchase consideration	2,384
Acquisition of subsidiary net of cash acquired	
Cash balances acquired	467
Direct cash costs of acquisition	(50)
Net cash inflow	417

Details of the provisional fair values of the assets and liabilities acquired are as follows:

	Provisional fair value \$'000
Provisional fair value of net identifiable assets acquired	502
Add: Provisional goodwill	1,882
Provisional net assets acquired	2,384

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

37. EARNINGS PER SHARE

	CONSOLIDATED		CONSOLIDATED	
	2011 Number ('000)	2010 Number ('000)	2011 Cents	2010 Cents
Basic earnings per share	138,421	100,908	11.72	(16.72)(i)
Diluted earnings per share	142,880	106,732	11.35	(16.72)(i)

(i) Earnings per share are not diluted for net losses

Reconciliation of weighted average number of ordinary shares

Weighted average number used in calculating basic earnings per share	138,421	100,905	-	-
Effect of share options on issue	4,459	5,827	-	-
Weighted average number used in calculating diluted earnings per share	142,880	106,732	-	-

Information concerning earnings per share

Options

Options granted are usually considered to be potential ordinary shares and taken into account in the determination of diluted earnings per share and are not included in the determination of basic earnings per share.

38. EVENTS AFTER THE REPORTING PERIOD

Acquisition of additional 50% interest in the Oakey Power Station

On 1 July 2011 the Group acquired an additional 50% interest in Oakey Power Holdings Pty Ltd from Redbank Energy Limited (formerly Alinta Energy Limited) taking the Group's total shareholding in Oakey Power Holdings Pty Ltd and interest in the Oakey Power Station from 12.5% to 62.5%.

The financial effects of the transaction have not been brought to account at 30 June 2011. The operating results and assets and liabilities of Oakey Power Holdings Pty Ltd and its wholly owned subsidiaries will be consolidated from 1 July 2011, the date at which the Group gained a controlling interest.

Details of the purchase consideration transferred and the provisional net fair values of the assets and liabilities acquired are:

Purchase consideration

	\$'000
Cash paid	61,691
Total purchase consideration	61,691

	\$'000
Provisional fair value of net identifiable assets acquired	156,000
Less: Provisional acquisition date fair value of previously held equity interest of 12.5%	(18,541)
Less: Provisional fair value of minority interests	(58,338)
Less: Provisional discount on acquisition	(17,430)
Provisional net assets acquired	61,691

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

38. EVENTS AFTER THE REPORTING PERIOD continued

At the time that the financial statements were authorised for issue the Group has not yet completed the accounting for the acquisition of the additional 50% of Oakey Power Holdings Pty Ltd.

Acquisition related costs to be included in profit and loss for the year ended 30 June 2012 and are expected to be approximately \$0.5 million.

The fair value of net identifiable assets acquired, discount on acquisition and minority interests have only been determined provisionally at the time that the financial statements were authorised for issue as the independent valuation had not been finalised. It is also not yet possible to provide detailed information about each class of acquired receivables and contingent liabilities.

Provisional fair values may be used for a period of 12 months from acquisition. During the 12 month period from acquisition date the Group will continue to assess the fair value of identifiable assets and liabilities acquired, the minority interest as well as any goodwill on acquisition.

Other events after the reporting period

Since 30 June 2011, there have been no other matters or circumstances not otherwise dealt with in the financial report that have significantly affected or may significantly affect the Group.

DIRECTOR'S DECLARATION

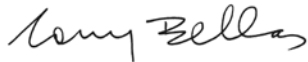
FOR THE YEAR ENDED 30 JUNE 2011

1. In the opinion of the directors of ERM Power Limited ("Company"):
 - (a) the financial statements and notes set out on pages 46 to 104 are in accordance with the *Corporations Act 2001*, including:
 - i. giving a true and fair view of the financial position of the consolidated entity as at 30 June 2011 and of its performance for the year then ended, and
 - ii. complying with Australian Accounting Standards (including the Australian Accounting Interpretations), the *Corporations Regulations 2001* and other mandatory professional reporting requirements.
 - (b) the financial report complies with International Financial Reporting Standards as disclosed in note 1;
 - (c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Note 1(a) confirms that the financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

The directors have been given the declarations by the chief executive officer and chief financial officer required by section 295A of the *Corporations Act 2001*.

Signed in accordance with a resolution of the directors:



Tony Bellas
Director
Brisbane

25 August 2011



Independent auditor's report to the members of ERM Power Limited

Report on the financial report

We have audited the accompanying financial report of ERM Power Limited (the company), which comprises the consolidated statement of financial position as at 30 June 2011, and the consolidated statement of comprehensive income, the consolidated statement of changes in equity and consolidated statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration for ERM Power Limited (the consolidated entity). The consolidated entity comprises the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with *International Financial Reporting Standards*.

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report.

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

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*

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DX 77 Brisbane, Australia
T +61 7 3257 5000, F +61 7 3257 5999, www.pwc.com.au

Liability limited by a scheme approved under Professional Standards Legislation.



Auditor's opinion

In our opinion:

- (a) the financial report of ERM Power Limited is in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the consolidated entity's financial position as at 30 June 2011 and of its performance for the year ended on that date; and
 - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*; and
- (b) the financial report and notes also comply with International Financial Reporting Standards as disclosed in Note 1.

Report on the Remuneration Report

We have audited the attached remuneration report for the year ended 30 June 2011. The directors of the company are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's opinion

In our opinion, the remuneration report of ERM Power Limited for the year ended 30 June 2011, complies with section 300A of the *Corporations Act 2001*.

Yours sincerely

A handwritten signature in black ink that reads 'PricewaterhouseCoopers'.

PricewaterhouseCoopers

A handwritten signature in black ink that appears to read 'Timothy J Allman'.

Timothy J Allman
Partner

25 August 2011

SHARE AND SHAREHOLDER INFORMATION

TWENTY LARGEST SHAREHOLDERS

The following table sets out the 20 largest holders of listed shares (when multiple holdings are grouped together) and the percentage of capital each holds as at 7 October 2011:

Shareholders	Number of shares	% of issued shares
1. Energy Resource Managers Holdings Pty Ltd	43,549,488	26.83
2. Sunset Power Pty Ltd	20,438,364	12.59
3. Citicorp Nominees Pty Limited	8,900,098	5.48
4. Gaffwick Pty Ltd	8,705,182	5.36
5. Ilwella Pty Limited	8,571,429	5.28
6. Sunset Power A Pty Ltd	5,160,934	3.18
7. Sunset Power B Pty Ltd	5,160,934	3.18
8. Sunset Power C Pty Ltd	5,160,934	3.18
9. Sunset Power D Pty Ltd	5,160,934	3.18
10. National Nominees Limited	5,152,406	3.17
11. Philip St Baker & Peta St Baker	3,264,036	2.01
12. AMP Life Limited	2,046,825	1.26
13. Trinity Management Pty Ltd	2,004,224	1.24
14. St Baker Investments Pty Ltd	2,002,088	1.23
15. Andrew James St Baker & Cathryn Jeanne St Baker	1,841,814	1.13
16. Bond Street Custodians Ltd	1,499,586	0.92
17. WH & LL St Baker Pty Ltd	1,447,100	0.89
18. HSBC Custody Nominees (Australia) Limited	1,214,714	0.75
19. St Baker-Childs Investments Pty Ltd	1,199,532	0.74
20. J P Morgan Nominees Australia Limited	778,935	0.48
Total	133,260,147	82.08

As at 7 October 2011 there were 162,304,453 shares on issue.

DISTRIBUTION OF SHARES

The following table summarises the distribution of listed shares as at 7 October 2011:

Ordinary Shares	Number of shareholders	% of issued shares
1 – 1,000	92	0.03
1,001 – 5,000	474	0.90
5,001 – 10,000	465	2.20
10,000 – 100,000	570	9.04
100,001 – and over	72	87.82
Total	1,673	100.00

The number of shareholders holding less than a marketable parcel of shares was 29 holding 5,041 shares.

SUBSTANTIAL SHAREHOLDERS

The following table shows holdings of five per cent or more of voting rights in ERM Power's shares as notified to ERM Power Limited under the *Corporations Act 2001*, Section 671B:

Class of Securities	Identity of person or group	Date of notice received	Relevant interest in number of securities	Percentage of total voting rights
Ordinary Shares	Trevor Charles St Baker ¹	10/12/2010	84,631,588	52.97%
Ordinary Shares	Gaffwick Pty Ltd	10/12/2010	8,571,429	5.37%
Ordinary Shares	Ilwella Pty Limited	10/12/2010	8,571,429	5.37%

1. Trevor Charles St Baker controls each registered shareholder of Energy Resource Managers Holdings Pty Ltd as trustee for the Energy Resource Managers Trust, Sunset Power Pty Ltd as trustee for the St Baker Family Trust, Sunset Power A Pty Ltd as trustee for Sunset Power Trust A, Sunset Power B Pty Ltd as trustee for Sunset Power Trust B, Sunset Power C Pty Ltd as trustee for Sunset Power Trust C and Sunset Power D Pty Ltd as trustee for the Sunset Power Trust D.

VOTING RIGHTS

As a meeting of members, each member who is entitled to attend and vote may attend and vote in person or by proxy, attorney or representative. On a show of hands, every person present who is a member, proxy, attorney or representative, shall have one vote and on a poll, every member who is present in person or by proxy, attorney or representative shall have one vote for each fully paid share held.

SECURITIES EXCHANGE LISTING

ERM Power Limited shares are traded on the Australian Securities Exchange (ASX) under the symbol "EPW".

VOLUNTARY ESCROW

98,679,437 shares are subject to voluntary escrow until the date that is 3 business days after the release of the full year results for the year ending 30 June 2012.

UNQUOTED SECURITIES

As at 7 October 2011, there were 11,444,518 options to acquire fully paid ordinary shares. The options do not carry any entitlement to participate in any share issue. All options expire on the earlier of their expiry date, or for those with a 2017 expiry date, termination of the holder's employment, or as otherwise determined by the Board.

Expiry Date	Issue price of shares (cents)	Number of options	Number of holders
6 June 2013	80.6	9,655,412	49
30 June 2013	80.6	250,000	2
1 November 2017	275.0	1,296,400	24
8 November 2017	275.0	242,706	1

GLOSSARY

AASB	Australian Accounting Standards Board
ACF	the ratio of the actual output of a power plant and its output if it had operated at full capacity over the entire year
AEMO	Australian Energy Market Operator Limited ACN 072 010 327 (formerly National Electricity Market Management Company Limited)
AGL	AGL Energy Limited ACN 115 061 375 or its controlled entities
Alinta	Alinta Energy Limited ACN 116 665 608 (formerly Babcock & Brown Power Limited)
ANZSAM	ANZ Specialist Asset Management Limited ACN 098 827 671
Arrow Energy	Arrow Energy Limited ACN 078 521 936 or its controlled entities
ASIC	Australian Securities and Investments Commission
ASX	ASX Limited ACN 008 624 691 or the exchange operated by it
Base load	generating power plant that is normally operated to take all or part of the minimum load of a system, and which produces electricity at an essentially constant rate
BBSY	bank bill swap bid rate
Board	the Board of directors of ERM Power
Braemar 1	the Braemar 1 power station, a 504 MW power station, situated approximately 30 kilometres west of Dalby, Queensland
Braemar 2	means the Braemar 2 power station, a 519 MW power station, situated approximately 30 km west of Dalby, Queensland
Braemar 3	the proposed 550 MW Braemar 3 power station, to be situated approximately 30 km west of Dalby, Queensland
Broker	an ASX participating organisation
CCGT	combined-cycle gas turbine
Company	ERM Power
Contact Energy	Contact Energy Limited ARBN 080 480 477
Corporations Act	<i>Corporations Act 2001</i> (Cth)
CO₂	carbon dioxide
CY	the calendar year ended or ending 31 December
Directors	the directors of ERM Power
DRP	dividend reinvestment plan
EBITDAIF	earnings before interest, tax, depreciation, amortisation, goodwill impairment and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts
EBITF	earnings before interest, tax and net fair value gains/losses on financial instruments designated at fair value through profit and loss and gains/losses on onerous contracts
Empire Oil and Gas	Empire Oil Company (WA) Limited ACN 009 475 423 a wholly owned subsidiary of Empire Oil and Gas NL
ERM Gas	ERM Gas Pty Ltd ACN 126 836 799, ERM Power's gas business focussed on procurement of long term gas supplies for future projects through commercial contracts and exploration

ERM Generation Assets	ERM Power's business of owning interests in gas-fired power stations, currently comprised of interests in Oakey and Neerabup
ERM Land Holdings	ERM Land Holdings Pty Ltd ACN 083 762 056, the entity that holds ERM Power's strategic land holdings
ERM Oakey	E.R.M Oakey Power Pty Ltd ACN 075 130 022, the entity that holds ERM Power's interest in the Oakey power station
ERM Power	ERM Power Limited ACN 122 259 223 ('ERM Power' and 'Company' shall have a corresponding meaning)
ERM Power Generation	ERM Power Generation Pty Ltd ACN 117 443 035, ERM Power's operation services company that manages and operates electricity generation and gas pipeline businesses
ERM Sales	ERM Power Retail Pty Ltd ACN 126 175 460, ERM Power's electricity sales business targeting the larger end of the business customer market
Forecast Period	the period from 1 July 2010 to 30 June 2012
FY	the financial year ended or ending 30 June
Group	ERM Power and each of its subsidiaries
GW	gigawatt
GWh	gigawatt hours
Infrastructure Capital Group	Infrastructure Capital Group Limited ACN 094 815 513 as manager for the Energy Infrastructure Trust
Intermediate	generating power plant that operates between the extremes of baseload and peaking power plants, curtailing their output in periods of low demand
IPO	initial public offering
ISDA	means the International Swaps and Derivatives Association
km	kilometre
km²	square kilometre
Kwinana	means the Kwinana power station, a 320 MW baseload power station located approximately 30 km south of Perth, Western Australia
LTOT	Long Term Incentive Option Trust
LTIST	Long Term Incentive Share Trust
MW	megawatt
MWh	megawatt hours
NEM	National Electricity Market
Neerabup	means the Neerabup power station, a 330 MW peaking power station located in the town of Neerabup, approximately 40 km north of Perth, Western Australia
NewGen Braemar 2	means the partnership between ERM Braemar 2 Pty Ltd and Arrow Southern Generation Pty Ltd, which owns Braemar 2
NewGen Neerabup	means the partnership between ERM Neerabup Pty Ltd ACN 126 964 583 and EIT Neerabup Power Pty Ltd ACN 128 916 478, which owns Neerabup
NewGen Power Kwinana	means the partnership between ERM Kwinana Power Pty Ltd ACN 115 348 171 and Summit Kwinana Power Pty Ltd ACN 116 803 779, which owns Kwinana

GLOSSARY continued

New Shares	new Shares to be issued by ERM Power
NPAT	net profit after tax
Oakey	means the Oakey power station, a 332 MW peaking power station situated in the Darling Downs, 150 km west of Brisbane, Queensland
Oakey Power Holdings	Oakey Power Holdings Pty Ltd ACN 075 260 794
OCGT	open-cycle gas turbine
Option	an option to acquire a Share in ERM Power
Personnel	employees and professional service contractors of ERM Power
PJ	petajoules
Powerlink	Powerlink, the Queensland state government corporation that owns, operates and maintains Queensland's high voltage electricity transmission network
PPA	Power Purchase Agreement
Prospectus	Prospectus lodged by ERM Power on 17th November 2011
RECs	Renewable Energy Certificates produced when generating electricity from eligible renewable generators under the ERET
Shareholders	holders of Shares in ERM Power
Share Registry	Link Market Services ABN 54 083 214 537
Shares	fully paid Shares in ERM Power
Siemens	Siemens Ltd ACN 004 347 880
STIST	Short Term Incentive Share Trust
Sunset Power	Sunset Power Pty Ltd ACN 101 619 658, an entity controlled by Trevor St Baker
Synergy	Electricity Retail Corporation ABN 71 743 446 839, trading as Synergy
Uranquinty	the Uranquinty power station, a 664 MW power station, located in Uranquinty, New South Wales
Wellington 1	the proposed 550 MW Wellington 1 power station to be situated in Wellington, New South Wales
Western Power	Western Power, the electricity networks corporation owned by the Western Australia Government

**Company**

ERM Power Limited
(ACN: 122 259 223)

Directors

Trevor St Baker
Non-Executive Chairman

Anthony (Tony) Bellas
Independent Non-Executive Director

Martin Greenberg
Independent Non-Executive Director

Antonino (Tony) Iannello
Independent Non-Executive Director

Brett Heading
Independent Non-Executive Director

Philip St Baker
Managing Director

Company Secretaries

Peter Jans
Graeme Walker

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Perth WA 6000

Tel: (08) 9841 1100
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Bankers

National Australia Bank

Auditors

PricewaterhouseCoopers

Lawyers

McCullough Robertson
Freehills

Share Registry

Link Market Services

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