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Shareholder agreement

Ausgrid
Statement of Corporate Intent
Year ending 30 June 2017

This Statement of Corporate Intent has been agreed between:

Roger Massy-Greene
Chairman Ausgrid
on behalf of the Board of Directors

Trevor Armstrong
Acting Chief Executive Officer Ausgrid

The Honourable Gladys Berejiklian MP
Treasurer of New South Wales

The Honourable Dominic Perrottet MP
Minister for Finance, Services and Property

6 September 2016
Objectives

Principal objectives for energy distributors under the *Energy Services Corporations Act 1995* are:

- To be a successful business and, to this end:
  - Operate at least as efficiently as any comparable businesses;
  - Maximise the net worth of the state’s investment in it; and
  - Exhibit a sense of social responsibility by having regard to the interests of the community in which it operates.
- To protect the environment by conducting its operations in compliance with the principles of ecologically sustainable development contained in section 6(2) of the *Protection of the Environment Administration Act 1991 (NSW)*.
- To exhibit a sense of responsibility towards regional development and decentralisation in the way in which it operates.
- To operate efficient, safe and reliable facilities for the distribution of electricity.
- To be an efficient and responsible supplier of electricity and of services relating to the use and conservation of electricity.

Each of these principal objectives is of equal importance.

Ausgrid focuses on three key goals:

- **SAFETY** – We will protect ourselves, our colleagues, our contractors and the community by continued improvement of our safety performance
- **RELIABILITY** - We will provide a network that delivers reliable electricity supply and quality service to our customers.
- **SUSTAINABILITY** - We will ensure our business is sustainable by making it efficient and competitive so that we can meet future challenges.
Business overview – the Ausgrid network

- Ausgrid serves approximately 1.7 million customers
- Ausgrid’s supply area covers 22,275 square kilometres from Waterfall, in Sydney’s south, to Auburn in Western Sydney, and the upper Hunter Valley to the north
- At 30 June 2016 Ausgrid employed 4,100 full time equivalent employees* over 41 primary locations
- Projected regulated asset base of $16.1 billion at 30 June 2017
- Projected annual revenue in FY17 of $2.6 billion
- Projected net profit after tax in FY17 of $166 million
- Actual FY16 system peak demand of 5,488 MW
- Actual Energy delivered in FY16 totalled 25,618 GWh

### Assets managed (as at 30 June 2016)

<table>
<thead>
<tr>
<th>Asset</th>
<th>Unit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Substations – Transmission</td>
<td>46</td>
</tr>
<tr>
<td>- Zone</td>
<td>191</td>
</tr>
<tr>
<td>- Distribution</td>
<td>31,449</td>
</tr>
<tr>
<td>Power Poles</td>
<td>509,044</td>
</tr>
<tr>
<td>Transmission system</td>
<td>930 km</td>
</tr>
<tr>
<td>Sub transmission system</td>
<td>3,222 km</td>
</tr>
<tr>
<td>High voltage system – Overhead line</td>
<td>10,049 km</td>
</tr>
<tr>
<td>- Underground cable</td>
<td>8,175 km</td>
</tr>
<tr>
<td>Low voltage system** – Overhead line</td>
<td>19,269 km</td>
</tr>
<tr>
<td>- Underground cable</td>
<td>7,294 km</td>
</tr>
</tbody>
</table>

* The reported FTEs amount includes labour hire employees.

** Low voltage asset length includes street lighting but excludes service mains

Source: Maximum Demand sourced from internal energy consumption report (June 2016). Assets managed - as at June 2016 (unaudited) per SAP and GIS.
Business overview

Our purpose
To be of service to our communities by efficiently distributing electricity to our customers in a way that is safe, reliable and sustainable.

Our values
Safety excellence  Respect for people  Customer and community focus  Continuous improvement  Act with integrity
## Business environment

### Sector & market

Ausgrid's network is expected to have sufficient network capacity for the next 5-10 years without the need for substantial investment in additional capacity. The primary driver of growth in Ausgrid's RAB is asset renewal. Sydney's population is forecast to rise and there will continue to be pockets of localised demand growth associated with transport corridor development. Ausgrid will play a key role and partner with others to provide the infrastructure to meet this growth in specific locations. Pressure to keep regulated costs low will continue.

The energy sector is being disaggregated and deregulated. The sector has moved from a vertically integrated industry to an independent disaggregated environment. New non-traditional players are entering the energy market and providing competition for customers' attention and spending. Ausgrid has key technical capabilities, data, economies of scale, and customer relationships that can be deployed to manage the disruption to the value chain.

New technology is transforming the energy sector. Ausgrid's network area has experienced a lower impact on consumption from solar PV than its peers. However, technology will continue to influence the future through better ways of operating and maintaining the network, availability of new information and data to make better decisions, availability of energy storage, and potential new sources of consumption (e.g. electric vehicles). This provides opportunities and risks that Ausgrid will need to manage prudently.

### Stakeholders

Ausgrid is trusted in times of emergency by its customers. However, expectations of our customers are shifting and require Ausgrid to pay greater attention to their needs. Ausgrid is improving how it engages with customers to better understand customer needs and improve regulatory outcomes.

Ausgrid's financial circumstances have changed as a result of the AER's 2015 Final Determination. Ausgrid is executing its plans to transform the business to reduce costs and manage regulatory risk in the context of the appeal of the AER's Determination and Judicial Review. Ausgrid's challenge is to demonstrate to the AER that its operations are delivering an efficient service.

Ausgrid has a highly experienced workforce that has served the company well. To become a more commercially agile asset manager and service provider, Ausgrid must find the right balance in the skills and capabilities of its people, whilst resetting the size of the workforce to align to the AER's funding allowance. We also need to prepare our people to lead in times of continuous change and build on our strong safety culture to become more customer-focused and commercially oriented.
Operating environment over the next 1-3 years

In our operating environment:

- Safety continues to be our number one priority.
- We are striving to put customers at the centre of our decision making.
- Knowledge and experience will be leveraged to improve efficiency of business operations and asset management.
- Technology improvements will bring positive change to field operations.
- Regulated returns on investment (WACC) are significantly lower in FY15-19 regulatory period than in FY09-14 period.
- Operating expenditure allowed by AER is significantly lower than current levels of operating expenditure, driving the need for cost reduction and productivity improvement.
- Focus is on sustainable efficiency programs to continue delivering benefits and reduce our operating costs.
- Successful EBA negotiation is key to establishing a more competitive workforce and cost base. A policy to manage excess employees continues to be negotiated.
- Support of the NSW Government's policy initiative to lease 50.4% of Ausgrid and Endeavour Energy to fund infrastructure investment within NSW is a priority for Ausgrid.
- Priorities are well set out and embedded in corporate strategies.
- On 1 July 2015, prices fell by 20.3% on average and subsequently increased by only 1.51% in July 2016. We will continue to put downward pressure on network charges in line with the AER's 2015 Final Determination (subject to Judicial Review) and other legislated pricing commitments.
Strategic response

Ausgrid has identified four key priority areas to pursue to deliver a commercial and efficient business by FY19. Ausgrid recognises it must focus on efficiency as well as maintain awareness of opportunities in an evolving energy market, and build capabilities to capture these opportunities when they arise.

The delivery of strategic initiatives within each priority is incorporated into performance agreements with senior management.

<table>
<thead>
<tr>
<th>Strategic Plan</th>
<th>Priorities</th>
<th>Purpose</th>
</tr>
</thead>
<tbody>
<tr>
<td>FINANCIALS</td>
<td>Create certainty in regulated revenue</td>
<td>Secure a good regulatory outcome by making efficient investments, running efficient operations, and building trust with government and regulators through our actions and communications</td>
</tr>
<tr>
<td>OPERATIONS</td>
<td>Enhance core business</td>
<td>Continue to drive improvement, innovation, and efficiency in core business operations to earn acceptable returns, improve future regulatory outcomes, and create a platform for growth</td>
</tr>
<tr>
<td>CUSTOMERS</td>
<td>Improve the customer experience</td>
<td>Embed a business-wide focus on customers and build capability to design and manage their whole experience, including customer engagement and customer service</td>
</tr>
<tr>
<td>PEOPLE</td>
<td>Shift leadership, capability &amp; culture</td>
<td>Leverage our peoples' talent and industry experience to drive diversity and growth, build a sustainable workforce of employees and contractors with the right skills for our future, and maintain a safe workplace and culture</td>
</tr>
</tbody>
</table>
Financial performance targets

Ausgrid’s financial performance targets for FY17 and beyond are set out below.

The outcomes in the SCI reflect the ongoing implementation of Ausgrid’s Transformation Program – a program which began in early FY16, designed to substantially reduce operating cost and capital expenditure to FY19. The financial projections reflect the gradual and orderly transition of Ausgrid’s business to a sustainable level of employees as per legislative requirement 1 by the first quarter FY19, and the associated corporate restructuring costs e.g. voluntary redundancy payments and stranded labour costs.

<table>
<thead>
<tr>
<th></th>
<th>Q1FY17</th>
<th>Q2FY17</th>
<th>Q3FY17</th>
<th>Q4FY17</th>
<th>FY17 4,5</th>
<th>FY18 5</th>
<th>FY19 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>EBITDA ($m)</td>
<td>377.03</td>
<td>357.98</td>
<td>343.18</td>
<td>368.92</td>
<td>1,447.11</td>
<td>1,254.59</td>
<td>1,339.19</td>
</tr>
<tr>
<td>Net profit after tax ($m)</td>
<td>-3.73</td>
<td>52.77</td>
<td>49.06</td>
<td>67.67</td>
<td>165.77</td>
<td>50.42</td>
<td>107.25</td>
</tr>
<tr>
<td>Dividend payout ratio 2</td>
<td>70%</td>
<td>70%</td>
<td>70%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total shareholder distributions 3 ($m)</td>
<td>523.56</td>
<td>304.77</td>
<td>383.39</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Return on assets</td>
<td>5.6%</td>
<td>4.3%</td>
<td>4.7%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Return on equity</td>
<td>4.0%</td>
<td>1.2%</td>
<td>2.6%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

2 Dividend payout ratio is based on distributable net profit after tax and is before Additional Dividends.
3 Total shareholder distributions includes dividends as per NSW Treasury’s Financial Distribution Policy for Government Businesses (TPP14-04), Additional Dividends, the current portion of income tax equivalents and Government Guarantee Fee (GGF). Additional Dividends are special dividends used to fund the NSW Government’s energy rebate program. Additional Dividends of $63.6m have been recognised in FY17. No Additional Dividends have been recognised in relation to the later years of the SCI.
4 FY17 NPAT projections include mark-to-market losses of $55 million expected to be crystallised through the early retirement of a portion of long term debt as directed by the NSW Treasurer.
5 On 26 February 2016 the Australian Competition Tribunal set aside the AER’s 2015 Final Determination and Ausgrid’s Allowed Annual Revenue for the period FY15-19. In the absence of an applicable FY15-19 distribution determination, Ausgrid has entered into an enforceable undertaking with the AER under section 59A of the National Electricity (NSW) Law to set pricing for the 2017 financial year. The price and revenue projection in FY17 has been based on FY16 prices plus a CPI of 1.51% for distribution charges and 1.69% for transmission charges. Revenues in FY18 and FY19 are consistent with the AER’s 2015 Final Determination.
Dividend policy

NSW Treasury's Financial Distribution Policy for Government Businesses TPP14-04 (Distribution Policy) normally requires SOC to pay an ordinary dividend equal to 70 per cent of net profit after tax.

The payment of a dividend calculated as a percentage of net profit after tax is constrained by a number of factors specified in the Distribution Policy.

For FY16, Ausgrid is forecasting to make an operating loss after income tax of $294.8 million, due to mark-to-market losses on partially retired long-term borrowings, and will therefore pay no ordinary dividend from Distributable Profits.

The NSW Government has determined that Ausgrid will pay an Additional Dividend of $63.5m in relation to the FY16 financial year to fund the Government's energy rebate program.
Non-financial performance targets

Ausgrid's non-financial performance targets are set to improve safety performance and maintain the reliability of the network.

<table>
<thead>
<tr>
<th></th>
<th>FY17</th>
<th>FY18</th>
<th>FY19</th>
</tr>
</thead>
<tbody>
<tr>
<td>Safety – lost time injury frequency rate</td>
<td>1.1</td>
<td>1.0</td>
<td>0.8</td>
</tr>
<tr>
<td>Network reliability – unplanned system average interruption duration index</td>
<td>73.6</td>
<td>73.6</td>
<td>73.6</td>
</tr>
<tr>
<td>Energy delivered (GWh)</td>
<td>25,341</td>
<td>25,419</td>
<td>25,511</td>
</tr>
<tr>
<td>Total network customer connections</td>
<td>1,723,116</td>
<td>1,747,086</td>
<td>1,768,330</td>
</tr>
</tbody>
</table>
Reporting obligations

Ausgrid’s reporting obligations throughout the year are summarised below:

**Annual report**
- Consistent with *Annual Reports (Statutory Bodies) Act 1984* and *Regulation 2000*.
- Includes general purpose financial statements (in accordance with Australian Accounting Standards), *State Owned Corporations Act 1989*, the *Public Finance and Audit Act 1983* and the *Regulation 2010*.

**Half yearly report**
- A report on the operations of the corporation during that half year delivered one month after the end of the first six months of the financial year (Section 23 of the *State Owned Corporations Act 1989*).
- Contain summary financial statements, details of the corporate profile, strategic directions and performance highlights.

**Quarterly report**
- Includes detailed actual quarterly and year to date performance of the business, comparisons to SCI targets, and highlights significant issues.
- Provided to NSW Treasury within ten working days of the board meeting following quarter end at which the quarterly results are considered (extended to 20 working days for the quarter end which is also financial year end).

**Other information to be provided:**
- Forecast financial statements requested by NSW Treasury via Treasury Online Electronic System (TOES);
- Forecast of financial distributions and tax equivalents requested by NSW Treasury (budget round forecasts);
- Forecast capital works program via CAPTOES;
- Reporting on capital projects as required via the Major Capital Projects Reporting System (MCPRS);
- CEO wages policy certification of 2017 financial year result provided one month prior to submission of annual report; and
- Submissions for Projects of State Significance.
Representation and commitment statement

Ausgrid’s board makes the following commitment in relation to the Statement of Corporate Intent:

The board of Ausgrid confirms that:

- Performance targets within the 2016-17 SCI are based on management assumptions and 10 year financial projections approved by the Board;
- The voting shareholders will be provided with financial and other information, including information on major capital expenditure projects, on a quarterly basis to enable shareholders to assess the performance against commitments in this SCI and to assess the value of the shareholder’s investment in the business;
- Asset maintenance policies and processes are adequate and appropriate to manage and control risks associated with physical assets as far as reasonably possible;
- All known key risks and major emerging contingent liabilities which could materially impact the current and future results of Ausgrid have been disclosed;
- Internal audit and risk management practices are consistent with standards recommended for Australian Securities Exchange (ASX) listed companies and where appropriate, Ausgrid has applied any additional requirements that are set out in TPP15-03 Internal Audit and Risk Management Policy for the NSW Policy Sector;
- The Acting Chief Executive Officer has an employment contract and performance agreement. Performance under the employment contract is appraised annually;
- Ausgrid adheres to Commercial Policy Framework policies, as listed in State Owned Corporations: Applicable Treasury Policy Papers under the Commercial Policy Framework (as issued by NSW Treasury as at November 2015);
- Ausgrid complies with NSW Treasury accounting circulars and policies applicable for SOCs, as listed in the State Owned Corporations Mandatory Accounting Policies – NSW Treasury Circulars and Treasury Policy Papers (as issued by NSW Treasury as at November 2015);
- Ausgrid complies with the requirements of Premier’s Memoranda M2012-04 Application of NSW Public Sector Wages Policy 2011 to State Owned Corporations and further guidance contained in the Treasurer’s January 2014 letter;
- Ausgrid will apply the principles of Premier’s Memoranda M2012-03 Application of Biofuels; and
- Ausgrid will apply the principles of Premier’s Memoranda M2013-04 Implementation guidelines for procurement of publicly funded construction services.