Santos

Annual Report
2017

# Transform
# Build
# Grow




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This *2017 Annual Report* is a summary of Santos' operations, activities and financial position as at 31 December 2017.

All references to dollars, cents or $ in this document are to US currency, unless otherwise stated.

An electronic version of this report is available on Santos' website, www.santos.com

Santos' Corporate Governance Statement can be viewed at: www.santos.com/who-we-are/corporate-governance

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Santos

# An Australian Energy Pioneer

**Santos is an Australian natural gas company. Established in 1954, the company's purpose is to provide sustainable returns for our shareholders by supplying reliable, affordable and cleaner energy to improve the lives of people in Australia and Asia.**

Five core long-life natural gas assets sit at the heart of a three phase strategy to Transform, Build and Grow the business: Northern Australia, Papua New Guinea, Western Australia Gas, Queensland and the Cooper Basin. Each of our core assets provide stable production, long-term revenue streams and significant upside opportunities.

With one of the largest exploration and production acreages in Australia, a significant and growing footprint in Papua New Guinea, and a strategic infrastructure position, Santos is well positioned to benefit from the growing global demand for energy.

To deliver our vision to be Australia's leading energy company by 2025, we will aspire to:

- Reduce emissions and improve air quality across Asia and Australia by displacing coal with natural gas, and support the economic development of combined gas and renewable energy solutions
- Be the leading national supplier of domestic gas in Australia
- Be a leading regional LNG supplier by increasing LNG sales to our Asian customers to over 4.5 million tonnes per annum
- Be recognised as the safest and lowest cost onshore gas developer in Australia
- Become the market leader in running the safest and lowest cost facilities and infrastructure operations
- Contribute positively to the communities in which we operate by providing jobs, energy supply and local partnerships
- Develop our people and culture to deliver our vision

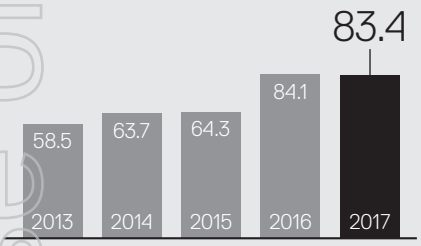
Santos is now a stronger, more resilient organisation with the capacity to execute and bring on-line growth opportunities across the core asset portfolio. As a low-cost, reliable and high performance business, we are proud to deliver the economic and environmental benefits of natural gas to homes and businesses throughout Australia and Asia.

# Financial Overview

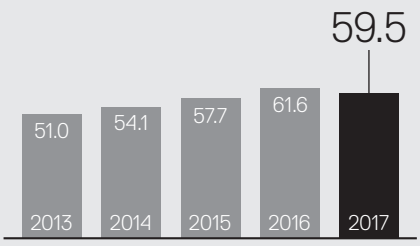
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## STRONG OPERATING PERFORMANCE

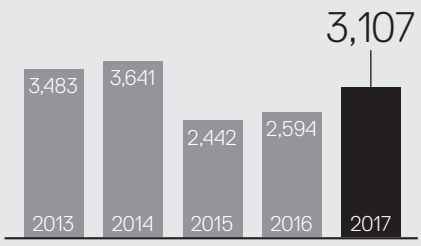
**Sales volume**
mmboe




**Production**
mmboe

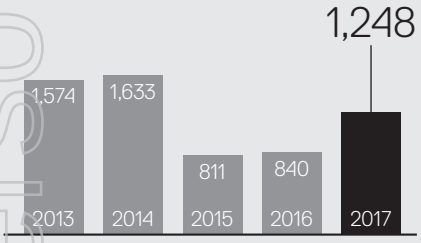



**Sales revenue**
US$million

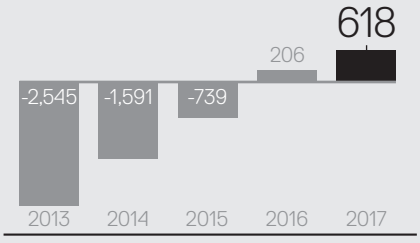



## CASH FLOW TRANSFORMED AND UNDERLYING PROFIT INCREASING

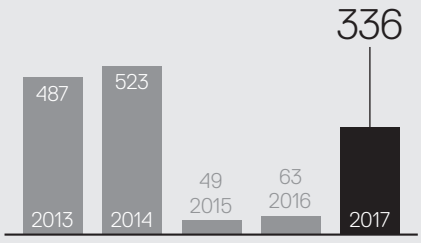
**Operating cash flow**
US$million




**Free cash flow**
US$million

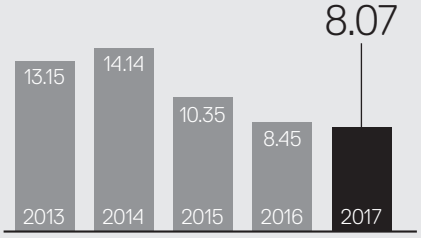



**Underlying net profit after tax**
US$million

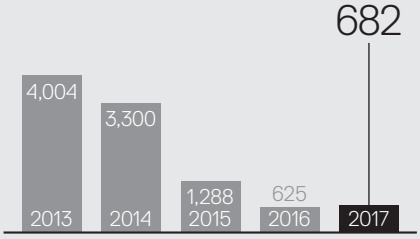



## COSTS REDUCED AND BALANCE SHEET STRENGTHENED

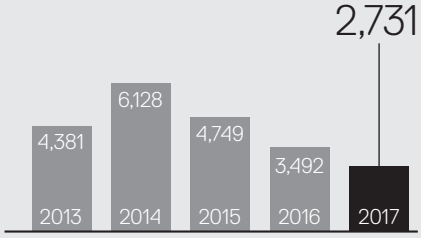
**Unit production costs**
US$ per boe




**Capital expenditure**
US$million

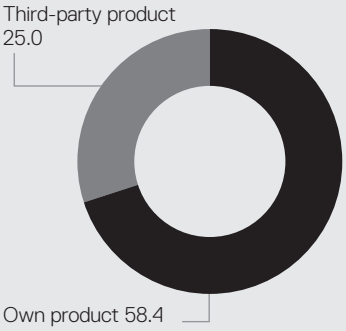



**Net debt**
US$million

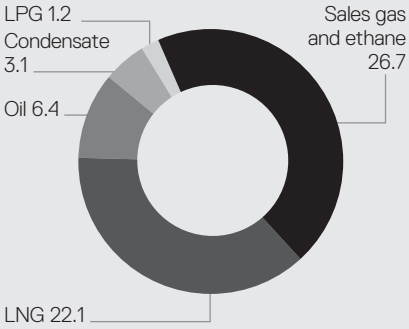


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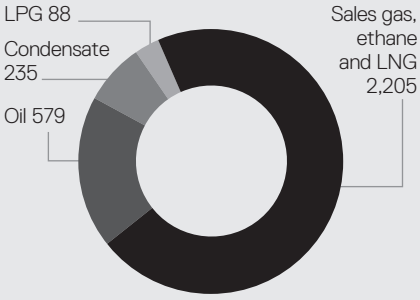
**2017 Sales volumes**
mmboe




**2017 Production**
mmboe




**2017 Sales revenue**
US$million

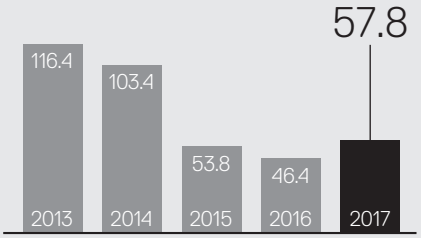



## 2017 RESULTS

| | | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|---|
| Sales volume | mmboe | 58.5 | 63.7 | 64.3 | 84.1 | **83.4** |
| Production | mmboe | 51.0 | 54.1 | 57.7 | 61.6 | **59.5** |
| Average realised oil price | US$/bbl | 116.4 | 103.4 | 53.8 | 46.4 | **57.8** |
| Net profit after tax | US$million | 499 | (630) | (1,953) | (1,047) | **(360)** |
| Underlying net profit after tax | US$million | 487 | 523 | 49 | 63 | **336** |
| Sales revenue | US$million | 3,483 | 3,641 | 2,442 | 2,594 | **3,107** |
| Operating cash flow | US$million | 1,574 | 1,633 | 811 | 840 | **1,248** |
| EBITDAX[1] | US$million | 1,926 | 2,076 | 1,454 | 1,199 | **1,428** |
| Total assets | US$million | 18,407 | 18,281 | 15,949 | 15,262 | **13,706** |
| Earnings per share | US cents | 51.6 | (64.4) | (169.5) | (58.2) | **(17.3)** |
| Dividends declared | AUD cents | 30 | 35 | 20 | - | **-** |
| Number of employees | | 3,502 | 3,636 | 2,946 | 2,366 | **2,080** |

1 EBITDAX (earnings before interest, tax, depreciation, depletion, exploration, evaluation and impairment), EBIT (earnings before interest and tax) and underlying profit are non-IFRS measures that are presented to provide an understanding of the performance of Santos' operations. Underlying profit excludes the impacts of asset acquisitions, disposals and impairments, as well as items that are subject to significant variability from one period to the next including the effects of fair value adjustments and fluctuations in exchange rates. The non-IFRS financial information is unaudited, however, the numbers have been extracted from the audited financial statements.

**Average realised oil price**
US$ per barrel



# Message from the Chairman and from the Managing Director and Chief Executive Officer

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Dear Shareholder,

In 2017 our strategy to Transform, Build and Grow delivered ahead of expectations. Whilst there is still more to be done, the business has been re-set. Santos is now a stronger, more resilient company with the capacity to execute and bring on-line growth opportunities across our core asset portfolio.

Over the course of 2017 we:

- Reduced our free cash flow breakeven to US$32 per barrel oil price
- Generated $618 million in free cash flow, before asset sales
- Reduced net debt by $761 million to $2.7 billion, and
- Reported an underlying net profit after tax of $336 million

A strong operating performance across our core assets resulted in sales volumes of 83.4 million barrels of oil equivalent (mmboe) exceeding the top end of guidance, and production of 59.5 mmboe. LNG sales volumes were up 10% to a record 3.1 million tonnes following continued strong performance from PNG LNG and the ramp-up of GLNG. LNG sales revenues were up 33% to a record US$1.2 billion.

At our half-year results we announced a change in the asset and macro assumptions that determine the carrying value of our assets. This triggered a non-cash net impairment charge of $689 million after tax. The impairment reflected a write-down of our GLNG asset and the undeveloped Ande Ande Lumut oil field in Indonesia, predominantly due to lower oil price assumptions. This was offset by a positive net write-back on our Cooper Basin asset due to higher assumed development activity and production supported by significant improvements in costs, particularly across our drilling operations. Additional impairment charges of $14 million after tax were recorded against other assets in the second half, resulting in a full-year net loss after tax of $360 million.

## CAPITAL MANAGEMENT

In 2017 we made strong progress to strengthen the balance sheet. By year end net debt was $2.7 billion, down from $3.5 billion twelve months prior. Debt repayment continues to be a key priority for the company as we target $2 billion in net debt by the end of 2019.

Given the current focus on debt reduction, the Board did not declare a final dividend. While this decision will be disappointing for some shareholders, we are confident that prioritising debt repayment is the right course of action at this time and will position the company to fund growth opportunities from a position of strength and generate sustainable shareholder returns.

In light of the substantial turnaround in the underlying business, should market conditions remain supportive and the company achieves its debt reduction target ahead of plan, the Board will consider capital management strategies to return value to shareholders.

## TRANSFORMING OUR OPERATIONS

Core to the transformation of Santos has been the turnaround in our onshore "drill–complete–connect" operations across the Cooper Basin and GLNG acreage. Running our onshore upstream operations as a separate business has provided the focus and discipline required to adopt innovative, lean principles and drive quick-cycle learnings.

As a result of these efforts, Santos is now Australia's lowest-cost onshore operator, a significant point of differentiation that is not easy to replicate. To leverage these capabilities, we are working hard to be the "go-to" upstream operator of choice as we seek to enter new plays and capture incremental value for shareholders.

In addition to the significant cost-out and efficiency gains across our onshore operations, our high-margin conventional assets continued to perform strongly in 2017.

PNG LNG operated 20% above nameplate capacity to produce 8.3 million tonnes (gross) of LNG in 2017, shipping a total of 110 cargoes. Our core asset position was strengthened with the Muruk exploration well drilling program in the Southern Highlands confirming the discovery of a potentially significant new gas field. Muruk is situated only 21 kilometres from the existing PNG LNG Hides gas conditioning plant and an appraisal well is due to be drilled in the first half of 2018. We also announced two new farm-in agreements. We are excited about our growth prospects in PNG, and will continue to explore and develop opportunities that further align partner interests over the coming year.

In Northern Australia, Darwin LNG consistently demonstrated excellent reliability and availability, delivering its 600th cargo since start-up in 2006. A two-well appraisal campaign in the Barossa field resulted in a significant increase in 2C resources and positioned the field as the lead candidate for backfill to Darwin LNG. Good progress is being made on the proposed development and we expect to approve Front End Engineering and Design ("FEED") in the second quarter of 2018 with a Final Investment Decision ("FID") currently scheduled for the third quarter of 2019.

In Western Australia we signed two new domestic supply agreements. Our low-cost operations are well positioned with the capacity and reserves to meet short- and long-term demand in the region.

## DISCIPLINED OPERATING MODEL

In 2017 we continued to evolve and implement our operating model to ensure Santos remains focused on maximising free cash flow through the oil price cycle. Portfolio rules have now been ingrained in our day-to-day operations. At the heart of this model is the requirement for each of our core assets to generate positive free cash flow at ≤US$40 per barrel oil price, pre major-growth spend. Budgets across our Exploration, Development, Production and Marketing activities will

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only be approved if this criteria is met. This approach ensures we remain disciplined in a rising oil price environment and positioned to benefit from higher margins to pay down debt, fund exploration, grow the business and deliver shareholder returns.

## RELIABLE, AFFORDABLE AND SUSTAINABLE ENERGY SUPPLY

In 2017 Santos delivered on its commitment to meet domestic gas demand while also honouring our long-term LNG contractual obligations. We worked closely with our joint-venture partners and industry to support the Federal Government in bringing more supply into the domestic market to help mitigate gas supply concerns. Over the course of the year we signed agreements to facilitate the delivery of more than 140 PJ of gas into the east coast domestic market.

In Eastern Queensland we signed transport agreements to unlock significant gas reserves that sit outside the GLNG project. This allows Santos to meet contractual obligations to supply gas to GLNG while freeing up Cooper Basin gas for domestic east coast markets. We are also using our Moomba infrastructure and pipeline capacity positions to assist in the delivery of gas to the east coast.

Santos will continue to proactively pursue transactions that capture value for our shareholders and extend our long and proud history of delivering competitive wholesale gas supply to east coast domestic gas market end users.

In February 2017 we lodged the Environmental Impact Statement ("EIS") for the Narrabri Gas Project and in November announced that the project would re-enter the core portfolio. The project will be managed under our onshore upstream business, where we will apply our low cost "drill–complete–connect" model to improve the commercial outlook for the project. We believe that the east coast of Australia requires more gas and that Narrabri could play a significant role in meeting this demand outlook. Any significant capital expenditure will only occur when the project has the necessary approvals in place to facilitate development.

Our natural gas portfolio strategically aligns with the global transition to a low-carbon economy. Offering both reliability and lower emissions, gas is a natural complement to renewables that can be quickly turned up and down to deal with the intermittency of solar and wind. When used for power generation, natural gas is also 50% less emissions intensive than coal.

Global greenhouse gas emissions are around 50 billion tonnes per year, about half of which come from Asia. A large portion of this is from coal-fired power generation. This makes natural gas a clear choice for the Asian region. Gas demand in Asia is forecast to double by 2040, and Santos is well positioned to take advantage of this growth.

In 2017 Santos set up an Energy Solutions team to actively assess opportunities to reduce Santos' footprint and prepare for a lower-carbon future and in early 2018 we released our inaugural Climate Change Report. This report is aligned with the recommendations of the G20's Task Force on Climate-Related Financial Disclosures ("TCFD") and is available on our website at www.santos.com/sustainability

## BOARD RENEWAL

Progressive renewal of the Board continued in 2017 as we acknowledged the services of Roy Franklin OBE, Greg Martin and Scott Sheffield following their retirements and welcomed Eugene Shi and Dr Vanessa Guthrie. In February 2018, Peter Coates stepped down as Chairman and also retired from the Board.

We would like to thank Peter and the retiring Board members for their valuable counsel and guidance. Their support for our new senior executive team and three phase strategy to Transform, Build and Grow the business has set the strong foundations required to create long-term shareholder value.

## LOOKING AHEAD

In 2017 we re-structured the business to focus on five, core long-life natural gas assets, and embedded our lean, disciplined operating model. Through operational efficiency we dramatically decreased costs, improved free cash flow and reduced debt. We also invested in improving our systems and governance processes with a focus on safety and operational integrity.

2018 will be an exciting year for Santos. We are at an inflection point, poised to start our journey to growth. We will increase our capital investment across our core Australian assets and increase exploration and appraisal activities in Queensland and the Cooper Basin as well as drill more production wells. We will continue to work through the approvals process on our Narrabri Gas Project in New South Wales, with a view to leveraging our low-cost operating model to make this project a reality. We also expect to start Front End Engineering and Design on the Barossa offshore gas project which is the lead candidate for backfilling the Darwin LNG Project. In PNG we will be drilling the Muruk 2 appraisal well and potentially the Karoma exploration prospect. And we will look to the future with our new Energy Solutions business for ways to develop integrated gas, solar and energy storage projects.

We enter 2018 from a position of strength and would like to thank you, our shareholders, for your continued support.

Yours sincerely



Keith Spence
**Chairman**



Kevin Gallagher
**Managing Director and Chief Executive Officer**

# Board of Directors



## KEITH SPENCE

**Chairman**

BSc (First Class Honours in Geophysics), FAIM

Mr Spence is an independent non-executive Director. He joined the Board on 1 January 2018 and became Chairman on 19 February 2018. He is Chairman of Santos Finance Ltd and Chair of the Nomination Committee.

Mr Spence has over 40 years' experience in managing and governing oil and gas operations in Australia, Papua New Guinea, the Netherlands and Africa.

A geologist and geophysicist by training, Mr Spence commenced his career as an exploration geologist with Woodside Petroleum Limited in 1977. He subsequently joined Shell (Development) Australia, where he worked for 18 years. In 1994 he was seconded to Woodside to lead the North West Shelf Exploration team. In 1998, he left Shell to join Woodside. He retired from Woodside in 2008 after a 14-year tenure in top executive positions in the company. Upon his retirement he took up several board positions, including Clough Limited, where he served as Chairman from 2010 to 2013, Geodynamics Limited where he served as a non-executive Director from 2008 to 2016 (including as Chairman from 2010 to 2016) and Oil Search Limited, where he served as a non-executive Director from 2012 to 2017. Mr Spence is also a past Chair of the National Offshore Petroleum Safety and Environmental Management Authority Board and led the Commonwealth Government's Carbon Storage Taskforce.

Mr Spence is currently Chairman of Base Resources Limited (since 2015) and a non-executive Director of Independence Group NL (since 2014) and Murray and Roberts Holdings Limited (since 2015).



## KEVIN GALLAGHER

**Managing Director & Chief Executive Officer**

BEng (Mechanical) Hons, FIEAust

Kevin joined Santos as Managing Director and Chief Executive Officer on 1 February 2016, bringing more than 25 years' experience in managing oil and gas operations in Australia, the USA and North and West Africa.

A turnaround specialist with a track record in transforming underperforming operations, Kevin commenced his career as a drilling engineer with Mobil North Sea, before joining Woodside in 1998. During his 13-year tenure with Woodside, Kevin led the drilling organisation through rapid growth, delivering several Australian and international development projects and exploration campaigns. He also led the Australian Oil Business and was the CEO of the North West Shelf Venture at Woodside, where he was responsible for production on Australia's largest resource project.

Kevin joined Clough Limited as CEO and Managing Director in 2011, and during his 4-year tenure he implemented strategies that transformed the business and delivered record financial results. He oversaw the development of innovative programs to improve safety and drive productivity and also executed an M&A and international expansion strategy which saw Clough enter five new regions including the US, UK, Canada, Africa and Asia.

Since joining Santos, Kevin has restructured the business, removed substantial costs and significantly improved production and financial performance. He has implemented a growth strategy to focus the business on five, core long-life gas assets and has strengthened the balance sheet to provide a sustainable business in a low oil price environment.



## YASMIN ALLEN

BCom FAICD

Ms Allen is an independent non-executive Director. She joined the Board on 22 October 2014 and is the Chair of the People and Remuneration Committee and a member of the Audit and Risk Committee and Nomination Committee.

Ms Allen has extensive experience in finance and investment banking, including senior roles at Deutsche Bank AG, ANZ and HSBC Group Plc, as former Chairman of Macquarie Global Infrastructure Funds, and a former Director of EFIC (Export, Finance and Insurance Corporation). She is a Director of Cochlear Limited (since 2010), chairs its Audit Committee and is a member of the Nomination and Remuneration Committee. Ms Allen is also Director of ASX Limited (since 2015), a Director of the ASX Clearing and Settlement boards and a member of its Audit Committee.

Ms Allen is also a Director of the National Portrait Gallery and is a member of the George Institute for Global Health Board. She is Chair of Advance, was appointed a member of the Australian Government Takeovers Panel in March 2017 and is a member (and former Council member) of Chief Executive Women.

Ms Allen is a former non-executive Director of Insurance Australia Group Limited (2004 to 2015) and a former national Director (2010 to 2016), and acting Chair (2015 to 2016), of the Australian Institute of Company Directors.



## GUY COWAN

BSc (Hons), Engineering, FCA (UK) MAICD

Mr Cowan is an independent non-executive Director. He joined the Board on 10 May 2016 and is the Chair of the Audit and Risk Committee and a Director of Santos Finance Limited.

Mr Cowan had a 23-year career with Shell International in various senior commercial and financial roles. His last two roles were as CFO and Director of Shell Oil US and CFO of Shell Nigeria. He was CFO of Fonterra Co-operative Ltd between 2005 and 2009.

Mr Cowan is currently Chairman of Queensland Sugar Limited (since 2015) and a past Director of UGL Limited (2008 to 2017) where he chaired the Health and Safety Committee. Mr Cowan is also a former Director of Coffey International (2012 to 2016) and Ludowici Limited (2009 to 2012) where he chaired the Audit and Risk Committees for both companies. Mr Cowan was also a Shell-appointed alternative director of Woodside between 1992 and 1995.

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## HOCK GOH

BEng (Hons) Mech Eng

Mr Goh is an independent non-executive Director. He joined the Board on 22 October 2012 and is a member of the Environment, Health, Safety and Sustainability Committee, Audit and Risk Committee and Nomination Committee.

Mr Goh has more than 30 years' experience in the global oil and gas industry, having spent 25 years with Schlumberger Limited, including as President of Network and Infrastructure Solutions division in London, President of Asia, and Vice President and General Manager of China. He previously held managerial and staff positions in Asia, the Middle East and Europe.

Mr Goh is Chairman of MEC Resources Ltd (since 2006) and of Advent Energy Ltd (since 2007). He is a non-executive Director of Stora Enso Oyj (Finland) (since 2012), AB SKF (Sweden) (since 2014), Harbour Energy (US) (since 2015) and Vesuvius PLC (UK) (since 2015).

He was previously a non-executive Director of BPH Energy Ltd (2007 to 2015), an Operating Partner of Baird Capital Partners Asia, based in China, (2007 to 2012), and a non-executive Director of Xaloy Holding Inc in the US (2006 to 2008).



## DR VANESSA GUTHRIE

Hon DSc, PhD, BSc (Hons)

Dr Guthrie is an independent non-executive Director. She joined the Board on 1 July 2017 and is a member of the Environment, Health, Safety and Sustainability Committee.

Dr Guthrie has more than 30 years' experience in the resources sector in diverse roles such as operations, environment, community and indigenous affairs, corporate development and sustainability. She has qualifications in geology, environment, law and business management including a PhD in Geology. She was awarded an Honorary Doctor of Science from Curtin University in 2017 for her contribution to sustainability, innovation and policy leadership in the resources industry.

Dr Guthrie is the former Managing Director and CEO of Toro Energy Limited (2013 to 2016) and VP Sustainable Development at Woodside Energy, and is currently Chair of the Minerals Council of Australia, Deputy Chair of the WACA, a non-executive Director of the Australian Broadcasting Corporation, Vimy Resources Limited (since 2017), and Adelaide Brighton Limited (since 2018), and a Council member of Curtin University.

She is an active member of the Australian Institute of Company Directors and Chief Executive Women, and a Fellow of the Australian Academy of Technological Sciences and Engineering.



## PETER HEARL

BComm (With Merit), FAICD

Mr Hearl is an independent non-executive Director. He joined the Board on 10 May 2016 and is Chair of the Environment, Health, Safety and Sustainability Committee and a member of the People and Remuneration Committee and the Nomination Committee.

During an 18-year career in the oil industry with Exxon in Australia and the USA, he held a variety of senior marketing, operations, logistics and strategic planning positions. Mr Hearl joined YUM Brands (formerly PepsiCo) as KFC Australia's Director of Operations in 1991 and subsequently had several senior international leadership roles as well as being President of Pizza Hut USA, before assuming the global role of YUM Brands' Chief Operating and Development Officer in 2006, based in Dallas, Texas and Louisville, Kentucky.

He is currently a non-executive Director of Australia's largest telecommunications company, Telstra Ltd (since 2014), and chairs its Remuneration Committee.

Mr Hearl is a former non-executive Director of the Australian-listed global wine company, Treasury Wine Estates (2012 to 2017), where he chaired the Remuneration Committee and served on the Audit and Risk Committee. He was also a non-executive Director of Goodman Fielder Ltd from 2010 until that company was sold to overseas interests in 2015.



## EUGENE SHI

MBA in International Business

Mr Shi is a non-executive Director. He joined the Board on 26 June 2017 as a nominee of a substantial shareholder. Mr Shi is a member of the People and Remuneration Committee and the Audit and Risk Committee.

Mr Shi has more than 20 years of professional experience, including five years in management consultancy and 15 years in senior management roles. His industry experience covers energy, health care, retail and finance in Europe and Asia-Pacific. His specialties include capital operation, M&A and restructuring, strategy, value management, and cost optimisation.

Mr Shi is currently the Vice President of ENN Ecological (since February 2017), and General Manager of Investment Management Dept ENN Group (since 2013). His previous roles include Department Head of Business Performance Service with KPMG China and Transformation Service with KPMG Europe.

## COMMITTEES OF THE BOARD

### Audit and Risk Committee

Mr G Cowan (Chair)
Ms Y Allen
Mr H Goh
Mr E Shi

### Nomination Committee

Mr K Spence (Chair)
Ms Y Allen
Mr H Goh
Mr P Hearl

### People and Remuneration Committee

Ms Y Allen (Chair)
Mr P Hearl
Mr E Shi

### Environment, Health, Safety and Sustainability Committee

Mr P Hearl (Chair)
Mr K Gallagher
Mr H Goh
Dr V Guthrie

# Santos Executive Committee



## KEVIN GALLAGHER

**Managing Director & Chief Executive Officer**

Mr Gallagher's biography can be read on page 6.



## PHILIP BYRNE

**Executive Vice President, Marketing, Trading & Commercial**

MA (Natural Science), MSc, DIC (Petroleum Geology)

Philip joined Santos in 2017 and is responsibile for the marketing and trading of all of Santos' gas, LNG and liquid hydrocarbon products as well as the commercial function.

Philip has over 35 years' experience in the international oil and gas industry, starting his career as a Petroleum Geologist in the North Sea with Hamilton Brothers Oil & Gas. He subsequently spent 14 years with the BG Group in senior commercial and exploration leadership roles in the UK, Europe, Tunisia and India. He spent a further seven years with BHP Petroleum including General Manager Pakistan, President Gas Marketing Asia/ Australia, and Country Manager Petroleum Australia. Philip was then seconded as President of the North West Shelf Australia LNG organisation, which is the marketing arm of the North West Shelf LNG project.

Most recently, Philip was Managing Director and Chief Executive Officer of Nido Petroleum an ASX listed company with oil production and exploration acreage in the Philippines.



## BRUCE CLEMENT

**Executive Vice President, Conventional Oil & Gas**

BSc (Maths and Computer Science), BEng (Civil) Hons, MBA

Bruce joined Santos in 2016 and is responsible for building and growing Santos' conventional assets across Papua New Guinea, Northern Australia, Western Australia and Asia.

Bruce previously held the role of Vice President responsible for Santos' Narrabri Gas Project, Asian assets in Indonesia, Vietnam and Malaysia, and the company's Western Australian oil assets.

Bruce has more than 35 years' experience in the energy sector, having held managerial, financial, project management and senior technical roles in a number of companies, including Esso Australia, Ampolex and AIDC. Prior to joining Santos, Bruce was Managing Director of Roc Oil Company from 2008 to 2010 and Managing Director of AWE Limited from 2011 to 2016.



## ANGUS JAFFRAY

**Executive Vice President, Strategy & Corporate Services**

BA (Hons) Geography, MBA

Angus joined Santos in 2016, and is responsible for the delivery of the organisation's long-term strategic plan while maintaining quality corporate support services including human resources and information systems.

Angus has over 20 years of leadership and consulting experience as a Director of Azure Consulting, a Partner at The Boston Consulting Group (BCG) and a Supply Chain Manager with the global packaging group Crown Cork and Seal.

At Azure Consulting Angus supported companies in developing strategy and driving organisational change. At BCG Angus set up the Perth office, led the Australian Operations practice and was a core member of both the Mining & Metals practice and the Energy Practice. He served clients in Australia, New Zealand, Asia, Europe and North America building strong capabilities in strategy, operational efficiency and running transformation programs. As a Supply Chain Manager, Angus was accountable for procurement, planning, logistics and product delivery.



## NAOMI JAMES

**Executive Vice President, Environment, Health, Safety & Governance**

LLB (Hons), MLM

Naomi joined Santos in 2016 and is responsible for Santos' risk and audit, legal, company secretary, environment and access and safety functions, and chairs the GLNG Project Operating Committee.

Prior to joining Santos, Naomi held a range of functional and line leadership roles with Arrium including as Chief Executive of the Group's non-integrated steel businesses, Chief Legal Officer and Chief Executive, Strategy. Naomi's roles with Arrium included leading major acquisitions and divestments, business restructuring and turnaround and the legal, company secretary, government affairs and strategy functions. Naomi has previously worked in private practice at law firms in Australia and the UK.

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## ANTHONY NEILSON

### Chief Financial Officer

B.Com, MBA, FFin, ACA

Anthony joined Santos as Chief Financial Officer in 2016, and is responsible for the finance, tax, treasury and investor relations' functions. He brings over 20 years' experience in chartered accounting, banking and corporate financial roles including 15 years' experience in the upstream and downstream oil and gas industry.

Prior to joining Santos, Anthony was CEO of Roc Oil Company Ltd (ROC), which was acquired in 2014 by Hong Kong-listed investor Fosun International Limited. Previously, Anthony was Chief Financial Officer of ROC (ASX listed) and has held commercial, finance and business services roles at Caltex Australia, Credit Suisse First Boston (London) and Arthur Andersen (Sydney).

Anthony holds a Masters of Business Administration from AGSM and is a Fellow of the Financial Services Institute of Australasia and a Member of Chartered Accountants Australia and New Zealand.



## BILL OVENDEN

### Executive Vice President, Exploration & New Ventures

BSc (Hons) Geology and Geophysics

Bill joined Santos in 2002, and is responsible for developing and executing a targeted exploration and appraisal strategy across Santos' core asset hubs, while identifying new high value exploration targets.

Bill is a geologist with over 30 years of experience in the oil and gas industry. He has worked on exploration projects in Australia, Central and South-East Asia, North Africa, the Middle East and South America, with Sun Oil, Kufpec, ExxonMobil and Ampolex. He joined Santos after working for ExxonMobil in Indonesia.



## VINCE SANTOSTEFANO

### Chief Operations Officer, Operations Services

BEng (Civil), SPE

Vince joined Santos in March of 2016 and is responsible for the provision of technical and operational services to increase the scale and strategic value of Santos' assets.

Vince retired from Woodside Energy in November 2013 as Chief Operating Officer. As COO he was responsible for Woodside's producing Business Units; the Production Function including 6 LNG trains with associated offshore infrastructure, four FPSOs; the Marine Division and the Brownfields Projects Group. During 2014 and 2015, Vince was engaged in board work as a non-executive director and various management-consulting assignments. Vince has a deep and respected knowledge of the industry, with significant experience in onshore and offshore operations and asset management. He has a proven capability to manage a demanding workload and to drive cultural change.



## BRETT WOODS

### Executive Vice President, Onshore Upstream Division

BSc (Hons) Geology and Geophysics

Brett joined Santos in February 2013 and is responsible for Santos' onshore upstream assets, including Cooper Basin, GLNG and Narrabri.

Brett previously held the role as Vice President, Eastern Australia which included leading the turnaround of the production, development and commercialisation of the company's oil and gas resources in Central Australia. Prior to that he led the company's Perth-based Western Australia and Northern Territory business unit, which participates in Darwin LNG, and extensive domestic gas and oil operations in Western Australia.

Brett is a geophysicist and geologist, and has over 20 years of oil and gas industry experience operating assets throughout West Africa, Europe, Australia and Asia. Previously, Brett was Managing Director and Chief Executive Officer of Rialto Energy and has held executive management, technical leadership and business development roles with Woodside Energy and Sterling Energy PLC.

He is also a member of the APPEA Board.

# Reserves Statement
For the year ended 31 December 2017

Proved ("1P") petroleum reserves were 470 million barrels of oil equivalent ("mmboe") at the end of 2017. 1P reserves increased by 44 mmboe before production and the organic 1P reserves replacement ratio was 90%.

Proved plus probable ("2P") petroleum reserves were 848 mmboe. 2P reserves increased by 19 mmboe before production and the organic 2P reserves replacement ratio was 62%.

The key movements in 2P reserves before production in 2017 were:

- 17 mmboe increase in Papua New Guinea due to a PNG LNG reserves upgrade.
- 7 mmboe increase due to reserves upgrades in Vietnam and Indonesia.
- 5 mmboe increase in the Cooper Basin primarily due to positive field development results.
- 3 mmboe increase in WA Gas primarily due to a reserves upgrade in the John Brookes field.
- 13 mmboe net reduction in other assets primarily due to the sale of Victoria and Mereenie.

After deducting 2017 production of 60 mmboe, 1P and 2P reserves declined by 3% and 5%, respectively. Developed 2P reserves as a proportion of total 2P reserves increased to 57% (2016: 51%).

## RESERVES (SANTOS SHARE)

| Santos share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Proved reserves | mmboe | **470** | 485 | (3) |
| Proved plus probable reserves | mmboe | **848** | 889 | (5) |

## COOPER BASIN

The Cooper Basin produces natural gas, gas liquids and crude oil. Gas is sold primarily to domestic retailers, industry and for the production of liquefied natural gas ("LNG"), while gas liquids and crude oil are sold in domestic and export markets.

**Cooper Basin proved plus probable reserves by product (Santos share)**

| Santos share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Sales gas | PJ | 621 | 672 | (8) |
| Crude oil | mmbbl | 18 | 18 | (0) |
| Condensate | mmbbl | 9 | 10 | (4) |
| LPG | 000 tonnes | 1,207 | 1,288 | (6) |
| **Total** | mmboe | **144** | **154** | **(6)** |

Proved plus probable reserves increased by 5 mmboe before 2017 production primarily due to positive field results and new oil and gas development opportunities.

The significant efficiencies and cost reductions already realised in onshore drill, complete and connect activities, combined with a renewed commitment to exploration and appraisal, are expected to result in reserve additions over time.

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## QUEENSLAND

In Queensland, Santos has a 30% interest in the GLNG project and various interests in other non-operated fields. GLNG produces LNG for export to global markets from the LNG plant at Gladstone. Gas is also sold into domestic markets.

**Queensland proved plus probable reserves by product (Santos share)**

| Santos share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Sales gas – GLNG JV | PJ | 1,536 | 1,577 | (3) |
| Sales gas – other non-operated | PJ | 387 | 403 | (4) |
| **Total** | mmboe | **331** | **341** | **(3)** |

Proved plus probable reserves increased by 2 mmboe before 2017 production. Santos share Queensland reserves include Santos' share of the non-operated Combabula, Ramyard and Spring Gully fields.

**GLNG reserves (GLNG 100% share)**

| GLNG 100% share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Proved reserves | PJ | 2,390 | 2,486 | (4) |
| Proved plus probable reserves | PJ | 5,119 | 5,256 | (3) |

GLNG share proved plus probable reserves were maintained before 2017 production. In addition to the reserves in the table above, GLNG has Santos portfolio and third party gas supply agreements in place for periods of up to 20 years.

Santos is committed to ongoing appraisal and operational efficiencies to potentially mature resources to reserves and develop for additional gas supply to the project.

## PAPUA NEW GUINEA

Santos' business in Papua New Guinea ("PNG") is centred on the PNG LNG Project. Completed in 2014, PNG LNG produces LNG for export to global markets, as well as gas and gas liquids. Santos has a 13.5% interest in PNG LNG.

**Papua New Guinea proved plus probable reserves by product (Santos share)**

| Santos share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Sales gas | PJ | 1,234 | 1,215 | 2 |
| Condensate | mmbbl | 15 | 14 | 11 |
| **Total** | mmboe | **227** | **222** | **2** |

Proved plus probable reserves increased by 17 mmboe before 2017 production. Continued strong Hides field performance, including a revised condensate forecast, and improved LNG plant performance contributed to the increase.

PNG LNG underpins the majority of Santos' reserves and resources in Papua New Guinea. As a foundation partner of the PNG LNG project, Santos' equity provides a strong position off which to leverage growth opportunities, including LNG backfill and expansion.

Santos also has an extensive exploration position throughout Papua New Guinea and holds interests in several licences across the Papua New Guinea Fold Belt, Gulf of Papua and Papua New Guinea Forelands, which contain large-scale discoveries and propectivity that could provide future backfill, expansion or standalone development opportunities.

- **PPL-402** (Santos 20%, subject to future government back-in) contains the recent Muruk gas discovery. The Muruk gas field is located in close proximity to the Hides gas field and PNG LNG network infrastructure, potentially providing a simplified development pathway and access to export LNG markets via backfill or expansion of the PNG LNG project. A seismic acquisition program to assist in delineating the Muruk gas discovery and the adjacent Karoma prospect is planned for the first half of 2018, with an appraisal well on Muruk expected to be spudded in the second quarter.
- **PRL-38** (Santos 10%, subject to future government back-in) is located offshore in the Gulf of Papua and contains the Pandora A and B gas fields. The Joint Venture intends to drill a well in PRL-38 in 2018–19 to test near-field exploration opportunities or appraise discovered resources. The Joint Venture is continuing to assess the technical and commercial viability of various potential development options.
- **PRL-9** (Santos 40%, subject to future government back-in) contains the Barikewa gas discovery. The Joint Venture intends to drill an appraisal well during 2018 to appraise the discovered resources. The Barikewa gas field is located in close proximity to the PNG LNG network infrastructure and the Joint Venture is continuing to assess the technical and commercial viability of various development options.

# Reserves Statement
continued

## NORTHERN AUSTRALIA

In Northern Australia, Santos has an 11.5% interest in the Bayu-Undan/Darwin LNG Project, which produces LNG and gas liquids for export to global markets.

**Northern Australia proved plus probable reserves by product (Santos share)**

| Santos share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Sales gas | PJ | 65 | 72 | (9) |
| Condensate | mmbbl | 2 | 2 | (21) |
| LPG | 000 tonnes | 94 | 141 | (33) |
| **Total** | mmboe | **14** | **15** | **(12)** |

Proved plus probable reserves increased by 2 mmboe before 2017 production primarily due to the sanction of the next phase of Bayu-Undan infill well development.

Santos has a strong infrastructure and discovered resource position across Northern Australia, with multi-tcf scale discoveries across the Browse and Bonaparte Basins, in close proximity to Darwin LNG and other LNG projects under construction in the region.

- **Bayu-Undan** (Santos 11.5%) is the current gas supply source to Darwin LNG ("DLNG"). Reserves are being extended through the drilling of infill wells, with first gas targeted for late 2018.
- **Barossa Caldita** (Santos 25%) is a multi-tcf discovery being positioned to backfill DLNG. Successful appraisal drilling in 2017 resulted in a significant resource upgrade. A FEED-entry decision is targeted for the first half of 2018.
- **Petrel-Tern and Frigate** (Santos 35% and 40% respectively) are well appraised assets located approximately 300 kilometres from Darwin. Potential commercialisation options are being evaluated with opportunity to target LNG, NT domestic and east coast markets.
- **Crown and Lasseter** (Santos 30%) have material resources with further prospectivity and are located near large LNG projects under construction. Concept evaluation to support standalone and joint development options are being considered.

## WA GAS

Santos is one of the largest producers of domestic natural gas in Western Australia and is also a significant producer of gas liquids.

**WA Gas proved plus probable reserves by product (Santos share)**

| Santos share | Unit | 2017 | 2016 | %change |
|---|---|---|---|---|
| Sales gas | PJ | 608 | 641 | (5) |
| Condensate | mmbbl | 6 | 7 | (5) |
| **Total** | mmboe | **111** | **117** | **(5)** |

Proved plus probable reserves increased by 3 mmboe before 2017 production, primarily due to a reserves upgrade at John Brookes.

Santos has an established position in the Carnarvon Basin which underpins the Western Australia domestic gas business. The Varanus Island and Devil Creek domestic gas infrastructure is supplied by John Brookes, Spar, Halyard and Reindeer, and a discovered and prospective resource base that supports backfill of these facilities in the longer term.

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## PROVED RESERVES

### Year-end 2017 (Santos share)

| Asset | Sales gas PJ | Crude oil mmbbl | Condensate mmbbl | LPG 000 tonnes | All products mmboe Developed | Undeveloped | Total |
|---|---|---|---|---|---|---|---|
| Cooper Basin | 291 | 8 | 4 | 519 | 47 | 19 | 66 |
| Queensland[1] | 859 | - | - | - | 110 | 38 | 148 |
| PNG | 891 | 0 | 11 | - | 110 | 53 | 163 |
| Northern Australia | 53 | - | 1 | 58 | 9 | 2 | 11 |
| WA Gas | 369 | - | 4 | - | 61 | 6 | 67 |
| Other Assets[2] | 28 | 10 | 0 | - | 14 | 1 | 15 |
| **Total 1P** | **2,491** | **18** | **20** | **577** | **349** | **120** | **470** |
| Proportion of total proved reserves that are unconventional | | | | | | | 32% |

1 Queensland proved sales gas reserves include 717 PJ GLNG and 142 PJ other Santos non-operated Eastern Queensland assets.

2 Indonesia, Vietnam and Western Australia oil.

## PROVED RESERVES RECONCILIATION

| Product | Unit | Reserves Year-end 2016 | Production | Revisions and extensions | Discoveries | Net acquisitions and divestments | Reserves Year-end 2017 |
|---|---|---|---|---|---|---|---|
| Sales gas | PJ | **2,590** | (284) | 237 | 2 | (54) | **2,491** |
| Crude oil | mmbbl | **17** | (6) | 8 | - | (0) | **18** |
| Condensate | mmbbl | **19** | (3) | 4 | 0 | (0) | **20** |
| LPG | 000 tonnes | **638** | (145) | 81 | 3 | - | **577** |
| **Total 1P** | mmboe | **485** | **(60)** | **53** | **0** | **(10)** | **470** |

# Reserves Statement
continued

## PROVED PLUS PROBABLE RESERVES

### Year-end 2017 (Santos share)

| Asset | Sales gas PJ | Crude oil mmbbl | Condensate mmbbl | LPG 000 tonnes | All products mmboe Developed | Undeveloped | Total |
|---|---|---|---|---|---|---|---|
| Cooper Basin | 621 | 18 | 9 | 1,207 | 100 | 44 | 144 |
| Queensland[1] | 1,922 | - | - | - | 110 | 221 | 331 |
| PNG | 1,234 | 0 | 15 | - | 152 | 75 | 227 |
| Northern Australia | 65 | - | 2 | 94 | 10 | 3 | 14 |
| WA Gas | 608 | - | 6 | - | 89 | 21 | 111 |
| Other Assets[2] | 45 | 15 | 0 | - | 21 | 2 | 23 |
| **Total 2P** | **4,496** | **33** | **33** | **1,301** | **483** | **366** | **848** |
| Proportion of total proved plus probable reserves that are unconventional | | | | | | | 39% |

1 Queensland proved plus probable sales gas reserves include 1,536 PJ GLNG and 387 PJ other Santos non-operated Eastern Queensland assets.

2 Indonesia, Vietnam and Western Australia oil.

## PROVED PLUS PROBABLE RESERVES RECONCILIATION

| Product | Unit | Reserves Year-end 2016 | Production | Revisions and extensions | Discoveries | Net acquisitions and divestments | Reserves Year-end 2017 |
|---|---|---|---|---|---|---|---|
| Sales gas | PJ | **4,730** | (284) | 147 | 4 | (101) | **4,496** |
| Crude oil | mmbbl | **33** | (6) | 7 | - | (1) | **33** |
| Condensate | mmbbl | **33** | (3) | 4 | 0 | (0) | **33** |
| LPG | 000 tonnes | **1,429** | (145) | 9 | 8 | - | **1,301** |
| **Total 2P** | mmboe | **889** | **(60)** | **36** | **1** | **(18)** | **848** |

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**Notes**

1. This reserves statement:
   a. is based on, and fairly represents, information and supporting documentation prepared by, or under the supervision of, the qualified petroleum reserves and resources evaluators listed in note 14 of this reserves statement. Details of each qualified petroleum reserves and resources evaluator's employment and professional organisation membership are set out in note 14 of this reserves statement; and
   b. as a whole has been approved by Barbara Pribyl, who is a qualified petroleum reserves and resources evaluator and whose employment and professional organisation membership details are set out in note 14 of this reserves statement; and
   c. is issued with the prior written consent of Barbara Pribyl as to the form and context in which the estimated petroleum reserves and contingent resources and the supporting information are presented.
2. The estimates of petroleum reserves and contingent resources contained in this reserves statement are as at 31 December 2017.
3. Santos prepares its petroleum reserves and contingent resources estimates in accordance with the Petroleum Resources Management System ("PRMS") sponsored by the Society of Petroleum Engineers ("SPE").
4. This reserves statement is subject to risk factors associated with the oil and gas industry. It is believed that the expectations of petroleum reserves and contingent resources reflected in this statement are reasonable, but they may be affected by a range of variables which could cause actual results or trends to differ materially, including but not limited to: price fluctuations, actual demand, currency fluctuations, geotechnical factors, drilling and production results, gas commercialisation, development progress, operating results, engineering estimates, loss of market, industry competition, environmental risks, physical risks, legislative, fiscal and regulatory developments, economic and financial markets conditions in various countries, approvals and cost estimates.
5. All estimates of petroleum reserves and contingent resources reported by Santos are prepared by, or under the supervision of, a qualified petroleum reserves and resources evaluator or evaluators. Processes are documented in the Santos Reserves Guidelines which are overseen by a Reserves Committee. The frequency of reviews is dependent on the magnitude of the petroleum reserves and contingent resources and changes indicated by new data. If the changes are material, they are reviewed by the Santos internal technical leaders, prior to overall approval by management and the Reserves Committee.
6. Santos engages independent experts Gaffney, Cline & Associates, Netherland, Sewell & Associates, Inc. and DeGolyer and MacNaughton to audit and/or evaluate reserves and contingent resources. Each auditor found, based on the outcomes of its respective audit and evaluation, and its understanding of the estimation processes employed by Santos, that Santos' 31 December 2017 petroleum reserves and contingent resources quantities in aggregate compare reasonably to those estimates prepared by each auditor. Thus, in the aggregate, the total volumes summarised in the tables included in this reserves statement represent a reasonable estimate of Santos' petroleum reserves and contingent resources position as at 31 December 2017.
7. Unless otherwise stated, all references to petroleum reserves and contingent resources quantities in this reserves statement are Santos' net share.
8. Reference points for Santos' petroleum reserves and contingent resources and production are defined points within Santos' operations where normal exploration and production business ceases, and quantities of produced product are measured under defined conditions prior to custody transfer. Fuel, flare and vent consumed to the reference points are excluded.
9. Petroleum reserves and contingent resources are aggregated by arithmetic summation by category and as a result, proved reserves may be a very conservative estimate due to the portfolio effects of arithmetic summation.
10. Petroleum reserves and contingent resources are typically prepared by deterministic methods with support from probabilistic methods.
11. Any material concentrations of undeveloped petroleum reserves that have remained undeveloped for more than 5 years: (a) are intended to be developed when required to meet contractual obligations; and (b) have not been developed to date because they have not yet been required to meet contractual obligations.
12. Petroleum reserves replacement ratio is the ratio of the change in petroleum reserves (excluding production) divided by production. Organic reserves replacement ratio excludes net acquisitions and divestments.
13. Information on petroleum reserves and contingent resources quoted in this reserves statement is rounded to the nearest whole number. Some totals in the tables may not add due to rounding. Items that round to zero are represented by the number 0, while items that are actually zero are represented with a dash "-".
14. Qualified Petroleum Reserves and Resources Evaluators

| Name | Employer | Professional organisation |
|---|---|---|
| B Pribyl | Santos Ltd | SPE |
| S Chipperfield | Santos Ltd | SPE |
| B Camac | Santos Ltd | SPE, PESA |
| E Klettke | Santos Ltd | SPE, APEGA |
| N Pink | Santos Ltd | SPE |
| S Lawton | Santos Ltd | SPE |
| J Telford | Santos Ltd | SPE |
| A Wisnugroho | Santos Ltd | SPE |
| C Harwood | Santos Ltd | PESA, AAPG |
| I Pedler | Santos Ltd | SPE |
| D Smith | NSAI | SPE |

SPE: Society of Petroleum Engineers

APEGA: The Association of Professional Engineers and Geoscientists of Alberta

PESA: Petroleum Exploration Society of Australia

AAPG: American Association of Petroleum Geologists

**Abbreviations and conversion factors**

**Abbreviations**

| | |
|---|---|
| 1P | proved reserves |
| 2P | proved plus probable reserves |
| GJ | gigajoules |
| LNG | liquefied natural gas |
| LPG | liquefied petroleum gas |
| mmbbl | million barrels |
| mmboe | million barrels of oil equivalent |
| NGLs | natural gas liquids |
| PJ | petajoules |
| tcf | trillion cubic feet |
| TJ | terajoules |

**Conversion factors**

| | |
|---|---|
| Sales gas and ethane, 1 PJ | 171,937 boe |
| Crude oil, 1 barrel | 1 boe |
| Condensate, 1 barrel | 0.935 boe |
| LPG, 1 tonne | 8.458 boe |

# Directors' Report

## DIRECTORS' REPORT

The Directors present their report together with the consolidated financial report of the consolidated entity, being Santos Limited ("Santos" or "the Company") and its controlled entities, for the financial year ended 31 December 2017, and the Auditor's Report thereon. Information in the Annual Report referred to in this report, including the Remuneration Report, or contained in a note to the financial statements referred to in this report forms part of, and is to be read as part of, this report.

## DIRECTORS, DIRECTORS' SHAREHOLDINGS AND DIRECTORS' MEETINGS

### Directors and Directors' Shareholdings

The names of Directors of the Company in office at the date of this report and details of the relevant interest of each of those Directors in shares in the Company at that date are as set out below:

| Surname | Other Names | Shareholdings in Santos Limited |
|---|---|---|
| Allen | Yasmin Anita | 15,883 |
| Cowan | Guy Michael | 15,000 |
| Gallagher | Kevin Thomas | 341,614 |
| Goh | Hock | 37,215 |
| Guthrie | Vanessa Ann | 0 |
| Hearl | Peter Roland | 48,808 |
| Shi | Eugene | 0 |
| Spence | Keith William (Chairman) | 65,000 |

The above-named Directors held office during and/or since the end of the financial year. Mr Scott Sheffield was a Director until his retirement at the Annual General Meeting on 4 May 2017. Mr Gregory Martin retired as a Director on 25 August 2017. Mr Roy Franklin retired as a Director on 30 September 2017. Mr Eugene Shi was appointed as a Director on 26 June 2017. Dr Vanessa Guthrie was appointed as a Director on 1 July 2017. Mr Keith Spence was appointed as a Director on 1 January 2018, and as Chairman on 19 February 2018. Mr Peter Coates was a Director and Chairman until his retirement on 19 February 2018. There were no other persons who acted as Directors at any time during the financial year and up to the date of this report. All shareholdings are of fully paid ordinary shares. No Director holds a relevant interest in a related body corporate of Santos Limited.

At the date of this report, Mr Gallagher holds 1,739,872 share acquisition rights (SARs) and 111,038 Restricted Deferred Shares. No other Director holds options or SARs.

Details of the qualifications, experience and special responsibilities of each Director are set out in the Directors' biographies on pages 6 and 7 of this Annual Report. This information includes details of other listed company directorships held during the last three years.

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**Directors' Meetings**

The number of Directors' meetings and meetings of committees of Directors held during the financial year and the number of meetings attended by each Director are set out below:

***Table of Directors' Meetings***

| Director | | Directors' Meeting | Audit & Risk Committee | Environment Health, Safety & Sustainability Committee | People & Remuneration Committee | Nomination Committee |
|---|---|---|---|---|---|---|
| | | Attended/Held[1] | Attended/Held[1] | Attended/Held[1] | Attended/Held[1] | Attended/Held[1] |
| Allen[2] | Yasmin A. | 14 of 15 | 1 of 1 | 3 of 3 | 4 of 4 | 1 of 1 |
| Coates | Peter R. | 15 of 15 | n/a | n/a | n/a | 3 of 3 |
| Cowan | Guy M. | 14 of 15 | 4 of 4 | n/a | n/a | n/a |
| Franklin[3] | Roy A. | 10 of 11 | n/a | 3 of 3 | 2 of 2 | 2 of 2 |
| Gallagher | Kevin T. | 15 of 15 | n/a | 4 of 4 | n/a | n/a |
| Goh[4] | Hock | 11 of 15 | 3 of 4 | 3 of 4 | n/a | n/a[5] |
| Guthrie[6] | Vanessa A. | 9 of 9 | n/a | 1 of 1 | n/a | n/a |
| Hearl[7] | Peter R. | 13 of 15 | 3 of 3 | 1 of 1 | 2 of 2 | 1 of 1 |
| Martin[8] | Gregory J. W. | 10 of 10 | 3 of 3 | n/a | 2 of 2 | 2 of 2 |
| Sheffield[9] | Scott D. | 4 of 5 | n/a | n/a | n/a | n/a |
| Shi[10] | Eugene | 9 of 10 | 1 of 1 | n/a | 2 of 2 | n/a |

1 Reflects the number of meetings held during the time the Director held office, or was a member of the Committee, during the year.

2 Ms YA Allen was appointed as the Chair of the People and Remuneration Committee and a member of the Nomination Committee on 21 September 2017. Ms YA Allen retired as a member of the Environment, Health, Safety and Sustainability Committee and was appointed as a member of the Audit and Risk Committee on 25 October 2017.

3 Mr RA Franklin retired as a Director on 30 September 2017.

4 In November 2017, Mr H Goh commenced a leave of absence due to a conflict of interest arising from his position as a Director of Harbour Energy.

5 Mr H Goh was appointed as a member of the Nomination Committee on 25 October 2017.

6 Dr VA Guthrie was appointed as a Director on 1 July 2017 and as a member of the Environment, Health, Safety and Sustainability Committee on 25 October 2017.

7 Mr PR Hearl was appointed as a member of the Nomination Committee on 21 September 2017 and as Chairman of the Environment, Health, Safety and Sustainability Committee on 25 October 2017. Mr PA Hearl retired as a member of the Audit and Risk Committee on 25 October 2017.

8 Mr GJW Martin retired as a Director on 25 August 2017.

9 Mr SD Sheffield retired as a Director on 4 May 2017.

10 Mr E Shi was appointed as a Director on 26 June 2017, was appointed as a member of the People and Remuneration Committee on 21 September 2017 and as a member of the Audit and Risk Committee on 25 October 2017.

# Directors' Report
continued

## OPERATING AND FINANCIAL REVIEW

Santos' principal activities during 2017 were the exploration for, and development, production, transportation and marketing of, hydrocarbons. There were no significant changes in the nature of these activities during the year. Revenue is derived primarily from the sale of gas and liquid hydrocarbons.

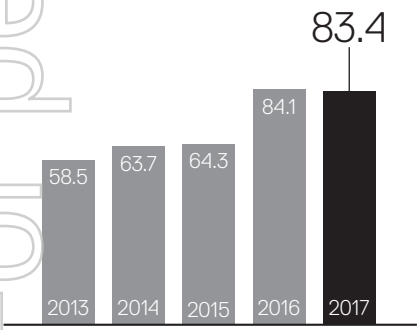
A review of the operations and of the results of those operations of the consolidated entity during the year is as follows:

### Summary of results table

| | **2017 mmboe** | 2016 mmboe | Variance % |
|---|---|---|---|
| Production volume | **59.5** | 61.6 | (3) |
| Sales volume | **83.4** | 84.1 | (1) |
| | **US$million** | US$million | |
| Product sales | **3,107** | 2,594 | 20 |
| EBITDAX[1] | **1,428** | 1,199 | 19 |
| Exploration and evaluation expensed | **(94)** | (138) | 32 |
| Depreciation and depletion | **(742)** | (741) | – |
| Net impairment loss | **(938)** | (1,561) | 40 |
| Change in future restoration assumptions | **31** | 37 | (16) |
| EBIT[1] | **(315)** | (1,204) | 74 |
| Net finance costs | **(270)** | (281) | 4 |
| Taxation benefit | **225** | 438 | (49) |
| Net loss for the period and attributable to equity holders of Santos | **(360)** | (1,047) | 66 |
| Underlying profit for the period[1] | **336** | 63 | 433 |
| Underlying earnings per share (cents)[1] | **16.2** | 3.5 | 363 |

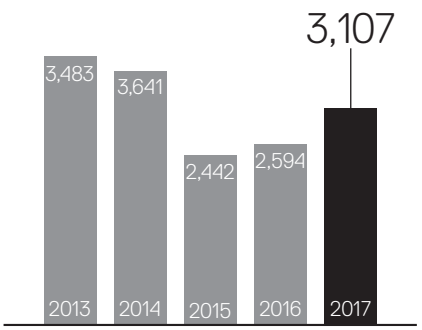
1 EBITDAX (earnings before interest, tax, depreciation, depletion, exploration and evaluation and impairment), EBIT (earnings before interest and tax) and underlying profit are non-IFRS measures that are presented to provide an understanding of the underlying performance of Santos' operations. Underlying profit excludes the impacts of asset acquisitions, disposals and impairments, as well as items that are subject to significant variability from one period to the next, including the effects of fair value adjustments and fluctuations in exchange rates. Please refer to page 22 for the reconciliation from net loss to underlying profit for the period. Underlying earnings per share represents underlying profit for the period divided by the weighted average number of shares on issue during the year. The non-IFRS financial information is unaudited however the numbers have been extracted from the audited financial statements.

**Sales volume**
mmboe



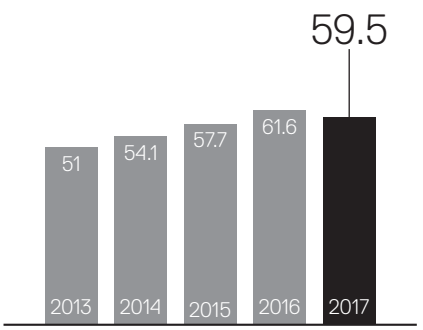

Sales volumes of 83.4 million barrels of oil equivalent (mmboe) were 1% lower than the previous year. Higher LNG sales volumes due to the ramp-up of GLNG, ongoing strong production from PNG LNG, and higher domestic gas sales in WA, were offset by asset sales and lower Cooper Basin sales volumes, slightly reducing sales volumes compared to the prior year.

**Product sales revenue**
US$million




Sales revenue increased 20% compared to the previous year to $3.1 billion, primarily due to higher oil and LNG prices, and higher LNG sales volumes. The average realised oil price increased 25% to US$57.85/bbl and the average realised LNG price increased 21% to US$7.31/mmBtu.

**Production volume**
mmboe




Production was 3% lower than the previous year primarily due to the sale of the Victorian, Mereenie and Stag assets, partially offset by the ramp-up of GLNG and higher PNG LNG production.

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**Review of operations**

Santos' operations are focused on five core, long-life natural gas assets: Cooper Basin, Queensland, Papua New Guinea, Northern Australia and Western Australia Gas. Other assets are run separately for value as a standalone business.

***Cooper Basin***

The Cooper Basin produces natural gas, gas liquids and crude oil. Gas is sold primarily to domestic retailers, industry and for the production of liquefied natural gas, while gas liquids and crude oil are sold in domestic and export markets.

Santos' strategy in the Cooper Basin is to deliver a low-cost, cash flow positive business by building production, investing in new technology to lower development and exploration costs, and increasing utilisation of infrastructure including the Moomba plant.

| **Cooper Basin** | **2017** | 2016 |
|---|---|---|
| Production (mmboe) | **14.4** | 15.1 |
| Sales volume (mmboe) | **21.0** | 23.5 |
| Revenue (US$m) | **833** | 768 |
| Production cost (US$/boe) | **9.32** | 10.71 |
| EBITDAX (US$m) | **328** | 258 |
| Capex (US$m) | **199** | 173 |

Cooper Basin EBITDAX was $328 million, 27% higher than 2016 primarily due to higher sales revenue impacted by higher oil prices, in addition to lower production costs resulting from cost-saving initiatives.

Santos' share of Cooper Basin sales gas and ethane production of 58.4 petajoules (PJ) was 5% lower than the corresponding period (61.2 PJ) as new development activity predominantly offset the impact of natural field decline.

At June 2017, Santos recognised an impairment write-back of $336 million after tax. The impacts of lower US$ oil price assumptions were more than offset by a continuation of the cost efficiencies and performance improvement achieved during 2016, allowing increased drilling activity and production.

***Queensland***

GLNG produces liquefied natural gas (LNG) for export to global markets from the LNG plant at Gladstone. Gas is also sold into the domestic market. Santos has a 30% interest in GLNG.

The LNG plant has two LNG trains with a combined nameplate capacity of 7.8 mtpa. Production from Train 1 commenced in September 2015 and Train 2 in May 2016. Feed gas is sourced from GLNG's upstream fields, Santos portfolio gas and third-party suppliers.

The LNG plant produced 5.2 million tonnes of LNG in 2017 and shipped 89 cargoes.

Santos aims to build GLNG gas supply through upstream development, seek opportunities to extract value from existing infrastructure and drive efficiencies to operate at lowest cost.

| **Queensland** | **2017** | 2016 |
|---|---|---|
| Production (mmboe) | **11.5** | 9.5 |
| Sales volume (mmboe) | **22.7** | 19.2 |
| Revenue (US$m) | **764** | 540 |
| Production cost (US$/boe) | **5.92** | 6.44 |
| EBITDAX (US$m) | **329** | 191 |
| Capex (US$m) | **178** | 228 |

GLNG EBITDAX of $329 million increased 72% compared to 2016. This was a result of higher sales revenue reflecting the ramp-up of upstream production and higher LNG prices and lower costs.

At June 2017, Santos recognised an impairment charge against the carrying value for GLNG of $867 million after tax. The impairment was primarily due to lower forecast US$ oil prices.

# Directors' Report
continued

***Papua New Guinea***

Santos' business in Papua New Guinea is centred on the PNG LNG project. Completed in 2014, PNG LNG produces LNG for export to global markets, as well as sales gas and gas liquids. Santos has a 13.5% interest in PNG LNG.

The LNG plant near Port Moresby has two LNG trains with the combined capacity to produce more than eight million tonnes per annum. Production from both trains commenced in 2014 and operated at record rates in 2017, producing 8.3 million tonnes of LNG and shipping 110 cargoes. Condensate production was 10.9 million barrels.

Santos' strategy in Papua New Guinea is to work with its partners to align interests, and support and participate in backfill and expansion opportunities at PNG LNG.

During 2017, Santos and its partners announced a potentially significant new gas discovery at Muruk, located 21 kilometres from the existing PNG LNG production facilities at Hides. Data from the Muruk drilling program is being evaluated to inform forward appraisal options. Well site preparations are underway ahead of a planned Muruk appraisal program in 2018.

| **PNG** | **2017** | 2016 |
|---|---|---|
| Production (mmboe) | **12.6** | 12.2 |
| Sales volume (mmboe) | **12.0** | 11.8 |
| Revenue (US$m) | **532** | 444 |
| Production cost (US$/boe) | **4.37** | 4.59 |
| EBITDAX (US$m) | **430** | 350 |
| Capex (US$m) | **18** | 8 |

Papua New Guinea EBITDAX of $430 million increased 23% compared to 2016, mainly due to higher LNG prices.

***Northern Australia***

Santos' business in Northern Australia is focused on the Bayu-Undan/Darwin LNG (DLNG) project. In operation since 2006, DLNG produces LNG and gas liquids for export to global markets. Santos has an 11.5% interest in DLNG.

The LNG plant near Darwin has a single LNG train with a nameplate capacity of 3.7 mtpa. The plant produced 3.3 million tonnes of LNG in 2017 and shipped 51 cargoes. Condensate production was three million barrels.

Santos' strategy in Northern Australia is to support plans to progress Darwin LNG backfill, expand the company's acreage footprint and appraise the onshore McArthur Basin.

During 2017, a two-well appraisal drilling campaign in the Barossa field (Santos 25%) was successfully completed. Positive results from the campaign, including a successful production test of Barossa-6, strengthened the field's position as lead candidate to supply backfill gas to Darwin LNG.

| **Northern Australia** | **2017** | 2016 |
|---|---|---|
| Production (mmboe) | **4.0** | 4.2 |
| Sales volume (mmboe) | **4.0** | 4.2 |
| Revenue (US$m) | **153** | 145 |
| Production cost (US$/boe) | **18.95** | 17.58 |
| EBITDAX (US$m) | **87** | 86 |
| Capex (US$m) | **55** | 14 |

Northern Australia EBITDAX of $87 million was 1% higher than 2016.

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***Western Australia Gas***

Santos is one of the largest producers of domestic natural gas in Western Australia and is also a significant producer of gas liquids.

Santos' position in two WA domestic gas hubs (Varanus Island and Devil Creek) provides opportunities to meet short-term and long-term domestic gas demand in the state.

Santos' focus in WA is to grow production and market share in the WA domestic gas market.

| **WA Gas** | **2017** | 2016 |
|---|---|---|
| Production (mmboe) | **9.2** | 8.9 |
| Sales volume (mmboe) | **9.4** | 8.8 |
| Revenue (US$m) | **262** | 184 |
| Production cost (US$/boe) | **5.82** | 5.11 |
| EBITDAX (US$m) | **201** | 206 |
| Capex (US$m) | **37** | 24 |

WA Gas EBITDAX of $201 million was 2% lower than 2016.

Santos' share of Western Australia gas and condensate production was 51.2PJ and 0.5 mmbbl respectively.

***Other assets – Asia, NSW and WA Oil***

Santos' other assets have been packaged and run separately as a standalone business. These assets include Santos interests in Indonesia, Vietnam, New South Wales and Western Australia oil. The portfolio will be continually optimised to drive efficiency and shareholder value. Effective 1 January 2018, the Narrabri asset in New South Wales will be managed as part of the core asset portfolio.

Consistent with optimising the portfolio to maximise value, Santos sold its Victorian assets and Mereenie (Northern Territory) effective 1 January 2017.

| **Other assets** | **2017** | 2016 |
|---|---|---|
| Production (mmboe) | **7.7** | 11.8 |
| Sales volume (mmboe) | **7.7** | 11.7 |
| Revenue (US$m) | **346** | 411 |
| Production cost (US$/boe) | **15.91** | 14.06 |
| EBITDAX (US$m) | **223** | 246 |
| Capex (US$m) | **81** | 84 |

Other assets EBITDAX of $223 million was 9% lower than 2016.

Total production and sales volumes from Other assets were lower than the previous year primarily due to the sale of the Victorian, Mereenie and Stag assets.

During 2017, Santos recognised an impairment charge of $149 million after tax on the non-core Ande Ande Lumut asset in Indonesia, following an assessment of the impact of lower oil prices.

# Directors' Report
continued

## Net loss

The 2017 net loss attributable to equity holders of Santos Limited of $360 million is $687 million lower than the net loss of $1,047 million in 2016. This decrease is primarily due to lower impairment losses of $703 million after tax ($1,101 million in 2016) and higher sales revenue as a result of favourable product prices and LNG volumes.

Net loss includes items before tax of $1,048 million ($696 million after tax), as referred to in the reconciliation of net loss to underlying profit below. Underlying profit was $336 million, $273 million higher than 2016.

***Reconciliation of net loss to underlying profit[1]***

| | 2017 US$million | | | 2016 US$million | | |
|---|---|---|---|---|---|---|
| | **Gross** | **Tax** | **Net** | Gross | Tax | Net |
| Net loss after tax attributable to equity holders of Santos Limited | | | **(360)** | | | (1,047) |
| Add/(deduct) the following: | | | | | | |
| Net gains on sales of non-current assets | **(79)** | **20** | **(59)** | (25) | 8 | (17) |
| Impairment losses | **938** | **(235)** | **703** | 1,561 | (460) | 1,101 |
| Change in future restoration assumptions | **(31)** | **9** | **(22)** | (37) | 10 | (27) |
| Foreign exchange (gains)/ losses | **153** | **(16)** | **137** | (34) | 6 | (28) |
| Fair value adjustments on embedded derivatives and hedges | **(14)** | **4** | **(10)** | 39 | (11) | 28 |
| Remediation (income)/costs for incidents net of related insurance recoveries | **–** | **–** | **–** | (10) | – | (10) |
| Fair value adjustments on commodity hedges | **63** | **(19)** | **44** | 15 | (5) | 10 |
| Other expense items[2] | **18** | **(3)** | **15** | 63 | (18) | 45 |
| Tax impact of foreign exchange on deferred tax assets | **–** | **(100)** | **(100)** | – | 15 | 15 |
| Other one-off tax adjustments | **–** | **(12)** | **(12)** | – | (7) | (7) |
| | **1,048** | **(352)** | **696** | 1,572 | (462) | 1,110 |
| **Underlying profit[1]** | | | **336** | | | 63 |

1 Underlying profit is a non-IFRS measure that is presented to provide an understanding of the underlying performance of Santos' operations. The measure excludes the impacts of asset acquisitions, disposals and impairments, as well as items that are subject to significant variability from one period to the next, including the effects of fair value adjustments and fluctuations in exchange rates. The non-IFRS financial information is unaudited, however the numbers have been extracted from the financial statements which have been subject to audit by the Company's auditor.

2 Other expense items in 2017 relate to a dispute settlement payment, restructure costs including redundancy payments and a provision for a doubtful debtor; offset by onerous contract provision movement for unutilised transport capacity.

## Financial position

***Summary of financial position***

| | **2017 US$million** | 2016 US$million | Variance US$million |
|---|---|---|---|
| Exploration and evaluation assets | **459** | 495 | (36) |
| Oil and gas assets and other land, buildings, plant and equipment | **9,662** | 10,533 | (871) |
| Restoration provision | **(1,528)** | (1,468) | (60) |
| Other net assets/(liabilities)[1] | **120** | 167 | (47) |
| Total funds employed | **8,713** | 9,727 | (1,014) |
| Net debt[2] | **(2,731)** | (3,492) | 761 |
| Net tax assets/(liabilities)[3] | **1,169** | 845 | 324 |
| Net assets/equity | **7,151** | 7,080 | 71 |

1 Other net assets/(liabilities) comprises trade and other receivables, prepayments, inventories, other financial assets, share of investments in joint ventures, offset by trade and other payables, deferred income, provisions and other financial liabilities.

2 Net debt reflects the net borrowings position and includes interest bearing loans, net of cash and interest rate and cross-currency swap contracts.

3 Net tax assets/(liabilities) comprises deferred tax assets and tax receivable, offset by deferred tax liabilities and current tax payable.

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**Impairment of assets**

During the Company's regular review of asset carrying values, Santos undertook an impairment review as part of the preparation of its 2017 full-year accounts.

At 31 December 2017, non-cash after-tax impairment losses of $14 million were recognised in addition to the non-cash after-tax impairment of $689 million recognised at 30 June 2017. The total after-tax impairment losses of $703 million for the year primarily relate to the 30 June 2017 impairment of GLNG.

**Exploration and evaluation assets**

Exploration and evaluation assets were $459 million compared to $495 million at the end of 2016, a decrease of $36 million, mainly due to impairment losses before tax of $163 million, exploration and evaluation expenses of $17 million; offset by 2017 capital expenditure, including drilling in Papua New Guinea, Cooper Basin and Barossa Caldita, along with evaluation studies, in addition to acquisition costs comprising interests in Muruk and Western Farm-in.

**Oil and gas assets and other land, buildings, plant and equipment**

Oil and gas assets and other land and buildings, plant and equipment of $9,662 million were $871 million lower than in 2016 mainly due to impairment losses before tax of $770 million and depreciation and depletion charges, offset by 2017 capital expenditure, including GLNG, WA Gas and the Cooper Basin.

**Restoration provision**

Restoration provision balances have increased by $60 million to $1,528 million mainly due to revised restoration cost estimates and unfavorable exchange differences.

**Net debt**

Net debt of $2,731 million was $761 million lower than at the end of 2016 primarily as a result of free cash flow before asset acquisitions and divestments of $618 million and proceeds from asset sales of $145 million.

**Net tax assets/(liabilities)**

Net tax assets of $1,169 million have increased by $324 million primarily as a result of higher carry-forward tax losses recognised by the group.

**Net assets/equity**

Total equity increased by $71 million to $7,151 million at year end. The increase primarily reflects the increase in issued capital of $151 million and movements in the translation reserve of $301 million, partially offset by the net loss after tax attributable to owners of Santos of $360 million.

**Future commitments**

Due to the nature of Santos' operations, the Company has future obligations for capital expenditure, for which no amounts have been provided in the financial statements. Santos also has certain requirements to perform minimum exploration work and spend minimum amounts of money pursuant to the terms of the granting of petroleum exploration permits in order to maintain rights of tenure. The minimum exploration commitments are less than the normal level of exploration expenditures expected to be undertaken by the Company.

Santos leases LNG carriers and tug facilities under finance leases. The leases have terms of between 10 and 20 years with varying renewal options. At the reporting date, finance lease liabilities for a purpose-built LNG carrier and tug boats were recorded on the balance sheet. Santos also leases floating production, storage and offtake facilities, floating storage offloading facilities, LNG carriers and mobile offshore production units under operating leases. These leases typically run for a period of four to six years and may have an option to renew after that time. The group also leases building office space and a warehouse under operating leases. These leases are generally for a period of 10 years, with an option to renew the lease after that date.

**Oil price hedging**

The objectives of Santos' oil price hedging policy are to reduce the effect of commodity price volatility and support annual capital expenditure plans. The Company will continue to monitor commodity market conditions and will enter hedging transactions as appropriate.

As at 31 December 2017, the Company had hedged 12.5 million barrels of oil in 2018 using zero-cost three-way collars. Under the collars, where the Brent oil price is above $60.30, Santos receives $60.30. Where the Brent oil price is between $48.48 and $60.30, Santos receives the actual Brent price. Where the Brent oil price is between $40.80 and $48.48, Santos receives $48.48, and where the Brent oil price is below $40.80, Santos receives the actual Brent price plus $7.68.

# Directors' Report
continued

### Business strategy and prospects for future financial years

***Business strategy***

In December 2016, the Company announced a new strategy to transform Santos into a low-cost, reliable and high-performance business. It is a disciplined, focused strategy to drive shareholder value which sees five core, long-life natural gas assets at the heart of the Company's operations, each with significant upside potential. The remaining non-core assets have been packaged and run separately to maximise value. This will ensure a simplified, focused organisation.

The Company's strategy has three phases:

**Transform**

- Focus on five core, long-life natural gas assets: Cooper Basin, Queensland, Papua New Guinea, Northern Australia and WA Gas;
- Implement disciplined, low-cost operating model to maximise cash flows. The core asset portfolio must be free cash flow positive at oil prices less than $40 per barrel and each core asset must be free cash flow positive at less than $40 per barrel, pre-major growth spend;
- Maximise production, drive down costs and increase gas supply; and
- Implement effective governance and risk management framework to enable new operating model.

**Build**

- Identify and develop growth opportunities across the five core long-life natural gas assets;
- Develop the lowest cost onshore drill–complete–connect business;
- Establish facilities and infrastructure operations strategic capability; and
- Maximise margins through Marketing and Trading business.

**Grow**

- Execute and bring on-line growth opportunities across the core portfolio;
- Focused exploration strategy to identify new high-value targets and unlock future core assets; and
- Generate new revenue through low-carbon Energy Solutions projects.

Significant progress was made in 2017 in the **Transform** and **Build** phases of the strategy, including:

- Free cash flow breakeven point reduced to $32 per barrel. The Company generated $618 million in free cash flow before asset sales in 2017;
- Net debt reduced by 22% to $2.7 billion with gearing of 27%;
- Upstream unit production costs reduced by 4% to $8.07 per barrel of oil equivalent;
- Significant reductions in Cooper Basin and GLNG average well costs;
- Barossa two-well appraisal campaign supports a significant increase in the resource base and strengthens Barossa as the lead candidate for Darwin LNG backfill;
- Strengthened Papua New Guinea partner alignment through Santos farm-ins to prospective acreage;
- Executed agreements to evacuate uncontracted Eastern Queensland gas volumes; and
- The announcment that the Narrabri Gas Project in NSW would re-enter the Company's core asset portfolio.

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***Prospects for future financial years***

Santos enters 2018 with a clear strategy and a solid platform for growth. The business turnaround will continue as the Company focuses the organisation to support the five core assets. This singular focus will enable Santos to become a leaner, lower cost and higher performing business with significant upside opportunities across the portfolio. The Company will also begin to increase focus on the **Build** and **Grow** phases of its new strategy.

The Company is well placed to withstand any extended period of low oil prices, with $1.2 billion in cash as at 31 December 2017 and no material debt maturities until 2019. Santos will continue to focus on reducing costs and building on the significant improvements made in 2017 to operating efficiency.

Santos expects 2018 sales volumes to be in the range of 72–78 mmboe and production to be in the range of 55–60 mmboe. Capital expenditure is expected to be in the range of $825 to $875 million.

Santos remains confident in the long-term underlying demand for energy on the back of Asian economic growth, the rising global population and rapid urbanisation in developing economies. Large cuts in capital expenditure by oil and gas companies are expected to lead to falling production and a recalibration of oil prices to higher levels. However, the Company will continue to focus on resetting the cost base in order to operate profitably and sustainably in periods of low oil prices, and is confident that the measures taken will drive returns for shareholders.

**Material business risks**

The achievement of Santos' purpose and vision, business strategy, production growth outlook and future financial performance is subject to various risks including the material business risks summarised below. Santos undertakes steps to identify, assess and manage these risks and operates under a Board-approved enterprise-wide Risk Management Policy.

This summary refers to significant risks identified at a whole of entity level relevant to Santos. It is not an exhaustive list of all risks that may affect the Company, nor have they been listed in any particular order of importance.

***Strategic risks***

*Volatility in oil and gas prices*

Santos' business relies primarily on the production and sale of oil and gas products (including LNG) to a variety of buyers under a range of short-term and long-term contracts. The majority of oil and gas produced (or to be produced) in Santos' portfolio has been sold under sales contracts where the sale price is linked to the global price of oil. Lower global oil prices will therefore reduce Santos' revenues and the profitability of its operations.

Global oil prices are affected by numerous factors beyond the Company's control and have fluctuated widely historically. Santos' three-tiered strategy, operating model and Hedging Policy introduced in 2016 directly address oil price risk with a clear focus on cash flow management, operational and cost efficiencies, production growth opportunities and debt reduction, to build resilience to oil price fluctuations.

*Oil and gas reserves development*

Calculations of recoverable oil and gas reserves and resources contain significant uncertainties, which are inherent in the reservoir geology, seismic and well data available and other factors such as project development and operating costs, together with commodity prices. A failure to successfully develop existing reserves may impact Santos' ability to fully supply LNG, gas or oil under customer contracts.

Santos has adopted a reserves management process that is consistent with the Society of Petroleum Engineers' Petroleum Resource Management System. The Company's reserves and resources estimations are subject to independent audits and evaluations on a rolling basis.

Santos applies an integrated management system across all aspects of business performance, including reserves estimation and delivery. Progress against key reserves metrics is routinely reviewed by senior management and the Board and reserves estimates are published annually.

*Exploration and reserves replacement*

Santos' future long-term prospects are also directly related to the success of efforts to replace existing oil and gas reserves as they are depleted through production, from either exploration or acquisition. Exploration is a high-risk endeavour subject to geological and technological uncertainties and the failure to replace utilised reserves is a risk inherent in the oil and gas exploration and production industry.

Santos employs an established exploration prospect evaluation methodology and risking process, consistent with industry standards, to manage the risks associated with exploration. Business Development processes identify, review and progress opportunities to build reserves through acquisition in support of the Company's strategy and objectives.

# Directors' Report

*Demand and market*

The demand for oil, gas, LNG and other products Santos markets may be adversely affected by a range of external factors including competition from alternative sources of oil, gas and LNG, competition from other sources of energy supply or changes in consumer behaviour or government policy.

Santos' business strategy development and review processes consider independent oil, gas and LNG market forecasts, and other relevant macro-economic factors, to assess the Santos portfolio under a range of scenarios, to deliver robust plans in support of the Company's purpose and vision.

*Project development*

Santos undertakes investment in a variety of oil and gas projects to extract, process and supply oil and gas to a variety of customers, including long-term high-volume contracts to supply feedstock gas to the GLNG project. Such projects may be delayed or be unsuccessful for many reasons, including unanticipated economic, financial, operational, engineering, technical, environmental, contractual, regulatory, community or political events. Delays, changes in scope, cost increases or poor performance outcomes pose risks that may impact the Company's financial performance.

Santos has comprehensive project and risk management and reporting systems in place. Progress and performance of material projects is regularly reviewed by senior management and the Board.

*Joint venture arrangements*

Much of Santos' business is carried out through joint ventures. The use of joint ventures is common in the oil and gas exploration and production industry and serves to mitigate the risk and associated cost of exploration, production and operational failure. However, failure of agreement or alignment with joint venture partners, or the failure of third-party joint venture operators, could have a material effect on Santos' business. The failure of joint venture partners to meet their commitments and share costs and liabilities can result in increased costs to Santos.

Santos has clear standards and requirements related to the establishment and management of joint venture arrangements and activities. The Company works closely with its joint venture partners to reduce the risk of misalignment in joint venture activities.

***Operational risks***

*Technical and engineering*

Santos is exposed to risks in relation to its ongoing oil and gas exploration and production activities, such as failure of drilling and completions equipment, pipeline and facilities integrity failures, major processing or transportation incidents, release of hydrocarbons or other substances, security incidents and other well control and process safety risks, which may have an adverse effect on Santos' profitability and results of operations.

Santos applies an integrated management system across all operational activities to manage and monitor operations performance and material risk controls. The management system includes all relevant technical, operational, asset reliability and integrity standards and incident management standards and competency requirements designed to ensure the Company meets regulatory and industry standards in all operations.

*Access and licence to operate*

Santos has interests in areas which may be subject to claims by communities and landowners, who may have concerns over the social or environmental impacts of oil and gas operations or the distribution of oil and gas royalties and access to mining and petroleum related benefits. This has the potential to impact on land access or result in community unrest and activism targeted towards project infrastructure impacting Santos' reputation.

A number of Santos' interests are also located within areas which are the subject of one or more claims or applications for native title determination. In Australia, compliance with the requirements of the *Native Title Act 1993* (Cth) can delay the grant of mineral and petroleum tenements and consequently impact generally the timing of exploration, development and production operations.

Santos and its operating joint venture partners work closely with relevant governments, communities, landowners and indigenous groups to ensure all concerns are fairly addressed and managed, and Santos' operations benefit from their support. In addition, Santos and its operating joint venture partners develop and employ security and risk management plans, and are committed to conducting operations in a way that protects the security of its personnel, facilities and operations.

Santos has a long history of safe and sustainable operations undertaken working with communities and landholders across the country. The Company has hundreds of land access agreements in place and a team of experienced community and land access representatives who work with Aboriginal stakeholders, landholders and communities to ensure that issues are understood and addressed appropriately.

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*Cyber security*

Cyber security risks, including threats to Santos' information and operational systems from computer viruses, unauthorised access, cyber-attack and other similar disruptions, have evolved rapidly and can impact all sectors of the economy, including the energy industry. The increasing technological advances in operations require monitoring and protection to ensure cyber security threats are appropriately prevented and managed. Cyber security risks may lead to a breach of privacy, fraud, disruption of critical business processes or theft of commercially sensitive information. Such events could lead to operational disruptions and have an adverse impact on Santos' profitability and financial position.

Focused cyber security risk management is incorporated into Santos' risk management and assurance processes and practices across the Company's business and operational information management systems.

*Workforce*

Santos' future success is significantly influenced by the expertise and continued service of certain key executives and technical personnel. An inability to attract or retain such personnel could adversely affect the results of Santos' operations and financial condition.

Santos has a suite of employment arrangements designed to secure and retain the services of such personnel. Key workforce metrics and succession plans are routinely reviewed by senior management and the Board.

***Environmental, safety and sustainability risks***

*Health, safety and environmental*

The size, nature and complexity of Santos' operations pose risks in relation to the health and safety of the employees and contractors involved, including risks associated with travel to and from operations.

A range of environmental risks exist within oil and gas exploration and production activities. Accidents, environmental incidents and real or perceived threats to the environment or the amenity of local communities could result in a loss of Santos' licence to operate leading to delays, disruption or the shut-down of exploration and production activities.

Santos has a comprehensive approach to management of health, safety and environmental risks. The Company's management system integrates technical and engineering requirements with personal health and safety requirements to comprehensively manage safety risks within company operations.

*Climate change*

Santos is likely to be subject to increasing regulations and costs associated with climate change and management of carbon emissions.

Strategic, regulatory and operational risks and opportunities associated with climate change are incorporated into Company policy, strategy and risk management processes and practices. The Company actively monitors current and potential areas of climate change risk and takes actions to prevent and/or mitigate any impacts on its objectives and activities. Reduction of waste and emissions is an integral part of delivery of cost efficiencies and forms part of the Company's routine operations.

***Financial risks***

Santos' overall financial risk management strategy seeks to ensure that Santos is able to fund its corporate objectives and meet its obligations to stakeholders. Financial risk management is carried out by a central treasury department which operates under a Board-approved framework and policies. The framework and principles for overall financial risk management address specific financial risks, such as foreign exchange risk, interest rate risk and credit risk, approved derivative and non-derivative financial instruments, and liquidity management.

Santos has an oil price hedging policy with the objective of reducing the effect of commodity price volatility and support annual capital expenditure plans. Santos continues to monitor commodity market conditions and will enter hedging transactions as appropriate.

*Foreign currency*

Santos' foreign exchange risk arises from commercial transactions and valuations of assets and liabilities that are denominated in a currency that is not the entity's functional currency.

Santos is exposed to foreign currency risk principally through the sale of products denominated in currencies other than the functional currency, borrowings denominated in currencies other than US$ and capital and operating expenditure incurred in currencies other than US$, principally A$. Santos also has certain investments in domestic and foreign operations whose net assets are exposed to foreign currency translation risk.

*Credit*

Credit risk for Santos represents a potential financial loss if counterparties fail to perform as contracted, and arises from investments in cash and cash equivalents, derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to customers including outstanding receivables and committed transactions.

# Directors' Report

*Access to capital and liquidity*

Santos' business and, in particular, the development of large-scale projects, relies on access to debt and equity financing. The ability to secure financing, or financing on acceptable terms, may be adversely affected by volatility in the financial markets, globally or affecting a particular geographic region, industry or economic sector, or by a downgrade in its credit rating.

***Contract and counterparty risks***

As part of its ongoing commercial activities, Santos is party to a number of material contracts including finance agreements, infrastructure access agreements, agreements for the sale and purchase of hydrocarbon, transportation agreements, joint venture agreements, and engineering, procurement and construction (EPC) contracts. Santos also enters into sale and purchase contracts with various third parties for the sale and purchase of natural gas, LNG and other products.

The economic effects of these contracts over their term may be impacted by fluctuations in commodity prices, price reviews, operational performance and other market conditions. Failure to perform material obligations under these contracts by Santos and/or the applicable counterparties, or to secure any extensions or amendments to these contracts, may result in a material impact on Santos' operations and financial results.

Santos tracks key contractual obligations and monitors performance across its material contracts.

***Political and legal risks***

*Political, legal and regulatory*

Santos' business is subject to various laws and regulations in each of the countries in which it operates that relate to the development, production, marketing, pricing, transportation and storage of its products. A change in the laws which apply to the Company's business, or the way in which it is regulated, could have a material adverse effect on Santos' business, results of operations and financial condition. For example, a change in taxation laws, environmental laws or land access laws could have a material effect on the Company.

Santos' domestic gas business and GLNG project, including its ability to purchase gas, develop future growth projects and meet supply commitments, may also be adversely impacted by any governmental intervention, including limitations on LNG export volumes and/ or the redirection of gas from export to domestic markets. Any such intervention may also have broader implications for the future of the gas industry in Australia.

Santos continually monitors legislative and regulatory risk and engages appropriately with regulators and governments to manage regulatory risks.

*Litigation and dispute*

The nature of Santos' business means that it is likely to be involved in litigation or regulatory actions arising from a wide range of matters. Santos may also be involved in investigations, inquiries or disputes, debt recoveries, commercial and contractual disputes, native title claims, land tenure and access disputes, environmental claims or occupational health and safety claims. Any of these claims or actions could result in delays, increase costs or otherwise adversely impact Santos' assets and operations, and adversely impact Santos' financial performance and future financial prospects.

Santos has an experienced legal team that monitors and manages potential and actual claims, actions and disputes.

**Material prejudice**

As permitted by sections 299(3) and 299A(3) of the *Corporations Act 2001* (Cth), Santos has omitted some information from the above Operating and Financial Review in relation to the Company's business strategy, future prospects and likely developments in operations and the expected results of those operations in future financial years on the basis that such information, if disclosed, would be likely to result in unreasonable prejudice (for example, because the information is premature, commercially sensitive, confidential or could give a third party a commercial advantage). The omitted information typically relates to internal budgets, forecasts and estimates, details of the business strategy, and contractual pricing.

**Forward-looking statements**

This report contains forward-looking statements, including statements of current intention, opinion and predictions regarding the Company's present and future operations, possible future events and future financial prospects. While these statements reflect expectations at the date of this report, they are, by their nature, not certain and are susceptible to change. Santos makes no representation, assurance or guarantee as to the accuracy or likelihood of fulfilling of any such forward-looking statements (whether express or implied) and, except as required by applicable law or the ASX Listing Rules, disclaims any obligation or undertaking to publicly update such forward-looking statements.

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## SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

The Material Business Risks section (pages 25 to 28) refers to risks which, if materialised, may have a significant effect on the state of affairs of the Company.

## DIVIDENDS

On 20 February 2018, the Directors resolved not to pay a final dividend.

## ENVIRONMENTAL REGULATION

The consolidated entity's Australian operations are subject to various environmental regulations under Commonwealth, State and Territory legislation. Applicable legislation and requisite environmental licences are specified in the consolidated entity's EHS Compliance Database, which forms part of the consolidated entity's overall Environmental Management System. Environmental compliance performance is monitored on a regular basis and in various forms, including audits conducted by regulatory authorities and by the Company, either through internal or external resources.

On 15 February 2017, Santos received a penalty infringement notice and $12,190 fine from the Queensland Department of Environment and Heritage Protection for non-compliance with a Soils Management Plan. The consolidated entity undertook corrective measures in respect of the infringements to prevent re-occurrences.

This was the only penalty infringement notice and fine the consolidated entity received.

## POST BALANCE DATE EVENTS

Except as mentioned below or elsewhere in this report, in the opinion of the Directors there has not arisen, in the interval between the end of the financial year and the date of this report, any matter or circumstance that has significantly affected or may significantly affect the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in future financial years.

On 20 February 2018, the Directors of Santos Limited resolved not to pay a final dividend in respect of the 2017 financial year.

## SHARES UNDER OPTION AND UNVESTED SHARE ACQUISITION RIGHTS (SARs)

### Options

Unissued ordinary shares of Santos Limited under option at the date of this report are as follows:

| Date options granted | Expiry date | Issue price of shares[1] | Number of options |
|---|---|---|---|
| 3 May 2008 | 2 May 2018 | $15.39 | 447,540 |
| 3 May 2008 | 2 May 2018 | $15.39 | 227,951 |
| 28 July 2008 | 27 July 2018 | $17.36 | 81,948 |
| 2 March 2009 | 2 March 2019 | $14.81 | 50,549 |
| | | | **807,988** |

1 This is the exercise price payable by the option holder.

Options do not confer an entitlement to participate in a bonus or rights issue, prior to the exercise of the option.

# Directors' Report

### Unvested SARs

Unissued ordinary shares of Santos Limited under unvested SARs at the date of this report are as follows:

| Date SARs granted | Number of shares under unvested SARs |
|---|---|
| 6 March 2015 | 1,913,744 |
| 28 July 2015 | 587,787 |
| 10 February 2016 | 166,911 |
| 1 May 2016 | 42,585 |
| 14 June 2016 | 4,154,730 |
| 31 August 2016 | 628,141 |
| 21 March 2017 | 4,226,683 |
| 29 September 2017 | 549,024 |
| | 12,269,605 |

No amount is payable on the vesting of SARs. SARs do not confer an entitlement to participate in a bonus or rights issue, prior to the vesting of the SAR. Further details regarding the SARs (including when they will lapse) are contained in the Remuneration Report commencing on page 34 of this report and in note 7.2 to the financial report.

## SHARES ISSUED ON THE EXERCISE OF OPTIONS AND ON THE VESTING OF SARS

### Options

No options were exercised during the year ended 31 December 2017 or up to the date of this report.

### Vested SARs

The following ordinary shares of Santos Limited were issued during the year ended 31 December 2017 on the vesting of SARs granted under the Santos Employee Equity Incentive Plan (SEEIP) (formerly known as the Santos Employee Share Purchase Plan (SESAP)) and ShareMatch Plan (ShareMatch). No amount is payable on the vesting of SARs and accordingly no amounts are unpaid on any of the shares.

| Date SARs granted | Number of shares issued |
|---|---|
| 1 July 2014 | 300,870 |
| 28 July 2015 | 45,130 |
| 1 February 2016 | 166,911 |
| 31 August 2016 | 38,039 |
| 1 December 2016 | 23,777 |
| 29 September 2017 | 271 |
| | 574,998 |

Since 31 December 2017, 4,197 ordinary shares of Santos Limited have been issued on the vesting of SARs granted under the SEEIP and ShareMatch.

## DIRECTORS' AND SENIOR EXECUTIVES' REMUNERATION

Details of the Company's remuneration policies and the nature and amount of the remuneration of the Directors and senior management (including shares, options and SARs granted during the financial year) are set out in the Remuneration Report commencing on page 34 of this report and in notes 7.2 and 7.3 to the financial report.

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# 2017 Remuneration in Brief

This section is in addition to the Remuneration Report on pages 34 to 53. This section therefore does not form part of the audited Remuneration Report. It provides additional information in relation to the amount of remuneration paid to the Company's Managing Director and Chief Executive Officer (CEO), Kevin Gallagher, and Senior Executives during 2017. The Company has chosen to do this so that investors have the benefit of this information in addition to the Remuneration Report, which has been prepared in accordance with statutory requirements and Accounting Standards.

## DELIVERING STRONG PERFORMANCE

Since commencing its turnaround to deliver a low-cost, reliable and high-performance business, Santos has taken tough and decisive action to restructure the business, remove substantial costs, rebuild cash flow and strengthen the balance sheet.

The Transform Build Grow strategy is now delivering ahead of expectations. Focused on five core, long-life natural gas assets: Cooper Basin, Queensland (including GLNG), Papua New Guinea (PNG), Northern Australia and West Australian Gas, our simplified portfolio is now positioned to provide stable base production for the next decade and positive free cash flow at an oil price of less than or equal to US$40 per barrel (bbl), pre-major growth opportunities.

The Santos share price increased by 36% in 2017 to A$5.45 as at 31 December 2017 and market capitalisation increased by 39% over the same period.

In 2017, the Transform phase of the Company's strategy delivered:

- free cash flow breakeven oil price of US$32/bbl, down 12% on 2016;
- upstream unit production costs of US$8.07 per barrel of oil equivalent (boe), down 5%; and
- net debt of US$2.7 billion, down 22%.

In 2017 under the Build phase, Santos continued to strengthen its core asset positions in PNG, Northern Australia and Queensland, and added the Narrabri project in NSW to the core portfolio.

In the Grow phase, a two-well appraisal campaign in the Barossa field offshore Northern Australia significantly increased the resource size and strengthened the Company's position as the lead candidate for Darwin LNG backfill. In Papua New Guinea, additional debottlenecking opportunities were identified at PNG LNG to further increase production. Across GLNG and the Cooper Basin, significant cost savings and efficiencies have led to increased drilling activity.

The Santos turnaround strategy is on track and delivering strong results. In light of this the Board has approved a Company Scorecard result of 88.5%, which will be used to determine Short-Term Incentive (STI) awards.

## ALIGNING REMUNERATION AND COMPANY PERFORMANCE

Despite strong operational performance during 2017, no Long-Term Incentive (LTI) awards vested because the Company did not achieve the required relative Total Shareholder Return (TSR) performance over the four years since 2014 LTI was awarded. This is the seventh consecutive year that relative TSR-tested LTI awards have not vested, reflecting the clear link between shareholder returns and Senior Executive remuneration.

In 2017 the Company continued to align Executive remuneration with the interests of shareholders by:

- emphasising the importance of financial and operational performance in the Company Scorecard, at an overall 60% weighting of the total, including production, debt reduction, profit and Return on Average Capital Employed (ROACE) and Free Cash Flow Breakeven Point (FCFBP) measures;
- requiring that STI cash payments were to be fully funded by free cash flow (FCF), such that if Santos did not reach its gateway of achieving positive FCF in excess of the total net Santos STI cash cost, all of the CEO and Senior Executives' STI would be awarded as two-year deferred equity rather than cash (noting that if FCF targets are met, 30% of the CEO and Senior Executives' STI awards will continue to be deferred into equity for two years);
- focusing the CEO and Senior Executives on ongoing shareholder returns and operational efficiency through the LTI plan's relative TSR, FCFBP and ROACE performance hurdles; and
- maintaining the same fees for non-executive Directors in 2017 that have been unchanged since October 2013.

## REPORTING CURRENCY

The majority of the Remuneration Report is disclosed in US$ (unless otherwise indicated) with all remuneration components having been converted from A$ to US$ using an average rate of $0.7667 for 2017 and $0.7451 for 2016.

The Actually Realised Remuneration table in this section at page 33 is disclosed in A$.

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# 2017 Remuneration in Brief
continued

## ACTUALLY REALISED REMUNERATION

The Actually Realised Remuneration Table shows remuneration "actually realised" by the CEO and Senior Executives in relation to 2017 namely:

- cash payments on account of Total Fixed Remuneration (TFR);
- cash STI awards earned in respect of 2017 performance;
- deferred STI awards in respect of prior performance years which vested in 2017; and
- Share Acquisition Rights (SARs) granted as part of the LTI program, only if they vest, valued on the basis of their closing price on the date of vesting.

These amounts differ from the amounts reported in the Remuneration Report which are prepared in accordance with the Corporations Act and Accounting Standards. This is because the Accounting Standards require a value to be placed on "share based payments" at the time of grant, and for that "accounting value" to be reported as remuneration, even though the CEO and Senior Executives may ultimately not realise any actual value from the "share based payments" (e.g. because the performance conditions are not satisfied, as was the case for the 2014 four-year LTI award tested at the end of 2017).

Termination payments, leave entitlements and cashing out of leave entitlements, where allowable under legislation, are not included in the table below. The total remuneration amounts determined in accordance with the requirements of the *Corporations Act 2001* (Cth) and Accounting Standards are set out in Table 5 "2016 and 2017 Senior Executive remuneration details" (see page 43).

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**Actually realised remuneration (unaudited and non-IFRS)**

| | Year | TFR[1] | Cash STI[2] | 2015 deferred STI that vested in 2017[3] | Ordinary shares[4] | LTI[5] | Other vested grants[6] | Other[7] | Total |
|---|---|---|---|---|---|---|---|---|---|
| | | A$ | A$ | A$ | A$ | A$ | A$ | A$ | A$ |
| **Current** | | | | | | | | | |
| K Gallagher CEO | 2017 | 1,800,000[8] | 1,159,200 | – | – | – | 667,644[9] | 5,341 | 3,632,185 |
| | 2016 | 1,650,000 | 712,600 | – | 285,000 | – | – | 9,804[10] | 2,657,404 |
| P Byrne[11] Executive Vice President (EVP) Marketing, Trading and Commercial | 2017 | 271,370 | 129,400 | – | – | – | – | 9,804[12] | 410,574 |
| A Neilson[13] Chief Financial Officer (CFO) | 2017 | 800,000 | 423,600 | – | – | – | 122,214[14] | 2,626 | 1,348,440 |
| V Santostefano[15] Chief Operations Officer, Operations Services | 2017 | 850,000 | 379,300 | – | – | – | – | 2,684 | 1,231,984 |
| | 2016 | 662,195 | 243,100 | – | 97,200 | – | – | 9,804[16] | 1,012,299 |
| B Woods[17] | 2017 | 695,000 | 355,600 | 297,330 | – | – | – | 6,408[18] | 1,354,338 |
| EVP Onshore Upstream | 2016 | 660,000 | 202,600 | – | 81,000 | – | – | 3,248[19] | 946,848 |
| **Former** | | | | | | | | | |
| J Anderson[20] EVP Marketing and Trading | 2017 | 750,000 | 366,300[21] | 408,101 | – | – | – | – | 1,524,401 |
| | 2016 | 740,504 | 275,700 | 54,817 | 110,300 | – | – | 15,000 | 1,196,321 |

1 TFR comprises base salary and superannuation. The amount shown here is the actually received TFR, i.e. pro-rated amount is shown for any Executive who commenced during the year.

2 This relates to the 70% of the STI award for 2017 performance for continuing Executives which will be paid in cash. The remaining 30% will be awarded as equity restricted for two-years. The 2017 Company Scorecard outcome is presented at Table 1 "2017 STI scorecard performance" on page 36. 2016 and 2017 Senior Executive remuneration details, including deferred STI accounting valuations, can be found on page 43.

3 This relates to the deferred restricted shares from the 2015 STI award that vested on 31 December 2017. The amount shown is based on the closing share price of A$5.45 on the vesting date of 31 December 2017.

4 This relates to the 2016 STI in which Senior Executives received 20% of the STI award as ordinary shares. The amount reflected is based on the closing share price of A$4.02 on 31 December 2016, being the end of the applicable performance year.

5 No LTI vested in 2017. For the value of share based payments calculated in accordance with the Accounting Standards, see Table 5 "2016 and 2017 Senior Executive remuneration" on page 43.

6 This relates to any other grants that have vested, such as the sign-on grants received by the CEO and CFO that have now vested.

7 "Other" comprises ad hoc payments treated as remuneration, such as assignment and mobilisation allowances and other non-monetary benefits.

8 Mr Gallagher received no TFR increase in 2017. The 2017 figures represented for the CEO are for the full 12 months of 2017, whereas the 2016 figures only include the 11 months following his February 2016 commencement.

9 This figure represents the first tranche of the CEO's sign-on grant (166,911 SARs) that vested on 31 January 2017. The amount reflected is based on a closing share price of A$4.00 on 31 January 2017.

10 Mr Gallagher received a relocation allowance in February 2016.

11 Mr Byrne became a KMP on 14 August 2017 when he commenced as EVP Marketing and Trading. His part-year remuneration is shown.

12 Mr Byrne received a relocation allowance on commencement of his employment.

13 Mr Neilson became a KMP on 1 January 2017 when he commenced as CFO.

14 This relates to Mr Neilson's 2016 sign-on grant (23,777 SARs) that vested on 1 December 2017. The amount is based on the closing share price of A$5.14 on 1 December 2017.

15 Mr Santostefano received no TFR increase in 2017. The 2017 figures for Mr Santostefano are for the full 12 months of 2017, whereas the 2016 figures only relate to the period following his 21 March 2016 commencement.

16 In 2016 Mr Santostefano received a relocation allowance.

17 Mr Woods received a TFR increase on 1 July 2017 of 7.5% (TFR of $720,000) reflecting his increased responsibilities and promotion to EVP Onshore Upstream.

18 Includes 353 SARs that vested from when Mr Woods previously participated in the Company's employee share plan prior to becoming a KMP. The value of the 353 SARs reflects a share price of A$3.02 on 3 July 2017 on its vesting date. Also included are any non-monetary benefits.

19 Mr Woods previously participated in the Company's employee share plan prior to becoming a KMP and 808 of these shares vested in 2016.

20 Mr Anderson was a KMP from 1 January 2017 to 13 August 2017 while in the role of EVP Marketing and Trading. He ceased to be a KMP on 14 August 2017. Mr Anderson continued to provide transitionary support after ceasing to be a KMP and his total remuneration earned for 2017 has been provided for comparison purposes.

21 Given Mr Anderson will no longer be working for the Company, his pro-rated 2017 STI will be delivered wholly in cash in accordance with his contractual agreement. The figures for Mr Anderson do not include his termination payments, details of which are set out in Table 5 "2016 and 2017 Senior Executive remuneration details".

# Remuneration Report

The Directors of Santos Limited (referred to as the Company or Santos in this Report) present this Remuneration Report for the consolidated entity for the year ended 31 December 2017. The information provided in this Report has been audited as required by section 308(3C) of the *Corporations Act 2001* (Cth) (Corporations Act) and forms part of the Directors' Report.

The Remuneration Report outlines the Company's key remuneration activities in 2017 and remuneration information pertaining to the Company's Directors, Managing Director and Chief Executive Officer (CEO), Kevin Gallagher, and Senior Executives who are the key management personnel (KMP) of the consolidated entity for the purposes of the Corporations Act and Accounting Standards. These are the personnel who have authority and responsibility for planning, directing and controlling the activities of the Company's major financial, commercial and operating divisions.

## REMUNERATION APPROACH

**Remuneration policy objective**

| Attracting and retaining talented and qualified executives | Focusing executives to strive for superior performance | Aligning executive and shareholder interests |
|---|---|---|
| ↓ | ↓ | ↓ |

**Implemented through the company's remuneration framework**

| | | |
|---|---|---|
| Remuneration levels are market-aligned against similar roles in comparable companies.<br><br>The Company compares remuneration levels for similar roles in a benchmarking group.<br><br>This group comprises peer companies across broader based industries of the ASX100 and also the oil and gas sector (and related resources sectors). | A significant component of remuneration is "at risk" under the Short-Term Incentive plan. The value to the executive is dependent on meeting challenging targets.<br><br>Short-Term incentive outcomes are based on performance measures that include production, free cash flow, profit, safety, environment, reserves development, value creation and leadership measures. | Long-term incentives are delivered in the form of Share Acquisition Rights (SARs).<br><br>Vesting of performance-based Long-Term incentives is contingent on achieving performance hurdles.<br><br>Long-Term incentives are "at risk" and executives cannot hedge equity instruments that are unvested or subject to restrictions. These incentives are also subject to clawback. |

## REMUNERATION GOVERNANCE

### People and Remuneration Committee

The People and Remuneration Committee (Committee) oversees and formulates recommendations to the Board on the remuneration policies and practices of the Company generally, including the remuneration of non-executive Directors, the CEO and Senior Executives.

### External advisors and remuneration advice

The Board has adopted a protocol for engaging and seeking advice from remuneration consultants. In 2017 market benchmarking was undertaken to provide information on KMP remuneration however no remuneration recommendations were provided by remuneration consultants.

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## REMUNERATION FRAMEWORK

### Remuneration benchmarking

Total Fixed Remuneration (TFR), Short-Term Incentive (STI) and Long-Term Incentive (LTI) levels are set by reference to market data to ensure that the Company offers competitive remuneration that enables it to attract and retain the skills it needs to deliver the Company's short-term and long-term objectives.

### Total Fixed Remuneration

TFR comprises base pay and superannuation and is reviewed annually and formally benchmarked against comparable peer companies. It is set in consideration of an individual's role and responsibilities and also the Executive's experience and competencies.

### Short-Term Incentive

The Company provides an annual STI program to align Executive interests with the delivery of its short-term operational and financial targets for the year. These are chosen to drive outcomes and behaviours that support the safe operation and delivery of the business and lead to long-term growth in shareholder value. These are reviewed annually by the Board. Table 1 on page 36 outlines the short-term objectives used in 2017 to measure performance for STI purposes and the reasons why these objectives were chosen.

In 2017 the Company maintained its focus on delivering strong financial returns with the financial based metrics remaining at 60% weighting. The free cash flow (FCF) gateway for the CEO and Senior Executives' cash STI award also remained whereby if the FCF gateway is met, 30% of the STI award for the CEO and Senior Executives are deferred into shares or SARs. If the gateway is not met, 100% of the CEO and Senior Executives' STI awards will be delivered as shares or SARs that vest at the end of a two-year deferral period. If a Senior Executive resigns during the period, they will ordinarily forfeit their deferred shares or SARs.

Further details in relation to the STI program are provided on page 50.

### Long-Term Incentive

In order to align the interests of Executives with the creation of long-term shareholder value, the Company awards its LTI as SARs. The SARs are granted at no cost and only vest if the Company meets a number of performance hurdles.

Vesting of the 2017 LTI grants is based on the following performance targets:

- 25% relative Total Shareholder Return (TSR) measured against companies in the ASX100;
- 25% relative Total Shareholder Return (TSR) measured against companies in the S&P Global 1200 Energy Index (GEI);
- 25% Free Cash Flow Breakeven Point; and
- 25% Return on Average Capital Employed.

Further details are provided in relation to the LTI program on page 51.

### Clawback

The share plan rules give the Company the discretion to lapse or forfeit unvested deferred shares or SARs awarded under the STI or LTI programs as well as claw back any vested shares or cash paid in certain circumstances. These circumstances include dishonest or fraudulent conduct, breach of material obligations, miscalculation or error, a material misstatement or omission in the accounts of a group company or events which require re-statement of the group's financial accounts in circumstances where an LTI or deferred STI award would not otherwise have been granted or would not have vested. This is in addition to any rights the Company has under the plan rules and general legal principles to seek to recover payments made in error.

# Remuneration Report
continued

### Link between performance and remuneration

***2017 STI scorecard performance***

The Company's performance against the 2017 Company Scorecard as assessed by the Board resulted in a score of 88.5%. The table below summarises the short-term objectives in the Scorecard, their rationale and the Company's performance against them.

***Table 1: 2017 Company scorecard performance***

| | Measure | Rationale | Performance | Score |
|---|---|---|---|---|
| Operational Integrity (20%) | ***Personnel safety***<br>Measured by the rolling average number of Lost-Time Injuries per million hours worked over a three-year period (2015 to 2017). | The Company is committed to providing a workplace without injury or illness and managing the impact of our operations on the environment. | Lost time injury frequency rate (LTIFR) (three-year rolling average) of 0.38. Threshold performance level was not achieved. | 13.75% |
| | ***Process safety***<br>Measured by the number of Tier 1 loss of containment of hydrocarbon incidents. | The integrated targets for personnel safety, process safety, and the environment, represent the Company's holistic approach to safety management which is aimed at reducing the number of injuries to employees and contractors, the likelihood of low-frequency but high-impact incidents such as fires and explosions, and the occurrence of significant environmental incidents. | Tier 1 loss of containment of hydrocarbon incidents achieved better than target performance. | |
| | ***Environmental incidents***<br>Measured by the number of environmental incidents of moderate or greater consequence. | | There were no environmental incidents of moderate or greater consequence, achieving better than target performance. | |
| | ***Santos Management System (SMS)***<br>Reflect SMS project delivery for new policies, management standards and supporting procedures and tools. | The SMS forms the Company's key control framework, setting out the mandatory performance requirements across the Company's primary activities in a consolidated framework for effective outcomes, operations and risk management. | The SMS was developed and substantially rolled out in 2017, with all management standards and most supporting procedures and tools launched, achieving target outcome. | |

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| | Measure | Rationale | Performance | Score |
|---|---|---|---|---|
| Financial & Operating Performance (60%) | ***Production*** | Production is critical to the Company's profitability, and is a key measure of the Company's overall performance, underpinning annual earnings and cash flow. | Production of 59.5 mmboe met stretch performance. | 57.65% |
| | ***Adjusted net debt*** | Adjusted net debt is included to prioritise debt reduction and reflect Santos' target to reduce net debt. Adjusted net debt reflects the focus on reducing Company debt, following start-up of major projects and resultant high gearing level, and against a backdrop of a low oil price environment. | Adjusted net debt was substantially reduced to US$2.73 billion which met stretch performance. | |
| | ***Free cash flow breakeven point (FCFBP)*** | Included to ensure continual reduction in the company's cost base. | Free cash flow breakeven point was further improved in 2017 down to US$31.90 per barrel. Stretch performance was achieved. | |
| | ***Return on average capital employed (ROACE)*** | This measure is included to focus on earning improvement and drive improved returns for the business. | ROACE of 6.9% resulted in target performance being achieved. | |
| | ***Underlying net profit after tax (NPAT)*** | Included to deliver earning improvement for the business. | Stretch performance achieved through strong sales revenue and cost reduction. Final underlying NPAT at US$336m achieving stretch performance. | |
| Value Creation (15%) | ***Reserves replacement***<br>The volume of proven and probable (2P) reserves added by the Company organically compared to the volume of reserves used in the current year's production. | Reserves replacement reflects the Company's ability to replace the reserves it uses in the current year's production to ensure the longer-term sustainability of the Company. | The 2P reserves replacement growth result met threshold. | 13.37% |
| | ***Discover / acquire new 2C resource (% of production)***<br>The volume of 2C contingent resources added by the Company through discovery, appraisal and acquisition compared to the volume of reserves used in the current year's production. | Resource replacement reflects the Company's ability to build a portfolio of future development projects through new exploration, appraisal and acquisition opportunities. | The new 2C contingent resources replacement growth stretch target was achieved. | |
| | ***Core asset portfolio build*** | This metric is focused on increasing the value of the Company's core asset portfolio through the delivery of commercial, operational and efficiency improvements. | Significant progress has been made in driving down Cooper Basin and GLNG cost structure and unlocking value from new and existing commercial arrangements. The Company achieved a score above target. | |
| Leadership and Culture (5%) | ***Leadership and culture***<br>To equip the organisation to achieve the Company Strategy and Values. | Focus on developing the capability of our employees. | There was a focus on ensuring all employees had development plans to drive strong performance outcomes in 2017. The Company achieved threshold for this measure. | 3.75% |
| | | Employee survey introduced to establish a baseline for culture improvement, engagement and productivity. | An employee survey was completed by Quarter 3 2017 with the analysis used to develop plans to address critical gaps within the Company. The Company achieved stretch performance for this measure. | |
| | | | **Total** | **88.5%** |

# Remuneration Report
continued

## LTI PERFORMANCE

The Company's Total Shareholder Return for the period 1 January 2014 to 31 December 2017 ranked below the 51st percentile in both the comparator groups comprising the companies in the ASX 100 and the S&P GEI. As a result, none of the SARs granted to the recipients in 2014 as part of the four-year grant vested. This reflects the alignment of the Company's LTI program with the interests and long-term returns of shareholders.

Details about how performance targets are set and tested for the purposes of STI and LTI awards are set out on pages 50 and 52.

## FINANCIAL PERFORMANCE

Table 2 sets out the Company's performance over the past five years in respect of several key financial and non-financial indicators and the STI and LTI awards during this period.

***Table 2: Key metrics of company performance 2013–2017***

| | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|
| Injury frequency | | | | | |
| total recordable case frequency rate | 3.8 | 3.5 | 2.8 | 2.2 | 3.5 |
| lost time injury frequency rate (three-year[1] rolling average) | 0.8 | 0.7 | 0.5 | 0.4 | 0.38 |
| Production (mmboe) | 51.0 | 54.1 | 57.7 | 61.6 | 59.5 |
| Reserve replacement rate – 2P organic (%) | 3 | 0 | 0 | 19 | 62 |
| Net profit/(loss) after tax[2] ($m) | US$499 | US$(630) | US$(1,953) | US$(1,047) | US$(360) |
| Dividends per ordinary share (cents) A$ | 30 | 35 | 20 | 0 | 0 |
| Share price – closing price on first trading day of year | A$11.11 | A$14.63 | A$8.25 | A$3.68 | A$4.02[3] |
| LTI performance (% vesting) – shown against final year of performance period | 0% | 0% | 0% | 0% | 0% |
| STI score (% of maximum) | 60% | 58%[4] | 67% | 86.5% | 88.5% |

1 From the 2015 performance year onwards the figures reflect a rolling three-year average.

2 2013 – 2015 NPAT figures have been translated from A$ to US$ at an applicable exchange rate for the year for comparison purposes following the change in the Company's presentation currency to US$ in 2016.

3 Closing share price at 31 December 2017 was A$5.45.

4 Whilst the 2014 company performance result was 78%, the actual STI payout was reduced by the Board to 58%.

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## CEO REMUNERATION

| | |
|---|---|
| What is the CEO's TFR? | US$1,380,060 per annum. There was no TFR increase for the CEO in 2017. The difference in the amount compared with last year relates to US$ exchange rate movements. |
| What notice periods are applicable for termination? | The CEO's contract has no fixed term and may be terminated with 12 months' notice by either party.<br>Employment may be ended immediately in certain circumstances including misconduct, incapacity, and mutual agreement or in the event of a fundamental change in the CEO's role or responsibility. |
| What termination benefits apply? | The Company may elect to pay the CEO in lieu of any unserved notice period. If termination is by mutual agreement, the CEO will receive a payment of US$1,150,050.<br>In the case of death, incapacity or fundamental change, the CEO is entitled to a payment equivalent to 12 months' base salary. |
| What sign-on grants were received? | In recognition of previous incentives foregone from his former employer, Mr Gallagher received a sign-on grant of SARs when he commenced employment with Santos in 2016. The SARs had a face value of US$766,700 equal to a total of 333,822 SARs divided as follows:<br>• 50% (166,911 SARs) that vested on 31 January 2017; and<br>• 50% (166,911 SARs) that vested on 31 January 2018.<br>Mr Gallagher has five years from the date of vesting to convert the SARs into Santos shares. Mr Gallagher does not need to pay any amount on conversion of the SARs. |
| **STI** | |
| What is the maximum STI the CEO could receive? | The CEO has a maximum STI opportunity of 100% of his TFR. |
| How much STI did the CEO receive in respect of 2017 performance? | The Board formally assessed the CEO's 2017 performance and awarded an STI of US$1,269,655, equivalent to 92% of his maximum STI. This award will be delivered as 70% cash and 30% in deferred equity restricted for two years. This award recognises Mr Gallagher's strong leadership of the Company's turnaround. |
| **LTI** | |
| What is the amount of LTI the CEO can receive? | The CEO has a maximum LTI opportunity of 150% of TFR allocated on a face value basis. In accordance with the approval of shareholders at the May 2017 Annual General Meeting (AGM), the CEO was granted 671,641 SARs in respect of his 2017 LTI. |
| What are the performance conditions of the 2017 LTI program for the CEO? | The performance conditions of the CEO's grant are the same as those of the Senior Executives' grant outlined on page 51. |

# Remuneration Report
continued

## SENIOR EXECUTIVE REMUNERATION

| | |
|---|---|
| **Fixed remuneration** | |
| Was there an increase in Senior Executives' TFR? | Independent market benchmarking was undertaken to review Senior Executives' remuneration. Mr Woods received a 7.5% TFR increase from 1 July 2017 reflecting his increased accountabilities and promotion to EVP Onshore Upstream. All other KMPs remained the same. |
| **STI** | |
| What was the maximum STI Senior Executives could receive? | The Senior Executives have a maximum STI opportunity of up to 85% of their TFR. |
| How were STI payments calculated? | The STI payments for Mr Byrne, Mr Santostefano and Mr Woods are based on 60% Company and 40% individual performance; for Mr Neilson, STI is based on 80% Company and 20% individual performance. |
| How was performance assessed for STI purposes? | Company performance against the overall Company Scorecard is assessed by the Committee and the Board.<br>Each Senior Executive's individual performance is assessed by the CEO against a number of objectives, including financial, operational and strategic measures. |
| How much STI will Senior Executives receive in respect of 2017 performance? | The Company's performance against the 2017 Company Scorecard as assessed by the Board resulted in a score of 88.5%. Further details of each individual Senior Executive's remuneration is provided in Table 5 "2016 and 2017 Senior Executive remuneration details" on page 43. |
| **LTI** | |
| How much LTI was granted to Senior Executives in 2017? | In 2017, Senior Executives received an LTI award equivalent to 80% of TFR which was allocated on a face value basis. For the 2017 year only, Mr Neilson received an LTI award equivalent to 100% of his TFR. |
| What are the LTI performance conditions? | The grant has a four year performance period from 1 January 2017 to 31 December 2020. Vesting is based on the four equally weighted performance targets as indicated on page 51. The vesting schedule can be also be found on page 52. |
| What proportion of prior year LTI grants vested in 2017? | Nil.<br>The testing of the 2014 LTI grant with a performance period 1 January 2014 to 31 December 2017 occurred in early 2018. As the performance hurdle was not achieved, there was no vesting of the grant and it was forfeited. |

### Service agreements and termination entitlements

The Company has entered into service agreements with the Senior Executives. For all existing Senior Executives, the service agreements are ongoing until termination by the Company upon giving between 6 and 12 months' notice, or by the Senior Executive giving between 6 and 12 months' notice. In a Company-initiated termination, the Company may make a payment in lieu of notice equivalent to the TFR that the Senior Executive would have received over the notice period. All Senior Executives' service agreements may be terminated immediately for cause, whereupon no payments in lieu of notice or other termination payments are payable under the agreement.

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## AT RISK REMUNERATION SUMMARY

### At risk remuneration

A higher proportion of the CEO's total remuneration package is "at risk" relative to that of the Senior Executives because the CEO has the greatest scope to personally influence the Company's performance.

***Table 3: Relative weightings of remuneration components for CEO and Senior Executives[1]***

| | | | At risk remuneration | | | |
|---|---|---|---|---|---|---|
| | | **Fixed remuneration** | **STI[2]** | **LTI** | **Total "at risk"** | **Total** |
| **CEO[3]** | **2017** | **28.6%** | **28.6%** | **42.8%** | **71.4%** | **100%** |
| | 2016 | 28.6% | 28.6% | 42.8% | 71.4% | 100% |
| **Senior Executives** | **2017** | **37.7%** | **32.1%** | **30.2%** | **62.3%** | **100%** |
| | 2016 | 38.2% | 31.2% | 30.6% | 61.8% | 100% |

1 These figures do not reflect the actual relative value derived by the Executive from each of the components, which is dependent on actual performance against targets for the "at risk" components. The figures represent maximum potential of each component.

2 Also includes deferred STI component.

3 The figures here do not include the CEO's sign-on grant.

## NON-EXECUTIVE DIRECTOR REMUNERATION

### Remuneration policy

The diagram below shows the key objectives of Santos' non-executive Director Remuneration Policy and how these are implemented through the Company's remuneration framework.

| Securing and retaining talented, qualified Directors | Promoting independence and impartiality | Aligning Director and shareholder interests |
|---|---|---|
| Fee levels are set with regard to:<br>• time commitment and workload;<br>• the risk and responsibility attached to the role;<br>• experience and expertise; and<br>• market benchmarking. | • Fee levels do not vary according to the performance of the Company or individual Director performance from year to year.<br>• Independent Directors' performance is assessed at the time of re-election. | • Santos encourages its non-executive Directors to build a long-term stake in the Company and established a minimum shareholding requirement of 15,000 shares for all non-executive Directors to be acquired within three years.<br>• Non-executive Directors can acquire shares through acquisition on market during trading windows and/or through the non-executive Director share plan. |

# Remuneration Report
continued

### Maximum aggregate amount

Total fees paid to all non-executive Directors in a year, including Board Committee fees, must not exceed US$1,993,420 being the amount approved by shareholders at the 2013 AGM.

Directors may also be paid additional fees for special duties or exertions, and are entitled to be reimbursed for all business-related expenses.

### Remuneration

There have been no increases in non-executive Director fees since October 2013.

Remuneration details for the non-executive Directors are provided in Table 11 "2016 and 2017 non-executive Director remuneration details" on page 46.

### Fee structure

***Table 4: Non-executive Directors' fees per annum[1]***

| | Chair[2] | Member |
|---|---|---|
| | US$ | US$ |
| Board | $386,072 | $128,461 |
| Audit and Risk Committee | $32,201 | $16,101 |
| Environment, Health, Safety and Sustainability Committee | $16,867 | $11,501 |
| Nomination Committee[3] | N/A | $7,667 |
| People and Remuneration Committee | $23,001 | $12,267 |

1 Fees are shown exclusive of superannuation.

2 The Chair of the Board does not receive any additional fees for serving on or chairing any Board committee.

3 The Chair of the Board is the Chair of the Nomination Committee, in accordance with its Charter.

### Superannuation and retirement benefits

Superannuation contributions are made on behalf of non-executive Directors in accordance with the requirements of the Company's statutory superannuation obligations. Non-executive Directors are not entitled to retirement benefits (other than mandatory statutory entitlements).

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## DETAILED REMUNERATION INFORMATION

Table 5 presents summarised details of the remuneration for the KMPs in 2016 and 2017 as required under the Corporations Act. The current KMP are the executives that Santos considers to have the requisite authority and responsibility to meet the definition of Key Management Personnel as required under the Corporations Act. All remuneration components have been converted from A$ to US$ using an average rate of $0.7667 for 2017 and $0.7451 for 2016.

***Table 5: 2016 and 2017 Senior Executive remuneration details***

| | | Short-term employee benefits | | | Post-employment | Share-based payments[1] | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Base salary | STI[2] | Other[3] | Superannuation contributions | LTI | Deferred STI[4] | Options | Ordinary shares[5] | Total share-based payments | Termination | Other long-term benefits (long service)[6] | Total | Total "at risk" |
| | | US$ | US$ | US$ | US$ | US$ | US$ | US$ | US$ | US$ | US$ | US$ | US$ | % |
| KT Gallagher[7] | 2017 | 1,357,059 | 888,759 | 4,095 | 23,001 | 910,807 | 222,427 | _ | _ | 1,133,234 | _ | 15,559 | 3,421,707 | 59% |
| | 2016 | 1,205,510 | 530,958 | 7,305 | 23,905 | 904,818 | 101,448 | _ | 212,354 | 1,218,620 | _ | _ | 2,986,298 | 59% |
| P Byrne[8] | 2017 | 198,899 | 99,211 | 7,517 | 9,161 | _ | 13,530 | _ | _ | 13,530 | _ | _ | 328,318 | 34% |
| | 2016 | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ |
| A Neilson[9] | 2017 | 592,276 | 324,774 | 2,013 | 21,084 | 155,046[10] | 44,274 | _ | _ | 199,320 | _ | 6,649 | 1,146,116 | 46% |
| | 2016 | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ | _ |
| V Santostefano[11] | 2017 | 630,611 | 290,809 | 2,058 | 21,084 | 154,858 | 74,193[12] | _ | _ | 229,051 | _ | 7,347 | 1,180,960 | 44% |
| | 2016 | 476,637 | 181,134 | 7,305 | 16,765 | 67,947 | 29,523 | _ | 72,424 | 169,894 | _ | _ | 851,735 | 41% |
| BK Woods | 2017 | 511,772 | 272,639 | 4,095 | 21,084 | 192,764 | 119,951 | _ | _ | 312,715 | _ | 14,300 | 1,136,605 | 52% |
| | 2016 | 469,413 | 150,957 | _ | 22,353 | 171,509 | 84,362 | _ | 60,353 | 316,224 | _ | 3,601 | 962,548 | 49% |
| JH Anderson[13] | 2017 | 386,480 | 280,842 | _ | 15,684 | 275,866 | 113,640 | _ | _ | 389,506 | 287,513 | 36,190 | 1,396,215 | 48% |
| | 2016 | 525,671 | 205,424 | 11,177 | 26,079 | 293,560 | 140,048 | _ | 82,185 | 515,793 | _ | (2,737) | 1,281,407 | 56% |

1 In accordance with the requirements of the Accounting Standards, remuneration includes a proportion of the value of the equity-linked compensation determined as at the grant date and progressively expensed over the vesting period. The amount allocated as remuneration is not relative to or indicative of the actual benefit (if any) that the Senior Executives may ultimately realise should the equity instruments vest. The value of equity-linked compensation was determined in accordance with AASB 2 *Share-based Payment* applying the Monte Carlo simulation method. Details of the assumptions underlying the valuation are set out in note 7.2 to the financial statements.

2 This amount represents the cash portion of the STI performance award for 2017, which will be paid in March 2018.

3 "Other" comprises ad hoc payments treated as remuneration, such as assignment and mobilisation allowance and other non-monetary benefits.

4 This amount represents a proportion of the estimated value of the deferred STI, determined in accordance with the requirements of AASB 2 *Share-based Payment* and progressively expensed over a three-year vesting period being the year of performance and a two-year period of service to which the grant relates. The amount allocated as remuneration is not relative to or indicative of the actual benefit (if any) that the Senior Executives may ultimately realise should the equity instruments vest. The value has been calculated in accordance with AASB 2 *Share-based Payment* based on an estimate of the fair value of the equity instruments.

5 This relates to the 2016 STI award where 20% was delivered as ordinary shares. In 2016, the Board agreed that in addition to the 30% of any STI award being deferred into equity for two years, a further 20% of the 2016 STI award would be awarded in ordinary shares, rather than cash.

6 "Other long-term benefits" represents the movement in the Senior Executive's long service leave entitlements measured as the present value of the estimated future cash outflows to be made in respect of the Senior Executive's service between the respective reporting dates. Mr Byrne will not have any other long-term benefits accrued for accounting purposes until after 12 months of service.

7 Mr Gallagher received no TFR increase in 2017. The 2017 figures represented for the CEO are for the full 12 months of 2017 whereas in 2016 only 11 months was earned after he commenced on 1 February 2016.

8 Mr Byrne became a KMP on 14 August 2017 when he commenced as EVP Marketing and Trading. Figures shown for Mr Byrne are for the period 14 August 2017 to 31 December 2017.

9 Mr Neilson became a KMP on 1 January 2017 when he commenced as Chief Financial Officer.

10 Mr Neilson received an LTI award equivalent to 100% of TFR for the 2017 LTI grant only.

11 The 2017 figures are for the full 12 months of 2017 whereas in 2016, Mr Santostefano became a KMP on 21 March 2016.

12 In 2016 Mr Santostefano's 2016 STI deferred equity component was delivered as SARs rather than shares.

13 Mr Anderson ceased to be a KMP on 14 August 2017. Figures shown for Mr Anderson are for the period 1 January 2017 to 13 August 2017 as well as the termination payment he will receive in 2018 on the cessation of his employment, in accordance with his contractual arrangements.

# Remuneration Report
continued

Tables 6 and 7 contain details of the number and value of SARs and shares granted, vested and lapsed for the CEO in 2017. The CEO did not have any options granted, vesting or lapsing in 2017. The CEO has no options to exercise.

***Table 6: 2017 SARs outcomes for CEO***

| | Granted | | Vested | | Lapsed |
|---|---|---|---|---|---|
| | Number | Maximum value[2] | Number | Value | Number |
| | | US$ | | US$ | |
| SARs | 671,641[1] | 1,390,357 | 166,911[3] | $511,883[4] | – |

1 The number of SARs granted to the CEO relate to his 2017 LTI performance grant as approved at the 2017 Annual General Meeting (AGM).

2 Maximum value represents the fair value of LTI grants received in 2017 determined in accordance with AASB 2 *Share-based Payment*. The fair value of the grant as at the grant date of 19 May 2017 is weighted at a fair value of A$2.70. Details of the assumptions underlying the valuations are set out in note 7.2 to the financial statements. The minimum total value of the grant to the CEO, if the applicable vesting conditions are not met, is nil in all cases. All values have been converted to US$.

3 The number of SARs vested for the CEO relate to the first tranche of his 2016 sign-on grant (vested on 31 January 2017).

4 The value of SARs vested for the CEO relates to the first tranche of his 2016 sign-on grant (vested on 31 January 2017), using the share price of A$4.00 on that date. All values have been converted to US$.

***Table 7: 2017 share outcomes for CEO***

| | Granted | | Vested | | Lapsed |
|---|---|---|---|---|---|
| | Number | Maximum value | Number | Value | Number |
| | | US$ | | US$ | |
| Shares | 181,933[1] | 502,864 | – | – | – |

1 The number of equity instruments granted to the CEO relate to his 2016 STI award being 111,038 restricted shares (deferred shares restricted for two years) and 70,895 ordinary shares, granted without restriction. For the 111,038 restricted shares maximum value represents the fair value of 2016 STI grant of deferred shares received in 2017 determined with AASB 2 *Share-based Payment*. The fair value of the deferred STI grant as at the grant date of 19 April 2017 was A$3.57. The minimum total value of the restricted shares grant to the CEO is nil. In respect of the 70,895 ordinary shares granted without restriction on 19 April 2017, the value reflects the closing share price of A$3.66 on that date. All values have been converted to US$.

Tables 8 and 9 contain details of the number and value of SARs and shares granted, vested and lapsed for Senior Executives in 2017. No Senior Executive had any options granted, vesting or lapsing in 2017. No options were exercised in 2018.

***Table 8: 2017 SARs outcomes for Senior Executives***

| | Granted | | Vested | | Lapsed |
|---|---|---|---|---|---|
| | Number[1] | Maximum value[2] | Number | Value | Number[3] |
| | | US$ | | US$ | |
| PA Byrne[4] | – | – | – | – | – |
| AM Neilson | 222,781[5] | 520,677[6] | 23,777[7] | 93,701[8] | – |
| V Santostefano | 207,024[9] | 479,757 | – | – | – |
| BK Woods | 133,333 | 296,457 | 353[10] | 817 | (20,545) |
| JH Anderson | 149,253 | 331,854 | – | – | (48,980) |
| **Total** | **712,391** | **1,628,745** | **24,130** | **94,518** | **(69,525)** |

1 This number relates to the full LTI award for the four-year performance period ended on 31 December 2020 plus any individual SARs granted which is explained below.

2 Maximum value represents the fair value of LTI grants received in 2017 determined in accordance with AASB 2 *Share-based Payment*. The fair value of the grant as at the grant date of 21 March 2017 is weighted at a fair value of A$2.90. Details of the assumptions underlying the valuations are set out in note 7.2 to the financial statements. The minimum total value of the grant to the Senior Executives, if the applicable vesting conditions are not met, is nil in all cases. All values have been converted to US$.

3 Lapsed SARs relate to the 2014 four-year LTI grant.

4 Mr Byrne only commenced in the second half of 2017 and did not participate in the 2017 LTI offer.

5 The figure for Mr Neilson reflects the 2017 LTI grant of 199,004 SARs and 2016 sign-on grant of 23,777 SARs.

6 Mr Neilson's SARs included for the 2017 LTI maximum value is in accordance with note 2 above. For the 23,777 sign-on SARs, maximum value reflects the fair value of A$4.29 as at the grant date of 1 December 2016. All values have been converted to US$.

7 The number of SARs vested for Mr Neilson relate to his sign-on grant (vested on 1 December 2017).

8 This figure shows the value of Mr Neilson's sign-on grant using the share price of A$5.14 reflecting the vesting date of 1 December 2017. All values have been converted to US$.

9 The figure for Mr Santostefano reflects the 2017 LTI grant of 169,154 SARs and 2016 STI deferred equity component delivered as SARs of 37,870. For the 37,870 SARs delivered as deferred equity, maximum value reflects the fair value of A$3.57 as at the grant date of 19 April 2017. The minimum total value of the grant, if the applicable vesting conditions are not met, is nil in all cases. All values have been converted to US$.

10 Mr Woods previously participated in the Company's general employee share plan prior to becoming a KMP in August 2015. In 2017 a total of 353 SARs vested. The value shown is based on the closing price of A$3.02 on the vesting date of 3 July 2017. All values have been converted to US$.

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***Table 9: 2017 share outcomes for Senior Executives***

| | Granted | | Vested | | Lapsed |
|---|---|---|---|---|---|
| | Number[1] | Maximum value[2] | Number[3] | Value[4] | Number |
| | | US$ | | US$ | |
| PA Byrne[5] | – | – | – | – | – |
| AM Neilson[6] | – | – | – | – | – |
| V Santostefano | 24,179[7] | 67,849 | – | – | – |
| BK Woods | 51,707[8] | 142,919 | 54,556 | 227,963 | – |
| JH Anderson | 70,398[9] | 194,581 | 74,881 | 312,891 | – |
| **Total** | **146,284** | **405,349** | **129,437** | **540,854** | **–** |

1 This relates to the 2016 STI award delivered as restricted shares and ordinary shares.

2 Maximum value represents the fair value of 2016 STI deferred shares determined in accordance with AASB 2 *Share-based Payment*. The fair value of the deferred STI grant as at the grant date of 19 April 2017 was A$3.57. The minimum total value of the grant, if the applicable vesting conditions are not met, is nil. For the ordinary shares granted without restriction on 19 April 2017, the value represents the share price of A$3.66 on that date, All values have been converted to US$.

3 This relates to the 2015 STI grant that was deferred for two years from 1 January 2016 to 31 December 2017 and vested in full on 31 December 2017.

4 These figures show the value of the 2015 deferred STI grant, using a share price of A$5.45 on 31 December 2017 converted to US$.

5 Mr Byrne only commenced on 14 August 2017 when he commenced as EVP Marketing and Trading and did not participate in the 2016 STI plan.

6 Mr Neilson only commenced in December 2016 and did not participate in the 2016 STI plan.

7 These figures relate to the 2016 STI award delivered as ordinary shares.

8 These figures relate to the 2016 STI award delivered as 31,558, deferred shares and 20,149 ordinary shares.

9 These figures relate to the 2016 STI award delivered as 42,961 deferred shares and 27,437 ordinary shares.

Table 10 outlines the LTI grants that were tested or still in progress in 2017.

***Table 10: LTI grants***

| Grant year | Grant type | Vesting condition(s) | Performance/ vesting period | Status |
|---|---|---|---|---|
| 2014 | Four-year Performance Award | Relative TSR performance against ASX 100 companies (75%) and S&P GEI (25%) | 1 January 2014 to 31 December 2017 | Testing completed. Resulted in 0% of the grant vesting. |
| 2015 | Four-year Performance Award | Relative TSR performance against ASX 100 companies (75%) and S&P GEI (25%) | 1 January 2015 to 31 December 2018 | In progress. |
| 2016 | Four-year Performance Award | Relative TSR performance against ASX 100 companies (25%) and S&P GEI (25%)<br>FCFBP (25%)<br>ROACE (25%) | 1 January 2016 to 31 December 2019 | In progress. |
| 2016 | CEO sign on grant | Service based | 50% vesting (12 months) 1 February 2016 to 31 January 2017 | Vested. |
| | | Service based | 50% vesting (24 months) 1 February 2016 to 31 January 2018 | Vested. |
| 2017 | Four-year Performance Award | Relative TSR performance against ASX 100 companies (25%) and S&P GEI (25%)<br>FCFBP (25%)<br>ROACE (25%) | 1 January 2017 to 31 December 2020 | In progress. |
| 2017 | CFO sign-on grant[1] | Service based | 1 December 2016 to 30 November 2017 | Vested. |

1 Mr Neilson became a KMP on 1 January 2017.

Full details of all grants made prior to 2017 can be found in note 7.2 to the financial statements and in prior Remuneration Reports.

# Remuneration Report
continued

Details of the fees and other benefits paid to non-executive Directors in 2017 are set out in Table 11. No fee increases were received in 2017. Differences in fees received between 2016 and 2017 reflect changes in roles and responsibilities (i.e. Chair or Committee appointments), superannuation payments and currency fluctuations. No share-based payments were made to any non-executive Directors.

***Table 11: 2016 and 2017 Non-executive Director remuneration details***

| Director | | Short-term benefits | | | Retirement benefits | | |
|---|---|---|---|---|---|---|---|
| Director | Year | Directors' fees (incl. committee fees) | Fees for special duties or exertions | Other | Superannuation[11] | Share-based payments | Total |
| | | US$ | US$ | US$ | US$ | US$ | US$ |
| YA Allen[1] | 2017 | 156,693 | – | – | 14,631 | – | 171,324 |
| | 2016 | 148,463 | – | – | 14,104 | – | 162,567 |
| PR Coates[2] | 2017 | 384,495 | – | – | 15,205 | – | 399,700 |
| | 2016 | 373,938 | 30,621 | – | 17,410 | – | 421,969 |
| GM Cowan[3] | 2017 | 159,085 | – | – | 15,068 | – | 174,153 |
| | 2016 | 99,463 | – | – | 9,405 | – | 108,868 |
| RA Franklin[4] | 2017 | 133,065 | – | – | 652 | – | 133,717 |
| | 2016 | 173,173 | – | – | 677 | – | 173,850 |
| H Goh[5] | 2017 | 170,629 | – | – | 489 | – | 171,118 |
| | 2016 | 164,353 | – | – | 557 | – | 164,910 |
| V Guthrie[6] | 2017 | 65,501 | – | – | 6,223 | – | 71,724 |
| | 2016 | – | – | – | – | – | – |
| PR Hearl[7] | 2017 | 148,734 | – | – | 14,087 | – | 162,821 |
| | 2016 | 89,411 | – | – | 8,494 | – | 97,905 |
| GJW Martin[8] | 2017 | 113,526 | – | – | 10,048 | – | 123,574 |
| | 2016 | 166,514 | – | – | 14,501 | – | 181,015 |
| SD Sheffield[9] | 2017 | 48,609 | – | – | 149 | – | 48,758 |
| | 2016 | 137,799 | – | – | 287 | – | 138,086 |
| Y Shi[10] | 2017 | 71,757 | – | – | 7,074 | – | 78,831 |
| | 2016 | – | – | – | – | – | – |

1 Ms Allen was appointed Chair of the People and Remuneration Committee and as a member of the Nomination Committee on 21 September 2017. Ms Allen was appointed as a member of the Audit and Risk Committee and retired as a member of the Environment, Health, Safety and Sustainability Committee on 25 October 2017.

2 Mr Coates was Chairman of the Board during 2017, and in accordance with its Charter, as Chairman of the Board, Mr Coates was the Chair of the Nomination Committee during 2017.

3 Mr Cowan is the current Chair of the Audit and Risk Committee.

4 Mr Franklin retired as a non-executive Director on 30 September 2017.

5 Mr Goh is a member of the Audit and Risk Committee, Environment, Health, Safety and Sustainability Committee and was appointed to the Nomination Committee on 25 October 2017.

6 Dr Guthrie was appointed to the Board on 1 July 2017 and became a member of the Environment, Health, Safety and Sustainability Committee on 25 October 2017.

7 Mr Hearl is a member of the People and Remuneration Committee. He was appointed as a member of the Nomination Committee on 21 September 2017. On 25 October 2017, Mr Hearl was appointed as Chair of the Environment, Health, Safety and Sustainability Committee and he retired from the Audit and Risk Committee.

8 Mr Martin retired as a non-executive Director on 25 August 2017.

9 Mr Sheffield retired as a non-executive Director on 4 May 2017.

10 Mr Shi was appointed to the Board on 26 June 2017, and was appointed as a member of the People and Remuneration Committee on 21 September 2017 and the Audit and Risk Committee on 25 October 2017.

11 Includes superannuation guarantee payments. Superannuation guarantee payments were made to Mr Franklin, Mr Goh, Mr Sheffield only in relation to days worked in Australia.

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## KEY MANAGEMENT PERSONNEL DISCLOSURES

### (a) Loans to key management personnel

There have been no loans made, guaranteed or secured, directly or indirectly, by the Company or any of its subsidiaries at any time throughout the year to any KMP, including to their related party.

### (b) Equity holdings of key management personnel

#### *Options and SARs holdings*

The movement during the reporting period in the number of options and SARs over ordinary shares of the Company held directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

| | Opening balance | Granted[1] | Options exercised/ rights vested | Other changes[2] | Sold/ transferred | Closing balance | Vested at end of the year | Vested and exercisable at end of the year | Vested but not exercisable at end of the year |
|---|---|---|---|---|---|---|---|---|---|
| **2017** | | | | | | | | | |
| **Options** | | | | | | | | | |
| ***Directors*** | | | | | | | | | |
| Gallagher, Kevin Thomas | – | – | – | – | – | – | – | – | – |
| ***Senior Executives*** | | | | | | | | | |
| Anderson, John Hugh[3] | 39,593 | – | – | (39,593) | – | – | – | – | – |
| Byrne, Philip Ambrose[4] | – | – | – | – | – | – | – | – | – |
| Neilson, Anthony Myles[5] | | | | | | | | | |
| Santostefano, Vincent | – | – | – | – | – | – | – | – | – |
| Woods, Brett Kenneth | – | – | – | – | – | – | – | – | – |
| Seaton, Andrew John[7] | 22,213 | – | – | (22,213) | – | – | – | – | – |
| **Total** | **61,806** | **–** | **–** | **(61,806)** | **–** | **–** | **–** | **–** | **–** |
| **SARs** | | | | | | | | | |
| ***Directors*** | | | | | | | | | |
| Gallagher, Kevin Thomas | 1,235,142 | 671,641 | (166,911) | – | – | 1,739,872 | 166,911 | 166,911 | – |
| ***Senior Executives*** | | | | | | | | | |
| Anderson, John Hugh[3] | 294,998 | 149,253 | – | (444,251) | – | – | – | – | – |
| Byrne, Philip[4] | – | – | – | – | – | – | – | – | – |
| Neilson, Anthony[5] | 23,777 | 199,004 | (23,777) | – | – | 199,004 | 23,777 | 23,777 | – |
| Santostefano, Vincent | 176,620 | 207,024 | – | – | – | 383,644 | – | – | – |
| Woods, Brett Kenneth | 214,676 | 133,333 | (353)[6] | 20,545 | – | 368,201 | 353 | 353 | – |
| Seaton, Andrew John[7] | 310,790 | – | – | (310,790) | – | – | – | – | – |
| **Total** | **2,256,003** | **1,360,255** | **(191,041)** | **(734,496)** | **–** | **2,690,721** | **191,041** | **191,041** | **–** |

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# Remuneration Report continued

| | Opening balance | Granted | Deferred shares vested | Other changes | Sold/ transferred | Closing balance | Vested at end of the year | Vested and exercisable at end of the year | Vested but not exercisable at end of the year |
|---|---|---|---|---|---|---|---|---|---|
| **2017** | | | | | | | | | |
| **Deferred shares** | | | | | | | | | |
| ***Directors*** | | | | | | | | | |
| Gallagher, Kevin Thomas | – | 111,038 | – | – | – | 111,038 | – | – | – |
| ***Senior Executives*** | | | | | | | | | |
| Anderson, John Hugh[3] | 74,881 | 42,961 | (74,881) | (42,961) | – | – | 74,881 | 74,881 | – |
| Byrne, Philip Ambrose[4] | – | – | – | – | – | – | – | – | – |
| Neilson, Anthony Myles[5] | – | – | – | – | – | – | – | – | – |
| Santostefano, Vincent | – | – | – | – | – | – | – | – | – |
| Woods, Brett Kenneth | 54,556 | 31,558 | (54,556) | – | – | 31,558 | 54,556 | 54,556 | – |
| **Total** | **129,437** | **185,557** | **(129,437)** | **(42,961)** | **–** | **142,596** | **129,437** | **129,437** | **–** |

1 SARs and deferred shares granted to the CEO and Senior Executives are disclosed in Tables 6–9.

2 Other changes include SARs that did not vest due to not satisfying the vesting conditions and were forfeited during the year; deferred shares that were forfeited; and changes resulting from individuals ceasing to be and becoming KMPs during the period.

3 Mr Anderson remained a KMP from 1 January 2017 to 13 August 2017. He ceased to be a KMP on 14 August 2017.

4 Mr Byrne became a KMP on 14 August 2017.

5 Mr Neilson became a KMP on 1 January 2017. Mr Neilson's opening balance includes his sign-on grant of 23,777 SARs.

6 Mr Woods previously participated in the Company's general employee share plan prior to becoming a KMP in August 2015. In 2017 a total of 353 SARs vested.

7 Mr Seaton ceased to be a KMP on 1 January 2017.

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## SHARE HOLDINGS

| | Opening balance | Received vesting of SARs | Purchased[1] | Sold | Deferred 2015 STI that vested on 31 December 2017 | Other Changes[2] | Closing balance | Balance held nominally at end of the year |
|---|---|---|---|---|---|---|---|---|
| **2017** | | | | | | | | |
| **Ordinary shares - fully paid** | | | | | | | | |
| ***Directors*** | | | | | | | | |
| Allen, Yasmin Anita | 15,883 | – | – | – | – | – | 15,883 | – |
| Coates, Peter Roland | 120,446 | – | 11,424 | – | – | – | 131,870 | – |
| Cowan, Guy Michael | 15,000 | – | – | – | – | – | 15,000 | – |
| Franklin, Roy Alexander[3] | 25,188 | – | 3,808 | – | – | (28,996) | – | – |
| Gallagher, Kevin Thomas | 100,000 | 166,911 | 3,808 | – | – | 70,895 | 341,614 | – |
| Goh, Hock | 33,407 | – | 3,808 | – | – | – | 37,215 | – |
| Guthrie, Vanessa[4] | – | – | – | – | – | – | – | – |
| Hearl, Peter Roland | 45,000 | – | 3,808 | – | – | – | 48,808 | – |
| Martin, Gregory John Walton[5] | 38,912 | – | 3,808 | – | – | (42,720) | – | – |
| Sheffield, Scott Douglas[6] | 63,529 | – | – | – | – | (63,529) | – | – |
| Shi, Yujiang[7] | – | – | – | – | – | – | – | – |
| ***Senior Executives*** | | | | | | | | |
| Anderson, John Hugh[8] | 131,287 | – | – | – | 74,881 | (206,168) | – | – |
| Byrne, Philip[9] | – | – | – | – | – | 5,804 | 5,804 | – |
| Neilson, Anthony[10] | – | 23,777 | – | – | – | – | 23,777 | – |
| Santostefano, Vincent | – | – | – | – | – | 24,179 | 24,179 | – |
| Seaton, Andrew John[11] | 53,054 | – | – | – | – | (53,054) | – | – |
| Woods, Brett Kenneth | 1,861 | 353 | – | – | 54,556 | 20,149 | 76,919 | – |
| **Total** | **643,567** | **191,041** | **30,464** | **–** | **129,437** | **(273,440)** | **721,069** | **–** |

1 Includes shares issued in 2017 as part of the share purchase plan.

2 20% of the 2016 STI awarded as ordinary shares as well as changes resulting from individuals ceasing to be Directors or KMPs during the period.

3 Mr Franklin retired as a non-executive Director on 30 September 2017.

4 Dr Guthrie was appointed to the Board on 1 July 2017.

5 Mr Martin retired as a non-executive Director on 25 August 2017.

6 Mr Sheffield retired as a non-executive Director on 4 May 2017.

7 Mr Shi was appointed to the Board on 26 June 2017.

8 Mr Anderson ceased to be a KMP on 14 August 2017.

9 Mr Byrne became a KMP on 14 August 2017. The 5,804 represents balances held before he commenced employment.

10 Mr Neilson became a KMP on 1 January 2017.

11 Mr Seaton ceased to be a KMP on 1 January 2017.

# Remuneration Report
continued

## DETAILED INFORMATION ABOUT LINKING COMPANY PERFORMANCE TO AT RISK REMUNERATION

**STI questions and answers**

| | |
|---|---|
| How are the Company's short-term performance targets determined? | The Company's short-term performance targets comprise a combination of financial and operational targets, all of which are agreed with the Board and directly related to stabilising the base business and improving financial performance. These are captured in the Company's annual performance scorecard. |
| What is measured in the Company's annual performance scorecard? | The Company Scorecard includes a range of Company performance measures used to drive balanced business performance. These measures include lagging indicators to assess the Company's past performance, as well as forward-looking indicators to ensure the Company is positioning itself effectively for future growth – see Table 1 "2017 STI scorecard performance" on page 36.<br><br>The Board believes that this Scorecard is balanced and focuses CEO and Senior Executives to achieve the key outcomes necessary to deliver stronger returns to shareholders. |
| How is Company performance assessed? | Company performance is formally assessed by the People and Remuneration Committee against the overall Company Scorecard at the end of each financial year, and this forms the basis of a recommendation to the Board.<br><br>Each metric within the Company Scorecard is assessed against an agreed target and assigned a percentage weighting of the total Scorecard. The actual versus target performance of each metric is assigned a score between 0% and 100%. The weightings are then applied to these scores to derive a rating for that metric. The sum of each metric's rating is used to determine the Company's overall performance score.<br><br>The Board believes the above method of assessment is rigorous and provides a balanced assessment of the Company's performance. |
| How does Company performance impact the STI program? | The Company's overall performance score sets the budget available for STI allocations across the organisation in respect of that performance year. This is calculated by applying the percentage performance score to the maximum potential STI of all eligible employees. |

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**LTI questions and answers**

| | |
|---|---|
| How is the LTI linked to Company performance? | LTI aligns the rewards received by the CEO and Senior Executives with the longer-term performance of Santos. Measuring relative TSR performance across two comparator groups in addition to FCFBP and ROACE ensures Santos is able to measure its performance relative to other ASX 100 companies and international energy sector peers in addition to ensuring strong cash flows and shareholder returns. All 2017 LTI grants were solely performance based, ensuring further alignment with shareholder interests. |
| How is LTI awarded? | All LTI grants are delivered in the form of SARs, i.e. a conditional entitlement to a fully paid ordinary share at zero price, subject to satisfaction of the performance condition. Nothing is payable by Senior Executives if and when SARs vest. The Board has discretion to settle the SARs in cash if they vest. |
| What is the performance period? | SARs issued under the annual LTI program have a four-year performance period. This period represents an appropriate balance between providing a genuine and foreseeable incentive to Senior Executives and fostering a long-term view of shareholder interests. |
| What performance hurdles are applied to the LTI? | Vesting of the 2017 LTI grant is based on the following performance measures: |

| Weighting | Performance measures |
|---|---|
| 25% | Relative TSR measured against companies of the ASX100 |
| 25% | Relative TSR measured against companies of the S&P GEI |
| 25% | Free Cash Flow Breakeven Point (FCFBP) |
| 25% | Return on Average Capital Employed (ROACE) |

The Board has discretion to adjust the TSR comparator groups for example to take account of takeovers, mergers and demergers that occur during the performance period. Relative TSR performance, being a market-based measure, is tested by an independent third party and reviewed by the Board prior to vesting. FCFBP and ROACE, being non-market based measures, will be tested and audited internally with all results externally audited as part of the *Annual Report* release.

| | |
|---|---|
| Why have the current LTI performance hurdles been chosen? | The Board believes that relative TSR continues to effectively align the interests of individual Senior Executives with that of the Company's shareholders, by motivating Senior Executives to achieve superior shareholder outcomes relative to Santos' competitors for investor capital and its energy sector peers. TSR takes into account share price and dividend yield and is therefore a robust and objective measure of shareholder returns.<br><br>FCFBP is the US$ oil price at which cash flows from operating activities equals cash flows from investing activities, as published in the Company's financial statements. This performance hurdle is aimed at driving the underlying business to become an operationally efficient low-cost producer focused on delivering shareholder value throughout the oil price cycle. As the aim of the performance hurdle is to measure the performance of the underlying business, the Board will have discretion to adjust the FCFBP for individual material items including asset acquisitions and disposals that may otherwise distort the measurement.<br><br>ROACE is measured as the underlying earnings before interest and tax (EBIT) divided by the average capital employed, being shareholders' equity plus net debt, as published in the Company's financial statements. Including ROACE as a performance measure aligns management to ensure that the business is optimised for profitability. |
| Why have the ASX 100 and S&P Global Energy Index been chosen as the comparator groups for Relative TSR? | The ASX 100 represents the companies in which most of the Company's shareholders would invest in as an alternative to Santos. If Santos performs well relative to these companies, it means that Santos shareholders' investments have performed well relative to alternative investments.<br><br>The S&P GEI was chosen as a second comparator group because the global energy market is of increasing relevance to Santos. Many of the companies that comprise the S&P GEI have oil and gas operations and are likely to be affected by similar global cyclical issues as Santos. Santos' major competitors are included in the Index, along with other leading industry players based in various countries. |

# Remuneration Report
continued

**LTI questions and answers**

How is vesting determined?

The vesting scales below apply to both the CEO's and Senior Executives' 2017 LTI performance grants.

There is no re-testing of the performance condition. SARs that do not vest upon testing of the performance condition will lapse.

**Relative TSR against the ASX100 and S&P GEI**

| TSR percentile ranking | % of grant vesting |
|---|---|
| Below 51st percentile | 0% |
| 51st percentile | 50% |
| straight line pro-rata vesting in between | |
| 76th percentile and above | 100% |

**Free cash flow breakeven point**

| FCFBP | % of grant vesting |
|---|---|
| >US$40/bbl | 0% |
| US$40/bbl | 50% |
| straight line pro-rata vesting in between | |
| Equal to or below US$35/bbl | 100% |

**Return On Average Capital Employed**

| ROACE | % of grant vesting |
|---|---|
| Below 100% of the Weighted Average Cost of Capital (WACC) | 0% |
| Equal to 100% of WACC | 50% |
| straight line pro-rata vesting in between | |
| Equal to or above 120% of WACC | 100% |

When can vested SARs be traded?

Upon vesting of SARs, shares will automatically be allocated to the Senior Executive. Trading in these shares is subject to compliance with the Company's Securities Dealing Policy.

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## CHANGES TO EXECUTIVE REMUNERATION FOR THE 2018 PERFORMANCE YEAR

In 2017, the Board continued to consider opportunities to deliver contemporary and competitive remuneration programs across the Company, having regard to its Transform Build Grow strategy. In particular the Board has decided to address the market competitiveness of the Executives' maximum STI level, which has been low relative to Executives' target STI.

As a result, the Board has approved changes that will enable greater upside opportunity for exceptional performance, offset by more challenging stretch KPIs in the 2018 Company Scorecard and an increased proportion of any award into deferred equity. Target STI will be maintained at the current level.

The changes are as follows for the 2018 performance year:

- increasing the maximum STI opportunity for the CEO from 100% to 125% of TFR;
- increasing the maximum STI opportunity for the Senior Executives up to 105% of TFR; and
- for both the CEO and Senior Executives reducing the cash component of any STI award from 70% to 50% and increasing the deferred equity component from 30% to 50% restricted for two years.

Following an independent external remuneration benchmarking review, the Board also decided to increase the CEO's TFR to A$1,890,000 (US$1,449,063) effective from 1 January 2018. This is the first TFR increase since the CEO joined in February 2016. Since the CEO's commencement at the beginning of 2016, both the Company's share price and market capitalisation have improved significantly, underpinned by a transformation of the Company's operations and business practices.

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# Directors' Report
continued

## INDEMNIFICATION

Rule 61 of the Company's Constitution provides that the Company indemnifies, on a full indemnity basis and to the full extent permitted by law, officers of the Company for all losses or liabilities incurred by the person as an officer of the Company, a related body corporate or trustee of a company-sponsored superannuation fund. Rule 61 does not permit the Company to indemnify an officer for any liability involving a lack of good faith.

Rule 61 also permits the Company to purchase and maintain a Directors' and Officers' insurance policy.

In conformity with Rule 61, the Company is party to Deeds of Indemnity in favour of each of the Directors referred to in this report who held office during the year and certain senior executives of the consolidated entity. The indemnities operate to the full extent permitted by law and are not subject to a monetary limit. Santos is not aware of any liability having arisen, and no claims have been made during or since the financial year ending 31 December 2017 under the Deeds of Indemnity.

During the year, the Company paid premiums in respect of Directors' and Officers' Liability and Legal Expenses insurance contracts for the year ended 31 December 2017 and since the end of the year the Company has paid, or agreed to pay, premiums in respect of such contracts for the year ending 31 December 2018. The insurance contracts insure against certain liability (subject to exclusions) persons who are or have been directors or officers of the Company and its controlled entities. A condition of the contracts is that the nature of the liability indemnified and the premium payable not be disclosed.

## NON-AUDIT SERVICES

Amounts paid or payable to the Company's auditor, Ernst & Young, for non-audit services provided during the year were:

| | |
|---|---|
| Taxation and other services | $355,000 |
| Assurance services | $401,000 |

The Directors are satisfied, based on the advice of the Audit and Risk Committee, that the provision of the non-audit services detailed above by Ernst & Young is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001* (Cth).

The reason for forming this opinion is that all non-audit services have been reviewed by the Audit and Risk Committee to ensure they do not impact the impartiality and objectivity of the auditor.

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* (Cth) is set out on page 129.

## ROUNDING

Australian Securities and Investments Commission Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 applies to the Company. Accordingly, amounts have been rounded off in accordance with that Instrument, unless otherwise indicated.

This report is made out on 20 February 2018 in accordance with a resolution of the Directors.



Director

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# Financial Report

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# Consolidated Income Statement
for the year ended 31 December 2017

| | Note | 2017 US$million | 2016 US$million |
|---|---|---|---|
| Product sales | 2.2 | **3,107** | 2,594 |
| Cost of sales | 2.3 | **(2,272)** | (2,153) |
| **Gross profit** | | **835** | 441 |
| Other revenue | | **65** | 33 |
| Other income | 2.7 | **123** | 157 |
| Impairment of non-current assets | 3.3 | **(938)** | (1,561) |
| Other expenses | 2.3 | **(411)** | (284) |
| Finance income | 5.2 | **24** | 15 |
| Finance costs | 5.2 | **(294)** | (296) |
| Share of net profit of joint ventures | 6.3(c) | **11** | 10 |
| **Loss before tax** | | **(585)** | (1,485) |
| Income tax benefit | 2.4(a) | **211** | 445 |
| Royalty-related tax benefit/(expense) | 2.4(b) | **14** | (7) |
| Total tax benefit | | **225** | 438 |
| **Net loss for the period attributable to owners of Santos Limited** | | **(360)** | (1,047) |
| **Earnings per share attributable to the equity holders of Santos Limited (¢)** | | | |
| Basic loss per share | 2.5 | **(17.3)** | (58.2) |
| Diluted loss per share | 2.5 | **(17.3)** | (58.2) |
| **Dividends per share (¢)** | | | |
| Paid during the period | 2.6 | **–** | 4 |
| Declared in respect of the period | 2.6 | **–** | – |

The consolidated income statement is to be read in conjunction with the notes to the consolidated financial statements.

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# Consolidated Statement of Comprehensive Income
for the year ended 31 December 2017

| | 2017 US$million | 2016 US$million |
|---|---|---|
| **Net loss for the period** | **(360)** | (1,047) |
| **Other comprehensive income, net of tax:** | | |
| *Items to be reclassified to profit or loss in subsequent periods:* | | |
| Exchange gain/(loss) on translation of foreign operations | **168** | (36) |
| Tax effect | **–** | – |
| | **168** | (36) |
| Gain on foreign currency loans designated as hedges of net investments in foreign operations | **191** | 20 |
| Tax effect | **(57)** | (6) |
| | **134** | 14 |
| (Loss)/gain on derivatives designated as cash flow hedges | **(3)** | 27 |
| Tax effect | **1** | (8) |
| | **(2)** | 19 |
| **Net other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods** | **300** | (3) |
| *Items not to be reclassified to profit or loss in subsequent periods:* | | |
| Remeasurement of defined benefit obligation | **–** | 2 |
| Tax effect | **–** | (1) |
| | **–** | 1 |
| Loss on financial liabilities at fair value through other comprehensive income (FVOCI) | **(32)** | – |
| Tax effect | **11** | – |
| | **(21)** | – |
| **Net other comprehensive (loss)/income not to be reclassified to profit or loss in subsequent periods** | **(21)** | 1 |
| **Other comprehensive income/(loss), net of tax** | **279** | (2) |
| **Total comprehensive loss attributable to owners of Santos Limited** | **(81)** | (1,049) |

The consolidated statement of comprehensive income is to be read in conjunction with the notes to the consolidated financial statements.

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# Consolidated Statement of Financial Position
as at 31 December 2017

| | Note | 2017 US$million | 2016 US$million |
|---|---|---|---|
| **Current assets** | | | |
| Cash and cash equivalents | 4.1 | **1,231** | 2,026 |
| Trade and other receivables | 4.2 | **440** | 367 |
| Prepayments | | **28** | 34 |
| Inventories | 4.3 | **266** | 321 |
| Other financial assets | 5.5(g) | **–** | 7 |
| Tax receivable | | **7** | 15 |
| Assets held for sale | | **–** | 180 |
| **Total current assets** | | **1,972** | 2,950 |
| **Non-current assets** | | | |
| Receivables | 4.2 | **–** | 5 |
| Prepayments | | **17** | 17 |
| Investments in joint ventures | 6.3(b) | **43** | 56 |
| Other financial assets | 5.5(g) | **134** | 152 |
| Exploration and evaluation assets | 3.1 | **459** | 495 |
| Oil and gas assets | 3.2 | **9,536** | 10,398 |
| Other land, buildings, plant and equipment | | **126** | 135 |
| Deferred tax assets | 2.4(d) | **1,419** | 1,054 |
| **Total non-current assets** | | **11,734** | 12,312 |
| **Total assets** | | **13,706** | 15,262 |
| **Current liabilities** | | | |
| Trade and other payables | 4.4 | **495** | 520 |
| Deferred income | | **8** | 23 |
| Interest-bearing loans and borrowings | 5.1 | **207** | 420 |
| Current tax liabilities | | **17** | 3 |
| Provisions | 3.4 | **142** | 121 |
| Other financial liabilities | 5.5(g) | **82** | 366 |
| Liabilities directly associated with assets held for sale | | **–** | 103 |
| **Total current liabilities** | | **951** | 1,556 |
| **Non-current liabilities** | | | |
| Deferred income | | **114** | 99 |
| Interest-bearing loans and borrowings | 5.1 | **3,736** | 4,819 |
| Deferred tax liabilities | 2.4(d) | **240** | 221 |
| Provisions | 3.4 | **1,494** | 1,464 |
| Other financial liabilities | 5.5(g) | **20** | 23 |
| **Total non-current liabilities** | | **5,604** | 6,626 |
| **Total liabilities** | | **6,555** | 8,182 |
| **Net assets** | | **7,151** | 7,080 |
| **Equity** | | | |
| Issued capital | 5.3 | **9,034** | 8,883 |
| Reserves | 5.4 | **51** | (510) |
| Accumulated losses | 5.4 | **(1,934)** | (1,293) |
| Equity attributable to owners of Santos Limited | | **7,151** | 7,080 |
| **Total equity** | | **7,151** | 7,080 |

The consolidated statement of financial position is to be read in conjunction with the notes to the consolidated financial statements.

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# Consolidated Statement of Cash Flows
for the year ended 31 December 2017

| | Note | 2017 US$million | 2016 US$million |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Receipts from customers | | **3,217** | 2,708 |
| Dividends received | | **12** | 12 |
| Pipeline tariffs and other receipts | | **66** | 60 |
| Payments to suppliers and employees | | **(1,611)** | (1,600) |
| Restoration expenditure | | **(37)** | (17) |
| Exploration and evaluation seismic and studies | | **(71)** | (68) |
| Royalty and excise paid | | **(57)** | (34) |
| Borrowing costs paid | | **(254)** | (226) |
| Income taxes paid | | **(28)** | (17) |
| Royalty-related taxes paid | | **(15)** | (4) |
| Other operating activities | | **26** | 26 |
| **Net cash provided by operating activities** | 4.1(b) | **1,248** | 840 |
| **Cash flows from investing activities** | | | |
| Payments for: | | | |
| Exploration and evaluation assets | | **(146)** | (128) |
| Oil and gas assets | | **(483)** | (500) |
| Other land, buildings, plant and equipment | | **(5)** | (4) |
| Acquisitions of oil and gas assets | | **(49)** | (18) |
| Proceeds from disposal of non-current assets | 2.7 | **145** | 447 |
| Borrowing costs paid | | **(6)** | (20) |
| Other investing activities | | **10** | 18 |
| **Net cash used in investing activities** | | **(534)** | (205) |
| **Cash flows from financing activities** | | | |
| Dividends paid | | **–** | (43) |
| Drawdown of borrowings | | **783** | – |
| Repayment of borrowings | | **(2,442)** | (147) |
| Net proceeds from issues of ordinary shares | | **149** | 733 |
| Purchase of shares on-market (Treasury shares) | | **(8)** | – |
| **Net cash provided by financing activities** | | **(1,518)** | 543 |
| **Net (decrease)/increase in cash and cash equivalents** | | **(804)** | 1,178 |
| **Cash and cash equivalents at the beginning of the period** | | **2,026** | 839 |
| Effects of exchange rate changes on the balances of cash held in foreign currencies | | **9** | 9 |
| **Cash and cash equivalents at the end of the period** | 4.1 | **1,231** | 2,026 |

The consolidated statement of cash flows is to be read in conjunction with the notes to the consolidated financial statements.

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# Consolidated Statement of Changes in Equity
for the year ended 31 December 2017

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| | | Equity attributable to owners of Santos Limited | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Note | Issued capital US$million | Translation reserve US$million | Hedging reserve US$million | Financial liabilities at FVOCI US$million | Accumulated profits reserve US$million | Accumulated losses/ Retained earnings US$million | Total equity US$million |
| Balance at 1 January 2016 | | 8,119 | (808) | (12) | – | 121 | 1 | 7,421 |
| Transfer retained profits to accumulated profits reserve | 5.4 | – | – | – | – | 258 | (258) | – |
| *Items of comprehensive income:* | | | | | | | | |
| Loss for the period | | – | – | – | – | – | (1,047) | (1,047) |
| Other comprehensive (loss)/income for the period | | – | (22) | 19 | – | – | 1 | (2) |
| Total comprehensive (loss)/income for the period | | – | (22) | 19 | – | – | (1,046) | (1,049) |
| *Transactions with owners in their capacity as owners:* | | | | | | | | |
| Shares issued | 5.3 | 764 | – | – | – | – | – | 764 |
| Dividends to shareholders | 2.6 | – | – | – | – | (66) | – | (66) |
| Share-based payment transactions | 7.2 | – | – | – | – | – | 10 | 10 |
| **Balance at 31 December 2016** | | 8,883 | (830) | 7 | – | 313 | (1,293) | 7,080 |
| Opening balance adjustment on adoption of new accounting standard (refer note 8.5) | | – | – | – | – | – | (5) | (5) |
| **Balance at 1 January 2017** | | **8,883** | **(830)** | **7** | **–** | **313** | **(1,298)** | **7,075** |
| Transfer retained profits to accumulated profits reserve | 5.4 | **–** | **–** | **–** | **–** | **282** | **(282)** | **–** |
| *Items of comprehensive income:* | | | | | | | | |
| Loss for the period | | **–** | **–** | **–** | **–** | **–** | **(360)** | **(360)** |
| Other comprehensive income/(loss) for the period | | **–** | **302** | **(2)** | **(21)** | **–** | **–** | **279** |
| Total comprehensive income/(loss) for the period | | **–** | **302** | **(2)** | **(21)** | **–** | **(360)** | **(81)** |
| *Transactions with owners in their capacity as owners:* | | | | | | | | |
| Shares issued | 5.3 | **151** | **–** | **–** | **–** | **–** | **–** | **151** |
| On-market share purchase (Treasury shares) | 5.3 | **(8)** | **–** | **–** | **–** | **–** | **–** | **(8)** |
| Share-based payment transactions | 7.2 | **8** | **–** | **–** | **–** | **–** | **6** | **14** |
| **Balance at 31 December 2017** | | **9,034** | **(528)** | **5** | **(21)** | **595** | **(1,934)** | **7,151** |

The consolidated statement of changes in equity is to be read in conjunction with the notes to the consolidated financial statements.

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# Notes to the Consolidated Financial Statements for the year ended 31 December 2017
# Section 1: Basis of Preparation

This section provides information about the basis of preparation of the financial report, and certain accounting policies that are not disclosed elsewhere in the financial report. Accounting policies specific to individual elements of the financial statements are located within the relevant section of the report.

## 1.1 STATEMENT OF COMPLIANCE

The consolidated financial report of Santos Limited ("the Company") for the year ended 31 December 2017 was authorised for issue in accordance with a resolution of the Directors on 20 February 2018.

The consolidated financial report of the Company for the year ended 31 December 2017 comprises the Company and its controlled entities ("the Group"). Santos Limited ("the Parent") is a company limited by shares incorporated in Australia, whose shares are publicly traded on the Australian Securities Exchange ("ASX"), and is the ultimate parent entity in the Group. The Group is a for-profit entity for the purpose of preparing the financial report. The nature of the operations and principal activities of the Group are described in the Directors' Report.

This consolidated financial report is:

- a general purpose financial report which has been prepared in accordance with the requirements of the *Corporations Act 2001* (Cth), Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board ("AASB");
- compliant with Australian Accounting Standards as issued by the AASB and International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board, including new and amended accounting standards issued and effective for reporting periods beginning on or after 1 January 2017;
- presented in United States dollars ("US$");
- prepared on the historical cost basis except for derivative financial instruments, fixed-rate notes that are hedged by an interest rate swap or a cross-currency swap, and financial assets not recorded at amortised cost, which are measured at fair value; and
- rounded to the nearest million dollars, unless otherwise stated, in accordance with ASIC Corporations (Rounding in Financial/ Directors' Reports) Instrument 2016/191.

## 1.2 KEY EVENTS IN THE CURRENT PERIOD

The financial position and performance of the Group was particularly impacted by the following events and transactions during the year:

- production of 59.5 mmboe (2016: 61.6 mmboe), and sales of 83.4 mmboe (2016: 84.1 mmboe);
- sale of non-core assets resulting in $145 million in proceeds with a gain on disposal of $79 million;
- average realised oil price of $57.85 per barrel compared to $46.43 per barrel in 2016;
- issue of US$800 million 10-year Reg-S bond in August 2017;
- redemption of €1 billion Subordinated Notes, redeemed on first call in September 2017;
- net debt reduced to $2,731 million at 31 December 2017, from $3,492 million at 31 December 2016; and
- completion of the 2016 Share Purchase Plan during February 2017, resulting in an increase in issued capital of $153 million, less issue costs of $2 million.

# Notes to the Consolidated Financial Statements
# Section 1: Basis of Preparation

## 1.3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The carrying amounts of certain assets and liabilities are often determined based on management's judgement regarding estimates and assumptions of future events. The key judgements, estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of certain assets and liabilities within the next annual reporting period are disclosed in the following notes:

- Note 2.4 Taxation
- Note 3.1 Exploration and evaluation assets
- Note 3.2 Oil and gas assets – Estimates of reserve quantities
- Note 3.3 Impairment of non-current assets
- Note 3.4 Restoration obligations and other provisions

In addition to the significant judgements referenced above, other areas of estimation and judgement are highlighted throughout the financial report.

## 1.4 FOREIGN CURRENCY

### Functional and presentation currency

The Group's financial statements are presented in United States dollars ("US$"), as that presentation currency most reliably reflects the global business performance of the Group as a whole and is more comparable with our peers.

The functional currency of the Parent is Australian dollars ("A$").

The assets, liabilities, income and expenses of non-US dollar denominated functional operations are translated into US dollars using the following applicable exchange rates:

| Foreign currency amount | Applicable exchange rate |
|---|---|
| Income and expenses | Average rate prevailing for the relevant period |
| Assets and liabilities | Period-end rate |
| Equity | Historical rate |
| Reserves | Historical and period-end rate |
| Statement of cash flows | Average rate prevailing for the relevant period |

Foreign exchange differences resulting from translation to presentation currency are initially recognised in the foreign currency translation reserve and subsequently transferred to the income statement on disposal of the operation.

The period-end exchange rate used was A$/US$ 1:0.7809 (2016: 1:0.7221).

### Transactions and balances

Transactions in currencies other than an entity's functional currency are initially recorded in the functional currency by applying the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in currencies other than an entity's functional currency are retranslated at the foreign exchange rate ruling at the reporting date. Foreign exchange differences arising on translation are recognised in the income statement.

Foreign exchange differences that arise on the translation of monetary items that form part of the net investment in a foreign operation are recognised in the translation reserve in the consolidated financial statements.

Non-monetary assets and liabilities that are measured in terms of historical cost in currencies other than an entity's functional currency are translated using the exchange rate at the date of the initial transaction. Non-monetary assets and liabilities denominated in currencies other than an entity's functional currency that are stated at fair value are translated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined.

### Group companies

The results of subsidiaries with a functional currency other than Australian dollars (the functional currency of the Parent) are translated to Australian dollars as at the date of each transaction. The assets and liabilities are translated to Australian dollars at foreign exchange rates ruling at the reporting date. Foreign exchange differences arising on retranslation are recognised directly in the translation reserve.

Exchange differences arising from the translation of the net investment in foreign operations and of related hedges are recognised in the translation reserve. They are released into the income statement upon disposal of the foreign operation.

Also refer to note 5.5(c) Foreign currency risk for further details on the net investment hedge in place.



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# Notes to the Consolidated Financial Statements
# **Section 2: Financial Performance**

This section focuses on the operating results and financial performance of the Group. It includes disclosures of segmental financial information, taxes, dividends and earnings per share, including the relevant accounting policies adopted in each area.

## 2.1 SEGMENT INFORMATION

The Group has identified its operating segments to be the five key assets/operating areas of the Cooper Basin, Queensland, Papua New Guinea ("PNG"), Northern Australia, and Western Australia ("WA") Gas, based on the nature and geographical location of the assets, plus "Other" non-core assets. This is the basis on which internal reports are provided to the Chief Executive Officer for assessing performance and determining the allocation of resources within the Group.

Segment performance is measured based on earnings before interest, tax, impairment, exploration and evaluation, depletion, depreciation and amortisation ("EBITDAX"). Corporate and exploration expenditure and inter-segment eliminations are included in the segment disclosure for reconciliation purposes.

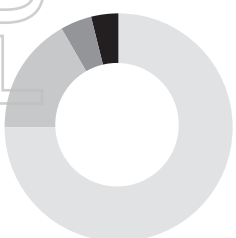
# Notes to the Consolidated Financial Statements
# Section 2: Financial Performance

## 2.1 SEGMENT INFORMATION (CONTINUED)

| US$million | Cooper Basin 2017 | Queensland 2017 | PNG 2017 | Northern Australia 2017 | WA Gas 2017 | Other 2017 | Corporate, exploration, eliminations 2017 | Total 2017 |
|---|---|---|---|---|---|---|---|---|
| **Revenue** | | | | | | | | |
| Sales to external customers | 754 | 731 | 526 | 153 | 242 | 339 | 362 | 3,107 |
| Inter-segment sales[1] | 50 | 27 | – | – | – | 2 | (79) | – |
| Other revenue from external customers | 29 | 6 | 6 | – | 20 | 5 | (1) | 65 |
| **Total segment revenue** | **833** | **764** | **532** | **153** | **262** | **346** | **282** | **3,172** |
| **Costs** | | | | | | | | |
| Production costs | (134) | (68) | (55) | (75) | (54) | (123) | 28 | (481) |
| Other operating costs | (88) | (73) | (46) | – | (20) | (13) | (70) | (310) |
| Third-party product purchases | (200) | (275) | (1) | – | – | – | (220) | (696) |
| Inter-segment purchases[1] | (1) | (34) | – | – | – | – | 35 | – |
| Other | (82) | 15 | – | 9 | 13 | 13 | (225) | (257) |
| **EBITDAX** | **328** | **329** | **430** | **87** | **201** | **223** | **(170)** | **1,428** |
| Depreciation and depletion | (194) | (196) | (113) | (54) | (78) | (82) | (25) | (742) |
| Exploration and evaluation expensed | – | – | – | – | – | – | (94) | (94) |
| Net impairment reversal/(loss) | 479 | (1,238) | – | – | – | (170) | (9) | (938) |
| Change in future restoration assumptions | – | 5 | 1 | – | – | 25 | – | 31 |
| **EBIT** | **613** | **(1,100)** | **318** | **33** | **123** | **(4)** | **(298)** | **(315)** |
| Net finance costs | | | | | | | (270) | (270) |
| Loss before tax | | | | | | | | (585) |
| Income tax benefit | | | | | | | 211 | 211 |
| Royalty-related tax benefit/(expense) | 5 | 2 | – | 3 | (29) | 10 | 23 | 14 |
| **Net loss** | | | | | | | | **(360)** |
| **Asset additions and acquisitions:** | | | | | | | | |
| Exploration and evaluation assets | 11 | 8 | – | 44 | – | 21 | 58 | 142 |
| Oil and gas assets[2] | 146 | 196 | 9 | (5) | 84 | 16 | – | 446 |
| | **157** | **204** | **9** | **39** | **84** | **37** | **58** | **588** |

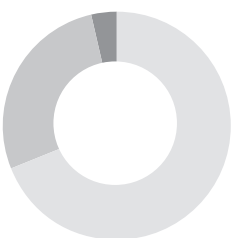
1. Inter-segment pricing is determined on an arm's length basis. Inter-segment sales and purchases are eliminated on consolidation.
2. Includes impact on restoration assets following changes in future restoration provision assumptions (refer note 3.4).

**2017 Revenue from external customers by geographical location US$million**



| | |
|---|---|
| Australia | 2,384 |
| Papua New Guinea | 532 |
| Vietnam | 138 |
| Indonesia | 118 |
| Total | 3,172 |

**2017 Non-current assets by geographical location (excluding financial and deferred tax assets) US$million**



| | |
|---|---|
| Australia | 7,020 |
| Papua New Guinea | 2,784 |
| Other countries | 360 |
| Total | 10,164 |

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## 2.1 SEGMENT INFORMATION (CONTINUED)

| US$million | Cooper Basin 2016 | Queensland 2016 | PNG 2016 | Northern Australia 2016 | WA Gas 2016 | Other 2016 | Corporate, exploration, eliminations 2016 | Total 2016 |
|---|---|---|---|---|---|---|---|---|
| **Revenue** | | | | | | | | |
| Sales to external customers | 716 | 521 | 439 | 145 | 184 | 405 | 184 | 2,594 |
| Inter-segment sales[1] | 33 | 13 | – | – | – | 4 | (50) | – |
| Other revenue from external customers | 19 | 6 | 5 | – | – | 2 | 1 | 33 |
| **Total segment revenue** | **768** | **540** | **444** | **145** | **184** | **411** | **135** | **2,627** |
| **Costs** | | | | | | | | |
| Production costs | (160) | (61) | (56) | (73) | (46) | (166) | 42 | (520) |
| Other operating costs | (77) | (74) | (38) | – | (5) | (16) | (116) | (326) |
| Third-party product purchases | (201) | (142) | (1) | – | – | (3) | (197) | (544) |
| Inter-segment purchases[1] | (18) | (75) | – | – | – | – | 93 | – |
| Other | (54) | 3 | 1 | 14 | 73 | 20 | (95) | (38) |
| **EBITDAX** | **258** | **191** | **350** | **86** | **206** | **246** | **(138)** | **1,199** |
| Depreciation and depletion | (178) | (192) | (105) | (46) | (72) | (114) | (34) | (741) |
| Exploration and evaluation expensed | – | – | – | – | – | – | (138) | (138) |
| Net impairment (loss)/reversal | (49) | (1,500) | – | – | – | 54 | (66) | (1,561) |
| Change in future restoration assumptions | – | – | – | – | – | 37 | – | 37 |
| **EBIT** | **31** | **(1,501)** | **245** | **40** | **134** | **223** | **(376)** | **(1,204)** |
| Net finance costs | | | | | | | (281) | (281) |
| Loss before tax | | | | | | | | (1,485) |
| Income tax benefit | | | | | | | 445 | 445 |
| Royalty-related tax benefit/(expense) | 2 | (3) | – | (4) | (18) | (7) | 23 | (7) |
| **Net loss** | | | | | | | | **(1,047)** |
| **Asset additions and acquisitions:** | | | | | | | | |
| Exploration and evaluation assets | 9 | 1 | – | 2 | 10 | 37 | 94 | 153 |
| Oil and gas assets[2] | 37 | 241 | 14 | 36 | 75 | (33) | – | 370 |
| | **46** | **242** | **14** | **38** | **85** | **4** | **94** | **523** |

1. Inter-segment pricing is determined on an arm's length basis. Inter-segment sales and purchases are eliminated on consolidation.
2. Includes impact on restoration assets following changes in future restoration provision assumptions (refer note 3.4).

**2016 Revenue from external customers by geographical location US$million**



| | |
|---|---|
| Australia | 1,923 |
| Papua New Guinea | 443 |
| Indonesia | 138 |
| Vietnam | 123 |
| Total | 2,627 |

**2016 Non-current assets by geographical location (excluding financial and deferred tax assets) US$million**



| | |
|---|---|
| Australia | 7,622 |
| Papua New Guinea | 2,840 |
| Other countries | 622 |
| Total | 11,084 |

# Notes to the Consolidated Financial Statements
# Section 2: Financial Performance

## 2.2 REVENUE

Revenue is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue is recognised and measured at the fair value of the consideration or contributions received, net of goods and services tax or similar taxes, to the extent it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured.

### Sales revenue

Sales revenue is recognised on the basis of the Group's interest in a producing field ("entitlements" method), when the physical product and associated risks and rewards of ownership pass to the purchaser, which is generally at the time of ship or truck loading, or on the product entering the pipeline.

Revenue earned under a production sharing contract ("PSC") is recognised on a net entitlements basis according to the terms of the PSC. Generally, under these terms the local government retains title to the resources, and is therefore entitled to its share of the production and revenue, after allowing for the joint venture partners to extract and sell their share of hydrocarbons to recover specified costs and a profit margin.

During the year, revenue from one customer amounted to $358 million (2016: $324 million), arising from sales from two segments of the Group.

### Deferred income

A liability is recorded for obligations under sales contracts to deliver natural gas in future periods for which payment has already been received.

| **Sales revenue** | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Product sales:** | | |
| Gas, ethane and liquefied natural gas | **2,205** | 1,784 |
| Crude oil | **579** | 575 |
| Condensate and naphtha | **235** | 183 |
| Liquefied petroleum gas | **88** | 52 |
| **Total product sales**[1] | **3,107** | 2,594 |

1. Total product sales include third-party product sales of $926 million (2016: $643 million).

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## 2.3 EXPENSES

| | 2017 US$million | 2016 US$million |
|---|---|---|
| **Cost of sales:** | | |
| Production costs: | | |
| Production expenses | **412** | 469 |
| Production facilities operating leases | **69** | 51 |
| Total production costs | **481** | 520 |
| Other operating costs: | | |
| LNG plant costs | **63** | 58 |
| Pipeline tariffs, processing tolls and other | **181** | 174 |
| Fair value (gains)/losses on onerous pipeline contracts | **(16)** | 29 |
| Royalty and excise | **64** | 43 |
| Shipping costs | **18** | 22 |
| Total other operating costs | **310** | 326 |
| Total cash cost of production | **791** | 846 |
| Depreciation of plant, equipment and buildings | **472** | 463 |
| Depletion of subsurface assets | **268** | 273 |
| Total depreciation and depletion | **740** | 736 |
| Third-party product purchases | **696** | 544 |
| Decrease in product stock | **45** | 27 |
| **Total cost of sales** | **2,272** | 2,153 |
| **Other expenses:** | | |
| Selling | **18** | 19 |
| Corporate | **84** | 88 |
| Depreciation | **2** | 5 |
| Foreign exchange losses/(gains) | **153** | (34) |
| Fair value hedges, (gains)/losses: | | |
| On the hedging instrument | **43** | 59 |
| On the hedged item attributable to the hedged risk | **(57)** | (19) |
| Fair value losses on commodity derivatives (oil hedges) | **63** | 14 |
| Exploration and evaluation expensed | **94** | 138 |
| Other | **11** | 14 |
| **Total other expenses** | **411** | 284 |

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# Notes to the Consolidated Financial Statements
# Section 2: Financial Performance

## 2.4 TAXATION

### Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except in relation to items recognised directly in equity.

Current tax is the amount of income tax payable on the taxable profit or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from, or paid to, the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date in the countries where the Group operates and generates taxable income.

The Company and all of its wholly-owned Australian resident entities are part of a tax-consolidated group under Australian taxation law. Santos Limited is the head entity in the tax-consolidated group. The head entity and the controlled entities in the tax-consolidated group continue to account for their own current and deferred tax amounts. Current tax liabilities and assets and deferred tax assets arising from unused tax losses and tax credits of the members of the tax-consolidated group are recognised by the Company (as head entity in the tax-consolidated group).

The Company and the other entities in the tax-consolidated group have entered into a tax funding agreement and a tax sharing agreement.

### Royalty-related tax

Petroleum Resource Rent Tax ("PRRT"), Resource Rent Royalty and Timor-Leste's Additional Profits Tax are accounted for as income tax.

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## 2.4 TAXATION (CONTINUED)

Current income tax and royalty-related tax recognised in the income statement for the Group are as follows:

| | 2017 US$million | 2016 US$million |
|---|---|---|
| **(a) Income tax expense/(benefit)** | | |
| *Current tax expense/(benefit)* | | |
| Current year | **144** | 86 |
| Adjustments for prior years | **(5)** | (12) |
| | **139** | 74 |
| *Deferred tax benefit* | | |
| Origination and reversal of temporary differences | **(336)** | (510) |
| Adjustments for prior years | **(14)** | (9) |
| | **(350)** | (519) |
| **Total income tax benefit** | **(211)** | (445) |
| **(b) Royalty-related tax expense** | | |
| *Current tax expense* | | |
| Current year | **9** | 14 |
| | **9** | 14 |
| *Deferred tax benefit* | | |
| Origination and reversal of temporary differences | **(23)** | (7) |
| | **(23)** | (7) |
| **Total royalty-related tax (benefit)/expense** | **(14)** | 7 |
| **(c) Numerical reconciliation between pre-tax net loss and tax benefit** | | |
| Loss before tax | **(585)** | (1,485) |
| Prima facie income tax benefit at 30% (2016: 30%) | **(176)** | (446) |
| (Decrease)/increase in income tax (benefit)/expense due to: | | |
| Foreign losses not recognised | **51** | (2) |
| Non-deductible expenses | **5** | 3 |
| Exchange and other translation variations | **(71)** | 14 |
| Tax adjustments relating to prior years | **(19)** | (21) |
| Other | **(1)** | 7 |
| Income tax benefit | **(211)** | (445) |
| Royalty-related tax (benefit)/expense | **(14)** | 7 |
| **Total tax benefit** | **(225)** | (438) |

# Notes to the Consolidated Financial Statements
# Section 2: Financial Performance

## 2.4 TAXATION (CONTINUED)

### (d) Deferred tax assets and liabilities

Deferred tax is determined using the statement of financial position approach, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the appropriate tax bases.

The following temporary differences are not provided for:

- the initial recognition of assets or liabilities that affect neither accounting or taxable profit; nor
- differences relating to investments in subsidiaries to the extent it is probable that they will not reverse in the foreseeable future.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date.

***Significant judgement – Deferred taxes recognised***

The calculation of the Group's tax charge involves a degree of estimation and judgement in respect of certain items for which the ultimate tax determination is uncertain.

The Group recognises deferred tax assets only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Future taxable profits are estimated by internal budgets and forecasts. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

| | Assets | | Liabilities | | Net | |
|---|---|---|---|---|---|---|
| **Recognised deferred tax assets and liabilities** | **2017 US$million** | 2016 US$million | **2017 US$million** | 2016 US$million | **2017 US$million** | 2016 US$million |
| Exploration and evaluation assets | **49** | 28 | **(46)** | (66) | **3** | (38) |
| Oil and gas assets | **116** | 15 | **–** | – | **116** | 15 |
| Other assets | **75** | 10 | **(115)** | (46) | **(40)** | (36) |
| Derivative financial instruments | **6** | 85 | **–** | – | **6** | 85 |
| Interest-bearing loans and borrowings | **66** | 162 | **–** | – | **66** | 162 |
| Provisions | **51** | 82 | **–** | – | **51** | 82 |
| Royalty-related tax | **–** | – | **(15)** | (60) | **(15)** | (60) |
| Other items | **–** | – | **(54)** | (37) | **(54)** | (37) |
| Tax value of carry-forward losses recognised | **1,046** | 660 | **–** | – | **1,046** | 660 |
| Tax assets/(liabilities) | **1,409** | 1,042 | **(230)** | (209) | **1,179** | 833 |
| Set-off of tax | **10** | 12 | **(10)** | (12) | **–** | – |
| **Net tax assets/(liabilities)** | **1,419** | 1,054 | **(240)** | (221) | **1,179** | 833 |

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## 2.4 TAXATION (CONTINUED)

***Accounting judgement and estimate – Deferred taxes unrecognised***

Deferred tax assets have not been recognised in respect of the following items set out below, because it is not probable that the temporary differences will reverse in the future and that there will be sufficient future taxable profits against which the benefits can be utilised. Tax losses of $65 million (2016: $64 million) will expire between 2021 and 2028. The remaining deductible temporary differences and tax losses do not expire under current tax legislation.

| **Unrecognised deferred tax assets** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Deferred tax assets have not been recognised in respect of the following items: | | |
| Temporary differences in relation to investments in subsidiaries | **4,705** | 5,705 |
| Deductible temporary differences relating to royalty-related tax (net of income tax) | **5,751** | 5,284 |
| Other deductible temporary differences | **162** | 128 |
| Tax losses | **327** | 373 |
| | **10,945** | 11,490 |

## 2.5 EARNINGS PER SHARE

Basic earnings per share amounts are calculated by dividing net profit or loss for the year attributable to ordinary equity holders of Santos Limited by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by adjusting basic earnings per share by the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

Earnings used in the calculation of basic and diluted earnings per share reconciles to the net profit or loss after tax in the income statement as follows:

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Earnings used in the calculation of basic and diluted earnings per share | **(360)** | (1,047) |

The weighted average number of shares used for the purpose of calculating diluted earnings per share reconciles to the number used to calculate basic earnings per share as follows:

| | **2017 Number of shares** | 2016 Number of shares |
|---|---|---|
| Basic earnings per share | **2,078,858,067** | 1,797,896,876 |
| Dilutive potential ordinary shares[1] | **–** | – |
| Diluted earnings per share | **2,078,858,067** | 1,797,896,876 |

| **Earnings per share attributable to the equity holders of Santos Limited** | **2017 ¢** | 2016 ¢ |
|---|---|---|
| Basic earnings per share | **(17.3)** | (58.2) |
| Diluted earnings per share | **(17.3)** | (58.2) |

1. Due to a net loss after tax in 2017 and 2016, potential ordinary shares are anti-dilutive and therefore excluded from the calculation of diluted earnings per share.

# Notes to the Consolidated Financial Statements
# Section 2: Financial Performance

## 2.6 DIVIDENDS

Dividends are recognised as a liability at the time the Directors resolve to pay or declare the dividend.

| Dividends recognised during the year | Dividend per share US¢ | Total US$million |
|---|---|---|
| **2017** | | |
| No dividends were recognised during 2017. | | |
| 2016 | | |
| Final 2015 ordinary – paid 30 March 2016 (A$0.05) | 4 | 66 |
| | 4 | 66 |

| Dividends declared in respect of the year |
|---|
| **2017** |
| No dividends were declared in respect of 2017. |
| 2016 |
| No dividends were declared in respect of 2016. |

| Dividend franking account | 2017 US$million | 2016 US$million |
|---|---|---|
| 30% franking credits available to the shareholders of Santos Limited for future distribution, after adjusting for franking credits which will arise from the refund of the current tax receivable at 31 December | **399** | 363 |

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## 2.7 OTHER INCOME

Other income is recognised at the fair value of the consideration received or receivable, when significant risks and rewards have been transferred to the buyer or when the service has been performed.

Gain or loss arising on disposal of a non-current asset is included as other income at the date control of the asset passes to the buyer.

| | Note | **2017 US$million** | 2016 US$million |
|---|---|---|---|
| **Other income** | | | |
| Liquidated damages of gas sales agreement | | **–** | 69 |
| Change in future restoration assumptions | 3.4 | **31** | 37 |
| Gain on sale of non-current assets | | **79** | 25 |
| Insurance proceeds | | **–** | 10 |
| Other | | **13** | 16 |
| **Total other income** | | **123** | 157 |
| **Net gain on sale of non-current assets:** | | | |
| Proceeds on disposals | | **145** | 447 |
| *Adjusted for:* | | | |
| Book value of exploration and evaluation assets disposed | | **2** | – |
| Book value of oil and gas assets disposed | | **(62)** | (162) |
| Book value of other land, buildings, plant and equipment disposed | | **(4)** | (5) |
| Book value of working capital disposed | | **(2)** | (255) |
| **Total net gain on sale of non-current assets** | | **79** | 25 |
| **Comprising:** | | | |
| Net gain/(loss) on sale of exploration and evaluation assets | | **10** | (2) |
| Net gain on sale of oil and gas assets | | **60** | 13 |
| Net (loss)/gain on sale of other land, buildings, plant and equipment | | **(1)** | 8 |
| Net gain on liquidation of controlled entities | | **10** | 6 |
| | | **79** | 25 |
| **Reconciliation to cash inflows from proceeds on disposal of non-current assets:** | | | |
| Proceeds after recoupment of current year exploration and evaluation expenditure | | **145** | 447 |
| Amounts receivable | | **–** | – |
| Amounts received from disposals | | **145** | 447 |
| **Total proceeds on disposal of non-current assets** | | **145** | 447 |
| **Comprising:** | | | |
| Proceeds from disposal of exploration and evaluation assets | | **3** | – |
| Proceeds from disposal of oil and gas assets | | **134** | 432 |
| Proceeds from disposal of other land, buildings, plant and equipment | | **8** | 15 |
| | | **145** | 447 |

# Notes to the Consolidated Financial Statements
# Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

This section includes information about the assets used by the Group to generate profits and revenue, specifically information relating to exploration and evaluation assets, oil and gas assets, associated restoration obligations, and commitments for capital expenditure not yet recognised as a liability.

The life cycle of the Group's assets is summarised as follows:




## 3.1 EXPLORATION AND EVALUATION ASSETS

### Exploration and evaluation expenditure

Exploration and evaluation activity involves the search for hydrocarbon resources, the determination of technical feasibility and the assessment of commercial viability of an identified resource. Expenditure in respect of each area of interest is accounted for using the successful efforts method of accounting.

The successful efforts method requires all exploration and evaluation expenditure to be expensed in the period it is incurred, except the costs of acquiring interests in new exploration and evaluation assets, the cost of successful wells and appraisal costs relating to determining development feasibility, which are capitalised as intangible exploration and evaluation assets.

Exploration and evaluation expenditure is recognised in relation to an area of interest when the rights to tenure of the area of interest are current and either:

- such expenditure is expected to be recovered through successful development and commercial exploitation of the area of interest or, alternatively, by its sale; or
- the exploration activities in the area of interest have not yet reached a stage that permits reasonable assessment of the existence of economically recoverable reserves and active and significant operations in, or in relation to, the area of interest are continuing.

Where an ownership interest in an exploration and evaluation asset is exchanged for another, the transaction is recognised by reference to the carrying value of the original interest. Any cash consideration paid, including transaction costs, is accounted for as an acquisition of exploration and evaluation assets. Any cash consideration received, net of transaction costs, is treated as a recoupment of costs previously capitalised with any excess accounted for as a gain on disposal of non-current assets.

No amortisation is charged during the exploration and evaluation phase.

### Acquisition of assets

All assets acquired are recorded at their cost of acquisition, being the amount of cash or cash equivalents paid, and the fair value of assets given, shares issued or liabilities incurred. The cost of an asset comprises the purchase price including any incidental costs directly attributable to the acquisition, any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating, and the estimate of the costs of dismantling and removing the asset and restoring the site on which it is located.

Exploration licence and leasehold property acquisition costs are capitalised as intangible assets. Licence costs paid in connection with a right to explore in an existing exploration area are capitalised and amortised over the term of the permit.

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## 3.1 EXPLORATION AND EVALUATION ASSETS (CONTINUED)

***Significant judgement – Exploration and evaluation***

The application of this policy requires management to make certain estimates and assumptions as to future events and circumstances, particularly in relation to the assessment of whether economic quantities of resources have been found. Any such estimates and assumptions may change as new information becomes available. If, after having capitalised exploration and evaluation expenditure, management concludes that the capitalised expenditure is unlikely to be recovered by future exploitation or sale, then the relevant capitalised amount will be impaired through the income statement.

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Cost | **2,012** | 1,805 |
| *Less*: Impairment | **(1,553)** | (1,310) |
| **Balance at 31 December** | **459** | 495 |
| **Reconciliation of movements** | | |
| Balance at 1 January | **495** | 520 |
| Acquisitions | **48** | 37 |
| Additions | **94** | 116 |
| Transfer to assets held for sale | **–** | (28) |
| Expensed | **(17)** | (71) |
| Impairment losses | **(163)** | (59) |
| Transfer to oil and gas assets in development | **–** | (1) |
| Transfer to oil and gas assets in production | **(13)** | (15) |
| Exchange differences | **15** | (4) |
| **Balance at 31 December** | **459** | 495 |
| **Comprising:** | | |
| Acquisition costs | **95** | 150 |
| Successful exploration wells | **253** | 249 |
| Pending determination of success | **111** | 96 |
| | **459** | 495 |

## 3.2 OIL AND GAS ASSETS

Oil and gas assets are usually single oil or gas fields being developed for future production or that are in the production phase. Where several individual oil or gas fields are to be produced through common facilities, the individual oil or gas field and the associated production facilities are managed and reported as a single oil and gas asset.

### Assets in development

When the technical and commercial feasibility of an undeveloped oil or gas field has been demonstrated and approval of commercial development occurs, the field enters its development phase from the exploration and evaluation phase. Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines, and the drilling of development wells, as well as exploration and evaluation costs, are capitalised as tangible assets within oil and gas assets. Other subsurface expenditures include the costs of de-watering coal seam gas fields to provide access to coal seams to enable production from coal seam gas reserves. De-watering costs include the costs of extracting, transporting, treating and disposing of water during the development phase of the coal seam gas fields.

When commercial operation commences, the accumulated costs are transferred to oil and gas producing assets.

# Notes to the Consolidated Financial Statements
# Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

## 3.2 OIL AND GAS ASSETS (CONTINUED)

**Producing assets**

The costs of oil and gas assets in production are separately accounted for as tangible assets and include past exploration and evaluation costs, pre-production development costs and the ongoing costs of continuing to develop reserves for production and to expand or replace plant and equipment and any associated land and buildings.

**Ongoing exploration and evaluation activities**

Often the initial discovery and development of an oil or gas asset will lead to ongoing exploration for, and evaluation of, potential new oil or gas fields in the vicinity with the intention of producing any near-field discoveries using the infrastructure in place.

Exploration and evaluation expenditure associated with oil and gas assets is accounted for in accordance with the policy note in 3.1. Exploration and evaluation amounts capitalised in respect of oil and gas assets are separately disclosed in the table below.

**Depreciation and depletion**

Depreciation charges are calculated to write off the value of buildings, plant and equipment over their estimated economic useful lives to the Group. Each component of an item of buildings, plant and equipment with a cost that is significant in relation to the total cost of the asset is depreciated separately.

Depreciation of onshore buildings, plant and equipment and corporate assets is calculated using the straight-line method of depreciation from the date the asset is available for use, unless a units of production method represents a more reasonable allocation of the asset's depreciable value over its economic useful life.

The estimated useful lives for each class of onshore assets for the current and comparative periods are generally as follows:

- Buildings 20 – 50 years
- Pipelines 10 – 30 years
- Plant and facilities 10 – 50 years

Depreciation of offshore plant and equipment is calculated using the units of production method from the date of commencement of production.



***Significant judgement – Estimates of reserve quantities***

The estimated quantities of Proved plus Probable ("2P") hydrocarbon reserves reported by the Group are integral to the calculation of depletion and depreciation expense and are incorporated into the assessment of impairment of assets. Estimated reserve quantities are based upon interpretations of geological and geophysical models and assessments of the technical feasibility and commercial viability of producing the reserves. These assessments require assumptions to be made regarding future development and production costs, commodity prices, exchange rates and fiscal regimes. The estimates of reserves may change from period to period as the economic assumptions used to estimate the reserves can change from period to period, and as additional geological data is generated during the course of operations. Reserves estimates are prepared in accordance with the Group's policies and procedures for reserves estimation which conform to guidelines prepared by the Society of Petroleum Engineers.

***Accounting judgement and estimate – Depletion charges***

Depletion and certain depreciation charges are calculated using the units of production method. This is based on barrels of oil equivalent which will amortise the cost of carried forward exploration, evaluation and subsurface development expenditure ("subsurface assets") over the life of the estimated 2P hydrocarbon reserves for an asset or group of assets, together with future subsurface costs necessary to develop the hydrocarbon reserves in the respective asset or group of assets.

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## 3.2 OIL AND GAS ASSETS (CONTINUED)

| | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|
| | **Subsurface assets US$million** | **Plant and equipment US$million** | **Total US$million** | Subsurface assets US$million | Plant and equipment US$million | Total US$million |
| Cost | **8,985** | **15,442** | **24,427** | 9,244 | 15,652 | 24,896 |
| *Less*: Accumulated depreciation, depletion and impairment | **(6,847)** | **(8,044)** | **(14,891)** | (7,467) | (7,031) | (14,498) |
| **Balance at 31 December** | **2,138** | **7,398** | **9,536** | 1,777 | 8,621 | 10,398 |
| **Reconciliation of movements** | | | | | | |
| ***Assets in development*** | | | | | | |
| Balance at 1 January | **71** | **19** | **90** | 96 | 941 | 1,037 |
| Additions[1] | **1** | **28** | **29** | 11 | 50 | 61 |
| Transfer from exploration and evaluation assets | **–** | **–** | **–** | 1 | – | 1 |
| Disposals | **–** | **–** | **–** | (2) | – | (2) |
| Transfer to oil and gas assets in production | **(1)** | **(1)** | **(2)** | (35) | (972) | (1,007) |
| Exchange differences | **2** | **–** | **2** | – | – | – |
| **Balance at 31 December** | **73** | **46** | **119** | 71 | 19 | 90 |
| ***Producing assets*** | | | | | | |
| Balance at 1 January | **1,706** | **8,602** | **10,308** | 2,514 | 8,853 | 11,367 |
| Additions[1] | **297** | **120** | **417** | (14) | 323 | 309 |
| Transfer from exploration and evaluation assets | **13** | **–** | **13** | 15 | – | 15 |
| Transfer from oil and gas assets in development | **1** | **1** | **2** | 35 | 972 | 1,007 |
| Disposals | **–** | **(4)** | **(4)** | (10) | (38) | (48) |
| Depreciation and depletion | **(268)** | **(450)** | **(718)** | (272) | (435) | (707) |
| Net impairment reversals/(losses) | **255** | **(1,020)** | **(765)** | (521) | (968) | (1,489) |
| Transfer of assets held for sale | **–** | **–** | **–** | (29) | (97) | (126) |
| Net impairment losses on assets transferred to held for sale | **–** | **–** | **–** | – | (4) | (4) |
| Exchange differences | **61** | **103** | **164** | (12) | (4) | (16) |
| **Balance at 31 December** | **2,065** | **7,352** | **9,417** | 1,706 | 8,602 | 10,308 |
| **Total oil and gas assets** | **2,138** | **7,398** | **9,536** | 1,777 | 8,621 | 10,398 |
| **Comprising:** | | | | | | |
| Exploration and evaluation expenditure pending commercialisation | **90** | **5** | **95** | 202 | 21 | 223 |
| Other capitalised expenditure | **2,048** | **7,393** | **9,441** | 1,575 | 8,600 | 10,175 |
| | **2,138** | **7,398** | **9,536** | 1,777 | 8,621 | 10,398 |

1. Includes impact on restoration assets following changes in future restoration provision assumptions (refer note 3.4).

# Notes to the Consolidated Financial Statements
# Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

## 3.3 IMPAIRMENT OF NON-CURRENT ASSETS

The carrying amounts of the Group's oil and gas assets are reviewed at each reporting date to determine whether there is any indication of impairment. Where an indicator of impairment exists, a formal estimate of the recoverable amount is made.

**Indicators of impairment – Exploration and evaluation assets**

The carrying amounts of the Group's exploration and evaluation assets are reviewed at each reporting date, to determine whether any of the following indicators of impairment exists:

- tenure over the licence area has expired during the period or will expire in the near future, and is not expected to be renewed; or
- substantive expenditure on further exploration for, and evaluation of, mineral resources in the specific area is not budgeted or planned; or
- exploration for, and evaluation of, resources in the specific area have not led to the discovery of commercially viable quantities of resources, and the Group has decided to discontinue activities in the specific area; or
- sufficient data exists to indicate that although a development is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or from sale.

**Cash-generating units – Oil and gas assets**

Oil and gas assets, land, buildings, plant and equipment are assessed for impairment on a cash-generating unit ("CGU") basis. A CGU is the smallest grouping of assets that generates independent cash inflows, and generally represents an individual oil or gas field, or oil and gas fields, that are being produced through a common facility. Impairment losses recognised in respect of CGUs are allocated to reduce the carrying amount of the assets in the CGU on a pro-rata basis.

Individual assets within a CGU may become impaired if their ongoing use changes or if the benefits to be obtained from ongoing use are likely to be less than the carrying value of the individual asset. An impairment loss is recognised in the income statement whenever the carrying amount of an asset or its CGU exceeds its recoverable amount.

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## 3.3 IMPAIRMENT OF NON-CURRENT ASSETS (CONTINUED)

### Recoverable amount

The recoverable amount of an asset or CGU is the greater of its fair value less costs of disposal ("FVLCD") (based on level 3 fair value hierarchy) and its value-in-use ("VIU"), using an asset's estimated future cash flows (as described below) discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

***Significant judgement – Impairment of oil and gas assets***

For oil and gas assets, the expected future cash flow estimation is based on a number of factors, variables and assumptions, the most important of which are estimates of reserves, future production profiles, commodity prices, costs and foreign exchange rates. In most cases, the present value of future cash flows is most sensitive to estimates of future oil price and discount rates.

The estimated future cash flows for the VIU calculation are based on estimates, the most significant of which are hydrocarbon reserves, future production profiles, commodity prices, operating costs including third-party gas purchases and any future development costs necessary to produce the reserves. Under a FVLCD calculation, future cash flows are based on estimates of hydrocarbon reserves in addition to other relevant factors such as value attributable to additional resource and exploration opportunities beyond reserves based on production plans.

Estimates of future commodity prices are based on the Group's best estimate of future market prices with reference to external market analysts' forecasts, current spot prices and forward curves. Future commodity prices are reviewed at least annually. Where volumes are contracted, future prices are based on the contracted price.

Future prices (US$/bbl) used were:

| 2018 | 2019 | 2020 | 2021 | 2022[1] | 2023[1] |
|---|---|---|---|---|---|
| 55.00 | 60.00 | 65.00 | 70.00 | 77.29 | 78.83 |

1. Based on US$70/bbl (2017 real) from 2022 escalated at 2.0% p.a.

Forecasts of the foreign exchange rate for foreign currencies, where relevant, are estimated with reference to observable external market data and forward values, including analysis of broker and consensus estimates. The future estimated rate applied is A$1/US$0.75.

The discount rates applied to the future forecast cash flows are based on the weighted average cost of capital, adjusted for risks where appropriate, including functional currency of the asset, and risk profile of the countries in which the asset operates. The range of pre-tax discount rates that have been applied to non-current assets is between 11% and 14%.

In the event that future circumstances vary from these assumptions, the recoverable amount of the Group's oil and gas assets could change materially and result in impairment losses or the reversal of previous impairment losses.

Due to the interrelated nature of the assumptions, movements in any one variable can have an indirect impact on others and individual variables rarely change in isolation. Additionally, management can be expected to respond to some movements, to mitigate downsides and take advantage of upsides, as circumstances allow. Consequently, it is impracticable to estimate the indirect impact that a change in one assumption has on other variables and hence, on the likelihood, or extent, of impairments, or reversals of impairments, under different sets of assumptions in subsequent reporting periods.

# Notes to the Consolidated Financial Statements
# Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

## 3.3 IMPAIRMENT OF NON-CURRENT ASSETS (CONTINUED)

| Impairment expense | 2017 US$million | 2016 US$million |
|---|---|---|
| **Current assets** | | |
| Assets held for sale | **–** | 4 |
| Other receivables | **5** | – |
| Total impairment of current assets | **5** | 4 |
| **Non-current assets** | | |
| Exploration and evaluation assets | **163** | 59 |
| Oil and gas assets | **765** | 1,489 |
| Land and buildings | **5** | 9 |
| Total impairment of non-current assets | **933** | 1,557 |
| **Total impairment** | **938** | 1,561 |

Recoverable amounts and resulting impairment write-downs/(reversals) recognised in the year ended 31 December 2017 are:

| 2017 | Segment | Subsurface assets US$million | Plant and equipment US$million | Total US$million | Recoverable amount[1] US$million |
|---|---|---|---|---|---|
| ***Exploration and evaluation assets:*** | | | | | |
| Ande Ande Lumut – Indonesia | Other | 149 | – | 149 | nil[2] |
| Gunnedah Basin | Other | 10 | – | 10 | nil[2] |
| Papua New Guinea – PPL 287 | Exploration | 4 | – | 4 | nil[2] |
| Total impairment of exploration and evaluation assets | | 163 | – | 163 | |
| ***Oil and gas assets – producing:*** | | | | | |
| GLNG | Queensland | – | 1,238 | 1,238 | 4,099 |
| Barrow | Other | – | 6 | 6 | nil |
| Cooper – unconventional resources[3] | Cooper Basin | 1 | – | 1 | nil |
| Cooper Basin | Cooper Basin | (256) | (224) | (480) | 1,388 |
| Total impairment of oil and gas assets | | (255) | 1,020 | 765 | |
| **Total impairment of exploration and evaluation and oil and gas assets** | | (92) | 1,020 | 928 | |

1. Recoverable amounts represent the carrying values of assets before deducting the carrying value of restoration liabilities. All producing oil and gas asset amounts are calculated using the VIU method, whilst all exploration and evaluation asset amounts use the FVLCD method.
2. Impairment of exploration and evaluation assets relates to certain individual licences/areas of interest that have been impaired to nil.
3. Cooper – unconventional resources comprises exploration and evaluation expenditure pending commercialisation within oil and gas assets, producing assets. The impairment in the current year relates to Paragoona-ATP 820P.

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## 3.3 IMPAIRMENT OF NON-CURRENT ASSETS (CONTINUED)

### Exploration and evaluation assets

The impairment of Ande Ande Lumut has arisen mainly from the impact of lower oil prices.

### Oil and gas assets

*GLNG*

The impairment of GLNG has arisen mainly due to a reduction in the US$ oil price assumption, combined with a higher discount rate and lower assumed volumes of third-party gas, partially offset by higher assumed equity gas volumes resulting from positive upstream performance and lower costs.

*Cooper Basin*

Whilst the Cooper Basin has been impacted by lower US$ oil price assumptions, this has been more than offset by lower forecast development and operating costs, combined with increased drilling activity and production, resulting in a reversal of impairment.

### Sensitivity analysis

To the extent the CGUs have been written down to their respective recoverable amounts in the current and prior years, any change in key assumptions on which the valuations are based would further impact asset carrying values. When modelled in isolation, it is estimated that changes in the key assumptions would result in the following additional impairments/lower impairment reversals in 2017 for the GLNG and Cooper Basin CGUs, respectively:

| Sensitivity | Production decrease 5% US$million | Discount rate increase 0.50% US$million | Oil price decrease US$5/bbl all years US$million |
|---|---|---|---|
| GLNG | 271 | 219 | 566 |
| Cooper Basin | 222 | 85 | 262 |

As identified above, the impact of changes in key assumptions such as reserves, production levels, commodity prices and discount rates are significant on the determination of recoverable amount. Due to the number of factors that could impact any of these assumptions, as well as any actions taken to respond to adverse changes, actual future determinations of recoverable amount may vary from those stated above.

Recoverable amounts and resulting impairment write-downs/(reversals) recognised in the year ended 31 December 2016 were:

| 2016 | Segment | Subsurface assets US$million | Plant and equipment US$million | Total US$million | Recoverable amount[1] US$million |
|---|---|---|---|---|---|
| ***Exploration and evaluation assets:*** | | | | | |
| Papua New Guinea | Exploration | 56 | – | 56 | nil[2] |
| Vietnam | Other | – | 2 | 2 | nil[2] |
| Gunnedah Basin | Other | – | 1 | 1 | nil[2] |
| Total impairment of exploration and evaluation assets | | 56 | 3 | 59 | |
| ***Oil and gas assets – producing:*** | | | | | |
| GLNG | Queensland | 519 | 981 | 1,500 | 5,487 |
| Cooper – unconventional resources[3] | Cooper Basin | 49 | – | 49 | nil |
| Sampang | Other | – | (5) | (5) | 22 |
| Vietnam (Chim Sáo/Dua) | Other | (47) | (8) | (55) | 135 |
| Total impairment of oil and gas assets | | 521 | 968 | 1,489 | |
| **Total impairment of exploration and evaluation and oil and gas assets** | | 577 | 971 | 1,548 | |

1. Recoverable amounts represent the carrying values of assets before deducting the carrying value of restoration liabilities. All producing oil and gas asset amounts are calculated using the VIU method, whilst all exploration and evaluation asset amounts use the FVLCD method.
2. Impairment of exploration and evaluation assets relates to certain individual licences/areas of interest that have been impaired to nil.
3. Cooper – unconventional resources comprises exploration and evaluation expenditure pending commercialisation within oil and gas assets, producing assets. The impairment relates to the Basin Centered Gas exploration.

# Notes to the Consolidated Financial Statements
# Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

## 3.4 RESTORATION OBLIGATIONS AND OTHER PROVISIONS

Provisions for future removal and environmental restoration costs are recognised where there is a present obligation as a result of exploration, development, production, transportation or storage activities having been undertaken, and it is probable that future outflow of economic benefits will be required to settle the obligation. The estimated future obligations include the costs of removing facilities, abandoning wells and restoring the affected areas and is the best estimate of the present value of the future expenditure required to settle the restoration obligation at the reporting date, based on current legal requirements. Any changes in the estimate are reflected in the present value of the restoration provision at the reporting date, with a corresponding change in the cost of the associated asset. In the event the restoration provision is reduced, the cost of the related oil and gas asset is reduced by an amount not exceeding its carrying value. If the decrease in restoration provision exceeds the carrying amount of the asset, the excess is recognised immediately in the income statement as other income.

The amount of the provision for future restoration costs relating to exploration, development and production facilities is capitalised and depleted as a component of the cost of those activities.

***Significant judgement – Provision for restoration***

The Group estimates the future removal and restoration costs of oil and gas production facilities, wells, pipelines and related assets at the time of installation of the assets and reviews these assessments periodically. In most instances the removal of these assets will occur many years in the future. The estimate of future removal costs therefore requires management to make judgements regarding the removal date, future environmental legislation, and the extent of restoration activities required.

The Group has recorded provisions for restoration obligations as follows:

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Current provision | **85** | 69 |
| Non-current provision | **1,443** | 1,399 |
| | **1,528** | 1,468 |

Movements in the provision during the financial year are set out below:

| | **Total restoration US$million** |
|---|---|
| Balance at 1 January 2017 | **1,468** |
| Provisions made during the year | **9** |
| Provisions used during the year | **(40)** |
| Unwind of discount | **45** |
| Change in discount rate | **(19)** |
| Exchange differences | **65** |
| **Balance at 31 December 2017** | **1,528** |

Payments made into escrow accounts relating to future restoration obligations of $68 million (2016: $62 million) are included within other non-current financial assets (note 5.5(g)).

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## 3.4 RESTORATION OBLIGATIONS AND OTHER PROVISIONS (CONTINUED)

### Other provisions

In addition to the provision for restoration shown above, other items for which a provision has been recorded are:

| | Note | 2017 US$million | 2016 US$million |
|---|---|---|---|
| **Current** | | | |
| Employee benefits | 7.1 | **49** | 45 |
| Onerous lease provisions | | **8** | 7 |
| | | **57** | 52 |
| **Non-current** | | | |
| Employee benefits | 7.1 | **8** | 10 |
| Defined benefit obligations | | **1** | 3 |
| Onerous pipeline contracts | | **42** | 52 |
| | | **51** | 65 |

## 3.5 COMMITMENTS FOR EXPENDITURE

The Group has certain obligations to perform minimum exploration work and expend minimum amounts of money pursuant to the terms of the granting of petroleum exploration permits in order to maintain rights of tenure.

These commitments may be varied as a result of renegotiations of the terms of the exploration permits, licences or contracts or alternatively upon their relinquishment. The minimum exploration commitments are less than the normal level of exploration expenditures expected to be undertaken by the Group.

The Group leases floating production, storage and offtake facilities, floating storage offloading facilities, LNG carriers and mobile offshore production units under operating leases. The leases typically run for a period of four to six years, and may have an option to renew after that time.

The Group also leases building office space and a warehouse under operating leases. The leases are generally for a period of 10 years, with an option to renew the lease after that date. The lease payments typically increase annually by the Consumer Price Index.

During the year ended 31 December 2017, the Group recognised $69 million (2016: $51 million) as an expense in the income statement in respect of operating leases.

The Group has the following commitments for expenditure for which no liabilities have been recorded in the financial statements as the goods or services have not been received, including non-cancellable operating lease rentals:

| | Capital | | Minimum exploration | | Operating lease | |
|---|---|---|---|---|---|---|
| **Commitments** | **2017 US$million** | 2016 US$million | **2017 US$million** | 2016 US$million | **2017 US$million** | 2016 US$million |
| Not later than one year | **124** | 161 | **46** | 80 | **65** | 83 |
| Later than one year but not later than five years | **18** | 14 | **334** | 292 | **128** | 129 |
| Later than five years | **–** | – | **13** | – | **78** | 93 |
| | **142** | 175 | **393** | 372 | **271** | 305 |

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# Notes to the Consolidated Financial Statements
# Section 4: Working Capital Management

This section provides information about the Group's working capital balances and management, including cash flow information. Cash flow management is a significant consideration in running our business in an efficient and resourceful manner. We also consider inventories which contribute to the business platform for generating profits and revenues.

## 4.1 CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash balances and short-term deposits that are readily convertible to cash, are subject to an insignificant risk of changes in value, and generally have an original maturity of three months or less.

The carrying amounts of cash and cash equivalents represent fair value. Bank balances and short-term deposits earn interest at floating rates based upon market rates.

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Cash at bank and in hand | **384** | 392 |
| Short-term deposits | **847** | 1,634 |
| | **1,231** | 2,026 |

### (a) Restricted cash balances

In accordance with the terms of the PNG LNG project financing, cash relating to the Group's interest in undistributed cash flows from the PNG LNG project is required to be held in secured bank accounts. As at 31 December 2017, $135 million (2016: $122 million) was held in these accounts.

| **(b) Reconciliation of cash flows from operating activities** | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Loss after income tax** | **(360)** | (1,047) |
| Add/(deduct) non-cash items: | | |
| Depreciation and depletion | **742** | 741 |
| Exploration and evaluation expensed | **17** | 71 |
| Net impairment loss | **938** | 1,561 |
| Net loss on fair value derivatives | **49** | 54 |
| Share-based payment expense | **10** | 11 |
| Unwind of the effect of discounting on provisions | **45** | 41 |
| Foreign exchange losses/(gains) | **153** | (34) |
| Other | **(107)** | (94) |
| Net cash provided by operating activities before changes in assets or liabilities | **1,487** | 1,304 |
| Add/(deduct) change in operating assets or liabilities, net of acquisitions or disposals of businesses: | | |
| (Increase)/decrease in trade and other receivables | **(62)** | 25 |
| Decrease in inventories | **55** | 15 |
| Decrease in other assets | **14** | 35 |
| Increase in net deferred tax assets | **(292)** | (500) |
| Increase in current tax liabilities | **21** | 75 |
| Increase/(decrease) in trade and other payables | **46** | (82) |
| Decrease in provisions | **(21)** | (15) |
| **Net cash provided by operating activities** | **1,248** | 857 |

### (c) Non-cash financing and investing activities

| | | |
|---|---|---|
| Santos Dividend Reinvestment Plan | **–** | 23 |

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## 4.1 CASH AND CASH EQUIVALENTS (CONTINUED)

### (d) Reconciliation of liabilities arising from financing activities to financing cash flows

| | Short-term borrowings US$million | Long-term borrowings US$million | Finance lease liabilities US$million | Liabilities held to hedge borrowings US$million | Assets held to hedge borrowings US$million | Total US$million |
|---|---|---|---|---|---|---|
| **Balance as at 1 January 2017** | **419** | **4,755** | **65** | **349** | **(84)** | **5,504** |
| Financing cash flows[1] | (432) | (1,010) | – | (217) | – | (1,659) |
| Non-cash changes: | | | | | | |
| Effect of changes in exchange rates | – | 144 | – | (144) | – | – |
| Changes in fair values | (6) | (14) | (2) | 12 | 23 | 13 |
| Reclassification to current liability | 222 | (222) | – | – | – | – |
| Other | 3 | 21 | – | – | – | 24 |
| **Balance as at 31 December 2017** | **206** | **3,674** | **63** | **–** | **(61)** | **3,882** |

1. Financing cash flows consist of the net amount of proceeds from borrowings and repayments of borrowings in the statement of cash flows.

## 4.2 TRADE AND OTHER RECEIVABLES

Trade and other receivables are initially recognised at fair value, which in practice is the equivalent of cost, less any impairment losses.

Long-term receivables are discounted and are stated at amortised cost, less any impairment losses.

Trade receivables are non-interest-bearing and settlement terms are generally within 30 days. Trade receivables that are neither past due nor impaired relate to a number of independent customers for whom there is no recent history of default.

| | 2017 US$million | 2016 US$million |
|---|---|---|
| **Current** | | |
| Trade receivables | **334** | 269 |
| Other receivables | **106** | 98 |
| | **440** | 367 |
| **Non-current** | | |
| Other receivables | **–** | 5 |

Due to the nature of the Group's receivables, their carrying amount is considered to approximate their fair value.

The Group applies the simplified approach to providing for expected credit losses for all trade receivables as set out in note 5.5(e).

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# Notes to the Consolidated Financial Statements
# Section 4: Working Capital Management

## 4.3 INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. Cost is determined as follows:

- drilling and maintenance stocks, which include plant spares, consumables and maintenance and drilling tools used for ongoing operations, are valued at weighted average cost; and
- petroleum products, which comprise extracted crude oil, liquefied petroleum gas, condensate and naphtha stored in tanks and pipeline systems and processed sales gas and ethane stored in subsurface reservoirs, are valued using the absorption cost method.

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Petroleum products | **167** | 219 |
| Drilling and maintenance stocks | **99** | 102 |
| **Total inventories at lower of cost and net realisable value** | **266** | 321 |
| Inventories included above that are stated at net realisable value | **29** | 47 |

## 4.4 TRADE AND OTHER PAYABLES

Trade and other payables are recognised when the related goods or services are received, at the amount of cash or cash equivalents that will be required to discharge the obligation, gross of any settlement discount offered. Trade payables are non-interest-bearing and are settled on normal terms and conditions.

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Trade payables | **416** | 417 |
| Non-trade payables | **79** | 103 |
| | **495** | 520 |

The carrying amounts of trade and other payables are considered to approximate their fair values, due to their short-term nature.

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# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

Our business has exposure to capital, credit, liquidity and market risks. This section provides information relating to our management of, as well as our policies for measuring and managing, these risks.

**Capital risk management objectives**

The Group's objectives when managing capital are to safeguard its ability to continue as a going concern, allowing returns to shareholders and benefits for other stakeholders to be maintained, and to retain an efficient capital structure. In order to optimise the capital structure, the Group may adjust its dividend distribution policy, return capital to shareholders, issue new shares, draw or repay debt or undertake other corporate initiatives consistent with its strategic objectives.

In applying these objectives, the Group aims to:

- minimise the weighted average cost of capital whilst retaining appropriate financial flexibility;
- ensure ongoing access to a range of debt and equity markets; and
- maintain an investment-grade credit rating.

A range of financial metrics are used to monitor the capital structure including ratios measuring gearing, funds from operations to debt ("FFO-to-Debt") and debt to earnings before interest, tax, depreciation and amortisation ("Debt-to-EBITDA"). The Group monitors these capital structure metrics on both an actual and forecast basis.

At 31 December 2017 Santos Limited's corporate credit rating was BBB- (stable outlook) from Standard & Poor's.

## 5.1 INTEREST-BEARING LOANS AND BORROWINGS

Interest-bearing loans and borrowings are recognised initially at fair value, net of transaction costs incurred. Subsequent to initial recognition, interest-bearing loans and borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis. The fair values of the Group's interest-bearing loans and borrowings are shown below.

Fixed-rate notes that are hedged by interest rate swaps are recognised at fair value.

All borrowings are unsecured, with the exception of the secured bank loans and finance leases.

All interest-bearing loans and borrowings, with the exception of secured bank loans and finance leases, are borrowed through Santos Finance Ltd, which is a wholly-owned subsidiary of Santos Limited. All interest-bearing loans and borrowings by Santos Finance Ltd are guaranteed by Santos Limited.

| | Ref | **2017 US$million** | 2016 US$million |
|---|---|---|---|
| **Current** | | | |
| Bank loans – secured | (a) | **141** | 132 |
| Bank loans – unsecured | (b) | **65** | 82 |
| Long-term notes | (c) | **–** | 205 |
| Finance leases | (e) | **1** | 1 |
| | | **207** | 420 |
| **Non-current** | | | |
| Bank loans – secured | (a) | **1,475** | 1,617 |
| Bank loans – unsecured | (b) | **992** | 1,653 |
| Long-term notes | (c) | **1,207** | 413 |
| Subordinated notes | (d) | **–** | 1,072 |
| Finance leases | (e) | **62** | 64 |
| | | **3,736** | 4,819 |

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.1 INTEREST-BEARING LOANS AND BORROWINGS (CONTINUED)

The Group's weighted average interest rate on interest-bearing liabilities is 5.15% for the year ended 31 December 2017 (2016: 4.79%).

**(a) Bank loans – secured**

| *Facility* | ***PNG LNG*** |
|---|---|
| *Currency* | US dollars |
| *Limit* | $1,692 million (2016: $1,838 million) |
| *Drawn principal* | $1,692 million (2016: $1,838 million) |
| *Accounting balance* | $1,616 million (2016: $1,749 million) including prepaid amounts |
| *Effective interest rate* | 5.37% (2016: 4.97%) |
| *Maturity* | 2024–2026 |
| *Other* | Loan facilities for the PNG LNG project, in which Santos entities hold an equity interest of 13.5%, were entered into by the joint venture participants on 15 December 2009 and are provided by commercial banks and export credit agencies, bear fixed and floating rates of interest and have final maturity dates of June 2024 and June 2026 respectively.<br><br>*Assets pledged as security and restricted cash*<br><br>The PNG LNG facilities include security over assets and entitlements of the participants in respect of the project. The total carrying value of the Group's assets pledged as security is $2,852 million at 31 December 2017 (2016: $2,959 million).<br><br>As referred to in note 4.1, under the terms of the project financing, cash relating to the Group's interest in undistributed project cash flows is required to be held in secured bank accounts. |

**(b) Bank loans – unsecured**

| *Facility* | ***Term bank loans*** |
|---|---|
| *Currency* | US dollars |
| *Limit* | Nil (2016: $17 million) |
| *Drawn principal* | Nil (2016: $17 million) |
| *Accounting balance* | Nil (2016: $17 million) |
| *Effective interest rate* | 1.35% (2016: 0.87%) |
| *Maturity* | 2017 |

| *Facility* | ***Export credit agency supported loan facilities*** |
|---|---|
| *Currency* | US dollars |
| *Limit* | $1,065 million (2016: $1,730 million) |
| *Drawn principal* | $1,065 million (2016: $1,730 million) |
| *Accounting balance* | $1,057 million (2016: $1,718 million) including prepaid amounts |
| *Effective interest rate* | 2.83% (2016: 2.64%) |
| *Maturity* | 2017–2024 |
| *Other* | Loan facilities are supported by various export credit agencies. |

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## 5.1 INTEREST-BEARING LOANS AND BORROWINGS (CONTINUED)

### (c) Long-term notes

| *Facility* | ***US private placement notes*** |
|---|---|
| *Currency* | US dollars |
| *Limit* | $377 million (2016: $577 million) |
| *Drawn principal* | $377 million (2016: $577 million) |
| *Accounting balance* | $424 million (2016: $618 million) including fair value accounting measurement and prepaid amounts |
| *Effective interest rate* | 1.84% (2016: 1.41%) |
| *Maturity* | 2017–2027 |
| *Other* | Long-term notes bear a fixed interest rate of 6.05% to 6.81% (2016: 6.05% to 6.81%), which have been swapped to floating rate commitments. |

| *Facility* | ***Regulation-S bond*** |
|---|---|
| *Currency* | US dollars |
| *Limit* | $800 million (2016: Nil) |
| *Drawn principal* | $800 million (2016: Nil) |
| *Accounting balance* | $783 million (2016: Nil) including fair value accounting measurement and prepaid amounts |
| *Effective interest rate* | 4.39% (2016: Nil) |
| *Maturity* | 2027 |
| *Other* | The bond bears a fixed interest rate of 4.125%. |

### (d) Subordinated notes

| *Facility* | ***Subordinated notes*** |
|---|---|
| *Currency* | Euro |
| *Limit* | Nil (2016: €1,000 million) |
| *Drawn principal* | Nil (2016: €1,000 million) |
| *Accounting balance* | Nil (2016: $1,072 million) including fair value accounting measurement and prepaid amounts |
| *Effective interest rate* | 7.03% (2016: 6.60%) |
| *Other* | The notes were redeemed at the first call date on 22 September 2017. |

### (e) Finance leases

Finance lease commitments are payable as follows:

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Not later than one year | **10** | 10 |
| Later than one year but not later than five years | **37** | 37 |
| Later than five years | **115** | 124 |
| Minimum lease payments | **162** | 171 |
| Future finance charges | **(99)** | (106) |
| Leases not commenced at reporting date | **–** | – |
| **Total lease liabilities** | **63** | 65 |

The Group participates in leases of LNG carriers and tug facilities under finance leases. The leases have terms of between 10 and 20 years with varying renewal options. Title does not pass to the Group on expiration of the relevant lease period.

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.2 NET FINANCE COSTS

### Borrowing costs

Borrowing costs relating to major oil and gas assets under development are capitalised as a component of the cost of development. Where funds are borrowed specifically for qualifying projects, the actual borrowing costs incurred are capitalised. Where the projects are funded through general borrowings, the borrowing costs are capitalised based on the weighted average cost of borrowing. Borrowing costs incurred after commencement of commercial operations are expensed to the income statement.

All other borrowing costs are recognised in the income statement in the period in which they are incurred.

### Interest income

Interest income is recognised in the income statement as it accrues using the effective interest method.

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Finance income:** | | |
| Interest income | **24** | 15 |
| **Total finance income** | **24** | 15 |
| **Finance costs:** | | |
| Interest paid to third parties | **255** | 275 |
| Deduct borrowing costs capitalised | **(6)** | (20) |
| | **249** | 255 |
| Unwind of the effect of discounting on provisions | **45** | 41 |
| **Total finance costs** | **294** | 296 |
| **Net finance costs** | **270** | 281 |

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## 5.3 ISSUED CAPITAL

### Ordinary share capital

Ordinary share capital is classified as equity. The issued shares do not have a par value and there is no limit on the authorised share capital of the Company.

Fully paid ordinary shares carry one vote per share, which entitles the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of, and amounts paid on, the shares held. The market price of the Company's ordinary shares on 31 December 2017 was A$5.45 (2016: A$4.02).

### Transaction costs

Transaction costs of an equity transaction are accounted for as a deduction from equity, net of any related income tax benefit. During 2017 transaction costs of $2 million in respect of capital raisings completed have been deducted from equity.

| Movement in ordinary shares | Note | **2017 Number of shares** | 2016 Number of shares | **2017 US$million** | 2016 US$million |
|---|---|---|---|---|---|
| Balance at 1 January | | **2,032,389,675** | 1,766,210,639 | **8,883** | 8,119 |
| Institutional placement, net of costs | | **–** | 256,000,000 | **–** | 738 |
| Share purchase plan, net of costs | | **50,847,537** | – | **151** | – |
| Santos Dividend Reinvestment Plan ("DRP") | | **–** | 8,205,002 | **–** | 23 |
| Santos Employee Share1000 Plan | 7.2 | **–** | 297,036 | **–** | 1 |
| Santos Employee ShareMatch Plan | 7.2 | **–** | 719,764 | **–** | 2 |
| Shares purchased on-market (Treasury shares) | | **–** | – | **(8)** | – |
| Utilisation of Treasury shares on vesting of employee share schemes | | **–** | – | **8** | – |
| Shares issued on vesting of Share Acquisition Rights ("SARs") | 7.2 | **5,365** | 578,818 | **–** | – |
| Shares issued on vesting of Executive Deferred Short-Term Incentive ("STI") | | **–** | 253,747 | **–** | – |
| Shares issued on vesting of Executive Strategy Grant | | **–** | 106,827 | **–** | – |
| Non-executive Director Share Plan | | **–** | 17,842 | **–** | – |
| Replacement of ordinary shares with shares purchased on-market | | **(171,698)** | – | **–** | – |
| **Balance at 31 December** | | **2,083,070,879** | 2,032,389,675 | **9,034** | 8,883 |

Included within the Group's ordinary shares at 31 December 2017 are 25,000 (2016: 25,000) ordinary shares paid to one cent with a value of nil (2016: nil).

### Treasury shares

Treasury shares are purchased primarily for use on vesting of employee share schemes. Shares are accounted for at weighted average cost. During the period, $8 million of Treasury shares were purchased on-market.

| Movement in Treasury shares | Note | **2017 Number of shares** |
|---|---|---|
| Balance at 1 January | | **–** |
| Shares purchased on-market | | **2,600,000** |
| Treasury shares utilised: | | |
| Santos Employee Share1000 Plan | 7.2 | **(301,584)** |
| Santos Employee ShareMatch Plan | 7.2 | **(553,416)** |
| Utilised on vesting of SARs | 7.2 | **(378,945)** |
| 2016 Executive STI (deferred SARs) | 7.2 | **(261,011)** |
| 2016 Executive STI (ordinary shares) | | **(193,977)** |
| 2016 Executive sign-on grants | | **(190,688)** |
| Santos Employee Share1000 Plan (relinquished shares) | | **39,312** |
| Replacement of ordinary shares with shares purchased on-market | | **(171,698)** |
| **Balance at 31 December** | | **587,993** |

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.4 RESERVES AND RETAINED EARNINGS

The Group's reserves and retained earnings balances, and movements during the period, are disclosed in the statement of changes in equity.

**Translation reserve**

The translation reserve comprises all foreign exchange differences arising from the following:

- the translation of the financial statements of foreign operations where their functional currency is different from the functional currency of the Parent entity;
- the translation of liabilities that hedge the Company's net investment in a foreign subsidiary;
- exchange differences that arise on the translation of the monetary items that form part of the net investment in a foreign operation; and
- the impact of translation of the Group from Australian dollars to USD presentation currency.

**Hedging reserve**

The hedging 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.

**Financial liabilities at fair value through OCI ("FVOCI") reserve**

The financial liabilities at FVOCI reserve includes the component of fair value movements in the Group's financial liabilities measured at fair value that result from changes in the Group's own credit risk. Such fair value movements were previously recorded in profit or loss however, due to adoption of AASB 9 effective from 1 January 2017, these movements are now required to be recorded through other comprehensive income and accumulate in this reserve.

**Accumulated profits reserve**

The accumulated profits reserve acts to quarantine profits generated in current and prior periods. The reserve was established during 2015.

## 5.5 FINANCIAL RISK MANAGEMENT

Exposure to foreign currency risk, interest rate risk, commodity price risk, credit risk and liquidity risk arises in the normal course of the Group's business. The Group's overall financial risk management strategy is to seek to ensure that the Group is able to fund its corporate objectives and meet its obligations to stakeholders. Derivative financial instruments may be used to hedge exposure to fluctuations in foreign exchange rates, interest rates and commodity prices.

The Group uses various methods to measure the types of financial risk to which it is exposed. These methods include Cash Flow at Risk and sensitivity analysis in the case of foreign exchange, interest rate and commodity price risk, and ageing and credit rating concentration analysis for credit risk.

Financial risk management is carried out by a central treasury department ("Treasury") which operates under Board-approved policies. The policies govern the framework and principles for overall risk management and cover specific financial risks, such as foreign exchange risk, interest rate risk and credit risk, approved derivative and non-derivative financial instruments, and liquidity management.

**(a) Financial instruments**

The Group classifies its financial instruments in the following categories: financial assets at amortised cost, financial assets at fair value through profit or loss ("FVTPL"), financial assets at fair value through other comprehensive income ("FVOCI"), financial liabilities at amortised cost and derivative instruments. The classification depends on the purpose for which the financial assets were acquired, which is determined at initial recognition based upon the business model of the Group.

***Financial assets at amortised cost***

The Group classifies its financial assets at amortised cost if the asset is held with the objective of collecting contractual cash flows and the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest. These include trade receivables and bank term deposits. Bank term deposits are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are financial assets at amortised cost and are included in current assets, except for those with maturities greater than 12 months after the reporting date.

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## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (a) Financial instruments (continued)

***Financial assets at fair value through profit or loss***

The Group classifies its financial assets at fair value through profit or loss if they are acquired principally for the purpose of selling in the short-term, i.e. are held for trading. For assets classified at fair value through profit or loss, the element of gains or losses attributable to changes in the Group's own credit risk are recognised in other comprehensive income. The Group has not elected to designate any financial assets at fair value through profit or loss.

***Financial assets at fair value through other comprehensive income***

Financial assets at fair value through other comprehensive income comprise debt securities where the contractual cash flows are solely principal and interest and the objective of the Group's business model is achieved both by collecting contractual cash flows and selling financial assets. Upon disposal, any balance within the OCI reserve for these debt investments is reclassified to retained earnings.

***Financial liabilities***

On initial recognition, the Group measures a financial liability at its fair value minus, in the case of a financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the issue of the financial liability.

After initial recognition, trade payables and interest-bearing loans and borrowings are stated at amortised cost. Fixed-rate notes that are hedged by an interest rate swap are recognised at fair value.

Policies for the recognition and subsequent measurement of derivative liabilities are as outlined below.

***Derivative instruments***

Derivative financial instruments entered into by the Group for the purpose of managing its exposures to changes in foreign exchange rates and interest rates arising in the normal course of business qualify for hedge accounting. The principal derivatives that may be used are forward foreign exchange contracts, cross-currency interest rate swaps and interest rate swaps. Commodity derivatives are also used to manage the Group's exposure to changes in oil prices and do not qualify for hedge accounting. The use of derivative financial instruments is subject to a set of policies, procedures and limits approved by the Board of Directors. The Group does not trade in derivative financial instruments for speculative purposes.

The Group holds the following financial instruments:

| **Financial assets** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Financial assets at amortised cost: | | |
| Cash and cash equivalents | **1,231** | 2,026 |
| Trade receivables | **440** | 372 |
| Available-for-sale financial assets | **–** | 8 |
| Amounts held in escrow[1] | **68** | 62 |
| Financial assets at FVTPL: | | |
| Equity investments | **2** | – |
| Derivative financial instruments | **61** | 84 |
| | **1,805** | 2,557 |

1. Amounts represent cash held in escrow for future restoration obligations relating to certain assets.

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (a) Financial instruments (continued)

| Financial liabilities | 2017 US$million | 2016 US$million |
|---|---|---|
| Financial liabilities at amortised cost: | | |
| Trade and other payables | **495** | 520 |
| Borrowings at amortised cost | **3,519** | 4,620 |
| Financial liabilities at FVTPL: | | |
| Borrowings at FVTPL | **424** | 619 |
| Derivative financial instruments | **79** | 363 |
| Embedded derivatives | **–** | 3 |
| Other | **23** | 23 |
| | **4,540** | 6,148 |

The Group's financial instruments resulted in the following income, expenses, gains and losses recognised in the income statement:

| Financial assets and liabilities | 2017 US$million | 2016 US$million |
|---|---|---|
| Interest on cash investments | **24** | 15 |
| Interest on debt held at FVTPL | **(29)** | (37) |
| Interest on debt held at amortised cost | **(277)** | (268) |
| Interest on derivative financial instruments | **57** | 30 |
| Amounts reclassified from other comprehensive income to profit or loss | **(7)** | – |
| Fair value gains/(losses) on debt held at FVTPL | **31** | (17) |
| Fair value gains on debt held at amortised cost | **26** | 36 |
| Fair value losses on derivative financial instruments | **(106)** | (73) |
| Net impairment expense recognised on trade receivables | **(5)** | – |
| Net foreign exchange (losses)/gains recognised in profit before income tax for the period, included in other income and finance costs | **(153)** | 34 |
| | **(439)** | (280) |

### (b) Liquidity

The Group adopts a prudent liquidity risk management strategy and seeks to maintain sufficient liquid assets and available committed credit facilities to meet short-term to medium-term liquidity requirements. The Group's objective is to maintain flexibility in funding to meet ongoing operational requirements, exploration and development expenditure, and other corporate initiatives.

The following tables analyse the contractual maturities of the Group's financial assets and liabilities held to manage liquidity risk. The relevant maturity groupings are based on the remaining period to the contractual maturity date, as at 31 December. The amounts disclosed in the table are the contractual undiscounted cash flows comprising principal and interest repayments. Estimated variable interest expense is based upon appropriate yield curves as at 31 December.

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## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (b) Liquidity (continued)

| Financial assets and liabilities held to manage liquidity risk 2017 | Less than 1 year US$million | 1 to 2 years US$million | 2 to 5 years US$million | More than 5 years US$million |
|---|---|---|---|---|
| Cash and cash equivalents | **1,231** | **–** | **–** | **–** |
| **Derivative financial assets** | | | | |
| Interest rate swap contracts | **16** | **20** | **45** | **5** |
| **Non-derivative financial liabilities** | | | | |
| Trade and other payables | **(495)** | **–** | **–** | **–** |
| Obligations under finance leases | **(10)** | **(10)** | **(27)** | **(115)** |
| Bank loans | **(305)** | **(898)** | **(920)** | **(1,070)** |
| Long-term notes | **(57)** | **(207)** | **(356)** | **(985)** |
| | **380** | **(1,095)** | **(1,258)** | **(2,165)** |

| Financial assets and liabilities held to manage liquidity risk 2016 | Less than 1 year US$million | 1 to 2 years US$million | 2 to 5 years US$million | More than 5 years US$million |
|---|---|---|---|---|
| Cash and cash equivalents | 2,026 | – | – | – |
| **Derivative financial assets** | | | | |
| Interest rate swap contracts | 31 | 25 | 36 | 11 |
| **Derivative financial liabilities** | | | | |
| Cross-currency swap contracts | (368) | – | – | – |
| **Non-derivative financial liabilities** | | | | |
| Trade and other payables | (520) | – | – | – |
| Obligations under finance leases | (9) | (9) | (28) | (125) |
| Bank loans | (355) | (323) | (2,124) | (1,420) |
| Long-term notes | (237) | (24) | (204) | (247) |
| Subordinated debt | (1,136) | – | – | – |
| | (568) | (331) | (2,320) | (1,781) |

### (c) Foreign currency risk

Foreign exchange risk arises from commercial transactions and valuations of assets and liabilities that are denominated in a currency that is not the entity's functional currency.

The Group is exposed to foreign currency risk principally through the sale of products, borrowings and capital and operating expenditure incurred in currencies other than the functional currency. In order to economically hedge foreign currency risk, the Group from time to time enters into forward foreign exchange, foreign currency swap and foreign currency option contracts.

The Group has certain investments in domestic and foreign operations whose net assets are exposed to foreign currency translation risk.

All foreign currency denominated borrowings of Australian dollar functional currency companies are either designated as a hedge of US dollar-denominated investments in foreign operations (2017: $1,407 million; 2016: $824 million), swapped using cross-currency swaps to US dollars and designated as a hedge of US dollar-denominated investments in foreign operations (2017: $nil; 2016: $1,410 million), or offset by US dollar-denominated cash balances (2017: $835 million; 2016: $1,500 million). As a result, there were no net foreign currency gains or losses arising from translation of US dollar-denominated borrowings recognised in the income statement in 2017.

Monetary items, including financial assets and liabilities, denominated in currencies other than the functional currency of an operation, are periodically restated to US dollar equivalents, and the associated gain or loss is taken to the income statement. The exception is foreign exchange gains or losses on foreign currency provisions for restoration at operating sites that are capitalised in oil and gas assets.

***Sensitivity to foreign currency movement***

Based on the Group's net financial assets and liabilities at 31 December 2017, the estimated impact of a ±15 cent movement in the Australian dollar exchange rate (2016: ±15 cent) against the US dollar, with all other variables held constant is $22 million (2016: $5 million) on post-tax profit and $1,374 million (2016: $980 million) on equity.

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (d) Market risk

***Cash flow and fair value interest rate risk***

The Group's interest rate risk arises from its borrowings. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk.

The Group adopts a policy of ensuring that the majority of its exposure to changes in interest rates on borrowings is on a floating rate basis. Interest rate swaps have been entered into as fair value hedges of long-term notes. When transacted, these swaps had maturities ranging from 1 to 20 years, aligned with the maturity of the related notes.

The Group's interest rate swaps have a notional contract amount of $1,577 million (2016: $1,777 million) and a net fair value of $61 million (2016: $84 million). The net fair value amounts were recognised as fair value derivatives.

***Sensitivity to interest rate movement***

Based on the net debt position as at 31 December 2017, taking into account interest rate swaps, it is estimated that if the US dollar London Interbank Offered Rate ("LIBOR") interest rates changed by ±0.50% (2016: ±0.50%), Euro Interbank Offered Rate ("EURIBOR") changed by ±0.50% (2016: ±0.50%) and Australian Bank Bill Swap reference rate ("BBSW") changed by ±0.50% (2016: ±0.50%), with all other variables held constant, the impact on post-tax profit is nil (2016: $6 million).

This assumes that the change in interest rates is effective from the beginning of the financial year and the net debt position and fixed/floating mix is constant over the year. However, interest rates and the debt profile of the Group are unlikely to remain constant and therefore the above sensitivity analysis will be subject to change.

***Commodity price risk exposure***

The Group is exposed to commodity price fluctuations through the sale of petroleum products and other oil price linked contracts. The Group may enter into crude oil price swap and option contracts to manage its commodity price risk. At 31 December 2017, the Group has 12.5 million barrels of open oil price option contracts (2016: 10.95 million), covering 2018 exposures. The 3-way collar option structure utilised does not qualify for hedge accounting, with the movement in fair value recorded in the income statement.

### (e) Credit risk

Credit risk represents the potential financial loss if counterparties fail to complete their obligations under financial instrument or customer contracts. Santos employs credit policies which include monitoring exposure to credit risk on an ongoing basis through management of concentration risk and ageing analysis.

The majority of Santos' gas contracts are spread across major Australian energy retailers and industrial users. Contracts exist in every mainland state whilst the largest customer accounts for less than 15% of sales revenue.

The Group considers the probability of default upon initial recognition of the asset and whether there has been a significant depreciation in credit quality on an ongoing basis throughout each reporting period. A significant decrease in credit quality is defined as a debtor being greater than 30 days past due in making a contractual payment.

A default on a financial asset is when the counterparty fails to make contractual payments within 60 days of when they fall due.

Financial assets are written off when there is no reasonable expectation of recovery. The Group categorises a loan or receivable for write off when a debtor fails to make contractual repayments greater than 120 days past due. Where loans or receivables have been written off, the Group continues to engage in enforcement activity to attempt to recover the receivable due. Where recoveries are made, these are recognised in profit or loss.

At 31 December 2017 there were no significant concentrations of credit risk within the Group and financial instruments are spread amongst a number of financial institutions to minimise the risk of counterparty default.

The maximum exposure to financial institution credit risk is represented by the sum of all cash deposits plus accrued interest, bank account balances and fair value of derivative assets.

The Group applies the simplified approach to providing for expected credit losses prescribed by AASB 9, which permits the use of the lifetime expected loss provision for all trade receivables. Under this method, determination of the loss allowance provision and expected loss rate incorporates past experience and forward-looking information, including the outlook for market demand and forward-looking interest rates. As the expected loss rate at 31 December 2017 is nil (2016: nil), no loss allowance provision has been recorded at 31 December 2017 (2016: nil).

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## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (f) Fair values

The financial assets and liabilities of the Group are all initially recognised in the statement of financial position at their fair values. Receivables, payables, interest-bearing liabilities and other financial assets and liabilities, which are not subsequently measured at fair value, are carried at amortised cost. The following summarises the significant methods and assumptions used in estimating the fair values of financial instruments:

***Derivatives***

The fair value of interest rate swaps is calculated by discounting estimated future cash flows based on the terms of maturity of each contract, using market interest rates for a similar instrument at the reporting date. Where these cash flows are in a foreign currency, the present value is converted to US dollars at the foreign exchange spot rate prevailing at the reporting date.

***Financial liabilities***

Fair value is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. Where these cash flows are in a foreign currency, the present value is converted to US dollars at the foreign exchange spot rate prevailing at the reporting date.

***Interest rates used for determining fair value***

The interest rates used to discount estimated future cash flows, where applicable, are based on the market yield curve and credit spreads at the reporting date.

The interest rates including credit spreads used to determine fair value were as follows:

| | **2017 %** | 2016 % |
|---|---|---|
| Derivatives | **1.4 – 2.5** | (0.3) – 3.9 |
| Loans and borrowings | **1.4 – 2.5** | (0.3) – 3.9 |

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets and liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly;

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

All of the Group's financial instruments were valued using the Level 2 valuation technique.

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (g) Derivatives and hedging activity

The Group early adopted AASB 9 *Financial Instruments* from 1 January 2017. Upon adoption of AASB 9, the component of fair value changes of qualifying instruments relating to the Company's own credit risk is recognised in other comprehensive income ("OCI"). Amounts recorded in OCI related to credit risk are not subject to recycling in profit or loss, but are reclassified to retained earnings when realised. The change to hedge accounting is undertaken prospectively, with instruments held by the Group prior to the change accounted for in accordance with the previous policy.

The change in accounting policy allows the Group to manage risk in an effective manner, without the accounting treatment of the instruments distorting the reported results.

Refer to note 8.5 for further details of the transition impacts of AASB 9.

The Group's accounting policy for fair value and cash flow hedges are as follows:

| Types of hedges | Fair value hedges | Cash flow hedges |
|---|---|---|
| What is it? | A derivative or financial instrument designated as hedging the change in fair value of a recognised asset or liability. | A derivative or financial instrument to hedge the exposure to variability in cash flows attributable to a particular risk associated with an asset, liability or forecast transaction. |
| Recognition date | At the date the instrument is entered into. | At the date the instrument is entered into. |
| Measurement | Measured at fair value, being the estimated amount that the Group would receive or pay to terminate the contracts at the reporting date. | Measured at fair value, being the estimated amount that the Group would receive or pay to terminate the contracts at the reporting date. |
| Changes in fair value | The gains or losses on both the derivative or financial instrument and hedged asset or liability attributable to the hedged risk are recognised in the income statement immediately.<br><br>The gain or loss relating to the effective portion of interest rate swaps hedging fixed-rate borrowings is recognised in the income statement within finance costs, together with loss or gain in the fair value of the hedged fixed-rate borrowings attributable to interest rate risk.<br><br>The gain or loss relating to the ineffective portion is recognised in the income statement within other income or other expenses.<br><br>If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to the income statement over the period to maturity using a recalculated effective interest rate. | Changes in the fair value of derivatives designated as cash flow hedges are recognised directly in other comprehensive income and accumulated in equity in the hedging reserve to the extent that the hedge is highly effective.<br><br>Ineffectiveness is recognised on a cash flow hedge where the cumulative change in the designated component value of the hedging instrument exceeds on an absolute basis the change in value of the hedged item attributable to the hedged risk. In hedges of foreign currency purchases this may arise if the timing of the transaction changes from what was originally estimated.<br><br>To the extent that the hedge is ineffective, changes in fair value are recognised immediately in the income statement within other income or other expenses.<br><br>Amounts accumulated in equity are transferred to the income statement or the statement of financial position, for a non-financial asset, at the same time as the hedged item is recognised.<br><br>When a hedging instrument expires or is sold, terminated or exercised, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the underlying forecast transaction occurs.<br><br>When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement. |

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## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (g) Derivatives and hedging activity (continued)

Hedge effectiveness is determined at the inception of the hedge relationship, and through periodic prospective effectiveness assessments to ensure that an economic relationship exists between the hedged item and hedging instrument. The Group enters into hedge relationships where the critical terms of the hedging instrument match exactly with the terms of the hedged item, and so a qualitative assessment of effectiveness is performed. If changes in circumstances affect the terms of the hedged item such that the critical terms no longer match exactly with the critical terms of the hedging instrument, the Group uses the hypothetical derivative method is to assess effectiveness.

***Hedge of monetary assets and liabilities***

When a derivative financial instrument is used to hedge economically the foreign exchange exposure of a recognised monetary asset or liability, hedge accounting is not applied and any gain or loss on the hedging instrument is recognised in the income statement.

***Hedge of net investment in a foreign operation***

The gain or loss on an instrument used to hedge a net investment in a foreign operation is recognised directly in equity. On disposal of the foreign operation, the cumulative value of any such gains or losses recognised directly in equity is transferred to the income statement.

The table below contains all "other financial assets and liabilities" as shown in the statement of financial position, including derivative financial instruments used for hedging:

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Current assets** | | |
| Interest rate swap contracts | **–** | 7 |
| | **–** | 7 |
| **Non-current assets** | | |
| Interest rate swap contracts | **61** | 77 |
| Available-for-sale assets | **–** | 8 |
| Equity investments | **2** | – |
| Amounts held in escrow | **68** | 62 |
| Defined benefit surplus | **3** | 5 |
| | **134** | 152 |
| **Current liabilities** | | |
| Cross-currency swap contracts | **–** | 349 |
| Commodity derivatives (oil hedges) | **79** | 14 |
| Other | **3** | 3 |
| | **82** | 366 |
| **Non-current liabilities** | | |
| Embedded derivatives | **–** | 3 |
| Other | **20** | 20 |
| | **20** | 23 |

# Notes to the Consolidated Financial Statements
# Section 5: Funding and Risk Management

## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (g) Derivatives and hedging activity (continued)

The effects of applying hedge accounting on the Group's financial position and performance are as follows:

| ***Derivative financial instruments – Interest rate swap contracts*** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Carrying amount | **61** | 84 |
| Notional amount | **1,577** | 1,777 |
| Maturity date | **2019–2027** | 2017–2027 |
| Hedge ratio[1] | **1:1** | 1:1 |
| Change in value of outstanding hedging instruments since 1 January | **(23)** | (8) |
| Change in value of hedged item used to determine hedge effectiveness | **23** | 8 |
| Weighted average hedged rate | **1.10%** | 1.18% |

| ***Derivative financial instruments – Cross-currency swap contracts*** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Carrying amount | **–** | (349) |
| Notional amount | **–** | 1,410 |
| Maturity date | **–** | 2017 |
| Hedge ratio[1] | **1:1** | 1:1 |
| Change in value of outstanding hedging instruments since 1 January | **349** | (67) |
| Change in value of hedged item used to determine hedge effectiveness | **(349)** | 67 |
| Weighted average hedged rate | **6.83%** | 6.30% |

| ***Reserves – Cash flow hedge reserve*** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Balance at 1 January | **(7)** | 12 |
| *Add:* Change in fair value of hedging instrument recognised in OCI for the year (effective portion) | **3** | (27) |
| *Less:* Deferred tax | **(1)** | 8 |
| **Balance at 31 December** | **(5)** | (7) |

| ***Reserves – FVOCI reserve*** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Balance at 1 January | **–** | – |
| *Add:* Change in fair value of hedging instrument recognised in OCI for the year (effective portion) | **32** | – |
| *Less:* Deferred tax | **(11)** | – |
| **Balance at 31 December** | **21** | – |

| ***Reserves – Foreign currency hedge reserve*** | **2017 US$million** | 2016 US$million |
|---|---|---|
| Balance at 1 January | **707** | 721 |
| *Add:* Change in fair value of hedging instrument recognised in OCI for the year (effective portion) | **(191)** | (20) |
| *Less:* Deferred tax | **57** | 6 |
| **Balance at 31 December** | **573** | 707 |

1. The value of the derivative contract is the same as the value of the underlying instrument that is being hedged. Therefore, the hedge ratio is 1:1.

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# Notes to the Consolidated Financial Statements
# **Section 6: Group Structure**

This section provides information which will help users understand how the Group structure affects the financial position and performance of the Group as a whole. Specifically, it contains information about consolidated entities, acquisitions and disposals of subsidiaries, joint arrangements as well as parties to the Deed of Cross Guarantee under which each company guarantees the debts of others.

## 6.1 CONSOLIDATED ENTITIES

Subsidiaries are entities controlled by the Company. Control exists when the Company is exposed to, or has the rights to, variable returns from its involvement with an entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Acquisitions of subsidiaries are accounted for using the acquisition method of accounting, and are initially recorded in the parent entity's financial statements at the cost of acquisition less any impairment charges.

A change in ownership interest of a subsidiary that does not result in the loss of control is accounted for as an equity transaction.

Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions are eliminated in preparing the consolidated financial statements.

# Notes to the Consolidated Financial Statements
# Section 6: Group Structure

## 6.1 CONSOLIDATED ENTITIES (CONTINUED)

| Name | Country of incorporation |
|---|---|
| **Santos Limited[1] (Parent Company)** | **AUS** |
| **Controlled entities:** | |
| Alliance Petroleum Australia Pty Ltd[1] | AUS |
| Basin Oil Pty Ltd[1] | AUS |
| Bridgefield Pty Ltd | AUS |
| Bridge Oil Developments Pty Ltd[1] | AUS |
| Bronco Energy Pty Ltd | AUS |
| Doce Pty Ltd | AUS |
| Fairview Pipeline Pty Ltd[1] | AUS |
| Gidgealpa Oil Pty Ltd | AUS |
| Moonie Pipeline Company Pty Ltd | AUS |
| Reef Oil Pty Ltd[1] | AUS |
| Santos Asia Pacific Pty Ltd | AUS |
| *Controlled entities of Santos Asia Pacific Pty Ltd* | |
| Santos (Sampang) Pty Ltd | AUS |
| Santos (Warim) Pty Ltd | AUS |
| Santos Australian Hydrocarbons Pty Ltd | AUS |
| Santos (BOL) Pty Ltd[1] | AUS |
| *Controlled entity of Santos (BOL) Pty Ltd* | |
| Bridge Oil Exploration Pty Ltd | AUS |
| Santos Browse Pty Ltd | AUS |
| Santos CSG Pty Ltd | AUS |
| Santos Darwin LNG Pty Ltd | AUS |
| Santos Direct Pty Ltd | AUS |
| Santos Finance Ltd | AUS |
| Santos GLNG Pty Ltd | AUS |
| *Controlled entity of Santos GLNG Pty Ltd* | |
| Santos GLNG Corp | USA |
| Santos (Globe) Pty Ltd | AUS |
| Santos International Holdings Pty Ltd | AUS |
| *Controlled entities of Santos International Holdings Pty Ltd* | |
| Barracuda Ltd | PNG |
| Lavana Ltd | PNG |
| Sanro Insurance Pte Ltd | SGP |
| Santos Americas and Europe Corporation | USA |
| *Controlled entities of Santos Americas and Europe Corporation* | |
| Santos TPY Corp | USA |
| *Controlled entities of Santos TPY Corp* | |
| Santos Queensland Corp | USA |
| Santos TOG Corp | USA |
| *Controlled entities of Santos TOG Corp* | |
| Santos TOGA Pty Ltd | AUS |
| Santos TPY CSG Corp | USA |
| Santos Bangladesh Ltd | GBR |
| Santos Baturaja Pty Ltd | AUS |

| Name | Country of incorporation |
|---|---|
| *Controlled entities of Santos International Holdings Pty Ltd (cont)* | |
| Santos (BBF) Pty Ltd | AUS |
| *Controlled entities of Santos (BBF) Pty Ltd* | |
| Santos (SPV) Pty Ltd | AUS |
| *Controlled entity of Santos (SPV) Pty Ltd* | |
| Santos (Madura Offshore) Pty Ltd | AUS |
| Santos Belida Pty Ltd | AUS |
| Santos EOM Pty Ltd | AUS |
| Santos Hides Ltd | PNG |
| Santos International Pte Ltd[5] | SGP |
| Santos International Operations Pty Ltd | AUS |
| Santos OIG Pty Ltd | AUS |
| Santos P'nyang Ltd | PNG |
| Santos Sabah Block R Limited | GBR |
| Santos Sangu Field Ltd | GBR |
| Santos (UK) Limited | GBR |
| *Controlled entities of Santos (UK) Limited* | |
| Santos Northwest Natuna B.V. | NLD |
| Santos Petroleum Ventures B.V. | NLD |
| Santos Sabah Block S Limited[2] | GBR |
| Santos Vietnam Pty Ltd | AUS |
| Santos (JPDA 91–12) Pty Ltd | AUS |
| Santos (NARNL Cooper) Pty Ltd[1] | AUS |
| Santos NSW Pty Ltd | AUS |
| *Controlled entities of Santos NSW Pty Ltd* | |
| Santos NSW (Betel) Pty Ltd | AUS |
| Santos NSW (Hillgrove) Pty Ltd | AUS |
| Santos NSW (Holdings) Pty Ltd | AUS |
| *Controlled entities of Santos NSW (Holdings) Pty Ltd* | |
| Santos NSW (LNGN) Pty Ltd | AUS |
| Santos NSW (Pipeline) Pty Ltd | AUS |
| Santos NSW (Narrabri Energy) Pty Ltd | AUS |
| *Controlled entity of Santos NSW (Narrabri Energy) Pty Ltd* | |
| Santos NSW (Eastern) Pty Ltd | AUS |
| Santos NSW (Narrabri Power) Pty Ltd | AUS |
| Santos NSW (Operations) Pty Ltd | AUS |
| Santos (N.T.) Pty Ltd | AUS |
| *Controlled entity of Santos (N.T.) Pty Ltd* | |
| Bonaparte Gas & Oil Pty Ltd | AUS |
| Santos Offshore Pty Ltd[1] | AUS |
| Santos Petroleum Pty Ltd[1] | AUS |
| Santos QLD Upstream Developments Pty Ltd | AUS |
| Santos QNT Pty Ltd[1] | AUS |
| *Controlled entities of Santos QNT Pty Ltd* | |
| Outback Energy Hunter Pty Ltd | AUS |

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| Name | Country of incorporation |
|---|---|
| *Controlled entities of Santos QNT Pty Ltd (cont)* | |
| Santos QNT (No. 1) Pty Ltd[1] | AUS |
| *Controlled entities of Santos QNT (No. 1) Pty Ltd* | |
| Santos Petroleum Management Pty Ltd | AUS |
| Santos Petroleum Operations Pty Ltd[4] | AUS |
| TMOC Exploration Proprietary Limited | AUS |
| Santos QNT (No. 2) Pty Ltd | AUS |
| *Controlled entities of Santos QNT (No. 2) Pty Ltd* | |
| Moonie Oil Pty Ltd | AUS |
| Petromin Pty Ltd | AUS |
| Santos (299) Pty Ltd[3] | AUS |
| Santos TPC Pty Ltd | AUS |
| Santos Wilga Park Pty Ltd | AUS |
| Santos Resources Pty Ltd | AUS |
| Santos (TGR) Pty Ltd | AUS |
| Santos Timor Sea Pipeline Pty Ltd | AUS |
| Santos Ventures Pty Ltd | AUS |
| SESAP Pty Ltd | AUS |
| Shaw River Power Station Pty Ltd | AUS |
| Vamgas Pty Ltd[1] | AUS |

**Notes**

1. Company is party to a Deed of Cross Guarantee. Refer note 6.5.
2. Company was deregistered on 21 March 2017.
3. In liquidation.
4. Company was deregistered on 19 December 2017.
5. Application to deregister lodged on 18 December 2017.

**Country of incorporation**

AUS – Australia
GBR – United Kingdom
NLD – Netherlands
PNG – Papua New Guinea
SGP – Singapore
USA – United States of America

## 6.2 ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES

There were no acquisitions or disposals of subsidiaries during 2017.

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# Notes to the Consolidated Financial Statements
# Section 6: Group Structure

## 6.3 JOINT ARRANGEMENTS

The Group's investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations each investor has, rather than the legal structure of the joint arrangement. Santos' exploration and production activities are often conducted through joint arrangements governed by joint operating agreements, production sharing contracts or similar contractual relationships.

The differences between joint operations and joint ventures are as follows:

| Types of arrangement | Joint operation | Joint venture |
|---|---|---|
| Characteristics | A joint operation involves the joint control, and often the joint ownership, of assets contributed to, or acquired for the purpose of, the joint operation. The assets are used to obtain benefits for the parties to the joint operation and are dedicated to that purpose. | The Group has interests in joint ventures, whereby the venturers have contractual arrangements that establish joint control over the economic activities of the entities. |
| Rights and obligations | Each party has control over its share of future economic benefits through its share of the joint operation, and has rights to the assets, and obligations for the liabilities, relating to the arrangement. | Parties that have joint control of the arrangement have rights to the net assets of the arrangement. |
| Accounting method | The interests of the Group in joint operations are brought to account by recognising the Group's share of jointly controlled assets, share of expenses and liabilities incurred, and the income from its share of the production of the joint operation. | The Group recognises its interest in joint ventures using the equity method of accounting.<br><br>Under the equity method, the investment in a joint venture is initially recognised in the Group's statement of financial position at cost and adjusted thereafter to recognise the post-acquisition changes to the Group's share of net assets of the joint venture. After application of the equity method, the Group determines whether it is necessary to recognise any impairment loss with respect to the Group's net investment in the joint venture.<br><br>The Group's share of the joint venture's post-acquisition profits or losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in the statement of changes in equity and, when applicable, in the statement of comprehensive income. Dividends receivable from the joint venture reduce the carrying amount of the investment in the consolidated financial statements of the Group. |

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## 6.3 JOINT ARRANGEMENTS (CONTINUED)

### (a) Joint operations

The following are the material joint operations in which the Group has an interest:

| Joint operation | Area of cash-generating unit/area of interest | Principal activities | 2017 % Interest | 2016 % Interest |
|---|---|---|---|---|
| **Oil and gas assets – Producing assets** | | | | |
| Barrow Island | Barrow | Oil production | **28.6** | 28.6 |
| Bayu-Undan | Bayu-Undan | Gas and liquids production | **11.5** | 11.5 |
| Casino[1] | Victoria | Gas production | **–** | 50.0 |
| Chim Sáo/Dua | Vietnam (Block 12W) | Oil and gas production | **31.9** | 31.9 |
| Fairview | GLNG | Gas production | **22.8** | 22.8 |
| GLNG Downstream | GLNG | LNG facilities | **30.0** | 30.0 |
| Halyard/Spar | Varanus Island | Gas production | **45.0** | 45.0 |
| John Brookes | Varanus Island | Gas production | **45.0** | 45.0 |
| Madura Offshore | Madura PSC | Gas production | **67.5** | 67.5 |
| Mutineer-Exeter/ Fletcher Finucane | Mutineer-Exeter/ Fletcher Finucane | Oil production | **37.5** | 37.5 |
| PNG LNG | PNG LNG | Gas and liquids production | **13.5** | 13.5 |
| Reindeer | Reindeer | Gas production | **45.0** | 45.0 |
| Roma | GLNG | Gas production | **30.0** | 30.0 |
| SA Fixed Factor Area | Cooper Basin | Oil and gas production | **66.6** | 66.6 |
| Sampang | Sampang PSC | Oil and gas production | **45.0** | 45.0 |
| SWQ Unit | Cooper Basin | Gas production | **60.1** | 60.1 |
| **Exploration and evaluation assets** | | | | |
| EPP43 | Ceduna Basin | Contingent oil or gas resource | **50.0** | 50.0 |
| EP161, EP162 and EP189[2] | McArthur Basin | Contingent gas resource | **75.0** | 50.0 |
| Block R | Sabah Block R PSC | Oil and gas exploration | **20.0** | 20.0 |
| Caldita/Barossa | Bonaparte Basin | Contingent gas resource | **25.0** | 25.0 |
| Ande Ande Lumut | Northwest Natuna PSC | Oil resource | **50.0** | 50.0 |
| PEL1 and 12 | – | Contingent gas resource | **65.0** | 65.0 |
| PEL238 and PAL2 | Gunnedah Basin | Contingent gas resource | **80.0** | 80.0 |
| PPL269[3] | PNG Exploration | Oil and gas exploration | **–** | 30.0 |
| WA-58-R (WA-274-P) | Bonaparte Basin | Gas development | **30.0** | 30.0 |
| WA-323-P | Bonaparte Basin | Contingent gas resource | **75.0** | 75.0 |
| WA-49-R[4] | Carnarvon Basin | Contingent gas resource | **31.5** | 24.8 |

1. Asset sold in 2017.
2. During 2017 the Group acquired an additional 25% interest, which is subject to customary regulatory approvals.
3. Licence has expired and is not being renewed.
4. During 2017 the Group acquired an additional 6.7% interest in WA-49-R. In addition, one of the joint venture parties resolved to withdraw from the permit in 2017. Registration of transfer will result in Santos' interest increasing to 35%.

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# Notes to the Consolidated Financial Statements
# Section 6: Group Structure

## 6.3 JOINT ARRANGEMENTS (CONTINUED)

### (b) Share of investments in joint ventures

The Group's only material joint venture is Darwin LNG Pty Ltd, which operates the Darwin LNG liquefaction facility that currently processes gas from the Bayu-Undan gas fields.

Summarised financial information of the joint venture, based on the amounts presented in its financial statements, and a reconciliation to the carrying amount of the investment in the consolidated financial statements, are set out below:

| **Share of investments in Darwin LNG Pty Ltd** | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Reconciliation to carrying amount:** | | |
| **Opening net assets 1 January** | **490** | 620 |
| Profit for the period | **93** | 88 |
| Reduction in capital | **(115)** | (130) |
| Dividends paid | **(93)** | (88) |
| **Closing net assets 31 December** | **375** | 490 |
| Group's share (%) | **11.5%** | 11.5% |
| Group's share of closing net assets ($million) | **43** | 56 |
| Carrying amount of investments in joint ventures ($million) | **43** | 56 |
| **Summarised statement of comprehensive income:** | | |
| **Profit for the period** | **93** | 88 |
| Other comprehensive income | **–** | – |
| **Total comprehensive income** | **93** | 88 |
| Group's share of profit | **11** | 10 |
| Dividends received from joint venture | **11** | 10 |

The following are the joint ventures in which the Group has an interest, including those which are immaterial:

| **Joint venture** | **2017 % Interest** | 2016 % Interest |
|---|---|---|
| Darwin LNG Pty Ltd | **11.5** | 11.5 |
| GLNG Operations Pty Ltd | **30.0** | 30.0 |
| GLNG Property Pty Ltd | **30.0** | 30.0 |
| Lohengrin Pty Ltd | **–** | 50.0 |

### (c) Income from all joint ventures

A reconciliation of the Group's total income from all joint ventures:

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| Share of Darwin LNG Pty Ltd net profits | **11** | 10 |
| **Total share of net profits** | **11** | 10 |

At 31 December 2017 the Group reassessed the carrying amount of its investments in joint ventures for indicators of impairment. As a result, no impairment was recorded (2016: nil).

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## 6.4 PARENT ENTITY DISCLOSURES

Selected financial information of the ultimate parent entity in the Group, Santos Limited, is as follows:

| | 2017 US$million | 2016 US$million |
|---|---|---|
| **Net profit for the period** | **282** | 42 |
| Total comprehensive income | **282** | 43 |
| Current assets | **344** | 414 |
| Total assets | **11,897** | 9,757 |
| Current liabilities | **474** | 529 |
| Total liabilities | **4,564** | 3,390 |
| Issued capital | **9,034** | 8,883 |
| Accumulated profits reserve | **595** | 313 |
| Other reserves | **(556)** | (1,079) |
| Accumulated losses | **(1,740)** | (1,750) |
| **Total equity** | **7,333** | 6,367 |

### Commitments of the parent entity

The parent entity's capital expenditure commitments and minimum exploration commitments are:

| | | |
|---|---|---|
| Capital expenditure commitments | **44** | 42 |
| Minimum exploration commitments | **10** | 27 |

### Guarantees entered into by the parent entity in relation to the debts of its subsidiaries

All interest-bearing loans and borrowings, as disclosed in note 5.1, with the exception of the finance leases and secured bank loans, are arranged through Santos Finance Ltd, which is a wholly-owned subsidiary of Santos Limited. All interest-bearing loans and borrowings of Santos Finance Ltd are guaranteed by Santos Limited.

### Contingent liabilities of the parent entity

Contingent liabilities arise in the ordinary course of business through claims against Santos Limited, including contractual, third-party and contractor claims. In most instances it is not possible to reasonably predict the outcome of these claims, and as at reporting date Santos Limited believes that the aggregate of such claims will not materially impact the Company's financial report.

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# Notes to the Consolidated Financial Statements
# Section 6: Group Structure

## 6.5 DEED OF CROSS GUARANTEE

As a condition of the Instrument, the Company and each of the wholly-owned subsidiaries identified in note 6.1 (collectively, "the Closed Group") have entered into a Deed of Cross Guarantee ("the Deed"). The effect of the Deed is that the Company has guaranteed to pay any deficiency in the event of winding up of any of the subsidiaries under certain provisions of the *Corporations Act 2001*. The subsidiaries have also given a similar guarantee in the event that the Company is wound up.

Pursuant to ASIC Corporations (Wholly-owned Companies) Instrument 2016/785, the wholly-owned subsidiaries within the Closed Group are relieved from the *Corporations Act 2001* requirements for preparation, audit and lodgement of their financial reports.

Set out below is a consolidated income statement, consolidated statement of comprehensive income and summary of movements in consolidated retained earnings for the year ended 31 December 2017 of the Closed Group.

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Consolidated income statement** | | |
| Product sales | **1,200** | 1,147 |
| Cost of sales | **(1,015)** | (1,008) |
| **Gross profit** | **185** | 139 |
| Other revenue | **96** | 369 |
| Other income | **94** | 98 |
| Other expenses | **(130)** | (126) |
| Impairment of non-current assets | **328** | (306) |
| Interest income | **15** | 9 |
| Finance costs | **–** | (5) |
| **Profit before tax** | **588** | 178 |
| Income tax expense | **(232)** | (45) |
| Royalty-related tax expense | **(1)** | (15) |
| Total tax expense | **(233)** | (60) |
| **Net profit for the period** | **355** | 118 |
| **Consolidated statement of comprehensive income** | | |
| **Net profit for the period** | **355** | 118 |
| **Other comprehensive income, net of tax:** | | |
| Net actuarial gain on defined benefit plan | **–** | 1 |
| **Total comprehensive profit** | **355** | 119 |
| **Summary of movements in the Closed Group's accumulated losses:** | | |
| Accumulated losses at 1 January | **(2,256)** | (2,133) |
| Opening balance adjustment on adoption of new accounting standard (refer note 8.5) | **5** | – |
| Adjusted accumulated losses at 1 January | **(2,251)** | (2,133) |
| *Add:* Opening retained earnings of companies added during the period | **–** | 6 |
| Transfer to accumulated profits reserve | **(282)** | (258) |
| Net profit for the period | **355** | 118 |
| Net actuarial gain on defined benefit plan | **–** | 1 |
| Share-based payment transactions | **6** | 10 |
| *Less:* Retained earnings of companies removed during the period | **19** | – |
| **Accumulated losses at 31 December** | **(2,153)** | (2,256) |

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## 6.5 DEED OF CROSS GUARANTEE (CONTINUED)

Set out below is a consolidated statement of financial position as at 31 December 2017 of the Closed Group.

| | 2017 US$million | 2016 US$million |
|---|---|---|
| **Current assets** | | |
| Cash and cash equivalents | **89** | 130 |
| Trade and other receivables | **3,121** | 1,665 |
| Other current assets | **168** | 268 |
| **Total current assets** | **3,378** | 2,063 |
| **Non-current assets** | | |
| Other financial assets | **15,736** | 7,316 |
| Exploration and evaluation assets | **166** | 143 |
| Oil and gas assets | **2,372** | 1,891 |
| Other non-current assets | **524** | 1,064 |
| **Total non-current assets** | **18,798** | 10,414 |
| **Total assets** | **22,176** | 12,477 |
| **Current liabilities** | | |
| Trade and other payables | **4,971** | 1,339 |
| Other current liabilities | **146** | 154 |
| **Total current liabilities** | **5,117** | 1,493 |
| **Non-current liabilities** | | |
| Interest-bearing loans and borrowings | **9,188** | 4,053 |
| Provisions | **1,010** | 1,041 |
| Other non-current liabilities | **101** | 86 |
| **Total non-current liabilities** | **10,299** | 5,180 |
| **Total liabilities** | **15,416** | 6,673 |
| **Net assets** | **6,760** | 5,804 |
| **Equity** | | |
| Issued capital | **9,036** | 8,883 |
| Reserves | **(123)** | (823) |
| Accumulated losses | **(2,153)** | (2,256) |
| **Total equity** | **6,760** | 5,804 |

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# Notes to the Consolidated Financial Statements
# Section 7: People

This section includes information relating to the various programs the Group uses to reward and recognise our people. It includes details of our employee benefits, share-based payment schemes and key management personnel.

## 7.1 EMPLOYEE BENEFITS

### Wages, salaries and sick leave

Liabilities for wages and salaries, including non-monetary benefits that are expected to be settled within 12 months of the reporting date, are recognised in respect of employee service up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled. Expenses for non-vesting sick leave are recognised when the leave is taken and are measured at the rates paid or payable.

### Long-term service benefits

Liabilities for long service leave and annual leave that is not expected to be taken within 12 months of the respective service being provided, are recognised and measured at the present value of the estimated future cash outflows to be made in respect of employee service up to the reporting date.

### Defined benefit plan

The Group's net obligation in respect of the defined benefit superannuation plan is calculated by estimating the discounted amount of future benefits that employees have earned in relation to their service in the current and prior periods and deducting the fair value of any plan assets.

Actuarial gains or losses that arise in calculating the Group's obligation in respect of the plan are recognised directly in retained earnings.

Defined benefit members of the Santos Superannuation Plan receive a lump sum benefit on retirement, death, disablement or withdrawal. The defined benefit section of the plan is closed to new employees. All new employees receive accumulation-only benefits.

During the period, an expense of $1 million (2016: $2 million) was recorded in relation to the defined benefit plan.

The Group expects to contribute $1 million to the defined benefit superannuation plan in 2018 (2017: $2 million).

### Defined contribution plans

The Group makes contributions to several defined contribution superannuation plans. Obligations for contributions are recognised as an expense in the income statement as incurred. The amount incurred during the year was $10 million (2016: $12 million).

The following amounts are recognised in the Group's statement of financial position in relation to employee benefits:

| | **2017 US$million** | 2016 US$million |
|---|---|---|
| **Non-current assets** | | |
| Defined benefit surplus | **3** | 5 |
| **Current provisions** | | |
| Employee benefits | **49** | 45 |
| **Non-current provisions** | | |
| Employee benefits | **8** | 10 |
| Defined benefit obligations | **1** | 3 |
| Total non-current provisions | **9** | 13 |
| **Total employee benefits provisions** | **58** | 58 |

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## 7.2 SHARE-BASED PAYMENT PLANS

The Group provides benefits to employees of the Group through share-based incentives. Employees are paid for their services or incentivised for their performance in part through shares or rights over shares.

There are two main share-based payment plans: equity-settled share-based payment plans and cash-settled share-based payment plans. The equity-settled plans consist of the general employee share-based payment plans and Executive Long-Term Incentive share-based payment plans.

The amounts recognised in the income statement of the Group during the financial year in relation to shares issued under the share plans are summarised as follows:

| | Note | **2017 US$000** | 2016 US$000 |
|---|---|---|---|
| *Employee expenses:* | | | |
| General employee share plans: | | | |
| Share1000 Plan | 7.2(a)(i) | **(948)** | (1,007) |
| ShareMatch Plan (matched SARs) | 7.2(a)(i) | **(2,300)** | (3,604) |
| Executive Long-Term Incentive share-based payment plans – equity settled | 7.2(a)(ii) | **(6,120)** | (6,392) |
| Executive Short-Term Incentive share-based payment plans – equity settled | 7.2(a)(iii) | **(1,005)** | – |
| | | **(10,373)** | (11,003) |

The net impact on retained earnings from share-based payment plans, net of Treasury shares utilised in the current year, is $6 million. The impact on retained earnings from share-based payment plans in 2016 was $10 million.

# Notes to the Consolidated Financial Statements
# Section 7: People

## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

### (a) Equity-settled share-based payment plans

The cost of equity-settled transactions is determined by the fair value at the grant date using an appropriate valuation model. The cost is recognised, together with a corresponding increase in other capital reserves in equity, over the period in which the performance and/or service conditions are met. Currently, the Company has four equity-settled share-based payment plans in operation, the details of which are as follows:

#### *i. General employee share plans*

Santos operates two general employee share plans, the Share1000 Plan and the ShareMatch Plan. Eligible employees have the option to participate in either the Share1000 Plan or the ShareMatch Plan. Members of the Executive Committee ("Excom"), Directors of the Company, casual employees, employees on fixed-term contracts and employees on international assignment are excluded from participating in the Share1000 Plan and the ShareMatch Plan.

| | Share1000 | ShareMatch |
|---|---|---|
| What is it? | The Share1000 Plan provides for grants of fully paid ordinary shares up to a value determined by the Board, which in 2017 was A$1,000 per employee (2016: A$1,000). | The ShareMatch Plan allows for the purchase of shares through salary sacrificing up to A$5,000 over a maximum 12-month period, and to receive matched SARs at a 1:1 ratio or as otherwise set by the Board. |
| The employee's ownership and right to deal with them | Subject to restrictions until the earlier of the expiration of the three-year restriction period and the time when the employee ceases to be in employment. | Upon vesting, subject to restrictions until the earlier of the expiration of the restriction period (which will be three, five or seven years from the date of the offer, depending on any election made by the employee) and the time when he or she ceases to be an employee. |
| How is the fair value recognised? | The fair value of these shares is recognised as an employee expense with a corresponding increase in issued capital, and the fair value per share is determined by the Volume Weighted Average Price ("VWAP") of ordinary Santos shares on the ASX during the week up to and including the date of issue of the shares. | The fair value of the shares is recognised as an increase in issued capital and a corresponding increase in loans receivable. The fair value per share is determined by the VWAP of ordinary Santos shares on the ASX during the week up to and including the date of issue of the shares.<br>The fair value of services required in return for matched SARs granted is measured by reference to the fair value of matched SARs granted. The estimate of the fair value of the services received is measured by discounting the share price on the grant date using the assumed dividend yield and recognised as an employee expense for the term of the matched SARs. |

The following shares were issued pursuant to the employee share plans during the period:

| | | Share1000 Plan | | ShareMatch Plan | |
|---|---|---|---|---|---|
| Year | Issue date | Issued shares No. | Fair value per share A$ | Issued shares No. | Fair value per share A$ |
| **2017** | **20 Oct 2017** | **244** | **4.23** | **–** | **–** |
| **2017** | **28 Sep 2017** | **301,340** | **4.10** | **553,416** | **4.10** |
| 2016 | 1 Sep 2016 | 297,036 | 4.44 | 719,764 | 4.44 |

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## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

### *i. General employee share plans (continued)*

The number of SARs outstanding, and movements throughout the financial year are:

| Year | Beginning of the year No. | Granted No. | Lapsed No. | Vested No. | End of the year No. |
|---|---|---|---|---|---|
| **2017 Total** | **1,665,931** | **553,416** | **(70,085)** | **(384,310)** | **1,764,952** |
| 2016 Total | 1,600,103 | 719,764 | (75,118) | (578,818) | 1,665,931 |

The inputs used in the valuation of the SARs are as follows:

| **Matched SARs grant** | **2017** |
|---|---|
| Share price on grant date (A$) | **4.08** |
| Exercise price (A$) | **Nil** |
| Right life (weighted average, years) | **3** |
| Expected dividends (% p.a.) | **1.3** |
| Fair value at grant date (A$) | **3.92** |

The loan arrangements relating to the ShareMatch Plan are as follows:

During the year the Company utilised $2 million of Treasury shares (2016: issued $3 million of share capital) under the ShareMatch Plan, with $2 million (2016: $4 million) received from employees under loan arrangements. The movements in loans receivable from employees are:

| | **2017 US$000** | 2016 US$000 |
|---|---|---|
| Employee loans at 1 January | **1,350** | 2,695 |
| Ordinary share capital issued during the year | **–** | 2,622 |
| Treasury shares utilised during the year | **1,779** | – |
| Cash received during the year | **(1,869)** | (3,942) |
| Foreign exchange movement | **67** | (25) |
| **Employee loans at 31 December** | **1,327** | 1,350 |

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# Notes to the Consolidated Financial Statements
# Section 7: People

## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

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### *ii. Executive Long-Term Incentive share-based payment plans*

The Company's Executive Long-Term Incentive Program ("LTI Program") provides for eligible executives selected by the Board to receive SARs upon the satisfaction of set market and non-market performance conditions. Each SAR is a conditional entitlement to a fully paid ordinary share, subject to the satisfaction of performance or service conditions, on terms and conditions determined by the Board. The Board has the discretion to cash-settle SARs granted under the amended Santos Employee Equity Incentive Plan.

The fair value of SARs is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and recognised over the period during which the executive becomes unconditionally entitled to the SARs. The fair value of the performance-based SARs granted is measured using a Monte Carlo simulation method, taking into account the terms and market conditions upon which the SARs were granted. The fair value of the deferred-based SARs granted is measured by discounting the share price on the grant date using the assumed dividend yield for the term of the SAR. The amount recognised as an expense is only adjusted when SARs do not vest due to non-market-related conditions.

The 2017 LTI Program offers consisted only of SARs. Performance Awards were granted to eligible executives in 2017 who were granted one four-year grant (1 January 2017 – 31 December 2020).

Vesting of the grants is based on the following performance targets:

- 25% of the SARs are subject to Santos' Total Shareholder Return ("TSR") relative to the performance of the ASX 100 companies ("ASX 100 comparator group");
- 25% are subject to Santos' TSR relative to the performance of the Standard & Poor's Global 1200 Energy Index companies ("S&P GEI comparator group");
- 25% are subject to Santos' Free Cash Flow Breakeven Point ("FCFBP") relative to internal targets; and
- 25% are subject to Santos' Return on Average Capital Employed ("ROACE") relative to internal targets, measured at the end of the performance period.

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## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

### *ii. Executive Long-Term Incentive share-based payment plans (continued)*

The numbers of SARs outstanding at the end of, and movements throughout, the financial year are:

| Year | Beginning of the year No. | Granted No. | Lapsed No. | Vested No. | End of the year No. |
|---|---|---|---|---|---|
| **2017 Total** | **9,402,644** | **4,291,977** | **(2,196,369)** | **–** | **11,498,252** |
| 2016 Total | 7,650,098 | 4,799,922 | (3,047,376) | – | 9,402,644 |

The SARs granted during 2017 totalling 4,291,977 were issued across the following four tranches, each with varying valuations:

***Senior Executive LTI – granted 21 March 2017***

| | 2017 | | | |
|---|---|---|---|---|
| **Performance Awards** | **O1** | **O2** | **O3** | **O4** |
| Performance index | ASX 100 | S&P GEI | FCFBP | ROACE |
| Fair value at grant date (A$) | 2.23 | 2.29 | 3.55 | 3.55 |
| Share price on grant date (A$) | 3.73 | 3.73 | 3.73 | 3.73 |
| Exercise price (A$) | nil | nil | nil | nil |
| Expected volatility (weighted average, % p.a.) | 45 | 45 | 45 | 45 |
| Right life (weighted average, years) | 4 | 4 | 4 | 4 |
| Expected dividends (% p.a.) | 1.3 | 1.3 | 1.3 | 1.3 |
| Risk-free interest rate (% p.a.) | 2.2 | 2.2 | 2.2 | 2.2 |
| Total granted (No.) | 905,108 | 905,091 | 905,075 | 905,062 |

***CEO LTI – granted 19 May 2017***

| | 2017 | | | |
|---|---|---|---|---|
| **Performance Awards** | **O1** | **O2** | **O3** | **O4** |
| Performance index | ASX 100 | S&P GEI | FCFBP | ROACE |
| Fair value at grant date (A$) | 2.02 | 2.08 | 3.34 | 3.34 |
| Share price on grant date (A$) | 3.52 | 3.52 | 3.52 | 3.52 |
| Exercise price (A$) | nil | nil | nil | nil |
| Expected volatility (weighted average, % p.a.) | 45 | 45 | 45 | 45 |
| Right life (weighted average, years) | 4 | 4 | 4 | 4 |
| Expected dividends (% p.a.) | 1.4 | 1.4 | 1.4 | 1.4 |
| Risk-free interest rate (% p.a.) | 1.8 | 1.8 | 1.8 | 1.8 |
| Total granted (No.) | 167,911 | 167,910 | 167,910 | 167,910 |

The above tables include the valuation assumptions used for Performance Awards SARs granted during the current year. The expected vesting period of the SARs is based on historical data and current expectations and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility over a period similar to the life of the SARs is indicative of future trends, which may not necessarily be the actual outcome.

# Notes to the Consolidated Financial Statements
# Section 7: People

## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

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### *ii. Executive Long-Term Incentive share-based payment plans (continued)*

#### *Vesting of Performance Awards*

All Performance Awards are subject to hurdles based on the Company's TSR relative to both the ASX 100 and S&P GEI comparator group over the performance period, as well as the FCFBP and ROACE at the end of the vesting period. There is no re-testing of performance conditions. Each tranche of the Performance Awards subject to TSR granted during 2017 vests in accordance with the following vesting schedule:

| TSR percentile ranking | % of grant vesting |
|---|---|
| < 51st percentile | 0% |
| = 51st percentile | 50% |
| 52nd to 75th percentile | Further 2.0% for each percentile over 51st |
| ≥ 76th percentile | 100% |

#### *Restriction period*

Shares allocated on vesting of SARs granted in 2011 and 2012 may be subject to additional restrictions on dealing for five or seven years after the original grant date, depending on whether the executive elected to extend the trading restrictions period beyond the vesting date. Shares allocated on the vesting of SARs that were granted prior to 2012 will be subject to further restrictions on dealing for a maximum of 10 years after the original grant date. No amount is payable on grant or vesting of the SARs.

### *iii. Executive Deferred Short-Term Incentives ("STIs")*

#### *Deferred shares*

Deferred STIs represent a proportion of the total executive STI of the applicable year that has been deferred into shares. The deferred shares are subject to a 24-month continuous service period following the year to which the STI related. The number of deferred STIs outstanding at the end of, and movements throughout, the financial year are:

| Year | Beginning of the year No. | Granted No. | Lapsed No. | Vested No. | End of the year No. |
|---|---|---|---|---|---|
| **2017 Total** | **308,163** | **261,011** | **–** | **(308,163)** | **261,011** |
| 2016 Total | 154,409 | 308,163 | – | (154,409) | 308,163 |

On 19 April 2017 the Company issued 261,011 deferred shares to eligible executives. The share price on the grant date was A$3.66 and the fair value was A$3.57 after applying a 1.4% dividend yield assumption to the valuation.

#### *Share acquisition rights*

On 19 April 2017 the Company also issued 80,571 SARs subject to a 24-month continuous service condition starting on 1 January 2017 and ending on 31 December 2018. If this service condition is satisfied, the SARs granted will vest on 1 January 2019. The share price on the grant date was A$3.66 and the fair value was A$3.57 after applying a 1.4% dividend yield assumption to the valuation. The issued SARs represented the portion of 2016 deferred STI which was allocated to eligible executives as SARs rather than deferred shares.

### *iv. Executive sign-on grants*

a. On 11 February 2016 the Company issued 333,822 SARs split across two tranches, as follows:

- 50% (166,911) which were subject to a 12-month continuous service condition starting on 1 February 2016 and ending on 31 January 2017. As this service condition was satisfied, the SARs vested on 1 February 2017; and
- 50% (166,911) were subject to as 24-month continuous service condition starting on 1 February 2016 and ending on 31 January 2018. If this service condition is satisfied, the SARs will vest on 1 February 2018.

The share price on the grant date was A$3.05 and the fair values were A$2.95 (12-month term) and A$2.86 (24-month term) after applying a 3.3% dividend yield assumption to the valuation.

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## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

***iv. Executive sign-on grants (continued)***

b. On 11 July 2016 the Company issued 42,585 SARs subject to a 24-month continuous service condition starting on 1 May 2016 and ending on 30 April 2018. If this service condition is satisfied, the SARs will vest on 1 February 2018.

The share price on the grant date was A$4.80 and the fair value was A$4.61 after applying a 2.2% dividend yield assumption to the valuation.

c. On 1 December 2016 the Company issued 23,777 SARs subject to a 12-month continuous service condition starting on 1 December 2016 and ending on 30 November 2017, which vested on 1 December 2017.

The share price on the grant date was A$4.39 and the fair value was A$4.29 after applying a 2.2% dividend yield assumption to the valuation.

### (b) Options

The Company has not granted options over unissued shares under the Executive Long-Term Incentive share-based payment plans since 2009. The information as set out below relates to options issued under the Executive Long-Term Incentive share-based payment plans in 2009 and earlier that have vested in prior years:

| | Beginning of the year No. | Lapsed No. | Exercised No. | End of the year No. | Exercisable at end of the year No. |
|---|---|---|---|---|---|
| **2017** | | | | | |
| **Vested in prior years** | **1,159,288** | **(351,300)** | **–** | **807,988** | **807,988** |
| **Weighted average exercise price (A$)** | **15.01** | **13.76** | **–** | **15.55** | **15.55** |
| 2016 | | | | | |
| Vested in prior years | 3,922,588 | (2,763,300) | – | 1,159,288 | 1,159,288 |
| Weighted average exercise price (A$) | 12.38 | 11.28 | – | 15.01 | 15.01 |

### (c) Cash-settled share-based payment plans

The Group recognises the fair value of cash-settled share-based payment transactions as an employee expense with a corresponding increase in the liability for employee benefits. The fair value of the liability is measured initially, and at the end of each reporting period until settled, at the fair value of the cash-settled share-based payment transaction, by using a Monte Carlo simulation method.

## 7.3 KEY MANAGEMENT PERSONNEL DISCLOSURES

### (a) Key management personnel compensation

| | 2017 US$000 | 2016 US$000 |
|---|---|---|
| Short-term employee benefits | **7,306** | 6,444 |
| Post-employment benefits | **195** | 194 |
| Other long-term benefits | **80** | 29 |
| Termination benefits | **288** | 836 |
| Share-based payments | **2,277** | 2,631 |
| | **10,146** | 10,134 |

### (b) Loans to key management personnel

There have been no loans made, guaranteed or secured, directly or indirectly, by the Group or any of its subsidiaries at any time throughout the year to any key management person, including their related parties.

# Notes to the Consolidated Financial Statements
# Section 8: Other

This section provides information that is not directly related to the specific line items in the financial statements, including information about contingent liabilities, events after the end of the reporting period, the Group's commitment to the removal of the shareholder cap, remuneration of auditors and changes to accounting policies and disclosures.

## 8.1 CONTINGENT LIABILITIES

Contingent liabilities arise in the ordinary course of business through claims against the Group, including contractual, third-party and contractor claims. In most instances it is not possible to reasonably predict the outcome of these claims, and as at reporting date the Group believes that the aggregate of such claims will not materially impact the Group's financial report.

## 8.2 EVENTS AFTER THE END OF THE REPORTING PERIOD

On 20 February 2018, the Directors of Santos Limited resolved not to pay a final dividend in respect of the 2017 financial year.

## 8.3 COMMITMENT ON REMOVAL OF SHAREHOLDER CAP

Pursuant to a Deed of Undertaking to the Premier of South Australia dated 16 October 2007, and as a consequence of the enactment of the *Santos Limited (Deed of Undertaking) Act 2007* on 29 November 2007, Santos agreed to:

- continue to make payments under its existing Social Responsibility and Community Benefits Program specified in the Deed totalling A$60 million over a 10-year period from the date the legislation was enacted. As at 31 December 2017, this condition has been fully met; and
- continue to maintain the South Australian Cooper Basin asset's Head Office and Operational Headquarters together with other roles in South Australia for 10 years subsequent to the date the legislation was enacted. At 31 December 2017 this condition has been fully met. If this condition had not been met, the Company would have been liable to pay a maximum of A$50 million to the State Government of South Australia.

Santos was required to make these payments only if the State Government of South Australia did not reintroduce a shareholder cap on the Company's shares or introduce any other restriction on, or in respect of, the Company's Board or senior management which had an adverse discriminatory effect in their application to the Company relative to other companies domiciled in South Australia.

## 8.4 REMUNERATION OF AUDITORS

The auditor of Santos Limited is Ernst & Young.

### (a) Audit and review services

Amounts received or due and receivable for an audit or review of the financial report of the entity and any other entity in the Group by:

| | **2017 US$000** | 2016 US$000 |
|---|---|---|
| Ernst & Young (Australia) | **1,047** | 1,070 |
| Overseas network firms of Ernst & Young (Australia) | **116** | 150 |
| | **1,163** | 1,220 |

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## 8.4 REMUNERATION OF AUDITORS (CONTINUED)

### (b) Other services

Amounts received or due and receivable for other services in relation to the entity and any other entity in the Group by:

| | 2017 US$000 | 2016 US$000 |
|---|---|---|
| Ernst & Young (Australia) for other assurance services | **401** | 360 |
| Ernst & Young (Australia) for taxation and other services | **341** | 2 |
| Overseas network firms of Ernst & Young (Australia) for taxation services | **14** | 14 |
| | **756** | 376 |

## 8.5 ACCOUNTING POLICIES

### (a) Changes in accounting policies and disclosures

The Group applied the following amendments to accounting standards applicable for the first time for the financial year beginning 1 January 2017:

- AASB 2016-1 *Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses*;
- AASB 2016-2 *Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107*; and
- AASB 2017-2 *Amendments to Australian Accounting Standards – Further Annual Improvements 2014-2016 Cycle*.

The adoption of these amendments did not have any impact on the amounts recognised in prior periods and will also not affect the current or future periods.

The amendments to AASB 107 require disclosure of changes in liabilities arising from financing activities (refer note 4.1(d)).

In addition, several other standard amendments and interpretations were applicable for the first time in 2017, but were not relevant to the Company and do not impact the Group's annual consolidated financial statements or half-year condensed financial statements.

### (b) Adoption of AASB 9 – *Financial Instruments*

The Group elected to early adopt AASB 9 *Financial Instruments* from 1 January 2017. AASB 9 replaces AASB 139 *Financial Instruments: Recognition and Measurement*, and generally simplifies the classification and measurement of financial instruments, introduces a new expected credit loss model for calculating impairment of financial assets, and aligns hedge accounting more closely with an entity's risk management practices.

The Group has applied the new hedge accounting requirement prospectively, while the remainder of the requirements of AASB 9 have been applied retrospectively in line with the requirements of the standard.

The adoption of AASB 9 results in the following key changes in the Group's accounting and reporting:

- For the Group's financial liabilities that are measured at fair value through profit or loss ("FVTPL"), the element of gains or losses attributable to changes in the Group's own credit risk will now be recognised in other comprehensive income ("OCI") instead of profit or loss. During the year ended 31 December 2017 this amounted to a $21 million loss.
- Hedge effectiveness testing will now be performed on a prospective basis with no defined numerical range of effectiveness applied in this testing.
- The Group holds an equity investment previously measured at cost under AASB 139 which is now measured at FVOCI. An opening adjustment of $5 million loss has been recognised in retained earnings upon initial measurement under AASB 9.

# Notes to the Consolidated Financial Statements
# Section 8: Other

## 8.5 ACCOUNTING POLICIES (CONTINUED)

### (b) Adoption of AASB 9 – *Financial Instruments* (continued)

The table below shows changes in the classification and measurement categories of the Group's financial instruments on adoption of AASB 9.

| AASB 139 (previous) classification of financial instrument | Impact of AASB 9 | AASB 139 (previous) measurement category | Impact of AASB 9 |
|---|---|---|---|
| Cash and cash equivalents | No change | Amortised cost | No change |
| Term deposits | No change | Amortised cost | No change |
| Trade and other receivables | No change | Amortised cost | No change |
| Hedging instruments (financial derivatives) | No change | FVTPL (fair value hedges) | FVTPL[1] |
| | | FVOCI (cash flow hedges) | No change |
| Commodity derivatives | No change | FVTPL | No change |
| Available-for-sale financial assets | Equity investments | Cost | FVOCI |
| Amounts held in escrow | No change | Amortised cost | No change |
| Trade and other payables | No change | Amortised cost | No change |
| Interest-bearing loans and borrowings | No change | Amortised cost | No change |
| | | FVTPL | No change |

1. Gains or losses attributable to changes in the Group's own credit risk are recognised in OCI instead of profit or loss.

No other changes arising from the adoption of AASB 9 have had a material effect on the financial reporting of the Group.

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## 8.5 ACCOUNTING POLICIES (CONTINUED)

### (c) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual reporting periods beginning on or after 1 January 2018, and have not been applied in preparing these consolidated financial statements. The Group's assessment of the impact of these new standards, amendments to standards and interpretations is set out below.

| Reference | Description | Application of standard | Impact on Group financial report |
|---|---|---|---|
| AASB 15 *Revenue from Contracts with Customers* | AASB 15 as issued replaces AASB 111 *Construction Contracts*, AASB 118 *Revenue* and related IFRIC Interpretations. The core principle of AASB 15 is that an entity recognises revenue in accordance with the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity recognises revenue in accordance with that core principle by applying the following steps:<br>Step 1: Identify the contract(s) with a customer;<br>Step 2: Identify the performance obligations in the contract;<br>Step 3: Determine the transaction price;<br>Step 4: Allocate the transaction price to the performance obligations in the contract; and<br>Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation. | 1 January 2018 – the Group intends to adopt the standard using the full retrospective approach. | In the current year, a project team was established comprising appropriate revenue subject matter specialists, with a detailed review of AASB 15 and relevant industry guidance being performed, in addition to a detailed review of revenue contracts entered into during the transition period of the standard.<br>As a result of the assessment, it is concluded there will be no material adjustments to profit or retained earnings on adoption of AASB 15.<br>There will be a change from the "entitlements method" to "sales method" of accounting. The sales method results in recording revenue in accordance with amounts invoiced to customers, as opposed to the Group's percentage interest in a producing asset.<br>The product sales and cost of sales line items in the consolidated income statement will also be subject to insignificant adjustments of equal, or similar, amounts due to revised accounting for the Group's gas swap arrangements. The Group estimates the impact on each line item to be approximately US$10 million.<br>Further reclassifications from other revenue to revenue will also arise where amounts recorded in other revenue are deemed under AASB 15 to constitute contracts with customers. |

# Notes to the Consolidated Financial Statements
# Section 8: Other

## 8.5 ACCOUNTING POLICIES (CONTINUED)

| Reference | Description | Application of standard | Impact on Group financial report |
|---|---|---|---|
| AASB 16 *Leases* | The key features of AASB 16 on lessee accounting are as follows:<br>• Lessees are required to recognise right-of-use assets and lease liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value.<br>• A lessee measures right-of-use assets similarly to other non-financial assets (such as property, plant and equipment) and lease liabilities similarly to other financial liabilities.<br>• Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease.<br>• AASB 16 contains disclosure requirements for lessees. | 1 January 2019 | The group only operates as a lessee. The standard will affect primarily the accounting for the Group's operating leases. As at the reporting date, the Group has non-cancellable operating lease commitments of US$271 million (refer note 3.5).<br>The Group has not yet completed its assessment of what adjustments, if any, are necessary on adoption of AASB 16. Adjustments may arise from:<br>• changes in the definition of the lease term;<br>• different treatments of variable lease payments; and<br>• available extension and termination options.<br>It is therefore not yet possible to estimate the amount of right-of-use assets and lease liabilities that will have to be recognised on adoption of the new standard and how this may affect the Group's profit or loss and classification of cash flows going forward. |

Several other amendments to standards and interpretations will apply on or after 1 January 2018, and have not yet been applied, however they are not expected to impact the Group's annual consolidated financial statements or half-year condensed consolidated financial statements.

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# Directors' Declaration
## For the year ended 31 December 2017

In accordance with a resolution of the Directors of Santos Limited ("the Company"), we state that:

1. In the opinion of the Directors:
   (a) the financial statements and notes of the consolidated entity are in accordance with the *Corporations Act 2001* (Cth), including:
      (i) giving a true and fair view of the consolidated entity's financial position as at 31 December 2017 and of its performance for the year ended on that date; and
      (ii) complying with Accounting Standards and the *Corporations Regulations 2001* (Cth); and
   (b) the financial statements and notes comply with International Financial Reporting Standards as disclosed in note 1.1; and
   (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.
2. This declaration has been made after receiving the declarations required to be made to the Directors in accordance with section 295A of the *Corporations Act 2001* (Cth) for the financial year ended 31 December 2017.
3. As at the date of this declaration, there are reasonable grounds to believe that the members of the Closed Group identified in note 6.5 will be able to meet any obligations or liabilities to which they are or may become subject by virtue of the Deed of Cross Guarantee between the Company and those members of the Closed Group pursuant to ASIC Corporations (Wholly-owned Companies) Instrument 2016/785.

Dated this 20th day of February 2018

On behalf of the Board:



Director

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# Independent Auditor's Report
to the members of Santos Limited

## Report on the Audit of the Financial Report

### *Opinion*

We have audited the financial report of Santos Limited ("the Company") and its subsidiaries (collectively, "the Group"), which comprises the consolidated statement of financial position as at 31 December 2017, the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, notes to the financial statements, including a summary of significant accounting policies, and the Directors Declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

(a) giving a true and fair view of the consolidated financial position of the Group as at 31 December 2017 and of its consolidated financial performance for the year ended on that date; and

(b) complying with Australian Accounting Standards and the *Corporations Regulations 2001.*

### Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* ("the Code") that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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

### Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

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**Estimation of oil and gas reserves and resources**

| Why significant | How our audit addressed the key audit matter |
|---|---|
| Estimation of oil and gas reserves and resources was conducted by specialist engineers, requiring significant judgment and the use of a number of assumptions, particularly those disclosed in note 3.2 of the financial report, by the Group.<br><br>These estimates can have a material impact on the financial report and the results of the Group, primarily in the following areas:<br><br>• capitalisation and classification of expenditure as exploration and evaluation (E&E) assets (refer note 3.1), or oil and gas (O&G) assets (note 3.2);<br><br>• valuation of oil and gas assets and impairment testing (note 3.3);<br><br>• calculation of depreciation, depletion and amortisation ("DD&A") of assets (note 3.2); and<br><br>• the calculation of decommissioning and restoration provisions (note 3.4). | Our audit procedures focused on the work of the Group's experts and included the following:<br><br>• assessed the qualifications, competence and objectivity of both the Group's internal and external experts involved in the estimation process;<br><br>• evaluated the adequacy of the experts' work to determine if the work undertaken was appropriate;<br><br>• considered the Group's reserves estimation process and controls, including Santos' internal certification process for technical and commercial experts who are responsible for reserves, and the design of Santos Reserves Guidelines and Reserves Management Process and its alignment with the guidelines prepared by the Society of Petroleum Engineers ("SPE");<br><br>• assessed the Group's controls over the estimation process, to assess and approve the reserves and resources volumes in accordance with the guidelines prepared by the SPE;<br><br>• assessed that key economic assumptions used in the estimation of reserves and resources volumes were consistent with those utilised by the Group in the impairment testing of exploration and evaluation and oil and gas assets, where applicable;<br><br>• analysed the reasons for reserve revisions, or the absence of reserves revisions where expected, and assessed changes in reserves or lack of changes in reserves for consistency with other information that we obtained throughout the audit; and<br><br>• agreed the reserves and resources volumes to the applicable financial information, including the calculation of DD&A, valuation of assets and impairment testing, and the calculation of decommissioning provisions, as applicable. |

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# Independent Auditor's Report
to the members of Santos Limited
(continued)

**Recovery of carrying value of exploration and evaluation and oil and gas assets**

| Why significant | How our audit addressed the key audit matter |
|---|---|
| Under Australian Accounting Standards, an entity shall assess throughout the reporting period whether there is any indication that an asset may be impaired, or that reversal of a previously recognised impairment may be required. If any such indication exists, an entity shall estimate the recoverable amount of the asset. Impairment indicators were present during the period for certain cash-generating units ("CGUs") and impairment testing was undertaken.<br><br>The impairment testing process is complex and highly judgmental and is based on assumptions and estimates that are affected by expected future performance and market conditions. Key assumptions, judgments and estimates used in the formulation of the Group's impairment of exploration and evaluation assets and oil and gas assets are set out in the financial report in note 3.3.<br><br>During the period, the Group has recognised impairment of certain CGUs, including the GLNG CGU, and an impairment reversal on the Cooper Basin CGU. A net impairment expense of US$0.9 billion pertaining to exploration and evaluation assets and oil and gas assets has been recorded. Refer to note 3.3 in the financial report. | We evaluated the assumptions and methodologies used by the Group and the estimates made. In particular we considered those estimates and judgments relating to the forecast cash flows and the inputs used to formulate those cash flows, such as discount rates, reserves and resources, inflation rates, operating and capital costs, foreign exchange rates and commodity prices.<br><br>We involved our valuation specialists to assist in these procedures. Our audit procedures were undertaken across all material CGUs with the extent of procedures commensurate with the level of impairment risk.<br><br>Specifically, we evaluated the discounted cash flow models and other data supporting the Group's assessment. In doing so, we:<br><br>• understood future production profiles compared to latest reserves and resources estimates, as outlined in the key audit matter above, current sanctioned budgets and historical operations;<br><br>• evaluated commodity price assumptions with reference to contractual arrangements, market prices (where available), broker consensus, analyst views and historical performance;<br><br>• evaluated discount rates and foreign exchange rates with reference to risk-free rates, market indices, applicable tax rates, market risk and country risk premia, broker consensus, and historical performance;<br><br>• compared future operating and development expenditure to current sanctioned budgets and historical expenditure, and ensured variations were in accordance with our expectations based upon other information obtained throughout the audit; and<br><br>• tested the mathematical accuracy of the Group's discounted cash flow models.<br><br>We also considered the adequacy of the financial report disclosures regarding impairment and the recoverable amount of the Group's assets. |

**Decommissioning and restoration provisions**

| Why significant | How our audit addressed the key audit matter |
|---|---|
| The calculation of decommissioning and restoration provisions is conducted by both internal and external specialist engineers and requires judgment in respect of asset lives, timing of restoration work being undertaken, environmental legislative requirements, the extent of restoration activities required and estimation of future costs.<br><br>The judgments and estimates made can have a material impact on the financial report. The Group has recognised decommissioning and restoration provisions of US$1.5 billion at 31 December 2017 which are disclosed in note 3.4. | Our audit procedures focused on the work of the Group's experts, and included the following:<br><br>• assessed the competence and objectivity of both the Group's internal and external experts involved in the estimation process;<br><br>• evaluated the adequacy of the experts' work to determine whether their work was appropriate;<br><br>• evaluated the Group's decommissioning and restoration estimation processes;<br><br>• assessed the Group's controls over the restoration estimation process;<br><br>• tested the consistency of the application of principles and assumptions to other areas of the audit, such as reserves estimation and impairment testing;<br><br>• tested the mathematical accuracy of the Group's present value calculations and considered the appropriateness of the discount rate applied in the calculation; and<br><br>• agreed the calculations to the financial report. |

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**Accounting for deferred tax and Petroleum Resource Rent Tax**

| Why significant | How our audit addressed the key audit matter |
|---|---|
| The financial report of the Group includes deferred tax assets arising from income taxes, including in respect of income tax losses, and Petroleum Resource Rent Tax (PRRT). The determination of the quantum, likelihood and timing of the realisation of deferred tax assets arising from income taxes and PRRT is judgmental, due to the interpretation of PRRT and income tax legislation, as well as the estimation of future taxable income.<br><br>The Group recognised a net deferred tax asset of US$1.2 billion at 31 December 2017 in respect of corporate income tax, which is disclosed in note 2.4 of the financial report. | We assessed the Group's determination of tax payable now and in the future. We involved our taxation specialists to assist in this assessment.<br><br>We considered the Group's methodologies, assumptions and estimates in relation to the calculation of current taxes and the likelihood of generating future taxable profits to support the recognition of deferred tax assets. We considered forecasts of taxable profits and the consistency of these forecasts with the Group's budgets approved by the Board and those used in the Group's asset impairment testing.<br><br>We evaluated the assessment of estimates and assumptions made through enquiries with the Group's taxation department, reviewed correspondence with local tax authorities and involved our tax specialists, where appropriate, to assess the associated provisions and disclosures.<br><br>We assessed the Group's disclosures in respect of PRRT and Income Taxes which are included in the summary of significant accounting policies in note 2.4. |

**Information Other than the Financial Report and Auditor's Report Thereon**

The Directors are responsible for the other information. The other information comprises the information included in the Company's 2017 Annual Report, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

**Responsibilities of the Directors 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 gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

**Auditor's Responsibilities for the Audit of the Financial Report**

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

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# Independent Auditor's Report
to the members of Santos Limited
(continued)

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Directors with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the Directors, we determine those matters that were of most significance in the audit of the financial report of the current year and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

**Report on the Audit of the Remuneration Report**

***Opinion on the Remuneration Report***

We have audited the Remuneration Report included in pages 34 to 53 of the Directors' Report for the year ended 31 December 2017.

In our opinion, the Remuneration Report of Santos Limited for the year ended 31 December 2017 complies with section 300A of the *Corporations Act 2001*.

***Responsibilities***

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.

Ernst & Young

**Ernst & Young**

**R J Curtin**
Partner
Adelaide
20 February 2018

**L A Carr**
Partner

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# Auditor's Independence Declaration
to the Directors of Santos Limited

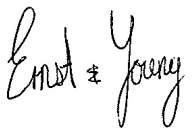
Auditor's Independence Declaration to the Directors of Santos Limited

As lead auditor for the audit of Santos Limited for the financial year ended 31 December 2017, I declare 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 Santos Limited and the entities it controlled during the financial year.



**Ernst & Young**



**R J Curtin**
Partner
Adelaide
20 February 2018

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# Securities Exchange and Shareholder Information

Listed on the Australian Securities Exchange at 31 January 2018 were 2,082,911,041 fully paid ordinary shares. Unlisted were 12,500 partly paid Plan 0 shares, 12,500 partly paid Plan 2 shares, 94,759 restricted fully paid ordinary shares issued to eligible Senior Executives pursuant to the Santos Employee Share Purchase Plan ("SESPP"), 10,979 fully paid ordinary shares issued pursuant to the Non-executive Director Share Plan ("NED Share Plan"), 48,722 fully paid ordinary shares issued with further restrictions pursuant to the ShareMatch Plan and 5,378 fully paid ordinary shares issued with further restrictions pursuant to the SESPP.

There were 132,026 holders of all classes of issued ordinary shares, including: 2 holders of Plan 0 shares; 2 holders of Plan 2 shares; 17 holders of restricted shares pursuant to the SESPP; 1 holder of NED Share Plan shares: 41 holders of ShareMatch shares with further restrictions and 1 holder of SESPP shares with further restrictions. This compared with 148,925 holders of all classes of issued ordinary shares a year earlier.

On 20 January 2018 there were also: 34 holders of 807,988 Options granted pursuant to the Santos Executive Share Option Plan; 99 holders of 10,585,224 Share Acquisition Rights pursuant to the SESPP and 1,034 holders of 1,775,865 Share Acquisition Rights pursuant to the ShareMatch Plan.

The listed issued ordinary shares plus the ordinary shares issued pursuant to the SESPP, and the restricted shares issued pursuant to the SESPP, ShareMatch Plan and NED Share Plan represent all of the voting power in Santos. The holdings of the 20 largest holders of ordinary shares represent 68.32% of the total voting power in Santos (64.43% on 31 January 2017). The largest shareholders of fully paid ordinary shares in Santos as shown in the Company's Register of Members at 31 January 2018 were:

| Name | No. of shares | % |
|---|---|---|
| HSBC Custody Nominees (Australia) Limited | 464,530,367 | 22.30 |
| Citicorp Nominees Pty Limited | 325,778,721 | 15.64 |
| JP Morgan Nominees Australia Limited | 266,461,014 | 12.79 |
| United Faith Ventures Limited | 140,189,820 | 6.73 |
| National Nominees Limited | 116,493,663 | 5.59 |
| BNP Paribas Nominees Pty Ltd <Agency Lending DRP A/c> | 29,039,169 | 1.39 |
| BNP Paribas Noms Pty Ltd <DRP> | 14,935,279 | 0.72 |
| Argo Investments Limited | 12,990,748 | 0.62 |
| HSBC Custody Nominees (Australia) Limited <NT-Comnwlth Super Corp A/c> | 11,041,641 | 0.53 |
| Citicorp Nominees Pty Limited <Colonial First State Inv A/c> | 9,206,425 | 0.44 |
| AMP Life Limited | 8,098,468 | 0.39 |
| HSBC Custody Nominees (Australia) Limited-GSCO ECA | 4,158,236 | 0.20 |
| Dynamic Supplies Investments Pty Ltd | 4,091,868 | 0.20 |
| CS Third Nominees Pty Limited <HSBC Cust Nom Au Ltd 13 A/c> | 3,385,827 | 0.16 |
| UBS Nominees Pty Ltd | 3,135,000 | 0.15 |
| BNP Paribas Nominees Pty Ltd <IB AU Noms Retailclient DRP> | 2,689,148 | 0.13 |
| Custodial Services Limited <Beneficiaries Holding A/c> | 2,327,300 | 0.11 |
| Citicorp Nominees Pty Limited <Citibank NY ADR Dep A/c> | 2,238,064 | 0.11 |
| Nulis Nominees (Australia) <Navigator Mast Plan Sett A/c> | 2,048,203 | 0.10 |
| Navigator Australia Ltd <MLC Investment Sett A/c> | 2,027,227 | 0.10 |
| **Total:** | **1,424,866,188** | **68.41** |

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## ANALYSIS OF SHARES – RANGE OF SHARES HELD

| | Fully paid ordinary shares (holders) | % of holders | % of shares held |
|---|---|---|---|
| 1-1,000 | 44,408 | 33.65 | 1.02 |
| 1,001-5,000 | 57,140 | 43.30 | 6.95 |
| 5,001-10,000 | 16,997 | 12.88 | 5.88 |
| 10,001-100,000 | 13,048 | 9.88 | 13.41 |
| 100,001 and over | 369 | 0.28 | 72.74 |
| **Total** | **131,962** | **100.00** | **100.00** |

Substantial Shareholders as disclosed by notices received by the Company as at 13 February 2018:

| Name | Number of voting shares held | Date of Notice |
|---|---|---|
| Hony Partners Group, L.P. and others | 309,734,518* | 5 May 2017 |
| ENN Ecological Holdings Co Ltd and others | 314,734,518* | 5 May 2017 |
| Santos Limited | 318,192,274* | 27 June 2017 |

* At 27 June 2017, Hony held approximately 4.8% of Santos' issued capital and ENN held approximately 10.31%. Hony and ENN have a relevant interest in each other's shares by reason of an Acting in Concert agreement dated 27 April 2017. Santos has a relevant interest in the shareholdings of Hony and ENN by reason of the Strategic Relationship agreement announced by Santos on 27 June 2017.

For Directors' shareholdings see the Directors' Report as set out on page 16 of this Annual Report.

## VOTING RIGHTS

Every member present in person or by an attorney, a proxy or a representative shall on a show of hands, have one vote and upon a poll, one vote for every fully paid ordinary share held. Pursuant to the Rules of the Santos Executive Share Plan, Plan 2 and Plan 0 shares do not carry any voting rights except on a proposal to vary the rights attached to Plan shares.

# Glossary

**barrel/bbl**
The standard unit of measurement for all oil and condensate production. One barrel = 159 litres or 35 imperial gallons.

**Boe**
Barrels of oil equivalent.

**the company**
Santos Ltd and all its subsidiaries.

**condensate**
A natural gas liquid that occurs in association with natural gas and is mainly composed of pentane and heavier hydrocarbon fractions.

**contingent resources (2C)**
Those quantities of hydrocarbons which are estimated, on a given date, to be potentially recoverable from known accumulations, but which are not currently considered to be commercially recoverable. Contingent resources may be of a significant size, but still have constraints to development. These constraints, preventing the booking of reserves, may relate to lack of gas marketing arrangements or to technical, environmental or political barriers.

**crude oil**
A general term for unrefined liquid petroleum or hydrocarbons.

**EBITDAX**
Earnings before interest, tax, depreciation, depletion, exploration and impairment.

**exploration**
Drilling, seismic or technical studies undertaken to identify and evaluate regions or prospects with the potential to contain hydrocarbons.

**hydrocarbon**
Compounds containing only the elements hydrogen and carbon, which may exist as solids, liquids or gases.

**joules**
Joules are the metric measurement unit for energy.

A gigajoule (GJ) is equal to 1 joule × $10^9$

A terajoule (TJ) is equal to 1 joule × $10^{12}$

A petajoule (PJ) is equal to 1 joule × $10^{15}$

**liquid hydrocarbons (liquids)**
A sales product in liquid form; for example, condensate and LPG.

**LNG**
Liquefied natural gas. Natural gas that has been liquefied by refrigeration to store or transport it. Generally, LNG comprises mainly methane.

**Lost-Time Injury Frequency Rate (LTIFR)**
A statistical measure of health and safety performance, calculated by the number of hours worked. A lost-time injury is a work-related injury or illness that results in a persons disability, or time lost from work of one day shift or more.

**LPG**
Liquefied petroleum gas. A mixture of light hydrocarbons derived from oilbearing strata which is gaseous at normal temperatures but which has been liquefied by refrigeration or pressure to store or transport it. Generally, LPG comprises mainly propane and butane.

**market capitalisation**
A measurement of a company's stock market value at a given date. Market capitalisation is calculated as the number of shares on issue multiplied by the closing share price on that given date.

**mmbbl**
million barrels

**mmboe**
million barrels of oil equivalent.

**mtpa**
million tonnes per annum

**oil**
A mixture of liquid hydrocarbons of different molecular weights.

**proved reserves (1P)**
Reserves that, to a high degree of certainty (90% confidence), are recoverable. There is relatively little risk associated with these reserves. Proved developed reserves are reserves that can be recovered from existing wells with existing infrastructure and operating methods. Proved undeveloped reserves require development.

**proved plus probable reserves (2P)**
Reserves that analysis of geological and engineering data suggests are more likely than not to be recoverable. There is at least a 50% probability that reserves recovered will exceed proved plus probable reserves.

**sales gas**
Natural gas that has been processed by gas plant facilities and meets the required specifications under gas sales agreements.

**Santos**
Santos Limited and its subsidiaries.

**seismic survey**
Data used to gain an understanding of rock formations beneath the earth's surface using reflected sound waves.

**t**
tonnes

**total recordable case frequency rate (TRCFR)**
A statistical measure of health and safety performance. Total recordable case frequency rate is calculated as the total number of recordable cases (medical treatment injuries and lost-time injuries) per million hours worked.

**Conversion factors**

| | |
|---|---|
| Sales gas and ethane | 1 PJ = 171.937 boe x $10^3$ |
| Crude oil | 1 barrel = 1 boe |
| Condensate | 1 barrel = 0.935 boe |
| LPG | 1 tonne = 8.458 boe |
| LNG | 1 PJ = 18,040 tonnes |
| LNG | 1 tonne = 52.54 mmBtu |

For a comprehensive online conversion calculator tool, please visit our homepage at **www.santos.com**

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# Corporate Directory

Santos Limited ABN 80 007 550 923

## SECURITIES EXCHANGE LISTING

Santos Limited. Incorporated in Adelaide, South Australia, on 18 March 1954.

Quoted on the official list of the Australian Securities Exchange (ordinary shares code STO).

## COMPANY SECRETARY

Christian Paech joined Santos in 2004 and was appointed to the role of General Counsel in 2010 and Company Secretary in 2017. He has over 20 years' experience in commercial and corporate law and governance, including in private practice with Herbert Smith Freehills and Ashurst. He holds a Bachelor of Commerce and a Bachelor of Laws (Honours) from the University of Adelaide.

Amanda Devonish joined Santos in 2012 and was appointed to the role of Company Secretary in 2017. She has over 14 years' experience in commercial and corporate legal practice. She holds a Bachelor of Commerce and a Bachelor of Laws from the University of Adelaide.

## REGISTERED AND HEAD OFFICE

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## SHARE REGISTER

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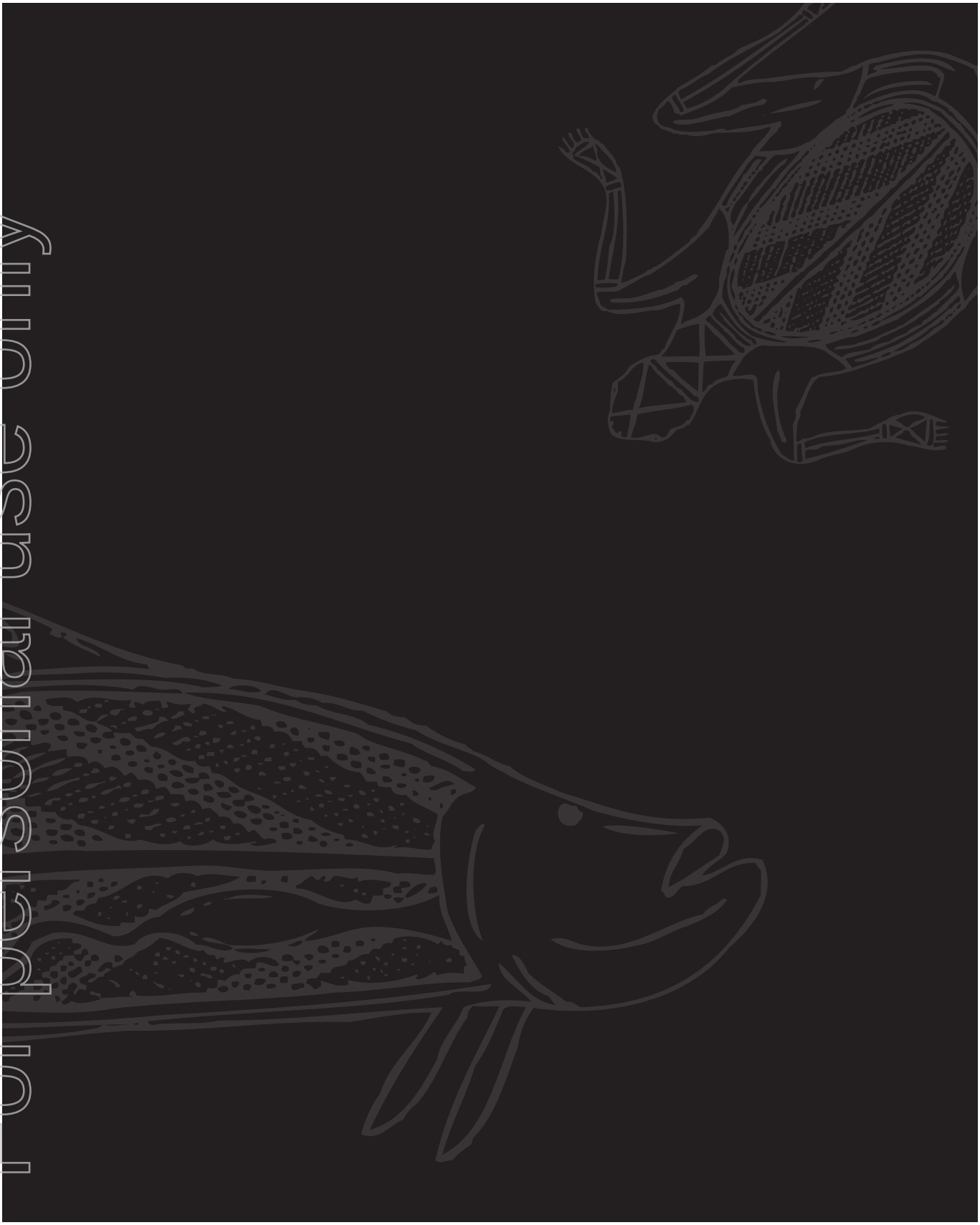
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