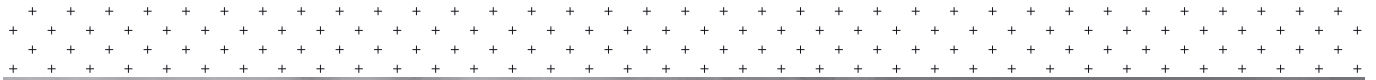


# Transform Build Grow

Annual  
Report  
2016



**Santos**

This *2016 Annual Report* is a summary of Santos' operations, activities and financial position as at 31 December 2016.

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](http://www.santos.com)

Santos' Corporate Governance Statement can be viewed at: [www.santos.com/who-we-are/corporate-governance](http://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 is proud to deliver the economic and environmental benefits of natural gas to homes and businesses throughout Australia and Asia.**

Five core long-life natural gas assets sit at the heart of a disciplined, focused strategy to drive sustainable shareholder value: the Cooper Basin, GLNG, Papua New Guinea, Northern Australia and Western Australia Gas. Each of these 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.

The Santos turnaround is now well underway. A three phase strategy to Transform, Build and Grow the business will drive returns as we continue to focus on the exploration, development, production and sale of natural gas.

Santos is focused on driving sustainable shareholder value by becoming a low-cost, reliable and high performance business with the financial flexibility to build and grow the business through the oil price cycle.

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# Corporate Directory

Santos Limited ABN 80 007 550 923

## SECURITIES EXCHANGE LISTING

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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

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David Lim joined Santos in 2007 and was appointed to the role of Company Secretary in 2010. He has over 20 years of experience in commercial and corporate legal practice. He is an accredited Chartered Secretary, and holds a Bachelor of Economics and a Bachelor of Laws from the University of Adelaide.

## REGISTERED AND HEAD OFFICE

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Ground Floor Santos Centre  
60 Flinders Street  
Adelaide SA 5000  
Australia

GPO Box 2455  
Adelaide SA 5001  
Australia

Telephone: +61 8 8116 5000  
Facsimile: +61 8 8116 5050  
Website: [www.santos.com](http://www.santos.com)

## SHARE REGISTER

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Computershare Investor Services Pty Ltd  
Yarra Falls, 452 Johnston Street  
Abbotsford VIC 3067  
Australia

GPO Box 2975  
Melbourne VIC 3001  
Australia

Online enquiries: [www.investorcentre.com/contact](http://www.investorcentre.com/contact)  
Website: [www.investorcentre.com/sto](http://www.investorcentre.com/sto)

Telephone: 1300 017 716 (within Australia)  
+61 3 9938 4343 (international)



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

## Peter Coates and Kevin Gallagher

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Dear Shareholder,

2016 was a year of transformational change for Santos. With the oil price trading at less than US\$30 per barrel at the start of the year, decisive action was taken to stabilise the business and increase operating cash flow. The aim was to be free cash flow breakeven at US\$35-40 per barrel on a portfolio basis. The key strategic imperative was to create shareholder value by becoming a low-cost, reliable, high performance business and position Santos to deliver positive cash returns through the cycle.

A new leadership team with strong technical expertise was established. Stronger levels of governance and central controls were also implemented around key decision making and planning processes. A new operating model was embraced to focus on our primary business of exploration, development, production and sales of natural gas both onshore and offshore.

As a result of the changes implemented by the Board and management, Santos is beginning to turnaround. The free cash flow breakeven oil price was reduced from US\$47 per barrel at the start of the year to US\$36.50 per barrel by year-end. Santos generated \$370 million positive free cash flow over the last eight months of 2016 resulting in a net \$206 million of free cash flow for the full-year, before asset sales. Whilst these results are pleasing and faster than anticipated, we recognise that there is still more to do and we will continue to focus on sustainably driving costs out of the business in the coming year.

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### OPERATIONAL PERFORMANCE

Operations continued to perform well, with annual sales volumes up 31% to a record 84.1 million barrels of oil equivalent (mboe) reflecting a ramp up in LNG from GLNG train 1 and first LNG from train 2 in May 2016. Record annual production of 61.6 mboe was also reported, up 7% on 2015.

A statutory net loss after tax, of \$1,047 million was recorded which included after tax impairments of \$1,050 million on GLNG, announced earlier in the year. The impairment was due to the scaling back of activity in the field in response to lower oil prices, which impacted the ramp-up of production. Combined with an increase in the price of third party gas, this resulted in the need to update long-term operating assumptions for the asset.

Excluding impairments and other significant items, underlying net profit after tax was \$63 million, 29% higher than the prior year.

Excellent progress has been made over the past twelve months in sustainably taking costs out of the business and has contributed to a 51% reduction in capital expenditure to \$625 million and an 18% reduction in upstream unit production costs to \$8.45 per barrel of oil equivalent.

In 2015 the Board announced a new dividend framework to reflect Santos' exposure to oil-linked LNG pricing and the cyclical characteristics of global oil markets. This framework states that dividends are expected to be a minimum of 40 percent of underlying net profit, subject to business conditions.

Consistent with the company's immediate focus to strengthen the balance sheet and reduce net debt, the Board resolved not to pay a final dividend. Whilst we understand that some shareholders will be disappointed, it is our firm view that a disciplined focus on debt reduction is the most responsible course of action in the circumstances. With the strong progress being made in reducing costs and improving free cash flow, the Board is confident in the company's ability to return to paying dividends and will next review this position at the 2017 half-year results.

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### SAFETY

The company recorded its lowest three-year rolling average lost time injury frequency rate on record. It is a credit to all Santos employees that they have stayed focused during the restructuring of the organisation and indeed have embraced a low-cost, high performance mindset to re-establish Santos as a strong and sustainable business with a proud history.

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### STRONGER BALANCE SHEET

Strengthening the balance sheet was a significant focus for the organisation in 2016. Net debt was reduced by \$1.3 billion to \$3.5 billion via a combination of assets sales, free cash flow and the successful completion of the A\$1,040 million institutional placement in December. The decision to raise capital was not taken lightly. It was deemed necessary to enable the company to operate in a lower oil price environment and to provide the financial flexibility to build and grow the business in 2017 and beyond.



We will continue to adopt a disciplined approach to capital management and will target a further \$1.5 billion reduction in net debt by the end of 2019 through free cash flow, asset sales and monetisation of infrastructure assets.

\$447 million in proceeds from asset sales were received in 2016, including the sale of the Kipper asset offshore Victoria, Stag asset offshore Western Australia and pastoral holdings in the Cooper Basin.

The sale of the company's Gippsland and Otway Basin assets offshore Victoria were announced in October and completed in early January 2017, with proceeds of A\$61 million received. A A\$118 million abandonment liability was removed from the balance sheet upon completion.

In December 2016, we also entered into an agreement to sell our remaining 50% interest in the Mereenie oil and gas asset in the Northern Territory for A\$52 million. Completion is expected in the first quarter of 2017.

## NEW GROWTH STRATEGY

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In December 2016 Santos announced a new three phase growth strategy to drive shareholder value – **Transform, Build, Grow**.

Under the **Transform** phase we have simplified the business to focus on five core long-life natural gas assets:

- Cooper Basin,
- GLNG,
- Papua New Guinea,
- Northern Australia, and
- Western Australia Gas.

This focus is not only driving improved performance and further productivity gains but also providing a clear line-of-sight to higher-margin growth opportunities and the delivery of Australia's lowest-cost onshore operations.

Our remaining assets are being run separately as a stand-alone business. Bruce Clement, ex-CEO of AWE, has been appointed Vice President Asia, NSW and WA Oil Assets to manage these assets with a mid-tier oil and gas company mindset to maximise value.

Under the **Build** phase we are building the portfolio of development and exploration opportunities across the five core long-life natural gas assets to maximise production, drive down costs and increase gas supply.

Future **Growth** will come from focussing on opportunities to increase production from our core assets and an exploration strategy to identify new high-value gas targets.

In 2017 we will continue to refine our operating model and look to further improve the asset mix and value drivers as well as build our capabilities and focus on a disciplined cost structure to drive more value out of our assets.

## BOARD RENEWAL

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In the first-half of the year we continued the process of Board renewal by acknowledging the services of Ken Dean and Jane Hemstritch who both retired from the Board and welcomed Peter Hearl and Guy Cowan as Directors. Peter has over 30 years' international business experience, including 18 years in the oil and gas industry with Exxon Mobil. He

is a director of Telstra Corporation and Treasury Wine Estates. Guy also has over 30 years' experience, including 25 years in the oil and gas industry with Shell and is Chairman of Queensland Sugar Limited.

These new appointments underscore the Board renewal process with more than half the Directors appointed within the last 3 years.

Thank you for your continued support for Santos. We enter 2017 with a clear strategy, a new leadership team and a solid platform off which we can build and grow. We are confident that we have the strategy, assets, people and growth options to drive future success and deliver shareholder value.

Sincerely,

**Peter Coates AO**

Chairman

**Kevin Gallagher**

Managing Director and CEO

# Board of Directors



## COMMITTEES OF THE BOARD

### Audit and Risk Committee

Mr G Cowan (Chair)  
Mr H Goh  
Mr P Hearl  
Mr G Martin

### Nomination Committee

Mr P Coates (Chair)  
Mr R Franklin  
Mr G Martin

### People and Remuneration Committee

Mr G Martin (Chair)  
Ms Y Allen  
Mr R Franklin

### Environment, Health, Safety and Sustainability Committee

Mr R Franklin (Chair)  
Ms Y Allen  
Mr K Gallagher  
Mr H Goh

## PETER COATES AO

### CHAIRMAN

BSc (Mining Engineering), FAICD, FAusIMM

Independent non-executive Director. Member of the Board since March 2008, Chairman from December 2009 to May 2013, reappointed Chairman April 2015 and appointed Executive Chairman from August 2015 to January 2016. Chairman of Santos Finance Ltd and Chair of the Nomination Committee.

Non-executive Director of Glencore plc since its float in April 2011 until its merger with Xstrata plc in May 2013. Joined the Board of the merged company in June 2013 and worked as an Executive Director assisting with the integration of Glencore and Xstrata before resuming the position as a non-executive Director from 1 January 2014.

Non-executive Director of Event Hospitality & Entertainment Limited (formerly Amalgamated Holdings Limited) since July 2009.

Former non-executive Chairman of Xstrata Australia Pty Limited from January 2008 to August 2009, former Chairman and non-executive Director of Minara Resources Limited from May 2008 to April 2011, and former Chairman of Sphere Minerals from May 2013 to June 2016. Previously Chief Executive of Xstrata Coal, Xstrata plc's global coal business. Past Chairman of the Minerals Council of Australia, the NSW Minerals Council and the Australian Coal Association.

Made an Officer of the Order of Australia in June 2009 and was awarded the 2010 Australasian Institute of Mining and Metallurgy Medal.

## 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 Unit consisting of five floating production and storage offloading (FPSO) operations and east-coast domestic gas plants. As CEO of the North West Shelf Venture at Woodside, Kevin was responsible for production on Australia's largest resource project.

Kevin joined Clough Limited as CEO and Managing Director in 2011, and during his four-year tenure he implemented strategies that transformed the business. He established a strong leadership team, improved cost and operational performance and delivered record financial results. He oversaw the development of innovative programs to improve safety and drive productivity and 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

BComm, FAICD

Independent non-executive Director since 22 October 2014. A member of the People and Remuneration Committee and Environment, Health, Safety and Sustainability Committee.

Ms Allen has more than 20 years' experience in finance and investment banking, including senior roles at Deutsche Bank AG, ANZ and HSBC Group Plc, former chairman of Macquarie Global Infrastructure Funds, former Director of EFIC (Export, Finance and Insurance Corporation). She is a Director of Cochlear Limited, chairs its Audit Committee and is a member of the Nomination and Remuneration Committee.

She is a member of the George Institute for Global Health Board and a Director of the National Portrait Gallery. Ms Allen is a non-executive Director of ASX Limited, a Director of the ASX Clearing and Settlement boards and a member of its Audit Committee.

Ms Allen was a former non-executive Director of Insurance Australia Group Limited and a former national Director and acting Chair of the Australian Institute of Company Directors.

## GUY COWAN

BSc (Hons) Engineering

Independent non-executive Director since 10 May 2016. Chair of the Audit and Risk Committee and a Director of Santos Finance Limited.

Currently Chairman of Queensland Sugar Limited. Formerly a Director of UGL Limited, where he chaired the Health and Safety Committee, and Coffey International and Ludowici Limited, where he chaired the Audit and Risk Committees for both companies. Shell appointed alternative director of Woodside between 1992 and 1995.

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.





### ROY FRANKLIN OBE

BSc (Hons)

Independent non-executive Director since 28 September 2006. Chair of the Environment, Health, Safety and Sustainability Committee, member of the People and Remuneration Committee and Nomination Committee.

Chairman of Cuadrilla Resources Holdings Limited since April 2015. Appointed deputy Chairman of Statoil with effect from 1 July 2015, and as a Director of Amec Foster Wheeler plc with effect from 1 January 2016.

Non-executive Director of Keller Group plc from 2007 to 2016 and Chairman from 2009 to 2016. Chief Executive Officer of Paladin Resources plc from 1997 to 2005 and former Group Managing Director of Clyde Petroleum plc. Chairman of BRINDEX, the trade association for UK independent oil and gas companies, from 2002 to 2005 and a former member of PILOT, the joint industry/UK Government task force set up to maximise hydrocarbon recovery from the UK North Sea from 2002 to 2005.

In 2004, awarded the OBE for services to the UK oil and gas industry.



### HOCK GOH

BEng (Hons) Mech Eng

Independent non-executive Director since 22 October 2012. Member of the Environment, Health, Safety and Sustainability Committee and the Audit and Risk Committee.

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. Previously held managerial and staff positions in Asia, the Middle East and Europe.

Chairman of MEC Resources Ltd since October 2006. Appointed as non-executive Director of Stora Enso Oyj (Finland) in April 2012. Also a non-executive Director of AB SKF (Sweden) since March 2014 and Vesuvius PLC (UK) since April 2015.

Previously a non-executive Director of BPH Energy Ltd from 2007 to March 2015, an Operating Partner of Baird Capital Partners Asia, based in China, from 2007 to June 2012, and non-executive Director of Xaloy Holding Inc in the US from 2006 to 2008.



### PETER HEARL

BComm (With Merit), FAICD

Independent non-executive Director since 10 May 2016. Member of the Audit and Risk Committee.

During an 18-year career in the oil industry with Esso Australia Ltd and Exxon USA, subsidiaries of oil giant Exxon, he held a variety of senior marketing, operations, logistics and strategic planning positions. Mr Hearl joined PepsiCo as KFC Australia's Director of Operations in 1991 and subsequently held several Regional Vice President (Managing Director) roles before assuming the role of YUM Brands' global Chief Operating & Development Officer in 2006, based in Dallas, Texas and Louisville, Kentucky.

Non-executive Director of Australia's largest telecommunications company, Telstra Ltd since August 2014, and chairs that company's Remuneration Committee. Also a non-executive Director of the Australian listed, global wine company, Treasury Wine Estates since 2012, where he serves on the Audit and Risk Committee.

Former non-executive Director on the board of Goodman Fielder Ltd from 2010 until that company was sold to overseas interests in 2015.



### GREGORY MARTIN

BEc, LLB, FAIM, MAICD

Independent non-executive Director since 29 October 2009. Chair of the People and Remuneration Committee, member of the Audit and Risk and Committee and member of the Nomination Committee.

Director of Spark Infrastructure from 1 January 2017. Appointed Deputy Chairman of the Board of Electricity Networks Corporation, trading as Western Power in 2015. Mr Martin was also appointed to the COAG Energy Council Energy Appointments Selection Panel in 2015. The role of the Panel is to provide recommendations to COAG's Energy Council on appointments to the Australian Energy Market Operator, Australian Energy Market Commission, Australian Energy Regulator and Energy Consumers Australia.

Chairman of Iluka Resources Limited from 2013. Chairman and Joint Managing Partner of Prostar Capital from July 2012 and independent non-executive Chairman of Sydney Desalination Plant Pty Ltd from December 2012.

Formerly non-executive Director of Australian Energy Market Operator Limited (July 2008 to November 2014) and Energy Developments Limited (May 2006 to October 2015), Deputy Chairman of the Australian Gas Association and inaugural Chairman of the Energy Supply Association of Australia. Past member of the Business Council of Australia, Committee for the Economic Development of Australia, and the Council on Australia Latin America Relations. Formerly Managing Director and Chief Executive Officer of AGL, Chief Executive, Infrastructure at Challenger Financial Services Group and Managing Director of Murchison Metals Limited.



### SCOTT SHEFFIELD

BS Petroleum Engineering

Independent non-executive Director since 24 February 2014. Executive Chairman of Pioneer Natural Resources Company, which is listed on the New York Stock Exchange and included in the S&P 500 Index, since 1999.

Serves on various industry and education-related boards, including the National Petroleum Council and the Maguire Energy Institute of the SMU Cox School of Business.

Recipient of the Permian Basin Association's Top Hand award, which recognises individuals who have demonstrated exceptional leadership within the oil and gas industry and the Permian Basin community. He is also a 2013 inductee into the Permian Basin Petroleum Museum Hall of Fame.

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# Santos Executive Committee



**KEVIN GALLAGHER**

**MANAGING DIRECTOR  
& CHIEF EXECUTIVE  
OFFICER**

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



**ANTHONY NEILSON**

**CHIEF FINANCIAL  
OFFICER**

BComm; MBA; FFin; ACA

Anthony Neilson 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 Master 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.



**JOHN ANDERSON**

**EXECUTIVE VICE  
PRESIDENT COMMERCIAL  
& BUSINESS  
DEVELOPMENT**

LLB, BEc, GDCL

John Anderson is accountable for commercial and business development.

John joined Santos in 1996 as a Corporate Counsel in Brisbane having previously worked for 10 years as a solicitor with a large corporate law firm in Brisbane, and Melbourne.

John has held a number of senior roles in Santos including Vice President Commercial, Vice President Strategic Projects and Group Executive Business Development, and was responsible for taking Santos' interests in the Hides gas field to FEED in the PNG LNG Project. In 2009, John relocated to Perth to run Santos' WA & NT operations including domestic gas and oil production in the Carnarvon Basin, exploration activity in the Browse and Bonaparte basins and the company's first LNG project, Darwin LNG.

In 2014, John moved to Singapore after his responsibilities were extended to include Santos' Asian activities including the company's second LNG project, PNG LNG, as well as oil and gas production assets in Indonesia and Vietnam. John returned to Australia in the second half of 2016 to his current position of Executive Vice President, Commercial and Business Development.



**VINCE SANTOSTEFANO**

**CHIEF OPERATIONS  
OFFICER**

BEEng (Civil), SPE

Vince joined Santos in March of 2016 as COO, accountable for the profit and loss of all our operated producing 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 six 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**

### **VICE PRESIDENT DEVELOPMENT**

BSc (Hons) Geology and Geophysics

Brett is responsible for delivering projects, sustaining capital work programs across the Cooper Basin, Narrabri and Queensland CSG, Drilling and Completions and non-operated assets including Darwin LNG, PNG LNG, Asia and Western Australia Domestic Gas.

Brett previously held the role as Vice President, Eastern Australia from August 2015 which included production, development and commercialisation of the company's oil and gas resources in Central Australia.

Brett joined Santos in February 2013 as the Manager Exploration for the company's Perth-based WA and NT business unit. Brett is a geologist and geophysicist, and has over 20 years of oil and gas industry experience including executive management, technical and business development roles. He is a member of the APPEA Board.



## **ANGUS JAFFRAY**

### **EXECUTIVE VICE PRESIDENT STRATEGY & CORPORATE SERVICES**

BA (Hons) Geography, MBA

Angus has over 20 years of leadership and consulting experience. Prior to joining Santos he was a Director of Azure Consulting, a Partner at The Boston Consulting Group 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, mainly in Western Australia. 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 EHS & GOVERNANCE**

LLB (Hons), MLM

Naomi joined Santos in 2016 and is responsible for Santos' legal, risk and audit, company secretary, environment and safety functions.

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.



## **BILL OVENDEN**

### **VICE PRESIDENT EXPLORATION**

BSc (Hons) Geology and Geophysics

Bill Ovenden is accountable for developing and executing a targeted exploration strategy.

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 companies including Sun Oil, Kufpec, ExxonMobil and Ampolex. He joined Santos in 2002 after working for ExxonMobil in Indonesia.

# Reserves statement

## for the year ended 31 December 2016

Santos proved (1P) petroleum reserves were 485 million barrels of oil equivalent (mmboe) at the end of 2016. 1P reserves increased by 61 mmboe before production and the organic 1P reserves replacement ratio was 106%.

Proved plus probable (2P) petroleum reserves were 889 mmboe. 2P reserves increased by 6 mmboe before production and the organic 2P reserves replacement ratio was 19%.

The key movements in 2P reserves before production in 2016 were:

- 15 mmboe increase due to a reserves upgrade at Reindeer (WA Gas).
- 14 mmboe increase due to positive field performance at PNG LNG.
- 18 mmboe reduction at GLNG primarily due to revisions in field development plans.
- 5 mmboe net reduction in other assets.

After deducting 2016 production of 62 mmboe, 1P reserves were in line with the prior year and 2P reserves reduced by 6%.

### RESERVES (SANTOS SHARE)

| Santos share                  | Unit  | 2016       | 2015 | %change |
|-------------------------------|-------|------------|------|---------|
| Proved reserves               | mmboe | <b>485</b> | 485  | (0)     |
| Proved plus probable reserves | mmboe | <b>889</b> | 945  | (6)     |

### COOPER BASIN

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

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

| Santos share | Unit       | 2016       | 2015       | %change    |
|--------------|------------|------------|------------|------------|
| Sales gas    | PJ         | 672        | 726        | (7)        |
| Crude oil    | mmbbl      | 18         | 20         | (11)       |
| Condensate   | mmbbl      | 10         | 11         | (14)       |
| LPG          | 000 tonnes | 1,288      | 1,457      | (12)       |
| <b>Total</b> | mmboe      | <b>154</b> | <b>168</b> | <b>(9)</b> |

Sales gas proved plus probable reserves were maintained before 2016 production.

Work continues to mature the Permian Source Rock (Deep Coal) play to assess the potential for the recovery of incremental volumes of gas, while exploration and development of shale and tight gas within the Nappamerri Trough has been suspended.

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## GLNG

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

### GLNG JV reserves (GLNG 100% share)

| GLNG 100% share               | Unit | 2016  | 2015  | %change |
|-------------------------------|------|-------|-------|---------|
| Proved reserves               | PJ   | 2,486 | 2,540 | (2)     |
| Proved plus probable reserves | PJ   | 5,256 | 5,546 | (5)     |

GLNG JV share proved plus probable reserves decreased by 3% before 2016 production, primarily due to revisions to field development plans and some reclassification in deeper low permeability coals. There was no change to reserves in the Raslie area of the Roma field, where remediation plans are progressing. In addition to the reserves in the table above, GLNG JV has Santos portfolio and third party gas supply agreements for an aggregate of between approximately 2,100 PJ and 2,800 PJ over periods of up to 20 years.

GLNG JV share contingent resources increased in 2016. Santos is committed to ongoing appraisal and operational efficiencies to potentially mature resources to reserves and develop for additional gas supply to the project.

### GLNG proved plus probable reserves by product (Santos share)

| Santos share | Unit  | 2016 | 2015 | %change |
|--------------|-------|------|------|---------|
| Sales gas    | mmboe | 341  | 367  | (7)     |

Santos share GLNG asset proved plus probable reserves decreased by 5% before 2016 production. Santos share GLNG asset reserves in the table above include Santos' share of the Combabula, Ramyard, Spring Gully and Denison fields.

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## PAPUA NEW GUINEA

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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.

### PNG proved plus probable reserves by product (Santos share)

| Santos share | Unit         | 2016       | 2015       | %change  |
|--------------|--------------|------------|------------|----------|
| Sales gas    | PJ           | 1,215      | 1,173      | 4        |
| Condensate   | mmbbl        | 14         | 20         | (29)     |
| <b>Total</b> | <b>mmboe</b> | <b>222</b> | <b>220</b> | <b>1</b> |

Sales gas proved plus probable reserves increased by 9% before 2016 production. Positive Hides field performance and revised fuel, flare and vent assumptions led to the increase. Condensate reserves were lower due to revisions to the forecast condensate to gas ratio in the Hides field.

PNG LNG underpins the majority of Santos' reserves and resources in PNG. 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. The project has recently undergone an independent contingent resource recertification which resulted in an increase in 1C project resources, supporting extended production at current plateau rates.

Santos holds an extensive exploration and production position throughout PNG and is a foundation partner in the nationally significant PNG LNG project. Santos has interests in several large scale discoveries across the PNG Fold Belt, Gulf of Papua, and PNG Forelands, which could provide future backfill, expansion or standalone development opportunities.

- **PPL-402** (Santos 20%, subject to future government back-in) contains the recently drilled and potentially multi-tcf Muruk discovery. Following the discovery at the Muruk-1 exploration well in December 2016, sidetrack drilling has commenced to further appraise the size and quality of the Muruk discovery. The Muruk gas field is located within 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.
- **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.

# Reserves statement

## continued

- **PRL-9** (Santos 40%, subject to future government back-in) contains the Barikewa gas discovery. The Joint Venture intends to drill an appraisal well prior to permit expiry in 2020 to appraise the discovered resources. The Barikewa gas field is located within 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.

### NORTHERN AUSTRALIA

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

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

| Santos share | Unit       | 2016      | 2015      | %change     |
|--------------|------------|-----------|-----------|-------------|
| Sales gas    | PJ         | 72        | 93        | (23)        |
| Condensate   | mmbbl      | 2         | 3         | (22)        |
| LPG          | 000 tonnes | 141       | 178       | (21)        |
| <b>Total</b> | mmboe      | <b>15</b> | <b>20</b> | <b>(23)</b> |

Sales gas proved plus probable reserves were maintained before 2016 production.

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

- **Bayu Undan** (Santos 11.5%) is the current gas supply source to DLNG. Reserves and field are expected to be 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. Appraisal drilling commenced in early 2017 and pre-FEED activities and regulatory approvals are being progressed.
- **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  | 2016       | 2015       | %change  |
|--------------|-------|------------|------------|----------|
| Sales gas    | PJ    | 641        | 606        | 6        |
| Condensate   | mmbbl | 7          | 7          | (3)      |
| <b>Total</b> | mmboe | <b>117</b> | <b>111</b> | <b>5</b> |

Sales gas proved plus probable reserves increased by 14% before 2016 production, primarily due to a reserves upgrade at the Reindeer asset.

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

- **John Brookes, Spar, Halyard and Reindeer** (Santos 45%). Reserves growth from the producing fields has extended production plateau and new projects such as Spar-2 tieback and Varanus Island Inlet Compression will unlock undeveloped reserves. Modern seismic datasets in the vicinity of existing infrastructure are being analysed to deliver low cost supply tiebacks into existing infrastructure.
- **Zola-Bianchi** (Santos 25%). Seismic acquisition is planned for 2017, targeting new prospects to build volume in the vicinity of the discovered resource base.
- **Maitland-Davis** (Santos 45%). Resources increased in 2016 with successful well Davis-1, with further work being done to refine the appraisal and development plan.
- **Spartan** (Santos 45%). Discovered in 2016, development planning is underway with seismic acquisition planned for 2017 targeting similar near-field opportunities to aggregate volume.

## PROVED RESERVES

### Year-end 2016 (Santos share)

| Asset   | Sales gas<br>PJ | Crude oil<br>mmbbl | Condensate<br>mmbbl | LPG<br>000 tonnes | All products<br>mmboe |             | Total      |
|---|-----------------|--------------------|---------------------|-------------------|-----------------------|-------------|------------|
|   |                 |                    |                     |                   | Developed             | Undeveloped |            |
| Cooper Basin  | 309             | 10                 | 4                   | 579               | 48                    | 23          | 71         |
| GLNG <sup>1</sup>   | 888             | -                  | -                   | -                 | 72                    | 81          | 153        |
| PNG   | 855             | 0                  | 10                  | -                 | 107                   | 49          | 156        |
| Northern Australia  | 51              | -                  | 1                   | 59                | 10                    | -           | 10         |
| WA Gas  | 399             | -                  | 4                   | -                 | 54                    | 18          | 73         |
| Other Assets <sup>2</sup>                                   | 88              | 7                  | 0                   | -                 | 16                    | 7           | 22         |
| <b>Total 1P</b>   | <b>2,590</b>    | <b>17</b>          | <b>19</b>           | <b>638</b>        | <b>307</b>            | <b>179</b>  | <b>485</b> |
| Proportion of total proved reserves that are unconventional |                 |                    |                     |                   |                       |             | 32%        |

1 GLNG Asset proved sales gas reserves include 746 PJ Santos share GLNG Joint Venture and 142 PJ other Santos Queensland assets.

2 Other Assets include Indonesia, Vietnam, Western Australia oil, Victoria and onshore Northern Territory.

### Proved reserves reconciliation

| Product         | Unit         | Reserves         | Production  | Revisions and | Discoveries | Net                                | Reserves         |
|-----------------|--------------|------------------|-------------|---------------|-------------|------------------------------------|------------------|
|                 |              | Year-end<br>2015 |             | extensions    |             | acquisitions<br>and<br>divestments | Year-end<br>2016 |
| Sales gas       | PJ           | <b>2,534</b>     | (286)       | 366           | -           | (23)                               | <b>2,590</b>     |
| Crude oil       | mmbbl        | <b>21</b>        | (8)         | 4             | -           | -                                  | <b>17</b>        |
| Condensate      | mmbbl        | <b>23</b>        | (4)         | (1)           | -           | (0)                                | <b>19</b>        |
| LPG             | 000 tonnes   | <b>873</b>       | (147)       | (87)          | -           | -                                  | <b>638</b>       |
| <b>Total 1P</b> | <b>mmboe</b> | <b>485</b>       | <b>(62)</b> | <b>65</b>     | -           | <b>(4)</b>                         | <b>485</b>       |

# Reserves statement

## continued

### PROVED PLUS PROBABLE RESERVES

#### Year-end 2016 (Santos share)

| Asset   | Sales gas PJ | Crude oil<br>mmbbl | Condensate<br>mmbbl | LPG 000<br>tonnes | All products<br>mmbae |             | Total      |
|---|--------------|--------------------|---------------------|-------------------|-----------------------|-------------|------------|
|   |              |                    |                     |                   | Developed             | Undeveloped |            |
| Cooper Basin  | 672          | 18                 | 10                  | 1,288             | 101                   | 53          | 154        |
| GLNG <sup>1</sup>   | 1,980        | -                  | -                   | -                 | 82                    | 259         | 341        |
| PNG   | 1,215        | 0                  | 14                  | -                 | 147                   | 75          | 222        |
| Northern Australia  | 72           | -                  | 2                   | 141               | 15                    | -           | 15         |
| WA Gas  | 641          | -                  | 7                   | -                 | 76                    | 41          | 117        |
| Other Assets <sup>2</sup>   | 150          | 15                 | 0                   | -                 | 32                    | 9           | 41         |
| <b>Total 2P</b>   | <b>4,730</b> | <b>33</b>          | <b>33</b>           | <b>1,429</b>      | <b>453</b>            | <b>436</b>  | <b>889</b> |
| Proportion of total proved plus probable reserves that are unconventional |              |                    |                     |                   |                       |             | 38%        |

1 GLNG Asset proved plus probable sales gas reserves include 1,577 PJ Santos share GLNG Joint Venture and 403 PJ other Santos Queensland assets.

2 Other Assets include Indonesia, Vietnam, Western Australia oil, Victoria and onshore Northern Territory.

#### Proved plus probable reserves reconciliation

| Product    | Unit       | Reserves         | Production | Revisions         | Discoveries | Net                                | Reserves         |
|------------|------------|------------------|------------|-------------------|-------------|------------------------------------|------------------|
|            |            | Year-end<br>2015 |            | and<br>extensions |             | acquisitions<br>and<br>divestments | Year-end<br>2016 |
| Sales gas  | PJ         | 4,931            | (286)      | 120               | -           | (34)                               | 4,730            |
| Crude oil  | mmbbl      | 42               | (8)        | (1)               | -           | -                                  | 33               |
| Condensate | mmbbl      | 42               | (4)        | (5)               | -           | (0)                                | 33               |
| LPG        | 000 tonnes | 1,933            | (147)      | (357)             | -           | -                                  | 1,429            |
| Total 2P   | mmbae      | 945              | (62)       | 12                | -           | (6)                                | 889              |



## 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 2016.
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 2016 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 2016.
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                      |
| 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

### 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 2016, 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                          |
| Coates    | Peter Roland (Chairman) | 131,870                         |
| Cowan     | Guy Michael             | 15,000                          |
| Franklin  | Roy Alexander           | 28,996                          |
| Gallagher | Kevin Thomas            | 103,808                         |
| Goh       | Hock                    | 37,215                          |
| Hearl     | Peter Roland            | 48,808                          |
| Martin    | Gregory John Walton     | 42,720                          |
| Sheffield | Scott Douglas           | 63,529                          |

The above named Directors held office during and since the end of the financial year. Mr Kenneth Dean and Ms Jane Hemstritch were Directors until their retirement at the Annual General Meeting on 4 May 2016. Mr Kevin Gallagher was appointed Managing Director effective 16 February 2016. Mr Guy Cowan and Mr Peter Hearl were appointed Directors on 10 May 2016. 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 1,235,142 share acquisition rights (SARs). No other Director holds options or SARs.

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

## 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 <sup>1</sup> | Attended/Held <sup>1</sup> | Attended/Held <sup>1</sup>                             | Attended/Held <sup>1</sup>      | Attended/Held <sup>1</sup> |
| Allen <sup>2</sup>      | Yasmin A.     | 11 of 13                   | 1 of 2                     | 4 of 4   | 2 of 2                          | n/a                        |
| Coates <sup>3</sup>     | Peter R.      | 13 of 13                   | n/a                        | n/a  | n/a                             | 4 of 4                     |
| Cowan <sup>4</sup>      | Guy M.        | 7 of 7                     | 3 of 3                     | n/a  | n/a                             | n/a                        |
| Dean <sup>5</sup>       | Kenneth A.    | 6 of 6                     | 1 of 1                     | n/a  | n/a                             | 2 of 2                     |
| Franklin                | Roy A.        | 12 of 13                   | n/a                        | 4 of 4   | 3 of 5                          | 4 of 4                     |
| Gallagher <sup>6</sup>  | Kevin T.      | 11 of 11                   | n/a                        | 4 of 4   | n/a                             | n/a                        |
| Goh                     | Hock          | 13 of 13                   | 4 of 4                     | 4 of 4   | n/a                             | n/a                        |
| Hearl <sup>7</sup>      | Peter R.      | 7 of 7                     | 2 of 3                     | n/a  | n/a                             | n/a                        |
| Hemstritch <sup>8</sup> | Jane S.       | 5 of 6                     | 1 of 1                     | n/a  | 1 of 2                          | n/a                        |
| Martin <sup>9</sup>     | Gregory J. W. | 13 of 13                   | 4 of 4                     | n/a  | 5 of 5                          | 2 of 2                     |
| Sheffield               | Scott D.      | 11 of 13                   | n/a                        | n/a  | n/a                             | 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 retired as a member of the Audit & Risk Committee and became a member of the People & Remuneration Committee on 24 June 2016

3 Mr PR Coates retired as a member of the Environment Health, Safety & Sustainability Committee on 16 February 2016

4 Mr GM Cowan was appointed as a Director and became Chair of the Audit & Risk Committee on 10 May 2016

5 Mr KA Dean retired as a Director on 4 May 2016

6 Mr KT Gallagher was appointed Managing Director and became a member of the Environment, Health, Safety & Sustainability Committee on 16 February 2016

7 Mr PR Hearl was appointed as a Director and member of the Audit & Risk Committee on 10 May 2016

8 Ms JS Hemstritch retired as a Director on 4 May 2016

9 Mr GJW Martin became a member of the Nomination Committee on 3 May 2016

# Directors' Report

## continued

### OPERATING AND FINANCIAL REVIEW

Santos' principal activities during 2016 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.

The consolidated entity has changed its reporting currency from Australian dollars to United States (US) dollars, effective 1 January 2016. Consequently, unless otherwise stated, all references to dollars are to US dollars.

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

|  | <b>2016</b>        | 2015        | Variance |
|--|--------------------|-------------|----------|
|  | <b>mmboe</b>       | mmboe       | %        |
| Production volume  | <b>61.6</b>        | 57.7        | 7        |
| Sales volume   | <b>84.1</b>        | 64.3        | 31       |
|  | <b>US\$million</b> | US\$million |          |
| Product sales  | <b>2,594</b>       | 2,442       | 6        |
| EBITDAX <sup>1</sup>   | <b>1,199</b>       | 1,454       | (18)     |
| Exploration and evaluation expensed                                  | <b>(138)</b>       | (188)       | 27       |
| Depreciation and depletion   | <b>(741)</b>       | (793)       | 7        |
| Net impairment loss  | <b>(1,561)</b>     | (2,854)     | 45       |
| Change in future restoration assumptions                             | <b>37</b>          | -           | -        |
| EBIT <sup>1</sup>  | <b>(1,204)</b>     | (2,381)     | 49       |
| Net finance costs  | <b>(281)</b>       | (217)       | (29)     |
| Taxation benefit   | <b>438</b>         | 645         | (32)     |
| Net loss for the period and attributable to equity holders of Santos | <b>(1,047)</b>     | (1,953)     | 46       |
| Underlying profit for the period <sup>1</sup>                        | <b>63</b>          | 49          | 29       |
| Underlying earnings per share (cents)                                | <b>3.5</b>         | 4.3         | (18.6)   |

<sup>1</sup> EBITDAX (earnings before interest, tax, depreciation, depletion, amortisation, 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 21 for the reconciliation of 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 period. The non-IFRS financial information is unaudited however the numbers have been extracted from the audited financial statements.

#### Production and sales

Santos achieved record production and sales volumes in 2016. Higher volumes were driven by the ramp-up of production at GLNG, record production from PNG LNG and strong performance from Darwin LNG, the Cooper Basin and WA Gas.

Production of 61.6 million barrels of oil equivalent (mmboe) was the Company's highest annual production and a 7% increase on the prior year, primarily due to a full year of production from GLNG Train 1 and the start-up of Train 2, and record production from PNG LNG.

Sales volumes were up 31% to a record 84.1 mmboe. LNG sales volumes were up 89% to 2.8 million tonnes, due to the ramp-up at GLNG and strong performance from PNG LNG and Darwin LNG. Sales of third party volumes increased to 20.1 mmboe due to higher domestic gas and LNG volumes, partially offset by lower crude oil volumes.

Sales revenue of \$2.6 billion was 6% higher than 2015, reflecting the growth in sales volumes but offset by lower realised oil and LNG prices. The average realised crude oil price for the year was \$46.43 per barrel, 14% lower than 2015, while the average realised LNG price was down 33% to \$6.03 per mmbtu.

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## **Review of operations**

In 2016, Santos undertook swift and decisive action to stabilise the business, reduce costs and increase operating cash flow. These measures delivered tangible results, with the business achieving record production and sales volumes, unit production costs of \$8.45/boe were down 18% compared to last year, capital expenditure (excluding capitalised interest) of \$625 million was down 51% and the Company generated \$206 million in free cash flow before asset acquisitions and divestments in 2016.

Santos also restructured its business to focus on five core, long-life natural gas assets: Cooper Basin, GLNG, PNG, Northern Australia and WA 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 the domestic and export markets.

Santos' share of Cooper Basin gas production of 61.2 petajoules (PJ) was slightly lower than 2015, reflecting lower raw gas capacity due to natural field decline, offset by higher uptime and production optimisation activities. Santos' share of Cooper Basin condensate production was in line with the prior year at 938,500 barrels.

Santos' share of Cooper Basin oil production of 2.7 million barrels (mmbbl) was 5% lower than 2015 due to reduced development activity and natural field decline. Volumes of third party crude oil processed at Moomba decreased as activity in the Basin was curtailed in response to lower oil prices.

Cooper Basin EBITDAX was \$265 million, 10% lower than 2015 primarily due to lower commodity prices.

Significant reductions were achieved in operating and development costs in 2016. Unit production costs were down 15% to \$10.71/boe and average gas well costs were down 12% to \$4.2 million per well. As operator, Santos aims to continue to reduce costs and drive efficiencies to deliver a low-cost, cash flow positive business in the Cooper Basin.

### **GLNG**

GLNG produces liquefied natural gas (LNG) for export to global markets from the LNG plant at Gladstone. Gas is also sold into domestic markets. 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. The plant produced 4.6 million tonnes of LNG in 2016 and shipped 75 cargoes.

Santos' share of sales gas to the LNG plant increased to 30.2 PJ in 2016, reflecting the ramp-up of Train 1 and start-up of Train 2 during the year. In addition, Santos' share of domestic gas production was 5 PJ.

GLNG EBITDAX was \$183 million, 490% higher than 2015 primarily due to the ramp-up of GLNG operations with first cargo in October 2015.

Santos' strategy is to transform GLNG to deliver steady-state operations and a cash flow positive business. GLNG LNG sales are expected to ramp-up from 2016 levels to approximately six million tonnes per annum over the next three years.

### **PNG**

Santos' business in 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.

The LNG plant near Port Moresby has two LNG trains with a combined nameplate capacity of 6.9 mtpa. Production from both trains commenced in 2014 and they operated at record rates in 2016, producing over 7.9 million tonnes of LNG and shipping 106 cargoes.

Santos' share of sales gas to the LNG plant increased to 62.5 PJ in 2016, reflecting the strong operating performance. Santos' share of condensate production was 1.5 mmbbl. Unit upstream production costs were down 17% to \$4.59/boe.

PNG LNG EBITDAX was \$350 million, 21% lower than 2015 primarily due to lower commodity prices.

Santos' strategy in PNG is to work with its partners to align interests to support LNG expansion opportunities. In December 2016, Santos and its partners announced a gas discovery with the Muruk-1 exploration well, which is located near to existing PNG LNG production facilities.

# Directors' Report

## 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.

In operation since 2006, Darwin LNG continued to perform strongly in 2016, producing 3.6 million tonnes of LNG and shipping 57 cargoes. Santos' net entitlement to gas production of 19.3 PJ was in line with the prior year. Santos' net entitlement to condensate from Bayu-Undan was 0.59 mmbbl. Unit upstream production costs were reduced by 7% to \$17.57/boe.

Northern Australia EBITDAX was \$86 million, 40% lower than 2015 primarily due to lower commodity prices.

Santos has extensive discovered resources across Northern Australia which are well positioned to backfill and expand existing LNG infrastructure. These resource opportunities include the Barossa-Caldita (Santos 25%), Petrel-Tern (Santos 35-40%) and Crown-Lasseter (Santos 30%) fields. Engineering studies are underway to assess Barossa-Caldita as a candidate for Darwin LNG backfill. Two Barossa appraisal wells are planned to be drilled in 2017.

### **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.

Santos' Western Australia gas and condensate production of 49.3 PJ and 478,100 barrels respectively, were both slightly lower than 2015 primarily due to lower customer nominations.

WA Gas EBITDAX was \$210 million, 30% higher than 2015.

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

### **Other assets**

Santos' other assets have been packaged and run separately for value as a standalone business. These assets include Santos interests in Indonesia, Vietnam, East Coast Australia Gas and WA Oil. The portfolio will be continually optimised to drive efficiency and shareholder value.

Santos' share of gas production from the Otway Basin offshore Victoria was 10.4 PJ, 20% lower than 2015 due to natural field decline. Santos announced the sale of its Victorian assets in October 2016 for up to A\$82 million, and the sale (excluding Minerva) was completed in early January 2017. Completion of the sale of Minerva is expected in the first quarter of 2017.

In December 2016, Santos entered an agreement to sell its remaining 50% interest in the Mereenie oil and gas assets in the Northern Territory to a subsidiary of Macquarie Group Limited for A\$52 million. Completion is expected in the first quarter of 2017.

Santos' share of Western Australia oil production of 2.3 mmbbl was in line with 2015, as higher production from Mutineer-Exeter/Fletcher Finucane was offset by the sale of the Company's interest in the Stag asset, which was completed in November 2016.

Santos' net entitlement to oil production in Vietnam of 2.6 mmbbl was in line with 2015.

Santos' net entitlement to gas production in Indonesia of 22.3 PJ was 6% lower than 2015, primarily due to natural field decline and lower net contractor entitlement.

## Net loss

The 2016 net loss attributable to equity holders of Santos Limited of \$1,047 million is \$906 million lower than the net loss of \$1,953 million in 2015. This decrease is primarily due to lower impairment losses of \$1,101 million after tax (\$2,014 million in 2015), higher sales revenue and higher cost of sales as a result of the ramp-up of the GLNG project following first cargo on 16 October 2015.

Net loss includes items before tax of \$1,572 million (\$1,110 million after tax), as referred to in the reconciliation of net loss to underlying profit below. Underlying profit was \$63 million, \$14 million higher than 2015.

### Reconciliation of net loss to underlying profit<sup>1</sup>

|  | 2016<br>US\$million |              |                | 2015<br>US\$million |       |                |
|--|---------------------|--------------|----------------|---------------------|-------|----------------|
|  | Gross               | Tax          | Net            | Gross               | Tax   | Net            |
| Net loss after tax attributable to equity holders of Santos Limited          |                     |              | <b>(1,047)</b> |                     |       | <b>(1,953)</b> |
| Add/(deduct) the following:  |                     |              |                |                     |       |                |
| Net gains on sales of non-current assets                                     | <b>(25)</b>         | <b>8</b>     | <b>(17)</b>    | (1)                 | –     | (1)            |
| Impairment losses  | <b>1,561</b>        | <b>(460)</b> | <b>1,101</b>   | 2,854               | (840) | 2,014          |
| Change in future restoration assumptions                                     | <b>(37)</b>         | <b>10</b>    | <b>(27)</b>    |                     |       |                |
| Foreign exchange (gains)/ losses   | <b>(34)</b>         | <b>21</b>    | <b>(13)</b>    | (196)               | 173   | (23)           |
| Fair value adjustments on embedded derivatives and hedges                    | <b>54</b>           | <b>(16)</b>  | <b>38</b>      | (9)                 | 3     | (6)            |
| Remediation (income)/costs for incidents net of related insurance recoveries | <b>(10)</b>         | –            | <b>(10)</b>    | –                   | –     | –              |
| Other expense items <sup>2</sup>   | <b>63</b>           | <b>(18)</b>  | <b>45</b>      | 50                  | (15)  | 35             |
| Other tax adjustments  | –                   | <b>(7)</b>   | <b>(7)</b>     | –                   | (17)  | (17)           |
|  | <b>1,572</b>        | <b>(462)</b> | <b>1,110</b>   | 2,698               | (696) | 2,002          |
| <b>Underlying profit<sup>1</sup></b>   |                     |              | <b>63</b>      |                     |       | <b>49</b>      |

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 2016 relate to restructure costs including redundancy payments and an onerous contract provision for unutilised transport capacity.

## Financial position

### Summary of financial position

|   | 2016<br>US\$million | 2015<br>US\$million | Variance<br>US\$million |
|---|---------------------|---------------------|-------------------------|
| Exploration and evaluation assets                                 | <b>495</b>          | 520                 | (25)                    |
| Oil and gas assets and other land, buildings, plant and equipment | <b>10,533</b>       | 12,585              | (2,052)                 |
| Restoration provision   | <b>(1,468)</b>      | (1,778)             | 310                     |
| Other net assets/(liabilities) <sup>1</sup>                       | <b>167</b>          | 453                 | (286)                   |
| Total funds employed  | <b>9,727</b>        | 11,780              | (2,053)                 |
| Net debt <sup>2</sup>   | <b>(3,492)</b>      | (4,749)             | 1,257                   |
| Net tax assets/(liabilities) <sup>3</sup>                         | <b>845</b>          | 390                 | 455                     |
| Net assets/equity   | <b>7,080</b>        | 7,421               | (341)                   |

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 and commodity derivatives.

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

# Directors' Report

## continued

### **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 2016 full-year accounts.

Some assets were assessed to be impaired and non-cash after-tax impairment losses of \$1,101 million have been recognised in the 2016 accounts.

The impairment losses primarily relate to the 30 June 2016 impairment of GLNG.

### **Exploration and evaluation assets**

Exploration and evaluation assets were \$495 million compared to \$520 million at the end of 2015, a decrease of \$25 million, mainly due to impairment losses before tax of \$59 million, exploration and evaluation expensed of \$71 million and the Sole project in Victoria classified as held for sale, offset by 2016 capital expenditure, including drilling in Papua New Guinea, two near-field exploration wells in Indonesia along with evaluation studies, in addition to acquisition costs comprising interests in PPLs 402, 261 and 287 in Papua New Guinea.

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

Oil and gas assets and other land and buildings, plant and equipment of \$10,533 million were \$2,052 million lower than in 2015 mainly due to impairment losses before tax of \$1,502 million and depreciation and depletion charges, offset by 2016 capital expenditure, including GLNG, PNG LNG and the Cooper Basin. Assets classified as held for sale in 2016 include Mereenie, Casino/Henry, Patricia Baleen and Vic/P44.

### **Restoration provision**

Restoration provision balances have decreased by \$310 million to \$1,468 million mainly due to revised restoration cost estimates, provisions sold as part of asset sales or classified as held for sale and favourable changes in discount rates.

### **Net debt**

Net debt of \$3,492 million was \$1,257 million lower than at the end of 2015 primarily as a result of free cash flow before asset acquisitions and divestments of \$206 million, an institutional share placement of \$751 million and proceeds from asset sales of \$447 million, offset by acquisitions and unfavourable fair value movements in other financial assets and liabilities.

### **Net tax assets/(liabilities)**

Net tax assets of \$845 million have increased by \$455 million primarily as a result of higher carry-forward tax losses recognised by the group and impairments of non-current assets.

### **Net assets/equity**

Total equity decreased by \$341 million to \$7,080 million at year end. The decrease primarily reflects the net loss after tax attributable to owners of Santos of \$1,047 million, partially offset by the increase in issued capital of \$764 million, primarily as a result of the institutional share placement in December 2016.

### **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.



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### **Oil price hedging**

During 2016, the Company implemented an Oil Price Hedging Policy. The objectives of the 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 2016, the Company had hedged 11 million barrels of oil in 2017 using zero-cost three-way collars. Under the collars, where the Brent oil price is above \$62.85, Santos receives \$62.85. Where the Brent oil price is between \$50 and \$62.85, Santos receives the actual Brent price. Where the Brent oil price is between \$40 and \$50, Santos receives \$50, and where the Brent oil price is below \$40, Santos receives the actual Brent price plus \$10.

### **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 new strategy has three phases:

#### **Transform**

- New leadership team and simplified operating model to deliver a low-cost, reliable and high performance business.
- Focus on five core, long-life natural gas assets: Cooper Basin, GLNG, PNG, Northern Australia and WA Gas.

#### **Build**

- Identify and develop growth opportunities, including exploration, across the five core long-life natural gas assets.
- Maximise production, drive down costs and increase gas supply.

#### **Grow**

- Execute and bring on-line growth opportunities across the core portfolio.
- Focused exploration strategy to identify new high-value gas targets.
- Find and unlock sixth core long-life natural gas asset.

Significant progress in the **Transform** phase of the strategy was made in 2016, including:

- Appointment of new Chief Executive Officer and Executive Committee (Excom).
- Restructured the business and new operating model established.
- Removed substantial costs: unit production costs cut by 18%, capital expenditure by 51% and employee headcount by 20%.
- Free cash flow breakeven point reduced to \$36.50 per barrel. The Company generated \$206 million in free cash flow before asset sales in 2016.
- Sold non-core assets.
- Implemented oil price hedging strategy.
- Strengthened the balance sheet via an institutional placement which raised \$751 million.
- Reduced net debt by \$1.3 billion.

Importantly, during a period of significant organisational change, Santos continued to maintain record safety performance.

# Directors' Report

## continued

### **Prospects for future financial years**

Santos enters 2017 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 an extended period of low oil prices, with more than \$2 billion in cash as at 31 December 2016 and no material debt maturities until 2019. Santos will continue to focus on reducing costs and building on the significant improvements made in 2016 to operating efficiency.

Santos expects 2017 sales volumes to be in the range of 73-80 mmbob and production to be in the range of 55-60 mmbob. Capital expenditure is expected to be in the range of \$700-750 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 prolonged weakness in the oil price, and is confident that the measures taken will drive better returns for shareholders.

### **Material business risks**

The achievement of the 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.

#### **Volatility in oil and gas prices**

- Santos' business relies primarily on the production and sale of oil and gas products to a variety of buyers under a range of short-term and long-term contracts. A significant part of Santos' business consists of the production and sale of LNG through its holdings in PNG LNG, GLNG and Darwin LNG. The majority of LNG produced or to be produced from these projects has been sold under long-term LNG sales contracts where the LNG 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. Oil prices in 2016 saw Santos continue to manage risks associated with a lower oil price operating environment. In conjunction with the implementation of a new three-tiered strategy and aligned operating model, further action was taken to progress operational efficiencies, reduce capital expenditure and strengthen the Company's balance sheet. Additionally, in 2016 the Board implemented a dividend framework that reflects Santos' exposure to oil-linked LNG pricing and the cyclical characteristics of global oil markets.

#### **Project development risks**

- 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 and the progress and performance of material projects is regularly reviewed by senior management and the Board.

#### **Oil and gas reserves**

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

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### **Exploration risks**

- 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. Exploration is a high-risk endeavour subject to geological and technological uncertainties and the failure to replace utilised reserves with additional proved reserves is a risk inherent in the oil and gas exploration and production industry.
- Santos employs a well-established exploration prospect evaluation methodology and risking process to manage the risks associated with exploration.

### **Regulatory and licence to operate risks**

- Santos' business is subject to various laws and regulations, in each of the countries in which it operates, relating 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 its business, results of operations and financial condition. For example, a change in taxation laws, environmental laws, land access laws or the application of existing laws could also have a material effect on Santos.
- A range of health, safety and environmental risks exists with 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 the Company's licence to operate and access to land, leading to delays, disruption or the shut-down of exploration and production activities.
- Santos has interests in areas which may be subject to claims by landowners, who may have concerns over the distribution of oil and gas royalties and access to mining and petroleum-related benefits. This has the potential to result in community unrest and activism targeted towards project infrastructure.
- 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 continually monitors legislative and regulatory developments and engages appropriately with legislative and regulatory bodies to manage regulatory risks. Santos and its operating joint venture partners work closely with relevant governments and landowners to ensure all concerns are fairly addressed and managed, and Santos' operations benefit from the support of governments and landowners. Santos and its operating joint venture partners also have comprehensive security and risk management plans in place, 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.

### **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, operational performance and other market conditions. Any failure to perform any of the 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.

### **Litigation risks**

- 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' legal team actively monitors and manages potential and actual claims, actions and disputes.

# Directors' Report

## continued

### **Operational, environmental and safety risks**

- 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 has a comprehensive approach to management of environmental, health and safety risks, which includes technical, operational and asset reliability and integrity standards and competency requirements designed to ensure it meets regulatory requirements and industry standards.

### **Joint venture arrangements**

- Santos' business is carried out through joint ventures. The use of joint ventures is common in the 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 works closely with its joint venture partners in order to reduce the risk of misalignment in joint venture activities.

### **Financial risks**

- Foreign currency risk

Santos is exposed to foreign currency risk principally through the sale of products denominated in US dollars, borrowings denominated in US dollars and Euros and foreign currency capital and operating expenditure.

- Credit risk

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.

- 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.

Santos' overall financial risk management strategy is to seek 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.

Consistent with the Company's focus on maximising operating cash flow and mitigating risk in volatile oil markets, in 2016 Santos established a specific Oil Price Hedging Policy. The objectives of the policy are to reduce 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.

### **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

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The Operating and Financial Review on (pages 18 to 26) outlines a number of significant changes in the state of affairs of the Company during the year and the Material business risks section (pages 24 to 26) outlines various risks, which if materialised, may have a significant effect on the state of affairs of the Company in subsequent financial years.

## DIVIDENDS

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On 16 February 2017, the Directors resolved not to pay a final dividend.

A fully franked final dividend of US\$66 million (A\$0.05 cents per fully paid ordinary share) was paid on 30 March 2016 in respect of the year ended 31 December 2015, as disclosed in the 2015 Annual Report. The Dividend Reinvestment Plan (DRP) was in operation and shares were allocated based on the DRP issue price that was advised to the market.

## ENVIRONMENTAL REGULATION

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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. Compliance performance is monitored on a regular basis and in various forms, including environmental audits conducted by regulatory authorities and by the Company, either through internal or external resources.

On 25 February 2016, Santos received a penalty infringement notice and \$8,835 fine from the Department of Environment and Heritage Protection (DEHP) for causing environmental nuisance due to black smoke releases from the GLNG facility on Curtis Island in November 2015. 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

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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 6 February 2017 Santos completed the Share Purchase Plan, as announced during December 2016, with total proceeds of approximately A\$201 million received.

On 16 February 2017, the Directors of Santos Limited resolved not to pay a final dividend in respect of the 2016 financial year.

## SHARES UNDER OPTION AND UNVESTED SHARE ACQUISITION RIGHTS

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### 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 <sup>1</sup> | Number of options |
|----------------------|------------------|------------------------------------|-------------------|
| 1 July 2007          | 30 June 2017     | \$14.14                            | 203,900           |
| 1 July 2007          | 30 June 2017     | \$14.14                            | 47,400            |
| 3 September 2007     | 2 September 2017 | \$12.81                            | 100,000           |
| 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            |
| 02 March 2009        | 2 March 2019     | \$14.81                            | 50,549            |
|                      |                  |                                    | <b>1,159,288</b>  |

<sup>1</sup> 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

## continued

### 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 |
|-------------------|--------------------------------------|
| 7 March 2014      | 1,253,618                            |
| 1 July 2014       | 304,787                              |
| 6 March 2015      | 2,072,453                            |
| 28 July 2015      | 658,853                              |
| 10 February 2016  | 333,822                              |
| 1 May 2016        | 42,585                               |
| 14 June 2016      | 4,556,550                            |
| 31 August 2016    | 690,195                              |
| 1 December 2016   | 23,777                               |
|                   | 9,936,640                            |

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 31 of this report and in note 7.2 to the financial statements.

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

#### Options

No options were exercised during the year ended 31 December 2016 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 2016 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 |
|-------------------|-------------------------|
| 21 June 2012      | 88,706                  |
| 15 April 2013     | 18,121                  |
| 1 July 2013       | 322,671                 |
| 21 January 2014   | 26,787                  |
| 1 July 2014       | 69,991                  |
| 28 July 2015      | 125,552                 |
| 31 August 2016    | 33,817                  |
|                   | 685,645                 |

Since 31 December 2016, the following ordinary shares of Santos Limited have been issued on the vesting of SARs granted under the SEEIP and ShareMatch.

| Date SARs granted | Number of shares issued |
|-------------------|-------------------------|
| 1 July 2014       | 1,412                   |
| 28 July 2015      | 2,100                   |
| 31 August 2016    | 977                     |
|                   | 4,489                   |

### 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 31 of this report and in notes 7.2 and 7.3 to the financial statements.

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# Remuneration in brief

This section is in addition to the Remuneration Report on pages 31 to 49. 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 2016. The Company has chosen to do this so that investors have the benefit of this information in addition to the Remuneration Report on pages 31 to 49, which has been prepared in accordance with statutory requirements and accounting standards.

## 2016 – THE START OF THE COMPANY'S TURNAROUND

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Santos' performance in 2016 points to the Company's turnaround having begun. Under the leadership of the new CEO, Kevin Gallagher, and the newly formed Executive team, Santos achieved record production of 61.6 mmbbl, record sales of 84.1 mmbbl, generated free cash flow of US\$206 million (before asset sales) and implemented sustainable cost out and productivity measures that will drive further value from the existing asset base and position the Company to deliver its strategy over the next few years. By year end 2016, the Company had reached a free cash flow breakeven oil price of US\$36.50 per barrel. Santos is also proud to have continued its strong safety record and achieved its lowest three-year rolling average lost time injury frequency rate in five years.

The actions of the CEO and the Executive team have set a strong foundation for delivering value to shareholders over the coming years. In recognition that the CEO and many of the Executive joined Santos in 2016, and are responsible for the swift and decisive actions to stabilise the business, reduce costs, increase operating cash flow and reduce debt, the Board has determined that the 2016 Short-Term Incentive (STI) award will be based on the Company's Scorecard performance score of 86.5% (see page 33 for explanation of the score). The Board determined that awarding the 2016 STI in accordance with the Scorecard recognises and rewards the achievement of the targets specifically set at the beginning of the year in order to drive the Company's turnaround and incentivises management to maintain the progress and momentum of that turnaround into 2017 and beyond. However, having regard to the year of continued volatile oil prices and modest returns for shareholders, and the Company's focus on maximising free cash flow, the Board and management have agreed that in addition to the 30% of any STI award that is deferred into equity for two years, a further 20% of the 2016 STI award to the CEO and Senior Executives will be awarded in ordinary shares, rather than in cash.

## ALIGNING REMUNERATION AND COMPANY PERFORMANCE

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Despite the strong operational performance during 2016, no Long-Term Incentive (LTI) vested because the Company did not achieve its relative Total Shareholder Return (TSR) targets. This is the sixth year in a row that relative TSR-tested LTI awards have lapsed, reflecting the clear link between shareholder returns and Senior Executive remuneration.

Santos continued to manage its Executive remuneration conservatively in response to market conditions by:

- setting the CEO's total remuneration package with a greater proportion "at risk" based on performance linked incentives;
- driving sustainable free cash flow generation and effective capital deployment through two additional new measures in the LTI plan, Free Cash Flow Breakeven Point (FCFBP) and Return on Average Capital Employed (ROACE), given success in these areas should lead to long-term shareholder value;
- allocating Share Acquisition Rights (SARs) on a face value, rather than fair value basis, for the Company's 2016 LTI Plan;
- focussing on financial performance in the Company Scorecard, taking it from the previous year's 45% to a 60% weighting of overall performance, and setting more challenging performance levels across the Scorecard;
- ensuring that any STI cash payments could be fully funded by free cash flow (FCF), such that if Santos did not reach its FCF gateway of achieving positive FCF in excess of the total net Santos STI cash cost, the CEO and Senior Executives' STI would be awarded as two-year deferred equity and not cash; and
- maintaining the same fees for non-Executive Directors (NED) that have been fixed since October 2013.

## REPORTING CURRENCY

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As announced to the market on 19 July 2016, Santos changed its reporting currency from A\$ to US\$ for the 2016 performance year. In line with Santos' US\$ reporting currency the majority of the Remuneration Report is now disclosed in US\$ (unless otherwise indicated) with all remuneration components having been converted from A\$ to US\$ using an average rate of \$0.7451 for 2016 and \$0.7523 for 2015.

The Actually realised remuneration table in this section will continue to be disclosed in A\$. Given the CEO and Senior Executives are contracted and paid in A\$ and are predominantly based in the Australian Head Office located in South Australia, the Actually realised remuneration table will continue to clearly provide the remuneration "actually realised" by the CEO and Senior Executives without US\$ exchange rate fluctuations.

# Remuneration in brief

## continued

### ACTUALLY REALISED REMUNERATION

The Table below shows remuneration "actually realised" by the CEO and Senior Executives in relation to 2016, namely:

- cash payments on account of Total Fixed Remuneration (TFR);
- STI awarded in cash and ordinary shares in respect of 2016 performance;
- deferred STI awards in respect of prior performance years which vested in 2016; and
- 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 2001* (Cth) 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 three-year LTI award tested at the end of 2016).

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: 2015 and 2016 Senior Executive remuneration details (see page 40).

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

|   | Year | 2014 deferred STI that vested in 2016 <sup>3</sup> |                       |                              |                  |                    |                     |           | Total |
|---|------|--|-----------------------|------------------------------|------------------|--------------------|---------------------|-----------|-------|
|   |      | TFR <sup>1</sup>                                   | Cash STI <sup>2</sup> | Ordinary shares <sup>4</sup> | LTI <sup>5</sup> | Other <sup>6</sup> | A\$                 |           |       |
|   |      | A\$  | A\$                   | A\$                          | A\$              | A\$                | A\$                 | A\$       |       |
| K Gallagher <sup>7</sup><br>Chief Executive Officer   | 2016 | 1,650,000  | 712,600               | –                            | 285,000          | –                  | 9,804 <sup>8</sup>  | 2,657,404 |       |
| J Anderson <sup>9</sup><br>Executive Vice President<br>Commercial and Business<br>Development | 2016 | 740,504  | 275,700               | 54,817                       | 110,300          | –                  | 15,000              | 1,196,321 |       |
|   | 2015 | 712,016  | –                     | –                            | –                | –                  | 45,000              | 757,016   |       |
| V Santostefano <sup>10</sup><br>Chief Operations Officer                                      | 2016 | 662,195  | 243,100               | –                            | 97,200           | –                  | 9,804               | 1,012,299 |       |
| A Seaton<br>Chief Financial Officer   | 2016 | 770,752  | 566,700 <sup>11</sup> | 58,310                       | –                | –                  | –                   | 1,395,762 |       |
|   | 2015 | 770,752  | –                     | –                            | –                | –                  | –                   | 770,752   |       |
| B Woods <sup>12</sup><br>Vice President Development   | 2016 | 660,000  | 202,600               | –                            | 81,000           | –                  | 3,248 <sup>13</sup> | 946,848   |       |
|   | 2015 | 561,167  | –                     | –                            | –                | –                  | 9,804               | 570,971   |       |
| T Brown <sup>14</sup><br>Vice President Queensland  | 2016 | 365,429  | 126,900 <sup>15</sup> | 63,608                       | –                | –                  | –                   | 555,937   |       |
|   | 2015 | 724,914  | –                     | –                            | –                | –                  | 1,477               | 726,391   |       |

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

2 50% of the STI award for 2016 performance for continuing Executives will be paid in cash and this is the amount reported in the "Cash STI" column above. The remaining 50% will be awarded as equity with 20% delivered as ordinary shares and the remaining 30% delivered as deferred shares or SARs (subject to a two-year service-based period). The 2016 Company Scorecard outcome is presented at Table 1: 2016 STI scorecard performance on page 33. 2015 and 2016 Senior Executive remuneration details including deferred STI accounting valuations, can be found on page 40.

3 This relates to deferred restricted shares from the 2014 STI award that vested on 31 December 2016. The amount reflected is based on the closing share price of A\$4.02 on the vesting date.

4 This relates to the ordinary shares the CEO and Senior Executives will receive as part of the 2016 STI award. The amount reflected is based on the closing share price of A\$4.02 on 31 December 2016.

5 No LTI vested in 2016. For the value of share-based payments calculated in accordance with the Accounting Standards, see Table 5: 2015 and 2016 Senior Executive remuneration details on page 40.

6 "Other" comprises ad hoc payments treated as remuneration, such as assignment and mobilisation allowances.

7 Mr Gallagher became a key management personnel (KMP) on 1 February 2016 when he commenced as the CEO.

8 Mr Gallagher received a relocation allowance in February 2016.

9 Mr Anderson remained a KMP for the whole of 2016, initially as Vice President (VP) Asia, WA and NT and then in the role of Executive Vice President (EVP) Commercial and Business Development from 1 July 2016.

10 Mr Santostefano became a KMP on 21 March 2016 when he commenced as Chief Operations Officer.

11 At the time of paying Mr Seaton's 2016 STI in April 2017, he will no longer be employed by the Company. His 2016 STI will be delivered wholly in cash. These figures for Mr Seaton do not include any termination payments, details of which are set out in Table 5: 2015 and 2016 Senior Executive remuneration details.

12 For comparison purposes when Mr Woods' was promoted to VP Eastern Australian Business Unit his TFR on an annual basis was A\$630,000. His 2016 TFR of A\$670,000 represents a 6.3% increase, in line with his increased responsibilities as VP Development.

13 This amount represents Mr Woods' previous participation in the Company's employee share plan prior to becoming a KMP in August 2015 and 808 of these shares vested in 2016. The amount reflected is based on the closing share price of A\$4.02 on 31 December 2016. This value may not reflect the actual benefit received.

14 Mr Brown was a KMP from 1 January 2016 to 20 March 2016 while in the role of VP Queensland. He ceased to be a KMP on 21 March 2016. Mr Brown continued to provide transitional support for three months after ceasing to be a KMP and his total remuneration earned for 2016 has been provided for comparison purposes. The figures for Mr Brown do not include his termination payments, details of which are set out in Table 5: 2015 and 2016 Senior Executive remuneration details.

15 Given Mr Brown is no longer employed by the Company, his pro-rated 2016 STI will be delivered wholly in cash.

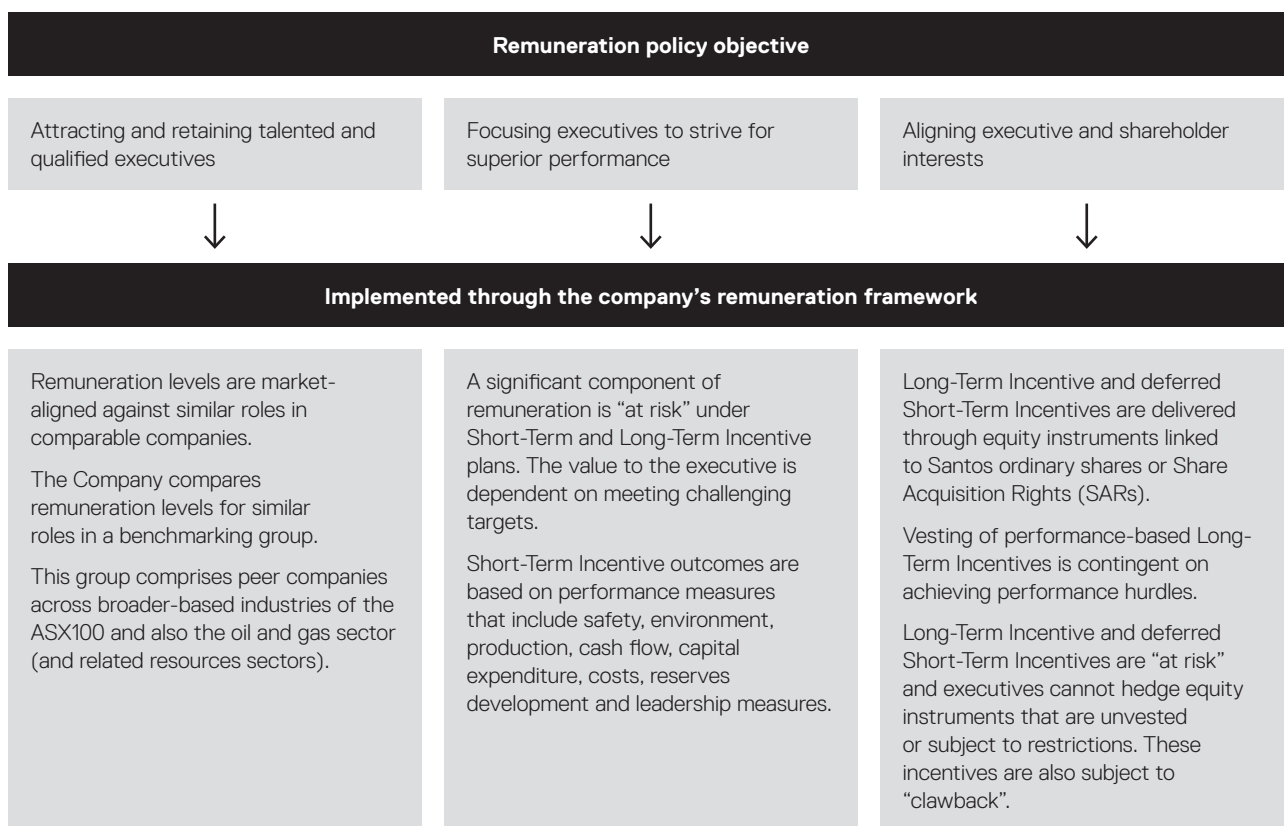


# Remuneration Report

The Directors of Santos Limited (referred to as “the Company” or “Santos”) present this Remuneration Report for the consolidated entity for the year ended 31 December 2016. 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 2016 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 Executives 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 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 2016, no remuneration recommendations were provided by remuneration consultants.

# Remuneration Report

## continued

### REMUNERATION FRAMEWORK

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#### Remuneration benchmarking

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

#### TFR

TFR comprises base pay and superannuation and is reviewed annually and formally benchmarked against comparable peer companies. It is set by reference to an individual's role and responsibilities and also reflects an individual's experience and competencies.

#### STI

The Company sets a range of short-term operational and financial targets to be achieved annually. 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 33 outlines the short-term objectives used in 2016 to measure performance for STI purposes and the reasons why these objectives were chosen.

To drive a focus on productivity and cash flow in a low oil price environment significant changes were made to the 2016 Company Scorecard and remuneration framework including increasing the financial based metrics to 60% weighting and introducing a Free Cash Flow (FCF) gateway for any cash STI award.

If the FCF gateway is met, the Company's policy is to deliver 30% of any STI award for the CEO and Senior Executives into deferred shares or SARs. If the gateway is not met, 100% of any STI award 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 are provided in relation to the STI program on page 47.

#### LTI

In order to align the interests of executives with the creation of long-term shareholder value, the Company awards its LTI grants as SARs. The SARs are granted at no cost and only vest if the Company meets a number of performance hurdles. In 2016 the Company introduced two new performance conditions into the LTI program: Free Cash Flow Breakeven Point (FCFBP) and Return on Average Capital Employed (ROACE), in addition to the two relative Total Shareholder Return (TSR) measures. Both FCFBP and ROACE align with the Company's focus on cash flow generation, debt reduction and effective use of capital to grow shareholder value.

Vesting of the 2016 LTI grants is based on the following performance targets:

- 25% relative TSR measured against companies in the ASX100;
- 25% relative 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 48.

#### 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 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.

## Link between performance and remuneration

### 2016 STI scorecard performance

The Company's performance against the 2016 STI scorecard as assessed by the Board resulted in a score of 86.5%. The table below summarises the short-term objectives in the scorecard, their rationale and the Company's performance against them.

**Table 1: 2016 STI scorecard performance**

|   | STI Measure   | Rationale  | Performance  | Score |
|---|---|--|--|-------|
| <b>Risk and Operational Integrity (20%)</b> | <p><b>Personnel safety</b></p> <p>Measured by the rolling average number of lost time injuries per million hours worked over a three-year period (2014 to 2016).</p>  | The Company is committed to providing a workplace without injury or illness and managing the impact of our operations on the environment.  | The Company achieved a three-year rolling lost time injury frequency rate of 0.40, exceeding the Company target.                           | 17.3% |
|   | <p><b>Process safety</b></p> <p>Measured by the number of Tier 1 loss of containment of hydrocarbon incidents, and the level of Safety Critical Compliance performed on plant and equipment in enclosed and open areas.</p> | The integrated targets for personnel safety, process safety, and the environment represent the Company's holistic approach to safety management. This 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 incidence of significant environmental incidents. | Safety Critical Maintenance was slightly below target and Tier 1 loss of containment of hydrocarbon incidents achieved better than target. |       |
|   | <p><b>Environmental incidents</b></p> <p>Measured by the number of environmental incidents of moderate or greater consequence.</p>  |  | There were no environmental incidents of moderate or greater consequence.  |       |
|   | <p><b>Enterprise risk reviews</b></p> <p>Measured by the number of reviews conducted by the Executive Committee of the Company's Risk Management Framework.</p>   | The continued focus on the Company's Risk Management Framework represented a commitment by the Santos Executive Committee for risk to be a regular part of the conversation.   | Enterprise risk reviews were conducted by the Executive Committee at the target level.   |       |

# Remuneration Report

## continued

|                               | STI Measure   | Rationale  | Performance   | Score        |
|-------------------------------|---|--|---|--------------|
| Financial & Operational (60%) | <b>Production</b>   | Production is critical to the Company's profitability and overall performance, and underpins annual earnings and cash flow.  | Production of 61.6 mmbob, the highest annual production ever, was at the upper end of the guidance range.   | 55.0%        |
|                               | <b>Operating cash flow</b><br>Operating cash flow measures the net cash flow from operating activities as reported in the Company's Consolidated Statement of Cash Flows.                 | Maximising cash from operating activities is essential to drive returns and support reinvestment for future growth.  | Strong operating cash flow of US\$857 million exceeded target due to a focus on maximising production, cost reductions and operational efficiencies. This improved the Free Cash Flow Breakeven Point to US \$36.50 per barrel.   |              |
|                               | <b>Capital expenditure</b>  | Capital expenditure was introduced as a measure to reflect the focus on preserving capital in a low oil price environment.   | Capital expenditure was significantly reduced for a result of US\$625 million which was better than target (including the average Cooper Basin gas well costs down 12% to US\$4.2 million per well).  |              |
|                               | <b>Total cash operating costs and selling, general and administration costs</b>   | Total Cash Operating Costs and Selling, General and Administration costs were introduced to reflect the focus on reducing costs and lifting efficiency across the entire Company.                    | Total Cash Operating Costs and Selling, General and Administration costs of US\$924 million met target. Efficiencies delivered through restructuring incurred a one-off cost of US\$40 million.   |              |
| Value Creation (10%)          | <b>Reserves replacement</b><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 target was not achieved as our focus in 2016 was conversion of undeveloped reserves and resources to developed.  | 5.6%         |
|                               | <b>2P undeveloped to developed reserves conversion cost (\$/boe)</b><br>The cost of developing existing 2P reserves into developed reserves ready for production.                         | This conversion cost metric assesses how efficiently capital is being deployed to develop booked 2P reserves for production.   | The Undeveloped to Developed Reserves conversion cost (\$/boe) was slightly below target.   |              |
|                               | <b>Net debt</b>   | Net debt was introduced to reflect 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. | Net debt was substantially reduced to US\$4.23 billion which met the target (excluding the proceeds of the Institutional Placement at the end of 2016).   |              |
| Leadership (10%)              | <b>Leadership</b><br>To drive leadership behaviours and a "one team" culture.   | The new Excom must have a results focus to drive Santos' transformation, generate stronger returns and ensure the long-term sustainability of the Company.   | The Excom delivered strong leadership performance in 2016. The organisation restructured and a new operating model was established. A low cost high performing culture was driven through the business as demonstrated through the significant improvements in Free Cash Flow and Net Debt reduction. | 8.6%         |
|                               |   |  | <b>Total</b>  | <b>86.5%</b> |

## LTI PERFORMANCE

The Company's TSR for the period 1 January 2014 to 31 December 2016 ranked below the 51<sup>st</sup> percentile in the comparator groups comprising the companies in the ASX 100 and S&P GEI. As a result, none of the SARs granted to the Executives in 2014 as part of the three-year transitional 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 47 and 48.

## 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 2012 – 2016**

|  | 2012     | 2013     | 2014             | 2015        | 2016                 |
|--|----------|----------|------------------|-------------|----------------------|
| Injury frequency   |          |          |                  |             |                      |
| total recordable case frequency rate   | 5.0      | 3.8      | 3.5              | 2.8         | 2.2                  |
| lost time injury frequency rate (three-year rolling average)                 | 0.9      | 0.8      | 0.7              | 0.5         | 0.4                  |
| Production (mmboe)   | 52.1     | 51.0     | 54.1             | 57.7        | 61.6                 |
| Reserve replacement rate – 2P organic (%)                                    | 136      | 3        | 0                | 0           | 19                   |
| Net profit/(loss) after tax <sup>1</sup> (\$m)                               | US\$537  | US\$499  | US\$(630)        | US\$(1,953) | US\$(1,047)          |
| Dividends per ordinary share (cents) A\$                                     | 30       | 30       | 35               | 20          | 0                    |
| Share price – closing price on first trading day of year                     | A\$12.34 | A\$11.11 | A\$14.63         | A\$8.25     | A\$3.68 <sup>2</sup> |
| LTI performance (% vesting) – shown against final year of performance period | 0%       | 0%       | 0%               | 0%          | 0%                   |
| STI score (% of maximum)   | 68%      | 60%      | 58% <sup>3</sup> | 67%         | 86.5%                |

1 2012–2015 Net profit/(loss) after tax figures have been translated from A\$ to US\$ at an applicable exchange rate for the year for comparison purposes.

2 Closing share price at 31 December 2016 was A\$4.02.

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

# Remuneration Report

## continued

### CEO REMUNERATION

|   |   |
|---|---|
| What is the CEO's TFR?                              | US\$1,341,180 per annum.  |
| 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\$1,117,650.<br><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 previous employer, the CEO received SARs with a face value of US\$745,100 equal to a total of 333,822 SARs. The conditions of the grant were as follows: <ul style="list-style-type: none"> <li>• 50% (166,911 SARs) that vested on 31 January 2017; and</li> <li>• 50% (166,911 SARs) will vest on 31 January 2018.</li> </ul> <p>The unvested rights will vest in line with the above provided the CEO has not resigned or been terminated by the Company for cause or terminated his employment by mutual agreement with the Company.</p> <p>Any unvested rights will vest immediately (or at his election stay on foot and vest at the end of the two-year period) if the Company terminates his employment without cause or if the CEO terminates his employment due to a fundamental change in his role or his employment is terminated due to death or incapacity.</p> <p>Following vesting, the CEO will have five years to convert the rights into Santos shares. The CEO does not need to pay any amount on conversion of the rights.</p> |

### 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 2016 performance? | The CEO's performance was assessed using the Company Scorecard. The overall result was 86.5% of maximum. Given the CEO's commencement date of 1 February 2016, his STI was pro-rated for the period from his commencement date to 31 December 2016. This has a total value equivalent to US\$1,061,842: 50% will be paid in cash, 20% delivered as ordinary shares and 30% delivered as deferred equity. |

### 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 2016 Annual General Meeting (AGM), the CEO was granted 901,320 SARs as his 2016 LTI. |
| What are the performance conditions of the 2016 LTI grant for the CEO? | The performance conditions of the CEO's grant are the same as the Senior Executives' grant as outlined on page 48.  |

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## SENIOR EXECUTIVE REMUNERATION

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### Fixed remuneration

|  |   |
|--|---|
| Was there an increase in Senior Executives' TFR? | Mr Anderson and Mr Woods' received TFR increases of between 5.3% and 6.3% as a result of market benchmarking of their roles. Market appropriate remuneration levels for new KMP were set at the commencement of their employment in 2016. |
|--|---|

### STI

|   |   |
|---|---|
| What was the maximum STI Senior Executives could receive?                   | The Senior Executives have a maximum STI opportunity of between 70% and 85% of their TFR.   |
| How were STI payments calculated?   | To promote alignment and focus of the new Excom on the organisation's turnaround, in 2016, all Senior Executives shared the Corporate Scorecard as the basis for 90% of their performance outcome. The other 10% of the performance outcome was based on the individual Executive's leadership and contribution to the delivery of the Company's results.   |
| How was performance assessed for STI purposes?                              | Company performance against the overall Corporate scorecard was assessed by the Committee and the Board.<br><br>Senior Executives' performance against the individual Leadership component was assessed by the CEO, and reviewed and endorsed by the Committee.   |
| How much STI will Senior Executives receive in respect of 2016 performance? | The Company's performance against the 2016 STI Scorecard as assessed by the Board resulted in a score of 86.5%. 50% of the STI award will be paid in cash and the remaining 50% will be awarded as equity with 20% delivered as ordinary shares and the remaining 30% delivered as deferred shares or SARs (subject to a two-year service-based period). Further details for each individual Senior Executive's remuneration are provided in Table 5: 2015 and 2016 Senior Executive remuneration details on page 40. |

### LTI

|  |   |
|--|---|
| How much LTI was granted to Senior Executives in 2016?   | In 2016, all Senior Executives received an LTI award equivalent to 80% of TFR which was allocated on a face value basis. This is different to the 2015 grant size in which Senior Executives received an LTI award of between 50% and 60% of TFR and SARs were allocated on a fair value basis. |
| What are the performance conditions?                     | The grant has a four-year performance period from 1 January 2016 to 31 December 2019. Vesting is based on the four equally weighted performance targets as indicated on page 48. The vesting schedule can be also be found on page 49.  |
| What proportion of prior year LTI grants vested in 2016? | Nil.<br><br>The testing of the three-year 2014 LTI grant with a performance period 1 January 2014 to 31 December 2016 occurred in early 2017. As the performance hurdle was not achieved, there was no vesting of the grant and this 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.

# Remuneration Report

## continued

### 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.

For Senior Executives, the slight increase in proportion of "at risk" remuneration reflects the change in LTI allocation methodology, given an increase in LTI as a percentage of TFR occurred to partially offset the move from fair to face value basis for allocating SARs.

**Table 3: Relative weightings of remuneration components for CEO and Senior Executives<sup>1</sup>**

|  |                   | At risk remuneration |                  |              |                           | Total       |
|--|-------------------|----------------------|------------------|--------------|---------------------------|-------------|
|  |                   | Fixed remuneration   | STI <sup>2</sup> | LTI          | Total "at risk"           |             |
| <b>CEO<sup>3</sup> (Kevin Gallagher)</b> | <b>2016</b>       | <b>28.6%</b>         | <b>28.6%</b>     | <b>42.8%</b> | <b>71.4%</b>              | <b>100%</b> |
| <b>Former CEO (David Knox)</b>           | 2015 <sup>4</sup> | 33.3%                | 33.3%            | 33.3%        | 66.6%                     | 100%        |
| <b>Senior Executives</b>                 | <b>2016</b>       | <b>38.2%</b>         | <b>31.2%</b>     | <b>30.6%</b> | <b>61.8%</b> <sup>5</sup> | <b>100%</b> |
|  | 2015              | 40.8%                | 34.7%            | 24.5%        | 59.2%                     | 100%        |

<sup>1</sup> These figures represent maximum potential of each component. They 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.

<sup>2</sup> Also includes deferred STI component.

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

<sup>4</sup> 2015 relates to the former CEO.

<sup>5</sup> As noted on page 37 the increase in LTI as a percentage of TFR was made with the change from fair to face value allocation basis and is reflected in the proportion of Senior Executive remuneration being "at risk".

### 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  |
|---|---|--|
| <p>Fee levels are set with regard to:</p> <ul style="list-style-type: none"> <li>time commitment and workload;</li> <li>the risk and responsibility attached to the role;</li> <li>experience and expertise; and</li> <li>market benchmarking.</li> </ul> | <ul style="list-style-type: none"> <li>Fee levels do not vary according to the performance of the Company or individual Director performance from year to year.</li> <li>Independent Directors performance is assessed at the time of re-election.</li> </ul> | <ul style="list-style-type: none"> <li>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 within three years.</li> <li>Non-executive Directors can acquire shares through acquisition on market during trading windows and/or through the Non-executive Director share plan.</li> </ul> |



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### Maximum aggregate amount

Total fees paid to all non-executive Directors in a year, including Board Committee fees, must not exceed US\$1,937,260, 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 10: 2015 and 2016 Non-executive Director remuneration details on page 43.

### Fee structure

**Table 4: Non-executive Directors' fees per annum<sup>1</sup>**

|  | <b>Chair<sup>2</sup></b> | <b>Member</b> |
|--|--------------------------|---------------|
|  | <b>US\$</b>              | <b>US\$</b>   |
| Board  | \$375,195                | \$124,842     |
| Audit and Risk Committee                                 | \$31,294                 | \$15,647      |
| Environment, Health, Safety and Sustainability Committee | \$16,392                 | \$11,177      |
| Nomination Committee <sup>3</sup>                        | N/A                      | \$7,451       |
| People and Remuneration Committee                        | \$22,353                 | \$11,922      |

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).

# Remuneration Report

## continued

### DETAILED REMUNERATION INFORMATION

Table 5 presents summarised details of the remuneration for the KMPs in 2015 and 2016 as required under the Corporations Act. The current KMP are the Executives that Santos considers having the requisite authority and responsibility to meet the definition of Key Management Personnel following the formation of the new Excom. All remuneration components have been converted from A\$ to US\$ using an average rate of \$0.7451 for 2016 and \$0.7523 for 2015.

**Table 5: 2015 and 2016 Senior Executive remuneration details**

|                             | Short-term employee benefits |                  |                    | Post-employment              |        |         | Share-based payments <sup>1</sup> |         |                              |                            | Other long-term benefits (long service) <sup>5</sup> |         | Total "at risk" <sup>6</sup> |     |
|-----------------------------|------------------------------|------------------|--------------------|------------------------------|--------|---------|-----------------------------------|---------|------------------------------|----------------------------|--|---------|------------------------------|-----|
|                             | Base salary                  | STI <sup>2</sup> | Other <sup>3</sup> | Superannuation contributions |        | LTI     | Deferred STI <sup>4</sup>         | Options | Ordinary shares <sup>5</sup> | Total share-based payments | Termination  | Total   |                              | %   |
|                             |                              | US\$             | US\$               | US\$                         | US\$   |         | US\$                              | US\$    |                              |                            | US\$   |         |                              |     |
| KT Gallagher <sup>7</sup>   | 2016                         | 1,205,510        | 530,958            | 7,305                        | 23,905 | 904,818 | 101,448                           | –       | 212,354                      | 1,218,620                  | –  | –       | 2,986,298                    | 59% |
|                             | 2015                         | –                | –                  | –                            | –      | –       | –                                 | –       | –                            | –                          | –  | –       | –                            | –   |
| JH Anderson                 | 2016                         | 525,671          | 205,424            | 11,177                       | 26,079 | 293,560 | 140,048                           | –       | 82,185                       | 515,793                    | –  | (2,737) | 1,281,407                    | 56% |
|                             | 2015                         | 515,419          | –                  | 33,854                       | 20,231 | 305,903 | 84,342                            | –       | –                            | 390,245                    | –  | 3,531   | 963,280                      | 41% |
| V Santostefano <sup>8</sup> | 2016                         | 476,637          | 181,134            | 7,305                        | 16,765 | 67,947  | 29,523                            | –       | 72,424                       | 169,894                    | –  | –       | 851,735                      | 41% |
|                             | 2015                         | –                | –                  | –                            | –      | –       | –                                 | –       | –                            | –                          | –  | –       | –                            | –   |
| AJ Seaton <sup>9</sup>      | 2016                         | 548,209          | 422,248            | –                            | 26,079 | 313,566 | 26,587                            | –       | –                            | 340,153                    | 430,715  | 13,520  | 1,780,924                    | 43% |
|                             | 2015                         | 559,607          | –                  | –                            | 20,231 | 330,863 | 26,771                            | –       | –                            | 357,634                    | –  | 6,872   | 944,344                      | 38% |
| BK Woods <sup>10</sup>      | 2016                         | 469,413          | 150,957            | –                            | 22,353 | 171,509 | 84,362                            | –       | 60,353                       | 316,224                    | –  | 3,601   | 962,548                      | 49% |
|                             | 2015                         | 186,126          | –                  | 7,376                        | 9,283  | 51,722  | 17,766                            | –       | –                            | 69,488                     | –  | 4,633   | 276,906                      | 25% |
| TJ Brown <sup>11</sup>      | 2016                         | 115,891          | 94,553             | –                            | 3,171  | 48,241  | 22,484                            | –       | –                            | 70,725                     | 405,100  | 14,990  | 704,430                      | 23% |
|                             | 2015                         | 531,025          | –                  | 1,111                        | 14,328 | 311,012 | 89,454                            | –       | –                            | 400,466                    | –  | 5,759   | 952,689                      | 42% |

<sup>1</sup> 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.

<sup>2</sup> This amount represents the cash portion of the STI performance award for 2016, which will be paid in April 2017.

<sup>3</sup> "Other" comprises ad hoc payments treated as remuneration, such as assignment and mobilisation allowance.

<sup>4</sup> 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.

<sup>5</sup> 20% of the 2016 STI award will be delivered as ordinary shares. The amount reflected is based on the closing share price of A\$4.02 at 31 December 2016. All values have been converted to US\$.

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

<sup>7</sup> Mr Gallagher became a KMP on 1 February 2016. Figures shown for Mr Gallagher are for the period 1 February 2016 to 31 December 2016.

<sup>8</sup> Mr Santostefano became a KMP on 21 March 2016. Figures shown for Mr Santostefano are for the period 21 March 2016 to 31 December 2016.

<sup>9</sup> Mr Seaton remained a KMP for the entire year and figures shown are for the period 1 January 2016 to 31 December 2016 as well as the termination payment he will receive in 2017 on the cessation of his employment.

<sup>10</sup> Mr Woods remained a KMP for the entire year and figures shown are for the period 1 January 2016 to 31 December 2016. In 2015, he became a KMP on 3 August 2015 and the figures for 2015 are for the period 3 August 2015 to 31 December 2015.

<sup>11</sup> Mr Brown ceased to be a KMP on 21 March 2016. Figures shown for Mr Brown are for the period 1 January 2016 to 20 March 2016.

Table 6 contains details of the number and value of SARs that were granted, vested and lapsed for the CEO in 2016. The CEO did not have any options granted, vesting or lapsing in 2016. The CEO has no options to exercise.

**Table 6: 2016 SARs outcomes for CEO**

|      | Granted                |                            | Vested |       | Lapsed |
|------|------------------------|----------------------------|--------|-------|--------|
|      | Number                 | Maximum value <sup>1</sup> | Number | Value | Number |
|      | US\$                   |                            |        |       |        |
| SARs | 1,235,142 <sup>2</sup> | 3,211,862                  | –      | –     | –      |

1 Maximum value represents the fair value of LTI grants received in 2016 determined in accordance with AASB 2 *Share-based Payment*. The fair values represent multiple grants in 2016 weighted at a fair value of A\$3.49. 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\$.

2 The number of SARs granted to the CEO relate to his 2016 sign-on grant of 333,822 and the 2016 LTI performance grant of 901,320.

Tables 7 and 8 contains details of the number and value of shares and SARs granted, vested and lapsed for Senior Executives in 2016. No Senior Executive had any options granted, vesting or lapsing in 2016. No options were exercised in 2016.

**Table 7: 2016 SARs outcomes for Senior Executives**

|                | Granted             |                            | Vested   |          | Lapsed                 |
|----------------|---------------------|----------------------------|----------|----------|------------------------|
|                | Number <sup>1</sup> | Maximum value <sup>2</sup> | Number   | Value    | Number <sup>3</sup>    |
|                | US\$                |                            |          |          |                        |
| JH Anderson    | 155,844             | 429,642                    | –        | –        | (48,980)               |
| V Santostefano | 176,620             | 486,918                    | –        | –        | –                      |
| AJ Seaton      | 160,156             | 441,529                    | –        | –        | (53,020)               |
| BK Woods       | 139,220             | 383,811                    | –        | –        | (20,545)               |
| TJ Brown       | –                   | –                          | –        | –        | (125,693) <sup>4</sup> |
| <b>Total</b>   | <b>631,840</b>      | <b>1,741,900</b>           | <b>–</b> | <b>–</b> | <b>(248,238)</b>       |

1 The grant relates to the Senior Executives' full LTI awards for the four-year performance period ending on 31 December 2019.

2 Maximum value represents the fair value of LTI grants received in 2016 determined in accordance with AASB 2 *Share-based Payment*. The fair values of the grant as at the grant date of 29 June 2016 is weighted at a fair value of A\$3.70. 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 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 LTI grant.

4 The total for Mr Brown includes SARs related to previous LTI grants which lapsed after he ceased to be a KMP on 21 March 2016 (84,152 lapsed SARs) in addition to the lapsed SARs related to the 2014 LTI grant (41,541 lapsed SARs).

# Remuneration Report

## continued

**Table 8: 2016 share outcomes for Senior Executives**

|                             | Granted             |                            | Vested              |                    | Lapsed   |
|-----------------------------|---------------------|----------------------------|---------------------|--------------------|----------|
|                             | Number <sup>1</sup> | Maximum Value <sup>2</sup> | Number <sup>3</sup> | Value <sup>4</sup> | Number   |
|                             |                     | US\$                       |                     | US\$               |          |
| JH Anderson                 | 74,881              | 217,038                    | 13,636              | 40,844             | –        |
| V Santostefano <sup>5</sup> | –                   | –                          | –                   | –                  | –        |
| AJ Seaton <sup>6</sup>      | –                   | –                          | 14,505              | 43,447             | –        |
| BK Woods <sup>7</sup>       | 54,556              | 158,127                    | 808 <sup>8</sup>    | 2,420              | –        |
| TJ Brown                    | 76,242              | 220,983                    | 15,823              | 47,395             | –        |
| <b>Total</b>                | <b>205,679</b>      | <b>596,148</b>             | <b>44,772</b>       | <b>134,106</b>     | <b>–</b> |

1 This relates to the 2015 STI award. The entire award was deferred into shares for two-years that were granted on 11 May 2016.

2 Maximum value represents the fair value of 2015 STI shares received in 2016 determined in accordance with AASB 2 Share-based Payment. The fair value of the grant as at the grant date of 11 May 2016 is weighted at a fair value of A\$3.89. The minimum total value of the grant, if the applicable vesting conditions are not met, is nil. All values have been converted to US\$.

3 This relates to the 2014 STI grant that was deferred for two-years from 1 January 2015 to 31 December 2016 which vested in full on 31 December 2016.

4 These figures show the value of the 2014 deferred STI grant, using the share price of A\$4.02 on 31 December 2016 converted to US\$.

5 Mr Santostefano only commenced in 2016 and did not participate in the 2015 STI Plan.

6 Mr Seaton forfeited his 2015 STI award.

7 Mr Woods did not participate in the 2014 deferred STI grant as he was not a Senior Executive at that time.

8 Mr Woods previously participated in the Company's general employee share plan prior to becoming a KMP in August 2015. In 2016 a total of 808 shares vested. The value reflected is based on the closing share price of A\$4.02 on 31 December 2016 converted to US\$.

Table 9 outlines the LTI grants that were tested or still in progress in 2016.

**Table 9: LTI grants**

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

Full details of all grants made prior to 2016 can be found in note 7.2 to the financial statements and in prior Remuneration Reports.

Details of the fees and other benefits paid to non-executive Directors in 2016 are set out in Table 10. No fee increases were received in 2016. Differences in fees received between 2015 and 2016 reflect changes in roles and responsibilities (i.e. Chair or Committee appointments) and superannuation payments. No share-based payments were made to any non-executive Directors.

**Table 10: 2015 and 2016 Non-executive Director remuneration details**

| Director                   | Year | Short-term benefits                               |  |               | Retirement benefits                 |                              | Total   |
|----------------------------|------|---|--|---------------|-------------------------------------|------------------------------|---------|
|                            |      | Directors' fees<br>(incl. committee fees)<br>US\$ | Fees for special duties or exertions<br>US\$ | Other<br>US\$ | Superannuation <sup>9</sup><br>US\$ | Share-based payments<br>US\$ |         |
| YA Allen <sup>1</sup>      | 2016 | 148,463   | –  | –             | 14,104                              | –                            | 162,567 |
|                            | 2015 | 146,916   | –  | –             | 13,957                              | –                            | 160,873 |
| PR Coates <sup>2</sup>     | 2016 | 373,938   | 30,621                                       | –             | 17,410                              | –                            | 421,969 |
|                            | 2015 | 299,885   | 131,797                                      | –             | 26,738                              | –                            | 458,420 |
| GM Cowan <sup>3</sup>      | 2016 | 99,463  | –  | –             | 9,405                               | –                            | 108,868 |
|                            | 2015 | –   | –  | –             | –                                   | –                            | –       |
| KA Dean <sup>4</sup>       | 2016 | 50,374  | –  | –             | 4,786                               | –                            | 55,160  |
|                            | 2015 | 154,056   | –  | –             | 14,106                              | –                            | 168,162 |
| RA Franklin <sup>5</sup>   | 2016 | 173,173   | –  | –             | 677                                 | –                            | 173,850 |
|                            | 2015 | 170,598   | –  | –             | 1,295                               | –                            | 171,893 |
| H Goh                      | 2016 | 164,353   | –  | –             | 557                                 | –                            | 164,910 |
|                            | 2015 | 165,896   | –  | –             | 607                                 | –                            | 166,503 |
| PR Hearl <sup>6</sup>      | 2016 | 89,411  | –  | –             | 8,494                               | –                            | 97,905  |
|                            | 2015 | –   | –  | –             | –                                   | –                            | –       |
| JS Hemstritch <sup>7</sup> | 2016 | 57,277  | –  | –             | 5,073                               | –                            | 62,351  |
|                            | 2015 | 168,726   | –  | –             | 14,328                              | –                            | 183,054 |
| GJW Martin <sup>8</sup>    | 2016 | 166,514   | –  | –             | 14,501                              | –                            | 181,015 |
|                            | 2015 | 168,958   | –  | –             | 14,328                              | –                            | 183,286 |
| SD Sheffield               | 2016 | 137,799   | –  | –             | 287                                 | –                            | 138,086 |
|                            | 2015 | 142,729   | –  | –             | 440                                 | –                            | 143,169 |

1 Ms Allen retired from the Audit and Risk Committee on 24 June 2016 and was appointed to the People and Remuneration Committee on 24 June 2016.

2 Mr Coates was appointed as the Chair of the Board on 1 May 2015. In addition to his role as Chair of the Board, Mr Coates acted in the role of Executive Chairman from 24 August 2015 until 31 January 2016. His remuneration in Table 10 shows his fees as both the Chair of the Board and the Executive Chairman.

3 Mr Cowan was appointed to the Board on 10 May 2016 and is the current Chair of the Audit and Risk Committee.

4 Mr Dean retired as a non-executive Director on 4 May 2016.

5 Mr Franklin is the current Chair of the Environment, Health, Safety and Sustainability Committee.

6 Mr Hearl was appointed to the Board on 10 May 2016 and is a member of the Audit and Risk Committee.

7 Ms Hemstritch retired as a non-executive Director on 4 May 2016.

8 Mr Martin is the current Chair of the People and Remuneration Committee, and was appointed to the Nomination Committee on 3 May 2016.

9 Includes superannuation guarantee payments. Superannuation guarantee payments are made to Mr Franklin, Mr Goh and Mr Sheffield only in relation to days worked in Australia.

# Remuneration Report

continued

## 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 key management person, including 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 <sup>1</sup> | Options exercised/<br>rights vested | Other changes <sup>2</sup> | Sold/<br>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 |
|--------------------------------------|---------------------|----------------------|-------------------------------------|----------------------------|----------------------|------------------|---------------------------|---|---|
| <b>2016</b>                          |                     |                      |                                     |                            |                      |                  |                           |   |   |
| <b>Options</b>                       |                     |                      |                                     |                            |                      |                  |                           |   |   |
| <b>Directors</b>                     |                     |                      |                                     |                            |                      |                  |                           |   |   |
| Gallagher, Kevin Thomas <sup>3</sup> | -                   | -                    | -                                   | -                          | -                    | -                | -                         | -   | -   |
| <b>Senior Executives</b>             |                     |                      |                                     |                            |                      |                  |                           |   |   |
| Anderson, John Hugh                  | 117,693             | -                    | -                                   | (78,100)                   | -                    | 39,593           | 39,593                    | 39,593                                    | -   |
| Brown, Trevor John <sup>4</sup>      | 37,137              | -                    | -                                   | (37,137)                   | -                    | -                | -                         | -   | -   |
| Santostefano, Vince <sup>5</sup>     | -                   | -                    | -                                   | -                          | -                    | -                | -                         | -   | -   |
| Seaton, Andrew John <sup>6</sup>     | 22,213              | -                    | -                                   | -                          | -                    | 22,213           | 22,213                    | 22,213                                    | -   |
| <b>Total</b>                         | <b>177,043</b>      | <b>-</b>             | <b>-</b>                            | <b>(115,237)</b>           | <b>-</b>             | <b>61,806</b>    | <b>61,806</b>             | <b>61,806</b>                             | <b>-</b>                                      |
| <b>SARs</b>                          |                     |                      |                                     |                            |                      |                  |                           |   |   |
| <b>Directors</b>                     |                     |                      |                                     |                            |                      |                  |                           |   |   |
| Gallagher, Kevin Thomas <sup>3</sup> | -                   | 1,235,142            | -                                   | -                          | -                    | 1,235,142        | -                         | -   | -   |
| <b>Senior Executives</b>             |                     |                      |                                     |                            |                      |                  |                           |   |   |
| Anderson, John Hugh                  | 188,134             | 155,844              | -                                   | (48,980)                   | -                    | 294,998          | -                         | -   | -   |
| Brown, Trevor John <sup>4</sup>      | 191,542             | -                    | -                                   | (191,542)                  | -                    | -                | -                         | -   | -   |
| Santostefano, Vince <sup>5</sup>     | -                   | 176,620              | -                                   | -                          | -                    | 176,620          | -                         | -   | -   |
| Seaton, Andrew John <sup>6</sup>     | 203,654             | 160,156              | -                                   | (53,020)                   | -                    | 310,790          | -                         | -   | -   |
| Woods, Brett Kenneth                 | 96,001 <sup>7</sup> | 139,220              | -                                   | (20,545)                   | -                    | 214,676          | -                         | -   | -   |
| <b>Total</b>                         | <b>679,331</b>      | <b>1,866,982</b>     | <b>-</b>                            | <b>(314,087)</b>           | <b>-</b>             | <b>2,232,226</b> | <b>-</b>                  | <b>-</b>                                  | <b>-</b>                                      |

|                                      | 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 |
|--------------------------------------|-----------------|----------------|------------------------|-----------------|------------------|-----------------|---------------------------|---|---|
| <b>2016</b>                          |                 |                |                        |                 |                  |                 |                           |   |   |
| <b>Deferred shares</b>               |                 |                |                        |                 |                  |                 |                           |   |   |
| <b>Directors</b>                     |                 |                |                        |                 |                  |                 |                           |   |   |
| Gallagher, Kevin Thomas <sup>3</sup> | –               | –              | –                      | –               | –                | –               | –                         | –   | –   |
| <b>Senior Executives</b>             |                 |                |                        |                 |                  |                 |                           |   |   |
| Anderson, John Hugh                  | 13,636          | 74,881         | (13,636)               | –               | –                | 74,881          | 13,636                    | 13,636                                    | –   |
| Brown, Trevor John <sup>4</sup>      | 15,823          | 76,242         | (15,823)               | (76,242)        | –                | –               | 15,823                    | 15,823                                    | –   |
| Santostefano, Vince <sup>5</sup>     | –               | –              | –                      | –               | –                | –               | –                         | –   | –   |
| Seaton, Andrew John <sup>6</sup>     | 14,505          | –              | (14,505)               | –               | –                | –               | 14,505                    | 14,505                                    | –   |
| Woods, Brett Kenneth                 | –               | 54,556         | –                      | –               | –                | 54,556          | –                         | –   | –   |
| <b>Total</b>                         | <b>43,964</b>   | <b>205,679</b> | <b>(43,964)</b>        | <b>(76,242)</b> | <b>–</b>         | <b>129,437</b>  | <b>43,964</b>             | <b>43,964</b>                             | <b>–</b>                                      |

1 SARs and deferred shares granted to Senior Executives including the CEO are disclosed in Tables 7 and 8.

2 "Other changes" include SARs that did not vest due to the non-fulfillment of vesting conditions and were forfeited during the year, deferred shares that were forfeited as well as changes resulting from individuals ceasing to be and becoming KMPs during the period.

3 Mr Gallagher became a KMP on 1 February 2016.

4 Mr Brown ceased to be a KMP on 21 March 2016.

5 Mr Santostefano became a KMP on 21 March 2016.

6 Mr Seaton remained a KMP up to and including 31 December 2016.

7 Mr Woods previously participated in the Company's general employee share plan prior to becoming a KMP in August 2015. His opening balance includes an additional 1,053 SARs from the general employee share plan (353 SARs from 2014 and 700 SARs from 2015).

# Remuneration Report

continued

## SHARE HOLDINGS

|                                      | Opening balance      | Received vesting of SARs | Purchased <sup>1</sup> | Sold             | Deferred 2014 STI that vested on 31 December 2016 | Other changes <sup>2</sup> | Closing balance | Balance held nominally at end of the year |
|--------------------------------------|----------------------|--------------------------|------------------------|------------------|---|----------------------------|-----------------|---|
| <b>2016</b>                          |                      |                          |                        |                  |   |                            |                 |   |
| <b>Ordinary shares – fully paid</b>  |                      |                          |                        |                  |   |                            |                 |   |
| <b>Directors</b>                     |                      |                          |                        |                  |   |                            |                 |   |
| Allen, Yasmin Anita                  | 15,883               | –                        | –                      | –                | –   | –                          | 15,883          | –   |
| Coates, Peter Roland                 | 92,872               | –                        | 26,315                 | –                | –   | 1,259                      | 120,446         | –   |
| Cowan, Guy Michael                   | –                    | –                        | 15,000                 | –                | –   | –                          | 15,000          | –   |
| Dean, Kenneth Alfred <sup>3</sup>    | 67,581               | –                        | 4,090                  | –                | –   | (71,671)                   | –               | –   |
| Franklin, Roy Alexander              | 25,104               | –                        | –                      | –                | –   | 84                         | 25,188          | –   |
| Gallagher, Kevin Thomas <sup>4</sup> | –                    | –                        | 100,000                | –                | –   | –                          | 100,000         | –   |
| Goh, Hock                            | 33,407               | –                        | –                      | –                | –   | –                          | 33,407          | –   |
| Hearl, Peter Roland                  | –                    | –                        | 45,000                 | –                | –   | –                          | 45,000          | –   |
| Hemstritch, Jane Sharman             | 63,482               | –                        | –                      | (63,804)         | –   | 322                        | –               | –   |
| Martin, Gregory John Walton          | 38,912               | –                        | –                      | –                | –   | –                          | 38,912          | –   |
| Sheffield, Scott Douglas             | 63,529               | –                        | –                      | –                | –   | –                          | 63,529          | –   |
| <b>Senior Executives</b>             |                      |                          |                        |                  |   |                            |                 |   |
| Anderson, John Hugh                  | 117,651 <sup>5</sup> | –                        | –                      | –                | 13,636  | –                          | 131,287         | –   |
| Brown, Trevor John <sup>6</sup>      | 437,680              | –                        | –                      | (328,597)        | 15,823  | (124,906)                  | –               | –   |
| Santostefano, Vince <sup>7</sup>     | –                    | –                        | –                      | –                | –   | –                          | –               | –   |
| Seaton, Andrew John <sup>8</sup>     | 58,494               | –                        | –                      | (20,000)         | 14,505  | 55                         | 53,054          | –   |
| Woods, Brett Kenneth                 | 1,861 <sup>9</sup>   | –                        | –                      | –                | –   | –                          | 1,861           | –   |
| <b>Total</b>                         | <b>1,016,456</b>     | <b>–</b>                 | <b>190,405</b>         | <b>(412,401)</b> | <b>43,964</b>                                     | <b>(194,857)</b>           | <b>643,567</b>  | <b>–</b>                                  |

1 Includes purchases on market and shares issued from post-tax fees under the non-executive Director Share Plan.

2 Dividend Reinvestment Plan allocations as well as changes resulting from individuals ceasing to be KMPs during the period.

3 Mr Dean retired as a non-executive Director on 4 May 2016.

4 Mr Gallagher became a KMP on 1 February 2016.

5 Mr Anderson's opening balance has increased by 6,492 shares being shares previously held.

6 Mr Brown ceased to be a KMP on 21 March 2016.

7 Mr Santostefano became a KMP on 21 March 2016.

8 Mr Seaton remained a KMP for the entire year up to and including 31 December 2016. He will cease to be a KMP on 1 January 2017.

9 Mr Woods previously participated in the Company's general employee share plan prior to becoming a KMP in August 2015. Mr Woods' holdings are included from 2013 (808 shares), 2014 (353 shares and 353 SARs) and 2015 (700 shares and 700 SARs). As highlighted in Table 8, Mr Woods' 808 shares from the 2013 Company's general employee share plan vested.



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

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### STI questions and answers

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|  |   |
|--|---|
| 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 of 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?  | <p>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: 2016 STI scorecard performance on page 33.</p> <p>The Board believes that this scorecard is balanced and focuses the CEO and Senior Executives' attention on achieving the key conditions and milestones necessary to deliver stronger returns to shareholders.</p>   |
| How is Company performance assessed?                             | <p>Company performance is formally assessed by the Committee against the overall Company scorecard at the end of each financial year, and this forms the basis of a recommendation to the Board.</p> <p>Each metric is assessed against an agreed target and assigned a percentage weighting of the total scorecard. The actual versus the 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.</p> <p>The Board believes the above method of assessment is rigorous and provides a balanced assessment of the Company's performance.</p> |
| How does Company performance impact the STI program?             | <p>First, 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 values of all eligible employees.</p> <p>Secondly, the Company's overall performance score contributes to the actual STI payment made to individuals in a given year. For the CEO, the Company performance outcome determines 100% of his 2016 STI payment. For Senior Executives, the Company performance outcome determines 90% of their STI payment. The other 10% is based on their individual performance assessment.</p>  |

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# Remuneration Report

## continued

### LTI questions and answers

How are LTIs linked to Company performance? LTI aligns the rewards received by the CEO and Senior Executives with the longer-term performance of Santos. The 2016 performance measures ensures Santos is able to measure its performance relative to other ASX 100 companies and international energy sector peers in addition to stabilising the business through strong cash flows and shareholder returns.

All 2016 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 the CEO and 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 after 2014 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 2016 LTI grants 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 additional performance hurdles been introduced into the LTI in 2016? In line with the Company's focus on cash flow generation, debt reduction and effective use of capital these additional performance hurdles will align the CEO and Senior Executives to deliver long-term shareholder value. Demonstrating improvements in cash flow and capital efficiency will be critical indicators of the successful delivery of the Company's new strategy. These performance hurdles aim to drive the underlying business to become an operationally efficient low-cost producer focused on delivering shareholder value throughout the oil price cycle.

FCFBP is the US\$ oil price at which cash flows from operating activities equal cash flows from investing activities, as published in the Company's financial statements. 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 individually material items including asset acquisitions and disposals that may otherwise distort the measurement.

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. As the aim of the condition is to measure the performance of the underlying business, the Board will have discretion to adjust the ROACE for individually material items that may otherwise distort the measurement.

For 2016, these performance hurdles will be measured at the end of the four-year performance period.

Why is Relative TSR also used as a performance target in the LTI? 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.

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## LTI questions and answers

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 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.

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.

How is vesting determined?

The vesting scales below apply to both the CEO and Senior Executives' 2016 LTI performance grants.

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

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

| <b>TSR percentile ranking</b>             | <b>% of grant vesting</b> |
|---|---------------------------|
| 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)

| <b>FCFBP</b>                              | <b>% of grant vesting</b> |
|---|---------------------------|
| Above US\$40/bbl                          | 0%                        |
| Equal to 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)

| <b>ROACE</b>   | <b>% of grant vesting</b> |
|--|---------------------------|
| Below 75% of the weighted average cost of capital (WACC) | 0%                        |
| Equal to 75% of WACC                                     | 50%                       |
| straight line pro-rata vesting in between                |                           |
| Equal to or above WACC                                   | 100%                      |

When can vested SARs be traded?

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

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# Directors' Report

## continued

### INDEMNIFICATION

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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 2016 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 2016 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 2017. 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

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

|                             |           |
|-----------------------------|-----------|
| Taxation and other services | \$16,000  |
| Assurance services          | \$360,000 |

The Directors are satisfied, based on the advice of the Audit & 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 & Risk Committee to ensure they do not impact the impartiality and objectivity of the auditor.

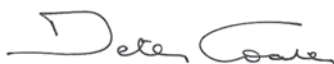
A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* (Cth) is set out on page 121.

### ROUNDING

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Australian Securities and Investments Commission Corporations (Rounding in Financial/Directors' Report) 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 16 February 2017 in accordance with a resolution of the Directors.



Director

# Financial Report

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# Consolidated Income Statement

## for the year ended 31 December 2016

|  | Note   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|--------|---------------------|-----------------------------------|
| Product sales  | 2.2    | <b>2,594</b>        | 2,442                             |
| Cost of sales  | 2.3    | <b>(2,153)</b>      | (1,883)                           |
| <b>Gross profit</b>  |        | <b>441</b>          | 559                               |
| Other revenue  |        | <b>33</b>           | 36                                |
| Other income   | 2.7    | <b>157</b>          | 9                                 |
| Impairment of non-current assets   | 3.3    | <b>(1,561)</b>      | (2,854)                           |
| Other expenses   | 2.3    | <b>(284)</b>        | (141)                             |
| Finance income   | 5.2    | <b>15</b>           | 6                                 |
| Finance costs  | 5.2    | <b>(296)</b>        | (223)                             |
| Share of net profit of joint ventures  | 6.3(c) | <b>10</b>           | 10                                |
| <b>Loss before tax</b>   |        | <b>(1,485)</b>      | (2,598)                           |
| Income tax benefit   | 2.4(a) | <b>445</b>          | 621                               |
| Royalty-related tax (expense)/benefit  | 2.4(b) | <b>(7)</b>          | 24                                |
| Total tax benefit  |        | <b>438</b>          | 645                               |
| <b>Net loss for the period attributable to owners of Santos Limited</b>            |        | <b>(1,047)</b>      | (1,953)                           |
| <b>Earnings per share attributable to the equity holders of Santos Limited (¢)</b> |        |                     |                                   |
| Basic loss per share   | 2.5    | <b>(58.2)</b>       | (169.5)                           |
| Diluted loss per share   | 2.5    | <b>(58.2)</b>       | (169.5)                           |
| <b>Dividends per share (¢)</b>   |        |                     |                                   |
| Paid during the period   | 2.6    | <b>4</b>            | 22                                |
| Declared in respect of the period  | 2.6    | <b>–</b>            | 15                                |

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

# Consolidated Statement of Comprehensive Income

## for the year ended 31 December 2016

|  | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|---------------------|-----------------------------------|
| <b>Net loss for the period</b>   | <b>(1,047)</b>      | <b>(1,953)</b>                    |
| <b>Other comprehensive income, net of tax:</b>   |                     |                                   |
| <i>Other comprehensive income to be reclassified to profit or loss in subsequent periods:</i>        |                     |                                   |
| Exchange loss on translation of foreign operations   | <b>(36)</b>         | (128)                             |
| Tax effect   | -                   | -                                 |
|  | <b>(36)</b>         | (128)                             |
| Gain/(loss) on foreign currency loans designated as hedges of net investments in foreign operations  | <b>20</b>           | (518)                             |
| Tax effect   | <b>(6)</b>          | 158                               |
|  | <b>14</b>           | (360)                             |
| Gain on derivatives designated as cash flow hedges   | <b>27</b>           | 4                                 |
| Tax effect   | <b>(8)</b>          | (1)                               |
|  | <b>19</b>           | 3                                 |
| <b>Net other comprehensive loss to be reclassified to profit or loss in subsequent periods</b>       | <b>(3)</b>          | (485)                             |
| <i>Items not to be reclassified to profit or loss in subsequent periods:</i>                         |                     |                                   |
| Remeasurement of defined benefit obligation  | <b>2</b>            | 4                                 |
| Tax effect   | <b>(1)</b>          | (1)                               |
|  | <b>1</b>            | 3                                 |
| <b>Net other comprehensive income not being reclassified to profit or loss in subsequent periods</b> | <b>1</b>            | 3                                 |
| <b>Other comprehensive loss, net of tax</b>  | <b>(2)</b>          | (482)                             |
| <b>Total comprehensive loss attributable to owners of Santos Limited</b>                             | <b>(1,049)</b>      | <b>(2,435)</b>                    |

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

# Consolidated Statement of Financial Position

as at 31 December 2016

|   | Note     | 2016<br>US\$million | (Restated)<br>2015<br>US\$million | (Restated)<br>2014<br>US\$million |
|---|----------|---------------------|-----------------------------------|-----------------------------------|
| <b>Current assets</b>                                     |          |                     |                                   |                                   |
| Cash and cash equivalents                                 | 4.1      | 2,026               | 839                               | 634                               |
| Trade and other receivables                               | 4.2      | 367                 | 392                               | 518                               |
| Prepayments   |          | 34                  | 47                                | 75                                |
| Inventories   | 4.3      | 321                 | 360                               | 362                               |
| Other financial assets                                    | 5.5(f)   | 7                   | 1                                 | 54                                |
| Tax receivable  |          | 15                  | 85                                | 47                                |
| Assets held for sale                                      | 3.6      | 180                 | 401                               | –                                 |
| <b>Total current assets</b>                               |          | <b>2,950</b>        | 2,125                             | 1,690                             |
| <b>Non-current assets</b>                                 |          |                     |                                   |                                   |
| Receivables   | 4.2      | 5                   | 4                                 | 8                                 |
| Prepayments   |          | 17                  | 20                                | 154                               |
| Investments in joint ventures                             | 6.3(b)   | 56                  | 71                                | 79                                |
| Other financial assets                                    | 5.5(f)   | 152                 | 158                               | 136                               |
| Exploration and evaluation assets                         | 3.1      | 495                 | 520                               | 905                               |
| Oil and gas assets  | 3.2      | 10,398              | 12,404                            | 15,071                            |
| Other land, buildings, plant and equipment                |          | 135                 | 181                               | 219                               |
| Deferred tax assets                                       | 2.4(d)   | 1,054               | 466                               | 19                                |
| <b>Total non-current assets</b>                           |          | <b>12,312</b>       | 13,824                            | 16,591                            |
| <b>Total assets</b>                                       |          | <b>15,262</b>       | 15,949                            | 18,281                            |
| <b>Current liabilities</b>                                |          |                     |                                   |                                   |
| Trade and other payables                                  | 4.4      | 520                 | 618                               | 1,131                             |
| Deferred income   |          | 23                  | 7                                 | 41                                |
| Interest-bearing loans and borrowings                     | 5.1      | 420                 | 152                               | 267                               |
| Current tax liabilities                                   |          | 3                   | 8                                 | 12                                |
| Provisions  | 3.4, 7.1 | 121                 | 125                               | 138                               |
| Other financial liabilities                               | 5.5(f)   | 366                 | 2                                 | 3                                 |
| Liabilities directly associated with assets held for sale | 3.6      | 103                 | 14                                | –                                 |
| <b>Total current liabilities</b>                          |          | <b>1,556</b>        | 926                               | 1,592                             |
| <b>Non-current liabilities</b>                            |          |                     |                                   |                                   |
| Deferred income   |          | 99                  | 158                               | 123                               |
| Interest-bearing loans and borrowings                     | 5.1      | 4,819               | 5,246                             | 6,483                             |
| Deferred tax liabilities                                  | 2.4(d)   | 221                 | 153                               | 486                               |
| Provisions  | 3.4, 7.1 | 1,464               | 1,736                             | 1,747                             |
| Other financial liabilities                               | 5.5(f)   | 23                  | 309                               | 149                               |
| <b>Total non-current liabilities</b>                      |          | <b>6,626</b>        | 7,602                             | 8,988                             |
| <b>Total liabilities</b>                                  |          | <b>8,182</b>        | 8,528                             | 10,580                            |
| <b>Net assets</b>   |          | <b>7,080</b>        | 7,421                             | 7,701                             |
| <b>Equity</b>   |          |                     |                                   |                                   |
| Issued capital  | 5.3      | 8,883               | 8,119                             | 5,762                             |
| Reserves  | 5.4      | (510)               | (699)                             | (335)                             |
| Accumulated (losses)/retained earnings                    | 5.4      | (1,293)             | 1                                 | 2,278                             |
| Equity attributable to owners of Santos Limited           |          | 7,080               | 7,421                             | 7,705                             |
| Non-controlling interests                                 |          | –                   | –                                 | (4)                               |
| <b>Total equity</b>                                       |          | <b>7,080</b>        | 7,421                             | 7,701                             |

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



# Consolidated Statement of Cash Flows

## for the year ended 31 December 2016

|   | Note   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|--------|---------------------|-----------------------------------|
| <b>Cash flows from operating activities</b>   |        |                     |                                   |
| Receipts from customers   |        | 2,708               | 2,711                             |
| Dividends received  |        | 12                  | 13                                |
| Pipeline tariffs and other receipts   |        | 60                  | 25                                |
| Payments to suppliers and employees   |        | (1,600)             | (1,520)                           |
| Exploration and evaluation seismic and studies                                      |        | (68)                | (111)                             |
| Royalty and excise paid   |        | (34)                | (43)                              |
| Borrowing costs paid  |        | (226)               | (164)                             |
| Carbon costs paid   |        | -                   | (16)                              |
| Income taxes paid   |        | (17)                | (50)                              |
| Royalty-related taxation paid   |        | (4)                 | (43)                              |
| Other operating activities  |        | 26                  | 9                                 |
| <b>Net cash provided by operating activities</b>                                    | 4.1(b) | <b>857</b>          | 811                               |
| <b>Cash flows from investing activities</b>   |        |                     |                                   |
| Payments for:   |        |                     |                                   |
| Exploration and evaluation assets   |        | (128)               | (279)                             |
| Oil and gas assets  |        | (517)               | (1,125)                           |
| Other land, buildings, plant and equipment  |        | (4)                 | (17)                              |
| Acquisitions of oil and gas assets  |        | (18)                | (102)                             |
| Proceeds from disposal of non-current assets  | 2.7    | 447                 | 60                                |
| Borrowing costs paid  |        | (20)                | (109)                             |
| Other investing activities  |        | 18                  | (20)                              |
| <b>Net cash used in investing activities</b>  |        | <b>(222)</b>        | (1,592)                           |
| <b>Cash flows from financing activities</b>   |        |                     |                                   |
| Dividends paid  |        | (43)                | (161)                             |
| Drawdown of borrowings  |        | -                   | 636                               |
| Repayment of borrowings   |        | (147)               | (1,770)                           |
| Proceeds from issues of ordinary shares   |        | 733                 | 2,300                             |
| <b>Net cash provided by financing activities</b>                                    |        | <b>543</b>          | 1,005                             |
| <b>Net increase in cash and cash equivalents</b>                                    |        | <b>1,178</b>        | 224                               |
| <b>Cash and cash equivalents at the beginning of the period</b>                     |        | <b>839</b>          | 634                               |
| Effects of exchange rate changes on the balances of cash held in foreign currencies |        | 9                   | (19)                              |
| <b>Cash and cash equivalents at the end of the period</b>                           | 4.1    | <b>2,026</b>        | 839                               |

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

# Consolidated Statement of Changes in Equity

## for the year ended 31 December 2016

|  |  | Equity attributable to owners of Santos Limited |                     |                 |                             |                                      |              |                           |              |
|--|--|---|---------------------|-----------------|-----------------------------|--------------------------------------|--------------|---------------------------|--------------|
|  |  | Issued capital                                  | Translation reserve | Hedging reserve | Accumulated profits reserve | Accumulated losses/Retained earnings | Total equity | Non-controlling interests | Total equity |
| Note   |  | US\$million                                     | US\$million         | US\$million     | US\$million                 | US\$million                          | US\$million  | US\$million               | US\$million  |
| (Restated)   |  |   |                     |                 |                             |                                      |              |                           |              |
|  | Balance at 1 January 2015                                | 5,762   | (320)               | (15)            | –                           | 2,278                                | 7,705        | (4)                       | 7,701        |
|  | Transfer retained profits to accumulated profits reserve | 5.4   | –                   | –               | 121                         | (121)                                | –            | –                         | –            |
| <i>Items of comprehensive income:</i>                        |  |   |                     |                 |                             |                                      |              |                           |              |
|  | Loss for the period                                      | –   | –                   | –               | –                           | (1,953)                              | (1,953)      | –                         | (1,953)      |
|  | Other comprehensive (loss)/income for the period         | –   | (488)               | 3               | –                           | 3                                    | (482)        | –                         | (482)        |
|  | Total comprehensive (loss)/income for the period         | –   | (488)               | 3               | –                           | (1,950)                              | (2,435)      | –                         | (2,435)      |
| <i>Transactions with owners in their capacity as owners:</i> |  |   |                     |                 |                             |                                      |              |                           |              |
|  | Shares issued  | 5.3   | 2,357               | –               | –                           | –                                    | 2,357        | –                         | 2,357        |
|  | Dividends to shareholders                                | 2.6   | –                   | –               | –                           | (219)                                | (219)        | –                         | (219)        |
|  | Share-based payment transactions                         | 7.2   | –                   | –               | –                           | 17                                   | 17           | –                         | 17           |
|  | Non-controlling interest exit from foreign operations    | –   | –                   | –               | –                           | (4)                                  | (4)          | 4                         | –            |
|  | Balance at 31 December 2015                              | 8,119   | (808)               | (12)            | 121                         | 1                                    | 7,421        | –                         | 7,421        |
|  | <b>Balance at 1 January 2016</b>                         | <b>8,119</b>                                    | <b>(808)</b>        | <b>(12)</b>     | <b>121</b>                  | <b>1</b>                             | <b>7,421</b> | <b>–</b>                  | <b>7,421</b> |
|  | Transfer retained profits to accumulated profits reserve | 5.4   | –                   | –               | 258                         | (258)                                | –            | –                         | –            |
| <i>Items of comprehensive income:</i>                        |  |   |                     |                 |                             |                                      |              |                           |              |
|  | Loss for the period                                      | –   | –                   | –               | –                           | (1,047)                              | (1,047)      | –                         | (1,047)      |
|  | Other comprehensive (loss)/income for the period         | –   | (22)                | 19              | –                           | 1                                    | (2)          | –                         | (2)          |
|  | Total comprehensive (loss)/income for the period         | –   | (22)                | 19              | –                           | (1,046)                              | (1,049)      | –                         | (1,049)      |
| <i>Transactions with owners in their capacity as owners:</i> |  |   |                     |                 |                             |                                      |              |                           |              |
|  | Shares issued  | 5.3   | 764                 | –               | –                           | –                                    | 764          | –                         | 764          |
|  | Dividends to shareholders                                | 2.6   | –                   | –               | (66)                        | –                                    | (66)         | –                         | (66)         |
|  | Share-based payment transactions                         | 7.2   | –                   | –               | –                           | 10                                   | 10           | –                         | 10           |
|  | <b>Balance at 31 December 2016</b>                       | <b>8,883</b>                                    | <b>(830)</b>        | <b>7</b>        | <b>313</b>                  | <b>(1,293)</b>                       | <b>7,080</b> | <b>–</b>                  | <b>7,080</b> |

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

# Notes to the Consolidated Financial Statements

## for the year ended 31 December 2016

### STRUCTURE OF THE FINANCIAL REPORT

The notes are organised into key sections to provide an enhanced understanding of the Group's performance that is aligned with management's view of the business, as shown below.

Significant and other accounting policies that summarise the measurement bases and that are relevant to an understanding of the financial statements are provided throughout the notes to the financial statements.

| <b>SECTION 1</b>   |             | <b>SECTION 5</b>                                 |             |
|--|-------------|--|-------------|
| <b>BASIS OF PREPARATION</b>  | <b>PAGE</b> | <b>FUNDING AND RISK MANAGEMENT</b>               | <b>PAGE</b> |
| 1.1 Statement of compliance  | 58          | 5.1 Interest-bearing loans and borrowings        | 85          |
| 1.2 Key events in the current period                                     | 58          | 5.2 Net finance costs                            | 88          |
| 1.3 Significant accounting judgements, estimates and assumptions         | 58          | 5.3 Issued capital                               | 89          |
| 1.4 Foreign currency   | 59          | 5.4 Reserves and retained earnings               | 89          |
|  |             | 5.5 Financial risk management                    | 90          |
| <b>SECTION 2</b>   |             | <b>SECTION 6</b>                                 |             |
| <b>FINANCIAL PERFORMANCE</b>   | <b>PAGE</b> | <b>GROUP STRUCTURE</b>                           | <b>PAGE</b> |
| 2.1 Segment information  | 60          | 6.1 Consolidated entities                        | 95          |
| 2.2 Revenue  | 63          | 6.2 Acquisitions and disposals of subsidiaries   | 97          |
| 2.3 Expenses   | 64          | 6.3 Joint arrangements                           | 98          |
| 2.4 Taxation   | 65          | 6.4 Parent entity disclosures                    | 101         |
| 2.5 Earnings per share   | 69          | 6.5 Deed of Cross Guarantee                      | 102         |
| 2.6 Dividends  | 70          |  |             |
| 2.7 Other income   | 71          | <b>SECTION 7</b>                                 | <b>PAGE</b> |
| <b>SECTION 3</b>   |             | <b>PEOPLE</b>                                    |             |
| <b>CAPITAL EXPENDITURE, OPERATING ASSETS AND RESTORATION OBLIGATIONS</b> | <b>PAGE</b> | 7.1 Employee benefits                            | 104         |
| 3.1 Exploration and evaluation assets                                    | 72          | 7.2 Share-based payment plans                    | 105         |
| 3.2 Oil and gas assets   | 73          | 7.3 Key management personnel disclosures         | 110         |
| 3.3 Impairment of non-current assets                                     | 76          | <b>SECTION 8</b>                                 | <b>PAGE</b> |
| 3.4 Restoration obligations  | 80          | <b>OTHER</b>                                     |             |
| 3.5 Commitments for expenditure  | 81          | 8.1 Contingent liabilities                       | 111         |
| 3.6 Assets held for sale   | 82          | 8.2 Events after the end of the reporting period | 111         |
| <b>SECTION 4</b>   |             | 8.3 Commitment on removal of shareholder cap     | 111         |
| <b>WORKING CAPITAL MANAGEMENT</b>  | <b>PAGE</b> | 8.4 Remuneration of auditors                     | 112         |
| 4.1 Cash and cash equivalents  | 83          | 8.5 Accounting policies                          | 112         |
| 4.2 Trade and other receivables  | 84          |  |             |
| 4.3 Inventories  | 84          |  |             |
| 4.4 Trade and other payables   | 84          |  |             |

# Notes to the Consolidated Financial Statements

## 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 2016 was authorised for issue in accordance with a resolution of the Directors on 16 February 2017.

The consolidated financial report of the Company for the year ended 31 December 2016 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*, 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 2016;
  - 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 available-for-sale financial assets, which are measured at fair value; and
  - rounded to the nearest million dollars, unless otherwise stated, in accordance with ASIC Instrument 2016/191.
- 

### 1.2 KEY EVENTS IN THE CURRENT PERIOD

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

- restructure of the business completed with new operating model established, including new Executive Committee team (“Excom”);
  - both record production of 61.6 mmboe (2015: 57.7 mmboe), and sales of 84.1 mmboe (2015: 64.3 mmboe) in 2016;
  - in May 2016 GLNG Train 2 commenced production;
  - sale of non-core assets resulting in \$447 million in proceeds with a gain on disposal of \$25 million; and
  - completion of an institutional placement in December 2016 which raised \$751 million (A\$1,040 million).
- 

### 1.3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

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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

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

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## 1.4 FOREIGN CURRENCY

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### Functional and presentation currency

The Directors have elected to change the Group's presentation currency from Australian dollars ("A\$") to United States (US) dollars effective from 1 January 2016. The change in presentation currency is a voluntary change which is accounted for retrospectively. All other accounting policies are consistent with those adopted in the annual financial report for the year ended 31 December 2015. The financial report has been restated to US dollars using the procedures outlined below:

1. Income Statement and Statement of Cash Flows have been translated into US dollars using average foreign currency rates prevailing for the relevant period.
2. Assets and liabilities in the Statement of Financial Position have been translated into US dollars at the closing foreign currency rates on the relevant balance sheet dates.
3. The equity section of the Statement of Financial Position, including foreign currency translation reserve, retained earnings, share capital and the other reserves, have been translated into US dollars using historical rates.
4. Earnings per share and dividend disclosures have also been restated to US dollars to reflect the change in presentation currency.

The functional currency of the Parent is Australian dollars, whilst the presentation currency of the Group is now in United States dollars. Some subsidiaries have a functional currency other than Australian dollars which is translated to the presentation currency.

### 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.

The year-end exchange rate used was A\$/US\$ 1:0.7221 (2015: 1:0.7274, 2014: 1:0.8181).

### 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. The Group's consolidated Australian dollar financial statements are then translated to United States dollars (presentation currency) in line with the procedures outlined above.

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(b) 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

---

Commencing in the second half of 2016, the Group identified its operating segments to be the five key assets/operating areas of: Cooper Basin; Gladstone LNG (“GLNG”); 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. Comparative disclosures have been restated to a consistent basis.

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.

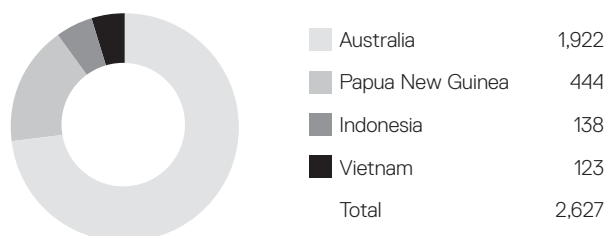
## 2.1 SEGMENT INFORMATION (CONTINUED)

| US\$million                              | Cooper<br>Basin<br>2016 | GLNG<br>2016   | PNG<br>2016 | Northern<br>Australia<br>2016 | WA<br>Gas<br>2016 | Other<br>2016     | Corporate,<br>exploration,<br>eliminations<br>2016 | Total<br>2016  |
|--|-------------------------|----------------|-------------|-------------------------------|-------------------|-------------------|--|----------------|
| <b>Revenue</b>                           |                         |                |             |                               |                   |                   |  |                |
| Sales to external customers              | 716                     | 521            | 439         | 145                           | 184               | 405               | 184  | 2,594          |
| Inter-segment sales <sup>1</sup>         | 33                      | 13             | –           | –                             | –                 | 4                 | (50)   | –              |
| Other revenue from external customers    | 19                      | 6              | 5           | –                             | –                 | 2                 | 1  | 33             |
| <b>Total segment revenue</b>             | <b>768</b>              | <b>540</b>     | <b>444</b>  | <b>145</b>                    | <b>184</b>        | <b>411</b>        | <b>135</b>   | <b>2,627</b>   |
| <b>Costs</b>                             |                         |                |             |                               |                   |                   |  |                |
| Production costs                         | (162)                   | (61)           | (56)        | (73)                          | (45)              | (164)             | 41   | (520)          |
| Other operating costs                    | (77)                    | (74)           | (38)        | –                             | (5)               | (16)              | (116)  | (326)          |
| Third-party product purchases            | (201)                   | (142)          | (2)         | –                             | –                 | (3)               | (196)  | (544)          |
| Inter-segment purchases <sup>1</sup>     | (18)                    | (75)           | –           | –                             | –                 | –                 | 93   | –              |
| <b>Results</b>                           |                         |                |             |                               |                   |                   |  |                |
| <b>EBITDAX</b>                           | <b>265</b>              | <b>183</b>     | <b>350</b>  | <b>86</b>                     | <b>210</b>        | <b>217</b>        | <b>(112)</b>                                       | <b>1,199</b>   |
| Depreciation and depletion               | (179)                   | (192)          | (105)       | (46)                          | (72)              | (115)             | (32)   | (741)          |
| Exploration and evaluation expensed      | –                       | –              | –           | –                             | –                 | –                 | (138)  | (138)          |
| Net impairment (loss)/reversal           | (49)                    | (1,500)        | –           | –                             | –                 | 47                | (59)   | (1,561)        |
| Change in future restoration assumptions | –                       | –              | –           | –                             | –                 | 37                | –  | 37             |
| <b>EBIT</b>                              | <b>37</b>               | <b>(1,509)</b> | <b>245</b>  | <b>40</b>                     | <b>138</b>        | <b>186</b>        | <b>(341)</b>                                       | <b>(1,204)</b> |
| Net finance costs                        |                         |                |             |                               |                   |                   | (281)  | (281)          |
| Loss before tax                          |                         |                |             |                               |                   |                   |  | (1,485)        |
| Income tax benefit                       |                         |                |             |                               |                   |                   | 445  | 445            |
| Royalty-related tax benefit/(expense)    | 2                       | (3)            | –           | (4)                           | (19)              | (7)               | 24   | (7)            |
| <b>Net loss</b>                          |                         |                |             |                               |                   |                   |  | <b>(1,047)</b> |
| <b>Asset additions and acquisitions:</b> |                         |                |             |                               |                   |                   |  |                |
| Exploration and evaluation assets        | 9                       | 1              | –           | 2                             | –                 | 47                | 94   | 153            |
| Oil and gas assets                       | 37                      | 238            | 14          | 36                            | 75                | (30) <sup>2</sup> | –  | 370            |
|  | <b>46</b>               | <b>239</b>     | <b>14</b>   | <b>38</b>                     | <b>75</b>         | <b>17</b>         | <b>94</b>  | <b>523</b>     |

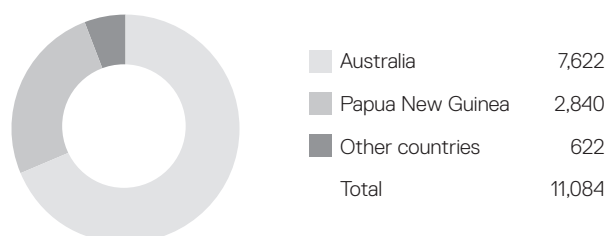
1. Inter-segment pricing is determined on an arm's length basis. Inter-segment sales and purchases are eliminated on consolidation.

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**



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



# Notes to the Consolidated Financial Statements

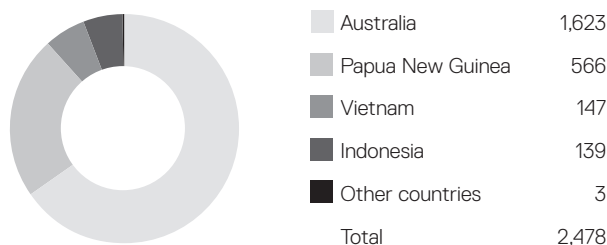
## Section 2: Financial Performance

### 2.1 SEGMENT INFORMATION (CONTINUED)

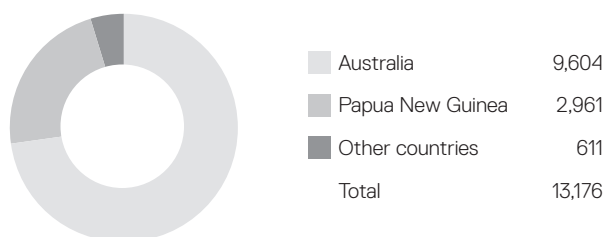
| US\$million (Restated)                   | Cooper<br>Basin<br>2015 | GLNG<br>2015 | PNG<br>2015 | Northern<br>Australia<br>2015 | WA<br>Gas<br>2015 | Other<br>2015 | Corporate,<br>exploration,<br>eliminations<br>2015 | Total<br>2015  |
|--|-------------------------|--------------|-------------|-------------------------------|-------------------|---------------|--|----------------|
| <b>Revenue</b>                           |                         |              |             |                               |                   |               |  |                |
| Sales to external customers              | 829                     | 97           | 559         | 215                           | 227               | 452           | 63   | 2,442          |
| Inter-segment sales <sup>1</sup>         | 9                       | 22           | –           | –                             | –                 | 14            | (45)   | –              |
| Other revenue from external customers    | 13                      | 4            | 7           | –                             | –                 | 7             | 5  | 36             |
| <b>Total segment revenue</b>             | <b>851</b>              | <b>123</b>   | <b>566</b>  | <b>215</b>                    | <b>227</b>        | <b>473</b>    | <b>23</b>  | <b>2,478</b>   |
| <b>Costs</b>                             |                         |              |             |                               |                   |               |  |                |
| Production costs                         | (197)                   | (36)         | (61)        | (81)                          | (47)              | (215)         | 40   | (597)          |
| Other operating costs                    | (83)                    | (25)         | (47)        | (1)                           | (4)               | (19)          | (21)   | (200)          |
| Third-party product purchases            | (230)                   | (46)         | (2)         | –                             | –                 | (13)          | (67)   | (358)          |
| Inter-segment purchases <sup>1</sup>     | (26)                    | (13)         | –           | –                             | –                 | –             | 39   | –              |
| <b>Results</b>                           |                         |              |             |                               |                   |               |  |                |
| <b>EBITDAX</b>                           | <b>293</b>              | <b>31</b>    | <b>443</b>  | <b>143</b>                    | <b>162</b>        | <b>217</b>    | <b>165</b>   | <b>1,454</b>   |
| Depreciation and depletion               | (269)                   | (82)         | (103)       | (47)                          | (74)              | (185)         | (33)   | (793)          |
| Exploration and evaluation expensed      | –                       | –            | –           | –                             | –                 | –             | (188)  | (188)          |
| Net impairment loss                      | (1,541)                 | (454)        | –           | –                             | –                 | (373)         | (486)  | (2,854)        |
| <b>EBIT</b>                              | <b>(1,517)</b>          | <b>(505)</b> | <b>340</b>  | <b>96</b>                     | <b>88</b>         | <b>(341)</b>  | <b>(542)</b>                                       | <b>(2,381)</b> |
| Net finance costs                        |                         |              |             |                               |                   |               | (217)  | (217)          |
| Loss before tax                          |                         |              |             |                               |                   |               |  | (2,598)        |
| Income tax benefit                       |                         |              |             |                               |                   |               | 621  | 621            |
| Royalty-related tax benefit              | 20                      | 7            | –           | (14)                          | (26)              | 14            | 23   | 24             |
| <b>Net loss</b>                          |                         |              |             |                               |                   |               |  | <b>(1,953)</b> |
| <b>Asset additions and acquisitions:</b> |                         |              |             |                               |                   |               |  |                |
| Exploration and evaluation assets        | 21                      | 11           | 24          | 6                             | 1                 | 43            | 200  | 306            |
| Oil and gas assets                       | 503                     | 441          | 96          | 22                            | 38                | 121           | –  | 1,221          |
|  | <b>524</b>              | <b>452</b>   | <b>120</b>  | <b>28</b>                     | <b>39</b>         | <b>164</b>    | <b>200</b>   | <b>1,527</b>   |

1. Inter-segment pricing is determined on an arm's length basis. Inter-segment sales and purchases are eliminated on consolidation.

**2015 Revenue from external customers  
by geographical location  
US\$million**



**2015 Non-current assets by geographical location  
(excluding financial and deferred tax assets)  
US\$million**





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## 2.2 REVENUE

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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 \$324 million (2015: \$464 million from one customer), 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                          | 2016         | (Restated)<br>2015 |
|--|--------------|--------------------|
|  | US\$million  | US\$million        |
| <b>Product sales:</b>                  |              |                    |
| Gas, ethane and liquefied natural gas  | <b>1,784</b> | 1,442              |
| Crude oil                              | <b>575</b>   | 740                |
| Condensate and naphtha                 | <b>183</b>   | 183                |
| Liquefied petroleum gas                | <b>52</b>    | 77                 |
| <b>Total product sales<sup>1</sup></b> | <b>2,594</b> | 2,442              |

1. Total product sales include third-party product sales of \$643 million (2015: \$440 million).

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# Notes to the Consolidated Financial Statements

## Section 2: Financial Performance

### 2.3 EXPENSES

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| <b>Cost of sales:</b>   |                     |                                   |
| Production costs:   |                     |                                   |
| Production expenses   | 469                 | 524                               |
| Production facilities operating leases  | 51                  | 73                                |
| Total production costs  | 520                 | 597                               |
| Other operating costs:  |                     |                                   |
| LNG plant costs   | 58                  | 29                                |
| Pipeline tariffs, processing tolls and other  | 174                 | 106                               |
| Onerous pipeline contract   | 29                  | –                                 |
| Royalty and excise  | 43                  | 42                                |
| Shipping costs  | 22                  | 23                                |
| Total other operating costs   | 326                 | 200                               |
| Total cash cost of production   | 846                 | 797                               |
| Depreciation of plant, equipment and buildings  | 463                 | 470                               |
| Depletion of subsurface assets  | 273                 | 321                               |
| Total depreciation and depletion  | 736                 | 791                               |
| Third-party product purchases   | 544                 | 358                               |
| Decrease/(increase) in product stock  | 27                  | (63)                              |
| <b>Total cost of sales</b>  | <b>2,153</b>        | <b>1,883</b>                      |
| <b>Other expenses:</b>  |                     |                                   |
| Selling   | 19                  | 20                                |
| Corporate   | 88                  | 128                               |
| Depreciation  | 5                   | 2                                 |
| Foreign exchange gains  | (34)                | (196)                             |
| Losses from change in fair value of derivative financial instruments designated<br>as fair value through profit or loss | 14                  | 5                                 |
| Fair value hedges, (gains)/losses:  |                     |                                   |
| On the hedging instrument   | 59                  | 49                                |
| On the hedged item attributable to the hedged risk  | (19)                | (63)                              |
| Exploration and evaluation expensed   | 138                 | 188                               |
| Other   | 14                  | 8                                 |
| <b>Total other expenses</b>   | <b>284</b>          | <b>141</b>                        |

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## 2.4 TAXATION

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### 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.

# Notes to the Consolidated Financial Statements

## Section 2: Financial Performance

### 2.4 TAXATION (CONTINUED)

#### Royalty-related tax

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

Current income tax and royalty-related tax recognised in the income statement for the group is as follows:

|  | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|---------------------|-----------------------------------|
| <b>(a) Income tax expense/(benefit)</b>                                      |                     |                                   |
| <i>Current tax expense/(benefit)</i>   |                     |                                   |
| Current year   | 86                  | 11                                |
| Adjustments for prior years  | (12)                | 24                                |
|  | <b>74</b>           | <b>35</b>                         |
| <i>Deferred tax benefit</i>  |                     |                                   |
| Origination and reversal of temporary differences                            | (510)               | (589)                             |
| Adjustments for prior years  | (9)                 | (67)                              |
|  | <b>(519)</b>        | <b>(656)</b>                      |
| <b>Total income tax benefit</b>  | <b>(445)</b>        | <b>(621)</b>                      |
| <b>(b) Royalty-related tax expense</b>                                       |                     |                                   |
| <i>Current tax expense</i>   |                     |                                   |
| Current year   | 14                  | 25                                |
|  | <b>14</b>           | <b>25</b>                         |
| <i>Deferred tax benefit</i>  |                     |                                   |
| Origination and reversal of temporary differences                            | (7)                 | (49)                              |
|  | <b>(7)</b>          | <b>(49)</b>                       |
| <b>Total royalty-related tax expense/(benefit)</b>                           | <b>7</b>            | <b>(24)</b>                       |
| <b>(c) Numerical reconciliation between pre-tax net loss and tax benefit</b> |                     |                                   |
| Loss before tax  | (1,485)             | (2,598)                           |
| Prima facie income tax benefit at 30% (2015: 30%)                            | (446)               | (779)                             |
| (Decrease)/increase in income tax (benefit)/expense due to:                  |                     |                                   |
| Foreign losses not recognised  | (2)                 | 29                                |
| Non-deductible expenses  | 3                   | 9                                 |
| Exchange and other translation variations                                    | 14                  | 111                               |
| Tax adjustments relating to prior years                                      | (2)                 | 5                                 |
| Other  | (12)                | 4                                 |
| Income tax benefit   | (445)               | (621)                             |
| Royalty-related tax expense/(benefit)  | 7                   | (24)                              |
| <b>Total tax benefit</b>   | <b>(438)</b>        | <b>(645)</b>                      |

## 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.

| Recognised deferred tax assets and liabilities | Assets              |                                   | Liabilities         |                                   | Net                 |                                   |
|--|---------------------|-----------------------------------|---------------------|-----------------------------------|---------------------|-----------------------------------|
|  | 2016<br>US\$million | (Restated)<br>2015<br>US\$million | 2016<br>US\$million | (Restated)<br>2015<br>US\$million | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
| Exploration and evaluation assets              | 28                  | –                                 | (66)                | (55)                              | (38)                | (55)                              |
| Oil and gas assets                             | 15                  | –                                 | –                   | (246)                             | 15                  | (246)                             |
| Available-for-sale financial assets            | –                   | –                                 | –                   | (20)                              | –                   | (20)                              |
| Other assets                                   | 10                  | –                                 | (46)                | (42)                              | (36)                | (42)                              |
| Derivative financial instruments               | 85                  | 58                                | –                   | –                                 | 85                  | 58                                |
| Interest-bearing loans and borrowings          | 162                 | 174                               | –                   | –                                 | 162                 | 174                               |
| Provisions                                     | 82                  | 44                                | –                   | –                                 | 82                  | 44                                |
| Royalty-related tax                            | –                   | –                                 | (60)                | (54)                              | (60)                | (54)                              |
| Other items                                    | –                   | 14                                | (37)                | (12)                              | (37)                | 2                                 |
| Tax value of carry-forward losses recognised   | 660                 | 452                               | –                   | –                                 | 660                 | 452                               |
| Tax assets/(liabilities)                       | 1,042               | 742                               | (209)               | (429)                             | 833                 | 313                               |
| Set-off of tax                                 | 12                  | (276)                             | (12)                | 276                               | –                   | –                                 |
| <b>Net tax assets/(liabilities)</b>            | <b>1,054</b>        | <b>466</b>                        | <b>(221)</b>        | <b>(153)</b>                      | <b>833</b>          | <b>313</b>                        |

# Notes to the Consolidated Financial Statements

## Section 2: Financial Performance

### 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 \$64 million (2015: \$65 million) will expire between 2021 and 2028. The remaining deductible temporary differences and tax losses do not expire under current tax legislation.

| <b>Unrecognised deferred tax assets</b>   | <b>2016</b>        | (Restated)          |
|---|--------------------|---------------------|
|   | <b>US\$million</b> | 2015<br>US\$million |
| Deferred tax assets have not been recognised in respect of the following items:         |                    |                     |
| Temporary differences in relation to investments in subsidiaries                        | <b>5,705</b>       | 5,527               |
| Deductible temporary differences relating to royalty-related tax<br>(net of income tax) | <b>5,284</b>       | 4,430               |
| Other deductible temporary differences  | <b>128</b>         | 220                 |
| Tax losses  | <b>373</b>         | 366                 |
|   | <b>11,490</b>      | 10,543              |

## 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:

|  | <b>2016</b><br><b>US\$million</b> | (Restated)<br>2015<br>US\$million |
|--|-----------------------------------|-----------------------------------|
| Earnings used in the calculation of basic and diluted earnings per share | <b>(1,047)</b>                    | (1,953)                           |

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:

|   | <b>2016</b><br><b>Number of shares</b> | 2015<br>Number of shares |
|---|--|--------------------------|
| Basic earnings per share                        | <b>1,797,896,876</b>                   | 1,151,977,771            |
| Dilutive potential ordinary shares <sup>1</sup> | -                                      | -                        |
| Diluted earnings per share                      | <b>1,797,896,876</b>                   | 1,151,977,771            |

| <b>Earnings per share attributable to the equity holders of Santos Limited</b> | <b>2016</b><br><b>¢</b> | 2015<br>¢ |
|--|-------------------------|-----------|
| Basic earnings per share   | <b>(58.2)</b>           | (169.5)   |
| Diluted earnings per share   | <b>(58.2)</b>           | (169.5)   |

1. Due to a net loss after tax in 2016 and 2015, 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<br>per share<br>US¢ | Total<br>US\$million |
|--|------------------------------|----------------------|
| <b>2016</b>  |                              |                      |
| Final 2015 ordinary – paid 30 Mar 2016 (A\$0.05)   | 4                            | 66                   |
|  | <b>4</b>                     | <b>66</b>            |
| 2015 (Restated)                                    |                              |                      |
| Interim 2015 ordinary – paid 30 Sep 2015 (A\$0.15) | 11                           | 109                  |
| Final 2014 ordinary – paid 25 Mar 2015 (A\$0.15)   | 11                           | 110                  |
|  | 22                           | 219                  |

| Dividends declared in respect of the year          | Dividend<br>per share<br>US¢ | Total<br>US\$million |
|--|------------------------------|----------------------|
| <b>2016</b>  |                              |                      |
| No dividends were declared in respect of 2016.     |                              |                      |
| 2015 (Restated)                                    |                              |                      |
| Final 2015 ordinary – paid 30 Mar 2016 (A\$0.05)   | 4                            | 66                   |
| Interim 2015 ordinary – paid 30 Sep 2015 (A\$0.15) | 11                           | 109                  |
|  | 15                           | 175                  |

All dividends declared were franked dividends and were franked at the tax rate of 30%.

| Dividend franking account  | 2016<br>US\$million | (Restated)<br>2015<br>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 | 363                 | 429                               |



## 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 | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|------|---------------------|-----------------------------------|
| <b>Other income</b>   |      |                     |                                   |
| Liquidated damages of gas sales agreement   |      | 69                  | –                                 |
| Change in future restoration assumptions  | 3.4  | 37                  | –                                 |
| Gain on sale of non-current assets  |      | 25                  | 1                                 |
| Insurance proceeds  |      | 10                  | –                                 |
| Other   |      | 16                  | 8                                 |
| <b>Total other income</b>   |      | <b>157</b>          | <b>9</b>                          |
| <b>Net gain on sale of non-current assets:</b>  |      |                     |                                   |
| Proceeds on disposals   |      | 447                 | 93                                |
| Book value of oil and gas assets disposed   |      | (162)               | (54)                              |
| Book value of other land, buildings, plant and equipment disposed                     |      | (5)                 | (2)                               |
| Book value of exploration and evaluation assets disposed                              |      | –                   | (28)                              |
| Recoupment of current year exploration and evaluation expenditure                     |      | –                   | (9)                               |
| Book value of working capital disposed  |      | (255)               | 1                                 |
| <b>Total net gain on sale of non-current assets</b>                                   |      | <b>25</b>           | <b>1</b>                          |
| <b>Comprising:</b>  |      |                     |                                   |
| Net (loss)/gain on sale of exploration and evaluation assets                          |      | (2)                 | 3                                 |
| Net gain/(loss) on sale of oil and gas assets   |      | 13                  | (3)                               |
| Net gain on sale of other land, buildings, plant and equipment                        |      | 8                   | 1                                 |
| Net gain on liquidation of controlled entities  |      | 6                   | –                                 |
|   |      | <b>25</b>           | <b>1</b>                          |
| <b>Reconciliation to cash inflows from proceeds on disposal of non-current assets</b> |      |                     |                                   |
| Proceeds after recoupment of current year exploration and evaluation expenditure      |      | 447                 | 84                                |
| Amounts receivable  |      | –                   | (24)                              |
| Amounts received from disposals   |      | 447                 | 60                                |
| <b>Total proceeds on disposal of non-current assets</b>                               |      | <b>447</b>          | <b>60</b>                         |
| <b>Comprising:</b>  |      |                     |                                   |
| Proceeds from disposal of oil and gas assets  |      | 432                 | 32                                |
| Proceeds from disposal of exploration and evaluation assets                           |      | –                   | 28                                |
| Proceeds from disposal of other land, buildings, plant and equipment                  |      | 15                  | –                                 |
|   |      | <b>447</b>          | <b>60</b>                         |

# 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:



Key information to note in this section includes:

- the carrying values of various assets were written down at 31 December 2016; as a result a pre-tax impairment charge of \$1,561 million was recognised in impairment expenses; and
- significant movements in oil and gas assets resulted from the continued construction of the GLNG project, with the completion of various aspects of the project seeing the assets transition from assets in development to producing assets.

### 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.

### 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 written off through the income statement.

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| Cost  | 1,805               | 1,834                             |
| Less impairment                               | (1,310)             | (1,314)                           |
| <b>Balance at 31 December</b>                 | <b>495</b>          | 520                               |
| <b>Reconciliation of movements</b>            |                     |                                   |
| Balance at 1 January                          | 520                 | 905                               |
| Acquisitions                                  | 37                  | 95                                |
| Additions                                     | 116                 | 211                               |
| Transfer to assets held for sale              | (28)                | (27)                              |
| Expensed                                      | (71)                | (88)                              |
| Impairment losses                             | (59)                | (498)                             |
| Transfer to oil and gas assets in development | (1)                 | -                                 |
| Transfer to oil and gas assets in production  | (15)                | (1)                               |
| Exchange differences                          | (4)                 | (77)                              |
| <b>Balance at 31 December</b>                 | <b>495</b>          | 520                               |
| <b>Comprising:</b>                            |                     |                                   |
| Acquisition costs                             | 150                 | 207                               |
| Successful exploration wells                  | 249                 | 233                               |
| Pending determination of success              | 96                  | 80                                |
|   | <b>495</b>          | 520                               |

### 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 Proven plus Probable (“2P”) hydrocarbon reserves reported by the Group are integral to the calculation of depletion and depreciation expense and to assessments of possible 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.

### 3.2 OIL AND GAS ASSETS (CONTINUED)

|  | 2016                           |                                  |                    | 2015 (Restated)                |                                  |                    |
|--|--------------------------------|----------------------------------|--------------------|--------------------------------|----------------------------------|--------------------|
|  | Subsurface assets<br>\$million | Plant and equipment<br>\$million | Total<br>\$million | Subsurface assets<br>\$million | Plant and equipment<br>\$million | Total<br>\$million |
| Cost   | 9,244                          | 15,652                           | 24,896             | 9,659                          | 15,565                           | 25,224             |
| Less accumulated depreciation, depletion and impairment          | (7,467)                        | (7,031)                          | (14,498)           | (7,049)                        | (5,771)                          | (12,820)           |
| <b>Balance at 31 December</b>                                    | <b>1,777</b>                   | <b>8,621</b>                     | <b>10,398</b>      | <b>2,610</b>                   | <b>9,794</b>                     | <b>12,404</b>      |
| <b>Reconciliation of movements</b>                               |                                |                                  |                    |                                |                                  |                    |
| <b>Assets in development</b>                                     |                                |                                  |                    |                                |                                  |                    |
| Balance at 1 January   | 96                             | 941                              | 1,037              | 346                            | 4,555                            | 4,901              |
| Additions <sup>1</sup>   | 11                             | 50                               | 61                 | 18                             | 276                              | 294                |
| Capitalised depreciation   | -                              | -                                | -                  | -                              | 24                               | 24                 |
| Transfer from exploration and evaluation assets                  | 1                              | -                                | 1                  | -                              | -                                | -                  |
| Disposals  | (2)                            | -                                | (2)                | -                              | -                                | -                  |
| Transfer to oil and gas assets in production                     | (35)                           | (972)                            | (1,007)            | (179)                          | (3,785)                          | (3,964)            |
| Transfer to oil and gas assets held for sale net of impairment   | -                              | -                                | -                  | (69)                           | (100)                            | (169)              |
| Net impairment losses on assets transferred to held for sale     | -                              | -                                | -                  | (9)                            | (14)                             | (23)               |
| Exchange differences   | -                              | -                                | -                  | (11)                           | (15)                             | (26)               |
| <b>Balance at 31 December</b>                                    | <b>71</b>                      | <b>19</b>                        | <b>90</b>          | <b>96</b>                      | <b>941</b>                       | <b>1,037</b>       |
| <b>Producing assets</b>  |                                |                                  |                    |                                |                                  |                    |
| Balance at 1 January   | 2,514                          | 8,853                            | 11,367             | 3,446                          | 6,724                            | 10,170             |
| Acquisitions of oil and gas assets                               | -                              | -                                | -                  | 1                              | -                                | 1                  |
| Additions <sup>1</sup>   | (14)                           | 323                              | 309                | 387                            | 539                              | 926                |
| Transfer from exploration and evaluation assets                  | 15                             | -                                | 15                 | 1                              | -                                | 1                  |
| Transfer from oil and gas assets in development                  | 35                             | 972                              | 1,007              | 179                            | 3,785                            | 3,964              |
| Disposals  | (10)                           | (38)                             | (48)               | (51)                           | (23)                             | (74)               |
| Depreciation and depletion                                       | (272)                          | (435)                            | (707)              | (321)                          | (458)                            | (779)              |
| Net impairment losses  | (521)                          | (968)                            | (1,489)            | (926)                          | (1,403)                          | (2,329)            |
| Transfer of assets held for sale                                 | (29)                           | (97)                             | (126)              | -                              | -                                | -                  |
| Net impairment losses on assets transferred to held for sale     | -                              | (4)                              | (4)                | -                              | -                                | -                  |
| Exchange differences   | (12)                           | (4)                              | (16)               | (202)                          | (311)                            | (513)              |
| <b>Balance at 31 December</b>                                    | <b>1,706</b>                   | <b>8,602</b>                     | <b>10,308</b>      | <b>2,514</b>                   | <b>8,853</b>                     | <b>11,367</b>      |
| <b>Total oil and gas assets</b>                                  | <b>1,777</b>                   | <b>8,621</b>                     | <b>10,398</b>      | <b>2,610</b>                   | <b>9,794</b>                     | <b>12,404</b>      |
| <b>Comprising:</b>   |                                |                                  |                    |                                |                                  |                    |
| Exploration and evaluation expenditure pending commercialisation | 202                            | 21                               | 223                | 206                            | -                                | 206                |
| Other capitalised expenditure                                    | 1,575                          | 8,600                            | 10,175             | 2,404                          | 9,794                            | 12,198             |
|  | <b>1,777</b>                   | <b>8,621</b>                     | <b>10,398</b>      | <b>2,610</b>                   | <b>9,794</b>                     | <b>12,404</b>      |

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

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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 unit on a pro-rata basis.

Individual assets within a CGU may become impaired if their ongoing use changes, or that 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 cash-generating unit exceeds its recoverable amount.

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

#### Recoverable amount

The recoverable amount of an asset 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 2P 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 2P hydrocarbon reserves in addition to other relevant factors such as value attributable to additional resource and exploration opportunities beyond 2P 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:

| 2017  | 2018  | 2019 <sup>1</sup> | 2020 <sup>1</sup> | 2021 <sup>1</sup> | 2022 <sup>1</sup> |
|-------|-------|-------------------|-------------------|-------------------|-------------------|
| 60.00 | 70.00 | 80.77             | 82.79             | 84.86             | 86.98             |

1. Based on US\$75/bbl (2016 real) from 2019 escalated at 2.5% p.a., consistent with June 2016 assumptions.

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\$/US\$ of 0.70 in 2017, and A\$/US\$ of 0.75 in all subsequent years.

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 9.7% and 18.9%.

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                     | Note | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|------|---------------------|-----------------------------------|
| <b>Current assets</b>                  |      |                     |                                   |
| Assets held for sale                   | 3.6  | 4                   | 23                                |
| Other assets                           |      | –                   | 4                                 |
| Total impairment of current assets     |      | <b>4</b>            | <b>27</b>                         |
| <b>Non-current assets</b>              |      |                     |                                   |
| Exploration and evaluation assets      |      | <b>59</b>           | 498                               |
| Oil and gas assets                     |      | <b>1,489</b>        | 2,329                             |
| Land and buildings                     |      | <b>9</b>            | –                                 |
| Total impairment of non-current assets |      | <b>1,557</b>        | <b>2,827</b>                      |
| <b>Total impairment</b>                |      | <b>1,561</b>        | <b>2,854</b>                      |

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

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

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 charges noted above for exploration and evaluation assets, primarily result from the lower oil price environment and, in some cases, a consequential reduction or delay in future capital expenditure that diminishes or removes the path to commercialisation. The impairment reversal for Vietnam arose due to a reduction in future operating costs.

#### GLNG

Sustained low oil prices continue to constrain capital expenditure and impact GLNG. During 2016 there has been a slower ramp-up of GLNG equity gas production and an increase in the price of third-party gas and this has led to a change in upstream gas supply and third-party gas pricing assumptions. As a consequence, the GLNG asset carrying value has been written down and an impairment charge of \$1,500 million before tax (\$1,050 million after tax) has been recognised.



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

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 impairment in 2016 for the GLNG CGU:

| Sensitivity | Discount rate<br>increase 0.50%<br>US\$million | Oil price<br>decrease<br>US\$5/bbl<br>all years<br>US\$million |
|-------------|--|--|
| GLNG        | 189  | 439  |

As identified above, the impact of changes in key assumptions such as 2P 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 recognised in the year ended 31 December 2015 were:

| 2015 (Restated)  | Segment      | Subsurface<br>assets<br>US\$million | Plant and<br>equipment<br>US\$million | Total<br>US\$million | Recoverable<br>amount <sup>1</sup><br>US\$million |
|--|--------------|-------------------------------------|---------------------------------------|----------------------|---|
| <b>Exploration and evaluation assets:</b>  |              |                                     |                                       |                      |   |
| Gunnedah Basin   | Exploration  | 409                                 | 18                                    | 427                  | nil <sup>2</sup>                                  |
| Cooper – unconventional resources  | Cooper Basin | 17                                  | –                                     | 17                   | nil <sup>2</sup>                                  |
| Papua New Guinea   | Exploration  | 38                                  | –                                     | 38                   | nil <sup>2</sup>                                  |
| Malaysia   | Exploration  | 16                                  | –                                     | 16                   | nil <sup>2</sup>                                  |
| Total impairment of exploration and evaluation assets                            |              | 480                                 | 18                                    | 498                  |   |
| <b>Oil and gas assets – producing:</b>   |              |                                     |                                       |                      |   |
| Cooper Basin   | Cooper Basin | 570                                 | 954                                   | 1,524                | 982   |
| Mereenie   | Other        | –                                   | 9                                     | 9                    | 45  |
| Patricia Baleen  | Other        | 7                                   | 5                                     | 12                   | 19  |
| Barrow   | Other        | 70                                  | 111                                   | 181                  | 47  |
| WA&NT oil assets   | Other        | 55                                  | 12                                    | 67                   | 18  |
| Vietnam (Chim Sáo/Dua)   | Other        | 46                                  | 31                                    | 77                   | 118   |
| SE Gobe  | Corporate    | 1                                   | 4                                     | 5                    | nil   |
| GLNG   | GLNG         | 163                                 | 248                                   | 411                  | 6,847   |
| Denison  | GLNG         | 14                                  | 29                                    | 43                   | nil   |
| Total impairment of oil and gas assets   |              | 926                                 | 1,403                                 | 2,329                |   |
| <b>Total impairment of exploration<br/>and evaluation and oil and gas assets</b> |              | <b>1,406</b>                        | <b>1,421</b>                          | <b>2,827</b>         |   |

1. Recoverable amounts represent the carrying values of assets before deducting the carrying value of restoration liabilities.

2. Impairment of exploration and evaluation assets relates to certain individual licences/areas of interest that have been impaired to nil.

# Notes to the Consolidated Financial Statements

## Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

### 3.4 RESTORATION OBLIGATIONS

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:

|                       | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|-----------------------|---------------------|-----------------------------------|
| Current provision     | 69                  | 52                                |
| Non-current provision | 1,399               | 1,726                             |
|                       | <b>1,468</b>        | 1,778                             |

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

|   | Total restoration<br>US\$million |
|---|----------------------------------|
| Balance at 1 January 2016   | 1,778                            |
| Impact of changes in future restoration assumptions – restoration asset | (18)                             |
| Impact of changes in future restoration assumptions – other income      | (37)                             |
| Provisions used during the year   | (25)                             |
| Unwind of discount  | 41                               |
| Disposal of provision   | (56)                             |
| Change in discount rate   | (111)                            |
| Transferred to liabilities held for sale                                | (99)                             |
| Exchange differences  | (5)                              |
| <b>Balance at 31 December 2016</b>                                      | <b>1,468</b>                     |

Payments made into escrow accounts relating to future restoration obligations included in the table above of \$62 million (2015: \$52 million) are included within other non-current financial assets (note 5.5(f)).

#### Other provisions

In addition to the provision for restoration shown above and employee provisions in note 7.1, other items for which a provision has been recorded are other current provisions \$7 million (2015: \$13 million), and other non-current provisions \$52 million (2015: nil).

### 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 buildings including 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 2016, the Group recognised \$51 million (2015: \$73 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:

| Commitments                                       | Capital             |                                   | Minimum exploration |                                   | Operating lease     |                                   |
|---|---------------------|-----------------------------------|---------------------|-----------------------------------|---------------------|-----------------------------------|
|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million | 2016<br>US\$million | (Restated)<br>2015<br>US\$million | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
| Not later than one year                           | 161                 | 277                               | 80                  | 170                               | 83                  | 112                               |
| Later than one year but not later than five years | 14                  | 36                                | 292                 | 340                               | 129                 | 216                               |
| Later than five years                             | –                   | –                                 | –                   | 1                                 | 93                  | 147                               |
|   | 175                 | 313                               | 372                 | 511                               | 305                 | 475                               |

# Notes to the Consolidated Financial Statements

## Section 3: Capital Expenditure, Operating Assets and Restoration Obligations

### 3.6 ASSETS HELD FOR SALE

Non-current assets are classified as held for sale and measured at the lower of their carrying amount or fair value less costs of disposal if their carrying amount will be recovered principally through a sale transaction. Assets are not depreciated or amortised. For an asset to be classified as held for sale, it must be available for immediate sale in its present condition and its sale must be highly probable.

An impairment loss is recognised for any initial or subsequent write-down of the asset (or disposal group) to fair value less cost of disposal. A gain is recognised for any subsequent increases in fair value less cost of disposal of an asset (or disposal group) but not in excess of any cumulative impairment loss previously recognised. A gain or loss not previously recognised by the date of the sale of the non-current asset (or disposal group) is recognised at the date of derecognition.

Following agreement to sell the Group's interests in its offshore Victoria assets, and interest in Mereenie, the associated assets and liabilities have been classified as held for sale at 31 December 2016. The sale agreements remained subject to outstanding conditions at 31 December 2016 and will be accounted for upon completion or waiver of each significant condition.

The following amounts are included within the financial statements in relation to assets classified as held for sale:

| <b>Assets and liabilities classified as held for sale</b> | <b>2016<br/>US\$million</b> |
|---|-----------------------------|
| Trade and other receivables                               | 24                          |
| Inventories   | 2                           |
| Exploration and evaluation assets                         | 28                          |
| Oil and gas assets  | 126                         |
| <b>Assets classified as held for sale</b>                 | <b>180</b>                  |
| Trade and other payables                                  | 1                           |
| Other liabilities and deferred income                     | 3                           |
| Restoration provisions                                    | 99                          |
| <b>Liabilities classified as held for sale</b>            | <b>103</b>                  |
| <b>Net assets</b>   | <b>77</b>                   |

A net impairment loss of \$4 million attributed to the write-down of assets to fair value, in the Other segment, has been recorded.

# 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.

|                          | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--------------------------|---------------------|-----------------------------------|
| Cash at bank and in hand | 392                 | 366                               |
| Short-term deposits      | 1,634               | 473                               |
|                          | <b>2,026</b>        | 839                               |

#### (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 2016, \$122 million (2015: \$24 million) was held in these accounts.

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| <b>(b) Reconciliation of cash flows from operating activities</b>                                       |                     |                                   |
| <b>Loss after income tax</b>  | <b>(1,047)</b>      | (1,953)                           |
| Add/(deduct) non-cash items:  |                     |                                   |
| Depreciation and depletion  | 741                 | 793                               |
| Exploration and evaluation expensed   | 71                  | 88                                |
| Net impairment loss   | 1,561               | 2,854                             |
| Net loss/(gains) on fair value hedges   | 54                  | (14)                              |
| Share-based payment expense   | 11                  | 17                                |
| Unwind of the effect of discounting on provisions   | 41                  | 47                                |
| Foreign exchange gains  | (34)                | (41)                              |
| Other   | (94)                | 16                                |
| Net cash provided by operating activities before changes in assets or liabilities                       | <b>1,304</b>        | 1,807                             |
| Add/(deduct) change in operating assets or liabilities, net of acquisitions or disposals of businesses: |                     |                                   |
| Decrease in trade and other receivables   | 25                  | 60                                |
| Decrease/(increase) in inventories  | 15                  | (63)                              |
| Decrease/(increase) in other assets   | 35                  | (20)                              |
| Decrease in net deferred tax liabilities  | (500)               | (642)                             |
| Increase/(decrease) in current tax liabilities  | 75                  | (39)                              |
| Decrease in trade and other payables  | (82)                | (261)                             |
| Decrease in provisions  | (15)                | (31)                              |
| <b>Net cash provided by operating activities</b>  | <b>857</b>          | 811                               |
| <b>(c) Non-cash financing and investing activities</b>  |                     |                                   |
| Santos Dividend Reinvestment Plan   | <b>23</b>           | 61                                |

# Notes to the Consolidated Financial Statements

## Section 4: Working Capital Management

### 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.

|                    | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--------------------|---------------------|-----------------------------------|
| <b>Current</b>     |                     |                                   |
| Trade receivables  | 269                 | 248                               |
| Other receivables  | 98                  | 144                               |
|                    | <b>367</b>          | 392                               |
| <b>Non-current</b> |                     |                                   |
| Other receivables  | 5                   | 4                                 |

Of the Group's \$372 million total receivables (2015: \$396 million), \$363 million (2015: \$385 million) is not yet due and \$2 million (2015: \$1 million) is past due by over 12 months but not impaired. No amounts are considered impaired at 31 December 2016 (2015: nil).

### 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.

|  | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|---------------------|-----------------------------------|
| Petroleum products   | 219                 | 263                               |
| Drilling and maintenance stocks                                    | 102                 | 97                                |
| <b>Total inventories at lower of cost and net realisable value</b> | <b>321</b>          | 360                               |
| Inventories included above that are stated at net realisable value | 47                  | 62                                |

### 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.

|                    | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--------------------|---------------------|-----------------------------------|
| Trade payables     | 417                 | 537                               |
| Non-trade payables | 103                 | 81                                |
|                    | <b>520</b>          | 618                               |

# 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.

On 15 December 2016 Santos Limited's BBB- corporate credit rating was affirmed by Standard & Poor's and the outlook revised from 'negative' to 'stable'.

### 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.

Fixed-rate notes that are hedged by an interest rate swap 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 | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|------------------------|-----|---------------------|-----------------------------------|
| <b>Current</b>         |     |                     |                                   |
| Bank loans – secured   | (a) | 132                 | 119                               |
| Bank loans – unsecured | (b) | 82                  | 32                                |
| Long-term notes        | (c) | 205                 | –                                 |
| Finance leases         | (e) | 1                   | 1                                 |
|                        |     | <b>420</b>          | 152                               |
| <b>Non-current</b>     |     |                     |                                   |
| Bank loans – secured   | (a) | 1,617               | 1,750                             |
| Bank loans – unsecured | (b) | 1,653               | 1,712                             |
| Long-term notes        | (c) | 413                 | 603                               |
| Subordinated notes     | (d) | 1,072               | 1,146                             |
| Finance leases         | (e) | 64                  | 35                                |
|                        |     | <b>4,819</b>        | 5,246                             |

# 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 4.79% as at 31 December 2016 (2015: 4.07%).

#### (a) Bank loans – secured

| <i>Facility</i>                | <b>PNG LNG</b>   |
|--------------------------------|--|
| <i>Currency</i>                | US dollars   |
| <i>Limit</i>                   | \$1,838 million (2015: \$1,973 million)  |
| <i>Drawn principal</i>         | \$1,838 million (2015: \$1,973 million)  |
| <i>Accounting balance</i>      | \$1,749 million (2015: \$1,869 million) including prepaid amounts  |
| <i>Effective interest rate</i> | 4.97% (2015: 4.57%)  |
| <i>Maturity</i>                | 2024–2026  |
| <i>Other</i>                   | 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.  |
|                                | <i>Assets pledged as security and restricted cash</i>  |
|                                | 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 \$2,959 million at 31 December 2016 (2015: \$2,910 million).   |
|                                | 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. Funds held in these accounts attributable to the Group may be withdrawn on the provision of acceptable credit support to the lenders. As at 31 December 2016, no letters of credit (2015: \$100 million) had been provided. |

#### (b) Bank loans – unsecured

| <i>Facility</i>                | <b>Term bank loans</b>            |
|--------------------------------|-----------------------------------|
| <i>Currency</i>                | US dollars                        |
| <i>Limit</i>                   | \$17 million (2015: \$32 million) |
| <i>Drawn principal</i>         | \$17 million (2015: \$32 million) |
| <i>Accounting balance</i>      | \$17 million (2015: \$32 million) |
| <i>Effective interest rate</i> | 0.87% (2015: 0.41%)               |
| <i>Maturity</i>                | 2017                              |

| <i>Facility</i>                | <b>Export credit agency supported loan facilities</b>             |
|--------------------------------|---|
| <i>Currency</i>                | US dollars  |
| <i>Limit</i>                   | \$1,730 million (2015: \$1,730 million)                           |
| <i>Drawn principal</i>         | \$1,730 million (2015: \$1,730 million)                           |
| <i>Accounting balance</i>      | \$1,718 million (2015: \$1,712 million) including prepaid amounts |
| <i>Effective interest rate</i> | 2.64% (2015: 2.40%)   |
| <i>Maturity</i>                | 2017–2024   |
| <i>Other</i>                   | Loan facilities are supported by various export credit agencies.  |



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

### (c) Long-term notes

| <i>Facility</i>                | <b>Long-term notes</b>   |
|--------------------------------|--|
| <i>Currency</i>                | US dollars   |
| <i>Limit</i>                   | \$577 million (2015: \$577 million)  |
| <i>Drawn principal</i>         | \$577 million (2015: \$577 million)  |
| <i>Accounting balance</i>      | \$618 million (2015: \$603 million) including fair value accounting measurement and prepaid amounts  |
| <i>Effective interest rate</i> | 1.41%  |
| <i>Maturity</i>                | 2017–2027  |
| <i>Other</i>                   | Long-term notes bear a fixed interest rate of 6.05% to 6.81% (2015: 6.05% to 6.81%), which have been swapped to floating rate commitments. |

### (d) Subordinated notes

| <i>Facility</i>                | <b>Subordinated notes</b>   |
|--------------------------------|---|
| <i>Currency</i>                | Euro  |
| <i>Limit</i>                   | €1,000 million (2015: €1,000 million)   |
| <i>Drawn principal</i>         | €1,000 million (2015: €1,000 million)   |
| <i>Accounting balance</i>      | \$1,072 million (2015: \$1,146 million) including fair value accounting measurement and prepaid amounts |
| <i>Effective interest rate</i> | 6.60% (2015: 6.12%)   |
| <i>Maturity</i>                | 2070  |
| <i>Other</i>                   | The notes mature in 2070 and can be redeemed at the Group's option on or after 22 September 2017.       |

### (e) Finance leases

Finance lease commitments are payable as follows:

|   | <b>2016</b>        | (Restated)<br>2015 |
|---|--------------------|--------------------|
|   | <b>US\$million</b> | US\$million        |
| Not later than one year                           | <b>10</b>          | 8                  |
| Later than one year but not later than five years | <b>37</b>          | 37                 |
| Later than five years                             | <b>124</b>         | 131                |
| Minimum lease payments                            | <b>171</b>         | 176                |
| Future finance charges                            | <b>(106)</b>       | (55)               |
| Leases not commenced at reporting date            | <b>–</b>           | (85)               |
| <b>Total lease liabilities</b>                    | <b>65</b>          | 36                 |

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.

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| <b>Finance income:</b>                            |                     |                                   |
| Interest income                                   | 15                  | 6                                 |
| <b>Total finance income</b>                       | <b>15</b>           | <b>6</b>                          |
| <b>Finance costs:</b>                             |                     |                                   |
| Interest paid to third parties                    | 275                 | 294                               |
| Deduct borrowing costs capitalised                | (20)                | (118)                             |
|   | <b>255</b>          | 176                               |
| Unwind of the effect of discounting on provisions | 41                  | 47                                |
| <b>Total finance costs</b>                        | <b>296</b>          | <b>223</b>                        |
| <b>Net finance costs</b>                          | <b>281</b>          | <b>217</b>                        |

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## 5.3 ISSUED CAPITAL

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### 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 2016 was A\$4.02 (2015: A\$3.68).

### Transaction costs

Transaction costs of an equity transaction are accounted for as a deduction from equity, net of any related income tax benefit. During 2016 transaction costs of \$13 million have been deducted from equity.

| Movement in ordinary shares   | Note | 2016                 | 2015             | 2016         | (Restated)       |
|---|------|----------------------|------------------|--------------|------------------|
|   |      | Number of shares     | Number of shares | US\$million  | 2015 US\$million |
| Balance at 1 January  |      | <b>1,766,210,639</b> | 983,750,151      | <b>8,119</b> | 5,762            |
| Institutional placement, net of costs                                       |      | <b>256,000,000</b>   | 73,529,412       | <b>738</b>   | 352              |
| Rights issue, net of costs  |      | –                    | 654,198,741      | –            | 1,781            |
| Santos Dividend Reinvestment Plan ("DRP")                                   |      | <b>8,205,002</b>     | 15,052,884       | <b>23</b>    | 61               |
| DRP underwriting  |      | –                    | 37,960,195       | –            | 158              |
| Santos Employee Share1000 Plan  | 7.2  | <b>297,036</b>       | 180,040          | <b>1</b>     | 1                |
| Santos Employee ShareMatch Plan   | 7.2  | <b>719,764</b>       | 890,889          | <b>2</b>     | 4                |
| Shares issued on vesting of Share Acquisition Rights ("SARs")               | 7.2  | <b>578,818</b>       | 611,618          | –            | –                |
| Shares issued on vesting of Executive Deferred Short-term incentive ("STI") |      | <b>253,747</b>       | –                | –            | –                |
| Shares issued on vesting of Executive Strategy Grant                        |      | <b>106,827</b>       | –                | –            | –                |
| Santos Executive Share Plan   |      | –                    | 18,000           | –            | –                |
| Non-executive Director Share Plan   |      | <b>17,842</b>        | 18,709           | –            | –                |
| <b>Balance at 31 December</b>   |      | <b>2,032,389,675</b> | 1,766,210,639    | <b>8,883</b> | 8,119            |

Included within the Group's ordinary shares at 31 December 2016 are 25,000 (2015: 25,000) ordinary shares paid to one cent with a value of nil (2015: nil).

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## 5.4 RESERVES AND RETAINED EARNINGS

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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; and
- exchange differences that arise on the translation of the monetary items that form part of the net investment in a foreign operation.

### 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.

### Accumulated profits reserve

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

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# Notes to the Consolidated Financial Statements

## Section 5: Funding and Risk Management

### 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 analysis in the case of interest rate, foreign exchange and commodity price risk, and ageing 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 covers 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) 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.

| <b>Financial assets held to manage liquidity risk<br/>2016</b> | <b>Less than<br/>1 year<br/>US\$million</b> | <b>1 to 2<br/>years<br/>US\$million</b> | <b>2 to 5<br/>years<br/>US\$million</b> | <b>More than<br/>5 years<br/>US\$million</b> |
|--|---|---|---|--|
| Cash and cash equivalents                                      | 2,026                                       | -                                       | -                                       | -  |
| <b>Derivative financial assets</b>                             |   |   |   |  |
| Interest rate swap contracts                                   | 31  | 25                                      | 36                                      | 11   |
| <b>Derivative financial liabilities</b>                        |   |   |   |  |
| Cross-currency swap contracts                                  | (368)                                       | -                                       | -                                       | -  |
| <b>Non-derivative financial liabilities</b>                    |   |   |   |  |
| 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 <sup>1</sup>                                 | (1,136)                                     | -                                       | -                                       | -  |
|  | <b>(568)</b>                                | <b>(331)</b>                            | <b>(2,320)</b>                          | <b>(1,781)</b>                               |

1. Subordinated debt matures in 2070, however it can be redeemed at the Group's option on or after September 2017.

| <b>Financial assets held to manage liquidity risk<br/>2015 (Restated)</b> | <b>Less than<br/>1 year<br/>US\$million</b> | <b>1 to 2<br/>years<br/>US\$million</b> | <b>2 to 5<br/>years<br/>US\$million</b> | <b>More than<br/>5 years<br/>US\$million</b> |
|---|---|---|---|--|
| Cash and cash equivalents   | 839   | -                                       | -                                       | -  |
| <b>Derivative financial assets</b>  |   |   |   |  |
| Interest rate swap contracts  | 30  | 26                                      | 37                                      | 17   |
| <b>Derivative financial liabilities</b>                                   |   |   |   |  |
| Cross-currency swap contracts   | 3   | (323)                                   | -                                       | -  |
| <b>Non-derivative financial liabilities</b>                               |   |   |   |  |
| Trade and other payables  | (618)                                       | -                                       | -                                       | -  |
| Obligations under finance leases  | (5)   | (5)                                     | (15)                                    | (66)   |
| Bank loans  | (288)                                       | (330)                                   | (2,157)                                 | (1,709)                                      |
| Long-term notes   | (37)  | (237)                                   | (214)                                   | (262)  |
| Subordinated debt   | (90)  | (1,183)                                 | -                                       | -  |
|   | <b>(166)</b>                                | <b>(2,052)</b>                          | <b>(2,349)</b>                          | <b>(2,020)</b>                               |

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## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

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### (b) 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 denominated in currencies other than the functional currency, borrowings denominated in Euros and capital and operating expenditure incurred in currencies other than US dollars, principally Australian dollars. 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 (2016: \$824 million; 2015: \$2,340 million), swapped using cross-currency swaps to US dollars and designated as a hedge of US dollar denominated investments in foreign operations (2016: \$1,410 million; 2015: \$1,410 million), or offset by US dollar denominated cash balances (2016: \$1,500 million; 2015: nil). 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 2016.

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 2016, the estimated impact of a  $\pm 15$  cent movement in the Australian dollar exchange rate (2015:  $\pm 15$  cent) combined with a  $\pm 10$  cent movement in the Euro exchange rate (2015:  $\pm 10$  cent), each against the US dollar, with all other variables held constant is \$5 million (2015: \$26 million) on post-tax profit and \$980 million (2015: \$1,020 million) on equity.

### (c) 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 and subordinated debt. 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 had a notional contract amount of \$1,777 million (2015: \$1,824 million) and a net fair value of \$83 million (2015: \$91 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 2016, taking into account interest rate swaps, it is estimated that if the US dollar London Interbank Offered Rate ("LIBOR") interest rates changed by  $\pm 0.50\%$  (2015:  $\pm 0.50\%$ ), Euro Interbank Offered Rate ("EURIBOR") changed by  $\pm 0.50\%$  (2015:  $\pm 0.50\%$ ) and Australian Bank Bill Swap reference rate ("BBSW") changed by  $\pm 0.50\%$  (2015:  $\pm 0.50\%$ ), with all other variables held constant, the impact on post-tax profit is \$6 million (2015: \$10 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 2016, the Group has 10.95 million barrels of open oil price option contracts (2015: nil), covering 2017 exposures. The 3-way collar option structure does not qualify for hedge accounting, with the movement in fair value recorded in the income statement. The Group continues to monitor oil price volatility and to assess whether further commodity price hedging is appropriate.

# Notes to the Consolidated Financial Statements

## Section 5: Funding and Risk Management

### 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

#### (d) 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. 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.

At 31 December 2016 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.

#### (e) 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 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 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:

|                      | 2016<br>%          | 2015<br>%   |
|----------------------|--------------------|-------------|
| Derivatives          | <b>(0.3) – 3.9</b> | (0.1) – 4.1 |
| Loans and borrowings | <b>(0.3) – 3.9</b> | (0.1) – 4.1 |

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.

## 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

### (f) Hedging

The Group uses derivative financial instruments to hedge its exposures to changes in foreign exchange rates, interest rates and commodity markets arising in the normal course of business. The principal derivatives that may be used are forward foreign exchange contracts, cross-currency interest rate swaps, interest rate swaps and oil price options. Their use 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'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 | <p>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.</p> <p>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.</p> <p>The gain or loss relating to the ineffective portion is recognised in the income statement within other income or other expenses.</p> <p>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.</p> | <p>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. 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.</p> <p>Amounts accumulated in equity are transferred to the income statement or the balance sheet, for a non-financial asset, at the same time as the hedged item is recognised.</p> <p>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.</p> <p>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.</p> |

#### **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.

# Notes to the Consolidated Financial Statements

## Section 5: Funding and Risk Management

### 5.5 FINANCIAL RISK MANAGEMENT (CONTINUED)

#### (f) Hedging (continued)

##### *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.

##### *Hedges in place*

The Group has issued €1,000 million subordinated notes with a fixed interest rate of 8.25%.

In order to reduce the variability of the cash flows arising from the Euro principal and interest payments to September 2017, the Group entered into cross-currency interest rate swap contracts in March 2011, under which it has a right to receive interest at fixed Euro rates and pay interest at floating US dollar interest rates. These contracts are in place to cover principal and interest payments on €950 million of the subordinated notes through to the call date in 2017.

Subordinated notes totalling €50 million have been swapped to a fixed US dollar interest rate of 8.48% through to the call date in 2017.

The cross-currency and interest rate swap contracts are recognised at fair value and all gains and losses attributable to the hedged risks are recognised in the hedge reserve and reclassified into the income statement when the interest expense is recognised.

The table below contains all "other financial assets and liabilities" as shown on the balance sheet, including derivative financial instruments used for hedging:

|                                     | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|-------------------------------------|---------------------|-----------------------------------|
| <b>Current assets</b>               |                     |                                   |
| Interest rate swap contracts        | 7                   | –                                 |
| Other                               | –                   | 1                                 |
|                                     | <b>7</b>            | <b>1</b>                          |
| <b>Non-current assets</b>           |                     |                                   |
| Interest rate swap contracts        | 77                  | 91                                |
| Available-for-sale financial assets | 8                   | 7                                 |
| Amounts held in escrow <sup>1</sup> | 62                  | 52                                |
| Defined benefit surplus             | 5                   | 8                                 |
|                                     | <b>152</b>          | <b>158</b>                        |
| <b>Current liabilities</b>          |                     |                                   |
| Cross-currency swap contracts       | 349                 | –                                 |
| Commodity derivatives               | 14                  | –                                 |
| Other                               | 3                   | 2                                 |
|                                     | <b>366</b>          | <b>2</b>                          |
| <b>Non-current liabilities</b>      |                     |                                   |
| Cross-currency swap contracts       | –                   | 282                               |
| Embedded derivatives                | 3                   | 4                                 |
| Other                               | 20                  | 23                                |
|                                     | <b>23</b>           | <b>309</b>                        |

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



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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

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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.

#### **Non-controlling interests**

Non-controlling interests in the net assets of consolidated entities are allocated their share of net profit after tax in the income statement, and are identified separately from the Group's equity in those entities. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

# Notes to the Consolidated Financial Statements

## Section 6: Group Structure

### 6.1 CONSOLIDATED ENTITIES (CONTINUED)

| Name  | Country of incorporation | Name   | Country of incorporation |
|---|--------------------------|--|--------------------------|
| <b>Santos Limited<sup>1</sup> (Parent Company)</b>                  | <b>AUS</b>               | <i>Controlled entities of Santos International Holdings Pty Ltd (cont)</i> |                          |
| <b>Controlled entities:</b>   |                          | Santos (BBF) Pty Ltd   | AUS                      |
| Alliance Petroleum Australia Pty Ltd <sup>1</sup>                   | AUS                      | <i>Controlled entities of Santos (BBF) Pty Ltd</i>                         |                          |
| Basin Oil Pty Ltd <sup>1</sup>                                      | AUS                      | Santos (SPV) Pty Ltd   | AUS                      |
| Bridgefield Pty Ltd   | AUS                      | <i>Controlled entity of Santos (SPV) Pty Ltd</i>                           |                          |
| Bridge Oil Developments Pty Ltd <sup>1</sup>                        | AUS                      | Santos (Madura Offshore) Pty Ltd   | AUS                      |
| Bronco Energy Pty Ltd   | AUS                      | Santos Belida Pty Ltd  | AUS                      |
| Canso Resources Pty Ltd <sup>5</sup>                                | AUS                      | Santos (Donggala) Pty Ltd <sup>5</sup>                                     | AUS                      |
| Doce Pty Ltd  | AUS                      | Santos Egypt Pty Ltd <sup>4</sup>  | AUS                      |
| Fairview Pipeline Pty Ltd <sup>1,2</sup>                            | AUS                      | Santos EOM Pty Ltd   | AUS                      |
| Farmout Drillers Pty Ltd <sup>5</sup>                               | AUS                      | Santos Hides Ltd   | PNG                      |
| Gidgealpa Oil Pty Ltd   | AUS                      | Santos International Pte Ltd   | SGP                      |
| Kipper GS Pty Ltd <sup>5</sup>                                      | AUS                      | Santos International Operations Pty Ltd                                    | AUS                      |
| <i>Controlled entities of Kipper GS Pty Ltd</i>                     |                          | Santos OIG Pty Ltd   | AUS                      |
| Santos Carbon Pty Ltd <sup>5</sup>                                  | AUS                      | Santos P'nyang Ltd   | PNG                      |
| <i>Controlled entity of Santos Carbon Pty Ltd</i>                   |                          | Santos (Papalang) Pty Ltd <sup>5</sup>                                     | AUS                      |
| SB Jethro Pty Ltd <sup>5</sup>                                      | AUS                      | Santos (Popodi) Pty Ltd <sup>5</sup>                                       | AUS                      |
| Moonie Pipeline Company Pty Ltd                                     | AUS                      | Santos Sabah Block R Limited   | GBR                      |
| Reef Oil Pty Ltd <sup>1</sup>                                       | AUS                      | Santos Sangu Field Ltd   | GBR                      |
| Santos Asia Pacific Pty Ltd   | AUS                      | Santos (UK) Limited  | GBR                      |
| <i>Controlled entities of Santos Asia Pacific Pty Ltd</i>           |                          | <i>Controlled entities of Santos (UK) Limited</i>                          |                          |
| Santos (Sampang) Pty Ltd  | AUS                      | Santos Northwest Natuna B.V.   | NLD                      |
| Santos (Warim) Pty Ltd  | AUS                      | Santos Petroleum Ventures B.V.   | NLD                      |
| Santos Australian Hydrocarbons Pty Ltd                              | AUS                      | Santos Sabah Block S Limited   | GBR                      |
| Santos (BOL) Pty Ltd <sup>1</sup>                                   | AUS                      | Santos Vietnam Pty Ltd   | AUS                      |
| <i>Controlled entity of Santos (BOL) Pty Ltd</i>                    |                          | Santos (JBJ1) Pty Ltd <sup>5</sup>   | AUS                      |
| Bridge Oil Exploration Pty Ltd                                      | AUS                      | <i>Controlled entities of Santos (JBJ1) Pty Ltd</i>                        |                          |
| Santos Browse Pty Ltd   | AUS                      | Santos (JBJ2) Pty Ltd <sup>5</sup>   | AUS                      |
| Santos CSG Pty Ltd  | AUS                      | Santos (JPDA 06-104) Pty Ltd <sup>5</sup>                                  | AUS                      |
| Santos Darwin LNG Pty Ltd <sup>1,3</sup>                            | AUS                      | Santos (JPDA 91-12) Pty Ltd  | AUS                      |
| Santos Direct Pty Ltd   | AUS                      | Santos (NARNL Cooper) Pty Ltd <sup>1</sup>                                 | AUS                      |
| Santos Facilities Pty Ltd <sup>5</sup>                              | AUS                      | Santos NSW Pty Ltd   | AUS                      |
| Santos Finance Ltd  | AUS                      | <i>Controlled entities of Santos NSW Pty Ltd</i>                           |                          |
| Santos GLNG Pty Ltd   | AUS                      | Santos NSW (Betel) Pty Ltd   | AUS                      |
| <i>Controlled entity of Santos GLNG Pty Ltd</i>                     |                          | Santos NSW (Hillgrove) Pty Ltd   | AUS                      |
| Santos GLNG Corp  | USA                      | Santos NSW (Holdings) Pty Ltd  | AUS                      |
| Santos (Globe) Pty Ltd  | AUS                      | <i>Controlled entities of Santos NSW (Holdings) Pty Ltd</i>                |                          |
| Santos International Holdings Pty Ltd                               | AUS                      | Santos NSW (LNGN) Pty Ltd  | AUS                      |
| <i>Controlled entities of Santos International Holdings Pty Ltd</i> |                          | Santos NSW (Pipeline) Pty Ltd  | AUS                      |
| Barracuda Ltd   | PNG                      | Santos NSW (Sales) Pty Ltd <sup>5</sup>                                    | AUS                      |
| Lavana Ltd  | PNG                      | Santos NSW (Narrabri Energy) Pty Ltd                                       | AUS                      |
| Sanro Insurance Pte Ltd   | SGP                      | <i>Controlled entities of Santos NSW (Narrabri Energy) Pty Ltd</i>         |                          |
| Santos Americas and Europe Corporation                              | USA                      | Santos NSW (Eastern) Pty Ltd   | AUS                      |
| <i>Controlled entities of Santos Americas and Europe Corp</i>       |                          | Santos NSW (Sulu) Pty Ltd <sup>5</sup>                                     | AUS                      |
| Santos TPY Corp   | USA                      | Santos NSW (Tooncomet) Pty Ltd <sup>5</sup>                                | AUS                      |
| <i>Controlled entities of Santos TPY Corp</i>                       |                          | Santos NSW (Narrabri Power) Pty Ltd  | AUS                      |
| Santos Queensland Corp  | USA                      | Santos NSW (Operations) Pty Ltd  | AUS                      |
| Santos TOG Corp   | USA                      | Santos (N.T.) Pty Ltd  | AUS                      |
| <i>Controlled entities of Santos TOG Corp</i>                       |                          | <i>Controlled entity of Santos (N.T.) Pty Ltd</i>                          |                          |
| Santos TOGA Pty Ltd   | AUS                      | Bonaparte Gas & Oil Pty Ltd  | AUS                      |
| Santos TPY CSG Corp   | USA                      | Santos Offshore Pty Ltd <sup>1</sup>                                       | AUS                      |
| Santos Bangladesh Ltd   | GBR                      | Santos Petroleum Pty Ltd <sup>1</sup>                                      | AUS                      |
| Santos Baturaja Pty Ltd   | AUS                      | Santos QLD Upstream Developments Pty Ltd                                   | AUS                      |

| <b>Name</b>  | <b>Country of incorporation</b> | <b>Name</b>  | <b>Country of incorporation</b> |
|--|---------------------------------|--|---------------------------------|
| Santos QNT Pty Ltd <sup>1</sup>                          | AUS                             | Santos Timor Sea Pipeline Pty Ltd  | AUS                             |
| <i>Controlled entities of Santos QNT Pty Ltd</i>         |                                 | Santos Ventures Pty Ltd  | AUS                             |
| Outback Energy Hunter Pty Ltd                            | AUS                             | SESAP Pty Ltd  | AUS                             |
| Santos QNT (No. 1) Pty Ltd <sup>1</sup>                  | AUS                             | Shaw River Power Station Pty Ltd   | AUS                             |
| <i>Controlled entities of Santos QNT (No. 1) Pty Ltd</i> |                                 | Vamgas Pty Ltd <sup>1</sup>  | AUS                             |
| Santos Petroleum Management Pty Ltd                      | AUS                             |  |                                 |
| Santos Petroleum Operations Pty Ltd <sup>5</sup>         | AUS                             | <b>Notes</b>   |                                 |
| TMOE Exploration Proprietary Limited                     | AUS                             | 1. Company is party to a Deed of Cross Guarantee. Refer note 6.5.                              |                                 |
| Santos QNT (No. 2) Pty Ltd <sup>1,3</sup>                | AUS                             | 2. Company joined the Deed of Cross Guarantee during 2016.                                     |                                 |
| <i>Controlled entities of Santos QNT (No. 2) Pty Ltd</i> |                                 | 3. Company has entered into a Revocation Deed to be released from the Deed of Cross Guarantee. |                                 |
| Moonie Oil Pty Ltd                                       | AUS                             | 4. Company was deregistered on 28 January 2016.  |                                 |
| Petromin Pty Ltd   | AUS                             | 5. Company placed in liquidation during 2016 and deregistered on 19 December 2016.             |                                 |
| Santos (299) Pty Ltd <sup>6</sup>                        | AUS                             | 6. In liquidation.   |                                 |
| Santos Exploration Pty Ltd <sup>5</sup>                  | AUS                             | <b>Country of incorporation</b>  |                                 |
| Santos Gnuco Pty Ltd <sup>5</sup>                        | AUS                             | AUS – Australia  |                                 |
| Santos Upstream Pty Ltd <sup>5</sup>                     | AUS                             | GBR – United Kingdom   |                                 |
| Santos TPC Pty Ltd                                       | AUS                             | NLD – Netherlands  |                                 |
| Santos Wilga Park Pty Ltd                                | AUS                             | PNG – Papua New Guinea   |                                 |
| Santos Resources Pty Ltd                                 | AUS                             | SGP – Singapore  |                                 |
| Santos (TGR) Pty Ltd                                     | AUS                             | USA – United States of America   |                                 |

## 6.2 ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES

There were no acquisitions or disposals of subsidiaries during 2016.

# 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.                     | <p>The Group recognises its interest in joint ventures using the equity method of accounting.</p> <p>Under the equity method, the investment in a joint venture is initially recognised in the consolidated 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.</p> <p>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.</p> |

## 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/<br>area of interest | Principal activities           | 2016<br>% Interest | 2015<br>% Interest |
|---|---|--------------------------------|--------------------|--------------------|
| <b>Oil and gas assets – Producing assets</b>      |   |                                |                    |                    |
| Barrow Island                                     | Barrow  | Oil production                 | 28.6               | 28.6               |
| Bayu-Undan  | Bayu-Undan  | Gas and liquids production     | 11.5               | 11.5               |
| Casino <sup>1</sup>                               | Victoria  | Gas production                 | 50.0               | 50.0               |
| Chim São  | 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 PSC (Maleo)                       | Madura PSC  | Gas production                 | 67.5               | 67.5               |
| Mutineer-Exeter/<br>Fletcher Finucane             | Mutineer-Exeter/<br>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 PSC (Oyong, Wortel)                       | Sampang PSC                                       | Oil and gas production         | 45.0               | 45.0               |
| Stag  | Stag  | Oil production                 | –                  | 66.7               |
| SWQ Unit  | Cooper Basin                                      | Gas production                 | 60.1               | 60.1               |
| <b>Oil and gas assets – Assets in development</b> |   |                                |                    |                    |
| Kipper  | Kipper  | Gas development                | –                  | 35.0               |
| <b>Exploration and evaluation assets</b>          |   |                                |                    |                    |
| EPP43   | Ceduna Basin                                      | Contingent oil or gas resource | 50.0               | 50.0               |
| EP161, 162 and 189                                | McArthur Basin                                    | Contingent gas resource        | 50.0               | 50.0               |
| Block R   | –   | Oil and gas exploration        | 20.0               | 20.0               |
| Caldita/Barossa                                   | Bonaparte Basin                                   | Contingent gas resource        | 25.0               | 25.0               |
| Northwest Natuna                                  | –   | 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  | –   | Oil and gas exploration        | 30.0               | 30.0               |
| PPL402 <sup>2</sup>                               | –   | Gas discovery                  | –                  | –                  |
| 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 <sup>3</sup>                              | Carnarvon Basin                                   | Contingent gas resource        | 24.8               | 24.8               |

1. Asset classified as held for sale.

2. During 2016 the Group acquired a 20% interest in PPL402, which is subject to customary regulatory approvals.

3. During 2016 the Group acquired an additional 6.7% interest in WA-49-R, which is subject to customary regulatory approvals.

# 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                   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|---------------------|-----------------------------------|
| <b>Reconciliation to carrying amount:</b>                    |                     |                                   |
| <b>Opening net assets 1 January</b>                          | <b>620</b>          | 693                               |
| Profit for the period  | <b>88</b>           | 91                                |
| Reduction in capital   | <b>(130)</b>        | (70)                              |
| Dividends paid   | <b>(88)</b>         | (94)                              |
| <b>Closing net assets 31 December</b>                        | <b>490</b>          | 620                               |
| Group's share (%)  | <b>11.5%</b>        | 11.5%                             |
| Group's share of closing net assets (\$million)              | <b>56</b>           | 71                                |
| Carrying amount of investments in joint ventures (\$million) | <b>56</b>           | 71                                |
| <b>Summarised statement of comprehensive income:</b>         |                     |                                   |
| <b>Profit for the period</b>                                 | <b>88</b>           | 91                                |
| Other comprehensive income                                   | –                   | –                                 |
| <b>Total comprehensive income</b>                            | <b>88</b>           | 91                                |
| Group's share of profit                                      | <b>10</b>           | 10                                |
| Dividends received from joint venture                        | <b>10</b>           | 10                                |

The following are the joint ventures in which the Group has an interest, including those which are immaterial:

| Joint venture                                  | 2016<br>% interest | 2015<br>% interest |
|--|--------------------|--------------------|
| Darwin LNG Pty Ltd                             | <b>11.5</b>        | 11.5               |
| Easternwell Drilling Services Holdings Pty Ltd | –                  | 50.0               |
| GLNG Operations Pty Ltd                        | <b>30.0</b>        | 30.0               |
| GLNG Property Pty Ltd                          | <b>30.0</b>        | 30.0               |
| Lohengrin Pty Ltd                              | <b>50.0</b>        | 50.0               |

#### (c) Income from all joint ventures

A reconciliation of the Group's total income from all joint ventures:

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| Share of Darwin LNG Pty Ltd net profits | <b>10</b>           | 10                                |
| <b>Total share of net profits</b>       | <b>10</b>           | 10                                |

At 31 December 2016 the Group reassessed the carrying amount of its investments in joint ventures for indicators of impairment. As a result, no impairment was recorded (2015: nil).

## 6.4 PARENT ENTITY DISCLOSURES

Selected financial information of the ultimate parent entity in the Group, Santos Limited, is as follows:

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| <b>Net profit/(loss) for the period</b> | <b>42</b>           | (2,519)                           |
| Total comprehensive income/(loss)       | <b>43</b>           | (2,514)                           |
| Current assets                          | <b>414</b>          | 963                               |
| Total assets                            | <b>9,757</b>        | 9,290                             |
| Current liabilities                     | <b>529</b>          | 1,351                             |
| Total liabilities                       | <b>3,389</b>        | 3,619                             |
| Issued capital                          | <b>8,883</b>        | 8,119                             |
| Reserves                                | <b>(766)</b>        | (899)                             |
| Accumulated losses                      | <b>(1,750)</b>      | (1,549)                           |
| <b>Total equity</b>                     | <b>6,367</b>        | 5,671                             |

### Commitments of the parent entity

The parent entity's capital expenditure commitments and minimum exploration commitments are:

|                                 |           |    |
|---------------------------------|-----------|----|
| Capital expenditure commitments | <b>42</b> | 75 |
| Minimum exploration commitments | <b>27</b> | 18 |

### 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.

# 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 (refer footnote 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 2016 of the Closed Group.

|  | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|--|---------------------|-----------------------------------|
| <b>Consolidated income statement</b>                                 |                     |                                   |
| Product sales  | 1,147               | 1,193                             |
| Cost of sales  | (1,008)             | (1,103)                           |
| <b>Gross profit</b>  | <b>139</b>          | 90                                |
| Other revenue  | 369                 | 311                               |
| Other income   | 98                  | 11                                |
| Other expenses   | (126)               | (231)                             |
| Impairment of non-current assets                                     | (306)               | (3,791)                           |
| Interest income  | 9                   | 4                                 |
| Finance costs  | (5)                 | (41)                              |
| <b>Profit/(loss) before tax</b>                                      | <b>178</b>          | (3,647)                           |
| Income tax (expense)/benefit   | (45)                | 638                               |
| Royalty-related tax (expense)/benefit                                | (15)                | 18                                |
| Total tax (expense)/benefit  | (60)                | 656                               |
| <b>Net profit/(loss) for the period</b>                              | <b>118</b>          | (2,991)                           |
| <b>Consolidated statement of comprehensive income</b>                |                     |                                   |
| <b>Net profit/(loss) for the period</b>                              | <b>118</b>          | (2,991)                           |
| <b>Other comprehensive income, net of tax:</b>                       |                     |                                   |
| Net actuarial gain on defined benefit plan                           | 1                   | 3                                 |
| <b>Total comprehensive profit/(loss)</b>                             | <b>119</b>          | (2,988)                           |
| <b>Summary of movements in the Closed Group's retained earnings:</b> |                     |                                   |
| Retained earnings at 1 January                                       | (2,133)             | 1,178                             |
| Add opening retained earnings of companies added during the period   | 6                   | –                                 |
| Transfer to accumulated profits reserve                              | (258)               | (121)                             |
| Net profit/(loss) for the period                                     | 118                 | (2,991)                           |
| Net actuarial gain on defined benefit plan                           | 1                   | 3                                 |
| Dividends to shareholders  | –                   | (219)                             |
| Share-based payment transactions                                     | 10                  | 17                                |
| <b>Accumulated losses at 31 December</b>                             | <b>(2,256)</b>      | (2,133)                           |



## 6.5 DEED OF CROSS GUARANTEE (CONTINUED)

Set out below is a consolidated statement of financial position as at 31 December 2016 of the Closed Group:

|                                       | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---------------------------------------|---------------------|-----------------------------------|
| <b>Current assets</b>                 |                     |                                   |
| Cash and cash equivalents             | 130                 | 683                               |
| Trade and other receivables           | 1,665               | 1,398                             |
| Other current assets                  | 268                 | 134                               |
| <b>Total current assets</b>           | <b>2,063</b>        | 2,215                             |
| <b>Non-current assets</b>             |                     |                                   |
| Other financial assets                | 7,316               | 6,093                             |
| Exploration and evaluation assets     | 143                 | 125                               |
| Oil and gas assets                    | 1,891               | 2,160                             |
| Other non-current assets              | 1,064               | 1,432                             |
| <b>Total non-current assets</b>       | <b>10,414</b>       | 9,810                             |
| <b>Total assets</b>                   | <b>12,477</b>       | 12,025                            |
| <b>Current liabilities</b>            |                     |                                   |
| Trade and other payables              | 1,339               | 1,286                             |
| Other current liabilities             | 154                 | 749                               |
| <b>Total current liabilities</b>      | <b>1,493</b>        | 2,035                             |
| <b>Non-current liabilities</b>        |                     |                                   |
| Interest-bearing loans and borrowings | 4,053               | 3,593                             |
| Provisions                            | 1,041               | 1,293                             |
| Other non-current liabilities         | 86                  | 134                               |
| <b>Total non-current liabilities</b>  | <b>5,180</b>        | 5,020                             |
| <b>Total liabilities</b>              | <b>6,673</b>        | 7,055                             |
| <b>Net assets</b>                     | <b>5,804</b>        | 4,970                             |
| <b>Equity</b>                         |                     |                                   |
| Issued capital                        | 8,883               | 8,119                             |
| Reserves                              | (823)               | (1,016)                           |
| Accumulated losses                    | (2,256)             | (2,133)                           |
| <b>Total equity</b>                   | <b>5,804</b>        | 4,970                             |

# 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 employees and key management personnel. It includes details of our employee benefits and share-based payment schemes.

### 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 benefit 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 and 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 \$2 million (2015: \$1 million) was recorded in relation to the defined benefit plan.

The Group expects to contribute \$2 million to the defined benefit superannuation plan in 2017 (2016: \$1 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 \$12 million (2015: \$11 million).

The following amounts are recognised on the Group's balance sheet in relation to employee benefits:

|   | 2016<br>US\$million | (Restated)<br>2015<br>US\$million |
|---|---------------------|-----------------------------------|
| <b>Non-current assets</b>                 |                     |                                   |
| Defined benefit surplus                   | 5                   | 8                                 |
| <b>Current provisions</b>                 |                     |                                   |
| Employee benefits                         | 45                  | 60                                |
| <b>Non-current provisions</b>             |                     |                                   |
| Employee benefits                         | 10                  | 10                                |
| Defined benefit obligations               | 3                   | –                                 |
| Total non-current provisions              | 13                  | 10                                |
| <b>Total employee benefits provisions</b> | <b>58</b>           | <b>70</b>                         |

## 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 financial statements of the Group during the financial year in relation to shares issued under the share plans are summarised as follows:

|  | 2016<br>US\$000 | (Restated)<br>2015<br>US\$000 |
|--|-----------------|-------------------------------|
| <i>Statement of financial position:</i>                                  |                 |                               |
| General employee share plans – ShareMatch Plan                           | <b>2,622</b>    | 4,583                         |
|  | <b>2,622</b>    | 4,583                         |
| <i>Issued capital:</i>   |                 |                               |
| General employee share plans:  |                 |                               |
| Share1000 Plan   | <b>1,007</b>    | 917                           |
| ShareMatch Plan (matched Share Acquisition Rights (“SARs”))              | <b>2,622</b>    | 4,583                         |
|  | <b>3,629</b>    | 5,500                         |
| <i>Retained earnings:</i>  |                 |                               |
| General employee share plans – matched SARs                              | <b>3,604</b>    | 4,337                         |
| Executive Long-Term Incentive share-based payment plans – equity-settled | <b>6,392</b>    | 11,797                        |
| 2012–2015 Four-year CEO Strategy Grant                                   | –               | (134)                         |
| 2013–2015 Three-year Executive Strategy Grant                            | –               | 73                            |
|  | <b>9,996</b>    | 16,073                        |
| <i>Employee expenses:</i>  |                 |                               |
| General employee share plans:  |                 |                               |
| Share1000 Plan   | <b>(1,007)</b>  | (917)                         |
| ShareMatch Plan (matched SARs)   | <b>(3,604)</b>  | (4,337)                       |
| Executive Long-Term Incentive share-based payment plans – equity-settled | <b>(6,392)</b>  | (11,797)                      |
| 2012–2015 Four-year CEO Strategy Grant                                   | –               | 134                           |
| 2013–2015 Three-year Executive Strategy Grant                            | –               | (73)                          |
|  | <b>(11,003)</b> | (16,990)                      |
| <b>Total equity</b>  | <b>2,622</b>    | 4,583                         |

# 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 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 2016 was A\$1,000 per employee (2015: 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><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:

| Year | Issue date  | Share1000 Plan    |                          | ShareMatch Plan   |                          |
|------|-------------|-------------------|--------------------------|-------------------|--------------------------|
|      |             | Issued shares No. | Fair value per share A\$ | Issued shares No. | Fair value per share A\$ |
| 2016 | 1 Sep 2016  | 297,036           | 4.44                     | 719,764           | 4.44                     |
| 2015 | 28 Jul 2015 | 180,040           | 7.14                     | 890,889           | 7.14                     |

## 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. |
|-------------------|---------------------------|----------------|-----------------|------------------|---------------------|
| <b>2016 Total</b> | <b>1,600,103</b>          | <b>719,764</b> | <b>(75,118)</b> | <b>(578,818)</b> | <b>1,665,931</b>    |
| 2015 Total        | 1,361,730                 | 890,889        | (56,025)        | (596,491)        | 1,600,103           |

The inputs used in the valuation of the SARs are as follows:

| Matched SARs grant                   | 2016        |
|--------------------------------------|-------------|
| Share price on grant date (A\$)      | <b>4.44</b> |
| Exercise price (A\$)                 | <b>Nil</b>  |
| Right life (weighted average, years) | <b>3</b>    |
| Expected dividends (% p.a.)          | <b>2.25</b> |
| Fair value at grant date (A\$)       | <b>4.15</b> |

The loan arrangements relating to the ShareMatch Plan are as follows:

During the year the Company issued \$3 million (2015: \$5 million) of share capital under the ShareMatch Plan, with \$4 million (2015: \$5 million) received from employees under loan arrangements. The movements in loans receivable from employees are:

|   | 2016<br>US\$000 | (Restated)<br>2015<br>US\$000 |
|---|-----------------|-------------------------------|
| Employee loans at 1 January                   | <b>2,695</b>    | 2,954                         |
| Ordinary share capital issued during the year | <b>2,622</b>    | 4,583                         |
| Cash received during the year                 | <b>(3,942)</b>  | (4,759)                       |
| Foreign exchange movement                     | <b>(25)</b>     | (83)                          |
| <b>Employee loans at 31 December</b>          | <b>1,350</b>    | 2,695                         |

### 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 2016 LTI Program offers consisted only of SARs. Performance Awards were granted to eligible executives in 2016 who were granted one four-year grant (1 January 2016 – 31 December 2019).

In each of the grants 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.

# Notes to the Consolidated Financial Statements

## Section 7: People

### 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. |
|-------------------|---------------------------|------------------|--------------------|------------|---------------------|
| <b>2016 total</b> | <b>7,650,098</b>          | <b>4,799,922</b> | <b>(3,047,376)</b> | <b>–</b>   | <b>9,402,644</b>    |
| 2015 total        | 6,631,253                 | 3,158,016        | (2,124,044)        | (15,127)   | 7,650,098           |

The SARs granted during 2016 totalling 4,799,922 were issued across the following four tranches, each with varying valuations:

| Performance awards                             | 2016      |           |           |           |
|--|-----------|-----------|-----------|-----------|
|  | N1        | N2        | N3        | N4        |
| Performance index                              | ASX 100   | S&P GEI   | FCFBP     | ROACE     |
| Fair value at grant date (A\$)                 | 3.18      | 3.20      | 4.21      | 4.21      |
| Share price on grant date (A\$)                | 4.54      | 4.54      | 4.54      | 4.54      |
| Exercise price (A\$)                           | nil       | nil       | nil       | nil       |
| Expected volatility (weighted average, % p.a.) | 42        | 42        | 42        | 42        |
| Right life (weighted average, years)           | 4         | 4         | 4         | 4         |
| Expected dividends (% p.a.)                    | 2.2       | 2.2       | 2.2       | 2.2       |
| Risk-free interest rate (% p.a.)               | 1.6       | 1.6       | 1.6       | 1.6       |
| Total granted (No.)                            | 1,199,981 | 1,199,981 | 1,199,980 | 1,199,980 |

The above table includes 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.

#### 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 Company's FCFBP and ROACE at the end of the vesting period. There is no re-testing of performance conditions. Each tranche of the Performance Awards granted during 2016 vests in accordance with the following vesting schedule, relative to the TSR conditions:

| 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.

## 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

### iii. Executive sign-on grants

- a. On 11 February 2016 the Company issued 333,822 SARs split across two tranches, as follows:
- 50% (166,911) are subject to a 12-month continuous service condition starting on 1 February 2016 and ending on 31 January 2017. If this service condition is satisfied, the SARs will vest on 1 February 2017; and
  - 50% (166,911) are subject to a 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.

- 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. If this service condition is satisfied, the SARs will vest on 1 December 2017.

The share price on 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.

### iv. Executive Deferred Short-Term Incentives (“STIs”)

Deferred STIs represent a proportion of the total executive STI of the applicable year that has been deferred in to 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:

|                   | Beginning of<br>the year<br>No. | Granted<br>No. | Lapsed<br>No. | Vested<br>No.  | End of<br>the year<br>No. |
|-------------------|---------------------------------|----------------|---------------|----------------|---------------------------|
| <b>2016 Total</b> | <b>154,409</b>                  | <b>308,163</b> | –             | <b>154,409</b> | <b>308,163</b>            |
| 2015 Total        | –                               | 154,409        | –             | –              | 154,409                   |

On 11 May 2016 the Company issued 308,163 deferred shares to eligible executives. The share price on the grant date was A\$4.06 and the fair value was A\$3.89 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<br>the year<br>No. | Lapsed<br>No.      | Exercised<br>No. | End of<br>the year<br>No. | Exercisable<br>at end of<br>the year<br>No. |
|--|---------------------------------|--------------------|------------------|---------------------------|---|
| <b>2016</b>                                  |                                 |                    |                  |                           |   |
| <b>Vested in prior years</b>                 | <b>3,922,588</b>                | <b>(2,763,300)</b> | –                | <b>1,159,288</b>          | <b>1,159,288</b>                            |
| <b>Weighted average exercise price (A\$)</b> | <b>12.38</b>                    | <b>11.28</b>       | –                | <b>15.01</b>              | <b>15.01</b>                                |
| 2015   |                                 |                    |                  |                           |   |
| Vested in prior years                        | 3,992,038                       | (69,450)           | –                | 3,922,588                 | 3,922,588                                   |
| Weighted average exercise price (A\$)        | 12.31                           | 8.46               | –                | 12.38                     | 12.38                                       |

# Notes to the Consolidated Financial Statements

## Section 7: People

### 7.2 SHARE-BASED PAYMENT PLANS (CONTINUED)

#### (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

| <b>(a) Key management personnel compensation</b> | <b>2016</b>    | (Restated)      |
|--|----------------|-----------------|
|  | <b>US\$000</b> | 2015<br>US\$000 |
| Short-term employee benefits                     | <b>6,444</b>   | 5,415           |
| Post-employment benefits                         | <b>194</b>     | 181             |
| Other long-term benefits                         | <b>29</b>      | 47              |
| Termination benefits                             | <b>836</b>     | 1,754           |
| Share-based payments                             | <b>2,631</b>   | 3,324           |
|  | <b>10,134</b>  | 10,721          |

#### (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.



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# 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.

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### 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.

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### 8.2 EVENTS AFTER THE END OF THE REPORTING PERIOD

On 6 February 2017 Santos completed the Share Purchase Plan, as announced during December 2016, with total proceeds of approximately A\$201 million received.

On 16 February 2017, the Directors of Santos Limited resolved not to pay a final dividend in respect of the 2016 financial year.

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### 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 has 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 2016, approximately A\$3.5 million (2015: A\$6 million) remains to be paid over the remainder of the 10-year period through to 29 November 2017; 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 2016, if this condition had not been met, the Company would have been liable to pay a maximum of A\$50 million (2015: A\$50 million) to the State Government of South Australia.

Santos is required to make these payments only if the State Government of South Australia does 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 has an adverse discriminatory effect in their application to the Company relative to other companies domiciled in South Australia.

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# Notes to the Consolidated Financial Statements

## Section 8: Other

### 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:

|   | 2016<br>US\$000 | (Restated)<br>2015<br>US\$000 |
|---|-----------------|-------------------------------|
| Ernst & Young (Australia)                           | 1,070           | 1,102                         |
| Overseas network firms of Ernst & Young (Australia) | 150             | 168                           |
|   | <b>1,220</b>    | <b>1,270</b>                  |

#### (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:

|   | 2016<br>US\$000 | (Restated)<br>2015<br>US\$000 |
|---|-----------------|-------------------------------|
| Ernst & Young (Australia) for other assurance services                    | 360             | 381                           |
| Ernst & Young (Australia) for taxation and other services                 | 2               | 48                            |
| Overseas network firms of Ernst & Young (Australia) for taxation services | 14              | 15                            |
|   | <b>376</b>      | <b>444</b>                    |

### 8.5 ACCOUNTING POLICIES

#### Changes in accounting policies and disclosures

The Group applied a number of amendments to accounting standards applicable for the first time for the financial year beginning 1 January 2016.

The amendments below did not impact the consolidated financial statements and disclosures of the Group:

- AASB 2014-3 *Amendments to Australian Accounting Standards – Accounting for acquisitions of Interests in Joint Operations (AASB 1 & AASB 11)*; and
- AASB 2015-2 *Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 101*.

In addition, several other standard amendments and interpretations were applicable for the first time in 2016, but were not relevant to the Company and do not impact the Group's annual consolidated financial statements or half-year condensed financial statements.

#### New standards and interpretations not yet adopted

The Group has not elected to apply any pronouncements before their effective date for the annual reporting period ended 31 December 2016.

## 8.5 ACCOUNTING POLICIES (CONTINUED)

### New standards and interpretations not yet adopted (continued)

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2017, 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 are set out below:

| Reference  | Description   | Application of standard   | Impact on Group financial report   |
|--|---|---|--|
| AASB 9 <i>Financial Instruments</i>                  | <p>AASB 9 as issued replaces AASB 139 and includes a logical model for classification, measurement and derecognition of financial assets, a single, forward-looking "expected loss" impairment model and a substantially reformed approach to hedge accounting. The main changes to the classification and measurement of financial assets and liabilities are:</p> <ul style="list-style-type: none"> <li>Financial assets that are debt instruments will be classified based on: (1) the objective of the entity's business model for managing the financial assets; and (2) the characteristics of the contractual cash flows.</li> <li>Irrevocable election are allowed on initial recognition to present gains and losses on investments in equity instruments that are not held-for-trading in other comprehensive income. Dividends in respect of these investments that are a return on investment can be recognised in profit or loss and there is no impairment or recycling on disposal of the instrument.</li> <li>Financial assets can be designated and measured at fair value through profit or loss at initial recognition if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would arise from measuring assets or liabilities, or recognising the gains and losses on them, on different bases.</li> <li>Where the fair value option is used for financial liabilities, the change attributable to changes in credit risk is presented in other comprehensive income, and the remaining change is presented in profit or loss.</li> </ul> | Effective 1 January 2018, however the Group intends adopting from 1 January 2017 (retrospective application). | The impact of adoption is not expected to be material. The most significant change will be the classification of fair value gains/losses on financial instruments resulting from changes in Santos' credit risk being recorded in other comprehensive income (rather than the income statement), which in 2016 totalled \$39 million (2015: \$14 million). |
| AASB 15 <i>Revenue from Contracts with Customers</i> | <p>AASB 15 as issued replaces AASB 111, AASB 118 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:</p> <p>Step 1: Identify the contract(s) with a customer</p> <p>Step 2: Identify the performance obligations in the contract</p> <p>Step 3: Determine the transaction price</p> <p>Step 4: Allocate the transaction price to the performance obligations in the contract</p> <p>Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation.</p>  | 1 January 2018  | Impact is currently being assessed. It is expected the key impacts will relate to: accounting for production imbalances and consideration of the entitlements method versus sales method; take-or-pay contracts; gas balance arrangements; and provisional pricing.  |

# 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 <i>Leases</i> | <p>The key features of AASB 16 are as follows:</p> <p><i>Lessee accounting</i></p> <ul style="list-style-type: none"> <li>Lessees are required to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value.</li> <li>A lessee measures right-of-use assets similarly to other non-financial assets and lease liabilities similarly to other financial liabilities.</li> <li>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 also includes 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.</li> <li>AASB 16 contains disclosure requirements for lessees.</li> </ul> <p><i>Lessor accounting</i></p> <ul style="list-style-type: none"> <li>AASB 16 substantially carries forward the lessor accounting requirements in AASB 117. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently.</li> <li>AASB 16 also requires enhanced disclosures to be provided by lessors that will improve information disclosed about a lessor's risk exposure, particularly to residual value risk.</li> </ul> | 1 January 2019          | Impact yet to be assessed.       |

Several other amendments to standards and interpretations will apply on or after 1 January 2017, 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 2016

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 2016 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 2016.
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 16th day of February 2017

On behalf of the Board:



Director

# Independent Auditor's Report to the members of Santos Limited

To the Shareholders of Santos Limited

## Report on the Audit of the Financial Report

### Opinion

We have audited the financial report of Santos Limited (the Company), including its subsidiaries (the Group), which comprises the consolidated statement of financial position as at 31 December 2016, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information and the Directors' Declaration.

In our opinion:

the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

- (i) giving a true and fair view of the Group's consolidated financial position as at 31 December 2016 and of its consolidated financial performance for the year ended on that date; and
- (ii) 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 *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's *APES110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia; and we have 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 judgement, 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 statements. 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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## 1. Recovery of carrying value of oil and gas assets

### Why significant

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 at 31 December 2016 and impairment testing was undertaken. The principal indicators of impairment were the ongoing low oil price and deficit between the net assets and market capitalisation of the Company.

The impairment testing process is complex and highly judgemental and is based on assumptions and estimates that are affected by expected future performance and market conditions. Key assumptions, judgements and estimates used in the formulation of the consolidated entity's impairment of exploration and evaluation assets and oil and gas assets are set out in the financial report in note 3.3.

At 31 December 2016, the consolidated entity has recognised a net impairment expense totalling US\$1.6 billion pertaining to exploration and evaluation assets and oil and gas assets. Refer to note 3.3 in the financial report.

### How our audit addressed the key audit matter

In obtaining sufficient audit evidence we evaluated the assumptions and methodologies used by the consolidated entity and the estimates made. In particular we considered those estimates and judgements relating to the determination of cash generating units (CGU's), the forecast cash flows and the inputs used to formulate those cash flows, such as discount rates, reserves and resources, inflation rates, operating costs, foreign exchange rates and commodity prices.

We involved our business modelling and valuation specialists to assist in the impairment assessment for the audit. Our audit procedures were undertaken across all material CGUs.

Specifically, we evaluated the discounted cash flow models and other data supporting the consolidated entity's assessment. In doing so, we:

- understood future production profiles compared to reserves and resources, as outlined in key audit matter 4, current sanctioned budgets and historical operations;
- evaluated commodity prices with reference to contractual arrangements, market prices (where available), broker consensus, analyst views and historical performance;
- evaluated discount rates and foreign exchange rates with reference to market prices (where available), market research, market practice, market indices, broker consensus and historical performance;
- compared future operating and development expenditure to current sanctioned budgets, historical expenditure and ensured variations were in accordance with our expectations based upon other information obtained throughout the audit; and
- tested the mathematical accuracy of the discounted cash flow models.

We also considered the adequacy of the financial report disclosures regarding impairment and the recoverable amount of the consolidated entity's assets.

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## 2. Funding and liquidity

### Why significant

While the consolidated entity had cash at bank at 31 December 2016 of US\$2.0 billion, the consolidated entity's interest-bearing loans and borrowings at 31 December 2016 were US\$5.3 billion. The consolidated entity has debt repayments due in the next 2 years, as outlined in note 5.5 of the financial report.

### How our audit addressed the key audit matter

We evaluated the consolidated entity's funding and liquidity position at 31 December 2016 and the ability of the consolidated entity to repay its debts as and when they fall due for a minimum of 12 months from the date of signing the financial report. We took specific note of the equity raise completed on 15 December 2016 raising A\$1 billion.

In order to assess the funding and liquidity position, we:

- understood the process undertaken to determine the appropriateness of the use of the going concern basis;
- understood the funding plan for the consolidated entity;
- obtained external confirmation of the consolidated entity's cash, short-term deposits and debt;
- assessed the debt covenant compliance calculations performed by the consolidated entity; and
- assessed the classification and disclosure of debt.

# Independent Auditor's Report

## to the members of Santos Limited (continued)

### 3. Accounting for deferred tax and uncertain tax positions

#### Why significant

The financial report of the consolidated entity includes deferred tax assets arising from Petroleum Resources Rent Tax (PRRT), as well as Income Taxes. The determination of the quantum, likelihood and timing of the realisation of deferred tax assets arising from PRRT and Income Taxes is highly judgemental, due to the interpretation of PRRT and income tax legislation, as well as the estimation of future taxable profits.

The consolidated entity recognised a net deferred tax asset of US\$0.8 billion at 31 December 2016 in respect of corporate income tax, which is disclosed in note 2.4 of the financial report.

#### How our audit addressed the key audit matter

We assessed the consolidated entity's determination of tax payable now and in the future. We involved our taxation specialists to assist in this assessment of the determination of the tax bases.

We considered the consolidated entity'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 made reference to forecasts of taxable profits and consistency of these forecasts with the consolidated entity's budgets approved by the Board and those used in impairment modelling.

We evaluated the assessment of uncertain tax positions through enquiries with the consolidated entity's taxation department, reviewed correspondence with local tax authorities and involved our tax specialists, where appropriate, to assess the associated provisions and disclosures.

We assessed the consolidated entity's disclosures about PRRT and Income Taxes which are included in the summary of significant accounting policies in note 2.4.

### 4. Estimation of oil and gas reserves and resources

#### Why significant

Estimation of oil and gas reserves and resources is conducted by specialist engineers, requiring significant judgement and the use of a number of assumptions, particularly those disclosed in note 3.2, by the consolidated entity. These estimates can have a material impact on the financial report, primarily in the following areas:

- 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);
- valuation of assets and impairment testing (note 3.3);
- calculation of depreciation, depletion and amortisation (DD&A) of assets (note 3.2); and
- the calculation of decommissioning and restoration provisions (note 3.4).

#### How our audit addressed the key audit matter

Our audit procedures focused on the work of the consolidated entity's experts, in accordance with ASA 620 *Using the Work of an Auditor's Expert* (ASA 620).

In obtaining sufficient audit evidence, we:

- assessed the competence and objectivity of both the consolidated entity's internal and external experts involved in the estimation process;
- evaluated the adequacy of the expert's work;
- understood the consolidated entity's reserves estimation process and controls;
- assessed the design and operating effectiveness of key controls over the reserves review process;
- understood the reasons for reserve revisions or the absence of reserves revisions where expected, and assessed changes in reserves or lack of changes in reserves with other information that we obtained throughout the audit; and
- reconciled to the applicable financial information.



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## 5. Decommissioning and restoration provisions

| Why significant   | How our audit addressed the key audit matter  |
|---|---|
| <p>The calculation of decommissioning and restoration provisions is conducted by specialist engineers and requires significant judgement 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.</p> <p>The judgements and estimation can have a material impact on the financial report. The consolidated entity has recognised decommissioning and restoration provisions of US\$1.5 billion at 31 December 2016 which are disclosed in note 3.4.</p> | <p>Our audit procedures focused on the work of the consolidated entity's experts, in accordance with ASA 620.</p> <p>In obtaining sufficient audit evidence, we:</p> <ul style="list-style-type: none"><li>assessed the competence and objectivity of both the consolidated entity's internal and external experts involved in the estimation process;</li><li>evaluated the adequacy of the expert's work;</li><li>understood the consolidated entity's decommissioning and restoration estimation processes;</li><li>tested the consistency in the application of principles and assumptions to other areas of the audit such as reserves estimation and impairment testing;</li><li>tested the mathematical accuracy of the net present value calculations and discount rate applied; and</li><li>reconciled the calculations to the financial report.</li></ul> |

### Information Other than the Financial Statements and Auditor's Report

The Directors are responsible for the other information. The other information comprises the information in the Group's Annual Report for the year ended 31 December 2016, but does not include the financial report and the auditor's report thereon.

Our opinion on the financial report does not cover the other information and we do not express any form of assurance conclusion thereon.

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 upon 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.

### Directors' Responsibilities 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 related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or 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 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 Australian Auditing Standards, we exercise professional judgement 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.
- 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 entity's internal control.

# Independent Auditor's Report to the members of Santos Limited (continued)

- 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 in the preparation of the financial report. We also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events and conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the disclosures in the financial report about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial report. However, future events or conditions may cause an entity 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 consolidated financial statements represent 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 to 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 Remuneration Report

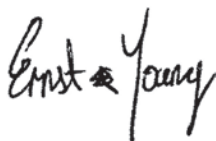
### Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 31 to 49 of the Directors' Report for the year ended 31 December 2016.

In our opinion, the Remuneration Report of Santos Limited for the year ended 31 December 2016 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



**R J Curtin**  
Engagement Partner  
Adelaide  
16 February 2017



**L A Carr**  
Engagement Partner

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# 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 2016, 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

16 February 2017

# Securities Exchange and Shareholder Information

Listed on the Australian Securities Exchange at 31 January 2017 were 2,032,086,651 fully paid ordinary shares. Unlisted were 12,500 partly paid Plan 0 shares, 12,500 partly paid Plan 2 shares, 228,039 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), 87,140 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 148,853 holders of all classes of issued ordinary shares, including: 2 holders of Plan 0 shares: 2 holders of Plan 2 shares: 24 holders of restricted shares pursuant to the SESPP; 1 holder of NED Share Plan shares: 36 holders of ShareMatch shares with further restrictions and 1 holder of SESPP shares with further restrictions. This compared with 162,013 holders of all classes of issued ordinary shares a year earlier.

On 31 January 2017 there were also: 35 holders of 1,159,288 Options granted pursuant to the Santos Executive Share Option Plan: 80 holders of 9,802,828 Share Acquisition Rights pursuant to the SESPP and 1,242 holders of 1,657,620 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 64.43% of the total voting power in Santos (56.94% on 29 February 2016). The largest shareholders of fully paid ordinary shares in Santos as shown in the Company's Register of Members at 31 January 2017 were:

| <b>Name</b>  | <b>No. of Shares</b> | <b>%</b>    |
|--|----------------------|-------------|
| HSBC Custody Nominees (Australia) Limited                              | 412,120,228          | 20.28       |
| Citicorp Nominees Pty Limited  | 260,795,613          | 12.83       |
| JP Morgan Nominees Australia Limited                                   | 223,729,440          | 11.01       |
| United Faith Ventures Limited  | 140,189,820          | 6.90        |
| National Nominees Limited  | 118,915,116          | 5.85        |
| BNP Paribas Nominees Pty Ltd <Agency Lending DRP A/c>                  | 44,675,737           | 2.20        |
| BNP Paribas Nominees Pty Ltd <Agency Lending Collateral>               | 19,257,000           | 0.95        |
| BNP Paribas Noms Pty Ltd <DRP>   | 14,356,090           | 0.71        |
| AMP Life Limited   | 11,427,593           | 0.56        |
| Argo Investments Limited   | 11,326,884           | 0.56        |
| HSBC Custody Nominees (Australia) Limited <NT-Comnwlth Super Corp A/c> | 11,066,981           | 0.54        |
| Citicorp Nominees Pty Limited <Colonial First State Inv A/c>           | 7,179,188            | 0.35        |
| HSBC Custody Nominees (Australia) Limited – A/c 2                      | 6,939,796            | 0.34        |
| UBS Nominees Pty Ltd   | 5,439,059            | 0.27        |
| RBC Investor Services Australia Nominees Pty Limited <PI Pooled A/c>   | 5,312,953            | 0.26        |
| Merrill Lynch (Australia) Nominees Pty Limited                         | 3,943,881            | 0.19        |
| HSBC Custody Nominees (Australia) Limited-GSCO ECA                     | 3,583,702            | 0.18        |
| Dynamic Supplies Investments Pty Ltd                                   | 3,091,868            | 0.15        |
| RBC Investor Services Australia Nominees Pty Ltd <VFA A/c>             | 2,990,901            | 0.15        |
| Bainpro Nominees Pty Limited   | 2,988,680            | 0.15        |
| <b>Total:</b>  | <b>1,309,330,530</b> | <b>64.4</b> |

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## ANALYSIS OF SHARES – RANGE OF SHARES HELD

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|  | <b>Fully paid<br/>ordinary<br/>shares<br/>(holders)</b> | <b>% of holders</b> | <b>% of shares<br/>held</b> |
|--|---|---------------------|-----------------------------|
| 1–1,000                                | 51,209  | 34.40               | 1.21                        |
| 1,001–5,000                            | 66,954  | 44.98               | 8.28                        |
| 5,001–10,000                           | 17,270  | 11.60               | 6.15                        |
| 10,001–100,000                         | 13,022  | 8.75                | 14.03                       |
| 100,001 and over                       | 398   | 0.27                | 70.33                       |
| <b>Total</b>                           | <b>148,853</b>  | <b>100.00</b>       | <b>100.00</b>               |
| Less than a marketable parcel of \$500 | 7,959   |                     |                             |

Substantial Shareholders as disclosed by notices received by the Company as at 16 February 2017:

| <b>Name</b>                    | <b>Number of voting<br/>shares held</b> |
|--------------------------------|---|
| ENN Ecological Holdings Co Ltd | 209,734,518                             |

For Directors' shareholdings see the Directors' Report as set out on page 16 of this Annual Report.

## VOTING RIGHTS

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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

## Aboriginal

Refers to both Aboriginal and Torres Strait Islander people.

## 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 its subsidiaries.

## condensate

A natural gas liquid that occurs in association with natural gas and is mainly composed of pentane and heavier hydrocarbon fractions.

## proven, probable plus possible reserves 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.

## CSG

Coal seam gas. Predominantly methane gas stored within coal deposits or seams.

## 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  $\times 10^9$

A terajoule (TJ) is equal to 1 joule  $\times 10^{12}$

A petajoule (PJ) is equal to 1 joule  $\times 10^{15}$

## 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 oil-bearing 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.

## medical treatment injury

A work-related injury or illness, other than a lost-time injury, that is serious enough to require more than minor first aid treatment. Santos classifies injuries that result in modified duties as medical treatment injuries.

## mmbbl

million barrels

## mmboe

million barrels of oil equivalent.

## mtpa

million tonnes per annum

## oil

A mixture of liquid hydrocarbons of different molecular weights.

## proven reserves (1P)

Reserves that, to a high degree of certainty (90% confidence), are recoverable. There is relatively little risk associated with these reserves. Proven developed reserves are reserves that can be recovered from existing wells with existing infrastructure and operating methods. Proven undeveloped reserves require development.

## proven 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 proven 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

|                        |                           |
|------------------------|---------------------------|
| Crude oil              | 1 barrel = 1 boe          |
| Sales gas              | 1 petajoule = 171,937 boe |
| Condensate/<br>naphtha | 1 barrel = 0,935 boe      |
| LPG                    | 1 tonne = 8,458 boe       |

For a comprehensive online conversion calculator tool, visit the Santos website at [www.santos.com](http://www.santos.com)





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