



**STATEMENT OF CORPORATE INTENT**

**2015/16**

## PURPOSE OF THE STATEMENT OF CORPORATE INTENT

This Statement of Corporate Intent (**SCI**) is prepared in accordance with Part 5 of the *Electricity Corporations Act 2005 (the Act)*, and reflects the business intentions of the Electricity Generation and Retail Corporation, trading as Synergy, for the 2015/16 financial year.

Consistent with the requirements of section 99 of the Act, amongst other things, this SCI outlines the objectives, functions, main undertakings and performance targets for the year, the community service obligations, the dividends and accounting policies to apply and the information to be provided to the Minister. Pursuant to section 97 of the Act, this SCI is intended to apply for the Corporation and any subsidiary.

The SCI is consistent with the Corporation's Strategic Development Plan (**SDP**) 2015/16 to 2019/20. The SDP sets out Synergy's economic and financial objectives and operational targets over the medium term, and the commercial strategies and initiatives it will pursue.

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## FROM THE CHAIRMAN

The SCI outlines Synergy's business and corporate social responsibility objectives for 2015/16, framing how Synergy intends to meet its legislative and statutory obligations.

This SCI reflects the opportunities and challenges confronting Synergy over the coming year as the entity continues to navigate an uncertain regulatory and commercial environment as WA's largest electricity generator and retailer.

The SCI addresses key external factors confronting the consolidated entity which have had a disruptive effect on Synergy's business (but are common to power utilities globally), and have subsequently contributed to weaker demand and rising price pressures for grid supplied electricity. These external challenges have a range of implications for Synergy's internal positioning, across retail, wholesale, generation and corporate.

External challenges present an opportunity for Synergy to improve the way it engages with customers during 2015/16. Customer awareness and engagement on energy issues has increased, with customers seeking greater dialogue on the energy matters that will impact them now and into the future. A continuing focus on deepening customer engagement levels, moving dialogue with customers beyond the price of electricity, and extending products and services to reflect customer needs will ensure Synergy responds to these challenges.

Synergy has developed a robust and effective strategy which will set the future direction for the business including:

- (a) driving efficiencies across the business to create a sustainable cost base;
- (b) build out capabilities and complete the integration; and
- (c) provide advice and energy solutions our customers want.

Synergy must consider a number of economic and social responsibilities in its planning. In particular, Synergy has a statutory obligation to operate in accordance with prudent commercial principles consistent with maximising its long-term value. A key focus for Synergy is continuing to decrease its reliance on operating subsidies and strengthening its foundations to mature into a robust and adaptable corporation able to meet the challenges of an uncertain future and a more competitive market.

Synergy has determined a strategy for the merged business which is underpinned by strategic initiatives to achieve our vision of being first choice in energy, providing trusted advice, information and energy solutions our customers want. In this context, Synergy has embarked on a dedicated corporate wide programme to identify efficiencies for a sustainable cost base whilst continuing to providing a reliable and efficient service.

**LYNDON ROWE**  
**CHAIRMAN**



## 1 BUSINESS OVERVIEW

The SCI considers Synergy's strategic vision, objectives and associated initiatives.

### 1.1 Operations/activities

Synergy is the largest integrated electricity generator and energy retailer servicing the south west interconnected system (SWIS) in Western Australia. Its objective is to utilise its diverse energy generation portfolio to supply reliable and efficient energy to wholesale and retail customers.

In its current state, the merged entity employs more than 1,000 employees servicing over one million electricity customer accounts and nearly 400 industrial and commercial gas customers.

Synergy owns Western Australia's largest electricity generation portfolio with 2,815 megawatts (MW) of capacity, and 1,400 MW contracted under power purchase agreements. Synergy has a wholesale market share of 78%<sup>1</sup>, including power purchase agreements and joint ventures, and a retail market share of 61%<sup>1</sup>.

The organisation structure of Synergy, provided for by regulations made under the Act, comprises:

- (a) Retail – carries out the retail operations of Synergy, involving the pricing, sale and marketing of electricity and gas to end-user customers in the SWIS. Retail is focussed on customer experience and driving high-levels of customer service and engagement;
- (b) Wholesale – responsible for the wholesale trading of electricity and gas. Wholesale manages the dispatch of Synergy's generation fleet and independent power producer contracts, as well as fuel contracts. Wholesale buys electricity and related products, and sells to the retail and wholesale market participants under ring fenced arrangements;
- (c) Generation – responsible for the management of Synergy's generating assets, including the safe and reliable operations and maintenance of Synergy's power stations and associated infrastructure;
- (d) Corporate Services – provides essential service support in critical business areas including legal, risk, audit, regulation and compliance, internal auditing, environment, document management and company secretary;
- (e) Commercial – responsible for the corporate strategies, business development and value creation; corporate communications, managing corporate relations with primary stakeholders including government, media and community groups, policy, long-term fuel procurement and business modelling;
- (f) Finance – responsible for all financial control matters across all of the individual business units, financial planning and analysis, procurement and fleet management services;

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<sup>1</sup> Calculated based on SWIS sent-out volumes

- (g) People & Culture – provides essential leadership across organisational development and human resources areas; and
- (h) ICT – responsible for the management of all information and communications technologies.

Key functions are segregated to protect any potential for commercially sensitive information to be used by Synergy's business units to potentially obtain an unfair advantage over competitors. These "ring fenced" areas are outlined below.

### **1.2 Ring fencing arrangements**

As provided for in the regulations, Synergy is bound by ring fencing arrangements intended to support the objectives of competitive neutrality in the generation and contestable retail market.

As the wholesale function is obliged to provide standard and non-standard (customised) products to the market on a competitively neutral basis, no advantage may be given to the retail function over any external competitors. In addition, access to competitor information that Wholesale may obtain or have access to in the course of discussions with competitors is restricted to ensure that retail or generation do not benefit.

All Synergy employees, including consultants, independent contractors and agents must comply with obligations pertaining to restricted information. Key items of sensitivity comprise information relating to generation and retail competitors, obtained by or provided to wholesale staff in their dealings in the wholesale market, and which might be expected to materially adversely affect the competitor if disclosed to staff in retail or generation.

## 2 EXTERNAL ENVIRONMENT AND INTERNAL CHALLENGES

In recent years, a variety of disruptive economic and technological changes have emerged around the world to compete with utility-provided services. In particular, an oversupply of generation capacity in the wholesale electricity market (**WEM**), weaker demand and rising price pressures for grid supplied electricity have both contributed to and exacerbated the continued competitiveness of a range of efficient, renewable and/or distributed generation technologies.

### 2.1 *Declining growth in customer demand*

Growth in electricity grid demand in the SWIS continues to decelerate over recent years. Key drivers include improvements in appliance and building energy efficiency, demand response to price increases, increased penetration of distributed generation (e.g. rooftop photovoltaic systems) and slower demand growth due to weaker manufacturing and mining activity. Retail competition for contestable volumes has also intensified due to excess supply in the wholesale market. Synergy's retail sales volumes declined by 14.5% from a peak in 2008/09 to 2013/14, and forecasts for coming years have been revised down.

### 2.2 *Excess supply in the wholesale market*

Lower electricity demand growth and a significant over supply of generation capacity have resulted in a large surplus of capacity and energy in the WEM. The situation has led to the underutilisation and suboptimal operations of Synergy's base load generation portfolio. This situation is likely to continue for the medium term in the absence of further plant retirements following Kwinana C in March 2015.

### 2.3 *Fuel markets*

Synergy is facing increased fuel price and supply risks due to financial difficulties of coal suppliers and higher priced and less flexible future gas supply arrangements relative to existing contract terms. Coal remains an important fuel source for baseload generation in the SWIS given relatively higher gas prices, and in providing fuel diversity to help mitigate the electricity supply security risks associated with gas produced in the north west and transported to the SWIS via a single major gas pipeline.

### 2.4 *Regulatory and policy environment*

Synergy faces an uncertain regulatory and political environment, reflecting potential changes to Commonwealth environmental policies and schemes, and market settings and rules at the state level. Key drivers include:

- (a) the application of the Commonwealth Government's Direct Action Plan to the electricity sector;
- (b) uncertainty regarding the large-scale renewable energy target (**LRET**) requirement to deliver 41,000 gigawatt hours (GWh) of energy from renewable sources by 2020. The Australian Government has completed a review of the renewable energy target including the interaction of small-scale generation under the small-scale renewable energy scheme (**SRES**); and
- (c) the State government's electricity market review with the objectives of reducing costs, facilitating private sector investment, and ensuring long-term stability.



### **3 STRATEGIC OBJECTIVES AND INITIATIVES**

The following strategic objectives represent key focus areas for Synergy:

- (a) driving efficiencies across the business to create a sustainable cost base;
- (b) understanding and managing our risks to drive profitable trading outcomes; and
- (c) creating profitable energy solutions whilst building a distinctive brand.

In addition to our strategic objectives, the safety and wellbeing of our people is fundamental to our business.

#### ***3.1 Driving efficiencies across the business to create a sustainable cost base***

Synergy will ensure it maximises the long term value of the business by actively driving efficiencies and achieving a sustainable cost base, which will enable it to remain competitive in wholesale and retail markets. Through a comprehensive whole of business program, we will simplify our business, understand and control our costs and invest where it makes sense to do so.

Synergy will need to drive plant efficiencies and optimisation to maintain its competitive position, while not compromising the safety and reliability of its operations. Business technology improvements together with leveraging and extracting efficiencies in the operation of the generation portfolio will also contribute to Synergy maintaining its competitive position within the SWIS generation market and enable more efficient decision making within the business.

#### ***3.2 Understanding and managing our risks to drive profitable trading outcomes***

Synergy is making good progress in understanding the role its ring fenced wholesale business unit plays in generating commercial returns for our business. Through informed decision making we will optimise our portfolio and improve our overall performance. We will do this by:

- (a) continuing to develop the wholesale trading function, including developing a sales and wholesale contract strategy which balances margin and market risks;
- (b) optimising Synergy's wholesale electricity portfolio (the combined former Synergy's power purchase arrangements and the former Verve Energy's generation assets and power purchase arrangements) to ensure energy is delivered at the lowest possible cost; and
- (c) optimising the combined wholesale sales and generation gas portfolio with the retail gas portfolio. This will include the optimisation of the gas supply and gas transport portfolio in conjunction with Mondarra gas storage operations.

#### ***3.3 Creating profitable energy solutions whilst building a distinctive brand***

Synergy will remain relevant to our customers by improving brand perception, deepening customer relationships and developing retail products and services to meet known customer needs. Key strategic activities include:



- (a) increasing brand engagement with customers across all target markets;
- (b) delivering new products and services with compelling value propositions;
- (c) improving customer interaction by enhancing digital services and channels; and
- (d) continuing to deepen engagement with customers.

Through delivery of these customer focussed objectives, Synergy hopes to be viewed within the franchise market as a trusted provider of advice on key energy management matters, including through self-service experience. Synergy's presence in the contestable market will encompass the provision of new energy solutions as required to meet changing customer needs.

## 4 PERFORMANCE MEASURES AND OBLIGATIONS

Synergy's most recently approved forecast financial outlook is presented below.

### 4.1 Key performance indicators

The business will manage day-to-day performance through the use of a wide range of operational key performance indicators. The measures and targets for these operational key performance indicators for 2015/16 are as detailed below:

Forecasts	2015/16
<b>Financial performance</b>	
EBITDA margin (%) *	7.6
NPAT margin (%) *	1.2
Return on assets (%)	2.1
Return on capital employed (%)	4.3
<b>Operational performance</b>	
Electricity sales – wholesale (GWh) *	4,093
Electricity sales – retail (GWh) *	10,012
Plant availability (%) *	81.7
Forced outage factor (%)	1.8
Portfolio capacity factor (%) <sup>2</sup>	40.3
Portfolio thermal efficiency (%) <sup>2</sup>	33.1
Greenhouse gas emissions (MtCO <sub>2</sub> e) <sup>3</sup>	8.3
Carbon intensity (tCO <sub>2</sub> e/GWh s/out) <sup>3</sup>	0.86
<b>Targets</b>	
<b>Operational performance</b>	
Worksafe breaches	Zero
Environmental incidents	Zero
Water licence incidents	Zero
Market rule breaches	Zero
<b>Customers</b>	
Grade of service	Greater than 80%
Number of complaints referred to the Energy Ombudsman	<1,800
Net promoter score *	+60
<b>Employee</b>	
Safety – Recordable Injury Frequency Rate *	< 8

\* Indicates inclusion in the Quarterly Report to the Minister and Treasurer

### 4.2 Dividend policy

Consistent with the performance targets, dividends are agreed annually with the Government

<sup>2</sup> Includes Synergy owned generation plant, PPAs, excludes Muja AB and JVs

<sup>3</sup> Includes Synergy owned generation plant, 50% Worsley, excludes PPAs, Muja AB and JVs

according to the profit results. Synergy will comply with the requirements of the Act and relevant regulations with regards to the dividend payout ratio to be paid from after tax profits.

### **4.3 Accounting policies and governance standards**

Synergy's accounting policies are consistent with corporations law requirements. Financial statements adopt the historic cost convention and reflect the accrual basis of accounting. Consistent with the State Budget, the projected financial outlook is in accordance with the International Financial Reporting Standards.

In addition, the following guidelines and standards are considered to be most relevant to Synergy's corporate governance practice.

- (a) Government of Western Australia: Corporate Governance Guidelines for Western Australian Public Sector CEOs.
- (b) Australian Standard: AS 8000-2003: Good Governance Principles.
- (c) Australian Standard: AS 3806-1999: Compliance Programs.
- (d) Australian Standard: AS 4360-2004: Risk Management.
- (e) Australian Stock Exchange Corporate Governance Council: Principles of Good Corporate Governance and Best Practice Recommendations ("ASX Guidelines").

Although Synergy is not obliged to comply with the ASX Guidelines, the business has committed to adopt best practice principles and practices that are in the best interests of its stakeholders.

### **4.4 Ministerial reporting**

To meet the reporting requirements as outlined in the Act, Synergy will provide the Minister and Treasurer with a quarterly report (including a separate statement of financial performance for each business unit and subsidiary), for the first three quarters, and an annual report for the whole financial year.

Each Quarterly Report will be submitted one month after the end of the quarter. It will include:

- (a) an overview of performance including specific performance indicators as detailed in the SCI;
- (b) highlights of important achievements; and
- (c) consolidated financial statements with relevant accompanying notes.

The following additional confidential information will be provided:

- (a) on a quarterly basis, for the profit and loss statement, a summary of key variances to year-to-date budget with accompanying commentary; and
- (b) on an annual basis, within three months of the end of the financial year, a schedule comparing actual capital expenditure against budgeted capital expenditure, by project.



The Annual Report will follow the end of the financial year and will be provided to the Minister and Treasurer within the time specified by the Act. It will include:

- (a) consolidated statutory financial statements;
- (b) other statutory information required of any company under the Corporations Law;
- (c) an overview of major achievements and an appraisal of future prospects;
- (d) a comparison of performance with the SCI targets; and
- (e) other information required by the Act to be included, such as the particulars of any directions given by the Minister.

In addition to quarterly and annual reports, the Minister and Treasurer will be provided with:

- (a) a five-year SDP and a one-year SCI;
- (b) a report on staff compliance with any board issued codes of conduct; and
- (c) any information in Synergy's possession requested by the Minister.

In communicating with the Minister, a formal protocol has been developed with the Minister's Office covering comprehensive communications with the Minister. The protocol is consistent with the Act and the *Public Sector Management Act 1994*. It seeks to ensure the Minister is provided with information that is factual, timely and reflects the best information available at the time. Consistent with the requirements of the Act, Synergy will consult the Minister on items of significant public interest.

#### **4.5 Community Service Obligations**

Section 99(1) of the Act defines "community service obligations" as "obligations to perform functions or to meet performance targets that it is not in the commercial interests of the corporation concerned to perform or meet".

Synergy is subject to a number of obligations that are not in its commercial interests. These are primarily transitional obligations imposed on Synergy to facilitate the development of the electricity market.

Synergy also administers the payment of a number of concessions, such as the Cost of Living Allowance and Dependant Child Rebates. Synergy is also required to administer the payment of the net feed-in tariff to eligible photo-voltic owners, representing the shortfall in available rebate provided for by the State government.

Synergy understands that it has been the government's view that, until the market is more fully developed, Synergy should be subjected to specific market power mitigation measures in addition to existing trade practices legislation.

The operating subsidy that Synergy receives is forecast to reduce from historical levels, but continues to remain high despite the historical price increases. As such the operating subsidy remains a significant risk to be addressed to ensure that Synergy remains a viable and sustainable business in the future.

## APPENDIX 1: EXPLANATORY NOTES CONCERNING KEY PERFORMANCE INDICATORS

KPI	Explanation
<b>Financial Performance</b>	
Earnings Before Interest, Depreciation, Amortisation and Tax (EBITDA) Margin	Measure of operating profitability margin regardless of capital structure (depreciation and interest payments) or taxes, calculated as: EBITDA / Total Revenue.
Net Profit After Tax (NPAT) Margin	Measure of profits of business operations - i.e. what remains after subtracting all the costs including depreciation, interest, and taxes from total revenue.
Return on Assets (ROA)	Measure of how profitable a company is relative to its total assets, calculated as: NPBT / Total Assets.
Return on Capital Employed (ROCE)	Measure of capital return, i.e. how much profit a company generated for each \$1 in capital employed (shareholder's capital plus short and long-term borrowed funds), calculated as: NPBT / (Total Assets – Non-Interest Bearing Liabilities).
<b>Operational Performance</b>	
Worksafe Breaches	Proven breaches of occupational health and safety legislation.
Environmental Incidents	Proven breaches of environmental protection legislation.
Water Licence Incidents	Proven breaches of conditions of water licences.
Market Rule Breaches	Proven breaches of market rules resulting in penalties.
Electricity Sales	Total electricity sales to customers sourced from both internal generation and purchases from other power producers.
Plant Availability	Measure of the percentage of energy a generating unit could deliver in any given period operating continually at full load.
Forced Outage Factor	Measure of plant reliability, i.e. the impact of unscheduled plant outages resulting in market penalties. Reductions in FOF are made possible by increases in Maintenance Outage Factor.
Portfolio Capacity Factor	The total portfolio generation in megawatt hours divided by the product of the period hours and the maximum dependable capacity in megawatts.
Portfolio Thermal Efficiency	Fuel to electrical energy conversion ratio, i.e. Energy Generated/Fuel Input.
Greenhouse Gas Emission	Million tonnes of carbon dioxide equivalent emitted.
Carbon Intensity	Tonnes of carbon dioxide equivalent emitted per Gigawatt of electricity sent out of generation portfolio.

<b>Customers</b>	
Grade of Service	The % of calls that were answered within 30 seconds.
Number of customer complaints referred to the Energy Ombudsman	The number of customers who choose to contact the Energy Ombudsman to resolve a dispute involving Synergy.
Net promoter score	A tool used to measure the loyalty of Synergy's residential (non-contestable) and contestable customers.
<b>Employee</b>	
Recordable Injury Frequency Rate (RIFR)	An occurrence that resulted in a fatality, permanent disability or time lost from work of one day/shift or more ( <a href="#">Workplace Injury and Disease Recording Standard (Australian Standard 1885.1 – 1990)</a> )