



AUSTAL LIMITED | 2017 | ANNUAL REPORT

## Contents

Contents.....	1
Index to the notes to the financial statements.....	2
Chairman’s report .....	3
Chief Executive Officer’s report.....	6
Review of operations .....	9
Directors’ report .....	13
Remuneration report (audited).....	20
Auditor independence.....	44
Consolidated statement of profit or loss and other comprehensive income for the year ended 30 June 2017 .....	45
Consolidated statement of financial position as at 30 June 2017 .....	46
Consolidated statement of changes in equity for the year ended 30 June 2017.....	47
Consolidated statement of cash flows for the year ended 30 June 2017.....	48
Notes to the financial statements .....	49
Directors’ declaration.....	121
Independent audit report to the members of Austal Limited .....	122
Shareholder information .....	127
Corporate governance statement .....	128
Corporate directory.....	130



Seaspovill launch at Austal Philippines in Cebu

## Index to the notes to the financial statements

Basis of preparation .....	49
Note 1 Corporate information .....	49
Note 2 Basis of preparation.....	49
Current year performance .....	57
Note 3 Operating segments .....	57
Note 4 Revenue .....	61
Note 5 Other Profit and Loss Disclosures.....	63
Note 6 Earnings per share .....	66
Note 7 Reconciliation of net profit after tax to net cash flows from operations .....	68
Note 8 Dividends paid and proposed .....	69
Note 9 Income and other taxes .....	70
Capital structure .....	75
Note 10 Cash and cash equivalents.....	75
Note 11 Interest bearing loans and borrowings .....	76
Note 12 Contributed equity and reserves.....	78
Note 13 Government grants relating to assets.....	80
Working capital.....	81
Note 14 Trade and other receivables.....	81
Note 15 Vessel construction and support contracts in progress.....	83
Note 16 Inventories and work in progress .....	84
Note 17 Trade and other payables.....	85
Infrastructure & other assets.....	86
Note 18 Property, plant and equipment .....	86
Note 19 Intangible assets and Goodwill.....	89
Note 20 Other financial assets .....	92
Other liabilities .....	93
Note 21 Provisions .....	93
Note 22 Fair value measurements .....	96
Note 23 Financial risk management .....	100
Note 24 Derivative financial instruments and hedging.....	106
Unrecognised items.....	109
Note 25 Commitments and contingencies.....	109
Note 26 Events after the balance date.....	109
The Group, management and related parties .....	110
Note 27 Parent interests in subsidiaries.....	110
Note 28 Related party disclosure .....	111
Note 29 Key management personnel compensation .....	111
Note 30 Share based payments .....	112
Note 31 Parent entity .....	120

## Chairman's report

It is my pleasure to present the 2017 Annual Report to you on behalf of the Board of Austal Limited.

The 2017 financial year was one of positive momentum right across the business, with operational improvements, stronger financial results, and important strategic milestones achieved as we look to the longer term.

We saw encouraging signs in the USA that our single largest contract – the Littoral Combat Ship (LCS) program – is proceeding broadly to plan after successful shock trial testing of the vessel was completed by the US Navy in July 2016. Meanwhile, our operationally mature Expeditionary Fast Transport (EPF) program continued to perform very well.



EPF 4, USNS Fall River was chosen by the US Navy to lead a goodwill mission to Myanmar in March 2017.

In Australia, we combined with leading German ship designer and builder Fassmer to submit a bid in March 2017 for the Royal Australian Navy's new Offshore Patrol Vessel, a circa \$3 billion shipbuilding program and sustainment.

We also commenced production of the Pacific Patrol Boat Replacement vessels (Guardian class) on schedule. These are critical programs for our Western Australia operations as they form the start of the Commonwealth's new continuous shipbuilding plan that will underpin our operations in Henderson for more than a decade.

The final shape of the Commonwealth's plan is crucial to ensure that Australia possesses a sovereign shipbuilding capability for decades to come across design, construction, and ongoing sustainment of defence vessels. Export aptitude is integral to leveraging additional export revenue from this newly-installed sovereign capability.

It is pleasing that Western Australia was selected as one of only two states that will form the centrepiece of the nation's shipbuilding plan. This, combined with our ability to deliver defence programs on time and on budget as 'The Australian Shipbuilder', positions Austal well to win our share of work. The task ahead is to translate this optimism into contracts.

The other significant leg of our shipbuilding activities is the high-speed commercial ferry market, which we reported on last year as showing signs of revival. This revival appeared to gather momentum in the year, evidenced by the award of two new ferry sales and substantial progress on further vessels likely to be signed in the near future.

There were a number of commercial and operational highlights during the year which include:

- \$1.309 billion Group Revenue and EBIT of \$45.538 million, which was in line with guidance provided at the start of FY2017.
- The award of LCS 28 from the US Navy in a contract valued at up to \$779 million, bringing total LCS orders to date to approximately \$7.2 billion and deliveries out to FY2022.
- Award of EPF 11 and EPF 12 from the US Navy under a contract worth \$431 million, taking total orders for this class of vessel to approximately \$2.7 billion and deliveries out to FY2020.
- Delivery of two vessels to the US Navy – the USS Gabrielle Giffords (LCS 10) and USNS Yuma (EPF 8). LCS 12 undertook acceptance trials and is expected to be delivered in the first half of FY2018.

- Delivery of Cape Inscription and Cape Fourcroy to the Royal Australian Navy (Cape Class Patrol Boats 9 and 10). Austal has now built and delivered 74 patrol vessels domestically and for five overseas markets, with a further 19 patrol vessels under contract.
- Delivery of the second 72-metre High Speed Support Vessel built in Australia for the Royal Navy of Oman, heralding a new class of ships for export markets based on the successful US-built EPF.
- Delivery of two crew transfer vessels – the ‘Rashid Behbudov’ to Caspian Marine Services and the ‘Pacific Kestrel’ to Swire Pacific Offshore. These vessels were designed to allow their crew to safely transfer onto offshore oil and gas platforms in rough sea conditions using walk to work capabilities, creating a viable cost effective alternative to helicopter crew transfer.
- Award of a 56 metre high-speed catamaran passenger ferry from FRS Group of Germany and the award of a 40 metre high speed passenger ferry from Blue Sea Jet, the first ferry contract awarded to Austal’s shipbuilding joint venture in China.
- Award of the Armidale remediation contract from the Royal Australian Navy. Austal completed a major overhaul of two ships in FY2017 under this contract, with further vessels due for refurbishment in FY2018.

Austal entered into a teaming agreement with ASC Shipbuilding in June 2017, to offer an Australian shipbuilding solution to the three shortlisted international designers in the Royal Australian Navy’s Future Frigate program. ASC Shipbuilding and Austal will act as one in seeking to support the Frigate program, pooling our complementary strengths, skills and experience under this agreement.

## Financial results

- Revenue for the year decreased by 2.2 per cent from \$1,339.970 million in FY2016 to \$1,310.128 million.
- FY2017 earnings before interest, tax, depreciation and amortisation (EBITDA) was \$77.060 million compared to \$(90.966) million in FY2016.
- Austal reported a net profit after tax of \$15.350 million in FY2017, compared to a net loss after tax of \$(84.182) million in FY2016.

- NPAT was suppressed by a high effective tax rate as a result of double taxation on inter-company royalties imposed by the Australian Tax Office and no recognition of carry forward tax losses from Australia. This tax treatment is explained in Note 9.
- USA operations remained the largest contributor to revenue and earnings, delivering \$1,172.066 million in revenue (FY2016: \$1,133.024 million) and \$76.061 million EBIT (FY2016: \$(90.457) million EBIT loss).
- Australia operations declined in FY2017, with revenue of \$113.744 million (FY2016: \$187.054 million) and an EBIT loss of \$(2.059) million (FY2016: \$6.756 million).
- Philippines operations reported revenue of \$33.832 million (FY2016: \$33.899 million) and EBIT of \$0.330 million (FY2016: \$(3.766) million EBIT loss).

## Financial summary

	2017 '000	2016 '000
Revenue <sup>1</sup>	\$ 1,308,603	\$ 1,338,864
EBITDA	\$ 77,060	\$ (90,966)
Depreciation Amortisation	\$ (30,379) (1,143)	\$ (28,461) (1,438)
EBIT	\$ 45,538	\$ (120,865)
Finance income	\$ 1,525	1,106
Finance cost	(7,198)	(6,605)
Profit / (loss) before income tax	\$ 39,865	\$ (126,364)
Income tax benefit / (expense)	\$ (24,515)	\$ 42,182
Profit / (loss) after tax	\$ 15,350	\$ (84,182)
% EBIT <sup>2</sup> / Revenue	3.5%	(9.0%)
Basic earnings per share (\$ per share)	\$ 0.04	\$ (0.24)
Net assets	\$ 456,914	\$ 457,552

1. Revenue from customers only

2. Earnings before interest and tax (EBIT)

EBIT and EBITDA are non-IFRS measures. The information is unaudited but is extracted from the audited financial statements. EBIT is used to understand segment performance and EBITDA is used by management to understand cash flows within the group.



## Board and Executive management

Austal undertook an extensive global search for an additional independent board member during the year, to strengthen and broaden our capability. Our objective is to infuse more advanced technological capability into both our ships and our shipbuilding operations aimed at 'smart ship' control systems and developing the 'digital shipyard'. Our search for a new Board member was focused on someone who understood this world as well as being able to contribute more broadly.

The Board intends to appoint Sarah Adam Gedge as an Independent, Non-Executive Director. Ms Gedge is currently Managing Director of Avanaide, a company dedicated to solving complex business issues for clients using the leading technologies of the Microsoft ecosystem. She has also held senior roles at IBM and PwC.

The Executive Management team was strengthened by the addition of Patrick Gregg in FY2017, who joined as Chief Operating Officer covering Australia and the Philippines. We also appointed Rusty Murdaugh as Chief Financial Officer for Austal USA following an extensive search.

Collectively the Executive Leadership Team continues to implement our strategic plan and deliver against our key operational objectives.

## Strategy and governance

The Board has continued its active engagement in reviewing the development of the Group strategy proposed by Executive management.

The annual review of the Group's risk management framework was conducted with involvement by the Audit and Risk committee and Remuneration and Nomination committee to ensure that the necessary controls and governance are in place, fit for purpose and amended as required.

## People

I wish to thank and acknowledge our hardworking employees for their consistent efforts and ongoing loyalty after a significant year, with many achievements to be proud of. Finally, my sincere thanks goes to Austal's shareholders for your ongoing support of the Company.



John Rothwell AO  
Chairman



LCS 8 arrives in San Diego after commissioning

## Chief Executive Officer's report

Austal is the largest aluminium shipbuilder in the world, with more than 300 ships either delivered or under construction for 100 customers in 54 countries globally. Austal is the world leader in large aluminium catamarans and the only successful builder of trimarans for the military and commercial ferry industries.

Austal's focus on innovation and manufacturing efficiency has driven the Company's success, most aptly characterised by its expansion from building commercial vessels in Australia to running two prime shipbuilding programs for military vessels in the United States. In fact, Austal is the only foreign company to deliver prime shipbuilding contracts to the US Navy since American independence, in what is arguably the world's most demanding market. These achievements mark out a successful past and provide a strong foundation for the next phase of Austal's development.

Austal is currently undergoing one of its most strategically active and defining periods in the Company's 29 year history. The Australian government issued tendering documents for two major shipbuilding programs during the last year, the Offshore Patrol Vessel (OPV) and the Future Frigate. These programs will define the shape of the domestic market and with it, Austal's future structure in Australia for decades to come.

Austal bid for the next award of Littoral Combat Ships (LCS) from our USA operations in FY2017, a program which remains our largest single generator of revenue. Austal was successful in the first phase of this through the award of its 14th LCS (LCS 28) in June 2017, with the strong likelihood of more to come.

I indicated in the 2016 Annual Report that the market for new passenger and vehicle ferries was showing signs of resurgence after several years in the doldrums in the wake of the financial crisis. This trend has continued and we have been making plans and investing in this part of our business as a result.

We strengthened our determination to retain Austal's leading position in fast aluminium vessels during FY2017, taking the Company's already efficient shipyards to a completely new level through employing more of the advanced manufacturing techniques that have

become available or that we have pioneered. This investment will benefit all of our shipyard locations and many of our products, be they military or civil.

We are resolute in remaining the product leader in trimaran vessels, high speed catamarans, and on-board systems that deliver real maintenance, operational, and fuel efficiency benefits in each vessel we deliver. The upcoming programs in the US and Australian navies and the growing fast ferry markets are the targets for these investments to ensure that we retain and develop our leading position and offer superior products to our customers.

### Australia operations

The Australian government has committed \$89 billion to a re-equipment program for the Royal Australian Navy, which includes new submarines, frigates, and patrol vessels. The first program was for the Pacific Patrol Boat Program, a \$305 million contract awarded to Austal by the Commonwealth of Australia in May 2016 to design, construct, and sustain (for an initial seven year period) 19 steel vessels destined for deployment to 12 Pacific Island nations for maritime protection. The contract is significant because it will be the first major steel navy fleet built by Austal and as such increases capability and credibility for the company outside of its core aluminium construction heritage. The program is on time and has met all of its key milestone events thus far, with the first vessel under construction and heading towards its planned delivery in October 2018. This program is strategically important because both the Offshore Patrol Vessel (OPV) and Future Frigate programs are steel ships.

Austal teamed with Fassmer GmbH, a world-class German ship designer and builder – lodged a bid for the OPV contract in March 2017. The program is to build twelve 80-metre vessels in a continuous shipbuilding plan for the next decade and a half, underpinning operations at our Henderson shipyard for that entire period. The result of the OPV Competitive Evaluation Program will be known by the end of calendar year 2017.

We have also been strategically positioning Austal to deliver the much larger Future Frigate program during FY2017. The Australian Department of Defence (DoD) has down selected three foreign designs for the future frigate and is currently undertaking a tendering process to define which vessel and which industrial solution for its construction they wish to pursue. Austal's unique success story as an Australian builder and designer of ships is undisputed, however we do not have a large steel ship pedigree nor operated in South Australia, the designated build location for these vessels.

Consequently, Austal has entered into a teaming agreement with the Government-owned shipyard, ASC to develop a compelling all-Australian option to the Government for the vessel construction. ASC has recent practical experience in building the Hobart class destroyers in Adelaide. We are also strengthening our steel shipbuilding expertise through the Pacific Patrol Boat Program. This approach is being marketed to both the Department of Defence and the Government as a locally capable, all-Australian alternative to a foreign-managed construction.

### United States operations

Austal's US operations remained the biggest revenue and profit driver for the business in FY2017 as we continued to deliver on two significant shipbuilding programs for the US Navy. Austal has designed and built the most modern and highly advanced naval shipyard in America which uses a modular construction system that incorporates production flow line techniques, similar in nature to the modern large aircraft industry.

The primary focus for Austal USA during the year was on improving operational efficiency, particularly for our LCS program as we move down the construction learning curve. Our ability to achieve this was driven by a US team of people who embody the culture of absolute determination. LCS costs to completion have trended to the budgets we set following our reset to the program in FY2016, and our confidence in a successful outcome has increased. For example, the operations team reduced labour hours used in constructing LCS 12 by almost 20% from LCS 6 (4 vessels).

This was achieved through a relentless program of maximising the use of the Module Manufacturing Facility, where efficiency is naturally high, to reduce work required at the completion facility or wharf side activity, where costs are always much higher. The significantly lower level of vessel modifications being required by the US Navy combined with the efficiency gains combined to deliver positive outcomes in FY2017. We expect that the LCS program will progressively mature to the reliable delivery performance exemplified by the Expeditionary Fast Transport (EPF) vessel, which continued to deliver strong financial performance in the year.

Austal USA has been preparing for the next stage of its journey in this environment. The US Navy announced its intention to truncate the LCS program, potentially in 2019, to transition the small surface combatant concept to a frigate – FFG(X) – which is able to provide lethal support for carrier group operations. Austal USA undertook funded design concept work on a modified version of LCS to meet the conceptual frigate requirement announced at the Sea Air and Space Exhibition in Washington during the second half of FY2017. The US Navy issued a Request for Information for the FFG(X) to potential contenders, including Austal, shortly after the end of FY2017.

### Philippines operations

Our aim in the Philippines is to ensure that our Cebu shipyard develops into the most cost efficient yard for our commercial customers, using designs for vessels from our proven design centre in Henderson, Australia.

We completely re-organised our management team in Cebu during the year and this has reaped immediate rewards with the team successfully delivering two vessels on time and at better than budget performance. Two additional vessels are also nearing completion.

Austal is also completing plans to increase capacity at the shipyard to cope with an expected increase in ship orders. This may include a new construction hall and launch facility. Our intention is to start construction of the new facilities in FY2018 if we are successful in securing new orders which are currently under negotiation.



## Ship support

Austal continues to focus on building its service and support businesses to sustain vessels, primarily delivered to navies, that will provide a steady stream of recurring revenue. Total support revenue grew by 37.7% to \$187.357 millions in FY2017, from activities in Australia and the USA. The opportunity to drive activity in post-delivery and in-service support of these vessels has increased as the US Navy fleet of LCS grows with the delivery of each vessel. The recent commencement of deployment of the ships overseas has prompted Austal to open a service centre in Singapore, our first in that country.

Support revenue in Australia in FY2017 was generated predominantly from a mid-life hull remediation and configuration changes program for the Armidale class patrol boats (ACPB) and planned, in-service maintenance for the Border Force fleet of Cape class patrol boats. The ACPB sustainment program was a significant success story as Austal won it in competition against an incumbent Singaporean-based company who had a positive track record on the vessels. Austal won this competition on price, in a victory for Australian excellence, and has delivered the program to date on time and at the target margins.

Austal has also expanded its presence in the north of Australia where many of the Austal-built Bay, Cape, and Armidale class patrol boats are based. Austal's Darwin service centre was expanded to further strengthen our capability during the year, while we opened a vessel sustainment office in Cairns early in FY2018 which includes significantly expanded infrastructure that is servicing our customers' needs.

## Outlook

Progress on all fronts in FY2017 provides us with increasing optimism for the future. We remain acutely aware that new construction programs must be won and current programs must be delivered on time and on cost if this optimism is to crystallise into results for our shareholders.

The procurement decisions to be made in the Australian defence sector in the new financial year will define the nature of Austal's operations in Australia for decades to come. Equally, the new Frigate program in the USA, offers long term opportunity and business continuity in a similar way, albeit with an outcome unlikely before FY2020. In the meantime, the business must and will continue to deliver its current order book efficiently and profitably.

Signature



David Singleton

Managing Director and Chief Executive Officer



EPF 8 USNS Yuma

## Review of operations

A financial breakdown for each business unit has been included below, including IFRS and non-IFRS information. This information has been extracted from the audited financial statements and included in order to demonstrate growth across the primary segments.

### US operations

Year ended 30 June	2017	2016
	\$'000	\$'000
Revenue	\$ 1,172,066	\$ 1,133,024
EBIT	76,061	(90,457)
EBIT Margin	6.5%	N/A

USA EBIT of \$76.061 million was a significant turnaround after the change of estimate for the costs to completion of the LCS (6 – 26) program during FY2016 with shipbuilding margin of 6.80% positioned towards the upper end of the guidance range provided in July 2016.

The USA operations had 12 vessels under construction during the year and delivered two vessels to the US Navy in FY2017 – one Littoral Combat Ship (LCS 10) and one Expeditionary Fast Transport vessel (EPF 8).

The total USA workforce has reduced to approximately 4,000 as a direct result of driving greater efficiency on of the two vessel programs down the learning curve. The entire workforce is focussed on identifying and exploiting opportunities for productivity improvements with results in keeping with internal expectations.

USA bid for 13 additional LCS during FY2017 with a reset material and labour cost base. Award of all 13 vessels would extend production activities until 2030. LCS 28, the first of the 13 vessels, was awarded to Austal in June 2017, with the possibility of a second award (LCS 30) during FY2018.

The order book was also replenished by the full contract award of EPF 11 & 12 which extended the Expeditionary Fast Transport (EPF) program beyond the original ten vessels.

There was significant progress in both major programs during the year from a construction perspective.

EPF 8, USNS Yuma was delivered in April 2017 after successfully completing acceptance trials in January 2017 and EPF 9, USNS City of Bismarck, was launched in June 2017. EPF 10 and 11 were under construction during FY2017.

The EPF program is mature with progressive improvements in efficiency and profit generation from each successive vessel that is delivered.



Austal opened a Singapore service centre during FY2017, providing support to US Navy operations of LCS & EPF.

LCS 10 USS Gabrielle Giffords was delivered in December 2016 and seven LCS (12 - 24) were at various stages of construction in FY2017; LCS 12 is undergoing sea trials and will be delivered in FY2018 H1, LCS 14 is preparing for sea trials, and LCS 16 was launched in March 2017. Assembly is well underway for LCS 18 and LCS 20 whilst modules for the future LCS 22 and LCS 24 are under construction in the modular manufacturing facility (MMF).

Austal continued to profitably expand its LCS and EPF Sustainment business, within the United States and elsewhere around the world. Austal USA opened a service centre in Singapore to support the forward deployment of US Navy EPF and LCS vessels.

## Australia operations

Year ended 30 June	2017 \$'000	2016 \$'000
Revenue	\$ 113,744	\$ 187,054
EBIT	(2,059)	6,756
EBIT Margin	N/A	3.6%

Austal's Australia operations were impacted by a forecasted contraction in production activity and profit generation as a result of three key drivers which are described in further detail below:

- The Pacific Patrol Boat fleet was under design with construction commencing late in FY2017
- A significant research and development phase for the Mols 109 metre ferry which was under design with construction commencing late in FY2017
- Construction of Cape Class Patrol Boats 9 & 10 for the Royal Australian Navy (RAN) under a financing arrangement with the National Australia Bank (NAB) which resulted in no profit recognition until a three year charter commenced late in FY2017.

Profitability in Australia was also significantly impacted by the recognition of an overall loss of \$(3.974) million including a \$(3.233) million loss provision for the Cape Class Patrol Boat (CCPB) In Service Support contract that was deemed to be onerous at the end of the financial year. (Refer provisions Note 21).



The 19 vessel PPB-R program is the first multi-vessel steel program Austal has undertaken and largest ever contract, by number of vessels.

Austal received a \$65 million order to construct a further two CCPB (9 & 10) for the Royal Australian Navy (RAN) in December 2015. Construction of both vessels commenced during FY2016 and was completed in late FY2017 with both vessels placed into service with the RAN. The RAN is chartering the vessels from the National Australia Bank under an initial contractual term of three years.

Austal won a \$305 million contract to design, construct and sustain nineteen 40 metre steel Pacific Patrol Boats (PPB) for the Commonwealth of Australia (CoA) in May 2016. The CoA is gifting the vessels to 12 Pacific Island nations.

A detailed PPB design review was completed and approved by the CoA during FY2017 H2 which permitted construction to commence.

Austal opened a dedicated facility for the construction of the steel Pacific Patrol Boats in March 2017 and a keel laying ceremony was held for the first vessel after year end in July 2017.

The PPB contract is Austal's first significant order for steel vessels which will both enhance and demonstrate the company's broader capability across multiple hull forms and hull materials.

The second of two 72 metre High Speed Support Vessels (HSSV) for the Royal Navy of Oman, was delivered in September 2016. Both HSSV are being sustained by Austal's Oman service centre in Muscat.

Construction of a 70 metre fast crew boat for Caspian Marine Services of Azerbaijan was completed in September 2016. The forward hull module was fabricated in the Austal Philippines shipyard and the aft hull module and superstructure were constructed concurrently in Australia. The forward hull was transported to Henderson in March 2016 for integration with the superstructure and aft hull modules, achieving an interval from commencement of construction to launch of just eight months.

Austal successfully applied a 'hybrid' construction strategy, which integrated the Australia and Philippines shipyards and the company's global supply chain.

Austal was awarded a \$100 million contract to design and construct a new 109 metre high speed aluminium ferry for Mols Linien of Denmark in June 2016. A significant research & development program was undertaken to significantly reduce structural weight and improve fuel efficiency.

The majority of the design was completed during FY2017 and construction commenced in April 2017 with the first cutting of aluminium plate.

Australia was awarded significant remediation contracts for four Armidale Class Patrol Boats (ACPB) during FY2017 with two vessels completed and returned to service with the RAN, one undertaking sea trials and one still under remediation at reporting date.

Austal teamed with Fassmer GmbH of Germany to jointly bid for the RAN Offshore Patrol Vessel (SEA1180) program, comprising 12 vessels to be



Mid-life remediation works began on four Armidale class patrol boats in Western Australia. Up to three more will be contracted in FY2018.

built in South Australia and Western Australia. The bid was submitted in March 2017 and was under review by the CoA at reporting date. The CoA has stated that it intends to negotiate and award a contract by December 2017.

### Philippines operations

Year ended 30 June	2017 \$'000	2016 \$'000
Revenue	\$ 33,832	\$ 33,899
EBIT	330	(3,766)
EBIT Margin	1.0%	N/A

Austal Philippines delivered three commercial vessels during FY2017.

A 57 metre offshore crew transfer vessel was delivered in FY2017 H1 after commencement in FY2016.

Austal Philippines secured a contract to build two 30 metre ferries new contracts for Philippines operator 2Go' in June 2016. Both vessels were designed, constructed, launched, commissioned and contractually delivered to the customer in June 017.

These vessels mark an important milestone as the first Austal ships to be constructed and delivered to a customer in the Philippines.

Austal was also awarded a contract to build a 50 metre ferry for Seaspovill of South Korea in June 2016. The vessel was designed and constructed during FY2017 with commissioning and contractual delivery completed after year end in July 2017.

These three vessels are valued collectively at approximately \$30 million.

The Philippines was awarded a \$21 million contract to build a 56 metre ferry for FRS in Germany in December 2016.

The design was completed and construction commenced during FY2017 H2. Delivery is scheduled for mid FY2018.

The Philippines shipyard continues to play a pivotal role in cost optimisation of manufacturing activities within the Group by supplying sub-assemblies and components to Australia, for programs such as the high speed crew transfer vessel for Caspian Marine Services in Azerbaijan.

### Safety performance

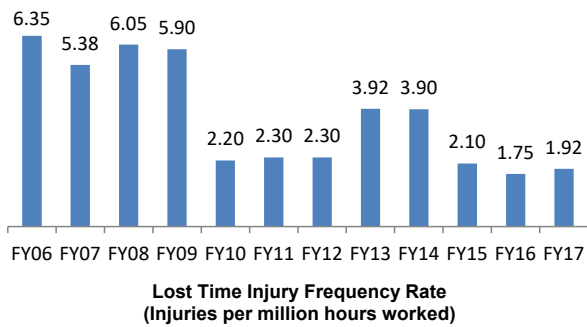
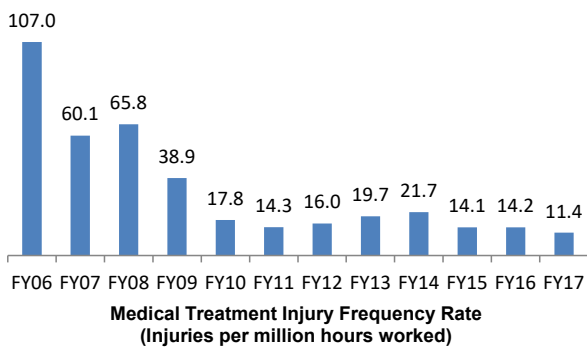
Safety is and must remain the most important value for everyone at Austal. To this end, we continue to develop our 'Zero Harm' approach to health and safety, underscoring Austal's commitment to customers, employees, regulators and the communities in which it operates.

Austal USA was awarded their 8th Safety Award from the Shipbuilders Council of America for Excellence in Safety in April 2017. Austal USA also saw a year on year (FY2017 versus FY2016) reduction of recordable injuries of just over 20%.

Austal USA's safety performance leads the industry and our current incident rate is less than half of the industry average.

We manage the risk of safety incidents by understanding those risks and driving a culture where safety is a core value. Whilst systems, procedures and people's behaviours are all important, it is a focus on building a sustainable safety culture across the business where every person looks after their own safety and the safety of others.

We have seen encouraging signs in our safety performance indicators over the course of this year, with trends remaining steady with FY2017 Lost Time Injury Frequency Rate at 1.92 injuries per million hours worked compared to our FY2016 result of 1.75.





**Goal  
Zero**

**Zero Harm. Zero Waste.**

**PLAN • DO • CHECK • ACT**

Our Zero Harm initiative was reinforced across operations in Australia with messages targeted to reduce accidents and injuries in the workplace.



## Directors' report

The Board of Directors of Austal Limited submit their report for the year ended 30 June 2017.

### Directors

The names and details of the Company's Directors in office during the financial year and until the date of this report are detailed below. Directors were in office for the entire financial year unless otherwise stated.

#### John Rothwell AO – Non-Executive Chairman



John has played a major role in the development of the Australian aluminium shipbuilding industry with over 40 years of experience in boat and shipbuilding. He is the architect responsible for the establishment of Austal and was the founding Managing Director. John identified markets for high speed ferries throughout Asia which resulted in Austal's rapid growth. He saw the potential for US Defense contracts for high speed aluminium naval ships and he led the formation of a new shipyard in Mobile, Alabama in 1998.

John was appointed as an Officer of the Order of Australia (AO) in January 2004 for services to the Australian shipbuilding industry, and for significant contributions to vocational education and training. He was named "Australian Entrepreneur of the Year" by Ernst and Young in 2002 and he was awarded the Western Australia Citizen of the Year in the category of Industry and Commerce in 1999.

John stepped down as Executive Chairman and Chief Executive Officer in 2008 to continue as Non-Executive Chairman after managing the Company for 20 years.

#### Jim McDowell – Independent Director



Jim brings strong industry background to Austal, with more than 30 years of experience in the defence and aerospace sectors. He was most recently Chief Executive Officer at BAE Systems Saudi Arabia operations. Jim was Chief Executive Officer at BAE Systems Australia prior to this, where he oversaw a significant expansion of its operations.

Jim joined BAE Systems in 1996 and held senior management positions prior to his CEO roles. Jim worked for 18 years at aerospace company Bombardier Shorts in legal, commercial, and marketing positions before commencing at BAE Systems.

Jim left BAE Systems Saudi Arabia in 2013 to return to Australia. He has taken a strong interest in the continuing education sector, and is currently Chairman of the Australian Nuclear Science and Technology Organisation. Jim is a Non-Executive Director at Codan Limited. Jim is Chancellor of the University of South Australia.

Jim holds a Bachelor of Laws from the University of Warwick in England.

## Giles Everist – Independent Director



Giles has a breadth of board and executive experience with a range of industrial and service based businesses gained over more than 27 years, working internationally in Australia, UK and Africa, largely in the resources, engineering and construction industries.

Giles was appointed as Non-Executive Director in November 2013 and Audit & Risk Committee Chair in November 2015. Giles holds a mechanical engineering degree and is a qualified chartered accountant. He was Chairman of ASX listed Decmil Group Limited between 2011 and 2014 and was formerly the Chief Financial Officer and Company Secretary of Monadelphous Group Limited between 2003 and 2009. He has held senior financial executive roles during his career with Rio Tinto in the United Kingdom and Australia, as well as major US design engineering group Fluor

Corporation.

Giles has held a number of other Non-Executive Director and Audit & Risk Committee Chair roles with ASX listed, private and not for profit organisations, and is currently a Non-Executive Director of Macmahon Holdings Limited and Norwood Systems.

## David Singleton – Chief Executive Officer



David has spent much of his career in the defence industry around the world in roles encompassing design, heavy manufacturing, customer support and international sales. He was a Non-Executive Director of Austal for four years before becoming CEO in April 2016.

David has held numerous senior roles with BAE Systems, one of the world's largest defence companies, including Group Head of Strategy and Mergers & Acquisitions in London from 1997 to 1998 and again in 2003.

David was the Chief Executive Officer of Alenia Marconi Systems (AMS) in the intervening years; a joint venture between BAE Systems and Finmeccanica that had turnover of circa €1.4 billion and employed 7,500 people across the UK, Italy, the USA and Germany. AMS was a European leader of naval warfare and air defence systems,

C4I (command, control, communications, computers and intelligence), ground and naval radars, naval command and control training systems and long term naval support.

David started his career with the UK Ministry of Defence with an Honours degree in Mechanical Engineering from University College London, and worked in research, development and manufacturing as well as senior management roles in Royal Ordnance, which was eventually sold to BAE. He has also served as a member of the National Defence Industries Council in the UK, and as a Board member and Vice President (Defence) of Intellect, a leading trade association for the UK technology industry.

Most recently, David was the CEO and Managing Director of Perth-based mining company Poseidon Nickel Limited. Prior to this role, he served as CEO and Managing Director of Clough Limited between 2003 and 2007.

## Interests in the shares and options of the company and related corporate bodies

The interests of the Directors in the shares of Austal Limited at the date of this report were as follows:

Director	Number		
	Ordinary Shares	Share Rights	Performance Rights
John Rothwell	32,807,692	-	-
Jim McDowell	33,751	-	-
Giles Everist	10,000	-	-
David Singleton	28,600	289,100	1,194,121

## Principal activities

The principal activities of entities within the consolidated entity during the year were the design, manufacture and support of high performance vessels. These activities are unchanged from the previous year.

## Results

The net profit after tax of the consolidated entity for the financial year was \$15.350 million after income tax (FY2016: net loss after tax of \$84.182 million).

## Review of operations

A review of the operations and financial position of the consolidated entity is outlined in the Review of Operations on page 9.

## Share price

The closing share price was \$1.83 for the year ended 30 June 2017 (Year ended 30 June 2016: \$1.21).

## Dividends

A dividend of 2 cents per share was paid after the FY2017 H1 results (FY2016 H1: 2 cents per share) and a further dividend of 2 cents per share has been proposed for FY2017 (FY2016 final: 2 cents per share).

## Significant events after the balance date

The Directors have declared a fully franked dividend of 2 cents per share in respect of the year ended 30 June 2017. More information is available in the Dividends section above.

## Likely developments and future results

A general discussion of the Group's outlook is included in the Chairman's Report on page 3 and the Review of Operations on page 9.

## Significant changes in the state of the affairs

There were no significant changes to structure or operations of the Group during the financial year.

## Environmental regulation and performance

The Group has a policy of at least complying with, but in most cases exceeding, environmental performance requirements. No environmental breaches have been notified by any Government agency during the year ended 30 June 2017.

## Share options and performance rights

There were 1,374,196 un-issued ordinary shares under options and 4,543,728 un-vested performance rights at year end. Refer to Note 30 for further details of the options outstanding. There were no options exercised during the year. There were 191,740 share rights granted as part of the CEO remuneration during FY2017.

## Indemnification and insurance of Directors and Officers

An indemnity agreement has been entered into between the parent entity and each of the Directors named in this report. The company has agreed to indemnify those Directors against any claim for any expenses or costs which may arise as a result of work performed in their respective capacities to the extent allowed by the law.

The parent entity paid premiums during the financial year in respect of a contract insuring the Directors and Officers of the Group in respect of liability resulting from these indemnities. The terms of the insurance arrangements and premiums payable are subject to a confidentiality clause.

## Indemnification of auditors

The parent entity has agreed to indemnify its auditors, Ernst & Young, against claims by third parties arising from the audit (for an unspecified amount) to the extent permitted by law, as part of the terms of its audit engagement agreement. No payment has been made to indemnify Ernst & Young during or since the financial year.

## Committee membership

The Company has an Audit & Risk Committee and a Nomination & Remuneration Committee of the Board of Directors.

Members acting on the committees of the Board during the year were:

### Audit & Risk

Jim McDowell  
Giles Everist <sup>1</sup>

### Nomination & Remuneration

Jim McDowell <sup>1</sup>  
Giles Everist  
John Rothwell

1. Designates the Chairman of the committee

## Directors' meetings

The number of meetings of Directors (including meetings of committees of Directors) held during the year and the number of meetings attended by each Director was as follows:

	Meeting		
	Board	Audit & Risk Committee	Nomination & Remuneration Committee
<b>Number of meetings held</b>	6	4	3
<b>Number of meetings attended:</b>			
John Rothwell	6	-	3
Jim McDowell	6	4	3
Giles Everist	6	4	3
David Singleton	6	4 <sup>1</sup>	3 <sup>1</sup>

1. Attended as a guest

## Rounding

The amounts contained in this report and in the financial report have been rounded to the nearest \$1,000 (where rounding is applicable) under the option available to the Company under ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191. The Company is an entity to which the instrument applies.



The new Cairns service centre opened in July 2017, to provide local support to the Australian Border Force and Royal Australian Navy Cape class fleets operating across Northern Australia.

The office is also preparing for the Cairns based sustainment of the new Guardian Patrol Boat fleet (under construction by Austal), to be gifted by Australia to 12 Pacific Islands from 2018.



## Message from the Nomination & Remuneration Committee (NRC)

Dear Shareholder,

We are pleased to present Austal's Remuneration Report for the year ending 30 June 2017.

Austal's remuneration framework, is designed to create value for all stakeholders, to differentiate rewards based on the Group and individual performance and to provide competitive rewards that attract, motivate and retain talented individuals. Similarly, the framework ensures a focus on achieving short term targets whilst ensuring critical positioning for the longer term success of the Company.

The NRC and Board have been successful in redesigning Austal's remuneration governance practices over the past three years. Future modifications are expected to be minor in nature as the NRC ensures the ongoing relevance and success of the structure that has been implemented.

The NRC will maintain an engagement with Godfrey Remuneration Group (GRG) for FY2018 to ensure that Austal maintains contemporary remuneration practices that support the strategic objectives of the business.

### New executive appointments

Austal has further strengthened the level of calibre within Executive Management with the appointment of new Management Personnel (KMP) during the year following the appointment of Mr David Singleton as Chief Executive Officer in April 2016.

Mr Patrick Gregg was appointed to the role of Chief Operating Officer in February 2017. Mr Patrick Gregg began his career with BAE Systems in the UK where his final position was Head of Project for the second of class hunter killer nuclear submarine, HMS Ambush. He left BAE Systems after delivering this project and joined Network Rail as Route Delivery Director for the Western and Wales region with responsibility for multi-million pound upgrades in rail infrastructure.

### Remuneration outcomes

Austal is committed to having remuneration outcomes that are aligned with performance and the creation of shareholder value. Specific incentive metrics have been selected to realise the Company's strategies, including the focus on becoming Australia's sovereign ship builder and extension of the US vessel programs.

Austal finished FY2017 with a strong return to profitability, fundamentally driven by stabilisation of the LCS program and continued strong profit generation from the EPF program, both in the USA. Total Shareholder Return for FY2017 was 54.5%.

The estimated vesting of STI and LTI for key management personnel (KMP) for the FY2017 year is:

- 72% of the maximum achievable STI
- Vesting of ~ 217,307 performance rights from the FY2014 and FY2015 LTI Grants which represents 30% of the maximum achievable.

### Changes to remuneration structures

The Nomination and Remuneration Committee has a strong focus on the relationship between business performance, risk management and remuneration, and regularly reviews the executive remuneration structure to ensure that it remains appropriate.

Austal's remuneration strategy is designed to motivate, attract and retain employees to deliver on the Company's strategic objectives, both on a short and long term basis. This includes ensuring a higher proportion is fundamentally aligned to shareholder returns. The strategy drives management accountability for the achievement of stretch targets for the business.

The Board of Directors has approved a change to the measure of Total Shareholder Return (TSR) for the FY2018 Long Term Incentive (LTI) Program. The indexed TSR (iTSR) metric will be replaced with relative TSR (rTSR) for future grants because the Board considers that it represents a more transparent and stronger basis for measuring and rewarding performance. Further details are provided within the Remuneration Report.

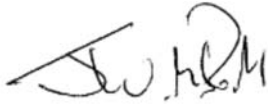
### Conclusion

It is hoped that shareholders will support the Remuneration report at the coming Annual General Meeting given the significant efforts of the Board to review and improve remuneration practices, to consult with stakeholders, and having demonstrated the improved alignment of incentives with external assessments of company performance.

We thank you for your feedback and continued support.

Yours sincerely,

Signature



Jim McDowell

Chairman, Nomination & Remuneration Committee



Austal's design team has hit a century, with our 100th designer joining the team in May 2017.

Austal now boasts the largest naval architecture and design team in Australia.

## Remuneration report (audited)

This Remuneration Report for the year ended 30 June 2017 outlines the remuneration arrangements of the Company and the Group in accordance with the requirements of the Corporations Act 2001 (the Act) and its regulations. This information has been audited as required by section 308(3C) of the Act.

The Remuneration Report is presented under the following sections:

1.	Persons covered by this report .....	21
2.	Remuneration governance framework and strategy .....	22
1.	Nomination & Remuneration Committee Charter .....	22
2.	Share Trading Policy .....	22
3.	Executive Remuneration Consultant Engagement Policy .....	22
4.	Remuneration framework .....	23
3.	Executive KMP remuneration policy .....	24
1.	Structure .....	24
2.	Base remuneration KMP .....	24
3.	Short Term Incentive (STI) Plan Policy .....	25
4.	Long Term Incentive (LTI) Plan Policy .....	28
4.	Non-Executive Director remuneration .....	31
1.	Application .....	31
2.	Remuneration structure .....	31
3.	Fees .....	31
4.	Termination benefits .....	31
5.	Remuneration of KMP .....	32
6.	Equity instruments held by KMP .....	34
1.	FY2014 Performance Rights Vesting .....	34
2.	FY2015 Performance Rights Vesting .....	36
3.	FY2016 Performance Rights Grant .....	38
4.	FY2017 Performance Rights Grant .....	39
5.	FY2018 Performance Rights Grant .....	40
6.	Share rights earned during the period .....	40
7.	Rights holdings .....	41
8.	Shareholdings .....	41
7.	Other related matters .....	42
1.	Board composition .....	42
2.	Details of contractual provisions for KMP .....	42
3.	Loans to KMP .....	42
4.	Other transactions with KMP .....	42
5.	Use of Independent remuneration consultants .....	43

## 1. Persons covered by this report

This report covers all Key Management Personnel (KMP) as defined in the Accounting Standards, including all Directors, as well as those Executives who have specific responsibility for planning, directing, and controlling material activities of the Group.

The KMP for the year ended 30 June 2017 were:

### Executive Director

Mr David Singleton                      Chief Executive Officer and Managing Director since April 2016

### Executives with no Director duties

Mr Greg Jason                              Group Chief Financial Officer since January 2013  
Mr Craig Perciavalle                      President USA since November 2012  
Mr Patrick Gregg                            Chief Operating Officer Australia and Philippines since February 2017

The following person ceased to be an executive KMP of Austal during FY2017:

Mr Joselito Turano                        President Philippines until July 2016

### Non-Executive Directors

Mr John Rothwell                         Chairman since 1998  
Member of the Nomination & Remuneration Committee since December 1998

Mr Jim McDowell                         Independent non-executive director since December 2014  
Chairman of the Nomination & Remuneration Committee since May 2016  
Member of the Audit & Risk Committee since February 2015

Mr Giles Everist                            Independent non-executive director since November 2013  
Chairman of the Audit & Risk Committee since October 2014  
Member of the Nomination & Remuneration Committee since February 2014

## 2. Remuneration governance framework and strategy

The following framework and strategy broadly outlines the principles and policies that the Board applies in overseeing KMP remuneration.

### 1. Nomination & Remuneration Committee Charter

The role and responsibilities of the committee are outlined in the Nomination & Remuneration Committee Charter (the Charter), which is available on the Austal website.

The role of the Nomination & Remuneration Committee (NRC) is to ensure that appropriate remuneration policies are in place which are designed to meet the needs of the Company and to enhance corporate and individual performance.

The Committee also oversees the implementation of the policies in setting remuneration and performance objectives related to the Short Term Incentive (STI) and Long Term Incentive (LTI) plans.

The remit of the Nomination & Remuneration Committee also includes succession planning which was reviewed by the Board again in FY2017.

The Charter specifies that the NRC is to be composed of at least three members with the majority being independent directors.

### 2. Share Trading Policy

The Share Trading Policy of Austal is available on the Austal website. The Policy contains the standard references to insider trading restrictions that are a legal requirement under the Corporations Act, as well as conditions associated with good corporate governance. The Policy specifies "Closed Periods" during which Directors and related parties, KMP, Senior Executives, and any employee in possession of inside information must not trade in the securities of the Company, unless written permission is provided by the Board following an assessment of the circumstances.

All equity based remuneration awards which have vested are subject to the Group's Share Trading Policy.

### 3. Executive Remuneration Consultant Engagement Policy

Austal has adopted an executive remuneration consultant (ERC) engagement policy which is intended to manage the interactions between the Company and the ERC. The policy is intended to ensure independence of advice and ensure that the NRC has clarity regarding the extent of any interactions between management and the ERC. This policy enables the Board to state with confidence that advice received has been independent. The policy states that ERC are to be approved and engaged by the Board before any advice is received and that such advice may only be provided to a non-executive director. Any interactions between management and the ERC must be approved and overseen by the Nomination & Remuneration Committee, this includes the collection of factual internal records (e.g. superannuation paid or allowances and benefits etc.).



#### 4. Remuneration framework

Austal is committed to responsible remuneration practices. The need to reward the Group's employees fairly and competitively based on performance needs to be balanced with the requirement to do so within the context of principled behaviour and action, particularly in the area of safety, risk, compliance and control.

Remuneration should contribute to the Group's achievements in a way that supports the Group's culture and goals. The Remuneration Policy Framework set out below summarises the key features of the Group's remuneration approach.

##### Our Vision:

Maintain a responsible, performance-based Remuneration Policy that is aligned with the long-term interests of our shareholders.

Certain incentive metrics are utilised on the Remuneration framework to capture the impact of the Group's strategy.

##### Our Goal:

Strike the right balance between meeting shareholders' expectations, paying our employees competitively, and responding appropriately to the regulatory environment.

##### Our Approach:

###### Governance

Clearly defined and documented governance procedure  
Independent NRC  
Independent ERC  
Annual assessment of Remuneration Policy

###### Individual Remuneration

Reward annual performance of Group relative to planned key performance indicators  
Business performance aligned  
Recognise and reward teamwork and development of the culture of the organisation  
Award and differentiate based on individual performance and contributions

###### Individual Remuneration Determination

Total remuneration based approach  
Facilitate competitiveness by paying remuneration levels for comparable roles and experience, subject to performance  
Promote meritocracy by recognising individual performance, with an emphasis on contribution, ethics and safety  
Equal remuneration opportunity

###### Remuneration Structure

Provide the appropriate balance of fixed and variable remuneration consistent with the position and role in the Group  
Significant portion of variable remuneration deferred and aligned with the long-term performance of the Group  
Promote ethical behaviour and do not create incentives to expose the Group to inappropriate risk

### 3. Executive KMP remuneration policy

#### 1. Structure

The following policy applies to executive KMP and executive directors:

- Total Remuneration Packages (TRP) should be composed of:
  - Base Package (inclusive of superannuation, allowances, social security, benefits and any applicable fringe benefits tax (FBT) as well as any salary sacrifice arrangements).
  - STI which provides a reward for performance against annual objectives.
  - LTI which provides an equity-based reward for performance against indicators of shareholder benefit or value creation, over a three year period.
- Internal TRP relativities and external market factors should be considered.
- TRP should be structured with reference to market practices and the particular circumstances of the Group where appropriate.

#### 2. Base remuneration KMP

##### i. Framework

- Base Packages should be set with reference to the market practice of ASX listed companies at the P50 level, where 50% of the comparator group are above the level and 50% are below this point in the data set.
- Total Remuneration Package (TRP) at Target bonus levels (being the Base Package plus incentive awards intended to be paid for targeted levels of performance) should be set in the P50 to P75 range of the relevant market practice to create a strong incentive to achieve targeted objectives in both the short and long term.
- Remuneration will be managed within a range to allow for the recognition of individual differences such as individual experience, knowledge or competency with which they fulfil a role (a range of +/- 20% is generally targeted in line with common market practices).

##### ii. Total Fixed Remuneration (TFR) – CEO effective from February 2016

The CEO's TFR is to be paid in cash, whilst the CEO and the Board may agree at the commencement of each year for up to 30% of TFR to be unconditionally (not subject to performance conditions since it is part of TFR) payable in share rights. The number of share rights will be based upon the volume weighted average closing price of Austal Limited shares in the last 5 trading days of each month.

Mr Singleton and the Board of Directors agreed that 30% of Mr Singleton's TFR would be paid in share rights for FY2017 and again in FY2018.

### 3. Short Term Incentive (STI) Plan Policy

The STI policy of the Group dictates that an annual component of the KMP executives' remuneration will be aligned to the individual business unit, and Company performance. The principles of the plan are that:

- STI should be aligned with clear and measurable targets which are set at the start of the financial year, and the targets will be aligned with the achievement of the company's business plan.
- The STI should be paid in cash.
- The STI should have a weighting in the remuneration mix that is no greater than the LTI to ensure an adequate balance in focus between short and long term objectives.
- STI payments will be determined after the end of the financial year and the full year accounts have been approved by the Board.
- STI payments are at the full discretion of the Board.

#### i. Purpose

The purpose of the STI Plan is to incentivise KMP, Senior Executives and Managers to deliver and outperform key performance indicators (KPI) and annual business plans that are challenging but achievable. This is intended to lead to sustainable superior returns for shareholders and to modulate the cost of employing KMP, Senior Executives and Managers such that the cost of employment reflects the performance of the company.

#### ii. Measurement Period

The measurement period for STI awards is aligned with the financial year of the Group.

#### iii. Key Performance Indicators (KPI)

KPI are customised for each KMP, Senior Executive and Manager and reflect the nature of their role, whilst creating shared objectives where appropriate.

Weightings are applied to the KPI selected for each participant to reflect the relative importance of each KPI.

Satisfaction of KPIs performance conditions are assessed qualitatively and quantitatively against the targets defined at the start of the financial year.

iv. **FY2017 Key Performance Indicators (KPI)**

KPI measures and weightings set for the KMP in FY2017 were as follows:

<b>David Singleton - CEO</b>	<b>Weight</b>
Group EBIT <sup>1</sup>	30%
Group Cashflow <sup>1</sup>	10%
Group New Vessel Orders	20%
- New EPF orders in USA <sup>1</sup>	
- Additional LCS appropriation in USA <sup>1</sup>	
- New commercial vessels to keep Austal Philippines at greater than 75% load	
Group Strategy Development & Execution	20%
- Down selection for the CoA, OPV contract as shipbuilder	
- US LCS program to plan	
- Increase value of support activities in USA & Australia defence	
Implementation of Business Improvement Initiatives	20%
- Achieve Key Defence Supplier status in Australia	
- Target and reduce procurement & shipbuilding costs by 3% to 5% respectively	
- Drive people development plan	
<b>Total</b>	<b>100%</b>

<b>Greg Jason - CFO</b>	<b>Weight</b>
Group EBIT <sup>1</sup>	30%
Group Cashflow <sup>1</sup>	10%
Group New Vessel Orders <sup>1</sup>	20%
Deliver IT strategy including digital shipyard transition	10%
Group Strategy Development & Execution	20%
Implementation of Business Improvement Initiatives	10%
<b>Total</b>	<b>100%</b>

<b>Craig Perciavalle - President USA</b>	<b>Weight</b>
USA financial performance	40%
USA New Vessel and support Orders	10%
Sign new EPF contracts <sup>1</sup>	10%
Increase support contracts <sup>1</sup>	10%
Down select additional LCS contracts <sup>1</sup>	10%
Implementation of Business Improvement Initiatives	20%
- LCS shipbuilding and profitability	
- Reduce vessel shipbuilding and procurement costs <sup>1</sup>	
<b>Total</b>	<b>100%</b>

<b>Patrick Gregg - COO Australia &amp; Philippines</b>	<b>Weight</b>
Group EBIT <sup>1</sup>	30%
Group Cashflow <sup>1</sup>	10%
Group New Vessel Orders <sup>1</sup>	20%
Implementation of Business Improvement Initiatives	40%
- Philippines productivity and cost efficiency	
- Australia productivity and cost efficiency	
- OPV implementation plan	
<b>Total</b>	<b>100%</b>

1. Figures not released due to commercial confidentiality.

v. **FY 2018 Key Performance Indicators (KPI)**

KPI measures and weightings set for the KMP in FY2018 are as follows:

<b>David Singleton - CEO</b>	<b>Weight</b>
Group EBIT <sup>1</sup>	30%
Group Cashflow <sup>1</sup>	10%
Group New Vessel Orders	20%
- New LCS orders in USA <sup>1</sup>	
Group Strategy Development & Execution	30%
- Down selection for the CoA OPV contract as shipbuilder	
- Design compelling frigate solution for USN based on LCS	
- Increase value of support activities in USA & Australia defence	
Implementation of Business Improvement Initiatives	10%
- Implement AP yard expansion	
- Meet 'Advanced Manufacturing' goals in Australia to drive down costs	
- LCS to targets or better <sup>1</sup>	
<b>Total</b>	<b>100%</b>

<b>Greg Jason - CFO</b>	<b>Weight</b>
Group EBIT <sup>1</sup>	30%
Group Cashflow <sup>1</sup>	10%
Group New Vessel Orders <sup>1</sup>	20%
Deliver IT strategy including digital shipyard transition	10%
Group Strategy Development & Execution	20%
Implementation of Business Improvement Initiatives	10%
<b>Total</b>	<b>100%</b>

<b>Craig Perciavalle - President USA</b>	<b>Weight</b>
USA financial performance <sup>1</sup>	40%
USA Cashflow <sup>1</sup>	10%
New orders including LCS 30 & EPF 13	10%
Progress LCS conversion to Frigate FFG(x)	10%
Implementation of Business Improvement Initiatives <sup>1</sup>	30%
- LCS cost and productivity performance	
- Safety target for total reportable incidents	
- Growth of Sustainment business	
<b>Total</b>	<b>100%</b>

<b>Patrick Gregg - COO Australia &amp; Philippines</b>	<b>Weight</b>
Group EBIT <sup>1</sup>	30%
Group Cashflow <sup>1</sup>	10%
Group New Vessel Orders <sup>1</sup>	20%
Implementation of Business Improvement Initiatives <sup>1</sup>	40%
- Philippines productivity and cost efficiency	
- Australia productivity and cost efficiency	
- OPV implementation upon successful award	
- Growth of Sustainment business	
<b>Total</b>	<b>100%</b>

1. Figures not released due to commercial confidentiality.

**vi. Determination of STI award**

The Board reviews and approves performance targets and objectives annually for the CEO and the executive management team. The final STI award is determined subsequent to year end, with the payment made in September of the following financial year.

The Board has the discretion to not grant STI performance awards in the event of standard Group performance, notwithstanding that individuals may have achieved their agreed performance targets. This demonstrates the Board’s commitment to aligning remuneration with the expectations and experience of shareholders.

**vii. Target and maximum STI award**

Target and maximum awards are applied to base remuneration.

Position	Incumbent	FY2017			FY2018	
		% of TFR			% of TFR	
		Target	Maximum	Estimated	Target	Maximum
Chief Executive Officer	Mr David Singleton	50%	100%	80%	50%	100%
Chief Financial Officer	Mr Greg Jason	30%	60%	48%	30%	60%
President USA	Mr Craig Perciavalle	25%	50%	33%	25%	50%
Chief Operating Officer	Mr Patrick Gregg	20%	40%	13%	30%	60%
President Philippines	Mr Joselito Turano <sup>1</sup>	-	-	-	-	-

1. Mr Joselito Turano forfeited his STI upon resignation on 13 July 2016

**4. Long Term Incentive (LTI) Plan Policy**

The long term incentive plan policy of the Company is for a component of annual remuneration of executives to be at-risk, payable in equity in the Company and based on an assessment of long term performance over not less than three years.

The board implemented a number changes in FY2016 after undertaking a review of the LTI plan. Those changes were described in the FY2015 Annual Report and they have been maintained in the FY2017 plan. The purpose of the changes was to ensure that the scheme continued to drive long term executive performance as well as meet normal industry practice.

**i. Purpose**

The purpose of the LTI Plan is to incentivise Senior Executives to deliver long term Group performance that will lead to sustainable superior returns for shareholders and to modulate the remuneration of Senior Executives relative to this performance.

**ii. Form of incentive**

The LTI should be based on Performance Rights that vest based on an assessment of performance against objectives. No dividends are payable or accrued on Performance Rights which are unvested.

**iii. Measurement period**

The standard measurement period has been three years from FY2017 onwards, however the Board has discretion to modify the duration of the measurement period if it deems an extension to be appropriate. An extension of the measurement period will only apply to measures that may be pro-rata increased in difficulty to take account of the additional time.



#### iv. Measures of long term performance

The Company uses two long term performance measures:

- Total Shareholder Return (TSR) which the Board believes best reflects an external measure of performance.
- Return on Invested Capital (ROIC) which the Board believes best reflects an internal measure of performance.

#### v. Total Shareholder Return Measure (TSR)

The Board believes that TSR is the measure that has the strongest alignment with shareholders. Absolute TSR can be influenced by macro-economic factors that are not specific to the Austal Group, and therefore the FY2016 & FY2017 LTI grants were offered to executives based on Indexed TSR (iTSR).

iTSR determines the shareholders returns of Austal relative to a market index rather than capturing the absolute performance of the Group. Setting an appropriate iTSR performance level (e.g. 200% stretch in FY2016 & FY2017 grants) is inherently difficult because of the focus on a single market average rather than the breadth of market results.

The Board assessed a peer group of companies that include TSR within their LTI schemes and greater than 90% of companies in the peer group utilise Relative TSR (rTSR) which sets performance hurdles in reference to percentiles of TSR for stocks included in the All Ordinaries Total Return Index (XAOA).

The Board has resolved to adopt rTSR for all LTI grants from FY2018 because rTSR is considered to represent a more transparent and understandable basis for measuring performance which is therefore easier to articulate and explain to beneficiaries and shareholders. Achieving company TSR that is below the 50th percentile of the market is considered to be substandard whilst delivering a TSR that is in the top quartile is clearly strong performance that should be rewarded.

#### vi. Return on Invested Capital Measure (ROIC)

Senior Executives are faced with significant and long term business development and project based challenges. Therefore, the LTI is also linked to the achievement of ROIC growth objectives that will lead to value creation for shareholders. This measure is considered to be the best measure of long term performance from an internal perspective by recognising the long term nature of investment in fixed assets necessary in a shipbuilding business.

ROIC is calculated by dividing the Net operating profit after tax by Net Assets (excluding Cash, Debt, Derivatives and Tax accounts).

Actual ROIC results are compared against internal targets set by the Board.

## vii. Vesting of Performance Rights

The Performance Rights for each employee vest at the end of the measurement period, subject to meeting the performance hurdles, unless the Board exercises its discretion to extend the original measurement period and the difficulty of hurdles.

Participants are not required to make any payments in respect of Performance Rights at grant or at vesting.

## viii. Holding period

A one year holding period applies to all shares awarded as a result of LTI performance rights vesting. Recipients are prevented from selling their shares during this period. This effectively extends the incentive period to four years and increases the accumulation of equity by executives to strengthen their alignment with shareholders.

## ix. Reduction or cancellation

The LTI Plan Rules give the Board broad discretion to amend either the Plan Rules or the terms of an offer made to an executive in order to correct errors (such as errors in the financial statements on which an allocation of Performance Rights was made) or for other legal purposes. The Board may also determine that a Participant's entitlement to Performance Rights is forfeited or reduced under the Plan Rules, in the event of serious misconduct, fraudulent behaviour or dishonesty. The Board also considers the 1 year holding period discussed above (in addition to the 3 year Performance Period) provides an additional safeguard against participants benefiting unjustly from financial misstatements or misconduct.

## x. Target and maximum award

Target and maximum LTI awards are applied to base remuneration, valued at their grant calculation date.

Position	Incumbent	FY2017 Grant Vesting		FY2018 Grant Vesting	
		Target	Maximum	Target	Maximum
CEO	Mr David Singleton	50%	100%	50%	100%
Chief Financial Officer	Mr Greg Jason	35%	70%	35%	70%
President USA	Mr Craig Perciavalle	35%	70%	35%	70%
Chief Operating Officer	Mr Patrick Gregg	0%	0%	35%	70%
President Philippines	Mr Joselito Turano <sup>1</sup>	-	-	-	-

1. Mr Joselito Turano resigned effective 13 July 2016

## 4. Non-Executive Director remuneration

### 1. Application

The Non-executive Director Remuneration Policy applies to non-executive directors (NED) of the Company in their capacity as directors and as members of committees.

### 2. Remuneration structure

Remuneration is composed of:

- Board fees
- Committee fees

Both fee types include superannuation to the extent applicable to the incumbent.

### 3. Fees

#### i. Fee cap

The Remuneration for Non-Executive Directors will be managed within the aggregate fee limit (AFL) of \$3,000,000 approved by shareholders of the Company. The cap has remained unchanged since listing on the Australian Securities Exchange (ASX) in 1998.

#### ii. Chairman

Remuneration for the current Chairman of the Board reflects his continued high level of contribution to the company and the Board. The fee level is reviewed every year, and the Board decided to set the remuneration fee at \$200,000 per annum during FY2017.

#### iii. Non-executive director fees

Board fees paid for membership of the Board, inclusive of superannuation and exclusive of committee fees have been set with reference to the 50th percentile of the market of comparable ASX listed companies (as previously described for executive remuneration). No changes to Non-executive Director fees are planned for FY2018.

#### iv. Committee fees

Committee fees recognise additional contributions to the work of the Board by members of committees. They are similarly referenced to the benchmark group as above.

### 4. Termination benefits

Termination benefits are not paid to NED by the Company.

## 5. Remuneration of KMP

Year ended 30 June 2017

	Short-Term Benefits			Post Employment Benefits	Long Term Benefits	Share Based Payments Expense			Total	% Share Based Payments Expense	% Performance Related	STI	
	Salary & Fees	FY2017 STI Accrued	Other Monetary Benefits	Super- annuation / Social Security	Leave Accrued	Termination Benefits	Fixed	Long Term Incentive				FY2016 STI Paid <sup>3</sup>	FY2017 Unpaid STI
<b>Non-executive directors</b>													
John Rothwell	\$ 185,540	\$ -	\$ -	\$ 14,460	\$ -	\$ -	\$ -	\$ -	\$ 200,000	-	-	\$ -	\$ -
Giles Everist	114,529	-	-	7,971	-	-	-	-	122,500	-	-	-	-
Jim McDowell	112,192	-	-	7,808	-	-	-	-	120,000	-	-	-	-
<b>Executive directors</b>													
David Singleton	\$ 650,885	\$ 841,072	\$ -	\$ 35,000	\$ 46,302	\$ -	\$ 324,234	\$ 200,509	\$ 2,098,002	25.0	49.6	\$ -	\$ 841,072
<b>Other key management personnel</b>													
Greg Jason	\$ 364,649	\$ 198,969	\$ -	\$ 19,308	\$ 40,760	\$ -	\$ -	\$ 101,380	\$ 725,066	14.0	41.4	\$ -	\$ 198,969
Craig Perciavalle	629,556	204,606	21,011	80,402	-	-	-	149,795	1,085,370	13.8	32.7	-	204,606
Patrick Gregg <sup>1</sup>	162,066	59,178	-	7,617	12,746	-	-	-	241,607	-	24.5	-	59,178
Joselito Turano <sup>2</sup>	14,673	-	1,394	-	1,019	94,795	-	(20,759)	91,122	(22.8)	(22.8)	-	-
	<u>\$ 2,234,090</u>	<u>\$ 1,303,825</u>	<u>\$ 22,405</u>	<u>\$ 172,566</u>	<u>\$ 100,827</u>	<u>\$ 94,795</u>	<u>\$ 324,234</u>	<u>\$ 430,925</u>	<u>\$ 4,683,667</u>			<u>\$ -</u>	<u>\$ 1,303,825</u>

1 Mr Patrick Gregg was appointed Chief Operating Officer on 24 February 2017.

2 Mr Joselito Turano resigned on 13 July 2016

3 Final STI paid is based on whether the KMP is still in employment at the end of the financial year, and have met their respective KPIs

Year ended 30 June 2016

	Short-Term Benefits			Post Employment Benefits	Long Term Benefits	Share Based Payments Expense				Total	% Share Based Payments Expense	% Performance related	STI	
	Salary & Fees	FY2016 STI Accrued	Other Monetary Benefits	Super- annuation / Social Security	Leave Accrued	Termination Benefits	Fixed	Long Term Incentive				FY2015 STI Paid <sup>5</sup>	FY2016 Unpaid STI	
<b>Non-executive directors</b>														
John Rothwell	\$ 250,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 250,000	-	-	-	-
Giles Everist	122,500	-	-	-	-	-	-	-	-	122,500	-	-	-	-
Jim McDowell	107,500	-	-	-	-	-	-	-	-	107,500	-	-	-	-
<b>Executive directors</b>														
David Singleton <sup>1</sup>	\$ 327,333	\$ -	\$ -	\$ 13,712	\$ 27,387	\$ -	\$ 108,070	\$ 86,628		\$ 563,130	34.6	15.4	\$ -	\$ -
Andrew Bellamy <sup>2</sup>	798,176	-	-	19,308	74,725	697,160	-	(44,005)		1,545,364	(2.8)	(2.8)	363,922	-
<b>Other key management personnel</b>														
Greg Jason	\$ 364,091	\$ -	\$ -	\$ 19,308	\$ 41,356	\$ -	\$ -	\$ 50,682		\$ 475,437	10.7	10.7	\$ 96,451	\$ -
Craig Perciavalle	639,662	-	27,451	83,294	-	-	-	84,207		834,614	10.1	10.1	32,239	-
Brian Leathers <sup>3</sup>	319,010	-	27,946	50,715	-	141,969	-	(11,099)		528,541	(2.1)	(2.1)	15,582	-
Joselito Turano <sup>4</sup>	287,107	-	31,211	5,091	-	-	-	32,274		355,683	9.1	9.1	-	-
	<u>\$ 3,215,379</u>	<u>\$ -</u>	<u>\$ 86,608</u>	<u>\$ 191,428</u>	<u>\$ 143,468</u>	<u>\$ 839,129</u>	<u>\$ 108,070</u>	<u>\$ 198,687</u>		<u>\$ 4,782,769</u>			<u>\$ 508,194</u>	<u>\$ -</u>

1 Mr David Singleton was appointed Chief Executive Officer on 4 April 2016. Salary & Fees include Non-executive Directors fees paid up until 4 April 2016

2 Mr Andrew Bellamy resigned on 4 April 2016

3 Mr Brian Leathers resigned on 11 March 2016

4 Mr Joselito Turano resigned on 13 July 2016

5 Final STI paid is based on whether the KMP is still in employment at the end of the financial year, and have met their respective KPIs

## 6. Equity instruments held by KMP

### 1. FY2014 Performance Rights Vesting

#### i. FY2014 Performance Rights Grant

147,013 performance rights were granted to KMP in FY2014, who were still employed by Austal and remain unvested at 30 June 2017.

Mr Joselito Turano forfeited 46,760 performance rights upon resignation in FY2017.

#### ii. Measurement Periods

There were two measurement periods for the performance rights granted in FY2014 as outlined in the LTI transition plan that was depicted in the FY2014 Annual Report:

- 1 July 2013 – 30 June 2015 for 50% of the Performance Rights
- 1 July 2013 – 30 June 2016 for 50% of the Performance Rights

The Board decided to extend the measurement period of performance rights due to vest at 30 June 2016 by one year after FY2016 year end. The decision was taken due to the trading halt that was initiated on 30 June 2016 pending the release of the FY2016 earnings guidance, and the subsequent reduction in share price on 4 July 2016 which was outside of the original measurement period. The vesting criteria for the performance rights have been adjusted pro-rata for the one year extension in the measurement period. No further extensions to the validity of these rights will be considered.

The Group used a Monte Carlo model to value the extension of the performance rights:

<b>Monte Carlo simulation method assumptions:</b>	<b>Measurement Period 2</b>		
Discount Rate	1.4% p.a.		
Share Price Volatility	45% p.a.		
Grant Date	1 September 2016		
Expected life of option (years)	1		
<b>Summarised results based on performance conditions:</b>	<b>TSR</b>	<b>ROIC</b>	<b>Total</b>
Number of performance rights issued to all participants	74,901	174,768	249,669
Fair value per performance right - with vesting conditions	\$ 1.26		
Fair value per performance right - without vesting conditions		\$ 1.43	
Share price at grant date	\$ 1.45	\$ 1.45	\$ 1.45
Total value of performance rights	\$ 94,375	\$ 249,918	\$ 344,294
Number of performance rights expected to vest <sup>1</sup>	74,901	-	74,901
Total value of performance rights expected to vest	\$ 94,375	\$ -	\$ 94,375

1. There was no prospect of ROIC rights vesting because of the magnitude of the Group EBIT loss in FY2016.



### iii. FY2014 Grant Performance Criteria

The revised ROIC and TSR performance criteria relating to the FY2014 grant of performance rights to KMP are detailed below.

<u>Measure</u>	<u>Weight</u>	<u>Threshold</u>	<u>Vesting %</u>	<u>Performance</u>
<b>Austal</b>	30%	<= 20.5%	0%	At or below Threshold
<b>Absolute TSR</b>			Pro-rata	
<b>(CAGR)</b>		27.5%	50%	Target
			Pro-rata	
		>= 34.7%	100%	Stretch or Above
<hr/>				
<b>ROIC</b>	70%	6.0%	0%	At or below Threshold
			Pro-rata	
		8.0%	50%	Target
			Pro-rata	
		10.0%	100%	Stretch or Above
<hr/>				
<b>Total</b>	100%			

### iv. Vesting of Performance Rights from the FY2014 Grant

The actual TSR performance for the extended measurement period from 1 July 2013 – 30 June 2017 was calculated to be 186% which exceeds the stretch target.

The actual ROIC performance for the measurement period from 1 July 2013 – 30 June 2017 vesting of performance will be calculated using the FY2017 audited accounts. The estimated ROIC performance for the measurement period from 1 July 2013 – 30 June 2017 is 3.5% which will not meet the minimum threshold for award.

		Measurement Period 2						
		Rights Granted	Forfeiture		Estimated Vesting			
			Resigned	Lapsed <sup>2</sup>	ROIC	TSR	Total	
<b>Estimated Result</b>					3%	186%		
<b>Weight</b>					70%	30%	100%	
<b>Award</b>					-	100%	30%	
<b>Vesting %</b>					-	30%	30%	
<b>Employee</b>								
	Greg Jason	Chief Financial Officer	62,674	-	(43,872)	-	18,802	18,802
	Craig Perciavalle	President USA	84,339	-	(59,038)	-	25,301	25,301
	Joselito Turano <sup>1</sup>	President Philippines	46,760	(46,760)	-	-	-	-
	<b>Total</b>		<b>193,773</b>	<b>(46,760)</b>	<b>(102,910)</b>	<b>-</b>	<b>44,103</b>	<b>44,103</b>

1. Mr Joselito Turano resigned on 13 July 2016 and forfeited all of his performance rights
2. Did not meet vesting performance criteria

## 2. FY2015 Performance Rights Vesting

### i. FY2015 Performance Rights Grant

251,980 performance rights were granted to KMP in FY2015, who were still employed by Austal and remain unvested at 30 June 2017.

Mr Joselito Turano forfeited 73,130 performance rights upon resignation in FY2017.

### ii. Measurement Periods

There were two measurement periods for the performance rights granted in FY2015 as outlined in the LTI transition plan that was depicted in the FY2014 Annual Report:

- 1 July 2014 – 30 June 2016 for 25% of the Performance Rights
- 1 July 2014 – 30 June 2017 for 75% of the Performance Rights

The Board decided to extend the measurement period of performance rights due to vest at 30 June 2016 by one year post FY2016 year end. The decision was taken due to the trading halt that was initiated on 30 June 2016 pending the release of the FY2016 earnings guidance, and the subsequent reduction in share price on 4 July 2016 which was outside of the original measurement period. The vesting criteria for the performance rights have been adjusted pro-rata for the one year extension in the measurement period. No further extensions to the validity of these rights will be considered.

The Group used a Monte Carlo model to value the extension of the performance rights:

		Measurement Period 1		
<b>Monte Carlo simulation method assumptions:</b>				
Discount Rate		1.4% p.a.		
Share Price Volatility		45% p.a.		
Grant Date		1 September 2016		
Expected life of option (years)		1		
<b>Summarised results based on performance conditions:</b>				
		<b>TSR</b>	<b>ROIC</b>	<b>Total</b>
Number of performance rights issued to all participants		35,603	83,074	118,677
Fair value per performance right - with vesting conditions	\$	1.10		
Fair value per performance right - without vesting conditions			\$ 1.43	
Share price at grant date	\$	1.45	\$ 1.45	\$ 1.45
Total value of performance rights	\$	39,163	\$ 118,796	\$ 157,959
Number of performance rights expected to vest <sup>1</sup>		35,603	-	35,603
Total value of performance rights expected to vest	\$	39,163	\$ -	\$ 39,163

1. There was no prospect of ROIC rights vesting because of the magnitude of the Group EBIT loss in FY2016.

### iii. FY2015 Grant Performance Criteria

The ROIC and TSR performance criteria relating to the FY2015 grant of performance rights to KMP are detailed below.

Measure	Weight	Threshold	Vesting %	Performance
<b>Austal Absolute TSR (CAGR)</b>	30%	<= 15%	0%	At or below Threshold
			Pro-rata	
		20%	50%	Target
		>= 25%	100%	Stretch or Above
<b>ROIC</b>	70%	6.9%	0%	At or below Threshold
			Pro-rata	
		7.8%	50%	Target
		8.8%	100%	Stretch or Above
<b>Total</b>	100%			

### iv. Vesting of Performance Rights from the FY2015 Grant

The actual TSR performance for the extended measurement period from 1 July 2014 – 30 June 2017 was calculated to be 82% which exceeds the stretch target.

The actual ROIC performance for the measurement period from 1 July 2014 – 30 June 2017 vesting of performance will be calculated using the FY2017 audited accounts. The estimated ROIC performance in the measurement period from 1 July 2014 – 30 June 2017 is 1.6% which will not meet the minimum threshold for award.

		Measurement Periods 1 & 2						
	Rights Granted	Forfeiture		Estimated Vesting				
		Resigned	Lapsed <sup>2</sup>	ROIC	TSR	Total		
<b>Actual Result</b>				2%	82%			
<b>Weight</b>				70%	30%	100%		
<b>Award</b>				-	100%	30%		
<b>Vesting %</b>				-	30%	30%		
<b>Employee</b>								
	Greg Jason	Chief Financial Officer	109,288	-	(76,502)	-	32,786	32,786
	Craig Perciavalle	President USA	142,692	-	(99,885)	-	42,807	42,807
	Joselito Turano <sup>1</sup>	President Philippines	73,130	(73,130)	-	-	-	-
	<b>Total</b>		<b>325,110</b>	<b>(73,130)</b>	<b>(176,387)</b>	<b>-</b>	<b>75,593</b>	<b>75,593</b>

1. Mr Joselito Turano resigned on 13 July 2016 and forfeited all of his performance rights

2. Did not meet vesting performance criteria

### 3. FY2016 Performance Rights Grant

#### i. FY2016 Performance Rights Grant

385,455 performance rights were granted to KMP in FY2016, who were still employed by Austal and remain unvested at 30 June 2017.

Mr Joselito Turano forfeited 61,921 performance rights upon resignation in FY2017.

#### ii. Measurement Periods

100% of the performance rights granted in FY2016 have a 3 year measurement period from 1 July 2015 – 30 June 2018.

#### iii. FY2016 Grant Performance Criteria

The ROIC and iTSR performance criteria relating to the FY2016 grant of performance rights to KMP are detailed below.

<b>Measure</b>	<b>Weight</b>	<b>Threshold<sup>1</sup></b>	<b>Vesting %</b>	<b>Performance</b>
<b>Indexed TSR</b>	40%	<= 100%	0%	At or below Threshold
		100% < iTSR < 200%	Pro-rata 50%	Target
		>= 200%	Pro-rata 100%	Stretch or Above
<b>ROIC</b>	60%	<= 8.0%	0%	At or below Threshold
		10.0%	Pro-rata 50%	Target
		>= 12.0%	Pro-rata 100%	Stretch or Above
<b>Total</b>	100%			

1. 100% is equal to the TSR of the All Ordinaries Total Return Index (XAOA).

#### 4. FY2017 Performance Rights Grant

Performance rights granted to KMP in FY2017 are depicted in the table below.

Name	Grant date	Rights granted	Fair value per right		Value at grant date
			TSR	ROIC	
David Singleton	28 Oct 2016	1,194,121	\$ 1.11	\$ 1.45	\$ 1,049,632
Greg Jason	1 Sep 2016	262,887	0.97	1.37	210,047
Craig Perciavalle	1 Sep 2016	402,621	0.97	1.37	321,694
Total		<u>1,859,629</u>			<u>\$ 1,581,373</u>

##### i. FY2017 Grant Performance Criteria

The ROIC and iTSR performance criteria relating to the prospective FY2017 grant of performance rights to KMP are detailed below.

Measure	Weight	Threshold <sup>1</sup>	Vesting %	Performance
Indexed TSR	40%	<= 100%	0%	At or below Threshold
			Pro-rata	
		100% < iTSR < 200%	50%	Target
			Pro-rata	
>= 200%	100%	Stretch or Above		
ROIC	60%	< 6.6%	0%	At or below Threshold
			Pro-rata	
		6.6%	25%	Threshold
		7.4%	50%	Target
		Pro-rata		
> 8.3%	100%	Stretch or Above		
<b>Total</b>	<b>100%</b>			

1. 100% is equal to the TSR of the All Ordinaries Total Return Index (XAOA).

##### ii. Measurement Period

100% of the performance rights granted in FY2017 have a 3 year measurement period from 1 July 2016 – 30 June 2019.

## 5. FY2018 Performance Rights Grant

### i. FY2018 Grant Performance Criteria

The ROIC and rTSR performance criteria relating to the prospective FY2018 grant of performance rights to KMP are detailed below.

<u>Measure</u>	<u>Weight</u>	<u>Threshold</u>	<u>Vesting %</u>	<u>Performance</u>
<b>Relative TSR<sup>1</sup></b>	40%	< 50th percentile	0%	Below Threshold
		= 50th percentile	50%	Threshold
		>= 75th percentile	100%	Stretch or Above
<b>ROIC</b>	60%	< 6.6%	0%	At or below Threshold
			Pro-rata	
		6.6%	25%	Threshold
			Pro-rata	
		7.4%	50%	Target
			Pro-rata	
		> 8.3%	100%	Stretch or Above
<b>Total</b>	100%			

1. Percentile for TSR of stocks listed included in the All Ordinaries Total Return Index (XAOA).

### ii. Measurement Period

100% of the performance rights granted in FY2018 will have a 3 year measurement period from 1 July 2017 – 30 June 2020.

## 6. Share rights earned during the period

Details of share rights provided as fixed remuneration to key management personnel are shown below.

Further information is set out in Note 30. These share rights are in lieu of TFR normally paid in cash and are not a bonus nor performance based (i.e. on a salary sacrifice basis). The share rights were approved by shareholders during the 2016 Annual General Meeting.

<u>Name</u>	<u>Period earned</u>	<u>Measurement date</u>	<u>Earned</u>	<u>Fair value per right</u>	<u>Fair value</u>
David Singleton	FY2017	28 Oct 2016	191,740	\$ 1.53	\$ 293,362



## 7. Rights holdings

	Balance at 30 June 2016	FY2017 Movements				Balance at 30 June 2017	Vested and	
		Granted	Forfeited	Expired	Exercised		Exercisable	Unvested
<b>Directors</b>								
David Singleton								
Share Rights	97,360	191,740	-	-	-	289,100	289,100	-
Performance Rights	-	1,194,121	-	-	-	1,194,121	-	1,194,121
<b>Executives</b>								
Greg Jason								
Performance Rights	324,206	262,887	-	-	-	587,093	-	587,093
Craig Perciavalle								
Performance Rights	460,242	402,621	-	-	-	862,863	-	862,863
Patrick Gregg								
Performance Rights	-	-	-	-	-	-	-	-
Joselito Turano <sup>1</sup>								
Performance Rights	181,811	-	(181,811)	-	-	-	-	-

<sup>1</sup> Mr Joselito Turano resigned on 13 July 2016

## 8. Shareholdings

	Balance at 30 June 2016	FY2017 Movements				Balance at 30 June 2017
		Share Rights Exercised	Performance Rights Vested	Acquired / (Disposed)	No longer KMP	
<b>Non - Executive Directors</b>						
John Rothwell	32,500,745	-	-	306,947	-	32,807,692
Jim McDowell	33,751	-	-	-	-	33,751
Giles Everist	10,000	-	-	-	-	10,000
<b>Executives</b>						
David Singleton	28,600	-	-	-	-	28,600
Greg Jason	62,671	-	-	(29,226)	-	33,445
Craig Perciavalle	84,336	-	-	-	-	84,336
Patrick Gregg	-	-	-	-	-	-
<b>Total</b>	<b>32,720,103</b>	<b>-</b>	<b>-</b>	<b>277,721</b>	<b>-</b>	<b>32,997,824</b>

None of the shares held by key management personnel are held nominally.

## 7. Other related matters

### 1. Board composition

The Nomination & Remuneration Committee reviews the structure, size and composition of the Board annually, taking inputs from investors and other independent advisors received during the year into account. The NRC has recommended that the current practice of maintaining three independent Non-Executive Directors on the Board should remain following the FY2017 review.

The Committee also undertook an annual review of the position of Chairman at Austal, in part because he is now aged over 70 years. The Board (excluding the Chairman) unanimously agreed that the Chairman's intimate knowledge of the shipbuilding industry, of Austal and its major customers, together with his demonstrated high level of commitment, meant that he remains a significant asset to the Group and he was requested to remain as Chairman, to which he has agreed.

### 2. Details of contractual provisions for KMP

Name	Employing company	Contract Duration	Termination Notice Period	
			Group	Individual
David Singleton	Austal Limited	Unlimited	3 months	3 months
Greg Jason	Austal Limited	Unlimited	12 weeks	12 weeks
Craig Perciavalle	Austal USA LLC	Unlimited	0 months	0 months
Patrick Gregg	Austal Limited	Unlimited	3 months	3 months

Austal may choose to terminate the contract immediately by making a payment equal to the Group Notice Period fixed remuneration in lieu of notice. Executives are not entitled to this termination payment in the event of termination for serious misconduct or other nominated circumstances.

Executives will be entitled to the payment of any fixed remuneration calculated up to the termination date, any leave entitlement accrued at the termination date and any payment or award permitted under the remuneration policy upon termination of employment.

### 3. Loans to KMP

There were no loans to Directors nor other key management personnel at any time during the year ended 30 June 2017.

### 4. Other transactions with KMP

There were no transactions involving key management personnel other than compensation and transactions concerning shares and performance rights as discussed in other sections of the Remuneration Report.

## 5. Use of Independent remuneration consultants

The Company established policies and procedures governing engagements with external remuneration consultants to ensure that KMP remuneration recommendations were free from undue influence from the KMP to whom they relate.

Godfrey Remuneration Group (GRG) were engaged by the NRC during FY2017 to conduct an analysis of TSR metrics utilised in long term incentive plans. GRG did not provide a specific recommendation however the NRC and Board utilised the data to inform the decision to change from indexed TSR (iTSR) to relative TSR (rTSR).

GRC was remunerated \$26,470 for services provided during the period FY2017.

End of Remuneration Report



2 Go Super Cat ferries built at Austal Philippines and delivered June 2017

## Auditor independence

The Directors received the following declaration from the auditor of Austal Limited.



Ernst & Young  
11 Mounts Bay Road  
Perth WA 6000 Australia  
GPO Box M939 Perth WA 6843

Tel: +61 8 9429 2222  
Fax: +61 8 9429 2436  
ey.com/au

### Auditor's Independence Declaration to the Directors of Austal Limited

As lead auditor for the audit of Austal Limited for financial year ended 30 June 2017, I declare to the best of my knowledge and belief, there have been:

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

This declaration is in respect of Austal Limited and the entities it controlled during the financial period.

Ernst & Young

Robert A Kirkby

Partner

25 August 2017

A member firm of Ernst & Young Global Limited  
Liability limited by a scheme approved under Professional Standards Legislation

## Consolidated statement of profit or loss and other comprehensive income for the year ended 30 June 2017

	Notes	2017 '000	2016 '000
<b>Continuing operations</b>			
Revenue	4	\$ 1,310,128	\$ 1,339,970
Cost of sales		(1,192,969)	(1,396,921)
<b>Gross Profit</b>		<b>\$ 117,159</b>	<b>\$ (56,951)</b>
Other income and expenses	5	\$ 2,356	\$ 13,289
Administration expenses		(55,850)	(61,488)
Marketing expenses		(16,493)	(14,609)
Finance costs	5	(7,198)	(6,605)
Share of profit / (loss) from joint venture	27	(109)	-
<b>Profit / (loss) before income tax</b>		<b>\$ 39,865</b>	<b>\$ (126,364)</b>
Income tax benefit / (expense)	9	\$ (24,515)	\$ 42,182
<b>Profit / (loss) after tax</b>		<b>\$ 15,350</b>	<b>\$ (84,182)</b>
<b>Profit attributable to:</b>			
Owners of the parent		\$ 15,350	\$ (84,281)
Non-controlling interests		-	99
Total		<b>\$ 15,350</b>	<b>\$ (84,182)</b>
<b>Other comprehensive income (OCI)</b>			
<b>Amounts that may subsequently be reclassified to profit and loss:</b>			
Cash flow hedges			
- Gain / (loss) taken to equity		\$ 8,639	\$ 2,829
- (Gain) / loss recycled out of equity		2,010	13,789
- Income tax benefit / (expense)		(4,482)	(3,800)
- Net		<b>\$ 6,167</b>	<b>\$ 12,818</b>
Foreign currency translations			
- Gain / (loss) taken to equity		\$ (11,073)	\$ 14,323
- Income tax benefit / (expense)		-	(21)
- Net		<b>\$ (11,073)</b>	<b>\$ 14,302</b>
<b>Other comprehensive income not to be reclassified to profit and loss in subsequent periods</b>			
Asset Revaluation Reserve			
- Gain taken to equity		\$ -	\$ 29,667
- Income tax expense		-	(10,710)
- Net		<b>\$ -</b>	<b>\$ 18,957</b>
<b>Other comprehensive income net of tax for the period</b>		<b>\$ (4,906)</b>	<b>\$ 46,077</b>
<b>Total comprehensive income for the year</b>		<b>\$ 10,444</b>	<b>\$ (38,105)</b>
<b>Total comprehensive income attributable to:</b>			
Owners of the parent		\$ 10,444	\$ (38,204)
Non-controlling interests		-	99
Total		<b>\$ 10,444</b>	<b>\$ (38,105)</b>
<b>Earnings per share (\$ per share)</b>			
- basic for profit for the year attributable to ordinary equity holders of the parent	6	\$ 0.044	\$ (0.242)
- diluted for profit for the year attributable to ordinary equity holders of the parent	6	0.044	(0.242)

The consolidated statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.

## Consolidated statement of financial position as at 30 June 2017

	Notes	2017 '000	2016 '000
<b>Assets</b>			
<b>Current</b>			
Cash and cash equivalents	10	\$ 150,471	\$ 224,318
Trade and other receivables	14	100,444	128,340
Inventories	16	170,422	108,974
Prepayments		6,077	5,408
Derivatives	22	1,051	147
Assets held for sale		2,529	2,908
Income tax refundable	9	706	-
<b>Total</b>		<b>\$ 431,700</b>	<b>\$ 470,095</b>
<b>Non - Current</b>			
Other financial assets	20	\$ 9,626	\$ 7,638
Investment in joint venture	27	1,847	-
Derivatives	22	1,985	340
Property, plant and equipment	18	500,304	490,798
Intangible assets and goodwill	19	8,909	9,296
Deferred tax assets	9	5,630	34,959
<b>Total</b>		<b>\$ 528,301</b>	<b>\$ 543,031</b>
<b>Total</b>		<b>\$ 960,001</b>	<b>\$ 1,013,126</b>
<b>Liabilities</b>			
<b>Current</b>			
Trade and other payables	17	\$ (154,914)	\$ (229,774)
Derivatives	22	(4,052)	(10,690)
Interest bearing loans and borrowings	11	(9,868)	(2,545)
Provisions	21	(46,586)	(42,291)
Deferred grant income	13	(7,934)	(8,543)
Income tax payable	9	-	(98)
Progress payments received in advance	15	(15,554)	(12,812)
<b>Total</b>		<b>\$ (238,908)</b>	<b>\$ (306,753)</b>
<b>Non - Current</b>			
Derivatives	22	\$ (1,073)	\$ (5,712)
Interest bearing loans and borrowings	11	(186,487)	(170,066)
Provisions	21	(2,864)	(1,052)
Deferred grant income	13	(62,881)	(71,991)
Deferred tax liabilities	9	(10,874)	-
<b>Total</b>		<b>\$ (264,179)</b>	<b>\$ (248,821)</b>
<b>Total</b>		<b>\$ (503,087)</b>	<b>\$ (555,574)</b>
<b>Net Assets</b>		<b>\$ 456,914</b>	<b>\$ 457,552</b>
<b>Equity</b>			
<b>Equity attributable to owners of the parent</b>			
Contributed equity		\$ 116,384	\$ 114,738
Reserves		91,637	100,672
Retained earnings		248,893	242,142
<b>Total</b>		<b>\$ 456,914</b>	<b>\$ 457,552</b>
<b>Total</b>		<b>\$ 456,914</b>	<b>\$ 457,552</b>

The consolidated statement of financial position should be read in conjunction with the accompanying notes.



# Consolidated statement of changes in equity for the year ended 30 June 2017

	Issued Capital '000	Reserved Shares <sup>1</sup> '000	Retained Earnings '000	Foreign Currency Transl'n Reserve '000	Employee Benefits Reserve '000	Cash Flow Hedge Reserve '000	Common Control Reserve '000	Asset Reval'n Reserve '000	Total '000	Non Controlling Interest '000	Total Equity '000
<b>Equity at 1 July 2015</b>	\$ 121,753	\$ (9,230)	\$ 343,798	\$ 63,676	\$ 6,016	\$ (19,678)	\$ (15,925)	\$ 21,757	\$ 512,167	\$ 232	\$ 512,399
<b>Comprehensive Income</b>											
Loss for the year	\$ -	\$ -	\$ (84,281)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (84,281)	\$ 99	\$ (84,182)
Other Comprehensive Income	-	-	-	14,302	-	12,818	-	18,957	46,077	-	46,077
<b>Total</b>	\$ -	\$ -	\$ (84,281)	\$ 14,302	\$ -	\$ 12,818	\$ -	\$ 18,957	\$ (38,204)	\$ 99	\$ (38,105)
<b>Other equity transactions</b>											
Shares issued	1,608	-	-	-	-	-	-	-	\$ 1,608	\$ -	\$ 1,608
Dividends	-	-	(17,375)	-	-	-	-	-	(17,375)	-	(17,375)
Repayment of shareholder loans	-	229	-	-	-	-	-	-	229	-	229
Acquisition of minority stake	-	-	-	-	-	-	(1,669)	-	(1,669)	(331)	(2,000)
Vesting performance rights	378	-	-	-	(378)	-	-	-	-	-	-
Share based payments expense	-	-	-	-	796	-	-	-	796	-	796
<b>Total</b>	\$ 1,986	\$ 229	\$ (17,375)	\$ -	\$ 418	\$ -	\$ (1,669)	\$ -	\$ (16,411)	\$ (331)	\$ (16,742)
<b>Equity at 1 July 2016</b>	\$ 123,739	\$ (9,001)	\$ 242,142	\$ 77,978	\$ 6,434	\$ (6,860)	\$ (17,594)	\$ 40,714	\$ 457,552	\$ -	\$ 457,552
<b>Comprehensive Income</b>											
Profit for the year	\$ -	\$ -	\$ 15,350	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 15,350	\$ -	\$ 15,350
Other Comprehensive Income	-	-	-	(11,073)	-	6,167	-	-	(4,906)	-	(4,906)
<b>Total</b>	\$ -	\$ -	\$ 15,350	\$ (11,073)	\$ -	\$ 6,167	\$ -	\$ -	\$ 10,444	\$ -	\$ 10,444
<b>Other equity transactions</b>											
Shares issued	\$ 1,690	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,690	\$ -	\$ 1,690
Dividends	-	-	(13,795)	-	-	-	-	-	(13,795)	-	(13,795)
Transfer between reserves <sup>2</sup>	-	-	5,196	(256)	(4,940)	-	-	-	-	-	-
Transfer between reserves <sup>3</sup>	2,891	(2,891)	-	-	-	-	-	-	-	-	-
Transfer between reserves <sup>4</sup>	-	-	-	(2)	-	-	-	2	-	-	-
Tax expense - employee share plan	(44)	-	-	-	-	-	-	-	(44)	-	(44)
Share based payments expense	-	-	-	-	1,067	-	-	-	1,067	-	1,067
<b>Total</b>	\$ 4,537	\$ (2,891)	\$ (8,599)	\$ (258)	\$ (3,873)	\$ -	\$ -	\$ 2	\$ (11,082)	\$ -	\$ (11,082)
<b>Equity at 30 June 2017</b>	\$ 128,276	\$ (11,892)	\$ 248,893	\$ 66,647	\$ 2,561	\$ (693)	\$ (17,594)	\$ 40,716	\$ 456,914	\$ -	\$ 456,914

1. Reserved Shares are held in relation to the Austal Group Management Share Plan.

2. Transfer of expired awards that have not been exercised.

3. Transfer of vested Reserved Shares.

4. Transfer between reserves.

The consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

## Consolidated statement of cash flows for the year ended 30 June 2017

	Notes	2017 '000	2016 '000
<b>Cash flows from operating activities</b>			
Receipts from customers		\$ 1,256,187	\$ 1,536,356
Payments to suppliers and employees		(1,302,771)	(1,425,455)
Interest received	4	1,525	1,106
Interest paid		(5,033)	(5,098)
Income tax refunded / (paid)		12,198	(4,843)
Net cash from / (used in) operating activities	7	\$ (37,894)	\$ 102,066
<b>Cash flows from investing activities</b>			
Receipts of government infrastructure grants		\$ 1,134	\$ 14,463
Proceeds from sale of property, plant and equipment		110	2,469
Purchase of property, plant and equipment		(9,195)	(12,793)
Purchase of intangible assets		(823)	(995)
Construction of Cape Class Patrol Boats 9 & 10		(42,776)	(18,023)
Construction of vessel completion yard		-	(10,098)
Investment in joint venture		(1,956)	-
Net cash from / (used in) investing activities		\$ (53,506)	\$ (24,977)
<b>Cash flows from financing activities</b>			
Repayment of borrowings		\$ (13,455)	\$ (11,992)
Loans received for Cape Class Patrol Boats 9 & 10		38,074	23,046
Dividends paid (net of dividend reinvestment program)		(12,260)	(15,767)
Net cash from / (used in) financing activities		\$ 12,359	\$ (4,713)
<b>Net increase / (decrease) in cash and cash equivalents</b>		<b>\$ (79,041)</b>	<b>\$ 72,376</b>
<b>Cash and cash equivalents</b>			
Cash and cash equivalents at beginning of year		\$ 224,318	\$ 148,468
Net foreign exchange differences		5,194	3,474
Net increase / (decrease) in cash and cash equivalents		(79,041)	72,376
Cash and cash equivalents at end of year	10	\$ 150,471	\$ 224,318

The consolidated statement of cash flows should be read in conjunction with the accompanying notes.

## Notes to the financial statements

### Basis of preparation

#### Note 1 Corporate information

The financial report of the Austal Limited Group of Companies (the Group) for the year ended 30 June 2017 was authorised for issue in accordance with a resolution of the Directors on 25 August 2017.

Austal Limited is a limited liability company incorporated and domiciled in Australia whose shares are publicly traded on the Australian Securities Exchange.

The principal activities of the Group during the year were the design, manufacture and sustainment of high performance vessels. These activities are unchanged from the previous year.

#### Note 2 Basis of preparation

##### i Introduction

The financial report is a general-purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001 and Australian Accounting Standards (AASB).

The financial report has also been prepared on a historical cost basis, except for derivative financial instruments and land and buildings that have been measured at fair value.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars (\$'000) unless otherwise stated under the option available to the Group under ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191. The Company is an entity to which the Instrument applies.

The financial report presents the figures of the consolidated entity, unless otherwise stated. Austal Limited is a for profit entity.

##### ii Reporting structure

The notes to the consolidated financial statements have been divided into 8 main sections which are summarised as follows:

###### 1. Current year performance

This section focuses on the results and performance of the Group, including profitability, earnings per share, cash generation, and the return of cash to shareholders via dividends.

###### 2. Capital structure

This section focuses on the long term funding of the Group including cash, interest bearing loans and borrowings, contributed equity and reserves and government grants.

### **3. Working capital**

This section focuses on shorter term working capital concepts such as trade and other receivables and payables, construction contracts in progress, inventories including work in progress.

### **4. Infrastructure & other assets**

This section focuses on property, plant & equipment as well as intangible assets of the Group.

### **5. Other liabilities**

This section focuses on provisions such as employee benefits and future warranty costs.

### **6. Financial risk management**

This section focuses on the Group's approach to financial risk management, fair value measurements and foreign exchange hedging and the associated derivative financial instruments.

### **7. Unrecognised items**

This section focuses on commitments and contingencies that are not recognised in the financial statements and events occurring after the balance date.

### **8. The Group, management and related parties**

This section focuses on the corporate structure of the Group, parent entity data, key management personnel compensation and related party transactions.

## **iii Basis of consolidation**

The consolidated financial statements comprise the financial statements of the Group for the year ended 30 June 2017.

Subsidiaries are all of those entities over which the Group has power over the entity, exposure or rights to variable returns from its involvement with the entity and the ability to use its power over the entity to affect its returns. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Financial statements of foreign controlled entities presented in accordance with overseas accounting principles are adjusted to comply with Group policy and generally accepted accounting principles in Australia for consolidation purposes. All intercompany balances, transactions, unrealised gains and losses resulting from intra-Group transactions and dividends have been eliminated in preparing the consolidated financial statements.

Subsidiaries are fully consolidated from the date on which control is obtained by the Group and cease to be consolidated from the date on which control is transferred out of the Group.

Investments in subsidiaries held by Austal Limited are accounted for at cost in the separate financial statements of the parent entity less any impairment charges. Dividends received from subsidiaries are recorded as a component of other revenues in the statement of comprehensive income of the parent entity, and do not impact the recorded cost of the investment. The parent will assess whether any indicators of impairment of the carrying value of the investment in the subsidiary exist upon receipt of dividend payments from subsidiaries. An impairment loss is recognised to the extent that the carrying value of the investment exceeds its recoverable amount where such indicators exist.

#### iv Foreign currency transactions and translation

Both the functional and presentation currency of Austal Limited and its Australian subsidiaries are Australian dollars (AUD). The Company determines the functional currency for each entity within the Group and items included in the financial statements of each entity are measured using that functional currency.

Transactions in foreign currencies are initially recorded in the functional currency by applying the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance date. All exchange differences arising from the above procedures are taken to the statement of comprehensive income.

The functional currency of the USA and the Philippines operations is United States Dollars (USD).

The assets and liabilities of the overseas subsidiaries are translated into the presentation currency of Austal Limited at the closing foreign exchange rate for the reporting date. The statement of comprehensive income is translated at the average exchange rates for the period. The exchange differences arising on translation are taken directly to a separate reserve in equity. The deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the statement of comprehensive income on disposal of a foreign entity.

#### v Statement of compliance

The financial report complies with Australian Accounting Standards and International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board.

#### vi Changes in accounting policies

##### 1. New and amended standards adopted by the Group

The Group has applied all new and amended accounting standards and interpretations effective from 1 July 2017, including:

- Australian Accounting Standards Board (AASB) 2014-9 amendments to Australian Accounting Standards – Equity Method in Separate Financial Statements. The amendments to AASB 127 Separate Financial Statements allow an entity to use the equity method as described in AASB 128 to account for its investments in subsidiaries, joint ventures and associates in its separate financial statements.
- Australian Accounting Standards Board (AASB) 2015-1 amendments to Australian Accounting Standards – Annual Improvements to Australian Accounting Standards 2012–2014 Cycle.

The amendments clarify certain requirements in:

- AASB 7 Financial Instruments: Disclosures - servicing contracts; applicability of the amendments to AASB 7 to condensed interim financial statements
- AASB 119 Employee Benefits - regional market issue regarding discount rate
- AASB 134 Interim Financial Reporting - disclosure of information 'elsewhere in the interim financial report

- AASB 2015-2 Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 101. This Standard amends AASB 101 Presentation of Financial Statements to clarify existing presentation and disclosure requirements and to ensure entities are able to use judgement when applying the Standard in determining what information to disclose, where and in what order information is presented in their financial statements. For example, the amendments make clear that materiality applies to the whole of financial statements and that the inclusion of immaterial information can inhibit the usefulness of financial disclosures.

The adoption of these standards did not have any effect on the financial position or performance of the Group.

## vii Pronouncements issued and not effective

A number of Australian Accounting Standards and Interpretations have been issued or amended but are not yet effective. A full assessment of the impact of all the new or amended Accounting Standards and interpretations issued but not effective has not yet been completed.

The pronouncements relevant to the Group which have not been adopted by the Group are as follows:

### 1. AASB 9: Financial Instruments [AASB 9] (effective 1 July 2018):

AASB 9 (December 2014) is a new standard which replaces AASB 139. This new version supersedes AASB 9 issued in December 2009 (as amended) and AASB 9 (issued in December 2010) and includes a model for classification and measurement, a single, forward-looking 'expected loss' impairment model and a substantially-reformed approach to hedge accounting.

AASB 9 is effective for annual periods beginning on or after 1 January 2018. The Standard is available for early application. The own credit changes can be early applied in isolation without otherwise changing the accounting for financial instruments.

#### Classification and measurement

AASB 9 includes requirements for a simpler approach for classification and measurement of financial assets compared with the requirements of AASB 139. There are also some changes made in relation to financial liabilities.

The main changes are described below.

## Financial assets

- a) 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; (2) the characteristics of the contractual cash flows.
- b) Allows an irrevocable election 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.
- c) 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.

## Financial liabilities

Changes introduced by AASB 9 in respect of financial liabilities are limited to the measurement of liabilities designated at fair value through profit or loss (FVPL) using the fair value option.

The change in fair value is to be accounted for as follows, where the fair value option is used for financial liabilities: The change attributable to changes in credit risk are presented in other comprehensive income (OCI). The remaining change is presented in profit or loss.

AASB 9 also removes the volatility in profit or loss that was caused by changes in the credit risk of liabilities elected to be measured at fair value. This change in accounting means that gains caused by the deterioration of an entity's own credit risk would be recognised in OCI. These amounts recognised in OCI are not recycled to profit or loss if the liability is ever repurchased at a discount.

## Impairment

The final version of AASB 9 introduces a new expected-loss impairment model that will require more timely recognition of expected credit losses. Specifically, the new Standard requires entities to account for expected credit losses from when financial instruments are first recognised and to recognise full lifetime expected losses on a more timely basis.

## Hedge accounting

Amendments to AASB 9 (December 2009 & 2010 editions and AASB 2013-9) issued in December 2013 included the new hedge accounting requirements, including changes to hedge effectiveness testing, treatment of hedging costs, risk components that can be hedged and disclosures.

Consequential amendments were also made to other standards as a result of AASB 9, introduced by AASB 2009-11 and superseded by AASB 2010-7, AASB 2010-10 and AASB 2014-1 – Part E.

AASB 2014-7 incorporates the consequential amendments arising from the issuance of AASB 9 in Dec 2014.

AASB 2014-8 limits the application of the existing versions of AASB 9 (AASB 9 (December 2009) and AASB 9 (December 2010)) from 1 February 2015 and applies to annual reporting periods beginning on after 1 January 2015.

## **2. AASB 15 Revenue from Contracts with Customers (effective date 1 July 2018):**

AASB 15 Revenue from Contracts with Customers replaces the existing revenue recognition standards AASB 111 Construction Contracts, AASB 118 Revenue and related Interpretations (Interpretation 13 Customer Loyalty Programmes, Interpretation 15 Agreements for the Construction of Real Estate, Interpretation 18 Transfers of Assets from Customers, Interpretation 131 Revenue—Barter Transactions Involving Advertising Services and Interpretation 1042 Subscriber Acquisition Costs in the Telecommunications Industry). AASB 15 incorporates the requirements of IFRS 15 Revenue from Contracts with Customers issued by the International Accounting Standards Board (IASB) and developed jointly with the US Financial Accounting Standards Board (FASB).

AASB 15 specifies the accounting treatment for revenue arising from contracts with customers (except for contracts within the scope of other accounting standards such as leases or financial instruments). The core principle of IFRS 15 is that an entity recognises revenue to depict 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:

- (a) Step 1: Identify the contract(s) with a customer
- (b) Step 2: Identify the performance obligations in the contract
- (c) Step 3: Determine the transaction price
- (d) Step 4: Allocate the transaction price to the performance obligations in the contract
- (e) Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

AASB 2015-8 amended the AASB 15 effective date so it is now effective for annual reporting periods commencing on or after 1 January 2018. Early application is permitted.

AASB 2014-5 incorporates the consequential amendments to a number Australian Accounting Standards (including Interpretations) arising from the issuance of AASB 15.

AASB 2016-3 Amendments to Australian Accounting Standards – Clarifications to AASB 15 amends AASB 15 to clarify the requirements on identifying performance obligations, principal versus agent considerations and the timing of recognising revenue from granting a licence and provides further practical expedients on transition to AASB 15. AASB 2014-5 incorporates the consequential amendments to a number Australian Accounting Standards (including Interpretations) arising from the issuance of AASB 15.

Austal has undertaken implementation project to analyse the impact of AASB 15 Revenue from Contracts with Customers which replaces the existing revenue recognition standards AASB 111 Construction Contracts.

As at 30 June 2017, assessment of the impact of AASB 15 on Austal revenue recognition is ongoing. Determination of the transition approach is also under evaluation.

## **3. AASB 2014-10 Amendments to Australian Accounting Standards – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (effective date 1 July 2018):**

AASB 2014-10 amends AASB 10 Consolidated Financial Statements and AASB 128 to address an inconsistency between the requirements in AASB 10 and those in AASB 128 (August 2011), in dealing with the sale or contribution of assets between an investor and its associate or joint venture.



The amendments require:

- (a) a full gain or loss to be recognised when a transaction involves a business (whether it is housed in a subsidiary or not); and
- (b) a partial gain or loss to be recognised when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary.

AASB 2014-10 also makes an editorial correction to AASB 10.

AASB 2015-10 defers the mandatory effective date (application date) of AASB 2014-10 so that the amendments are required to be applied for annual reporting periods beginning on or after 1 January 2018 instead of 1 January 2016.

#### **4. AASB 16 Leases (effective date 1 July 2019):**

The key features of AASB 16 are as follows:

Lessee accounting

- 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.
- A lessee measures right-of-use assets similarly to other non-financial assets and lease liabilities similarly to other financial liabilities.
- 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.
- AASB 16 contains disclosure requirements for lessees.

Lessor accounting

- 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.
- 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.

AASB 16 supersedes:

- (a) AASB 117 Leases
- (b) Interpretation 4 Determining whether an Arrangement contains a Lease
- (c) SIC-15 Operating Leases—Incentives
- (d) SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease

The new standard will be effective for annual periods beginning on or after 1 January 2019. Early application is permitted, provided the new revenue standard, AASB 15 Revenue from Contracts with Customers, has been applied, or is applied at the same date as AASB 16.

#### **5. 2016-1 Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses [AASB 112] (effective date 1 July 2019):**

This Standard amends AASB 112 Income Taxes (July 2004) and AASB 112 Income Taxes (August 2015) to clarify the requirements on recognition of deferred tax assets for unrealised losses on debt instruments measured at fair value.

**6. 2016-2 Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107 (effective date 1 July 2019):**

This Standard amends AASB 136 to remove references to depreciated replacement cost as a measure of value in use for not-for-profit entities and clarify that not-for-profit entities holding non-cash-generating specialised assets at fair value in accordance with AASB 13 [under the revaluation model in AASB 116 and AASB 138] no longer need to consider AASB 136.

Not-for-profit entities holding such assets at cost will determine recoverable amounts using current replacement cost in AASB 13.

**7. IFRS 2 (Amendments) Classification and Measurement of Share-based Payment Transactions [Amendments to IFRS 2] (effective date 1 July 2018):**

This standard amends to IFRS 2 Share-based Payment, clarifying how to account for certain types of share-based payment transactions. The amendments provide requirements on the accounting for:

- The effects of vesting and non-vesting conditions on the measurement of cash settled share-based payments
- Share-based payment transactions with a net settlement feature for withholding tax obligations
- A modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash settled to equity settled.

## Current year performance

### Note 3 Operating segments

	Australia '000	USA '000	Philippines '000	Unallocated '000	Elimination / Adjustments '000	Total '000
<b>Year ended 30 June 2017</b>						
<b>Revenue</b>						
External customers	\$ 99,671	\$ 1,172,066	\$ 33,698	\$ 3,080	\$ 88	\$ 1,308,603
Inter-segment	14,073	-	134	-	(14,207)	-
Finance income	-	-	-	1,525	-	1,525
<b>Total</b>	<b>\$ 113,744</b>	<b>\$ 1,172,066</b>	<b>\$ 33,832</b>	<b>\$ 4,605</b>	<b>\$ (14,119)</b>	<b>\$ 1,310,128</b>
<b>Profit / (loss) before tax</b>						
Earnings before interest and tax	\$ (2,059)	\$ 76,061	\$ 330	\$ (28,932)	\$ 138	\$ 45,538
Finance income	-	-	-	1,525	-	1,525
Finance expenses	-	-	-	(7,198)	-	(7,198)
<b>Profit / (loss) before income tax</b>	<b>\$ (2,059)</b>	<b>\$ 76,061</b>	<b>\$ 330</b>	<b>\$ (34,605)</b>	<b>\$ 138</b>	<b>\$ 39,865</b>
Depreciation and amortisation	\$ (1,544)	\$ (26,572)	\$ (1,502)	\$ (1,904)	\$ -	\$ (31,522)
<b>Balance sheet</b>						
Segment assets	\$ 180,727	\$ 705,163	\$ 27,379	\$ 50,659	\$ (3,927)	\$ 960,001
Segment liabilities	(118,163)	(359,895)	(9,128)	(15,901)	-	(503,087)
<b>Year ended 30 June 2016</b>						
<b>Revenue</b>						
External customers	\$ 173,593	\$ 1,133,024	\$ 27,160	\$ 6,083	\$ (996)	\$ 1,338,864
Inter-segment	13,461	-	6,739	-	(20,200)	-
Finance income	-	-	-	1,106	-	1,106
<b>Total</b>	<b>\$ 187,054</b>	<b>\$ 1,133,024</b>	<b>\$ 33,899</b>	<b>\$ 7,189</b>	<b>\$ (21,196)</b>	<b>\$ 1,339,970</b>
<b>Profit / (loss) before tax</b>						
Earnings before interest and tax	\$ 6,756	\$ (90,457)	\$ (3,766)	\$ (32,038)	\$ (1,360)	\$ (120,865)
Finance income	-	-	-	1,106	-	1,106
Finance expenses	-	-	-	(6,605)	-	(6,605)
<b>Profit / (loss) before income tax</b>	<b>\$ 6,756</b>	<b>\$ (90,457)</b>	<b>\$ (3,766)</b>	<b>\$ (37,537)</b>	<b>\$ (1,360)</b>	<b>\$ (126,364)</b>
Depreciation and amortisation	\$ (878)	\$ (24,246)	\$ (1,633)	\$ (3,142)	\$ -	\$ (29,899)
<b>Balance sheet</b>						
Segment assets	\$ 117,227	\$ 745,056	\$ 23,379	\$ 132,206	\$ (4,742)	\$ 1,013,126
Segment liabilities	(93,816)	(453,224)	(6,695)	(9,781)	7,942	(555,574)

Inter-segment revenues, investments, receivables and payables are eliminated on consolidation.

	2017 '000	2016 '000
<b>Analysis of Unallocated</b>		
<b>Revenue</b>		
Support / sustainment	\$ 2,068	\$ 4,425
Charter vessel revenue	1,012	1,658
Finance income	1,525	1,106
Total	<u>\$ 4,605</u>	<u>\$ 7,189</u>
<b>Profit / (loss) before tax</b>		
Foreign exchange gains / (losses)	\$ (606)	\$ 923
Net profit / (loss) on sale of vessel	-	(208)
Write down of charter vessels	(379)	(1,630)
Warranty Provision	-	(10,966)
Settlement of Warranty Defects	(13,154)	-
Administration expenses	(11,865)	(10,489)
Marketing expenses	(12,383)	(8,559)
Charter vessel profit / (loss)	48	(1,109)
Share of profit / (loss) from joint venture	(109)	-
Research and development credit	9,516	-
Finance income	1,525	1,106
Finance expenses	(7,198)	(6,605)
Total	<u>\$ (34,605)</u>	<u>\$ (37,537)</u>
<b>Segment assets</b>		
Cash	\$ 23,848	\$ 87,917
Property, plant and equipment	4,099	4,618
Inventories	417	31
Other receivables	10,903	-
Derivatives	1	13
Deferred tax assets	5,589	33,765
Income tax receivable	1,075	945
Assets held for sale	2,529	2,908
Investment in joint venture	1,847	-
Other	351	2,009
Total	<u>\$ 50,659</u>	<u>\$ 132,206</u>
<b>Segment liabilities</b>		
Deferred tax liabilities	\$ (10,893)	\$ (27)
Income tax payable	-	(1,039)
Derivatives	(2)	(4,379)
Progress payments received in advance	(48)	(62)
Creditors & provisions	(4,958)	(4,274)
Total	<u>\$ (15,901)</u>	<u>\$ (9,781)</u>

One customer in the USA segment generated revenue of \$1,172.217 million during FY2017 (FY2016: \$1,133.024 million).

	<b>2017</b>	<b>2016</b>
	<b>\$'000</b>	<b>\$'000</b>
<b>Revenue from external customers by geographical location of customers</b>		
North America	\$ 1,172,154	\$ 1,155,769
Europe	20,740	66,157
Asia	29,932	-
Australia	70,630	32,431
Middle East	15,147	84,507
Other	-	-
Total	<u>\$ 1,308,603</u>	<u>\$ 1,338,864</u>

	<b>2017</b>	<b>2016</b>
	<b>\$'000</b>	<b>\$'000</b>
<b>Non-current assets, other than financial instruments, prepayments and deferred tax assets</b>		
<b>Geographical location</b>		
North America	\$ 379,513	\$ 411,399
Asia	20,719	22,157
Europe	3,987	4,430
Australia	104,994	62,108
Total	<u>\$ 509,213</u>	<u>\$ 500,094</u>
<b>Composition</b>		
Property, plant and equipment	\$ 500,304	\$ 490,798
Intangible assets	8,909	9,296
Total	<u>\$ 509,213</u>	<u>\$ 500,094</u>

## i Identification of reportable segments

The Group is organised into three business segments for management purposes based on the location of the production facilities, related sales regions and types of activity.

The Chief Executive Officer, who is the Chief Operating Decision Maker (CODM), monitors the performance of the business segments separately for the purpose of making decisions about the allocation of resources and assessing performance. Segment performance is evaluated based on operating profit or loss. Finance costs, finance income and income tax are managed on a Group basis.

## ii Reportable segments

The Group's reportable segments are Australia, USA and Philippines:

### 1. Australia

The Australia business manufactures high performance defence vessels for markets worldwide, excluding the USA and provides training and on-going support and maintenance for high performance vessels.

### 2. USA

The USA business manufactures high performance aluminium defence vessels for the US Navy and provides training and on-going support and maintenance of these performance vessels for the US Navy.

### 3. Philippines

The Philippines business manufactures high performance aluminium commercial vessels for global markets excluding the USA. The Philippines segment also provides support to other segments not just manufacturing for external buyers.

## iii Aggregation of segments

No operating segments are aggregated.

## iv Accounting policies and inter-segment transactions

The accounting policies used for reporting segments internally are the same as those utilised for reporting the accounts of the Group.

Inter-entity sales are recognised based on an arm's length pricing structure.

## v Unallocated

The following items and associated assets and liabilities are not allocated to operating segments because they are not considered to be part of the core operations of any segment:

- Cost of Group services
- Corporate overheads
- Finance revenue and costs
- Taxation
- Assets held for sale
- Commercial vessel charter contracts
- Property, plant and equipment relating to the parent entity

## Note 4 Revenue

	2017 '000	2016 '000
<b>Revenue</b>		
Vessel construction and support	\$ 1,306,178	\$ 1,313,465
Charter vessels	2,425	25,399
Total Revenue from customers	\$ 1,308,603	\$ 1,338,864
Finance income	\$ 1,525	\$ 1,106
Total	\$ 1,310,128	\$ 1,339,970

### i Recognition and measurement

Revenue is recognised and measured at the fair value of the consideration received or receivable to the extent that it is probable that the economic benefits will flow to the Group and that the revenue can be measured reliably. The following specific recognition criteria must also be met before revenue is recognised:

#### 1. Construction and support contract revenue

Construction and support contract revenue is brought to account based on percentage of completion which is calculated on actual costs incurred as a proportion of estimated total contract costs.

Contract costs are recognised as an expense as incurred and revenue is recognised only to the extent of the costs incurred where it is probable that the costs will be recovered and the contract outcome cannot be measured reliably during the term of the contract.

The estimated total contract costs are determined prior to commencement and re-evaluated every month thereafter for the purposes of recognising construction contract revenue. Construction contract revenue is adjusted in the event of a change to the cost of completion during the life of the contract and revenue is recognised for the remaining life of the contract based upon the adjusted value.

#### 2. Charter vessel revenue

Charter revenue is generated from operating rentals received on charter of vessels and is recognised when the control over the right to revenue is achieved.

#### 3. Finance income

Finance income is recognised as interest accrues using the effective interest method. This is a method of calculating the amortised cost of a financial asset and allocating the interest income over the relevant period using the effective interest rate, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to the net carrying amount of the financial asset.

## ii Significant accounting judgements and estimates

### 1. Contract revenue and expected construction profits at completion

The assessment of contract revenue in accordance with the Group's accounting policies requires certain estimates to be made of total contract revenues, total contract costs and the current percentage of completion.

The percentage of completion is calculated on actual project costs to date, divided by the sum of projected costs to complete. Contract revenue and contract costs are recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the balance sheet date ("percentage-of-completion method") when the outcome of a contract can be estimated reliably. Contract revenue is recognised to the extent of contract costs incurred that are likely to be recoverable when the outcome of a contract cannot be estimated reliably.

Management has made estimates in this area, which if ultimately inaccurate will impact the level of revenue recognised in the Consolidated Statement of Comprehensive Income of FY2017 and future years.

Estimates were made by management with respect to total contract revenues, and total contract costs, which had a resulting impact on the percentage of completion, in line with the Group's accounting policy for contract revenue.

All other projects' revenue and cost estimates at completion were updated with no material impact to the Group.

### 2. USA LCS Program

The US Navy completed physical "shock trials" of LCS 6 in July 2016 to measure and assess the impact of an explosive charge detonated at a specified proximity to the vessel whilst underway at sea. The specific results of these trials remain classified by the US Navy, and are unlikely to ever be released to either Austal or the public in light of the extreme sensitivity of the vessel's capability to withstanding the impact of shock.

Austal has not been advised of any material issues regarding vessel performance by the US Navy, however the analysis conducted by the US Navy has not been finalised which means that the risk of incurring additional cost to address issues that may be identified by the analysis cannot be discounted entirely.

The residual risk regarding the performance of LCS and the shock trial analysis will reduce over time as the vessel continues to demonstrate its capabilities.



## Note 5 Other Profit and Loss Disclosures

	2017 '000	2016 '000
<b>Other income and expenses</b>		
Government infrastructure grants	\$ 8,522	\$ 4,877
Training reimbursement grants	3,864	5,351
Gain / (loss) on disposal of property, plant and equipment	(23)	(200)
Net foreign exchange gains / (losses)	(742)	834
Sale of scrap materials	3,486	3,558
Other income	782	1,872
Settlement of warranty defects	(13,154)	-
Write down of assets held for sale	(379)	-
Write down of charter vessels	-	(1,903)
Write down of other inventory	-	(1,100)
Total	<u>\$ 2,356</u>	<u>\$ 13,289</u>
<b>Finance costs</b>		
Interest to unrelated parties	\$ (5,998)	\$ (5,377)
Amortisation of capitalised loan origination costs	(1,200)	(1,228)
Total	<u>\$ (7,198)</u>	<u>\$ (6,605)</u>
<b>Share of profit from joint venture</b>		
Share of profit / (loss) of Aulong Shipbuilding Co Ltd Joint Venture	\$ (109)	-
Total	<u>\$ (109)</u>	<u>\$ -</u>
<b>Depreciation and amortisation</b>		
Depreciation excluding impairment	\$ (30,379)	\$ (28,461)
Amortisation of intangible assets	(1,143)	(1,438)
Total	<u>\$ (31,522)</u>	<u>\$ (29,899)</u>
<b>Employee benefits</b>		
Wages and salaries	\$ (385,986)	\$ (415,183)
Superannuation	(5,340)	(4,766)
Share based payments expense	(1,067)	(796)
Workers' compensation costs	(6,609)	(10,450)
Annual leave expense	(18,467)	(20,062)
Long service leave expense	(709)	(1,265)
Total	<u>\$ (418,178)</u>	<u>\$ (452,522)</u>
Employee benefits listed above includes expenses that are disclosed in cost of sales.		
<b>Research &amp; development credit recognised in cost of sales</b>		
Research & development credit	\$ 11,517	\$ 1,311
<b>Auditor's remuneration</b>		
Amounts received or due and receivable by Ernst & Young Australia for:		
An audit or review of the financial report of the entity and any other entity in the Group	\$ (319,731)	\$ (297,404)
Amounts received or due and receivable by related practices of Ernst & Young for:		
An audit or review of the financial report of the entity and any other entities in the Group	(604,072)	(892,079)

## **i Recognition & measurement**

The following recognition and measurement criteria must be met before the following specific items are recognised in profit or loss:

### **1. Grants relating to expense items**

Grants include US Government infrastructure grants and training reimbursement grants.

Grants are recognised when there is reasonable assurance that the grant will be received and all attaching conditions will be complied with.

All grants are recognised as income when it relates to an expense item. The grants are recognised over the periods necessary to match the grant to the costs that it is intended to compensate.

### **2. Research and Development (R&D) Tax Credit**

R&D tax incentives in excess of the statutory tax rate are accounted for in accordance with the Group's accounting policies as a government grant under AASB 120 rather than as an income tax benefit under AASB 112.

The excess R&D tax credits are recognised as a reduction to each vessel's cost estimate at completion when there is reasonable assurance that the credits will be received and utilised. The entire credit is recognised in cost of sales and changes the calculation of percent complete which impacts the timing of Revenue recognition for the projects.

The net impact to profit before tax in FY2017 is \$11.517 million.

### **3. Finance costs**

Finance costs directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of that asset. There are no qualifying assets in FY2017. All other finance costs are expensed in the period they occur.

Finance costs include interest payments, amortisation of capitalised loan origination costs and other costs that an entity incurs in connection with the borrowing of funds.

### **4. Depreciation and amortisation**

Refer to accounting policies for depreciation disclosed in Note 18, and to accounting policies related to amortisation of Intangible assets in Note 19.

### **5. Employee benefits**

Refer to accounting policies for employee benefits in Note 21.

### **6. Leases**

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight-line basis over the lease term.

## **7. Sale of scrap materials**

Revenue for the sale of scrap is recognised when the significant risks and rewards of ownership of the materials have passed to the buyer. Risk and rewards of ownership are considered to have passed to the buyer at the time of delivery of the goods to the customer.

## **ii Foreign exchange gains and losses included in profit and loss**

Foreign exchange gains and losses included in profit and loss comprise:

- Fair value adjustments on non-derivative financial assets such as foreign currency denominated loans.
- Gains and losses on cash flow hedges that were deemed to be ineffective during the accounting period.

## **iii Significant accounting judgements and estimates**

### **1. Research & development tax credits**

The Group engages in research and development activities over new vessel designs. Certain judgements are required in assessing whether the research and development tax offset has been recognised in accordance with the Group's accounting policies and in accounting for R&D as a government grant under AASB 120 rather than as an income tax benefit.

Research and development credits in excess of the statutory tax rate are recognised as a government grant, to the extent that expenditure is of a kind eligible for the research and development tax incentive, and the credit is assessed as recoverable.

Management has made judgements regarding which expenditure is classified as eligible for the credit, including assessing activities to determine whether they are conducted for the purposes of generating new knowledge, and whose outcome cannot be known or determined in advance.

## Note 6 Earnings per share

		<u>2017</u>	<u>2016</u>
<b>Net profit / (loss) after tax</b>			
Net profit attributable to ordinary equity holders of the parent from continuing operations	\$'000	\$ 15,350	\$ (84,281)
<b>Weighted average number of ordinary shares</b>			
Basic	Number	345,094,616	347,665,088
Effect of dilution	Number	2,893,640	-
Diluted	Number	<u>347,988,256</u>	<u>347,665,088</u>
<b>Earnings per share</b>			
Basic earnings per share	\$ / share	\$ 0.044	\$ (0.242)
Diluted earnings per share	\$ / share	\$ 0.044	\$ (0.242)

### i Measurement

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

Diluted earnings per share amounts are calculated by dividing the net profit attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all dilutive potential ordinary shares into ordinary shares.

### ii Information concerning the classification of securities

#### 1. Performance rights

Performance rights granted to executives under the Group's Long Term Incentive Plan are included in the calculation of diluted earnings per share where the conditions would have been met at balance sheet date. The rights are not included in the determination of basic earnings per share. There are 1,266,289 performance rights which are not dilutive to earnings per share.

Further information about the performance rights is provided in Note 30.

#### 2. Share rights

Share rights may be provided to the CEO as part of his total fixed remuneration. The share rights are subject to a 12 month holding period from the date at which the shares are released to the CEO, and no performance condition exists because they are considered to be part of his base remuneration. This arrangement was approved by shareholders at the 2016 Annual General Meeting for a period ending 31 December 2019. The share rights are included in the calculation of basic earnings per share. 191,740 share rights were issued during the year.

Further information about the share rights is provided in Note 30.

### **3. Options**

Austal Limited issued two tranches of options to the sellers of KME Engineering (NT) Pty Ltd & Hydraulink when they were acquired by Austal Service Darwin Pty Ltd in FY2013. The options are not included in the determination of basic earnings per share. There are 1,374,196 options which are dilutive to earnings per share.

Further information about the options is provided in Note 30.

### **4. Austal Group Management Share Plan (AGMSP)**

The trustee holds a total of 4,015,539 shares at balance date on behalf of the AGMSP plans.

3,702,000 shares allocated under Plans 1 and 2 are not dilutive to earnings per share.

Further information about the options is provided in Note 30.

### **5. Other equity transactions**

There have been no transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of completion of these financial statements.

## Note 7 Reconciliation of net profit after tax to net cash flows from operations

	2017 <u>'000</u>	2016 <u>'000</u>
<b>Net (loss) / profit after tax</b>	\$ 15,350	\$ (84,182)
<b>Adjustments for:</b>		
Depreciation and amortisation	\$ 31,522	\$ 29,899
Write down of charter vessels	379	1,903
Net (gain) / loss on disposal of property, plant and equipment	23	200
Share based payments expense	1,067	796
Net exchange differences	742	(834)
Government infrastructure grants income	(8,522)	(4,877)
<b>Total</b>	<b>\$ 25,211</b>	<b>\$ 27,087</b>
<b>Changes in assets and liabilities:</b>		
Increase / (decrease) in provisions for:		
Income tax (current and deferred)	\$ 39,424	\$ (52,370)
Workers' compensation insurance	203	515
Warranty	(854)	9,736
Employee benefits	2,779	4
Other provisions	3,979	(1,821)
(Increase) / decrease in trade & other receivables	24,590	(26,922)
(Increase) / decrease in inventories	(61,448)	230,729
(Increase) / decrease in prepayments	(669)	913
(Increase) / decrease in other financial assets	(1,988)	(3,854)
Increase / (decrease) in trade and other payables	(80,986)	15,111
Increase / (decrease) in progress payments in advance	2,742	(13,365)
Increase / (decrease) in derivative assets & liabilities	(5,030)	(1,799)
Increase / (decrease) in government grants	(1,197)	2,284
<b>Total</b>	<b>\$ (78,455)</b>	<b>\$ 159,161</b>
<b>Net cash (outflow) / inflow from operating activities</b>	<b>\$ (37,894)</b>	<b>\$ 102,066</b>

## Note 8 Dividends paid and proposed

### i Dividends on ordinary shares

	2017 '000	2016 '000
<b>Dividends paid on Ordinary Shares</b>		
Fully franked final dividend for the prior year, 2 cents per share (2016: 2 cent per share)	\$ (6,968)	\$ (10,422)
Fully franked interim dividend for the current year, 2 cents per share (2016: 2 cent per share)	(6,982)	(6,953)
Total	<u>\$ (13,950)</u>	<u>\$ (17,375)</u>
<b>Dividend declared subsequent to the reporting period end (not recorded as liability)</b>		
Fully franked final dividend 2 cents per share (2016: 2 cents per share)	\$ (6,989)	\$ (6,968)

### ii Franking credit balance

	2017 '000	2016 '000
<b>Opening Balance</b>	\$ 11,104	\$ 5,871
Franking credits movement from the payment / (refund) of income tax	\$ (1,697)	\$ 12,680
Franking credits distributed	(5,979)	(7,447)
Movement	<u>\$ (7,676)</u>	<u>\$ 5,233</u>
<b>Closing Balance</b>	<u>\$ 3,428</u>	<u>\$ 11,104</u>

## Note 9 Income and other taxes

### i Income tax expense

	2017 '000	2016 '000
<b>Major components of tax (expense) / benefit for the years ended 30 June 2017 and 2016 are:</b>		
<b>Consolidated Profit &amp; Loss</b>		
<b>Current Income Tax</b>		
Current income tax charge	\$ 3,189	\$ (2,987)
Adjustments in respect of current income tax of the previous year	7,461	(765)
Total	\$ 10,650	\$ (3,752)
<b>Deferred Income Tax</b>		
Relating to origination and reversal of temporary differences	\$ (25,709)	\$ 44,861
Adjustments in respect of deferred income tax of the previous year	(9,456)	1,073
Total	\$ (35,165)	\$ 45,934
<b>Total income tax (expense) / benefit</b>	<b>\$ (24,515)</b>	<b>\$ 42,182</b>
<b>Other Comprehensive Income (OCI)</b>		
<b>Current and deferred income tax related items charged or credited directly to OCI</b>		
Current and deferred gains and losses on foreign currency contracts and consolidation adjustments	\$ (4,482)	\$ (3,800)
Current gains and losses in FCTR	-	(21)
Deferred gains on revaluation of property, plant and equipment	-	(10,710)
<b>Total (expense) / benefit charged to OCI</b>	<b>\$ (4,482)</b>	<b>\$ (14,531)</b>
<b>A reconciliation between tax expense and the product of accounting profit before income tax multiplied by the Group's applicable income tax rate is as follows:</b>		
<b>Accounting profit / (loss) before income tax from continuing operations</b>	<b>\$ 39,865</b>	<b>\$ (126,364)</b>
<b>Income Tax at the Group's statutory income tax rate of 30% (2016: 30%)</b>	<b>\$ (11,960)</b>	<b>\$ 37,909</b>
Adjustment for Austal USA statutory income tax rate of 36.9% (2016: 36.9%)	\$ (5,851)	\$ 5,182
Other foreign tax rate differences	138	126
Branch (profit) / loss	(145)	(847)
US section 199 domestic manufacturing deduction	123	-
Non assessable research & development credit to cost of sale	1,416	-
WHT leakage due to losses in Australia	(454)	-
Non-deductible share based payments expense	(256)	(684)
Australian Tax Group losses not recognised	(3,412)	-
Transfer pricing adjustments in respect of intercompany royalties	(1,361)	-
Other non-assessable or non-deductible items	(758)	188
Adjustments in respect of current and deferred income tax of the previous year	(1,995)	308
Total Adjustments	\$ (12,555)	\$ 4,273
<b>Income tax (expense) / benefit reported in Consolidated statement of profit or loss</b>	<b>\$ (24,515)</b>	<b>\$ 42,182</b>
<b>Income tax payable</b>		
Income tax receivable / (payable)	\$ 706	\$ (98)



ii Analysis of temporary differences

	Statement of Financial Position		Consolidated Profit & Loss	
	2017 '000	2016 '000	2017 '000	2016 '000
<b>Deferred income tax - USA</b>				
<b>Deferred tax assets</b>				
Trade & other receivables	\$ 8,658	\$ -	\$ 8,863	\$ 1,214
Payables	199	10,572	(10,279)	3,824
Provisions	8,895	4,615	4,526	385
Deferred grant income	25,723	28,925	(2,372)	(1,644)
Losses available for offset against future taxable income - Federal	-	45,501	(45,140)	42,998
Losses available for offset against future taxable income - State	2,537	2,026	586	1,901
Work opportunity tax credits	-	215	(213)	-
Charitable donations	-	42	(41)	-
Alternative minimum tax	1,738	-	1,778	-
Inventories	108	72	34	(565)
Deferred gains and losses on foreign currency contracts	1,041	3,461	51	-
<b>Total</b>	<b>\$ 48,899</b>	<b>\$ 95,429</b>	<b>\$ (42,207)</b>	<b>\$ 48,113</b>
<b>Deferred tax liabilities</b>				
Property, plant and equipment	\$ (59,318)	\$ (65,897)	\$ 4,663	\$ (2,699)
Deferred gains and losses on foreign currency contracts	(455)	(33)	-	-
<b>Total</b>	<b>\$ (59,773)</b>	<b>\$ (65,930)</b>	<b>\$ 4,663</b>	<b>\$ (2,699)</b>
<b>Net deferred tax asset / (liability)</b>	<b>\$ (10,874)</b>	<b>\$ 29,499</b>	<b>\$ (37,544)</b>	<b>\$ 45,414</b>
<b>Deferred income tax - Australia</b>				
<b>Deferred tax assets</b>				
Trade & other receivables	\$ 53	\$ 36	\$ 18	\$ (1,738)
Payables	400	166	233	(607)
Provisions	7,953	6,428	1,523	2,510
Deferred gains and losses on foreign currency contracts	538	2,100	119	(6)
Undeducted section 40 - 880 costs	3	184	(180)	(176)
Assets classified as held for sale	439	-	439	-
Financial liabilities	140	-	140	-
Inventories	34	320	(284)	238
Losses available for offset against future taxable income	-	180	(181)	(51)
<b>Total</b>	<b>\$ 9,560</b>	<b>\$ 9,414</b>	<b>\$ 1,827</b>	<b>\$ 170</b>
<b>Deferred tax liabilities</b>				
Property, plant and equipment	\$ (3,291)	\$ (3,841)	\$ 552	\$ 542
Deferred gains and losses on foreign currency contracts	(639)	(113)	-	(192)
<b>Total</b>	<b>\$ (3,930)</b>	<b>\$ (3,954)</b>	<b>\$ 552</b>	<b>\$ 350</b>
<b>Net deferred tax asset / (liability)</b>	<b>\$ 5,630</b>	<b>\$ 5,460</b>	<b>\$ 2,379</b>	<b>\$ 520</b>
<b>Net deferred tax asset / (liability)</b>	<b>\$ (5,244)</b>	<b>\$ 34,959</b>	<b>\$ (35,165)</b>	<b>\$ 45,934</b>

### iii Recognition and measurement

#### 1. Current tax assets and liabilities

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by balance date.

#### 2. Deferred income tax

Deferred income tax is provided on all temporary differences at the balance date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes except:

- when the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the taxable temporary differences associated with investments in subsidiaries, associates or interests in joint ventures, and the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

#### 3. Deferred income tax asset recognition

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised except:

- when the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the deductible temporary differences are associated with investments in subsidiaries, associates and interests in joint ventures in which case a deferred tax asset is only recognised to the extent that taxable profits will be available in the foreseeable future.

The carrying amount of deferred income tax assets is reviewed at each balance date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Unrecognised deferred income tax assets are reassessed at each balance date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and deferred tax liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity and the same taxation authority.

#### 4. Deferred income tax asset and liability measurement

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance date.

#### 5. Income taxes relating to equity items

Income taxes relating to items recognised directly in equity are recognised in equity and not in the statement of comprehensive income.

#### iv Tax consolidation

Austal Limited (the Company) is the head entity in a Tax Consolidated Group comprising the Company and its 100% owned Australian resident subsidiaries. The implementation date of the tax consolidated system for the Tax Consolidated Group was 1 July 2002. Members of the Group have entered into a tax sharing arrangement in order to allocate income tax expense to the wholly owned subsidiaries on a pro-rata basis.

The agreement provides for the allocation of income tax liabilities between the entities in the event that the head entity defaults on its tax payment obligations. The possibility of default was assessed to be remote at the balance date.

The current and deferred tax amounts for the Tax Consolidated Group are allocated amongst the entities in the Tax Consolidated Group using a stand-alone taxpayer approach whereby each entity in the Tax Consolidated Group measures its current and deferred taxes as if it had continued to be a separately taxable entity in its own right. Deferred tax assets and deferred tax liabilities are measured by reference to the carrying amounts of the assets and liabilities in each entity's statement of financial position and their tax values applying under tax consolidation.

Any current tax liabilities (or assets) and deferred tax assets arising from unused tax losses assumed by the head entity from the subsidiaries in the Tax Consolidated Group are recognised in conjunction with any tax funding arrangement amounts (refer below).

The Tax Consolidated Group recognises deferred tax assets arising from unused tax losses of the Tax Consolidated Group to the extent that it is probable that future taxable profits of the Tax-Consolidated Group will be available against which the asset can be utilised.

Any subsequent period adjustments to deferred tax assets arising from unused tax losses assumed from subsidiaries are recognised by the head entity only.

The members of the Tax Consolidated Group have entered into a tax funding arrangement which sets out the funding obligations of members of the Tax Consolidated Group in respect of tax amounts. The tax funding arrangements require payments to / from the head entity equal to the current tax liability (asset) assumed by the head entity and any tax-loss deferred tax asset assumed by the head entity.

No amounts have been recognised as tax consolidation contribution/distribution adjustments in preparing the accounts for the parent company for the current year.

#### v Significant accounting judgements and estimates

Deferred tax assets are recognised for deductible temporary differences because management considers that it is probable that future taxable profits will be available to utilise those temporary differences.

Uncertainties exist with respect to the interpretation of complex tax regulations, changes in tax laws, and the amount and timing of future taxable income. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to tax income and expense already recorded given the wide range of international business relationships and the long-term nature and complexity of existing contractual agreements.

The Group establishes a provision, based on reasonable estimates, for likely outcomes of audits by the tax authorities of the respective countries in which it operates. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences in interpretation may arise for a wide variety of issues depending on the conditions prevailing in the respective domicile of the Group companies.

Deferred tax assets are recognised for unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

A deferred tax asset has not been recognised in relation to unused tax losses that were generated in the Australian Consolidated Tax Group, primarily during FY2017. The Australian Consolidated Tax Group includes the Australia segment and the majority of the Group Corporate overhead which is reported within the Unallocated segment (refer Note 3). The generation of future taxable profit in Australia is dependent upon the award of new vessel contracts and hence the recognition criteria for a deferred tax asset were not met.

## vi Other taxes

Revenues, expenses and assets are recognised net of the amount of Goods Services Tax (GST) except:

- when the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables, which are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross profit basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority, are classified as operating cash flows. Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

## Capital structure

### Note 10 Cash and cash equivalents

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Current</b>		
Cash at bank and in hand	\$ 150,471	\$ 224,318
<b>Total Cash per Cash Flow Statement</b>	<u>\$ 150,471</u>	<u>\$ 224,318</u>

#### i Recognition and measurement

Cash and short-term deposits in the statement of financial position comprise cash at bank and in hand and short-term deposits with an original maturity of three months or less.

Cash and cash equivalents for the purposes of the Consolidated statement of cash flows consists of cash and cash equivalents as defined above, net of cash held as a guarantee.

## Note 11 Interest bearing loans and borrowings

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Current</b>		
Finance Leases	\$ (2,532)	\$ (2,545)
Vessel finance for Cape Class Patrol Boats 9 & 10	(7,336)	-
Total	<u>\$ (9,868)</u>	<u>\$ (2,545)</u>
<b>Non - Current</b>		
Finance Leases	\$ (5,329)	\$ (8,110)
Go Zone Bonds	(123,303)	(136,113)
Vessel finance for Cape Class Patrol Boats 9 & 10	(57,855)	(25,843)
Total	<u>\$ (186,487)</u>	<u>\$ (170,066)</u>
<b>Total</b>	<u>\$ (196,355)</u>	<u>\$ (172,611)</u>

### i Recognition and measurement

All loans, borrowings and finance leases are initially recognised at the fair value of the consideration received less directly attributable transaction costs. Interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Gains and losses are recognised in the statement of comprehensive income when the liabilities are derecognised.

### ii Go Zone Bonds

The Gulf Opportunity Zone Bonds (Go Zone Bonds or GZB) are a form of indebtedness that was authorised by the US Federal Government to incentivise private investment in infrastructure in geographical areas that were affected by Hurricane Katrina in 2005. Austal qualified to borrow US\$225.000 million with a 30 year maturity to invest in the development of shipbuilding infrastructure in Austal USA between FY2008 & FY2013.

Go Zone Bonds are tax-exempt municipal bonds in the United States and attracted an average coupon rate of 0.70% in FY2017. GZB bondholders are secured by letters of credit issued by Austal's banking syndicate with a maturity date of 30 November 2018. The average cost of the letters of credit in FY2017 was 1.54%.

Austal has redeemed (repaid) a cumulative amount of ~ US\$127.960 million of GZB funds and owes US\$97.040 million at 30 June 2017.

### iii Finance leases

Austal USA entered into 5 year Finance leases in FY2015 to fund mobile equipment and a plot of land in Mobile, Alabama, USA, and the following average interest rates were incurred in FY2017:

- mobile equipment 2.0%
- land 2.3%

#### iv Vessel finance for Cape Class Patrol Boats 9 & 10

Austal entered into a finance arrangement with National Australia Bank (NAB) and the Australian Border Force (ABF) for the construction of two Cape Class Patrol Boats (9 & 10) in December 2015.

National Australia Bank financed the purchase of the vessels and is now leasing them to the ABF for an initial 3 year term. Whilst extensions or a future sale of the two vessels is probable, the contract contains a put option granting NAB the right to sell the vessels back to Austal at an option price equal to the residual value of \$21 million per vessel at the end of the 3 year term. The notional effective interest rate incurred in FY2017 was 2.54%.

#### v Banking facilities

Austal has a Syndicated Facility Agreement which matures in October 2018. The Agreement includes US\$97.040 million for letters of credit to secure the Go Zone Bonds and a A\$170.000 million revolving credit facility. The entire revolving credit facility can be used for contingent non-financial instruments, up to \$50.000 million of any unused part of the facility can be used for cash advances and up to \$20.000 million of any unused part of the facility can be used for contingent financial instruments.

Contingent non-financial instruments (excluding the letters of credit supporting the Go Zone Bonds) are issued to support concepts such as refund payment guarantees, performance bonds, warranty bonds (refer to Note 25).

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Facilities used at reporting date</b>		
Finance Leases	\$ (7,861)	\$ (10,655)
Go Zone Bonds	(123,303)	(136,113)
Contingent Instrument Facility	(57,597)	(133,602)
Total	<u>\$ (188,761)</u>	<u>\$ (280,370)</u>
<b>Facilities unused at reporting date</b>		
Contingent Instrument & Cash Loan Facility	\$ (112,403)	\$ (36,398)
Total	<u>\$ (112,403)</u>	<u>\$ (36,398)</u>
<b>Total Facilities Available</b>		
Finance Leases	\$ (7,861)	\$ (10,655)
Go Zone Bonds	(123,303)	(136,113)
Contingent Instrument & Cash Loan Facility	(170,000)	(170,000)
Total	<u>\$ (301,164)</u>	<u>\$ (316,768)</u>

#### vi Fair value of borrowings

The fair values of all classes of borrowings are not materially different to their carrying amounts since the interest payable on those borrowings is either close to current market rates or the borrowings are of a short-term nature. The interest rates on Go Zone Bonds are reset on a weekly basis.

## Note 12 Contributed equity and reserves

	Shares		'000	
	2017	2016	2017	2016
<b>Ordinary Shares on Issue</b>				
1 July	348,393,449	346,923,451	\$ 123,739	121,753
Shares issued during the year	1,079,194	1,469,998	\$ 1,690	\$ 1,986
Transfer of vested Reserved Shares	-	-	2,891	-
Tax expense on employee share plan (AGMSP <sup>1</sup> )	-	-	(44)	-
30 June	349,472,643	348,393,449	\$ 128,276	\$ 123,739
<b>Reserved Shares</b>				
1 July	(4,015,539)	(4,015,539)	\$ (9,001)	\$ (9,230)
Movement in Reserved Shares	-	-	\$ -	\$ 229
Transfer of vested Reserved Shares	-	-	(2,891)	-
30 June	(4,015,539)	(4,015,539)	\$ (11,892)	\$ (9,001)
<b>Net</b>	<b>345,457,104</b>	<b>344,377,910</b>	<b>\$ 116,384</b>	<b>\$ 114,738</b>

1. Austal Group Management Share Plan

### i Recognition and measurement

#### 1. Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds of the new shares or options.

Ordinary shares have no par value and the company does not have a limited amount of authorised capital.

Fully paid ordinary shares carry one vote per share and carry the right to dividends.

A transfer was booked between Reserved Shares and Ordinary Shares on issue with zero movement in total Contributed Equity.

#### 2. Reserved shares

Own equity instruments which are issued and held by a trustee under the Austal Group Management Share Plan are classified as reserved shares and are deducted from equity. No gain or loss is recognised in the statement of comprehensive income on the purchase, sale, issue or cancellation of the Group's own equity instruments.

Refer to Note 30 for more information in relation to the Austal Group Management Share Plan.



## ii Movements in ordinary share capital

	Shares	
	2017	2016
<b>Ordinary Shares on Issue</b>		
1 July	348,393,449	346,923,451
Dividend reinvestment plan	1,079,194	972,814
Performance rights exercised	-	497,184
30 June	<u>349,472,643</u>	<u>348,393,449</u>

The movement in ordinary shares during year ended 30 June 2017 is comprised of shares issued as part of dividends declared and paid during the year.

The Group announced a FY2016 final dividend of 2 cents per share with an option for dividend reinvestment of \$1.52 per share on 23 September 2016, followed by a FY2017 interim dividend of 2 cents per share with an option for dividend reinvestment of \$1.65 per share, which was announced on 27 March 2017.

## iii Nature & purpose of reserves

### 1. Foreign currency translation reserve (FCTR)

This reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

### 2. Employee benefits reserve

This reserve is used to record the value of equity benefits provided to employees and Directors as part of their remuneration. Refer to Note 30 for further details of share based payment plans for the Group.

### 3. Cash flow hedge reserve

This reserve records the portion of the gain or loss on hedging instruments in cash flow hedges that are determined to be an effective hedge.

### 4. Common control reserve

This reserve represents the premium paid on the acquisition of the minority interest in a controlled entity.

### 5. Asset revaluation reserve

This reserve is used to record increases in the fair value of land and buildings.

## Note 13 Government grants relating to assets

	2017 <u>'000</u>	2016 <u>'000</u>
<b>Deferred Grant Income</b>		
<b>Current</b>		
Infrastructure Development	\$ (7,934)	\$ (8,543)
Total	<u>\$ (7,934)</u>	<u>\$ (8,543)</u>
<b>Non - Current</b>		
Infrastructure Development	\$ (62,881)	\$ (71,991)
Total	<u>\$ (62,881)</u>	<u>\$ (71,991)</u>
<b>Total</b>	<u>\$ (70,815)</u>	<u>\$ (80,534)</u>
<b>Movements in Grants</b>		
Opening Balance	\$ (80,534)	\$ (66,966)
Grants received during the year	\$ (1,134)	\$ (16,746)
Amortised to the profit and loss	8,522	4,877
Exchange rate adjustment	2,331	(1,699)
Closing Balance	<u>\$ (70,815)</u>	<u>\$ (80,534)</u>

### i Recognition and measurement

Austral has received grants from various government bodies in the USA to fund the infrastructure required for the expansion of the Group's USA operations in Mobile, Alabama.

The fair value of grants related to assets is credited to a deferred income liability account and is released to profit and loss over the expected useful life of the relevant asset.

The fair value of grants related to expense items is recognised as income over the periods necessary to match the grants on a systematic basis to the costs that it is intended to compensate.

Government grants are only recognised when received or when there is reasonable assurance that the grant will be received and all attaching conditions will be complied with.

## Working capital

### Note 14 Trade and other receivables

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Current</b>		
Trade amounts owing by unrelated entities	\$ 100,701	\$ 128,505
Allowance for doubtful debts	(257)	(165)
Total	<u>\$ 100,444</u>	<u>\$ 128,340</u>

#### i Recognition and measurement

Trade receivables which are within the normal credit terms are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. An allowance for doubtful debts is made when there is objective evidence that the Group will not be able to collect the debts. Bad debts are written off when identified.

#### ii Impaired trade receivables

Individual receivables which are known to be uncollectible are written off by directly reducing the carrying amount. The other receivables are assessed collectively to determine whether there is objective evidence that an impairment has been incurred but not yet been identified. The estimated impairment losses for these receivables are recognised in a separate impairment allowance account. The Group considers that there is evidence of impairment if any of the following indicators are present:

- significant financial difficulties of the debtor
- probability that the debtor will enter bankruptcy or financial reorganisation, and
- default or delinquency in payments (more than 90 days overdue).

Receivables for which an impairment provision was recognised are written off against the provision when there is no expectation of recovering additional cash.

Impairment losses are recognised in profit or loss within other expenses. Subsequent recoveries of amounts previously written off are credited against other expenses.

Refer to Note 23 for an analysis of the Group's credit risk.

### iii Ageing analysis of current trade & other receivables

		Days outstanding				Impaired	Total
		0-30	31-60	61-90	90+		
2017	'000	\$ 83,295	\$ 2,713	\$ 6,352	\$ 8,341	\$ (257)	\$ 100,444
2016	'000	122,506	3,171	1,501	1,327	(165)	128,340

Receivable balances are monitored on an ongoing basis. A major percentage of the trade and other receivables comprises Government institutions and the credit quality is deemed to be of a high quality.

The full trade and other receivables excluding the impairment is deemed to be recovered within the next 12 months.

Any trade and other receivable which is aged greater than 30 days is considered to be overdue.

### iv Fair values of current trade and other receivables

The carrying amount of the receivables is assumed to be the same as their fair value due to their short term nature.

## Note 15 Vessel construction and support contracts in progress

	2017 '000	2016 '000
<b>Work in Progress</b>		
Construction and support revenue recognised to date	\$ 8,010,526	\$ 6,983,610
less Progress payments received & receivable	(7,842,168)	(6,876,021)
Total due from customers	\$ 168,358	\$ 107,589
<b>Progress Payments Received in Advance</b>		
Construction and support revenue recognised to date	\$ 77,146	\$ 22,572
less Progress payments received & receivable	(92,700)	(35,384)
Total due to customers	\$ (15,554)	\$ (12,812)
<b>Total due from / (to) customers</b>	<b>\$ 152,804</b>	<b>\$ 94,777</b>

### i Recognition and measurement

Construction and support work in progress is valued at contract revenue recognised to date, less any provision for anticipated future losses and progress billings. Construction and support profits are recognised on the percentage of completion basis. Percentage of completion is determined by reference to actual costs to date as a proportion of estimated total contract costs.

Refer to Note 23 for an analysis of the Group's credit risk.

### ii Significant accounting judgements and estimates

Refer to Note 4 for details of estimates made regarding construction and support contracts.

## Note 16 Inventories and work in progress

	<u>Notes</u>	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Current</b>			
Work in progress	15	\$ 168,358	\$ 107,589
Other inventory		2,064	1,385
Total		<u>\$ 170,422</u>	<u>\$ 108,974</u>

### i Recognition and measurement

Stock and finished goods are valued at the lower of cost and net realisable value. Cost of stock is determined on the weighted average cost basis.

No inventories are expected to be realised more than 12 months after balance sheet date.

## Note 17 Trade and other payables

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Current</b>		
Trade & other payables owed to unrelated entities <sup>1</sup>	\$ (154,914)	\$ (229,774)
Total	<u>\$ (154,914)</u>	<u>\$ (229,774)</u>

1. Trade payables are unsecured, non-interest bearing and are normally settled on 45 day terms.

### i Recognition and measurement

Trade payables and other payables are carried at amortised costs and represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services.

### ii Fair value of trade and other payables

The carrying amounts of trade and other payables are assumed to be the same as their fair values, due to their short-term nature.

## Infrastructure & other assets

### Note 18 Property, plant and equipment

#### i Net carrying amount

	Freehold				Total
	Land & Buildings	Leasehold Improvements	Plant & Equipment	Capital WIP	'000
	'000	'000	'000	'000	'000
<b>Balance 30 June 2016</b>					
Gross carrying amount at fair value	\$ 420,638	\$ -	\$ -	\$ -	\$ 420,638
Gross carrying amount at cost		46,283	159,453	18,066	223,802
Accumulated Depreciation & Impairment	(52,989)	(5,822)	(94,831)	-	(153,642)
Net Carrying Amount	\$ 367,649	\$ 40,461	\$ 64,622	\$ 18,066	\$ 490,798
<b>Balance 30 June 2017</b>					
Gross carrying amount at fair value	\$ 362,869	\$ 44,879	\$ -	\$ -	\$ 407,748
Gross carrying amount at cost	-	-	218,761	5,670	224,431
Accumulated Depreciation & Impairment	(14,607)	(12,328)	(104,940)	-	(131,875)
Net Carrying Amount	\$ 348,262	\$ 32,551	\$ 113,821	\$ 5,670	\$ 500,304

#### ii Reconciliation of movement for the year

	Freehold				Total
	Land & Buildings	Leasehold Improvements	Plant & Equipment	Capital WIP	'000
	'000	'000	'000	'000	'000
<b>Balance 1 July 2015</b>	<b>\$ 338,795</b>	<b>\$ 19,839</b>	<b>\$ 72,184</b>	<b>\$ 11,704</b>	<b>\$ 442,523</b>
Additions	\$ 905	\$ 215	\$ 14,212	\$ 28,815	\$ 44,147
Transfer in / (out)	463	22,703	242	(23,408)	-
Transfer to Assets Held for Sale	-	-	(2,908)	-	(2,908)
Disposals	-	-	(3,598)	-	(3,598)
Depreciation charge for the year	(10,353)	(2,873)	(15,235)	-	(28,461)
Impairment	-	-	(1,903)	-	(1,903)
Revaluation	28,675	954	-	-	29,629
Exchange Adjustment	9,164	(377)	1,628	955	11,370
Total	\$ 28,854	\$ 20,622	\$ (7,562)	\$ 6,362	\$ 48,276
<b>Balance 1 July 2016</b>	<b>\$ 367,649</b>	<b>\$ 40,461</b>	<b>\$ 64,622</b>	<b>\$ 18,066</b>	<b>\$ 490,798</b>
Additions	\$ 124	\$ 6	\$ 49,097	\$ 3,597	\$ 52,824
Transfer in / (out)	522	11	15,416	(15,949)	0
Disposals	-	-	(100)	-	(100)
Depreciation charge for the year	(9,892)	(6,817)	(13,670)	-	(30,379)
Exchange Adjustment	(10,141)	(1,110)	(1,544)	(44)	(12,839)
Total	\$ (19,387)	\$ (7,910)	\$ 49,199	\$ (12,396)	\$ 9,506
<b>Balance 30 June 2017</b>	<b>\$ 348,262</b>	<b>\$ 32,551</b>	<b>\$ 113,821</b>	<b>\$ 5,670</b>	<b>\$ 500,304</b>



### iii Recognition and measurement

Plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses.

Land and buildings are measured at fair value less accumulated depreciation on buildings and any impairment losses recognised after the date of revaluation. Valuations are performed on a regular basis to ensure that the fair value of a revalued asset does not differ materially from its carrying value.

The carrying amount would be as detailed in the table below, if land and buildings were measured using the cost model.

	2017 <u>'000</u>	2016 <u>'000</u>
<b>Land &amp; Buildings valued using cost model</b>		
Cost	\$ 381,122	\$ 391,399
Accumulated Depreciation & Impairment	(77,063)	(69,169)
Net Carrying Amount	<u>\$ 304,059</u>	<u>\$ 322,230</u>

Any revaluation surplus is recorded in other comprehensive income and hence credited to the asset revaluation reserve in equity, except to the extent that it reverses a revaluation decrease of the same asset previously recognised in the statement of comprehensive income, in which case, the increase is recognised in the profit and loss.

A revaluation deficit is recognised in the statement of comprehensive income except to the extent that it offsets an existing surplus on the same asset recognised in the asset revaluation reserve.

Accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

### iv De-recognition and disposal

An item of property, plant and equipment is derecognised upon disposal or when no further future economic benefits are expected from its use.

Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the profit and loss in the year the asset is derecognised.

### v Key judgements and accounting estimates

#### 1. Impairment of non-financial assets

The Group assesses whether there is an indication that an asset may be impaired at each reporting date. The Group considered impairment triggers including observable indications, significant market, technological, economic or legal changes that have occurred, significant decreases in market interest rates or market rates of return, the market capitalisation of the Group compared to the net assets of the Group, evidence that any major asset or process is obsolete or damaged and other evidence from internal reporting. Refer to in Note 19 for impairment testing of goodwill and non-current assets.

The carrying values of plant and equipment are reviewed for impairment at each reporting date, with the recoverable amount being estimated when events or changes in circumstances indicate the carrying value of the asset may be impaired. The recoverable amount of plant and equipment is the higher of fair value less costs to sell and value in use. The estimated future cash flows are 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 in assessing value in use.

The recoverable amount for an asset that does not generate largely independent cash inflows is determined for the cash-generating unit to which the asset belongs, unless the asset's value in use can be estimated to be close to its fair value.

An impairment exists when the carrying value of an asset or a cash-generating unit exceeds its estimated recoverable amount. The asset or cash-generating unit is then written down to its recoverable amount.

Impairment losses on plant and equipment are recognised in the statement of comprehensive income.

The asset or cash-generating unit that suffered an impairment is tested for possible reversal of the impairment whenever events or changes in circumstances indicate that the impairment may have reversed.

The key assumptions used to determine the recoverable amount for cash-generating units (CGU) are disclosed and further explained in Note 19.

## **2. Estimation of useful lives of assets**

The estimation of the useful lives of assets has been based on historical experience and the condition of the assets is assessed at least once per year and considered against the remaining useful life. Adjustments to useful life are made when considered necessary.

Depreciation is calculated on a straight-line or diminishing value basis over the estimated useful life of the asset.

The following useful lives have been adopted as follows:

- Buildings – 20 to 40 years
- Plant and equipment – 2 to 10 years
- Leasehold improvements – Lease term

The assets' residual values, useful lives and amortisation methods are reviewed, and adjusted at the end of each financial year if appropriate.

## **3. Revaluation of land and buildings**

The Company's land and buildings consist of office properties in Australia and USA. Management determined that these constitute one class of asset under AASB 13, based on the nature, characteristics and risk of the property.

The valuation methodology utilised a market comparison approach based on highest and best use (refer to 0) which is consistent with the Group's current use of the assets.

The cycle of review for independent revaluation has been determined by management to occur every three to five years. In the years between obtaining independent valuations, management undertakes an assessment to ensure that the latest independent valuation remains appropriate and representative of fair value as at balance sheet date.

The last independent revaluation of the Company's land and buildings occurred during FY2016 by independent licensed valuers. The Land and Buildings assets were not revalued during the FY2017 year. There has not been any indication of impairment nor any material change in the valuation of the assets since they were last revalued.

## Note 19 Intangible assets and Goodwill

### i Net carrying amount

	Computer Software '000	Goodwill '000	Total '000
<b>Balance 1 July 2016</b>			
Cost	\$ 17,233	\$ 6,463	\$ 23,696
Accumulated Amortisation & Impairment	(14,400)	-	(14,400)
Net Carrying Amount	<b>\$ 2,833</b>	<b>\$ 6,463</b>	<b>\$ 9,296</b>
<b>Balance 30 June 2017</b>			
Cost	\$ 17,525	\$ 6,463	\$ 23,988
Accumulated Amortisation & Impairment	(15,079)	-	(15,079)
Net Carrying Amount	<b>\$ 2,446</b>	<b>\$ 6,463</b>	<b>\$ 8,909</b>

### ii Reconciliation of movement for the year

	Computer Software '000	Goodwill '000	Total '000
<b>Balance 1 July 2015</b>			
	<b>\$ 3,174</b>	<b>\$ 6,463</b>	<b>\$ 9,637</b>
Additions	\$ 994	-	\$ 994
Amortisation for the year	(1,438)	-	(1,438)
Exchange Adjustment	103	-	103
Total	\$ (341)	-	\$ (341)
<b>Balance 30 June 2016</b>			
	<b>\$ 2,833</b>	<b>\$ 6,463</b>	<b>\$ 9,296</b>
<b>Balance 1 July 2016</b>			
	<b>\$ 2,833</b>	<b>\$ 6,463</b>	<b>\$ 9,296</b>
Additions	\$ 822	-	\$ 822
Amortisation for the year	(1,143)	-	(1,143)
Exchange Adjustment	(66)	-	(66)
Total	\$ (387)	-	\$ (387)
<b>Balance 30 June 2017</b>			
	<b>\$ 2,446</b>	<b>\$ 6,463</b>	<b>\$ 8,909</b>

### iii Recognition and measurement

Intangible assets acquired separately are initially measured at cost and subsequently carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is charged against profit or loss in the year in which the expenditure is incurred.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least once per financial year. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, which is a change in accounting estimate.

The amortisation expense on intangible assets with finite lives is recognised in the statement of comprehensive income in the expense category consistent with the function of the intangible asset.

A summary of the policies applied to the Group's intangible assets is as follows:

### 1. Computer software

Computer software is initially measured at cost and amortised on a straight-line basis over the estimated useful life of each asset. Impairment testing is conducted annually. Computer software is amortised on a straight-line basis over 2 to 5 years.

### 2. Goodwill

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interest over the net identifiable assets acquired and liabilities assumed in a business combination.

Goodwill is measured at cost less any accumulated impairment losses after initial recognition. Goodwill acquired in a business combination is allocated to each of the Group's cash-generating units that are expected to benefit from the combination from the acquisition date for the purpose of impairment testing, irrespective of whether other assets or liabilities acquired are assigned to those units.

Goodwill is tested annually for impairment regardless of whether impairment triggers are identified. The Impairment is determined for goodwill by assessing the recoverable amount of each Cash Generating Unit (CGU) (or Group of CGU) to which the goodwill relates. An impairment loss is recognised when the recoverable amount of the CGU is less than its carrying amount. Impairment losses relating to goodwill cannot be reversed in future periods.

Goodwill allocated to a cash-generating unit that has a partial disposal of the operation within that unit is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the cash-generating unit retained.

### 3. Impairment testing of goodwill and non-current assets

Non-current assets are reviewed on an annual basis in accordance with the Group's accounting policies, to determine whether there is an impairment indicator. An estimate of the recoverable amount is made where an impairment indicator exists.

The recoverable amounts have been assessed at the CGU level as identified below:

- Australia
- USA
- Philippines

Corporate assets have been allocated to CGU to the extent that they relate to the CGU.

Goodwill, with a carrying amount of \$6.4 million at 30 June 2017, acquired through business combinations has been allocated to the Australia segment (refer to Note 3 for details).

The recoverable amounts, excluding charter vessels that are assessed independently, for each CGU have been determined based on value in use calculations using cash flow projections from financial budgets approved by senior management covering a five-year period. Key inputs into the budget include contracted and projected vessels.

Management concluded that the recoverable amount is greater than the carrying amount and that no impairment charge is required as a result of this analysis.

#### iv Significant accounting judgement and estimates

##### 1. Recoverable amount of the CGU

The following table sets out the key assumptions:

<u>CGU</u>	<u>Australia</u>	<u>USA</u>	<u>Philippines</u>
Growth assumptions	Award of Projected vessels	Award of Projected vessels	Award of Projected vessels
Perpetuity growth rate	0.0%	0.0%	0.0%
Pre-tax discount factor	13.7%	15.6%	12.2%
Inflation on costs	2.0%	1.5%	2.5%

##### 2. Growth assumptions

Growth assumptions are based on future vessel construction and service projects to be awarded. These contracts are based on tender price or historical experience on the size of the vessel.

##### 3. Perpetuity growth rate

Management has taken a conservative view and included a 0% perpetuity growth rate in calculation of the terminal value.

##### 4. Pre-tax discount factor

Discount rates represent the current market assessment of the risks specific to each CGU, taking into consideration the time value of money and individual risks of the underlying assets that have not been incorporated in the cash flow estimates.

##### 5. Inflation on costs

Estimates are obtained from published indices for the countries from which materials are sourced, as well as data relating to specific commodities. Forecast figures are used if data is publically available, otherwise past actual raw material price movements are used as an indicator of future price movements.

##### 6. Sensitivity to changes in assumptions

Any change in the key assumptions used to determine the recoverable amount would result in a change in the assessed recoverable amount (excluding charter vessels that are assessed independently). An impairment of assets may result if the variation in assumption has a negative impact on the recoverable amount.

The estimated recoverable amounts of each of the CGU are significantly greater than the carrying value of the assets within the respective CGU. No reasonably foreseeable changes in any of the key assumptions are likely to result in an impairment loss.

## Note 20 Other financial assets

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
<b>Other financial assets</b>		
Collateral <sup>1</sup>	\$ 9,467	\$ 7,476
Security deposits	159	162
Total	<u>\$ 9,626</u>	<u>\$ 7,638</u>

1. Legal requirement in the USA to provide cash collateral to ensure that workers' compensation claims will be paid if they eventuate.

### i Recognition and measurement

Collateral in the statement of financial position comprises cash at bank with an original maturity of twelve months or more. Collateral and security deposits are classified as receivables and measured at amortised cost.

## Other liabilities

### Note 21 Provisions

	Employee Benefits '000	Workers' Compensation '000	Warranty '000	Other '000	Total '000
<b>Provisions at 30 June 2016</b>	\$ (23,193)	\$ (3,591)	\$ (14,388)	\$ (2,171)	\$ (43,343)
Arising during the year	\$ (76,267)	\$ (6,718)	\$ (6,315)	\$ (57,708)	\$ (147,008)
Utilised	71,985	6,400	5,987	53,657	138,029
Unused amounts reversed	1,020	-	1,160	-	2,180
Effects of foreign exchange	483	115	22	72	692
Movement	\$ (2,779)	\$ (203)	\$ 854	\$ (3,979)	\$ (6,107)
<b>Provisions at 30 June 2017</b>	\$ (25,972)	\$ (3,794)	\$ (13,534)	\$ (6,150)	\$ (49,450)

	Employee Benefits '000	Workers' Compensation '000	Warranty '000	Other '000	Total '000
<b>2016</b>					
Current	\$ (22,141)	\$ (3,591)	\$ (14,388)	\$ (2,171)	\$ (42,291)
Non-Current	(1,052)	-	-	-	(1,052)
Total	\$ (23,193)	\$ (3,591)	\$ (14,388)	\$ (2,171)	\$ (43,343)
<b>2017</b>					
Current	\$ (24,628)	\$ (3,794)	\$ (13,534)	\$ (4,630)	\$ (46,586)
Non-Current	(1,344)	-	-	(1,520)	(2,864)
Total	\$ (25,972)	\$ (3,794)	\$ (13,534)	\$ (6,150)	\$ (49,450)

#### i Recognition and measurement

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Provisions are discounted using a current pre-tax rate that reflects the risks specific to the liability if the effect of the time value of money is material.

The increase in the provision due to the passage of time is recognised as a finance cost when discounting is used.

## ii Information about individual provisions and significant accounting estimates

### 1. Employee Benefits

Liabilities for wages and salaries, including non-monetary benefits and accumulating sick leave expected to be wholly settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled.

The Group does not expect its long service leave and annual leave benefits provision to be settled wholly within 12 months of each reporting date. The Group recognises a liability for long service and annual leave measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Consideration is given to expected future wage and salary levels, experience of employee departures, and periods of service. Expected future payments are discounted using market yields at the reporting date on high quality corporate bonds with terms to maturity and currencies that match, as closely as possible, the estimated future cash outflows.

### 2. Warranties

Provision for warranty is made upon delivery of the vessels based on the estimated future costs of warranty repairs on vessels. The estimated future costs are based on the Group's history of warranty claims on similar vessels of currently and known vessels that are in warranty periods.

### 3. Workers' compensation insurance

A provision for workers' compensation insurance is recognised for the expected costs of current claims and claims incurred but not reported at the balance date.

### 4. Others

Loss provisions are established when it is probable that a contract may be deemed onerous. An onerous contract arises when estimated total contract costs will exceed estimated total contract revenue, in which case the estimated loss must be immediately recognised in the Statement of Comprehensive Income (Profit & Loss).

Other provisions at 30 June 2017 includes a \$(3.233) m loss provision for the Cape Class Patrol Boat In Service Support Contract (CCPB ISS) with the Australian Border Force (ABF) which was deemed onerous at 30 June 2017. The cost of resources required to deliver upon the contracted services through to the maturity date on 1 August 2019 were estimated to exceed the contract revenues at reporting date and hence a provision was booked with a corresponding expense in Profit & Loss. The ABF has an option to extend the contract in unspecified increments up to a total duration of 12 years from 1 August 2019. A loss provision for an extension period beyond 1 August 2019 has not been recognised on the basis that the option to extend has not been exercised, and the total duration of extensions is indeterminate at reporting date. Austal would protest the extension of an onerous contract beyond the original term and the cost of estimating an exit or continuation cannot be reliably measured at reporting date. There is a risk that Austal may bear additional cost associated with this contract.



## 5. Dividends

A provision for dividends is not recognised as a liability unless the dividends are declared, determined or publicly recommended on or before the reporting date. A dividend of 2 cents per share was issued for the half year 31 December 2016 (FY2016 H1: 2 cents).

A final fully franked dividend of "2" cents per share is proposed and not recognised as a liability for the year ended 30 June 2017 (FY2016 final fully franked proposed and not recognised: 2 cents).



Mols is the largest passenger ferry to be constructed at Henderson since 2013 and the largest ever by volume, by Austal in 29 years.

## Note 22 Fair value measurements

### i Financial assets and financial liabilities

The Group holds the following financial instruments:

<b>Financial Assets</b>	<b>Notes</b>	<b>Derivatives used for hedging at fair value '000</b>	<b>Assets at amortised cost '000</b>	<b>Total '000</b>
<b>2017</b>				
Cash and cash equivalents	10	\$ -	\$ 150,471	\$ 150,471
Trade & other receivables	14	-	100,444	100,444
Other financial assets	20	-	9,626	9,626
Derivatives	23	3,036	-	3,036
Total		<u>\$ 3,036</u>	<u>\$ 260,541</u>	<u>\$ 263,577</u>
<b>2016</b>				
Cash and cash equivalents	10	\$ -	\$ 224,318	\$ 224,318
Trade & other receivables	14	-	128,340	128,340
Other financial assets	20	-	7,638	7,638
Derivatives	23	487	-	487
Total		<u>\$ 487</u>	<u>\$ 360,296</u>	<u>\$ 360,783</u>
<b>Financial Liabilities</b>				
	<b>Notes</b>	<b>Derivatives used for hedging at fair value '000</b>	<b>Liabilities at amortised cost '000</b>	<b>Total '000</b>
<b>2017</b>				
Trade & other payables	17	\$ -	\$ (154,914)	\$ (154,914)
Derivatives	23	(5,125)	-	(5,125)
Interest bearing borrowings	11	-	(196,355)	(196,355)
Total		<u>\$ (5,125)</u>	<u>\$ (351,269)</u>	<u>\$ (356,394)</u>
<b>2016</b>				
Trade & other payables	17	\$ -	\$ (229,774)	\$ (229,774)
Derivatives	23	(16,402)	-	(16,402)
Interest bearing borrowings	11	-	(172,611)	(172,611)
Total		<u>\$ (16,402)</u>	<u>\$ (402,385)</u>	<u>\$ (418,787)</u>

The Group's exposure to various risks associated with the financial instruments is discussed in Note 23. The maximum exposure to credit risk at the end of the reporting period is the carrying amount of each class of financial asset mentioned above.

The fair value of assets and liabilities held at amortised cost is described in the associated note referenced in the table above.

## 1. Fair value measurements - fair value hierarchy

This section explains the judgements and estimates made in determining the fair values of the financial instruments that are recognised and measured at fair value in the financial statements. The Group has classified its financial instruments into the three levels prescribed under the accounting standards to provide an indication about the reliability of the inputs used in determining fair value. An explanation of each level follows underneath the table.

	Notes	Level 1 '000	Level 2 '000	Level 3 '000	Total '000
<b>Balance 30 June 2017</b>					
<b>Financial assets</b>					
Derivatives	23	\$ -	\$ 3,036	\$ -	\$ 3,036
<b>Financial liabilities</b>					
Derivatives	23	\$ -	\$ (5,125)	\$ -	\$ (5,125)
<b>Balance 30 June 2016</b>					
<b>Financial assets</b>					
Derivatives	23	\$ -	\$ 487	\$ -	\$ 487
<b>Financial liabilities</b>					
Derivatives	23	\$ -	\$ (16,402)	\$ -	\$ (16,402)

There were no transfers between any of the levels for recurring fair value measurements during the year.

### Level 1

The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the Group is the current bid price. These instruments are included in level 1.

### Level 2

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques which maximise the use of observable market data and rely as little as possible on entity-specific estimates. The instrument is included in level 2 if all significant inputs required to fair value an instrument are observable.

The Group enters into derivative financial instruments with various counterparties, principally financial institutions with investment grade credit ratings. Foreign exchange forward contracts are valued using valuation techniques, which employs the use of market observable inputs. The most frequently applied valuation techniques include forward pricing and swap models, using present value calculations. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates, yield curves of the respective currencies, currency basis spreads between the respective currencies, interest rate curves and forward rate curves of the underlying commodity. The fair value of derivative asset positions at 30 June 2017 is net of a credit valuation adjustment attributable to derivative counterparty default risk. The changes in counterparty credit risk had no material effect on the hedge effectiveness assessment for derivatives designated in hedge relationships and other financial instruments recognised at fair value.

### Level 3

The instrument is included in level 3 if one or more of the significant inputs is not based on observable market data.

## ii Impairment – Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset which is measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows, discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in Groups that share similar credit risk characteristics.

All impairment losses are recognised in profit or loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. The reversal is recognised in profit or loss for financial assets measured at amortised cost.

Impairment testing of trade receivables is described in Note 14.

## iii Non-financial assets and liabilities

This section explains the judgements and estimates made in determining the fair values of the non-financial instruments that are recognised and measured at fair value in the financial statements. The Group has classified its non-financial assets and liabilities measured at fair value into the three levels prescribed under the accounting standards to provide an indication about the reliability of the inputs used in determining fair value.

	Notes	Level 1 '000	Level 2 '000	Level 3 '000	Total '000
<b>Balance 30 June 2017</b>					
Land & buildings	18	\$ -	\$ -	\$ 348,262	\$ 348,262
<b>Balance 30 June 2016</b>					
Land & buildings	18	\$ -	\$ -	\$ 367,649	\$ 367,649

There were no transfers between any of the levels for recurring fair value measurements during the year.

## 2. Valuation techniques used to determine fair values

The Group engages independent accredited valuation specialists on a periodic basis to determine the fair values of these assets. The Group reviews market indicators in the interim periods to ensure that the carrying value of revalued property is not materially different from fair value.

The revaluations were performed by independent valuers, with valuation dates of 31 December 2015. The valuation methodology utilised a market comparison approach for land and property, and a depreciated replacement cost approach for buildings based on highest and best use, which is consistent with the Group's current use of the assets. This valuation method is classified as level 3, under the fair value hierarchy.

	Date of valuation	Level 1 '000	Level 2 '000	Level 3 '000	Total '000
<b>Balance 30 June 2017</b>					
<b>Financial assets</b>					
Land and buildings	31 Dec 2015	\$ -	\$ -	\$ 392,419	\$ 392,419
Total		\$ -	\$ -	\$ 392,419	\$ 392,419
<b>Balance 30 June 2016</b>					
<b>Financial assets</b>					
Land and buildings	31 Dec 2015	\$ -	\$ -	\$ 392,419	\$ 392,419
Total		\$ -	\$ -	\$ 392,419	\$ 392,419

## 3. Valuation inputs and relationships to fair value

The following table summarises the quantitative information about the significant unobservable inputs used in recurring level 3 fair value measurements.

Description	Fair value at 30 June 2017 '000	Unobservable inputs	Range of inputs (probability-weighted average)	Relationship of unobservable inputs to fair value
Land - Mobile	US\$30,700	Selection of land with similar approximate utility	US\$3.89 - US\$4.67 (US\$4.25) per ft <sup>2</sup>	Higher value of similar land increases estimated fair value
Buildings - Mobile	US\$223,491	Cost per square foot floor area (ft <sup>2</sup> )	US\$100 - \$212.36 (\$189.58) per ft <sup>2</sup>	Higher cost per ft <sup>2</sup> increases fair value.
Land - Henderson	\$ 12,250	Selection of land with similar approximate utility	\$225-275 (\$250) per m <sup>2</sup>	Higher value of similar land increases estimated fair value
Buildings - Henderson	\$ 19,206	Consumed economic benefit/ obsolescence of asset	2.50%	Greater consumption of economic benefit or increased obsolescence lowers fair value.
		Cost per square meter floor area (m <sup>2</sup> )	\$500 - \$1,750 (\$998) per m <sup>2</sup>	Higher cost per m <sup>2</sup> increases fair value.

## Note 23 Financial risk management

This note explains the Group's exposure to financial risks and how these risks could affect the Group's future financial performance. Current year profit and loss information has been included where relevant to add further context.

<b>Risk</b>	<b>Exposure arising from</b>	<b>Monitoring</b>	<b>Management</b>
Market risk - interest rate	Long-term borrowings at variable rates	Sensitivity analysis	Sustainable gearing levels through business cycles
Market risk - interest rate	Cash	Sensitivity analysis	Excess cash investment within high interest deposit accounts
Market risk - foreign currency	Future commercial transactions, recognised financial assets and liabilities not denominated in functional currency	Cash flow forecast, Sensitivity analysis	Forward foreign exchange contracts, Forward currency options
Credit risk	Cash, short term deposits, trade receivables and derivative financial instruments	Ageing analysis, credit ratings	Monitoring credit allowances
Liquidity	Borrowings, trade payables and derivative financial instruments	Rolling cash flow forecasts	Availability of committed credit lines and borrowing facilities

### i Objectives and policy

The objective of the Group's financial risk management policy is to reduce the impacts of external threats to the Group, and to afford the opportunity to seek further investments.

Ultimate responsibility for identification and control of financial risks rests with the Board of Directors. The Board reviews and agrees policies for managing each of the risks identified below, including hedging cover of foreign currency, credit allowances, and future cash flow forecast projections.

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

### ii Market risk

#### 1. Capital management

The Group undertakes capital management to ensure that secure and flexible funding resources are available to meet all operating and capital expenditure requirements.

The Group's policy is to maintain a strong and flexible capital base to provide investor, creditor and market confidence to sustain future development of the business. The Group monitors the return on capital, which the Group defines as total shareholders' equity attributable to members of Austal Limited. The Board determines the level of dividends to shareholders.

The Group monitors statement of financial position strength and flexibility using cash flow forecast analysis and detailed budgeting processes. The gross gearing ratio is monitored and maintained at a level that does not limit the Group's growth opportunities and is in line with peers and industry norms.

There were no changes in the Group's approach to capital management during the year. Risk management policies and procedures are established with regular monitoring and reporting.

Neither the Group nor any of its subsidiaries are subject to externally imposed capital requirements, other than normal banking requirements.

## 2. Interest rate risk exposure

Interest rate risk management is undertaken by the Group in order to reduce the potential volatility towards its financial position due to fluctuations in prevailing market interest rates.

The Group's exposure to market interest rates relates primarily to the Group's long-term debt obligations and investment in cash funds.

The Group constantly analyses its interest rate exposure. Consideration is given to potential renewal of existing positions and alternative financing structures.

The Group had the following variable rate borrowings outstanding at the end of the reporting period.

	<b>2017</b>	<b>2016</b>
	<b>'000</b>	<b>'000</b>
<b>Financial Assets</b>		
<b>Cash and cash equivalents</b>		
Australian variable rate interest	\$ 5,227	\$ 79,165
US variable rate interest	138,481	137,713
Other variable rate interest	6,791	7,440
Total	<u>\$ 150,499</u>	<u>\$ 224,318</u>
<b>Financial Liabilities</b>		
<b>Interest bearing loans and borrowings</b>		
US variable rate interest	\$ (134,116)	\$ (151,028)
Total	<u>\$ (134,116)</u>	<u>\$ (151,028)</u>
<b>Net Exposure</b>	<u>\$ 16,383</u>	<u>\$ 73,290</u>

Profit or loss is sensitive to higher / lower interest income from cash and cash equivalents and interest expenses on borrowings as a result of changes in interest rates. There would be no material impact on other components of equity as a result of changes in interest rates. The sensitivity analysis below shows the impact on post tax profit had a 25 basis point movement in interest rates occurred. 25 basis points was deemed to be a reasonable level of volatility based on FY2017 observations.

	<b>2017</b>	<b>2016</b>
	<b>'000</b>	<b>'000</b>
<b>Post tax gain / (loss)</b>		
<b>AUD</b>		
+0.25% (25 basis points)	\$ 37	\$ 383
-0.25% (25 basis points)	(37)	(383)
<b>USD</b>		
+0.25% (25 basis points)	\$ 31	\$ (83)
-0.25% (25 basis points)	(31)	83

### iii Interest rate risk strategies, policies and procedures

The cash, debt, bank covenants and interest cover ratio of the Group are forecasted and monitored on a monthly basis in order to forecast and monitor the interest rate risk. A variable interest rate is maintained because repayments are carried out as soon as practicable, where a fixed interest rate is less flexible. The interest rate exposure is currently immaterial.

### iv Foreign currency risk

Refer to Note 24 for Derivatives.

The Group is exposed to currency risk on sales, purchases or components for construction that are denominated in a currency other than the respective functional currencies of the Group entities, primarily Australian Dollars (AUD) for the Australian operation and US Dollars (USD) for the USA and Philippines operations. These transactions are primarily denominated are AUD, USD and EUR.

The Group's objective in relation to foreign currency risk is to minimise the risk of a variation in the rate of exchange used to convert foreign currency revenues and expenses and assets or liabilities to the functional currency of each cash generating unit.

The Group limits the exposure to adverse movement in exchange rates in the following ways:

- negotiation of contracts to adjust for adverse exchange rate movements
- use of natural hedges
- using financial instruments (refer to Note 24).

Sales contracts are negotiated based at the current market rate on the contract signing date. The Group seeks to mitigate significant foreign currency exposures in contract tenders by incorporating rise and fall clauses for exchange rate movements between the date of price calculation to the date the contract becomes effective.

The Group's financial assets and liabilities exposed to foreign currency risk at the end of the reporting period were as follows:



All values are stated in AUD equivalents					
	AUD '000	USD <sup>1</sup> '000	EUR '000	Other '000	Total '000
<b>Balance 30 June 2017</b>					
<b>Financial assets</b>					
Cash and cash equivalents	\$ 41	\$ 11,230	\$ 1,951	\$ 1,714	\$ 14,936
Trade and other receivables	-	1,311	2,548	668	4,527
Derivatives	717	874	3,482	53	5,126
<b>Total</b>	<b>\$ 758</b>	<b>\$ 13,415</b>	<b>\$ 7,981</b>	<b>\$ 2,435</b>	<b>\$ 24,589</b>
<b>Financial liabilities</b>					
Trade and other payables	\$ (769)	\$ (2,689)	\$ (232)	\$ (534)	\$ (4,224)
Derivatives	(398)	(9)	(2,524)	(106)	(3,037)
<b>Total</b>	<b>\$ (1,167)</b>	<b>\$ (2,698)</b>	<b>\$ (2,756)</b>	<b>\$ (640)</b>	<b>\$ (7,261)</b>

All values are stated in AUD equivalents					
	AUD '000	USD <sup>1</sup> '000	EUR '000	Other '000	Total '000
<b>Balance 30 June 2016</b>					
<b>Financial assets</b>					
Cash and cash equivalents	\$ 12	\$ 3,744	\$ 2	\$ 1,135	\$ 4,893
Trade and other receivables	-	11,216	2,308	1,447	14,971
Derivatives	2,778	2,724	10,834	60	16,396
<b>Total</b>	<b>\$ 2,790</b>	<b>\$ 17,684</b>	<b>\$ 13,144</b>	<b>\$ 2,642</b>	<b>\$ 36,260</b>
<b>Financial liabilities</b>					
Trade and other payables	\$ (17,651)	\$ (3,804)	\$ (9)	\$ (423)	\$ (21,887)
Derivatives	(102)	(41)	(322)	-	(465)
<b>Total</b>	<b>\$ (17,753)</b>	<b>\$ (3,845)</b>	<b>\$ (331)</b>	<b>\$ (423)</b>	<b>\$ (22,352)</b>

1. Spot USD / AUD rate at 30 June 2017 was 0.7686 (30 June 2016: 0.7450)
2. Spot EUR / AUD rate at 30 June 2017 was 0.6722 (30 June 2016: 0.6705 )

Known foreign exchange transaction exposures which result from normal operational business activities, are hedged utilising financial instruments.

Net profit after tax and equity would have been affected as illustrated below had the AUD, USD and EUR moved relative to one another at balance date with all other variables held constant:

Judgement of reasonable possible movements	Post tax profit higher / (lower)		Equity higher / (lower)	
	2017 '000	2016 '000	2017 '000	2016 '000
<b>USD / AUD</b>				
+10%	\$ 1,581	\$ 971	\$ 2,097	\$ 1,408
-10%	(1,581)	(971)	(2,217)	(1,639)
<b>EUR / AUD</b>				
+10%	\$ -	\$ -	\$ (4,385)	\$ (4,037)
-10%	-	-	5,360	4,934

Derivative financial instruments such as forward currency contracts and currency options are utilised to eliminate foreign currency exposures. Timing gaps are mitigated using foreign currency accounts or financial instruments such as swaps.

The Group's policy is to negotiate the terms of the hedge derivatives to match the terms of the hedged item to maximise hedge effectiveness.

Speculative trading is specifically prohibited. The financial impact of the derivative instrument is incorporated into the cost of goods acquired or the sales proceeds. General hedges are not undertaken.

Foreign currency contracts designated as cash flow hedges to mitigate the movements in foreign exchange rates are outlined in Note 24.

## v Credit risk

The Group trades only with recognised, creditworthy third parties. The Group's policy is that all customers who wish to trade on credit terms are subject to credit verification procedures, which are conducted internally. The Group, while exposed to credit related losses in the event of non-performance by counterparties to financial instruments, does not expect counterparties to fail to meet their obligations given their credit ratings.

The Group minimises concentrations of credit risk and the risk of default of counterparties in relation to cash and cash equivalents and financial instruments by spreading them amongst a number of financial institutions.

The Group's policy is to minimise the risk that the principle amount will not be recovered and the risk that funds will not be available when required whilst at the same time obtaining the maximum return relative to the risk. The Group's policy is to restrict its investment of surplus cash funds to financial institutions with a Standard and Poor credit rating of at least A-2, and for a period not exceeding 180 days to manage this risk. The Group undertakes investments in short term deposits, term deposits or negotiable certificates of deposit in order to achieve this objective.

Vessel sales contracts are structured to ensure that the Group will be paid on delivery of the vessel through the following measures:

- obtaining progress payments from the client to cover the cost of the construction; or
- obtaining a letter of credit from a credible bank to cover payment of the contract; or
- obtaining a minimum payment of 20% of the contract price and a letter from the bank or financial institution providing finance to the customer that funding has been arranged for the balance of the purchase price.

The Group's exposure to counter party credit default risk arising from the other financial assets of the Group, which comprise cash and cash equivalents and certain derivative instruments, is equal to the carrying amount of these instruments. The maximum exposure to credit risk at the reporting date is disclosed in Note 24.

Cash and term deposits are predominantly held with two tier one Australian and US financial institutions, which are considered to be low concentrations of credit risk.

## vi Liquidity risk

The liquidity position of the Group is managed to ensure sufficient liquid funds are available to meet financial commitments in a timely and cost-effective manner.

The Group's policy is to continually review the Group's liquidity position including cash flow forecasts to determine the forecast liquidity position and maintain appropriate liquidity levels. Austal executed a new syndicated banking facility during FY2016. The syndicated facility agreement matures in October 2018, and hence all liabilities relating to the facility agreement have been disclosed as non-current at the reporting date.

The contractual maturities of financial liabilities, including interest payments are as follows:

	Carrying Amount '000	Years to maturity				Contractual Cash Flows (ii) '000
		0 - 1 '000	1 - 2 '000	2 - 5 '000	> 5 '000	
<b>Balance 30 June 2017</b>						
<b>Derivative financial assets / (liabilities)</b>						
Outflow	\$ (253,996)	\$ (160,799)	\$ (76,004)	\$ (21,362)	\$ -	\$ (258,165)
Inflow	217,666	139,341	63,872	17,957	-	221,170
Net derivative financial assets / (liabilities)	\$ (36,330)	\$ (21,458)	\$ (12,132)	\$ (3,405)	\$ -	\$ (36,995)
<b>Non Derivative financial liabilities</b>						
Trade & other payables	\$ (154,914)	\$ (154,914)	\$ -	\$ -	\$ -	\$ (154,914)
Go Zone Bond facility (i)	(123,303)	(10,908)	(11,412)	(35,449)	(68,457)	(126,226)
Finance lease	(7,861)	(2,684)	(2,631)	(2,795)	-	(8,110)
Vessel finance for Cape Class Patrol Boats 9 & 10 (iii)	(65,192)	-	-	(42,000)	-	(42,000)
Total	\$ (351,270)	\$ (168,506)	\$ (14,043)	\$ (80,244)	\$ (68,457)	\$ (331,250)

(i) Go Zone Bonds are classified with 1 to 2 years to maturity because the letters of credit securing the bonds mature in October 2018.

(ii) Contractual cash flows include interest

(iii) Contractual cashflows are equal to the residual value of the vessels. Refer to Note 11 for further information.

	Carrying Amount '000	Years to maturity				Contractual Cash Flows '000
		0 - 1 '000	1 - 2 '000	2 - 5 '000	> 5 '000	
<b>Balance 30 June 2016</b>						
<b>Derivative financial assets / (liabilities)</b>						
Outflow	\$ (257,952)	\$ (104,852)	\$ (153,088)	\$ (4,228)	\$ -	\$ (262,168)
Inflow	242,817	94,230	148,640	4,034	-	246,904
Net derivative financial assets / (liabilities)	\$ (15,135)	\$ (10,622)	\$ (4,448)	\$ (194)	\$ -	\$ (15,264)
<b>Non Derivative financial liabilities</b>						
Trade & other payables	\$ (229,774)	\$ (229,774)	\$ -	\$ -	\$ -	\$ (229,774)
Go Zone Bond facility	(136,113)	(4,210)	(4,210)	(141,725)	-	(150,145)
Finance lease	(10,655)	(2,544)	(2,631)	(7,769)	(333)	(13,277)
Revolving Credit Facility	(25,843)	-	(11,221)	(15,478)	-	(26,699)
Total	\$ (402,385)	\$ (236,528)	\$ (18,062)	\$ (164,972)	\$ (333)	\$ (419,895)

The Group had \$112.403 million (FY2016: \$36.398 million) of unused credit facilities available for immediate use at balance date (Note 11) and \$150.471 million (FY2016: \$224.318 million) in cash and cash equivalents, which can be used to meet its liquidity needs.

## Note 24 Derivative financial instruments and hedging

The Group is exposed to the risk of adverse movements in the Australian Dollar, US Dollar and Euro relative to each other arising from receipts from export sales and the purchase of components for construction.

The Group uses derivative financial instruments such as forward exchange contracts and forward currency options to hedge its risks associated with foreign currency fluctuations. These contracts are matched to highly probable receipts and payments and they are timed to mature when the receipts and payments are scheduled to be received and made.

### i Recognition and measurement

Derivative financial instruments are stated at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Any gains or losses arising from changes in the fair value of derivatives are taken to the statement of profit and loss, except for those that qualify as cash flow hedges, which are taken to cash flow hedge reserve in other comprehensive income.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. Credit risk has been included in foreign currency contracts.

The Group's derivatives are categorised in level 2 of the valuation hierarchy, because their fair value has been calculated using valuation techniques where the inputs that have a significant effect on the valuation are directly or indirectly based on market observable data.

### ii Hedge designation

For the purposes of hedge accounting, hedges are classified as:

- fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment other than foreign currency risk; or
- cash flow hedges when they hedge exposure to variability in cash flows that is attributable either to a particular risk associated with a recognised asset or liability or foreign exchange risks on firm commitments.

The Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge at the inception of a hedge relationship.

The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk.

Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

### iii Fair value hedge accounting

Fair value hedges are hedges of the Group's exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment other than foreign exchange rate risk, or an identified portion of such an asset, liability or firm commitment that is attributable to a particular risk and could affect profit or loss. The carrying amount of a hedged item is adjusted for gains and losses attributable to the risk being hedged, the derivative is remeasured to fair value and gains and losses from both are taken to the statement of comprehensive income.

The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised to the statement of comprehensive income. Amortisation may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

### iv Cash flow hedge accounting

Cash flow hedges are hedges of the Group's exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction and the foreign exchange risks on firm commitments and that could affect profit or loss. The effective portion of the gain or loss on the hedging instrument is recognised directly in other comprehensive income, while the ineffective portion is recognised in the profit and loss.

Amounts taken to other comprehensive income are transferred to the profit and loss when the hedged transaction affects profit or loss, such as when hedged income or expenses are recognised or when a committed and future sale or the asset is consumed. The amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability when the hedged item is the cost of a non-financial asset or liability.

Amounts previously recognised in equity are transferred to the profit and loss if the forecast transaction is no longer expected to occur. Amounts previously recognised in equity will remain in equity until the forecast transaction occurs if the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked.

## v Summary of forward foreign exchange contracts

The following table summarises the AUD value of the significant forward foreign exchange agreements by currency. Foreign currency amounts are translated at rates current at the reporting date. The 'buy' amounts represent the Australian dollar equivalent of commitments to purchase foreign currencies, and the 'sell' amount represents the Australian dollar equivalent of commitments to sell foreign currencies.

	2017				2016			
	Average Forward Rate	Buy '000	Average Forward Rate	Sell '000	Average Forward Rate	Buy '000	Average Forward Rate	Sell '000
<b>USD / AUD</b>		<b>AUD</b>		<b>AUD</b>		<b>AUD</b>		<b>AUD</b>
less than 3 months	0.8527	\$ 8,018	0.7584	\$ (132)	0.8047	\$ 8,456	0.7655	\$ (261)
3 - 12 months	0.8373	3,782	-	-	0.8214	24,853	0.7246	(6,070)
> 12 months	0.7569	11,668	-	-	0.8228	13,832	0.7259	(565)
Total		<u>\$ 23,468</u>		<u>\$ (132)</u>		<u>\$ 47,141</u>		<u>\$ (6,896)</u>
<b>EUR / AUD</b>								
less than 3 months	0.6471	\$ 7,701	0.6505	\$ (80)	-	\$ -	0.5930	\$ (349)
3 - 12 months	0.6467	13,764	0.6300	(23)	-	-	0.6271	(2,676)
> 12 months	0.6294	51,071	-	-	0.6355	69,333	0.6351	(103)
Total		<u>\$ 72,536</u>		<u>\$ (103)</u>		<u>\$ 69,333</u>		<u>\$ (3,128)</u>
<b>USD / EUR</b>		<b>EUR</b>		<b>EUR</b>				
less than 3 months	1.2309	\$ 1,827	1.0577	\$ (3,061)	-	\$ -	1.1328	\$ (253)
3 - 12 months	1.2030	38,062	1.0691	(7,050)	-	-	1.2789	(50,831)
> 12 months	1.2136	24,383	-	-	-	-	1.2831	(67,222)
Total		<u>\$ 64,272</u>		<u>\$ (10,111)</u>		<u>\$ -</u>		<u>\$ (118,306)</u>

## vi Offsetting financial instruments

The Group presents its assets and liabilities on a gross basis. Derivative financial instruments entered into by the Group are subject to enforceable master netting arrangements such as International Swaps and Derivatives Associations (ISDA) master netting agreement. All outstanding transactions under an ISDA agreement are terminated in certain circumstances, for example, when a credit event such as a default occurs. The termination value is assessed and only a single net amount is payable in settlement of all transactions.

The amounts set out in the table above represent the derivative financial assets and liabilities of the group that are subject to the above arrangements and are presented on a gross basis.

## Unrecognised items

### Note 25 Commitments and contingencies

The Group entities may have potential financial liabilities that could arise from historical commercial contracts. No material losses are anticipated in respect of any of those contingencies.

	2017 '000	2016 '000
<b>Operating lease commitments</b>		
<b>Future minimum rentals payable under non-cancellable leases as at 30 June are as follows</b>		
Within one year	\$ (2,552)	\$ (2,947)
After one year but not more than five years	(6,244)	(6,291)
Total	<u>\$ (8,796)</u>	<u>\$ (9,238)</u>
<b>Capital commitments</b>		
No material commitments	\$ -	\$ -
Total	<u>\$ -</u>	<u>\$ -</u>
<b>Guarantees</b>		
Bank performance guarantees <sup>1</sup>	\$ (57,597)	\$ (133,602)

1. The bank performance guarantees are secured by a mortgage over the land and buildings and floating charges over cash, receivables, work in progress and plant and equipment.

### Note 26 Events after the balance date

#### i Dividend proposed

A fully franked final dividend of 2 cents per share (FY2016 final: 2 cents) has been proposed.

## The Group, management and related parties

### Note 27 Parent interests in subsidiaries

The consolidated financial statements include the financial statements of Austal Limited and the subsidiaries listed in the following table.

Company	Country of Incorporation	Equity Interest	
		2017	2016
Austal Ships Pty Ltd	Australia	100%	100%
Austal Cyprus Ltd	Cyprus	100%	100%
Austal Egypt LLC	Egypt	100%	100%
Austal Muscat LLC	Oman	100%	100%
Austal Service Pty Ltd	Australia	100%	100%
Austal Service Darwin Pty Ltd	Australia	100%	100%
Hydraulink (NT) Pty Ltd	Australia	100%	100%
KM Engineering (NT) Pty Ltd	Australia	100%	100%
Austal Systems Pty Ltd	Australia	100%	100%
Austal UK Ltd	United Kingdom	100%	100%
Austal Holdings Inc	USA	100%	100%
Austal USA LLC	USA	100%	100%
Austal USA Service LLC	USA	100%	100%
Austal Philippines Pty Ltd	Australia	100%	100%
Austal Middle East Pty Ltd	Australia	100%	100%
Austal Holdings China Pty Ltd <sup>1</sup>	Australia	100%	-
Oceanfast Luxury Yachts Pty Ltd	Australia	100%	100%
Oceanfast Pty Ltd	Australia	100%	100%
Seastate Pty Ltd	Australia	100%	100%

1. Austal China Holdings Pty Ltd incorporated in FY2017

#### i Investment in joint venture

	2017 '000	2016 '000
<b>Investment In Joint Venture</b>		
Investment in Aulong Shipbuilding Co Ltd Joint Venture <sup>1</sup>	\$ 1,847	\$ -
Total	\$ 1,847	\$ -
	2017 '000	2016 '000
<b>Share of profit of joint venture</b>		
Share of profit / (loss) of joint venture	\$ (109)	\$ -
Total	\$ (109)	\$ -

The investment in Aulong joint venture represents the Group's 40% interest in the Chinese joint venture, Aulong Shipbuilding Co Ltd. The remaining 60% of the joint venture is held by Chinese company Jianglong Shipbuilding Co Ltd.



## Note 28 Related party disclosure

Group policy is that all transactions with related parties are conducted on commercial terms and conditions.

No related party transactions occurred with the consolidated entity other than the remuneration of Directors and Key Management Personnel and the matters disclosed in this report.

## Note 29 Key management personnel compensation

	<u>2017</u> <u>'000</u>	<u>2016</u> <u>'000</u>
Short-term employee benefits	\$ 3,560	\$ 3,303
Post-employment benefits	173	191
Termination benefits	95	839
Long term benefits	101	143
Share-based payment	755	307
Total	<u>\$ 4,684</u>	<u>\$ 4,783</u>

Detailed remuneration disclosures are provided in the Remuneration Report commencing on page 18.



LCS 8 delivered June 2016

## Note 30 Share based payments

### i Long Term Incentive (LTI) Plan

The long term incentive policy of the Company is that an annual component of remuneration of executives should be at risk and based on equity in the Company to ensure that executives hold a stake in the Company and to align their interests with those of shareholders.

The board will implement a change to the LTI plan for FY2018 to ensure that the scheme continues to drive long term executive performance as well as meet normal industry practice. The Total Shareholder Return (TSR) measure will be changed from indexed TSR (iTSR) to relative TSR (rTSR) for the FY2018 grant and all other future awards following market feedback and advice from the remuneration consultant.

iTSR determines the shareholders returns of Austal relative to a market index rather than capturing the absolute performance of the Group. Setting an appropriate iTSR performance level (e.g. 200% stretch in FY2016 & FY2017 grants) is inherently difficult because of the focus on a single market average rather than the breadth of market results.

The Board assessed a peer group of companies that include TSR within their LTI schemes and greater than 90% of companies in the peer group utilise Relative TSR (rTSR) which sets performance hurdles in reference to percentiles of TSR for stocks included in the All Ordinaries Index.

The Board resolved to adopt rTSR for all LTI grants from FY2018 because rTSR is considered to represent a more transparent and understandable basis for measuring performance which is therefore easier to articulate and explain to beneficiaries and shareholders. Achieving company TSR that is below the 50th percentile of the market is considered substandard whilst delivering a TSR that is in the top quartile is clearly strong performance that should be rewarded.

#### 1. Purpose

The purpose of the LTI Plan is to incentivise senior executives to deliver Group performance that will lead to sustainable superior returns for shareholders and to modulate the cost of employing Senior Executives.

#### 2. Form of incentive

The LTI should be based on Performance Rights that vest based on an assessment of performance against objectives

#### 3. Measurement period

The Company instituted a transitional arrangement for the LTI scheme for FY2014 and FY2015 which was explained in the FY2014 Annual Report.

The standard measurement period from FY2016 onwards is three years, however the Board has the discretion to modify the duration of the measurement period if it deems an extension to be appropriate.

#### 4. Measures of long term performance

The Company uses two long term performance measures:

- Total Shareholder Return (TSR)
- Return on Invested Capital (ROIC)

## 5. Performance hurdles

The granting of performance rights is tied exclusively to overall Group performance, measured against ROIC and TSR targets set periodically by the Board. The targets will be based on Group performance, rather than business unit performance in order to maximise alignment with shareholder interests; Performance rights will not vest unless these hurdles, are met. Performance hurdles will be measured over a prescribed period determined by the Board.

The performance hurdles for rights granted in FY2017 are as follows:

## 6. Return on Invested Capital (ROIC) measure

Senior Executives are faced with significant and long term business development and project based challenges, therefore the LTI should also be linked to the achievement of ROIC growth objectives that will lead to value creation for shareholders. This measure is considered the best measure of long term performance from an internal perspective by the Board and by major stakeholders.

ROIC is calculated by dividing the Net operating profit after tax exclusive / Net Assets (excluding cash, debt, derivatives and tax accounts).

Actual ROIC results are compared against internal targets.

The number of performance rights expected to vest is adjusted based on current and future Group ROIC estimates.

ROIC: 60% of the FY2017 LTI Plan is determined by ROIC .

Performance Level	ROIC	Vesting %
Below Threshold	< 6.6%	0%
Threshold	6.6%	25%
Between Threshold and Target	> 6.6% ROIC > 7.4%	Pro-rata
Target	7.4%	50%
Between Target and Stretch	> 7.4 % ROIC < 8.3%	Pro-rata
Stretch	>= 8.3%	100%

## 7. Total Shareholder Return (TSR) measure

Indexed Total Shareholder Return (iTSR): 40% of the FY2017 LTI plan performance rights issued will be assessed against Austal's iTSR. This is calculated by comparing the actual shareholder return of Austal Limited, measured over the three year measurement period, to the All Ordinaries Total Return Index (XAOA) for the same period to determine the number of performance rights that vest. The fair value is determined by an external valuer using a Monte Carlo model.

Performance Level	TSR v iTSR	Vesting %
Below Threshold	<= 100%	0%
Threshold	100%	25%
Between Threshold and Target	100% < iTSR < 150%	Pro-rata
Target	150%	50%
Between Target and Stretch	More than 150% but less than 200%	Pro-rata
Stretch	>= 200%	100%

## 8. Vesting of Performance Rights

The Performance Rights for each employee vest at the end of the performance period, subject to meeting the performance hurdles and continued service with the Group at the time of vesting.

Performance rights that do not vest will lapse.

## 9. Holding period

A one year holding period applies to shares that are awarded as a result of Performance Rights vesting.

## 10. Rights issued and valuation

3,103,111 (FY2016: 1,566,127) performance rights were issued during the year.

Grant	Balance at 30 June 2016	Issued	Exercised	Forfeited / Lapsed	Balance at 30 June 2017	Tranche 1 Expiry date	Tranche 2 Expiry date
FY2014	296,429		-	(46,760)	249,669	30 Jun 2015	30 Jun 2017
FY2015	547,845		-	(73,130)	474,715	30 Jun 2017	30 Jun 2017
FY2016	821,133		-	(61,921)	759,212	30 Jun 2018	-
FY2017	-	3,103,111	-	(42,979)	3,060,132	30 Jun 2019	-
Total	1,665,407	3,103,111	-	(224,790)	4,543,728		

The board has the discretion to decide if performance rights will lapse or vest.

The Group uses the Monte Carlo model to value the performance rights. The following table lists the inputs to the valuation model used:



Cape Class Patrol Boat 9 (Cape Inscription) launch in Henderson, Western Australia

FY2017	Assumptions	
	Tranche A	Tranche B
<b>Monte Carlo simulation method assumptions:</b>		
Discount Rate	1.4% p.a.	1.7% p.a.
Share Price Volatility	45% p.a.	45% p.a.
Grant Date	1 September 2016	28 October 2016
Expected life of option (years)	3	3
<b>The fair values of the rights at grant date were as follows:</b>		
Fair value per performance right - TSR	\$0.97	\$1.11
Fair value per performance right - ROIC	\$1.37	\$1.45
Share price at grant date	\$1.45	\$1.53

FY2016	Assumptions		
	Tranche A	Tranche B	Tranche C
<b>Monte Carlo simulation method assumptions:</b>			
Discount Rate	1.8% p.a.	1.8% p.a.	1.9% p.a.
Share Price Volatility	40% p.a.	40% p.a.	40% p.a.
Grant Date	30 October 2015	13 October 2015	23 September 2015
Expected life of option (years)	3	3	3
<b>The fair values of the rights at grant date were as follows:</b>			
Fair value per performance right - TSR	\$1.71	\$1.52	\$1.63
Fair value per performance right - ROIC	\$2.16	\$2.00	\$2.06
Share price at grant date	\$2.28	\$2.11	\$2.18

FY2015	Tranche A		Tranche B	
	Measurement Period 1	Measurement Period 2	Measurement Period 1	Measurement Period 2
<b>Monte Carlo simulation method assumptions:</b>				
Discount Rate	1.8% p.a.	1.8% p.a.	1.8% p.a.	1.8% p.a.
Share Price Volatility	40% p.a.	40% p.a.	40% p.a.	40% p.a.
Grant Date	30 October 2014	30 October 2014	21 October 2014	21 October 2014
Expected life of option (years)	2	3	2	3
<b>The fair values of the rights at grant date were as follows:</b>				
Fair value per performance right - TSR	\$0.86	\$0.90	\$0.77	\$0.81
Fair value per performance right - ROIC	\$1.30	\$1.30	\$1.24	\$1.24
Share price at grant date	\$1.30	\$1.30	\$1.23	\$1.23

## 11. Extension of FY2014 & FY2015 LTI measurement periods

The Board decided to extend the measurement period of performance rights due to vest at 30 June 2016 by one year. The decision was taken due to the trading halt that was initiated on 30 June 2016 pending the release of the FY2016 earnings guidance, and the subsequent reduction in share price on 4 July 2016 which was outside of the original measurement period. The vesting criteria for the performance rights have been adjusted pro-rata for the one year extension in the measurement period. No further extensions to the validity of these rights will be considered.

The Group used a Monte Carlo model to value the extension of the performance rights:

		<b>Measurement Period 2</b>		
<b>Monte Carlo simulation method assumptions:</b>				
Discount Rate		1.4% p.a.		
Share Price Volatility		45% p.a.		
Grant Date		1 September 2016		
Expected life of option (years)		1		
<b>Summarised results based on performance conditions:</b>				
	<b>TSR</b>	<b>ROIC</b>	<b>Total</b>	
Number of performance rights issued to all participants	74,901	174,768	249,669	
Fair value per performance right - with vesting conditions	\$ 1.26			
Fair value per performance right - without vesting conditions		\$ 1.43		
Share price at grant date	\$ 1.45	\$ 1.45	\$ 1.45	
Total value of performance rights	\$ 94,375	\$ 249,918	\$ 344,294	
Number of performance rights expected to vest <sup>1</sup>	74,901	-	74,901	
Total value of performance rights expected to vest	\$ 94,375	\$ -	\$ 94,375	

1. There was no prospect of ROIC rights vesting because of the magnitude of the Group EBIT loss in FY2016.

		<b>Measurement Period 1</b>		
<b>Monte Carlo simulation method assumptions:</b>				
Discount Rate		1.4% p.a.		
Share Price Volatility		45% p.a.		
Grant Date		1 September 2016		
Expected life of option (years)		1		
<b>Summarised results based on performance conditions:</b>				
	<b>TSR</b>	<b>ROIC</b>	<b>Total</b>	
Number of performance rights issued to all participants	35,603	83,074	118,677	
Fair value per performance right - with vesting conditions	\$ 1.10			
Fair value per performance right - without vesting conditions		\$ 1.43		
Share price at grant date	\$ 1.45	\$ 1.45	\$ 1.45	
Total value of performance rights	\$ 39,163	\$ 118,796	\$ 157,959	
Number of performance rights expected to vest <sup>1</sup>	35,603	-	35,603	
Total value of performance rights expected to vest	\$ 39,163	\$ -	\$ 39,163	

1. There was no prospect of ROIC rights vesting because of the magnitude of the Group EBIT loss in FY2016.

## ii Acquisition of KM Engineering (NT) Pty Ltd & Hydraulink (NT) Pty Ltd Option Plan (KME)

Austal Limited issued three tranches of options to the sellers of KME Engineering (NT) Pty Ltd & Hydraulink when they were acquired by Austal Service Darwin Pty Ltd in FY2013. The third tranche did not vest. The remaining two tranches were as follows:

- 687,098 of zero priced options as part of the equity consideration. The number of options was adjusted based on EBIT targets for the 3 years post acquisition. The options expire on 5 October 2018.
- 687,098 options to acquire shares as an executive incentive to the owners who remained employed on as managers. The number of options was adjusted based on EBIT targets for the 3 years post acquisition. The options expire on 4 March 2019.
- The total number of options vested and exercisable is 1,374,196.

## iii Austal Group Management Share Plans (AGMSP)

The trustee holds a total of 4,015,539 shares at balance date on behalf of the AGMSP plans represented by:

- 597,846 shares allocated under Plans 1 and 2 with a weighted average price of \$1.27 each, with no contractual life; and
- 3,417,693 shares that are unallocated.

### 1. Plan 1

The Group established the first Austal Group Management Share Plan (Plan 1) in 1998 so that Directors and key managers could participate in owning shares in the Company. The features of the Plan are:

- Austal offered loans to participants for up to 100% of the purchase consideration for their shares on a limited recourse basis.
- The shares were made available to the participants at market value.
- The Board determined the number of shares that were made available to each participant.
- The shares are required to be held by a trustee on behalf of the participant.
- All shares have vested and may be transferred to participants provided that any loan in respect of these shares has been repaid.
- Dividends on shares held under the Plan must be applied to pay interest on the loans with any surplus in excess of the interest expense distributed to participants. Participants with an interest in shares under the Plan have full voting rights.
- Interest on the loans is charged at a fixed rate of 6%, or such other rate as determined by the Board.
- The shares must be sold and the loan (if any) repaid upon termination of employment or contract arrangements.

## 2. Plan 2

Plan 2 was established by the Group in 2000. Plan 2 is similar to Plan 1 with one main point of distinction being:

- The interest on loans offered under Plan 1 is calculated as 6% per annum, whilst the interest on loans offered under Plan 2 is calculated as 60% of any dividends paid on any shares acquired by the person to whom the loan was made.

## 3. Summary of movement

Details of the movement in the number of options issued under the Austal Group Management Share Plan are shown below:

	2017 '000	2016 '000
<b>Summary of options granted under AGMSP</b>		
<b>1 July</b>	684	684
Exercised	-	-
Lapsed	(86)	-
<b>30 June</b>	<u>598</u>	<u>684</u>

All remaining options were fully vested and exercisable throughout the year

## iv CEO fixed remuneration share rights issue

The structure of Base Remuneration for the CEO, David Singleton, for the period ended 30 June 2017 is as follows:

- Fixed cash remuneration is 70% of Total Fixed Remuneration (TFR)
- Fixed share based remuneration equal to 30% of TFR. The number of shares are based on the volume weighted average closing price of ASB shares in the last 5 trading days of each month.

30% of the CEO's fixed remuneration is provided in shares which are subject to a 12 month holding period from the date at which the shares are released to the CEO and no performance condition exists because it is considered part of his base remuneration. 191,740 share rights were earned for FY2017. The number of share rights are based upon the volume weighted average closing price of Austal Limited (ASX Ticker: ASB) shares in the last 5 trading days of each month. The fair value per share right is based on the closing share price of \$1.53 / share on the date of the 2016 Annual General Meeting when the arrangement was approved for a period up to 31 December 2019.

## v Recognition - equity settled transactions

The Group provides benefits to employees (including executive Directors and key management personnel) of the Group in the form of share-based payments, whereby employees render services in exchange for shares or rights over shares (equity settled transactions).

Equity settled benefits have been provided to senior management and Directors under the following plans in the current and prior years:

- The Austal Group Management Share Plan (AGMSP)
- The Long Term Incentive Plan (LTI Plan)
- CEO shares



No account is taken of any performance conditions, other than conditions linked to the price of the shares of Austal Limited (market conditions) if applicable in valuing equity settled transactions.

The cost of these equity settled transactions with employees is recorded by reference to the fair value at the date at which they are granted. The cost of equity settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the vesting period).

The cumulative expense recognised for equity settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the number of awards that, in the opinion of the Directors of the Group, will ultimately vest. This opinion is formed based on the best available information at balance date. No adjustment is made for the likelihood of market performance conditions being met because the effect of these conditions is included in the determination of fair value at grant date. The statement of comprehensive income charge or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition.

An expense is recognised as if the terms had not been modified. An expense also is recognised for any modification that increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee, as measured at the date of modification.

An equity settled award that is cancelled is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately, however, cancelled awards and new awards are treated as if they were a modification of the original award if a new award is substituted for the cancelled award and designated as a replacement award on the date that it is granted, as described in the previous paragraph.

Shares in the Group held by the AGMSP are classified and disclosed as reserved shares and deducted from equity.

## vi Recognised share-based payment expenses

The expense recognised for share based payments during the year is shown in the table below:

	<b>2017</b>	<b>2016</b>
	<b>'000</b>	<b>'000</b>
<b>Share Based Payments Expense</b>		
Expense arising from equity-settled share-based payment transactions	\$ (1,067)	\$ (796)

## Note 31 Parent entity

Information relating to Austal Limited, the Parent entity, is detailed below:

	<b>2017</b>	<b>2016</b>
	<b>'000</b>	<b>'000</b>
<b>Balance sheet</b>		
<b>Assets</b>		
Current	\$ 42,860	\$ 80,583
Non - Current	292,440	289,944
Total	<u>\$ 335,300</u>	<u>\$ 370,527</u>
<b>Liabilities</b>		
Current	\$ (3,918)	\$ (7,786)
Non - Current	(3,537)	(3,996)
Total	<u>\$ (7,455)</u>	<u>\$ (11,782)</u>
<b>Net Assets</b>	<u>\$ 327,845</u>	<u>\$ 358,745</u>
<b>Equity</b>		
Contributed equity	\$ 116,384	\$ 114,738
Employee benefits reserve	2,561	5,688
Asset revaluation reserve	10,656	10,656
Cash flow hedge reserve	(153)	(1,577)
Retained earnings	198,397	229,241
Total	<u>\$ 327,845</u>	<u>\$ 358,746</u>
<b>Income</b>		
Net Profit / (Loss) after tax	\$ (22,246)	\$ 14,031
Total Comprehensive Income	(20,822)	35,048

Austal Limited provides parent company guarantees in respect of contract performance by various members of the Austal Group including Austal USA LLC, Austal Ships Pty Ltd and Austal Philippines Pty Ltd.

## Directors' declaration

I state in accordance with a resolution of the Directors of Austal Limited, that:

In the opinion of the Directors:

- The financial statements and notes of the consolidated entity are in accordance with the Corporations Act 2001, including:
- Giving a true and fair view of the consolidated entity's financial position at 30 June 2017 and of its performance for the year ended on that date; and
- Complying with Accounting Standards (including the Australian Accounting Interpretations) and Corporations Regulations 2001.
- The financial Statements and notes also comply with International Financial Reporting Standards as disclosed in Note 2.

In the opinion of the Directors, there are reasonable grounds to believe that the consolidated entity will be able to pay its debts as and when they become due and payable at the date of this declaration.

This declaration has been made after receiving the declarations required to be made to the Directors in accordance with sections 295A of the Corporations Act 2001 for the financial period ending 30 June 2017.



John Rothwell AO  
Chairman  
on behalf of the Board  
25 August 2017



Austal USA has established a new office in Singapore to provide in-theatre support to the US Navy's Littoral Combat Ship (LCS) and Expeditionary Fast Transport (EPF) fleets. A full-time on-site technical representative, augmented by fly-away teams from the US is supporting the USS Coronado in Guam and three EPFs operating in the vicinity of Singapore.

## Independent audit report to the members of Austal Limited



Ernst & Young  
11 Mounts Bay Road  
Perth WA 6000 Australia  
GPO Box M939 Perth WA 6843

Tel: +61 8 9429 2222  
Fax: +61 8 9429 2436  
ey.com/au

### Report on the audit of the financial report

#### Opinion

We have audited the financial report of Austal Limited (the Company) and its subsidiaries (collectively the Group), which comprises the consolidated statement of financial position as at 30 June 2017, 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 to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

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

- a) giving a true and fair view of the consolidated financial position of the Group as at 30 June 2017 and of its consolidated financial performance for the year ended on that date; and
- b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

#### Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

## 1. Recognition of revenues and profits on long-term contracts

### Why significant

The Group's business involves entering into contractual relationships with customers to provide construction services and other maintenance services. A significant proportion of the Group's revenues and profits is derived from long-term contracts.

Revenue recognition on these long-term contracts involves judgment, with estimates being made to:

- Assess the estimated total contract costs over the life of the contract;
- Assess the stage of completion of the contract; and
- Forecast the contract revenues after taking into consideration scope and price variations to the original contract.

The Group's disclosures are detailed in Note 4 - *Revenue*, Note 15 - *Vessel Construction and Support contracts in progress* and Note 16 - *Inventories and work in progress* to the financial report.

### How our audit addressed the key audit matter

We examined all key contracts and made enquiries of the Group to obtain a full understanding of the specific terms and risks, which in turn allowed us to assess whether revenue was appropriately recognised.

We evaluated and tested the design and operating effectiveness of relevant controls that underpin the underlying contract related cost balances including the purchase to pay, and payroll cycles.

We tested the accuracy and timing of revenue recognised in the financial report. In obtaining sufficient audit evidence, we:

- Tested the revenue and billing cycles for material contracts including vouching material cash receipts and comparing forecast revenue to contracts and approved variations;
- Tested the accuracy of the computation of the revenue recognition based on percentage completion for material contracts on a sample basis; and
- Recalculated the profit margin on material contracts and made inquiries of key executives regarding any changes in margin from the prior period.

For the material contracts we performed the following additional procedures:

- Obtained an understanding of the performance and status of the contracts through inquiry of key executives having oversight over the various contract portfolios;
- Tested the contract status through the examination of externally generated evidence, such as customer correspondence;
- Performed physical observations of the stage of completion of key vessel contracts;
- Involved our government contract services specialists to evaluate the Group's cost estimates for key contracts; and
- Assessed the Group's accounting policies and the adequacy of its related disclosures as detailed in the financial report.

## 2. Carrying value of non-current assets and intangible assets including goodwill

### Why significant

The Group has significant property, plant and equipment and intangible assets including goodwill totalling \$509.2 million as at 30 June 2017.

An assessment is required to be made annually by the Group to determine whether there are indicators that the carrying value of these assets is impaired.

If indicators are identified, and for goodwill intangibles, the assessment of impairment involves judgment, with estimates being made in relation to cash flow projections, growth rates and discount rates.

The Group identified impairment indicators relating to two Cash Generating Units ('CGUs') being Australia and the Philippines.

The Group's disclosures relating to the recognition and measurement of non-current assets and intangibles and impairment are included in Note 18 - *Property, plant and equipment* and Note 19 - *Intangible assets and goodwill* to the financial report.

### How our audit addressed the key audit matter

We examined the impairment assessment prepared by the Group. We made enquiries of the Group regarding market, technological and economic factors as well as any planned business changes to understand the basis for the assessment of impairment indicators.

We examined the Group's model for assessing impairment in the two CGUs and, together with our valuation specialists, we assessed and tested:

- The appropriateness of the methodology adopted in the model;
- The assumptions underpinning the cash flow projections of the CGUs as well as considered the historical reliability the Group's cash flow forecasting process;
- The assumptions underpinning the terminal value growth rate by performing a historical budget analysis and a sensitivity analysis; and
- The appropriateness of the discount rate applied.

We assessed the adequacy of the Group's disclosures relating to the recognition and measurement of non-current assets and intangibles and impairment.

### 3. Warranty obligation

#### Why significant

The Group recognises a warranty obligation upon the delivery of vessels to customers based on the estimated future cost of warranty repairs on vessels. The warranty obligation is estimated using the value of historical claims and known potential claims relating to vessel contracts excluding those contracts in the USA.

Warranty obligation relating to USA contracts is recognised in Inventory as part of estimated total contract costs over the life of the construction, rather than as a provision in the financial report.

The determination of the warranty obligation involves judgment, with estimates being made to determine the value of future potential claims.

The Group's disclosures relating to warranty provisions are included in Note 21 – *Provisions* to the financial report.

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

We tested the Group's assessment of the value of historic claims and known potential claims relating to warranty repairs by vouching warranty repair costs incurred subsequent to the year end, where applicable.

We made inquiries of key executives having oversight over the various contract portfolios, regarding the adequacy of the warranty obligation based on the likely outcome of claims, and the estimated cost of repairs including labour hours and materials.

We assessed the adequacy of the Group's disclosures relating to warranty provisions.

### 4. Taxation

#### Why significant

The Group's geographic operations results in significant income tax expense, across two main jurisdictions, being USA and Australia.

In addition, significant deferred tax assets and liabilities are recognised by the Group.

During the year an audit was completed by the Australian Taxation Office ('ATO'). Amended tax assessments have been issued by the ATO in respect of the matters and the tax years that the audit focused on. The Group has provided for any additional tax or penalties arising from the ATO audit.

The Group's disclosures relating to taxation are included in Note 9 – *Income and other taxes* to the financial report.

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

Together with our tax specialists we assessed the Group's tax-related balances and the underlying assumptions and calculations on which these were derived.

We examined correspondence from the Group's tax advisers in both Australia and the USA and correspondence between the Group and the ATO.

We also assessed the independence and competence of the Group's tax advisers.

We involved our tax specialists to assist in evaluating the potential exposure to additional tax or penalties that may become payable as a result of the tax audit, and the Group's provision for additional tax or penalties. We assessed the adequacy of the Group's disclosures relating to taxation.

### Information other than the financial report and auditor's report thereon

The directors are responsible for the other information. The other information comprises the information included in the Company's 2017 Annual Report, but does not include the financial report and our auditor's report thereon.

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

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## Responsibilities of the directors for the financial report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

## Auditor's responsibilities for the audit of the financial report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.



We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and 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 audit of the remuneration report

### Opinion on the remuneration report

We have audited the Remuneration Report included in pages 20 to 43 of the directors' report for the year ended 30 June 2017.

In our opinion, the Remuneration Report of Austal Limited for the year ended 30 June 2017, complies with section 300A of the *Corporations Act 2001*.

### Responsibilities

The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Ernst & Young

Robert A Kirkby

Partner

Perth

25 August 2017



## Shareholder information

The following information was extracted from the Company's register at 28 July 2017.

### Distribution of shares

<b>Individual shareholding</b>	<b>Number of shares</b>	<b>% of Total issued capital</b>	<b>Number of holders</b>
1 - 1000	755,882	0.22%	1,695
1,001 - 5,000	5,382,949	1.54%	1,999
5,001 - 10,000	6,123,448	1.75%	805
10,001 - 100,000	20,704,908	5.93%	809
100,001 and over	316,505,456	90.57%	68
<b>Total</b>	<b>349,472,643</b>	<b>100.00%</b>	<b>5,376</b>

### Twenty largest shareholders

<b>Rank</b>	<b>Shareholder</b>	<b>Number of shares</b>	<b>% of Total issued capital</b>	<b>Substantial shareholder</b>
1	HSBC Custody Nominees (Australia) Limited	107,629,283	30.80%	Yes
2	J P Morgan Nominees Australia Limited	59,208,602	16.94%	Yes
3	Citicorp Nominees Pty Ltd	40,860,758	11.69%	Yes
4	Austro Pty Ltd	32,807,692	9.39%	Yes
5	National Nominees Limited	23,427,053	6.70%	Yes
6	BNP Paribas Noms Pty Ltd	8,812,137	2.52%	
7	Zero Nominees Pty Ltd	6,984,807	2.00%	
8	Onyx (WA) Pty Ltd	6,800,000	1.95%	
9	Austal Group Management Share Plan Pty Ltd	4,015,539	1.15%	
10	Mr William Robert Chambers	3,260,791	0.93%	
11	Mr Garry Heys & Mrs Dorothy Heys	2,844,670	0.81%	
12	Sandhurst Trustees Ltd	2,648,607	0.76%	
13	Lavinia Shipping Limited	1,970,000	0.56%	
14	Mossisberg Pty Ltd	1,912,000	0.55%	
15	Lujeta Pty Ltd	1,300,000	0.37%	
16	AMP Life Limited	1,124,036	0.32%	
17	ACE Property Holdings Pty Ltd	1,000,000	0.29%	
18	Aust Executor Trustees Ltd	998,476	0.29%	
19	Kenny Nominees (NT) Pty Ltd	815,783	0.23%	
20	Warbont Nominees Pty Ltd	578,688	0.17%	
	<b>Total</b>	<b>308,998,922</b>	<b>88.42%</b>	

### Voting rights

All ordinary shares issued by Austal Limited carry one vote per share without restriction.

## Corporate governance statement

The Company has elected to post its Corporate Governance Statement on its website in accordance with ASX Listing Rule 4.10.3. The Corporate Governance Statement can be found at the following URL: [www.austal.com/corporategovernance](http://www.austal.com/corporategovernance).

### Enterprise Risk

Austal manages a number of material risks to its business on an ongoing basis. The impact of these risks could reasonably be expected to have a material impact on the value of the business if they were to occur and to the ongoing viability of the Company in exceptional circumstances. Investors are advised to take these risks into account when investing in Austal and be mindful that such risks can materialise at short notice.

### LCS program in the USA

LCS is Austal's biggest single contract and could be cancelled or curtailed by the US Government at any time. Austal currently has firm orders for ships up to LCS 28 (vessels up to and including LCS 10 have been delivered thus far) and expects further orders in US fiscal year 2017 and 2018 but these orders are not guaranteed to materialise. The US Government has also announced an early curtailment of the LCS version of the small surface combatant programme to be replaced by a FFG(X) program in 2020 which may or may not be based upon the LCS platform.

The US Navy completed physical "shock trials" of LCS 6 in July 2016 to measure and assess the impact of an explosive charge detonated at a specified proximity to the vessel whilst underway at sea. The specific results of these trials remain classified by the US Navy, and are unlikely to ever be released to either Austal or the public in light of the extreme sensitivity of the vessel's capability to withstanding the impact of shock.

Austal has not been advised of any material issues regarding vessel performance by the US Navy, however the analysis conducted by the US Navy has not been finalised which means that the risk of incurring additional cost to address issues that may be identified by the analysis cannot be discounted entirely.

The residual risk regarding the performance of LCS and the shock trial analysis will reduce over time as the vessel continues to demonstrate its capabilities.

### EPF program in the USA

The currently stated acquisition program for the EPF vessel is for 10 ships although 12 vessels have been ordered to date. The US fiscal year 2017 budget contains no plans for further vessel orders. Austal is of the view that further vessels may be ordered in future but this presents a significant risk and may not occur.

### Offshore Patrol Vessel (OPV) in Australia

The OPV contract represents the single most important program for the Henderson shipyard operations in Australia due to the size and duration of the potential contract. Austal is in a joint venture with Fassmer of Germany for this contract in competition with 2 other consortia. Failure to win the contract will seriously impede the future viability of the Australian operations and could lead to partial or full closure of the Henderson shipyard operations when current contracts come to an end.

### Commercial Ferries

The commercial high speed aluminium ferry business is a key market for Austal and provides significant workload to both the Philippines and Australia business units. Whilst there is strong current evidence of significant growth in this market, this cannot be guaranteed. The ferry industry can be adversely affected by economic, political, social, security and other factors which delay or eliminate future orders for vessels or even cancellations of current vessels as was experienced following the financial crisis of 2008. Closure of this market could force a closure of shipyards or severe curtailment of operations.

## Product Liability

Austal's products are typically large and complex. A high degree of expertise is required in their construction but also in their operation and sustainment. The customers to which Austal sells its vessels and the environments in which our vessels are used – whether defence, paramilitary or commercial – are equally demanding. The risk of product failure or fault applies to every manufacturing business, however the unique complexities of large vessel design and construction, and the particularly taxing conditions in which Austal's vessels operate generally mean that the potential consequences of any issues with either construction or operation are significant. Austal has a comprehensive insurance portfolio in place to mitigate this risk but coverage is subject to typical limitations, so material claims arising from either construction issues, or by third parties following operational issues, could require Austal to either undertake significant remedial or restorative work at its own expense, or potentially pay compensation to third parties if insurance coverage is restricted, delayed or not available.

## Banking Arrangements

Austal has financial facilities provided by a syndicate of four banks with financial covenants that must be adhered to at all times. A material adverse change in the financial performance of the Austal Group could result in a breach of these covenants which would place Austal in default of its banking arrangements. A financial breach could result in Austal needing to raise capital from debt or equity markets on unfavourable terms or result in the Directors of Austal or the banking syndicate placing Austal in administration, receivership or liquidation.

## Health, safety and environment

Austal is exposed to typical health and safety risks associated with the operation of major manufacturing facilities like shipbuilding yards. Potential safety events include those arising from working from heights and in confined spaces, operation of lifting machinery, fabrication tools and the use of hazardous substances. There is also risk of impacting the surrounding environment given the nature of Austal's operations and their close proximity to waterways.

Austal has a number of measures in place to mitigate these risks. Austal has Safety, Health and Environment (SHE) Management Plans that underpin all of Austal's operations and clearly outline its health, safety and environment strategies. The SHE Plans are monitored by SHE teams at each shipbuilding facility. Austal's ongoing focus is achieving 'Zero Harm and Zero Waste' and ensuring it meets applicable health and safety and environmental legislative standards.

Austal has a certified management system to OHSAS 18001 and AS/NZS 4801. Austal also has a formal Risk Management Framework, designed in accordance with ISO31000: Risk Management – Principles and Guidelines, which is aligned to Australian Defence standard ABR6492 and the Royal Australian Navy Technical Regulations Manual. Austal considers itself an industry leader in overall safety performance however it is acknowledged that a degree of risk will always be present as an industrial manufacturer.

## Cyber security

Austal's production of vessels for the USA and Australian governments and other governments of other countries means that it handles sensitive information. Austal has established information handling policies and standards and cyber security measures that seek to prevent the disclosure and theft of such information, however, we have seen the ability of parties to hack into even the most well protected systems around the world and sometimes create high levels of interference or public disclosure, which may include but are not limited to demands of large financial payments or interruption of service. Such a breach could inflict severe damage on the Company given Austal's position in defence contracting in the USA, Australia and around the world and, affect its ability to continue operations in an extreme outcome.

## Tax treatment in Australia, USA and other jurisdictions

Austal believes that it has materially met its tax obligations in the jurisdictions that it operates which includes cross border tax arrangements currently under scrutiny by authorities around the world including the ATO (Australia) and the IRS (USA). Austal is currently reviewing its tax arrangements which could alter its tax treatment both in Australia and overseas and is therefore seeking tax rulings and agreements between international revenue authorities to reduce the risk of non-compliance.

## Corporate directory



Pacific Patrol Boat Replacement (PPB-R) under construction at Austal Australia



PPB-R new facility ribbon cutting by The Honourable Christopher Pyne, Australian Minister for Defence Industry



Swire Pacific built in Austal Philippines

### Directors

#### Executive Directors

Mr David Singleton

#### Non-Executive Directors

Mr John Rothwell

Mr Giles Everist

Mr Jim McDowell

### Auditors

Ernst & Young

The Ernst & Young Building

11 Mounts Bay Road

Perth 6000

Western Australia

### Company Secretary

Mr Adrian Strang

### Registered office

100 Clarence Beach Road

Henderson 6166

Western Australia

Telephone: +61 8 9410 1111

### Share registry

Advanced Share Registry Services

110 Stirling Highway

Nedlands 6009

Western Australia

Telephone: +61 8 9389 8033