

# Key performance indicator (KPI) system

## Principles of the KPI system

In order to fulfill a list of instructions issued by Russian President Vladimir Putin,<sup>2</sup> the Russian Ministry of Economic Development has drawn up requirements for the creation of a vertical strategic planning system at joint-stock companies included in lists approved by Directive No. 91-r of the Government of the Russian Federation dated January 23, 2003. This system involves the drafting of a long-term development program and a system of key performance indicators.

In accordance with the Regulation on Financial Incentives for the Executive Bodies of PJSC Inter RAO, one of the financial incentives for the Company's management is an annual bonus for reaching the Key Performance Indicators (KPIs) and Performance Benchmarks (PBs) set by the Company. This aspect of the incentive system aims to ensure that managers have a vested interest in their personal performance and in achieving the objectives set by the Strategy/ Long-Term Development Program. The list of the Company's annual KPIs and PBs is approved by the Board of Directors. In particular, the KPIs and PBs for the Chairman and members of the PJSC Inter RAO Management Board for 2018 were set by the PJSC Inter RAO Board of Directors.<sup>3</sup>

The main objectives of the KPI and PB system are to assess the achievement of the Company's strategic goals, monitor and control the implementation of the Strategy, and create the proper motivation for the Company's management taking into account the focus on achieving the target strategic indicators.

When the list of KPIs and PBs of PJSC Inter RAO is compiled, both the specific aspects of the Inter RAO Group's operations and the principles of minimum sufficiency are taken into account along with the transparency and measurability of indicators, their consistency, and the focus on increasing the Company's financial and operating results.

## Special aspects of the KPI system in 2018

The list of KPIs and PBs of PJSC Inter RAO for 2018 was compiled taking into account the requirements of the Regulation on Key Performance Indicators of PJSC Inter RAO, which was approved by a resolution of the PJSC Inter RAO Board of Directors dated December 25, 2014.<sup>4</sup> Per the Regulation, the list of KPIs and PBs contains financial, economic, and industry-specific indicators as well as bonus cancellation indicators (PB). The total number of financial and economic indicators is limited to seven, while their total sum should range from 50% to 70% of the total sum of all indicators.

<sup>2</sup> In accordance with clause 34 of List of Instructions No. Pr-3086 of the President of the Russian Federation dated December 27, 2013, the Government of the Russian Federation was put in charge of ensuring that joint-stock companies included in the lists approved by Directive No. 91-r of the Government of the Russian Federation dated January 23, 2003 adopt long-term programs for their development and also ensuring that audits of such programs are conducted.

<sup>3</sup> Minutes No. 214 dated December 21, 2017.

<sup>4</sup> Minutes No. 131 dated December 29, 2014.

**FINANCIAL AND ECONOMIC INDICATORS OF THE KPI AND PB SYSTEM OF PJSC INTER RAO IN 2018**

The total weight of the financial and economic indicators

**60%**

Return on equity (ROE) KPI The indicator determines the efficiency of equity usage, i.e. the Company's income per ruble of its own funds. It indicates the efficiency of the use of the portion of equity that belongs to shareholders, rather than all equity (or assets).			Weight: 20%
Lower level 95% (11.7)	Target level 100% (12.4)	Upper level 110% (13.6)	Mandatory indicator
Total shareholder return (TSR) KPI The indicator determines the market return for the Company and represents the shareholders' rate of return as a result of changes in stock exchange quotations and the distribution of dividends.			Weight: 10%
Lower level N/A	Target level ≥ Average	Upper level ≥ Average (+)	Mandatory indicator
Operating cash flow KPI The indicator describes the ability to maintain a certain level of solvency and ensure coverage of existing debt obligations with the required liquidity. This indicator is not part of the list of mandatory financial and economic indicators and, per the Regulation, falls within the category of an Indicator at the Discretion of the Board of Directors.			Weight: 15%
Lower level 95% (76,265,393)	Target level 100% (80,279,361)	Upper level 110% (88,307,297)	Optional indicator
EBITDA/person KPI This indicator determines the labor productivity of Company employees and describes the efficiency of manpower utilization. Positive trends in this indicator are achieved through implementing measures that aim to improve the attributes of personnel and the organizational structure of the Group's companies. Per the Regulation, this indicator falls within the category of an Indicator at the Discretion of the Board of Directors.			Weight: 15%
Lower level 95% (2.0)	Target level 100% (2.1)	Upper level 110% (2.3)	Optional indicator

The total weight of the financial and economic indicators is 60% of the sum of the weight of all the indicators of PJSC Inter RAO, which is consistent with the requirements of the Regulation.

Per the Regulation, the total number of industry-specific indicators should be no more than four, and the total weight of these indicators should range from 30% to 50% of the sum of the weight of all the Company's indicators. The list of industry-specific indicators is open.

For 2018, the aforementioned resolution of the Board of Directors set the following indicators for PJSC Inter RAO:

**INDUSTRY-SPECIFIC INDICATORS OF THE KPI AND PB SYSTEM OF PJSC INTER RAO IN 2018**

Investment program fulfillment KPI

This indicator is set to achieve the following strategic objectives:

- improving the operating efficiency of generating assets
- ensuring modernization and technological development
- increasing installed capacity through the implementation of investment projects within the set time limits and the approved estimated cost

Weight:  
20%

This KPI is used to assess the fulfillment of the investment program in terms of the funding and spending of capital investments and the commissioning of generating capacity.

Lower level  
80%

Target level  
100%

Upper level  
100%  
(+savings)

Mandatory indicator

Integrated innovation index fulfillment KPI

An integrated innovation index is established to assess innovative activities and, among other things, envisages a combination of four indicators: the number of the Inter RAO Group's intellectual property items for the reporting year; the percentage of R&D expenditures in the Inter RAO Group's revenue; the percentage of new advanced technologies in the total capacity of the Group's TPPs; the quality of the drafting (updating) of the innovative development program/ implementation of the innovative development program.

Weight:  
20%

Lower level  
90%

Target level  
100%

Upper level  
110%

Mandatory indicator

The total weight of the industry-specific indicators is 40% of the sum of the weight of all indicators of PJSC Inter RAO, which is consistent with the requirements of the Regulation.

The total weight of all key performance indicators of PJSC Inter RAO established for 2018 is 100%.

To enhance the efficiency of the Company's business management, bonus cancellation indicators (PB) are used per the Regulation. For 2018, the Company's Board of Directors established the following bonus cancellation indicators:

#### **BONUS CANCELATION INDICATORS (PB) OF PJSC INTER RAO IN 2018<sup>1</sup>**

PB for the implementation of the instructions of the PJSC Inter RAO Board of Directors This indicator describes the accuracy and timeliness with which the Company's management fulfills the instructions of the Board of Directors.	
Weight for the purpose of financial incentives for the Chairman of the Management Board	Up to 25%
PB for the implementation of the (routine and priority) instructions of the Chairman of the PJSC Inter RAO Management Board This indicator describes the accuracy and timeliness with which members of the Management Board fulfill the instructions of the Chairman of the Management Board.	
Weight for the purpose of financial incentives for members of the Management Board	Up to 100%
Debt/EBITDA PB This indicator is a generally recognized global indicator that describes the Company's level of debt burden and its ability to pay off existing liabilities.	
Weight for the purpose of financial incentives for the Chairman and members of the Management Board	25%
PB for reducing operating expenses by 2-3% annually This indicator aims to improve the Company's operating efficiency through the implementation of targeted cost optimization parameters based on the corresponding cost items.	
Weight for the purpose of financial incentives for the Chairman and members of the Management Board	20%
PB for the absence of fatal accidents or group accidents involving employees of the Inter RAO Group This indicator describes the Group management's performance with regard to ensuring occupational health and safety.	
Weight for the purpose of financial incentives for the Chairman and members of the Management Board	Up to 15%

The list of KPIs and PBs of PJSC Inter RAO for 2018 was applied in 2017 and was compiled based on the Group's strategic development priorities approved by the Inter RAO Board of Directors. There were no changes in the KPIs and PBs in 2018 compared with 2017.

According to the Regulation on Financial Incentives for the Chairman and Members of the PJSC Inter RAO Management Board approved by the Company's Board of Directors on November 1, 2013 (with amendments and additions), the size of the annual bonus is calculated based on the standard payroll, the planned amount of the annual bonus, and the actual KPI values. The Board of Directors approves the list of annual KPIs and PBs as well as their target values for the Chairman and members of the Company's Management Board as determined on the basis of the approved strategic development priorities and the business plan. At the end of the year, the Company's Board of Directors considers the fulfillment

of the KPIs and PBs for the relevant period based on the recommendations of the Nomination and Remuneration Committee. If the Company fulfills all the PBs and achieves the target 'Lower Level' value for the relevant KPIs, a decision is made on the appropriate remuneration for managers based on the Company's performance results.

#### **Results of the fulfillment of the KPIs and PBs for 2018**

The KPIs were achieved based on the results of 2018. The actual values of the KPIs were approved by a resolution of the Company's Board of Directors on April 18, 2019<sup>2</sup> based on the Company's annual accounting (financial) statements for the 12 months of 2018 and the Company's consolidated financial statements for the 12 months of 2018 in accordance with the methods for calculating and evaluating the achievement of annual KPIs and PBs for 2018, which were approved by resolutions of the PJSC Inter RAO Board of Directors on December 21, 2017,<sup>3</sup> and also based on the report on the implementation of the Inter RAO Group's business plan approved by a resolution of the PJSC Inter RAO Board of Directors on March 15, 2019.<sup>4</sup>

<sup>1</sup> No changes were made to the bonus cancellation indicators in 2016-2018.

<sup>2</sup> Minutes No. 245 dated April 22, 2019.

<sup>3</sup> Minutes No. 214 dated December 21, 2017.

<sup>4</sup> Minutes No. 242 dated March 18, 2019.

## COMPARISON OF KPI ACHIEVEMENT LEVEL

Name of annual KPI	Ratio of indicator/target achievement for 2016	Ratio of indicator/target achievement for 2017	Ratio of indicator/target achievement for 2018	Change vs. 2017, %
Return on equity (ROE)	1.2	1.2	1.2	0
EBITDA/person	1.2	1.1	1.2	9
Operating cash flow	1.2	1.09	1.2	10
Investment program implementation	0.95	1.2	1.2	0
Integrated innovation index implementation	1.12	1.19	1.14	-4
Total shareholder return (TSR)	-	1.0	1.2	20

# Principles for responsible business

## Development of energy assets

The Inter RAO Group's Strategy/Long-Term Development Program involves the systematic development of energy assets. In January 2019, the Government of the Russian Federation approved a program for the modernization of thermal power plants drafted by the Russian Ministry of Energy. This project will make it possible to upgrade up to 41 GW (including the Far East and non-price zones) of the installed capacity of TPPs. The modernization program will not only update the outdated capacities of TPPs, but will also provide orders for domestic manufacturers of power equipment and localize the use of foreign technologies and equipment in Russia.

## Innovative Development Program

Mechanisms for meeting innovative development objectives set by the Inter RAO Group's Strategy are spelled out in the Innovative Development Program of PJSC Inter RAO for the period until 2020 and beyond to 2025, were approved by the PJSC Inter RAO Board of Directors on October 28, 2016,<sup>5</sup> and include:

- enhancing energy efficiency
- developing new production technologies
- developing a quality control system
- cooperation with universities and research organizations
- modernizing existing facilities
- introducing R&D results

The Innovative Development Program is being implemented in three basic areas:

- the development of new technologies – technological innovations
- the development, release, and introduction to the market of new products and services – product (including service) and marketing innovations
- the selection and testing of new approaches in management – management innovations

<sup>5</sup> Minutes No. 183 dated October 31, 2016