Roinn Cumarsáide, Fuinnimh agus Acmhainní Nádúrtha
Department of Communications, Energy and Natural Resources

Oifig an Aire
Office of the Minister

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Baile Átha Cliath

29-31 Adelaide Road
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Mr John Horgan
Chairman
Bord na Móna plc
Main Street
Newbridge
Co Kildare

11 April 2014

Dear John

The Minister for Public Expenditure and Reform and I have given consideration to the way in which Government objectives for Bord na Móna PLC ("**BnM**" or the "**company**") are formulated and shared with BnM, and our respective Departments have consulted with the NewERA unit of the National Treasury Management Agency ("**NewERA**") in this regard. Arising from that work we have decided to initiate a more structured approach to confirming Government's objectives for the company over the short and medium term with a view to assisting it in its operations and in complying with its obligations under the prevailing governance framework.

This letter is intended to provide guidance to BnM and its Board of Directors (the "**Board**") with respect to Government's current objectives for BnM and the primary considerations which will be taken account of by us (and other relevant Government Ministers) in respect of certain of the matters for which our consent is required under the Turf Development Acts 1946 to 1998 and the Code of Practice for the Governance of State Bodies (the "**Code**"). We believe that this letter will be helpful to the company particularly in its corporate and strategic planning processes. It is our intention that we would issue henceforth a similar letter on an annual basis.

The specific objectives outlined in this letter should be considered in the context of the Government's overall current policy objectives for BnM, namely that:

- BnM should continue to deliver on its corporate strategy, including contributing to regional economic development in the Midlands and West, providing sustainable, quality employment in these regions and contributing to the development of the wind generation and biomass industries.
- BnM should remain as a profitable company with financial policies and a capital structure that is consistent with same.

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1. Dividends

The 2013 Budget figures included an additional €100 million in dividends, to come from across all the commercial semi-State companies. I note the Board's payment of an additional dividend of approximately €2 million in 2013, which was very much appreciated.

Aside from the dividend referred to above, it is the Government's wish that BnM would now develop a new formal dividend policy which would reflect the following principles:

(A) an appropriate balance should be struck between payment of dividends and reinvestment in the business; in this context it is the strong objective that a robust medium term framework for the calculation of dividends be put in place which would reflect the imperative that Bord na Móna remain strong financially and in a position to invest commercially whilst also delivering an appropriate return to the Shareholders,
and

(B) the proposed policy should also be related to an agreed proportion of a cash flow as well as net profit after tax.

The objective of formulating a new dividend policy is to assist the Board by bringing clarity to the Government's objectives as regards future dividend payments over the medium term, thereby avoiding the uncertainty created by special dividends potentially being requested from time to time. It may still be necessary or appropriate for special dividends to be paid from time to time (e.g. in event of sales of assets, windfall gains etc). To the extent that any special dividend is paid, it is our expectation that the likely impact of such payment on the dividend policy would be reviewed at the time.

We ask that you engage actively with NewERA and my Department with a view to developing an appropriate new dividend policy.

2. Shareholder Returns

We propose to augment our monitoring and measurement of BnM shareholder returns and in this regard we will be reviewing total shareholder return (TSR) over a 5 year period, assisted in this process by NewERA. We acknowledge that returns will vary from year to year, sometimes due to temporary or non-controllable factors but it is a key Government objective that BnM delivers shareholder returns over the relevant period that are in excess of its equity cost of capital.

It may be helpful for us to provide the company further guidance as to our views on the cost of capital. In this regard, we have asked NewERA to contact BnM management with a view to progressing a review of the company's cost of capital and the process by which the cost of capital is estimated, which will inform our guidelines to the company on the cost of capital.

As regards measuring TSR, Appendices I and II set out the financial performance measures in respect of profitability and shareholder return which we propose to apply. As you will see one of those measures necessitates the use of the commercial equity value of the company. We ask that BnM procure an independent third party to carry out a formal commercial equity valuation of the company with a valuation date as at 31 March 2014. We are conscious of the process you are engaged in regarding the potential merger with Coillte, so we are requesting that this valuation be submitted to my Department by 27 June 2014. The terms of reference for the valuation should be agreed with my Department and NewERA in advance of appointing the third party. This valuation will be reviewed by NewERA and my Department, in consultation with the Department of Public Expenditure and Reform, and your views in relation to any divergence will form part of the discussion. We expect that a similar valuation exercise will then be carried out on an annual basis with a valuation to be carried out by an independent party at least every three years.

This proposed approach to developing a perspective on shareholder return will be reviewed on an on-going basis and may be adapted as necessary.

3. Specific Policy Objectives

In addition to the specific policy objectives listed above, I wish to ensure that BnM continues to work actively to support delivery of key government policy objectives in terms of safeguarding security of energy supply, development of a sustainable energy future, and competitive, efficient and properly regulated energy markets, while also working to support important new national policy initiatives, subject to commercial considerations.

We are aware that BnM has the potential to play a key role in developing significant wind generation projects in the Midlands, both for domestic and potential export markets. In principle, we are supportive of the company continuing to be active in this area as a commercial proposition, i.e. subject to ensuring the correct balance between commercial returns and financial and other risks for the company.

We are also aware of the ongoing interaction between BnM, Dublin City Council and Irish Water in relation to the proposed Dublin Water Supply Project, and that BnM has a potentially critical role to play in its successful delivery. We are supportive of the company's involvement in this project, again subject to commercial considerations.

We appreciate the contribution that Bord na Mona has made to the evaluation of how to give effect to a beneficial merger of BnM with Coillte, on a commercial basis, to create a streamlined and refocused commercial state company operating in the bio-energy and forestry sectors, as committed to in the Programme for Government.

We acknowledge that the above will require an appropriate level of ongoing investment by BnM. In developing and implementing any new projects, care must be taken by BnM to prioritise core areas of activity.

4. Governance Arrangements

Corporate Plan

With respect to the rolling 5 year corporate plan which BnM is required to prepare and submit to us pursuant to the Code, NewERA and our Departments will engage with you early in this process in order for us to provide feedback to you on the plan in a more timely fashion.

We welcome the fact that the Board has undertaken a strategic review of the company's corporate strategy. We acknowledge the imperative for BnM to continue its move away from reliance on the declining peat market and believe that it is timely to review the diversification strategy and refocus on the higher growth potential business options.

Reporting

As you know the Code sets out current requirements in terms of reporting obligations, which supplement BnM's obligations in this regard under the Turf Development Acts 1946 to 1998, as amended. We also expect BnM to continue with the quarterly meetings that are held with NewERA and our Departments, and we are very appreciative of the co-operation that BnM have shown to date in this regard. We also anticipate a continuation of the existing policy of regular communication with both Departments and NewERA should any material matters arise.

Board Evaluation

Consistent with the requirement in the Code we expect that the Board will continue to review its own operation and performance and that of its committees and individual members, with the Board undertaking an evaluation of its performance on an annual basis and that the Board considers having such an evaluation facilitated by an independent assessment every three years. We know that such a review and evaluation process in BnM is currently led by the Chairman and expect that it allows each Director to give honest and constructive feedback on performance, both individually and for the Board as a whole.

We request that a formal high-level feedback report be provided to us (copied to NewERA) on overall Board performance, key focus areas for continuing development and assurance that the process has been properly implemented.

Ministerial Approvals

Existing arrangements for obtaining Ministerial approvals required under the Turf Development Acts and other relevant legislation will continue to apply. NewERA and our Departments will engage with you in relation to such requests in order for us to deal with these issues in a timely fashion.

Engagement

Our expectation is that you will engage with NewERA and our Departments in the near term to discuss the matters set out in this letter in more detail. This process will enable the company to set out its perspectives in relation to the proposed approach set out in the letter and appendices. I am, however, anxious that this process would be concluded quickly and in this regard, I would be grateful if you would make appropriate arrangements for discussions with NewERA and the Departments.

Yours sincerely

Pat Rabbitte

Pat Rabbitte T.D.
Minister for Communications, Energy and Natural Resources

CC Brendan Howlin T.D.
Minister for Public Expenditure and Reform

CC Eileen Fitzpatrick
Director, NewERA

Appendix I: Financial Performance Measures

Shareholder Return

Measure	Calculation
Total Shareholder Return (TSR)	(Commercial equity value (end) *less* Commercial equity value (beg) *plus* Dividends *less* equity injected) / Commercial equity value (beg).
Dividend yield	Dividends paid / Average commercial equity value
Dividend payout	(i) Dividends paid / Adjusted net profit after tax (prior year) (ii) Dividends paid / net cash flow from operating activities
Return on Equity	Adjusted net profit after tax / Average Equity
Earnings Growth	Compound Annual Growth Rate in Adjusted net profit after tax

Profitability / Efficiency

Measure	Calculation
Return on Capital Employed (ROCE)	(i) Adjusted EBIT / Average Capital Employed (ii) Adjusted EBIT / Adjusted Average Capital Employed

Leverage / Solvency

Measure	Calculation
Gearing Ratio (net)	(i) Net debt / net debt *plus* equity (ii) Net debt / Net debt *plus* pension liabilities *plus* employee related liabilities *plus* equity
Interest Cover	Adjusted EBITDA / Interest paid
FFO Interest Coverage	Funds from Operations *plus* Interest Paid / Interest Paid
FFO / Debt	Funds from Operations / Gross Debt
Retained Cash Flow (RCF) / Capex	Funds from Operations (FFO) *less* Dividends / Capex [Measures ability of cashflow generated to cover Capex]

Definitions of Key Terms used in calculations

Term	Definition
Adjusted EBIT	Earnings before interest and tax adjusted for exceptional or extraordinary items, payment of dividend or other distribution on, or in respect of any share in the capital of the Company or the transfer of any sum to reserves, the proportion of profits or gains which is attributable to minority interests in subsidiaries, any credit shall have been taken for income from associated undertakings which increase the consolidated net profit in that financial period and in no event taking account of any finance costs and income in respect of any pension

	scheme deficit or surplus or IFRS fair value movements. For the avoidance of doubt, land sales in the ordinary course of the business of any member of the Group shall not be deemed extraordinary or exceptional.
Adjusted EBITDA	Earnings before interest, tax, depreciation and amortisation or writing off of goodwill or other intangible assets adjusted for exceptional items writing off of goodwill or other intangible assets or IFRS fair value movements. For the avoidance of doubt, if a Subsidiary has been acquired or disposed of since the date as at which the latest audited consolidated financial statements of the Group were prepared, EBITDA shall be deemed to be adjusted in order to take into account the acquisition or disposal of that Subsidiary and its annualized earnings during the relevant Rolling Twelve Months.
Adjusted Net Profit after Tax	Net profit after tax adjusted for exceptional items and IFRS fair value movements
Adjusted Capital Employed	Net debt *plus* equity *plus* pension liabilities *plus* employee related liabilities
Capital Employed	Net debt *plus* equity
Commercial Value	See Section 2 of this letter
Dividends Paid	Dividends paid during the financial year per the cashflow statement (excl. special dividends)
Equity	Total shareholder(s) equity taken from the balance sheet
Fair value adjustments	Includes unrealised fair value gains/losses on derivatives or all fair value gains/losses on derivatives where the entity does not separately identify unrealised items
Funds from Operations	Net cashflow from operating activities (post interest, pre capex and tax paid and pre-working capital changes)
Gross Debt	Interest bearing debt such as loans, bonds and commercial paper *plus* interest bearing finance leases
Interest Paid	Interest paid for the financial year on interest-bearing debt per the company's cashflow statement
Net cashflow from operating activities	Taken directly from the cashflow statement - ensure interest paid is included
Net Debt	Interest bearing debt (defined below) less cash Debt means: Moneys borrowed; Any amount raised by acceptance under any acceptance credit facility or dematerialised equivalent; Any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument; The amount of any liability in respect of any lease or hire purchase contract which would, in

	accordance with GAAP, be treated as a finance or capital lease; Receivables sold or discounted (other than any receivables to the extent they are sold on a non-recourse basis); Any amount rained under any other transaction (including any forward sale or purchase agreement) having the commercial effect of a borrowing; Any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price (and, when calculating the value of any derivative transaction, only the net market value shall be taken into account, if any);Any counter-indemnity obligation in respect of a guarantee, indemnity, bond, standby or documentary letter of credit or any other instrument issued by a bank or financial institution; and the amount of any liability in respect of any guarantee of indemnity for any of the items referred to above
Net Debt to EBITDA	As determined on a rolling twelve month basis as at each Accounting half year

Appendix II: Financial Performance Measures – TO BE CALCULATED AT YEAR END ONLY

Shareholder Return

Measure	Calculation
Total Shareholder Return (TSR)	(Commercial equity value(end) *less* Commercial equity Value (beg) plus Dividends *less* equity injected) / Commercial equity value (beg)
Dividend yield	Dividends paid / Average commercial equity value
Dividend payout	(iii) Dividends paid / Adjusted net profit after tax (prior year) (iv) Dividends paid / net cash flow from operating activities (v)Dividends paid / (net cash from operating activities less capex)
Return on Equity	Adjusted net profit after tax / Average Equity

Earnings Growth	Compound Annual Growth Rate in Adjusted net profit after tax

Profitability / Efficiency

Measure	Calculation
Return on Capital Employed (ROCE)	(iii) Adjusted EBIT / Average Capital Employed (iv) Adjusted EBIT / Adjusted Average Capital Employed

Leverage / Solvency / Credit Metrics

Measure	Calculation
Gearing Ratio (net)	(iii) Net debt / Net debt plus equity (iv) Net debt / Net debt plus pension liabilities plus employee related liabilities plus equity
Interest Cover	Adjusted EBITDA / Interest paid (PP Covenant Basis)
FFO Interest Coverage	S&P, Moody's & Fitch bases
FFO / Debt	S&P and Moody's basis
FFO Adjusted Net Leverage	Fitch Basis (equivalent to FFO / Debt metric)
RCF / Capex	Moody's Basis [(FFO – Dividends) / Capex] [Measures ability of cashflow generated to cover Capex]

Definitions of Key Terms used in calculations

Term	Definition
Adjusted EBIT	Earnings before interest and tax adjusted for exceptional items and IFRS fair value movements
Adjusted EBITDA	Earnings before interest, tax, depreciation and amortisation adjusted for exceptional items and IFRS fair value movements
Adjusted Net Profit after Tax	Net profit after tax adjusted for exceptional items and IFRS fair value movements
Adjusted Capital Employed	Net debt *plus* equity *plus* pension liabilities *plus* employee related liabilities
Capital Employed	Net debt *plus* equity
Commercial Value	See Section 3 of this letter
Dividends Paid	Dividends paid during the financial year per the cashflow statement (excl. special dividends)
Equity	Total shareholder(s) equity taken from the balance sheet
Fair value adjustments	Includes unrealised fair value gains / losses on derivatives or all fair value gains / losses on derivatives where the entity does not separately identify unrealised items.
Interest Paid	Interest paid for the financial year on interest-bearing

	debt per the company's cashflow statement.
Net cashflow from operating activities	Taken directly from the cashflow statement - ensure interest paid is included
Net Debt	Interest bearing debt such as loans, bonds and commercial paper plus interest bearing finance leases *less* cash