

LEGISLATIVE COUNCIL

GOVERNMENT BUSINESSES SCRUTINY COMMITTEE A

Thursday 2 December 2010

MEMBERS

Ms Forrest
Dr Goodwin
Mr Hall (Chair)
Mr Harriss
Mr Wilkinson

IN ATTENDANCE

Hon. Bryan Green, Minister for Energy and Resources

Ministerial Office

Ms Alison Turner, Adviser
Mr Gary Swain, Head of Office

Aurora Energy Pty Ltd

Mr John Hasker AM, Chairman
Dr Peter Davis, Chief Executive Officer
Mr Darren Smith, Chief Financial Officer and General Manager, Commercial Services Division
Mr Rick Inglis, General Manager, Strategy and Corporate Affairs
Mr Michael Brewster, Chief Operations Officer, Energy Business and CEO AETV Power
Mr Andre Botha, General Manager, Network
Mr Mike Larkin, General Manager, Telecommunications

The committee met at 9 a.m.

CHAIR (Mr Hall) - Welcome, everyone.

Mr GREEN - We are pleased to be here. There is no doubt that 2009-10 has been a challenging year for Aurora. It recorded its first annual loss since the inception of the company 12 years ago, largely as a result of integrating the AETV Power station into the operations and progressing the development of the new billing system. The year 2009-10 was also one of increased storm activity, which created some unreliability issues and at the time when customers are feeling the impact of rising prices. Despite the challenges, including the focus on prices and the billing system and the relationships with other electricity businesses, Aurora realised some very notable achievements during 2009-10 and I would like to ensure that these are placed firmly on the record.

The distribution business spent a record \$145.4 million upgrading and maintaining the State's poles and wires network to improve electricity supply and reliability for Tasmanians. The investment is obviously critical to ensuring that we keep the lights on for all Tasmanians. The construction of the gas-fired Tamar Valley Power Station, which now meets around 10 per cent of the State's energy needs, was completed on time and \$25 million under budget. Controlled costs were \$18.1 million below budget. The safety sensor, marketed in Tasmania as Cable PI and nationally as WireAlert, was distributed to all Tasmanian households and small businesses and is helping to protect customers from a wide range of potentially life-threatening electrical faults. The company delivered on responsibilities under the Tasmanian rollout of the NBN. Electricity sales volumes were up by 8.6 per cent in the year, with retail sales revenue now more than \$1.05 billion, which is helped by new contracts such as the Victorian Health department.

To the future, I am confident of an improved outlook for Aurora. Improved contractual arrangements will assist in this and I expect Aurora will be able to make a significant positive contribution to the expert panel. I know the Government and Aurora are looking forward to that. I also acknowledge and thank the Chairman of the Board, John Hasker, and CEO Peter Davis, and all his employees for their efforts throughout the year. There has been a significant amount of sustained pressure on Aurora but they have handled it extremely well.

Finally, I would like to thank outgoing directors, Brian Keane and Tony Beach and welcome the appointment of Dr Michael Vertigan and Mr Mervyn Davies and the reappointment of Geoff Willis to the board. I hand over to the Chairman - if you would like to make a few comments.

Mr HASKER - Thank you, Minister, I would be happy to. I reiterate what the minister said and the report copies are here for those who solicited them. I think that I've covered fairly well in the annual report the things that affected us both positively and negatively in the 12 months. It was a year that we had never seen or ever thought we would see, which flowed on from the purchase of a half-built power station in the Tamar Valley which we set about completing, and we completed it within budget, on time and uniquely without a single accident occurring to the workforce that was there. The additional quarter of a billion dollars in debt that we took on plus the dislocation that emerged in our market as a result caused us to suffer the year that we did.

Minister, I thank you for your leadership. You took on the role with us at a very difficult time and we particularly thank you for sitting down and working with us and with the industry to sort out a pricing arrangement which will position us well, I believe, for the next period, which is three years. Our results in the months that have flowed since 1 July have been very encouraging. I thank you for that. I also thank my fellow directors and particularly CEO, Peter Davis. Peter really did, along with his staff, suffer a lot of flak during the year as things emerged and we received criticism which, in many cases, was overdone or unjustified.

You mentioned the Cable PI and I have a little one sitting here. This was a piece of technology developed here in Hobart; absolutely unique. I think it is world class technology and already there is some excitement nationally with most of the other distributors looking at it, testing it, trialling it, seeing if they can include it in their capital program. I think there is a chance that it will have some use in the international market. So, well done; it was developed here in town and is a very worthwhile thing.

Mr Chairman, I think that supports what you have said; thank you once again for your leadership. We look forward to a very sound trading year in the year that we are in.

CHAIR - Thanks, Minister. I think we might start with financials of the enterprise. I have a couple of questions to kick things off, Minister. I am just trying to understand that whilst Aurora recorded a loss of some \$20 million for 2009-10, they were still required to pay a dividend of about \$4.5 million to the Government. Is it the case that whilst it seems that Aurora is borrowing to cover its operating losses, it is also borrowing to pay its dividend to the Government? If so, would you not agree that it is a very unusual and potentially unsustainable scenario?

Mr GREEN - You mean the dividend in normal circumstances?

CHAIR - Yes. As I say, you paid \$4.5 million.

Mr GREEN - We didn't take the dividend. The recommendation was issued for us not to take a dividend.

CHAIR - At all?

Mr GREEN - Yes; in recognition of the issues faced.

Mr HASKER - Chairman, I think the dividend that you are talking about is the one in our annual accounts.

CHAIR - Yes.

Mr HASKER - It was the dividend that we declared for the year 2008-09 and it was therefore a cash payment that emerged earlier on.

CHAIR - Right. So there was no dividend at all this year, given the situation.

Mr HASKER - We have a dividend formula that we traditionally use which smooths our performance over a number of years. Using that formula, the ability was there for us to pay a dividend and we satisfied the financial criteria within the appropriate regulatory institutions but the Government advised us that they would not accept that, so no dividend was declared for the year we have finished.

Mr GREEN - The year that we have just finished.

CHAIR - Okay.

Mr HASKER - So a payment will not head to government during this year we are in; for that year it will be zero.

Mr HARRISS - Just on that then, Mr Chairman, if I may, to the minister or John or both, my understanding is that the board, as you have just said, John, has concluded that the payment of a dividend of about \$3.9 million was possible under the process which you have explained and you have explained the smoothing process over about a five-year period - I think that has been the rule of thumb that you have been operating with, and you could have. Is my understanding correct that the board actually did recommend that the payment of a dividend could be facilitated, and if that understanding is correct that that would have been way under the 50 per cent benchmark set by the Treasurer's Instructions or the Government for GBEs and SOCs, and it would have been a negative 30 per cent on the numbers that I have looked at rather than the 50 per cent after tax?

Mr HASKER - We developed a figure based on our five-year smoothing rather than a percentage of our net profit so that we have a smoother payment rather than taking a figure. Was the figure \$3.9 million, as Paul has indicated, or was it lower than that?

Dr DAVIS - The Aurora board did recommend that a dividend could be paid for this year and, as the chairman and the minister have both indicated, to try to ensure that the State gets predictable and smooth returns from Aurora rather than a huge dividend one year and nothing the next year we have traditionally calculated our dividend based on 50 per cent of after-tax profits averaged over the last five years.

Mr HARRISS - Which is the government benchmark anyway.

Dr DAVIS - That is correct. In the year that has just gone we have made a loss of \$20 million so the Government is not going to give us money back, if you like, so 50 per cent is zero zero but when you average it over the five years it means that you have the benefit of four previous good years to accommodate.

In terms of the other part of the question about borrowing to fund the dividend, the reality is Aurora produces a substantial amount of cash. The company basically sells electricity and it brings revenue from customers and that is used to defray the operating costs of the company, so paying salaries, contractors, dividends and so on like that, and it also funds the majority of the capital program. We have a very large capital program that sets the company up for the next 30 years building infrastructure for Tasmanians and the cashflow in the last couple of years in fact has not been sufficient to fund the full capital program. Where the borrowing comes from in fact is borrowing for the long-term investment in infrastructure in Tasmania and that is like an investment loan, if you like, a bit like taking a loan if you have an investment property - the tenants pay the rent; in our case the returns on that loan are through the tariff and these are long-life assets. They last for 30 or 40 years and over that time the Tasmanian people get the benefit of those assets and they effectively pay for those assets through the annual tariff. That is what the borrowing is there for; it is to fund that long-term investment.

CHAIR - On that same point, if you had paid the dividend, it would have had to come out of borrowings, is that what you are saying?

Dr DAVIS - It depends on which order you calculate the money and where it comes from but traditionally you would fund the operations out of the cash, you fund the dividend out of the cash, you fund the majority of the capital program out of the cash but obviously if you are funding for 30 years' worth of infrastructure you do not necessarily generate enough cash in any one year to fund all of that, particularly in the circumstance where the network is growing and, as the minister

pointed out, Aurora invested a record \$145 million in improving the security and reliability of supply. A lot of that was due to customer demand for new connections so, as the economy has grown, there has been something in the order of \$45 million worth of customer-generated work. This is where customers might want to connect in a factory or a shopping centre or build a subdivision and so we have to basically respond to all of that. The customers pay for it over time and Aurora takes a loan to fund the upfront cost so in some ways we act like a bit of an infrastructure bank: we are providing the infrastructure for the customers, for the people of Tasmania, and effectively we are borrowing to do that so the dividend is really not part of that equation.

[9.15 a.m.]

CHAIR - To follow on from that, very quickly, while we are on the subject of dividends and it may be a philosophical type of question, it has been said by some people that if the Tasmanian economy is under the pump and some of the energy authorities can be under the pump, and the Tasmanian taxpayers being effectively the shareholder of the whole lot, then really should dividends be paid back to government at this time? If there are problems, would it not be better not to pay those dividends and allow cheaper power prices to small business and other consumers? It is a question I put to the minister, philosophically.

Mr GREEN - Philosophically, I think, given that these are corporations operating under normal corporate law and part regulated mean that, yes, there should be a return to government and those funds distributed in the appropriate way. I think that Aurora, overall, made a significant contribution to Tasmania in facilitating the workforce that it has, the payroll tax that it has paid, \$31.3 million et cetera. There is a significant contribution to the State overall as a result of Aurora operating within the Tasmanian context. Of course, as indicated, a significant part of the growth opportunities that Aurora has is through an opportunity it has right now with the Victorian Health department, so we are talking about customers interstate as well as part of the national market. So I think, philosophically, the right thing to do is to take the dividend from the company.

Mr HASKER - Our cash returns to government, excluding dividends, amounted to some \$31 million.

Ms FORREST - That includes your income tax equivalents, your payroll tax and everything, the whole lot?

Mr HASKER - Yes, the whole thing, the money that flows into the Government other than dividends.

Dr DAVIS - Perhaps, Chairman, if I could add to that answer. The company, Aurora, is owned by the people of Tasmania. So in many ways, the people of Tasmania invested in the company and its prime purpose is to deliver reliable supplies of electricity at the lowest sustainable cost. If you own a company, as the Tasmanian people do, it is appropriate that they see some return on that ownership. So the majority of the money that the company earns is being kept within the company to continue to fund the programs that it is involved in for Tasmanians. But there is a small proportion in the form of a dividend and these income tax equivalents and loan guarantee fees and so on that is returned effectively to the owner. So it is like an investment that the Tasmanian people have because the Tasmanian people own these companies, rather than if they were privately owned, the private shareholder would expect a return in the same way.

Mr GREEN - They also provide obviously for essential services and other things, Mr Chairman.

Mr WILKINSON - Can I ask a general question in relation to the business? I suppose it is a question that we should be asking ourselves each year and that is, you look at your pluses and minuses for the year. You have spoken about the pluses, I take it, so you have your \$31.3 million payroll tax, you have your employment, which I think is something that a number of people forget from time to time, that you have to have industry and employment within the State to make the wheels go round. What, this year, do you believe have been your bad things that we should look at?

Mr HASKER - You want a balanced view, Jim.

Mr WILKINSON - Yes, I know you are a Melbourne footy supporter.

Mr HASKER - Yes, I am used to a balanced view.

Mr WILKINSON - What I am asking you is: what do you think you could have done better this past year?

Mr HASKER - I have given some overall comments. Perhaps if I ask Dr Davis to explain those as he sees them.

Dr DAVIS - It is always wonderful being asked in a committee like this -

Mr WILKINSON - Yes, hindsight is 20/20 vision, I believe.

Dr DAVIS - That is right, with all the things you could have done better and there is always a number. I think the energy market proved to be more challenging than we expected and I think we did not fully anticipate the cost challenges of operating the gas-fired power station. In retrospect, maybe some alternative hedging strategies or perhaps a more or less bullish forecast of the returns from that would have been appropriate.

A second area that has achieved quite a bit of media coverage during the year is the billing system and I am sure we will get some questions on the billing system during the process. We underestimated the complexity of that project before it was started and it was necessary to apply additional resources to complete it. They were two areas in which the results were a little disappointing.

Our safety performance slipped slightly. In terms of the Australian energy industry, we achieved a lost time injury frequency rate of 3.0 and the top quartile is 2.6. It is very disappointing when people are injured in the workplace. We did have one serious injury during the year when one of our staff received a flashover burn and we have done a very detailed investigation of that. We have a culture of trying to do the right thing by the customers and that means we do a lot of work that is live on the system. This employee was injured working on a switchboard for a supermarket that was being done live to try to avoid interruption to the customer. Clearly, when we reviewed the incident that was not something that we should have pursued. So that would have been another disappointment that I could comment on.

Most disappointing were the attacks that our people received, both in the media and as abuse from members of the public. I think it is very easy for people, responding to rises in the price of power, to latch on to topical issues. During the year we saw criticism of such things as the number of employees, whether or not employees get a discount, even whether there was a Christmas hamper handed out last year. I found that very disappointing because it really missed the point, and the point was that power prices have gone up due to the investment in infrastructure. Aurora accounted for only 39 per cent of the total energy bill. The power price rises on 1 July were a result of a decision by the Australian Energy Regulator to cater for an increase in transmission costs. It is very pleasing to see that Transend is building more infrastructure to strengthen the backbone of the system. The power price rise on 1 December, again approved by independent regulators, relates to the wholesale energy market costs and, in particular, the increase in the security of the energy markets. They are the real reasons, but of course that was not what got attention during the year. It is quite disappointing because, as I mentioned, Aurora is owned by the people of Tasmania and damaging the Aurora brand is not a good thing for a business owned by the people of Tasmania, when we face competition.

The financial performance during the year we are reviewing, 2009-10, was disappointing, but we will come out of that. We have a new wholesale purchasing arrangement with Hydro Tasmania which is good for Hydro and good for Aurora. What is hard to recover from is the brand damage that has occurred due to ongoing negative publicity. That will take a while to recover from and we see that measured in terms of how our staff are treated when they go to people's premises, in the letters and complaints that we receive and, indeed, in the independent measurement that we undertake of our brand image in the community.

There you go, I gave you an open answer to those disappointments.

CHAIR - Yes, we have to keep the answers succinct.

Mr WILKINSON - Always you have to be your hardest marker. So, being your hardest marker, they would be the areas that you would be focusing on next year and that is why you did not do as well as you thought you would in the past year.

To balance the ledger, I did note that you said the results since 1 July were very encouraging. What have they been, to give us that balance that we spoke about at the start?

Dr DAVIS - When we looked at last year's results, we found the losses arose from two factors. One was what we learned about the operation of the Tamar Valley Power Station and the purchase arrangements we had prior to June with Hydro Tasmania. Those issues have largely been addressed through a new wholesale purchasing agreement. Secondly, we had costs associated with the billing system. Both those issues have been addressed and Aurora has returned to a sustainable position and is likely to return profits akin to previous years. We are on budget at the moment. We are very focused, however, on customer prices and there is a lot of work going on in Aurora to keep costs down as much as we can. Next year, when we attend this inquiry, I am hopeful we will have much better results.

Dr GOODWIN - One of the questions I have concerns the Tamar Valley Power Station. This keeps cropping up as a significant issue in Aurora's financial troubles and I am trying to understand exactly what the issues are with the Tamar Valley Power Station. Obviously one issue is the level of debt and, Dr Davis, you just mentioned the challenges associated with operating a

gas-fired power station. Can you elaborate on what the issues were with the Tamar Valley Power Station?

Dr DAVIS - The main issue was that customers were not paying enough to cover the running costs of the Tamar Valley Power Station. The purchase price we were paying Hydro was greater than the money we were receiving from customers for the balance because Tamar Valley does not cover the whole of the load, it covers part of it. It might be appropriate to call the CEO of our subsidiary, which is called Aurora Energy Tamar Valley -

CHAIR - As long as we keep the answers brief because we have a lot of other things to do as well.

Dr DAVIS - Absolutely. Mike Brewster is an engineer so I am sure he will be very brief.

Mr HASKER - Chair, Mike joined us at the time of the acquisition. Prior to that he was the chief engineer with the Hydro, so he was seconded to us and has remained with us. He is now the chief operations officers for the whole Aurora group.

Mr GREEN - Can I inquire as to how you expect questions to be answered, Mr Chairman? Obviously some of the questions are detailed and quite open-ended and I am not quite sure what sort of format you want, whether you want an open discussion, or do you want really succinct answers to some very specific questions?

CHAIR - The latter.

Mr GREEN - Well, the questions needs to be along those lines as well then.

CHAIR - It is a big enterprise and we probably have hundreds of questions to get through so if we have long, open-ended questions and/or long answers we are never going to get where we want to be.

Mr HASKER - I would suggest that the power station has really been the issue.

Dr GOODWIN - It seems to be, that is why I asked the question, to try to narrow the discussion.

Mr GREEN - We are happy to give you a long history of the power station.

Ms FORREST - We do not need a long history, we want to know what the challenges are.

Dr GOODWIN - We need to know what the challenges are and why it led to the financial difficulties and why they were not anticipated in the first place.

Mr BREWSTER - I think I can give it fairly simply. When construction of the power station started there were three parties: Alinta, Hydro Tasmania and Aurora. Under that deal Aurora had a very economical energy price from Alinta, which subsequently became Babcock & Brown, which allowed us to compete. When we purchased the power station we inherited all the running costs of the power station, which were far in excess of the hedge price that we had been given by Alinta. Why Alinta chose to give us a very economic price is for them to discuss. All of

a sudden we got a very expensive operating regime compared with what we had under the original hedge deal. That is one half of the equation.

The other half of the equation is that until we brought the power station in there had been no competitive wholesale market and little variation in the electricity spot price in Tasmania, so no one had observed significant variations in spot price, which can vary from -1 200 to 12 500. We came into the market, and obviously Hydro responded in a competitive manner, and there was subsequent volatility. When there are only two players in the market it is a binary outcome.

You put those two together and it makes for a very different outcome than Aurora would have had under the original hedge deal. To be frank, that is the price you pay for security. That is the judgment that always has to be made. What we struggled with was estimating what the spot price would be. We sat back and said what is the historical spot price? What do we learn from the mainland? What should we expect here? But ultimately on the mainland there are many competitors. So when there is an issue with a power station, such as the Tamar Valley Power Station, there is another power station to come in. In Tasmania that does not occur. Any issues where there is a loss of energy in the market are replaced by only one other provider. They determine the spot price because there is only one competitor. Does that answer your question?

[9.30 a.m.]

Ms FORREST - I want to go down that path a bit further. With the issues with the volatility in the spot market in June and April last year, you were referring the matter to the ACCC -

Mr HASKER - We never referred the matter.

Ms FORREST - Okay. The matter was being dealt with by the ACCC.

Mr HASKER - I would like to put that on the record. We never referred the matter. It was in the public arena and they picked it up from that.

Ms FORREST - There were some costs incurred by Aurora through that.

Mr HASKER - Our cost was zero.

Mr BREWSTER - Our external legal costs were zero.

Ms FORREST - The decision was made when the power station was bought by Aurora as opposed to buying by the Hydro. That was on a recommendation of the ACCC, I understand. That is what we were told during the debate. Otherwise Hydro might have potentially been given the power station.

In a situation here where you are producing power from another energy source, you are using one energy source to create another energy source and to make money out of it, I am interested in how you intend to make it profitable. If you are going to be selling power across Basslink at a relatively competitive price, you have to compete with the other major player in the game, which is Hydro. Is that ever going to work?

Mr BREWSTER - We do not sell energy across Basslink so in essence we can only sell it to Tasmania. Only Hydro can supply across Basslink. It gets more complicated and I can explain that if you want me to. But in essence most energy sales are not about the spot market. What

happens is that you sell your energy on the back of a hedge deal. Basically we have an arrangement whereby a customer comes and says, 'We want 1 000 megawatts. What are you prepared to charge?' The hedge provides a fixed price for that. Where it gets difficult is that if their load in any five minutes is greater or less than the load they have nominated, then that has to be supplied from the spot price. But the majority of energy is sold at a contract price. Provided we can get an appropriate contract price, we can keep it stable.

Where it is challenging is, if you can imagine, if the spot price moves to \$10 000 for an hour. Then you very quickly lose your margins. So it is trying to prevent yourself from being caught in a position where you are short - in other words where you do not have enough energy to cover the customer load. In Tasmania quite often when that occurs, because there are only two parties, the price can shoot up to \$10 000 per hour or \$12 500. Sometimes we have to secure more energy than we would like to ensure that never occurs. That is the balance in the fine balancing act that we have to get right.

Ms FORREST - You have had a net hedge position deteriorating \$90 million over the last year, according to your figures. How is that reflected in your profit and loss? Has the hedging been appropriate in the last 12 months?

Mr BREWSTER - I cannot recall the exact hedge number.

Ms FORREST - It was \$45 million in 2006-07 down to -\$40 million - that is, a movement of \$95 million.

Mr BREWSTER - It could be market to market. It depends how much we are using of our own generation as well. A hedge is what we basically take from Hydro. Maybe we can come back to it; I have lost the thread of your primary question.

Ms FORREST - I am wondering whether the hedging arrangements that are being used are the most appropriate. We have a power station here that appears to be the noose around Aurora's neck. There are other impacts that we will get to at a later time, billing, for one, but the power station seems to be the big noose around the neck. How is the company going to turn it around so that it is a profitable business for the taxpayers of Tasmania?

Mr BREWSTER - Well, that, in essence, has already happened. As we advised earlier, we are making budget, particularly the energy business, and we are providing a return at the moment. The reason for that is we renegotiated the wholesale deal with Hydro for the regulated customers. Put simply, that is it in terms of your question about the effectiveness of our hedging. Of course, we would always look back and say, as earlier, we could do things a bit better. The hedging decision is made on the basis of an assessment of history of the market. We had no history of the market, as I said earlier; zero history. Normally, what would happen is, when you make a decision as to how you back your load, you look at a combination of fixed contracts like hedges, as I talked about earlier, and a combination of spot markets. There is some risk in spot markets, so the majority is on hedges. That is pretty much where we started. What we quickly found, unlike the mainland - as I said earlier, it is pretty much binary - is that we cannot afford to be exposed in the spot market as opposed to the mainland -

Ms FORREST - So you limited your exposure to the spot market.

Mr BREWSTER - We had to limit our exposure. That has helped. In addition, some of the difficulties occurred prior to the commissioning of the CCGT. As we were running up to that, we had some plant failures as part of the commissioning. They came on very quickly. When that occurs it is difficult to get an immediate hedge, particularly if you do not know how long it is going to be sustained or what the particular root cause is. So there are judgments to be made. You will find now that we take a very conservative position in the Tasmanian market. To this point in time, we are actually ahead of budget in the energy business. That has already been turned around.

Dr GOODWIN - So it has been a fairly steep learning curve, by the sound of things.

Mr GREEN - I guess it gets back to the principal decision with respect to why the Government asked Aurora to purchase the power station. It was because the global financial crisis meant that the power station would not be built. It was important, and people tend to overlook this, from an energy security point of view, to have that power station existing because of the fluctuations with respect to water levels in Tasmania and the very low levels that were achieved. Even with Basslink when the Hydro was at very low levels, the power station was needed. It effectively represents 10 per cent. So it was an important asset from our energy security point of view to have for Tasmania and the Tasmanian people.

It is true that it has been a significant learning curve. The Government had to act effectively to ensure that the negotiations took place to get it to a point where the power station could operate within the market, and that has happened. On top of that, Mr Chairman, we have a panel of experts who are without doubt leaders within the energy world, nationally, looking at how the energy businesses and supply is provided in Tasmania over the next 12 months. This will be important and, of course, Aurora will participate in that.

CHAIR - I suppose you partially answered the fundamental question, that is, as Ms Forrest said, since the gas-fired power station at Bell Bay has been a noose around the neck, would the Basslink cable not have provided enough security without Bell Bay?

Mr BREWSTER - No. I think people have a tendency to forget about the drought. You have to look at the history of water inflows to the system, not just for the last two years but the last 20 years, to get a sense of what the issue is. We have had extraordinarily good inflows in Tasmania in the last two years. Prior to that, without going back to exact numbers, we had seven or eight years where we had extraordinarily low inflows compared to before 2001. If we went back to where the water situation was three years ago we would be desperate for the Tamar Valley Power Station, particularly given the issues we had in the old Bell Bay Power Station; it is coming to the end of its life, we are having failures, so when you have a hydro power system you have water risk. There is water variability and it does not take a huge amount of variability -

CHAIR - I understand that.

Mr GREEN - The short answer is no.

Mr BREWSTER - Yes, and Basslink also has risks. There are limits on how much you can import on Basslink. Basslink can go down for other reasons so you still need security.

CHAIR - Are you confident about the security? Obviously there is a gas supply because you are buying one form of energy to convert into another form of energy.

Mr GREEN - We used to use oil.

CHAIR - Yes, I know we did but obviously gas is a much better option than oil. Do you have secure long-term contracts at a competitive price for the gas to be able to run that?

Mr BREWSTER - Yes, we have and not only that, we have diesel backup as well so we can run the peaking plant on diesel if there is extended loss of the gas-fired power station as well.

Mr GREEN - And we have some flexibility with respect to gas for mainland options as well. We can actually sell gas.

Mr BREWSTER - That is exactly right. We have more gas than we need for the power station and we sell the excess gas on the wholesale market at a margin.

Dr GOODWIN - I think the original plan was to sell the Tamar Valley Power Station when the GFC settled down. Is that still part of the plan?

Mr BREWSTER - The statements by the Premier at the time, Vanessa, loosely said five years so we are not quite halfway through that period since he made the statement. It was a five-year time cycle that was indicated.

Dr GOODWIN - There is still a possibility but it has not really been -

Mr GREEN - We have had no discussion about that.

Mr HARRISS - Just on the back of that then, Mr Chairman, unless Ms Forrest -

Ms FORREST - That is where I was going anyway. When the sale was debated in Parliament that was on the understanding that it was an interim measure to prepare it and sell it in the future.

Mr GREEN - The question was: are we intending to sell it? We have had no discussions at a board level or cabinet level with respect to selling the power station.

Ms FORREST - You have not even tested the market at all to see what is out there?

Mr GREEN - No.

Mr BREWSTER - I think, Mr Chairman, the critical issue, too, is that it is a matter for the Government as to whether the power station is sold at some point or not but Aurora's objective and that of AETV is to make sure that it is a viable, sustainable, profitable business so that it is something that people might want to buy and clearly the last year we had where we were commissioning it and we had some challenges, it was probably not the ideal time to be thinking about selling it. Our task, irrespective of who owns it, is to make sure that it is running well and that is what Mike and his team do. They take a lot of care with that and we use a lot of expertise from the suppliers of the kit to make sure that it is run safely and efficiently and at the lowest sustainable cost.

Mr GREEN - We are also looking forward to what the expert panel might say about the construct of the energy regime, if you like, in Tasmania from the point of view of competition.

Mr HARRISS - Still on that same thread, Mr Chairman, can I go back to a comment that Peter made when he was describing the landscape for the Tamar Valley Power Station? Peter, you said that there were somewhat 'bullish forecasts' regarding its operation. Who made those 'bullish forecasts'?

Mr BREWSTER - We made those forecasts because, as Mike indicated, there was no experience of how the market would operate so we had looked at previous spot prices in the market and spot prices had tended to be \$40, \$45, \$50 a megawatt-hour. We had no history to indicate that they would go to \$10 000 a megawatt-hour, which they did during our commissioning process so that was unexpected. There have been some other occasions when we found ourselves so-called long in the market, which means we have excess to sell, and the spot prices have dropped to \$20 per megawatt-hour. The market has been a little more variable than I think anyone anticipated, including ourselves, and that is one of the reasons that we have now entered into a three-year wholesale deal with Hydro Tasmania to provide us with a hedge so we have a known purchase price from Hydro Tasmania to basically work with the power station and avoid too much exposure to that spot market.

[9.45 a.m.]

Ms FORREST - When did that new arrangement start?

Dr DAVIS - On 1 July this year.

Ms FORREST - How has it been going since then?

Dr DAVIS - Very well, exactly as predicted which is why, as Mike has indicated, Tamar Valley Power Station is now operating in accordance with its budget and it is producing stable returns, which is good.

Mr BREWSTER - In answer to your question, yes, I am accountable. I was responsible for the bullish forecasts on the basis of the knowledge I had in April last year - that is the net result.

Mr HARRISS - That business, by itself, has what I would, I think accurately, describe as a massive debt exposure of about 300 per cent, debt to equity.

Dr DAVIS - It has \$260 million worth of debt and \$100 million or thereabouts worth of equity.

Mr HARRISS - So that still represents a significant challenge to that component of Aurora's business, doesn't it? The debt-to-equity issue at the Tamar Valley Power Station is significant, and will be, for what projected period down the track?

Dr DAVIS - I think, as was on the public record during the year and in discussions with the Treasurer and others, that, yes, the power station has a higher level of gearing than you would ideally like. It is serviceable, so we can pay the debt but obviously you are paying more interest than you would like to. So, in the event that the Government had a spare bit of money floating around that they would like to contribute to reduce that debt, that would be great, but that has not been possible and, indeed, as the minister indicated, the Government elected not to take a

dividend from Aurora this year in lieu of an equity contribution, I think that was the wording. So there is \$3 million towards reducing our debt. But the debt is serviceable, there are not issues with it, but to improve the profitability, obviously it would be preferable to reduce the debt.

The Tamar Valley Power Station will in fact start paying its debt down progressively from, I think, next year. So it will start to reduce the debt but clearly, it is a \$260 million debt against an asset that we spent \$360 million on; the building.

Mr HARRISS - That is the issue, isn't it, because that point that you have just made, Peter, the valuation being below the costs of acquisition and building to completion meant an overcapitalisation, in simplistic terms I suppose, for me. Was there a time when Aurora considered impairing the Tamar Valley Power Station and if that consideration was on the table at any time, what would the impact of that have been on the company's business? Specifically, I suspect a downgrading in your credit rating as a result of that, higher borrowing costs, and why wasn't part of the business impaired?

Dr DAVIS - Perhaps, Mr Chairman, if we could ask the Chief Financial Officer of Aurora to come forward because that is a rather technical accounting question but, as Darren Smith makes his way to the table, I can advise the committee that power station was not impaired, so it does generate sufficient revenues to justify its asset value on the balance sheet. Clearly, having the right arrangements in place for Hydro and having less exposure to the spot market was a very important part of that. But perhaps Darren Smith could comment on how we approached the impairment and those issues that we dealt with and why it was not impaired.

This is Darren Smith, Chief Financial Officer for the Aurora Energy Group.

Mr SMITH - We take impairment very seriously and I think there are some notes in the accounts about the critical estimates involved in doing an impairment - that is towards the back where a lot of the power prices and gas prices and all those things are. It is a very big focus on estimation, so there is a lot of rigour around that and it goes through the Audit Committee and the board.

Mr HASKER - Also the Auditor-General.

Mr SMITH - Also the Auditor-General and the external auditor as well. But it is probably fair to say that impairment I think is a good example of where the accounting requirements really just mirror commercial reality. Probably, to draw it to a head, if the deal had not been done from 1 July onwards, if the commercial fortunes of the company had not improved, there would have been an impairment and it would have been substantial. You can imagine that the difference in profit built for the year could imply that it would have been a substantial differential but it is therefore very important that the commercial fortunes did turn around and it is very pleasing to see that through July to November, we are on budget.

Mr HARRISS - On the back of the arrangement.

Mr SMITH - On the back of the arrangement and on the back of our focus on efficiencies and a number of other aspects, but it was a very clear focus of considerable levels of the organisation and fully worked through in terms of the accounting standards. I think it is a good example. Some of the hedging accounting standards are very complicated to the reader whereas impairment mirrors commercial reality, so it was definitely considered.

Mr HARRISS - Is there any emerging threat to the possibility of impairment going forward?

Mr SMITH - Certainly not at this stage. I can draw your attention to note 34 on page 117. There is a number of critical aspects and if any of those changed materially you would have to reassess it, but at this stage no.

Ms FORREST - How long is that arrangement with Hydro?

Mr SMITH - Three years - June 2013, I believe.

Ms FORREST - Would you like to address your mind to the questions I was asking about the hedging arrangements now that you are at the table?

Mr SMITH - I certainly can. It is an incredibly complicated set of accounting standards. In terms of commercial reality you can very often strike a hedge deal and then when the price goes the other way afterwards you can very often look back and say, 'I wish we hadn't hedged'. If I can draw you back to Mike Brewster's comments, not securing hedging and being exposed to that incredibly volatile spot market would have been potentially catastrophic, so we will always hedge.

Ms FORREST - But spot markets have been much more stable since that time.

Mr SMITH - Since 1 July, correct. At 30 June there are two factors at play. The first one is that the old arrangements with Hydro had unwound, so the charge through the profit and loss account in the year was just the unwinding of the previous hedge. The new hedge comes in from 1 July, so when we get to 30 June 2011 you will probably see quite large numbers in the accounts then for the new hedge deal.

Ms FORREST - That explains the net hedge position at the moment then, the unwinding of those?

Mr SMITH - Yes. One of the reasons it went down was because of the unwinding. The accounting rules are very complicated as to whether it is termed 'effective' in an accounting sense or not. If it is not effective, the change in market value goes through your profit and loss account. If it is deemed effective, it does not go through your profit and loss account but goes through the balance sheet. There are very complicated rules as to whether it is effective or not.

Ms FORREST - Has it been effective?

Mr SMITH - In a commercial sense or in an accounting sense?

Ms FORREST - Both.

Mr SMITH - In a commercial sense, absolutely effective. There are some very tricky clauses in the accounting standards as to how you treat it from an accounting point of view.

Ms FORREST - In an accounting sense?

Mr SMITH - In an accounting sense it is definitely effective, but whether you can explain it to the average punter is pretty complicated.

Dr GOODWIN - Just picking up a couple of things, Minister: you mentioned that one of the benefits of having the Tamar Valley Power Station is the drought-proofing issue. Is it a benefit to the community for it to remain with Aurora? You mentioned that the debt will start to be reduced next year but that one way of getting rid of the debt altogether is to sell it. Is there any community benefit in it staying with Aurora in the longer term?

Mr GREEN - As I have indicated, I think from the point of view of providing security to Tasmania's energy needs it is essential.

Dr GOODWIN - To stay with Aurora?

Mr GREEN - No, the plant itself is essential. I have been frank in that there have been no discussions with regard to a sale, certainly with me or the Treasurer or anybody else that I am aware of. We want to see it bed down. We have just finished building the station and we have got over a couple of major hurdles to allow it to operate within the market that is established here in Tasmania, which was challenging but we managed to work our way through that. Significantly, I think, as I mentioned in my opening statement, Aurora should be given credit at the outset, given the circumstances that prevailed with the global financial crisis. They came in and constructed the power station under budget, which is a significant achievement in itself.

Dr GOODWIN - And on time.

Mr GREEN - From a policy point of view overall, I guess that is a decision to be made. I indicated early on that there were thoughts as to how long we might hang on to the power station, but at this stage we have made no firm policy decision along those lines. You might want to announce your policy with respect to that today, I am not sure.

Dr GOODWIN - What I was really trying to get at was if there is some community benefit in it staying with Aurora.

Dr DAVIS - Perhaps, Mr Chair, if I could just add to the minister's answer there. We need to recognise that the Government's decision to purchase the power station was in relation to drought security. So you are talking about the fundamental security of the Tasmanian electricity system. If you wish to have that in the decision-making framework of a private board over which you would have no control and it might be that you have a situation like we did last year where the station makes losses, whilst it remains under Aurora ownership then at least the Government can be confident that the good of Tasmania is being thought about and the drought security is being addressed because we are a State-owned company.

If it were to be sold and privately owned then the decisions would be made in a boardroom in another jurisdiction or overseas or something and they would not have a lot of interest about whether the lights stayed on in Tasmania or not. So from a community perspective, and here I guess I am talking about the fact that Aurora is also the retailer, Aurora is very focused on ensuring that we deliver electricity supplies safely and securely to our Tasmanian customers.

The power station is quite an important part of Aurora's portfolio. It provides risk mitigation in a financial sense because of the hedges that Mike referred to, but it does mean that we have some control over the end-to-end generation from generation through wholesale to the customers. But at the end of the day it is there for drought security so that if it does not rain in Tasmania, as

long as the gas flows through the gas pipeline the lights stay on. That is really our fundamental charter.

Mr WILKINSON - I hear what you say. It is always a difficult area when you look at State-owned companies and government business enterprises but it is a bit different from what we were told when the legislation came before us previously.

Dr DAVIS - I am expressing the view as the Chief Executive of Aurora, having been given the task of making this thing work. I guess what I am saying to the committee is, we are making it work and it is fulfilling its objective in terms of providing security, and if we can play the debt down maybe the Government will have another look at it in a few years.

Mr GREEN - They are decisions to be made. Look at it within five years; we did not say we are going to sell it in five years.

Dr GOODWIN - It depends on whether there is a buyer or not. You cannot sell if there is not a buyer.

Mr GREEN - Which is a very good point, and which means that we would want to maximise any returns to the State as a result of a sale, we would not -

Ms FORREST - You do not want a fire sale.

Mr GREEN - You are not putting your arm up to sell it, are you?

Ms FORREST - No, I am asking you the question, asking you what the position is. When the legislation came to approve the sale that was what was said: with a view to selling it into the future.

CHAIR - That is right.

Mr GREEN - A view to selling it in the future. I was asked whether it was up for sale now.

Mr HARRISS - There is a really clear message coming from the chief executive, and that is that the business would really appreciate some equity contribution because of that debt to equity problem that you have. It is a problem. I would have thought there was no question about that, given the capitalisation.

Dr DAVIS - I think all businesses would like to have more equity because they are interested in paying less money to the lender and having more money for the shareholder. There is a review of the balance sheet structures of the energy businesses underway as we understand it and Aurora is contributing to that. We will get advice and the Government will get advice from independent experts in this field as to what is an appropriate debt ratio. What I can say though, Paul, is that Aurora operates one bank account. We have one balance sheet, one profit and loss and we can identify the debt associated with the Tamar Valley Power Station. We have a subsidiary, but we also have a distribution business that is heading towards \$2 billion worth of assets, which in fact if it was privately owned could probably sustain more debt. So we have a lower leverage on the distribution side and a higher leverage on the power station side, all money washes out into the one bank account so it ends up -

Mr HARRISS - The other way round, higher leverage on your distribution.

[10.00 a.m.]

Dr DAVIS - No, we have low leverage on the distribution, meaning we have less debt in distribution than we could comfortably service, and on the power station we have high leverage, meaning we have more debt than we would prefer, but because we have one balance sheet when Darren, the group's chief financial officer, looks at it Aurora's debt is fine. Is that right, Darren?

Mr SMITH - At the overall group level we have strong financial management objectives and target a strong investment rate. We would like a bit of equity but we can service it. Optimal capital structures is what we need to aim for. Can we service the debt? Yes, we can, but certainly we would not want to see our ratings slipping.

Mr HARRISS - You can service the debt based on the Energy Regulator, but before the latest decision by the Energy Regulator you would not have been able to?

Mr SMITH - We are looking at fairly strong records of debt serviceability. If the 2009-10 result occurred each year in perpetuity, that would have caused problems, but clearly the debt servicing outlook is on a sustainable footing.

Mr HARRISS - Mr Chairman, that just leads me to one other question regarding the Tamar Valley Power Station and mentioned by Peter. You have one set of accounts but you can identify the two different components of your business. Why, then, would you not, transparently, split them?

Ms FORREST - Segment reporting.

Mr HARRISS - Tasrail does, as Ruth said, segment reporting. I know the standards allow you to do what you are doing, but why would you not go another track?

Dr DAVIS - We do have accounts for the power station because it has own subsidiary company, AETV, with its own board, and so a set of accounts are produced for the power station but they are rolled up into the Aurora accounts. There is no issue about hiding them, it is just that we aggregate them at the top. I am not sure if there is any other answer to that.

Mr SMITH - If I could also add that one of the things is you find the distribution business, which is a substantial chunk of the Aurora business, actually has one customer - well it does have more than one customer but materially it sells its product to the retail business, which is one of the reasons that it is very hard to disaggregate.

Mr HASKER - Paul, what would you see achieved if we did something else?

Mr HARRISS - I really do not know, John. We are looking at Tasrail later in the day and in our study of their situation we became aware that they segment report, which I believe leads to a higher level of accountability, and makes it easier for us mugs around here, year in year out, to more readily identify just where the hot spots are. Clearly the Tamar Valley Power Station is one of your real hot spots.

Ms FORREST - On that particular point, firstly you have the retail, the generation and you have easy key. There may be others that you would identify in that segment reporting. The

Auditor-General would prefer, I believe, segment reporting. He has made comments to other GBEs along the same lines, not just in relation to Aurora. It would help anyone understand how retail is going, and that includes the average punter who is paying their power bill. Generation obviously, as Paul has alluded to, but also easy key. I did hear some media coverage the other day about the potential benefit of that company to Aurora's business. Would it not be helpful to have those separate within the account to make it clearer about where things are going in the various parts of the business?

Dr DAVIS - I think it is a good point. I should assure the committee that at a management level admittedly the management accounts are not audited but on a monthly basis we look at the performance of each of the elements of the business, so whether it is easy key or the telco business or the distribution, or what we call the energy business, which includes the power station, at a management level we do review that. Once you go to the level of externally audited accounts, it is quite a complex and detailed process, but perhaps it is something we could think about -

Ms FORREST - I think it would help everybody; us on this side of the table, as well as the other stakeholders in the community.

Dr DAVIS - It is a very interesting question, Ruth, because if you look at some of our competitors, for example Origin Energy, which has upstream gas, it has retail, it has power stations, it has wind farms, there is no transparency of where they make their money, and we do operate in a competitive market, so that is another factor we must keep in mind. I accept the need for scrutiny and the need for the Tasmanian people to understand how we are going, but we have to be aware that if segment recording revealed the margins we are making in one customer group compared with another customer group then that is an invitation for a competitor to target that because they know our margins. I accept the point you are making.

Ms FORREST - You are talking about segment recording within the segment. I am talking about broader segment reporting.

Dr DAVIS - It is a good point.

Mr HASKER - It is a tricky issue. I think that if the world knows the potential of this then it will draw a lot of -

Ms FORREST - It could be to the benefit of the business; that is my point as well.

Mr HASKER - Well, yes, if there is a potential sale, but in the case of - and the Auditor-General does sign off on the AETV accounts -

Ms FORREST - Oh yes.

Mr HASKER - So the scrutiny on behalf of the shareholders, in a sense, is conducted by the Auditor-General.

Mr HARRISS - Following up on Peter's contribution that the management group has monthly assessments. My question then goes to the minister. How often, Minister, would you expect the board, after a process like this, to alert you, as the shareholder minister, to issues related to the company?

Mr GREEN - Are you referring to the latest Auditor-General's report?

Mr HARRISS - No, it is just a general question. You are the minister. We asked you some questions during budget Estimates earlier this year and this was an emerging issue. It is all about accountability and your expectation of the various State-owned companies or government businesses that you are accountable for, specifically this one.

Mr GREEN - Well, the CEO and the chair meet with me after each board meeting.

Ms FORREST - How often are the board meetings?

Mr HASKER - Once a month.

Ms FORREST - So you would have those figures that you referred to in your previous answer and you would see them monthly?

Mr GREEN - Yes.

Ms FORREST - Which breaks down the segments.

Dr DAVIS - No, we do not go into that level of detail because the management team meets twice a month for half a day to go through these numbers. The board then meets once a month for a whole day to go through these numbers and deal with strategic issues and then we brief the minister. The minister's time is valuable so what we do is try to ensure that the key issues are brought to the minister's attention in any areas where we are not tracking in accordance with the approved budget or corporate plan.

CHAIR - Minister, while we are on matters financial, did Aurora seek any financial support from the State Government at any time during this last year and, a subsequent question to that, has Aurora prepared any submission or documentation canvassing the option of seeking further financial support from the Government?

Mr GREEN - With respect to the equity injection?

CHAIR - Yes, exactly.

Mr GREEN - Well, there was obviously a range of discussions into how we manage the issues associated with the Tamar Valley Power Station early on, but there was no formal submission that I am aware of regarding an equity injection.

CHAIR - So even though there might not have been a formal submission, the issue was canvassed.

Mr GREEN - We talked about a range of issues on how to get Tamar Valley power onto an even playing field.

Mr SMITH - As part of the lodgement to the final corporate plan it was, as Peter Davis mentioned earlier, part of the overall review of the company structures. So that was a good

avenue for us to have our input because that review is ongoing in any event. That is how we obviously contributed to that review.

CHAIR - A subsequent question to that is, when did you become aware Aurora was not going to make its profit target of \$26.6 million? Can you recall when that arose?

Mr SMITH - Through the year of 2009-10. It was an evolving thing that really happened in quarter one 2010 as we were putting a corporate plan together. By the time, we were at December 2009, we were pretty well on budget and it was the market events that unfolded at that point as we put in the corporate plan.

CHAIR - So in December 2009 you were on budget?

Mr SMITH - Yes, I do not recall exactly but I believe we were pretty close to budget.

CHAIR - Then when did you become aware that there would be a loss?

Mr SMITH - It then became evolutionised, as Mike Brewster was saying. As the CCGT came on and began operating in the market, the true nature of the market became apparent. It culminated in our lodgement of our corporate plan in March which showed the outlook as not being particularly positive if we did not get a longer-term deal in place.

Mr WILKINSON - It seems as though there was a sledgehammer on your head at that time though, doesn't it? That is, the thing that I am finding it hard to understand is that there was this debt that you have spoken about and there is this sudden change. But from all we are hearing, that was not known and that is what scares me a bit. If that is the case, until, as you say, the first quarter of this year when, bang, here we go with this debt. That scares me and that is what I am saying, what have you put in place for that not to occur again?

Mr SMITH - It was certainly known that the debt on the power station was going to happen at \$260 million. So the debt was always known and it was always a consideration for us looking forward. We knew the debt levels of the power station because we knew the construction costs. The actual market events transpired after the CCGT became operational and we saw how the market events unfolded which was outside any prior norms, as Mike Brewster mentioned earlier. So there are really two parts to it.

Mr WILKINSON - It has happened once. My suggestion would be that if it has happened once and there are no safeguards put in place, it could well happen again. What safeguards have been put in place, if there can be, for it not to occur again?

Mr DAVIS - One of the first safeguards is that we are no longer building a power station. So there were issues that arose, as Mike Brewster indicated, with the power station being incomplete at the time and unable to, therefore, cover the customer load. So we found ourselves exposed to the market. That will not happen again. We are not planning to build another power station in the foreseeable future.

Mr WILKINSON - But you would have budgeted for that, would you not because it came in under budget, as I understand?

Dr DAVIS - No, because the capital cost and debt is all known and that was all very well handled and \$25 million under budget. Construction of the asset was not an issue. It was the performance of the asset in the market, particularly as it did not all come online on one day. There are, in fact, six separate turbines at the power station. The first little group to be commissioned were the FT8s. So we have 120 megawatts of FT8s. They come online first. Then we have the Rolls Royce open cycle gas turbine which is 60 megawatts that came online and finally, the big, main frame plant which is the Mitsubishi combined cycle plant. That is 203 megawatts. They were coming on incrementally at the same time the market was hopping around. So the way that we have handled that, Jim, is through the very conservative hedge arrangements that Mike Brewster referred to. That it not going to happen again. The power station is built. We understand its operating costs. We have good, long-term maintenance arrangements in place and we have good hedge cover from Hydro Tasmania for the periods when the station is out of service.

[10.15 a.m.]

Dr GOODWIN - I wanted to pick up on the Chairman's question about this need for an equity injection and I am looking at the Auditor-General's report on the 5 per cent cap issue. It says in his report that in December 2009, the Chairman wrote to the shareholder minister outlining his concerns. I am just wondering whether, in that letter, the Chairman mentioned the need for an equity injection? I just ask that question because it states in the report, in the context of this on page 20, that the Chairman also believed the company needed an equity injection of between \$150 million to \$200 million accompanied by improved electricity market arrangements. I am not sure whether that was actually in the letter or not. It is not completely clear.

Mr HASKER - Vanessa, I do not have the letter with me.

Mr GREEN - That was before my time.

Dr GOODWIN - Is it possible to get a copy of the letter?

Mr SMITH - I think from recollection, as I said before, we knew that the debt was not the level of debt that you would normally have in a power station if you were building on a greenfield site. So we clearly said, in order to get it to a normal 30:70 ratio or 40:60, I am sure that there would have been reference at some point in an isolated case, not about the overall group picture, that this power station probably had more debt than we would normally like. But then, as we move through into 2010, we have the input into the Government's own review. We have been happy to participate in that. About \$100 million of debt would be something more reasonable in a commercial sense. It would not be out of the question, although I do not recall the actual number.

Ms FORREST - Is it fair to say the only reason you were allowed to take on that level of debt was the letter of comfort that the Treasurer issued to Tascorp?

Mr SMITH - When you come up to the group level again because Aurora owns AETV, the level of debt is sustainable but if you look at what you would like in terms of debt to keep the strong investment rating then there would be need for an equity injection.

Ms FORREST - Then why the need for a letter of comfort?

Mr SMITH - Now you are actually down at the AETV. It is a separate legal entity.

Ms FORREST - Hence the need.

Mr SMITH - Yes. We have the legal entities treated separately, with separate boards. There is a separate need to treat AETV in its own legal entity side as well.

Ms FORREST - So the letter of comfort related to AETV not to Aurora?

Mr SMITH - Back in December 2009 I think so. I just need to double-check that.

Mr HARRISS - I want to pursue that question of Vanessa's as to whether that letter could be provided to the committee. The Auditor-General mentions parts of it so the Auditor-General has seen the letter I presume. That may provide some comfort in terms of exactly where the business was tracking.

Mr GREEN - I do not know. I am not sure.

Dr DAVIS - Maybe if we could review the correspondence. It is in the past, just to make sure that there is nothing that is commercially inappropriate.

CHAIR - Okay, so you are going to review that. It may well be that the committee decide to write formally to you anyway to request that information.

Mr HARRISS - Still on that thread. Darren, you indicated that in December you were on track with budget.

Mr SMITH - Yes, that is right, materially.

Mr HARRISS - Is it true to say that your December quarterly year-to-date reality of earnings before interest and tax was -\$12.6 million, which is a fair measure of expected profit, is it not?

Mr SMITH - Without the actual information in front of me I would prefer to be providing a copy of the information.

Mr HARRISS - that December quarterly report -

Mr SMITH - To Treasury?

Mr HARRISS - No, your own.

Mr SMITH - The quarterly report that we do is to Treasury.

Mr HARRISS - 4.1 and 8.5 or 4.5 and 8.1 in the first two quarters?

Mr SMITH - Yes.

Mr HARRISS - Leave it?

Mr SMITH - Yes.

Mr HARRISS - Then -\$12.6 million. How then are you tracking on budget for profit?

Mr SMITH - That would have been the budget.

Mr HARRISS - My understanding from the papers that I have looked at was that it was \$12.6 million under budget.

Mr SMITH - You also have to be careful of mark to market because mark to market is quite volatile and it is very often blacked out depending on which particular line item of profit you are looking at. I would need to look at the actual numbers. We worked relatively close to budget. You have to be careful of the mark-to-market aspect and it did go south in the new year.

Dr DAVIS - The line of questioning that Mr Harris is taking is very much the same line of questioning that the Auditor-General took. We were required to provide detailed briefings to the Auditor-General on what our financial position was in the December quarter and then how it deteriorated by the time we did our corporate plan in March. So those numbers have been provided in great detail to the Auditor-General and he has written his public report.

Mr HARRISS - In either that report or indeed his larger assessment of all GBEs and SOCs he used the terminology 'there should have been some red traffic signals at that point in time'. Is my recollection of that correct? Is that the sort of terminology the Auditor-General used?

Mr GREEN - In the quarterly reporting effectively that is how it is reported - red and green lights and goodness knows what.

Dr DAVIS - If Mr Harriss would like a more detailed answer on this, our general manager, Strategy and Corporate Affairs, dealt directly with the Auditor-General and he has the numbers probably more on the top of his head than the rest of us, so I could ask Mr Inglis to join us and respond to that question.

Mr GREEN - Can he explain mark-to-market?

Dr DAVIS - He could try.

Mr HASKER - Which are big numbers and completely transform your bottom line.

Dr DAVIS - The mark-to-market, at a very superficial level and from a non-accountant, is looking at the value of your hedge book and imagining if you were to sell it what you would get for it, so whether you are in the money or out of it, but clearly you are not going to sell your hedge book so it is a bit of a hypothetical accounting trend. It goes through the profit so it is a bit confusing. As Darren said, the more important issue is the commercial numbers and how we are tracking the budget, and I think that is the red traffic light, green traffic light thing that you were asking about.

Mr INGLIS - I think the key thing was that the report from the Auditor-General had information from Aurora and Treasury that has been provided to the minister and the Treasurer. We are not party to some of the advice that Treasury provides to the Treasurer and I believe the references to red traffic lights and those sorts of things were in relation to those briefings that were provided to the Treasurer, so I am not able to comment on what the traffic lights were. I do not have all the numbers in my head but what the Auditor-General did show was a chart showing our profit before tax. Again, that has some mark-to-market issues in there so it moves the

numbers around a bit. In the first half of the financial year there were some monthly ups and downs, but in terms of an operating earnings level they were broadly tracking. There were no significant trends going one way or the other. You can see from the chart on page 19 that our profit was strong. It was going into 2010 that the earnings showed a trend of a decline, for the reasons that Mike Brewster and Darren Smith talked about.

Mr HARRISS - I go back to that study of the December quarterly report that I have done, and did in preparation for this process, showing that your operating EBIT was accumulated over the two quarters negative 12.6, as against budget - not just a nebulous figure; it was as against budget. Budget in one column, actual in the other. That indicates clearly to me - and correct me if I am wrong - some difficulty or problems confronting the business. That is against your own budget, 12.6 negative in two quarters. How was the business going to come out of that? I have had a look at the graph in the Auditor-General's Report, so what went so dramatically wrong at that point in time, from December to March, with the smash?

Mr INGLIS - Two things. Firstly, in terms of the quarterly report - and those numbers do not sound familiar - on a month-to-month basis in 2009 there were ups and downs. We had some major storms in September 2009 and that led to some major increases in costs for part of the business. There were things that contributed to the different costs to the business. In another month there was a change in customer load that was either above or below budget - if it is warmer or colder the change in consumption of energy by customers has an impact - so there were pluses and minuses. Certainly for the whole of the business the figure you mention does not ring a bell in terms of the overall earnings result for the business as at December. I would have to go back and check the report you are referring to.

Dr DAVIS - In terms of the answer to your question about why it fell off the cliff in March, would you like some further elaboration on that?

Mr HARRISS - Please.

Dr DAVIS - I will get Mike Brewster to come back because he was the man in charge of the hedge.

Mr BREWSTER - Up until 31 December we had a certain hedge position with Hydro. That hedge position changed. We became very long in the market and spot prices dropped significantly and when spot prices drop significantly you are a long way from recovering your cost. It was very difficult prior to 31 December to anticipate what the impact of that would be and we were working assiduously to do that but you have to remember that we have a value chain that starts right with gas and works all the way through to the retail price. It is quite complex and there are a lot of assumptions in that.

When that changed we were not sure where the spot price would be. We did a lot of modelling to see where the spot price would go and the spot price went a lot lower than we expected because we were long, and it evolved over time, it progressively got worse as time went on. That hedge deal was struck when we had the Alinta deal so this was all about the original Alinta deal which would not have been an issue for us but when you got the power station all of a sudden you have all of these running costs of the power station with no means of recovering it. Under the hedge deal we would have been protected.

Fundamentally, that is what happened. We were working through how bad is this going to be, what is the impact of it and it took an extensive period of time to get through the modelling, and we had externals come in to help us with that modelling. That is what happened and the new deal that we have negotiated, along with other things, corrected it so that we do not find ourselves so long ever again but it was a decision that was rightly made long before the purchase of the power station, put simply.

Ms FORREST - A risky business.

Mr BREWSTER - Of course, but energy markets are a risky business. They are complex businesses and that is why most businesses go for a full value chain and go right up to the gas end to try to protect themselves in all segments of the value chain.

Ms FORREST - Some of that risk has now been mitigated, though, that is what you are saying.

Mr BREWSTER - The majority, and that is why we are now ahead of budget. Whether that is sustained until the end of the year I do not know but it looks pretty good. At the moment we are ahead but it is primarily because we addressed it.

Ms FORREST - How much exposure have you to the spot market now then?

Mr BREWSTER - We would have virtually zero at the moment. When you take a hedge you have to make an estimate of what your customer load is going to be every five minutes. If the demand is greater than that and you have not sufficient coverage and all of a sudden it is a really cold day and this happens and there is a lot of what is called flex so the demand goes up significantly, you could find yourself in a position where you are exposed for that excess energy to the spot market and, as I say, this occurs every five minutes.

When that occurs in Tasmania there are no other players so the other competitor - depending on Basslink, et cetera - largely can determine if they are on import what they want the spot price to be.

Ms FORREST - The competitor being Hydro?

Mr BREWSTER - The other competitor being Hydro.

Ms FORREST - I come back to that point that you continue to be vulnerable because of that arrangement with Hydro being your competitor. Here you are as a generator competing with the big boy in town, who is Hydro, in a risky business.

Mr BREWSTER - I agree, Ruth, but the difference is that we have chosen this year to take a very conservative hedge position to counter that and if we were on the mainland we would take a much less conservative hedge position.

Ms FORREST - Because there is much more competition?

Mr BREWSTER - Yes, and having done that, we are meeting budget and we are providing a return from the energy business.

Mr GREEN - And we are providing energy.

Ms FORREST - What you are saying, though, is if there was more competition in Tasmania there would be more options and you would not have to take such a conservative hedge.

Mr BREWSTER - Sure, but there are other downsides to that as well that need to be looked at. All the arguments have gone on as to should we put it all back together, should we create more businesses. It is a complex answer and I think that is why the Government has established the inquiry, I would have thought, to answer that question.

Mr HASKER - So that there will be a better playing field for all the parties.

Mr GREEN - We had PricewaterhouseCoopers looking at it prior to that which will form part of it. Obviously we have known there has been an issue with respect to the disaggregation and how competition works and the size of our market and all those other things.

Ms FORREST - It has been going on for quite a few years.

Mr GREEN - But in the meantime we have Basslink, we are part of the National Electricity Market which has been extremely complex. We have gas to the State and there is competition from that point of view. We have made progress but we are an island State and we all know that.

[10.30 a.m.]

Mr BREWSTER - I think to be fair, Minister, you have to understand that you do not really know what is going to happen until you bring competition in. Competition only came in the last year. Some very smart people on the mainland give analysis on what the spot price would be in Tasmania. I received all of that and I can tell you that every one of them got it substantially wrong.

Ms FORREST - It is a bit like predicting the GFC, really, isn't it?

Mr BREWSTER - That is the reality of life.

Dr GOODWIN - There has been quite a lot of discussion about the financial difficulties emerging from the corporate planning process and everything becoming much clearer as part of that process. What is the timing of all this? These issues that you talk about with the Tamar Valley Power Station and the modelling and that taking a long period of time - did these also feed into the corporate planning process and are they part of the reason why everything started to emerge at that point of the picture?

Mr BREWSTER - Well, that's right. It was an emerging issue because you have to remember we had just commissioned the power station so we are dealing with that; we are dealing with the market changes, as Peter rightly said, when all of our equipment comes on line. So we are dealing with a change in the market behaviour and dealing with trying to predict the outcome of a significant future change in our hedge position; we are also trying to deal with the fact that the gas situation in Australia has changed significantly in the last 12 months where there is an oversupply of gas, and because we are in the gas market, we are having to manage what the impact of that is going to be on our value chain. So it is not a simple one-step answer. You learn a bit, you test it, you prove it, you see what happens in the market. Ultimately, you choose a position. We chose a position which is: we have to take a conservative position, have the

wholesale arrangement with Hydro renewed in a way that we can provide a sensible commercial return to the shareholder, and that is what ultimately happened.

Dr GOODWIN - Was there anything else that emerged through the corporate planning process, any other issues that became much clearer as a result of that or is the power station the main problem?

Mr HASKER - I think to take it back and perhaps I should have answered Jim earlier, bear in mind the Premier only opened the power station in October so that is well into the financial year that we are scrutinising. There were a number of pieces of kit and particularly the Pratt & Whitney turbines were sent back to Seattle to be brought up to date and so on; one by one it took a long time for them to come in and be reinstalled and commissioned so this is very modern history. We were new players on the block. Bear in mind, the power station was opened, and it may not have even been fully completed, in October, which is very recent.

Dr GOODWIN - So it all comes back to the power station, it would seem.

Mr HASKER - Yes, and its implications on the market and the additional debt that the corporation took on. Put them all in the pot together, Vanessa, and that is the scene.

Dr GOODWIN - Do you think there was anything more that could have been done in terms of due diligence with the purchase of the power station that might have put you in a better position, or did you really do everything that you could; you just could not anticipate any more?

Mr BREWSTER - I was there in the negotiations and I think we did pretty much what we could. There was a very fast track due diligence for good reason. No-one was going to finance the power station; Babcock & Brown were in a position where it would have been shut down so the choice was we either buy it and buy it now or it is shut down and we don't have that energy security. We must remember, as I said, at that point in time we were in the midst of a drought. So a hard call had to be made. Of course we would have liked more time for more due diligence. It would not have changed the outcome in terms of the power station. I think the outcome in terms of the power station -

Mr GREEN - The price was at a discount.

Mr BREWSTER - It was at a discount; it worked out on budget and it was right. The issues with the market: maybe if you did a truckload more of analysis, you might have got a better guess at what that would be but I would add that at that time I had a report from IES that told me what I should expect the spot price to be and I can assure you, it was a long way out. I can understand why but at that point that is where we were.

Mr WILKINSON - Just before breaking for a cup of tea, talking about the debt and getting back to the debt level, I understand the major reason for the debt level to increase and its increase of 103.79 per cent from 2007 through to 2010, from \$505 million to \$1.029 billion, according to the Auditor-General's report. The Auditor-General further notes that there seems little doubt that its debt will increase. Do you accept that your debt is going to increase? If so, by how much? When will that debt peak? I think those three questions will be a starting point.

Mr HASKER - We will get our Chief Financial Officer back. I think Dr Davis made a statement in clarity about our business in saying that we invested \$145 million in the network in

advance of anyone paying us for it and that will then pay us back over the life of 40 or 50 years. So we are investors and, by definition, we have to go and borrow that money and that goes on. Plus, we had the additional quarter of a billion dollars through the power stations.

Darren, will you answer Mr Wilkinson's question on your estimate of debt going forward?

Mr SMITH - I think it is reflected at 30 June that about 60 to 70 per cent of the debt is associated with our distribution business at the group level and that is where we have various internal debates about good debt and bad debt and of course this debt does earn stable regulated return which, as Peter Davis has mentioned, if it were a separate business, could sustain high levels of debt. The rest of it is from the energy business which is the billing of power station, the billing system that has been built, and obviously some of the difficulties of 2009-10. That is how the debt stands today.

The debt in the future is not for the energy business, the only debt that we are forecasting to increase to fund the distribution capex program of work on which we do earn a regulated return. So there is no forecast expansion of debt with the energy business.

Mr WILKINSON - In relation to the debt that you have just spoken about though, when is that going to peak, do you believe?

Mr SMITH - We do a five-year planning process at the moment. It is likely to rise somewhere between \$200 million and \$300 million over the five-year period. But we are doing everything we can to make the business more efficient to reduce that. So I would say it will be probably more in the \$200 million to \$250 million range over the five years on the capital program of work because we are still dealing with the bow wave of expenditure on the network.

Ms FORREST - Are you talking about the poles and wires?

Mr SMITH - Yes, the distribution business; it is not an energy business debt.

Ms FORREST - No. So there was \$145 million spent in the last 12 months on power poles and wires?

Mr SMITH - Yes.

Ms FORREST - So how much are you forecasting for the next 12 months?

Mr SMITH - It will be, on average, probably circa \$150 million per annum and then there are obviously some other parts of capex that go with that, general programs, IT in respect to those kinds of programs. But the distribution of poles and wires will be about \$150 million.

Dr DAVIS - We should recognise that the current capital expenditure is in accordance with the approved pricing determination that the regulator approved for the five-year period and in that he approved \$588 million worth of expenditure on the distribution network over five years. So we have a line of expenditure that is approved that is forecast in the tariffs and what that does is to allow us to improve the capacity, reliability and safety of the network and that is subject to the regulatory scrutiny. So that takes us through to the end of next year. Then of course we have to put in a submission for the next five-year period from 2012 to 2017 and that regulatory determination will be made by the Australian Energy Regulator. So we are going into the national

regulatory framework and we will need to put up a submission that outlines how we plan to invest in the network to deliver customer needs and the Regulator will make a determination as to what he will allow us to spend, what is prudent and that will then inform the debt levels that we might need to go forward. But, again, these are investments. We build infrastructure, it is paid for over 30 years, so it has a rental return.

Mr GREEN - Can I make a point, Mr Chairman, in context, you talk about it a lot and you say it quickly, the capital expenditure and then obviously there is the maintenance associated with running all those poles and wires, 22 000 kilometres of wire - from Sydney to London, effectively - around the State of Tasmania and 220 000 poles in the ground and 30 000 other poles, substation type of arrangements around the State. It is an amazing network. It is such a small State and it is important that we expend that money.

Ms FORREST - Through you, Mr Chairman, the point is that the next price determination to be done by the AER will effectively, no doubt, recommend a price rise and that will be mainly related to the capital expenditure on the poles and wires, the distribution network. Is that the expectation here? So when people get their notification from the AER that there is another power price rise on the way, will that be what it relates to?

Dr DAVIS - Yes, it is purely in relation to the regulated network, that is, poles and wires, transformers and all the things the minister referred to. The regulator looks at both capex, which is capital new spend, and also opex, which is operating spend to maintain the network. I would not like to predict what the AER will determine because there is no doubt that customer price rises are a problem right around the country, including Tasmania. It is not our desire to contribute to further price rises. However, the infrastructure is being built because of customer demands. I mentioned that we spent \$45 million last year on customer-generated work. This is where customers turn up and say, 'I want to construct a new shopping centre near the airport and I need electricity'. As the monopoly supplier of electricity, we cannot say, 'We are a bit short on cash, go away. You can't be joined to the Tasmanian network'. There are demands and pressures on us from customers. What we will do with the AER is put in a submission to try to minimise those price rises while maintaining the key performance indicators of safety, reliability and capacity. There is no doubt that we will be put through the wringer because the regulators right around the country know that customers have had enough of price rises. Price rises have occurred because of the cost of building infrastructure, but are there smarter ways or more efficient ways to build and maintain the network? Perhaps after morning tea we could talk about that because we have a new General Manager, Network, who has recently joined the company. His name is Andre Botha. Andre has joined the company largely to help us with this next phase where involving the customer more through smart grid and distributed generation will hopefully allow us to minimise those price rises.

CHAIR - With respect, there are always demands for new infrastructure to be built and that has been happening for decades. Why has it suddenly compounded now? Is it because you have not kept up your infrastructure upgrades?

Mr GREEN - We had a regulated market here previously and the regulator determined where you could spend the funds. We had significant frustration regarding, say, Strahan, which is struggling to gain a decent power supply. The regulator would not, under the rules, allow that power line to be upgraded when work needed to be done in Hobart, where there was a greater population. There were always issues around where you could spend the money on the network and that is how it has always been.

Ms FORREST - Does that come down to how it is sold, though? The company puts its case to the regulator and the regulator says, 'No, forget Strahan, let's fix Hobart' -

Mr GREEN - There was a time when we were spending well over our own balance sheet to upgrade infrastructure - this is under the old scenario with the Tasmanian regulator.

CHAIR - What I am saying is, are we trying to catch up now? That appears to be the case. It is catch-up now and therefore the consumers are going to pay for it.

Dr DAVIS - If you go back a decade, in Queensland there were stories about Energex in the *Courier Mail* every day because the storms were coming across the Gold Coast and the power was going off and staying off for a week. Energex then put a submission to the regulator saying, 'We need to spend more on capital' - and it has happened right around the country. Is it a catch-up? Well, it tends to go in cycles. I think what is happening now is people are saying, 'Electricity is too expensive, let's not spend so much on electricity'. The risk is that if prudent managers of the assets such as ourselves do not invest enough and then in five years' time the lights start going out people will say, 'We had a barbecue last night and the lights went out' or 'Our factory couldn't operate'. It is an essential service and we must deliver it. It is a catch-up and it goes through cycles. I think there are additional pressures at the moment, such as dealing with the environmental issues. There are higher standards of diligence and higher standards of safety. I have been looking at some numbers, during the year there were lots of questions about why everything had gone up so much. The customer-generated work over the past seven years has gone up by 300 per cent, so that is how much the network has grown. Aurora does not go out and build things just for the fun of it, we go out to build things because customers demand it. We try to do it as efficiently and cost-effectively as possible and there is a regulator to make sure we do that.

The committee suspended from 10.45 a.m. to 10.55 a.m.

CHAIR - We will now resume. We have only an hour to go and we have some financials to finish off and then there are quite a few other operational questions no doubt members will want to ask.

In general terms, are you confident that Aurora will return to a profit and that dividends will be paid to the Government over the next few years? Is that the case? Can you unequivocally say that is going to be the case?

Mr GREEN - Certainly the quarterly report so far is indicating just that.

Mr HASKER - The board, at the November meeting a week ago, reviewed the accounts up until the end of October and I have to say the results were very strong, but I know that tough times are ahead. We are not expecting the accelerated start to be maintained but at this stage we are very confident.

CHAIR - What are the future projections for the next four or five years?

Mr HASKER - They were reflected in our corporate plan, which I know was done a while ago now.

CHAIR - Yes, it was.

Mr SMITH - With the new deal in place from 1 July there is a very stable pattern for the five years so, as Peter has mentioned, there is a return to a stable financial outlook. Of course with the level of dividends, there is a new policy being released to be looked at for entities owned by the Government and whether this moving is continued into the future and what happens with equity, which is a big capital structure piece. Could we pay if we stayed on the same footing? Yes, we could, but then you have to address dividends each year under the corporate law requirements and also in the context of the available capital structure.

Mr HASKER - Chair, looking at five years out I do have to say - and I guess it was Ruth's question - that the Hydro deal is three years, so it does come pretty much in the middle of where we are looking.

Ms FORREST - We now have some regulations to use a bit of pressure, though, if they do not play the game so well.

Mr WILKINSON - We have heard accounts that Rio, big businesses, pay less for their energy than your normal consumer. How is Transend's deal going with Hydro in relation to that? Are you happy with the agreement that you have reached with Hydro?

Mr HASKER - Yes.

Mr WILKINSON - You are.

Mr HASKER - Yes. Perhaps the minister who sits looking at both might like to comment.

Mr GREEN - Well, there is a wall there between them.

Mr WILKINSON - Between whom?

Mr GREEN - Between Hydro, Aurora and Transend. I am the minister for each and every one of them and of course if you were asking Hydro some of the questions that were asked today of Aurora there would be a different view in commercial terms.

Mr WILKINSON - Put your Aurora hat on for this question.

Mr GREEN - I was very pleased that they were able to negotiate a sensible outcome that stood them both in good stead.

Mr WILKINSON - Was that a long drawn-out negotiation?

Mr GREEN - I do not think it was that drawn-out. To get the parties together in the first place was an important step forward in the process and then once we had some parameters around the Government's expectations, the negotiations went pretty well after that, as I understand it.

Mr WILKINSON - Was it difficult to get Hydro to the table? Is that what you are saying?

Mr GREEN - There are two sides to every debate and -

Mr WILKINSON - It sounds like the answer is yes.

Mr GREEN - There are two sides to every debate and these are both proud and aggressive companies with respect to how they operate and, let us face it, there has been an enormous amount of scrutiny. I say to the member that there has been an enormous amount of scrutiny over the last little while with respect to both businesses - how they have operated within the market, the ACCC, the Auditor-General, a whole range of things have been audited - and effectively there is no case to answer. In the meantime we have been able, through regulatory pressure, to -

Ms FORREST - Using a big stick is the only way they got together, was it not?

Mr GREEN - We got them together, the negotiations took place and we have a favourable outcome that stands us in good stead. I think that is the best way of answering.

Mr WILKINSON - Were you disappointed, Minister, in the fact that, it would seem to me, it was difficult not on Aurora's part but on Hydro's part to get them to the table to discuss what is very much a State issue in recent times?

Mr GREEN - I think that the GBEs are charged with the responsibility of conducting themselves under that act and that is how they are conducting themselves. I have to be extremely careful, as you would well know, when intervening or trying to suggest things or whatever. The Treasurer and I looked at ways that we could, through legitimate means, ensure that the parties got together and negotiated an outcome, and that is exactly what we did with the support of Parliament.

Ms FORREST - Will those regulations persist into the next agreement in three years' time when that is being renegotiated?

Mr GREEN - I have no plans to change them.

Ms FORREST - So they will still be there?

Mr GREEN - As far as I am concerned they will be.

CHAIR - Jim, are you going to expand on that matter, I think, of bulk power consumers? I know that there are deals with Hydro in particular and that is another hat that the minister wears.

Mr WILKINSON - I do not want to step into commercial confidentiality -

CHAIR - No.

Mr GREEN - My answer would be straight up and down with respect that. They are conducting commercial negotiations and really it is outside the premise of this discussion.

CHAIR - Okay. Would you agree that small business, particularly in this State, is stymied quite a bit because of a lack of contestability, compared to, say, Victoria, where organisations can bargain with other providers?

Mr HASKER - That is a good question, Jim. I am certain Dr Davis is going to enjoy answering this.

Laughter.

Mr GREEN - He will say that we encourage full retail contestability.

Dr DAVIS - The reality is that we do have competition in this State for small business. The Government has announced progressive opening up of the market to competition. There have been four tranches of customers made contestable already. We have been dealing with Tranche 4 customers of which there are several thousand this year and on 1 July next year -

Mr GREEN - Farmers too.

Dr DAVIS - Yes, including farmers. On 1 July next year, we move to what is known as Tranche 5a, which is getting down to even smaller businesses; these are ones that use 150 megawatt hours per annum. Aurora needs to be in a position to offer a good service to those customers. There are four or five retailers active in the State competing with Aurora and a number of business customers have chosen to vote with their feet and go with the alternative retailer. This again brings me back to my earlier point that unnecessary negative media commentary about Aurora can see customers electing to switch to interstate retailers and that is money going out of the State.

CHAIR - If I, as a small business, take on another retailer and there is a power blackout or technical issues, who is responsible to sort that out?

Dr DAVIS - If there is a power blackout or technical issues that would be Aurora Network. You do not want competitors building duplicate poles and wires up the other side of the street and painting them a different colour so, basically, we have the regulated monopoly. We have the distribution network and we have to provide open access to that network for other retailers. So, Greg, if you chose to swap to a retailer based in Queensland, for instance, which you could do, then the electricity still has to get to your home or business through our wires, so in your bill you would find there would be a component for energy which comes from basically Hydro in the majority of them, there is a part of the bill for transmission because it has to get through the Transend network, there is a bit for distribution which is the Aurora part but you would actually be paying the retail part to someone else if you had chosen to turn away.

CHAIR - Okay.

Dr GOODWIN - To reduce your level of debt and to ensure that you can keep your poles and wires up to scratch, obviously it would seem power prices will have to keep going up. Do you have any idea of how much that will be in the short to long term or can you provide some sort of idea?

Dr DAVIS - Certainly in the short term I can indicate what the price rises are because they have already been advised publicly. The regulator has recently elected to try to avoid too much impact on Tasmanian customers by doing what he calls smoothing, which is basically putting revenues that Aurora could in theory get now, into future years. So the price rise that occurred on -

Mr WILKINSON - Sounds like a back-end contract in sport.

Dr DAVIS - It is about minimising the impact in one go, Jim. Prices went up by 8.8 per cent on 1 December and that was largely reflecting the costs of energy in the wholesale market and that was all approved by the regulator and then there is a further 8 per cent on 1 July next year and a further 8 per cent the following July. That completes all the price rises that we see in the next three years. After that, going out to 2012-17, you become part of that other process with the Australian Energy Regulator. As I have stated already to the committee, it is not Aurora's desire to see prices continue to go up. We are only part of the value chain. I cannot speak for the other parts of the value chain but certainly as we put our submission to the AER we will be trying to find smart ways to minimise the contribution that distribution expenditure makes to future price rises.

The reality is that Tasmanian customers are finding it difficult -

Dr GOODWIN - Absolutely.

Dr DAVIS - And we see that and we have generous concessions for a large number of customers. Clearly not everyone can benefit from those, so we need to try to make sure that we can stand a scrutiny inquiry like this and hold our heads up high and say we have done our absolute best to deliver power as cheaply as we can.

Mr GREEN - In new South Wales they are predicting 42 per cent over the next three years. I picked a headline up because I noticed it was about the Saints being bashed, but then I had a look and there was another issue on there with respect to power prices in Victoria, a \$150 shock to each household.

That revolves around CEOs and others taking great big bonuses and goodness knows what with respect to the privately owned power companies throughout Victoria. There is no doubt about it, there is a lot of pressure with respect to prices right around the country. We will understand to a far greater degree in the short term where Tasmania sits.

But that is no excuse for our not wanting to do it as cheaply as we possibly can based on the regulator and the panel of experts providing us with some advice with respect to some of those issues.

I think Tasmania in a national context is pretty well positioned overall.

Mr HASKER - Chair, following on from the minister's comments, I have some data here from the Victorian market. It is fairly current up to the end of September 2010. The Victorians have faced an increase over that 12 months of 20.3 per cent.

Dr GOODWIN - I want to ask a follow-up question which is related to your hardship policy. The Energy Ombudsman makes a comment in his annual report on page 15 that, in their experience, the hardship payment does not go very far in mitigating customers' debts to Aurora. I am just wondering if you are likely to revisit the whole issue of the hardship payment, given the anticipated increase in power prices, and whether you can flesh out how it works. Is it a set payment that is provided to a customer or is it on a case-by-case basis and will you be increasing the amount of hardship payments?

Mr GREEN - I think we put \$270 000 with the Salvation Army and other provisions exist. Anglicare and TasCOSS have put to us a position with respect to making energy affordable. It will be built into the whole cost of living analysis that we are having. They have suggested concessions and flat rate concessions, lifeline through tariffs and a range of other things, including retrofitting low-income houses to make them more energy efficient. From the government perspective we do want to make sure that we understand what we can do within reasonable parameters to provide the best social outcomes for low-income earners and people on fixed incomes in the face of rising power prices. But that in itself is complex, particularly when you want to start talking about issues associated with feed-in tariffs or more renewable energy. The costs associated with all that ends up coming to bear on someone. Often it comes to bear on the fixed-income earner.

[11.15 a.m.]

We talk about energy efficiency and all those other things, subsidies, even rent prices and a whole range of things. In the end somebody has to pay. It really is a balancing act but it is true that we have to make sure that we look at every opportunity to ensure that those less well-off in the community can survive through pretty tough times.

Dr DAVIS - The Government provides concessions, which are \$367 a year, to each pensioner and then there was an additional \$100 provided this year in recognition of the price rises. I understand there is about \$30 million that the Tasmanian Government provides in assistance. The Aurora hardship policy is on top of that, so we provide \$270 000. On page 39 of our annual report there is a graph that shows the amount and how it has increased. The company has made a commitment to continue to increase the hardship payment at least at CPI, so we are trying to match price rises. The way it is dispersed is that we are not experts on who is the most deserving so we provide that money to the Salvation Army. Then they act as the lead agency to distribute it through other community support groups. Often that is in the form of case-by-case electricity vouchers, or whatever, to help people who are really struggling. The other thing that Aurora does is that we established, and continue to support, the no-interest loan scheme. We are effectively working with a couple of banks. We provide the underwriting for no-interest loans so that people, who cannot normally get a line of credit, can go and buy an appliance such as a washing machine, a fridge or whatever and do not have to pay any interest. Again, that is a way of helping people in the most disadvantaged segments of our community to manage.

Ms FORREST - In regard to who pays and the cost that flows on to the customer, before the break you alluded to smart meter technology. Obviously if that is going to come in, someone will pay and surely that will be the customer? Where is that at?

Mr GREEN - There is even a cost associated with bringing competition to the market generally.

Dr DAVIS - I think it is a very important question because there is a lot of hype about smart grid and smart meters.

Ms FORREST - And particularly with the NBN rollout.

Dr DAVIS - Yes. Perhaps we could ask Andre Botha, the General Manager, Network, to come to the table because he has a very clear vision as to how we might be able to do this without

seeing customer prices go up. Perhaps, Andre, you could answer the question of how we might roll out smart meters and what would be in it for the customers?

Ms FORREST - At what cost?

Mr BOTHA - We have a very clear strategy for the distribution business going forward. As Peter alluded to, it is about keeping prices for customers as low as possible and not contributing to prices through the way we manage the network, the assets we deploy and the technology we use. A very key part of that is the rollout of a smaller grid, because the key benefits with a smaller grid are that it can help you to run your current assets harder. It also reduces the operational costs because you are running out sensors on the network as opposed to sending people, crews and trucks to look at things. The key thing there is that NB is an enabler for that so that is why it is a wonderful opportunity for Tasmania to do it now. We will only do it if it can help us with our vision not to contribute to price increases. The smart meter in itself, is more expensive than a traditional black meter. However, if you look at the parties that will pay for that, there is the retail component which is the cost of getting the consumption data back into the system. Currently we do it manually. We send people out, we estimate bills, we read only four times per year. There is a benefit that pays for part of the meter. From an asset-management perspective, you have another 240 000 eyes and ears on the network that can help you do things such as condition assessment, help with your fault response, once again optimising your cost to serve. There is another component that pays for it. At the end of the day, the total cost will not be for the customer because it will offset other costs that we currently have in the business.

Ms FORREST - So it will be cost-neutral? Are you saying it could be rolled out in a cost-neutral way?

Mr BOTHA - We will only do it if it contributes to our strategy of keeping prices for customers as low as possible. Our aspirational goal, as Peter alluded to earlier, is not to contribute to price increases from a network perspective.

Ms FORREST - So you will not be going to the regulator asking for an increase in price determination based on the fact that you want to put in smart meters?

Mr BOTHA - There are two components to that question that I would like to answer. In the first instance, we operate under the revenue cap which says that it's your regulated asset base times the work, which is the cost of capital, and that amount of revenue can be recovered from your customer base. To keep prices as low as possible we are not looking at increasing that. We cannot do it, otherwise prices will go up. So in the first instance, we are not going to the regulator to say, listen, we would like to run 300 000 smart meters across the network, it will add this capital cost to our current expenditure. So, therefore, you need to approve this funding because all that will happen is customers will pay out more. Within the constraints of our current spend and our accountability we are looking at keeping the lights on and delivering reasonable and appropriate customer service, and we are looking at funding it from that.

Mr WILKINSON - So, in short, there will be no added cost to the consumer -

Ms FORREST - Minimal, he said.

Dr DAVIS - Less than it would otherwise have been, Jim.

Mr WILKINSON - That is what I am trying to get at because -

Mr HARRISS - Keep it at 5 per cent if you can.

Mr WILKINSON - So the question is, why do you do it and you do it because it assists the business and you do not have to, I would imagine, have as many people going out to check the meters all the time and you get a more up-to-date idea of what the businesses are doing than you do when people are checking four times a year. Is that right?

Mr BOTHA - When we developed the strategy we were very conscious of the fact that 30 to 40 per cent of our customers get some help from the Government or from Aurora. That, therefore, puts the obligation on us as a network company which currently contributes to 30 per cent of the bill to keep that as low as possible and even reduce it in the future if we can. Then, on top of that you have, therefore, 60 to 70 per cent of customers who can afford to pay it and would like a choice and would like a lifestyle that fits the Tasmanian image. They would like electric vehicles and they would like the ability to take the load from day into night. To do that you need a smaller network. So it comes back to what customers need and we have used a proxy. In the first instance the power is as affordable as possible and in the second instance, choice, where customers want to exercise that. That is the only reason we will even consider rolling out a smart meter.

Ms FORREST - So if I wanted to build a new house next month and get a smart meter, can I do it?

Mr BOTHA - If you want a smart meter, yes, you can.

Ms FORREST - But it would not provide that feedback to me at this stage?

Mr BOTHA - No, because it is not rolled out yet. We can connect it -

Ms FORREST - I would want it in Smithton because I live in Smithton.

Mr BOTHA - Okay. If you are in Smithton and you have a connection to your house, in about nine months' time you can get a meter that will be able to connect to that.

Mr WILKINSON - They still have semaphore up there as well.

Mr BOTHA - I do need to reiterate that at the beginning of developing the implementation of the strategy, the pricing arrangements, the tariff signals, everything has to be developed. The technology issue is quite a small part of it. There are a lot of big developments happening at the technology end which make it really cost-effective now to roll it out. The NBN is a wonderful opportunity for us to do it. But, at the same time, you need the business, you need to take the customers with you and you need to educate the customers on what this means and those are the issues that we are working on right now. So it is at the start of the strategy but we are very clear on where we want to be, not to contribute to prices and to give customers choice.

Mr WILKINSON - It is not a bad time then, I suppose, to turn to the billing system and the blowout that has occurred on that. I do not want to be mean when I say it, but no doubt with the billing system, again, the same type of argument would have taken place as to why this billing

system is better than previously. But there has been a blowout of approximately \$50 million, I believe.

Mr GREEN - People have wanted to couch it in that way but I think the first thing to say is that the billing system itself effectively was ticked off by the regulator I think in 2007. It was accepted that there was a requirement for a new billing system, bearing in mind that the billing system effectively takes in the \$1 billion of revenue that Aurora brings in each year, which is under a complex of circumstances, bearing in mind that we have entered the National Electricity Market which puts a whole range of other layers over the billing system with respect to the openness of the system and how that operates overall.

I think that it is fair to say that the estimate in the first place was probably undershot.

Mr BOTHA - Optimistic.

Mr GREEN - Optimistic.

Mr WILKINSON - \$15 million.

Mr GREEN - It did not take into consideration the complexity of the parameters outside of that, particularly issues associated with NEM entry and other things that needed to be built -

Ms FORREST - Why not? Did it come up for tender? It should not be that unique; there are many energy entities around the country that would be using the billing system so why do we end up with this situation?

Mr GREEN - When external consultants looked at that they said that what we were doing was in fact in line with what it would actually cost. In terms of the underestimation, that has been explained to me, in terms of what their expectation was in the first place. But Dr Davis might want to build on it.

Dr DAVIS - I think the issue here is not so much that the billing system has blown out because we have now had advice to indicate that what we are spending on it is what you would expect to spend on a system of this complexity. The issue is that several years ago when we started the process we underestimated what it was going to cost.

Mr WILKINSON - Peter, you would have estimated what it would cost as a result of the best information you had at the time.

Dr DAVIS - That is right. Hindsight is a wonderful thing, Jim.

Mr WILKINSON - As a result of that it was \$15 million, as I understand it.

Dr DAVIS - It was never going to cost \$15 million; that is the reality.

Mr WILKINSON - Therefore the advice that you had was poor advice?

Dr DAVIS - The simplest analogy that I can refer to is that if you want to replace a piece of software you go and get a package. And our objective here was to get a package and not customise it too much. The cost of the package was \$15 million. The issue is that as you start to

interface it into all the other systems that it needs to talk to it has to be customised at the interfaces. In the case of the billing system that Aurora is building it has a very complex set of arrangements that have to respond to the National Electricity Market. There are some 36 individual systems and 70 interfaces. The original \$15 million was like 'Here is the cost to buy the CD, go down to Harvey Norman and buy Microsoft Word and you stick it in and it works'. That was all right, that was the \$15 million which was the core part of it. All the complication have been the 70 interfaces that have had to be built to make all the necessary connections.

Ms FORREST - Why didn't you know about that? That's the question here, isn't it? If you are going to buy something off the shelf, which is what you effectively did, knowing your business you would have known the complexities about the number of interfaces that you had, so why was it \$15million?

Dr DAVIS - To be blunt, it was missed. There were advisers we were using that supported the business case that went forward to the board. We have now changed advisers and the new advisers are saying what we are spending now is about right.

Ms FORREST - Did it go out to tender? How was it arranged?

Dr DAVIS - Yes, it did go out to tender.

Ms FORREST - But the tender process did not even detect this?

Dr DAVIS - No, because despite our attempts to make it as simple as possible -

Mr GREEN - Can you explain with respect to the NEM entry issues, the interfaces and why you have to have it even in preparation for competition?

Dr DAVIS - Yes. Effectively it is a whole business-wide application. There are interactions to the network business to allow for churn of customers - customers might churn to go to another retailer - there were settlements with the National Electricity Market and AEMO and all of their systems, there are market transactions that have to be handled, there are meter readings that have to go through and be passed through numerous systems and at the end of the day the result has to be accurate.

Ms FORREST - That is my point; you have just listed a whole range of things to be considered in the tender process.

Dr DAVIS - The scope becomes apparent as you get into the project. If you think about these systems they typically last 10-12 years and they get enhanced and added to along the way and they get bigger and more complex. In the time that our existing billing system has operated, we have entered the National Electricity Market, we have had Basslink come onboard, we have a new power station, so the system has continued to be enhanced over the last decade to build it up. It has got more and more complex but it has been done incrementally. On the day that you move to the new billing system you have to turn the old one off and the new one has to work. I think that it was the fact that the existing one had grown incrementally to accommodate the changes in the market that was missed. It is no excuse but other utilities have had the same issue. The complexity of these billing systems is quite extraordinary.

[11.30 a.m.]

Mr GREEN - There are 120 people working on them.

Dr DAVIS - Yes, there are 120 people working on it full-time at the moment.

Ms FORREST - To get the bill out - and don't we look forward to when we get it!

Dr DAVIS - Absolutely.

Mr GREEN - But it will be right.

Ms FORREST - No, it's not, that is the trouble.

Mr GREEN - That is on the old system.

Dr DAVIS - We hope it will be right.

Mr WILKINSON - Because that has obviously contributed to price rises as well in relation to the consumer, has it not?

Dr DAVIS - No, it has not, and that is the really pleasing thing from the customers' perspective, not so good from Aurora's perspective. Effectively what the regulator has done is look at what he believes is an efficient level of costs to deliver a billing system. It is basically the amount that he is prepared to pass through to the Tasmanian customers, and he has come to a view on that. Aurora is at a bit of a disadvantage because we are small. We operate in Tasmania with 250 000 customers, but the basic functionality that we need in this billing system has to be the same as if we were a utility with several million customers. We struggle with the economies of scale, we just do not have enough customers. You cannot get a cut-down version of the billing system because it still has to perform all the functions. The regulator has looked at our position and he has said, 'Given the size of the Tasmanian market, I'm not prepared to pass the full cost through to the Tasmanian customers', and that is one of the reasons why in our result this year we expensed, which means effectively wrote off, \$20 million worth of expenditure. The reason for that is that the regulator said he is not prepared to have that \$20 million paid for by the customer, it is just 'Tough, Aurora'. We have another report that says, 'You've spent the right amount of money'. We are aware of the difficulties that customers are facing so we are not going to go back and appeal to the regulator and say, 'I've got this report here, please give us the extra \$20 million and put the prices up'. We are not doing that. It has flowed through to our profits this year and the regulator has passed through to the customers what he deems to be an efficient and sustainable amount. The task now for us is to make sure that we get it right. When it goes live we want to make sure that everyone in the room gets the right bill and not a bill that is wrong and creates a whole lot of other work.

CHAIR - Who conducted the independent review on how much it would cost?

Dr DAVIS - It was undertaken by Deloitte.

CHAIR - What did that cost?

Dr DAVIS - I do not have the actual cost of it here.

CHAIR - Can you provide that to the committee?

Dr DAVIS - Yes, we can provide that cost. The issue here is that when you are dealing with something so complex - and I think to Ruth's point, 'Haven't other utilities done it?' - every utility is different. They operate in different jurisdictions, under different rules and customer numbers and so on, so none of them is the same. If we could have found one that was identical, we would have. We always use independent assurance -

Mr GREEN - We were quite proud of our old billing system.

Dr DAVIS - We were.

CHAIR - What did they find?

Dr DAVIS - They found that the project is being managed well. The cost of the billing system, which is around the \$60 million mark - a huge amount of money, but that is about right, they are comfortable with the program management and testing we are doing. We are moving to deliver that billing system probably at the end of the first quarter next year.

Mr WILKINSON - Did you have independent advice when you were first setting it up?

Dr DAVIS - Yes.

Ms FORREST - How much did you pay for that?

Dr DAVIS - Again, I would have to get you the detail on that. I know we have recently had some freedom of information requests from a member of parliament on the same topic, so the information is available but I do not have it at hand today.

Mr WILKINSON - With a legal background one would argue, is there a legal case as a result of the advice you had which 'may be' classed as negligent information?

Dr DAVIS - I suspect there isn't, Jim, and the reason for that is that the billing system that we are replacing, called Frontline, was built in-house. In fact, I sponsored that project about 15 years ago. Effectively every line of code was written, and there are hundreds of thousands of lines of code, and it reflects the business's processes. It is very hard for anyone to say, 'You should have known that this piece of code needed to be written in this way'. The billing engine, the key engine that is provided by Oracle, does perform to expectations. The issue is making sure all these interfaces work correctly so that it passes the pieces of data to all the parties that need to see them.

Mr HASKER - What sort of moneys would AGL or Origin have spent, to give Ruth an example, on their billing system?

Dr DAVIS - I think there has been public information of several hundred million dollars spent by the larger companies to build their billing systems, and they do not necessarily work.

Mr GREEN - Modern technology.

Mr WILKINSON - It is a worry, isn't it, in some ways. Are there any other systems that Aurora is putting in place, or about to put in place, that have the same complexities surrounding them which could cause the same price irregularities and cause peaks or troughs in your budget?

Dr DAVIS - I do not think I would be sticking my neck out to say this is probably the most complex IT system probably ever built in Tasmania in history and Aurora has no other IT systems of this scale or complexity that are needed. We do have some work to do in the network business to ensure that the network business is able to deal with different retailers but there is nothing in the scale of the billing system.

It is indeed the fundamental engine for the entire electricity supply industry and all the revenues that Transend and Hydro get as well all have to be processed through this system, so it is by far the largest one. Replacing these billing systems is a once-in-a-decade exercise and in this particular decade we have ended up in a much more complex environment than we were last time we did this.

Dr GOODWIN - The 120 people who are working on it at the moment, are they all Aurora staff or where are they all from? Are some external?

Dr DAVIS - A large number of them are Aurora staff. Aurora provides what you call 'business resources' to test the system and to make sure it works, say if they are on the phone to a customer, that it all operates properly but there is a range of consulting companies working with us and obviously the product vendors who provide the core code are working with us. The 120 is a mix of Aurora people and external contractors.

Dr GOODWIN - I think you said \$60 million, is that the cost all up?

Dr DAVIS - Yes.

Dr GOODWIN - Does that include the cost of the staff working on it?

Dr DAVIS - Yes, it does. It is the total cost. I think that is the issue: as these things take time to build, people have to be paid to work on them and that all adds to the cost so it is not just the cost of buying the piece of software.

Dr GOODWIN - What will the Aurora staff who are currently working on the billing system do when that project finishes, hopefully?

Dr DAVIS - Many of them will return to their original positions in Aurora. Many of them come out of the customer service area.

CHAIR - Any more on the billing system? If not, there are a couple of questions I have on the NBN rollout and originally you wanted to be a joint venture partner in that. What changed in that respect?

Mr HASKER - We might ask Mike Larkin to take over on that.

Dr DAVIS - I am just getting my mind around the NBN, another one of Aurora's interesting exercises. I would like to welcome Mike Larkin to the table. Mike is the General Manager, Telecommunications, for Aurora. Mike is a recent appointment to that role and he is charged with constructing the NBN in Tasmania as an agent for NBN Co, which is the Federal company but he also heads up our group that provides wholesale telecommunications so I think as we talk here specific to the NBN I am happy for Mike to answer that.

In answer to your question about the joint venture, the joint venture was never consummated so it was a concept that was described as a memorandum of understanding and that still exists. The critical thing is not the vehicle by which the NBN is rolled out but whether the objectives of the original MOU are being met and they are and they relate to delivering fibre to the premises for Tasmanian customers. Some of the media reports that have been around recently about the NBN and the joint venture and Aurora walking away from it, that is not the case. The joint venture was not created. What we saw instead was a different arrangement whereby Aurora acts as an agent for NBN Co and perhaps, Mike, could you explain some of what we do there?

CHAIR - With respect, the members have had a briefing on this matter so we understand all those parts of it. So there are just a couple of questions there: how will it be financially different for Aurora or, in other words, what are the costs and benefits?

Dr DAVIS - There are significant benefits in terms of Aurora's purpose. Aurora has a purpose to see the Tasmanian community prosper from our efforts so constructing a high-speed broadband network fits very nicely with that purpose so it is good for the customers. It is also good for us in the sense that we have developed a capability under Mike's leadership in terms of design, so we have some expertise in the State which I think is probably the best in the country. Could you just elaborate on the benefits, Mike?

Mr LARKIN - We undertake the detailed design work for the fibre-optic network construction. We also undertake the energy design works and provide as-built and build some material documentation for others to construct the network against. We also provide under stages 1 and 2 the PMO function or the commercial aspects of the other side of the project.

CHAIR - What is a contract worth to Aurora?

Mr LARKIN - For which element of the bill?

CHAIR - To actually do the whole -

Mr LARKIN - It is commercially sensitive and I am not at liberty to release that information because of the confidentiality arrangements in our agreement.

Dr DAVIS - Effectively, we are acting as an agent for NBN Co so there has been a lot of discussion in the Federal arena about the cost of the NBN. The pleasing thing for Aurora is that we are actively involved in making sure that Tasmania is the first State to get the benefits of the fibre and we do make sure that we conduct this work for NBN on a commercial basis so that we do get a return. Going back to the question earlier on segment reporting, when we look at our management accounts, our telecommunications business is a positive addition to the Aurora group.

CHAIR - So you are confident that you will get a good return on the project?

Dr DAVIS - Yes.

CHAIR - It will help the bottom line next year, next couple -

Mr GREEN - We hope it keeps rolling out.

Dr GOODWIN - Can I ask some questions on employee relations? Your current Aurora agreement, which covers 82 per cent of the Aurora workforce, is due to expire in May next year. How far advanced are the preparations or negotiation for a new agreement?

Dr DAVIS - I notice we have Nicole Wells sitting in the audience, but that will not change the way I answer the question in any way.

Dr GOODWIN - I am sure she will be interested anyway.

Dr DAVIS - She will be very interested in the answer. It is fairly early days. We are developing our strategy, but clearly we would like the enterprise agreement to support Aurora's strategy and we would expect to commence negotiations with the unions probably in February next year. The agreement that we currently have expires in May next year. It is in the preparation stage.

Dr GOODWIN - It is amazing how quickly May will come around.

Dr DAVIS - Absolutely.

Dr GOODWIN - You mention in the annual report that Aurora has introduced a cultural change program. What is that about and why was it considered necessary to embark on it?

Dr DAVIS - We are very proud of our cultural change work. It is to make sure that the people we have are focused on delivering our strategy and maintaining our safe and healthy workplace. Aurora is a company that has grown up from the Hydro but we operate in a much more challenging environment now than in the past.

Dr GOODWIN - Operating power stations - the Tamar Valley Power Station.

Dr DAVIS - Absolutely. We have a cultural program that is ensuring we have a very skilled workforce with the right attitudes and approach and culture, to help us deliver on our strategies and be a successful company. We are focusing on accountability - making sure that our staff feel that they are held accountable for delivering results; placing customers at the centre of all of our decision-making; good communication within the businesses; and, very importantly, mastering risk - being aware of the risks that we have and making sure that our people are well equipped to think about the risks and consequences of our actions. Finally, we are empowering our people so that their capability is matched to what they have to do within defined limits. It is a program which is being run in-house. We are using our own senior leaders to work with our own people and the language is really translating very well into the organisation because you really have to have everyone empowered and motivated to deliver on what is quite a complex business.

Dr GOODWIN - You have a group of apprentices graduating in December this year which includes your first fully qualified female distribution powerline workers.

Dr DAVIS - That is correct.

Dr GOODWIN - I am wondering how their experience has been. It seems that Aurora is still predominantly male, with women comprising only about 26 per cent of the total Aurora workforce.

Ms FORREST - A bit like this room.

Dr GOODWIN - Yes.

Laughter.

[11.45 a.m.]

Dr GOODWIN - Quite. Whether it is anticipated that they will remain with Aurora after they graduate.

Dr DAVIS - It is unfortunate that the ladies are not here to answer the question themselves, but when I have been out in the field and met ladies working for Aurora in what are traditionally male-dominated areas, I think they hold their own. We have ladies in senior positions in the field workforce now as well as apprentices and line workers and I think their experience has been very positive. We are very proud of the fact that we have more women in the workforce, but we still have some way to go.

This year the ladies, not I, initiated 'women in energy' which is a support network for women workers in Aurora and they brought in a number of ladies who had been -

Mr GREEN - I bet you wished you had thought of it?

Laughter.

Dr DAVIS - No, it would not be appropriate.

Ms FORREST - He would have been called sexist if he had done so.

Dr DAVIS - That is right.

So the women in energy network brought in external speakers who were ladies who had been very successful in their careers to provide inspiration and my understanding is that it is going very well.

Mr HASKER - You might also tell Vanessa what is the likelihood that these graduates will be continuously employed, Peter.

Ms FORREST - Are you keeping them on, that was the other question?

Dr DAVIS - Our apprentices are trained at Aurora but they are employed by a group training company and at the end of the four-year apprenticeship we evaluate how they have performed as apprentices and if they have met the appropriate standards and are going to be a valuable addition to our staff, we would generally recruit them and keep them on. So not everyone gets a job at the end of their apprenticeship, but the majority do.

CHAIR - How many apprentices are you putting on next year?

Dr DAVIS - We are not putting any new apprentices on next year. We are having a break in our apprentice program.

CHAIR - Why is that?

Dr DAVIS - There is a range of reasons for it, but one of them is related to the previous question. We do not want to put on a bunch of apprentices to find ourselves going into the AER submission and we have no work for them. If you are training people to specifically work on, for instance, powerlines - and we are the major provider of powerlines - you do not want to put them through four years of training and then discover you have no job for them at the end because the program of work has decreased. So that is one of the factors.

Ms FORREST - How likely is that though?

Dr DAVIS - We have been talking about customer price rises and, as I said, the AER is unlikely to support a major increase in capital for Aurora. We still have 46 apprentices going through our system in 2011. We have a further 17 trainees currently employed. So we still have a substantial apprentice program, we are just not putting some new ones on this year.

Ms FORREST - But if you have \$150 million annually to spend on poles and wires, which you said previously is sustaining the apprentices that you have at the moment, why would you expect that in four years' time there will not be work for them?

Dr DAVIS - Because the environment in which the last price determination occurred was not the same as the one that we are facing now. The pressures on customer price rises are so great, and we heard from Andre about smart grid, that in a few years we may need fewer people to carry out the program of work. We felt that we needed a year to consolidate. The other factor is that we are building a new training school to provide better facilities for our apprentices.

Ms FORREST - Where is that?

Dr DAVIS - That is at Mornington, on the Eastern Shore in Hobart, in the electorate of Pembroke.

Dr GOODWIN - Absolutely.

Dr DAVIS - That project has just been awarded to a builder and so there will be quite a lot of disruption occurring next year and the first-year apprentices do spend a lot of time in the classroom, so it is an appropriate year to have a breather on the apprentice program.

Dr GOODWIN - It mentions in the annual report, employee engagement is now at 61 per cent, or was for the last financial year which was a slight drop from 2009. What does that mean? What does it measure, employee engagement?

Dr DAVIS - Employee engagement is a very tough measure and it is one that tries to look at how motivated people are when working in the organisation.

Mr HASKER - It is measured by an international corporation. So it is world measure. It is benchmarked as far as you want to go.

Dr GOODWIN - Do you think the 61 per cent is a good figure or would you like to see -

Mr HASKER - I am always keen to see it increase and I am confident. We have had a lot of dislocation and employees, because of the flack they have been under the last 12 months, are probably a little disengaged and even threatened. I would like to see it increased but on a comparative scale, 61 per cent is a very good performance.

Peter, how would you - perhaps you might use more accurate words to benchmark it than I have.

Dr DAVIS - I think the Chairman is absolutely right. Having an engaged workforce is really important and it is something that we want to work very hard on. We are very transparent and open in this so we conduct an external survey every year. It is an anonymous survey done electronically so that all of our staff can give their views as to whether they think their manager is doing a good job or whether I am and so on. There are usually about 80 or 90 questions on the survey and it is conducted -

CHAIR - How has it been going?

Dr DAVIS - We got 61 per cent.

Laughter.

Dr DAVIS - The interesting thing with the 61 per cent engaged is that of the 90 questions, there are only six questions that are used as that measure. There are two on say, two on stay and two on strive. Say means what do people say about Aurora and do they feel proud to work with the organisation. In terms of stay, are they likely or would they like to stay with the organisation or would they be tempted by a job offer to go elsewhere. In terms of strive, do they provide additional discretionary effort beyond the day to day. So they are six quite difficult questions. They look at the score, 1 to 5, and then the external consultants give us a score.

Mr WILKINSON - How has that been affected as a result of what you were saying, the bad publicity?

Dr GOODWIN - Leapt 3 per cent this last year.

Dr DAVIS - I think there has been quite a bit about it. When I go out into the workforce, I find stories from all my people who have had unpleasant experiences with customers and a lot of that has been as a result of the publicity. The classic one was, we had one employee this year who achieved the remarkable milestone of 55 years continuous service. We normally only have awards at 15 years, 25 years and 40 years but this guy has done 55 years. He is a lovely guy; he tests poles for us so we gave a him little certificate and the *Mercury* came and took a photo of him. I thought I would just ask him, as he is one of our most valued long serving employees. I said, 'How is it going, Brian, are you getting any flack?' He said, 'Oh yeah, I stopped for lunch the other day and I was sitting in the truck when someone came up, banged on the window and tapped the watch and said what are you doing?' I said I was having lunch. This is a guy who has been working for the company for 55 years. It has had an impact on employee morale. I think the staff of Aurora are very pleased of the fact that the Premier wrote a personal letter to them indicating that he was supportive of what they were doing. I had certainly gone into the media to say that if people had a gripe about electricity prices, they need to understand what is driving it. It is not the Aurora employees. As the chairman says, we hope that it will improve next year.

CHAIR - We are getting to the stage where we have only seven minutes left so there are probably a few other important little bits we need to raise. Vanessa, have you finished?

Dr GOODWIN - Yes.

CHAIR - I will raise, Minister, something which crosses over to another one of your portfolios. There have been quite a few concerns raised, particularly if we start talking about irrigation and wealth from water. The concerns are some of these new irrigation schemes which are being rolled out. I refer particularly to pipelines in the Meander Valley. We talk about farmers coming on line with a myriad of new pumps to irrigate with at night, on off-peak tariffs. There are great concerns that there is not enough power in the system or that the infrastructure will not be able to cope with those particular issues.

Dr DAVIS - The specific one about Meander?

CHAIR - Yes, in this case but there will probably be others as well.

Ms FORREST - As irrigation is rolled out, there will be others.

CHAIR - Yes, that is right. It will keep going on. That has become a real concern out there from TFGA, from farmers themselves. We know from experience. We have had blackouts before. Where are we at with that?

Mr GREEN - I thought you were going to talk to me about irrigation tariff policy so I was going to do a brief on that.

CHAIR - That is another one.

Mr GREEN - With respect to whether or not you can actually service potential customers, I will have to seek some advice about that from a service point of view.

CHAIR - The issue was raised some months ago. I know there was a meeting in Westbury where all of this was canvassed and we have not had responses back yet.

Mr GREEN - I have not had it canvassed with me at this stage, as far as I am aware.

CHAIR - It has been canvassed with your office.

Mr GREEN - Has it?

CHAIR - Yes, it certainly has. That is a concern; the wealth for water is not going to work if you cannot get the juice at the right time.

Mr GREEN - It will work.

CHAIR - Well.

Mr GREEN - It has been canvassed but whether it is real or not, I am not sure.

CHAIR - It is, because a lot of electrical contractors were in on that. Somebody from Aurora did actually come up and met with the stakeholders and so that is something that is really missing in the system. The TFGA have been waiting for responses and they have not got them. The responses were promised some time ago so we need -

Mr GREEN - Mr Chairman, with all due respect, I will have to check that.

Ms FORREST - There is also no intelligence in the system either, the lack of feedback when things go further down line when you have a single line. That was another issue that was raised.

Mr GREEN - It really highlights what we were talking about before. Often irrigation dams are out in the middle of the farm somewhere and we have to provide the necessary infrastructure to get there. There is a significant cost associated with that.

CHAIR - But that is not the issue. The issue is whether, when all those pumps come on at night whether or not the system will be able to cope with it. Our understanding is that a lot of those are fed from two ways, from Railton and Prospect substations, and it will not.

Mr GREEN - I will have to take that on notice.

Dr DAVIS - We are happy to explore that one, Greg, and give you some more feedback on it. Again I am conscious of the time but our General Manager Network could certainly give quite a lengthy briefing on the work that we are doing to strengthen the system generally in terms of network planning.

CHAIR - At this time I do not think we need to.

Mr GREEN - What about a very short response?

Mr BOTHA - At the end of the day, irrigation farms on the network is not a new issue to us. It is really consistent with the way we manage networks. If in that specific case it is overloading the feeder then we need to reinforce the feeder. If a load comes on at night, there is no problem. With regard to the specific example and why my staff has not given me the feedback on attending a meeting and making promises, I will take it on notice and come back to you. But irrigation pumps coming on at night is not a problem for a 22KB line.

CHAIR - Okay. We will wait and see.

Mr GREEN - I would remember that.

CHAIR - We know it has been gone through anyway.

I know that the meter readers have to meet certain OH&S requirements but there have been a lot of complaints whereby meter readers have come and dogs particularly became an issue. If they are not chained up, the meter readers will not do it and then they do an estimate. But also from the rural sector if tanks have been wet and suddenly you get a bill, 'It was too wet to walk across even', it does not help the public relations when it seems it would be quite easy for those meters to have been read. That is the public perception.

Mr DAVIS - Absolutely, and there is no doubt that Aurora has received a large amount of correspondence. I have learned a lot about people who own pet ducks and dogs as safe as rabbits and dogs that are sitting inside. It has been quite fascinating. I think the issue here is that this is a -

Mr GREEN - A bloke still got bitten by a dog last week.

Mr DAVIS - Absolutely. We had a meter reader bitten last week.

CHAIR - Like politicians doorknocking. We all know.

Laughter.

Dr DAVIS - We have tried to improve the safety of our meter readers. We recognise people cannot have their dogs tied up all week so we have also agreed to narrow the window in which we guarantee to do the meter reading. It used to be five days but we have now narrowed it to three days. If we do not meet the three days we guarantee to do a special read.

The brochure that we sent out 'Is your dog a meter reader eater?' did generate a lot of interest from the public. That has been useful for us in terms of improving our database but when the meter reader turns up and looks over the fence and sees a kennel and cannot see the dog, he cannot go in. We have had meter readers who have been severely injured by dogs. A few of our guys have this gung-ho attitude, 'We'll be right' and we are actually trying to discourage them from that.

I went out a couple of weeks ago with one of the team leaders. He reckons he is pretty good with dogs. He got into the yard and a big Alsatian trotted up, 'I don't like the good of that' but he spoke nicely to the Alsatian and it was fine. He walked up talking to the dog, got to the meter and started to do his meter read. At that moment the owner came out of the door and the dog latched onto him because that was what the dog was supposed to be doing. It is a very difficult area until we get smart meters -

Mr GREEN - What about wet paddocks?

Dr DAVIS - With wet paddocks access is a bit of a challenge. I have not had a lot of specific feedback that people could not get in but again we cannot afford to have vehicles getting bogged and so on.

CHAIR - No, but people can walk. Some of them have been very short distances like about 30 or 40 metres. You do not have to drive that far.

Dr GOODWIN - Perhaps they might need to be equipped with gum boots, Greg.

Dr DAVIS - One of the other things we are encouraging customers to do, that we have just trialled, is to self-read. We actually are training the customers in those difficult-to-access readings to read the meter themselves and send the information in to us. That saves everybody trouble.

CHAIR - Unfortunately, our three hours are up. They have gone very quickly.

Dr GOODWIN - I was just going to ask this one but it could be provided on notice. I wondered whether it is possible to get a breakdown of your employees in terms of where they work and also your vehicle fleet. What sort of vehicles do you have and how many?

Dr DAVIS - I am very happy to do so.

CHAIR - That was quoted in a *Warm* magazine at one stage. It seemed as if you have 1 400 employees and 1 000 vehicles or something like that.

Dr DAVIS - We count trailers as well, anything with wheels.

Mr GREEN - Could I thank the CEO and the Chairman and each and every person who has contributed?

CHAIR - We probably have a lot of other things that we could do but our three hours are up. I would just like to thank yourself and your team for coming along. Thank you very much.

Mr GREEN - Could I pass on my thanks particularly to the Chairman and the CEO and each and everybody who has contributed particularly to Anton and everyone else who has put together all the documentation, et cetera, so that we could provide you with this full and frank briefing. Thank you.

The committee adjourned at 12.02 p.m.