

**Tuesday, 6 December 2016 - Legislative Council - Government Businesses Scrutiny Committee A -
Tasmanian Public Finance Corporation**

LEGISLATIVE COUNCIL

GOVERNMENT BUSINESSES SCRUTINY COMMITTEE A

Tuesday 6 December 2016

MEMBERS

Mr Armstrong
Mr Farrell
Ms Forrest (Deputy Chair)
Mr Gaffney
Mr Hall (Chair)
Mrs Hiscutt
Mr Mulder

IN ATTENDANCE

Hon. Peter Gutwein MP, Treasurer

Ministerial Office

Mr James Craigie, Chief of Staff

Tasmanian Public Finance Corporation

Mr Tony Ferrall, Chair

Mr Stephen Rochester, Chief Executive Officer

Mr Heath Baker, Head of Financial Markets and Client Services*

Mr Ignacio Welch, Chief Financial Officer*

CHAIR - Good morning, Treasurer.

Mr GUTWEIN - I place on the public record my thanks to the outgoing chairman, Don Challen, who retired during the year. Mr Challen was well known to all of you. He served as the chair of Tascorp since 1993 after first becoming a director in 1991. Mr Challen built a sound organisation with a strong sense of strategic direction and a culture of providing value to the clients of the business, and as a result has provided significant value to the state of Tasmania. Tascorp, under the new chair, Mr Ferrall, will be in good hands. I am sure he will continue to build on the strong foundations Mr Challen put in place.

As I explained to Estimates committees on prior occasions, Tascorp is one of the government's more solidly performing businesses. Maintaining essential borrowing authority by pooling the borrowing requirements of individual clients ensures that benefits such as lower borrowing and operating costs, better risk management, as well as access to financial markets are available across the entities that utilise the services of Tascorp.

Providing this service, Tascorp strives to add value and also provide a return to the state. A net profit before tax of \$13.9 million was achieved for the year, which is around 9.5 per cent higher than the business plan budget of \$12.7 million. During the last financial year, the state received \$5.867 million in income tax equivalent payments. This year the corporation will pay a tax equivalent payment of \$4.178 million to the government in December of 2016.

Additionally, under the lump sum dividend and tax equivalent regime, an ordinary dividend of \$0.822 million will be paid. In accordance with the statement of corporate intent, a discretionary dividend of \$4 million will be paid in December 2016.

Staff numbers have remained fairly constant compared to previous years. The business has performed strongly, and I acknowledge the board, management and staff for their efforts during the past financial year.

CHAIR - We might start off with your main customers. We had a briefing session with the A-G yesterday to clarify a few points. We are sitting on TasNetworks at 52 per cent, Hydro at 26 per cent, TasWater at 12.8 per cent, and the balance are local government entities. That is about correct in terms of percentages.

Mr GUTWEIN - In percentage terms, I will not argue with the A-G. If you turn to page 32 of the annual report, there is a list there of all of the state entities.

CHAIR - Given TasNetworks is 52 per cent, they actually paid out some of their original loans and then renegotiated with your entity here to get themselves back on another even keel. You are not concerned about a very big exposure to TasNetworks in that respect?

Mr GUTWEIN - TasNetworks is a very sound business. It has a regulated revenue stream. It does not require a letter of comfort and I have not been asked for one from Tascorp. I would like a few more clients like TasNetworks. Mr Ferrall can speak about the percentages, but at the end of the day they are a very solid business.

Mr FERRALL - Tascorp was very comfortable with the exposure to TasNetworks. As the Treasurer said, they are a strongly performing business. They operate in a regulated environment. They have a regulated return. We look at all of our client exposures, including TasNetworks, and the board was comfortable with the level of exposure and did not require any additional comfort from the Treasurer in relation to the borrowing.

CHAIR - Are most of those major customers on an interest only deal at the moment or are they paying capital back?

Mr FERRALL - Most of them are interest only.

CHAIR - If they went out to the commercial market, given things are competitive at the moment, could they do better in that respect than going to Tascorp?

Mr GUTWEIN - We are very competitive. There hasn't be a flurry of activity with government businesses requesting different arrangements or the opportunity to look elsewhere. They seem very comfortable with Tascorp.

CHAIR - With the terms of those loans, if they are interest only, eventually you would expect in the commercial world the capital has to be repaid. You are not concerned or would they renegotiate the loan and keep on rolling along? How does that work?

Mr FERRALL - They tend to have a rolling capital program and as that rolls forward they renegotiate the loans. Something like TasNetworks has some very long loans and I can talk a bit about that later on. They have exposures over a period out to 10 years and they have a long loan which goes much longer. As those loans come up for maturity, they then make decisions, depending on their financial and cash position, whether they retire the loans or renegotiate.

CHAIR - Can you give an indication as to how long they may be able to fix their interest rates, an interest-only component?

Mr GUTWEIN - I think there is quite a good story. There is some very long money at the moment.

Mr ROCHESTER - Tascorp's job is basically to take the economies of scale and scope of all the individual bodies and aggregate it into Tascorp. We can go to the market for a wider range of forms of debt and for larger amounts of money than each of our individual clients is able to do. The market we operate in is the Australian bond market and that market runs out to 10 years. Our strategy is to have a bond every two years, given our size. We can have what is called liquid tradable bonds that world markets and the Australian market can deal in. We have a bond every two years and we can use that to provide each of our clients with a bond equivalent maturity of every year over those 10 years. Then it is up to each business, for example, TasNetworks. It is a regulated body, the regulator sets the cost of capital based on a rolling 10-year average of maturities. We provide them with the equivalent of that, a tenth of their exposure broadly every year for 10 years.

During this financial year, TasNetworks sees what we describe as an opportunity in the market to go to the market for what was then Australia's longest term bond. We were able, on behalf of TasNetworks, to issue a 30-year bond. It was the first issue by any Australian issuer in that ultra-long end of the bond market. Subsequent to that, the Commonwealth Government has decided also to issue in that long space and launched a 30-year bond a few months ago.

We are able to replicate anything that happens in the market and provide that to each client according to their business requirements. The bulk of their exposure is in that one-to-10-year range but they have this ultra-long bond of 30-year exposure that was issued earlier this financial year.

Ms FORREST - If you go to page 21 of the annual report, interest revenue was \$209.7 million. The cash receipts on page 24 in your cash flow statement are only \$177.8 million. When you look at the note on page 33, they only increased by \$5 million. You would expect cash to be less than accrued by \$5 million but the difference is \$32 million. You also see that there is a \$5 million reconciliation figure in Note 17C on page 36, so can you explain to the lay person, as most of us are in regard to this, where the other \$27 million of interest revenue came from? If it wasn't cash received, and I'm talking about interest only revenue as per the income statement and Note 3A, was it from TasNetworks? They recorded a loss on a debt restructure, which we have just been discussing, of \$23 million. I assume it is a book entry around that debt restructure of TasNetworks, but I would like you to go through that process if you wouldn't mind, referring to those particular documents?

Mr WELCH - I will answer that in the first instance. Tascorp's financial statements don't flow like general companies' costs financial statements. When you look at cash movements and outstanding accruals on loans it is captured in the market value of the loans. It won't appear through the receivable note in the financial statements, so it is quite difficult. You can't take those numbers and work your way through it like that.

Ms FORREST - How does the layperson understand it then?

Mr WELCH - Good question. The key at the end of the statement is to look at the interest revenue. With cash flow one of the things you have to realise is the cash flow on the bonds we issue to market and the cash flow we get from the loans off the customers don't match up on the same dates. It is quite difficult. You won't see it from the receivable note you will see it flowing through the market value of the client loans.

If you look at the cash flows - I'm trying to think of the easiest way to show this - you will see how cash flows can vary from year to year quite significantly on interest, inasmuch as last year in 2014-15 there was in the region of \$40 million positive cash flow on the trust. This year there is a negative \$13 million. That is because the coupons on these bonds, on these loans, happen at different times. The financial year is 30 June to 30 June. We have one payment going out, say, 15 June one year and the received side doesn't happen to July/August, so there can be big swings from a cash flow perspective. I hope that helps.

Mr GUTWEIN - There are timing issues.

Mr ROCHESTER - The key is we lend to each client a margin above what the funds cost us. If we can do a bond issue at 2.5 per cent then we lend to a customer at, say, 2.8 per cent. It is that margin that is important for us over time, not in any particular one year. It is a rolling, ongoing business.

Ms FORREST - The debt restructure that TasNetworks did basically cost them \$23 million?

Mr ROCHESTER - In terms of the debt that was repaid, but offsetting that they took on new debt at a lower interest rate.

Ms FORREST - Did the \$23 million have a positive impact on your revenues?

Mr ROCHESTER - No, we survive on the margin between what we borrow at and what we lend at. The interest rate risk goes through to each customer. For example, with TasNetworks they repaid debt that had been at a higher interest rate and took on new debt at a lower interest rate. The debt that was repaid has a loss to it, but they are saving money on the lower interest rate.

Ms FORREST - They are, but in terms of Tascorp's -

Mr ROCHESTER - It has no impact on us over time.

Ms FORREST - In this year?

Mr ROCHESTER - In this year, again, we will get to some detail.

Mr WELCH - The vast majority of our financial statements are on a market value basis. What that means is Tascorp is very conservative in how we process interest rate to management. An interest rate exposure in terms of the client is largely offset by an interest rate exposure to the market. The figure quoted there of TasNetworks, we already had that number in our financial statements from a previous time.

Ms FORREST - For the debt refinancing they did and the difference they had to pay between their current and former interest rates, which is a difference of between \$3 million - we did discuss this with the Auditor-General as well - without that extra revenue for Tascorp, and I know there is timing difference when money comes in and out, but would it have meant that TasCorp would almost have recorded a loss without that money coming in or not?

Mr WELCH - No, because we market value everything literally day in, day out. From TasNetworks perspective - and I am pre-supposing - that \$23 million is the difference between the market value of those loans when they repaid it and the book value of those loans. Whilst in our books it is always the market value. So the current market value is always reflected in these statements which is a mixture of our assets and our liabilities.

I cannot quote the number here, but from our perspective, the figure would probably be in the tens of thousands rather than in millions.

Ms FORREST - Going back to page 5 of your annual report, the charts with the Tasmanian economy, why do you only mention the state's fiscal position? Isn't it more important from TasCorp to consider the whole state sector, because that is where all the debt is. Shouldn't TasCorp be more concerned with that in terms of reporting to the users, particularly? Treasurer, one for you.

Mr GUTWEIN - The point made in page 5, being the chairman's report, the credit rating of the state, is based on the total state sector. In regards to highlighting this - which is a very good thing to highlight - as it is the chairman's report, I might ask Mr Ferrall to speak.

Mr FERRALL - This is Tascorp's annual report. Effectively the chairman's report is picking up some highlights and commentary. It is not a formal part of the reporting frame, per say.

The issue is the position of the general government sector is of interest to readers in terms of the context for Tascorp's operation, and to put it in is quite reasonable. I take your point, you could put more information more broadly around the total state sector. We have put some commentary about the Tasmanian economy, which again is a higher level, bigger picture.

Ms FORREST - Literally, they are not in the general government sector, they are all in the total state sector with the GBEs and local government all outside of it. Perhaps it would be more helpful to have as well, not instead.

Mr FERRALL - I have no problem with broadening or putting further commentary.

Ms FORREST - Because, let's face it, the charts are a bit different.

Mr FERRALL - Absolutely, and the overriding point is those things are reported elsewhere in terms of the Treasurer's annual financial statements through the Budget process, et cetera.

Ms FORREST - Which is always a good document of the year.

Mr FERRALL - Absolutely.

Mr ROCHESTER - The purpose of the commentary was to summarise for investors who do credit limits for Tasmania. If our investor is going to buy a Tascorp or a Tasmanian bond, they first have to get a credit limit from their investment committee. One of the things they do in the process is look at the performance of the economy - the Gross State Product part of this introduction. The second part is, what is the fiscal strategy of the state government and that picks up the net debt summary there. Then they start looking in more detail to the performance of the individual components to the economy and then the borrowing program of Tasmania and what it is targeted for. The purpose for this is to pick up that high level first step a credit analyst will go through in terms of looking at Tasmania and deciding whether they wish to invest or not in Tasmania with the bonds.

Mr FERRALL - It is an important point, because they are looking at Tasmania. They are not necessarily looking at Hydro or TasNetworks. They look at the credit of the State of Tasmania. Tascorp has the exposure to Hydro or TasNetworks or whoever we lend to. The market, effectively, has an exposure to the State of Tasmania so that is the split there.

Mrs HISCUTT - On page 32, your client, University of Tasmania, borrowed \$108 million. It is a bugbear of mine that the university can borrow that sort of money and then purchase naming rights for Blundstone Arena. It doesn't seem right, but the only concern here is if they can pay the money back, and do they pay it back with interest?

Mr GUTWEIN - Tascorp's concern is whether it is a good loan. In regard to the naming rights, Aurora Stadium springs to mind. The growth in students, both internationally and from the national base, is very important to the university and our broader economy. That has been a sensible investment and will have great

reach around the country. It has the opportunity to dovetail into what will be a very strong precinct in Launceston. Whether they can pay the money back is a matter for Tascorp, and I am sure they can.

Mr FERRALL - The university has a very strong cash flow, very little debt, and a very strong balance sheet overall. From a Tascorp perspective, we are very comfortable to loan to the University of Tasmania.

Ms FORREST - Wasn't that a lot to do with the NRAS funding?

Mr FERRALL - I understand, and I may be corrected, that was related to their housing developments.

Mrs HISCUTT - On purchases from Tasmanian businesses that fall into the Treasurer's Instructions to buy local, you have a figure of 29 per cent of purchasing local. Do you have plans to improve that? Why is it only 29 per cent?

Mr FERRALL - In effect, Tascorp is not a significant purchaser. The sorts of things we purchase in financial products, IT, software, et cetera, are generally unlikely to be purely Tasmanian based. We try to make the most of the Tasmanian base where we can, but our percentage is likely to be low because of the products we need. Part of it is also fees to Standard and Poor's and Moody's.

Mrs HISCUTT - Your figure for consultancies, \$30 422, is fairly low. Does that reflect the fact Tascorp has those brains working within the company?

Mr GUTWEIN - It is a very smart business, I can assure you of that.

Mrs HISCUTT - The consultancy and expertise has to come from somewhere. You must have them within your company.

Mr FERRALL - The expertise is within Tascorp. It is not exclusively within Tascorp and there are times we need external support.

Mrs HISCUTT - The hierarchy for your organisation - you only have three women, which is fairly low. The Government's idea is to bring more women to boards. Do you have plans for recruiting women or is this simply the way it is?

Mr FERRALL - At board level we have a 50:50 split, which is positive. Organisationally, it is a work in progress. It is improving. I am not making excuses, but it is a difficult area, in a market sense, to attract women. The areas we tend to recruit from don't have a significant component of women employees either, so it makes it hard in a recruitment sense. It is one of those areas where we know we have to do better and need to do more work.

CHAIR - Treasurer, of the client listing, which is extensive, we talked about those percentages of the GBEs making up most of those. We have 29 councils, which may reduce at some stage. Do you have any concerns about any of those local government entities on the borrowing list at this stage or do they all have a capacity to do what they have to do?

Mr GUTWEIN - In terms of do they have the capacity to do what they need to do, yes. Tascorp takes a very conservative approach in regard to lending with local government. I think the ratio, correct me if I am wrong, is that they cannot borrow any more than 50 per cent of their rateable revenues. If you consider the total quantum of local government borrowings, which I think is \$100 million or thereabouts -

CHAIR - It is a more conservative approach than what you would take, say, to TasNetworks or whatever, is that what you are saying?

Mr GUTWEIN - If you consider local governments' net asset position, excluding TasWater, is around \$7 billion and the sector carries only \$100 million worth of borrowings. Again, if you look at their revenues at the local government sector level I think last year the total income that local government has at its disposal is around \$750 million - that is in both rates and grants revenue. They are particularly strong.

CHAIR - TasWater, for example, which we will have this afternoon, has a ceiling, if you like, up to which they can go to in borrowings. Are you across that one at all?

Mr GUTWEIN - Again, TasWater is not in my purview and these are questions that should more properly be directed at TasWater. However, I have held the view for a long time that their debt to equity ratio on their balance sheet has been low for a regulated business. I was very pleased that recently the board took a position whereby they are going to increase their borrowings over time and deal with some of those more problematic challenges.

CHAIR - To whom?

Mr GUTWEIN - The board is going to increase their borrowings over time, as I understand it, and they are going to deal with some of the more problematic issues they have, the more than 20 boil water alerts, and also we have the combined system in Launceston and other matters to deal with. My recollection is that the ratio they were borrowing at was sub-25 per cent whereas most regulated businesses would be closer to 60 per cent. I think they have capacity on their balance sheet but they have increased their borrowings in the last year.

CHAIR - Then there is the old hoary chestnut of FT that attracts criticism from some. Any comment there at all?

Mr GUTWEIN - FT operates under a letter of comfort. We have been very public in regard to our strategy with FT, the fact that a portion of the plantation estate will be sold to assist both with the restructuring and refocusing of that business but at the same time to ensure that it can repay its borrowings. Again, looking at the annual report, the level of borrowings that FT finished the year at was only around \$14 million. My understanding, from previous discussions with the company, was that their net position was around \$10 million, taking into account the cash they held. It's a work in progress.

Mr FARRELL - Treasurer, you mentioned they had a letter of comfort. Last year there were, I think, six letters of comfort. How many are there currently and who has them?

Mr GUTWEIN - There were letters of comfort to Forestry Tasmania as we have discussed, Hydro Tasmania, Tasmanian Irrigation, Tasmanian Railways, TasPorts and Tasracing. So there were six, as there were last year.

Ms FORREST - On that point, I haven't looked at TasPorts' annual report and we are not scrutinising them this year, we have had others to look at. Why do they require a letter of comfort?

Mr GUTWEIN - They had a letter of comfort in place solely for the loan to purchase the Burnie woodchip facility. That was \$7.5 million.

Ms FORREST - That letter of comfort is still in place?

Mr GUTWEIN - It's still in place.

Ms FORREST - Do you expect it will not be required in the short to medium term?

Mr FERRALL - That was a very specific facilities civic loan and that is why the letter of comfort is in place. From a purely Tascorp's perspective it would be a question of when that loan is repaid.

Ms FORREST - With Hydro Tasmania and their letter of comfort, and this was one of our businesses that provided enormous returns to government over time, it is a sad state they have found themselves in. I understand the reasons, we all do. What is your expectation, Treasurer, on managing to return to a position where they don't require a letter of comfort?

Mr GUTWEIN - Perhaps it would be useful to provide some history regarding Hydro and letters of comfort, so everyone is aware. The current letter of comfort is for \$1.085 billion. A letter of comfort issued on 17 July 2009, it was in place then. There was a previous letter of comfort initially issued in July 2006. The limit on that was increased to \$1.385 billion, significantly higher than the letter of comfort in place today. Hydro are operating well within their letter of comfort at the moment. They have a further \$50 million equity transfer I expect will be paid later in January.

Ms FORREST - Correct me if I am wrong, but back then Hydro tended to be loaded up with debt and TasNetworks - Transend, it was called at the time - was not loaded up. We keep seeing this restructuring from former governments, not only yours, Treasurer, that have done that. If you are going to try to compare apples with apples then you need to compare apples with apples. The question now is, what is your expectation about Hydro's letter of comfort? There could be a range of things to do with insurance and all sorts of stuff that may flow from there.

Mr GUTWEIN - There are a range of matters. Over time, I would expect Hydro's financial position to improve. They are in a very strong position with the amount of water they hold. There are other matters that need to play out. I would expect over time Hydro's financial position to improve.

Ms FORREST - Do you have a desired outcome for the removal of the letter of comfort?

Mr GUTWEIN - The letters of comfort are based on Tascorp's view. I would prefer to have businesses that did not require a letter of comfort.

Mr FERRALL - Hydro has engaged with Tascorp. Without speaking for Hydro, they have engaged with Tascorp looking at a longer term or medium term strategy to improve their position and not be reliant on the letter of comfort.

Ms FORREST - Do you have an expectation around the time frame for that?

Mr FERRALL - No, we don't, but there are preliminary discussions with Hydro around how they would operate to alleviate the need for a letter of comfort. That has come through to Tascorp from Hydro. It is a matter you would need to take up from Hydro rather than Tascorp. I think Hydro is attempting to improve its performance significantly over time. They don't like having a letter of comfort. That is not a position they like, having a letter of comfort issued, and I think we will see that improve.

Mr FARRELL - Are there concerns within Tascorp about Hydro's financial sustainability?

Mr FERRALL - No.

Mr FARRELL - You don't feel there is any risk of insolvency?

Mr FERRALL - Absolutely not. It is important to understand why Tascorp seeks a letter of comfort. We set a very high benchmark in entities we are going to lend to. We want the entities to be a high investment grade. If we believe they are not quite at that point, then we go through a process of engaging with the entity and engaging with the Treasurer in relation to a letter of comfort. The letter of comfort provides a signalling mechanism to the Treasurer and it also involves Treasury in the process because Treasury then has to provide advice to the Treasurer on whether to support the proposed letter of comfort. It is not a signal that we believe they are insolvent or bankrupt, for want of a better description, because we do not want to have to rely on the

letter of comfort. We want the entities to repay the borrowings over time. We do not want to have to go back and say, x entity cannot repay the borrowing because that leaves us with significant exposure.

Ms FORREST - You talk about if a letter of comfort is required by Tascorp then Treasury give advice to the Treasurer - you are wearing two hats there, Tony. I am assuming you are part of that advice. Are there any conflict issues or how do you manage that?

Mr FERRALL - No, there are not any conflict issues. The performance of Tascorp and how Tascorp operates is intrinsically linked to the state and vice versa. There is not a conflict scenario because the interests are aligned and it is not a scenario where either one entity would be advantaged by a particular decision approach or where, from a personal perspective, I have any personal gain that will create a conflict.

It is very important, and it is the model followed right around the country, that Treasury is very closely linked to Tascorp. I do not believe you could have a model which did not have the Treasury secretary on the board or at least a senior person from Treasury on the board. You would not necessarily have to have the Chair as that person. But having someone on the board is critical to the state's interest.

Mr GUTWEIN - Under the previous Chair, letters of comfort were requested in regard to Hydro at a higher level than they currently have in place. It is not unusual. There has been some interest in the media lately in respect of Hydro having a letter of comfort in place but we can demonstrate that back to 2006, letters of comfort have occurred.

Ms FORREST - A letter of comfort in 2006 when Hydro already has significant borrowings, was for a major capital expenditure like a dam. I do not know what it was for at that time and maybe you do, Treasurer.

Mr GUTWEIN - I would need to look back.

Ms FORREST - People can understand that. I suppose that they have had them in the past is a relevant point but not necessarily. This is a different situation the Hydro are facing now. A one in 3000 years event, I believe the Chairman of Hydro said.

Mr GUTWEIN - As a business, the value of Hydro in its assets base in 2006, is a more valuable business today and it is carrying a lower letter of comfort today.

Ms FORREST - I accept what you are saying.

Mr FARRELL - The Legislative Council had an inquiry into the unfunded superannuation liability. Does Tascorp have any concerns relating to that?

Mr FERRALL - I do not think it is a matter for Tascorp. It is a discussion for Treasury and the Treasurer but it is not a Tascorp issue per se.

Mr FARRELL - Fair enough. We did not hear from Tascorp in that inquiry. That is probably why.

Ms FORREST - Probably for the obvious reason.

You mentioned earlier on, Treasurer - well, either you or the secretary did. On page 7 you talk about the launch of the 26 preferred bond and issue of a 2046 bond. I will put all of my questions to you, and then you can answer them.

Are these two things the same thing? I know 2046 is to do with TasNetworks. These bonds are on the borrowing side, are there matching loans on the asset side? Are they predominantly with TasNetworks? Can you explain that?

Can you also explain the extended longer-term bonds, and what assumptions have been made? What are the risks and the rates? Some of the rates are mentioned. On page 35 there is a description in note 14. I am interested in the whole picture.

Mr GUTWEIN - I will allow either the Chair or Stephen - I know Tascorp is very proud they were able to land that 2046 bond. Steve has indicated, subsequently tied the federal Government locking in money, which makes a great deal of sense at the moment when you consider interest rates are at historically low levels. Even with the most recent outcome in the American election we have seen some upward pressure on rates. I think over the longer term this will be seen to be a very sensible decision taken by Tascorp.

Mr ROCHESTER - The chart on page 7 shows the bonds we have on issue and how they have changed over the year. Our strategy is to have a bond maturing every two years. We use funds from those bonds to provide lendings back to each individual client. There may be timing differences. We may raise funds before they are lent, but funds are used solely to provide funding to each individual client.

They are also looking for that rolling 10-year exposure. One year drops off and a new year comes on, and we are looking to add - our next bond will be in 2028, which we contemplated issuing sometime next year or the year after. That is then used to keep that rolling 10-year cycle going across our own bond issuance and the financing provided for each client.

The 2026 was to extend our curve. Before that we only had it at 2024. The 2026 added that next two-year bond. That money was then used to lend to each individual client. As you have pointed out, TasNetworks is our largest single customer, so it takes a larger share of those. Their own benchmark is a regulated 10-year rolling average, and is extended each year as well.

That is the rolling cycle of the business we are in. We expect to add a new bond each two years to our own bond issuance program in the marketplace. That is used to finance ongoing lending to individual clients, according to their particular needs. The 2046 was, I think as we covered in earlier conversations, a one-off. Interest rates were very low. TasNetworks and Tascorp saw a benefit in diversifying our exposure to reduce the maturities in each year. There was a confluence of requirements.

Ms FORREST - Is that at a fixed rate?

Mr ROCHESTER - Yes.

Ms FORREST - What is the rate of that? I cannot see it in here.

Mr ROCHESTER - I do not have the coupon off the top of my head. There were two issuances -

Mr WELCH - On average it is about 4.3, I think, a 4.3 yield.

Ms FORREST - Are any other assumptions being made around that?

Mr ROCHESTER - No. It was raised in the market and lent, at its same terms and conditions with our administrative margins, to TasNetworks. As far as we are concerned, all the risks and cash flows with that bond issuance have been locked in at the time of issuance. We raised it in the market. On the day we raised it, it was lent to TasNetworks, which is about as efficient as you can get in our market.

Ms FORREST - One of the gentlemen mentioned - I think it was you, Treasurer - that Tascorp pays income tax equivalents on profits, which include fair value gains and losses, which is different from Hydro Tasmania, for example. Why is that different approach taken? Can you explain the fair-value gains to me? When you talk about the credit risk of client advantages - note 18B on page 37 and top of page 38 - you are talking about credit risk of lending to TasWater, government and the university, for example. Can you take me through that?

Mr FERRALL - Tascorp is quite variable because of its role in the market and marked market accounting. As to Tascorp's profit position, it can be quite variable, which is why, going back in history, the lump sum dividend and income tax equivalent regime was established for Tascorp. The current recommendation we make is a payout ratio of 50 per cent of the general reserve. The general reserve was \$10 million -

Ms FORREST - It still is, isn't it?

Mr FERRALL - Yes. So that gives us an equivalent for - say for 2016-17 - of \$5 million but our tax equivalents are calculated out at \$4.17 million. We make an ordinary dividend of \$820[?], which gets to that round \$5 million. In addition to that, the board considers the capital requirements of the organisation every year. We are paying, as we have in a number of other years, an additional discretionary dividend of \$4 million because we believe we have more than adequate capital held within the organisation. That is how the lump sum dividend tax regime works.

Ms FORREST - I want to mention the \$10 million reserve. We had a discussion with the Auditor-General yesterday and he was questioning the necessity for that \$10 million reserve. It could be retained revenue.

Mr FERRALL - Tascorp has an approved capital limit of \$38 million from the Treasurer. Tascorp operates like a pseudo bank and our available capital, like a bank, limits the activities we can perform both in a lending sense and an investment sense. The importance of the general reserve is that in circumstances where there was some variability in any particular year we know from a board perspective we have the capacity to fund that without becoming a call on the general government. I am happy to talk to the Auditor-General about what might be an appropriate level, but I don't think the Treasurer of the day would be necessarily comfortable in the circumstance where there was some variability if Tascorp said, 'Because of market changes or particular issues we need \$2 million this year'.

Ms FORREST - Couldn't you take that out of retained profits? I am struggling to see why it's not just part of retained profits.

Mr FERRALL - What we do as a board is look at what capital we need, which is why we are making a discretionary dividend of \$4 million this year on top of the ordinary dividend and tax equivalents. Going forward over the next couple of years we have budgeted, I believe it is \$4 million per year, as discretionary dividends which would be paid back to the state.

Ms FORREST - It comes out of that?

Mr FERRALL - Yes, coming out of our holdings.

Mr FARRELL - We asked this question of our previous GBE. In relation to the money you have loaned to Hydro, if one of the major industrials fell over for whatever reason, what impact would that have on Tascorp? Do you take that into consideration when you are looking at the money you provide to Hydro?

Mr FERRALL - We do an assessment of Hydro in terms of, let me call it a banking assessment, where we assess as a lending entity whether we are comfortable lending to Hydro. We take into account a range of factors. Quite obviously, an impact of a major industrial ceasing to be a customer would have a significant impact but we haven't directly picked that up in any of our assessment. We assume that - again, it would be a matter for Hydro - they would look for an alternative customer or alternative sources of revenue in those circumstances.

Mr GUTWEIN - One thing about Hydro, and I know there will be interest throughout the course of this week in its financial circumstances, in regard to the letter of comfort that is in place for the Hydro, that was actually revised down in the 2015 year and hasn't been increased or altered since. It is not as if the events at the end of 2015 and the challenges we faced earlier on this year have put upward pressure in regard to the Government needing to issue either a new or an increased letter of comfort. In fact, the level of borrowing was

revised down early in 2015 to the current level of \$1.085 billion, has remained at that level and Hydro are operating within that envelope. I know there has been some interest from the press about them having a level of comfort but truth be told, earlier on in that year the event first became noticed, the level of the letter of comfort was reduced and hasn't been increased or altered since.

Ms FORREST - There is potentially more of an issue for TasNetworks if they lose a major customer because, in the regulated environment in which they work, I don't believe that would affect their borrowings as such as it just means that everyone else - all of us - would have to pay more for the networking part of our energy bills.

Mr FERRALL - I think any significant change to the MIs will have a large impact on the state more broadly. It would impact on all of our energy businesses effectively.

CHAIR - Thank you. On behalf of the committee, thank you very much, Treasurer, and to your staff. I have to say, usually this particular GBE has less complexity than some of the others that we have to roll through. It makes it a fairly straightforward process. Thank you very much.

The committee suspended at 11.03 a.m.