



LEGISLATIVE ASSEMBLY OF THE NORTHERN TERRITORY

12th Assembly

Public Accounts Inquiry into Splitting the Power and Water Corporation

Public Hearing Transcript

9.00 am, Monday, 28 April 2014

Litchfield Room, Level 3, Parliament House

Members: Ms Lia Finocchiaro, MLA, Member for Drysdale
Mr Gary Higgins, MLA, Member for Daly
Mr Nathan Barrett, MLA, Member for Blain
Ms Nicole Manison, MLA, Member for Wanguri
Mr Kon Vatskalis, MLA, Member for Casuarina
Mr Gerry Wood, MLA, Member for Nelson

Witnesses: New Corporations Unit
Mr Alan Tregilgas, Executive Director
Department of Treasury and Finance
Ms Jodie Ryan, Under Treasurer
Mr Craig Graham, Assistant Under Treasurer
QEnergy
Ms Kate Farrar, Managing Director
University of Queensland
Professor John Quiggin
Power and Water Corporation
Mr Ken Clarke, Chairman of the Board
Mr John Baskerville, Managing Director
Ms Djuna Pollard, Senior Executive Manager, Strategy, Economics & Regulation
Ms Lisa Watson, Senior Executive Manager, Governance & Corporate Services

Mr Jim Bamber, General Manager, Remote Operations

Electrical Trades Union of Australia

Mr Lance McCallum, National Policy Officer

Mr Paul Kirby, NT Organiser

DRAFT

Opening Statement tabled by Alan Tregilgas on 30 April 2014

Madam Chair, I would like to make a brief opening statement.

In support of my evidence I have provided the Committee with a short written submission. This submission puts on the record:

- the role of my Unit in implementing the Government's structural separation decision,
- certain background information relating to my Unit's establishment,
- certain details regarding the progress to date in implementing structural separation, and
- our current estimates of the cost of structural separation.

In December last year, I was asked by the Treasurer – in his capacity as Power and Water Corporation's Shareholding Minister – to take responsibility for establishing two new government owned corporations. These new corporations are to be formed from the power generation and power retail businesses being separated from PWC. I agreed to undertake this role as Executive Director of the New Corporations Unit (or NewCo for short). While I am based in DCM, I have a line reporting relationship with the Shareholding Minister, with DCM providing administrative support.

My role, and so NewCo's, is a time limited one, commencing on 1 January 2014 and concluding 30 June 2014.

This role is essentially a technical one, that of representing the interests of the Boards (and executive management) of the two new corporations prior to the legal establishment of those corporations. Until such time as the Boards of the new Corporations are in place, NewCo is responsible for making all *management* decisions essential to the separation and establishment of the new corporations.

My riding instructions from the Government are clear. Besides the usual project management objectives (of completing the separation 'on time' and 'within budget'), I am also to ensure that PWC's structural separation is achieved:

- at no inconvenience or disruption to end users,
- consistent with the fair and equitable treatment of employees,

- in a manner supportive of improving competition and efficiency through regulatory reform, and
- last but not least, in ways that involve *no net cost* to Territory power consumers.

In fact, all separation decisions are being made in support of the Government's overarching policy objective for every elements of its PWC reform agenda (regulatory reform and business improvement as well as structural separation) – namely to strengthen the Government's ability:

- to put a lid on power prices, and
- to put downward pressure on power costs.

In particular, structural separation provides the instruments essential for identifying and rooting out inefficiencies:

- by putting more focussed Boards and management teams into place,
- by making the finances of the power businesses truly transparent, so enabling greater accountability for corporate performance and a robust benchmarking of corporate costs, and
- by turning up the blowtorch on costs in ways possible only through effective competition.

In this way, we expect the actual costs of structural separation to be recovered by the new corporations *not* from their customers *but by* the improved efficiency and operations arising from the focussed governance, the financial transparency and the more effective competitive pressures *only* made possible as a result of structural separation.

Achieving PWC's structural separation in little more than six months is ambitious. This is more so because we have committed to achieving the separation within a budget which I consider to be modest given the size and complexity of the task at hand. The planned spend on structural separation is summarised in section 5 of my written submission.

Bringing structural separation to fruition relies in the main on extremely hard work on the part of a range of senior and middle managers within PWC – all of whom also have very important day jobs. In this sense, PWC is very much “in the tent” – something essential if we

are to keep separation costs down and if we are to avoid adverse impacts on business as usual operations.

For all of us involved in implementing the structural separation, more than making up for the hard work is the excitement genuinely felt about creating *both*:

- a Territory based (and government owned) *power retailer* that is customer focussed and capable of prospering even where there are other significant retail competitors; *and*
- a Territory based (and government owned) *power generator* that is confident of its long-term place in a competitive power generation market and recognised as financially self supporting.

Madam Chair, this ends my opening remarks.

Due to technical issues, recording did not commence until 9.45am

Madam CHAIR: Mr Tregilgas, I think you were half-way through (inaudible) ...

Mr TREGILGAS: I was; I think the question dealt with competition and what role competition would play. I will concede that in some parts of the Northern Territory market competition will have a limited role to play for a time. That is where regulation will continue to be significant. Regulation attempts to simulate competitive outcomes, hence the focus is on networks. It will continue to be on retail prices down the track. Competition is likely to have the most obvious impact in the Darwin-Katherine power market.

We are talking about competition, we are talking rivalry, we are not talking about private sector involvement. Private monopolies are as bad, if not worse, than government owned ones. We are looking at competition where in fact, we have more than one generator, hopefully two or perhaps three, and the rivalry that goes with that ensures prices are kept as low as they possibly can. This is because lower prices and lower costs provide competitive advantage. That mindset is missing from a government owned monopoly and that has been the case for Power and Water for over a decade.

Mr WOOD: How can you have competition if the government owned - they have got a contract for gas, so it is their gas they buy from any at a certain price. Do they actually bump the price of that gas up for themselves? So has gas got a retail on the wholesale price?

Mr TREGILGAS: I have not been privy to the gas contract.

Mr WOOD: Because it is really important because Northern Power want to come in. The Minister said in parliament that one of the reasons that there were changes to the legislation

was to allow a company like Northern Power to come to the market. They build a power house at Weddell, they are more than likely will want to have gas.

Mr TREGILGAS: Yes.

Mr WOOD: If they take gas from our existing system, the question is what price do they get? The people have paid for that gas through the taxpayers. So are we going to sell at a cheaper price ...

Mr TREGILGAS: I do not know why it would be cheaper.

Mr WOOD: How would they be competitive if they came?

Mr TREGILGAS: They are competitive because of the generation equipment that they are going to bring and they are competitive because of the management structure that they will bring. Their generation sets are more efficient, use less gas, use – cost less money.

Mr WOOD: I understand that, they are going to bring recycled diesel plants in, so then how can Power and Water be competitive with that if they have just spent millions on upgrading their generation equipment? Do they have to sell theirs and ...

Mr TREGILGAS: There are two questions there. What role does Power and Water have in that. As I see it, or as I understand it, Northern Power are wishing to enter as what we call a base load operator, which means running their generation sets flat out all the time, or as much as they can be. That by its nature only provides part of the market. There is still a question of who turns their generators on and off during the day to provide for peak as opposed to off-peak power. That is clearly an area where a dedicated generator like the new Generation Corporation will have a significant role to play in that regard. It is not the role, as I understand it, that Northern Power wishes to play. They are not proposing to build a power station that can provide the whole market, they are only providing a power station that is going to provide a fraction of the market.

Mr WOOD: I have been told a fairly reasonable fraction, but the question that I asked was, has someone done a study of what the effect of bringing a large generating company into the present market would do to the efficiency and the profitability of Power and Water, as it is today. Because that is really the question I think consumers want to know because if they take the best part of the market which is what is being said a number of times, they will go and look for the big users of power and Power and Water will get left with the rest.

Mr TREGILGAS: I can indicate today that the new retail corporation is also in discussion with Northern Power. It is the expectation of the new retail corporation that the new retail business, because it is unhooked from arrangements with the generation company is ...

Mr WOOD: How will that benefit the average householder? Power and Water will make less money, because someone will take some of their profit away. They still have to own all those facilities, all the generation plants. They still have to pay for the gas...

Mr TREGILGAS: They only have to pay for the gas that is used. Part of the problem to date is that there has been take or pay elements. There are take or pay elements in the gas contract and Power and Water has not been taking the contracted amount and so that results in a penalty. For whatever reason, the Power and Water Corporation to date has not done what it is able to do and sell that surplus gas to other potential users. It has sat on it. That has come at a cost and that cost is borne by power consumers. It is only borne by power consumers where in some sense Power and Water dominates the market. If Power and Water no longer dominates the market, , the ongoing Power and Water will have the motivation and the requirement on it from its shareholder, I am sure, to make sure that the excess gas does not come at a cost but is made available to the Territory's wider benefit.

Mr WOOD: Why has there not been an in-depth and open discussion about all these issues? This is the bit that I am finding difficult. I am reading submissions. I have got some doubts as to why we have to go down this path. I am not saying that there is not probably a good reason to break up the divisions and show where they make their money and where they are not subsidising one another and all sorts of things. People want to know the whole picture and they want to know what this will cost: what will it cost the Territory government, what will be the cost in relation to tariffs and how will profitability of Power and Water affect having to supply money to Indigenous Essential Services, all those sorts of things. Why has there not been something that we can discuss? I know you say well, today, in an hour or maybe less than one hour. Why has this sort of thing not come to discussion out there in the broader world? I did not know that Power and Water pay whether they use the gas or not. In all the documents that I have seen that is the case.

Mr TREGILGAS: Yes, well this in some sense is an aspect of Power and Water's own past that, you know, some of these issues ought to be in the public arena from a Power and Water perspective through annual reports, through communications, through a PR role that for various reasons Power and Water has not felt able to embrace or appropriate to embrace. Most of the questions that you have got have genuine answers and I repeat again that the purpose we are doing the structural separation is to put a lid on power prices and to put downward pressure on power costs. That is the only reason we are doing this.

Mr HIGGINS: Can I just ask the question; back on the shared ...

Madam CHAIR: Sorry, Hansard is working again so we can use our normal ...

Mr HIGGINS: Back on the shared resources, I know you said it is all done in the backroom and so forth, and if we get these three bodies then sharing that cost—to me that goes against having a level playing field when you are competing with outside companies. I mean part of the justification for this is to have a level playing field for anyone who comes into this market. If you get Power and Water sharing all these resources how does that conflict with that? Are they going to then pay a third of the cost each or are we going to put in true cost while we have got this sharing in place?

Mr TREGILGAS: The new corporations will pay for the privilege of purchasing these shared services.

Mr HIGGINS: Would that then be available to the private companies if they wanted to use it?

Mr TREGILGAS: Oh, they would, I am not really sure whether any private company would want to. You know, most of these private companies in fact do have access to shared services; they are part of larger groups. They have invested in billing systems and these billing system costs they have are spread across a range of markets and things like. Power and Water has just got the NT market.

Ms MANISON: So Mr Tregilgas, just to bring you a bit back to where the member for Nelson was before ...

Madam CHAIR: Sorry Ms Manison - Mr Tregilgas had you finished answering Mr Higgins' question?

Mr TREGILGAS: Sure, I think there was one other aspect of the question and it is; how is this consistent, how does a sharing of back office services reconcile with competition? It is not inconsistent because one of the successful areas of regulation in recent times has been a ring fencing arrangement and ring fencing does work at the administrative levels and Power and Water has a fairly disciplined process where information that in some senses is commercially sensitive in some areas is not made available to other parts of the business. There are ring fencing protocols which to this limited extent, are effective so that is partly how it is not disadvantageous. It is not actually providing a benefit because they are going to have to pay, these new businesses, pay for this service so in that sense there is competitively neutral and the pricing arrangements will be competitively neutral and will be subject to some oversight. So in that sense even if there was an advantage - and I cannot

think of any advantage - this new retail corporation will come to the market with still a range of disadvantages against the arrangements that are available to private sector competitors who operate in other markets, unlike this retail business.

Mr HIGGINS: Earlier you were talking about the vertical and horizontal integration. Is that actually saying the decision to amalgamate NTEC years ago with water which I have forgotten which department it was with, was a wrong decision?

Mr TREGILGAS: Oh, with the benefit of hindsight yes, but it was the way governments did things in those days and it was not only the Territory government that was putting things together back in the 80s. Although again, the businesses have grown, we have got regulatory environment that has been put in place and changed, we have policies that have moved towards more corporatisation policies and the environment has changed and for that reason probably it is a justification for an altered change policy stance compared with the arrangements in the policies and circumstances in the 80s.

Ms MANISON: So just going back a bit to the theme of the questions that the member for Nelson had, regarding competition. This morning we have heard that we cannot see any detailed cost benefit analysis of what structural separation will mean by splitting up Power and Water for ordinary Territorians. Very keen to find out - clearly NEWCO has been talking to potential competitors to come into the Territory market; just keen to find out about who you have been talking to but also what work has been done around looking at whether or not when we have a small population and a huge amount of land and distance that we cover here in the Territory including some very remote communities and so forth. Is competition going to be sustainable here in the Territory? How is it going to go given that we are not South Australia, we are not Victoria, we are not the east coast network. We have got a very small population here. We are just getting told at the moment that; "she'll be right, competition will happen, it is going to be a good thing for everybody". But we have not seen any evidence to show that, we have not seen any documentation around that, just keen to find out about the discussions with the competitors but also do they see that competition is feasible here in the Territory?

Mr TREGILGAS: The substance of those discussions with competitors are commercially confidential but I can assure you that from the generation perspective there are discussions with alternative retailers and from the retail perspective, there is discussion taking place with an alternative generator. Each of these two new businesses' interests are to encourage competition in their area of resourcing generation for retail, and in the retail end of the spectrum for generation. These are continuing.

I do not think we should show our inferiority complex as the Territory.

Mr WOOD: We're not! We are worried about Territorians

Mr TREGILGAS: We can support more than one retailer - probably three retailers in the Top End and a couple of generators, at least, in the Top End as well. We have generation sets sittings on the other side of the harbour that, if Power and Water had been more open to the possibility of active involvement by others in the market, might have been part of our Darwin-Katherine grid. That was discouraged by a board and management interested in preserving its business and, ultimately, it preserved its business to the cost of Territory consumers who are now paying more for their power than they need.

Ms MANISON: With regard to the legislation before the parliament that we are examining at the PAC, was NEWCO responsible for the drafting of that legislation?

Mr TREGILGAS: No, the legislation was drafted – Treasury is responsible for that legislation.

Ms MANISON: Are we able to go into some of the details and some of the elements of that legislation, particularly to do with the *Government Owned Corporations Act*? I am assuming you were consulted on the drafting of that legislation?

Mr TREGILGAS: Obviously, yes, I was consulted and basically support the framework and structure of that legislation. Treasury can answer the details, but if you have a general question I am happy to deal with it.

Mr VATSKALIS: Alan, a question about the competition and the – I understand what you are trying to do. However, let us say you have the generation GOC, the transmission GOC and the retail GOC. Somebody comes here to generate power, uses the network to transmit the power wherever they want they pay a fee to the GOC. You now have a power generation monopoly generating power. They say there is no alternative but to transmit the power through the network GOC. Fine. What happens if the GOC realises if they go to a private retail company they will pay less than what they pay the retail GOC? Would they be allowed to employ an outside company for the billing, retail and everything else because they are cheaper? If that happens, what will happen to our own retail GOC? Will it go up in flames because there are no clients anymore?

Mr TREGILGAS: Our retail GOC will have a long-term role in our market.

Mr VATSKALIS: How, if it is competition, if it is profit?

Mr TREGILGAS: How? There are many segments of the market that, for whatever reason, the private sector competitors do not have an appetite to deal with and, of course, I am referring to small business and residential parts of the market. I think in time the government might have to give some thought to opening up the residential and small business market to more effective competition. In the meantime, our retail business will have an important role to play there. It will continue to be the retail of last resort, a vital function within the market to make sure people are not disadvantaged either by their circumstances or by the fact that a private retailer might decide to withdraw at some stage.

Retailing is a difficult game for competitors, as it is for government-owned business. The advantage of having focused generation and retail businesses is they can start to variabilise their costs. These businesses will have trouble if their costs are basically fixed. Most government-owned monopolies seem to have most of their costs fixed. They are not as smart as some of their competitors who are able to make sure their costs are variable and, therefore, as their market share goes up and down they can actually retain their profitability, irrespective of whether they lose market share or gain it. They do not have to increase market share to increase profits. That is how these two new government-owned businesses should be, that is the mindset and the management for the culture that is required.

Mr VATSKALIS: That means that retail would have the housing residential sector. All the big companies would probably move to a private sector, like this Parliament House.

Mr TREGILGAS: That will not be the aim of the government-owned retailer.

Mr VATSKALIS: No, it will not be the aim of the retailer but it will be the aim of big business to cut costs.

Mr TREGILGAS: It will be an effective competitor - and the last thing that we want is for one segment of the market to become dominated, because once there is dominance, irrespective of whether it is private dominance or government-owned dominance, that is not to the benefit ultimately of the consumers.

Ms MANISON: I just have some questions regarding the legislation to the Government-Owned Corporations Act particularly in relation to section 53.

Mr TREGILGAS: Oh look, if you are dealing with the transfer mechanisms, I think Treasury are the ones that should deal with that. All I can say is that, that mechanism is a well tried and tested mechanism. It has been a mechanism used in all other states that have gone through a process of divestment for whatever reason. This particular process is a

process that was strongly advocated by both our legal advisers in this process and there are two legal advisers currently working with the separation process.

Ms MANISON: Okay. I suppose my concerns were in relation to the definitions around relevant entities and we were talking about this process of separating the government-owned corporations. When you go into entities there are quite a diverse range of definitions of what an entity is, including the government-owned corporation as subsidiary, a statutory corporation, a corporation as defined in the Corporations Act 2001, or any other body corporate that is owned by the Territory and the Territory. Given that the structural separation and the purpose of this legislation I would assume would be to divide the assets and the liabilities of the Power and Water Corporation as it stands to set up the new retail corp., gen corp. and whatnot. If it is all about transfer between one government-owned corporation to another and we have transfer regulations in here that give the ability to the minister to tick and flick assets and liabilities, why is there a need, as a definition for relevant entity, to go beyond just a government-owned corporation? Why have we opened it up to a subsidiary to a statutory corporation, to a corporation as defined under the Corporations Act? Why have we opened up that definition for the transfer of Power and Water assets?

Mr TREGILGAS: I think it sounds like an excessive amount of legal caution by the drafters. Power and Water does have some subsidiaries so it is legitimate in the preparation of that legislation to, I guess, contemplate the possibility that there might be some assets currently in a subsidiary structure that might need to be transferred. I am not really aware that that is the case, but I agree with your point that fundamentally it is a fairly straightforward transfer by and large between one government-owned corporation to new corporations and the listing of all the possibilities is not actually essential to, as I understand it, to this part of the legislation but I think the Parliamentary Council might have ...

Ms MANISON: It seems to open it up to ...

Mr VATSKALIS: Mine will be much shorter than, that in this legislation section 53T about ministerial direction, it states that the minister can direct the government-owned corporation to do something unlawful. Can you give me an example of what kind of unlawful thing the minister can ask the government-owned corporation to do and why it should do so, and why is it in the legislation? I have been a minister for 12 years and introduced legislation; I've never, ever seen anything like that, that the minister can ask them to do something in the words here, that it could not otherwise lawfully do. That is 53T clause 2. I have never seen anything like that.

Mr TREGILGAS: I am not sure whether it is actually saying you can do unlawful things.

Mr VATSKALIS: The minister can ask the corporation to do something they could not do lawfully.

Mr TREGILGAS: Our corporations have limited power, their powers are limited by legislation and I think what has been recognised is that, some of the things that might have to be done in a structural separation might go beyond the usual powers of a government-owned corporation.

Our government-owned corporation Act as currently drafted only ever envisaged one corporation and that is the Power and Water Corporation. It never envisaged that there would be other corporations. The amendments have been drafted to now recognise that the game is now a bit more complex than the simple world that was envisaged by the drafters of the original government owned corporation Act where there was just one.

Ms MANISON: Given the definition of relevant entities here - and it goes well beyond government-owned corporation to include corporations as defined under the *Corporations Act* - would this not be opening it up for Power and Water assets to be transferred to non-government organisations to effectively go out to a private buyer?

Mr TREGILGAS: That is certainly not the purpose or the intent of this structural separation.

Ms MANISON: With this legislation, this makes it possible?

Mr TREGILGAS: Certainly not an unnecessary or a helpful feature of that.

Mr VATSKALIS: Since you said you were consulted about the drafting of this legislation; was this legislation drafted by Parliamentary Counsel or by outside lawyers that were especially engaged for this purpose?

Mr TREGILGAS: Look I think Treasury would answer that one directly.

Mr VATSKALIS: Okay I will ask the Treasury, who is next.

Mr TREGILGAS: Yes, but Parliamentary Counsel I understand was heavily involved in the process but we did go outside.

Madam CHAIR: The government, or the former government asset management system has given the Territory a severe loss in the importance of committing sufficient time and resources to planning major changes to avoid long-term costs. In your opinion, do you have sufficient time and resources to ensure that the Territory enjoys the maximum benefits and the least long-term costs from the power and water changes that will take place?

Mr TREGILGAS: We could always use more time, but more time comes at more cost. So it is a cost-benefit analysis. We undertake cost-benefit analysis all the time as part of a bureaucracy. We do not always publish them in learned tomes, nor do they usually cost the large amounts of money that external experts charge often without a full understanding of local conditions, but we have had enough time to do the establishment process. The new boards and the new management are going to have an equal, if not larger, responsibility in ultimately delivering the benefits to the government as shareholder and to Territory consumers as we in the establishment process. They have a challenge and they will have to rise to that challenge.

Mr WOOD: When the minister introduced these bills, he said that this was going to assist corporations in becoming financially sustainable and efficient organisations. What is your belief that financially-sustainable means in the context of power and water and the words; 'is it meant to make a profit' in the sense of above and beyond what it costs, or is it meant to make a profit and still keep prices at a reasonable level? What do you see as that definition meaning?

Mr TREGILGAS: This will be a challenge for these new boards. My advice to these new boards and it is going to be written into the Statement of Corporate Intent, that we will be negotiating and discussing, is that financially sustainable does involve them earning a rate of return on capital employed, that is a reasonable rate. So it does involve a profit, but of course a profit is a return on capital.

Mr WOOD: Will there be anything in this – because there is another side to this and that is the cost to the consumer. We have NCOSS in here. Will the sustainability include keeping prices at a level that the average person can afford?

Mr TREGILGAS: Prices have risen recently, fairly significantly as you are well aware. As far as I am concerned in this process - as I said, the government's instructions to us are to use this Power and Water reform process to put a lid on prices and downward pressure on costs. This process is not about raising prices further. Customers have played their part. We now have prices approaching the average Australians pay and that is a reasonable expectation. We now have to see if our government owned power companies in the Territory are getting their costs more in line with costs of their peers in other power markets in Australia.

Mr WOOD: Why do we look at states? Fundamentally we have a business which says, 'This is how much it costs to run electricity, we need to return this much in tariffs,' whether it is industry or householders. The question really is how much of that cost has to be shared by the people who pay for it, and how much will be subsidised by the government because that is what happens presently?

Mr TREGILGAS: Taxpayers are paying a greater portion of power costs and power prices in the Territory than elsewhere. You asked me about financial sustainability; it is about getting a greater return on capital. It is seeing these businesses starting to pay a dividend.

Part of the problem Power and Water caused the government is our friends at Moody's, the international credit rating agency, takes a negative view of the government's credit rating and outlook because of the size and burden of the Power and Water debt and the fact that, by and large, the government is underwriting that debt. This is a situation other governments are not faced with. The aspiration for Power and Water and its offsprings need to be a serviceable level of debt - you have to borrow as part of a utility business – most utility businesses have a reasonable gearing rate, but at the moment Power and Water's ability to service that debt is quite minimal and it relies heavily on government support. For that reason, Moody's talks about Power and Water as not being self-supporting, and because it is not self-supporting Moody's takes a much wider view of the government's debt than should normally be the case.

The government's debt should simply be the general government debt. It should be the debt the government enters into to pay for roads, schools and hospitals not for buying power stations and things like that.

Mr WOOD: I will get back to some fundamental questions. Do you regard Power and Water as a business, or business and service – we have a bus service - we had one but it has been privatised – you provide services at a loss. I am not saying you want a big loss, but do you regard the provision of power, water and sewerage as a service?

Mr TREGILGAS: I am talking about power because that is where the structural separation is focused, and certainly power is a commodity. Like any other commodity, there is no public good element to electricity and power.

Mr WOOD: What do you mean by that?

Mr TREGILGAS: I mean you can always charge people who benefit from their consumption of power for the benefit they derive. Power consumption benefits us all. By its nature, costs can be recovered through prices and that is the nature of a private good as opposed to a public good.

Mr WOOD: That is my concern. The minister said this has to be financially sustainable and laughs at me when I say power is a human right, just like water. You cannot live without it in this day and age ...

Mr TREGILGAS: You cannot live without Vegemite.

Mr WOOD: You can, even though I had withdrawal symptoms when I was in Europe. The point is, they are some basic fundamental rights most people in the world believe in. I am concerned financially sustainable could be to maximise the business - that prices could become too high for a lot of people and NCOSS has a concern about that.

Mr TREGILGAS: Prices do not need to rise. We have scope within our cost structure to keep a lid on power prices and put downward pressure on costs. That is what this structural separation is all about, to make sure that we have got boards and management teams now focused on that and not distracted by a wide range of responsibilities, and where we have often then seen neglect certain issues. Boards and management in the past in Power and Water have often focused on some sets of issues and neglected others. This is going to be addressed by structural separation and the fact that we will now have boards and management taking a great deal of focus and interest in generation, in the generation company, in retailing in the retail company and in network service provision in the ongoing Power and Water.

Ms MANISON: Just following on from that, there have been a lot of concerns raised with regard to the separation and what is left in the monopoly GOC of Power and Water Corporation: we have got power networks, which as we know have a long, extensive history of needing significant infrastructure investment; system control. We have just seen recent issues there - water and sewerage services, which will remain there and clearly people have to pay; and, of course, Indigenous essential services which are servicing all the remote communities, supplying power, water and sewerage.

We know that as part of this we are getting told by the government that this is about putting a lid on power prices. However, when you are taking out the generation arm of Power and Water, which is more likely to be able to generate profits and bring money into the organisation, and you are taking out the retail arm as well that is more able and more capable of bringing in money and revenue into Power and Water, how are they going to keep

a lid on the prices in the monopoly GOC given they have got less opportunity to raise revenue?

Mr TREGILGAS: The most profitable part of the power business is the network business. It is a natural monopoly. It is the reason why that business is regulated. That is the reason why the Utilities Commission is given a role, although it is a reason why I think the government is thinking about moving the regulatory responsibility to the national regulator in the belief that you need a bigger and uglier regulator than we have got at the moment.

The fact of the matter is, I will concede, that generation and retail are in fact the areas where a profit is harder to make, not easier to make, and that is in fact why you need focused boards and management, because there are greater risks; when you have got competition there are greater risks. The government is planning to move to a wholesale market set of arrangements and that provides opportunities, but that provides risks. So, I think if there is concern about the profitability and the scope for financial improvement, you ought to be focused on these two new businesses rather than the existing business which continues to have a monopoly—no pressure of competition. Hopefully the board and executive management of the ongoing Power and Water will now be able to focus a bit more on these network issues, the water issues, and not be distracted by having to think about dealing with competitive pressures in the generation and the retail areas, which cause difficulties and have not been well dealt with in the past by the board of Power and Water and the executive management of Power and Water.

Mr VATSKALIS: Alan, just one question, we are splitting the monopoly into three, what happens to the debt? Is it going to be split in three? Is it going to sit with the monopoly or is it going to go to the government?

Mr TREGILGAS: No, it will be split. For competitive neutrality reasons the generation company needs an appropriate amount of debt, whether that is 60% or 50% or 40% of its assets. We are going through the process at the moment of a financial carve up and certainly the liabilities as well as the assets of Power and Water are to be split. They are not being split with the wisdom of Solomon that is evenly. They are being split appropriately and that requires some careful consideration because again we have to set these businesses up to succeed, not to fail.

Madam CHAIR: I might just say we have kept Mr Tregilgas about half an hour after his time. Maybe if there are any further questions we can just do a ...

Mr WOOD: Can I just do a quick ...

Madam CHAIR: Yes, a final quick question.

Mr WOOD: I am concerned about the generation of so-called competition. We have existing generating capacity—Power and Water has, when I say we, it is us - and you are going to introduce someone like Northern Power who will come in with a couple of generators and my understanding is that they will set up next to the existing, or in the area of Weddell, with new recyclable (inaudible) heat type generating systems which are much more efficient than what we have got.

Now if they come into the market and get gas at a cheaper price because now you tell me Power and Water can sell the gas...

Mr TREGILGAS: I do not know about cheaper, but they will get it at a wholesale price.

Mr WOOD: They will get it at a wholesale price I would imagine because they might be required to.

Mr TREGILGAS: I do not know about cheaper, but comparable with Power and Water, although Power and Water is probably entitled to a better price because it has a bigger contract and a longer term one.

Mr WOOD: They come into the market and start producing power. Power and Water will then have less efficient generating capacity because their plants are older, although the Rolls Royce ones at Weddell are fairly recent, but they are not as efficient as what Northern Power want to bring in. So they cannot compete unless they sell those generators. They are behind the eight-ball to start with and the other thing is that we do not take into account is that a lot of people have solar panels on their roofs and we know that one of the problems with solar panels on the roof is during the day you need less capacity, but at night you need the full capacity.

So who will take up the role of having full capacity? Will Northern Power not have to worry about that side of it? Will they just have to worry about whoever they supply electricity to or would they be required to take up some of the responsibility for providing a full power load in the evening? Or does all that go back to Power and Water, who then are disadvantaged because they have got to do that as part of their job?

Mr TREGILGAS: It is certainly true that the business model of Northern Power - as I understand it, and from the public announcements that they have made - is that they want to operate a base load operation and that means that they are not involved in undertaking any

peaking generation. That will fall to Power and Water. Power and Water's gen sets I think are better suited to peaking. That is part of the reason why in fact there is an opportunity at the base load level for competition. Power and Water has hedged its bets, it has not necessarily got the right mix of generation sets, but it has got generation sets that will do the peaking and the balancing part of the generation operation well. I think that will be Power and Water's niche, though the term 'niche' minimises its very important role. In a market sense, Power and Water will get paid more for the peak provision, because that is the nature of the market process. Base load is the cheapest and the lowest priced amount. Any retailer is going to have to purchase both base load and peak for its customers. They cannot simply write contracts based upon the base load and so Power and Water will have a long-term role in this market providing at least the peaks and balancing, as well as a whole raft of ancillary services that are essential to the ongoing effectiveness of the generation market.

Ms MANISON: To go back, just a question before we finish up regarding budgets. In relation to your submission you have put down that the NEWCO budget alone - that is not including Power and Water or Treasury and whatnot was about \$6.8m and that is for this financial year and next financial year.

Mr TREGILGAS: I need to correct that. That budget is the total budget for the entire structural separation and that is being incurred partly by my unit, although my unit's budget is very small – it is actually two employees, myself and my executive officer. Power and Water and Treasury are incurring the bulk of the costs, so those amounts there include all their expenditure as well.

Ms MANISON: I was curious to see in your submission that you do state that this is an estimate and will be reviewed once enabling legislation passes. I am keen to find out why that is, given that your project governance document does state that all budgets are to be prepared on a best case scenario. I am keen to find out, given that you are forecasting on the best case scenario - you have been quite open in your submission to say that is only an estimate for now and that will be reviewed. Why is that?

Mr TREGILGAS: I can only work on estimates, we do not have a crystal ball and things like that. As we get closer to 1 July we will have to make some decisions as to whether, to ensure we get to 1 July with the least risk, whether there is a need to undertake some additional work, and whether that additional work requires additional resources. It all depends on where we need to access those resources and things like that so our expenditure is an ongoing process. We are subject to approval by the Treasurer, and if we have to adjust that estimate we will have to go back to the Treasurer and explain why. He is a pretty hard taskmaster when it comes to these types of things. So, in a sense, all the recognition is that as we get closer and closer to the day one, D-Day, we will have to keep under consideration the resourcing needed to make sure we hit 1 July with a least risk scenario. In doing that we then might have to say that this will cost us more than we are comfortable with, which might mean there may be some advantage in slipping that date.

There could be a trade-off. We, in a project sense, do not want a return of this issue until we know parliament has passed the legislation.

Ms MANISON: Given your project governance document shows you have your budget development principles, but you also have tracking and monitoring principles, I assume there is a bit of documentation around that. With due respect, the submission does not go into much detail around the expenditure. Are you able to table any of those budgets, the monitoring and how that is going – any of the documentation around that?

Mr TREGILGAS: We recently prepared some answers to some questions on notice I think from you, amongst others, which go into that. I did not feel it necessarily appropriate to put it in the submission, although there are estimates of expenditure through to 31 March.

Madam CHAIR: Is there a last question?

Ms MANISON: I have some questions I did not get to put on notice.

Mr VATSKALIS: Alan, you said this morning that the Territory is really high cost in transmission because of the network. Is it because of ageing infrastructure or because of previous unwise decisions to acquire the Katherine/Darwin power line, isolated networks like the Tennant Creek, Ali Curung 150 km power line to supply power to one town? Is this what contributes to the high cost of networking the Territory?

Mr TREGILGAS: High cost is, I think, a function both of a fairly high valuation of assets, which I think the Utilities Commission has just validated, and the operating expenditure is relatively high. Operating expenditure includes maintenance so there is a range of reasons. I do not think there is any single reason. I do not think it is the age of our networks which, by their nature, are relatively young because lots of them were flattened in ...

Mr VATSKALIS: In Cyclone Tracy, yes.

Mr TREGILGAS: I think the depreciation charge is fairly high, so that is a reflection of the asset valuation as well. At some point ongoing Power and Water will need to look at its costs- the board of management of the ongoing Power and Water.

Madam CHAIR: Thank you very much Mr Tregilgas. We have questions on notice. I apologise on behalf of the committee, but if we could have answers by Friday this week – obviously, due to the constraints with the legislation coming before the House at the next sittings. Hopefully that is fine with you guys.

On behalf of the committee, thank you very much for your time today. We know we kept you over and we very much appreciate your leniency with your time. Thank you very much.

Mr TREGILGAS: Thank you.

Madam CHAIR: If Treasury can come forward now.

The committee suspended.

Madam CHAIR: Thank you for resuming after the break.

On behalf of the committee I would like to welcome everyone to this public hearing into the splitting of the Power and Water Corporation. I welcome to the table, to give evidence to the committee, Ms Jodie Ryan, Under Treasurer from the Department of Treasury and Finance, and Mr Craig Graham, Assistant Under Treasurer from the Department of Treasury and Finance. Welcome and thank you for coming this morning. We appreciate you taking the time to speak to the committee and look forward to hearing from you today.

This is a formal proceeding of the committee and the protection of parliamentary privilege and the obligation not to mislead the committee apply. This is a public hearing and is being webcast through the Assemblies website. A transcript will be made for use of the committee and may be put on the committee's website. Because of the short time before the Assembly may consider the related bills, the committee has agreed to publish the draft transcripts of this hearing before any corrections are received. If at any time during the hearing you are concerned that what you say should not be made public, you may ask that the committee go into a closed session and we can take your evidence in private.

I will ask each witness to state their name for the record and the capacity in which they appear. I will then ask you to make a brief opening statement before proceeding to the committee's questions. Witnesses, could you please state your name and capacity in which you are appearing.

Ms RYAN: Jodie Ryan, Under Treasurer, Department of Treasury and Finance.

Mr GRAHAM: Craig Graham, Assistant Under Treasurer, Department of Treasury and Finance.

Madam CHAIR: Welcome! Ms Ryan would you like to make an opening statement this morning?

Ms RYAN: Yes, thank you. I just wanted to point out firstly that Treasury's main role in this process is one of looking after the regulatory aspects in the market reform aspects of the reform process. It is a broader reform in that you have structural reform and regulatory reform together, but our main focus is on the regulatory side. I also thought before we started it would be worth going back over some of the history and I know some members of the committee have been dealing with this for a long time, but some are a bit newer. So I thought that we would go back over some of the history that we have been dealing with.

Madam CHAIR: Thank you.

Ms RYAN: So as you know the Power and Water Corporation is a government-owned utility and it is a fully-integrated service provider and it has been our main electricity provider in the Territory since self-government. Until the early 1990s the traditional model for delivering electricity and water supply across Australia was through government-owned monopoly utility institutes such as the Power and Water Authority. However, in the mid-1990s state governments began to undertake market reforms and restructure their utilities companies in order to encourage more reliable and efficient services. These reforms included structural separation of the utilities companies into component businesses, introducing market competition and establishing independent economic regulation. In recognition of the need to coordinate this economic reform nationally COAG - the Council of Australian Governments - agreed to a national competition policy in 1995. From that time all of the eastern and southern states began to pursue development of a national electricity market, what we now call the NEM, and also nationally consistent water reform.

At that time the Territory chose to remain outside of the national electricity market, however we did begin a reform program in 2000. Part of that reform program was to try and meet our national competition policy commitments. The reforms that we implemented at that time included the abolition of the statutory monopoly model for electricity supply, removal of regulatory barriers to competition in electricity generation and retail sectors, introduction of retail competition, implementation of a third-party access regime for electricity networks, and also the establishment of the independent regulator, the Utilities Commission. Their role was to regulate network prices, licence market participants and then monitor conduct.

In 2001, we continued the reforms and implemented the Government Owned Corporations Act and the Power and Water Authority became the Power and Water

Corporation. The new framework provided for the adoption of a shareholder model of corporate governance involving greater financial and operational autonomy from government and the establishment of a board of directors who were responsible for the strategic management of Power and Water and also directly accountable to a shareholder minister for financial performance. However we did keep - at that time we did not keep it as integrated entity. Since 2001 we have tried a range of reforms, administrative reforms of the business, to try and attempt to approve accountability, transparency and efficiency. That has included operational separation of the component businesses, accounting and financial reporting by business line and the introduction of a ring fencing code to ensure that Power and Water did not discriminate between competing businesses and its own affiliates.

Despite these measures Power and Water Corporation's integrated legal structure has not always translated into clear benefits for Territory consumers. The integrated structure of Power and Water dilutes incentives for it to operate as efficiently as possible, does not result in transparent financial management, and it serves as a deterrent to competition in the electricity market. Fourteen years after the introduction of these market and regulatory arrangements, the Territory remains the only jurisdiction in Australia where there is no competition in the electricity supply chain other than the small retail share that has been gained by QEnergy.

Power and Water's financial position over that period has also been deteriorating. In 2009, in response to concerns about financial sustainability, the Reeves review was commissioned. The report from the Reeves review recommended significant increases in utilities tariffs to ensure Power and Water could achieve financial sustainability. However, Power and Water continues to perform below industry benchmarks and remains heavily reliant on taxpayer funding and borrowing. As part of the 2012 mini-budget this government started a program to improve the efficiency of Power and Water Corporation. Over the year following the mini-budget we considered a range of options in the bureaucracy and put them to government to help Power and Water achieve commercial sustainability and to address our ability to attract competition into the electricity market. The outcome of this consideration, and on looking at the options, was that the government approved a broad-ranging utilities market reform program in September 2013.

The reforms aim to bring the Territory's utility provider and electricity market structure in line with the rest of the country and the reform program consisted of two interrelated work streams.

The first, from our perspective, is regulatory reform and that includes the introduction of wholesale electricity market arrangements suitable for the Territory and the adoption of relevant national electricity laws and rules. The second aspect is the structural separation of Power and Water's monopoly in contestable businesses into three government-owned corporations. Together these reforms are expected to achieve the overriding objective of

providing safe and reliable least cost electricity to Territorians. As I mentioned, our focus is on the regulatory reform.

In regard to structural separation, there are two distinct problems the separation of the monopoly in contestable functions seeks to address. Firstly, the operation of a vertically and horizontally integrated entity has proven to be administratively complex and detrimental to the financial performance of PWC. Although there are potential economies of scope and scale with an integrated ownership model, the historical financial performance of Power and Water suggests these economies have been more than offset by the additional complexity that comes from integration.

Secondly, as the Power and Water authority operates across both monopoly and contestable parts of the electricity market there is scope to engage in anti-competitive behaviour. While we have no evidence such behaviour has happened, it does provide for a perception that it could happen and has prevented competitors from coming into the market.

Structural separation involves both legal and government separation which will address many of the issues that led to the failure of our previous reforms. Legal separation involves establishment of separate corporations, separate financial information, assets and employees, and governance separation involves each corporation being subjected to separate board's directors as well as operational separation of policies, processes and systems.

The result of that is we have complete financial transparency from an owner/shareholder perspective and it ensures greater exposure to the various lines of business to external reporting requirements, external audit requirements. It also requires the formalisation of all contractual arrangements between the separated lines of business, and it is this level of transparency in separation that PWC, to date, has not been able to achieve. The separation of monopoly in contestable functions also allows the boards of each of the three GOCs to exert an increased degree of specialisation in their particular areas. This should also lead to productivity and efficiency gains over time.

Given to date accounting separation has not been achieved by Power and Water, legal separation alone would still see a single board faced with multiple competing priorities. It was considered that structural separation was the best option to achieve what we wanted - financial transparency - and what the consumer wants, which is efficiency. It also increases the prospects for competition in the Territory's electricity generation and retail markets.

One of the consequences of the existing arrangements we have is all Territory households – taxpayers, not necessarily the users directly of electricity - are bearing the costs of an inefficient utility sector. That is through the need for government to be the

primary funder of the utility's infrastructure and services and diverting resources away from other core government responsibilities such as education, health and police. Further, having access to efficient utility services is essential input for industry and industries will not come to the Territory and develop in the Territory unless they have access to the most efficient electricity services.

Although we remain a small market - that has been raised this morning - compared to other jurisdictions there are now technology improvements that mean economies of scale are no longer the only justification for retaining a vertically integrated system. There is also the fact a degree of investment uncertainty continues for new competitors looking to establish if they think there is one entity and it can act anti-competitively. Therefore, our view is that regulatory and structural reform in the utilities sector is in the longer-term economic interests of the Territory.

Thank you.

Madam CHAIR: Thank you, Ms Ryan.

Ms MANISON: A bit of housekeeping to start with, Ms Ryan. In relation to Treasury's role in the structural separation, was Treasury involved in the initial analysis, Cabinet submission, approaching government about the decision?

Ms RYAN: Yes.

Ms MANISON: Also the drafting of the legislation?

Ms RYAN: Yes.

Ms MANISON: In relation to that, was there any cost benefit analysis done around the decision to go forward and structurally separate Power and Water?

Ms RYAN: As Mr Tregilgas mentioned earlier, in everything we do we are always looking at the costs and benefits of undertaking any kind of project, new program or reform. We have had a look at what other jurisdictions have been doing and have been looking for some time. We are 15 to 20 years behind where other jurisdictions are at.

Internationally, this has been happening. Japan and Singapore are starting to look at it now as well, so there is a lot of information and research out there around the benefits of

structural separation, improving competition, or access to competition, and what those benefits are. We have also undertaken a look at the costs and for us the costs are relatively minimal in our view, compared to the long-term cost of not doing structural separation.

Mr WOOD: Can I just ask on that—I have seen figures that show, in America, municipal power and the generation plants have produced cheaper power than private companies, so you are saying that we are following what other places have done. Can you tell us whether the introduction of the ownership of power by private companies has actually shown benefits to the household lease in price of electricity? Is it being done cheaper than say a government monopoly would have done it and where are those figures to show that?

Ms RYAN: What you can see is that if a private provider comes in, particularly ones that come into - if competition does come into the Territory and what we are doing is putting in a structure that enables them to come into the Territory - they are operating larger businesses across Australia. They already have systems, they already have processes, they have a lower set up cost. In the case of the potential new entrant to the market they are going to, as Alan mentioned, be running generators aimed at doing the base load. They are more efficient generators so that can only be of benefit to consumers in the long-term. It will keep the costs down.

Mr WOOD: You are not likely to look at consumers in such a small market. Most of those companies will have shareholders; they will be a shareholding company; they will have their own boards that will have to be paid for; they will require a profit.

Ms RYAN: But they will be selling lower cost power to the retailer and the retailer and the retailer will be able to pass that on. Now whether that means ...

Mr WOOD: So will the person in Wanguri get that?

Ms RYAN: ... I said the power price will drop, but we do think that the increases will be lower as a result.

Ms MANISON: So given there has been some work done around that, I am assuming it would be looking at the cost-based analysis. We know Treasury loves forecasting a lot. Is there any documentation, aside from the information paper that Treasury put out to do with the structural separation that shows that analysis, that you would be able to share with the PAC?

Ms RYAN: I think it is really just the work that we have been undertaking in-house. We have put it into Cabinet submissions so obviously we have got Cabinet-in-confidence issues. We have not gone out and paid a consultant to come up with the answer that we already know. As far as we are concerned we are Treasury. We do not like spending money, we would rather save it for other things, so we have not actually got a report that we could table to you, but the history is there. The other benefit of actually undertaking this so late is that we can see what has happened in other jurisdictions: what they have done right, what they have done wrong, and try to avoid those pitfalls and actually try to implement the best practice from what we have seen around the rest of the country.

Mr VATSKALIS: I hear what you say about the new entrant to the market who is going to pick up the base load. Now looking around the Territory, if you look at Darwin, the peak time is when everybody wakes up in the morning and prepares for work and then the peak hour again is in the afternoon when everybody comes back, the air-conditioner goes on, the television and they are cooking dinner. So there are two distinctive peaks and that happens not only in Darwin, perhaps everywhere else. For somebody to come here and say 'I will pick up the base load'; that means that person intends to use much of a muchness of power that he has to sell somewhere and to me that indicates that guy is actually targeting the big business: Defence, hospitals, big consumers. So that means that this guy, or whoever he is - and I said this guy because he is a company entity - is picking up the big energy and Power and Water Corporation will be left to pick up the residential at peaks.

Ms RYAN: In terms of the generator, the generator actually ...

Mr VATSKALIS: Is it not logical that the power business wants to pick up the base load? Why does Power and Water want to give away the goose that lays the golden eggs and pick up the real ones which inevitably will incur increases, because they have to recover their costs? If they do not have the big players, me and you and everybody else will be asked to pick up the pieces.

Ms RYAN: So in terms of the generation aspect, the generators, the power generation company and any other new generation companies, will sell to the retailers. So they will either sell to power retail, QEnergy, or anyone else that might come into the market. They sell to those people. The retailers ...

Mr VATSKALIS: So they would not have any direct access to a consumer?

Ms RYAN: No, the retailers would then be the ones that ...

Mr VATSKALIS: So where is the competition then?

Ms RYAN: Because they will be ...

Mr VATSKALIS: If it can produce the power, it sells to the government-owned corporation, the corporation does metered power to somebody else. Where is the competition?

Ms RYAN: So they will be producing power at a lower cost presumably than Power and Water can currently do. They will be more efficient, they will have lower set up-costs.

Mr VATSKALIS: Why can we copy that efficiency to a government-owned corporation then?

Ms RYAN: That would be our long-term aim.

Mr VATSKALIS: Why can we not do that now if we know what they are doing well, we know how they do it well in other places, why can we not copy their structure, the mechanisms to produce it cheaper? Why do we actually have to virtually destroy our state-owned enterprise and give the thing to somebody else because they can do it better than us, why can we not do it better? Why would we not pick up what they are doing and translate it into our operations and do it better?

Ms RYAN: By separating out the generation business, we would be hoping that it will do better, it will become more efficient and it will be competing on a better footing with the better generator ...

Mr WOOD: Only if we can afford to buy new generators because we just bought them. The two Rolls Royce that are only about four or five years old and then we are not going to get rid of them and they are not as efficient as what Northern Power are bringing in. We are in, or Power and Water are in a difficult situation to compete.

Mr GRAHAM: I guess that the idea behind competition - Power and Water have been able to make these investment decisions in the past; we are not expert, we are not electrical engineers or anything like that. As it turns out it looks like they probably have not made the most efficient investment decisions in terms of their generation plant.

Mr WOOD: It may have been a budget decision of course. The Treasurer was involved in that.

Ms RYAN: Not necessarily.

Mr GRAHAM: Not really, but what competition forces the generators to do is to make the most efficient investment in their plant and being able to sell them to a wholesale market means that Power and Water might actually be able to use their existing plant more efficiently.

Mr WOOD: Well I would be interested to know how they can. It is a set machine, it has gas and electricity comes out the other end.

Mr GRAHAM: But because of the type of the generator - they are aero-derivatives - they can be started up quickly and possibly be used at peak times. They might end up selling less electricity but they will sell that at a higher price because they will be selling at peak times.

Madam CHAIR: Ms Ryan, if there were no structural changes made to Power and Water Corporation what would their debt projections be?

Ms RYAN: I guess where we are coming from, from Treasury's perspective - and this is not new to us - we have tried numerous ways of improving the financial sustainability of Power and Water, and it is not just about putting up prices. It is actually about making sure that the costs are as low as possible. If what we have found - and we had thought in 2009 with the Reeves Review - we went through a very intense process of, structurally, what we thought was accounting separation within Power and Water, actually making sure that there was accounting separation, that each business was appropriately accounting for its own business, it was charging the other lines of business and there would be more transparency.

What we found when we got to start looking at them again through the Renewal Management Board process was that that had actually fallen away and it has not happened. We have actually tried a number of things to improve the efficiency and the transparency processes of Power and Water and we actually are of the view that structurally separating would give everyone a chance to focus and specialise on that area of activity. So you will have generation able to focus on generation, retail would be focussed on that aspect. We will still have the monopoly aspects which will still be a large business. That is why once we have bedded down this aspect we want to be putting more focus on making sure that the monopoly business also has rigorous accounting separation of their various lines of business.

Mr WOOD: Why not sell Power and Water then?

Ms RYAN: Sell Power and Water?

Mr WOOD: You can have two competitions, not uneven competitions, sell it.

Ms RYAN: So we would be selling? Are networks a natural monopoly?

Mr WOOD: No, take out the - take the generation side, why not sell it? What is the reason for keeping it?

Mr VATSKALIS: At the end of the day we have the networks so everybody has to come to us. Why do we keep something that actually loses money and is not as efficient as private business? He is right.

Ms RYAN: Oh, yes, it is an option for government. That is not the option that we put forward - we have actually - it is not the intention at the moment. We just want to ensure that structure separation so that we can get that improved accountability, transparency and improve efficiency.

Mr WOOD: And I understand that but will Power and Water be worse off? That is the question that really worries me. Will they make less money? It says they make \$450m profit. Someone has taken the nice juicy bits out of the market. Are they going to make less money?

Mr GRAHAM: But Power and Water will still be by far the largest generator.

Mr WOOD: Will they make less profit because they have a debt they have to repay? If they make less profit - for instance their other arm, Indigenous Essential Services, which is subsidised by the government, all that profit goes into Treasury. From those Treasury funds comes money to pay for Indigenous Essential Services and if Power and Water has less profit it means the government has to subsidise, in a roundabout way, Indigenous Essential Services because they have to find some extra money from the taxpayer to keep Indigenous Essential Services going.

Ms RYAN: IES is a budget issue.

Mr WOOD: Will it make less money? What is the effect on Power and Water, profitability wise?

Ms RYAN: We do not expect it to make less money. In profit, while they may get less revenue their cost should also be lower. If there is a better focus on their costs and they become more efficient their profit should stay either the same as it is now, or our expectation is it will improve.

Mr WOOD: Is there a paper to show us how you came up to that conclusion? I would be very interested to know how that works. What is the formula to show that will happen in real terms?

Ms RYAN: Any time you introduce competition - and even if other competitors do not come into the market, we have allowed competition - there will be incentive for these businesses to operate more efficiently. If Woolies set up in Darwin and everyone said, 'It is too small. We are going to walk out and leave Woolies here by itself,' you know what would happen.

Mr WOOD: We can have competition that is correct. Under existing legislation - you said that - we can have competition.

Ms RYAN: We can have competition under existing legislation, but the perception is - this is some of the people we have spoken to in the industry who want to come to the Territory - that Power and Water - the monopoly could do something to undercut them and, therefore, there is not a level playing field. By separating out the businesses, by having wholesale market arrangements in place provides the regulatory certainty that new business comes in.

From a Treasury perspective, the other reason we want competition in the market from a generation perspective particularly is someone else is investing in new infrastructure. It is not always the government having to cough up for the new infrastructure; someone else will be incentivised to invest.

Mr WOOD: I am concerned Power and Water will be on an uneven playing field and that is why I asked why not just sell it. If you want true competition just have a privatised electricity generation market. You are going to leave Power and Water to be able to produce – you have said, theoretically, it will have lower costs and still produce a higher profit. I would love to see how those figures are worked out but, from my point of view, they will make less money because they will not be able to get rid of their generators. Those generators will last quite a number of years because they can be fixed up and kept going. They are at a disadvantage from day one because they have generators they cannot replace and are less efficient than Northern Power's. The competition will be extremely difficult for them.

Ms RYAN: They may be able to stop using generators that are more inefficient.

Mr WOOD: They have to be maintained. You cannot let a big generator sit there. They are very expensive, and part of the debt they incurred was in coming up with new generating plants.

Mr HIGGINS: Can I go back a minute? It is a basic thing I have heard a lot with the split and that is we have not been able to get this accounting separation - there is one thing - and the perception by people who might want to come in that Power and Water is fudging the figures or whatever. I have heard they can do some cost shifting from one entity another, but I have never heard examples of that.

Can someone explain what they have been doing wrong that has not given you that separation? This is pretty basic question. Are they moving their labour cost from one area to another or what are they doing?

Ms RYAN: In regard to the cross-subsidisation, we do not have any evidence of that. There is a perception ...

Mr HIGGINS: It is a perception.

Ms RYAN: The other point is we do not have any evidence of that because we do not have the financial transparency to understand whether there is any cross-subsidisation. You would think if accounting separation had been done fully and was completely transparent, we would be able to say, 'You are cross-subsidising' but we cannot say it is or is not. We do not think that, but there is a possibility they could shift cost. If it was to happen you would shift cost from the generation business onto the network business. The generation business would have a lower cost of operating and would be able to charge a lower price. That is the perception of new entrants.

Mr HIGGINS: Why can we not put in place accounting practices to stop that? Is there a reason for that?

Ms RYAN: We have actually tried in the past. Since 2001 we have been trying and, as I mentioned, in 2009 we thought we had put a more rigorous process in place. The systems did not quite support it, staff moved on, there was turnover. When we looked at it in 2012, thinking that had been undertaken for the last three years, we found that in fact that was not the case.

Mr HIGGINS: When we talk about the costs of doing all of this and the previous fellow actually said that there is going to be all these backroom systems and so forth and eventually they are going to replace those, and there is a cost to doing those. What is going to stop a government in future from saying the costs are too high, they will stop the separation and pass costs on. What is in place to stop that?

When I look back with Power and Water and everything that has happened right back to NTEC - in the 30 years I have been up here, this has been a continual problem. We have change that is going to solve it. When is this one going to finish? In other words, when are we going to start to see some benefit?

Ms RYAN: That is a very good question.

Mr GRAHAM: Hopefully the benefits will accrue over time and into the future.

Mr HIGGINS: How much time? (Inaudible).

Mr GRAHAM: I mean that is like asking how long is a piece of string. The legislation prevents the retail and the generation businesses moving back together for five years and I think in Western Australia they introduced their legislation eight years ago and they are now looking at reintegrating and they have achieved - 30% of their generation market now is provided by private generators and they do have retailers actively operating in their market. They have achieved a level of competition. They are also now going back and looking at their wholesale market and saying whether that is the best model for Western Australia. That has happened over an eight-year period, I guess. I would have thought five or ten years is the time frame that you would be looking towards, because it is fairly major structural reform that we are undertaking and it will take - the benefits will accrue into the future, while the costs will be born up-front.

Mr HIGGINS: So when we say we cannot re-join them after five years, I think from memory there was - is it all of them five years or is there one in there that is a bit different?

Mr GRAHAM: No, I thought it was five years.

Ms RYAN: Five years – within the next five years. So after five years they may be brought back together again if that is the best thing for the Territory.

Mr GRAHAM: Yes, if that is an effective option.

Mr VATSKALIS: You said before what the government is doing now is wanting to increase competition, to bring benefits to consumers. The reality is for a private company to come to Darwin or to the Territory to establish a power generation facility will take a year, 18 months. We are not going to see anything until the next election. If the government changes and the new government changes its opinion we are not going to see anything, or, if government has decided to actually either gift or sell some of the current assets, let us say the Weddell Power Station, so the new entrant in the Territory can start very quickly—have you had any discussions with companies? Have you offered any incentives, for example land, equipment or offered to sell equipment?

Ms RYAN: No. We have had discussions. There have been approaches but, no, not to offer any incentives or equipment or land or anything. They have to enter in on a commercial basis. They probably do not want to buy our generation assets because they want to build their own that they understand will be more efficient. I think if they got started - it is 12 to 18 months before they are up and running, so probably we would be looking at the end of next year.

Ms MANISON: Have you consulted with companies' external to the Territory here in relation to the drafting of the legislation?

Ms RYAN: Yes.

Ms MANISON: And have you consulted with commercial lawyers in relation to the drafting of the ...

Ms RYAN: So Parliamentary Counsel has done all the internal work. We have got a consultant on who is well versed in this area and Power and Water have also got legal advice. They have also been helping out with the legislation.

Ms MANISON: Can you outline for the Public Accounts Committee which companies you have been consulting with in regard to the legislation?

Ms RYAN: So for Treasury, we have used ...

Ms MANISON: In regard to the utilities companies.

Ms RYAN: So we have used Armature Proprietary Limited to help with our legal consulting. I understand that you would have to talk to Power and Water, but I think they use Clayton Utz. I am not sure who Power and Water are using. What was the other aspect?

Ms MANISON: In terms of any utilities potential competitors that you have consulted with.

Mr GRAHAM: We have not consulted with any utilities companies on structural separation. We have consulted with utilities companies on the wholesale market design.

Ms MANISON: Okay, can you outline who those companies are?

Mr GRAHAM: Northern Power, QEnergy, I think we sent copies – the Utilities Commission did that review, they sent copies of their issues paper to the Energy Associations, Industry Associations. I think they got 14 odd submissions on their issues paper, all up on their website.

Ms MANISON: Just going back into the legislation, you will have seen I put some questions to the Chair of NEWCO before, asking some fairly detailed questions in relation to the government owned Corporations Act legislation, so Treasury have prepared this legislation?

Ms RYAN: The amendments, yes.

Ms MANISON: I have some questions in relation to 53A and B, particularly to do with the definition of a relevant entity there. Again as I brought up before, if the purpose of this legislation is to be able to transfer assets or liabilities between the monopoly GOC and the newly created GOCs, why is it necessary in the definition of a relevant entity to go into a subsidiary, a statutory corporation? A corporation as defined in the Corporations Act 2001 or other body corporate that is owned by the Territory and a Territory - given that the shareholding minister will, by regulation, be able to transfer assets and liabilities to relevant entities.

Why is it necessary to go beyond that government-owned corporation definition?

Ms RYAN: My understanding is the definition of the entity is in the existing GOC legislation.

Mr GRAHAM: No, no. These are all government-owned entities and the legislation is being – this is a generic piece of legislation. So in this legislation it is not just specific to the structural separation of Power and Water. It has been drafted in a way that has been broad and generic to give government flexibility, I guess, in terms of whatever it wants to do in the future.

Ms MANISON: Would you say that this legislation would give government the flexibility to be able to transfer assets or sell assets to organisations outside of the government?

Mr GRAHAM: Well they are all government-owned entities and that...

Ms RYAN: So this would be selling them or transferring them to other government entities which is our understanding and that allows the transfers to happen and the establishment of the new entities to be set up.

Ms MANISON: So effectively they can be transferred between those and beyond that, would there be the potential or the ability for government to be able to transfer or sell an asset from one of these government-owned corporations to a private owner?

Ms RYAN: It is certainly not our intention in this, but words to draft things generically ...

Mr GRAHAM: The intent is to just provide for the transfer of assets, liabilities between government-owned entities.

Ms MANISON: I find D in particular there, a corporation - it seems fairly loose, particularly when you go into as defined by the Corporations Act.

Ms RYAN: That is owned by the Territory.

Mr GRAHAM: That is a government. That is a Corporations Act company that is owned by the Territory.

Ms MANISON: Yes, it seems a bit loose to me in regards to it. It is just a few commas in different places, but open to a bit of interpretation.

Ms RYAN: I guess it has not been our interpretation, but lawyers interpret lots of things. Certainly our intent is to make sure that we can set up the new entities in an effective way.

Ms MANISON: Also going to the provision in 53T and ii: why is it necessary to have something there that says: ‘

Gives the ministerial directions, so the minister can give the direction may require the government-owned corporation to do something that it could not otherwise lawfully do

Why is it necessary to have something like that in the legislation?

Ms RYAN: The GOC Act outlines what a GOC can do and there might be something outside of that act that the government wants the GOC to do. Now that is already in place at the moment, so the government can issue a direction to the board.. For example, what we saw with the system black under the guaranteed service levy code, only those people who had power out for 12 hours should have got a payment, but the government has said ‘No, we want everyone to have a payment’ and issued a direction.

Ms MANISON: Within this legislation you are effectively giving the shareholding minister of the day the power, by regulation, to transfer assets and liabilities of the existing Power and Water Corporation as they see fit. It would not need to go through parliament. It would not have to go through any scrutiny; it is something that they can decide to do themselves.

Ms RYAN: To another government entity, yes.

Mr WOOD: Can I ask another broad question? You said in your opening statement we are 15 years behind the times; that does not always mean we are not on the correct path, by the way ...

Ms RYAN: No, it gives us time to look at what everyone else is doing.

Mr WOOD: That is right. Has there been a study to show real benefits to the consumer? We can talk about industry, and I am not saying industry is not important, but the average person’s concern about what the government is proposing is they will not receive any benefits. In fact, if Power and Water’s profit decreases the logical thing is they will increase tariffs to make up for lost income. It will take a long time to bring in these efficiencies, but has there been a study to compare the prices under private ownership of power compared to if it was operated by an efficient monopoly?

We keep saying governments cannot be efficient. Why not? Governments do not have to have shareholders; we are the shareholders. Governments do not have to have a board of

directors on a few million dollars a year. Can someone show me there has been a benefit by privatising power in Australia?

Ms RYAN: There have been studies done.

Mr GRAHAM: I think there have been many and various studies ...

Mr WOOD: Not from the industry by the way, by some independent body?

Mr GRAHAM: I think there have been academic studies. I think there have been many different studies, all producing conflicting results based on whatever assumptions that are used, whatever data sets are used, how they have defined productivity and efficiency and how they have measured changes and prices over time. For every report you find that says privatisation is good, you will find one that says privatisation is bad.

Mr WOOD: If this was a single business in Darwin you could call it a monopoly - not many people run big power plants - but why can you not run a government monopoly in an efficient way? The Auditor-General looks at things, Treasury looks at things, the media looks at things; we have a whole range of checks and balances and you might say we have a board. You might say the board was not doing its job. The previous speaker said, more or less, they did not do what they should, and I will not get into that argument. Why is it you cannot run an efficient government monopoly when it comes to power?

Mr GRAHAM: I think the history and evidence has shown us without a profit motive and forces of competition and rivalry, the incentives for management to operate the business in the most efficient way are not there.

Mr WOOD: We have the Utilities Commission that was set up to ...

Mr GRAHAM: Yes, but again there are issues with that. It is very costly to regulate monopolies and to impose benchmarks on them and things like that. They can gain those benchmarks. The incentives can be perverse, but that is not to say it is not possible. I am not aware of anywhere it has been done.

Madam CHAIR: Sorry, can I interrupt you? Ms Ryan, you said nationally this reform has been happening over some time and now we are in a position where we want to move forward. What are the implications for the Territory if we do not go down this road?

Ms RYAN: If we do not go down the road - there are both aspects. The regulatory reform and the structural reform are two issues. If we do not go down the path of the regulatory reform implementing wholesale market arrangements we will not have competition in the Territory. History shows - and we all know - competition can only be good for consumers. It forces prices and costs to stay down.

If structural separation does not happen Power and Water will continue as it is. Yes, we will monitor and we will try to enforce greater financial transparency in accountability but, inevitably, with a company that has both monopoly and contestable businesses, you have got different aspirations, you have got different incentives of those businesses. It is hard for one entity, one board, one executive to actually make sure that they are appropriately taking each of those businesses forward in the direction they need to go. So I think you would find that we would just stagnate and Power and Water would continue on as it is.

Alan mentioned Moody's and we meet with Moody's every year. Every year they are worried about Power and Water, and increasingly worried. So the large reason that the Territory is on a negative outlook at the moment is because of the rising debt in Power and Water and the rising need for government to subsidise Power and Water. Power and Water should be, to the extent it can be, self-supporting.

Mr WOOD: If government sold Power and Water tomorrow, and a private company bought it, would they run ...

Ms RYAN: The whole business?

Mr WOOD: The whole business, yes.

Ms RYAN: We would have to pay somebody.

Mr WOOD: Would they make three boards or would they put in a smart fellow, a manager, who did all the things that you said Power and Water have not been doing? I am having trouble working out why we have got to have duplication of administration, which we will have, and duplication of boards. We will have CEOs for a very small company really. In Australian terms Power and Water is not a big company. There are a lot of other companies bigger. If a private company took it over, would they not just set up a management structure which did all that without having to have boards, boards and boards and administration and administration?

Ms RYAN: If one private company took it over you would not have structural separation, you would have ...

Mr GRAHAM: And you would not have competition.

Ms RYAN: You would not have competition.

Mr GRAHAM: You would have a private monopoly.

Mr WOOD: That is true, but I bet you they would want to know which parts of their departments are working profitably. That is how businesses operate and they get rid of the bits that – or they will make them profitable? They will work out which ones are making profits and they will work out where they are not making a profit.

Mr HIGGINS: If you had a private company take it over – and I own a private company – I will tell you what I would be doing. I would be pushing the price up because there is no competition.

Mr WOOD: That is right.

Mr HIGGINS: So do you agree with that?

Mr GRAHAM: Yes, you will have a private monopoly and, as Alan alluded to, private monopolies can be a lot worse than ...

Mr WOOD: Yes, but I was not really – I understand the ...

Mr HIGGINS: I would not need a management structure.

Mr WOOD: No.

Mr HIGGINS: I would just have a dictator at the top that says the price is going to triple.

Mr WOOD: That is true, but what I was trying to get at is why can you not get that structural separation without all this bureaucracy we are having? Why could someone not

step into Power and Water and achieve what you are wanting? The government gives them the power to look right into the guts – you have said you are not even sure if they do cross-subsidise. So we are going on this pretence that they might cross-subsidise therefore we need to do this. We do not even know if they do cross-subsidise.

Ms RYAN: We have put this in – what we have now and what we have tried to do is what you have described and that has been in place for the last 14 years and we ...

Mr WOOD: And so why has it not worked?

Ms RYAN: That is a good question. We think it is because it is too complex, it is too large. You say it is small. It is small, but there are small generation and retail companies on the eastern seaboard. Maybe a bigger company can come in and be a generator or a retailer and pick up their systems and processes. It does not necessarily mean that a new person has to come in and set everything up new. In terms of the administrative structure, there are costs, but we already have a general manager of generation and a general manager of retail. We will now have CEs of those two entities that will be paid slightly more, maybe. I do not know if that has been worked out yet, but it is not like it is a whole new cost.

We have got a board of Power and Water now that has had somewhere between five and seven people on it. The three corporations will have about three. So we would increase by a couple of board members, but what we think we will get is that board, the CEOs executive management, will be able to focus on their business and do the best they can for their business.

Mr WOOD: I was not advocating, by the way, a private monopoly. I was using a hypothetical.

Ms RYAN: We would probably have to pay someone at the moment.

Mr VATSKALIS: So we are actually going to a major structural reform of a government-owned corporation based on assumptions, like we believe they are cross-subsidised, but we cannot prove it?

Ms RYAN: No.

Mr VATSKALIS: We have a cost-benefit analysis, but we cannot show it to you because we have not got one. How can we go out to people and tell them, 'It is going to be for your benefit, but we cannot show you anything'? How are people going to believe that this is

going to benefit consumers in the Territory? If I was a board, a director on the board of Power and Water and I heard you saying that, 'We believe they do cross-subsidisation, but we cannot prove it,' I would be offended.

Ms RYAN: I am not saying that we believe in cross-subsidisation.

Mr VATSKALIS: But you just said before, but you cannot prove it.

Ms RYAN: No. Other people coming into the market are of the view that there would be cross-subsidisation.

Mr VATSKALIS: No, no, no, you said before when you were trying to establish new transparency in different (inaudible) can prove it. So really it is a major restructure of a major organisation based on assumptions, not evidence. We ask for a cost-benefit analysis and nobody can actually assist. 'Here is the document, here is the cost-benefit analysis, it is in black and white and it is going to be good for you.' Where is it? If somebody comes to me and says, 'We are going to sell the Health department. We really do not know what is going to happen, but we believe it is going to be good for you.' I am not blaming you, it is a government decision. It is not a personal decision.

Mr GRAHAM: I do not think it is assumptions. The mini-budget demonstrated the situation that Power and Water found itself in, in terms of its financial outlook. The 2012 SCI for Power and Water indicated that it was going to be a bit of a financial basket-case if something was not done. We put a competitive regulatory regime in place 14 years ago and we still have no competition. I think those are fairly telling, I guess, indicators that something needs to be done.

Mr VATSKALIS: Certainly, I have no problem, but show me why it has to be done. Gerry said utilities in America provide power cheaper to the consumer under private providers. If you come to us with a piece of paper, a table with cost-benefit analysis, black and white examples, I can say I understand. It does not matter which political party you have – if you come to us with a document that shows the true picture and I say, 'Yes I accept that one you might be right' - I have not seen anything. We asked Mr Tregilgas and he could not give it to us. We ask you and you say you work with other entities and other jurisdictions but do not have anything to show us. How am I going to actually tell my people this will be good for them?

Ms RYAN: The benefits that will derive from this ...

Mr VATSKALIS: Perceived benefits.

Ms RYAN: ... will be competition benefits.

Mr VATSKALIS: You think it is going to happen, because it is not going to happen yet. This budget paper we have got, legislation in place will allow for it.

Ms RYAN: We know it will have financial transparency, we know it will be able to be more efficient just by focusing on those smaller businesses and we know that will keep the lower, reduced requirement on governments to keep rising prices in order so that government on the other side does not have to subsidise the business. So those are the benefits. They are long-term benefits. We want to increase industry in the Territory, we want to grow our economy and to do that you need to be allowed to open up competition and allow others to come in.

Mr HIGGINS: At least it will have an impact on the Moody's outlook. If Moody's outlook goes bad, what is the cost to us if it improves? What is the benefit to us?

Ms RYAN: So if we go from a negative outlook and actually get downgraded, our cost of borrowing immediately goes up. So instead of spending money in delivering services ...

Mr HIGGINS: And it is not just across the borrowing is it?

Ms RYAN: ... we are spending money on interest repayments.

Mr HIGGINS: It is not just Power and Water, it is across the board.

Ms RYAN: No, it is the Territory.

Mr WOOD: Could you not give us an example in Australia where we would have a similar – that the government would own part of the power generating and private industry also owns some of the power generations. I have just come back from Europe and I asked in France what the story is there. France still has, I think - most of its power is government owned and a small amount is owned by private companies. I just want to know if you could give us any examples in Australia that I could go and ...

Ms RYAN: Queensland has three 13 private generators and three government generators; New South Wales has six private generators, seven government generators; Victoria has nine private, two government; South Australia has 11 private, one government; Tasmania has one private, one government; and us and Western Australia have government.

Mr WOOD: I will just ask a silly question because I do not really know. Do they share the network?

Ms RYAN: No, the network is a monopoly business.

Mr WOOD: Yes, okay.

Mr VATSKALIS: Again I understand Queensland has got thirteen private, three public but (inaudible) might be in Cairns or might be in Cape York because they have to have it there because nobody will go there. The same way we are meant to have one in Ali Curung and Papunya because I do not think there would be any private investor wanting to invest there.

Ms RYAN: No we expect, as Alan mentioned, competition will first appear in the Darwin-Katherine market. That is the market that people want to target. The government will still be providing uniform tariffs for the rest of the Territory. We will still be paying for IES, there is no intent to change the arrangements for IES, to change the funding for IES.

Mr WOOD: I was not saying that. I said there is less money in the coffers because if Power and Water's profit goes down, then the government has to find a bit more money to keep that subsidy for the Indigenous Essential Services.

Ms RYAN: We do not actually – we will find more money to have to do other things, it does not necessarily directly go to IES that profit.

Mr GRAHAM: Power and Water's profits are not used to fund IES.

Ms RYAN: Directly.

Mr WOOD: No, but indirectly they are. I am not saying directly, I am saying they go into the coffers and you still have to pay out of those coffers. If the coffers have gone down

because Power and Water's profits have gone down it means the taxpayer has to, theoretically, pay more money to keep Indigenous Essential Services.

Ms RYAN: If everything else stayed the same.

Mr GRAHAM: Power and Water's profits would have been going down if we had done nothing.

Mr WOOD: I am not saying we should do nothing. It is a matter of which way we should be going.

Mr HIGGINS: Our interest bill would be going up because of the Moody's downgrade. It is a bit of a catch-22. The argument we would have less money for IES is exactly the same argument as you use with Moody's, but in the opposite direction.

Madam CHAIR: Ms Ryan, the information paper notes the government has committed to the electricity markets in Darwin, Katherine, Tennant Creek and Alice Springs becoming subject to relevant provisions of the national energy laws and rules and the jurisdiction of the Australian Energy Market Commission and the Australian Energy Regulator. Can you explain what the form of that commitment is and what analysis of the NT Energy market informed that commitment?

Mr GRAHAM: We are looking at adopting the national electricity laws for the economic regulation of networks. That is on the principle the national regulator is much better resourced than our own local regulator to regulate our networks. It has a lot more expertise and a lot more resources available to it and the AER, the Australian Energy Regulator, regulates networks in the national energy market. It is a much larger and well-resourced entity. The Commonwealth is interested in us doing that because it would mean the Northern Territory would then have nationally consistent laws.

That is also one of the arguments for encouraging competition because electricity generators or retailers that operate in the national electricity market, or operate in other states, would be able to set up in the Northern Territory and not have to become familiar with a totally different set of law and rules. We first looked at that in 2006 and did some work around what that would mean for the Northern Territory. That work is informing the decisions we are making now.

Madam CHAIR: Thank you. Are there no further questions?

Mr WOOD: It might sound like a backward question, but the Utilities Commission's job was to make sure the network area running as a monopoly would not act as a monopoly, yet you talk about bringing in the Australian Energy Market Commission instead of the Utilities Commission. Could they have acted in that role for the three divisions that presently exist to do what you hoped Power and Water would have done over the last 14 years? That is, made them operate in an efficient manner so they were not operating as a monopoly and you could see how they were operating.

I assume we have a Utilities Commission to make sure the network does not operate as a monopoly. Mr Tregilgas said that was not necessarily done that well, but could you not have the Australian Energy Market Commission keeping an eye on those three divisions and we continue down the path we are?

Mr GRAHAM: It cannot because under its legislation it can only regulate entities that are separate. It cannot regulate a network provider which is also a generator. It cannot do that under its own legislation.

Mr WOOD: A GOC would give that separation? There is no other form of legally separating a division without going down the path of a GOC?

Mr GRAHAM: Not really.

Mr WOOD: That means there might be.

Mr GRAHAM: There are various forms of legal separation. You can have a parent company and things like that, but my understanding of the national law is they have to be legally separate.

Madam CHAIR: Ms Ryan, as a result of the government's structural reform announcement APA has announced a feasibility study into connecting the Northern Territory's gas pipeline to the rest of the network in southern states. If this happens, what will the effect on the Northern Territory economy be?

Ms RYAN: I am not really sure how that relates to the structural reform. That would open up our gas markets. I presume we would be able to be incentivising people to explore and try to buy new gas fields. It would not necessarily relate to the Power and Water structure.

Madam CHAIR: It would not increase competition?

Mr GRAHAM: Yes, it could facilitate wholesale market competition, and more available sources of gas can encourage new entry by generators, can encourage competition between gas providers, which would put downward pressure on gas prices. That would help competition.

Ms MANISON: Just going to the cost that Treasury has incurred due to the structural separation, given you would have been working on this for some time before 1 January with your own internal staff and utilising some consultants by the sound of it as well. To date how have you got on with this?

Ms RYAN: To date I think it is \$335 000 we have spent I think. We actually got additional funding as a result of the first Cabinet decision of \$1m over the two years to do this and at this stage it looks like we will be spending about \$600 000 this financial year.

Ms MANISON: And just a question in relation to the financial transparency, given that for some time the monopoly GOC is going to be providing shared services to particularly the power retail corporation. Will that still be able to be fenced off and financially transparent?

Ms RYAN: Absolutely. So what will happen is that the ongoing Power and Water Corporation will charge the new corporations for whatever services they have to provide and you will be able to see that in the statement of corporate intent I would think.

Mr GRAHAM: And that would need to be done through arms-length contracts, service level agreements.

Mr RYAN: At the moment they have got informal contracts between some of the bits of the business but they will actually have to formalise all of that into proper contract arrangements.

Mr VATSKALIS: Will this charge be subject to GST?

Ms RYAN: What, sorry?

Mr VATSKALIS: Will charges, from one corporation to another be subject to GST?

Ms RYAN: I am not sure of the Power and Water's GST arrangements, sorry, Kon.

Mr VATSKALIS: Because if they are we would pay an extra 10% on every transaction between government-owned organisations.

Ms RYAN: With other government entities, the GST is refundable, I am not just sure of Power and Water's arrangements.

Mr VATSKALIS: If this is actually operating a government-owned corporation on commercial grounds in order to attract competition. Can you find out and please let us know about it?

Ms RYAN: Sure.

Mr GRAHAM: I would presume that one would pay it and the other one would receive the benefit of it at the other end so effectively to government, the end result is nil.

Mr VATSKALIS: Well, let us find out about it because my suspicion is that because it is goods and services and there is a commercial basis, it may attract GST.

Mr HIGGINS: I pay GST on services provided to me, so I am paying them (inaudible) 10% but I then get the 10% back because I claim it and am entitled to it.

Mr VATSKALIS: Because you are entitled to it.

Madam CHAIR: We can take the question on notice and if Treasury could have the answer by Friday that would be very much appreciated, just due to our time situation there.

The splitting of Power and Water Corporation can be seen as a step in implementing the Industry Commission's 1991 recommendations on energy generation and distribution and the consequent COAG competition policy agreements. To what extent is the Northern Territory obligated to split up Power and Water in order to comply with the national agreement?

Ms RYAN: So part of what we did in 2000 was to meet our competition policy requirements. What we are doing now is taking the next step and making sure that we are nationally consistent, that we have the nationally consistent laws and rules and that we have our wholesale market arrangements in place. But the national competition policy program that was in place in the Commonwealth government in the 90s - that is actually completed.

Mr VATSKALIS: Is that the one that applies to the national network? Because we are not part of the national network.

MR GRAHAM: No, so we are still outside of the Australian energy market brand, but if we elect to do this and adopt national laws and rules, it would allow us to become part of the Australian energy market agreement.

Mr VATSKALIS: Have we got a cost-benefit analysis to do that? Western Australia is not doing it.

Mr GRAHAM: No, that is right.

Mr VATSKALIS: There must be a reason for that, so why are we doing it?

Mr GRAHAM: Because Western Australia, I guess, has a completely different wholesale market to what applies in the Territory. We do not have a wholesale market yet so we are looking at setting one up. If we have nationally consistent laws and rules I guess it makes it. Again I allude to my earlier point that electricity operators, or electricity suppliers, that operate in the national electricity market would have, I guess, less uncertainty about coming to the Northern Territory. They would be coming to a jurisdiction that has national laws and rules that they are already operating under.

Mr VATSKALIS: But Craig, they have no problem in Western Australia and they are not part of the national network. Why do they have concerns coming here?

Mr GRAHAM: Because as I said at the moment we do not actually have a wholesale market ...

Ms RYAN: At all.

Mr GRAHAM: ... at all. We rely on a bilateral contract and we have our own laws and rules that are nothing like what applies in the NEM or Western Australia.

Mr WOOD: Can I just ask then – what worries me is that Power and Water could be left – from its point of view it will not be competitive. You are going to take – it is a small market, the people who can tick off the best of the market will take it and Power and Water will be trying to operate with generating capacity that is less efficient. This is not because, necessarily, it was less efficient at the time they bought it; it might have been the latest for all I know, and they are left to run a power system. I am not sure where the competition from

their point of view will be except it might be – they have cut it up into nice little clear divisions where you can clearly see transparency. I am really concerned that Power and Water will be well behind the eight-ball, because they are not competing on a level playing field. You might say they have all got generating plants.

They have had to operate within the constraints of whatever they had to operate within and bought generating plants what they – for instance, we know that the generating plants at Channel Island were both operating on diesel and gas, so they were not as efficient as the Rolls Royce models at Weddell which are very highly efficient, but not as efficient as Northern Power which has recyclable heat. So they have got to live with generating systems they have got because they cannot really afford to – who is going to buy them? Anyway, they would be second hand generators, and they have got a lot of debt. I do not think they really want to be buying generating equipment at the moment.

So will they not struggle to be competitive because of ...

Ms RYAN: So what – I am just struggling to – do you want us to ...

Mr WOOD: Well, you say ...

Ms RYAN: The alternative is to maintain Power and Water Corporation operating inefficiently and us subsidizing, so what ...

Mr WOOD: Yes, I know ...

Ms RYAN: ... is the issue with Power and Water Corporation ...

Mr WOOD: Well, you are saying that competition – I am not sure that it is. Like Woolies and Coles, they can compete because they are pretty well on the same level and they know how to – they can compete against one another. Power and Water have got legacies attached to them, right?

Ms RYAN: Absolutely.

Mr WOOD: So how do they really compete with companies that come in with brand new equipment, who do not have to worry about the network, who do not have to worry about other things? Is that real competition or is it one-sided competition?

Ms RYAN: For the benefit of Territory consumers though, Territory consumers should be allowed to – all consumers, residents, new industries – have access to the most efficient, lowest cost electricity.

Mr WOOD: But will that happen?

Ms RYAN: If Power and Water cannot compete ...

Mr WOOD: Will that happen? Is Northern Power going to supply householders? That is a fundamental question. Are they going to come in and want to ...

Ms RYAN: If they cannot do it and it does not happen then Power and Water remains as it is.

Mr WOOD: So for the average consumer competition is not going to make any difference. In fact, it could even mean that tariffs might go up to recover less profit.

Ms RYAN: No.

Mr GRAHAM: Power and Water will still own most of the generation stock in the Darwin-Katherine system. So they will still have to compete and will still be able to sell base load and they will also own the peaking plant.

Ms RYAN: Which is more expensive.

Mr GRAHAM: Yes, so ...

Ms RYAN: That electricity is more expensive to sell.

Mr GRAHAM: So the wholesale market will just mean that Power and Water will have to use their system plan more efficiently than how they have had to use it in the past. They will have to. With the wholesale market will be introduced a thing called economic dispatch, which is where the market operator sends out the cheapest, lowest cost generators first and as load increases they bring on the higher-cost generators until you get up to the peaks and then that is when the high-cost generators sell into the market.

Mr WOOD: Who is your wholesaler?

Mr GRAHAM: Who is the wholesaler?

Mr WOOD: Yes, who would be the wholesale electricity provider in the Northern Territory?

Ms RYAN: The wholesale market arrangements allow for the generators to sell into retailers. So the retailers will be able to get the lowest cost generation.

Mr WOOD: I always wonder in a small market, if you have got a wholesale price, why that is not the retail price. Someone is making a ...

Ms RYAN: It is not about a wholesale price.

Mr WOOD: I know.

Ms RYAN: It is a wholesale market.

Mr WOOD: Yes, I know, but in a small market someone is making a bit of cream in there. That is simply you have got the gas, for instance, at this price. Why are you selling it at this price which keeps the price of electricity up? Why are you not just selling it at the wholesale price for a small market?

Mr GRAHAM: I guess the wholesaler needs to earn a return.

Mr WOOD: Yes, I was trying to find out who the wholesaler was.

Mr GRAHAM: I'm not sure I understand the question.

Mr WOOD: Well, is Power and Water the wholesaler?

Mr GRAHAM: It is the generator.

Ms RYAN: The generators are the wholesaler.

Mr WOOD: Yes, but technically in a monopoly that should not exist. You should not be a wholesaler, you just should be a supplier of electricity based on the cost of producing the electricity, but by making him a wholesaler you build in an extra price.

Mr GRAHAM: Yes.

Mr WOOD: You build in a wholesale price and a retail price and there is a bit in there that ...

Mr GRAHAM: But even if it is an integrated business, each part of that business, each part of that supply chain needs to be able to earn a return, or if you just have the profit all on the top and just have it at the retail level because it is that profit that is used to reinvest in the infrastructure.

Mr WOOD: I am not saying they should make it private. Can you explain the gas - what is the name of the company that supplies gas from ENI to Power and Water?

Mr VATSKALIS: ENI.

Mr WOOD: No, not ENI.

Mr HIGGINS: OPA.

Mr WOOD: No, the gas unit. I thought Power and Water would buy gas directly from ENI and what you had is the ...

Mr HIGGINS: While he is looking for that – the Utilities Commission told the Committee on the Northern Territory's Energy Future, which I chair, that one of its key regulatory priorities for the Territory was implementing a consumer protection regime for both small and large electricity consumers in the Territory. The commission further stated this is one area where the Territory contrasts with other jurisdictions. Many of the basic consumer protection provisions seem to be absent here. The Northern Territory Council of Social Services has, in its submission to this inquiry, called for consumer protections to accompany any disaggregation of Power and Water. Are you aware of the commission's NT cost concerns about the lack of consumer protection in the Territory? Is improving consumer protections a priority for the government as it seeks to increase competitions in the market? What is being done to improve protections for both large and small electricity consumers?

Ms RYAN: Moving to the national laws and rules will provide the same level of consumer protection that exists on the eastern section.

Mr GRAHAM: One thing that exists in the national market is the National Energy Customer Framework. Prior to that all states had their own consumer protection laws, but under COAG they have agreed to set up a national one. If we move to the national electricity market that is one of the things we would look at.

Mr HIGGINS: The protection laws at the moment - I did two years as a Commissioner of Consumer Affairs here. Is it covered under the Consumer Affairs Act?

Mr GRAHAM: That is right, yes.

Mr HIGGINS: If we go to this system we will fall under a different act?

Mr GRAHAM: Yes. At the moment generic consumer protection laws apply. If we adopt the national laws then we would have an energy specific set of consumer protection laws.

Mr WOOD: A point on that question, it was called gas purchasing. It is one of the service responsibilities of Power and Water. Do they also make a profit? Are they a business?

Ms RYAN: The gas purchasing is within Power and Water and it is responsible for contract management with ENI for the gas we buy from ENI.

Mr WOOD: Is it a wholesaler, the gas purchasing unit?

Ms RYAN: It manages the contracts for Power and Water Corporation.

Mr WOOD: If Northern Power came along and said it wanted gas ...

Ms RYAN: If Northern Power said, 'We want gas' and they decide to go to Power and Water and ask for their gas, then that unit would be responsible for negotiating with Northern Power.

Mr WOOD: That is where you get the wholesaler gas rate, I presume?

Mr GRAHAM: Yes.

Mr WOOD: Right, thank you.

Madam CHAIR: If there are no other questions we will let you go back to work and enjoy the rest of your day. On behalf of the committee I thank you very much for answering all our questions, taking questions on notice and committing your time today. Thank you very much.

The committee suspended

The draft transcript of the hearing in relation to the Inquiry into Management of ICT Projects with the Department of Corporate and Information Services is not yet authorised for publication.

Madam CHAIR: On behalf of the committee, I welcome everyone to this public hearing into splitting the Power and Water Corporation. I welcome to the videoconference Ms Kate Farrar, Managing Director of QEnergy. Thank you for coming before the committee. We appreciate you taking the time to speak to the committee and look forward to hearing from you today.

This is a formal proceeding of the committee and the protection of parliamentary privilege and the obligation not to mislead the committee apply. This is a public hearing and is being webcast through the Assembly's website. A transcript will be made for use of the committee and may be put on the committee's website. Because of the short time before the Assembly may consider the related bills, the committee has agreed to publish the draft transcript of this hearing before any corrections are received.

If at any time during the hearing you are concerned that what you may say should not be made public, you may ask that the committee go into a closed session and take your evidence in private. We are more than happy to do that.

I will ask each witness to state their name for the record and the capacity in which they appear. I will then ask you to make a brief opening statement before proceeding to the committee's questions.

Ms Farrar, could you please state your name and the capacity in which you are appearing?

Ms FARRAR: Kate Farrar. I am the Managing Director of QEnergy. QEnergy is an electricity retailer with a licence in the Northern Territory as well as customers throughout the National Electricity Market.

Madam CHAIR: Thank you. Would you like to make an opening statement?

Ms FARRAR: Yes, I will.

Madam CHAIR: Thank you.

Ms FARRAR: Thank you very much for giving me the time. QEnergy and I both welcome the moves being made by the Northern Territory to deregulate further the electricity market. As I noted, QEnergy is an electricity retailer and has had a licence in the Northern Territory for some years now. We are, in fact, the only electricity retailer to have consistently acquired customers competitively and to be servicing and billing customers outside of Power and Water Corporation.

I have had significant experience in the national electricity market. I have been running retailers for 15 years throughout the processes of deregulation in Queensland, Victoria, New South Wales and now the Northern Territory, and QEnergy has been operating for four years. I bring a perspective of deregulation, particularly deregulated electricity markets, to bear on the question which I hope will be useful in your consideration of these issues.

I have been writing submissions to Northern Territory Treasury and the Utilities Commission around the state of Northern Territory electricity since 2011, which is around the time that QEnergy started retailing in Darwin. QEnergy effectively is focusing on the Darwin-Katherine grid. I guess in 2012 it became apparent that with the structures that are in place currently in the Northern Territory, both in terms of the structure of Power and Water Commission and also some of the other corporate regulatory arrangements that are in place, that it was going to be very difficult for us to make significant headway. So in 2012 I did take the liberty of talking to people at that time about some of the issues that I saw. What I plan to do now is to run through the issues that I saw at that time, because I do consider that they are still relevant to the board of deregulation of the Northern Territory electricity market, but also to the question of the separation of Power and Water into its component parts.

The central issue that I saw right from the start when I commenced operations in the Northern Territory was that as a vertically integrated monopoly, Power and Water Corporation is really just not - the incentives are not in place to promote efficient competition or necessarily efficient outcomes. That is no way a disparagement of the people involved, it is just a function I guess of what happens in a vertically integrated monopoly. I should say that I for a long time - for eight years actually - worked within an energy corporation which is (inaudible) Queensland retailer and distribution. I ran the retailer at that time and (inaudible) because there is no - a huge CSO and really no competition in that area, I recognised a lot of the things that I had seen throughout the Ergon Energy process. But I guess it was even more vertically integrated in Power and Water Corporation because obviously there is generation M networks and retail from an electricity perspective all tied up together.

So the first thing that we noticed when we got into - I also should say that I went into the Northern Territory with a business partner, Power PI, who have been actively involved in the Northern Territory for decades and in my view understood the environment that we were going into. At the time that we went in, it really staggered me how much PWC generation was costing or quoting. For the quotes that we were getting from Power and Water generation, they were effectively three times the cost that we were finding were the generation costs in the national electricity market. So right from the start that did suggest that there was a problem with Power and Water generation in particular. They were either unexpectedly inefficient or there were incorrect allocation of some of the overheads or perhaps a combination of those two. I did note at the time that seven, I think, of the generators had been licenced as independent power producers. Because they had power purchase agreements which were written back to Power and Water Corporation, effectively there was no way of turning them, those independent power producers, into any sort of competitive market, given the structure that they had at the time and also that the extreme hold that Power and Water Corporation in general had over the market.

The retail market was also quite problematic from our perspective and that was not all to do with Power and Water Corporation. As you probably also know there are significant CSO, community service obligations, that go to supporting customers in the Northern Territory. Unlike anywhere else in Australia that I have seen, those CSOs extend up to very, very large customers. So you have a community service obligation out in some places. Certainly in regional Queensland there is a large CSO for smaller customers, but large customers in the Northern Territory are also price capped and price constrained. What that means is that you have lesser capability to have a competitive electricity retail market, which in turn is also not supported by this enormously high generation cost that you get from Power and Water Corporation.

So when we actually looked at it, there were only really about 20 customers that were entirely unfettered and available for retail competition in the Northern Territory. There were price caps for everybody else and there was a very high underlying cost-base because of the Power and Water generation costs which seemed to be very significantly higher.

When I was having a look at the regulatory overviews at the various markets at the time, I wanted to check that my observations were the same as the observations that other people were making and I went to one of my favourite websites, the Office of the Tasmanian Economic Regulators, the OTER website. They do a view of tariff relativities across Australia. Sure enough the Northern Territory was right at the bottom, so it was very clear from that process that the prices were being significantly capped. When you have a very uncontrolled cost-base, that obviously means it is very difficult to make anything viable work.

I articulated some reform objectives which I thought were appropriate and I still think were appropriate. The first thing is to create a financially sustainable electricity market and I think that that is one of the things that I observe to be driving this process that we are talking about today. Obviously you need to ensure appropriate security and stability of physical electricity supply, but that needs to be done in the least cost-efficient way, and drive least cost-efficient available pricing to customers. I am somebody who has grown up with markets, I am somebody who operates in markets and my background is as a cliometrician. I do prefer markets with the way of driving these cost outcomes, but I have also worked for both private and public sector organisations in both competed and un-competed markets. Certainly my own personal experience is that markets do deliver very efficient least cost outcomes and I certainly support them.

So in pursuit of those objectives I guess the suite of actions that we proposed in 2012 was particularly the focus of Power and Water generation. It was a separate company because they did not appear to be pursuing a long-term sustainable goal, even for themselves, but certainly did not appear to be supporting any sort of competitive outcome at the retail level. I have been thirty years in markets and I have never seen a market where customers wanted reform more than in the Northern Territory. Now that is through the whole process. This process has been quite a long process for QEnergy. We are a small company - we do not have masses amounts of resources - so it has been quite a commitment for us to keep going in the Northern Territory against quite a difficult regulatory environment. The one thing that really has kept me focused on thinking that there is something that should be done here and that we can participate in is the fact that we have so much of a drive from customers.

The first point was to establish Power and Water generation as a separate company. The second was to update the framework for generation competition so that other participants could come in. So there has, as you know recently, been a wholesale structure review with a proposal for potentially for NTEM. I very much support that. I put in a submission regarding that, and I think that is a really welcome and wonderful move in the right direction.

That will deal with the cost-base side of it. You do also need to look at the customer payment side and I know it sounds ridiculous to say, 'Look, you know you need to raise prices to make long-run efficient pricing work', but unfortunately when you have had

subsidised prices in place for a long time it does drive unsustainable outcomes. I think that is a part of what we are looking at here and in order to fix the unsustainable outcomes you do need to address both the cost side and the revenue side. Particularly for large customers there is a pricing order that has set price constraints in place for customers who consume more than 750 megawatt hours per annum. That has been extended twice now and it is this total subsidy for customers who are so large is not something that I have seen in other markets that we have participated in at all.

Probably over the long run you can look at bringing your electricity tariffs in line with some of the other states because you only have to look at the OTER website and see that they are substantially lower. There has been recently, obviously, some attempts to rectify that and again I think that was good, very courageous, but also the move in the right direction in terms of fiscal sustainability of the sector. When bringing all this together you want a competitive framework that, over the long run, delivers your sustainable least cost outcome. What you need is an environment supportive of competition, both at the retail and the generation level, and from a regulatory perspective and also from a customer perspective.

Government procurements in the Northern Territory are an important part of the customer base and QEnergy has certainly been very happy with our government customers, but the processes there are very important to developing a competitive framework.

I think the Utilities Commission is excellent. I think they have served you very well, and I think Alan Tregilgas is doing a really good job. I am very heartened by not just the steps taken by the Northern Territory government, but also by the people involved in opening up the market and making it something that, over time, more people can participate in to the betterment of customers.

Mr HIGGINS: Thanks, Kate, Gary Higgins here. Can I ask you the first question? Your submission to the Utilities Commission was very supportive of the introduction of competition in the electricity market, and you spoke briefly then about some of the barriers the current structure imposes. What sort of scope do you see for the development of a competitive market in the Northern Territory - you mentioned Katherine/Darwin – and what benefits would a more open market in the Northern Territory provide to consumers? You could split that into the larger and smaller consumers if you could?

Ms FARRAR: I guess the first thing to say is over the long run, unless the Northern Territory government wants to continue to put a lot of money into electricity development, into funding electricity, which is obviously a choice they may decide to make, but regardless of that, the mechanism you would use to attract private sector money and probably more efficient pricing, particularly at the wholesale level, is the introduction of a competitive framework because competition keeps you honest.

We are a company that participates in a competitive market every day and it certainly keeps us honest. We have to look at our efficient processes, we have to look at our team sizes, we have to look at our practices and we have to look at everything we do. Over the long run, competition delivers cheaper prices to customers but it also delivers better outcomes in innovation and the ability to do things differently in a lower cost way.

From the customer perspective, large customers – I assume over the long run large customers will be put on to a cost reflective tariff. At present, most large customers, by number, are not paying in full for their electricity. If the decision is made that they should pay for their electricity in full as a cost base, the way that cost base can be reduced is by introducing competition into the input supply chain.

There is already a framework for retail competition and QEnergy and Power and Water Corporation Retail do compete pretty much head-to-head on the large customers and we are happy to do that. I think it delivers good outcomes and delivers savings. I am sure we are keeping Power and Water Corporation Retail honest and I am sure they are keeping us honest. It is, I think, an all-round good process.

The thing about retail right through – anywhere you look in the electricity value chain, but particularly with large customers - is this is only a fairly small portion of the cost for large customers. Large customer costs are predominantly either network, which is regulated by the Utilities Commission and not open to competition or generation. So the key area of the supply chain that is not being competed in the Northern Territory is around generation. You have only got to look at capacity utilisation and wholesale cost in the national electricity market over the past ten years of deregulation - or 15 years of deregulation actually, the reform focus has been going on for some decades now—to be able to see just how much of a difference (inaudible), having a good healthy competitive wholesale market in place, makes to ultimate customer outcomes. So when you break it down, my view has always been that the thing that will deliver cheaper prices over the long run will be some sort of generation competition.

That generation competition cannot take place with Power and Water generation vertically integrated with the incumbent retailer. They simply will not price, you cannot price, if you are pricing for the corporation's good and you have got a retailer over there. You simply cannot price and deal with counter parties in the same way that you would if you were a stand-alone generator. Again, I would turn to the different behaviours of the vertically integrated versus independent generators in the national electricity market to see that. So just to summarise: at the large customer level, assuming that ongoing subsidies are not what the government plans to do to large customers, then introduction of competition at a retail level but more importantly at the wholesale level, will drive customer costs down over the long run.

To small customers there is obviously an open question about how far government might want to go in terms of supporting retail prices and how transparent government wishes to be about the fact that those retail prices are being supported. In terms of generation competition though, as long as the input costs are going down and generation is an input cost for small customers as well as being an input cost for large customers, the cost of that subsidy will be going down. That is going to be good for taxpayers, whether or not it is directly given back to customers via their electricity bills or just via the fiscal help at this stage.

Ms MANISON: Kate, this is Nicole Manison, the member for Wanguri. Just going back to your opening statement: you talked about pricing orders and concerns about those orders at the moment and the subsidisation around that. So, in the immediate future, as a competitor, who wants to come into the Territory market a bit more. Do you see a need for prices to go up? I think you were referring to the bigger customers in the immediate future in order, you are saying, to get a better outcome in the long run. Can you just talk me through that a bit?

Ms FARRAR: Yes, sure. There is a set of side constraints around price increases for customers consuming between 750 megawatt hours and two gigawatt hours per annum. It was initially established and then it was due to expire in mid-2013. It was extended to 1 January 2014 and then extended again to the 1 January 2015. The pricing orders for that class of customer remain in place and what that does is it limits the increases that Power and Water can put on their market rate. In some cases the cumulative effect of those increases that they have had under that pricing order - even though they are not the increases they would have had under a normal market process - has led to customers being over a market contract and they are on the market contract anyway. So we can compete with them but we cannot actively prospect to them, because we do not know who they are.

We do respond to them so we often have tenders come into us and we definitely respond and compete in those tenders. In order for a more vigorous retail electricity market to be in place and therefore the sort of long run platform for sustainability to be in place, those pricing orders do need to expire so that at least customers that are above 750 megawatt hours per annum, those customers who are consuming around \$200 000 of electricity per year - those sign constraints do need to fall away so that the market can actually start to operate the way it was intended to operate.

Mr BARRETT: You comment that the disaggregation of Power and Water Corporation's generation division into two generation companies would facilitate the introduction of competition into the market immediately. Can you explain the impact of this additional disaggregation?

Ms FARRAR: At the moment there are seven independent power producers who are currently contracted to Power and Water Corporation and then Power and Water Corporation

have their own generation assets. Should Power and Water's generation just be established as a single company? While that is absolutely a step in the right direction and I thoroughly endorse it, that alone will not establish competition in the wholesale market. It is competition in the wholesale market that does tend to reduce prices and does tend to facilitate more general competition and sustainable industry over the long- run. I think they could be split up into the IPPs so somebody who owns the IPPs and somebody who does their own generation assets - to me that would sort of make sense and what that would mean is that you effectively have two generation companies who are competing with both Power and Water retail and QEnergy to provide offers and that straight away will drive the disciplines of competition in

Break in video conference

Mr BARRETT: I just want to ask you about what you think about the threat of competition and the effect on the business model of Power and Water generation to the threat of competition, not just the opening up. Obviously if we open up the pathway for competition that does not immediately provide competition, but the very threat of competition may actually alter the way that they conduct business.

Ms FARRAR: Look I think that that has already had some impact in Power and Water generation. As you are probably aware QEnergy are participating in the Northern Territory market with Northern Generation which is a consortium looking to potentially provide gas-fired generators into the Darwin-Katherine grid. I do think that that threat of competition has already impacted on the way that Power and Water generation are pricing and potentially are acting. I guess to make it real and self-sustaining, so that over the long term it will all sort of stay there. I think more competition is better than (inaudible) competition, small pieces is better. The idea that you might have two power and water generators, then a Northern Generation, I think, genuinely provides you with the opportunity to have some wholesale competition in the market. That would be undisputed at that point.

That is probably the point that I would make.

Mr BARRETT: Would you think that the threat, or the reaction to the threat of competition that they have had, has affected them in terms of the cost side of their business or do you think that it has changed their behaviour in light of monopoly control and altering the things they are doing to maintain control of that market?

Ms FARRAR: Look, I do not think the culture has changed. A business only competes in a competitive market to the extent that the culture allows it to compete in the competitive market. Whilst some of their pricing in Power and Water generation may now reflect the threat of landed generations from someone else, I do not believe that Power and Water

generation are able to be truly competitive in the way that they think, the way that they act, the way that they price and the way that they interact with counter parties, whilst they are still part of this vertically integrated monopoly which is the total Power and Water Corporation. Whilst our dealings with Power and Water generation are good they are not, by any means, proactively facilitative of retail competition and retail competitors. That is probably something we see when we look to generators in the national electricity market who are operating in a fully competitive environment.

Mr BARRETT: Have you seen the cost side and monopoly control on the retail sector alter as a result of your incursion into this market?

Ms FARRAR: I have not.

Mr BARRETT: We have not seen any particular change in the behaviour of the retail company in its ability to compete in relation to you coming on board in this market?

Ms FARRAR: I am probably not the person to ask. The customers are probably better to ask that question of. The point I would make is we do - because of the site constraints issue QEnergy is not proactively up-marketing into the Northern Territory. However, a continuous stream of customers come to us requesting quotes and asking for offers so that latest demand I spoke of earlier is still there.

That being the case, that would suggest there is still some way to go for the offerings from Power and Water retail to being fully competitive.

Mr BARRETT: In your opening statement you said the market is showing it is keen for reform. Could you back that up with some information around why you think that is the case?

Ms FARRAR: The feedback from customers was – and we had our own dealings with Power and Water Corporation which would back up some of these cultural issues. The feedback from customers was really that Power and Water Corporation did not behave like a retailer which was customer-focused and innovative within the context of a competitive environment. A lot of that comes down to not just price – obviously, everybody has been very concerned about price. I do not think that is Power and Water retail. I think that is the generation structure or Power and Water more generally, however you cut it up. The thing we have definitely found when dealing with Power and Water Corporation over time is an unpreparedness to consider innovation around basic commercial terms which we found a whole lot easier to deal with in the national electricity market than we did in the Northern Territory.

Ms MANISON: If you were to expand your activities in the Northern Territory - we know you have spoken about wanting to see price orders removed in the first instance, but would you, as a company, be seeking any incentives or in-kind financial support from the government to allow you to enter the market a bit further?

Ms FARRAR: No, we have already established our operations with respect to Northern Territory large customers. We are already offering to large customers who are on market contracts. We know how to bill, we know how to manage the customers and we understand the market arrangements. I am excited about the prospect of reform. We have done all that funded by QEnergy, and do not particularly seek additional funding to come into the Northern Territory, no.

Ms MANISON: We know you already have some contracts in the Northern Territory. If you were to come into the Territory, would you be looking beyond those business contracts - those bigger contracts – and trying to target householders, for example.

Ms FARRAR: In the national electricity market QEnergy's business is smaller businesses. They are the ones who are really well under the subsidy threshold in the Northern Territory. We would like to be able to extend our core business into those small businesses in the Northern Territory. However, they are currently significantly subsidised and that subsidy goes to Power and Water Retail and, consequently, we cannot compete with those prices.

Mr VATSKALIS: You said you want to enter the energy market in the Territory. Do you want to be a power generator business? If so are you going to establish your own generators in the Territory and how long will it take to actually establish such a network in the Territory?

Ms FARRAR: Yes. QEnergy is an electricity retailer and we are not looking to land our own generation anywhere in Australia. However, we have been partners with Northern Generation to work through their development, which is in the Darwin-Katherine grid, as I said, and that would be – once it is closed and the close will depend on a variety of different things, including the way that the regulatory environment outplays, outworks, itself in the Northern Territory. Once it is closed that would take about 18 months to two years to actually develop the gas generation.

Madam CHAIR: I am just very conscious of time. Do we have one last question?

Mr WOOD: Yes, Kate, Gerry Wood here. I just have a question on competition in relation to generation. Any new customer coming in, like we gather Northern Power is interested in coming in to the Northern Territory with new generators – Power and Water have got existing generators which pre-date some of the more modern equipment. Do you think that it is possible for Power and Water to actually be able to compete, especially as there are really only two things or three things that generation is about? One is the price of gas, two is the wages for the workers who look after the generating plants, and three is the cost and maintenance of the generators. So if their equipment is not old, but perhaps pre-dates some of the more modern equipment, do you see that as a difficulty for government to realistically compete, unless they sell all the equipment and start again?

Ms FARRAR: I suppose the thing that I would say about that is that whilst old equipment might be less efficient, it is also heavily depreciated and consequently the sort of residual cost base that you have got for old equipment tends to be much lower. So if you look at new entrants into generation markets, there are often times they will in fact buy old equipment at cheap prices and utilise that as a way of making their way relatively cheaply into the market.

Power and Water generation has a portfolio that includes some very new kits actually. They do have some quite new generation equipment within it, which should be competitive. It should be competitive with some of the new equipment that Northern Power might put down on the ground or which is being built in the national electricity market. They also have some old equipment, I will grant you that, but as I said it should be heavily depreciated by now. My feeling is that any generation company - if you task good people with an objective of making the company work in a competitive environment you will end up, in fact, with the lowest cost, most sustainable outcome.

Ms MANISON: Just my final question: you have said before that you have been in discussion or provided submissions, for example, to the Utilities Commission since about 2011. As somebody seeking or wanting to look at opportunities in the Northern Territory market, in relation to the split up of the Power and Water Corporation, have you been in discussion with Power and Water Corporation or other agencies in the Northern Territory government to provide advice from your perspective as a retailer into what you think that separation should look like?

Ms FARRAR: I have provided advice to Alan Tregilgas through this process. I have not provided advice to the Power and Water Corporation. I did not particularly think that was appropriate as a competitor of theirs, but I would certainly be very happy to talk to anybody about my experience and share the benefit of my experience if that is helpful, but I have not done so to date.

I have spoken over time to Treasury. I have spoken to the Utilities Commission and I have more recently spoken to Alan Tregilgas in his capacity as an adviser throughout this whole process.

Ms MANISON: Thank you.

Madam CHAIR: Thank you very much, Kate. We really appreciate your time.

Ms FARRAR: Thank you.

Madam CHAIR: And I am sure we are a lot warmer than you over in Queensland right now, but thank you very much. Enjoy the rest of your day.

Ms FARRAR: Thank you.

Madam CHAIR: Okay we have Professor Quiggin, who I believe is just going to pop into that chair. Is that Professor Quiggin?

Professor QUIGGIN: Good afternoon.

Madam CHAIR: I am Lia Finocchiaro, Chair of the committee. On behalf of the committee I could like to welcome you and everybody else to the public hearing into splitting the Power and Water Corporation.

I welcome to the table to give evidence to the committee, Professor John Quiggin, Professor of Economics at the University of Queensland. Thank you for coming before the committee. We appreciate you taking the time to speak to the committee and look forward to hearing from you today.

This is a formal proceeding of the committee and the protection of parliamentary privilege and the obligation not to mislead the committee. This is a public hearing and is being webcast through the Assembly's website. The transcript will be made for the use of the committee and may be put on the committee's website. Because of the short time before the Assembly may consider the related bills, the committee has agreed to publish the draft transcript of this hearing before any corrections are received. If at any time during the hearing you are concerned that what you will say should not be made public you may ask that the committee go into a closed session and take your evidence in private and we are more than happy to do so.

I will ask each witness to state their name for the record and the capacity in which they appear. I will then ask you to make a brief opening statement before proceeding to the committee's questions.

Professor Quiggin, could you please state your name and the capacity in which you are appearing?

Professor QUIGGIN: My name is John Quiggin. I am a professor of economics at the University of Queensland. I am appearing in a private capacity.

Madam CHAIR: Thank you. Would you like to make an opening statement this afternoon?

Professor QUIGGIN: I would. You should know that I have not studied closely the operations of Northern Territory Power and Water, rather I am drawing on experience of similar reform processes throughout Australia over the past 20 years, during which time I have been engaged in analysing that process. The suggested reforms to the structure of the NT Power and Water Corporation are very similar in their spirit to the kinds of reforms that have guided the creation of national electricity markets and associated reforms including privatisation. Those two - although privatisation is not explicitly part of the proposal, I think it is fair to say that most of the advocates of this style of reform see privatisation as the logical end point. That is certainly true, for example, of the Electricity Supply Association of Australia I mentioned briefly in my submission.

My view is that the process of electricity market reform in Australia has failed to deliver on most of the key promises that were made 20 years ago when the process started and that failure reflects fundamental misconceptions about the nature of electricity markets and about the relative roles of the public and private sectors in electricity provision. What we have seen is that the price of electricity fell in real terms, keeping steady over most of the twentieth century, largely under a statutory authority model of provision. With community service objectives we expected, and very briefly realised, that we expected substantially further price declines under the reforms proposed as part of the national electricity market. In fact, however, particularly the household customers, we never saw those benefits. Real prices levelled out in 1990 and early 2000 and they have been rising steadily since around 2007. That increase has very little to do with things like renewable energy targets and the carbon price, some of the scapegoats that are sometimes put forward, very much to do with failures in the central regulatory systems and guidance to investment that is provided as part of the process of the electricity market reform.

So my view is that these reforms have been misconceived Australia-wide and need to be fundamentally reconsidered. I also want to make the observation on privatisation, because

this has been part of the process that it is commonly presented as if it is a way in which governments can get their hands on free money which can then be used to invest in non-income generating assets of various kinds, schools, hospitals, and so forth. I want to make the point that no economist believes this to be true. That includes those economists who favour privatisation for reasons of market competition and economists such as myself who are certainly sceptical of the case of privatisation in areas like electricity. Thank you.

Madam CHAIR: Professor, just before we continue, just for your benefit there is no question of privatisation. It is not part of the bill and it is not part of any plan of this government, but thank you. I will pass on to the committee for questions.

Professor QUIGGIN: Sure.

Mr VATSKALIS: How are you, Professor? My name is Kon Vatskalis and I agree with Lia. This issue, as a government, is not about privatisation. It is about splitting up the Power and Water Corporation to make it ready for privatisation later. However, I heard what you said about power prices. I recently read a report by the ABC which actually points out exactly the same thing. From 1960 to 1990 we had some of the lowest electricity prices in the world, now we have some of the highest. A lot of it had to do with the network. A lot of companies saw fit to upgrade their networks against the advice of experts because they had a guaranteed 10% profit return. Do you really believe the splitting up of a public utility like the Power and Water Corporation in the Territory will have any real benefits to consumers?

Professor QUIGGIN: I think it is fairly unlikely. I endorse the point that you raised. I think what we have seen - and this is a well-known effect in (inaudible) regulation-is with rates of return that are in excess of the true risk adjusted cost of capital, there is a very strong incentive for networks to seek large capital investments at the regulated rate. This is while simultaneously running down labour costs which are not typically commented so well and are typically able to be reduced. We have seen in my own state of Queensland, under corporatisation rather than privatisation, a run down in maintenance followed by very high cost expansion of the network that greatly increase costs. That, combined with the fact we have not really had any sensible reform of prices to take account of things like time of day pricing - I do not see that in the absence of a restructure of the entire market there have been significant benefits for householders, particularly from the introduction of retail competition.

Mr VATSKALIS: Do not get me wrong, I do not mind modernising public utilities and it is probably time for us to look at it seriously and do it. A lot of the comments we get is they are top heavy, not efficient, do not do the job properly and there is no transparency. Do you think it is better to find a new structure for public utilities rather than split them apart and start selling them off?

Professor QUIGGIN: In my view the statutory authority model that pre-dates corporatisation was substantially less top-heavy than current structures. If we look at developments- the Australian Institute has done this - the picture appears to be there have been significant reductions, indeed often redundancies in technical areas of employment, while there has been expansion in sales, marketing and managerial positions. In fact, we have seen increasing top heaviness over the course of the reform process rather than a reduction. We have seen not only expansion in the number of managers, but also significant increases in managerial salaries relative to the statutory authority period.

Mr HIGGINS: Since the economic reforms in Victoria, Victoria's electricity consumers have enjoyed the lowest prices of any state within the national electricity market, and the state is widely observed as being the most competitive market of this type in the world, with one in four householders switching their provider each year. Can you dispute the fact that these substantial savings have occurred principally because the competitive markets structure sees generators and retailers competing for consumers based on efficiency of pricing and the broader services offered?

Professor QUIGGIN: Yes, I can dispute all those things. First, Victorian electricity consumers, like electricity consumers everywhere else in Australia, have experienced substantial real increases in the cost of electricity and hot price reductions. Victorian electricity prices are in fact not ...

Mr HIGGINS: I did not say reduction, I said lowest.

Professor QUIGGIN: Sorry, I will go on. Victorian electricity prices are not the lowest in Australia. The claim commonly made is they have experienced a lower price increase than other states, but the fact is prices were raised substantially in the period immediately prior to privatisation in an effort to make the electricity assets more attractive. It is certainly true that Victoria is - by having its reform put forward as a model there is plenty of retail tune and so forth, but the benefits in cost reductions to households have not flowed through.

South Australia went through the same process and experienced very sharp price increases immediately following privatisation. I would not overstress the relative role of privatisation. The real problem has been the failure of market orientated reform as a whole, and that has been common to the whole of the national electricity market.

Mr HIGGINS: In 2011, an Ernst & Young study found Victoria's network costs decreased by 9% on a customer basis between 1996 and 2010, so do you acknowledge that the separation regulation monopoly transmission and distribution networks have also driven substantial efficiencies into the cost posed by these networks?

Professor QUIGGIN: Again you only have to look at what has happened to retail prices to realise they did not correct. Retail prices...

Mr HIGGINS: You are disputing Ernst and Young's study?

Professor QUIGGIN: I have not seen Ernst and Young's study. I am only making the point that whatever figure they have produced are belied by the fact that Victorian electricity prices have risen very much in line with those in other states. You can certainly pick and choose your starting and finishing dates to produce more favourable outcomes, but I do not think anybody is going to...

Mr HIGGINS: As can you.

Professor QUIGGIN: No one, however you pick the dates, can suggest that electricity prices have not risen substantially in real terms in Victoria as elsewhere in Australia.

Mr BARRETT: The question I have is what do you think is attributable? Where are these price rises coming from? Are they coming from a general rise in the price of factor inputs or variable cost inputs to production or does it come from the nature of industrialised sectors globally, which we have seen also in terms of roads? The price that it cost a government to make a road 30 years ago is astronomically different from the price that it costs the government to make a road now. Are we talking about just an increase in prices generally due to most infrastructure things having that same effect or is it contributable to a large extent, as you say, the whole mechanism by which those transfers happen from a statutory process to a corporatised process? I ask you the question because under the corporatised model that we have been running with in the Northern Territory we have had a shocker.

Professor QUIGGIN: Certainly in terms of worldwide trends - obviously worldwide trends are important - we have seen Australia's relative electricity costs go from being among the lowest in the world to among the highest. It is clear that problems in the Australian approach to electricity market reform have played a major role here. I emphasise again, I do not think we have seen sensible incentives for investment in distribution. We have seen that an initial run-down of distribution networks is followed by high cost investment and the impact of that has been exacerbated by rates of return, which are justified in terms of calculations for cost per corporate capital, but which in my view lead to over return of the assets. You can see that by the fact that the market value of regulated distribution assets typically substantially exceeds the actual cost to provision, which is the rate of return to capital is higher in fact than the investors require.

I would emphasise the problems in distribution, but also the problems in sequencing that we have not - for this reform process to have worked at all we really need to start with smart meters and the ability for people to manage their electricity consumption on a time-of-day basis, then work backwards to reform. Instead of which, we have gone in the opposite direction and the attempts of rolling out smart meters unfortunately have also been bungled, which has further lead to debate in this area.

Mr BARRETT: The high cost of assets that you speak of, these investment decisions that have been made, if you have a look at the numbers coming back on a lot of these investment decisions they look poor at best. In terms of these high cost assets, what kind of issue has that created in terms of the allocation of funds to poor investment being reflected in the cost?

Professor QUIGGIN: These of course regulate the assets so the corporate - the distribution companies have to justify their investments before regulators. Having been involved in the process myself, it is relatively difficult to avoid proving distribution investments which are said to be necessary to maintain the liability.

Again, it has certainly been very difficult to argue for a rate of return as low in my view would be justified. So we have just seen these costs multiplying, at the same time which I do not think we have seen adequate investment in long distance transmission.

Mr BARRETT: Forgive me, because I am young - what is the reason that the government has chosen to move from a statutory process of operating these assets to the corporatised model in the first place?

Professor QUIGGIN: This of course has been a process which we have seen across the entire utility sector which results in, I think it is fair to say, a mix at best. The expectation was certainly that we would see better customer service and greater customer satisfaction. I do not believe that has been realised on the whole. Certainly the competition will produce lower prices and clearly that has not been realised. So there was a belief going back to the 1980s and 1990s that we would see certain outcomes. Those outcomes have not been delivered, but nonetheless we have not really seen much rethinking of the issues.

Ms MANISON: Nicole Manison here. You are talking about your two decades of study in relation to what happens in electricity markets. Generally would you say that when government-owned utilities go towards structural separation, does that tend to lead down the pathway towards privatisation and sell-off of assets?

Professor QUIGGIN: I do not think there is any doubt about that. I think it is clear that if you look at, say, the website of the Electricity Supply Association in Australia it has a

checklist of what it regards as good. Structural separation is on that checklist, so is privatisation. These two things are very much a part of the same logic. Similarly if you read the reports of the Productivity Commission, there is very little doubt that these are considered as part of the same process.

Ms MANISON: Given the government's intent here in the Northern Territory is to encourage more competition and to put a cap on price increases of electricity, given the size of the Northern Territory - it is a smaller place population wise, we have got an extremely large and remote land mass - do you see that as more of a challenge or more of an opportunity for the government in achieving what it is trying to set out to do?

Professor QUIGGIN: It is certainly a challenge and obviously at the beginning of this process there was substantial hope that we would see some form of competition emerge, even in distribution. For example, Victoria chose to split up its urban distribution into a number of separate companies with local monopolies on the theory (inaudible) they might compete. That of course has not happened anywhere or in any jurisdiction.

The other point I would make is that what we have seen through the structural separation process is, in large measure - in most places where it has taken place, it has been at least partly reversed by the reintegration of generation and retailing where those two have been separated. That reflects the fact that, particularly in a poor type market the separation of generation and retail creates risks on both sides which can be eliminated by recombining generation and retail. So we have seen the so called gentailer model re-emerge in most places where it has been attempted to be separate where we tend to have (inaudible) separation of generation and retailing.

Coming to the Northern Territory I am not fully familiar with the generation side, but I would have thought that it is unlikely that there would be substantial numbers of separate generators supplying into the same parts of the grid. Now, I should say that I am not aware of the full details of how electricity generation is organised in the Northern Territory, but it seems unlikely that there is going to be a huge amount of competition on the generation side. That in turn limits the scope of competition in retail.

Mr WOOD: Gerry Wood here, Professor. Just in relation to the efficiency of a statutory authority: one of the reasons that the government is looking at breaking up the present Power and Water Corporation into three government-owned corporations is because it is claimed it is basically inefficient and this will bring efficiencies. We have had some discussions with various groups today saying why they believe that the present structure is inefficient. If you do not go down the path of competition, how can you make sure that a government-owned corporation like Power and Water is actually operating as efficiently as possible?

Professor QUIGGIN: At this point reviving the statutory authority model - which I regard as the optimal approach - is largely off the agenda, partly because of things like national competition policy. But if we observe the operations of public and private enterprises in this sector there is not a lot of difference between the public and private corporations. I will repeat the claim that is made on behalf of Victoria first is not correct and second is utterly belied by the contrary experience of South Australia, which has experienced paying some of the highest prices and some of the highest costs.

Looking at the sector as a whole what we see is, I think, that the management disciplines that were hoped would be introduced by corporatisation have largely – the benefits in terms of reduced numbers of frontline employees have largely been offset by expansion in marketing, managerial and similar ad hoc office-type operations.

Madam CHAIR: Professor, in your view how have power prices been affected by the federal government's carbon tax and other renewable energy schemes?

Professor QUIGGIN: Those numbers - I do not have the numbers to hand, I have in front of me a report from ABC Radio National which estimated the renewable energy target raised prices by around 4%, the impact of the carbon price has been similarly low. There have been very modest impacts from those two sources; they are really second order issues. I think we are seeing that from the fact price sensitive consumers, like electricity smelters, despite the impending demise of the carbon tax or carbon price and like reforms to the renewable energy target - those industries are announcing their closure because they do not expect, in my view, to see substantial reductions in input costs from electricity.

Mr BARRETT: In regard to the market characteristics you spoke about earlier, you said one of the failings of this whole process has been policy makers failing to understand certain aspects and characteristics of this market as opposed to a normal market structure. What are the characteristics you speak of and what is it we are failing to understand?

Professor QUIGGIN: First, the idea of separating generation and retail. This largely stemmed from a misperception that the wholesale - the distributor was the national retailer. Under the integrated statutory authority model that was typically how things were done since it made some sense for the same person to supply both the physical connection to your house and the billing functions. What we saw was a wider separation of generation and retail. That has largely been abandoned and we have seen reintegration of generation and retail. I think that is the first misunderstanding.

The second one is we have seen the notion of competition wavered about at times where households really do not have the capacity to manage their electricity consumption in ways

that make competition useful to them. We really needed to develop and install smart meters, get people experienced with managing their electricity use over the time of day with a range of tariffs before we can consider real benefits arising from retail level competition.

The third problem is policy makers, in setting the regulation of distribution, did not really understand distribution is not their biggest connection and the volume of usage is important. We have distribution charges which have been fixed in pro rata terms when what matters in distribution is peak usage. What we have seen is an effective subsidy in particular to how to use an air conditioner, people responded to that subsidy by moving and expanded use and that, in turn, has increased the demand on the distribution network.

All these things were misconceived and most of them reflect a measurable faith in competition as opposed to an analysis to what competition achieves.

Mr BARRETT: The user in competition you are talking about in regard to installing smart meters: could you run through exactly what the process is and how that can better equip customers to make informed decisions as to their utilisation and why that assists competition in the future?

Professor QUIGGIN: Sure, and most of this is more applicable to the national electricity market. I am not fully aware, as I say, of the details of the Northern Territory, but what you see in the national electricity market is most of the costs on the generation side, or most returns to generators arise on the relatively small number of days the entire system is operating flat out. The big cost is just to maintain enough capital stock to operate the system flat out. Those typically are hot summer afternoons, but consumers do not see any difference between the price of electricity they pay on a hot summer afternoon and the price they pay mid-morning in spring. Some of that could be handled by pricing but has not been, but the big problem is that measuring the fact it is not there to enable consumers to respond to those price changes.

Until we have that, there is no real sense in the pricing on the production side feeds through to consumers. We should have moved to those things before we started down the path of attempting to introduce things like retail competition.

Mr BARRETT: So you do not per se have an issue with competition in these market structures, we just need a better understanding of these market structures so as to utilise the positive effects of competitions effectively?

Professor QUIGGIN: That is correct, yes.

Mr WOOD: Could I just ask a question in relation to how the reforms have not made a difference, or a substantial difference, compared to having power run by statutory authorities? Is there somebody who has done a study which can actually show that is the case? At the present time I have got a figure in front of me which says the residential tariff January 2014 for Victoria is 30.16¢ per kilowatt. If I was arguing for competition, is there a way I could go and say, if that was under a statutory authority or Victoria was still being run by the—whoever it was in those days—the price would be lower or higher than that quoted for 1 January this year?

Professor QUIGGIN: What you certainly can do is look at the inflation adjusted price when we had statutory authorities and observe it is substantially lower and you can look at the predictions made at the time that the electricity market was introduced which were for further real reductions. So I think what you can certainly say is that it would be unwise to place a great deal of reliance on any market experts who are not able to give an explanation as to why things went so badly wrong.

Madam CHAIR: I am just conscious of time. Is there a final question? No?

Thank you very much, Professor, we very much enjoyed listening to you. We very much appreciate your time. It all helps our inquiry. So thank you and I am sure we will cross paths one day in the future.

Professor QUIGGIN: Thank you.

Madam CHAIR: Thank you.

We will now have Power and Water. I think you guys are all ready to rock and roll.

Okay. On behalf of the committee I welcome everyone to this public hearing into the splitting of the Power and Water Corporation. I welcome to the table to give evidence to the committee Mr Ken Clarke, the Chairman of the Board of the Power and Water Corporation; Mr John Baskerville, Managing Director, Power and Water Corporation; Mr Jim Bamber, General Manager Remote Operations of Power and Water Corporation; and Ms Djuna Pollard, Senior Executive Manager, Strategy, Economics and Regulation of Power and Water; and Ms Lisa Watson, Senior Executive Manager, Governance and Corporate Services for the Power and Water Corporation. Have I got all of you? Yes, okay, great.

Thank you for coming before the committee. We appreciate you taking the time to speak to the committee and look forward to hearing from you today.

This is a formal proceeding of the committee and the protection of parliamentary privilege and the obligations not to mislead the committee apply. This is a public hearing. It is being webcast through the Assembly's website. A transcript will be made for use of the committee and may be put on the committee's website. Because of the short time before which the Assembly may consider the related bills, the committee has agreed to publish a draft transcript of this hearing before any corrections are received. If at any time during the hearing you are concerned that what you will say should not be made public, you may ask that the committee go into a closed session and take your evidence in private.

I will ask that each witness state their name for the record and the capacity in which they appear. I will then ask you to make a brief opening statement before proceeding to the committee's questions.

Witnesses, could you please state your name and the capacity in which you are appearing?

Mr CLARKE: Ken Clarke, I am the Chairman of the Power and Water Corporation.

Mr BASKERVILLE: John Baskerville, Managing Director Power and Water.

Ms POLLARD: Djuna Pollard, Senior Executive Manager, Strategy, Economics and Regulation, Power and Water Corporation.

Mr BAMBER: Jim Bamber, General Manager, Remote Operations.

Ms WATSON: Lisa Watson, Senior Executive Manager, Governance and Corporate Services.

Madam CHAIR: Thank you. Mr Clarke, would you like to make an opening statement?

Mr CLARKE: I would.

Madam CHAIR: Thank you.

Mr CLARKE: I attend this hearing in my role as Chairman of the Power and Water Corporation. We have already discussed who is with me. Power and Water Corporation is

pleased to contribute to the Public Accounts Committee enquiry into the structural separation of the Corporation. Power and Water Corporation is closely involved in the process of transitioning to structural separation and will be of assistance to the Public Accounts Committee. Our comments relate to the operational aspects of the process. Power and Water's role is to operate within a framework set by the Northern Territory government policy. It is therefore inappropriate for the Power and Water Corporation to address the rationale for the structural separation policy decision. The same applies to the wider economic impacts.

These are not matters for the Power and Water Corporation. Rather, these are matters for the Northern Territory government and/or the executive director of NEWCO, Mr Alan Tregilgas. But as indicated earlier, Power and Water Corporation are keen to help the committee in relation to considering the operational aspects of achieving the policy objectives as they relate to the corporation by elaborating on the processes to achieve structural separation. Power and Water Corporation is well placed to do this as we are hoping to ensure there is a smooth transition to the new arrangements.

Now there is considerable interest in the cost to establish the new GOCs. I had previously indicated to the committee I thought the costs would be between \$2.5m and \$10m. This off-the-cuff comment was made in the context of earlier comments that costs would be upwards of \$100m. The cost to establish the two new GOCs will be closer to the \$2.5m estimate than the \$10m estimate.

Power and Water Corporation have a defined budget for 2013-14 of around \$2.2m and are striving to stay within it. The \$2.2m excludes some IT costs but we cannot be too definitive about the total establishment costs as these are shared between structural separation and what we need to do independently for structural separation. There may also be some costs that will be incurred in 2014-15. The cost in 2014-15 will partly depend on the choices made by the new GOCs on the scope and standard of service they want than the shared services functions PWC will be providing. PWC is implementing the structural separation program in a manner to meet the following objectives. The program is to be delivered on schedule. There is to be no incentive, no inconvenience and disruption to end users. There is to be a small transition of employees to the new entities.

The costs re structural separation are to be managed within the approved budget. There is to be no net cost to power consumers over the long-term and to support improved competition and efficiency. The Territory government has instructed the Power Retail Corp and the Power Generation Corp it will provide electricity retail and generation services respectively in Darwin, Katherine, Alice, Tennant, Yulara, Borroloola, Ti Tree, Timber Creek, Kings Canyon, Daly Waters and Elliott. All other existing service responsibilities are to remain with the Power and Water Corporation. These include water and sewerage including associated retailer functions; power networks including metering; power system control and at least until the establishment of the wholesale electricity market, gas purchasing and to a

later date that is determined by the Territory government, Indigenous Essential Services and a corporate services unit.

I would also like to acknowledge the hard-working commitment from Power and Water Corporation staff to the program. Thank you Madam Chair.

Madam CHAIR: Thank you.

Ms MANISON: Just a few questions Mr Clarke. Following on from your opening statement: firstly in regards to the budget you just discussed there, was it right to say that \$2.2m is what you budgeted for 2013-14 from Power and Water alone and that is just for this financial year?

Mr CLARKE: Yes, that is correct.

Ms MANISON: And 2014-15; do you have any preliminary figures regarding the budget or what you are forecasting?

Mr CLARKE: No we do not. But it will not be certainly nothing like the \$2.2m.

Ms MANISON: Okay, so that is \$2.2m for this year. So you just also mentioned as well that Indigenous Essential Services may be moved on from Power and Water at a later date. Is that correct?

Mr CLARKE: No, no, no, that is going to stay with us.

Ms MANISON: Okay.

Mr CLARKE: The ones that might move are the-gas purchasing, which might go to another organisation and I think also the structural separation system control once the new wholesale arrangements are in place. They might need to have a separate independent system control process.

Ms MANISON: Thank you Mr Clarke. I also note that you did say in your opening statement that clearly you are not keen to comment on decisions, policy decisions by the government who clearly have made the decision to go towards structural separation here. Clearly, given that you are chairman of the board and you are going to be left with the

monopoly governing corporation there and the businesses that run within that, has there been any cost-benefit analysis, any economic analysis, any analysis done into the outcomes of structural separation, and what it is going to mean for customers on pricing and the Power and Water Corporation going forward?

Mr CLARKE: We have not done an overall study. Most of that would be to do with the government, but we would have a good feel for what the costs for us will be. We do not know at this stage.

Ms MANISON: You are unable to provide the committee with any firm documentation, any analysis around forecasting, around prices about the economic outcomes, the fiscal outcomes for the corporation due to the structural separation?

Mr CLARKE: No, definitely things like prices - do not get me wrong. Prices for the residual corporation are set by the Utilities Commission for the networks. Government sets the price for water and sewerage. I forgot the start of the question but the ...

Ms MANISON: Do you want to see if there is some paperwork I could have tabled, Mr Clarke?

Mr CLARKE: No, and the costs - we will not really know what costs will be left with us. There are issues going on with staff, and there is a lot of work going on working out what costs will transfer from the Power and Water Corporation to the two new bodies. The sum total of those, initially, will be the same amount. Then the idea is both the two new bodies and us, the remainder, will strive to produce lowest cost.

Ms MANISON: We heard from Mr Tregilgas this morning about the work happening around the structural separation, particularly the fact we are two months away so it is very close. I understand you have had to take a lot of people offline internally to work on different business streams, which I think you discussed in your submission, in preparation for the structural separation. You will have some staff working in shared services and what not, particularly around billing and credit control, that type of area, and corporate services to support the new generation and retail corporation. It has been a big body of work and a very complex body I imagine.

Mr CLARKE: It has been quite a significant amount of work, yes!

Ms MANISON: How are you going towards a 1 July 2014 implementation?

Mr CLARKE: We have some concerns for sure. There is one area zoned as being in the red, and red for us means there is a risk there they have to fix quickly or there could be a delay. The bottom line is we are not proceeding with the 1 July start if material issues are not sorted out. Djuna is in charge of the show and they are doing a fantastic job, but it is time consuming and there is a lot of work to be done.

Ms MANISON: Are all staff affected by the structural separation aware of where they are going under the new work structures you have within Power and Water Corporation?

Ms WATSON: I am Lisa Watson. At this stage we are working through the consultation process with the new org charts for the new government-owned corporation. We have put in place a subcommittee to JCC and discussions on the new org charts took place over the last couple of weeks. We are now starting to consult with staff.

Ms MANISON: Is it possible to get those new org charts tabled for the committee?

Mr CLARKE: Yes, sure.

Ms MANISON: As part of the structural separation do you anticipate any job losses within Power and Water Corporation?

Mr CLARKE: No, the whole - this is one of the key things with this. We are seeking to say to staff essentially you will go home one night and turn up the next day and your job - nothing will have changed other than the fact you are in either power retail or power generation. A small number might have some other implication for them, but the idea is the number of staff will remain the same.

Ms MANISON: A number of staff will have their jobs varied, changed according to ...

Ms WATSON: Our ultimate goal is exactly that smooth transition for all our staff. There will be some staff within the new structures that may have different functions within their role and we will talk to those individuals, but it is limited in numbers. The majority of staff will wake up on 1 July and go to work about their normal business. They have raised with us that they just want to get on with their everyday job come 1 July and do not really care what they are called.

Mr BASKERVILLE: I have regular coffees, chats, and get around the organisation as much as I can. In particular in the generations space they are saying, 'Get on with it'.

Ms MANISON: Okay.

Mr WOOD: Can I ask what happens to your water and sewerage employees.

Mr BASKERVILLE: No different.

Ms WATSON: No

Mr WOOD: Right.

Mr BASKERVILLE: No different. Turn up on Monday and it will be the same; no change whatsoever in water and sewerage.

Mr WOOD: The operation of water and sewerage, will that be split from ...

Mr BASKERVILLE: No way, no.

Mr WOOD: No.

Mr BASKERVILLE: Still a part of Power and Water under the monopoly GOC.

Mr VATSKALIS: Which Power and Water monopoly?

Mr CLARKE: Under the ...

Mr BASKERVILLE: Monopoly GOC.

Mr WOOD: Right. It will be split from the divisions.

Mr HIGGINS: Ken, the power generation costs have never been scrutinised to the extent the power network costs have been under the Electricity Network Code. As you are aware under the code the Utilities Commission is required to set the revenues the network services provided can recover. How can you reassure the public that if power network operational

expenditure is 27% higher than its peers this does not extend to power generation or any other business?

Mr CLARKE: That it does not extend to any other – the thing with the power networks - there is a large increase there because the Utilities Commission conducts a review every five years and what they were doing there was looking, going from a period which – when does it start, Djuna, 2014-15, is it?

Ms POLLARD: 1 July 2014.

Mr CLARKE: Okay, that is the new period. They had a pricing for the previous five years they determined five years ago. An awful lot of capital expenditure had been incurred over the last five years, other cost adjustments, and so the 27% for the networks really reflects a catching up. In fact, our analysis was that it should have been quite a lot more than that, and it is really understandable in the sense that - the increase I mean, because the – I cannot remember how much was spent on capital on the networks, but following the – when was the failure at ...

Mr BARRETT: Casuarina substation.

Mr CLARKE: ... Casuarina substation. Merv Davies did that report and ...

Mr HIGGINS: 2010, I think.

Mr CLARKE: Yes, and that had a very good process for identifying all the things that had to be done. They did them and it cost a lot of money and so, at the end of the day, that is translated into that price.

Mr WOOD: In relation to what the effect of these changes will be - I know you say your job is only to worry about how it will work in practice, but we have heard today that competition has been brought into the market. We have heard today there will be a breaking up of the generating section so competition can come into the market. What is in the Power and Water generating section that can be made cheaper so you can compete with, for example, Northern Power? What is there for you to compete? Are you going to reduce wages or reduce employees? One person said from QEnergy - I think you have the ability because some of the generators are old - you have a reduced depreciation cost. The gas is the same price for you as it will be for Northern Power. How will you be able to compete?

Mr BASKERVILLE: The big cost in power generation is fuel.

Mr WOOD: That is right, gas in our case.

Mr BASKERVILLE: Yes.

Mr WOOD: Yes.

Mr BASKERVILLE: The way you get benefits out of that is efficiency. Northern Power will install – this is my belief – the same type of generators we have at Weddell, the same machines. They are saying they can run their machines more efficiently than we can. We have to get up to that standard. That is where it is coming from. It has to come from efficiency.

Mr WOOD: My information from Power and Water is they will be much more efficient because they will be recycling the heat and getting up to even 60% more efficiency.

Mr BASKERVILLE: Different machines, yes.

Mr WOOD: How can you compete with that unless you – are you able to upgrade your existing equipment?

Mr BASKERVILLE: We are only talking 60 megawatts and our system is nearly 400. We have other machinery at Channel Island that we have to – which they started on the weekend - refurbish. We have steam generation there and that steam generation has to be right up to spick and span and run flat strap for us to get the efficiency to compare or compete with Northern Power or whoever else comes into the equation.

Mr WOOD: If Northern Power had not come into the equation would have you done the things you are doing, because that is what competition ...

Mr BASKERVILLE: Yes, exactly, that is what ...

Mr WOOD: If they had not come in ...

Mr BASKERVILLE: That is why I am here.

Mr WOOD: Yes, all right. For argument's sake, if there was no Northern Power, nobody was there, no competition, would have you upgraded your generating capacity to a higher standard?

Mr BASKERVILLE: Definitely, as I said, we started to do that on the weekend.

Mr WOOD: So even without competition?

Mr BASKERVILLE: Even without competition.

Mr BARRETT: Was it the threat of competition or was it just because it was a good idea?

Mr BASKERVILLE: No, it just needed to be done. We want it running as efficiently as we should and that has been the goal for the last year.

Mr VATSKALIS: John, I want to continue what Gerry said and you mentioned that Northern Power is going to establish 16 power generators. Are they talking about base load? Now how can they provide base load with 60 kilowatt generators? I mean we have got 400 kilowatt generators and we provide base load. Are they saying (inaudible) we have got this, they are going to come here and sell base load? A 60 kilowatt generator will be nothing enough. I cannot believe they are talking about base load unless they have got other plans we do not know.

Mr BASKERVILLE: We have heard that too.

Mr VATSKALIS: That was what came today from Treasury this morning.

Mr BASKERVILLE: Base load.

Mr VATSKALIS: The other thing we heard also, and do not get me wrong on hearsay, was that there were a lot of problems with Power and Water. There was not financial transparency, they tried to find out what money went where, they believe there was cross-subsidisation but they could not find how it happened. Is your organisation so bad that you can hide it from Treasury or so good that you can hide it from Treasury?

Mr CLARKE: Kon look, I think I can safely say that one of the biggest issues that we have had with the Power and Water Corporation is understanding the costs and revenues by

location and line of business. Now we are a very complicated business. It is really how many functions by the number of towns that is really the number of businesses that we have got so it is a complicated messy business. Nevertheless you would think that we have got these functions of water sewerage, electricity and there are bits of generation networks, system control and these sorts of things. These are all important functions all of which cost a lot of money and you would think that we would be able to instantly press button A and produce costs and revenues that you can rely on for those lines of business. Now we cannot - and we are getting pretty close to getting there - even now with the exercise that I have got on the go at the moment, we have not got that sort of information. Now this has been going on for many, many years. This sort of information has not been available and this lack of transparency is not good for any of us. It is not good for us, it is not good for the public, people need to know what the costs are by line of business and you also really need to know by location so you can understand it.

Now the structural separation - this is one of the reasons why I have been quite keen to do it as it forces that to occur. Now it sure does not do everything because quite a lot of the costs will still be left within what we call the rump, the Power and Water Corporation which is us. Nevertheless the key costs of generation - generation is the main one, retail is sort of relatively much, much smaller. It forces that separation of those costs and that is a good thing. Now if you do not have the formal processes - it is like some of the other stuff we have seen around where things are - 'Yes we are going to do it, we will do it' but it does not actually happen. This formal process forces that separation which produces the transparency. Now the competition side, I am going to stay away from that, but certainly that transparency which allows accountability and that is good for everybody, so that is why I like it.

Mr WOOD: Can I just go along that?

Mr VATSKALIS: One more thing I mentioned before is that you have done some work with the organisation to find out how good it would be for the Territory. We hear the government wants to do the separation because it is good for the consumers, it is going to bring the prices down, it is going (inaudible). Have you done any analysis on what would be the benefits for Power and Water Corporation? How then can you go along for a structural separation without actually doing the work to find out if it is going to be good for us? I am saying that because if it is good, then it is fine, it is good, you can sell it. But if it is not good you can say to your government it is not the right way to go about it.

Mr CLARKE: We have not done it and it is not really our job to do it.

Mr VATSKALIS: You have the assets you have to protect on behalf of Territorians. You have a structure you are running and you have a workforce, how can you say it is not for you to do it. You have to show the government that despite the advice you got, you have other

advice which says this is good or not good, or you can change it. You can change the organisation, you can be more transparent, you can make change within the organisation, but has this not happened?

Mr CLARKE: Because the government has said it wishes to separate them.

Mr VATSKALIS: So that is it.

Mr CLARKE: The part we will be concerned about will be the Power and Water Corporation - the residual amount - and for sure we are – we will soon know what the residual cost is because whatever is taken out of us the residual cost is ours, and it will then become our responsibility to operate at least cost. There is a bit extra I suppose because we will be providing shared services functions to the generation GOC and the retail GOC and, interestingly, that means our shared service function - and they are pretty expensive; we spent a lot of money on these things - they will now have greater scrutiny as well as being separately identified costings wise, the power retail and power generation will be saying, 'Hang on, how come this is costing so much?'

There is competition from within the Power and Water Corporation for those shared services function and that is a good thing for everybody.

Mr BARRETT: You are better situated to get an understanding of your own costing and price structures within that network GOC?

Mr CLARKE: Yes we are. The network costs are not too bad because the Utilities Commission processes require this ring-venting, but really they look at that part of our total cost. What we want to do is have a good understanding of all costs by line of business.

Mr BARRETT: Yes, wonderful.

Mr WOOD: Can I go back to some basics. This is about the breaking up. I want to know why you could not do it within the divisions you already have instead of having GOCs. You just told the committee you have nearly got to understanding all the costs under the existing divisions, is that correct?

Mr CLARKE: Yes, we are almost there.

Mr WOOD: If that is the case why would we have to go to GOCs? If the reason for going down the GOC path is to find out exactly what costs are associated with all the parts of your business, are you saying you could do that, nearly, with the existing divisions we have?

Mr CLARKE: Gerry, I always think of Paul Everingham's comment that the public sector is a bit like the coiled spring. Push the public sector in a direction and the spring bends over, you look away and it jumps back into place. The analogy applies here that sure with us and this regime we may well maintain a good costing system and revenue keeping system, but unless you have a formal process requiring that accountability forever the spring will return to its position.

Mr WOOD: Okay, that is good. The bit I need clarified is the reason for GOCs now. We have heard from various people today about keeping prices down etcetera, but if it is just for making sure you keep tabs on how much money it costs to run each section of your – you have an understanding of where your costs are that is fine, but is that the main reason it is being done? Is the main reason so you can have competition?

Mr CLARKE: The government has told us ...

Mr WOOD: What it says might be fine, but you are saying you want to find out what it costs to run your divisions. By bringing that into a GOC format, you are forced to do it so you do not have this spin. From your point of view, is it more about the efficient running of Power and Water rather than competition? Are you doing it for competition reasons or so you have a better run business?

Mr CLARKE: We are doing it because the government has said it wishes to. That is the framework we operate within, which is right and proper. There are certain side benefits that come out of that, one of which will be greater transparency in the accounting processes.

Mr WOOD: Regardless of competition, will it make you a better corporation?

Mr CLARKE: Yes, it will.

Mr WOOD: I am going back to what John said about fixing those machines anyway regardless of competition - regardless of whether there is competition, will this make you more cost effective by going down the path of splitting this corporation?

Mr CLARKE: I would say yes, if only because there will be much greater scrutiny of our own costs internally - our shared services cost, which is quite a material cost.

Mr WOOD: One of the concerns of a lot of people is this is leading down the path of privatisation. I do not want to get into that debate at the moment, but if the government had written on a legal document it will not privatise Power and Water - forget that - but if we did what you are talking about today - the government is taking about - would you say that was a good move to make Power and Water a better operating company or corporation?

Mr CLARKE: Yes, I would.

Mr WOOD: Right, okay.

Ms MANISON: Mr Clarke, you now know what your networks tariff will be given the Utilities Commissioner has passed on that increase and granted you - I think it is about 32%.

Mr CLARKE: I think 29%.

Ms MANISON: You also know what the water and sewerage set tariffs are as well, and I understand you have your funding agreement for Indigenous Essential Services locked in for the next two years. Is that correct?

Mr CLARKE: I am not sure. Jim, two years is it. Okay.

Mr BAMBER: Two years.

Ms MANISON: With the loss of generation from Power and Water and the loss of retail from Power and Water, are you confident the monopoly GOC of Power and Water Corporation will be able to continue on with its investment in infrastructure programs, repairs and maintenance and maintain current employment levels where they are at going into the future?

Mr CLARKE: Yes, I am.

Ms MANISON: Thank you.

Mr WOOD: I need to go back one step to the bit that has always worried me. Under the present organisation we can have competition, so I get confused as to whether competition, in theory, already exists. You have a splitting up of the Power and Water monopoly into three sections. Technically, is that really the status quo except that we have a better breakup of Power and Water from its own point of view? In other words, it knows exactly where it is going with its expenditure and runs its business better. What we have now, before this legislation goes through, is it any different than what we would have if this legislation was passed - in regard to competition?

Mr CLARKE: Mr Wood, it really is a matter for the Treasury people, but the reality is yes, it is different because it does allow effective competition. The current arrangements do not.

Mr WOOD: Why not?

Mr CLARKE: They rely on bilateral contracting. The investment in generators it is a lot of money so they need long-term contracts to be sure they will get a return on the capital. The current arrangements - the retail contracts are only two or three years or something of that order, and a generator is unlikely to come in there unless they had it as part of some sort of - like INPEX, for example, if they chose to ...

Mr WOOD: That is a change in the legislation, is it not? It allows that longer term contract.

Mr CLARKE: Effectively if does. I am not sure about the legislation, but it must do because that is what - by setting up the new generation. I have not gone through the legislation in detail, but that is the rationale.

Mr WOOD: Philosophically the same thing could occur now, except for the problems you mentioned, as would happen if the legislation was changed. Competitions could still occur, someone could get into the generating market right now if they so desired - it might be difficult but ...

Mr CLARKE: Yes, that is true. We meet the competition requirements because - competition is possible it just will not happen.

Mr WOOD: I think I raised this question when we had a briefing on the bill - the gas side of it, which is something I did not know about. The gas comes from ENI under contract to the government. I am not asking the dollar price, but what is the agreement the government has

with ENI. Do they have to use X amount of gas regardless of whether they burn it up or not and pay for that?

Mr CLARKE: Yes, there is a take or pay arrangement for quite a lot of the gas.

Mr WOOD: My understanding, from speaking to someone today, is that is not necessarily the case. I am not sure who we were speaking to.

Mr CLARKE: No, no, no. It is take or pay.

Mr BAKERVILLE: We have take or pay obligations.

Mr WOOD: Take or pay?

Mr CLARKE: Yes.

Mr WOOD: You can sell that gas to others?

Mr CLARKE: Yes.

Mr WOOD: Do you sell that - you have a wholesale and a retail price. If someone like Northern Power says they want to buy gas, you have to sell it to them at a wholesale price?

Mr CLARKE: It is a negotiated price.

Mr WOOD: That is what would happen. Is that a company this gas ...

Mr CLARKE: No.

Mr WOOD: What is it?

Mr BASKERVILLE: It is the gas unit within Power and Water Corporation.

Mr WOOD: It does not do a lot unless someone comes along and asks for some gas?

Mr CLARKE: No, they are very active.

Mr WOOD: What are they active in?

Mr BASKERVILLE: A lot of people in the mining industry and the like, the abattoir - I am just rattling them off the top off the top of my head, but quite a few people in to see us about gas supply.

Mr CLARKE: We are in the market.

Mr BASKERVILLE: We have a group of people looking at LNG for remote communities so they have been talking to us about gas prices.

Mr VATSKALIS: Does Power and Water Corporation have to buy gas from the gas unit?

Mr CLARKE: No, no.

Mr VATSKALIS: There is no transaction with the gas unit?

Mr CLARKE: There may be in the future, Kon. If the competitive market eventuates the gas unit is quite conceivable. That might be quite an independent unit altogether.

Mr VATSKALIS: If we talk about competition, you cannot have a gas unit inside the monopoly?

Mr CLARKE: They have left it there because we are a separate entity. At the moment we are not competing with generation or retail. That is why it can sit there for the time, and there is a case for saying it could sit there forever. However, it is such a specialised task and you would not want the negotiation.

Mr VATSKALIS: One of the things that concerns me and was discussed previously is you will have companies coming to the Territory talking about having power stations generating base load. That means you do not have to generate that load which means you cannot use gas. You will have surplus gas which is take or pay. If you cannot sell it you are still paying for gas you cannot use - a domino effect - one causes the other.

Mr CLARKE: Yes, there is no issue the gas is a matter which has to be sorted out. If the generator comes in, I am not sure how much – they are relatively small in the overall scheme of things, but they have to get their gas from somewhere as well. We are in the market and Santos is in the market.

Mr VATSKALIS: The separation of generation and transmission will apply only to the greater Darwin area, or will it go as far as Alice Springs, Tennant Creek and Katherine?

Mr CLARKE: My understanding is it is all them. I read them out at the start.

Mr VATSKALIS: Power and Water - because nobody will want to enter the market in Tennant Creek - will generate power there and will have to negotiate a price for transmission?

Mr BASKERVILLE: Yes, they, do it now.

Mr VATSKALIS: They do it now, but not in a competitive environment like it will be in the future?

Mr BASKERVILLE: But you might get a competitor in Tennant Creek.

Mr VATSKALIS: In Alice Springs you may.

Mr CLARKE: Yes, sure, possible, hope so.

Madam CHAIR: Mr Clarke, does the Board have a forecast on its debt levels over the next five years and can Territorians expect those levels to go up or down?

Mr CLARKE: We have it in the SCI, I have not got them here with me. We have the current SCI. Our borrowings for the next - this is the 2013-14 SCI - we had borrowings of around about \$80m, \$77m, \$68m and \$69m in the next four years. That is the new borrowings. The nett debt end of 2013-14 - we were anticipating at the time is \$1.4bn, 2014-15 is \$1.5m - I am rounding these up - and it still remains at about \$1.5m in 2015-16 and gets up to \$1.6m by 2016-17. Those numbers will be pretty much the same in the new SCI.

Mr HIGGINS: Given the gravity of the debt you are talking about - the \$1.3m or \$1.4m increasing to \$1.6m - do you acknowledge a tariff adjustment was necessary to improve Power and Water's financial position?

Mr CLARKE: Yes.

Mr HIGGINS: How sustainable do you consider increasing debt when the Moody's ratings agency, in 2013, noted that tariff increases should be phased in at a slower pace, which could have had a negative implication for the corporate's financial performance?

Mr CLARKE: As far as I am concerned the corporation should be incurring debt when it has to. There should be a return – it should be able to show there is a return on that investment. If there is not a return then it has to say to government, 'This particular investment is necessary in order to achieve a reliable supply and therefore we need a CSO to meet it'. I do not know if that meets your query.

Mr HIGGINS: Yes, I think the answer I was looking for was if you borrow money and increase your debt you have to start your repayment straightaway, you do not phase it in over five years.

Mr CLARKE: Yes, sure.

Ms MANISON: In relation to the legislation, Treasury, I understand, has been responsible for the drafting of it. Have you been consulted with the drafting of that legislation?

Mr CLARKE: Yes. Djuna and co were consulted, yes.

Ms MANISON: Were any consultants engaged to advise you in regard to the legislation and the drafting?

Ms POLLARD: Yes, we did. We had Clayton Utz in to assist with that, and they are also conducting our legal due diligence review.

Ms MANISON: Is the cost to get consultants in part of the \$2.2m or is that ...

Mr CLARKE: Yes, it is part of the \$2.2m.

Ms MANISON: In relation to the structural separation, has Power and Water Corporation been having any discussions with any other potential people with interests, any companies with interests, any possible competitors in the Territory market?

Mr CLARKE: We had – I presume we can mention this – probably not. We might be able to say something in camera on that.

Mr BARRETT: You can say you have been having conversations, but not necessarily with whom?

Ms POLLARD: Yes.

Mr CLARKE: Yes, we have had discussions. I am not sure how much we should talk about that in public.

UNKNOWN: Feel free.

Madam CHAIR: That is fair enough, Mr Clarke.

Mr CLARKE: It is not as though it was a material issue. It was pretty low key stuff.

Mr BARRETT: What do you feel about your debt position?

Mr CLARKE: It is obviously a worry and something – I am not sure what our ratios are, but they are a worry and we have to be very careful.

Mr BARRETT: In terms of your asset value and the debt value, if there were instances where assets had to be written down is the ratio between your debt and assets still okay?

Mr CLARKE: I think we would still – we have some room, but nevertheless it is something we have to be very conscious of.

Mr WOOD: Following up from what Nathan said, one of the questions we have is in response to Power and Water's concerns about stranded assets arising from the entry of generation competition, something I have been concerned about. The Utilities Commission has said Gen Corp will need to write down its non-performing assets. How will such a

scenario impact on Gen Corp and how would the cost of such a write down flow through to consumers or taxpayers?

Mr CLARKE: The reality is there was overinvestment and we will have to – in fact I think we have already written down a number of assets. How does that translate? Ultimately it translates – it has a lower cost in generation and therefore that translates through to the contracted customers - they will see the lower price. The residential customers' price is set by the government, so effectively the lower cost would give us a slightly larger capacity to pay a dividend to the government.

Mr VATSKALIS: You said the big consumers can have a better price, a lower price?

Mr CLARKE: Yes.

Mr VATSKALIS: The residential price is set by the government?

Mr CLARKE: Well, the government ...

Mr VATSKALIS: The argument from the government that it will benefit consumers - it should be it will benefit the big consumers but not necessarily the small consumers because the government can offset the reduction in the price for the big business by increasing the price in my house and your house?

Mr CLARKE: The government has – I will describe it like this. Commercial users are here, that is their price and residential users are there.

Mr VATSKALIS: Well, at this stage.

Mr CLARKE: I am saying residential users' prices are lower.

Mr VATSKALIS: The fact remains the big consumers will benefit by the government proposing privatisation; however, it will not necessarily flow over to the residential consumer since the government sets the price for the households.

Mr CLARKE: I think of this competition as being a long-term issue. In the very short-term, because the government is setting the prices, it does not matter what we do with costs - whether we raise them or lower them - the prices for residential customers are currently set,

but in the long-term prices will move with costs and, therefore, the residential customers will get the benefit of whatever lower costs come about as a result of the structural change.

Mr VATSKALIS: Somehow you do not persuade me because if the costs increase because we have dropped the tariffs for big business, we have to recoup them somewhere. There are so many thousands households out there and if we put the price up a little then we can recoup the cost to make it even.

Mr CLARKE: I think your starting point is wrong, Kon. That is ...

Mr VATSKALIS: I agree the benefit to consumers is important, but the benefit to all consumers is more important than benefit to some consumers.

Mr CLARKE: No, but that is the short-term and the long-term. The whole idea of the structural separation is to have lower costs in the long-term. Because there is not a perfect market at the moment, the government is setting the prices for residential customers and they are locked into those prices; it does not matter what happens to costs in the very short-term because the prices are set, but in the long-term when you know the prices are going to be related to costs, if the costs come down, then the prices will be lower than otherwise would be.

Mr WOOD: John, in your submission to the Utilities Commission Review of Wholesale Electricity Market Generation, you raised an overarching concern that due consideration had not been given to the relative costs and benefits of the alternative wholesale market frameworks considered in the review and recommended a comparative analysis be performed to determine the selective framework is the optimal one for the Northern Territory market. Can you explain this concern, and are you aware of whether the structural review is to be undertaken?

Mr BASKERVILLE: I will start at the back. The review will definitely be undertaken, that is a given. My concern is after looking at utility prices interstate and other costs associated with running an organisation such as Power and Water, more so on the power side, we are out of whack. The only way to pull us back into line is to get a review done that compares us with, for argument's sake, somewhere in northern Queensland or Western Australia.

Mr WOOD: Thank you.

Ms MANISON: In relation to Indigenous Essential Services and the contractual arrangements you have in place now, Power and Water is funded by the Northern Territory

government through the Department of Community Services - sorry, can you talk me through the current arrangements and how long they are in place?

Mr BAMBER: Jim Bamber, General Manager Remote Operations. The arrangement is we will see something like \$71m roughly per annum from the Department of Community Services for provision of power, water and sewerage services to 72 communities and 66 outstations. We supplement that with approximately \$38m to \$39m of direct revenue. This is where we either recover through pre-paid meter token sales or through direct charging of non-residential customers - stores, government centres etcetera - in those communities. The total revenue is made up of the funding agreement and the direct revenue plus some other funding we get from federal bodies.

Ms MANISON: My understanding is government has said, as part of the structural separation, this arrangement is to not change. How long is this contract in place for?

Mr BAMBER: It is a three-year agreement. An initial five-year agreement was replaced by another three-year agreement, and we just enacted another three-year agreement and we are one year into it now.

Ms MANISON: Okay, so two years left outstanding on that agreement. In relation to the current enterprise bargaining agreement applying to employees of Power and Water Corporation which is set to expire – when does that expire?

Mr BASKERVILLE: 2015.

Ms MANISON: My understanding is that is part of the structural separation. That is 2015 current existing employees will transfer over on whatever has been agreed under that EBA?

Mr BASKERVILLE: No change.

Ms MANISON: In relation to communications with your customers and the broader community across the Territory regarding the changes in Power and Water Corporation, is any work under way there or is that something Retail Corp and GenCorp will be expected to conduct on their own?

Mr BASKERVILLE: A customer campaign will use print advertising and direct communication through customer billing and place inserts in the bills to explain what is happening in Power and Water, what the charges mean to customers and what the billing process will be. A public relations campaign will communicate public information through

media releases, and possibly target interviews and talkback radio. The Power and Water call centre, which remains in the Power and Water monopoly GOC, will continue to provide information for customers on the changes, directing general inquiries to the government information paper on the Treasury and Finance website. So, it is pretty intense.

Ms MANISON: Will Power and Water be conducting the communication on behalf of GenCorp and Retail Corporation?

Mr BASKERVILLE: The initial stage, yes.

Ms MANISON: If somebody is to ring - this is a very operational question - Power and Water because they want to get a connection, a disconnection, inquire about their bill under the new world after 1 July ...

Mr BASKERVILLE: It will come direct to Power and Water for the monopoly GOC.

Ms MANISON: The same thing, they can go in to the retail front counter?

Mr BASKERVILLE: There will not be any changes to that.

Mr WOOD: One step backwards - I should have asked when you said the review was coming out. When do you think that review will be finished? Is it in the process already?

Mr BASKERVILLE: It is a long drawn out process. It will take us probably to the middle of next year before we get a result.

Mr WOOD: Will this give us an idea of what a comparative city cost would be?

Mr BASKERVILLE: That is the intent.

Mr WOOD: Will that city also have GOCs or will it be a similar setup to what we have here? How will the comparison work?

Mr BASKERVILLE: That has been the problem with this review. I have been looking at this for some time now. Power and Water is unique. There is no other utility around the country like Power and Water with the fact we have power, water, IES, so we have had to

pick an area where there is some similarities. I think the one we have found is in Western Australia and I have spoken to the CEO on a couple of occasions about the reviews done in that part of the world. They have the same problem as us and are not connected to any grid, the same as the Northern Territory. They tell me their review took over two years to get the correct information out. We are trying to do ours inside twelve months.

Mr WOOD: What are you expecting out of that review?

Mr BASKERVILLE: Some benchmarking is what we are trying to gather, and not only that, but productivity - to see whether we can compare with other utilities as far as our productivity goes. We are very much hamstrung as far as generation goes because they are connected to a grid whereas we are not. That is also an issue for us. As I said, it is not straightforward but, hopefully, we will have something on the table by mid-2015.

Mr WOOD: Is there a comparable city in Australia with roughly the same population - it is probably limited because we are in the tropics - that runs on a private generator.

Mr BASKERVILLE: No.

Mr WOOD: You could not compare?

Mr BASKERVILLE: We are unique. A comparable city in Australia is Kalgoorlie, but it is connected to a grid.

Mr WOOD: Then it has a different climate?

Mr BASKERVILLE: A different climate, yes. Yes, that is our problem.

Mr WOOD: Kununurra is a bit small?

Mr BASKERVILLE: Katherine is a bit small. It is connected to a grid.

Mr WOOD: Yes, all right. Thank you for that, John.

Ms MANISON: Call me a cynic, but I would be very keen while we are here to get staffing numbers tabled for the Public Accounts Committee in relation to each business unit that currently exists within Power and Water.

Mr CLARKE: Sure.

Ms MANISON: As we look down the pathway, post-structural separation, we can look at those and contrast and compare?

Mr CLARKE: Sure.

Ms MANISON: Thank you.

Madam CHAIR: Because of our reasonably tight time limit, if you could have that information to the committee by Friday it would be much appreciated.

Mr HIGGINS: There are 24 hours in a day, not a problem.

Madam CHAIR: If there are no further questions I would like to thank all of you for coming today. We know it takes you out of your core business. We are extremely grateful for your contribution to this inquiry and hope you enjoy the rest of your afternoon and best of luck with whatever proceeds.

Mr CLARKE: Thank you very much.

Madam CHAIR: Thank you.

The committee suspended.

Madam CHAIR: On behalf of the committee I welcome everyone to this public hearing into splitting the Power and Water Corporation. I welcome to the table to give evidence to the committee from the Electrical Trades Union, Queensland and Northern Territory branch, Mr Paul Kirby, NT Organiser and Mr Lance McCallum National Policy Officer.

Thank you for coming before the committee. We appreciate you taking the time to speak to the committee and look forward to hearing from you today. This is a formal proceeding of the committee and the protection of parliamentary privilege and the obligation not to mislead the committee apply. This is a public hearing and is being webcast through the Assembly's website. A transcript will be made for use of the committee and may be put on the committee's website.

Because of the short time before the Assembly may consider the related bills the committee has agreed to publish the draft transcript to this hearing before any corrections are received. If at any time during the hearing you are concerned that what you will say should not be made public, you may ask that the committee go into closed session and take your evidence in private and we are more than happy to do that.

I will ask you each witness to state their name for the record and the capacity in which they appear. I will then ask you to make a brief opening statement before proceeding to the committees questions. Witnesses could you please state your name and the capacity in which you are appearing.

Mr McCALLUM: Lance McCallum, National Policy Officer for the Electrical Trades Union of Australia, good afternoon.

Mr KIRBY: Paul Kirby, Northern Territory organiser for the Electrical Trades Union.

Madam CHAIR: Thank you. Mr McCallum, would you like to make an opening statement?

Mr McCALLUM: Yes, thank you.

Mr McCALLUM: Thank you very much for that welcome, Chair. We would like to start by acknowledging we meet on the traditional lands of the Larrakia people, the Indigenous owners of the land that we honour, the nurturing of those lands over thousands of years and their custodianship.

I would also like to extend our thanks to the committee members for the opportunity to speak at today's hearing, and also acknowledge the staff of the committee secretariat for their assistance prior to today.

We appreciate the opportunity to appear today as part of the inquiry into the current proposal by the Northern Territory government to disaggregate the publicly owned Northern Territory Power and Water Corporation.

This energy reform proposed by the government not only impacts directly on our members as employees through their workplaces, but more broadly speaking a secure, reliable and affordable supply of electricity is fundamental to providing the standard of living we all expect in a First World country such as Australia.

The Territory government has the responsibility of providing electricity to Territorians in a reliable, affordable and sustainable manner and the current proposal to fundamentally reform the energy market will affect each and every consumer and business in the Territory.

Therefore, we believe it is of paramount importance to get the reform right and to ensure it delivers real improvements and positive outcomes in the everyday lives of Territorians.

The proposal by the government is for NT Power and Water to be restructured by disaggregating the business into separate government entities for retail generation and network and transmission, and to hopefully introduce a competitive wholesale generation market in the Territory.

This will include the establishment of several new governance and regulatory bodies and associated arrangements. The government believes this reform will attract future investment into the Territory energy sector and, more importantly, should deliver better outcomes for consumers by downward pressure on prices and ensure security and reliability of supply for the future.

Unfortunately, we do not share the government's optimism. We believe the new arrangements are costly, have significant cost implications for Territory taxpayers and will ultimately only place upward pressure on power prices and lead to lower service levels.

There are several reasons we hold this view. Under the proposed reform, the current publicly owned vertically integrated single business will be split up and replaced by approximately six to eight new entities under the proposed new market arrangements. We consider this to be costly, inefficient and counter to the stated fundamental premise of the reforms.

We also believe there are real questions over whether or not a market the size of the Territory can sustain a competitive wholesale generation market. Making an informed

assessment on the impacts of this reform is not only impossible due to the lack of publicly available detailed modelling of the proposed reform. We find this absence of information very concerning. For example, there has been no evidence provided that lower electricity costs will result from these reforms - no hard data at all.

The government, we submit, should have undertaken detailed modelling studies on the impact of the reforms and made them available to the public before deciding to embark on these reforms. The 'build it and they will come' approach to energy market reform is asking taxpayers to sign up to reforms on the basis of blind faith and that it will lead to positive consumer pricing outcomes and increased energy investment while leaving the detailed arrangements of the reform left to develop throughout the implementation phase, thereby avoiding property scrutiny. We believe the reform process should, as it currently stands, be paused until detailed independent modelling on electricity price paths over five, 10 and 15 year periods are undertaken to ascertain the residential and commercial price impact of the disaggregation of PWC and the associated market reforms. This information should be made publicly available, as I have already stated, and reported back to this committee before any further consideration of the current reforms.

We also believe the full range of available energy market reform options has not been properly investigated and further analysis investigation on alternative market designs needs to be undertaken. We think there is an unseemly rush to introduce the new arrangements without the appropriate level of analysis being carried out for the cost benefit analysis of the full range of options available. We base that view on the fact we all know the Katherine/Darwin system has sufficient generation capacity under current projections to 2019-20; therefore the need to rush this reform in to allow for new investment is incomprehensible in that it provides higher risks. When I say risks, I mean bad public policy outcomes.

The government has, on the public record, gone to some lengths to assure Territorians of two main things: the reforms will place downward pressure on power prices and the splitting up of PWC will not result in privatisation.

We, at the ETU, have long held grave concerns this reform process is simply a prelude to privatisation and, unfortunately, as the draft bills are currently before the House it would seem these fears have been well-founded. As they stand they clearly allow, in our submission, for partial or full privatisation of public assets via part 5A of the PWC Legislation Amendment Bill that is currently before the House. Our members do not want their industry carved up and sold off, neither does the public want to see a cloud hanging over the security of the essential services they own.

We believe the government needs to give substance to its public claims that there is no plan to split up PWC and sell it. The good news is this can easily be done by removing the

offending, in our view, legislative sections and going one step further. We are also advocating for legislative amendments that provide ownership restrictions for public assets to be hard-wired into current and/or proposed future government owned business legislation to ensure ongoing public ownership of essential service assets and reassure taxpayers. Thank you.

Madam CHAIR: Thank you. I note your concern that part 5A of the legislation - in your view it provides for privatisation of public assets. In the second reading speech the Treasurer explained this part sets out a regime for making regulations to transfer business from one government owned to another. While that part allows the making of regulations regarding the transfer of the business of a corporation, such a transfer can only be a relevant entity under the bill which are owned by the Northern Territory. I am not sure how you see part 5A providing for the privatisation of public assets.

Mr McCALLUM: We are basing it on advice we have received. There might be a fundamental disagreement as to statutory interpretation here, but we believe it does provide for partial or full privatisation and if the government is saying - I understand they say that is the mechanism by which they want to effect this reform, well there should be a sunset clause that says those amendments cease to exist as soon as the current reform is over. You could, once again, introduce a range of other amendments that protect public ownership. That is fine.

Mr WOOD: I was asking this of Power and Water, you can have privatisation of generating plants and also retail under the present system. Is your concern more that this could lead to privatisation of Power and Water rather than anything changing in say – like we know Northern Power is looking at coming?

Mr McCALLUM: Yes.

Mr WOOD: They could come under the existing legislation, or they could come under the new legislation.

Mr McCALLUM: Yes.

Mr WOOD: That is not the concern. The concern is you believe the restructuring of Power and Water will lead to privatisation, but if the government gave a watertight guarantee that Power and Water will not be sold off or it would not be considered for the next 10, 15 or 20 years - was built into something - would your concerns about the restructuring of Power and Water still exist?

Mr McCALLUM: That would go a long way to allaying our fears. Yes, to be absolutely clear, we are not opposed to private participants in a market. The more generators there are in the energy industry here the better, whether they are public or private owned. We have no issue with that.

You are absolutely right in saying our concern, fundamentally, is the way these bills are structured at the moment allow for the generation or GenCorp or Retail Corp, as they would be in the future, to be sold and they are currently under public ownership. Yes, absolutely, if legislative amendments were put in there that were hardwired into an act saying there had to be a full referendum with a minimum percentage of yes votes for there to be ...

Mr WOOD: Or something similar.

Mr McCALLUM: Exactly.

Mr BARRETT: Why are you so concerned about privatisation?

Mr McCALLUM: Because experience in other states, whether it is South Australia, particularly Victoria - privatisation has ended up in employees losing their jobs. I think in Victoria, when the then Kennett government privatised the State Electricity Commission over about five years in the mid-1990s, employment in the energy industry went from about 14 000 down to about 4000. That is one of the fundamental cornerstones we, as an industrial organisation representing our members' interests, have. I could go on in terms of we would also argue it is not just job losses, we have seen reduction in service levels while prices still go up.

Mr HIGGINS: If I can go back to the issue with the section that talks about privatisation, a question was asked this morning where it is going from one government-owned corporation to another - the question was asked of Treasury. Treasury said no, it is only when you go from one corporation to another. You said you have advice that it is not restricted to that. Can we get a copy of that advice?

Mr McCALLUM: Yes.

Mr HIGGINS: I presume that is legal advice?

Mr McCALLUM: Yes, we can get you something.

Mr HIGGINS: Would we be able to get a copy of that?

Ms MANISON: Based on the experience of the ETU and your membership across other jurisdictions across Australia, when you have seen structural separation occur in other jurisdictions what have the consequences been and do you anticipate those for the Northern Territory as well?

Mr McCALLUM: Looking at the experience in other jurisdictions in Australia the one that immediately comes to mind is Western Australia where some years ago the then government went through a process of disaggregation, where there was – very similar to what is being proposed here - a single state-owned vertically integrated business and retail and generation were taken out of it for the exact reasons being spoken about here - to attract investment and place downward pressure on prices. A Labor government implemented those reforms.

What is happening at this exact moment under a conservative government in WA is they are implementing a market review to look at a process of reaggregation. This is in a market several times larger than the Northern Territory. I think it has about one million consumers as opposed to - I think the market size here is about 80 000. Once again, the fundamental question

Mr McCALLUM (cont) : I think the market size here is about 80 000. Once again, the fundamental system question of sustainability and what the market is able to sustain in competition. It has to be very closely looked at. In Western Australia they still have skyrocketing prices. The government has had to subsidise - I think it was the generation business - to the tune of \$500m a year, and it has been clear that the breaking up of the industry did not result in any addition investment. I would be extremely concerned that the Territory might be heading down a similar path. They are the outcomes there; that is a fact. Of course, there are differences between one market and another and that needs to be understood but, at the same time, the experience in Western Australia needs a close going over.

Mr HIGGINS: The reaggregation in Western Australia, does that include the network? My understanding is it does not; it only includes the generation and retail. It does not include the network at all so it is not as simple as you make out - that you have deaggregation then join them back together because you are not joining it all back together ...

Mr WOOD: We get the aggravation.

Mr HIGGINS: There is a very distinct difference and that is the network is not included. I think the reason it is going that way is because some of the private competitors do both.

They have come into the market and do the generation and the retail. What they are doing is joining theirs together to compete with the private one.

Mr McCALLUM: Right, which is also proposed in the current bills after the four- and five-year exclusionary periods expire for generation and retail respectively. If you are uncomfortable with what I am saying with regard to reaggregation in Western Australia I will stop just one step before that. What happened in Western Australia ...

Mr HIGGINS: I am not uncomfortable with it, do not get me wrong. I asked the question because I want to make sure the truth is given to me.

Mr McCALLUM: Absolutely! What happened in Western Australia is there was one vertically integrated state owned enterprise that had retail and generation taken out of it to allow for a competitive market. That experience has not worked out in Western Australia, so much so that the government has had to pay \$500m in subsidies every year as part of the ..

Mr HIGGINS: Is that \$500m related directly to the splitting? I cannot see the connection between the two.

I know you have said they subsidised \$500m to the generation, but where is the link to the fact it was split up?

Mr McCALLUM: I will quote from a ministerial statement from the current Energy minister in Western Australia. There is plenty on the public record over there.

Mr HIGGINS: I want to know some here, that is all.

Mr McCALLUM: This is from Thursday 6 March 2014, 'Review Seeks to Reform Electricity Market' just a couple of excerpts:

The state government has established the Electricity Market Review to address the long-standing problem of rising electricity costs, a result of the flawed disaggregation of Western Power by the previous Labor government ...

It goes on to say, 'Government Subsidy to Synergy':

This review is required to ensure that the sustainability of the electricity market in the south west interconnected system while winding back the high levels of government support current ballooning to more than \$550m a year and rising ...

The exact breakup of that \$500m in subsidises - I cannot provide you with any further detail on that, but I am sure colleagues in Western Australia will be able to.

Mr BARRETT: The objectives of a government owned corporation is to operate at least as efficiently as any comparable business and to maximise the sustainable return to the Territory on its investment in the corporation. The status of government owned corporations, Part C, is it cannot render the Territory liable for the debts, liabilities or obligations of the government owned corporation or any of its subsidiaries. The issue we are facing and the question you raise about ballooning and subsidises being paid, we are already there, mate. The issue we face is what we do about it now.

Mr McCALLUM: Sure.

Mr BARRETT: Clearly, we cannot leave it the way it is. The options we are taking and the things we are looking at are in front of you to look at. If you disagree with them, what do you suggest?

Mr McCALLUM: I do not have a magic bullet for energy reform in the Territory. We are a union with limited resources. We do not have the might of the energy department and Treasury and, frankly, we are not the elected government.

Mr BARRETT: Would it surprise you that those organisations have come to the conclusion that this is the way forward and the most logical and coherent way through the issue we are in right now?

Mr McCALLUM: I have seen that is what the consultants engaged have concluded in their reports, and that those reports were written to specific terms of reference issued by the government, yes.

Mr KIRBY: Part of our concern is not being able to see any hard evidence that will be the case, that there will be benefits out of it, there will be cost savings, there will be downward pressure put on people's tariffs and that no assets of Power and Water that have already been extensively paid for will be mothballed. We cannot see any evidence of any of that and that is our concern.

Mr HIGGINS: Our concern is we have a debt of \$1.3bn growing to \$1.6bn and that has to be addressed. While your opening remarks said we should not rush into this, I think this reform was started in 2000. All the states agreed to this reform back then and it has been stalled. I think the Reeves report in 2009 highlighted the problem with the growing debt and failing infrastructure. It is not something that has just popped up in the last six months.

Mr McCALLUM: Are you referring to energy industry national competition policy reforms?

Mr HIGGINS: Yes.

Mr McCALLUM: That had nothing to do with Territory debt? I am asking a general question.

Mr HIGGINS: No, no, no.

Mr McCALLUM: Right.

Mr HIGGINS: I am saying what we have at the moment is a ballooning debt in Power and Water and we are saying, as a government, something needs to be done about that full stop.

Mr McCALLUM: Sure.

Mr HIGGINS: You also said in your opening remarks this government is rushing into this. I am saying, 'Hang on', a review of the electricity market has been around since 2000, so I do not see it as something that is being rushed into. It should have been addressed 10 years ago.

Mr McCALLUM: My understanding is the reform in the energy market has been the introduction of full retail contestability. That started in the early 2000s. It initially failed, did it not, and the government had to then introduce contestability - only in the retail part of the energy market - in tranches until it became fully contestable in 2010, which is fairly recent, and the reform we are talking about before the committee is introducing competition into the generation sector as well as slicing and dicing PWC. They are different things.

Mr KIRBY: Before we move on, I would like to pick up on one of those comments around where Power and Water was 10 years ago. I worked there for about 16 ...

Mr HIGGINS: I did not say where it was 10 years ago.

Mr KIRBY: Where the reforms were 10 years ago and the state of the infrastructure might have been the terminology you used.

Mr HIGGINS: No, I did not mention that, I do not think. I only spoke about that in terms of the ballooning debt we have today.

Mr KIRBY: Well, permit me then make a link?

Mr HIGGINS: The Reeves report of 2009 talked about the state of the infrastructure.

Mr McCALLUM: Yes.

Mr KIRBY: Can you permit me to speak on that for a moment?

Mr HIGGINS: Yes, go ahead.

Mr KIRBY: Up until last year I worked at Power and Water for 16 years. One of the reasons that money had to be borrowed and invested into the infrastructure around the time of those Casuarina Zone Substation failures was because the people I represent, the people of the Northern Territory that work at Power and Water, were continually concerned about standing in front of high voltage equipment when they could not guarantee the way it would behave when they went to operate it because it had not been maintained properly.

The government of the day had a choice of leaving those gen sets hooked up and basically abandoning the network, borrowing the money to fix the network because of the situation it was in, and going to Power and Water staff and telling them they could not guarantee they would go home at night. Yes, it is unfortunate that is the situation we have ended up in, but that is the situation we are in. The avenue we would prefer to see is that debt responsibly paid off, not profit-making portions - and this is the conversation harking back to earlier that if it is just privatisation that is our concern. My concern is why are those contestable customers being taken out of Power and Water so it can be easier for people to pick them off? That will be significant monies out of the Territory finances the Territory government will not have access to if that happens.

Mr HIGGINS: I do not think this committee will be considering privatisation in any way or form. We are looking at the legislation full stop. The Treasurer has made it quite clear that

privatisation is not on the agenda. He made the statement in his second reading speech that the movement of assets is simply between government corporations. There is nothing to come out of this committee that will talk about privatisation.

Ms MANISON: In regard to previous statements by the Treasurer - this is probably one where you can give us a bit of insight into Power and Water due to your job representing your members - the Treasurer said earlier this year that, and I am quoting from an ABC interview on 9 January:

Well, there's not a lot being done at this stage, but it's probably fair to say that they're over-staffed and that they have far too much equipment than they actually require to do the job.

He goes on to say - he is talking about structural separation and the separation of Power and Water at this stage:

Well look, it would be my expectation that there will be reductions in staff numbers. How many there are and that sort of stuff I am aware of. That's a matter for management team of Power and Water Corporation.

Given the workload of Power and Water employees at the moment, how are they going in regard to being able to do their job, and how would staff reductions impact them given they have been forecast by the Treasurer's as part of this structural separation?

Mr KIRBY: I guess one of the concerning statements I heard Power and Water senior people making earlier was around the over-capitalisation within Power and Water. My experience and my opinion would be that money invested into the infrastructure is just what had to be done to ensure a safe and reliable supply. To say there has been over-capitalisation or too many Power and Water staff and that is what the debt is derived from, we put a lot of effort into - not the union and not the government of the day - getting independent industry experts from southern states that had history and good relevant experience to come up and spend a month going through Power and Water, going through their books, going through their maintenance regimes so we knew where we were short so we could organise to attack that and get that fixed as quickly as we could.

One of our guys made a comment a couple of years ago: it is a bit like turning the Titanic around with plastic paddles. It does not happen in a hurry with an entity like Power and Water when it was as run down as it was, but any removal away from the investment, or the people in Power and Water, will see us pretty quickly go back to those days. There will be an inertia effect. You can cover it up for a lot of years, you can - it is like a car, you cannot

invest money into a car for a long time and get away with it, but the trouble that we have with an essential service that works in some of the harshest conditions in Australia is once it tips beyond that point, it is very difficult and very expensive.

One of the reasons it is so expensive now is because the loads are that high that a majority of the work within those zone substations has to be done at night time. That was the issue with the blackout - that work had to be done at 1 am when the loads had dropped. You cannot do it at any other time, so that brings a bunch of other factors into play.

Madam CHAIR: Can I ask you a question about jobs? Obviously, as a union that is a massive concern for you professionally and is part of what you do. I think you were both in the room when Power and Water staff were saying, as part of the structural separation, there would be no job losses and they were very conscious of making sure people were getting up one day and the next day going to work under a different name and they had done consultation and that staff were getting the full bottle on that. That must be heartening and give you confidence in the process, to some extent, that jobs will not be lost as part of the separation?

Mr KIRBY: Our concern is harking back to the Treasurer's comments saying he expects there will be job losses.

Madam CHAIR: In his final comments he said - and Ms Mansion said - that would be a matter for the hierarchy of Power and Water. We have heard that from the horse's mouth today, so any fears created by the comment should really be allayed.

Mr McCALLUM: We would love to be optimistic that that will come to fruition, and Paul can correct me if I am wrong here, but I also heard the current EBAs expire next year and the industrial arrangements beyond that, if there is a splitting up, are at this point unknown. It can go a number of ways so that places a question mark over our members' fundamental employment arrangements. Yes, they hope they have a job, and they will take as much solace as they possibly can in the statements from the Chairman I believe it was.

Mr KIRBY: For me a key flag along those lines is always apprentices. One of the really disturbing comments through the industry out of Victoria was for 10 years - once they split up and sold off they did not employ any junior apprentices for something like 10 years. Through working at Power and Water, we have a massive turnover of staff a number of years ago. We would get tradesmen from down south who struggled to cope with the conditions. They would move into this environment not understanding what the cost of living was, and Power and Water's pay structures at the time would make sure they sat on the bottom pay level for years and people could not afford that. We have done some work around making sure it is more equitable for people, but what really disturbs me is we have already almost halved the

Power and Water apprentice intake this year from other years. That, to me, is a pretty good indication about where things will head.

Mr McCALLUM: Without going into too much detail, Paul has covered most of it, but quite often we have seen in other jurisdictions that through a process of attrition as well as the normal industrial avenues, starting levels are run down in both generation and transmission and distribution. This can still happen under a no redundancies arrangement in EBAs, so there are ways and means absolutely.

Mr VATSKALIS: Paul, just before we ask questions a couple of comments. You are right, the changes in Power and Water started 10 years ago when the CLP government introduced legislation for corporatisation. It was the same government that cut a lot of the workforce and did not spend a lot of money on maintenance that culminated in the explosion at Casuarina Substation.

Mr HIGGINS: It was once they joined NTEC with the water people too.

Mr VATSKALIS: The reality is every government in the Territory has paid subsidies simply because it is such a unique market. If you did not pay subsidies and you lived in Yuendumu you had to pay 75¢ per kilowatt hour rather than what you pay now which is the same as everybody. Under the new arrangements we know they will continue to pay subsidies otherwise we will have the same problem.

I am all for efficiencies, and my comment is if the private sector does so well, why do we not copy the practices and bring them back into Power and Water Corporation and imitate them as efficiencies? There have been admissions there has been economic transparency and we can do things better, but why do we go to this disaggregation of this existing organisation? My major concern is should we have another blackout like before, where you had one organisation dealing with a major problem now you will have three. How will you coordinate three organisations in the middle of the night - generation, transmission and retail? Retail would probably be trying to explain why you have no power, but transmission and generation? Will it be efficient, will it be quick, or instead will we have 12 hours, 24 hours, 48 hours or a repeat of the Auckland experience? Can you assure me this may not happen or how it will not happen? Can this new split guarantee that will not happen?

Mr McCALLUM: In my view it cannot. I think fears that longer lead times for repairs and slower response times to network issues are a real concern. I would point to evidence in other states such as South Australia and Victoria, and the experiences that have followed similar regulatory reforms in those jurisdictions. That is the path they headed down. I do not want to be overly dramatic in referring to the Victorian bushfires, but purely because you

mentioned responding to emergencies etcetera, it was clearly found to be operational issues within network distributors admittedly ...

Mr WOOD: And owned by an overseas company.

Mr McCALLUM: Exactly. So, merely to respond to your point and to offer evidence as to why we have concerns and think it is a possibility.

Mr KIRBY: One of the things highlighted in those significant industry reports we had done in the mid to late 2000s was a big portion of the problem with the network here is a design issue. I do not think anybody ever envisaged the northern part of the Territory would grow to the level it has. That has meant having different parts of plant as a single point of failure - I guess they were called in those reports - does leave us compromised. When you couple that with Territory conditions things have to operate in, if you walk into some of those power station or distribution yards during the middle of the build-up it is a wonder any of that equipment can work. It is amazing it holds up as well as it does, but to clarify we could have had 16 generators available to us that night, but once that distribution part of the equipment failed we were always going to be in trouble.

Unfortunately, sometimes gas does not behave the way it should. It is not the first time that has happened, but to say injecting competition will fix those problems, no, it will not.

Madam CHAIR: Going to reports, you have cited two reports showing that privatisation has failed, but both those reports were commissioned by the ETU. Are there any other reports not commissioned by the ETU that support your position?

Mr McCALLUM: We can definitely find as much historical material as you like. However, I would like to respond to the fact you mentioned those reports were commissioned by the ETU. Yes, they were, but I believe you heard from one report author earlier today who is a Professor of Economics at the University of Queensland. The second report we paid for, but they were independent economists in much the same way the Utilities Commission or the government has engaged Evans & Peck or whoever it is - Clayton Utz etcetera to get advice. That is exactly what we did because they are economists and that is what their speciality is. We were asking a question about financials and economics. We do not have the internal capacity.

I hope you were not inferring simply because they were commissioned by the union they do not carry any weight. That would undercut the professionalism of the authors of those reports.

Madam CHAIR: That was not my question.

Mr KIRBY: Just one comment on that, there is a lady called Sharon Beder who is on public record quite a bit around the risks of privatisation. She has written a book called *Power Face*. To my knowledge she speaks openly and freely about the risks of splitting entities and that in Australia's history that has always led to privatisation in some way, shape or form which has always led to increased costs and decreased services. To my knowledge she has no links to the ETU at all.

Mr HIGGINS: I have said we are not looking at privatisation, and to put it on the record I do not support privatisation of Power and Water okay, full stop.

Mr McCALLUM: Yes.

Mr HIGGINS: The splitting of it, yes, I do, for various reasons, but privatisation, no, okay.

Mr McCALLUM: Yes.

Mr HIGGINS: You said apprentice numbers have dropped since the split up and sale. Did they drop when they were split up or was it the sale? In other words, is it when you privatise that that problem occurs, or do you see that occurring if we split Power and Water?

Mr KIRBY: Well, two things, the information we had from Victoria was around privatisation - was when their trouble started. I have not got a level of history that would tell me if they split or deregulated before that. I would not be able to tell you, but as for the local example in our enterprise agreement for Power and Water it states they will employ at least 12 apprentices. Over the last few years, given the ageing workforce and a reasonably high turnover of staff, they would always employ 22 to 24 apprentices. This year, because of the change of government I suggest, it went back to 12 because that is what is written in the EBA and that was the very least that could be employed at the time.

Mr HIGGINS: I would not put it down to change of government. Government does not tell people how many staff they should employ.

Ms MANISON: Given you are in a fairly unique position to have an insight into what is happening on the ground within Power and Water and with staff, what is the feedback you are getting from staff about Power and Water being ready for the structural separation by 1 July given that is two months away, and how has the internal communication process been?

Mr KIRBY: I guess a few things at the higher level, I am sure there is a massive body of work going on in a pretty short space of time to make sure they are as close to the mark as being ready. On the floor, the changes that will mean for people or their level of understanding, because of the rapid pace it has happened. We have probably got a better understanding of what that will mean for them than they do. There is probably a fair element of the workforce that just do not understand what is coming up and what changes it may make, if not immediately, but certainly in the future.

One personal comment I would like to make is these people live in our community, people that who alongside you and in your street and play in your sporting fields, and to see the way they have been put to the sword around some of the terminology used over the last probably 18 months from pretty early in the piece when the full page advertisements started coming out saying they are a waste of time, a basket case, bloated and inefficient and things like that is pretty distressing.

There are some recent examples for members of a different union from Gove who are going through some significant change where we had, unfortunately, one fatality and a couple of other bad injuries. I have a real concern that people at Power and Water are probably struggling to keep their mind on their work at the moment. Their workload through the Wet Season and the storms will drop off, but that is where their body of project work arks up, so there will still be a high level of work being done. Yes, I have some concerns personally that at some stage people will not have their heads in the game and it is a very high risk industry and a dangerous industry to work in.

Mr WOOD: Probably a more personal question, but what do you think of Power and Water as a business? Some of what I was asking today was if they go down the path of structural disaggregation – because the aim under NEWCO is this will significantly improve the financial transparency of Power and Water's various lines of business, in Power and Water's focus and specialised boards and management and remove certain deterrents to competition. Do you think that is needed in Power and Water when you look at it now?

Mr KIRBY: I understand the comments that have been made around - it is quite convoluted, the tariff arrangement, particularly with remote subsidies and sections of the business that cannot possibly run at a profit in the Territory and those areas being subsidised by areas of Power and Water that can make a profit. I am sure there is always tightening up that can be done to make sure that is more transparent.

As to the point you made earlier that if we already have retail and generation competition in the market why do we need - my query would be why do we need to go to this extent where every example we can find is it will cost significant millions of dollars to set things up

with triple the boards, let alone some of the staff underneath the boards, uniforms, letterheads, the whole lot must be a significant cost involved in that.

Mr WOOD: That is one of the difficulties I have an Independent. Some people say that cost will be covered by Power and Water becoming more efficient. It will reduce some of its costs and that will be the savings it makes by spending that money in the first place. I will go through all the stuff that has been said as well. I do not support privatisation of Power and Water, but we have a responsibility to make sure Power and Water runs efficiently and does not waste our money doing things in a bad way.

My other question is has the government done due diligence to see whether your concerns as to whether this would make sense have been addressed. I have a fair bit of tossing up to do because I have heard lots of different opinions today - the professor, and QEnergy was barracking for the process to change. I want the best for the Territory, but the bottom line is I will not support anything unless I get a watertight guarantee from the government it will not privatise Power and Water. I have other concerns as well, not just hanging on that one issue.

Mr KIRBY: One concern I have is all the people who seem to be speaking heavily in favour for this stand to make something out of it. Is there anybody independent who says this is a fantastic idea?

Mr WOOD: Power and Water said it was. They said today, and I was trying to – that is what I was trying to get out of them - would it make them a better company? Forget the competition, forget the privatisation would it make them a better company. Their argument was, 'We are just about there now, but the advantage of having these boards would be those GOCs would be required to do this all the time'. Whether that is right or wrong, I have to think about some of these things. It is a pity it has been rushed. This is one of the sad things.

These bills really should have been given some adequate time, not rushed. That is one of the problems. That is the way it is at the moment; we cannot change that.

Mr McCALLUM: One of the big things missing from the picture from our perspective is when it comes to trying to decide your view, whether this is a good idea, and weighing up the pros and the cons is there has not been any solid data to say prices will go down this much or it will save - GenCorp and Retail Corp will be X amount of dollars better or worse off. Here is the best case scenario, the worst case scenario, this is the range. Normally you would expect that type of data to be available and accompanying this kind of reform; it is just not there.

Mr KIRBY: From my time at Power and Water, if we had a piece of equipment that was letting us down and wanted to change that - as simple as a bucket truck, a different type of vehicle - we would have to put a cost benefit analysis to \$100 000 piece of equipment to argue that up through the streams before it would be supported. I find it pretty amazing that we can get this far into this discussion and not be able to prove any figures.

One of my real concerns is we heard some figures bandied around from the \$40m and \$70m types of subsidies that the remote and bush rely on. If it took power networks and the Utilities Commission so long to agree on how many cents and dollars they could put their side of the tariff up by, we cannot have any idea of what the effect will be in the remote areas if those profit making portions of Power and Water are to be split off, which they are going to be, and the rest of the Territory taxpayer will be left with the other portions of Power and Water. We have no idea what those costs will be and how that will affect people in the bush. I guess what we understand is when the tariffs first went up a while ago Power and Water had to hire charter planes to get more tokens out into the regions because they were burning through the tokens so much faster than they ever had before.

If you get to a stage of increasing that a fair percentage again a bunch of our bush people will not be able to afford essential services and we cannot guarantee what those costs will be.

Mr McCALLUM: The restructure of the market will necessarily split at least one level, which is the generation level – Darwin-Katherine versus the rest of the market. We briefly raised in our written submission whether this means there is – what does it mean going forward for those people who are not going to be part – or people living in communities who will not be part of the competitive market? Will there be two sets of tariffs for example?

The government has recently been talking about possibly involving federal regulators such as the Australian Energy Market Operator or the Australian Energy Regulator to come in under the new market arrangements and provide the expertise for market governance etcetera. One can only assume the AER and the AEMO will be looking at the wholesale competitive market, but you have so many communities and such a large part of your market outside that one competitive line. What happens there? None of that is here. There is no answer to it and that is really concerning.

Mr WOOD: Are you saying if the tariff stabilised in the city and if the government wanted to stick with its policy of the same tariff in the bush, where the cost might have gone up because of no competition, we would we be paying more to keep that tariff at the city level?

Mr McCALLUM: Yes, that is part of it. On the issue of governance, if it does move to what is proposed and the government has been saying it might get federal regulators in to

look at the competitive market, the competitive market will only be between Darwin and Katherine. What about everything else? What happens to that? That has not really been covered in any detail I have seen publicly.

Madam CHAIR: Thank you both for coming. Lance, you travelled to be here today so thank you very much. I really appreciated your contribution to our inquiry and we hope you enjoy the rest of your afternoon. Thank you very much.

Mr McCALLUM: Thank you very much, I appreciate being here. Thanks for the robust discussion, have a good night.

Madam CHAIR: That concludes the public hearing today into the separation of the Power and Water Corporation. On behalf of the committee I would like to thank committee staff and all our witnesses for coming along, and for my colleagues for participating in the inquiry. Thank you.

DRAFT