



8 February 2011

Submissions
Electricity Review
PO Box 123
HOBART TAS 7001

RE: ELECTRICITY SUPPLY INDUSTRY EXPERT PANEL – STATEMENT OF APPROACH

Aurora Energy (Aurora) appreciates the opportunity to provide comments on the Tasmanian Electricity Supply Industry Expert Panel's Statement of Approach for its review of the Tasmanian energy industry.

Introduction

Aurora is a fully integrated energy and network business with complementary activities in telecommunications and energy related technologies. Aurora owns and operates the natural gas-fired Tamar Valley Power Station in northern Tasmania and wholesales electricity and natural gas in south-eastern Australia. It retails electricity to all grid-connected homes and most businesses in Tasmania as well as business customers interstate. It also retails natural gas to Tasmanian customers and owns and maintains Tasmania's electricity distribution network.

The Tasmanian energy industry is at a critical point, with the upward pressure on electricity supply input costs continuing to put parallel pressure on the cost to customers for the electricity they use. Effective future energy market arrangements are vital for the State, for energy consumers, for Aurora and for the other Government-owned energy businesses.

Aurora is therefore fully supportive of this review and considers that it is well placed to make a valuable contribution to the process.

General Comments

Aurora considers the Statement of Approach a balanced presentation of the key issues for the Panel to consider. It is evident the review will balance the need to review major developments and historical decisions as well as future pressures. Aurora supports this to the extent that ex-post analysis will inform potential implications of future changes, and notes that any changes that have occurred in the past have aimed to improve the industry and outcomes for both contestable and non-contestable customers.

*From the Office of the
Chief Executive Officer*

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A significant number of matters relevant to the review have been highlighted in the Statement of Approach, which provides a clear process and logical steps for input and consultation. Overall Aurora considers that the methodology is sound.

Aurora appreciates the opportunity to provide input to a variety of information papers and values the Panel's approach of engagement and open dialogue as being vital to the success of the review. Specific comments regarding the Panel's approach to the review are set out below.

Timetable for the Review Process

The Panel has acknowledged the unique characteristics of the Tasmanian energy market in its Statement of Approach and has identified the need to determine the similarities and differences of the Tasmanian context with that of other jurisdictions, determining to do this via consultation with market participants and key stakeholders including members of the general public.

This process of in-depth consultation is definitely required and will also build engagement and understanding, as well as confidence in the process. In addition, the Statement of Approach sets out a breadth and depth of analytical rigour necessary for such a review. This has, however, resulted in an involved and time intensive undertaking.

Whilst there is a fine balance between creating an unnecessarily protracted process and one which is efficient enough to achieve a good outcome, Aurora's position is that the timeframe proposed is insufficient to allow for all issues to be identified and analysed appropriately and for all stakeholders to be adequately consulted through hearings, public forums and responses to issues papers. As such, Aurora would be supportive of the Panel seeking an extension of the timeframe should the Panel require one.

In addition it would be preferable for the review to allow for the evolution of key energy industry developments including the Australian Government's climate change policies and the introduction of a carbon tax and the commencement of the Tranche 5a contestable market segment in Tasmania.

Aurora is also committed to the preparation of Aurora's first submission to the Australian Energy Regulator (AER) for the network pricing determination process (due for submission on 30 May 2011 and a draft determination released during November 2011).

Given the above factors, it is suggested that a final report by 31 August 2011 may be a challenging deadline for the Panel to meet, particularly given the complexity of the relevant issues and the interrelationships between the various processes that are ongoing. Releasing the Draft Report for comment significantly later than an approximate date of June 2011¹ would enable policy and regulatory frameworks to evolve and inevitably provide a much better outcome for all stakeholders.

¹ As derived from estimations within the Review Road Map. Electricity Supply Industry Expert Panel - Statement of Approach. 2010: 13

Aurora thus suggests that a final report released closer to the end of the calendar year, rather than the proposed date of 31 August 2011, may prove to be a more realistic timeframe.

Terms of Reference

In its Terms of Reference, the Panel has been asked to consider the advice that was provided to the State Government by the senior management or Directors of Aurora Energy from 1 October 2009 to 16 June 2010 inclusive (ToR 8).

In November 2010, the Auditor General completed his investigation into the Government's election commitment to cap prices and the information provided by Aurora regarding its financial position. The Auditor General considered extensive input from Aurora covering the period in question as well as from Treasury and the Treasurer, and his findings were published and tabled in Parliament (Special Report Number 94).

Aurora understands that the Auditor-General Report directly addresses the issues that were raised at the time that Parliament included ToR 8 in the Terms of Reference for the Review. Accordingly, the Auditor-General's report could be considered as already meeting ToR 8.

The Terms of Reference also explicitly indicates that non-contestable customers will be part of the review process (ToR 2) and also infers that the efficiency and effectiveness of the Tasmanian energy industry, which includes both contestable and non-contestable customers, will be considered (TOR 1). However, there is no direct reference to the contestable market as a direct input into the Terms of Reference for the Review.

The Panel's Statement of Approach has identified a need to understand the contestable market issue in the context of "...the level of competition at the retail level in the contestable market, the factors that drive it, and the opportunities to increase it". Aurora fully supports the Panel's approach, and notes that as the issue of retail competition is inextricably linked to the effectiveness of the wholesale energy market in Tasmania, the Panel should also consider an analysis of the performance of the wholesale energy market and how it operates as a key input into the Review process.

Delivering a Sustainable Sector

In considering the Panel's Statement of Approach and the potential pathways to change for the future for the Tasmanian energy industry (competitive, regulatory and governance frameworks), it is inevitable that any scenario-analysis work will have a number of criteria to apply to the investigation process. These may include:

- Price and customer impacts – and whether the outcome encourages a competitive discipline on price;
- Efficiency – what efficiencies or economies of scale benefits may be achieved through a particular action;

- Market Structure/ Competition – whether (and how) changes to the industry structure may reduce or remove barriers to entry, and allow for participants to enter (or exit) the market; and
- Shareholder value – the potential impact of an action on shareholder value in the Government Business Enterprises and State Owned Enterprises as well as the broader implications for the Tasmanian economy.

The notion of price and more specifically the impact that any industry decision or activity will have on energy prices is undoubtedly, and rightly, a key driver for the review. However ensuring the balance between ‘lowest prices’ and ‘shareholder value’ is particularly important in the Tasmanian context, given the inextricable link that all of the energy businesses have with the State’s economy. For example:

- As a State owned entity, any dividends are returned back to the Government for investment back into Tasmania;
- Providing electricity to major industrial businesses, as well as small-medium businesses across the State, is an integral contributor to the economy through the outputs of these businesses as well as the employment that is created; and
- The three energy businesses are major employers of Tasmanians, with Aurora alone employing more than 1300 people and spending \$153.6m in 2009/10 on supplier contracts, in many cases with local businesses.

In addition, the Statement of Approach identifies the Panel’s interpretation of the Terms of Reference as being:

“...To consider regulatory, governance and structural reform options that could enhance the efficiency of price outcomes in Tasmania without jeopardising other key objectives such as security of supply, reliability or the financial sustainability of the sector”²

Whilst sustainability of ‘the sector’ is arguably a broad definition encompassing many aspects of the energy industry, the three energy businesses play a key role in helping the Tasmanian Government to fulfil the social responsibility aspect of its function, via the financial returns that the energy businesses provide to the State, which enable the Government to provide broader public services and important infrastructure to the community.

Implementation Issues

As with any change to the status quo, deciding to proceed with a particular course of action will have trade-offs or opportunity costs. Accordingly, it will be important for the Panel to give some focus to the implications of the potential changes, the implementation issues that are evident, as well as the potential costs attached to these issues given the result of the review could again lead to significant reform of the industry. In broad terms, the implementation issues that could be considered may include:

² Ibid. Page 9

- Legislative change and potential impediments;
- Corporate activity through merger or demerger issues;
- Commercial renegotiations, possibilities and challenges; and
- Management of potential loss in asset values.

Aurora recognises that there are many reform options and variations to consider for the Tasmanian energy market as part of this review. Aurora would like to again emphasise its willingness to participate in any part of the review process to achieve an outcome that is in the best interest of Tasmanian energy consumers and for the State in general.

Thank you again for the opportunity to provide comment on the Statement of Approach document. Should any member of the Panel or the Panel Secretariat require clarification on any aspect or would like to discuss any of the matters raised in this submission, please contact Rick Inglis, General Manager Strategy and Corporate Affairs in the first instance, on telephone 6237 3314.

Yours sincerely

A handwritten signature in cursive script, reading "Darren Smith". The signature is written in black ink and is positioned above a horizontal line that spans the width of the page.

Darren Smith
Acting Chief Executive Officer