

## Part Three

### Specification

#### Introduction

*The Electricity Supply Industry Expert Panel Act 2010* (the Act) establishes an independent Panel to conduct an investigation into, and provide guidance to Parliament on, the current position and future development of Tasmania's electricity industry. The terms of reference for the Panel require it to investigate and report on:

1. The current efficiency and effectiveness of the Tasmanian energy industry with particular reference to the existing regulatory framework and the cost and operation of the energy industry elsewhere in Australia.
2. The primary factors that have driven recent increases in non-contestable electricity prices in Tasmania including the impact of major infrastructure development decisions.
3. The competitiveness of non-contestable electricity prices in Tasmania compared with those in other states.
4. The financial position of the state-owned energy businesses: Transend Networks, Hydro Tasmania and Aurora Energy.
5. The impact of interaction between the three state-owned businesses on the effective operation of the Tasmanian energy industry and Tasmanian energy prices.
6. Having regards to trends in electricity prices and market developments at the national level and Tasmanian-specific circumstances, the implications of Tasmania's market and regulatory arrangement for electricity tariffs over the coming years.
7. Actions that would guide and inform the development of a Tasmanian Energy Strategy particularly in relation to the Government's primary objectives of minimising the impact on the cost of living in Tasmania and ensuring Tasmania's long term energy sustainability and security.
8. 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.
9. Any other matters that the Expert Panel considers are relevant to the above matters.

The Panel is supported by a small Secretariat, which is responsible for:

- managing and undertaking the detailed work program under the direction of the Panel;
- undertaking research relevant to the review;
- represent that Panel in engaging with stakeholders on issues relevant to the Inquiry; and
- the development of papers, advice and other materials for the Panel's consideration and the preparation of reports on its behalf.

The Panel is seeking to appoint a financial advisor to assist it meet its Terms of Reference. The principal focus of the consultancy is to address Terms of Reference 4 – the financial position of the state-owned energy businesses (SOEBs), although advice relevant to other aspects of the Panel's scope will also be required.

The successful Tenderer will be expected to work closely with the Secretariat in fulfilling this assignment. A key element of the selection decision is the ability of the Tenderer to work with the Secretariat to enhance its understanding of the detail financial matters relevant to the scope of this assignment, noting that the Secretariat members are non-expert in financial matters (but do have relevant backgrounds).

### **Objectives of the Consultancy**

Through the completion of this consultancy, the Panel is seeking to achieve the following objectives:

1. To understand the financial performance of Hydro Tasmania, Aurora Energy and Transend Networks, specifically:
  - the entities' historic (since disaggregation) and expected (future 5 years, or as far as the Corporate/business plans forecast) financial performance. To understand the sources of value within each of the electricity businesses, how this has changed over time and to identify the financial flows between the entities and how this has moved value over time.
  - the relative contributions to business value and shareholder returns from 'core' electricity activities (generation, transmission, distribution and retail on mainland Tasmania) and business diversifications<sup>1</sup>. The Panel wishes to understand the implications of the diversification strategies on risk, capital needs, management and Board focus.
  - the comparative financial performance with like entities elsewhere in

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<sup>1</sup> In the case of Hydro Tasmania, diversifications are Entura (Consulting), Momentum and Roaring 40s. In the case of Aurora Energy, diversification include telecommunications and mainland activities. In the case of Transend Networks, diversifications include non regulated activities, principally telecommunications.

Australia (or internationally if that is the better basis of comparison, for example, for Hydro Tasmania).

2. To understand how the electricity businesses and Government have balanced the trade-offs between debt, returns and business growth. The Panel would like to identify the aggregate current and future (10 years) capital needs of the electricity businesses (separating core capital needs and growth/diversification), the projected sources of funding and implications for risk.
  - In this regard, it should be noted that a capital structure review of the 3 entities has been recently completed and is available to the Panel. That Panel does not wish to redo this work.
3. To understand the likely benefits, consequences and risks of the integration of Aurora Networks and Transend Networks and the implications for Aurora's residual businesses, particularly the energy business.
  - The Panel has available to it work undertaken on behalf of the Government that provides a high-level estimate of the gains available from combining the two network entities into a single business.
  - The Panel understands that Aurora Energy and Transend Networks have been working together to identify and capture joint savings through integration measures that do not involve common ownership. A key objective will be to identify the net gains available from common ownership and more fully document the likely costs and risks of this approach.
4. To compare the shareholder oversight model for Tasmanian Government businesses with institutional investor arrangements in the private sector and/or shareholder oversight models in other jurisdictions and identify areas for improvement.

The Panel considers it important that its findings and recommendations are supported by rigorous qualitative and quantitative assessments. On this basis, the Panel is of the view that an integrated financial model of the State-owned electricity businesses will be important for its work program to enable it to examine the financial implications of proposed structure, regulatory and governance arrangements.

Tenders should outline their experience in developing integrated financial models with the purpose of exploring policy options in their bid. The proposed fee for model development should be separately identified in the bid, assuming that the model needs to be compiled from scratch<sup>2</sup>.

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<sup>2</sup> The Tasmanian Department of Treasury and Finance has a financial and market model (referred to as the FEMM) that it developed with the assistance of IES. An early task for the successful Tenderer will be to examine the applicability of the FEMM to meet the Panel's requirements, in conjunction with Treasury and the Secretariat. This may provide a

The Panel considers it very important that the model be successfully 'handed over' to the Secretariat for use, and Tenderers are requested to explain the strategies that they will deploy to ensure this occurs.

### **Other work streams**

The Panel will be progressing other work programs that will interconnect with this financial analysis consultancy. At this time, the Panel anticipates working with specialist advisers to examine:

- the efficiency and effectiveness of the SOEB; and
- competition analysis, particularly in the generation.

The Panel has yet to consider its need for market modelling resources, but it is likely that some expert advice in this regard will be sought during the Review.

The efficiency and effectiveness work will examine how the technical performance and cost structures of the SOEBs have changed over time, and how they compare with relevant peers. It will examine the major cost drivers for each entity, their cost accounting/control methodologies and their internal processes that govern major capital expenditure, along with the entities' broad approach to asset management. Clearly, the interplay between these issues and the market (in the case of generation and contestable retail sectors) and the regulatory framework (in the network and non-contestable retail sector) will drive the financial performance of the entities.

In relation to the competition analysis, the focus of the work will be to identify the nature and extent of Hydro Tasmania's market power in the generation sector (spot, contract and FCAS markets), identifying the impact of that market power and to work with the Panel on means of addressing it. Policy responses to identified market power issues will need to be assessed from a number of perspectives, including their financial impact on the entities – establishing net impacts and identifying transfers of value will be important.

With the above in mind, it will be very important that each of these work programs maintain close relationships with Secretariat to ensure that there is no duplication in effort and that all three bodies of work come together in an integrated manner for the Panel's consideration and reporting purposes.

Moreover, the Panel anticipates that some level of cross-involvement and input will be advantageous between the work streams, although the exact scope of this involvement is unclear at this stage.

The Panel anticipates that once these three 'fact finding' assignments have been concluded, a subsequent package of work will be issued to relevant advisors work

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reasonable starting point to meet the modelling needs of the Panel.

collaboratively with the Panel and Secretariat to develop and/or assess the potential impact of structural, regulatory and governance reforms that would underpin the Panel's draft recommendations. This work is **not within the scope** of this tender.

### **Time frames**

The assignment will commence as soon as practical. It is anticipated that the Tender process will be resolved and the contract awarded in early April.

The Panel wishes to publish interim findings on the financial performance of the entities in August 2011, meaning that the Tenderer will be required to produce a report on Items 1 and 2 above in mid-June 2011.

The financial model will be a key tool in assessing the impact of reform options. It would be desirable to have the model operational within 8 weeks of the commencement of the assignment.

The work on network integration is not as time critical as that above, and could be delivered in late June 2011. Advice in relation to the shareholder oversight arrangements could be provided in mid July.

### **Methodology**

This brief highlights the Panel's objectives for the assignment, and deliberately does not specify how it believes Tenders should go about meeting those objectives. This is a central issue for Tenderers, and the clarity and quality of the proposed methodology is a critical element of the selection decision.

Tenders are required to explain how they will go about achieving the objectives of the consultancy and to identify, *inter alia*:

- the issues that they would seek to address in meeting the assignment objectives, separately discussing items 1-4 noted above;
- the nature of the involvement of each nominated team member.
- the types of information that they would need to obtain (noting that the Panel has wide ranging information gathering powers under the Act);
- the way in which they would interact with the Secretariat;
- the way in which they would interact with the SOEBs.

The Consultant will be required to enter into a Tasmanian Government standard Contract for Services Agreement (proforma attached) and should note that expenses for travel, accommodation and allowances are required to be charged at rates allowable to State Government employees.

## Selection Criteria

The selection of the successful Tender will be made according to the following selection criteria and weighting:

Criteria	%
Demonstrated experience of the firm and proposed team members in analysing the business performance of electricity entities.	15
Demonstrated understanding of the Tasmanian electricity supply industry and the State-owned electricity entities.	10
Demonstrated understanding of the issues, constraints and implications of Government ownership of commercial enterprises.	10
Clarity and quality of methodology.	20
Demonstrated ability to work with non-experts clients.	10
Demonstrated experience in effectively handing-over analytical tools to clients for ongoing use	5
Price (hourly rates and overall fee).	30

## Information to be provided by the Tender

Tenderers are to provide:

- completed Tender Form
- a response to the Selection Criteria
- CVs for all team members and a clear articulation of the roles that each would play in fulfilling the objectives of the assignment, with a reference to past performance of similar roles
- contact details for at least two client referees able to confirm the Tenderer's ability to meet the Selection Criteria
- pricing structure, including fees and methodology for charging services – **estimated time of each team member and the costs per hour must be shown**
- Tenderers must provide a copy of the original Tender, marked accordingly, plus three hardcopies or an electronic copy on CD.
- details of the Tenderer's insurance cover, including type and amount of cover, policy number, name of insurer and policy expiry dates; and

A Tenderer lodging a Tender using the Electronic Tender System must lodge the Tender in accordance with one of the formats and with the naming conventions specified in Clause 15.