LEGISLATIVE ASSEMBLY FOR THE AUSTRALIAN CAPITAL TERRITORY

STANDING COMMITTEE ON FINANCE AND PUBLIC ADMINISTRATION
(INCORPORATING THE PUBLIC ACCOUNTS COMMITTEE)

INTERIM REPORT ON

PROPOSED ACTEW/AGL PARTNERSHIP ARRANGEMENT

Finance Committee Report No 7
June 2000

RESOLUTION OF APPOINTMENT

The Standing Committee for the Chief Minister's Portfolio was appointed by the Legislative Assembly on 28 April 1998 to examine any matter under the responsibility of the Chief Minister's portfolio. The Assembly also resolved that the committee perform the duties of a public accounts committee, specifically:

(a) to examine:

   (i) the accounts of the receipts and expenditure of the Australian Capital Territory;

   (ii) the financial affairs of authorities of the Australian Capital Territory; and

   (iii) all reports of the Auditor-General which have been laid before the Assembly;

(b) to report to the Assembly, with such comments as it thinks fit, on any items or matters in those accounts, statements and reports, or any circumstances connected with them, to which the Committee is of the opinion that the attention of the Assembly should be directed; and

(c) to inquire into any question in connection with the public accounts which is referred to it by the Assembly and to report to the Assembly on that question.

On 26 November 1999, the Assembly retitled the committee as the Standing Committee on Finance and Public Administration (Incorporating the Public Accounts Committee), omitted reference to matters under the responsibility of the Chief Minister's portfolio and included reference to women's affairs, Aboriginal and Torres Strait Islander issues, asset management, gaming and racing and any other related matter.

MEMBERSHIP OF THE COMMITTEE

Mr Ted Quinlan MLA Committee Chair

Mr Trevor Kaine MLA Deputy Committee Chair

Mr Greg Cornwell MLA

Secretary: Bill Symington
Consultant to the committee: Mr Ted Mathews

1. COMMITTEE STATEMENT

1.1. The purpose of this interim report is to inform the Assembly of the committee's role on behalf of the Assembly in monitoring the path by which the proposed partnership arrangement between ACTEW and AGL is being brought to fruition as anticipated by the parties.

1.2. Some four months ago the ACTEW and AGL were firmly of the view that the arrangement would be settled and formal agreement reached before the end of June 2000. The committee has met regularly, generally on a weekly basis, with the parties and has received fulsome reports on progress with negotiations. In the most recent briefings it was clear that while there has been significant progress towards completion of a range of subsidiary agreements, several important issues had yet to be resolved. As a consequence the committee was advised that formal completion of the arrangement was unlikely before July.

1.3. This interim report outlines the thrust of discussions between the committee and relevant parties to this point. It is considered important that the committee account to the Assembly on what has been happening, before the winter recess. The committee anticipates that its final report will be released during July or early August.

Scrutiny framework

1.4. The overall project is one of significant complexity, employing a raft of specialised professional involvement as well as considerable resources from ACTEW, AGL and the ACT Administration. The committee has adopted a strategic approach, focussing on primary outcomes and risks. Practically, it could not embroil itself in the minutiae of all or any of the elements of the project. Prime responsibility for scrutiny rests with the ACTEW shareholders, the ACTEW Board and the independent probity Auditor who have had the opportunity for close involvement in negotiations on a day-to-day basis.

1.5. The committee's final report will be based upon the information provided at the reporting date. It will be constructed to complement reports that are anticipated to be provided by the Government (or shareholders), the appointed independent valuer, and the independent Probity Auditor who is directly accountable to the Assembly.

1.6. The committee's final report cannot deal with or pursue every issue to its conclusion and it will not seek to justify the totality of the final partnership arrangements or otherwise. Rather, it will attempt to advise the Assembly on the extent to which the promised benefits of the venture have been realised and what collateral risks will remain. It may also contain identification of matters that the Assembly might wish to consider as requiring further Assembly direction.

Roles of ACTEW and AGL in discussions

1.7. The committee and the parties have benefited from open and frank discussion and exchange of views. ACTEW and AGL have fully met the reporting undertakings they gave the Assembly and have been open and transparent in their dealings with the committee and responses to questions. ACTEW appears to have handled its side of the negotiations in a competent and professional manner.

1.8. The committee also appreciates ACTEW's undertaking to provide a report, when the transaction is completed, on the key features of the final arrangements and how they have secured the promised benefits and dealt with collateral risks. This report should provide a focus of accountability for the Assembly in assessing the arrangements and monitoring the future partnership operations.

Disclaimer

1.9. The establishment of a partnership agreement has the Assembly's advance in-principle support. The committee has determined that it will not reflect on that decision. However, committee members hold individual opinions, and obviously reserve the right to express their views in any consequent debate both in the Assembly and beyond.

BACKGROUND

1.10. On 9 March 2000 the Assembly enacted the *ACTEW/AGL Partnership Facilitation Act 2000* the purpose of which is to facilitate the process and establishment of any future agreement between ACTEW and AGL to form a joint venture by way of partnerships between subsidiaries of each company for the provision of electricity and gas, and for the undertaking of certain water and sewerage operations and maintenance activities.

1.11. Under the Act, ACTEW will retain ownership of assets, rights and liabilities associated with water and sewerage operations and will contract the partnership to maintain, manage and operate these business activities. ACTEW and AGL will vest other existing assets, rights and liabilities in one or more joint venture entities or the joint venture partnerships owned by them.

1.12. ACTEW will have a beneficial interest of not less than 50% in the Partnership and will appoint 50% of the directors appointed to the board of the

Partnership. ACTEW employees will be seconded to the joint venture entities and ACTEW will delegate certain powers to the joint venture entities. The employees will remain employees of ACTEW.

1.13. The accounts and records of the partnership will be jointly audited by the ACT Auditor-General and an auditor appointed by AGL. The Independent Pricing and Regulatory Commission (IPARC) will make price determinations and be responsible for access and other issues normally falling within its jurisdiction.

Committee's role

1.14. On 9 March 2000, the Assembly also noted, and availed itself of, an offer by ACTEW and AGL jointly to provide fulsome reports on progress of the negotiations to the Assembly and to appear before relevant committees to answer questions. The Assembly further resolved that after consultation with this committee, the Treasurer appoint an Independent Probity Auditor to oversight the establishment of the proposed partnership arrangements. In this regard Mr Stephen Marks of Stephen Marks and Co Pty Ltd was nominated and subsequently appointed by the Treasurer.

1.15. The committee forthwith began a series of regular consultations with ACTEW/AGL and the Independent Probity Auditor. On 30 March 2000 the committee notified the Assembly that it had resolved to inquire into the proposed ACTEW/AGL Partnership Arrangement as a formal means of enabling it to report to the Assembly in due course on the outcome of its consultations with the parties and the Independent Probity Auditor.

1.16. As mentioned earlier, the committee's involvement in the proposed ACTEW/AGL Partnership Arrangement has been to monitor developments having regard to regular reporting by the parties and the Probity Auditor. This approach has been consistent with the enactment of the *ACTEW/AGL Partnership Facilitation Act 2000.*

1.17. It has not been the committee's function to assume any responsibility the ACTEW shareholders have to be accountable to the Assembly about the partnership arrangement with AGL. It remains the responsibility of the shareholders and the Probity Auditor to satisfy the Assembly that the Territory interest has been properly considered and protected in relation to crucial issues including:

- Due diligence
- A fair and equitable agreement
- The legality of the agreement and regulatory issues
- Staffing and employment

- Energy network and retail businesses
- Water and sewerage business
- Valuation
- Taxation issues

Committee approach

1.9. The principal objectives within the focus of the committee have been:

(i) the evolving state of negotiations on the heads of agreement, including key milestones and timing
(ii) the corporate and financial structure of the new organisation
(iii) the asset structure including valuations
(iv) due diligence and related matters

1.10. Having regard to the complexity of the issues and the limited time available for the committee to pursue them in depth the committee engaged the services of Mr Ted Mathews, from Price Waterhouse Coopers, a former senior executive in the Federal public service with extensive high level policy experience in the electricity and gas industries. Mr Mathews assistance proved to be of considerable value to the committee.

1.11. It was agreed that ACTEW and AGL would meet with the committee on a regular basis. These meetings were held and the Probity Auditor was present at most. The committee also had separate meetings with the Probity Auditor and there were a series of informal discussions between committee representatives, the parties and the Probity Auditor. In addition, the committee met with the Treasurer as one of the two ACTEW shareholders.

2. PROBITY AUDIT

2.1. The independent Probity Auditor was required to specifically address the following terms of reference:

(1) To ensure that due processes are followed at all stages of negotiation of the proposed Joint Venture
(2) To ensure by the provision of proposer independent and professional advice the interests of ACTEW shareholders are protected and that any agreement is fair and equitable
(3) To ensure by the provision of proper independent and professional advice the contract governing the Joint Venture complies with the law and any resolution of the Assembly or other pre-existing undertaking by ACREW (for example, jobs guarantee)
(4) To ensure the final contract reflects all Terms and Conditions and agreements and there are no side or undisclosed agreements

(5) To ensure the probity of the selection process for the engagement of all advisers

(6) To take action to address all conflicts of interest issues as and when they might arise.

2.2. The committee met regularly with the Independent Probity Auditor who, at various times advised that:

- He or his senior representative attended most meetings of the steering committee (comprising ACTEW, AGL, Arthur Anderson Corporate Finance, Macquarie Bank Ltd and Malleson Stephen Jaques, Gillbert and Tobin) established to oversight the negotiation of the proposed joint venture
- He or his senior representative attended a number of the working groups established to progress the joint venture as an observer to ensure that due process was followed.
- He or his senior representative met on a regular basis with ACTEW executives and the Under Treasurer to provide independent professional advice on issues raised, and met with AGL executives as required
- There had been briefings with Malleson Stephen Jaques, Gillbert and Tobin in regard to some of the agreements which are to form the basis of the final contract and comments had been provided
- He was satisfied as to the probity of the selection process relating to the engagement of the legal and financial advisers for the proposal
- He had sought statements from all advisers to the effect that they do not have any conflicts of interest and in two cases had sought additional information as to how they would address the possibility of perceived conflict of interest
- He had ensured a clear audit trail through minutes and action lists for the steering committee and working groups.

2.3. As indicated earlier, final agreement between the parties has yet to be reached and until then the Probity Audit cannot be completed. The Probity Auditor’s report, when the partnership arrangements are finalised, will be an important element in the Assembly’s assessment of the arrangements.

3. MULTI-UTILITY IMPLEMENTATION AGREEMENT

3.1. The principal vehicle covering the joint venture is a Multi-Utility Implementation Agreement.

Negotiations and timing

3.2. The Multi-Utility Implementation Agreement signed between the parties on 24 March 2000 has acted as a project control document for the negotiations and provides *inter alia* that:

- The parties negotiate to form the multi-utility joint venture
- ACTEW's water and sewerage assets remain with ACTEW, with the joint venture to provide maintenance and operations services to ACTEW on a contract basis
- As envisaged at the time, the joint venture to include 2 partnerships – one for distribution of gas and electricity, the other for retailing gas and electricity
- ACTEW to contribute its electricity distribution and retail businesses to the partnerships
- ACTEW may contribute its other businesses to the joint venture subject to satisfactory due diligence and agreement between the parties as to valuation of each of the other businesses
- AGL to contribute its gas distribution and retail businesses in and around the ACT and other assets to the partnerships
- A party and/or its subsidiary may receive a payment based on the difference in the value of the contributions of the parties to the joint venture
- The parties to attempt to agree on the terms of establishment agreements for the joint venture
- Completion of the joint venture is conditional, among other things, on each party performing satisfactory due diligence

3.3. At that time, the anticipated date for implementation of the agreement was 30 June 2000 with, in the lead-up to implementation date, completion of the following milestones during the period March-June 2000:[1]

- Due diligence and further commercial investigation
- Legal documentation and negotiation
- Business structure and business plan development
- Valuation/financial modelling analysis.

[1] Presentation to committee by the parties 24 March 2000

Corporate governance

3.4. The parties advised the committee that each would be entitled to appoint three members of the management committee and that all decisions of the committee must be unanimous. The joint venture chief executive, to be appointed initially by the parties but thereafter by the joint venture management committee, will be a non-voting member of the committee.[2]

Territory Owned Corporations (TOC) Act 1990 and relations with the Legislative Assembly

3.5. The committee notes that ACTEW and its wholly owned subsidiaries will continue to be regulated by the TOC Act. Accountability by the joint venture will be subject to the *ACTEW/AGL Partnership Facilitation Act 2000* while any decision to invest in the proposed gas fired power plant would be subject to approval under the TOC Act.

3.6. Following implementation of the joint venture the corporate governance of ACTEW will remain subject to corporations law as well as the TOC Act. The Chief Executive of ACTEW will continue to be responsible to the ACTEW Board for the administration of the ongoing functions of ACTEW and particularly management of water and sewerage operations and maintenance agreement and ACTEW’s relationship with its partner subsidiaries.[3]

Shareholder value

3.7. The valuation principles in Schedule 2 of the Multi-Utility Implementation Agreement set out the contributions to be made to the joint venture by the two parties, deals with surplus assets and establishes that the respective contributions be assessed on the basis of fair market value, and open book process and arm’s-length commercial arrangements.

3.8. The primary valuation methodology is the discounted cash flow approach.[4] The approach for the DCF methodology will broadly involve cash flows to discount, a projection period (to be determined for each component to be contributed), rates of return (to be agreed), terminal value calculation, tax treatment, revenue price paths, operating cost assumptions, capital requirements, depreciation allowances, balance sheet items at completion date, certain macroeconomic assumptions, accounting policies and full transparency of workings by an open book process.

3.9. The parties advised the committee that they had agreed to determine a value of their respective contribution to the joint venture and then to agree to a

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[2] report to committee dated 5 May 2000

[3] ditto

[4] ditto and Responses to questions raised by the committee dated 13 April 2000

single valuation of each contribution.[5] The parties were to agree to a suitable equalisation payment to ACTEW which acknowledged that the value of ACTEW's contribution will be greater than that of AGL.

3.10. The ACT Government independent valuer was to begin an assessment in the week beginning 19 June 2000.

Working groups

3.11. By early April a series of joint working groups had been established to progress the joint venture, those groups being:[6]

- A steering committee
- Retail businesses group
- Network businesses group
- Water and sewerage group
- Staff services group
- Partnership agreement group
- Regulatory group.

3.12. A steering committee was also established within the ACT administration, chaired by the Chief Executive of the Chief Minister's Department and including senior representation from the Departments of Urban Services, Justice and Community Safety, and Treasury and Infrastructure, in connection with the proposed partnership arrangement with the role of setting a timetable to progress legislative and other measures, to monitor developmental steps to ensure that each of the ACT's entities adhered to timelines and to monitor progress of utilities legislation in tandem with the proposed partnership.[7]

4. STATE OF PLAY AS AT 23 JUNE 2000

4.1. The committee last met with ACTEW and the independent Probity Auditor on 23 June when ACTEW provided a comprehensive status report prepared by ACTEW with input from AGL in relation to progress with all the elements of the joint venture. This report is fulsome, providing substantial detail about the commercial negotiations as at 23 June. In summary, the position with negotiations as presented by the parties is:

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[5] Report to committee dated 19 May 2000
[6] Presentation to committee by the parties 7 April 2000
[7] Chief Minister letter to committee dated 26 April 2000

(1) Commercial negotiations are at an advanced stage. As indicated below, the Probity Auditor has not identified any issues in relation to the probity of the conduct of negotiations. The Independent Valuer has commenced a review of ACTEW's approach to valuation

(2) The parties have reached in principle commercial agreement in relation to most key commercial issues outstanding between them

(3) The parties have reached in principle agreement in relation to valuation assumptions to be used to agree the value of their respective contributions to the joint venture. These principles accord with those annexed to the Implementation Agreement

(4) The parties are close to agreeing, and expect to be able to reach agreement, on the final range of amounts ("Expected Valuation Range") for the equalisation payments from AGL, to ACTEW ("Equalisation Payment”)

(5) Substantial progress has been made towards finalisation of the Umbrella Agreement, the Distribution Partnership Agreement, the Retail Partnership Agreement, the ACTEW Staff Services Agreement, and the Water and Sewerage Operations and Maintenance Agreement

(6) The current drafts of the agreements may change through the addition of detailed schedules, as a result of final negotiation, following detailed tax and accounting review, or through the need to ensure all of the agreements operate as an interrelated package. At this stage, it is not expected any further changes or additions will be material or controversial

(7) The parties are in the process of negotiating, in legally binding form, the In Principle Commercial Agreement for the AGL Network Services Agreement, the AGL Retail Services Agreement, the AGL Gas Wholesale Agreement, and the AGL Electricity Trading Agreement. The substantive commercial negotiations between the parties have been concluded but there is the potential for further amendment as drafting is finalised over the next several weeks

(8) The parties are negotiating the detailed terms of the Completion Agreement. This agreement, in particular, requires careful drafting and review (commercial, accounting and tax) to ensure it accurately reflects the position between the parties in relation to payment, adjustments to payment, and identification of assets and liabilities to be included in or excluded from the joint venture. There is expected to be considerable drafting and negotiation of this agreement at a technical level. At this

stage, there is not expected to be further substantive commercial negotiation between the parties

(9) The ACTEW Board and the ACTEW shareholders have been kept fully informed of the status and progress of negotiations between the parties. The Board and shareholders have expressed general satisfaction with the status and progress of negotiations, and in relation to the positions reached by ACTEW on the In Principle Commercial Agreement and the Expected Valuation Range

(10) The ACTEW and AGL negotiating teams are continuing to progress the matters referred to in (1) to (8) above. This process is expected to conclude between 3 and 7 July

(11) Following that process, ACTEW Management expects to be in a position to seek authorisation from its Board and shareholders for the final Equalisation Payment within a defined range, and any outstanding commercial or contractual matters with AGL in the final agreement

(12) Final negotiation of these matters and finalisation of documentation is expected to conclude between 13 and 21 July

(13) The ACTEW Board will then make a final decision in relation to the Joint Venture proposal and seek formal approval of the ACTEW shareholders to that decision

(14) It is anticipated that the ACTEW shareholders will continue to take advice from the steering committee chaired by the CEO of the Chief Minister's Department. That committee will continue to seek advice from the Probity Auditor and the Independent Valuer throughout this process and in relation to its advice to Government.

4.2. The committee was advised that although commercial negotiations are at an advanced stage other detailed matters in the status report are potentially subject to fine tuning to take account of the respective commercial interests of the parties.

Probity Auditor's interim report to the committee

4.3. The Probity Auditor provided an interim report to the committee at the 23 June meeting which advised that the negotiation process between ACTEW and AGL had been closely observed and minutes of meetings, due diligence reports and other documents and correspondence had been examined. The Probity Auditor concluded that to this stage due process had been followed.

4.4. The Probity Auditor also accessed the ACTEW/AGL status report and advised that report sets out a complete and accurate summary of the transaction to date.

4.5. With regard to ensuring provision of proper independent professional as well as fair and equitable advice to ACTEW and the shareholders, the Probity Auditor gave a succinct statement of the issues examined. In particular, the Probity Auditor advised that:

(i) draft contracts had been examined specifically to ensure the protection of ACTEW and its shareholder interest
(ii) the clauses in relation to the equalisation payment and the formula for IPARC adjustment had been specifically examined
(iii) the clauses in relation to the public interest protection, operational liability, dissolution, capital structure and related party transactions had been examined
(iv) the due diligence report had been examined to ensure no issues had been raised which are not compatible or resolution and would lead to an exposure by ACTEW or the shareholders
(v) the six original criteria proposed at the initiation of the process have been examined to ensure the objectives have been met
(vi) the terms of reference for the independent valuer had been examined
(vii) preparation of a document comparing the implementation agreement with the final position agreed in negotiations had been initiated
(viii) the preparation of a document cross referencing any resolution of the Assembly to the final agreements to ensure compliance had been requested
(ix) a detailed Board paper to provide a basis for any Board resolution on the completed arrangements had been recommended.

4.6. The Probity Audit report concluded that:

- while final contracts are not complete the Auditor was unaware of any side or undisclosed agreements
- the Auditor was satisfied as to the probity of the selection process for engaging all advisers
- there are no outstanding conflict of interest issues at the date of reporting
- there is a clear audit trail
- there are no outstanding probity issues at the date of reporting.

Assembly access to the joint venture status report and the Probity Audit report

4.7. The committee understands that the status report will also be presented to the Government. While the committee has access to the report, the committee is firmly of the view that publication of the status report is the responsibility of the Government and the committee strongly urges the Government to present the report to the Assembly as a matter of priority, preferably during the current sittings of the Assembly.

4.8. The committee has a similar view about the Probity Audit report. While the interim Probity report is directed to the committee, the Auditor’s prime responsibility is to the Assembly and the committee considers it the responsibility of the Government to facilitate that process.

5. SPECIFIC ISSUES

5.1 As indicated above the committee has focused at a strategic level on how well the negotiations have secured the promised benefits of the proposed merger and how effectively they have dealt with collateral risks arising from the transaction.

Key Benefits

Energy Trading Risk Reduction

5.2 The wholesale acquisition of electricity and gas is a complex function that carries with it a number of significant risks including volume risk and price risk. Due to competitive pressures these risks are often difficult to pass through directly to customers and can thus translate into substantial financial risks for energy retailers.

5.3 The proposed partnership arrangements appear to shift volume and price risk for both electricity and gas onto AGL which is a major energy trader. The key partnership objective of reduced risk for ACTEW in this area thus appears to have been achieved and the probity auditor considers the contractual arrangements with AGL to be equitable to the ACT.

5.4 Because of the close relationship with AGL and the need to secure its approval to write new retail business under these arrangements, the partnership is likely to remain a niche competitor outside the ACT. But the committee considers that this may be no bad thing.

Employee and Shareholder Benefits

5.5 The proposed arrangements appear set to secure the employment security promised for ACTEW employees. ACTEW has informed the committee that it will continue to consult closely with its employees in finalising its staff services agreement with the partnership.

5.6 ACTEW has also reiterated its expectation that the partnership will allow the delivery of synergies that are greater than those being achieved by ACTEW or AGL alone. To this end the retail and distribution partnership agreements both require the preparation of annual four year business plans which among other things “contain a description of the synergies between the partnership gas and electricity businesses, which the Central Management Committee will seek to achieve for the partnership during the period to which the business plan relates”.

5.7 Given that the initial business plans are to be attached as schedules to the partnership agreements, the committee would expect that more specific information on expected synergies would be provided prior to establishment of the partnerships.

Public Interest Protection

5.8 ACTEW has reiterated that it and its wholly owned subsidiaries will continue to be subject to the full range of controls applicable under the TOC Act (including for approval of borrowings, preparation of statements of corporate intent and appointment of directors) and all other relevant legislation (including FOI, ADJR, Ombudsman, Annual Report, Audit). Customer and community interests are to be protected by the regulation of partnership activities under the proposed Utilities Act.

5.9 In preparing its final report the committee will seek to explore the mechanics of these arrangements by examining the revised memorandum and articles and constitutions for ACTEW and its partnership subsidiaries and the partnership licences which will secure public interest protection.

Collateral Risks

Joint and Several Liability

5.10 ACTEW has advised that the partnership form for the joint venture has been chosen for a variety of tax, commercial and regulatory reasons. From ACTEW’s and the ACT’s perspective, this structure preserves tax payments to the ACT under the tax equivalents regime.

5.11 However, in general, partners are jointly and severally liable for all liabilities incurred in respect of the partnership business. There is thus a risk of a partner becoming liable to a third party on account of a liability incurred by the other partner without authority or consent.

5.12 ACTEW has advised that the proposed arrangements address this risk by:

- each partner indemnifying the other against these liabilities; and

- guarantee of those liabilities by each partner’s parent (ACTEW and AGL).

5.13 Under this arrangement, each ACTEW partner (and indirectly, ACTEW) thus bears a credit risk in relation to the AGL partner and AGL parent company. The incurring of a material liability or failure to pay under the partner indemnity or the parent company guarantee would be a basis for dissolving the joint venture. ACTEW considers the credit risk on AGL to be low (reporting AGL’s credit rating at A+) and the commercial risk of an unauthorised liability incurred by AGL also to be low.

5.14 The probity auditor has assessed these proposed arrangements as being equitable to the ACT.

Related Party Transactions

5.15 The proposed arrangements entail the partnership entering into sole source contractual arrangements with AGL for energy trading (electricity and gas) and gas retail and network services. While aimed at helping to secure the energy trading risk reduction and business synergies promised for the partnership, these arrangements could expose ACTEW to the risk of unfair transfer pricing by AGL unless action is taken to mitigate this risk.

5.16 ACTEW has advised of a variety of provisions in the proposed arrangements to mitigate this risk including:

- “most favoured customer” requirements;
- provision for independent audit of AGL prices;
- provision for accessing alternative sources of supply if AGL does not deliver; and
- responsibility on decisions on the enforcement of a remedy or exercise of a right under partnership contracts with AGL being ceded to ACTEW management committee members acting alone (and a corresponding right for AGL management committee members for partnership contracts with ACTEW).

5.17 The probity auditor has assessed these arrangements as being equitable to the ACT.

Constraints on Dissolution of the Partnership

5.18 While it is in both parties’ interests to ensure that the partnership arrangements provide a secure and sustainable basis for future business operations and investment, it is important that the arrangements retain sufficient flexibility to cater for unforeseen developments in a volatile and rapidly changing industry.

5.19 In preparing its final report the committee will seek to explore further with ACTEW and the ACT Government whether the proposed arrangements for partnership dissolution strike an appropriate balance of stability and flexibility for the ACT.

Valuation Adjustments for Post Partnership IPARC Decisions

5.20 ACTEW has advised that the valuation of asset contributions by each of the parties will be critically affected by IPARC price path decisions. While ACTEW has an IPARC price determination in place for its electricity network assets, a corresponding determination for AGL gas assets may not be available until after the target completion date for the joint venture.

5.21 Accordingly, the parties have agreed in principle to an arithmetic adjustment to the equalisation payment once the IPARC Final Determination has been made. This adjustment is to be based on the difference between the initial capital base proposed by AGL for its assets and that included in the IPARC Final Determination.

5.22 ACTEW further advises that the parties considered an adjustment formula based on a combination of changes to other variables in the final IPARC Determination (for example rate of return) but agreed to the initial capital base adjustment mechanism primarily on the basis of its simplicity and workability. ACTEW considers the risk of a change in other variables having a material value impact to be low. A similar approach is proposed to any reopening of IPARC gas or electricity price path decisions within 24 months of partnership establishment.

5.23 The probity auditor was closely involved in the development of this approach and considers it equitable to the ACT. The committee expects that the independent valuation review will also address this issue.

Capital Structure

5.24 At establishment the partnership would be fully equity funded compared with regulatory price path benchmarks suggesting debt levels of between 50-60 percent. Decisions on the future capital structure would be for the partnership management committee to consider in consultation with ACTEW, AGL and the ACT Government.

5.25 ACTEW advises that were the partnership to be geared at 50 percent debt/50 percent equity a capital repayment of around $200 million (in addition to the $100-$140 million equalisation payment) would be payable to ACTEW. In preparing its final report the committee intends to seek an indication from ACTEW and the ACT Government on how such a capital repayment would be applied.

Ted Quinlan MLA
Chair
26 June 2000