

## Chapter 2

### The lease of Ausgrid and *Rebuilding NSW*

#### The Ausgrid lease

2.1 As part of a wider set of fiscal measures laid out in June 2014, the Premier of NSW, the Hon. Mike Baird MP, announced that the NSW Government would seek to lease 49 per cent of the state's electricity network for a period of 99 years.<sup>1</sup> The NSW Government also announced that leasing the three largest providers in the state-owned electricity distribution network – Transgrid, Ausgrid and Endeavour Energy – would allow it to fund 'once-in-a-generation' investments in significant areas of state infrastructure.<sup>2</sup>

2.2 According to the NSW Government, leasing 49 per cent of the state's electricity distributions network will provide the capital funding necessary to implement the investment plans outlined in *Rebuilding NSW*, one of the Government's major strategic policy documents.<sup>3</sup> In particular, the strategy outlined in *Rebuilding NSW* calls for a total government investment in the NSW economy of approximately \$20 billion, including a significant proportion on a range of state infrastructure projects, such as \$4.1 billion on improving regional transport and \$1 billion for enhancements to water security, among other major investment measures.<sup>4</sup>

2.3 In June 2014, the NSW Government announced that the overall cost of its infrastructure strategy would be met through a differentiated approach to leasing 49 per cent of the state's electricity network. The entirety of Transgrid would be offered for a lease period of 99 years, while only 50.4 per cent of Ausgrid and Endeavour Energy would be offered to potential investors.<sup>5</sup> Essential Energy, which provides services to many parts of rural NSW, is not included in the NSW Government's leasing plans and will remain wholly state-owned.<sup>6</sup>

2.4 After securing the passage of the *Electricity Network Assets (Authorised Transactions) Act 2015*, the legislation that enabled the lease process, the NSW

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1 The NSW Treasury, *Electricity Network Transactions*, [http://www.treasury.nsw.gov.au/electricity\\_network\\_transactions](http://www.treasury.nsw.gov.au/electricity_network_transactions) (accessed 15 April 2016).

2 The NSW Treasury, *Electricity Network Transactions*.

3 The NSW Government, *Rebuilding NSW*, <https://www.nsw.gov.au/rebuilding> (accessed 15 April 2016).

4 The NSW Government, *Rebuilding NSW*.

5 The NSW Treasury, *Electricity Network Transactions*, [http://www.treasury.nsw.gov.au/electricity\\_network\\_transactions](http://www.treasury.nsw.gov.au/electricity_network_transactions) (accessed 15 April 2016).

6 The NSW Treasury, *Electricity Network Transactions* .

Government formally launched the process of soliciting bids for the 99-year lease of Transgrid.<sup>7</sup>

2.5 On 25 November 2015, the NSW Government announced that a newly-formed consortium, NSW Electricity Networks, had been successful in its bid for Transgrid. The consortium is reported to have paid the NSW Government \$10.285 billion for the right to lease and operate Transgrid for a period of 99 years.<sup>8</sup> While NSW Electricity Networks is majority owned by foreign interests, including state-owned investment vehicles from Kuwait and Abu Dhabi, the consortium also includes two major Australian companies, Spark Infrastructure and Hastings, which together have a 35.03 per cent stake in the 99 year lease of Transgrid.<sup>9</sup>

2.6 According to the NSW Government, the gross proceeds from the lease transaction will be used to fund parts of the infrastructure strategy outlined in *Rebuilding NSW*.<sup>10</sup> The NSW Government also announced that, as a direct consequence of the lease, it would be eligible for a payment of \$1 billion from the Commonwealth Government, on the basis of provisions contained in the National Partnership Agreement on Asset Recycling.<sup>11</sup>

2.7 On 24 November 2015, the day before the announcement that NSW Electricity Networks had won the right to lease Transgrid for 99 years, the NSW Government opened the Expression of Interest (EOI) process for the lease of 50.4 per cent of Ausgrid on the basis of a Trade Sale.<sup>12</sup>

2.8 One of the largest electricity providers in Australia, Ausgrid's network encompasses almost 50,000 kilometres of above and below ground cables, servicing a total of approximately 1.7 million customers in Sydney, the Hunter Valley and the Central Coast.<sup>13</sup> According to media reports, Ausgrid's regulated asset base was approximately \$15.5 billion as of June 2015, which could make a 50.4 per cent lease

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7 *Electricity Network Assets (Authorised Transactions) Act 2015*, [http://www.austlii.edu.au/au/legis/nsw/consol\\_act/enata2015566/](http://www.austlii.edu.au/au/legis/nsw/consol_act/enata2015566/) (accessed 15 April 2016).

8 The Hon. Mike Baird MP, Premier of NSW, and the Hon. Gladys Berejiklian MP, Treasurer of NSW, 'NSW Achieves Outstanding Result in \$10.258 billion Transgrid lease', *Media Release*, 25 November 2015, [http://www.treasury.nsw.gov.au/\\_data/assets/pdf\\_file/0013/127030/25-11-15\\_NSW\\_achieves\\_outstanding\\_result\\_in\\_TransGrid\\_lease.pdf](http://www.treasury.nsw.gov.au/_data/assets/pdf_file/0013/127030/25-11-15_NSW_achieves_outstanding_result_in_TransGrid_lease.pdf) (accessed 29 February 2016).

9 The Hon. Mike Baird MP, Premier of NSW, and the Hon. Gladys Berejiklian MP, Treasurer of NSW, 'NSW Achieves Outstanding Result in \$10.258 billion Transgrid lease', *Media Release*, 25 November 2015, [http://www.treasury.nsw.gov.au/data/assets/pdf\\_file/0013/127030/25-11-15\\_NSW\\_achieves\\_outstanding\\_result\\_in\\_TransGrid\\_lease.pdf](http://www.treasury.nsw.gov.au/data/assets/pdf_file/0013/127030/25-11-15_NSW_achieves_outstanding_result_in_TransGrid_lease.pdf) (accessed 29 February 2016).

10 The NSW Treasury, *Electricity Network Transactions*, [http://www.treasury.nsw.gov.au/electricity\\_network\\_transactions](http://www.treasury.nsw.gov.au/electricity_network_transactions) (accessed 15 April 2016).

11 The NSW Treasury, *Electricity Network Transactions*.

12 The NSW Treasury, *Electricity Network Transactions*.

13 The NSW Treasury, *About Ausgrid*, [http://www.treasury.nsw.gov.au/electricity\\_network\\_transactions/about\\_ausgrid](http://www.treasury.nsw.gov.au/electricity_network_transactions/about_ausgrid) (accessed 15 April 2016).

of the company worth approximately \$9.4 billion to \$10.4 billion, including the company's debt liability.<sup>14</sup>

2.9 At the time of writing, the NSW Government has not announced the outcome of the Ausgrid lease, nor has it provided any public updates on the current status of the process. According to information made available by the government, the EOI process for the lease of 50.4 per cent of Endeavour Energy, the final stage of the NSW Government's leasing arrangements, will begin in the course of 2016.<sup>15</sup>

### **The Ausgrid lease and *Rebuilding NSW***

2.10 In the lead up to the March 2015 state election, the NSW Government committed itself to a large-scale investment plan, aimed at upgrading major parts of the state's infrastructure and providing an investment-driven boost to the NSW economy.<sup>16</sup> According to a report by Deloitte Access Economics, published in November 2014, the NSW Government's plans are likely to see an overall injection into the state's economy of \$300 billion over approximately 20 years. Job creation is forecast to be approximately 100,000 new jobs by 2035–36.<sup>17</sup>

2.11 According to the NSW Government, its plan to invest \$20 billion in major state infrastructure is dependent on releasing the capital that is 'locked up' in major state assets, including the state-owned companies, such as Ausgrid, that operate large parts of the state's electricity distribution network.<sup>18</sup> Additionally, the NSW Government's investment plans, as outlined in *Rebuilding NSW*, are required to remain in conformity with the state's *Fiscal Responsibility Act 2012*.<sup>19</sup> This requires that the Government acts to protect the state's AAA credit rating. Significant debt financing is thereby largely ruled out.<sup>20</sup>

2.12 In addition to the projected release of approximately \$20 billion in capital currently embedded in the state's electricity distribution network, the NSW Government has announced that, once the full lease process has been completed, it

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14 Angela MacDonald-Smith, 'Ausgrid lines up as 'plan b' for losing Transgrid bidders', *Sydney Morning Herald*, 23 November 2015, <http://www.smh.com.au/business/energy/ausgrid-lines-up-as-plan-b-for-losing-transgrid-bidders-20151122-gl5881.html> (accessed 15 April 2016).

15 The NSW Treasury, *Electricity Network Transactions*, [http://www.treasury.nsw.gov.au/electricity\\_network\\_transactions](http://www.treasury.nsw.gov.au/electricity_network_transactions) (accessed 15 April 2016).

16 The NSW Government, *Rebuilding NSW*, <https://www.nsw.gov.au/rebuilding> (accessed 15 April 2016).

17 Deloitte Access Economics, *Economic Impact of State Infrastructure Strategy – Rebuilding NSW*, <https://www.nsw.gov.au/sites/default/files/miscellaneous/economic-impact-of-state-infrastructure-strategy.pdf> (accessed 15 April 2016), p.5 and p.11.

18 The NSW Government, *Rebuilding NSW*, <https://www.nsw.gov.au/rebuilding> (accessed 15 April 2016).

19 *Fiscal Responsibility Act 2012*, [http://www.austlii.edu.au/au/legis/nsw/consol\\_act/fra2012243/](http://www.austlii.edu.au/au/legis/nsw/consol_act/fra2012243/) (accessed 15 April 2016).

20 The NSW Government, *Rebuilding NSW*, <https://www.nsw.gov.au/rebuilding> (accessed 15 April 2016).

will be eligible for a \$2 billion contribution from the Commonwealth Government, pursuant to the National Partnership Agreement on Asset Recycling.<sup>21</sup> The capital generated by the full lease process, including Commonwealth Government contributions, will fund a number of major state infrastructure investments, including:

- An additional \$1.1 billion to invest in the northern and southern extensions to WestConnex, along with the Western Harbour Tunnel.
- An extra \$7 billion for Sydney Metro, to fully fund a second harbour rail crossing.
- \$2 billion in additional education and health funding.
- \$4.1 billion for regional transport.
- \$1 billion for regional water security.
- \$300 million for regional tourism and the environment.
- More funds to Sports and Cultural infrastructure, up from \$500 million to \$1.2 billion.<sup>22</sup>

2.13 According to the NSW Government, leasing 49 per cent of the state's electricity distribution infrastructure will have a dual benefit. Firstly, leasing 49 per cent of the state's electricity distribution network will produce the primary benefit of freeing up scarce state resources for infrastructure investments that would otherwise be beyond the Government's fiscal capacity. Secondly, as a consequence of private sector involvement, there is likely to be an increase the efficiency of, and the rate of capital investment in, the leased entities.<sup>23</sup>

### **The Ausgrid Lease and the Australian Energy Regulator**

2.14 Recent media reports have suggested that the NSW Government's plan to lease 50.4 per cent of both Ausgrid might be affected, to the detriment of the final lease price, by a recent decision of the Australian Energy Regulator (AER). The AER's determination covers the regulatory period from 1 July 2014 to 30 June 2019, and could therefore affect the overall attractiveness of Ausgrid to potential private sector investors.<sup>24</sup>

2.15 After reviewing the distribution charges that electricity networks are entitled to charge consumers, AER ruled that the three state-owned electricity distributors – Ausgrid, Endeavour Energy and Essential Energy – must reduce the charges that they

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21 The NSW Government, *Rebuilding NSW*.

22 The NSW Government, *Rebuilding NSW*.

23 The NSW Government, *Rebuilding NSW*.

24 Australian Energy Regulator, *Ausgrid - Determination 2014-19*, <https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/ausgrid-determination-2014-19> (accessed 15 April 2016).

levy on consumers.<sup>25</sup> According to the Australian Financial Review, AER's decision could have the effect of reducing the operating revenue of Networks NSW – the state-owned company that currently owns Ausgrid, Endeavour Energy and Essential Energy – by up to \$566 million.<sup>26</sup>

2.16 According to Networks NSW, the AER's determination in relation to distribution charges is likely to have a damaging effect on the lease process, since a potential investor could be forced to commit new and significant funds to a company that could, well into the foreseeable future, generate low or even negative equity returns.<sup>27</sup> While the investment strategies of private sector companies and consortiums are difficult to predict, Networks NSW maintained that a continued high level of regulatory uncertainty, especially over the longer term, will have the effect of lowering the value of Ausgrid for potential investors, both domestic and foreign.<sup>28</sup>

2.17 In February 2016, however, the Australian Competition Tribunal (ACT) ruled that AER committed a number of errors in arriving at its determination. On the basis of that ruling, the tribunal set aside AER's revised network charges.<sup>29</sup> As a consequence of the ACT's decision – which has led AER, in turn, to seek a judicial review in the Federal Court – the overall regulatory environment in respect of network distribution charges remains comparatively unclear.

2.18 It remains possible that this degree of regulatory uncertainty, which might not be resolved in the near term, could negatively affect the price that potential bidders are willing to offer for Ausgrid. In turn, this could have an equally negative effect on the \$20 billion that the NSW Government, as outlined in its *Rebuilding NSW* policy, expects to raise from leasing 49 per cent of the state's electricity distribution network.

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25 Sarah Gerathy, 'Energy companies thrown lifeline in battle against NSW regulator', *ABC News*, 26 February 2016, <http://www.abc.net.au/news/2016-02-26/energy-companies-thrown-lifeline-in-battle-with-nsw-regulator/7202724> (accessed 15 April 2016).

26 Geoff Winestock, 'NSW power sale: prices to rise after court win', *Australian Financial Review*, 26 February 2016, <http://www.afr.com/news/politics/nsw-power-sale-prices-to-rise-after-court-win-20160225-gn45h6> (Accessed 15 April 2016).

27 Geoff Winestock, 'NSW power sale 'not viable' if AER decision stands', *Australian Financial Review*, 21 September 2015.

28 Geoff Winestock, 'NSW power sale 'not viable' if AER decision stands', *Australian Financial Review*, 21 September 2015.

29 Sarah Gerathy, 'Energy companies thrown lifeline in battle against NSW regulator', *ABC News*, 26 February 2016, <http://www.abc.net.au/news/2016-02-26/energy-companies-thrown-lifeline-in-battle-with-nsw-regulator/7202724> (accessed 15 April 2016).

