

Chapter 1

Introduction

1.1 On 2 October 2014, the Senate referred an inquiry into the performance and management of electricity network companies to the Environment and Communications References Committee. The terms of reference for the inquiry are as follows:

- (a) the manner in which electricity network companies have presented information to the Australian Energy Regulator (AER), and whether they have misled the AER in relation to:
 - (i) their weighted average costs of capital,
 - (ii) the necessity for the infrastructure proposed,
 - (iii) their regulated asset valuations, and
 - (iv) actual interests rates claimed against actual borrowing costs;
- (b) how electricity companies, including state government owned electricity companies such as Energex, have calculated the weighted average cost of capital and how this measure has changed over time;
- (c) where anomalies are identified in relation to price structuring or allegations of price rorting by electricity companies, such as Energex, are raised, the possibility of these matters being investigated by a national independent body created by the Federal Government with the required powers and reach to investigate and prosecute, where necessary;
- (d) to ascertain whether state-owned network companies have prioritised their focus on future privatisation proceeds above the interests of energy users;
- (e) whether the arrangements for the regulation of the cost of capital are delivering allowed rates of return above the actual cost of capital;
- (f) whether the AER has actively pursued lowest-cost outcomes for energy consumers;
- (g) whether network monopolies should have the right to recover historic overspending that has delivered unwanted and unused infrastructure;
- (h) how the regulatory structure and system could be improved;
- (i) whether the arrangements for the connection and pricing of network services is discriminating against households and businesses that are involved in their own electricity production;
- (j) whether the current system provides adequate oversight of electricity network companies; and

(k) any other related matter.¹

1.2 The committee was initially required to report by the first sitting day in March 2015 (2 March 2015). However, on 2 March 2015, the Senate granted an extension of time to report until 20 April 2015.² On 20 April 2015, the committee requested a further extension to 5 May 2015 to report. The committee subsequently requested a further extension to 5 June 2015.

Conduct of the inquiry

1.3 The committee advertised the inquiry on its website and in *The Australian* newspaper. The committee also wrote to relevant organisations and individuals inviting written submissions.

1.4 The committee received 73 submissions, which are listed at Appendix 1. Included in the submissions are 552 letters co-ordinated by a community organisation that the committee agreed to receive as a submission.³ The non-confidential submissions were published on the committee's website.

1.5 The committee held public hearings for this inquiry in Brisbane on 16 February 2015, Sydney on 17 February 2015, Melbourne on 18 February 2015, Adelaide on 19 February 2015 and Canberra on 24 March 2015. A list of witnesses who appeared at the hearings may be found at Appendix 2.

1.6 The committee thanks all of the organisations, individuals and government departments and agencies that contributed to the inquiry.

First interim report

1.7 On 20 April 2015, the committee presented an interim report that addressed many of the key issues canvassed during the inquiry.⁴ Among other matters, the first interim report:

- outlined various developments that help place this inquiry in context;
- provided an overview of the regulatory framework for electricity networks;
- considered in detail the revenue determination process and the components that determine the maximum allowable revenue for a network business, such as the regulatory asset base (RAB), weighted average cost of capital (WACC) and operating expenditure;

1 *Journals of the Senate*, 2013–15, no. 59 (2 October 2014), pp. 1586–87.

2 *Journals of the Senate*, 2013–15, no. 79 (2 March 2015), p. 2203.

3 These letters were published as *Submission 65* and as a supplementary submission (*Submission 65.1*).

4 The interim report may be viewed online at www.aph.gov.au/Parliamentary_Business/Committees/Senate/Environment_and_Communications/Electricity_and_AER/Interim_Report.

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- discussed particular issues that may arise when regulating government-owned network businesses;
 - considered information asymmetries that exist in the regulation process and whether there are incentives for network businesses to 'game' the regulator;
 - examined concerns about the process by which the rules that apply to electricity network businesses are made, as well as concerns regarding the framework of rule-making and regulatory institutions more generally; and
 - discussed the future of electricity networks and the implications for consumers, policymakers and regulators.

1.8 The committee made 18 recommendations in its first interim report. These recommendations are reproduced at Appendix 3.

Second interim report and final report

1.9 As explained in the first interim report, by mid-April 2015 the committee had finalised its deliberations on many of the key issues canvassed during this inquiry. However, the committee required additional time to consider particular instances where the conduct of network service providers was questioned. The committee presented a second interim report on 5 May 2015 that requested a further extension of time to consider these matters.

1.10 The evidence that the committee had not concluded examining by the time the first interim report was finalised include:

- allegations made by a whistleblower that a Queensland government-owned distribution network business, Energex, manipulated data about its costs; and
- allegations put forward by other stakeholders who consider the regulator is being misled about the necessity of particular infrastructure proposals.

1.11 Also not addressed in the first interim report were matters that appear to be intrinsically linked to the allegations outlined above. These matters include:

- the AER's powers to obtain from network businesses the information necessary for the AER to perform its regulatory functions;
- the penalties for providing the AER with false or misleading information; and
- clause (c) of the terms of reference, which outlines a proposal for a new agency to be charged with investigating certain allegations related to electricity networks pricing.

1.12 These outstanding matters are considered in the following chapter of this report. Readers should refer to the first interim report for background information and explanations of key concepts related to the regulation of electricity networks.

