Australian Government

**CLEAN ENERGY FINANCE CORPORATION**

5 March 2014

Senator David Bushby
Chair
Senate Economics Legislation Committee
Parliament House
CANBERRA ACT 2600

Dear Senator

In reviewing the transcript of last week's Additional Estimates hearings, I wish to clarify the record in relation to evidence provided by the Clean Energy Finance Corporation (CEFC).

At the Committee's hearing of 26 February 2014, the following exchange occurred in relation to Fiscal Balance and the public debt interest cost of the CEFC with respect to projections in the *Clean Energy Finance Corporation (Abolition) Bill 2014*:

**CHAIR:** I will use this example: page 3 of the explanatory memorandum to the CEFC (Abolition) Bill shows that abolition of the CEFC would have a positive fiscal impact of $710 million over the forward estimates. Firstly, is that something that you object to? If not, how does that work into the positive contribution to the budget that you quote?

**Ms Broadbent:** We stand by that figure, but what it does not pick up—perhaps our CEO or Treasury would like to comment on this—is the cost of debt in that particular figure, because the line items in the Treasury figures only pick up the CEFC and they pick up the borrowing cost in another line item, but it is in our communication about the impact of the entity as a whole that we pick up both.

**Mr Yates:** Maybe we could revert to the CFO. I can understand where the question would be coming from and would be delighted to answer.

**Mr Powell:** The numbers that were quoted on page 3 of the explanatory memorandum were calculated as the delta between the MYEFO estimates and the PEFO estimates for the corporation. Neither of those numbers includes the cost of borrowing, so that number is before any public debt interest cost.

**CHAIR:** What impact would it have on that figure if the public interest cost were also included?

**Ms Broadbent:** The current cost of borrowings is between three and 3½ per cent.

**CHAIR:** Which is what in dollar terms for what has been borrowed so far?

**Ms Broadbent:** Depending on how much we have drawn from—

**CHAIR:** Yes, but in terms of how much you have drawn down now.

**Ms Broadbent:** In terms of what we have drawn down now, Andrew, what do those projections assume our balance sheet—

**Mr Powell:** That assumed that by that point in time we would have drawn close to $6 billion on a gross basis, but we would have been repaying that as well. So it is not that we would have had $6 billion outstanding; we would have had about $3 billion outstanding.

**CHAIR:** That is always a dynamic thing. We were talking today with AOFM about actual dollars. It is always hard, because that is turning over all the time as well.

**Ms Broadbent:** So probably about $150 million in additional cost.

**CHAIR:** On average about $150 million a year?

**Ms Broadbent:** Something like that.

**CHAIR:** So that is the cost to government of providing the CEFC with the capital—

**Ms Broadbent:** The $5 billion, yes.

**CHAIR:** that you then use for the purposes that you are—

**Ms Broadbent:** Yes, on which we earn a return above that.

**CHAIR:** On those figures, is it projected that you would be making a positive contribution to the budget?

**Ms Broadbent:** It is.

**CHAIR:** Taking into account the public debt interest?

**Ms Broadbent:** Yes.

In the interests of clarifying the evidence above, I wish to advise on the following issues:

1. *Concessionality included in the Fiscal Balance impact over the forward estimates*

   - The "positive fiscal impact of $710 million over the forward estimates" you referred to in your question was a $706 million estimate by the Departments of Finance and Treasury of the Fiscal Balance impact over the forward estimates of abolishing the CEFC.
   - This $706 million figure included a $ 917 million non-cash charge as it assumes the CEFC largely uses the $300m per annum concessionality available to it under the Investment Mandate in each year of the forward estimates. The CEFC has only incurred some $11 million of concessionality charge since its inception, so the actual Fiscal Balance impact is already materially different to that shown in the forward estimates.
   - Concessionality is a non-cash charge that has a net zero impact over the term of the investment. It has a negative impact in the initial years of an investment which is offset by a positive impact over the subsequent years. By looking out only to 2017, the Fiscal Balance numbers are misleading as to the true cost to the Commonwealth of abolishing the CEFC, since it includes the concessionality charge in full but not the unwind of this concessionality which happens in later years. The Fiscal Balance impact

(from the Explanatory Memorandum) excluding the non-cash concessionality charge and associated unwind are shown below:

| | *2013-14* | *2014-15* | *2015-16* | *2016-17* | *Total 2013-14 to 2016-17* |
|---|---|---|---|---|---|
| Impact on Fiscal Balance | $177.4m | $276.9m | $191.4m | $60.3m | $706.1m |
| Add back net Concessionality (non-cash) charge | ($167.3m) | ($285.0m) | ($256.2m) | ($208.5m) | ($917.0m) |
| Impact on Fiscal Balance excluding non-cash net charge for concessionality | $10.1m | ( $8.1m) | ($64.8m) | ($148.2m) | ($210.9m) |

2. *The CEFC is outperforming Treasury estimates used for Fiscal Balance impact*

- The CEFC is currently outperforming the estimates that were used to calculate the cost of abolishing the CEFC, which means the negative impact on both the Fiscal Balance and the Underlying Cash Balance from abolishing the CEFC are likely to be significantly higher than shown in the Explanatory Memorandum:
    - the interest rates and fees being received by the CEFC from its investments are higher than assumed in PEFO; and
    - the CEFC is significantly underutilising the available $300 million pa of concessionality. The CEFC has only incurred some $11 million of concessionality charge since its inception.

3. *Items not included in the estimate of Fiscal Balance impact over the forward estimate period*

- The Explanatory Memorandum to the *Clean Energy Finance Corporation (Abolition) Bill 2014* states that the estimates used do not make any allowance for the costs of shutting down the CEFC, such as employee redundancies and contract termination costs, nor do they make any allowance for the lower public debt interest costs of ceasing further CEFC investment.
- They also do not include the cost of Treasury administering (or alternatively contracting out the administration of) the CEFC's investment Portfolio following abolition of the CEFC.

4. *Estimated public debt interest cost impact of abolition of the CEFC is not included in the Fiscal Balance impact over the forward estimates*

- In answer to your question as to "What impact would it have on that figure if the public interest cost were also included?", the Australian Office of Financial Management (AOFM) is responsible for the management of Australian Government debt and the finance costs associated with funding the CEFC. The CEFC does not have clear visibility into these specific finance costs. For its own investment purposes, the CEFC uses a Portfolio Benchmark Return, as specified in the Investment Mandate from the Australian Government under *Section 64* of the *CEFC Act*. This Portfolio Benchmark is based on a weighted average of the five-year Australian Government bond rate.
- My response citing $150 million in additional cost, referred to the estimated annual borrowing cost associated with the CEFC once it has reached an average investment portfolio balance of around $5 billion.
- To best respond to your question of what public debt interest cost (PDIC) would be avoided over the forward estimates period if the CEFC were abolished; assuming a gradual deployment of funds and using the five-year Australian Government bond rate as a proxy for this cost (in accordance with our Investment Mandate), then the estimated total PDIC avoided over the four year forward estimates period would be approximately $195 million.

I again thank you and the Committee for the sustained interest in the progress of the CEFC. Should you require any further information, please do not hesitate to contact Mr Simon Every, Director – Corporate Affairs, Government and Stakeholder Relations on

Yours sincerely

Jillian Broadbent AO
Chair