



Submission to the Review of Institutional Arrangements for ACTEW Corporation Limited

September 2013



ACTEW Corporation Limited (ACTEW) is an unlisted public company that owns and operates the water and sewerage assets and business in the ACT. The company is owned by the ACT Government and has two voting shareholders: the Chief Minister and Deputy Chief Minister of the ACT.

ACTEW has two subsidiary companies: ACTEW Retail Limited and ACTEW Distribution Limited. Investments include 50 per cent ownership of ActewAGL.

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Executive Summary

ACTEW Corporation is one of the largest and most high profile corporations in the ACT.

It is an organisation which has for more than 40 years ensured the safe, secure and reliable provision of water, sewerage and energy services to the people of the ACT, but which has also changed over time to meet government, community and industry expectations.

ACTEW is a territory owned corporation of the ACT Government, incorporated under the *Corporations Act 2001 (Cth)* (**Corporations Act**), with responsibilities to its shareholders, customers, the environment and the ACT community. ACTEW takes these responsibilities very seriously, given the key role that it plays in the provision of services and infrastructure for the ACT.

ACTEW has two primary activities: providing water and sewerage services for the community, and as a principal partner in the ActewAGL joint venture. Its total assets are valued at \$2.8 billion which includes water and sewerage assets valued at \$2 billion.

It is now over a decade since the commencement of the ActewAGL Joint Venture, and given the evolving nature of the services provided by ACTEW and the environment in which it operates, it is timely and important that ACTEW's functions, role and structure be reviewed.

ACTEW welcomes the opportunity to provide a submission to this Review, which considers:

- ACTEW's history - how ACTEW became the corporate entity that it is today;
- ACTEW's business – the business of ACTEW today, its corporate direction, its organisational structure and underlying vision, mission, values and strategic imperatives, its interaction with the community and some of the key issues that ACTEW faces in the future;

- ACTEW's relationship with ActewAGL - outlining the structure of the ActewAGL investment and ACTEW's current approach to the management of that investment;
- the successes of, and potential issues in relation to, the current ACTEW structure and relationship with ActewAGL;
- given those successes and issues, what other structural options may be available for the management of the water and sewerage business and the investment in ActewAGL;
- what are the key parts of the regulatory framework that govern ACTEW; and
- the relationship with the ACT Government - including in relation to the current dividend policy and the raising of debt.

As a result of the above considerations, ACTEW submits the following when considering the structure of, and regulatory framework for, ACTEW:

- The ACTEW and ActewAGL structures have been very successful. Since 2000 ACTEW has:
 - returned **\$1.4 billion** to the ACT Government (plus a further \$100 million paid in 1998), in the form of:
 - \$812 million in dividends;
 - \$174 million in taxes;
 - \$300 million in capital repatriations; and
 - the \$119 million equalisation payment.
 - delivered significant capital expenditure projects, supported community programs and organisations, while ensuring the delivery of safe, secure, reliable, compliant and cost effective utility services. Indeed, ACTEW is currently the second cheapest water and sewerage utility of the Australian capital cities.
- Notwithstanding this success, ACTEW agrees that it is important to regularly review its functions, role and structure.

- In this context, ACTEW believes that there are four possible approaches that could be taken in relation to its structure:
 - given the enormous success of the ACTEW and ActewAGL model since their commencement - simply maintain the status quo;
 - change the name of ACTEW to separate its business from the business and brand of ActewAGL (so that stakeholders and the community better understand the role of ACTEW as opposed to ActewAGL), while enhancing and further formalising the governance and review process for ACTEW's investment in ActewAGL - this is the preferred option of the ACTEW Board;
 - change the name of ACTEW and undertake a complete structural separation of ACTEW from ActewAGL - that is, ACTEW would transfer its interest in ActewAGL to a new territory-owned corporation and leave the ActewAGL joint venture. ACTEW would focus on the water business only, with the new corporation holding and managing the ActewAGL investment; and
 - change the name of ACTEW, and restructure its holding of ActewAGL so that there was a new subsidiary of ACTEW, whose sole function was to manage the ActewAGL investment.
- ACTEW is subject to an extensive governance, compliance and reporting regime - a regime that may not always be consistent with the corporate nature of ACTEW. ACTEW has a preference towards the following regulatory framework:
 - the Independent Competition and Regulatory Commission (**ICRC**) should be the primary economic regulator;
 - the primary regulatory operational document should be the Utilities Act;
 - the primary governance document should be the Corporations Act, with the *Territory-owned Corporations Act 1990 (TOC Act)* supplementing the obligations under the Corporations Act (consistent with the views of the ICRC); and
 - rather than introducing any further rights for the ACT Government to oversee the actions of ACTEW (a position not consistent with the concept of ACTEW acting as a corporate entity), the ACTEW



Constitution should be utilised by Voting Shareholders as a governance, accountability and information gathering document - consistent with the intent of the document and the Corporations Act.

Or, put simply, ACTEW would prefer to see more emphasis placed on the corporate nature of ACTEW, the scope of the Corporations Act, and the rights of Voting Shareholders, as essential limbs of the accountability framework.

- The dividend policy and debt raising positions that apply to ACTEW as a result of the position of the ACT Government need to change , taking into account:
 - the KPMG report commissioned by the ACT Government;
 - ACTEW's proposals in this submission;
 - the position in other jurisdictions in Australia; and
 - the corporate nature and commercial viability of ACTEW.

1. Historical Origins of ACTEW and ActewAGL

Summary:

- *Since its origins as a Commonwealth agency, ACTEW's functions have developed over time to become the largest and most commercial ACT Government corporation.*
- *ACTEW was incorporated in 1995.*
- *To ensure competitiveness in the gas and energy markets, ACTEW formed the ActewAGL joint venture with AGL in 2000.*
- *In 2012 ACTEW took over full operational responsibility for the delivery of water and sewerage services from ActewAGL.*

Before assessing the current structure of ACTEW, or considering what future structures may be available, it is helpful to understand how ACTEW became the entity that it is today.

1.1. Progression to ACTEW

ACTEW's functions were originally performed within the Commonwealth Public Service. However, with time these functions were passed to the ACT Government through a number of processes:

- in 1962 the Australian Capital Territory Electricity Authority (**ACTEA**, a Commonwealth agency) was formed to undertake the energy functions;
- in 1988 the Australian Capital Territory Electricity and Water Authority (**ACTEWA**, originally a Commonwealth agency) was established from ACTEA and the Water and Sewerage Branch of ACT Administration;
- in 1989 ACTEWA was transferred to ACT Government control after the granting of self-government for the ACT;
- in 1990 the TOC Act was introduced, allowing for the establishment and operation of territory-owned corporations; and
- in 1995, ACTEWA was abolished and ACTEW Corporation Limited was established as a Corporations Act company, but in accordance with the



requirements of the TOC Act. The Voting Shareholders of ACTEW are the Chief Minister and the Treasurer of the ACT.

At the time, the ACT Government's primary stated reasons for corporatising ACTEW were to:

- provide incentives to improve efficiency within ACTEW by setting appropriate performance and accountability targets;
- separate the regulatory functions away from the company;
- identify and fund accordingly the Government's community service obligations;
- allow the corporate body to set itself up along company lines, in line with Corporations Law;
- place ACTEW on a comparable footing with other commercial enterprises to become competitive; and
- allow the Government and community to maximise the returns on their investment in such enterprises.

Having a corporation that owned and managed the utility services was consistent with competition policies adopted by governments across Australia, separated operations from regulation, and more appropriately, addressed risk for the ACT Government, in that the risk and liability associated with running such a utility would primarily be dealt with by a commercially-focused, corporate entity that was now ACTEW.

Under the TOC Act, ACTEW's responsibilities, on corporatisation, were:

- to operate at least as efficiently as any comparable business;
- to maximise the sustainable return to the Australian Capital Territory on its investment in ACTEW and its subsidiaries in accordance with the performance targets in the annual statement of corporate intent of ACTEW, as agreed with the shareholders;
- to show a sense of social responsibility by having regard to the interests of the community in which ACTEW operates, and by trying to accommodate or

encourage those interests; and

- where ACTEW's activities affect the environment, to operate in accordance with the object of ecologically sustainable development.

Those responsibilities remain integral to how ACTEW operates.

1.2. The Creation of the ActewAGL Partnerships

In response to increasing competition in the energy market, and to mitigate against the cost and hedge risk of the supply of gas and electricity, in October 2000 ACTEW and AGL entered into the ActewAGL Joint Venture - the first multi-utility in Australia operating as a public-private partnership.

ACTEW and AGL, as equal partners after the payment of an equalisation payment to ACTEW of \$119 million by AGL, combined ACTEW's electricity network and retail operations with AGL's ACT and Queanbeyan gas network and retail operations. While water and sewerage assets were retained by ACTEW, the operation and maintenance of these assets was undertaken under contract by ActewAGL. Historically, a range of corporate support services have also been provided to ACTEW by ActewAGL.

Partly due to competition issues affecting AGL outside of the ACT and AGL responding by restructuring its businesses, business arrangements in 2006 saw the separation of AGL's retail and distribution businesses, which ultimately resulted in Jemena becoming ACTEW's partner in the ActewAGL Distribution Partnership, while AGL Energy remained the ActewAGL Retail Partner.

1.3. Re-integration of the Water Business

In 2011 ACTEW instigated an internal review of the contractual and governance arrangements for the water and sewerage business.

The review concluded that the re-integration of the management, operation and maintenance of the water and sewerage business into ACTEW would provide the best balance of outcomes for ACTEW, ActewAGL, their customers and the community, while enabling ACTEW to operate the business in its entirety and connect the business more directly to its owners and shareholders.

As such, from 1 July 2012 ACTEW assumed direct responsibility for the management and operation of water and sewerage business (under the brand "ACTEW Water"), while continuing to source corporate and retail services from ActewAGL under a new, commercial contract, that specified targets and key performance indicators.

2. Current Business

Summary:

- **ACTEW's businesses are the provision of water, sewerage and other services to the ACT and surrounding community and the holding and management of the ActewAGL investment.**
- **ACTEW's assets include dams, water treatment plants, sewerage treatment plants, pipelines, water reservoirs and the water and sewerage network.**

ACTEW has two primary activities: providing water and sewerage services, and being a 50 per cent partner in the ActewAGL joint venture.

2.1. Water and Sewerage Services

ACTEW is the main supplier, and the licence holder under the *Utilities Act 2000 (Utilities Act)*, of water, sewerage and associated services in the ACT. It owns and operates the ACT's network of dams, water treatment plants, sewerage treatment plants, reservoirs, water and sewerage pumping stations, mains and other related infrastructure, and includes the supply of bulk treated water to the NSW City of Queanbeyan.



Figure 1. ACTEW's water business



ACTEW consistently delivers safe, high quality drinking water and reliable sewerage services to a community of over 360,000 people. Its water and sewerage infrastructure assets are valued at \$2 billion and it produces the second lowest cost water and sewerage services across Australian capital cities.

Assets include:

- water treatment plants at Mount Stromlo and Googong;
- Googong, Cotter, Bendora and Corin Dams with a combined storage capacity of approximately 280 gigalitres;
- Australia's largest inland sewage treatment plant (the Lower Molonglo Water Quality Control Centre) and the Fyshwick Sewerage Treatment Plant;
- over 6,000 kilometres of water and sewerage mains;
- the Murrumbidgee to Googong Water Transfer Pipeline;
- 47 water reservoirs;
- over 50 water and sewerage pumping stations; and
- 9.549 gigalitres of high security water entitlements and 12.523 gigalitres of general security entitlements.



Figure 2. Key water and sewerage assets in the ACT region

Water is sourced from storages on the Cotter and Queanbeyan Rivers and directly from the Murrumbidgee River and is treated to a high standard at either the Stromlo or Googong Water Treatment Plants. It is then stored in numerous local reservoirs around the ACT before being distributed to customers.

Sewage, including household waste and liquid trade waste, is carried by the sewerage network for treatment at the Lower Molonglo Water Quality Control Centre (LMWQCC). After treatment the water is either released into the Murrumbidgee River, contributing to the flows in the Murrumbidgee River and the Murray-Darling Basin, or re-used in irrigation and other non-potable uses.



Significant steps have been made in recent years to secure the ACT's water supply, with the construction of the Enlarged Cotter Dam (ECD) and the Murrumbidgee to Googong Water Transfer (M2G) Pipeline.

2.2. Investment in ActewAGL

ACTEW's other business is as a 50 per cent owner in the ActewAGL joint venture with Jemena and AGL.

The ActewAGL joint venture consists of two partnerships:

- the ActewAGL Distribution Partnership (**ActewAGL Distribution**), which owns and operates the electricity and gas distribution networks in the ACT and in certain adjacent regional centres; and
- the ActewAGL Retail Partnership (**ActewAGL Retail**), which sells electricity and gas to its retail and commercial customers in the ACT and surrounding region.

While details of ACTEW's investment in ActewAGL are set out later in this submission, it is worth noting that, in terms of cash distributions alone, this investment has provided \$592 million (from 2000-2012) to ACTEW.

3. Strategic Direction

Summary:

- ***ACTEW undertakes its business by reference to its vision, mission values, and the strategic imperatives.***
- ***ACTEW's overarching aim is to provide safe, innovative and sustainable water, energy and related services to support the economic, cultural and social development of the Capital Region.***

3.1. Business Transformation

With the re-integration of the water business, ACTEW took the opportunity to focus on improving the business and setting a new strategic direction for the organisation, with a view to becoming an industry leader as a safe and sustainable business and a major contributor to the economic, social and environmental interests of the Capital Region.

A team of ACTEW staff is involved in a three year program to help shape the organisation. The program commenced with the following five assessments:

- A diagnostic assessment of the business was undertaken, benchmarking ACTEW with other businesses and utilities and identifying priorities and opportunities for the business.
- A cultural review was conducted by holding interviews with staff and undertaking an organisation-wide survey to provide a cultural baseline.
- An organisational strategy was developed through senior manager workshops, examining the long term strategic direction for the organisation and developing a new mission, vision and set of strategic imperatives for the organisation.
- A 'quick wins' business improvement action plan was developed and implemented with projects that could provide immediate benefits, such as financial savings, process improvements and enhanced communication.
- A stakeholder engagement study was undertaken to obtain external feedback on ACTEW's performance.

In addition to the above assessments, longer term value adding projects were also initiated.

The results of the assessments identified the need to build a business that:

- is based on strategic, long term goals;
- is more commercially and customer focused;
- has a greater focus on safety, sustainability and operational efficiency;
- continues to go beyond the regulatory requirements for ACTEW;
- has a collaborative and driven culture; and
- is agile and responsive to challenges as they arise, such as climate change, population growth, new technologies, shareholder requirements, infrastructure, environmental and financial pressures.

Given this, and in compliance with the TOC Act, the ACTEW Board endorsed a new mission and vision as well as a set of strategic imperatives for the organisation.

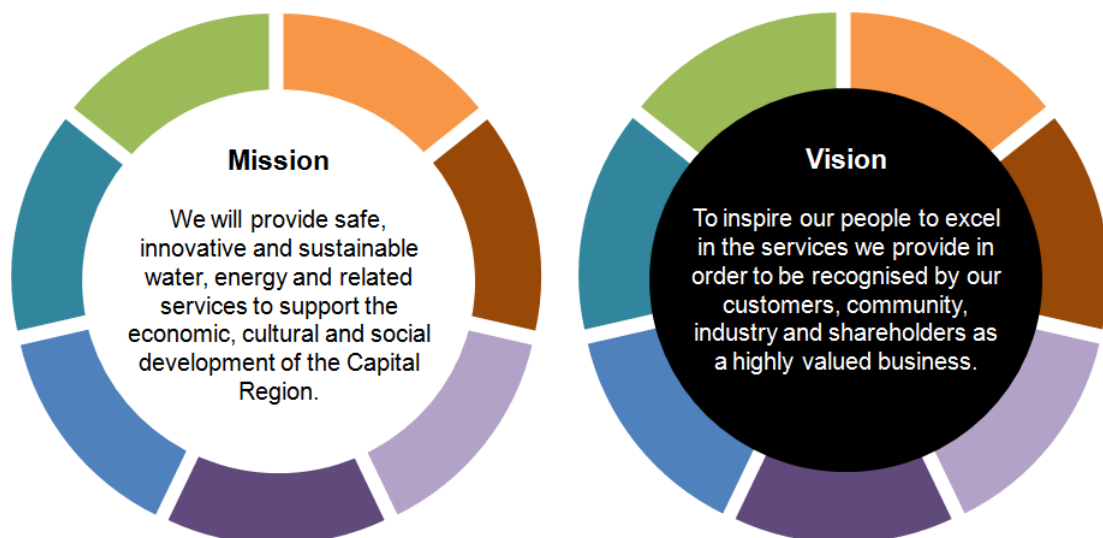


Figure 3. Mission and Vision statements

3.2. Strategic Imperatives

The strategic imperatives represent ACTEW’s overall objectives. These imperatives have been shaped to guide the business to achieve its vision, mission, values and strategic objectives.



Figure 4. ACTEW drivers

They inform the structure of ACTEW’s operating model and the nature and scope of the specific activities that ACTEW will be undertaking now and in the future.

There are seven strategic imperatives, with a clear focus on safety, sustainability, customers and operational efficiency:



Figure 5. Strategic Imperatives

ACTEW believes that these strategic imperatives provide clear and focused targets against which ACTEW can be measured and held to account by its shareholders, the community, its suppliers and its customers.

3.3. Setting Priorities

In addition to the strategic imperatives, there are several key strategic documents that have informed and continue to inform ACTEW's planning and priority setting. These include:

- **Statement of Corporate Intent 2013-2014 to 2016-17** - ACTEW's corporate plan that details the performance targets and priorities for ACTEW during the upcoming financial year. It is an annual publication and a requirement under the TOC Act. A copy can be found at:

[www.actew.com.au/News and Publications/Reports and Publications/Key Publications](http://www.actew.com.au/News%20and%20Publications/Reports%20and%20Publications/Key%20Publications)

- **Future Water Options for the ACT Region** - assessed nearly 30 options for improving Canberra's water supply and provided the background to inform the current investment into the large water security projects. The *Water Security Program 2007* report made firm recommendations to Government on the construction of the Enlarged Cotter Dam, the Murrumbidgee to Googong Pipeline and the purchase of water entitlements to be accessed from the Tantangara Reservoir.
- **Canberra Sewerage Strategy 2010-2060: Options Report** - a 50 year plan that explores various options to treat wastewater in the ACT to maximise community benefit, and the related possibilities for reuse of reclaimed water and biosolids to address future challenges.
- **Asset Management Plan 2013-2014 to 2032-2033** - sets out the asset management and asset improvement programs for the next 20 year horizon. This document is reviewed every year, with a more formal review and update every 5 years.
- **Capital Program Priority Plan 2013-2018** - the result of developing, prioritising and approving the capital program and lists the projects for the next 5 year period.
- **Strategic Asset Management Plans** - for the long term planning and management of the Mount Stromlo and Googong Water Treatment Plants,



the Lower Molonglo Water Quality Control Centre (50 year Plan), and Fyshwick Sewerage Treatment Plant (50 year Plan).

These documents, and others, assist ACTEW with planning, prioritising and managing its water and sewerage networks to ensure that customers continue to receive the reliable services they have come to expect. These documents also provide the operational framework within which ACTEW works to achieve best practice in the delivery of water and wastewater services.

3.4. Environmental Sustainability

Sustainability is a core element of ACTEW's new corporate strategy and a sustainability framework has been developed to support the business transformation process going forward. It will provide the platform to deliver a balanced approach to financial, social, environmental and cultural sustainability across the business, providing supporting systems, tools and education.

To align with ACTEW's strategic imperatives to be a customer-centric organisation and a sustainable business, ACTEW is researching what are the most important sustainability issues for ACTEW's external stakeholders, and the business. Interviews and surveys have been conducted with key external and internal stakeholders. The results of this research will influence how ACTEW reports on its sustainability performance, will help to inform strategy and action planning, and ensure ACTEW's priorities align with those of its customers and stakeholders.

3.5. Community Interaction and Engagement

In addition to its obligations under the TOC Act, ACTEW has had a longstanding corporate commitment to support the local community, and puts considerable effort into working and engaging with the community.

This includes:

- public information campaigns to inform the community about targeted programs, such as the importance of sustainable water use;
- hosting information and educational displays at events across the ACT;
- facilitating reference groups to share and discuss information on ACTEW projects;

- encouraging community engagement about ACTEW projects by holding public open days;
- developing and promoting public recreation areas, such as the Cotter Dam Discovery Trail and the Canberra Discovery Garden at the National Arboretum Canberra (which provides an educational demonstration of sustainable, water-efficient plantings and water-wise gardening principles);
- supporting education across the region. ACTEW provides an endowment for PhD research at the Australian National University as well as supporting school learning on topics related to the water business; and
- funding a wide range of community events and community support programs annually (over 20 community events and 48 community support programs were funded by ACTEW in 2012-13), together with the provision of support to Canberra's 2013 Centenary celebrations.

ACTEW is proud of its history of supporting the Canberra community and, in a city that has few large corporations to provide sponsorships or community support, ACTEW believes that this is an important element of its business.

In this regard, ACTEW was asked by the Voting Shareholders in December 2012 to have an independent review undertaken that considered the governance framework around decision making concerning sponsorships, corporate marketing and entertainment.

ACTEW engaged PricewaterhouseCoopers (**PwC**) to undertake this review, which was led by two Sydney based partners. In relation to sponsorships, PwC, in its summary of findings:

- found that, relative to its water utility peers:
 - ACTEW discloses a high level of detail relating to sponsorship information through its annual reporting process; and
 - ACTEW was the only utility reviewed which publicly disclosed both the total investment and component parts of its sponsorship program;
- suggested that ACTEW could enhance its documentation to more clearly demonstrate how sponsorship related to key business decisions and strategy - including by establishing clearer delineation between sponsorship and marketing activities; and

- suggested that this detailed level of disclosure in addition to the broader information about sponsorship programs and access to funding, could be replicated through ACTEW's website.

The ACTEW Board has already resolved to adopt and implement these suggestions for improvement. Further information on the PwC Governance Review is set out in section 6.3 of this Submission.

3.6. Key Challenges for the Future

While ACTEW believes that it has the structure, vision and processes in place to deal with most future events – there are still some key challenges and circumstances that will have a significant effect on the future operations of ACTEW:

- **Environment** – ACTEW operates in a changing environment - climatic variations are hard to predict and such variations can determine the demands made upon the capital assets of ACTEW. It is critically important that ACTEW remains focused on environmental risks and developments to plan for the future and ensure the continued delivery of services for the Canberra community.
- **Growing customer environmental awareness** - There is a growing environmental and sustainability awareness among the community, leading to an increase in customer expectations. In recognition of this, ACTEW will be promoting its social, environment and economic work, which does not always receive the credit it deserves.
- **Energy**
 - **Rising Energy Prices** - Since July 2007 there has been a significant rise in electricity costs associated with retail and network charges and the pass through of the carbon price from energy companies to its customers. ACTEW has experienced a 40 per cent increase in electricity prices at its large sites and an increase of approximately 230 per cent at its small sites since 2007. Forecasting by SKM-MMA shows this price growth is expected to continue with an additional price increase of up to 60 per cent predicted by 2030. ACTEW has developed a strategy to reduce its energy consumption and greenhouse gas emissions to build resilience to these rising energy prices as well as helping ACTEW reach greenhouse gas emission targets set by the ACT Government.

- **Renewable Technologies** – The cost of renewable technologies has reduced significantly in the past few years and is now becoming a more cost effective alternative for ACTEW. Federal and ACT Governments have renewable energy targets in place and ACTEW has already achieved its target of 15 per cent renewable electricity to comply with the 2012 ACT Government target. However, a change in the political environment may lead to a repeal of the carbon policy or a review of the renewable energy targets, which may reduce or increase electricity prices over the short term (depending on the approach taken by the relevant government).
- **New Technologies** – New technologies may be able to deliver efficiencies within ACTEW, but depending on their size and complexity, may result in significant up front capital costs - particularly where their use requires changes to network infrastructure.
- **Population Growth** – The ACT is one of the fastest growing regions in Australia and its population is expected to increase by 50 per cent between 2007 and 2056, according to the Australian Bureau of Statistics. This will increase the volume of water and sewerage treatment and services required to be delivered by ACTEW. While it has, in part, prepared for this growth through the implementation of the water security projects, ACTEW will need to plan for future growth of its water and sewerage assets and consider the funding options for this growth and the associated costs.
- **Regulatory Simplification and Certainty** – ACTEW is a capital expenditure intensive organisation. Indeed, in most cases ACTEW undertakes projects with significant up front capital expenditure on the basis that over a very long period of time ACTEW will be able to recoup the relevant costs and make an acceptable return. However, this model is severely undermined when there is regulatory uncertainty, and where regulatory decisions are made that impact on the ability of ACTEW to recoup those costs and deliver a return. Without such certainty, it is difficult for ACTEW to justify the incurring of significant upfront costs for the undertaking of major infrastructure projects.
- **Dividend Policy** – as described later in this submission, the current dividend policy is unsustainable. It is not consistent with the industry position, other jurisdictions, or the commercial nature of ACTEW, and has the following effect:
 - given the 100 per cent dividend policy, growth and development of ACTEW can only be achieved through borrowings;



- borrowings have costs – costs that would not be incurred if ACTEW was able to effectively manage its capital;
- borrowings further affect the gearing of ACTEW (noting ACTEW has one of the highest gearing ratios of comparable utilities as a result of the dividend policy); and
- given the borrowings have to be undertaken through the ACT Government, the effective decision making ability of ACTEW Management and the Board is materially reduced. That is, even if a decision was made at the ACTEW level to undertake a project, where that project needed funding (which it almost certainly would, given the 100 per cent dividend policy), the ACT Government would have an effective approval right over the project given that debt could only be raised through the ACT Government.

The current dividend policy is reducing commercial growth, reducing development works, weakening the financial position of ACTEW, and potentially reducing the decision making ability of Management and the Board.

4. Current Governance and Organisational Structure

Summary:

- *ACTEW is managed by a Managing Director and Executive team, who report to the Board.*
- *The Board is appointed by the Voting Shareholders – the Chief Minister and the Treasurer.*
- *The Board has established a number of committees with specific functions to assist the Board in the overall governance and management of ACTEW.*

4.1. Organisational Structure

The corporate strategy outlined in the previous section led to the development of a revised organisational structure that could best facilitate the achievement of ACTEW's mission, vision and strategic imperatives.

The new organisational structure, accommodating approximately 390 staff, was implemented on 1 July 2013 after a carefully planned transition across the business.

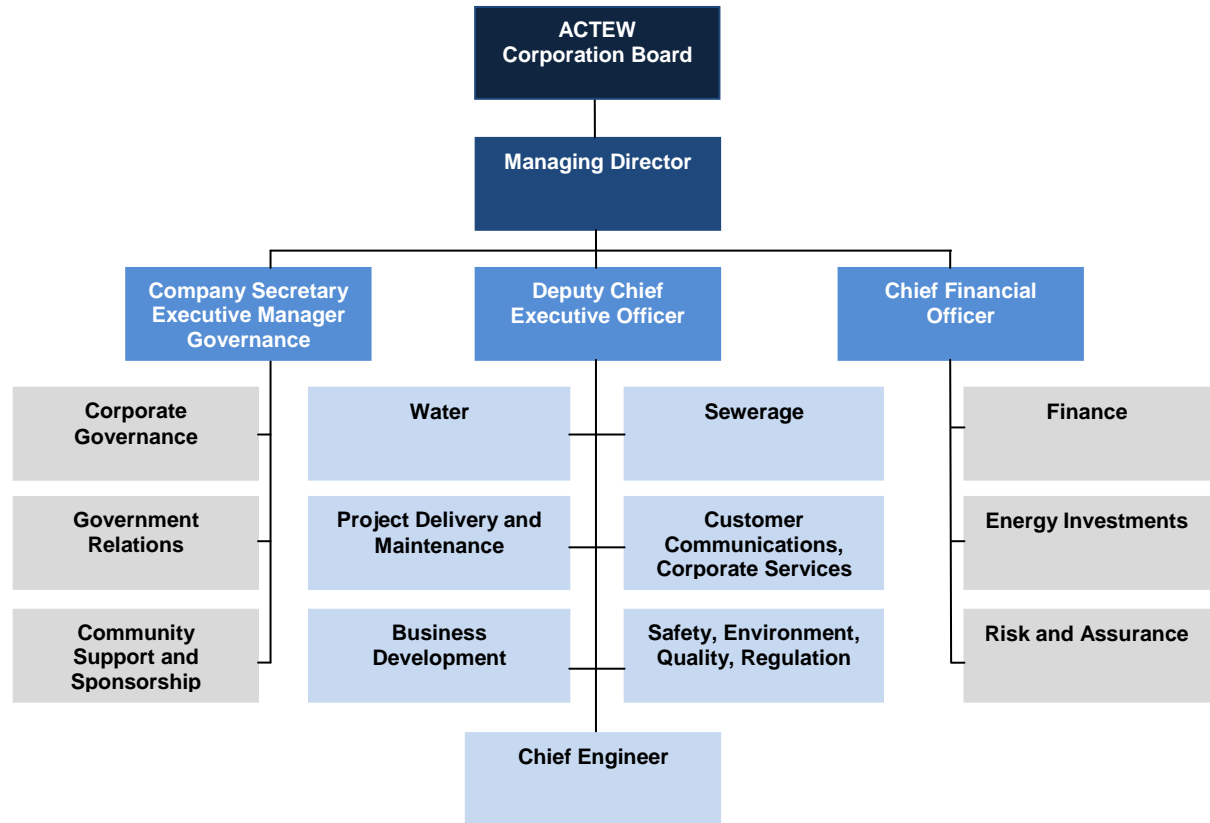


Figure 6. Organisational Structure

The new structure recognises that the provision of water and sewerage services is core to the business, with distinct areas managing each service. This allows for the water and sewerage management teams to each be responsible for their own operations as well as the management and maintenance of their assets. The structure also gives enhanced emphasis to customer relationships, safety, business development, corporate governance, management of ACTEW's energy investments and government relations. This structure allows each area to be more strategic and commercially minded than the previous organisational structure.

4.2. ACTEW Board

The Board exercises a governance, strategic and oversight role in relation to the operation of the water business and ACTEW's investment in ActewAGL, consistent with its obligations under the Corporations Act.

The Managing Director reports to the ACTEW Board, which comprises eight Directors: seven Non-Executive Directors and the Managing Director.

In addition to their obligations under the Corporations Act, the ACTEW Constitution, common law and relevant accounting and reporting requirements, the TOC Act also

places the Board members under a set of specific obligations, including that the Directors must:

- as soon as practicable after becoming aware of a ‘significant event’ affecting the ACTEW Group, tell the Voting Shareholders about the event;
- give effect to a lawful direction by the Voting Shareholders under section 17 of the TOC Act;
- ensure that the applicable ACT Government policies advised to it by the Voting Shareholders are, as far as practicable, complied with by ACTEW;
- establish an audit committee;
- prepare and submit ACTEW’s Statement of Corporate Intent; and
- give the Voting Shareholders, within the prescribed period after the end of each financial year, an annual report on the operations of ACTEW.

4.3. Board Committees

To assist in the overall management of the organisation, the Board has established the following committees to provide high standards of governance accountability and compliance under the umbrella of the Corporate Governance Charter:

- ***Audit and Risk Management Committee*** – to oversee risk management and review ACTEW’s risk register; to review the outcomes of external and internal audits and ensure the accepted recommendations are addressed; and review and endorse financial statements.
- ***Safety and Environment Committee*** – to review and endorse standards, work practices and behaviours that promote safety and environmental performance and review investigations of major safety or environmental incidents.
- ***Remuneration Committee*** – to set the remuneration and employment terms and conditions for the Managing Director and to monitor and review his performance.
- ***Nomination Committee*** – to advise on the composition and performance of the Board, to assist in ensuring the Board is comprised of the right mix of skills and develop succession plans for the Chairman and the Managing Director.



4.4. Executive

Day to day management of the Corporation is undertaken by an Executive team comprising the Managing Director, Deputy Chief Executive Officer, Company Secretary and Chief Financial Officer.

5. ActewAGL Investment

Summary:

- *ACTEW is a 50 per cent owner of ActewAGL.*
- *ActewAGL was established by both legislative and contractual arrangements.*
- *Two separate partnerships make up ActewAGL – ActewAGL Distribution which owns and manages networks, and ActewAGL Retail which provides services to customers.*
- *ActewAGL Distribution and ActewAGL Retail also provide corporate services to ACTEW, to support the delivery of the water business, under separate services agreements.*

5.1. Ownership Structure

As noted above, ACTEW is a 50 per cent owner of ActewAGL, a multi utility provider of electricity and gas services to the ACT and surrounding regional New South Wales centres. ActewAGL comprises two partnerships:

- **ActewAGL Retail** - a partnership between ACTEW Retail Limited and AGL ACT Retail Investments Pty Ltd. This partnership is owned equally by AGL Energy Ltd (**AGL Energy**) and ACTEW via their respective subsidiary companies; and
- **ActewAGL Distribution** - a partnership between ACTEW Distribution Limited and Jemena Networks (ACT) Pty Limited. This partnership is owned equally by SPI (Australia) Assets Pty Ltd (through its interest in Jemena Limited (**Jemena**)) and ACTEW via their respective subsidiary companies.

The ActewAGL structure is set out below:

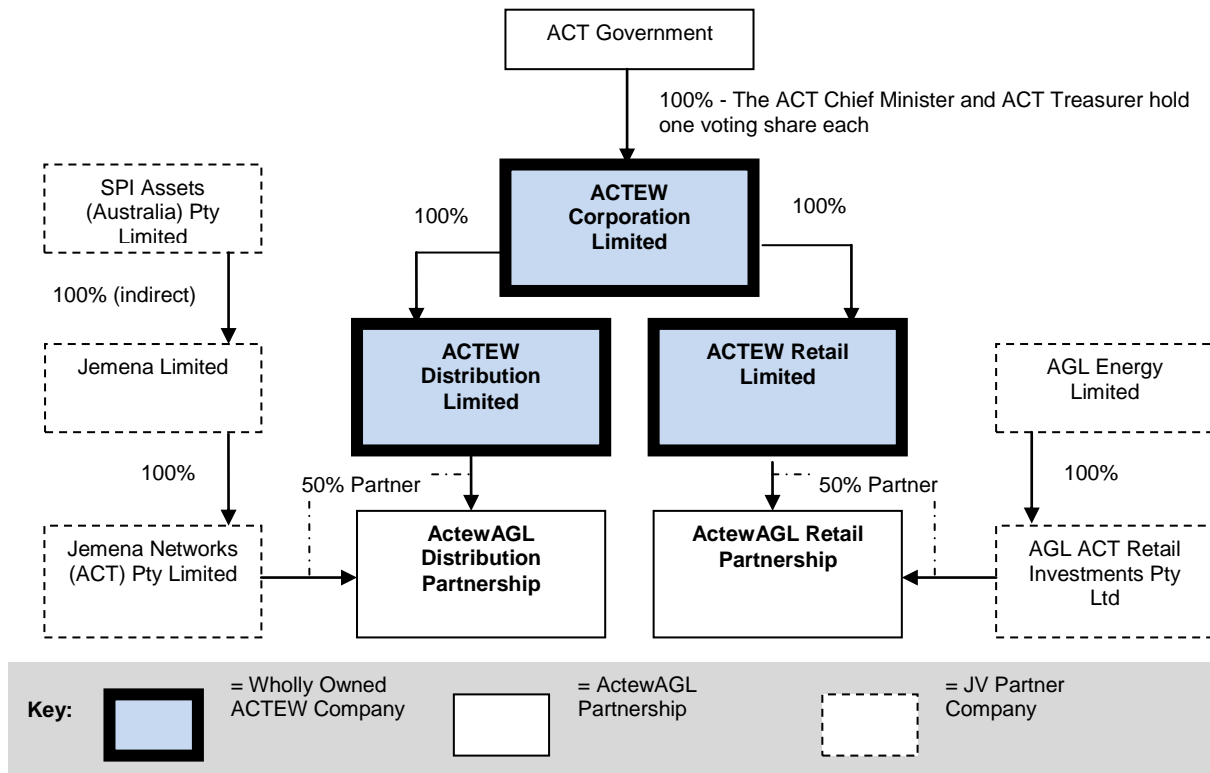


Figure 7. ActewAGL ownership structure

Note that as of May 2013, Singapore Power International Pty Ltd and State Grid International Development Limited entered into an agreement for the latter to purchase a 60 per cent shareholding in SPI (Australia) Assets Pty Ltd. The shareholding transfer has not yet been finalised.

5.2. Functions and Operations

ActewAGL Distribution owns and operates the electricity network in the ACT and the gas network in the ACT, Shoalhaven and Queanbeyan regions.

Until July 1 2012, ActewAGL Distribution also managed the ACT’s water and wastewater network on behalf of ACTEW. While these services have now been integrated back into ACTEW, ActewAGL Distribution continues to provide corporate and other services to ACTEW under a number of agreements (these are discussed later in this submission).

ActewAGL Retail provides customer service and marketing of electricity, gas and water. ActewAGL Retail also provides certain retail services to ACTEW.



ActewAGL's energy network operations are located in the ACT, with the retailing of energy occurring throughout the Capital region, which extends to areas such as Goulburn, Boorowa, Yass, Young and Shoalhaven.

5.3. ACTEW's Approach to Managing the ActewAGL Investment

ACTEW's approach to managing its investment in ActewAGL is founded upon the following three principles:

- ACTEW should at all times be an active and informed investor in ActewAGL. To this end, ActewAGL's Partnerships Board consists of six members, three of whom are ACTEW appointees;
- The investment should deliver benefits to ACTEW which are consistent with ACTEW's main objectives under the TOC Act; and
- Given ACTEW's reliance upon ActewAGL for the provision of corporate services, in making any decision about its investment in ActewAGL, ACTEW considers whether the relevant decision would result in any operational impacts on ACTEW.

5.4. Legal Establishment of ActewAGL

ActewAGL was established through both legislative and contractual arrangements. In this regard, reference should be made to the following establishment documents:

- **ACTEW/AGL Partnership Facilitation Act 2000** - this Act allowed for the vesting of assets, rights and liabilities in the ActewAGL partnerships and dealt with other matters concerning the treatment of employees, public accountability and the treatment of assets at the end of the ActewAGL joint venture.
- **ACTEW/AGL Completion Agreement** - this contract dealt with the terms upon which ACTEW and AGL agreed to establish the ActewAGL partnerships between their subsidiaries and the vesting of assets in those partnerships (including relevant gas and electricity assets).
- **ACTEW/AGL Umbrella Agreement** - this contract governs the on-going management arrangements of ActewAGL, including in relation to the establishment and operation of the Partnerships Board. The Partnerships Board is constituted as follows:
 - three members appointed by Jemena Networks (ACT) Pty Limited and

AGL ACT Retail Investments Pty Ltd; and

- three members appointed by ACTEW Retail Limited and ACTEW Distribution Limited.

The function of the Partnerships Board is to manage the business of the ActewAGL partnerships on behalf of the partner companies and in the interest of the business of both partnerships as a whole.

- **ActewAGL Management Agreement** - this contract governs the manner in which AGL Energy and Jemena co-operate to give effect to certain provisions of the Umbrella Agreement, namely in relation to the appointment and removal of the private sector members to the Partnerships Board and those members' decision making and voting on the business of the ActewAGL partnerships.
- **Partnership Agreements** between:
 - ACTEW Distribution Limited and Jemena Networks (ACT) Pty Limited in respect of ActewAGL Distribution; and
 - ACTEW Retail Limited and AGL ACT Retail Investments Pty Ltd in respect of ActewAGL Retail.

The Partnership Agreements place certain governance and management requirements on each partner, but also operate in conjunction with the Umbrella Agreement to establish the partnerships that make up the ActewAGL joint venture. ACTEW is not a party to either Partnership Agreement.

- **Wholesale Electricity Sale Agreement** under which AGL Electricity (a wholesale provider of electricity) sells electricity to ActewAGL Retail for subsequent resale.
- **Wholesale Gas Sale Agreement** under which AGL Wholesale Gas (a wholesale provider of gas) sells gas to ActewAGL Retail for subsequent resale.
- **Corporate Services Agreements** between ActewAGL and ACTEW, being the:
 - Corporate Services Agreement between ACTEW and ActewAGL Distribution (**CSA**) - this agreement sets out the terms under which ActewAGL Distribution provides corporate services to ACTEW for a fee. These services are wide ranging and include accounts payable, business



systems, human resources, regulatory, tax and accounting, and legal services; and

- Customer Services and Community Support Agreement between ACTEW and ActewAGL Retail (**CSCSA**) - this agreement sets out the terms under which ActewAGL Retail provides retail services to ACTEW in relation to its water and sewerage business.

Please note the above lists the main agreements in relation to the ActewAGL joint venture - there are other ancillary agreements, including in relation to intellectual property, trademarks, charges and staff.

6. Successes of the Current Structure

Summary:

- *The current structure of ACTEW and its relationship with ActewAGL has been a success.*
- *ACTEW and ActewAGL consistently deliver safe, secure and reliable water and energy services to over 360,000 people each day.*
- *There have been financial, risk, service and efficiency benefits with the current structure.*
- *ACTEW believes there should be a greater emphasis on the application of the Corporations Act, the ACTEW Constitution and the Statement of Corporate Intent in the governance and accountability framework for ACTEW.*

6.1. ACTEW Structure and ActewAGL

The current ACTEW structure and the relationship with ActewAGL has resulted in the safe, reliable, efficient, cost effective and secure provision of utility services.

In particular:

- ACTEW and ActewAGL consistently deliver energy services, safe drinking water and reliable sewerage services to a local community of over 360,000 people, and energy services to regional communities.
- ACTEW has undertaken significant capital expenditure projects over the last 10 years (in excess of \$1.2 billion) for the purpose of ensuring the continued provision of these services to the community. While providing long term water security, these capital expenditure projects have also stimulated the local economy and provided jobs to hundreds of people.

In addition to the above, there are other benefits arising out of the current structure. For instance:

- There have been significant financial benefits for the ACT Government and, through it, the ACT community - since 2000 ACTEW has returned **\$1.4 billion**

to the ACT Government (in addition to a further \$100 million previously paid), in the form of:

- \$812 million in dividends;
- \$174 million in taxes;
- \$300 million in capital repatriations; and
- the \$119 million equalisation payment.

In 2000, the Electricity Business, which at the time was 100 per cent owned by ACTEW returned a profit of \$48 million. In 2012, with ACTEW having contributed the electricity business for a 50 per cent share in the joint venture, ActewAGL returned \$81 million to ACTEW. This is almost double the return ACTEW was receiving when it was the 100 per cent owner 12 years ago. When you also consider that ACTEW was also paid \$119 million when entering the joint venture, this is an incredibly significant achievement.

- The current links between ACTEW and ActewAGL have provided critical synergies between the gas, water and electricity networks. There has been a significant transfer of knowledge and experience between ACTEW and ActewAGL across all levels of both organisations from the staff/management level through to Board level (with common Board members). Amongst other things:
 - there has been a consistent approach taken to network management, to the production of standard processes and procedures, to the production of documentation and to emergency planning and response. A practical example of the mutual benefits that have been achieved was during the 2003 bushfires, where a unified emergency plan was deployed across both water and energy networks;
 - ACTEW and ActewAGL have been able to act in a co-ordinated manner in relation to the construction, development and management of significant infrastructure; and
 - network planning can be undertaken in a holistic manner – covering all aspects of the delivery of utility services.
- By corporatising ACTEWA, an element of business risk and liability protection was provided to the ACT Government. In short:

- the corporation is responsible for liabilities arising out of the business;
- the corporation is responsible for managing those liabilities;
- the corporation is responsible for managing business risk; and
- the corporation is responsible for ensuring the efficient and safe management of the business.

The main financial risk for the ACT Government is in relation to the dividend payable by the corporate entity.

- There is a regular examination of ACTEW's pricing, asset base and future capital expenditure to ensure appropriate pricing of water and other services;
- The corporate and support services required by both ACTEW and ActewAGL are similar. Given this, rather than develop its own corporate services capability, ACTEW has leveraged off ActewAGL corporate services through corporate service level agreements. As noted above, ActewAGL provides human resources, business systems support, legal, regulatory, finance, marketing and retail services (including account management, billing, and contact centre). This arrangement benefits ACTEW as it has access to ActewAGL economies of scale and does not have to "double up" on internal management costs.
- Service standards have remained consistent and there have been no major operational or services issues that have arisen since corporatisation – the development and operation of the utility networks in the ACT have been consistently safe, secure and provided to a best practice standard. This is supported by the National Water Commission's 'National Performance Report 2011-12 for Urban Water Utilities', which shows ACTEW benchmarks well against comparable utilities.
- The business structures of ACTEW and ActewAGL have provided a flexible model that has allowed both organisations to develop organically over time. It has allowed the organisations to adapt and deal with a variety of issues, operate with a commercial mindset and capitalise on these efficiencies to make the most of the operating environment.
- The corporation structure has allowed ACTEW to consider and be involved in other businesses and activities - including in relation to TransACT, Ecowise Environmental, acquisition of businesses and as a partner or consortium member in activities undertaken or proposed by ActewAGL. In this regard,

because it has adopted a standard corporate structure, it has been able to more easily enter into commercial arrangements and take commercial risks (balanced against its responsibility to provide utility services) for the purposes of maximising its return to shareholders and the ACT community.

6.2. ICRC's view of ACTEW's Structure

Comments made about ACTEW's governance and structure by the ICRC in its final report on regulated water and sewerage service issued in June 2013 also require consideration. The ICRC sought to revisit and reaffirm the core reasons for establishing ACTEW, including to:

- provide incentives to improve efficiency within ACTEW by setting appropriate performance and accountability targets;
- separate the regulatory functions from the company;
- identify and fund accordingly the government's community service obligations;
- allow the corporate body to set itself up along company lines, in line with the corporations law;
- put it on a comparable footing with other commercial enterprises to become competitive; and
- allow the government and the community to maximise the returns on their investment in such enterprises.

ACTEW agrees with the ICRC's comment that there is no compelling reason to change the actual corporate entity or existence of ACTEW. Indeed, ACTEW believes that the most appropriate structure for the operation of the water business in Canberra is a corporate one - providing a simple and well known structure for the operation of the business.

ACTEW would, however, like to comment on some points in the ICRC's report:

- ACTEW's position is that the Corporations Act, its Constitution and the Statement of Corporate Intent could be better used to provide objectives or goals for ACTEW to meet in the provision of services. In particular ACTEW considers that:

- the Corporations Law provides effective instruments for the setting of such targets and goals, including through the operation of the Constitution; and
 - a greater focus on the corporate nature of its operations - with particular focus on the Constitution and shareholders' rights - would be an appropriate way to implement targets or objectives for ACTEW to achieve.
- ACTEW believes that the TOC Act should be seen as "supplemental" to the Corporations Act, and that some provisions of the TOC Act are inconsistent with those in the Corporations Act.
 - On the question of externally imposed service standards, ACTEW notes that it has detailed obligations under its Customer Contracts to deliver services to certain standards, under the Service and Installation Rules and the various Codes implemented under the Utilities Act.

6.3. Governance Review

As noted briefly above, in December 2012 the Chief Minister requested the ACTEW Board undertake a review into the governance arrangements for the Corporation. The PricewaterhouseCoopers review was commissioned in February 2013. PwC assessed ACTEW's governance framework against corporate governance themes including structure, management and oversight, remuneration, ethical decision making, stakeholder management, reporting and risk management.

The review found ACTEW's governance framework to be consistent with key principles of effective governance and identified a number of key strengths and proactive steps being taken to continuously improve and strengthen ACTEW's governance.

The Board also noted opportunities for further improvement described by PwC and has asked ACTEW management to prepare an implementation plan.

The review was publicly released on 19 August 2013 - a copy of the report can be found at www.actew.com.au/News and Publications/Reports and Publications/Key Publications

7. Issues with the Current ACTEW Structure

Summary:

- *As with any business there are always areas of the structure and operations that could be improved or which may benefit from further consideration.*
- *It may be of benefit to further review and consider whether the current structure is too complex, restricts commercial growth and flexibility, and exposes the separate businesses of water and energy to risks and loss incurred in the other.*

While ACTEW believes that the corporatisation of ACTEWA and the holding of the interest in ActewAGL by ACTEW has been a success, as with any business, there are areas that could be improved or which could benefit from further consideration. In this regard:

- The complexity of the structures of ACTEW and ActewAGL has led to some confusion regarding the responsibilities and functions of each business. In particular there has been lack of clarity:
 - concerning the operational roles and responsibilities of ACTEW and ActewAGL;
 - concerning the branding of the organisations, including in relation to the provision of sponsorships and other community support;
 - concerning the status of ActewAGL - there may not be an appreciation that it is a commercial joint venture with private sector participants, each based interstate, and each of whom contribute to the Canberra community through their involvement in the joint venture; and
 - around the business development activities of the two organisations - noting that ActewAGL, as a commercial joint venture, is able to be undertake a greater range of strategic investments and activities.

The similar names and branding have not helped in developing an understanding of the demarcation between the two organisations. In this regard, as discussed later in this submission, ACTEW is considering a name change of ACTEW Water to further differentiate its business from that of ActewAGL.

- The opportunities for growth and commercial flexibility are currently restricted by the regulatory system that ACTEW operates in - a model that:
 - hinders ACTEW's ability to independently obtain debt facilities - meaning all major activities are effectively subject to government oversight (as discussed later in this submission); and
 - limits ACTEW's ability to move quickly in relation to business opportunities or acquisitions given the consent and approval requirements under the existing regulatory framework.
- As noted previously, the 100 per cent dividend policy imposed by the ACT Government limits the commercial potential of using funds for alternative purposes.
- The present legal and commercial identity of ACTEW and ActewAGL has the risk that if one business was to suffer a significant impact or loss, the other business may also be significantly impacted. For example, if there was a significant impact of any type in the water business, this impact may also be felt on the energy side of the business because of ACTEW's joint involvement in both the water and energy business, notwithstanding that the relevant impact otherwise had no link with the energy business. Arranging the businesses so that they are independent of one another, or marketed as such as different brands, may decrease this potential risk, particularly reputational risk.
- Due to the confusion around the differentiation between ACTEW and ActewAGL (as discussed above), there is a perception in parts of the community that there is a duplication of roles between the organisations. While a perception only, ACTEW accepts that perceptions matter and that it would be preferable to adopt a structure where it was transparent that there was no duplication or confusion of the business activities, management and community obligations of ACTEW and ActewAGL.

8. Potential New Structure

Summary:

- *ACTEW considers there are four main options for consideration:*
 - *Given the success of ACTEW and its relationship with ActewAGL – maintain the status quo;*
 - *A change of name of ACTEW to differentiate it and its role from that of ActewAGL, coupled with enhancing the governance of the investment in ActewAGL;*
 - *A formal separation of the ActewAGL business from ACTEW – the ActewAGL investment would be transferred to a new territory company and ACTEW would leave the ActewAGL joint venture;*
 - *A restructure of ACTEW’s investment in ActewAGL so that it was held by a new subsidiary of ACTEW – attempting to further separate the energy business from the water business without the need for the formal separation described above.*
- *Each option has benefits and risks and involve different levels of complexity to implement the relevant change.*

8.1. General

Given the advantages and disadvantages with the current structure, it is appropriate to constantly review and consider the legal and regulatory structure of ACTEW.

In this context, and taking into account the issues raised as part of this Institutional Review, ACTEW considers that there are a number of potential options concerning the structure of ACTEW that may be considered. These options include:

- given the successes of the current structure, maintain the status quo with no change to ACTEW or its holding in ActewAGL; (**Option 1**)
- changing the name of ACTEW to better differentiate the company, its business and its responsibilities from ActewAGL and enhance the reporting and governance requirements for the ACTEW Partners in the ActewAGL joint venture; (**Option 2**)

- changing the name of ACTEW as contemplated under Option 2 and separating ACTEW's interest in the electricity and gas business operated by ActewAGL (**Energy Business**) from its water and sewerage business (**Water Business**); (**Option 3**) and
- changing ACTEW's name as contemplated under Option 2 and utilising a subsidiary of ACTEW to hold ACTEW's interest in ActewAGL. This would have all the advantages of changing ACTEW's name, but also structurally separate the Energy Business from the Water Business. (**Option 4**)

Each option will be considered in turn.

8.2. Option 1 - Status Quo

As noted in section 6 - ACTEW and its investment in ActewAGL have been an enormous success for the ACT community. In this regard:

- the financial returns have been significant for the Voting Shareholders;
- there have been no major operational or service issues with respect to the services provided by ACTEW and ActewAGL;
- ACTEW has undertaken major capital works programs that have ensured the secure supply of water for coming generations - these projects include the Enlarged Cotter Dam, the Stromlo Water Treatment Plant, and the M2G Pipeline;
- the pricing for the water services are the second cheapest of any Australian capital city - and this is notwithstanding the major costs of undertaking the capital works referred to above;
- ACTEW and ActewAGL have continued to support the ACT Community through a range of sponsorships and other activities; and
- the holding of the ActewAGL investment by ACTEW has allowed for synergies and efficiencies to develop between the two organisations - there has been the sharing and development of commercial, operational, engineering, governance and financial expertise and knowledge.

The current structure has resulted in a very successful utility enterprise.



8.3. Option 2 - Name Change and Enhanced Subsidiary Governance Arrangements – ACTEW’s Preferred Option

However, as noted in section 7, there are some areas of the current ACTEW structure that may be improved. In particular, one common theme concerning the structure of ACTEW has been a level of confusion amongst stakeholders and the public concerning its role and identity and that of ActewAGL.

To assist in establishing the demarcation between ACTEW and ActewAGL, ACTEW is considering:

- a full branding and name change. Such a change is relatively easy as it does not involve any change to the structure of ACTEW, to any of its contracts, or to any Act or other determination or instrument; and
- enhancing the reporting and governance arrangements between ACTEW and its subsidiary company partners in the ActewAGL joint venture - ACTEW Distribution Limited and ACTEW Retail Limited.

This is currently the preferred option of the ACTEW Board.

With respect to the name change, ACTEW has considered some of the steps that would need to be taken to affect such a name change:

1. Corporations Act Requirements

If ACTEW wanted to change its name then, under the Corporations Act, it must:

- pass a special resolution adopting the new name in accordance with the requirements of the Constitution; and
- lodge an application with the Australian Securities and Investments Commission (ASIC) within 14 days after the special resolution is passed.

The change of name takes effect when ASIC alters the details of ACTEW's registration.

2. Constitution Requirements

While ACTEW's Constitution has no specific requirement concerning a change of name - if ACTEW does change its name it may be preferable to amend the Constitution to refer to the new name and replace the references to ACTEW.

In this regard, under the Corporations Act, ACTEW can amend its Constitution by special resolution and must lodge a copy of that special resolution and the amended Constitution with ASIC within 14 days.

3. TOC Act Requirements

Section 16A of the TOC Act requires that ACTEW's Directors inform the Voting Shareholders if they become aware of a significant event that affects ACTEW. Therefore, if a conservative position was taken, this name change would constitute such an event.

4. Legal effect of Name Change under Corporations Act

It should be noted that a change of an Australian company name does not:

- create a new legal entity;
- affect the company's existing property, rights or obligations; or
- render defective any legal proceedings by or against the company.

That is, any change in ACTEW's name:

- is unlikely to affect ACTEW's rights or obligations under any existing legislation, determinations, or other instruments (including the TOC Act and existing legal proceedings); and
- would have no effect on ACTEW's rights and obligations under any existing contracts (including any existing supplier contracts).

5. Customer Contracts

While ACTEW's Customer Contracts currently refer to "ACTEW" throughout, clause 14.1 of the contract permits ACTEW to vary the terms of the contract at any time in accordance with the Utilities Act.

6. Other Process Matters

Other matters that would need to be dealt with in changing ACTEW's name include:

- undertaking an extensive marketing campaign to inform the Canberra community about the new name;

- while the TOC Act does not specifically deal with the ability of a territory-owned corporation to change its name, the TOC Act does refer to "ACTEW Corporation Limited" in its text. However, the Act foreshadows that name changes are acceptable - section 6(2) of the TOC Act states that:

"A regulation may amend schedule 1 to reflect a change in the name of a company."

This power does not appear to extend to amending the other references to "ACTEW Corporation Limited" in the Act, and for clarity these references may ultimately need to be changed by an amending Act at some future time;

- registering new business names;
- in relation to relevant intellectual property arising out of the change of name (i.e. logos and other trademarks):
 - apply to IP Australia to register any new trademarks and other IP or branding related to the new name; and
 - once the name is changed ACTEW needs to notify IP Australia of this in relation to any trademarks and other IP of which ACTEW is the owner;
- production of a new common seal and changing stationery and other documentation and branding material to refer to the new name; and
- registration of a new Domain Name with The Australian Domain Name Administrator (auDA).

With respect to the enhancement and formalisation of the governance arrangements between ACTEW and its subsidiaries, while ACTEW already actively manages its investment in ActewAGL (as referred to in section 5.3 above), including managing the investment in accordance with the Corporations Act and applicable governance requirements, ACTEW proposes to further enhance this governance by implementing the following requirements in relation to its ACTEW Partners in the ActewAGL joint venture:

- at each ACTEW Board meeting ACTEW Management (through the Managing Director) would be required to provide a formal report on the performance of ActewAGL from an ACTEW perspective - covering any significant events or future issues in relation to ActewAGL;

- a Director of the subsidiary companies (most likely the Managing Director of ACTEW) must report on the actions of the subsidiaries in relation to their participation on the Partnerships Board for ActewAGL;
- relevant personnel within ACTEW who currently manage the energy investments would be seconded to the subsidiaries to undertake that role; and
- there is a formalisation of the support provided to the subsidiaries by ACTEW - to recognise and emphasise the different business of the subsidiaries from the parent company.

The point of the above formalisation is to:

- place greater emphasis on the roles of the subsidiaries so as to further detail the delineation between the functions of ACTEW and the subsidiaries - i.e. to provide greater delineation between the operations of the water business (as undertaken by ACTEW) and the energy business (as undertaken by the subsidiaries of ACTEW);
- ensure that there is a regular, formal and clear governance review of ACTEW's investment in ActewAGL; and
- allow the subsidiaries to operate on a day to day basis without the need to involve ACTEW - in a practical sense separating the water business from the energy business.

This option 2 is the preferred option of ACTEW - it provides governance, brand differentiation and operational differentiation without the need for a complex, costly and time consuming restructure of ACTEW or ACTEW's investment in ActewAGL.

Key benefits of Option 2

- 1. Relatively simple and quick**
- 2. Lower costs than other options**
- 3. Deals with stakeholder and community confusion concerning ACTEW and ActewAGL**
- 4. Does not require extensive changes to legislation**

5. Allows the seconded management to the subsidiaries to focus solely on the investment in ActewAGL

6. Provides an enhanced and formalised governance framework for the oversight and management of the ActewAGL investment

Key risks of Option 2

1. May be perceived as not dealing with third party perceived governance and structural issues

2. May still expose the Water Business and Energy Business to liability and risk incurred by the other



8.4. Option 3 - Separation of the Businesses and Change of Name

ACTEW considers that changing its name, consistent with Option 2 above, and separating the Water Business from the Energy Business through ACTEW divesting its investment in ActewAGL may:

- through the change in name, deal with some of the misunderstandings of the role of ACTEW as opposed to ActewAGL;
- allow for flexibility with respect to the operation and governance of the Water Business and Energy Business;
- quarantine the two separate businesses from risks incurred by the other business;
- help ensure that the Water and Energy Businesses are managed in a nimble and agile manner (i.e. decisions can be made in relation to those businesses without the need to consider multiple stakeholders in other businesses); and
- allow the two separate businesses to focus on their core areas of business.

While the same issues as set out in option 2 apply in relation to changing the name of ACTEW, on the assumption that there was a view taken that separation of the two businesses was an option to be pursued, ACTEW considers that there are two possible methods by which its Energy Investment Business and Water Business could be separated:

- **Share Sale** - ACTEW transfers its interest in the ActewAGL joint venture to a newly incorporated territory-owned corporation (**NewTOC**) by a share sale in ACTEW Retail Limited and ACTEW Distribution Limited to NewTOC; or
- **Trade Sale** - ACTEW transfers its Water Business to NewTOC by trade sale, but retains its interest in ActewAGL. ACTEW would transfer assets, contracts and personnel associated with the water business to NewTOC, with ACTEW retaining its interest in the ActewAGL joint venture.

ACTEW believes that the share sale would be the preferable approach as:

- it would not require the transfer of title in any physical assets;
- it would not require the transfer or novation of contracts from ACTEW to NewTOC in relation to the Water Business;



- existing energy contracts would remain with the ActewAGL partnerships, with the change in ultimate ownership of the partnerships expected to result in minimal third party contractual variation costs;
- there would be no need to change the Customer Contracts for water under the Utilities Act;
- there would be little or no impact on the operations of the ActewAGL partnerships from a customer perspective;
- there would be little or no need to change employee contracts or the positions of employees; and
- the relevant licences issued under the Utilities Act could remain with their respective parties (i.e. if a new party was to take on the Water Business they would need relevant licences to do so. With the Water Business staying with ACTEW, it can utilise its existing water licences under relevant utilities and environmental legislation).

In the event that a share sale was undertaken, the final structure may be as follows:

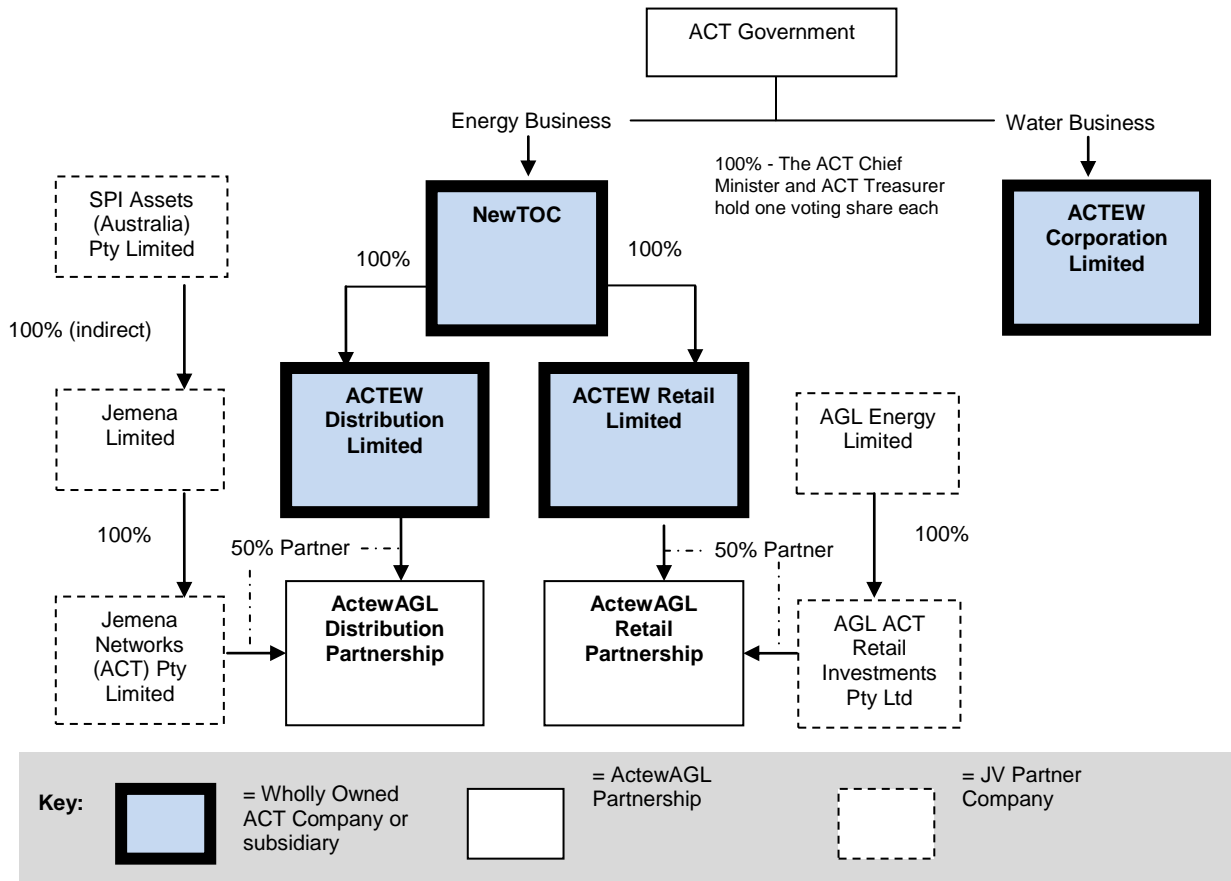


Figure 8. Possible structure post share sale

On the assumption that a share sale is proposed, ACTEW has, at a high level, considered the issues that would need to be considered and/or dealt with to affect such a transaction. Please note that this list of issues is not intended to be exhaustive. If such a transaction was finally recommended, a further detailed analysis of this would need to be undertaken given the complexity of the proposed transaction.

1. Shareholder Consent and Legislative Assembly Approval

In order to transfer its interest in ActewAGL to NewTOC, ACTEW would need:

- the consent of its Voting Shareholders under both its Constitution and the TOC Act; and

- a resolution from the Legislative Assembly approving the transaction and noting the establishment of NewTOC (see sections 9, 13 and 16 of the TOC Act).

In this regard, under section 16 of the TOC Act, ACTEW must not dispose of a main undertaking or enter into a transaction which leads to a company ceasing to be a subsidiary without the consent of its Voting Shareholders and a resolution from the Legislative Assembly approving the transaction.

Further, under section 27 of the *ACTEW/AGL Partnership Facilitation Act 2000 (ACT) (Facilitation Act)*, ACTEW must not, without the prior approval of the Legislative Assembly, dispose of its beneficial interest in an ActewAGL partnership if it would result in ACTEW's beneficial interest falling to below 50 per cent of the total equity of the partnership.

2. Approval of the ICRC

Under the Utilities Act, ACTEW Distribution Limited and Jemena Networks (ACT) Pty Limited (trading as ActewAGL Distribution) hold a:

- Licence to provide gas distribution and connection services under the *Utilities Act 2000 (ACT)*; and
- Licence to provide electricity distribution and connection services under the *Utilities Act 2000 (ACT)*, (**Licences**).

Under clause 10.2 of the Licences, the licence holder is restricted from assigning its interest in the Licence without the prior consent of the ICRC. Under clause 10.4 a change in more than 50 per cent of the shareholding of one of the licensees to a third party is deemed to be an assignment. As such, to ensure that there can be no question of a breach of the Licences, the prior consent of the ICRC should be obtained before transfer of shares in ACTEW Distribution Limited to NewTOC.

3. Facilitation Act Amendments

In addition to providing the authority to the Minister to establish ActewAGL, the Facilitation Act provides the Minister with the authority to make vesting declarations upon a dissolution of the ActewAGL partnerships. In particular, under section 13 of the Act, the Minister may make declarations vesting the assets, rights or liabilities that relate to the reticulation and distribution of electricity in ACTEW or a subsidiary of ACTEW. Such a declaration requires ACTEW's and AGL's consent.

Before ACTEW transfers its interest in ActewAGL to NewTOC, it may be appropriate to consider whether the Facilitation Act should be amended to remove the requirement for AGL consent to a declaration (given it is no longer a member of ActewAGL Distribution) and to state that the relevant assets may vest in NewTOC or a subsidiary of NewTOC (given that NewTOC would be the holding company of the ACTEW Distribution Limited).

Section 28 of the Facilitation Act also states that a company is not eligible to become a joint venture entity to represent the interests of ACTEW in a partnership unless the full beneficial interest in all its shares vest in ACTEW. If a share sale was proposed, it would be prudent to amend this provision at the same time as a resolution of the Legislative Assembly approving the transaction to make it clear that the proposed structure is valid for the purposes of the Facilitation Act.

4. Management of NewTOC

The current view of ACTEW is that NewTOC would have minimal employees and would act as a true holding company. The management of the Energy Business would be run through ActewAGL, and NewTOC's role would be one of managing the investment only, not managing the business.

Given this, while NewTOC would operate as a separate TOC, to avoid costly duplication of management costs and structures between ACTEW, NewTOC and ActewAGL, ACTEW proposes that:

- ACTEW and NewTOC would have the same Board, Managing Director, Company Secretary and Chief Financial Officer;
- NewTOC would enter into an agreement with ACTEW under which ACTEW would provide NewTOC with access to relevant resources and personnel of ACTEW (that is, a small group of ACTEW employees (the current energy investment group within ACTEW) would be seconded to NewTOC);
- new Statements of Corporate Intent and overarching governance arrangements would need to be produced for NewTOC;
- subject to the comment below, NewTOC may enter into a corporate services type agreement with ActewAGL, that may be based on the existing CSA; and
- ACTEW would keep the existing CSA and CSCSA with ActewAGL as these services would still be required for the operation of the Water Business. However, these agreements may need to be renegotiated to reflect the new



structure, and ACTEW may enter an arrangement with NewTOC where these services are supplied to NewTOC.

5. Regulatory Compliance

As outlined in detail below, ACTEW, as a territory-owned corporation, is subject to an extensive governance, compliance and reporting regime. In particular, it is required to produce a wide range of reports for its Voting Shareholders, the ICRC and the ACT Government.

If a new territory-owned corporation was established to hold the investment in ActewAGL, it would be subject to the majority of the reporting requirements that apply to ACTEW.

As a result of the proposed separation the reporting requirements for the current business would effectively double notwithstanding that there was no change in the size or operations of the business.

6. Third Party Contracts

One advantage of separating ACTEW's Water Business and Energy Business by having ACTEW transfer its shares in ACTEW Retail Limited and ACTEW Distribution Limited to NewTOC is that the contracts with ACTEW's and the ACTEW Partner's various suppliers, contractors and customers may not need to be assigned or novated as a result of the transaction, significantly reducing the number of consents and transaction costs associated with the separation of the businesses.

However, if a share transfer was to proceed, ACTEW and/or ActewAGL would still incur costs reviewing all contracts in detail to ensure that they do not contain a change of control or other restriction with respect to ACTEW Retail Limited, ACTEW Distribution Limited or the proposed transfer of the business.

7. Competition Issues

Given that, under this Option 2, ACTEW is not proposing any change to the structure of the partnerships, or the substantive entities or commercial arrangements that are the foundation for the partnerships, ACTEW does not expect any significant competition issues to arise.

This would of course need to be confirmed formally before the transaction occurred.

8. Tax Issues and Pricing



The potential transfer of the ActewAGL partnerships to NewTOC does give rise to questions around the operation of the tax equivalent regime under which ACTEW operates.

While detailed taxation advice would be required, it is likely that ACTEW would submit that given the restructure was imposed by the ACT Government, the transaction should be treated in a tax neutral manner under the national tax equivalent regime.

There is also the question of what effect taking such a significant asset (presumably for little or no return) away from ACTEW would have on the ACTEW balance sheet. In 2012, the ACTEW investment in the ActewAGL partnerships was valued at \$552 million, with the joint venture providing a yearly dividend of approximately \$87 million. Without this level of return careful consideration would need to be made concerning ACTEW's ability to continue to finance debt obligations and ACTEW's security position. In this regard, discussions would also have to be held concerning the transfer of debt obligations currently associated with ActewAGL Distribution.

9. Employment Issues

Given that the proposed transaction does not include a restructure or change to the operational parts of either business, it is not expected that there would be any significant employment issues.

Those employees involved in the Water Business would continue to be employed by ACTEW, and those involved in the Energy Business would continue to be employed by the ActewAGL partnerships.

10. ACTEW Board Issues

Corporations law issues for the Board of ACTEW must also be kept in mind when considering any transfer of the ACTEW partners to NewTOC. In particular:

- under ACTEW's Constitution, the Directors are under a duty to make decisions relating to the operation of ACTEW in accordance with its Statement of Corporate Intent. The current Statement of Corporate Intent does not contemplate a separation of the Water Business and the Energy Business; and
- under the Corporations Act, ACTEW's Directors are under a duty to exercise their powers and discharge their duties with the degree of care, skill and diligence that a reasonable person would exercise if they were in the Directors' position. They can meet this duty when making a business

judgement if they rationally believe that the judgement they have made is in the best interests of ACTEW. Disposing of one of the main business interests of the company (for potentially little or no return), where that interest is more profitable than the business retained by ACTEW, may raise questions as to whether the ACTEW Directors were complying with this duty.

While formal advice may need to be obtained for the Board, these issues may potentially be remedied by the Voting Shareholders issuing a written direction under section 17 of the TOC Act requiring ACTEW to undertake the transfer of the business.

ACTEW also notes that, when the Voting Shareholders provide ACTEW with such a direction, the Territory must reimburse ACTEW for the net reasonable expense of complying with the direction.

11. Lost Productivity and Opportunity Costs

Any transaction such as this is likely to affect the productivity of ACTEW. ACTEW anticipates that this transaction may:

- take time from ACTEW Management to consider, develop and assist in the implementation of the new structure, with time spent managing the transfer of the business;
- take time from the partnerships to the extent that they are required to assist in the implementation of the new structure;
- divert resources from other business development activities; and
- result in incurring third party consultant costs.

12. Existing Joint Venture Documentation

In order for ACTEW to transfer its shares in ACTEW Retail Limited and ACTEW Distribution Limited, there are a number of steps that would need to be taken under the Joint Venture Agreements that establish ActewAGL. Outlined below are some of the steps that would need to be taken under the relevant agreements:

❖ Umbrella Agreement

ACTEW's initial view is that, if it was to transfer its interest in the ActewAGL joint venture to NewTOC, ACTEW would seek to cease being a party to the Umbrella



Agreement (with the result being that ACTEW would effectively leave the ActewAGL joint venture), with its rights and obligations being transferred to NewTOC.

However, in order to achieve this outcome the consent of the other parties to the joint venture would be required. It is also likely, though not certain, that the other parties to the joint venture would require some sort of guarantee from the Territory as to the continued solvency of NewTOC (given that its only assets would be its interest in the ActewAGL Joint Venture).

If a decision was made that ACTEW would remain a party to the joint venture notwithstanding the transfer of shares in the ACTEW partners, then ACTEW would still require consents to such a share transfer under the Umbrella Agreement.

In this regard, it needs to be appreciated that by exiting the joint venture there would be a significant loss in the synergies between ACTEW and ActewAGL. There would be no joint approach to the management of utilities of the ACT and it is almost certain that efficiencies gained in the linking of ACTEW and ActewAGL would be lost.

❖ **Management Agreement**

As with the Umbrella Agreement, if it was to transfer its interest in the ActewAGL joint venture to NewTOC, ACTEW would seek to cease being a party to this agreement, with its rights and obligations being transferred to NewTOC. This assignment or novation would require the consent of each other party to the Management Agreement (see clause 11.9).

The Management Agreement does not otherwise restrict a change of control in the ACTEW partners.

❖ **Partnership Agreements**

Given ACTEW is not a party to these agreements, it does not consider that these agreements would need to be varied, assigned or amended if ACTEW simply transferred its shares in ACTEW Retail Limited and ACTEW Distribution Limited to NewTOC.

❖ **Equitable Charges held by ACTEW over Partnership Assets**

As noted earlier in this submission, ACTEW has rights under the Umbrella Agreements to a share of the assets of the partnerships on their dissolution. In order to protect these rights, ACTEW has equitable charges over the share of the partnership assets related to its initial contribution to the partnerships.



If ACTEW was to transfer its interest in the Energy Business to NewTOC (and on the assumption that the TOC Act is amended so that on dissolution of the partnerships the assets can be declared to vest in NewTOC rather than ACTEW), consideration would need to be given as to whether it was appropriate for these charges to remain with ACTEW, or whether they should be transferred to, or placed by, NewTOC.

❖ **CSA and CSCSA**

As noted above, ACTEW has contracted with ActewAGL for the provision of certain corporate and customer services.

If ACTEW was to transfer its interest in the Energy Business to NewTOC, the parties may need to consider the scope of services received by ACTEW under the CSA and CSCSA and the ability for these services to also be provided to NewTOC - either directly by ActewAGL or through ACTEW. It should be noted that any reduction in the services may also lead to the incurring of unwind, transaction and lost opportunity costs in accordance with the terms of the relevant agreement.

Key benefits of Option 3

- 1. Deals with stakeholder and community confusion concerning ACTEW and ActewAGL**
- 2. Deals with structural issues previously raised**
- 3. Results in a position where risk/liability in one business (i.e. water or energy) is not able to directly affect the other business**
- 4. Would help ensure that the Water and Energy Businesses are managed in a nimble and agile manner (i.e. decisions can be made in relation to those businesses without the need to consider multiple stakeholders in other businesses)**
- 5. Would allow the two separate businesses to focus on their core areas of business**

Key risks of Option 3

- 1. It is a very complex process involving changes to legislation, contracts, third party consents, tax issues and a potential increase in regulatory reporting**
- 2. It would be costly and time consuming to implement**



- 3. ACTEW would lose the business synergies it has built over time with ActewAGL**
- 4. There would be a doubling of regulatory reporting, even though the business has not actually changed**
- 5. The establishment and operation of NewTOC would require additional personnel with associated additional costs and may reduce the return to the shareholders**

8.5. Option 4 - New Managing Subsidiary and Name Change

Option 4 involves the renaming of ACTEW consistent with Option 2 above, and the restructure of the ACTEW group, so that ACTEW's interest in ActewAGL is held by a new subsidiary (**NewSub**) rather than ACTEW itself.

In the event that a share transfer to NewSub was undertaken, the final structure may be as follows:

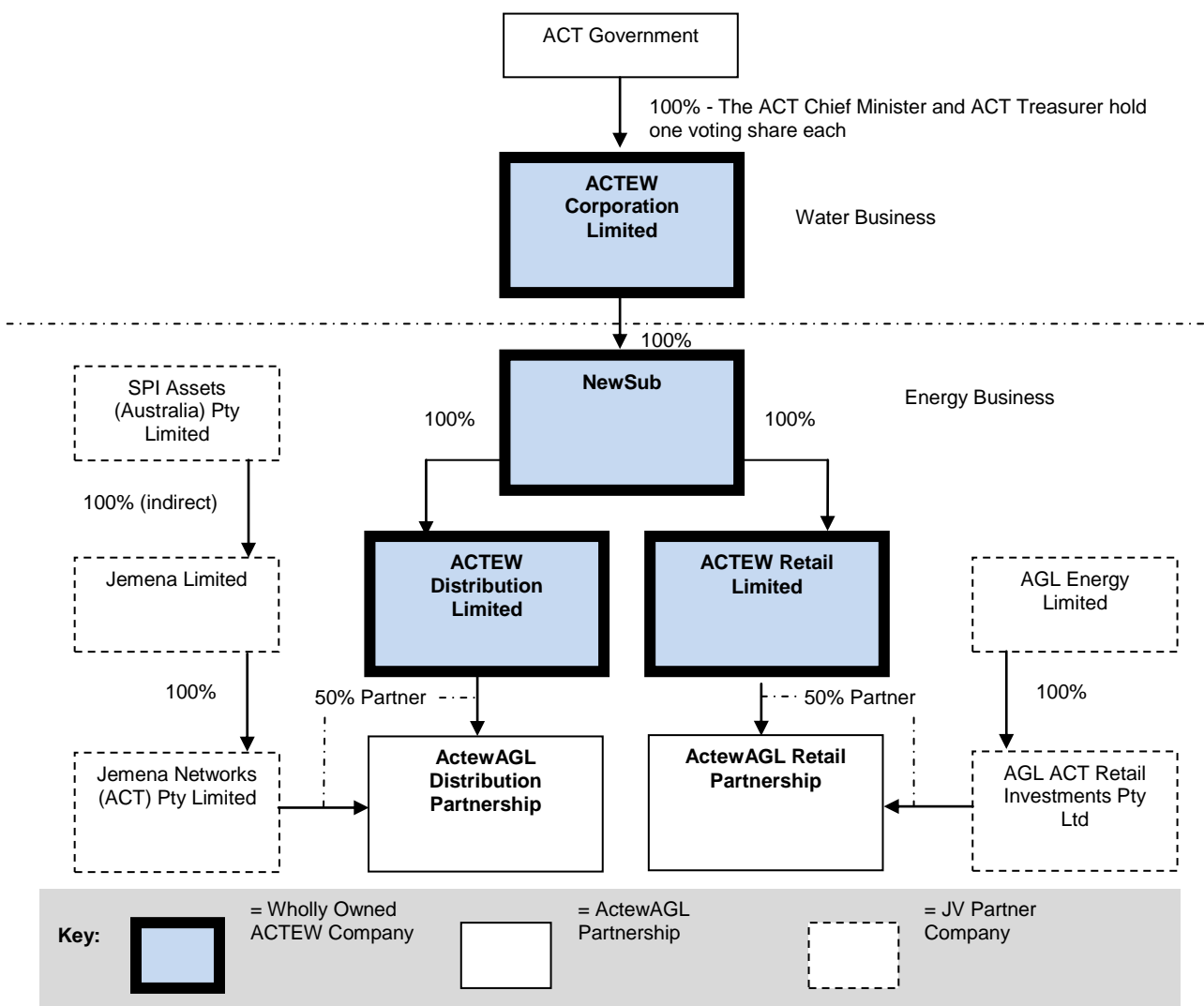


Figure 9. Possible structure share transfer to NewSub

If this option was adopted some issues similar to those described for Option 3 would need to be considered. For instance:

- **Shareholder and Legislative Assembly Consent** - Shareholder consent under the TOC Act would still be required, though Legislative Assembly approval may no longer be required given that ACTEW is not disposing any business undertaking under this option;
- **ICRC Consent** - ICRC consent may still be required (for the reasons set out in the Option 3 section above and depending on the approach taken to the change of control restriction);
- **Amendments to Facilitation Act** - If ACTEW was to retain its ultimate beneficial interest in the ActewAGL Partnerships, it may still be appropriate to consider whether the Act (and, in particular, section 13) should be amended to remove the requirement for AGL consent to a declaration (given AGL is no longer a member of ActewAGL Distribution);
- **NewSub Management** - As with NewTOC, the current view of ACTEW is that NewSub would act as a true holding company. The management of the Energy Business would be run through ActewAGL, and NewSub's role would be one of managing the investment only, not managing the business. In this context, ACTEW would expect that NewSub would be treated as part of the ACTEW group, but would have a small group of ACTEW employees (the current energy investment group within ACTEW) who would be seconded to NewSub and who would take day to day responsibility for the management of NewSub and its investment in ActewAGL;
- **Third Party Contracts** - As with Option 3 referred to above, the contracts with ACTEW's and the ActewAGL Partnerships' various suppliers, contractors and customers may not need to be assigned or novated as a result of the transaction given that there would be no change to the contracting entities for the purposes of those contracts – i.e. there would be no transfer of business;
- **Competition Issues** - As with Option 3 referred to above, ACTEW does not expect any significant competition issues would arise from a share transfer to NewSub;
- **Tax** - Given there would be a share transfer between ACTEW and NewSub of the shares in the ACTEW Partners, as with Option 3, detailed advice on the application of the National Tax Equivalent regime (under the *Taxation (Government Business Enterprises) Act 2003 (ACT)*) would need to be considered. However, the issues surrounding the removal of the ActewAGL asset from the ACTEW balance sheet would not arise – given that the asset remains in the ACTEW Group, just owned by a new ACTEW subsidiary;

- **Employment Issues** - As with Option 3, it is not expected that there would be any significant employment issues arising out of a share transfer in ACTEW Retail Limited and ACTEW Distribution Limited to NewSub;
- **Board Issues** - If ACTEW was to transfer the shares in ACTEW Retail Limited and ACTEW Distribution Limited to NewSub, the Corporations law issues for the Board as described for Option 3 are unlikely to arise, given that ACTEW would not be disposing of one of the main business interests of the ACTEW group;
- **Lost Productivity** - As with the share sale scenario referred to above, any transaction involving the creation of a subsidiary and transfer of shares to that subsidiary is likely to affect the productivity of ACTEW (even if in a relatively minor way); and
- **Joint Venture Documentation** – Given that ACTEW remains in the joint venture under this proposal, and given that the ACTEW partners remain subsidiaries of ACTEW, there would not be any major issues under, or significant amendments required to, the ActewAGL joint venture documentation.

Key benefits of Option 4

- 1. Deals with stakeholder and community confusion concerning ACTEW and ActewAGL**
- 2. It may to a limited extent quarantine the risk/liability in one business (i.e. water or energy) from affecting the other**
- 3. Allows the seconded management of NewSub to focus solely on the business of NewSub's investment in ActewAGL**
- 4. Avoids the double regulatory reporting obligations that would arise with the creation of a NewTOC**

Key risks of Option 4

- 1. It does not fundamentally change ACTEW's structure, or change or address the issues and concerns raised about ACTEW's structure and its accountability mechanisms**

9. Regulatory Framework

Summary:

- ***ACTEW is subject to an extensive framework of legislation that covers accountability, reporting, operations, development, environmental and safety issues.***
- ***ACTEW believes that greater emphasis should be given to its obligations under the Corporations Act and the ACTEW Constitution rather than the TOC Act.***
- ***Many of the obligations of ACTEW under the TOC Act could be either incorporated into the ACTEW Constitution or are already covered by obligations under the Corporations Act.***
- ***ACTEW's strong preference would be to review the regulatory structure around the following key principles:***
 - ***the ICRC should be the primary economic regulator of ACTEW;***
 - ***the primary regulatory operational document for ACTEW should be the Utilities Act;***
 - ***the primary governance document for ACTEW should be the Corporations Act, with the TOC Act supplementing the obligations under the Corporations Act (consistent with the views of the ICRC); and***
 - ***the ACTEW Constitution should be used by shareholders as a governance, accountability and information gathering document, consistent with the intent of the document and the Corporations Act.***

9.1. Regulatory Certainty

In its response to the ICRC's Draft Report into Regulated Water and Sewerage Services in April 2013, ACTEW acknowledged that the role of a regulator is a difficult one. Within the framework of its legislation and terms of reference the ICRC is properly independent. It particularly seeks to ensure that the need for innovation and efficiency, which so often comes naturally in a competitive environment, is not missed in a monopoly setting and it ensures that along with efficiency comes prudent decision making and not over-investment or under-investment.

The ICRC is a small scale regulator with broad powers. It called its recent Draft Report “novel”, which sounded alarm within ACTEW at the time, as it was certainly against previous regulatory practice. What ACTEW seeks is a measured, prudent approach by the regulator. The utility, on behalf of ACT water customers now and in the future, requires regulatory certainty.

ACTEW is a multi-regulated business. It is not just the ICRC that ACTEW deals with, it is also regulated by the Commonwealth, NSW and ACT Governments, covering such things as environmental compliance, drinking water quality, dam safety and water policy issues.

ACTEW's concern is that there may be some current legislative requirements that:

- may not be necessary when taken in the context of ACTEW's obligations under the Corporations Act, and given the rights of the Voting Shareholders under the ACTEW Constitution;
- appear contrary to the concept of ACTEW acting as a corporatised entity; and
- when taken together, impose a regulatory burden on the operations of ACTEW.

ACTEW's strong preference would be to clarify the regulatory structure around the following key principles:

- the ICRC should be the primary economic regulator of ACTEW;
- the primary regulatory operational document for ACTEW should be the Utilities Act;
- the primary governance document for ACTEW should be the Corporations Act, with the TOC Act supplementing the obligations under the Corporations Act (consistent with the views of the ICRC); and
- the ACTEW Constitution should be used by shareholders as a governance, accountability and information gathering document, consistent with the intent of the document and the Corporations Act.

9.2. Corporations Act - Governance and Reporting Requirements

It needs to be remembered when considering the regulatory framework that ACTEW, as a company incorporated under the Corporations Act, is subject to all of the relevant requirements and obligations as set out in that Act.

ACTEW's position is that the application of the Corporations Act is an important part of the accountability regime for ACTEW and that more emphasis should be had on the corporate rights afforded to shareholders, rather than on the development of additional reporting or accountability legislation that largely tries to mirror a public sector framework, which may not be the preferred approach for a corporatised organisation.

In this regard, ACTEW's Directors and Officers are subject to extensive duties and obligations under the Corporations Act, including the following:

1. Directors' and Officers' Duties

Under section 180 and 181 of the Corporations Act, directors must:

- exercise their powers and discharge their duties with care and diligence;
- make any business decisions in good faith and for a proper purpose;
- ensure they do not have any material personal interest in any material decision;
- be properly informed about the business and decisions being made; and
- act in the best interests of the company.

Directors are personally responsible for keeping proper company records and directors that act dishonestly or recklessly can be exposed to civil and criminal penalties.

These are important duties that govern the actions of all members of the ACTEW Board.

2. Records, Financial Accounts and Reporting

Under sections 286 - 289 of the Corporations Act, ACTEW must keep up-to-date financial records that correctly record and explain its transactions and explain its financial position and performance and would enable true and fair financial statements to be prepared and audited.

The financial records that the law requires ACTEW to keep are:

- invoices, receipts, orders for the payment of money, bills of exchange, cheques, promissory notes and vouchers;
- documents of prime entry; and
- working papers and other documents needed to explain:

- the methods by which financial statements are made up, and
- adjustments to be made in preparing financial statements.

ACTEW must also:

- prepare a financial report and directors' report for each financial year;
- have its accounts audited every financial year by an independent auditor registered under and regulated by the Corporations Act;
- provide its financial reports, an auditor's report and a directors' report to shareholders on an annual basis. The Act also sets out the requirements for an annual report and the information that must be contained in such a report; and
- lodge its annual report with ASIC as well as inform ASIC of any changes of details to be kept on ASIC's public database. This includes change of officeholders, shareholders, holding company and solvency.

ACTEW is also required to keep:

- registers of members (shareholders);
- registers of option holders (if applicable);
- minutes of general meetings; and
- minutes of meetings of directors.

None of the above are minor or trivial obligations. ACTEW is required to report, to be audited, to keep records, to provide information and to follow standards of behaviour - requirements that the ACTEW Board takes seriously and upon which it expends time and resources ensuring compliance.

What's more, the information maintained under the Corporations Act can be provided to, and the oversight of actions can be undertaken by, the shareholders in the company - in this case the Chief Minister and Treasurer on behalf of the ACT Government.

9.3. TOC Act Accountability Requirements

In addition to the obligations set out in the Corporations Act, ACTEW must also comply with the reporting and accountability requirements set out in the TOC Act.

Amongst other things, the TOC Act:

- requires ACTEW to show social responsibility and operate in accordance with ecologically sustainable development objectives; (section 7)
- sets additional requirements for the eligibility and appointment of directors; (section 12)
- restricts certain activities with respect to the acquisition of shares by territory-owned corporations; (section 14)
- requires ACTEW to provide a wide range of information to Voting Shareholders, including:
 - an annual report on the operations of the territory-owned corporation, financial reports and an auditor's report;
 - performance reports; and
 - any other information asked for about the territory-owned corporation or a subsidiary; (sections 15 and 22)
- requires shareholder consent and, in some cases, Legislative Assembly approval to undertake certain transactions such as:
 - the acquisition or disposal of the shares in another company;
 - the disposal of a main undertakings or the acquisition of an undertaking that may become a main undertaking;
 - changes to its interests in partnerships, trust or joint ventures; or
 - acquiring, disposing of, mortgaging or giving security over a "significant asset", or giving a charge over a significant part of its assets. (section 16)
- requires the territory-owned corporation to tell Voting Shareholders about significant events that may affect the territory-owned corporation's (or a subsidiary's) value, a significant part of its assets, its performance or the carrying out of a significant activity; (section 16A)
- provides for Voting Shareholders to give directions to territory-owned corporations to perform an activity that may, in the view of the directors of the territory-owned corporation, be against that territory-owned corporation's best commercial interests, and provides legal protections to directors who follow such directions with respect to their ordinary directors' duties; (section 17)

- provides that territory-owned corporations must follow certain Government policies when advised by Voting Shareholders to do so; (section 17A)
- provides that a territory-owned corporation (and its subsidiaries) can only be audited by the Territory Auditor-General; (section 18)
- requires territory-owned corporations to establish an audit committee responsible for:
 - helping the corporation and its directors comply with relevant legislation;
 - providing a forum for communication between the directors and senior managers of the corporation and the auditor-general;
 - overseeing risk management;
 - reviewing accounting and reporting structures;
 - monitoring internal controls and performance; and
 - undertaking reviews or investigations at the request of the directors; (section 18A)
- requires territory-owned corporations to prepare annual Statements of Corporate Intent for the Treasurer's consideration and requires territory-owned corporations to consult with its Voting Shareholders as to the contents of such a statement. This statement must set out:
 - the commercial objectives of the corporation or group;
 - a description of the main undertakings of the corporation or group;
 - a description of the nature and scope of the activities to be undertaken;
 - business and corporate strategies;
 - the targets and performance measurements by which the performance of the corporation or group may be judged in relation to its stated objectives; and
 - any other information that the Voting Shareholders may have requested in writing the directors of the territory-owned corporation to include in the statement. (sections 19 and 20)
- regulates a territory-owned corporation's rights to borrow money from the Territory or privately and the territory-owned corporation's rights to give guarantees for the payment of money or performance of an obligation. (sections 24 and 25).

9.4. Issues for Consideration Regarding the TOC Act Requirements

ACTEW accepts that it is appropriate that it be subject to a certain level of shareholder oversight to reflect its role as a territory-owned corporation.

However, as stated, given the extensive governance and reporting regime in place under the Corporations Act, ACTEW believes that the TOC Act should be seen as a supplemental document to the Corporations Act, rather than as a regulatory governance document in its own right.

Indeed, it may be that much of the reporting and accountability regime of the TOC Act is either already covered by the Corporations Act and the ACTEW Constitution, or could be appropriately incorporated into the ACTEW Constitution.

In this regard:

- sections 12 (appointment of directors), 16 (acquisition/disposal of subsidiaries and undertakings), 21 (modifying a statement of corporate intent) and 23 (adopting a particular financial year period) - as a general proposition, the sections in the TOC Act that state that Voting Shareholder consent is required for a particular activity or transaction could be easily removed from the TOC Act and incorporated into the ACTEW Constitution. Such an approach would achieve a number of things:
 - it would emphasise the corporate nature of ACTEW - put simply ACTEW would be more like other companies with consent requirements and authority limits contained within the corporate constitution;
 - it would emphasise the primacy of the Corporations Act as the governance document for ACTEW;
 - it would simplify compliance issues - there would be only two documents containing the majority of the corporate compliance requirements for ACTEW - the Corporations Act and the ACTEW Constitution;
 - it would allow for simpler updating of the governance requirements from time to time; and
 - it would mean that compliance with the obligations would be governed by the Corporations Act, providing access to the remedies and rights under that Act.

ACTEW does not propose changing the rights of the Legislative Assembly under the TOC Act;

- sections 15 and 22 - many of the reporting requirements under these sections are already covered by the Corporations Act requirements or by the rights of the Voting Shareholders under the ACTEW Constitution. However, if there was a particular reporting requirement needed by the ACT Government, it could be incorporated into the ACTEW Constitution;
- sections 14 and 16 - rather than have a broad section that limits ACTEW's ability to make corporate strategic investments, it may be more consistent with the corporate nature of ACTEW and the Corporations Act for specific restrictions to be included within the ACTEW Constitution (again, allowing for these to be updated from time to time by the Voting Shareholders);
- section 17 - ACTEW accepts the need for this directions power in the context of a publicly owned corporation. However, it may be useful to also incorporate such a requirement or acknowledgement into the ACTEW Constitution;
- section 17A - rather than have a section requiring compliance with Government policy, it may be more appropriate to rely upon the rights of the ACTEW Voting Shareholders under the ACTEW Constitution - noting the basic intent of corporatisation is to treat the relevant business as a commercial entity, rather than a body that is subject to or responsible for the implementation of governmental policy. If necessary, the ACTEW Constitution could be updated to cover this issue in more detail;
- section 18 - ACTEW should be able to use independent auditors on occasion rather than the Auditor-General, especially in circumstances where the Auditor-General outsources the activity to private accounting houses and where the use of an auditor is something that is advised to ASIC;
- section 18A - it may be more appropriate to include the requirement for the audit committee in the ACTEW Constitution;
- sections 19 and 20 - as noted earlier, the Statement of Corporate Intent is an important accountability document. However, given its importance, and consistent with the view that the TOC Act should be supplemental to the Corporations Act, the requirement for a Statement of Corporate Intent should be only covered in the ACTEW Constitution, with a requirement that it be made public for review by customers of ACTEW; and
- section 25 - please see section 10.3 of this submission concerning ACTEW's ability to raise debt in its own right.

9.5. Additional Regulatory Requirements

In addition to its obligations under the Corporations Act, ACTEW is subject to a range of other governance and regulatory requirements that further increase accountability regime for ACTEW. In this section ACTEW has highlighted just some of the legislative requirements that govern how it undertakes its business.

While this legislation serves an important public purpose, it may nevertheless be possible to:

- remove or modify some of the requirements;
- move those requirements to the ACTEW Constitution (for governance type requirements);
- rely on the rights under the Corporations Act; or
- consolidate those requirements into the Utilities Act (for operational requirements).

In this context:

1. *Annual Reports (Government Agencies) ACT 2004 (ACT)*

This Act regulates the presentation of annual reports to the Legislative Assembly from Government Ministers, sets out the requirements for such annual reports and provides details of the relevant Minister to complete each report. ACTEW must, as a public authority, for each financial year prepare a report about the operations of the authority during the year and must comply with an annual report direction from the Minister and provide the statements required by that direction, in accordance with sections 6 and 9 of the Act. The structure of the reporting is based on a public sector organisational framework, not that of a corporate commercial entity. This is a separate and additional reporting requirement to that required by the Corporations Act.

2. *Auditor-General Act 1996 (ACT)*

This Act provides the ACT Auditor-General with powers to conduct performance and financial audits of ACTEW at any time.

Most relevantly, the Auditor-General may audit ACTEW's accounts and records in relation to each financial year and conduct a performance audit at any time. These functions are supported by broad information gathering and access to premises powers.

3. *Dangerous Substances Act 2004 (ACT)*

This Act regulates ACTEW's activities in relation to dangerous substances, like asbestos.

While ACTEW fully accepts that it is important to retain legislative safeguards around the use of such substances, the concern is that the Act requires the implementation of safety management systems (and consequent reporting to the director-general) in relation to the handling of dangerous substances in trade or commerce when ACTEW is already required to adopt safety management processes under the *Work Health and Safety Act 2011*(Act).

If possible, there should be a consistent approach, especially given the extensive obligations that ACTEW has under Commonwealth and ACT workplace safety legislation.

4. *Environment Protection Act 1997 (ACT)*

This Act provides, amongst other things, for ACTEW to take practicable and reasonable steps to prevent or minimise environmental harm and nuisance caused by an activity of ACTEW.

5. *Freedom of Information Act 1989 (ACT)*

This Act gives members of the public rights of access to ACTEW documents (other than those relating to ACTEW's competitive commercial activities), subject to certain exemptions.

6. *Human Rights Act 2004 (ACT)*

This Act provides for the protection and promotion of human rights by entities whose functions are or include functions of a public nature, when it is exercising those functions for the Territory (which includes the services of gas, electricity and water supply).

ACTEW must act consistently with human rights and must not commit any of the unlawful acts set out in the Act.

7. *Independent Competition and Regulatory Commission Act 1997 (ACT)*

This Act establishes an independent commission to regulate pricing, access and other matters in relation to industries involving the provision of water, electricity and sewerage services, and other industries, and to investigate competitive neutrality complaints and government-regulated activities. The commission has access and audit powers and may require National Energy Retail Law retailers bound



by the Utilities Act to conduct audits and provide the results to the commission (section 41).

As stated previously, ACTEW accepts that an Act and body of this type is necessary. However, ACTEW believes that as part of this Institutional Review, consideration should also be given to the role of the ICRC, and the practices and processes it follows, in relation to pricing determinations and other matters. For instance:

- why should the ICRC determine whether or not a particular piece of capital expenditure is or is not part of a community service obligation - ACTEW's position is that this should be a matter best determined by the relevant TOC and the Voting Shareholders – particularly where the Voting Shareholders have been elected by the community and are implementing Government policy for the community;
- should there be a legislative requirement for a detailed consultation and dialogue process between the ICRC and the relevant industry - this in turn may also help reduce the significant costs incurred by ACTEW in preparing submissions for ICRC reviews by focusing all parties on agreed matters of contention;
- should the ICRC be required to follow a consistent approach and method for each review - providing at least some certainty as to the factors that will be taken into account by the ICRC and the scope of potential outcomes;
- should there be an agreed dispute resolution process if the ICRC and relevant industry participant do not agree on process or procedural matters;
- what oversight should the ACT Government have over the ICRC processes - should there be an ACT Government representative as part of each pricing inquiry;
- should there be a formalised right of appeal with respect to ICRC decisions beyond the current rights of review in the Act;
- should reviews, reports and determinations of the ICRC be subject to confirmation by the Voting Shareholders or the relevant Portfolio Minister;
- can utility providers go to the ICRC for confirmation as to the status of projects before undertaking the relevant project; and
- what is the appropriate role of the ICRC in approving the relevant codes under the Utilities Act.

8. *Lands Acquisition Act 1994 (ACT)*

This Act provides for the acquisition of interests in land by the Executive and certain authorities and for dealings with land so acquired. The Act prescribes the process that must be followed by utilities (under section 104 of the *Utilities Act 2000*) to compulsorily acquire land and the compensation payable for such acquisitions.

9. *Ombudsman Act 1989 (ACT)*

This Act establishes the office of the ACT Ombudsman, and provides the Ombudsman power to investigate complaints made against ACTEW as a corporation and its employees. The Act applies to ACTEW as a territory-owned corporation established for a public purpose.

10. *Public Interest Disclosure Act 2012 (ACT)*

This Act is designed to enable people to raise concerns about significant wrongdoings in the public sector without fear of reprisal.

As a result of the Act, ACTEW has established guidelines and a corporate procedure for making and investigating public interest disclosures.

11. *Taxation (Government Business Enterprises) Act 2003 (ACT)*

This Act gives effect to the National Tax Equivalent regime in the ACT with respect to ACTEW Corporation Limited, ACTEW Distribution Limited and ACTEW Retail Limited.

12. *Territory-owned Corporations Act 1990 (ACT)*

As outlined above in detail, this Act imposes additional reporting and corporate governance requirements on ACTEW, its Directors and its Voting Shareholders.

13. *Territory Records Act 2002 (ACT)*

This Act applies to ACTEW as a territory-owned corporation, and imposes on ACTEW obligations in relation to the creation, management (including having an approved records management program), keeping, protection, preservation, storage and disposal of, and access to, records.

14. *Tree Protection Act 2005 (ACT)*

The objects of this Act include protecting individual trees in the urban area that have exceptional qualities because of their natural and cultural heritage values or their contribution to the urban landscape and ensuring trees of value are protected during periods of construction. ACTEW has a responsibility to outline protected trees to employees to ensure that these trees are protected when commencing construction.

15. Utilities Act

This Act regulates the provision of certain gas, electricity, water and sewerage utility services in the Territory - it is the key regulatory document for ACTEW and ActewAGL.

Under the Act ACTEW must, amongst other things:

- have and maintain a licence to provide utility services in accordance with ICRC conditions (sections 21(1) and 25);
- provide the ICRC with an annual financial report in relation to the exercise of its functions and compliance with the conditions of its licence under the Act (note the provision of another additional financial report) (section 25(2)(d));
- comply with the relevant industry codes - these codes are extensive and cover many aspects of the operations of utilities in the ACT (noting that there are industry codes and the consumer protection code for customers of water and wastewater services - these codes are ultimately subject to the approval of the ICRC) (sections 55-56A);
- provide utility services in accordance with Government programs including community service obligations (section 219); and
- comply with street lighting and storming water obligations under Part 14 of the Act.

Further, the Act regulates:

- the rights of consumers with respect to utilities services and consumer contracts; and
- ACTEW's responsibilities with respect to operating and protecting a utilities network.

16. *Water and Sewerage Act 2000 (ACT)*

This Act regulates the supply of plumbing and drainage services in the ACT.

Again, ACTEW believes that relevant requirements could be incorporated into the Utilities Act.

17. *Water Resources Act 2007 (ACT)*

This Act provides for the sustainable management of the water resources of the Territory. In order for ACTEW to undertake its water and sewerage business, it must obtain a number of licences under the Act, including:



- a licence to take water;
- a driller's licence to do bore work;
- a bore work licence;
- a waterway licence; and
- a recharge licence.

ACTEW's water flow must also be approved by the Minister and be in accordance with the environmental flow guidelines in Part 3 of the Act and an application must be made to the Minister for water access entitlements.

As above, these requirements could all be incorporated into the Utilities Act.

10. Relationships with ACT Government

Summary:

- ***ACTEW is in a strategic partnership with the ACT Government to develop and deliver water policy.***
- ***ACTEW is directly accountable for its actions – it is accountable under legislation, under contract, under the ACTEW Constitution, to regulators, to the Legislative Assembly, and most importantly, to the community.***
- ***The current position of the ACT Government on the payment of ACTEW dividends and borrowings is unsustainable and will inhibit the growth and development of the corporation.***
- ***ACTEW does not believe that there is a question of prioritising commercial, social or environmental objectives – ACTEW needs to be a success in each area.***

10.1. Water Policy

ACTEW has been, and will continue to be, a critical stakeholder in enabling the ACT Government to achieve its water strategies. The previous water policy *Think water, act water* set out many targets and, from undertaking infrastructure works to the management of water conservation measures, ACTEW played a very important role in assisting the ACT Government achieve those targets.

ACTEW believes that a firm strategic partnership between the ACT Government and ACTEW is necessary to deliver the water policy objectives detailed in the draft water policy *Water for the Future – Striking the Balance*. ACTEW has a critical role in informing the ACT Government on policy and then assisting the ACT Government, where appropriate, in the implementation of that policy.

ACTEW also notes and agrees with the Hawke Report on the ACT Public Service, “Governing the City State - One ACT Government, One ACT Public Service, February 2011” which stated that water policy was actually a matter spread across a number of different ACT Departments (now Directorates). ACTEW believes it is important that strong relationships be maintained between ACTEW and each of these Directorates to ensure the continued delivery of water policy.

ACTEW does not have access to the business of Government, and more specifically is not generally consulted on the preparation of Cabinet Submissions in relation to water policy or other matters that have direct impacts on ACTEW. It does not have

the ability to formally input into key decisions on water. In the past, certain mechanisms have existed that gave due consideration to water policy issues, such as the Chief Executives Water Group. This forum was particularly active during the planning and early implementation phases of the Water Security Major Projects but has, over recent time, largely been in abeyance.

It is essential that ACTEW is integrally involved in the evolution and implementation of proposed action plans in relation to water policy. In particular, it will be essential to formally agree the financial implications of implementing agreed ACT Government policy with the ICRC so as to allow ACTEW to recover any expense incurred outside its normal business.

ACTEW is a proponent of NSW / ACT cross-border co-operation in water and sewerage matters. Such co-operation is capable of providing mutual benefit to Capital Region Councils, the ACT Government and ACTEW.

The vision for the Draft Strategy is to “support a vibrant, sustainable and thriving region.” This vision for the Capital Region will only be achieved where neighbouring regional councils have an opportunity to access the water and water and sewerage treatment resources of the ACT. To that end, ACTEW encourages a long-term water strategy which:

- recognises that regional water strategies will be most effective where there is ongoing cross-border dialogue between the ACT and neighbouring NSW local councils;
- foreshadows the potential sharing of corporate, engineering, environmental, scientific, IT systems, procurement, educational, risk management and other services across water and sewerage operations;
- facilitates the interconnection of ACT water and sewerage networks with corresponding networks in neighbouring NSW council areas; and
- provides for the supply of water from the ACT to neighbouring NSW councils.

10.2. Accountability

As previously set out in this submission, ACTEW is directly accountable to its shareholders and others under the Corporations Act, the TOC Act, the Utilities Act, its Constitution and other pieces of legislation. However, in addition to these fundamental accountability requirements, ACTEW:

- provides all ACTEW Board papers and a summary letter to each Voting Shareholder after each Board meeting;
- has consulted with the ACT Government on all major decisions regarding the Corporation - either as Voting Shareholders, as a requirement of the TOC Act or as a result of prudent management of ACTEW;
- notes that quarterly reports on ACTEW's Water Security Major Projects were sent to Voting Shareholders from 2008 through to late 2012;
- is required to produce over 60 compliance reports per annum, some due periodically, others as requested, under 9 separate pieces of legislation covering the operational side of the water business;
- is required to produce 37 compliance reports per annum specifically related to meeting approval conditions of the Water Security Major Projects;
- has been subject to a number of reviews or inquiries including:
 - in November 2009, the Attorney-General referred an investigation to the ICRC on the costs and related matters of the Enlarged Cotter Dam. The ICRC undertook a public process, including the engagement of engineering consultants Halcrow, to analyse the project. On 30 June 2010 the Commission released its final report, which endorsed the project costs and alliancing arrangements;
 - a governance review by PricewaterhouseCoopers, the outcome of which found that ACTEW's governance framework is consistent with key principles of effective governance;
 - various performance audits by the ACT Auditor-General; and
 - the recently announced audit of the Enlarged Cotter Dam by the ACT Auditor-General.

ACTEW does not believe that there can be any question of it not being accountable for its actions or decisions. ACTEW is accountable under legislation, under contract, under its Corporate Constitution, to regulators, to the Legislative Assembly, and most importantly, to the community.

10.3. Dividends and Borrowings

❖ Dividend policy

ACTEW and the ACT Government are continuing to consider the position on the ACT Government Dividend policy. Both ACTEW and the ACT Government have received advice that highlights the following:

- There are a number of factors which differentiate ACTEW's capital structure from other utilities. The most significant of these are the current dividend policy, borrowing through the ACT Government and the investment in the debt-free ActewAGL joint venture.
- The current ACT Government dividend policy of 100 per cent of net profit after tax being provided to its shareholders exceeds that of other water utilities in Australia.
- While this type of dividend policy may be appropriate for some businesses, or over a short term, it is not generally advisable as a long term position for utilities. ACTEW is a capital intensive business that experiences waves of major capital expenditure, the most recent being the \$600 million on the Water Security Major Projects. Financial flexibility is needed to meet expenditure, as required, for upgrades to major assets and for unforeseen situations like a severe drought. It also provides ACTEW with the opportunity to grow the business and invest in beneficial investment opportunities.
- A 100 per cent dividend policy does not offer any cash retention flexibility and, perhaps more importantly, requires all asset investments to be funded through borrowings, which has the effect of increasing the cost of those investments. It also puts both ACTEW, and the ACT Government, in a position where they are required to raise debt externally at times when it may not be advantageous to do so - for instance in periods of higher interest rates.

In addition to ACTEW's capital expenditure funding requirements, the capital expenditure of ActewAGL Distribution is currently funded through business cashflows. As such, there is a shortfall between the net profit after tax applicable to the ActewAGL Distribution Partnership and the cash which is distributed to ACTEW. As this profit flows through ACTEW to its shareholders, as does the shortfall in cash, ACTEW is further required to borrow funds to pay dividends.

The graph below details the impact on ACTEW's borrowing and gearing level with respect to the recent Water Security Major Projects. Gearing ($\text{debt}/(\text{debt} + \text{equity})$) demonstrates how a company's activities are funded between owners' equity and

borrowed funds. The level of gearing affects the riskiness of a business’s return to shareholders. The requirement to fund the \$600 million expenditure entirely from debt, as well as continue to fund dividend payments, has seen ACTEW’s gearing level double from 30 per cent to 60 per cent - this is the maximum gearing level that the ACTEW Board believes is acceptable for ACTEW. The drop in gearing level in 2007 was the result of a revaluation of ACTEW’s assets, which did not result in an improved cash position for ACTEW.

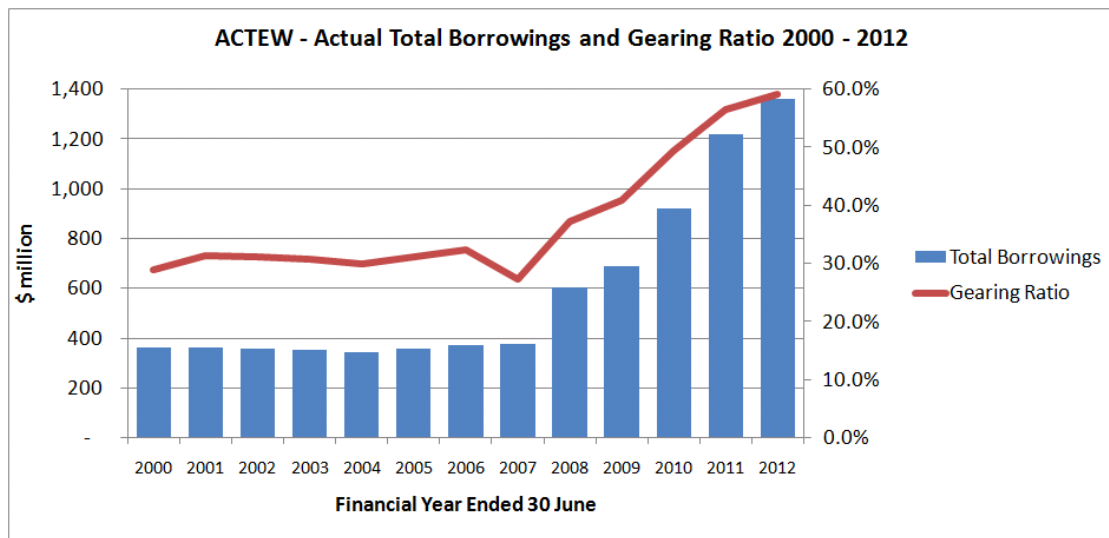


Figure 10. ACTEW total borrowings and gearing ratio 2000 - 2012

During the same period the level of interest expense has tripled and the interest coverage ratio (EBITDA/Interest Expense), which is the company's ability to meet its debt payments, has decreased to a ratio of 2.5 which is bottom of a BBB credit rating. This is highlighted by the figure below:

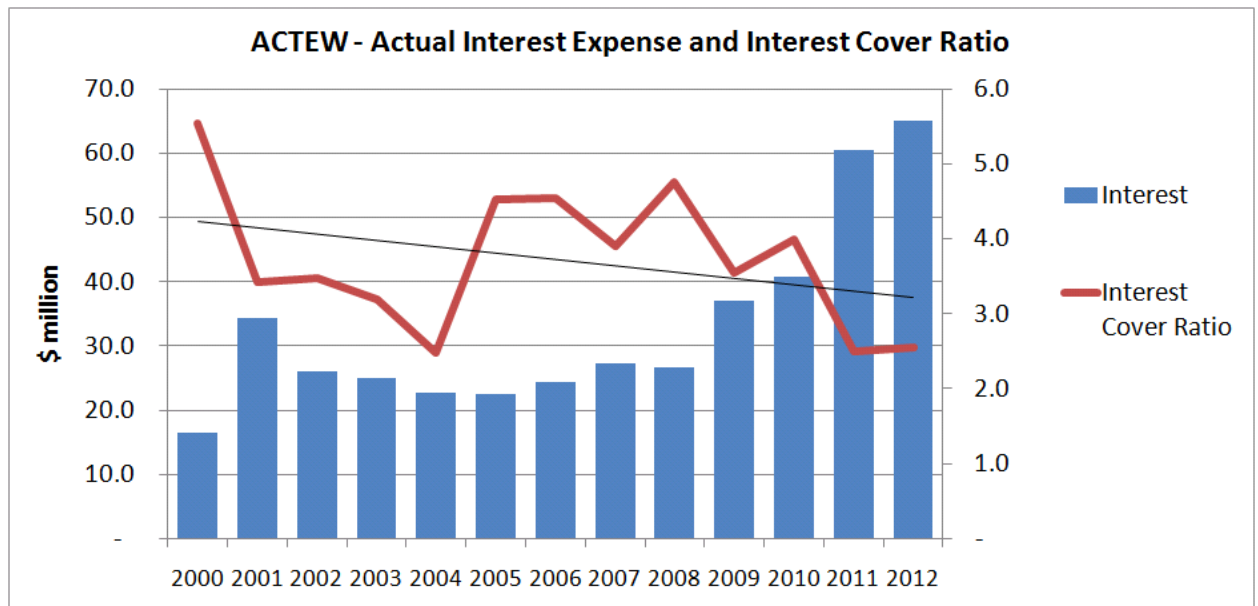


Figure 11. ACTEW actual interest expense and interest cover ratio 2000 - 2012

ACTEW also engaged Pacific Road to advise on a reasonable dividend policy, the outcomes of which were provided to the Voting Shareholders. Accordingly, ACTEW believes that a revised ~~the~~ dividend policy needs to take into account:

- operating cash in conjunction with maintenance capital expenditure and agreed capital structure requirements;
- the ability to repay debt funded growth capital expenditure;
- profit share vs. cash distribution from the ActewAGL joint venture, including ActewAGL's access to borrow funds; and
- the effect of gifted assets (non-cash assets contributed to ACTEW) to net profit after tax.

In any event, ACTEW submits that a change in dividend policy is necessary.

As detailed previously, the purpose of the incorporation of ACTEW was that it was to operate in a similar fashion to commercial businesses. To this end, it is preferable to have a dividend policy that more accurately reflects the returns to be paid to shareholders, while maintaining financial stability within the business and having less impact on the borrowing level and gearing ratio of the business.

The table below indicates the likely impacts on ACTEW's gearing level should the Directors of ACTEW not be given the ability to control the capital structure and should the current dividend arrangements continue.

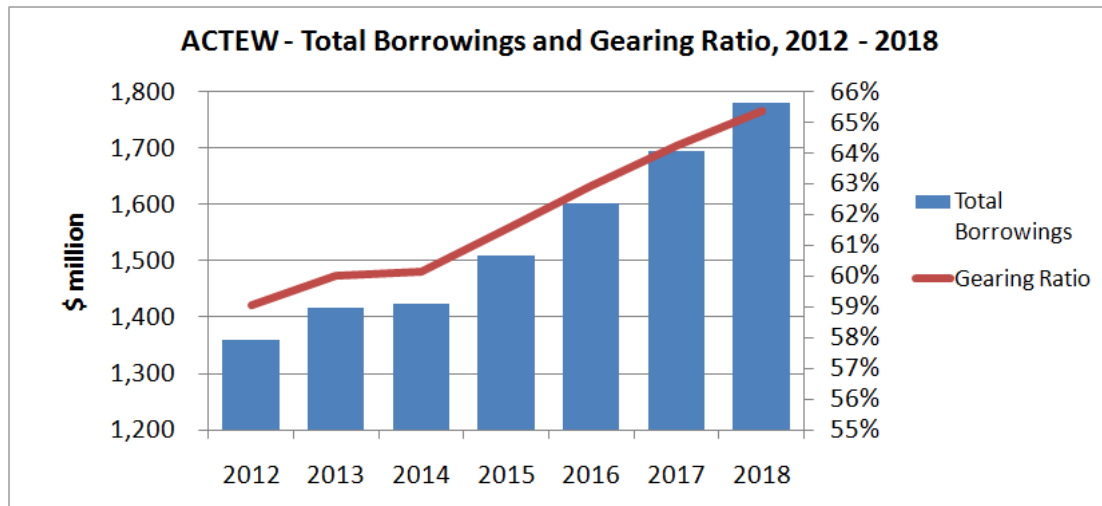


Figure 12. ACTEW forecast gearing ratio

The graph below details the dividend payout ratio (as a percentage of net profit after tax) of the other major water utilities in Australia. The variability of other utilities' dividend payouts indicates that all other major water utilities in Australia vary their dividend policy in accordance with cashflow requirements. Of particular note is the Sydney Water Corporation dividend payout ratio, which was significantly reduced in the 2009-10 year during construction of the desalination plant.

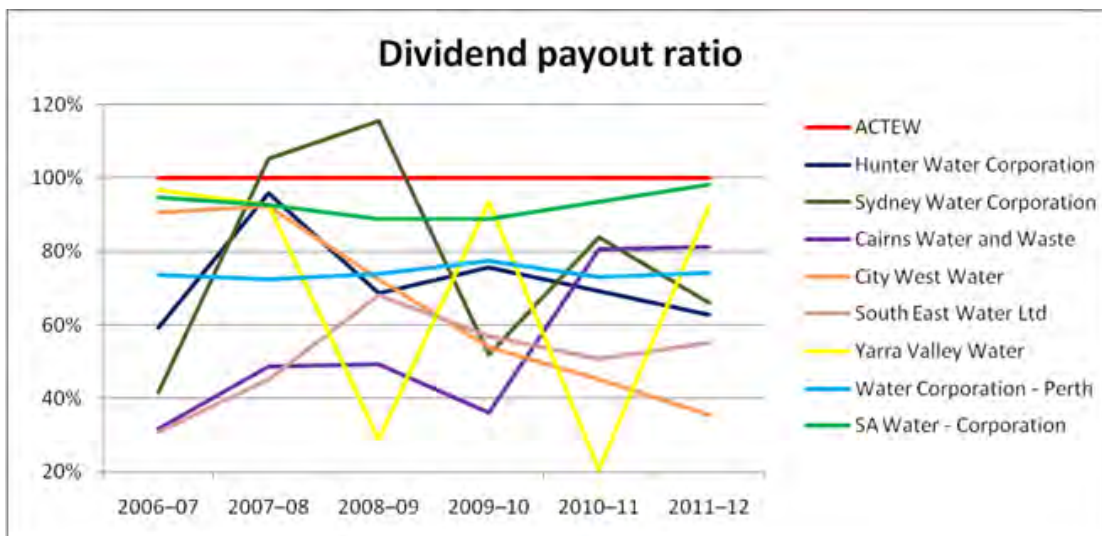


Figure 13. Dividend payout ratio

As a result of the current dividend policy, ACTEW now has the highest gearing ratio of any major water utility.

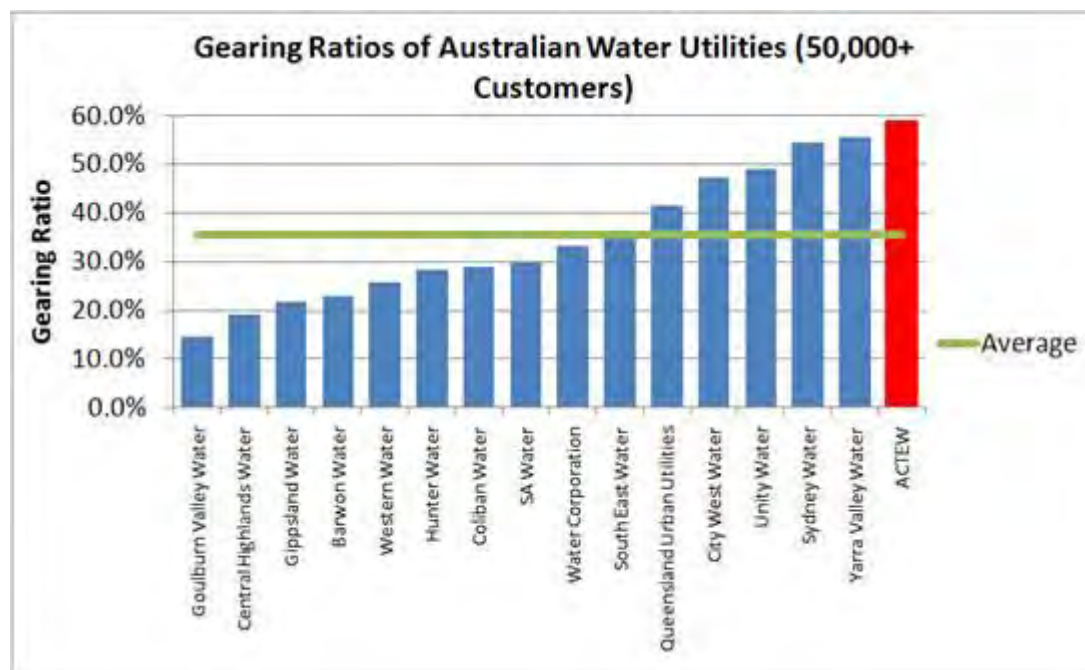


Figure 14. Australian water utility gearing ratios

❖ Borrowings

The major benefit to ACTEW of borrowing through the ACT Government is the applicable interest rate at which the borrowings are made. This allows ACTEW to obtain funding at a rate which may be more advantageous than if ACTEW was to borrow within the debt market. The utilisation of State and Territory Treasury borrowings is common within state and territory-owned corporations. For example, Sydney Water Corporation utilises the borrowings of NSW Treasury Corporation almost entirely.

However, the use of these rates by the ICRC in the calculation of the costs of the ACTEW business can hide the actual commercial cost that ACTEW would otherwise incur from the debt market. The concern is that if the ICRC is going to use these rates for the purposes of the pricing determination, there needs to be some undertaking or commitment that:

- the ACT Government would always allow ACTEW to borrow through it at the relevant rate for the term of the relevant pricing determination; and

- the ACT Government would not attempt to impose any premium that tried to reflect the commercial market for debt for the term of the relevant pricing determination,

unless there was also a review of the relevant pricing determination to allow for the pass through of any increased costs.

Currently, the ACT Government could charge a premium on the rates at which it borrows and the dividend policy is enforced by the Voting Shareholders on ACTEW whereby all profits are required to be delivered to the ACT Government. At this stage, the Directors of ACTEW are not in a position to determine the borrowings position of the business. It is, therefore, considered to be inadvisable within the Territory Government to have one agency determining the premium rate to apply to ACTEW's debt while the Voting Shareholders are making decisions directly affecting the level of debt required.

Furthermore, the TOC Act specifically requires Treasurer approval for ACTEW to raise debt, thereby restricting ACTEW's ability to borrow independently of the ACT Government.

10.4. Territory Decision Making

As stated before, despite the complexity of the ACTEW and ActewAGL model - both ACTEW and ActewAGL have been successful for the Canberra community and the ACT Government.

In this regard, it needs to be acknowledged that the Voting Shareholders have worked to recognise the corporate status and nature of ACTEW and its business and have provided the organisation with appropriate guidance and oversight without attempting to manage the business.

In this context, ACTEW accepts that it should be subject to oversight by its Voting Shareholders and other regulatory agencies, however ACTEW does not believe that there is a need for the ACT Government to be provided with an additional express right to review or change decisions made by the ACTEW Board.

The ACT Government has the power to intervene in, prevent, or vary ACTEW decisions within the context of ACTEW as a corporate entity.

In this regard, ACTEW notes the following:

- as previously stated, the Voting Shareholders have existing rights under the TOC Act, the Corporations Act and the ACTEW Constitution, all of which

provide the ACT Government of the day with a level transparency and oversight with respect to decisions made by ACTEW;

- given that ACTEW can only raise debt with the approval of the ACT Government (and indeed through the ACT Government), it is not practically possible for ACTEW to undertake any significant project without the consent of the ACT Government;
- the Voting Shareholders are provided with Board Papers and are advised of all significant matters;
- the ACT Government and the ACTEW Board both agree that it would be retrograde to return the business to a public authority - something that the ICRC itself noted was an unwarranted outcome and which may have consequences for the achievement of the goals of corporatisation as set out earlier in this submission;
- the technical expertise for the water business is within ACTEW and, given this, ACTEW should be able to make decisions regarding the water business, especially in circumstances where the ACT Government already has other existing rights of review and consent in relation to major and significant events; and
- any major projects will also require environmental and other approvals - all of which are managed by the ACT Government - providing another layer of oversight for ACTEW projects.

For completeness, the following highlights some key decisions that ACTEW may be required to take from time to time – as can be seen the Voting Shareholders and the Legislative Assembly have extensive rights to control decisions made by ACTEW, and to hold ACTEW accountable for decisions made:

Decision	Approval Required		
	ACTEW Board	Voting Shareholders	Legislative Assembly
Capital Expenditure	✓	✓	
		<ul style="list-style-type: none"> • Voting Shareholders can overturn or vary the relevant capital expenditure • Approval may be required under s16 	

Decision	Approval Required		
	ACTEW Board	Voting Shareholders	Legislative Assembly
		<p>of the TOC Act if the capital expenditure can be considered "a main undertaking"</p> <ul style="list-style-type: none"> In any event, in a practical sense ACTEW will need Voting Shareholder approval (including under the TOC Act) as it must borrow from the ACT Government to fund any capital expenditure Note also, notification would be given under s16A of the TOC Act 	
Day to day Operating Expenditure	✓		
Appoint or Remove Directors	Can informally advise Voting Shareholders on candidates for directorships	<p>✓</p> <p>Constitution (cl. 47) TOC Act (s 12)</p>	<p>TOC Act (s 12) Voting Shareholders must consult with the "Relevant Committee" nominated by the speaker of the Legislative Assembly on the appointment of Directors.</p>
Incorporate a subsidiary	✓	<p>✓</p> <p>Constitution (cl. 95) TOC Act (ss 13, 16)</p>	<p>TOC Act (s 16) Portfolio Minister must inform Legislative Assembly of the matter if consent is given.</p>
Acquire a subsidiary	✓	<p>✓</p> <p>Constitution (cl. 95, 97) TOC Act (s 16)</p>	<p>TOC Act (s 16) Portfolio Minister must inform Legislative Assembly of the matter if consent is given.</p>

Decision	Approval Required		
	ACTEW Board	Voting Shareholders	Legislative Assembly
Dispose of subsidiary	✓	✓ Constitution (cl. 97) TOC Act (s 16)	✓ TOC Act (s 16) Facilitation Act (s 27) Latter applies if subsidiary is an ActewAGL partner
Change company name	✓	Approval not required but must inform Voting Shareholders of significant events (s16A, TOC Act)	
Sale of business	✓	✓ TOC Act (s 16) On the assumption the business is a "main undertaking"	✓ TOC Act (s 16) On the assumption the business is a "main undertaking"
Acquire a major asset	✓	✓ TOC Act (s 16) On the assumption that a major asset may become or is a "main undertaking".	TOC Act (s 16) Portfolio Minister must inform Legislative Assembly of the matter if consent is given.
Enter into a commercial contract	ACTEW Management decision – unless this exceeds delegations, in which case Board approval may be required		
Enter into major commercial contract	✓	✓ TOC Act (s 16) On the assumption that a major commercial contract may become a "main undertaking".	Portfolio Minister must inform Legislative Assembly of the matter if consent is given.
Terminate an employee	ACTEW Management decision		
Change of management structure	✓		
Give security over an asset	ACTEW Management decision		

Decision	Approval Required		
	ACTEW Board	Voting Shareholders	Legislative Assembly
Give security over a major asset or significant part of its assets	✓	✓ TOC Act (s 16)	

10.5. Prioritisation of Commercial, Social and Environmental Objectives

ACTEW notes that one of the areas within the scope of this review is to examine, and provide recommendations on, potential approaches which could enhance the process of setting specific goals and objectives for ACTEW, including the potential prioritisation of commercial, social and environmental objectives.

As noted throughout this submission, ACTEW is a corporate commercial entity and is required to make a reasonable turnover and operating profit to provide for:

- the funding of its operations;
- delivery of services to the ACT community;
- meeting its debt obligations, where such debt was primarily incurred to fund capital expenditure projects, and was in part necessary given the ACT dividend policy; and
- returns to the ACT Government in the form of dividends.

However:

- ACTEW's operations and business are intimately affected by the environment - ACTEW cannot ignore environmental issues, it has to be an active participant in the consideration and management of certain environmental concerns and issues. For example, the construction of the Enlarged Cotter Dam was undertaken directly as a result of the severe drought that affected Canberra and the surrounding region from 2000 to 2010; ACTEW's operations have been reviewed in order to reach the greenhouse gas emissions set by the ACT Government, and will be indirectly affected as the result of a price on carbon. ACTEW also considers that, as a large utility provider in the region, it should be a leader in the areas of environmental awareness and implementing sustainable practices; and



- As a utility provider, ACTEW provides essential services to the community. The manner in which it provides these services and the business decisions it makes can and do have a profound social impact on the community in which it operates. ACTEW considers that it has a responsibility to the community in how it acts in relation to both its core business and its involvement in community support activities.

In short, ACTEW does not believe that it is a question as to whether a prioritisation of its commercial, social and environmental objectives is required - the simple fact is that, if we fail in any one of those areas, we have failed as an organisation.

It is for this reason that ACTEW has through its Statement of Corporate Intent, through its governance, and through its liaison with the community and the Voting Shareholders, ensured that commercial, social and environmental objectives are given equal weight and attention given their importance to the success or failure of ACTEW.