Australian Government
Productivity Commission

Financial Performance of Government Trading Enterprises 1999-00 to 2003-04

Productivity Commission Research Paper

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Foreword

This report into the financial performance of government trading enterprises (GTEs) continues previous work by the Commission and an earlier series of broader 'Red Book' reports of the Steering Committee on National Performance Monitoring of Government Trading Enterprises.

There has been a pronounced improvement in the financial performance of GTEs since the early 1980s, primarily attributable to National Competition Policy (NCP) and related governance reforms. Nevertheless, despite some improvement in overall profitability, in 2003-04 over half of the monitored GTEs recorded rates of return below the risk-free government bond rate. This unsatisfactory outcome is difficult to reconcile with government agreements to operate GTEs on a fully commercial basis — a key plank of the GTE governance model.

GTE external governance arrangements presented in this report exhibit various deficiencies. These can have potentially serious consequences, given the value of public assets under these arrangements. As noted in the Commission's recent Review of NCP Reforms, if such businesses are to remain in public ownership, there would be considerable benefits from further governance reform and performance improvement. With current concerns about the adequacy of infrastructure, and the need for further reform identified in the NCP Inquiry, the Commission proposes to continue monitoring the performance of GTEs.

This study was undertaken in the Economic Infrastructure Branch under the guidance of Commissioners Michael Woods and Tony Hinton. The Commission is grateful for the continuing cooperation of State and Territory Governments. Input from a range of individuals and organisations on external governance issues has also been valuable.

Gary Banks
Chairman

July 2005

Contents

Part B

Abbreviations and explanations

Abbreviations

AAS	Australian Accounting Standard
AASB	Australian Accounting Standards Board
ABARE	Australian Bureau of Agricultural and Resource Economics
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ACTEW	ACTEW Corporation Ltd
ACTION	Australian Capital Territory Internal Omnibus Network Authority
AEPU	Agreement Equally Proportionally Underperformed
AGS	Auditing Guidance Statements
AIE	Australian Inland Energy
AIEWI	Australian Inland Energy and Water Infrastructure
ANAO	Australian National Audit Office
ANRC	Australian National Railways Commission
APA	Albany Port Authority
ARA	Australasian Reporting Awards
ARG	Australian Railroad Group
ARIF	Australian Rail Infrastructure Foundation
ARTC	Australian Railtrack Corporation

ASA	Airservices Australia
BACL	Brisbane Airport Corporation Limited
BCC	Brisbane City Council
BPA	Benchmark Pricing Agreement
BPC	Burnie Port Corporation
CCW	Cradle Coast Water
CHW	Central Highlands Water Authority
CoAG	Council of Australian Governments
CPA	Competition Principles Agreement
CPI	Consumer Price Index
CSO	Community Service Obligation
CWW	City West Water
DBCT	Dalrymple Bay Coal Terminal
DDSO	Digital Data Service Obligation
DPA	Dampier Port Authority
DPC	Darwin Port Corporation
EBIT	Earning Before Interest and Tax
EDI	Electronic Data Interchange
ESC	Essential Services Commission
ESC Act	*Energy Services Corporations Act 1995*
ETEF	Electricity Tariff Equalisation Fund
ETF	Economic Type Framework
FPA	Fremantle Port Authority

FPCWA	Forest Products Commission of Western Australia
GBE	Government Business Enterprise
GCCC	Gold Coast City Council
GFS	Government Financial Statistics
GMW	Golburn–Murray Rural Water Authority
GOC	Government Owned Corporation
GPA	Gladstone Port Authority
GPFR	General Purpose Financial Reports
GPOC	Government Prices Oversight Commission
GTE	Government Trading Enterprise
GVW	Golburn Valley Regional Water Authority
GWh	Giga (10^9) watt hours
HEC	Hydro-Electric Corporation
HIA	Hobart International Airport Pty Ltd
HPC	Hobart Ports Corporation
HWC	Hunter Water Corporation
ICAA	Institute of Chartered Accountants in Australia
ICRC	Independent Competition and Regulatory Commission
IPART	Independent Pricing and Regulatory Tribunal
KPI	Key Performance Indicator
kWh	Kilo (10^3) watt hours
MPA	Mackay Port Authority
MPC	Melbourne Port Corporation

MW	Mega (10^6) watts
MWC	Melbourne Water Corporation
MWh	Mega (10^6) watt hours
NCC	National Competition Council
NCP	National Competition Policy
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company
NFPS	National Forestry Policy Statement
NPC	Newcastle Port Corporation
NRC	National Rail Corporation
NTER	National Tax Equivalent Regime
NWWA	North West Water Authority
OPT	Office of Public Transport
ORG	Office of the Regulator-General
OTER	Office of the Tasmanian Energy Regulator
PAWC	Power and Water Corporation
PBC	Port of Brisbane Corporation
PCQ	Ports Corporation of Queensland
PDC	Port of Devonport Corporation
PEP	Port Enhancement Project
PHPA	Port Hedland Port Authority
PKCTL	Port Kembla Coal Terminal Limited
PKPC	Port Kembla Port Corporation

PoMC	Port of Melbourne Corporation
PPA	Power–Purchase Agreement
PTA	Public Transport Authority
PTB	Passenger Transport Board
PTE	Public Trading Enterprise
QNI	Queensland–New South Wales Interconnector
QPTC	Queensland Power and Trading Corporation
QR	Queensland Rail
QTSC	Queensland Transmission and Supply Corporation
RBA	Reserve Bank of Australia
RFA	Regional Forest Agreement
RIC	Rail Infrastructure Corporation
SA Water	SA Water Corporation
SCA	Sydney Catchment Authority
SCI	Statement of Corporate Intent
SEW	South East Water
SFNSW	State Forests of New South Wales
SGARA	Self-generating and Regenerating Assets
SHTPL	Snowy Hydro Trading Pty Ltd
SMHEA	Snowy Mountains Hydro-Electric Authority
SOC	State Owned Corporation
SOC Act	*State Owned Corporations Act 1989*
SOE	State Owned Enterprise

SPC	Sydney Ports Corporation
SPS	Sydney Pilot Service Pty Ltd
SRA	State Rail Authority
STA	State Transit Authority
SVA	Shareholder Value Added
SWC	Sydney Water Corporation
TOC	Territory Owned Corporation
TPA	Townsville Port Authority
USO	Universal Service Obligation
VCA	Victorian Channels Authority
VRCA	Victorian Regional Channels Authority
WACC	Weighted Average Cost of Capital
WAGRC	Western Australian Government Railways Commission
WMW	Wimmera Mallee Rural Water Authority
YVW	Yarra Valley Water

PART A

Key points

- Government trading enterprises (GTEs) provide services in key sectors of the economy — including electricity, water, urban transport, railways, ports and forestry. In 2003-04, the 83 GTEs monitored in this report controlled assets valued at more than $174 billion and generated $55 billion in revenue.
- Aggregate profitability increased in all sectors, other than rail and forestry, in 2003-04 compared with the previous year.
- Over a longer period, the profitability of the 50 GTEs (excluding Telstra) monitored continuously since 1999-00 did not improve, with the aggregate return on assets falling slightly from 6.8 per cent to 6.7 per cent.
- The aggregate debt to assets ratio rose from 26 per cent in 1999-00 to 29 per cent in 2003-04 for this group.
- Nearly half of the 83 currently monitored GTEs earned less than the long-term bond rate in 2003-04. An even greater number failed to earn a commercial rate of return (which includes a margin for risk).
- In total, currently monitored GTEs made tax-equivalent and dividend payments to their owner-governments of almost $7.9 billion in 2003-04.
- There are some deficiencies in the governance arrangements for GTEs. Given the economic significance of the GTE sector, improvements in governance could yield significant benefits to the community and reduce the need for GTE specific regulation. These improvements should include:
  - clarification and public scrutiny of the rationale for ongoing government ownership of GTEs;
  - greater clarification and transparency of objectives (both commercial and other public interest), together with their prioritisation or weighting; and
  - making a clearer distinction between external and internal governance, with improved transparency of the external governance role of ministers.

1 Introduction

This is the third report in the current three-year work program monitoring the financial performance of government trading enterprises (GTEs) and reporting on the arrangements for their external governance. This continues the work undertaken by the Productivity Commission's predecessor — the Industry Commission — for the Council of Australian Governments. The approach has been to update the data annually and to analyse the factors affecting financial performance over the preceding five years.

Financial performance monitoring of GTEs forms part of the Commission's research into the performance of Australian industries and the progress of microeconomic reform. Performance monitoring, with increased transparency, strengthens accountability. It also facilitates 'yardstick' competition — based on a comparable set of performance indicators — which is particularly important in industries where businesses do not face vigorous competition.

The information presented in this report is suitable for making a general assessment of financial performance within and across sectors. It does not provide information suitable for a detailed analysis of the performance of individual GTEs — a thorough examination of their financial statements is required for that purpose.

1.1 Scope

GTEs are government-owned or government-controlled entities that are mainly engaged in the production of goods and services, with the requirement to substantially or fully cover their costs. They are outside the general government sector and are also separate from government financial enterprises (in the banking, insurance and related sectors). GTEs are also commonly referred to as:

- GBEs (government business enterprises);
- GOCs (government-owned corporations);
- PTEs (public trading enterprises);
- Public corporations;
- SOCs (state-owned corporations);

- SOEs (state-owned enterprises); or
- TOCs (territory-owned corporations).

These terms are often used interchangeably. In some cases, the terms have specific local and statutory relevance. For example, the term GBE, when used in Tasmania, refers to specific entities in schedule 1 of the *Government Business Enterprises Act 1995* (Tasmania), including Forestry Tasmania and the Hydro-Electric Corporation.

This report contains a consistent set of financial performance indicators for 83 such entities — referred to generically as GTEs — for the period 1999-00 to 2003-04. In 2003-04, the GTEs monitored in this report (listed in appendix A) generated $55 billion in revenue and controlled assets valued at $174 billion. In aggregate, they account for around 85 per cent of the revenue generated by all government-owned businesses in Australia (ABS 2004d).

The monitored GTEs undertake a range of activities across six main sectors — electricity; water, sewerage, drainage and irrigation (hereafter referred to as 'water'); urban transport; railways; ports; and forestry. Three Australian Government trading enterprises that do not fit within these sectors — Australia Post, Airservices Australia and Telstra — are grouped together.

The size of the GTEs varies substantially across and within sectors (see figure 1.1). In 2003-04, the smallest in terms of asset value was the Albany Port Authority ($39 million) and the largest was Telstra ($35 billion).[1] Telstra accounted for 20 per cent of the total assets of the 83 monitored GTEs and the largest seven GTEs accounted for around 51 per cent of total assets.

The GTEs monitored represent the majority, but not all, of the GTEs currently operating in their respective sectors. Where GTEs operated over part of the reporting period (but not in 2003-04), they have not been included despite being monitored in previous years. These GTEs have generally been privatised or had their assets and operations transferred to other GTEs or new entities.

1.2 External governance

The findings of a three year research program into external governance are presented in this report (chapter 4). This work was commenced after external governance issues were identified in earlier reports as a possible factor affecting the slow progress in achieving governmental reform objectives (PC 2002a).

[1] Telstra is partly privatised. The Australian Government retains 50.1 per cent of issued shares.

External governance refers to the control and accountability arrangements between the enterprise and ministers (and government agencies) acting on behalf of the community. External governance is distinct from internal governance, which covers the systems of direction and control within an organisation that are the responsibility of the governing body and senior management of the organisation.

The first tranche of the research program focussed on the institutional arrangements and control mechanisms and was reported two years ago (PC 2003). The second, on accountability arrangements (auditing, reporting and performance measurement), was reported last year (PC 2004).

A workshop held in September 2003 helped guide the Commission's work. A second workshop was held in March 2005 to obtain feedback on a Discussion Draft of the Commission's findings. This workshop, like the first, was attended by some GTE board members and CEOs, academics and Australian and State Government officials. The comments received on the Discussion Draft and subsequently in submissions broadly supported the Commission's analysis and findings.

The Commission's findings report on the sustainability of the current corporatisation model in terms of performance, competitive neutrality and accountability. The implications of price and service regulation are also discussed.

1.3 Report structure

Chapter 2 provides an overview of the financial performance of the monitored GTEs over the last five years. A summary of the data and financial performance indicators used in the report are then presented in chapter 3. The findings of the research into external governance, as described above, are presented in chapter 4.

In part B, GTE performance reports are presented on a sector basis, with commentary on the influence of structural reforms and the market environment on performance. The Australian Government trading enterprises are reported separately.

State and Territory Treasury Departments were given the opportunity to review the GTE performance reports.

Figure 1.1 **Assets — monitored GTEs by sector, June 2004**

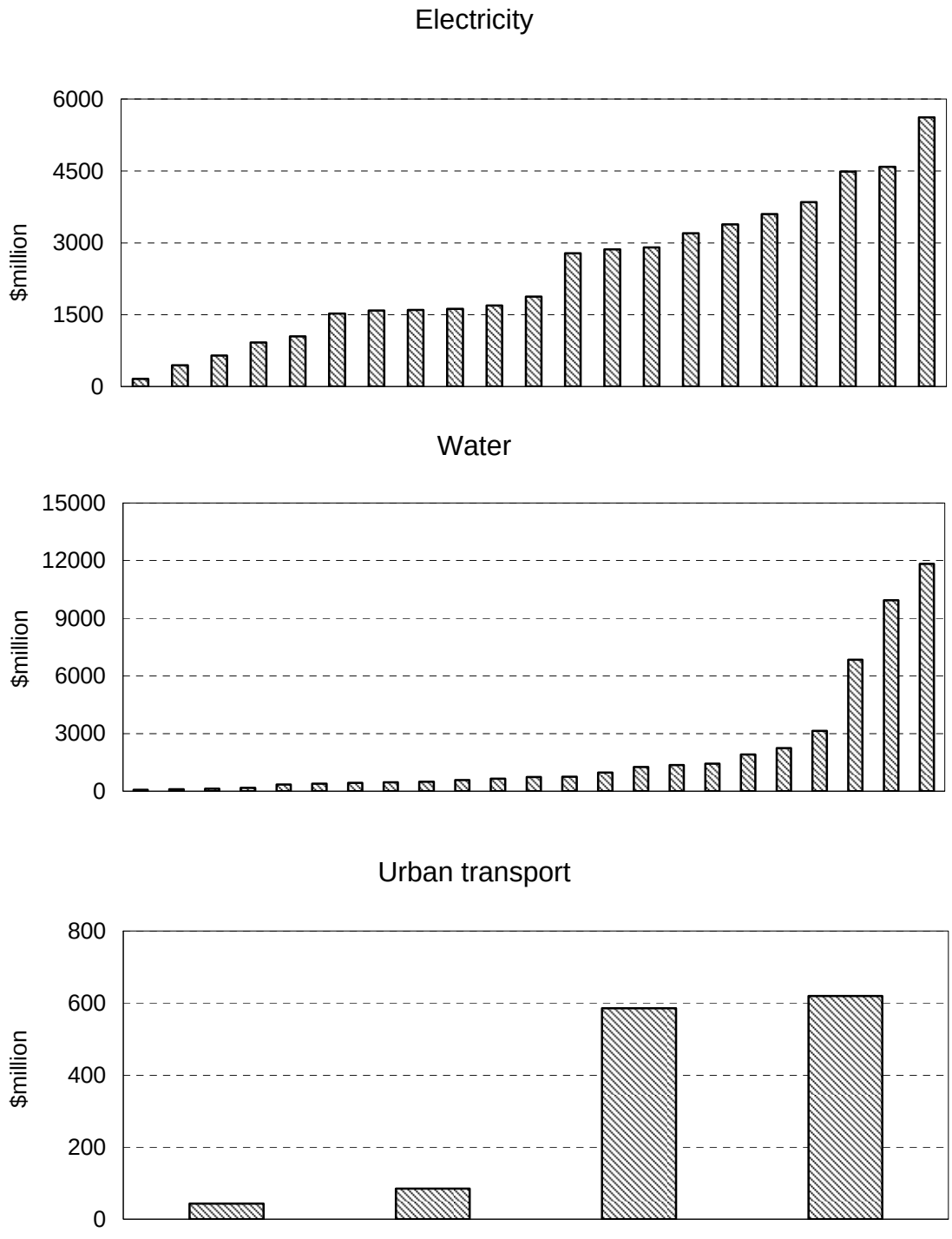

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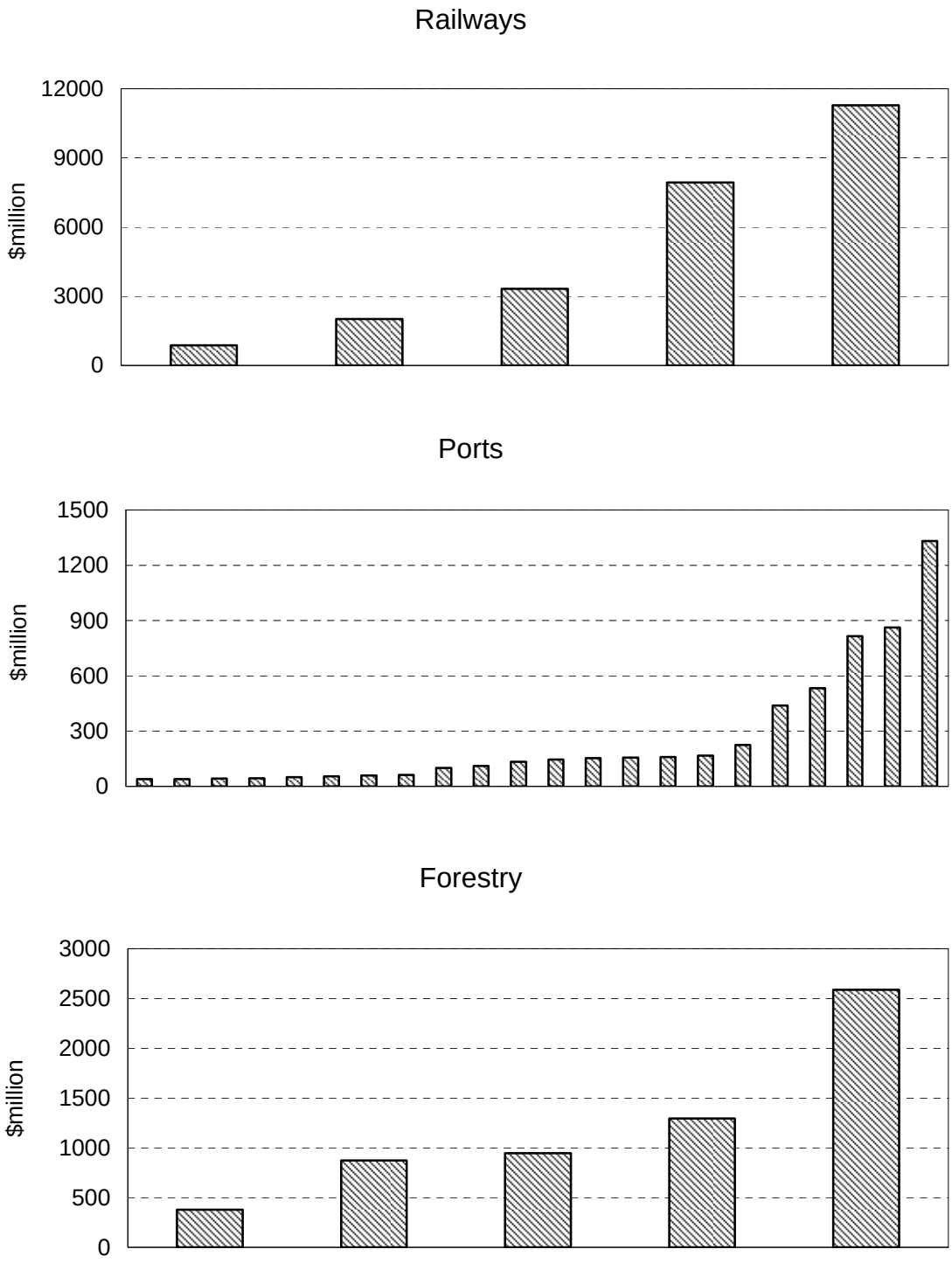
Figure 1.1 (continued)



Note Three Australian Government trading enterprises that do not fit within these six sectors — Australia Post (assets $3.5 billion), Airservices Australia ($545 million) and Telstra ($35 billion) — are grouped together and are excluded from this figure.

Source: Productivity Commission estimates.

2 Financial performance overview

In this chapter, an overview of government trading enterprise (GTE) performance is presented for the six industry sectors. The financial performances of each of the 83 GTEs over the period 1999-00 to 2003-04 are reported in part B of this report. Their financial performances were examined using a consistent set of financial indicators and ratios. Information on the data and measures used in assessing performance — both at a sector level and for individual GTEs — are presented in chapter 3.

2.1 Profitability

Profitability reflects a business's capacity to generate earnings from the capital invested in its activities. Increases in the retained profits (or surpluses) add value to an owner's equity in that company. If equity holders (the community) are to obtain a full financial return on their investment in GTEs, profits need to be sufficient to generate a return similar to that available from alternative investments with similar risk profiles.

In this report, the profitability measures include the level of operating profit, the return on assets (and equity), and the cost recovery ratio. For more information on these and other performance indicators used throughout the report, see chapter 3.

A full financial return would equate at least to the risk-free return on capital plus a margin reflecting the non-diversifiable market risk inherent in the investment. The 10-year Australian Government bond rate is widely used as the risk-free return benchmark.

The average rate of return on 10-year Australian Government bonds in 2003-04 was 5.7 per cent (RBA 2005).[1] In 2003-04, 45 per cent (37) of monitored GTEs were earning nominal pre-tax returns above this level. In comparison, 50 per cent of GTEs monitored in 2002-03 achieved a return greater than the long-term bond rate (5.4 per cent). At the start of the reporting period (1999-00), 50 per cent of the 51 GTEs which have been monitored

1 Based on the average daily rate over the 12 months to June 2004. The rate is usually based on the average bond rate over a specified period rather than an 'on the day' rate in order to minimise the effect of short-term volatility.

over the full reporting period also earned a rate of return above that year's long-term bond rate.[2]

Over the reporting period, several GTEs earned negative returns on assets and equity — notably in the urban transport and rail sectors (chapters 7 and 8). In 2003-04, 11 per cent of all monitored GTEs reported a pre-tax operating loss, a similar proportion to that observed in previous years.

Given the non-diversifiable risk inherent in any business activity, it is reasonable to expect that almost all GTEs should be generating returns above the risk-free rate.[3]

In 2003-04, the overall financial performance of the electricity, ports, water and urban transport sectors improved, while the results for the forestry and rail sectors were lower overall than for the previous year (see table 2.1).

Table 2.1 **Selected profitability measures, by sector in 2003-04 (2002-03)**

Sector	*Return on assets*		*Return on equity*		*Cost recovery*	
	per cent		per cent		per cent	
Electricity	7.8	(7.0)	7.9	(6.6)	126.3	(123.3)
Water	4.8	(4.6)	3.5	(3.1)	160.4	(157.7)
Urban transport	0.7	(0.1)	- 1.0	(-2.5)	99.5	(98.6)
Railways	- 10.5	(1.4)	- 21.3	(- 0.1)	37.6	(90.4)
Ports	7.2	(4.8)	5.9	(3.1)	156.0	(131.4)
Forestry	1.8	(7.0)	1.1	(6.8)	115.3	(154.9)

Note Indicators are the sector-wide weighted means. Results for 2002-03 are shown in brackets.

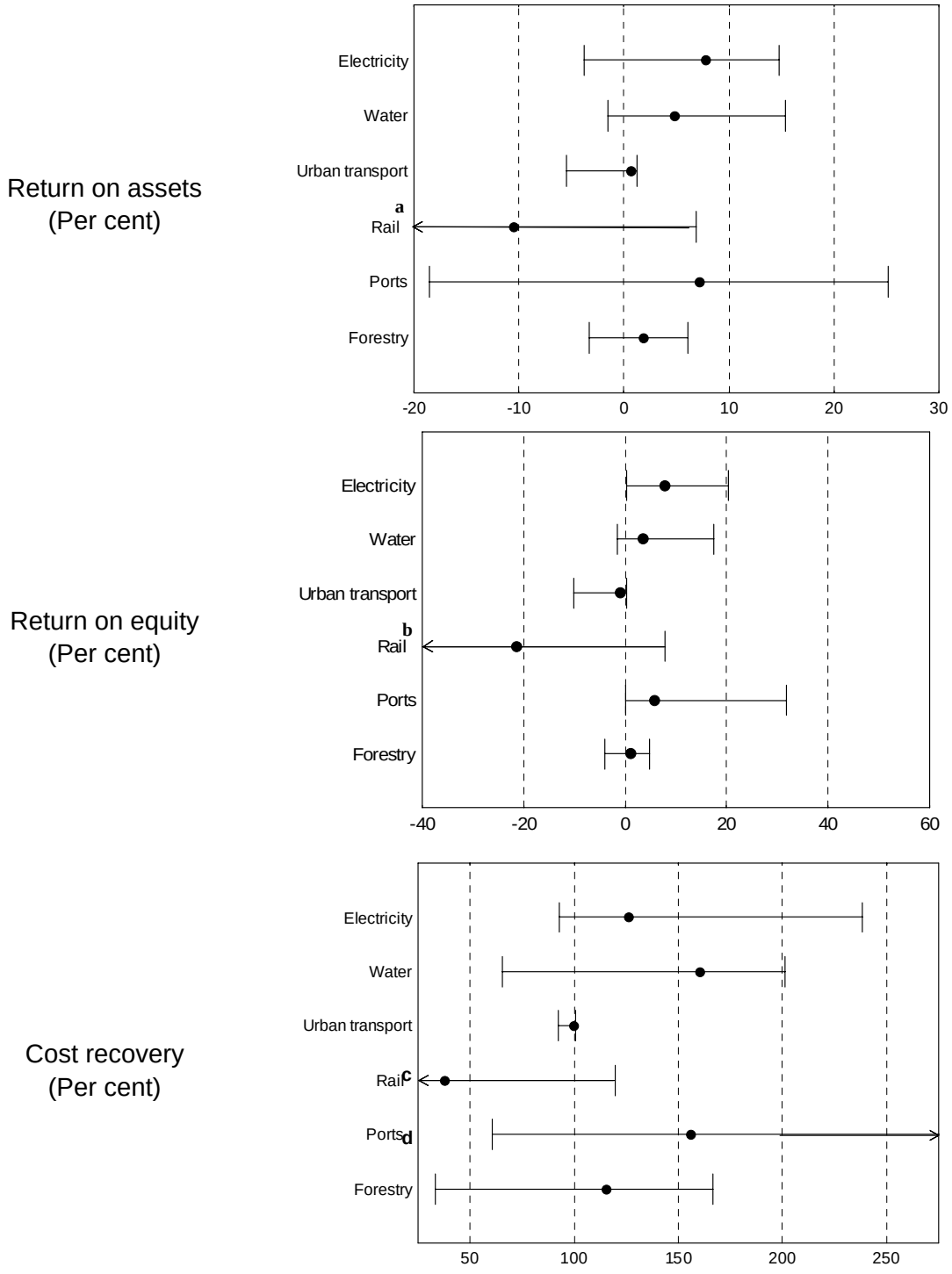
Source: Productivity Commission estimates.

Profitability varied considerably among and within each sector in 2003-04 (see figure 2.1).

2 The proportion of GTEs achieving a rate of return above the risk-free rate in 1999-00 relates to only those GTEs monitored for the entire reporting period. This can lead to problems in comparison with more recent years because of differences in the set of GTEs included. For example, eight rural water GTEs were included for the first time in 2001-02, of which none recorded a return above the risk-free rate in 2003-04. Of the GTEs included for the entire reporting period, 52 per cent (28) achieved a rate of return above the risk-free rate in 2003-04.

3 Typical values estimated by regulators as an approximate overall rate of return (including an allowance for non-diversifiable risk) are somewhat higher than the risk-free rate. For example, regulators accepted a nominal post-tax return of between 6 per cent and 7 per cent for electricity distributors in New South Wales over the period February 2004 to June 2008 (IPART 2004b) and nominal pre-tax returns of between 8.2 per cent and 10.8 per cent for the NSW rail access business (IPART 1999a).

Figure 2.1 **Selected profitability measures, by sector in 2003-04**



Note The dot represents the weighted mean value and the 'whiskers' represent the range of values for a given performance indicator. For example, the lowest return on assets in the electricity sector was -4 per cent, the highest value was 15 per cent and the weighted mean return on assets was 8 per cent. **a** The lowest return on assets for the rail sector was -44 per cent **b** The lowest return on equity for the rail sector was -50 per cent. **c** The lowest cost recovery ratio for the rail sector was -119 per cent. **d** The highest cost recovery ratio for the ports sector was 319 per cent.

Source: Productivity Commission estimates.

The financial performance of GTEs — relative to that in previous periods and to the performance of other GTEs operating in different parts of the economy — will be affected by variations in operating conditions. Such changes in conditions can include variations in the demand for a GTE's goods and services and changes to its costs of production.

The existence of non-commercial objectives may also affect the financial performance of GTEs. The emphasis that governments place on non-commercial objectives should therefore be considered when comparing the performance of GTEs across sectors and over time. If a GTE is directed to undertake non-commercial activities without adequate funding, its financial performance will suffer — especially in sectors where community service obligation (CSO) payments contribute a significant proportion of total revenue.

The GTEs monitored in this report generally operate in regulated industries, where prices are largely determined by independent price regulators or require ministerial approval. The influence of regulators' decisions on revenue means that their decisions can affect the profitability of GTEs. For example, in some cases, poor operating results may reflect regulated prices being set too low, rather than being indicative of poor management by the GTEs themselves.

The valuation of assets, and their periodic revaluation, can also affect the recorded financial performance of GTEs. For example, forestry GTEs are affected annually by revaluations of growing timber assets, the effect of which is written directly into the statement of financial performance (see chapter 10).

In addition, if a regulator, when determining the prices a GTE can charge for its services, assigns a different value to the assets than the value carried in the GTE's statement of financial position, measured financial performance will be affected. The Commission has also found, in some cases, differences between the asset valuation implicit in the regulator's final price determination and the regulator's stated asset valuation (PC 2002b).

Changes in GTE performance 1999-00 to 2003-04

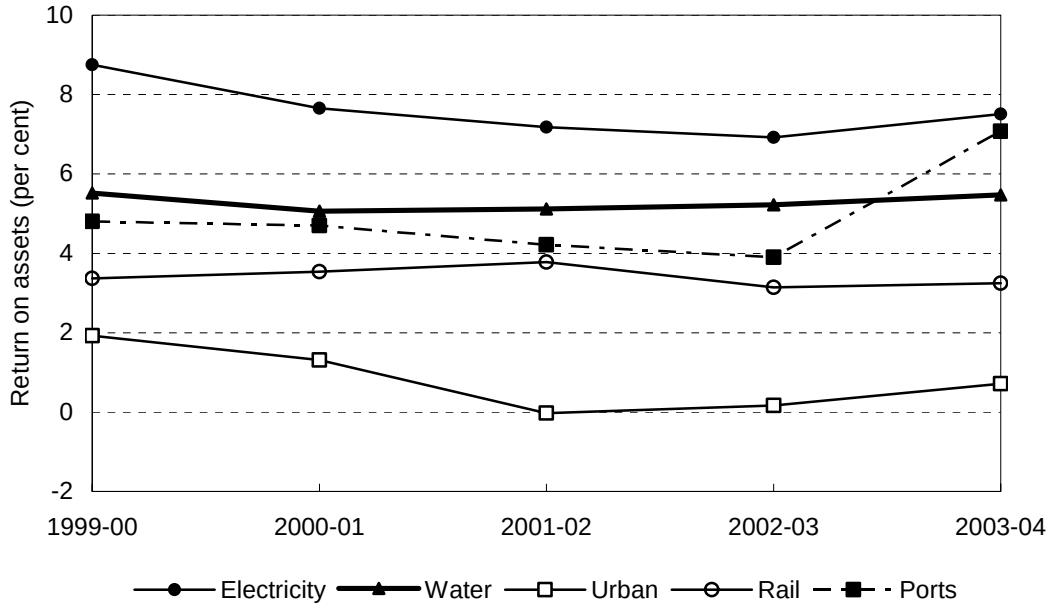
Fifty-one GTEs have been monitored over the entire five-year period from 1999-00 to 2003-04. Aggregate profitability of these GTEs — measured by the weighted average return on assets — fell from 10.3 per cent to 9.9 per cent between 1999-00 and 2003-04. However, this overall decline was largely due to a decrease in Telstra's profitability.[4]

4 Telstra's return on assets fell from 20.6 per cent in 1999-00 to 18.7 per cent in 2003-04. Telstra accounted for almost 27 per cent of the total assets of monitored GTEs in 2003-04.

The return on assets for all GTEs monitored over the entire reporting period, *excluding* Telstra, was much the same in 2003-04 (6.7 per cent) as at the start of the reporting period (6.8 per cent).

The aggregate profitability increased marginally in all sectors in 2003-04, compared with the previous year, with the exception of ports, which experienced a significant increase. However, over the reporting period, profitability fell in all sectors other than the port sector (see figure 2.2).[5]

Figure 2.2 **Profitability of GTEs, by sector**



Note Return on assets is the sector-wide weighted mean of GTEs monitored for the entire reporting period, from 1999-00 to 2003-04. Forestry GTEs were only monitored from 2001-02 and therefore are not included in this graph.

Source: Productivity Commission estimates.

The electricity sector had the strongest returns of all the monitored GTE sectors. The weighted average return on assets in 2003-04 for the subset of electricity GTEs monitored over the entire reporting period was 7.5 per cent, down from 8.8 per cent in 1999-00.

5 GTEs in the forestry sector were only monitored from 2001-02. This sector recorded an deterioration in profitability in 2003-04 (see table 2.1).

2.2 Financial management

The financial management indicators in this report include the ratio of debt to assets (and debt to equity), the current ratio and the level of interest cover. For more information on these and other performance indicators used throughout the report, see chapter 3.

The average debt level of the GTEs monitored since 1999-00 increased by 22 per cent in real terms over the five-year monitoring period. Approximately half of this increase was in the electricity sector, around a third was from Telstra and a further 20 per cent was in the water sector. Much of the $3.6 billion increase in debt in the electricity sector was due to restructuring and equity withdrawals, mostly from New South Wales and Queensland GTEs. The increase in debt in the water sector was incurred mainly by a small number of the larger water GTEs.

The increase in debt led to corresponding increases in the ratios of debt to assets and debt to equity. For the GTEs monitored since 1999-00 (50, excluding Telstra), the aggregate debt to assets ratio increased from 26 per cent in 1999-00 to 29 per cent in 2003-04.

Despite an overall increase in debt, more than 40 per cent of the GTEs monitored since 1999-00 decreased their nominal debt level over this period. This decline was attributable to a number of factors, including debt reduction programs, debt for equity swaps with shareholder governments, reduced capital expenditure and the partial privatisation of some businesses.

Debt to equity ratios varied considerably among sectors, ranging from 6 per cent in the forestry sector to 84 per cent in the electricity sector. In 2003-04, 12 GTEs — mainly in the ports and water sectors — operated debt free.

Interest cover varied significantly across sectors in 2003-04. In the forestry sector, the weighted average interest cover was 9.3 times. This contrasts with the urban transport sector, where interest cover was only 0.5 times and the rail sector, where interest cover was negative (see table 2.2).

Table 2.2 **Selected financial performance measures, by sector in 2003-04 (2002-03)**

Sector	*Debt to equity*		*Current ratio*		*Interest cover*	
	per cent		per cent		times	
Electricity	83.8	(93.3)	71.4	(71.7)	3.0	(2.6)
Water	23.0	(20.6)	55.4	(61.8)	4.7	(4.5)
Urban transport	27.9	(30.8)	42.2	(38.6)	0.5	(0.1)
Railways	29.7	(23.1)	127.2	(74.0)	-7.2	(1.1)
Ports	30.2	(32.8)	157.1	(130.4)	5.5	(3.6)
Forestry	5.9	(6.2)	144.4	(128.4)	9.3	(32.2)

Note Indicators are the sector-wide weighted means. Results for 2002-03 are shown in brackets.

Source: Productivity Commission estimates.

Financial management performance indicators also varied considerably within each sector (see figure 2.3).

2.3 Government transactions

In 1995, the Council of Australian Governments endorsed the corporatisation of GTEs, as part of a range of reforms under the Competition Principles Agreement. Under the Agreement, governments introduced tax-equivalent payments and debt guarantee fees for all significant GTEs, where the benefits outweighed the costs.

The dividend payments, tax-equivalent payments and CSO payments of GTEs are examined in this report. For more information, see chapter 3.

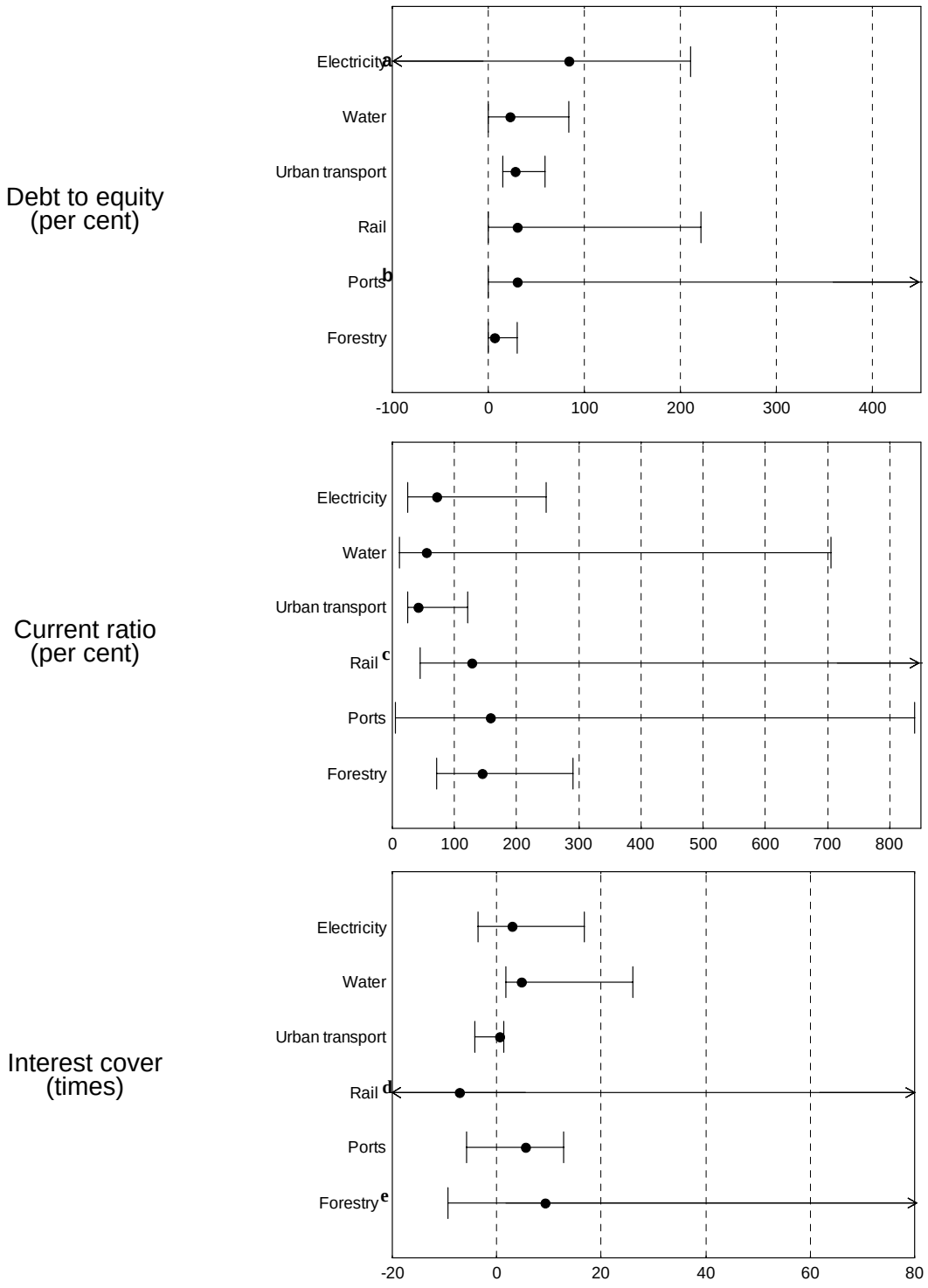
Dividends

Dividend payments are a return on the funds invested in GTEs. The payments are designed to bring GTEs into line with private sector businesses that typically distribute a proportion of their profits to shareholders.

Procedures and policies

Operating profits earned by a corporation can be retained by the company to invest or build up cash reserves. Alternatively, profits can be distributed entirely or in part to shareholders through dividends and buying back shares.

Figure 2.3 **Selected financial management indicators, by sector, 2003-04**



Note The dot represents the weighted mean value and the 'whiskers' represent the range of values for a given performance indicator by sector. **a** The lowest debt to equity ratio for the electricity sector was -172 per cent. **b** The highest debt to equity ratio for the ports sector was 504 per cent. **c** The highest current ratio for the rail sector was 2774 per cent. **d** The lowest interest cover for the rail sector was -1493 times and the highest interest cover for the rail sector was 708 times. **e** The highest interest cover for the forestry sector was 477 times.

Source: Productivity Commission estimates.

In the private sector, a company's constitution will typically specify the procedures by which dividends are to be determined. Usually, these will provide that dividends recommended by the directors are declared by vote at the general meeting (Cassidy 2003).

Procedures for determining GTE dividend payments across jurisdictions are set out in box 2.1. Although broadly similar, there are important procedural differences affecting the extent to which boards have prime responsibility for determining dividends.

The GTE board should be responsible for making recommendations for dividend payments. Boards are best placed to make judgements of this kind. It is appropriate that ministers, as representatives of the owners, have the power to override board recommendations. However, they should be reluctant to do so unless there is a sound basis and they should be required to publicly provide reasons for rejecting board recommendations on dividends.

The 'residual approach' is the theoretical efficient basis of determining dividends. Under this approach, dividends are only paid if there are 'residual earnings' after the financing of all value-adding investment opportunities. This ensures that shareholder value is maximised by exploiting value-adding investment opportunities in the business. When retained earnings are inadequate to meet new investments, businesses issue shares or borrow and no dividend is paid.

It is common in the private sector to 'smooth' dividends.[6] Unsustainable expectations about dividend rates are avoided by making only partial adjustments from year to year, minimising adverse stockholder reactions.

There is limited information on government dividend policies in jurisdictions other than New South Wales. The NSW Treasury (2002) financial distribution guidelines for government businesses is based on the 'residual approach'. However, the NSW Treasury also noted that, given the unique circumstances for government as shareholder:

> … the residual approach must be modified to take into account the Government's strong preference for dividends over capital gain and for a reasonably stable stream of total dividends from its portfolio of businesses. (NSW Treasury 2002a).

6 In maintaining a target dividend level, the volatility of cash flow will affect the size of cash payments and the magnitude of any adjustment to dividends. For example, a company with relatively volatile cash flows is more likely to pay lower dividends in years of high profits to smooth dividends than a company with relatively stable cash flows.

Box 2.1 **Procedures for GTE dividend payments across jurisdictions**

- For Telstra, the power to declare dividends, pay dividends and fix the time for their payment is vested in the Directors.
- For Australia Post, the Board must recommend a dividend payment for the financial year to the Australian Government. The Minister must either approve the recommendation or direct the dividend amount. In the later case, the Minister must inform each House of Parliament. Australia Post's dividend for a financial year must not exceed its profit (after tax) for the financial year.
- For Airservices Australia, the Board must recommend a dividend payment for the financial year to the relevant Minister. The Minister must either approve the recommendation or direct the dividend amount. Airservices Australia's dividend for a financial year may be made out of either, or out of a mixture of both, its profit for the financial year to which the payment relates, or profits for any earlier financial year or years.
- In New South Wales, GTEs are to have a share dividend scheme, as provided in their constitutions, in a form approved by the Treasurer. Further, the Treasurer may direct a GTE to pay a special dividend.
- In Victoria, GTE dividend payments are determined by the Treasurer, after consultation with the board and the relevant Minister.
- In Queensland, a GTE's board must recommend a dividend payment for the financial year to the shareholding ministers, after consultation between the two parties. The recommendation must be accompanied with the board's estimate of the GTE's after-tax profits for the financial year. The shareholding ministers must either approve the recommendation or direct the dividend amount. A GTE's dividend payment must not exceed its estimated profits for the financial year.
- In South Australia, a GTE must recommend a dividend payment for the financial year to the Treasurer. The Treasurer may, after consultation with the GTE's shareholding ministers, either approve the recommendation or direct the dividend amount.
- In Western Australia, generally a GTE's board must recommend a dividend payment for the financial year to the relevant Minister. The Minister, with the concurrence of the Treasurer, may either approve the recommendation or direct the dividend amount.

(Continued next page)

Box 2.1 (continued)

- In Tasmania, a GTE's board must advise the Treasurer and the Portfolio Minister of its recommendation for a dividend payable by the GTE for the financial year. The Treasurer and Portfolio Minister must jointly either approve the recommendation or direct the dividend amount. A GTE's dividend payment must not exceed its consolidated profit (after tax) for the financial year. Further, the Portfolio Minister and the Treasurer, jointly, have the power to direct the GTE to pay a special dividend.[1]
- In the Australian Capital Territory, a GTE's Directors declare a dividend as is agreed to between them and the voting shareholders or, failing agreement, as the voting shareholders direct. A GTE's dividend payment must not exceed its available profit.
- In the Northern Territory, a GTE's board must declare a dividend amount, which may be discussed by the shareholding minister with the board. The board of the GTE must make a recommendation to the shareholding minister as to the amount to be paid as a dividend. The shareholding minister may either approve the recommendation or direct the dividend amount. Further, the shareholding minister may direct the board of a GTE to declare a special dividend.

Source: Relevant Acts.

1 The Portfolio Minister and the Treasurer must not direct a GTE to pay a special dividend unless they have consulted with the board and are satisfied that there are sufficient liquid assets to meet the special dividend and the GTE's contingent and financial needs during the period covered by its corporate plan. A direction to pay a special dividend may be given regardless of whether the GTE is likely to make a consolidated profit during the financial year in which the special dividend is payable. The Treasurer must inform each House of Parliament.

Moreover, the NSW Government prefers that individual businesses do not smooth dividend payments over time by saving some funds in surplus years, for distribution in years when there would otherwise be limited or no capacity to pay a dividend. It prefers excess cash accumulated by government businesses to be returned to shareholders, under the assumption that these funds are more efficiently managed by NSW Treasury.

That said, maintaining relatively stable revenue from GTE dividends to finance budgets is consistent with taking a whole-of-government perspective. However, particular budgetary circumstances in any one year might lead to the declaration of special dividends or a restructuring of the balance sheet.

Trends

In 2003-04, 65 GTEs (78 per cent of those monitored) made dividend payments to their owner-governments, an increase from 56 GTEs (71 per cent) in 2002-03. Total dividends

paid or provided for were around $6 billion. A large proportion of these came from the Australian Government's 50.1 per cent share of Telstra's $3.2 billion dividend.

Total dividends increased by 29 per cent (3.5 per cent excluding Telstra) in 2003-04. This was mainly because Telstra's 2002-03 final dividend was recognised in 2003-04.

Dividend payments have increased by 30 per cent (26 per cent excluding Telstra) over the reporting period.[7] The proportion of GTEs monitored over the entire reporting period not paying, or providing for, a dividend has fallen from around 14 per cent in 1999-00 to 12 per cent in 2003-04.

For the purpose of the analysis that follows, dividends were included in the year that they relate to. Consequently, there are differences between the results reported below and the rest of the report in which dividends are accounted for in the year that they are declared.

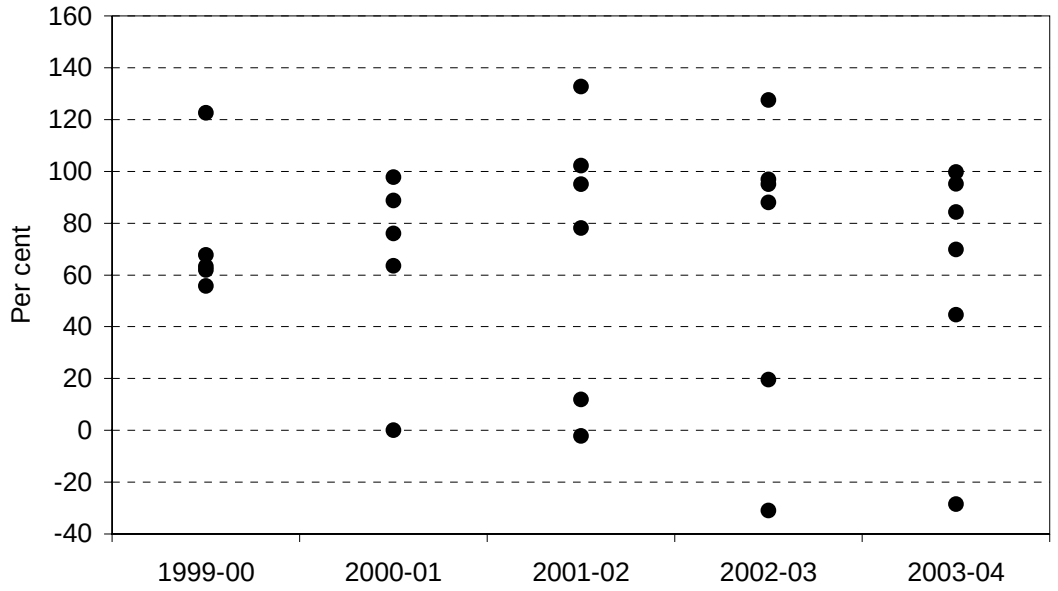
Almost half of the reported GTEs made dividend payments that exceeded profit at some time during the reporting period. Indeed, there were cases of average sector payout ratios exceeding 100 per cent in some years (see figure 2.4).

Dividends in excess of profits that have to be financed through debt could cause a deviation from the optimal capital structure over time — which is the level of debt to equity that minimises the weighted-average cost of capital. They could also result in forgone worthwhile investments, or the burden of further debt if they are debt financed. Under the *Corporations Act*, a 'normal dividend' may only be paid out of profits of a private company, this being a way of protecting creditors of the company.

Some GTEs made dividend payments after reporting operating losses, resulting in negative dividend payout ratios. This suggests that GTEs have been required by their owner-governments to pay dividends regardless of after-tax operating profits. However, negative dividend payout ratios can also occur when dividend payments during the year are based on prior year operating results, as occurs for some GTEs reporting under accounting standard AASB 1044 (see chapter 3).

7 The value of dividend payments in 1999-00 was converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

Figure 2.4 **Dividend payout ratios, by GTE sector**

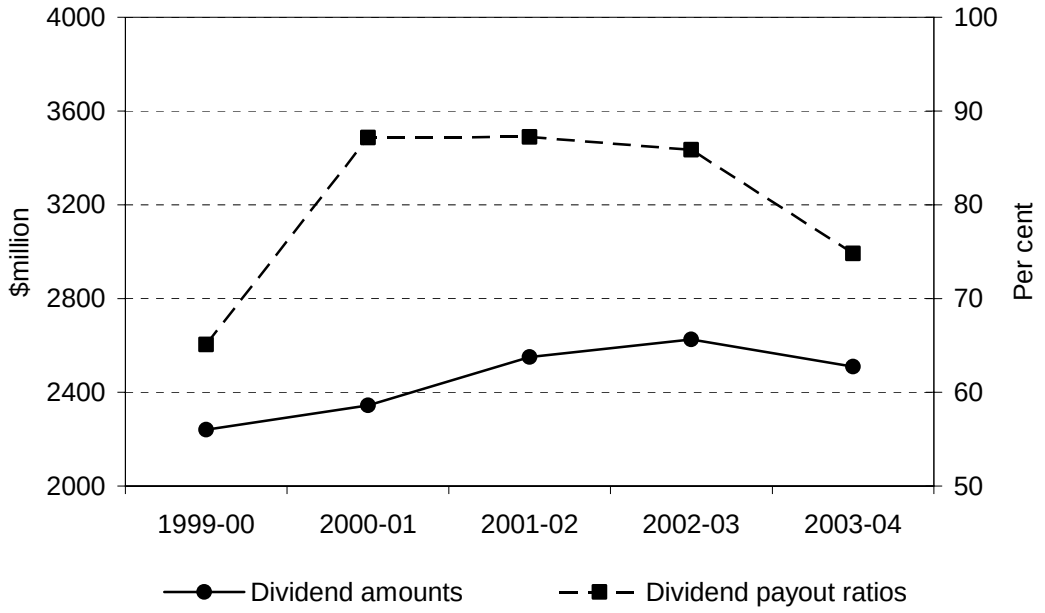


Note GTEs include those GTEs monitored over the entire period and five forestry GTEs monitored since 2001-02. The GTE sectors include electricity, water, urban transport, railways, ports and forestry. For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid.

Data source: Productivity Commission estimates.

Although dividend payout ratios varied, dividend payments to governments were relatively more stable over the reporting period (see figure 2.5). This is consistent with a government preference for a stable stream of total dividends.

Figure 2.5 **Dividend payout ratios and dividend amounts**



Note GTEs include those GTEs monitored over the entire period and five forestry GTEs monitored since 2001-02, though because of the size of Telstra relative to other GTEs, it has been excluded. For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid.

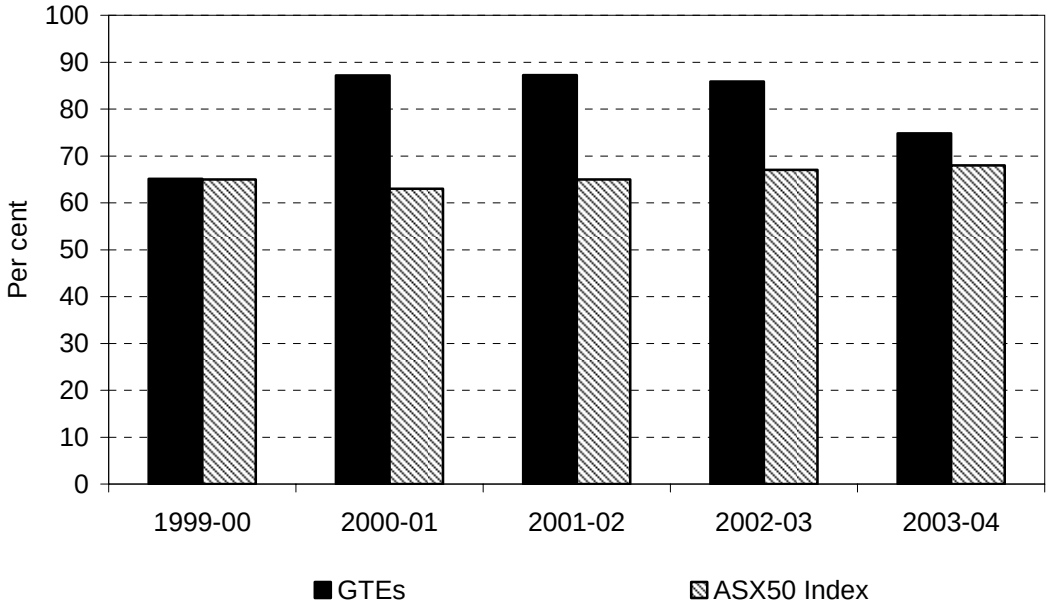
Data source: Productivity Commission estimates.

Comparison with the private sector

GTEs appear to have a generally higher level of dividend payout ratios than that of the companies in the ASX50 Index (see figure 2.6).[8] Over the reporting period, the average dividend payout ratio for the public and the median for the private sector were approximately 79 per cent and 66 per cent respectively. This is consistent with a preference for dividends over capital gains which was explicitly expressed in the NSW Government policy.

8 This analysis of dividends was restricted to the companies in the ASX50 index, as at 28 April 2005, because of the requirement to examine each company's financial ratios for the last five financial years.

Figure 2.6 **Dividend payout ratios, public and private sector**



Note GTEs include those GTEs monitored over the entire period and five forestry GTEs monitored since 2001-02, although because of the size of Telstra relative to other GTEs, it has been excluded. For the private sector companies, the median dividend payout ratio was used, although a weighted average was used for GTEs as more information was available for this sector. For the purpose of this figure, GTE dividends are included in the year that they relate to, rather than the year in which they were provided for or paid. Companies in the ASX50 Index as at May 2005 and included in the previous five financial years were used in the analysis of dividends. It was assumed that the majority of these ASX50 companies declared dividends in the period they relate to, rather than the year in which they were provided for or paid.

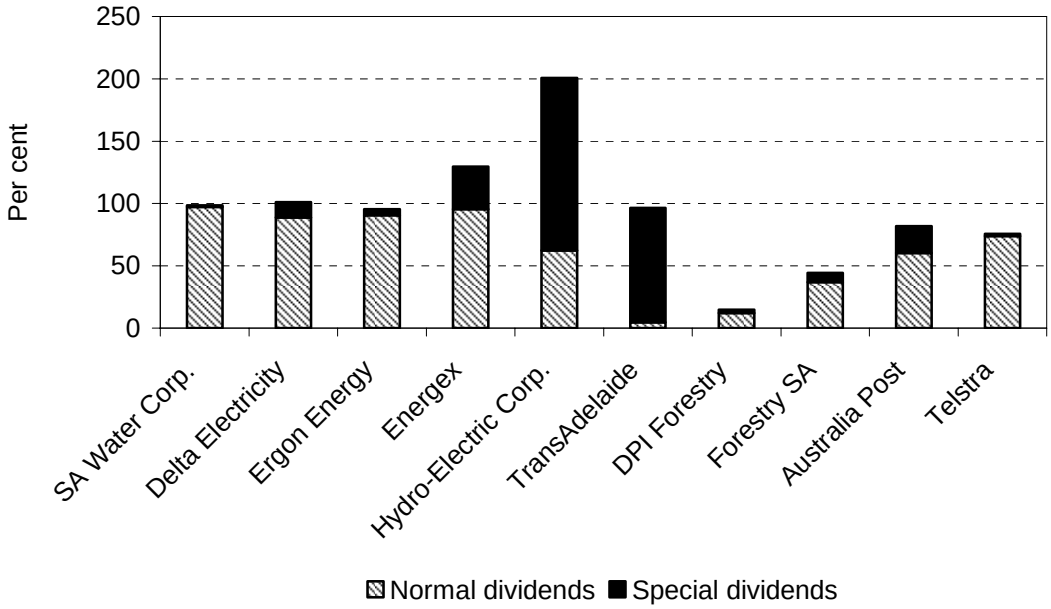
Data source: Productivity Commission estimates, Comsec.

Special dividends

Special dividends are additional, one-off payments made by a business. They are unrelated to current year profits and are used as a mechanism to return excess funds to shareholders. Under Corporations Law, 'special dividends' are payable only from accumulated profits or capital reserves.

A recent sample of ten GTEs reported special dividend payments in either 2002-03 or 2003-04. As shown in figure 2.7, the payout ratio, including special dividends, for these ten GTEs over the 1999-00 and 2003-04 reporting period produced an overall dividend payout ratio close to or above 100 per cent in a number of cases.

Figure 2.7 **'Special' dividend payout ratio over the 1999-00 to 2003-04 reporting period for GTE paying a special dividend in either 2002-03 or 2003-04**



Note The dividend payout ratio is the sum of special and ordinary dividends for the reporting period divided by the sum of after-tax operating profit over the reporting period. A dividend payout ratio greater than 100 per cent indicates that a GTE has paid a dividend that exceeds its after-tax profit over the reporting period. For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid.

Data source: Productivity Commission estimates.

Although governments could at times use GTE special dividends to underpin budgets, special dividends are relatively uncommon and possibly justifiable. For example, there may be substantial retained earnings or reserves prior to the commencement of a reporting period. Further, some special dividends could be associated with capital restructuring.

Shareholder returns

The overall return from dividends and capital growth obtained by investors is commonly referred to as the shareholder return. Generally, if businesses are to attract investor capital, shareholder returns should exceed the expected risk-adjusted returns on forgone investment opportunities.

GTE shareholder returns have implications for both performance and competitive neutrality. Appropriate levels of shareholder return signify that there is an efficient

allocation of resources and that GTEs are not being advantaged relative to competing private businesses.

Both sources of capital, debt and equity, come at a cost to the business. Debt financing involves the payment of interest, and equity will only be provided in the expectation of returns. The return on assets expected from a business must be sufficient to cover the respective costs of its debt and equity — the weighted average cost of capital (WACC).

To ensure competitive neutrality, governments apply a 'debt guarantee fee', which is set at the difference between the actual borrowing costs of the GTE and the borrowing cost that would apply in the absence of a government guarantee. Theoretically, this removes any advantage GTEs gain over competitors through being able to raise debt capital from government sources. While under the corporatisation model, governments generally set commercial targets for their businesses, there is no enforceable mechanism to ensure that GTEs generate commercially competitive returns on equity.

Since GTEs are not listed on the stock exchange, the cost of attracting and retaining equity funds is not directly observable. Consequently, annual shareholder returns have to be estimated by adding the change in the reported value of equity — that is, the implicit capital gain — to the announced dividend payments for the corresponding year. A summary of the results is presented in table 2.3.

Table 2.3 **Summary of results – shareholder returns (per cent)**

	1999-00	2000-01	2001-02	2002-03	2003-04	Average
Sector Returns						
Electricity	16.0	25.4	11.8	14.6	12.3	16.0
Water	-1.2	5.0	5.1	3.0	-2.9	1.8
Urban Transport	0.6	13.4	-3.0	16.9	-0.2	5.5
Railways[a]	-5.5	-2.7	24.7	8.3	6.6	6.3
Ports	7.6	10.2	-0.2	18.1	28.5	12.8
Forestry	na	na	na	6.8	5.9	6.4
Australian Government	28.0	23.3	24.9	34.8	28.7	27.9
All monitored GTE returns	4.2	11.2	8.2	8.2	4.2	7.2
Risk free rate	6.5	5.8	5.9	5.4	5.6	5.9
S&P/ASX200	14.0	5.4	- 7.9	- 5.9	16.7	4.5
Borrowing costs	7.6	6.9	6.3	6.5	6.5	6.8

Note This figures in this table are weighted averages of the 49 GTEs monitored since 1998-99. For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid. **a** The rail sector is represented by Queensland Rail as it is the only rail GTE which has been monitored for the whole reporting period.

Data source: RBA (2005), S&P/ASX200 Index, Productivity Commission estimates.

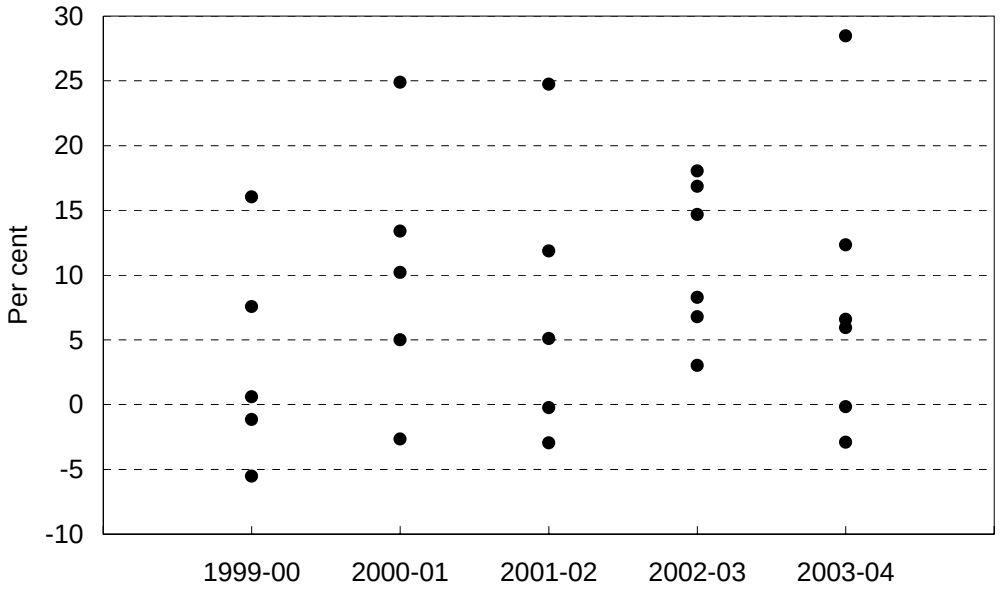
Sector returns

Shareholder returns varied considerably among GTE sectors within the reporting period (see figure 2.8). This variation was particularly pronounced in 2003-04, when the ports sector experienced a substantial increase in shareholder return, while extensive restructuring in the water sector led to a large decrease in calculated shareholder return.

The Australian Government GTEs as a group produced the highest total shareholder returns, averaging approximately 28 per cent per annum over the reporting period. The sector with the highest returns was electricity at 16 per cent per annum.

Generally though, average sector shareholder returns were comparatively lower. The sample of 48 (excluding Telstra) GTEs produced estimated shareholder returns averaging 7.2 per cent per annum (see table 2.3). This figure may have been influenced by the extensive restructuring and associated asset revaluations which occurred in a number of GTEs.

Figure 2.8 **Total shareholder returns — GTE sectors**



Note The GTE sectors included in this graph are electricity, water, urban transport, railways, ports and forestry. For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid.

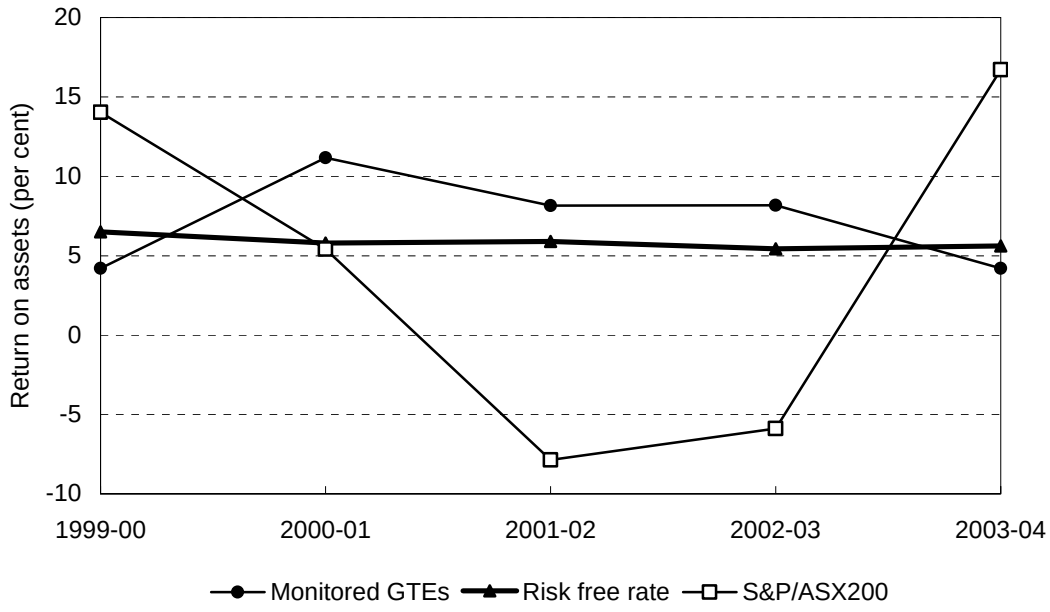
Data source: Productivity Commission estimates.

On average, GTE shareholder returns exceeded those recorded by the companies in the ASX200 Index, which averaged 4.5 per cent over the reporting period (see figure 2.9).

However, large fluctuations in the share market during the period make it difficult to compare the performance of GTEs with the private sector. To meaningfully compare average returns, a longer timeframe would be needed.

The sampled GTEs produced shareholder returns above the risk free rate of return benchmark — approximated by the redemption yield of 10 year Australian Government bonds — in three of the five years in the reporting period (see figure 2.9), and averaged 1.3 per cent per annum above the 10-year bond rate average of 5.9 per cent.

Figure 2.9 **GTE shareholder return comparisons**



Note For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid.

Data sources: RBA (2005), S&P/ASX200 Index, Productivity Commission estimates.

It is generally understood that debt, having less risk than equity, is a cheaper method of finance and therefore that shareholder returns are usually higher than the cost of debt financing. The average rate of return to their shareholder governments was higher than the average cost of debt (gross interest expense divided by debt) in three of the five years and the average shareholder return for monitored GTEs over the reporting period was higher than the average cost of debt (see figure 2.10).

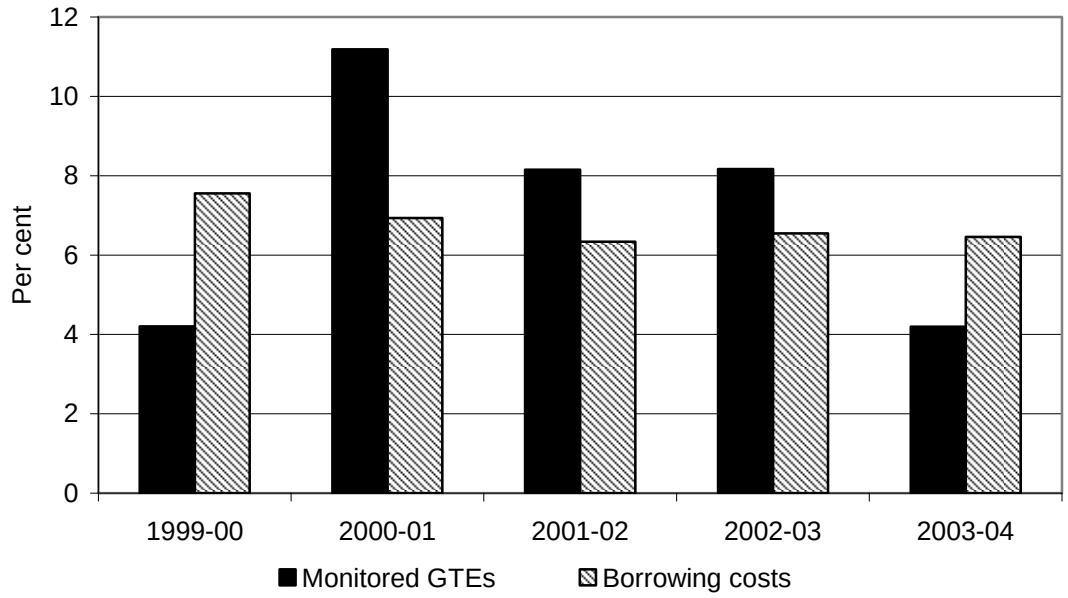
The average shareholder returns achieved by the sampled GTEs compare favourably to the private sector and are marginally (1.3 per cent) above the risk-free rate in the period monitored. However, 30 per cent of these GTEs did not earn average shareholder returns

above the risk free rate over this period. In those cases where a commercial rate of return is not being achieved, there are implications for efficient governance and incentive regulation.

Shareholder returns below a commercial rate could be the result of one or more of a number of factors, including:

- weak market conditions;
- inadequate management and associated inefficiency;
- underpayment for CSOs;
- regulatory error leading to prices being set too low;
- environmental and equity considerations that lead to restrictions on sales for some GTEs — particularly in the water sector; and
- the presence of overvalued assets, which artificially inflate equity and reduce shareholder returns.

Figure 2.10 **GTE shareholder returns and cost of GTE debt**



Note For the purpose of this figure, dividends are included in the year that they relate to, rather than the year in which they were provided for or paid. Borrowing costs is measured as gross interest expense divided by debt.

Data source: Productivity Commission estimates.

GTEs might also provide returns on equity in the form of spillover social benefits. Therefore a desire by governments to maximise social returns could reduce profits. The

maximisation of the financial returns of some GTEs could reduce social returns, through higher prices and lower service quality. However, the use of GTEs to meet social objectives in this way would be inconsistent with the GTE corporatisation model, under which GTEs are first and foremost operated commercially and social obligations are transparently recognised and fully funded.

Unless GTEs diligently pursue commercial targets, governance might be compromised through reduced board accountability. Moreover, the effectiveness of incentive regulation, that requires GTEs to pursue commercial rates of return, is likely to be compromised in the absence of such commercial disciplines.

Tax-equivalent payments

Under a tax-equivalent payment regime, GTEs are required to pay tax on their operating profit at the same company tax rate as private businesses. If this were not the case, all other things being equal, a GTE would be able to earn the same after-tax commercial rate of return as its competitors with lower prices or higher operating costs.

During 2003-04, most of the 83 GTEs monitored were subject to the National Tax Equivalent Regime (NTER). A majority of GTEs were also subject to the NTER in 2002-03. The NTER unified the tax equivalent arrangements of State and Territory Government-owned entities that were previously subject to inconsistent tax-equivalent regimes of their respective owner governments.

> The primary objective of the NTER is to promote competitive neutrality, through a uniform application of income tax laws, between the NTER entities and their privately held counterparts (ATO 2001).

In 2003-04, the 83 monitored GTEs paid almost $3.5 billion in tax-equivalent payments to governments, of which Telstra contributed more than 50 per cent. The remaining GTEs each paid an average of approximately $21 million. Total tax-equivalent payments were 13 per cent ($399 million) higher than the previous year, largely as a result of a 13 per cent ($197 million) increase in Telstra's tax payments. Average tax-equivalent payments from the remaining GTEs also increased during 2003-04, by more than 14 per cent.

Community service obligations

GTEs often provide economic and social benefits to the community over and above the direct benefits of their goods and services as paid for by consumers. For example, urban public transport GTEs provide explicit community benefits such as greater mobility and

access for disadvantaged groups, as well as other positive externalities such as reduced motor vehicle pollution and urban road congestion.

Historically, governments have recognised these benefits through the funding of operating deficits of the relevant GTEs. However, current government policy is to make on-budget payments directly to the GTEs for the provision of certain CSOs, such as pensioner concession fares.

In 2003-04, governments paid monitored GTEs almost $3 billion in disclosed CSO payments. In some cases, GTEs did not disclose CSO funding. Some GTEs also provide CSOs without reimbursement. For example, Telstra does not receive government funding for the Universal Service Obligation (USO) or Digital Data Service Obligation (DDSO) (see chapter 11).

Rail GTEs received almost 60 per cent of the overall CSO funding, with GTEs in the water sector receiving 16 per cent and the electricity sector 13 per cent. The urban transport sector received almost all of the remaining 11 per cent of CSO funding. As a percentage of the sector's total revenue, urban transport received the largest amount of CSO funding at 38 per cent, followed by water at 31 per cent.

Total CSO payments to those GTEs monitored for the entire reporting period increased by 12 per cent in real terms from 1999-00 to 2003-04. Real CSO payments in the electricity, water and urban transport sectors increased by 70 per cent, 17 per cent and 29 per cent respectively over the reporting period. Real CSO payments in the rail and ports sectors decreased by 30 per cent and 24 per cent respectively.

3 Interpretation of performance measure

The assessment of the financial performances of government trading enterprises (GTEs) monitored in this report is based on performance indicators derived from a data set that is broadly consistent over time and across jurisdictions. The data sources, the construction of the performance indicators and the issues relevant to the interpretation of the results are discussed in this chapter.

3.1 Data

The data used in calculating the financial performance indicators for 1999-00 to 2003-04 were taken from two sources:

- Government Finance Statistics (GFS) collection — data collected by State and Territory Treasury Departments for the Australian Bureau of Statistics (ABS); and

- General Purpose Financial Report (GPFR) — data extracted from audited GTE financial statements.

The GFS framework uses concepts and classifications developed by the ABS in the preparation of public finance reports. The framework is based on international standards developed by the International Monetary Fund and the United Nations. The concepts used are consistent with those underlying the national accounts.

Governments also report financial information under the GPFR framework, based on accounting standards. Australian Accounting Standards used for this purpose have been developed by the Australian Accounting Standards Board (AASB) and are based on generally accepted accounting principles. The primary purpose of the GPFR framework is to facilitate financial analysis.

GFS data were used to calculate the financial performance indicators for each GTE. However, in a small number of cases GPFR data were used because some items are not reported separately under GFS. No GFS data were available for the Australian Government GTEs and GPFR data were therefore used.

Differences between GFS and GPFR

Financial reports under the GFS and GPFR frameworks are generally similar. Although these are minor measurement, labelling and presentation differences, there are a number of differences in the treatment of transactions that GTEs undertake on a regular basis (see table 3.1). Other less numerous differences arise from the treatment of foreign exchange gains and losses, swaps and derivatives, and superannuation expenses.

As a result of these differences, care is required when comparing the financial indicators in this publication with those obtained from GTE financial statements.

Table 3.1 **Differences between GFS and GPFR — selected items**

Items	*GFS*	*GPFR*
Gains and losses on assets	Treated as revaluations and as such are excluded from the net operating balance.	Can be treated as revenue and expenses and may therefore be included in the net operating balance.
Distributions to owners	Distributions to owners in the form of dividends are treated as operating expenses.	Distributions are disclosed after operating results and therefore do not form part of the operating statement.
Prior-period adjustments	Operating results can include prior-period adjustments.	Operating results reflect only items that represent revenue and expenses transactions relevant to the reporting period.

Source: SA Treasury (2001).

Gains and losses

The differing treatment of gains and losses on assets may generate inconsistencies in areas such as the profit (or loss) on the sale of assets, and revenue (or expenses) from asset revaluations. These differences can affect the reported operating profit. For example, under the GFS framework, revaluations are recorded directly in equity and have no influence on operating profit. In contrast, under the GPFR framework, changes in asset valuations may be recorded in the statement of financial performance.[1]

1 Under accounting standards, any increase in the value of assets must be recorded in an asset revaluation reserve. The exception is any increase that reverses a downward revaluation previously recognised as an expense in the statement of financial performance, which must be recognised as revenue. A downward revaluation must be recognised as an expense. The exception is any decrement that reverses a previous revaluation increment, which must be recorded in an asset revaluation reserve.

Differences in the approach to the timing of asset valuation also have the potential to generate inconsistencies. Revaluation of non-current assets prior to disposal is not required under the GPFR framework, whereas under the GFS framework it is. Consequently, the GPFR operating statements may contain gains or losses incurred in the disposal of the asset that are not recorded under the GFS framework.

These discrepancies between the GFS and the GPFR treatment of asset revaluations at disposal are not expected to affect indicators substantively. The majority of GTEs value their non-current assets using current valuation methodologies, ensuring minimal gains or losses on disposal.

Distributions to owners

Distributions to owners in the form of dividends and income tax-equivalent payments are regarded as operating expenses under the GFS framework. These amounts can be separately identified and are excluded from expenses in the calculation of performance measures.

Prior-period adjustments

Under the GFS framework, operating results reflect only items that represent revenue and expense transactions relevant to the current period, whereas operating results in the GPFR may include prior-period adjustments.[2] The AASB has outlined when such differences are most likely to occur (see box 3.1).

2 Under the GFS framework, prior-period items arising in the current period are allocated to the relevant prior-period. Under Australian Accounting Standards, prior-period items arising in the current period are allocated to the current period.

Box 3.1 **GFS differences resulting from prior-period adjustments**

Revision of estimates — Unlike GPFR, estimates of GFS data may be adjusted in the future. With GFS, adjustments may be made to prior-period operating results as a consequence of a revision to estimates.

Correction of errors — In GPFR, any error made in a prior-period is corrected in the period in which the error is discovered. With GFS, prior-periods are revised to take account of errors made in the relevant period.

Voluntary changes in accounting policy — In GPFR, the effects of any voluntary change in accounting policy are calculated on the basis that the new policy has always been in place. Any effects are recognised as revenue or expenses in the reporting period in which the change is made. With GFS, prior-period operating results are revised to take account of the effect of changes in the relevant period.

Change in accounting policy due to the adoption of an accounting standard — In GPFR, the adoption of accounting standards requires that a retrospective adjustment be made at the beginning of the reporting period in which the standard is first applied. With GFS, the effects of adopting a new accounting policy result in revisions to prior-period operating results.

Source: Material provided by the AASB.

Effect of differences between GFS and GPFR

In most cases, the operating results obtained using the GFS framework match, or are almost identical to, the GPFR framework, once adjustments have been made to the GFS for dividend and tax-equivalent payments.

In a small number of cases there may be significant differences caused by the treatment of a gain or loss made on asset sales. For example, in 2001-02, TransAdelaide reported an operating loss of around $12 million under the GPFR framework, largely due to a $12 million loss on asset sales. Under the GFS framework, it achieved an operating profit of around $6000.

Adjusting nominal values

Data presented in this report are based on nominal values — amounts denominated in terms of values at a particular point in time using 'dollars of the day'. Where changes in real values are reported, nominal values were adjusted to their present values using price changes relating to capital investment by government businesses.[3] However, there are

3 The deflator used was the implicit price deflator for gross fixed capital formation — public corporations (ABS 2004c).

alternative measures of price change that can be used which may result in different real values (see table 3.2).

Table 3.2 **Selected deflators, 1999-00 to 2003-04**

	Implicit price deflator			*Consumer price index*
	Gross fixed capital formation (public corporations)	*Final consumption expenditure (other government)*	*Gross domestic product*	*All groups (Australia)*
1999-00	0.974	0.862	0.870	0.870
2000-01	0.992	0.898	0.914	0.921
2001-02	1.001	0.933	0.939	0.948
2002-03	1.001	0.966	0.967	0.977
2003-04	1.000	1.000	1.000	1.000

Source: ABS (2004a; 2004c).

Real values were obtained by dividing nominal values for each year by the deflator that more closely reflected the underlying cost structure of GTEs. For example, the nominal revenue in 2000-01 for the Hunter Water Corporation's revenue of $130.6 million is divided by 0.992 (Gross fixed capital formation — public corporations) to obtain a real value of $131.7 million. The real value using the Consumer Price Index — All Groups (Australia) deflator (0.921) would be $141.8 million.

3.2 Performance indicators

The performances of GTEs are reported using a consistent set of financial indicators. These indicators are presented under three broad headings — profitability, financial management and transactions with government.

The indicators provide an overall picture of how a GTE is performing over time and relative to other GTEs. Generally, it is reasonable to make comparisons across GTEs in the same sector in Australia.

In some cases, intra-sectoral comparisons need to take into account the broad range of activities undertaken within a sector. For example, in the electricity sector, Western Power (WA) and Power and Water (NT) are vertically integrated — undertaking generation, transmission, distribution and retail activities. In contrast, other GTEs in the electricity sector generally specialise in one, or in some cases two, of these activities.

Analyses of privately-owned businesses operating in similar sectors in Australia and overseas may also provide useful benchmarks, against which the performance of GTEs can

be compared. However, care is required because of differences in accounting standards, including those relating to asset valuation.

Profitability

Profitability indicators provide a concise and consistent way of presenting financial information. In the absence of stock market valuations, they are an important guide to the performance of a GTE.[4] Profitability indicators provide governments and the community with a means of evaluating how well GTEs are using the assets vested in them.

Profitability can be affected by factors largely outside the control of GTEs. For example, the weather impacts on the revenue of many GTEs in the water sector. This can significantly affect profitability from year-to-year, particularly given that many GTEs have relatively high fixed costs.

Listed below are the five profitability indicators used in this report. Also included is an explanation of what they represent and how they are interpreted. For derivations of these indicators, see tables 3.1 and 3.2 at the end of this chapter.

Operating profit before tax — is an indicator of the operational performance of an entity, before income tax is paid. It measures the difference between total revenue and total expenses (excluding income tax).

Operating sales margin — is an indicator of the surplus (not including interest and income tax) earned on sales revenue. It measures trends in operating revenue and expenses that are independent of changes in capital structure and tax regimes.

Cost recovery — is an indicator of the ability of an entity to generate adequate revenue to meet operating expenses. Investment income, receipts from government to cover operating deficits and gross interest expense are excluded. A cost recovery ratio of 100 per cent indicates that a GTE is able to meet its operating expenses from its operating revenue, excluding the cost of servicing debt.[5]

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4 If a company is listed on the stock exchange, the market assessment of the value of its equity will generally be expressed through the price of its shares. Hence, expected returns are capitalised into the value of the company through movements in its share price, consistent with the cost of capital. At any particular time, the price of a company's shares encapsulates investors' views of its current and prospective financial performance.

5 In 1999-00, 'abnormal' revenue and expenses were also excluded from the cost recovery ratio. In 2000-01, the concept of 'abnormal items' under accounting standards was replaced by the narrower concept 'significant items'. Significant items were not excluded from the cost

Return on assets — is an indicator of the rate of return earned from all assets. The ratio provides a measure of the efficiency with which an entity uses the assets vested in it to produce operating profit before interest and tax. It is a useful indicator for comparing the profitability of GTEs and businesses in similar industries against a benchmark rate of return equal to the risk-adjusted weighted average cost of capital.

The return on assets is affected by changes in asset values arising from asset revaluations, transfers or sales. Some GTEs use different asset valuation methodologies, depending on the type of assets. Reported asset values may vary significantly for a given GTE over time, which reduces comparability. If assets are overvalued, GTEs might not appear to earn sufficient returns. Further, inappropriate asset valuations have implications for the efficiency of prices — because it is unlikely that those prices will properly incorporate the actual cost of capital and depreciation.

Return on equity — is an indicator of the rate of return that an entity is providing to shareholders. The ratio allows the rate of return achieved by a GTE to be contrasted with that expected from alternative investments with a similar level of risk.

Financial management

Debt is a major source of funds from which GTEs finance their activities. At the end of 2003-04, the accumulated borrowings of monitored GTEs were around $47 billion and the debt to equity ratio was 45.8 per cent. The capital structure of a GTE is partly determined by the financial risk associated with the use of debt finance. This risk stems from the commitment to pay interest and repay principal, irrespective of earnings. For example, a decline in operating revenue or an increase in the cost of servicing debt can result in liquidity problems if a GTE's debt is not well managed.

Financial management indicators provide information on the extent debt is used to finance a GTE's assets, and the GTE's ability to meet periodical interest payments and short-term liabilities. There are various factors — including the impact of government directives, changes in asset values and financial restructuring — that have to be taken into account when assessing financial management performance, particularly over time.

recovery ratio in 2000-01 because it was apparent that GTEs treated 'abnormal' and 'significant' items differently (see PC 2002a).

Listed below are the five financial management indicators used in this report. Also included is an explanation of what they represent and how they are interpreted. For derivations of the indicators, see tables 3.1 and 3.2 at the end of this chapter.

Debt to total assets ratio — is an indicator of the proportion of assets that are financed with borrowed capital. It gives an indication of the level of exposure to creditors and their interest in the GTE.

Debt to equity ratio — is an indicator of the risk of the entity's capital structure in terms of the amount of capital sourced from borrowing and the amount from shareholders (governments in the case of GTEs). The greater the debt to equity ratio, the more geared the GTE.

Total liabilities to equity ratio — is an indicator of the exposure to claims over the assets of the GTE by all creditors, in the event that the business ceases operations. An acceptable level for these debt ratios is likely to vary over time and between industries.

Current ratio — is an indicator of an entity's ability to meet short-term liabilities by realising short-term assets. A current ratio greater than 100 per cent indicates that current assets exceed current liabilities and, if realised, their disposal would meet short-term obligations. An acceptable level for the current ratio will be related to the stability of cash flows.

Interest cover — is an indicator of an entity's ability to meet periodic interest payments from current profit (before interest expense). The level of interest cover gives an indication of how much room there is for interest payments to be maintained in the face of interest rate increases or reduced profitability.

Apart from the effect of changes in the value of assets, financial management ratios are also affected by changes in liabilities. The debt to equity ratio is affected, as equity is a residual measure obtained by deducting total liabilities from total assets. For example, an adjustment to provisions for employee entitlements would, if it leads to an increase in total liabilities, decrease equity (and vice versa), other things being equal.

The debt to equity and debt to total assets ratios are also affected by financial restructuring. Debt for equity swaps, debt transfers to governments, retirement of debt and debt revaluations will influence these ratios either directly through their impact on debt levels or indirectly through their impact on the value of equity.

Transactions with government

Transactions with government cover tax-equivalent and dividend payments made by GTEs to governments, and payments from governments to GTEs for community service obligations (CSOs).

Listed below are the five indicators used in this report to measure transactions with government. Also included is an explanation of what they represent and how they are interpreted. For derivations of the indicators, see tables 3.1 and 3.2 at the end of this chapter.

Dividends — are the value of funds transferred from the present and past after-tax profits of an entity to its owners. Dividends are reported when an adjustment is made to retained earnings (equity) in the statement of financial position (previously the balance sheet).

In some cases, governments have effected changes to the capital structure of a GTE by requiring the payment of special dividends.

Dividend payout ratio — is an indicator of the relative size of an entity's dividend payments to its profitability. It gives an indication of the share of after-tax profits that are returned to shareholders. The greater the dividend payout ratio, the higher the share of after-tax profit that is returned to shareholders. A ratio greater than 100 per cent indicates that an entity has paid a dividend that exceeds its current after-tax profits.

Dividend to equity ratio — is an indicator of the relative size an entity's dividend payments to shareholders' equity. A low dividend to equity ratio may indicate that profits are being retained by the entity to fund capital expenditure.

In some cases, comparisons of dividend ratios have to be interpreted with caution. The timing of dividend payments, declarations of dividends by boards, and ministerial approval or directions to pay dividends can result in instances where dividends reported for a financial year relate to operating results in previous years.

Typically, dividends are provided for in the year that they accrue. However, there are many cases where:

- dividends are declared and provided for in the year following the year that they accrued; and

- interim dividends for a financial year are provided in the year that they accrue and a final dividend is provided for in the subsequent year.[6]

Unless noted otherwise, dividends for a financial year were not adjusted or re-allocated to previous years to take account of changes in practices or policies. However, a note is included that indicates that an adjustment can be made to ascertain its effect on dividend payout ratios (see box 3.2).

Changes in policies and practices by GTEs and governments over the reporting period can sometimes make comparisons difficult. For example, Victorian GTEs typically paid an interim and final dividend relating to each financial year. The interim dividend was paid during the year and the final dividend was recorded as a provision (liability) at the end of the year.

In 2000-01, following a change in accounting policy, Victorian GTEs did not provide for the final dividend because they had not yet been approved by the Treasurer. Therefore, only the interim dividend was included by these GTEs in 2000-01. In 2001-02, the reported dividends for Victorian GTEs included the final dividend that was approved by the Treasurer relating to 2000-01 and the interim dividend for 2001-02.

Income tax expense — is the value of tax-equivalent payments made to government by GTEs. Trends in the value of tax-equivalent payments do not always follow trends in pre-tax operating profit because of past tax losses, changes in tax rates and timing and other differences between accounting and taxable income.

CSO funding — is the value of payments by governments to GTEs for the specific non-commercial activities that they are directed by governments to undertake. CSO payments are reported only when separately disclosed in financial statements.

6 Creating a provision for a specific final dividend does not necessarily imply that the amount will eventually be paid.

Box 3.2 Current Accounting Standard

A number of GTEs adopted accounting standard AASB 1044 *Provisions, Contingent Liabilties and Contingent Assets* for the first time from 1 July 2002, even though policies with similar effect had already been adopted in Victoria for example. As explained below, the timing changes resulting from the application of AASB 1044 have the potential to affect some of the year to year dividend and ratio calculations used in this report.

It has been common practice for governments to announce a dividend after the end of the financial year, but before the financial statements for that year were finalised. Previously, even though the dividends may have been announced after 30 June 2002 for example, they were nevertheless recognised or recorded as a liability or provision in the financial statements for the 2001-02 year, even though they were not actually paid until the 2002-03 year.

The effect of the new standard AASB 1044 is to record a dividend announced after 30 June 2002 in the financial statements for the year in which the dividend is announced. In the above example, such a dividend would not now be reported in 2001-02, but be included in the financial statements for the 2002-03 year. Any amount that had been disclosed but that remains undistributed at 30 June 2003, would be recorded as a liability.

Whenever an announced dividend is paid, it is deducted from retained profits. The reported net profit in the current year is unaffected, because dividends are paid after net profit is calculated. However, AASB 1044 can affect the calculated dividend payout ratio, and any other financial ratio — where its calculation varies according to the level of current liabilities associated with dividend recognition.

Source: AASB (2004).

Table 3.1 **Published financial performance indicators**

Code	*Ratio*	*Definition*
B.01	Operating sales margin B.17 / (B.14 - B.33)	$\frac{\text{EBIT less investment income}}{\text{Total revenue less investment income}}$
B.02	Cost recovery ratio B.24 / B.36	$\frac{\text{Revenue from operations}}{\text{Expenses from operations}}$
B.03	Return on assets B.16 / B.19	$\frac{\text{Earnings before interest and tax and after abnormals (EBIT)}}{\text{Average total assets}}$
B.04	Return on equity (B.15 - B.31) / B.34	$\frac{\text{Operating profit after income tax}}{\text{Average total equity}}$
B.05	Debt to equity B.27 / B.26	$\frac{\text{Debt}}{\text{Total equity}}$
B.06	Debt to total assets B.27 / B.19	$\frac{\text{Debt}}{\text{Average total assets}}$
B.07	Total liabilities to equity B.22 / B.26	$\frac{\text{Total liabilities}}{\text{Total equity}}$
B.08	Interest cover B.16 / B.28	$\frac{\text{EBIT}}{\text{Gross interest expense}}$
B.09	Current ratio B.21 / B.23	$\frac{\text{Current assets}}{\text{Current liabilities}}$
B.10	Leverage ratio B.13 / B.26	$\frac{\text{Total assets}}{\text{Total equity}}$
B.11	Dividend to equity ratio B.18 / B.34	$\frac{\text{Dividends paid or provided for}}{\text{Average total equity}}$
B.12	Dividend payout ratio B.18 / (B.15 - B.31)	$\frac{\text{Dividends paid or provided for}}{\text{Operating profit after tax}}$

Table 3.2 **Non-published financial performance indicators**

Code	*Ratio*	*GFS code*	*Definition*
B.13	Total Assets	ETF 81	The service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured at the end of the reporting period).
B.14	Total Revenue	ETF 11	Includes revenue from sales and levies, revenue from asset sales, investment income, receipts from governments for specific agreed services (eg community service obligations), other revenue from operations, receipts from governments to cover deficits on operations and abnormal revenue. Excludes equity contributions from governments. GFS has a separate group for abnormals and extraordinary items, ETF 19. Adjustments are made to include abnormal revenue.
B.15	Operating profit before income tax B.14 - B.25		Total revenue less total expenses. Includes abnormal items.
B.16	Earnings before interest and tax (EBIT) B.15 + B.28		Operating profit before income tax plus gross interest expense.
B.17	EBIT from operations B.16 - B.33		Operating profit before income tax plus gross interest expense less investment income.
B.18	Dividends paid or provided for		The amount included in the profit and loss statement for dividends. Includes normal and special dividends and statutory levies on profits and revenue. Excludes returns of capital.
B.19	Average total assets		Average of the value of assets at the beginning and end of the reporting period.
B.21	Current assets	Not classified[a]	Cash and other assets that would, in the ordinary course of operations, be available for conversion into cash within 12 months after the end of the reporting period.
B.22	Total liabilities	ETF 82	The future sacrifice of service potential or future economic benefits that the entity is obliged to make to other entities as a result of past transactions or other events (measured as at the end of the reporting period). Includes provisions for employee entitlements, creditors, deferred revenue, all repayable borrowings and interest bearing non-repayable borrowings.
B.23	Current liabilities	Not classified[a]	Liabilities that would, in the ordinary course of operations, be due and payable within 12 months after the end of the reporting period.

a The Economic Type Framework (ETF) does not differentiate between current and non-current assets.

(Continued next page)

Table 3.2 (continued)

Code	*Ratio*	*GFS code*	*Definition*
B.24	Revenue from operations B.14 - B.29 - B.33 - B.35		Total revenue less abnormal revenue, investment income and receipts from governments to cover deficits on operations.
B.25	Total Expenses	ETF 12	Includes salaries and wages, purchases, interest, bad and doubtful debts, material losses from the sale of non-current assets, charges for depreciation, amortisation or diminution in the value of assets and abnormal expenses. GFS has a separate group for abnormals and extraordinary items, ETF 19. Adjustments are made to include abnormal revenue.
B.26	Total equity B13 - B.22		Total assets less total liabilities.
B.27	Debt		Includes all repayable borrowings (both interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Excludes creditors and provisions (but not offsetting assets such as contributions to sinking funds).
B.28	Gross interest expense	ETF 1262	Amount charged to the profit and loss account. Includes finance charges on finance leases and all debt related financial expenses.
B.29	Abnormal revenue		Revenue included in operating profit (or loss) after income tax, which are considered abnormal by reason of their size and effect on the operating result. Abnormal revenue differs from extraordinary revenue in that extraordinary revenue is attributable to events or transactions of a type that are outside the ordinary operations of the entity and are not of a recurring nature.
B.30	Abnormal expenses		Same as description for B.29, except for expenses.
B.31	Income tax	ETF 1264	Income tax expense, or income tax-equivalent expense, on operating profit before tax (including abnormal items) calculated using tax effect accounting (AAS3).
B.33	Investment income	ETF 1131, ETF 1132	Income received and receivable on financial assets.
B.34	Average total equity		Average of total equity at the beginning and end of the reporting period.
B.35	Receipts from Government to cover deficits on operation		Receipts from Government to cover deficits on operations, but excludes receipts from governments for specific agreed services (for example, community service obligations).
B.36	Expenses from operations B.25 - B.30 - B.28		Total expenses less abnormal expenses and gross interest expense.

4 External Governance of GTEs

Key points

- There are some deficiencies in the governance arrangements for GTEs. Given the economic significance of the GTE sector, improvements in governance could yield significant benefits to the community.
  - clearer and more effective governance procedures could also reduce the need for specific regulation of individual GTEs.
- Governance reforms must recognise, and address, the inherent tension in the corporatisation model between the commercial imperative and the non-commercial objectives that underpin government ownership.
- Priorities in the reform agenda should include:
  - clarification and public scrutiny of the rationale for ongoing government ownership of GTEs;
  - greater clarification and transparency of objectives (both commercial and other public interest), together with their prioritisation or weighting;
  - making a clearer distinction between external and internal governance, with improved transparency of the external governance role of ministers;
  - greater independence of GTE boards, with CEOs appointed by, and accountable only to, GTE boards; and
  - a general strengthening of accountability, including the public availability of statements of corporate intent that express objectives as target outcomes.
- Performance monitoring is important in assessing whether the public interest is being met. Sufficient resources should be provided to enable substantive performance reporting and greater national harmonisation of that reporting.
- In reforming external governance arrangements, the commercial focus of GTEs should be maintained by ensuring that community service obligations are fully funded from government budgets and that capital market disciplines are strictly maintained.

In the last two annual monitoring reports, the Commission analysed external governance issues relating to government trading enterprises (GTEs). This chapter draws out the key findings and messages from that analysis.

External governance refers to the authority and systems utilised by ministers and government agencies for the control and supervision of public organisations (OECD 2002). It is a feature that makes GTEs distinctly different from private sector enterprises.

Internal governance refers to the systems of direction and control within an organisation, and is the responsibility of the governing body, usually a board, and senior management of the organisation. The distinction between internal and external governance is one of responsibility not focus. Indeed, in performing their responsibilities, boards must have regard for the external environment in which the GTE operates.

In the Commission's recent National Competition Policy (NCP) inquiry report, the development of effective governance arrangements for GTEs was identified as a key factor in achieving performance improvement (PC 2005a). In this year's monitoring report, the Commission examines ways in which external governance arrangements can be improved.

Collectively, GTEs in Australia control more than $174 billion worth of assets and provide, often as a monopoly, essential services to the community such as water, electricity, gas and transport. Poor governance practices potentially distort the operational, asset management, investment and dividend distribution decisions of these significant sectors of the economy. Improved governance practices therefore have the potential to reap a significant 'reform dividend'.

4.1 Background

Current governance arrangements for GTEs largely reflect the various reforms introduced over the past 15 years or so to improve the performance of government infrastructure providers, and to increase their exposure to competition. These reforms followed concerns in the late 1980s about the quality of their goods and services, high prices, levels of indebtedness, lack of transparency and high public subsidies. The poor performance of these departments and statutory authorities providing these services at the time came to be viewed as a major impediment to economic growth (Morton 1999).

Governments responded to these concerns by commercialising many GTEs, replicating private sector principles and practices, shedding non-core activities and placing greater emphasis on cost recovery.

The next round of reforms involved the corporatisation of many commercialised entities. These reforms were subsequently incorporated into the Competition Principles Agreement

(CPA) of 1995, through which governments agreed to adopt a corporatisation model for significant GTEs (and major agency business activities and public financial enterprises) to the extent that the benefits of corporatisation outweighed the costs.

Under the CPA, each jurisdiction undertook to remove from monopolies any responsibilities for industry regulation before introducing competition. Further, when exposing public monopolies to competition or privatising them, governments undertook to review:

- the appropriate objectives for the public monopoly;
- the merits of separating any natural monopoly elements from potentially competitive elements of the public monopoly;
- the most effective means of separating regulatory functions from the commercial functions of the public monopoly;
- the most effective way of implementing competitive neutrality principles;
- the merits of any community service obligations (CSOs) and the best way of funding and delivering them;
- the price and service regulation to be applied to the industry; and
- appropriate financial relationships between the owners and management of public monopolies (including rates of return, dividends and capital structure) (CoAG 1995).

The competitive neutrality principles required governments to impose full tax (or tax-equivalent systems) and debt guarantee fees, while also subjecting the corporatised entities to normal private sector business regulations. Prices charged by businesses were to fully reflect their costs.

Each government was free to determine its own timing and scope of the structural reform of its public monopolies, including whether or not to privatise them.

4.2 Characteristics of corporatised entities

The external governance of corporatised GTEs needs to be founded on their key characteristics, many of which distinguish them from private companies and departments of state:

- *Ownership and legal status* — Ownership is non-contestable, with government retaining ownership (or part ownership) of the GTE on behalf of the public. The GTE is not part of a government department, but is established as a separate corporatised legal entity. Few are established as company GTEs (to which Corporations Law applies).

Most are established as statutory GTEs, under legislation that may be specific to a GTE, to the relevant industry, or to cover all GTEs in a jurisdiction.

- *Functions* — Although the corporatised GTE is commercially and competitively focussed, it generally has other objectives that can conflict with that focus. The GTE has no regulatory functions — these, where they existed, have been transferred to separate agencies or government departments. Most policy functions were similarly moved. The GTE is required to abide by competitive neutrality principles.

- *Ministerial authority and responsibilities* — Ministers, as voting shareholders, undertake the role of owners on behalf of the community. The responsible minister(s) exercises external governance through broad strategic control over the GTE. There are varying legislative models among the jurisdictions, some of which also permit a measure of ministerial involvement in internal governance.

  Ministers specify the CSOs they expect the GTE to meet and ideally, for the purposes of transparency, provide the GTE with separate budget funding to satisfy those CSOs. Ministers may, in some cases, also direct the GTE to adopt other public policy or whole-of-government practices.

  The establishing legislation generally provides for directions by the responsible minister(s) to a GTE's board to be in writing and tabled in Parliament.

- *Board authority* — A board is established. It is presumed to be autonomous and accountable for internal governance. Directors are generally appointed because of their expertise and ability to contribute to the GTE's overall corporate goals, rather than being representatives of particular constituent interest groups.

  The board normally prepares statements of corporate intent (SCIs) for approval by the responsible minister(s) — these specify objectives, undertakings, activities and financial and non-financial targets by which the performance of the board's management of the GTE can be judged.

4.3 Government ownership — and the public interest

There is an inherent tension in the corporatisation model.

On the one hand, GTEs have been corporatised, as a step beyond commercialisation, to enable them to operate as if they were private sector businesses. This is to bring to their operations the efficiencies spurred by a commercial imperative, competition (where it exists), an expert and accountable board and, for the most part, the incentives and sanctions which apply to their private sector counterparts.

On the other hand, government ownership brings with it ministerial political and policy intervention, whole-of-government policies, the stewardship of public funds and assets, and protection from bankruptcy. In essence, governments have decided that there is a 'public interest' that warrants ongoing ownership of the enterprise, rather than proceeding with privatisation.

This tension can be addressed, though never fully resolved, by establishing sound governance procedures and by clearly defining the non-commercial objectives and their weightings relative to commercial objectives. Without such clarification it is not possible to assess whether the corporatisation model is the best way of promoting the public interest.

Contextual differences between public and private corporations

The overriding objective of private sector businesses is to maximise the long-term value of their owners' (the shareholders) investment. Nevertheless, private sector businesses do accept social responsibility where this is consistent with that principal objective (even, potentially, at the expense of short-term profitability).

Private businesses are subject to laws and regulations designed to ensure the public interest is protected. For GTEs, voting shareholder minister(s) may also impose public interest requirements through ownership controls.

Ministerial understanding of the public interest is influenced by the values and policy platforms of their political party. This can become evident in a range of matters, from the selection of board members to the sponsorship of particular community activities. Ministers might also wish to influence decisions that could be politically 'contentious'. While boards should address commercial risk as part of their internal governance, the management of political risk should remain a matter for ministers.

Ministers can be expected to take a whole-of-government perspective on what constitutes the public interest when making decisions on issues such as GTE dividend policies, CSOs, terms of employment and industrial policies. This can range from decisions on balance sheet restructuring and special dividends, that assist the annual budget of the government, to deciding that GTE staff should be subject to particular terms and conditions of employment.

As GTEs have stewardship of public monies, and particularly because the community 'owners' are unable to withdraw their capital, the parliament, auditors-general, media and the broader community question how efficiently and effectively those monies are being spent. Accordingly, GTEs are subjected to different operational accountability than the private sector.

There is also likely to be differences in the approach to commercial risk, particularly in high risk-reward activities. These differences arise because:

- governments are constrained in the extent to which they can align the material incentives of board members to those of the public owners; and
- control of public rather than private funds and assets potentially affects the incentive for wealth creation.

These different incentives can promote increased or reduced levels of risk aversion. Although stewardship of public funds can lead to conservatism, implicit government guarantees for borrowings, or the ability to borrow at a lower cost than the private sector, can increase risk taking.

Unlike in the private sector, the threat of bankruptcy or takeover does not act as a discipline on the good governance of GTEs. Factor and final market disciplines are muted. Governments have endeavoured to replicate capital market disciplines by requiring GTEs to be profitable as well as to pay dividends, taxes and debt guarantee fees. However, failure to meet these disciplines does not have the same consequences as those facing private enterprise in a competitive market. Indeed, governments have clearly been prepared to accept rates of return that would be unsustainable under commercial market conditions.

4.4 How can external governance be improved?

The remainder of this chapter summarises the deficiencies in external governance identified by the Commission in the two previous monitoring reports. It contains suggestions on how these deficiencies may be addressed to make implementation consistent with corporatisation best practice principles as espoused by governments. This includes discussion on defining the public interest, objective setting, appointment of GTE boards, ministerial directions, dividend setting and performance reporting.

International GTE governance reform

Recent OECD (2005) guidelines on corporate governance for state-owned enterprises, which cover both external and internal governance arrangements, provide some assurance that current Australian arrangements are reasonably sound in principle, if not entirely in practice. These guidelines also lend support for a renewed commitment to rigorous governance arrangements. The principles that apply specifically to external governance are listed in box 1.

One area where the OECD has proposed different arrangements is the establishment of an entity within government to undertake the external governance role currently performed by ministers in Australia. The OECD's view is that such an entity is less likely to interfere with the operations of a public corporation for political purposes than would a minister. Under the Australian model, the main safeguard against such interference is through transparency measures, such as the legislative requirement for publication of directions to the board.

The relative strength of the Australian model is that ministers are more accountable for their governance of GTEs on behalf of the community than would be an independent entity. If the entity reports to a minister, it is in effect another layer of bureaucracy. Moreover, the OECD makes the implicit assumption that the perceived advantage of this arrangement outweighs the cost of altered accountabilities and incentives.

In the Commission's view, the pathway to strengthening safeguards is to achieve a clear distinction between external and internal governance, to clarify and make all objectives (both commercial and other public interest) more transparent, to make boards as independent as possible and to enhance accountability generally.

Defining the public interest

A clear definition of the public interest reasons for government ownership, and consequent ministerial control, is crucial for sound GTE governance. For ministers to be held accountable, their actions should be open and transparent. The public should be confident that the public interest has been defined, is widely known and is being served.

Finn (1993) suggests that ministerial responsibility to act in the public interest is legally established in rulings by members of the High Court. For example, Mason CJ in *Australian Capital Television Pty Ltd v Commonwealth of Australia* (1992, 177 CLR 106), stated:

> The very concept of representative government and representative democracy signifies government by the people through their representatives. Translated into constitutional terms, it denotes that the sovereign power which resides in the people is exercised on their behalf by their representatives.

Box 1 **OECD guidelines on corporate governance of state-owned enterprises**

The OECD Working Group on Privatisation and Corporate Governance of State-Owned Assets has developed a set of non-binding guidelines and best practices on corporate governance of state-owned enterprises. The guidelines were formally adopted by the OECD in April 2005.

Some of the major guidelines relating to external governance are:

- clear separation of ownership and regulation;
- the state should clarify and prioritise its main objectives, give indications about how it intends to achieve these and clarify how it will resolve the inherent trade-offs;
- the exercise of ownership rights should be clearly identified within government, perhaps by setting up a coordinating entity or, more appropriately, by the centralisation in a single entity of the ownership function (this entity being independent or under the control of one ministry);
- boards should be comprised of members with relevant competence and experience, nominated through a transparent process;
- the government should not be involved in the day-to-day management of enterprises and should allow full operational autonomy to achieve defined objectives, with any direction by the ownership entity publicly disclosed;
- a clear statement on company objectives should be publicly available, as well as a report on the fulfilment of those objectives;
- when the enterprise is used for policy purposes, such as service obligations, it should report on how these are being achieved;
- chairpersons should have relevant competencies and be separate from the CEO;
- boards should have the power to appoint and remove the CEO; and
- boards should carry out an annual evaluation to appraise their performance.

Source: OECD (2005).

A recent UK report on regulation from the House of Lords found:

> Responsibility for environmental and social standards should normally remain with Ministers as the authority of a democratic mandate is required for decisions in these areas (Select Committee on the Constitution 2004).

Judgements about welfare outcomes, efficiency and other matters within the purview of the public interest are more properly made if information is available about public preferences. In relation to GTE services, however, there are limited avenues for preferences to be revealed. Typically, there are no alternative service providers to switch to, and there may be limited substitutes for some services. Prices may not reflect willingness to pay. Further,

the costs (and benefits) of externalities, while important to assessing the public interest, may be difficult to measure and internalise through prices.

Ministers, as elected representatives, have responsibility for resolving the inevitable trade-offs between conflicting commercial and other public interest objectives. Holding ministers accountable for their performance in this regard requires transparent and unambiguous governance processes and substantive performance reporting. It is also important that there is clarity of vision and agreement across all arms of government about the objectives to be pursued by GTEs.

A requirement for ministers to publicly provide reasons for their decisions would improve the transparency and accountability of these decisions. It could also improve the quality of the decisions and reduce the possibility that preferences of minority interests or political considerations were given undue weight. In some instances, public consultation may be appropriate prior to ministerial decision making.

There can be limits on the accountability for ministers through difficulties in obtaining a clear public view on what will maximise community wellbeing. Further, even where the public is widely dissatisfied with ministers regarding the objectives of particular GTEs, accountability through the ballot box is likely to be weak because election outcomes are usually determined by broader government policies and performance.

Ministers should not be held accountable for the actual performance of the GTE itself. This is a board responsibility (differentiating the GTE model from the departmental model). However, ministers may ultimately be seen as responsible for failures of a GTE if the external governance processes were inadequate or unsound, or if they failed to act after becoming aware of problems with the governance of the board.

In the event of a significant failure of an essential service, it is probable that governments would be held responsible regardless of governance arrangements. In cases of extreme failure, the public might even hold the government accountable irrespective of whether an essential service is in public or private ownership.

Attribution of responsibility for safeguarding the public interest is made more difficult where boards and ministers are jointly involved in drafting and approving SCIs. Increasingly, regulators and supervisory bureaucracies are also becoming involved, further diffusing responsibility. For example, various regulatory acts require regulators to make an assessment of the public interest. Further, there is increasing reliance on quasi-regulation such as licensing agreements and memoranda of understanding.

Objective setting and dealing with conflicting objectives

The various levels of GTE objectives can be summarised as:

- *Guiding principles*: objectives set out in corporatisation acts to guide boards in their strategic planning.
- *High level objectives*: objectives contained in SCI in the form of goals which support mission statements. They are generally not directly measurable.
- *Performance indicators and targets*: objectives contained in the SCI and corporate plans that are generally subordinate to higher level objectives. They must be achieved if their antecedent objective(s) are to be met. They are more specific and more likely to be measurable than higher level objectives (PC 2003).

Guiding principles

Corporatisation legislation typically provides only broad guidance on the types of objectives that should be set, such as requiring that there be objectives relating to a GTE's commercial operations. Further, there is generally limited guidance as to the relative importance to be given to commercial objectives when they conflict with, or are modified by, non-commercial objectives. There is usually no guidance on the relative weighting of each. For example, under its act the Western Australian Water Corporation must set objectives on continuity of supply, maintenance of assets to ensure proper water provision and optimisation of customer satisfaction.

One apparent exception is Sydney Water, which is required to give equal weight to three objectives relating to financial outcomes, environmental protection and public health. Even in this case, however, guidance is limited because public health and environmental outcomes cannot be measured on a simple interval scale in the same way as profit.

Ministers bring to the objective setting process their responsibility to act in the public interest. However, as the reasons for the determination of objectives are not published in any Australian jurisdiction, there is no transparency as to how the public interest is identified, what it constitutes and how it relates to the objectives of GTEs.

There is a strong case for governments to make public their rationale for ongoing public ownership of each GTE, including a statement of the perceived public interest benefit, the objectives to be pursued through ownership and the prioritisation or weighting of particular commercial or other public interest outcomes.

High level objectives

Specific GTE objectives and goals are established within the SCI framework. SCIs are generally tabled in parliament and, in Queensland, must be included in annual reports.

The benefit of comprehensive SCIs is that the information they contain facilitates accountability. Their usefulness is reduced, however, where they have poorly defined objectives and performance targets, which (based on those examined by the Commission) appears to be the case.

Under current governance arrangements it is difficult to determine the extent of ministerial involvement in shaping SCI objectives. Generally, boards submit their SCI to ministers before the start of each financial year. The minister can then ask the board to reconsider some aspects of the statement. In South Australia, the process is reversed, with the minister preparing the SCI for the board after a period of consultation with the board. Typically, ministers may then direct the board to modify their objectives if the draft has not been agreed one month before the beginning of the financial year.

In addition to formal consultation processes, ministers and staff can interact informally with the board. As these informal interactions may not be open to public scrutiny, the effectiveness of the process cannot be observed and the participants cannot be held directly accountable.

Measurable objectives contribute to greater clarity of purpose and accountability. The most effective way of making objectives measurable is to define them in terms of outcomes. Examples of quantifiable outcomes have included ‘maintain an accident free workplace’ and ‘be profitable and maximise long-term value’. However, at least half of the current objectives reviewed by the Commission were expressed in a non-measurable or ambiguous manner, or as outputs or inputs (PC 2003).

The public availability of a timely, informative, ministerially agreed SCI that includes objectives expressed in terms of target outcomes would strengthen ministerial accountability.

Performance indicators and targets

Performance indicators are widely used in SCIs and, in some cases, a number of indicators relate to the same high level objective. In most SCIs, however, objectives and performance indicators are not themselves linked. Where they are linked, their relevance is not always clear.

Where objectives are ambiguous (for example, 'to improve financial performance while … meeting community and environmental responsibilities'), it is difficult to establish meaningful subordinate performance indicators other than for component parts of the objective. Moreover, the use of performance indicators relating to ambiguous objectives can lead to perverse outcomes if those indicators are poorly designed. For example, performance indicators focused on a GTE's short-term financial performance could undermine the long-term value of the enterprise.

Performance monitoring, as a form of reporting, is discussed in greater detail later in this chapter.

Appointment of boards

The responsibilities of GTE boards are broadly outlined in corporatisation acts. Typically, the board is responsible for managing the GTE in accordance with the processes, objectives and performance targets contained in the SCI. A common responsibility is to ensure that the GTE's functions are performed in an efficient and effective manner, consistent with commercial principles. Board members are also subject to a fiduciary duty responsibility under common law to act in good faith in the best interests of the corporation and for a proper purpose.

Ideally, boards would act independently in their internal governance. Any lack of board independence from government potentially reduces ministerial and board accountability for their respective external and internal governance responsibilities. However, as GTE board members are appointed by shareholding ministers, there is scope for governments to facilitate compliance through political patronage. Even where no direct ministerial directions are given to board members, there are opportunities for informal communications (Whincop 2005). It is also possible that board members might believe that they are to pursue particular objectives of the government, even in the absence of informal directives.

A related potential problem is departmental or ministerial staff issuing directions to boards, possibly without ministerial knowledge or authority. Protocols should be established to ensure that such third parties do not exert influence on GTE governance.

Recent amendments in Tasmania allow boards to nominate candidates for directorship positions, based on the board's identification of any skill or knowledge deficiencies within the existing board. The final decision regarding appointments remains with ministers.

The issue of appointing public sector boards was investigated by the Nolan Committee (COSIPL 1995) appointed by the UK Parliament. The recommendations of the Committee were adopted in full by the UK government, including the creation of an Office of the Commissioner for Public Appointments to monitor appointments to boards. Other major Nolan Committee recommendations included:

- ultimate responsibility for appointments should remain with ministers;
- appointments should be guided by the overriding principle of appointment on merit;
- merit selection procedures should take account of the balance of skills and backgrounds required, and these should be clearly specified;
- the basis on which members are appointed and how they are expected to fulfil their role should be made explicit; and
- candidates for appointment should be required to declare any significant political activity which they have undertaken in the past five years.

The recommendations of the Nolan Committee potentially provide a basis for improving current procedures of appointing board members.

An issue sometimes raised about GTE boards is that they lack the knowledge or experience of their private sector counterparts. It is argued that unless governments are able to attract the same calibre of directors as the private sector, good internal governance is potentially compromised.

One way of addressing this would be for governments to ease constraints on remuneration levels for GTE boards so that they are competitive with private sector remuneration. However, there currently appears to be little public acceptance of paying private sector levels of remuneration to GTE board members. Indeed, this might be seen as a contradiction almost inherent in the GTE model — that between the government acting as owner of a commercial enterprise and as custodian of public funds. This is not withstanding that the cost of internal governance failure is very high.

In any case, it is evident that, even with current rates of remuneration for GTE directors, many adequately qualified candidates make themselves available for directorships.

To improve board member performance, the Audit Office of New South Wales has recommended that they be provided with training on their roles and responsibilities, the environment in which the board operates and on the impact of legislation affecting the agency (AONSW 1998). This would represent a sound step.

Ministerial directions

Responsible ministers of all monitored GTEs have the power to direct boards, although there may be restrictions. For example, directions are sometimes confined to non-commercial objectives or they may need to be based on public interest criteria. Where more than one minister has responsibility for a GTE, the power to give specific types of directions is often restricted to one of those ministers. In some jurisdictions, notably Queensland and the Northern Territory, ministers are required to consult with boards before issuing directions. For one quarter of monitored GTEs, there are no restrictions on ministerial directions.

Around 80 per cent of monitored GTEs are required to publicly report ministerial directions. Over half are required to publish them in the government gazette and two thirds of these are also required to report them to parliament in their annual report. In some cases, for example in South Australia, these public disclosure requirements may be overridden if disclosure is considered detrimental to the GTE's commercial interests; to represent a breach of a duty of confidence; or to potentially prejudice an investigation. Such override provisions need very clear criteria to ensure the transparency of the minister–GTE relationship.

For the 80 per cent of GTEs with public disclosure, it appears that formal ministerial directions are rare. For example, ministers have only made three disclosed directions under the *State Owned Corporations Act 1989* (New South Wales) since 1995. Directions to pay special dividends are required to be made public for around 50 per cent of monitored GTEs, and rarely have such public instructions been given.

One possible interpretation of this limited number of formal directions is that ministerial wishes are being relayed to the boards in an informal, non-transparent manner.

Funding community service obligations

Historically, governments have recognised the broader public benefits of non-commercial functions undertaken by GTEs by funding their operating deficits. Current government policy, but not necessarily practice, is generally to recognise the costs of providing the CSOs and to make corresponding payments from the budget. For example, public transport providers would be 'compensated' for the need to provide concession fares to students or pensioners. In 2003-04, monitored GTEs received almost $3 billion in disclosed CSO payments. In some cases, CSO funding was not disclosed by GTEs. In other cases, GTEs provided CSOs without reimbursement, involving transfers, and potentially cross subsidies, between GTE customers.

A stricter adherence to explicit on-budget funding for CSOs by governments would improve external governance because it would promote the recognition, clarification and funding of the economic and social benefits to the community provided by the GTEs over and above the direct benefits of their goods and services as paid for by consumers. It would subject them to annual scrutiny to ensure programs are appropriate, cost effective and reflective of government priorities (Humphry 1997).

In their submission to the Commission's recent NCP inquiry, the Energy Retailers Association of Australia saw an increased role for CSOs to remove consideration of equity issues from price regulation:

> The ERAA recognises that governments may wish to pursue social equity and/or affordability issues. To the extent that governments identify these issues, they should be addressed not through price controls which inhibit competition, but through direct and transparent government payments (ERAA 2004 p.5).

Although accountability is best served where CSO arrangements are rigorously costed, made transparent, monitored and reported against (IC 1997), there is little evidence that this is presently occurring (see PC 2002a). Once it is determined that a particular CSO is justified, it should be included in the SCI and the performance of the GTE in meeting the CSO would ideally be monitored and publicly reported.

Humphry (1997) has recommended that CSOs should be fully funded at avoidable cost to ensure they did not adversely affect the financial performance of the GTE. Avoidable cost represents the cost burden that would be avoided if the organisation were not required to provide the CSO (excluding any common costs that would have been incurred anyway).

Determination of dividends

Responsible ministers are typically required to agree to (and have the power to amend) a dividend amount proposed by the board according to a policy developed by the Treasurer. The dividend may be specified in the SCI. In some cases, as noted earlier, ministers can demand a special dividend.

Statutory limits on dividends that can be paid apply in some jurisdictions. In Tasmania, for example, ordinary dividends are limited to 100 per cent of current year after-tax profit. This cap is relatively high, and yet dividends sometimes exceed 100 per cent of the after-tax operating profit in other jurisdictions.

The ability of ministers to effectively determine the level of ordinary and special dividends potentially limits the capacity of GTE boards to plan for the use of retained earnings for

future investment and capital replacement (particularly if combined with restrictions on GTE borrowing). If the efficient management of assets is impeded or investment curtailed, inadequate provision of services and higher costs could result, particularly in future years.

Transparency and accountability would be enhanced if GTEs included future investment intentions in their corporate plans and if these plans were publicly available. The public would then be better placed to make judgements about whether dividend payments to governments were consistent with each GTE's disclosed investment intentions and growth potential.

To be consistent with the private sector, the initial recommendation of the size of dividends and assessment of the capacity to pay should be an internal governance responsibility of the board. While it would be appropriate for ministers, as representatives of the owners, to have the power to override this recommendation, they should be required to publicly provide reasons for doing so.

Shareholding ministers also have a role in ensuring that, over time, dividends provide a reasonable return on public funds and assets. To this end, pre-agreed dividend policies would improve the transparency of, and accountability for, both external and internal governance, and reduce the degree to which GTE dividends could be caught up in annual whole-of-government budget decisions.

Board responsibilities

Statutory limitations on the board's authority apply in some jurisdictions. These relate to the setting of charges; the acquisition, use and disposal of assets; borrowing or investing; and staffing and remuneration.

Boards typically set prices subject to ministerial approval, or via planning documents such as the SCI. Broad limits are sometimes placed on board authority to set prices due to requirements to meet or balance a range of commercial or non-commercial objectives. In some cases, statutory limitations apply on the board's ability to set prices, while prices for around one third of monitored GTEs are determined by independent pricing regulators.

Some boards are limited in their power to acquire or dispose of assets, both in terms of the size of transactions and the location of activities. In some cases (for example, Tasmania), the transaction cannot take place unless it is approved by parliament. All corporatisation acts require ministerial approval to enter into joint ventures or to form subsidiaries.

Arrangements for GTE borrowing and investing are typically the same as for other government agencies, whereby the Treasurer is required to approve broad borrowing and

investment limits and risk management processes. An outline of borrowing and investing intentions is also usually required to be included in planning documents such as the SCI.

The accountability of the board for overall performance is diminished where limitations are placed on board authority (AONSW 1997). For example, it is difficult to hold board members fully accountable for a GTE's rate of return on their assets if the GTE is forced to set charges at levels barely covering costs. Similarly, limitations on borrowing or investing can impact on a GTE's capital expenditure program, and ultimately on future costs or the reliability and quality of the service provided.

GTE boards are generally given broad discretion over the terms and conditions of employment of their staff. A limited number of GTEs are subject to whole-of-government employment terms and conditions applying to general public service appointments. Such public sector limitations might lead to difficulties in attracting senior management as experienced or well trained as their private sector counterparts. As with board remuneration, this could have the effect of compromising best practice internal governance and performance.

Chief Executive Officer (CEO) authority

The CEO is generally responsible for implementing the board's strategy and specific directions, as well as managing the GTE's day-to-day operations.

Generally, ministers have at least some involvement in the selection and appointment of the CEO. For around half of all monitored GTEs, the CEO is effectively appointed by the responsible minister, usually after consultation with the board and, in jurisdictions such as Queensland, on the recommendation of the board. Where ministers have power to appoint or approve CEOs, they usually have the equivalent capacity to dismiss CEOs.

Around one third of GTEs have CEOs appointed by the board, although ministerial approval is generally required. For the few remaining GTEs, boards have the power to appoint CEOs without requiring ministerial approval.

Ministerial involvement in appointing or setting the terms of employment for a CEO may blur the lines of responsibility and diminish the board's accountability for performance (AONSW 1997). Potentially, it can compromise the board's ability to govern effectively where the CEO does not share the same vision. A clear delineation between external and internal governance would be achieved where the CEO was appointed by, and accountable only to, the board.

Reporting

External reporting by GTEs increases transparency by enabling their performance to be scrutinised. External reporting includes corporate plans, SCIs, annual operational and financial reports and associated statements, *ad hoc* reporting to ministers and special reports. Some of these reports remain confidential between ministers and GTE management.

The timing and nature of reporting vary by jurisdiction, sector and corporate status. All company GTEs are subject to the reporting requirements of Corporations Law, although some jurisdictions prescribe the provision of additional information such as corporate plans or reports to ministers.

There are three broad forms of accountability:

- *ex ante accountability* — for significant policy or resource decisions;
- *process accountability* — for the implementation of policies and the resources being used; and
- *ex post accountability* — for outcomes (Bottomley 2000).

Reporting by a board to the shareholding minister enables the minister to verify that the board is operating in accordance with the agreed objectives in the corporate plan and SCI. However, the effectiveness of this reporting depends on how well the information enables ministers to hold GTE boards to account. This, in turn, is heavily dependent on whether objectives and targets are measurable and defined in terms of outcomes.

Transparency is central to effective accountability, and is particularly important where there is a potential conflict of interest. This comes to the fore, for instance, when governments consider whether ministers' formal instructions to boards should remain confidential, or whether they should be published. It is important for reported information to be timely, relevant and of a high standard.

The provision of information also imposes costs on GTEs, both in terms of time and resources required for preparing reports. Consequently, there is the need to achieve the right balance between the costs and benefits of disclosure.

Annual and interim reports

The primary accountability document available to the public is the annual report, which summarises operating achievements and financial results for each financial year. Many GTEs must report formal ministerial directions in annual reports or directly to parliament.

The degree and nature of reporting can be influenced by: the status of the entity; corporatisation acts or other enabling legislation; whether there are memoranda of understanding requiring reporting; financial management and auditing legislation; instructions from the Treasurer; government policy; exemptions from reporting requirements and government ownership levels (among other factors). The quality of annual reports will vary according to the entity's ability to convey timely and relevant information.

Many GTEs are required to produce interim reports to ministers throughout the year. These typically include interim financial statements, information on capital expenditure and operational reports. These reports are not generally made public.

The contents of both annual and interim reports relate to the objectives established in the SCI, which is intended to be a planning and accountability document specifying outcomes in the year, or years, ahead. The benefit of robust SCIs is that they provide information for *ex ante* accountability. The poor quality of many SCIs has been discussed earlier.

Corporate plans

Most GTEs are required to produce a detailed corporate plan for the next three to five years. Corporatisation acts provide guidance on the content of corporate plans. Generally, the minister has discretion to negotiate and approve the plan.

The corporate plan is viewed as an accountability document between the board and the minister and is not generally tabled in parliament. Justification for such confidentiality is often on the basis of the commercial sensitivity of information provided to the minister, although this reduces *ex ante* accountability for GTE board performance and ministerial governance.

While there may be legitimate confidentiality concerns surrounding the detailed strategic business directions of GTEs, such concerns should not apply to publishing ministerially agreed higher level GTE objectives, and these should be made public.

Ad hoc reports

Ministers typically have extensive powers to request any information that they require, which means GTEs might be compelled to produce *ad hoc* reports on any operational or politically important matter. Boards are also required to keep ministers informed of emerging strategic issues and changes in operating environments.

Some GTEs are also obliged to provide specific non-financial information under their operating licences or enabling legislation. For example, the Sydney Catchment Authority is obliged to share information with some regulatory agencies and to furnish reports to ministers for presentation to parliament.

Other mechanisms by which GTE performance is publicly reported include parliamentary committee processes, especially in Tasmania, and via regulatory reviews (for example, in New South Wales by the Independent Pricing and Regulatory Tribunal).

Information in *ad hoc* reports is often very revealing, but these reports do not represent a systematic accountability mechanism.

Performance monitoring

Performance monitoring provides a means for evaluating performance against objectives and targets, both over time and against the performance of comparable entities. It represents a potentially powerful accountability mechanism as it can enable customers and the community to assess how efficiently and effectively GTEs are using resources in the production of goods and services. Ultimately, it allows parliament to assess the efficacy of government policies and corporatisation strategies.

Accordingly, there are advantages in adopting outcome rather than output, input or process measures as they relate more directly to the high level objectives. Where outcomes are difficult to measure, it is important to report outputs and inputs and explain their relationship with the intended outcomes.

The major challenge in performance monitoring of GTEs is to determine appropriate measures. The Victorian Essential Services Commission (ESC) (2004) has outlined the following key principles:

- performance indicators need to be relevant to the nature of the services provided by each business;
- performance indicators need to be meaningful and relate to key issues of concern to both businesses and their customers;
- performance indicators need to be defined and collected on a consistent basis across businesses to provide a valid measure of actual performance and to aid reasonable comparisons;
- the costs associated with collecting information and data need to be balanced against the benefits of collecting that information;

- the accuracy and reliability of information provided by businesses must be verifiable; and
- it is desirable to identify whether there is scope for national consistency in reporting and comparison, to facilitate national assessment of relative performance.

All GTEs report partial financial performance measures, such as earnings before interest and taxation, which are simple to calculate, intuitive and easy to understand. On its own, any single one of these indicators represents only part of the financial story, and therefore might be misleading about the GTE's overall financial performance. GTEs, therefore, typically also report multiple partial measures. Multiple partial measures can, however, make gauging overall performance difficult to interpret, particularly if indicators move in opposite directions over time.

Increasingly, governments are setting complex financial objectives, such as 'shareholder value added' or 'total factor productivity' as they provide a more holistic impression of performance. However, the detail and complexity of data can impose significant compliance burdens and confound the usefulness of the measures.

There are particular problems associated with GTEs reporting on their non-financial objectives, with indicators typically being partial and reflective of a particular aspect of operation. Unlike financial measures, this information is rarely standardised across GTEs and measures are often reported without definitions or contextual information. Greater national harmonisation of these measures would assist in the comparative analysis of performance.

External performance monitoring

In most jurisdictions, treasuries and line departments monitor the performance of GTEs and inform ministers accordingly. In the Australian Government these functions are performed by the Department of Finance and Administration. Generally, a designated section of treasury has oversight of government-owned businesses and, apart from undertaking monitoring, develops governance policies and guidelines and provides advice on these.

Most GTEs are also subject to some regulatory supervision. The regulation of prices usually goes hand-in-hand with monitoring service quality levels, to ensure financial targets are not met through a reduction in service standards. Consequently, the publication of these regulator's reports exposes aspects of the GTEs' performance to scrutiny by customers, media and other stakeholders. However, as discussed later, the information provided is not comprehensive for the purpose of *ex post* accountability.

The ‘off budget’ status of GTEs has led to fewer opportunities for their operations to be subject to parliamentary questioning. The concept of ‘commercial in confidence’ has also further eroded parliamentary accountability. However in Tasmania, specific GTE scrutiny committees have operated since the mid-1990s, with transcripts and investigations published in Hansard and, on occasion, in anthology reports.

The Productivity Commission, the Bureau of Transport and Regional Economics and other bodies also assess aspects of GTE performance on an *ad hoc* basis, but are not part of the governance process. These reports can complement other sources of performance monitoring.

Performance monitoring ultimately relies on setting clear and measurable objectives and providing relevant, accurate and timely data. If performance monitoring is inadequate, ministers, boards and management cannot be held fully accountable for their decisions concerning the public interest, internal governance and operational performance respectively. Provision of sufficient resources to enable substantive performance monitoring is important.

Auditing

There are two main types of auditing of GTEs, namely financial and performance auditing. A third type — compliance auditing — is sometimes also conducted.

External financial auditing involves a third party review of financial reports to assess whether they are free from error or misrepresentation. Performance auditing provides an independent opinion on whether an entity’s activities have been carried out efficiently and effectively.

External auditing of GTEs is primarily undertaken by or on behalf of the auditor-general in each jurisdiction. Private companies appoint external auditors of their own choice.

Auditors-general are protected under their enabling acts of parliament from removal by the executive. This protection of independence stems from their role of assisting the parliament in holding the government accountable. Typically, auditors-general have a seven year tenure, although it can be until retirement.

Auditors-general have a broad measure of operational flexibility. In most jurisdictions they have a capacity to self-initiate work and are able to undertake performance audits.

Financial auditing

Financial auditing involves a review of financial statements and auditors must report on whether their opinion is qualified or unqualified. Financial reports are qualified when they fail to present a fair view of the entity's financial position or results. Auditors are not responsible for the detection of fraud or error, but an audit should provide reasonable assurance that financial reporting is free of material error or misrepresentation.

Currently, financial auditing of company GTEs must be undertaken by the auditor-general in all jurisdictions except in Tasmania and in the case of Snowy Hydro (which is jointly owned by the Australian, NSW and Victorian governments). In Tasmania, ministers can use any auditor, although government policy has been to use the auditor-general. Australian Government company GTEs, other than Telstra, are able to choose any auditor, although the auditor-general must still carry out an independent audit of their financial statements.

Performance auditing

A difference between public and private sector accountability is that auditors-general can conduct, and report publicly on, performance audits of government entities. In most jurisdictions performance audits have an outcome-based focus. For example, in New South Wales and Tasmania, performance audits are specifically aimed at determining whether activities are carried out economically, efficiently and effectively. In Queensland and the Northern Territory, auditors-general are restricted to audits of performance management systems.

In New South Wales, Victoria, Western Australia, Tasmania and the Australian Capital Territory, performance audits are undertaken solely at the auditor-general's discretion, and this is similarly true for the more narrowly defined audits in Queensland and the Northern Territory. In South Australia, the auditor-general can only undertake a performance audit in the course of an annual financial audit.

In Western Australia, statutory authorities are required to report performance indicators in their annual report and these are to be audited by the auditor-general each year to ensure their relevance and appropriateness. This institutionalises regular checks of the veracity of performance indicators by the auditor-general.

The only jurisdiction where the auditor-general cannot currently self-initiate performance audits of GTEs is the Australian Government. The Australian Auditor-General can only undertake a performance audit of a GTE at the request of a minister or the Joint Committee

for Public Accounts and Audit. For Australian Government authorities and companies other than GTEs (that is, those authorities and companies not prescribed as GTEs under the *Commonwealth Authorities and Companies Act 1997*), the Auditor-General is able to undertake performance audits at his or her discretion.

An area of tension regarding performance audits is that the distinction between policy objectives and their implementation is not always clear. It is generally accepted that policy formulation is strictly the responsibility of executive government (and legislation usually proscribes the auditor-general from directly questioning government policy objectives). However, governments and auditors-general have come into conflict when reports of performance audits have questioned whether governments are obtaining value for money and have therefore been seen as being critical of government policy.

There have been only a few performance audits relating solely to GTEs over the last five years, ranging from five in New South Wales to none in Western Australia, South Australia and Tasmania.

External governance implications

Financial and performance audits both have the potential to strengthen incentives for good GTE governance.

Financial auditing contributes to good governance through its assurance as to financial and other outcomes, but also provides the board with an incentive to report fully and accurately, so as to avoid an independent expert disclosing error.

Performance audits can be used constructively to improve the operations of an entity, and they can also act as an incentive for efficient and effective performance given that exposed deficiencies could reflect poorly on the board. Any such deficiencies could also be portrayed by some as evidence of poor ministerial stewardship.

Consideration could be given to removing restrictions on the ability of auditors-general to undertake performance audits in some jurisdictions. There is also a strong case for much greater use of performance audits, and in some cases it could be appropriate to perform them on a regular basis to ensure that the non-financial objectives of GTEs are being adequately met.

Auditors-general could strengthen incentives for good governance by undertaking independent audits of the efficacy of the non-financial performance measures employed by GTEs. Such audits are rare in most jurisdictions or do not take place at all.

Currently, much of the assessment of the efficiency of GTEs is undertaken by regulators. This is an indirect way of achieving performance reporting, and it will be of limited use if regulators do not comprehensively report on all aspects of performance. This applies equally to regulation of private sector entities.

Regulation

As part of the corporatisation reform, there has been a reliance on regulators or quasi-regulation (such as operating licenses or memoranda of understanding) to determine service quality and, in some cases, price. While the presence of independent regulators may be superior to having the government act as both regulator and owner of infrastructure providers, clearer external governance processes could allow for less reliance on regulation.

Regulation can incur high compliance costs and carries the potential for regulatory risk and regulatory error (see box 2). Regulatory interventions involve the use of imperfect instruments, devised under circumstances of asymmetric information and uncertainty (PC 2001c).

Box 2 **Price and service regulation issues**

Although regulation can assist in the efficient functioning of markets, this must be weighed up against the associated costs when determining the level of reliance governments may wish to place on regulation. Notable problems with regulation can include:

- significant administration and compliance costs for government and business, and potential for wasteful strategic behaviour;
- the prevention of efficient pricing and reduced incentives to invest;
- diminished incentives for organisations to cut costs;
- the imposition of excessive regulation or micro-management of businesses;
- bias or capture of the regulator;
- second guessing of consumer preferences and prescription of high standards of technology which may be unnecessary or not consistent with consumer preferences;
- being constrained by previous decisions (even where these decisions may have been wrong);
- undue emphasis on unlikely extreme events; and
- inconsistency over time, particularly following an adverse event.

Source: PC (2001b), Banks (2003) and the Select Committee on the Constitution (UK) (2004).

When making price determinations, regulators make judgements on matters such as the appropriateness of capital investment programs and about service quality. There is a risk that regulators will make overly prescriptive determinations of service quality that are better left to enterprises responding to consumer demand within a price–quality trade-off.

One particular problem emerges where GTEs — and private sector enterprises — are subject to regulatory price or revenue caps. The Commission has previously noted the potential trade-off between cheap services today and inadequate services tomorrow. While the setting of prices at too low a level may have little impact on current service levels because of the inherent resilience of network assets, it could deter future investment in new or replacement facilities (PC 2001b, Banks 2003).

The problem was recently recognised in a report by the Audit Office of New South Wales:

> … public enterprises are not earning enough to replace their assets. Their charges may have to increase or they may have difficulty maintaining services (AONSW 2004).

Similar problems emerge from the regulation of quality standards. For example, mandating service of a high standard may mean that it is not affordable to the entire population and that considerable resources may be required to meet the mandated standard. Given that decisions in setting guidelines or standards involve difficult judgements, it is important that those responsible act in the public interest and are fully accountable (PC 2000). Such decisions are traditionally, and should remain, the preserve of ministers.

4.5 Towards best practice

GTE performance is likely to be compromised where there are conflicting objectives, shared responsibilities and difficulties in measuring outcomes. At issue is whether these governance issues can be satisfactorily dealt with by improving current practice or whether undertaking more significant reform of the current corporatisation model is warranted.

A number of enterprises that were corporatised have subsequently been privatised. In part, the rationale for public ownership was seen to have diminished due to:

- technological developments that reduced the natural monopoly elements of many sectors;
- the increased maturity of private markets (where competitive markets had developed to provide some services);

- the development of regulatory frameworks to deal with natural monopolies;
- an increased capacity within government to design CSOs that could be delivered through contractual arrangements without governments actually owning enterprises;
- a belief by some governments that privatisation maximised the incentive for enterprises to become more efficient; and
- concern about government debt levels.

Notwithstanding the above considerations, the decision to privatise requires a clear understanding of the nature and relative importance of commercial and non-commercial objectives. Assuming governments consider that non-commercial objectives continue to serve a public interest, there are various mechanisms for their delivery within a private ownership framework, such as regulation or contracting. However, each can involve transactions costs, potentially offsetting some or all of the efficiency gain governments might otherwise anticipate from privatisation. Indeed, private monopoly provision of an essential service might on balance be no better than public monopoly.

Privatisation of GTEs is therefore likely to be predicated on finding satisfactory ways to ensure that core non-commercial objectives can be met by the private sector. Relevant considerations include:

- whether particular government objectives or customer needs could be met without ownership of a GTE;
- the consequences of disruption to an essential service;
- whether the presence of externalities represents an impediment to private sector provision of a good or service, or results in private sector provision being inadequate or inequitable;
- the ability of government to transfer accountability to the private sector;
- whether services could be purchased from the private sector at a lower cost and whether the required services could be adequately specified and enforced through a contractual arrangement;
- the need for taxpayers to accept market and other risks associated with owning businesses, and whether the level of risk involved with some projects (particularly sovereign risk) may preclude private sector participation;
- whether involvement in commercial activities distracts government from its core activities;
- whether CSOs could be effectively provided via contractual arrangements with the private sector (taking account of the transaction costs involved);

- whether competitive neutrality is threatened by government ownership, with managers of GTEs feeling more secure if they believe enterprises are effectively underwritten by governments, or because government enterprises may be able to borrow funds more cheaply because of government guarantees (or perceived guarantees); and

- whether there are conflict of interest concerns between governments as owners and regulators (NCoA 1996, Humphry 1997).

An alternative to both corporatisation and privatisation is to revert to a departmental or statutory authority model where the minister has direct control. It has greatest relevance where the public interest objectives significantly outweigh the commercial focus of the enterprise. While this may increase the accountability of ministers to parliament and the broader community, a return of direct ministerial control is likely to diminish the effectiveness of a commercial focus, and result in the loss of some of the efficiency gains from the GTE reform process.

Improving the current corporatisation model

The current GTE model (that is, corporatisation with external governance) has evolved essentially because:

- the departmental and statutory authority approaches in many instances did not deliver efficiencies of the kind that should occur for commercial activities; and
- in many cases, privatisation is not appropriate or warranted at this stage.

However, the corporatisation model has inherent tensions arising from commercial performance and other public interest objectives being pursued concurrently. Various systems of governance, as described above, have been developed by governments in Australia to address these tensions. These systems are comprised of a patchwork of arrangements, many of which fall short of best practice.

In view of the importance of GTEs to the Australian economy, governance reform has the potential to enhance economic performance and community wellbeing. By encouraging governments to clarify their policy objectives and the appropriate role of GTEs, there will be improvements to allocative efficiency — with the public interest and consumer preferences fully taken into account — and better decisions about ownership and appropriate governance models. By clarifying responsibilities and objectives, there will be improvements in the performance of boards, resulting in better customer service, investment decisions and asset management.

To fully obtain the potential benefits of GTE reform undertaken over the last 15 years or so, each jurisdiction should pursue improvements in governance arrangements for their GTEs, drawing on identified best practice.

The reform agenda should focus particularly on obtaining a clearer distinction between external and internal governance, with greater transparency and scrutiny of the external governance role played by ministers. The non-commercial public interest objectives of GTEs should be made explicit and weighed against commercial performance. Without clarification of the non-commercial objectives, it is not possible to assess whether the corporatisation model best achieves the public interest.

Other priorities in the reform agenda include:

- greater independence of GTE boards, with board members to be appointed solely on merit;
- a general strengthening of accountability, including the public availability of SCIs which express objectives as target outcomes;
- rigorous reporting of outcomes, with sufficient resources available for substantive performance reporting and for national harmonisation of that reporting; and
- appointment of CEOs by GTE boards to further reinforce the delineation between external and internal governance, with CEOs subsequently being accountable only to the board.

In reforming external governance arrangements, the commercial focus of GTEs should be maintained by ensuring that CSOs are fully funded from government budgets and that capital market disciplines are strictly maintained.

Clearer external governance processes could reduce the need for some specific regulation of individual GTEs. Regulation can incur high compliance costs and carries significant potential for error.

Finally, governments should be prepared to expose to public scrutiny their rationales for ongoing public ownership. This is important in clarifying the non-commercial objectives of GTEs.

PART B

5 Electricity

The financial performances of 21 electricity government trading enterprises (GTEs) are reported in this chapter. The GTEs vary significantly in their size and the range of generation, transmission and distribution services they provide.

In 2003-04, these GTEs generated $18 billion in revenue and controlled assets valued at $50 billion. The group also returned just over $2.2 billion to their respective owner-governments, through income tax-equivalent payments and dividends.

The majority (16) of the monitored GTEs operated in the National Electricity Market (NEM). The five monitored GTEs not currently operating in the NEM are based in Western Australia, Tasmania and the Northern Territory. Tasmania is due to enter the NEM in 2005.

The overall performance of the electricity sector is presented in table 5.4 at the end of this overview. This is followed by performance summaries for each GTE. For a discussion of the data, the financial indicators used and some of the factors that should be considered when assessing performance, see chapter 3.

5.1 Monitored GTEs

The types of activities undertaken by the individual electricity GTEs and their involvement in ancillary services should be taken into account when comparing financial performances.

The four principal activities carried out by electricity businesses are: generation of electricity; the transmission of electricity at high voltages; the distribution of electricity at low voltages; and the retailing of electricity to customers. Of the 21 GTEs monitored, eight solely generated electricity, three transmitted electricity, seven were distributors of electricity and provided retail services, and one traded in power from privately owned generators (see table 5.1).

Western Power (Western Australia) and Power and Water Corporation (Northern Territory) were the only fully integrated electricity utilities monitored — providing generation, transmission, distribution and retail services.

Table 5.1 **Activities — electricity GTEs, 2003-04**

Electricity GTE	*Jurisdiction*	*Activities*			
		Generation	Transmission	Distribution	Retail
Eraring Energy	NSW	✓	✗	✗	✗
Delta Electricity	NSW	✓	✗	✗	✗
Macquarie Generation	NSW	✓	✗	✗	✗
Transgrid	NSW	✗	✓	✗	✗
Australian Inland	NSW	✗	✗	✓	✓
Energy Australia	NSW	✗	✗	✓	✓
Integral Energy	NSW	✗	✗	✓	✓
Country Energy	NSW	✗	✗	✓	✓
CS Energy	Queensland	✓	✗	✗	✗
Stanwell Corporation	Queensland	✓	✗	✗	✗
Tarong Energy	Queensland	✓	✗	✗	✗
Enertrade	Queensland	✓ **a**	✗	✗	✗
Powerlink	Queensland	✗	✓	✗	✗
Ergon	Queensland	✗	✗	✓	✓
ENERGEX	Queensland	✗	✗	✓	✓
Western Power Corporation	WA	✓	✓	✓	✓
Hydro-Electric Corporation	Tasmania	✓	✗	✗	✓
Transend	Tasmania	✗	✓	✗	✗
Aurora	Tasmania	✗	✗	✓	✓
Power and Water Corporation	NT	✓	✓	✓	✓
Snowy Hydro	NSW, Victoria, Australian Government	✓	✗	✗	✗

a Enertrade trades power from privately-owned generators into the National Electricity Market.

In addition to providing generation, transmission, or distribution and retailing services, many electricity GTEs are involved in engineering consulting services. In 2003-04, seven of the monitored GTEs also supplied gas and two — Australian Inland, and Power and Water Corporation — were involved in supplying water.

The number of GTEs monitored has changed over the reporting period (see table 5.2). In 2003-04, the number of monitored GTEs remained the same as the previous year.

There are no electricity GTEs from Victoria or South Australia as the electricity supply is privatised in these states. In Victoria, the distribution GTEs were sold to the private sector during 1995-96. In March 1996, Yallourn Energy Limited, the generation GTE, was also sold. In South Australia, electricity GTEs were progressively restructured and their assets sold or transferred under long-term lease to the private sector in 1999 and 2000.

In the Australian Capital Territory, ACTEW Corporation Limited (ACTEW) is a government-owned holding company which contracts the provision of electricity to ActewAGL, a joint-venture with AGL — a private energy services company. Because most of ACTEW's assets and revenue are associated with the provision of water services, its financial performance is discussed in chapter 6.

Table 5.2 **Changes to monitored electricity GTEs, 1999-00 to 2003-04**

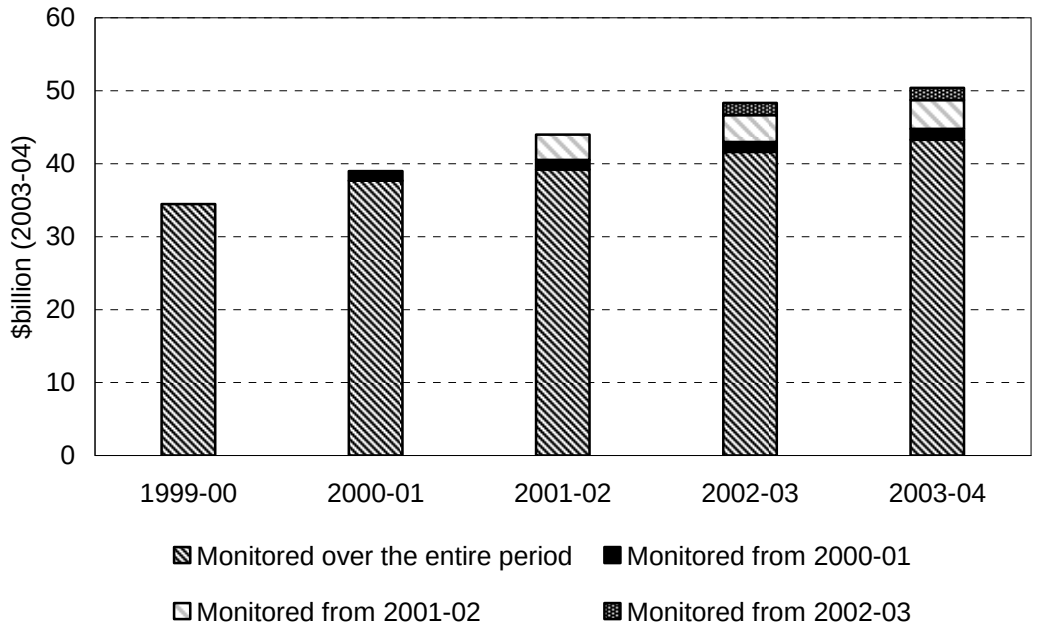
Period	*Number Monitored*	*Included*	*Excluded*
1999-00	22		
2000-01	23	Eraring Energy	
2001-02	21	Power and Water Authority, Country Energy[a]	Pacific Power, NorthPower, Advance Energy, Great Southern Energy
2002-03	21	Snowy Hydro	Snowy Mountain Hydro-Electric Authority
2003-04	21		

[a] Country Energy was formed from a merger of NorthPower, Advance Energy and Great Southern Energy.

Over the reporting period, the total asset base for all the monitored electricity GTEs has risen from $34 billion in 1999-00 to more than $50 billion in 2003-04. The inclusion of additional GTEs, added within the reporting period, accounted for approximately $7 billion of this $16 billion increase (see figure 5.1).

The asset base of distribution GTEs increased by $7 billion over the reporting period. More than $2 billion of this increase was due to the inclusion of Country Energy in 2001-02. The newly included GTEs also accounted for a significant proportion of the growth in the overall assets of generation GTEs ($6 billion).

Figure 5.1 **Sector assets — electricity GTEs**



Note The value of sector assets prior to 2003-04 was converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

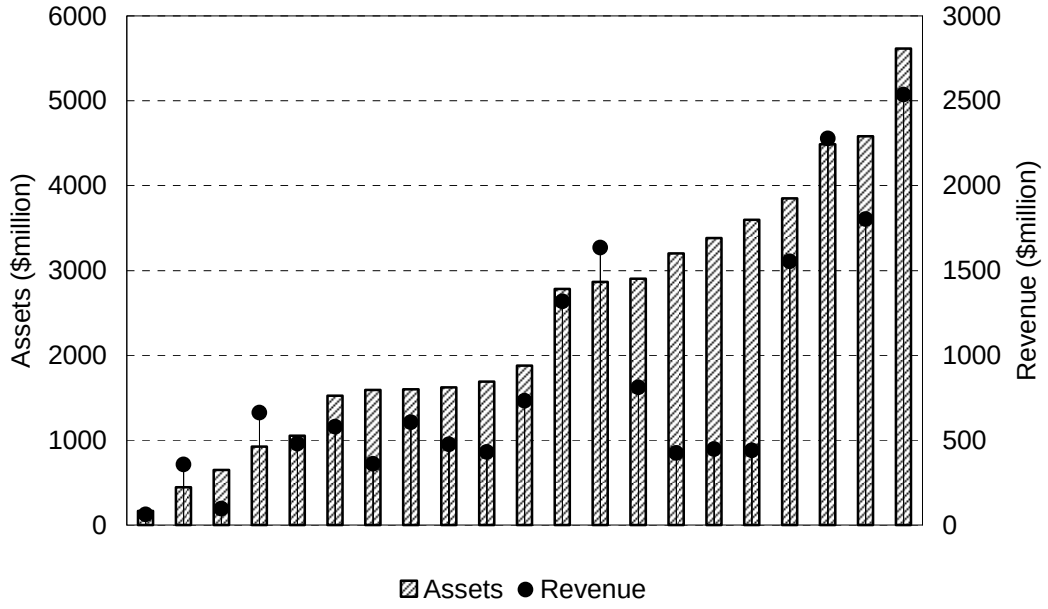
Source: Productivity Commission estimates.

The size of the monitored electricity GTEs, in terms of the value of the assets controlled and revenue, is quite varied (see figure 5.2). In 2003-04, the smallest in terms of asset value was Australian Inland ($164 million) and the largest was EnergyAustralia ($5.6 billion).

5.2 Market Environment

Governments have introduced reforms aimed at improving the efficiency and financial performances of electricity GTEs. Reforms have focused on the governance of GTEs, the efficiency of the production process and the competitiveness of market structures in which the GTEs operate. These reforms have implications for the financial performance of GTEs and the comparison of performances over time.

Figure 5.2 **Assets and revenue — electricity GTEs, 2003-04**



Source: Productivity Commission estimates.

The National Electricity Market

Over the reporting period, the most significant change to the market environment was the continued development of the NEM and the progressive introduction of choice of electricity supplier, beginning with larger customers and eventually extending to all customers (see table 5.3). The NEM is a wholesale market for the supply and purchase of electricity.

The National Electricity Market Management Company manages the NEM, in accordance with the National Electricity Code (the Code). The Code specifies the market arrangements that govern the operation of the wholesale market, such as system security requirements, rules for bids and dispatch of generating capacity, and metering standards. The NEM officially commenced operating in December 1998, although trade between the New South Wales and Victorian wholesale markets commenced in May 1997.

Table 5.3 **Timetable for retail competition — by jurisdiction**

Jurisdiction	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*	*2003*	*2004*
New South Wales	>40 GWh (July)	>4 GWh (April) >750 MWh (July)	>160 MWh (July)			>100 MWh (January) >40 MWh (July)	All customers (January)		
Victoria	>750 MWh (July)		>160 MWh (July)				All customers (January)		
Queensland		>40 GWh (March)	>4 GWh (October)	>200 MWh (July)					>100 MWh (July)
South Australia				>750 MWh (July)	>160 MWh (January)			All customers (January)	
Western Australia		>88GWh (July)	>44 GWh (July)		>9 GWh (January)	>2 GWh (July)		>300 MWh (January)	
Northern Territory					>4 GWh (April) >3 GWh (October)	>2 GWh (April)	>750 MWh (April)		
Australian Capital Territory		>20 GWh (October)	>4 GWh (March) >750 MWh (May) >160 MWh (July)			>100 MWh (January) >40 MWh (July)	All customers (January)		

Note 1000 KWh = 1 MWh, 1000 MWh = 1 GWh. Amounts refer to the minimum annual electricity a customer must consume to be eligible to choose their supplier.

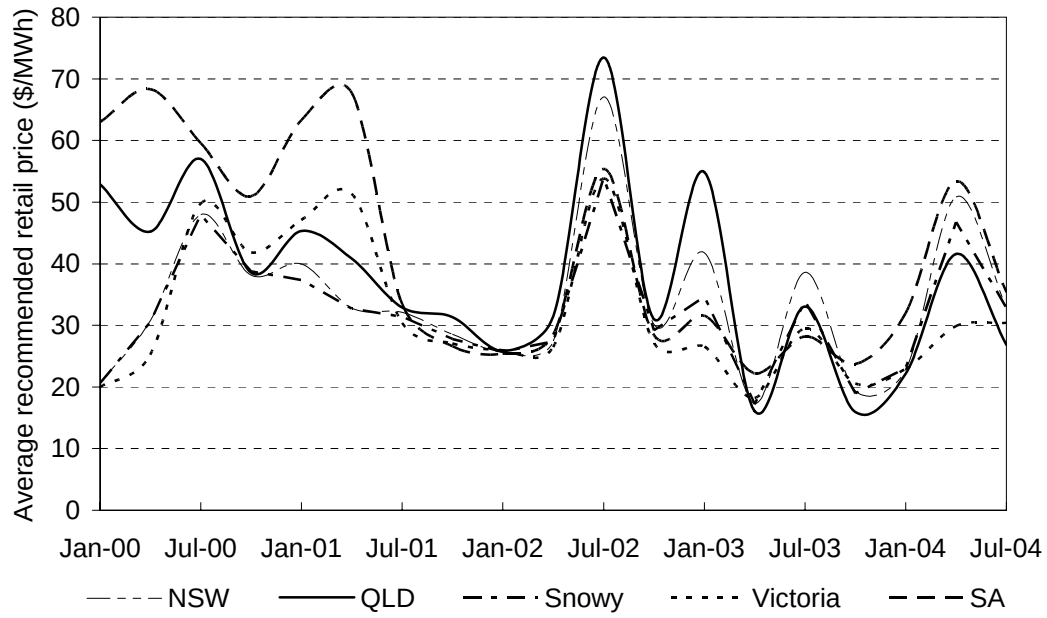
Source: Energex (2004), Power and Water (2004), Wester power (2004).

The development of the NEM has a number of implications for GTE performance. Most electricity retailer GTEs now face greater competition than they experienced in the past. Competition has also been facilitated in most jurisdictions by the adoption of the access provisions of the Code for distribution and transmission networks. These provisions give retailers and businesses purchasing wholesale electricity a right of access to these networks.

With the introduction of the NEM, electricity GTEs have had to come to terms with operating effectively in this new environment. There has been significant price volatility in some parts of the NEM, including price differences between sub-markets. However, these differences have lessened since a change in market rules in 2001-02 (see figure 5.3).

The price differentials in the NEM's five market regions are due to differences in generator cost structures, regional demand and the limits on arbitrage. Arbitrage is the purchase of a commodity (electricity) in one market for immediate resale in others in order to profit from unequal returns. The physical limitations of existing interconnectors and the costs associated with transmitting electricity over large distances (including the loss of electricity) limit arbitrage between regions in the NEM.

Figure 5.3 **Average prices — National Electricity Market**



Data source: NEMMCO (2005).

Although Western Australia and the Northern Territory are not party to the NEM, both jurisdictions have introduced (under commitments to National Competition Policy) choice in electricity supplier for large users of electricity. In addition, the *Electricity Corporation Act 1994* (WA) and *Electricity Networks (Third Party Access Act)* (NT) provide for third-party access to the respective electricity transmission network.[1]

In June 2003, the WA Government endorsed an electricity reform program based on the recommendations of the Electricity Reform Task Force (ERTF 2002). The reform program involved the disaggregation of Western Power into four separate entities — generation, networks, retail and regional power — and the establishment of a wholesale electricity market.

Price and environmental regulation

Most of the monitored electricity GTEs operate under some form of price regulation. In New South Wales, the Independent Pricing and Regulatory Tribunal (IPART) regulates distribution and electricity prices for small retail customers. Prices to customers who use more than 160 MWh per year are unregulated. IPART was also responsible for regulating the transmission network until July 1999, when this responsibility was transferred to the Australian Competition and Consumer Commission (ACCC).

In January 2001, the NSW Government commenced operation of the Electricity Tariff Equalisation Fund (ETEF) to reduce the market risk faced by retail suppliers of electricity (NSW Treasury 2000).[2] The ETEF is designed to offer regulatory price protection to retail customers (who purchase less than 160 MWh per annum), while ensuring that suppliers are not exposed to unacceptable financial risk. Essentially the ETEF operates to insulate New South Wales retailers and their customers from price movements in the NEM.[3]

1 Following the departure in 2001-02 of NT Power from the Northern Territory, Power and Water Corporation is the only supplier of electricity to the vast majority of Territorians.

2 COAG's Independent Review of Energy Market Directions (the Parer panel) released its final report on 20 December 2002, under the title 'Towards aTruly National and Efficient Energy Market'. Among other things, the review recommended that the NSW Government should abolish the ETEF. However, the NSW Government retained the ETEF for the suppliers of small, regulated retail customers (ACCC 2004, NSW Treasury 2005).

3 When the market price of electricity is higher than the strike rate — the energy cost component that retailers may recover from regulated customers — retailers withdraw the difference from the ETEF, enabling them to earn a commercial return whilst selling at the regulated tariff. If the market price is lower, then retailers pay the difference into the fund. If the fund slips into deficit, then NSW government-owned generators pay into the fund, ensuring it is always in balance.

In Queensland, prices for non-contestable customers are set by the Minister responsible for Energy. The Treasurer was responsible for regulating the prices charged for use of the transmission network, until the ACCC took over this responsibility in January 2002. The Queensland Competition Authority has had responsibility for distribution network prices since December 2000.

In June 1999, Queensland introduced the Benchmark Pricing Agreement (BPA). The BPA is a negotiation between the Queensland Treasury and the Queensland retail GTEs — Energex and Ergon. Under a BPA, a retailer will receive a negotiated payment (CSO) if the regulated revenue they receive from non-contestable customers is less than the cost of their energy purchases. If this revenue exceeds expenses, then the GTE must pay a franchise surplus (or negative CSO) to the Queensland Treasury.

In Tasmania, the Office of the Tasmanian Electricity Regulator sets maximum charges for the sale and supply of electricity services, including charges for distribution and retail supply.

In the Northern Territory, retail prices for non-contestable customers are set by the Government. The Utilities Commission sets the maximum allowable revenue that Power and Water Corporation can earn from network access tariffs and charges.

On 8 December 2000, the Commonwealth Parliament passed the *Renewable Energy (Electricity) Act 2000*, which established a 2 per cent renewable energy target for electricity supply in Australia. From 1 April 2001, energy wholesalers have had to purchase increasing amounts of electricity generated from renewable sources. Most electricity generation GTEs are pursuing investment opportunities, including wind and solar power, to meet this target and also to satisfy consumer demand for 'green' energy.

The Australian Ministerial Council on Energy recently created a new Australian energy regulatory framework. The framework, comprising an Australian Energy Market Commission and an Australian Energy Regulator, will replace the current state-based system with nationally consistent regulation. The Australian Energy Market Commission will be the rule-maker for the wholesale electricity market and, in the future, will also take responsibility for the National Gas Code. The Australian Energy Regulator, which is planned to begin operations in late 2005, will have responsibility for the regulation of electricity and gas wholesale transmission networks, and will eventually regulate distribution and retailing.[4]

4 This is consistent with CoAG's Independent Review of Energy Market Directions 2002 recommendation that a National Energy Regulator be established to encompass the energy

Structural reform

The Australian electricity supply industry originally developed on a state-by-state basis, with vertically integrated, government-owned utilities. The major driver for structural reform in the electricity industry during the 1990s was a series of inter-governmental agreements, culminating in the National Competition Policy (NCP) agreements, aimed at establishing the competitive NEM.[5] The intention behind structural change within the electricity supply industry was to introduce competition in the generation and retail sectors by separating these competitive elements from the natural monopoly elements of transmission and distribution.[6]

In New South Wales, Pacific Power was restructured on 1 February 1995 into a transmission network and three generator businesses. Pacific Power's transmission activities were transferred to TransGrid and six of Pacific Power's power stations were transferred to two new generators — Delta Electricity and Macquarie Generation. On 2 August 2000, the remaining generation assets of Pacific Power were transferred to a new generation company, Eraring Energy.

New South Wales' 25 existing electricity distributors were amalgamated in October 1995, to form six new distribution businesses — Integral Energy, Advance Energy, Great Southern Energy, NorthPower, EnergyAustralia and Australian Inland Energy and Water.[7] On 1 July 2001, the NSW Government merged three distributors — Great Southern Energy, NorthPower and Advance Energy — to form Country Energy.

In Queensland, AUSTA Electric was horizontally separated into three generators — CS Energy, Stanwell Corporation and Tarong Energy — which commenced operating on 1 July 1997. At the same time, the Queensland Transmission and Supply Corporation's eight subsidiaries — seven regional distributors and the Queensland Electricity

regulation roles of the ACCC, the state regulators, the National Electricity Code Administrator and the National Competition Council (CoAG 2002).

5 In July 1991, governments agreed to work co-operatively to improve competitiveness in the electricity industry and the National Grid Council was established. In June 1993, six governments (Australian Government, New South Wales, Victoria, Queensland, South Australia and the Australian Capital Territory) committed to undertake reforms necessary to allow a competitive electricity market to commence from July 1995. At the April 1995 Council of Australian Governments meeting, these reforms were extended and brought within the NCP process.

6 An industry is considered to be a natural monopoly if total costs of production are lower when a single firm produces the entire industry output, than when two or more firms produce the same output. It is generally accepted that electricity transmission and distribution networks exhibit natural monopoly characteristics.

7 Australian Inland Energy and Water traded as Australian Inland Energy to 15 December 2000.

Transmission Corporation, trading as Powerlink — were established as independent government-owned corporations.

Three entirely new retail corporations were established and two of these merged to form Ergon Energy Pty Ltd.[8] Ergon Energy Pty Ltd was owned by six of the regional distribution corporations. On 30 June 1999, the six regional distributors amalgamated to form Ergon Energy Corporation, of which Ergon Energy Pty Ltd became a wholly-owned subsidiary.

The Queensland Power Trading Corporation was established to assist in the transition to the new industry structure by finalising a range of financial and administrative matters arising from the restructure of the Queensland Transmission and Supply Corporation. The Queensland Power Trading Corporation was also involved in trading electricity generated by a number of private sector generators. Although originally established as a transitional body, the QPTC became Queensland's fourth generation GTE in June 1999. In July 1999, the QPTC was renamed Enertrade.

In Western Australia, Western Power was established in 1995 as a government-owned corporation following the disaggregation of the State Energy Commission of Western Australia.

In Tasmania, the Hydro-Electric Corporation (HEC) was restructured into three businesses on 1 July 1998. The HEC retained responsibility for generation, while the transmission network was transferred to Transend Networks and the retailing and distribution functions were transferred to Aurora Energy.

5.3 Profitability

Profitability is influenced by a number of factors, including prices (and therefore price regulation), business volumes and expenses. Other factors, such as changes in asset values and capital restructuring, also influence reported profitability through the impact of depreciation and restructuring expenses.

The majority of monitored electricity GTEs made operating profits throughout the reporting period. However, Enertrade reported operating losses from 2000-01 to 2003-04, primarily due to contracts entered into prior to the commencement of the NEM. The conditions of Enertrade's purchase contracts (power-purchase agreements) — the longest

8 Ergon Energy Pty Ltd was formed through a merger of the Northern Electricity Retail Corporation (Omega Energy) and Central Electricity Retail Corporation (Ergon Energy) in February 1998. The third electricity retailer was Energex.

of which is for 35 years — are expected to result in significant future losses (Enertrade 2004). Transgrid reported an operating loss in 2001-02, mainly attributable to debt restructuring in that year.

The electricity sector as a whole has experienced a substantial increase in profits since the beginning of the reporting period, with profits growing by 44 per cent ($777 million) from less than $1.8 billion in 1999-00 to more than $2.5 billion in 2003-04. Without the inclusion of additional GTEs, added within the reporting period, the growth in monitored profits was $515 million (30 per cent).[9]

This increase in profits is largely attributable to improvements in the performance of distribution GTEs, which experienced a collective increase in profits of 54 per cent ($285 million) between 1999-00 and 2003-04. Generation and integrated GTEs also experienced substantial growth, with an overall increase in profits for the reporting period of $230 million (24 per cent). The profits of transmission GTEs increased by $6 million (2 per cent) over the reporting period.

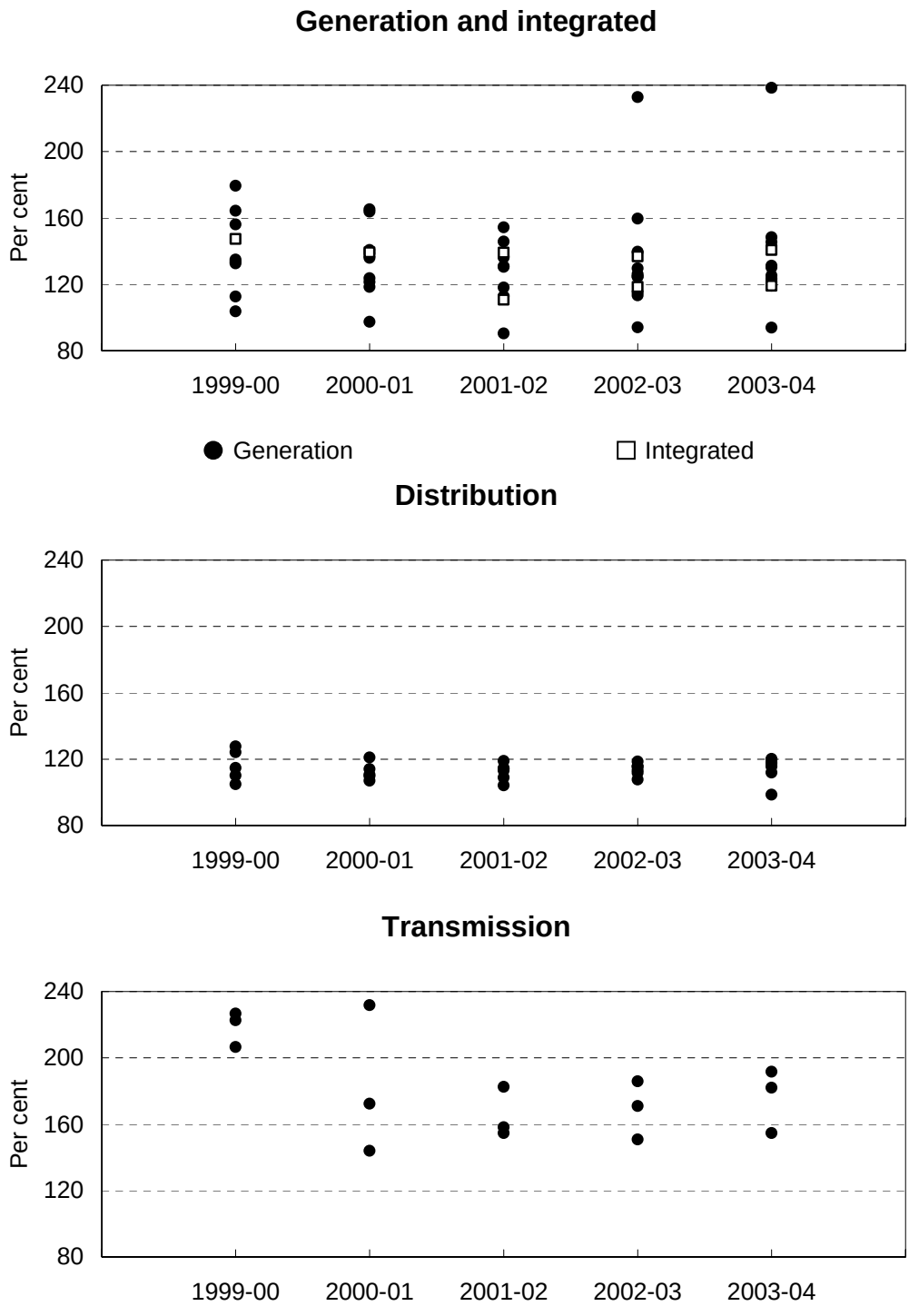
Over the reporting period, most electricity GTEs recovered between 100 and 150 per cent of operating costs (see figure 5.4). Cost recovery is a measure of the ability of a GTE to generate adequate revenue to meet expenses. A cost recovery ratio below 100 per cent suggests that a GTE was unable to meet its operating costs even before the cost of servicing debt is taken into account.

In 2003-04, three of the five highest cost recovery ratios were recorded by transmission GTEs, with TransGrid, Powerlink and Transend all recording cost recovery ratios of over 150 per cent. A generator, Snowy Hydro, recorded the highest cost recovery ratio, of almost 240 per cent. Distribution GTEs, as a group, recorded the lowest average cost recovery ratio of 113 per cent.

The return on assets for electricity GTEs as a whole fell slightly over the reporting period. However, the returns on assets for different groups of electricity GTEs, and individual GTEs within those groups, are quite diverse (see figure 5.5). To some extent, their variability reflects the influence of restructuring expenses, asset revaluations and the continuing development of the NEM. For example, the opening up of interconnectors and the introduction of retail contestability have affected the operating results of individual GTEs at different times during the reporting period.

9 In their initial years monitored, the addition of Eraring Energy in 2000-01, Country Energy and Power and Water Corporation in 2001-02 and Snowy Hydro in 2002-03 together accounted for $261 million of the $776 million increase in sector profits. The profit growth of these GTEs in years subsequent to their initial inclusion is part of the remaining $515 million increase in sector profits throughout the reporting period.

Figure 5.4 **Cost recovery — electricity GTEs**



Note Each data point represents the cost recovery ratio for a government trading enterprise in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting investment income and receipts from governments to cover deficits from total revenue. Expenses from operations are calculated by subtracting gross interest expense from total expenses. Prior to 2000-01, abnormal items were also subtracted from operating expenses and revenue.

Source: Productivity Commission estimates.

The variation of profitability within the sector is also reflected in the return on equity ratio. That ratio, for the sector as a whole, fell over the reporting period although it increased in 2003-04. Individually, most of the monitored electricity GTEs have experienced variable return on equity ratios over the reporting period.

It appears that several electricity GTEs are not achieving a sufficient return on their assets when compared to benchmark returns recommended by regulatory agencies.

IPART suggested that a nominal pre-tax return of 8.5 per cent on assets would be sufficient for electricity GTEs, taking into account the risks faced by entities operating in the sector (IPART 1998). Similarly, the Queensland Competition Authority has recommended returns for its distribution GTEs of 8.1 per cent (QCA 2001).

In 2003-04, only eight of the 21 monitored GTEs achieved a return on assets in excess of 8 per cent.[10] The median rate of return was close at 7.6 per cent.

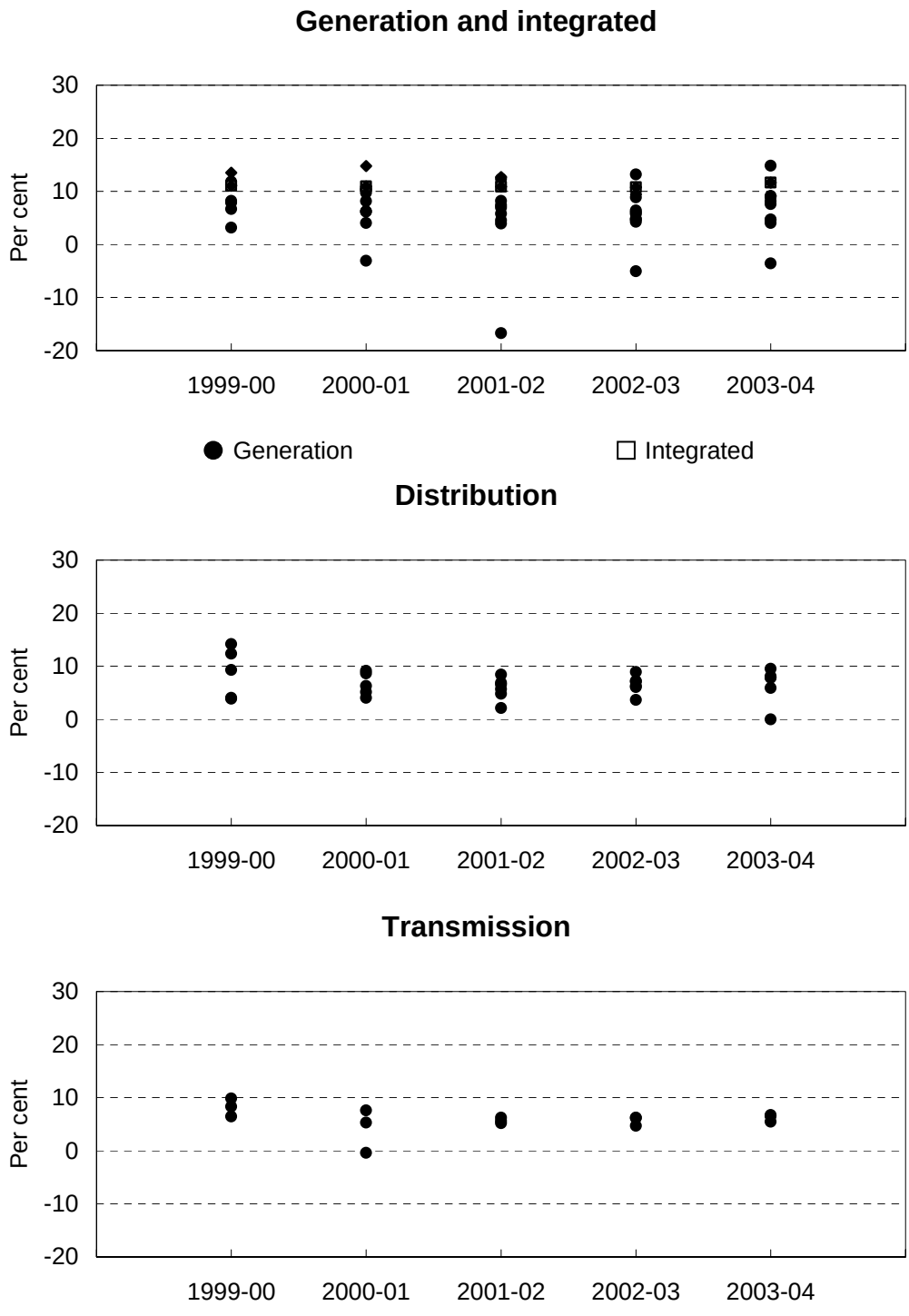
5.4 Financial management

Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

Governments have, on occasion, imposed financial restructuring on their electricity GTEs. This has generally involved the transfer of both assets and liabilities to the State and Territory Governments, and the withdrawal of equity. Financial restructuring adds to the difficulty of comparing financial performances over time.

10 Of the remaining 16 electricity GTEs, five failed to achieve the risk-free rate of 5.7 per cent (the ten year Government bond rate).

Figure 5.5 **Return on assets — electricity GTEs**



Note Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue and adding back gross interest expense. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

Examples of capital restructuring by shareholder governments are described below:

- In New South Wales, more than $5 billion in equity has been returned to the Government from electricity GTEs over the last decade. In 2000-01, $3 billion in equity was returned from the New South Wales distribution GTEs — Delta Electricity, Macquarie Generation and TransGrid. The GTEs generally increase their borrowings by a commensurate amount to pay for these transfers. Such transfers affect financial management indicators, including debt to equity, debt to total assets, interest cover and leverage ratios. For example, Eraring's debt increased by 79 per cent ($71 million) in 2003-04, through a non-cash equity for debt swap. This resulted in substantial increases in Eraring's debt to equity and debt to total assets ratios.

- In Queensland, Powerlink was required to make interest free loans (valued at $249 million) to the Government in 1997-98, as part of a capital restructure. This resulted in a 90 per cent increase in debt as Powerlink borrowed funds to make the payment. In 1998-99, $249 million of contributed equity was withdrawn, which resulted in an increase in the debt to equity, debt to total assets and total liabilities to equity ratios in that year. Similar restructuring occurred during 1999-00 and 2000-01. In 1999-00, an interest free loan of $150 million was made to the Government (funded by an increase in Powerlink debt). In 2000-01, Powerlink bought back $150 million worth of ordinary shares from the government and the share capital proceeds were used to offset the loan.
- In 2002-03, Power and Water's debt level increased due to a $56 million debt for equity swap with the NT Government. The transaction resulted in an increase in Power and Water's interest bearing liabilities and a corresponding decrease in Power and Water's equity.

A number of electricity GTEs have reduced their debt levels through financial restructuring, which has allowed them to reduce repayment periods and to negotiate improved interest terms. For example, during 1999-00 and 2000-01, the HEC paid out loans with a face value of $317 million and interest rate swaps of $898 million prior to maturity — reducing their borrowing costs by more than 20 per cent from 1999-00 levels. In 2003-04, CS Energy's level of debt fell by 44 per cent ($296 million), facilitated by a $260 million equity injection by the Queensland Government.

In 2003-04, the majority of electricity GTEs had debt to total asset ratios within the 30 to 60 per cent range (see figure 5.6). The median debt to total assets ratio was just over 29 per cent for generation and integrated GTEs, with transmission and distribution GTEs both around 44 per cent.

In 2003-04, eight electricity GTEs had an interest cover of over three times. Only one GTE had negative interest cover. No other GTE had interest cover multiples of less than two.

The margin insulating electricity GTEs from increases in interest rates or falling revenues seems to be increasing. This suggests that, going forward, these GTEs more likely to be able to meet their debt repayment commitments from current earnings.

5.5 Financial transactions

As part of the reform process, governments have increased the commercial focus of GTEs and facilitated competitive neutrality by exposing them to incentives and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles, see chapter 2.

The introduction of income tax-equivalent regimes and requirements to pay dividends and debt guarantee fees are examples of how governments have imposed the principles of competitive neutrality on their electricity GTEs.

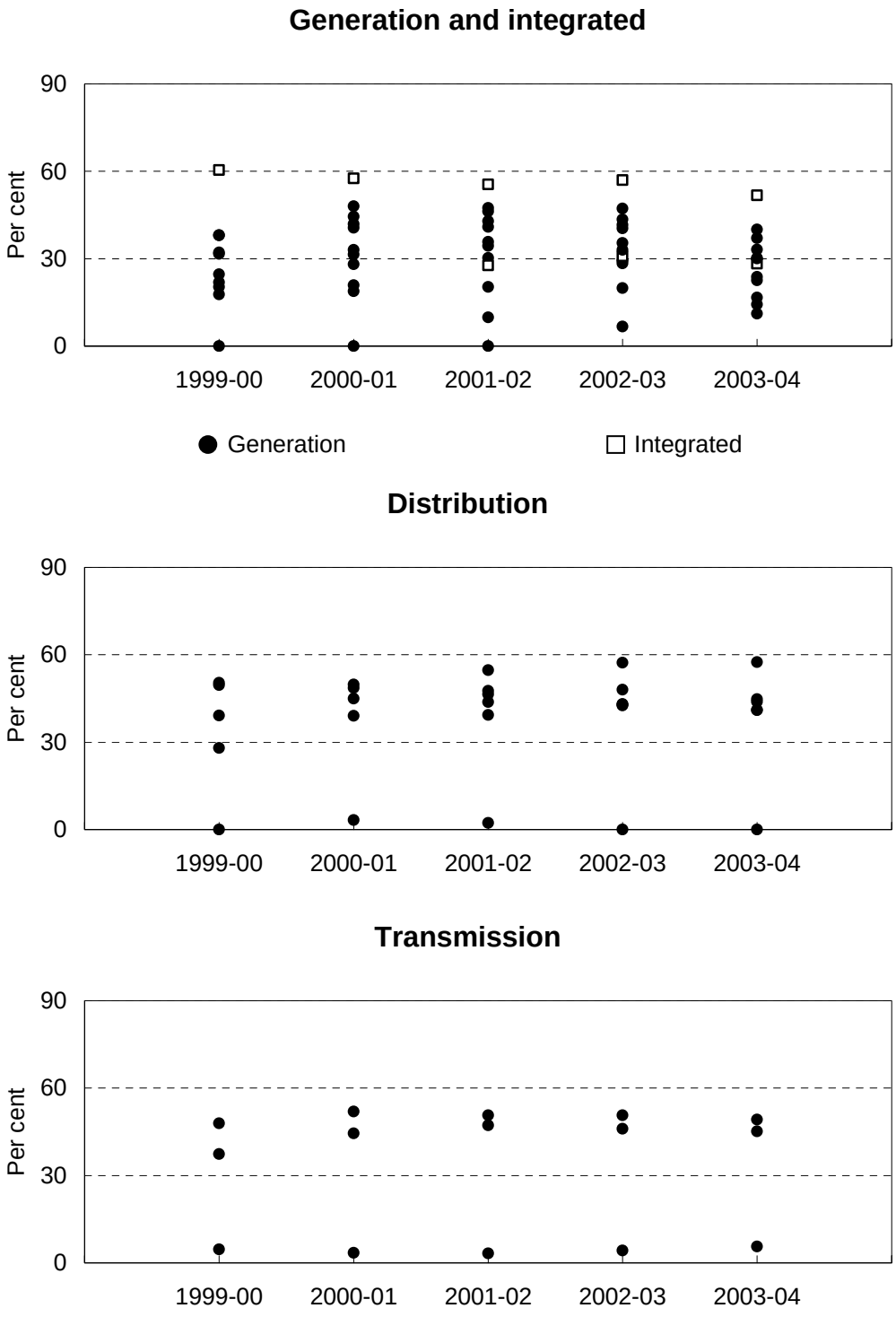
Prior to 1999-00, tax-equivalent payments were based on a company tax rate of 36 per cent. Under tax-effect accounting, income tax-equivalent expenses for any year may differ from the actual amount of tax paid to the State and Territory Governments for that year because of permanent and timing differences. Changes in the company tax rate announced by the Australian Government in December 1999 led to the restatement of deferred tax liabilities in 1999-00.[11]

The number of electricity GTEs making tax-equivalent and dividend payments has been increasing over the reporting period and most now make such payments. The tax-equivalent and dividend payments received by owner-governments have increased with profit growth over the reporting period (see figure 5.7).

Dividend payments represent a return on shareholder funds and their size reflects financial performance. In 2003-04, New South Wales electricity GTEs paid approximately $600 million in dividend payments, Queensland electricity GTEs returned $472 million while Western Australian and Tasmanian electricity GTEs returned $104 million and $67 million respectively. Power and Water Corporation returned $20 million to the NT Government.

11 The company tax rate was decreased to 34 per cent for 2000-01 and then to 30 per cent from 2001-02.

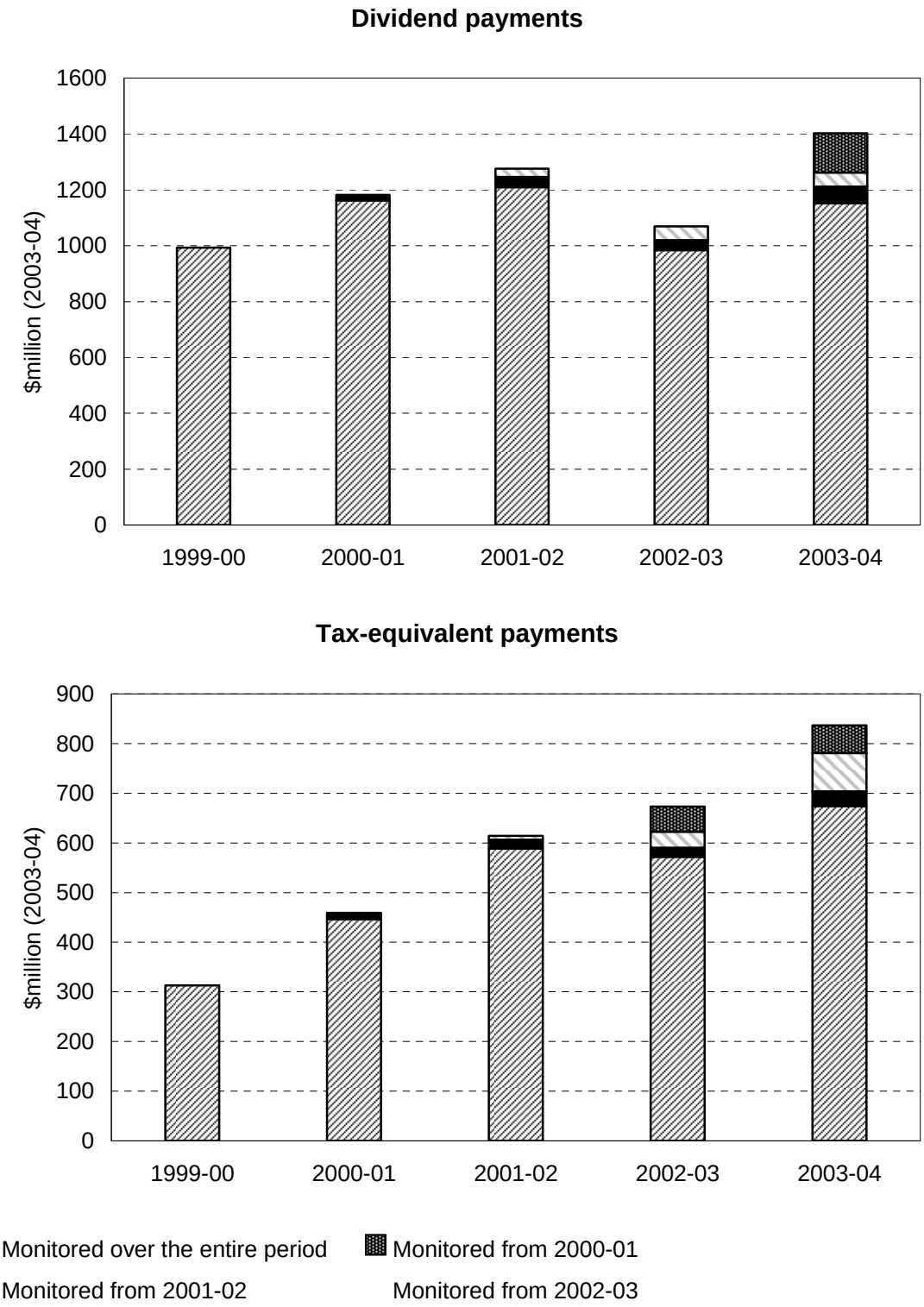
Figure 5.6 **Debt to total assets — electricity GTEs**



Note Each data point represents the debt to total assets ratio for a government trading enterprise in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

Figure 5.7 **Dividend and tax-equivalent payments — electricity GTEs**



Note The value of dividends and tax-equivalent payments prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

As part of the reform process, governments have also moved to identify, cost and fund the CSOs that they impose on electricity GTEs. CSO funding is received for the provision of rebates, concessions, the uneconomic supply of electricity to some customers and for electrical inspections.

Several of the electricity GTEs received CSO funding over the reporting period. Generally, it is GTE retailers are subject to these obligations, although there are some examples of CSOs being placed on generation GTEs.

In 2003-04, disclosed CSO payments to electricity GTEs amounted to over $400 million. Approximately 75 per cent of all CSO payments were made to distribution GTEs.

ELECTRICITY

Table 5.4 **Whole of sector performance indicators 1999-00 to 2003-04**

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	33 568	38 675	44 062	48 402	50 402
Total revenue	$m	12 927	14 077	16 067	17 193	18 122
Profitability						
Operating profit before tax	$'000	1 770 042	1 638 670	1 827 492	2 012 397	2 547 156
Operating sales margin	%	20.9	19.0	18.1	18.9	20.8
Cost recovery	%	128.8	124.7	122.1	123.3	126.3
Return on assets	%	8.3	7.4	6.9	7.0	7.8
Return on equity	%	9.8	7.2	6.6	6.6	7.9
Financial management						
Debt to equity	%	80.6	91.5	95.2	93.3	83.9
Debt to total assets	%	38.0	42.0	41.7	41.5	38.3
Total liabilities to equity	%	117.6	128.9	133.2	131.1	123.9
Interest cover	times	2.8	2.5	2.6	2.6	3.0
Current ratio	%	91.2	77.5	77.8	71.7	71.3
Leverage ratio	%	217.6	228.9	233.2	231.1	223.9
Payments to and from government						
Dividends	$'000	967 407	1 162 287	1 276 647	1 079 422	1 401 884
Dividend to equity ratio	%	6.5	7.1	6.9	5.3	6.5
Dividend payout ratio	%	66.0	98.2	105.2	80.7	82.0
Income tax expense	$'000	304 700	455 501	614 264	674 090	836 705
CSO funding	$'000	336 266	305 746	39 1382	397 671	402 599

5.6 GTE performance reports

Delta Electricity (NSW)
Macquarie Generation (NSW)
Eraring Energy (NSW)
TransGrid (NSW)
Australian Inland (NSW)
EnergyAustralia (NSW)
Integral Energy (NSW)
Country Energy (NSW)
CS Energy (Queensland)
Stanwell Corporation (Queensland)
Tarong Energy (Queensland)
Enertrade (Queensland)
Powerlink (Queensland)
Ergon Energy (Queensland)
Energex (Queensland)
Western Power (WA)
Hydro-Electric Corporation (Tasmania)
Aurora Energy (Tasmania)
Transend Networks (Tasmania)
Power and Water Corporation (NT)
Snowy Hydro (Australian Government)

DELTA ELECTRICITY — New South Wales

Delta Electricity (Delta) was formed on 1 March 1996 as part of the NSW Government's restructure of the State's electricity industry. Delta operates under the *State Owned Corporations Act 1989* and the *Energy Services Corporations Act 1995*. Delta's primary business is the generation of electricity, most of which is sourced from four coal-fired power stations with a combined generation capacity of 4240 MW. It also owns two small hydro-electric plants.

Delta generates electricity for sale into the National Electricity Market (NEM) — to which it contributes around 12 per cent of total supply. Although Delta does not face direct price regulation, it is subject to the rules and conditions governing the NEM.

Delta's pre-tax operating profit rose by 9 per cent to $111 million in 2003-04, with a $6 million increase in revenues and a $2 million decrease in expenses. This improvement is mainly attributable to adjustments in Delta's defined benefit superannuation funds.

In 2003-04, the value of Delta's total assets reduced by $129 million (6 per cent). This largely represented a $92 million decrease in the value of Delta's current assets — including a $25 million reduction in cash, a $31 million reduction in inventories and a $15 million reduction in receivables — and a $39 million fall in the value of Delta's property, plant and equipment as a result of asset write-offs and depreciation expense.

Despite the reduction in asset values, Delta's debt to equity and debt to total assets ratios improved in 2003-04 with an 18 per cent reduction in its level of debt. However, Delta's liquidity, as measured by the current ratio, decreased substantially in 2003-04 through a 34 per cent decrease in current assets and an 8 per cent increase in current liabilities.

Under the provisions of the *State Owned Corporations Act 1989*, Delta is required to make tax-equivalent and dividend payments. Dividend payments are made in accordance with the share dividend scheme, which is determined by the voting shareholders and as required by the *Energy Services Corporations Act 1995*. In 2003-04, Delta provided for a $74 million dividend payment — which represents 100 per cent of after tax profit — and recorded an income tax-equivalent expense of $37 million.

DELTA ELECTRICITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*[c]	*2003-04*
Size						
Total assets	$m	1 492	1 555	1 600	2 006	1 877
Total revenue	$m	674	757	732	725	731
Profitability						
Operating profit before tax	$'000	158 671	188 072	142 359	102 003	111 042
Operating sales margin	%	28.0	28.9	26.8	22.9	23.8
Cost recovery	%	133.6	140.6	136.6	129.7	131.2
Return on assets	%	13.5	14.8	12.7	9.5	9.1
Return on equity	%	16.1	23.2	24.3	10.3	9.3
Financial management						
Debt to equity	%	46.2	190.3	183.9	98.0	80.3
Debt to total assets	%	24.6	48.0	46.2	43.5	33.1
Total liabilities to equity	%	96.1	304.8	303.9	150.5	134.5
Interest cover	times	5.7	6.1	3.4	2.5	2.7
Current ratio	%	134.3	127.1	126.7	126.7	77.5
Leverage ratio	%	196.1	404.8	403.9	250.5	234.5
Payments to and from government						
Dividends	$'000	86 653	119 740	85 482	113 068	74 170
Dividend to equity ratio	%	11.6	20.9	21.9	18.9	9.3
Dividend payout ratio	%	72.4	90.0	90.0	184.3	100.0
Income tax expense	$'000	38 966	55 028	47 379	40 653	36 872
CSO funding	$'000	0	0	0	0	0

a Includes an abnormal gain of $26 million related to surpluses in superannuation funds. A fall in the future company tax rate reduced tax-equivalent payments by $18 million. **b** Delta Electricity returned $380 million in contributed equity to the NSW Government. This was paid for by additional borrowings, thereby increasing the level of debt by a commensurate amount. **c** Following the adoption of a new accounting policy regarding the valuation of physical non-current assets, in 2002-03, the value of total assets increased by $406 million. Property, plant and equipment is recognised at fair value in accordance with AASB 1041 *Revaluation of Non-Current Assets* and the *New South Wales Treasury Accounting Policy for the Valuation of Non-Current Assets at Fair Value*. Prior to 2002-03, Delta recognised property plant and equipment on a historical cost basis, except where revalued following the approval of the directors. In 2002-03, Delta's dividend payment included a $50 million special dividend.

MACQUARIE GENERATION — New South Wales

Macquarie Generation (Macquarie) operates under the *State Owned Corporations Act 1989* and the *Energy Services Corporations Act 1995*. It currently operates two coal-fired power stations — Bayswater and Liddell — with a combined generating capacity of 4640 MW.

Macquarie generates electricity for sale into the National Electricity Market (NEM) — to which it contributes over 14 per cent of total supply. Although Macquarie does not face direct price regulation, it is subject to the rules and conditions governing the NEM.

In 2003-04, Macquarie's pre-tax operating profit rose by 57 per cent ($58 million) to almost $159 million, with a 7 per cent ($50 million) increase in revenue — a result of a 9 per cent increase in sales volume. This result represented a partial recovery from the $81 million fall in profits in 2002-03, caused by a reduction in the average New South Wales electricity spot price and increased competition from interstate generators.

Macquarie's total assets increased by 3 per cent ($77 million) in 2003-04, attributed mainly to a revaluation of physical non-current assets. Macquarie's debt was reduced by $109 million (9 per cent) in 2003-04 as part of its debt repayment strategy. This debt repayment strategy, combined with Macquarie's debt restructure in December 2002, significantly reduced its borrowing costs.

Under the provisions of the *State Owned Corporations Act 1989*, Macquarie is required to make tax-equivalent and dividend payments. Dividend payments are made in accordance with the share dividend scheme, which is determined by the voting shareholders and as required by the *Energy Services Corporations Act 1995*. In 2003-04, Macquarie provided for a $100 million dividend payment and recorded an income tax-equivalent expense of $57 million.

MACQUARIE GENERATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*[c]	*2003-04*[d]
Size						
Total assets	$m	2 158	2 065	2 127	2 828	2 905
Total revenue	$m	733	808	815	761	811
Profitability						
Operating profit before tax	$'000	65 134	143 230	181 571	100 718	158 576
Operating sales margin	%	19.2	26.4	31.4	28.4	31.2
Cost recovery	%	132.5	135.9	145.8	139.6	145.4
Return on assets	%	6.7	10.3	12.3	8.8	8.9
Return on equity	%	6.3	12.7	17.5	6.1	8.3
Financial management						
Debt to equity	%	86.9	135.2	130.0	100.7	83.7
Debt to total assets	%	38.0	44.5	42.9	47.2	37.0
Total liabilities to equity	%	129.5	197.2	207.4	143.3	129.0
Interest cover	times	1.8	3.0	3.4	1.8	2.6
Current ratio	%	81.3	54.3	64.3	52.4	62.0
Leverage ratio	%	229.5	297.2	307.4	243.3	229.0
Payments to and from government						
Dividends	$'000	50 000	100 000	125 000	56 000	100 000
Dividend to equity ratio	%	5.3	12.2	18.0	6.0	8.2
Dividend payout ratio	%	84.4	96.5	103.0	98.9	98.8
Income tax expense	$'000	5 918	39 597	60 257	44 081	57 335
CSO funding[e]	$'000	7 854	0	0	0	0

a Abnormal revenue relating to investment returns on externally managed superannuation funds of $19 million was reported. This was offset by an abnormal loss of $53 million due to the termination of a long-term coal supply contract. The fall in income tax-equivalent payments reflects an $18 million downward adjustment in the future company tax rate. **b** Macquarie returned $240 million in contributed equity to the NSW Government. The return was paid for with additional borrowings, increasing the level of debt by a commensurate amount. **c** In 2002-03, the capital restructure and asset revaluation increment significantly affected Macquarie's financial management indicators. The debt to equity and total liabilities to equity ratios both fell, primarily due to the substantial increase in the valuation of Macquarie's assets. Macquarie returned $400 million in contributed equity to the NSW Government. The return was paid for with additional borrowings, increasing the level of debt. **d** Macquarie's total assets increased by 3 per cent ($77 million) in 2003-04, with a revaluation of physical non-current assets. **e** Until 1999-00, the NSW Government provided Macquarie with funding for the provision of CSOs. Macquarie was reimbursed for the full cost of providing rebates and subsidies to certain customers in line with NSW Government policy decisions. CSOs (and funding) ceased on 5 December 1999.

ERARING ENERGY — New South Wales

Eraring Energy (Eraring) commenced operations on 2 August 2000 following the transfer of generation assets, staff, rights and liabilities from Pacific Power. Eraring operates under the *State Owned Corporations Act 1989* and the *Energy Services Corporations Act 1995*.

Eraring generates and trades electricity within the National Electricity Market (NEM). Its generation assets have a capacity of 3041 MW, from coal, hydro and wind electricity plants — the largest being the Eraring coal-fired power station which provides around 87 per cent of the company's output. Eraring also has a wholly-owned subsidiary, Pacific Western, which operates the Collie Power Station in Western Australia under contract to Western Power.

Despite a fall in the average spot price for electricity in the NEM, Eraring's revenue was $27 million (5 per cent) higher in 2003-04 than in the previous year. An increase in electricity sales accounted for $14 million of the improvement and the remainder was made up mostly of an insurance provision write back and movement in superannuation provisions. Paired with a $14 million (3 per cent) reduction in expenses, the increase in revenue resulted in a $40 million (69 per cent) rise in Eraring's pre-tax operating profit to $98 million in 2003-04.

In 2003-04, Eraring's total asset value grew by $138 million (10 per cent), largely attributable to a revaluation increment to the power station equipment and power station buildings. Eraring's debt increased by 79 per cent ($71 million) in 2003-04, through a non-cash equity for debt swap. This resulted in substantial increases in Eraring's debt to equity and debt to total assets ratios. Eraring's liquidity, as measured by the current ratio, decreased substantially over the last two financial years.

Under the provisions of the *State Owned Corporations Act 1989*, Eraring is required to make tax-equivalent and dividend payments. Dividend payments are made in accordance with the share dividend scheme, which is determined by the voting shareholders and as required by the *Energy Services Corporations Act 1995*. In 2003-04, Eraring returned almost $90 million to the State Government in tax-equivalent and dividend payments.

Eraring received $67 000 in CSO payments from the NSW Government in 2003-04.

ERARING ENERGY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*[d]
Size						
Total assets	$m		1 319	1 327	1 385	1 523
Total revenue	$m		463	533	553	580
Profitability						
Operating profit before tax	$'000		36 812	48 574	58 182	98 101
Operating sales margin	%		17.6	11.3	11.8	19.0
Cost recovery	%		121.3	112.7	113.4	123.5
Return on assets	%		6.2	4.5	4.8	7.6
Return on equity	%		2.7	3.2	3.8	6.2
Financial management						
Debt to equity	%		28.1	12.6	8.3	14.4
Debt to total assets	%		18.9	9.9	6.7	11.1
Total liabilities to equity	%		49.0	27.7	26.1	35.3
Interest cover	times		1.8	5.2	9.2	9.0
Current ratio	%		72.2	104.2	74.7	50.2
Leverage ratio	%		149.0	127.7	126.1	135.3
Payments to and from government						
Dividends[c]	$'000		19 479	36 471	35 828	60 064
Dividend to equity ratio	%		2.2	3.8	3.4	5.4
Dividend payout ratio	%		80.8	119.1	88.3	87.2
Income tax expense	$'000		12 716	17 954	18 090	29 258
CSO funding	$'000		125	59	110	67

a In August 2001, the NSW Government agreed to repurchase $150 million of Eraring's debt. **b** The figures for 2001-02 have been adjusted retrospectively to allow comparability with 2002-03 figures which recognise energy sales on a gross basis. Current assets and current liabilities were adjusted upward by $78 million. In 2001-02, Eraring's debt to equity and debt to total asset ratios were significantly lower than in 2000-01, due to the NSW Government re-purchasing $150 million of Eraring's debt. **c** The dividend payments for 2001-02 and 2002-03 were reduced by $4.3 million and $4.7 million respectively. These amounts were paid for worker's compensation and dust disease court determinations for other than Eraring Energy employees. The liability was transferred from the NSW Government to Eraring Energy on corporatisation, with agreement that the matter would be treated as a CSO and deducted from dividends. In 2002-03 Eraring's debt ratios decreased due to a reduction in debt ($40 million) and an upward revaluation of non-current assets ($55 million). **d** Eraring Energy repaid capital of $137 million in October 2003 via a non-cash equity for debt swap.

TRANSGRID — New South Wales

TransGrid operates under the *State Owned Corporations Act 1989*. It was established under the *Electricity Transmission Authority Act 1994* and corporatised on 14 December 1998 under the *Energy Services Corporations Amendment (TransGrid Corporatisation) Act 1998.*

TransGrid is responsible for the planning, management and development of the New South Wales high voltage electricity transmission network — the largest high voltage network in Australia. It transmits power between generators and bulk distributors, some large direct customers and to interconnectors linking Victoria, South Australia and Queensland.

In accordance with the requirement of the National Electricity Code, the Australian Competition and Consumer Commission is required to set 'caps' on TransGrid's regulated revenue for each 5-year regulatory periods. The next period commences on 1 July 2004.

A 10 per cent ($40 million) increase in revenue resulted in TransGrid's pre-tax operating profit rising to almost $115 million in 2003-04, 55 per cent higher than the previous year. The increase is a result of greater revenue from electricity generation and unregulated work, and movement in the employer's superannuation reserve.

The value of TransGrid's total assets increased steadily over the reporting period. In 2003-04, the value of total assets increased by almost 21 per cent ($577 million), caused by a significant revaluation increment of property, plant and equipment and the addition of work in progress.

Debt increased by 10 per cent ($135 million) in 2003-04 to over $1.5 billion. The net effect of the higher level of debt and increased asset value decreased TransGrid's debt to total asset and debt to equity ratios.

TransGrid is required to make tax-equivalent and dividend payments to the NSW Government. In 2003-04, TransGrid provided for a $70 million dividend payment and recorded an income tax-equivalent expense of $32 million.

TRANSGRID (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*[c]	*2003-04*
Size						
Total assets	$m	2 392	2 550	2 674	2 807	3 384
Total revenue	$m	354	360	381	407	447
Profitability						
Operating profit before tax	$'000	152 763	- 84 968	53 092	82 294	114 995
Operating sales margin	%	64.1	- 3.3	35.4	41.5	45.1
Cost recovery	%	226.8	172.4	154.7	171.0	182.0
Return on assets	%	9.8	- 0.4	5.2	6.2	6.5
Return on equity	%	10.4	- 9.6	2.3	4.2	6.3
Financial management						
Debt to equity	%	64.8	121.1	119.6	123.6	100.5
Debt to total assets	%	37.4	52.0	50.7	50.7	49.2
Total liabilities to equity	%	78.9	140.4	141.5	149.9	123.2
Interest cover	times	3.0	- 0.1	1.6	1.9	2.3
Current ratio	%	160.4	73.4	51.0	26.0	35.2
Leverage ratio	%	178.9	240.4	241.5	249.9	223.2
Payments to and from government						
Dividends	$'000	54 623	0	0	46 199	70 000
Dividend to equity ratio	%	4.2	0.0	0.0	4.1	5.3
Dividend payout ratio	%	40.6	0.0	0.0	97.5	84.2
Income tax expense	$'000	18 345	29 567	27 774	34 892	31 814
CSO funding	$'000	0	0	0	0	0

a Includes an abnormal gain of $66 million due to previous overfunding of superannuation contributions. A change in accounting policy led to interest on some capital expenditure being capitalised. Income tax-equivalent payments were adjusted downwards by $11 million due to a reduction in the future company tax rate. **b** TransGrid returned $260 million of contributed equity to the NSW Government in 2000-01, as part of a capital restructure. Debt increased by a commensurate amount in that year. As part of the restructure, TransGrid incurred an expense of $162 million due to the prepayment of its existing debt portfolio. This restructure had a significant effect on TransGrid's financial performance ratios. **c** In 2002-03, TransGrid returned $60 million of contributed equity to the NSW Government.

AUSTRALIAN INLAND — New South Wales

On 15 December 2000, Australian Inland Energy (AIE) merged with the Broken Hill Water Board to form a new entity, Australian Inland Energy and Water Infrastructure (AIEWI).[1] In 2002-03, AIEWI commenced trading as Australian Inland.[2] AIE was originally established on 1 March 1996, as a government-owned electricity distributor and retailer, under the *State Owned Corporations Act 1989*. Until 1999-00, it traded as AIE providing energy services in the far west and south-west of New South Wales.

The *Electricity Supply Act 1995* (and its regulations) and the National Electricity Code govern Australian Inland's electricity operations. Australian Inland operates under a revenue cap as determined by the Independent Pricing and Regulatory Tribunal (IPART).[3]

Pre-tax operating profit decreased to $7000 in 2003-04 from $5.8 million in 2002-03, with a $3.4 million decrease in expenses only partially compensating for a $9.2 million decrease in revenue.

Australian Inland received a $456 000 income tax benefit in 2003-04 and no dividend was announced for the year. Australian Inland operated debt free in 2002-03 and 2003-04.

Australian Inland receives CSO payments from the NSW Government to compensate for the supply of electricity to sparsely populated areas. The value of this CSO was $7.6 million in 2003-04.

1 In 2002-03, $45 million (65 per cent) of Australian Inland's revenue was earned through electricity sales and $9.5 million (14 per cent) was earned through water rates and charges, and sewer services.

2 Legislation has been passed for the legal merger of Country Energy and Australian Inland on 1 July 2005. Country Energy is already providing services on behalf of Australian Inland.

3 In December 1999, IPART set revenue caps for each distribution GTE in New South Wales, covering the period from February 2000 to June 2004. The determination provides for a real price decrease equal to 16 per cent over the period, when averaged across the distribution GTEs in New South Wales.

AUSTRALIAN INLAND (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*[a]	*2001-02*	*2002-03*[b]	*2003-04*
Size						
Total assets	$m	67	154	158	158	164
Total revenue	$m	37	52	64	71	62
Profitability						
Operating profit before tax	$'000	9 261	4 351	3 063	5 786	7
Operating sales margin	%	23.0	6.5	3.9	7.1	- 1.4
Cost recovery	%	124.2	107.0	104.1	107.6	98.6
Return on assets	%	14.2	4.1	2.1	3.7	0.0
Return on equity	%	13.2	3.5	1.5	3.4	0.3
Financial management						
Debt to equity	%	0.0	2.8	2.7	0.0	0.0
Debt to total assets	%	0.0	3.3	2.3	0.0	0.0
Total liabilities to equity	%	29.0	17.4	17.4	14.7	14.2
Interest cover	times	n.r.	32.5	12.9	232.4	n.r.
Current ratio	%	184.7	166.4	175.3	226.4	207.2
Leverage ratio	%	129.0	117.4	117.4	114.7	114.2
Payments to and from government						
Dividends	$'000	2 670	1 112	549	464	0
Dividend to equity ratio	%	5.3	1.2	0.4	0.3	0.0
Dividend payout ratio	%	40.4	34.2	26.7	10.1	0.0
Income tax expense	$'000	2 652	1 098	1 007	1 198	- 456
CSO funding[c]	$'000	5 300	5 300	5 300	5 300	7 620

a Australian Inland Energy merged with the Broken Hill Water Board in December 2000 and was renamed Australian Inland Energy and Water Infrastructure (AIEWI). Assets increased by $78 million as a result of the merger. **b** In 2002-03, AIEWI was replaced by Australian Inland.**c** Australian Inland, (formerly AIEWI), receives CSO payments from the NSW Government to compensate for the supply of electricity to sparsely populated areas. **n.r.** Not relevant.

ENERGYAUSTRALIA — New South Wales

EnergyAustralia operates under the *State Owned Corporations Act 1989* (SOC Act) and the *Energy Services Corporations Act 1995*. EnergyAustralia distributes and retails electricity within the framework of the *Electricity Supply Act 1995* and the National Electricity Code. Its electricity distribution network covers over 22 275 square kilometres and stretches from Sydney to the upper Hunter Valley in New South Wales. It holds electricity retail licences in New South Wales, Victoria, Queensland and the Australian Capital Territory. EnergyAustralia also distributes and retails natural gas.

EnergyAustralia operates as a holding company with four subsidiary businesses — Customer Service, Retail and Marketing, Eneserve and Network. The distribution and retail businesses operate under a revenue cap determined by the Independent Pricing and Regulatory Tribunal (IPART).[1]

In 2003-04, pre-tax operating profit increased by 25 per cent ($52 million) compared with the previous year. A 5 per cent ($132 million) rise in revenue related to an increase in the sale and delivery of energy was the main cause of this improved operating result.

The value of EnergyAustralia's assets increased by 5 per cent ($275 million) to $5.6 billion in 2003-04. The increase is mainly attributable to capital investment in the network. The level of debt also increased 5 per cent ($125 million) to $2.4 billion. EnergyAustralia's liquidity, as measured by the current ratio, has decreased over the reporting period owing to substantial increases in current liabilities.

EnergyAustralia is required to make tax-equivalent and dividend payments. In 2003-04, EnergyAustralia provided for a $164 million dividend payment and recorded an income tax-equivalent expense of $79 million.

The NSW Government funds EnergyAustralia for the provision of agreed community service obligations (CSOs). These include provision of rebates to pensioners and low income households, medical rebates for life support systems, and the electricity payment assistance scheme. In 2003-04 EnergyAustralia received $35 million.

1 In December 1999, IPART set revenue caps for each distribution GTE in New South Wales, covering the period from February 2000 to June 2004. The determination provides for a real price decrease equal to 16 per cent during the period, when averaged across the distribution GTEs in New South Wales. On 25 January 2000, the Australian Competition and Consumer Commission also made a determination in relation to EnergyAustralia's distribution assets.

ENERGYAUSTRALIA (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	3 732	5 194	5 276	5 341	5 616
Total revenue	$m	2 099	2 196	2 255	2 404	2 536
Profitability						
Operating profit before tax	$'000	380 606	224 935	184 435	204 673	256 451
Operating sales margin	%	22.0	17.4	15.8	15.6	16.8
Cost recovery	%	127.7	121.0	118.8	118.5	120.2
Return on assets	%	12.4	8.6	6.9	7.1	7.8
Return on equity	%	19.4	8.9	5.3	5.8	8.2
Financial management						
Debt to equity	%	59.5	110.7	106.9	105.7	110.7
Debt to total assets	%	28.0	49.8	43.8	42.9	43.8
Total liabilities to equity	%	111.2	158.8	146.3	147.9	159.0
Interest cover	times	5.5	2.4	2.1	2.2	2.5
Current ratio	%	73.6	56.3	58.0	52.0	54.5
Leverage ratio	%	211.2	258.8	246.3	247.9	259.0
Payments to and from government						
Dividends	$'000	184 300	92 500	47 500	106 400	163 500
Dividend to equity ratio	%	10.9	4.9	2.3	5.0	7.6
Dividend payout ratio	%	56.0	55.4	43.2	84.7	92.1
Income tax expense	$'000	51 732	57 821	74 480	79 121	78 886
CSO funding[c]	$'000	0	0	29 300	35 500	0

a An abnormal gain of $24 million was reported relating to revised superannuation provisions. This was partly offset by abnormal expenses incurred due to year 2000 costs ($11 million). Accounting policy changed to treat tax on superannuation and capital contributions as a permanent difference, rather than a timing difference. This change reduced the tax-equivalent expense by $39 million. A fall in the future company tax rate also reduced tax payable by $13 million. **b** EnergyAustralia returned over $1.1 billion in contributed equity to the State. The return was paid for with borrowings, increasing the level of EnergyAustralia's debt by a commensurate amount. Assets increased by $1.5 billion, largely due to a revaluation of non-current, physical assets. **c** The NSW Government funds EnergyAustralia for the provision of agreed CSOs relating to rebates to pensioners and low income households, medical rebates for life support systems and the electricity payment assistance scheme. These amounts were not disclosed by EnergyAustralia in its annual reports prior to 2001-02.

INTEGRAL ENERGY — New South Wales

Integral Energy (Integral) operates under the *State Owned Corporations Act 1989* and the *Energy Services Corporations Act 1995*. Integral distributes and retails electricity within the framework of the *Electricity Supply Act 1995* and the National Electricity Code. Integral holds licences to retail electricity in New South Wales, Victoria, Queensland, South Australia and the Australian Capital Territory, through the National Electricity Market (NEM).

Revenue from the distribution network is capped by the Independent Pricing and Regulatory Tribunal (IPART).[1]

In 2003-04, Integral's pre-tax operating profit was more than 110 per cent ($87 million) higher than the previous year, largely due to a 10 per cent ($119 million) increase in revenue — which included a $75 million increase in metered electricity sales and a $25 million increase in revenue from sale of non-current assets.

The value of Integral's assets increased 4 per cent ($107 million) in 2003-04 and its debt increased by slightly more than 1 per cent ($12 million). Integral's 'debt to equity' and 'debt to total assets' ratios remained stable over the reporting period, while its current ratio decreased steadily.

Integral is required to make tax-equivalent and dividend payments to the NSW Government. In 2003-04, Integral paid a dividend of $102 million and made tax-equivalent payments of $62 million.

Integral receives funding for the provision of CSOs related primarily to rebates for pensioners. In 2003-04, Integral received payment of $21 million for CSOs.

1 In December 1999, IPART set revenue caps for each distribution GTE in New South Wales, covering the period from February 2000 to June 2004. The determination provides for a real price decrease equal to 16 per cent, during the period, when averaged across the distribution GTEs in New South Wales.

INTEGRAL ENERGY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*	*2003-04*
Size						
Total assets	$m	1 917	2 559	2 669	2 674	2 781
Total revenue	$m	1 122	1 142	1 135	1 199	1 318
Profitability						
Operating profit before tax	$'000	83 422	104 242	99 066	76 941	164 140
Operating sales margin	%	13.1	15.5	15.3	13.1	18.7
Cost recovery	%	112.6	118.3	118.0	115.1	123.0
Return on assets	%	7.9	8.2	6.9	6.1	9.2
Return on equity	%	15.6	8.8	5.9	4.2	10.1
Financial management						
Debt to equity	%	93.2	78.3	105.9	105.2	102.4
Debt to total assets	%	38.0	40.6	40.9	40.4	40.0
Total liabilities to equity	%	149.9	120.6	164.3	160.9	161.0
Interest cover	times	2.3	2.3	2.2	1.9	2.9
Current ratio	%	104.0	74.7	66.4	51.6	48.0
Leverage ratio	%	249.9	220.6	264.3	260.9	261.0
Payments to and from customers						
Dividends	$'000	29 743	52 776	88 764	43 783	102 324
Dividend to equity ratio	%	4.1	6.3	9.3	4.3	10.1
Dividend payout ratio	%	26.1	71.8	157.7	101.9	100.0
Income tax expense	$'000	-30 648	30 721	42 793	33 986	61 817
CSO funding	$'000	13 399	0	17 025	19 417	21 238

a Includes an abnormal gain of $24 million related to superannuation provisions. NSW Treasury changed the basis of dividend payments from available cash, to 90 per cent of net profit before tax (excluding abnormals). A change in the accounting treatment for tax purposes of capital and superannuation contributions reduced tax payable by $32 million. The fall in the future company tax rate also reduced tax payable by $10.2 million. **b** Integral Energy returned $200 million in contributed equity to the NSW Government. The return was paid for with borrowings, increasing the level of debt by a commensurate amount. Assets were revalued upwards on 1 January 2001. The amount of CSO funding received by Integral Energy was not disclosed in its 2000-01 annual report. **c** Integral Energy returned $150 million in contributed equity to the NSW Government in 2001-02. The return was paid for with borrowings, increasing the level of debt by an equivalent amount.

COUNTRY ENERGY — New South Wales

Country Energy was established on 1 July 2001, from the merger of three regional energy businesses: NorthPower, Advance Energy and Great Southern Energy.[1] Country Energy operates under the *State Owned Corporations Act 1989* and the *Energy Services Corporations Act 1995*.

Country Energy is the largest regionally-based energy business in Australia. Its distribution network covers 72 per cent of New South Wales. County Energy holds distribution and retail licenses in New South Wales and Victoria (for electricity and gas) and holds retail licenses in Queensland, South Australia and the Australian Capital Territory.[2]

Country Energy's distribution and retail businesses operate under a revenue cap determined by the Independent Pricing and Regulatory Tribunal (IPART).[3]

In 2003-04, Country Energy's pre-tax operating profit more than doubled, increasing by over $85 million to almost $141 million, with a 4 per cent ($53 million) increase in expenses more than offset by a 9 per cent ($138 million) increase in revenue.

In 2003-04, total assets increased by 9 per cent ($227 million) to $2.9 billion, largely due to an increase in the value of property, plant and equipment through investment in infrastructure.

Country Energy is required to make tax-equivalent and dividend payments. In 2003-04, it provided for a $30 million dividend payment and recorded an income tax-equivalent expense of $62 million.

Country Energy receives funding for CSOs from the NSW Government for pensioners, customers in caravan parks and people who rely on life support machines. In 2003-04, it received CSO payments equal to $23 million.

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1 On 1 June 2001, NorthPower changed its name to Country Energy. On 1 July 2001, the net assets and equity of Advance Energy and Great Southern Energy were merged with the net assets and equity of Country Energy.

2 Country Energy also has special approval for the distribution and retailing of electricity in parts of south–west Queensland.

3 In December 1999, IPART set revenue caps for each distribution GTE in New South Wales, covering the period from February 2000 to June 2004. The determination provides for a real price decrease equal to 16 per cent during the period, when averaged across the distribution GTEs in New South Wales.

COUNTRY ENERGY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			2 450	2 639	2 866
Total revenue	$m			1 417	1 497	1 635
Profitability						
Operating profit before tax	$'000			25 112	55 439	140 710
Operating sales margin	%			8.2	10.6	15.3
Cost recovery	%			109.0	111.8	118.1
Return on assets	%			4.8	6.3	9.5
Return on equity	%			2.6	5.5	11.2
Financial management						
Debt to equity	%			199.5	215.7	210.6
Debt to total assets	%			54.7	57.3	57.5
Total liabilities to equity	%			264.8	290.7	296.0
Interest cover	times			1.3	1.5	2.3
Current ratio	%			42.9	51.4	47.9
Leverage ratio	%			364.8	390.7	396.0
Payments to and from government						
Dividends	$'000			19 827	29 557	29 764
Dividend to equity ratio	%			3.0	4.4	4.3
Dividend payout ratio	%			111.5	80.1	38.0
Income tax expense	$'000			7 335	18 550	62 371
CSO funding	$'000			18 508	21 962	22 666

a Country Energy was established on 1 July 2001, from the merger of NorthPower, Advance Energy and Great Southern Energy. **n.r.** Not relevant.

CS ENERGY — Queensland

CS Energy was established on 1 July 1997, as part of the restructure of the Queensland electricity industry.[1] It is subject to the provisions of the *Government Owned Corporations Act 1993* and the *Corporations Act 2001* (Cwlth). CS Energy operates power stations with a combined generating capacity of 3000 MW at three locations around Queensland. CS Energy generates electricity within the National Electricity Market (NEM).[2]

Over the five year reporting period, CS Energy's pre-tax operating profit fell by over 60 percent. In 2003-04, pre-tax operating profit was 30 per cent ($17 million) less than the previous year, with a 1 per cent ($4 million) decrease in revenue and a 3 per cent ($13 million) increase in expenses.

Debt to equity and debt to total assets ratios decreased substantially in 2003-04, improved by a 44 per cent ($296 million) fall in the level of debt, which was facilitated by a $260 million equity injection by the Queensland Government. The liquidity of CS Energy, as measured by the current ratio, improved in 2003-04, with an increase in current assets.

CS Energy is required to make tax-equivalent and dividend payments. CS Energy's dividend payment is determined in accordance with the provisions of the *Government Owned Corporations Act 1993*. Under the Act, the board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers may either approve the recommendation or direct the board to pay a specified dividend. In 2003-04, CS Energy provided for a $29 million dividend payment and recorded an income tax-equivalent expense of $10 million.

1 Prior to 1997, the assets of CS Energy formed part of Queensland's largest generator AUSTA Electric. On 1 July 1997, AUSTA Electric was separated into three generators — CS Energy, Stanwell Corporation, and Tarong Energy. An engineering services corporation was also established through the restructure.

2 The Queensland–New South Wales Interconnector commenced operation in February 2001. This improved the integration of the Queensland wholesale electricity market into the NEM. The NEM connects generation and transmission assets in New South Wales, Victoria, Queensland and South Australia.

CS ENERGY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	1 323	1 458	1 663	1 610	1 620
Total revenue	$m	480	452	494	479	475
Profitability						
Operating profit before tax	$'000	113 047	48 734	88 045	57 608	40 865
Operating sales margin	%	28.3	19.2	23.4	19.6	16.0
Cost recovery	%	134.8	123.7	130.5	124.4	119.0
Return on assets	%	11.2	6.2	7.4	5.7	4.7
Return on equity	%	13.9	4.8	10.0	6.6	4.1
Financial management						
Debt to equity	%	60.4	95.6	122.8	111.6	44.1
Debt to total assets	%	31.7	41.9	47.4	41.6	23.8
Total liabilities to equity	%	108.0	139.6	175.7	164.3	86.1
Interest cover	times	5.9	2.3	4.2	2.6	2.2
Current ratio	%	79.2	81.3	113.3	81.8	105.9
Leverage ratio	%	208.0	239.6	275.7	264.3	186.1
Payments to and from government						
Dividends	$'000	57 111	74 934	72 652	37 730	28 877
Dividend to equity ratio	%	9.3	12.0	12.0	6.2	3.9
Dividend payout ratio	%	66.7	251.3	119.7	95.0	95.0
Income tax expense	$'000	27 381	18 916	27 353	17 892	10 468
CSO funding	$'000	0	0	0	0	0

a Dividend includes $20.7 million attributed to 1998-99, but not provided for in that year. **b** Dividend includes $45.9 million attributed to 1999-00, but not provided for in that year. **c** Dividend includes $21 million attributed to 2000-01, but not provided for in that year.**d** In 2002-03, CS Energy adopted a new accounting policy whereby provision is made for a dividend if the dividend is declared prior to the end of the financial year. Previously provision could be made for a dividend if it was declared after the end of the financial year but before the completion of the financial report. The effect of adopting the new accounting standard is that $51 million in dividends previously attributed to 2001-02 have been recognised in the 2002-03 financial statement. This adjustment is not included in the figure recorded in this year's report to avoid double counting. **e** In 2003-04, CS Energy's level of debt was reduced through a $260 million equity injection by the Queensland Government.

STANWELL CORPORATION Queensland

Stanwell Corporation (Stanwell) was established on 1 July 1997, as part of the restructure of the Queensland electricity industry. It is subject to the provisions of the *Government Owned Corporations Act 1993* and the *Corporations Act 2001* (Cwlth).[1] Stanwell generates electricity for sale into the National Electricity Market (NEM).[2]

Stanwell operates the Stanwell coal-fired station and several gas, bio-mass, hydro and wind generation plants with a combined generating capacity in excess of 1640 MW.

Stanwell's pre-tax operating profit increased 3 per cent ($2 million) in 2003-04 after falling 63 per cent ($103 million) from 1999-00 to 2002-03. The previous fall in profits was mainly caused by new generation, particularly low-cost baseload plants, entering the Queensland energy market in recent years.

Despite a 6 per cent ($103 million) reduction in the value of Stanwell's assets, the debt to equity and debt to total asset ratios fell in 2003-04, following a 5 per cent reduction in the level of debt held. Debt levels have declined steadily throughout the reporting period. The current ratio, which reflects Stanwell's liquidity, worsened in 2003-04, with a 55 per cent fall in current assets more than offsetting a 39 per cent decrease in current liabilities.

Stanwell is required to make tax-equivalent and dividend payments. Stanwell's dividend payments are determined in accordance with the provisions of the *Government Owned Corporations Act 1993*.[3] In 2003-04, Stanwell provided for a $39 million dividend payment and recorded an income tax-equivalent expense of $21 million.

1 Prior to 1997, the assets of Stanwell formed part of Queensland's largest generator AUSTA Electric. On 1 July 1997, AUSTA Electric was separated into three generators — CS Energy, Stanwell and Tarong Energy. An engineering services corporation was also established through the restructure.

2 The Queensland–New South Wales Interconnector commenced operation in February 2001. This integrated the Queensland wholesale electricity market into the NEM. The NEM is serviced by generation and transmission assets in New South Wales, Victoria, Queensland and South Australia.

3 Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers may either approve the recommendation or direct the Board to pay a specified dividend.

STANWELL CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*	*2003-04*
Size						
Total assets	$m	1 693	1 660	1 666	1 693	1 590
Total revenue	$m	431	416	361	373	360
Profitability						
Operating profit before tax	$'000	162 454	138 608	77 864	59 430	61 237
Operating sales margin	%	44.3	38.9	26.5	20.7	20.2
Cost recovery	%	179.4	163.8	136.0	126.1	125.2
Return on assets	%	11.3	9.7	5.8	4.7	4.6
Return on equity	%	13.0	9.4	5.3	4.1	4.0
Financial management						
Debt to equity	%	36.1	34.0	33.6	33.1	23.2
Debt to total assets	%	21.8	20.9	20.3	19.9	14.3
Total liabilities to equity	%	64.1	61.0	65.7	68.0	57.4
Interest cover	times	6.4	6.7	5.2	4.1	5.3
Current ratio	%	74.2	65.1	85.8	116.3	86.5
Leverage ratio	%	164.1	161.0	165.7	168.0	157.4
Payments to and from government						
Dividends	$'000	123 591	98 097	71 020	39 479	38 691
Dividend to equity ratio	%	12.0	9.5	7.0	3.9	3.8
Dividend payout ratio	%	92.8	101.4	130.6	95.0	95.0
Income tax expense	$'000	29 218	41 831	23 477	17 866	20 508
CSO funding	$'000	0	0	0	0	0

a Dividend includes $27.8 million attributed to 1998-99 but not provided for in that year. Dividend also includes a proposed final dividend attributed to 1999-00 of $96 million. **b** Dividend includes $25.5 million attributed to 1999-00 but not provided for in that year. **c** Dividend includes $19.4 million attributed to 2000-01 but not provided for in that year. Also includes a final dividend of $52 million attributed to 2001-02.

TARONG ENERGY Queensland

Tarong Energy (Tarong) was established on 1 July 1997, as part of the restructure of the Queensland electricity industry. It is subject to the provisions of the *Government Owned Corporations Act 1993* and the *Corporations Act 2001* (Cwlth).[1] Tarong generates electricity for sale into the National Electricity Market (NEM).[2] Tarong also owns and operates the South Australian gas supplier, Terra Gas Trader.[3]

Tarong operates power stations (two coal-fired, one gas turbine, one hydro and one wind) with a combined generating capacity of 2395 MW. In 2002-03, Tarong Energy entered into a joint-venture with two Japanese companies TEPCO and Mitsui. Under the joint-venture agreement, which came into effect in August 2003, TEPCO and Mitsui acquired a 50 per cent interest in Tarong North Power Station.

Despite a 1 per cent ($5 million) fall in revenue, Tarong's pre-tax operating profit increased by 7 per cent ($8 million) to over $123 million in 2003-04. This was caused by a 3 per cent ($13 million) reduction in expenses for the year — primarily due to lower costs associated with production of electricity and the distribution of gas by Terra Gas Trader.

The value of Tarong's assets decreased by 18 per cent ($359 million) in 2003-04, with asset disposals of $310 million. A 56 per cent ($381 million) reduction in Tarong's level of debt — financed mainly with proceeds from the sale of non-current assets associated with the joint venture-agreement — resulted in its debt to equity and debt to total assets ratios falling in 2003-04, reversing an upward trend evident since 1999-00.

Tarong Energy is required to make tax-equivalent and dividend payments. In 2003-04, Tarong provided for a dividend payment of almost $82 million and recorded an income tax-equivalent expense of over $37 million.

1 Prior to 1997, the assets of Tarong Energy formed part of Queensland's largest generator AUSTA Electric. On 1 July 1997, AUSTA Electric was separated into three generators — CS Energy, Stanwell Corporation and Tarong Energy. An engineering services corporation was also established through the restructure.

2 The Queensland–New South Wales Interconnector commenced operation in February 2001. This integrated the Queensland wholesale electricity market into the NEM. The NEM is serviced by generation and transmission assets in New South Wales, Victoria, Queensland and South Australia.

3 Terra Gas Trader was sold in January 2005.

TARONG ENERGY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*	*2003-04*[d]
Size						
Total assets	$m	1 418	1 604	1 874	1 957	1 598
Total revenue	$m	440	562	602	611	606
Profitability						
Operating profit before tax	$'000	142 633	136 186	137 702	115 643	123 371
Operating sales margin	%	35.9	27.9	23.6	19.8	23.1
Cost recovery	%	156.1	138.8	130.9	124.7	130.1
Return on assets	%	11.8	10.5	8.2	6.4	8.1
Return on equity	%	13.2	10.7	11.3	9.5	10.1
Financial management						
Debt to equity	%	27.1	48.7	70.5	79.5	34.5
Debt to total assets	%	17.8	28.1	34.4	35.4	16.6
Total liabilities to equity	%	61.2	84.3	121.0	129.6	86.6
Interest cover	times	9.9	7.0	27.1	18.1	6.8
Current ratio	%	56.6	57.0	67.2	24.9	54.2
Leverage ratio	%	161.2	184.3	221.0	229.6	186.6
Payments to and from government						
Dividends	$'000	96 330	102 515	129 711	76 562	81 608
Dividend to equity ratio	%	11.2	11.7	15.1	9.0	9.6
Dividend payout ratio	%	84.7	109.7	133.7	95.0	95.0
Income tax expense	$'000	28 946	42 759	40 715	35 052	37 469
CSO funding	$'000	0	0	0	0	0

a Non-current assets were revalued downwards by $9.9 million. Dividend includes $31 million that was attributed to 1998-99 but not provided for in that year. Also includes a proposed final dividend of $65 million attributed to 1999-00. **b** Tarong Energy acquired South Australian-based Terra Gas Trader on 31 October 2000, increasing Tarong Energy's asset base, revenue and expenses. Dividend includes $38 million that was attributed to 1999-00 but not provided for in that year. Also includes a proposed final dividend of $64 million attributed to 2000-01. **c** Dividend includes $37.5 million that was attributed to 2000-01 but was not provided for in that year. **d** Under a joint-venture agreement which came into effect on 6 August 2003, TEPCO and Mitsui have acquired a 50 per cent interest in Tarong North Power Station. Proceeds from the sale of non-current assets, associated with the joint venture-agreement, were used to fund a reduction in Tarong's level of debt in 2003-04.

ENERTRADE — Queensland

The Queensland Power Trading Corporation (QPTC) commenced operations as Queensland Transitional Power Trading Corporation on 1 July 1997 following a restructure of Queensland's electricity supply industry. It became QPTC, trading as Enertrade, in October 2000. Enertrade is subject to the provisions of the *Government Owned Corporations Act 1993*. It trades electricity — purchased under fixed contracts from privately-owned power stations — into the National Electricity Market (NEM).

A number of Enertrade's long-term, power-purchase agreements (PPAs) constitute onerous contracts and are expected to result in significant future losses. The agreements commit Enertrade to purchasing power at fixed prices over their term and selling it into the NEM at prevailing (currently lower) pool prices.[1]

On 1 July 2002, Enertrade applied accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*, for the first time. As a result, Enertrade made provision for estimated future losses related to its PPAs, totalling $485.6 million. Under this standard, the carrying amount of the provision must be revised annually to the best estimate as at the reporting date, which will depend on future changes in the market prices for electricity.[2]

In 2003-04, Enertrade recorded a pre-tax operating loss of $20 million — close to the same amount recorded in the previous year. A 9 per cent ($42 million) decrease in expenses, associated mainly with the annual adjustment to the provision for onerous contracts, was balanced by a 9 per cent ($40 million) decline in revenue, which continues a trend evident over the reporting period.

The value of Enertrade's assets increased by 7 per cent ($28 million) in 2003-04, mainly from an increase in property, plant and equipment.

The provision for onerous contracts had a significant effect on Enertrade's financial indicators. In particular, the provision caused liabilities to exceed assets, resulting in negative values for ratios that are related to equity.

Enertrade is required to make tax-equivalent and dividend payments. No dividend or tax-equivalent payments have been made since 2000-01 because of pre-tax operating losses.

1 The longest of these contracts is for a term of 35 years, which extends to 2029.

2 The provision is recorded as a liability in the Statement of Financial Position and the annual revision is recognised as an expense in the Statement of Financial Performance.

ENERTRADE (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*[b]	*2003-04*
Size						
Total assets	$m	310	273	265	413	441
Total revenue	$m	680	625	472	434	393
Profitability						
Operating profit before tax	$'000	30 602	- 14 332	- 48 997	- 21 350	- 19 827
Operating sales margin	%	4.3	- 2.7	- 10.7	- 6.3	- 6.6
Cost recovery	%	103.7	97.4	90.4	94.1	93.8
Return on assets	%	8.2	- 3.1	- 16.7	- 5.0	- 3.6
Return on equity	%	7.4	- 16.5	- 65.2	n.r.[c]	n.r.[c]
Financial management						
Debt to equity	%	88.7	95.1	196.5	-64.0	- 157.8
Debt to total assets	%	20.3	33.0	35.8	28.4	22.5
Total liabilities to equity	%	214.2	169.8	440.1	- 374.8	- 822.6
Interest cover	times	7.3	- 1.7	- 11.1	- 4.0	- 3.3
Current ratio	%	201.5	269.9	164.6	330.2	248.0
Leverage ratio	%	314.2	269.8	540.1	- 274.8	- 722.6
Payments to and from government						
Dividends	$'000	15 444	0	0	0	0
Dividend to equity ratio	%	6.2	0.0	0.0	0.0	0.0
Dividend payout ratio	%	83.5	0.0	0.0	0.0	0.0
Income tax expense	$'000	12 114	2 123	0	0	0
CSO funding	$'000	0	0	0	0	0

a On 29 June 2000, 307 million ordinary shares were cancelled and offset against a loan receivable from the Shareholding Ministers. Includes an abnormal gain of $5.7 million related to the write-back of provision for settlement of disputes. **b** In 2002-03, the Queensland Government injected $300 million of contributed equity into Enertrade. In 2002-03, Enertrade had negative equity, largely as a result of a provision for onerous contracts related to power purchasing agreements. **c** Liabilities exceeded assets. **n.r**. Not relevant.

POWERLINK Queensland

Powerlink was established on 1 July 1997 as part of a restructure of the Queensland electricity industry. It is subject to the provisions of the *Government Owned Corporations Act 1993* and the *Corporations Act 2001* (Cwlth). Powerlink owns and controls the Queensland high voltage transmission network and operates in the National Electricity Market (NEM).[1]

Powerlink has minority equity interests in ElectraNet, a provider of electricity transmission services in South Australia, and Electranet Transmission Services — a provider of asset management services.

The Australian Competition and Consumer Commission is responsible for determining the allowable revenue applying to Powerlink's regulated transmission assets.[2]

Pre-tax operating profit rose by 20 per cent ($23 million) to $135 million in 2003-04, with a 5 per cent ($149 million) increase in revenue and a 6 per cent ($17 million) increase in expenses.

Assets increased by 5 per cent (or $149 million) to $3.2 billion in 2003-04, mainly through an increase in the value of property, plant and equipment. Asset additions of $187 million and upward revaluations totalling $63 million, more than offset depreciation ($109 million).

Under the provisions of the *Government Owned Corporations Act 1993*, Powerlink is required to make tax-equivalent and dividend payments. Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers may either approve the recommendation or direct the Board to pay a specified dividend. In 2003-04, Powerlink provided for a $88 million dividend payment and recorded an income tax-equivalent expense of $43 million.

1 The Queensland–New South Wales Interconnector commenced operation in February 2001, integrating the Queensland wholesale electricity market into the NEM. The NEM is serviced by generation and transmission assets in New South Wales, Victoria, Queensland and South Australia.

2 Prior to 1 January 2002, transmission prices were regulated by the Queensland Office of Energy.

POWERLINK (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	2 554	2 588	2 821	3 052	3 201
Total revenue	$m	300	339	362	385	425
Profitability						
Operating profit before tax	$'000	89 254	112 611	101 271	112 016	135 426
Operating sales margin	%	46.0	56.9	45.2	46.2	47.8
Cost recovery	%	222.7	231.8	182.5	185.9	191.7
Return on assets	%	6.4	7.6	6.2	6.3	6.7
Return on equity	%	7.1	15.4	6.2	5.7	6.5
Financial management						
Debt to equity	%	86.1	101.1	99.9	97.1	96.5
Debt to total assets	%	48.0	44.5	47.2	46.0	45.2
Total liabilities to equity	%	113.8	128.9	120.6	119.3	118.6
Interest cover	times	2.8	2.3	2.5	2.6	2.8
Current ratio	%	142.3	42.0	67.8	73.0	59.0
Leverage ratio	%	213.8	228.9	220.6	219.3	218.6
Payments to and from government						
Dividends	$'000	72 441	165 644	70 545	72 855	87 924
Dividend to equity ratio	%	7.4	14.2	5.9	5.5	6.2
Dividend payout ratio	%	104.4	92.3	95.0	95.0	95.0
Income tax expense	$'000	19 846	- 66 940	27 012	35 330	42 870
CSO funding	$'000	0	0	0	0	0

a Includes abnormal expenses of $28 million relating to sales — tax-equivalent payments ($27 million) and year 2000 compliance costs ($1.4 million). The growth in assets reflects capital expenditure of $245 million and an increase in asset values of $774 million following a revaluation of supply system assets, freehold land and buildings. Powerlink made a $150 million loan to the Queensland Government. Income tax-equivalent payments were reduced by $18 million due to a fall in the future company tax rate. **b** Powerlink received an income tax benefit of almost $67 million. This was primarily due to the Cross-Border Lease entered into during the year, which reduced tax-equivalent payments by $113 million. The Queensland Government reduced its equity stake by $150 million, completing a debt for equity swap which commenced in 1999-00.

ERGON ENERGY GROUP Queensland

The Ergon Energy Group (Ergon) comprises Ergon Energy Corporation Ltd, a regulated electricity distributor, and Ergon Energy Pty Ltd, an energy retailer. Ergon was established on 30 June 1999, through the amalgamation of six regional distribution corporations and their retail subsidiary, Ergon Energy Pty Ltd.[1] Ergon is subject to the provisions of the *Government Owned Corporations Act 1993* and the *Corporations Act 2001* (Cwlth).

Ergon is regulated by the Queensland Competition Authority, which sets the maximum allowable revenue that it can earn through network access tariffs and charges. The prices that it can charge non-contestable customers for electricity are set by the Minister for Energy under the *Electricity Act 1994*.[2]

Pre-tax operating profit increased by less that 1 per cent ($1 million) in 2003-04, with a 4 per cent ($56 million) rise in revenue almost entirely offset by a 4 per cent ($55 million) increase in expenses.

In 2003-04, the value of Ergon's assets rose by 13 per cent ($429 million) to almost $3.9 billion, with asset additions of almost $775 million. This increase contributed to improvements in Ergons's debt to equity and debt to total assets ratios.

Ergon is required to make tax-equivalent and dividend payments. Its dividend payment is determined in accordance with the provisions of the *Government Owned Corporations Act 1993*. Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers may either approve the recommendation or direct the Board to pay a specified dividend. In 2003-04, Ergon paid $87 million in dividend payments and $36 million in tax-equivalent payments.

Ergon receives CSO payments to cover any shortfall incurred in supplying electricity to non-contestable customers at gazetted tariffs. Ergon received $224 million in CSO payments in 2003-04.

1 The six regional distribution corporations were the Far North Queensland Electricity Corporation, North Queensland Electricity Corporation, Mackay Electricity Corporation, Capricornia Electricity Corporation, Wide Bay–Burnett Electricity Corporation and South-West Queensland Electricity Corporation. The retail subsidiary, Ergon Energy Pty Ltd, was formed in February 1998, following the merger of Northern Electricity Retail Corporation and Central Electricity Retail Corporation.

2 Queensland does not have full retail contestability. Customers who use no more than 200 MWh a year cannot choose between electricity retailers. The Queensland Government aims to ensure consistent State-wide retail tariffs for non-contestable customers, regardless of the cost of supply.

ERGON ENERGY CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*[b]	*2003-04*
Size						
Total assets	$m	2 786	3 211	3 392	3 423	3 852
Total revenue	$m	1 323	1 418	1 442	1 499	1 555
Profitability						
Operating profit before tax	$'000	45 779	89 262	116 155	126 913	128 392
Operating sales margin	%	7.6	10.5	12.7	13.5	13.5
Cost recovery	%	110.1	110.6	114.6	115.5	115.6
Return on assets	%	3.9	5.1	5.7	6.0	5.9
Return on equity	%	4.1	6.2	6.0	7.1	5.7
Financial management						
Debt to equity	%	100.4	81.6	88.2	98.1	85.1
Debt to total assets	%	39.1	39.0	39.4	42.6	41.0
Total liabilities to equity	%	156.4	124.2	130.3	131.5	120.1
Interest cover	times	1.7	2.4	2.6	2.6	2.5
Current ratio	%	111.3	112.9	139.6	136.5	155.4
Leverage ratio	%	256.4	224.2	230.3	231.5	220.1
Payments to and from government						
Dividends	$'000	38 928	69 305	73 702	119 311	87 413
Dividend to equity ratio	%	3.6	5.5	5.1	8.1	5.4
Dividend payout ratio	%	86.8	89.1	85.1	113.4	95.0
Income tax expense	$'000	917	11 505	29 506	21 736	36 377
CSO funding	$'000	244 768	232 354	188 456	191 798	223 596

a Includes an abnormal expense of $20 million relating to sales tax. **b** Dividend includes $20 million special dividend payment. **n.r.** Not relevant.

ENERGEX — Queensland

The South East Queensland Electricity Corporation Limited commenced operations on 1 July 1997. The company name was changed to ENERGEX Limited on 15 December 1998. It is subject to the provisions of the *Government Owned Corporations Act 1993* and the *Corporations Act 2001* (Cwlth).

ENERGEX distributes electricity and gas in Queensland. The company includes two wholly-owned subsidiary companies, ENERGEX Retail — which retails gas and electricity, to contestable customers throughout the National Electricity Market — and Allgas Energy.

ENERGEX's electricity distribution network is regulated by the Queensland Competition Authority, which sets the maximum allowable revenue that it can earn through network access tariffs and charges. Non-contestable customer prices are determined by the Minister for Energy under the *Electricity Act 1994*.[1]

Pre-tax operating profit increased by 28 per cent ($53 million) in 2003-04. This was attributable to a 6 per cent ($136 million) increase in sales revenue — associated with sales growth in electricity and natural gas — and an increase in the value of services rendered.

The value of total assets increased by 6 per cent ($248 million) in 2003-04. This was mainly a result of capital expenditure on additional property, plant and equipment.

ENERGEX is required to make tax-equivalent and dividend payments. Under the *Government Owned Corporations Act 1993*, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers may either approve the recommendation or direct the Board to pay a specified dividend. In 2003-04, ENERGEX provided for a $148 million dividend payment and recorded an income tax-equivalent expense of $84 million.[2]

ENERGEX receives CSO payments to cover any shortfall incurred in supplying electricity to its non-contestable customers at gazetted tariffs, as well as for the payment and administration of pensioner rebates.

1 Unlike Victoria and New South Wales, Queensland does not have full retail contestability. Customers who use no more than 200 MWh a year are not permitted to choose between electricity retailers. The Queensland Government aims to ensure consistent State-wide retail tariffs for non-contestable customers, regardless of the cost of supply.

2 The 2003-04 dividend was provided on the basis of 95 per cent of its after-tax profit.

ENERGEX (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*
Size						
Total assets	$m	3 237	3 708	3 902	4 241	4 489
Total revenue	$m	1 736	1 908	1 950	2 142	2 278
Profitability						
Operating profit before tax	$'000	41 121	116 096	170 443	186 469	239 069
Operating sales margin	%	6.9	11.0	12.4	13.4	14.8
Cost recovery	%	104.9	109.7	114.2	115.5	117.4
Return on assets	%	4.0	6.3	6.6	7.2	7.9
Return on equity	%	3.3	6.8	6.5	8.8	9.7
Financial management						
Debt to equity	%	128.2	97.2	119.4	123.6	121.6
Debt to total assets	%	50.3	44.9	47.6	48.0	44.7
Total liabilities to equity	%	166.1	131.1	157.2	168.1	179.6
Interest cover	times	1.5	2.1	3.2	2.7	3.3
Current ratio	%	197.6	125.8	137.8	147.3	133.3
Leverage ratio	%	266.1	231.1	257.2	268.1	279.6
Payments to and from government						
Dividends	$'000	43 051	102 520	246 319	158 909	147500
Dividend to equity ratio	%	3.5	7.3	15.8	10.3	9.3
Dividend payout ratio	%	105.2	107.1	243.0	117.1	95.0
Income tax expense	$'000	209	20 381	69 060	50 780	83800
CSO funding	$'000	23 597	24 626	27 419	29 600	32500

a Includes abnormal expenses related to a write-down in the value of land and buildings ($4.7 million), a change in sales tax exemption status ($1.7 million), loss on disposal of assets from a discontinued project ($1.8 million) and year 2000 compliance costs ($1.8 million). Dividend includes a $12.5 million payment attributed to 1998-99 but not provided for in that year. Also includes a proposed final payment of $31 million attributed to 1999-00. **b** ENERGEX revalued its supply system, upon adoption of AASB 1041, resulting in a revaluation increment of $495 million to non-current assets. Includes expenses of $12 million relating to redundancy restructuring and development costs. Dividend includes an $8.2 million payment attributed to 1999-00 but not provided for in that year. Also includes a proposed final dividend of $94 million attributed to 2000-01. **c** Includes expenses of $27 million relating to a write-down of investments, and redundancy and restructuring costs. Dividends include a $150 million special dividend **d** Dividends include a $30 million special dividend.

WESTERN POWER — Western Australia

Western Power is a government-owned corporation established under the *Electricity Corporation Act 1994*. Western Power operates four major and 24 smaller power stations with a total capacity of 3500 MW — 56 per cent of WA's total generation capacity.[1] Western Power is also involved in the transmission and retailing of electricity.[2]

An independent enquiry was undertaken into the events surrounding a power restriction incident, which occurred in February 2004. The Committee of the review reported in late April 2004, making a number of adverse findings against Western Power and a series of recommendations. All of these recommendations were accepted and will be implemented.

In 2003-04, Western Power's pre-tax operating profit was more than 17 per cent ($55 million) higher than in the previous year, reflecting a rise in revenue of more than 4 per cent ($77 million).

Western Power has carried a high level of debt over the reporting period, as reflected in its debt to equity and debt to total assets ratios. These ratios fell slightly in 2003-04, with a 4 per cent ($176 million) increase in the value of Western Power's assets. Capital expenditure was almost $327 million in 2003-04, down from the previous year's high of $473 million, directed mainly at new generation and network infrastructure.

Western Power makes dividend and income tax-equivalent payments to the State Government. In 2003-04, Western Power provided for a $104 million dividend payment and recorded an income tax-equivalent expense of almost $110 million.

Western Power received an entitlement of $35 million for the performance of CSOs in 2003-04.

1 Western Power operates and maintains all but one of the major power stations, the exception being Collie Power station, which is operated and maintained by a private operator.

2 Western Power's customers are supplied through two major interconnected systems — one in the South–West corner of Western Australia and the other in the Pilbara in the North. Western Power also operates 28 separate systems in remote parts of the State.

WESTERN POWER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	4 038	4 180	4 231	4 407	4 583
Total revenue	$m	1 575	1 597	1 623	1 725	1 802
Profitability						
Operating profit before tax	$'000	230 294	289 138	302 697	319 979	375 183
Operating sales margin	%	28.1	28.1	28.1	26.9	29.0
Cost recovery	%	147.2	139.2	139.1	136.8	140.6
Return on assets	%	11.0	11.0	10.9	10.8	11.6
Return on equity	%	12.9	15.3	15.6	15.0	17.0
Financial management						
Debt to equity	%	195.9	188.7	160.3	162.2	145.2
Debt to total assets	%	60.4	57.5	55.5	57.0	51.7
Total liabilities to equity	%	224.9	233.7	190.8	190.5	186.1
Interest cover	times	2.1	2.8	3.0	3.2	3.5
Current ratio	%	41.9	133.5	117.6	112.4	110.7
Leverage ratio	%	324.9	333.7	290.8	290.5	286.1
Payments to and from government						
Dividends	$'000	46 209	94 100	116 972	114 050	103 513
Dividend to equity ratio	%	4.1	7.5	8.6	7.7	6.6
Dividend payout ratio	%	31.5	49.3	55.3	51.1	39.0
Income tax expense	$'000	83 828	98 121	91 342	96 901	109 604
CSO funding	$'000	27 000	28 700	31 400	34 600	34 700

a Includes abnormal revenue relating to adjustments for debtors with unread meters ($28 million). This was offset by abnormal expenses relating to refinancing costs ($47 million), redundancy costs ($27 million) and decommissioning costs ($8 million). A fall in the future company tax rate reduced income tax-equivalent payments by $7.8 million. **b** The dividend payment in 2000-01 was comprised of a $47 million interim dividend, paid on 29 June 2001 and provision for a $47 million dividend, to be paid during December 2001.

HYDRO-ELECTRIC CORPORATION — Tasmania

The Hydro-Electric Corporation (HEC) operates under the *Hydro-Electric Corporation Act 1995* and is subject to the provisions of the *Government Business Enterprises Act 1995*. On 1 July 1998, the HEC was disaggregated into three separate businesses — the HEC, Aurora Energy and Transend Networks.[1]

The HEC retained responsibility for electricity generation on mainland Tasmania and for generation, distribution and retailing on the Bass Straight Islands.[2] The maximum prices that can be charged by the HEC are determined by the Office of the Tasmanian Energy Regulator.[3]

The HEC's revenue and expenses were both 11 per cent higher than in the previous year. Overall, this led to a 6 per cent ($4 million) increase in pre-tax operating profit in 2003-04.

The value of HEC's assets increased by 1 per cent ($40 million) in 2003-04, with capital expenditure of $133 million. The value of HEC's assets and debts have remained largely unchanged over the reporting period, resulting in stable debt to equity, debt to total asset and current ratios.

The HEC is required to make tax-equivalent and dividend payments to the Tasmanian Government. In 2003-04, the HEC paid a $43 million dividend, including a $26 million special dividend,[4] and recorded an income tax-equivalent expense of $37 million.

Throughout the reporting period, the HEC has received CSO payments for the provision of concessional arrangements to customers living on the Bass Strait Islands. In 2003-04, CSO payments amounted to $4.7 million.

1 Prior to disaggregation, the HEC had sole responsibility for the generation, transmission and sale of electricity in Tasmania. Transend Networks is now responsible for electricity transmission and Aurora Energy is responsible for electricity distribution and retailing.

2 Delivery of services to the Bass Straight Islands has been contracted to Aurora Energy.

3 In 1999-00, OTER determined maximum prices that HEC could charge from 1 January 2000 to 31 December 2002. This price determination was later extended to December 2003. The arrangement has subsequently been further extended by contract between HEC and Aurora Energy. This contract set in place pricing arrangements up to March 2007.

4 This dividend payment refers to 2002-03. The HEC Board proposed a dividend of $40 million for 2003-04, including a special dividend of $17.4 million, which will be included in the 2004-05 financial report.

HYDRO-ELECTRIC CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*[c]	*2003-04*[d]
Size						
Total assets	$m	3 250	3 342	3 515	3 568	3 598
Total revenue	$m	323	332	371	397	439
Profitability						
Operating profit before tax	$'000	1 676	46 284	60 056	68 100	71 981
Operating sales margin	%	31.5	40.2	36.0	38.0	32.9
Cost recovery	%	164.3	165.2	154.3	159.6	148.4
Return on assets	%	3.2	4.1	3.9	4.3	4.0
Return on equity	%	0.4	0.8	1.4	1.7	1.7
Financial management						
Debt to equity	%	57.5	55.0	52.1	50.2	52.1
Debt to total assets	%	32.1	31.5	30.2	29.3	30.2
Total liabilities to equity	%	80.4	77.2	76.8	72.9	73.5
Interest cover	times	1.0	1.5	1.8	1.8	2.0
Current ratio	%	25.2	27.6	32.5	25.9	24.4
Leverage ratio	%	180.4	177.2	176.8	172.9	173.5
Payments to and from government						
Dividends	$'000	45 062	49 230	60 503	0	43 553
Dividend to equity ratio	%	2.6	2.7	3.1	0.0	2.1
Dividend payout ratio[e]	%	623.9	323.4	217.6	0.0	123.3
Income tax expense	$'000	- 5 547	31 060	32 252	34 453	36 661
CSO funding	$'000	4 551	4 914	5 356	5 238	4748

a The HEC reported an abnormal expense of $27 million related to debt restructuring. Includes an asset valuation increase of $129 million. **b** Includes debt restructuring expenses relating to the repurchase of loans ($6.8 million) and the termination of interest rate swaps ($670 000). Includes an abnormal income tax item ($22.5 million) relating to the restatement of deferred tax balances due to a change in the income tax rate. Includes an asset revaluation increment of $74 million. **c** 2002-03 the HEC changed its policy regarding dividend payments in accordance with accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*. Under this standard, dividends are recognised at the time they are declared, determined or publicly recommended. In August 2003 the HEC Board proposed a dividend payment of $43 million, including a $26 million special dividend. This dividend payment is reported for 2003-04. **d** The HEC Board proposed a dividend of $40 million for 2003-04, including a special dividend of $17.4 million. This dividend payment will be included in the 2004-05 financial report. **e** The high dividend payout ratios are due to payment of special dividends throughout the reporting period.

AURORA ENERGY — Tasmania

Aurora Energy Pty Ltd (Aurora) was established on 1 July 1998, following the dissaggregation of the Hydro-Electric Corporation (HEC).[1] Aurora is incorporated under the *Corporations Act 2001* (Cwlth), pursuant to the *Electricity Companies Act 1997*.

Aurora is mainland Tasmania's only electricity distribution and retail company. It also holds retail licences for electricity in New South Wales and Victoria.[2] Aurora's charges are regulated by the Office of the Tasmanian Energy Regulator (OTER).[3]

Aurora's pre-tax operating profit decreased by 2 per cent ($1 million) in 2003-04 to less than $46 million, owing to a 6 per cent ($33 million) increase in expenses. This increase in expenses is mainly attributable to an increase in the value of energy and transmission purchases.

Aurora's debt to equity and debt to total assets ratios have declined over the reporting period, due mainly to increases in the value of total assets. The value of Aurora's assets increased by 7 per cent ($59 million) in 2003-04.

Aurora is required to make dividend and tax-equivalent payments to the Tasmanian Government. In 2003-04, Aurora provided for a $15 million dividend payment and recorded an income tax-equivalent expense of $18 million.

Aurora receives CSO payments for providing pensioners with discounted electricity. In 2003-04, Aurora received $11 million in CSO payments.

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1 Prior to disaggregation, the HEC had sole responsibility for the generation, transmission and sale of electricity in Tasmania. Transend Networks is now responsible for electricity transmission and Aurora is responsible for electricity distribution and retailing. Aurora also delivers services on Bass Strait Islands under sub-contract for the HEC.

2 Since disaggregation, Aurora has broadened its range of products and services. In 2001-02, it entered an alliance with Signature Security Group for the purpose of marketing security products. This follows the establishment of a telecommunications joint-venture (TasTel) in 2000-01, and the formation of a subsidiary company — EziKey — to market its bill paying system. Aurora Gas Pty Ltd was formed as a wholly owned subsidiary in February 2002 to participate in the Tasmanian gas supply tendering process.

3 On 1 January 2004 a new electricity pricing framework was implemented to set the retail pricing structure until December 2006 and distribution prices until December 2007. The OTER approved average increases of the CPI plus 0.8 per cent for the 2004 calendar year, with increases at or slightly above the rate of inflation in 2005 and 2006. At the same time, the OTER imposed a cut in Aurora's retail margin and imposed a lower cap on earnings from electricity distribution.

AURORA ENERGY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*	*2003-04*[c]
Size						
Total assets	$m	765	792	836	864	923
Total revenue	$m	551	572	587	631	663
Profitability						
Operating profit before tax	$'000	29 105	37 002	40 139	46 761	45 648
Operating sales margin	%	12.7	12.3	11.6	11.8	10.7
Cost recovery	%	114.7	114.0	113.1	113.4	112.0
Return on assets	%	9.3	9.2	8.4	8.9	8.1
Return on equity	%	8.6	8.0	11.1	9.0	7.7
Financial management						
Debt to equity	%	158.8	143.9	127.0	107.9	97.4
Debt to total assets	%	49.5	48.6	46.4	43.1	41.0
Total liabilities to equity	%	221.2	201.0	180.8	154.7	145.6
Interest cover	times	1.7	2.1	2.4	2.6	2.7
Current ratio	%	76.7	55.2	80.3	88.6	72.7
Leverage ratio	%	321.2	301.0	280.8	254.7	245.6
Payments to and from government						
Dividends [b]	$'000	10 052	10 244	12 567	0	14 754
Dividend to equity ratio	%	4.3	4.1	4.5	0.0	0.1
Dividend payout ratio	%	50.0	50.8	40.5	0.0	53.8
Income tax expense	$'000	9 002	16 856	9 082	17 995	18 225
CSO funding	$'000	9 797	9 727	9 745	13 005	11 319

a Aurora Energy reported abnormal expenses of $2.9 million relating to redundancy and retirement payments, rebranding costs, costs associated with year 2000 compliance and the Goods and Services Tax implementation. This was offset by abnormal revenue of $2.3 million for a reversal of superannuation provisions. **b** In 2002-03, Aurora changed its policy regarding dividend recognition in accordance with accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*. Under this standard dividends are recognised at the time they are declared, determined or publicly recommended (see chapter 3 for details). **c** The Aurora Board recommended a dividend of $14 million for 2003-04. This dividend payment will be included in the 2004-05 report.

TRANSEND NETWORKS Tasmania

Transend Networks (Transend) was established on 1 July 1998, following the dissaggregation of the Hydro-Electric Corporation (HEC).[1] Transend is incorporated under the *Corporations Act 2001* (Cwlth), pursuant to the *Electricity Companies Act 1997*.

Transend owns and operates the high voltage electricity transmission system in Tasmania, which includes almost 3500 km of overhead transmission lines, 45 substations and 8 switching stations.

On 1 July 2000, Transend assumed the role of system controller for the Tasmanian electricity network from the HEC, making it responsible for maintaining power system security and assisting with power system planning.

As part of Tasmania's entry into the National Electricity Market — planned for May 2005 — the Australian Competition and Consumer Commission (ACCC) began regulation of Transend's transmission network from 1 January 2004. In December 2003, the ACCC released its decision on Transend's regulated revenue cap until 30 June 2009. The decision provides for Transend's transmission charges to be increased by an average of 9 per cent per annum.

In 2003-04, the value of Transend's assets increased by 7 per cent ($45 million) to $649 million, with $48 million in additions to transmission lines and substations.

Compared to the previous year, Transend's pre-tax operating profit was 19 per cent ($5 million) higher in 2003-04. This was the net result of a 17 per cent ($14 million) increase in revenue and a 15 per cent ($9 million) increase in expenses.

Transend's debt to equity and debt to total asset ratios both increased in 2003-04 after also increasing the previous year. These increases were caused by a 46 per cent ($8 million) and a 38 per cent ($10 million) increase in the level of debt in 2002-03 and 2003-04 respectively. However, Transend's level of debt remains low compared to other electricity GTEs.

Transend is required to make dividend and tax-equivalent payments to the Tasmanian Government. In 2003-04, Transend provided for an $8 million dividend payment and recorded an income tax-equivalent expense of $12 million.

1 Prior to disaggregation, the HEC had sole responsibility for the generation, transmission and sale of electricity in Tasmania. Transend Networks is now responsible for electricity transmission and Aurora Energy is responsible for electricity distribution and retailing.

TRANSEND NETWORKS (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*[c]
Size						
Total assets	$m	437	464	593	604	649
Total revenue	$m	68	78	81	83	97
Profitability						
Operating profit before tax	$'000	34 220	22 407	28 637	27 155	32 199
Operating sales margin	%	51.6	30.6	36.7	33.7	35.3
Cost recovery	%	206.5	144.0	158.1	150.8	154.6
Return on assets	%	8.3	5.3	5.6	4.7	5.5
Return on equity	%	6.2	2.6	4.3	3.1	3.7
Financial management						
Debt to equity	%	5.2	3.9	3.3	4.9	6.4
Debt to total assets	%	4.6	3.5	3.3	4.3	5.6
Total liabilities to equity	%	16.8	17.4	13.3	15.6	17.6
Interest cover	times	41.4	16.4	25.8	28.7	16.7
Current ratio	%	27.3	35.8	39.8	62.9	33.2
Leverage ratio	%	116.8	117.4	113.3	115.6	117.6
Payments to and from government						
Dividends	$'000	11 199	10 091	9 837	0	8 183
Dividend to equity ratio	%	3.1	2.6	2.1	0.0	1.5
Dividend payout ratio	%	50.0	100.2	50.0	0.0	41.2
Income tax expense	$'000	11 821	12 341	8 963	10 789	12 327
CSO funding	$'000	0	0	0	0	0

a Includes an asset revaluation increase of $118 million. **b** In 2002-03 Transend changed its policy regarding dividend recognition in accordance with accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*. Under this standard, dividends are recognised at the time they are declared, determined or publicly recommended (see chapter 3 for details). Therefore, the $8 million dividend referring to Transend's 2002-03 financial results is recorded in 2003-04. **c** The Transend Board recommended a dividend of $9.9 million in respect of 2003-04, this dividend will be included in the financial statements for 2004-05.

POWER AND WATER CORPORATION — Northern Territory

Power and Water Corporation (PAWC) was established on 1 July 2002, following the corporatisation of the Power and Water Authority (PAWA).[1] PAWC operates under the *Government Owned Corporations Act 2001*. PAWC generates, transmits, distributes and retails electricity throughout the Northern Territory, as well as providing water and sewerage services.

PAWC's electricity operations are regulated by the *Electricity Reform Act 2001*. Three separate grid systems operate in the Northern Territory — Darwin–Katherine, Alice Springs and Tenant Creek.

Under the *Electricity Reform Act*, the NT Government regulates electricity retail charges to non-contestable customers via an Electricity Pricing Order.[2] Under the *Network Access Code* (a schedule to the *Electricity Networks (Third Party) Access Act*), the maximum prices that PAWC can charge for use of its transmission and distribution networks (through network access tariffs and charges) are set by the Utilities Commission.[3]

PAWC's pre-tax operating profit increased by 20 per cent ($10 million) in 2003-04, with a 7 per cent ($32 million) increase in sales and services revenue.

PAWC is required to make dividend and tax-equivalent payments to the NT Government. In 2003-04, PAWC provided for a $20 million dividend payment and recorded an income tax-equivalent expense of almost $15 million.

PAWC receives CSO payments from the NT Government. In 2003-04, PAWC received $44 million in CSO payments for pensioner concessions, geographic equalisation, Government price freeze policy and Tranche 4 electricity policy.

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1 PAWA was established under the *Power and Water Authority Act in 1987*.

2 The Northern Territory does not have full retail contestability, customers using less than 750 000 kWh per annum cannot choose their electricity supplier. Tranche 4 customers (those using between 750 000 kWh and 2 000 000 kWh) became contestable on 1 April 2002. A pricing order was issued in March 2004 that increased affected Tranche 4 customer prices by 5.1 per cent. Although larger customers are entitled to choose their electricity supplier, PAWC is currently the sole licensed retailer operating in the contestable segments of the Northern Territory electricity market, following the withdrawal of a competitor, NT Power, in September 2002. The NT Government is, therefore, planning to implement a Pricing Oversight regime to ensure that monopoly pricing does not occur. It is expected that the final arrangements for the regime will be agreed in 2005-06.

3 On 2 April 2004, the Utilities Commission approved PAWC's schedule of regulated network tariffs for 2004-05.

POWER AND WATER CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*
Size						
Total assets	$m			1013	1043	1 051
Total revenue	$m			390	448	480
Profitability						
Operating profit before tax	$'000			18 560	45 772	55 046
Operating sales margin	%			9.6	15.5	16.0
Cost recovery	%			110.6	118.4	119.1
Return on assets	%			4.0	7.1	7.7
Return on equity	%			2.8	5.1	6.5
Financial management						
Debt to equity	%			42.5	52.0	47.1
Debt to total assets	%			27.7	30.9	28.3
Total liabilities to equity	%			53.3	70.9	66.8
Interest cover	times			1.9	2.7	3.2
Current ratio	%			138.9	133.1	97.8
Leverage ratio	%			153.3	170.9	166.8
Payments to and from government						
Dividends	$'000			9 227	20 000	20 046
Dividend to equity ratio	%			1.4	3.1	3.2
Dividend payout ratio	%			49.7	62.3	49.8
Income tax expense	$'000			0	13 672	14 818
CSO funding	$'000			58 814	42 241	44 145

a The Power and Water Authority was included in this report for the first time in 2001-02. It was established in 1987 under the *Power and Water Authority Act*. **b** In 2002-03, the PAWC was involved in a $56 million debt for equity swap with the NT Government. The transaction increased interest-bearing liabilities and decreased equity by a commensurate amount.

SNOWY HYDRO — Australian Government

Snowy Hydro Limited (Snowy Hydro) commenced operations on 28 June 2002, when it assumed responsibility for the assets and liabilities of the Snowy Mountains Hydro-electric Authority, under the *Snowy Corporatisation Act 1997*.[1] Snowy Hydro operates under the *Corporations Act 2001* (Cwlth) and is jointly owned by the Australian Government, New South Wales and Victorian Governments.[2]

Snowy Hydro controls the Snowy Mountains Scheme — a dual-purpose hydro-electric and irrigation development — which consists of seven power stations and 16 dams in the Kosciusko National Park. The company generates electricity for sale into the National Electricity Market and includes the wholly-owned subsidiary, Snowy Hydro Trading Pty Ltd (SHTPL).[3] In 2003-04, the scheme generated 4320 GWh of power.

Snowy Hydro's pre-tax operating profit increased by almost 18 per cent ($32 million) in 2003-04 to $215 million, with an 11 per cent ($44 million) increase in revenue and a 6 per cent ($13 million) increase in expenses.

Snowy Hydro is required to make dividend and tax-equivalent payments. In 2003-04, Snowy Hydro recorded an income tax-equivalent expense of $56 million and provided for a $140 million dividend payment.[4]

1 The SMHEA was abolished on 27 June 2002. Prior to its abolition, the SMHEA sold its transmission assets to TransGrid and paid the balance owing for Australian Government advances it received to construct the Snowy Mountains Scheme. The Australian Government assumed any future liability in respect of Inscribed Stock, previously issued by the Authority.

2 Shareholdings in Snowy Hydro are New South Wales (58 per cent), Victoria (29 per cent) and Australian Government (13 per cent).

3 From 1 July 2002, Snowy Hydro and its wholly-owned subsidiary elected to be treated as a single entity for income purposes. On 10 March 2004, Snowy Hydro was granted a Financial Services Licence by Australian Securities and Investments Commission. This licence was previously held by SHTPL. At the reporting date it was Snowy Hydro's intention to deregister SHTPL as it had ceased operations.

4 The $140 million dividend for 2003-04 includes an unfranked cash dividend of $70 million paid on 12 September 2003 and another fully franked cash dividend of $70 million paid on 2 February 2004.

SNOWY HYDRO (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*[a]	*2003-04*[b]
Size						
Total assets	$m				1 680	1 691
Total revenue	$m				386	430
Profitability						
Operating profit before tax	$'000				182 546	214 544
Operating sales margin	%				57.0	58.1
Cost recovery	%				232.7	238.4
Return on assets	%				13.2	14.8
Return on equity	%				13.9	16.4
Financial management						
Debt to equity	%				58.5	52.6
Debt to total assets	%				33.0	30.1
Total liabilities to equity	%				77.2	74.9
Interest cover	times				5.7	6.9
Current ratio	%				66.0	69.5
Leverage ratio	%				177.2	174.9
Payments to and from government						
Dividends	$'000				0	140 000
Dividend to equity ratio	%				0.0	14.5
Dividend payout ratio	%				0.0	88.1
Income tax expense	$'000				50 875	55 681
CSO funding	$'000				0	0

a 2002-03 is the first year that Snowy Hydro was included in this report. It was established under the *Snowy Corporatisation Act* 1997. **b** The $140 million dividend for 2003-04 includes an unfranked cash dividend of $70 million paid on 12 September 2003 and another fully franked cash dividend of $70 million paid on 2 February 2004.

6 Water, sewerage, drainage and irrigation

The financial performances of 23 water, sewerage, drainage and irrigation (referred to hereafter as water) government trading enterprises (GTEs) is reported in this chapter. In 2003-04, these GTEs generated almost $6 billion in revenue and controlled assets valued at around $46 billion.

The monitored water GTEs vary in size and the range of services they provide. Several carry out all the activities involved in the supply of water and the disposal of stormwater and sewage. Others provide only a limited range of these services.

The GTEs monitored include those that provide services to major urban areas, as well as several that provide services in regional areas.

Financial performance summaries, including performance indicators for the water sector and each water GTE, are presented after this introduction. The performance indicators are consistent across individual GTEs. However, when making comparisons, care should be taken to consider differences in market environments and issues relating to the valuation of assets.

For a discussion of the data and the performance indicators used, and some of the factors that should be considered when assessing performance, see chapter 3.

6.1 Monitored GTEs

The activities of the monitored water GTEs are shown in table 6.1. Some also have interests in other areas. For example, ACTEW Corporation of the Australian Capital Territory has a joint venture interest with the private sector for the supply of gas and electricity.

Table 6.1 **Activities — water GTEs, 2003-04**

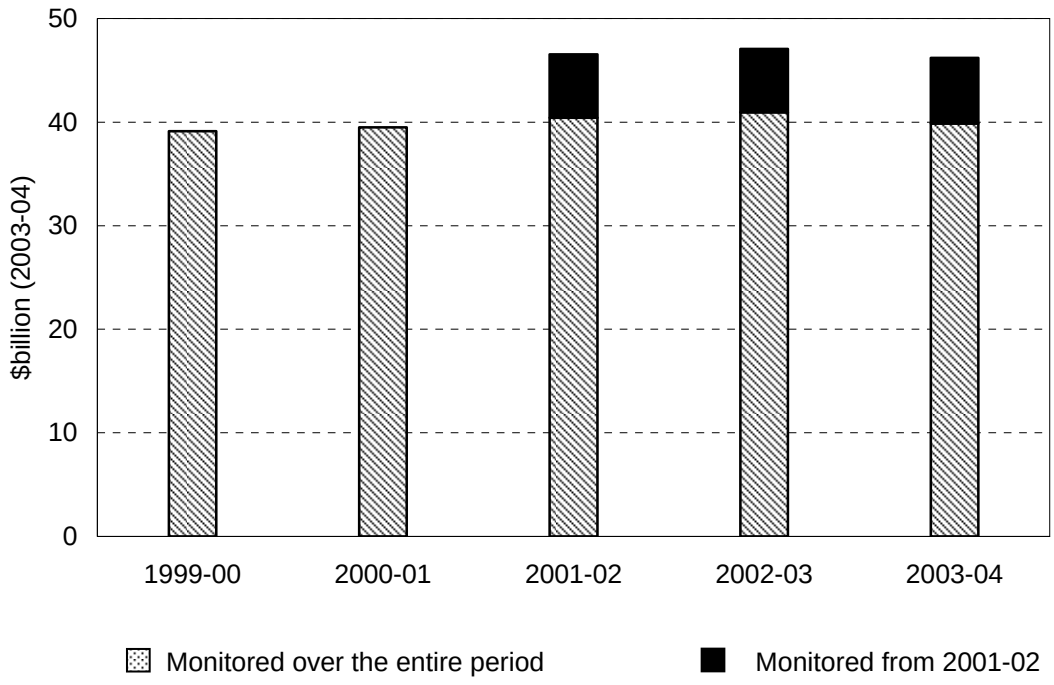
Water GTE	*Jurisdiction*	*Activity*				
		Catchment management	Bulk water	Reticulation	Wastewater treatment	Irrigation supply[a]
Sydney Catchment Authority	NSW	✓	✓	✗	✗	✗
Sydney Water	NSW	✗	✗	✓	✓	✗
Hunter Water	NSW	✓	✓	✓	✓	✗
Melbourne Water	Victoria	✓	✓	✓	✓	✓
City West Water	Victoria	✗	✗	✓	✗	✗
South East Water	Victoria	✗	✗	✓	✗	✗
Yarra Valley Water	Victoria	✗	✗	✓	✗	✗
Barwon Water	Victoria	✓	✓	✓	✓	✗
Coliban Water	Victoria	✗	✓	✓	✓	✗
Goulburn Valley Water	Victoria	✗	✓	✓	✓	✗
Gippsland Water	Victoria	✗	✓	✓	✓	✗
Central Highlands Water	Victoria	✗	✓	✓	✓	✗
Southern Rural Water	Victoria	✗	✓	✗	✗	✓
Sunraysia Rural Water	Victoria	✗	✓	✗	✗	✓
Wimmera Mallee Rural Water	Victoria	✗	✓	✗	✗	✓
Goulburn–Murray Rural Water	Victoria	✗	✓	✗	✗	✓
Sunwater	Queensland	✗	✓	✗	✗	✓
SA Water	SA	✗	✓	✓	✓	✓
Water Corporation	WA	✓	✓	✓	✓	✓
Hobart Water	Tasmania	✗	✓	✗	✗	✓
Cradle Coast Water	Tasmania	✗	✓	✗	✗	✓
Esk Water	Tasmania	✗	✓	✗	✗	✓
ACTEW Corporation	ACT	✓	✓	✓	✓	✗

a Not including wastewater sales for irrigation purposes.

The set of monitored water GTEs does not include local government service providers. In some cases, the value of assets of these providers are substantial. For example, the water operations of the Brisbane City Council and Gold Coast City Council generated revenue of over $500 million and $200 million respectively in 2003-04 (BCC 2004, GCCC 2004).

The Commission has expanded the number of monitored water GTEs over the reporting period (see figure 6.1). Nine GTEs — eight from regional Victoria — were included for the first time in 2001-02.

Figure 6.1 **Sector assets — water GTEs**



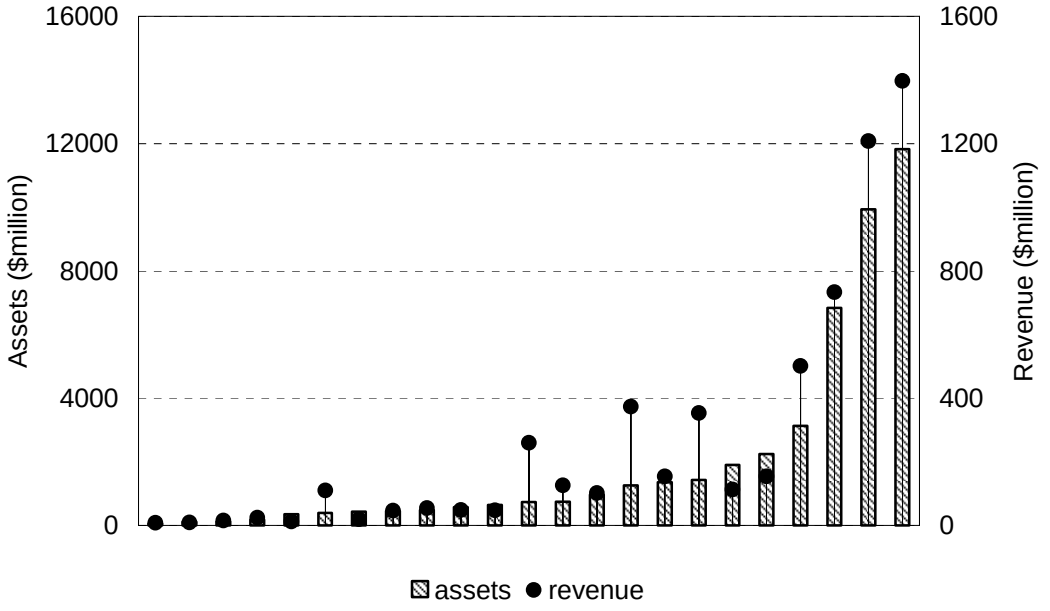
Note An additional nine water GTEs were included in 2001-02. The value of sector assets prior to 2003-04 was converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation for Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

Four of the newly included Victorian water GTEs provide water and sewerage services to households and businesses in regional Victoria.[1] Another four are mainly involved in the storage of bulk water and its sale to irrigators in regional Victoria. ACTEW Corporation, a vertically integrated water GTE operating predominantly in the Australian Capital Territory was the other water GTE included for the first time in 2001-02.

The size of the water GTEs — in terms of the value of the assets controlled and revenue earned — varies substantially (see figure 6.2). In 2003-04, the smallest water GTE monitored in terms of asset value was Cradle Coast Water ($65 million) and the largest was the Sydney Water Corporation (SWC) ($11.8 billion).[2]

Figure 6.2 **Assets and revenue — water GTEs, 2003-04**



Source: Productivity Commission estimates.

The regulatory framework for monitored water GTEs differs across jurisdictions. Most monitored water GTEs operate under licences that specify standards for water

1 There are 15 GTEs providing water and sewerage services to household and business customers in regional Victoria. For this report, the five largest by historical population served — Barwon Water (monitored for the entire reporting period), Coliban Water, Goulburn Valley Water, Central Gippsland Water and Central Highlands Water — were monitored. They accounted for almost 60 per cent of the 15 GTEs' overall revenue in 2003-04 (VWIA 2004).

2 The Sydney Water Corporation is the second largest GTE monitored in this report. The largest is Telstra.

quality and supply reliability and cover the extraction of water from rivers and underground systems.

There are also differences across jurisdictions in the operating principles established for water GTEs. These differences include the emphasis on commercial objectives by boards and governments compared to other objectives, such as compliance with the principles of ecologically sustainable development.

Most monitored water GTE prices are set by the board and approved by the minister. The prices charged by New South Wales, Victorian and the Australian Capital Territory GTEs are regulated by independent bodies.[3] Prices for a small number of the remaining monitored water GTEs were set directly by government.

6.2 Market environment

Changes in the operating environment — obligations and objectives, demand and supply conditions, and regulated charges — of water GTEs can affect their financial performance. Further, weather conditions and water restrictions impact on the availability of, and demand for, water.

Corporate reforms

Water industry reforms have been aimed at improving efficiency and financial performance by making the GTEs more commercially focused.

In February 1994, the Council of Australian Governments (CoAG) agreed to develop a 'strategic framework' for water reform. Governments decided in April 1995 to bring this framework within the ambit of the National Competition Policy (NCP) process. Under the framework, governments agreed to introduce:

- consumption-based two-part tariffs, full cost recovery, and to remove or make transparent subsidies and cross-subsidies;
- explicit identification and funding of community service obligations (CSOs);
- structural separation of water resource management, standard setting and regulatory enforcement from water provision;

[3] The Independent Pricing and Regulatory Tribunal regulates prices for New South Wales water GTEs, the Independent Competition and Regulatory Commission regulates ACTEW Corporation's prices and the Essential Services Commission regulates prices for all water GTEs in Victoria.

- trading in rural water entitlements; and
- the allocation of water for the environment.

Most jurisdictions have implemented two-part tariffs for water and sewerage services in urban areas and removed cross-subsidies between customers. However, South Australia and Western Australia retain property-based charges for sewerage services.

Almost half of the monitored GTEs received funding for CSOs over the reporting period. The CSOs were mainly for the provision of water to country areas and pensioner concessions.[4] Most of the GTEs receiving their CSOs did so over the reporting period. An exception was Cradle Coast Water, which received CSO payments for fluoridation up until 2000-01.

Regulatory, standard setting and resource management functions have been removed from service providers in most jurisdictions. The establishment of the Sydney Catchment Authority (SCA), which began operations in 1999, is one such consequence of this policy.

The SCA was established as a result of a 1998 review of the detection of the parasites *Cryptosporidium* and *Giardia* in Sydney's drinking water. The SCA was made responsible for the management and protection of Sydney's water supply catchments, dams, raw water transfer pipelines and canals, and associated infrastructure. These assets, valued at $647 million, were transferred from the SWC to the SCA. The SWC continued to supply water, drainage and sewerage services.

Some activities have been privatised or outsourced. For example, SA Water contracted out the management and operation of the water supply for the Adelaide metropolitan area to a private company for a period of 15 years in 1996. Coliban Water contracts out a range of activities to the private sector including operations and maintenance, revenue collection, technical and laboratory operations, and information technology management. Coliban Water also has several water treatment plants constructed under public–private sector partnerships.

Water demand and supply

Since all the monitored water GTEs charge volumetric rates for water use, their financial performance is directly related to the amount of water they distribute. This

4 Most Victorian water GTEs are reimbursed by the Government for the provision of concessions to pensioners and other eligible customers. However, in many cases these reimbursements have not been separately disclosed in financial statements.

depends on both the demand for water and the GTEs' ability to supply enough water to meet this demand.

The demand for water is determined primarily by factors such as population, industry composition and activity. However, demand is also affected by weather conditions. For example, the SWC supplied 2400 million litres of water per day in March 1998 (a dry summer) compared to 1700 million litres per day at the same time in 1997 (SWC 1999).

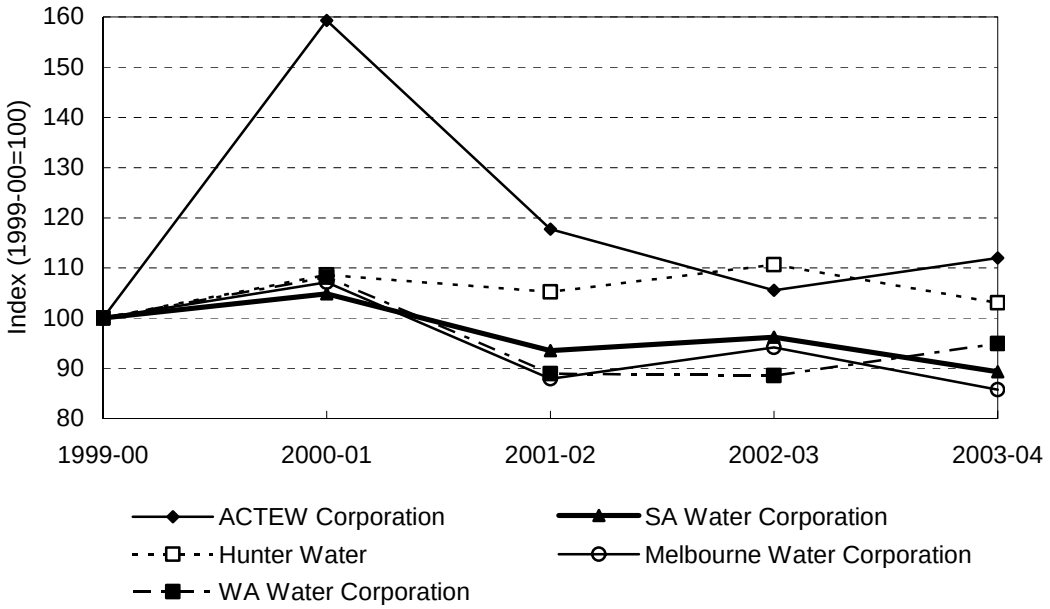
For many GTEs, the amount of water they are able to supply is strictly limited and may also be affected by weather conditions. As a consequence, the performance of several GTEs was adversely affected by the drought in 2003-04 because of limited water availability. In October 2003, SA Water became the first GTE to implement permanent water restrictions.

Responses by governments and GTEs to reduced water availability include restrictions on consumption by specific customers and general restrictions applying to specific activities. For example, in September 2001, the WA Government restricted the use of sprinklers by households and businesses to two days per week (Water Corporation 2002).

Many GTEs have environmental objectives included in their governing legislation. Demand management measures can be useful in meeting objectives such as improving environmental flows.

Over the reporting period the volume of water supplied by water GTEs varied year-to-year (see figure 6.3 for selected GTEs). Water restrictions and water conservation efforts appear to have had a significant impact on water sales. Aggregate urban water sales in Australia declined by around 8 per cent between 1999-00 and 2003-04.

Figure 6.3 **Water sales — selected urban water GTEs**



Data sources: WSAA (2004).

Customer charges

Historically, water and sewerage charges were based on property values, accompanied by a free allowance of water that could be consumed without any usage charge. Property-based charges rarely reflected the cost of providing water and sewerage services and sometimes resulted in cross-subsidisation between customers (PC 2002b).

All monitored water GTEs now have usage-based charges, typically comprising a fixed access charge and a volumetric charge based on water use.[5] The access charge is intended to reflect the fixed costs of supplying a customer including billing, system maintenance and environmental costs. The volumetric charge is intended to reflect the variable cost of supplying water. In some cases, usage-based charges were in the form of inclining block tariffs, implemented partly as a demand management initiative.

GTEs that earn a significant share of total revenue from the volumetric component of usage-based charges have a greater exposure to changes in the demand for water.

5 Usage-based charges were first introduced in 1982 by the Hunter District Water Board (now the Hunter Water Corporation) under the late Dr John Paterson, AO (1982-84).

Most water GTEs were required to comply with standards relating to the quality of treated water and sewage. Changes in the stringency of standards may affect financial performance, depending on whether additional treatment processes or facilities are required. For example, in May 2003, SA Water commenced a two-year implementation plan to comply with the Australian Drinking Water Guidelines Framework, launching initiatives such as training over 300 staff in water quality management practices.

Customer growth

Revenue volatility is also affected by the inclusion of developer and customer contributions as revenue. Developer and customer contributions entail payments to GTEs to finance new infrastructure. Alternatively, developers may be required to construct or install infrastructure assets themselves, which are then transferred to the responsible GTE at no cost.

During 1999-00, the building sector experienced considerable growth, with the value of work done on residential buildings increasing by 17 per cent. Further, contributions to monitored water GTEs grew by over 30 per cent in 1999-00. In subsequent years, the level of building activity changed markedly from year-to-year, declining by 27 per cent (2000-01), then increasing by 23 per cent (2001-02) and 17 per cent (2002-03), and becoming stable at around 5 per cent growth (2003-04) (ABS 2005).

Changes in the level of developer and customer contributions affect some water GTEs more than others. For example, Goulburn Valley Water's developer charges and contributions accounted for around 29 per cent of its total revenue in 2003-04. In contrast, developer charges and contributions accounted for less than 6 per cent of ACTEW Corporation's total revenue in that year and were not received at all by Tasmanian GTEs.

6.3 Profitability

Profitability indicators provide information on how well GTEs are using the assets vested in them by shareholder governments to generate earnings. However, in using these indicators to make comparisons across GTEs, the diverse range of activities of the entities has to be taken into account.

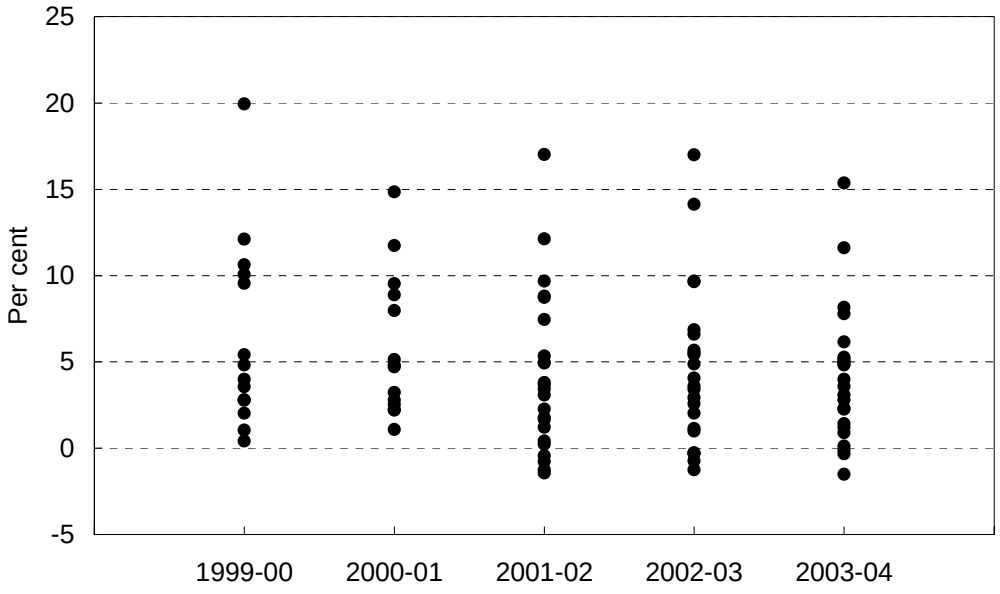
Under CoAG reforms (CoAG 1998), governments undertook a commitment to set prices to achieve cost recovery within a band. The lower bound of cost recovery includes operational, maintenance and administrative costs, externalities, taxes or

tax-equivalent payments, dividends, provisions for the cost of asset consumption and interest costs on debt. The upper bound of cost recovery encompasses the total opportunity cost of the GTE's investment in assets (calculated using a weighted average cost of capital). Water GTEs should at least achieve the lower bound cost recovery and move towards the upper bound where practicable.

Overall, the operating profit of water GTEs was relatively stable during the reporting period. Total sector operating profit before tax was $1.7 billion in 2003-04.

The return on assets for the sector overall also was stable during the reporting period. However, there was a wide range of variation across GTEs in each financial year over the reporting period (see figure 6.4). Indeed, only five monitored GTEs — Melbourne Water Corporation, City West Water, South East Water, Yarra Valley Water and Water Corporation — had a rate of return on assets greater than the risk free rate of 5.7 per cent for 10-year Australian Government bonds in 2003-04.

Figure 6.4 **Return on assets — water GTEs**



Note Nine GTEs were included for the first time in 2001-02. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue and adding back gross interest expense. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

The rural water GTEs, such as Southern Rural Water, Sunraysia Rural Water, Wimmera Mallee Water and Goulburn–Murray Water, do not set prices to be

profitable (see box 6.1). With governments only committed to set lower bound prices, the expectation is for these GTEs to earn sufficient revenue to ensure their ongoing viability, with no requirement to achieve a commercial rate of return.

In 2003-04, around 25 per cent of the monitored water GTEs were unable to recover their recurrent costs. While this is an improvement from 40 per cent in 2002-03, from 1999-00 to 2003-04 there has been a decline in the level of cost recovery.

A possible reason for the low level of cost recovery in 2002-03 was that prices charged by water GTEs were too low given the effect of the drought on supply and demand. If water charges remain the same when water restrictions are applied, revenue is likely to be reduced. In 2003-04, the easing of the drought coincided with the improved level of cost recovery.

Setting charges that are not sufficient to cover costs, including the cost of capital, has implications for the integrity of the corporatisation model, particularly when considering future investment decisions.

There are distinct differences in the profitability of water GTEs operating in metropolitan and non-metropolitan areas in Victoria.[6] The aggregated return on assets for metropolitan water GTEs in 2003-04 was around 9.5 per cent, compared to a return on assets of around 1.5 per cent for regional water GTEs. Victorian rural water GTEs used the renewals annuity approach (see box 6.1) to determine water charges, but use accounting depreciation in reporting operating results.

As noted in box 6.1, using the renewals annuity approach to set prices results in lower prices and decreased profitability, contributing to the Victorian rural GTEs reporting a negative return on assets in 2003-04.

6 The metropolitan water GTEs are City West Water, Yarra Valley Water, South East Water and the Melbourne Water Corporation. The regional water GTEs are Barwon Water, Coliban Water, Goulburn Valley Water, Gippsland Water and Central Highlands Water. The rural water GTEs are Southern Rural Water, Sunraysia Rural Water, Wimmera Mallee Water and Goulburn–Murray Water.

Box 6.1 **Renewals annuity pricing**

Charges for rural water GTEs in Victoria during 2003-04 were based on providing adequate funding to maintain the condition of existing channels, pipelines and structures using the renewals annuity concept. This involved setting aside funds for known future asset replacement and rehabilitation. It is an alternative to setting prices based on the consumption of existing fixed assets using an accounting measure of depreciation.

A renewals-based pricing approach is consistent with the minimum full cost recovery requirements of National Competition Policy agreements for the water sector — 'to recover the operational, maintenance and administrative costs, externalities, taxes or tax-equivalents (not including income tax), the interest cost on debt, dividends (if any) and provision for future asset refurbishment and replacement' (NCC 2003b).

To calculate a renewals annuity, a GTE identifies those assets that will reach the end of their life in the renewals period. It estimates the costs of replacing these assets and calculates the annual cash requirement to meet these costs.

The effect on the operating result using this approach can be derived by substituting accounting depreciation with a renewals charge (see table B.1).

Table B.1 Renewals reconciliation — Wimmera Mallee Water, 2003-04

	($'000)
Net operating result (accounting depreciation based)	- 5 577
Add back accounting depreciation	6 337
Less renewals annuity	3 544
Net operating result (renewals-based)	- 2 784

As in table B.1, the renewals annuity charge is typically less than the equivalent accounting depreciation expense. Therefore, other things being equal, a GTE's net operating result at prices set under the renewals–based approach, is generally worse than it would be if prices provided for accounting depreciation (see table B.2).

Table B.2 Renewals reconciliation — Southern Rural Water, 1999-00 to 2003-04

Year	Net operating result ($'000)	Net operating result (renewals-based) ($'000)
1999-00	90	1 434
2000-01	528	3 409
2001-02	- 5 536	167
2002-03	- 3 234	944
2003-04	- 1 404	2 001

Sources: WMW (2004); SRW (2004).

Another ratio used to measure profitability is return on equity — the rate of earnings on the capital provided by shareholder governments. The return on equity for most water GTEs improved over the reporting period.

Return on equity largely refects a GTE's operating profit, but can also be affected by tax-equivalent payments since it is calculated using after tax profit. For example, return on equity for City West Water decreased between 2000-01 and 2002-03, despite operating profits increasing by over 25 per cent. This was because there was a 120 per cent increase in tax-equivalent payments over this period, as a result of the implementation of the National Tax Equivalent Regime.

6.4 Financial management

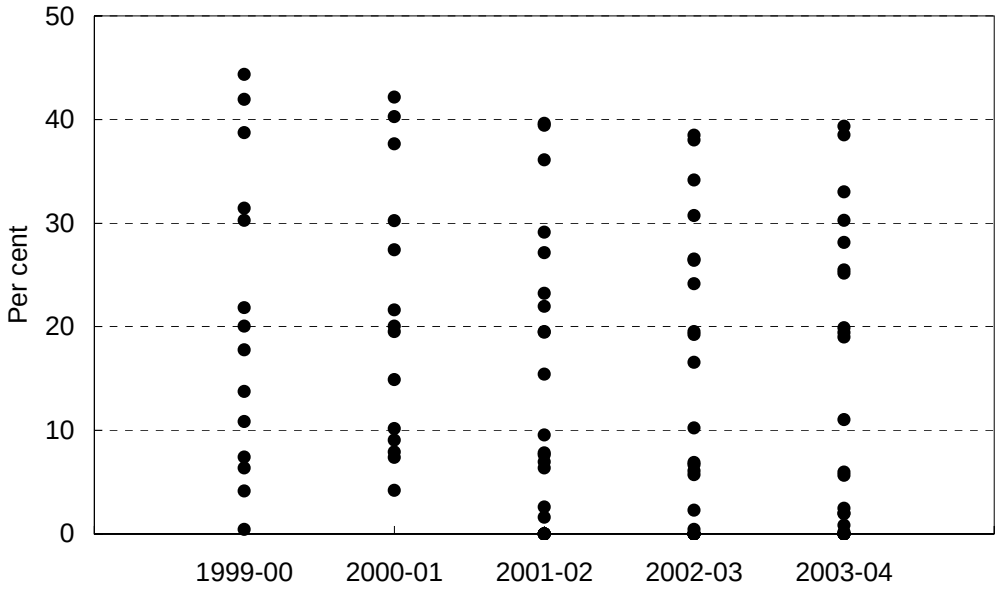
Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

Debt levels of monitored water GTEs increased in nominal terms from $6 billion in 1999-00 to around $8 billion in 2003-04, mainly because of increased borrowings by a small number of the large water GTEs. Debt levels for the majority of GTEs that carried debt declined over the reporting period, contributing to falls in their debt to total assets ratio (see figure 6.5). Five of the smaller monitored water GTEs operated debt free in 2003-04. These GTEs, along with Goulburn–Murray Water, which incurred debt for the first time in 2003-04, were debt free when monitoring commenced in 2001-02.

Asset revaluations affected the debt to total assets ratios of some water GTEs over the reporting period. For example, SWC's assets decreased by $2.6 billion in 2003-04, following a revaluation of systems assets and easements. The revaluation contributed to an increase in the debt to total assets ratio from 16.6 per cent in 2002-03 to 19.9 per cent in 2003-04.

Interest cover — which measures the capacity of a GTE to meet periodic interest payments out of current earnings — for the sector in 2003-04 was 4.7 times. Interest cover remained largely unchanged over the reporting period.

Figure 6.5 **Debt to total assets — water GTEs**



Note Nine GTEs were included for the first time in 2001-02. Six of these GTEs operated debt free from 2001-02 to 2003-04. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

The ability of water GTEs to meet short-term liabilities, as indicated by the current ratio, has remained largely unchanged since 1999-00. Although most water GTEs had current ratios below 100 per cent during the reporting period, the reasonably stable cash flows that are generally a feature of the water sector suggest that low current ratios can be sustained.

6.5 Transactions with government

As a part of the reform process, governments have sought to give GTEs a greater commercial focus and facilitate competitive neutrality by exposing them to capital market disciplines and regulations similar to those faced by private sector businesses.

Dividends

The dividend payable by each GTE depends on the dividend policy of its owner government (see chapter 2). In 2003-04, about 50 per cent of monitored water GTEs

had dividend payout ratios above 50 per cent. Two GTEs made a dividend payment despite recording operating losses.

Seven GTEs did not record a dividend in 2003-04. ACTEW Corporation has recorded dividends in each year of the reporting period except for 2003-04, when the dividend payment was postponed to 2004-05 to assist the financing of capital expenditure.

Tax-equivalent payments

The introduction of tax-equivalent regimes varied across GTEs. However, by the end of the five-year reporting period, all water GTEs were subject to tax-equivalent payments under the National Tax Equivalent Regime.

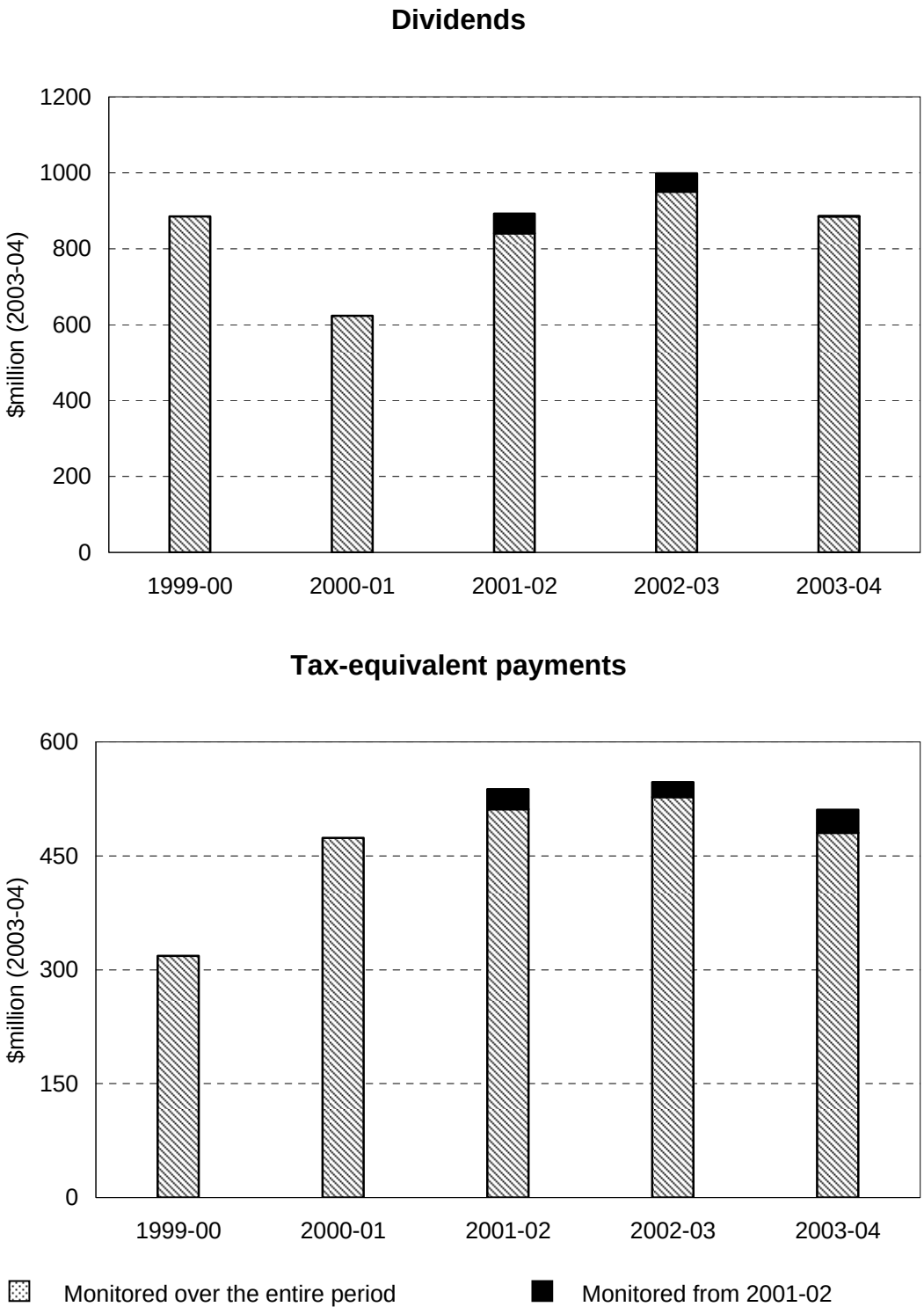
The level of dividend and tax-equivalent payments varied from year-to-year (see figure 6.6). Income tax expenses decreased in 1999-00 as a result of a reduction in the future company tax rate.[7] Across the sector, this led to a downward adjustment in tax-equivalent payments by around $150 million. In 2003-04, water GTEs made around $510 million in income tax-equivalent payments to owner governments. The Victorian and WA Governments were the major recipients, receiving 30 per cent and 33 per cent of all income tax-equivalent payments made by water GTEs respectively.

CSOs

CSOs provided by some water GTEs include concessions, the supply of services below the cost of provision and upgrading sewerage infrastructure. In 2003-04, eleven water GTEs received funding for CSOs totalling around $500 million. Several other water GTEs were reimbursed by governments for pensioner and other concessions but the amounts were not disclosed in financial statements.

7 The company tax rate was reduced from 36 per cent in 1999-00 to 34 per cent for 2000-01. It was further reduced to 30 per cent from 2001-02.

Figure 6.6 **Dividend and income tax-equivalent payments — water GTEs**



Note Nine GTEs were included for the first time in 2001-02. The value of dividend and tax-equivalent payments prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

WATER

Whole of sector performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	38 122	39 169	46 573	47 110	46 196
Total revenue	$m	4 933	4 861	5 529	5 822	5 865
Profitability						
Operating profit before tax	$'000	1 673 307	1 478 064	1 612 691	1 682 172	1 774 773
Operating sales margin	%	42.5	39.2	37.5	36.9	38.1
Cost recovery	%	174.0	165.3	159.3	158.0	160.4
Return on assets	%	5.4	5.0	4.6	4.6	4.8
Return on equity	%	4.5	3.4	3.0	3.1	3.5
Financial management						
Debt to equity	%	20.6	21.9	19.8	20.7	23.0
Debt to total assets	%	15.6	17.2	15.7	16.1	17.2
Total liabilities to equity	%	28.9	29.3	27.7	29.3	32.3
Interest cover	times	4.8	4.4	4.4	4.5	4.7
Current ratio	%	43.8	59.2	71.2	62.5	55.4
Leverage ratio	%	128.9	129.3	127.7	129.3	132.3
Payments to and from government						
Dividends	$'000	862 253	618 691	893 370	999 368	885 467
Dividend to equity ratio	%	2.8	2.1	2.5	2.7	2.5
Dividend payout ratio	%	63.2	61.4	83.2	88.1	70.0
Income tax expense	$'000	309 958	470 004	538 387	547 702	510 580
CSO funding	$'000	412 547	409 156	463 558	481 719	501 398

6.6 GTE performance reports

Sydney Catchment Authority (NSW)
Sydney Water Corporation (NSW)
Hunter Water Corporation (NSW)
Melbourne Water Corporation (Victoria)
City West Water (Victoria)
South East Water (Victoria)
Yarra Valley Water (Victoria)
Barwon Regional Water Authority (Victoria)
Coliban Regional Water Authority (Victoria)
Goulburn Valley Regional Water Authority (Victoria)
Central Gippsland Water Authority (Victoria)
Central Highlands Water Authority (Victoria)
Gippsland and Southern Rural Water Authority (Victoria)
Sunraysia Rural Water Authority (Victoria)
Wimmera Mallee Rural Water Authority (Victoria)
Goulburn–Murray Water Authority (Victoria)
Sunwater (Queensland)
South Australia Water Corporation (SA)
Water Corporation (WA)
Hobart Regional Water Authority (Tasmania)
Cradle Coast Water (Tasmania)
Esk Water Authority (Tasmania)
ACTEW Corporation (ACT)

SYDNEY CATCHMENT AUTHORITY — New South Wales

The Sydney Catchment Authority (SCA) was established by the *Sydney Water Catchment Management Act 1998* to provide, construct, operate, manage and maintain efficient systems for the supply of bulk water. The SCA's activities are carried out under an operating licence granted by the Governor and a Water Management Licence with the Department of Land and Water Conservation.[1]

Catchment management and protection is a key function of the SCA and it has regulatory enforcement powers aimed at reducing threats to water quality. Initiatives in 2003-04 included the implementation of the Healthy Catchment Program, and development of a regional plan for the drinking water catchments of Sydney and adjacent regional centres.

Charges for bulk water and other services are determined by the Independent Pricing and Regulatory Tribunal of New South Wales (IPART). Under a determination made in September 2000, real charges did not change in 2003-04.[2] Bulk water sales to Sydney Water Corporation (SWC) accounted for around 97 per cent of total revenue.[3]

A refurbishment of Warragamba Dam was commenced in June 2004, with capital improvements of $24 million. The upgrade was necessary because of the age of the asset and changes in safety requirements.

In 2003-04, operating profit before tax decreased slightly to $26 million. This change can be attributed to the ongoing drought and water restrictions, which reduced water sales. Total water storage levels in SCA dams have reportedly fallen from around 62 per cent to 47.5 per cent in the financial year.

The funding of some non-commercial activities is not explicitly reported in the financial statements.[4]

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1 The operating licence places obligations on SCA with respect to customer service, system performance and environmental performance.

2 Under the determination, charges were to remain fixed in real terms over the period 2000-01 to 2004-05.

3 Responsibility for managing catchments, dams and their associated infrastructure was transferred from SWC to the SCA in July 1999. There was a transfer of $492 million in net assets, largely comprising $619 million in system assets, property and equipment, and $162 million of debt.

4 Under its operating licence, the SCA is also required to manage a range of heritage items, including old dams and weirs, walking tracks and bridges.

SYDNEY CATCHMENT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*[b]	*2002-03*	*2003-04*
Size						
Total assets	$m	736	746	711	736	745
Total revenue	$m	123	124	120	131	125
Profitability						
Operating profit before tax	$'000	59 880	47 436	26 650	28 266	26 022
Operating sales margin	%	56.5	46.6	31.8	30.9	30.5
Cost recovery	%	230.0	187.3	146.7	144.7	143.9
Return on assets	%	9.5	8.0	5.3	5.7	5.3
Return on equity	%	7.5	5.9	3.1	3.9	3.8
Financial management						
Debt to equity	%	30.9	30.1	32.0	34.9	37.3
Debt to total assets	%	21.8	21.6	21.9	24.1	25.2
Total liabilities to equity	%	41.5	40.0	42.2	47.2	49.0
Interest cover	times	6.8	5.1	3.2	3.2	3.0
Current ratio	%	92.7	70.4	40.0	55.8	78.3
Leverage ratio	%	141.5	140.0	142.2	147.2	149.0
Payments to and from government						
Dividends	$'000	10 600	17 600	30 500	18 877	18 354
Dividend to equity ratio	%	2.0	3.3	5.9	3.8	3.7
Dividend payout ratio	%	27.3	56.5	189.5	97.0	97.0
Income tax expense	$'000	21 100	16 278	10 555	8 805	7 101
CSO funding	$'000	n.p.	n.p.	n.p.	n.p.	n.p.

a On 2 July 1999 the Sydney Catchment Authority (SCA) commenced operations. On this date, $492 million in net assets were transferred from Sydney Water Corporation (SWC) to the SCA. **b** Includes a downward revaluation of some land ($6.9 million), land transfers to the SWC ($11.7 million) and the National Parks and Wildlife Service ($5.6 million). **n.p.** Not published.

SYDNEY WATER CORPORATION — New South Wales

Sydney Water Corporation (SWC) operates under the *State Owned Corporations Act 1991* and the *Sydney Water Act 1994*.[1] SWC supplies drinking water and provides wastewater services and some stormwater services to a population of around 4.2 million in Sydney, the Blue Mountains and Illawarra under an operating licence granted by the Governor.[2]

SWC's charges are regulated by the Independent Pricing and Regulatory Tribunal of New South Wales (IPART) using a CPI-X pricing regime.[3] There was reportedly a small increase in the water usage charge in the 2004 financial year.

Total assets decreased by around $2030 million, largely due to a revaluation decrement of $2580 million to system assets and easements during 2003-04. Increased debt ($224 million) combined with a decreased asset base led to increases in both debt to equity and debt to total assets ratios, a continuation of the trend over the reporting period.

In 2003-04, operating profit before tax increased by $87 million to $306 million, despite the ongoing drought and water restrictions. While revenue decreased by $54 million, expenses also decreased by $141 million, with a reduction to non-recurrent items such as a $106 million change in superannuation expense.

SWC receives funding for the provision of CSOs, including rebates for pensioners and low income households. The payment was $79 million in 2003-04.

1 The enactment of the *Water Legislation Amendment (Drinking Water and Corporate Structure) Act 1998* changed the status of SWC from a 'company' State Owned Corporation (SOC) to a 'statutory' SOC. The change gave the responsible Minister greater power to make directions and access information, among other things.

2 The operating licence places obligations on SWC with respect to customer service, system performance and environmental performance.

3 IPART issued a new price determination in May 2003, which set charges for the following two years and provided an overall price adjustment marginally above the CPI for each of those years. IPART is also responsible for conducting annual audits of SWC's compliance with its licence.

SYDNEY WATER CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	13 053	13 471	14 253	13 856	11 827
Total revenue	$m	1 467	1 431	1 492	1 450	1 397
Profitability						
Operating profit before tax	$'000	385 296	283 510	334 548	218 761	305 921
Operating sales margin	%	35.3	29.4	31.6	24.8	32.7
Cost recovery	%	153.4	145.3	146.2	132.9	148.6
Return on assets	%	4.0	3.2	3.4	2.6	3.6
Return on equity	%	3.0	1.5	1.6	1.1	2.8
Financial management						
Debt to equity	%	17.0	18.1	18.8	21.8	30.1
Debt to total assets	%	13.8	14.9	15.4	16.6	19.9
Total liabilities to equity	%	22.6	23.2	25.7	29.6	39.6
Interest cover	times	3.8	3.0	3.4	2.5	3.0
Current ratio	%	41.0	59.5	51.2	43.7	42.5
Leverage ratio	%	122.6	123.2	125.7	129.6	139.6
Payments to and from government						
Dividends	$'000	129 271	53 353	110 000	115 000	115 000
Dividend to equity ratio	%	1.2	0.5	1.0	1.0	1.2
Dividend payout ratio	%	40.3	32.7	60.1	91.5	42.7
Income tax expense	$'000	64 253	120 292	151 460	93 110	36 404
CSO funding	$'000	87 686	73 300	78 343	79 661	79 095

a Sydney Water Corporation (SWC) was required over a three year period commencing 1997-98, to pay 100 per cent of its profit after tax and developer contributions as a dividend to the NSW Government. Responsibility for managing catchments, dams and their associated infrastructure were transferred to the Sydney Catchment Authority. The transfer included $492 million in net assets, comprised mainly of $619 million in system assets, property and equipment and $162 million of debt. **b** Includes expenses relating to superannuation adjustments ($56 million), redundancy ($8.1 million) and the repayment of excess government contributions for sewerage backlog projects ($36 million). Includes a revaluation increment of $168 million relating to system and property assets. **c** Includes a $101 million expense relating to superannuation adjustments and a revaluation increment of $334 million to system assets. **d** Includes expenses relating to superannuation adjustments ($82 million), the write-off of the Customer Information Billing System project costs ($51 million), the South Western Suburbs Ocean Outfall Scheme ($30 million) and a revaluation decrement of $698 million to system assets and easements. **e** Includes a $106 million expense relating to superannuation adjustments and a revaluation decrement of around $2580 million to system assets and easements.

HUNTER WATER CORPORATION — New South Wales

Hunter Water Corporation (HWC) operates under the *State Owned Corporations Act 1989* and the *Hunter Water Act 1991*.[1] HWC provides water, wastewater and drainage services to almost half a million people living in the Newcastle, Lake Macquarie, Maitland, Cessnock and Port Stephens areas, under an operating licence granted by the Governor.[2] Hunter Water Australia Pty Ltd, a wholly-owned subsidiary of HWC, provides water treatment, engineering, surveying and laboratory services to HWC and external clients.

HWC's charges are regulated by the Independent Pricing and Regulatory Tribunal of New South Wales (IPART) using a CPI-X pricing regime.[3] In 2003-04, there was reportedly an overall price increase in real terms of under $7 on the average bill.

HWC increased its revenue and decreased its expenses in 2003-04, which resulted in a $7 million increase in pre-tax operating profit to $41 million. The increase in revenue was mainly attributed to customer growth and higher water sales, while future superannuation liabilities fell after adjustment.

In 2003-04, HWC paid a $36 million dividend, down from $38 million in 2002-03. The dividend payout ratio also decreased from 386 per cent to 178 per cent over the same period. Since 2000-01, HWC has been required to pay dividends that exceed its operating profit before tax.

CSOs provided by HWC are funded by the NSW Government to cover tariff rebates to pensioners and for exempt properties such as churches. HWC received $9 million to fund these CSOs in 2003-04.

1 The enactment of the *Water Legislation Amendment (Drinking Water and Corporate Structure) Act 1998* changed the status of HWC from a 'company' State Owned Corporation (SOC) to a 'statutory' SOC. The change gave the responsible Minister greater power to make directions and access information, among other things.

2 The operating licence places obligations on HWC with respect to customer service, system performance and environmental performance.

3 IPART issued a new price determination in May 2003, which set charges for the following two years and provided an overall price adjustment marginally above the CPI for each of those years. IPART is also responsible for conducting annual audits of HWC's compliance with its licence.

HUNTER WATER CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*	*2003-04*[d]
Size						
Total assets	$m	1 970	2 017	2 095	2 179	2 246
Total revenue	$m	136	131	133	147	154
Profitability						
Operating profit before tax	$'000	50 123	36 420	26 254	34 026	41 479
Operating sales margin	%	39.5	32.4	24.4	27.9	32.1
Cost recovery	%	142.9	140.9	125.8	132.1	139.8
Return on assets	%	2.8	2.2	1.7	2.0	2.3
Return on equity	%	1.9	1.3	0.4	0.5	1.0
Financial management						
Debt to equity	%	4.6	4.5	7.1	6.8	6.3
Debt to total assets	%	4.1	4.2	6.4	6.1	5.6
Total liabilities to equity	%	8.9	9.0	12.8	13.6	13.5
Interest cover	times	9.0	5.8	4.2	4.8	5.5
Current ratio	%	107.7	116.5	151.6	75.0	76.2
Leverage ratio	%	108.9	109.0	112.8	113.6	113.5
Payments to and from government						
Dividends	$'000	28 000	30 000	31 110	38 000	36 000
Dividend to equity ratio	%	1.5	1.6	1.7	2.0	1.8
Dividend payout ratio	%	80.1	126.4	452.7	386.4	178.4
Income tax expense	$'000	15 185	12 677	19 382	24 191	21 301
CSO funding	$'000	8 277	8 463	8 550	9 261	9 043

a Includes contributions for capital works and abnormal revenue of $11.6 million for a reduction in superannuation liability. The value of assets was written down over a range of asset classes by $105 million following a recoverable amounts test. **b** Includes an asset revaluation increment of $54.3 million relating to water and sewerage assets, and an expense of $1.6 million for an increase in superannuation liability. **c** Includes an expense of $13.4 million as a result of an adjustment to superannuation liabilities and a revaluation increment of $26.8 million relating to sewers. **d** Includes an asset revaluation increment of $67.9 million relating to water and sewerage assets and an expense of $1.6 million for an increase in superannuation liability.

MELBOURNE WATER CORPORATION Victoria

Melbourne Water Corporation (MWC) operates under the *Melbourne Water Corporation Act 1992* and the *State Owned Enterprises Act 1992*. MWC's activities include water catchment management, wholesale water supply, sewerage services such as major sewers and sewage pump stations, sewage treatment and stormwater management. Its main customers are the three retail water GTEs in Melbourne, however services are also provided to other water authorities, local councils and land developers.

Prior to 2004, charges were set by the Victorian Government under the *Melbourne Metropolitan Water, Wastewater and Drainage Services Pricing Order 2001*.[1] Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

MWC's trading activities are dependent to a significant extent on the sale of bulk water and sewage services to the metropolitan retail water GTEs. It also relies on these GTEs for billing and payment collection for its drainage services.

Assets increased by $80 million over 2003-04, driven by $151 million of capital expenditure, which increased by $33 million from the previous year. Debt increased $41 million to help finance investment.

In 2003-04, MWC experienced a decrease in revenue by $5 million and an increase in expenses by $34 million, resulting in a $39 million (18 per cent) reduction in operating profit before tax. Factors reportedly influencing this included lower water demand, delayed asset sales, and higher than expected legal and insurance costs.

MWC was not subject to CSOs over the reporting period.

1 Under the Order, charges for water, wastewater and drainage increased by around the rate of inflation plus 2 per cent in 2001-02, inflation plus 1 per cent in 2002-03 and the rate of inflation in 2003-04.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in MWC's retail licence, and addressing other non-pricing issues.

MELBOURNE WATER CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*[a]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	2 852	2 954	2 995	3 051	3 132
Total revenue	$m	477	461	477	506	501
Profitability						
Operating profit before tax	$'000	204 234	178 094	185 811	218 425	179 462
Operating sales margin	%	59.1	56.0	54.9	57.8	50.3
Cost recovery	%	243.4	226.5	221.8	236.8	201.4
Return on assets	%	10.1	8.9	8.8	9.7	8.2
Return on equity	%	17.7	10.4	9.9	11.1	8.8
Financial management						
Debt to equity	%	106.5	93.0	88.3	83.2	84.5
Debt to total assets	%	44.4	42.1	39.4	38.0	38.5
Total liabilities to equity	%	144.4	124.4	125.5	120.9	122.2
Interest cover	times	3.6	3.2	3.4	3.9	3.5
Current ratio[b]	%	10.3	16.9	19.0	16.6	12.0
Leverage ratio	%	244.4	224.4	225.5	220.9	222.2
Payments to and from government						
Dividends[b]	$'000	126 246	58 300	98 942	99 400	95 700
Dividend to equity ratio[b]	%	11.3	4.7	7.5	7.3	6.9
Dividend payout ratio[b]	%	64.1	45.2	76.0	66.3	77.6
Income tax expense	$'000	7 348	49 066	55 555	68 472	56 089
CSO funding	$'000	0	0	0	0	0

a Includes a $59.1 million increase in the value of Crown Land assets that was previously unrecognised. **b** A change in accounting policy in 2000-01 resulted in a final dividend not being provided for because it was not yet announced by the shareholding ministers. From 2001-02 to 2003-04, the dividend included the final dividend from the previous year's operating results and the current year's interim dividend. This change in accounting standard affected the current ratio, and the comparability of the dividend to equity ratio and dividend payout ratio with those from before 2000-01. Under AASB 1044, dividends are now recognised in the financial year in which they are announced (see chapter 3). The proposed final dividend payable in relation to the 2003-04 financial year is $41.3 million. This amount is subject to final determination by the Treasurer after consultation with the Melbourne Water Board of Directors and the Minister for Water and consequently was not provided for as at 30 June 2004.

CITY WEST WATER Victoria

City West Water (CWW) commenced operations on 1 January 1995. CWW is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to a licence issued under the *Water Industry Act 1994*. It provides water, sewerage and trade waste services to approximately 280 000 residential, commercial and industrial customers in Melbourne's central business district, and its inner and western suburbs.

Prior to 2004, charges were set by the Victorian Government under the *Melbourne Metropolitan Water, Wastewater and Drainage Services Pricing Order 2001*.[1] Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

In 2003-04, assets grew by $49 million mainly because of increased capital expenditure, which also increased debt levels by $21 million.

CWW is required to make dividend payments to the Victorian Government. In 2002-03, the dividend payout increased by $36 million, however, the payment fell in 2003-04 by $49 million to $42 million. This has led to a significant decline in the dividend payout ratio.

CWW is reimbursed for the value of concessions provided to pensioners and others, and for the administration of the concession schemes. This amount has gradually increased since 2001-02 to $9 million in 2003-04.

1 Under the Order, charges for water, wastewater and drainage increased by around the rate of inflation plus 2 per cent in 2001-02, inflation plus 1 per cent in 2002-03 and the rate of inflation in 2003-04.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in CWW's retail licence, and addressing other non-pricing issues.

CITY WEST WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	625	641	660	686	735
Total revenue	$m	255	228	243	261	260
Profitability						
Operating profit before tax	$'000	110 147	82 340	100 070	104 800	97 697
Operating sales margin	%	48.0	41.2	45.4	43.7	42.1
Cost recovery	%	192.2	170.2	183.1	177.7	172.6
Return on assets	%	19.9	14.8	17.0	17.0	15.4
Return on equity	%	34.0	19.4	19.4	19.0	17.6
Financial management						
Debt to equity	%	57.1	46.7	38.6	47.9	50.1
Debt to total assets	%	30.3	27.4	23.2	26.5	28.1
Total liabilities to equity	%	91.6	72.3	68.8	84.0	84.3
Interest cover	times	9.7	8.1	10.5	12.0	9.5
Current ratio[a]	%	32.7	56.1	69.7	55.7	44.0
Leverage ratio	%	191.6	172.3	168.8	184.0	184.3
Payments to and from government						
Dividends[a]	$'000	57 400	22 350	54 750	90 800	41 600
Dividend to equity ratio[a]	%	18.9	6.4	14.4	23.8	10.8
Dividend payout ratio[a]	%	55.6	33.0	74.0	124.8	61.4
Income tax expense	$'000	6 915	14 574	26 036	32 072	29 926
CSO funding[b]	$'000	n.p.	n.p.	8 837	8 977	9 030

a A change in accounting policy in 2000-01 resulted in a final dividend not being provided for because it was not yet announced by the shareholding ministers. From 2001-02 to 2003-04, the dividend included the final dividend from the previous year's operating results and th e current year's interim dividend. This change in accounting standard affected the current ratio, and the comparability of the dividend to equity ratio and dividend payout ratio with those from before 2000-01. Under AASB 1044, dividends are now recognised in the financial year in which they are announced (see chapter 3). City West Water has not made a provision for an estimated $21.8 million final dividend for 2003-04, to be payable in 2004-05. **b** CSO payments were first recorded in the 2002-03 financial report. **n.p.** Not published.

SOUTH EAST WATER — Victoria

South East Water (SEW) is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to a licence issued under the *Water Industry Act 1994*. SEW provides water supply and sewerage services to 1.3 million customers in the southern and eastern suburbs of Melbourne.

Prior to 2004, charges were set by the Victorian Government under the *Melbourne Metropolitan Water, Wastewater and Drainage Services Pricing Order 2001*.[1] Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

In 2003-04, assets continued to grow by $95 million to $1250 million, primarily because of $65 million invested in capital works, which also led to an increase in debt by $18 million.

Operating profit (pre-tax) decreased by $21 million (15 per cent) in 2003-04, reportedly because of lower water sales, as well as reduced developer income — particularly developer contributed assets (falling $10 million).

SEW is required to make dividend payments to the Victorian Government. In 2003-04, dividends decreased by $48 million to $54 million, impacting the dividend payout ratio significantly. Previously, SEW had recorded increases in dividends since 2000-01.

SEW is reimbursed for the value of concessions provided to pensioners and others, as well as for the administration of the concession schemes. However, these amounts are not disclosed in SEW's financial statements.

1 Under the Order, charges for water, wastewater and drainage increased by around the rate of inflation plus 2 per cent in 2001-02, inflation plus 1 per cent in 2002-03 and the rate of inflation in 2003-04.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in SEW's retail licence, and addressing other non-pricing issues.

SOUTH EAST WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	1 048	1 070	1 105	1 160	1 255
Total revenue	$m	331	329	343	387	373
Profitability						
Operating profit before tax	$'000	104 883	103 587	111 989	139 545	118 877
Operating sales margin	%	37.9	37.7	38.4	41.2	37.5
Cost recovery	%	161.6	160.6	162.4	170.2	160.0
Return on assets	%	12.1	11.7	12.1	14.1	11.6
Return on equity	%	19.3	14.7	12.7	15.7	12.8
Financial management						
Debt to equity	%	59.5	53.2	51.2	56.7	53.7
Debt to total assets	%	31.4	30.2	29.1	30.7	30.3
Total liabilities to equity	%	90.9	77.6	78.6	88.9	84.4
Interest cover	times	6.0	6.0	6.7	8.1	6.6
Current ratio[a]	%	36.2	64.4	77.7	42.8	37.8
Leverage ratio	%	190.9	177.6	178.6	188.9	184.4
Payments to and from government						
Dividends[a]	$'000	68 175	33 000	62 300	102 200	54 400
Dividend to equity ratio[a]	%	12.8	5.7	10.2	16.6	8.4
Dividend payout ratio[a]	%	66.6	39.1	80.3	105.5	65.9
Income tax expense	$'000	2 488	19 169	34 434	42 636	36 326
CSO funding	$'000	n.p.	n.p.	n.p.	n.p.	n.p.

a A change in accounting policy in 2000-01 resulted in a final dividend not being provided for because it was not yet announced by the shareholding ministers. From 2001-02 to 2003-04, the dividend included the final dividend from the previous year's operating results and the current year's interim dividend. This change in accounting standard affected the current ratio, and the comparability of the dividend to equity ratio and dividend payout ratio with those from before 2000-01. Under AASB 1044, dividends are now recognised in the financial year in which they are announced (see chapter 3). The estimated final dividend in respect of 2003-04 is $20.1 million, though no final dividend had been provided for as at 30 June 2004. **n.p.** Not published.

YARRA VALLEY WATER Victoria

Yarra Valley Water (YVW) is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to a licence issued under the *Water Industry Act 1994.* It provides retail water supply and sewerage services, as well as the collection of tradewaste to more than 1.5 million people in the eastern and northern suburbs of Melbourne.

Prior to 2004, charges were set by the Victorian Government under the *Melbourne Metropolitan Water, Wastewater and Drainage Services Pricing Order 2001*.[1] Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

In 2003-04, assets grew by $74 million to $1430 million, with a record level of capital expenditure of $91 million. This also contributed to a sharp rise in current liabilities by $71 million (68 per cent).

Operating profit before tax fell $19 million (20 per cent) in 2003-04, with revenue decreasing $17 million. Water restrictions, which led to a reduction in water usage, was the main reason for the decline in profitability.

YVW is required to make dividend payments to the Victorian Government. In 2003-04, the dividend payout decreased $12 million to $48 million, coinciding with a decrease in operating profit.

YVW is reimbursed for the value of concessions provided to pensioners and others, and for the administration of the concession schemes. These figures were not reported separately prior to 2001-02.

1 Under the Order, charges for water, wastewater and drainage increased by around the rate of inflation plus 2 per cent in 2001-02, inflation plus 1 per cent in 2002-03 and the rate of inflation in 2003-04.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in YVW's retail licence, and addressing other non-pricing issues.

YARRA VALLEY WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	1 230	1 263	1 296	1 356	1 430
Total revenue	$m	353	342	336	370	353
Profitability						
Operating profit before tax	$'000	96 471	86 165	78 988	94 724	75 595
Operating sales margin	%	36.3	34.7	33.2	34.4	30.7
Cost recovery	%	157.2	153.0	149.7	152.5	144.4
Return on assets	%	10.6	9.5	8.7	9.6	7.8
Return on equity	%	18.7	11.9	9.6	10.3	8.2
Financial management						
Debt to equity	%	91.5	82.6	82.6	80.3	85.7
Debt to total assets	%	42.0	40.3	39.6	38.5	39.3
Total liabilities to equity	%	122.2	107.7	111.1	113.3	123.5
Interest cover	times	4.0	3.6	3.4	4.0	3.3
Current ratio[a]	%	41.1	37.0	46.6	45.3	25.5
Leverage ratio	%	222.2	207.7	211.1	213.3	223.5
Payments to and from government						
Dividends[a]	$'000	62 707	23 614	52 693	60 400	48 400
Dividend to equity ratio[a]	%	11.7	4.1	8.6	9.7	7.6
Dividend payout ratio[a]	%	62.8	34.3	89.5	93.7	92.2
Income tax expense	$'000	- 3 417	17 285	20 136	30 290	23 121
CSO funding	$'000	n.p.	n.p.	18 726	19 227	20 278

a A change in accounting policy in 2000-01 resulted in a final dividend not being provided for because it was not yet announced by the shareholding ministers. From 2001-02 to 2003-04, the dividend included the final dividend from the previous year's operating results and the current year's interim dividend. This change in accounting standard affected the current ratio, and the comparability of the dividend to equity ratio and dividend payout ratio with those from before 2000-01. Under AASB 1044, dividends are now recognised in the financial year in which they are announced (see chapter 3). The Yarra Valley Water Board's preliminary final dividend estimate in respect of 2003-04 is $21.7 million, which will be payable in 2004-05. **n.p.** Not published.

BARWON REGIONAL WATER AUTHORITY — Victoria

Barwon Regional Water Authority (Barwon Water) was established under the *Water Act 1989*. Barwon Water provides water and sewerage services to nearly 260 000 residents in Geelong and surrounding areas, making it Victoria's largest regional urban water authority.

Prior to 2004, Barwon Water's Board set charges subject to ministerial approval. Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[1]

Barwon Water utilise a two-part pricing structure with volume charges accounting for 60 per cent of revenue from water and sewerage tariffs.

Reportedly, the strong financial performance helped finance capital expenditure of $35 million, contributing to a $59 million (6 per cent) increase in assets in 2003-04. Consistent with strategic direction to reduce interest bearing liabilities, debt levels continued to fall, resulting in a further decline in the debt to equity and debt to total assets ratios.

In 2003-04, revenue improved by $6 million (6 per cent) largely because of proceeds from the sale of developed land. Continued growth in the property market has contributed to the improvement in Barwon Water's financial performance since 2000-01, with revenue increasing by more than 40 per cent.

No dividend was payable by Barwon Water between 1999-00 and 2003-04, as determined by the Treasurer.

Barwon Water has not identified any payments for CSOs in its accounts.[2]

1 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in Barwon Water's retail licence, and addressing other non-pricing issues.

2 Barwon Water is reimbursed for the value of concessions provided to pensioners and others, and for the administration of the concession schemes. However, these amounts are not disclosed in Barwon Water's financial statements.

BARWON WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m	841	847	880	904	963
Total revenue	$m	73	71	81	95	101
Profitability						
Operating profit before tax	$'000	4 080	4 359	10 841	22 030	22 245
Operating sales margin	%	11.3	12.7	18.7	27.4	25.8
Cost recovery	%	118.7	114.3	123.0	137.7	134.7
Return on assets	%	1.0	1.1	1.8	2.9	2.8
Return on equity	%	0.5	0.6	1.4	1.9	1.9
Financial management						
Debt to equity	%	8.2	8.1	7.5	7.3	6.4
Debt to total assets	%	7.4	7.4	6.9	6.7	6.0
Total liabilities to equity	%	1 0.3	10.2	9.6	10.5	10.2
Interest cover	times	1.9	1.9	3.5	6.4	6.6
Current ratio	%	94.6	111.9	122.1	119.2	130.8
Leverage ratio	%	110.3	110.2	109.6	110.5	110.2
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0.0	0.0	0.0	0.0	0.0
Dividend payout ratio	%	0.0	0.0	0.0	0.0	0.0
Income tax expense	$'000	0	0	0	6 679	6 344
CSO funding	$'000	0	0	0	0	0

[a] Includes a revaluation increment of $25.4 million relating mainly to water distribution assets.

COLIBAN REGIONAL WATER AUTHORITY Victoria

Coliban Regional Water Authority (Coliban Water) was established in July 1992 under the *Water Act 1989*. It provides water and sewerage services to around 130 000 people in northern central Victoria.

Prior to 2004, Coliban Water's Board set charges subject to ministerial approval. Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[1]

Coliban Water contracts out a range of activities to the private sector and has several water treatment plants constructed under public–private sector partnerships. Contract payments for assets under public–private sector partnerships comprise fixed and variable components to be made by Coliban Water over a 25 year contract period.[2] In 2003-04, contract payments for water treatment services of $12 million was made, accounting for 25 per cent of total expenses.

In 2003-04, total assets declined by $16 million (22 per cent), largely because of a decrease in current investments by $15 million.

Despite an operating loss of $675 000, Coliban Water has continued to improve its position since 2000-01, when a loss of $5 million was recorded.

Coliban Water is subject to dividend and tax-equivalent payments. In 2003-04, no dividend or income tax was paid or provided for, reflecting Coliban Water's financial position.[3]

The Victorian Government reimbursed Coliban Water $2 million for concessions provided to pensioners and for rebates to non-profit organisations. This amount was not separately identified in Coliban Water's financial statements.

1 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in Coliban Water's retail licence, and addressing other non-pricing issues.

2 Coliban Water estimated that the present value in June 2004 of future contract payments over the life of the contract was $172 million.

3 Coliban Water expects to remain in a tax loss position for some time and thus is unlikely to incur tax-equivalent payments in the near future.

COLIBAN WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			640	652	648
Total revenue	$m			31	44	47
Profitability						
Operating profit before tax	$'000			- 4 913	- 2 041	- 675
Operating sales margin	%			- 32.7	- 13.5	- 7.6
Cost recovery	%			75.4	88.1	92.9
Return on assets	%			- 0.8	- 0.3	- 0.1
Return on equity	%			- 0.8	- 0.3	- 0.1
Financial management						
Debt to equity[b]	%			0.0	0.0	0.0
Debt to total assets[b]	%			0.0	0.0	0.0
Total liabilities to equity	%			1.4	2.1	1.5
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			1 021.0	595.3	672.7
Leverage ratio	%			101.4	102.1	101.5
Payments to and from government						
Dividends	$'000			3 760	0	0
Dividend to equity ratio	%			0.6	0	0.0
Dividend payout ratio	%			- 76.5	0	0.0
Income tax expense	$'000			0	0	0
CSO funding	$'000			n.p.	n.p.	n.p.

a 2001-02 was the first year that Coliban Water was included in this report. It was established in July 1992 under the *Water Act 1989*. **b** Coliban Water operates debt free, with capital expenditure funded from retained earnings and government grants. **n.r.** Not relevant. **n.p.** Not published.

GOULBURN VALLEY REGIONAL WATER AUTHORITY Victoria

Goulburn Valley Regional Water Authority (GVW) was established in March 1994 under the *Water Act 1989*. It provides water and sewerage services to a population of more than 100 000 in northern central Victoria, including the major towns of Seymour, Euroa and Shepparton.

Prior to 2004, GVW's Board set charges subject to ministerial approval. Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[1]

Capital expenditure in 2003-04 was $23 million.[2]

Operating profit before tax fell $6 million (37 per cent) in 2003-04, with revenue decreasing $4 million. Water restrictions, which led to a reduction in water usage, was the main reason for the decline in profitability.

GVW is subject to dividend and tax-equivalent payments. In 2003-04, the Treasurer determined that no dividend was payable and the tax–equivalent payment was deferred.[3]

GVW was not subject to CSOs over the reporting period.

1 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in GVW's retail licence, and addressing other non-pricing issues.

2 From 2003-04 to 2007-08, borrowings of $38 million will finance an expansive capital works program.

3 The payment has been deferred because of timing differences. The provision for deferred income tax has not been brought to account in the annual reports since it is considered unlikely that any taxation will occur in the foreseeable future.

GOULBURN VALLEY WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			430	448	457
Total revenue	$m			40	50	46
Profitability						
Operating profit before tax	$'000			8 751	15 000	9 448
Operating sales margin	%			21.1	29.6	20.5
Cost recovery	%			126.8	142.1	124.6
Return on assets	%			2.3	3.6	2.3
Return on equity	%			2.1	3.6	2.2
Financial management						
Debt to equity	%			2.7	2.3	2.6
Debt to total assets	%			2.6	2.3	2.5
Total liabilities to equity	%			4.3	4.6	4.5
Interest cover	times			10.0	19.3	13.4
Current ratio	%			441.4	125.3	126.4
Leverage ratio	%			104.3	104.6	104.5
Payments to and from government						
Dividends	$'000			0	0	0
Dividend to equity ratio	%			0.0	0.0	0.0
Dividend payout ratio	%			0.0	0.0	0.0
Income tax expense	$'000			0	0	0
CSO funding	$'000			0	0	0

a 2001-02 was the first year that Goulburn Valley Water was included in this report. It was established in March 1994 under the *Water Act 1989*.

CENTRAL GIPPSLAND WATER AUTHORITY — Victoria

Central Gippsland Water Authority (Gippsland Water) operates under the *Water Act 1989*. It provides water and sewerage services to over 130 000 people in 41 towns in the Traralgon area.

Prior to 2004, Gippsland Water's Board set charges subject to ministerial approval. Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[1]

In 2003-04, sales revenue from domestic customers and businesses accounted for 42 per cent and 35 per cent of total revenue respectively. Of this sales revenue, 66 per cent was from property-based charges with the remainder from usage-based charges.

Gippsland Water improved operating profit (pre-tax) by $5 million during 2003-04 to $6 million. This was reportedly because of the continued high level of property development, resulting in a $3 million increase in contributed assets.

Gippsland Water is subject to dividend and tax-equivalent payments. In 2003-04, the Treasurer determined that no dividend was payable and the tax–equivalent payment was deferred.[2]

The Victorian Government reimbursed Gippsland Water $2 million in 2003-04 for concessions including pensioner rebate and health care card schemes, water for fire-fighting purposes, and student education programs.

1 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in Gippsland Water's retail licence, and addressing other non-pricing issues.

2 The payment has been deferred because of timing differences. The provision for deferred income tax has not been brought to account in the annual reports since it is considered unlikely that any taxation will occur in the foreseeable future.

CENTRAL GIPPSLAND WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			480	479	487
Total revenue	$m			45	46	54
Profitability						
Operating profit before tax	$'000			1 062	- 1 404	5 743
Operating sales margin	%			0.7	- 5.0	9.0
Cost recovery	%			100.7	95.2	109.9
Return on assets	%			0.2	- 0.3	1.2
Return on equity	%			0.2	- 0.3	1.2
Financial management						
Debt to equity[d]	%			0.0	0.0	0.0
Debt to total assets[d]	%			0.0	0.0	0.0
Total liabilities to equity	%			1.1	1.3	2.1
Interest cover	times			n.r.	n.r.	n.r.
Current ratio[b]	%			547.4	541.7	355.2
Leverage ratio	%			101.1	101.3	102.1
Payments to and from government						
Dividends	$'000			0	0	0
Dividend to equity ratio	%			0.0	0.0	0.0
Dividend payout ratio	%			0.0	0.0	0.0
Income tax expense	$'000			0	0	0
CSO funding	$'000			1 912[c]	1 968	2 071

a 2001-02 was the first year that the Central Gippsland Water Authority (Gippsland Water) was included in this report. It was established in July 1994 under the *Water Act 1989*. **b** Gippsland Water's relatively high current ratio reflects its large holdings of liquid investments. **c** CSO payments were not disclosed separately in Gippsland Water's financial reports in 2001-02. This figure was obtained from the 2002-03 annual report. **d** Gippsland Water operates debt free, with capital expenditure funded from retained earnings and government grants. **n.r.** Not relevant.

CENTRAL HIGHLANDS WATER AUTHORITY — Victoria

Central Highlands Water Authority (CHW) operates under the *Water Act 1989*. It provides water and sewerage services to a population of 113 000 in Ballarat and surrounding areas.

CHW entered into a public–private sector agreement with Thames Water Ballarat on 12 April 1999. The contract requires CHW Water to pay an annual charge comprising both fixed and variable components for 25 years, after which ownership of the water treatment facility will transfer to CHW.[1]

Prior to 2004, CHW's Board set charges subject to ministerial approval. Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

In 2003-04, prices reportedly increased by 9 per cent, though this follows a 21 per cent reduction in charges from 1997-98 to 2002-03.

Total assets increased during 2003-04 by $9 million to $578 million, with $17 million invested in capital works, up from $13 million in 2002-03, as well as developer contributed assets rising $2 million. Further, debt has decreased $1 million (54 per cent) over the 2004 financial year, which is also down $8 million from 2001-02.

CHW is subject to dividend and tax-equivalent payments. In 2003-04, the Treasurer determined that no dividend was payable and the tax–equivalent payment was deferred.[3]

CHW is reimbursed for the value of concessions provided to pensioners and others, as well as for the administration of the concession schemes.

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1 At 30 June 2004, CHW estimated that the present value of the contract payments was $96 million, using a discount rate of 10 per cent. The payment obligation is subject to the future performance of Thames Water and, as such, is an Agreement Equally Proportionally Underperformed (AEPU) under accounting standard AASB 1044. AEPUs are not required to be recognised in the statement of financial position.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in CHW's retail licence, and addressing other non-pricing issues.

3 The payment has been deferred because of timing differences. The provision for deferred income tax has not been brought to account in the annual reports since it is considered unlikely that any taxation will occur in the foreseeable future.

CENTRAL HIGHLANDS WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*
Size						
Total assets	$m			570	569	578
Total revenue	$m			40	46	49
Profitability						
Operating profit before tax	$'000			1 230	4 806	4 900
Operating sales margin	%			2.6	9.1	8.2
Cost recovery	%			102.7	110.0	108.9
Return on assets	%			0.4	1.0	0.9
Return on equity	%			0.2	0.9	0.9
Financial management						
Debt to equity	%			1.6	0.4	0.2
Debt to total assets	%			1.6	0.4	0.2
Total liabilities to equity	%			3.0	1.7	1.5
Interest cover	times			2.1	7.2	26.1
Current ratio	%			529.1	529.1	486.9
Leverage ratio	%			103.0	101.7	101.5
Payments to and from government						
Dividends	$'000			516	0	0
Dividend to equity ratio	%			0.1	0.0	0.0
Dividend payout ratio	%			42.0	0.0	0.0
Income tax expense	$'000			0	0	0
CSO funding	$'000			2 025	2 010	2 079

a 2001-02 was the first year that the Central Highlands Water Authority was included in this report. It was established in July 1994 under the *Water Act 1989*. **b** Includes amendments to income tax expense and total liabilities due to the incorrect treatment of deferred assets by GFS.

GIPPSLAND AND SOUTHERN RURAL WATER AUTHORITY Victoria

Gippsland and Southern Rural Water Authority (Southern Rural Water) was established on 1 July 1995 under the *Water Act 1989*.

Southern Rural Water provides irrigation water to over 10 000 customers in three irrigation districts and administers over 8200 licences, managing the taking and use of water from rivers, streams and groundwater sources in southern Victoria. It also manages several water storage dams that provide water to irrigators, urban water authorities and several power generators.

Prior to 2004, Southern Rural Water's Board set charges for irrigation water in consultation with customer committees subject to ministerial approval. Charges are based on providing adequate funding to maintain the condition of channels, pipelines and structures using the renewals annuity concept (see box 6.1). Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[1]

Reportedly, overall prices increased during 2003-04 to meet cost recovery requirements.

In 2003-04, Southern Rural Water recorded a net loss, however, operating losses have decreased since 2001-02 from $6 million to $1 million in 2003-04. Despite the losses, Southern Rural Water was required to make dividend payments.

Southern Rural Water is subject to tax-equivalent payments. In 2003-04, no income tax was paid, reflecting Southern Rural Water's financial position.[2]

Southern Rural Water receives CSO payments for programs including salinity projects, state water assessment, groundwater investigations and water resource management.[3]

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1 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in Southern Rural Water's retail licence, and addressing other non-pricing issues.

2 Southern Rural Water expects to remain in a tax loss position for some time and thus is unlikely to incur tax-equivalent payments in the near future.

3 Southern Rural Water also manages recreation facilities at Blue Rock, Cowwarr, Glenmaggie, Melton, Merrimu and Pykes Creek Reservoir. It is not reimbursed by the Government for the associated expenses.

GIPPSLAND AND SOUTHERN RURAL WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			440	435	435
Total revenue	$m			14	18	19
Profitability						
Operating profit before tax	$'000			- 5 536	- 3 234	- 1 404
Operating sales margin	%			- 43.2	- 19.6	- 8.5
Cost recovery	%			69.8	83.6	92.2
Return on assets	%			- 1.3	- 0.7	- 0.3
Return on equity	%			- 1.3	- 0.7	- 0.3
Financial management						
Debt to equity[b]	%			0.0	0.0	0.0
Debt to total assets[b]	%			0.0	0.0	0.0
Total liabilities to equity	%			1.1	0.9	1.0
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			309.1	257.0	274.4
Leverage ratio	%			101.1	100.9	101.0
Payments to and from government						
Dividends	$'000			418	418	418
Dividend to equity ratio	%			0.1	0.1	0.1
Dividend payout ratio	%			- 7.6	- 12.9	- 29.8
Income tax expense	$'000			0	0	0
CSO funding	$'000			957	882	1 159

a 2001-02 was the first year that the Gippsland and Southern Rural Water Authority (Southern Rural Water) was included in this report. It was established in July 1995 under the *Water Act 1989*. **b** Southern Rural Water operates debt free, with capital expenditure funded from retained earnings and government grants. **n.r.** Not relevant.

SUNRAYSIA RURAL WATER AUTHORITY — Victoria

Sunraysia Rural Water Authority (Sunraysia Rural Water) was established on 1 July 1994 under the *Water Act 1989*. [1]

Sunraysia Rural Water provides irrigation water to growers in the irrigation districts of Merbein, Red Cliffs and Robinvale. It also delivers water for stock and garden purposes to residents of the Millewa Rural District and the Waterworks District of Carwarp–Yelta and manages private water diversion activities from the Murray River between the Nyah pumps and the South Australia border.

Prior to 2004, Sunraysia Rural Water's Board set charges subject to ministerial approval. Charges are based on providing adequate funding to maintain the condition of the required network of channels, pipelines and structures using the renewals annuity concept (see box 6.1). Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

The majority of Sunraysia Rural Water's revenue comes directly from supplying water. During 2003-04, around 60 per cent of Sunraysia Rural Water's revenue came from fixed water charges, with a further 28 per cent from variable water charges. Operating profit (pre-tax) increased slightly in 2003-04.

During 2003-04, the Victorain Government reimbursed Sunraysia Rural Water $133 000 for community service obligation programs including pensioner concessions ($11 000), salinity management and the construction of drainage schemes.

1 On 1 July 2004, Sunraysia Rural Water and Lower Murray Water merged, trading under the name Lower Murray Water.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in Sunraysia Rural Water's retail licence, and addressing other non-pricing issues.

SUNRAYSIA RURAL WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			118	121	124
Total revenue	$m			13	14	15
Profitability						
Operating profit before tax	$'000			1 425	1 362	1 720
Operating sales margin	%			7.4	6.5	7.2
Cost recovery	%			108.0	107.0	107.8
Return on assets	%			1.2	1.1	1.4
Return on equity	%			1.0	0.8	1.0
Financial management						
Debt to equity[b]	%			0.0	0.0	0.0
Debt to total assets[b]	%			0.0	0.0	0.0
Total liabilities to equity	%			4.6	5.1	6.2
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			250.4	294.0	303.8
Leverage ratio	%			104.6	105.1	106.2
Payments to and from government						
Dividends	$'000			88	88	88
Dividend to equity ratio	%			0.1	0.1	0.1
Dividend payout ratio	%			8.1	9.5	7.4
Income tax expense	$'000			339	432	538
CSO funding	$'000			197	186	133

a 2001-02 was the first year that the Sunraysia Rural Water Authority (Sunraysia Rural Water) was included in this report. It was established in July 1994 under the *Water Act 1989*. **b** Sunraysia Rural Water operates debt free, with capital expenditure funded from retained earnings and government grants. **n.r.** Not relevant.

WIMMERA MALLEE RURAL WATER AUTHORITY — Victoria

Wimmera Mallee Rural Water Authority (WMW) was established on 1 July 1994 under the *Water Act 1989*. WMW supplies water in central western Victoria to farm dams and irrigators, through pipelines or open channel systems. It also provides bulk water to regional urban water suppliers and manages water storages.[1]

Prior to 2004, WMW's Board set charges subject to ministerial approval. Charges are based on providing adequate funding to maintain the condition of the required network of channels, pipelines and structures using the renewals annuity concept (see box 6.1). Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[2]

The current ratio has risen significantly from 356 per cent in 2001-02 to 706 per cent in 2003-04. This was due to current assets increasing 60 per cent and current liabilities decreasing 19 per cent from 2001-02 to 2003-04.

In 2003-04, total revenue fell by $4 million following a one-off contribution of $5 million for capital works in 2002-03. This was the third consecutive reporting year WMW recorded an operating loss. Despite the losses, WMW was required to make dividend payments.

WMW is subject to tax-equivalent payments. In 2003-04, no income tax was paid reflecting WMW's financial position.[3]

In 2003-04, WMW received $9000 for CSOs relating to the provision of concessions to pensioners, though this amount was not disclosed separately in the financial statements.

1 On 1 July 2004, WMW and Grampians Water merged, trading under the name Grampians Wimmera Mallee Water.

2 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in WMW's retail licence, and addressing other non-pricing issues.

3 WMW expects to remain in a tax loss position for some time and thus is unlikely to incur tax-equivalent payments in the near future.

WIMMERA MALLEE RURAL WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			352	357	351
Total revenue	$m			11	16	12
Profitability						
Operating profit before tax	$'000			- 5 067	- 153	- 5 368
Operating sales margin	%			- 38.7	- 2.5	- 52.5
Cost recovery	%			72.1	97.5	65.6
Return on assets	%			- 1.4	0.0	- 1.5
Return on equity	%			- 1.5	0.0	- 1.5
Financial management						
Debt to equity [b]	%			0.0	0.0	0.0
Debt to total assets [b]	%			0.0	0.0	0.0
Total liabilities to equity	%			1.1	1.1	1.0
Interest cover	times			- 1 265.8	n.r.	n.r.
Current ratio	%			356.1	627.3	706.0
Leverage ratio	%			101.1	101.1	101.0
Payments to and from government						
Dividends	$'000			209	209	209
Dividend to equity ratio	%			0.1	0.1	0.1
Dividend payout ratio	%			- 4.1	- 4.1	- 3.9
Income tax expense	$'000			0	0	0
CSO funding	$'000			n.p.	n.p.	n.p.

a 2001-02 was the first year that the Wimmera Mallee Rural Water Authority (WMW) was included in this report. It was established in July 1994 under the *Water Act 1989*. **b** WMW operates debt free, with capital expenditure funded from retained earnings and government grants. **n.r.** Not relevant. **n.p.** Not published.

GOULBURN–MURRAY RURAL WATER AUTHORITY Victoria

Goulburn–Murray Rural Water Authority (GMW) was established on 1 July 1994 under the *Water Act 1989*. GMW is responsible for the supply, storage and delivery of water to irrigators and regional urban water authorities over an area of 68 000 square kilometres in northern Victoria. It is also responsible for the management and operation of several facilities for the Murray–Darling Basin Commission.

Prior to 2004, GMW's Board set charges for water entitlements subject to ministerial approval. Charges are based on providing adequate funding to maintain the condition of the required network of channels, pipelines and structures using the renewals annuity concept (see box 6.1). Commencing 1 January 2004, the Essential Services Commission (ESC) was given the responsibility to regulate pricing and service standards of all Victorian water authorities.[1]

GMW's total assets increased by $183 million in 2003-04, primarily because of a revaluation increment of $157 million in infrastructure. Also, capital expenditure decreased by $10 million to $33 million, with $15 million borrowed from Treasury.

In 2003-04, GMW recorded an operating profit before tax of $2 million, improving from a $22 million operating loss in 2002-03. An increase in revenue of $20 million ($10 million for Victorian Government funding and $9 million for rates and consumptive charges revenue) contributed to this result.

GMW is subject to dividend and tax-equivalent payments. In 2003-04, the Treasurer determined that no dividend was payable and the tax–equivalent payment was deferred.[2]

During 2003-04, GMW received $37 000 for CSOs relating to provisions of concessions to pensioners, though this amount was not disclosed separately in financial statements.

1 Prior to 1 January 2004, the ESC's role was limited to monitoring and enforcing service standard obligations contained in GMW's retail licence, as well as addressing other non-pricing issues.

2 The payment has been deferred because of timing differences. The provision for deferred income tax has not been brought to account in the annual reports since it is considered unlikely that any taxation will occur in the foreseeable future.

GOULBURN–MURRAY RURAL WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*[b]
Size						
Total assets	$m			1 738	1 719	1 902
Total revenue	$m			103	93	113
Profitability						
Operating profit before tax	$'000			- 7 526	- 21 608	2 086
Operating sales margin	%			- 8.7	- 24.5	1.3
Cost recovery	%			92.0	80.3	101.3
Return on assets	%			- 0.4	- 1.3	0.1
Return on equity	%			- 0.4	- 1.3	0.1
Financial management						
Debt to equity[c]	%			0.0	0.0	0.8
Debt to total assets[c]	%			0.0	0.0	0.8
Total liabilities to equity	%			2.0	2.2	2.9
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			200.1	83.0	147.5
Leverage ratio	%			102.0	102.2	102.9
Payments to and from government						
Dividends	$'000			0	0	0
Dividend to equity ratio	%			0.0	0.0	0.0
Dividend payout ratio	%			0.0	0.0	0.0
Income tax expense	$'000			0	0	0
CSO funding	$'000			n.p.	n.p.	n.p.

a 2001-02 was the first year that the Goulburn–Murray Water Authority was included in this report. It was established in July 1994 under the *Water Act 1989*. **b** Includes a revaluation increment of $157 million in infrastructure. **c** GMW operated debt free, with capital expenditure funded from retained earnings and government grants until 2003-04. A $20 million loan from Victoria Treasury for 20 years at a fixed interest rate of 6.34 per cent was taken in July 2003. **n.r.** Not relevant. **n.p.** Not published.

SUNWATER Queensland

Sunwater was established under the *Government Owned Corporations Act 1993* on 1 October 2000, assuming the roles and responsibilities of State Water Projects.[1] Sunwater owns and operates bulk water storage and distribution infrastructure and supplies irrigators, industrial and urban bulk water customers.

Charges for rural customers are determined by Sunwater's shareholding ministers. A price direction in October 2000 set a price path of between five and seven years to achieve minimum cost recovery targets for the irrigation sector of Sunwater's various water supply schemes.

In 1999-00 there was a revaluation of water infrastructure with a move from deprival valuation to fair value methodology. The resulting large fall in the value of assets — from $2.1 billion to $235 million — led to $1.9 billion being written-down against the asset revaluation reserve.

Water infrastructure assets were subsequently revalued upward, by $23.3 million in 2000-01, $33.8 million in 2001-02 and $82.5 million in 2002-03. In 2003-04, a $70 million revaluation decrement led to assets decreasing by $64 million and lower returns on assets and returns on equity.

In 2003-04, debt fell by $15 million resulting in a significant decline in debt to equity and debt to total assets.

Operating profit before tax fell $7 million (25 per cent) in 2003-04, reportedly because of an increase in depreciation and amortisation, as well as a decrease in the gain on revaluation of non-current assets.

Sunwater received CSO funding from the Queensland Government for shortfalls in revenue from providing water to rural water users, costs to comply with new governing legislation and payment for new rural water assets or extensions to existing schemes built for reasons other than commercial return.[2]

1 Eungella Water Pipeline Pty Ltd and North–West Queensland Water Pipeline Pty Ltd are wholly-owned subsidiaries of Sunwater.

2 Sunwater is also responsible for the provision and maintenance of recreational facilities, for which it receives no CSO payments.

SUNWATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[f]
Size						
Total assets	$m	235	312	360	457	392
Total revenue	$m	99	92	113	110	109
Profitability						
Operating profit before tax	$'000	4 706	4 656	30 359	26 102	19 541
Operating sales margin	%	2.5	4.5	27.1	23.2	16.5
Cost recovery	%	101.4	104.8	137.2	130.2	119.8
Return on assets	%	0.4	2.2	9.7	6.9	5.0
Return on equity	%	0.4	1.9	11.1	7.5	3.7
Financial management						
Debt to equity	%	2.2	11.1	8.6	5.9	2.5
Debt to total assets	%	0.4	10.2	7.6	5.7	2.0
Total liabilities to equity	%	2.5	25.0	20.3	16.0	15.4
Interest cover	times	4 707.0	4.2	15.0	14.6	12.0
Current ratio	%	309.9	268.2	344.8	407.9	467.0
Leverage ratio	%	102.5	125.0	120.3	116.0	115.4
Payments to and from government						
Dividends	$'000	0	0	0	4 127[e]	4 000
Dividend to equity ratio	%	0.0	0.0	0.0	1.2	1.1
Dividend payout ratio	%	0.0	0.0	0.0	19.5	29.5
Income tax expense	$'000	0	1 869	4 219	4 890	5 976
CSO funding	$'000	25 681	15 368	15 368	9 494	8 663

[a] A revaluation to water infrastructure assets in 1999-00 resulted in $1.9 billion being written down directly against the asset revaluation reserve. [b] Includes the operations of Sunwater from October 2000 to June 2001. State Water Projects' revenue and expenses for the period July 2000 to September 2000 were combined with Sunwater to obtain results for the full financial year. Results include a $23.3 million revaluation increment to water infrastructure assets. [c] Includes a revaluation increment of $33.8 million relating to water infrastructure assets. [d] Includes a revaluation increment of $82.5 million relating to water infrastructure assets. [e] Includes $600 000 for 2001-02 and $3.6 million for 2002-03. [f] Includes a revaluation decrement of $69.8 million relating to water infrastructure assets.

SA WATER CORPORATION — South Australia

South Australia Water Corporation (SA Water) was established under the *South Australian Water Corporation Act 1994* and operates subject to the *Public Corporations Act 1993*. SA Water provides water and wastewater services to 1.4 million customers in both the metropolitan and country areas of South Australia.

SA Water's metropolitan water and sewerage operations generated 65 per cent of revenue and accounted for 60 per cent of its assets in 2003-04. Country operations generated 30 per cent of revenue and accounted for 40 per cent of assets. Charges for water and sewerage services are set by the Minister for Administrative Services after consultation with SA Water.

The management, operation and maintenance of SA Water's metropolitan water and sewerage operations was contracted out in 1996 for a period of 15 years. The contract requires the private contractor to meet performance targets under a fee-for-service arrangement.

Total assets increased by $280 million (4.3 per cent) in 2003-04 mainly because of an asset revaluation increment of $188 million, as well as an increase in capital expenditure by $56 million to $187 million, which also contributed to an increase debt by $73 million (6 per cent).

In 2003-04, SA Water's operating profit before tax improved slightly despite the introduction of water restrictions and water conservation measures.

SA Water receives CSO payments relating to the provision of water and wastewater services in country areas, the administration of a pensioner concession scheme, and the provision of water and wastewater concessions to exempt properties, such as charities.

SOUTH AUSTRALIAN WATER CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*[b]
Size						
Total assets[a]	$m	6 026	6 059	6 212	6 562	6 843
Total revenue	$m	598	604	629	701	733
Profitability						
Operating profit before tax	$'000	196 445	200 539	215 368	264 081	267 309
Operating sales margin	%	48.0	47.9	48.2	49.5	47.2
Cost recovery	%	197.3	190.5	191.5	196.2	182.8
Return on assets	%	4.8	4.8	4.9	5.4	5.2
Return on equity	%	3.0	2.9	3.2	3.8	3.4
Financial management						
Debt to equity	%	22.6	25.9	24.7	23.9	24.4
Debt to total assets	%	17.8	20.0	19.5	19.2	19.4
Total liabilities to equity	%	28.4	29.5	28.8	27.7	28.3
Interest cover	times	3.2	3.2	3.5	4.2	4.4
Current ratio	%	62.2	97.3	97.0	75.3	76.1
Leverage ratio	%	128.4	129.5	128.8	127.7	128.3
Payments to and from government						
Dividends	$'000	175 200	135 470	137 175	164 845	174 110
Dividend to equity ratio	%	3.8	2.9	2.9	3.3	3.3
Dividend payout ratio	%	123.6	100.6	89.0	86.8	96.9
Income tax expense	$'000	54 706	65 827	61 161	74 233	87 544
CSO funding	$'000	85 259	86 104	90 358	91 706	101 556

a Asset revaluations in each year of the reporting period resulted in an increase in the value of assets by $87.2 million (1999-00), $9.5 million (2000-01), $130 million (2001-02), $322 million (2002-03) and $188 million (2003-04). **b** Includes a special dividend of $10 million.

WATER CORPORATION — Western Australia

The Water Corporation was established on 1 January 1996 under the *Water Corporation Act 1995*. The Water Corporation provides public water supply, sewerage and drainage services and bulk water to almost 2 million people in 255 towns and communities throughout Western Australia.

The Water Corporation operates under a 25 year licence issued under the *Water Services Licensing Act 1995*. On 1 January 2004, the Economic Regulation Authority (ERA) assumed responsibility for the licensing regime of service providers and the ability to conduct reviews of various industry issues, including water pricing. The ERA is currently conducting a pricing review, with the final report due in August 2005. The WA Government remains responsible for the setting of water prices.

In 2003-04, assets grew by $226 million to $9940 million, mainly because of capital expenditure of $440 million, which also contributed to an increase in debt by $95 million.

In 2003-04, operating profit before tax increased by $85 million to $554 million, with revenue increasing by $104 million while expenses increased only $18 million. Strong growth in the property market, resulting in an increase in developer contributions by $43 million (34 per cent), contributed to the improvement in the Water Corporation's financial performance.

Over the reporting period, the Water Corporation received CSO payments for costs incurred in providing country services, a program to eliminate septic tanks to protect groundwater, waterways and public health, and pensioner concessions.

WATER CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	9 174	9 457	9 579	9 713	9 939
Total revenue	$m	987	1 012	1 042	1 104	1 208
Profitability						
Operating profit before tax	$'000	452 238	445 083	422 851	469 015	554 474
Operating sales margin	%	49.4	47.0	45.1	48.0	49.9
Cost recovery	%	197.5	188.8	182.1	192.3	199.6
Return on assets	%	5.4	5.1	5.0	5.5	6.2
Return on equity	%	3.9	3.6	3.6	4.0	4.7
Financial management						
Debt to equity	%	7.1	10.4	11.1	12.0	13.0
Debt to total assets	%	6.4	9.1	9.6	10.2	11.0
Total liabilities to equity	%	13.7	16.3	17.2	17.7	19.1
Interest cover	times	13.2	14.5	9.5	8.5	11.8
Current ratio	%	47.8	51.2	33.9	46.1	29.8
Leverage ratio	%	113.7	116.3	117.2	117.7	119.1
Payments to and from government						
Dividends	$'000	201 215	240 753	259 811	255 293	291 545
Dividend to equity ratio	%	2.5	3.0	3.2	3.1	3.5
Dividend payout ratio	%	64.4	82.0	87.9	77.8	75.4
Income tax expense	$'000	139 894	151 575	127 260	140 971	168 034
CSO funding	$'000	205 617	225 890	240 197	258 403	268 393

HOBART REGIONAL WATER AUTHORITY — Tasmania

The Hobart Regional Water Authority, trading as Hobart Water, was established as a Joint Authority under the *Local Government Act 1993*. Hobart Water commenced operations on 1 January 1997 following the transfer of assets, property rights and liabilities from its predecessor, the Hobart Regional Water board. Hobart Water provides bulk water supplies to its owner-councils.[1]

In 2003-04, 88 per cent of Hobart Water's revenue came from bulk water and a further 12 per cent from investments and favourable hedging outcomes.

Maximum charges for bulk water are determined by the Minister for Local Government on recommendations by the Government Prices Oversight Commission.[2] In 2003-04, nominal charges reportedly increased by 6.1 per cent.

In 2003-04, Hobart Water recorded an increase of $382 000 (11 per cent) in operating profit before tax, largely because of increased water sales.

Hobart Water was not subject to CSOs over the reporting period.[3]

1 The councils that comprise the Joint Authority are Brighton Council, Clarence City Council, Derwent Valley Council, Glenorchy City Council, Hobart City Council, Kingborough Council, Sorell Council and Southern Midlands Council.

2 Under the *Government Prices Oversight Act 1995*, the recommendations may take the form of maximum revenue, maximum prices, pricing principles or a combination of these.

3 In 2003-04, Hobart Water identified expenses of $252 000 relating to the maintenance of recreation facilities.

HOBART REGIONAL WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	171	169	171	169	180
Total revenue	$m	19	20	20	24	24
Profitability						
Operating profit before tax	$'000	2 757	2 535	3 272	3 420	3 802
Operating sales margin	%	24.0	23.5	26.6	27.7	28.2
Cost recovery	%	131.6	130.7	136.3	138.3	139.2
Return on assets	%	2.8	2.8	3.8	4.9	4.9
Return on equity	%	1.4	1.5	1.9	2.4	2.1
Financial management						
Debt to equity	%	27.1	26.3	26.2	26.2	24.4
Debt to total assets	%	20.0	19.5	19.5	19.5	19.0
Total liabilities to equity	%	35.0	34.1	35.2	33.5	32.1
Interest cover	times	2.4	2.2	2.0	1.7	1.8
Current ratio	%	34.4	26.9	51.6	60.4	80.2
Leverage ratio	%	135.0	134.1	135.2	133.5	132.1
Payments to and from government						
Dividends[a]	$'000	2 500	2 400	2 100	0	3 000
Dividend to equity ratio	%	2.0	1.9	1.7	0.0	2.3
Dividend payout ratio	%	137.9	129.0	88.2	0.0	109.7
Income tax expense	$'000	944	675	892	407	1 068
CSO funding	$'000	0	0	0	0	0

Note All results taken from General Purpose Financial Report data because of the unavailability of Government Financial Statistics data (see chapter 3). **a** A change in accounting policy to meet the requirements of AASB 1044 meant that no dividend was recognised in 2002-03 (see chapter 3). The Board of Management of the Hobart Regional Water Authority (Hobart Water) has recommended to the Joint Authority Members that a $2.8 million dividend be declared from the profits of 2003-04 in accordance with Hobart Water's Dividend Policy. The provision for dividend had not been recognised in the financial statements as at 30 June 2004.

CRADLE COAST WATER — Tasmania

Cradle Coast Water (CCW) was established as a Joint Authority on 10 August 1999 under the *Local Government Act 1993*.[1] CCW collects, treats and supplies bulk drinking water to its joint owning councils — Circular Head, Central Coast, Waratah-Wynyard, Devonport City, Latrobe and Kentish.

Maximum charges for bulk water are determined by the Minister for Local Government on recommendations by the Government Prices Oversight Commission.[2] During 2003-04, the variable charge component for water fell 0.5 per cent, however fixed charges increased by 3 per cent.

Largely as a result of new investments, current assets increased by $236 000 (9.4 per cent) in 2003-04. However, a rise in CCW's current debt levels by $417 000 and a bank overdraft of $268 000 contributed to an increase in current liabilities by $557 000 (20.5 per cent), which significantly decreased the current ratio.

In 2003-04, operating profit before tax increased $69 000 (5.8 per cent), despite a $12 000 (22 per cent) decrease in investment income. CCW's improved financial performance can be attributed a $249 million increase in water sales.

CCW did not receive CSO payments in 2003-04. Prior to 2001-02, fluoridation was identified as a CSO and reimbursed by the Government.

1 CCW was the trading name of the North West Water Authority (NWWA) over the period July 2000 to December 2001. On 12 December 2001, the NWWA adopted the trading name as its legal title.

2 Under the *Government Prices Oversight Act 1995*, the recommendations can take the form of maximum revenue, maximum prices, pricing principles, or a combination of these.

CRADLE COAST WATER (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*[a]	*2001-02*[b]	*2002-03*[c]	*2003-04*[d]
Size						
Total assets	$m	59	61	61	64	65
Total revenue	$m	7	8	8	8	8
Profitability						
Operating profit before tax	$'000	838	1 390	856	1 190	1 259
Operating sales margin	%	29.9	34.7	28.3	30.9	30.2
Cost recovery	%	151.1	153.3	139.5	144.8	143.3
Return on assets	%	3.6	4.7	3.7	4.1	4.0
Return on equity	%	1.9	3.7	2.2	3.0	2.8
Financial management						
Debt to equity	%	68.2	63.0	60.2	53.2	51.7
Debt to total assets	%	38.7	37.7	36.1	34.2	33.0
Total liabilities to equity	%	74.5	69.6	66.8	59.4	58.0
Interest cover	times	1.6	2.0	1.6	1.9	2.0
Current ratio	%	90.0	121.4	97.8	92.6	84.0
Leverage ratio	%	174.5	169.6	166.8	159.4	158.0
Payments to and from government						
Dividends	$'000	345	514	428	0[e]	595
Dividend to equity ratio	%	1.0	1.5	1.2	0.0	1.5
Dividend payout ratio	%	53.9	40.0	53.1	0.0	52.4
Income tax expense	$'000	197	104	49	39	123
CSO funding	$'000	27	31	0	0	0

Note All results taken from General Purpose Financial Report data because of the unavailability of Government Financial Statistics data (see chapter 3). **a** Includes an asset revaluation increment of $2 million. **b** Includes an asset revaluation increment of $191 000. **c** Includes an asset revaluation increment of $2.6 million. **d** Includes an asset revaluation decrement of $32 000. **e** A change in accounting policy to meet the requirements of AASB 1044 meant that no dividend was recognised in 2002-03 (see chapter 3).

ESK WATER AUTHORITY Tasmania

The Esk Water Authority, trading as Esk Water, was established as a Joint Authority under the *Local Government Act 1993*. Esk Water commenced operations in July 1997, following the transfer of assets from its predecessors, the North Esk Scheme, West Tamar Scheme and the Launceston City Council. Esk Water provides bulk water supply to councils and industrial users in the Launceston–Tamar Valley region.[1]

Maximum charges for bulk water are determined by the Minister for Local Government on recommendations by the Government Prices Oversight Commission.[2] Esk Water utilise a two-part tariff structure, which was implemented in 2001-02. The variable component of the price reportedly was reduced by 8.1 per cent during 2003-04.

Total assets increased by $6 million to $106 million and total liabilities decreased $4 million to $9 million in 2003-04. Further, current assets fell by $3 million (37 per cent) and current liabilities also dropped by $5 million (85 per cent) in the financial year. These results are attributable to Esk Water repaying a large proportion of debt ($5 million or 71 per cent), which significantly improved the levels of debt to equity, debt to total assets, total liabilities to equity and the current ratio.

Capital expenditure of $1.1 million in 2003-04 was internally funded.

In 2003-04, operating profit before tax fell $307 000 (11 per cent) to $2.6 million with a $470 000 (7 per cent) increase in expenses.

Esk Water was not subject to CSOs over the reporting period.

1 The participating councils in the Joint Authority are Launceston City, George Town, Meander Valley and West Tamar. On its inception, Esk Water's equity was contributed by the State Government (88 per cent), Launceston City Council (11 per cent) and Meander Valley Council (0.6 per cent).

2 Under the *Government Prices Oversight Act 1995*, the recommendations may take the form of maximum revenue, maximum prices, pricing principles or a combination of these.

ESK WATER AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*[c]	*2003-04*[d]
Size						
Total assets	$m	100	102	103	100	106
Total revenue	$m	8	8	9	9	10
Profitability						
Operating profit before tax	$'000	1 209	1 950	2 546	2 926	2 619
Operating sales margin	%	25.0	30.5	34.9	35.5	30.8
Cost recovery	%	130.5	144.0	153.5	155.1	144.5
Return on assets	%	2.0	2.5	3.1	3.4	3.1
Return on equity	%	1.0	1.5	1.9	2.3	1.9
Financial management						
Debt to equity	%	12.8	8.9	8.9	8.0	2.1
Debt to total assets	%	10.8	7.9	7.8	6.9	1.9
Total liabilities to equity	%	16.6	13.9	14.9	14.4	8.8
Interest cover	times	2.4	4.2	5.2	6.3	5.7
Current ratio	%	83.2	175.6	205.0	124.4	526.0
Leverage ratio	%	116.6	113.9	114.9	114.4	108.8
Payments to and from government						
Dividends	$'000	594	1 337	1 683	2 011	2 048
Dividend to equity ratio	%	0.7	1.5	1.9	2.3	2.2
Dividend payout ratio	%	68.8	100.0	100.7	100.0	115.1
Income tax expense	$'000	345	613	875	914	839
CSO funding	$'000	0	0	0	0	0

Note All results taken from General Purpose Financial Report data because of the unavailability of Government Financial Statistics data (see chapter 3). [a] Includes abnormal revenue of $156 000 from the revaluation of superannuation liability. [b] A revaluation resulted in an increase of $3.3 million in the value of pipes and other fixed assets. [c] Includes an asset revaluation decrement of $3 million. [d] Includes an asset revaluation increment of $10 million.

ACTEW CORPORATION — Australian Capital Territory

ACTEW Corporation provides water and sewerage services to around 125 000 domestic and commercial customers in the Australian Capital Territory and Queanbeyan. ACTEW Corporation was established under the *Corporations Act 2001* (Cwlth) and has reporting and compliance obligations under the *Territory Owned Corporations Act 1990*. ActewAGL — a joint venture with privately-owned energy company AGL — provides gas and electricity services and manages ACTEW Corporation's water and sewerage assets under contract.[1]

ACTEW Corporation also has a 25 per cent investment in TransACT Communications Pty Ltd, a broadband communications provider in the Canberra area. ACTEW Corporation's ownership interest in ActewAGL represented 26 per cent.

Water, sewerage, gas and electricity charges are set by the Australian Capital Territory Independent Competition and Regulatory Commission (ICRC).[2]

Total assets increased by $20 million in 2003-04, largely because of an increase in short-term securities held and strong capital expenditure growth over the financial year. Capital expenditure was funded from cash reserves, with debt reduced by $9 million from the previous financial year. Water and sewerage assets accounted for around 64 per cent of total assets in 2003-04.

ACTEW Corporation's operating profit (pre-tax) fell by $21 million (33 per cent) in 2003-04, primarily because of a $40 million write-down of TransACT.

The ACT Treasury allowed the dividend payment for 2003-04 to be postponed to 2004-05 to assist in expanding the water treatment plant at Googong, a new water treatment plant at Mt Stromlo, catchment remediation costs and water conservation.

ACTEW Corporation was not subject to CSOs over the reporting period.

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1 ActewAGL's operations are included in ACTEW Corporation's financial results using the 'equity accounting' method. Under this method, ACTEW Corporation's initial investment in ActewAGL is recognised as an asset. Adjustments are made to the value of the investment to reflect ACTEW Corporation's share of profits or losses in ActewAGL each year. In 2003-04, ActewAGL's assets were valued at around $874 million with revenue of $547 million. ACTEW Corporation holds a 50 per cent share in ActewAGL.

2 Commencing 1 July 2004, a four year price path of CPI plus 2.5 per cent for water and CPI plus 1 per cent for wastewater will take effect, as determined by the ICRC.

ACTEW CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			1 326	1 334	1 354
Total revenue	$m			185	191	154
Profitability						
Operating profit before tax	$'000			72 862	62 942	42 022
Operating sales margin	%			53.2	45.3	41.0
Cost recovery	%			203.8	174.6	159.6
Return on assets	%			7.5	6.6	4.8
Return on equity	%			5.9	5.5	1.5
Financial management						
Debt to equity	%			45.2	44.4	42.6
Debt to total assets	%			27.2	26.4	25.5
Total liabilities to equity	%			66.5	68.5	68.4
Interest cover	times			3.8	3.5	2.8
Current ratio	%			104.7	136.7	145.3
Leverage ratio	%			166.5	168.5	168.4
Payments to and from government						
Dividends	$'000			46 887	47 700	0[b]
Dividend to equity ratio	%			5.9	6.0	0.0
Dividend payout ratio	%			100.1	110.0	0.0
Income tax expense	$'000			26 034	19 561	29 846
CSO funding	$'000			0	0	0

[a] 2001-02 was the first year that ACTEW Corporation was included in the water sector. It commenced operations as a water business in July 1995. [b] The dividend payment for 2003-04 was postponed to 2004-05.

7 Urban transport

The financial performances of four urban transport government trading enterprises (GTEs) are covered in this chapter. At the end of 2003-04, they controlled $1.3 billion in assets and had generated around $740 million in revenue in that year. These urban transport GTEs vary in size and the range of services they provide.

Financial performance summaries, including performance indicators for each individual GTE and a summary of performance indicators for the sector as a whole, are presented after this introduction. The performance indicators are consistent across individual GTEs. However, when making comparisons, care should be taken to consider differences in the nature and scale of the businesses, their market environments and issues relating to the valuation of their assets.

For a discussion of the data, the financial indicators used and some of the factors that should be considered when assessing performance, see chapter 3.

7.1 Monitored GTEs

The selected GTEs vary in the range of services they provide, their size and their corporate structure. The primary activity of most of the urban transport GTEs is the provision of bus services (see table 7.1). However, the State Transit Authority (STA) in New South Wales and TransAdelaide operate other modes of transport. In addition to its bus services, the STA also operates passenger ferries. TransAdelaide operates passenger rail and tram services and is also responsible for the management of the metropolitan rail network.

Table 7.1 **Activities — monitored urban transport GTEs, 2003-04**

	Bus	*Ferry*	*Tram*	*Train*
State Transit Authority (NSW)	✓	✓ [a]	✗	✗
TransAdelaide[b]	✗ [c]	✗	✓	✓
Metro Tasmania	✓	✗	✗	✗
ACTION	✓	✗	✗	✗

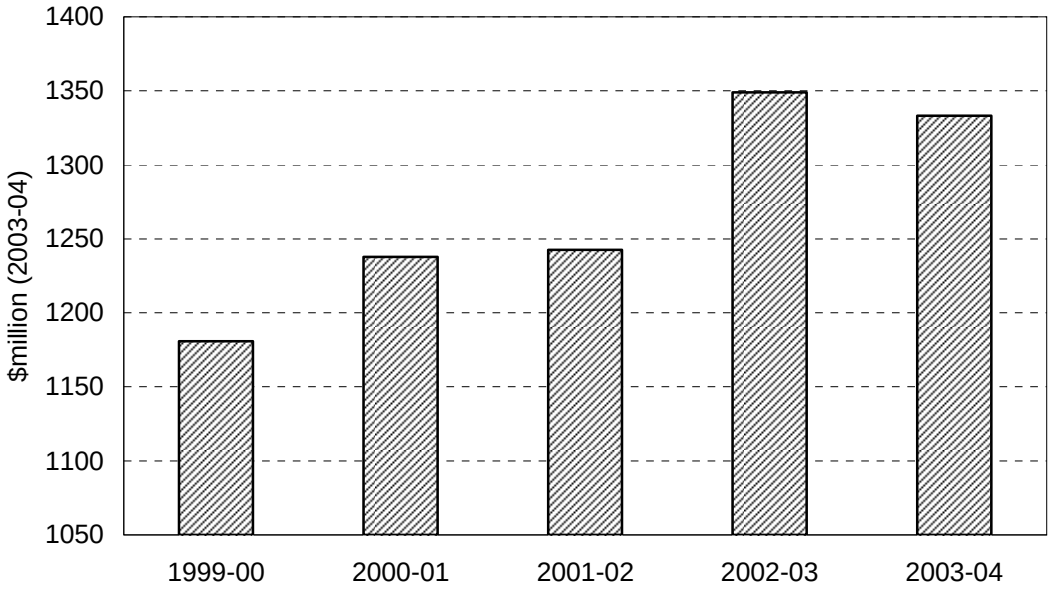
[a] The Sydney Ferries Corporation was established as a separate entity from State Transit from 1 July 2004. [b] In addition to its passenger transport activities, TransAdelaide is the infrastructure manager for the Adelaide metropolitan rail network. [c] TransAdelaide does not operate bus services in its own right. However, it has a joint-venture operation that provides bus services in the Adelaide hills.

Urban transport services are also provided by Queensland Rail, the Western Australian Government Railways Commission and the State Rail Authority (NSW), as a part of their broader rail operations. The performance of these GTEs is reported in chapter 8.

Over the reporting period, total assets of the four GTEs have grown by $154 million (13 per cent) in real terms (see figure 7.1). The increase is largely attributable to STA's significant revaluation ($137 million) of property, plant and equipment in 2002-03.

The 1 per cent reduction in total assets in 2003-04 was due to devaluations of property, plant and equipment by both TransAdelaide and STA.

Figure 7.1 **Sector assets — urban transport GTEs**

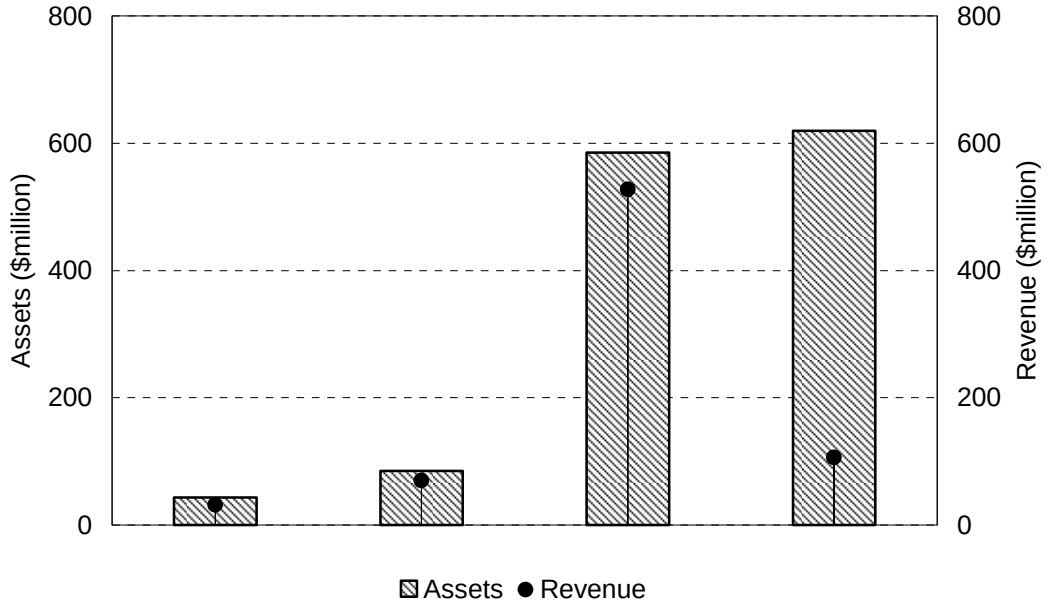


Note The value of sector assets prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation for Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

In 2003-04, TransAdelaide controlled 46 per cent of the aggregate assets of the monitored urban transport GTEs, while the STA accounted for a further 44 per cent. The four GTEs generated over $735 million of revenue in 2003-04, with the STA accounting for approximately 72 per cent of this total (see figure 7.2). The large size of TransAdelaide's asset base relative to its revenue reflects the high value of rail infrastructure assets *vis a vis* buses and ferries for the other urban transport GTEs.

Figure 7.2 **Assets and revenue — urban transport GTEs, 2003-04**



Source: Productivity Commission estimates.

7.2 Market environment

The patronage and financial performances of urban transport GTEs are significantly affected by the market environment in which they operate. Travel demand and revenue depend on a number of factors, including competition from private operators of urban transport, the cost of alternative methods of transport, including the costs involved with driving and parking privately-owned motor vehicles, as well as changes in fares and urban demographics.

In 2003-04, patronage increased for the sector as a whole (represented by the four monitored GTEs). TransAdelaide experienced the largest increase in patronage, recording a 5 per cent increase in total train boardings and a 3.8 per cent increase in tram patronage for the year. Patronage was largely unchanged in Sydney, although STA noted a continued turnaround in the previous decline, with a small amount of patronage growth in 2003-04. Metro Tasmania recorded a 1.4 per cent increase in patronage over the period. ACTION was the only monitored GTE to record a patronage decline (of less than 1 per cent).

Urban Transport services were provided almost exclusively by governments prior to the 1990s. The rationale for government intervention in the provision of urban transport services includes the benefits of service coordination and system-wide

ticketing, limited competition, the existence of positive externalities and providing access to the disadvantaged.

Microeconomic reform has been aimed at introducing institutional and regulatory changes in order to reduce the reliance of service providers on government funding by commercialising publicly-owned services and exposing service providers to market competition (PC 2005b). The principal areas of reform in urban transport have been governance, the supplier market and the setting of setting tariffs.

Governance reform

The relationships between urban transport GTEs and their owner-governments have been reformed to increase their commercial focus. The implementation of these reforms has varied across jurisdictions. However, there has been a general trend to separate urban transport policy, planning and regulatory functions from operational functions.

The only significant change in the governance structure of the STA since the passing of the *Transport Administration Act* in 1988 was the separation — under legislation passed by the NSW parliament in 2003 — of Sydney Ferries (now operating as the Sydney Ferries Corporation) from State Transit on 1 July 2004.

In South Australia, the former State Transport Authority was restructured in 1994-95. As a part of the restructure:

- TransAdelaide was corporatised and assumed the operating functions of the former State Transport Authority; and
- the planning and regulatory functions, including the responsibility for setting urban transport prices, were transferred to a new organisation — the Passenger Transport Board (PTB), a statutory authority within the Department for Transport, Urban Planning and the Arts.

In 1998, legislation was passed by Parliament to corporatise TransAdelaide, and the TransAdelaide board was appointed in 1999.

The *Passenger Transport (Dissolution of Passenger Transport Board) Amendment Act 2003*, dissolved the PTB effective from 1 January 2004. In conjunction with this Act, the Government established an Office of Public Transport within the Department of Transport and Urban Planning to assist the Minister in performing the functions previously carried out by the PTB.

In 1997-98, the Metropolitan Transport Trust of Tasmania became a government-owned company (Metro Tasmania) subject to Corporations Law.

On 1 January 2002, the status of ACTION changed from a division of the Department of Urban Services to a statutory authority.

Market reforms

Some aspects of the National Competition Policy (NCP) reforms have had an impact on administrative and operational arrangements in the urban transport sector. These include the application of competitive neutrality principles and the contracting out of some services.

Competitive tendering arrangements have been introduced to improve the commercial performance of GTEs. Urban transport GTEs have been required to compete with private sector providers for the right to operate certain urban passenger services in New South Wales, South Australia and Victoria.

For example, a tendering process introduced in South Australia in 1995-96 requires TransAdelaide to compete with the private sector on the basis of a set of costing rules designed to ensure competitive neutrality. On 22 April 2000, TransAdelaide ceased providing bus services after it was unsuccessful in tendering for service contracts with the PTB. It does, however, continue to participate in a joint-venture with Australian Transit Enterprises to operate bus services in the Adelaide hills.

Competitive tendering is also planned for the ACT. In January 2002, ACTION entered into an exclusive contract with the ACT Government for the provision of urban transport services. It is intended that on the expiration of this contract in December 2006, ACTION will be required to compete with the private sector to secure new service contracts.

STA expanded its bus services in Western Sydney after winning a tender to deliver high frequency services along the Liverpool-Parramatta Transitway. STA was awarded the contract in January 2002 ahead of competition from local and multinational companies, with services subsequently commencing operations in February 2003.

STA established a subsidiary corporation, Western Sydney Buses, to operate services on the Transitway. This was to ensure competitive neutrality and to enable an industrial agreement containing different conditions from those that apply in the enterprise agreements with State Transit.

Tariff reforms

Over the reporting period, the pricing of urban transport services was determined by independent pricing regulatory bodies in New South Wales and the Australian Capital Territory. In Tasmania, they are set by the Minister after considering reports by the Government Prices Oversight Commission (GPOC). In South Australia, prices were determined by the PTB until its abolition in December 2003. Public transport prices in South Australia are now determined by the Government.

Apart from ACTION, all monitored urban transport GTEs increased prices in 2003-04. The Australian Capital Tarritory's Independent Pricing and Regulatory Commission determined that ACTION's prices would not increase in the two years to 2005.

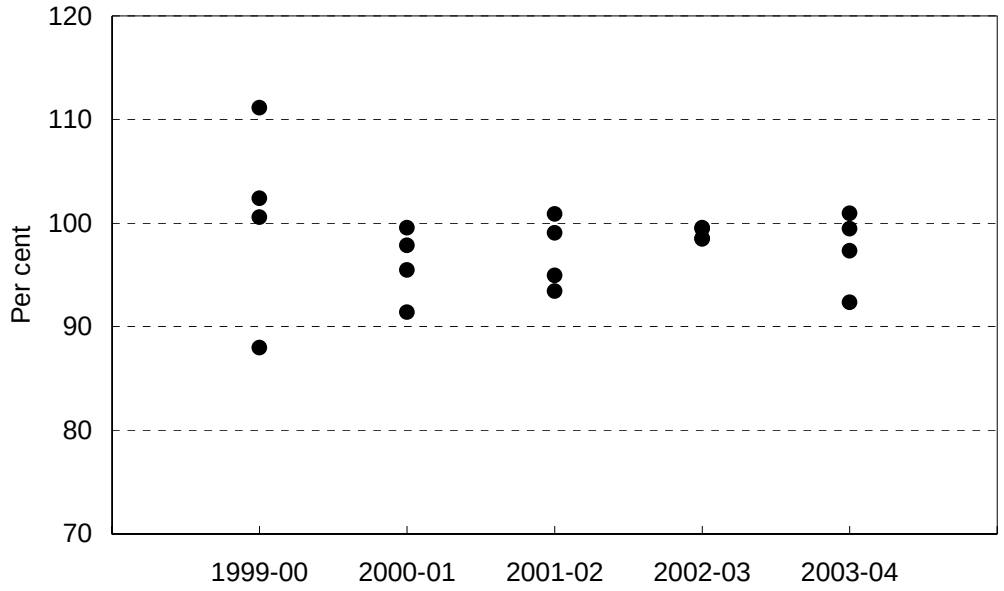
7.3 Profitability

In 2003-04, Metro Tasmania and TransAdelaide returned small positive, pre-tax operating profits after receiving community service obligation (CSO) payments, while both STA and ACTION, which also received significant CSO payments, returned losses of approximately $5 million.

The incidence over the reporting period of negative or small positive operating results is mainly due to expenses growing faster than revenues. Among other things, the increase in total expenses reflects higher labour and general maintenance costs and increased depreciation expenses.

The average level of cost recovery for urban transport GTEs overall has remained close to 100 per cent over the reporting period (see figure 7.3). The introduction of CSO payments to ACTION in 1996-97 and Metro Tasmania in 1997-98 — to reflect the value of concession and other non-commercial benefits of public transport — significantly improved their cost recovery performance. In 2003-04, cost recovery for ACTION and TransAdelaide worsened slightly, while STA's cost recovery improved.

Figure 7.3 **Cost recovery — urban transport GTEs**



Note Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting from total revenue, investment income and receipts from governments to cover operational deficits. Expenses from operations are calculated by subtracting gross interest expense from total expenses. Prior to 2000-01, abnormal items were also subtracted from operating expenses and revenue. A number of GTEs had virtually identical cost recovery ratios in 2002-03, which is why only two dots appear in figure 7.3 for 2002-03.

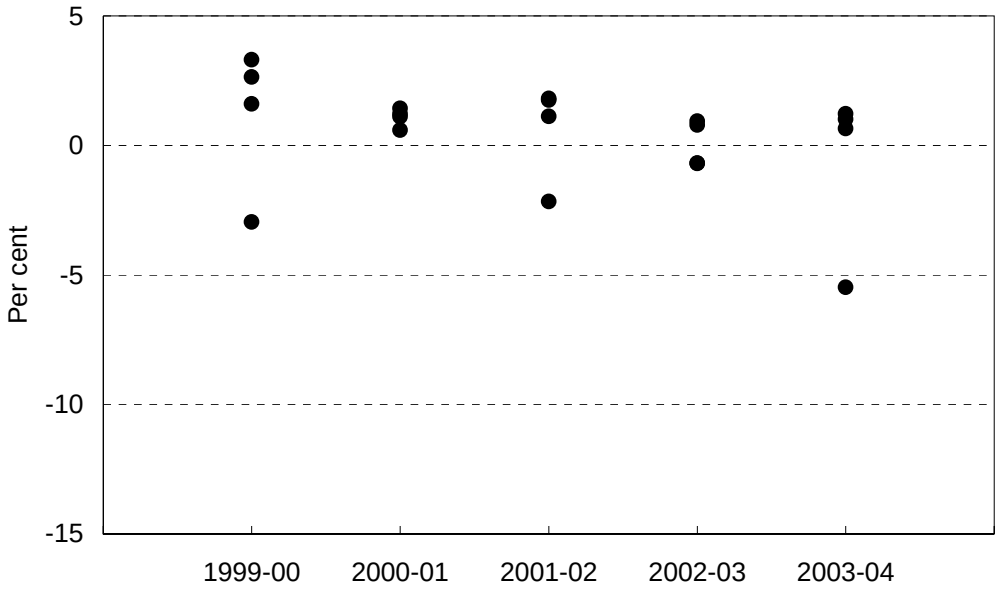
Source: Productivity Commission estimates.

Over the reporting period, the return on assets varied across urban transport GTEs (see figure 7.4), with significant convergence in recent years. The major factors affecting urban transport GTEs' returns on assets are changes in total revenues and total expenses. However, return on assets is also influenced by changes in asset values — through asset transfers, sale and lease-buy-back arrangements, asset revaluations, asset disposals and depreciation.

Overall, returns are well below those required by private operators, indicating that urban transport GTEs are not being required to operate on a commercially viable basis.[1]

1 Governments may not require a commercial rate of return from urban transport GTEs because urban transport provides external benefits that are not captured on the balance sheet — such as reductions in road user cost, environmental benefits and access for the young, elderly and poor. Alternatively, governments may feel that there is scope for further efficiency gains within the GTEs and set prices to reflect the efficient cost of service provision. In this case, low returns would be indicative of inefficient operations.

Figure 7.4 **Return on assets — urban transport GTEs**



Note Each data point represents the return on assets ratio for a GTE in that financial year. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue and adding back the gross interest expense. Average total assets is the average of the value of assets at the beginning and end of each financial year.

Source: Productivity Commission estimates.

Like return on assets, the return on equity achieved by urban transport GTEs has varied substantially over the reporting period. Metro Tasmania and TransAdelaide reported (small) positive returns to equity in 2003-04, while STA and ACTION reported negative returns to equity.

7.4 Financial management

Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

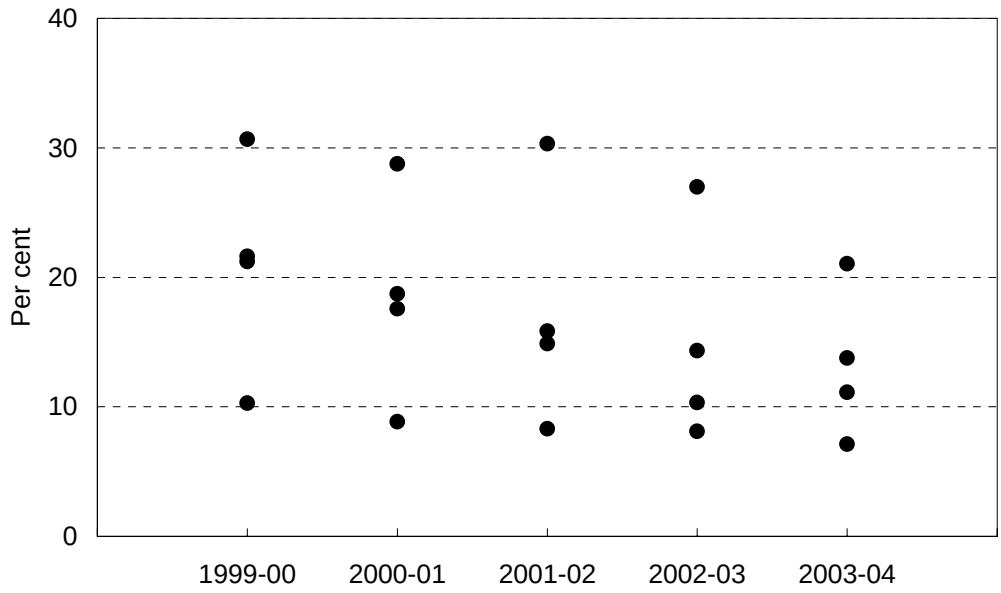
Most urban transport GTEs have restructured their capital over the reporting period and reduced debt levels. This restructuring includes debt for equity swaps, debt transfers to government and debt repayments.

Changes in the capital structure of the GTEs make it difficult to assess financial management performance over time. Asset revaluations also have an impact on inter-temporal performance comparisons.

Over the reporting period, the debt to total assets ratios have generally declined across the monitored GTEs (see figure 7.5). This may suggest a decrease in the proportion of total assets obtained through the use of borrowing. However, an improvement in this ratio can also result from debt restructuring and the transfer of liabilities to government departments. For example, despite an absolute increase in its level of debt, the upward revaluation of assets by STA in 2002-03 facilitated a 3 per cent decrease in its debt to total assets ratio.

The STA is the only urban transport GTE to have increased its level of debt over the reporting period (by 2 per cent since 1999-00). Borrowing for the purchase of new buses accounted for most of this increase. Over the reporting period, TransAdelaide, Metro Tasmania and ACTION decreased their level of debt by 33 per cent, 22 per cent and 45 per cent respectively.

Figure 7.5 **Debt to total assets — urban transport GTEs**



Note Each data point represents the debt to total assets ratio for a GTE in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Average total assets is the average of the value of assets at the beginning and end of each financial year.

Source: Productivity Commission estimates.

Sound financial management requires that profits are sufficient to ensure interest payments can be met. A high level of interest cover — the ratio of earnings before interest and tax expenses to gross interest expenses — indicates that the entity can sustain a fall in profit or increased interest expense and still meet the cost of servicing debt.

In 2003-04, the interest cover levels reported by the urban transport GTEs ranged from -4.2 times to 1.3 times. This was a lower level and larger range than the previous year, when each GTE reported an interest cover level of between -0.4 times and 1.4 times.

ACTION's interest cover was negative in 2003-04, indicating that it may have to fund interest expenses from sources other than current operating profits. The other urban transport GTEs are likely to be able to meet their interest commitments from operating profit. However, due to the small margins involved, cover may be significantly affected by increases in interest rates or falling revenues.

7.5 Transactions with government

As part of the reform process, governments have sought to facilitate competitive neutrality by giving GTEs a greater commercial focus and exposing them to factor market disciplines and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles, see chapter 3.

The monitored urban transport GTEs are required to make tax-equivalent and dividend payments, along with debt guarantee fee payments, to achieve competitive neutrality with private sector businesses.

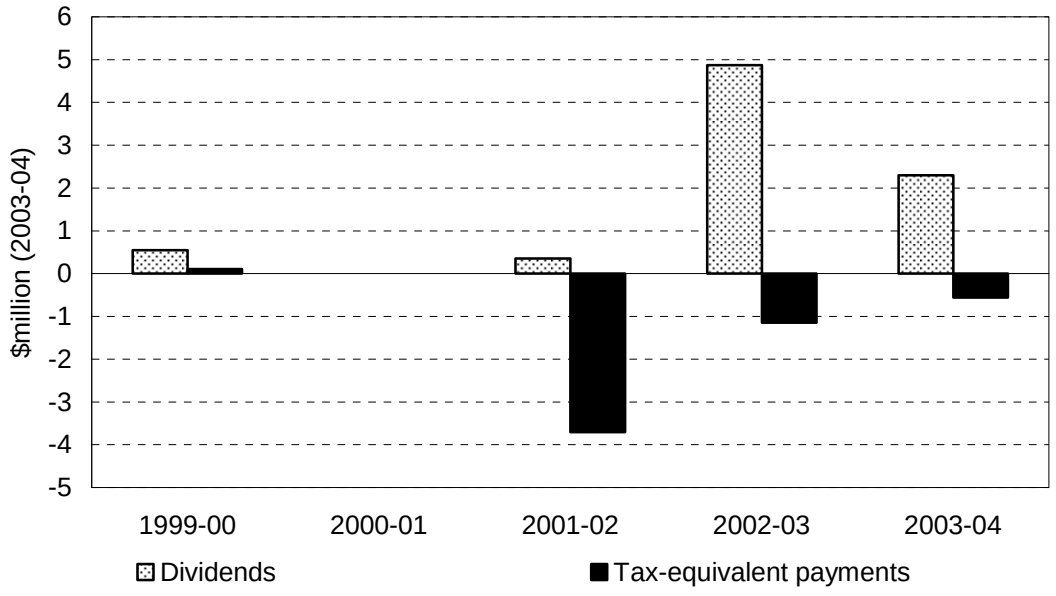
Income tax and dividend payments by the urban transport GTEs have been low in comparison to payments made by GTEs in other industry sectors and have varied considerably since 1999-00 (see figure 7.6). This reflects the small and volatile returns of urban transport GTEs over the reporting period.

TransAdelaide was the only urban transport GTE to make a tax-equivalent payment over the reporting period. Tax-equivalent payments were not required of the other urban transport GTEs because of negative operating results and accumulated tax losses.

Since 1999-00, Metro Tasmania has made two dividend payments and TransAdelaide has made one dividend payment, as well as two special dividend payments from retained earnings.

Traditionally, the social benefits associated with the provision of low cost urban transport services were recognised implicitly by governments and paid for by funding operating deficits in addition to the provision of CSO payments.

Figure 7.6 **Dividend and tax-equivalent payments — urban transport GTEs**



Note The value of dividends and tax-equivalent payments were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation for Public Corporations (see chapter 3). No dividends or tax-equivalent payments were made in 2000-01. The negative values for tax-equivalent payments in 2001-02, 2002-03 and 2003-04 represent recorded income tax benefits for those years.

Source: Productivity Commission estimates.

Governments have entered into CSO contracts with their respective urban transport GTEs. CSO contracts across urban transport GTEs include:

- *Pricing* — to reimburse GTEs for offering fares at below a commercial level. The government pays the difference between the full fare applicable for the journey and the fare paid by the traveller.
- *Service* — to reimburse GTEs for providing non-commercial services such as late night services when patronage is low.
- *Concessions* — to reimburse GTEs for offering government determined concessions. This includes the provision of free and concession travel for school students, tertiary students, pensioners and senior citizens, people with disabilities and welfare recipients.

The STA, Metro Tasmania and ACTION receive CSO payments, although Metro Tasmania does not reveal the value of this funding in its accounts. TransAdelaide also receives government payments, but these payments are included as part of the figure for total income and are not separately identified in its accounts.

For most urban transport GTEs, CSOs account for a relatively large share of total revenue. In 2003-04, CSO funding accounted for 71 per cent of ACTION's total revenue and 46 per cent of revenue for the STA.

URBAN TRANSPORT

Table 7.2 **Whole sector performance indicators, 1999-00 to 2003-04**

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	1 150	1 228	1 244	1 350	1 333
Total revenue	$m	748	680	691	723	735
Profitability						
Operating profit before tax	$'000	969	- 7 297	- 19 504	- 16 878	- 8 603
Operating sales margin	%	2.6	1.8	- 0.3	- 0.3	1.0
Cost recovery	%	101.7	96.8	94.7	98.7	99.5
Return on assets	%	1.9	1.3	0.0	0.2	0.7
Return on equity	%	0.1	- 1.1	- 2.2	- 2.1	- 1.0
Financial management						
Debt to equity	%	43.3	35.8	37.2	30.8	27.9
Debt to total assets	%	24.3	21.5	20.9	19.1	16.6
Total liabilities to equity	%	82.7	72.0	79.6	67.8	66.5
Interest cover	times	1.0	0.7	0.0	0.1	0.5
Current ratio	%	64.0	59.5	46.7	38.6	42.2
Leverage ratio	%	182.7	172.0	179.6	167.8	166.5
Payments to and from government						
Dividends	$'000	533	0	353	4878	2296
Dividend to equity ratio	%	0.1	0.0	0.1	0.7	0.3
Dividend payout ratio	%	61.9	0.0	- 2.2	- 31.0	- 28.5
Income tax expense	$'000	107	0	- 3711	- 1152	- 558
CSO funding	$'000	220 928	236 406	255 398	288 473	291 493

7.6 GTE performance reports

State Transit Authority (NSW)

TransAdelaide (SA)

Metro Tasmania (Tasmania)

ACTION Authority (ACT)

STATE TRANSIT AUTHORITY — New South Wales

The State Transit Authority (STA) is incorporated under the *Transport Administration Act 1988*. In 2003-04, it operated four metropolitan passenger transport businesses — Sydney Buses; Sydney Ferries[1]; Newcastle Bus and Ferry Services and Western Sydney Buses. The STA operates within the regulatory framework of the *Passenger Transport Act 1990*.

Capital expenditure in 2003-04 was $29 million compared with $48 million in 2002-03. The capital works program in 2003-04 comprised $22 million on the bus replacement program and $7 million on the renewal or replacement of assets required for bus servicing, ferry maintenance, depot facilities and computing resources. The value of total assets decreased by $14 million in 2003-04.

Prices for STA's services are set by the Independent Pricing and Regulatory Tribunal of NSW. In accordance with the *Public Transport Fares Determination*, single tickets on Sydney buses rose by approximately 1 per cent and bus fares in Newcastle increased by a weighted average of approximately 3 per cent in 2003-04.

In 2003-04 total revenue increased by 2 per cent to $527 million. This growth was largely attributable to a 4 per cent increase in passenger revenue. Patronage on State Transit's services grew slightly during the year, reversing the declining trend of recent years.

Costs are recovered by a combination of fare box revenue and fares paid by government as part of its social policy programs. Of the $241 million CSO funding in 2003-04, $155 million was payment of fares by government for pensioners, school children and other eligible groups. The remaining $86 million was for two general reimbursements: the pricing CSO, to cover the gap between State Transit's fares and those generally prevailing in the private bus sector; and the Service CSO, which is a payment to cover losses on non-commercial services.

However, the 2 per cent increase in revenue combined with a small decrease in expenses resulted in a $9 million reduction in the net operating loss for 2003-04 to $5 million. The underlying result, excluding Sydney Ferries, was a surplus of $12 million.

1 In accordance with legislation, passed by the NSW Parliament in 2003, Sydney Ferries was separated from State Transit on 1 July 2004 and now operates as the Sydney Ferries Corporation.

STATE TRANSIT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*[c]	*2003-04*[b]
Size						
Total assets	$m	434	439	467	599	585
Total revenue	$m	424	479	490	519	527
Profitability						
Operating profit before tax	$'000	699	- 4 313	- 19 580	- 13 968	- 4 556
Operating sales margin	%	1.3	0.9	- 2.0	- 0.8	1.0
Cost recovery	%	100.6	97.9	93.4	98.5	100.9
Return on assets	%	1.6	1.2	- 2.2	- 0.7	1.0
Return on equity	%	0.5	- 3.0	- 15.0	7.7	- 1.9
Financial management						
Debt to equity	%	85.5	89.9	112.4	59.2	51.6
Debt to total assets	%	30.7	28.8	30.3	27.0	21.1
Total liabilities to equity	%	201.5	214.5	282.3	146.5	142.6
Interest cover	times	1.1	0.6	- 1.0	- 0.4	0.6
Current ratio	%	42.8	44.9	30.5	20.9	24.4
Leverage ratio	%	301.5	314.5	382.3	246.5	242.6
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0.0	0.0	0.0	0.0	0.0
Dividend payout ratio	%	0.0	0.0	0.0	0.0	0.0
Income tax expense	$'000	0	0	0	0	0
CSO funding	$'000	178 297	193 675	208 860	239 430	241395

a The increase in the value of assets is due to $56 million in capital expenditure for bus replacement and a $27 million upward revaluation of non-current assets. In 1999-00, the STA reported an abnormal gain of over $3 million from the profit on property sales, which contributed to the reported pre-tax operating profit. **b** Return on assets was positive, despite the STA recording a negative operating result. Return on assets is the ratio of Earnings Before Interest and Tax (EBIT) to total assets. The discrepancy between pre-tax operating profit and return on assets reflects an increase in borrowing costs (which are excluded from EBIT) as a percentage of total costs. **c** The increase in the value of assets is largely attributable to a $137 million asset revaluation increment.

TRANSADELAIDE — South Australia

TransAdelaide provides passenger rail services to the Adelaide metropolitan area under contract to the Office of Public Transport (OPT)[1] and is responsible for the management of train and tram infrastructure. TransAdelaide also has a 50 per cent interest in TransitPlus Pty Ltd, a joint-venture to provide bus services in the Adelaide hills.[2] Under the *TransAdelaide (Corporate Structure) Act 1998*, TransAdelaide is subject to the provisions of the *Public Corporations Act 1993*.

TransAdelaide obtains the majority of its revenue from the OPT and receives funding from the SA Government. In 2003-04, ticket revenue was remitted to the OPT, which set fares for metropolitan public transport. The OPT then paid TransAdelaide in accordance with its passenger rail service contract. TransAdelaide recorded revenue from the OPT as 'sales of goods and services' in their financial statements. TransAdelaide is required to make tax-equivalent and dividend payments.

TransAdelaide's patronage grew for the fifth year in a row. A five per cent increase in total train boardings and a 3.8 per cent increase in tram patronage was recorded for the year. TransAdelaide made a profit of $1.2 million in 2003-04. After prior year adjustments and the inclusion of grant funding, TransAdelaide recorded an income tax benefit of $558 000 for 2003-04.

Operating profit did not meet budgeted levels due to the impact of the cost of a diesel fuel spill. The spill occurred at TransAdelaide's Railcar Depot in July 2003, resulting in 15 000 litres of fuel entering the River Torrens.

There was no declared dividend paid to the Department of Treasury and Finance during 2003-04. However, a special dividend of $2.3 million was paid from retained earnings.

Government funding for CSOs is not separately identified in TransAdelaide's financial statements.

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1 TransAdelaide is required to compete with the private sector to secure OPT service contracts. On 23 April 2000, TransAdelaide ceased the provision of bus services in its own right after unsuccessful bids to the OPT. In December 2000, TransAdelaide secured the contract for the provision of rail transport services until 2005. In 2003-04, the contract for provision of passenger rail services was renewed to April 2010 after it met the renewal performance benchmarks of the contract.

2 In April 2000, the joint-venture operation was awarded a five year contract to provide passenger transport to the Algate and Mount Barker area. Previously, this service was provided by a former TransAdelaide subsidiary, Hills Transit, which was dissolved by regulation on 30 June 2000.

TRANSADELAIDE (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*	*2003-04*
Size						
Total assets	$m	609	685	670	642	620
Total revenue	$m	227	107	104	104	106
Profitability						
Operating profit before tax	$'000	3 848	- 1 755	6	- 1 225	1 235
Operating sales margin	%	6.6	7.2	6.2	2.7	6.5
Cost recovery	%	111.1	91.4	99.0	99.6	97.3
Return on assets	%	2.6	1.4	1.1	0.9	1.2
Return on equity	%	0.9	- 0.4	0.7	0.0	0.4
Financial management						
Debt to equity	%	30.4	22.0	21.1	19.0	18.0
Debt to total assets	%	21.2	17.6	15.8	14.3	13.8
Total liabilities to equity	%	42.4	32.6	31.9	29.5	28.8
Interest cover	times	1.3	0.8	1.0	0.8	1.2
Current ratio	%	127.6	89.5	76.1	61.0	76.4
Leverage ratio	%	142.4	132.6	131.9	129.5	128.8
Payments to and from government						
Dividends [d]	$'000	0	0	353	4 592	2 296
Dividend to equity ratio	%	0.0	0.0	0.1	0.9	0.5
Dividend payout ratio	%	0.0	0.0	9.5	- 193.2	128.1
Income tax expense	$'000	107	0	-3 711	- 1 152	-558
CSO funding[e]	$'000	0	0	0	0	0

a Includes abnormal revenue relating to the withdrawal of bus services ($11 million) and abnormal expenses relating to a loss on disposal of assets ($7.8 million), expenses associated with the withdrawal of bus services ($3.1 million), fleet and depot restoration costs ($5.9 million), Hills Transit termination payments ($0.6 million) and the write-off of tax losses associated with the bus business ($7.6 million). Includes an upward revaluation of land, buildings and rollingstock of $6.7 million. **b** An independent revaluation increased the value of TransAdelaide's assets by almost $90 million. The reduced total revenue reflects the first full year of operations after losing the Office of Public Transport bus service contract. **c** The financial data for the years 1999-00 to 2001-02 are predominantly based on Government Finance Statistics (GFS) data — in contrast with the General Purpose Financial Report (GPFR) data on which the Annual Report is based. The concepts underlying GFS and GPFR may lead to different reported statistics (see chapter 3). The small profit shown for 2001-02 is based on GFS data and did not take into account the loss on sale of assets, which resulted in a $12 million loss in 2001-02 based on the GPFR framework. This loss on sale of assets in 2001-02 was primarily due to the transfer of TransAdelaide's interest in the Belair rail line to the Australian Railways Track Corporation for nil consideration, pursuant to an agreement reached in 1999 between State and Federal ministers. **d** A special dividend was paid as directed by the Treasurer from retained earnings for depreciation funding in 2001-02, 2002-03 and 2003-04. **e** Community service obligation funding is not separately identified in TransAdelaide's accounts.

METRO TASMANIA Tasmania

Metro Tasmania Pty Ltd (Metro) was incorporated on 2 February 1998, under the *Metro Tasmania Act 1997*. Upon incorporation, the assets and liabilities of the Metropolitan Transport Trust were transferred to Metro, which provides passenger bus services to Hobart, Launceston and Burnie. In May 1999, Metro formed a subsidiary company, Metro Coaches (Tas) Pty Ltd to operate bus services from Hobart to Blackman's Bay, the Channel, Campania and New Norfolk.

The maximum prices that Metro can charge are determined by the Government after considering reports by the Government Prices Oversight Commission (GPOC). Metro's fares for adult and tertiary student passengers were increased by approximately 7 per cent in January 2004. Fares for children and other student passengers remained the same.

In 2003-04, patronage and total revenues increased compared with the previous year. However, due to increased expenses, Metro returned a profit of $63 000, which was $13 000 lower than the preceding year. Return on assets and return on equity both declined slightly.

The increase in expenses in 2003-04 were partially caused by an increase in superannuation provisions resulting from changes in actuarial assumptions. In addition, ownership costs, particularly bus depreciation, increased with Metro's bus replacement program because of the accelerated depreciation of buses in the first few years of their effective life.

The *Metro Tasmania Act 1997* and the *Government Business Enterprises Act 1995* require Metro to make income tax-equivalent payments to the Tasmanian Government. However, due to accumulated tax losses, Metro has not made tax-equivalent payments during the reporting period. No dividend was announced in 2003-04.

Metro has a Community Service Agreement with the Tasmanian Government. The funding provided under the agreement is designed to enable Metro to achieve a break-even operating result. It includes provision for concession travel for specified categories of passengers and for the provision of non-commercial services. However, CSO funding is not separately identified in Metro's accounts.

METRO TASMANIA (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*[b]	*2002-03*	*2003-04*
Size						
Total assets	$m	35	36	37	37	43
Total revenue	$m	30	29	30	30	32
Profitability						
Operating profit before tax	$'000	763	- 53	413	80	63
Operating sales margin	%	2.9	- 0.4	0.9	- 0.6	- 0.6
Cost recovery	%	102.4	99.6	100.9	99.5	99.4
Return on assets	%	3.3	0.6	1.8	0.8	0.7
Return on equity	%	4.8	- 0.3	2.4	0.5	0.3
Financial management						
Debt to equity	%	23.2	18.2	17.7	17.9	13.3
Debt to total assets	%	10.3	8.8	8.3	8.1	7.1
Total liabilities to equity	%	118.3	108.5	118.0	119.6	100.9
Interest cover	times	2.8	0.8	2.8	1.4	1.3
Current ratio	%	71.7	109.5	118.0	159.7	102.1
Leverage ratio	%	218.3	208.5	218.0	219.6	200.9
Payments to and from government						
Dividends[c]	$'000	533	0	0	286	0
Dividend to equity ratio	%	3.4	0.0	0	1.7	0.0
Dividend payout ratio	%	69.9	0.0	0	357.5	0.0
Income tax expense	$'000	0	0	0	0	0
CSO funding[d]	$'000	0	0	0	0	0

a Includes abnormal revenue of $0.6 million relating to a reduction in superannuation provisions. Metro also reported abnormal expenses relating to workers' compensation ($250 000), a wholesale sales tax adjustment ($90 000) and costs incurred during a price regulation investigation by the GPOC ($130 000). **b** Includes a one-off receipt of $336 000 from the Tasmanian Government for prior year increases in superannuation provisions. **c** A change in accounting policy adopted by Metro from 1 July 2002 means that dividends will now be recognised in the financial statements for the year in which they are announced. As explained in chapter 3, this change affects certain year to year comparisons. **d** Metro receives CSO payments under its Community Service Agreement with the Tasmanian Government. The level of CSO funding under this contract is not reported separately.

ACTION AUTHORITY — Australian Capital Territory

The Australian Capital Territory Internal Omnibus Network Authority (ACTION) provides urban and school bus services to the Canberra metropolitan area.[1] ACTION operates pursuant to the *Road Transport (Public Passenger Services) Act 2001*, which came into force on 1 December 2001.

On 1 January 2002, the *ACTION Authority Act 2001* came into effect, changing the status of ACTION from a division of the ACT Government's Department of Urban Services, to a statutory authority.

Prices for ACTION's services are set by the ACT's Independent Pricing and Regulatory Commission, which determined that there should be no fare increases for the two years ending in 2005. Such regulatory decisions have implications for patronage and the level of financial support provided to ACTION by the ACT government.

In 2003-04, ACTION reported a slight reduction in total passenger numbers compared with the previous year. Despite this reduction in fares revenue, total revenue was approximately 2 per cent higher than in 2002-03. This was due mainly to additional Australian Government grants, a net increase in charter revenue and additional revenue from interest. Total expenses for 2003-04 were also higher than the previous year, by approximately 6 per cent. The operating result for the 2003-04 financial year was a deficit of $5.3 million, which is larger than the deficit in 2002-03 of $1.8 million.

ACTION receives CSO payments for offering fares below a commercial level as well as providing general route off-peak services, concession travel for students, school services and special needs transport. In 2003-04, CSO funding comprised 71 per cent of ACTION's total revenue, with most of the remainder coming from fare revenue.

ACTION's operating result is budgeted to be in deficit. In general, recurrent expenditure is met from annual revenue, with the exception of depreciation. ACTION receives capital grants to fund its capital expenditure on plant and equipment.

ACTION did not make tax-equivalent or dividend payments over the reporting period.

1 The ACTION Authority has a five year contract with the Department of Urban Services for the exclusive provision of public transport in the Australian Capital Territory. The contract expires on 31 December 2006.

ACTION AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	72	68	70	73	85
Total revenue	$m	67	65	67	69	70
Profitability						
Operating profit before tax	$'000	- 4 342	- 1 176	- 343	- 1 764	- 5 345
Operating sales margin	%	- 3.3	1.1	1.6	- 1.3	- 6.9
Cost recovery	%	88.0	95.5	94.9	98.7	92.4
Return on assets	%	- 3.0	1.1	1.8	- 0.7	- 5.5
Return on equity	%	- 10.2	- 2.9	- 0.8	- 3.7	- 10.1
Financial management						
Debt to equity	%	38.3	32.4	22.6	15.0	15.4
Debt to total assets	%	21.6	18.7	14.9	10.3	11.1
Total liabilities to equity	%	72.5	68.5	53.4	48.0	49.5
Interest cover	times	- 1.0	0.4	0.8	- 0.4	- 4.2
Current ratio	%	46.2	60.3	123.9	134.1	120.5
Leverage ratio	%	172.5	168.5	153.4	148.0	149.5
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0.0	0.0	0.0	0.0	0.0
Dividend payout ratio	%	0.0	0.0	0.0	0.0	0.0
Income tax expense	$'000	0	0	0	0	0
CSO funding	$'000	42 631	42 731	46 538	53 240	50 098

[a] Includes an abnormal gain of $1.1 million relating to participation in a Commonwealth Government program. An abnormal expense of $0.3 million was incurred relating to a loss from the sale of obsolete stores.

8 Railways

The financial performances of five rail government trading enterprises (GTEs) are covered in this chapter. In 2003-04, they controlled $25.4 billion in assets and generated around $2.7 billion in revenue.

Financial performance summaries, including performance indicators for the rail sector and each rail GTE are presented. The performance indicators are consistent across individual GTEs. However when making comparisons, consideration should be given to differences in the nature and scale of the businesses, their market environments and issues relating to the valuation of their assets.

For a discussion of the data, the financial indicators and some of the factors that should be considered when assessing performance, see chapter 3.

8.1 Monitored GTEs

The activities of the five monitored rail GTEs are shown in table 8.1. Queensland Rail (QR) is vertically integrated, providing all the activities involved in managing a rail network and operating rail freight and passenger services. The other four have fewer activities. Rail Corporation New South Wales (RailCorp) and the Public Transport Authority (PTA) of Western Australia operate urban and regional rail passenger transport services and are responsible for managing rail infrastructure. Rail Infrastructure Corporation (RIC) of New South Wales and Australian Rail Track Corporation (ARTC) provide track management services, including the administration of rail access regimes.

Table 8.1 **Activities — rail GTEs, 2003-04**

Rail GTE	*Jurisdiction*	*Activities*			
		Track[a]	*Freight transport*	*Urban passenger transport*	*Regional passenger transport*
Rail Infrastructure Corporation	NSW	✓	✗	✗	✗
Rail Corporation	NSW	✓	✗	✓	✓
Queensland Rail	Queensland	✓	✓	✓	✓
Public Transport Authority[b]	WA	✓	✗	✓	✓
Australian Rail Track Corporation	Australian Government	✓	✗	✗	✗

[a] Refers to the ownership of mainline tracks and does not include ownership of sidings, terminals and other 'below track' infrastructure. [b] The PTA also operates metropolitan, regional and school bus services, as well as ferry services.

Victoria's rail services are not included as they are undertaken by the private sector. TransAdelaide — South Australia's rail GTE — is included in chapter 9 because it provides urban passenger services only.

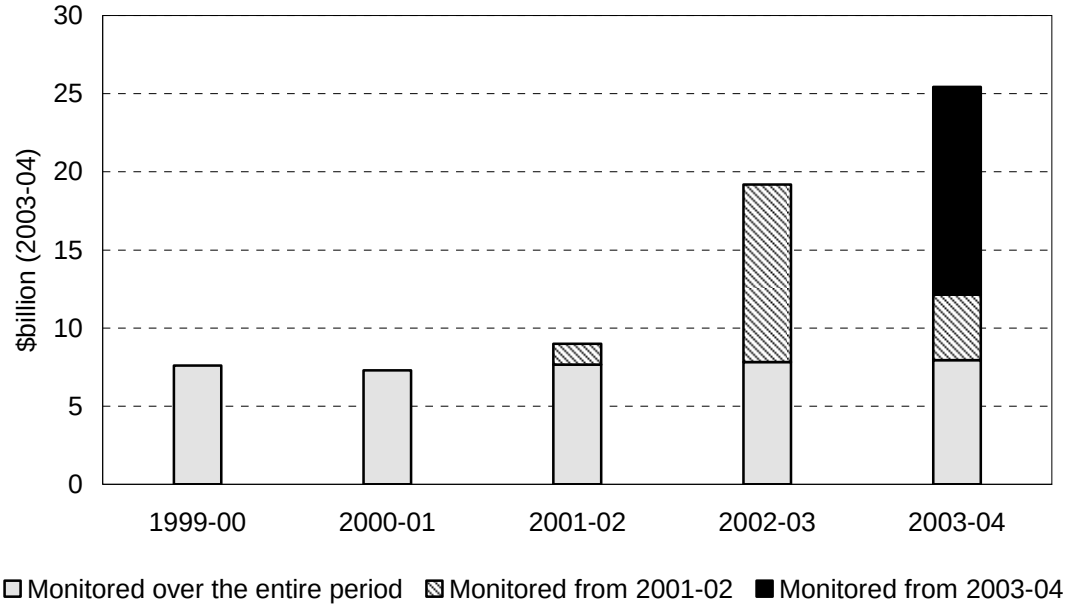
The financial performances of some rail GTEs have been affected by the transfer of some of their activities to another GTE or to the private sector. For example, in 2003-04, the metropolitan functions of RIC were transferred to RailCorp as part of a structural change to the New South Wales rail system.

The set of monitored GTEs included in the rail sector has changed over the reporting period. QR has been reported over the entire reporting period, RIC and ARTC have been reported since 2001-02, and the PTA and RailCorp are included for the first time for 2003-04. The PTA and RailCorp replaced the Western Australian Government Railway Commission (WAGRC) and State Rail Authority of New South Wales (StateRail) respectively, which were both previously monitored in this report. The financial performance of StateRail is reported separately at the end of this chapter, though its performance in 2003-04 is not comparable to previous years.

Two other rail GTEs monitored in previous reports — the National Rail Corporation and the New South Wales Freight Rail Corporation — have not been monitored since their privatisation in January 2002. Their financial performances over the period 1996-97 to 2000-01 were covered in an earlier edition (PC 2002a).

The assets controlled by the GTEs monitored in 2003-04 are shown in figure 8.1. However, the asset base of GTEs is highly dependent on the accounting policies used for their valuation.

Figure 8.1 **Sector assets — rail GTEs**



Note QR has been monitored over the entire reporting period, RIC and ARTC have been reported since 2001-02, and the PTA and RailCorp are included for the first time for 2003-04. A change in accounting policy led to a $10 billion revaluation increment to RIC's assets in 2002-03. The value of sector assets prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

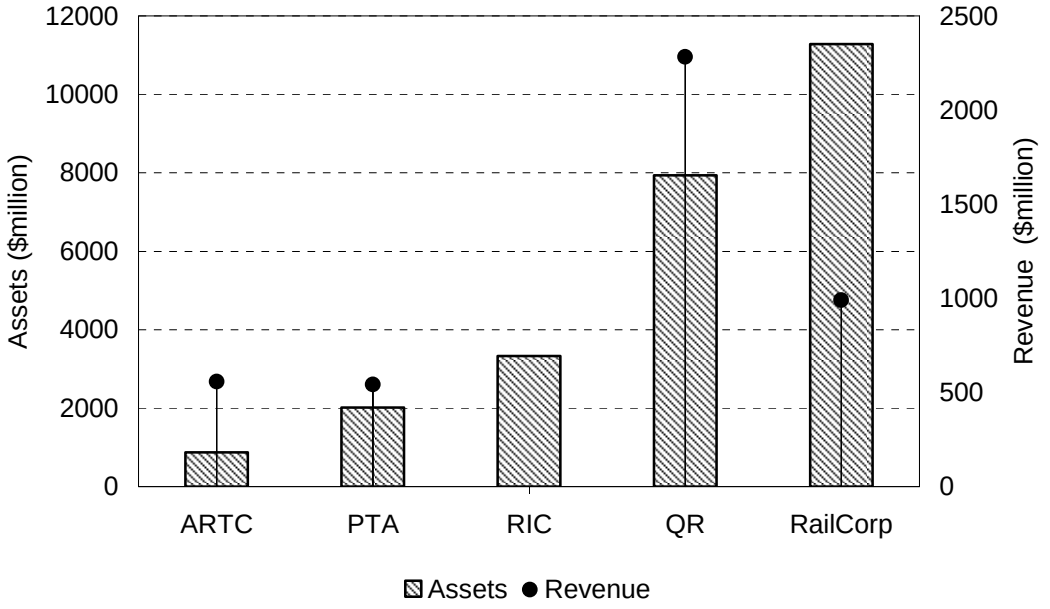
Source: Productivity Commission estimates.

A change in policy, from fair value to depreciated optimised replacement cost valuation, led to a revaluation of RIC's community service infrastructure assets in 2002-03. This increased the value of its assets by over $10 billion — or over 900 per cent — and was the major contributing factor to an increase in total rail GTE assets to over $19 billion in 2002-03.

In 2003-04, with the inclusion of RailCorp ($11 billion of assets) and the PTA ($2 billion of assets), total rail GTE assets increased to over $25 billion, despite RIC's decrease in assets ($8 billion) due to restructuring, with its metropolitan functions transferred to RailCorp.

The relative size of each GTE monitored for 2003-04 in terms of their asset values and revenue is shown in figure 8.2.

Figure 8.2 **Assets and revenue — rail GTEs, 2003-04**



Note RIC recorded negative revenue of $1.7 billion in 2003-04, with a write down of assets leased to ARTC of $3 billion.

Source: Productivity Commission estimates.

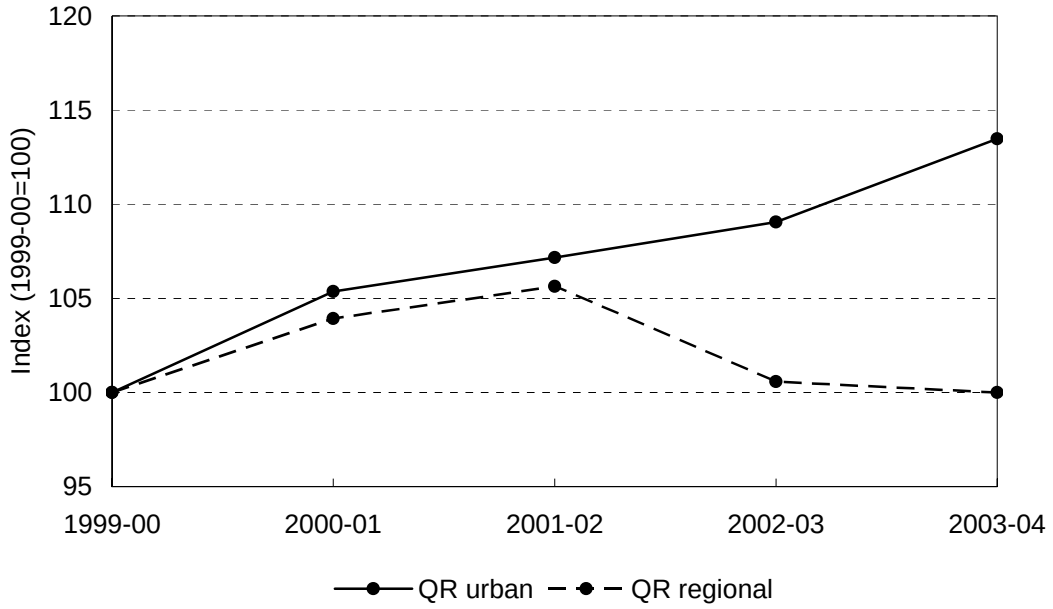
8.2 Market environment

Rail transport has been partly displaced in many of its traditional markets by road transport, causing rail's share of the transport market to decline over the last 30 years (ABS 2004b). However, rail has maintained a dominant role in the transport of bulk commodities, such as coal, grain and iron ore, for which it is well suited.

The demand for rail transport is dependent on intermodal competition, as well as demand and supply conditions in the relevant commodity markets. For example, QR has increased revenue in each year over the reporting period as the volume of coal transported increased.

Rail GTEs providing passenger transport services, such as QR, have typically faced differing trends in the demand for urban and regional passenger services (see figure 8.3).

Figure 8.3 **Passenger trends — Queensland Rail**



Note QR urban refers to passenger trips on Queensland Rail's Citytrain services. QR regional refers to passenger trips on Traveltrain services.

Source: QR (2004).

Government railways are regulated. Charges for RailCorp's CityRail services are determined by the Independent Pricing and Regulatory Tribunal (IPART) of New South Wales. Charges for CountryLink services are determined by the Minister for Transport after a recommendation from RailCorp's Board. Charges for QR and the PTA passenger services are determined by their respective boards, but are subject to the approval of the relevant Minister.

Rail access charges are typically set by negotiation between the track owners and rail operators or under the relevant access regime. Disputes may be settled by arbitration.[1]

1 In New South Wales, IPART may arbitrate access disputes. Access to the ARTC's network may be arbitrated by a nominated party or by the Australian Competition and Consumer Commission. In Queensland, a nominated party may act as arbitrator or, if no agreement can be reached between the track owners and rail operators, the Queensland Competition Authority is the default arbitrator.

Structural reforms

Reforms within the rail sector have been aimed at improving performance by subjecting operators to stronger financial disciplines and competitive pressures. Changes included the vertical and horizontal separation of rail GTEs and the introduction of rail access regimes to promote increased competition in operations.

Access regimes seek to encourage competition in the market for rail infrastructure by stipulating the methods by which a third party may gain access to rail track. They are covered by Part IIIA of the *Trade Practices Act 1974*, which provides three ways for a firm to gain access — by using an existing, state-based access regime; by seeking access under the terms and conditions specified in an undertaking given by the service provider; or, by having a service declared under the provisions of the National Access Regime.

Applications for declaration are made to the National Competition Council (NCC) and initiate a process of negotiation and, if required, compulsory arbitration in order to settle disputes between operators and track managers. However, if the state-based access regime has been certified by the NCC, or if a private undertaking has been accepted by the Australian Competition and Consumer Commission (ACCC), access seekers are unable to use the declaration process.

RIC is responsible for managing New South Wales rail infrastructure and for providing rail operators with access to the network.[2] The access regime was established by the NSW Government in 1996 and was certified in November 1999 under the *Trade Practices Act 1974* by the Australian Government Minister for Financial Services and Regulation. However, the access regime is no longer certified.[3]

ARTC manages parts of the interstate rail network, mainly in New South Wales, Victoria, South Australia and Western Australia.[4] ARTC has a registered undertaking with the ACCC with respect to the terms and conditions by which it provides access to the network.

2 RIC was established on 1 January 2001 by a merger between the Rail Access Corporation and Rail Services Australia.

3 The certification, issued 15 November 1999, remained valid until 31 December 2000, pending finalisation of the national access arrangements for rail. Certification by the relevant Australian Government Minister is not essential for rail access regimes to operate effectively, but without certification the declaration process remains open.

4 The Australian Government and NSW Governments agreed on 5 December 2003 to lease the New South Wales interstate and Hunter Valley networks to ARTC for 60 years, commencing September 2004.

In Queensland, the Network Access Unit — a division of QR — has been responsible for negotiating access with third-party operators and the development of network access provisions. QR has put in place accounting arrangements to separately identify network infrastructure and operating costs. These arrangements are designed to treat third-party operators and internal business groups equally for the purposes of access pricing. Queensland's draft access undertaking was approved by the Queensland Competition Authority (QCA) in December 2001.[5] However, the regime has not yet been certified under the *Trade Practices Act 1974*.

In Western Australia, the Office of the Independent Rail Access Regulator was established during 2000 to oversee the implementation of a rail access regime under the *Railways (Access) Act 1998*. The regime covers track controlled by the PTA and WestNet Rail, a subsidiary of the Australian Railroad Group (ARG).[6] Like the New South Wales and Queensland access regimes, the Western Australia regime is not certified.[7]

A feature of structural reform in some jurisdictions has been the separation and sale to the private sector of rail freight operations. In New South Wales, the freight operations of StateRail were transferred to the Freight Rail Corporation in 1996-97. The Freight Rail Corporation was sold to the private sector, together with the government-owned National Rail Corporation in January 2002.[8]

Structural reforms that change the scope of a GTE's activities complicate the assessment of performance over time. Changes to the asset base, liability structure and revenue stream, together with any redundancy payments that accompany such reforms, affect the financial ratios presented in the individual GTE performance reports. Over the reporting period, financial reforms included capital restructuring, the revaluation of assets, the identification and direct funding of CSOs, and the development of dividend policies.

For example, RIC's revaluation of property, plant and equipment assets in 2002-03 increased the asset base by over 900 per cent and directly caused expenses to rise by around 45 per cent due to increased depreciation.

5 In April 2004, QR submitted a draft access undertaking in response to an initial undertaking notice issued by the QCA in November 2003.

6 The sale of the WAGRC's freight business on 18 December 2000 incorporated a 49 year lease of track infrastructure to the privately-owned ARG.

7 The only regime certified under the *Trade Practices Act 1974*, as of May 2004, was the AustralAsia Railway (Third Party Access) Code, which applies to the Tarcoola–Darwin corridor.

8 The Australian Government, NSW and Victorian Governments were co-owners of NRC.

8.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings.

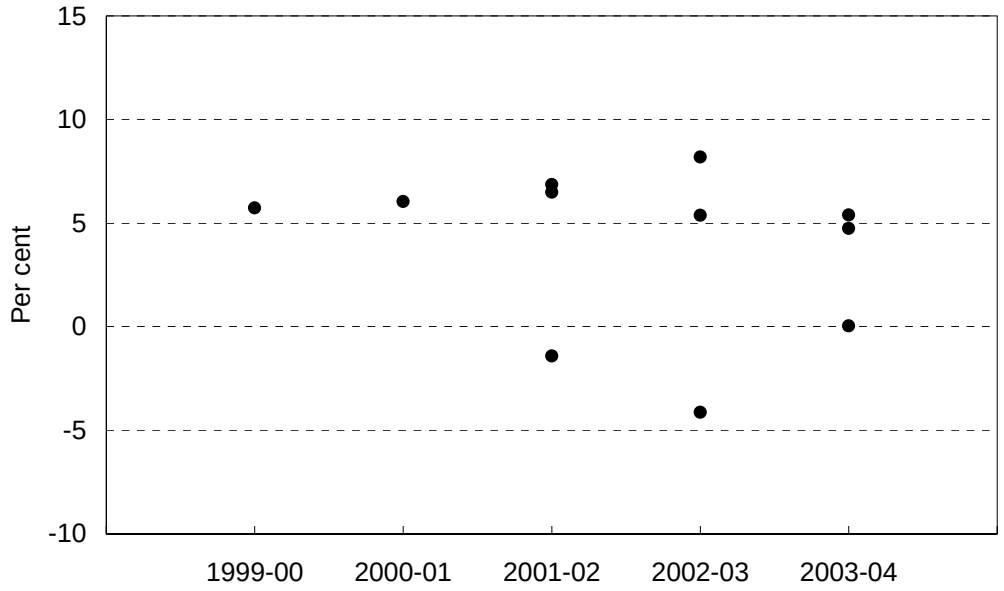
In 2003-04, the rail sector recorded an operating loss before tax of $2.5 billion, largely because RIC recorded a $3 billion write down of assets, which were leased to ARTC.

Profitability, in terms of return on assets, has varied across railway GTEs (see figure 8.4).[9] QR has earned returns between 5.4 per cent and 6.5 per cent over the reporting period. RIC has recorded negative returns on assets since first being included in this report in 2001-02, with the return worsening in 2003-04 because of the write down of assets. As a result of a special government grant and an equity injection, ARTC recorded returns of 82.7 per cent in 2003-04, an increase from 8.2 per cent in 2002-03.

Trends in the return on equity for each rail GTE have generally reflected trends in the return on assets (see figure 8.4). Excluding RIC, return on assets was 4.8 per cent and return on equity was 5.1 per cent for the rail sector in 2003-04.

9 Asset revaluations can have a significant influence on the return on assets ratio because of their impact on asset values and operating profit (through depreciation expense). In addition to RIC's major revaluation, QR has also revalued assets throughout the reporting period.

Figure 8.4 **Return on assets — rail GTEs**



Note QR has been monitored over the entire reporting period, RIC and ARTC have been reported since 2001-02, and the PTA and RailCorp are included for the first time for 2003-04. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue and adding back gross interest expense. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

The return on assets of RIC (- 44.2 per cent) and ARTC (82.7 per cent) are not shown in the figure.

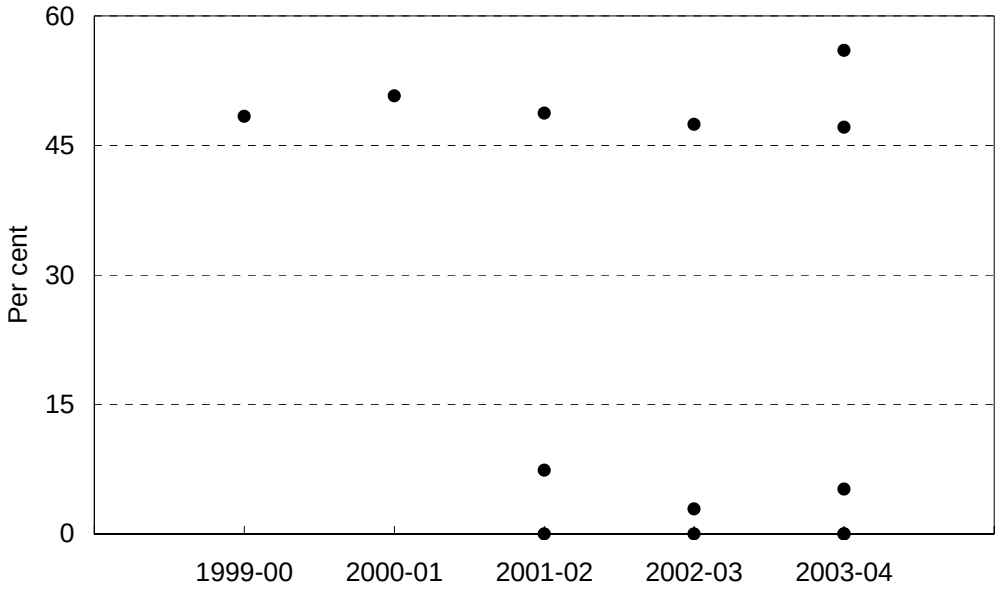
Source: Productivity Commission estimates.

8.4 Financial management

Financial management indicators provide information about the capital structure of a GTE and whether the costs of servicing debt and other liabilities can be met in a timely manner.

In 2003-04, QR and the PTA were carrying debt levels equivalent to around 45 per cent and 55 per cent respectively of their total assets (see figure 8.5). RIC had a debt to total assets ratio of 5.2 per cent. Two rail GTEs, RailCorp and ARTC, operated debt free.

Figure 8.5 **Debt to total assets — rail GTEs**



Note QR has been monitored over the entire reporting period, RIC and ARTC have been reported since 2001-02, and the PTA and RailCorp are included for the first time for 2003-04. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

Over the reporting period, debt to total assets ratios for rail GTEs have not only been influenced by the acquisition and retirement of debt, but also through changes in the total value of assets. For example, RIC's debt level increased by almost 120 per cent during 2002-03, but its debt to assets ratio fell because the increase in debt was not proportionally as large as the increase in asset values. Though, despite a similar increase in debt levels (113 per cent) in 2003-04, RIC's debt to assets ratio increased.

Under sound financial management, profits will be sufficient to ensure interest payments can be met. A high interest cover ratio indicates that the entity can sustain a fall in profit or increased interest expense and still meet the cost of servicing debt.

In 2003-04, two of the three rail GTEs with debt reported positive interest cover ratios. However, there does not appear to be a significant margin to insulate these GTEs from increases in interest rates or falling revenue.

A current ratio of less than 100 per cent indicates that the short-term obligations of the GTE may need to be met using sources of funds other than current assets. The current ratio

for the sector overall was 127 per cent in 2003-04, though only two of the five GTEs recorded a current ratio of more than 100 per cent in 2003-04.

8.5 Transactions with government

As a part of the reform process, governments have sought to give GTEs a greater commercial focus and facilitate competitive neutrality by exposing them to financial disciplines and regulations similar to those faced by privately-owned businesses.

Dividend payments from GTEs are a return on shareholder funds that impose capital disciplines and are consistent with competitive neutrality. In 2003-04, QR and ARTC were the only rail GTEs that made dividend payments ($115 million and $2 million respectively).

QR was also the only rail GTE required to make tax-equivalent payments. ARTC did not make tax-equivalent payments in 2003-04 because of permanent differences between taxable and accounting incomes, whilst RIC did not make tax-equivalent payments because of timing differences. RailCorp and the PTA were not required to make tax-equivalent payments in 2003-04.

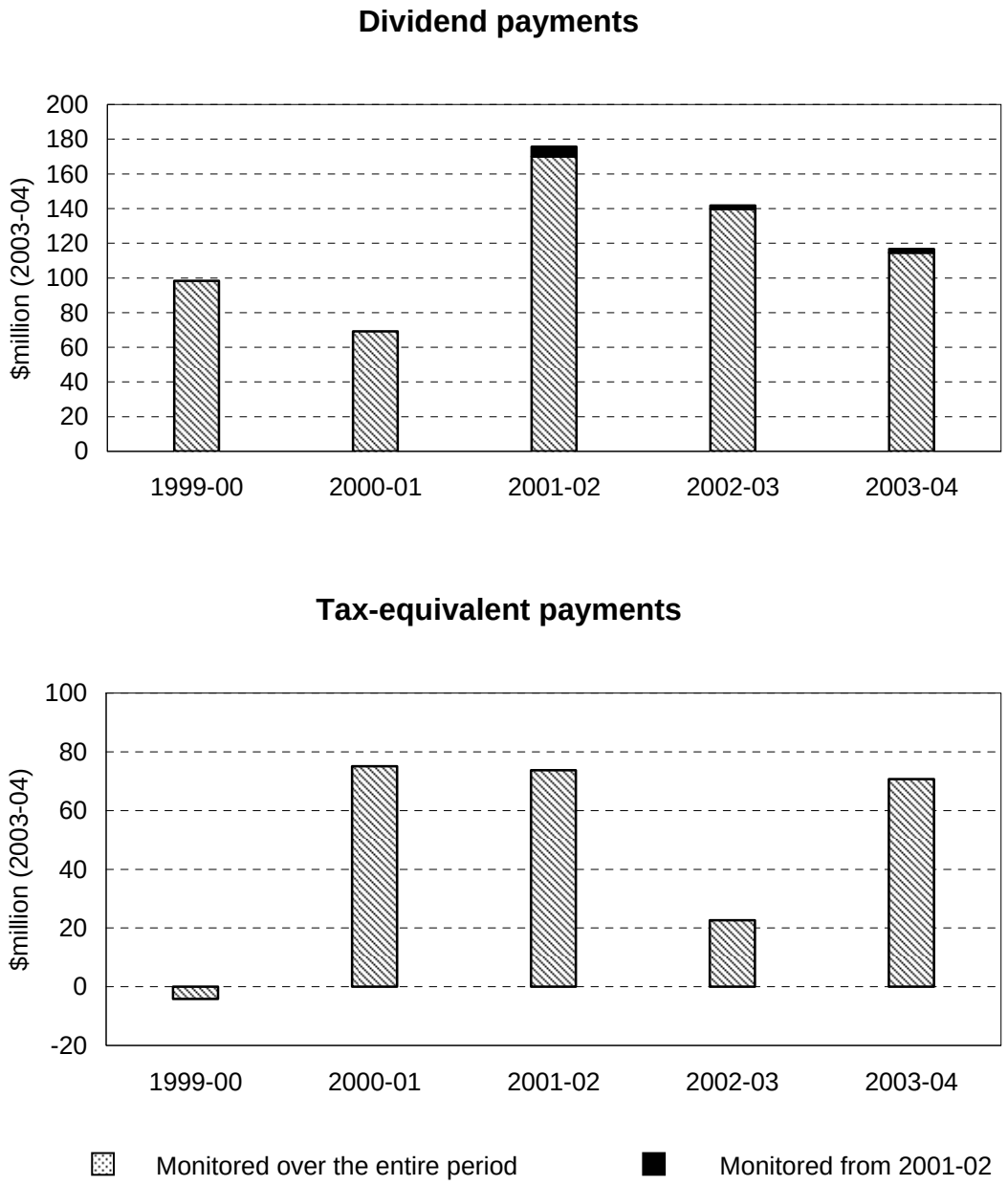
Dividend and income tax-equivalent payments over the reporting period are shown in figure 8.6.

The level of tax-equivalent payments was negative in 1999-00 because of adjustments made in QR accounts to reflect changes in the company tax rate. The value of this adjustment, which reduced future tax payable, was offset against the value of tax that applied to taxable income in 1999-00. Tax-equivalent payments made by QR decreased significantly in 2002-03 because of over provision by QR in the previous year.

Governments have moved towards identifying, costing and explicitly funding CSOs provided by rail GTEs. All of the monitored rail GTEs, except ARTC, had agreements to provide CSOs over the reporting period.

CSOs form a significant part of revenue for some rail GTEs. For example, CSO funding received by RailCorp for concessional fares and the provision of certain train services at the request of the NSW Government, accounted for around 40 per cent of revenue for the six months ended 30 June 2004.

Figure 8.6 **Dividend and income tax-equivalent payments — rail GTEs**



Note QR has been monitored over the entire reporting period, RIC and ARTC have been reported since 2001-02, and the PTA and RailCorp are included for the first time for 2003-04 (no dividend or tax has been paid by either the PTA or RailCorp). The value of dividends and tax-equivalent payments prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

RAIL

Whole of sector performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	7 796	7 354	8 985	19 167	25 437
Total revenue	$m	2 083	2 092	3 430	3 459	2 653
Profitability						
Operating profit before tax	$'000	176 817	185 531	249 134	- 65 054	- 2 498 717
Operating sales margin	%	21.1	21.8	14.0	5.1	- 84.2
Cost recovery	%	122.8	124.5	108.9	102.0	37.6
Return on assets	%	3.4	3.5	3.4	0.9	- 10.5
Return on equity	%	2.7	1.7	2.4	- 0.7	- 21.3
Financial management						
Debt to equity	%	159.9	174.8	108.5	28.9	29.7
Debt to total assets	%	28.4	29.7	26.3	19.6	25.0
Total liabilities to equity	%	234.6	234.5	161.0	44.2	45.0
Interest cover	times	1.7	1.7	2.0	0.7	- 7.2
Current ratio	%	87.1	117.3	94.4	88.4	127.2
Leverage ratio	%	334.6	334.5	261.0	144.2	145.0
Payments to and from government						
Dividends	$'000	101 000	69 736	175 466	141 639	116 603
Dividend to equity ratio	%	1.5	1.1	2.4	1.1	1.0
Dividend payout ratio	%	55.8	63.5	100.0	- 161.5	- 4.5
Income tax expense	$'000	- 4 301	75 722	73 698	22 622	70 725
CSO funding	$'000	670 826	637 269	852 020	941 677	1 823 111

Note QR has been monitored over the entire reporting period, RIC and ARTC have been reported since 2001-02, and the PTA and RailCorp are included for the first time for 2003-04.

8.6 GTE performance reports

Rail Infrastructure Corporation (NSW)
Rail Corporation New South Wales
Queensland Rail (Queensland)
Public Transport Authority (WA)
Australian Rail Track Corporation (Australian Government)

RAIL INFRASTRUCTURE CORPORATION — New South Wales

Rail Infrastructure Corporation (RIC) operates under the *Transport Administration Act 1988* and the *State Owned Corporations Act 1989*. It was formed by merging the assets, rights and liabilities of two NSW Government owned corporations — the Rail Access Corporation, which was responsible for rail network management and access, and Rail Services Australia, which operated principally as a maintenance contractor.

On 1 January 2004, the metropolitan functions of RIC were transferred to Rail Corporation New South Wales (RailCorp). RIC's current role is owner of the New South Wales country rail network, as well as managing various engineering and operational facilities throughout country New South Wales. RIC also provide RailCorp with a number of business services.[1]

RIC operates the New South Wales rail network on behalf of the State Government and provides access to passenger and freight operators. The NSW Rail Access Regime establishes floor and ceiling prices based on RIC's costs and the maximum allowable rate of return on assets. The Independent Pricing and Regulatory Tribunal of New South Wales arbitrates disputes under the access regime.

In 2003-04, the major sources of revenue were access fees paid by rail service operators ($402 million), CSO funding from the NSW Government ($356 million), and maintenance and construction services ($331 million). However in the period, a write down of assets leased to Australian Rail Track Corporation (ARTC) led to a negative revenue item of almost $3 billion.[2]

Assets decreased by $7.8 billion in 2003-04, primarily because of a $4.7 billion transfer to RailCorp and Transport Infrastructure Development Corporation, and the write down of assets leased to ARTC ($3.0 billion).

RIC is subject to dividend and tax-equivalent payments. In 2003-04, no dividend or income tax was paid reflecting RIC's financial position.[3]

RIC receives CSO funding for the cost of maintaining non-commercial railway lines.

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1 From September 2004, RIC will monitor and manage the various agreements with ARTC, including the ARTC's lease of the NSW interstate and Hunter Valley rail corridors and tracks.

2 In accordance with Treasury Directions, the ARTC lease is a finance lease, which is to be treated as a sale with the relevant infrastructure assets written down.

3 RIC expects to remain in a tax loss position for some time and thus is unlikely to incur tax-equivalent payments in the near future.

RAIL INFRASTRUCTURE CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*[c]
Size						
Total assets	$m			1 085	11 086	3 327
Total revenue	$m			1 184	1 141	- 1 721
Profitability						
Operating profit before tax	$'000			- 20 414	- 255 637	-3 190 667
Operating sales margin	%			- 1.8	- 22.7	185.2
Cost recovery	%			84.8	77.4	- 119.4
Return on assets	%			- 1.4	- 4.1	- 44.2
Return on equity	%			- 3.1	- 4.6	- 49.6
Financial management						
Debt to equity	%			12.3	1.7	15.2
Debt to total assets	%			7.4	2.9	5.2
Total liabilities to equity	%			66.3	6.5	35.0
Interest cover[d]	times			- 3.1	- 57.6	- 1 493.5
Current ratio	%			98.4	69.6	113.2
Leverage ratio	%			166.3	106.5	135.0
Payments to and from government						
Dividends	$'000			0	0	0
Dividend to equity ratio	%			0.0	0.0	0.0
Dividend payout ratio	%			0.0	0.0	0.0
Income tax expense	$'000			0	0	0
CSO funding	$'000			246 625	285 813	356 343

a 2001-02 was the first year that Rail Infrastructure Corporation (RIC) was included in this report. It was established on 1 January 2001 from a merger of the Rail Access Corporation and Rail Services Australia by the *Transport Administration Amendment (Rail Management) Act 2000*. **b** From 2002-03, the New South Wales Treasury Accounting Policy on Valuation of Physical Non-Current Assets at Fair Value required RIC to value assets at depreciated optimised replacement cost. This necessitated the revaluation of community service infrastructure assets — previously valued at zero to represent the net present value of their future cash flows — and increased the balance sheet value of property, plant and equipment by almost $10 billion. Total depreciation increased from $46.7 million in 2001-02 to $479 million in 2002-03. **c** Includes a $4.7 billion transfer to Rail Corporation and Transport Infrastructure Development Corporation, and a $3.0 billion write down of assets leased to Australian Rail Track Corporation. **d** Due to the capitalisation of certain borrowings and borrowing costs, interest cover is not a reliable measure of RIC's ability to make interest payments.

RAIL CORPORATION — New South Wales

Rail Corporation New South Wales (RailCorp) was established as a State Owned Corporation on 1 January 2004 and operates under the *Transport Administration Act 1988* and the *State Owned Corporations Act 1989*. RailCorp commenced operations by merging the State Rail Authority of New South Wales (StateRail) with the metropolitan arm of Rail Infrastructure Corporation. The financial performance of StateRail is reported separately at the end of this section, though its performance in 2003-04 is not comparable to previous years.

RailCorp is responsible for the control and operation of CityRail and CountryLink in providing passenger rail transport. Additionally, RailCorp control the metropolitan rail network and provide access to freight operators in the metropolitan area. Charges for RailCorp's CityRail services are regulated by the Independent Pricing and Regulatory Tribunal of New South Wales. Charges for CountryLink services are determined by the Minister for Transport after a recommendation from RailCorp's Board.

For the six months ended 30 June 2004, RailCorp managed over $11 billion of assets, of which property, plant and equipment accounted for around 98 per cent.

RailCorp received $991 million in revenue over the period, with $401 million from CSO payments, $260 million from passenger services, and $253 million from capital and other government contributions. Operating profit before tax was $5 million in the period.

RailCorp is not subject to dividend payments and was not required to make tax-equivalent payments.[1]

RailCorp receives CSO payments relating to the provision of concession fares to specified classes of passengers and for revenue shortfalls resulting from providing certain train services at the request of the NSW Government.

1 Section 20S (Dividends) of the *State Owned Corporations Act 1989* does not apply to RailCorp, under Section 17B of the of the *Transport Administration Act 1988*.

RAIL CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*[a]
Size						
Total assets	$m					11 280
Total revenue	$m					991
Profitability						
Operating profit before tax	$'000					4 952
Operating sales margin	%					- 0.5
Cost recovery	%					73.8
Return on assets	%					0.0
Return on equity	%					0.0
Financial management						
Debt to equity	%					0.0
Debt to total assets	%					0.0
Total liabilities to equity	%					2.5
Interest cover	times					708.4
Current ratio	%					94.2
Leverage ratio	%					102.5
Payments to and from government						
Dividends	$'000					0
Dividend to equity ratio	%					0.0
Dividend payout ratio	%					0.0
Income tax expense	$'000					0
CSO funding	$'000					401 383

a 2003-04 was the first year that Rail Corporation was included in this report, commencing operations on 1 January 2004. Performance indicators are only provided for the six months ended 30 June 2004.

QUEENSLAND RAIL — Queensland

Queensland Rail (QR) is subject to the *Transport Infrastructure Act 1994* and the *Government Owned Corporations Act 1993*. QR provides freight services throughout regional Queensland, and operates passenger rail services in the Brisbane metropolitan area and between key regional centres.[1] It also manages Queensland's rail infrastructure.

In December 2001, the Queensland Competition Authority (QCA) approved QR's Access Undertaking. This set floor and ceiling prices for access to rail infrastructure, to be paid by third-party operators and QR's freight and passenger services. In accordance with the Undertaking, prices are determined by QR's network access unit, which operates separately from their other business units.

Since 1999-00, total assets have increased slightly. In July 2000, QR moved from the deprival value to either the cost or fair value method of accounting for non-current assets (depending on the asset class).[2] Capital expenditure increased from $445 million in 2002-03 to $470 million in 2003-04.

Increased coal and freight revenue have underpinned a rise in total revenue in each year of the reporting period. In 2003-04, revenue increased by 2.9 per cent with sales growth in metropolitan rail services and increased Transport Service Contract payments. Operating profit before tax increased by around 13 per cent, largely because of a reduction in borrowing costs by close to 5 per cent.

QR has CSO contracts with the Queensland Department of Transport for urban and intercity passenger services, low volume freight services and infrastructure. QR also receives reimbursements from various state government departments for concessions provided to senior citizens, pensioners and students. In 2003-04, CSO payments — in the form of Transport Service Contract payments — accounted for around 30 per cent of total revenue.

1 QR is the sole government-owned rail freight operator in Australia, following the sale of the Western Australian Government Railway Commission's freight division in December 2000 and the joint sale of the National Rail Corporation and FreightCorp in January 2002.

2 This was the first stage of a progressive revaluation to be completed by 30 June 2005 and led to revaluations of most non-current assets between 2000-01 and 2003-04.

QUEENSLAND RAIL (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	7 796	7 353	7 649	7 818	7 936
Total revenue	$m	2 083	2 091	2 151	2 218	2 283
Profitability						
Operating profit before tax	$'000	176 817	185 531	252 373	169 612	191 198
Operating sales margin	%	21.1	21.8	22.5	18.7	18.5
Cost recovery	%	122.8	124.5	125.8	120.1	119.7
Return on assets	%	5.7	6.0	6.5	5.4	5.4
Return on equity	%	7.4	4.8	7.5	5.6	4.5
Financial management						
Debt to equity	%	159.9	174.8	142.1	138.7	137.1
Debt to total assets	%	48.4	50.7	48.7	47.5	47.1
Total liabilities to equity	%	234.6	234.5	197.3	195.5	193.3
Interest cover	times	1.7	1.7	2.1	1.7	1.8
Current ratio	%	87.1	117.3	86.9	90.3	65.8
Leverage ratio	%	334.6	334.5	297.3	295.5	293.3
Payments to and from government						
Dividends	$'000	101 000	69 736	169 741	139 639	114 603
Dividend to equity ratio	%	4.1	3.1	7.1	5.4	4.3
Dividend payout ratio	%	55.8	63.5	95.0	95.0	95.1
Income tax expense	$'000	- 4 301	75 722	73 698	22 622	70 725
CSO funding	$'000	670 826	637 269	605 395	655 864	665 671

a Future tax benefits and liabilities were adjusted, causing a negative tax expense. A Cross-Border Lease transaction resulted in assets being written-down by $232 million. A Cross-Border Lease involves the leasing of equipment or assets between entities in different jurisdictions — that is, where the lessor is from overseas and the lessee is in Australia. The lease is structured so that tax savings may be passed on from the overseas lessor to the local lessee, thereby lowering leasing costs. **b** In 2000-01, further lease transactions from previous years were written down by $376 million, contributing to a $540 million asset devaluation. **c** A revaluation in 2001-02 led to a $253 million increment to infrastructure assets. **d** Revaluation of assets during 2002-03 led to a net increase of $53 million in asset values. **e** Revaluation of assets during 2003-04 led to an increase in asset value by $68 million.

PUBLIC TRANSPORT AUTHORITY — Western Australia

The Public Transport Authority (PTA) was established as a State Owned Corporation on 1 July 2003 and operates under the *Public Transport Authority Act 2003*. The PTA is no longer classified as a GTE and is an 'on budget agency' in the Department of Planning and Infrastructure.

The PTA replaces the Western Australian Government Railway Commission and is responsible for providing transport for rail, bus and ferry services in the metropolitan area, public transport services in regional centres, coach and rail passenger services to regional areas, and school buses. The PTA is accountable for the control and operation of the Transperth System, Transwa regional services, and the school bus system. The PTA is also responsible for designing, building, managing and maintaining transport infrastructure throughout the state.

Charges for QR and the PTA passenger services are determined by their respective Boards but are subject to the approval of the relevant Minister.

The PTA managed $2 billion of assets with around $1.9 billion in property, plant, equipment and vehicles in 2003-04. Interest bearing liabilities were $1.1 billion in the period.

In 2003-04, the PTA received around $540 million in revenue, of which $400 million was from the WA Government and $72 million was from Transperth.

The PTA is not subject to dividend payments and was not required to make tax-equivalent payments.

The PTA receives CSO funding for the provision of non-commercial services.

PUBLIC TRANSPORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*[a]
Size						
Total assets	$m					2 019
Total revenue	$m					542
Profitability						
Operating profit before tax	$'000					26 190
Operating sales margin	%					17.5
Cost recovery	%					116.5
Return on assets	%					4.7
Return on equity	%					5.1
Financial management						
Debt to equity	%					221.6
Debt to total assets	%					56.0
Total liabilities to equity	%					295.8
Interest cover	times					1.4
Current ratio	%					45.7
Leverage ratio	%					395.8
Payments to and from government						
Dividends	$'000					0
Dividend to equity ratio	%					0.0
Dividend payout ratio	%					0.0
Income tax expense	$'000					0
CSO funding	$'000					399 714

a 2003-04 was the first year that the Public Transport Authority (PTA) was included in this report, commencing operations on 1 July 2003. The PTA replaced the Western Australian Government Railway Commission.

AUSTRALIAN RAIL TRACK CORPORATION Australian Government

Australian Rail Track Corporation Ltd (ARTC) was established on 28 February 1998 as part of the corporatisation of the former Australian Government owned Australian National Railways Commission (ANRC). It operates as an access provider and infrastructure manager. ARTC owns interstate track, principally in South Australia and Western Australia, and manages interstate track in New South Wales and Victoria under long-term lease arrangements.[1] It is bound by the *Corporations Act 2001*.

Rail access prices are set by the ARTC Board. Price guidelines are contained in the Rail Access Undertaking, a binding agreement between the Australian Competition and Consumer Commission (ACCC) and ARTC.[2] These guidelines specify floor and ceiling access prices based on ARTC's costs and risk profile.

ARTC's assets increased from $262 million in 2002-03 to $874 million in 2003-04, with an increase in cash assets by $607 million as a result of a $450 million special government grant and a $143 million equity injection.

In 2003-04, over 90 per cent of ARTC's revenue from ordinary activities was derived from access fees. Revenue increased by almost $460 million largely because of the government grant, to be mainly used for upgrading the rail network between Sydney and Brisbane.

In addition to ARTC's own capital investment programs, it is Trustee of the Australian Government's Australian Rail Infrastructure Foundation (ARIF). Disbursements by the ARIF do not directly appear in ARTC's financial statements.[3]

Division 58 of the *Income Tax Assessment Act 1997*, entitles ARTC to value its assets for tax purposes at the book value recorded in the accounts of its precursor, the ANRC. This is a higher value than that used by ARTC for accounting purposes and generates higher depreciation for taxation purposes, leading to significant tax losses. As a result, ARTC has not made income tax-equivalent payments over the reporting period. ARTC does not receive CSO funding.

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1 The NSW Government agreed in December 2003 to lease the interstate and Hunter Valley networks to ARTC for 60 years, commencing September 2004.

2 ARTC's voluntary access undertaking was approved by the ACCC in May 2002. The undertaking binds ARTC for five years and establishes processes for determining rail access terms and conditions, as well as pricing principles.

3 Projects funded by the ARIF are not recognised as revenue and are progressively recognised as assets when ARTC revalues rail infrastructure assets. The last revaluation was undertaken in June 2000.

AUSTRALIAN RAIL TRACK CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			251	262	874
Total revenue	$m			94	99	558
Profitability						
Operating profit before tax	$'000			17 175	20 971	469 610
Operating sales margin	%			16.9	19.4	84.1
Cost recovery	%			120.3	124.1	117.8
Return on assets	%			6.9	8.2	82.7
Return on equity	%			7.9	9.2	86.5
Financial management						
Debt to equity	%			0.0	0.0	0.0
Debt to total assets	%			0.0	0.0	0.0
Total liabilities to equity	%			14.8	10.5	3.1
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			187.2	301.8	2 773.7
Leverage ratio	%			114.8	110.5	103.1
Payments to and from government						
Dividends	$'000			5 725	2 000	2 000
Dividend to equity ratio	%			2.6	0.9	0.4
Dividend payout ratio	%			33.3	9.5	0.4
Income tax expense	$'000			0	0	0
CSO funding	$'000			0	0	0

a 2001-02 was the first year that Australian Rail Track Corporation was included in this report. It was established on 28 February 1998. **n.r.** Not relevant.

STATE RAIL AUTHORITY OF NSW

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*	*2003-04*[b]
Size						
Total assets	$m	5 356	5 362	5 412	5 636	766
Total revenue	$m	1 613	1 727	1 840	2 035	1 386
Profitability						
Operating profit before tax	$'000	84 134	14 055	1 848	80 840	104 587
Operating sales margin	%	6.0	1.6	0.7	4.5	8.2
Cost recovery	%	74.6	66.5	69.8	70.8	81.3
Return on assets	%	1.8	0.5	0.3	1.7	3.7
Return on equity	%	2.0	0.3	0.0	2.0	5.5
Financial management						
Debt to equity	%	4.8	4.8	4.8	4.6	- 50.3
Debt to total assets	%	3.7	3.7	3.6	3.5	5.9
Total liabilities to equity	%	30.5	30.0	32.4	34.7	- 303.5
Interest cover	times	7.1	1.9	1.1	7.1	9.1
Current ratio	%	31.5	65.7	79.6	49.5	65.9
Leverage ratio	%	130.5	130.0	132.4	134.7	- 203.5
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0	0	0	0	0
Dividend payout ratio	%	0	0	0	0	0
Income tax expense	$'000	0	0	0	0	0
CSO funding	$'000	478 900	593 116	634 083	769 472	413 616

a Land was revalued upwards by $147 million and buildings by $304 million. Net assets to the value of $564 million were transferred to the Rail Access Corporation. **b** State Rail Authority of New South Wales was disbanded in 2003-04 and will eventual be dissolved. The transactions, cash flows, assets, liabilities and equity items at 30 June 2004 are not directly comparable with those of the previous years.

9 Ports

The financial performances of 22 port government trading enterprises (GTEs) are covered in this chapter.[1] In 2003-04, these GTEs were responsible for assets valued at over $5.7 billion and earned around $1 billion in revenue.

These GTEs vary in size and the range of services they provide. The principal activities undertaken include the provision and maintenance of port infrastructure and, in some cases, port services such as mooring, stevedoring and pilotage. A small number of port GTEs are also involved in airport operations.

The overall performance of the sector is presented in table 9.2 at the end of this overview. This is followed by performance summaries for each GTE. For a discussion of the data and the performance indicators used, and some of the factors that should be considered when assessing performance, see chapter 3.

9.1 Monitored GTEs

The port GTEs monitored in this report do not all undertake the same activities, although the management of port land and channels is common to almost all (see table 9.1). The nature of involvement (if at all) in other port activities — such as pilotage, stevedoring, towage and cold storage facilities —varies across GTEs.

[1] For completeness, the financial performance of the Victorian Regional Channels Authority, which commenced operations on 1 April 2004, is also reported in this chapter.

Table 9.1 **Activities — port GTEs, 2003-04**

Port GTE	*Jurisdiction*	*Activities*				
		Port facilities management	Pilotage	Stevedoring	Cold storage	Airport operations
Newcastle Port Corporation	NSW	✓	✓	✗	✗	✗
Port Kembla Port Corporation	NSW	✓	✓	✗	✗	✗
Sydney Ports Corporation	NSW	✓	✓	✗	✗	✗
Port of Melbourne Corporation	Victoria	✓	✗	✗	✗	✗
Victorian Channels Authority[a]	Victoria	✗	✗	✗	✗	✗
Victorian Regional Channels Authority[b]	Victoria	✗	✗	✗	✗	✗
Gladstone Port Authority	Queensland	✓	✓	✓	✗	✗
Port of Brisbane Corporation	Queensland	✓	✗	✗	✗	✗ [c]
Cairns Port Authority	Queensland	✓	✗	✗	✗	✓
Townsville Port Authority	Queensland	✓	✓	✗	✗	✗
Ports Corporation of Queensland	Queensland	✓	✓	✗	✗	✗
Mackay Port Authority	Queensland	✓	✗	✗	✗	✓
Fremantle Port Authority	WA	✓	✗	✗	✗	✗
Bunbury Port Authority	WA	✓	✓	✗	✗	✗
Port Hedland Port Authority	WA	✓	✓	✗	✗	✗
Dampier Port Authority	WA	✓	✗	✗	✗	✗
Geraldton Port Authority	WA	✓	✓	✗	✗	✗
Albany Port Authority	WA	✓	✓	✗	✗	✗
Burnie Port Corporation	Tasmania	✓	✓	✗	✓	✗
Hobart Ports Corporation	Tasmania	✓	✓	✓[d]	✓	✗ [c]
Port of Devonport Corporation	Tasmania	✓	✓	✗	✓	✓
Port of Launceston Pty Ltd	Tasmania	✓	✓	✗	✗	✗
Darwin Port Corporation	NT	✓	✓	✗	✗	✗

a The Victorian Channels Authority (VCA) was transferred to the Port of Melbourne Corporation in November 2003 and the VCA was abolished pursuant to Section 181 of the PSA on 31 March 2004. **b** The Victorian Regional Channels Authority (VRCA) began operations on 1 April. **c** Investment only — Not direct operation. **d** Subsidiaries of the Hobart Ports Corporation provide stevedoring services in several SA ports and in Tasmania.

A number of port GTEs also have interests in other areas of business, including airports. For example, the Port of Brisbane Corporation (PBC) and the Hobart Ports Corporation (HPC) each have a substantial interest in their local airport.[2] Some regional port GTEs — including the Cairns Port Authority, Mackay Port Authority and the Port of Devonport Corporation — also own and operate airports.

Changes to the range of services should be taken into account when assessing and comparing financial performances overtime. The financial performances of some port GTEs have been affected by the franchising of some activities, for example, the issuing of exclusive or non-exclusive licences to operate or provide services within the port, such as stevedoring, pilotage and towage.

The number of monitored port GTEs has changed over the reporting period. In 2003-04, the set of monitored GTEs included one extra port than the previous year, due to the inclusion of both the former Victorian Channels Authority (VCA) and the Victorian Regional Channels Authority (VRCA).[3]

The size of the monitored port GTEs — in terms of the value of the assets controlled and revenue — varies substantially (see figure 9.2). In 2003-04, the smallest in terms of asset value was the Albany Port Authority ($39.3 million) and the largest was the PBC ($1.3 billion).

There are also differences across jurisdictions in the operating principles established for port GTEs. These differences include the emphasis on commercial objectives by boards and governments, compared to the importance of other objectives such as trade facilitation and regional development. In most jurisdictions, port GTEs operate under a jurisdiction-specific, GTE-wide corporatisation framework.

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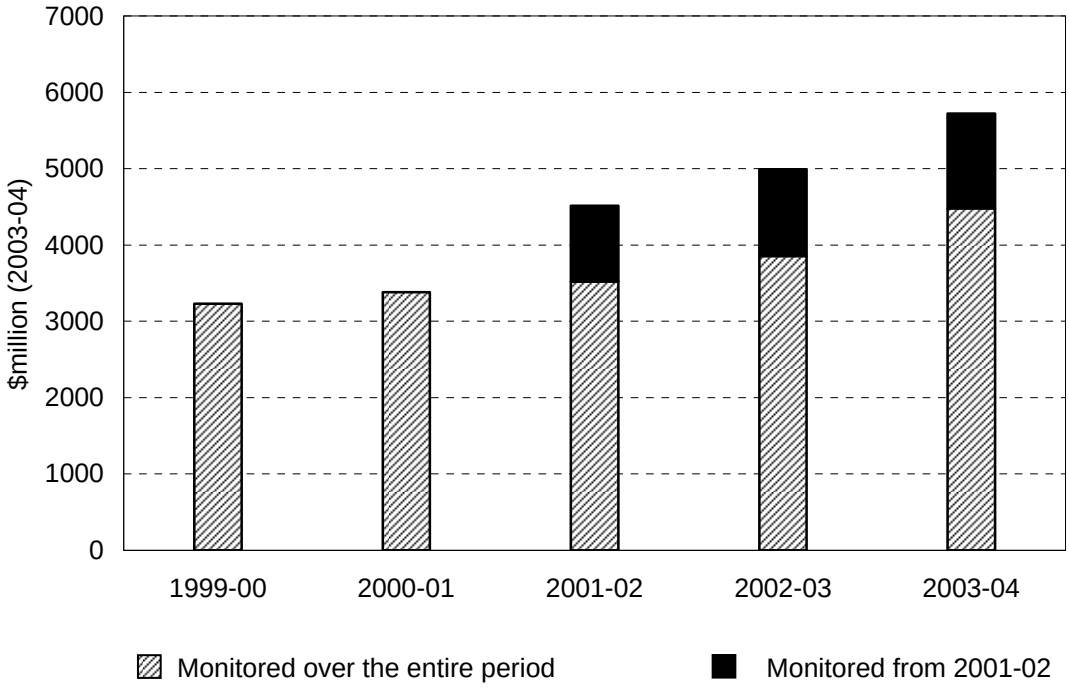
2 In 2003-04, the PBC owned 38 per cent of the Brisbane Airport Corporation Limited and the HPC owned 98 per cent of Hobart International Airport Pty Ltd (HIA). These airport investments are not consolidated in either GTE's financial accounts because neither have a controlling interest in the airport in which they have an ownership interest. Despite HPC's 98 per cent ownership share in the HIA, its operations were not consolidated in HPC's 2003-04 accounts because a joint venture agreement limits its capacity to make decisions over financial and operating policies. On 30 June 2004, HPC acquired the remaining HIA shares, HIA therefore became a wholly-owned subsidiary of HPC.

3 The VCA was transferred to the Port of Melbourne Corporation in November 2003 and the VRCA began operations on 1 April 2004. As the VCA and the VCRA were both operating for a proportion — but not all — of the financial year, the financial performance of both these GTEs are reported.

Figure 9.1 **Sector assets — port GTEs**



Note An additional eight regional port GTEs (four in Queensland and four in Western Australia) were monitored for the first time in 2001-02. The values of sector assets prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation for Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

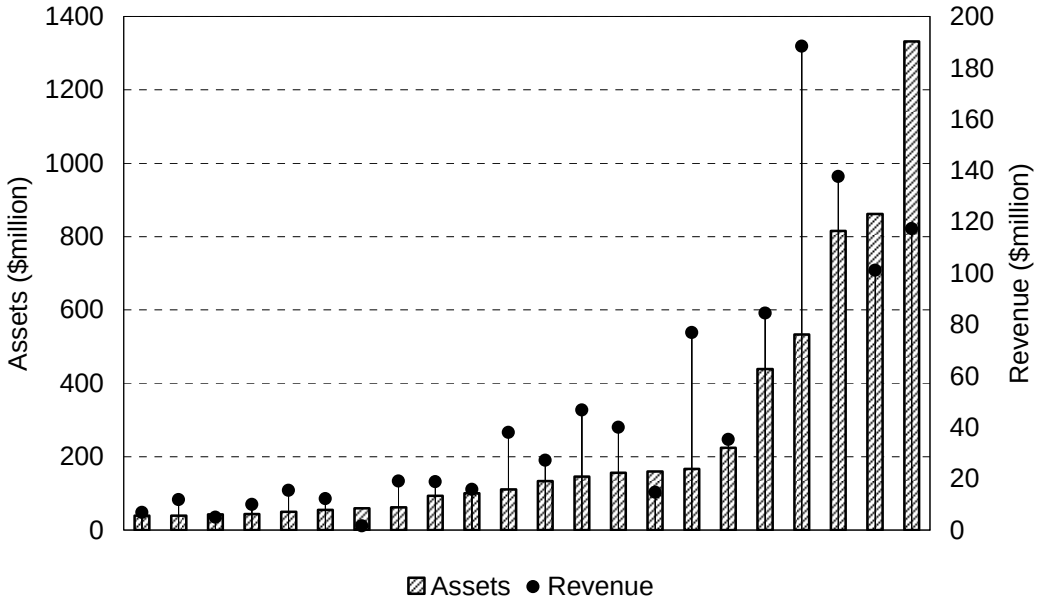
9.2 Market environment

The financial performances of port GTEs are affected by changes in the level and composition of trade throughput. Port reforms over the last decade have also affected performance by changing the scope and nature of activities carried out by some port GTEs and by increasing their commercial focus.

Trade throughput

Trade throughput is susceptible to changes in both domestic and international markets, particularly shifts in demand for key trade commodities. Due to differences in the composition and size of the markets served, changing market environments do not impact on all GTEs uniformly.

Figure 9.2 **Assets and revenue — port GTEs, 2003-04**



Source: Productivity Commission estimates.

Port GTEs with a diversified range of cargoes are less affected by market trends in key commodities, but may retain an exposure to changes in the overall level of economic activity. For port GTEs where a single commodity accounts for a dominant share of total port throughput — such as Newcastle Port, where coal accounted for around 94 per cent of throughput in 2003-04 — changes in market conditions for that commodity can substantially affect the GTE's financial performance.

Over the reporting period, some monitored port GTEs have experienced extraordinary changes in the market environment specific to a particular port or activity, such as the closure of BHP–Billiton steel making facilities in Newcastle in 1999-00. Events of this nature usually have a significant effect on financial performance and make comparisons with previous years difficult.

Corporate reforms

Government reforms for the ports sector over the last decade or so were aimed at improving the efficiency and financial performance of GTEs by making them more commercially focused. In general, the reforms were consistent with those recommended in the 1993 Industry Commission report *Port Authority Services and*

Activities (IC 1993). Some of the major recommendations of the Industry Commission's report were:

- ports should be constituted as statutory bodies, which are separate from the departmental structure of government;
- ports should be exposed to a tax-equivalent regime, be reimbursed for any community service obligations (CSOs) and pay dividends from after tax profits;
- the adoption, where cost efficient, of a landlord model of operation;[4] and
- where the landlord model is adopted, governments should identify and divest non-core activities and contract out, where cost effective, core activities.

The primary aim of these reforms was the establishment of clear objectives that eliminate any conflicts arising out of the commercial and non-commercial activities of the GTE, as well as replicating factor market disciplines. With reform, competition in the provision of port services has increased, mainly through the competitive tendering and franchising to private operators of activities such as stevedoring, pilotage, mooring, general maintenance and ship cleaning.

Most restructuring and rationalisation occurred prior to the reporting period. For example, three independent port corporations replaced the former Maritime Services Board of NSW in 1995-96.[5] In the same year, the Port of Melbourne Authority was divided into three separate entities.

Changes to the legislative framework governing some port GTEs have occurred during the reporting period. In Victoria, the *Port Services Act 1995* was amended in 2003 as part of the Victorian Government's port reform process. As a result, the Melbourne Port Corporation (MPC) was abolished on 1 July 2003 and replaced by the Port of Melbourne Corporation (PoMC).

On 3 November 2003, the PoMC also assumed responsibility for the management of the Melbourne channels, which were formerly managed by the Victorian Channels Authority (VCA). All assets of the VCA, with the exception of those assets required for the ongoing management of the ports of Geelong, Hastings and Portland, were transferred to the PoMC on this date. Responsibility for the Geelong channels and the approaches to the ports of Portland and Hastings has been assigned to a new entity, the Victorian Regional Channels Authority (VRCA), which began operations on 1 April 2004.

4 The landlord model is characterised by the port authority concentrating on the supply of core activities only, with the more contestable waterfront services, such as stevedoring and pilotage, supplied privately.

5 Newcastle Port Corporation, Port Kembla Port Corporation and Sydney Port Corporation were established.

In Western Australia, separate legislation covering several individual port authorities was repealed and replaced by the *Port Authorities Act 1999*. This provided for the commercialisation of port authorities and included provisions relating to the establishment of boards of directors, financial arrangements and dividend payments.

In the Northern Territory, the *Darwin Port Authority Act 1983* was replaced by the *Darwin Port Corporation Act 1999*. Included in the new Act were provisions relating to the establishment of a commercial charter, a board of directors and ministerial directions.

Port charges

A number of reforms have led to improved pricing and allocative mechanisms over the reporting period. Consumption-based charging has been progressively introduced, resulting in port users incurring charges that relate to their individual service requirements, rather than the value of their cargo (PC 2002b).

In Victoria, port charges are regulated by the Essential Services Commission (ESC).[6] In all other jurisdictions, port charges are determined by the board of each GTE, but are subject to the approval of the relevant minister.

Generally, charges of port GTEs in capital cities have declined in real terms over the last decade. For example, real charges for container vessels fell by more than 50 per cent in Sydney and Melbourne between 1990-91 and 2000-01 (PC 2002b).[7] Port charges have also fallen in some regional ports. For example, although Port Hedland Port Authority's nominal charges increased by 7.9 per cent in 2002-03, its charges have fallen 24 per cent — in real terms — since 1999-00.

6 Formerly the Office of the Regulator-General (ORG).

7 Beyond this period, the Victorian ORG determined that land-based prescribed services charges should be reduced by an average of 5.2 per cent per annum in real terms and that channel-based prescribed services should be reduced by 2.1 per cent per annum in real terms over the period 2000-01 to 2004-05.

9.3 Profitability

Port GTEs experienced substantial variation in their profitability over the reporting period. Some of this variation can largely be explained by restructuring related to the reform process. For example, the transfer of administration of a channel deepening project from the VCA to the PoMC affected the profit results of both GTEs in 2003-04.

The increase in trade throughput experienced by many monitored port GTEs contributed to the 93 per cent ($152 million) increase in sector profits in 2003-04. This is a considerable change compared with an increase in profits of 27 per cent ($35 million) between 1999-00 and 2002-03.

In 2003-04, the cost recovery ratio for the sector as a whole increased from 131 per cent to 156 per cent, due mainly to substantial improvements in some large GTEs within the sector, including the Brisbane Port Authority, Sydney Port Authority and Gladstone Port Authority. Previously, this ratio had fallen from approximately 170 per cent in 1999-00 to 130 per cent in 2001-02, mainly reflecting the inclusion of the eight additional port GTEs in 2001-02 — which, as a group, had an overall cost recovery ratio of around 110 per cent.

The substantial increase in profits facilitated an increase in the return on assets ratio for the sector as a whole from 4.8 per cent in 2002-03 to 7.2 per cent in 2003-04. Prior to this, the return on assets ratio had fallen from 6.1 per cent in 1999-00 to 4.8 per cent in 2002-03. The majority of monitored port GTEs reported returns on assets in the range of zero to 12 per cent (see figure 9.3), although returns by some of the GTEs have on occasion been substantially lower than zero.

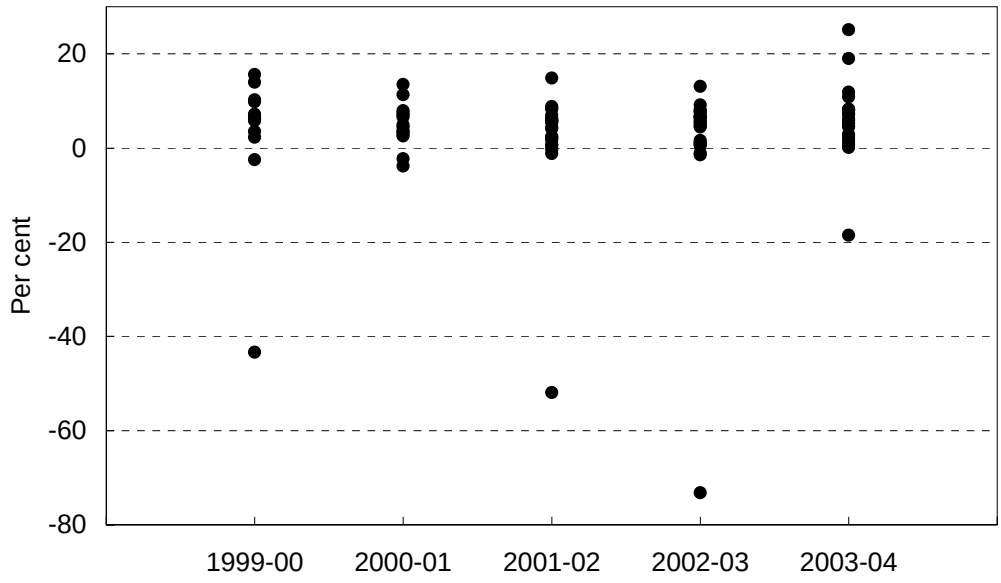
In 2003-04, the median rate of return on assets for the monitored port GTEs was close to the 2003-04 risk free rate of 10-year Commonwealth Government bonds of 5.7 per cent.

Downward asset revaluations were a major contributor to the recorded operating losses of certain port GTEs and the associated negative returns on assets.[8] For example, downward asset revaluations at the Burnie Port Corporation resulted in a negative return on assets in 1999-00 and 2000-01. The lowest return on assets over the reporting period occurred in 2002-03 for the Darwin Port Corporation, where assets were revalued downward by more than $43 million.

8 Profitability is reduced by downward asset revaluations because the reduction is recognised as an expense against revenue earned in that year. However, downward asset revaluations tend to improve profitability in future years because depreciation expenses will generally fall in line with the reduction in asset values.

Some GTEs have also experienced significant upward asset revaluations. For example, the Port of Brisbane Corporation's assets were revalued upward by a total of around $360 million during the reporting period, including an increase of more than $215 million in recorded land values in 2003-04.

Figure 9.3 **Return on assets — port GTEs**



Note The figure includes eight GTEs (4 from Queensland and 4 from Western Australia) that were included for the first time in 2001-02. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue and adding back gross interest expense. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

The return on equity — the ratio of a GTE's earnings to equity provided by the shareholder government — closely followed the trend in return on assets. In 2003-04, the sector return to equity ratio increased from 3.1 to 5.9 per cent. The ORG (now the ESC) proposed a benchmark return on equity of 7.3 per cent for the MPC and 6.7 per cent for the VCA (ORG 2000). In 2003-04, only nine out of the 23 port GTEs had a return on equity ratio of above 7 per cent, with the PoMC achieving only 1.1 per cent[9] and the VCA achieved 0.2 per cent.[10]

9 This figure represents the return on equity ratio for PoMC's first year of operations and was substantially affected by restructuring.

10 This figure represents the return to equity ratio for VCA's last 9 months in operation.

9.4 Financial management

Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

Over the reporting period there was considerable diversity in port GTEs' capital structure (see figure 9.4). In 2003-04, four port GTEs operated debt free.

In addition to being influenced by the acquisition and retirement of debt, the debt to total assets ratios for port GTEs have been influenced by changes in the total value of port assets. Asset revaluations in particular have a large impact on this ratio. For example, the Darwin Port Corporation's debt to total assets ratio increased from 34 per cent in 1999-00 to 55 per cent in 2003-04, despite borrowings declining by 5 per cent in nominal terms. The rise in the debt to total assets ratio was mostly due to downward asset revaluations of around $160 million made between 1999-00 and 2003-04.

A decline in the debt position of some GTEs was achieved through the retirement of debt. For example, the Burnie Port Corporation reduced nominal debt levels by 62 per cent over the reporting period, contributing to the fall in the debt to total assets ratio from 43 per cent in 1999-00 to 18 per cent in 2003-04.

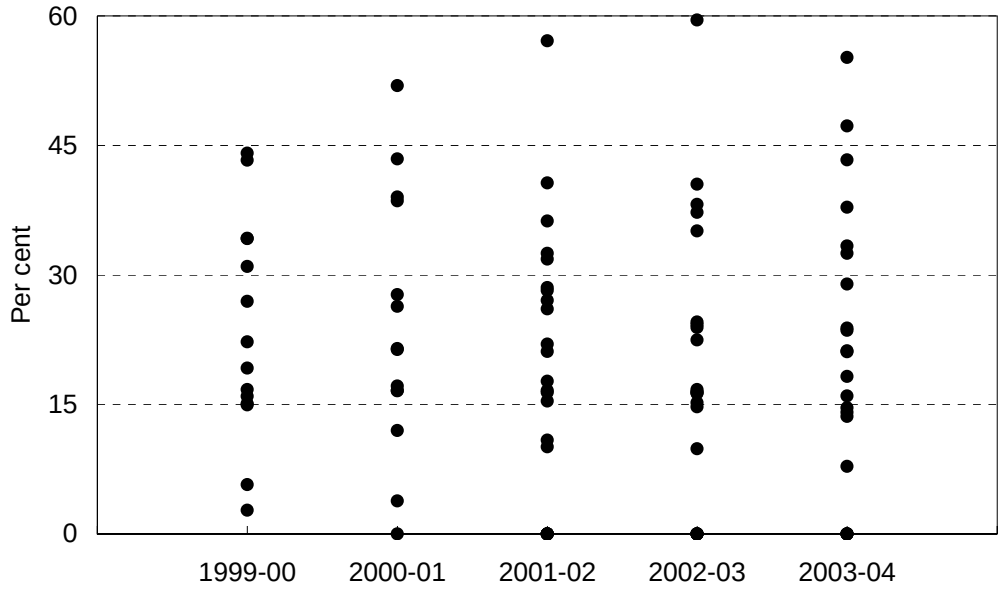
In 2003-04, interest cover — a measure of the capacity to meet periodic interest payments out of current earnings — was 5.5 times for the sector. This was higher than the previous year (3.6 times), and higher than the sector-wide interest cover at the beginning of the reporting period (3.2 times).

Changes in interest cover from year-to-year for some GTEs were related to asset revaluations. For example, the Gladstone Port Authority's interest cover increased from 3.7 times in 2002-03 to 9.7 times in 2003-04 with a $61 million increase in revenue, mainly attributable to a large asset revaluation increment.

The ability of port GTEs to meet short-term liabilities from short-term assets has improved over the reporting period, with the current ratio for the sector overall increasing from 105 per cent in 1999-00 to 157 per cent in 2003-04. However, five GTEs recorded a current ratio of less than 100 per cent in 2003-04 — this indicates that the short-term obligations of these GTEs may need to be met from sources of funds other than current assets.[11]

11 Current assets comprise cash and other assets that would, in the ordinary course of operations, be available for conversion into cash within 12 months after the end of the reporting period.

Figure 9.4 **Debt to total assets — port GTEs**



Note The figure includes eight GTEs (4 in Queensland and 4 in Western Australia) that were included for the first time in 2001-02. One port GTE did not have any debt in 2000-01, five port GTEs did not have any debt in 2001-02 or 2002-03 and four port GTEs did not have debt in 2003-04. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

9.5 Transactions with government

As a part of the reform process, governments have sought to give GTEs a greater commercial focus and facilitate competitive neutrality by exposing them to market disciplines and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles, see chapter 3.

Owner-governments generally require their GTEs to make tax-equivalent and dividend payments, along with debt guarantee fees. The introduction of these requirements resulted in an increase in payments to governments.

The dividend required to be paid by each GTE depends on the dividend policy of its State or Territory Government. In 2003-04, nine of the port GTEs had dividend

payout ratios above 50 per cent. Four port GTEs did not pay, or propose, a dividend for 2003-04.[12]

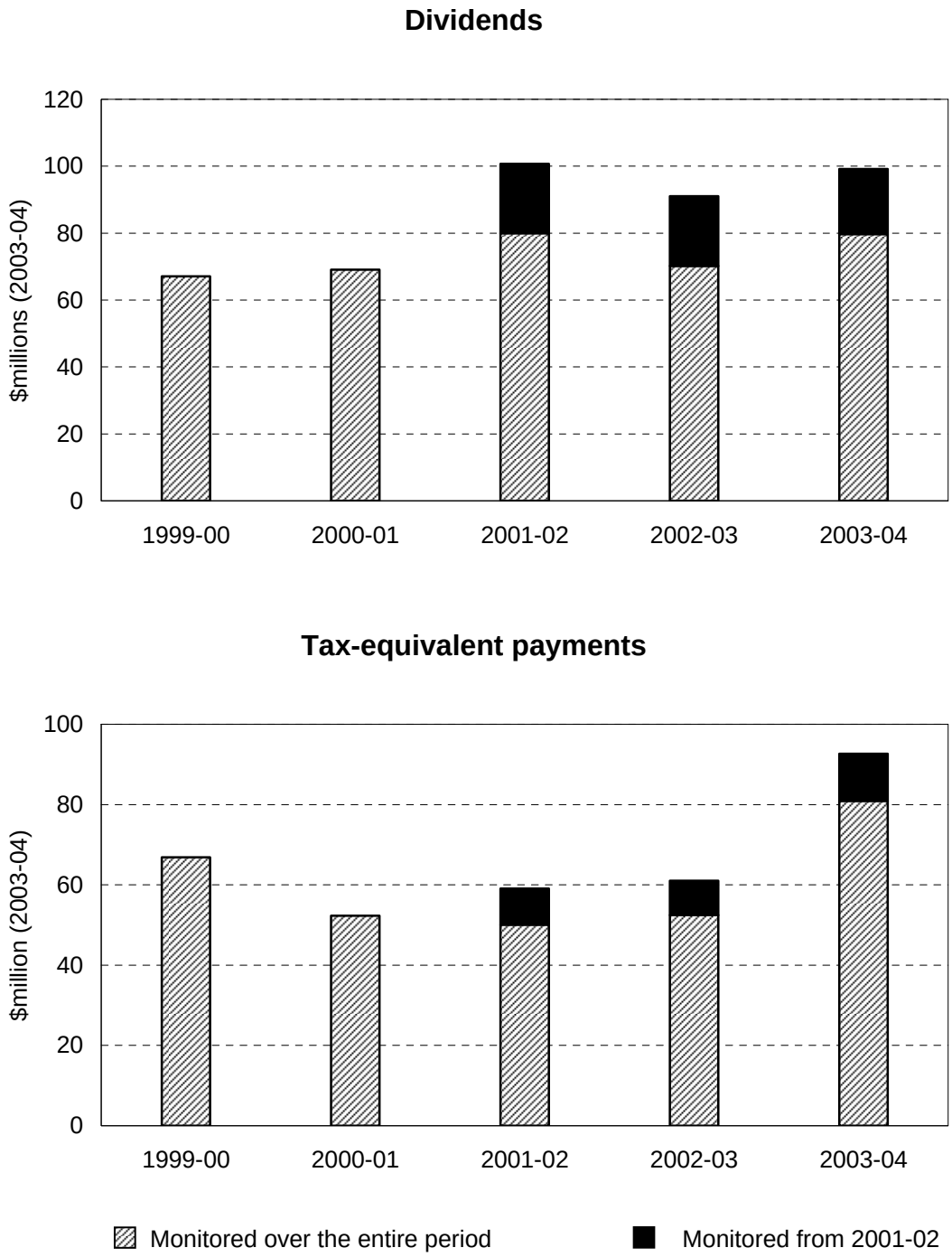
The level of tax-equivalent and dividend payments varies from year-to-year (see figure 9.5). In 2003-04, port GTEs made around $192 million in tax-equivalent and dividend payments to owner governments. The Queensland and NSW governments were the major beneficiaries, receiving 55 per cent and 26 per cent of the total payments respectively.

Under agreed reforms, port GTEs required to undertake non-commercial activities receive government CSO payments equivalent to the net cost incurred through these non-commercial activities.

Two port GTEs received CSO payments over the entire reporting period. In 2003-04, Port Kembla Port Corporation received CSO funding of $3.2 million. The payment was provided as compensation for the shortfall in income generated by the NSW Rental Relief Scheme for the Port Kembla Coal Terminal. The Darwin Port Corporation received $4.6 million to cover costs associated with small craft services, tourism and real estate, cruise and defence facilities, the Fort Hill Wharf, the NT Express, dredging of the City Wharves and the East Arm Port development.

12 This figure includes both the VRCA, which began operations on 1 April 2004, and the VCA, which ceased operations on 31 March 2004.

Figure 9.5 **Dividend and tax-equivalent payments — port GTEs**



Note The figure includes eight GTEs (four in Queensland and four in Western Australia) that were included for the first time in 2001-02. The value of dividends and tax-equivalent payments prior to 2003-04 were converted to 2003-04 dollars using the implicit price deflator — Gross Fixed Capital Formation for Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

PORTS

Table 9.2 **Whole of sector performance indicators 1999-00 to 2003-04**

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	3 149	3 356	4 521	4 997	5 722
Total revenue	$m	605	606	821	890	1 024
Profitability						
Operating profit before tax	$'000	128 949	140 715	130 548	163 659	315 874
Operating sales margin	%	29.5	31.2	23.6	23.9	35.9
Cost recovery	%	171.3	146.7	130.8	131.3	156.0
Return on assets	%	6.1	6.1	4.7	4.8	7.2
Return on equity	%	3.1	3.9	2.3	3.1	5.9
Financial management						
Debt to equity	%	32.4	32.3	30.1	32.8	30.2
Debt to total assets	%	23.2	23.3	21.5	23.8	22.5
Total liabilities to equity	%	44.6	43.0	42.7	44.9	42.3
Interest cover	times	3.2	3.5	2.7	3.6	5.5
Current ratio	%	105.1	128.2	136.8	130.4	157.1
Leverage ratio	%	144.6	143.0	142.7	144.9	142.3
Payments to and from government						
Dividends	$'000	65 346	68 533	100 838	91 136	99 165
Dividend to equity ratio	%	3.1	3.0	3.2	2.8	2.6
Dividend payout ratio	%	102.4	77.1	141.3	88.8	44.4
Income tax expense	$'000	65 149	51 869	59 163	61 075	92 629
CSO funding	$'000	9 926	12 184	13 994	15 354	7 778

9.6 GTE performance reports

Newcastle Port Corporation (NSW)
Port Kembla Port Corporation (NSW)
Sydney Ports Corporation (NSW)
Port of Melbourne Corporation (Victoria)
Victorian Channels Authority (Victoria)
Victorian Regional Channels Authority (Victoria)
Gladstone Port Authority (Queensland)
Port of Brisbane Corporation (Queensland)
Cairns Port Authority (Queensland)
Ports Corporation of Queensland (Queensland)
Mackay Port Authority (Queensland)
Townsville Port Authority (Queensland)
Fremantle Port Authority (WA)
Bunbury Port Authority (WA)
Port Hedland Port Authority (WA)
Albany Port Authority (WA)
Dampier Port Authority (WA)
Geraldton Port Authority (WA)
Burnie Port Corporation (Tasmania)
Hobart Ports Corporation (Tasmania)
Port of Devonport Corporation (Tasmania)
Port of Launceston Pty Ltd (Tasmania)
Darwin Port Corporation (NT)

NEWCASTLE PORT CORPORATION — New South Wales

Newcastle Port Corporation (NPC) operates under the *State Owned Corporations Act 1989* and the *Ports Corporatisation and Waterways Management Act 1995*. The NPC has responsibility for the management of port facilities and provides pilotage services.

Charges for most port services are set by the NPC's board and are subject to approval by the Minister for Transport.[1]

Newcastle is one of Australia's largest ports by tonnage, with a total throughput of 82.7 million tonnes in 2003-04. Coal accounted for around 94 per cent of throughput in 2003-04.

Pre-tax operating profit increased by 56 per cent in 2003-04, with a 15 per cent ($5 million) decrease in expenses. This substantial increase in profit is largely attributable to an adjustment to the defined benefit superannuation schemes and a decrease in labour, services, administration and materials costs as well as a small increase in revenue.

The NPC's current ratio increased substantially in 2003-04, following a large increase in the previous year also. In 2003-04 this was mainly caused by a 48 per cent ($9 million) increase in cash assets. The increase in 2002-03 was in the most part created by a decrease in current liabilities related to a reduction of $6 million in provision for dividends.

The NPC is required to make both dividend and tax-equivalent payments. In 2003-04, the NPC provided for a $2.4 million dividend payment and recorded a income tax-equivalent expense of $4 million.

1 Under the *Ports Corporatisation and Waterways Management Act 1995*, charges for navigation, pilotage, site occupation and wharfage are set by the board subject to approval by the Minister (ss. 51, 54, 62). Port cargo access charges are set by the Minister (s. 57) and berthing charges are set by the board (s. 66).

NEWCASTLE PORT CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	144	141	138	135	157
Total revenue	$m	38	38	39	40	40
Profitability						
Operating profit before tax	$'000	16 774	6 737	9 251	8 650	13 524
Operating sales margin	%	49.8	23.1	29.0	26.1	37.8
Cost recovery	%	177.4	130.1	140.8	135.3	160.8
Return on assets	%	14.0	6.6	8.3	8.0	10.9
Return on equity	%	14.1	8.9	6.7	6.4	9.7
Financial management						
Debt to equity	%	35.6	34.9	36.5	35.2	28.5
Debt to total assets	%	22.3	21.5	22.0	22.5	21.1
Total liabilities to equity	%	67.2	60.5	64.5	54.8	44.8
Interest cover	times	7.7	3.6	4.9	4.7	6.9
Current ratio	%	82.2	94.8	117.6	240.8	323.9
Leverage ratio	%	167.2	160.5	164.5	154.8	144.8
Payments to and from government						
Dividends	$'000	9 000	9 000	9 000	3 012	2 429
Dividend to equity ratio	%	10.6	10.4	10.5	3.5	2.5
Dividend payout ratio	%	75.3	116.0	156.3	55.0	25.5
Income tax expense	$'000	4 827	- 1 023	3 494	3 176	4 007
CSO funding	$'000	0	0	0	0	0

a Includes abnormal revenue of $4.1 million relating to superannuation interest earnings and a reduction in member liability. A restatement of deferred tax balances following a change in the future company tax rate resulted in a decline in income tax payments of $1.4 million. **b** Includes a $3.6 million expense relating to an adjustment to superannuation payments. An asset revaluation resulted in a $2.5 million increase in the value of plant and breakwater assets. Income tax expense is negative due to a write-back of the tax effect on the superannuation adjustment expense.

PORT KEMBLA PORT CORPORATION — New South Wales

Port Kembla Port Corporation (PKPC) operates under the *State Owned Corporations Act 1989* and the *Ports Corporatisation and Waterways Management Act 1995*. As well as managing the port, the PKPC provides pilotage services, and berths and equipment for private sector lease or common use.

Charges for most port services are set by the PKPC Board and are subject to the approval of the Minister for Transport.[1] The major cargoes that move through the port are coal, iron ore and steel products.

Pre-tax operating profit increased by $31 million in 2003-04, resulting in a pre-tax operating profit of almost $29 million. This was largely due to a upward revaluation of non-current assets.[2] However, even excluding the effect of the asset revaluation, pre-tax operating profit increased by approximately $10 million.

PKPC's debt level remained stable in 2003-04 after falling significantly in the two proceeding financial years.

PKPC is required to make both income dividend and tax-equivalent payments. In 2003-04 PKPC recorded a dividend of $2.3 million and a tax-equivalent expense of $7 million.

In 2003-04, PKPC received $3.2 million in community service obligation (CSO) funding from the NSW Government. The CSO is related to a rental relief package negotiated between the PKPC, NSW Treasury and Port Kembla Coal Terminal Limited (PKCTL). PKPC is paid the difference between the commercial rate for coal per tonne and a rate negotiated between PKCTL and the Government.

1 Under the *Ports Corporatisation and Waterways Management Act 1995*, charges for navigation, pilotage, site occupation and wharfage are set by the Board subject to approval by the Minister (ss. 51, 54, 62). Port cargo access charges are set by the Minister (s. 57) and berthing charges are set by the Board (s. 66).

2 A substantial portion of this revaluation was a net valuation increment of $22 million to the PKPC's recorded coal terminal value.

PORT KEMBLA PORT CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*[b]	*2002-03*[c]	*2003-04*[d]
Size						
Total assets	$m	135	139	127	114	146
Total revenue	$m	32	33	30	21	47
Profitability						
Operating profit before tax	$'000	8 302	10 588	7 226	- 2 731	28 575
Operating sales margin	%	40.6	45.4	39.0	1.4	68.6
Cost recovery	%	201.4	183.2	164.0	101.4	318.8
Return on assets	%	9.8	11.3	8.8	1.2	25.1
Return on equity	%	23.7	11.3	7.0	- 6.4	31.7
Financial management						
Debt to equity	%	100.2	90.1	91.1	87.7	61.3
Debt to total assets	%	44.1	43.4	40.7	40.5	37.8
Total liabilities to equity	%	127.8	110.4	114.5	104.4	82.0
Interest cover	times	2.7	3.2	2.6	0.3	8.1
Current ratio	%	91.9	137.4	193.1	182.1	282.4
Leverage ratio	%	227.8	210.4	214.5	204.4	182.0
Payments to and from government						
Dividends	$'000	7 988	8 200	3 928	0	2 333
Dividend to equity ratio	%	14.2	13.1	6.3	0.0	3.4
Dividend payout ratio	%	59.7	116.0	90.0	0.0	10.8
Income tax expense	$'000	- 5 077	3 516	2 862	956	7 065
CSO funding	$'000	4 490	8 784	9 251	8 510	3 186

a Includes an abnormal expense of $4.1 million relating to asset transfers and abnormal revenue of $2.2 million after a reassessment of superannuation liabilities. Includes a $700 000 adjustment to superannuation payments and a $700 000 expense relating to redundancy provisions. Income tax expense is reported as a negative amount largely due to a reduction in tax liability of $9 million following the recoverable amounts test undertaken in 1998-99. **b** Includes $500 000 in revenue related to a redundancy provision write-back and a $900 000 adjustment to superannuation payments. A recoverable amounts test resulted in an expense and downward asset revaluation of $2.8 million. **c** Includes a net revaluation decrement of property, plant and equipment equal to $9.5 million. Port Kembla Corporation incurred a tax expense in 2002-03 from permanent differences in accounting and tax profit. **d** Includes a net revaluation increment of property, plant and equipment of $19 million.

SYDNEY PORTS CORPORATION — New South Wales

Sydney Ports Corporation (SPC) operates under the *State Owned Corporations Act 1989* and the *Ports Corporatisation and Waterways Management Act 1995*. The SPC manages the commercial ports of Sydney Harbour and Botany Bay, and leases land to private stevedores. SPC also owns Sydney Pilot Service Pty Ltd (SPS) which operates as the pilot service provider for Sydney Harbour and Port Botany.[1]

Charges for most port services are set by the SPC Board and are subject to the approval of the Minister for Transport.[2] The SPC handled container throughput of approximately 1.27 million twenty-foot equivalent units in 2003-04, a 9.5 per cent increase on the previous year. The major cargoes moving through Sydney Harbour and Botany Bay included chemicals, manufactures and machinery. Sydney Harbour was also visited on 81 occasions by cruise ships.

The SPC's throughput, revenue and profitability increased in 2003-04. The increase in overall trade was due to the combination of a 7.5 per cent increase in total export cargoes and a 6 per cent increase in total import cargoes. Revenue increased by $15 million, resulting in a 26 per cent ($11 million) increase in pre-tax operating profit.

Total assets increased by 3 per cent ($24 million) in 2003-04. This had a positive effect on the SPC's financial indicators, with debt to equity, debt to total assets and total liabilities to equity ratios all decreasing slightly.

The SPC is required to make both dividend and tax-equivalent payments to the NSW Government. In 2003-04, SPC provided for a $18 million dividend payment and recorded an income tax-equivalent expense of $17 million.

1 SPS commenced operations in 2002-03, before this pilotage services were carried out by private operators.

2 Under the *Ports Corporatisation and Waterways Management Act 1995*, charges for navigation, pilotage, site occupation and wharfage are set by the Board subject to approval by the Minister (ss. 51, 54, 62). Port cargo access charges are set by the Minister (s. 57) and berthing charges are set by the Board (s. 66).

SYDNEY PORTS CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*[a]	*2003-04*
Size						
Total assets	$m	581	576	606	792	816
Total revenue	$m	108	109	106	123	138
Profitability						
Operating profit before tax	$'000	45 059	33 044	28 825	41 230	51 789
Operating sales margin	%	52.2	41.0	38.2	44.1	46.4
Cost recovery	%	222.6	169.4	161.9	178.8	186.4
Return on assets	%	10.2	7.9	7.0	7.9	8.1
Return on equity	%	7.1	6.5	4.3	5.5	6.1
Financial management						
Debt to equity	%	40.9	39.7	42.9	29.8	29.0
Debt to total assets	%	27.0	26.4	28.5	24.2	21.2
Total liabilities to equity	%	56.6	49.8	54.0	39.3	39.2
Interest cover	%	4.6	3.6	3.3	4.0	5.0
Current ratio	%	124.7	95.8	51.0	65.4	149.1
Leverage ratio	%	156.6	149.8	154.0	139.3	139.2
Payments to and from government						
Dividends	$'000	13 030	10 994	8 540	13 157	17 625
Dividend to equity ratio	%	3.6	2.9	2.2	2.7	3.1
Dividend payout ratio	%	50.0	44.8	50.9	50.0	50.1
Income tax expense	$'000	19 001	8 478	12 049	14 915	16 610
CSO funding	$'000	0	0	0	0	0

a Total assets increased by $186 million in 2002-03, caused mainly by an upward revaluation of non-current assets. Land accounted for $139.5 million of this revaluation increment.

PORT OF MELBOURNE CORPORATION — Victoria

The Port of Melbourne Corporation (PoMC) operates under the *Ports Services Act 1995* and commenced operations in 2003-04.[1] Under the Act, the PoMC is responsible for managing and developing the Port of Melbourne, ensuring the availability of essential port services and the management of channels.[2]

Charges for prescribed services, including the provision of berths and cargo marshalling facilities are subject to regulation by the Essential Services Commission (previously the Office of the Regulator-General (ORG)). The current price determination will expire on 30 June 2005.[3]

The PoMC handled around 37 per cent of Australia's total container trade in 2003-04 and hosted over 3200 commercial ship visits.

The PoMC's pre-tax operating profit was $15 million in 2003-04. Revenue was $101 million and expenses totalled $86 million. Large consultant expenses and costs relating to the preliminary design studies for the channel deepening project contributed significantly to the expenses figure.

The PoMC's total assets were $862 million in 2003-04. The PoMC is required to make both dividend and tax-equivalent payments to the Victorian Government. In 2003-04, the PoMC provided for a $5.8 million dividend payment and recorded an income tax-equivalent expense of $6.7 million.

The financial performance of MPC in the years 1999-00 to 2002-03 is reported separately in a table included at the end of this chapter.

1 The Melbourne Port Corporation (MPC), which began operation on 1 March 1996, ceased operations on 30 June 2003 and was replaced by the Port of Melbourne Corporation (PoMC).

2 On 3 November 2003, the transfer of the former Victorian Channels Authority to the PoMC was completed. PoMC took over responsibility for the channels and port waters of the Port of Melbourne at this time.

3 In June 2000, the ORG determined that land-based prescribed service charges in the Port of Melbourne should be reduced by an average of 5.2 per cent per annum in real terms and that channel-based prescribed service charges should be reduced by 2.1 per cent per annum in real terms over the period 2000-01 to 2004-05.

PORT OF MELBOURNE CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*[a]
Size						
Total assets	$m					862
Total revenue	$m					101
Profitability						
Operating profit before tax	$'000					14 801
Operating sales margin	%					16.8
Cost recovery	%					120.2
Return on assets	%					2.3
Return on equity	%					1.1
Financial management						
Debt to equity	%					9.0
Debt to total assets	%					7.8
Total liabilities to equity	%					15.4
Interest cover	times					4.2
Current ratio	%					84.7
Leverage ratio	%					115.4
Payments to and from government						
Dividends	$'000					5 880
Dividend to equity ratio	%					0.8
Dividend payout ratio	%					73.0
Income tax expense	$'000					6 743
CSO funding	$'000					0

[a] The Port of Melbourne Corporation (PoMC) commenced operations on 1 July 2003.

VICTORIAN CHANNELS AUTHORITY — Victoria

The Victorian Channels Authority (VCA) was a statutory authority established under the *Port Services Act 1995*, with the objective of managing channels and port waters for use on a fair, reasonable and commercial basis. It commenced operations on 1 March 1996. The VCA was abolished pursuant to Section 181 of the *Port Services Act 1995* on 31 March 2004.[1]

In July 2003, legislation was passed to create the Port of Melbourne Corporation (PoMC). The PoMC took over the land and waterside functions of the Port of Melbourne, including the Melbourne operations of the VCA, on 3 November 2003. All assets of the VCA, with the exception of those assets required for the ongoing management of the ports of Geelong, Hastings and Portland, were transferred to the PoMC on this date. Responsibility for the Geelong channels and the approaches to the ports of Portland and Hastings has been assigned to a new entity, the Victorian Regional Channels Authority (VRCA). The VCRA began operations on 1 April 2004.

The VCA was subject to pricing regulation, administered by the Essential Services Commission. The pricing regulation is aimed at progressively reducing the channel fees charged by the VCA, in real terms.

For the nine months ended 31 March 2004, the VCA reported a pre-tax profit of $500 000 compared to a full year tax loss of $1.6 million in 2002-03. This result was substantially affected by the transfer of administration of the channel deepening project to the PoMC in July 2003. This project cost VCA almost $6 million in 2002-03 and therefore contributed significantly to the loss experienced in that year. Transition costs also adversely affected the VCA's results for its final nine months of operation.

In 2003-04, the debt to equity and debt to total assets ratios were zero. The VCA was required to make tax-equivalent payments under the *State Owned Enterprises Act 1992*. In addition, the VCA was required to pay dividends to the Victorian Government. Tax expense of $279 000 was recorded and no dividend was paid in the first three quarters of 2003-04.

The financial performance of the VRCA, for its first three months of operation has been reported separately.

[1] As the VCA was abolished on 31 March 2004, its financial performance is only being reported for three quarters.

VICTORIAN CHANNELS AUTHORITY

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*	*2003-04*[d]
Size						
Total assets	$m	138	158	155	158	59
Total revenue	$m	19	20	21	22	10
Profitability						
Operating profit before tax	$'000	3 466	3 789	837	- 1 631	511
Operating sales margin	%	15.9	15.7	1.8	- 10.6	0.3
Cost recovery	%	118.9	118.6	101.8	90.5	100.3
Return on assets	%	3.5	2.6	0.5	- 1.0	0.5
Return on equity	%	1.0	0.3	2.8	- 0.9	0.2
Financial management						
Debt to equity	%	2.2	0.0	0.0	0.0	0.0
Debt to total assets	%	2.7	0.0	0.0	0.0	0.0
Total liabilities to equity	%	11.0	8.5	3.7	6.4	1.7
Interest cover	times	n.r.	n.r.	n.r.	n.r.	n.r.
Current ratio	%	244.9	175.4	668.7	303.4	1 293.8
Leverage ratio	%	111.0	108.5	103.7	106.4	101.7
Payments to and from government						
Dividends	$'000	1 000	0	0	0	0
Dividend to equity ratio	%	1.2	0.0	0.0	0.0	0.0
Dividend payout ratio	%	122.5	0.0	0.0	0.0	0.0
Income tax expense	$'000	2 650	3 410	- 3 349	- 242	279
CSO funding	$'000	0	0	0	0	0

a Revaluations resulted in an increase in the value of assets of $13 million, most of which related to channel assets ($11 million). **b** The negative income tax expense reflects an over-provision of $3.5 million for income tax expenses in previous years. **c** The Victorian Channel Authority's current ratio increased significantly in 2001-02, mainly from a reduction in current liabilities relating to trade creditors. In 2002-03, the current ratio fell, with an increase in current liabilities relating to employee entitlements and non-trade creditors. **d** This data is for the nine months to 31 March 2004. The transfer of the former VCA to the PoMC was completed in November 2003. The VRCA began operations on 1 April 2004. **n.r.** Not relevant.

VICTORIAN REGIONAL CHANNELS AUTHORITY — Victoria

The Victorian Regional Channels Authority (VRCA) was established under the *Port Services Act 1995* to manage channels in the port waters of Geelong and overseeing channel operations in the ports of Hastings and Portland. It commenced operations on 1 April 2004.[1] The VRCA is directly responsible for shipping control in the port waters of Geelong and contracts out the shipping control and navigation services for their ports of Portland and Hastings.

The VRCA is subject to pricing regulation, administered by the Essential Services Commission (ESC). The current pricing order, administered in accordance with Section 50 of the *Port Services Act 1995*, will operate until 30 June 2005.[2]

In the last quarter of 2003-04, VRCA recorded a small operating profit of $68 000, with revenues and expenses almost equal at approximately $2 million.[3]

The VRCA has total assets valued at $59 million. The debt to equity and debt to total assets ratios were zero in 2003-04, as the VRCA had no interest bearing liabilities.

The VRCA is required to make tax-equivalent payments under the *State Owned Enterprises Act 1992*. In addition, the VRCA is required to pay dividends to the Victorian Government. A tax benefit of $56 000 was recorded and no dividend was paid and in the last quarter of 2003-04.

1 The Victorian Channels Authority (VCA) commenced operations on 1 March 1996. In July 2003, legislation was passed to create the PoMC. The PoMC took over the land and waterside functions of the Port of Melbourne, including the Melbourne operations of the VCA. The transfer of the former VCA to the PoMC was completed in November 2003 and the VRCA commenced operations on 1 April 2004.

2 In December 1999, a price determination by the Office of the Regulator-General (now the ESC) for the period 2000-01 to 2004-05 required the VCA to reduce average charges by 2.1 per cent annually in real terms.

3 As the VRCA began operations on 1 April 2004, only one quarter of financial performance is being reported.

VICTORIAN REGIONAL CHANNELS AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*[a]
Size						
Total assets	$m					59
Total revenue	$m					2
Profitability						
Operating profit before tax	$'000					68
Operating sales margin	%					- 0.5
Cost recovery	%					99.5
Return on assets	%					0.1
Return on equity	%					0.2
Financial management						
Debt to equity	%					0.0
Debt to total assets	%					0.0
Total liabilities to equity	%					2.2
Interest cover	times					n.r.
Current ratio	%					840.7
Leverage ratio	%					102.2
Payments to and from government						
Dividends	$'000					0
Dividend to equity ratio	%					0.0
Dividend payout ratio	%					0.0
Income tax expense	$'000					- 56
CSO funding	$'000					0

[a] The VRCA commenced operations on 1 April 2004. The 2003-04 figures represent only one quarter.

GLADSTONE PORT AUTHORITY — Queensland

The Gladstone Port Authority (GPA) operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*.[1] The GPA is responsible for the provision of infrastructure for bulk operations as well as pilotage and stevedoring services.

Charges for the GPA's port services are set by the Board.[2] In 2003-04, the GPA recorded total throughput of almost 60 million tonnes. Coal exports accounted for around 71 per cent of port throughput. Other major cargoes included alumina and cement.

Revenue has increased steadily over the reporting period. In 2003-04, total revenue increased by 48 per cent ($61 million) with large asset revaluations. Excluding asset revaluations, operating revenue was slightly lower than in 2002-03. Expenses fell by 3 per cent ($3 million) in comparison to the previous financial year. GPA's profit increased by $65 million (or $1 million if the effect of asset revaluations is excluded) in 2003-04.

Since 1999-00, the GPA's total assets have grown steadily, with asset revaluations and ongoing capital works programs. Recorded assets increased substantially (18 per cent) in 2003-04, mainly attributable to the large asset revaluation increment. This led to improvements in the debt to equity, debt to total assets and total liabilities to equity ratios.

The GPA is required to make both dividend and tax-equivalent payments to the Queensland Government. In 2003-04, GPA provided for a $12.8 million dividend payment and recorded income tax-equivalent expense of $24.6 million.

1 Under the Government Owned Corporations (Central Queensland Ports Authority) Regulation 2004, the Central Queensland Ports Authority - an authority combining the Port of Gladstone and Port Alma - will commence on 1 July 2004.

2 There is no legislative requirement for shareholding ministers to approve charges, although in practice charges are typically put to shareholding ministers for consideration.

GLADSTONE PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*[a]	*2001-02*[b]	*2002-03*	*2003-04*[c]
Size						
Total assets	$m	369	389	410	452	533
Total revenue	$m	86	98	108	127	188
Profitability						
Operating profit before tax	$'000	25 486	16 071	20 801	18 774	83 956
Operating sales margin	%	29.6	15.7	22.1	19.7	49.5
Cost recovery	%	142.0	118.6	128.4	124.6	197.9
Return on assets	%	7.2	4.4	6.2	5.9	19.0
Return on equity	%	3.8	2.9	4.8	5.1	21.0
Financial management						
Debt to equity	%	6.5	4.3	43.3	60.5	45.1
Debt to total assets	%	5.7	3.8	27.1	35.1	29.0
Total liabilities to equity	%	15.5	15.7	64.0	80.9	68.4
Interest cover	times	43.5	25.0	6.2	3.7	9.7
Current ratio	%	141.5	124.5	85.0	89.1	79.1
Leverage ratio	%	115.5	115.7	164.0	180.9	168.4
Payments to and from government						
Dividends	$'000	3 938	13 085	16 874	12 200	12 860
Dividend to equity ratio	%	1.2	4.0	5.8	4.9	4.5
Dividend payout ratio	%	32.5	135.8	119.0	95.0	21.7
Income tax expense	$'000	13 354	6 434	6 625	5 932	24 627
CSO funding	$'000	0	0	0	0	0

a An asset revaluation in January 2001 resulted in an increase of $16 million in the value of assets, mainly relating to channels, plant and equipment. Dividend includes $3.5 million that was attributed to 1999-00 but not provided for. **b** Dividend includes $3.4 million that was attributed to 2000-01 but not provided for. **c** The substantial increase in assets recorded in 2003-04 was caused mainly by large asset revaluation increments.

PORT OF BRISBANE CORPORATION — Queensland

The Port of Brisbane Corporation (PBC) operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. The PBC manages the Port of Brisbane, Brisbane Multimodal Terminal, and the boat harbours of Manly, Scarborough, Cabbage Tree Creek and Gardens Point. It is also a major shareholder in Brisbane Airport Corporation Ltd (BACL).

Charges for the PBC's port services are set by the Board. Although in practice charges are typically put to shareholding ministers for consideration, there is no legislative requirement for shareholding ministers to approve charges. In 2003-04, the PBC's major bulk cargoes included oil and coal. Container throughput was almost 640 000 twenty-foot equivalent units.

Pre-tax operating profit increased by 24 per cent ($8 million) in 2003-04, with a 7 per cent ($8 million) increase in revenue. Contributing to the increase were trade growth, improved rental and interest revenue, and the proceeds from the sale of land not used for core activities.

The PBC's total assets have increased in the reporting period by over 80 per cent in nominal terms. Major contributors to this growth were investment in the BACL[1] and a number of upward revaluations over the reporting period totalling $367 million.[2] The 35 per cent increase in the PBC's assets in 2003-04 is largely attributable to $218 million in upward asset revaluations, which were mainly to recorded land and land improvements values.

Despite a 7 per cent increased debt in 2003-04, the PBC's debt to equity, debt to total assets and total liabilities to equity ratios decreased and interest cover improved with substantial upward asset revaluations. However, the PBC's liquidity, as measured by the current ratio, decreased substantially in 2003-04 with a 36 per cent decrease in current assets and a 29 per cent increase in current liabilities.

The PBC is required to make both dividend and tax-equivalent payments. In 2003-04, PBC provided for a $29 million dividend payment and recorded an income tax-equivalent expense of $12 million.

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1 The PBC invested in BACL in 1996-97. The initial investment was entirely funded through borrowings from the Queensland Treasury Corporation. In 1999-00, the PBC increased its shareholding in the BACL to 38 per cent.

2 Over the reporting period, increases in the value of assets attributable to revaluations — $36 million (1999-00), $63 million (2000-01), $17 million (2001-02), $33 million (2002-03) and $218 million in 2003-04.

PORT OF BRISBANE CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*[a]	*2001-02*[b]	*2002-03*	*2003-04*[c]
Size						
Total assets	$m	737	868	912	988	1 332
Total revenue	$m	84	88	96	109	117
Profitability						
Operating profit before tax	$'000	26 205	19 535	31 806	33 636	41 783
Operating sales margin	%	51.6	44.3	49.7	46.2	48.1
Cost recovery	%	206.6	186.4	198.6	185.9	192.7
Return on assets	%	6.3	5.0	5.4	5.5	5.3
Return on equity	%	4.2	2.1	4.4	4.6	4.2
Financial management						
Debt to equity	%	52.2	60.2	60.8	64.1	44.3
Debt to total assets	%	34.2	38.6	36.3	38.2	33.3
Total liabilities to equity	%	61.0	68.8	71.7	74.6	52.4
Interest cover	times	2.5	2.0	2.9	2.8	3.1
Current ratio	%	94.0	73.9	79.1	186.0	92.2
Leverage ratio	%	161.0	168.8	171.7	174.6	152.4
Payments to and from government						
Dividends	$'000	17 580	13 184	21 980	23 396	28 678
Dividend to equity ratio	%	4.0	2.7	4.2	4.3	4.0
Dividend payout ratio	%	94.8	130.5	95.0	91.8	95.0
Income tax expense	$'000	7 667	9 429	8 669	8 158	11 590
CSO funding	$'000	0	0	0	0	0

a An asset revaluation resulted in an increase in the value of assets by $63 million, mainly relating to the Port of Brisbane Corporation's investment in Brisbane Airport Corporation Ltd. Includes $1.8 million expense relating to redundancy payments. **b** An asset revaluation resulted in an increase in the value of assets by $17 million, mainly relating to land improvements. Revenue includes a profit on the sale of assets of $3.3 million. **c** The 35 per cent increase in the PBC's assets in 2003-04 is largely attributable to $218 million in upward asset revaluations, which were mainly to recorded land and land improves values.

CAIRNS PORT AUTHORITY — Queensland

The Cairns Port Authority operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. It has responsibility for the management and operation of the port of Cairns, Cairns International Airport, and associated land and property. Most port activities such as towage and stevedoring are conducted by private operators.

The Cairns Port Authority's Board sets charges for port services (harbour dues, plant hire and berthage).[1] In 2003-04, total cargo was approximately 1.2 million tonnes, which was slightly lower than the previous year. The major cargoes moving through the port were petroleum products and sugar.

In 2003-04, pre-tax operating profit increased by $5 million, with an upward revaluation of non-current assets. Excluding the effect of asset revaluations in both years, the CPA's profit decreased by $2 million.[2] Revenue increased by 20 per cent in 2003-04 (or 12 per cent without the effect of asset revaluations). Operating expenditure remained stable.

The CPA's assets increased by $61 million (16 per cent) in 2003-04, after a revaluation. This resulted in decreases in the debt to equity and debt to total assets ratios, despite an increase in borrowings of $2 million. The CPA's liquidity, as measured by the current ratio, increased substantially in 2003-04 with the inclusion of $27 million of land held for sale in current assets.

The CPA is required to make dividend and tax-equivalent payments to the Queensland Government. In 2003-04, the CPA provided for a $5 million dividend payment and recorded income tax-equivalent expense of $3 million.

1 There is no legislative requirement for shareholding ministers to approve charges, although in practice charges are typically put to shareholding ministers for consideration.

2 An upward adjustment of $61 million in land values occurred in 2003-04. Of this amount, $21 million was recorded by the CPA as a revenue after reversing debits arising from previous revaluations.

CAIRNS PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*[b]
Size						
Total assets	$m			325	378	439
Total revenue	$m			57	71	85
Profitability						
Operating profit before tax	$'000			12 014	25 218	29 784
Operating sales margin	%			22.4	37.6	39.9
Cost recovery	%			128.9	160.1	166.3
Return on assets	%			4.1	7.6	8.3
Return on equity	%			3.1	7.7	8.4
Financial management						
Debt to equity	%			12.7	20.0	17.1
Debt to total assets	%			10.1	16.4	14.6
Total liabilities to equity	%			26.0	31.4	25.7
Interest cover	times			9.7	17.6	8.4
Current ratio	%			84.9	71.3	227.5
Leverage ratio	%			126.0	131.4	125.7
Payments to and from government						
Dividends	$'000			13 986	6 096	5 190
Dividend to equity ratio	%			5.4	1.1	1.6
Dividend payout ratio	%			176.5	29.0	19.3
Income tax expense	$'000			4 089	4 214	2 922
CSO funding	$'000			0	0	0

a 2001-02 was the first year that the Cairns Port Authority was included in this report. It was established in July 1995 under the *Government Owned Corporations Act 1993*. Dividends include $6.6 million for a dividend under-provision in 2000-01. **b** An upward adjustment of $61 million in land values occurred in 2003-04. The current ratio, increased substantially in 2003-04 with the inclusion of $27 million of land held for sale in current assets.

PORTS CORPORATION OF QUEENSLAND — Queensland

The Ports Corporation of Queensland (PCQ) operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. The PCQ manages the commercial ports of Hay Point, Abbot Point, Lucinda, Mourilyan, Cape Flattery, Weipa, Karumba and Skardon River and also manages five other non-trading ports. It is responsible for maintaining the channels and providing pilotage services. Stevedoring and towage are generally franchised.

Charges for port services are determined by the PCQ Board. There is no legislative requirement for shareholding ministers to approve charges, although in practice charges are typically put to shareholding ministers for consideration. Most of the PCQ's ports specialise in handling bulk cargo such as coal, sugar or bauxite.

In 2003-04, the PCQ ports exported over 107 million tonnes of product, 3 million tonnes higher than the previous year. Pre-tax operating profit was $16.5 million, compared to $16 million in 2002-03. The small reduction in revenue the PCQ experienced in 2003-04 — a result of port pilotage operations being transferred to Maritime Safety Queensland — was offset by a corresponding reduction in expenditure.

PCQ's assets decreased by 4 per cent ($10 million) in 2003-04, mainly caused by a decrease in cash assets associated with capital repayments. The PCQ did not have any outstanding borrowings at the end of 2003-04 and therefore has debt to equity and debt to total asset ratios of zero.

The PCQ is required to make both dividend and tax-equivalent payments. In addition to a tax-equivalent payment of $4 million and a dividend payment of $11 million in 2003-04, the PCQ made a capital repayment of $15 million to the Queensland Government.[1]

1 The capital repayment is the second of three instalments, totalling $45 million, to be returned in 2002-03, 2003-04 and 2004-2005 in return for cancellation of shares.

PORTS CORPORATION OF QUEENSLAND (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			237	234	224
Total revenue	$m			57	37	35
Profitability						
Operating profit before tax	$'000			- 13 544	16 019	16 501
Operating sales margin	%			0.4	37.5	41.6
Cost recovery	%			100.4	159.9	171.3
Return on assets	%			2.4	6.8	7.2
Return on equity	%			- 8.2	7.2	6.5
Financial management						
Debt to equity	%			0.0	0.0	0.0
Debt to total assets	%			0.0	0.0	0.0
Total liabilities to equity	%			16.7	19.2	22.9
Interest cover [b]	times			0.3	n.r.	n.r.
Current ratio	%			309.5	245.7	198.9
Leverage ratio	%			116.7	119.2	122.9
Payments to and from government						
Dividends	$'000			5 780	13 000	11 456
Dividend to equity ratio	%			2.8	3.3	6.0
Dividend payout ratio	%			- 34.5	90.6	92.8
Income tax expense	$'000			3 231	1 675	4 157
CSO funding	$'000			0	0	0

a 2001-02 was the first year that the Ports Corporation of Queensland (PCQ) was monitored. It was established in July 1994 under the *Government Owned Corporations Act 1993*. The dividend of $5.8 million relates to a dividend under-provision in 2000-01. **b** An interest cover ratio is reported in 2001-02 because the PCQ incurred borrowing costs during the year despite the absence of outstanding debt at the end of that financial year. **n.r**. Not relevant.

MACKAY PORT AUTHORITY — Queensland

Mackay Port Authority (MPA) operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. The MPA has responsibility for the management of the port of Mackay and Mackay Airport. The MPA franchises pilotage, towage and stevedoring activities.

Charges for port services are set by the MPA Board. There is no legislative requirement for shareholding ministers to approve charges, although in practice charges are typically put to shareholding ministers for consideration. In 2003-04, the major cargoes moving through the port were sugar and grain.

The MPA's cargoes fell slightly from 2 to 1.9 million tonnes in 2003-04, due in part to a 21 per cent drop in sugar throughput. Despite the decreased throughput, the MPA's revenue increased by approximately 5 per cent through higher charge rates, increased rental revenue and an increase in investment income. Seaport expenses increased slightly, with a write down in inventory values.

Aircraft passenger numbers increased by 21 per cent in 2003-04 leading to a substantial increase in revenue from airport operations. Expenses from airport operations also increased due, in part, to an increase in maintenance and staff costs. Overall the MPA's pre-tax profit increased by 35 per cent ($3 million) in 2003-04.

Assets have remained stable at approximately $160 million since monitoring of the MPA began in 2001-02. The MPA has not carried any debt over the reporting period.

The MPA is required to make tax-equivalent and dividend payments to the Queensland Government. In 2003-04, $146 000 in dividend payments and $1.1 million in tax-equivalent payments were made.

MACKAY PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			158	159	160
Total revenue	$m			12	14	15
Profitability						
Operating profit before tax	$'000			- 513	960	1 300
Operating sales margin	%			- 16.6	- 0.3	0.5
Cost recovery	%			85.8	99.7	100.5
Return on assets	%			- 0.3	0.6	0.8
Return on equity	%			- 0.4	0.3	0.1
Financial management						
Debt to equity	%			0.0	0.0	0.0
Debt to total assets	%			0.0	0.0	0.0
Total liabilities to equity	%			4.6	5.8	6.2
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			784.5	702.1	701.9
Leverage ratio	%			104.6	105.8	106.2
Payments to and from government						
Dividends	$'000			0	459	146
Dividend to equity ratio	%			0.0	0.2	0.1
Dividend payout ratio	%			0.0	94.3	94.8
Income tax expense	$'000			84	473	1 146
CSO funding	$'000			0	0	0

a 2001-02 was the first year that the Mackay Port Authority was monitored. It was established in July 1995 under the *Government Owned Corporations Act 1993*. **n.r.** Not relevant.

TOWNSVILLE PORT AUTHORITY — Queensland

Townsville Port Authority (TPA) operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. The TPA is responsible for the management of Townsville Port.

Charges for the TPA's port services are determined by the Board.[1] In 2003-04, the major cargoes passing through the port included nickel ore, minerals and sugar. Over 10 million tonnes of cargo passed through the TPA in 2003-04.

In 2003-04, the TPA recorded a pre-tax operating profit of almost $3 million following a loss of $236 000 the previous financial year. This result is a combination of a 5 per cent increase in revenue and a 5 per cent decrease in expenses for the financial year.

Total assets increased by $6 million (almost 5 per cent) in 2003-04, with an increase in cash assets and receivables. This increase in current assets resulted in a large increase in the current ratio in 2003-04. The TPA's debt to equity and debt to total assets ratios also improved.

In 2001-02, the TPA paid $23 million to the Queensland Government as part of a capital restructure. The payment was financed by a loan from the Queensland Treasury Corporation.

The TPA is required to make tax-equivalent and dividend payments to the Queensland Government. It made a dividend payment of $1.2 million — the first since monitoring of the TPA began — and a tax-equivalent payment of $1.4 million in 2003-04.

1 There is no legislative requirement for shareholding ministers to approve charges, although in practice charges are typically put to shareholding ministers for consideration.

TOWNSVILLE PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			131	127	133
Total revenue	$m			25	26	27
Profitability						
Operating profit before tax	$'000			1 156	- 236	2 651
Operating sales margin	%			8.4	3.1	13.2
Cost recovery	%			109.2	103.2	115.2
Return on assets	%			1.7	0.8	2.9
Return on equity	%			0.1	- 0.8	1.2
Financial management						
Debt to equity	%			20.7	19.3	16.4
Debt to total assets	%			16.4	15.2	13.6
Total liabilities to equity	%			26.7	25.0	23.2
Interest cover	times			2.0	0.8	3.3
Current ratio	%			147.5	104.3	143.6
Leverage ratio	%			126.7	125.0	123.2
Payments to and from government						
Dividends	$'000			0	0	1 170
Dividend to equity ratio	%			0.0	0.0	1.1
Dividend payout ratio	%			0.0	0.0	95.0
Income tax expense	$'000			1 065	585	1 419
CSO funding	$'000			0	0	0

[a] 2001-02 was the first year that the Townsville Port Authority was monitored. It was established in July 1995 under the *Government Owned Corporations Act 1993*.

FREMANTLE PORT AUTHORITY — Western Australia

The Fremantle Port Authority (FPA) operates under the *Port Authorities Act 1999*. It provides and maintains port infrastructure and port services, including ship scheduling, port communications and mooring. The FPA contracts pilotage, towage and stevedoring to the private sector.

Charges are set by the FPA Board and are subject to approval by the Minister. There was no change in nominal charges in 2003-04. The FPA's pre-tax profit decreased slightly for the year, caused by a 1 per cent increase in expenses.

Major cargoes moving through the port were petroleum products and grain. In 2003-04, container throughput grew by 8 per cent to 466 000 twenty-foot equivalent units.

Total assets increased in value by 6 per cent ($10 million) in 2003-04, with a large increase in current assets. As a consequence, the FPA's debt to equity, debt to total assets and current ratios improved in 2003-04.

The FPA is required to make both income tax-equivalent and dividend payments to the WA Government. In 2003-04, the FPA provided for a $6 million dividend payment and recorded an income tax-equivalent expense of $6 million. The dividends in 2001-02, 2002-03 and 2003-04 include amounts for 'Government efficiency dividends' that are not related to profit.

FREMANTLE PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*[b]	*2002-03*[c]	*2003-04*[d]
Size						
Total assets	$m	120	132	150	156	166
Total revenue	$m	60	54	63	76	77
Profitability						
Operating profit before tax	$'000	14 768	15 637	19 462	17 779	17 634
Operating sales margin	%	29.2	29.7	32.1	25.1	22.6
Cost recovery	%	149.9	142.2	147.2	133.6	129.1
Return on assets	%	15.6	13.5	14.9	13.0	11.9
Return on equity	%	12.4	12.1	16.3	13.1	11.3
Financial management						
Debt to equity	%	22.9	26.8	32.6	25.9	24.5
Debt to total assets	%	15.1	17.1	21.1	16.7	16.0
Total liabilities to equity	%	55.8	63.5	64.3	58.4	58.1
Interest cover	times	5.2	12.5	14.4	9.1	12.8
Current ratio	%	105.5	150.0	160.4	107.9	118.9
Leverage ratio	%	155.8	163.5	164.3	158.4	158.1
Payments to and from government						
Dividends	$'000	1 750	1 907	6 798	5 155	5 760
Dividend to equity ratio	%	2.5	2.4	7.9	5.4	5.7
Dividend payout ratio	%	19.9	20.0	48.7	41.5	50.0
Income tax expense	$'000	5 989	6 102	5 496	5 358	6 115
CSO funding	$'000	0	0	0	0	0

a Includes abnormal revenue of $4.3 million relating to land transfers and an abnormal expense of $5.2 million as a result of a revaluation of non-current assets using deprival methodology. **b** The dividend includes $413 000 for a 'Government efficiency dividend' that is not related to profit. **c** The dividend includes $438 000 for a 'Government efficiency dividend' that is not related to profit. **d** The dividend includes $449 000 for a 'Government efficiency dividend' that is not related to profit.

BUNBURY PORT AUTHORITY — Western Australia

Bunbury Port Authority (BPA) operates under the *Port Authorities Act 1999*. It owns and manages port facilities and provides pilotage services. Stevedoring and towage services are franchised.

Charges are set by the BPA Board and are subject to approval by the Minister. An increase in charges on port infrastructure was approved in 2003-04.

BPA handled 11.7 million tonnes of cargo in 2003-04, 2.6 per cent lower than the previous financial year. In 2003-04, alumina accounted for 72 per cent of total port throughput by tonnage. Other major cargoes included caustic soda, woodchips and mineral sands.

Pre-tax operating profit decreased by 14 per cent ($800 000) to $4.8 million in 2003-04, with a 2 per cent ($300 000) decrease in revenue and a 5 per cent ($500 000) increase in expenses. The reduction in pre-tax profit was caused mainly by a reduction in trade and an under provision of depreciation for the capitalised dredging maintenance in previous financial years.

The value of BPA's assets have remained stable throughout the reporting period. Its debt to equity and debt to total assets ratios have declined, with a steady decrease in the level of debt since 1999-00.

BPA is required to make dividend and income tax-equivalent payments to the WA Government. In 2003-04, BPA provided for a $1.5 million dividend payment and recorded income tax-equivalent expense of $1.5 million.

BUNBURY PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	94	99	99	100	100
Total revenue	$m	14	15	14	16	16
Profitability						
Operating profit before tax	$'000	4 889	6 076	4 768	5 623	4 824
Operating sales margin	%	41.0	45.5	35.7	37.5	31.4
Cost recovery	%	176.8	186.7	164.2	168.9	145.8
Return on assets	%	6.4	7.4	5.7	6.6	5.7
Return on equity	%	4.5	5.8	4.2	4.8	4.2
Financial management						
Debt to equity	%	24.1	21.8	20.2	18.2	17.9
Debt to total assets	%	19.2	16.6	15.4	14.7	14.1
Total liabilities to equity	%	27.1	34.7	31.3	24.6	26.9
Interest cover	times	5.8	6.5	6.6	7.0	6.5
Current ratio	%	470.6	391.4	354.4	428.2	547.5
Leverage ratio	%	127.1	134.7	131.3	124.6	126.9
Payments to and from government						
Dividends	$'000	951	1 276	1 582	1 882	1 525
Dividend to equity ratio	%	1.3	1.7	2.1	2.4	1.9
Dividend payout ratio	%	30.0	30.0	50.0	50.0	46.1
Income tax expense	$'000	1 720	1 823	1 604	1 859	1 517
CSO funding	$'000	0	0	0	0	0

[a] The dividend of $951 000 in 1999-00 was later revised to $634 000 to reflect the premature application of a dividend policy in 1999-00 applying to Western Australia port government trading enterprises for 2000-01. If the revised dividend was applied to 1999-00, the dividend to equity and dividend payout ratios for 1999-00 would have been 0.9 per cent and 23.6 per cent respectively.

PORT HEDLAND PORT AUTHORITY — Western Australia

The Port Hedland Port Authority (PHPA) operates under the *Port Authorities Act 1999*. It manages port facilities including wharves and storage areas, and provides pilotage services. Stevedoring, towage and lineboat services are franchised.

Charges are set by the PHPA Board and are subject to approval by the Minister. PHPA's charges did not increase in 2003-04, although charges were increased by 7.9 per cent in 2002-03. In real terms, PHPA's charges have fallen 24 per cent since 1999-00.

In 2003-04, ship-based charges accounted for around 54 per cent of revenue, with most of the remainder derived from cargo-based charges (30 per cent) and lease rentals (11 per cent). The major expenses for the PHPA in 2003-04 were pilotage transit and hydrology services (31 per cent) and maintenance (22 per cent).

Pre-tax operating profit decreased 24 per cent ($721 000) in 2003-04, as a result of a 5 per cent increase in expenses.[1] PHPA's total throughput for 2003-04 was almost 90 million tonnes. Iron ore accounted for around 94 per cent of port throughput by tonnage. The other main cargoes were salt and hot briquetted iron.

The PHPA operates debt free. The PHPA's liquidity, as measured by the current ratio, decreased in 2003-04, with an increase in current liabilities relating to trade creditors.

The PHPA is required to make tax-equivalent and dividend payments to the WA Government. In 2003-04, PHPA provided for a $1 million dividend payment and recorded an income tax-equivalent expense of $1 million.

1 The Government Finance Statistics (GFS) data used for this report recorded PHPA's 2003-04 revenue as $1.6 million lower than the figure reported in PHPA's annual report. The annual report therefore recorded a 5 per cent increase in profit for 2003-04. This discrepancy arises because of differences between the recorded values for charges, lease rentals and other revenues in the GFS and annual report (see chapter 3).

PORT HEDLAND PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			44	46	50
Total revenue	$m			13	15	15
Profitability						
Operating profit before tax	$'000			2 617	2 952	2 231
Operating sales margin	%			17.5	16.1	11.3
Cost recovery	%			121.1	119.2	112.7
Return on assets	%			6.0	6.6	4.7
Return on equity	%			4.8	5.3	2.7
Financial management						
Debt to equity	%			0.0	0.0	0.0
Debt to total assets	%			0.0	0.0	0.0
Total liabilities to equity	%			9.9	14.6	10.2
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			378.5	285.7	256.9
Leverage ratio	%			109.9	114.6	110.2
Payments to and from government						
Dividends	$'000			949	1 043	1 119
Dividend to equity ratio	%			2.4	1.3	2.6
Dividend payout ratio	%			50.0	50.0	96.4
Income tax expense	$'000			718	865	1 070
CSO funding	$'000			0	0	0

a 2001-02 was the first year that the Port Hedland Port Authority was monitored. It was established under the *Port Authorities Act 1999*. **n.r.** Not relevant.

ALBANY PORT AUTHORITY — Western Australia

Albany Port Authority (APA) operates under the *Port Authorities Act 1999*. The APA manages port facilities including wharves, and provides pilotage services. Stevedoring, mooring and cold storage services are franchised.

Charges are set by the APA Board and are subject to approval by the Minister. In 2003-04, APA's total throughput was 45 per cent greater than the previous year. The main cargoes moving through the port were grain, silica sand and woodchips.

The APA recorded a pre-tax profit of $2.3 million in 2003-04. A 40 per cent ($2 million) increase in revenue and a 30 per cent ($2 million) decrease in expenses reversed a loss of $1.4 million in 2002-03, when expenses were unusually high due to a write-down of assets for unexpected costs. Had these additional costs not occurred in 2002-03, profit would have grown by $1.9 million in 2003-04.

The APA's debt to equity and debt to total assets ratios decreased in 2003-04, caused by a combination of a 16 per cent ($2 million) decrease in debt and a 3 per cent ($1 million) increase in total assets.

The APA is required to make tax-equivalent and dividend payments to the WA Government. In 2003-04, APA recorded an income tax-equivalent expense of $700 000 but did not make a dividend payment.

ALBANY PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*
Size						
Total assets	$m			42	38	39
Total revenue	$m			4	5	7
Profitability						
Operating profit before tax	$'000			- 36	- 1 463	2 306
Operating sales margin	%			1.4	- 17.7	42.9
Cost recovery	%			101.4	84.9	175.1
Return on assets	%			0.7	- 1.4	8.0
Return on equity	%			0.3	- 9.8	7.5
Financial management						
Debt to equity	%			59.2	72.6	54.0
Debt to total assets	%			31.8	37.3	32.5
Total liabilities to equity	%			86.0	86.7	68.1
Interest cover	times			0.9	- 0.6	3.8
Current ratio	%			43.6	32.1	48.5
Leverage ratio	%			186.0	186.7	168.1
Payments to and from government						
Dividends	$'000			0	0	0
Dividend to equity ratio	%			0.0	0.0	0.0
Dividend payout ratio	%			0.0	0.0	0.0
Income tax expense	$'000			- 99	643	653
CSO funding	$'000			0	0	0

a 2001-02 was the first year that the Albany Port Authority was monitored. It was established under the *Port Authorities Act 1999*. **b** Includes an extraordinary write-down of assets totalling $1.8 million.

DAMPIER PORT AUTHORITY — Western Australia

Dampier Port Authority (DPA) operates under the *Port Authorities Act 1999*. The DPA manages port facilities including wharves and storage areas. Stevedoring, pilotage and towage services are franchised.

In 2003-04, DPA's total throughput reached 88.8 million tonnes, marginally below the previous year's tonnage of 92.3 million tonnes. The reduced level of trade reflected the impact of a cyclone and the disruption to normal operations at Hamersley Iron due to new expansion works. Iron ore accounted for around 80 per cent of port throughput by tonnage in 2003-04. The other main cargoes moving through the port were liquefied natural gas, condensate and salt. Charges are set by the DPA Board and are subject to approval by the Minister. Port dues were increased by 10 per cent on 1 July 2003.

The DPA's pre-tax operating profit increased by 43 per cent ($153 000) to $513 000 in 2003-04, achieved mainly by a 4 per cent ($183 000) reduction in operating expenses.

Assets increased by 87 per cent ($20 million) in 2003-04. This large increase was the result of an increase in the recorded value of DPA's property plant and equipment, after $25 million was spent on port expansion.

The DPA operated debt free in 2001-02 and 2002-03, but it had $16 million of debt in 2003-04. The total loan facility of $75 million is expected to be fully drawn in 2004-05. The DPA's liquidity, as measured by the current ratio, decreased substantially in 2003-04. This can be attributed to an increase in debt — to fund the port expansion project — an increase in accounts payable and a $5 million decrease in cash reserves.

The DPA is required to make tax-equivalent and dividend payments to the WA Government. In 2003-04, the DPA recorded an income tax-equivalent expense of $27 000 and provided for a $230 000 dividend payment[1]. The dividend included a $24 000 'efficiency dividend' that was not related to the DPA's profitability.

1 In 2002-03, the operating dividend was found to have been overestimated by $37 000 after a capital gains liability was realised on the sale of three Authority houses. This over-statement was adjusted against the 2003-04 operating dividend.

DAMPIER PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*[b]	*2003-04*[b]
Size						
Total assets	$m			22	23	43
Total revenue	$m			3	5	5
Profitability						
Operating profit before tax	$'000			- 269	360	513
Operating sales margin	%			- 13.4	3.4	7.5
Cost recovery	%			88.2	103.5	108.2
Return on assets	%			- 1.2	1.6	1.5
Return on equity	%			- 0.9	1.2	2.2
Financial management						
Debt to equity	%			0.0	0.0	71.5
Debt to total assets	%			0.0	0.0	47.3
Total liabilities to equity	%			3.5	8.1	96.0
Interest cover	times			n.r.	n.r.	n.r.
Current ratio	%			692.2	368.5	29.0
Leverage ratio	%			103.5	108.1	196.0
Payments to and from government						
Dividends	$'000			96	150	230
Dividend to equity ratio	%			0.4	0.7	1.1
Dividend payout ratio	%			- 48.5	59.8	47.3
Income tax expense	$'000			- 71	109	27
CSO funding	$'000			0	0	0

a 2001-02 was the first year that the Dampier Port Authority was monitored. It was established under the *Port Authorities Act 1999*. **b** In 2002-03, the operating dividend was found to have been overestimated by $37 000 after a capital gains liability was realised on the sale of three Authority houses. This overstatement was adjusted against the 2003-04 operating dividend. **n.r.** Not relevant.

GERALDTON PORT AUTHORITY — Western Australia

Geraldton Port Authority (GPA) operates under the *Port Authorities Act 1999*. It manages port facilities including wharves and storage areas, and provides pilotage and mooring services. Stevedoring and towage services are franchised.[1]

Total port throughput was 4.36 million tonnes in 2003-04, which was 74 per cent higher than the previous year. The main cargoes moving through the port were grains and minerals.

Charges are set by the GPA Board and are subject to approval by the Minister. Upon completion of the Port Enhancement Project (PEP), a $2 per tonne 'port enhancement charge' was introduced. This charge was introduced to finance the interest and capital repayments to WA Treasury Corporation for the $103 million cost of the project. The PEP involved deepening the harbour basin and deepening and widening shipping access channels to allow deeper draft access to the port.

Despite a 48 per cent ($5 million) increase in expenses,[2] GPA's pre-tax operating profit improved by almost $4 million in 2003-04, as a result of a 90 per cent ($9 million) increase in revenue. The improved revenue was mainly achieved by higher earnings from charges on ships and charges on cargo as well as the introduction of the new 'port enhancement charge'.

In 2003-04, total assets increased by $23 million (18 per cent), following the completion of the PEP. Debt also increased substantially, reflecting increased borrowing to fund the PEP. These developments have had a significant effect on the GPA's financial management indicators since 2001-02.

GPA is required to make tax-equivalent and dividend payments to the WA Government. In 2003-04, GPA recorded an income tax-equivalent expense of $318 000 and provided for a $129 000 dividend payment. The dividend included a $126 000 'efficiency dividend' that was not related to GPA's profitability.

1 The GPA issues non-exclusive licences to stevedores operating in the port. Under the licences, the GPA monitors tariffs, manning levels, operational procedures, continuity of service, customer satisfaction and improvement in working practices.

2 The Government Finance Statistics (GFS) data used for this report recorded GPA's 2003-04 expenses as $3 million lower than the figure reported in GPA's annual report. The annual report therefore recorded a profit figure which was $3 million lower than the GFS data. This discrepancy arises largely because of differences in the recorded values for borrowing costs.

GERALDTON PORT AUTHORITY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			36	130	153
Total revenue	$m			10	10	19
Profitability						
Operating profit before tax	$'000			25	103	3 967
Operating sales margin	%			5.4	6.3	44.9
Cost recovery	%			105.7	106.7	181.3
Return on assets	%			2.1	0.9	6.0
Return on equity	%			0.0	0.5	16.3
Financial management						
Debt to equity	%			46.2	441.2	504.1
Debt to total assets	%			28.2	114.1	83.2
Total liabilities to equity	%			63.6	505.6	556.7
Interest cover	times			1.0	1.2	1.9
Current ratio	%			131.2	76.0	128.7
Leverage ratio	%			163.6	605.7	656.7
Payments to and from government						
Dividends	$'000			0	126	129
Dividend to equity ratio	%			0.0	0.3	0.6
Dividend payout ratio	%			0.0	117.8	3.5
Income tax expense	$'000			19	- 4	318
CSO funding	$'000			0	0	0

[a] The Geraldton Port Authority was established under the *Port Authorities Act 1999*. 2001-02 was the first year that it was monitored. Actual return on equity was 0.03 per cent.

BURNIE PORT CORPORATION — Tasmania

Burnie Port Corporation (BPC) was established on 30 July 1997 under the *Port Companies Act 1997* and is subject to the *Corporations Act 2001* (Cwlth). The BPC owns and manages port and cold storage facilities, and provides pilotage services.

Charges are set by the BPC Board. Throughput for the year was 4.2 million tonnes of cargo, an increase of almost 8 per cent from 2002-03. In 2003-04, the main cargoes passing through the port were woodchips, logs, minerals and paper.

Pre-tax operating profit increased by 57 per cent ($638 000) to $1.8 million in 2003-04, with a 10 per cent increase in revenue. This increase in revenue was achieved principally from increased service revenue of $551 000.

Total assets increased by 3 per cent ($1 million) in 2003-04. Debt levels have fallen each year since 1999-00. The decline in debt has contributed to a fall in the debt to equity ratio and a rise in interest cover.

The BPC is required to make both tax-equivalent and dividend payments to the Tasmanian Government. In 2003-04, BPC paid a dividend of $383 000.[1] There has been no income tax expense or provision for income tax over the reporting period because of carried forward tax losses.

[1] At the Board meeting held on 30 August 2004, the directors recommended a dividend of $617 000 for 2003-04. The $383 000 paid in 2003-04 was recommended in respect of the previous year.

BURNIE PORT CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	41	38	41	38	39
Total revenue	$m	15	12	11	11	12
Profitability						
Operating profit before tax	$'000	- 2 584	- 2 536	1 377	1 126	1 764
Operating sales margin	%	- 10.4	- 12.0	16.8	11.8	14.8
Cost recovery	%	130.2	107.2	120.1	113.4	117.4
Return on assets	%	- 2.5	- 2.3	5.8	4.7	5.9
Return on equity	%	- 12.8	- 14.4	8.2	6.4	9.4
Financial management						
Debt to equity	%	99.7	95.1	75.3	53.8	36.3
Debt to total assets	%	43.3	39.0	32.5	24.5	18.2
Total liabilities to equity	%	118.4	135.0	140.2	109.8	102.6
Interest cover	times	- 0.7	- 0.6	2.5	2.5	4.3
Current ratio	%	101.5	206.6	353.7	352.5	242.6
Leverage ratio	%	218.4	235.0	240.2	209.8	202.6
Payments to and from government						
Dividends	$'000	0	0	0	270	383
Dividend to equity ratio	%	0.0	0.0	0.0	1.5	2.0
Dividend payout ratio	%	0.0	0.0	0.0	24.0	21.7
Income tax expense	$'000	0	0	0	0	0
CSO funding	$'000	0	0	0	0	0

a Includes an abnormal expense of $5.1 million due to an asset devaluation. **b** Includes an abnormal expense of $2.6 million due to an asset devaluation. **c** The Burnie Port Corporation Board recommended a dividend payment of $225 000. However, it was not provided for in the financial statements. If this amount had been provided for, the dividend to equity ratio would have been 1.3 per cent and the dividend payout ratio would have been 16.3 per cent. **d** In 2002-03, an *ex-gratia* dividend payment of $270 000 (revised from $225 000), was paid out of retained profits. This payment relates to 2001-02, but was not provided for in the financial statements for that year. **e** At the Board meeting held on 30 August 2004, the directors recommended a dividend of $617 000 for 2003-04. The $383 000 paid in 2003-04 was recommended in respect of the profits achieved in 2002-03.

HOBART PORTS CORPORATION — Tasmania

Hobart Ports Corporation (HPC) was established on 30 July 1997 under the *Port Companies Act 1997* and is subject to the *Corporations Act 2001* (Cwlth). The HPC owns and operates port facilities in Hobart, Triabunna, Port Huon, Strahan, Stanley and King Island. It also provides stevedoring and plant hire services in several other Tasmanian and South Australian ports.[1] The HPC owns 98 per cent of the Hobart International Airport Pty Ltd (HIA) and 100 per cent of King Island Ports Corporation.[2]

Charges are set by the HPC's Board. In 2003-04, total port trade was over 3 million mass tonnes. The main bulk cargoes were zinc and petroleum products.

In 2003-04 the HPC's profit rose by only 1 per cent ($56 000), with a 6 per cent (almost $2 million) increase in expenses counteracting a 5 per cent (almost $2 million) increase in revenue.

The HPC's assets increased by 46 per cent ($35 million) and debt increased by $28 million in 2003-04. These major balance sheet changes primarily reflect HIA becoming a wholly owned subsidiary of HPC on 30 June 2004.

The HPC is required to make tax-equivalent and dividend payments. In 2003-04, the HPC recorded an income tax-equivalent expense of $1.3 million and paid a $875 000 dividend.[3]

1 During 2001-02, the HPC formed a wholly-owned subsidiary — Risdon Port Services Pty Ltd — to provide stevedoring and maintenance services to Pasminco Ltd.

2 Despite having a 98 per cent ownership share in the HIA, it's operations were not consolidated in the HPC's 2003-04 accounts because a joint venture agreement limited its capacity to make decisions over financial and operating policies. The HPC's interest in the HIA was accounted for using the 'equity method', whereby the initial investment in the HIA is recognised as an asset and adjustments are made to its value to reflect the HPC's share of profits or losses in each subsequent year. On 30 June 2004, HPC acquired the remaining HIA shares, HIA therefore became a wholly-owned subsidiary of the HPC.

3 A dividend of $1 million was recommended for 2003-04. The $875 000 paid in 2003-04 was recommended in respect of the previous year.

HOBART PORTS CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*[b]	*2003-04*[c]
Size						
Total assets	$m	64	70	73	76	111
Total revenue	$m	17	22	31	36	38
Profitability						
Operating profit before tax	$'000	765	1 220	5 285	6 122	6 178
Operating sales margin	%	7.8	7.9	18.5	18.3	17.4
Cost recovery	%	108.5	108.6	122.8	122.4	121.0
Return on assets	%	2.3	2.8	8.4	9.1	7.2
Return on equity	%	1.7	1.5	7.5	8.8	8.6
Financial management						
Debt to equity	%	20.8	29.8	24.9	22.2	68.5
Debt to total assets	%	15.9	21.4	17.7	16.4	43.3
Total liabilities to equity	%	33.5	45.6	43.9	37.8	87.8
Interest cover	times	2.1	2.8	8.8	10.3	11.7
Current ratio	%	146.9	100.7	128.4	186.1	218.0
Leverage ratio	%	133.5	145.6	143.9	137.8	187.8
Payments to and from government						
Dividends	$'000	540	540	975	0	875
Dividend to equity ratio	%	1.2	1.1	2.0	0.0	0.0
Dividend payout ratio	%	67.4	76.9	26.4	0.0	17.8
Income tax expense	$'000	- 37	518	1 590	1 452	1 271
CSO funding	$'000	0	0	0	0	0

a In 1999-00, the negative tax-equivalent payment was mainly the result of the restatement of deferred tax balances following a reduction in the company tax rate. **b** In 2002-03, the Hobart Ports Corporation adopted accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*. Under this standard dividends are recognised at the time they are declared, determined or publicly recommended. In previous years, dividend payments were recognised in the financial year to which they related. As a result no provision for dividend was recognised for 2002-03 (see chapter 3). **c** A dividend of $1 million was recommended for 2003-04. The $875 000 paid in 2003-04 was recommended in respect of the previous year.

PORT OF DEVONPORT CORPORATION — Tasmania

The Port of Devonport Corporation (PDC), formerly the Port of Devonport Authority, was established on 30 July 1997 under the *Port Companies Act 1997* and is subject to the *Corporations Act 2001* (Cwlth). The PDC's activities cover the management of port facilities, cold storage operations and the ownership and management of an airport.

Charges are set by the PDC Board. In 2003-04, the port handled 3.2 million mass tonnes of cargo, representing a 1.3 per cent increase over the previous financial year's figure. Port operations accounted for 67 per cent of total revenue. Cold storage and airport operations accounted for around 17 per cent and 10 per cent of total revenue respectively.

Pre-tax operating profit increased by over $1 million (40 per cent) in 2003-04, with revenue growth of 9 per cent and expenses reducing by 3 per cent. The increase in port revenue was primarily due to the introduction of the third TT-line ferry. Port expenditure was reduced mainly by a reduction in maintenance costs.

The value of assets increased by $8 million (17 per cent) in 2003-04 and the level of debt increased by $5 million (61 per cent). The increase in the value of assets is mainly attributable to capital expenditure on berth improvements and modifications to a passenger vehicle yard.

The PDC is required to make tax-equivalent and dividend payments to the Tasmanian Government. The PDC paid income tax of $1.1 million and a dividend of over $900 000 in 2003-04. [1]

[1] A dividend of $1.5 million was recommended for 2003-04. The $900 000 paid in 2003-04 was recommended in respect of the previous year.

PORT OF DEVONPORT CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	46	45	45	47	55
Total revenue	$m	10	11	10	11	12
Profitability						
Operating profit before tax	$'000	2 069	1 068	499	2 530	3 553
Operating sales margin	%	21.8	9.0	5.2	23.7	31.9
Cost recovery	%	127.8	109.9	105.4	131.0	146.8
Return on assets	%	5.9	3.5	2.3	6.6	8.1
Return on equity	%	3.6	0.6	0.5	4.7	6.7
Financial management						
Debt to equity	%	22.2	22.0	21.7	20.9	32.2
Debt to total assets	%	16.7	16.6	16.6	16.3	23.6
Total liabilities to equity	%	33.5	32.0	30.4	31.4	47.0
Interest cover	times	4.3	3.0	2.0	6.0	7.1
Current ratio	%	322.7	336.0	675.4	436.4	278.4
Leverage ratio	%	133.5	132.0	130.4	131.4	147.0
Payments to and from government						
Dividends	$'000	925	108	0	78	902
Dividend to equity ratio	%	2.7	0.3	0.0	0.2	2.5
Dividend payout ratio	%	75.8	50.0	0.0	4.7	37.0
Income tax expense	$'000	849	852	343	869	1 116
CSO funding	$'000	0	0	0	0	0

a Dividend includes $304 000 paid in relation to the previous year. **b** Includes a net loss of $1.6 million on the sale of assets. **c** A dividend of $78 000 was declared by the Board subsequent to the end of the financial year but not included in the financial accounts. If this had been provided for in the accounts for 2001-02, the dividend to equity ratio would have been 0.2 per cent and the dividend payout ratio would have been 49.3 per cent. **d** In 2001-02, the PDC adopted accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*. Under this standard, dividends are recognised at the time they are declared, determined or publicly recommended. In previous years, dividend payments were recognised in the financial year to which they related. A dividend of $902 000 was declared by the Board subsequent to the end of the 2002-03 financial year and therefore not included in the 2002-03 financial accounts. **e** A dividend of $1.5 million was recommended for 2003-04. The $900 000 paid in 2003-04 was recommended in respect of the previous year.

PORT OF LAUNCESTON PTY LTD — Tasmania

Port of Launceston Pty Ltd was established on 30 July 1997 under the *Port Companies Act 1997* and is subject to the *Corporations Act 2001* (Cwlth). The Port of Launceston provides pilotage services and port facilities, including wharves and equipment.

Charges are set by the Port of Launceston Board. In 2003-045 million tonnes of cargo passed through the port, almost the same as the previous year. The major cargoes traded through the port are woodchips, metals, minerals and containerised cargoes.

Pre-tax operating profit rose by 3 per cent ($36 000) in 2003-04, with a 2 per cent ($205 000) increase in revenue essentially offset by a 2 per cent ($169 000) increase in expenses.

The value of the Port of Launceston's total assets have remained stable since 1999-00, while its level of debt has fallen by 25 per cent ($3.5 million). This resulted in a decline in the Port of Launceston's debt to total asset ratio over the reporting period.

The Port of Launceston is required to make tax-equivalent and dividend payments to the Tasmanian Government. In 2003-04, the Port of Launceston recorded income tax-equivalent expense of $330 000 and made a $475 000 dividend payment for the previous year. [1]

[1] The dividend recommended for the year ended 30 June 2004 will be recorded in the Port of Launceston's 2004-05 financial statements.

PORT OF LAUNCESTON PTY LTD (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	45	43	44	44	44
Total revenue	$m	10	9	9	10	10
Profitability						
Operating profit before tax	$'000	1 432	462	942	1 097	1 133
Operating sales margin	%	24.1	14.8	19.7	19.2	18.9
Cost recovery	%	105.6	117.4	124.5	123.8	123.3
Return on assets	%	5.8	3.5	4.3	4.5	4.5
Return on equity	%	4.6	0.8	1.9	2.7	3.0
Financial management						
Debt to equity	%	52.9	29.3	43.3	39.4	39.0
Debt to total assets	%	31.0	27.7	26.1	23.9	23.8
Total liabilities to equity	%	69.3	4.1	67.6	64.2	63.5
Interest cover	times	2.2	1.4	2.0	2.3	2.4
Current ratio	%	185.5	161.9	170.7	147.6	150.0
Leverage ratio	%	169.3	104.1	167.6	164.2	163.5
Payments to and from government						
Dividends	$'000	0	939	0	662	475
Dividend to equity ratio	%	0.0	2.8	0.0	2.5	1.8
Dividend payout ratio	%	0.0	333.6	0.0	90.8	59.2
Income tax expense	$'000	259	180	298	370	330
CSO funding	$'000	0	0	0	0	0

a Includes abnormal revenue of $2 million, mainly the result of the settlement of a writ issued by the Port of Launceston against Coastal Express Line for the termination of a lease. **b** The dividend includes $604 000 that was attributed to 1999-00 but not provided for in that year. **c** Dividend payments totalling $335 000 relating to 2000-01 were provided for in 2001-02. **d** In 2001-02, the Port of Launceston adopted accounting standard AASB 1044 *Provisions, Contingent Liabilities and Contingent Assets*. Under this standard dividends are recognised at the time they are declared, determined or publicly recommended (see chapter 3 for details). **e** The $475 000 dividend paid in 2003-04 was recommended in respect of the previous year. The dividend recommended for the year ended 30 June 2004 will be recorded in the Port of Launceston's 2004-05 financial statements.

DARWIN PORT CORPORATION — Northern Territory

The Darwin Port Corporation (DPC) was established under the *Darwin Port Corporation Act 1999*.[1] The DPC is responsible for the management of a portfolio of marine facilities, pilotage services and the provision of services such as reception facilities for cruise and naval vessels.

The DPC operates the East Arm and City wharves in the Port of Darwin and offers facilities and services to commercial shipping and non-trading vessels. In 2003-04, the major cargoes passing through the port included petroleum products, metal products and livestock. Charges for port services are set by the DPC Board and are subject to approval by the Minister.

Total revenue has remained stable over most of the reporting period. The significant increase in revenue in 1999-00 was mainly due to $21 million in proceeds from the sale of non-current assets. The DPC has made several downward revaluations of its assets during the reporting period, which have adversely affected profitability. The adjustments were $2 million, $61 million, $7 million, $35 million, $44 million and, in 2003-04, $18 million.

The NT Department of Infrastructure, Planning and Environment is funding the construction of new facilities at East Arm wharf. Work in progress on the East Arm Wharf is transferred to the DPC annually and treated as an equity injection. In 2001-02, 2002-03 and 2003-04 the values of assets transferred to DPC were written down to zero as no extra income is expected to be accrued from these assets.

The DPC undertook debt restructuring in 1999-00, reducing its debt levels by transferring land and buildings valued at $21 million to the NT Government in exchange for the retirement of an equivalent level of debt.

The DPC is required to make tax-equivalent and dividend payments. Dividend payments are set at 50 per cent of operating profit after tax. No dividend has been paid in the reporting period.

In 2003-04, the DPC received a total of $4.6 million in CSO funding to cover costs associated with small craft services, tourism and real estate, cruise and defence facilities, the Fort Hill Wharf, the NT Express, dredging of the City Wharves and the East Arm Port development.[2]

1 Prior to September 1999, the DPC's operations were carried out by the Darwin Port Authority.

2 This CSO addressed debt servicing and costs incurred in the duplication of services at DPC's current operations and at the new wharf.

DARWIN PORT CORPORATION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	68	62	55	57	62
Total revenue	$m	38	15	17	19	19
Profitability						
Operating profit before tax	$'000	- 47 685	- 5 202	- 33 072	- 43 458	- 12 961
Operating sales margin	%	- 117.5	- 20.5	- 188.7	- 221.6	- 64.7
Cost recovery	%	174.4	83.0	34.6	31.1	60.7
Return on assets	%	- 43.4	- 3.8	- 52.0	- 73.2	- 18.5
Return on equity	%	- 97.7	- 21.1	- 198.6	- 272.5	- 63.3
Financial management						
Debt to equity	%	132.4	173.1	227.5	187.7	142.7
Debt to total assets	%	34.2	51.9	57.1	59.5	55.2
Total liabilities to equity	%	158.3	218.0	275.8	220.7	169.4
Interest cover	times	- 12.5	- 0.9	- 11.6	- 17.8	- 5.9
Current ratio	%	244.2	180.9	201.6	429.4	418.2
Leverage ratio	%	258.3	318.0	375.8	320.7	269.4
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0.0	0.0	0.0	0.0	0.0
Dividend payout ratio	%	0.0	0.0	0.0	0.0	0.0
Income tax expense	$'000	1 234	-362	879	- 865	-18
CSO funding	$'000	5 436	3 400	4 743	6 844	4 592

a Operating profit decreased by $61 million resulting from a revaluation of assets. Revenue includes $21 million from asset sales. **b** Includes a $15 million revaluation decrement resulting from a revaluation of harbour improvements using deprival methodology. **c** Includes a revaluation decrement of $4.8 million relating to assets that are used to fulfil CSOs rather than to generate profits. Includes a decrement of $30 million relating to assets that were written down to zero to reflect that they will result in no extra income to the Darwin Port Corporation, after being transferred from the NT Department of Infrastructure, Planning and Environment. **d** Includes a decrement of $43 million relating to assets that were written down to zero to reflect that they will result in no extra income to the Darwin Port Corporation, after being transferred from the NT Department of Infrastructure, Planning and Environment. **e** Includes a decrement of $18 million relating to assets that were written down to zero to reflect that they will not generate additional income to the Darwin Port Corporation.

MELBOURNE PORT CORPORATION

Performance indicators 1999-00 to 2002-03

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*[c]	*2002-03*[d]	*2003-04*[e]
Size						
Total assets	$m	568	596	670	705	
Total revenue	$m	75	82	83	86	
Profitability						
Operating profit before tax	$'000	30 002	34 226	31 089	30 999	
Operating sales margin	%	49.2	49.0	43.7	40.9	
Cost recovery	%	209.9	196.0	177.7	169.1	
Return on assets	%	6.9	7.0	5.8	5.3	
Return on equity	%	4.1	4.5	4.0	3.5	
Financial management						
Debt to equity	%	17.7	14.0	12.1	11.3	
Debt to total assets	%	15.0	12.0	10.9	9.9	
Total liabilities to equity	%	24.7	19.5	17.5	17.3	
Interest cover	times	5.1	6.4	6.8	6.9	
Current ratio	%	40.8	160.1	90.9	42.0	
Leverage ratio	%	124.7	119.5	117.5	117.3	
Payments to and from government						
Dividends	$'000	8 644	9 300	10 350	10 450	
Dividend to equity ratio	%	2.1	1.9	1.9	1.8	
Dividend payout ratio	%	50.0	42.8	48.1	51.2	
Income tax expense	$'000	12 713	12 512	9 567	10 577	
CSO funding	$'000	0	0	0	0	

a An abnormal expense of $2.3 million was incurred, with the write-off of assets. **b** Total assets increased by $26 million with a revaluation of buildings, improvements and land. Does not include a provision for a final dividend because of a change in accounting policy. **c** Includes an asset revaluation increment of $60 million for land. Includes a final dividend of $4.5 million relating to 2000-01 and an interim dividend of $5.9 million for 2001-02. Does not include the Board's estimated final dividend of $4.9 million for 2001-02. **d** Includes a final dividend of $4.9 million relating to 2001-02 and an interim dividend of $5.6 million relating to 2001-02. Does not include the Board's estimated final dividend of $4.9 million for 2002-03. **e** The Melbourne Port Corporation ceased operations on 30 June 2003 and was replaced by the Port of Melbourne Corporation.

10 Forestry

The financial performances of five forestry government trading enterprises (GTEs) are covered in this chapter. The forestry sector was first included in this series of reports on financial performance monitoring in 2001-02.

Forestry GTEs from five states are monitored — State Forests of New South Wales (SFNSW), DPI Forestry Queensland (DPI Forestry), the Forests Products Commission of Western Australia (FPCWA), ForestrySA and Forestry Tasmania. These forestry GTEs have undergone significant restructuring to improve their commercial focus.

Financial data are presented from 2001-02 to 2003-04. Given the volatile nature of changes in the valuation of standing timber assets, profit is reported both before and after movements in forest valuations for all GTEs in the sector.

In 2003-04, the five monitored forestry GTEs had a combined asset value of around $6 billion and generated around $730 million in revenue.

Victoria, the Australian Capital Territory and the Northern Territory forestry GTEs are not reported. In Victoria, VicForests undertakes comparable activities to the monitored forestry GTEs. However, it is not possible to compare its financial performance because the Department of Sustainability and the Environment does not produce separate financial statements or Government Financial Statistics (see chapter 3). The Northern Territory does not have a government-owned forestry GTE. In the Australian Capital Territory, ACT Forests operates within the Department of Urban Services and is not reported because of substantial restructuring following the catastrophic bushfire in 2002-03.

Financial performance summaries, including performance indicators for the forestry sector and each forestry GTE, are presented after this introduction. The performance indicators are consistent across individual GTEs. For a discussion of the data and the financial indicators used, and some of the factors that should be considered when assessing performance, see chapter 3. Specifically, care should be taken because of differences in market environments and issues relating to the valuation of forestry assets.

10.1 Monitored GTEs

The monitored forestry GTEs provided a broad range of services (see table 10.1) including:

- plantation and native forest management;
- supply of forest products to the timber industry;
- research and development of new forestry techniques and processes;
- contributions to the marketing of forest products; and
- management of activities not related to timber production, which occur in state-managed native forests and plantations, including beekeeping, recreation facilities, grazing and quarrying.

In addition, forestry GTEs generally have responsibility for fire-fighting and other ancillary forest management activities.

The sizes of monitored forestry GTEs — in terms of the value of their assets and revenue — vary substantially (see figure 10.1). In 2003-04, the smallest GTE, in terms of asset value, was the FPCWA ($380 million) and the largest was SFNSW ($2.6 billion).

Governance for forestry GTEs differs across jurisdictions. Differences include the degree of emphasis on commercial objectives by boards and governments — compared to other objectives such as environmental management and community education.

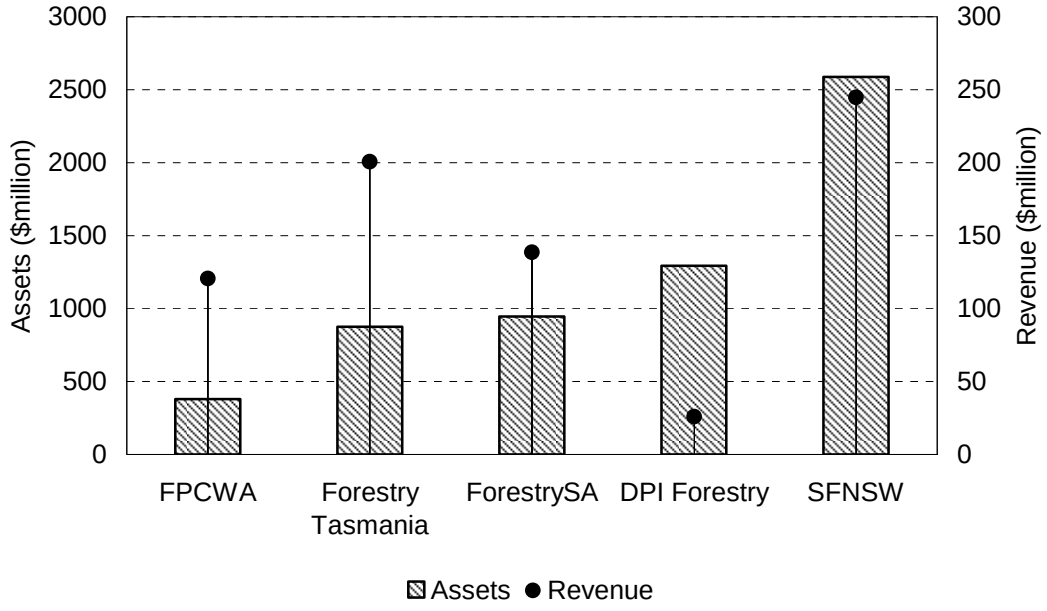
SFNSW, ForestrySA, the FPCWA and Forestry Tasmania are corporatised GTEs. DPI Forestry is a commercialised business unit within the Queensland Department of Primary Industries.

Table 10.1 **Activities — forestry GTEs, 2003-04**

Forestry GTE	*Activities*			
	Plantation management	Native forest management	Research and marketing	Tourism and recreation activities
SFNSW	✓	✓	✓	**a**
DPI Forestry	✓	✓	✓	**a**
FPCWA	✓	✓	✓	✗
ForestrySA	✓	✓**b**	✓	**a**
Forestry Tasmania	✓	✓	✓	✓

a Most of the monitored forestry GTEs provided services and infrastructure for tourism activities, such as scenic drives, picnic areas and hiking trails. Except for Forestry Tasmania, these activities generated negligible revenue for the GTEs over the reporting period. **b** ForestrySA receives CSO funding for specific native forest management activities.

Figure 10.1 **Assets and revenue — forestry GTEs, 2003-04**



Source: Productivity Commission estimates.

10.2 Market environment

The financial performances of forestry GTEs are linked to the volatility of demand for timber products, industry reforms and changes to accounting standards (see section 10.3).

Demand for forest products

The major traded output of forestry GTEs are logs. These are either harvested by the GTEs themselves or by private loggers operating as sub-contractors. Logs can be harvested as either:

- sawlogs — for conversion into sawn-timber, plywood, or veneer products that are mainly used in the construction and furniture industries; or
- pulp logs — for conversion into woodchips and fibreboard, particleboard or pulp (for subsequent conversion into paper and paperboard products).

Sawlogs are generally not exported and the demand for them is influenced by local economic conditions and government policies. For example, the introduction of the Goods and Services Tax (in July 2000) negatively affected the building industry. However, with a return to more buoyant building activity, demand for sawn timber and ultimately sawlogs increased strongly over the reporting period (ABS 2005).

According to the Australian Bureau of Agricultural and Resource Economics (ABARE) (2000), 40 per cent of pulpwood harvested in Australia each year is sold domestically for making pulp and paper products, while the majority (60 per cent) is exported — mainly as woodchips. Almost 90 per cent of Australia's woodchip exports go to Japan. Researchers from the Forestry Department at the Australian National University considered that factors such as the accumulation of paper stocks in Japan and a depressed Japanese economy contributed to the decline in export demand for pulpwood during the late 1990s, causing the world price of woodchips to steadily decrease from 1995 (ANU 1999, ABARE 2003).

Industry reforms

During the 1990s, forestry GTEs were reformed. The reforms arose out of the National Forest Policy Statement (NFPS), Regional Forest Agreements (RFAs), the Plantations 2020 Strategy and the application of National Competition Policy (NCP).

National Forest Policy Statement

The Commonwealth and all State and Territory governments signed the NFPS in 1992. The NFPS was a comprehensive agreement that sought to provide a 'blueprint' for the future management of Australia's forests, particularly its native forests. Aspects of the statement that were of particular significance to forestry GTEs were:

- the establishment of market-based pricing principles for forest resources;
- the use of RFAs as a means of providing integrated management of forest resources; and
- the expansion of Australia's commercial plantations of softwoods and hardwoods.

Regional Forest Agreements

RFAs are intended to provide greater certainty and more security in relation to forest conservation and timber resource supply. More specifically, RFAs are intended to:

- reduce uncertainty for industry and duplication in government processes for land-use decision making;
- produce long-term solutions that meet the requirements of governments, the community and industry, while also being consistent with the principles of ecologically sustainable development;
- equitably balance competing objectives and coordinate the policies and activities of governments;
- maintain regional, environmental, heritage and social values; and
- provide secure access to resources for the forestry industry.

Since 2000, hardwood woodchips from native forests could only be exported from forest regions in which RFAs had been successfully negotiated. South Australia, the Northern Territory and the Australian Capital Territory do not have commercial native forest operations.

Plantations 2020

The Plantations 2020 strategy included a proposal to treble the area of Australia's plantation forests by 2020, in line with previous proposals in the NFPS. In July 1996, this initiative was endorsed by the Ministerial Council on Forestry, Fisheries and Aquaculture. In addition to providing timber assets, plantations can provide salinity controls, biomass energy and carbon sequestration.

ABARE has forecast that by 2010 forest plantations could be providing 75 per cent of domestic wood supplies, compared with earlier expectations of only 62 per cent (ABARE 2002).

National Competition Policy

Under NCP, governments have agreed, among other things, to minimise resource allocation distortions relating to any competitive advantage derived by forestry GTEs as a result of their public sector ownership. Under clause 3 of the Competition Principles Agreement, governments, to the extent that the benefits outweigh the costs, are obliged to:

- adopt a corporatisation model where appropriate; and
- impose taxes or tax-equivalents, debt guarantee fees and regulations equivalent to those of private sector competitors.

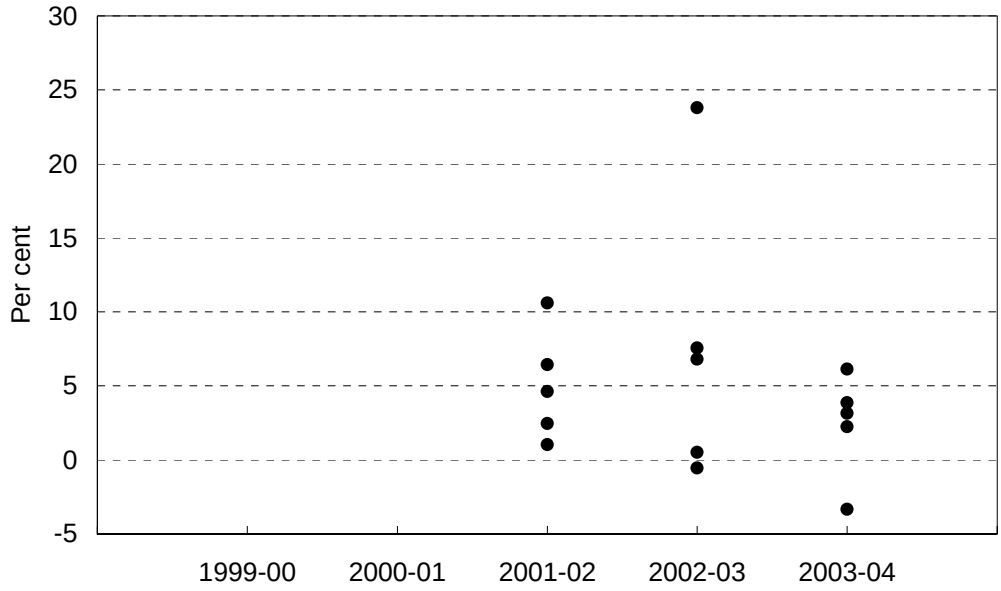
10.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings. All GTEs recorded a positive return in 2003-04 except for DPI Forestry (see figure 10.2). Two of the forestry GTEs improved their return on assets in 2003-04. However, the return on assets for the sector as a whole decreased from 6.7 per cent in 2002-03 to 1.8 per cent in 2003-04.

Following the introduction of accounting standard AAS 35 in June 2000, self generating and regenerating assets (SGARAs), which are held primarily for profit, have been valued at their net market value at each reporting date. Increments and decrements to SGARAs are recognised directly in the statement of financial performance.

From year-to-year, the profitability indicators of forestry GTEs can vary dramatically due to the recognition of movements in the market value of SGARAs. Even small changes to the asset's total value are likely to have a significant impact on reported operating performance.

Figure 10.2 **Return on assets — forestry GTEs**



Note Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue and adding back the gross interest expense. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used. The Commission commenced monitoring the forestry sector in 2001-02.

Source: Productivity Commission estimates.

The value of SGARAs will be influenced primarily by changes in the following:

- *The volume of timber* — The volume of timber is affected by changes in the area of commercial forests (natural or plantation) controlled by a GTE, or by changes in the commercial timber available within the existing commercial forest areas.
- *Age and quality of timber* — Trees of different ages attract a different value per cubic metre. Older, larger trees generally have higher value uses — such as building materials and furniture — than do younger, smaller trees. Different species of trees also have different use values and attract different prices in the market.
- *Market prices* — The prevailing market prices for the sawlogs and pulp logs harvested from SGARA assets.

Other things being equal, forestry GTEs can model with some precision the expected physical changes in their SGARA asset base resulting from the first two items. However, changes in the demand for SGARAs can be highly variable and are outside the control of forestry GTEs.

Importantly, changes in demand conditions are generally the predominant factor influencing market prices because supply is relatively constant. Therefore, fluctuations in demand largely determine movement in the overall value of SGARAs from year-to-year. Over the reporting period, each monitored forestry GTE adjusted the value of their SGARAs, which in some cases had a significant impact on reported revenue (see table 10.2). For example, DPI Forestry's SGARA revaluation in 2002-03 resulted in a $334 million increment in the valuation of plantation timber, accounting for around 93 per cent of its revenue during the period.

Table 10.2 **Size of SGARA revaluations — forestry GTEs**

GTE	*SGARA revaluation ($million)*		
	2001-02	2002-03	2003-04
SNFSW	34.3	57.1	9.0
DPI Forestry	155.7	334.2	1.5
ForestrySA	3.8	21.0	14.8
FPCWA	- 1.2	13.7	22.4
Forestry Tasmania	9.6	- 25.3	9.3

Source: Relevant annual reports.

Typically forest assets are valued at the net present value (NPV) of expected future profits. Under AAS 35, forest assets may be valued at either the *in situ* market price of the timber asset, or at the NPV. However, there is a great deal of uncertainty attached to the *in situ* market prices since there are few transactions on which to value forest-lots of *in situ* timber.

There is a link between asset values and rates of return when assets are valued using the NPV approach. This arises because there is an implicit assumption of a required rate of return in determining the NPV, linking the asset value to the rate of return. Since rates of return themselves depend on asset values, this creates a circularity between asset values and rates of return.

This 'circularity', coupled with the sensitivity of rate of return measures to factors unrelated to the performance of the forestry agency (for example, changes in market conditions), suggests that, for performance monitoring purposes, annual rates of return need to be assessed in the context of longer-term trends and other relevant information (CCNCO 2001).

Over the reporting period, DPI Forestry, the FPCWA and Forestry Tasmania used different approaches to estimating the NPV of timber assets. ForestrySA used current market prices, though 'pre-commercial' stands of timber (those aged less than 15 years) were valued at historical cost. SFNSW used market price to assess

softwood plantation and native forest timber but valued hardwood plantations on the basis of historical cost, due to difficulties in determining market prices for this asset.

Profitability measures can also be affected by the correction of modelling errors relating to previous financial years. For example, Forestry Tasmania reported that the net market value of standing timber in 2000-01 was overstated by $12.5 million. If the error had not been discovered, Forestry Tasmania's pre-tax operating profit would have been $21.7 million (or 236 per cent) higher in 2001-02.

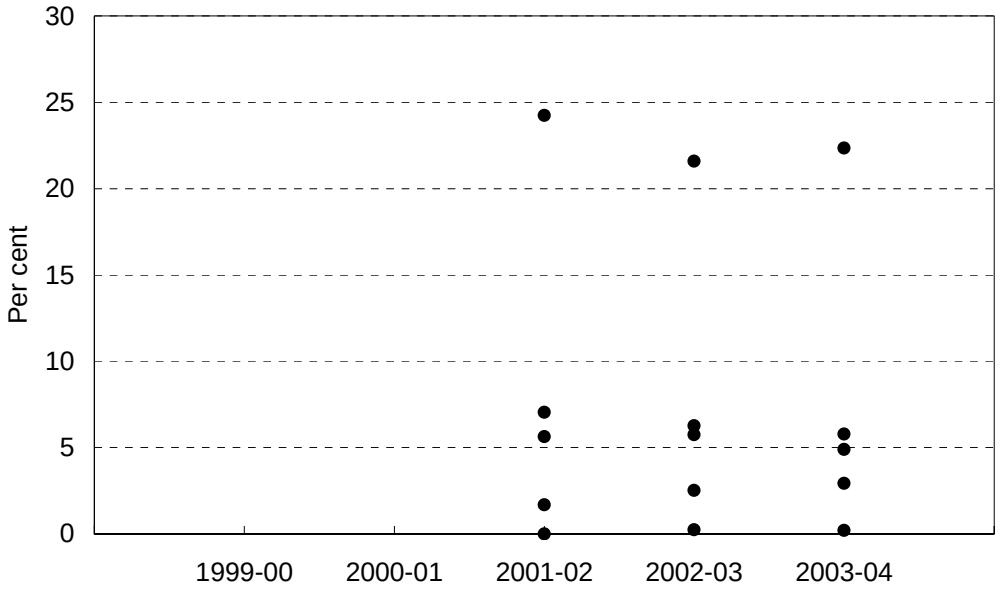
The cost recovery ratio indicates whether there was adequate revenue to cover expenses. Over the reporting period, most forestry GTEs reported a cost recovery ratio of over 100 per cent. In 2002-03, SFNSW and Forestry Tasmania reported cost recovery ratios of just under 100 per cent, and in 2003-04 DPI Forestry's cost recovery ratio fell to 33 per cent.

10.4 Financial management

Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

The total level of debt for the monitored forestry sector overall in 2003-04 was around $300 million, with no forestry GTE operating debt-free. Over the reporting period, the debt to total assets ratio has marginally declined (see figure 10.3).

Figure 10.3 **Debt to total assets — forestry GTEs**



Note Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Average total assets is the average of the value of assets at the beginning and end of each financial year. Where an average was not available, the value of total assets at the end of the financial year was used. During 2002-03 and 2003-04, no forestry GTE operated debt free, while in 2001-02, only one forestry GTE — ForestrySA — operated debt free. The Commission commenced monitoring the forestry sector in 2001-02.

Source: Productivity Commission estimates.

As a whole, the monitored forestry GTEs in 2003-04 had a far lower debt to assets ratio (5.1 per cent) than did other industry sectors. GTEs in the electricity (38 per cent), ports (23 per cent), water (17 per cent), rail (25 per cent) and urban transport (17 per cent) sectors, all reported significantly higher debt to assets ratios in 2003-04.

Sound financial management requires that profits are sufficient to ensure that interest payments can be met. A high interest cover ratio indicates that the entity can sustain a fall in profit or an increased interest expense and still meet the cost of servicing debt.

Three forestry GTEs reported positive interest cover ratios in 2003-04. This indicates that these GTEs can currently meet their interest commitments from operating profit. It was not possible to calculate an interest cover ratio for SFNSW because their reported interest expenses were capitalised. DPI Forestry's interest cover was negative in 2003-04.

A current ratio of less than 100 per cent indicates that the short-term obligations of the GTE may need to be met using sources of funds other than current assets. Four of the five GTEs recorded a current ratio of over 100 per cent in 2003-04, with SFNSW being the exception.

10.5 Transactions with government

As a part of the reform process, governments have sought to give GTEs a greater commercial focus and facilitate competitive neutrality by exposing them to capital market disciplines and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles, see chapter 3.

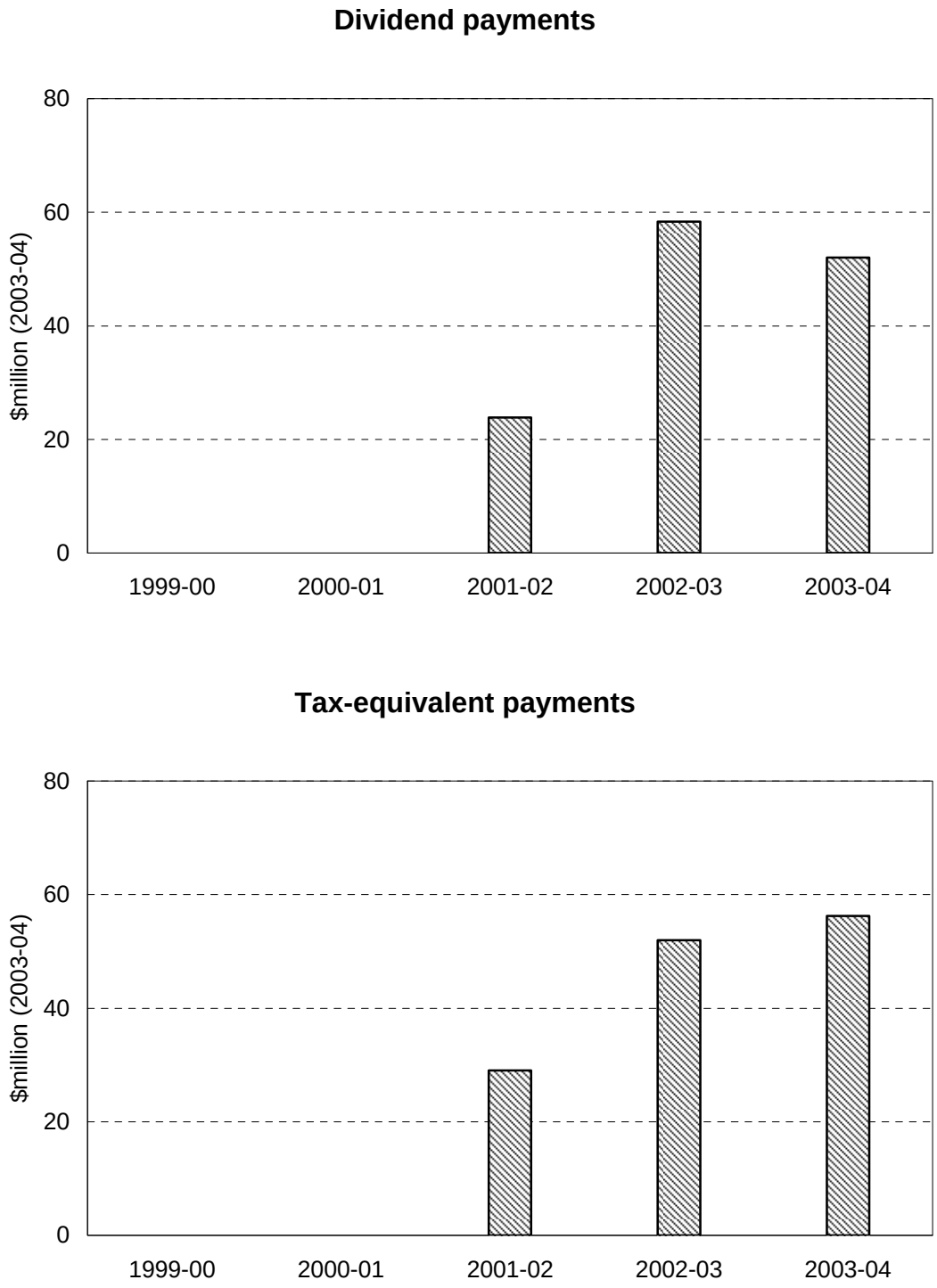
Governments act as the shareholder of forestry GTEs on behalf of the community. Dividend payments from GTEs are generally justified as a return on shareholder funds. In 2003-04, all forestry GTEs reported dividend payments to their respective owner-governments (see figure 10.4). Forestry Tasmania reported a dividend during 2001-02, but did not recognise a dividend during 2002-03 because of a change in accounting policy to meet the requirements of AASB 1044 (see chapter 3).

All forestry GTEs fall within the National Tax Equivalent Regime and are required to make income tax-equivalent payments. All except DPI Forestry made tax-equivalent payments over the reporting period. DPI Forestry did not make payments because of permanent differences between accounting and taxable incomes and it is considered unlikely that any taxation payments will be required in the foreseeable future.

Dividend and tax-equivalent payments from the forestry GTEs decreased in 2003-04, although they have increased over the reporting period (see figure 10.4). The majority of the increase in tax was paid by SFNSW, which contributed over 45 per cent of the total tax payment from forestry GTEs. ForestrySA was the only forestry GTE to pay a special dividend during the year.

Three of the monitored forestry GTEs — SFNSW, ForestrySA and the FPCWA — had agreements to provide CSOs in 2003-04.

Figure 10.4 **Dividend and income tax-equivalent payments — forestry GTEs**



Note The Commission commenced monitoring the forestry sector in 2001-02. The value of dividends and tax-equivalent payments prior to 2003-04 were converted to 2003-04 dollars using the using the implicit price deflator — Gross Fixed Capital Formation of Public Corporations (see chapter 3).

Source: Productivity Commission estimates.

FORESTRY

Whole of sector performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			5 470	5 802	6 082
Total revenue	$m			811	986	730
Profitability						
Operating profit before tax	$'000			230 790	371 014	96 978
Operating sales margin	%			29.7	38.6	14.4
Cost recovery	%			140.3	160.7	115.3
Return on assets	%			4.4	6.7	1.8
Return on equity	%			4.2	6.4	1.1
Financial management						
Debt to equity	%			6.5	6.2	5.9
Debt to total assets	%			5.5	5.4	5.1
Total liabilities to equity	%			15.5	16.2	16.2
Interest cover	times			20.5	32.2	9.3
Current ratio	%			151.5	128.4	144.4
Leverage ratio	%			115.5	116.2	116.2
Payments to and from government						
Dividends	$'000			23 873	58 415	56 268
Dividend to equity ratio	%			0.5	1.2	1.1
Dividend payout ratio	%			11.8	18.3	98.8
Income tax expense	$'000			29 065	52 051	40 002
CSO funding	$'000			13 604	14 639	14 355

[a] 2001-02 was the first year that the forest sector was included in this report.

Whole of sector performance indicators before SGARA revaluation 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Profitability						
Operating profit before tax	$'000			28 682	- 29 585	40 064
Return on assets	%			0.7	- 0.3	0.9
Return on equity	%			0.0	- 1.7	0.0

10.6 GTE performance reports

State Forests of New South Wales
DPI Forestry (Queensland)
ForestrySA (SA)
Forest Products Commission (WA)
Forestry Tasmania

The Forestry Commission of New South Wales — trading under the name State Forests of New South Wales (SFNSW) — operates under the *Forestry Act 1916*. SFNSW is responsible for managing almost 3 million hectares of plantation and native forests throughout New South Wales. During 2003-04, 1500 hectares of new hardwood plantations were established, as well as an additional 6500 hectares of softwood plantations.

SFNSW earns almost all its revenue from trading hardwood and softwood timber products — most of which are utilised within the Australian building industry. The prices it receives largely depend on the level of activity in these industries.[1]

More than 60 per cent (over $1.6 billion) of SFNSW's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.[2]

In 2003-04, capital expenditure increased by 13 per cent to $36 million. This was reportedly because of a lack of expenditure on plantation establishment in 2002-03, when resources were focused more towards fire prevention.

Operating profit was favourably influenced by a $34 million (2001-02), $57 million (2002-03) and a $9 million (2003-04) increment in the market value of SFNSW's standing timber assets. Revenue increased by $24 million (11 per cent) in 2003-04, with revenue before SGARA revaluation increasing by $72 million (44 per cent). SFNSW's financial performance was largely improved by a reduction in non-recurrent items such as a $56 million write down of road assets.

SFNSW significantly improved its return on assets and return on equity in 2003-04, following a decline from 2001-02 to 2002-03.

SFNSW is funded for the provision of CSOs, including the provision of recreational facilities, education and advisory services, community fire protection, research, and regulatory services.

1 Residential building activity increased significantly in 2001-02, due mainly to a combination of low interest rates and the First Home Owners Grant. The market remained buoyant during 2002-03 and 2003-04.

2 Under AAS 35, SGARAs are reported at their net market value. SFNSW uses three separate net market value models to determine the value of their softwood plantation, hardwood plantation and native forest timber. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

STATE FORESTS (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			2 365	2 362	2 588
Total revenue	$m			232	220	245
Profitability						
Operating profit before tax	$'000			57 903	12 154	55 252
Operating sales margin	%			24.7	5.4	22.5
Cost recovery	%			117.3	99.7	124.4
Return on assets	%			2.4	0.5	2.2
Return on equity	%			2.2	- 0.9	1.8
Financial management						
Debt to equity	%			6.8	7.1	5.7
Debt to total assets	%			5.6	5.7	4.9
Total liabilities to equity	%			20.9	24.0	21.7
Interest cover[b]	times			n.r.	n.r.	n.r.
Current ratio	%			80.1	62.8	71.1
Leverage ratio	%			120.9	124.0	121.7
Payments to and from government						
Dividends	$'000			4 717	4 162	13 096
Dividend to equity ratio	%			0.2	0.2	0.6
Dividend payout ratio	%			11.0	- 24.6	35.4
Income tax expense	$'000			15 014	29 071	18 246
CSO funding	$'000			9 557	9 557	9 455

a 2001-02 was the first year that State Forests of New South Wales was included in this report. **b** All interest expenses related to borrowings from acquisitions of land, and the establishment and development of new plantations have been capitalised, as these assets take a considerable period to become commercially productive. Consequently, interest cover cannot be calculated. **n.r.** Not relevant.

Performance indicators before SGARA revaluation 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Profitability						
Operating profit before tax	$'000			23 646	- 44 904	46 259
Return on assets	%			1.0	- 1.9	1.9
Return on equity	%			0.4	- 3.8	1.4

DPI FORESTRY Queensland

DPI Forestry of Queensland was established on 1 July 1995, as a commercial business unit within the Queensland Department of Primary Industries.[1] It is responsible for 84 per cent of Queensland's domestic timber production. DPI Forestry manages plantation estates that cover 190 000 hectares.

Around 90 per cent ($1.2 billion) of DPI Forestry's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.[2]

In 2003-04, assets decreased by $57 million (4 per cent) with plantation timber reduced by $82 million (7 per cent). Capital expenditure was $9 million over the financial year.

Operating profit was favourably influenced by a $156 million (2001-02), $334 million (2002-03) and a $2 million (2003-04) increment in the market value of DPI Forestry's standing timber assets. Revenue fell by $335 million (93 per cent) in 2003-04, with revenue before SGARA revaluation decreasing by $2 million (8 per cent). A reduction in revenue from specialised forestry industry services, such as service level agreements for maintaining roads, contributed to DPI Forestry's decline in financial performance.

DPI Forestry recorded a negative return on assets and also a negative return on equity during 2003-04, reflecting operating losses.

DPI Forestry is subject to dividend and tax-equivalent payments. The dividend payable is declared at a negotiated percentage (currently 50 per cent) of profit from ordinary activities after tax and adjustments for plantation timber valuation increments. In 2003-04, the tax–equivalent payment was deferred.[3]

DPI Forestry was not subject to CSOs over the reporting period.

1 DPI Forestry was established as a commercial business group on 15 May 1995.

2 Under AAS 35, SGARAs are reported at their net market value. DPI Forestry determines net market value by calculating the net present value of future cash flows it expects to realise from the timber. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

3 The payment has been deferred because of timing differences. The provision for deferred income tax has not been brought to account in the annual reports since it is considered unlikely that any taxation will occur in the foreseeable future.

DPI FORESTRY (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			1 087	1 352	1 294
Total revenue	$m			187	361	26
Profitability						
Operating profit before tax	$'000			110 630	285 348	- 48 832
Operating sales margin	%			61.6	80.3	- 195.9
Cost recovery	%			260.5	508.3	33.3
Return on assets	%			10.6	23.8	- 3.3
Return on equity	%			11.2	25.4	- 4.0
Financial management						
Debt to equity	%			7.7	6.1	6.4
Debt to total assets	%			7.0	6.3	5.8
Total liabilities to equity	%			9.7	7.9	8.5
Interest cover	times			24.6	61.8	- 9.4
Current ratio	%			276.9	251.9	290.3
Leverage ratio	%			109.7	107.9	108.5
Payments to and from government						
Dividends	$'000			10 979	24 795[b]	16 065
Dividend to equity ratio	%			1.1	2.2	1.3
Dividend payout ratio	%			9.9	8.7	- 32.9
Income tax expense	$'000			0	0	0
CSO funding	$'000			0	0	0

[a] DPI Forestry, established in 1995, was monitored for the first time in 2001-02. In 2001-02, the application of AASB 1041 led to the revaluation of several non–current assets. [b] Includes dividend payable of $14.8 million as well as a special dividend of $10 million. Before the special dividend, the dividend to equity and dividend payout ratios would have been 1.3 per cent and 5.2 per cent respectively.

Performance indicators before SGARA revaluation 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Profitability						
Operating profit before tax	$'000			- 45 069	- 48 871	- 50 344
Return on assets	%			- 3.7	- 3.6	- 3.4
Return on equity	%			- 4.5	- 4.4	- 4.1

FORESTRY SA — South Australia

The South Australia Forestry Corporation, trading under the name ForestrySA, was incorporated under the *South Australia Forestry Corporation Act 2000*, on 1 January 2001.[1] It is also subject to the provisions of the *Public Corporations Act 1993* and the *Forestry Act 1950*. ForestrySA is responsible for managing over 82 000 hectares of plantation forests. During 2003-04, over 2400 hectares of new trees were planted.

Around 65 per cent ($633 million) of ForestySA's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.[2]

ForestrySA earns almost all its revenue from trading softwood timber products — most of which are utilised by the Australian building industry. In 2003-04, over 2 million cubic metres of log and pulp products were sold, 56 percent of which were log products. This included over 1.8 million cubic metres harvested from ForestrySA plantations, with the balance from logs harvested by ForestrySA for private forest owners.

Operating profit was favourably influenced by a $4 million (2001-02), $21 million (2002-03) and a $15 million (2003-04) increment in the market value of ForestrySA's standing timber assets. Revenue fell by $2 million (1 per cent) in 2003-04, with revenue before SGARA revaluation increasing by $5 million (4 per cent). ForestrySA's strong financial performance was largely because of increased sales of timber products, which was influenced by solid results in the housing construction and renovation market over the reporting period.

ForestrySA is subject to dividend and tax-equivalent payments. In 2003-04, the Treasurer determined that a dividend of $22 million ($28 million in 2002-03) was payable, of which $21 million was from trading operations and $1 million was a special dividend from earnings in the previous financial year.

ForestrySA is funded for the provision of CSOs, including forest industry development, policy and legislative support, community use of forests, and native forest management.

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1 Prior to the creation of the South Australia Forestry Corporation, its functions were carried out by the ForestrySA business unit within the Department for Administrative and Information Services.

2 Under AAS 35, SGARAs are reported at their net market value. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

FORESTRY SA (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			842	890	946
Total revenue	$m			115	140	139
Profitability						
Operating profit before tax	$'000			38 847	58 858	56 125
Operating sales margin	%			33.4	41.5	40.1
Cost recovery	%			149.1	170.1	166.4
Return on assets	%			4.6	6.8	6.1
Return on equity	%			3.4	5.6	4.9
Financial management						
Debt to equity	%			0.0	0.2	0.2
Debt to total assets	%			0.0	0.2	0.2
Total liabilities to equity	%			1.8	2.0	2.2
Interest cover	times			n.r.	1 436.6	476.6
Current ratio	%			285.3	259.0	255.3
Leverage ratio	%			101.8	102.0	102.2
Payments to and from government						
Dividends[b]	$'000			3 216	27 901	21 793
Dividend to equity ratio	%			0.4	3.3	2.4
Dividend payout ratio	%			11.4	59.0	49.7
Income tax expense	$'000			10 653	11 593	12 251
CSO funding	$'000			3 547	3 512	3 600

a ForestrySA, established on 1 January 2001, was monitored for the first time in 2001-02. **b** Includes special dividend payments of $7.8 million (2002-03) and 920 000 (2003-04). **n.r.** Not relevant.

Performance indicators before SGARA revaluation 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Profitability						
Operating profit before tax	$'000			35 047	37 838	41 369
Return on assets	%			4.2	4.4	4.5
Return on equity	%			2.9	3.1	3.2

FOREST PRODUCTS COMMISSION — Western Australia

The Forest Products Commission of Western Australia (FPCWA) was established in November 2000 under the *Forest Products Act 2000*. The FPCWA is responsible for the commercial production, allocation and sale of forest products from Western Australia's native forests and state-owned and state-managed plantations. FPCWA manages tree farms in Western Australia, with the land controlled by the public and the private sector.

Over 80 per cent ($320 million) of the FPCWA's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.[1]

Operating profit was influenced by a $1 million (2001-02) decrement, and a $14 million (2002-03) and a $22 million (2003-04) increment in the market value of the FPCWA's standing timber assets. Operating profit before tax fell by $11 million (57 per cent) in 2003-04, with operating profit (pre-tax) before SGARA revaluation decreasing by $20 million (313 per cent). The FPCWA's decline in financial performance was reportedly because of forest conservation efforts and a $7.6 million write down of assets (not including standing timber assets).

The FPCWA's return on assets and return on equity has declined over the reporting period, largely because of a reduction in operating profit before tax of $7 million (44 per cent) and an increase in assets of $40 million (12 per cent).

The FPCWA receives CSO payments for its forest enhancement program.

1 Under AAS 35, SGARAs are reported at their net market value. FPCWA determines net market value by calculating the net present value of future cash flows it expects to realise from the timber. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

FOREST PRODUCTS COMMISSION (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			340	360	379
Total revenue	$m			123	122	121
Profitability						
Operating profit before tax	$'000			15 468	20 122	8 630
Operating sales margin	%			17.7	21.6	11.8
Cost recovery	%			121.3	127.6	113.4
Return on assets	%			6.4	7.6	3.9
Return on equity	%			5.6	5.9	2.3
Financial management						
Debt to equity	%			34.4	29.7	31.8
Debt to total assets	%			24.2	21.6	22.3
Total liabilities to equity	%			41.8	41.8	45.9
Interest cover	times			3.4	4.2	2.5
Current ratio	%			175.4	122.5	112.3
Leverage ratio	%			141.8	141.8	145.9
Payments to and from government						
Dividends	$'000			0	1 557	1 470
Dividend to equity ratio	%			0.0	0.6	0.6
Dividend payout ratio	%			0.0	10.7	24.3
Income tax expense	$'000			2 158	5 622	2 592
CSO funding	$'000			500	1 570	1 300

[a] The Forest Products Commission, established in November 2000, was included in this report for the first time in 2001-02.

Performance indicators before SGARA revaluation 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Profitability						
Operating profit before tax	$'000			16 693	6 443	- 13 720
Return on assets	%			6.8	3.6	- 2.2
Return on equity	%			6.1	0.3	- 6.3

FORESTRY TASMANIA — Tasmania

Forestry Tasmania was established by the *Forestry Act 1920* and is subject to the *Government Business Enterprises Act 1995*. Forestry Tasmania is responsible for managing around 1.5 million hectares of state forests and plantations. During 2003-04, 4700 hectares of hardwood and 3500 hectares of softwood plantations were established.

Over 80 per cent ($714 million) of Forestry Tasmania's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.[1]

Operating profit was influenced by a $25 million (2002-03) decrement, and a $10 million (2001-02) and a $9 million (2003-04) increment in the market value of Forestry Tasmania's standing timber assets. Revenue increased by $58 million (41 per cent) in 2003-04, with revenue before SGARA increasing by $24 million (14 per cent). Forestry Tasmania's improved financial performance since 2001-02 was largely because of strong forest sales revenue.

Changes in accounting polices and a capital restructure significantly affected Forestry Tasmania's equity structure in 2001-02. Previously debt free, $14 million in new borrowings were acquired to finance investment in roads, plantations and other revenue-generating capital items. Borrowings of $7 million in 2002-03 and $4 million in 2003-04 were made to assist with expansion of the forest estate and to invest in roads.

Forestry Tasmania was not subject to CSOs over the reporting period.

1 Under AAS 35, SGARAs are required to be reported at their net market value. Forestry Tasmania determines net market value by calculating the net present value of cash flows it expects to realise from the timber. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

FORESTRY TASMANIA (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*[a]	*2002-03*	*2003-04*
Size						
Total assets	$m			837	838	874
Total revenue	$m			154	142	201
Profitability						
Operating profit before tax	$'000			7 942	- 5 468	25 803
Operating sales margin	%			5.3	- 3.7	13.2
Cost recovery	%			115.4	96.5	115.2
Return on assets	%			1.0	- 0.6	3.2
Return on equity	%			0.9	- 1.6	2.6
Financial management						
Debt to equity	%			2.0	3.0	3.4
Debt to total assets	%			1.7	2.5	2.9
Total liabilities to equity	%			16.2	18.2	20.3
Interest cover	times			11.5	- 5.6	22.9
Current ratio	%			138.9	155.5	149.1
Leverage ratio	%			116.2	118.2	120.3
Payments to and from government						
Dividends	$'000			4 961	0[b]	3 844
Dividend to equity ratio	%			0.7	0.0	0.5
Dividend payout ratio	%			74.0	0.0	20.3
Income tax expense	$'000			1 240	5 765	6 913
CSO funding	$'000			0	0	0

[a] Forestry Tasmania, established in 1995, was monitored for the fist time in 2001-02. [b] A change in accounting policy to meet the requirements of AASB 1044 meant that no dividend was recognised in 2002-03 (see chapter 3). Forestry Tasmania has proposed a $4.4 million dividend for 2003-04. The proposed dividend is subject to approval by the Treasurer and the relevant Minister and had not been recognised as a provision as at June 2003-04.

Performance indicators before SGARA revaluation 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Profitability						
Operating profit before tax	$'000			- 1 635	19 909	16 500
Return on assets	%			- 0.1	2.5	2.1
Return on equity	%			- 0.4	2.0	1.3

11 Australian Government GTEs

Three Australian Government trading enterprises are covered in this chapter — Airservices Australia, Australia Post and Telstra. These GTEs vary significantly in size and in the range of services that they provide.

For a discussion of the data and the performance indicators used and some of the factors that should be considered when assessing performance, see chapter 3.

AIRSERVICES AUSTRALIA — Australian Government

Airservices Australia (ASA) was established in July 1995 under the *Air Services Act 1995*, and is responsible for providing and managing Australia's air navigation and air traffic services infrastructure. In April 2004, the commercial activities and regulatory functions of ASA were separated. It is proposed that the regulatory functions will ultimately be transferred to an airspace directorate within the Department of Transport and Regional Services.

Terminal navigation charges are levied for the use of terminal navigation facilities and services for each landing or practice instrument approach. These charges vary with the maximum take-off weight of the aircraft, the time services used and where the aerodrome is located.

In 2003-04, ASA's assets decreased by almost $58 million (9.6 per cent), largely because of a $61 million decrease in current assets (33 per cent). Some of these current assets were used to reduce current liabilities by around $20 million (14 per cent). The current ratio fell by nearly 22 per cent in the financial year.

Operating profit before tax increased by around $3 million in 2003-04, reportedly reflecting the worldwide aviation industry recovery from the impact of the SARS (sever acute respiratory syndrome) outbreak in 2002-03. ASA's operating profit (pre-tax) had declined by around $50 million and revenue had fallen by over $70 million in 2001-02, mainly as a result of the downturn in the aviation industry (post September 11) and the collapse of Ansett.

ASA is subject to dividend and tax-equivalent payments. An interim dividend of $11 million for 2002-03 was not recognised until 2003-04, this largely accounted for the $15.5 million increase in dividends for 2003-04.

ASA receives an Australian Government CSO payment, which has been set at $7 million since 2001-02. The CSO is aimed at enabling ASA to continue to cap prices at regional and general aviation airports. ASA also internally funds a number of other non-commercial community service activities, including an environmental information (maps, reports and statistics) gathering service, as well as aircraft noise and flight path monitoring.[1]

1 In 2003-04, ASA estimated that for non-commercial community service activities, expenses exceeded CSO reimbursement by $20.4 million.

AIRSERVICES AUSTRALIA (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	619	592	585	602	545
Total revenue	$m	636	583	511	617	615
Profitability						
Operating profit before tax	$'000	78 291	86 695	36 118	65 871	68 932
Operating sales margin	%	13.4	15.4	7.3	10.8	11.8
Cost recovery	%	112.1	118.2	107.9	112.1	113.4
Return on assets	%	13.3	15.5	7.2	12.3	13.3
Return on equity	%	15.9	23.2	9.9	13.5	22.3
Financial management						
Debt to equity	%	42.3	40.7	38.8	44.2	52.4
Debt to total assets	%	15.5	16.5	17.0	16.9	17.5
Total liabilities to equity	%	162.0	140.9	126.2	166.1	185.2
Interest cover	times	11.0	13.0	6.7	10.6	10.8
Current ratio	%	85.5	76.5	194.3	135.4	105.9
Leverage ratio	%	262.0	240.9	226.2	266.1	285.2
Payments to and from government						
Dividends	$'000	13 000	22 100	11 400	14 900	30 600[b]
Dividend to equity ratio	%	5.8	9.2	4.5	6.1	14.7
Dividend payout ratio	%	36.4	39.5	45.9	45.6	65.7
Income tax expense	$'000	42 544	30 744	11 269	33 187	22 368
CSO funding	$'000	11 000	7 000	7 000	7 000	7 000

a Includes abnormal revenue of $21.1 million generated by the write-back of legal provisions and asset sales. Successful outcomes in litigation enabled the write-back of legal provisions totalling $31 million. **b** An interim dividend ($11 million) for 2002-03 was not recognised until 2003-04.

AUSTRALIA POST — Australian Government

Australia Post was established in 1975 and corporatised in 1989 under the *Australian Postal Corporation Act 1989*. Its principal activities are letter delivery, parcel delivery, third party agency services (receiving payments for company and government services and charges), as well as the sale of postal products and merchandise. Australia Post holds a statutory monopoly for the processing and distribution of letters weighing 250 grams or less, or priced at less than two dollars.

In 2003-04, Australia Post's assets increased by $107 million (3.2 per cent), while liabilities decreased by $134 million (6.5 per cent). Debt to equity declined in 2003-04 by over 15 per cent, with debt levels unchanged and equity increasing by around 18 per cent. Capital expenditure on business infrastructure and the large letters and parcels networks was $207 million in the financial year.

In 2003-04, operating profit before tax was almost 13 per cent higher because of strong revenue growth in each of Australia Post's core activities, resulting in a record level of revenue ($4160 million). This followed a year of similar progress in 2002-03, with an increase in the basic postage rate, as well as volume growth in non-mail products and services.

Australia Post is subject to dividend and tax-equivalent payments. In 2003-04, dividend payments decreased by $95.5 million to $219 million, with no special dividend paid.

Australia Post is required to internally fund CSOs, estimated by Australia Post on an avoidable cost basis at $79.1 million in 2003-04. It must provide a standard letter service to all parts of Australia at a uniform price. In doing so, Australia Post must also meet particular standards.

Achievement of the prescribed standards — mainly relating to service frequency, on-time delivery and geographical access to postal facilities — is audited by the Australian National Audit Office. All of the prescribed standards were met or exceeded in 2003-04.

AUSTRALIA POST (continued)

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*	*2000-01*[a]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	3 037	3 199	3 229	3 365	3 472
Total revenue	$m	3 743	3 733	3 758	3 972	4 161
Profitability						
Operating profit before tax	$'000	391 900	402 100	407 200	462 000	521 100
Operating sales margin	%	10.9	11.2	11.1	11.7	12.7
Cost recovery	%	113.5	112.7	112.4	113.2	114.6
Return on assets	%	14.4	14.0	13.6	14.9	16.2
Return on equity	%	25.0	24.7	26.3	26.9	25.8
Financial management						
Debt to equity	%	47.8	47.5	46.5	40.2	34.0
Debt to total assets	%	18.0	17.0	16.5	16.1	15.5
Total liabilities to equity	%	173.8	186.6	183.3	155.2	122.6
Interest cover	times	13.3	13.1	15.3	16.7	17.2
Current ratio	%	93.8	100.2	108.8	106.7	111.6
Leverage ratio	%	273.8	286.6	283.3	255.2	222.6
Payments to and from government						
Dividends	$'000	155 700	274 500	291 800	314 000	218 500
Dividend to equity ratio	%	15.0	24.7	25.9	25.5	15.2
Dividend payout ratio	%	60.0	100.0	98.2	94.9	58.9
Income tax expense	$'000	132 400	127 600	110 200	131 200	150 000
CSO funding	$'000	0	0	0	0	0

a Includes net abnormal expenses of $34 million incurred for year 2000 compliance and GST implementation costs.

TELSTRA — Australian Government

Telstra Corporation Ltd was established in April 1993 and operates under the *Telecommunications Act 1997*. Telstra was first partially privatised in November 1997, when 33 per cent of the Corporation was floated. The second sell-off of 16 per cent occurred in October 1999. The Australian Government retains 50.1 per cent of issued shares.

Telstra offer a full range of services and competes in all telecommunications markets throughout Australia. Most of these services are provided at both a retail level and at a wholesale level to other carriers, carriage service providers and Internet service providers.

Total assets in 2003-04 decreased by $606 million (1.7 per cent) and current assets declined by 2.7 per cent, with current liabilities rising by 29.9 per cent. The current ratio consequently decreased by 28.7 per cent.

In 2003-04, operating profit before tax increased by $920 million (18.7 per cent), mainly because in 2002-03, Telstra had incurred a $965 million write-off of the investment in a 50 per cent owned overseas joint venture, Reach Ltd.

Telstra is subject to dividend and tax-equivalent payments. A change in accounting policy resulted in the 2002-03 final dividend being recognised and paid in 2003-04, which contributed to the significant decline in dividends in 2002-03.

Telstra's Universal Service Obligation (USO) requires that standard telephone services, public payphones and prescribed carriage services are reasonably accessible to all people in Australia, including services for the disabled, on an equitable basis, wherever they reside or carry on business. Telstra is also subject to the Digital Data Service Obligation (DDSO) whereby it must provide reasonable and equitable access to a digital data service with a data speed broadly equivalent to 64kbps. Telstra fulfils the DDSO through the supply of Integrated Services Digital Network services, to which at least 96 per cent of the Australian population have access, and through the Bigpond satellite one way services for the remainder of the population.

Telstra does not receive government funding for the USO or DDSO, though it receives contributions from other carriers for recognised USO costs.[1]

1 The net cost of the USO in 2003-04 was shared among carriers based on the proportion of eligible telecommunications revenue. The Communications Minister determines USO costs ($231.7 million in 2003-04), although Telstra considers this amount to be significantly less than its costs.

Performance indicators 1999-00 to 2003-04

	Units	*1999-00*[a]	*2000-01*[b]	*2001-02*	*2002-03*	*2003-04*
Size						
Total assets	$m	30 339	37 473	38 219	35 599	34 993
Total revenue	$m	19 840	23 086	20 928	21 700	21 335
Profitability						
Operating profit before tax	$'000	5 349 000	6 297 000	5 446 000	4 928 000	5 848 000
Operating sales margin	%	29.9	30.2	29.9	26.5	30.8
Cost recovery	%	148.7	143.4	142.6	136.0	144.6
Return on assets	%	20.6	20.8	16.8	15.7	18.7
Return on equity	%	33.5	32.1	26.2	23.0	26.7
Financial management						
Debt to equity	%	84.6	102.0	101.9	81.4	79.8
Debt to total assets	%	33.9	41.3	38.0	34.0	34.7
Total liabilities to equity	%	161.5	173.1	170.9	130.8	127.8
Interest cover	times	9.5	9.2	7.1	6.6	8.6
Current ratio	%	51.9	67.4	77.5	98.7	70.3
Leverage ratio	%	261.5	273.1	270.9	230.8	227.8
Payments to and from government						
Dividends	$'000	2 316 000	2 445 000	2 830 000	1 930 000[c]	3 186 000[d]
Dividend to equity ratio	%	21.2	19.3	20.8	13.1	20.7
Dividend payout ratio	%	63.1	60.2	77.5	56.9	77.4
Income tax expense	$'000	1 676 000	2 236 000	1 796 000	1 534 000	1 731 000
CSO funding	$'000	0	0	0	0	0

a Includes abnormal expenses of $574 million for planned and actual redundancies. **b** Includes net unusual revenue of $600 million, mainly relating to the sale of a global wholesale business, acquisition costs and superannuation adjustments. **c** A special dividend of $386 million was paid in 2002-03. A change in accounting policy in 2002-03 to meet the requirements of AASB 1044 meant provisions for dividends can no longer be raised at balance date when the dividend is declared after that date (see chapter 3). **d** A provision for dividend payable was raised as at the date of declaration (12 August 2004), amounting to $1.6 billion for the 2003-04 financial year. This dividend payment will be made in 2004-05. Only part of Telstra's dividend payments are made to the government.

A Monitored GTEs

Table A.1 **Monitored GTEs — by jurisdiction, 2003-04**

GTE	*Sector*
New South Wales	
Delta Electricity	Electricity
Macquarie Generation	Electricity
Eraring Energy	Electricity
TransGrid	Electricity
Country Energy	Electricity
Australian Inland	Electricity
EnergyAustralia	Electricity
Integral Energy	Electricity
Hunter Water Corporation	Water
Sydney Water Corporation	Water
Sydney Catchment Authority	Water
State Transit Authority	Urban Transport
Rail Corporation New South Wales	Railways
Rail Infrastructure Corporation	Railways
Newcastle Port Corporation	Ports
Port Kembla Port Corporation	Ports
Sydney Ports Corporation	Ports
State Forests of New South Wales	Forestry
Victoria	
Barwon Water	Water
City West Water	Water
Gippsland and Southern Rural Water Authority	Water
Melbourne Water Corporation	Water
South East Water	Water
Yarra Valley Water	Water
Coliban Water	Water
Goulburn Valley Water	Water
Central Gippsland Water	Water
Central Highlands Water	Water

(Continued next page)

Table A.1 (continued)

GTE	*Sector*
Wimmera Mallee Water	Water
Goulburn–Murray Water	Water
Sunraysia Rural Water	Water
Port of Melbourne Corporation	Ports
Victorian Channels Authority	Ports
Queensland	
CS Energy	Electricity
Stanwell Corporation	Electricity
Tarong Energy	Electricity
Enertrade	Electricity
Powerlink	Electricity
Ergon Energy	Electricity
Energex	Electricity
Sunwater	Water
Queensland Rail	Railways
Gladstone Port Authority	Ports
Port of Brisbane Corporation	Ports
Cairns Port Authority	Ports
Townsville Port Authority	Ports
Ports Corporation of Queensland	Ports
Mackay Port Authority	Ports
DPI Forestry	Forestry
Western Australia	
Western Power	Electricity
Water Corporation	Water
Public Transport Authority	Railways
Bunbury Port Authority	Ports
Fremantle Port Authority	Ports
Port Hedland Port Authority	Ports
Dampier Port Authority	Ports
Geraldton Port Authority	Ports
Albany Port Authority	Ports
Forest Products Commission	Forestry
South Australia	
SA Water Corporation	Water
TransAdelaide	Urban Transport
ForestrySA	Forestry

(Continued next page)

Table A.1 (continued)

GTE	*Sector*
Tasmania	
Hydro-Electric Corporation	Electricity
Aurora Energy	Electricity
Transend Networks	Electricity
Hobart Regional Water Authority	Water
Cradle Coast Water	Water
Esk Water Authority	Water
Metro Tasmania Pty Ltd	Urban Transport
Burnie Port Corporation	Ports
Hobart Ports Corporation	Ports
Port of Devonport Corporation	Ports
Port of Launceston Pty Ltd	Ports
Forestry Tasmania	Forestry
Australian Capital Territory	
ACTEW Corporation	Water/Electricity
ACTION Authority	Urban Transport
Northern Territory	
Power and Water Corporation	Electricity/Water
Darwin Port Corporation	Ports
Australian Government	
Snowy Hydro	Electricity
Australian Rail Track Corporation	Railways
Airservices Australia	Other Australian Government
Australia Post	Other Australian Government
Telstra Corporation	Other Australian Government

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