



Australian Government
Productivity Commission

Financial Performance of Government Trading Enterprises 2004-05 to 2005-06

Productivity
Commission
Research Paper

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Publications Inquiries:

Media and Publications
Productivity Commission
Locked Bag 2 Collins Street East
Melbourne VIC 8003

Tel: (03) 9653 2244
Fax: (03) 9653 2303
Email: maps@pc.gov.au

General Inquiries:

Tel: (03) 9653 2100 or (02) 6240 3200

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The Productivity Commission

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Foreword

This report on the performance of government trading enterprises (GTEs) is the latest in a series that originally commenced as a wider exercise (the ‘red book’) in 1991, with the Industry Commission as Secretariat. The present series of reports focuses on financial performance, and is undertaken by the Productivity Commission with the cooperation of the Australian, State and Territory Governments. It forms part of the Commission’s research into the performance of Australian industries and the progress of microeconomic reform.

GTEs provide services that are fundamental to the wellbeing of Australians. Further, as recently noted by COAG, it has become increasingly important for both Australia’s export industries and import-competing businesses to have access to infrastructure services that are reliable and competitive by world standards.

Consequently, it is imperative that GTEs, as significant providers of infrastructure services, operate efficiently. Nevertheless, after almost two decades of reform, many GTEs are insufficiently profitable to achieve a commercial rate of return on their assets. Indeed, although governments have given undertakings to operate their businesses on a fully commercial basis, more than half of those monitored continued to earn a return on assets below the risk-free rate.

This picture of under-performance reinforces the need for efficient capital management, which is the focus of some additional research included in this edition.

The study was undertaken in the Economic Infrastructure Branch under the supervision of Chris Sayers and the guidance of Commissioners Michael Woods and Steven Kates. The Commission is grateful for the continuing cooperation of State and Territory governments in the preparation of this annual series.

Gary Banks
Chairman

July 2007

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Abbreviations

AAS	Australian Accounting Standard
AASB	Australian Accounting Standards Board
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ACT	Australian Capital Territory
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
AIFRS	Australian-equivalent International Financial Reporting Standards
ARR	Accounting rate of return
BOOT	Build Own Operate Transfer
BPA	Benchmark Pricing Agreement
COAG	Council of Australian Governments
CPI	Consumer Price Index
CSO	Community service obligation
CWWT	Castlemaine Wastewater Treatment Pty Ltd
DDSO	Digital data service obligation
DORC	Depreciated optimised replacement cost
DRC	Depreciated replacement cost
DTEI	Department of Transport, Energy and Infrastructure (SA)

EBIT	Earnings before interest and tax
ERA	Economic Regulation Authority (WA)
ERR	Economic rate of return
ESC	Essential Services Commission (Victoria)
ESC Act	<i>Energy Services Corporations Act 1995 (NSW)</i>
ETEF	Electricity Tariff Equalisation Fund
FPQO	Forestry Plantations Queensland Office
FRC	Full Retail Contestability
GBE	Government business enterprise
GFS	Government Finance Statistics
GOC	Government-owned corporation
GOC Act	<i>Government Owned Corporations Act 1993 (Queensland)</i>
GPFR	General Purpose Financial Report
GTE	Government trading enterprise
GWh	Gigawatt hour
IC	Industry Commission
ICRC	Independent Competition and Regulatory Commission (ACT)
IDC	Interest during construction
IPART	Independent Pricing and Regulatory Tribunal (NSW)
MCE	Ministerial Council on Energy
MPM	Major periodic maintenance
MW	Megawatt
MWh	Megawatt hour

NCC	National Competition Council
NCP	National Competition Policy
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company
NER	National Electricity Rules
NFPS	National Forestry Policy Statement
NIBLs	Non-interest bearing liabilities
NPV	Net present value
NSW	New South Wales
NT	Northern Territory
NTER	National Tax Equivalent Regime
NWI	National Water Initiative
OTTER	Office of the Tasmanian Energy Regulator
PC	Productivity Commission
PPA	Power-purchase agreement
PTB	Passenger Transport Board
PTE	Public trading enterprise
QCA	Queensland Competition Authority
RAB	Regulatory asset base
RAT	Recoverable amount test
RFAs	Regional Forestry Agreements
SA	South Australia
SGARA	Self-generating and regenerating asset

SMHEA	Snowy Mountains Hydro-Electric Authority
SOC	State-owned corporation
SOC Act	<i>State Owned Corporations Act 1989</i> (NSW)
SOE	State-owned enterprises
TCFA	Tasmanian Community Forest Agreement
TOC	Territory-owned corporation
TRP	Timber release plan
UC	Utilities Commission (NT)
USO	Universal service obligation
WA	Western Australia
WACC	Weighted average cost of capital

PART A

Key points

- The performance of 85 government trading enterprises (GTEs) providing services in key sectors of the economy — including electricity, water, urban transport, railways, ports and forestry — are presented in this report. These GTEs controlled about 3.3 per cent of Australia's non-household assets (\$197 billion), and accounted for around 2 per cent of GDP in 2005-06.
- Overall, the profitability of GTEs increased by 61 per cent in 2005-06 with improvements recorded in all sectors compared with the previous year. The largest improvements were in the electricity, railways and forestry sectors. However, profitability varied among GTEs:
 - profits declined for 37 per cent of GTEs;
 - eleven GTEs (six in the water sector) failed to report a profit; and
 - for most sectors recording a profit improvement, much of this was derived from the performance of only one of the GTEs in that sector (between 39 and 65 per cent of increased profits).
- Although the return on assets improved on average, about half of the monitored GTEs earned less than the long-term bond rate in 2005-06. This implies that an even greater proportion did not earn a commercial rate of return (which would include a margin for risk).
- The poor financial performance of many GTEs underscores a longer-term failure to operate these businesses on a fully commercial basis in accordance with competition policy agreement undertakings.
- In total, GTEs made dividend payments to owner-governments of almost \$5.6 billion in 2005-06 (\$3 billion excluding Telstra). In addition, tax and tax-equivalent payments totalled \$3.3 billion (\$1.9 billion excluding Telstra).
- Asset valuation methods influence capital management through their effect on performance measurement, transparency and accountability. A survey of 58 GTEs revealed that 41 per cent used an historical cost method in 2005-06, even though the optimal deprival value method has been endorsed by governments as the preferred method for valuing GTE assets.
- The economic rate of return (ERR) is a measure of capital management efficiency that has regard for the capital as well as the cash streams of income. The more widely used accounting rate of return (ARR) only captures cash streams of income. Estimates for 56 GTEs over the period 2000-01 to 2003-04 indicate that:
 - many GTEs did not achieve a return on assets exceeding the risk-free rate using either the ERR (42 per cent of GTEs) or the ARR (52 per cent of GTEs); and
 - ERR estimates were higher than those of the ARR.

1 Introduction

This report contains a consistent set of financial performance indicators for 85 government trading enterprises (GTEs) covering the period 2004-05 to 2005-06. It is one in a series of reports commenced in 1991 by the Productivity Commission's predecessor, the Industry Commission.

The monitoring forms part of the Commission's research into the performance of Australian industries and the progress of microeconomic reform. Reporting performance also increases transparency and, thereby, strengthens accountability. In addition, a comparable set of performance indicators can facilitate 'yardstick' competition, which is particularly important in industries where businesses do not face vigorous direct competition.

The information presented in this report covers annual financial performance and management. This information is suitable for making a general assessment of financial performance within and across sectors. It cannot be used for a detailed performance analysis of individual GTEs. A thorough examination of their financial statements and the market circumstances that they face would be required for that purpose.

1.1 Scope

GTEs are government-owned or government-controlled entities that produce goods and services on a commercial basis by substantially or fully covering their costs. They are outside the general government sector and are separate from government financial enterprises in 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, they have specific local and statutory relevance. For example, the term GBE in Tasmania refers to specific entities in schedule 1 of the *Government Business Enterprises Act 1995* (Tasmania), such as Forestry Tasmania and the Hydro-Electric Corporation.

The monitored GTEs represent the majority, but not all, of the GTEs currently operating in their respective sectors. Data for GTEs monitored in previous reports were not included in this report if the GTE was not operating in 2005-06. These GTEs have generally been privatised or had their assets and operations transferred to other GTEs or new entities.

1.2 Approach

Performance indicators for each monitored GTE were derived from a data collection that is broadly consistent over time and across jurisdictions.

Financial performance indicators

Financial performance indicators provide an overall picture of how a GTE is performing over time as well as relative to other GTEs. These indicators are presented under three broad headings — profitability, financial management and transactions with government.

Generally, it is reasonable to make comparisons across GTEs in the same sector in Australia. However, in comparing performance within a sector, the broad range of activities undertaken by GTEs has to be taken into account. For example, Horizon Power (WA) and Power and Water (NT) were vertically integrated electricity GTEs during the reporting period — 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 might also provide useful benchmarks against which the performance of GTEs can be compared.

Profitability indicators

Profitability indicators are 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.¹ Profitability indicators provide governments and the community with a means of evaluating how well GTEs are using the assets vested in them.

Profitability, however, can be affected by factors outside the control of GTEs. For example, the weather impacts on the revenue of many GTEs in the water and electricity sectors. This can significantly affect profitability from year to year, particularly as many GTEs have relatively high fixed costs.

The five profitability indicators used in this report are listed in box 1.1 along with an explanation of what they represent and how they are interpreted. Definitions for data items used in the estimation of these indicators are provided in attachment 1.1.

Box 1.1 Profitability indicators

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).

$$\text{Operating Profit Before Tax} = \text{Total Revenue} - \text{Total Expenses}$$

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.

$$\text{Operating Sales Margin} = \frac{\text{EBIT} - \text{Investment Income}}{\text{Total Revenue} - \text{Investment Income}}$$

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.

$$\text{Cost Recovery} = \frac{\text{Revenue from Operations}}{\text{Expenses from Operation}}$$

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.

(Continued next page.)

¹ If a company is listed on the stock exchange, the market assessment of the value of its equity is generally expressed through the price of its shares. Expected returns are capitalised into the value of the company through movements in its share price which encapsulates, at any particular time, investors' views of its current and prospective financial performance.

Box 1.1 (continued)

The return on assets is affected by changes in asset values arising from asset revaluations, transfers or sales. Some GTEs use different asset valuation methods, 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 they do not properly incorporate the actual cost of depreciation and might lead to imperfect measures of the rates of return on assets.

$$\text{Return on Assets} = \frac{\text{EBIT}}{\text{Average Total Assets}}$$

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.

$$\text{Return on Equity} = \frac{\text{Operating Profit After Tax}}{\text{Average Total Equity}}$$

Financial management

Debt is a major source of funds from which GTEs finance their activities. 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 capital structure is poorly managed.

Financial management indicators provide information on the extent to which debt is used to finance a GTE's assets, and the GTE's ability to meet periodic interest payments and short-term liabilities.

Various factors — including the impact of government directives, changes in asset values and financial restructuring — should be taken into account when assessing financial management performance, particularly over time.

The debt to equity ratio, for example, is affected by changes in liabilities as equity is a residual measure obtained by deducting total liabilities from total assets. 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.

The six financial management indicators used in this report are listed in box 1.2 along with an explanation of what they represent and how they are interpreted. Definitions for data items used in the estimation of these indicators are provided in attachment 1.1.

Box 1.2 Financial management indicators

Debt to equity ratio — is an indicator of the risk associated with 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 wholly-owned GTEs).

$$\text{Debt to Equity Ratio} = \frac{\text{Debt}}{\text{Total Equity}}$$

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.

$$\text{Debt to Total Assets Ratio} = \frac{\text{Debt}}{\text{Average Total Assets}}$$

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.

$$\text{Total Liabilities to Equity Ratio} = \frac{\text{Total Liabilities}}{\text{Total Equity}}$$

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.

$$\text{Interest Cover} = \frac{\text{EBIT}}{\text{Gross Interest Expense}}$$

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.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

(Continued next page.)

Box 1.2 (continued)

Leverage ratio — is an indicator of an entity's ability to meet long-term debt through the disposal of current and non-current assets. A ratio greater than 100 per cent means that some of the fixed assets are financed by debt. A negative ratio indicates that liabilities exceed assets.

$$\text{Leverage Ratio} = \frac{\text{Total Assets}}{\text{Total Equity}}$$

Transactions with government

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

Changes in policies and practices by GTEs and governments over the reporting period can sometimes make comparisons difficult. For example, prior to July 2005, the Victorian Government required rural water GTEs to achieve a 4 per cent return on assets used for bulk water services to regional urban authorities. This revenue was used to fund dividend payments to government as well as activities such as water quality monitoring and provision of recreational facilities at storages. Subsequently, the *Securing our Water Future Together* white paper announced the Victorian Government's decision to:

- forgo the dividend paid by rural authorities attributable to the 4 per cent rate of return in the 2005-06 financial year; and
- implement alternative arrangements for activities previously funded by the 4 per cent rate of return revenue, by 1 July 2005 (DSE 2004).

The five indicators used in this report to measure transactions with government are listed in box 1.3, along with an explanation of what they represent and how they are interpreted. Definitions for data items used in the estimation of these indicators are provided in attachment 1.1.

Data

The data used in calculating the financial performance indicators for 2004-05 to 2005-06 were taken from General Purpose Financial Statements reported in published annual reports. This represents a departure from the approach adopted for previous reports (see section 1.3 for a discussion of this change).

Box 1.3 **Transactions with government indicators**

Dividends — are the value of funds transferred from present and past after-tax profits of an entity to its owners. Dividends are generally 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.

Dividends are typically provided for in the year that they accrue but can be declared and provided for in the following year. Alternatively, an interim dividend for a financial year can be provided for in the year that it accrues and a final dividend is then provided for in the subsequent year.^a

Unless noted otherwise, dividends for the financial year were not adjusted or re-allocated to previous years to take account of changes in practices or policies.

Dividend to equity ratio — is an indicator of the size of an entity's dividend payments relative 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.

$$\text{Dividend to Equity Ratio} = \frac{\text{Dividends Paid or Provided For}}{\text{Average Total Equity}}$$

Dividend payout ratio — is an indicator of the size of an entity's dividend payments relative to its profits. 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.

$$\text{Dividend Payout Ratio} = \frac{\text{Dividends Paid or Provided For}}{\text{Operating Profit After Tax}}$$

Income tax expense — is the value of tax or tax-equivalent expenses payable 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.

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

Unless otherwise stated, the data presented in this report are in nominal values — amounts denominated in terms of values at a particular point in time using 'dollars

of the day'. Where changes in real (inflation adjusted) values are reported, nominal values were adjusted to their 2005-06 values using a price deflator.

The ABS *implicit price deflator for gross fixed capital formation — public corporations* was used to convert nominal into real data. It was judged to most closely reflect the underlying cost structure of GTEs. However, there are alternative measures of price change that could have been used, which would have resulted in different real values (table 1.1).

Table 1.1 **Selected deflators, (Index 2005-06 = 100)**

Year	Implicit price deflator			Consumer price index
	Gross fixed capital formation (public corporations)	Final consumption expenditure (other government)	Gross domestic product	All groups (Australia)
2001-02	92.6	86.0	85.6	89.2
2002-03	91.7	88.6	88.4	91.6
2003-04	91.8	90.4	91.5	93.8
2004-05	95.5	94.7	95.7	96.2
2005-06	100.0	100.0	100.0	100.0

Source: ABS (2007b, 2007c).

Consultation

State and Territory governments were given the opportunity to comment on the individual GTE reports to ensure accuracy of the information presented.

1.3 Performance comparisons over time

Care should be exercised when comparing performance measures presented in this report with those presented in previous reports. Comparisons over time are affected by changes in accounting standards and data sources.

Change in accounting standards

Most GTEs reported under the new Australian-equivalent International Financial Reporting Standards (AIFRS) for the first time for the 2005-06 financial year. As foreshadowed in last year's report, this change in standard has significantly affected some of the data items used to measure performance (PC 2006, chapter 3). For example, recognition and measurement of assets, liabilities and equity items in the

statement of financial position are affected by changes to accounting standards relating to:

- fair value or revaluation as deemed cost;
- financial instruments;
- income tax (tax-equivalent regimes) assets and liabilities;
- intangible assets; and
- investment properties.

Measures of revenue and expenses are affected by changes to accounting standards relating to impairment write-downs and pension accounting. There are numerous changes to other standards — such as leases, borrowing costs, grant accounting — and the accounting choices available within individual standards, that also impact on GTEs financial data.

An analysis of 2004-05 data reveals that the indicators are affected to such an extent that those derived from AIFRS and pre-AIFRS data are not always comparable (figure 1.1). It was therefore decided to break the series and report performance for 2005-06 and 2004-05 using AIFRS financial reporting data.

Change in data sources

Performance was measured in previous reports using data taken from two sources:

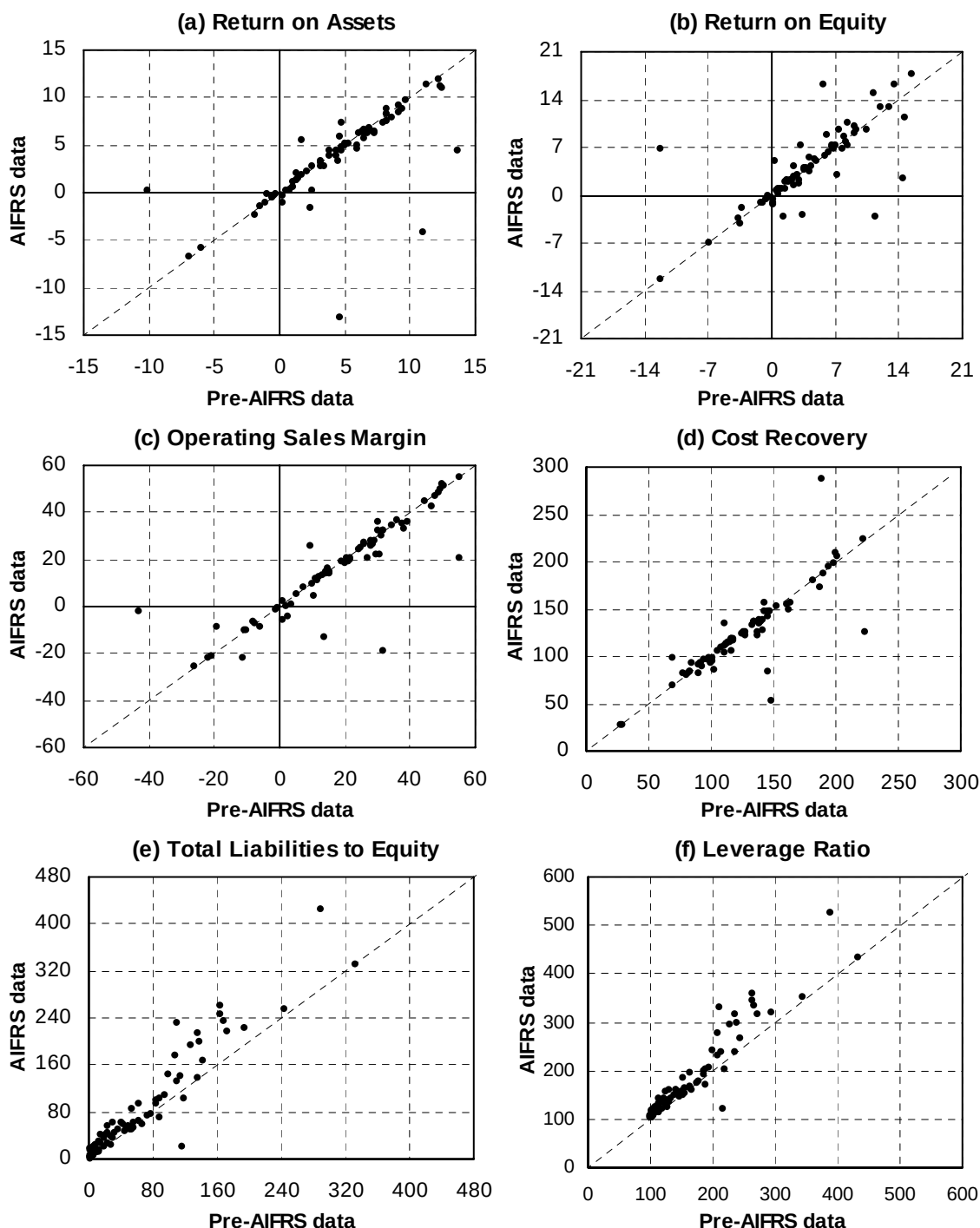
- the Government Finance Statistics (GFS) collection — which was used for most indicators; and
- General Purpose Financial Report (GPFR) data from audited GTE financial statements — which were used where data from GFS were not available.

This resulted in some confusion because performance measures based on published financial statements could not always be reconciled with those presented in this report series.

Although data from the GFS collection have advantages (including consistency with the economic accounting used in the National Accounts), there are also a number of disadvantages, namely:

- not all the required data were obtainable from the GFS transaction-based system of accounting, necessitating the use of some GPFR;
- the differences between the treatment of items under the GPFR and GFS framework resulted in significant differences in measured performance, albeit in a small number of cases; and

Figure 1.1 Implications of transition to Australian-equivalent International Financial Reporting Standards for selected performance indicators, 2004-05^a (Per cent)



^a Derived from Australian-equivalent International Financial Reporting Standards (AIFRS) and Pre-AIFRS data reported in published 2005-06 annual reports. Observations on the 45° line indicate that the indicators are identical when estimated using either data set. Observations above the 45° line indicates that indicator values are higher using AIFRS data. Some outlier observations have been excluded for data presentation purposes.

Source: Productivity Commission estimates

-
- the reported performance measures could not always be reproduced by others who had access only to financial statements.

Given the disadvantages associated with data from the GFS collection, it was decided to report performance for 2004-05 and 2005-06 using published GPFR financial reporting data.

1.4 Capital management research

The Commission is currently undertaking a program of research into GTE capital management in conjunction with the financial performance monitoring. Capital management was identified as warranting closer analysis given that most GTEs have capital intensive operations. Improvements to capital productivity arguably offer the greatest scope for further gains in financial performance. Labour productivity has been substantially improved as a result of past reforms.

The topics covered in the previous report were GTE capital structures and equity withdrawals (PC 2006). The areas covered this year are:

- implication of trends in asset valuation methods for measuring asset performance (chapter 3); and
- economic rates of return on assets (chapter 4).

Assets valuation methods influence the measurement of capital structure and the efficient use of capital. There have been a number of changes since the Commission last reviewed asset valuation methods — including the implementation of the AIFRS. The research in chapter 3 provides a record of trends in asset valuation methods across time as well as comparison across jurisdictions and sectors, and how these trends might influence the interpretation of performance.

The research in chapter 4 was undertaken to investigate whether economic rate of return provides insight into the performance of GTEs that was additional to that provided by accounting rates of return.

1.5 Report structure

For the remainder of this part of the report, Part A, an overview of the financial performance of the monitored GTEs over the last two years is presented in chapter 2. The findings of the research into trends in asset valuation methods and economic rates of return are presented in chapters 3 and 4 respectively.

In Part B, GTE performance reports are presented by sector, with commentary on the influence of structural reforms and the market environment on performance. State and Territory treasury departments were given the opportunity to review these performance reports.

Attachment 1.1 Data item definitions

Definitions for data items used to estimate the financial performance indicators reported in this report are provided in table 1.2.

Table 1.2 Data item definitions

<i>Data item</i>	<i>Definition</i>
Average total assets	Average of the value of assets at the beginning and end of the reporting period.
Average total equity	Average of total equity at the beginning and end of the reporting period
Current assets	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.
Current liabilities	Liabilities that would, in the ordinary course of operations, be due and payable within 12 months after the end of the reporting period.
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).
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.
Earnings before interest and tax (EBIT)	Operating profit before income tax plus gross interest expense.
EBIT from operations	Operating profit before income tax plus gross interest expense less investment income.
Expenses from operations	Total expenses less abnormal expenses and gross interest expense.
Gross interest expense	Amount charged to the profit and loss account. Includes finance charges on finance leases and all debt related financial expenses.
Income tax	Income tax expense, or income tax-equivalent expense, on operating profit before tax (including abnormal items) calculated using tax effect accounting (AAS3).
Investment income	Income received and receivable on financial assets.
Operating profit before income tax	Total revenue less total expenses
Receipts from Government to cover deficits on operation	Receipts from governments to cover deficits on operations, but excludes receipts from governments for specific agreed services (for example, community service obligations).

(Continued next page.)

Table 1.2 (continued)

<i>Data item</i>	<i>Definition</i>
Revenue from operations	Total revenue less abnormal revenue, investment income and receipts from governments to cover deficits on operations.
Total assets	Provides an indicator of 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).
Total equity	Total assets less total liabilities.
Total expenses	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.
Total liabilities	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.
Total revenue	Includes revenue from sales and levies, revenue from asset sales, investment income, receipts from governments for specific agreed services (such as community service obligations), other revenue from operations, receipts from governments to cover deficits on operations and abnormal revenue. Excludes equity contributions from governments.

2 Financial performance overview

An overview of the financial performance of the monitored GTEs over the period 2004-05 to 2005-06 is provided in this chapter. Detailed assessments of the performance of each sector and of individual monitored GTEs are included in part B of this report.

GTE performance is 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 — can be found in chapter 1.

2.1 Monitored GTEs

The 85 GTEs monitored in this report undertake a range of activities across six sectors — electricity, water (which includes sewerage, drainage and irrigation services), urban transport, railways, ports and forestry (table 2.1). Three Australian Government trading enterprises that do not fit within these sectors — Airservices Australia, Australia Post and Telstra — are reported separately.

Table 2.1 **Monitored GTEs, by sector and jurisdiction, 2005-06**

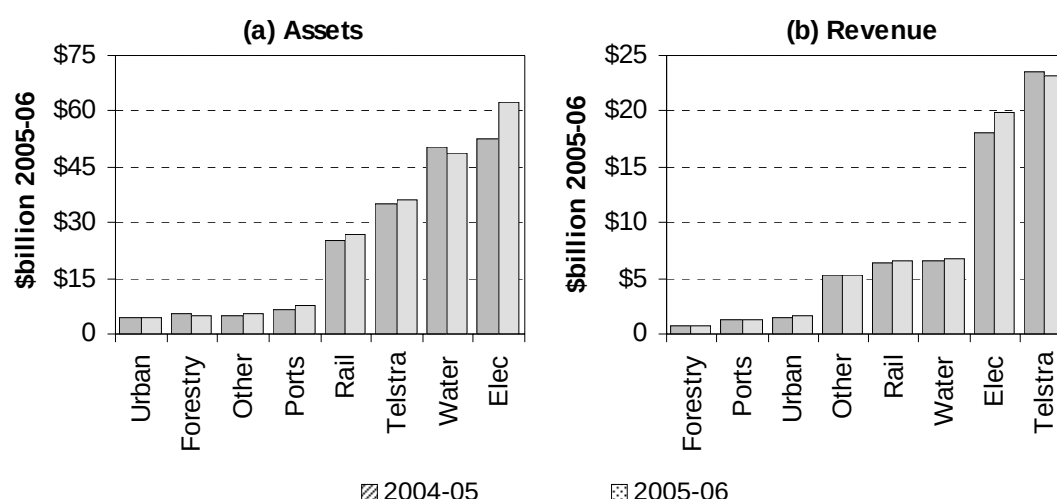
	<i>NSW</i>	<i>Vic</i>	<i>Qld</i>	<i>WA</i>	<i>SA</i>	<i>Tas</i>	<i>ACT</i>	<i>NT</i>	<i>Aust Govt</i>	<i>Total</i>
Electricity (chapter 5)	7	–	7	4 ^a	–	3	–	1	1 ^b	23
Water (chapter 6)	3	13	1	1	1	3	1	–	–	23
Urban transport (chapter 7)	2	–	–	1	1	1	1	–	–	6
Railways (chapter 8)	2	1	1	–	–	–	–	–	1	5
Ports (chapter 9)	3	2	6	6	–	1 ^c	–	1	–	19
Forestry (chapter 10)	1	1	1 ^d	1	1	1	–	–	–	6
Other (chapter 11)	–	–	–	–	–	–	–	–	3 ^e	3
All	18	17	16	13	3	9	2	2	5	85

^a Four GTEs — Verve Energy, Western Power, Synergy and Horizon Power — were included for the first time in this report. These GTEs were formed when the WA Western Power Corporation was disaggregated on 1 April 2006. ^b Snowy Hydro, which is jointly owned by the Australian, NSW and Victorian Governments. ^c Tasmanian Ports Corporation is included for the first time in this report. It commenced trading on 1 January 2006 following the amalgamation of Burnie Port Corporation, Hobart Ports Corporation, Port of Devonport Corporation and Port of Launceston Pty Ltd. ^d Forestry Plantations Queensland is included for the first time in this report. It was established on 1 May 2006 when the functions and responsibilities of the former DPI Forestry were disaggregated into Forestry Plantations Queensland and Forestry Plantations Queensland Office. ^e Includes Airservices Australia, Australia Post and Telstra. – Zero or rounded to zero.

Six GTEs are monitored for the first time in this report (four in the electricity sector, one in the ports sector and one in the forestry sector). These GTEs were created as a result of the restructuring of GTEs monitored in previous reports.

Government-owned businesses contributed just over 2 per cent to Australia's GDP in 2005-06 (ABS 2006a). The monitored GTEs controlled assets valued at \$197 billion¹ and generated \$65 billion in revenue in 2005-06 (figure 2.1). In aggregate, they account for around 92 per cent of the revenue generated by all government-owned businesses in Australia (ABS 2007d).

Figure 2.1 Assets and revenue by sector, (\$billion 2005-06)^{a,b}



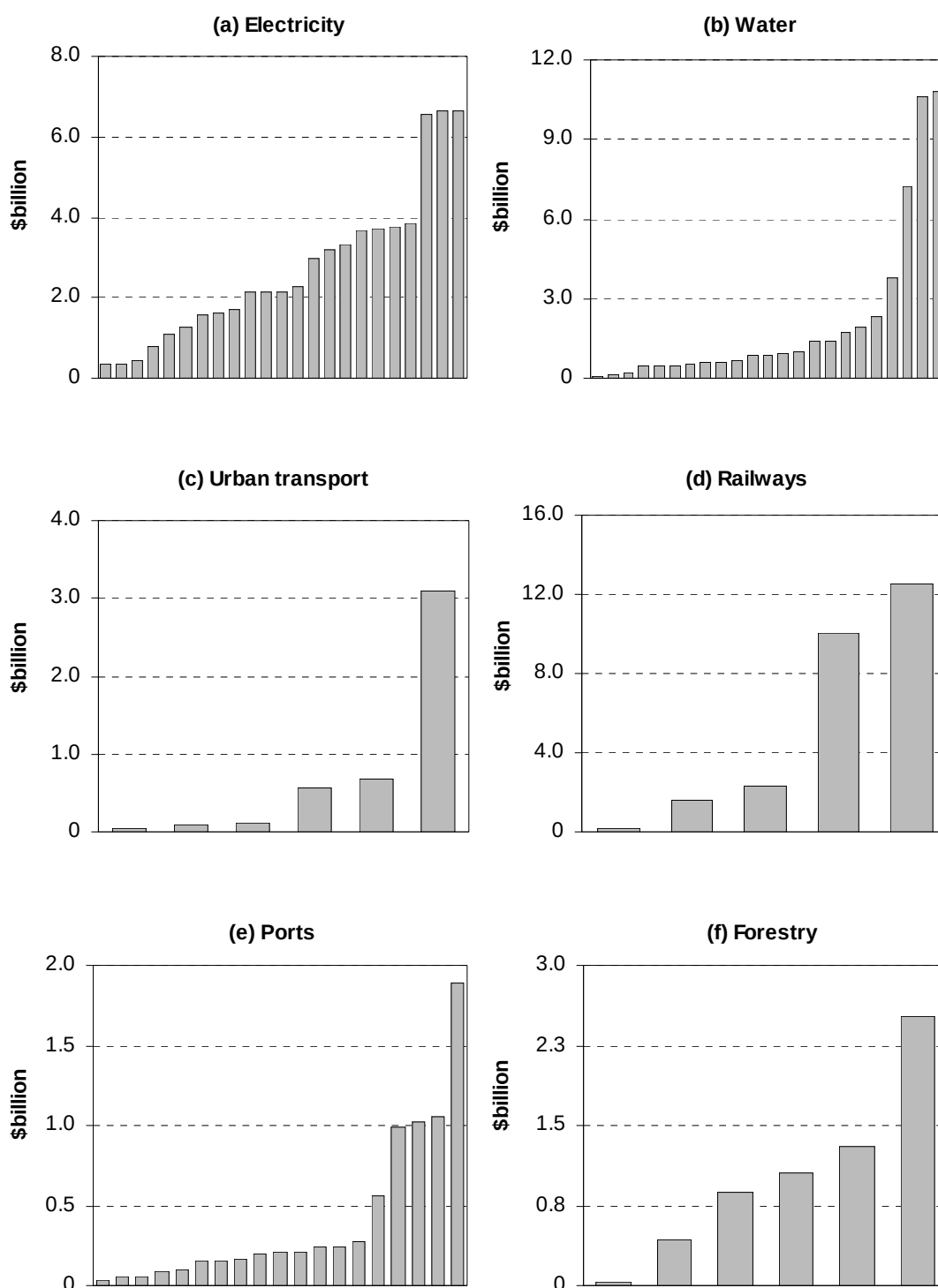
^a The values of sector assets for 2004-05 were converted to 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1). ^b **Other** Includes Airservices Australia and Australia Post (Telstra is reported separately). **Elec** Electricity sector GTEs.

Source: Productivity Commission estimates.

The size of monitored GTEs — measured in assets — varies substantially across and within sectors (figure 2.2). In 2005-06, the smallest in terms of asset value was VicForests (\$35 million) and the largest was Telstra (\$36 billion). Telstra accounted for 18 per cent of the monitored GTEs' total assets and the largest eight GTEs accounted for around 51 per cent.

¹ This represented about 1.7 per cent of total assets or 3.3 per cent of non-household assets in Australia at 30 June 2006 (ABS 2006a).

Figure 2.2 Assets — monitored GTEs by sector, 2005-06^a



^a Three monitored Australian Government trading enterprises that do not fit within these six sectors — Australia Post (assets \$4.8 billion), Airservices Australia (\$707 million) and Telstra (\$36 billion) — are excluded from this figure.

Source: Productivity Commission estimates.

2.2 Market environment

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 — is affected by differences in operating conditions. These differences include variations in the demand for a GTE's goods and services and the costs of production.

The pursuit of non-commercial objectives can also affect the financial performance of GTEs. If a GTE is directed to undertake community service obligations (CSOs) without adequate funding, its financial performance will suffer — especially in the urban and railways transport sectors where the payments would otherwise contribute a significant proportion of total revenue.

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

Regulators determine prices to provide a return on the regulatory asset base (RAB). However, the value of the RAB can vary from that of the accounting asset base because of exclusions from the RAB (such as contributions and gifted assets), and 'line-in-the-sand' approaches to setting initial regulatory asset values. For example, the Victorian Government excludes all investments prior to 1 July 2004 from the initial RAB of rural water GTEs (DSE 2004). Where the RAB excludes assets that have an economic value, prices might be set at levels below that necessary to earn an appropriate rate of return on the GTE's own valuation of assets.

The valuation of assets, and the frequency of revaluation, can also affect the reported financial performance of GTEs. Forestry GTEs, for example, are affected annually by revaluations of growing timber assets, the effect of which is written directly into the statement of financial performance (chapter 10).

Infrequent asset revaluations affect measured performance in two ways. First, the divergence between the book value and economic value of assets (and therefore between measured and actual performance) is likely to increase with the interval since the most recent valuation. Second, the size of revaluation is likely to increase with greater intervals between revaluations (resulting in volatility in measured performance over time).

2.3 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 a business. If equity holders (the community, in the case of GTEs) are to obtain a full financial return on their investment, profits have to be sufficient to generate a return similar to that available from alternative investments with similar risk profiles. In this report, profitability measures include the level of operating profit, the return on assets (and equity), and the cost recovery ratio as defined in chapter 1.² The economic rate of return, which provides an alternative measure of performance, is reported in chapter 4.

The monitored GTEs reported a total pre-tax operating profit of \$6.2 billion in 2005-06, representing a 61 per cent (\$2.4 billion) increase in real (inflation-adjusted) terms from 2004-05. Although operating profits increased, in real terms, in all sectors between 2004-05 and 2005-06, results varied significantly for individual GTEs (table 2.2).

In the water sector, for example, pre-tax operating profit declined between 2004-05 and 2005-06 for almost half (11) of the monitored GTEs, while the sector-wide increase was 25 per cent. In addition, 61 per cent of the increase in pre-tax operating profit was attributable to one GTE (Sydney Water Corporation). Despite the overall sector improvement, one-quarter of water GTEs reported pre-tax operating losses in 2005-06.

The overall financial performance of all sectors generally improved in 2005-06, with the largest improvements in the electricity, railways and forestry sectors. However, despite improvements in operating profit and return on assets (and equity), the cost recovery ratio for the urban transport and railways sectors declined marginally (table 2.3). Cost recovery ratios of less than 100 in these two sectors arose because revenue from operations was insufficient to cover expenses from operations.

A commercial rate of 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.

² The three monitored Australian Government trading enterprises — Australia Post, Airservices Australia and Telstra — that do not fit within the six broad sector categories are excluded from commentary in this section. The performance of these GTEs is discussed in chapter 11. The six monitored GTEs that did not operate in both 2004-05 and 2005-06 are also excluded.

Table 2.2 Real change in pre-tax operating profit between 2004-05 and 2005-06^a

	<i>Declines^b</i>			<i>Increases^c</i>			<i>Net change^d</i>		<i>GTEs making profits^e</i>
	<i>Amount</i>	<i>GTEs</i>	<i>Share of largest</i>	<i>Amount</i>	<i>GTEs</i>	<i>Share of largest</i>			
	\$million	no.	%	\$million	no.	%	\$million	%	no.
Electricity	-83	5	28.9	1 451	14	40.6	1 368	90.4	18
Water	-59	11	32.5	485	12	60.6	427	25.3	17
Urban	-84	3	55.8	86	3	60.8	2	32.6	4
Railways	-171	2	96.9	571	3	38.8	400	142.3	4
Ports	-68	6	76.9	115	12	65.3	46	12.2	17
Forestry ^f	-11	1	100.0	118	4	41.5	107	na	5
All	-476	28	na	2 827	48	na	2 351	60.9	65

^a Excludes six GTEs that did not operate in 2004-05 and 2005-06. Also excludes three monitored Australian Government trading enterprises — Australia Post, Airservices Australia and Telstra — that do not fit within the six broad sector categories. ^b **GTEs** refers to the number of monitored GTEs reporting a decline in pre-tax operating profit between 2004-05 and 2005-06. **Share of largest** is the proportion of total sector decline in pre-tax operating profit between 2004-05 and 2005-06 that is attributable to the GTE reporting the largest decline in dollar terms. ^c **GTEs** refers to the number of monitored GTEs reporting an increase in pre-tax operating profit between 2004-05 and 2005-06. **Share of largest** is the proportion of total sector increase in pre-tax operating profit between 2004-05 and 2005-06 that is attributable to the GTE reporting the largest increase in dollar terms. ^d Total increases in pre-tax operating profit less total declines in pre-tax operating profit. The percentage change is the net change compared to total sector pre-tax operating profits in 2004-05, measured in 2005-06 dollars. ^e Number of monitored GTEs reporting a pre-tax operating profit in 2005-06. ^f The percentage change is not available for the forestry sector as it improved from a sector loss in 2004-05 to a sector profit in 2005-06. **na** Not available.

Source: Productivity Commission estimates.

Table 2.3 Selected profitability measures, by sector (per cent)^a

<i>Sector</i>	<i>Return on assets</i>		<i>Return on equity</i>		<i>Cost recovery</i>	
	<i>2004-05</i>	<i>2005-06</i>	<i>2004-05</i>	<i>2005-06</i>	<i>2004-05</i>	<i>2005-06</i>
Electricity ^a	5.2	7.8	5.2	10.1	117.2	126.8
Water	4.4	5.5	3.3	4.2	148.9	163.5
Urban	2.6	3.0	0.4	0.5	69.9	66.4
Railways	2.2	3.8	1.3	3.9	93.9	93.7
Ports	6.7	7.1	5.8	6.8	156.9	159.2
Forestry (excl. FPQ)	0.1	2.3	-0.7	1.8	99.0	115.4

^a Excludes data for the WA Western Power Corporation which was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. Comparisons between 2004-05 and 2005-06 would have been misleading because the data for the new entities were available only for the period 1 April 2006 to 30 June 2006.

Source: Productivity Commission estimates.

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 2005-06 was 5.4 per cent (RBA 2007a).³ Given the non-diversifiable risk inherent in any business activity, it is reasonable to expect that GTEs should be generating returns on assets above the risk-free rate.⁴

Only 49 per cent of monitored GTEs earned a pre-tax return on assets above the 10-year bond rate (5.4 per cent) in 2005-06. This is an improvement on the 39 per cent of monitored GTEs that achieved a return greater than the risk-free bond rate in 2004-05.

The proportion of monitored GTEs that achieved a negative return on assets decreased from 21 per cent in 2004-05 to 14 per cent in 2005-06. Thirty-six per cent of those GTEs with a zero or negative return, operated in the water sector. Profitability also varied considerably between and within sectors in 2005-06 (figure 2.3).

2.4 Financial management

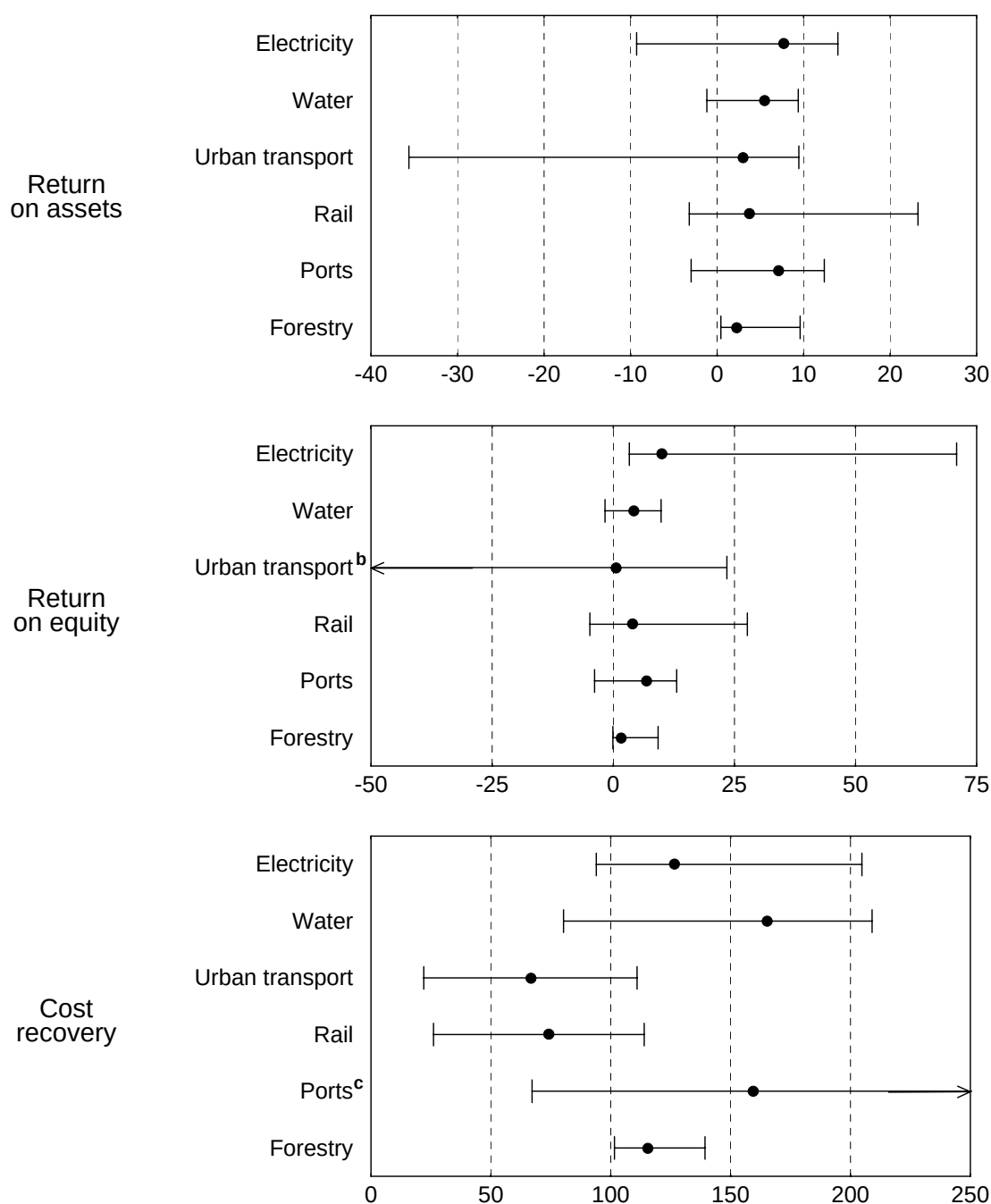
The financial management indicators in this report provide information about the capital structure of GTEs and their ability to meet the costs of servicing debt and other liabilities as they fall due. Further information on these indicators is provided in chapter 1.

The average debt level of GTEs monitored for both 2004-05 and 2005-06 increased by 4 per cent in real terms (table 2.4). The greatest increases were in the electricity, water, railways and ports sectors where average debt increased by 6 per cent (\$58 million), 9 per cent (\$34 billion), 12 per cent (\$98 billion) and 13 per cent (\$10 million) respectively. Debt was relatively stable for the urban transport sector and Telstra, reporting increases of less than 3 per cent. For the forestry sector, as well as for Australia Post and Airservices Australia, real debt declined.

³ Based on the average daily rate over the 12 months to June 2006. The rate is usually based on the average bond rate over a specified period (12 months) rather than the 'on the day' rate at 30 June 2006, in order to minimise the effect of short-term volatility.

⁴ 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, the NSW Independent Pricing and Regulatory Tribunal accepted a nominal post-tax return of between 6 per cent and 7 per cent for electricity distributors over the period February 2004 to June 2008 (IPART 2004).

Figure 2.3 Selected profitability measures, by sector in 2005-06 (per cent)^a



^a The dot represents the weighted mean value and the 'whiskers' represent the range of values for a given performance indicator. For example, for the electricity sector, the lowest return on assets was -9 per cent, the highest value was 14 per cent and the weighted mean return on assets was 8 per cent. ^b The lowest return on equity ratio for the urban transport sector was -81 per cent. ^c The highest cost recovery ratio for the ports sector was 328 per cent.

Source: Productivity Commission estimates.

More than 44 per cent of monitored GTEs decreased their real debt level between 30 June 2005 and 30 June 2006. This decline was attributable to a number of factors, including debt reduction programs, reduced capital expenditure and the partial privatisation of some businesses. Ten GTEs carried no debt at 3 Jun 2006 (the same number as at 3 Jun 2005, but different GTEs) (table 2.4).⁵

Table 2.4 Debt levels of monitored GTEs (\$2005-06)

	2004-05		2005-06		GTEs with no debt ^a		Monitored GTEs ^c
	Total	Average ^b	Total	Average ^b	2004-05	2005-06	
	\$million	\$'000	\$million	\$'000	no.	no.	no.
Electricity ^d	18 687	983 530	19 790	1 041 603	1	1	19
Water ^e	8 895	386 751	9 683	421 020	2	2	23
Urban transport ^f	1 895	315 827	1 932	322 022	—	—	6
Railways ^g	4 031	806 217	4 519	903 771	3	3	5
Ports ^h	1 367	75 950	1 540	85 539	4	4	18
Forestry ⁱ	279	55 853	274	54 800	—	—	5
Australian Govt. ^j	13 696	4 565 397	14 012	4 670 673	—	—	3
<i>All monitored GTEs</i>	<i>48 851</i>	<i>7 189 525</i>	<i>51 751</i>	<i>7 499 428</i>	<i>10</i>	<i>10</i>	<i>79</i>

^a Different GTEs were debt free in 2004-05 and 2005-06. ^b Averages are based on the number of GTEs that carried debt at 30 June. ^c Six GTEs monitored in this report did not operate for 2004-05 and 2005-06. ^d Eight GTEs account for more than 77 per cent of electricity sector debt. ^e Four GTEs account for more than 71 per cent of water sector debt. ^f The WA Public Transport Authority accounts for more than 89 per cent of urban transport sector debt. ^g Queensland Rail accounts for more than 99 per cent of railways sector debt. ^h Five GTEs account for more than 74 per cent of port sector debt. ⁱ Forests NSW accounts for close to 40 per cent of forestry GTE debt. ^j Telstra accounts for more than 95 per cent of Australian Government trading enterprises debt. — Zero or rounded to zero.

Source: Productivity Commission estimates.

Although the debt levels of about half of the GTEs monitored for both 2004-05 and 2005-06 increased, this was offset by the growth in assets. As a consequence, the aggregate debt to asset ratio for monitored GTEs (excluding Telstra) remained unchanged at 24 per cent between 2004-05 and 2005-06.

The weighted average debt to equity ratio for the monitored GTEs increased from 42 per cent in 2004-05 to 48 per cent in 2005-06. However, the ratio varied considerably between sectors — ranging from 7 per cent in the forestry sector to 100 per cent in the urban transport sector in 2005-06 (table 2.5).

⁵ Absence of debt is not *prima facie* evidence of good financial management as a GTE might be missing opportunities to increase earnings by financing projects that would give a better return than the cost of the debt.

In 2005-06, interest cover increased in all sectors, with the exception of the urban transport sector (table 2.5). The substantial increase in the forestry sector's weighted average interest cover since 2004-05 reflects increased profits rather than a decline in debt for that sector. Financial management performance indicators also varied considerably within each sector (figure 2.4).

Caution is required when comparing financial management indicators over time because changes in the capital structure of GTEs — including those arising from valuation methods and revaluations — affect inter-temporal performance comparisons (chapter 1).

Table 2.5 Selected financial performance measures, by sector (per cent)^a

<i>Sector</i>	<i>Debt to equity</i>		<i>Current ratio</i>		<i>Interest cover</i>	
	<i>2004-05</i>	<i>2005-06</i>	<i>2004-05</i>	<i>2005-06</i>	<i>2004-05</i>	<i>2005-06</i>
Electricity ^a	93.9	97.0	62.7	70.8	2.2	3.3
Water	24.8	28.6	52.1	51.1	4.1	4.7
Urban transport	121.1	100.3	21.1	8.2	1.1	1.1
Railways	22.4	24.8	110.5	112.3	2.0	3.3
Ports	31.2	32.9	175.6	183.3	5.6	5.8
Forestry ^b	7.3	7.4	135.8	179.8	2.1	12.2

^a Excludes data for the WA Western Power Corporation which was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. Comparisons between 2004-05 and 2005-06 would have been misleading because data for the new entities were available only for the period 1 April 2006 to 30 June 2006. ^b FPQ is excluded from all measures. SFNSW is excluded from interest cover.

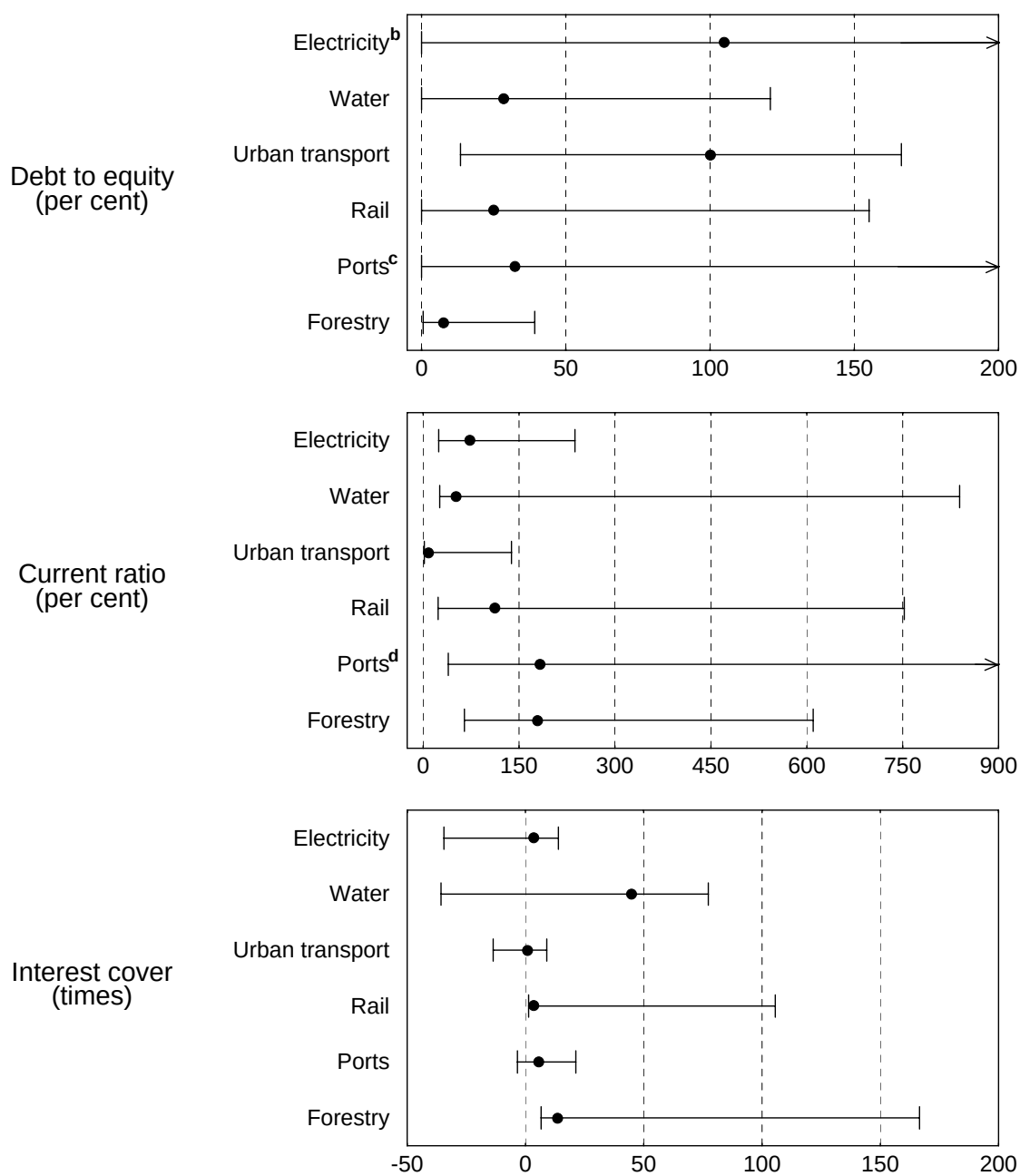
Source: Productivity Commission estimates.

2.5 Transactions with government

In 1995, the Council of Australian Governments endorsed the corporatisation of GTEs, as part of a range of reforms under the Competition Principles Agreement. An objective of the Agreement was to enhance the efficient allocation of resources by removing any competitive advantage that government-owned businesses have as a result of public ownership. Accordingly, governments re-committed to tax-equivalent payments and debt guarantee fees for all significant GTEs, where the benefits outweighed the costs.

The dividend, tax-equivalent and CSO payments of GTEs are examined in the following sections. For more information, see chapter 1.

Figure 2.4 Selected financial management indicators, by sector, 2005-06^a



^a The dot represents the weighted mean value and the 'whiskers' represent the range of values for a given performance indicator by sector. ^b The highest debt to equity ratio for the electricity sector was 266 per cent. ^c The highest debt to equity ratio for the ports sector was 617 per cent. ^d The highest current ratio for the ports sector was 1180 per cent.

Source: Productivity Commission estimates.

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 commercial rate of return (after-tax) as its competitors with lower prices or higher operating costs.

Since June 2001, most GTEs have been subject to the National Tax Equivalent Regime (NTER).⁶ The NTER unified the tax equivalent arrangements of GTEs that were previously subject to the 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 2006, p. 6).

In 2005-06, the monitored GTEs recorded almost \$3.3 billion in tax-equivalent expenses to governments, of which Telstra contributed 42 per cent. The remaining GTEs each recorded an average of approximately \$23 million. Total tax-equivalent expenses (excluding Telstra) were 49 per cent (\$633 million) higher than the previous year.

Dividends

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

In 2005-06, 57 GTEs declared dividends to their owner-governments, one more than in the previous year. Total dividends paid or provided for were just over \$5.7 billion. Over 45 per cent of this payment came from the Australian Government's then 52 per cent share of Telstra's \$5 billion dividend.

Total dividends for all GTEs monitored in 2005-06 increased by 18 per cent (\$878 million), largely because of an increased dividend payment by Telstra. Excluding Telstra, total dividends increased by 17 per cent (\$439 million) from 2004-05.

⁶ Australian Government-owned entities pay income tax to the Australian Taxation Office.

The weighted average dividend to equity ratio for monitored GTEs was 8.2 per cent in 2005-06 compared with 7.1 per cent in 2004-05. Excluding Telstra, the dividend to equity ratio increased from 3.2 per cent in 2004-05 to 3.6 per cent in 2005-06.

Eight GTEs in 2005-06 (10 in 2004-05), mainly in the water and forestry sectors, reported dividend payout ratios of over 100 per cent. This indicates that dividends paid or provided for exceeded operating profit (after tax) in that year. It implies that the GTE might be required to fund the dividend payment from previous years' retained earnings or by borrowing.

Some GTEs (10 in 2004-05 and three in 2005-06) made dividend payments after reporting after-tax operating losses, resulting in negative dividend payout ratios. This can be explained by GTEs being required by their owner-governments to pay pre-determined special dividends of a given amount regardless of after-tax operating profits. Negative dividend payout ratios can also occur when dividend payments during the year are based on prior year operating results.⁷

Community service obligations

GTEs often provide economic and social benefits to the community over and above the direct benefits paid for by consumers. For example, urban 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 2005-06, governments paid monitored GTEs \$3.6 billion in disclosed CSO payments. In some cases, GTEs did not disclose CSO funding. Some GTEs also provide CSOs without reimbursement. For example, Forestry Tasmania did not receive CSO payments over the reporting period for the provision of public forest land management.⁸ Other GTEs provide CSOs and are refunded through general government subsidies rather than explicit CSO payments. The V/line Passenger Corporation in Victoria, for example, derived 43 per cent of its farebox revenue

⁷ Under AASB 1044, dividends must be reported in the year that they are announced rather than the year to which they relate. For example, a dividend from 2005-06 profits will not be reported in the 2005-06 operating result, if it is not declared prior to 30 June 2006.

⁸ Forestry Tasmania estimated the cost of meeting these obligations at \$5 million in 2005-06 (chapter 10).

from concession fares in 2005-06, and, although it did not receive CSO payments, it did receive government grants of \$162 million (accounting for 66 per cent of total revenue) (chapter 8).

Rail GTEs received 64 per cent of the overall CSO funding, with GTEs in the water sector receiving 16 per cent and in the electricity sector 10 per cent, in 2005-06. The urban transport sector accounted for almost all of the remaining CSO funding. The railways, water and urban transport sectors rely most heavily on CSO funding as a source of revenue with 34 per cent, 10 per cent and 8.2 per cent respectively of total revenue being accounted for by CSO funding in 2005-06.

Total CSO payments to monitored GTEs declined by 1.4 per cent (\$50 million) in real terms from 2004-05 to 2005-06. Real CSO payments increased by 38 per cent in the electricity sector, 15 per cent in the water sector and 3.3 per cent in the forestry sector. Real CSO funding ceased completely for Airservices Australia,⁹ and declined by 63 per cent in the urban transport sector, 27 per cent in the ports sector, and 2 per cent in the railways sector in 2005-06.

The decline in CSO funding in the urban transport sector was almost exclusively attributable to changes to NSW State Transit Authority funding arrangements. From 30 June 2005, CSO obligations previously funded by CSO funding are included in contract payments (chapter 7). The decline in the ports sector was exclusively due to a reduction in the payments to the Dampier Port Authority which is the only port GTE that receives CSO funding (chapter 9).

⁹ Cost recovery of CSO pricing for regional and general aviation airports is included in the pricing arrangements that came into effect on 30 June 2005 (chapter 11).

3 Asset valuation and capital management

Key points

- Incorrectly valued assets can result in misleading performance measurement, inefficient capital management, as well as reduced transparency and accountability.
- Approximately 75 per cent of GTE assets are specialised, for which current market prices are not readily available.
- Specialised assets are ideally valued using depreciated optimised replacement cost if they would be replaced, and recoverable amount otherwise,
 - in accordance with the optimal deprival value method recommended by the COAG Steering Committee on National Performance Monitoring of Government Trading Enterprises.
- Of 58 GTEs surveyed across the electricity, water, ports, rail and urban transport sectors in 2005-06:
 - 41 per cent used historical cost to value their specialised assets;
 - 40 per cent used a current cost method, either depreciated replacement cost or depreciated optimised replacement cost;
 - 14 per cent used the deprival value method; and
 - 5 per cent used the net present value method.
- With inflation, the historical cost method normally leads to under-valuation of assets over time. However, it can also lead to over-valuation if the rate of technological progress exceeds the rate of cost inflation for these assets.
- The net present value method can exhibit circularity in that the discount rate used to deflate future income flows will become the GTE's measured rate of return on assets, if the forecast income flows are realised.
- Overall, there was little change in the valuation methods used by the surveyed GTEs from 2001-02 to 2005-06. In particular, the first-time adoption of Australian-equivalent International Financial Reporting Standards (AIFRS) in 2005-06 had only a minor impact on GTEs' choice of valuation method.
 - Although the change by seven Victorian water GTEs to historical cost valuation in 2005-06 coincided with the transition to AIFRS, it was driven by a change in Victorian Treasury asset valuation guidelines.

Measures of capital structure, such as debt to equity and debt to assets ratios, are affected by asset valuation — as are measures of capital efficiency, such as return on equity and return on assets. Income and expenses related to asset valuation — such as depreciation and impairment expenses and gains or losses on revaluations — also affect measured returns.

Through its impact on performance measurement, the choice of asset valuation method has implications for efficient capital management and for public accountability. Managers require accurate measures of asset values, capital structure and return on assets in order to make optimal resource allocation and pricing decisions. Transparency and accountability to the owners or shareholders of an entity depend on meaningful published financial indicators that rely on accurate asset valuations.

Efficient capital management is particularly important for government trading enterprises (GTEs). Most GTEs operate in capital-intensive industries with a large proportion of specialised assets, which comprised 74.5 per cent of the total assets of surveyed GTEs in 2005-06 (table 3.1). These assets are designed for a specific purpose and are not rarely, except as part of a continuing operation. Consequently, market prices are not readily available to estimate the economic benefits associated with these assets.

Table 3.1 GTE specialised assets

Sector	Specialised assets	2001-02		2005-06	
		Value ^a	Share ^b	Value ^a	Share ^b
		\$b	%	\$b	%
Electricity	Power stations, transmission networks, supply system networks	31.3	77.8	40.5	74.6
Ports	Roads, wharves, channels and berths, harbours and jetties, breakwaters, bridges, dredging	1.1	33.1	1.6	25.9
Rail	Trackwork	6.5	71.7	9.0	64.0
Urban transport	Route infrastructure, wharves	0.8	65.6	0.7	53.2
Water	Water, sewerage and drainage infrastructure	39.3	87.9	39.3	84.6
All		79.0	80.2	91.1	74.5

^a Aggregate value of specialised assets controlled by the sector (\$billion). ^b Specialised assets as a proportion of total assets controlled by the sector.

Source: Productivity Commission estimates.

The methods currently used by GTEs to value their specialised assets are discussed in this chapter. Valuation methods are described in section 3.1. The accounting standards and treasury guidelines governing GTEs' choice of valuation method are outlined in section 3.2. The valuation methods used by 58 GTEs surveyed over the period 2001-02 to 2005-06 are presented in section 3.3. Finally, the implications of the methods used for efficient capital management are discussed in section 3.4.

3.1 How can specialised assets be valued?

GTEs typically use different valuation methods for different 'classes' of assets, such as cash, inventory, financial instruments, property, plant and equipment, tax assets, and so on. The valuation of specialised assets is particularly important in the case of GTEs because:

- They are usually the infrastructure or system assets that are central — and essential — to a GTE's core activities, such as power stations for an electricity generator (table 3.1).
- They make up a large proportion of most GTEs' total assets. Specialised assets comprised 74.5 per cent of the aggregate total assets of surveyed GTEs in 2005-06 (table 3.1). Electricity and water have the largest proportions of specialised assets, which represented 74.6 per cent and 84.6 per cent of sector assets (for surveyed GTEs) respectively in 2005-06. In contrast, the ports sector has a lower proportion of specialised assets (25.9 per cent of sector assets for surveyed GTEs in 2005-06), as land, buildings and investment properties are also significant.
- They are often difficult to value. By their nature, these assets are usually not traded in a developed market, so there is limited or no available evidence of the current market selling price. They also tend to have long useful lives.

Specialised assets are mainly valued using the historical cost, current cost, current value and deprival value methods. Each of these is discussed below.

Historical cost method

Under the historical cost method — also known as the depreciated actual cost method — assets are valued at their acquisition cost, less accumulated depreciation. The acquisition cost is the asset's original purchase price (including duties and taxes) plus delivery and related costs. The acquisition cost is depreciated — written down over the asset's useful life — to adjust for age and usage.

The historical cost method is based on auditable financial data and demands little judgment or expertise. Also, unlike valuation methods based on current cost or current value, the pure historical cost method does not involve periodic revaluations (SCNPMGTE 1994). These factors make it objective, transparent and relatively inexpensive to implement (King 1997, OTTER 2002).

The major weakness of this method is that asset values become less relevant over time, potentially causing over- or under-valuation. An asset's original purchase price will understate the value of its economic benefits in today's dollars because of the effect of inflation. Changes in relative factor prices can affect the asset's economic benefits over its useful life. Historical cost can overstate the economic benefits of assets that become obsolete because of technological progress. GTEs' specialised assets often have long useful lives, which exacerbates the impact of changing prices and technologies (SCNPMGTE 1994).

Many GTEs are subject to price or revenue regulation or operate with some degree of market power. This can weaken the relationship between the historical cost of a GTE's assets and the economic benefits derived from their use, further reducing the relevance of the historical cost method.

Current cost methods

Under current cost methods — such as depreciated replacement cost (DRC) and depreciated optimised replacement cost (DORC) — assets are valued at the cost of obtaining their service potential in today's markets (box 3.1).

As assets are valued in today's prices — incorporating information on current technology, input prices and demand conditions — current cost methods have the strength of relevance. A further strength of the DORC method is that asset values can be adjusted if the capacity of existing assets is greater than required, as a result of changes in demand or over-investment (OTTER 2002).

Current cost methods, however, require more subjective judgment and estimation than the historical cost method. This increases the administrative expense and reduces the objectivity of the valuations obtained.

Box 3.1 **Current cost methods**

Under current cost methods, assets are valued at the cost of acquiring them — or otherwise obtaining their service potential — in today's markets. Current cost can be measured as the current market buying price of a similar asset, where a readily observable market for the asset exists. For specialised assets, where such a market usually does not exist, current cost can be measured using reproduction or replacement cost.

Reproduction cost measures the cost of replicating an asset's service potential with a similar asset of comparable technology and scale. Replacement cost is the cost of achieving this service potential with a different asset, allowing for the possibility of technological change. A variant of replacement cost is optimised replacement cost, which is a measure of the cost of the most efficient means of obtaining an asset's service potential. This uses the optimal technology available to meet current demand plus expected growth.

The reproduction or replacement cost is depreciated to allow for age and usage. These methods are then referred to as depreciated replacement (or reproduction) cost and depreciated optimised replacement cost.

Source: Evans et al. (2000); OTTER (2002); PC (2002a).

Current value methods

Current value can be measured as the current market selling price of a similar asset, less selling costs (PC 2002a). For specialised assets, where a readily observable market usually does not exist, current value can be estimated using net present value (NPV). This measures the value of the stream of future net income flows to be derived from the asset, measured the current dollars using an appropriate discount rate. The discount rate chosen would usually be the GTE's weighted average cost of capital (WACC).

The NPV method, like the current cost methods, is relevant as assets are valued in today's prices. The estimated income flows and discount rate can incorporate current information on input prices, expected demand and other market conditions.

The disadvantages of the NPV method include its requirement for substantial judgment and estimation. It involves the identification of an appropriate discount rate, as well as estimation of future income flows to be generated by the asset and the distribution of income flows over the asset's useful life. This has the effect of reducing objectivity and increasing administrative cost.

The main weakness of the NPV method is that it exhibits circularity, where the choice of discount rate determines measured return on assets. For example, suppose

a GTE uses a discount rate of 8 per cent, which it reports as an estimate of its WACC. If its estimation of future income is accurate, the measured rate of return on assets will also be 8 per cent. This problem might be incidental, or, as suggested by Bonbright et al. (1988), intentional, when future net cash flows are discounted by a target rate of return.

Deprival value method

The deprival value method is a ‘higher level’ method that gives direction on whether to value assets at current cost or recoverable amount (defined as the greater of net present value (NPV) and disposal value) depending on whether they would be replaced (box 3.2).

Box 3.2 Deprival value method

Under the deprival value method, the value of an asset is measured as the loss that an entity would expect to incur if deprived of the asset’s service potential. Assets are valued at current cost or recoverable amount, depending on whether the service potential of the assets would be replaced.

If an asset’s service potential would be replaced, it is measured at current cost, either current market buying price (if a readily observable market exists) or current replacement cost. If the asset would not be replaced, it is valued at the recoverable amount, defined as the greater of net present value (NPV) and disposal value.

A variant of this method is the optimal deprival method, in which the value of an asset that would be replaced is measured using depreciated optimised replacement cost (DORC) rather than depreciated replacement cost (DRC).

In most cases, the (optimal) deprival value method results in a DRC or DORC valuation. It is sometimes abbreviated to ‘lower of DORC and the recoverable amount’, based on the assumption that DORC will always be lower than the recoverable amount for assets that would be replaced. In practice, some GTE specialised assets would be replaced even though they do not generate net future income flows greater than their replacement cost, because of the externalities claimed from the provision of infrastructure services. However, if NPV is broadly defined to include all economic benefits derived from an asset (internal and external), it is likely that the recoverable amount would always exceed DORC for assets that would be replaced.

Source: King (1997), OTTER (2002); SCNPMGTE (1994).

The deprival value method has the strength that it is based on an economic view of an asset’s value. It shares the advantage of relevance with the current cost and current value methods, but it also allows for the situation where the recoverable amount is lower than the depreciated (optimised) replacement cost. However, the deprival value method requires substantial estimation, judgment and some

discretion in determining whether an asset would be replaced if the entity were deprived of it. Consequently, this method can involve additional subjectivity and is relatively costly to undertake.

Preferred valuation method

In 1994, the Australian, State and Territory Governments endorsed the principle that ideally GTEs' long-lived specialised assets should be valued using the optimal deprival value method. This endorsement was formalised in the *Guidelines on Accounting Policy for Valuation of Assets of Government Trading Enterprises Using Current Valuation Methods*, which were developed to promote consistent, relevant and reliable performance measurement for GTEs (SCNPMGTE 1994).

The Steering Committee on National Performance Monitoring of Government Trading Enterprises (the Steering Committee) recommended the optimal deprival method, because it provides the best indication of an asset's economic value to its owner-government. Importantly, the method recognises that market prices are generally unavailable or unreliable indicators of the economic benefits associated with the unique and specialised assets controlled by GTEs.

State and territory governments were encouraged to update their asset valuation guidelines to reflect the Steering Committee's recommendations. As of 2005-06, State and territory guidelines partially reflected the Steering Committee guidelines. These guidelines are discussed in section 3.2.

3.2 Accounting standards and Treasury guidelines

Australian accounting standards affect a GTE's choice of asset valuation method by specifying how different classes of assets are to be valued. All surveyed GTEs adopted Australian-equivalent International Financial Reporting Standards (AIFRS) for the first time in 2005-06. This led to minor changes in the requirements for valuing specialised assets.

State and territory treasury guidelines give further direction on how GTEs are to value their specialised assets. In some cases, these policies limit the asset valuation method options available under Australian accounting standards. Treasury guidelines appear to have been informed by the recommendations of the Steering Committee in 1994, although the extent to which they reflect those recommendations varies from one jurisdiction to another.

Box 3.3 **Key accounting standards for GTE asset valuation**

AASB 116 *Property, Plant and Equipment*

Under this standard, GTEs can value each class of property, plant and equipment using either the 'cost model' (historical cost method) or the 'revaluation model' (also termed 'fair value').^a GTEs must apply the chosen method to an entire class of property, plant and equipment.

Where the revaluation model is used, specialised assets for which current market prices are not readily observable can be valued using either an income or a depreciated replacement cost approach. The income approach implies the use of the net present value (NPV) method, while the replacement cost approach implies the use of depreciated replacement cost or depreciated optimised replacement cost. The choice of approaches also implies that the deprival value method can be used. The standard does not offer further direction about which of these two approaches to use under particular circumstances, or how to apply them.

AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*

Under this standard, GTEs that had been using current cost or current value methods in reporting periods prior to 2005-06 can take these prior valuations as 'cost' for the purpose of using the cost model under Australian-equivalent International Financial Reporting Standards (AIFRS). This is known as 'deemed cost', defined as an amount used as a surrogate for true historical cost at a given date. GTEs can choose to use either the fair value (that is, current cost or current value) at the time of adoption of AIFRS, or a previous revaluation that is 'broadly comparable to fair value', as deemed cost.

AASB 136 *Impairment of Assets*

Under this standard, GTEs are required to apply a 'recoverable amount test'. Recoverable amount is the higher of NPV and net realisable value, where the latter is market or disposal value, net of selling costs. If an asset's recoverable amount is lower than its net book value (using either the cost model or revaluation model under AASB 116), the net book value must be reduced to the recoverable amount.

^a In this chapter (and in chapter 4), fair value refers to the use of the current cost, current value or deprival value methods of valuing assets. In general (as in AASB116), fair value is defined as the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. However, for specialised assets, such a market-based valuation is usually unavailable. Consequently, fair value has to be estimated using the current cost, current value or deprival value methods.

Accounting standards

The standards of the Australian Accounting Standards Board (AASB) particularly relevant to valuation of specialised assets for the 2005-06 reporting year were (box 3.3):

-
- AASB 116 *Property, Plant and Equipment*;
 - AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*; and
 - AASB 136 *Impairment of Assets*.

None of these standards explicitly mention the optimal deprival value method recommended by the Steering Committee. However, it is arguable that the (optimal) deprival method is consistent with the concurrent application of AASB 116 and AASB 136. If GTEs value their specialised assets using depreciated (optimised) replacement cost under AASB 116, and apply the recoverable amount test (RAT) under AASB 136, they will be effectively valuing these assets at the lower of replacement cost and recoverable amount, consistent with the main thrust of the optimal deprival value method.

That said, GTEs are not compelled under AASB 116 to use depreciated replacement cost for specialised assets, nor does this standard require, if replacement cost is used, that it be optimised replacement cost. Further, under AASB 136, the RAT is applied only where there is evidence of ‘impairment’, such as changes in technology or physical damage to an asset, rather than being applied unconditionally to every asset.

Treasury guidelines

State and Territory asset valuation guidelines give further direction on valuing GTE assets beyond what is contained in accounting standards. All state and territory governments updated their asset valuation guidelines in response to the first-time adoption of AIFRS. As a result, these guidelines give direction on how GTEs in each jurisdiction are required to interpret and apply the provisions of AASB 116 and other AIFRS accounting standards.

New South Wales, SA, Tasmania and the NT guidelines mandate the use of the revaluation model rather than the cost model, under AASB 116, for valuing specialised assets (box 3.4). Of these, NSW, SA and the NT specify the use of the DORC method when the AASB 116 revaluation model is applied to specialised assets.

Queensland, WA and the ACT guidelines allow GTEs to choose either the revaluation model or the cost model under AASB 116. The WA guidelines state, however, that if the AASB 116 revaluation model is chosen for specialised assets, the DORC method must be used rather than the income approach (NPV) permitted under the accounting standard.

Box 3.4 Treasury guidelines for valuing specialised assets

New South Wales

Accounting Policy: Valuation of Physical Non-Current Assets at Fair Value, updated April 2007

- Specialised assets must be valued using the AASB 116 revaluation model. Use of the AASB 116 cost model is not permitted.
- Specialised assets for which market prices are unavailable must be valued using depreciated optimised replacement cost (DORC). The 'income approach' (using net present value, or NPV) of estimating fair value within the AASB 116 revaluation model is not permitted for specialised fixed assets.

Victoria

Financial Reporting Directive 103: Non-Current Physical Assets, April 2005

- Water and rail infrastructure assets must be valued at depreciated historical cost (the AASB 116 cost model).
- Plant and equipment (including rail GTEs' rolling stock), vehicles and assets under construction are also to be valued using the AASB 116 cost model.
- All other assets must be valued at fair value using the AASB 116 revaluation model.
- Specialised assets — excluding water and rail infrastructure assets — can be valued using either the income approach or depreciated replacement cost approach within the AASB 116 revaluation model.

Financial Reporting Directive 115: Non-Current Physical Assets — First Time Adoption, February 2005

- GTEs are encouraged to apply the exemption under AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* to take previous fair value valuations as cost (deemed cost) '... to avoid the burden of calculating true historical cost under AASB 116' (p. 3).

Queensland

Non-Current Asset Policies for the Queensland Public Sector, June 2005 (updated June 2006)

- The AASB 116 revaluation model is generally preferred to the AASB 116 cost model for valuing fixed assets.
- Assets should be valued using depreciated replacement cost, if they would be replaced. If an asset would not be replaced, it should be valued at NPV or disposal value.

(Continued next page.)

Box 3.4 (continued)

Western Australia

Treasurer's Instruction 954: Revaluation of Non-Current Physical Assets, updated April 2007

- Specialised assets can be valued using either the AASB 116 cost model or revaluation model, according to 'the agency's discretion'.
- If the AASB 116 revaluation model is chosen for specialised assets, the DORC method must be used. The income approach (NPV) within the AASB 116 revaluation model is not permitted.

South Australia

Accounting Policy Framework III: Asset Accounting Framework, updated June 2006

- Specialised assets must be valued using the AASB 116 revaluation model. Use of the AASB 116 cost model is not permitted for specialised assets.
- Specialised assets should be valued using the DORC method, if they would be replaced. If an asset would not be replaced, it should be valued at the greater of NPV and net realisable value.

Tasmania

Treasurer's Instruction 303: Recognition and Measurement of Non-Current Assets, April 2005

- Specialised assets must be valued using the AASB 116 revaluation model. Use of the AASB 116 cost model is not permitted for specialised assets.

Australian Capital Territory

Accounting Policy: Property, Plant and Equipment, updated January 2006

- Asset classes that are '... not used to make management decisions ...' can be valued using either the AASB 116 cost model or revaluation model (p. 3).
- Asset classes for which '... a current valuation is needed for management decisions or asset utilisation purposes ...' must be valued using the AASB 116 revaluation model (p. 3).

Northern Territory

Treasurer's Directions Section A2.4: Revaluation, updated August 2006

- Specialised assets must be valued using the AASB 116 revaluation model. Use of the AASB 116 cost model is not permitted for specialised assets.
- Specialised assets for which market prices are unavailable must be valued using DORC. The income approach (NPV) within the AASB 116 revaluation model is not permitted for specialised assets.

Source: ACT Treasury (2006); NSW Treasury (2007); NT Treasury (2006); Queensland Treasury (2006); SA Treasury (2006); Tasmanian Treasury (2005); Victorian Treasury (2005a, 2005b); WA Treasury (2007).

Victorian guidelines differ from those of other jurisdictions in that they mandate the use of the cost model for valuing some specialised assets, namely water and rail infrastructure assets. In its Financial Reporting Directive 103 *Non-Current Physical Assets*, the Department of Treasury and Finance took the view that historical cost is the ‘... most appropriate method of reporting across government for plant, equipment, vehicles, assets under construction/development and *water infrastructure assets* and *rail infrastructure assets*’ (Victorian Treasury 2005, p. 5, emphasis added).

The influence of the Steering Committee guidelines is apparent in most of the treasury guidelines. Four of the eight jurisdictions require (and a fifth recommends) the use of DORC for valuing specialised assets — which constitutes the key component of the deprival value method. Queensland and SA guidelines use deprival value terminology, recommending the DORC method for assets that would be replaced, and recoverable amount for assets that would not be replaced.

The decisions of some jurisdictions to use, or permit the use of, historical cost to value specialised assets, however, suggests that the guidelines allow a significant departure from the recommendations of the Steering Committee.

3.3 How are specialised assets valued?

The published financial statements of 58 GTEs monitored in the *Financial Performance of Government Trading Enterprises* report were surveyed for data on the type and value of specialised assets controlled and the methods used to value them over the period 2001-02 to 2005-06.

The survey included GTEs that had been monitored for the last five years, that had specialised assets for the whole period, and for which data on the valuation method used for specialised assets were publicly available. Forestry GTEs were excluded because their non-current assets largely comprise self-generating and regenerating assets, rather than specialised assets comparable with those of GTEs in the other sectors.

Care should be taken when comparing patterns in valuation methods across jurisdictions and sectors. The sample includes GTEs from the electricity, water, ports, rail and urban transport sectors. However, some jurisdictions are over-represented in some sectors and under-represented in others.

This lack of representativeness is attributable to both the sampling procedure (exclusion of GTEs not monitored for the entire five-year period) and to variation in sectoral structure among jurisdictions. For example, there are 11 surveyed water

GTEs in Victoria, including several relatively small rural water GTEs. In contrast, there is one large water GTE in each of Queensland and WA. This variation is the result of a number of factors, including privatisations, mergers and disaggregations.

It is also important to note that the survey results discussed below are based on the valuation methods reported in published financial reports. Hence, the accuracy of the results is influenced by the accuracy, completeness and consistency of the information provided in those reports.

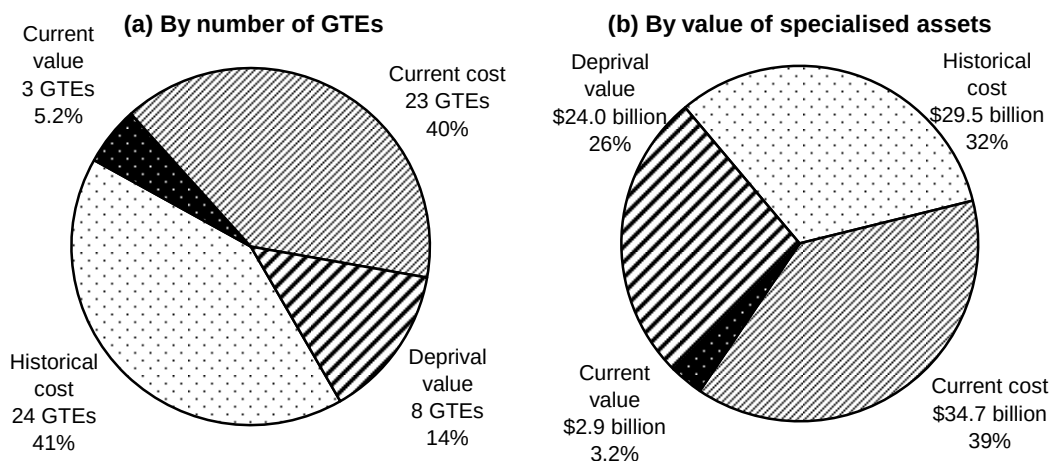
Finally, individual asset values were not examined to assess the accuracy or robustness of the valuation methods used.

Survey results

There was substantial variation in the methods GTEs used to value their specialised assets in 2005-06. Many GTEs (40 per cent of the sample) used a current cost method, while a comparable proportion (41 per cent) used the historical cost method (figure 3.1).

The group of GTEs using historical cost included several rural water and ports GTEs with relatively low asset values. Given their relative size, GTEs using historical cost represented only 32 per cent of the sample by value of specialised assets controlled, while those using current cost represented 39 per cent.

Figure 3.1 Valuation methods used in 2005-06^a



^a Data are from annual reports for a sample of 58 electricity, water, ports, rail and urban transport GTEs for 2005-06. ^b Aggregate value of specialised assets controlled by GTEs using each valuation method.

Source: Productivity Commission estimates.

Table 3.2 Valuation methods for surveyed GTEs, by year and by sector^a

	2001-02		2002-03		2003-04		2004-05		2005-06	
	no.	%	no.	%	no.	%	no.	%	no.	%
<i>Historical cost</i>										
Electricity	7	12.1	4	6.9	4	6.9	4	6.9	5	8.6
Ports	5	8.6	5	8.6	5	8.6	5	8.6	5	8.6
Rail & Urban transport	1	1.7	1	1.7	1	1.7	1	1.7	1	1.7
Water	6	10.3	6	10.3	6	10.3	6	10.3	13	22.4
All sectors	19	32.8	16	27.6	16	27.6	16	27.6	24	41.4
<i>Current cost</i>										
Electricity	7	12.1	8	13.8	8	13.8	7	12.1	8	13.8
Ports	7	12.1	7	12.1	7	12.1	8	13.8	9	15.5
Rail & Urban transport	1	1.7	3	5.2	3	5.2	3	5.2	3	5.2
Water	4	6.9	4	6.9	4	6.9	5	8.6	3	5.2
All sectors	19	32.8	22	37.9	22	37.9	23	39.7	23	39.7
<i>Current value</i>										
Electricity	1	1.7	1	1.7	1	1.7	1	1.7	1	1.7
Ports	1	1.7	1	1.7	1	1.7	1	1.7	1	1.7
Rail & Urban transport	2	3.4	1	1.7	1	1.7	1	1.7	1	1.7
Water	1	1.7	1	1.7	1	1.7	1	1.7	–	–
All sectors	5	8.6	4	6.9	4	6.9	4	6.9	3	5.2
<i>Deprival value</i>										
Electricity	2	3.4	4	6.9	4	6.9	4	6.9	3	5.2
Ports	2	3.4	2	3.4	2	3.4	1	1.7	–	–
Rail & Urban transport	2	3.4	1	1.7	1	1.7	1	1.7	1	1.7
Water	5	8.6	4	6.9	4	6.9	4	6.9	4	6.9
All sectors	11	19.0	11	19.0	11	19.0	10	17.2	8	13.8
<i>Combined</i>										
Electricity	–	–	–	–	–	–	1	1.7	–	–
Ports	–	–	–	–	–	–	–	–	–	–
Rail & Urban transport	–	–	–	–	–	–	–	–	–	–
Water	4	6.9	5	8.6	5	8.6	4	6.9	–	–
All sectors	4	6.9	5	8.6	5	8.6	5	8.6	–	–
<i>All methods</i>										
Electricity	17	29.3	17	29.3	17	29.3	17	29.3	17	29.3
Ports	15	25.9	15	25.9	15	25.9	15	25.9	15	25.9
Rail & Urban transport	6	10.3	6	10.3	6	10.3	6	10.3	6	10.3
Water	20	34.5	20	34.5	20	34.5	20	34.5	20	34.5
All sectors	58	100.0	58	100.0	58	100.0	58	100.0	58	100.0

^a Data are from the annual reports of a sample of 58 electricity, water, ports, rail and urban transport GTEs over the period 2001-02 to 2005-06. – Zero or rounded to zero.

Source: Productivity Commission estimates.

Use of the deprival value method was more limited, with 14 per cent of sampled GTEs indicating that this method was used to value their specialised assets in 2005-06. However, these GTEs were relatively large electricity, water and rail GTEs, with their specialised assets representing 26 per cent of the total specialised assets in the sample.

Overall, nearly 59 per cent of the sample used some form of current cost or current value in the last reporting year (including the deprival value method, which can lead to either a current cost or current value method being used). This is consistent with earlier findings that a majority of GTEs use current cost or current value methods (PC 2001; 2002a).

There was little change in the valuation methods used by the surveyed GTEs from 2001-02 to 2004-05. Greater change occurred between 2004-05 and 2005-06 (table 3.2). Seven rural water GTEs in Victoria moved from either a combined method or a current cost method to historical cost in 2005-06. Although this coincided with the first-time adoption of AIFRS, the change was attributable to the new Victorian Treasury guidelines requiring water infrastructure assets to be valued at historical cost (as discussed in section 3.2).

Apart from the Victorian water GTEs, there were few changes in valuation methods used from 2004-05 to 2005-06. This implies that the transition to AIFRS, by itself, had little impact on GTEs' choice of valuation method for specialised assets.

There was, however, wide variation in valuation methods between sectors over the survey period (table 3.2).

3.4 How do valuation methods affect capital management?

Efficient capital management requires accurate, reliable and relevant asset values. For GTEs, with their large proportion of unique, specialised assets, overcoming the difficulty of valuation where market prices are unavailable is an essential prerequisite for obtaining accurate asset values. The Steering Committee identified the optimal deprival value method as the preferred way to measure the service potential of specialised assets (SCNPMGTE 1994).

Nevertheless, more than a decade after the Steering Committee guidelines were released, there is substantial variation in the extent to which GTEs are using the deprival value method or a similar approach.

Current cost methods and the deprival value method

Of the surveyed GTEs, 13.8 per cent used the deprival value method to value their specialised assets in 2005-06, compared with 39.7 per cent using a current cost method (table 3.2). However, the combined effect of accounting standards AASB 116 and AASB 136 is that more GTEs might be using a deprival-type method than those that explicitly report doing so. As mentioned in section 3.2, GTEs that choose to use the DORC method under AASB 116 and then test for impairment using the recoverable amount test (RAT) under AASB 136 (recoverable amount being the maximum of NPV and disposal value) are effectively applying the deprival value method.

It should be noted, however, that the combination of DORC and compliance with AASB 136 does not guarantee that the optimal deprival value method is applied as recommended by the Steering Committee (SCNPMGTE 1994). One reason for this is the discretion involved in applying the RAT under AASB 136. The RAT is only applied when there is evidence of impairment (such as physical damage to an asset). Consequently, GTEs using DORC might not deem it necessary to value the recoverable amount of all their assets.

For assets that would not be replaced, the recoverable amount can be much lower than the DORC valuation. For example, the Rail Infrastructure Corporation (RIC) changed from NPV to DORC valuation in 2002-03. Most of the RIC's rail network was valued at zero under NPV as no positive net cashflows were directly attributable to these assets. This change in valuation method contributed to a tenfold increase in the value of RIC's specialised assets.

Similarly, the Darwin Port Corporation (DPC) used the deprival value method from 2001-02 to 2004-05, resulting in an NPV valuation for its harbour works-in-progress. These works-in-progress, transferred from the NT Government to the DPC each year, were written down to zero as they were not expected to generate any future cashflows. After the DPC changed to the depreciated replacement cost method in 2005-06, the value of its specialised assets increased sixfold.

If a DORC or DRC valuation method is used to value specialised assets that would not be replaced, total assets will be over-valued relative to the optimal deprival value and the return on assets will tend to be understated. As a consequence, decisions on the management of these specialised assets would not be based on accurate and relevant asset values.

Another source of discrepancy between current cost valuation and the optimal deprival method is that many GTEs using current cost are not using optimised replacement cost.

The information reported in GTE annual reports suggests that 13 of the 23 GTEs using current cost methods in 2005-06 used replacement cost (mainly port GTEs) and the other 10 used optimised replacement cost (mainly electricity GTEs). Those using optimised replacement cost either explicitly included the term 'optimised' or used terminology such as the valuation was '... based on the optimum set of replacement assets necessary to achieve the same service potential with no inappropriate surplus capacity' (Energex 2006, p. 108).

It could be that those GTEs indicating that they used DRC do, in fact, use DORC. For example, Delta Electricity and Transgrid report the use of replacement cost, but are required under the NSW Treasury guidelines to use optimised replacement cost.

If GTEs are not using optimised replacement cost, they could be failing to adjust for excess capacity or over-design inherent in existing assets. As a result, the effects of past capital investment decisions that caused these inefficiencies are less likely to be remedied in future if they are 'built into' the current valuation of the GTE's assets.

Historical cost method

Of the surveyed GTEs, 41.4 per cent used the historical cost method to value their specialised assets in 2005-06 (table 3.2). The number of GTEs using this method increased from 16 to 24 (27.6 to 41.4 per cent) from 2004-05 to 2005-06. This mainly reflects the move by seven Victorian rural water GTEs to historical cost in 2005-06, in line with a change to Victorian Department of Treasury and Finance asset valuation guidelines (box 3.4).

The use of the historical cost method by GTEs constitutes a significant departure from the recommendations of the Steering Committee. As discussed in section 3.1, this method can result in inaccurate and irrelevant asset values and misleading measured rates of return on assets, impeding efficient capital management.

Evidence of the discrepancy between historical cost and current cost valuations is available in the annual reports of some GTEs using current cost, which show asset values under historical cost. For example, TransGrid estimated that the value of its network assets under historical cost in its 2005-06 annual report was more than 30 per cent lower than the value under DRC.

Where assets are substantially under-valued, the measured rate of return on assets will be commensurately affected. Specifically, under-valuation of assets results in

overstated returns, making GTEs appear more profitable than they would if assets were valued at deprival value.

Many of the GTEs that used the historical cost method in 2005-06 have taken a previous valuation at current cost or current value as being the ‘historical cost’ from a given point in time. This is known as ‘deemed cost’ and is permissible under AASB 1 (box 3.3). The usual reason for using deemed cost is that an accurate and complete record of the historical cost is not always available, particularly in relation to long-lived assets.

Deemed cost was used in place of ‘true’ historical cost in 2005-06 by all seven rural water GTEs in Victoria, Stanwell Corporation and SunWater in Queensland, and the Hydro-Electric Corporation in Tasmania. For example, Stanwell’s generation assets were valued at DORC at the time of its incorporation in 1997 and the DORC valuation was thereafter taken as historical cost.

The use of deemed cost could mitigate, to some extent, the lack of relevance inherent in the historical cost method. If a valuation reported as historical cost is in fact a prior DORC or DRC valuation that has been depreciated in each reporting period, the extent of possible under-valuation (because of inflation) is not as great as if the true historical cost had continued to be used.

Nevertheless, asset values under the historical cost method will still become less relevant over time. This will increase the potential for inefficient asset management and decision-making because it is not informed by currently available information.

Performance measurement

The survey results reveal that many GTEs are using valuation methods that might not reflect the economic value of their specialised assets. This can make performance measurement indicators inaccurate and misleading, thereby reducing GTE accountability and increasing the potential for inefficient capital management decisions.

A key financial performance measure is the rate of return on assets. This is an indicator of how efficiently GTEs are using the capital vested in them. An analysis of two approaches to measuring the rate of return on assets, and of the importance of accurately measuring return on assets for efficient capital management, is contained in chapter 4.

4 Rate of return measures and capital management

Key points

- Reliable rate of return measures are required for efficient capital management and pricing.
- Public reporting of rates of return increases accountability by allowing shareholder ministers and the public to better assess the performance of GTEs over time.
- The accounting rate of return on assets (ARR) is widely reported and understood, but has some limitations. Specifically, it does not have adequate regard for the capital as well as cash streams of income.
- Conceptually, the economic rate of return (ERR) does not have this limitation and is directly comparable with the opportunity cost of capital.
 - In practice, data limitations and asset valuation methods can significantly affect ERR estimates.
- Empirical analysis of the rates of return of 56 GTEs over the period 2000-01 to 2003-04 revealed that:
 - generally estimates of the ERR were higher than estimates of the ARR (for 82 per cent of observations); and
 - some asset valuation methods were a major source of difference between the ARR and ERR estimates.
- A large proportion of GTEs did not achieve a return on assets greater than the risk-free rate using either the ARR (52 per cent) or the ERR (42 per cent). This indicates that many did not earn an adequate return on their capital, even with regard for capital gains as well as profits.

Government trading enterprises (GTEs) are involved in the production and provision of goods and services in key sectors of the economy. They are typically capital intensive and require substantial investment. Investment by GTEs can be financed through retained earnings, debt or capital contributions from government. In total, public corporations accounted for around 7 per cent of Australia's gross fixed capital formation in 2005-06 (ABS 2007b).

Public capital is subject to competing demands across both social and physical infrastructure. If GTEs are to operate efficiently and on a commercial basis, they must achieve an adequate rate of return on their assets over time.

The accounting rate of return on assets (ARR) is a widely used and understood measure of performance. This measure provides information about how well capital is being managed, but it suffers from a number of limitations. A conceptually superior measure is the economic rate of return (ERR). However, there are difficulties employing this measure in practice. In addition, both measures are affected by the method used to value assets. The trends and implications of asset valuation methods used by GTEs are discussed in chapter 3.

The importance of accurately measuring capital efficiency is discussed in section 4.1. The ARR and ERR measures are compared both conceptually and empirically in section 4.2. Trends in the rates of return of GTEs and factors influencing the results are described in section 4.3. The implications of the results for the performance and capital management of GTEs are discussed in section 4.4.

4.1 How can capital efficiency be measured?

Reliable measures of the rate of return on assets provide valuable information about the performance of GTEs. This can indicate whether the cost of capital is covered and shareholder value is maintained. It is particularly relevant for GTEs because other measures are unavailable (such as a share price) or difficult to estimate (such as productivity).

Managers can use measured rates of return to assess the performance of past investments, and inform future decisions on resource management and pricing. Further, published rates of return increase the transparency and public accountability of GTEs.

The ARR is a commonly used measure because it is derived from data readily available in published annual reports. It is the ratio of accounting income to the value of assets.

Despite its common use, there are limitations to the ARR as a measure of profitability. The major weakness is that the simple concept of income used — net cash flows — does not capture the other component of economic income — capital gains. Traditionally, it has also included assets valued at their historical cost (the

acquisition cost, less accumulated depreciation) rather than at fair value.¹ A discussion of common asset valuation methods and the implications of these methods for capital management is contained in chapter 3.

Ideally, the rate of return on assets for a period should be measured as the ratio of economic income earned (net cash flows plus the change in the fair value of assets) to the fair value of assets employed over the period. This is called the ERR.

Although the ERR is conceptually superior, it can be difficult to calculate in practice because of the complexity of estimating the fair value of assets and other limitations associated with publicly available data. Nevertheless, the potential benefits of the ERR warrant an examination.

4.2 Accounting and economic rate of return measures

There are a variety of equations used to calculate the rate of return on assets in financial literature. In this chapter, the definitions of the ARR and ERR are those presented in *An Economic Framework for Assessing the Financial Performance of Government Trading Enterprises* (SCNPMGTE 1996).

Functional forms

The ARR is defined as the ratio of net cash flows to the average value of assets:

$$ARR = \frac{EBIT}{\frac{1}{2}(A_b + A_e)} \quad [4.1]$$

Where:

- ARR = the nominal pre-tax accounting rate of return on total assets;
- $EBIT$ = operating profit before income tax plus gross interest expense;
- A_b = the value of assets at the beginning of the period;
- A_e = the value of assets at the end of the period.

The ERR is defined as the ratio of net cash flows (earnings before interest and tax (EBIT) with some adjustments) plus the change in the fair value of assets, to the fair value of assets at the beginning of the period:

¹ Fair value is defined as the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. However, for specialised assets, such a market-based valuation is usually unavailable. Consequently, fair value has to be estimated using the current cost, current value or deprival value methods for these assets as discussed in chapter 3.

$$ERR = \frac{(EBIT + Da + NIBL + FL + CSO) + (A_e - A_b - NI)}{A_b + (NI / 2)} \quad [4.2]$$

Where:

- ERR* = the nominal pre-tax economic rate of return on total assets;
- EBIT* = operating profit before income tax plus gross interest expense;
- Da* = accounting depreciation and amortisation;
- NIBL* = adjustment for the implicit interest cost of non-interest bearing liabilities;
- FL* = adjustment for the interest cost of assets under financial leases (if not already included in EBIT);
- CSO* = adjustment for the net economic cost of community service obligations (if CSO costs are not fully compensated);
- A_b* = the value of assets at the beginning of the period;
- A_e* = the value of assets at the end of the period;
- NI* = value of net investments throughout the year;
 $= A_e - A_b - (AsRR_e - AsRR_b) + Da$;
- AsRR_b* = the asset revaluation reserve at the beginning of the period;
- AsRR_e* = the asset revaluation reserve at the end of the period.

Conceptual differences

The main difference between the ARR and ERR is the treatment of income. Accounting income includes only net cash flows whereas economic income also includes capital gains (box 4.1). This captures all sources of returns to shareholders and is consistent with analysis commonly used to assess investments in the private sector.

The equation for economic income in the ERR (the numerator in equation 4.2) can be simplified to equal EBIT with some adjustments plus the change in the asset revaluation reserve (AsRR):

$$Economic\ income = EBIT + NIBL + FL + CSO + (AsRR_e - AsRR_b) \quad [4.3]$$

This representation is simpler and more comparable with the expression of income in the ARR. However, the ERR is a more effective measure when the cash and capital components of income can be separately analysed (SCNPMGTE 1996).

There are also differences in the definition of the asset base. In the ARR, an average value of assets across the period is used, whereas the initial assets plus the average value of net investment over the period is used for the ERR.

Although the ERR calls for the inclusion of assets at their fair value, in practice GTEs generally report assets valued by a variety of methods. A survey of GTEs from 2001-02 to 2005-06 revealed that about one third of GTEs estimated the value

of their specialised assets using historical cost and about two thirds used a fair value method (chapter 3).²

Box 4.1 Economic treatment of income

For the ARR, earnings before interest and tax (EBIT) is used to represent net cash flows. The ERR is a more robust measure because it adjusts EBIT to account for the cost of capital by excluding:

- The effect of accounting depreciation. Accounting depreciation is calculated according to accounting principles and can vary significantly from the economic depreciation of an asset. Instead, the effect of economic depreciation is accounted for in the capital component of income, through net investments.
- The implicit interest charge incorporated in the cost of non-interest bearing liabilities, because this represents a return on (debt) capital.
- Financial lease interest expenses (if not included in the gross interest expense contained in EBIT), because the rate of return should be independent of the capital structure.
- Community service obligation (CSO) expenses (if expenses are not fully reimbursed by government and included in EBIT), to estimate the rate of return if the government were to fully fund all CSOs.

In addition, the measure of income in the ARR results in inconsistent treatment of unrealised changes in capital. An unrealised capital loss resulting from a negative asset revaluation is included as an expense in EBIT and has a negative impact on the ARR. However, an unrealised capital gain is not recorded as revenue and is only included in the asset revaluation reserve, which has no effect on the ARR. This asymmetry is avoided by the ERR by including the change in the asset revaluation reserve in the capital component of income.

Source: SCNPMGTE (1996).

If the same asset value is used to calculate both measures, the ERR asset base will be equal to that in the ARR, adjusted down by the change in the asset revaluation reserve and up by accounting depreciation:

$$ERR \text{ asset base} = ARR \text{ asset base} - 0.5(AsRR_e - AsRR_b) + 0.5Da \quad [4.3]$$

² The method used to value other assets, such as land and buildings might vary.

For GTEs that do not utilise their asset revaluation reserves, this simplifies further to include only an adjustment for accounting depreciation:

$$ERR \text{ asset base} = ARR \text{ asset base} + 0.5Da \quad [4.4]$$

Empirical issues

The data used in this analysis were obtained from financial statements in GTE annual reports for the period 1999-2000 to 2004-05.

Annual estimates of the rate of return can be highly variable because of the effect of infrequent or large asset revaluations and changes outside the control of a GTE. Simple mid-point three-year moving average estimates were calculated to disperse these effects over time.³ This produced rate of return estimates for the period 2000-01 to 2003-04. All calculations were pre-tax and in 2004-05 dollars, adjusted using the gross fixed capital formation (public corporations) implicit price deflator (ABS 2007a).

The ARR and ERR measures were estimated for 56 GTEs from the electricity, ports, rail and urban transport sectors monitored in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report (PC 2006). GTEs were included in the analysis if there were publicly available data and they had not experienced a significant change in structural form since 1999-2000.

Data from 2005-06 were excluded because the first-time adoption of the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006 affected some financial data used to calculate rates of return. It changed the recognition and measurement of some assets, liabilities, equity items and income flows. For example, the pre-tax operating profit (EBIT less interest expenses) recorded by the electricity industry in 2004-05 was 37 per cent lower when measured under AIFRS (chapter 5).

All data collected from annual reports were assumed to be complete and accurate. The only variable not explicitly included in most annual reports was non-interest bearing liabilities (NIBLs). NIBLs, as reported, generally include items called non-interest bearing liabilities as well as payables, creditors, trade creditors, accruals and 'other' liabilities. Provisions, interest bearing liabilities, deferred tax liabilities and employee entitlements were specifically excluded from NIBLs. The weighted-average variable interest rate on credit outstanding for large businesses

³ Ideally, estimates should be averaged over a period consistent with the period of a GTE's corporate planning cycle, when assets are fully revalued. However, a constant three-year average was used in this analysis to provide consistency across GTEs.

was used to calculate the indirect interest charge embodied in these liabilities (RBA 2007b).

The costs of all community service obligation (CSO) expenses were assumed to be covered by CSO payments included as revenue, unless explicitly stated otherwise.

Only one GTE reported an unfunded CSO expense and two GTEs reported financial lease interest expenses that were not included in EBIT. Consequently, for the large majority of GTEs the ERR estimates effectively become:

$$ERR = \frac{(EBIT + Da + NIBL) + (A_e - A_b - NI)}{A_b + (NI / 2)} \quad [4.5]$$

4.3 Comparing accounting and economic rate of return measures

The ARR and ERR estimates exhibited a strong positive relationship (figure 4.1). Overall, the ERR estimates were higher than the ARR estimates (for 82 per cent of observations), but there was considerable variation between the rates of return using the two measures.

Effect of asset valuation methods on rate of return estimates

The method used to value assets has a major influence on the ARR and ERR relativities (table 4.1). The extent of the differences was examined by grouping the rate of return estimates by valuation method.⁴

Table 4.1 **Mean rate of return estimates by asset valuation method, 2000-01 to 2003-04 (per cent)^a**

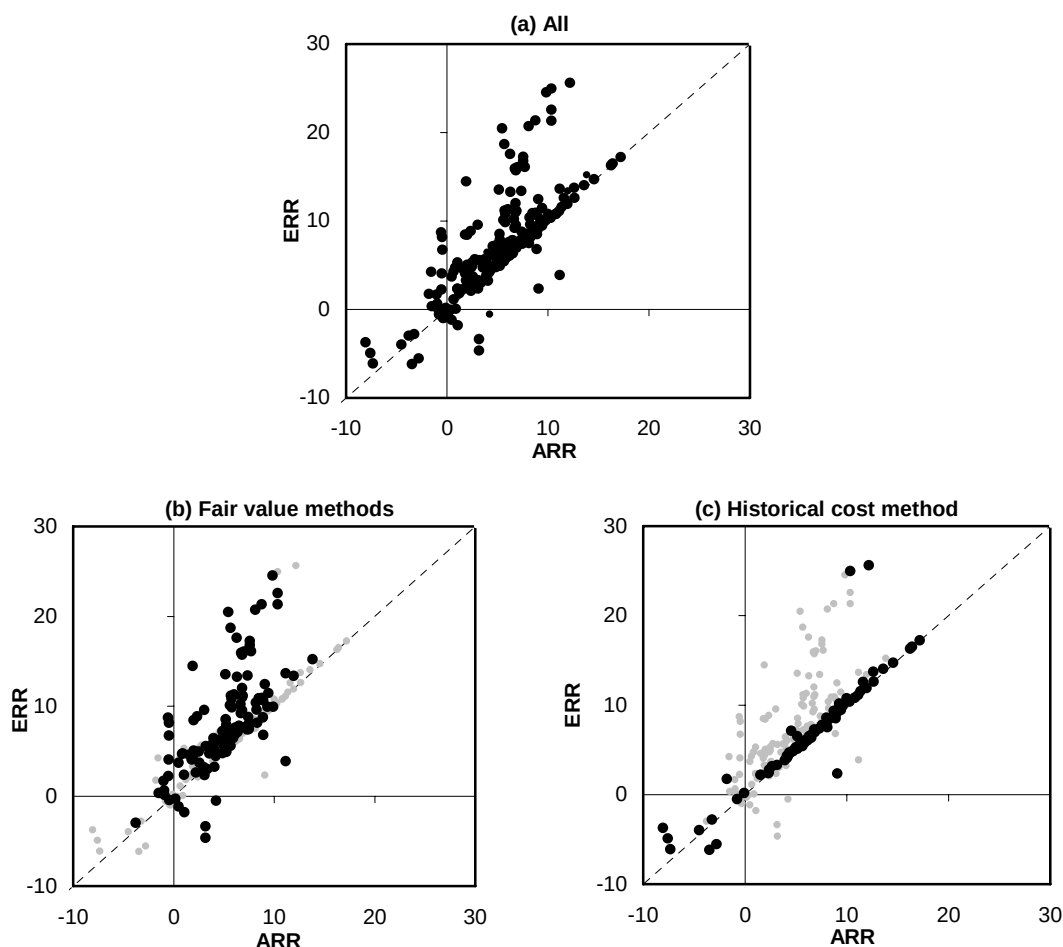
	<i>Historical cost method</i>	<i>Fair value methods</i>	<i>Other^b</i>	<i>All</i>
ARR	6.0	5.1	3.2	5.1
ERR	6.2	7.7	6.6	7.1

^a Rate of return data are mid-point estimates based on three-year simple moving averages of the primary data. For example, estimates for 2003-04 are based on data for 2002-03, 2003-04 and 2004-05. ^b Includes GTEs that used a combination of asset valuation methods in one year or changed methods over the period.

Source: Productivity Commission estimates.

⁴ GTEs were grouped by the method used to value specialised assets. The method used to value other assets, such as land and buildings might vary.

Figure 4.1 Rates of return by asset valuation method, 2000-01 to 2003-04, (per cent)^a



^a Rate of return data are mid-point estimates based on three-year simple moving averages of the primary data. For example, estimates for 2003-04 are based on data for 2002-03, 2003-04 and 2004-05. An observation on the 45° line is the same for each measure. An observation above the 45° line is higher when estimated by ERR. The observations in (b) and (c) are a decomposition of the observations in (a). (a) includes all observations over the four years. (b) highlights only observations for GTEs using a fair value method to value specialised assets. (c) highlights only observations for GTEs using the historical cost method to value specialised assets. Some outlier observations have been excluded for data presentation purposes.

Source: Productivity Commission estimates.

Historical cost method

For GTEs using historical cost valuations the ARR and ERR estimates were very similar (figure 4.1c). GTEs using this method rarely revalue their specialised assets. They use the historical value of assets and depreciate them over time. As a result, capital gains and losses are not recorded and the asset revaluation reserve does not

change from year to year.⁵ Where this is the case, the ERR estimate effectively becomes:

$$ERR = \frac{EBIT + NIBL}{\frac{1}{2}(A_e + A_b) + \frac{Da}{2}} \quad [4.6]$$

The simplified ERR measure is equal to the ARR adjusted for NIBLs and accounting depreciation. Depreciation reduces the value of the ERR relative to the ARR and NIBLs has the opposite effect. The data indicate that the net effect of these variables on the ERR is small, resulting in similar estimates for the ARR and ERR.

Fair value methods

The relationship between the ARR and ERR is more ambiguous for GTEs that value assets using a fair value method. The ERR resulted in systematically higher estimates of the rate of return than the ARR, but there is no clear linear relationship (figure 4.1b).

Under fair value methods, asset values change over time to reflect current market conditions, with capital gains (or losses) included in the asset revaluation reserve. Most GTEs using a fair value method (89 per cent) reported an increase in their asset revaluation reserve over the period, 2000-01 to 2003-04 (table 4.2). The rate of return is higher for most GTEs when estimated by the ERR because these capital gains are included in the measure of income in the ERR.

Table 4.2 Number of GTEs reporting changes in their asset valuation reserves, from 30 June 2001 to 30 June 2004

<i>Valuation method</i>	<i>Declines</i>	<i>Increases</i>	<i>Zero or less than 1 per cent</i>
Historical cost	2	3	14
Fair value	3	24	0
Other ^a	2	7	1

^a Includes GTEs that used a combination of asset valuation methods in one year or changed methods over the period.

Source: Productivity Commission estimates.

⁵ Over 70 per cent of GTEs using the historical cost method recorded no change, or a change of less than 1 per cent, in their asset revaluation reserve from 30 June 2001 to 30 June 2004 (table 4.2). For the remainder, most changes resulted from a revaluation of land rather than specialised assets.

GTEs that use a fair value method but record changes in the value of capital in EBIT, instead of in their asset revaluation reserves, yield a similar estimate of the rate of return using either measure, similar to GTEs using historical cost valuations. Variation in the level of capital gains along with the effects of depreciation and NIBLs reduce the correlation between the ARR and ERR estimates.

The effect of valuation methods on estimates of the rate of return is illustrated in box 4.2.

Box 4.2 Illustration of the effect of asset valuation methods on rate of return estimates

GTEs generally report their asset values using only one valuation method per year. However, Delta Electricity valued its property, plant and equipment using both the depreciated replacement cost method and the historical cost method in its 2005-06 annual report. This allowed the effect of asset valuation methods on the estimated rate of return to be analysed.

Annual rate of return estimates for Delta Electricity, 2005-06 (per cent)^a

<i>Valuation method</i>	<i>ARR</i>	<i>ERR</i>
Historical cost	20.9	19.6
Depreciated replacement cost	13.7	13.0

^a Based on data from 2004-05 and 2005-06. The methods used to value assets other than property, plant and equipment are detailed in the Delta Electricity 2005-06 annual report.

For each valuation method the estimates of ARR and ERR were very similar. However, for each measure of return the estimates differed significantly by the asset valuation method used.

Delta Electricity did not record a capital gain in 2005-06 (as reported in its asset revaluation reserve), simplifying the ERR measure (equation 4.6) and bringing it closer to the ARR (equation 4.1). Consequently, the ARR and ERR measures are similar irrespective of the asset values used, contrary to the trend in the total sample of GTEs using a fair value method.

For the ARR — and for the ERR if there is zero capital gain — higher asset values must result in a lower estimate of the rate of return. Using the depreciated replacement cost method, Delta Electricity's assets were valued 48 per cent higher than under the historical cost method. As a result, estimates of the ARR and ERR are around 50 per cent higher under the historical cost method.

The adjustments for NIBLs^a and accounting depreciation appear to have had negligible effects on the rate of return estimates.

^a NIBLs, as reported, generally include items called non-interest bearing liabilities as well as payables, creditors, trade creditors, accruals and 'other' liabilities. Provisions, interest bearing liabilities, deferred tax liabilities and employee entitlements were specifically excluded from NIBLs.

Source: Delta Electricity (2006).

Effect of large revaluations and acquisitions

Under both valuation methods, there are some outlying estimates that are inconsistent with observed trends. These estimates appear to be associated with large infrequent events such as acquisitions and asset revaluations.

Large acquisitions tend to distort results because the timing of changes in the balance sheet might differ from changes in the income statement, affecting the measured rate of return. These effects can be smoothed by calculating moving averages over a longer time period.

Fair value methods require regular asset revaluations. However, the frequency and size of revaluations, and changes in the method used, can significantly affect the measured rate of return of a GTE. Frequent asset revaluations and consistent use of methods over time encourage gradual changes in asset values and stable rates of return estimates. The effect of a large asset revaluation on the ARR and ERR estimates is illustrated in box 4.3.

Box 4.3 Illustration of the effect of large asset revaluations

Macquarie Generation revalues its property, plant and equipment assets every year. The value of land, buildings, plant and equipment associated with power stations is based on fair value. The valuation in 2002-03 resulted in a 52 per cent increase in the value of non-current property, plant and equipment and contributed to an \$871 million increase in the asset revaluation reserve. The capital gain produced a large one-off increase in the annual ERR estimate and had a small effect on the ARR estimate.

Annual rate of return, 1999-2000 to 2004-05 (per cent)

	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05
ARR	6.7	10.2	12.3	8.9	8.9	8.5
ERR	7.2	10.4	12.5	52.9	12.8	7.1

It had a smaller but more sustained effect on the three-year moving average ERR estimates.

Three-year moving average rate of return, 2000-01 to 2003-04 (per cent)

	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05
ARR	na	9.6	10.3	9.8	8.8	na
ERR	na	10.1	25.0	24.5	21.3	na

Source: Macquarie Generation annual reports (various); Productivity Commission estimates.

Other factors influencing rate of return estimates

There are a number of factors that could have contributed to the low rates of return consistently measured for some GTEs. Specifically, the underpayment of CSOs and the treatment of contributed assets and assets under construction have the effect of lowering estimated rates of return.

Community service obligations

Governments can direct GTEs to undertake non-commercial activities and services. If GTEs are to operate on a fully commercial basis, governments must make payments to cover the cost of the CSOs. Rates of return will be lower than otherwise, if payments do not cover the shortfall between the income received from delivery of services and their full cost — including a return on committed capital.

Productivity Commission analysis of CSO arrangements in the past revealed that some CSO activities are under funded or not funded at all (PC 2002a). For example, when GTEs are reimbursed for providing a CSO, they are not always compensated for the costs of administration, which reduces the rate of return they can achieve.

The ERR measure accounts for unfunded CSOs by removing their cost from economic income. This increases the rate of return to the level that would have been achieved if the government had fully funded the CSOs. However, unfunded CSO expenses are generally not recorded. Consequently, the reported ERR estimates could not be adjusted for most GTEs and understate the true rate of return from non-CSO operations.

Contributed assets

Some GTEs receive assets and funds from developers free of charge. This occurs most commonly in the electricity and water sectors. Some GTEs also receive capital contributions from government.

Contributed capital is generally recorded as revenue in the year it is received and thereafter is included in the asset base. These assets must be consistently accounted for in both income and the asset base in order to calculate the ERR accurately.

In its 1996 report, the Steering Committee on National Performance Monitoring of Government Trading Enterprises stated that consistency requires:

... that, in addition to the annual capital charge recorded in the profit and loss account, the implicit interest on the contribution should also be included in income. (SCNPMGTE 1996, p. 55)

Without this adjustment, the ERR estimates will be artificially low. The effect of ignoring the implicit interest is illustrated in box 4.4.

In addition, many jurisdictions exclude contributed capital from the regulatory asset base used to determine prices so that new users do not pay twice for the capital. This lowers the potential return that GTEs can achieve on their assets, irrespective of the measure used to estimate the rate of return.

The NSW Independent Pricing and Regulatory Tribunal (IPART), for example, does not provide for the replacement of contributed assets in Sydney Water's service charges until the expense is incurred.

IPART makes no provision for the replacement of such assets in determining Sydney Water's water and sewerage service charges until such time as they are due to be replaced, with the cost paid for by Sydney Water. IPART considers that to do otherwise would have the effect of Sydney Water being funded twice for the same assets. (Auditor-General NSW 2006, p. 179)

IPART's approach resulted in an estimated discounted future net cash inflow of \$10 billion, less than half the estimated replacement value of assets of \$22 billion in 2006.

Box 4.4 The effect of capital contributions on rate of return estimates

As part of its 2004 electricity price review, Country Energy undertook a revaluation of its system assets using a fair value method (depreciated optimised replacement cost). As part of this revaluation, capital contributions were estimated to account for around 24 per cent of system assets.

Assuming that the proportion of capital contributions remains stable over time, the ERR can be re-estimated, with the implicit interest included. This adjustment increased the ERR estimates by between 13 and 16 per cent, indicating that the treatment of contributed capital can significantly affect the ERR estimates.

The effect of implicit interest on contributed capital (per cent)^a			
	<i>2002-03</i>	<i>2003-04</i>	<i>2004-05</i>
ARR	7.4	7.8	9.5
ERR			
Original	7.8	7.2	9.2
Including implicit interest	9.0	8.4	10.4

^a Rate of return data are mid-point estimates based on three-year simple moving averages of the primary data. For example, estimates for 2003-04 are based on data from 2002-03, 2003-04 and 2004-05. Country Energy is not included in the total sample discussed above because its first year of operation was 2001-02.

Source: Country Energy annual reports (various); Productivity Commission estimates.

Assets under construction

Assets under construction require funding and are traditionally included in the reported asset base, even though they are not yet operational and do not produce a return. In order to consistently account for the effect of these assets on the rate of return, the interest during construction (IDC) must be estimated and included as a capital gain. However, the data required to estimate the IDC are unavailable from annual reports.

An alternative approach would be to include assets under construction in the asset base only upon completion. However, this would be conceptually inferior to estimating the IDC because it ignores the cost of capital committed during construction.

Ignoring the effects of assets under construction reduces the estimated economic income and the ERR.

4.4 What are the implications for capital management?

The estimated ARR of many GTEs suggests that they are not operating on a commercially viable basis. However, this measure provides limited insight into GTE performance because of its simplistic treatment of income and assets.

The ERR is conceptually superior, but in practice it also has some limitations because of poor data quality and availability. Despite its limitations, the ERR estimates provide some additional information about the profitability of GTEs.

Most GTEs recorded a higher ERR than ARR — primarily because of positive capital gains. The average rate of return on assets for GTEs using observations across the four years was 5.1 per cent using the ARR and 7.1 per cent using the ERR (table 4.1).

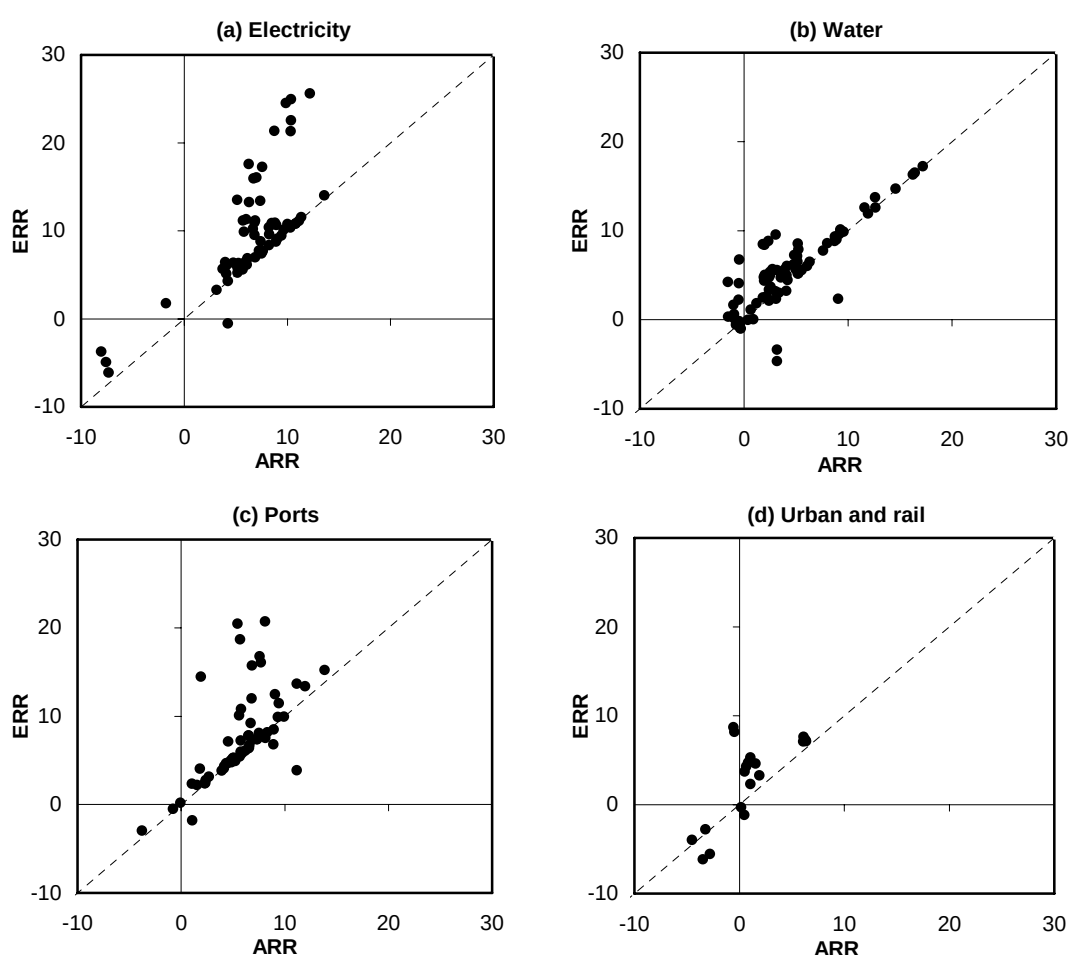
Still, many GTEs did not achieve an ERR above the risk-free benchmark, reinforcing the conclusion that significant shortcomings remain in the performance of GTEs. Of the 222 observations (excluding outliers) around 52 per cent (using the ARR) and 42 per cent (using the ERR) did not reach this very conservative target.⁶ Although the rates of return vary according to the measure used, the results consistently suggest many GTEs are underperforming.

⁶ The risk-free rate of return used is the interest rate on a 10-year Australian Government reference bond, which was 5.9 per cent in 2000-01, 5.4 per cent in 2001-02, 5.7 per cent in 2002-03, and 5.4 per cent in 2003-04 (RBA 2007a).

That said, there has been some improvement over time. Across the four-year period of analysis, the number of GTEs achieving the risk-free benchmark increased using both measures. In 2000-01, 40 per cent (using ARR) and 51 per cent (using ERR) of GTEs recorded a rate of return above the risk-free benchmark. This had increased to 54 per cent and 64 per cent respectively by 2003-04.

Across sectors, the rate of return on assets varied significantly (figure 4.2). Electricity GTEs recorded the highest rates of return on assets, with mean sector estimates of 6.6 per cent using the ARR and 9.8 per cent using the ERR. On average, urban transport GTEs had the lowest rates of return, recording -0.4 per cent using the ARR and 1.9 per cent using the ERR.

Figure 4.2 Rates of return by sector, 2000-01 to 2003-04 (per cent)^a



^a Rate of return data are mid-point estimates based on three-year simple moving averages of the primary data. For example, estimates for 2003-04 are based on data for 2002-03, 2003-04 and 2004-05. An observation on the 45° line is the same for each measure. An observation above the 45° line is higher when estimated by ERR. Some outlier observations have been excluded for data presentation purposes.

Source: Productivity Commission estimates.

The poor performance of many GTEs persists despite governments having agreed that corporatised businesses should operate on a fully commercial basis — that is, to ensure a return of at least the weighted average cost of capital on their assets over time. Furthermore, governments have agreed that they should operate on a competitively neutral basis with the private sector. Yet, after a decade of reform, many GTEs are still not achieving a normal rate of return and fulfilling their Council of Australian Governments undertakings.

There are a number of possible explanations for low profitability that are symptomatic of governance shortcomings, including:

- Governments are not prepared to fully fund CSOs, possibly to avoid public scrutiny of the extent of the subsidy or transfers between consumers;
- Prices are set below the level required to make a commercial rate of return:
 - regulators have used assumptions that differ from those underlying the GTE's operating circumstances or that are in error;
 - governments have written down assets or issued directives to boards to set low prices because there are externalities and other economic benefits that the government wishes to generate; and
- Prices are reflective of efficient costs but the GTE is operating inefficiently.

Failure to operate a business on a fully commercial basis potentially distorts demand and resource allocation over time. Consumers of GTE services make investment decisions concerning complementary activities based on not having to meet all costs. Further, GTE managers are not subject to market disciplines that are critical in the absence of strong competition.

PART B

5 Electricity

The financial performances of 23 electricity government trading enterprises (GTEs) are reported in this chapter. The GTEs vary significantly in size and the range of generation, transmission and distribution services they provide.

These GTEs generated \$19.0 billion in revenue in 2005-06 and controlled assets valued at \$62.2 billion. The group also returned almost \$2.3 billion to their respective owner-governments, through income tax-equivalent payments and dividends.

The majority (18) of the monitored GTEs operate in the National Electricity Market (NEM), a wholesale market for the supply and purchase of electricity. The five monitored GTEs not currently operating in the NEM are based in WA and the NT. Tasmania entered the NEM on 29 May 2005 and began trading with other states when the Basslink interconnector became operational on 29 April 2006.

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 defined in chapter 1.

When making comparisons, consideration should be given to: differences in the nature and scale of the businesses; their individual market environments; a number of issues relating to the valuation of their assets; and the level of payments for community service obligations. Care should also be exercised when comparing data presented in this chapter with that presented in previous reports for two reasons.

1. The performance data presented in this report are based, for the first time, on the new Australian-equivalent International Financial Reporting Standards.
2. Data from GTE general purpose financial reports have been used for this report, whereas data presented in previous reports were based on government financial statistics. The reason for this change is set out in chapter 1.

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 (table 5.1).

Table 5.1 Activities — electricity GTEs, 2005-06^a

<i>Electricity GTE</i>	<i>Activities</i>			
	<i>Generation</i>	<i>Transmission</i>	<i>Distribution</i>	<i>Retail</i>
<i>Australian Government, New South Wales, Victoria</i>				
Snowy Hydro	✓	x	x	x
<i>New South Wales</i>				
Country Energy	x	x	✓	✓
Delta Electricity	✓	x	x	x
EnergyAustralia	x	✓	✓	✓
Eraring Energy	✓	x	x	x
Integral Energy	x	x	✓	✓
Macquarie Generation	✓	x	x	x
Transgrid	x	✓	x	x
<i>Queensland</i>				
CS Energy	✓	x	x	x
ENERGEX	x	x	✓	✓
Enertrade ^b	✓	x	x	x
Ergon Energy Group	x	x	✓	✓
Powerlink	x	✓	x	x
Stanwell Corporation	✓	x	x	x
Tarong Energy	✓	x	x	x
<i>Western Australia</i>				
Horizon Power	✓	✓	✓	✓
Synergy	x	x	x	✓
Verve Energy	✓	x	x	x
Western Power	x	✓	✓	x
<i>Tasmania</i>				
Aurora	x	x	✓	✓
Hydro-Electric Corporation	✓	x	✓	✓
Transend Networks	x	✓	x	x
<i>Northern Territory</i>				
Power and Water Corporation	✓	✓	✓	✓

^a No electricity GTEs exist in Victoria or South Australia as the supply of electricity was completely privatised in these states during the mid 1990s. ^b Enertrade also trades power from privately-owned generators into the National Electricity Market.

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 23 GTEs monitored, 13 were involved in only one activity in 2005-06. Nine solely

generated electricity, three solely transmitted electricity and one solely provided retail services. The remaining 10 performed more than one activity, with two fully-integrated utilities — Horizon Power in WA and Power and Water Corporation in the NT — involved in all four activities.¹

In addition to providing generation, transmission, distribution or retailing services, and combinations thereof, many electricity GTEs are also involved in engineering consulting services. In 2005-06, five electricity GTEs also supplied gas and two — Country Energy and Power and Water Corporation — were involved in supplying water. A further two GTEs that generate hydro-electricity — the Hydro-Electric Corporation (HEC) in Tasmania and Snowy Hydro — had water management roles.

The set of monitored electricity GTEs has changed over the last five years (table 5.2). Two GTEs were excluded in 2005-06 and four new entities included. Country Energy absorbed the operations of Australian Inland Energy on 1 July 2005, and the Western Power Corporation was disaggregated into four independent corporations (Verve Energy, Western Power, Synergy and Horizon Power) on 1 April 2006.

Between 2004-05 and 2005-06, total assets controlled by electricity GTEs grew by \$9.6 billion (18 per cent) in real terms to \$62.2 billion (figure 5.1). Of this \$9.6 billion increase, \$6.1 billion was attributable to the inclusion of the four new WA GTEs, while the remaining \$3.5 billion represented real growth in assets of the

Table 5.2 Changes to monitored electricity GTEs, 2001-02 to 2005-06

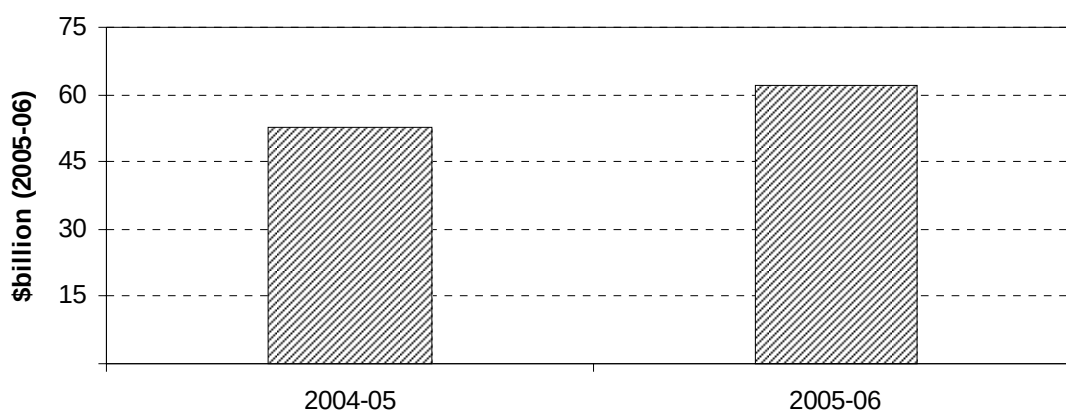
<i>Period</i>	<i>Number monitored</i>	<i>New entities</i>	<i>Replaced or merged entities</i>
2001-02	21	Power and Water Authority, Country Energy ^a	Pacific Power, NorthPower, Advance Energy, Great Southern Energy
2002-03	21	Snowy Hydro	Snowy Mountain Hydro-Electric Authority
2003-04	21		
2004-05	21		
2005-06	23	Verve Energy, Western Power, Synergy, Horizon Power ^b	Western Power Corporation, ^b Australian Inland Energy ^c

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

^b Western Power Corporation was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. ^c Country Energy absorbed the operations of Australian Inland Energy on 1 July 2005.

¹ For this chapter, electricity GTEs are classed as ‘generation’, ‘transmission’ or ‘distribution’ GTEs according to their primary activity (with distribution including retailing). The two GTEs that perform generation, transmission, distribution and retailing are classified as ‘integrated’ GTEs.

Figure 5.1 Sector assets — electricity GTEs^a



^a The value of sector assets is reported in 2005-06 dollars using the ABS implicit price deflator — gross fixed capital formation for public corporations (chapter 1).

Source: Productivity Commission estimates.

other electricity GTEs. Ergon Energy Group (Ergon) and ENERGEX were the largest contributors to total asset growth, with real increases in the value of their assets of \$762 million and \$734 million respectively.

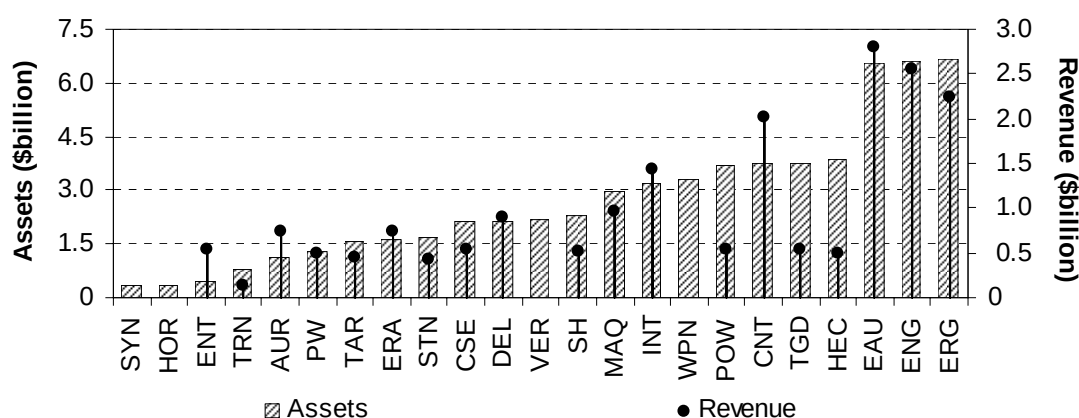
Among electricity GTEs, the asset base of transmission GTEs grew the most (relative to the asset bases of generation and distribution GTEs) in real terms from 2004-05 to 2005-06, increasing by \$3.4 billion. However, this was almost entirely because of the inclusion of the new Western Power transmission GTE, which had total assets of \$3.3 billion in 2005-06. Excluding the new WA GTEs, the asset base of distribution GTEs recorded the largest asset growth, increasing by \$2.2 billion in 2005-06.

The size of the monitored electricity GTEs, in terms of the value of the assets controlled and revenue generated, varies (figure 5.2). In 2005-06, the smallest in terms of asset value was Synergy (\$342 million) and the largest was Ergon (nearly \$6.7 billion).

Structural reform

The Australian electricity supply industry originally developed on a state-by-state basis, with vertically integrated, government-owned utilities. A major driver of structural reform in the electricity industry during the 1990s was the inter-governmental agreement on the National Competition Policy (NCP), which

Figure 5.2 Assets and revenue — electricity GTEs, 2005-06^a



^a Western Power Corporation was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. Data for the new entities are available for the period 1 April 2006 to 30 June 2006 only. In this figure, these entities have been included in assets but not in revenue.

Source: Productivity Commission estimates.

culminated in the establishment of the NEM. 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.²

In NSW, Pacific Power was successively broken up and restructured during the mid 1990s, resulting in the creation of the three separate generation businesses that are currently in operation. In distribution, 25 electricity distributors were amalgamated in 1995 to result in six distribution businesses, three of which were subsequently merged in 2001 to form four distribution GTEs. Country Energy absorbed the operations of Australian Inland Energy on 1 July 2005, leaving three distribution businesses in total in NSW.

A similar program of reform was undertaken in Queensland during the late 1990s. The assets of AUSTA Electric were used to form three generation businesses in July 1997. Around the same time, two retail GTEs were established as subsidiaries of regional distribution companies that had previously been part of the Queensland Transmission and Supply Corporation (QTSC). The transmission business of the

² An industry is considered to be a natural monopoly if average 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.

QTSC was established as a separate corporation trading as Powerlink, along with a fourth generation GTE subsequently renamed Enertrade.³

In WA, Western Power Corporation was established as a government-owned corporation in 1995 following the disaggregation of the State Energy Commission of Western Australia. On 1 April 2006, Western Power was itself disaggregated into four independent corporations — Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider).

In Tasmania, the 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 (Transend) and the retailing and distribution functions were transferred to Aurora Energy.

No electricity GTEs exist in Victoria or SA as the supply of electricity was completely privatised in these states during the mid-1990s. In SA, electricity GTEs were progressively restructured and their assets sold or transferred under long-term leases to the private sector in 1999 and 2000.

In the ACT, the government-owned ACTEW Corporation Limited (ACTEW) and joint venture partner AGL, provide electricity distribution and retailing services. This public-private joint venture, ActewAGL Distribution, owns and operates the electricity distribution network in the ACT, while retailing is performed by the partnership ActewAGL Retail. Since most of ACTEW's consolidated assets and revenue are associated with the provision of water services, its financial performance is discussed in chapter 6.

5.2 Market environment

Governments have introduced reforms aimed at improving the efficiency and financial performance of electricity GTEs. The 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

³ The Queensland Power Trading Corporation (QPTC) 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 QTSC. The QPTC was also involved in trading electricity generated by a number of private-sector generators. Although established as a transitional body, the QPTC became Queensland's fourth generation GTE in June 1999 and was renamed Enertrade.

have implications for the financial performance of GTEs and the comparison of performances over time.

The National Electricity Market

The most significant change to the market environment in the last decade has been the continued development of the NEM and its associated regulatory structures, along with the introduction of user choice of electricity supplier in each jurisdiction.

The National Electricity Market Management Company (NEMMCO) manages the NEM, in accordance with the National Electricity Rules (formerly known as the Electricity Code). The NEM officially commenced operating in December 1998, although trade between the NSW and Victorian wholesale markets commenced in May 1997.

Although WA and the NT do not participate in the NEM, both jurisdictions have introduced (under commitments to NCP) 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 networks.⁴

The WA Wholesale Electricity Market commenced operations in September 2006, providing a vehicle for electricity trading between generators and distributors. Market Rules governing the wholesale market were established on 1 October 2004, with a statutory corporation, the Independent Market Operator (responsible for administration and operation of the market), established on 1 December 2004.

These changes and the development of the NEM have a number of implications for GTE performance. Transmission and distribution businesses face greater regulatory scrutiny. Further, most electricity generation and 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 for distribution and transmission networks. These provisions give retailers and businesses purchasing wholesale electricity a right of access to these networks.

⁴ Following the departure in 2001-02 of NT Power from the NT market, Power and Water Corporation is the only supplier of electricity to the vast majority of Territorians.

Recent developments in the National Electricity Market

While difficult to measure at this time, there are a number of recent and prospective changes in the operation of the NEM which are likely to impact on the financial performances of GTEs (box 5.1).

Recent moves within the energy industry toward integration of generators and retailers might also affect efficiency and competitiveness in the NEM. In response to businesses seeking to merge generation and retail, the Australian Competition and Consumer Commission (ACCC) has argued that this type of merger can be beneficial because of improved risk management and that it is not necessarily anti-competitive (Willet 2005a, 2005b). Consequently, the ACCC does not currently have an objection *per se* to such vertical integration and some further merger activity can be expected.

Price and environmental regulation

Most of the monitored electricity GTEs operate under some form of price regulation. The various state and national regulators and the GTEs affected are summarised in table 5.3.

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).⁵ The ETEF is designed to provide a price cap for retail customers (those who purchase less than 160 MWh per annum), while enabling suppliers to earn a commercial rate of return.⁶

All electricity GTEs are subject to environmental regulation. On 8 December 2000, the Commonwealth Parliament passed the *Renewable Energy (Electricity) Act 2000*, establishing renewable energy targets for electricity supply in Australia. The legislation requires wholesale purchasers of electricity to proportionately contribute towards the generation of an additional 9500 GWh of renewable energy annually by 2010 (PC 2005c). From 1 April 2001, all energy wholesalers have had to purchase increasing amounts of electricity generated from renewable sources.

⁵ The Parer Review recommended that the NSW Government should abolish the Electricity Tariff Equalisation Fund. However, the NSW Government retained the ETEF for the suppliers of small, regulated retail customers (ACCC 2004, NSW Treasury 2005).

⁶ When the market price of electricity is higher than the energy cost component that retailers can recover from regulated customers (table 5.3), retailers withdraw the difference from the ETEF, enabling them to earn a commercial return while 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, the NSW government-owned generators are required to pay into the fund to ensure it is in balance.

Box 5.1 Recent developments in the National Electricity Market

Australian governments signed the Australian Energy Market Agreement in June 2004, giving effect to the recommendations of the Ministerial Council on Energy (MCE) that stemmed from the Council of Australian Governments (COAG) Energy Market Review in 2002 (the Parer Review).

The agreement includes the creation of the Australian Energy Market Commission (AEMC) with responsibility for rule making and market development, and the Australian Energy Regulator (AER) with responsibility for market regulation (other than retail pricing) and enforcement.

After being established on 1 July 2005, the AER has taken responsibility for the economic regulation of transmission networks in the National Electricity Market (NEM). The AER is expected to assume responsibility for the economic regulation (other than retail pricing) of the gas and electricity distribution networks in the NEM before the end of 2007.

Transmission capacity constraints were identified by the Parer Review as an impediment to improved competition in the NEM. The MCE recommended in December 2003 that the Regulatory Test applied by the AER to new transmission and distribution investment be revised to include the economic benefits of increased competition. The AER released a final decision on the review of the Regulatory Test in August 2004, which now provides for the specific inclusion of competition benefits and the appropriate definition to be used under the Test.

The Parer Review also noted that muted price signals for electricity users tend to inhibit the development of demand management and full retail contestability in the NEM. In the context of improving energy efficiency, the Productivity Commission has recommended any roll-out of 'smart metering' be subject to a comprehensive cost-benefit analysis (PC 2005c). At the February 2006 COAG meeting, the Australian, State and Territory Governments committed to a progressive roll-out of 'smart metering' technology from 2007, if the benefits outweigh the costs for residential users.

At the April 2007 COAG meeting, the Australian, State and Territory Governments agreed to establish a NEM Operator for both electricity and gas, encompassing a new national transmission planning function. It was decided that the new arrangements would not bind transmission companies to specific investment decisions, and that accountability for jurisdictional transmission investment, operation and performance will remain with the transmission network service providers. New South Wales stressed that its agreement to the establishment of the national transmission planning function was conditional on the planner not impeding the State's significant investment in its transmission network.

Source: COAG (2002, 2006a, 2007); PC (2005d).

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.

Table 5.3 Current economic regulation of electricity GTEs

<i>Jurisdictional regulators</i>	<i>Monitored GTEs affected</i>
Distribution and retailing	
<i>NSW — Independent Pricing and Regulatory Tribunal (IPART), Full Retail Contestability (FRC)</i> • IPART sets Regulated Retail Tariffs for customers using < 160 MWh. • Tariff regulation is transitional pending development of effective retail competition (in force until June 2007). • IPART sets a revenue cap and regulates access arrangements to distribution networks as jurisdictional economic regulator under National Electricity Rules (NER).	Country Energy, EnergyAustralia, Integral Energy
<i>QLD — Queensland Competition Authority (QCA), FRC in July 2007</i> • On delegation from Minister, QCA determines retail prices for non-contestable franchise customers (< 100 MWh). • QCA sets a revenue cap and regulates access arrangements to distribution networks as jurisdictional economic regulator under National Electricity Rules (NER).	Ergon Energy Group, ENERGEX
<i>WA — Economic Regulation Authority (ERA)</i> • Retail price cap for non-contestable customers <50 MWh, set by the Minister for Energy • FRC delayed until sufficient competition develops in generation and wholesale markets. • Minister for Energy directed Verve Energy to cap generation capacity at 3000 MW to reduce generation market dominance.	Synergy, Horizon Power
<i>TAS — Office of the Tasmanian Energy Regulator (OTTER), FRC by 2010</i> • OTTER sets maximum retail tariffs for residential and business customers. • Contestability to be phased in from July 2006 over a four-year period, beginning with larger customers (>20 GWh)	Aurora Energy
<i>NT — Utilities Commission (UC), FRC</i> • Retail prices for non-contestable customers <750 MWh subject to Treasurer's pricing order until competitive entry from other retailers. • Tranche 4 customers between 750 MWh and 2 GWh also subject to Treasurer's pricing order. • Revenue cap set by UC on the transmission and distribution assets of Power and Water.	Power and Water Corporation
Transmission	
<i>All States excluding WA and NT — Australian Energy Regulator</i> • Regulates the revenues of transmission network service providers by establishing revenue caps.	Transend Networks (Tas), EnergyAustralia (NSW), TransGrid (NSW), Powerlink (Qld)
<i>WA — Economic Regulation Authority (ERA)</i> • Regulates third-party access to the South West Interconnected Network, including determining revenue caps and tariffs for Western Power.	Western Power

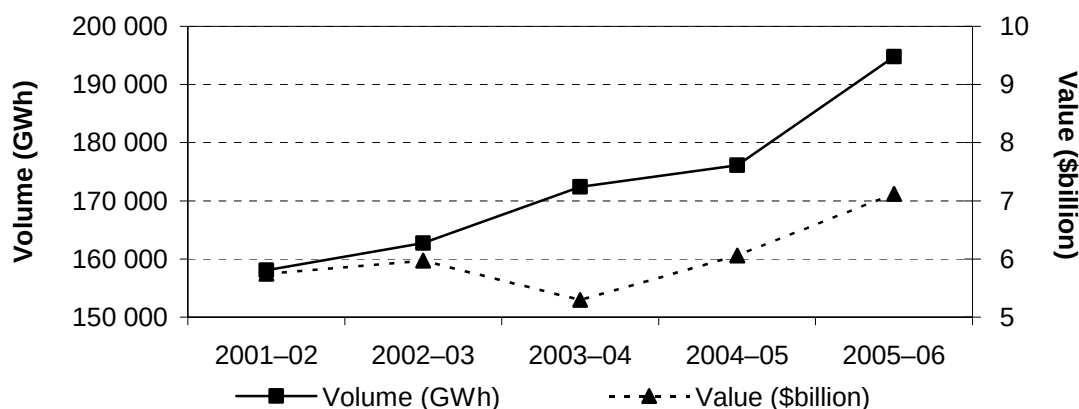
Source: AER (2007); IPART (2007); Office of Energy (2007a, 2007b); OTTER (2007a, 2007b); QCA (2005); UC (2007).

Production trends

Consumption of electricity in the NEM states is growing, with about 195 000 GWh of electricity passing through the NEM in 2005-06 (figure 5.3). This represents an 11 per cent increase on 2004-05 — more than double the average growth in demand for the previous three years. Further, peak demand increased to record levels in 2005-06 in all five states participating in the NEM (NEMMCO 2006).

Although prices varied across jurisdictions, the average price of electricity also increased by 6.2 per cent (to \$37 per MWh) in 2005-06. The net effect of increasing volumes and average prices was an increase of 17 per cent in the total value of electricity passing through the NEM (to \$7.1 billion) in 2005-06.

Figure 5.3 National Electricity Market electricity volume and value^a



^a Volume data represents volume of electricity sent out of the National Electricity Market.

Source: NEMMCO (2006).

5.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings.

The monitored electricity GTEs (excluding the new WA GTEs) recorded a total pre-tax operating profit of \$2.9 billion in 2005-06, representing a \$1.4 billion (90 per cent) increase in real terms from 2004-05.⁷ However, this included a real

⁷ Data on revenue and expenditure for the new WA corporations are available only for the period 1 April 2006 to 30 June 2006. As a result, these entities are excluded from analysis of profitability, interest cover and transactions with government for 2005-06.

increase of \$589 million in the HEC's profit from an (inflation-adjusted) operating loss of \$522 million in 2004-05 to a profit of \$67.1 million in 2005-06. Both of these results were affected by impairment expenses related to the HEC's writeoff of its Bell Bay Power Station. If the HEC is excluded, real growth in sector profitability would have been \$779 million, or 38 per cent, in 2005-06.

All but one GTE (Enertrade) achieved a positive operating profit in 2005-06. In 2004-05, all electricity GTEs except Enertrade and the HEC recorded a profit. Enertrade reported operating losses in both 2004-05 and 2005-06, mainly because of power-purchase agreements entered into prior to the commencement of the NEM. Enertrade considers a number of these agreements to be onerous contracts and expects them to result in significant future losses (Enertrade 2005).⁸

The increase in sector profitability is largely attributable to the generation and distribution GTEs. Collectively, the generation GTE profits increased by nearly 420 per cent (\$974 million) in real terms between 2004-05 and 2005-06. This includes the \$589 million increase in the HEC's operating profit, as stated above. Distribution GTEs recorded a combined profit increase of 30 per cent (\$286 million) in 2005-06 and transmission GTEs had profit growth of 50 per cent (\$133 million). The integrated electricity GTE (Power and Water in the NT) experienced a real decline in profitability of 45 per cent (\$23.9 million).

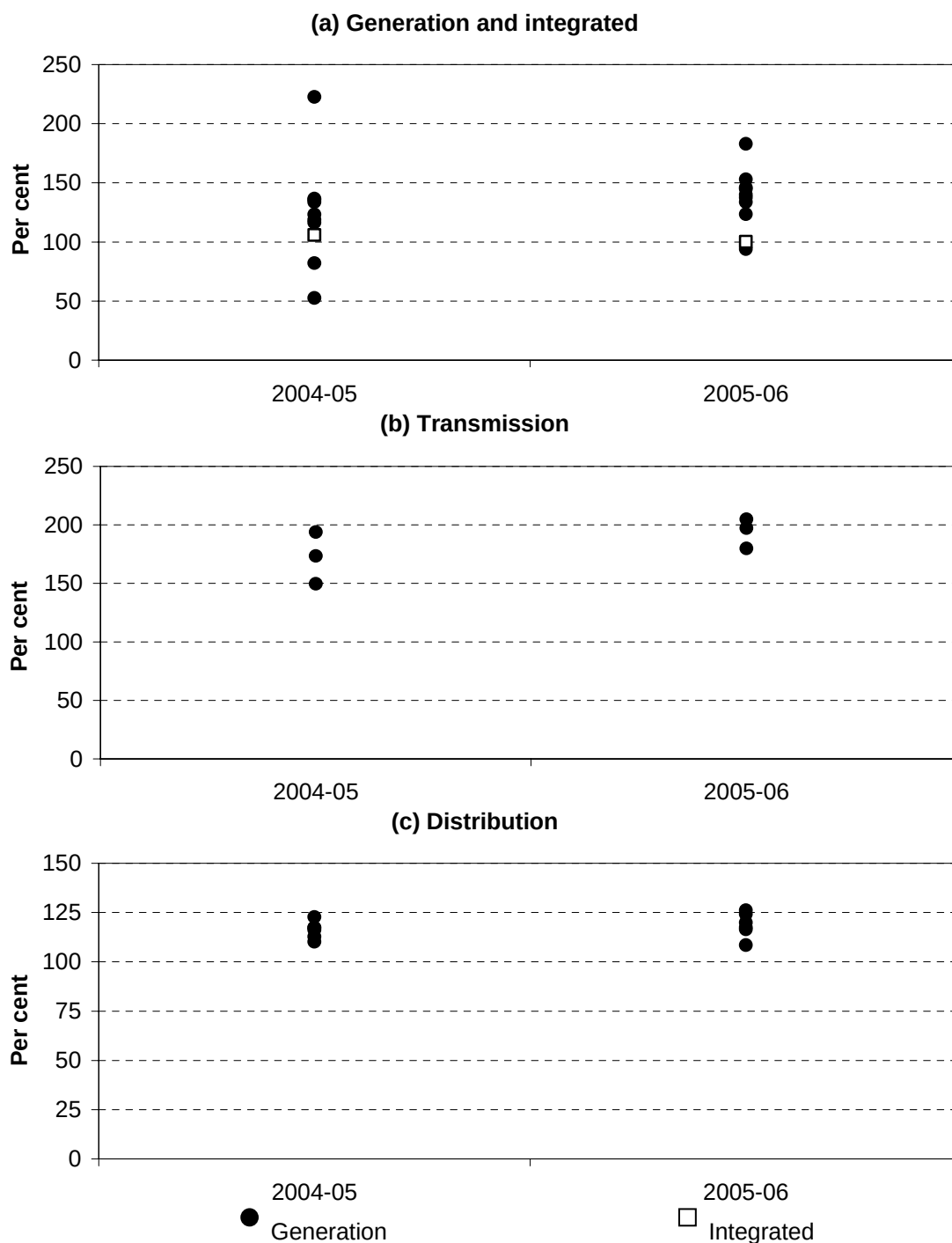
Increased demand for electricity was a major contributor to improved profitability in 2005-06. The volume of electricity in the NEM grew by 11 per cent to 195 000 GWh, contributing to a 17 per cent increase in the value of electricity dispatched. In addition, peak demand reached record levels in 2005-06 in every state in the NEM.

Cost recovery is a measure of a GTE's ability 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 (chapter 1).

Excluding the new WA GTEs, all but one of the electricity GTEs recorded a cost recovery ratio greater than 100 per cent in 2005-06, indicating that they were able to fully recover their operating costs from operating revenue (figure 5.4). The overall sector cost recovery ratio increased from 117.2 per cent to 126.8 per cent in 2005-06, a relatively small improvement in comparison with the growth in operating profits.

⁸ The agreements commit Enertrade to purchasing power at fixed prices over the terms of the respective agreements and selling it into the NEM at prevailing (currently lower) pool prices.

Figure 5.4 Cost recovery — electricity GTEs^{a,b}



^a 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 investment income and receipts from governments to cover deficits from total revenue. Expenses from operations is calculated by subtracting gross interest expense from total expenses. ^b Western Power Corporation was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. Data for the new entities are available only for the period 1 April 2006 to 30 June 2006, and so they have been excluded from this figure.

Source: Productivity Commission estimates.

The transmission GTEs had the highest level of cost recovery as a group in 2005-06, with TransGrid, Powerlink and Transend all recording cost recovery ratios of over 170 per cent. Distribution GTEs, as a group, had the lowest average cost recovery ratio of 119 per cent. Among generation and integrated GTEs, the level of cost recovery exhibited greater variation than in the other groups in both 2004-05 and 2005-06. In both of these years, the GTEs that did not fully recover operating costs were generation or integrated GTEs.

The increased level of operating profits in 2005-06 was reflected in an improvement in the overall sector return on assets, which rose from 5.2 per cent in 2004-05 to 7.8 per cent in 2005-06. Excluding the new WA GTEs, all but one of the electricity GTEs reported positive returns (up to 14 per cent) in 2005-06 (figure 5.5). Enertrade recorded a return of -9.3 per cent, following from its operating loss.

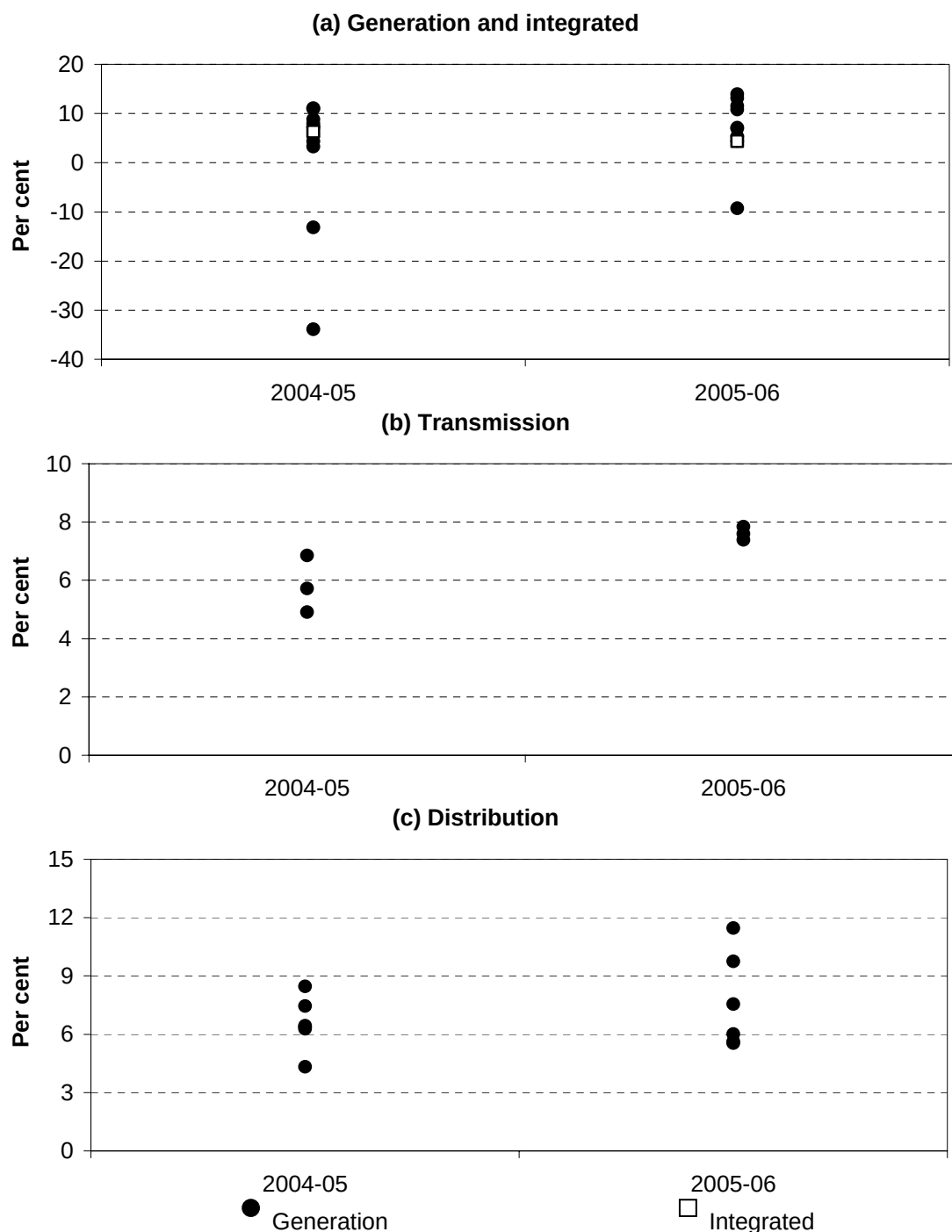
Substantial variation in return on assets exists within the generation and distribution groups of electricity GTEs. Among generation GTEs, returns ranged from -9.3 per cent to 14.0 per cent in 2005-06, and from -33.9 per cent to 11.1 per cent in 2004-05. The returns of distribution GTEs were in the range of 5.5 per cent to 11.5 per cent in 2005-06. However, there was much less variation in the returns achieved by the three transmission GTEs in 2005-06, which were all between 7.0 and 8.0 per cent.

The sector rate of return on assets of 7.8 per cent in 2005-06 was greater than the risk-free rate of return.⁹ The median rate of return on assets for the monitored electricity GTEs was 7.4 per cent, and therefore also exceeded the risk-free rate. Fifteen of the 19 electricity GTEs (excluding the WA GTEs) achieved a return on assets equal to or greater than 5.4 per cent in 2005-06.

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

⁹ The risk-free rate of return used is the 2005-06 interest rate on 10-year Australian Government reference bonds of 5.4 per cent (RBA 2007a).

Figure 5.5 Return on assets — electricity GTEs^{a,b}



^a 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 (includes abnormals) 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 could not be estimated, the value of total assets at the end of the financial year was used. ^b Western Power Corporation was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. Data for the new entities are available only for the period 1 April 2006 to 30 June 2006, and so they have been excluded from this figure.

Source: Productivity Commission estimates.

In 2005-06, only six of the 19 electricity GTEs (excluding the WA GTEs) achieved a return on assets in excess of 8.0 per cent. Further, the sector rate of return of 7.7 per cent and the median return of 7.4 per cent were both below 8.0 per cent. This indicates that most electricity GTEs, as well as the sector as a whole, are not achieving returns commensurate with the IPART and QCA benchmarks.

A lower than normal rate of return might be expected in the case of distributors. This is because a significant proportion of distributor assets are contributed, and as such, are excluded from the regulatory asset base in price determinations. Their revenue could be insufficient to achieve a normal rate of return on their total asset base.

The sector return on equity increased from 5.2 per cent in 2004-05 to 10.1 per cent in 2005-06, reflecting the improved sector profitability. Return on equity measures a GTE's earnings for the year expressed as a proportion of equity remaining in the business.

5.4 Financial management

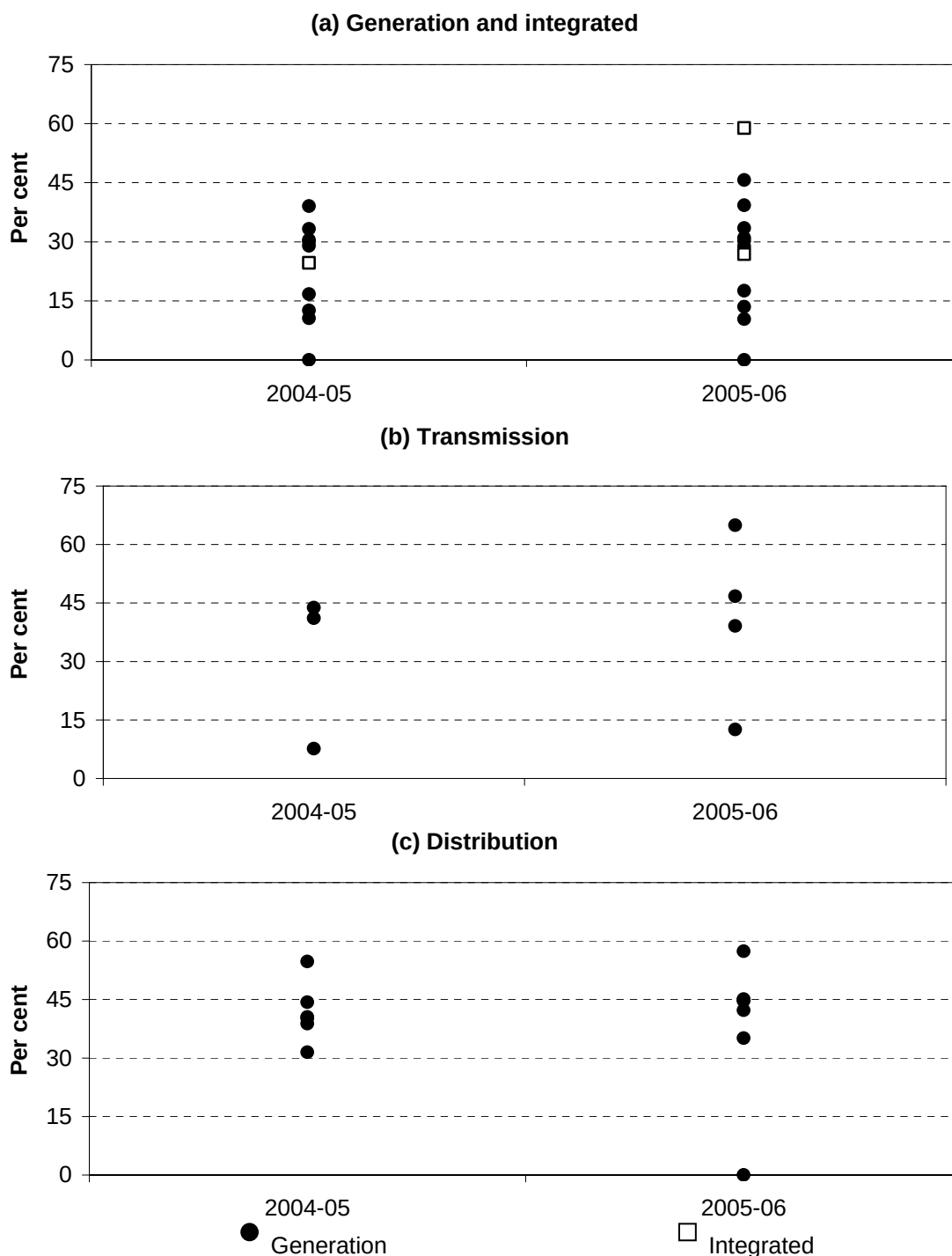
Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

Governments have, on occasion, imposed financial restructuring on their electricity GTEs. This has generally involved the transfer of both assets and liabilities to State and Territory governments, and the contribution or withdrawal of equity. In 2005-06, Eraring Energy made a \$49.0 million return of equity payment to the NSW Government. In contrast, CS Energy received a \$250 million equity contribution from the Queensland Government.

There is considerable diversity in the capital structure of electricity GTEs, as measured by the debt to total assets ratio (figure 5.6). Two electricity GTEs (Enertrade in Queensland and Synergy in WA) operated debt free in 2005-06, while three had debt to assets ratios of over 50 per cent. A majority (14 of 23) of electricity GTEs had debt to assets ratios between 25 per cent and 50 per cent in 2005-06.

The proportion of debt in the electricity sector's capital structure increased from 2004-05 to 2005-06, with the sector debt to assets ratio rising from 35.6 per cent to 41.2 per cent. Similarly, the median debt to assets ratio of the monitored electricity GTEs increased from 31.5 per cent in 2004-05 to 35.1 per cent in 2005-06. These

Figure 5.6 Debt to total assets — electricity GTEs^{a,b}



^a 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. Where an average was not available, the value of total assets at the end of the financial year was used. ^b Western Power Corporation was disaggregated into Verve Energy, Western Power, Synergy and Horizon Power on 1 April 2006. Data for the new entities are available only for the period 1 April 2006 to 30 June 2006, and so they have been excluded from this figure.

Source: Productivity Commission estimates.

results are partly attributable to the inclusion of the four new WA GTEs, three of which had debt to assets ratios of over 40 per cent in 2005-06.

A few electricity GTEs have moved against this trend by reducing their level of debt and, in turn, their debt to total assets ratio. For example, Macquarie Generation reduced its debt by 12 per cent in real terms from 2004-05 to 2005-06, leading to a fall in its debt to assets ratio from 33.2 per cent to 30.2 per cent. Stanwell reduced its borrowings by 20 per cent in real terms from 2004-05 to 2005-06, taking its debt to assets ratio from 12.6 per cent to 10.3 per cent, one of the lowest among the electricity GTEs.

In 2005-06, 10 electricity GTEs (excluding the WA GTEs) had an interest cover greater than 3.0 times. Only one GTE (Enertrade) had negative interest cover. The sector interest cover increased from 2.2 times in 2004-05 to 3.3 times in 2005-06, as the substantial increase in sector profitability outweighed the increase in borrowing costs. This indicates that the margin insulating electricity GTEs from increases in interest rates or falling revenue has increased in the last year, strengthening the ability of these GTEs to service their debt out of current earnings.

5.5 Transactions with government

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.

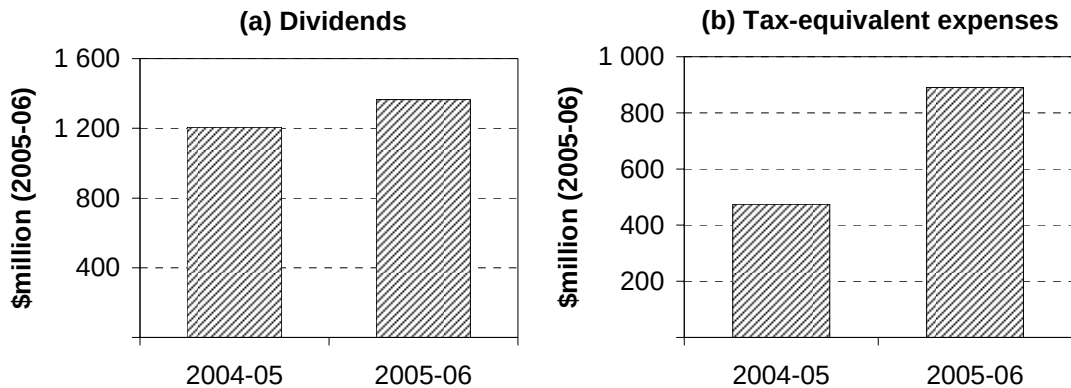
The introduction of income tax-equivalent regimes and requirements to pay dividends and debt guarantee fees are examples of how governments have imposed the principles of competitive neutrality on their electricity GTEs.

Most electricity GTEs now make tax-equivalent and dividend payments to their owner-governments. Between 2004-05 and 2005-06, tax-equivalent expenses for the sector as a whole increased by 88 per cent in real terms to \$890 million (figure 5.7), in line with the substantial increase in the sector's overall profitability.

Aggregate dividends also increased in 2005-06, but by a much smaller proportion (13 per cent in real terms) to \$1.4 billion. New South Wales electricity GTEs declared dividends totalling \$758 million in 2005-06, Queensland electricity GTEs declared dividends of \$462 million and Tasmanian electricity GTEs, \$65.7 million. Power and Water Corporation in the NT declared a dividend of \$10.2 million in 2005-06.

As part of the reform process, governments have also moved to identify, cost and fund the community service obligations (CSOs) that they imposed 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.

Figure 5.7 **Dividends and income tax-equivalent expenses — electricity GTEs^a**



^a The value of dividends and tax-equivalent expenses are reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1).

Source: Productivity Commission estimates.

Eight of the monitored electricity GTEs (excluding the new WA GTEs) received CSO funding in 2005-06. Generally, GTEs involved in distribution and retail are subject to these CSOs, although there are some examples of CSOs being placed on generation GTEs.

In June 1999, Queensland introduced the Benchmark Pricing Agreement (BPA), a negotiation between the Queensland Treasury and the Queensland retail GTEs — Energex and Ergon. Under the BPA, a retailer would receive a negotiated payment (CSO) if the regulated revenue from non-contestable customers is less than the cost of supplying their energy purchases. On 1 January 2004, the BPA was replaced by the Franchise Electricity Purchasing Agreement, which requires the retail GTEs to service specified ‘franchise’ customers in return for CSO funding.

Disclosed CSO payments to electricity GTEs amounted to \$484 million in 2005-06, a real increase of 38 per cent (\$133 million) from 2004-05. Approximately 88 per cent of total CSO payments were made to distribution GTEs, reflecting their involvement in retailing electricity.

5.6 Implications of the new accounting standards

From 2005-06, financial data for all monitored electricity GTEs are based on the Australian-equivalent International Financial Reporting Standards (AIFRS). The adoption of the new accounting standard changed the recognition and measurement of some assets, liabilities and equity items, and affected the recording of income flows. These changes, which were discussed in the previous *Financial Performance of Government Trading Enterprises* report (PC 2006, chapter 3), have had a significant effect on the comparability over time of financial performance and financial management indicators.

The aggregate impact of the transition to AIFRS for the monitored electricity GTEs can be gauged by comparing 2004-05 data on an AIFRS and pre-AIFRS basis (table 5.4). Similar comparisons can be made by reference to each GTE summary.

ELECTRICITY

Table 5.4 Whole of sector performance indicators, 2004-05 to 2005-06^a

		Pre-AIFRS ^{b,c}	AIFRS ^b	
	Units	2004-05	2004-05	2005-06 ^d
Size				
Total assets	\$m	50 274	50 189	62 177
Total revenue	\$m	17 657	17 238	19 019
Profitability				
Operating profit before tax	\$'000	2 278 194	1 446 442	2 882 742
Operating sales margin	%	19.2	15.0	21.4
Cost recovery	%	123.7	117.2	126.8
Return on assets	%	6.8	5.2	7.8
Return on equity	%	6.8	5.2	10.1
Financial management				
Debt to equity	%	79.7	93.9	104.8
Debt to total assets	%	35.6	35.6	41.2
Total liabilities to equity	%	123.8	164.1	181.8
Interest cover	times	3.0	2.2	3.3
Current ratio	%	69.9	62.7	73.1
Leverage ratio	%	223.8	264.1	281.8
Payments to and from government				
Dividends	\$'000	1 151 668	1 151 668	1 365 773
Dividend to equity ratio	%	5.1	6.1	6.9
Dividend payout ratio	%	75.7	115.9	68.5
Income tax expense	\$'000	756 873	453 104	890 314
CSO funding	\$'000	335 163	335 163	484 217

^a Figures are nominal values. ^b Electricity GTEs commenced reporting under Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for electricity GTEs. ^c Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^d On 1 April 2006, the former Western Power Corporation was disaggregated into four independent corporations (Verve Energy, Western Power, Synergy and Horizon Power). Data on revenue and expenditure for the new corporations in 2005-06 are available only for the period 1 April 2006 to 30 June 2006. As a result, these entities are excluded from the calculation of total revenue, all profitability indicators, all payments to and from government, and interest cover, for 2005-06. They are included in the calculation of total assets and all financial management indicators except interest cover.

5.7 GTE performance reports

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

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* (SOC Act) and the *Energy Services Corporations Act 1995* (ESC Act).

Delta generates electricity for supply into the National Electricity Market (NEM). Most of Delta's electricity is generated at its four coal-fired power stations, which have a total capacity of 4240 MW and which — according to Delta — provide 12 per cent of total supply in the NEM. Delta also generates a small amount of electricity from renewable energy sources. While not facing direct price regulation, Delta is subject to the National Electricity Law and National Electricity Rules, which set a maximum spot price of \$10 000 per MW (NEMMCO 2005).

Delta recorded a pre-tax operating profit of \$235 million in 2005-06, which represents a 54 per cent increase on the previous year. The increased profitability resulted from a relatively large increase in total revenue (\$72.8 million) combined with a decrease in total expenditure (\$9.1 million) from 2004-05 to 2005-06. High electricity prices during October–December 2005 — a period of peak electricity demand in NSW — accounted for most of the revenue growth.

The value of Delta's assets was \$2.1 billion in 2005-06, an increase of \$248 million from 2004-05. A \$195 million revaluation of plant and equipment accounted for a large part of this increase in total assets. Delta's level of debt was relatively steady at \$583 million in 2005-06. However, with an increase in the value of its assets, the debt to total assets ratio fell slightly from 30.5 per cent in 2004-05 to 28.8 per cent in 2005-06.

There was a shift towards short-term liabilities, as shown by a 34 per cent increase in current liabilities over the year. Current assets increased by a much smaller amount (4.8 per cent), leading to a decline in the current ratio from 62.8 per cent in 2004-05 to 49.0 per cent in 2005-06. This suggests that Delta's short-term assets would not have covered its short-term debts, if they had have fallen due.

Under the provisions of the SOC Act, 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 ESC Act. Delta provided for a \$132 million dividend payment, which represented 80 per cent of after-tax profit in 2005-06. It recorded an income tax-equivalent expense of \$70.3 million. Delta does not receive community service obligation funding from the NSW Government.

DELTA ELECTRICITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 892	1 900	2 148
Total revenue	\$m	829	816	889
Profitability				
Operating profit before tax	\$'000	180 481	152 910	234 748
Operating sales margin	%	28.2	25.2	31.6
Cost recovery	%	139.2	133.8	146.2
Return on assets	%	12.5	11.0	14.0
Return on equity	%	15.4	17.7	24.7
Financial management				
Debt to equity	%	72.4	95.9	79.9
Debt to total assets	%	30.6	30.5	28.8
Total liabilities to equity	%	136.3	214.5	194.3
Interest cover	times	4.2	3.8	5.9
Current ratio	%	70.0	62.8	49.0
Leverage ratio	%	236.3	314.5	294.3
Payments to and from government				
Dividends	\$'000	123 488	123 488	131 638
Dividend to equity ratio	%	15.4	20.4	19.7
Dividend payout ratio	%	100.0	115.6	80.0
Income tax expense	\$'000	56 993	46 046	70 257
CSO funding	\$'000	..	..	..

^a Delta Electricity (Delta) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Delta. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

MACQUARIE GENERATION

New South Wales

Macquarie Generation (Macquarie) operates under the *State Owned Corporations Act 1989* (SOC Act) and the *Energy Services Corporations Act 1995* (ESC Act). 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 estimates its contribution is around 14 per cent of total volume. Although it does not face direct price regulation, Macquarie is subject to the National Electricity Law and National Electricity Rules, which set a maximum spot price of \$10 000 per MW (NEMMCO 2005).

Macquarie's pre-tax operating profit increased 82 per cent (\$121 million) over the previous year to \$267 million in 2005-06. The result followed from revenue growth of 13 per cent (\$107 million), which Macquarie attributed to a 4.7 per cent increase in average sales prices and steady sales volume. This higher profitability caused the return on assets and return on equity to increase to 11.5 per cent and 18.7 per cent respectively.

Macquarie continued to reduce its debt over 2005-06 as part of an ongoing strategy. Total debt fell by \$74.4 million, or 7.8 per cent, from \$960 million to \$886 million. As a result, the debt to total assets ratio fell from 33.2 per cent in 2004-05 to 30.2 per cent in 2005-06. The lower debt level also reduced finance costs by 15 per cent, which in turn increased interest cover to 4.8 times (compared with 2.8 times in 2004-05).

Under the provisions of the SOC Act, Macquarie is required to make tax-equivalent and dividend payments. Dividend payments, as required by the ESC Act, are determined by the shareholder ministers. In 2005-06, Macquarie provided for a \$130 million dividend payment and recorded an income tax-equivalent expense of \$81.2 million.

Macquarie does not receive community service obligation funding from the NSW Government.

MACQUARIE GENERATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	2 882	2 889	2 972
Total revenue	\$m	852	852	958
Profitability				
Operating profit before tax	\$'000	166 844	146 489	267 098
Operating sales margin	%	28.9	26.5	34.6
Cost recovery	%	140.2	135.6	153.0
Return on assets	%	8.7	7.9	11.5
Return on equity	%	8.3	10.5	18.7
Financial management				
Debt to equity	%	75.7	97.6	88.3
Debt to total assets	%	33.3	33.2	30.2
Total liabilities to equity	%	127.1	193.6	196.2
Interest cover	times	3.0	2.8	4.8
Current ratio	%	59.4	56.7	72.6
Leverage ratio	%	227.1	293.6	296.2
Payments to and from government				
Dividends	\$'000	105 000	105 000	130 000
Dividend to equity ratio	%	8.3	10.7	13.1
Dividend payout ratio	%	99.6	101.4	69.9
Income tax expense	\$'000	61 423	42 892	81 247
CSO funding	\$'000	..	..	..

^a Macquarie Generation (Macquarie) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Macquarie. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

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* (SOC Act) and the *Energy Services Corporations Act 1995* (ESC Act).

Eraring generates and trades electricity within the National Electricity Market. Its generation assets have a capacity of 3042 MW — the largest being the Eraring coal-fired power station with a capacity of 2640 MW. While not facing direct price regulation, Eraring is subject to the National Electricity Law and National Electricity Rules, which set a maximum spot price of \$10 000 per MW (NEMMCO 2005).

Eraring's total revenue increased by \$130 million (22 per cent) from 2004-05 to 2005-06. Eraring attributes this to higher contract sales prices as well as higher spot prices on a small number of peak trading days. However, more than 70 per cent of the increase in total revenue resulted from increases in defined benefits superannuation revenue, insurance provision movements, and fair value movements in electricity derivatives.

As total expenditure increased by a relatively smaller amount (\$40.0 million, or 8.1 per cent), Eraring's pre-tax operating profit grew by 89 per cent from \$102 million in 2004-05 to \$192 million in 2005-06.

The value of Eraring's total assets was relatively steady at \$1.6 billion in 2005-06. However, total debt rose by \$47.6 million (28.9 per cent) to \$213 million, causing Eraring's debt to equity and debt to total assets ratios to increase to 23.4 per cent and 13.5 per cent respectively.

Eraring recorded a tax-equivalent expense of \$57.7 million in 2005-06. It provided for a \$41.3 million dividend payment, half the amount provided for in 2004-05.¹ Eraring also made a return of equity payment of \$49.0 million to the NSW Government.

Eraring received \$60 000 in community service obligation funding in 2005-06.

¹ In 2004-05, Eraring provided for \$82.3 million in dividend payments, which equated to a payout ratio greater than 100 per cent. Eraring reports that the dividend provision in 2004-05 was increased by \$2.2 million in order to fund payments relating to workers' compensation and dust disease court determinations for non-employees. The corporation noted this liability was transferred from the NSW Government to Eraring upon corporatisation, with agreement that the matter would be treated as a community service obligation to be paid for out of deductions from Eraring dividends.

ERARING ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05 ^c	2004-05 ^c	2005-06 ^d
Size				
Total assets	\$m	1 592	1 561	1 597
Total revenue	\$m	602	598	728
Profitability				
Operating profit before tax	\$'000	115 700	101 919	192 182
Operating sales margin	%	21.1	18.9	28.5
Cost recovery	%	126.7	123.3	139.9
Return on assets	%	8.0	7.3	13.2
Return on equity	%	6.9	6.8	13.8
Financial management				
Debt to equity	%	14.3	15.9	23.4
Debt to total assets	%	10.4	10.6	13.5
Total liabilities to equity	%	37.5	50.7	75.7
Interest cover	times	11.3	10.0	13.2
Current ratio	%	47.4	41.3	40.9
Leverage ratio	%	137.5	150.7	175.7
Payments to and from government				
Dividends	\$'000	82 327 ^e	82 327 ^e	41 320
Dividend to equity ratio	%	7.1	7.9	4.2
Dividend payout ratio	%	102.7	116.6	30.7
Income tax expense	\$'000	35 571	31 317	57 693
CSO funding	\$'000	89	89	60

^a Eraring Energy (Eraring) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Eraring. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Eraring repaid capital of \$16.0 million in August 2004 via a non-cash equity to debt swap. ^d In 2005-06, Eraring returned \$49.0 million of equity to the NSW Government. ^e In 2004-05, Eraring provided for more than \$82.0 million in dividend payments, which equated to a payout ratio greater than 100 per cent. Eraring reports that the provision for dividends in 2004-05 was increased by \$2.2 million in order to fund payments relating to workers' compensation and dust disease court determinations for non-employees. The Corporation noted this liability was transferred from the NSW Government upon corporatisation, with agreement that the matter would be treated as a community service obligation to be paid for out of deductions from Eraring dividends.

TransGrid 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 operates under the *State Owned Corporations Act 1989*, and its revenues are subject to regulation by the Australian Energy Regulator.

TransGrid is responsible for the planning, management and development of the NSW 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, Queensland and SA.

TransGrid more than doubled its pre-tax operating profit from \$77.4 million in 2004-05 to \$175 million in 2005-06. Total revenue grew by \$109 million (26 per cent) over this period. Of this increase, \$27.3 million was an increase in operating revenue, and \$81.7 million represented positive movements in the value of superannuation reserves. The growth in profitability resulted in increases in TransGrid's return on assets and return on equity to 7.4 per cent and 7.9 per cent respectively.

The value of TransGrid's total assets increased slightly from \$3.7 billion in 2004-05 to \$3.8 billion in 2005-06. Total debt fell by 4.2 per cent, which reduced the debt to equity and debt to total assets ratios to 89.8 per cent and 39.1 per cent respectively.

TransGrid is required to make tax-equivalent and dividend payments to the NSW Government. TransGrid provided for a dividend payment of \$69.5 million in 2005-06 (up from \$38.0 million in 2004-05),¹ and recorded an income tax-equivalent expense of \$50.6 million. TransGrid does not receive community service obligation funding from the NSW Government.

¹ The reduced dividend in 2004-05 was determined by the Board in accordance with TransGrid's Statement of Corporate Intent 2004-05, as agreed with shareholding ministers.

TRANSGRID (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	3 733	3 697	3 750
Total revenue	\$m	472	427	536
Profitability				
Operating profit before tax	\$'000	116 449	77 423	175 259
Operating sales margin	%	46.6	42.4	51.2
Cost recovery	%	187.2	173.5	204.8
Return on assets	%	5.9	4.9	7.4
Return on equity	%	4.1	3.4	7.9
Financial management				
Debt to equity	%	81.4	99.8	89.8
Debt to total assets	%	40.7	41.1	39.1
Total liabilities to equity	%	99.8	142.9	131.4
Interest cover	times	2.1	1.7	2.8
Current ratio	%	41.8	24.4	24.2
Leverage ratio	%	199.8	242.9	231.4
Payments to and from government				
Dividends	\$'000	38 000	38 000	69 500
Dividend to equity ratio	%	2.0	2.5	4.4
Dividend payout ratio	%	49.3	72.5	55.7
Income tax expense	\$'000	39 320	25 020	50 571
CSO funding	\$'000	..	..	..

^a TransGrid commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for TransGrid. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

EnergyAustralia operates under the *State Owned Corporations Act 1989* and the *Energy Services Corporations Act 1995*. The majority of EnergyAustralia's revenues are derived from electricity distribution and retailing, operating within the framework of the *Electricity Supply Act 1995*. EnergyAustralia operates retail gas and electricity businesses in NSW, Queensland and the ACT. In July 2005, the Corporation formed the EA-IPR Retail Partnership with International Power (Retail) Pty Ltd, a 50:50 joint venture to sell gas and electricity to retail customers in Victoria and South Australia. EnergyAustralia also owns and operates part of the NSW electricity transmission network.

EnergyAustralia's pre-tax operating profit increased by 42 per cent (\$87.0 million) to \$294 million in 2005-06. This was primarily driven by revenue growth of 8.7 per cent, which EnergyAustralia attributes to higher network volumes and lower cost of sales, as well as to an abnormal profit of \$53.0 million from an asset sale completed in July 2005.

The value of EnergyAustralia's assets increased by 9.3 per cent (\$557 million) to \$6.6 billion in 2005-06, attributable mainly to capital expenditure in property, plant and equipment. Total debt increased by 5.4 per cent (\$144 million) to \$2.8 billion and current liabilities grew by 12 per cent, leading to a 12 per cent (\$502 million) increase in total liabilities. The total liabilities to equity ratio increased from 259.9 per cent to 280.8 per cent. However, the higher level of debt did not reduce interest cover, which increased slightly from 2.2 times in 2004-05 to 2.6 times in 2005-06.

EnergyAustralia is required to make tax-equivalent and dividend payments. It provided for a \$205 million dividend payment in 2005-06 (up from \$81.1 million in 2004-05)¹ and recorded an income tax-equivalent expense of \$83.0 million.

The NSW Government funds EnergyAustralia for the provision of agreed community service obligations (CSOs). These include the provision of rebates to pensioners and low income households, medical rebates for people on life support systems, and the electricity payment assistance scheme. EnergyAustralia received \$29.8 million in CSO funding in 2005-06.

¹ The reduced dividend in 2004-05 was determined by the Board in accordance with EnergyAustralia's Statement of Corporate Intent 2004-05, as agreed with NSW Treasury.

ENERGYAUSTRALIA (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	6 017	6 012	6 569
Total revenue	\$m	2 836	2 582	2 806
Profitability				
Operating profit before tax	\$'000	264 500	206 500	293 500
Operating sales margin	%	15.5	14.8	16.7
Cost recovery	%	118.3	117.4	119.9
Return on assets	%	7.3	6.4	7.5
Return on equity	%	8.0	8.5	12.4
Financial management				
Debt to equity	%	117.4	159.6	162.8
Debt to total assets	%	44.3	44.3	44.6
Total liabilities to equity	%	165.1	259.9	280.8
Interest cover	times	2.5	2.2	2.6
Current ratio	%	52.9	43.0	45.5
Leverage ratio	%	265.1	359.9	380.8
Payments to and from government				
Dividends	\$'000	81 100 ^c	81 100 ^c	205 200
Dividend to equity ratio	%	3.6	4.9	12.1
Dividend payout ratio	%	44.7	57.1	97.5
Income tax expense	\$'000	83 100	64 400	83 000
CSO funding	\$'000	33 200	33 200	29 800

^a EnergyAustralia commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for EnergyAustralia. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The reduced dividend in 2004-05 was determined by the Board in accordance with EnergyAustralia's Statement of Corporate Intent 2004-05, as agreed with NSW Treasury.

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 to residential and commercial customers in New South Wales within the framework of the *Electricity Supply Act 1995* and the National Electricity Rules. It also provides metering and data services to industrial and commercial customers.

Integral's pre-tax operating profit increased by 22 per cent (\$37.0 million) to \$204 million in 2005-06. This was achieved through a 6.6 per cent (\$89.1 million) increase in revenue to \$1.4 billion, which exceeded a 4.4 per cent (\$52.1 million) rise in total expenditure. Integral attributes revenue growth to stronger energy sales, higher income from network charges and increases in the value of its superannuation assets.

Integral undertook capital expenditure of \$337 million in 2005-06, including nearly \$250 million on improving network assets. As a result, the value of property, plant and equipment grew by \$184 million from 2004-05 to 2005-06, the major contributor to a \$201 million (6.7 per cent) increase in Integral's total assets. The level of debt rose by \$185 million (15 per cent) in 2005-06, causing the debt to equity and debt to total assets ratios to increase to 156.4 per cent and 44.9 per cent respectively. The greater level of debt resulted in a 13 per cent (\$11.1 million) increase in finance costs. However, as profitability growth outweighed the rise in borrowing costs, interest cover improved slightly from 3.0 to 3.1 times in 2005-06.

Integral is required to make tax-equivalent and dividend payments to the NSW Government. Integral paid a dividend of \$104 million in 2005-06 (\$114 million in 2004-05)¹ and recorded an income tax-equivalent expense of \$65.2 million.

Integral receives funding for the provision of community service obligations relating primarily to rebates for pensioners. This funding amounted to \$20.6 million in 2005-06.

¹ According to Integral's annual report, the reduction in dividend from 2004-05 to 2005-06 resulted from a change in the distribution policy from 90 per cent of after-tax operating profit to 80 per cent, as well as adjustments related to year-end actuarial assessments.

INTEGRAL ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	3 007	2 979	3 179
Total revenue	\$m	1 370	1 354	1 443
Profitability				
Operating profit before tax	\$'000	191 403	166 821	203 801
Operating sales margin	%	20.1	18.5	20.8
Cost recovery	%	125.2	122.7	126.2
Return on assets	%	9.2	8.5	9.8
Return on equity	%	11.3	14.9	15.6
Financial management				
Debt to equity	%	106.6	134.4	156.4
Debt to total assets	%	39.8	40.2	44.9
Total liabilities to equity	%	167.8	234.5	259.9
Interest cover	times	3.2	3.0	3.1
Current ratio	%	35.4	32.2	37.1
Leverage ratio	%	267.8	334.5	359.9
Payments to and from government				
Dividends	\$'000	114 132	114 132	103 866 ^c
Dividend to equity ratio	%	10.2	12.8	11.7
Dividend payout ratio	%	90.0	86.0	74.9
Income tax expense	\$'000	64 590	34 160	65 213
CSO funding	\$'000	20 720	20 720	20 624

^a Integral Energy (Integral) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Integral. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c According to Integral's annual report, the reduction in dividend from 2004-05 to 2005-06 resulted from a change in the distribution policy from 90 per cent of after-tax operating profit to 80 per cent, as well as adjustments related to year-end actuarial assessments.

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*. On 1 July 2005, the operations of Australian Inland Energy Water Infrastructure (Australian Inland) were merged with Country Energy.

Country Energy is the largest regionally-based energy business in Australia. It holds distribution and retail licenses in NSW and Victoria (for electricity and gas) and holds retail licenses in Queensland, SA and the ACT.² Following the merger with Australian Inland, Country Energy is also listed as a water supply authority under the *Water Management Act 2000*.

Country Energy's pre-tax operating profit increased by 112 per cent (\$141 million) to \$268 million in 2005-06. Total revenue grew by 18 per cent from \$1.7 billion in 2004-05 to \$2.0 billion in 2005-06. Revenue from energy sales and developer and customer contributions accounted for most of this growth, along with an \$18.2 million reversal of a previously recognised impairment loss.

Total assets increased 17 per cent (\$549 million) to \$3.7 billion in 2005-06, following additions to property, plant and equipment totalling \$456 million as well as the receipt of \$85.3 million of assets from the merger with Australian Inland. Total liabilities increased by 14 per cent (\$362 million), leading to growth in equity of \$18.6 million. In turn, the total liabilities to equity ratio decreased from 425.8 per cent in 2004-05 to 371.3 per cent in 2005-06.

Country Energy is required to make tax-equivalent and dividend payments. It provided for a dividend payment of \$76.8 million in 2005-06 (\$18.1 million in 2004-05) and recorded an income tax-equivalent expense of \$81.7 million.

Country Energy receives community service obligation funding from governments for concessions given to pensioners, customers in caravan parks and those who rely on life support machines. This funding is not reported separately in Country Energy's accounts.

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 added to 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.

COUNTRY ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^c
Size				
Total assets	\$m	3 188	3 179	3 727 ^c
Total revenue	\$m	1 710	1 699	2 012
Profitability				
Operating profit before tax	\$'000	150 977	126 261	267 758
Operating sales margin	%	15.3	13.9	19.4
Cost recovery	%	118.0	116.2	124.1
Return on assets	%	8.2	7.5	11.5
Return on equity	%	12.1	13.0	26.7
Financial management				
Debt to equity	%	212.3	287.6	250.4
Debt to total assets	%	54.5	54.7	57.4
Total liabilities to equity	%	289.2	425.8	371.3
Interest cover	times	2.4	2.1	3.1
Current ratio	%	47.5	42.0	54.8
Leverage ratio	%	389.2	525.8	471.3
Payments to and from government				
Dividends	\$'000	18 100	18 100	76 756
Dividend to equity ratio	%	2.2	3.0	11.0
Dividend payout ratio	%	18.3	23.1	41.3
Income tax expense	\$'000	52 258	47 858	81 723
CSO funding ^d	\$'000	na	na	na

^a Country Energy commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Country Energy. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c On 1 July 2005, the operations of Australian Inland were merged with Country Energy. The merger increased the assets of Country Energy by \$85.3 million. ^d Although Country Energy receives funding from governments for concessions given to pensioners, customers in caravan parks and those who rely on life support machines, this funding is not reported separately in Country Energy's accounts. **na** Not available.

CS Energy was established on 1 July 1997 as part of the restructure of the Queensland electricity industry. It is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to the provisions of the *Government Owned Corporations Act 1993* (GOC Act). CS Energy operates power stations with a combined generating capacity of 2460 MW at three locations in Queensland. Generated electricity is sold into the National Electricity Market and is subject to the National Electricity Rules.

CS Energy's pre-tax operating profit increased by 54 per cent (\$28.4 million) to \$81.0 million in 2005-06, as total revenue growth of 13 per cent (\$62 million) exceeded growth in expenditure of 8.1 per cent (\$34 million). The major contributors to revenue growth in 2005-06 were a \$48.9 million increase in revenue from the sale of electricity, a \$13.1 million increase in revenue from operation, maintenance and services fees, and a \$6.3 million net gain on derivatives.

The value of CS Energy's assets increased by 22 per cent to \$2.1 billion in 2005-06. Capital investment in property, plant and equipment totalled \$491 million, assisted by a \$250 million equity injection by the Queensland Government in 2005-06. Total debt was \$645 million in 2005-06, an increase of 24 per cent from 2004-05. This caused the debt to total assets ratio to increase from 30.1 per cent in 2004-05 to 33.5 per cent in 2005-06.

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 GOC Act.¹ CS Energy provided for a \$40.2 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$24.5 million.

CS Energy does not receive community service obligation funding from the Queensland Government.

¹ Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers can either approve the recommendation or direct the Board to pay a specified dividend.

CS ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^c
Size				
Total assets	\$m	1 840	1 734	2 121
Total revenue	\$m	474	474	537
Profitability				
Operating profit before tax	\$'000	49 829	52 580	80 953
Operating sales margin	%	14.6	15.8	19.0
Cost recovery	%	117.1	118.7	123.5
Return on assets	%	3.8	4.4	5.3
Return on equity	%	4.2	5.4	6.5
Financial management				
Debt to equity	%	59.3	69.3	64.7
Debt to total assets	%	28.3	30.1	33.5
Total liabilities to equity	%	109.6	130.5	112.8
Interest cover	times	3.4	3.3	4.7
Current ratio	%	75.5	75.5	73.4
Leverage ratio	%	209.6	230.5	212.8
Payments to and from government				
Dividends	\$'000	29 151	29 151	40 170
Dividend to equity ratio	%	3.3	3.9	4.6
Dividend payout ratio	%	80.0	71.7	71.1
Income tax expense	\$'000	13 390	11 900	24 485
CSO funding	\$'000	..	..	..

^a CS Energy commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for CS Energy. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c In 2005-06, CS Energy received a \$250 million equity injection from the Queensland Government. .. Not applicable.

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

Stanwell operates the Stanwell coal-fired power 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 grew by 168 per cent (\$65.1 million) to \$104 million in 2005-06. However, this is largely attributable to activities unrelated to the sale of electricity. For example, total revenue increased by 14 per cent (\$51.7 million), but the sale of electricity contributed only a small proportion (\$8.0 million) to this increase. The majority of the revenue growth was attributable to the balance of an increase in coal-related revenue (\$51.5 million) and declines in other sources of revenue (\$6.5 million).¹

The value of Stanwell's assets increased by 3.5 per cent (\$57.0 million) to \$1.7 billion in 2005-06, accompanied by a 17 per cent (\$34.1 million) decrease in total debt. As a result, the debt to equity ratio decreased from 20.6 per cent in 2004-05 to 16.8 per cent in 2005-06, and the debt to total assets ratio fell to 10.3 per cent. Following from the decline in debt, borrowing costs fell by 16 per cent to \$12.4 million. When combined with the growth in profitability, this resulted in an increase in Stanwell's interest cover from 3.6 to 9.4 times. However, an increase of 125 per cent in current liabilities lowered the current ratio from 141 per cent in 2004-05 to 79.6 per cent in 2005-06.

Stanwell is required to make tax-equivalent and dividend payments. Its dividend payments are determined in accordance with the provisions of the GOC Act.² In 2005-06, Stanwell provided for a \$60.6 million dividend payment and recorded a tax-equivalent expense of \$31.0 million. Stanwell does not receive community service obligation funding from the Queensland Government.

¹ Coal-related revenue includes revenue from Stanwell's long-term coal supply contracts as well as from the on-sale of coal. Stanwell notes in its annual report that the coal supply contracts generate revenues from coal exports, as well as holding down the costs of obtaining coal during a period of rising prices.

² Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers can either approve the recommendation or direct the Board to pay a specified dividend.

STANWELL CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 653	1 636	1 693
Total revenue	\$m	372	373	425
Profitability				
Operating profit before tax	\$'000	39 126	38 733	103 842
Operating sales margin	%	14.1	14.1	27.2
Cost recovery	%	116.4	116.4	137.4
Return on assets	%	3.2	3.3	7.0
Return on equity	%	2.9	2.9	7.2
Financial management				
Debt to equity	%	20.3	20.6	16.8
Debt to total assets	%	12.5	12.6	10.3
Total liabilities to equity	%	62.7	63.6	65.0
Interest cover	times	3.7	3.6	9.4
Current ratio	%	139.1	141.0	79.6
Leverage ratio	%	162.7	163.6	165.0
Payments to and from government				
Dividends	\$'000	23 564	23 564	60 617
Dividend to equity ratio	%	2.3	2.4	6.0
Dividend payout ratio	%	80.0	80.8	83.2
Income tax expense	\$'000	9 671	9 553	30 953
CSO funding	\$'000	..	..	..

^a Stanwell Corporation (Stanwell) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Stanwell.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

Tarong Energy (Tarong) was established on 1 July 1997 as part of the restructure of the Queensland electricity industry. It is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to the provisions of the *Government Owned Corporations Act 1993* (GOC Act). Tarong generates electricity for sale into the National Electricity Market.

Tarong operates power stations (two coal-fired, one gas turbine, one hydro and one wind) with a combined generating capacity of 2395 MW. Under a joint-venture agreement with Tokyo Electric Power Company and Mitsui & Co Ltd, Tarong also owns a 50 per cent interest in the Tarong North Power Station. Tarong sold its interest in the South Australian gas supplier, Terra Gas Trader, on 12 February 2005.

Tarong's pre-tax operating profit fell by 15 per cent (\$18.1 million) to \$99.6 million in 2005-06. According to Tarong, the reduced profitability was mainly caused by expenditure on investigations into potential long-term fuel supply sources,¹ and increased operational expenditure relating to the Tarong power station.

The value of Tarong's assets remained largely unchanged at \$1.6 billion in 2005-06. Total debt increased by 6.2 per cent (\$16.0 million) to \$277 million, leading to increases in the debt to equity and debt to total assets ratios (to 33.7 per cent and 17.5 per cent respectively). Despite the growth in total debt, borrowing costs fell 37 per cent in 2005-06 to \$12.6 million. This was reflected in Tarong's interest cover of 8.9 times, up from 6.9 times in 2004-05.

Tarong is required to make tax-equivalent and dividend payments. Its dividend payment is determined in accordance with the provisions of the GOC Act.² Tarong provided for a dividend payment of \$55.5 million in 2005-06 and recorded an income tax-equivalent expense of \$30.2 million.

Tarong does not receive community service obligation funding from the Queensland Government.

¹ In its 2005-06 annual report, Tarong states that its coal supply arrangement with Rio Tinto Coal Australia is due to expire in December 2010, and that it is currently searching for alternative sources of fuel supply for the period after 2010.

² Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment, which the shareholding ministers can either approve or direct the Board to pay a specified dividend.

TARONG ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05 ^c	2004-05 ^c	2005-06
Size				
Total assets	\$m	1 614	1 563	1 593
Total revenue	\$m	505	505	441
Profitability				
Operating profit before tax	\$'000	113 700	117 617	99 565
Operating sales margin	%	25.9	26.8	25.2
Cost recovery	%	134.9	136.6	133.7
Return on assets	%	8.2	8.8	7.1
Return on equity	%	9.1	10.2	8.5
Financial management				
Debt to equity	%	29.9	32.1	33.7
Debt to total assets	%	16.1	16.7	17.5
Total liabilities to equity	%	85.0	92.9	94.0
Interest cover	times	7.0	6.9	8.9
Current ratio	%	41.2	41.2	45.7
Leverage ratio	%	185.0	192.9	194.0
Payments to and from government				
Dividends	\$'000	63 680	63 680	55 465
Dividend to equity ratio	%	7.3	7.9	6.8
Dividend payout ratio	%	80.0	77.2	80.0
Income tax expense	\$'000	34 100	35 107	30 233
CSO funding	\$'000	..	..	..

^a Tarong Energy (Tarong) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Tarong. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Tarong's revenue and expenses declined in 2004-05 following the sale of its interest in the SA gas supplier Terra Gas Trader on 12 February 2005. .. Not applicable.

The Queensland Power Trading Corporation commenced trading as Enertrade in October 2000. It is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to the provisions of the *Government Owned Corporations Act 1993*.

Enertrade's initial role was as wholesale trader of power-purchase agreements (PPAs) assigned to it as part of the industry restructure in 1997.¹ However, it has expanded its business activities to include the construction, ownership and operation of energy assets. Enertrade now owns and operates the North Queensland Gas Pipeline as well as a gas-fired power station at Barcaldine.

Since 1 July 2002, Enertrade has made provision for estimated future losses related to its legacy PPAs — originally totalling \$486 million in 2002-03. The carrying amount of the provision is revised annually to the best estimate as at the reporting date.²

Enertrade recorded a pre-tax operating loss of \$32.7 million in 2005-06, a reduction from the \$88.1 million loss posted in 2004-05. The reduced loss reflected revenue growth of 29 per cent (\$120 million), primarily from electricity production, the sale of Gas Electricity Certificates, and for the first time the North Queensland Gas Pipeline was in operation for a full year. In addition, revenue was boosted by \$13.6 million in 2005-06 through an increase in the fair value of derivative financial instruments.

The value of Enertrade's assets grew by 78 per cent (\$192 million) in 2005-06, primarily as a result of increased cash holdings. Enertrade had no outstanding debt in 2004-05 or 2005-06, and so had debt to total assets and debt to equity ratios of zero. Enertrade did not make a dividend provision in either 2004-05 or 2005-06 because of pre-tax operating losses, and recorded an income tax-equivalent credit of \$1.4 million in 2005-06. Enertrade does not receive community service obligation funding from the Queensland Government.

¹ In its annual report, Enertrade argues that a number of its long-term PPAs constitute onerous contracts and are expected to result in significant future losses. The agreements commit Enertrade to purchasing power at fixed prices over the terms of the respective agreements and selling it into the NEM at prevailing (currently lower) pool prices. The longest of these contracts is for a term of 35 years, which extends to 2029.

² The estimate depends on future changes in the market prices for electricity and the prevailing interest rates. The provision is recorded as a liability in the statement of financial position and the annual revision is recognised in expenses in the statement of financial performance.

ENERTRADE (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	262	245	438
Total revenue	\$m	497	411	532
Profitability				
Operating profit before tax	\$'000	-55 237	-88 109	-32 671
Operating sales margin	%	-11.3	-21.7	-6.4
Cost recovery	%	89.9	82.2	94.0
Return on assets	%	-19.3	-33.9	-9.3
Return on equity ^c	%	..	..	..
Financial management				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity ^d	%	..	..	835.9
Interest cover	times	-10.4	-17.0	-34.5
Current ratio	%	104.6	81.6	182.8
Leverage ratio	%	-315.4	-181.6	935.9
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	-292	-1 379
CSO funding	\$'000	..	..	..

^a Enertrade commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Enertrade. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Average total equity was negative in 2004-05 and 2005-06, because total liabilities exceeded total assets in 2004-05. This was largely attributable to provisions for onerous contracts related to power purchasing agreements. ^d Total equity was negative in 2004-05 as total liabilities exceeded total assets. This was largely attributable to provisions for onerous contracts related to power purchasing agreements. .. Not applicable. — Zero or rounded to zero.

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

Powerlink increased its pre-tax operating profit by 22 per cent (\$30.7 million) to \$170 million in 2005-06. This was driven by revenue growth of 15 per cent (\$68.3 million), primarily because of a \$59.0 million increase in grid sales revenue. Total expenditure grew by 12 per cent (\$37.7 million), including a \$13.0 million increase in expenditure on network maintenance and grid support and a \$10.3 million increase in depreciation. The greater profitability in 2005-06 in turn increased Powerlink's return on assets and return on equity to 7.6 per cent and 8.2 per cent respectively.

The value of Powerlink's total assets increased by 9.9 per cent (\$332 million) to \$3.7 billion in 2005-06. This mainly reflected capital works projects of \$347 million carried out as part of an investment in its transmission network in response to current and anticipated growth in Queensland's electricity demand. Powerlink estimated that about 48 per cent of its capital investment program in 2005-06 was funded from internally generated cash flows, with the remainder financed by new borrowings of \$176 million. In total, Powerlink's level of debt increased by \$176 million in 2005-06, a 12 per cent increase on 2004-05. This took the debt to equity ratio to 109.1 per cent, up from 104.9 per cent in 2004-05.

Under the provisions of the GOC Act, Powerlink is required to make tax-equivalent and dividend payments.¹ Powerlink provided for an \$95.2 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$51.5 million.

Powerlink does not receive community service obligation funding from the Queensland Government.

¹ Under the Act, the Board makes a recommendation to the shareholding ministers on its proposed dividend payment. Shareholding ministers can either approve the recommendation or direct the Board to pay a specified dividend.

POWERLINK (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	3 370	3 352	3 685
Total revenue	\$m	466	461	529
Profitability				
Operating profit before tax	\$'000	147 149	139 781	170 462
Operating sales margin	%	48.6	48.4	49.3
Cost recovery	%	194.6	193.8	197.2
Return on assets	%	7.0	6.9	7.6
Return on equity	%	6.6	6.9	8.2
Financial management				
Debt to equity	%	93.7	104.9	109.1
Debt to total assets	%	43.6	43.8	46.8
Total liabilities to equity	%	115.0	139.4	144.2
Interest cover	times	2.7	2.6	2.8
Current ratio	%	75.2	75.3	73.4
Leverage ratio	%	215.0	239.4	244.2
Payments to and from government				
Dividends	\$'000	82 649	82 649	95 167
Dividend to equity ratio	%	5.3	5.9	6.5
Dividend payout ratio	%	80.0	85.2	80.0
Income tax expense	\$'000	43 837	42 756	51 503
CSO funding	\$'000	..	..	..

^a Powerlink commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Powerlink. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

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

The retail arm of Ergon acquired the Victorian-based energy retailer Australian Energy Pty Ltd (Australian Energy) — trading as Powerdirect — on 24 April 2006, by purchasing 100 per cent of its shares.

Ergon recorded a pre-tax operating profit of \$213 million in 2005-06, an increase of 50 per cent (\$71.1 million) on 2004-05. This increase in profitability occurred as revenue growth of \$162 million (7.8 per cent) exceeded a \$90.8 million (4.7 per cent) increase in total expenditure. The growth in revenue mainly resulted from an increase of \$150 million in community service obligation (CSO) funding, as well as the addition of \$38.7 million in gains on revaluation of financial instruments.

The value of Ergon's assets increased by 18 per cent (\$1.0 billion) to \$6.7 billion in 2005-06. The increase was primarily due to additions to property, plant and equipment totalling \$1.2 billion, as well as an increase in current financial assets of \$332 million. (The acquisition of Australian Energy increased Ergon's net assets by \$102 million, comprising \$22.5 million in identifiable net assets and \$79.8 million in goodwill.)

Ergon reported capital investment of over \$700 million in 2005-06. According to Ergon, this was part of a \$3.2 billion capital investment plan for the five-year period to June 2010 aimed at improving network reliability. Total debt increased by 22 per cent (\$384 million) to \$2.2 billion in 2005-06.

Ergon is required to make tax-equivalent and dividend payments. Ergon provided for a dividend of \$87.5 million in 2005-06 and recorded an income tax-equivalent expense of \$68.8 million.

Ergon receives CSO payments to cover any shortfall incurred in supplying electricity to non-contestable customers at gazetted tariffs. CSO payments amounted to \$327 million in 2005-06.

¹ The Queensland Government announced in April 2006 its intention to sell Ergon's retail operations. The sale was completed in February 2007.

ERGON ENERGY GROUP (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^c
Size				
Total assets	\$m	5 642	5 625	6 652
Total revenue	\$m	2 087	2 085	2 247
Profitability				
Operating profit before tax	\$'000	147 335	141 890	212 999
Operating sales margin	%	11.5	11.3	14.9
Cost recovery	%	113.0	112.7	117.5
Return on assets	%	4.4	4.3	5.6
Return on equity	%	4.3	4.2	5.8
Financial management				
Debt to equity	%	74.3	74.6	83.3
Debt to total assets	%	31.4	31.5	35.1
Total liabilities to equity	%	136.5	136.8	157.1
Interest cover	times	2.5	2.4	2.6
Current ratio	%	152.2	146.9	129.8
Leverage ratio	%	236.5	236.8	257.1
Payments to and from government				
Dividends	\$'000	82 111	82 111	87 482
Dividend to equity ratio	%	3.4	3.5	3.5
Dividend payout ratio	%	80.0	83.1	60.7
Income tax expense	\$'000	44 696	43 049	68 847
CSO funding	\$'000	176 872	176 872	326 717

^a The Ergon Energy Group (Ergon) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Ergon.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The retail arm of Ergon, Ergon Energy Pty Ltd, acquired the Victorian-based energy retailer Australian Energy Pty Ltd (Australian Energy), trading as Powerdirect, on 24 April 2006 by purchasing 100 per cent of its shares.

ENERGEX was formed on 1 July 1997 following incorporation of the South–East Queensland Electricity Corporation and its wholly-owned subsidiary, Southern Electricity Retail Corporation. ENERGEX operates subject to the provisions of the *Government Owned Corporations Act 1993*.

ENERGEX distributes and retails electricity and gas in Queensland via two wholly-owned subsidiary companies, ENERGEX Retail — which changed its name to Sun Retail on 10 May 2006 — and Allgas Energy.¹

Operating profit (before tax) was relatively unchanged at \$236 million in 2005-06. A \$157 million (6.6 per cent) increase in total revenue offset a \$155 million (7.2 per cent) increase in total expenditure. According to ENERGEX, revenue growth was adversely affected by the Queensland Competition Authority's five-year regulatory determination commencing in 2005-06, which made a downward adjustment to ENERGEX's revenue cap for underspending in the previous determination. ENERGEX estimated that this had a \$24.0 million negative impact on its revenue in 2005-06. Growth in total expenditure was mainly driven by increases in employee benefits and depreciation of \$36.5 million and \$45.6 million respectively as well as a \$27.6 million rise in cost of sales.

Total assets grew by 18 per cent (\$1.0 billion) to \$6.6 billion in 2005-06, mainly because of additions to property, plant and equipment of \$777 million and a revaluation increment of \$150 million. ENERGEX reported system capital works of \$619 million in 2005-06, aimed at improving network security and reliability. Debt increased by 27 per cent (\$580 million) in 2005-06, causing the debt to equity ratio to increase from 115.8 per cent in 2004-05 to 134.1 per cent in 2005-06. However, current assets grew much faster than current liabilities — 79 per cent compared with 5.4 per cent — increasing the current ratio from 140.0 per cent to 237.4 per cent.

ENERGEX is required to make dividend and tax-equivalent payments. It provided for a \$123 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$72.9 million.

ENERGEX receives community service obligation (CSO) funding to cover any financial shortfall incurred in supplying electricity to its non-contestable customers at gazetted tariffs, as well as for the payment and administration of pensioner rebates. CSO funding amounted to \$35.9 million in 2005-06.

¹ The Queensland Government announced in April 2006 its intention to sell ENERGEX's retail operations. The sale was completed in February 2007.

ENERGEX (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	5 617	5 626	6 624
Total revenue	\$m	2 356	2 390	2 547
Profitability				
Operating profit before tax	\$'000	226 100	233 900	236 300
Operating sales margin	%	14.6	14.7	14.2
Cost recovery	%	117.1	117.3	116.5
Return on assets	%	6.1	6.3	6.0
Return on equity	%	6.2	8.7	8.3
Financial management				
Debt to equity	%	95.3	115.8	134.1
Debt to total assets	%	39.9	38.8	45.1
Total liabilities to equity	%	139.2	198.4	221.5
Interest cover	times	2.9	3.0	2.8
Current ratio	%	144.1	140.0	237.4
Leverage ratio	%	239.2	298.4	321.5
Payments to and from government				
Dividends	\$'000	115 600	115 600	122 600
Dividend to equity ratio	%	4.9	6.1	6.2
Dividend payout ratio	%	80.0	70.8	75.0
Income tax expense	\$'000	81 600	70 600	72 900
CSO funding	\$'000	34 700	34 700	35 900

^a ENERGEX commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for ENERGEX. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

Verve Energy was established on 1 April 2006 following the vertical disaggregation of the former Western Power Corporation into four independent corporations — Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). This disaggregation formed part of the WA Government's reform of the electricity industry. Verve Energy is subject to the *Electricity Corporation Act 1994*.

Verve Energy owns and operates power stations in the network known as the South West Interconnected System with a total capacity of 3480 MW. The WA Government has imposed a 3000 MW ceiling on Verve Energy's generation capacity to encourage competition in electricity generation. Verve Energy plans to achieve this limit by retiring old generation assets over the three years from 2006.

Financial data on Verve Energy's 2005-06 performance are available only for the period 1 April 2006 to 30 June 2006.

Verve Energy recorded a pre-tax operating loss of \$16.5 million for the three months to 30 June 2006. It attributed this to limited gas availability forcing the use of higher-priced liquid fuels. Fuel and electricity purchases comprised 58 per cent of Verve Energy's total expenditure of \$275 million in the three months to 30 June 2006.

The value of Verve Energy's assets was just under \$2.2 billion at the end of 2005-06. The generator also reported total debt of \$985 million, giving a debt to assets ratio of 45.7 per cent. Current liabilities of \$319 million exceeded current assets of \$242 million, leading to a current ratio of 75.9 per cent. This suggests that Verve Energy's short-term assets would not have covered its short-term debts, if they had fallen due.

Verve Energy is required to make dividend and income tax-equivalent payments to the WA Government. It made no dividend provision for the three months to 30 June 2006. As it reported an operating loss for this period, it received a tax-equivalent benefit of \$4.5 million.

Verve Energy does not receive community service obligation funding from the WA Government.

VERVE ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^a		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^b
<i>Size</i>				
Total assets	\$m	..	..	2 156
Total revenue	\$m	..	..	258
<i>Profitability</i>				
Operating profit before tax	\$'000	..	..	-16 465
Operating sales margin	%	..	..	1.2
Cost recovery	%	..	..	100.0
Return on assets	%	..	..	0.2 ^c
Return on equity	%	..	..	-1.9
<i>Financial management</i>				
Debt to equity	%	..	..	160.1
Debt to total assets	%	..	..	45.7
Total liabilities to equity	%	..	..	250.5
Interest cover	times	..	..	0.2
Current ratio	%	..	..	75.9
Leverage ratio	%	..	..	350.5
<i>Payments to and from government</i>				
Dividends	\$'000	..	..	—
Dividend to equity ratio	%	..	..	—
Dividend payout ratio	%	..	..	—
Income tax expense	\$'000	..	..	-4 546
CSO funding	\$'000	..	..	..

^a Verve Energy was established on 1 April 2006 following the vertical disaggregation of the former Western Power into four independent corporations: Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). Pre-AIFRS data for Western Power up to 2004-05 are available in previous *Financial Performance of Government Trading Enterprise* reports. ^b Data for 2005-06 are for the period 1 April 2006 to 30 June 2006. ^c Although Verve Energy recorded a pre-tax operating loss in the three months to 30 June 2006, it achieved a positive earnings before interest and tax, and so return on assets is positive. .. Not applicable. — Zero or rounded to zero.

WESTERN POWER

Western Australia

Western Power was established on 1 April 2006 following the vertical disaggregation of the former Western Power Corporation into four independent corporations —Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). This disaggregation formed part of the WA Government's reform of the electricity industry. Western Power is subject to the *Electricity Corporation Act 1994*.

Western Power transports and distributes electricity in Western Australia, via the power network known as the South West Interconnected System. It is responsible for maintaining the network and providing access services to generators, retailers and other users.

Financial data on Western Power's 2005-06 performance are available only for the period 1 April 2006 to 30 June 2006.

Western Power recorded a pre-tax operating profit of \$24.3 million for the three months to 30 June 2006. Total revenue was \$185 million, which included \$39.5 million in developer and customer contributions.

Western Power had total assets of \$3.3 billion at the end of 2005-06 and \$2.2 billion in debt, leaving it with net equity of \$809 million. Western Power's debt to equity ratio was 266 per cent, indicating that it is relatively highly geared. Western Power's debt level was also reflected in borrowing costs of \$30.4 million in the three months to 30 June 2006 — representing 19 per cent of total expenditure in this period — and its interest cover of 1.8 times.

Western Power is required to make dividend and income tax-equivalent payments to the WA Government. It recorded a tax-equivalent expense of \$7.3 million in the three months to 30 June 2006 and made no dividend payments in this period.

Western Power does not receive community service obligation funding from the WA Government.

WESTERN POWER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^a		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^b
<i>Size</i>				
Total assets	\$m	..	..	3 310
Total revenue	\$m	..	..	185
<i>Profitability</i>				
Operating profit before tax	\$'000	..	..	24 339
Operating sales margin	%	..	..	29.6
Cost recovery	%	..	..	142.0
Return on assets	%	..	..	1.7
Return on equity	%	..	..	2.1
<i>Financial management</i>				
Debt to equity	%	..	..	266.0
Debt to total assets	%	..	..	65.0
Total liabilities to equity	%	..	..	309.4
Interest cover	times	..	..	1.8
Current ratio	%	..	..	84.2
Leverage ratio	%	..	..	409.4
<i>Payments to and from government</i>				
Dividends	\$'000	..	..	—
Dividend to equity ratio	%	..	..	—
Dividend payout ratio	%	..	..	—
Income tax expense	\$'000	..	..	7 272
CSO funding	\$'000	..	..	..

^a Western Power was established on 1 April 2006 following the vertical disaggregation of the former Western Power into four independent corporations: Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). Pre-AIFRS data for the former Western Power up to 2004-05 are available in previous *Financial Performance of Government Trading Enterprise* reports. ^b Data for 2005-06 are for the period 1 April 2006 to 30 June 2006. .. Not applicable. — Zero or rounded to zero.

Synergy was established on 1 April 2006 following the vertical disaggregation of the former Western Power Corporation into four independent corporations — Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). This disaggregation formed part of the WA Government's reform of the electricity industry. Synergy is subject to the *Electricity Corporation Act 1994*.

Synergy is an energy retailer operating in the South West Interconnected System power network in Western Australia. Synergy currently purchases its wholesale electricity supply from Verve Energy under a transitional contract intended to cover the initial period after disaggregation. However, the WA Government requires Synergy to gradually source less of its electricity from Verve Energy to encourage competition in the wholesale supply market. In August 2006, Synergy announced a tender process seeking new wholesale electricity supply contracts, to become available from 2010.

Financial data on Synergy's 2005-06 performance are available only for the period 1 April 2006 to 30 June 2006.

Synergy recorded a pre-tax operating profit of \$19.6 million for the three months to 30 June 2006. Total revenue was \$371 million for this period, with total expenditure of \$352 million. A large part (\$218 million) of total expenditure was attributable to energy purchases. Further, network access costs of \$113 million comprised 32 per cent of Synergy's expenses.

Synergy had total assets valued at \$342 million at the end of 2005-06. The retailer reported no debt at this date, and consequently had finance costs of only \$191 000 in the three months to 30 June 2006. These costs related to short-term liabilities, which comprised 97 per cent of Synergy's total liabilities. However, Synergy's current assets, valued at \$331 million, exceeded its current liabilities of \$196 million, as reflected in a current ratio of 168.8 per cent.

Synergy is required to make dividend and income tax-equivalent payments to the WA Government. Synergy made dividend payments of \$6.9 million for the three months to 30 June 2006 and recorded a tax-equivalent expense of \$5.9 million.

Synergy did not receive community service obligation payments from the WA Government in the three months to 30 June 2006.

SYNERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^a		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^b
<i>Size</i>				
Total assets	\$m	..	..	342
Total revenue	\$m	..	..	371
<i>Profitability</i>				
Operating profit before tax	\$'000	..	..	19 592
Operating sales margin	%	..	..	5.0
Cost recovery	%	..	..	105.3
Return on assets	%	..	..	5.8
Return on equity	%	..	..	9.8
<i>Financial management</i>				
Debt to equity	%	..	..	—
Debt to total assets	%	..	..	—
Total liabilities to equity	%	..	..	144.7
Interest cover	times	..	..	103.6
Current ratio	%	..	..	168.8
Leverage ratio	%	..	..	244.7
<i>Payments to and from government</i>				
Dividends	\$'000	..	..	6 856
Dividend to equity ratio	%	..	..	4.9
Dividend payout ratio	%	..	..	50.0
Income tax expense	\$'000	..	..	5 881
CSO funding	\$'000	..	..	..

^a Synergy was established on 1 April 2006 following the vertical disaggregation of the former Western Power into four independent corporations: Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). Pre-AIFRS data for Western Power up to 2004-05 are available in previous *Financial Performance of Government Trading Enterprise* reports. ^b Data for 2005-06 are for the period 1 April 2006 to 30 June 2006. .. Not applicable. — Zero or rounded to zero.

HORIZON POWER

Western Australia

Horizon Power was established on 1 April 2006 following the vertical disaggregation of the former Western Power Corporation into four independent corporations — Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). Horizon Power operates under the *Electricity Corporation Act 1994*.

Horizon Power is an integrated electricity corporation involved in the generation, distribution and retailing of electricity to regional and remote areas of Western Australia. The retail arm can also purchase electricity for sale to these areas. Horizon Power services the Pilbara North West Interconnected System as well as non-interconnected systems in 27 townships in Western Australia.

Financial data on Horizon Power's 2005-06 performance are available only for the period 1 April 2006 to 30 June 2006.

Horizon Power recorded a pre-tax operating loss of \$17.3 million in the three months to 30 June 2006. Total revenue for this period was \$32.4 million, which included \$22.4 million in revenue from electricity sales and \$2.8 million in developer and customer contributions. Total expenditure was \$49.7 million, including \$17.5 million in fuel purchases and \$9.2 million in electricity purchases, as well as \$3.9 million in borrowing costs.

Horizon Power recorded total assets of \$342 million and total debt of \$201 million at the end of 2005-06, leading to a debt to total assets ratio of 58.9 per cent. Horizon Power's current liabilities, at \$71.7 million, were nearly three times as large as its current assets of \$26.0 million, as reflected in a current ratio of 36.3 per cent.

Horizon Power is required to make dividend and income tax-equivalent payments to the WA Government. No dividend provision was made for the three months to 30 June 2006. As Horizon Power reported an operating loss for this period, it received a tax-equivalent benefit of \$5.3 million.

Horizon Power receives community service obligation funding for state and regional development projects. It received \$3.2 million in CSO funding in the three months to 30 June 2006.

HORIZON POWER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^a		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^b
<i>Size</i>				
Total assets	\$m	..	..	342
Total revenue	\$m	..	..	32
<i>Profitability</i>				
Operating profit before tax	\$'000	..	..	-17 339
Operating sales margin	%	..	..	-42.7
Cost recovery	%	..	..	70.1
Return on assets	%	..	..	-3.9
Return on equity	%	..	..	-12.0
<i>Financial management</i>				
Debt to equity	%	..	..	200.5
Debt to total assets	%	..	..	58.9
Total liabilities to equity	%	..	..	240.5
Interest cover	times	..	..	-3.5
Current ratio	%	..	..	36.3
Leverage ratio	%	..	..	340.5
<i>Payments to and from government</i>				
Dividends	\$'000	..	..	—
Dividend to equity ratio	%	..	..	—
Dividend payout ratio	%	..	..	—
Income tax expense	\$'000	..	..	-5 260
CSO funding	\$'000	..	..	3 205

^a Horizon Power was established on 1 April 2006 following the vertical disaggregation of the former Western Power into four independent corporations: Verve Energy (generation), Western Power (distribution and transmission), Synergy (retail) and Horizon Power (integrated regional provider). Data for Western Power up to 2004-05 are available in previous *Financial Performance of Government Trading Enterprise* reports. ^b Data for 2005-06 are for the period 1 April 2006 to 30 June 2006. .. Not applicable. — Zero or rounded to zero.

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*. The HEC provides electricity generation to mainland Tasmania and generation, distribution and retailing to the Bass Strait Islands. The HEC entered the National Electricity Market on 29 May 2005, and commenced trading into the national grid after the Basslink power interconnector between Tasmania and mainland Australia began operating on 29 April 2006.

The HEC's pre-tax operating profit in 2005-06 was \$67.1 million, a substantial improvement on the 2004-05 operating loss of \$498 million. However, both results were affected by impairment expenses related to the Bell Bay Power Station, of \$542 million in 2004-05 and \$23.2 million in 2005-06.¹ In addition, the 2005-06 result included an actuarial gain on superannuation benefits of \$27.3 million, while the 2004-05 result included an actuarial loss of \$34.6 million. If these amounts were excluded from the operating results, the HEC would have recorded an operating profit of \$63.0 million in 2005-06 and a loss of \$9.4 million in 2004-05.

Total revenue grew by 8.1 per cent (\$37.5 million) to \$499 million in 2005-06. This was largely attributable, however, to a \$35.0 million gain on revaluation of the HEC's investment in its joint venture with CLP Power Asia.

The HEC's total assets grew by 24 per cent (\$746 million) to nearly \$3.9 billion in 2005-06. This was mainly attributable to an \$899 million increase in assets associated with Basslink in the balance sheet,² partially offset by a \$115 million reduction in the value of current financial investments. Total debt fell by 11 per cent (\$135 million) to \$1.1 billion in 2005-06.

The HEC paid a \$40.0 million dividend in 2005-06, including an \$8.0 million special dividend, taking the dividend payout ratio to 90.4 per cent. It recorded a tax-equivalent expense of \$22.8 million. The HEC receives community service obligation funding for providing concessional arrangements to customers living on the Bass Strait Islands. It received \$6.2 million in 2005-06.

¹ The HEC 2005-06 annual report states that the Bell Bay Power Station was no longer required as a backup for the hydro generating system following the commissioning of Basslink.

² This included \$151 million in financial assets (representing the fair value of the contractual rights under the Basslink Services Agreement), and \$748 million in property, plant and equipment. The recognition of Basslink in the balance sheet also involved a corresponding increase in total liabilities of \$899 million, representing the HEC's contractual commitments associated with Basslink. The recognition of Basslink in the balance sheet had no net effect on the HEC's equity.

HYDRO-ELECTRIC CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	3 248	3 105	3 851
Total revenue	\$m	461	462	499
Profitability				
Operating profit before tax	\$'000	80 396	-498 321 ^c	67 093
Operating sales margin	%	32.4	-90.2	31.0
Cost recovery	%	148.0	52.6	144.8
Return on assets	%	4.7	-13.2	4.4
Return on equity	%	2.9	-37.0	4.8
Financial management				
Debt to equity	%	78.8	128.7	118.7
Debt to total assets	%	37.3	39.0	31.0
Total liabilities to equity	%	111.3	229.8	324.4
Interest cover	times	2.1	-4.6	1.8
Current ratio	%	133.6	137.7	51.7
Leverage ratio	%	211.3	329.8	424.4
Payments to and from government				
Dividends ^d	\$'000	40 000	40 000	40 000
Dividend to equity ratio	%	2.6	4.2	4.3
Dividend payout ratio	%	90.1	-11.5	90.4
Income tax expense	\$'000	35 986	-149 908	22 824
CSO funding	\$'000	6 030	6 030	6 200

^a The Hydro-Electric Corporation (HEC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the HEC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The 2004-05 pre-tax operating loss reflected a \$540 million impairment expense related to the Bell Bay Power Station. The HEC judged this asset to be no longer required as a backup for the hydro generating system following commissioning of Basslink. ^d The 2004-05 dividend of \$40.0 million includes a special dividend of \$17.4 million. The 2005-06 dividend of \$40.0 million includes a special dividend of \$8.0 million.

Aurora Energy (Aurora) was established on 1 July 1998, following the disaggregation of the former Hydro-Electric Corporation. Aurora is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to the provisions of the *Electricity Companies Act 1997*.

Aurora is mainland Tasmania's only electricity distribution and retail company.¹ It also holds electricity retail licences in NSW and Victoria. Aurora commenced trading in the National Electricity Market on 29 May 2005 after the Basslink power interconnector between Tasmania and mainland Australia began operating.

Aurora recorded a pre-tax operating profit of \$32.1 million in 2005-06, a decline of 24 per cent (\$10.2 million) from 2004-05. In its 2005-06 annual report, Aurora attributes the lower profitability to weather events that increased fault costs, higher system controller charges, and higher depreciation as a result of increased capital expenditure. Capital expenditure amounted to \$134 million in 2005-06 and was partly funded by increased borrowings, with total debt increasing by 5.6 per cent to \$461 million.

The value of Aurora's assets remained steady at \$1.1 billion in 2005-06. Current assets fell by 30 per cent (\$60.8 million), largely because of a reduction in cash investments (used to reduce long-term debt) and market traded receivables. At the same time, current liabilities increased by 23 per cent (\$39.9 million), mostly because of an increase in short-term borrowings. Aurora's current ratio consequently declined from 119.6 per cent in 2004-05 to 68.4 per cent in 2005-06. This indicates that Aurora's short-term assets would not have been sufficient to cover its short-term debts, if they had fallen due.

Aurora is required to make dividend and tax-equivalent payments to the Tasmanian Government. It distributed dividends of \$12.0 million in 2005-06 and recorded an income tax-equivalent expense of \$9.7 million.

Aurora receives community service obligation payments for providing pensioners with discounted electricity. These payments amounted to \$11.2 million in 2005-06.

¹ The Hydro-Electric Corporation provides electricity distribution and retailing to the Bass Strait Islands (King and Flinders Islands).

AURORA ENERGY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 072	1 078	1 107
Total revenue	\$m	715	715	739
Profitability				
Operating profit before tax	\$'000	49 406	42 273	32 076
Operating sales margin	%	10.2	9.2	7.8
Cost recovery	%	111.4	110.2	108.5
Return on assets	%	7.1	6.4	5.5
Return on equity	%	7.5	9.4	6.9
Financial management				
Debt to equity	%	108.1	140.2	138.5
Debt to total assets	%	40.7	40.5	42.2
Total liabilities to equity	%	165.2	246.0	232.1
Interest cover	times	2.8	2.6	2.1
Current ratio	%	128.9	119.6	68.4
Leverage ratio	%	265.2	346.0	332.1
Payments to and from government				
Dividends	\$'000	13 942	13 942	11 977
Dividend to equity ratio	%	3.4	4.5	3.7
Dividend payout ratio	%	46.2	47.4	53.6
Income tax expense	\$'000	19 225	12 857	9 734
CSO funding	\$'000	11 513	11 513	11 198

^a Aurora Energy (Aurora) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Aurora. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

Transend Networks (Transend) was established on 1 July 1998, following the disaggregation of the Hydro-Electric Corporation. Transend is incorporated under the *Corporations Act 2001* (Cwlth) and operates subject to the provisions of 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 nine switching stations. Following commencement of the National Electricity Market in Tasmania on 29 May 2005, Transend handed over its responsibilities for the security of the system to the National Electricity Market Management Company Limited.

Transend recorded a pre-tax operating profit of \$53.6 million in 2005-06, an increase of 44 per cent (\$16.5 million) from 2004-05. The increased profitability reflected revenue growth of 9.1 per cent (\$10.9 million), which was partly the result of \$10.0 million of revenue recognised from gifted assets associated with the Basslink project. If the gifted assets were excluded from Transend's operating balance, it would have recorded an operating profit of \$43.6 million, an increase of 17 per cent on 2004-05.

Transend reported capital expenditure on projects to upgrade and modernise its transmission system of \$97.3 million in 2005-06. Accordingly, the value of Transend's assets rose by 13 per cent (\$89.8 million) to \$782 million in 2005-06. Total debt grew by 75 per cent (\$39.9 million) to \$92.8 million, which Transend attributes to increased borrowings to fund its capital investment program. The higher debt level increased Transend's debt to equity ratio from 10.7 per cent in 2004-05 to 17.6 per cent in 2005-06. In its annual report, Transend states that its capital structure will continue to change in this way as the capital works program continues over the next few years.

Transend is required to make dividend and tax-equivalent payments to the Tasmanian Government. Transend distributed dividends of \$13.8 million in 2005-06 and recorded an income tax-equivalent expense of \$16.1 million.

Transend does not receive community service obligation funding from the Tasmanian Government.

TRANSEND NETWORKS (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	698	692	782
Total revenue	\$m	119	119	130
<i>Profitability</i>				
Operating profit before tax	\$'000	43 366	37 133	53 647
Operating sales margin	%	38.3	33.2	44.4
Cost recovery	%	162.1	149.6	179.9
Return on assets	%	6.6	5.7	7.8
Return on equity	%	4.8	5.3	7.3
<i>Financial management</i>				
Debt to equity	%	9.2	10.7	17.6
Debt to total assets	%	7.6	7.6	12.6
Total liabilities to equity	%	22.0	40.1	48.0
Interest cover	times	18.7	16.2	13.9
Current ratio	%	26.6	25.3	27.2
Leverage ratio	%	122.0	140.1	148.0
<i>Payments to and from government</i>				
Dividends	\$'000	9 924	9 924	13 766
Dividend to equity ratio	%	1.7	2.0	2.7
Dividend payout ratio	%	36.0	38.2	36.7
Income tax expense	\$'000	15 833	11 164	16 099
CSO funding	\$'000	..	..	..

^a Transend Networks (Transend) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Transend. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

The Power and Water Corporation (PWC) was established on 1 July 2002, following the corporatisation of the Power and Water Authority. PWC operates under the *Government Owned Corporations Act 2001* (GOC Act).

The PWC generates, transmits, distributes and retails electricity throughout the NT. It owns and operates three separate grid systems and purchases gas supplies for electricity generation through its subsidiary, Gasgo Pty Ltd. Under an agreement with the NT Government, PWC also provides electricity, water and sewerage services to remote areas in the NT through its subsidiary, Darnor Pty Ltd.

The PWC's pre-tax operating profit fell by 43 per cent (\$21.5 million) to \$29.1 million in 2005-06, as expenditure growth of 6.6 per cent (\$29.1 million) exceeded revenue growth of 1.6 per cent (\$7.6 million). In its annual report, PWC attributed the increase in expenditure to higher distillate prices (following from higher world oil prices), increased usage of distillate in production due to gas supply problems, and higher priced gas contracts.

The value of the PWC's assets was \$1.3 billion in 2005-06, an increase of 5.8 per cent (\$69.2 million) from 2004-05.¹ This was mainly because of a \$52.1 million increase in cash holdings, which was also reflected in growth of 49 per cent (\$44.7 million) in current assets. The rise in current assets outweighed a 14 per cent increase in current liabilities, leading to an increase in the current ratio from 72.4 per cent in 2004-05 to 95.1 per cent in 2005-06.

Under the GOC Act, the PWC is required to make dividend and tax-equivalent payments to the NT Government. PWC provided for a \$10.2 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$8.5 million.

The PWC receives community service obligation (CSO) payments from the NT Government for pensioner concessions, uniform tariffs and the Tranche Four electricity reforms.² It received \$53.7 million in CSO payments in 2005-06.

¹ The Auditor-General issued a qualified audit opinion in relation to PWC's 2005-06 annual report. It stated that the PWC should have recognised a \$38.0 million impairment loss on its water system assets, which would have reduced the value of its assets by this amount and also created an impairment expense in the income statement. The PWC states that the figures in its 2005-06 annual report are correct.

² Tranche Four reforms relate to the introduction of retail contestability in the NT. More information about NT Government regulation in this sector is provided at the start of this chapter.

POWER AND WATER CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^c
Size				
Total assets	\$m	1 057	1 192	1 261
Total revenue	\$m	508	490	498
Profitability				
Operating profit before tax	\$'000	52 033	50 602	29 059
Operating sales margin	%	14.8	15.0	10.6
Cost recovery	%	117.3	105.9	100.2
Return on assets	%	7.2	6.3	4.4
Return on equity	%	5.8	5.8	3.3
Financial management				
Debt to equity	%	45.2	47.9	52.8
Debt to total assets	%	27.8	24.6	26.9
Total liabilities to equity	%	62.8	94.4	102.3
Interest cover	times	3.1	3.1	2.2
Current ratio	%	69.5	72.4	95.1
Leverage ratio	%	162.8	194.4	202.3
Payments to and from government				
Dividends	\$'000	18 900	18 900	10 249
Dividend to equity ratio	%	2.9	3.1	1.7
Dividend payout ratio	%	49.9	53.0	50.0
Income tax expense	\$'000	14 164	14 950	8 541
CSO funding	\$'000	52 039	52 039	53 718

^a The Power and Water Corporation (PWC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PWC. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The Auditor-General issued a qualified audit opinion in relation to PWC's 2005-06 annual report. It stated that the corporation should have recognised a \$38.0 million impairment loss on its water system assets, which would have reduced the value of its assets by this amount and also created an impairment expense in the income statement. The PWC claims that the figures in its 2005-06 annual report are correct.

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

Snowy Hydro owns and manages the Snowy Mountains Hydro-Electric Scheme, which consists of seven power stations and 16 dams mainly in the Kosciuszko National Park.

Snowy Hydro generates electricity for sale into the National Electricity Market. In 2005-06, it generated 5343 GWh of electricity. In 2005-06, Snowy Hydro acquired 100 per cent of Valley Power, a gas-fired generator operating in Victoria.

Snowy Hydro's pre-tax operating profit declined by 2.5 per cent (\$5.0 million) in 2005-06 to \$195 million. This followed from a 45 per cent (\$103 million) increase in total expenditure just outweighing a 23 per cent (\$97.8 million) increase in total revenue. Increases in expenses associated with electricity sales (\$39.4 million) and a reduction in the fair value of electricity derivatives (\$19.6 million) were the main factors contributing to higher total expenditure. The small decrease in Snowy Hydro's profitability was reflected in lower return on assets and return on equity ratios of 10.8 per cent and 10.2 per cent respectively.

The value of Snowy Hydro's assets grew by 7.2 per cent (\$153 million) to nearly \$2.3 billion in 2005-06. This was mainly because of the acquisition of Valley Power, which increased its assets by \$243 million (including \$72.0 million in goodwill). This increase in assets was partially offset by an \$83.5 million reduction in receivables.

Snowy Hydro is required to make dividend and income tax payments. In 2005-06, Snowy Hydro distributed dividends of \$70.0 million and recorded an income tax expense of \$65.9 million. Snowy Hydro does not receive community service obligation funding from its owner-governments.

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 SMHEA.

² Shareholdings in Snowy Hydro are the Australian (13 per cent), NSW (58 per cent) and Victorian (29 per cent) Governments.

SNOWY HYDRO (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 891	2 124	2 277 ^c
Total revenue	\$m	425	427	525
Profitability				
Operating profit before tax	\$'000	198 637	200 040	195 071
Operating sales margin	%	55.0	55.1	45.3
Cost recovery	%	222.3	222.8	182.9
Return on assets	%	12.4	11.1	10.8
Return on equity	%	14.7	11.3	10.2
Financial management				
Debt to equity	%	61.3	49.6	66.6
Debt to total assets	%	32.6	29.0	39.2
Total liabilities to equity	%	88.3	70.9	75.6
Interest cover	times	6.6	6.7	5.5
Current ratio	%	60.1	58.3	40.3
Leverage ratio	%	188.3	170.9	175.6
Payments to and from government				
Dividends	\$'000	110 000	110 000	70 000
Dividend to equity ratio	%	11.0	8.8	5.5
Dividend payout ratio	%	74.6	78.4	54.2
Income tax expense	\$'000	51 116	59 675	65 870
CSO funding	\$'000	..	..	..

^a Snowy Hydro commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Snowy Hydro. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c In 2005-06, Snowy Hydro acquired 100 per cent of Valley Power, a gas-fired generator operating in Victoria. The acquisition increased Snowy Hydro's assets by \$243 million, including \$72 million in goodwill. .. Not applicable.

6 Water

The financial performances of 23 water sector government trading enterprises (GTEs) are reported in this chapter. These GTEs generated around \$6.7 billion in revenue and controlled assets valued at \$49.0 billion in 2005-06.

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 defined in chapter 1.

When making comparisons, consideration should be given to: differences in the nature and scale of the businesses; their individual market environments; a number of issues relating to the valuation of their assets; and the level of payments for community service obligations. Care should also be exercised when comparing data presented in this chapter with that presented in previous reports for two reasons.

1. The performance data presented in this report are based, for the first time, on the new Australian-equivalent International Financial Reporting Standards.
2. Data from GTE general purpose financial reports have been used for this report, whereas data presented in previous reports were based on government financial statistics. The reason for this change is set out in chapter 1.

6.1 Monitored GTEs

The monitored water sector 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 nature of their activities and services also vary by whether they operate in major urban, regional or rural areas.

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

Table 6.1 Activities — water GTEs, 2005-06

Water GTE	Activity				
	Catchment management	Bulk water	Reticulation	Wastewater treatment	Irrigation supply ^a
<i>New South Wales</i>					
Sydney Catchment Authority	✓	✓	x	x	x
Sydney Water	x	x	✓	✓	x
Hunter Water	✓	✓	✓	✓	x
<i>Victoria</i>					
Melbourne Water	✓	✓	✓	✓	✓
City West Water	x	x	✓	x	x
South East Water	x	x	✓	x	x
Yarra Valley Water	x	x	✓	x	x
Barwon Water	✓	✓	✓	✓	x
Coliban Water	x	✓	✓	✓	x
Goulburn Valley Water	x	✓	✓	✓	x
Gippsland Water	x	✓	✓	✓	x
Central Highlands Water	x	✓	✓	✓	x
Southern Rural Water	x	✓	x	x	✓
Lower Murray Water	x	✓	✓	✓	✓
Grampians Wimmera Mallee Water	x	✓	✓	✓	✓
Goulburn–Murray Rural Water	x	✓	✓	x	✓
<i>Queensland</i>					
SunWater	x	✓	✓	x	✓
<i>South Australia</i>					
SA Water	x	✓	✓	✓	✓
<i>Western Australia</i>					
Water Corporation	✓	✓	✓	✓	✓
<i>Tasmania</i>					
Hobart Water	x	✓	✓	x	✓
Cradle Coast Water	x	✓	x	x	✓
Esk Water	x	✓	x	x	✓
<i>Australian Capital Territory</i>					
ACTEW Corporation	✓	✓	✓	✓	x

^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 revenues generated by these providers can be substantial. For example, the Brisbane City Council and Gold Coast City Council recorded revenue of over \$500 million and \$300 million respectively from their water operations in 2005-06 (BCC 2006; GCCC 2006).

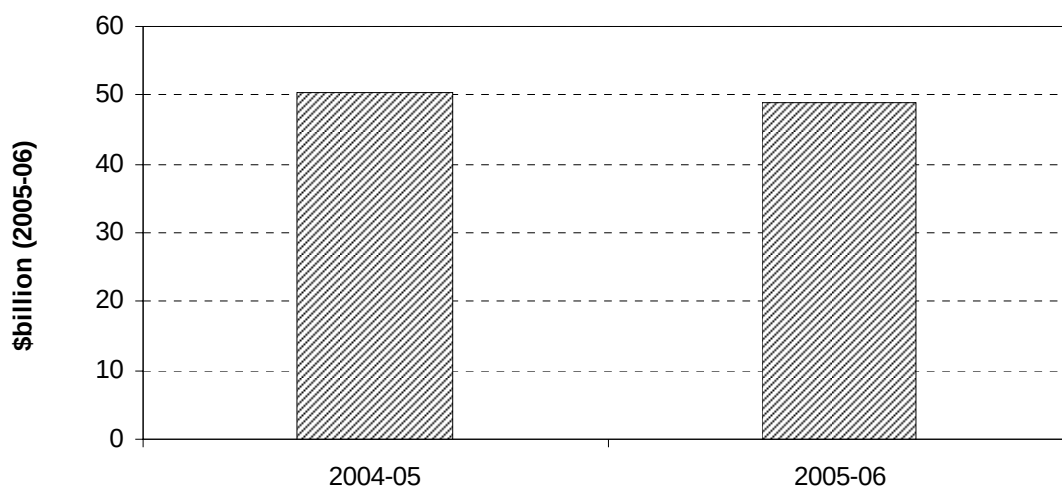
On 1 July 2004, Wimmera Mallee Water (rural water authority) merged with Grampians Water (regional urban water authority) to form Grampians Wimmera Mallee Water. Sunraysia (rural water authority) was also merged with Lower Murray Water (regional urban water authority), to trade as Lower Murray Water. Previous *Financial Performance of Government Trading Enterprises* reports monitored the financial performance of Wimmera Mallee Water and Sunraysia between 2001-02 and 2003-04.

The total assets of water GTEs fell by 3.1 per cent in real terms to \$49.0 billion in 2005-06. Most of this decrease was attributable to a devaluation of Sydney Water's assets. The change in total assets of monitored water GTEs for the last two years, measured in 2005-06 dollars, is shown in figure 6.1.

The size of the water sector GTEs — in terms of the value of the assets controlled and revenue earned — varies substantially (figure 6.2). The smallest monitored water GTE in 2005-06, was Cradle Coast Water (\$98.9 million in assets and \$8.8 million in revenue). The largest monitored water GTE was Sydney Water (\$10.8 billion in assets and \$1.5 billion in revenue).

The regulatory framework for the monitored water GTEs differs across jurisdictions. Most GTEs operate under licences that specify standards for water quality and supply reliability and cover the extraction of water from rivers and underground systems.

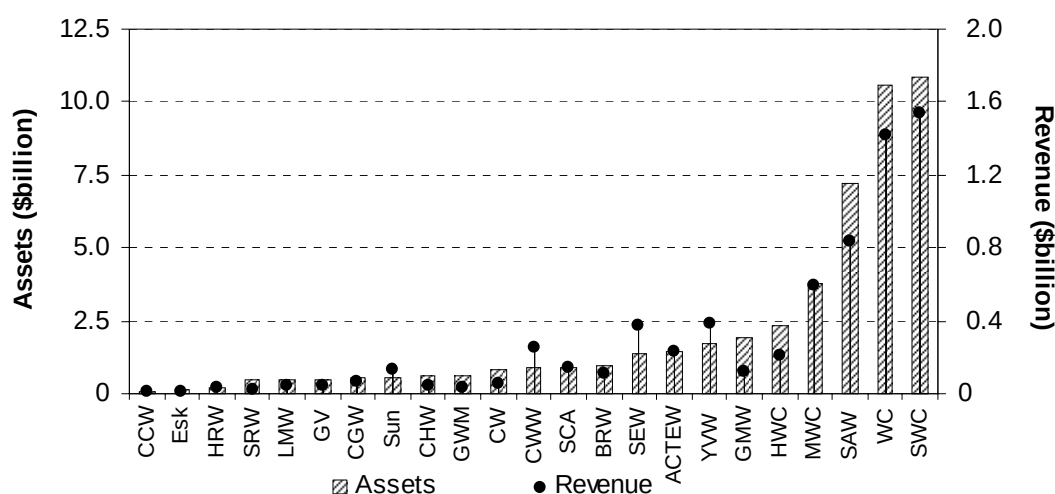
Figure 6.1 Sector assets — water GTEs^a



^a The value of sector assets is reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation for public corporations (chapter 1).

Source: Productivity Commission estimates.

Figure 6.2 Assets and revenue — water GTEs, 2005-06



Source: Productivity Commission estimates.

There are also jurisdictional differences in governance. These include the emphasis on commercial objectives by boards and governments compared with other objectives, such as compliance with the principles of ecologically sustainable development.

The prices charged by NSW, Victorian (metropolitan and regional urban) and ACT water GTEs are regulated by independent bodies.¹ The prices charged by Victorian rural water authorities were set by GTE Boards and approved by the minister in 2005-06. However, from 1 July 2006, they are subject to Essential Services Commission (ESC) price determinations.

In Queensland, WA, SA and Tasmania, government sets water and sewerage charges after consultation with respective water authorities and other stakeholders. A new rural water pricing policy took effect for SunWater from 1 July 2006 and set price paths until 30 June 2011.

¹ The Independent Pricing and Regulatory Tribunal regulates prices for NSW water GTEs, the Independent Competition and Regulatory Commission regulates ACTEW Corporation's prices and the Essential Services Commission (ESC) regulates prices for metropolitan and regional urban water GTEs in Victoria. The ESC's first price determination for regional urban water authorities took effect from 1 July 2005.

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.

Sector-wide 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. Governments agreed to:

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

In June 2004, COAG further agreed to the National Water Initiative (NWI).² The objective of the NWI is to optimise economic, social and environmental outcomes by improving the national consistency of markets and regulatory and planning frameworks for managing Australia’s surface and groundwater resources (COAG 2004). In 2006, COAG reaffirmed its commitment to the NWI and agreed to prioritise the delivery of six fundamental reform elements:

- conversion of existing water rights into secure and tradable water access entitlements;
- completion of water plans that are consistent with the NWI through transparent processes and using best available science;

² All Australian governments are now signatories to the agreement, although the WA and Tasmanian Governments did not initially sign the agreement in 2004.

-
- implementation of these plans to achieve sustainable levels of surface and groundwater extraction in practice;
 - establishment of open and low-cost water trading arrangements;
 - improvement of water pricing to support the wider water reform agenda; and
 - implementation of national water accounting and measurement standards, and adequate systems for measuring, metering, monitoring and reporting on water resources (COAG 2006b).

COAG agreed to establish the National Water Commission to manage the implementation of the NWI and to implement two programs of the Australian Government Water Fund. The Commission is to undertake biennial assessments of the progress with the NWI and state and territory implementation plans, with the first assessment expected to be finalised by mid-2007.

Previously, the National Competition Council assessed the progress of water reforms. The most recent assessment, completed in December 2004, found that all but two governments had made satisfactory progress in implementing their NCP water reform obligations. The exceptions were NSW and WA. NSW was found to have not allocated appropriate water to the environment in stressed and over-allocated systems. As a result, NSW received a suspension of 10 per cent of its 2004-05 NCP competition payment. WA was found to have not completed its program of review and reform of water industry legislation (NCC 2004).

Organisational changes

Some GTEs have privatised or outsourced business activities for commercial reasons. For example, SA Water contracted out the management and operation of the water supply for the Adelaide metropolitan area in 1996 to a private company for a period of 15 years. 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. In addition, Coliban Water has several water treatment plants constructed under public-private partnerships and Central Highlands Water entered into public-private partnerships for services and infrastructure provision in and around Ballarat.

Other GTEs have been restructured for governance reasons. For example, the Sydney Catchment Authority was established in 1999 as a result of a 1998 review of the detection of the parasites *Cryptosporidium* and *Giardia* in Sydney's drinking water. The Sydney Catchment Authority was made responsible for the management and protection of Sydney's water supply catchments, dams, raw water transfer pipelines and canals, and associated infrastructure. This infrastructure had

previously been managed by Sydney Water. Across NSW, there remain over 120 water service providers, most of which are local councils.

More recently, the Victorian water industry has undergone reform of its regulatory structure. The ESC became the economic regulator of the Victorian water sector on 1 January 2004. It is responsible for approving water, sewerage and other prescribed prices for the three metropolitan retail businesses, the regional urban and the rural water businesses operating in Victoria. The first urban water price review undertaken by the ESC was completed in 2005 and approved prices applied from 1 July 2005. The first rural water price review was completed in June 2006, and approved prices applied from 1 July 2006. For all Victorian GTEs, prices are approved until 30 June 2008.

Water demand and supply

Since all the monitored water sector GTEs charge volumetric rates for water use,³ their financial performance is directly related to the amount of water they distribute. This depends on the demand for water, regulated water charges and the GTEs' ability to supply enough water to meet 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 and any related restrictions on usage. For example, SA Water supplied Adelaide with 526 million litres of water per day in 2000-01 (a year with a prolonged hot summer) compared with 454 million litres per day during 2004-05 (SA Water 2005).

For many GTEs, the amount of water they are able to supply in any year is strictly limited, and dependent on current and previous seasonal conditions. The performance of several GTEs was adversely affected by the droughts in 2003-04 and 2005-06 because of limited water availability. South Australia was the first jurisdiction to introduce permanent water restrictions, in October 2003. The Victorian Government implemented similar restrictions in Melbourne in March 2005 and permanent restrictions were introduced in the ACT in March 2006.

Many areas of the country have also introduced temporary water restrictions. Across Victoria, 192 towns were subject to water restrictions as at 30 June 2006

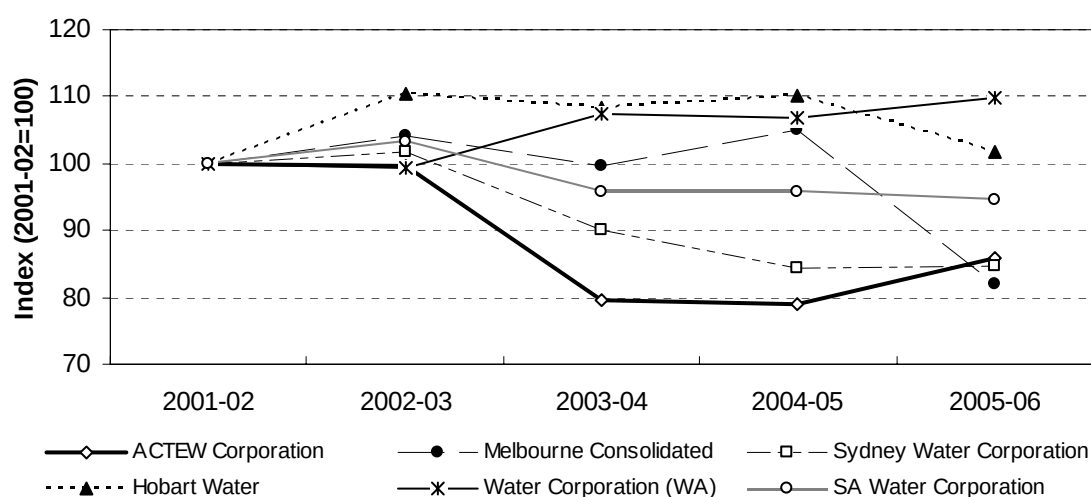
³ Three Tasmanian water GTEs — Hobart Water, Esk Water and Cradle Mountain Water — have a two-part water pricing structure including a variable component which they charge for bulk water supplied to local councils. However, residential and small non-residential properties are charged a flat rate for water supplied by their local council.

(Victorian Water Industry Association 2006). In South East Queensland, Level 1 water restrictions were introduced in May 2005, and because of the worsening drought conditions, Level 5 restrictions apply from 10 April 2007. In rural areas, the water allocation to irrigators depends on water availability and in many areas the drought has severely limited supply. In Victoria, Grampians Wimmera Mallee Water's irrigation customers received no water allocation in 2005-06 (Victorian Water Industry Association 2006).

Water restrictions can also apply to specific customers or specific activities. For example, since September 2001, the WA Government restricted the use of sprinklers by households and businesses to two days per week.

Water restrictions and water conservation efforts appear to have had a significant impact on water sales in some areas of Australia. The volume of water supplied by most urban water GTEs has decreased since 2001-02 (figure 6.3). The Water Corporation in WA was the only metropolitan water GTE to experience a significant increase (9.9 per cent). Overall, aggregate water supplied by urban water GTEs in Australia declined by around 11 per cent between 2001-02 and 2005-06 (WSAA 2007).

Figure 6.3 Urban water supplied — selected water GTEs^a



^a Melbourne Consolidated includes the total urban water supplied by the three Melbourne retail water GTEs, City West Water, South East Water and Yarra Valley Water.

Source: WSAA (2007).

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 for water supply services, typically comprising a fixed access charge and a volumetric charge based on water use.⁴ 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 are in the form of inclining block tariffs, implemented partly as a demand management initiative.

The Victorian Government introduced an inclining block tariff for domestic water users in Melbourne in 2004-05. In 2005-06, households paid 78 cents per kilolitre for the first 440 litres used per day, 92 cents per kilolitre for water used between 440 and 880 litres per day, and between \$1.36 and \$1.44 per kilolitre (dependent on the water retailer) for water used above 880 litres per day. SA Water introduced an inclining block pricing structure in 2004-05, with a fixed access charge and two-tier usage prices. Sydney Water also introduced an inclining block structure for some properties, effective from 1 January 2006.

Two GTEs — Water Corporation and SA Water — continue to use property-based charges for sewerage services.

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

Governments also use water charges to collect revenue for water-related initiatives. For example, from 1 October 2003, SA Water customers were required to pay the ‘Save the Murray Levy’.⁵

From 1 October 2004, Victorian metropolitan and regional urban water authorities were required to make environmental contributions of 5 per cent of revenue under the *Water Industry Act 1994*. With the exception of Goulburn–Murray Water, rural water authorities were required to contribute 2 per cent of revenue from 1 July 2005. Between 2004 and 2008, these water authorities are expected to contribute approximately \$225 million to fund environmental renewal projects

⁴ Usage-based charges were first introduced in 1982 by the Hunter District Water Board (now the Hunter Water Corporation).

⁵ The SA Government uses this to fund its \$13 million annual contribution to an agreement with the Australian, NSW, Victorian and ACT Governments to commit \$500 million over five years to improve the health of the Murray River.

around Victoria. In 2004, affected water authorities were permitted to, and did, increase their water charges to cover their contribution.

Customer growth

Revenue volatility is 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.

The level of contributed assets from developers that water GTEs receive each year is affected by the level of land development.⁶ For example, in 2004-05, the number of dwelling units commenced in SA increased by 5.7 per cent and the value of developer contributions received by SA Water increased by 60 per cent. In 2005-06, developer contributions fell by 9.3 per cent and the number of dwelling units commenced fell by 0.7 per cent (SA Water 2006; ABS 2006b).

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 17 per cent of its total revenue in 2005-06. In contrast, developer charges and contributions accounted for less than 2.9 per cent of ACTEW Corporation's total revenue in 2005-06, and were not required by the 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, the diverse range of activities of the entities has to be taken into account when comparing indicators across GTEs.

⁶ A proxy for the level of land development is the number of dwelling unit commencements. However, this can include some building activity in established areas that does not produce developer contributions. The total number of dwelling units commenced in Australia increased by 3.6 per cent in 2002-03 and 1.2 per cent in 2003-04, and fell by 8.6 per cent in 2004-05 and 4.4 per cent in 2005-06 (ABS 2006).

Under the NWI, metropolitan water GTEs are expected to achieve upper bound cost recovery by 2008, while rural water GTEs are expected to achieve lower bound cost recovery and, where practicable, move towards the upper bound (COAG 2004).⁷

For the water sector as a whole the pre-tax operating profit increased in real terms by 25 per cent to \$2.1 billion in 2005-06, despite the drought conditions affecting several states. This resulted from a 1.9 per cent increase in total revenue and a 6.1 per cent decrease in total expenses in real terms. Individually, 12 out of the 23 water sector GTEs reported an improvement in their real operating performance in 2005-06.

The rate of return on assets is a useful indicator of the efficiency with which an entity uses its assets. The asset base used to calculate the return on assets in this report is the total value of assets in a GTE's annual report. For some water GTEs, particularly in urban areas, this includes contributed assets from developers received at no cost to the GTE. However, GTE prices are set by regulators to provide a commercial rate of return on assets, excluding contributed assets, because they do not require a capital investment by the GTE.⁸ If contributed assets were excluded from the asset base, rates of return on assets would be higher than those included in this report.

The return on assets for the sector increased to 5.5 per cent in 2005-06 (4.4 per cent in 2004-05), as growth in profitability exceeded growth in the sector's assets. Thirteen of the 23 water sector GTEs reported an improved return on assets in 2005-06 compared with 2004-05 (figure 6.4).

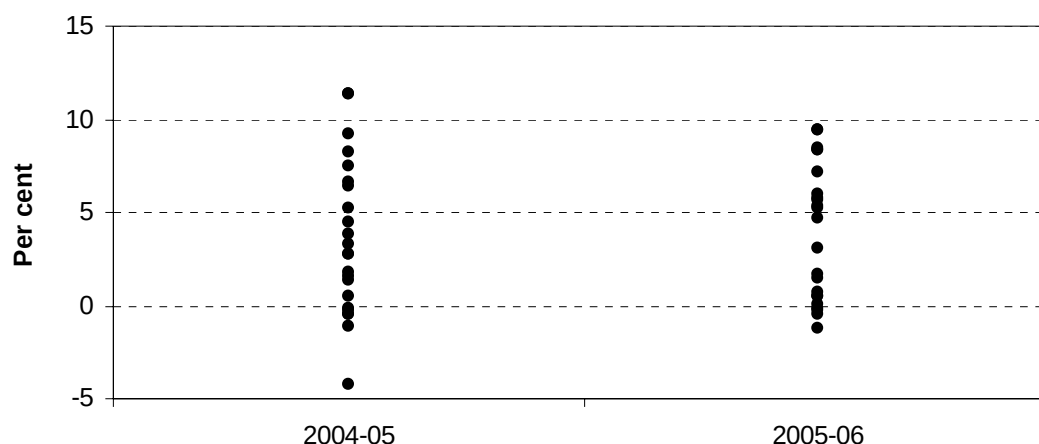
Of the 23 water GTEs, 15 did not achieve a return on assets that exceeded the risk-free benchmark return on assets in 2005-06.⁹ This suggests that these water GTEs are not operating on a commercially viable basis. Of the eight GTEs that did achieve this level, six were urban water GTEs and two were state-wide GTEs that

⁷ Lower bound cost recovery pricing 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. Upper bound — full cost recovery — pricing also encompasses the total opportunity cost of the GTE's investment in assets (calculated using a weighted average cost of capital). Governments first made the commitment to use cost recovery bands to set prices in 1998 (PC 2005a).

⁸ Contributed assets, however, are likely to require maintenance or replacement at some time in the future.

⁹ The risk-free rate of return used is the 2005-06 interest rate on a 10-year Australian Government reference bond (5.4 per cent) (RBA 2007a).

Figure 6.4 Return on assets — water GTEs^a



^a 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.

encompass large urban areas.¹⁰ The four monitored GTEs that generated negative return on assets ratios service regional and rural areas.¹¹

In Victoria, there are distinct differences in the profitability of water GTEs operating in metropolitan and non-metropolitan areas.¹² The aggregate return on assets for Victorian metropolitan water GTEs in 2005-06 was 8.0 per cent, compared with a return on assets of around 0.2 per cent for regional urban and rural water GTEs.

Victorian rural water GTEs — Southern Rural Water, Lower Murray Water, Grampians Wimmera Mallee Water and Goulburn–Murray Rural Water — use the renewals annuity approach in setting water charges, but use accounting depreciation in reporting operating results (box 6.1). Using the renewals annuity approach results in lower prices and decreased reported profitability on an accounting depreciation

¹⁰ The eight GTEs are Sydney Water, Melbourne Water Corporation, City West Water, South East Water, Yarra Valley Water, Water Corporation, SA Water and ACTEW Corporation.

¹¹ The four GTEs are Coliban Water, Southern Rural Water, Grampians Wimmera Mallee Water and Goulburn–Murray Rural Water.

¹² The metropolitan water GTEs are Melbourne Water Corporation, City West Water, Yarra Valley Water and South East Water. The other monitored water GTEs from Victoria are regional urban or rural water authorities.

Box 6.1 Renewals annuity pricing

Charges for rural water GTEs in Victoria during 2005-06 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. From 1 July 2006, the Essential Services Commission's first price determination takes effect to specify how prices can be determined by Victorian rural water GTEs. Under the new regulatory arrangement, renewals annuity pricing will continue to be used.

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 at least the operational, maintenance and administrative costs, externalities (defined as the environmental and natural resource management costs attributable to and incurred by the water business), taxes or tax equivalents (not including income tax), the interest cost on debt, dividends (if any) and provision for future asset refurbishment/replacement' (NWC 2005, p. 43).

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 below for a renewals reconciliation for Goulburn–Murray Water in 2005-06).

Renewals reconciliation — Goulburn–Murray Water, 2005-06 (\$'000)

Net operating result (accounting depreciation based)	-4 215
Add back accounting depreciation	30 516
Less renewals annuity	20 412
Net operating result (renewals-based)	5 889

The renewals annuity charge is typically less than the equivalent accounting depreciation expense. Therefore, a GTE's net operating result as reported on an accounting depreciation basis, with prices set under the renewals-based approach, is generally lower than if prices had provided for accounting depreciation. A comparison of Southern Rural Water's operating position over the reporting period, under the accounting depreciation and renewals-based approach, is provided below:

Renewals reconciliation — Southern Rural Water, 2004-05 to 2005-06^a

	2004-05	2005-06
Net operating profit (\$'000)	-1 079	-1 121
Net operating result (renewals-based result) (\$'000)	2 988	2 778

^a Data reported under Australian-equivalent International Financial Reporting Standards.

Source: GMW (2006); SRW (2005, 2006).

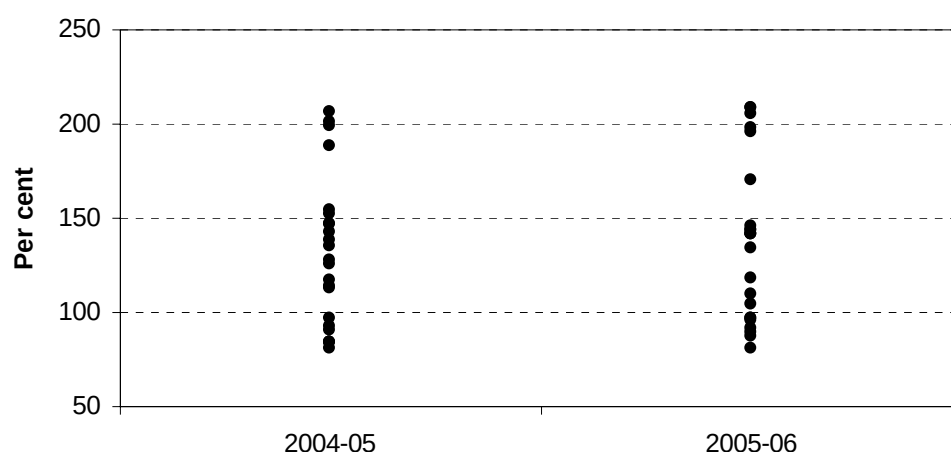
basis, contributing to the negative return on assets reported by Victorian rural GTEs in 2005-06.

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 followed a similar trend to return on assets for most water GTEs in 2005-06.

The cost recovery ratio indicates the ability of an entity to generate adequate revenue to meet expenses. For the sector as a whole, the cost recovery ratio increased 14.5 percentage points to 163.5 per cent in 2005-06. Seventeen of the water GTEs recorded a cost recovery ratio over 100 per cent in 2005-06 and 14 recorded an improved cost recovery ratio from 2004-05 (figure 6.5). The four Victorian rural GTEs that recorded negative return on assets ratios also failed to recover their recurrent costs.

Setting charges that do not cover costs, including the cost of capital, has implications for incentives, particularly when considering future investment decisions within the sector and across the economy. Under the full corporatisation model, the intention is to subject GTEs to the same capital market disciplines as the private sector.

Figure 6.5 Cost recovery — water GTEs^a



^a 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 government to cover operational deficits. Expenses from operations are calculated by subtracting gross interest expense from total expenses.

Source: Productivity Commission estimates.

6.4 Financial management

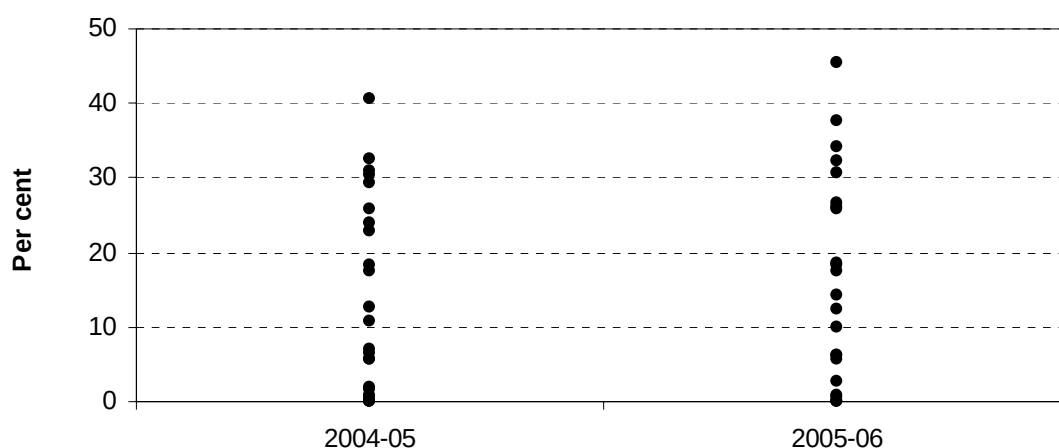
Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

The real level of debt of monitored water GTEs increased by \$788 million (8.9 per cent) to \$9.7 billion in 2005-06. More than 70 per cent of the growth in debt was attributable to three water GTEs — Water Corporation, Sydney Catchment Authority and Sydney Water — who hold 48 per cent of the sector's debt. The increase in debt for the sector was partly offset by growth in total assets, resulting in a small increase in the debt to total assets ratio from 17.6 per cent in 2004-05 to 19.9 per cent in 2005-06 (figure 6.6).

Individually, the debt to total assets ratio increased for 11 and declined for 11 of the water GTEs in 2005-06. Two GTEs — Southern Rural Water and Esk Water — operated debt free in 2005-06.

Interest cover measures the capacity of a GTE to meet periodic interest payments out of current earnings. A high interest cover ratio indicates that an entity can sustain a fall in profit or an increased interest expense and still meet the cost of servicing debt. The interest cover for the water sector was 4.7 times in 2005-06, up

Figure 6.6 Debt to total assets — water GTEs^a



^a 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.

from 4.1 times in 2004-05. Three GTEs had negative interest cover ratios and another four had ratios below 2 times in 2005-06.

The ability of water GTEs to meet short-term liabilities without having to use funds other than current assets is indicated by having a current ratio of over 100 per cent. The current ratio of the water sector as a whole was 51.1 per cent in 2005-06, suggesting it has low levels of liquidity. Individually, 10 water GTEs had current ratios less than 100 per cent, down from 13 in 2004-05, suggesting some improvement in the sector. Although some water GTEs had current ratios below 100 per cent, 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

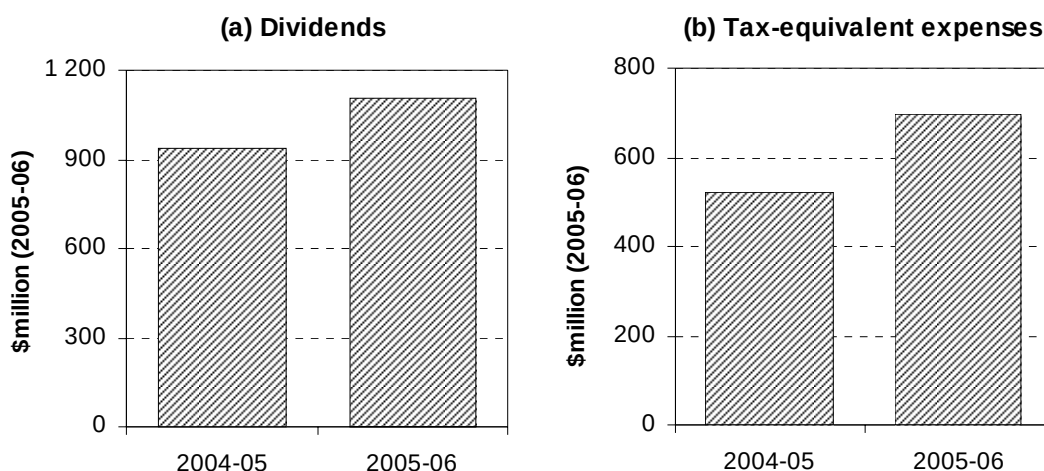
As part of the reform process, governments have sought to give GTEs a greater commercial focus and facilitate competitive neutrality by exposing them to capital market disciplines and regulations similar to those faced by private sector businesses.

The dividend payable by each GTE depends on the dividend policy of its owner government. Fourteen of the monitored water GTEs distributed a dividend in 2005-06. Of those, all but one recorded a dividend payout ratio above 50 per cent and four recorded ratios of at least 100 per cent. All nine of the GTEs that did not report a dividend payment in 2005-06 were Victorian regional water authorities. For the sector as a whole, dividend payments increased by \$167 million (18 per cent) in real terms to \$1.1 billion (figure 6.7a).

The value of recorded income tax-equivalent expenses increased by \$177 million (34 per cent) in real terms to \$697 million in 2005-06 (figure 6.7b). This was mostly a result of the 25 per cent real increase in the pre-tax operating profits recorded for the sector.

Seventeen GTEs recorded income tax-equivalent expenses in 2005-06. Ten of these GTEs recorded higher real income tax-equivalent expenses in 2005-06 than in 2004-05. The change in tax-equivalent expenses recorded by individual GTEs did not align so closely with movements in their pre-tax operating profit. This was because of the effect of other factors such as asset revaluations and previous tax payments. For example, in 2005-06, ACTEW Corporation's operating profit before tax decreased by 1.5 per cent in real terms and its tax-equivalent expense increased by 72 per cent. This increase was attributable to a lower than expected tax-equivalent expense in 2004-05.

Figure 6.7 Dividends and income tax-equivalent expenses — water GTEs^a



^a The value of dividends and tax-equivalent expenses are reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1).

Source: Productivity Commission estimates.

CSOs provided by some water GTEs include concessions, the supply of services below the cost of provision and upgrading sewerage infrastructure. Seventeen water GTEs received funding for CSOs in 2005-06 totalling \$673 million.¹³ CSO payments to the Water Corporation of WA accounted for over 50 per cent of all CSO funding in the water sector.

Of the GTEs that received CSO funding, all but three — Hunter Valley Water, Lower Murray Water and Yarra Valley Water — received an increase in the real value of CSO payments. Five GTEs experienced an increase of over 10 per cent in real terms.

CSO payments represented over 10 per cent of total revenue for three GTEs, Southern Rural Water (15 per cent), SA Water (18 per cent) and Water Corporation (24 per cent).

6.6 Implications of the new accounting standards

From 2005-06, financial data for all monitored water GTEs are based on the Australian-equivalent International Financial Reporting Standards (AIFRS). The adoption of the new accounting standards changed the recognition and measurement

¹³ Several Victorian GTEs disclose CSO payments in their annual reports, but do not report the amount separately in their financial statements.

of some assets, liabilities and equity items, and affected the recording of income flows. These changes, which were discussed in the previous *Financial Performance of Government Trading Enterprises* report (PC 2006, chapter 3), have had a significant effect on the comparability over time of financial performance and financial management indicators.

The aggregate impact of the transition to AIFRS for the monitored water GTEs can be gauged by comparing 2004-05 data on an AIFRS and pre-AIFRS basis (table 6.2). Similar comparisons can be made by reference to each GTE summary.

WATER

Table 6.2 Whole of sector performance indicators 2004-05 to 2005-06^a

		Pre-AIFRS ^{b,c}		AIFRS ^b
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	48 265	48 265	48 982
Total revenue	\$m	6 339	6 274	6 697
Profitability				
Operating profit before tax	\$'000	1 817 938	1 610 429	2 113 042
Operating sales margin	%	35.9	33.2	39.4
Cost recovery	%	155.4	148.9	163.5
Return on assets	%	4.8	4.4	5.5
Return on equity	%	3.6	3.3	4.2
Financial management				
Debt to equity	%	23.0	24.8	28.6
Debt to total assets	%	17.4	17.6	19.9
Total liabilities to equity	%	32.7	40.9	44.6
Interest cover	times	4.6	4.1	4.7
Current ratio	%	52.0	52.1	51.1
Leverage ratio	%	132.7	140.9	144.6
Payments to and from government				
Dividends	\$'000	908 532	893 682	1 102 687
Dividend to equity ratio	%	2.5	2.6	3.2
Dividend payout ratio	%	70.1	80.2	77.9
Income tax expense	\$'000	522 065	496 624	697 283
CSO funding	\$'000	556 169	558 193	672 503

^a Figures are nominal values. ^b Water GTEs commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for water GTEs. ^c Data prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

6.7 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)
Lower Murray Water (Victoria)
Grampians Wimmera Mallee Water (Victoria)
Goulburn–Murray Rural Water Authority (Victoria)
SunWater (Queensland)
Water Corporation (WA)
SA Water Corporation (SA)
Hobart Regional Water Authority (Tasmania)
Cradle Coast Water (Tasmania)
Esk Water Authority (Tasmania)
ACTEW Corporation (ACT)

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 issued by the Department of Land and Water Conservation.¹

The *Sydney Water Catchment Amendment Act 2003* came into effect on 20 November 2004, providing for the possibility of the SCA building small hydro-electricity plants as part of its catchment infrastructure. The *Public Sector Employment Legislation Amendment Act 2006*, which commenced on 17 March 2006, required the transfer of all staff from the SCA to the Sydney Catchment Authority Division of the Government Services (SCA Division). The SCA Division provides personnel services to the SCA.

Charges for bulk water and other services are determined by the Independent Pricing and Regulatory Tribunal (IPART). In September 2005, IPART released its final determination of SCA's prices to apply for one year from 1 October 2005.²

The SCA increased total assets by \$123 million (16 per cent) in 2005-06, through an increase in the value of work-in-progress in the Metropolitan water plan and the Prospect Reservoir upgrade. Total liabilities increased by \$122 million (46 per cent) because of an increase in long-term NSW Government loans.

Operating profit before tax increased by 127 per cent to \$28.3 million in 2005-06. This resulted from a \$16.5 million (13 per cent) increase in total revenue to \$141 million, while total expenses remained stable at \$112 million. The increase in revenue was mainly attributable to an increase in bulk water sales. Bulk water sales to Sydney Water Corporation accounted for 98 per cent of total revenue in 2005-06.

The SCA provided for a \$16.6 million dividend payment and recorded an \$11.1 million income tax-equivalent expense in 2005-06. The funding arrangements for SCA's non-commercial activities, such as managing a range of heritage items including old dams and weirs, walking tracks and bridges, are not reported in the financial statements. However, the SCA is required to provide these services under its operating licence.

¹ The operating licence places obligations on the SCA with respect to customer service and system and environmental performance.

² In September 2006, IPART released a further price determination for bulk water for the period 1 October 2006 to 30 June 2010. The determination sought to encourage better use of water by aligning usage charges with the estimated long-run marginal cost of the planned measures.

SYDNEY CATCHMENT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	775	780	903
Total revenue	\$m	126	124	141
Profitability				
Operating profit before tax	\$'000	21 841	12 485	28 284
Operating sales margin	%	27.2	20.1	31.5
Cost recovery	%	137.3	125.2	146.0
Return on assets	%	4.5	3.3	5.4
Return on equity	%	3.0	1.8	3.3
Financial management				
Debt to equity	%	35.4	36.5	61.5
Debt to total assets	%	24.0	24.0	37.6
Total liabilities to equity	%	47.4	51.9	75.6
Interest cover	times	0.3	1.9	2.7
Current ratio	%	33.3	31.4	28.3
Leverage ratio	%	147.4	151.9	175.6
Payments to and from government				
Dividends	\$'000	15 387	15 387	16 581
Dividend to equity ratio	%	2.9	3.0	3.2
Dividend payout ratio	%	97.0	169.9	97.0
Income tax expense	\$'000	5 977	3 426	11 191
CSO funding	\$'000	na	na	na

^a The Sydney Catchment Authority (SCA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the SCA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. **na** Not available.

Sydney Water Corporation (Sydney Water) operates under the *State Owned Corporations Act 1991* and the *Sydney Water Act 1994*.¹ Sydney Water supplies drinking water, wastewater services and some stormwater services to Sydney, the Blue Mountains and Illawarra under an operating licence granted by the Governor.²

Sydney Water's charges are regulated by the NSW Independent Pricing and Regulatory Tribunal (IPART). In September 2005, IPART released its final determination for Sydney Water's prices, effective from 1 October 2005 to 30 June 2009. This provided for a two-tier pricing structure and significant price increases for average residential customers to promote water conservation. IPART is also responsible for conducting annual audits of Sydney Water's compliance with its licence.

Assets decreased by around \$755 million (6.5 per cent) in 2005-06, primarily because of a devaluation of system assets and works-in-progress. Liabilities remained relatively unchanged at around \$4.3 billion, the net effect of a \$236 million increase in borrowings and a decrease in deferred tax liabilities and provisions.

Operating profit before tax increased by \$302 million (188 per cent) to \$462 million in 2005-06. This resulted from a combination of increased revenue, particularly from service availability and usage charges, and decreased expenses because of a net superannuation provision gain of \$191 million

Sydney Water provided for \$120 million in dividends and recorded a \$196 million income tax-equivalent expense in 2005-06.

Sydney Water received community service obligation payments from the NSW Government in 2005-06 for providing pensioner and other rebates (\$84.2 million), and priority sewerage social programs (\$1.9 million). It also received reimbursements from the Department of Energy, Utilities and Sustainability Water Savings Fund (\$17.0 million). Together these payments accounted for 7.0 per cent of Sydney Water's total revenue.

¹ The enactment of the *Water Legislation Amendment (Drinking Water and Corporate Structure) Act 1998* changed the status of Sydney Water from a 'company' to a 'statutory' state-owned corporation. The change gave the responsible minister greater power to make directions and access information, among other things.

² The operating licence places obligations on Sydney Water with respect to customer service, system performance and environmental performance. A new licence became effective on 1 July 2005.

SYDNEY WATER CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	12 120	11 574	10 819
Total revenue	\$m	1429	1425	1541
Profitability				
Operating profit before tax	\$'000	270 106	160 224	461 740 ^c
Operating sales margin	%	29.5	21.9	41.0
Cost recovery	%	141.8	128.0	167.7
Return on assets	%	3.5	2.7	5.7
Return on equity	%	2.5	1.5	3.9
Financial management				
Debt to equity	%	31.6	36.5	44.3
Debt to total assets	%	22.4	22.8	25.7
Total liabilities to equity	%	41.4	60.1	66.9
Interest cover	times	0.4	2.0	3.7
Current ratio	%	40.9	33.2	33.1
Leverage ratio	%	141.4	160.1	166.9
Payments to and from government				
Dividends	\$m	120	120	193
Dividend to equity ratio	%	1.4	1.7	2.8
Dividend payout ratio	%	55.8	110.0	72.7
Income tax expense	\$'000	55 025	51 089	196 155
CSO funding	\$'000	79 079	79 079	86 075

^a Sydney Water Corporation (Sydney Water) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Sydney Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c This includes a net superannuation gain of \$191 million (-\$85.6 million in 2004-05).

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.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 NSW Independent Pricing and Regulatory Tribunal (IPART). In September 2005, IPART issued a price determination for the period from 1 November 2005 to 30 June 2009. This determination phases out the discounted price for water users with over 1000 kilolitres of consumption per year and requires stormwater charges to be based on property size.

HWC's total assets decreased by \$43.1 million (1.8 per cent) to \$2.3 billion in 2005-06, primarily because of a decrease in the value of water and sewer assets. Total liabilities increased by \$12.2 million (1.8 per cent) to \$700 million.

HWC's operating profit increased by 71 per cent to \$95.5 million in 2005-06. Total revenue grew by 13 per cent to \$209 million primarily because of higher revenue from service and usage charges (\$13.8 million) and increases in developer contributions (\$6.5 million). Expenses decreased by 12 per cent to \$114 million because of a net gain on superannuation as opposed to the loss in 2004-05.

HWC is subject to dividend and tax-equivalent payments. HWC distributed \$35.1 million in dividends in 2005-06. The dividend payout ratio nearly halved to 46.9 per cent in 2005-06 because dividends increased by 3.8 per cent while profits increased by 71 per cent. HWC recorded a \$20.6 million income tax-equivalent expense in 2005-06.

The NSW Government funds HWC to provide tariff rebates to pensioners and for exempt properties such as churches. The community service obligation payments equalled \$9.5 million in 2005-06, accounting for 4.5 per cent of HWC's total revenue.

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 It operates under an operating licence, as granted by the Governor, which places obligations on HWC with respect to customer service, system performance and environmental performance.

HUNTER WATER CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	2 332	2 380	2 337
Total revenue	\$m	193	185	209
Profitability				
Operating profit before tax	\$'000	63 842	55 822	95 513
Operating sales margin	%	37.9	35.2	52.2
Cost recovery	%	161.0	154.3	209.0
Return on assets	%	3.2	2.8	4.7
Return on equity	%	2.1	2.3	4.5
Financial management				
Debt to equity	%	8.2	9.8	14.4
Debt to total assets	%	7.1	7.0	10.0
Total liabilities to equity	%	14.7	40.6	42.8
Interest cover	times	0.6	6.5	7.7
Current ratio	%	22.9	38.3	53.0
Leverage ratio	%	114.7	140.6	142.8
Payments to and from government				
Dividends	\$m	33 800	33 800	35 100
Dividend to equity ratio	%	1.7	2.0	2.1
Dividend payout ratio	%	78.6	87.9	46.9
Income tax expense	\$'000	20 819	17 350	20 629
CSO funding	\$'000	9 668	9 668	9 503

^a Hunter Water Corporation (HWC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for HWC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

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, sewage treatment and stormwater and drainage management. Its main customers are the three retail water GTEs in Melbourne — City West Water, South East Water and Yarra Valley Water.¹ Services are also provided to other water authorities, local councils, land developers and businesses that divert water. MWC's waterways and drainage boundaries were extended to include new areas of responsibility within the Port Phillip and Westernport regions in November 2005.

The Essential Services Commission became responsible for regulating the pricing and services of MWC on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 2.1 per cent above the inflation rate in each year until 30 June 2008.

Assets increased by \$136 million (3.7 per cent) in 2005-06, primarily because of additions to infrastructure such as replacing the Morang-Preston water pipeline and upgrading the Winneke Treatment Plant. Liabilities increased by \$103 million (5.7 per cent) attributable to an increase in deferred tax liabilities and debt.

Operating profit before tax increased by \$35.0 million (18 per cent) to \$228 million in 2005-06. Higher revenue from water, sewage and drainage services and receipt of assets from the drainage boundary expansion contributed to the increase in total revenue of \$67.0 million (13 per cent), while total expenses increased by \$32.0 million (9.6 per cent) because of an increase in operational and maintenance expenses.

MWC is required to make dividend and tax-equivalent payments. Dividend payments were \$97.0 million in 2005-06, up 135 per cent from 2004-05 when no interim dividend was paid. MWC recorded an income tax-equivalent expense of \$59.0 million in 2005-06, down 3.8 per cent from 2004-05.

MWC was not subject to community service obligations in 2005-06.

¹ Water supply and sewage treatment charges and drainage rates constitute the majority of MWC's revenue. MWC relies on the three retail water GTEs for billing and collection of its drainage services charges.

MELBOURNE WATER CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	3 263	3 633	3 769
Total revenue	\$m	528	526	593
Profitability				
Operating profit before tax	\$'000	188 621	192 723	227 714
Operating sales margin	%	50.5	51.5	52.1
Cost recovery	%	201.9	206.0	208.7
Return on assets	%	8.2	7.5	8.3
Return on equity	%	8.4	7.3	9.3
Financial management				
Debt to equity	%	78.8	65.6	68.5
Debt to total assets	%	36.1	32.6	34.1
Total liabilities to equity	%	118.5	101.0	104.8
Interest cover	times	0.8	3.5	3.8
Current ratio	%	19.3	17.6	26.0
Leverage ratio	%	218.5	201.0	204.8
Payments to and from government				
Dividends	\$m	41 300 ^c	41 300 ^c	97 000 ^d
Dividend to equity ratio	%	2.9	2.3	5.3
Dividend payout ratio	%	32.9	31.4	57.5
Income tax expense	\$'000	62 920	61 338	58 983
CSO funding	\$'000	..	..	..

^a Melbourne Water Corporation (MWC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 were reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for MWC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c This dividend includes the final dividend relating to 2003-04 but not the 2004-05 interim dividend because it was not recognised by 30 June 2005. ^d This dividend includes the interim and final dividends relating to 2004-05. The proposed interim and final dividends relating to 2005-06 were not recognised by 30 June 2006. .. Not applicable.

City West Water (CWW) commenced operations on 1 January 1995. CWW was 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 307 000 residential, commercial and industrial customers in Melbourne's central business district, and the inner and western suburbs.

The Essential Services Commission (ESC) became responsible for regulating the pricing and services of CWW on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 2.2 per cent above the inflation rate in each year until 30 June 2008. The ESC asserts that the key driver behind the price increase was infrastructure investment (ESC 2005).

Assets increased by \$60.5 million (7.5 per cent) in 2005-06, because of additions to property, plant and equipment. Liabilities increased by \$49.4 million (12 per cent) resulting from a trebling of current debt. Consequently, debt to equity and debt to total assets ratios both increased.

Operating profit before tax fell by \$15.4 million (20 per cent) to \$62.4 million in 2005-06. Expenses increased by \$8.2 million (4.4 per cent) because of an asset write off associated with the Altona Treatment Plant upgrade and increased environmental contribution payments. Total revenue decreased by \$7.2 million (2.7 per cent), the net effect of a small increase in sales revenue and a reduction in developer contributions (down 45 per cent to \$28.3 million, following an ESC determination).

CWW is required to make dividend and tax-equivalent payments. Dividend provisions decreased by 33 per cent to \$27.7 million in 2005-06. CWW recorded a \$23.6 million income tax-equivalent expense, down 17 per cent from 2004-05.

CWW is reimbursed for the value of concessions provided to pensioners and others, and for the administration of the concession schemes. Community service obligation payments of \$11.3 million accounted for 4.4 per cent of total revenue in 2005-06. These payments were not separately recorded in CWW's income statement but were acknowledged in its annual report commentary.

CITY WEST WATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	802	803	863
Total revenue	\$m	264	264	257
Profitability				
Operating profit before tax	\$'000	77 385	77 746	62 369
Operating sales margin	%	34.4	34.5	30.4
Cost recovery	%	152.3	152.6	143.7
Return on assets	%	11.3	11.3	9.4
Return on equity	%	13.0	12.8	9.9
Financial management				
Debt to equity	%	57.2	60.7	67.5
Debt to total assets	%	29.3	29.3	32.2
Total liabilities to equity	%	95.2	107.5	116.9
Interest cover	times	6.8	6.8	4.9
Current ratio	%	58.2	49.8	31.3
Leverage ratio	%	195.2	207.5	216.9
Payments to and from government				
Dividends	\$'000	41 600	41 600	27 700
Dividend to equity ratio	%	10.1	10.8	7.1
Dividend payout ratio	%	78.0	84.2	71.5
Income tax expense	\$'000	24 024	28 338	23 606
CSO funding ^c	\$'000	10 001	10 001	11 274

^a City West Water (CWW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for CWW. ^b Data for years prior to 2004-05 are available in previous Financial Performance of Government Trading Enterprises reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c CWW does not report community services obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary.

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 people in the southern and eastern suburbs of Melbourne.

The Essential Services Commission became responsible for regulating the pricing and services of SEW on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 2.0 per cent above the inflation rate in each year until 30 June 2008.

Assets and liabilities increased by \$44.5 million (3.4 per cent) and \$33.4 million (5.1 per cent) respectively in 2005-06, mainly because of increased capital expenditure funded by borrowing. There was also a \$9.1 million increase in deferred tax liabilities because of an increase in the value of property, plant and equipment.

Operating profit before tax fell by \$10.3 million (11 per cent) to \$86.5 million in 2005-06. While total revenue remained stable at around \$380 million, total expenses increased by 3.9 per cent to \$292 million. This rise was primarily attributable to an increase in bulk water and sewerage charges and in the environmental levy.

SEW is required to make dividend and tax-equivalent payments. It provided for a \$45.8 million dividend in 2005-06, an increase of \$11.0 million from 2004-05, and recorded an income tax-equivalent expense of \$29.6 million in 2005-06.

SEW administered the Pensioner Rebate Scheme, the Utility Relief Grant Scheme and the Water Conservation Assistance Pilot Program on behalf of the Victorian Government in 2005-06. SEW received \$20.9 million in community service obligation payments in relation to these schemes. These payments were not separately reported in SEW's income statement but were acknowledged in its annual report commentary.

SOUTH EAST WATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 318	1 319	1 363
Total revenue	\$m	381	378	379
Profitability				
Operating profit before tax	\$'000	96 249	96 853	86 537
Operating sales margin	%	31.7	32.1	29.6
Cost recovery	%	146.4	147.3	142.0
Return on assets	%	9.2	9.2	8.4
Return on equity	%	9.4	9.6	8.5
Financial management				
Debt to equity	%	53.4	61.4	60.7
Debt to total assets	%	28.9	31.0	30.6
Total liabilities to equity	%	84.8	98.1	101.4
Interest cover	times	4.9	4.9	4.4
Current ratio	%	54.0	59.5	54.9
Leverage ratio	%	184.8	198.1	201.4
Payments to and from government				
Dividends	\$'000	34 800	34 800	45 800
Dividend to equity ratio	%	4.9	5.2	6.8
Dividend payout ratio	%	51.8	54.2	80.4
Income tax expense	\$'000	29 082	32 665	29 588
CSO funding ^c	\$'000	19 231	19 169	20 906

^a South East Water (SEW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for SEW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c SEW does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary.

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 services more than 1.6 million people and 60 000 business customers in the northern and eastern suburbs of Melbourne, providing retail water supply and sewerage services, as well as the collection of tradewaste.

The Essential Services Commission became responsible for regulating the pricing and services of YVW on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 1.8 per cent above the inflation rate in each year until 30 June 2008.

Total assets increased by \$162 million (10 per cent) in 2005-06 — mainly from additions to infrastructure, property, plant and equipment, including the transfer of infrastructure assets from the Goulburn Valley Regional Water Authority. Total liabilities increased by \$129 million (13 per cent), primarily because of increased borrowings. As a result, debt to equity and debt to total assets ratios rose.

Operating profit before tax fell \$9.0 million (15 per cent) in 2005-06. Total revenue increased by \$2.3 million (0.6 per cent). However, total expenses increased by \$11.3 million (3.5 per cent) because of higher finance costs, depreciation expenses and environmental contributions. This led to a fall in the return on assets and return on equity ratios.

YVW is required to make dividend and tax-equivalent payments to the Victorian Government. YVW made \$36.8 million in dividend payments in 2005-06, a decrease of \$7.3 million from 2004-05. As a result the dividend payout ratio decreased but remained above 100 per cent. YVW recorded an income tax-equivalent expense of \$16.7 million in 2005-06.

YVW is reimbursed for the value of concessions provided to pensioners and others. Community service obligation payments were \$23.8 million in 2005-06, accounting for 6.2 per cent of total revenue. These payments were not separately recorded in YVW's income statement but were acknowledged in its annual report commentary.

YARRA VALLEY WATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 552	1 557	1 719
Total revenue	\$m	381	382	384
Profitability				
Operating profit before tax	\$'000	61 129	61 804	52 801
Operating sales margin	%	26.1	26.2	25.6
Cost recovery	%	135.3	135.5	134.4
Return on assets	%	6.4	6.4	6.0
Return on equity	%	6.6	7.3	6.0
Financial management				
Debt to equity	%	99.4	108.8	120.9
Debt to total assets	%	40.8	40.7	45.4
Total liabilities to equity	%	143.5	167.3	179.5
Interest cover	times	2.6	2.6	2.2
Current ratio	%	56.7	51.2	34.2
Leverage ratio	%	243.5	267.3	279.5
Payments to and from government				
Dividends	\$'000	44 100	44 100	36 800
Dividend to equity ratio	%	6.9	7.6	6.1
Dividend payout ratio	%	105.0	103.8	102.1
Income tax expense	\$'000	19 124	19 326	16 747
CSO funding ^c	\$'000	21 142	23 226	23 813

^a Yarra Valley Water (YVW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for YVW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c YVW does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary.

The Barwon Regional Water Authority (Barwon Water) was established under the *Water Act 1989*. Barwon Water provides water and sewerage services to 271 000 residents in Geelong and surrounding areas, making it Victoria's largest regional urban water authority.

The Essential Services Commission became responsible for regulating the pricing and services of Barwon Water on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 5.3 per cent above the inflation rate in each year until 30 June 2008. This resulted in a price increase of 7.8 per cent for 2005-06.

Assets increased by \$11.2 million to \$992 million in 2005-06 because of Barwon Water's continued investment in capital works. Although borrowings remained stable, there was an increase in deferred tax liabilities. This contributed to a 3.0 per cent rise in total liabilities to \$114 million.

Operating profit before tax increased by \$1.3 million (11 per cent) to \$12.5 million in 2005-06. Total revenue increased by \$3.7 million (3.6 per cent), the net effect of an increase in revenue from service and usage charges offset by a fall in developer contributions. Total expenses increased by \$2.4 million (2.7 per cent) because of growth in administration and direct operating expenses.

Dividend payments are based on a share of profits determined through consultation between the Board, the relevant portfolio minister and the Treasurer. No dividends were provided for in 2005-06. Barwon Water recorded an income tax-equivalent expense of \$3.8 million in 2005-06.

Barwon Water is reimbursed for the value of concessions provided to pensioners and others, and for the administration of the community service obligation (CSO) schemes. CSO payments totalled \$5.0 million in 2005-06, accounting for 4.8 per cent of total revenue. These payments were not separately recorded in Barwon Water's income statement but were acknowledged in its annual report commentary.

BARWON REGIONAL WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	981	981	992
Total revenue	\$m	103	102	106
Profitability				
Operating profit before tax	\$'000	11 236	11 236	12 506
Operating sales margin	%	14.3	14.5	15.6
Cost recovery	%	116.7	116.7	118.1
Return on assets	%	1.5	1.5	1.7
Return on equity	%	0.9	0.9	1.0
Financial management				
Debt to equity	%	6.3	6.4	6.9
Debt to total assets	%	5.7	5.7	6.2
Total liabilities to equity	%	11.1	12.7	13.0
Interest cover	times	4.0	4.0	4.0
Current ratio	%	91.0	61.3	56.3
Leverage ratio	%	111.1	112.7	113.0
Payments to and from government				
Dividends	\$'000	1 014	1 014	—
Dividend to equity ratio	%	0.1	0.1	—
Dividend payout ratio	%	13.0	13.0	—
Income tax expense	\$'000	3 461	3 461	3 832
CSO funding ^c	\$'000	4 691	4 694	5 035

^a The Barwon Regional Water Authority (Barwon Water) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Barwon Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Barwon Water does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. — Zero or rounded to zero.

The Coliban Regional Water Authority (Coliban Water) was established on 1 July 1992 under the *Water Act 1989*. It provides water and wastewater services to around 65 000 urban and rural customers across an area of 16 550 km in Northern Central Victoria. Coliban Water has two Build Own Operate Transfer (BOOT) schemes to provide water services in some regional areas.¹

The Essential Services Commission became responsible for regulating the pricing and services of Coliban Water on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 4.4 per cent above the inflation rate in each year until 30 June 2008.

Total assets decreased by \$13.2 million (1.5 per cent) to \$841 million in 2005-06, primarily attributable to a decrease in current investments. Total liabilities remained largely unchanged at \$119 million.

Coliban Water reported an operating loss before tax of \$12.4 million in 2005-06. Total revenue remained stable at \$50.3 million and total expenses increased by 3.6 per cent to \$62.8 million because of growth in administration expenses and finance charges relating to the BOOT schemes.

Coliban Water is subject to dividend and tax-equivalent payments. No dividends were paid and no income tax-equivalent expenses were recorded in 2005-06, as Coliban Water declared an operating loss.²

The Victorian Government reimbursed Coliban Water \$2.9 million for concessions provided to pensioners and rebates to non-profit organisations in 2005-06. This represents 5.7 per cent of total revenue. These payments were not separately recorded in Coliban Water's income statement but were acknowledged in its annual report commentary.

¹ Coliban Water has been engaged in three BOOT schemes over the last ten years. Two BOOT schemes remain in operation. One was signed with Bendigo Water Services Pty Ltd in 1999 for the provision of water treatment services in Bendigo, Castlemaine and Kyneton. The other was signed with ETE Coliban Pty Ltd in 2002 for the provision of water reclamation and reuse services for Echuca and Rochester. Contract payments comprise fixed and variable components made by Coliban Water over the 25 year contract period. A 1998 contract deed with Castlemaine Wastewater Treatment Pty Ltd (CWWT) was bought by Coliban Water on 5 August 2005 because the parent company of CWWT, Henry Walker Eltin, went into receivership in that year. The assets were purchased for \$1 million and are now included in Coliban Water's infrastructure asset base.

² Coliban Water states in its annual report that it 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 REGIONAL WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^{a,c}
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	753	855	841
Total revenue	\$m	50	50	50
Profitability				
Operating profit before tax	\$'000	-6 536	-8 981	-12 426
Operating sales margin	%	-18.9	-8.5	-11.6
Cost recovery	%	84.1	92.1	89.6
Return on assets	%	-0.9	-0.2	-0.5
Return on equity	%	-0.9	-1.2	-1.7
Financial management				
Debt to equity	%	—	14.6	14.6
Debt to total assets	%	—	12.6	12.5
Total liabilities to equity	%	1.7	16.3	16.5
Interest cover	times	..	-0.2	-0.5
Current ratio	%	399.3	199.4	110.7
Leverage ratio	%	101.7	116.3	116.5
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^d	\$'000	2 616	2 616	2 881

^a The Coliban Regional Water Authority (Coliban Water) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Coliban Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Under AIFRS Coliban Water includes its Build Own Operate Transfer schemes as financial leases. This affects its gross interest expense and level of debt, which are used to calculate a number of performance indicators (chapter 1). ^d Coliban Water does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. .. Not applicable. — Zero or rounded to zero.

The Goulburn Valley Regional Water Authority (GVW) was established in March 1994 under the *Water Act 1989*. It provides water and wastewater services to a population of more than 118 000 in Northern Central Victoria, including the major towns of Seymour, Euroa and Shepparton.

The Essential Services Commission became responsible for regulating the pricing and services of GVW on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 4.7 per cent above the inflation rate in each year until 30 June 2008.

Total assets remained relatively stable at \$483 million in 2005-06. Total liabilities increased by 6.3 per cent to \$57.9 million, partly because of growth in deferred tax liabilities.

Operating profit before tax fell by 91 per cent to \$463 000 in 2005-06. Total expenses increased by 4.6 per cent to \$44.9 million and total revenue fell by 6.0 per cent to \$45.3 million.¹ The decrease in revenue was mainly attributable to a decline in developer and land owner contributions.

GVW is subject to dividend and tax-equivalent payments. The Treasurer determined that no dividend was payable in 2005-06. GVW recorded a tax-equivalent expense of \$142 000 in 2005-06, less than one-tenth of that recorded in 2004-05.

GVW is reimbursed for the value of concessions provided to pensioners and others, and for the administration of the concession schemes. Community service obligation payments increased by 11 per cent to \$2.2 million in 2005-06, representing approximately 4.7 per cent of total revenue. These payments were not separately recorded in GVW's income statement but were acknowledged in its annual report commentary.

¹ Small percentage changes in revenue and expenses have a large impact on the change in profits because the level of profits is relatively small (\$483 000 in 2005-06 and \$5.3 million in 2004-05).

GOULBURN VALLEY REGIONAL WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	479	486	483
Total revenue	\$m	49	48	45
<i>Profitability</i>				
Operating profit before tax	\$'000	5 320	5 320	463
Operating sales margin	%	11.9	12.1	3.6
Cost recovery	%	112.8	113.1	103.8
Return on assets	%	1.4	1.3	0.5
Return on equity	%	1.2	0.9	0.1
<i>Financial management</i>				
Debt to equity	%	6.3	6.5	6.4
Debt to total assets	%	5.8	5.7	5.6
Total liabilities to equity	%	8.3	12.6	13.6
Interest cover	times	5.5	5.5	1.2
Current ratio	%	107.8	95.0	165.5
Leverage ratio	%	108.3	112.6	113.6
<i>Payments to and from government</i>				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	1 598	142
CSO funding ^c	\$'000	1 941	1 941	2 153

^a The Goulburn Valley Regional Water Authority (GVW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for GVW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

^c GVW does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. — Zero or rounded to zero.

The Central Gippsland Water Authority (Gippsland Water) was established in 1994 and operates under the *Water Act 1989*. It provides water and wastewater services to approximately 130 000 people in 41 towns in the Central Gippsland area.

The Essential Services Commission became responsible for regulating the pricing and services of Gippsland Water on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 4.7 per cent above the inflation rate in each year until 30 June 2008.

Total assets grew by \$57.6 million (12 per cent) to \$556 million in 2005-06. This was primarily due to increases in cash held and capital works-in-progress relating to major infrastructure investment. Gippsland Water borrowed for the first time in 2005-06 to finance part of this infrastructure development (previously, capital development was funded entirely from retained earnings and government grants). As a result, total liabilities increased by \$12.7 million (97 per cent) to \$25.7 million and debt to equity and debt to total assets ratios increased to 2.6 per cent and 2.7 per cent respectively.

Gippsland Water's operating profit before tax decreased by \$1.2 million (14 per cent) to \$7.7 million in 2005-06. Total expenses increased by \$3.1 million (5.6 per cent) because of a combination of increased environmental contribution payments, supplier costs and employee benefits. Total revenue increased by \$1.9 million (3.0 per cent), partly attributable to a \$1.3 million government contribution for non-operating activities. Sales revenue from domestic customers and businesses accounted for 46 per cent and 32 per cent of total revenue respectively in 2005-06.

Gippsland Water did not make tax-equivalent payments in 2005-06 because it did not generate a taxable income.¹ No dividend was paid in 2005-06.

The State Government reimbursed Gippsland Water \$2.7 million in 2005-06 for concessions including pensioner rebate and health care card schemes, rebates for non-profit organisations and other programs. This represented 4.1 per cent of total revenue. These payments were not separately recorded in Gippsland Water's income statement but were acknowledged in its annual report commentary.

¹ Gippsland Water noted in its annual report that it considers it unlikely that operating profits will be sufficient in the foreseeable future to offset income tax deductions associated with the tax depreciation of assets. This is due to higher (accelerated) tax depreciation rates compared to accounting depreciation rates.

CENTRAL GIPPSLAND WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	498	498	556
Total revenue	\$m	65	64	66
Profitability				
Operating profit before tax	\$'000	8 922	8 909	7 706
Operating sales margin	%	12.3	12.5	10.8
Cost recovery	%	114.1	114.3	109.9
Return on assets	%	1.8	1.8	1.5
Return on equity	%	1.8	1.8	1.5
Financial management				
Debt to equity ^c	%	—	—	2.6
Debt to total assets ^c	%	—	—	2.7
Total liabilities to equity	%	2.6	2.7	4.8
Interest cover ^c	times	..	..	77.3
Current ratio	%	281.5	229.3	358.6
Leverage ratio	%	102.6	102.7	104.8
Payments to and from government				
Dividends	\$'000	—	—	— ^d
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^e	\$'000	2 384	2 384	2 709

^a The Central Gippsland Water Authority (Gippsland Water) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Gippsland Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Gippsland Water operated debt free prior to 2005-06, with capital expenditure funded from retained earnings and government grants. ^d The dividend relating to the 2005-06 financial year was not determined by 30 June 2006 but the Board's preliminary estimate of the dividend was \$220,000. ^e Gippsland Water does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. .. Not applicable. — Zero or rounded to zero.

The Central Highlands Water Authority (CHW) was established in 1994 and operates under the *Water Act 1989*. It provides water and wastewater services to a population of 113 000 in Ballarat and surrounding areas.

CHW entered into a Build Own Operate and Transfer (BOOT) agreement with Thames Water Ballarat in April 1999. CHW entered into a second BOOT agreement with Thames Water in November 2003 for water treatment facilities for Beaufort, Blackwood, Forest Hill and Clunes. The contracts require CHW to pay an annual charge comprising both fixed and variable components for 20 years, after which ownership of the water facilities will be transferred to CHW.¹

The Essential Services Commission became responsible for regulating the pricing and services of CHW on 1 January 2004. Its first price determination, which became effective from 1 July 2005, provided for price increases of 4.8 per cent above the inflation rate in each year until 30 June 2008.

Total assets remained largely unchanged at \$619 million and total liabilities increased by 2.8 per cent to \$74.7 million in 2005-06. Water and wastewater infrastructure represented around 80 per cent of CHW's assets.

CHW reported an operating loss before tax of \$3.2 million in 2005-06, compared with a loss of \$2.5 million in 2004-05. Total revenue fell 11 per cent to \$44.4 million largely as a result of reduced developer charges and a fall in the value of resources received free of charge or for nominal cost. CHW's annual report noted that drought again affected its performance in 2005-06 reducing water demand. Despite this, revenue from volume charges increased by \$1.2 million. Total expenses decreased by 9.3 per cent to \$47.6 million. This was because of lower net losses on the sale of assets compared to 2004-05.

CHW did not make tax-equivalent payments in 2005-06 because of its poor operating performance. No dividend was paid in 2005-06.

CHW receives community service obligation payments for the provision of concessions to pensioners and others. These payments totalled \$2.7 million in 2005-06, accounting for 6.0 per cent of total revenue. These payments were not separately recorded in CHW's income statement but were acknowledged in its annual report commentary.

¹ As at 30 June 2005, the net book values of the BOOT assets and liabilities were \$23.5 million and \$26.1 million respectively.

CENTRAL HIGHLANDS WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	579	619	619
Total revenue	\$m	52	50	44
Profitability				
Operating profit before tax	\$'000	654	-2 500	-3 164
Operating sales margin	%	10.6	4.3	7.1
Cost recovery	%	111.3	103.9	107.5
Return on assets	%	1.1	0.5	0.7
Return on equity	%	0.1	-0.5	-0.9
Financial management				
Debt to equity	%	0.1	7.2	7.1
Debt to total assets	%	0.1	6.3	6.2
Total liabilities to equity	%	2.5	13.3	13.7
Interest cover	times	1.1	0.6	0.6
Current ratio	%	460.6	347.1	308.9
Leverage ratio	%	102.5	113.3	113.7
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	256	—	1 949
CSO funding ^c	\$'000	2 251	2 251	2 687

^a The Central Highlands Water Authority (CHW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for CHW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

^c CHW does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. — Zero or rounded to zero.

The 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 9000 customers in three districts and administers over 8400 licences. It manages the taking and use of water from rivers, streams and groundwater sources in Southern Victoria. It also manages several water storage dams that supply irrigators, urban water authorities and several power generators.

The Southern Rural Water Board sets water charges subject to ministerial approval, using the renewals annuity concept (box 6.1) to provide adequate funding to maintain the condition of the network of channels, pipelines and structures.¹

Southern Rural Water's total assets increased by 1.1 per cent to \$448 million and total liabilities increased by 5.2 per cent to \$5.7 million in 2005-06.

Southern Rural Water recorded a pre-tax operating loss of \$1.1 million in 2005-06, 3.9 per cent greater than in 2004-05. Total revenue increased by 25 per cent to \$25.4 million because of increases in revenue from service charges, chargeable works, and because of the sale of new water entitlements. Total expenses increased by 24 per cent to \$26.5 million, primarily resulting from a \$4.1 million increase in maintenance costs. From 2005-06, Southern Rural Water was required to pay an environmental contribution of \$200 000 to fund initiatives that encourage sustainable water management.

Southern Rural Water did not make tax-equivalent payments in 2005-06 because of its poor operating performance. No dividend was provided for in 2005-06.

Southern Rural Water stated in its annual report that the value of community service obligations (CSOs) in 2005-06 was \$3.9 million, for the provision of concession to pensioners. In addition, it received grants from the Victorian Government for programs including salinity projects, state water assessment and groundwater (\$600 000).² These payments were not separately recorded in Southern Rural Water's income statement but were acknowledged in its annual report commentary.

¹ The Essential Services Commission became responsible for regulating the pricing and service standards of Southern Rural Water on 1 January 2004. Its first price determination took effect from 1 July 2006.

² Prior to 1 July 2005 Southern Rural Water charged regional urban water providers in the area a Rate of Return on the value of headworks assets used in storing their bulk water entitlements. This revenue was used to fund a range of community programs and government priorities. A new CSO pricing regime was established on 1 July 2005, which increased government funding, recovered costs from entitlement holders in specific areas and from other water authorities.

GIPPSLAND AND SOUTHERN RURAL WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	443	443	448
Total revenue	\$m	21	20	25
Profitability				
Operating profit before tax	\$'000	-1 437	-1 079	-1 121
Operating sales margin	%	-8.1	-6.5	-6.4
Cost recovery	%	82.9	84.0	91.9
Return on assets	%	-0.3	- 0.2	-0.3
Return on equity	%	-0.3	- 0.2	-0.3
Financial management				
Debt to equity ^c	%	—	—	—
Debt to total assets ^c	%	—	—	—
Total liabilities to equity	%	1.2	1.2	1.3
Interest cover ^c	times	..	..	..
Current ratio	%	269.8	215.8	265.9
Leverage ratio	%	101.2	101.2	101.3
Payments to and from government				
Dividends	\$'000	380	380	— ^d
Dividend to equity ratio	%	0.1	0.1	—
Dividend payout ratio	%	-26.4	-35.2	—
Income tax expense	\$'000	—	—	—
CSO funding ^e	\$'000	2 428	2 428	3 853

^a The Gippsland and Southern Rural Water Authority (Southern Rural Water) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Southern Rural Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Southern Rural Water operates debt free, with capital expenditure funded from retained earnings and government grants. ^d The Victorian Government White Paper *Securing our Water Future Together* states at item 6.6 that the government will forgo its dividend entitlement for the 2005-06 financial year. ^e Southern Rural Water does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. .. Not applicable. — Zero or rounded to zero.

The Lower Murray Urban and Rural Water Authority (LMW) was established on 1 July 2004 under the *Water Act 1989*. LMW was formed by the merger of the Lower Murray Regional Water Authority's urban water and wastewater business with the Sunraysia Rural Water Authority's rural water business.

LMW provides urban water and wastewater services, river quality water for irrigation, stock and gardens, and the collection and disposal of irrigation drainage across its region in North-Western Victoria. The LMW Board set water charges in 2005-06, subject to ministerial approval. Rural water charges were calculated using the renewals annuity concept (box 6.1).¹

Total assets increased by \$6.1 million (1.3 per cent) to \$478 million in 2005-06. This comprised an increase in cash assets of \$8.9 million and a decrease in the value of property, plant and equipment because of depreciation. Total liabilities remained largely unchanged at \$66.8 million. No new loans were taken out in 2005-06.

LMW reported an operating profit before tax of \$53 000 in 2005-06, a \$2.5 million improvement in operating performance on 2004-05. Total revenue grew by \$4.8 million (12 per cent), primarily because of increased operating revenue and capital contributions. Total expenses increased by \$2.3 million (5.6 per cent) because of increased maintenance and employee expenses.

LMW reported no declaration of dividends in 2005-06. The dividend relating to the operating performance in 2005-06 was not finalised by the reporting date but the Board's expectation was that a dividend would not be paid.

LMW recorded an income tax-equivalent expense of \$81 000 in 2005-06. The high tax-equivalent expense relative to operating profit was because of the tax effect of depreciation and other items of income and expenditure.

LMW received \$1.2 million for community service obligations (CSOs) in 2005-06, relating to the provision of concessions to pensioners and the Utility Relief Grants Scheme. CSO payments accounted for 2.7 per cent of total revenue.

¹ The Essential Services Commission became responsible for regulating the pricing and service standards of LMW on 1 January 2004. Its first price determination took effect from 1 July 2006.

LOWER MURRAY WATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	468	472	478
Total revenue	\$m	39	39	43
Profitability				
Operating profit before tax	\$'000	-2 653	-2 426	53
Operating sales margin	%	-10.7	-10.1	-3.4
Cost recovery	%	90.0	90.5	96.7
Return on assets	%	-0.6	-0.5	–
Return on equity	%	-1.0	-1.0	–
Financial management				
Debt to equity	%	0.1	0.1	0.1
Debt to total assets	%	0.1	0.1	0.1
Total liabilities to equity	%	3.1	16.5	16.2
Interest cover	times	-84.6	-77.3	2.8
Current ratio	%	513.3	392.6	545.2
Leverage ratio	%	103.1	116.5	116.2
Payments to and from government				
Dividends ^c	\$'000	–	–	–
Dividend to equity ratio	%	–	–	–
Dividend payout ratio	%	–	–	–
Income tax expense	\$'000	1 791	1 828	81
CSO funding	\$'000	1 195	1 195	1 157

^a The Lower Murray Urban and Rural Water Authority (LMW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for LMW. ^b LMW was formed on 1 July 2004 when the Sunraysia Rural Water Authority (SRW) and the Lower Murray Regional Water Authority were merged. Data for SRW prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c LMW recorded no provision or payment of dividends in its equity statements. However, it reported dividend payments of \$88 000 in 2004-05 and \$80 000 in 2005-06 in its cash flow statements. – Zero or rounded to zero.

The Grampians Wimmera Mallee Rural Water Authority (GWMWater) was established on 1 July 2004 under the *Water Act 1989*. GWMWater was formed following the merger of Grampians Water and Wimmera Mallee Water and assumed all the functions previously undertaken by these entities. GWMWater provides water and wastewater services to urban and some rural customers in Central Western Victoria, serving approximately 70 000 people. GWMWater is also responsible for the Wimmera Mallee Pipeline Project, which commenced construction in September 2005.

The GWMWater Board set water charges in 2005-06, subject to ministerial approval. Rural water charges were calculated using the renewals annuity concept (box 6.1).¹

Total assets remained largely unchanged at around \$639 million in 2005-06. Total liabilities increased by \$2.5 million (27 per cent) to \$11.8 million, because of an increase in current liabilities, in particular payables.

GWMWater reported an operating loss of \$7.8 million, 11 per cent lower than in 2004-05. GWMWater attributed its operating position over the last two years to the impact of drought conditions. However, despite the effects of the drought, total revenue increased by \$2.3 million (6.6 per cent) to \$37.2 million, primarily due to increased sales revenue. While total expenses increased by \$3.0 million (7.2 per cent) to \$45.0 million, operating expenditure generally decreased as a result of the realisation of operational efficiencies from the merger.

GWMWater is subject to dividend and tax-equivalent payments. No dividends were distributed or income tax-equivalent expenses recorded in 2005-06, reflecting GWMWater's financial position.

GWMWater received \$1.8 million in community service obligation payments in 2005-06, relating to the provision of concessions to pensioners. This represented 4.9 per cent of total revenue. These payments were not separately recorded in GWMWater's income statement but were acknowledged in its annual report commentary.

¹ The Essential Services Commission became responsible for regulating the pricing and service standards of GWMWater on 1 January 2004. Its first price determination took effect from 1 July 2006.

GRAMPIANS WIMMERA MALLEE WATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	638	638	639
Total revenue	\$m	37	35	37
Profitability				
Operating profit before tax	\$'000	-7 168	-7 040	-7 786
Operating sales margin	%	-20.6	-21.2	-21.3
Cost recovery	%	81.1	80.6	80.3
Return on assets	%	-1.1	-1.1	-1.2
Return on equity	%	-1.1	-1.1	-1.2
Financial management				
Debt to equity	%	0.5	0.5	0.5
Debt to total assets	%	0.5	0.5	0.5
Total liabilities to equity	%	1.5	1.5	1.9
Interest cover	times	-42.4	-41.7	-35.7
Current ratio	%	229.1	145.8	145.4
Leverage ratio	%	101.5	101.5	101.9
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^c	\$'000	1 699	1 699	1 831

^a The Grampians Wimmera Mallee Rural Water Authority (GWMWater) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for GWMWater. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c GWMWater does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. — Zero or rounded to zero.

The 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.

The GMW Board sets water charges, subject to ministerial approval, using the renewals annuity concept (box 6.1). Under this concept, charges provide adequate funds to maintain the condition of the required network of channels, pipelines and structures.¹

Total assets increased by \$12.4 million (0.6 per cent) to approximately \$2.0 billion in 2005-06. This comprised a decrease in current assets, partly because of reduced cash holdings, and an increase in non-current infrastructure assets. Total liabilities decreased by \$2.5 million (4.2 per cent) because of a reduction in trade payables and other accruals.

GMW reported an operating loss before tax of \$4.2 million in 2005-06, a \$7.2 million improvement compared with 2004-05. Total revenue increased \$9.3 million (8.4 per cent) because of small increases in most revenue sources. Total expenses increased by \$2.1 million (1.7 per cent) in 2005-06, primarily because of increased maintenance expenses on irrigation and drainage infrastructure.

GMW is subject to dividend and tax-equivalent payments. However, due to its operating position, neither were paid in 2005-06.

GMW received \$69 000 in community service obligation payments in 2005-06 for the provision of concessions to pensioners. This was 31 per cent greater than payments received in 2004-05. GMW also received \$10.9 million in government grants for programs including the salinity program, the national landcare program and the water saving program. These payments were not separately recorded in GMW's income statement but were acknowledged in its annual report commentary.

¹ The Essential Services Commission became responsible for regulating the pricing and service standards of GMW on 1 January 2004. Its first price determination took effect from 1 July 2006.

GOULBURN–MURRAY RURAL WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 938	1 938	1 950
Total revenue	\$m	111	111	120
Profitability				
Operating profit before tax	\$'000	-11 410	-11 410	-4 215
Operating sales margin	%	-10.1	-10.1	-4.3
Cost recovery	%	83.6	83.5	87.0
Return on assets	%	-0.5	-0.5	-0.2
Return on equity	%	-0.6	-0.6	-0.2
Financial management				
Debt to equity	%	0.8	0.8	0.7
Debt to total assets	%	0.8	0.8	0.7
Total liabilities to equity	%	3.1	3.1	3.0
Interest cover	times	-8.6	-8.6	-2.7
Current ratio	%	157.0	128.5	108.5
Leverage ratio	%	103.1	103.1	103.0
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^c	\$'000	53	53	69

^a The Goulburn–Murray Rural Water Authority (GMW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for GMW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

^c GMW does not report community service obligation payments separately in the income statement. However, they are acknowledged in its annual report commentary. — Zero or rounded to zero.

SunWater was established under the *Government Owned Corporations Act 1993* on 1 October 2000, assuming the roles and responsibilities of the former State Water Projects. SunWater owns and operates bulk water storage and distribution infrastructure and supplies irrigators, industrial and urban bulk water customers.

Charges for rural customers were determined by SunWater's shareholding ministers. A price direction in October 2000 set a price path of between five and seven years for most of SunWater's service areas.¹

Total assets increased by \$152 million (36 per cent) to \$577 million in 2005-06. This growth primarily resulted from SunWater's acquisition of Burnett Water on 16 December 2005. The acquisition included additional water infrastructure, assets under construction, and \$56.4 million worth of water allocations. Total liabilities increased by \$101 million (179 per cent) because of increased borrowings and the inclusion of Burnett Water's liabilities.

SunWater reported an operating loss before tax of \$71 000 in 2005-06, an \$18.6 million improvement since 2004-05. Total revenue increased by \$13.0 million to \$130 million because of an increase in government grants and the fair value above cost obtained from the acquisition of Burnett Water. Total expenses decreased by \$5.6 million to \$130 million in part because of a reversal of a previous provision for doubtful debts.

SunWater is subject to dividend and tax-equivalent payments. Distributed dividends totalled \$3.0 million in 2005-06, eight times the distribution in 2004-05 (\$373 000) when no provision was made for a final dividend relating to the 2003-04 financial year.² SunWater recorded a tax credit of \$1.4 million in 2005-06.

SunWater received \$6.6 million in community service obligation (CSO) funding in 2005-06. CSO funding represented 5.1 per cent of total revenue.

¹ The 2004-05 pricing arrangements were extended for one year. The next five-year irrigation price path is effective from 1 July 2006.

² Total dividends include an interim dividend paid during the current financial year and a final dividend from the previous financial year.

SUNWATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	458	424	577
Total revenue	\$m	151	117	130
Profitability				
Operating profit before tax	\$'000	49 894	-18 671	-71
Operating sales margin	%	31.7	-19.3	0.2
Cost recovery	%	146.4	83.8	95.9
Return on assets	%	11.0	-4.3	0.5
Return on equity	%	11.5	-3.2	0.3
Financial management				
Debt to equity	%	1.9	2.0	22.0
Debt to total assets	%	1.6	1.8	18.5
Total liabilities to equity	%	14.0	15.3	37.5
Interest cover	times	94.3	-33.9	1.0
Current ratio	%	301.1	281.4	122.8
Leverage ratio	%	114.0	115.3	137.5
Payments to and from government				
Dividends	\$'000	373 ^c	373 ^c	3 003
Dividend to equity ratio	%	0.1	0.1	0.8
Dividend payout ratio	%	0.8	-3.2	231.9
Income tax expense	\$'000	3 729	-7 048	-1 366
CSO funding	\$'000	6 097	6 097	6 556

^a SunWater commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for SunWater. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c This dividend was not include the final dividend for 2004-05, as it was declared after the reporting date.

The Water Corporation was established on 1 January 1996 under the *Water Corporation Act 1995* and operates under a 25 year licence issued by the Economic Regulation Authority. It provides water and wastewater services to almost 2 million people across urban and regional WA, covering an area of 2.5 million square kilometres.

The WA Government is responsible for setting water prices. Prices increased by the consumer price index in 2005-06, as occurred in the previous year.

The Water Corporation's total assets grew by \$525 million (5.2 per cent) in 2005-06, primarily from investments in capital infrastructure, including the Perth Seawater Desalination Project. Total liabilities increased by \$413 million (25 per cent) with increased borrowings associated with the infrastructure expansion. This increased total debt by 38 per cent to \$1.5 billion.

Operating profit before tax increased by 12 per cent to \$676 million in 2005-06. Total revenue increased by \$106 million (8.1 per cent) primarily because of an increase in community service obligation (CSO) payments and developer contributions. Total expenses increased by \$31.5 million (4.4 per cent), in part because of increased labour expenses.

The Water Corporation is subject to dividend and tax-equivalent payments. It distributed \$362 million in dividends and recorded an income tax-equivalent expense of \$202 million in 2005-06, an increase of 18 per cent and 12 per cent respectively.

The Water Corporation receives CSO payments for costs incurred in providing country services, pensioner concessions and a program to eliminate septic tanks to protect groundwater, waterways and public health. CSO payments increased by \$51.6 million (18 per cent) to total \$340 million in 2005-06. This accounted for 24 per cent of the Water Corporation's total revenue.

WATER CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	10 094	10 054	10 579
Total revenue	\$m	1 326	1 315	1 421
Profitability				
Operating profit before tax	\$'000	605 034	601 274	675 991
Operating sales margin	%	49.6	50.0	51.6
Cost recovery	%	198.3	198.9	204.8
Return on assets	%	6.5	6.6	7.1
Return on equity	%	5.0	5.0	5.6
Financial management				
Debt to equity	%	12.7	12.8	17.4
Debt to total assets	%	10.6	10.7	14.3
Total liabilities to equity	%	19.4	19.6	24.2
Interest cover	times	11.8	11.0	12.5
Current ratio	%	26.3	29.0	49.7
Leverage ratio	%	119.4	119.6	124.2
Payments to and from government				
Dividends	\$'000	311 477 ^c	306 627 ^c	362 366
Dividend to equity ratio	%	3.6	3.6	4.3
Dividend payout ratio	%	72.7	72.8	76.5
Income tax expense	\$'000	183 531	179 879	202 160
CSO funding	\$'000	288 253	288 253	339 821

^a The Water Corporation commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the Water Corporation. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The adoption of AIFRS changed how dividends are recorded resulting in different dividend values for 2004-05 on an AIFRS and pre-AIFRS basis.

South Australian 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 approximately 1.4 million customers in metropolitan and country areas of SA.¹

Charges for water and sewerage services are set by the Minister for Administrative Services after consultation with SA Water. Urban water tariffs increased by 3 per cent on average in 2005-06.

Total assets increased by \$180 million (2.6 per cent) in 2005-06, mainly because of additions to infrastructure, plant and equipment. Total liabilities increased by \$90.9 million (4.7 per cent) because of an increase in current and deferred tax liabilities and the value of finance leases relating to Build Own Operate Transfer agreements.

SA Water's operating profit before tax increased by \$48.0 million (17 per cent) to \$327 million in 2005-06. This resulted from a \$48.7 million (6.2 per cent) increase in total revenue because of growth in revenue from rates and charges and increased community service obligation (CSO) payments. Total expenses remained unchanged at \$504 million.

SA Water is subject to dividend and tax-equivalent payments. In 2005-06, the provision of dividends increased by 40 per cent to \$217 million. An income tax-equivalent expense of \$98.0 million was recorded in 2005-06, an increase of 19 per cent.

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. CSO payments totalled \$152 million in 2005-06 — 47 per cent more than in 2004-05.²

¹ SA Water directly operates and maintains its non-metropolitan water assets. However, it contracts United Water to maintain and operate its metropolitan water and waste water assets.

² SA Water became subject to the SA Government's Public Non-Financial Corporations Ownership Framework on 1 July 2005. One of aims of this framework is to provide transparent and appropriate funding for CSOs, increasing payments in 2005-06. It also aims to ensure debt is maintained at a commercially viable level and specifies how dividend payments should be determined.

SOUTH AUSTRALIAN WATER CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	7 032	7 044	7 224
Total revenue	\$m	776	783	831
Profitability				
Operating profit before tax	\$'000	288 205	278 894	326 901
Operating sales margin	%	47.6	46.8	49.5
Cost recovery	%	190.7	187.9	198.0
Return on assets	%	5.2	5.2	5.8
Return on equity	%	3.6	3.9	4.5
Financial management				
Debt to equity	%	23.4	25.4	25.3
Debt to total assets	%	18.4	18.4	18.4
Total liabilities to equity	%	27.0	38.2	39.3
Interest cover	times	4.6	4.2	4.9
Current ratio	%	72.8	94.9	48.4
Leverage ratio	%	127.0	138.2	139.3
Payments to and from government				
Dividends	\$'000	155 189	155 189	217 455
Dividend to equity ratio	%	3.0	3.0	4.2
Dividend payout ratio	%	83.9	79.1	95.0
Income tax expense	\$'000	91 337	82 597	97 973
CSO funding	\$'000	103 440	103 440	152 180

^a South Australian Water Corporation (SA Water) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for SA Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

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 and provides water to some irrigators and commercial operators in outlying rural areas.

Maximum charges for bulk water are determined by the Minister for Local Government on recommendations by the Government Prices Oversight Commission.² Water charges increased by the consumer price index (3.3 per cent) in 2005-06.

Hobart Water's assets increased by \$3.9 million (2.0 per cent) to \$193 million in 2005-06. Total liabilities increased by \$3.2 million (6.4 per cent) to \$53.1 million from a combination of increased debt and deferred tax liabilities. The current ratio increase by 15.5 percentage points to 129.6 per cent because of the increase in current assets.

Hobart Water's operating profit before tax increased by 37 per cent to \$5.9 million. Total revenue increased by 10 per cent to \$27.7 million, primarily because of a positive change in the fair value of financial instruments, gains in the value of the defined-benefit superannuation scheme and higher income from rental and consulting services. Total expenses increased by 5.0 per cent to \$21.8 million partly because of higher employee expenses.

Hobart Water's distributed dividends totalling \$5.0 million, a 79 per cent increase since 2004-05. It recorded an income tax-equivalent expense of \$1.8 million, an increase of 34 per cent, because of the improved operating result.

Hobart Water did not specify the value of community service obligation (CSO) payments in its annual report. However, it reported a CSO administration expense of \$279 000 for 2004-05 and 2005-06.

¹ The councils that comprise the Joint Authority are Brighton, Clarence City, Derwent Valley, Glenorchy City, Hobart City, Kingborough, Sorell and Southern Midlands.

² Under the *Government Prices Oversight Act 1995*, the recommendations may take the form of maximum revenues, maximum prices, pricing principles or a combination of these.

HOBART REGIONAL WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	191	189	193
Total revenue	\$m	34	25	28
Profitability				
Operating profit before tax	\$'000	13 465	4 319	5 907
Operating sales margin	%	47.9	27.6	30.5
Cost recovery	%	192.1	138.2	144.0
Return on assets	%	9.2	4.5	5.2
Return on equity	%	8.2	2.1	3.0
Financial management				
Debt to equity	%	22.8	23.8	23.7
Debt to total assets	%	17.4	17.5	17.3
Total liabilities to equity	%	31.2	35.7	37.8
Interest cover	times	4.2	2.0	2.5
Current ratio	%	114.1	114.1	129.6
Leverage ratio	%	131.2	135.7	137.8
Payments to and from government				
Dividends	\$'000	2 800	2 800	5 000
Dividend to equity ratio	%	1.9	2.0	3.6
Dividend payout ratio	%	23.4	93.5	120.9
Income tax expense	\$'000	1 485	1 324	1 773
CSO funding ^c	\$'000	na	na	na

^a Hobart Water commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Hobart Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Community service obligation (CSO) payments were not specified in Hobart Water's annual reports. However, it did report a CSO administration expense of \$252 000 for 2004-05 and \$279 000 for 2005-06. **na** Not available.

Cradle Coast Water (CCW) was established as a Joint Authority on 10 August 1999 under the *Local Government Act 1993*. CCW collects, treats and supplies bulk drinking water to its joint owning councils — Circular Head, Waratah–Wynyard, Central Coast, Devonport, Latrobe and Kentish.

Maximum charges for bulk water are determined by the Minister for Local Government on recommendations by the Government Prices Oversight Commission.¹ The average price of bulk water increased by 13 per cent in 2005-06 as fixed charges remained unchanged with a substantial decrease in water usage.

CCW's total assets increased by \$29.0 million (41 per cent) to \$98.9 million in 2005-06, primarily because of a \$28.5 million positive revaluation of water infrastructure. Total liabilities grew \$7.9 million (33 per cent). This was partly attributable to an increase in deferred tax liabilities resulting from the revaluation of assets. These changes caused the debt to equity and debt to total asset ratios to fall.

Operating profit before tax decreased by \$96 000 (7.1 per cent) to \$1.2 million in 2005-06. This was attributable to a small decrease in total revenue — down 1.1 per cent to \$8.8 million because of a reduction in revenue from external contracts. Sales revenue remained stable despite the increase in the average price of water. Total expenses remained unchanged at \$7.6 million.

CCW is subject to dividend and tax-equivalent payments. It distributed \$774 000 in dividends in 2005-06. It recorded an income tax-equivalent expense of around \$374 000 in 2005-06, a decrease of 7.2 per cent, consistent with the weaker profit result.

CCW has not received community service obligation payments.

¹ Under the *Government Prices Oversight Act 1995*, the recommendations can take the form of maximum revenues, maximum prices, pricing principles, or a combination of these.

CRADLE COAST WATER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	65	70	99
Total revenue	\$m	8.9	8.9	8.8
<i>Profitability</i>				
Operating profit before tax	\$'000	1 489	1 344	1 248
Operating sales margin	%	31.3	29.7	29.2
Cost recovery	%	145.6	142.3	141.2
Return on assets	%	4.3	3.8	3.1
Return on equity	%	3.0	2.0	1.5
<i>Financial management</i>				
Debt to equity	%	51.5	46.2	32.6
Debt to total assets	%	32.8	30.5	25.9
Total liabilities to equity	%	56.9	51.8	47.3
Interest cover	times	2.1	2.0	1.9
Current ratio	%	48.9	49.5	127.1
Leverage ratio	%	156.9	151.8	147.3
<i>Payments to and from government</i>				
Dividends	\$'000	629	629	744
Dividend to equity ratio	%	1.5	1.4	1.3
Dividend payout ratio	%	50.4	66.8	85.1
Income tax expense	\$'000	241	403	374
CSO funding	\$'000	..	..	..

^a Cradle Coast Water (CCW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for CCW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

The Esk Water Authority, trading as Esk Water, was established as a Joint Authority under the *Local Government Act 1993*. 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 has a two-part tariff structure, which was implemented in 2001-02. Both the volumetric and fixed water charges were increased by 3.3 per cent in 2005-06 in accordance with the consumer price index.

Total assets decreased by 7.6 per cent to \$118 million, primarily because of a negative revaluation of systems infrastructure. Total liabilities fell by \$4.5 million (18 per cent) to \$19.9 million, with the elimination of debt and a reduction of deferred tax liabilities.

Total revenue decreased by 3.9 per cent, to \$9.8 million in 2005-06, partly because of a loss from the disposal of assets.³ There was little change in total expenses, which remained at \$6.8 million.

Esk Water is subject to dividend and tax-equivalent payments. In 2005-06, dividend payments fell by 3.2 per cent to \$1.6 million. Esk Water recorded an income tax-equivalent expense of \$900 000 in 2005-06, down 9.5 per cent from 2004-05.

Esk Water was not subject to community service obligations.

¹ Participant councils include Launceston City, George Town, Meander Valley and West Tamar. On its inception, Esk Water received its initial equity from the State Government (88 per cent), Launceston City Council (11 per cent) and Meander Valley Council (1 per cent).

² Under the *Government Prices Oversight Act 1995*, the recommendations can take the form of maximum revenues, maximum prices, pricing principles, or a combination of these.

³ Esk Water gained control of a pipeline as part of the West Tamar Highway improvement works in 2005-06, which made an old pipeline redundant. The carrying amount of the old pipeline was reclassified and recorded as a loss from the disposal of assets in the income statement.

ESK WATER AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	121	127	118
Total revenue	\$m	9.6	10.2	9.8
<i>Profitability</i>				
Operating profit before tax	\$'000	2 872	3 311	2 996
Operating sales margin	%	30.1	32.0	29.2
Cost recovery	%	143.1	147.2	141.2
Return on assets	%	2.5	2.7	2.5
Return on equity	%	1.7	2.2	2.1
<i>Financial management</i>				
Debt to equity	%	1.8	1.9	—
Debt to total assets	%	1.7	1.6	—
Total liabilities to equity	%	8.8	23.7	20.4
Interest cover	times	15.8	28.6	26.4
Current ratio	%	248.2	242.0	839.2
Leverage ratio	%	108.8	123.7	120.4
<i>Payments to and from government</i>				
Dividends	\$'000	1 662	1 662	1 608
Dividend to equity ratio	%	1.5	1.6	1.6
Dividend payout ratio	%	87.5	71.8	76.7
Income tax expense	\$'000	972	995	900
CSO funding	\$'000	..	..	..

^a Esk Water commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Esk Water. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. – Zero or rounded to zero.

ACTEW Corporation (ACTEW) provides water and sewerage services to over 130 000 domestic and commercial customers in the ACT and Queanbeyan. ACTEW was established in 1995 and operates in accordance with the *Corporations Act 2001* (Cwlth). ActewAGL — a joint venture with a privately-owned energy company AGL — provides gas and electricity services and operates and maintains ACTEW Corporation's water and sewerage networks under contract.

ACTEW owns a 50 per cent interest in ActewAGL.¹ In addition, ACTEW holds a 25 per cent interest in TransACT Communications Pty Ltd, a broadband and telecommunications provider in the Canberra area.

The ACT Independent Competition and Regulatory Commission sets prices for water and sewerage services, along with electricity and gas distribution network services. A price path of CPI plus 2.5 per cent for water and CPI plus 1 per cent for wastewater was determined by the ICRC for four years commencing 1 July 2004.

Total assets increased by \$31.3 million (2.3 per cent) to \$1.4 billion in 2005-06, because of an increase in current assets, including cash and receivables. Total liabilities also increased by \$31.3 million (5.3 per cent) to \$618 million, producing no change in total equity. The increase in liabilities was partly because of increased deferred tax liabilities and growth in long-term borrowings.

ACTEW's operating profit before tax increased by \$2.8 million (3.1 per cent) in 2005-06 to \$93.1 million. Total revenue grew by \$15.3 million (7.2 per cent) to \$228 million, mainly because of growth in sales revenue following increases in water prices and consumption. Total expenses increased by \$12.5 million (10 per cent) to \$135 million as a result of increases in water costs associated with higher usage, including catchment remediation.

ACTEW is subject to dividends and tax-equivalent payments. ACTEW declared a dividend of \$60.5 million in 2005-06 (\$94.0 million in 2004-05). It recorded a tax-equivalent expense of \$32.6 million, an increase of 80 per cent on 2004-05. This resulted from an \$8.8 million negative tax expense adjustment in 2004-05 because of over-provision from the previous year. ACTEW is not subject to community service obligations. However, it receives a Commonwealth subvention to help fund water supply and sewerage services in the ACT.

¹ ActewAGL's operations are included in ACTEW's financial results using the 'equity method'. The share of profits and losses of the partnership are recognised in the income statement, and the share of movements in reserves are recognised in reserves in the balance sheet. ActewAGL reported assets of \$903 million and revenue of \$576 million in 2005-06.

ACTEW CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 363	1 381	1 412
Total revenue	\$m	212	212	228
Profitability				
Operating profit before tax	\$'000	89 487	90 272	93 096
Operating sales margin	%	36.3	36.3	36.2
Cost recovery	%	147.9	147.9	148.3
Return on assets	%	8.2	8.2	8.4
Return on equity	%	9.1	9.1	7.6
Financial management				
Debt to equity	%	45.8	45.1	47.0
Debt to total assets	%	26.3	25.9	26.7
Total liabilities to equity	%	74.5	73.8	77.7
Interest cover	times	5.0	5.0	4.8
Current ratio	%	75.9	75.9	115.0
Leverage ratio	%	174.5	173.8	177.7
Payments to and from government				
Dividends	\$'000	94 021	94 021	60 530
Dividend to equity ratio	%	12.0	11.8	7.6
Dividend payout ratio	%	132.1	130.2	100.0
Income tax expense ^c	\$'000	18 291	18 055	32 566
CSO funding ^d	\$'000	—	—	—

^a ACTEW Corporation (ACTEW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for ACTEW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c In 2004-05 there was an \$8.8 million negative tax expense adjustment because of over provision the previous year. ^d ACTEW does not receive community service obligation payments. However, it receives a Commonwealth subvention, of \$9.3 million in 2005-06, to help fund water supply and sewerage services in the ACT. — Zero or rounded to zero.

7 Urban transport

The financial performances of six urban transport government trading enterprises (GTEs) are reported in this chapter. At the end of 2005-06, they controlled \$4.6 billion in assets and generated \$1.6 billion in revenue.

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 defined in chapter 1.

When making comparisons, consideration should be given to: differences in the nature and scale of the businesses; their individual market environments; a number of issues relating to the valuation of their assets; and the level of payments for community service obligations. Care should also be exercised when comparing data presented in this chapter with that presented in previous reports for two reasons.

1. The performance data presented in this report are based, for the first time, on the new Australian-equivalent International Financial Reporting Standards.
2. Data from GTE general purpose financial reports have been used for this report, whereas data presented in previous reports were based on government financial statistics. The reason for this change is set out in chapter 1.

7.1 Monitored GTEs

The monitored GTEs vary in their size, corporate structure, and in the range of services they provide. The primary activity of most urban transport GTEs is the provision of bus services (table 7.1). TransAdelaide and the WA Public Transport Authority (PTA) are also responsible for managing rail infrastructure.

The PTA, which was included in the rail sector in previous reports, has been moved to the urban transport sector for this report. This change was made because its main role is now the provision of passenger rail, bus and ferry services in metropolitan Perth.

Table 7.1 **Activities — monitored urban transport GTEs, 2005-06**

	<i>Bus</i>	<i>Ferry</i>	<i>Tram</i>	<i>Train</i>
State Transit Authority (NSW)	✓	✓	✗	✗
Sydney Ferries Corporation (NSW)	✗	✓	✗	✗
Public Transport Authority (WA) ^a	✓	✓	✗	✓
TransAdelaide (SA) ^b	✗ ^c	✗	✓	✓
Metro Tasmania (Tas)	✓	✗	✗	✗
ACTION (ACT)	✓	✗	✗	✗

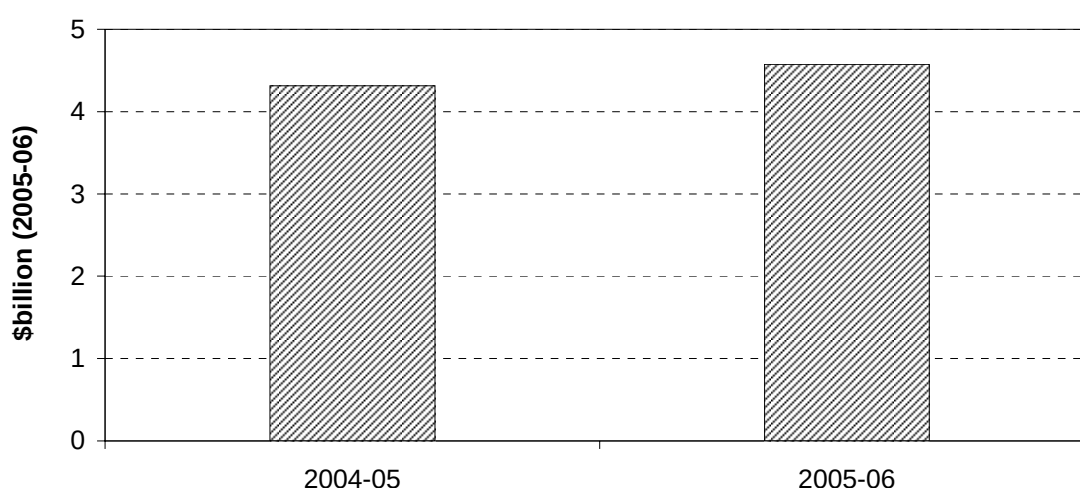
^a In addition to its passenger transport activities, the Public Transport Authority is responsible for managing rail infrastructure in WA, principally through its New MetroRail. ^b In addition to its passenger transport activities, TransAdelaide is the infrastructure manager for the Adelaide metropolitan 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.

Queensland Rail and the Victorian V/line Passenger Corporation also provide urban transport services as part of their broader rail operations. The performance of these GTEs is reported in chapter 8.

Total assets controlled by the monitored urban transport GTEs grew by \$261 million (6.1 per cent) in real terms between 2004-05 and 2005-06 (figure 7.1). Most of the growth was attributable to the PTA, which increased its total assets by 15 per cent in real terms, mainly as a result of capital investment.

The PTA controlled 68 per cent of the sector assets in 2005-06, while

Figure 7.1 **Sector assets — urban transport GTEs^a**

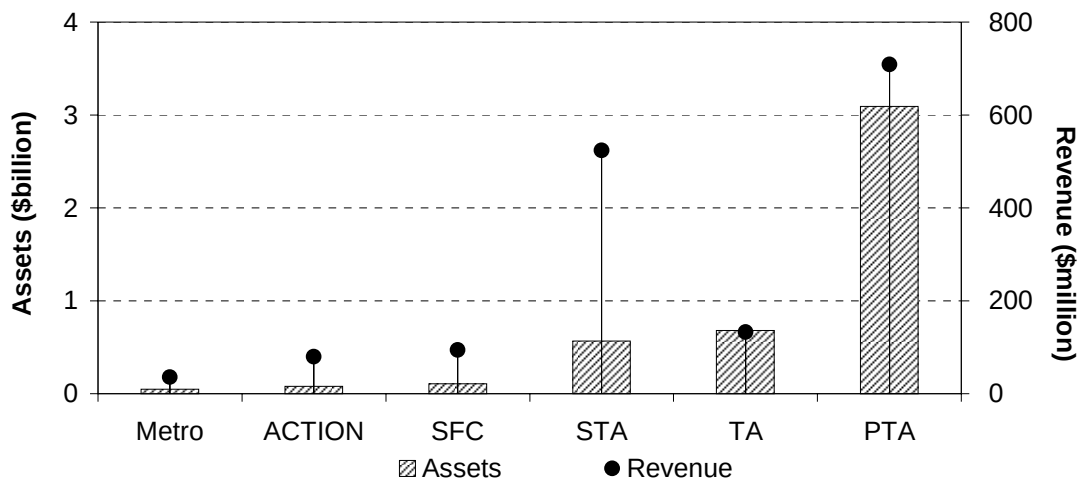


^a The value of sector assets is reported in 2005-06 dollars using the ABS implicit price deflator — gross fixed capital formation for public corporations (chapter 1).

Source: Productivity Commission estimates.

TransAdelaide and the State Transit Authority (STA) accounted for a further 15 per cent and 12 per cent respectively. The PTA accounted for 45 per cent (and the STA, 33 per cent) of the \$1.6 billion of revenue generated by the six GTEs in 2005-06 (figure 7.2). The large size of TransAdelaide's asset base relative to its revenue reflects the high valuation of rail infrastructure assets compared with buses and ferries for the other urban transport GTEs.

Figure 7.2 **Assets and revenue — urban transport GTEs, 2005-06**



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 quality of service, competition from private operators of urban transport, the cost of alternative methods of transport (including those associated with driving and parking privately-owned motor vehicles) as well as changes in fares and urban demographics.

Patronage growth was steady or increasing for urban transport in 2005-06, representing a reversal of the declining passenger numbers observed in 2004-05. The PTA, TransAdelaide, Metro Tasmania (Metro) and ACTION recorded growth in patronage of 3.7 per cent, 0.4 per cent, 3.8 per cent and 8.3 per cent, respectively. The STA and the Sydney Ferries Corporation (SFC) recorded steady passenger numbers, with 199 million and 14 million passengers respectively in 2005-06.

Within each GTE, patronage growth varied between passenger types and modes of travel. For example, the STA reported patronage growth of 19 per cent on its

Liverpool–Parramatta T-Way network and up to 16 per cent on some bus routes. TransAdelaide noted that its train patronage grew by 4.7 per cent, but its tram passenger numbers fell by 1.2 per cent (although this was the result of a six-week shutdown of tram services during a major upgrade of the tramline). Metro reported an 8.5 per cent increase in adult full fare patronage and a 5.8 per cent decrease in adult concession fare patronage.

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 included the benefits of service coordination and system-wide ticketing, the limited potential for competition, the existence of positive externalities and the provision of access to the disadvantaged.

Institutional and regulatory reform has been aimed at reducing the reliance of service providers on government subsidies by commercialising publicly-owned services, and promoting efficiency by exposing service providers to more competitive markets (PC 2005b). The principal areas of reform in urban transport have been in the areas of governance, supplier market competition and the setting of 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.

The only significant change in the governance structure of the STA since the passing of the *Transport Administration Act 1988* was the separation — under legislation passed by the NSW Parliament in 2003 — of Sydney Ferries (now operating as the Sydney Ferries Corporation) from the STA on 1 July 2004.

In SA, the *Passenger Transport (Dissolution of Passenger Transport Board) Amendment Act 2003* dissolved the Passenger Transport Board (PTB) effective from 1 January 2004. In conjunction with this Act, the SA 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.

On 1 January 2002, the status of ACTION changed from a division of the Department of Urban Services to a statutory authority. This was reversed on 30 June 2006, when the ACT Government abolished the statutory authority as part of its restructuring of the ACT public sector. From 1 July 2006, responsibility for

ACTION's services was transferred to the new Department of Territory and Municipal Services.

Market reforms

Some aspects of the National Competition Policy reforms have had an impact on administrative and operational arrangements in the urban transport sector. These include the application of competitive neutrality principles, the contracting out of some services, and in 2005-06, the use of funding contracts to provide performance incentives.

Competitive tendering arrangements have been introduced to provide incentives for improved commercial performance. Urban transport GTEs have been required to compete with private sector providers for the right to operate certain urban passenger services in NSW, Victoria and SA.

Since 1995-96, TransAdelaide has been required to compete with the private sector on the basis of a set of costing rules designed to ensure competitive neutrality. TransAdelaide ceased providing bus services after it was unsuccessful in tendering for service contracts with the PTB on 22 April 2000. However, it continues to participate in a joint venture with Australian Transit Enterprises to operate bus services in the Adelaide Hills.

The STA expanded its bus services in Western Sydney after winning a tender to deliver high frequency services along the Liverpool–Parramatta T-Way. The STA was awarded the contract in January 2002 ahead of competition from Australian and multinational companies. Services commenced under the new contract in February 2003.

The STA's new system of contract-based funding includes payments for achieving certain performance and patronage levels. For example, the STA received an incentive payment of \$2.1 million in 2005-06 for exceeding fare revenue benchmarks.

Tariff reforms

Prices for the services provided by urban transport GTEs are determined by either the responsible minister or the regulatory authority, as follows:

- Independent Pricing and Regulatory Tribunal in NSW;

-
- Minister for Planning and Infrastructure in WA;
 - Minister for Transport, Energy and Infrastructure in SA;¹
 - Minister for Infrastructure, Energy and Resources in Tasmania, after considering reports by the Government Prices Oversight Commission; and
 - Independent Competition and Regulatory Commission (ICRC) in the ACT.

With the exception of ACTION, all urban transport GTEs increased prices in 2005-06. In its May 2003 determination, the ICRC decided that ACTION's prices would not increase for the period ending 30 June 2006. The ICRC stated that ACTION lacked an 'overarching public transport strategy' and that the regulator wished to give the Authority an opportunity to increase its patronage — and the public, a degree of certainty — by maintaining fare levels (ICRC 2003, p. iv).

7.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by owner-governments to generate earnings.

Four of the six urban transport GTEs recorded pre-tax operating profits in 2005-06. The STA, TransAdelaide and Metro improved their profitability from 2004-05 to 2005-06, while the PTA's operating profit fell by 78 per cent in real terms from 2004-05.² The SFC and ACTION made operating losses in 2004-05 and 2005-06, with profitability falling over the period. The SFC's operating loss grew from \$1.6 million in 2004-05 (2005-06 dollars) to \$48.7 million in 2005-06, and ACTION's pre-tax operating loss more than doubled in real terms from \$7.0 million in 2004-05 (2005-06 dollars) to \$14.2 million in 2005-06.³

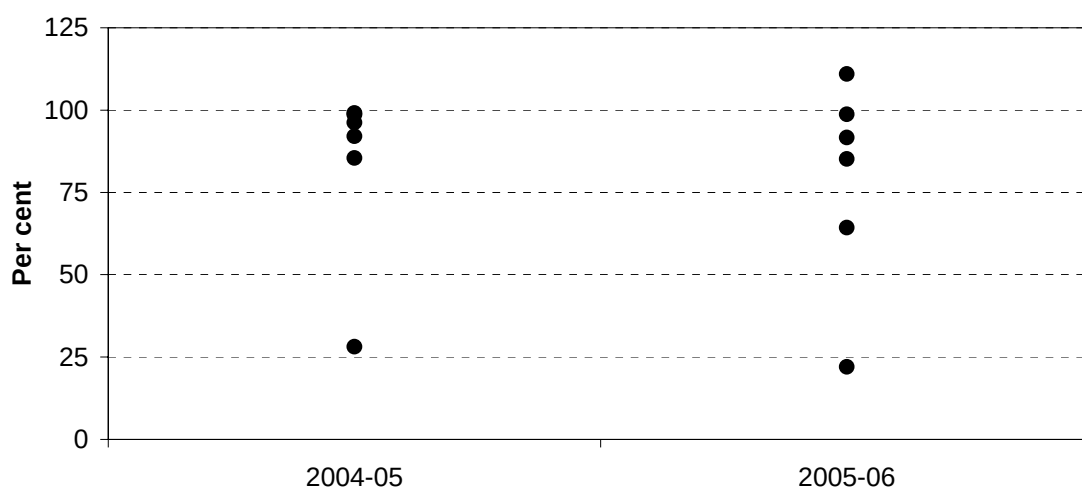
Most urban transport GTEs did not fully recover their operating costs in 2004-05 and 2005-06 (figure 7.3), meaning that revenue from operations did not exceed

¹ Prices were determined by the PTB until its abolition at the end of December 2003.

² The fall in the PTA's operating profit was mainly attributable to an increase in its depreciation and interest expenses, as well as an increase in the capital user charge levied by the WA Government. These expenses were related to the PTA's capital investment program (and corresponding increase in debt) undertaken in 2005-06.

³ The SFC notes in its 2005-06 annual report that the operating loss was largely the result of a fleet devaluation of \$35.8 million to revalue fleet at current depreciated replacement cost.

Figure 7.3 Cost recovery — urban transport GTEs^a



^a 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.

Source: Productivity Commission estimates.

expenses from operations.⁴ The STA was the only GTE to record a cost recovery ratio greater than 100 per cent in either of the two years. The PTA had a cost recovery ratio of 22.0 per cent in 2005-06 (down from 28.1 per cent in 2004-05). Despite this low level of cost recovery, the PTA recorded a positive operating profit because most of its revenue comes from the WA Government in the form of grants and service appropriations — with self-generated revenue from operations contributing only 23 per cent of total revenue in 2005-06.

Four of the six urban transport GTEs had a positive return on assets ratio in 2005-06, the same number (but different GTEs) that did so in 2004-05 (figure 7.4). In 2005-06, the STA was the only urban transport GTE to achieve a return on assets which was greater than the risk-free rate of return.⁵ The highest rates of return on assets recorded over the last two years were 9.5 per cent (the STA, in 2005-06) and 4.8 per cent (the PTA, in 2004-05). Two GTEs (the SFC and ACTION) had negative returns on assets in 2005-06 (-35.6 per cent and -8.2 per cent respectively).

⁴ GTEs can have a cost recovery ratio less than 100 per cent and still record a profit, as a result of revenue and expense items other than revenue and expenses from operations. Definitions of these measures are provided in chapter 1.

⁵ The risk-free rate of return is defined as the 2005-06 interest rate on 10-year Australian Government bonds of 5.4 per cent (RBA 2007a).

The sector return on assets was 3.0 per cent in 2005-06, up slightly from 2.6 per cent in 2004-05.

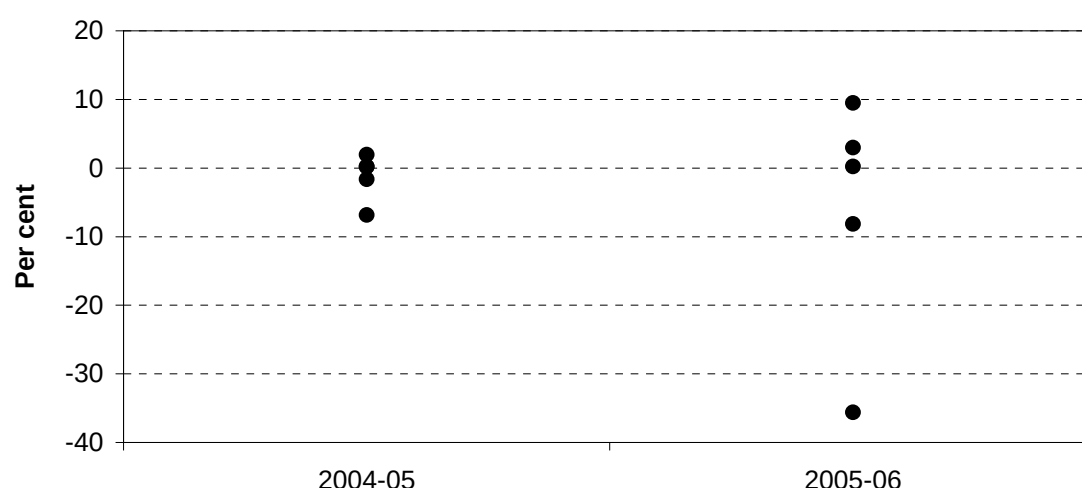
Except for the STA, in 2005-06, urban transport GTEs did not achieve the minimum commercial rate of return, represented by the risk-free rate.

Governments might not require a commercial rate of return from urban transport GTEs because urban transport provides external benefits 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 could believe 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.

Return on assets is influenced by a wide range of factors, including changes in total revenue and total expenses, changes in asset values — through asset transfers, sale and lease-buy-back arrangements, asset revaluations, asset disposals and depreciation.

The return on equity — the GTE's earnings for the year expressed as a proportion of equity held in the business — tends to move broadly in line with return on assets, but it is affected by changes in the value of liabilities as well as in the value of total assets.

Figure 7.4 Return on assets — urban transport GTEs^a



^a 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.

Source: Productivity Commission estimates.

Four of the six urban transport GTEs achieved a positive return on equity in 2005-06, an improvement from 2004-05 when five of the six GTEs recorded negative returns. The STA achieved a return on equity of 23.5 per cent in 2005-06. However, the remaining GTEs had low or negative returns on equity in 2005-06. The PTA, TransAdelaide and Metro reported returns of between zero and 3.0 per cent, while the SFC and ACTION reported returns of -80.7 per cent and -27.0 per cent respectively. The sector return on equity was largely unchanged at 0.5 per cent in 2005-06, compared with 0.4 per cent in 2004-05.

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 and reduced debt levels over the last two years. 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.

Five of the six urban transport GTEs recorded a decrease in their debt to total assets ratio from 2004-05 to 2005-06 (figure 7.5). The exception was the SFC, which increased its debt to assets ratio from 29.1 per cent in 2004-05 to 38.0 per cent in 2005-06. Most urban transport GTEs had a relatively low level of borrowings in 2005-06, with four out of the six having a debt to assets ratio of less than 15.0 per cent.

Besides a decline in total debt, an improvement in the debt to total assets ratio can also result from changes in the value of assets from capital works, asset revaluations, debt restructuring, and the transfer of liabilities to (or from) governments. For example, the PTA's capital investment — and the resultant \$407 million (15 per cent) real increase in its total assets — led to a reduction in its debt to assets ratio from 61.8 per cent in 2004-05 to 30.4 per cent in 2005-06, despite a \$60.5 million (3.6 per cent) real increase in the value of its debt.

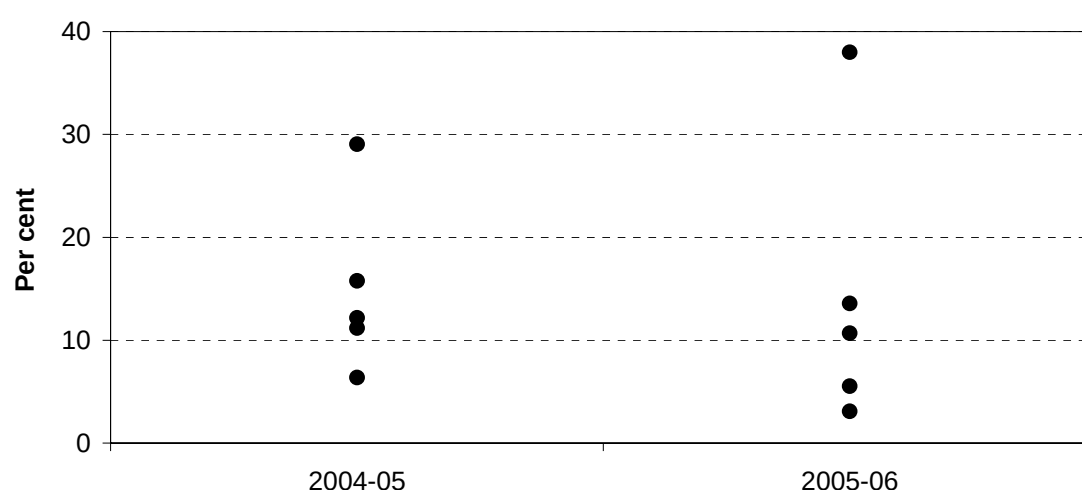
Sound financial management requires that profits are sufficient to ensure interest payments can be met. A high level of interest cover — the ratio of earnings before interest and tax expenses to gross interest expenses — indicates that the entity can

sustain a fall in profit or an increase in interest expenses and still meet the cost of servicing debt.

The interest cover levels reported by urban transport GTEs ranged from -13.7 times to 9.0 times in 2005-06. This was a larger range than in 2004-05, when interest cover levels were between -5.4 times and 1.4 times.

The SFC and ACTION had negative interest cover in 2005-06, while Metro and the PTA had interest cover of less than 2.0 times. This indicates that these GTEs might have to fund interest expenses from sources other than current operating profits. The STA and TransAdelaide are likely to be able to meet their interest commitments from operating profit, particularly the STA, which improved its interest cover from 0.1 times in 2004-05 to 9.0 times in 2005-06.

Figure 7.5 Debt to total assets — urban transport GTEs^a



^a 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.

Source: Productivity Commission estimates.

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 by exposing them to capital market disciplines and regulations similar to those faced by private sector businesses.

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.

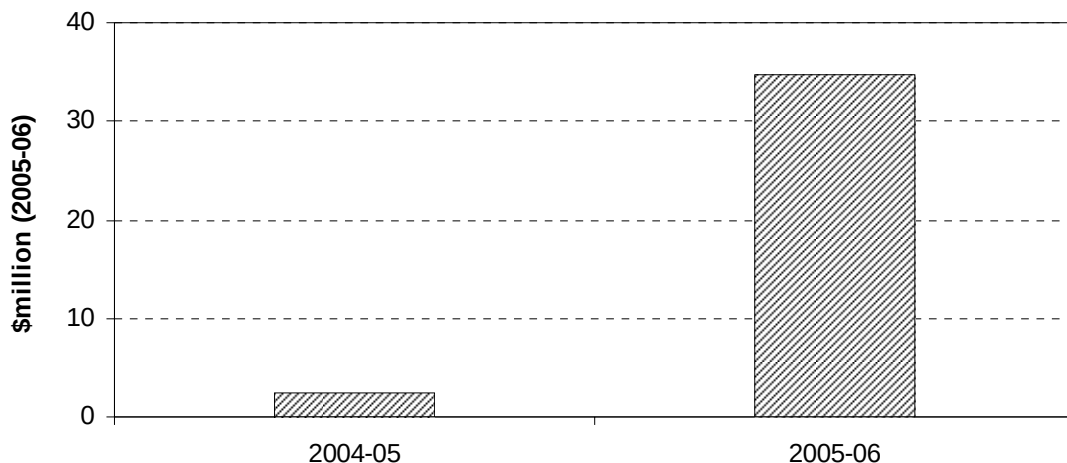
Dividend payments and income tax-equivalent expenses recorded by urban transport GTEs have been low compared with GTEs in other sectors, reflecting the small and volatile returns of these GTEs.

TransAdelaide was the only urban transport GTE to make dividend payments in 2004-05 and 2005-06 (figure 7.6). These payments were special dividends — \$2.3 million for depreciation funding in each of 2004-05 and 2005-06, as well as \$32.5 million paid to the SA Department of Transport, Energy and Infrastructure in 2005-06 for the sale of tram infrastructure assets.

None of the urban transport GTEs recorded a tax-equivalent expense in 2004-05 or 2005-06, as a result of negative operating results or accumulated tax losses.

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 community service obligation (CSO) payments.

Figure 7.6 **Dividends — urban transport GTEs^{a,b}**



^a Data relate to TransAdelaide, which was the only urban transport GTE to have made dividend payments in 2004-05 and 2005-06. The large increase in dividends in 2005-06 reflects special dividend payments of \$34.8 million made by TransAdelaide, which consisted of \$32.5 million for the sale of tram infrastructure assets to the Department of Transport, Energy and Infrastructure and \$2.3 million for depreciation funding.

^b The value of dividends are reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation for public corporations (chapter 1).

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 below commercial rates. 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 off-peak services with low patronage.
- *Concessions* — to reimburse GTEs for administering 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, the SFC, Metro and ACTION receive CSO payments, although Metro does not reveal the value of this funding in its published financial statements. TransAdelaide also receives government payments, though funding is generally in the form of capital and recurrent grants. The PTA, as an ‘on-budget’ agency, does not receive CSO funding as such. However, it receives a large proportion of its revenue from the WA Government, in the form of grants and service appropriations.

The STA adopted a new funding system in 2005-06 after it signed four Metropolitan Bus System Contracts with the Ministry of Transport on 1 July 2005. These contracts cover four separate regions of Sydney and are valid for the seven-year period to June 2012. Contract payments have replaced the STA’s previous Pricing and Service CSO funding as well as its concession payments for free school travel. The contract payments are not disclosed in the STA’s published financial statements.

For some urban transport GTEs, CSOs account for a relatively large share of total revenue. CSO funding accounted for 76 per cent of total revenue for ACTION and 46 per cent for the SFC in 2005-06, and government grants and appropriations represented 81 per cent of the PTA’s total revenue. However, CSOs accounted for 4.8 per cent of the STA’s total revenue in 2005-06, as a result of its transition to contract payments.

7.6 Implications of the new accounting standards

From 2005-06, financial data for all monitored urban transport GTEs are based on the Australian-equivalent International Financial Reporting Standards (AIFRS). The adoption of the new accounting standard changed the recognition and measurement of some assets, liabilities and equity items, and affected the recording of income

flows. These changes, which were discussed in the previous *Financial Performance of Government Trading Enterprises* report (PC 2006, chapter 3), have had a significant effect on the comparability over time of financial performance and financial management indicators.

The aggregate impact of the transition to AIFRS for the monitored urban transport GTEs can be gauged by comparing 2004-05 data on an AIFRS and pre-AIFRS basis (table 7.2). Similar comparisons can be made by reference to each GTE summary.

URBAN TRANSPORT

Table 7.2 Whole of sector performance indicators, 2004-05 to 2005-06^a

		Pre-AIFRS ^{b,c}		AIFRS ^b
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	4 024	4 120	4 574
Total revenue	\$m	1 457	1 432	1 575
Profitability				
Operating profit before tax	\$'000	44 578	5 686	7 896
Operating sales margin	%	9.8	7.3	8.0
Cost recovery	%	71.8	69.9	66.4
Return on assets	%	3.7	2.6	3.0
Return on equity	%	2.8	0.4	0.5
Financial management				
Debt to equity	%	120.5	121.1	100.3
Debt to total assets	%	45.0	43.9	44.4
Total liabilities to equity	%	168.0	175.6	137.4
Interest cover	times	1.4	1.1	1.1
Current ratio	%	22.5	21.1	8.2
Leverage ratio	%	268.0	275.6	237.4
Payments to and from government				
Dividends	\$'000	2 296	2 296	34 757 ^d
Dividend to equity ratio	%	0.2	0.2	2.0
Dividend payout ratio	%	5.6	40.4	440.2
Income tax expense	\$'000	3 239	—	—
CSO funding	\$'000	334 521	335 794	128 610

^a Figures are nominal values. ^b Urban transport GTEs commenced reporting under Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for urban transport GTEs. ^c Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^d The large increase in dividends in 2005-06 reflects special dividend payments of \$34.8 million made by TransAdelaide, which consisted of \$32.5 million for the sale of tram infrastructure assets to the Department of Transport, Energy and Infrastructure and \$2.3 million for depreciation funding. — Zero or rounded to zero.

7.7 GTE performance reports

State Transit Authority (NSW)

Sydney Ferries Corporation (NSW)

Public Transport Authority (WA)

TransAdelaide (SA)

Metro Tasmania

ACTION Authority (ACT)

The State Transit Authority (STA) was incorporated under the *Transport Administration Act 1988* and operates within the regulatory framework of the *Passenger Transport Act 1990*. In 2005-06, it operated three metropolitan passenger transport businesses — Sydney Buses, Western Sydney Buses, and Newcastle Bus and Ferry Services.

Prices for the STA's services are set by the NSW Independent Pricing and Regulatory Tribunal (IPART). In its December 2005 determinations, IPART increased fares for Sydney Buses and Newcastle Bus and Ferry Services by between zero and \$2.10, depending on ticket type (IPART 2005a, 2005c).

The STA entered into four Metropolitan Bus System Contracts with the NSW Minister of Transport on 1 July 2005. These contracts covered four separate regions of Sydney and cover the seven-year period to June 2012. Under the new system, contract payments for costs, patronage and performance levels replaced the Pricing and Service CSOs as well as payments for free school travel. The STA signed a fifth Metropolitan Bus System Contract — for the Newcastle region — on 30 June 2006.

The STA recorded a pre-tax operating profit of \$47.1 million in 2005-06, an increase of \$52.3 million from the \$5.2 million operating loss of 2004-05. Consequently, the return on assets and return on equity both improved significantly, to 9.5 per cent and 23.5 per cent respectively. The improved profitability was mainly attributable to increased revenue following the introduction of Metropolitan Bus System Contract payments, as well as reduced expenditure following a downward adjustment to staff entitlements of \$32.0 million.

The STA's total assets increased by \$12.7 million (2.3 per cent) to \$567 million in 2005-06. Capital expenditure was \$52.4 million, a reduction from \$55.5 million in 2004-05. The capital works program consisted of \$44.1 million for a bus replacement program and \$8.3 million for the renewal or replacement of assets required for bus servicing, ferry maintenance, depot facilities and computing resources.

The STA made no dividend payments, and did not record a tax-equivalent expense, in 2005-06.

Community service obligation funding amounted to \$25.1 million in 2005-06 — a reduction from the \$232 million received in 2004-05 — as a result of the introduction of the Metropolitan Bus System Contracts.

STATE TRANSIT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05 ^c	2004-05 ^c	2005-06
Size				
Total assets	\$m	462	554	567
Total revenue	\$m	500	488	524
Profitability				
Operating profit before tax	\$'000	5 776	-5 163	47 149
Operating sales margin	%	2.3	0.1	9.9
Cost recovery	%	101.3	99.1	111.0
Return on assets	%	2.6	0.2	9.5
Return on equity	%	3.4	-3.0	23.5
Financial management				
Debt to equity	%	51.6	50.0	33.4
Debt to total assets	%	18.9	15.8	13.6
Total liabilities to equity	%	173.4	217.2	149.3
Interest cover	times	2.0	0.1	9.0
Current ratio	%	32.1	25.8	29.3
Leverage ratio	%	273.4	317.2	249.3
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^d	\$'000	231 975	231 975	25 099

^a The State Transit Authority (STA) commenced reporting under Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the STA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c On 30 June 2004, the Minister for Transport Services authorised the transfer of certain assets and liabilities to Sydney Ferries, which had a net value of \$83.1 million. ^d The large decrease in community service obligation funding in 2005-06 was because of the replacement of such funding with contract payments under the new Metropolitan Bus System Contracts. — Zero or rounded to zero.

Sydney Ferries operated within the State Transit Authority until 1 July 2004 when it was incorporated as the Sydney Ferries Corporation (SFC). It operates under the *State Owned Corporations Act 1989*. The SFC provides approximately 110 000 ferry services per year, carrying more than 14 million people on Sydney Harbour and the Parramatta River.

Prices for the SFC's services are set by the NSW Independent Pricing and Regulatory Tribunal (IPART). In its December 2005 determination, IPART increased SFC's fares by between zero and \$2.20, depending on ticket type (IPART 2005b).

The SFC's total assets fell by \$37.7 million in 2005-06, mainly because of a \$35.8 million downward revaluation of its fleet. This contributed to a pre-tax operating loss of \$48.7 million, a substantial decline from the \$1.5 million loss in 2004-05. This in turn led to a negative rate of return on assets of -35.6 per cent in 2005-06.

The SFC's total debt increased from \$42.0 million in 2004-05 to \$47.7 million in 2005-06. With the reduction in total assets and a \$4.9 million increase in total liabilities, the debt to equity ratio increased to 122.2 per cent and the leverage ratio to 273.6 per cent.

The SFC is currently exempt from the Tax-Equivalent Regime under the NSW *State Owned Corporations Act 1989*.

Costs are recovered by a combination of fares, charters and tourism services, as well as government reimbursements for community service obligations (CSOs). Of the \$42.9 million in CSO payments in 2005-06, \$9.8 million was for fare concessions to pensioners, school children and other eligible groups. The remaining \$33.1 million was for two general reimbursements — a pricing CSO to cover the gap between SFC's fares and the equivalent commercial benchmark, and a service CSO to cover the operation of a number of non-commercial services.

SYDNEY FERRIES CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	143	145	107
Total revenue	\$m	96	96	94
Profitability				
Operating profit before tax	\$'000	-2 619	-1 513	-48 681
Operating sales margin	%	1.1	2.3	-47.7
Cost recovery	%	95.0	96.2	64.2
Return on assets	%	1.3	1.9	-35.6
Return on equity	%	-3.3	-1.9	-80.7
Financial management				
Debt to equity	%	52.2	51.5	122.2
Debt to total assets	%	29.4	29.1	38.0
Total liabilities to equity	%	77.5	77.1	173.6
Interest cover	times	0.4	0.6	-11.5
Current ratio	%	60.5	42.6	36.0
Leverage ratio	%	177.5	177.1	273.6
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense ^c	\$'000	..	..	..
CSO funding	\$'000	43 367	44 640	42 922

^a The Sydney Ferries Corporation (SFC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the SFC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The SFC is currently exempt from tax-equivalent payments. .. Not applicable. – Zero or rounded to zero.

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 an ‘on-budget’ agency in the Planning and Infrastructure Portfolio. It replaced the WA Government Railway Commission, Transperth, School Bus Services and local regional bus services.

The PTA is responsible for rail, bus and ferry services in Perth, school buses, public transport in regional areas, and for designing, building, managing and maintaining public transport infrastructure throughout the state.

In 2005-06, the PTA increased assets under management by \$528 million to \$3.1 billion. This mainly reflects the PTA’s capital expenditure of \$484 million on the New MetroRail project, as well as investment in gas-powered buses, a new smart card ticketing system and rolling stock. The investment expenditure was partly funded by capital contributions from the WA Government of \$425 million, and by a \$135 million increase in debt. The increase in liabilities caused the PTA’s current ratio to fall from 11.2 per cent in 2004-05 to 1.8 per cent in 2005-06. This indicates that the PTA’s current assets would not cover its current liabilities, if they were to fall due.

The PTA recorded an operating profit of \$8.7 million in 2005-06, \$28.4 million less than in 2004-05. This was caused by a \$105 million increase in total expenses to \$700 million, mainly attributable to an increase in its depreciation and interest expenses, as well as an increase in the capital user charge levied by the WA Government. These expenses were related to the PTA’s substantial capital investment program (and corresponding increase in debt) undertaken in 2005-06.

Total revenue also increased, but only by \$76.2 million to \$709 million. Of this revenue, \$560 million was provided by the WA Government as a service appropriation and \$90.3 million was generated from fees and user charges.

The PTA is not required to make dividend or tax-equivalent payments to the WA Government.

Funding from the WA Government, in the form of grants and service appropriations, constituted 81 per cent of the PTA’s total revenue in 2005-06, an increase from 77 per cent in 2004-05.

PUBLIC TRANSPORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	2 566	2 566	3 094
Total revenue	\$m	635	632	709
Profitability				
Operating profit before tax	\$'000	37 139	37 139	8 696
Operating sales margin	%	19.1	19.2	16.0
Cost recovery	%	28.6	28.1	22.0
Return on assets	%	4.8	4.8	2.0
Return on equity	%	6.3	6.3	1.1
Financial management				
Debt to equity	%	267.1	267.1	166.3
Debt to total assets	%	61.8	61.8	30.4
Total liabilities to equity	%	332.0	332.0	198.9
Interest cover	times	1.4	1.4	1.1
Current ratio	%	11.2	11.2	1.8
Leverage ratio	%	432.0	432.0	298.9
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^c	\$'000	..	..	..

^a The Public Transport Authority (PTA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PTA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c As the PTA is an 'on-budget' agency, it does not receive CSO funding as such. However, it received funding from the WA Government — in the form of grants and service appropriations — of \$488 million in 2004-05 and \$577 million in 2005-06. .. Not applicable. — Zero or rounded to zero.

TransAdelaide was established as a Public Authority under the *TransAdelaide (Corporate Structure) Act 1998* and is subject to the provisions of the *Public Corporations Act 1993*. TransAdelaide has a 50 per cent share in TransitPlus Pty Ltd, a joint-venture entity established for the provision of bus services in the Adelaide Hills. TransAdelaide provides passenger train and tram services to the Adelaide metropolitan area under a service contract with the Public Transport Division for the period April 2005 to April 2010, and is responsible for the management of train and tram infrastructure in Adelaide.

Total assets decreased by \$48.4 million (6.6 per cent) between 2004-05 and 2005-06. This was partly attributable to a \$22.0 million write-off of tax-related assets following changes to the SA Government's tax accounting guidelines. The decline in assets also reflected the sale of the upgraded Glenelg tram line to the Department of Transport, Energy and Infrastructure (DTEI).

TransAdelaide's return on assets increased from -1.6 per cent in 2004-05 to 3.0 per cent in 2005-06, reflecting a reduction in the value of assets and an increase in pre-tax operating profit.

Pre-tax operating profit increased from an \$18.0 million loss in 2004-05 to a \$14.9 million profit in 2005-06, largely attributable to the recognition of \$24.6 million in capital grant income triggered by the tram infrastructure asset sale.¹ TransAdelaide states that without this income, it would have recorded an operating loss of \$9.5 million.

TransAdelaide is subject to dividend and tax-equivalent payments. No ordinary dividend was paid in 2005-06, but special dividend payments totalling \$34.8 million were made. This included \$2.3 million for depreciation funding and \$32.5 million relating to the sale of tram related assets to the DTEI.²

TransAdelaide did not record an income tax-equivalent expense in 2005-06 because the proceeds from the tram infrastructure asset sale were excluded from net profit for tax-equivalent payment purposes. TransAdelaide does not receive community service obligation funding from the SA Government.

¹ According to TransAdelaide, this amount was mainly related to the Glenelg tram line upgrade, and would have been amortised against future depreciation if the assets had not been disposed of during 2005-06.

² The SA Government directed TransAdelaide to make a special dividend payment representing the net proceeds received from the sale of the Glenelg tram line.

TRANSADELAIDE (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	726	729	680
Total revenue	\$m	115	105	133
Profitability				
Operating profit before tax	\$'000	10 889	-18 029	14 855
Operating sales margin	%	13.6	-13.1	14.4
Cost recovery	%	102.2	85.4	91.6
Return on assets	%	2.3	-1.6	3.0
Return on equity	%	1.3	-3.1	2.6
Financial management				
Debt to equity	%	14.0	14.2	13.6
Debt to total assets	%	11.2	11.2	10.7
Total liabilities to equity	%	24.7	27.0	22.8
Interest cover	times	2.8	-1.9	3.5
Current ratio	%	92.5	100.9	124.3
Leverage ratio	%	124.7	127.0	122.8
Payments to and from government				
Dividends	\$'000	2 296	2 296	34 757 ^c
Dividend to equity ratio	%	0.4	0.4	6.2
Dividend payout ratio	%	30.0	-12.7	234.0
Income tax expense	\$'000	3 239	—	— ^d
CSO funding	\$'000	..	..	..

^a TransAdelaide commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for TransAdelaide. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c In 2005-06, special dividend payments of \$34.8 million were made, consisting of \$2.3 million for depreciation funding and \$32.5 million for the sale of tram infrastructure assets to the Department of Transport, Energy and Infrastructure. ^d TransAdelaide did not record an income tax-equivalent expense in 2005-06 because the proceeds from the tram infrastructure asset sale were excluded from net profit for tax-equivalent payment purposes. Based on its profit of \$14.9 million, TransAdelaide would otherwise have incurred an income tax-equivalent expense of around \$4.5 million in 2005-06. .. Not applicable. — Zero or rounded to zero.

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. Metro provides bus services within Hobart, Launceston and Burnie, as well as between Wynyard, Burnie and Ulverstone. On 30 June 2005, Metro acquired the business of its subsidiary, Metro Coaches (Tas) Pty Ltd. Since 1 July 2005, Metro has delivered regional services previously provided by Metro Coaches, under its regional services division, Hobart Coaches.

The maximum prices that Metro can charge are determined by the Tasmanian Government after considering reports by the Government Prices Oversight Commission. Fares were increased by between 5 per cent and 8 per cent in January 2006, although fares for children and other student passengers remained unchanged.

Metro recorded a pre-tax operating profit of \$30 000 in 2005-06, representing an improvement from the \$94 000 operating loss of 2004-05. However, Metro would have made an operating loss in 2005-06 if it were not for an adjustment to contract payments relating to the Corporation's superannuation provisions. According to Metro, it would have made a loss of about \$164 000 without this adjustment.

Metro's total assets increased by 5.4 per cent (\$2.4 million) to \$46.8 million in 2005-06, while total liabilities fell by 7.9 per cent (\$2.2 million) to \$26.1 million. As a result, the total liabilities to equity ratio decreased from 175.8 per cent in 2004-05 to 125.8 per cent in 2005-06.

The *Metro Tasmania Act 1997* and the *Government Business Enterprises Act 1995* require Metro to make income tax-equivalent payments to the Tasmanian Government. Metro has not made tax-equivalent payments during the reporting period because of accumulated tax losses. No dividend was declared for 2005-06.

Metro has a Community Service Activity Agreement with the Tasmanian Government, which enables Metro to deliver specified (quantity and quality) services while achieving a break-even operating result. Community service obligation funding is not separately identified in Metro's financial statements.

METRO TASMANIA (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	44	44	47
Total revenue	\$m	34	34	36
<i>Profitability</i>				
Operating profit before tax	\$'000	47	-94	30
Operating sales margin	%	-0.9	-1.4	-1.3
Cost recovery	%	99.1	98.7	98.7
Return on assets	%	0.5	0.2	0.2
Return on equity	%	0.2	-0.6	0.2
<i>Financial management</i>				
Debt to equity	%	13.2	17.6	13.5
Debt to total assets	%	6.4	6.4	3.1
Total liabilities to equity	%	107.1	175.8	125.8
Interest cover	times	1.2	0.5	1.2
Current ratio	%	142.4	151.2	138.2
Leverage ratio	%	207.1	275.8	225.8
<i>Payments to and from government</i>				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding ^c	\$'000	na	na	na

^a Metro Tasmania (Metro) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Metro. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Although Metro receives community service obligation (CSO) funding under its Community Service Activity Agreement with the Tasmanian Government, the level of CSO funding is not reported separately in Metro's annual report. — Zero or rounded to zero. **na** Not available.

The Australian Capital Territory Internal Omnibus Network Authority (ACTION) provides urban and school bus services to the Canberra metropolitan area. 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. This was reversed on 30 June 2006, when the ACT Government abolished the statutory authority as part of its restructuring of the ACT public sector. From 1 July 2006, responsibility for ACTION's services was transferred to the new Department of Territory and Municipal Services.

Prices for ACTION's services are set by the ACT's Independent Competition and Regulatory Commission, which determined that there should be no fare increases for the period ending in June 2006.

Total assets decreased by 2.6 per cent to \$80.0 million between 2004-05 and 2005-06, largely because of a downward revaluation of buildings. Current assets fell by 37 per cent to \$5.4 million, while current liabilities grew by 14 per cent to \$21.3 million, causing the current ratio to decline to 25.2 per cent from 45.1 per cent in 2004-05.

ACTION recorded a pre-tax operating loss of \$14.2 million in 2005-06, more than double the operating loss of \$6.7 million in 2004-05. Following from this, the return on assets declined to -8.2 per cent and the return on equity to -27.0 per cent.

ACTION is required to make income tax-equivalent payments to the ACT Government. However, ACTION did not incur a tax-equivalent expense in 2005-06 due to its operating loss. No dividend was announced for 2005-06.

ACTION receives community service obligation (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. CSO funding comprised 76 per cent of ACTION's total revenue in 2005-06.

ACTION AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	82	82	80
Total revenue	\$m	77	77	80
Profitability				
Operating profit before tax	\$'000	-6 654	-6 654	-14 153
Operating sales margin	%	-7.6	-7.6	-16.7
Cost recovery	%	92.0	92.0	85.1
Return on assets	%	-6.8	-6.8	-8.2
Return on equity ^c	%	-12.3	-12.3	-27.0
Financial management				
Debt to equity	%	18.4	18.4	17.6
Debt to total assets	%	12.2	12.2	5.5
Total liabilities to equity	%	51.2	51.2	57.8
Interest cover	times	-5.4	-5.4	-13.7
Current ratio	%	80.2	45.1	25.2
Leverage ratio	%	151.2	151.2	157.8
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding	\$'000	59 179	59 179	60 589

^a ACTION commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for ACTION. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Return on equity is lower than return on assets in each year of the reporting period because return on equity is based on profit after interest and tax while return on assets uses earnings before interest and tax. Although ACTION made no tax-equivalent payments in 2004-05 and 2005-06, it recorded an interest expense of more than \$900 000 in each of these years, which accounts for the difference between the profit measures. — Zero or rounded to zero.

8 Railways

The financial performances of five government trading enterprises (GTEs) in the rail sector are reported in this chapter. Together they controlled \$26.7 billion in assets and generated around \$6.6 billion in revenue in 2005-06.

Financial performance summaries, including performance indicators for each rail GTE and a summary of performance indicators for the sector as a whole, are presented after this introduction. The performance indicators are defined in chapter 1.

When making comparisons, consideration should be given to: differences in the nature and scale of the businesses; their individual market environments; a number of issues relating to the valuation of their assets; and the level of payments for community service obligations. Care should also be exercised when comparing data presented in this chapter with that presented in previous reports for two reasons.

1. The performance data presented in this report are based, for the first time, on the new Australian-equivalent International Financial Reporting Standards.
2. Data from GTE general purpose financial reports have been used for this report, whereas data presented in previous reports were based on government financial statistics. The reason for this change is set out in chapter 1.

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 Infrastructure Corporation (RIC) owns a large portion of the rural rail network in NSW. Its responsibilities have changed over the last five years. On 1 January 2004, the metropolitan functions of RIC were transferred to RailCorp. On 5 September 2004, the Australian Rail Track Corporation (ARTC) leased the NSW Interstate and Hunter Valley Networks for 60 years. The ARTC also entered into a management agreement with RIC to operate the Country Regional Network, with

Table 8.1 **Activities — rail GTEs, 2005-06**

Rail GTE	Jurisdiction	Activities			
		Track ^a	Freight transport	Urban passenger transport	Regional passenger transport
Rail Infrastructure Corporation	New South Wales	✓	x	x	x
Rail Corporation	New South Wales	✓	x	✓	✓
V/Line Passenger Corporation	Victoria	x	x	x	✓
Queensland Rail	Queensland	✓	✓	✓	✓
Australian Rail Track Corporation	Australian Government	✓	x	x	x

^a Refers to the ownership of mainline tracks and does not include ownership of sidings, terminals and other 'below track' infrastructure.

RIC retaining strategic ownership and the ARTC operating the infrastructure. The ARTC is also responsible for all operations relating to the greater part of the interstate rail networks, including track management services and the administration of rail access regimes.

Rail Corporation New South Wales (RailCorp) operates urban and regional rail passenger transport services and is responsible for managing rail infrastructure.

The V/Line Passenger Corporation (VPC) provides transportation services both to and within Victorian regional areas.

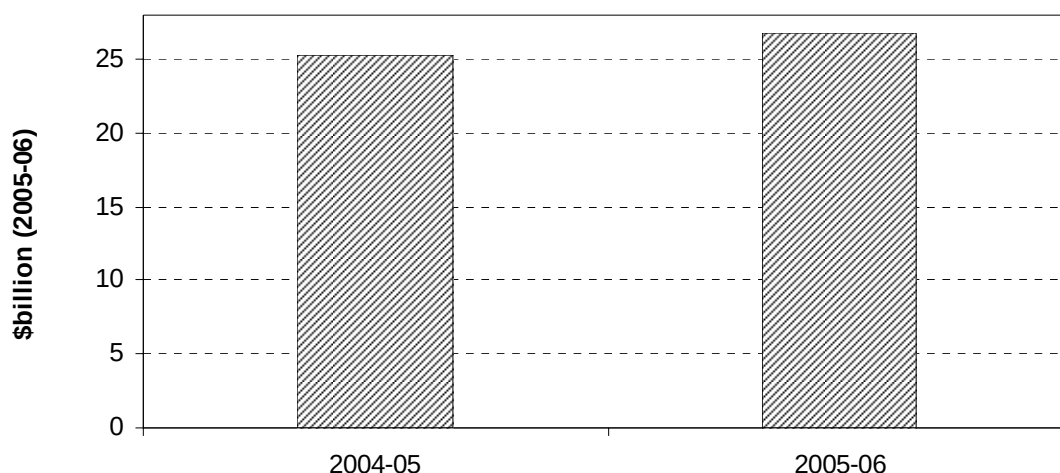
All of the rail GTEs monitored in this chapter were included in the rail sector of the previous *Financial Performance of Government Trading Enterprises* report.

The Public Transport Authority, which was included in the rail sector in previous reports has been moved to the urban transport sector for this report. This change was made because its main role is now the provision of passenger rail, bus and ferry services in metropolitan Perth. TransAdelaide — South Australia's rail GTE — is also included in the urban transport sector because it provides urban passenger services only. The urban transport sector is discussed in chapter 7.

There were also changes within the GTEs over the last five years. As described above, the metropolitan functions of RIC were transferred to RailCorp following a structural change to the NSW rail system and the ARTC leased the NSW Interstate and Hunter Valley Networks from RIC for 60 years.

The value of assets controlled by the GTEs monitored in 2005-06 is shown in figure 8.1.

Figure 8.1 Sector assets — rail GTEs^a



^a The value of sector assets is reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1).

Source: Productivity Commission estimates.

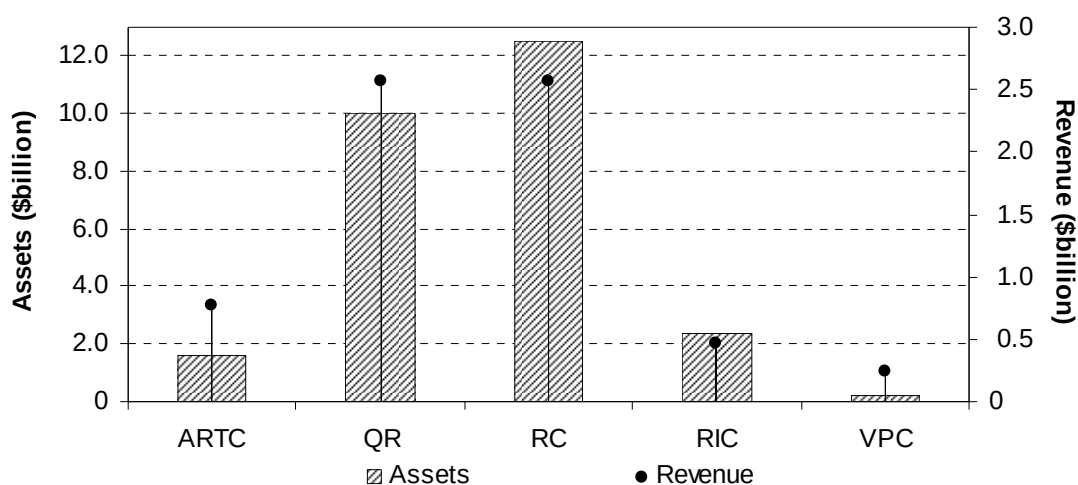
Total assets increased by 5.4 per cent to \$26.7 billion in 2005-06 in real terms. This increase occurred for four main reasons. First, QR acquired freight haulier ARG for \$446 million in 2005-06. Second, two rail operators received substantial transfers from government. ARTC obtained special government grants of \$270 million and buildings, land and other assets valued at \$256 million were transferred to RailCorp from other NSW Government transport organisations. Third, ARTC and RailCorp invested in capital infrastructure. Fourth, QR was exempted, under AASB 1 *First Time Adoption of AIFRS*, from including financial derivatives on the balance sheet in 2004-05. Instead, they were included on the balance sheet for the first time in 2005-06, increasing assets by \$693 million.

The relative size of each GTE monitored in 2005-06 in terms of asset values and revenue is shown in figure 8.2. RailCorp and QR are the largest rail GTEs. Together they comprise 85 per cent of the sector's assets and account for 78 per cent of the sector's revenue.

8.2 Market environment

Rail freight transport has been partly displaced in many of its traditional markets by road transport, causing rail's share of the market to decline over the last 30 years (ARA 2005). 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. Indeed,

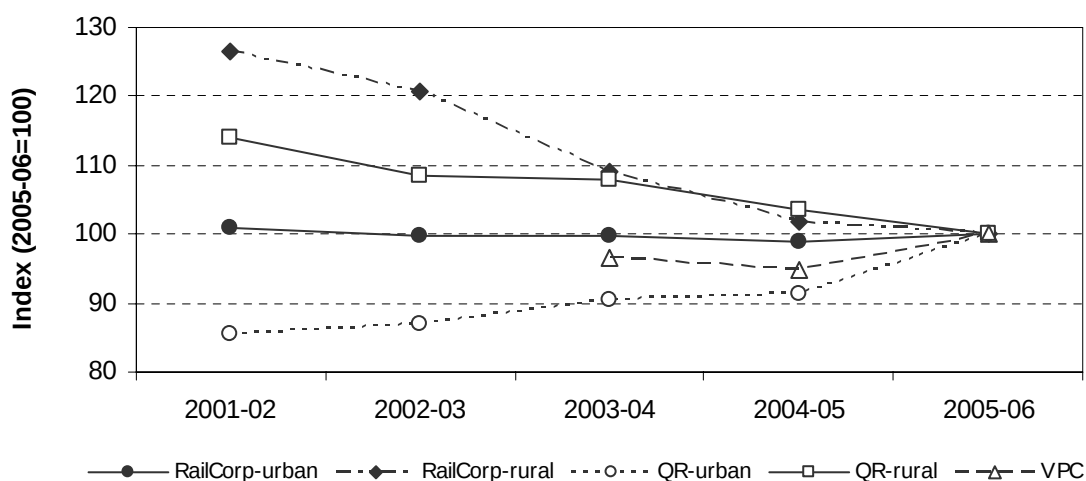
Figure 8.2 Assets and revenue — rail GTEs, 2005-06



Source: Productivity Commission estimates.

QR continued to expand its operations into the non-coal bulk freight market in 2005-06 with its acquisition of ARG.

Figure 8.3 Passenger trends — selected rail GTEs^a



^a QR-urban data refers to passenger trips on Queensland Rail's Citytrain services. QR-regional data refers to passenger trips on Traveltrain services. For 2004-05, QR-urban trips were conservatively estimated because of the introduction of a new ticketing system. RailCorp-urban data refers to passenger trips on CityRail and RailCorp-rural data refers to trips on CountryLink. CityRail and CountryLink were part of the State Rail Authority NSW (StateRail) until 2003-04 when the StateRail was subsumed into RailCorp. Data for CityRail and CountryLink for 2001-02 to 2005-06 was obtained from the RailCorp 2005-06 annual report. VPC data refers to rural rail passenger trips only.

Source: QR (2002, 2004, 2006); RailCorp (2006); VPC (2004, 2006).

Rail GTEs providing urban and regional passenger transport services have experienced increasing demand, whereas demand for rural passenger services have declined. For QR, demand for urban services increased each year since 2001-02, while demand for rural services has steadily declined. RailCorp experienced stable passenger numbers in urban services over the last five years and rural passenger services fell by over 20 per cent. The VPC was the only rail GTE to report positive growth in rural passenger numbers (figure 8.3).

Passenger charges are either set by, or subject to oversight by, external bodies. Maximum charges for RailCorp's CityRail services are regulated by the Independent Pricing and Regulatory Tribunal of NSW (IPART). Charges for CountryLink services are determined by the Minister for Transport after a recommendation from RailCorp's Board. Charges for QR's urban transport services are determined by Translink, a business unit within Queensland Transport. QR determines its own rural passenger charges but these are subject to ministerial oversight. In Victoria, the Minister for Transport determines charges for the VPC's transport services based on recommendations from the relevant government department, and subject to contractual obligations with the service provider.

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

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.

Access regimes were established to encourage competition in the market for rail service provision by stipulating the methods by which a third party can gain access to rail track. They are covered by Part IIIA of the *Trade Practices Act 1974*, which provides three ways of gaining access by:

1. using an existing, certified state-based access regime;

¹ In NSW, IPART may arbitrate access disputes. Access to the ARTC's network could 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.

-
2. seeking access under the terms and conditions specified in a voluntary undertaking approved by the Australian Competition and Consumer Commission (ACCC); or
 3. having a service declared which establishes the right of a party to negotiate access with the service provider.

Declaration also gives an access seeker the right to binding arbitration by the ACCC (NCC 2002).²

An application for a declaration is made to the National Competition Council (NCC). This initiates 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 ACCC, access seekers are unable to use the declaration process.

The ARTC manages parts of the interstate rail network, mainly in NSW, Victoria, SA and WA. The ARTC has a registered undertaking with the ACCC with respect to the terms and conditions by which it provides access to the network.

In Queensland, the QR Network Access Unit has been responsible for negotiating access with third-party operators and the development of network access provisions. The QR had an Access Undertaking, which became effective in 2001, to provide a framework for managing negotiations with access seekers. This undertaking remained in effect until Access Undertaking 2005 was endorsed on 30 June 2006. The Access Undertaking allows for negotiations with individual operators in some circumstances. However, for sections of the network that attract more competition there is a 'reference tariff' which is a set price for a nominated haul (QR 2006b).

The NSW Rail Access Undertaking, which commenced on 19 August 1996, controls access negotiations in NSW. The undertaking requires that revenue from the access seeker covers the direct costs of usage, including a 'levellised charge for variable MPM' (RIC 2002, p. 13).³

A feature of structural reform in some jurisdictions has been the separation and sale to the private sector of rail freight operations. In NSW, the freight operations of

² On 10 February 2006, COAG agreed to amend the economic regulation of significant infrastructure, including rail, to make access arrangements simpler and nationally consistent. In particular, they agreed that by 2010 there will be a streamlined certification process for access regimes in all States and Territories using the ARTC access undertaking as a model (COAG 2006).

³ A levellised MPM (major periodic maintenance) charge is an annual smoothed amount based on the anticipated long-term average of MPM expenditure.

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 (NRC) in January 2002.⁴ In contrast, the Victorian rural passenger rail provider — V/Line Passenger Pty Ltd — was purchased from the private sector in 2003 and now operates as a GTE.⁵

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.

Recent financial reforms include capital restructuring, the revaluation of assets, the identification and direct funding of community service obligations (CSOs), and the development of dividend policies. For example, since 2001-02, the role and responsibilities of RIC have changed substantially, as has its methodology for calculating the fair value of non-current assets. Since 2004-05, however, there have been few changes that substantially affect the assessment of performance over time.

8.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings.

The GTEs included in the rail sector recorded an aggregated operating profit before tax of \$682 million in 2005-06, a 142 per cent increase from 2004-05 in real terms. Individually, four of the five rail GTEs recorded a profit. The RIC reported a positive operating profit for the first time, because of changes to its responsibilities. In real terms RailCorp's profits increased tenfold to \$243 million and the ARTC's profits more than doubled to \$329 million. Although QR reported a \$93.5 million profit, this was down 64 per cent from 2004-05 in real terms, primarily because of reduced coal freight revenue.

The only rail GTE to record an operating loss was the VPC with a \$5.9 million loss in 2005-06. Under the Financial Reporting Directions of the Minister for Finance (FRD – 108) the VPC was designated to report as a 'not for profit' entity:

... since the primary obligation is the delivery of public transportation services to regional Victoria ... Neither the Corporation mission nor corporate strategy includes

⁴ The Australian, NSW and Victorian Governments were co-owners of NRC.

⁵ The VPC acquired National Express Group Australia (V/Line Passenger) Pty Ltd from the National Rail Group on 1 October 2003 at a cost of \$1.

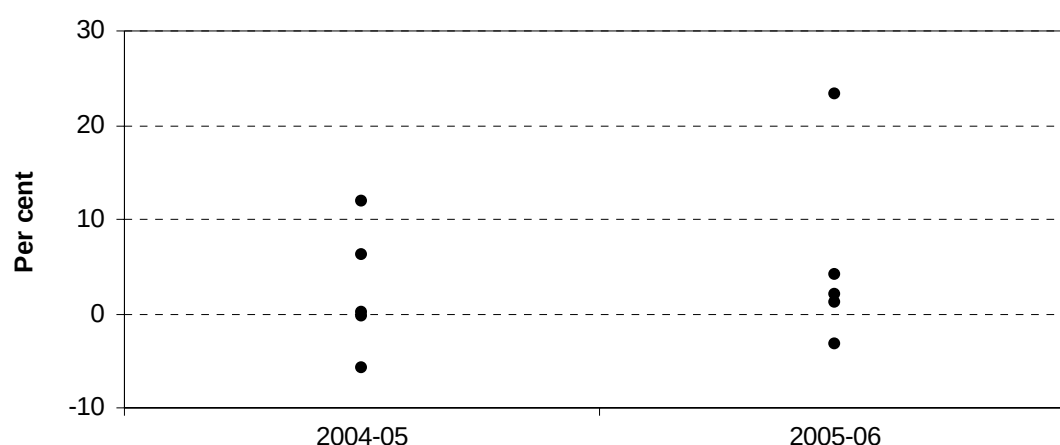
the achievement of profit as one of the consolidated entity's goals. As such, it has been deemed to be a not for profit entity. (V/Line 2006, p. 48)

Profitability, in terms of the rail sector's return on assets was 3.8 per cent in 2005-06, up from 2.2 per cent in 2004-05 but well below the risk-free benchmark rate of 5.4 per cent for 10-year Australian Government bonds (RBA 2007a). The ARTC was the only rail GTE to report a return on assets (23.2 per cent) above this rate. Across the sector the return on assets varied from -3.2 per cent to 23.2 per cent (figure 8.4). Overall, returns were well below those required by private operators, indicating that most rail GTEs are not operating on a commercially viable basis.

The return on equity for the sector also increased in 2005-06, to 3.9 per cent. The change in return on equity for each rail GTE mirrored the change in their return on assets.

The cost recovery ratio indicates the ability of an entity to generate an adequate revenue to meet expenses. For the sector as a whole the cost recovery ratio remained relatively stable at 93.7 per cent. However, there was considerable variation among individual rail GTEs. Two recorded an increase in their cost recovery ratio and three recorded a decrease, including RIC whose cost recovery ratio declined 25.1 percentage points to 44.5 per cent (figure 8.5). The ARTC and QR were the only rail GTEs to record cost recovery ratios over 100 per cent.

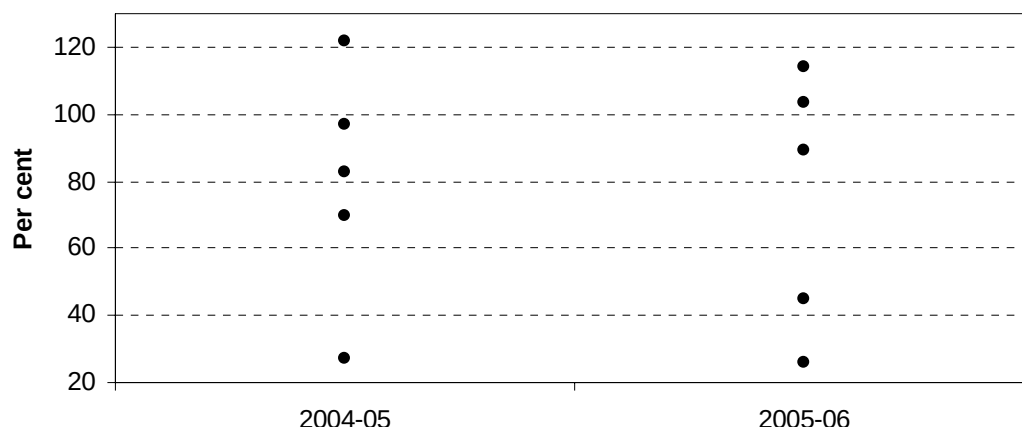
Figure 8.4 Return on assets — rail GTEs^a



^a 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 could not be calculated, the value of total assets at the end of the financial year was used.

Source: Productivity Commission estimates.

Figure 8.5 Cost recovery — rail GTEs^a



^a 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 government to cover operational deficits. Expense from operations are calculated by subtracting gross interest expense from total expenses.

Source: Productivity Commission estimates.

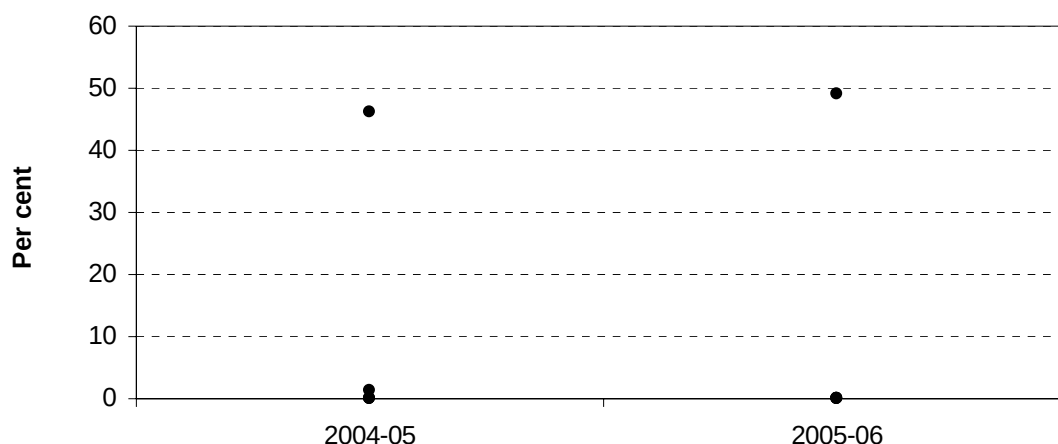
8.4 Financial management

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. Over the last five years, debt to total assets ratios for rail GTEs have been influenced by the acquisition and retirement of debt, and through changes in the total value of assets.

Three of the five rail GTEs operated debt free in 2005-06. The VPC and the ARTC have carried no debt in the last two years and RIC retired all debt in 2005-06. RailCorp carried debt for the first time in 2005-06 at a level equivalent to 0.1 per cent of its assets. QR carried debt equivalent to 49.1 per cent of its total assets, up from 46.0 per cent in 2004-05 (figure 8.6).

Under sound financial management, profits should 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. The level of interest cover for the two rail GTEs carrying debt differed considerably suggesting varied capacity to respond to changes in financial conditions. RailCorp can cover interest 105.6 times and QR can cover interest 1.3 times.

Figure 8.6 Debt to total assets — rail GTEs^a



^a 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.

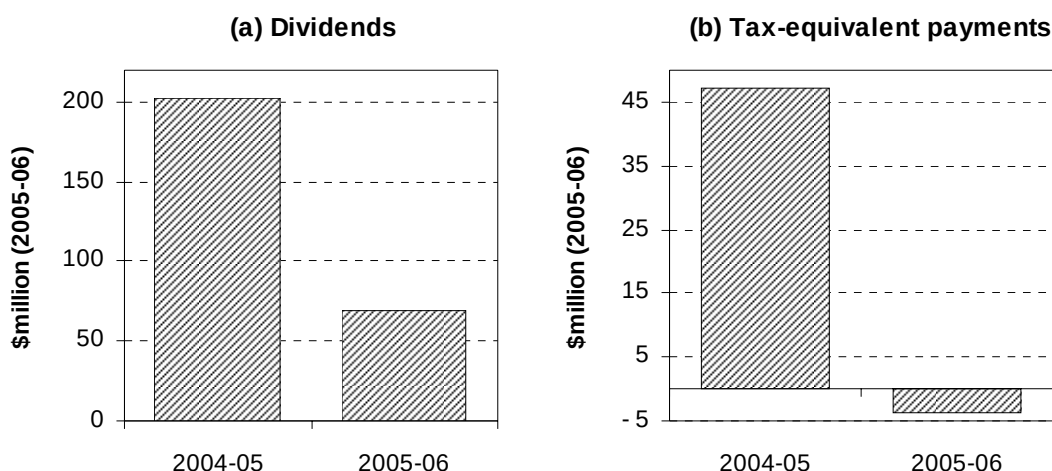
A current ratio of less than 100 per cent indicates the short-term obligations of the GTE might have to be met using sources of funds other than current assets. Both of the rail GTEs carrying debt recorded current ratios below 100 per cent for the last two years. RailCorp's current ratio fell from 71.7 per cent to 66.5 per cent in 2005-06 and QR's increased from 66.9 per cent to 72.4 per cent.

8.5 Transactions with government

As a part of the reform process, governments have sought to give GTEs a greater commercial focus, facilitate competitive neutrality and expose them to financial disciplines and regulations similar to those faced by privately-owned businesses. Dividends and income tax-equivalent expenses over the last two years are shown in figure 8.7.

Dividend payments from GTEs are a return on shareholder funds that impose capital disciplines and are consistent with competitive neutrality. QR was the only rail GTE to declare dividends in the last two years. It distributed \$68.5 million in 2005-06, a 66 per cent decrease in real terms from 2004-05, because of a lower operating profit.

Figure 8.7 Dividends and income tax-equivalent expenses — rail GTEs^a



^a The value of dividends and tax-equivalent expenses is reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1).

Source: Productivity Commission estimates.

QR was also the only rail GTE to record a tax-equivalent expense in the last two years. Its tax-equivalent expense decreased by 80 per cent in real terms in 2005-06 because of its lower operating profit.

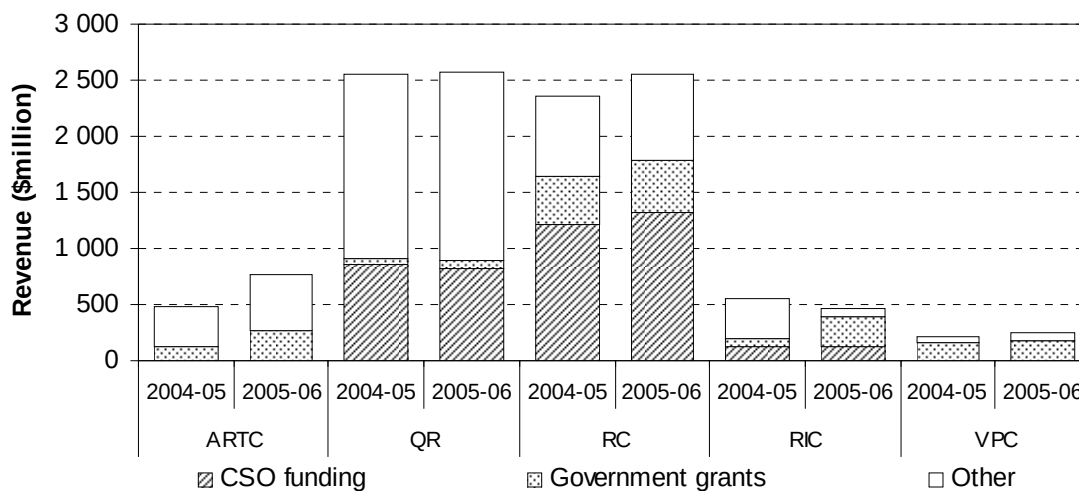
RailCorp and RIC were given exemptions from making tax-equivalent payments by the NSW Treasury. The VPC has reported an operating loss every year since it was established and is not required to make tax-equivalent payments.

The ARTC recorded a \$19.4 million tax benefit, offsetting QR's \$15.6 million tax expense to produce a net tax benefit for the rail sector in 2005-06.⁶

Governments have moved towards identifying, costing and explicitly funding community service obligations (CSOs) provided by rail GTEs. Three of the monitored rail GTEs, QR, RailCorp and RIC, received CSO funding in 2005-06. Overall, CSO funding to the rail sector was \$2.3 billion in 2005-06, accounting for 34 per cent of total revenue. This was a \$40.4 million (1.8 per cent) decrease in real terms from 2004-05. CSO funding forms a significant source of revenue for some rail GTEs. For example, CSO funding received by RIC for the cost of maintaining non-commercial rail lines accounted for 26 per cent of its revenue in 2005-06 (figure 8.8).

⁶ The ARTC's tax benefit represents an increase in deferred tax assets arising from assets revaluation. However, the ARTC did not record a current tax expense even though it recorded a \$60 million operating profit before tax.

Figure 8.8 Revenue sources — rail GTEs



Source: Productivity Commission estimates.

There are also implicit CSO payments if operations do not provide an adequate return. These can occur through government grants and services and equipment provided free of charge. The VPC, for example, does not receive CSO payments but does receive Victorian Government grants for the provision of public transport services to rural and regional areas. These grants totalled \$162 million in 2005-06, accounting for 66 per cent of revenue. The Victorian Government also provided VLocity trains free of charge to the VPC.

The level of government grants between 2004-05 and 2005-06 varied for some GTEs because of one-off funding agreements. However, the majority received a fairly stable level of government grants over the two years. Three of the five monitored rail GTEs received over 50 per cent of their revenue in 2005-06 from a combination of CSO payments and government grants.

8.6 Implications of the new accounting standards

From 2005-06, financial data for all monitored rail GTEs are based on the Australian-equivalent International Financial Reporting Standards (AIFRS). The adoption of the new accounting standard changed the recognition and measurement of some assets, liabilities and equity items, and affected the recording of income flows. These changes, which were discussed in the previous *Financial Performance of Government Trading Enterprises* report (PC 2006, chapter 3), have had a significant effect on the comparability over time of financial performance and financial management indicators.

The aggregate impact of the transition to AIFRS for the selected rail GTEs can be gauged by comparing 2004-05 data on an AIFRS and pre-AIFRS basis (table 8.2). Similar comparisons can be made by reference to each GTE summary.

Table 8.2 Whole of sector performance indicators 2004-05 to 2005-06^a

		Pre-AIFRS ^{b,c}		AIFRS ^b
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	24 522	24 205	26 723
Total revenue	\$m	6 123	6 161	6 613
Profitability				
Operating profit before tax	\$'000	381 349	269 079	681 835
Operating sales margin	%	9.8	8.0	13.8
Cost recovery	%	93.6	93.9	93.7
Return on assets	%	2.6	2.2	3.8
Return on equity	%	1.8	1.3	3.9
Financial management				
Debt to equity	%	21.8	22.4	24.8
Debt to total assets	%	15.7	15.9	17.7
Total liabilities to equity	%	38.6	40.9	46.7
Interest cover ^d	times	2.4	2.0	3.3
Current ratio	%	118.7	110.5	112.3
Leverage ratio	%	138.6	140.9	146.7
Payments to and from government				
Dividends	\$'000	193 100	193 100	68 530
Dividend to equity ratio	%	1.1	1.1	0.4
Dividend payout ratio	%	60.1	86.2	10.0
Income tax expense	\$'000	60 238	45 003	-3 765
CSO funding	\$'000	2 028 119	2 202 919	2 266 027

^a Figures are nominal values. ^b Rail GTEs commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2001-02 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for rail GTEs. ^c Data prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

8.7 GTE performance reports

Rail Infrastructure Corporation (NSW)

Rail Corporation NSW

V/Line Passenger Corporation (Victoria)

Queensland Rail

Australian Rail Track Corporation (Australian Government)

Rail Infrastructure Corporation (RIC) operates under the *Transport Administration Act 1988* and the *State Owned Corporations Act 1989*. It was formed on 1 January 2001 by merging the Rail Access Corporation, which was responsible for rail network management and access, and Rail Services Australia, which operated principally as a maintenance service provider.

Substantial changes have been made to the roles and responsibilities of RIC over the last three years. On 1 January 2004, the metropolitan functions of RIC were transferred to Rail Corporation NSW (RailCorp).¹ On 5 September 2004, the Australian Rail Track Corporation (ARTC) leased the NSW Interstate and Hunter Valley Networks for 60 years and commenced a management agreement with RIC to operate the Country Regional Network. RIC retains strategic ownership responsibilities and the ARTC is the infrastructure manager.

Both assets and liabilities decreased in 2005-06 (by \$38.3 million and \$9.4 million respectively). The decrease in assets was caused by a high level of depreciation of plant property and equipment. The decrease in liabilities was the net result of an increase in provisions and the elimination of debt, down from \$34.2 million in 2004-05. The current ratio increased by 53.3 percentage points to 85.8 per cent reflecting the increase in holdings of cash and cash equivalents and provisions.

The revenue from rendered services decreased by \$224 million, attributable to the restructuring of RIC's functions and the ongoing drought across NSW. Other major revenue in 2005-06 was from the NSW Government, including a contribution for debt reduction and working capital (\$90 million), community service obligation (CSO) payments (\$123 million),² and redundancy funding (\$180 million). While total revenue declined (\$84.5 million), the decrease in total expense was greater (\$249 million). As a result, RIC recorded its first positive pre-tax operating profit of \$21.9 million in 2005-06.

RIC received an exemption from tax-equivalent payments from the NSW Treasury in 2005-06.³ RIC does not make dividend payments.

¹ Metropolitan functions include, operating CityRail, owning and maintaining the metropolitan rail network and providing access to freight operators in the metropolitan area.

² The RIC receives CSO funding for the cost of maintaining non-commercial railway lines.

³ An exemption can be granted in exceptional circumstances. An application for exemption must be submitted to the NSW Treasury and the Treasurer can grant an exemption where both the following apply: First, the '... specific conditions warrant the Government business being regarded as non commercial ...' and '... secondly, competitive neutrality issues are unlikely to arise' (NSW Treasury 2003, p. 7).

RAIL INFRASTRUCTURE CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05 ^c	2004-05 ^c	2005-06
Size				
Total assets	\$m	2 379	2 380	2 342
Total revenue	\$m	553	550	465
Profitability				
Operating profit before tax	\$'000	-145 790	-142 851	21 905
Operating sales margin	%	-26.1	-25.3	5.8
Cost recovery	%	69.3	69.6	44.5
Return on assets	%	-6.0	-5.8	1.2
Return on equity	%	-6.9	-6.9	1.1
Financial management				
Debt to equity	%	1.6	1.6	—
Debt to total assets	%	1.4	1.4	—
Total liabilities to equity	%	13.0	14.7	14.4
Interest cover ^d	times	-56.2	-27.9	4.9
Current ratio	%	42.1	32.5	85.8
Leverage ratio	%	113.0	114.7	114.4
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding	\$m	133	133	123

^a Rail Infrastructure Corporation (RIC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for RIC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c On 5 September 2004, RIC leased the NSW Interstate and Hunter Valley rail corridors and dedicated metropolitan freight lines to the Sydney ports to the Australian Rail Track Corporation, for 60 years. ^d With the capitalisation of certain borrowings and borrowing costs, interest cover is not a reliable measure of RIC's ability to make interest payments. – Zero or rounded to zero.

Rail Corporation NSW (RailCorp) was established on 1 January 2004 under the *Transport Administration Amendment (Rail Agencies) Act 2003*, absorbing the functions of the State Rail Authority NSW (StateRail) and the metropolitan responsibilities of Rail Infrastructure Corporation.

RailCorp is responsible for the control and operation of CityRail and CountryLink in providing passenger rail transport. Additionally, RailCorp controls the metropolitan rail network and provides access to freight operators. Charges for RailCorp's CityRail services are regulated by the NSW Independent Pricing and Regulatory Tribunal. Charges for CountryLink services are determined by the Minister for Transport after a recommendation from the RailCorp Board.

Total assets increased by \$422 million (3.5 per cent) to \$12.5 billion in 2005-06, primarily due to growth in works-in-progress and the transfer of \$256 million worth of buildings, land and other assets from other NSW Government transport organisations.

RailCorp received \$2.6 billion in revenue in 2005-06, including \$527 million from passenger services, \$1.3 billion from community service obligation (CSO) payments, and \$474 million from subsidies and other contributions from government. Total expenses fell by 1.0 per cent to \$2.3 billion over the same period, producing a pre-tax operating profit of \$243 million, a twelve fold increase from 2004-05.

RailCorp is not subject to dividend payments.¹ In 2005-06, RailCorp was exempt from making tax-equivalent payments to the NSW Government.²

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. CSO payments represented 51 per cent of total revenue in 2005-06.

¹ Section 20S (Dividends) of the *State Owned Corporations Act 1989* does not apply to RailCorp under Section 17B of the *Transport Administration Act 1988*.

² An exemption can be granted in exceptional circumstances. An application for exemption must be submitted to the NSW Treasury and the Treasurer can grant an exemption where both the following apply: First, the '... specific conditions warrant the Government business being regarded as non commercial ...' and '... secondly, competitive neutrality issues are unlikely to arise' (NSW Treasury 2003, p. 7).

RAIL CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		<i>Pre-AIFRS^{a,b}</i>		<i>AIFRS^a</i>
	<i>Units</i>	<i>2004-05</i>	<i>2004-05</i>	<i>2005-06</i>
<i>Size</i>				
Total assets	\$m	12 188	12 125	12 547
Total revenue	\$m	2 362	2 362	2 560
<i>Profitability</i>				
Operating profit before tax	\$'000	92 581	20 275	243 155
Operating sales margin	%	3.6	0.6	9.0
Cost recovery	%	77.4	82.4	89.4
Return on assets	%	0.8	0.2	2.0
Return on equity	%	0.8	0.2	2.1
<i>Financial management</i>				
Debt to equity	%	—	—	0.1
Debt to total assets	%	—	—	0.1
Total liabilities to equity	%	6.4	7.3	7.1
Interest cover ^c	times	..	81.8	105.6
Current ratio	%	85.2	71.7	66.5
Leverage ratio	%	106.4	107.3	107.1
<i>Payments to and from government</i>				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding	\$'000	1 041 505	1 216 305	1 314 927

^a Rail Corporation NSW (RailCorp) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for RailCorp. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c With the capitalisation of certain borrowings and borrowing costs, interest cover is not a reliable measure of RailCorp's ability to make interest payments. — Zero or rounded to zero. .. Not applicable.

The V/Line Passenger Corporation (VPC) was established on 15 July 2003 as a statutory rail corporation under the *Rail Corporations Act 1996*. VPC acquired National Express Group Australia (V/Line Passenger) Pty Ltd from the National Rail Group and commenced operation on 1 October 2003.¹

The VPC provides public transport services to regional areas, comprising coach and rail passenger services. It is also responsible for maintaining regional train stations and providing a network of V/Line ticket and service agents.

Total assets increased by 0.7 per cent to \$185 million in 2005-06, while total liabilities increased 14 per cent to \$66.1 million. The increase in liabilities was primarily because of higher current liabilities, in particular accruals.

The VPC's pre-tax operating loss increased by \$5.3 million, to \$5.9 million in 2005-06. Total revenue was \$247 million, an increase of \$31.8 million (15 per cent) and total expenses increased by \$37.1 million (17 per cent) to \$253 million. Part of the increase in both revenue and expenses was attributable to the provision of new VLocity trains free of charge by Rolling Stock Holdings Pty Ltd, valued at \$18.6 million. This was recorded as both a revenue and a value-in-kind expense.

The VPC is subject to dividend and tax-equivalent payments. However, the VPC has made neither form of payment since commencing operation. Under the Financial Reporting Directions of the Minister for Finance (FRD – 108) the VPC was designated to report as a 'not for profit' entity:

... since the primary obligation is the delivery of public transportation services to regional Victoria. ... Neither the Corporation mission nor corporate strategy includes the achievement of profit as one of the consolidated entity's goals. As such, it has been deemed to be a not for profit entity. (V/Line 2006, p. 48)

Further, when the VPC has incurred tax losses they have not been recognised in its financial records as the Board determined there was little likelihood of future profits to offset prior year tax losses.

The Victorian Government subsidises the VPC's provision of public transport services to rural and regional areas through recurrent government grants.² These grants totalled \$162 million in 2005-06, accounting for 66 per cent of total revenue. The VPC did not receive community service obligation payments in 2005-06.

¹ The VPC is the parent corporation and the operating result reported in this chapter is for the consolidated entity.

² The VPC also received provision of VLocity trains free of charge from the government.

V/LINE PASSENGER (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	183	183	185
Total revenue	\$m	215	215	247
Profitability				
Operating profit before tax	\$'000	-650	-650	-5 904
Operating sales margin	%	-0.6	-0.6	-2.7
Cost recovery	%	27.3	27.3	26.0
Return on assets	%	-0.4	-0.4	-3.2
Return on equity	%	-0.5	-0.5	-4.8
Financial management				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity	%	46.2	46.2	55.7
Interest cover	times	..	..	..
Current ratio	%	36.2	20.0	23.5
Leverage ratio	%	146.2	146.2	155.7
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	—	—	—
CSO funding	\$'000	—	—	—

^a The V/Line Passenger (VPC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the VPC. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. — Zero or rounded to zero.

Queensland Rail (QR) is subject to the *Transport Infrastructure Act 1994* and the *Government Owned Corporations Act 1993*. QR manages Queensland's rail infrastructure, provides freight services in regional Queensland, and provides passenger rail services in the Brisbane metropolitan area and between key regional centres. It is also involved in freight transport in NSW, Victoria, WA and SA.

QR is subject to an Access Undertaking for third-party operators. Service charges are set by QR's Network Access Unit subject to floor and ceiling prices determined by the Queensland Competition Authority. The Unit operates separately from QR's other business units. Passenger service charges are determined by QR.

Total assets increased by around \$1.7 billion (21 per cent) in 2005-06 and total liabilities increased by \$1.4 billion (25 per cent). Part of the increase in both assets and liabilities in 2005-06 was attributable to the acquisition of freight haulier ARG for \$446 million, financed through borrowing. The inclusion of financial derivatives for the first time in 2005-06 also increased both assets and liabilities by \$693 million and \$637 million respectively.¹

The pre-tax operating profit was \$93.5 million in 2005-06, a decrease of \$154 million from 2004-05. While total revenue increased 1.0 per cent to \$2.6 billion, total expenses increased 7.8 per cent to \$2.5 billion. The primary reasons for decreased profits were reduced coal freight revenue, lower community service obligation (CSO) payments and increased expenses across the organisation.

The Queensland Government made \$784 million in CSO payments to QR in 2005-06 under Transport Services Contracts. These payments were for the provision of infrastructure, urban and intercity passenger services, low volume freight services, and concession fares. QR also received \$44.6 million of 'shareholder agreement revenue' in 2005-06.² Together these payments accounted for 32 per cent of revenue.

QR made provision for a dividend payment of \$68.5 million in 2005-06, down 65 per cent from 2004-05, because of lower net profits. QR recorded an income tax-equivalent expense of \$15.7 million.

¹ Under AASB 1 *First time Adoption of AIFRS*, QR was exempted from applying AASB 132 *Financial Instruments: Presentation* and AASB 139 *Financial Instruments: Recognition and Measurement* until 1 July 2005.

² Under the shareholder agreement QR receives funding for costs incurred resulting from the Queensland Government's (shareholder) request to carry out activities or adopt policies that QR would not do on a commercial basis.

QUEENSLAND RAIL (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^c
Size				
Total assets	\$m	8 557	8 299	10 033
Total revenue	\$m	2 503	2 549	2 574
Profitability				
Operating profit before tax	\$'000	287 358	247 991	93 515
Operating sales margin	%	21.8	19.9	14.4
Cost recovery	%	127.9	121.9	113.9
Return on assets	%	6.5	6.2	4.1
Return on equity	%	7.8	6.7	2.8
Financial management				
Debt to equity	%	131.1	147.6	155.1
Debt to total assets	%	44.6	46.0	49.1
Total liabilities to equity	%	193.9	221.0	245.6
Interest cover	times	2.1	1.9	1.3
Current ratio	%	64.1	66.9	72.4
Leverage ratio	%	293.9	321.0	345.6
Payments to and from government				
Dividends	\$'000	193 100	193 100	68 530
Dividend to equity ratio	%	6.6	7.0	2.5
Dividend payout ratio	%	85.0	111.6	88.0
Income tax expense	\$'000	60 238	74 721	15 662
CSO funding	\$'000	853 600	853 600	828 100

^a Queensland Rail (QR) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for QR. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c QR reported financial derivatives for the first time in 2005-06. Their inclusion increased the value of assets and liabilities by \$693 million and \$637 million respectively.

The Australian Rail Track Corporation Ltd (ARTC) was established on 28 February 1998 and operates as an access provider and infrastructure manager. The ARTC owns interstate tracks, principally in SA and WA, and manages interstate tracks in NSW 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 the ARTC.² These guidelines specify floor and ceiling access prices based on ARTC's costs and risk profile.

The ARTC's assets increased by \$399 million (33 per cent) to \$1.6 billion in 2005-06. This includes an increase of \$167 million in property, plant and equipment, a decrease of \$92.3 million in the holdings of cash and cash equivalents and the receipt of a \$270 million special government grant.

Total revenue increased by \$280 million (58 per cent) in 2005-06. This was the result of a \$170 million increase in Special Government Grants from the Australian Government, a \$44.1 million (18 per cent) increase in access fee revenue and a \$66.7 million (76 per cent) increase in revenue received from the Country Regional Network. The increase in revenue was partially offset by a \$95.4 million (28 per cent) increase in total expenses, primarily resulting from higher infrastructure maintenance and employee benefit expenses. Overall, pre-tax operating profit increased by \$185 million (128 per cent) to \$329 million in 2005-06.

The ARTC is subject to dividend and tax-equivalent payments. All operating profits were reinvested in the network and no dividends were declared in 2005-06. The ARTC recorded an income tax-equivalent benefit of \$19.4 million in 2005-06. Division 58 of the *Income Tax Assessment Act 1997* entitles the ARTC to value its assets for tax purposes at the book value recorded in the accounts of its precursor, the Australian National Railways Corporation. This is a higher value than that used by ARTC for accounting purposes and generates higher depreciation for taxation purposes, leading to significant tax benefits.

The ARTC does not receive community service obligation funding.

¹ The NSW Government agreed in December 2003 to lease the Interstate and Hunter Valley networks to ARTC for 60 years. This lease commenced on 5 September 2004.

² The ARTC's voluntary access undertaking was approved by the ACCC in May 2002. The undertaking binds the ARTC for five years.

AUSTRALIAN RAIL TRACK CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 216	1 218	1 616
Total revenue	\$m	490	486	767
Profitability				
Operating profit before tax	\$'000	147 850	144 314	329 164
Operating sales margin	%	24.3	23.8	39.4
Cost recovery	%	96.8	97.1	103.4
Return on assets	%	12.2	11.9	23.2
Return on equity	%	13.6	16.0	27.7
Financial management				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity	%	11.5	12.2	12.6
Interest cover	times	..	..	..
Current ratio	%	734.2	797.3	752.6
Leverage ratio	%	111.5	112.2	112.6
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	..	..	..
Dividend payout ratio	%	..	..	..
Income tax expense ^c	\$'000	—	-29 718	-19 427
CSO funding	\$'000	—	—	—

^a Australian Rail Track Corporation (ARTC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for ARTC. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. ^c ARTC incurred a negative tax expense because of deferred tax assets. It reported a current tax expense of zero. .. Not applicable. — Zero or rounded to zero.

9 Ports

The financial performances of 19 port government trading enterprises (GTEs) are reported in this chapter. At the end of 2005-06, they controlled \$7.7 billion in assets and generated \$1.3 billion in revenue.

These GTEs vary in size and the range of services they provide. The principal activities undertaken are the provision and maintenance of port infrastructure and, in some cases, port services such as mooring, stevedoring and pilotage.

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 defined in chapter 1.

When making comparisons, consideration should be given to: differences in the nature and scale of the businesses; their individual market environments; a number of issues relating to the valuation of their assets; and the level of payments for community service obligations. Care should also be exercised when comparing data presented in this chapter with that presented in previous reports for two reasons.

1. The performance data presented in this report are based, for the first time, on the new Australian-equivalent International Financial Reporting Standards (AIFRS).
2. Data from GTE general purpose financial reports have been used for this report, whereas data presented in previous reports were based on government financial statistics. The reason for this change is set out in chapter 1.

9.1 Monitored GTEs

The port GTEs monitored in this report do not all undertake the same activities, although the management of port facilities is common to almost all (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.

A number of port GTEs also have interests in other areas of business, such as airports. For example, the Port of Brisbane Corporation (PBC) has a substantial

Table 9.1 Activities — port GTEs, 2005-06

<i>Port GTE</i>	<i>Jurisdiction</i>	<i>Activities</i>				
		<i>Port facilities management</i>	<i>Pilotage</i>	<i>Stevedoring</i>	<i>Cold storage</i>	<i>Airport operations</i>
Newcastle Port Corporation	NSW	✓	✓	X	X	X
Port Kembla Port Corporation	NSW	✓	✓	X	X	X
Sydney Ports Corporation	NSW	✓	✓	X	X	X
Port of Melbourne Corporation	Victoria	✓	X	X	X	X
Victorian Regional Channels Authority ^a	Victoria	X	X	X	X	X
Central Queensland Ports Authority ^b	Queensland	✓	✓	✓	X	X
Port of Brisbane Corporation	Queensland	✓	X	X	X	X ^c
Cairns Port Authority	Queensland	✓	X	X	X	✓
Townsville Port Authority	Queensland	✓	✓	X	X	X
Ports Corporation of Queensland	Queensland	✓	✓	X	X	X
Mackay Port Authority	Queensland	✓	X	X	X	✓
Fremantle Port Authority	WA	✓	X	X	X	X
Bunbury Port Authority	WA	✓	✓	X	X	X
Port Hedland Port Authority	WA	✓	✓	X	X	X
Dampier Port Authority	WA	✓	X	X	X	X
Geraldton Port Authority	WA	✓	✓	X	X	X
Albany Port Authority	WA	✓	✓	X	X	X
Tasmanian Ports Corporation ^d	Tasmania	✓	✓	✓	✓	✓
Darwin Port Corporation	NT	✓	✓	X	X	X

^a The Victorian Regional Channels Authority began operations on 1 April 2004. It manages channels in the port waters of Geelong and oversees channel operations in the ports of Hastings and Portland ^b The Central Queensland Ports Authority was formed on 1 July 2004, from the merger of the Port Authorities responsible for the Port of Gladstone and Port Alma (Rockhampton). ^c The Port of Brisbane Corporation holds a 37 per cent interest in Brisbane Airport Corporation Holdings. It is not directly involved in the operation of the airport. ^d The Tasmanian Ports Corporation was incorporated on 1 July 2005. It began trading on 1 January 2006 following the amalgamation of Burnie Port Corporation, Hobart Ports Corporation, Port of Devonport Corporation and Port of Launceston Pty Ltd.

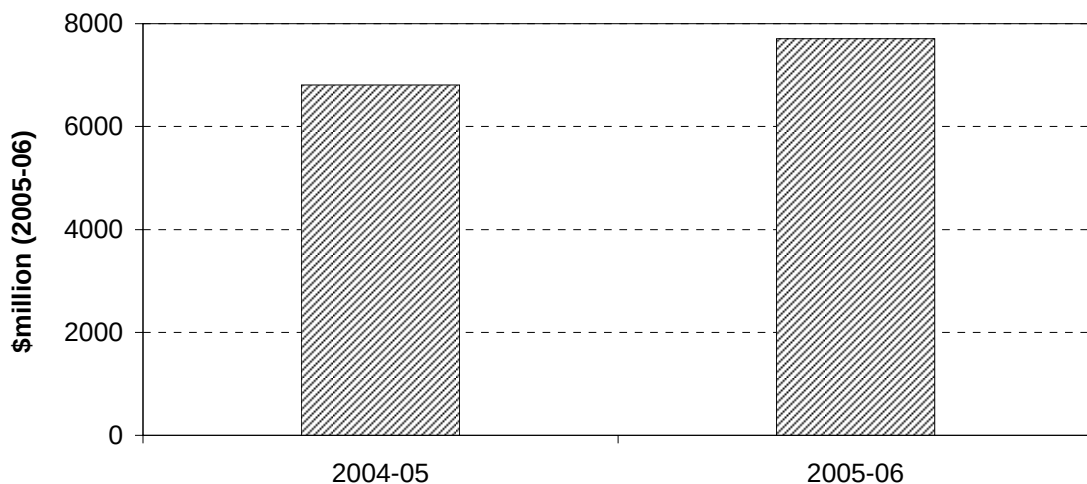
interest in Brisbane Airport,¹ and Hobart International Airport is a wholly owned subsidiary of Tasmanian Ports Corporation (TPC). The Cairns Port Authority and Mackay Port Authority also own and operate airports.

Changes to the range of services should be taken into account when comparing financial performances over time. 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 set of monitored port GTEs changed in 2005-06, as the TPC replaced Burnie Port Corporation (BPC), Hobart Ports Corporation (HPC), Port of Devonport Corporation (PDC) and Port of Launceston Pty Ltd (Port of Launceston).

Between 2004-05 and 2005-06, total assets controlled by port GTEs grew by \$897 million (13 per cent) in real terms (figure 9.1). This was mainly attributable to the inclusion of the TPC, which had assets of \$244 million in 2005-06, and to real increases of \$370 million and \$209 million in the assets of the Central Queensland Ports Authority (CQPA) and the Port of Brisbane Corporation (PBC) respectively, mostly because of capital works.

Figure 9.1 Sector assets — port GTEs^a



^a The value of sector assets is reported in 2005-06 dollars using the ABS implicit price deflator — gross fixed capital formation for public corporations (chapter 1).

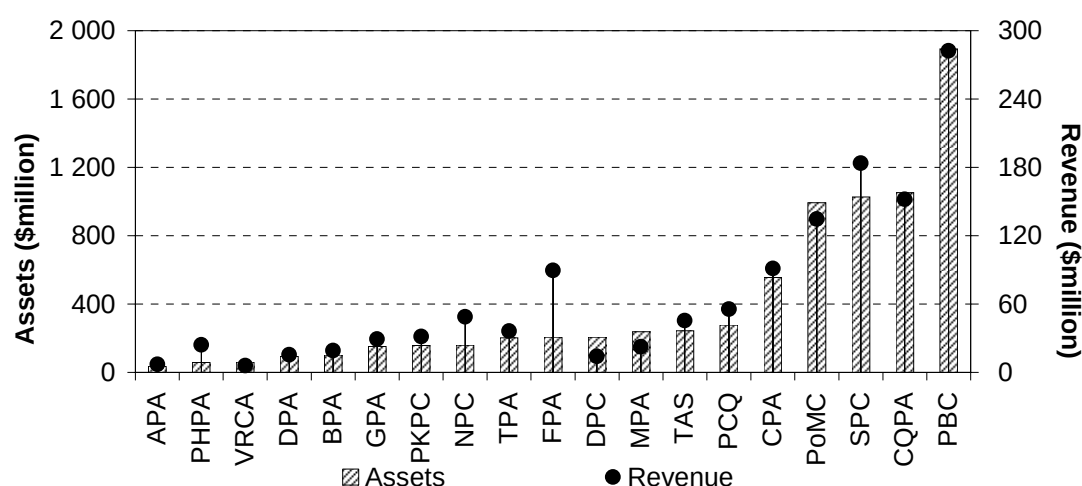
Source: Productivity Commission estimates.

¹ The PBC owned 37 per cent of Brisbane Airport Corporation Holdings in 2005-06. These airport investments are not consolidated in PBC's financial accounts as it does not own a controlling interest in the airport.

The size of the monitored port GTEs — in terms of revenue and the value of assets controlled — varied substantially in 2005-06 (figure 9.2). Based on asset value, the largest port GTE in 2005-06 was the PBC (\$1.9 billion) and the smallest was Albany Port Authority (\$36.0 million). The PBC accounted for nearly 25 per cent of sector assets in 2005-06 and 22 per cent of sector revenue.

There are also differences across jurisdictions in the operating principles established for port GTEs. These differences include varying emphasis on commercial and other objectives such as trade facilitation and regional development. In most jurisdictions, port GTEs operate under a jurisdiction-specific, GTE-wide corporatisation framework.

Figure 9.2 **Assets and revenue — port GTEs, 2005-06**



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 of throughput and size of the markets served, changing market environments do not impact on all GTEs uniformly.

Port GTEs with a diversified range of cargoes are less affected by market trends in key commodities, but usually retain an exposure to changes in the overall level of economic activity. Port GTEs relying on a single commodity for a large share of total throughput — such as the Newcastle Port Corporation, where coal accounted for 93 per cent of throughput in 2005-06 — can be substantially affected by changes in market conditions for that commodity.

Corporate reforms

Government reforms in 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 this 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. This involves the port authority concentrating on the supply of core activities only, with the more contestable waterfront services, such as stevedoring and pilotage, contracted out to the private sector.

The primary aim of these reforms was to establish clear objectives that eliminate any conflicts arising out of the commercial and non-commercial activities of the GTE, as well as replicating 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.

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 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

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 remained with the VCA, which was renamed the Victorian Regional Channels Authority (VRCA) and commenced operations on 1 April 2004.

In Queensland, the Gladstone Port Authority was amalgamated with the smaller Port of Alma (Rockhampton) in July 2004, forming the CQPA.

In Tasmania, the BPC, the HPC, the PDC and the Port of Launceston merged to form the TPC in 2005-06. The TPC was incorporated on 1 July 2005 and began trading as TasPorts on 1 January 2006, when it took over the assets and infrastructure of the four merged entities.

Port charges

A number of reforms have led to improved pricing and allocative mechanisms over the last five years. Volume-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 were previously regulated by the Essential Services Commission (ESC). The ESC introduced a price monitoring regulatory framework that applied from 1 July 2005. The framework involves port operators determining their own reference tariffs which are then subject to monitoring by the ESC. Port operators and users, however, are able to negotiate prices that differ from the tariff. In all other jurisdictions, port charges are determined by the board of each GTE, but are generally subject to the approval of the relevant minister.

9.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings.

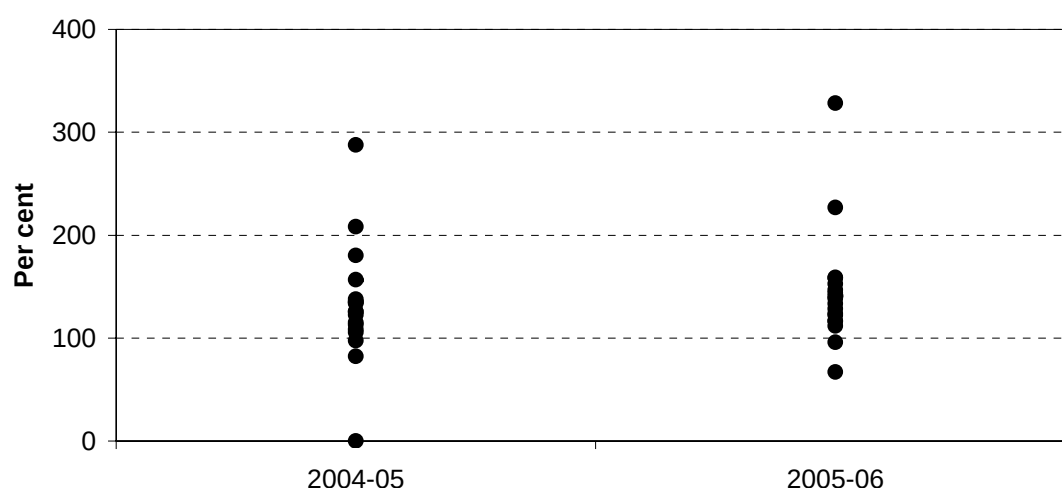
The monitored port GTEs recorded a total pre-tax operating profit of \$419 million in 2005-06, representing a \$42.0 million (11 per cent) increase in real (inflation-adjusted) terms from 2004-05. All except two port GTEs — the TPC and the Darwin Port Corporation (DPC) — achieved a positive operating profit in 2005-06, the same number as in 2004-05 (but different GTEs).

The cost recovery ratio for the port sector improved slightly from 156.9 per cent in 2004-05 to 159.2 per cent in 2005-06. Most port GTEs were able to fully recover their costs in 2005-06 (figure 9.3), with only the TPC and the DPC having cost recovery ratios below 100 per cent. The median cost recovery rate was 138.4 per cent, with the highest at 328.2 per cent (the PBC) and lowest at 67.2 per cent (the DPC).

The increased level of operating profits in 2005-06 was reflected in an improvement in the overall sector return on assets, which rose from 6.7 per cent in 2004-05 to 7.1 per cent in 2005-06. All but two port GTEs reported positive returns (up to 12.4 per cent) in 2005-06 (figure 9.4). The TPC and the DPC recorded returns of -0.8 per cent and -3.0 per cent respectively.

The aggregate sector rate of return on assets of 7.1 per cent in 2005-06 was greater than the risk-free rate of return.² This suggests that the port sector as a whole in 2005-06 achieved at least a minimum commercial rate of return, represented by the risk-free rate. The median rate of return on assets for the monitored port GTEs, at 6.0 per cent in 2005-06, was also above the risk-free rate. Eight of the 19 monitored port GTEs failed to achieve a return on assets equal to or greater than the risk-free rate in that year.

Figure 9.3 Cost recovery — port GTEs^a

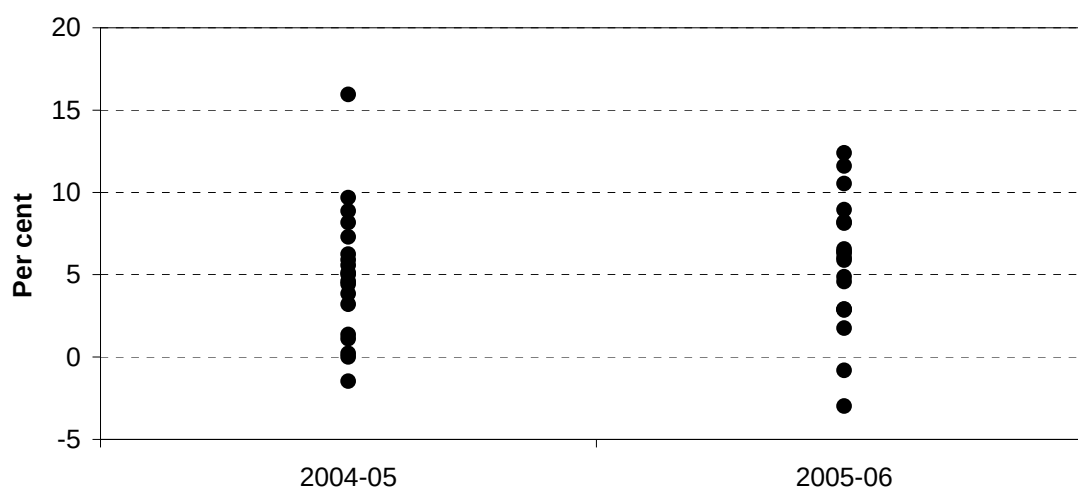


^a Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting from total revenue, investment income and receipts from governments to cover operational deficits. Expenses from operations are calculated by subtracting gross interest expense from total expenses.

Source: Productivity Commission estimates.

² The risk-free rate of return is defined as the 2005-06 interest rate on 10-year Australian Government bonds of 5.4 per cent (RBA 2007a).

Figure 9.4 Return on assets — port GTEs^a



^a 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 GTE's earnings for the year expressed as a proportion of equity held in the business — was similar to the trend in profitability and return on assets in 2005-06. The sector return on equity increased from 5.8 per cent in 2004-05 to 6.8 per cent in 2005-06.

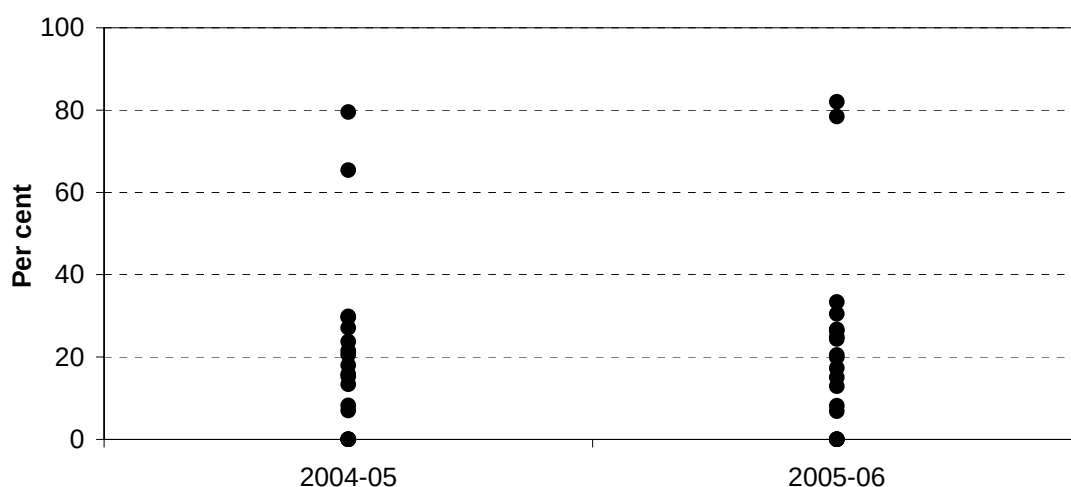
9.4 Financial management

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.

There is considerable diversity in the capital structure of port GTEs, as measured by the debt to total assets ratio (figure 9.5). Four port GTEs operated debt free in 2005-06, while two had debt to assets ratios of about 80 per cent. The median debt to assets ratio of port GTEs was 19.9 per cent in 2005-06, and the sector debt to assets ratio was 22.6 per cent. Most port GTEs operate with a relatively low level of borrowing.

In most cases, a decline in the debt position of port GTEs was achieved through retirement of debt. For example, the Townsville Port Authority (TPA) reduced its debt by 18 per cent (in real terms) from 2004-05 to 2005-06. This contributed to a

Figure 9.5 Debt to total assets — port GTEs^a



^a The Victorian Regional Channels Authority, Ports Corporation of Queensland, Mackay Port Authority and Port Hedland Port Authority operated debt free in both 2004-05 and 2005-06. 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.

fall in its debt to total assets ratio from 8.2 per cent to 6.9 per cent. An exception was the Sydney Ports Corporation (SPC), which recorded a decrease in its debt to total assets ratio from 18.0 per cent in 2004-05 to 17.3 per cent in 2005-06, despite a slight increase in the level of its debt. The decline in the debt ratio was a result of a 2.9 per cent real increase in the value of SPC's assets.

Interest cover, a measure of the capacity to meet periodic interest payments out of current earnings, was 5.8 times for the port sector in 2005-06. This is slightly higher than in 2004-05 (5.6 times). Given their (generally) low levels of debt, port GTEs would be well placed to continue meeting borrowing costs in the event of interest rate increases or a downturn in trade throughput.

The ability of port GTEs to meet short-term liabilities from short-term assets improved slightly in 2005-06, with the current ratio for the port sector increasing to 183.3 per cent from 175.6 per cent in 2004-05. However, three GTEs recorded a current ratio of less than 100 per cent in 2005-06 — this indicates that the short-term obligations of these GTEs may need to be met from sources of funds other than current assets.³

³ Current assets comprise cash and other assets that, in the ordinary course of operations, would be available for conversion into cash within 12 months after the end of the reporting period.

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 2.

Owner-governments generally require their port GTEs to make dividend and tax-equivalent payments, as well as pay 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 2005-06, seven of the port GTEs had dividend payout ratios of 50 per cent or greater. Five port GTEs did not declare a dividend in 2005-06.

Port GTEs recorded a total of \$110 million in tax-equivalent expenses in 2005-06 and declared dividends totalling \$122 million. The level of tax-equivalent expenses and dividends varies from year to year (figure 9.6). For the sector as a whole, dividends increased by 31 per cent in real terms from 2004-05 to 2005-06, reflecting the growth in profitability. Total income tax-equivalent expenses, which fell by 11 per cent, did not increase in line with profitability.⁴

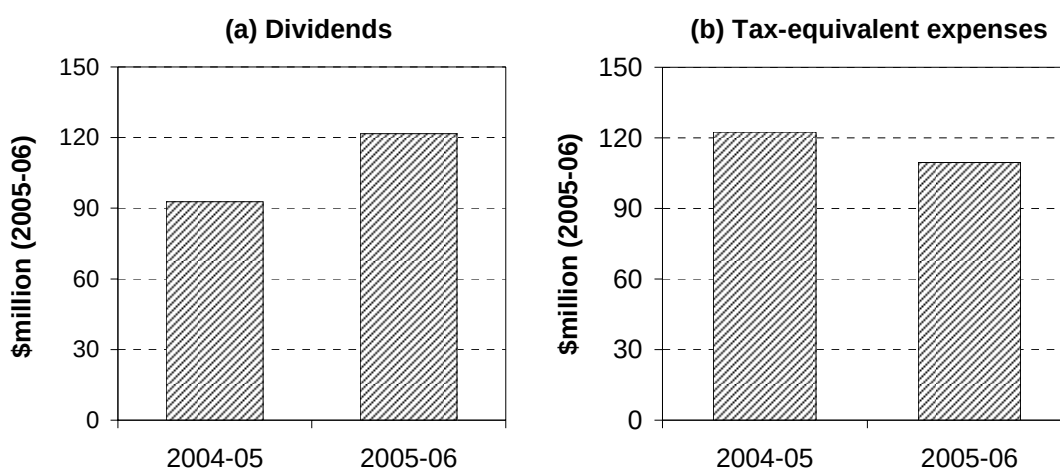
Under agreed reforms, port GTEs required to undertake non-commercial activities should receive CSO funding equivalent to the net cost incurred through these non-commercial activities.

The DPC is the only port GTE that receives CSO funding — \$2.3 million in 2005-06. The payments were to cover costs associated with small craft services, tourism and real estate, cruise and defence facilities, security of City Wharves, and the Swires and Hai Win shipping services. The amount of CSO funding received by the DPC declined from 2004-05, when it received \$3.0 million.

Some port GTEs receive payments from government that are not conditional on meeting particular non-commercial or other obligations, and so are not reported as CSOs. Such funding is usually in the form of capital or recurrent grants. For

⁴ This result was partly attributable to the PoMC, which recorded an income tax-equivalent expense of \$11.2 million in 2004-05 but a tax-equivalent benefit of \$6.2 million in 2005-06. This occurred despite a 31 per cent real increase in pre-tax operating profit. The PoMC's initial tax-equivalent expense of \$12.7 million for 2005-06 was adjusted downwards for a total of \$18.9 million in tax concessions for research and development associated with its channel deepening project.

Figure 9.6 Dividends and tax-equivalent expenses — port GTEs^a



^a The value of dividends and tax-equivalent expenses are reported in 2005-06 dollars using the ABS implicit price deflator — gross fixed capital formation for public corporations (chapter 1).

Source: Productivity Commission estimates.

example, the Dampier Port Authority (DPA) received \$7.8 million in contributions from the WA Government in 2005-06 upon commencement of operations of its new bulk liquids berth. This amount represented 50 per cent of the DPA's total revenue in 2005-06.

9.6 Implications of the new accounting standards

From 2005-06, financial data for all monitored port GTEs are based on AIFRS. The adoption of the new accounting standard changed the recognition and measurement of some assets, liabilities and equity items, and affected the recording of income flows. These changes, which were discussed in the previous *Financial Performance of Government Trading Enterprises* report (PC 2006, chapter 3), have had a significant effect on the comparability over time of financial performance and financial management indicators.

The aggregate impact of the transition to AIFRS for the selected port GTEs can be gauged by comparing 2004-05 data on an AIFRS and pre-AIFRS basis (table 9.2). Similar comparisons can be made by reference to each GTE summary.

PORTS

Table 9.2 Whole of sector performance indicators, 2004-05 to 2005-06^a

		Pre-AIFRS ^{b,c}	AIFRS ^b	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	6 415	6 505	7 708
Total revenue	\$m	994	1 144	1 288
Profitability				
Operating profit before tax	\$'000	246 179	360 375	419 305
Operating sales margin	%	30.0	36.4	37.2
Cost recovery	%	142.6	156.9	159.2
Return on assets	%	5.0	6.7	7.1
Return on equity	%	3.5	5.8	6.8
Financial management				
Debt to equity	%	28.2	31.2	32.9
Debt to total assets	%	20.3	20.1	22.6
Total liabilities to equity	%	38.9	55.5	58.1
Interest cover	times	4.2	5.6	5.8
Current ratio	%	174.5	175.6	183.3
Leverage ratio	%	138.9	155.5	158.1
Payments to and from government				
Dividends	\$'000	88 551	88 551	121 685
Dividend to equity ratio	%	1.9	2.1	2.7
Dividend payout ratio	%	55.2	36.4	39.3
Income tax expense	\$'000	85 691	116 981	109 534
CSO funding	\$'000	2 993	2 993	2 284

^a Figures are nominal values. ^b Port GTEs commenced reporting under Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for port GTEs. ^c Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports.

9.7 GTE performance reports

Newcastle Port Corporation (NSW)
Port Kembla Port Corporation (NSW)
Sydney Ports Corporation (NSW)
Port of Melbourne Corporation (Victoria)
Victorian Regional Channels Authority (Victoria)
Central Queensland Ports 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)
Tasmanian Ports Corporation (Tasmania)
Darwin Port Corporation (NT)

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.

The NPC recorded a total throughput of 85.6 million tonnes in 2005-06. Coal accounted for around 93 per cent of this throughput.

The NPC's pre-tax operating profit increased by 70 per cent (\$7.0 million) to \$17.1 million in 2005-06, as a result of a 15 per cent (\$6.3 million) increase in total revenue. Revenue growth was partly the result of increased income from port management, but also included \$4.7 million in revaluations of investment property.¹ Total expenditure declined by 2.1 per cent to \$31.8 million in 2005-06, mainly because of a reduction in expenditure on repairs and services. The improved profitability resulted in increased return on assets and return on equity ratios, which were 12.4 per cent and 12.0 per cent respectively in 2005-06.

Total assets were \$160 million in 2005-06, an increase of 6.4 per cent (\$9.6 million) from 2004-05, and the level of debt remained steady at \$30.8 million. Finance costs were correspondingly steady at \$2.1 million, and with the increased profitability this caused interest cover to rise from 5.6 times in 2004-05 to 9.1 times in 2005-06. However, total liabilities grew by 7.2 per cent (\$4.0 million) in 2005-06, primarily with increases to deferred tax liabilities.

The NPC is required to make dividend and tax-equivalent payments to the NSW Government. The Corporation provided for a \$6.0 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$5.5 million.

The NPC does not receive community service obligation funding from the NSW Government.

¹ Of this \$4.7 million, \$3.0 million was reported as a fair value adjustment to investment property and \$1.7 million was reported as the fair value of site improvements carried out in February 2006.

NEWCASTLE PORT CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	161	150	160
Total revenue	\$m	43	43	49
Profitability				
Operating profit before tax	\$'000	10 994	10 061	17 076
Operating sales margin	%	28.3	26.1	36.8
Cost recovery	%	139.5	135.3	158.3
Return on assets	%	8.2	8.2	12.4
Return on equity	%	7.1	7.3	12.0
Financial management				
Debt to equity	%	27.3	32.8	31.0
Debt to total assets	%	19.1	20.5	19.9
Total liabilities to equity	%	42.8	59.7	60.4
Interest cover	times	6.0	5.6	9.1
Current ratio	%	405.1	305.9	311.3
Leverage ratio	%	142.8	159.7	160.4
Payments to and from government				
Dividends	\$'000	3 057	3 057	6 024
Dividend to equity ratio	%	2.7	3.0	6.2
Dividend payout ratio	%	38.2	44.8	52.1
Income tax expense	\$'000	2 998	3 236	5 509
CSO funding	\$'000	..	..	..

^a Newcastle Port Corporation (NPC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the NPC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

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 offers pilotage services and provides berths and equipment for private sector lease or common use.

The major cargoes that move through Port Kembla are coal, iron ore and steel products. The port managed a total throughput of 25.9 million revenue tonnes in 2005-06, a 6.1 per cent increase on the previous year.¹

The PKPC doubled its pre-tax operating profit from \$3.4 million in 2004-05 to \$6.8 million in 2005-06. The Corporation attributes the increased profitability to higher trade volumes as well as to reduced costs. Total revenue grew by 8.7 per cent (\$2.5 million) to \$31.3 million, while total expenditure fell by 3.6 per cent (\$907 000) to \$24.5 million. The reduction in expenditure was mainly because of a \$1.5 million reduction in employee benefits expenses and a \$1.2 million fall in administrative expenses.

Total assets fell by 5.0 per cent (\$8.4 million) to \$158 million in 2005-06, and total debt was steady at \$49.3 million. The PKPC's current ratio increased substantially — from 215.1 per cent in 2004-05 to 399.4 per cent in 2005-06 — following an 8.5 per cent rise in current assets and a 42 per cent fall in current liabilities. The increase in current assets was mainly attributable to a \$7.3 million rise in cash holdings, while the fall in current liabilities was the result of a \$5.1 million reduction in current provisions (as no dividend was provided for in 2005-06) and a \$5.0 million reduction in short-term debt.

The PKPC is required to make dividend and tax-equivalent payments to the NSW Government. The Corporation made no dividend provision in respect of 2005-06, but recorded an income tax-equivalent expense of \$2.1 million.

The PKPC does not receive community service obligation funding from the NSW Government.

¹ A revenue tonne is a mass of 1000kg or a volume of one cubic metre, whichever gives the largest number of units of cargo.

PORT KEMBLA PORT CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	163	166	158
Total revenue	\$m	39	29	31
<i>Profitability</i>				
Operating profit before tax	\$'000	18 244	3 391	6 814
Operating sales margin	%	55.3	20.4	28.7
Cost recovery	%	223.9	125.6	140.3
Return on assets	%	13.6	4.4	6.6
Return on equity	%	14.4	2.5	5.6
<i>Financial management</i>				
Debt to equity	%	57.0	60.2	56.6
Debt to total assets	%	30.3	29.6	30.5
Total liabilities to equity	%	88.5	103.1	80.9
Interest cover	times	5.6	1.9	2.8
Current ratio	%	150.7	215.1	399.4
Leverage ratio	%	188.5	203.1	180.9
<i>Payments to and from government</i>				
Dividends	\$'000	6 233	6 233	—
Dividend to equity ratio	%	7.2	7.6	—
Dividend payout ratio	%	50.0	310.3	—
Income tax expense	\$'000	5 779	1 382	2 050
CSO funding	\$'000	..	..	..

^a Port Kembla Port Corporation (PKPC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PKPC. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. — Zero or rounded to zero.

Sydney Ports Corporation (SPC) was established in 1995 and 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. The SPC also owns Sydney Pilot Service Pty Ltd, which operates as the pilot service provider for Sydney Harbour and Port Botany.¹

The SPC handled container throughput of 1.4 million twenty-foot equivalent units in 2005-06, a 5.0 per cent increase on 2004-05. The major container cargoes handled were chemicals, manufactures and machinery. The SPC's total throughput increased by 3.1 per cent to 26.7 million mass tonnes in 2005-06, with the major bulk cargo commodities including sugar, cement, gases, oil and petroleum products and motor vehicles. Sydney Harbour is also regularly visited by cruise ships.

In October 2005, the NSW Government approved the SPC's plans to develop and expand its Port Botany facilities. According to the SPC, the expansion was planned in response to ongoing growth in container volumes at Port Botany. Onsite works for the 60 hectare, five berth expansion commenced in January 2006.

The SPC recorded a pre-tax operating profit of \$92.3 million in 2005-06, a 33 per cent (\$46.1 million) decrease on 2004-05, after a 21 per cent (\$47.5 million) reduction in total revenue. The fall in revenue was largely because of smaller investment property revaluation gains in 2005-06 (\$14.3 million) compared with 2004-05 (\$79.2 million). Total expenditure was steady at \$91.4 million.

Total assets grew by 7.7 per cent (\$73.7 million) to \$1.0 billion in 2005-06, mainly because of revaluations and additions to investment properties totalling \$65.8 million. Current assets fell by 4.4 per cent and current liabilities rose by 34 per cent, the latter reflecting increases in accounts payable and in dividend provisions. As a result, the SPC's current ratio fell from 182.6 per cent in 2004-05 to 129.7 per cent in 2005-06.

The SPC is required to make dividend and tax-equivalent payments to the NSW Government. It provided for a \$22.2 million dividend in 2005-06 and recorded an income tax-equivalent expense of \$28.3 million. The SPC does not receive community service obligation funding from the NSW Government.

¹ Sydney Pilot Service commenced operations in 2002-03. Before this, pilotage services were carried out by private operators.

SYDNEY PORTS CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	965	953	1 026
Total revenue	\$m	156	231	184
Profitability				
Operating profit before tax	\$'000	61 415	138 457	92 318
Operating sales margin	%	47.0	65.2	55.9
Cost recovery	%	188.7	287.6	226.7
Return on assets	%	7.8	16.0	10.5
Return on equity	%	5.8	16.3	10.4
Financial management				
Debt to equity	%	23.3	29.0	27.0
Debt to total assets	%	17.8	18.0	17.3
Total liabilities to equity	%	31.1	61.4	61.3
Interest cover	times	5.5	11.2	8.7
Current ratio	%	206.7	182.6	129.7
Leverage ratio	%	131.1	161.4	161.3
Payments to and from government				
Dividends	\$'000	18 910	18 910	22 160
Dividend to equity ratio	%	2.6	3.2	3.6
Dividend payout ratio	%	44.4	19.7	34.6
Income tax expense	\$'000	18 864	42 480	28 308
CSO funding	\$'000	..	..	..

^a Sydney Ports Corporation (SPC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the SPC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports .. Not applicable.

The Port of Melbourne Corporation (PoMC) commenced operations on 1 July 2003, replacing the former Melbourne Port Corporation. The PoMC operates under the *Ports Services Act 1995* and is subject to price regulation by the Essential Services Commission. The PoMC is responsible for managing and developing the Port of Melbourne, ensuring the availability of essential port services and managing channels.¹ Total trade was 64.2 million revenue tonnes in 2005-06, a slight (0.3 per cent) decline on 2004-05.²

The PoMC recorded a pre-tax operating profit of \$42.3 million in 2005-06, an increase of 37 per cent (\$11.4 million) from 2004-05. The higher profitability was mainly a result of an 8.4 per cent (\$10.5 million) increase in total revenue, and led to an increase in the PoMC's return on assets and return on equity. Finance costs were 61 per cent lower in 2005-06 than in the previous year, despite a 20 per cent rise in the Corporation's debt. This resulted from fair value adjustments to borrowings, which reduced total finance expenses by \$1.9 million in 2005-06.

Total assets were \$992 million in 2005-06, a 5.1 per cent (\$48.4 million) increase on 2004-05. The PoMC spent \$39.0 million on infrastructure investment in 2005-06. It also received an equity injection of \$3.6 million from the Victorian State Government to fund security upgrades at Station Pier. Current assets fell by 39 per cent to \$24.1 million, mainly because of a reduction in cash holdings. Current liabilities grew by 17 per cent to \$61.1 million, with increases in accounts payable and provisions for environmental restoration costs. Accordingly, the current ratio declined from 76.0 per cent in 2004-05 to 39.4 per cent in 2005-06.

The PoMC made a dividend payment of \$18.8 million in 2005-06.³ It also recorded a net tax-equivalent benefit of \$6.2 million.⁴ It does not receive community service obligation funding from the Victorian Government.

¹ On 3 November 2003, the PoMC assumed responsibility for the channels and port waters of the Port of Melbourne from the former Victorian Channels Authority.

² A revenue tonne is a mass of 1000kg or a volume of one cubic metre, whichever gives the largest number of units of cargo.

³ No dividend was paid for the 2004-05 financial year. The PoMC reported that the obligation to pay a dividend had not been determined in consultation with the Treasurer by 30 June 2005.

⁴ The net tax-equivalent benefit was achieved by adjusting the initial tax-equivalent expense of \$12.7 million for \$18.9 million in tax concessions for research and development associated with the channel deepening project. The \$18.9 million in concessions included \$12.3 million for current year research and development and \$6.6 million for the previous year's research and development.

PORT OF MELBOURNE CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	958	943	992
Total revenue	\$m	125	124	135
Profitability				
Operating profit before tax	\$'000	32 746	30 919	42 293
Operating sales margin	%	28.0	27.5	31.9
Cost recovery	%	138.9	137.9	146.8
Return on assets	%	3.9	3.8	4.6
Return on equity	%	2.6	2.7	6.5
Financial management				
Debt to equity	%	7.4	9.0	10.4
Debt to total assets	%	6.5	7.0	8.1
Total liabilities to equity	%	13.9	30.1	30.8
Interest cover	times	8.7	6.8	21.3
Current ratio	%	86.2	76.0	39.4
Leverage ratio	%	113.9	130.1	130.8
Payments to and from government				
Dividends	\$'000	—	—	18 800
Dividend to equity ratio	%	—	—	2.5
Dividend payout ratio	%	—	—	38.8
Income tax expense	\$'000	11 169	11 169	-6 206 ^c
CSO funding	\$'000	..	..	..

^a The Port of Melbourne Corporation (PoMC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PoMC. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c The PoMC recorded a net tax-equivalent benefit of \$6.2 million in 2005-06, as the initial tax-equivalent expense of \$12.7 million was adjusted for \$18.9 million in research and development tax concessions. The \$18.9 million in concessions included \$12.3 million for current year research and development and \$6.6 million for the previous year's research and development. .. Not applicable. – Zero or rounded to zero.

The Victorian Regional Channels Authority (VRCA) was established under the *Port Services Act 1995* to manage channels in the port waters of Geelong and oversee 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 the ports of Portland and Hastings.

The VRCA recorded a pre-tax operating profit of \$1.7 million in 2005-06, more than double the 2004-05 result of \$805 000. According to the VRCA, the increased profitability was primarily attributable to reduced operating costs. Total expenditure fell by 15 per cent (\$761 000) from 2004-05 to 2005-06, with the main reductions in expenditure on maintenance, marine services, and special projects. Total revenue grew by 2.7 per cent to \$6.0 million in 2005-06.

Total assets were steady at \$60.1 million in 2005-06, and the VRCA's level of borrowings remained at zero. As a result, the debt to equity and debt to total assets ratios were zero in 2005-06, as in 2004-05.

The VRCA is required to make tax-equivalent payments under the *State Owned Enterprises Act 1992*. It is also required to pay dividends to the Victorian Government. The VRCA recorded a tax-equivalent expense of \$603 000 in 2005-06 and distributed dividends totalling \$542 000.

The VRCA does not receive community service obligation funding from the Victorian Government.

¹ Responsibility for the Geelong channels and the approaches to the ports of Portland and Hastings was assigned to the new entity, the VRCA. The Port of Melbourne Corporation took over the land and waterside functions of the Port of Melbourne, including the Melbourne operations of the Victorian Channels Authority, on 3 November 2003.

VICTORIAN REGIONAL CHANNELS AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	59	59	60
Total revenue	\$m	6	6	6
<i>Profitability</i>				
Operating profit before tax	\$'000	797	805	1 724
Operating sales margin	%	7.5	7.8	22.2
Cost recovery	%	108.1	108.4	128.6
Return on assets	%	1.3	1.4	2.9
Return on equity	%	1.5	0.9	2.0
<i>Financial management</i>				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity	%	1.2	5.7	5.8
Interest cover	times	..	..	..
Current ratio	%	4 213.9	1 242.2	1 179.5
Leverage ratio	%	101.2	105.7	105.8
<i>Payments to and from government</i>				
Dividends	\$'000	100	100	542
Dividend to equity ratio	%	0.2	0.2	1.0
Dividend payout ratio	%	11.4	20.8	48.3
Income tax expense	\$'000	-82	324	603
CSO funding	\$'000	..	..	..

^a The Victorian Regional Channels Authority (VRCA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the VRCA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. – Zero or rounded to zero.

The Central Queensland Ports Authority (CQPA) commenced operations on 1 July 2004 following the merger of the Rockhampton Port Authority with the Gladstone Port Authority. The CQPA operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. It is responsible for the provision of infrastructure for bulk operations as well as pilotage and stevedoring services.

The CQPA recorded total combined throughput of 67.4 million tonnes in 2005-06, comprising 67.2 million tonnes at the Port of Gladstone (up from 63.1 million in 2004-05) and 138 000 tonnes at Port Alma (formerly Rockhampton).

The CQPA's total revenue grew by 12 per cent (\$16.4 million) to \$152 million in 2005-06, which the Authority attributes primarily to increased trade activity. Total expenditure increased by a smaller amount, 11 per cent (\$13.6 million), largely because of growth in labour costs. As a consequence, the CQPA's pre-tax operating profit grew by 24 per cent to \$14.2 million in 2005-06.

The value of the CQPA's assets increased by 61 per cent (\$401 million) to nearly \$1.1 billion in 2005-06. This was largely attributable to capital expenditure of \$249 million in 2005-06, which increased the value of property, plant and equipment. An increase of \$167 million in cash holdings also contributed to this growth. The proportional increase in assets outweighed the proportional growth in profitability, leading to a slight fall in both the return on assets and return on equity to 2.9 per cent and 1.8 per cent respectively.

Total debt grew by 48 per cent (\$67.4 million) to \$207 million as the CQPA increased its borrowings to fund its capital works program. The higher level of debt, as well as increases in trade payables, led to an overall increase in total liabilities of 42 per cent (\$97.6 million). However, because of the strong growth in total assets, the debt to equity ratio fell from 33.4 per cent in 2004-05 to 28.7 per cent in 2005-06. Borrowing costs rose by 13 per cent in 2005-06 following the growth in debt, but interest cover was steady at 2.3 times as a result of the increased profitability.

The CQPA is required to make dividend and tax-equivalent payments to the Queensland Government. The Authority provided for a \$7.0 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$4.2 million.

The CQPA does not receive community service obligation funding from the Queensland Government.

CENTRAL QUEENSLAND PORTS AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	652	652	1 052
Total revenue	\$m	135	135	152
<i>Profitability</i>				
Operating profit before tax	\$'000	11 432	11 432	14 218
Operating sales margin	%	13.2	13.2	14.2
Cost recovery	%	115.1	115.1	116.5
Return on assets	%	3.2	3.2	2.9
Return on equity	%	1.6	1.9	1.8
<i>Financial management</i>				
Debt to equity	%	32.3	33.4	28.7
Debt to total assets	%	21.5	21.5	24.4
Total liabilities to equity	%	50.4	55.5	45.7
Interest cover	times	2.2	2.2	2.3
Current ratio	%	330.4	330.4	461.1
Leverage ratio	%	150.4	155.5	145.7
<i>Payments to and from government</i>				
Dividends	\$'000	5 619	5 619	7 023
Dividend to equity ratio	%	1.3	1.3	1.2
Dividend payout ratio	%	80.0	68.8	70.2
Income tax expense	\$'000	4 408	3 268	4 212
CSO funding	\$'000	..	..	..

^a The Central Queensland Ports Authority (CQPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the CQPA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

The Port of Brisbane Corporation (PBC) was established on 1 July 1994 and operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. The PBC manages the Port of Brisbane, the Brisbane Multimodal Terminal, and the boat harbours of Manly, Scarborough, Cabbage Tree Creek and Gardens Point. It also has a 37 per cent interest in Brisbane Airport Corporation Holdings (BACH).

The PBC's container throughput was 766 000 twenty-foot equivalent units in 2005-06, an increase of 5.5 per cent on 2004-05. The Corporation's major traded commodities include oil, coal, cement, iron and steel.

The PBC recorded a pre-tax operating profit of \$171 million in 2005-06, an 86 per cent increase on 2004-05. There was a 33 per cent, or \$69.8 million, increase in total revenue. This included a \$59.8 million increase in the revaluation gain on investment properties and a \$7.7 million increase in dividend income from the Corporation's shareholding in BACH. Trade revenues grew by only 9.1 per cent, or \$5.9 million, from 2004-05 to 2005-06. Total expenditure fell by \$9.4 million (7.8 per cent), largely because of reductions in the cost of sales and maintenance expenses. The growth in profitability led to an increase in the PBC's return on assets and return on equity, to 11.6 per cent and 13.1 per cent respectively.

The value of the PBC's total assets grew by 18 per cent (\$284 million) to \$1.9 billion in 2005-06. The major contributors to this growth were investment in infrastructure totalling \$155 million and revaluation of investment properties and property, plant and equipment. In its annual report, the PBC stated that the asset revaluations occurred in response to a significant increase in land values and increasing construction costs of buildings and wharves.

The PBC is required to make dividend and tax-equivalent payments to the Queensland Government. The Corporation provided for a \$35.8 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$50.8 million.

The PBC does not receive community service obligation funding from the Queensland Government.

PORT OF BRISBANE CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 609	1 609	1 893
Total revenue	\$m	141	213	282
Profitability				
Operating profit before tax	\$'000	52 135	91 984	171 150
Operating sales margin	%	49.9	52.0	69.5
Cost recovery	%	199.8	208.2	328.2
Return on assets	%	4.8	7.3	11.6
Return on equity	%	3.3	7.4	13.1
Financial management				
Debt to equity	%	45.8	55.2	60.3
Debt to total assets	%	29.9	29.9	33.3
Total liabilities to equity	%	53.5	84.9	95.5
Interest cover	times	3.1	4.6	6.4
Current ratio	%	130.9	130.9	131.4
Leverage ratio	%	153.5	184.9	195.5
Payments to and from government				
Dividends	\$'000	27 977	27 977	35 811
Dividend to equity ratio	%	2.7	3.2	3.9
Dividend payout ratio	%	80.0	43.7	29.7
Income tax expense	\$'000	17 164	28 002	50 756
CSO funding	\$'000	..	..	..

^a The Port of Brisbane Corporation (PBC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PBC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

The Cairns Port Authority (CPA) operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. It has responsibility for the management and operation of the Cairns International Airport (which the CPA estimates represents over 80 per cent of its overall business in revenue terms), the Port of Cairns, and associated land and property. Most port activities such as towage and stevedoring are conducted by private operators.

Total passenger movements through the airport were 3.8 million in 2005-06, an increase of 3.9 per cent on the previous year. All of the growth was in domestic air travel, with domestic passenger movements increasing by 6.7 per cent while international passenger movements fell by 2.6 per cent. Total trade through the CPA's seaport was steady at approximately 1.1 million tonnes in 2005-06. The major cargoes moving through the seaport are sugar and petroleum products.

The CPA recorded a pre-tax operating profit of \$27.5 million in 2005-06, an increase of 6.0 per cent on 2004-05. According to the CPA, the increased profitability was primarily a result of revenue growth, particularly at the airport. Revenue from airport activities grew by 8.7 per cent, while revenue from seaport activities increased by 11 per cent (a larger percentage increase but a much smaller amount in dollar terms). Both return on assets and return on equity increased from 2004-05 to 2005-06, to 6.3 per cent and 5.2 per cent respectively.

The CPA invested \$50.4 million in capital works in 2005-06, of which \$46.3 million was spent on the expansion of airfield infrastructure and airport terminal redevelopments. The capital expenditure contributed to an 8.1 per cent (\$41.9 million) increase in the value of the CPA's assets. The asset growth was also a result of an increase in current receivables associated with the sale of land. The increase in receivables boosted current assets to \$45.9 million, 220 per cent higher than in 2004-05. In its annual report, the CPA acknowledged that this unusual item has inflated the current ratio, which grew from 40.3 per cent in 2004-05 to 118.8 per cent in 2005-06. Total debt rose by 39 per cent to \$109 million, as a result of the increased borrowings used to fund the capital works program.

The CPA is required to make dividend and tax-equivalent payments to the Queensland Government. It provided for a \$10.2 million dividend payment in 2005-06 and recorded an income tax-equivalent expense of \$8.7 million. The CPA does not receive community service obligation funding from the Queensland Government.

CAIRNS PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	534	514	556
Total revenue	\$m	81	83	91
<i>Profitability</i>				
Operating profit before tax	\$'000	20 618	25 986	27 547
Operating sales margin	%	30.3	36.1	37.1
Cost recovery	%	143.5	156.6	158.9
Return on assets	%	4.6	5.9	6.3
Return on equity	%	2.5	4.1	5.2
<i>Financial management</i>				
Debt to equity	%	19.4	21.8	29.7
Debt to total assets	%	14.7	15.3	20.5
Total liabilities to equity	%	32.0	43.0	51.0
Interest cover	times	6.2	7.1	5.4
Current ratio	%	40.0	40.3	118.8
Leverage ratio	%	132.0	143.0	151.0
<i>Payments to and from government</i>				
Dividends	\$'000	8 030	8 030	10 232
Dividend to equity ratio	%	2.0	2.2	2.8
Dividend payout ratio	%	80.0	53.9	54.2
Income tax expense	\$'000	10 580	11 080	8 680
CSO funding	\$'000	..	..	..

^a The Cairns Port Authority (CPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the CPA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

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 as well as five other non-trading ports. Pilotage services at the ports are provided by Maritime Safety Queensland, an agency of the Queensland Department of Transport. Stevedoring and towage are generally franchised to the private sector.

The PCQ handled total throughput of 116 million tonnes, a 1.6 per cent decline on 2004-05. The Corporation's trading ports handle bulk cargo including coal, sugar and bauxite.

The PCQ recorded a pre-tax operating profit of \$21.0 million in 2005-06, representing an increase of 95 per cent (\$10.2 million) over 2004-05. The increased profitability was driven by revenue growth of 35 per cent (\$14.4 million), which the Corporation attributes largely to the first full year of the Operations and Maintenance Agreement at Abbot Point. The PCQ also notes that repairs and maintenance expenses increased as a result of this agreement, contributing to growth of 14 per cent (\$4.1 million) in total expenditure in 2005-06. The higher operating result was reflected in an increase in return on assets from 4.6 per cent in 2004-05 to 8.2 per cent in 2005-06.

The PCQ's total assets increased by 18 per cent (\$41.6 million) in 2005-06. This was mainly because of additions to property, plant and equipment of \$56.2 million. The PCQ had no outstanding borrowings at the end of 2005-06, and thus had debt to equity and debt to total assets ratios of zero. However, its total liabilities rose by 55 per cent to \$94.5 million following a \$22.8 million increase in trade and other payables. This increased the total liabilities to equity ratio from 34.8 per cent in 2004-05 to 51.7 per cent in 2005-06.

The PCQ is required to make dividend and tax-equivalent payments to the Queensland Government. It declared a dividend of \$11.4 million in 2005-06 and recorded an income tax-equivalent expense of \$6.2 million. The PCQ does not receive community service obligation funding from the Queensland Government.

PORTS CORPORATION OF QUEENSLAND (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	235	235	277
Total revenue	\$m	41	41	56
Profitability				
Operating profit before tax	\$'000	14 181	10 811	21 034
Operating sales margin	%	30.7	22.1	35.4
Cost recovery	%	138.0	122.7	152.7
Return on assets	%	6.0	4.6	8.2
Return on equity	%	7.2	3.0	8.3
Financial management				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity	%	19.6	34.8	51.7
Interest cover	times	..	..	..
Current ratio	%	169.4	169.4	57.3
Leverage ratio	%	119.6	134.8	151.7
Payments to and from government				
Dividends	\$'000	10 259	10 259	11 445
Dividend to equity ratio	%	5.2	5.9	6.4
Dividend payout ratio	%	72.2	196.5	77.3
Income tax expense	\$'000	-31	5 590	6 223
CSO funding	\$'000	..	..	..

^a The Ports Corporation of Queensland (PCQ) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PCQ. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. — Zero or rounded to zero.

The 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.

The MPA recorded passenger numbers of 656 000 through the Mackay Airport in 2005-06, representing a 13 per cent increase on 2004-05. The seaport recorded cargo throughput of 2.3 million tonnes in 2005-06, an increase of 3.1 per cent on the previous year. The seaport mainly handles bulk commodities, including sugar, petroleum and grain.

The MPA recorded a pre-tax operating profit of \$4.0 million in 2005-06, an increase of 64 per cent on the previous year. In its annual report, the MPA attributes the increased profitability to growth in airport passenger numbers as well as higher cargo levels at the seaport. Total revenue grew by 20 per cent (\$3.8 million) to \$22.4 million, following a 16 per cent (\$1.8 million) rise in seaport revenue and a 25 per cent (\$2.0 million) increase in airport revenue.

The value of the MPA's assets grew by 8.3 per cent (\$18.1 million) to \$237 million in 2005-06, mainly because of a \$16.2 million revaluation of property, plant and equipment. Total liabilities increased by 17 per cent (\$6.1 million), primarily as a result of a \$4.4 million increase in deferred tax liabilities. The MPA had no outstanding borrowings at the end of 2005-06, and thus had debt to equity and debt to total assets ratios of zero.

The MPA is required to make tax-equivalent and dividend payments to the Queensland Government. The Authority provided for a dividend of \$2.4 million in 2005-06 and recorded an income tax-equivalent expense of \$989 000. The MPA does not receive community service obligation funding from the Queensland Government.

MACKAY PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	218	218	237
Total revenue	\$m	19	19	22
Profitability				
Operating profit before tax	\$'000	2 419	2 419	3 973
Operating sales margin	%	5.2	5.3	10.4
Cost recovery	%	105.5	105.6	111.6
Return on assets	%	1.1	1.1	1.7
Return on equity	%	0.6	0.7	1.6
Financial management				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity	%	5.5	19.7	21.6
Interest cover	times	..	..	..
Current ratio	%	526.4	526.4	451.6
Leverage ratio	%	105.5	119.7	121.6
Payments to and from government				
Dividends	\$'000	952	952	2 387
Dividend to equity ratio	%	0.5	0.5	1.3
Dividend payout ratio	%	80.0	80.0	80.0
Income tax expense	\$'000	1 229	1 229	989
CSO funding	\$'000	..	..	..

^a The Mackay Port Authority (MPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the MPA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. — Zero or rounded to zero.

The Townsville Port Authority (TPA) was established on 1 July 1995 and operates under the *Government Owned Corporations Act 1993* and the *Transport Infrastructure Act 1994*. The TPA is responsible for the management of the Port of Townsville.

The TPA handled total cargo throughput of 9.9 million tonnes in 2005-06, representing a slight (0.6 per cent) decline on the previous year. The major cargoes passing through the port include nickel ore, minerals and sugar.

In September 2005, the Queensland Government approved the TPA's plans to build a terminal facility to allow visits by cruise ships and naval vessels, known as the Ocean Terminal project. In June 2006, after several months of negotiations with the Queensland Government and developers, the TPA signed off on key agreements to enable construction to proceed.

The TPA recorded a pre-tax operating profit of \$4.8 million in 2005-06, 51 per cent less than in 2004-05. However, the TPA notes that the 2004-05 pre-tax operating profit of \$9.6 million included a reversal of earlier asset writedowns of \$7.9 million.

The value of the TPA's assets rose by 5.2 per cent (\$10.0 million) to \$201 million in 2005-06. The growth in assets included a \$5.2 million increase in cash assets and a \$3.7 million increase in the value of investment properties. The increase in cash contributed to a 34 per cent rise in current assets in 2005-06. With current liabilities steady from 2004-05 to 2005-06, the current ratio increased from 182.3 per cent to 243.7 per cent. Total debt fell by 14 per cent to \$13.5 million, reducing both the debt to equity and debt to total assets ratios to 8.4 per cent and 6.9 per cent respectively.

The TPA is required to make dividend and tax-equivalent payments to the Queensland Government. The TPA recorded an income tax-equivalent expense of \$2.6 million in 2005-06, but made no dividend provision for this financial year.¹

The TPA does not receive community service obligation funding from the Queensland Government.

¹ This followed the acceptance of the TPA's recommendation to the shareholding Ministers that no dividend be payable in 2005-06.

TOWNSVILLE PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	178	191	201
Total revenue	\$m	29	40	36
Profitability				
Operating profit before tax	\$'000	2 173	9 636	4 768
Operating sales margin	%	9.8	25.9	14.1
Cost recovery	%	110.8	134.9	116.3
Return on assets	%	1.8	5.6	2.9
Return on equity	%	0.5	5.0	1.4
Financial management				
Debt to equity	%	10.1	10.4	8.4
Debt to total assets	%	8.8	8.2	6.9
Total liabilities to equity	%	14.6	26.7	26.3
Interest cover	times	3.2	10.6	6.6
Current ratio	%	182.3	182.3	243.7
Leverage ratio	%	114.6	126.7	126.3
Payments to and from government				
Dividends	\$'000	577	577	—
Dividend to equity ratio	%	0.4	0.4	—
Dividend payout ratio	%	80.0	7.6	—
Income tax expense	\$'000	1 452	2 087	2 590
CSO funding	\$'000	..	..	..

^a The Townsville Port Authority (TPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the TPA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. — Zero or rounded to zero.

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.

The FPA handled total port trade of 25.0 million tonnes in 2005-06, a 2.4 per cent decline on 2004-05. The major cargoes moving through the port are petroleum products, grain and alumina.

The FPA recorded a pre-tax operating profit of \$13.3 million in 2005-06, representing a decline of 13 per cent (\$1.9 million) on 2004-05. Total expenditure increased by 10 per cent (\$7.2 million), as a result of higher operational expenses. Revenue growth of 6.3 per cent (\$5.3 million) was insufficient to offset the increase in total expenses. The lower profitability was reflected in a slight fall in the FPA's return on assets from 8.9 per cent in 2004-05 to 8.1 per cent in 2005-06.

The value of the FPA's assets increased by 5.7 per cent (\$11.1 million) to \$206 million in 2005-06. This was mainly because of an increase in the value of property, plant and equipment, following the construction of the North Quay rail loop and the completion of the first stage of the North Quay rail terminal. Total debt grew by 14 per cent (\$6.7 million) in 2005-06. However, total liabilities increased by only 6.5 per cent (\$4.8 million), as a decline in current liabilities partially offset the increase associated with the expansion in borrowings.

The FPA is required to make income tax-equivalent and dividend payments to the WA Government. It distributed dividends of \$4.9 million in 2005-06 and recorded an income tax-equivalent expense of \$3.5 million.

The FPA does not receive community service obligation funding from the WA Government.

FREMANTLE PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	196	195	206
Total revenue	\$m	84	84	89
Profitability				
Operating profit before tax	\$'000	16 458	15 212	13 280
Operating sales margin	%	22.0	20.5	18.2
Cost recovery	%	128.2	125.8	122.2
Return on assets	%	9.5	8.9	8.1
Return on equity	%	10.4	9.6	7.8
Financial management				
Debt to equity	%	39.2	37.9	41.2
Debt to total assets	%	23.6	23.7	26.4
Total liabilities to equity	%	66.0	59.8	60.6
Interest cover	times	9.1	8.4	5.4
Current ratio	%	135.5	175.9	190.3
Leverage ratio	%	166.0	159.8	160.6
Payments to and from government				
Dividends	\$'000	5 760	5 760	4 929
Dividend to equity ratio	%	4.9	4.7	3.9
Dividend payout ratio	%	46.8	49.2	50.4
Income tax expense	\$'000	4 161	3 513	3 498
CSO funding	\$'000	..	..	..

^a The Fremantle Port Authority (FPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the FPA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable.

The 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 to the private sector.

The BPA handled 12 million tonnes of cargo in 2005-06, representing a 0.5 per cent decrease from the previous financial year. Alumina accounted for 70 per cent of total port throughput by tonnage in 2005-06. Other major cargoes handled by the port include caustic soda, woodchips and mineral sands.

The BPA recorded a pre-tax operating profit of \$5.3 million in 2005-06, a 37 per cent (\$1.6 million) increase on 2004-05. This improvement was assisted by an 8.5 per cent (\$1.5 million) increase in total revenue, primarily the result of a \$1.0 million increase in revenue from lease rentals.

The value of the BPA's assets remained stable at \$102 million in 2005-06. It recorded a slight fall in total debt, from \$13.6 million in 2004-05 to \$13.1 million in 2005-06. This is reflected in lower debt to equity and debt to total assets ratios in 2005-06.

The BPA is required to make dividend and income tax-equivalent payments to the WA Government. It recorded an income tax-equivalent expense of \$1.7 million in 2005-06 and distributed dividends of \$1.5 million.

The BPA does not receive community service obligation funding from the WA Government.

BUNBURY PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	102	102	102
Total revenue	\$m	18	18	19
Profitability				
Operating profit before tax	\$'000	4 351	4 351	5 316
Operating sales margin	%	25.1	25.2	27.8
Cost recovery	%	133.5	133.6	138.4
Return on assets	%	5.1	5.1	6.0
Return on equity	%	3.6	3.6	4.4
Financial management				
Debt to equity	%	17.0	16.5	15.5
Debt to total assets	%	13.3	13.4	12.9
Total liabilities to equity	%	27.2	23.6	19.9
Interest cover	times	6.0	6.0	7.4
Current ratio	%	423.3	595.1	972.4
Leverage ratio	%	127.2	123.6	119.9
Payments to and from government				
Dividends	\$'000	—	—	1 480 ^c
Dividend to equity ratio	%	—	—	1.8
Dividend payout ratio	%	—	—	40.4
Income tax expense	\$'000	1 478	1 348	1 655
CSO funding	\$'000	..	..	..

^a The Bunbury Port Authority (BPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the BPA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Dividend includes \$43 000 for a 'Government efficiency dividend' unrelated to profit. .. Not applicable. – Zero or rounded to zero.

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 to the private sector.

The PHPA handled total cargo throughput of 111 million tonnes in 2005-06, a 1.9 per cent increase on the previous year. It is Australia's largest port by tonnage throughput. Iron ore accounted for 95 per cent of port throughput by tonnage, with other main cargoes including salt and bulk minerals.

The PHPA recorded a pre-tax operating profit of \$4.7 million in 2005-06, nearly double the previous year's \$2.4 million result. A 23 per cent (\$4.5 million) increase in total revenue was a major contributor to the increased profitability. Revenue from charges on cargo grew by nearly 28 per cent and revenue from ship charges by 17 per cent. This revenue growth is attributable in part to most charges increasing by 10 per cent in 2005-06.

According to the PHPA, its prices were raised in response to strong inflationary pressures. Total expenditure increased from 2004-05 to 2005-06, but only by half as much as the increase in total revenue (13 per cent or \$2.2 million, compared to 23 per cent or \$4.5 million). In addition, cash holdings increased by \$7.8 million, mostly from growth in net cash flow from operating activities.

The increased profitability led to corresponding increases in the PHPA's return on assets and return on equity to 8.9 per cent and 7.2 per cent respectively in 2005-06.

The value of the PHPA's assets increased by 19 per cent (\$9.1 million) to \$57.1 million in 2005-06, mainly because of higher cash holdings. The increase in cash was also reflected in the PHPA's current assets, which grew by 225 per cent and increased the current ratio from 99.9 per cent in 2004-05 to 129.7 per cent in 2005-06. The PHPA had no outstanding borrowings at the end of 2005-06, and thus has debt to equity and debt to total assets ratios of zero.

The PHPA is required to make tax-equivalent and dividend payments to the WA Government. It recorded an income tax-equivalent expense of \$1.5 million in 2005-06, but did not declare a dividend. The PHPA does not receive community service obligation funding from the WA Government.

PORT HEDLAND PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	48	48	57
Total revenue	\$m	20	20	24
Profitability				
Operating profit before tax	\$'000	2 403	2 403	4 707
Operating sales margin	%	11.4	11.4	19.2
Cost recovery	%	112.9	112.9	123.7
Return on assets	%	5.0	5.0	8.9
Return on equity	%	3.8	3.9	7.2
Financial management				
Debt to equity	%	—	—	—
Debt to total assets	%	—	—	—
Total liabilities to equity	%	12.7	12.5	24.4
Interest cover	times	..	..	..
Current ratio	%	99.9	99.9	129.7
Leverage ratio	%	112.7	112.5	124.4
Payments to and from government				
Dividends	\$'000	810	810	— ^c
Dividend to equity ratio	%	1.9	1.9	—
Dividend payout ratio	%	50.0	48.5	—
Income tax expense	\$'000	783	732	1 497
CSO funding	\$'000	..	..	..

^a The Port Hedland Port Authority (PHPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the PHPA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c No dividend was declared in 2005-06. .. Not applicable. – Zero or rounded to zero.

The Albany Port Authority (APA) operates under the *Port Authorities Act 1999*. The APA manages port facilities and provides pilotage services. Stevedoring, mooring and cold storage services are contracted to the private sector.

The APA handled total cargo throughput of 2.7 million tonnes in 2005-06, representing an 11 per cent decrease on 2004-05. According to the APA, the decline in trade volume was caused by a three-month shutdown in grain exports while port facilities were upgraded. The main cargoes moving through the port are grain, silica sand and woodchips.

The APA recorded a pre-tax operating profit of \$1.8 million in 2005-06, a 40 per cent decrease on 2004-05. This followed a 7.7 per cent (\$592 000) fall in total revenue, which the APA attributes to a lower volume of trade throughput. Total expenditure grew by 12 per cent (\$586 000), mainly a result of increased spending on administration and on salaries and wages. The reduced profitability led to a decrease in return on assets and on equity, which were 6.4 per cent and 4.4 per cent respectively in 2005-06.

Total assets fell slightly to \$36.0 million in 2005-06, while total debt fell by 9.6 per cent to \$9.1 million. The lower level of debt was reflected in a decrease in the APA's debt to equity ratio from 40.3 per cent in 2004-05 to 36.0 per cent in 2005-06, and in a 12 per cent reduction in finance costs.

The APA is required to make tax-equivalent and dividend payments to the WA Government. It recorded an income tax-equivalent expense of \$648 000 in 2005-06 and distributed dividends of \$826 000.

The APA does not receive community service obligation funding from the WA Government.

ALBANY PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	38	37	36
Total revenue	\$m	8	8	7
<i>Profitability</i>				
Operating profit before tax	\$'000	2 985	2 938	1 760
Operating sales margin	%	44.8	44.6	30.4
Cost recovery	%	181.3	180.3	143.8
Return on assets	%	9.7	9.7	6.4
Return on equity	%	8.3	7.6	4.4
<i>Financial management</i>				
Debt to equity	%	41.3	40.3	36.0
Debt to total assets	%	26.9	27.1	24.9
Total liabilities to equity	%	53.4	48.9	42.1
Interest cover	times	5.4	5.4	4.0
Current ratio	%	43.4	50.4	46.5
Leverage ratio	%	153.4	148.9	142.1
<i>Payments to and from government</i>				
Dividends	\$'000	—	—	826
Dividend to equity ratio	%	—	—	3.3
Dividend payout ratio	%	—	—	74.3
Income tax expense	\$'000	958	1 021	648
CSO funding	\$'000	..	..	..

^a The Albany Port Authority (APA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the APA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. .. Not applicable. – Zero or rounded to zero.

The 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 to the private sector.

The DPA handled total cargo throughput of 110 million tonnes in 2005-06, a 15 per cent increase on 2004-05. It is Australia's second largest port by tonnage throughput, after the Port Hedland Port Authority. The main cargoes moving through the port include iron ore, liquefied natural gas, gas condensates and salt.

The DPA recorded a pre-tax operating profit of \$1.3 million in 2005-06, a substantial improvement over the \$1.1 million operating loss of 2004-05. The return to profitability resulted from a near trebling of total revenue, from \$5.3 million in 2004-05 to \$15.5 million in 2005-06. The main factors driving revenue growth were increased port charges, a rise in the number of ships entering the port, as well as the addition of revenue from the new bulk liquids berth that commenced operations in 2005-06. Revenue of \$8.0 million was derived from the bulk liquids berth, \$7.8 million of which comprised contributions from the WA Government.

Total expenditure more than doubled from \$6.4 million in 2004-05 to \$14.3 million in 2005-06. This was partly attributable to a \$2.8 million increase in borrowing costs associated with a \$20.0 million drawing on a \$73.1 million loan facility with the WA Treasury Corporation.¹ The higher total expenditure was also a result of increases in employee benefits, maintenance, depreciation, legal and consultancy expenses.

The value of the DPA's assets increased by 24 per cent to \$93.4 million in 2005-06, with an \$11.0 million increase in property, plant and equipment associated with port expansion works. Total borrowings grew by 41 per cent to \$69.1 million, increasing the debt to equity ratio from 231.1 per cent in 2004-05 to 311.2 per cent in 2005-06.

The DPA is required to make tax-equivalent and dividend payments to the WA Government. It paid an 'efficiency dividend' — unrelated to profit — of \$24 000 in 2005-06 and recorded an income tax-equivalent expense of \$319 000. The DPA does not receive community service obligation funding from the WA Government.

¹ The total loan facility was \$75.6 million until November 2005, when it was reduced to \$73.1 million. According to the DPA, the difference of \$2.5 million represents the portion of the facility that was no longer required. Of the \$73.1 million, \$69.1 million was drawn as at 30 June 2006.

DAMPIER PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	75	75	93
Total revenue	\$m	5	5	16
<i>Profitability</i>				
Operating profit before tax	\$'000	-1 108	-1 108	1 275
Operating sales margin	%	-21.5	-21.7	25.1
Cost recovery	%	82.3	82.2	133.6
Return on assets	%	-1.5	-1.5	4.9
Return on equity	%	-3.6	-3.4	4.4
<i>Financial management</i>				
Debt to equity	%	225.3	231.1	311.2
Debt to total assets	%	65.4	65.4	82.0
Total liabilities to equity	%	244.4	253.2	320.8
Interest cover	times	..	..	1.5
Current ratio	%	41.6	41.4	284.8
Leverage ratio	%	344.4	353.2	420.8
<i>Payments to and from government</i>				
Dividends	\$'000	267	267	24 ^c
Dividend to equity ratio	%	1.2	1.3	0.1
Dividend payout ratio	%	-34.0	-36.5	2.5
Income tax expense	\$'000	-322	-377	319
CSO funding	\$'000	..	..	..

^a The Dampier Port Authority (DPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the DPA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Dividend of \$24 000 in 2005-06 is an 'efficiency dividend' unrelated to profit. .. Not applicable.

The 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 to the private sector.¹

The GPA handled total port throughput of 5.2 million tonnes in 2005-06, representing a 5.2 per cent decline on 2004-05. The main cargoes moved through the port are wheat, iron ore and mineral sands.

In January 2006, the WA Government approved the GPA's plans to undertake a \$35.0 million upgrade of two of its berths. According to the GPA, the upgrade is planned in response to an anticipated increase in iron ore throughput. Work began on the upgrade in February 2006.

The GPA recorded a pre-tax operating profit of \$2.1 million in 2005-06, unchanged from 2004-05. Total revenue increased by 12 per cent (\$3.2 million) to \$29.0 million, largely because of increases in revenue from shipping charges and from rentals and leases. However, this was offset by a 13 per cent (\$3.2 million) rise in total expenditure, mainly attributable to the recognition of a \$5.3 million impairment on port facilities.

The GPA's total assets and total borrowings both fell slightly in 2005-06, to \$152 million and \$120 million respectively. This brought the debt to total assets ratio down to 78.5 per cent, which remains relatively high in comparison with other monitored port corporations.

The GPA is required to make tax-equivalent and dividend payments to the WA Government. The GPA recorded an income tax-equivalent expense of \$628 000 in 2005-06 and made a dividend payment of \$2020. The GPA does not receive community service obligation funding from the WA Government.

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.

GERALDTON PORT AUTHORITY (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
<i>Size</i>				
Total assets	\$m	154	155	152
Total revenue	\$m	26	26	29
<i>Profitability</i>				
Operating profit before tax	\$'000	2 891	2 092	2 093
Operating sales margin	%	39.1	35.9	29.1
Cost recovery	%	164.1	156.0	141.0
Return on assets	%	6.8	6.3	5.9
Return on equity	%	-12.2 ^c	6.7	7.8
<i>Financial management</i>				
Debt to equity	%	628.0	681.1	617.0
Debt to total assets	%	79.6	79.5	78.5
Total liabilities to equity	%	688.8	756.8	680.2
Interest cover	times	1.4	1.3	1.3
Current ratio	%	219.5	219.5	222.1
Leverage ratio	%	788.8	856.8	780.2
<i>Payments to and from government</i>				
Dividends	\$'000	—	—	2 ^d
Dividend to equity ratio	%	—	—	0.0
Dividend payout ratio	%	—	—	0.1
Income tax expense	\$'000	5 277	877	628
CSO funding	\$'000	..	..	..

^a The Geraldton Port Authority (GPA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the GPA.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Return on equity was negative in 2004-05 (pre-AIFRS) as after-tax profit was negative. ^d Dividend is an ordinary dividend of \$2023. Actual dividend to equity ratio was 0.01. .. Not applicable. — Zero or rounded to zero.

Tasmanian Ports Corporation (TPC) was incorporated on 1 July 2005 and began trading as TasPorts on 1 January 2006.¹ The TPC operates subject to the provisions of the *Port Companies Act 1997*, and manages port facilities in 14 locations across Tasmania. It provides pilotage, security and navigation services, and its subsidiary, Port Logistics and Services Pty Ltd, offers stevedoring and cold storage facilities. The TPC has three other wholly-owned subsidiaries, King Island Ports Corporation, Flinders Island Ports Company and Hobart International Airport (HIA).

The TPC handled total cargo throughput of 14.8 million tonnes in 2005-06, a 9.0 per cent decrease on the aggregate trade throughput of the former port corporations in 2004-05. The HIA recorded total passenger numbers of 1.6 million, representing a 5.3 per cent increase on 2004-05.

The TPC recorded a pre-tax operating loss of \$4.2 million for the period 1 January 2006 to 30 June 2006. Total revenue for this six-month period was \$45.5 million, and total expenditure was \$49.7 million.

The TPC had total assets of \$244 million in 2005-06 and total borrowings of \$65.0 million. It recorded a debt to total assets ratio of 26.7 per cent.

The TPC is required to make tax-equivalent and dividend payments. It recorded an income tax-equivalent credit of \$1.1 million. There was no dividend provision for the last six months of 2005-06. The TPC does not receive community service obligation funding from the Tasmanian Government.

¹ The assets and infrastructure of Burnie Port Corporation, Hobart Ports Corporation, Port of Devonport Corporation and Port of Launceston Pty Ltd were administered by their former owners until 1 January 2006, when they were handed over to the TPC.

TASMANIAN PORTS CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^a		AIFRS ^a
	Units	2004-05	2004-05	2005-06 ^b
<i>Size</i>				
Total assets	\$m	..	..	244
Total revenue	\$m	..	..	46
<i>Profitability</i>				
Operating profit before tax	\$'000	..	..	-4 159
Operating sales margin	%	..	..	-4.4
Cost recovery	%	..	..	95.8
Return on assets	%	..	..	-0.8
Return on equity	%	..	..	-2.1
<i>Financial management</i>				
Debt to equity	%	..	..	44.5
Debt to total assets	%	..	..	26.7
Total liabilities to equity	%	..	..	66.7
Interest cover	times	..	..	-0.9
Current ratio	%	..	..	168.8
Leverage ratio	%	..	..	166.7
<i>Payments to and from government</i>				
Dividends	\$'000	..	..	—
Dividend to equity ratio	%	..	..	—
Dividend payout ratio	%	..	..	—
Income tax expense	\$'000	..	..	-1 075
CSO funding	\$'000	..	..	..

^a Tasmanian Ports Corporation (TPC) was incorporated on 1 July 2005 and began trading as TasPorts on 1 January 2006, following the amalgamation of the Burnie Port Corporation, the Hobart Ports Corporation, the Port of Devonport Corporation and the Port of Launceston Pty Ltd. Pre-AIFRS data for the former merged entities up to 2004-05 are available in previous *Financial Performance of Government Trading Enterprise* reports. ^b Data for 2005-06 are for the period 1 January 2006 to 30 June 2006. .. Not applicable. — Zero or rounded to zero.

The Darwin Port Corporation (DPC) was established under the *Darwin Port Corporation Act 1999*. It manages the East Arm and City Wharves in the Port of Darwin and offers facilities and services to commercial shipping, including pilotage and navigation services. The DPC also operates facilities for non-trading vessels, including those engaged in research, fishing and pearling.

The DPC's throughput in 2005-06 was 1.1 million tonnes. Although this represents a 43 per cent decrease on the 2004-05 throughput, it is comparable to the 2003-04 result. The DPC states that 2004-05 throughput was atypical because of the cargo and rock shipped through the port for the construction of the Darwin LNG plant and pipeline. Major cargoes passing through the port include petroleum products, metal products and livestock.

The DPC recorded a pre-tax operating loss of \$7.9 million in 2005-06, nearly 460 per cent larger than the \$1.4 million operating loss of 2004-05. This result represents the net effect of a 28 per cent (\$5.4 million) reduction in total revenue — which the DPC attributed to a reduction in trade volumes and in the amount of community service obligation (CSO) funding — and a 5.1 per cent (\$1.1 million) increase in total expenditure.

The value of the DPC's assets increased slightly by 2.2 per cent (\$4.4 million) in 2005-06. This was a result of a \$18.6 million increase in capital works-in-progress, which was partly offset by a \$9.7 million drop in current assets, attributable mainly to reduced cash holdings. The reduction in current assets, and a 16 per cent rise in current liabilities — mainly because of an increase in payables — led to a substantial fall in the DPC's current ratio, from 425.6 per cent in 2004-05 to 159.8 per cent in 2005-06. Total debt fell by 3.5 per cent (\$1.1 million) to \$30.8 million in 2005-06, reducing the debt to equity ratio slightly to 17.9 per cent.

The DPC is required to make tax-equivalent and dividend payments to the NT Government. The DPC recorded an income tax-equivalent benefit of \$1.4 million in 2005-06 and made no provision for a dividend.

The DPC received \$2.3 million in CSO funding in 2005-06, to cover costs associated with small craft services, tourism and real estate, cruise and defence facilities, security of City Wharves, and the Swires and Hai Win shipping services.

DARWIN PORT CORPORATION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	71	202	206
Total revenue	\$m	19	19	14
Profitability				
Operating profit before tax	\$'000	-8 955	-1 414	-7 882
Operating sales margin	%	-43.0	-2.4	-48.7
Cost recovery	%	69.8	97.5	67.2
Return on assets	%	-10.0	0.2	-3.0
Return on equity	%	-26.7	-0.9	-3.9
Financial management				
Debt to equity	%	97.1	19.2	17.9
Debt to total assets	%	45.0	15.8	15.1
Total liabilities to equity	%	115.7	21.1	20.2
Interest cover	times	-3.9	0.2	-3.4
Current ratio	%	400.1	425.6	159.8
Leverage ratio	%	215.7	121.1	120.2
Payments to and from government				
Dividends	\$'000	—	—	—
Dividend to equity ratio	%	—	—	—
Dividend payout ratio	%	—	—	—
Income tax expense	\$'000	-174	20	-1 350
CSO funding	\$'000	2 993	2 993	2 284

^a The Darwin Port Corporation (DPC) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the DPC.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. — Zero or rounded to zero.

10 Forestry

The financial performances of six forestry government trading enterprises (GTEs) are reported in this chapter. Together they controlled \$6.2 billion in assets in 2005-06.

Financial performance summaries, including performance indicators for each forestry GTE and a summary of performance indicators for the sector as a whole, are presented after this introduction. The performance indicators are defined in chapter 1.

When making comparisons, consideration should be given to: differences in the nature and scale of the businesses; their individual market environments; a number of issues relating to the valuation of their assets; and the level of payments for community service obligations. In particular, care should be taken because of issues relating to the valuation of self-generating and regenerating assets (SGARAs). Given the volatile nature of changes in the valuation of standing timber assets, profits are reported both before and after movements in forest valuations. Care should also be exercised when comparing data presented in this chapter with that presented in previous reports for two reasons:

1. The performance data presented in this report are based, for the first time, on the new Australian-equivalent International Financial Reporting Standards.
2. Data from GTE general purpose financial reports have been used for this report, whereas data presented in previous reports were based on government financial statistics. The reason for this change is set out in chapter 1.

10.1 Monitored GTEs

Forestry GTEs from six states are monitored — Forests NSW (FNSW), VicForests, the Forest Products Commission of Western Australia (FPCWA), ForestrySA, Forestry Tasmania and Forestry Plantations Queensland (FPQ).¹

¹ ACT Forests operates within the Department of Urban Services and is not reported because of substantial restructuring following the catastrophic bushfire in 2002-03. The NT does not have a forestry GTE.

The financial performance of the FPQ was reported for the first time in 2005-06. It was established on 1 May 2006 and replaced DPI Forestry as the manager of Queensland's state-controlled softwood and hardwood plantation lands. Along with the creation of the FPQ, the Forestry Plantations Queensland Office (FPQO) was established to support and complement The FPQ's operations by providing administrative services and by having custodial responsibility for the new State Plantation Forest lands.²

The monitored forestry GTEs provided a broad range of services (table 10.1) including:

- management of plantation and native forests;
- supply of forest products to the timber industry;
- research and development of new forestry techniques and processes;
- contributions to marketing forest products; and
- management of activities unrelated to timber production which occur in state-managed native forests and plantations — including beekeeping, recreation facilities, grazing and quarrying.

Table 10.1 **Activities — forestry GTEs, 2005-06^a**

Forestry GTE	Activities			
	Plantation management	Native-forest management	Research and marketing	Tourism and recreation activities
Forests NSW	✓	✓	✓	✓ ^a
VicForests	✓	✗	✓	✗
Forestry Plantations Queensland	✓	✗	✓	✓ ^a
Forest Products Commission WA	✓	✓	✓	✗
ForestrySA	✓	✓ ^b	✓	✓ ^a
Forestry Tasmania	✓	✓	✓	✓

^a These forestry GTEs provide services and infrastructure for tourism activities, such as scenic drives, picnic areas and hiking trails. However, these activities generate negligible revenue. ^b ForestrySA receives community service obligation funding for specific native forest management activities.

² The FPQ's financial results for revenue, profit and tax relate to the two months that the entity traded in 2005-06. Its assets were transferred from its predecessor, DPI Forestry. Financial management and profitability ratios were not included in this report as they provide an inaccurate representation of the FPQ's performance. Similarly, the FPQ is excluded from the sector-wide performance analysis in the remainder of this chapter.

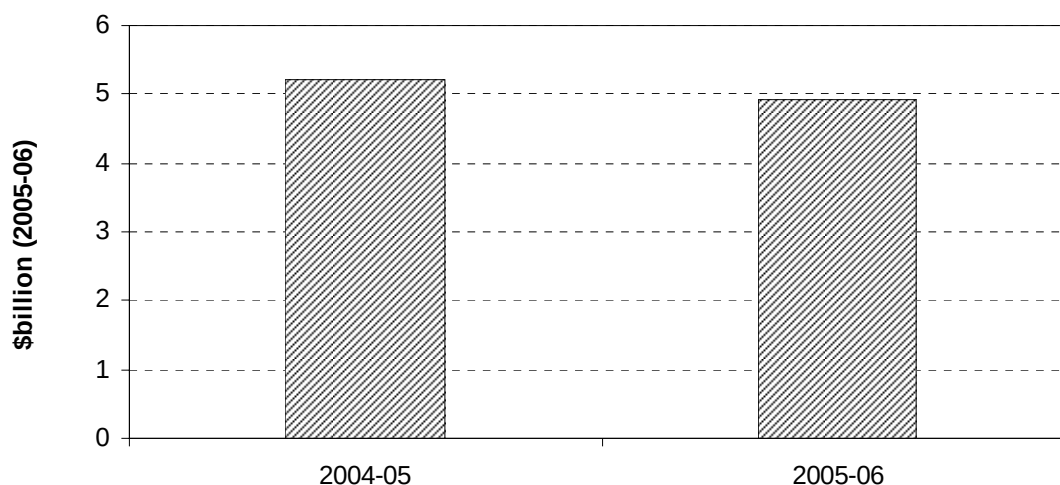
In addition, forestry GTEs generally have responsibility for fire-fighting and other ancillary forest-management activities.

The total assets of forestry GTEs (excluding the FPQ) fell by 5.4 per cent in real terms to \$4.9 billion in 2005-06. Most of this decrease was attributable to the FNSW, whose assets decreased in real terms by \$239 million in 2005-06. The change in total assets of monitored forestry GTEs for the last two years, measured in 2005-06 dollars, is shown in figure 10.1.

The size of monitored forestry GTEs vary substantially in terms of the value of their assets and revenue (figure 10.2). The largest forestry GTE in 2005-06 was the FNSW (\$2.5 billion in assets and \$293 million in revenue) and the smallest was VicForests (\$34.8 million in assets and \$36.9 million in revenue).

Governance objectives for forestry GTEs differ across jurisdictions. Differences include the degree of emphasis on commercial objectives by boards and governments compared with other objectives, such as environmental management and community education. All of the monitored GTEs are corporatised.

Figure 10.1 **Sector assets — forestry GTEs^a**



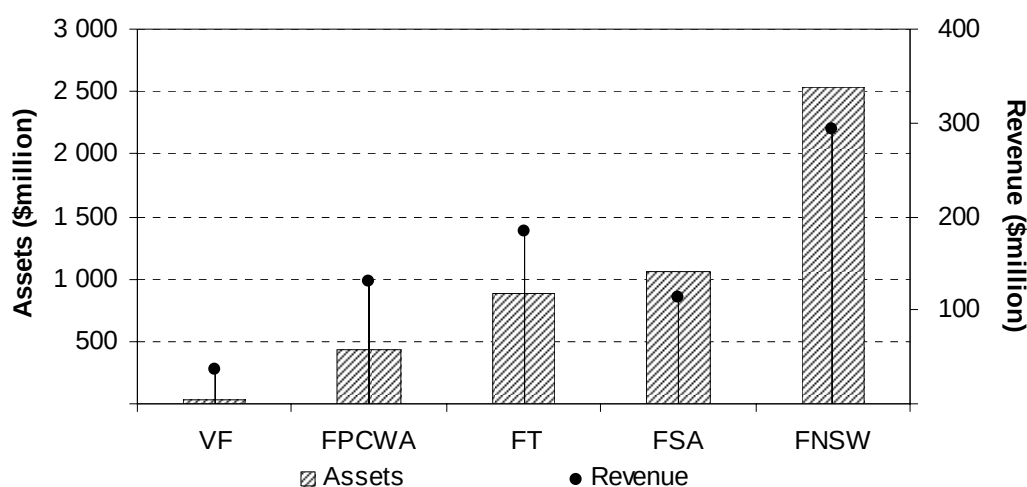
^a The value of sector assets is reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1).

Source: Productivity Commission estimates.

10.2 Market environment

The financial performances of forestry GTEs are affected by the volatility of demand for timber products, industry reforms and accounting standards.

Figure 10.2 Assets and revenue — forestry GTEs, 2005-06



Source: Productivity Commission estimates.

Demand for forest products

The major traded output of forestry GTEs is 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 used domestically, with 89 per cent of sawn-timber needs produced locally in 2004-05 (ABS 2007e). The demand for sawlogs is influenced by local economic conditions and government policies. Buoyant building activity has increased demand for sawlogs in recent years (ABS 2006b). However, in 2005-06, some forestry GTEs reported a reduction in demand for sawlogs resulting from the recent slowdown in the housing construction market.

Approximately 40 per cent of pulpwood harvested in Australia each year is sold domestically for pulp and paper products, while the balance is exported — mainly as woodchips (ABARE 2000). The total value of exports of forest products was \$2.1 billion in 2005-06, of which woodchips represented around 40 per cent and paper and paperboard products represented around 28 per cent. The top three destinations of Australian forestry exports in 2005-06 were Japan (\$802 million), New Zealand (\$351 million) and China (\$251 million) (BRS 2007).

The sources and types of forestry products have changed over time. Since 1999-2000 the production of logs from native forests has been in decline. Conversely, there has been a steady increase in the production of wood from hardwood plantations since the late 1990s. The production of logs from softwood plantations has remained relatively stable since 2002-03 (BRS 2007).

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 Vision and the application of National Competition Policy (NCP).

National Forest Policy Statement

The Australian, State and Territory Governments signed the NFPS in 1992. The NFPS was a comprehensive agreement on a ‘blueprint’ for the future management of Australia’s forests for the next 20 years, 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;
- use of RFAs as a means of providing integrated management of forest resources; and
- expansion of Australia’s commercial plantations of softwoods and hardwoods.

Regional Forest Agreements

RFAs are 20-year plans for the conservation and sustainable management of Australia’s native forests. Currently, four states have RFAs — NSW, Victoria, WA and Tasmania. They are intended to provide greater certainty and security in relation to forest conservation and timber resource supply. More specifically, RFAs are intended to:

- reduce uncertainty for industry and duplication of 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 can only be exported from forest regions in which RFAs have been successfully negotiated.

Plantations 2020

The Plantations 2020 Vision included a proposal to treble the area of Australia's plantation forests to around 3 million hectares, in line with previous proposals in the NFPS. This initiative was endorsed by the Ministerial Council on Forestry, Fisheries and Aquaculture in July 1996. The Plantations 2020 Vision was revised in 2001 to take account of developments grouped around five strategic elements. These are:

- encouraging a comprehensive policy approach;
- establishing the right legislative environment;
- promoting investor confidence, research and development and skills development;
- improving stakeholder engagement and identifying environmental benefits and services; and
- monitoring future developments and opportunities to maintain investment.

National Competition Policy

As part of the NCP, governments have agreed to minimise resource allocation distortions relating to any competitive advantage derived by forestry GTEs as a result of their public sector ownership. To the extent that the benefits outweigh the costs, under clause 3 of the Competition Principles Agreement, governments are obliged to:

- adopt a corporatisation model where appropriate; and
- impose taxes or tax-equivalent payments, debt guarantee fees and regulations equivalent to those of private sector competitors.

Valuation of SGARAs

SGARAs represent over half of the forestry sector's assets and are valued at up to 89 per cent of assets for some GTEs. Their value can also fluctuate significantly each year, thus affecting profitability measures. As a result, the method of valuing

SGARAs is important to monitoring the operation and performance of forestry GTEs.

The accounting standard for valuing SGARAs under AIFRS is AASB 141 *Agriculture*. SGARAs held primarily for profit are valued at fair value less estimated point-of-sale costs. When fair value cannot be reliably measured, SGARAs are measured at cost less any accumulated depreciation and any accumulated impairment losses. Increments and decrements to SGARA valuations are recognised directly in the income statement.

Although the forestry GTEs follow the standard, there remains some variation in its implementation, as demonstrated in the GTE summaries.

The value of SGARAs is also influenced by changes in the following:

- *The volume of timber* — changes in the area of commercial forests (natural or plantation) controlled by a GTE, or changes in the commercial timber available within the existing forest areas, can affect the volume of timber.
- *Age and quality of timber* — the value per cubic metre varies for trees of different ages. Older, larger trees generally have higher use values — such as building materials and furniture — than younger, smaller trees. Different species of trees also have different use values and attract different market prices.
- *Market prices* — the prevailing market prices for the sawlogs and pulp logs harvested from SGARA assets.

Forestry GTEs can model with some precision the expected physical changes in their SGARA assets, other things being equal. However, changes in the market price received for forestry products can be highly variable and are outside the control of forestry GTEs.

Changes in demand conditions are a primary 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 (table 10.2), which in some cases had a significant impact on reported revenue. For example, the FNSW's SGARA revaluation in 2005-06 resulted in a \$62.8 million decrement, representing around 21 per cent of total revenue.

Table 10.2 Size of SGARA revaluations — forestry GTEs (\$million)

Forestry GTE	SGARA revaluation	
	2004-05	2005-06
Forests NSW	-40.0	-62.8
VicForests	2.2	-2.0
Forestry Plantations Queensland	-0.5	13.1
Forest Products Commission WA	-24.5	-18.7
ForestrySA	-12.6	6.7
Total	-75.5	-63.7

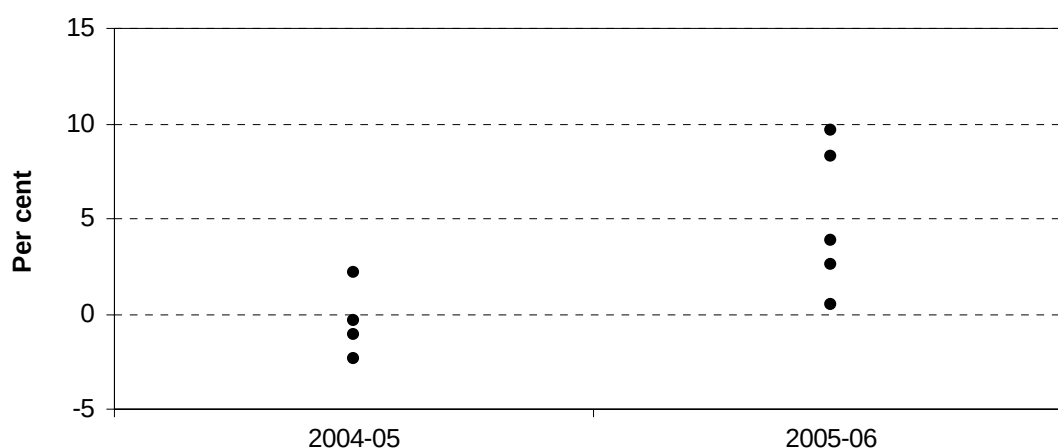
Source: GTE annual reports.

10.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings.

The measure of profitability for forestry GTEs can be significantly affected by the valuation of SGARAs (section 10.2).

Figure 10.3 Return on assets — forestry GTEs^{a,b}



^a 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.

^b VicForests' return on assets (36.2 per cent) in 2004-05 is not shown in the figure. The high value results from VicForests operating for less than 12 months in 2004-05. It received almost 12 months of revenue but incurred only 11 months of expenses, contributing to a strong operating profit.

Source: Productivity Commission estimates.

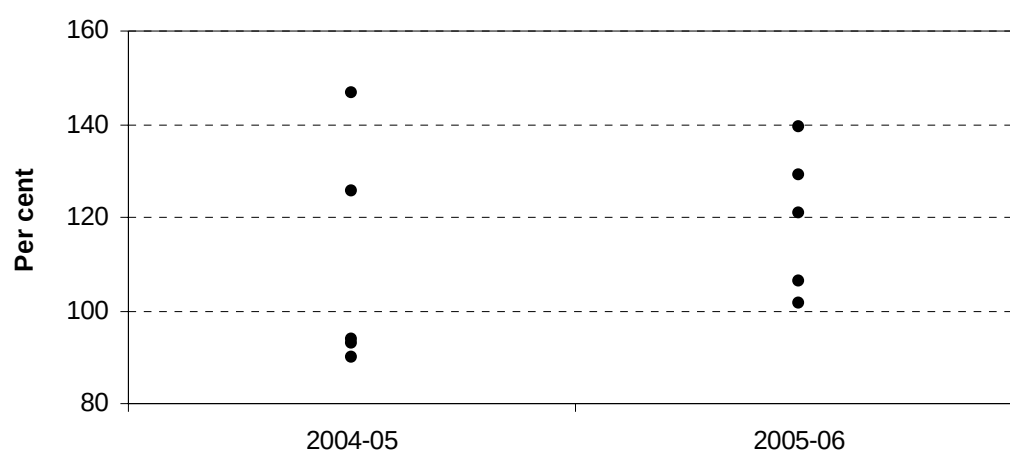
All forestry GTEs reported a positive return on assets in 2005-06 (figure 10.3), ranging from 0.4 per cent for the FNSW to 9.6 per cent for the FPCWA. VicForests was the only GTE to report a decline in performance from 2004-05 to 2005-06, resulting from a combination of one-off establishment expenses and a decrement in the value of SGARAs. Overall, return on assets for the forestry sector was 2.3 per cent in 2005-06, up from 0.1 per cent in 2004-05.

Three of the five forestry GTEs did not achieve a return that exceeded the risk-free benchmark return on assets.³ This suggests that these forestry GTEs are not operating on a commercially viable basis.

Forestry sector operating profits before SGARA revaluations (and before tax) increased by \$92.0 million, in real terms, to \$169 million in 2005-06. Operating profits after SGARA revaluations (and before tax) increased to \$106 million compared with an operating loss of \$1.7 million in 2004-05.

The cost recovery ratio indicates the ability of an entity to generate adequate revenue to meet expenses. The cost recovery ratio exceeded 100 per cent for each forestry GTE (figure 10.4) in 2005-06, indicating they are able to meet operating

Figure 10.4 **Cost recovery — forestry GTEs^a**



^a 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. Expense from operations are calculated by subtracting gross interest expense from total expenses.

Source: Productivity Commission estimates.

³ The risk-free rate of return is defined as the 2005-06 interest rate on a 10-year Australian Government bond (5.4 per cent) (RBA 2007a).

expenses from operating revenue. For the forestry sector, the cost recovery ratio increased from 99.0 per cent in 2004-05 to 115.4 per cent in 2005-06.

10.4 Financial management

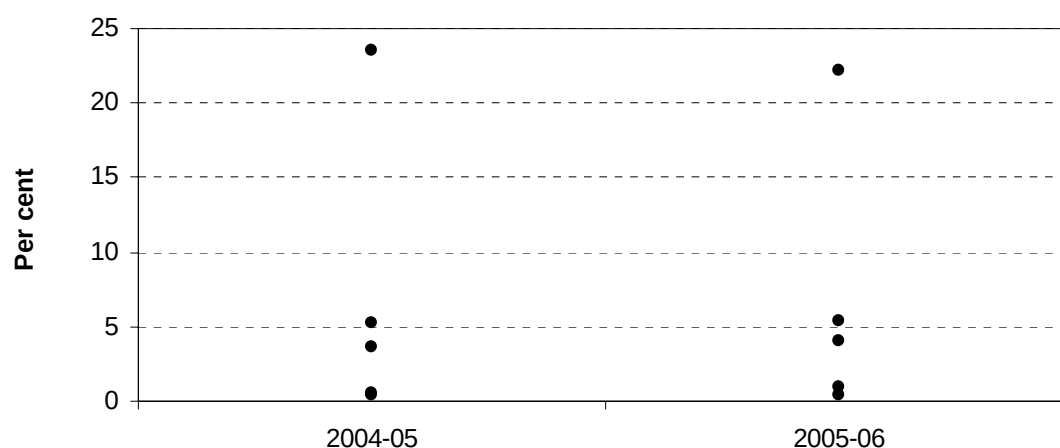
Financial management indicators provide information about the capital structure of GTEs and their ability to meet the cost of servicing debt and other liabilities as they fall due.

All forestry GTEs operated with debt for the past two years. The total level of debt for the forestry sector was around \$274 million in 2005-06, a decrease of 1.9 per cent on 2004-05 in real terms.

Debt to equity and debt to total assets ratios followed similar trends. Both ratios increased for the FNSW, ForestrySA, Forestry Tasmania and the sector as a whole in 2005-06. The debt to total assets ratio is shown for each forestry GTE over the last two years in figure 10.5.

The overall debt to assets ratio for forestry GTEs' was 5.5 per cent in 2005-06. GTEs in the other monitored sectors reported significantly higher ratios — electricity (41.2 per cent), ports (22.6 per cent), water (19.9 per cent), rail (17.7 per cent) and urban transport (44.4 per cent).

Figure 10.5 Debt to total assets — forestry GTEs^a



^a 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.

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 increase in interest expense, and still meet the cost of servicing debt. The forestry sector's ability to cover interest costs improved in 2005-06, with an interest cover of 12.2 times, up from 2.1 times in 2004-05.⁴ This was despite an increase in total debt for the sector. ForestrySA was the only GTE for which the interest cover ratio fell in 2005-06.

A current ratio of less than 100 per cent indicates that the short-term obligations of a GTE might need to be met using sources of funds other than current assets. All but one of the GTEs recorded a current ratio of over 100 per cent in 2005-06, the exception being the FNSW with a current ratio of 64.6 per cent. The current ratio for the sector overall was 179.8 per cent in 2005-06, up from 135.8 per cent in 2004-05.

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 financial disciplines and regulations similar to those faced by privately-owned businesses.

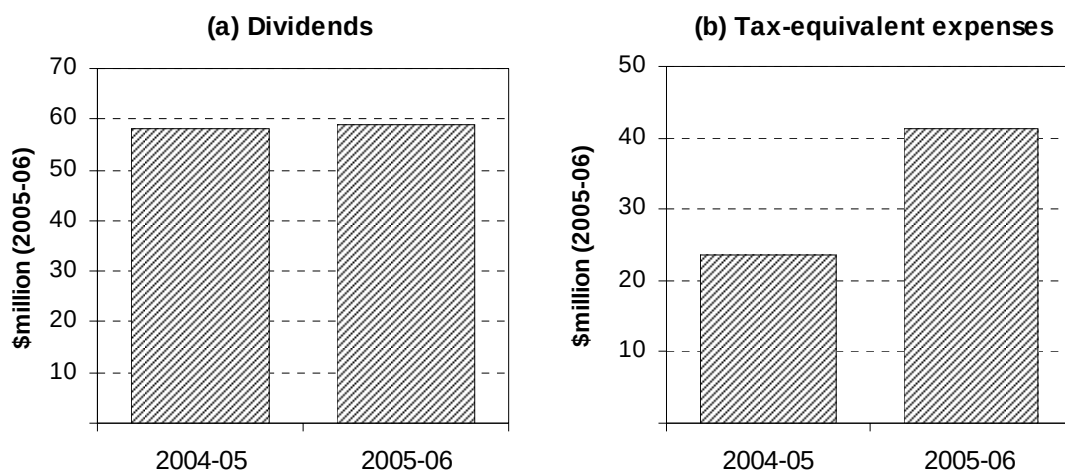
Dividend payments from GTEs are a return on shareholder funds that impose capital disciplines and are consistent with competitive neutrality. Four of the five forestry GTEs distributed dividends in 2005-06.

Overall, dividends from the forestry GTEs remained relatively stable in real terms at around \$59.1 million in 2005-06 (figure 10.6a). VicForests distributed dividends for the first time and ForestrySA increased its dividend payments in 2005-06. However, the FNSW and Forestry Tasmania decreased their dividend payments. The FPCWA did not distribute any dividends in relation to the 2005-06 financial year because of its poor operating performance.

The dividend to equity ratio remained largely unchanged in 2005-06 at 1.6 per cent. However, the dividend payout ratio increased from -228.6 per cent in 2004-05 to 91.7 per cent in 2005-06 because of growth in operating profits.

⁴ FNSW was excluded from the calculation of interest cover for the sector because its reported interest expenses were capitalised.

Figure 10.6 **Dividends and income tax-equivalent expenses — forestry GTEs^a**



^a The value of dividends and tax-equivalent expenses are reported in 2005-06 dollars using the implicit price deflator — gross fixed capital formation of public corporations (chapter 1).

Source: Productivity Commission estimates.

All forestry GTEs are subject to the National Tax Equivalent Regime and recorded income tax-equivalent expenses. Tax-equivalent expenses for the sector increased to \$41.2 million in 2005-06, an increase of 73 per cent in real terms since 2004-05, reflecting the increase in operating profits (figure 10.6b). Two of the five GTEs — the FPCWA and Forestry Tasmania — made higher payments than in 2004-05.

Three of the monitored forestry GTEs — the FNSW, ForestrySA and the FPCWA —received community service obligation (CSO) funding in 2005-06. In addition, Forestry Tasmania undertakes non-commercial community service activities which are not separately funded. CSO payments to the forestry sector totalled \$15.4 million in 2005-06, accounting for around 2.0 per cent of total revenue.

10.6 Implications of the new accounting standards

From 2005-06, financial data for all monitored forestry GTEs are based on the Australian-equivalent International Financial Reporting Standards (AIFRS). The adoption of the new accounting standards changed the recognition and measurement of some assets, liabilities and equity items, and affected the recording of income flows. These changes, which were discussed in the previous *Financial Performance of Government Trading Enterprises* report (PC 2006, chapter 3), have had a significant effect on the comparability over time of financial performance and financial management indicators.

The aggregate impact of the transition to AIFRS for the monitored forestry GTEs can be gauged by comparing 2004-05 data on an AIFRS and pre-AIFRS basis (table 10.3). Similar comparisons can be made by reference to each GTE summary.

FORESTRY

Table 10.3 Whole of sector performance indicators 2004-05 to 2005-06^a

		Pre-AIFRS ^{b,c}		AIFRS ^b
	Units	2004-05	2004-05	2005-06 ^d
Size				
Total assets	\$m	4 923	4 978	4 929
Total revenue	\$m	705	665	757
Profitability				
Operating profit before tax	\$'000	30 676	-1 663	105 645
Operating sales margin	%	5.1	0.6	14.5
Cost recovery	%	104.0	99.0	115.4
Return on assets	%	0.8	0.1	2.3
Return on equity	%	0.3	-0.7	1.8
Financial management				
Debt to equity	%	6.5	7.3	7.4
Debt to total assets	%	5.4	5.4	5.5
Total liabilities to equity	%	20.8	35.7	33.2
Interest cover	times	3.8	2.1	12.2
Current ratio	%	121.1	135.8	179.8
Leverage ratio	%	120.8	135.7	133.2
Payments to and from government				
Dividends	\$'000	55 622	55 622	59 120
Dividend to equity ratio	%	1.4	1.5	1.6
Dividend payout ratio	%	464.5	-228.6	91.7
Income tax expense	\$'000	18 701	22 667	41 162
CSO funding	\$'000	14 257	14 257	15 425

^a Figures are nominal values. ^b Forestry GTEs commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for forestry GTEs. ^c Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^d Data excludes Forestry Plantations Queensland which commenced operations on 1 May 2006.

Performance indicators before SGARA revaluation, 2004-05 to 2005-06^{a,b}

		Pre-AIFRS	AIFRS	
	Units	2004-05	2004-05	2005-06
Profitability				
Operating profit before tax	\$'000	106 179	73 840	169 342
Return on assets	%	2.3	1.6	3.5
Return on equity	%	2.4	1.7	4.3

^a Figures are nominal values. ^b Data excludes Forestry Plantations Queensland which commenced operations on 1 May 2006.

10.7 GTE performance reports

Forests NSW

VicForests (Victoria)

Forestry Plantations Queensland

Forest Products Commission (WA)

ForestrySA

Forestry Tasmania

The Forestry Commission of NSW, trading under the name Forests NSW (FNSW),¹ operates under the *Forestry Act 1916*. Although the FNSW became an administrative unit within the NSW Department of Primary Industries in June 2004, it continues to operate as an independent GTE.² The FNSW is responsible for managing almost 2.4 million hectares of native and planted forests throughout NSW. It established 264 hectares of new hardwood plantations and 6500 hectares of softwood plantations in 2005-06.

Approximately \$1.6 billion (62 per cent) of the FNSW's assets were self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.³

The FNSW reported an \$11.4 million operating profit in 2005-06, a significant improvement on the \$10.9 million loss reported in 2004-05. The turnaround was attributable to a \$45.6 million (18 per cent) increase in revenue, mainly from higher revenue from timber sales and superannuation gains. This more than offset a \$23.2 million (9.0 per cent) increase in expenses (the net effect of lower contractor, depreciation and employee related costs, and higher contract harvesting costs, biological asset depreciation and other costs).

The increase in profit before tax and before SGARA revaluation was even greater in 2005-06, increasing by \$45.1 million (155 per cent) to \$74.2 million.

The FNSW is subject to dividend and tax-equivalent payments. The FNSW provided for \$24.0 million in dividends in 2005-06, a decrease of \$3.3 million from 2004-05. The FNSW recorded a \$8.6 million income tax-equivalent expense in 2005-06.

The FNSW received \$9.6 million in community service obligation payments in 2005-06. This accounted for 3.3 per cent of total revenue. However, the FNSW reported that the costs of supplying these services was \$10.3 million in 2005-06.

¹ Prior to 1 July 2004, the Forestry Commission of NSW traded as State Forests of NSW.

² The NSW Government proclaimed the *Public Sector Employment Legislation Amendment Act 2006* in March 2006. Under the Act, FNSW employees became either employees of the Department of Primary Industries or a new entity, Forestry Commission Division. The FNSW is the parent reporting entity and its operations were consolidated with those of Forestry Commission Division in the data.

³ The FNSW uses three separate net market value models to determine the value of its softwood plantations, hardwood plantations and native forest timber. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

FORESTS NSW (continued)

Performance indicators 2004-05 to 2005-06

		<i>Pre-AIFRS^{a,b}</i>		<i>AIFRS^a</i>
	<i>Units</i>	<i>2004-05</i>	<i>2004-05</i>	<i>2005-06</i>
<i>Size</i>				
Total assets	\$m	2 592	2 643	2 529
Total revenue	\$m	264	248	293
<i>Profitability</i>				
Operating profit before tax	\$'000	7 656	-10 925	11 420
Operating sales margin	%	2.7	-4.6	3.7
Cost recovery	%	100.2	93.0	101.6
Return on assets	%	0.3	-0.4	0.4
Return on equity	%	0.1	-1.1	-0.1
<i>Financial management</i>				
Debt to equity	%	4.7	43.5	39.2
Debt to total assets	%	3.8	30.3	27.5
Total liabilities to equity	%	23.2	43.5	39.2
Interest cover ^c	times	..	..	..
Current ratio	%	78.9	49.6	64.6
Leverage ratio	%	123.2	143.5	139.2
<i>Payments to and from government</i>				
Dividends ^d	\$'000	27 254	27 254	24 000
Dividend to equity ratio	%	1.3	1.5	1.3
Dividend payout ratio	%	938.8	-139.7	-1582.1
Income tax expense	\$'000	4 753	8 584	12 937
CSO funding	\$'000	9 557	9 557	9 557

^a Forests NSW (FNSW) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the FNSW. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c Interest cover cannot be calculated because borrowing costs related to the acquisition of land and establishment and development of new plantations have been capitalised, as these assets take a considerable period to become commercially productive. ^d Dividends are the amount provided for and not the amount paid. .. Not applicable.

Performance indicators before SGARA revaluation 2004-05 to 2005-06

		Pre-AIFRS	AIFRS	
	Units	2004-05	2004-05	2005-06
Profitability				
Operating profit before tax	\$'000	47 648	29 067	74 179
Return on assets	%	1.8	1.1	2.8
Return on equity	%	2.2	1.5	3.9

VicForests was established under the *State Owned Enterprises Act 1992*, and commenced operation on 1 August 2004. VicForests is responsible for managing the harvesting and sale of timber resources from Victoria's state forests.¹ Approximately 5100 hectares of forest were harvested and 1500 hectares thinned by VicForests in 2005-06. VicForests introduced the Price Allocation Model in 2005-06 to auction timber online.

Total assets decreased by \$2.6 million (7.0 per cent) to \$34.8 million in 2005-06, primarily as a result of the revaluation of VicForests' self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management. Non-current SGARAs were valued at zero in 2005-06, down from \$6.3 million in 2004-05.² Total liabilities decreased by \$3.9 million (26 per cent) to \$11.0 million, largely due to a reduction in tax liabilities.

VicForests' operating profit before tax was \$3.0 million in 2005-06, down from \$13.1 million in 2004-05. This reflects a \$4.0 million (9.7 per cent) decline in revenue (which was largely attributable to a decrement in the net market value of its SGARAs),³ and a \$6.2 million (22 per cent) increase in expenditure (mainly in employee expenses, road construction and the full cost of services previously provided free of charge from the Department of Sustainability and Environment). In addition, revenue and expense data for 2004-05 relate only to the 11 months it operated in that year.

VicForests is subject to dividend and tax-equivalent payments. Dividends are determined by the Victorian Treasurer following consultation with the VicForests Board. A \$3.0 million dividend was distributed in 2005-06 relating to the financial performance in 2004-05. The 2005-06 dividend was not finalised by the reporting date. VicForests is not subject to community service obligations.

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- 1 The Department of Sustainability and Environment is responsible for the stewardship (policy and regulation) of Victorian state forests.
 - 2 Under the *Sustainable Forests (Timber) Act 2004*, the Minister for the Environment made an Allocation Order that VicForests may harvest in three 5-year tranches in the next 15 years. Only timber remaining to be harvested in the 5-year Timber Release Plan (TRP) is valued as SGARAs. There is only one year left in the current TRP so the value of non-current SGARAs is zero. Standing timber in the TRP is measured at fair value less estimated point-of-sale costs in accordance with Accounting Standard AASB 141 *Agriculture*. Fair value is determined using a discounted cash flow method to derive a net present value.
 - 3 Revenue from the sale of forest products remained stable despite the downturn in the housing market because of higher prices.

VICFORESTS (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^a	AIFRS ^a	
	Units	2004-05 ^b	2004-05 ^b	2005-06
Size				
Total assets	\$m	37	37	35
Total revenue	\$m	41	41	37
Profitability				
Operating profit before tax	\$'000	13 135	13 135	2 980
Operating sales margin	%	31.9	31.9	5.7
Cost recovery	%	146.9	146.9	106.0
Return on assets	%	36.8	36.2	8.3
Return on equity	%	36.4	36.3	9.0
Financial management				
Debt to equity	%	0.7	0.7	0.5
Debt to total assets	%	0.4	0.4	0.4
Total liabilities to equity	%	66.0	66.0	46.0
Interest cover	times	34.9	34.9	166.6
Current ratio	%	237.5	208.7	280.0
Leverage ratio	%	162.9	166.0	146.0
Payments to and from government				
Dividends	\$'000	—	—	3 024
Dividend to equity ratio	%	—	—	13.0
Dividend payout ratio	%	—	—	145.0
Income tax expense	\$'000	4 937	4 955	895
CSO funding	\$'000	..	..	..

^a VicForests commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for VicForests. ^b VicForests commenced operations on 1 August 2004. Data for 2004-05 reflect 11 months of operation. .. Not applicable. — Zero or rounded to zero.

Performance indicators before SGARA revaluation 2004-05 to 2005-06

		<i>Pre-AIFRS</i>		<i>AIFRS</i>
	<i>Units</i>	<i>2004-05</i>	<i>2004-05</i>	<i>2005-06</i>
<i>Profitability</i>				
Operating profit before tax	\$'000	10 985	10 985	5 019
Return on assets	%	32.9	32.3	14.0
Return on equity	%	52.0	52.0	21.6

Forestry Plantations Queensland (FPQ) was established on 1 May 2006 under the *Forestry Plantations Queensland Act 2006*.¹ The FPQ manages Queensland's 196 000 hectares of state-controlled softwood and hardwood plantations.

Around \$1.1 billion (87 per cent) of the FPQ's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly each year, affecting measures of profitability and financial management.² The FPQ's total liabilities were \$209 million in 2005-06.

The FPQ posted an operating loss before tax of \$7.4 million for the two months in which it traded in 2005-06. Total revenue was \$17.4 million, which primarily comprised a net increment in the value of its SGARAs (\$15.7 million) and revenue from product sales (\$547 000). Total expenses were \$24.8 million, which included an \$8.4 million devaluation of land, buildings and infrastructure. The operating result before SGARA revaluations was a loss of \$23.1 million. Financial management and profitability ratios are not representative of the performance of the FPQ in 2005-06 because of the short period the entity was in operation.

The FPQ is subject to dividend and tax-equivalent payments. A dividend of \$11.3 million was declared in 2005-06, however, no dividend was paid. The dividend was determined at a negotiated percentage (50 per cent) of profit from ordinary activities after tax-equivalent payments and adjustment in the value of SGARAs. The FPQ recorded an income tax-equivalent expense of \$2.0 million in 2005-06.

The FPQ did not receive community service obligation payments in 2005-06.

¹ The Queensland Government reformed the commercial forest management activities previously undertaken by DPI Forestry in 2006. DPI Forestry was replaced by two new entities, the FPQ and Forestry Plantations Queensland Office (FPQO). The FPQO was established on 1 May 2006 to support and complement the FPQ's operations by providing administrative services and by having the custodial responsibility for the new State Plantation Forest lands. Native forest harvesting formerly managed by DPI Forestry is now managed by the Department of Natural Resources and Water.

² Under AASB 141 *Agriculture*, SGARAs are reported at their net market value. Wollemi pine plants are valued at cost because they have only just been released and neither price nor demand can be predicted with any degree of certainty. The value of plantation growing timber is determined by calculating the net present value of future cash flows expected to be realised from the timber. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

FORESTRY PLANTATIONS QUEENSLAND (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	..	..	1 300
Total revenue	\$m	..	..	17
Profitability				
Operating profit before tax	\$'000	..	..	..
Operating sales margin	%	..	..	..
Cost recovery	%	..	..	..
Return on assets	%	..	..	..
Return on equity	%	..	..	..
Financial management				
Debt to equity	%	..	..	..
Debt to total assets	%	..	..	..
Total liabilities to equity	%	..	..	..
Interest cover	times	..	..	..
Current ratio	%	..	..	..
Leverage ratio	%	..	..	..
Payments to and from government				
Dividends	\$'000	..	..	11 274
Dividend to equity ratio	%	..	..	..
Dividend payout ratio	%	..	..	..
Income tax expense	\$'000	..	..	2 028
CSO funding	\$'000	..	..	—

^a Forestry Plantations Queensland (FPQ) was created when DPI Forestry was split into the FPQ and the Forestry Plantations Queensland Office (FPQO) on 1 May 2006. FPQ data for 2005-06 relate to the period 1 May 2006 to 30 June 2006. As a result, only limited performance data is included in this table. Although earlier data are not available for the FPQ, data for the FPQ's predecessor (DPI Forestry) are available in previous *Financial Performance of Government Trading Enterprises* reports. These data are not directly comparable for a number of reasons. First, DPI Forestry had additional responsibilities to the FPQ which were transferred to the FPQO and the Department of Natural Resources and Water. Second, DPI Forestry did not report under AIFRS prior to 2005-06. Third, DPI Forestry data were based on the Government Financial Statistics framework, whereas the data in this table are based on the FPQ's annual report. .. Not applicable. — Zero or rounded to zero.

Performance indicators before SGARA revaluation 2004-05 to 2005-06

		Pre-AIFRS	AIFRS	
	Units	2004-05	2004-05	2005-06
Profitability				
Operating profit before tax	\$'000	..	..	..
Return on assets	%	..	..	..
Return on equity	%	..	..	..

The Forest Products Commission WA (FPCWA) was established under the *Forest Products Act 2000* and is responsible for the commercial production, allocation and sale of forest products from WA's native forests and state-owned and state-managed plantations. The FPCWA manages tree farms in WA on public and private land.

About \$304 million (71 per cent) of the FPCWA's assets were self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly from year to year, affecting measures of profitability and financial management.¹

The FPCWA reported a \$33.2 million operating profit in 2005-06, a significant improvement on the \$15.1 million loss reported in 2004-05. This was primarily attributable to a \$28.9 million (28 per cent) increase in revenue (mainly related to increased revenue from harvesting operations and revaluation of SGARAs), and a \$19.4 million (17 per cent) decline in expenses (largely attributable to the reversal of provisions made in 2004-05).² The FPCWA's operating profit before tax and before SGARA revaluation increased to \$20.1 million in 2005-06.

The FPCWA is subject to dividend and tax-equivalent payments. No dividend was declared in 2005-06. However, subsequent to 30 June 2006 a dividend of \$2.7 million was declared for the 2005-06 financial year. The FPCWA recorded an income tax-equivalent expense of \$9.8 million in 2005-06.

The FPCWA received community service obligation payments of \$1.1 million for its forest enhancement program. It also received funding from the Australian Government relating to the National Action Plan for Salinity and Water Quality and for the Rural Industries Research and Development Corporation.³

¹ SGARAs are reported at their net market value. The FPCWA determines net market value by calculating the fair value, based on historical volume increases and historical cash flows, less estimated point-of-sale costs and costs necessary to get assets to market. Standing timber less than seven years old is carried at cost. Increments and decrements to SGARAs resulting from market value movements are recognised directly in the statement of financial performance.

² A provision raised for claims against the FPCWA, arising out of the WA Government's *Protecting Our Old Growth Forests* policy, was reversed as the FPCWA was cleared of liability. The amount of this provision was reported as a negative expense.

³ The FPCWA also received \$5.6 million from the Department of Environment and Conservation and the Department of Agriculture for cost recovery operations.

FOREST PRODUCTS COMMISSION (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	399	389	426
Total revenue	\$m	123	102	131
Profitability				
Operating profit before tax	\$'000	-13 319	-15 115	33 196
Operating sales margin	%	-6.1	-9.0	29.8
Cost recovery	%	92.7	89.9	139.3
Return on assets	%	-1.8	-2.3	9.6
Return on equity	%	-3.5	-4.2	9.3
Financial management				
Debt to equity	%	35.9	38.1	34.1
Debt to total assets	%	23.0	23.5	22.2
Total liabilities to equity	%	56.3	61.7	60.9
Interest cover	times	-1.2	-1.5	6.6
Current ratio	%	85.4	161.2	304.8
Leverage ratio	%	156.3	161.7	160.9
Payments to and from government				
Dividends	\$'000	1 470	1 470	—
Dividend to equity ratio	%	0.6	0.6	—
Dividend payout ratio	%	-16.5	-14.4	—
Income tax expense	\$'000	-4 399	-4 938	9 761
CSO funding	\$'000	1 100	1 100	1 070

^a Forest Products Commission of WA (FPCWA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for the FPCWA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. — Zero or rounded to zero.

Performance indicators before SGARA revaluation 2004-05 to 2005-06

		Pre-AIFRS	AIFRS	
	Units	2004-05	2004-05	2005-06
Profitability				
Operating profit before tax	\$'000	-12 822	-14 618	20 116
Return on assets	%	-1.8	-2.2	6.5
Return on equity	%	-8.0	-8.6	5.8

The South Australian Forestry Corporation was incorporated under the *South Australia Forestry Corporation Act 2000*, and commenced trading as ForestrySA on 1 January 2001. ForestrySA is responsible for managing over 125 000 hectares of plantation and native forest. Over 2600 hectares were planted during 2005-06.

Around \$518 million (49 per cent) of ForestrySA's assets were self-generating and regenerating assets (SGARAs) or 'growing timber'. These values can fluctuate significantly each year, affecting measures of profitability and financial management.¹ The value of SGARAs decreased by \$18.7 million in 2005-06.

ForestrySA earns most of its revenue from trading softwood timber products — most of which are used by the Australian building industry. In 2005-06, 1.9 million cubic metres of log and pulp products were sold, of which 63 per cent were log products. Over 1.7 million cubic metres were harvested from ForestrySA plantations, with the balance coming from logs harvested by ForestrySA for private forest owners, mostly in the Green Triangle Region in South Eastern SA.

Operating profit before tax increased by \$4.4 million (20 per cent) in 2005-06. This was mainly attributable to increased revenue from the sale of timber products and community service obligation (CSO) payments from the SA Government, and a devaluation of SGARA assets. Operating profit before tax and before SGARA revaluation fell by \$1.4 million (3.0 per cent) in 2005-06.

ForestrySA is required to make dividend and tax-equivalent payments. In 2005-06, a \$29.7 million dividend was declared² and an income tax-equivalent expense of \$13.4 million was recorded.

ForestrySA received \$4.8 million in CSO funding in 2005-06 to undertake activities including native forest management, forest industry development, policy and legislative support, community use of forests, and community protection.

¹ Most SGARAs are valued at net market value which is defined as the amount expected to be received from the disposal of the existing mix of forest products in an active and liquid market. This was determined by sampling market conditions over the 12 months preceding balance date. This policy is in accordance with AASB 141 *Agriculture*. Young timber is valued at fair value by annually compounding the current replacement cost of a reasonable proxy, from the date of preparation of the site for planting, at the current one-year bond rate.

² This dividend included an extra dividend of \$5 million relating to the 2004-05 financial year. ForestrySA also paid an extra dividend of \$10 million in 2005-06, relating to the 2003-04 financial year. ForestrySA's annual report states that an extra dividend of \$1.7 million is proposed for 2005-06 but was undeclared by the reporting date.

FORESTRY SA (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	1 032	1 035	1 059
Total revenue	\$m	104	104	113
Profitability				
Operating profit before tax	\$'000	22 343	22 337	26 736
Operating sales margin	%	20.6	20.6	22.5
Cost recovery	%	125.7	125.7	128.9
Return on assets	%	2.2	2.2	2.6
Return on equity	%	0.8	0.8	1.3
Financial management				
Debt to equity	%	0.5	0.5	1.0
Debt to total assets	%	0.5	0.5	1.0
Total liabilities to equity	%	3.5	3.5	3.2
Interest cover	times	139.8	139.7	67.5
Current ratio	%	190.4	465.0	610.1
Leverage ratio	%	103.5	103.5	103.2
Payments to and from government				
Dividends	\$'000	21 666	21 666	29 650 ^c
Dividend to equity ratio	%	2.2	2.2	2.9
Dividend payout ratio	%	263.0	263.2	222.3
Income tax expense	\$'000	14 105	14 105	13 396
CSO funding	\$'000	3 600	3 600	4 798

^a ForestrySA commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for ForestrySA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. ^c This includes a \$24.6 million dividend declared for 2005-06 and a \$5.1 million extra dividend declared for the 2004-05 financial year. In addition, ForestrySA paid an extra dividend of \$10.1 million relating to the 2003-04 financial year.

Performance indicators before SGARA revaluation 2004-05 to 2005-06

		Pre-AIFRS		AIFRS
	Units	2004-05	2004-05	2005-06
Profitability				
Operating profit before tax	\$'000	46 862	46 856	45 460
Return on assets	%	4.4	4.4	4.3
Return on equity	%	4.6	4.6	4.4

Forestry Tasmania was established by the *Forestry Act 1920* and is subject to the *Government Business Enterprises Act 1995*. It is responsible for managing approximately 1.5 million hectares of state forests and plantations. Around 2100 hectares of hardwood and softwood plantations were established in 2005-06.

About \$339 million (39 per cent) of Forestry Tasmania's assets are self-generating and regenerating assets (SGARAs). Their value can fluctuate significantly from year to year, affecting measures of profitability and financial management.¹ Total assets increased by 0.9 per cent (\$7.8 million) in 2005-06, mainly because of an increase in the value of forest estate assets such as roads and road structures. Total liabilities increased by 0.2 per cent (\$721 000), mainly because of growth in payables and interest bearing debt.

Forestry Tasmania reported a \$31.3 million pre-tax operating profit in 2005-06, a significant improvement on the \$11.1 million loss reported in 2004-05. Total revenue increased by \$11.9 million (6.9 per cent) — the net effect of a decline in revenue from forest sales, partially offset by an increase in the value of SGARAs and the introduction of the Tasmanian Community Forest Agreement (TCFA).² Total expenses declined by \$30.5 million (17 per cent), mainly because of a \$21.5 million reduction in the value of unfunded superannuation liabilities, but also due to lower contractor and freight expenses (down \$7.6 million and \$2.6 million respectively).

Forestry Tasmania is subject to dividend and tax-equivalent payments. It distributed \$2.4 million in dividends and recorded a \$8.5 million tax-equivalent expense in 2005-06.

Although Forestry Tasmania does not receive funding for community service obligations, its annual report states that it was required to undertake non-commercial activities costing \$4.9 million in 2005-06.

¹ The forest crop is valued using a discounted cash flow method to derive a net present 'market' value of the existing timber. The valuation includes an assumption that existing forest management and silviculture practices will continue. Hardwood and softwood plantations are accounted for under AASB 141 *Agriculture*.

² The TCFA which was established between the Australian and Tasmanian Governments in 2004-05. Projects qualifying for funding under the TCFA include the establishment of hardwood plantations, forestry management activities, road construction for Special Timber Management Units and various other research related tasks.

FORESTRY TASMANIA (continued)

Performance indicators 2004-05 to 2005-06

		<i>Pre-AIFRS^{a,b}</i>	<i>AIFRS^a</i>	
	<i>Units</i>	<i>2004-05</i>	<i>2004-05</i>	<i>2005-06</i>
<i>Size</i>				
Total assets	\$m	863	873	881
Total revenue	\$m	173	172	183
<i>Profitability</i>				
Operating profit before tax	\$'000	861	-11 095	31 313
Operating sales margin	%	1.0	-5.7	17.8
Cost recovery	%	101.0	93.8	121.1
Return on assets	%	0.3	-1.0	3.8
Return on equity	%	0.2	-1.2	4.0
<i>Financial management</i>				
Debt to equity	%	4.6	5.7	6.1
Debt to total assets	%	3.7	3.7	4.0
Total liabilities to equity	%	23.9	55.2	54.6
Interest cover	times	1.5	-4.1	15.9
Current ratio	%	160.9	161.8	147.9
Leverage ratio	%	123.9	155.2	154.6
<i>Payments to and from government</i>				
Dividends	\$'000	5 232	5 232	2 446
Dividend to equity ratio	%	0.8	0.9	0.4
Dividend payout ratio	%	336.2	-78.1	10.7
Income tax expense	\$'000	-695	-4 392	8 526
CSO funding	\$'000	—	—	—

^a Forestry Tasmania commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Forestry Tasmania.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. These data were based on the Government Financial Statistics framework and are not directly comparable with the data reported in this table which are based on GTE annual reports. — Zero or rounded to zero.

Performance indicators before SGARA revaluation 2004-05 to 2005-06

		Pre-AIFRS	AIFRS	
	Units	2004-05	2004-05	2005-06
Profitability				
Operating profit before tax	\$'000	13 506	1 550	24 568
Return on assets	%	1.7	0.4	3.0
Return on equity	%	1.7	-0.1	4.0

11 Australian Government Trading Enterprises

Three government trading enterprises (GTEs) owned by the Australian Government are covered in this chapter — Airservices Australia, Australia Post and Telstra. These GTEs vary significantly in size and in the range of services they provide.

For a discussion of the data, the performance indicators used and some of the factors that should be considered when assessing performance, see chapter 1.

Airservices Australia (ASA) was established in July 1995 under the *Air Services Act 1995*, and is responsible for providing and managing air navigation and air traffic services infrastructure in Australia. The commercial activities and regulatory functions of ASA were separated in April 2004.¹ It is proposed that the regulatory functions will ultimately be transferred to an airspace directorate within the Department of Transport and Regional Services.

The Australian Competition and Consumer Commission approved a new charging regime for aviation rescue and fire fighting services effective from 1 January 2006.

ASA's total assets increased by \$116 million (20 per cent) in 2005-06. This was largely a result of a revaluation of land, buildings, plant and equipment, and an increase in the value of a defined benefit fund asset. Total liabilities increased by \$6.8 million (1.8 per cent). As the percentage growth in assets was less than the percentage growth in total equity, the leverage ratio fell to 222.3 per cent in 2005-06 from 283.1 per cent in 2004-05.

ASA's pre-tax operating profit grew by around \$47.5 million (54 per cent) in 2005-06. This reflected a \$28.0 million (4.9 per cent) decline in total expenses, mainly attributable to decreased employee costs and depreciation expenses, in combination with a \$19.6 million increase in total revenue, primarily because of increased airways revenue.

ASA is subject to dividend and income tax payments. ASA made dividend payments of \$43.1 million in 2005-06, consisting of an interim and final dividend each worth approximately \$22 million. ASA recorded an income tax expense of \$42.1 million in 2005-06.

Prior to 30 June 2005, when the current pricing arrangements came into effect, ASA received community service obligation (CSO) payments of \$7.0 million per year to cap prices at regional and general aviation airports. Under the current arrangements, CSOs are measured as the difference between the cap and the actual cost of the service. As the cap now provides for full cost recovery at these airports, CSO payments are no longer made. In addition, ASA undertakes community service activities that the ASA Board considers to be non-commercial in nature and that were estimated to cost \$3.7 million in 2005-06. These activities include the operation of an Environmental Services Branch, aircraft noise and flight path monitoring, and noise inquiry services to handle questions and complaints.

¹ A separate unit was established within ASA on 1 July 2004. This unit provides regulatory services such as strategic airspace planning for Australian administered airspace.

AIRSERVICES AUSTRALIA (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}		AIFRS ^a
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	601	591	707
Total revenue	\$m	691	664	683
Profitability				
Operating profit before tax	\$'000	82 548	88 155	135 696
Operating sales margin	%	12.6	13.9	20.5
Cost recovery	%	114.4	116.2	125.8
Return on assets	%	14.8	16.0	21.9
Return on equity	%	26.6	27.2	35.5
Financial management				
Debt to equity	%	45.7	48.0	31.5
Debt to total assets	%	16.6	16.9	15.4
Total liabilities to equity	%	174.5	183.1	122.3
Interest cover	times	14.1	15.0	22.3
Current ratio	%	97.6	53.9	30.8
Leverage ratio	%	274.5	283.1	222.3
Payments to and from government				
Dividends	\$'000	30 300	30 300	43 100
Dividend to equity ratio	%	13.8	14.5	16.4
Dividend payout ratio	%	52.0	53.4	46.0
Income tax expense	\$'000	24 313	31 377	42 100
CSO funding ^c	\$'000	7 000	7 000	..

^a Airservices Australia (ASA) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for ASA. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. ^c The community service obligation payment arrangements expired on 30 June 2005. .. Not applicable.

AUSTRALIA POST

Australian Government

Australia Post was established in 1975 and was corporatised in 1989 under the *Australian Postal Corporation Act 1989*. Its principal activities include letter delivery, parcel delivery and logistics, third-party agency services (receiving payments for company and government services and charges), and 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.

Australia Post's pre-tax operating profit was \$516 million in 2005-06, an increase of \$45.8 million (10 per cent) on 2004-05. While total expenses increased by 4.1 per cent to \$4.0 billion, total revenue increased 4.7 per cent to \$4.5 billion because of increased sales revenue.

Australia Post's assets and liabilities increased by \$615 million (15 per cent) and \$198 million (8.9 per cent) respectively in 2005-06. The increase in assets was comprised of growth in non-current assets, particularly in superannuation assets, and the acquisition of the PrintSoft Group which produces software for letter and document production. The increase in liabilities was primarily a result of an increase in deferred tax liabilities.

The debt to equity ratio declined from 27.1 per cent to 22.4 per cent in 2005-06, with debt levels remaining largely unchanged and equity increasing by 21 per cent. The current ratio decreased from 117.3 per cent to 97.3 per cent because of an increase in current liabilities.

Australia Post pays dividends to the Australian Government and is subject to all taxes. It made dividend payments of \$283 million in 2005-06, an increase of \$40.8 million on 2004-05, and recorded an income tax expense of \$148 million.

Australia Post does not receive community service obligation payments. However, it is required to provide letter services that meet (or exceed) specified standards to all parts of Australia at a uniform price. Australia Post estimated that this obligation cost approximately \$87.9 million in 2005-06.

AUSTRALIA POST (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	3 762	4 193	4 808
Total revenue	\$m	4 324	4 326	4 530
Profitability				
Operating profit before tax	\$'000	524 500	469 800	515 600
Operating sales margin	%	11.9	10.4	10.8
Cost recovery	%	113.1	111.4	112.0
Return on assets	%	14.8	12.0	12.2
Return on equity	%	20.7	17.3	16.9
Financial management				
Debt to equity	%	29.3	27.1	22.4
Debt to total assets	%	14.1	12.7	11.9
Total liabilities to equity	%	107.4	112.7	101.3
Interest cover	times	17.2	15.1	17.2
Current ratio	%	127.9	117.3	97.3
Leverage ratio	%	207.4	212.7	201.3
Payments to and from government				
Dividends	\$'000	241 700	241 700	282 500
Dividend to equity ratio	%	13.3	12.3	13.0
Dividend payout ratio	%	64.5	70.8	76.7
Income tax expense	\$'000	149 600	128 500	147 500
CSO funding	\$'000	..	..	..

^a Australia Post commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Australia Post. ^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. .. Not applicable.

Telstra Corporation Limited (Telstra) was established in April 1993 and operates under the *Telecommunications Act 1997*. Telstra was partially privatised in November 1997, when 33 per cent of the Corporation's shares were offered for sale. A further sale of 16 per cent occurred in October 1999. At 30 June 2006, the Australian Government held 51.8 per cent of Telstra's shares.¹

Telstra offers a full range of telecommunication services. Most of these services are provided at both a retail and wholesale level to other carriers, carriage service providers and internet service providers.

Telstra's assets increased by \$964 million (2.7 per cent) to \$36.2 billion in 2005-06. Liabilities increased by \$1.8 billion (8.3 per cent), reducing total equity. The increase in liabilities was mainly attributable to a 7.5 per cent increase in debt and a 23 per cent increase in current liabilities (mainly trade creditors and accruals).

Operating profit before tax was \$4.6 billion in 2005-06, a decrease of 25 per cent from 2004-05. This was partly attributable to expenses related to redundancy and restructuring, resulting from implementing strategic review initiatives.

Telstra's dividend payments to government and other shareholders increased by \$846 million (21 per cent) to \$5.0 billion in 2005-06. This included two special dividend payments totalling \$1.5 billion. Telstra recorded an income tax expense of \$1.4 billion in 2005-06.

Telstra's universal service obligation (USO) requires that standard telephone services, public payphones and prescribed carriage services are reasonably and equitably accessible to all people in Australia, no matter where they live or conduct business. Telstra is also subject to the digital data service obligation (DDSO) whereby it must provide reasonable and equitable access to digital data services with a data speed equivalent to 64 kbps. Telstra fulfils the DDSO by supplying the Integrated Services Digital Network services and satellite downlink services.

Telstra does not receive government funding for the USO or DDSO. However, it receives contributions from other carriers for costs incurred on their behalf.²

¹ The Australian Government sold 34.2 per cent of Telstra in December 2006 through a public sale. As a result, 2005-06 is the last year that Telstra will be reported on as a government controlled business.

² The Minister for Communications determines the net cost of universal service provision, which is then shared among carriers based on the proportion of eligible telecommunications revenue. USO costs were set at \$171 million in 2005-06. Telstra considers that the Australian Government's determination is less than Telstra's actual costs of providing these services.

TELSTRA (continued)

Performance indicators 2004-05 to 2005-06

		Pre-AIFRS ^{a,b}	AIFRS ^a	
	Units	2004-05	2004-05	2005-06
Size				
Total assets	\$m	36 310	35 211	36 175
Total revenue	\$m	22 769	22 431	23 171
Profitability				
Operating profit before tax	\$m	6 269	6 055	4 561
Operating sales margin	%	30.9	31.3	23.8
Cost recovery	%	144.2	145.1	130.4
Return on assets	%	19.6	19.9	15.6
Return on equity	%	29.9	31.5	24.0
Financial management				
Debt to equity	%	89.6	91.1	104.3
Debt to total assets	%	36.7	35.4	37.5
Total liabilities to equity	%	144.0	157.8	181.9
Interest cover	times	8.5	7.3	5.6
Current ratio	%	96.8	87.1	61.9
Leverage ratio	%	244.0	257.8	281.9
Payments to and from government				
Dividends ^c	\$m	4 131	4 124	4 970
Dividend to equity ratio	%	27.8	30.2	37.5
Dividend payout ratio	%	92.9	95.7	156.2
Income tax expense	\$m	1 822	1 746	1 380
CSO funding	\$'000	..	..	..

^a Telstra Corporation Limited (Telstra) commenced reporting under the Australian-equivalent International Financial Reporting Standards (AIFRS) on 30 June 2006. The implications of the transition to AIFRS were discussed in the *Financial Performance of Government Trading Enterprises 2000-01 to 2004-05* report. Data for 2004-05 are reported on an AIFRS and pre-AIFRS basis to illustrate the effect of the transition for Telstra.

^b Data for years prior to 2004-05 are available in previous *Financial Performance of Government Trading Enterprises* reports. ^c Only 51.8 per cent of Telstra's dividend payments (\$2.6 billion in 2005-06) are made to the Australian Government. .. Not applicable.

A Monitored GTEs

Table A.1 **Monitored GTEs — by jurisdiction, 2005-06**

<i>GTE</i>	<i>Sector</i>
New South Wales	
Country Energy	Electricity
Delta Electricity	Electricity
EnergyAustralia	Electricity
Eraring Energy	Electricity
Integral Energy	Electricity
Macquarie Generation	Electricity
TransGrid	Electricity
Forests New South Wales	Forestry
Newcastle Port Corporation	Ports
Port Kembla Port Corporation	Ports
Sydney Ports Corporation	Ports
Rail Corporation New South Wales	Railways
Rail Infrastructure Corporation	Railways
State Transit Authority	Urban Transport
Sydney Ferries Corporation	Urban Transport
Hunter Water Corporation	Water
Sydney Catchment Authority	Water
Sydney Water Corporation	Water
Victoria	
VicForests	Forestry
Port of Melbourne Corporation	Ports
Victorian Regional Channels Authority	Ports
V/Line Passenger Corporation	Railways
Barwon Regional Water Authority	Water
Central Gippsland Water Authority	Water
Central Highlands Water Authority	Water
City West Water	Water
Coliban Regional Water Authority	Water
Gippsland and Southern Rural Water Authority	Water
Goulburn Valley Regional Water Authority	Water
Goulburn–Murray Rural Water Authority	Water

(Continued next page.)

Table A.1 (continued)

<i>GTE</i>	<i>Sector</i>
Grampians Wimmera Mallee Water	Water
Lower Murray Water	Water
Melbourne Water Corporation	Water
South East Water	Water
Yarra Valley Water	Water
Queensland	
CS Energy	Electricity
ENERGEX	Electricity
Enertrade	Electricity
Ergon Energy Group	Electricity
Powerlink	Electricity
Stanwell Corporation	Electricity
Tarong Energy	Electricity
Forestry Plantations Queensland	Forestry
Cairns Port Authority	Ports
Central Queensland Ports Authority	Ports
Mackay Port Authority	Ports
Port of Brisbane Corporation	Ports
Ports Corporation of Queensland	Ports
Townsville Port Authority	Ports
Queensland Rail	Railways
SunWater	Water
Western Australia	
Horizon Power	Electricity
Synergy	Electricity
Verve Energy	Electricity
Western Power	Electricity
Forest Products Commission	Forestry
Albany Port Authority	Ports
Bunbury Port Authority	Ports
Dampier Port Authority	Ports
Fremantle Port Authority	Ports
Geraldton Port Authority	Ports
Port Hedland Port Authority	Ports
Public Transport Authority	Urban Transport
Water Corporation	Water

(Continued next page.)

Table A.1 (continued)

<i>GTE</i>	<i>Sector</i>
South Australia	
ForestrySA	Forestry
TransAdelaide	Urban Transport
SA Water Corporation	Water
Tasmania	
Aurora Energy	Electricity
Hydro-Electric Corporation	Electricity
Transend Networks	Electricity
Forestry Tasmania	Forestry
Tasmanian Ports Corporation	Ports
Metro Tasmania	Urban Transport
Cradle Coast Water	Water
Esk Water Authority	Water
Hobart Regional Water Authority	Water
Australian Capital Territory	
ACTION Authority	Urban Transport
ACTEW Corporation	Water/Electricity
Northern Territory	
Power and Water Corporation	Electricity/Water
Darwin Port Corporation	Ports
Australian Government	
Snowy Hydro ^a	Electricity
Australian Rail Track Corporation	Railways
Airservices Australia	Other
Australia Post	Other
Telstra Corporation	Other

^a Jointly owned by the Australian, NSW and Victorian Governments.

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