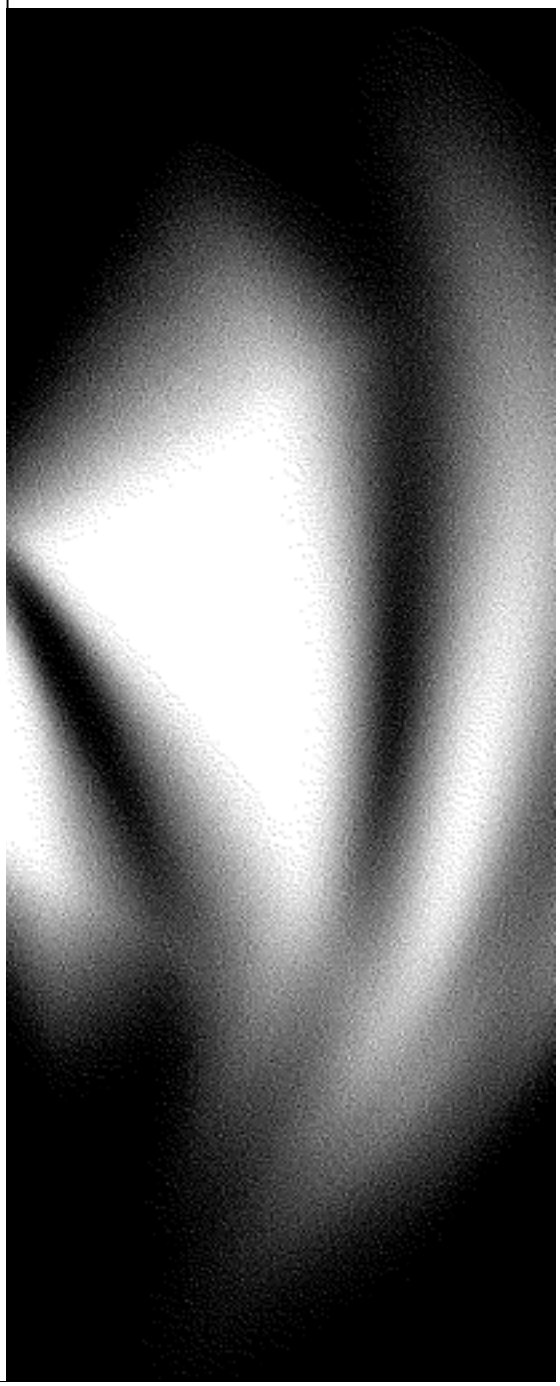
PRODUCTIVITY COMMISSION

Financial Performance of Government Trading Enterprises 1995-96 to 1999-00

Performance Monitoring



May 2001

ISBN 1 74037 026 0

Inquiries:
Media and Publications
Productivity Commission
Locked Bag 2
Collins Street East Post Office
Melbourne Vic 8003

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

An appropriate citation for this paper is:

Productivity Commission 2001, *Financial Performance of Government Trading Enterprises, 1995-96 to 1999-00*, Performance Monitoring, AusInfo, Canberra.

The Productivity Commission

The Productivity Commission, an independent Commonwealth agency, is the Government's principal review and advisory body on microeconomic policy and regulation. It conducts public inquiries and research into a broad range of economic and social issues affecting the welfare of Australians.

The Commission's independence is underpinned by an Act of Parliament. Its processes and outputs are open to public scrutiny and are driven by concern for the wellbeing of the community as a whole.

Information on the Productivity Commission, its publications and its current work program can be found on the World Wide Web at www.pc.gov.au or by contacting Media and Publications on (03) 9653 2244.

Foreword

This report is the second in a series initiated by the Productivity Commission into the financial performance of government trading enterprises (GTEs). The study forms part of a continuing program of research into the performance of economic infrastructure industries and the impact of micro-economic reforms. It is the successor to a series of broader reports by the Steering Committee on National Performance Monitoring of Government Trading Enterprises, with the Commission as secretariat.

For this report, the Commission examined the robustness of key performance measures used for monitoring. This was undertaken to increase understanding of the reliability of performance comparisons over time and across GTEs within an industry sector.

Notwithstanding recent progress on reform, many GTEs are not achieving adequate rates of return. This may detract from the best use of Australia's resources, suggesting the need for a closer examination of the underlying causes, including the current governance and regulatory framework.

Research for the study was undertaken in the Economic Infrastructure Branch, under the guidance of Commissioner Michael Woods. State and Territory governments cooperated by furnishing data collected for the Australian Bureau of Statistics Government Finance Statistics collection. The Commission is grateful for this support.

The Commission would also welcome feedback on this report, consistent with its objective of improving the information base on key issues affecting Australia's economic performance and community living standards.

Gary Banks
Chairman

May 2001

Contents

Foreword **iii**

Table of contents **v**

Abbreviations **vii**

1 Introduction and findings **1**
- 1.1 Background 2
- 1.2 Data 3
- 1.3 Performance indicators 6
- 1.4 Performance measurement issues 14
- 1.5 Effectiveness of financial reforms 33

2 Electricity **43**
- 2.1 Sector reforms 43
- 2.2 Market environment 48
- 2.3 Profitability 52
- 2.4 Financial management 55
- 2.5 Financial transactions 57
- 2.6 GTE performance reports 59

3 Water, sewerage, drainage and irrigation **105**
- 3.1 Sector reforms 105
- 3.2 Market environment 109
- 3.3 Profitability 110
- 3.4 Financial management 112
- 3.5 Financial transactions 115
- 3.6 GTE performance reports 117

4 Urban transport **147**
4.1 Sector reforms 147
4.2 Profitability 149
4.3 Financial management 151
4.4 Financial transactions 153
4.5 GTE performance reports 155

5 Railways **165**
5.1 Sector reforms 165
5.2 Market environment 169
5.3 Profitability 169
5.4 Financial management 172
5.5 Financial transactions 175
5.6 GTE performance reports 177

6 Ports **189**
6.1 Sector reforms 189
6.2 Market environment 193
6.3 Profitability 194
6.4 Financial management 198
6.5 Financial transactions 199
6.6 GTE performance reports 201

7 Commonwealth GTEs **233**

A Participating enterprises, 1999-00 **241**

B Definitions of financial performance indicators **245**

References **249**

Abbreviations

AASB	Australian Accounting Standards Board
ACCC	Australian Competition and Consumer Commission
AIE	Australian Inland Energy
AMSA	Australian Maritime Safety Authority
ARG	Australian Railroad Group
ASA	Airservices Australia
AUSTA Electric	Queensland Generation Corporation
BACL	Brisbane Airport Corporation Limited
BPA	Bunbury Port Authority
BPC	Burnie Port Corporation
COAG	Council of Australian Governments
CPI	Consumer Price Index
CSO	Community Service Obligation
DDO	Digital Data Obligation
DNR	Department of Natural Resources (QLD)
DPC	Darwin Port Corporation
DUS	Department of Urban Services (ACT)
EBIT	Earning Before Interest and Tax
FPA	Fremantle Port Authority
FreightCorp	Freight Rail Corporation

GBE	Government Business Enterprise
GHz	Giga (10^9) Hertz
GOC	Government Owned Corporation
GPA	Gladstone Port Authority
GSE	Great Southern Energy
GTE	Government Trading Enterprise
GWh	Giga (10^9) watt hours
HEC	Hydro-Electric Corporation
HPC	Hobart Port Corporation
HWC	Hunter Water Corporation
IPART	Independent Pricing and Review Tribunal
ISDN	Integrated Service Data Network
kbps	kilo bits per second
Kilolitres	1000 litres
kV	Kilo Volt
kWh	Kilo (10^3) watt hours
ML	Mega (10^6) litres
MPC	Melbourne Port Corporation
MTT	Metropolitan Transport Trust
MW	Mega (10^6) watts
MWC	Melbourne Water Corporation
MWh	Mega (10^6) watt hours
NAU	Network Access Unit

NCP	National Competition Policy
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company
NPC	Newcastle Port Corporation
NRC	National Rail Corporation
NWRWA	North West Regional Water Authority
NWWA	North West Water Authority
ORG	Office of the Regulator-General
PBC	Port of Brisbane Corporation
PDC	Port of Devonport Corporation
PKPC	Port Kembla Port Corporation
PSA	Ports Services Act 1995
PTB	Passenger Transport Board
QPTC	Queensland Power and Trading Corporation
QR	Queensland Rail
QTSC	Queensland Transmission and Supply Corporation
RAC	Rail Access Corporation
RAT	Recoverable Amounts Test
RSA	Rail Services Australia
SA Water	South Australian Water Corporation
SAPC	South Australia Ports Corporation
SAR	Search and Rescue
SCA	Sydney Catchment Authority

SECWA	State Energy Commission of Western Australia
SEQEB	South East Queensland Electricity Board
SEQEC	South East Queensland Electricity Corporation
SERC	Southern Electricity Retail Corporation
SEW	South East Water
SHTPL	Snowy Hydro Trading Pty Ltd
SMHEA	Snowy Mountains Hydro-Electric Authority
SPC	Sydney Ports Corporation
SRA	State Rail Authority
STA	State Transit Authority
SWC	Sydney Water Corporation
SWP	State Water Projects
Tascorp	Tasmanian Public Finance Corporation
TCV	Treasury Corporation of Victoria
UIG	Urgent Issues Group
USO	Universal Service Obligation
VCA	Victorian Channels Authority
YVW	Yarra Valley Water

Box 1 **Key messages**

- Government trading enterprises (GTEs) are an important part of the Australian economy. In 1999-00, the GTEs monitored in this report generated just over $51 billion in revenue.
- In 1999-00, GTEs controlled assets valued at more than $133 billion in the electricity, water, railways, urban transport and ports sectors. The asset base grew by over $4 billion after depreciation and revaluations in the same year.
- Governments have made substantial progress in creating a more commercial environment for these GTEs. Most GTEs have dividend ratios which are generally comparable to those of private companies operating in similar markets. There are provisions for tax-equivalent payments, debt guarantee fees and payments for community service obligations applied to most GTEs.
- The adoption of 'current' valuation methods by the GTEs over the last five years has led to more realistic valuations and increased the comparability of GTE financial performance.
- Notwithstanding this progress towards a more commercial framework, all sectors appear to be earning low rates of return, even if moderate levels of risk are assumed. Only the railways and water sectors have substantially improved profitability over the last five years — but even for these sectors, profitability remains low. Profitability in the urban transport sector has declined.
- The low rates of return may have a number of causes, including some combination of price regulation that suppresses profitability, low productivity growth, incomplete government funding of community service obligations, overvalued assets and the inclusion of a large number of abnormal expenses in GTE accounts.
- In a fully commercial setting, such low rates of return, if expected to continue, would discourage additional investment.
- It may be timely to review the objectives which governments have for their GTEs in the various sectors and the appropriateness of the current governance and regulatory framework.

1 Introduction and findings

This report contains a consistent set of financial performance indicators for 63 government trading enterprises (GTEs) (listed in appendix A). In 1999-00, the GTEs monitored in this report generated $51.1 billion in total revenue, accounting for three quarters of the revenue generated by Australian government-owned businesses (ABS 2000).

The study forms part of the Commission's research into the effects of micro-economic reform. The information was compiled for the purpose of making a general assessment of financial performance within and across industry sectors. It does not provide information suitable for a detailed analysis of the performance of individual GTEs — a thorough examination of their financial statements is required for that purpose.

The performance assessment focuses on the effectiveness of reform measures aimed at giving the Boards of GTEs clear financial objectives, replicating financial market disciplines and ensuring competitive neutrality. Financial performance monitoring facilitates transparency and hence, accountability. It also facilitates yardstick competition — which is important in industries where businesses do not face vigorous competition.

The influences on actual and measured performance over time are identified to provide some explanation of the factors both within and outside the control of GTEs that affect their performance. Some of these include structural reform, changes in the market environment, financial arrangements, comparability of data and changes in accounting procedures.

GTE performance reports are presented on a sector basis — electricity; water, sewerage, drainage and irrigation (referred to hereafter as the water sector); urban transport; railways; and ports (chapters 2 to 6 respectively). The Commonwealth Government GTEs — Airservices Australia, Australia Post and Telstra Corporation — that do not have peers in other jurisdictions are reported separately in chapter 7.

1.1 Background

In 1991, Australian Governments agreed that a system of national performance monitoring of GTEs should be established. The prime objective was to assist governments in their efforts to achieve and sustain performance improvement. Performance monitoring was seen as a way of promoting accountability through transparency, and performance improvement through yardstick competition.

A steering committee — The Steering Committee on National Performance Monitoring of Government Trading Enterprises (referred to hereafter as the Steering Committee) — was established to oversee the monitoring process. It was chaired and serviced by the Industry Commission, a predecessor of the Productivity Commission. The Steering Committee was responsible for the development of nationally consistent performance indicators and their publication on an annual basis.

With the achievement of substantial GTE reform and the privatisation of a number of enterprises, the Steering Committee recommended in 1997 that it should be disbanded.

At the time that formal agreement for disbandment was sought, the Commission indicated that it would continue to monitor GTEs under its general research program. This report is the second released by the Commission.

In continuing to provide a consistent set of financial performance information, it was the Commission's intention to minimise the burden on GTEs by using existing sources of financial data. The main source for this study was the Australian Bureau of Statistics' (ABS) Government Finance Statistics (GFS) collection provided by State and Territory governments.

For consistency, the Commission selected GTEs monitored by the Steering Committee for inclusion in this study. However, State and Territory governments were given the opportunity to nominate GTEs. Several GTEs were added as a consequence and a number were eliminated because they had been privatised.

GTEs that are no longer monitored include:

- ETSA Power, ETSA Transmission and Optima Energy (South Australia);
- Power and Water Authority (Northern Territory);
- ACTEW Corporation (ACT);
- AlintaGas and MetroBus (Western Australia);

- Public Transport Corporation and the State Electricity Commission of Victoria (Victoria); and
- ANL Limited and the Federal Airports Corporation (Commonwealth).

Most of these GTEs have been privatised or their operations contracted out to the private sector. In many cases, they were vertically and horizontally disaggregated before being sold. For example, the State Electricity Commission of Victoria was separated into generation, transmission and retail businesses and these were sold to the private sector between 1995 and 1997.

Each industry chapter of this report includes a summary which draws on the information in the performance reports to make comment on structural reform, market environment and performance. State and Territory governments were given the opportunity to review the GTE performance reports.

1.2 Data

The financial indicators for the years 1995-96 and 1996-97 were brought forward from previous Steering Committee publications. Data provided by GTEs from their financial management systems were used to calculate these indicators.

The data used in calculating the financial performance indicators for 1997-98 to 1999-00 were taken from two sources:

- *The GFS collection* — audited data collected by State and Territory Treasuries for the ABS was used for most indicators. It was chosen as a suitable data source because, when compared to general purpose financial data, it is less likely to be influenced by the policies of individual State and Territory auditors and therefore less likely to differ between jurisdiction.
- *GTE annual report financial statements* — General Purpose Financial Report (GPFR) data was extracted from audited GTE financial statements to supplement the GFS data. GTE financial statements are prepared on an accrual basis in accordance with applicable Australian accounting standards.

The GFS collection is primarily designed for National Accounts purposes. It is based on international standards set out in the *System of National Accounts 1993* and the draft accrual version of the International Monetary Fund's *A Manual of Government Finance Statistics*.

GFS data are consistent with the data collected in the previous Steering Committee publications. The ABS has demonstrated a concordance between the definitions

used for the GFS collection and those used for previous Steering Committee publications (see appendix B).

GPFR data were used to augment GFS data in instances where accrual GFS data were unavailable. For example, one jurisdiction was unable to provide consistent accrual GFS data for 1997-98 to 1999-00.

Further, GPFR data were used when certain items are not reported separately in GFS. For example, there is no distinction between current and non-current assets or current and non-current liabilities in GFS.

There are a small number of discrepancies between GFS data, financial statement data and the data collected for previous Steering Committee reports. The discrepancies arise mainly because GPFR and GFS data serve different purposes. In particular, the accounting treatment of certain items differ (see table 1.1).

Table 1.1 **Differences between GFS and GPFR data**

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

Source: SA Treasury (2001).

Gains and losses

The differing treatment of gains and losses on assets may generate inconsistencies in such areas as profit and loss on the sale of assets, and revenues or expenses arising from asset revaluations. These differences can affect the reported operating profit. For example, under GFS, revaluations are recorded directly in equity and have no influence on operating profit. Under Australian accounting standards, changes in asset valuations may be recorded in the profit and loss statement.[1]

Differences in the approach to the timing of asset valuation also have the potential to generate inconsistencies. Revaluation of non-current assets prior to disposal is not required under accounting standards, whereas under GFS it is. As a result,

1 For an explanation of accounting requirements see section 1.4.

GPFR operating statements may contain gains or losses incurred in the disposal of the asset that are not recorded under the GFS framework.

That said, discrepancies between GFS and GPFR valuations of assets at disposal are not expected to affect indicators substantively. The majority of GTEs value their non-current assets using current valuation methodologies, ensuring minimal gains and losses on disposal.

Distributions to owners

Total expense reported under GFS differs significantly to that reported in GPFRs. With GFS, both distributions to owners in the form of dividends and income tax-equivalent payments are regarded as operating expenses. For the purpose of consistency, and in order to derive meaningful indicators, the total expense figures sourced from the GFS were adjusted to exclude dividend expense and income tax expense.

Prior-period adjustments

Under GFS, operating results reflect only items that represent revenue and expense transactions relevant to the current period, whereas operating results in annual reports may include prior-period adjustments.[2] The Australian Accounting Standards Board (AASB) has outlined when such differences are most likely to occur (see box 1.1).

The treatment of abnormal items that represent transactions relevant to prior-periods has the potential to generate differences in indicators. Under GFS, such items are not reported in the current period — under Australian accounting standards they are.[3]

Abnormal revenue and expense items have been sourced from GPFR data. The indicators for 1995-96 to 1998-99 are brought forward from previous Steering Committee and Commission publications. As such, they were not recalculated to account for GFS treatment of prior-period adjustments. In order to capture prior-period adjustments, GPFR data for abnormal revenue and expense have been used.

---

2 Under GFS prior-period items arising in the current period are allocated to the relevant prior-period. Under Australian accounting standards, prior-period items arising in the current period are allocated to the current period.

3 The cost recovery ratio is the only indicator that uses both GFS and annual report expense and revenue items. The ratio is calculated using annual report data for abnormal revenue, abnormal expense, and receipts from government.

Box 1.1 **Differences generated by prior-period adjustments**

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

Correction of errors — In annual reports, any error made in a prior-period is corrected in the period in which the error is discovered. With GFS, errors relating to prior-periods are adjusted against the relevant prior-period operating results.

Voluntary changes in accounting policy — In annual reports, the effects of any voluntary change in accounting policy are calculated on the basis that the new policy has always been in place. Any effects are recognised as revenues or expenses in the reporting period in which the change is made. With GFS, such effects are adjusted against the relevant prior-period operating results.

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

Source: Material provided by the AASB.

The differences between GFS and GPFR data should be recognised when comparing financial indicators presented in this report and those presented elsewhere. However, these differences do not significantly affect performance indicators and are not significant when considering performance at a broad level.[4]

1.3 Performance indicators

The financial performance indicators in this report are presented under three broad headings — profitability, financial management and financial transactions (see appendix B for how indicators are derived).

Primarily, comparisons of indicators for a GTE over the reporting period provide an overall picture of how the GTE is performing and its performance relative to other GTEs. In some cases, it is appropriate to make comparisons across GTEs in the same sector in Australia. Comparisons with similar businesses operating in other countries may also provide useful information to evaluate the performance of GTEs.

4 Discrepancies between ratios reported by GTEs and those in this report are not attributable to differences between GFS and GPFR data. There are differing definitions of variables and differences in the construction of financial performance indicator formulas presented in annual reports from those used in this report (see section 1.3).

Financial performance indicators may be compared with established 'norms' or 'rules of thumb' that provide indicative benchmarks to evaluate performance. For example, rates of return on equity can be compared with returns available from alternative investment opportunities. It is important to recognise that there are many factors beyond the control of management that may affect year-to-year performance.

Profitability

Profitability indicators provide a concise and consistent way of presenting financial information. In the absence of stock market valuation, they are an important guide to the performance of a GTE.[5] Profitability indicators provide governments and the community with a method of evaluating the efficiency with which GTEs are using the assets vested in them.

That said, profitability can be affected by factors largely outside the control of GTEs. For example, the weather impacts on the revenue of many GTEs in the water sector. This can significantly affect profitability given their high fixed costs.

Over the reporting period, abnormal items contributed to variability in a number of profitability indicators — either through their impact on operating profit, total assets, total liabilities or a combination of these (see section 1.4). In the presence of abnormal items, it may be difficult to judge whether a GTE has performed satisfactorily during a particular financial year because of their impact on indicators.

Operating profit before tax — is an indicator of the operational performance of GTEs, before income tax is paid. It measures the difference between total revenue and total expenses and includes abnormals.

Cost recovery — is an indicator of the ability of a GTE to generate adequate revenue to meet operating expenses. Unlike other measures of profitability, it excludes abnormal revenue and expenses. Investment income, receipts from government to cover operating deficits and gross interest expense are also excluded.

A cost recovery ratio of 100 per cent indicates that a GTE is able to meet its operating expenses from its operating revenue, excluding the cost of servicing debt.

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

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 a GTE uses the assets vested in it to produce operating profit before tax and interest. 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.[6]

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

Financial management

Debt is a major source of funds from which GTEs finance their activities. The capital structure of a GTE is partly determined by the financial risk associated with the use of debt finance. This risk stems from the commitment to pay interest and repay principal, irrespective of earnings. For example, a decline in operating revenue or an increase in the cost of servicing debt can result in liquidity problems if a GTE's debt is not well managed.

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

Debt to total assets ratio — is an indicator of the proportion of assets that are acquired with the use of borrowed capital. It gives an indication of the level of creditor-interest in the GTE.

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

Total liabilities to equity ratio — is an indicator of the exposure to claims over the assets of the GTE by creditors, in the event that the business ceases operations. An

6 The weighted average cost of capital is used by regulators in some jurisdictions to determine price and revenue caps. It provides a target for the return required to compensate for the cost of equity and debt, taking into account the level of risk of the GTE and the risk in the market in which the GTE operates.

acceptable level for these debt ratios is likely to vary over time and between industries.

All of these ratios will be affected by changes in asset values arising from asset revaluations, asset transfers or sales. Some GTEs use different asset valuation methodologies, depending on the type of assets. Reported asset values may vary significantly for a given GTE over time. This can reduce comparability.

Apart from the value of assets, the debt to equity ratio is also affected by changes in liabilities. Equity is a residual measure, obtained by deducting total liabilities from total assets. Any change in the level of liabilities will affect the level of equity. For example, an adjustment to provisions for employee entitlements will, by increasing (decreasing) total liabilities, decrease (increase) the value of equity, other things being equal.

The debt to equity and debt to total assets ratios are also affected by financial restructuring. Financial restructuring in the form of debt for equity swaps, debt transfers to governments and 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.

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.

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.

Interest cover includes abnormal revenues and expenses and can vary significantly over time. The current ratio is less volatile because abnormals are excluded. Consequently, the current ratio is a more stable indicator of liquidity.

Several rules of thumb for current ratio and interest cover are sometimes used as a reference to indicate an appropriate level for these indicators. These range from a minimum of 200 to 300 per cent for the current ratio and a minimum of two times for interest cover.[7] Although these provide a guide for comparison, they may be subject to qualification. For example, a GTE that has stable cash flows may be able to operate with a current ratio or interest cover lower than these rules of thumb.

7 See for example, Hoggett and Edwards 2000, Hey-Cunningham 1998, and Hulls and Yeadon 1992.

Differences in performance indicators

GTEs report financial performance indicators similar to those covered in this report. However, these indicators may not be directly comparable. They are influenced by differing definitions of variables, such as operating profit and debt, and differences in the construction of financial performance indicator formulas, such as return on assets and return on equity, presented in annual reports (see table 1.2).

The ratios presented in this report were defined by the Steering Committee and have been applied in a consistent manner over the course of the reporting period. This was necessary because there are no reporting standards governing the definition of these financial ratios. The calculation of indicators is based on the particular accounting practices adopted and, as such, the ratios are not always consistent. In addition, the reporting of ratios by GTEs is in most cases voluntary and not subject to audit.

One source of difference between indicators reported by GTEs and those reported in this publication, is the practice of averaging assets and equity over the financial year. The Commission uses average assets and average equity in a number of indicators. The value of assets and equity are averaged because the profits were produced by employing assets throughout the financial year and not just on those held at the end of the financial year.

In 1999-00, the commonly reported indicators presented by GTEs were, return on assets, return on equity, interest cover, debt to assets (gearing ratio), debt to equity, current ratio (working capital ratio) and liabilities to equity. Of these reported indicators, only current ratios were the same as those presented in this report.

The indicators reported by GTEs in their annual reports were compared with those in this report. The differences between GTE and Commission calculated ratios were small, chiefly ranging between 0.1 and 3 percentage points. For example, in 1999-00 the Commission reported that Delta Electricity had a return on assets of 13.5 per cent. In its annual report, Delta Electricity presented a return on assets of 11.2 per cent, a difference of 2.3 percentage points.

There are cases, usually associated with abnormals, when significant differences occur. However, these are isolated. For example, in 1999-00 there was only one such instance. Integral Energy reported a return on equity of 6 per cent. In contrast the Commission reported a return on equity of 15.6 per cent. This resulted from differences in the construction of the ratio. In calculating return on equity, Integral Energy excluded abnormal items and income tax from operating profit, thereby decreasing operating profitability by $54 million.

Table 1.2 **Sources of differences between GTE and Commission calculated indicators**

Indicator	*Features of GTE reporting that differ from Commission reporting*
Return on assets	Exclusion of abnormal revenues and expenses in operating profit. Exclusion of capital contributions in operating profit. Exclusion of interest expenses in operating profit. Use of total assets instead of average total assets. Use of fixed assets instead of total assets. Use of net assets excluding interest bearing debt.
Return on equity	Exclusion of abnormal revenues and expenses in operating profit. Exclusion of income tax expenses in operating profit. Exclusion of capital contributions in operating profit. Exclusion of interest income in operating profit. Use of total equity instead of average total equity.
Interest cover	Inclusion of interest expense in earnings. Inclusion of financing charges other than interest in gross interest expense. Exclusion of abnormal revenues and expenses in earnings. Exclusion of capital contributions in earnings. Use of net interest expense instead of gross interest expense.
Debt to assets (gearing ratio)	Use of total assets instead of average total assets. Exclusion of bank overdrafts from debt.
Debt to equity	Addition of debt to total equity in denominator. Exclusion of retained profits in equity.
Liabilities to equity	Exclusion of intangible assets in equity.

Note Productivity Commission definitions are set out in appendix B.

Financial transactions

In 1995, the Council of Australian Governments agreed to a series of reforms designed to improve the performance of GTEs and encourage them to operate on a commercial basis. These reforms encompassed a range of initiatives, including the application of competitive neutrality principles to each of the sectors covered in this report.

These policies are designed to expose GTEs to factor market disciplines and regulations faced by private sector businesses. They include, among other things, the introduction of tax-equivalent regimes, dividend payments, debt guarantee

payments and the identification and explicit funding of community service obligations (CSOs).

Tax-equivalent payments

Tax-equivalent regimes are one of the measures intended to make GTEs operate under arrangements similar to those applying to the private sector. Generally, they require GTEs to pay tax on their operating profit at the same company tax rate as private businesses.

The income tax expense incurred is reported. However, the adoption of tax-effect accounting may result in the income tax expense for any year differing from the actual amount paid to State and Territory governments for that year because of timing differences.[8]

Where a GTE is not subject to a tax-equivalent regime, it potentially possesses a significant advantage over its competitors. This is because, all other things being equal, the GTE can earn the same after-tax commercial rate of return as its competitors at lower prices. Hence, private sector operators, or other GTEs that are subject to tax-equivalent payments, may not be able to compete and potential competitors may be dissuaded from entering the market.

In 1999-00, monitored GTEs paid around $2.5 billion in tax-equivalent payments to governments. This represents an increase of around $1.1 billion in nominal terms since 1995-96. During 1999-00, overall profits for monitored GTEs rose by $1.4 billion compared to the previous year. Despite this growth in profit, tax-equivalent payments declined by $558 million. The decline was due to adjustments to future tax benefits and liabilities by GTEs following the announcement of a reduction in the company tax rate applying from 2000-01.[9]

---

8 Tax-effect accounting in accordance with AASB 1020 *Accounting for income tax* leads to differences in how tax applies to income and the timing of tax payments. Permanent differences between taxable income and accounting income arise when disparities between tax law and accounting standards occur. For example, depreciation on buildings is charged as an expense under accounting profit but may not be allowable as a tax deduction in the calculation of taxable income. Timing differences may arise, for example, because of different depreciation schedules adopted by the GTE and the tax office.

9 Future tax benefits and liabilities were adjusted in 1999-00 by most GTEs, following the announcement by the Commonwealth Government in 1999 of a reduction in the company tax rate from 36 per cent in 1999-00, to 34 per cent for 2000-01 and then to 30 per cent from 2001-02. The total value of the reduction in future tax payable was around $1.1 billion.

Debt guarantee fees

A debt guarantee fee is a payment by GTEs to government to ensure that the financial decisions of GTEs reflect normal commercial circumstances rather than rely on the guarantee (explicit or implicit) by a government. This fee is intended to increase the notional cost of capital to a level obtainable by the GTE as a stand-alone entity without any contingent liability on the government.

In order to replicate the disciplines imposed by financial markets fully, these fees should also reflect differences in the costs of intermediation. These differences arise because investors in private businesses sometimes incur higher transaction costs in obtaining information and in monitoring the borrower. These higher transaction costs are reflected in the cost of capital.

Dividends

Dividend payment policies are justified as a return on the funds that government owners, who act as shareholders on behalf of the community, have invested in GTEs. Dividend payment policies are designed to bring GTEs into line with private sector businesses, which usually return some of their profits to shareholders (see section 1.4).

When a GTE is not required to pay dividends, it has proportionately more funds available for re-investment into its business, either for the development of new products and services or the improvement of existing ones. Further, the GTE need not rely on debt financing to the extent that its rivals must, and thus incurs lower overall operating costs.

For each monitored GTE, the total dividends paid are reported, along with the dividend to equity and dividend payout ratios. The dividend to equity ratio indicates the return to shareholders as a percentage of their equity in the GTE. The dividend payout ratio indicates the percentage of profit that is returned to the government shareholder in the form of dividends.

In 1999-00, the level of dividends paid or provided for was $4.7 billion, a fall of $2.6 billion compared to 1998-99. Although the average dividend to equity ratio was stable at around 7 per cent, the dividend payout ratio fell from 114 per cent in 1998-99 to 62 per cent in 1999-00.

Community service obligations

GTEs often provide economic and social benefits to the community over and above the direct benefits purchased by users of their goods and services. For example, rail GTEs provide community benefits such as reduced pollution and urban road congestion, and greater mobility and access for disadvantaged groups.

Historically, governments have recognised these benefits through the funding of operating deficits that GTEs often incurred as a result of providing these goods and services. However, with the advent of National Competition Policy agreements, most governments now make specific payments for the provision of certain CSOs such as pensioner concession fares.

The explicit CSO payments received by each of the monitored GTEs are recorded within this report.

In 1999-00, governments paid monitored GTEs around $2.3 billion in CSO payments. Urban transport GTEs received around 55 per cent of CSO funding and the water sector received around 18 per cent of CSO payments. In contrast, GTEs in the ports sector received CSO payments of $9.9 million in 1999-00.

However, an examination of annual reports revealed that several GTEs are required by governments to provide and fund non-commercial goods and services internally.

1.4 Performance measurement issues

A key objective of governments when establishing a national system of performance monitoring was to increase accountability for performance. There are substantial public assets under the control of GTEs that are not exposed to actual factor market disciplines, nor competition in many cases. Even though recent reforms have increased the commercial focus of GTEs, exposed some to greater competition and replicated financial market disciplines, the requirement for accountability still exists.

Despite recent reforms aimed at increasing the level of competition faced by GTEs, some still operate in markets where there is little direct competition. In these circumstances, yardstick competition — facilitated by performance monitoring — can add pressure for improvement.

Without comparability and consistency however, transparency is diminished because it becomes harder to distil meaningful conclusions about underlying performance. In previous years, the Commission examined several factors that

might diminish comparability and consistency, including the changed treatment of contributed assets following the development of accounting standards in 1996 and 1998 and CSO policies (see PC 2000).

Asset values and valuation

Asset values influence pricing, cost recovery, capital investment and infrastructure policies. During 1999-00 the level of assets controlled by all the GTEs monitored was valued, by GTEs, at $134 billion. Given the magnitude of the asset base, inappropriate measurement has the potential to affect resource allocation and financial performance monitoring.

This potential is further exacerbated by the characteristics of the assets that GTEs control. GTE assets are in general difficult to value. In particular, not all infrastructure assets have readily observable markets.

Over the reporting period, there have been significant changes in the asset values of most GTEs resulting from capital expenditure, asset transfers, and asset revaluations. In 1999-00, assets grew by more than 5 per cent ($6 billion) compared to the previous year. Of this growth around $860 million was directly attributed to asset revaluations.

Asset revaluations affect year-to-year GTE profitability. In particular, downward revaluations, which have generally been recorded as an abnormal expense, reduce profitability. For example, downward revaluations recorded as abnormal expense items amounted to over $963 million between 1998-99 and 1999-00.[10]

Asset values and related expenses affect almost all the financial indicators presented in this report. Because of the importance of asset values, variations in the methodology, timing and reporting standards associated with valuation may complicate comparison of financial performance over time and between GTEs.

Valuation practices

In the past, historical cost was used as the basis for valuing GTE assets. This method of asset valuation has been progressively abandoned by GTEs over the reporting period. The historical cost method equates asset values with the original purchase price less accumulated depreciation. Historical cost can produce

[10] Under accounting standards, any increase in the value of assets must be recorded in an asset revaluation reserve, with the exception of an increase which must be recognised as revenue if it reverses a downward revaluation previously recognised as an expense in the profit and loss account. A downward revaluation must be recognised as an expense, with the exception of any decrement that reverses a previous revaluation increment. These must be recorded in an asset revaluation reserve.

misleading results due to the impact of changing market environments, technical obsolescence and inflation, particularly given the relative longevity of some assets controlled by GTEs.

In the latest reporting year, GTEs were generally subject to two asset valuation and revaluation standards. These are State and Territory government reporting standards — mainly based on *Guidelines on Accounting Policy for Valuation of Assets of Government Trading Enterprises* — and accounting standards, such as, AASB 1010 *Accounting for the Revaluation of Non-current Assets*.[11]

The Steering Committee recommended in their *Guidelines on Accounting Policy for Valuation of Assets of Government Trading Enterprises* the deprival value approach to valuation based on 'current value to the entity' methodologies. The deprival method is aimed at recognising, as the most appropriate method of valuation, the service potential of assets used by a GTE to pursue its objective. It measures the deprival value — the value to the entity of the future economic benefits that the entity would forego if deprived of the asset.

In applying the deprival value method the basic principles are:

- Where the asset would be replaced or reproduced if a GTE were deprived of its service potential, the value of the asset is measured using current cost — the lowest cost at which the gross service potential of the asset could currently be obtained in the normal course of business. There are three main current cost methodologies (see box 1.2).
- Where an asset would not be replaced or reproduced if a GTE were deprived of its service potential, value should be measured at the greater of its market value and the present value of any future incomes that it may generate (see box 1.2).
- Where the asset is surplus to requirements it should be measured at its market value (selling price).

11 The *Guidelines on Accounting Policy for Valuation of Assets of Government Trading Enterprises* were published in 1994 by the Steering Committee. The Australian Accounting Standard referred to is that which was applicable for the year 1999-00. It should be noted that AASB 1010 and AAS 10 have been reissued as *Recoverable Amount of Non-Current Assets*. The new standards apply to reporting periods beginning on or after 1 July 2000. In addition, two new standards, AASB 1041 and AAS 38 *Revaluation of Non-Current Assets*, have been issued and will apply on or after 1 July 2000.

Box 1.2 **Current valuation methods**

Current cost methodologies

- Current market buying price — measures the current market buying price of a *similar asset*, where a similar asset can be purchased. This method is dependant on the existence of readily observable secondary or primary markets to give a reliable indication of value. As a result, it is not easily applied to many highly specialised and capital intensive infrastructure assets.
- Replacement cost — measures the current cost of replacing the same service potential of the existing asset, where a *differing asset* having a similar purpose can be purchased. It is most applicable in situations where more efficient and technologically advanced assets have superseded existing assets.
- Reproduction cost — measures the cost of replicating the asset's future economic benefits based on a *similar asset* with the same level of technology and scale. It is most suitable to situations where a similar asset exists and the existing asset is not technologically outdated.

Current value methodologies

- Net market selling price — measures the amount which the GTE would expect to receive if the asset were sold at the reporting date less any costs incurred in obtaining the proceeds of the sale. This method depends on the existence of a mature and readily observable market to indicate value. Problems could arise in regard to GTEs as infrastructure assets are not often traded and the resale value of specialised assets can differ markedly from purchase prices.
- Net present value — measures the present value of the net cash inflows that the entity expects to receive from the use of the asset over its remaining life. This approach may be more suitable to GTEs as it addresses the circumstance where the value to the GTE of highly specialised durable assets exceeds their market value.

Source: QLD Treasury (1997).

The choice of methodology adopted under the deprival method is dictated by the nature of the asset being valued. For example:

- *Land* — if land is retained it is valued at the greater of current market buying price (value in use) and the current market selling price of its feasible potential alternative use, taking into account the costs of achieving that potential. If land would not be replaced, it is valued at the greater of net present value in its current use and current market selling value.
- *Specialised assets* (where there is no secondary market for the asset) — if the asset is retained, it is valued at the lower of the current replacement cost or

current reproduction cost. If the asset would not be replaced, it is valued at greater of net present value in use and its selling price.[12]

Australian accounting standards have traditionally been more concerned with the reporting of revaluations rather than the methodologies applied in the valuation. However, AASB 1010 (1999) requires non-current assets to be written downwards to their recoverable amount, when and only if, their carrying amount is greater than their recoverable amount.

In order to meet the accounting standard, GTEs and other private businesses were required to conduct yearly Recoverable Amounts Tests. A direct consequence of the accounting standards is that they place a ceiling on asset valuations.

A Recoverable Amounts Test bears some similarity to the net present value method under the deprival value approach, but there are some differences. Accounting standards defined the recoverable amount of an asset as the net amount expected to be recovered through the net cash inflows arising from its continued use and subsequent disposal. Australian accounting standards did not mandate discounting in 1999-00. Under the deprival value approach the recoverable amount is defined as the greater of discounted net cash inflows based on existing use of the asset or its selling price at the reporting date. Discounting adjusts future income to reflect its present day value.

The adoption of 'current' value or cost methods by the public sector over the reporting period has lead to increased comparability between GTEs. For example, 49 per cent of the GTEs monitored by the Steering Committee in 1995-96 used historical cost valuation methodologies (SCNPMCTE 1997). Of the GTEs monitored by the Productivity Commission in 1999-00, less than 10 per cent employed the historical cost method.

However, comparisons over time have to be interpreted with care. There is a loss of comparability on indicators that include an estimate of asset value, due to the move from historical cost to current value methods. For example, in 1999-00 the Burnie Port Corporation valued its assets using the deprival value method, resulting in a $5.1 million write-down of assets.

As the assets controlled by most of the monitored GTEs are capital intensive, highly specialised and long-lived, the methods most applicable are replacement cost or net present value. Of the current valuation methodologies disclosed in 1999-00, replacement cost is used by over 30 per cent of GTEs and net present value of the

[12] Buying and selling price may differ substantially. For example, a highly specialised machine with no secondary market may have its best alternative use as scrap. Buying and selling prices may also differ as a result of different perceptions of risks associated with the purchase.

asset by over 25 per cent. The remaining GTEs did not disclose the current methodology used. The practice of using the net present value method was spread over all sectors. However, the majority of replacement cost valuations were in the electricity sector, where over 50 per cent of GTEs used depreciated optimised replacement cost method (DORC).[13]

The revaluation of assets using a consistent methodology allows comparison of the performance of entities operating in the same market where revaluations are required because of changed market circumstances. For example, the ports sector in 1998-99 reported $730 million of abnormal expenses resulting from asset write-downs. These write-downs were indicative of a fall in trade and an increase in the average total tonnage per ship visit — as such, they reflect external market change. Adjustments of this nature could be expected to recur in the future.

The use of net present value of the asset, under the deprival principles, implies that some GTEs would not replace their assets if deprived of them — if assets would be replaced, the principles stipulate a current cost valuation (see above). However, it could also indicate that there might be some practical difficulties inherent in current cost methods that lead GTEs to adopt other current value methods. Such difficulties include identifying, costing and depreciating the alternative optimal 'green-fields' investment.

The use of the net present value methodology has important implications for financial performance monitoring. The net present value of cash flows that assets provide is inextricably linked to prices, particularly when they are not set within a competitive market. If prices are set to recover a GTE's cost of capital, the sum of cash flows discounted at the same rate will, by implication, equal its present value. In effect, prices determine asset values and asset values determine the revenue required to recover the cost of capital, and hence the regulated prices.

The circular relationship between price regulation and asset values based on net present value is recognised by regulators. For example, the Queensland Competition Authority in a publication entitled *Draft Decision on QR's Draft Undertaking* (2000) stated that a current cost valuation method, which does not rely on the net present value of the asset, presents the most appropriate approach for asset valuation.

The use of depreciated current replacement cost by regulators avoids the problems of relying on the asset values recorded in companies' accounts, which may be measured using the current value methodology. For example, in a report

13 DORC is defined as the cost of replicating the required service potential of the assets in the most efficient way possible while allowing for the age of the existing assets through depreciation.

commissioned by the Independent Pricing and Regulatory Tribunal of New South Wales (IPART), a replacement cost asset valuation method was adopted when assessing the long-run marginal cost of electricity generation in NSW (CGEY 2000).

The relationship of asset values to performance indicators

Asset values have an integral relationship with most of the indicators presented in this report (see table 1.3). For example, profitability indicators can be misleading if the asset base does not reflect its current value. The carrying or book value of an asset may be less than that of its current value. As a result indicators such as return on assets and return on equity will be overstated.

The level of CSO funding has the potential to affect asset values and performance indicators. GTEs may be required to participate in the provision of non-commercial goods and services. If CSO funding does not fully reimburse the GTE for the costs of provision, the value of the social benefit of the CSO will not be reflected in the financial return of the GTE. As a result, some assets may be undervalued because revenues are lower than they would be if CSOs reflected their benefits. In these circumstances, financial performance indicators, such as return on assets and return on equity, will be affected.

Differences between the treatment of depreciation with current and historical value methods can also affect the comparability of profitability. Historical cost depreciation is treated solely as a cost allocation mechanism. Depreciation expense under all current valuation methodologies may be variable, as it can reflect the change in the value of the asset over the reporting period attributable to changed income flow or market conditions, thus reflecting technological and market change.

Similarly, the comparability of equity-based indicators can be affected, both between GTEs and over the time period.[14] Specifically, when a GTE shifts from historical to current valuations there is a once-off recognition, in equity, of any differential between the historical cost and the current asset value. For example, if the current value exceeds the historical cost, equity will increase.

14 Equity represents the residual interest of the owner in the assets of the entity and may be thought of as the government's residual claims against the net assets of the entity. In the case of some GTEs, equity is also referred to as accumulated surplus.

Table 1.3 **Performance indicators and asset value**

Indicator	*Definition*	*Relationship with asset value*
Operating profit before tax (includes abnormals)	Net operating profit plus abnormals before the deduction of tax expense.	Depreciation expense based on asset values is used to calculate operating profit.
Operating sales margin	$\frac{\text{EBIT - investment income}}{\text{Total revenue - investment income}}$	Depreciation expense based on asset values is used to calculate earnings.
Cost recovery	$\frac{\text{Revenue from operations}}{\text{Expenses from operations}}$	Depreciation expense based on asset values is used to calculate net expenses.
Return on assets	$\frac{\text{EBIT}}{\text{Average total assets}}$	Depreciation expense based on asset values is used to calculate earnings. Direct use of asset values.
Return on equity	$\frac{\text{Operating profit after income tax}}{\text{Average total equity}}$	Depreciation expense based on asset values is used to calculate operating profit. Equity is the difference between total assets and total liabilities.
Debt to equity	$\frac{\text{Debt}}{\text{Total equity}}$	Equity is the difference between total assets and total liabilities.
Debt to total assets	$\frac{\text{Debt}}{\text{Total assets}}$	Direct use of asset values.
Total liabilities to equity	$\frac{\text{Total liabilities}}{\text{Total equity}}$	Equity is the difference between total assets and total liabilities.
Interest cover	$\frac{\text{EBIT}}{\text{Gross interest expense}}$	Depreciation expense based on asset values is used to calculate net EBIT.
Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$	Direct use of asset values.
Leverage ratio	$\frac{\text{Total assets}}{\text{Total equity}}$	Direct use of asset values. Equity is the difference between total assets and total liabilities.
Dividend to equity ratio	$\frac{\text{Dividends paid or provided for}}{\text{Average total equity}}$	Equity is the difference between total assets and total liabilities.
Dividend payout ratio	$\frac{\text{Dividends paid or provided for}}{\text{Operating profit after tax}}$	Depreciation expense based on asset values is used to calculate operating profit.

A positive outcome of the adoption of current value or cost methods for performance monitoring is that the revaluation of assets represents changes in the expectations of future operating conditions. These changing expectations are then reflected in the fluctuating levels of equity in the GTE. As a result, equity may more closely mirror the role of the share price of a private sector listed company as an indication of changed expectations.

Abnormal and extraordinary items

The inclusion of both abnormal and extraordinary revenues or expenses can have an appreciable effect on financial performance indicators. The inclusion of these items in many financial indicators makes it difficult to compare the performance of GTEs over time and across GTEs at a given point in time. For example, some GTEs can make profits in some years because of the inclusion of abnormal items and not because of underlying performance improvements.

Abnormal items occur for many reasons, some reflecting the broader policy agendas of owner governments. They can also arise from recognition of poor performance in the past and a necessary cost of improved performance in the future. For these reasons they have been included in financial performance measures from the commencement of national GTE performance monitoring.

Australian accounting standards require the separate disclosure of abnormal and extraordinary items in annual financial statements. Their disclosure is intended to allow observers to distinguish between what constitutes 'ordinary' operating profit or loss and what would be regarded as 'abnormal'.

Abnormal items are defined in accounting standards as revenues or expenses of a 'recurring' nature, which are considered abnormal by reason of their size and effect on financial performance. For example, downward adjustments to asset value resulting from revaluations may be significant enough to warrant their separate disclosure as an abnormal item in a GTE's profit and loss statement.[15]

Extraordinary items are similar to abnormal items, but differ in that they are revenues or expenses that result from events that are outside normal operations and of a non-recurring nature. The AASB gives examples such as, destruction of property due to an earthquake or the expropriation of assets by government.

15 In cases where the downward adjustment is not a decrement reversing a previous increment (see footnote 12).

By their nature, extraordinary items are rare. Only one GTE reported extraordinary items in 1999-00.[16] Due to the infrequency of such items and the expected similarity of their effect on financial indicators, the following discussion focuses mainly on abnormal items.

Abnormal items reported by GTEs 1998-99 and 1999-00

The number and size of abnormal revenues and expenses may decline as the reform process takes effect. With the implementation of reforms such as financial restructuring and rationalisation of operations, the level of abnormal items disclosed could be expected to be high initially.

Abnormal items reported by GTEs for 1998-99 and 1999-00 had a total value of $5.9 billion in absolute terms (see table 1.4). These items are readily grouped into the following categories:

- *Asset revaluations* — includes the recognition of downward adjustments in the value of land and buildings as expenses.
- *Asset consolidations and disposals* — includes revenues or expenses resulting from land rationalisation, asset transfers and the disposal of assets either through sale or other means such as decommissioning.
- *Redundancy payments* — includes items resulting from redundancy programs. These are predominantly expenses, such as employee termination payments.
- *Financial restructuring* — includes revenues or expenses related to financial restructuring and the retirement of debt.
- *Superannuation adjustments* — includes recognition of benefits from overfunded superannuation reserves, adjustments to prepaid superannuation and funding adjustments due to actuarial assessment or changes to the liability base. Most of the items disclosed under this classification represented revenues, although some expenses were reported such as those arising from underfunded superannuation.
- *Other* — includes items that do not readily fall under any of the preceding categories. The most significant items were legal costs, GST transition costs and year 2000 compliance costs.

16 TransAdelaide reported net extraordinary revenue of $2.3 million relating to its withdrawal from the provision of bus services. This included extraordinary revenue of $11.3 million received from the South Australian Department of Treasury and Finance. Extraordinary costs incurred in the withdrawal included direct costs ($3.1 million), fleet and depot restoration costs ($5.9 million), employee termination payments ($0.06 million) and written-off tax losses ($7.6 million).

Table 1.4 **Abnormal expenses and revenues, 1998-99 to 1999-00**

	1998-99[a]		*1999-00*[b]	
Item	*Number*	*Value ($M)*	*Number*	*Value ($M)*
Asset revaluations	10	885.4	6	78.0
Asset consolidations and disposal	17	827.4	16	115.8
Redundancy payments	10	134.2	9	759.5
Financial restructuring	6	152.5	5	89.1
Superannuation adjustments	9	81.7	18	495.0
Other	44	389.5	47	378.4
JORN	0	0	2	1 468.0
All	**96**	**2 470.7**	**103**	**3 383.8**

[a] In 1998-99, 38 GTEs disclosed abnormal revenue or expense items. The ports sector recorded the highest level of abnormal items (in dollar terms), with a large proportion attributable to asset consolidation and disposal. Tasmanian GTEs had the highest level of abnormals (in dollar terms), most of which were asset consolidation and disposal. [b] In 1999-00, 44 GTEs reported abnormal revenues or expenses. The electricity sector recorded the highest number and value of abnormal items with a large proportion attributable to financial restructuring and superannuation adjustments (not including JORN). The water sector also recorded a high level of superannuation adjustments (in dollar terms). NSW GTEs had the highest number and value of abnormal items, most of which were superannuation adjustments in the electricity sector.

Source: PC estimates.

Abnormal revenues and expenses associated with Telstra and the Jindalee Operational Radar Network (JORN) are recorded separately in table 1.4 because of their size. Telstra disclosed abnormal revenue from the JORN contract of $734 million and abnormal expenses incurred in performing obligations under the JORN contract of the same amount. These two items offset each other and do not affect Telstra's profitability.

Most of the abnormal items disclosed in 1998-99 and 1999-00 appear to be associated with reform. For example:

- *Asset revaluations*, a major source of abnormal items, are a direct consequence of the adoption of current valuation methods.
- Abnormal items associated with *asset consolidation and disposal* are the most frequently disclosed items, accounting for just over 16 per cent of the total value of all abnormals over the two years (see table 1.4). They typically arise from restructuring such as the shedding of non-core activities and the separation of responsibility for regulation and policy making from service delivery.
- Items under the category of *redundancy payments* can also be caused by restructuring and labour productivity improvements.
- Abnormal revenues and expenses attributable to *financial restructuring* can be a consequence of moving to a more appropriate balance between debt and equity.

- Items classified as *superannuation adjustments* are related to reform such as the adoption of accrual accounting practices and improvements in labour productivity.[17]

The reporting of abnormal items by monitored GTEs

One issue concerning abnormals is the lack of consistency in their disclosure. What constitutes an abnormal item depends on subjective judgements about the importance of each item to the overall profit or loss.

This subjectivity is evident in the range of reported abnormal revenues and expenses. For example, in 1999-00 the Port of Launceston disclosed an abnormal expense of $28 700, representing less than 2 per cent of operating profit (before tax). In contrast, the Victorian Channels Authority in 1999-00 was exempted, by the Minister for Finance, from disclosing additions to assets — channels transferred from predecessor authorities — valued at $78.1 million as abnormal revenue. This revenue item was more than 20 times greater than the reported operating profit (before tax) for 1999-00.

Subjectivity in reporting may lead to inconsistent and misleading performance indicators. For example, varying the nature and amount of abnormal expenses and revenues can create an impression of profit change. Operating profit excluding abnormals can be made to appear higher by reporting some expenses as abnormal. On the other hand, if revenue is not reported as abnormal, apparent operating profit (excluding abnormals) is improved.

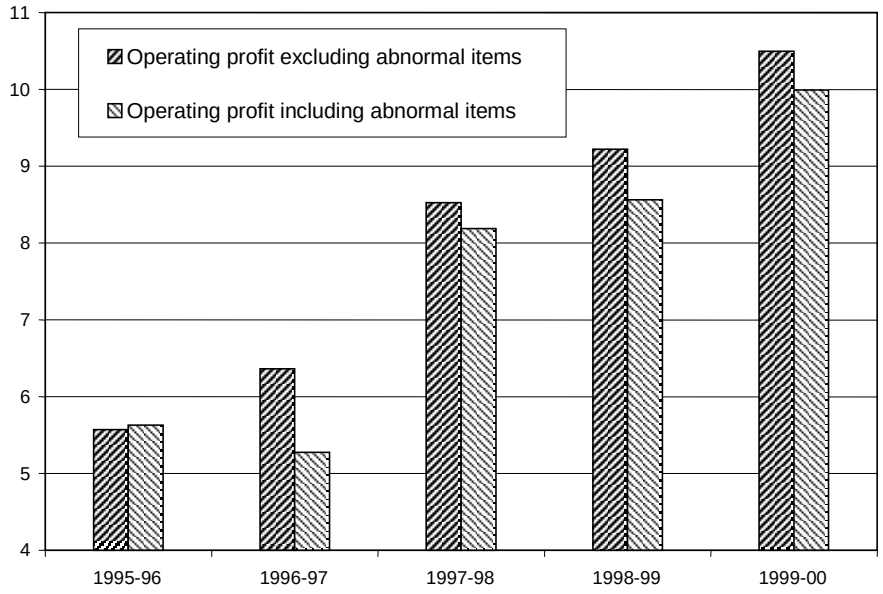
Analysis of abnormal items over the reporting period indicated that the number and value of abnormal expenses generally outweigh abnormal revenues. The disclosure of expenses results in operating profit excluding abnormal items being greater than operating profit including abnormal items over the reporting period (see figure 1.1).

This trend of disclosed expenses exceeding revenues may be attributed, in the short term, to the considerable level of restructuring which has accompanied GTE reform. Under these circumstances, it would be natural to expect GTEs to incur abnormal expenses.

---

17 A liability in respect of superannuation may be recognised and measured as the difference between the present value of employees' accrued benefits at the reporting date and net market value of the superannuation fund's assets at that date. The present value of accrued benefits may be based on expected future payments arising from membership of the fund at the reporting date.

Figure 1.1 **Operating profit including and excluding abnormal items, 1995-96 to 1999-00 ($billion)**



Note Operating profit is expressed in nominal terms.

Source: PC estimates.

A consequence of such a trend is that, in general, indicators based on operating profit including abnormal items have produced lower results than indicators that exclude them. Ratios such as return on assets, return on equity and interest cover are generally lower if abnormal items are included.

Effect of abnormal revenues and expenses on financial performance indicators

The impact of abnormals on indicators has to be assessed on a case-by-case basis. For example, the inclusion of abnormal items reported by Transgrid and the Darwin Port Corporation led to significant differences in several financial performance indicators (see table 1.5).

The inclusion of abnormal expenses deflates indicators in a particular year. For example, the Darwin Port Corporation's return on assets, in 1999-00, was 7.6 per cent before abnormals, but after the inclusion of abnormal expenses fell to -43.4 per cent.

Table 1.5 **Effect of abnormal items on indicators, 1999-00**

		Transgrid[a]		*Darwin Port Corporation*[b]	
Indicator	*Unit*	*Excluding abnormals*	*Including abnormals*	*Excluding abnormals*	*Including abnormals*
Operating profit before tax	($M)	87.1	152.8	4.2	-47.7
Operating sales margin	(%)	45.5	64.1	19.6	-117.5
Return on assets	(%)	7.0	9.8	7.6	-43.4
Return on equity	(%)	5.3	10.4	5.7	-97.7
Dividend payout ratio	(%)	79.4	40.6	0.0	0.0

a In 1999-00, Transgrid disclosed abnormal revenue of $65.6 million generated by superannuation funds reserve contributions. The calculation of the annual superannuation provision is undertaken by an actuarial review of assumptions used in the prior year. In 1999-00 these assumptions changed and resulted in a significant movement in the accrued superannuation liability. There was no other abnormal item reported in that year. **b** In 1999-00, the Darwin Port Corporation disclosed a net abnormal expense of $51.9 million largely attributable to a devaluation of non-current assets ($60.6 million).

Care should be taken when interpreting the effect of abnormal items on dividend payout ratios as the actual level of dividends paid may be decided after abnormal items. For example, in light of the abnormal expense disclosed by the Darwin Port Corporation in 1999-00, it was not required to provide a dividend.

In October 1999, AASB 1018 *Statement of Financial Performance* was reissued.[18] One of the differences between the revised standard and the standard under which GTEs operated is that the requirement to identify separately abnormal items in the profit and loss statement has been removed. Under the reissued standard, such items are to be disclosed in the accompanying notes.

The new treatment is in accordance with the long-standing approach used for monitoring GTE performance established by the Steering Committee. This will increase the consistency and comparability of financial performance indicators presented in financial statements prepared by GTEs with those used by the Commission.

18 The new standard is operative for half years ending on or after 31 December 2000 and for financial years ending on or after 30 June 2001. In instances where specific items are of such a size or nature that disclosure is relevant to explaining the GTEs' financial performance, the nature and amount of such an item must be disclosed separately in the accompanying notes. Under the new standard, extraordinary items are required to be disclosed in the profit and loss statement.

Dividend policies

Dividend payments are made out of a company's current and past profits and represent part of the return to shareholders on capital invested in the business.[19] The other part of the return to shareholders are capital gains, realised in the case of publicly listed companies when shares are traded.

The relative size of dividend payments is often expressed in terms of the dividend payout ratio, which indicates the percentage of profit that is returned to shareholders in the form of dividends. An alternative measure is the dividend to equity ratio, which indicates the return to shareholders as a percentage of their equity. Both indicators may provide useful comparisons for GTE managers as well as government shareholders aiming to replicate financial market disciplines and practices.

Dividend payments by private businesses

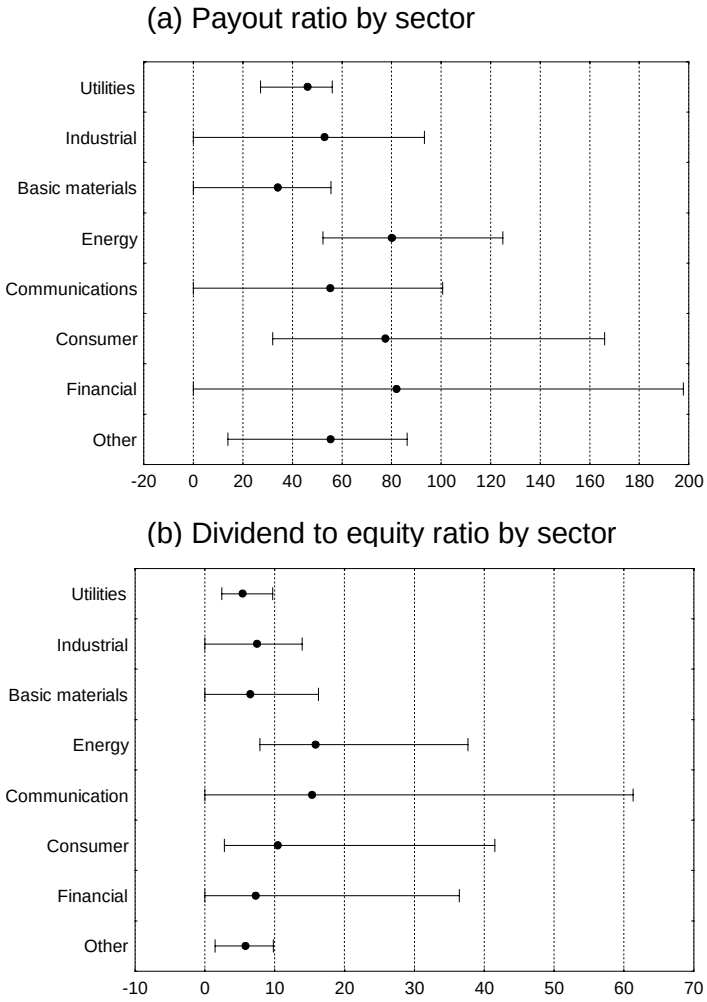
Private businesses listed on the Australian Stock Exchange paid around $24.2 billion in dividends in 1999-00. There was significant difference in the proportion of profits returned to shareholders by companies, both within and between sectors, as measured by the dividend payout ratio and dividend to equity ratio (see figure 1.2).

When a company board makes a recommendation for the payment of a dividend it does so with reference to potential business growth and level of risk. Future investments may be funded from accumulated profits or raised in other ways, including the issue of shares (for listed companies) or borrowings.

The preferences of shareholders can also influence a board's decision on the distribution of dividends. For example, the taxation system may favour capital gains over income and provide reason for some shareholders to prefer lower dividends.

[19] Under Corporations Law, dividends may only be taken out of operating profit (including retained earnings). Several court decisions have also allowed the payment of dividends from asset revaluation reserves. In the GFS framework, the proportion of dividend payment exceeding 100 per cent of annual profit would not be classified as a current year receipt. Any additional payments from retained earnings or asset revaluation reserves are treated as capital returns·

Figure 1.2 Dividend ratios, largest 100 ASX listed businesses, 1999-00 (per cent)



Note The dot represents the mean value and the 'whiskers' represent the range of values for a given performance indicator by sector. For example, the minimum dividend payout for the utilities sector was 27.2 per cent. The mean payout ratio for was 46.2 per cent. The maximum dividend payout was 56.0 per cent. Other includes technology and diversified businesses.

Data source: PC estimates based on Bloomberg (2001).

Dividend payments by GTEs

The payment of dividends by GTEs is part of a range of competitive neutrality policies introduced by governments requiring them to operate on a commercial basis. The payment of a dividend by a GTE is also intended to replicate the financial market discipline of providing a return to shareholder governments on equity invested in the GTE.Dividends from GTEs may represent a significant part of a government's budget. For example, in 1999-00 dividend payments contributed 3 per cent of total revenue in the NSW State budget.

Shareholder governments received around $3.5 billion in dividend payments from monitored GTEs in 1999-00. Around 40 per cent of this amount was paid by Commonwealth Government GTEs. Electricity GTEs accounted for 30 per cent of dividend payments and water GTEs accounted for 25 per cent.

As shareholders, governments may have preferences over how dividends are distributed by GTEs. For example, to meet financial commitments, governments may prefer a stable level of dividends in each year rather than a payment based on a stable proportion of operating profit.

Most shareholder governments have a published dividend policy that sets out the main requirements for a GTE to take into account when considering the payment of a dividend (see box 1.3).

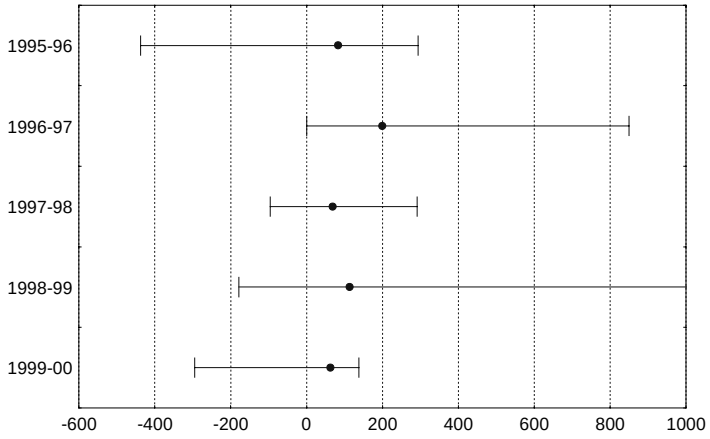
Box 1.3 **Main features of dividend policies for GTEs**

- No jurisdiction appears to use a fixed formula to determine the level of dividend each year. Tasmania is the only jurisdiction that limits in legislation the amount of the dividend paid to the level of after tax profit.
- With the exception of South Australia (where dividends are set out over a four year period), dividends are negotiated annually as part of the corporate planning or budget process.
- Many jurisdictions negotiate dividends based on a proportion of post-tax (including abnormals) profits. These were used by the Commonwealth, Western Australia (for water and electricity GTEs), Tasmania and the Northern Territory. Pre-tax profits were used as a basis by South Australian GTEs. Victoria used both pre-tax and post-tax profits. Western Australian port GTEs used the ratio of total liabilities to total assets as the basis of payment.
- Where a proportion of post-tax profits was used, a payout ratio of 50 per cent is generally applied as an indicative level when negotiating a target or amount of dividend payment. One exception is the Commonwealth, which used 60 per cent of post-tax profits. For those jurisdictions using pre-tax profits, Victoria nominated a rate of 65 per cent and South Australia nominated 60 per cent as a basis for negotiation.
- All dividends declared by the boards of GTEs are required to be approved by either the treasurer and/or the relevant minister. However, in most jurisdictions, the Treasurer and/or relevant minister has the power to direct the amount of dividend that the GTE must pay.
- Generally, most jurisdictions require dividends to be paid within six months after the end of the financial year (December). One exception is Tasmania, where dividends must be paid within 12 months.

Sources: State and Territory legislation covering GTEs and published and unpublished dividend policies.

Between 1995-96 and 1999-00, the average dividend payout ratio for monitored GTEs has varied (see figure 1.3). There was significant variability in the payout ratio for individual GTEs around the average. This reflects the variability in profit as each sector has undergone restructuring and may also reflect changes in dividend policy over the period. High positive and negative payout ratios for some GTEs may reflect financial restructuring or the payment of 'special' dividends that are not representative of long-run operating results.

Figure 1.3 **Average dividend payout ratio, monitored State and Territory GTEs, 1995-96 to 1999-00 (per cent)**



Note The dot represents the mean value and the 'whiskers' represent the range of values for a given performance indicator by jurisdiction. For example, the minimum dividend payout ratio in 1995-96 was -437 per cent, while the maximum value was 294 per cent. The mean payout ratio for 1995-96 was 83 per cent. The maximum dividend payout in 1998-99 was 1 644 per cent.

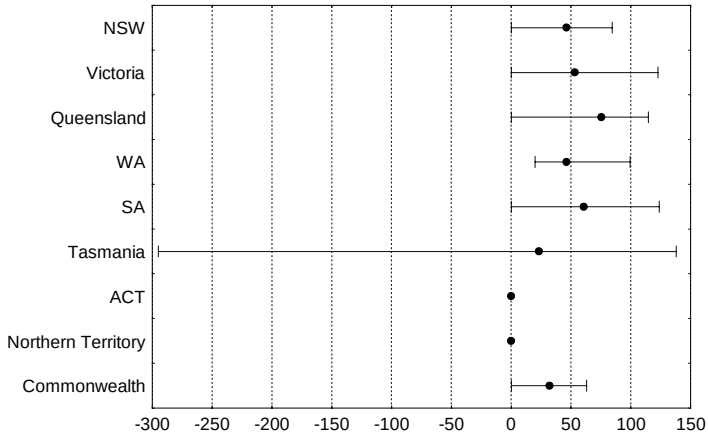
Data source: PC estimates.

In all years except 1996-97, there were occasions where negative dividend payout ratios were recorded. A negative payout ratio implies that GTEs are paying dividends when losses are incurred. For the largest 100 publicly listed private businesses, there were no instances of negative payout ratios in 1999-00.

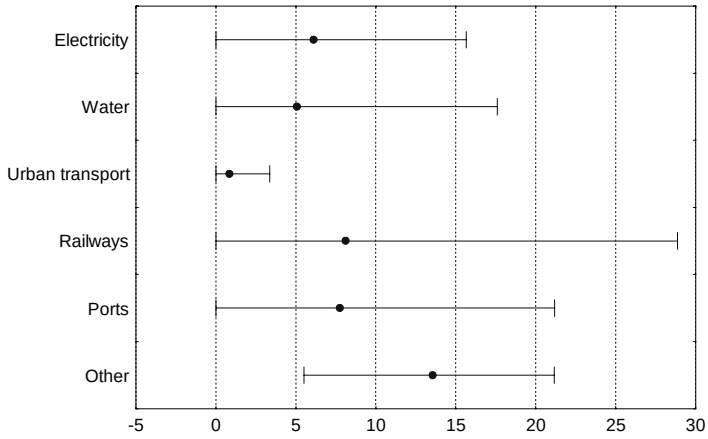
In 1999-00, the average value and range of dividend payout ratios for GTEs varied between jurisdictions (see figure 1.4). The data show that some jurisdictions achieved average dividend payout ratios around the level used as a starting point for dividend negotiations between GTEs and governments.

Figure 1.4 **GTE dividend ratios, 1999-00 (per cent)**

(a) Payout ratio by jurisdiction



(b) Dividend to equity ratio by sector



Note The dot represents the mean value and the 'whiskers' represent the range of values for a given performance indicator by jurisdiction and sector. For example, the minimum dividend payout ratio in NSW was zero, while the maximum value was 84 per cent. The mean payout ratio for NSW was 46 per cent.

Data source: PC estimates.

There were instances in several jurisdictions where dividends appear to be unrelated to profits. For example, in Tasmania in 1999-00, the Hydro-Electric Corporation paid a dividend of $45 million despite a loss of $2 million, leading to a large negative dividend payout ratio. Further, a dividend payout ratio higher than 100 per cent was recorded for the Hobart Regional Water Authority, which made a dividend payment of $2.5 million after earning $1.9 million in profits.

With the exception of urban transport, where the average dividend payout and dividend to equity ratio are comparatively low, most sectors appear to have average dividend ratios that are similar to private companies operating in comparable markets — namely, the utilities sector (compare figure 1.2 with figure 1.4). For

example, the average dividend to equity ratio for GTEs in the electricity, water, railways and ports sectors are similar to private businesses in the utilities sector.

The payment of dividends by GTEs may affect several financial performance indicators. The indicators may be affected in the period that the dividend is declared as well as future periods when the dividend is paid. If a dividend is declared at the end of the financial year, it directly increases liabilities and affects the current ratio (decreasing the ratio) and total liabilities to equity (increasing the ratio).

The payment of a dividend may also affect several financial indicators in future periods, depending on whether the dividend is directly paid out of cash or whether the GTE borrows additional funds. The source of funds for dividend payments affects the level of assets, liabilities and borrowings, and therefore the return on assets, return on equity, and other indicators in future periods. The effect on the indicator depends on the incidence and relative size of the dividend to assets, liabilities and debt.

On average for the monitored GTEs, dividends in 1999-00 were a relatively small proportion of liabilities, assets and borrowings. This suggests that there is likely to be only a small effect on performance indicators at the margin for most GTEs in terms of differences in the level of dividend over time and between GTEs. For example, a 10 per cent change in the level of dividends would, on average, change the debt to total assets ratio by 0.5 percentage points. That said, with large changes in the level of dividend payments, the impact on performance indicators could be more significant.

1.5 Effectiveness of financial reforms

An important objective of the GTE reform process has been to replicate financial market disciplines. Doing so improves incentives for sound investment, resource allocation and management decisions generally.

Profitability

Assets are used to produce goods and services and generate profits. Profits add value to shareholders' equity (in this case, governments on behalf of the community). If profits are insufficient to generate the returns available from alternative investments, having regard for differences in the level of risk, this suggests that the capital embodied in the assets could be put to more productive use.

An inadequate return on assets may expose governments and the broader community to additional risk. Prices that do not provide for an adequate return on assets may distort resource allocation in upstream and downstream markets. Failure to recover the cost of capital may compromise investor support for efficient investment.

Poor returns also raise competitive neutrality issues. If GTEs are not earning a commercial rate of return on appropriately valued assets it could be because they are offering lower prices than their private sector counterparts, prices that are not covering full costs, including the cost of capital.

Although the volatility in the indicators makes it difficult to examine trends, it is possible to detect a steady improvement in the financial performance of most GTEs over the reporting period. For example, more GTEs are recovering over 100 per cent of their operating costs and more are earning positive returns on assets and equity at the end of the period than at the beginning.

However, there are a number of GTEs that continue to perform poorly. Some GTEs, notably in the urban transport and rail sectors (see chapters 4 and 5) are not meeting their recurrent costs and are consequently earning very low or negative returns on assets and equity.

The inability of a GTE to meet its recurrent costs raises concerns about its financial viability. Under these circumstances a GTE will be unable to meet its commitments from its current earnings, raising questions about the adequacy of existing governance arrangements, including pricing and the size of CSO payments where appropriate.

Moreover, many GTEs are not earning an adequate rate of return on assets and equity. An adequate return would be the risk free return on capital plus an amount reflecting the non-diversifiable risk inherent in the investment.[20] The 10 year Commonwealth Government bond rate is widely used as the risk free return benchmark.

Some typical values estimated by regulators for the overall rate of return (including an allowance for non-diversifiable risk) include:

- A nominal post-tax return of between 10.5 per cent and 13.5 per cent for electricity distributors in NSW over the period February 2000 to June 2004 (IPART 1999a);

20 Non-diversifiable risk is the systematic or 'market risk' which cannot be managed.

- A real pre-tax return of 8.5 per cent for Melbourne Port Corporation over the period 2000-01 to 2004-05 (ORG 2000); and
- A nominal pre-tax return of between 8.2 per cent and 10.8 per cent for the NSW rail access regime (IPART 1999b).

The average rate of return on 10 year Commonwealth Government bonds in 1999-00 was 6.6 per cent.[21] Although some GTEs are earning nominal rates of return above this, the majority are not (see table 1.6 and figure 1.5). Given the non-diversifiable risk inherent in any business activity, it is reasonable to expect that GTEs should be generating returns above this rate.

Table 1.6 **Selected profitability measures across sectors, 1999-00 (per cent)**

Sector	*Cost recovery*		*Return on assets*		*Return on equity*	
Electricity	125.4	(40.3)	8.1	(27.0)	8.8	(27.9)
Water	174.4	(41.1)	5.5	(5.3)	4.7	(10.4)
Urban transport	94.7	(9.9)	1.9	(2.5)	-0.7	(5.5)
Railways	115.6	(12.5)	4.6	(4.2)	4.9	(13.6)
Ports	168.5	(38.3)	6.3	(13.7)	3.2	(27.3)

Note Indicators are sector-wide means. Standard deviations are shown in brackets. The large standard deviations recorded for indicators in some sectors may reflect the influence of abnormal items or other factors, such as asset revaluations. For example, nine GTEs in the ports sector reported abnormal items of $137 million in 1999-00.

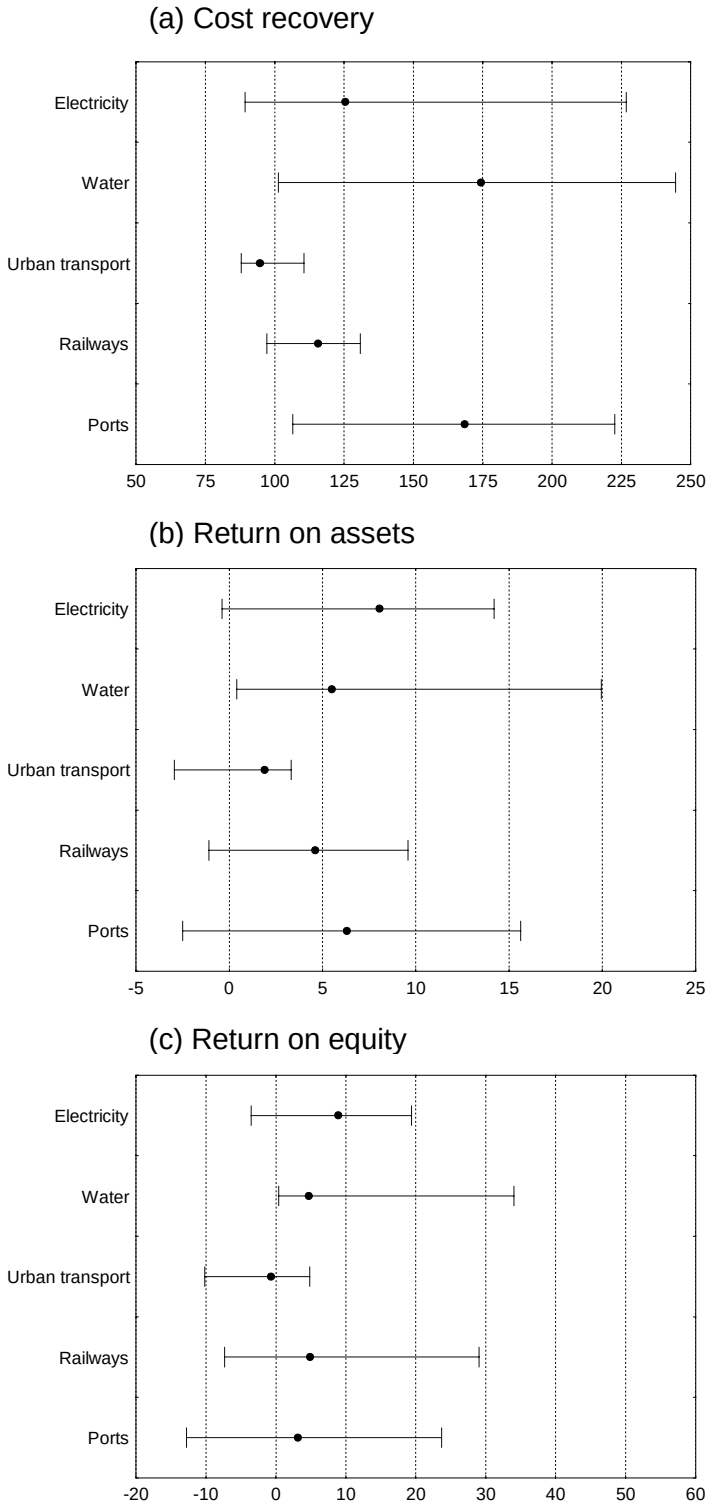
Source: PC estimates.

That said, governments may accept lower rates of return because of benefits that cannot be internalised or there are adverse social implications to pricing above costs. However, if this is the case, and governments are nevertheless requiring GTEs to pursue commercial objectives, CSO payments or funding from government should reflect benefits that cannot be recovered through direct pricing.

On average, profitability performance in 1999-00 improved on most measures in all sectors compared to 1998-99. Nevertheless, there was significant variation around the sector averages suggesting that there were abnormal or other items affecting performance, or that further improvements to profitability by some GTEs are possible.

21 Based on the average daily rate over the 12 months to June 2000. The rate is usually based on the average bond rate over a specified period rather than an 'on the day' rate in order to minimise short-term impacts. However, the averaging period used by regulators varies. For example, IPART (1999a) used the average of the 20 business days prior to a determination. The ACCC (1999) used an average of the rate over 12 months.

Figure 1.5 **Selected profitability measures by sector, 1999-00 (per cent)**



Note The dot represents the mean value and the 'whiskers' represent the range of values for a given performance indicator by sector. For example, in 1999-00 the minimum cost recovery ratio achieved in the electricity sector was 89 per cent, while the maximum value was 227 per cent. The mean cost recovery ratio for the sector was 125 per cent. For reasons of comparability in the ports sector, the return on assets and return on equity for Darwin Port Corporation (-43.4 per cent and -97.7 per cent respectively) were excluded.

GTE performance for 1998-99 and 1999-00 is correlated at the sector level. The degree of correlation differed across indicators. This suggests that performance within each sector was generally consistent between 1998-99 and 1999-00. Cost recovery, which is unaffected by abnormals, had the highest level of correlation across all sectors.

For the urban transport and ports sectors, which displayed less correlation in several indicators over the period, uneven performance may be related to the effect of abnormal items.

There are a number of reasons why GTEs might not generate commercial returns — earnings volatility, prices may be too low, costs may be too high, assets may be overvalued, CSO payments may be inadequate or some combination of these.

Earnings will vary from year to year as a consequence of changes in the market environment and this will contribute to volatility in the returns GTEs earn. However, GTEs like any other business, need to be aware of the dynamics of their market environment.

Inappropriate asset valuation has implications for the ability of GTEs to earn commercial returns. Assets should be valued to reflect current market conditions. If assets are overvalued, GTEs will not appear to earn sufficient returns. Further, inappropriate asset valuation has implications for the efficiency of prices — by compromising their ability to reflect the actual cost of capital and depreciation.

Payments for CSOs might be insufficient to meet the cost of provision. To the extent that GTEs do not receive an adequate financial return on the assets used in delivering CSOs, they could not be expected to meet the cost of their capital.

Financial management

Replicating financial market disciplines provides incentives for GTEs to make better use of debt and equity financing. Debt levels for many GTEs have fallen over the reporting period, suggesting that some GTEs may have relied too heavily on low cost government guaranteed debt financing in the past. Alternatively, low debt levels might suggest insufficient investment in capital stock. Other possible reasons for falling debt levels are debt for equity swaps, debt repayment and debt restructuring.

Many of the monitored GTEs have an interest cover of less than two times. Under some circumstances, they may have to meet financial commitments from sources of funds other than earnings from operations, such as injections of equity capital.

Across sectors there is significant variation in the financial management performance indicators presented in this report (see table 1.7 and figure 1.6). The large variability in these indicators might suggest that the financial restructuring of GTEs is incomplete. For example, some GTEs do not have any debt.

Table 1.7 **Selected financial management performance measures across industries, 1999-00**

	Debt to equity		*Current ratio*		*Interest cover*	
Sector	(per cent)		(per cent)		(times)	
Electricity	71.0	(50.7)	93.7	(52.4)	2.8	(28.3)
Water	20.6	(36.5)	43.8	(78.1)	4.8	(11.8)
Urban transport	43.1	(24.4)	64.0	(34.9)	1.0	(1.4)
Railways	75.5	(269.5)	63.8	(45.6)	1.8	(2.6)
Ports	31.8	(38.9)	100.8	(61.7)	3.3	(10.1)

Note Indicators are sector-wide means. Standard deviations are shown in brackets. The large standard deviations recorded for indicators in some sectors may reflect the influence of abnormal items or other factors, such as asset revaluations. For example, six GTEs in the water sector reported abnormal items of $147 million in 1999-00.

Source: PC estimates.

Effectiveness of financial reforms 1995-96 to 1999-00

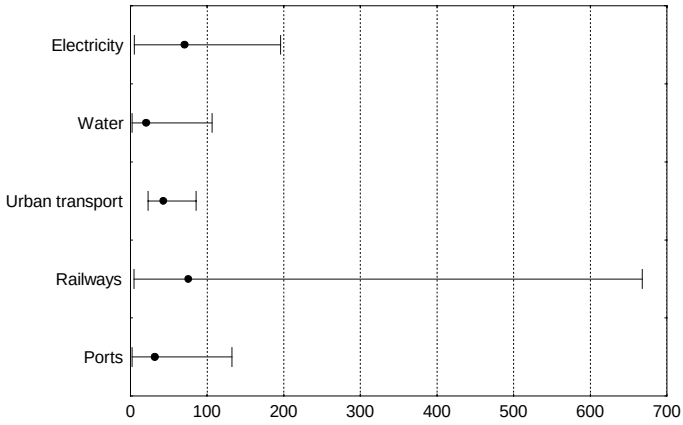
Reforms have generally required GTEs to operate at arms length from government on a commercial basis, subjecting them to factor market disciplines. Over the reporting period, profitability has improved in the railways and water sectors, remained stable in the ports and electricity sectors and declined in the urban transport sector (see table 1.8). This is also true of the average underlying performance if abnormals are excluded.

Over the reporting period, the variability in performance — as measured by the standard deviation — decreased in most sectors among GTEs (see table 1.8). A notable exception is the electricity sector, where the range of performance around the average increased. This may be due in part to adjustments required by some GTEs to compete in the national electricity market.

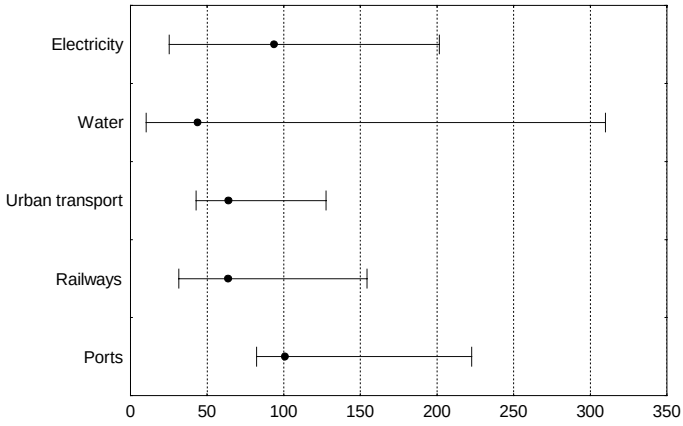
There has been some performance improvement over the reporting period. However, rates of return typically remain low, even if moderate levels of risk are assumed. This outcome is inconsistent with the goal of fully commercialising GTEs, subjecting them to factor market disciplines and ensuring competitive neutrality.

Figure 1.6 **Selected financial management performance by sector, 1999-00**

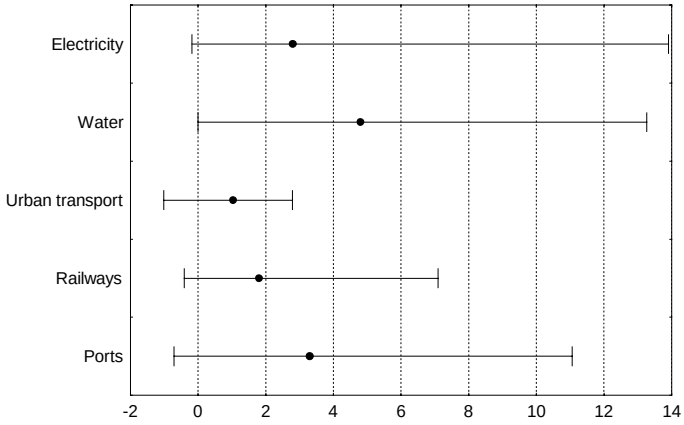
(a) Debt to equity (per cent)



(b) Current ratio (per cent)



(c) Interest cover (times)[a]



Note The dot represents the mean value and the 'whiskers' represent the range of values for a given performance indicator by industry. For example, in 1999-00 the minimum debt to equity ratio achieved in the electricity sector was 6 per cent, while the maximum value was 195 per cent. The mean debt to equity ratio for the sector was 71 per cent. **a** Abnormal items reported by several GTEs in the ports, water and electricity sectors result in a wide range of performance for some indicators. For reasons of comparability, Transend (electricity sector — interest cover 414 times), State Water Projects (water sector — interest cover 4 707 times), Gladstone Port Corporation and Darwin Port Corporation (ports sector — interest cover 37 times and -12.5 times respectively) are excluded.

Table 1.8 **GTE profitability performance including abnormals, 1995-96 and 1999-00[a] (per cent)**

Sector	*Year*	*Cost recovery*		*Return on assets*		*Return on equity*	
Electricity	1999-00	125.4	(40.3)	8.1	(27.0)	8.8	(27.9)
	1995-96	129.9	(49.9)	8.0	(10.9)	6.2	(13.3)
Water	1999-00	174.2	(41.1)	5.5	(5.3)	4.7	(10.4)
	1995-96	150.3	(40.4)	3.6	(4.9)	1.2	(9.1)
Urban transport	1999-00	94.7	(9.9)	1.9	(2.5)	-0.7	(5.5)
	1995-96	98.0	(32.4)	4.1	(6.1)	1.5	(10.5)
Railways	1999-00	115.6	(12.5)	4.6	(4.2)	4.9	(13.6)
	1995-96	96.7	(40.8)	0.0	(8.2)	-3.9	(6.0)
Ports	1999-00	168.5	(38.3)	6.3	(13.7)	3.2	(27.3)
	1995-96	169.3	(77.0)	6.1	(9.7)	3.1	(34.1)

a Excludes GTEs that were monitored in 1995-96 that were subsequently privatised or are no longer monitored by the Commission. Standard deviations are in brackets.

Source: PC estimates.

Commercially focussed businesses can be expected to undertake investments only if they are projected to earn at least the cost of capital faced by the businesses. Other things being equal, this should result in the overall rate of return earned by businesses converging, at least in trend terms, towards their cost of capital. This seems to be happening only slowly, if at all, in large parts of the government-owned utility sector.

This is most likely a manifestation of price reductions that have not been matched by sustained productivity improvements, inadequate CSO payments or over-valued assets.

Inadequate levels of return have implications for both efficiency and income distribution. The most obvious distributional impact is that dividend payments to government (the general community) are lower than they would be if rates of return were commensurate with those earned elsewhere in the economy.

The key issue is that the rate of return needs to be sufficient to maintain efficient levels of service provision in the long-term. If rates of return are too low, either due to regulation or through the incentive framework established in the corporate governance regime, the consequence can be that investment funds will not be allocated to the areas where they are most needed, unless the government intervenes. Given that the asset base of the GTEs monitored in this report grew by

over $4 billion after depreciation and revaluations in 1999-00 and given the importance of the services that they provide, any adverse efficiency consequences could be significant.

A review of the efficacy of existing policies would seem appropriate. In the first instance, pricing regulation, the operating efficiency, the level of CSOs and asset values of some GTEs warrant examination to assess whether current arrangements allow managers to generate appropriate commercial returns. The financial data also raise more fundamental questions about the corporate governance and regulatory frameworks within which the GTEs monitored in this report operate, and the extent to which governments have succeeded in encouraging commercial behaviour and replicating factor market disciplines.

It may be timely to review the objectives which governments have for their GTEs in the various industry sectors and the appropriateness of the current governance and regulatory framework.

2 Electricity

The financial performance of 22 electricity government trading enterprises (GTEs) are covered in this chapter.[1] The GTEs vary significantly in their size and the range of generation, transmission, distribution and retail services they provide. In 1999-00, the electricity GTEs monitored in this report generated $15.3 billion in revenue and controlled assets valued at $41.3 billion.

For a discussion of the data and the financial indicators used and some of the factors that should be considered when assessing performance see chapter 1.

2.1 Sector reforms

Governments have introduced reforms aimed at improving the efficiency and financial performance of electricity GTEs. Information on the nature of these reforms provides context to changes in financial performance.

Sector reforms also have implications for the consistency of performance measures over time as they influence the operating environment and the way that GTEs undertake their business.

The Australian electricity supply industry has undergone significant reform during the 1990s. Historically, the industry developed on a State-by-State basis with dominant government-owned vertically integrated utilities and limited scope for competition. However, over the last decade, the industry has been disaggregated into separate generation, distribution and transmission businesses in most jurisdictions (see table 2.1).

The major driver for structural reform in the electricity industry has been a series of inter-governmental agreements, culminating in the National Competition Policy (NCP) agreements, aimed at establishing a competitive national electricity market.[2]

---

1 This chapter does not cover former GTEs which have been privatised. For example, AlintaGas, which was listed on the Australian Stock Exchange on 17 December 2000 is not included. Nor does it provide any information on the Power and Water Authority (Northern Territory) as detailed disaggregated information on its electricity and water businesses was unavailable.

2 In July 1991, governments agreed to work cooperatively to improve competitiveness in the electricity industry and the National Grid Council was established. In June 1993, six

The intention behind structural change within the electricity supply industry has been to introduce competition in the generation and retail sectors by separating these contestable elements from the natural monopoly elements of transmission and distribution.[3] Of the jurisdictions monitored, only Western Australia is not party to the NCP agreements on electricity.

In NSW, Pacific Power was restructured into a transmission network and three generators. On 1 February 1995, its transmission activities were transferred to TransGrid and six of Pacific Power's power stations were transferred to two new generators — Delta Electricity and Macquarie Generation. In October 1995, the existing 25 electricity distributors were amalgamated to form six new distribution businesses, with each responsible for the distribution of electricity within a franchise area.

In Queensland, AUSTA Electric was horizontally separated into three competing government-owned generators — CS Energy, Stanwell Corporation and Tarong Energy — which commenced operating on 1 July 1997. At the same time, the Queensland Transmission and Supply Corporation's (QTSC) eight subsidiaries — seven regional distributors and the Queensland Electricity Transmission Corporation trading as Powerlink — were established as independent government-owned corporations.

governments (Commonwealth, NSW, Victoria, Queensland, South Australia and the ACT) committed to undertake reforms necessary to allow a competitive electricity market to commence from July 1995. At the April 1995 Council of Australian Governments meeting, these reforms were extended and brought within the NCP process.

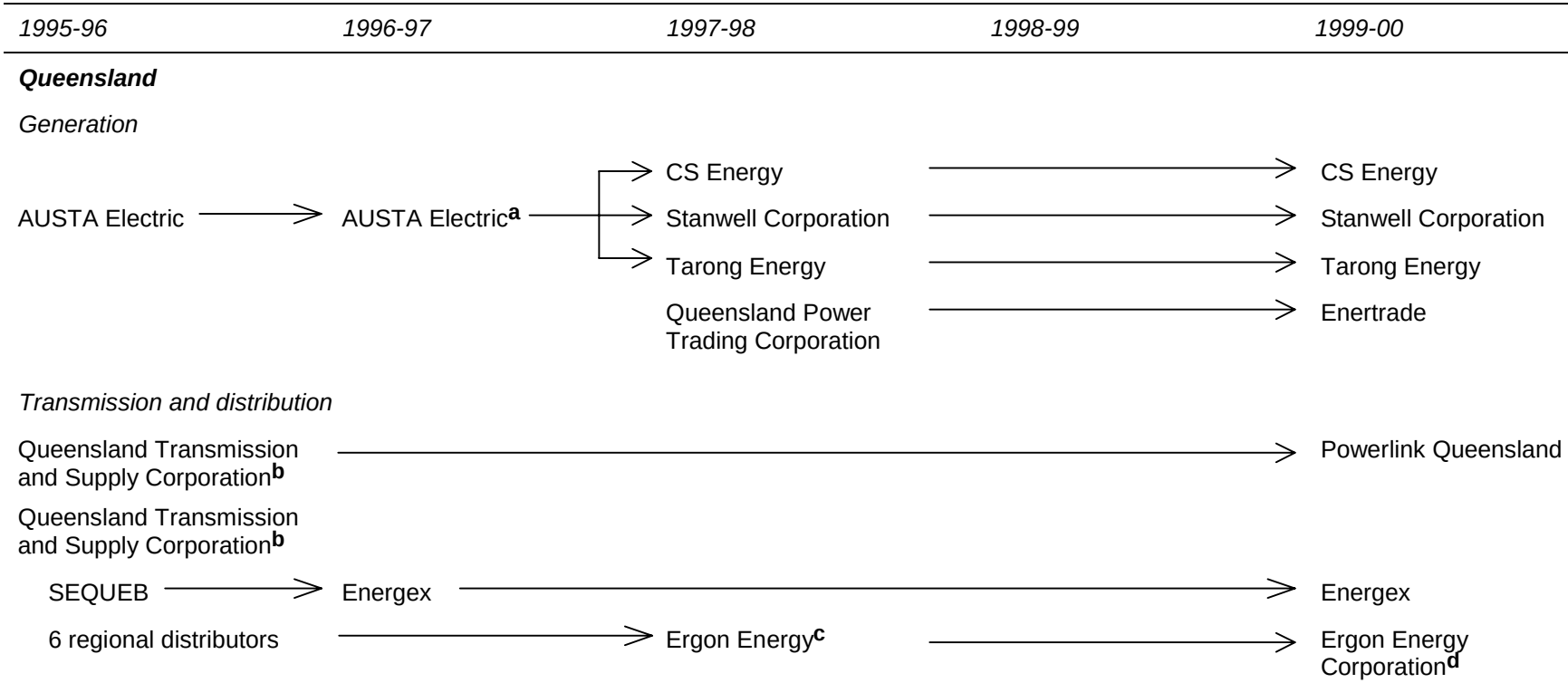
3 An industry is considered to be a natural monopoly if total costs of production are lower when a single firm produces the entire industry output, than when two or more firms divide the total among themselves. It is generally accepted that electricity transmission and distribution networks exhibit some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

Table 2.1 **Monitored electricity GTEs, 1995-96 to 1999-00**

1995-96	*1996-97*	*1997-98*	*1998-99*	*1999-00*
New South Wales				
Generation				
Pacific Power	→	→	→	Pacific Power
Delta Electricity	→	→	→	Delta Electricity
Macquarie Generation	→	→	→	Macquarie Generation
Transmission and System Operation				
TransGrid	→	→	→	TransGrid
Distribution				
EnergyAustralia	→	→	→	EnergyAustralia
NorthPower	→	→	→	NorthPower
Advance Energy	→	→	→	Advance Energy
Australian Inland Energy	→	→	→	Australian Inland Energy
Great Southern Energy	→	→	→	Great Southern Energy
Integral Energy	→	→	→	Integral Energy

(Continued next page)

Table 2.1 (continued) **Monitored electricity GTEs, 1995-96 to 1999-00**



a On 1 July 1997, AUSTA Electric was separated into three government-owned generation corporations. Originally, the Queensland Power and Trading Corporation (QPTC) was established on a temporary basis to assist in the transition to a new industry structure, by finalising a range of financial and administrative matters arising from the restructure of the former Queensland Transmission and Supply Corporation. Subsequently, the QPTC began trading electricity generated from several privately-owned power stations. **b** The Queensland Transmission and Supply Corporation (QTSC) commenced operations on 1 January 1995 as a holding company for eight subsidiary corporations — seven regional distribution corporations, one of which was SEQEB and Powerlink Queensland, which manages Queensland's high voltage transmission system. On 1 July 1997, QTSC's subsidiaries were established as independent government owned-corporations. **c** Ergon Energy Pty Ltd was established following a merger between the Northern Electricity Retail Corporation and Central Electricity Retail Corporation. Ergon Energy Pty Ltd remained under the ownership of regional distributors. **d** Ergon Energy Corporation was formed following the amalgamation of the six regional distributors and Ergon Energy Pty Ltd.

(Continued next page)

Table 2.1 (continued) **Monitored electricity GTEs, 1995-96 to 1999-00**

1995-96	*1996-97*	*1997-98*	*1998-99*	*1999-00*
Western Australia				
Western Power	→	→	→	Western Power
Tasmania				
Hydro-Electric Corporation	→	Hydro-Electric Corporation[e]	→	Hydro-Electric Corporation
			→	Transend Networks
			→	Aurora Energy
Commonwealth				
Snowy Mountains Hydro-Electric Authority	→	→	→	Snowy Mountains Hydro-Electric Authority

e On 1 July 1997, the Hydro-Electric Corporation (HEC) was separated into three businesses. The HEC continues to be responsible for generation, Transend Networks owns and operates Tasmania's transmission network and Aurora Energy is responsible for distribution.

Three new retail corporations were established and two of these merged to form Ergon Energy Pty Ltd.[4] Ergon Energy Pty Ltd was owned by six of the regional distribution corporations. Ergon Energy Pty Ltd is now a wholly-owned subsidiary of the Ergon Energy Corporation following the amalgamation of the six regional distributors on 30 June 1999.

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 originally established as a transitional body, the QPTC gained permanent status as Queensland's fourth generator in June 1999. In July 1999, the QPTC was renamed Enertrade.

In Western Australia, the State Energy Commission of Western Australia (SECWA) was separated in 1994-95 into electricity (Western Power) and gas (AlintaGas) businesses.[5] In Tasmania, the Hydro-Electric Corporation was restructured into three businesses on 1 July 1998. The Hydro-Electric Corporation retained responsibility for generation, the transmission network was transferred to Transend Networks and the retailing and distribution functions were transferred to Aurora Energy.

2.2 Market environment

The market environment that GTEs operate in has an impact on their performance. One of the most significant changes to the market environment of electricity GTEs over the reporting period has been the continued development of the National Electricity Market (NEM).

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

5 On 16 December 2000, legislation passed by the Western Australian parliament, enabled the sale of AlintaGas. On 17 October 2000, AlintaGas was publicly listed on the Australian Stock Exchange.

The NEM is a wholesale market for the supply and purchase of electricity combined with an access regime for transmission and distribution networks in NSW, Victoria, South Australia and the Australian Capital Territory. The Queensland wholesale electricity market commenced operating on 18 January 1998 based on the NEM.[6]

The National Electricity Market Management Company (NEMMCO) was established in May 1996 to manage the NEM in accordance with the National Electricity Code (the Code). The Code specifies the market arrangements that govern the operation of the wholesale spot market, such as system security requirements, rules for bids and dispatch of generating capacity and metering standards. The NEM officially commenced operating in December 1998, although trade between the NSW and Victorian wholesale markets commenced in May 1997.

As part of the development of the NEM, governments have progressively introduced choice of electricity supplier, starting with the largest users of electricity (see table 2.2). Moves to further increase competition in several jurisdictions are currently being considered. For example, the Queensland government is reassessing the introduction of retail competition for all consumers, originally scheduled for implementation in January 2001.

The development of the NEM has a number of implications for the environment in which electricity GTEs operate. Most electricity GTEs now face greater competition than they have in the past — through trade between wholesale electricity markets and the introduction of supplier choice in retail markets. There is also increased scope for competition with most jurisdictions adopting the access provisions of the Code for their distribution and transmission networks. These provisions give third parties a right of access to these networks, facilitating their entry into the market.

6 The Queensland market was physically connected to the NEM via the unregulated 180MW 'Directlink' in February 2000 and the Queensland-New South Wales Interconnector (currently 450MW) in February 2001. There are also proposals to build another link between NSW and South Australia and an underwater link between Tasmania and Victoria.

Table 2.2 **Timetable for retail competition, by jurisdiction**

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

Note In Victoria, customers with annual energy use of greater than 220 GWh were given choice from 1 December 1994 and customers consuming greater than 44 GWh were given choice from 1 July 1995. In Western Australia, customers in off-grid regional locations consuming greater than 300 MWh have been able to choose their supplier since July 1999. 1 000 KWh = 1 MWh, 1 000 MWh = 1 GWh.

Source: GSE 2001.

With the introduction of the NEM and its market rules, electricity GTEs and NEMMCO have had to come to terms with operating effectively in this new environment. There have been increases to the wholesale electricity prices and significant price volatility in some parts of the NEM. For example, the average monthly spot price in NSW in the six months to June 2000 was around $33 MWh compared to $25 MWh over the same period in 1999. However, during 1999-00, the maximum monthly prices recorded in NSW ranged between $19 MWh and $76 MWh (NEMMCO 2001).

Volatility in wholesale electricity prices has resulted in greater exposure to risk for both generators and retailers. Consequently, trade in electricity derivatives has developed as a means of managing the financial risks associated with trading in wholesale markets. For example, electricity futures contracts based on wholesale market prices in the NSW and Victorian regions of the NEM are traded on the Sydney Futures Exchange.

Although Western Australia is not party to the NEM, it has introduced choice in electricity supplier for large users of electricity under its commitments to NCP. In addition, the *Electricity Corporation Act 1994* provides for third party access to Western Power's electricity transmission network. Consequently, Western Power now faces the prospect of greater competition than it has in the past.

Most of the monitored electricity GTEs continue to operate under some form of price regulation. For example, in NSW, the Independent Pricing and Review Tribunal (IPART) regulates distribution and electricity prices for franchise customers. Prices to contestable customers are unregulated. IPART was also responsible for regulating the transmission network until July 1999, when this responsibility was transferred to the Australian Competition and Consumer Commission (ACCC).

In Queensland, pricing policy for franchise customers is set by the Treasurer, in his role as the Minister for Energy. He is responsible for regulating the prices charged for use of the transmission network, until ACCC takes on this responsibility in January 2002. In Tasmania, an independent electricity regulator is responsible for regulating electricity prices.

On 8 December 2000, the federal parliament passed legislation supporting the implementation of a 2 per cent renewable energy target to increase the contribution of renewable energy sources in Australia.[7] Most electricity generation GTEs are

7 From 1 April 2001, energy wholesalers will have to purchase increasing amounts of electricity generated from renewable sources.

pursuing investment opportunities including cogeneration, wind and solar power to meet this target and also satisfy demand from consumers for 'green' energy. For example, Pacific Power constructed a 10 MW wind farm during 1999-00.

2.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings. For a more detailed discussion of profitability indicators see chapter 1.

Profitability will be influenced by a number of factors including prices, business volumes and expenses. Other factors such as changes in asset values will also influence measures of profitability through the impact of abnormals and changes in depreciation expense.

Most of the electricity GTEs monitored use current asset valuation methods, although the actual method used varies between GTEs. Asset values have fallen over the reporting period for some GTEs following asset write-downs. For example, Great Southern Energy has written-down assets each year since 1995-96. In other cases, asset revaluations have resulted in an increase in the value of assets. For example, Aurora Energy revalued its assets upwards in both 1998-99 and 1999-00.

Pacific Power's and the Hydro-Electric Corporation's asset values fell significantly in 1995-96 and 1998-99 — following the transfer of assets to newly formed GTEs as part of an industry restructure.

The treatment of contributed assets can have a material effect on financial performance and asset and liability recognition. Where contributed assets are an issue, most GTEs indicate that they are now following Urgent Issue Group (UIG) Consensus Views — Abstract 11, *Accounting for contributions of, or contributions for the acquisition of, non-current assets* and Abstract 17, *Developer and customer contributions in price regulated industries* — to recognise contributed assets.[8]

The Productivity Commission's treatment of contributed assets has changed over the reporting period (see chapter 1). Therefore, it should be noted that the impact of these assets on profitability ratios such as return on assets has changed after 1997-98.

Operating profit before tax (including abnormals) varied over the reporting period. This variability not only reflects the influence of abnormals but the impact of the

8 The Australian Accounting Research Foundation issues UIG Consensus Views as Abstracts to assist in the interpretation of an existing accounting standard or guidance in the absence of one.

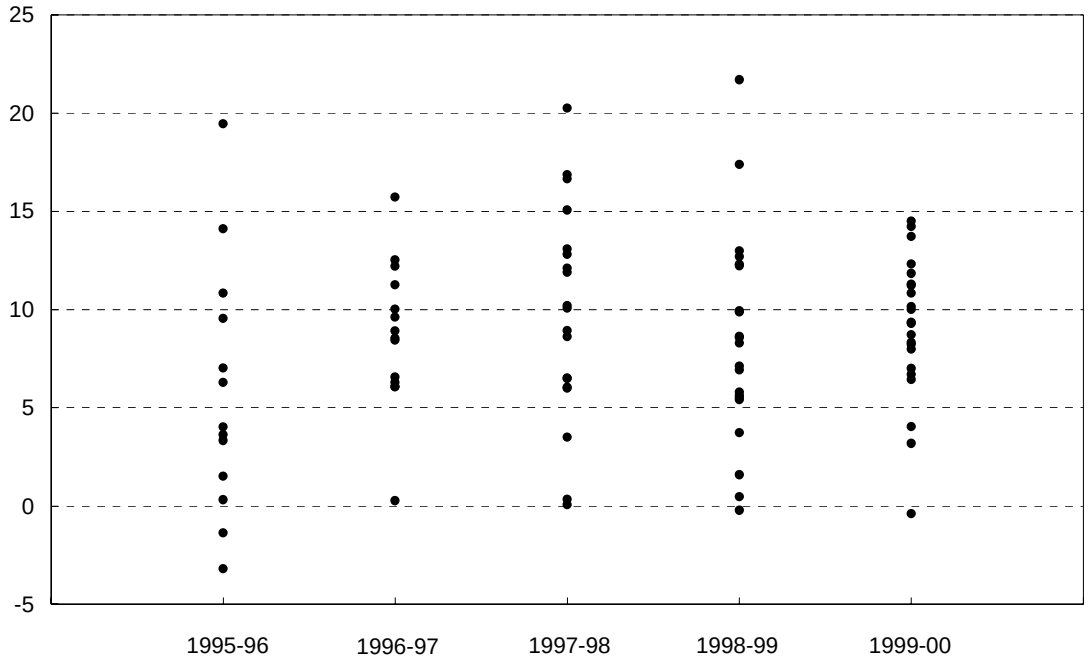
continuing development of the NEM as GTEs came to terms with operating in a new market environment.

Most of the electricity GTEs made operating profits over the reporting period. However, some incurred operating losses in their first year of operation.

The Snowy Mountains Hydro-Electric Authority (SMHEA) made an operating loss in each year of the reporting period. This largely reflects the way the Authority is funded and the impact of an asset revaluation in 1991.[1]

The rate of return on assets in the electricity sector varies considerably between GTEs, although the range of performance was narrower in 1996-97 and 1999-00 (see figure 2.1).

Figure 2.1 **Return on assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the return on assets ratio for a GTE in that financial year. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue (including abnormals) and adding back gross interest expense. Average total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period). In 1995-96, Australian Inland Energy had a return on assets of -25.2 per cent.

1 The SMHEA receives funding based on its net cost of production. Under its enabling legislation, additional depreciation charges resulting from the asset revaluation are not taken into account when determining the net cost of production.

While the average return on assets for electricity GTEs has remained constant at around 7 per cent over the reporting period, the performance of individual GTEs is quite diverse. GTEs with a stable rate of return include Transgrid and Western Power, which returned about 10 per cent on assets over the reporting period. Others, such as the Hydro-Electric Commission had a downward trend. Others were quite unstable. For example, asset revaluations and variable operating profit resulted in Northpower's return on assets fluctuating between 15 per cent in 1997-98 and 9 per cent in 1999-00.

The variability in profitability is reflected in the return on equity ratio. Most of the monitored electricity GTEs have had unstable return on equity ratios over the reporting period. In 1999-00, more than half were below 7 per cent. Two had return on equity ratios of over 20 per cent.

This contrasts to an alternative risk free investment in 10 year Commonwealth Government bonds that returned 6.6 per cent (June 2000). Taking into account the risks in the electricity sector, estimates of the weighted average cost of capital for electricity and gas distribution businesses, by IPART, the NSW Treasury and others (see IPART 1998), suggest that a nominal pre-tax return of 8.5 per cent would be sufficient to meet the cost of capital.

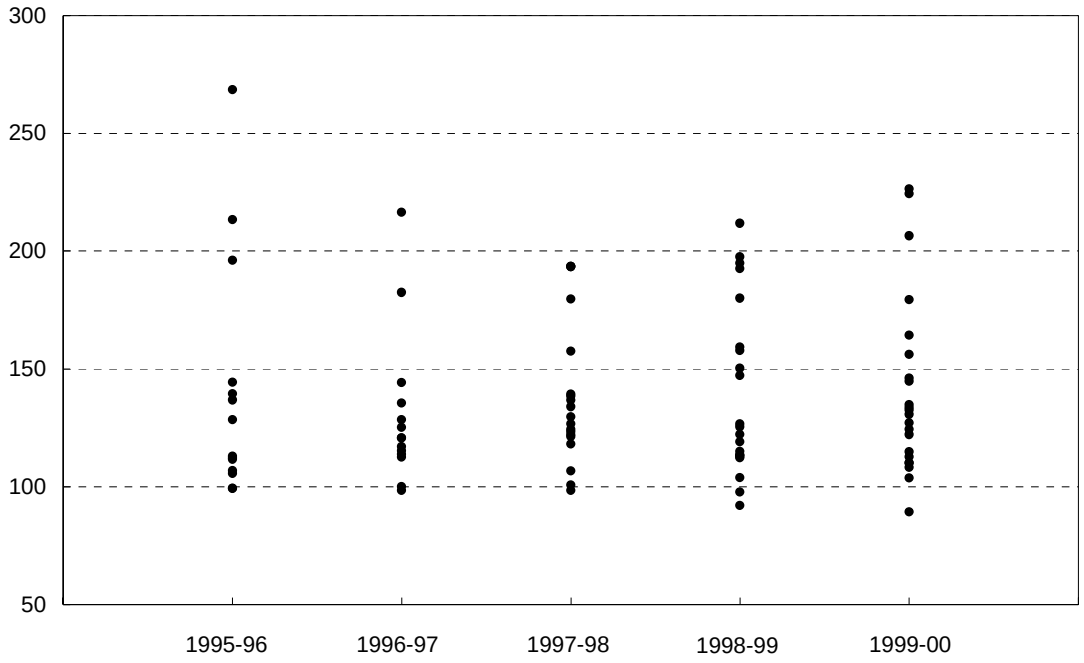
The cost recovery ratio measures the ability of a GTE to generate adequate revenue to meet expenses. A cost recovery ratio below 100 per cent suggests that a GTE is unable to meet its operating costs even before the cost of servicing debt is taken into account.

Over the reporting period, most electricity GTEs have recovered between 100 and 150 per cent of operating costs (see figure 2.2). However, the SMHEA generated a cost recovery ratio of just under 100 per cent each year, falling to below 90 per cent in 1999-00. Pacific Power's cost recovery ratio fell below 100 per cent for the first time in 1998-99 before recovering to 140 per cent in 1999-00.

The highest rates of cost recovery in 1999-00 were recorded by electricity distributors TransGrid, Powerlink and Transend — all recording cost recovery ratios of over 200 per cent.

Profitability, as measured by operating profit before tax (including abnormals), return on assets, return on equity and cost recovery has varied both between GTEs and over the reporting period. For example, in 1999-00, the SMHEA had a return on equity of -3.5 per cent and Delta Electricity had a return on equity of 16.1 per cent. The variability reflects the impact of abnormals largely arising from continued reform, the new market environment and increasing competition.

Figure 2.2 **Cost recovery, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting abnormal revenue, investment income and receipts from governments to cover deficits on operations from total revenue. Expenses from operations are calculated by subtracting abnormal expenses and gross interest expense from total expenses.

2.4 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. For a more detailed discussion of financial management indicators see chapter 1.

As a part of the reform process, governments typically imposed financial restructuring on their electricity GTEs. This has involved the transfer of both assets and liabilities to State and Territory governments, and the withdrawal of equity. Financial restructuring is usually justified on the grounds of establishing more appropriate capital structures for GTEs following the reform process.

Financial restructuring makes it difficult to undertake comparisons of financial performance over time. In Queensland, for example, Powerlink was required by its shareholding Ministers to make interest free loans (valued at $249 million) to the State in 1997-98, as part of a capital restructure. This resulted in a 90 per cent

increase in debt. In 1998-99, the capital restructure was completed with a corresponding reduction in share capital and hence equity. This resulted in an increase in the debt to equity, debt to total assets and total liabilities to equity ratios in 1998-99.

The level of debt carried by most electricity GTEs has fallen or remained relatively constant over the reporting period. A number of electricity GTEs have reduced their debt levels through financial restructuring, which has allowed them to reduce repayment periods and to negotiate improved interest terms. Debt levels have also fallen following the transfer of assets and liabilities to new entities as part of industry restructuring.

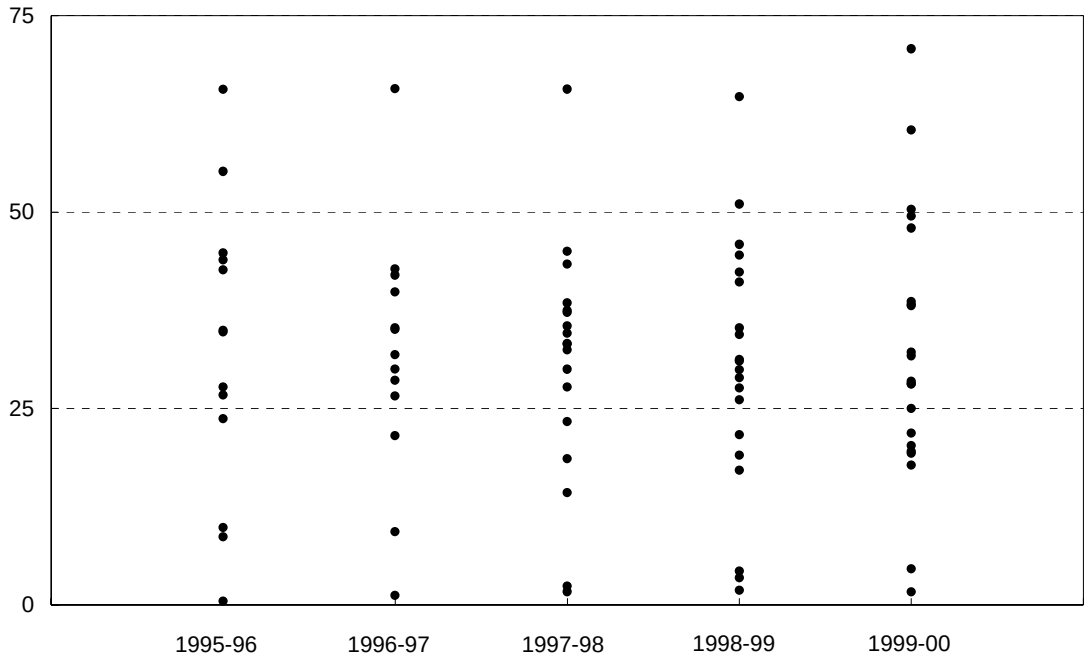
Stanwell reduced debt levels by $268 million (42 per cent) between 1997-98 and 1999-00. This resulted in a reduction in interest expense of 40 per cent. In 1997-98, interest expense accounted for 19 per cent of total expenses — by 1999-00 this had fallen to 11 per cent.

In some cases, debt levels have increased over the reporting period as the result of financial restructuring by shareholder governments. For example, Energex was directed to make interest free loans (valued at $300 million) as part of a capital restructure to the Queensland Government in 1997-98. These were financed through an increase in Energex's long-term debt.

Falling debt levels have resulted in lower debt to total asset and debt to equity ratios for a number of GTEs. Some electricity GTEs hold low levels of debt and this is reflected in relatively low ratios. Most of the electricity GTEs have debt to total asset ratios within 20 to 50 per cent (see figure 2.3). This indicates that, in most cases, at least 50 per cent of assets are now represented by equity finance.

In 1999-00, more than half of the electricity GTEs had an interest cover of over 3 times, suggesting that they are comfortably able to meet periodic interest payments. Some GTEs, such Tarong Energy, have significantly improved their interest cover over the period by retiring and restructuring some of their debt holdings.

Figure 2.3 **Debt to total assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the debt to total assets ratio for a GTE in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowing and finance leases. Total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period). Australian Inland Energy does not hold any debt. Therefore the debt to total assets ratio cannot be calculated.

2.5 Financial transactions

As part of the reform process, governments have sought to give GTEs a greater commercial focus and facilitate 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 1.

The introduction of income tax-equivalent regimes, requirements to pay dividends and debt guarantee fees are examples of how governments have imposed the principles of competitive neutrality on their electricity GTEs. Governments have also moved towards clearly defining, costing and explicitly financing community service obligations (CSOs).

Over the reporting period, an increasing number of electricity GTEs have been required to make tax-equivalent and dividend payments. Most now make such payments. The exception is the SMHEA which operates on a cost recovery basis and is not required to make dividend or tax-equivalent payments.

Prior to 1999-00, tax-equivalent payments were based on a company tax rate of 36 per cent. The adoption of tax-effect accounting means that the income tax-equivalent expense for any year may differ from the actual amount of tax paid to the State and Territory governments for that year, because of permanent and timing differences. Changes in the company tax rate introduced by the Commonwealth Government in December 1999 led to the restatement of deferred tax liabilities in 1999-00.[10] As a result of this adjustment, tax-equivalent payments by electricity GTEs in 1999-00 were reduced by $240 million (36 per cent).

Dividend payments represent a return on shareholder funds and their size reflects financial performance. There has been significant variation in the level of dividends paid or provided for by GTEs over the reporting period, reflecting annual variations in profitability.

A number of GTEs have been required to make special dividend payments which are unrelated to the current year's performance. For example, Pacific Power made a dividend payment in 1998-99 despite making a loss. This special dividend arose out of an agreement with the NSW Government whereby Pacific Power receives a fee to offset costs associated with managing transitional issues related to the restructure of the generation sector. Pacific Power is required to make a dividend payment equivalent to this fee.

As part of the reform process, governments have also moved to identify, cost and fund CSOs provided by electricity GTEs. Several of the electricity GTEs received CSO funding over the reporting period. Generally, retailers meet these obligations although there are some examples of CSOs being placed on generators. CSO funding has been received for the provision of rebates, concessions, the uneconomic supply of electricity to some customers and electrical inspections.

The total level of CSO payments to electricity GTEs has increased over the reporting period, reflecting an increase in the funding received and the increasing number of GTEs receiving CSO funding.

10 The company tax rate will fall to 34 per cent for 2000-01 and then to 30 per cent from 2001-02.

2.6 GTE performance reports

Delta Electricity (NSW)
Macquarie Generation (NSW)
Pacific Power (NSW)
TransGrid (NSW)
Advance Energy (NSW)
Australian Inland Energy (NSW)
EnergyAustralia (NSW)
Great Southern Energy (NSW)
Integral Energy (NSW)
NorthPower (NSW)
CS Energy (QLD)
Stanwell Corporation (QLD)
Tarong Energy (QLD)
Queensland Power Trading Corporation (QLD)
Powerlink (QLD)
Ergon Energy (QLD)
Energex (QLD)
Western Power (WA)
Hydro-Electric Corporation (Tas)
Aurora Energy (Tas)
Transend Networks (Tas)
Snowy Mountains Hydro-Electric Authority (C'wealth)

DELTA ELECTRICITY — New South Wales

Following a restructure of the NSW electricity industry, Delta Electricity commenced operations as a generator in March 1996. Delta Electricity operates under the *Energy Services Corporations Act 1995* and the *State Owned Corporations Act 1989*.

Delta Electricity operates mainly in the wholesale electricity market selling to energy retailers and a few large industrial customers. Delta operates four power stations with a combined generating capacity of 4 240 MW.

Record winter demands for electricity and an increase of 17 per cent in average prices contributed to strong growth in revenue in 1999-00. The improvement in profit in 1999-00 included an abnormal gain of $25.7 million related to asset surpluses in superannuation funds.

Delta Electricity has reduced the level of borrowings by over 50 per cent ($312 million) over the reporting period. This is reflected in consistently falling debt to equity and debt to total asset ratios.

Delta Electricity is required to make tax-equivalent and dividend payments. Income tax-equivalent payments in 1999-00 were reduced by $18.4 million as a result of a reduction in the future company tax rate.

In 1997-98, Delta Electricity received $5.4 million in community service obligation (CSO) income from the NSW Government for subsidised sales contracts assigned to Delta Electricity on its establishment. Delta Electricity has received no other CSO income over the reporting period.

DELTA ELECTRICITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*	*1998-99*	*1999-00*[c]
Size						
Total assets	$M	1 481	1 495	1 337	1 361	1 492
Total revenue	$M	220	701	573	574	674
Profitability						
Operating profit before tax (includes abnormals)	$'000	29 339	131 232	54 636	60 684	158 671
Operating sales margin	%	22.1	25.3	15.3	16.0	28.0
Cost recovery	%	128.4	100.0	118.1	119.0	133.6
Return on assets	%	3.3	12.5	6.5	6.9	13.5
Return on equity	%	2.8	3.1	4.5	5.3	16.1
Financial management						
Debt to equity	%	98.2	73.4	58.8	57.8	46.2
Debt to total assets	%	44.8	35.1	30.0	31.2	24.6
Total liabilities to equity	%	119.2	110.2	85.2	87.0	96.1
Interest cover	times	2.5	3.4	2.5	2.9	5.7
Current ratio	%	279.3	81.5	117.5	96.4	134.3
Leverage ratio	%	219.2	210.2	185.2	187.0	196.1
Payments to and from government						
Dividends	$'000	14 376	180 150	21 402	32 695	86 653
Dividend to equity ratio	%	2.1	26.0	3.0	4.5	11.6
Dividend payout ratio	%	76.6	849.6	67.1	85.0	72.4
Income tax expense	$'000	10 562	110 029	22 733	22 218	38 966[d]
CSO funding	$'000	0	0	5 400[e]	0	0

a Delta Electricity commenced operations as an electricity generator in March 1996. Hence, the data for the 1995-96 financial year relates only to operations between March and June 1996. In December 1995, the NSW wholesale electricity market commenced operating. **b** A number of the ratios reflect the impact of three cross border lease transactions relating to the Mt Piper Power Station, whereby the facility was leased to the State of NSW and sub-leased back to Delta Electricity. **c** Includes an abnormal gain of $25.7 million related to asset surpluses in superannuation funds. **d** A fall in the future company tax rate reduced tax equivalent payments by $18.4 million. **e** Delta Electricity received $5.4 million in community service obligation funding for subsidised sales contracts assigned on its establishment.

MACQUARIE GENERATION — New South Wales

Macquarie Generation was established as a government-owned corporation in March 1996 following a restructure of the NSW electricity industry. It operates two coal-fired power stations and generates electricity for sale into the National Electricity Market (NEM). The power stations have a combined generating capacity of 4 640 MW.

Macquarie Generation's first full year of operation was 1996-97. The phased introduction of contestability in the NSW retail market and the progression of the NEM to allow trading between the NSW and Victorian wholesale pools contributed to lower wholesale electricity prices after 1997.[1] Falling wholesale prices contributed to reduced total revenue and operating profit in 1997-98. However, since then average pool prices have almost doubled, leading to increases in revenue in 1998-99 and 1999-00.

The fall in operating profit (before tax, including abnormals) in 1999-00, notwithstanding higher revenues, reflects the inclusion of several abnormal items. Abnormal revenue of $18.8 million was reported as a result of investment returns on externally managed superannuation funds. However, this was offset by an abnormal loss of $53.2 million due to the termination of a long-term contract with a coal supplier.[2]

Debt restructuring has allowed Macquarie Generation to reduce its debt levels and the cost of financing that debt. Consequently, there has been a steady decrease in the debt to equity and leverage ratios.

Macquarie Generation 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 in consultation with the board of directors. Macquarie Generation also paid a debt guarantee fee of $14.1 million in 1999-00.

The NSW Government provides Macquarie Generation with funding for the provision of community service obligations. Macquarie Generation has been reimbursed for the full cost of providing rebates and subsidies to certain customers in line with NSW Government policy decisions.[3]

---

1 As a part of the development of the NEM, retail competition has been introduced in stages. The first stage involved giving choice of retail supplier to only the largest consumers of electricity (from October 1996).

2 Macquarie Generation's termination of the supply contract allows it to purchase market-priced coal. Macquarie Generation estimates it will make annual savings of $25 million for 10 years.

3 Community service obligations (and funding) ceased on 5 December 1999.

MACQUARIE GENERATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*	*1998-99*	*1999-00*[b]
Size						
Total assets	$M	2 518	2 260	2 199	2 138	2 158
Total revenue	$M	311	866	696	719	733
Profitability						
Operating profit before tax, (includes abnormals)	$'000	50 550	173 817	53 518	70 141	65 134
Operating sales margin	%	28.9	30.9	19.2	21.3	19.2
Cost recovery	%	139.5	144.2	123.3	126.5	132.5
Return on assets	%	3.6	11.3	6.0	7.1	6.7
Return on equity	%	3.5	12.0	3.7	4.7	6.3
Financial management						
Debt to equity	%	149.5	108.4	107.3	98.6	86.9
Debt to total assets	%	55.2	42.0	45.0	42.4	38.0
Total liabilities to equity	%	171.1	144.4	135.3	129.6	129.5
Interest cover	times	2.2	2.8	1.7	1.8	1.8
Current ratio	%	100.9	43.8	73.4	44.4	81.3
Leverage ratio	%	271.1	244.4	235.3	229.6	229.5
Payments to and from government						
Dividends	$'000	24 770	125 000	35 000	40 000	50 000
Dividend to equity ratio	%	2.7	13.5	3.8	4.3	5.3
Dividend payout ratio	%	76.6	112.4	100.9	91.6	84.4
Income tax expense	$'000	18 198	62 591	18 840	26 468	5 918[c]
CSO funding	$'000	2 447	2 891	20 336	18 153	7 854[d]

a Macquarie Generation commenced operations on 1 March 1996. Data relates only to the four months to June 1996. **b** Abnormal revenue reported related to investment returns on externally managed superannuation funds of $18.8 million. This was offset by an abnormal loss of $53.2 million due to the termination of a long-term coal supply contract. **c** The fall in income tax-equivalent payments reflects a $17.6 million downward adjustment due to a reduction in the future company tax rate. **d** Community service obligations (and funding) ceased on 5 December 1999.

PACIFIC POWER — New South Wales

Pacific Power's primary business is generating electricity for sale into the National Electricity Market (NEM). It is made up of four interrelated businesses — a domestic and international coal business, a thermal power station, an engineering services business and a business developing alternative sources of energy.

In moving towards the NEM, the NSW Government established a wholesale electricity market for the state. As part of this process, Pacific Power's transmission network was transferred to the newly formed TransGrid in 1994-95. In 1995-96, six power stations were transferred to Delta Electricity and Macquarie Generation.[1]

The introduction of competition through the NSW wholesale electricity market and the NEM has had a significant impact on Pacific Power's financial performance. Difficult market conditions characterised by excess generating capacity in NSW and an inflow of relatively cheaper electricity from Victorian generators, contributed to deteriorating financial performance in 1997-98 and 1998-99.

Improved performance in 1999-00 was the result of an increase in revenue from electricity sales and engineering services. Profit (before tax, including abnormals) was also lifted by a 5 per cent reduction in total expenses. Included in the improved profit result for 1999-00 were net abnormal expenses of $49.8 million.[2]

Pacific Power has reduced debt levels by $115 million since 1997-98. This has led to improvements in the debt to equity and debt to total assets ratios.

Pacific Power is required to make tax-equivalent and dividend payments. Despite making an operating loss in 1998-99, Pacific Power was required to make a special dividend payment. This payment was made under an agreement, with the NSW Government, where Pacific Power received a fee to offset any costs associated with managing transitional issues related to the restructure of generation in 1996. Under the agreement Pacific Power is required to make a special dividend payment equivalent to this fee.[3]

---

1 In July 2000, Eraring Energy was established under the *State Owned Corporations Act 1989*. On 2 August 2000, there was a transfer of generation assets from Pacific Power to Eraring Energy.

2 Abnormal expenses related to Powercor prior year loss and legal expenses ($49.4 million), insurance provision for asbestos claims ($40.4 million), write-down of leasehold improvements ($0.9 million), year 2000 costs ($3.4 million) and recognition of deferred hedge losses ($2.2 million). Abnormal revenue related to overfunded superannuation ($128.8 million), legal settlement ($11.2 million) and inter-pool settlement surpluses ($6.6 million).

3 Pacific Power has not paid a dividend based on operating profit since 1996-97.

PACIFIC POWER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*	*1998-99*	*1999-00*[c]
Size						
Total assets	$M	2 609	2 139	2 148	2 125	2 238
Total revenue	$M	2 369	937	785	865	1 005
Profitability						
Operating profit before tax (includes abnormals)	$'000	521 756	152 376	25 767	-39 274	149 603
Operating sales margin	%	30.8	22.5	9.0	0.9	21.3
Cost recovery	%	144.3	128.4	106.7	97.7	140.2
Return on assets	%	14.1	9.6	3.5	0.5	9.9
Return on equity	%	13.2	8.4	0.9	-2.0	13.0
Financial management						
Debt to equity	%	59.2	65.5	69.7	67.0	56.7
Debt to total assets	%	9.9	28.6	33.3	31.0	27.4
Total liabilities to equity	%	192.7	106.6	110.0	115.0	112.3
Interest cover	times	3.2	3.0	1.5	0.2	3.3
Current ratio	%	77.2	66.7	90.0	72.2	115.6
Leverage ratio	%	292.7	206.6	210.0	215.0	212.3
Payments to and from government						
Dividends[d]	$'000	315 675	219 937	21 982	27 660	31 573
Dividend to equity ratio	%	12.9	22.8	2.1	2.8	3.1
Dividend payout ratio	%	97.1	271.7	232.1	-138.0	23.8
Income tax expense	$'000	196 615	71 422	16 298	-19 230	16 746
CSO funding	$'000	0	0	0	0	0

a Pacific Power transferred assets ($4.5 billion) and liabilities ($2.2 billion) associated with six power stations to Delta Electricity and Macquarie Generation. **b** Includes abnormal revenue of $399 million associated with a reduction in the provision for employee accrued entitlements which were assumed by the Crown. **c** Abnormal expenses related to Powercor prior year loss and legal expenses ($49.4 million), insurance provision for asbestos claims ($40.4 million), write-down of leasehold improvements ($0.9 million), year 2000 costs ($3.4 million) and recognition of deferred hedge losses ($2.2 million). Abnormal revenue related to overfunded superannuation ($128.8 million), legal settlement ($11.2 million) and inter-pool settlement surpluses ($6.6 million). Operating power stations were revalued on 30 June prior to transfer to Eraring Energy. The revaluation resulted in a fall in the value of assets of $89.8 million. **d** Pacific Power has not paid a dividend based on operating profit since 1996-97. Dividends paid since 1997-98 are based on 100 per cent of fees received by Pacific Power to manage transitional issues relating to the restructure of generation.

TRANSGRID — New South Wales

TransGrid is a government-owned corporation responsible for the management and development of the NSW high voltage electricity network. It transmits power between generators, bulk distributor corporations, some direct customers and to other states. TransGrid's high voltage transmission network, comprising 72 substations and power station switchyards and 11 500km of transmission lines, is interconnected with the Victorian and South Australian systems.

TransGrid was formed as a statutory authority on 1 February 1995, under the *Electricity Transmission Authority Act 1994*. Following the initial establishment of the National Electricity Market (NEM) during 1996-97, TransGrid had the role of market and system operator for NSW.[1] On 14 December 1998, TransGrid became a corporatised entity under the *State Owned Corporations Act 1989*.

The large increase in profit (before tax, including abnormals) in 1999-00 reflects an abnormal gain of $65.7 million due to previous overfunding of superannuation contributions. This led to an improvement in profitability indicators. Revenue also declined in 1999-00, largely due to a determination by the Australian Competition and Consumer Commission (ACCC).[2]

TansGrid increased its capital expenditure during 1999-00 to $197 million. A change in accounting policy, relating to interest expenses incurred during the construction of assets, meant that interest payments were lower in 1999-00 despite an increase in the level of borrowings.[3] Changes in the duration of outstanding debt led to a sharp increase in the current ratio.

TransGrid makes tax-equivalent and dividend payments.[4] TransGrid is not required to provide any community service obligations by the NSW Government.

---

1 As the market and system operator responsible for the development and operation of the NSW wholesale electricity market, TransGrid was required to collect and pay monies associated with its operation. This role was subsequently transferred to the National Electricity Market Management Company in December 1998. With the exception of network charges and market fees, these monies are excluded from TransGrid's financial statements to avoid distortion.

2 Prior to 1999-00, network charges were regulated by the NSW Independent Pricing and Regulatory Tribunal. From 1 July 1999, the ACCC became the regulator. The ACCC issued a determination on 25 January 2000 setting revenue caps for TransGrid's regulated activities from 1 February 2000 to 30 June 2004.

3 Australian accounting standards require the capitalisation of borrowing costs that are directly attributable to the acquisition, construction of a 'qualifying' asset. Qualifying assets given as examples under the standards include assets resulting from development and construction activities in the extractive industries, manufacturing plants and power generation facilities.

4 TransGrid paid a debt guarantee fee of $257 000 in 1999-00.

TRANSGRID (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*	*1998-99*[b]	*1999-00*[c]
Size						
Total assets	$M	2 166	2 115	2 095	2 238	2 392
Total revenue	$M	402	386	374	371	354
Profitability						
Operating profit before tax (includes abnormals)	$'000	95 770	78 309	95 765	90 487	152 763
Operating sales margin	%	49.6	46.9	50.0	48.1	64.1
Cost recovery	%	196.0	182.4	199.9	192.5	226.8
Return on assets	%	9.5	8.5	8.9	8.3	9.8
Return on equity	%	5.9	4.4	5.5	4.9	10.4
Financial management						
Debt to equity	%	83.3	79.8	71.4	60.8	64.8
Debt to total assets	%	42.6	39.8	37.4	35.2	37.4
Total liabilities to equity	%	102.1	97.9	89.7	78.2	78.9
Interest cover	times	1.9	1.7	2.0	2.0	3.0
Current ratio	%	40.9	45.1	106.1	49.9	160.4
Leverage ratio	%	202.1	197.9	189.7	178.2	178.9
Payments to and from government						
Dividends	$'000	59 774	54 963	49 616	54 105	54 623
Dividend to equity ratio	%	5.9	5.1	4.6	4.6	4.2
Dividend payout ratio	%	100.6	115.7	82.8	92.8	40.6
Income tax expense	$'000	36 351	30 812	35 848	32 164	18 345[d]
CSO funding	$'000	0	0	0	0	0

a During 1996-97 TransGrid was the market and system operator responsible for the development and operation of the NSW wholesale electricity market. TransGrid was required to collect and pay monies associated with the market's operation. With the exception of network charges and market fees, these monies are excluded from TransGrid's financial statements. Market and system operation was transferred to the National Electricity Market Management Company in December 1998. **b** TransGrid's grid infrastructure assets were revalued using the optimised depreciated replacement cost methodology. This resulted in an increase in the value of infrastructure assets of $152.8 million. **c** Includes an abnormal gain of $65.7 million due to previous overfunding of superannuation contributions. A change in accounting policy in accordance with accounting standards led to interest on some capital expenditure being capitalised. **d** Income tax-equivalent payments were adjusted downwards by $10.8 million due to a reduction in the future company tax rate.

ADVANCE ENERGY — New South Wales

Advance Energy was established as a government-owned corporation on 1 March 1996 as part of the reform of the NSW electricity industry. Advance Energy is one of six distribution companies formed from the amalgamation of 25 distributors in 1995.

Under the retail supply market arrangements, Advance Energy is required to supply its franchise customers with electricity. Advance Energy's franchise region and distribution network are located in central NSW and cover a geographical area of 167 000 square kilometres. Advance Energy also supplies electricity to non-franchise customers.[1]

An increase in revenue of 18 per cent in 1999-00 compared to the previous year was underpinned by growth in Advance Energy's total customer base of 17 per cent and a 29 per cent increase in customers able to choose their retail supplier. However, profit (before tax, including abnormals) declined, reflecting a 22 per cent increase in expenses. In particular, profit was reduced by an abnormal expense of $1.6 million relating to a backpayment of sales tax.

Advance Energy operates under a revenue cap as determined by the Independent Pricing and Review Tribunal (IPART).[2] Prices for customers able to choose their electricity retailer are unregulated.

Debt levels increased by 13 per cent in 1999-00, reflecting $17 million in capital expenditure in Advance Energy's franchise area.

Advance Energy is required to make both tax-equivalent and dividend payments. Income tax-equivalent payments were reduced by $2.7 million in 1999-00 as a result of a fall in the future company tax rate.

Advance Energy receives funding for the provision of community service obligations (CSOs) from the NSW Government. These CSOs take the form of rebates and financial assistance to certain groups in the community.[3]

---

1 As part of the development of the National Electricity Market, retail competition has been introduced in stages. The first stage involved giving choice of retail supplier to only the largest consumers of electricity (from October 1996).

2 In March 1996, IPART set revenue caps for the network and retail supply businesses of the distributors for the three years to June 1999. IPART set revenue caps for the network business in December 1999 covering the period 1 February 2000 to 30 June 2004. In December 2000, IPART set prices for the retail business for the period 1 January 2001 to 30 June 2004.

3 Advance Energy internally funds losses incurred in supplying electricity to customers connected on uneconomic lines and installation and inspection services.

ADVANCE ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*	*1999-00*[c]
Size						
Total assets	$M	319	341	367	379	391
Total revenue	$M	189	199	219	230	272
Profitability						
Operating profit before tax (includes abnormals)	$'000	-6 682	24 811	43 897	24 354	20 276
Operating sales margin	%	-3.9	13.6	21.0	11.8	8.5
Cost recovery	%	106.8	117.0	124.3	113.4	110.0
Return on assets	%	-1.4	8.4	16.7	12.3	9.3
Return on equity	%	-3.8	6.3	17.5	7.8	7.8
Financial management						
Debt to equity	%	12.3	13.2	17.7	17.8	19.5
Debt to total assets	%	8.7	9.3	14.3	19.1	19.3
Total liabilities to equity	%	41.6	45.6	62.4	57.8	57.6
Interest cover	times	-1.9	9.3	17.3	8.4	7.4
Current ratio	%	98.7	106.8	82.7	89.6	81.9
Leverage ratio	%	141.6	145.6	162.4	157.8	157.6
Payments to and from government						
Dividends	$'000	1 701	17 963	37 568	3 773	11 150
Dividend to equity ratio	%	0.8	7.8	16.3	1.6	4.6
Dividend payout ratio	%	-20.1	124.9	93.6	20.7	58.9
Income tax expense	$'000	1 801	10 434	3 766	6 130	1 330[d]
CSO funding	$'000	315	2 318	2 466	2 464	2 495

a Data for the 1995-96 financial year reflects the combined operations of five former distributors to February 1996 and the newly established Advance Energy for the four month period to 30 June 1996. **b** 1997-98 is the first year that capital contributions by customers are included in total revenue. Capital contributions are recognised in the year they become receivable or are received. Contributions received at balance date but for which no work has been undertaken are recorded as a liability. **c** Includes abnormal expense of $1.6 million relating to a backpayment for sales tax. **d** Tax-equivalent payments were reduced by $2.7 million as a result of a fall in the future company tax rate.

AUSTRALIAN INLAND ENERGY — New South Wales

Australian Inland Energy (AIE) was established as a government-owned corporation on 1 March 1996 as part of the reform of the NSW electricity industry.[1] AIE is one of six distribution companies formed through the amalgamation of 25 distributors in 1995. It assumed the operations of the former Broken Hill Electricity and part of the operations of the former Murray River Electricity. AIE provides energy services to approximately 19 300 customers within a 155 100 square kilometre area in the far west and south-west of NSW.[2]

AIE has retained most customers within its franchise area that are able to choose their retail supplier following the staged introduction of competition as part of the National Electricity Market (NEM).[3]

Profitability declined in 1999-00 reflecting an increase in expenses. AIE recorded abnormal revenue of $1.6 million representing a prepayment of employer contributions for superannuation. AIE holds no debt and therefore does not make interest payments.

AIE operates under a revenue cap as determined by the Independent Pricing and Review Tribunal (IPART).[4] Prices for customers able to choose their electricity retailer are unregulated.

Since 1996-97, AIE has made tax-equivalent and dividend payments. The dividend for 1998-99 includes an additional payment of $2.2 million relating to the construction of the Balranald substation. This payment matched the NSW Government's subsidy for the construction of the substation.

AIE does not receive explicit community service obligation payments. However, it receives an operating subsidy from the NSW Government in recognition of the uneconomic nature of supplying electricity in sparsely populated areas. In 1999-00, the value of this subsidy was $5.3 million.

---

1 AIE was originally known as Far West Energy but was renamed in May 1996.

2 AIE merged with the Broken Hill Water Board to form Australian Inland Energy and Water in December 2000.

3 As part of the development of the NEM, retail competition has been introduced in stages. The first stage involved giving choice of retail supplier to only the largest consumers of electricity (from October 1996).

4 In March 1996, IPART set revenue caps for the network and retail supply businesses of the distributors for the three years to June 1999. IPART set revenue caps for the network business in December 1999 covering the period 1 February 2000 to 30 June 2004. In December 2000, IPART set prices for the retail business for the period 1 January 2001 to 30 June 2004.

AUSTRALIAN INLAND ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*	*1998-99*	*1999-00*[b]
Size						
Total assets	$M	45	53	58	63	67
Total revenue	$M	30	38	38	39	37
Profitability						
Operating profit before tax (includes abnormals)	$'000	-11 286	7 721	11 312	13 174	9 261
Operating sales margin	%	-39.1	19.1	28.1	32.0	23.0
Cost recovery	%	99.3	120.6	139.1	147.1	124.2
Return on assets	%	-25.2	15.7	20.2	21.7	14.2
Return on equity	%	-30.2	11.8	18.7	21.3	13.2
Financial management						
Debt to equity[c]	%	0	0	0	0	0
Debt to total assets[c]	%	0	0	0	0	0
Total liabilities to equity	%	20.0	31.6	31.0	30.9	29.0
Interest cover[c]	times	n.r.	n.r.	n.r.	n.r.	n.r.
Current ratio	%	251.7	231.0	290.1	278.7	184.7
Leverage ratio	%	120.0	131.6	131.0	130.9	129.0
Payments to and from government						
Dividends	$'000	0	3 100	3 583	5 721[d]	2 670
Dividend to equity ratio	%	0	8.0	8.4	12.3	5.3
Dividend payout ratio	%	0	67.6	45.0	57.9	40.4
Income tax expense	$'000	0	3 132	3 341	3 296	2 652
CSO funding[e]	$'000	0	0	0	0	0

a Australian Inland Energy incurred abnormal expenses ($11.5 million) related to the amalgamation and corporatisation process. In particular, there was a $10.9 million write-down in the value of current assets and a restructuring provision of $0.3 million. **b** Includes abnormal revenue of $1.6 million representing a prepayment of employer contributions for superannuation. **c** Australian Inland Energy does not hold any debt. Therefore the indicators cannot be calculated. **d** Includes an additional dividend of $2.2 million relating to the construction of the Balranald substation. **e** Australian Inland Energy does not receive explicit CSO payments. However, it receives an operating subsidy from the NSW Government in recognition of the uneconomic nature of supplying electricity in sparsely populated areas. In 1999-00, the value of the operating subsidy was $5.3 million. **n.r.** Not relevant.

ENERGYAUSTRALIA — New South Wales

EnergyAustralia was established as a government-owned corporation on 1 March 1996 as part of the reform of the NSW electricity industry. EnergyAustralia is one of six distribution companies formed through the amalgamation of 25 distributors in 1995.[1] EnergyAustralia's franchise distribution area covers over 22 275 square kilometres, with more than 24 000 GWh of electricity distributed annually to over 1.3 million customers.

Revenue growth due to increased consumption, capital contributions and non-regulated business growth underpinned EnergyAustralia's improved profit (before tax, including abnormals) in 1999-00. An abnormal gain of $23.5 million was reported relating to revised superannuation provisions. This was partly offset by abnormal expenses incurred due to year 2000 costs ($11.3 million).

The fall in the current ratio in 1999-00 reflects a $274 million reduction in current investments which was used to repay loans. As a result, debt levels have fallen by 20 per cent and financial management indicators improved.

EnergyAustralia operates under a revenue cap determined by the Independent Pricing and Review Tribunal (IPART).[2] Prices for non-franchise customers are unregulated. On 25 January 2000, the Australian Competition and Consumer Commission (ACCC) also made a determination in relation to EnergyAustralia's transmission assets.[3]

EnergyAustralia is required to make tax-equivalent and dividend payments. Tax-equivalent payments were lower in 1999-00 due to a change in accounting policy and a reduction in the future company tax rate.[4]

The NSW Government funds EnergyAustralia for the provision of agreed community service obligations. EnergyAustralia receives funding for the provision of rebates to pensioners and low income households, medical rebates for life support systems and the electricity payment assistance scheme.

---

1 EnergyAustralia was formed from the amalgamation of Sydney Electricity and Orion Energy.

2 In March 1996, IPART set revenue caps for the network and retail supply businesses of the distributors for the three years to June 1999. In December 1999, IPART set revenue caps for the period to June 2004. The determination provides for an average real price decrease of 16 per cent during the period.

3 The determination by the ACCC covers the same period as the IPART determination.

4 Accounting policy changed to treat tax on superannuation and capital contributions as a permanent difference rather than a timing difference.

ENERGYAUSTRALIA (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	3 634	3 609	3 746	3 788	3 732
Total revenue	$M	1 981	2 061	1 839	1 852	2 099
Profitability						
Operating profit before tax (includes abnormals)	$'000	-16 864	309 758	360 384	285 022	380 606
Operating sales margin	%	2.0	20.8	25.1	19.5	22.0
Cost recovery	%	112.3	125.1	129.6	125.3	127.7
Return on assets	%	1.5	12.2	12.8	9.9	12.4
Return on equity	%	-1.2	13.0	15.0	11.3	19.4
Financial management						
Debt to equity	%	83.2	83.7	82.6	79.9	59.5
Debt to total assets	%	34.9	35.2	35.5	34.4	28.0
Total liabilities to equity	%	138.0	136.6	137.1	133.5	111.2
Interest cover	times	0.8	3.4	4.3	4.2	5.5
Current ratio	%	76.1	67.3	96.7	117.8	73.6
Leverage ratio	%	238.0	236.6	237.1	233.5	211.2
Payments to and from government						
Dividends	$'000	32 613	199 166	177 868	138 800	184 300
Dividend to equity ratio	%	2.1	13.1	11.5	8.7	10.9
Dividend payout ratio	%	-184.3	100.4	76.6	76.5	56.0
Income tax expense	$'000	827	111 371	128 195	103 664	51 732[f]
CSO funding	$'000	22 683	24 606	25 800	28 500	26 468

a EnergyAustralia incurred abnormal expenses ($175.3 million) related to the amalgamation and corporatisation process. **b** Includes net abnormal revenue of $19.5 million related to prepaid superannuation contributions. **c** Includes net abnormal revenue of $54.3 million related to prepaid superannuation contributions. In line with Urgent Issues Group Abstract 17 issued by the Australian Accounting Research Foundation, EnergyAustralia moved from treating customer and developer capital contributions as revenue to recording them as a liability until the assets are constructed. This change in accounting policy reduced total revenue. **d** Includes abnormal expenses of $13.3 million relating to unfunded superannuation contributions. **e** An abnormal gain of $23.5 million was reported relating to revised superannuation provisions. This was partly offset by abnormal expenses incurred due to year 2000 costs ($11.3 million). **f** Accounting policy changed to treat tax on superannuation and capital contributions as a permanent difference rather than a timing difference. This change reduced the tax-equivalent expense by $39.2 million. A fall in the future company tax rate also reduced tax payable by $12.9 million.

GREAT SOUTHERN ENERGY — New South Wales

Great Southern Energy (GSE) was established, as a government-owned corporation in 1996, through the merger of nine southern NSW electricity distributors.[1] GSE distributes and retails electricity to approximately 223 000 customers over a franchise area of 174 450 square kilometres. GSE is also involved in the supply of natural gas and a number of ancillary activities, including specialist engineering services, advice on energy efficiency and electrical appliance sales.

GSE has increased market share following the phased introduction of choice of supplier in the retail electricity market.[2] Revenue from electricity sales has increased steadily over the reporting period. Revenue growth in 1999-00 reflected an increase in sales revenue and capital contributions.

Profitability also improved in 1999-00 due to an abnormal gain resulting from a change in superannuation provisions ($9.9 million). This was partly offset by several abnormal expenses including a loss on sale of buildings ($3.6 million), sales tax backpayment ($1.7 million) and restructuring and relocation costs ($1.4 million).

GSE operates under a revenue cap as determined by the Independent Pricing and Review Tribunal (IPART).[3] Prices for non-franchise customers are unregulated.

GSE is required to make tax-equivalent and dividend payments. Over the reporting period, GSE has declared dividends in accordance with NSW Treasury financial distribution policy.

No funding is received by GSE for community service obligations.[4]

---

1 Eight southern electricity distributors were merged with the southern part of the former Illawarra Electricity to form Energy South in October 1995. On 1 March 1996, Energy South became Great Southern Energy.

2 As a part of the development of the National Electricity Market, retail competition has been introduced in stages. The number of 'contestable' customers (those having choice of retail supplier) has gradually increased since March 1996, when the largest consumers of electricity had a choice of electricity supplier.

3 In March 1996, IPART set revenue caps for the network and retail supply businesses of the distributors for the three years to June 1999. In response to various IPART determinations, prices for standard urban residential customers fell by an average 1.9 per cent from 1 October 1999. At the same time, rural residential prices increased by an average 1.5 per cent. From 1 April 2000, prices fell by up to 3.2 per cent.

4 GSE provided concessions to pensioners, customers in caravan parks and to people who rely on life support machines worth $3.8 million in 1999-00.

GREAT SOUTHERN ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	497	579	628	626	677
Total revenue	$M	291	315	346	369	407
Profitability						
Operating profit before tax (includes abnormals)	$'000	-17 602	43 581	95 511	74 378	84 328
Operating sales margin	%	-8.9	13.5	28.9	21.3	21.6
Cost recovery	%	105.6	115.3	139.2	122.2	130.6
Return on assets	%	-3.2	8.9	16.9	13.0	13.9
Return on equity	%	-5.9	6.8	16.0	13.0	14.9
Financial management						
Debt to equity	%	17.2	25.0	24.5	23.6	22.1
Debt to total assets	%	0.5	1.2	1.7	1.9	1.7
Total liabilities to equity	%	41.3	57.0	69.1	65.0	68.2
Interest cover	times	-9.2	11.0	16.4	11.6	13.9
Current ratio	%	185.0	153.6	154.1	128.2	135.1
Leverage ratio	%	141.3	157.0	169.1	165.0	168.2
Payments to and from government						
Dividends	$'000	3 376	28 171	43 117	41 004	35 335
Dividend to equity ratio	%	1.0	7.8	11.6	10.9	9.0
Dividend payout ratio	%	-16.4	115.4	72.8	83.8	60.8
Income tax expense	$'000	3 024	19 165	36 283	25 467	26 258
CSO funding	$'000	0	0	0	0	0[e]

a Great Southern Energy (GSE) incurred abnormal expenses ($41 million) related to the amalgamation process. In particular, there was an expense of $18.3 million associated with an asset revaluation, $14.6 million relating to a restructure provision and $8.1 million associated with changes to the provision for employee entitlements. **b** GSE incurred abnormal revenue related to a superannuation actuarial assessment ($17.4 million) and an adjustment on the previous year's Transgrid charges ($4.9 million). GSE also incurred abnormal expenses related mainly to restructuring and relocation costs ($1.8 million) and an asset valuation adjustment ($8.7 million). Land and buildings were revalued downwards to current market value on 30 June 1998. The downward revaluation was offset by a significant increase in current assets. **c** GSE incurred abnormal expenses related mainly to a superannuation actuarial assessment ($4.2 million) and asset write-offs ($2 million). **d** GSE incurred abnormal expenses related to a loss on sale of buildings ($3.6 million), sales tax backpayment ($1.7 million), restructuring and relocation costs ($1.4 million) and other expenses ($0.5 million). This was offset by an abnormal gain due to a change in superannuation provisions ($9.9 million). **e** GSE provided concessions to pensioners, customers in caravan parks and to people who rely on life support machines of $3.8 million.

INTEGRAL ENERGY — New South Wales

Integral Energy was established as a government-owned corporation under the *Energy Services Corporations Act 1995*, following the merger of Prospect Electricity and the major portion of Illawarra Electricity in October 1996. Integral Energy distributes and retails electricity to over 1.9 million people in 760 000 households and businesses. Its franchise area of 24 500 square kilometres covers greater Western Sydney, the Illawarra and the Southern Highlands. It also operates a gas business.

With the introduction of a wholesale market for electricity and the phased introduction of choice in retail electricity supply, Integral Energy has been able to expand its customer base beyond its franchise area.[1]

An increase in profit (before tax, including abnormals) in 1999-00 reflected an abnormal gain of $23.7 million related to superannuation provisions.

Integral Energy's debt level was reduced by $102 million in 1999-00 compared to the previous year. This is reflected in an improvement in debt to equity and debt to total assets ratios.

In December 1999, the Independent Pricing and Review Tribunal set annual revenue requirements for the NSW distribution network for the period 1 February 2000 to 30 June 2004. The revenue cap provides for a real price reduction in network charges by 27 per cent over the period.

Integral Energy is required to make tax-equivalent and dividend payments to the NSW government. Dividend policy in 1999-00 was to pay 90 per cent of net profit before tax (excluding abnormals). The reporting of negative tax-equivalent payments in 1999-00 reflects a change in accounting policy regarding capital and superannuation contributions and reductions in the future company tax rate.

Integral Energy receives funding for the provision of community service obligations related primarily to rebates for pensioners.[2]

1 As part of the development of the National Electricity Market, retail competition has been introduced in stages. The first stage involved giving choice of retail supplier to only the largest consumers of electricity (from October 1996).

2 In 1999-00, the provision of pensioner rebates accounted for $12.8 million of the cost of social programs. Energy accounts payment assistance accounted for $3 million and life support equipment rebates of $0.3 million.

INTEGRAL ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	2 068	1 954	1 828	1 844	1 917
Total revenue	$M	1 108	1 047	1 119	1 177	1 122
Profitability						
Operating profit before tax (includes abnormals)	$'000	48 020	51 813	158 599	37 713	83 422
Operating sales margin	%	7.1	11.1	19.7	8.6	13.1
Cost recovery	%	111.7	120.7	121.2	113.3	112.6
Return on assets	%	4.0	6.1	11.9	5.6	7.9
Return on equity	%	1.4	1.7	13.1	2.8	15.6
Financial management						
Debt to equity	%	115.3	123.6	116.3	119.3	93.2
Debt to total assets	%	43.9	42.8	43.4	44.5	38.0
Total liabilities to equity	%	162.7	180.8	159.3	169.3	149.9
Interest cover	times	2.4	1.7	3.4	1.6	2.3
Current ratio	%	110.6	94.1	124.2	94.7	104.0
Leverage ratio	%	262.7	280.8	259.3	269.3	249.9
Payments to and from customers						
Dividends	$'000	27 487	98 460	92 066	45 918	29 743[f]
Dividend to equity ratio	%	3.5	13.1	12.0	6.8	3.9
Dividend payout ratio	%	243.2	768.8	91.7	242.0	26.1
Income tax expense	$'000	36 720	39 006	58 221	18 738	-30 648[g]
CSO funding	$'000	n.r.	12 770	12 978	13 069	13 399

a Includes abnormal expenses of $37.2 million related to the amalgamation process. **b** Integral Energy incurred abnormal expenses related to a write-down in the value of the street lighting system ($27 million) and some land and buildings ($40 million). Abnormal revenue ($7.6 million) related to prepaid superannuation contributions was also reported. **c** Includes abnormal revenue ($35 million) related to prepaid superannuation contributions and abnormal expenses ($3.9 million) related to a write-down in the value of some buildings. **d** Integral Energy incurred abnormal expenses ($36.5 million). In particular, there were abnormal expenses associated with a debt restructure ($9.4 million), prepaid superannuation contributions ($8 million) and year 2000 compliance costs ($10 million). **e** Includes an abnormal gain of $23.7 million related to superannuation provisions. **f** NSW Treasury changed the basis of dividend payments from available cash to 90 per cent of net profit before tax (excluding abnormals). **g** A change in the accounting treatment for tax purposes of capital and superannuation contributions reduced tax payable by $31.7 million. The fall in the future company tax rate also reduced tax payable by $10.2 million. **n.r.** Not relevant.

NORTHPOWER — New South Wales

NorthPower was established as a government-owned corporation in October 1996 following the merger of eight distributors. NorthPower's network franchise area covers 230 000 square kilometres in northern NSW. Currently, NorthPower has approximately 370 000 customers.

The phased introduction of choice in retail supply has allowed NorthPower to expand its customer base to outside the franchise area.

The increase in operating profit (before tax, including abnormals) in 1999-00 was mainly due to a 19 per cent growth in operating revenue. Abnormal revenue of $22.2 million relating to superannuation adjustments also contributed to the increase in profit.

Capital expenditure in 1999-00 was $89 million. Of this, $23 million was funded by capital contributions from customers. Most of the remainder of capital expenditure was financed by additional borrowings of $60 million. This has led to a rise in the debt to equity and debt to total assets ratios.

NorthPower makes tax-equivalent and dividend payments. Changes in the accounting treatment of capital contributions and an adjustment due to changes in the future company tax rate reduced tax-equivalent payments for 1999-00 by $19.4 million.[1]

NorthPower does not receive funding for community service obligations.[2]

1 The capital contributions were treated as timing differences and are now treated as permanent differences. This reduced tax-equivalent payments for 1999-00 by $17 million, relating to capital contributions over the period 1997–1999. Changes in the future company tax rate reduced tax-equivalent payments by $2.4 million.

2 NorthPower internally funds rebates and subsidies to disadvantaged customers in accordance with its own and the State Government's social welfare policies on financial assistance to certain disadvantaged groups in the community. In 1999-00, the value of these subsidies was estimated by NorthPower to be $9 million.

NORTH POWER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	638	665	831	1 117	1 227
Total revenue	$M	397	420	461	478	568
Profitability						
Operating profit before tax (includes abnormals)	$'000	114 781	30 237	102 387	46 972	88 180
Operating sales margin	%	30.7	9.6	24.1	11.3	17.4
Cost recovery	%	268.4	113.7	126.7	114.9	122.1
Return on assets	%	19.5	6.6	15.1	5.8	8.6
Return on equity	%	30.2	3.8	16.1	4.5	11.1
Financial management						
Debt to equity	%	42.0	35.3	27.2	22.2	27.8
Debt to total assets	%	23.7	21.5	18.6	17.1	19.2
Total liabilities to equity	%	77.3	67.5	62.8	48.6	51.3
Interest cover	times	13.3	3.4	11.0	6.0	8.1
Current ratio	%	106.9	112.2	114.9	77.4	88.0
Leverage ratio	%	177.3	167.5	162.8	148.6	151.3
Payments to and from government						
Dividends	$'000	6 341	17 969	58 080	35 522	31 731
Dividend to equity ratio	%	1.8	4.7	12.8	5.6	4.1
Dividend payout ratio	%	5.8	126.1	79.3	126.2	36.5
Income tax expense	$'000	6 043	15 990	29 134	18 829	-2 918
CSO funding	$'000	1 791	6 215	7 863	0	0

a NorthPower incurred abnormal expenses of $126.1 million. In particular, redundancy and early retirement payments ($11.3 million), a write-down in the value of assets ($105.5 million), debt restructuring ($4.9 million) and a provision for the cost of restructuring the organisation ($4.5 million). **b** NorthPower incurred abnormal expenses related to restructuring costs ($2 million) and a change in the provision for employee entitlements ($15.4 million). NorthPower also incurred abnormal revenue of $8.3 million. **c** NorthPower incurred abnormal expenses of $8.1 million. Major items included redundancy payments ($3.9 million) and a loss on the sale of properties ($3 million). NorthPower also incurred abnormal revenue of $28.2 million related to the recoupment of employer superannuation contributions ($21.5 million) and a change in the provision for employee entitlements ($6.7 million). The carrying amounts of network system assets were revalued upwards. **d** NorthPower incurred abnormal expenses of $8.2 million. Major items include redundancy payments ($2.1 million), an adjustment in the funding of employer superannuation contributions ($2.3 million) and year 2000 compliance costs ($2.5 million). The carrying amounts of network assets were revalued upwards by $247 million. **e** NorthPower reported abnormal revenue of $22.2 million as a result of an adjustment to superannuation contributions. This was partly offset by an abnormal expense of $1.9 million relating to inter-distributor charges for 1998-99.

CS ENERGY — Queensland

CS Energy was established as a government-owned corporation on 1 July 1997 as part of the reform of the Queensland electricity industry and is subject to the provisions of the *Government Owned Corporations Act 1999* (the GOC Act). Previously, the assets of CS Energy formed part of Queensland's largest generator AUSTA Electric.[1] CS Energy operates three power stations, generating electricity for Queensland's wholesale electricity market.[2]

Despite an increase in electricity production of 17 per cent in 1999-00, revenue was stable even though there was a 25 per cent fall in the average pool price. The decline in operating profit before tax (including abnormals) largely reflected an increase in expenses, including an additional $6 million depreciation expense as a result of a reassessment of the total useful life of a power station. The decrease in operating profit had a negative impact on a number of ratios, including return on assets and return on equity.

CS Energy reported capital expenditure of $252 million in 1999-00, most of which related to the construction of additional generating capacity. An increase in the level of borrowings of $119 million had a negative impact on financial management indicators.

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

CS Energy has not been required to perform any community service obligations over the reporting period.

1 On 1 July 1997, AUSTA Electric was separated into three independent and competing generation corporations and an engineering services corporation.

2 The Queensland wholesale electricity market commenced operating on 18 January 1998 based on the National Electricity Market (NEM). The Queensland market was physically connected to the NEM via the unregulated 180MW 'Directlink' in February 2000 and the Queensland-New South Wales Interconnector (currently 450MW) in February 2001.

CS ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*	*1999-00*
Size						
Total assets	$M	n.r.	n.r.	927	1 100	1 323
Total revenue	$M	n.r.	n.r.	447	478	480
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	98 566	161 826	113 047
Operating sales margin	%	n.r.	n.r.	25.3	36.6	28.3
Cost recovery	%	n.r.	n.r.	133.9	157.8	134.8
Return on assets	%	n.r.	n.r.	13.1	17.4	11.2
Return on equity	%	n.r.	n.r.	11.1	17.6	13.9
Financial management						
Debt to equity	%	n.r.	n.r.	36.8	44.6	60.4
Debt to total assets	%	n.r.	n.r.	23.3	26.1	31.7
Total liabilities to equity	%	n.r.	n.r.	63.5	85.4	108.0
Interest cover	times	n.r.	n.r.	6.4	12.3	5.9
Current ratio	%	n.r.	n.r.	89.0	81.4	79.2
Leverage ratio	%	n.r.	n.r.	163.5	185.4	208.0
Payments to and from government						
Dividends	$'000	n.r.	n.r.	38 800	75 800	57 111
Dividend to equity ratio	%	n.r.	n.r.	6.9	13.1	9.3
Dividend payout ratio	%	n.r.	n.r.	62.3	74.3	66.7
Income tax expense	$'000	n.r.	n.r.	36 315	59 825	27 381
CSO funding	$'000	n.r.	n.r.	0	0	0

a CS Energy was established on 1 July 1997. Hence, 1997-98 is the first year where financial data were available. **n.r.** Not relevant.

STANWELL CORPORATION — Queensland

Stanwell Corporation was established on 1 July 1997 as part of the restructure of the Queensland electricity industry and is subject to the provisions of the *Government Owned Corporations Act 1999* (the GOC Act). Stanwell Corporation is one of three generators established following the restructure of AUSTA Electric.[1] Stanwell Corporation operates six power stations with a combined generating capacity of 1 585 MW and supplies the Queensland wholesale electricity market.[2]

The decrease in operating profit before tax (including abnormals) in 1999-00, largely reflects decreased revenue from electricity sales and a reduction in the proceeds from the sale of non-current assets.

The debt to equity and debt to total asset ratios fell in 1999-00, following a reduction in the level of debt held by Stanwell Corporation. The fall in the current ratio reflects provision for an increase in dividends in 1999-00.

Stanwell Corporation is required to make income tax-equivalent and dividend payments. Its dividend payment is determined in accordance with the provisions of the GOC Act. Under the Act, the Board of Directors makes a recommendation to the shareholding Ministers on its proposed dividend payment. Shareholding Ministers may either approve the recommendation or direct the Board to pay a specified dividend.

Stanwell Corporation is not required to perform any community service obligations by the Queensland Government.

1 An engineering services corporation was also established through the restructure of AUSTA Electric.

2 The Queensland wholesale electricity market commenced operating on 18 January 1998 based on the National Electricity Market (NEM). The Queensland market was physically connected to the NEM via the unregulated 180MW 'Directlink' in February 2000 and the Queensland-New South Wales Interconnector (currently 450MW) in February 2001.

STANWELL CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*	*1999-00*
Size						
Total assets	$M	n.r.	n.r.	1 769	1 715	1 693
Total revenue	$M	n.r.	n.r.	384	450	431
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	123 171	179 538	162 454
Operating sales margin	%	n.r.	n.r.	44.3	48.7	44.3
Cost recovery	%	n.r.	n.r.	179.7	194.9	179.4
Return on assets	%	n.r.	n.r.	10.1	12.7	11.3
Return on equity	%	n.r.	n.r.	7.5	11.6	13.0
Financial management						
Debt to equity	%	n.r.	n.r.	62.9	51.0	36.1
Debt to total assets	%	n.r.	n.r.	37.2	29.9	21.8
Total liabilities to equity	%	n.r.	n.r.	73.8	68.0	64.1
Interest cover	times	n.r.	n.r.	3.5	5.3	6.4
Current ratio	%	n.r.	n.r.	155.1	204.4	74.2
Leverage ratio	%	n.r.	n.r.	173.8	168.0	168.0
Payments to and from government						
Dividends	$'000	n.r.	n.r.	40 000	107 808	123 591
Dividend to equity ratio	%	n.r.	n.r.	3.8	10.6	12.0
Dividend payout ratio	%	n.r.	n.r.	50.8	91.5	92.8
Income tax expense	$'000	n.r.	n.r.	44 441	61 752	29 218
CSO funding	$'000	n.r.	n.r.	0	0	0

[a] Stanwell Corporation was established on 1 July 1997. Hence, 1997-98 is the first year where financial data were available. **n.r.** Not relevant.

TARONG ENERGY — Queensland

Tarong Energy was established as a government-owned corporation on 1 July 1997, as part of the restructure of the Queensland electricity industry. Tarong Energy is subject to the provisions of the *Government Owned Corporations Act 1999* (the GOC Act). Previously the assets of Tarong Energy formed part of Queensland's largest generator, AUSTA Electric.[1] Tarong Energy operates two power stations and generates electricity for Queensland's wholesale electricity market.[2]

The debt to equity and debt to total assets ratios have fallen since 1997-98 as a result of a reduction in the level of borrowings. Debt reduction reduced Tarong Energy's interest expense by 40 per cent in 1999-00 compared to the previous year. Revaluations to several classes of non-current assets in 1999-00 led to a decrease in book value of $9.9m. However, this was more than offset by the construction of additional generators.

Tarong Energy is required to make tax-equivalent and dividend payments. Its dividend payment is determined in accordance with the provisions of the GOC Act. Under the Act, the Board of Directors makes a recommendation to the shareholding Ministers on its proposed dividend payment. Shareholding Ministers may either approve the recommendation or direct the Board to pay a specified dividend.

Tarong Energy is not required to perform any community service obligations by the Queensland Government.

1 On 1 July 1997 AUSTA Electric was separated into three independent and competing generation corporations and an engineering services corporation.

2 The Queensland wholesale electricity market commenced operating on 18 January 1998 based on the National Electricity Market (NEM). The Queensland market was physically connected to the NEM via the unregulated 180MW 'Directlink' in February 2000 and the Queensland-New South Wales Interconnector (currently 450MW) in February 2001.

TARONG ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*	*1999-00*[b]
Size						
Total assets	$M	n.r.	n.r.	1 391	1 263	1 418
Total revenue	$M	n.r.	n.r.	439	433	440
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	127 310	135 949	142 633
Operating sales margin	%	n.r.	n.r.	36.5	37.2	35.9
Cost recovery	%	n.r.	n.r.	157.5	159.3	156.1
Return on assets	%	n.r.	n.r.	12.1	12.2	11.8
Return on equity	%	n.r.	n.r.	10.0	10.7	13.2
Financial management						
Debt to equity	%	n.r.	n.r.	54.0	34.2	27.1
Debt to total assets	%	n.r.	n.r.	32.5	21.7	17.8
Total liabilities to equity	%	n.r.	n.r.	72.8	50.4	61.2
Interest cover	times	n.r.	n.r.	4.6	6.2	9.9
Current ratio	%	n.r.	n.r.	133.9	92.9	56.6
Leverage ratio	%	n.r.	n.r.	172.8	150.4	161.2
Payments to and from government						
Dividends	$'000	n.r.	n.r.	73 500	52 582	96 330
Dividend to equity ratio	%	n.r.	n.r.	9.0	6.4	11.2
Dividend payout ratio	%	n.r.	n.r.	90.0	60.0	84.7
Income tax expense	$'000	n.r.	n.r.	45 644	48 313	28 946
CSO funding	$'000	n.r.	n.r.	0	0	0

a Tarong Energy was established on 1 July 1997. Hence, 1997-98 is the first year where financial data were available. **b** Several classes of non-current assets were revalued downwards by $9.9 million. **n.r.** Not relevant.

ENERTRADE — Queensland

The Queensland Power Trading Corporation (QPTC) was established on 1 July 1997 following a restructure of Queensland's electricity supply industry. Its antecedents were the Queensland Transitional Trading Power Corporation and, before that, the Queensland Transmission and Supply Corporation. In October 2000, the QPTC was renamed Enertrade.

Enertrade has responsibility for trading electricity generated from several privately-owned power stations into the Queensland wholesale electricity market.[1] Enertrade also has several other functions including the management of assets and liabilities assumed from dissolved or superseded electricity corporations, remediation and disposal of disused power stations and sites and the disposal of surplus assets.

Between 1997-98 and 1999-00 there was a significant fall in the total assets held by Enertrade. As part of the restructuring of the Queensland electricity industry, QPTC was required to transfer its shares in subsidiary corporations to the Shareholding Ministers, and in return the Shareholding Ministers owed a debt (valued at $3.3 billion) to QPTC in relation to the transferred shares.[2]

The decline in revenue in 1999-00 reflected lower average pool prices. The level of profit (before tax, including abnormals) was increased by an abnormal gain of $5.7 million related to the write-back of provision for settlement of disputes.

Enertrade has made tax-equivalent payments and dividend payments over the reporting period. Its dividend payment is determined in accordance with the provisions of the *Government Owned Corporations Act 1999*. Under the Act, the Board of Directors makes a recommendation to the Shareholding Ministers on its proposed dividend payment. Shareholding Ministers may either approve the recommendation or direct the Board to pay a specified dividend.

Enertrade is not required to perform any community service obligations by the Queensland Government.

---

1 The Queensland wholesale electricity market commenced operating on 18 January 1998 based on the National Electricity Market (NEM). The Queensland market was physically connected to the NEM via the unregulated 180MW 'Directlink' in February 2000 and the Queensland-New South Wales Interconnector (currently 450MW) in February 2001.

2 On 1 April 1999, the net assets of AUSTA Electric were transferred to QPTC and this debt was reduced by $25 million. On 30 June 1999, 3 billion ordinary shares were cancelled and offset against the loan receivable from the Shareholding Ministers. A similar transaction on 29 June 2000 reduced the loan to nil.

ENERTRADE (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*[b]	*1999-00*[c]
Size						
Total assets	$M	n.r.	n.r.	3 528	553	310
Total revenue	$M	n.r.	n.r.	921	737	680
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	8 159	28 067	30 602
Operating sales margin	%	n.r.	n.r.	1.0	3.8	4.3
Cost recovery	%	n.r.	n.r.	100.7	103.8	103.7
Return on assets	%	n.r.	n.r.	0.3	1.6	8.2
Return on equity	%	n.r.	n.r.	0.2	1.1	7.4
Financial management						
Debt to equity	%	n.r.	n.r.	2.6	21.7	88.7
Debt to total assets	%	n.r.	n.r.	2.4	4.3	20.3
Total liabilities to equity	%	n.r.	n.r.	4.2	37.3	214.2
Interest cover	times	n.r.	n.r.	2.8	7.3	7.3
Current ratio	%	n.r.	n.r.	2 467.1	289.8	201.5
Leverage ratio	%	n.r.	n.r.	104.2	137.3	137.3
Payments to and from government						
Dividends	$'000	n.r.	n.r.	0	0	15 444
Dividend to equity ratio	%	n.r.	n.r.	0	0	6.2
Dividend payout ratio	%	n.r.	n.r.	0	0	83.5
Income tax expense	$'000	n.r.	n.r.	2 345	7 449	12 114
CSO funding	$'000	n.r.	n.r.	0	0	0

a The Queensland Power Trading Corporation (QTPC) was renamed Enertrade in October 2000. The QPTC was established on 1 July 1997. Hence, 1997-98 is the first year where financial data were available. **b** As part of the restructuring process, the QPTC was required to transfer its shares in subsidiary corporations to the Shareholding Ministers and in return the Shareholding Ministers owed a debt (valued at $3.3 billion) to QPTC in relation to the transferred shares. On 1 April 1999, the net assets of AUSTA Electric were transferred to QPTC and this debt was reduced by $25 million. On 30 June 1999, 3 billion ordinary shares were cancelled and offset against the loan receivable from the Shareholding Ministers. **c** On 29 June 2000, 307 million ordinary shares were cancelled and offset against the loan receivable from the Shareholding Ministers. **n.r.** Not relevant.

POWERLINK QUEENSLAND — Queensland

Powerlink Queensland was established in 1995 as a subsidiary of the Queensland Transmission and Supply Corporation. On 1 July 1997, Powerlink became a government-owned corporation reporting to Shareholding Ministers.[1] Powerlink owns and operates the Queensland transmission network. Its transmission grid extends over more than 1 700km, from far north Queensland to the NSW border.

The Queensland interim wholesale market commenced operating in January 1998.[2] The Queensland wholesale electricity market operates under the National Electricity Market's rules. Powerlink's transmission network prices are subject to regulation by the Office of Energy until January 2002. The current revenue caps cover the period 1999-00 to 2001-02.[3]

The increase in profitability in 1999-00 reflects a 16 per cent growth in revenue due to increased system demands. Profit (before tax, including abnormals) was moderated by abnormal expenses of $28.4 million relating to sales tax-equivalent payments ($27 million) and year 2000 expenses ($1.4 million). The large increase in Powerlink's assets in 1999-00 reflects capital expenditure of $244.8 million and asset revaluations of $773.8 million to supply system, land and buildings assets.

The increase in the current ratio in 1999-00 reflects a rise in receivables as a result of a $150 million loan to the Queensland Government. Powerlink funded the loan by increasing its level of borrowings.[4]

Powerlink is required to make income tax-equivalent and dividend payments. Powerlink is not required to perform any community service obligations by the Queensland Government.

1 The data included in this report refers only to Powerlink after it became an independent corporation in 1997-98.

2 The Queensland System Operator, a ring fenced business unit within Powerlink, acted as market and system operator. With the official commencement of the National Electricity Market in December 1998, this role was transferred to the National Electricity Market Management Company.

3 Powerlink will be regulated by the Australian Competition and Consumer Commission from January 2002.

4 The loan is part of capital restructuring and will be eliminated at the time capital restructuring (reduction in issued and paid up capital) is completed. The loan is unsecured, non-interest bearing and has no specified terms of repayment.

POWERLINK QUEENSLAND (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*[b]	*1999-00*[c]
Size						
Total assets	$M	n.r.	n.r.	1 842	1 737	2 554
Total revenue	$M	n.r.	n.r.	246	259	300
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	68 421	58 515	89 254
Operating sales margin	%	n.r.	n.r.	43.6	37.2	46.0
Cost recovery	%	n.r.	n.r.	193.4	197.5	224.4
Return on assets	%	n.r.	n.r.	6.5	5.4	6.4
Return on equity	%	n.r.	n.r.	4.5	4.1	7.1
Financial management						
Debt to equity	%	n.r.	n.r.	63.2	95.5	86.1
Debt to total assets	%	n.r.	n.r.	38.4	41.1	48.0
Total liabilities to equity	%	n.r.	n.r.	83.4	125.7	113.8
Interest cover	times	n.r.	n.r.	2.7	2.5	2.8
Current ratio	%	n.r.	n.r.	305.5	50.7	142.3
Leverage ratio	%	n.r.	n.r.	183.4	225.7	225.7
Payments to and from government						
Dividends	$'000	n.r.	n.r.	39 300	27 253	72 441
Dividend to equity ratio	%	n.r.	n.r.	4.0	3.1	7.4
Dividend payout ratio	%	n.r.	n.r.	88.1	75.0	104.4
Income tax expense	$'000	n.r.	n.r.	23 793	22 178	19 846[d]
CSO funding	$'000	n.r.	n.r.	0	0	0

a Powerlink Queensland was established as a separate government-owned corporation in 1997-98. Hence, 1997-98 is the first year where financial data were available. The Queensland interim wholesale market commenced operating in January 1998. The Queensland System Operator, a ring fenced business unit within Powerlink was given responsibility for managing the market and system security. Powerlink incurred abnormal expenses of $12.3 million related to a refund of capital contributions to contestable customers and abnormal revenue of $1.3 million related to the provision for a swing load rebate. As a part of a capital restructure, Powerlink was required by its Shareholding Ministers to make interest free loans (valued at $249 million) to the State of Queensland. This resulted in a 90 per cent increase in debt. **b** The National Electricity Market officially commenced operating in December 1998 and the role of market operator was transferred to the National Electricity Market Management Company. Powerlink incurred abnormal expenses of $9.8 million related to the refund of capital contributions to contestable customers and $1.5 million related to year 2000 compliance costs. **c** Includes abnormal expenses of $28.4 million relating to sales tax-equivalent payments ($27 million) and year 2000 compliance costs ($1.4 million). The growth in assets reflects capital expenditure of $244.8 million and an increase in asset values of $773.8 million following a revaluation of supply system assets, freehold land and buildings. Powerlink made a $150 million loan to the Queensland Government. **d** Income tax-equivalent payments were reduced by $17.9 million due to a fall in the future company tax rate. **n.r.** not relevant.

ERGON ENERGY — Queensland

In January 1995, the Queensland Government corporatised the Queensland Electricity Commission and separated the generation function from transmission and distribution. The transmission and distribution assets were owned by seven regional distribution corporations. The distribution corporations were, in turn, owned by the Queensland Transmission and Supply Corporation (QTSC) — a holding company. In December 1996, QTSC was abolished and the distribution companies were restructured, as separate government-owned corporations.[1]

Three new retail corporations were established and two of these were subsequently merged to form Ergon Energy Pty Ltd.[2] Ergon Energy Pty Ltd was owned by six of the regional distribution corporations.

Ergon Energy Corporation was established as a government-owned corporation under the *Government Owned Corporations (Ergon Corporatisation) Regulation* on 30 June 1999, by amalgamating the six regional distribution corporations. Ergon Energy Pty Ltd became a wholly-owned subsidiary. Ergon Energy Corporation has over 555 000 customers and manages over 135 000km of electricity network.

Whilst Ergon Energy Pty Ltd continues to provide retail services, 1999-00 presents information covering the first year of operation for Ergon Energy Corporation. It is difficult to compare results with previous years.[3]

In 1999-00, operating profit (before tax, including abnormals) was reduced by an abnormal expense of $20.4 million relating to sales tax-equivalent payments. The relatively high debt to equity and debt to total assets ratios reflects a level of debt for Ergon Energy Corporation of $1.1 billion in 1999-00, compared to Ergon Energy Pty Ltd borrowings of $22.2 million.

Ergon Energy Corporation is required to make income tax-equivalent and dividend payments. Tax-equivalent payments were reduced by $2.1 million as a result of a fall in the future company tax rate.

---

1 The six regional distribution corporations were the Far North Queensland Electricity Corporation Limited, North Queensland Electricity Corporation Limited, Mackay Electricity Corporation Limited, Capricornia Electricity Corporation Limited, Wide Bay-Burnett Electricity Corporation Limited and South West Queensland Electricity Corporation Limited.

2 Ergon Energy Pty Ltd was formed through a merger of the Northern Electricity Retail Corporation (Omega Energy) and Central Electricity Retail Corporation (Ergon Energy) in February 1998. The other retail corporation is Energex Retail.

3 Ergon Energy Pty Ltd accounts for about 12 per cent of Ergon Energy Corporation's total assets. However, it accounted for 90 per cent of the Corporation's revenue in 1999-00.

ERGON ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*	*1999-00*
Size						
Total assets	$M	n.r.	n.r.	n.r.	n.r.	2 786
Total revenue	$M	n.r.	n.r.	n.r.	n.r.	1323
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	n.r.	n.r.	45 779
Operating sales margin	%	n.r.	n.r.	n.r.	n.r.	7.6
Cost recovery	%	n.r.	n.r.	n.r.	n.r.	110.1
Return on assets	%	n.r.	n.r.	n.r.	n.r.	7.0
Return on equity	%	n.r.	n.r.	n.r.	n.r.	7.4
Financial management						
Debt to equity	%	n.r.	n.r.	n.r.	n.r.	100.4
Debt to total assets	%	n.r.	n.r.	n.r.	n.r.	70.8
Total liabilities to equity	%	n.r.	n.r.	n.r.	n.r.	156.4
Interest cover	times	n.r.	n.r.	n.r.	n.r.	1.7
Current ratio	%	n.r.	n.r.	n.r.	n.r.	111.3
Leverage ratio	%	n.r.	n.r.	n.r.	n.r.	223.4
Payments to and from government						
Dividends	$'000	n.r.	n.r.	n.r.	n.r.	38 928
Dividend to equity ratio	%	n.r.	n.r.	n.r.	n.r.	6.4
Dividend payout ratio	%	n.r.	n.r.	n.r.	n.r.	86.8
Income tax expense	$'000	n.r.	n.r.	n.r.	n.r.	917
CSO funding	$'000	n.r.	n.r.	n.r.	n.r.	244 768

n.r. Not relevant.

ENERGEX — Queensland

South East Queensland Electricity Board (SEQEB) became a subsidiary of the Queensland Transmission and Supply Corporation on 1 January 1995. On 1 July 1997, the Corporation and a newly formed, wholly owned subsidiary were registered to become South East Queensland Electricity Corporation (SEQEC) Pty Ltd (a licensed distributor) and Southern Electricity Retail Corporation (SERC) Pty Ltd (a licensed retailer). On 30 October 1997, SEQEB changed its trading name to Energex.

Following the acquisition of Allgas Energy Ltd during 1998-99, Energex Retail sells gas and electricity products and services to more than one million customers.

The incorporation of SEQEC and its wholly owned subsidiary SERC during 1997-98 makes it difficult to compare financial performance with previous years. The phased introduction of customer choice of retail supplier and the acquisition of Allgas Ltd have contributed to the growth in total revenue since 1997-98.[1]

Despite a growth in revenue in 1999-00, operating profit (before tax, including abnormals) declined. Expenses increased by 15 per cent due partly to abnormal expenses of $11 million. Interest expense also rose $9 million due to higher levels of borrowing.

As a part of a capital restructure, Energex was directed by its Shareholding Ministers to make interest free loans (valued at $300 million) to the Queensland Government in 1997-98. These were financed through an increase in long-term debt. In 1998-99, the loan was restructured as a reduction in issued capital.

Energex is required to make income tax-equivalent and dividend payments. Its dividend distribution policy is outlined in a statement of corporate intent agreed to by its Shareholding Ministers. A restatement of deferred tax balances due to a change in the future company tax rate led to an income tax payment of $209 000 for 1999-00.

Energex receives community service obligation (CSO) funding from the Queensland Government for the uneconomic supply of electricity to some franchise customers, electrical inspections, pensioner rebates and the administration of pensioner rebates.[2]

---

1 Customers with sites using $\geq$ 40GWh were given the choice of retail supplier from 29 March 1998. Customers with sites using $\geq$ 4GWh were given the choice of retail supplier from October 1998.

2 CSO funding for electrical inspections ceased in 1997-98.

ENERGEX (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	2 275	2 334	2 927	2 962	3 237
Total revenue	$M	1 303	1 343	1 424	1 560	1 736
Profitability						
Operating profit before tax (includes abnormals)	$'000	98 239	86 314	186 993	87 171	41 121
Operating sales margin	%	11.5	9.9	17.1	10.0	6.9
Cost recovery	%	113.0	112.6	122.0	112.2	108.1
Return on assets	%	7.0	6.1	8.6	5.5	4.0
Return on equity	%	5.4	4.9	8.4	4.5	3.3
Financial management						
Debt to equity	%	44.7	47.9	67.0	110.0	128.2
Debt to total assets	%	27.7	30.0	34.6	45.9	50.3
Total liabilities to equity	%	62.4	61.7	93.9	141.4	166.1
Interest cover	times	2.6	2.6	3.9	2.2	1.5
Current ratio	%	111.5	161.8	265.1	132.1	197.6
Leverage ratio	%	162.4	161.7	193.9	241.4	266.1
Payments to and from government						
Dividends	$'000	55 450	20 296	105 500	63 607	43 051
Dividend to equity ratio	%	4.0	1.4	7.0	4.6	3.5
Dividend payout ratio	%	74.9	29.4	83.6	104.1	105.2
Income tax expense	$'000	24 239	17 288	60 726	26 073	209[e]
CSO funding	$'000	20 820	22 341	21 734	22 625	23 597

a Energex incurred abnormal expenses ($12.6 million) related to redundancy payments and a land and building revaluation decrement ($5 million). **b** On 1 July 1997, South East Queensland Electricity Board and a newly formed, wholly-owned subsidiary were registered to become South East Queensland Electricity Corporation Pty Ltd and Southern Electricity Retail Corporation Pty Ltd. As a consequence, data for this year and previous years is not directly comparable. Energex incurred abnormal expenses related to redundancy payments ($13.4 million). **c** Energex incurred abnormal expenses related to redundancy payments ($5.8 million), year 2000 compliance costs ($4.7 million) and write-off expenses ($3 million). **d** Energex incurred abnormal expenses related to a write-down in the value of land and buildings ($4.7 million), a change in sales tax exemption status ($1.7 million), loss on disposal of assets from a discontinued project ($1.8 million) and year 2000 compliance expenses ($1.8 million). **e** Changes in the future company tax rate led to a restatement of deferred tax balances.

WESTERN POWER — Western Australia

Western Power was established on 1 January 1995 as a corporatised entity following the disaggregation of the State Energy Commission of Western Australia into separate gas and electricity businesses. Western Power operates five major and 26 smaller power stations with a total capacity of 3 280 MW. Western Power is also involved in the transmission and distribution of electricity. Its 775 000 customers are supplied through two major interconnected systems — one in the south-west corner of Western Australia and the other in the Pilbara in the north — as well as 29 separate systems in remote parts of the State.

Western Power has been able to improve profitability over the reporting period largely through increased revenue from electricity sales, funding for the provision of community service obligations (CSOs) and cost management.[1] A 3 per cent reduction in expenses in 1999-00 more than offset a decline in revenue and led to an improvement in profit (before tax, including abnormals) and the cost recovery ratio. In 1999-00, Western Power reported abnormal revenue relating to adjustments for unread debtors ($28 million). This was offset by abnormal expenses relating to refinancing costs ($47.3 million), redundancy costs ($26.6 million) and decommissioning costs ($8 million).

Over the reporting period, Western Power has carried a high level of debt as reflected in its debt to equity and debt to total asset ratios. Debt restructuring in 1998-99 contributed to a fall in the debt to equity ratio. A further fall in this ratio in 1999-00 was due to refinancing a portion of long-term debt. Debt restructuring should result in lower interest expenses in the future.

Western Power makes dividend and income tax-equivalent payments to the State Government.[2] It receives funding for CSOs in relation to rebates provided to customers.[3]

---

1 From January 1997 all customers taking supply at 66kV and above were able to purchase electricity from the supplier of their choice via Western Power's transmission network. From 1 January 1998, customers within the regional non-interconnected systems with an average load exceeding 300 000kWh were given choice of supplier, and from 1 July 1999, customers with an average load exceeding 5MW were given choice of supplier. The most recent stage came into effect on 1 January 2000, when customers with an average load exceeding 1MW were given choice of supplier.

2 Western Power also paid $4.2 million as a loan guarantee charge on borrowings in 1999-00.

3 Western Power is also required to offer residential and small to medium business customers in remote areas the same tariff as customers in metropolitan areas, despite any differences in the cost of providing the service. The losses incurred by Western Power in providing uniform tariffs are met internally.

WESTERN POWER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*[a]	*1999-00*[b]
Size						
Total assets	$M	3 388	3 684	3 990	4 018	4 038
Total revenue	$M	1 311	1 336	1 398	1 604	1 575
Profitability						
Operating profit before tax (includes abnormals)	$'000	138 325	155 370	227 620	223 369	230 294
Operating sales margin	%	26.9	26.2	27.8	24.4	28.1
Cost recovery	%	136.8	135.4	138.4	141.0	147.2
Return on assets	%	10.8	10.0	10.2	9.9	11.0
Return on equity	%	13.7	14.2	18.0	15.1	12.9
Financial management						
Debt to equity	%	325.0	317.9	299.0	251.2	195.9
Debt to total assets	%	65.6	65.7	65.6	64.7	60.4
Total liabilities to equity	%	412.1	404.3	373.9	289.8	224.9
Interest cover	times	1.6	1.8	2.4	2.3	2.1
Current ratio	%	166.9	154.8	108.1	106.5	41.9
Leverage ratio	%	512.1	504.3	473.9	389.8	324.9
Payments to and from government						
Dividends	$'000	25 000	30 000	30 000	42 332	46 209
Dividend to equity ratio	%	4.0	4.3	3.8	4.5	4.1
Dividend payout ratio	%	29.0	30.4	21.2	30.0	31.5
Income tax expense	$'000	52 116	56 598	85 986	82 273	83 828[c]
CSO funding	$'000	0	28 800	31 400	32 788	27 000

a Western Power incurred abnormal revenue relating to fuel back payments following the resolution of the gas price determination ($32.1 million), a reduction in a gas turbine operating lease provision following the purchase of five gas turbines ($38.3 million) and a payment from the Western Australian Government relating to future gas royalties from the North West Shelf ($57.2 million). Western Power also incurred abnormal expenses relating to debt refinancing ($107.5 million) and the write-down of prepaid gas following the agreement reached regarding the North West Shelf gas royalties ($57.2 million). Western Power changed its accounting policy for developer and customer contributions effective from 1 July 1998. Previously, these were treated as deferred income and amortised over the life of the assets that the contribution funded. Contributions are now treated as revenue in the year in which they are received. **b** Includes abnormal revenue relating to adjustments for unread debtors ($28 million). This was offset by abnormal expenses relating to refinancing costs ($47.3 million), redundancy costs ($26.6 million) and decommissioning costs ($8 million). **c** A fall in the future company tax rate reduced income tax-equivalent payments by $7.8 million.

HYDRO–ELECTRIC CORPORATION Tasmania

On 1 July 1998, the Hydro-Electric Corporation (HEC) was separated into three businesses.[1] With control of the State's 27 hydro, one thermal, two diesel power stations and a wind farm, the HEC generates electricity and provides consulting services on mainland Tasmania. The HEC is also responsible for generation, distribution and retailing on the Bass Straight Islands, although service delivery has been contracted to Aurora Energy.

The financial impact of the restructure was a reduction in the HEC's equity of $520.1 million — the net assets that were transferred to the two new businesses. The restructure makes direct comparisons of financial performance with previous years difficult. On 1 July 2000, the responsibility of system controller for the Tasmanian electricity network was transferred to Transend Networks.

An abnormal expense of $26.8 million relating to debt restructuring contributed to a decline in profit (before tax, including abnormals) and other profitability indicators in 1999-00.[2] Loans with a face value of $198 million and interest swaps of $302 million were terminated prior to maturity. The restructure provided a reduction in the future interest expense of the HEC.

The HEC is subject to the *Government Business Enterprises Act 1995* (GBE Act) and is required to make tax-equivalent and dividend payments. The HEC also makes payments for debt guarantees and a percentage of retail energy sales.[3]

An explicit community service obligation (CSO) payment was made to the HEC for the first time in 1998-99. The CSO payment covers the provision of electricity to customers on the Bass Strait Islands, which is supplied at below the cost of production.

---

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

2 Changes to accounting policy relating to abnormal expenditure have resulted in items being classified as abnormal only if they are of a very significant quantum. Abnormal expenses reported in 1998-99 would have been classified as operating expenditure under this policy.

3 The GBE Act also provides for the payment of special dividends. Special dividends are unrelated to the current year's profits and are seen as a return on excess reserves, capital or a provision to the government as owner. The HEC paid a debt guarantee fee of $3 million in 1999-00. The HEC also makes payments to consolidated revenue under the *Hydro-Electric Corporation (Contributions) Act*. These payments are at the rate of 5 per cent of the income derived from sales to retail customers to residents of Bass Straight Islands ($0.6m in 1999-00).

HYDRO–ELECTRIC CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	4 584	4 374	4 041	3 199	3 250
Total revenue	$M	517	528	538	323	323
Profitability						
Operating profit before tax (includes abnormals)	$'000	64 766	85 486	94 693	26 792	1 676
Operating sales margin	%	52.8	53.2	46.8	41.5	31.5
Cost recovery	%	213.3	216.5	193.4	179.9	164.3
Return on assets	%	6.3	6.3	6.0	3.7	3.2
Return on equity	%	1.0	1.3	1.7	0.1	0.4
Financial management						
Debt to equity	%	58.5	59.1	67.7	61.2	57.5
Debt to total assets	%	34.7	31.8	33.2	28.9	32.1
Total liabilities to equity	%	77.6	81.2	95.9	87.0	80.4
Interest cover	times	1.3	1.4	1.6	1.2	1.0
Current ratio	%	41.0	26.1	27.7	17.9	25.2
Leverage ratio	%	177.6	181.2	195.9	187.0	180.4
Payments to and from government						
Dividends	$'000	28 979	27 153	57 709	42 591	45 062
Dividend to equity ratio	%	1.2	1.1	2.6	2.3	2.6
Dividend payout ratio	%	127.5	84.0	148.3	1 643.8	623.9
Income tax expense	$'000	42 037	53 180	55 790	24 201	-5 547
CSO funding	$'000	0	0	0	4 390	4 551

a Property, plant and equipment is revalued each year to its deprival value. Includes asset revaluation increase of $542 million. **b** Includes asset revaluation decrement of $171 million. **c** The Hydro-Electric Corporation incurred abnormal expenses relating to the refurbishment of property assets in villages around power stations in readiness for their disposal. Includes asset revaluation decrement of $329 million. **d** On 1 July 1998, the HEC was structurally separated into three businesses. This involved the transfer of assets (valued at $1 billion) and liabilities (valued at $472.3 million) relating to transmission, distribution and retailing to Aurora Energy and Transend Networks. The data from 1998-99 relates only to the restructured HEC. The HEC incurred abnormal expenses relating to maintenance on one power station and the refurbishment of another to meet peak demand as a consequence of the maintenance being undertaken on the first. Includes asset revaluation increase of $209 million. **e** The HEC reported an abnormal expense of $26.8 million related to debt restructuring. Includes asset valuation increase of $129 million.

AURORA ENERGY — Tasmania

Aurora Energy Pty Ltd was established on 1 July 1998 following the structural separation of the Hydro-Electric Corporation (HEC).[1] Aurora Energy is mainland Tasmania's only electricity distribution and retail company. It was formed under the *Electricity Companies Act 1997* and incorporated under corporations law.

In November 1999, Aurora Energy was subject to a pricing determination by the Tasmanian Electricity Regulator covering the period January 2000 to January 2003. The outcome was a 7 per cent per year average reduction in prices for high voltage customers, 1.3 per cent reduction for low voltage customers and a 1 per cent rise for domestic customers.

In 1999-00, Aurora Energy reported abnormal expenses of $2.9 million relating to redundancy and retirement payments, rebranding costs, and costs associated with year 2000 preparation and GST implementation. This was offset by abnormal revenue of $2.3 million relating to a reversal of superannuation provisions.

Aurora Energy is subject to the income tax-equivalent provisions of the *Government Business Enterprises Act 1995* (GBE Act). Aurora Energy also paid dividends over the reporting period.[2]

Additional returns to government are paid in the form of a debt guarantee levy ($1 million in 1999-00) and a contribution to the consolidated fund related to energy sales ($14.5 million in 1999-00).[3]

Aurora Energy has a Community Service Activity Agreement with the Tasmanian Government under which it receives a payment for providing pensioners with discounted electricity.

---

1 The HEC continues to be responsible for the generation of electricity, system control and provides consulting services on mainland Tasmania. The HEC is also responsible for generation, distribution and retailing on the Bass Straight Islands, although service delivery has been contracted to Aurora Energy. Transend Networks is responsible for electricity transmission.

2 Under the GBE Act, nominated GBEs are required to make dividend payments. Aurora Energy is a government-owned company and is not explicitly subject to these provisions. It is not clear what dividend requirements have been placed on Aurora Energy by its shareholder government.

3 Under the *Electricity Companies Act 1997*, Aurora Energy is required to pay a guarantee fee. The rate is based on the difference between interest rates at which GTEs have borrowed and interest rates which would have been payable had the GTEs raised funds on the open market, without any explicit or implicit assistance from the Tasmanian Government. Under the provisions of the *Electricity Entities (Contributions Act) 1997* Aurora Energy pays a levy determined at the rate of 5 per cent of income derived from energy sales to retail customers, other than eligible pensioners in receipt of a discount.

AURORA ENERGY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*[a]	*1999-00*[b]
Size						
Total assets	$M	n.r.	n.r.	n.r.	762	765
Total revenue	$M	n.r.	n.r.	n.r.	543	551
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	n.r.	26 596	29 105
Operating sales margin	%	n.r.	n.r.	n.r.	11.9	12.7
Cost recovery	%	n.r.	n.r.	n.r.	112.7	114.7
Return on assets	%	n.r.	n.r.	n.r.	8.6	9.3
Return on equity	%	n.r.	n.r.	n.r.	5.5	8.4
Financial management						
Debt to equity	%	n.r.	n.r.	n.r.	171.2	158.8
Debt to total assets	%	n.r.	n.r.	n.r.	51.0	49.5
Total liabilities to equity	%	n.r.	n.r.	n.r.	235.7	221.2
Interest cover	times	n.r.	n.r.	n.r.	1.7	1.7
Current ratio	%	n.r.	n.r.	n.r.	72.2	76.7
Leverage ratio	%	n.r.	n.r.	n.r.	335.7	321.2
Payments to and from government						
Dividends	$'000	n.r.	n.r.	n.r.	6 200	10 052
Dividend to equity ratio	%	n.r.	n.r.	n.r.	2.7	4.2
Dividend payout ratio	%	n.r.	n.r.	n.r.	50.0	50.0
Income tax expense	$'000	n.r.	n.r.	n.r.	14 196	9 002
CSO funding	$'000	n.r.	n.r.	n.r.	9 826	9 797

a Aurora Energy commenced operations on 1 July 1998 following the restructure of the former Hydro-Electric Corporation. Aurora Energy is responsible for the low voltage distribution and retailing of electricity and has an exclusive retail licence for all of Tasmania, excluding the Bass Strait Islands. Aurora Energy incurred abnormal expenses ($3.8 million) relating to payments made to staff under redundancy and voluntary advanced retirement programs and rebranding costs. **b** Aurora Energy reported abnormal expenses of $2.9 million relating to redundancy and retirement payments, rebranding costs, and costs associated with year 2000 preparation and GST implementation. This was offset by abnormal revenue of $2.3 million relating to a reversal of superannuation provisions. **n.r.** Not relevant.

TRANSEND NETWORKS — Tasmania

Transend Networks owns and operates the electricity transmission system in Tasmania, which includes almost 3 500km of overhead transmission lines, 45 substations and 10 switching stations around Tasmania. Transend commenced trading on 1 July 1998 following the structural separation from the Hydro-Electric Corporation (HEC).[1]

Transend was formed under the *Electricity Companies Act 1997* and incorporated under corporations law. On 1 July 2000, Transend assumed responsibility of system controller for the Tasmanian electricity network from HEC, making it responsible for maintaining power system security and assisting with power system planning.

Capital expenditure to replace and refurbish assets amounted to $36.2 million in 1999-00. In November 1999, Transend was subject to a pricing determination by the Tasmanian Electricity Regulator covering the period January 2000 to January 2003. The outcome was that the revenue cap was increased by 4.3 per cent for Transend's regulated activities.

Transend's borrowing increased by 37 per cent in 1999-00. This led to a higher level of interest payments and a reduction in interest cover.

Transend is subject to the income tax-equivalent provisions of the *Government Business Enterprises Act 1995*. In 1999-00, Transend declared a dividend of $11.2 million — 50 per cent of after tax operating profit.[2]

Transend is not required to perform any community service obligations.

1 The HEC continues to be responsible for the generation of electricity on mainland Tasmania. Aurora Energy is responsible for electricity distribution and retailing.

2 Under the *Government Business Enterprises Act 1995* nominated Enterprises are required to make dividend payments. Transend is a government-owned company and is not explicitly subject to these provisions. It is not clear what dividend requirements have been placed on Transend by its shareholders.

TRANSEND NETWORKS (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*	*1999-00*
Size						
Total assets	$M	n.r.	n.r.	n.r.	406	437
Total revenue	$M	n.r.	n.r.	n.r.	66	68
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	n.r.	34 656	34 220
Operating sales margin	%	n.r.	n.r.	n.r.	52.8	51.6
Cost recovery	%	n.r.	n.r.	n.r.	211.7	206.5
Return on assets	%	n.r.	n.r.	n.r.	8.6	8.3
Return on equity	%	n.r.	n.r.	n.r.	5.7	5.2
Financial management						
Debt to equity	%	n.r.	n.r.	n.r.	4.0	5.2
Debt to total assets	%	n.r.	n.r.	n.r.	3.5	4.6
Total liabilities to equity	%	n.r.	n.r.	n.r.	15.7	16.8
Interest cover	times	n.r.	n.r.	n.r.	91.7	41.4
Current ratio	%	n.r.	n.r.	n.r.	27.1	27.3
Leverage ratio	%	n.r.	n.r.	n.r.	115.7	116.8
Payments to and from government						
Dividends	$'000	n.r.	n.r.	n.r.	9 994	11 199
Dividend to equity ratio	%	n.r.	n.r.	n.r.	2.8	3.1
Dividend payout ratio	%	n.r.	n.r.	n.r.	50.0	50.0
Income tax expense	$'000	n.r.	n.r.	n.r.	14 668	11 821
CSO funding	$'000	n.r.	n.r.	n.r.	0	0

n.r. Not relevant.

SNOWY MOUNTAINS HYDRO–ELECTRIC AUTHORITY — Commonwealth

The Snowy Mountains Hydro-Electric Authority (SMHEA) was established in 1949 under Commonwealth legislation to construct and operate the Snowy Mountains Scheme — a dual-purpose hydro-electric and irrigation development in the Snowy Mountains. The SMHEA is responsible for the collection, storage, diversion and release of water for irrigation purposes and the generation and transmission of electricity for NSW, Victoria and the Australian Capital Territory. The Commonwealth, NSW and Victoria are joint shareholder governments of the SMHEA.

The SMHEA remains a statutory authority and does not face the same type of financial market disciplines imposed on corporatised government trading enterprises by their shareholder governments.[1]

The SMHEA generates its revenue through contributions from the recipients of the Scheme's energy production. Under the *Snowy Mountains Hydro-Electric Power Act 1949*, contributions are made to the Authority's revenue on the basis of the net cost of production.[2] Net cost of production has fallen by 19 per cent over the reporting period. The Authority does not generate any revenue from its water operations.

Over the reporting period, the SMHEA has maintained a cost recovery ratio of around 90 per cent and earned a relatively low return on assets. The operating losses incurred over the period largely stem from an asset revaluation in 1991 which led to additional depreciation charges.[3]

The Authority is not subject to any explicit community service obligations, nor is it required to make dividend payments, pay tax or make tax-equivalent payments.

---

1 In 1997, Snowy Hydro Trading Pty Ltd (SHTPL) was established to trade electricity generated by the Snowy scheme in the National Electricity Market (NEM). It is expected that in 2000-01, a new corporation (Snowy Hydro Limited) will be formed from the merger of SMHEA and SHTPL. Snowy Hydro Limited will be incorporated under corporations law and subject to national competition laws as well as the overall regulatory framework applying to all participants in the NEM.

2 For any given year the net cost of production includes annual interest, an instalment for accumulated interest, depreciation, maintenance charges and operational costs less miscellaneous credits of a current nature.

3 Under the *Snowy Mountains Hydro-Electric Power Act 1949*, the additional depreciation charge resulting from the asset revaluation cannot be included in determining the net cost of production.

SNOWY MOUNTAINS HYDRO–ELECTRIC AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*	*1999-00*
Size						
Total assets	$M	3 605	3 423	3 346	3 241	3 161
Total revenue	$M	171	171	156	138	141
Profitability						
Operating profit before tax (includes abnormals)	$'000	-80 276	-79 402	-80 138	-78 783	-79 728
Operating sales margin	%	-0.7	-1.7	-1.6	-8.7	-12.0
Cost recovery	%	99.3	98.3	98.4	92.0	89.3
Return on assets	%	0.3	0.3	0.1	-0.2	-0.4
Return on equity	%	-3.1	-3.2	-3.3	-3.4	-3.5
Financial management						
Debt to equity	%	38.6	38.2	39.6	39.7	41.2
Debt to total assets	%	26.7	26.6	27.7	27.6	28.4
Total liabilities to equity	%	42.8	39.9	41.4	41.7	43.2
Interest cover	times	0.1	0.1	0	-0.1	-0.2
Current ratio	%	9.2	43.0	19.7	36.5	63.8
Leverage ratio	%	142.8	139.9	141.4	141.7	141.7
Payments to and from government						
Dividends	$'000	n.r.	n.r.	n.r.	n.r.	n.r.
Dividend to equity ratio	%	n.r.	n.r.	n.r.	n.r.	n.r.
Dividend payout ratio	%	n.r.	n.r.	n.r.	n.r.	n.r.
Income tax expense	$'000	n.r.	n.r.	n.r.	n.r.	n.r.
CSO funding	$'000	n.r.	n.r.	n.r.	n.r.	n.r.

n.r. Not relevant.

3 Water, sewerage, drainage and irrigation

The financial performance of 14 water, sewerage, drainage and irrigation (referred to hereafter as water) government trading enterprises (GTEs) is discussed in this chapter. At the end of 1999-00, these enterprises generated over $4.9 billion in revenue and controlled assets valued at $38 billion.

Service providers include government departments, statutory corporations and local governments. They undertake a variety of activities, including water treatment, bulk water supply, reticulation and retail supply, sewage collection and treatment, drainage and irrigation.

It should be noted, however, that this study only covers a limited number of water service providers. In most cases, it does not include water services provided by non-metropolitan urban water authorities, regional water authorities and local governments.

For a discussion of the data and the performance indicators used and some of the factors that should be considered when assessing performance see chapter 1.

3.1 Sector reforms

Reforms within the water industry 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 to bring this framework within the ambit of the National Competition Policy (NCP) process in April 1995. Under the framework, governments are to introduce:

- consumption-based two-part tariffs, full cost recovery, and 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.

Almost all jurisdictions have implemented two-part tariffs for water and sewerage services and removed many cross-subsidies between customer classes. However, Western Australia, South Australia and Tasmania mostly retain property-based charges for sewerage services.

Nearly two thirds of the studied GTEs did not receive explicit funding for CSOs. In particular, some Tasmanian and Victorian GTEs did not report CSO payments. However, funding for non-commercial activities is provided for in Victoria through an existing water and sewerage concessions or grants regime.

Regulatory, standard setting and resource management functions have been removed from service providers in most jurisdictions. The establishment of the Sydney Catchment Authority, which began operations in 1999, is an example of the separation of resource management from water provision.

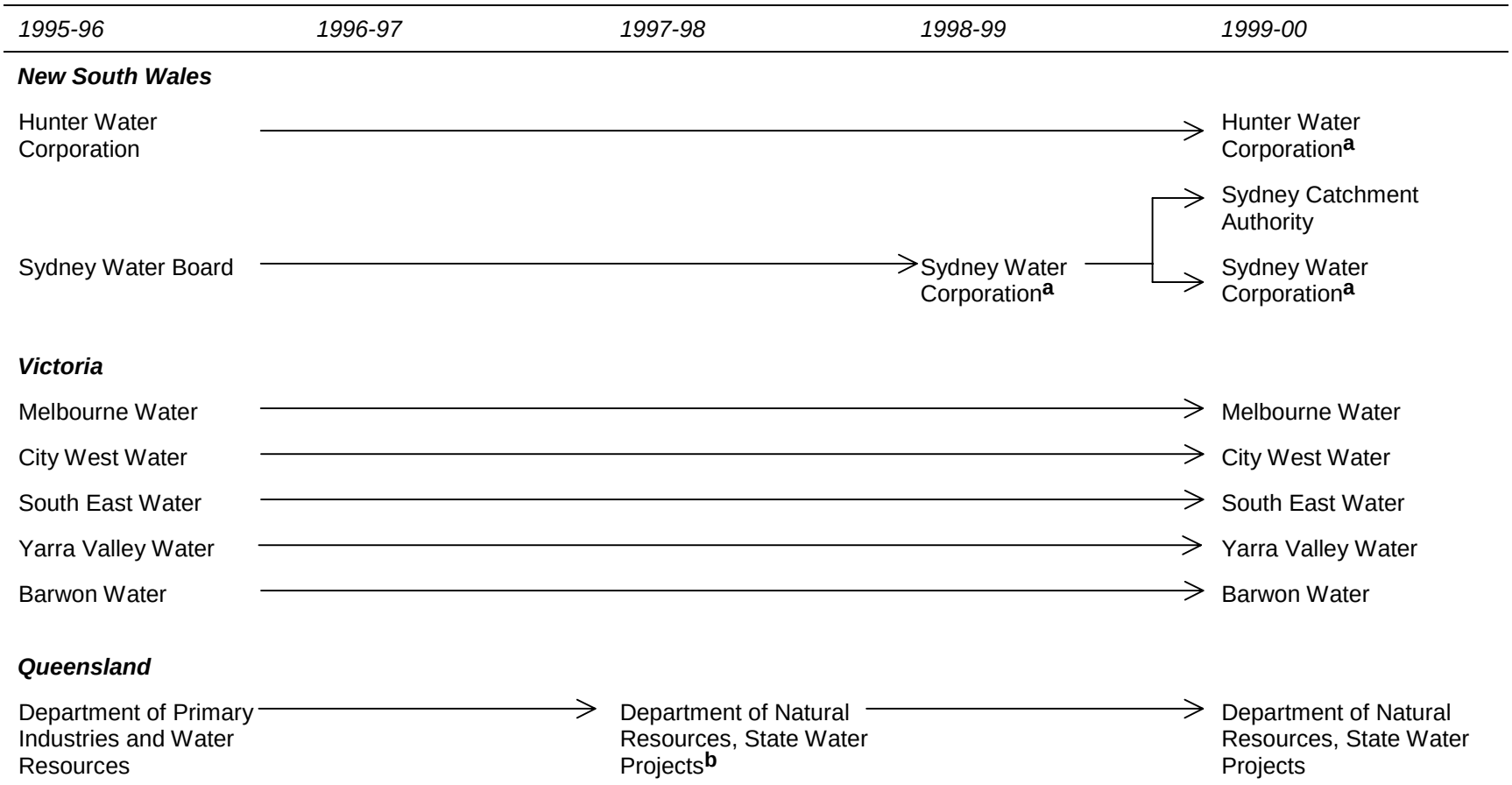
The Authority arose out of the review of the 1998 Sydney incidents concerning the detection of the parasites *Cryptosporidium* and *Giardia* in drinking water. The Authority was made responsible for the management and protection of Sydney's water supply catchments, dams, raw water transfer pipelines and canals, and associated infrastructure. These assets, valued at $647 million, were transferred from the Sydney Water Corporation to the Authority.

The COAG water industry reform is not the only path taken to improve the efficiency and financial performance of water GTEs. There have also been changes in governance arrangements and the structure of some GTEs.

Some activities have been privatised. For example, in 1996 the South Australia Government contracted out the management and operation of the water supply for the Adelaide metropolitan area to a private company. In contrast, Sydney Water and Hunter Water (NSW), changed their status from company to statutory government-owned corporations on 1 January 1999 — to give the responsible Minister greater power to access information and issue directions to the corporations (see table 3.1).

Some GTEs have been disaggregated into separate businesses. For example, the Melbourne Water Corporation was disaggregated into four separate government-owned enterprises on 1 January 1995 — a bulk water wholesaler and three water retail companies.

Table 3.1 **Monitored Water GTEs, 1995-96 to 1999-00**



a Changed from a company to a statutory government-owned corporation. **b** Fully commercialised on 1 July 1997.

Table 3.1 (continued) **Monitored Water GTEs, 1995-96 to 1999-00**

1995-96	*1996-97*	*1997-98*	*1998-99*	*1999-00*
Western Australia				
The Water Corporation[c]	→	→	→	The Water Corporation
South Australia				
South Australian Water Corporation	→	→	→	South Australian Water Corporation
Tasmania				
Hobart Regional Water Board	→	→	→	Hobart Regional Water Authority
Rivers and Water Supply Commission, North Esk	→	Esk Water Authority[d]	→	Esk Water Authority
North West Regional Water Authority	→	→	→	North West Water Authority[e]

[c] Previously the Water Authority of Western Australia. [d] Control and ownership transferred to local governments' joint venture. Assets from the North Esk Scheme, West Tamar Scheme and Launceston City Council were amalgamated to form the Esk Water Authority. [e] North West Regional Water Authority established on 10 August 1999 as a local government Joint Authority, North West Water Authority.

3.2 Market environment

A number of factors influence the market environment that water GTEs operate in. In particular, the demand and supply for water and the consequent revenue for GTEs is greatly affected by weather conditions. For example, following a dry summer, Sydney Water supplied 2 404 million litres per day in March 1998 compared to 1 700 million litres per day at the same time in 1997. In addition, water restrictions may have to be imposed in unusually dry weather, to the detriment of revenue.

The introduction of two-part tariffs has increased revenue volatility. When revenue was raised through property-based charges, the revenue stream was more stable and predictable unless there was a major change in property values. With the recent increased reliance on user based charges, revenue depends on the level of demand and is therefore less stable. However, usage charges provide an incentive to consumers to manage their demand.

Revenue volatility is also affected by the inclusion of developer and customer contributions as revenue.[1] During 1999-00, the building sector experienced considerable growth. The value of work done on new residential buildings rose by 20 per cent compared to the previous year (ABS 2001). As a result of this increased activity, area contributions and gifted assets grew by over 35 per cent.

For some of the monitored GTEs, the proportion of total revenue resulting from area contributions and gifted assets has also increased. For example, Melbourne Water developer charges and contributions accounted for nearly 10 per cent of total revenue in 1999-00 compared to just over 4 per cent of total revenue in 1998-99.

Water GTEs are usually required to strike a balance between consumptive and environmental needs in generating an acceptable return to shareholder governments. The amount of water that GTEs can draw from their surface and groundwater sources is usually limited for environmental reasons. For example, the Water Corporation of Western Australia holds a water allocation licence, issued by the Water and Rivers Commission, which specifies the amount of water the Corporation can draw from its surface and ground water sources.

Economic regulation of prices can also influence the market environment in which water GTEs operate. In most jurisdictions, the government or an independent pricing body regulates water prices. For example, in NSW the Independent Pricing

1 Developer and customer contributions entail the transfer of monetary or non-monetary assets to GTEs. GTEs may require customers and developers to contribute capital to finance new infrastructure. Alternatively, GTEs may require developers to construct or install infrastructure assets. Ownership of such assets is transferred to the responsible GTE at no cost.

and Regulatory Tribunal is responsible for determining prices for major urban centres and for rural bulk water provision. In September 2000, the tribunal issued the medium term price path for the Sydney Catchment Authority, to extend from 2000-01 to 2004-05.[2]

3.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings. For a more detailed discussion of profitability indicators see chapter 1.

The water industry is diverse. Some GTEs undertake a range of activities like bulk water provision, reticulation, sewerage and drainage, (for example Hunter Water). Others, such as State Water Projects (Queensland) undertake only one activity (primarily focused on the provision of bulk and raw water). This diversity in activities affects costs and the scope to recover costs in the transition to full commercialisation. Accordingly, it can also affect the comparability of financial performance.

The accounting treatment of contributed assets can have a material effect on profitability and asset and liability recognition. Almost all GTEs indicate that they are following Urgent Issue Group (UIG) Consensus Views, Abstract 11, 'Accounting for contributions of, or contributions for the acquisition of, non-current assets' and Abstract 17, 'Developer and customer contributions in price regulated industries' to recognise contributed assets.[3]

The Productivity Commission's treatment of contributed assets has changed over the reporting period. Therefore, it should be noted that the impact of these assets on profitability ratios such as return on assets has changed after 1997-98.

The profitability of most water GTEs has improved over the reporting period. Total industry operating profit before tax (including abnormals) had an average annual growth rate of 25 per cent. Operating profit is influenced by the combination of prices, business volumes and expenses. The impact of these factors varied among GTEs.

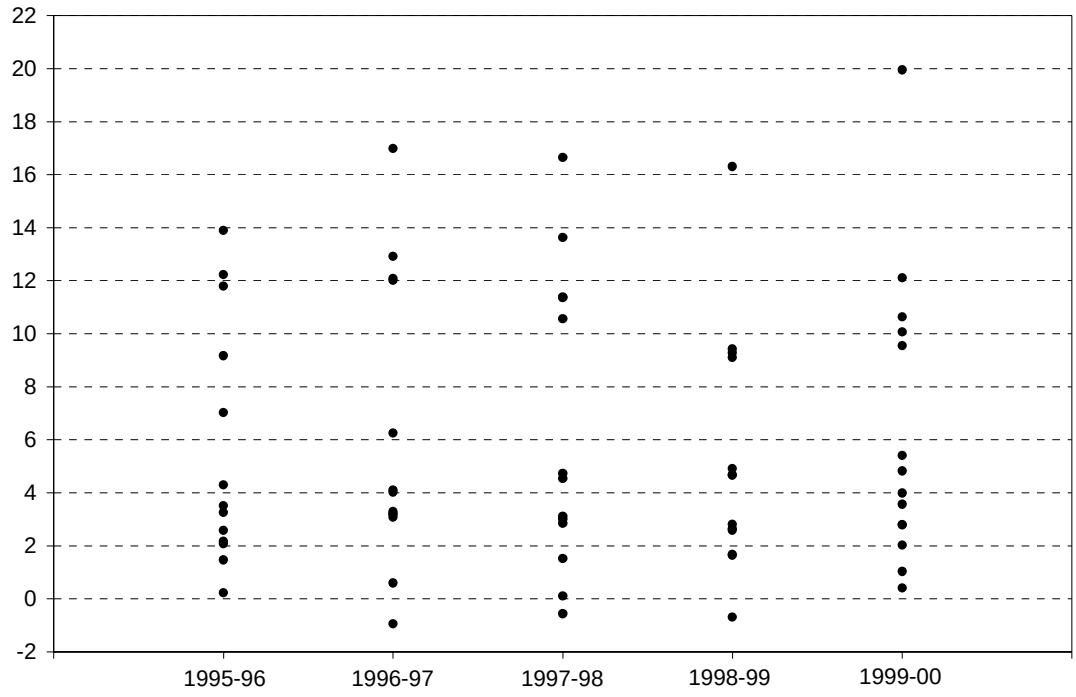
The increase in profitability of water GTEs has contributed to an improved return on assets. In 1999-00, the industry rate of return was 5.5 per cent compared to the

2 The Authority's charges to Sydney Water will be maintained in real terms at the 1999-00 level.

3 The Australian Accounting Research Foundation issues UIG Consensus Views as Abstracts to assist in the interpretation of an existing Accounting Standard or guidance in the absence of a standard.

previous year's average of 4.2 per cent. However, with the exception of Victorian GTEs, most have a rate of return less than 6 per cent (see figure 3.1), which is below the long-term bond rate.[4] In addition, all GTEs, excluding those in Victoria and the Sydney Catchment Authority, recorded a rate of return below that achieved by the water supply and sanitary services sector of the United States (5.7 per cent in 1999-00) (Troy 2000).

Figure 3.1 **Return on assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the return on assets ratio for a GTE in that financial year. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue (including abnormals) and adding back gross interest expense. The average value of assets at the beginning and end of the reporting period was used.

The return on assets is also affected by asset valuations. For example, the value of the State Water Projects (Qld) assets decreased by almost 90 per cent in 1999-00, as a result of the revaluation of non-current physical assets and a move from deprival valuation methodology to fair value methodology. Subsequently, return on assets and return on equity improved.

Another ratio used to measure profitability is return on equity — the rate of earnings on capital provided by shareholder governments. Over the reporting period the return on equity for most water GTEs improved. Return on equity is affected by debt restructuring and operating profits. For example, return on equity for the Water

4 The rate of return on 10 year bonds at June 2000 was 6.6 per cent.

Corporation of Western Australia's increased from 0.3 per cent in 1995-96 to 4.5 per cent in 1999-00 as operating profit increased and interest expenses reduced.

The cost recovery ratio indicates a GTE's ability to generate adequate revenue to cover expenses. High levels of cost recovery can be expected from highly capital intensive industries because of the need to meet expenses associated with maintaining and replacing capital.

With the exception of State Water Projects (Qld), all GTEs achieved cost recovery ratios between 100 and 250 per cent, over the reporting period. State Water Projects (Qld) has generally been unable to achieve a cost recovery ratio of 100 per cent, despite receiving CSO payments to cover the costs of operation, maintenance and administration (see figure 3.2). On the other hand, Melbourne Water has maintained a cost recovery ratio of over 200 per cent.

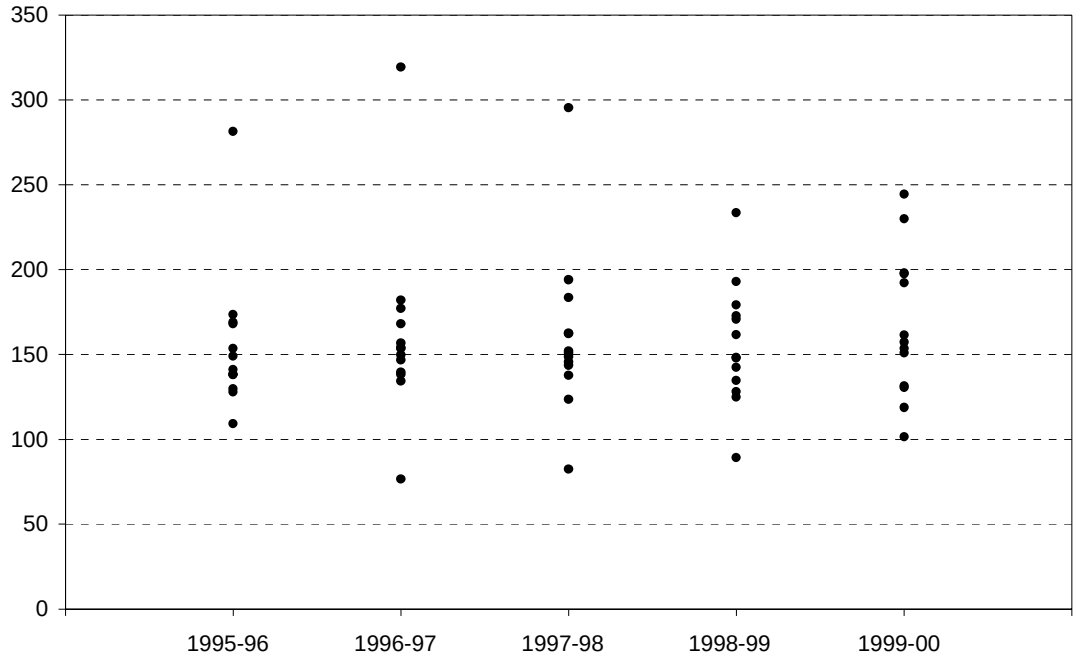
3.4 Financial management

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. For a more detailed discussion of financial management indicators see chapter 1.

Many water GTEs have undergone financial restructuring as part of the reform process. This has largely involved debt for equity swaps, debt repayments and debt novation.[5] The main aim of financial restructuring has been to establish a capital structure that is commercially viable.

5 Novation is the substitution of a new obligation for an old one. Usually it involves the substitution of a new debtor or a new creditor.

Figure 3.2 **Cost recovery, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting abnormal revenue, investment income and receipts from governments to cover deficits on operations from total revenue. Expenses from operations are calculated by subtracting abnormal expenses and gross interest expense from total expenses.

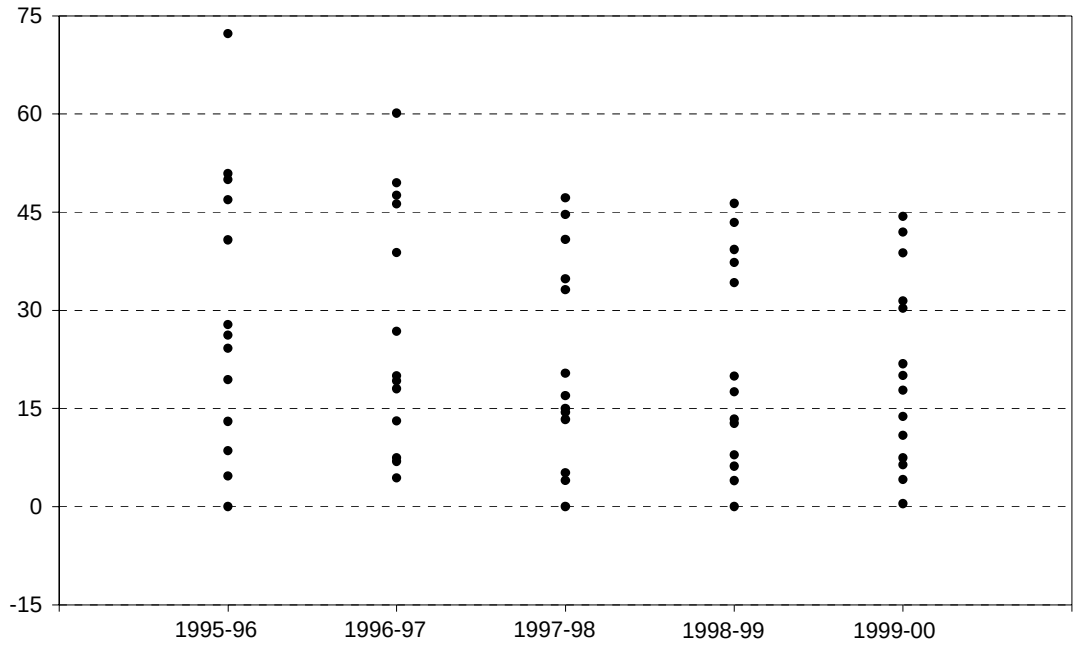
The magnitude of debt restructuring has typically depended on the GTE's initial capital structure. For example, the Barwon Region Water Authority's capital structure was changed in 1998-99 to lower borrowing costs and reduce exposure to interest rate fluctuations. The Authority undertook novation of its debt portfolio to the Treasury Corporation of Victoria (TCV).[6]

Overall, debt levels have declined over the period and as a result financial management ratios have improved. At the end of 1999-00 most GTEs have debt to total assets of below 25 per cent (see figure 3.3).

Between 1995-96 and 1996-97 there were four GTEs with debt to total assets above 45 per cent. These included Melbourne Water and the three retail GTEs in Victoria. From 1997-98, their debt to total asset ratios fell as a result of capital restructuring introduced by the Victorian Government as part of a $850 million financial reform package, which included a debt for equity swap. However, they continue to have debt to total asset ratios above the other monitored water GTEs.

6 The novation of debt to the TCV included 1 635 inscribed stockholders ($14.5 million) and three institutional investors ($15.5 million).

Figure 3.3 **Debt to total assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the debt to total assets ratio for a GTE in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period).

With the exception of the Victorian GTEs, the debt to equity ratio for most GTEs has been less than 50 per cent. The Melbourne Water Corporation had the highest debt to equity ratio — 452.5 per cent in 1995-96. This has subsequently declined over the reporting period to 106.5 per cent, following two debt for equity swaps in 1996-97 and 1997-98 respectively.

Most GTEs have current ratios below 100 per cent indicating that it would be difficult to meet short-term liabilities by realising short-term assets. Water GTEs have become less liquid over the reporting period. For example, from 1998-99 the Western Australian Water Corporation current ratio has fallen to below 50 per cent. The decline in the Corporation's current ratio is attributable to increased current liabilities, such as tax-equivalent payments.

Over the reporting period most GTEs have been able to maintain an interest cover in excess of 2 times and a growing number have achieved greater than 3 times. In 1999-00, the rate for water utilities in the United States was 1.5 times while in Australia the average was 4.8 times. High interest cover ratios indicate that an entity can sustain a fall in profit or increased interest expense and still meet the cost of

servicing debt. In most cases, improvements in interest cover over the reporting period have resulted from debt restructuring or increased operating profits.

3.5 Financial transactions

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 incentives and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles see chapter 1.

The timing of the introduction of tax-equivalent regimes has varied across jurisdictions. However, by the end of the reporting period all water GTEs, with the exception of Barwon Water, were required to make tax-equivalent payments.[7]

Income tax expense decreased in 1999-00 as a result of a reduction in the future company tax rate.[8] Before 1999-00, tax-equivalent payments were based on a company tax rate of 36 per cent. Due to timing differences and the adoption of tax-effect accounting, tax expense incurred in any given year may differ from the actual amount of tax payable. Changes in the future company tax rate, effective from 2000-01 led to a restatement of deferred tax liabilities in 1999-00. Across the sector, this adjustment led to a revaluation in tax-equivalent payments of around $150 million.

Dividends represent a return to shareholder government equity. Almost all the monitored water GTEs are required to make dividend payments. The amount payable by each depends on the dividend policy of their State government. In 1999-00, most GTEs dividend payout ratios — the proportion of operating profit that is paid or provided for as dividend — were between 50 per cent and 100 per cent.

One of the requirements of the COAG reforms is the disclosure of the costs of providing water services at less than full cost recovery and the compensation of these costs as CSO payments. This achieves transparency in CSO funding and removes the conflict between non-commercial objectives and cost recovery. Some examples of CSOs are concessions, sewer backlog programs and free provision of water for fire-fighting purposes.

---

7 Barwon Water as a Victorian non-metropolitan authority is not subject to a tax-equivalent regime.

8 The future company tax rate will fall from 36 per cent in 1999-00 to 34 per cent for 2000-01 and then to 30 per cent from 2001-02.

Most jurisdictions have CSO agreements. Two jurisdictions in which some GTEs do not receive CSO payments are Tasmania and Victoria. However, funding for non-commercial activities is provided for in Victoria through existing water and sewerage concessions or grants.[9]

9 The Victorian Government maintains a system whereby water companies and authorities deliver concessions to eligible customers on behalf of the Government and are then reimbursed for the cost of the concessions by the Department of Human Services. In 1998-99, City West Water, Yarra Valley Water and South East Water delivered concessions worth $41.1 million and 1 105 emergency relief grants valued at $380 500. Non-metropolitan GTEs delivered concessions worth $16.3 million and 781 emergency relief grants valued at $248 400. The arrangement for delivery of these payments is under review.

3.6 GTE performance reports

Sydney Catchment Authority (NSW)
Sydney Water Corporation (NSW)
Hunter Water Corporation (NSW)
Melbourne Water Corporation (Vic)
City West Water (Vic)
South East Water (Vic)
Yarra Valley Water (Vic)
Barwon Water (Vic)
Department of Natural Resources, State Water Projects (Qld)
South Australian Water Corporation (SA)
Water Corporation (WA)
Hobart Regional Water Authority (Tas)
North West Water Authority (Tas)
Esk Water Authority (Tas)

SYDNEY CATCHMENT AUTHORITY — New South Wales

The Sydney Catchment Authority (SCA) is a statutory body set up by the NSW Government to manage and protect Sydney's water supply catchments, dams, raw water transfer pipelines and canals, and associated infrastructure. In addition the SCA supplies bulk water to Sydney Water Corporation and local government areas outside the Sydney distribution system. The *Sydney Water Catchment Management Act 1998* and the *Sydney Catchment Authority Operating Licence* govern the SCA's activities. The SCA began operations in July 1999.

The SCA was created on the recommendation of an independent inquiry, headed by Peter McClellan QC, into the 1998 Sydney water quality incidents. The incidents refer to the detection of the parasites *Cryptosporidium* and *Giardia* in drinking water.

Responsibility for managing catchments, dams and their associated infrastructure were transferred from Sydney Water to the SCA. There was a transfer of $492 million in net assets, the largest items being $619 million in system assets, property and equipment and $162 million in debt.

The SCA has the ability to exercise concurrence and compliance functions in relation to certain types of proposed development. It can also exercise these functions under the legislation of other agencies. For example, the SCA is required to assess certain types of new development to determine whether they have a neutral or beneficial effect on water quality in the catchment.

The SCA's taxation liability is assessed according to the tax-equivalent regime of the NSW Treasury and income tax payments are directed to the NSW Government.

The SCA is required to make dividend payments to the State Government. The SCA does undertake non-commercial activities but the provision and funding of community service obligations are not explicitly reported in the financial statements.[1]

1 Examples of non-commercial activities include the provision of monetary or in-kind grants to groups such as National Trust and Landcare for catchment protection and improvement projects.

SYDNEY CATCHMENT AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*	*1999-00*[a]
Size						
Total assets	$M	n.r	n.r	n.r	n.r	736
Total revenue	$M	n.r	n.r	n.r	n.r	123
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r	n.r	n.r	n.r	59 880
Operating sales margin	%	n.r	n.r	n.r	n.r	56.5
Cost recovery	%	n.r	n.r	n.r	n.r	230.0
Return on assets	%	n.r	n.r	n.r	n.r	9.5
Return on equity	%	n.r	n.r	n.r	n.r	7.5
Financial management						
Debt to equity	%	n.r	n.r	n.r	n.r	30.9
Debt to total assets	%	n.r	n.r	n.r	n.r	21.8
Total liabilities to equity	%	n.r	n.r	n.r	n.r	41.5
Interest cover	times	n.r	n.r	n.r	n.r	7.2
Current ratio	%	n.r	n.r	n.r	n.r	92.7
Leverage ratio	%	n.r	n.r	n.r	n.r	141.5
Payments to and from government						
Dividends	$'000	n.r	n.r	n.r	n.r	10 600
Dividend to equity ratio	%	n.r	n.r	n.r	n.r	2.0
Dividend payout ratio	%	n.r	n.r	n.r	n.r	27.3
Income tax expense	$'000	n.r	n.r	n.r	n.r	21 100
CSO funding	$'000	n.r	n.r	n.r	n.r	0

a The *Sydney Water Catchment Management Act 1998* received assent on 14 December 1998. On 2 July 1999 the SCA commenced operations. On this date $491.6 million in net assets where transferred from Sydney Water to the Authority. **n.r**. not relevant.

SYDNEY WATER CORPORATION — New South Wales

The Sydney Water Corporation (SWC) was corporatised on 1 January 1999 following the enactment of the *Water Legislation Amendment (Drinking Water and Corporate Structure) Act 1998*. The SWC supplies drinking water and provides wastewater services and some stormwater services to the people of Sydney, the Blue Mountains and Illawarra. It serves more than 3.9 million customers.

The variability in SWC's operating profit before tax (including abnormals) is largely the result of abnormal items. The increase in the SWC's operating profit in 1997-98, resulted from increased water consumption caused by dry weather, abnormal revenue ($41.6 million) and reduced operating costs. Operating profit in 1998-99 was significantly affected by water contamination incidents, which resulted in an abnormal expense of $55.4 million and $19.2 million in forgone revenue.[1] Operating profit in 1999-00 grew as a result of increased contributions for capital works by developers and net abnormal revenue of $52.5 million arising from adjustments to superannuation expense.[2]

Following the water incidents, the Sydney Catchment Authority (SCA) was established in December 1998 and commenced operations in July 1999. The staff, assets, rights and liabilities relating to catchment management were transferred from the SWC to the SCA.[3]

Return on asset and return on equity declined in 1998-99. This reflects the impact of a pricing reform package introducing a $20 million and $40 million property tax reduction on customer's bills in 1997-98 and 1998-99 respectively.

SWC is required to makes tax-equivalent and dividend payments.[4] It receives funding for the provision of community service obligations.

---

1 The abnormal expense included a $15 rebate to affected customers ($19.2 million), outstanding and paid insurance claims ($14 million), monitoring and testing costs ($12.5 million), other costs ($7.7 million) and costs associated with the McClellan Inquiry ($2 million). The foregone revenue resulted from a decision to defer a price increase for a period of 12 months.

2 This abnormal reflects an increase in the SWC's superannuation stakeholding, resulting from the allocation of superannuation credits for past years, exceptional interest earnings and a large reduction in the SWC's superannuation liability.

3 The assets included catchments, dams and bulk water pipelines and resulted in a transfer of net assets worth $492 million.

4 SWC is required over a three year period commencing 1997-98, to pay 100 per cent of its profit after tax and developer contributions as a dividend to the NSW Government.

SYDNEY WATER CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*	*1998-99*[b]	*1999-00*
Size						
Total assets	$M	13 294	13 416	14 061	13 278	13 053
Total revenue	$M	1 168	1 283	1 372	1 377	1 467
Profitability						
Operating profit before tax (includes abnormals)	$'000	160 665	237 133	369 634	233 737	385 296
Operating sales margin	%	26.8	30.3	37.7	28.5	35.3
Cost recovery	%	138.3	138.3	153.6	145.3	153.4
Return on assets	%	2.6	3.2	4.0	3.0	4.0
Return on equity	%	0.6	1.3	2.2	1.4	3.0
Financial management						
Debt to equity	%	16.1	16.0	15.8	16.9	17.0
Debt to total assets	%	13.0	13.1	13.3	13.3	13.8
Total liabilities to equity	%	22.9	23.0	21.7	22.8	22.6
Interest cover	times	1.9	2.3	3.1	2.3	3.8
Current ratio	%	61.5	55.6	60.2	24.5	41.0
Leverage ratio	%	122.9	123.0	121.7	122.8	122.6
Payments to and from government						
Dividends	$'000	40 000	77 646	209 000	91 683	12 9271
Dividend to equity ratio	%	0.4	0.7	1.9	0.8	1.2
Dividend payout ratio	%	59.5	56.2	86.0	60.1	40.3
Income tax expense	$'000	93 402	98 966	126 533	81 160	64 253[c]
CSO funding	$'000	82 000	93 800	89 700	105 200	87 686

a The Sydney Water Corporation (SWC) abolished property tax to the residential sector from October 1995. **b** SWC recorded an abnormal expense of $55.4 million due to the water contamination incidents that occurred in July, August and September 1998. SWC was established as a statutory government-owned corporation on 1 January 1999. The Sydney Catchment Authority (SCA) was established in December 1998 following the enactment of the *Sydney Water Catchment Management Act 1998*. The SCA commenced operations in July 1999. The SCA was formed to improve the catchment management process and thereby drinking water quality. SWC is required over a three year period commencing 1997-98, to pay 100 per cent of its profit after tax and developer contributions as a dividend to the NSW Government. In 1998-99, the dividend declared excludes capital contributions in respect of the Rouse Hill Development and social program sewer backlog projects. **c** Income tax expense decreased due to a reduction in the future company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from the 2001-02. Consequently, deferred tax balances have been remeasured using the appropriate new rates.

HUNTER WATER CORPORATION — New South Wales

Hunter Water Corporation (HWC) was corporatised on 1 January 1999 following the enactment of the *Water Legislation Amendment (Drinking Water and Corporate Structure) Act 1998.*[1] The HWC provides water, wastewater and drainage services to a population of almost half a million people from five councils. These include Newcastle, Lake Macquarie, Maitland, Cessnock and Port Stephens. In November 1997, HWC created a wholly owned and controlled entity known as Hunter Water Australia Pty Ltd.[2]

From 1996-97 to 1999-00 total revenue decreased. One of the main factors contributing to this decrease is the Independent Pricing and Regulatory Tribunal 1996–2000 price determination for HWC, which applied a CPI-X pricing regime. Consequently prices for water and sewerage have been adjusted each year by 2 per cent less than inflation. Consistent rainfall contributed to the reduction in total revenue during 1999-00.

The decline in total assets during 1999-00 reflects a write-down in the valuation of property, plant and equipment. A Recoverable Amount Test determined that a shortfall existed between the net present value of future cash flows and accounting book value of the asset base, resulting in a $105.4 million write-down of assets.

HWC is required to make tax-equivalent and dividend payments. Community service obligations (CSOs) provided by HWC are funded by the NSW Government and reported explicitly in the financial statements. CSO payments for 1999-00 were for tariff rebates granted to pensioners and exempt properties such as churches.

1 This amendment changed the status of the HWC from a company to a statutory government-owned corporation, and gives the Minister responsible for Hunter Water greater power to access information.

2 Hunter Water Australia Pty Ltd's core services involve water treatment, engineering, surveying, laboratory services and selling their expertise to the external market. The Hunter Water Australia's financial results are incorporated with those of the HWC.

HUNTER WATER CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	1 972	2 027	2 038	2 064	1 970
Total revenue	$M	129	154	148	139	136
Profitability						
Operating profit before tax (includes abnormals)	$'000	32 891	54 207	56 205	50 548	50 123
Operating sales margin	%	27.7	37.3	40.5	39.0	39.5
Cost recovery	%	138.3	139.6	162.2	161.6	150.8
Return on assets	%	2.2	3.1	3.1	2.8	2.8
Return on equity	%	1.0	2.3	2.6	1.7	1.9
Financial management						
Debt to equity	%	4.8	4.8	4.4	4.3	4.6
Debt to total assets	%	4.7	4.4	4.0	4.0	4.1
Total liabilities to equity	%	10.2	10.4	9.5	9.9	8.9
Interest cover	times	6.0	8.5	8.8	8.2	9.0
Current ratio	%	192.7	187.4	151.1	91.5	107.7
Leverage ratio	%	110.2	110.4	109.5	109.9	108.9
Payments to and from government						
Dividends	$'000	29 600	35 500	39 000	45 000	28 000
Dividend to equity ratio	%	1.8	2.0	2.1	2.4	1.5
Dividend payout ratio	%	177.6	83.5	80.0	144.0	80.1
Income tax expense	$'000	16 226	11 670	7 471	19 295	15 185
CSO funding	$'000	8 000	8 100	8 300	8 200	8 277

a Variable rate debt of $20 million was converted to long-term fixed rate debt and consolidated from 13 loans into 7. **b** Hunter Water created a wholly owned and controlled entity, Hunter Water Australia Pty Ltd, in November 1997, which commenced operations on 1 January 1999. The core services of the subsidiary include water treatment, civil engineering, surveying, laboratory services and selling services to external markets. In 1996-97, Hunter Water adopted the Urgent Issues Group (UIG) Abstract 11 to recognise as income and assets the value of contributions received from developers. In 1997-98, Hunter Water adopted UIG Abstract 17, which states that these assets should be recognised at their assessed fair value. **c** On 1 January 1999, legislation came into effect that changed Hunter Water's status from a company to a statutory government-owned corporation. **d** Revenue for 1999-00 includes contributions for capital works and abnormal revenue of $11.6 million resulting from a reduction in superannuation liability.

MELBOURNE WATER CORPORATION Victoria

Melbourne Water Corporation (MWC) was separated into three retail water GTEs (City West Water, Yarra Valley Water and South East Water) and a wholesale water and sewerage business in January 1995.[1] MWC supplies water and sewerage services to the retail water GTEs through separate bulk water and sewerage supply agreements. It also provides waterways and drainage services.

MWC's total revenue, operating profit before tax (including abnormals), return on total assets and return on equity declined from 1996-97 to 1998-99. The decline in 1996-97 to 1997-98 was mainly due to the implementation of the Victorian Government's pricing reform package on 1 January 1998, which reduced MWC's bulk water charges to the retail water GTEs.[2]

This trend was reversed in 1999-00. Revenue grew by 7.6 per cent as a result of growth in development and high bulk water sales due to continuing dry weather conditions. Consequently operating profit, return on assets and return on equity increased.

MWC's debt to equity, debt to total asset and total liabilities to equity ratios declined significantly from 1995-96 to 1996-97 and have continued to improve over the reporting period. The significant decline from 1995-96 to 1996-97 was due to a debt for equity swap with the Victorian Government amounting to $250 million. In 1998-99, the debt for equity swap involved the transfer of $337 million of debt for an equivalent increase in equity.[3] A growth in total assets of 3.7 per cent and decreasing debt are mainly responsible for the decline in the debt to equity and debt to assets ratio in 1999-00.[4]

Dividend payments increased in 1999-00 as a result of increased revenue. Income tax expense decreased markedly during 1999-00 as a consequence of reduced future company tax rate and deferred tax balances, which are expected to reverse in 2000-01. MWC is not subject to community service obligations.

---

1 The trading activities of MWC are dependent to a significant extent on the sale of bulk water and sewerage services to the three retail water companies. MWC also depends on the three retail companies for the provision of billing and collection services with respect to drainage rates.

2 A usage-based billing system for retail water and sewerage services was introduced under the pricing reforms.

3 The debt reduction in 1996-97 was aimed at making MWC's debt ratios commercially acceptable. In 1997-98 capital restructuring was part of the pricing reform package.

4 Assets grew due to $105.2 million in capital works projects.

MELBOURNE WATER CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*	*1999-00*
Size						
Total assets	$M	2 731	2 714	2 721	2 751	2 852
Total revenue	$M	687	680	560	443	477
Profitability						
Operating profit before tax (includes abnormals)	$'000	146 469	263 397	254 334	176 664	204 234
Operating sales margin	%	54.9	68.0	66.1	57.2	59.1
Cost recovery	%	281.4	319.3	295.4	233.5	244.5
Return on assets	%	13.9	17.0	13.6	9.3	10.1
Return on equity	%	29.6	29.5	19.7	11.6	17.7
Financial management						
Debt to equity	%	452.5	235.5	121.2	119.4	106.5
Debt to total assets	%	72.3	60.1	47.2	46.3	44.4
Total liabilities to equity	%	530.0	290.7	157.3	159.1	144.4
Interest cover	times	1.6	2.3	3.2	3.3	3.6
Current ratio	%	7.9	10.1	12.1	8.4	10.3
Leverage ratio	%	630.0	390.7	257.3	259.1	244.4
Payments to and from government						
Dividends	$'000	80 000	141 315	141 149	106 175	126 246
Dividend to equity ratio	%	19.5	25.1	16.1	10.0	11.3
Dividend payout ratio	%	65.7	84.9	81.8	86.6	64.1
Income tax expense	$'000	24 639	96 977	81 875	54 090	7 348[c]
CSO funding	$'000	0	0	0	0	0

a Crown land valued at $13.8 million was divested from the Melbourne Water Corporation (MWC). Debt for equity swap with the Victorian Government amounting to $250 million. **b** Implemented Victorian Government pricing reform package. This resulted in the reduction of MWC's bulk water charges to the three retail water GTEs (City West Water, Yarra Valley Water and South East Water). Debt restructuring was part of this package and MWC swapped its debt for equity with the Victorian Government amounting to $337 million. **c** Income tax expense decreased due to a reduction in the future company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from 2001-02. Consequently, deferred tax balances have been remeasured using the appropriate new rates.

CITY WEST WATER — Victoria

City West Water commenced operations on 1 January 1995. Its operating licence was issued under the *Water Industry Act 1994*. City West Water provides water, sewerage and trade waste services to approximately 257 000 residential, commercial and industrial properties in Melbourne's central business district, and its inner and western suburbs.

City West Water implemented the pricing reform package announced by the Victorian Government in October 1997, which involved a move from a rate-based to a usage-based system of billing. This reduced operating revenue, recurrent cashflow and increased the exposure of revenue to weather conditions.

Operating profit before tax (including abnormals) increased in 1997-98, even though revenue declined. This was mainly due to lower bulk supply charges from the Melbourne Water Corporation, lower financial charges through debt restructuring and cessation of subsidy payments to South East Water and Yarra Valley Water.[1] The sharp increase in operating profit in 1999-00 is primarily the result of a $19.9 million growth in area contributions and gifted assets from developers.

City West Water's debt to equity, debt to total asset and leverage ratios declined from 1996-97 to 1997-98 due to a debt for equity swap, involving the issue of fully paid ordinary shares amounting to $20.6 million.[2] These ratios further declined in 1999-00 with a reduction in debt of $29.3 million. Interest cover has increased as a result of debt reduction.

City West Water is required to make tax-equivalent and dividend payments.[3] Income tax expense decreased in 1999-00 due to a reduction of the future company tax rate and deferred tax balances. City West Water is not subject to community service obligations (CSOs).[4]

---

1 The subsidy was provided to ensure that the three retail water GTEs operated on an equal footing in terms of return on assets. The subsidy payments ceased with the implementation of Victorian Government's pricing reform package.

2 Debt restructuring was part of the Victorian Government's pricing reform package that was implemented on 1 January 1998.

3 City West Water negotiates dividend payments each year with the Victorian Government based on its earnings and cash requirements.

4 The model of CSO agreements has not been applied to Victorian water GTEs. As such City West Water has no CSO, despite being required to engage in non-commercial activities such as the delivery of water and sewerage concessions and grants.

CITY WEST WATER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*[b]	*1999-00*
Size						
Total assets	$M	516	542	577	606	625
Total revenue	$M	294	301	270	228	255
Profitability						
Operating profit before tax (includes abnormals)	$'000	32 356	39 474	76 538	83 495	110 147
Operating sales margin	%	19.9	20.9	34.2	42.2	48.0
Cost recovery	%	128.0	134.4	152.0	172.9	192.2
Return on assets	%	11.8	12.0	16.6	16.3	19.9
Return on equity	%	12.0	14.3	26.0	26.1	34.0
Financial management						
Debt to equity	%	117.5	111.2	90.8	78.6	57.1
Debt to total assets	%	46.9	46.3	40.8	37.3	30.3
Total liabilities to equity	%	153.5	146.5	129.3	116.0	91.6
Interest cover	times	2.2	2.6	5.6	7.4	9.7
Current ratio	%	40.2	40.2	41.5	26.6	32.7
Leverage ratio	%	253.5	246.5	229.3	216.0	191.6
Payments to and from government						
Dividends	$'000	21 000	27 709	49 148	39 939	57 400
Dividend to equity ratio	%	10.6	13.1	20.8	15.0	18.9
Dividend payout ratio	%	88.1	91.3	80.0	57.5	55.6
Income tax expense	$'000	8 518	9 132	15 108	13 981	6 915[c]
CSO funding	$'000	0	0	0	0	0

a City West Water implemented a price reform package in October 1997 that involved a move from a rate-based to a usage-based system. **b** First full year of operation after the implementation of usage-based billing. The usage-based system changed the timing of cashflow such that customers are now billed in arrears. **c** Income tax expense decreased due to a reduction in the future company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from 2001-02. Consequently, deferred tax balances have been remeasured using the appropriate new rates

SOUTH EAST WATER — Victoria

South East Water (SEW) was incorporated in 1994 and commenced operations as a retail water supply and sewerage service business on 1 January 1995. Its operating licence was issued under the *Water Industry Act 1994*. SEW provides water supply and sewerage services to 1.3 million customers in the south east area of Melbourne.

SEW's cost recovery, return on total assets and return on equity declined from 1996-97 to 1998-99, due mainly to the implementation of the Victorian Government's pricing reform package in the second half of 1997-98. The reform involved a move from rate-based to usage-based billing. With the implementation of the pricing reform, the subsidy received by SEW from City West Water ceased.[1]

Operating profit before tax (including abnormals) increased in 1999-00, due to greater water consumption resulting from continuing dry weather conditions, and a growth in housing development. Higher levels of housing development resulted in an increase in gifted reticulation assets and cash contributions from developers. Higher operating profit has improved the return on assets, return on equity and cost recovery ratios.

The sharp decrease in SEW's debt to equity, debt to total asset and total liability to equity ratios in 1997-98 was the result of debt restructuring associated with the pricing reform package. The financial restructuring involved a debt for equity swap — debt of $160 million for $114.1 million fully paid ordinary shares to the State Trustees Limited on behalf of the State Government — and the establishment of a new portfolio with a more even spread of debt maturity and lower interest costs.

Debt was further reduced in 1999-00 by $20.5 million, resulting in an increase in interest cover.

Since incorporation, SEW has made tax-equivalent and dividend payments. The decrease in income tax expenses during 1999-00 is attributable to the restatement of deferred tax balances resulting from the change in the future company tax rate from 36 per cent to 34 per cent in 2000-01 and 30 per cent thereafter. SEW is not subject to community service obligations (CSO).[2]

1 The Victorian Government's pricing reform package was implemented on 1 January 1998. The purpose of the subsidy was to place the three retail water GTEs on a more equal financial footing.

2 The model of CSO agreements has not been applied to Victorian water GTEs. As such SEW has no CSO, despite being required to engage in non-commercial activities such as the delivery of water and sewerage concessions and grants.

SOUTH EAST WATER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*	*1999-00*
Size						
Total assets	$M	992	997	1 000	1 031	1 048
Total revenue	$M	385	404	371	305	331
Profitability						
Operating profit before tax (includes abnormals)	$'000	64 541	76 802	81 538	76 710	104 883
Operating sales margin	%	30.9	31.8	30.6	31.8	37.9
Cost recovery	%	149.1	153.5	148.6	148.2	161.6
Return on assets	%	12.2	12.9	11.4	9.6	12.1
Return on equity	%	11.4	13.5	14.8	12.6	19.3
Financial management						
Debt to equity	%	141.4	127.3	69.2	67.5	59.5
Debt to total assets	%	50.9	47.6	34.8	34.2	31.4
Total liabilities to equity	%	180.5	168.3	99.2	100.4	90.9
Interest cover	times	2.2	2.5	3.5	4.8	6.0
Current ratio	%	24.5	37.2	58.6	41.7	36.2
Leverage ratio	%	280.5	268.3	199.2	200.4	190.9
Payments to and from government						
Dividends	$'000	51 300	60 000	54 800	49 730	68 175
Dividend to equity ratio	%	14.8	16.5	12.5	9.8	12.8
Dividend payout ratio	%	130.3	122.6	84.5	77.4	66.6
Income tax expense	$'000	25 158	27 865	16 700	12 459	2 488[b]
CSO funding[c]	$'000	0	0	0	0	0

a The Victorian Government's pricing reform package was implemented on 1 January 1998. It involved a move form rate-based to usage-based pricing and included debt restructuring. **b** Income tax expense decreased due to a reduction in the future company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from 2001-02. **c** South East Water is required to provide non-commercial services. However, funding is not explicitly reported in the financial statements.

YARRA VALLEY WATER — Victoria

Yarra Valley Water (YVW) began operating on 1 January 1995. Its operating licence was issued under the *Water Industry Act 1994*. It is a government-owned company whose principal activities are the provision of retail water supply, sewerage services and the collection of tradewaste to 1.5 million people in the eastern and northern suburbs of Melbourne.

YVW implemented the Victorian Government's pricing reform package on 1 January 1998. It involved a move from rate-based to usage-based billing, which increased the proportion of customer accounts that are based on usage charges. This has also increased the exposure of revenue to weather conditions. With the implementation of the pricing reform, a subsidy received from City West Water also ceased.[1] The effect of the reform package is evident in 1999-00 with revenue generated from core business activities, water and sewerage, being $120 million less than 1996-97.

Operating profit before tax (including abnormals) increased in 1999-00 due mainly to a higher level of developer activity and subsequent increase of gifted reticulation assets and cash contributions, the sale of surplus land and increased water consumption resulting from continuing dry weather conditions. The growth in operating profits is responsible for increases in the return on assets and return on equity in 1999-00.

YVW's debt to equity, debt to total asset and total liability to equity ratios have declined over the reporting period. This is mainly due to financial restructuring associated with the 1998 water reform package, which involved a reduction in debt of $100 million and the issuing of 43.5 million fully paid ordinary shares. Debt was reduced further in 1999-00 by $16.9 million. Interest cover has increased as a result of debt reduction.

Since incorporation, YVW has been required to make tax-equivalent and dividend payments. Income tax expense was a negative figure in 1999-00, reflecting benefits generated from the restatement of deferred tax balance due to change in the future company tax rate and an over-provision of tax for developer contributions in prior years. YVW has not identified any community service obligations (CSOs).[2]

1 The reason for the subsidy was to make the three retail water GTEs operate on an equal financial footing.

2 The model of CSO agreements has not been applied to Victorian water GTEs. As such YVW has no CSO, despite being required to engage in non-commercial activities such as the delivery of water and sewerage concessions and grants.

YARRA VALLEY WATER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*	*1999-00*
Size						
Total assets	$M	1 093	1 130	1 157	1 185	1 230
Total revenue	$M	415	439	389	332	353
Profitability						
Operating profit before tax (includes abnormals)	$'000	42 808	76 573	79 469	75 913	96 471
Operating sales margin	%	23.9	30.5	30.9	32.1	36.3
Cost recovery	%	141.1	146.8	145.6	148.0	157.2
Return on assets	%	9.2	12.1	10.6	9.1	10.6
Return on equity	%	6.4	11.4	12.5	11.3	18.7
Financial management						
Debt to equity	%	130.0	126.1	100.3	98.4	91.5
Debt to total assets	%	50.0	49.5	44.6	43.4	42.0
Total liabilities to equity	%	161.9	158.9	127.4	129.5	122.2
Interest cover	times	1.8	2.3	2.9	3.5	4.0
Current ratio	%	18.3	60.4	39.1	34.0	41.1
Leverage ratio	%	261.9	258.9	227.4	229.5	222.2
Payments to and from government						
Dividends	$'000	45 900	54 972	51 652	48 738	62 707
Dividend to equity ratio	%	11.1	12.9	10.9	9.5	11.7
Dividend payout ratio	%	174.6	112.5	87.4	84.0	62.8
Income tax expense	$'000	16 524	27 700	20 340	17 885	-3 417[b]
CSO funding	$'000	0	0	0	0	0

a Yarra Valley Water implemented the Victorian Government's pricing reforms that involved a move from rate-based to usage-based charges. The pricing reform required Melbourne Water Corporation to reduce bulk water charges to the three retail GTEs. Return on assets declined in 1997-98 following an asset revaluation that resulted in an increase of $25.4 million. **b** Income tax expense decreased due to a reduction in the future company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from 2001-02. Consequently, deferred tax balances have been remeasured using the appropriate new rates.

BARWON WATER Victoria

Barwon Regional Water Authority is a statutory authority, providing water and sewerage services to more than 250 000 households in Geelong and surrounding areas. Barwon Water also manages 20 kilometres of the Barwon River through urban Geelong.

Barwon Water's operating profit (before tax and including abnormals), return on asset and return on equity increased substantially in 1997-98, owing to the merger with Otway Regional Water Authority, which resulted in abnormal revenue of $69.6 million. The significant decline in the above indicators in 1998-99 resulted from an increase in depreciation expense of assets and a change in pricing structure, which eliminated cross-subsidies between residential and business customers.[1] The decline in operating profit during 1999-00 was due mainly to a $3.8 million abnormal expense item resulting from a transfer of assets to the Corangamite Catchment Management Authority.

Barwon Water's debt to equity, debt to total asset, total liabilities to equity and leverage ratios declined sharply over the reporting period. The current and interest cover ratios increased in 1997-98 — partly due to the State Government's financial assistance package that was utilised by Barwon Water to repay borrowings.

During 1998-99, Barwon Water became a participating authority under the *Borrowing & Investment Power Act 1987*. Under the provisions of the Act, Barwon Water was able to restructure its debt portfolio, transferred all inscribed stock to the Treasury Corporation of Victoria (TCV) and simultaneously obtained loans from TCV. This resulted in reduced borrowing costs.

Barwon Water is required to make dividend payments but did not pay a dividend for 1998-99 and 1999-00 based on the final result for the reporting period. Barwon Water, as a non-metropolitan water authority, is not required to pay tax-equivalent payments.[2] Barwon Water is not subject to a community service obligation (CSO).[3]

1 Assets were revalued using optimised deprival valuation principles, resulting in an increase of $377.8 million.

2 Only the metropolitan sector of the Victorian water industry is subject to a tax-equivalent regime.

3 The model of CSO agreements has not been applied to Victorian water GTEs.

BARWON WATER (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*[b]	*1999-00*
Size						
Total assets	$M	378	384	858	841	841
Total revenue	$M	62	64	145	68	73
Profitability						
Operating profit before tax (includes abnormals)	$'000	11 386	10 206	51 960	6 049	4 080
Operating sales margin	%	40.9	35.5	47.4	18.3	11.3
Cost recovery	%	169.0	154.0	123.6	124.8	118.7
Return on assets	%	7.0	6.3	11.4	1.6	1.0
Return on equity	%	5.5	4.7	10.4	0.6	0.5
Financial management						
Debt to equity	%	71.2	65.9	11.9	8.8	8.2
Debt to total assets	%	40.7	38.8	14.4	7.9	7.4
Total liabilities to equity	%	76.6	71.3	14.0	10.9	10.3
Interest cover	times	1.8	1.7	3.8	1.8	1.9
Current ratio	%	85.6	88.1	187.6	91.4	94.6
Leverage ratio	%	176.6	171.3	114.0	110.9	110.3
Payments to and from government						
Dividends	$'000	4 160	4 213	1 663	0	0
Dividend to equity ratio	%	2.0	1.9	0.3	0	0
Dividend payout ratio	%	36.5	41.3	3.3	0	0
Income tax expense	$'000	0	0	1 388	1 643	0
CSO funding	$'000	0	0	0	0	0

a Barwon Water received $86 million under a State Government financial assistance package, which was utilised to repay borrowings. On 1 July 1997, Barwon Water assumed responsibility for the majority of the Otway Regional Water Authority's assets, liabilities and reserves. The merger resulted in abnormal revenue of $69.6 million, which significantly increased return on asset and return on equity. On 30 April 1998, Barwon Water paid out the unfunded superannuation liability it held with the Local Authorities Superannuation Fund amounting to $3.6 million. Fixed assets were revalued on a current cost basis at 30 June 1998, resulting in an increment of $377.8 million. **b** The exchange of Barwon Water's entire inscribed stock to the Treasury Corporation of Victoria (TCV), and the simultaneous issue of an identical loan by TCV to Barwon Water, resulted in all Barwon Water's borrowings being undertaken through TCV and being subject to a Victorian Government guarantee under the *Borrowing & Investment Power Act 1987.* The novation of debt to the TCV included 1 635 inscribed stockholders ($14.5 million) and three institutional investors ($15.5 million). 1998-99 is the first full year of Stage 1 water restrictions, which were implemented in January 1998.

DEPARTMENT OF NATURAL RESOURCES, STATE WATER PROJECTS — Queensland

State Water Projects (SWP) is a commercialised business unit within the Department of Natural Resources (DNR). SWP was fully commercialised on 1 July 1997 in accordance with the *Queensland Competition Authority Act 1997*.[1] During 1999-00 a decision to establish SWP as a statutory government-owned corporation entitled 'Sun Water', was announced. The corporatisation of SWP will separate service provision from regulatory functions, consistent with National Competition Policy requirements.

SWP develops and manages government-owned bulk water storage and distribution infrastructure and supplies water to about 7 500 customers, including irrigators, industrial customers and urban bulk water customers. The unit also provides facility management services to other water infrastructure owners, and engineering consultancy services to government and private sector clients.

The fall in total assets in 1999-00 is attributable to a revaluation of non-current physical assets and a move from deprival valuation methodology to fair value methodology — the amount by which an asset could be exchanged between knowledgeable willing parties in an arms length transaction. The revaluation resulted in $1.9 billion being written-down directly against accumulated funds. Subsequently, return on assets and return on equity improved.

In 1997-98 and 1998-99, SWP operated debt free. Therefore debt to equity and debt to total asset ratios are zero.[2] During 1999-00, SWP entered into financing arrangements with Queensland Treasury Corporation with the establishment of a $5 million loan. The loan is the first tranche of a loan facility of up to $25.6 million.

SWP is required to make income tax-equivalent payments. SWP receives community service obligation (CSO) funding from the State Government. CSO funding meets the shortfall in income resulting from operational costs.

1 The SWP group was separated from the Regional Infrastructure Development Program.

2 In 1997-98 commercialisation established SWP with a capital structure free of debt.

DEPARTMENT OF NATURAL RESOURCES, STATE WATER PROJECTS (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	1 855	2 110	2 096	2 102	235
Total revenue	$M	49	62	80	74	99
Profitability						
Operating profit before tax (includes abnormals)	$'000	4 178	-43 024	-11 843	-21 101	4 706
Operating sales margin	%	8.4	-30.5	-14.8	-31.7	2.5
Cost recovery	%	109.2	76.6	87.1	50.3	101.4
Return on assets	%	0.2	-1.0	-0.6	-1.0	0.4
Return on equity	%	n.r.	-4.5.	-0.6	-1.0	0.4
Financial management						
Debt to equity	%	0	7.7	0	0	2.2
Debt to total assets	%	0	7.4	0	0	0.4
Total liabilities to equity	%	n.r.	9.9	0.9	0.8	2.5
Interest cover	times	0	-0.8	0	0	4 7.1
Current ratio	%	n.r.	100.8	447.0	630.2	309.9
Leverage ratio	%	n.r.	109.9	100.9	100.8	102.5
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	n.r.	n.r.	0	0	0
Dividend payout ratio	%	n.r.	n.r.	n.r.	n.r.	0
Income tax expense	$'000	n.r.	n.r.	n.r.	n.r.	0
CSO funding	$'000	0	0	0	28 500	25 681

a Department of Natural Resources – State Water Projects (SWP) reported its financial operation on a full accrual basis for the first time in 1996-97. Therefore, previous years are not directly comparable. **b** The SWP group separated from the Regional Infrastructure Development Program. SWP was fully commercialised on 1 July 1997. SWP is a separate reporting entity under the *Financial Administration and Audit Act 1977* and produces its own audited general purpose financial report. When commercialised, SWP was established with a capital structure free of debt. At 1 July 1997, a future income tax benefit was recognised up to the amount of the provision for deferred income tax. An amount of $856 425, which is the excess of the future income tax benefit over the provision for deferred income tax, has not been recognised. **c** As at 1 July 1999, SWP will transfer all long service leave liabilities to a central actuarially assessed scheme administrated by the Government Superannuation Office. SWP will not be required to hold its liability for long service leave on its balance sheet. This financial effect has not been recognised for the year ending 30 June 1999. **d** A revaluation in 1999-00 resulted in $1.9 billion being written-down directly against accumulated funds. **n.r** Not relevant.

SOUTH AUSTRALIAN WATER CORPORATION South Australia

South Australian Water Corporation (SA Water) was established in 1 July 1995 under the provisions of the *South Australian Water Corporation Act 1994*. SA Water provides water and wastewater services for both the metropolitan and country areas of South Australia.

In December 1995, SA Water contracted out the operation, maintenance and management of Adelaide's water and wastewater system to United Water International.[1] In 1996, SA Water entered into the Water Treatment and Economic Development Agreement with Riverland Water Pty Ltd. Under this Agreement, Riverland Water was contracted to finance, design, construct, operate and maintain 10 water filtration plants for a minimum of 25 years.[2]

SA Water's operating profit before tax (including abnormals), return on assets and return on equity increased sharply in 1996-97 and increased steadily until 1999-00. The sharp rise in these indicators for 1996-97 reflects a $72 million increase in revenue due to community service obligation (CSO) funding, a $28 million increase in sales revenue and improved debt management.[3] The return on asset and return on equity ratios have improved over the reporting period.

Profitability indicators continued to rise in 1999-00 as a result of increased water and waste water revenue, increased capital contributions due to higher levels of activity in the building sector and additional CSO funding.

SA Water is subject to the South Australian Government's tax-equivalent regime and is required to make dividend payments.

Under CSO policy, SA Water receives supplementary payments relating to the provision of water and wastewater services in country areas from 1996-97. Prior to 1996-97, the costs of CSOs were met internally by other profitable activities.

1 Operations under the contract commenced in January 1996 for a term of 15 years with requirements for significant improvements in efficiency and service, with cost saving.

2 The Riverland Water contract involves an obligation on the part of its major shareholder, United Utilities Australia Ltd (formerly North West Water Australia Ltd) to generate substantial exports of technical and managerial expertise.

3 1996-97 was the first year of explicit CSO payments from the South Australian Government. During 1996-97, debt restructuring reduced costs by $18.8 million.

SOUTH AUSTRALIAN WATER CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*	*1998-99*	*1999-00*
Size						
Total assets	$M	5 511	5 757	5 766	5 897	6 026
Total revenue	$M	401	505	552	566	598
Profitability						
Operating profit before tax (includes abnormals)	$'000	3 288	135 568	171 737	179 802	196 445
Operating sales margin	%	27.9	44.8	47.5	47.9	48.0
Cost recovery	%	138.1	182.0	194.7	193.0	198.0
Return on assets	%	2.1	4.0	4.6	4.7	4.8
Return on equity	%	-0.2	1.9	2.6	2.7	3.0
Financial management						
Debt to equity	%	24.1	22.2	21.2	22.0	22.6
Debt to total assets	%	19.4	18.0	16.9	17.5	17.8
Total liabilities to equity	%	26.1	25.9	25.4	27.0	28.4
Interest cover	times	1.0	2.5	2.9	3.0	3.2
Current ratio	%	47.1	109.4	103.9	86.9	62.2
Leverage ratio	%	126.1	125.9	125.4	127.0	128.4
Payments to and from government						
Dividends	$'000	38 000	91 200	105 800	144 400	175 200
Dividend to equity ratio	%	0.9	2.0	2.3	3.1	3.8
Dividend payout ratio	%	-437.4	108.7	90.1	116.4	123.6
Income tax expense	$'000	11 976	51 698	54 253	55 762	54 706
CSO funding	$'000	0	72 000	74 365	77 135	85 259

a The Adelaide water and wastewater system was contracted out to United Water. The contract commenced on 1 January 1996 for a term of 15 years, with 1996-97 being the first full financial year of operation.

WATER CORPORATION — Western Australia

The Water Corporation was established on 1 January 1996, following a major restructure of the Western Australian water industry. It operates under a 25 year operating licence issued by the Office of Water Regulation. The Water Corporation provides public water supply, sewerage, drainage and irrigation services to a population of over 1.7 million, including 300 towns and communities throughout Western Australia.

The Water Corporation's total revenue, operating profit before tax (including abnormals), return on total assets and return on equity have increased over the reporting period. This is mainly due to increased water sales over a period of hot and dry weather conditions, increased tariffs for services and a higher level of property development and developer contributions.[1] Contributions from land developers grew 15.5 per cent in 1999-00.

There was a significant increase in interest cover from 1995-96 to 1996-97 due to debt reduction amounting to $125 million, and a sharp increase in operating profit.[2] Interest cover increased over the reporting period as debt was reduced.

The current ratio decreased sharply from 1996-97 to 1997-98 due to an early repayment of loans to the Western Australian State General Loan Fund and the Commonwealth Government, which lowered the cash balance.

The Water Corporation is required to make tax-equivalent and dividend payments. Tax-equivalent payments were payable from 1 July 1996. Income tax expense decreased in 1999-00 as a consequence of the restatement of deferred tax balances as a result of the implementation of lower company tax rates.

The Water Corporation received community service obligation (CSO) payments from the Western Australian Government from 1 July 1996.[3] CSO payments increased in 1999-00 with a required increase to revenue concessions and sewerage expenditure.

---

1 The tariff reform in 1997-98 involved an increase in prices by 4 per cent for customers using less than 350 kilolitres per annum and an increase of 10 per cent for those who use more. Tariffs increased by 2 per cent in 1999-00.

2 The increase in profit is attributable to abnormal revenue of $24.6 million for unbilled water consumption, $26 million from a favourable tax ruling on rate revenue on the previous year and $71 million in developer's contributions.

3 The Water Corporation has agreed to a fixed reduction of 2.5 per cent per year to CSO payments for country services.

WATER CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*	*1998-99*	*1999-00*
Size						
Total assets	$M	8 436	8 578	8 710	8 919	9 174
Total revenue	$M	587	800	890	926	987
Profitability						
Operating profit before tax (includes abnormals)	$'000	42 802	286 784	360 048	375 548	452 238
Operating sales margin	%	16.8	42.2	45.2	44.3	49.4
Cost recovery	%	129.8	168.1	183.6	179.2	197.5
Return on assets	%	1.5	4.1	4.7	4.7	5.4
Return on equity	%	0.3	2.4	2.9	2.7	4.5
Financial management						
Debt to equity	%	9.5	7.7	5.7	6.8	7.1
Debt to total assets	%	8.5	6.9	5.2	6.2	6.4
Total liabilities to equity	%	12.9	11.9	10.3	12.1	13.7
Interest cover	times	1.5	5.6	8.4	11.2	13.2
Current ratio	%	281.9	130.2	57.3	47.9	47.8
Leverage ratio	%	112.9	111.9	110.3	112.1	113.7
Payments to and from government						
Dividends	$'000	58 903	198 692	158 706	196 111	201 215
Dividend to equity ratio	%	0.8	2.6	2.0	2.5	2.5
Dividend payout ratio	%	293.9	110.7	70.7	90.4	55.3
Income tax expense	$'000	22 758	107 314	135 699	158 570	88 133[c]
CSO funding	$'000	0	182 253	180 316	192 124	205 617

a The Water Corporation commenced operations on 1 January 1996 after the disaggregation of the Water Authority of Western Australia. **b** The Water Corporation received payments for the provision of community service obligations from the Western Australian Government from 1 July 1996. The significant increase in profit is attributed to abnormal revenue of $24.6 million for unbilled water consumption, $26 million from a favourable tax ruling on rate revenue on the previous year and $71 million in developer's contributions. There was a 2.9 per cent growth in the customer base. Developer's contributions are recognised as revenue and the after tax value is transferred to a reserve during the year of receipt. On average, developer's contributions account for 10 per cent of total operating revenue. **c** Income tax expense decreased due to a reduction in the future company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from 2001-02.

HOBART REGIONAL WATER AUTHORITY — Tasmania

Hobart Regional Water Authority, trading as Hobart Water, was established as a joint authority under s. 38 of the *Local Government Act 1993*. Hobart Water commenced operation on 1 January 1997 when the assets, property rights and liabilities of its predecessor, the Hobart Regional Water Board, were transferred. Hobart Water provides bulk water supplies to eight councils in southern Tasmania.

Hobart Water introduced a new water pricing policy on 1 July 1997 that incorporates a two-part tariff.[1] Bulk water prices decreased by 3.6 per cent, in real terms, since implementation of the policy. Despite lower prices, prolonged dry conditions in 1999-00 lead to increased demand and a growth in revenue of $2 million.

Operating profit before tax (including abnormals) and profitability ratios declined in 1999-00. Increases in the costs of water supply were the main reason for this decline.

Hobart Water made an operating loss before tax (including abnormals) in 1997-98 as a result of debt refinancing. This resulted in an abnormal loss of $3.4 million. Return on asset and return on equity declined significantly.

Hobart Water's total liability to equity increased in 1997-98 as a result of a loss incurred from financial restructuring and the inclusion of provisions for dividends payable and deferred income tax liabilities for the first time. The current ratio increased significantly in 1997-98 as a result of increased investment and sundry debtors. Interest cover increased sharply in 1998-99 as a result of the debt reduction strategy, implementation of a new debt management policy and low interest rates.

Hobart Water is required to pay tax-equivalent and dividend payments. However, despite recording income tax expense over the reporting period, it has not paid tax due to the effect of timing and permanent differences.[2]

1 The model is structured such that the tariff is based on both the amount of water each council uses and a fixed charge apportioned on the basis of each council's share of average consumption for the previous three years.

2 An example of the effects of these differences is observable in 1999-00 when reported accounting profit was $2.8 million but taxable income was a $6.5 million loss.

HOBART REGIONAL WATER AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*	*1999-00*
Size						
Total assets	$M	184	175	184	171	171
Total revenue	$M	17	18	18	17	19
Profitability						
Operating profit before tax (includes abnormals)	$'000	1 470	1 398	-1 261	2 862	2 757
Operating sales margin	%	37.6	33.2	14.9	25.8	24.0
Cost recovery	%	153.5	149.8	150.8	134.7	131.6
Return on assets	%	3.5	3.3	1.5	2.6	2.8
Return on equity	%	1.2	1.1	-1.6	2.6	1.4
Financial management						
Debt to equity	%	37.6	25.7	27.6	27.7	27.1
Debt to total assets	%	26.2	19.2	20.4	19.9	20.0
Total liabilities to equity	%	43.6	30.5	39.1	34.3	35.0
Interest cover	times	1.3	1.3	0.7	2.7	2.4
Current ratio	%	90.6	14.2	40.9	52.4	34.4
Leverage ratio	%	143.6	130.5	139.1	134.3	135.0
Payments to and from government						
Dividends	$'000	0	0	2 000	2 200	2 500
Dividend to equity ratio	%	0	0	1.5	1.7	2.0
Dividend payout ratio	%	0	0	-95.8	64.8	137.9
Income tax expense	$'000	0	0	828	-533	944
CSO funding	$'000	0	0	0	0	0

a Ownership of the organisation passed from the Tasmanian Government to the eight southern Tasmanian councils, which comprise the joint authority. All non-current assets were revalued using replacement deprival value on 1 January 1997. The effect of the revaluation was to increase the value of non-current assets by $118 million. **b** From 1 July 1997, a new water pricing policy was introduced based on a two-part tariff. The two-part tariff incorporates a charge based on the amount of water each council uses and a fixed charge. Amendments to the *Local Government Act 1993* required Hobart Water to calculate income tax-equivalent payments, applying AAS3 Accounting for Income Tax as outlined in the *Government Business Enterprises Act 1995*. Operating loss reflects a $3.4 million abnormal expense generated by debt restructuring.

NORTH WEST WATER AUTHORITY — Tasmania

North West Water Authority (NWWA) is a joint authority established on 10 August 1999 under the Local Government Act.[1] The NWWA assumed all the prescribed property, obligations and liabilities of its predecessor the North West Regional Water Authority. NWWA collects, treats and supplies bulk drinking water to the councils of Circular Head, Waratah-Wynyard, Central Coast, Devonport City, Latrobe and Kentish.

NWWA's operating profit before tax (including abnormals) has fluctuated over the reporting period. NWWA made a loss in 1996-97 and 1997-98 due to a decrease in water consumption and abnormal expenses incurred in 1997-98.[2] Operating profit decreased in 1999-00, largely due to an abnormal expense of $275 307 relating to superannuation adjustments.[3]

Total assets declined by $26.7 million from 1996-97 to 1997-98, as a result of a revaluation of infrastructure assets, to written-down deprival value.

The significant decline in the interest cover ratio reflects the decline in operating profit. Operating profit increased in 1998-99 as a result of interest cost savings of $785 000 following debt restructuring and a decrease in depreciation expense of $579 000.

The 1997-98 asset revaluation resulted in debt to equity, debt to total asset and total liabilities to equity ratios increasing significantly. The current ratio declined substantially in 1996-97 as a result of loans totalling $3 million that became due in 1997-98. The increase in this ratio in 1999-00 is due principally to an increase in current assets such as stock on hand and prepayments, and a decrease in superannuation provision of $1.3 million.

NWWA has been required to make income tax-equivalent and dividend payments since 1997-98.[4] NWWA is also subject to State imposed payroll tax, capital gains tax-equivalents and sales tax-equivalents. Fluoridation is identified as a community service obligation and is reimbursed by the government.

1 As of July 2000 NWWA adopted the trading name Cradle Coast Water.

2 The abnormal expense comprised a $2.7 million loss on defeasance of loans and a $377 746 adjustment to the superannuation provision for redundancy payments in anticipation of NWRWA's transfer from State Government ownership to local government. Due to a debt restructure there was a $549 000 decline in financial expenses.

3 The adjustments include, among other things, a redundancy payout of $1.7 million.

4 No dividend was paid in 1997-98 and 1998-99 due to after tax losses.

NORTH WEST WATER AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	97	89	61	61	59
Total revenue	$M	9	8	8	7	7
Profitability						
Operating profit before tax (includes abnormals)	$'000	872	-11	-2 354	1 311	838
Operating sales margin	%	47.8	36.2	0.4	39.3	29.9
Cost recovery	%	173.5	156.7	162.7	170.8	151.1
Return on assets	%	4.3	3.2	0.1	4.9	3.6
Return on equity	%	1.3	0	-5.4	0.6	1.9
Financial management						
Debt to equity	%	39.2	40.8	76.1	70.1	68.2
Debt to total assets	%	27.8	26.8	33.1	39.3	38.7
Total liabilities to equity	%	43.0	45.7	85.9	78.5	74.5
Interest cover	times	1.3	1.0	0	1.8	1.9
Current ratio	%	60.3	37.7	39.4	67.1	90.0
Leverage ratio	%	143.0	145.7	185.9	178.5	174.5
Payments to and from government						
Dividends	$'000	0	0	0	0	345
Dividend to equity ratio	%	0	0	0	0	1.0
Dividend payout ratio	%	0	0	0	0	53.9
Income tax expense	$'000	0	0	161	1 100	197
CSO funding	$'000	23.92	23.92	23.92	25.9	27.45

a North West Regional Water Authority (NWRWA) earned abnormal revenue of $517 000 representing a gain on the retirement of an overseas loan ($150 530) and a superannuation provision write down ($366 830). **b** NWRWA's assets were revalued using written-down replacement cost value, which resulted in a reduction of the asset value, by $6.7 million. **c** NWRWA incurred abnormal expenses ($3.1 million), this included a $2.7 million loss on defeasance of loans and a $377 746 increase to the superannuation provision for redundancy payments in anticipation of the creation of a new joint authority. As a result of a debt restructure, financial expenses declined by $549 000. The price of water reduced from $0.72 per kilolitre to $0.70 per kilolitre. NWRWA became subject to dividend and tax-equivalent payments. No dividend was paid due to after tax losses. All infrastructure assets were revalued using deprival value thus resulted in the value of assets declining by $26.7 million. **d** NWRWA incurred an abnormal expense of $155 000 due to an adjustment of the superannuation provision. North West Water Authority was established on 10 August 1999 as a joint authority of the Circular Head, Waratah-Wynyard, Central Coast, Devonport City, Latrobe and Kentish councils under s. 38 of the *Local Government Act 1993*. **e** Staff, property, obligations and liabilities were transferred from NWRWA to the North West Water Authority (NWWA).

ESK WATER AUTHORITY — Tasmania

Esk Water Authority, trading as Esk Water, was established as a joint authority under the *Local Government Act 1993*. Esk Water commenced operation in July 1997 when the assets of its predecessors, the North Esk Scheme, West Tamar Scheme and the Launceston City Council, were transferred. Esk Water provides bulk water supply to councils and industrial users in the Launceston – Tamar Valley region.[1]

Fluctuations in operating profit between 1997-98 and 1999-00 are largely attributable to changes in water consumption and abnormal revenues. In 1998-99, operating profit decreased as a result of a 1 936 ML fall in the total volume of water sold. In 1999-00, operating profit was increased by $156 444 of abnormal revenue.[2]

The decrease in the current ratio in 1998-99 is attributable to an increase in current liabilities. In particular, a $1.4 million payment to West Tamar Council relating to asset transfers was recognised as a liability. The current ratio declined further in 1999-00, largely due to an increase in current borrowings and a decrease in current investments. The increase in current borrowings was due to long-term debt being partly repaid with short-term debt, as a result there has been a compensating movement in non-current liabilities.

Esk Water is required to make tax-equivalent and dividend payments. Differences between taxation and accounting depreciation rates may cause the actual tax-equivalent payments made to government to differ from those reported.[3]

Esk Water does not receive any explicit funding for community service obligations.

1 The participating councils are the four Tamar Valley councils, Launceston City, George Town, Meander Valley and West Tamar, which comprise the joint authority.

2 This abnormal revenue results from a change in accounting policy. Specifically, a change from determining the value of the superannuation provision on a vested liability basis to an accrued liability basis. This change led to a write-down of the superannuation provision being recognised as abnormal revenue.

3 The use of the *written down replacement cost* of contributed assets, for taxation depreciation purposes, results in taxation depreciation rates being greater than accounting depreciation rates. As a result, the Authority may record both an accounting operating profit and a taxation loss. If a loss is recorded, tax-equivalent payments are not paid.

ESK WATER AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	77	73	102	102	100
Total revenue	$M	6	6	8	7	7
Profitability						
Operating profit before tax (includes abnormals)	$'000	217	-1 713[e]	1 464	824	1 209
Operating sales margin	%	40.5	3.1	30.4	21.9	25.0
Cost recovery	%	168.1	177.2	143.7	128.0	130.5
Return on assets	%	3.3	0.6	2.8	1.7	2.0
Return on equity	%	0.4	-3.0	1.3	0.6	1.0
Financial management						
Debt to equity	%	32.5	26.6	15.1	15.2	12.8
Debt to total assets	%	24.2	20.0	15.0	12.7	10.8
Total liabilities to equity	%	36.4	29.7	17.7	19.6	16.6
Interest cover	times	1.1	0.2	2.4	1.9	2.4
Current ratio	%	336.6	15.9	503.1	174.2	83.2
Leverage ratio	%	136.4	129.7	117.7	119.6	116.6
Payments to and from government						
Dividends	$'000	0	0	351	198	594
Dividend to equity ratio	%	0	0	0.5	0.2	0.7
Dividend payout ratio	%	0	0	37.7	40.8	68.8
Income tax expense	$'000	0	0	534	339	345
CSO funding	$'000	0	0	0	0	0

a These figures relate to the North Esk Scheme, as such they are not directly comparable to Esk Water. **b** Assets from the North Esk Scheme, West Tamar Scheme and the Launceston City Council were transferred to the control and ownership of a joint authority, Esk Water Authority on 1 July 1997. **c** In March 1999, a Master Loan Facility Agreement was entered into with the Tasmanian Public Finance Corporation. This removes the need for any guarantee by the owner councils for loans taken out by Esk Water. **d** Figure includes an abnormal revenue item of $156 000 from the revaluation of superannuation liability. **e** Figure reflects the inclusion of an abnormal expense of $2 million resulting from debt repayment.

4 Urban transport

The financial performance of four urban transport government trading enterprises (GTEs) are reported in this chapter — the State Transit Authority, TransAdelaide, Metro Tasmania and ACTION (see table 4.1). These GTEs vary in size and the range of services they provide.

At the end of 1999-00, the four GTEs controlled $1.2 billion in assets and generated $748 million in revenue. TransAdelaide and the State Transit Authority and are the largest operators, accounting for 53 per cent and 38 per cent of assets, and 57 per cent and 30 per cent of revenues respectively.

For a discussion of the data and the performance indicators used and some of the factors that should be considered when assessing performance see chapter 1.

4.1 Sector reforms

Urban transport GTEs underwent considerable administrative and operational change over the reporting period. These changes were largely introduced to increase their commercial focus and reduce their reliance on government contributions. However, governments generally recognise that there are social benefits in the provision of urban transport services.

The principal reforms have been to separate the provision of bus, train and tram services and the competitive tendering of some of these services. The tendering process requires GTEs to compete with the private sector on the basis of a set of costing rules aimed at ensuring competitive neutrality. During 1999-00, TransAdelaide was unsuccessful in tendering for the provision of urban bus services in Adelaide. As a result, TransAdelaide no longer provides bus services in its own right.

Governance arrangements for urban transport GTEs have been reformed to make them similar to those of other GTEs. For example, in 1995-96, the Metropolitan Transport Trust of Tasmania became a GTE subject to the *Government Business Enterprise Act 1995* and in February 1998 a government-owned company subject to corporations law.

Table 4.1 **Monitored Urban Transport GTEs, 1995-96 to 1999-00**

1995-96	*1996-97*	*1997-98*	*1998-99*	*1999-00*
New South Wales				
State Transit Authority →	→	→	→	State Transit Authority
South Australia				
TransAdelaide →	→	→	→	TransAdelaide[a]
Tasmania				
Metropolitan Transport Trust →	→	Metro Tasmania Pty Ltd[b] →	→	Metro Tasmania Pty Ltd
Australian Capital Territory				
ACTION →	→	→	→	ACTION

[a] In April 2000, TransAdelaide was unsuccessful in tendering for the provision of urban bus services in Adelaide. As a result, TransAdelaide no longer provides bus services in its own right. [b] In February 1998, the Metropolitan Transport Trust became a government-owned company subjected to corporations law.

The pricing of urban transport services is determined by independent pricing regulatory bodies in NSW, Tasmania and the ACT. In South Australia, prices are determined by the Public Transport Board, a statutory authority under the Department for Transport, Urban Planning and the Arts.

Urban transport fares have generally increased over the reporting period. For example, on 21 July 1996 Metro Tasmania increased fares — ranging from 10 per cent to 37 per cent — to reduce its significant dependence on government funding to cover operating deficits.

The market environment in which urban transport GTEs operate can have a significant impact on their financial performance. Urban transport GTEs have experienced a general fall in demand for their services over the reporting period, partly resulting from increased competition from private operators of urban transport. The demand for urban transport services is also affected by competition from privately-owned motor vehicles, changes in fares and population.

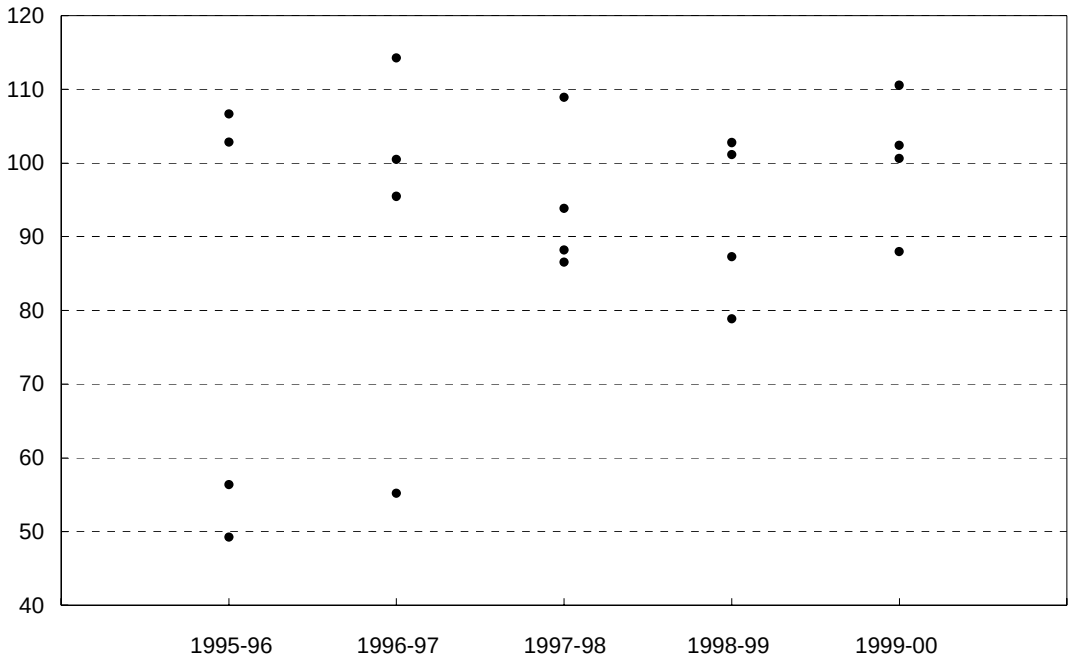
4.2 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings. For a more detailed discussion of profitability indicators see chapter 1.

Since 1996-97, most urban transport GTEs have not been able to sufficiently increase revenue to cover the upward trend in total expenses. The increase in total expenses reflects higher labour and general maintenance costs, increased redundancy and depreciation expenses and the introduction of accounting for superannuation liabilities, among other things.

Urban transport GTEs have moved towards full cost recovery over the reporting period with the average level of cost recovery for the GTEs overall around 95 per cent for most years. There was significant difference in cost recovery levels across GTEs prior to 1997-98 (see figure 4.1). This partly reflects the absence of community service obligation (CSO) payments to Metro Tasmania and ACTION. The introduction of CSO payments to ACTION in 1996-97 and Metro Tasmania in 1997-98, led to a significant improvement in their reported cost recovery.

Figure 4.1 **Cost recovery, 1995-96 to 1999-00 (per cent)**



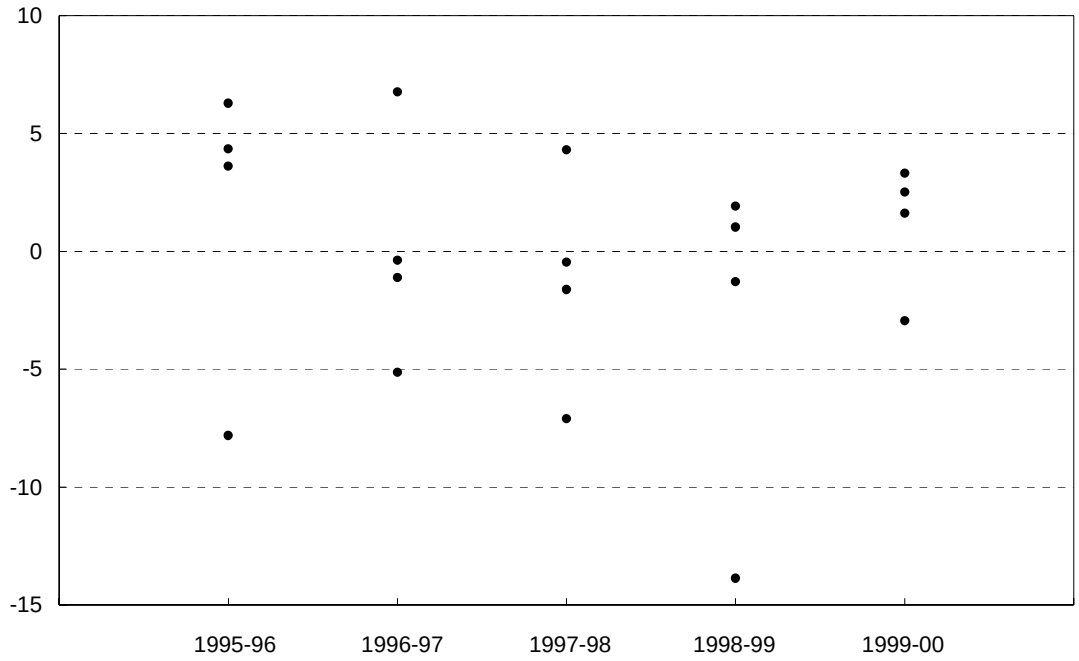
Note Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting abnormal revenue, investment income and receipts from governments to cover deficits on operations from total revenue. Expenses from operations are calculated by subtracting abnormal expenses and gross interest expense from total expenses.

Over the reporting period, the return on assets, like cost recovery, varied considerably across urban transport GTEs (see figure 4.2). The major factors affecting GTEs' return on assets are changes in total revenues and total expenses. However, apart from operating profit, this performance measure is also influenced by changes in asset values — for example, through asset transfers, sale and lease-buy-back arrangements, asset revaluations, asset disposals and depreciation.

TransAdelaide is the only urban transport GTE to earn a positive return on assets in each year of the reporting period. In 1999-00, TransAdelaide, the State Transit Authority and Metro Tasmania achieved a positive return on assets. However, these returns are well below those required by private operators and suggests that urban transport GTEs are not being required to operate on a fully commercial basis.[1]

1 This may indicate that further efficiency gains are possible. Urban transport GTEs could be placed on a commercial footing by governments making explicit CSO payments that recognise the broader economic benefits of the services and the social impact of subsidising some passengers.

Figure 4.2 **Return on assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the return on assets ratio for a GTE in that financial year. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue (including abnormals) and adding back gross interest expense. Average total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period).

Like return on assets, the return on equity achieved by urban transport GTEs has varied substantially over the reporting period. For example, Metro Tasmania's return on equity increased from -18.6 per cent in 1995-96 to 4.8 per cent in 1999-00.

In 1999-00, ACTION had a negative return on equity, although the return has improved compared to previous years. The State Transit Authority and Metro Tasmania moved from having negative return on equity in 1998-99 to positive returns in 1999-00. TransAdelaide had a negative return on equity in 1999-00 after having a positive return in the previous year.

4.3 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. For a more detailed discussion of financial management indicators see chapter 1.

Most urban transport GTEs have undertaken debt restructuring over the reporting period, resulting in a reduction in debt levels. This restructuring includes debt for equity swaps, debt transfers to government and debt repayments.

This financial restructuring changes the capital structure of the GTEs, making it difficult to assess financial management performance over time. Asset revaluations also have an impact on performance indicators.

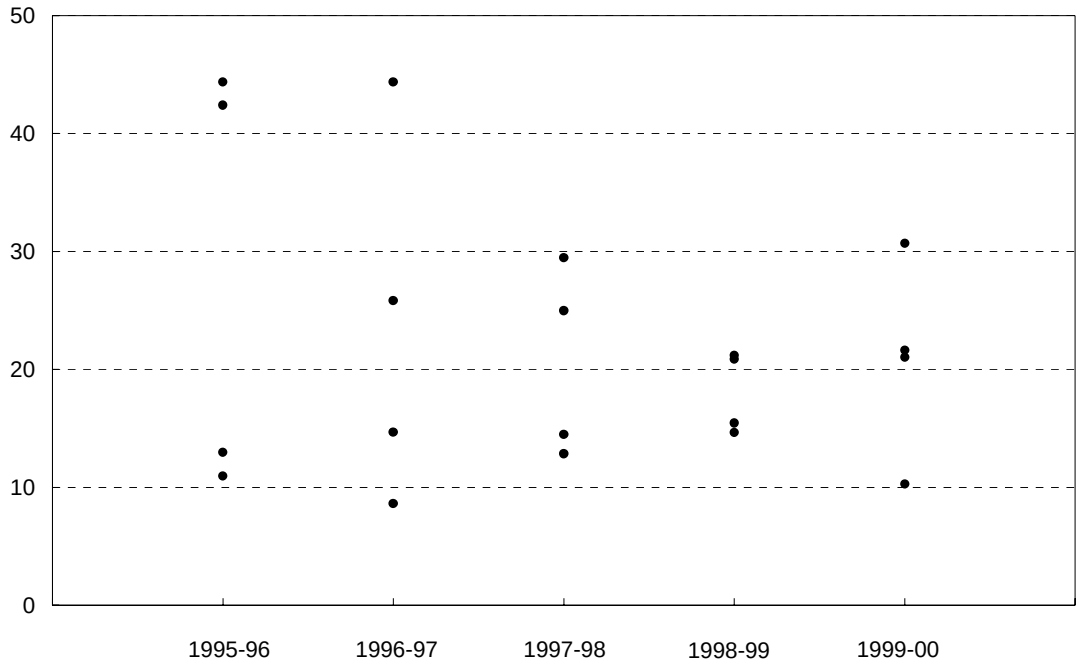
Many urban transport GTEs have revalued their assets over the reporting period. Moreover, valuation procedures are inconsistent. For example, ACTION uses current valuation for some assets, such as land and buildings, and historical cost for others, whereas the State Transit Authority applies current valuation for all property, plant and equipment.

Debt levels for all urban transport GTEs except the State Transit Authority have declined over the reporting period. The level of debt for the State Transit Authority has increased by over $80 million (195 per cent) over the reporting period. Borrowing for the purchase of new buses in 1999-00 accounted for most of the increase in debt levels.

Over the reporting period, the debt to total assets ratio has been generally declining across most GTEs (see figure 4.3). This may suggest a decrease in the proportion of total assets obtained through the use of borrowing. However, an improvement in this ratio can also result from debt restructuring and the transfer of liabilities to government departments. For example, ACTION's debt for equity swap improved their debt to total assets ratio in 1996-97 and the upward revaluation of assets by TransAdelaide achieved a similar result in 1996-97 and 1997-98.

Sound financial management requires that profits are sufficient to ensure interest payments can be met. A high interest cover ratio indicates that the entity can sustain a fall in profit or increased interest expense and still meet the cost of servicing debt. In 1999-00, urban transport GTEs with the exception of Metro Tasmania obtained ratios well below three. Consequently, financial commitments may have to be met from sources of funds other than earnings from time to time.

Figure 4.3 **Debt to total assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the debt to total assets ratio for a GTE in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period). In 1998-99, both ACTION and TransAdelaide had a debt to total assets ratio of 20.9 per cent.

4.4 Financial transactions

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 incentives and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles see chapter 1.

Traditionally, the additional social benefits associated with the provision of urban transport services were recognised implicitly by governments and paid for by funding operating deficits.

More recently, some governments have entered into CSO contracts with their GTEs. The State Transit Authority, Metro Tasmania and ACTION receive explicit CSO payments, while TransAdelaide receives payments as a consolidated figure in total income.

CSO contracts across urban transport GTEs include the following common elements:

- Pricing CSO payment — to reimburse GTEs for offering fares at below the commercial level. The government pays the difference between the full fare applicable for the journey and the fare paid by the traveller;
- Service CSO payment — to reimburse GTEs for providing non-commercial services in excess of minimum service level requirements; and
- Concession CSO payment — to reimburse GTEs for offering government determined concessions. This includes the provision of free and concession travel for school students, and concession travel for tertiary students, pensioners and senior citizens, people with disabilities and welfare recipients.

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.

Apart from the State Transit Authority in 1995-96 and TransAdelaide in 1999-00, no tax-equivalent payments to shareholder governments were made over the reporting period. The State Transit Authority, TransAdelaide and Metro Tasmania have made dividend payments in some years over the period.

4.5 GTE performance reports

State Transit Authority (NSW)
TransAdelaide (SA)
Metro Tasmania (Tas)
ACTION (ACT)

STATE TRANSIT AUTHORITY — New South Wales

The State Transit Authority (STA) is a statutory body incorporated under the *Transport Administration Act 1988.* The STA operates publicly-owned buses and ferry services in metropolitan Sydney and Newcastle.[1]

The increase in revenue in 1999-00 reflected a growth in patronage of 2.8 per cent. This was partly offset by a rise in expenses, largely due to an increase in fuel costs. Included in the positive operating profit of $699 000 (before tax, including abnormals) was an abnormal gain of $3.2 million relating to profit on the sale of properties.

In 1999-00, the STA reported $55.8 million in capital expenditure for bus replacement.[2] This was financed by borrowings (an increase of $68 million), leading to a sharp rise in the debt to equity and total liabilities to equity ratios. Several classes of non-current assets were also revalued upwards by $26.7 million.

During 1998-99, the STA sold property for $20 million. The net sale proceeds of $16.5 million was paid to the NSW Treasury as a special dividend on 30 June 1999. The STA has not made tax-equivalent payments since 1995-96 due to accumulated tax losses. The STA has an agreement with the NSW Government for the reimbursement of pricing, service and concession community service obligations (CSOs).[3]

1 In 1999-00, the STA acquired North and Western Buslines and Parramatta-Ryde Bus Service, increasing STA's market in the north west area of Sydney.

2 The STA is required to maintain the average age of the bus fleet at a maximum of 12 years under the *Passenger Transport Act 1990*. The average age of the bus fleet in 1999-00 was 12 years.

3 The STA does not receive CSO payments for non-commercial services provided by Sydney Bus services.

STATE TRANSIT AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*[b]	*1999-00*[c]
Size						
Total assets	$M	400	379	383	369	434
Total revenue	$M	335	362	372	394	424
Profitability						
Operating profit before tax (includes abnormals)	$'000	10 508	-3 982	-4 501	-9 635	699
Operating sales margin	%	2.8	-0.9	-0.5	-1.5	1.3
Cost recovery	%	102.8	100.5	88.2	87.3	100.6
Return on assets	%	3.6	-0.4	-0.4	-1.3	1.6
Return on equity	%	4.5	-0.9	-2.3	-6.4	0.5
Financial management						
Debt to equity	%	24.4	20.7	34.8	38.4	85.5
Debt to total assets	%	10.9	8.6	14.5	14.6	30.7
Total liabilities to equity	%	134.1	134.0	141.6	157.3	201.5
Interest cover	times	4.2	-0.6	-0.6	-1.0	1.1
Current ratio	%	90.2	38.6	36.7	35.0	42.8
Leverage ratio	%	234.1	234.0	241.6	257.3	301.5
Payments to and from government						
Dividends	$'000	5 177	0	0	16 560	0
Dividend to equity ratio	%	3.5	0	0	11.0	0
Dividend payout ratio	%	77.0	0	0	-171.9	0
Income tax expense	$'000	3 783	-2 536	-875	0	0
CSO funding	$'000	149 500	150 467	161 658	167 837	178 297

[a]Funds generated from Sydney Bus services are used to cover operating losses incurred by Newcastle services (bus and ferry) and Sydney ferry services. Includes capital expenditure of $46.5 million ($38.5 million for new buses) to maintain the average age of the bus fleet at maximum of 12 years as per the *Passenger Transport Act 1990* and meet anticipated demand for the Sydney Olympic Games. This expenditure was funded from investments held with, and borrowing from, the NSW Treasury Corporation. [b] The State Transit Authority (STA) sold land for $20 million, and paid the net sale proceeds to the NSW Treasury as a special dividend. Fares increased by 2.2 per cent as recommended by the Independent Pricing and Regulatory Tribunal. STA entered a sale and lease-buy-back arrangement for its 84 light motor vehicles with $1.8 million as sales proceed. Non-current assets were revalued on a current cost basis and resulted in a reduction of $345 000 in asset value. [c] The increase in the value of assets is due to $55.8 million in capital expenditure for bus replacement and a $26.7 million upward revaluation of non-current assets. The STA reported an abnormal gain of $3.2 million relating to profit on the sale of properties.

TRANSADELAIDE South Australia

TransAdelaide was formed in July 1994 under the *Passenger Transport Act 1994*. It assumed the operations of the former State Transport Authority, while the Passenger Transport Board (PTB) assumed the policy and planning functions. With the passing of the *TransAdelaide (Corporate Structure) Act 1998*, TransAdelaide became subject to the provisions of the *Public Corporations Act 1993*. It has three wholly-owned subsidiary corporations, Hills Transit, Transitplus and Austrics.[1]

During 1994-95, the PTB developed an area-based competitive tendering program for the provision of urban transport services within the metropolitan region. TransAdelaide was required to compete with the private sector on the basis of costing rules aimed at ensuring competitive neutrality.

On 22 April 2000, TransAdelaide ceased the provision of bus services in its own right after unsuccessful bids to the PTB. The disengagement of bus services led to the termination of employment for almost 900 employees and the disposal of around $20 million in assets (and related liabilities). TransAdelaide reported that the withdrawal from bus services would result in a loss of contractual income of $100 million per year.

Despite a decline in contract income received from the PTB of $11.6 million in 1999-00 compared to the previous year, TransAdelaide improved the level of operating profit before tax (including abnormals). The improvement was reduced due to abnormal items relating to the cessation of the provision of bus services.[2]

TransAdelaide makes tax-equivalent and dividend payments to the South Australian Government. TransAdelaide receives funding from the Department of Treasury and Finance to cover expenses incurred as a result of South Australian Government policies and practices.

---

1 Hills Transit was dissolved by regulation on 30 June 2000, as a result of a change to bus services provided by TransAdelaide. Hills Transit provided bus services to the Aldgate and Mount Barker area. Transitplus Pty Ltd (a company jointly owned with Australian Transit Enterprises) was awarded a five year contract for the provision of passenger transport to the area serviced by Hills Transit. Austrics is a software development company involved in the provision of computerised scheduling software.

2 TransAdelaide reported a net abnormal expense of $5.5 million in 1999-00. This included abnormal revenue relating to the withdrawal of bus services ($11.3 million) and separation and incentive payments ($37.8 million). TransAdelaide also reported abnormal expenses relating to separation packages and incentive payments ($37.8 million), loss on disposal of assets ($7.8 million), disengagement expenses ($3.1 million), fleet and depot restoration costs at disengagement ($5.9 million), Hills Transit termination payments ($0.6 million) and the write-off of tax losses associated with the bus business ($7.6 million).

TRANSADELAIDE (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	375	432	656	617	609
Total revenue	$M	205	191	193	193	227
Profitability						
Operating profit before tax (includes abnormals)	$'000	6 549	7 760	5 186	-1 483	3 848
Operating sales margin	%	11.8	13.9	11.5	6.1	6.2
Cost recovery	%	106.6	114.2	108.9	102.7	110.5
Return on assets	%	6.3	6.8	4.3	1.9	2.5
Return on equity	%	4.5	4.5	1.6	0.4	-0.3
Financial management						
Debt to equity	%	115.6	89.4	36.6	31.3	30.1
Debt to total assets	%	42.4	44.4	29.5	20.9	21.0
Total liabilities to equity	%	156.5	115.9	49.9	45.5	42.4
Interest cover	times	1.4	1.4	1.3	0.9	1.3
Current ratio	%	36.9	76.2	71.1	93.0	127.6
Leverage ratio	%	256.5	215.9	149.9	145.5	142.4
Payments to and from government						
Dividends	$'000	0	100	1267	0	0
Dividend to equity ratio	%	0	0.1	0.4	0.0	0.0
Dividend payout ratio	%	0	1.3	24.4	0.0	0.0
Income tax expense	$'000	0	0	0	-3 089	5 314
CSO funding	$'000	0	0	0	0	0

a TransAdelaide's assets were revalued upwards. **b** TransAdelaide's assets were revalued upwards. **c** As part of the South Australian Government's asset management plan, TransAdelaide's bus fleet was transferred to Transport SA resulting in a fall in total assets. 50 per cent of the debt associated with bus fleet assets was transferred to Transport SA. Operating profit before tax (including abnormals) also declined due to a net increase in abnormal expenses associated with the asset transfer. **d** Includes abnormal revenue relating to the withdrawal of bus services ($11.3 million) and separation and incentive payments ($37.8 million). TransAdelaide also reported abnormal expenses relating to separation packages and incentive payments ($37.8 million), loss on disposal of assets ($7.8 million), expenses associated with the withdrawal of bus services ($3.1 million), fleet and depot restoration costs ($5.9 million), Hills Transit termination payments ($0.6 million) and the write-off of tax losses associated with the bus business ($7.6 million). Includes an upward revaluation of land, buildings and rollingstock of $6.7 million.

METRO TASMANIA — Tasmania

Metro Tasmania Pty Ltd was incorporated on 2 February 1998 under the *Metro Tasmania Act 1997*. On the date of incorporation, the assets and liabilities of the Metropolitan Transport Trust were transferred to Metro, which provides urban public transport services to Hobart, Launceston and Burnie.[1]

Over the reporting period, Metro's performance has been affected by falling demand for urban transport services as a result of declining population and competition from motor vehicles.[2] In 1999-00, despite falling demand for services and no change in fares, Metro increased operating revenue by 6 per cent.

Metro's profitability performance has consistently improved each year over the reporting period. The improvement in profit (before tax, including abnormals) in 1999-00 included abnormal revenue relating to a reduction in superannuation provisions ($649 000). This was partly offset by abnormal expenses relating to workers' compensation ($250 000), wholesale sales tax adjustment ($90 000) and costs incurred during a price regulation investigation by the Government Prices Oversight Commission ($130 000).

Metro's debt to equity and total liabilities to equity ratios increased in 1997-98 as a result of a decline in equity. This was largely due to an increase in the provision for superannuation by $5 million.[3] In 1999-00, Metro lowered debt levels by 45 per cent leading to improved debt to equity and debt to total assets ratios.

Metro paid a dividend for the first time in 1999-00. Despite making a profit in 1999-00, Metro was not required to make tax-equivalent payments due to a restatement of future tax payments and benefits as a result of the reduction in the company tax rate from 2000-01 and accumulated tax losses.

Metro entered into a community service agreement with the Government on 31 October 1997. The agreement provides for concessional travel for specified categories of passengers, including school children and pensioners, and for the provision of non-commercial services, such as late night services and weekend services.

---

1 In May 1999, Metro formed a subsidiary company, Metro Coaches (Tas) Pty Ltd to operate bus services from Hobart to Blackman's Bay, the Channel, Campania and New Norfolk.

2 The greatest decline in demand for urban transport services occurred among full-fare paying adult passengers.

3 Metro's superannuation liability estimate was exceeded by $2.2 million in 1998-99 when more employees than anticipated elected to leave the State Government Retirement Benefits Fund Superannuation Scheme.

METRO TASMANIA (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*[a]	*1998-99*[b]	*1999-00*[c]
Size						
Total assets	$M	57	56	51	37	35
Total revenue	$M	31	31	32	28	30
Profitability						
Operating profit before tax (includes abnormals)	$'000	-5 651	-3 826	-1 128	-69	763
Operating sales margin	%	-21.3	-16.9	-10.1	-0.7	2.9
Cost recovery	%	49.2	55.2	93.8	101.1	102.4
Return on assets	%	-7.8	-5.1	-1.6	1.0	3.3
Return on equity	%	-18.6	-13.0	-5.5	-0.4	4.8
Financial management						
Debt to equity	%	29.2	35.4	38.3	43.5	23.2
Debt to total assets	%	13.0	14.7	12.8	15.4	10.3
Total liabilities to equity	%	113.9	138.8	185.2	137.2	118.3
Interest cover	times	-5.0	-3.1	-3.4	0.9	2.8
Current ratio	%	46.6	33.5	34.4	30.8	71.7
Leverage ratio	%	213.9	238.8	285.2	237.2	218.3
Payments to and from government						
Dividends	$'000	0	0	0	0	533
Dividend to equity ratio	%	0	0	0	0	3.4
Dividend payout ratio	%	0	0	0	0	69.9
Income tax expense	$'000	-113	-561	0	0	0
CSO funding[d]	$'000	0	0	18 824	18 300	18 725

a On 2 February 1998, Metropolitan Transport Trust (MTT) was incorporated under the *Metro Tasmania Act 1997* to form Metro Tasmania Pty Ltd. The financial statistics for 1997-98 consolidate MTT's and Metro's figures. On 31 October 1997, MTT entered into a community service obligations (CSO) contract with the Tasmanian Government, replacing the previous system of funding for the provision of services. As a consequence, grants received from the Tasmanian Government are reclassified as operating income. Metro purchased 15 buses on the expiration of their operating lease for $2.4 million. Metro earned a profit from the disposal of fixed assets amounting to $40 216. **b** In May 1999, Metro formed a subsidiary company, Metro Coaches (Tas) Pty Ltd. Includes an abnormal expense of $0.5 million relating to a change in assumptions of superannuation liabilities and an extraordinary expense of $2.2 million relating to underprovision for superannuation. **c** Includes abnormal revenue of $649 000 relating to a reduction in superannuation provisions. Metro also reported abnormal expenses relating to workers' compensation ($250 000), wholesale sales tax adjustment ($90 000) and costs incurred during a price regulation investigation by the Government Prices Oversight Commission ($130 000). **d** The level of funding is specified in a agreement between Metro and the Tasmanian Government. The level of CSO funding is not reported separately in Metro's financial statements. CSO amounts were specified in the Government Prices Oversight Commission *Investigation of Metro Pricing Policies*, June 2000.

ACTION — Australian Capital Territory

ACTION was established in 1977 pursuant to the *Motor Omnibus Services ACT 1955*, and is currently a division of the ACT Government's Department of Urban Services (DUS). ACTION provides urban and school bus services to the Canberra metropolitan area.

On 1 July 1998, ACTION entered into a purchaser–provider relationship with the DUS, whereby the DUS purchases public transport services from ACTION. As part of this arrangement, the majority of ACTION's property was transferred to DUS.[1] Furthermore, ACTION sold part of its fleet of buses for $6.5 million under a sale and lease-buy-back arrangement.[2]

Increased contributions from the ACT Government and a decrease in operating expenses led to an improvement in the cost recovery ratio and operating profit (before tax, including abnormals) in 1999-00 compared to previous years. ACTION reported an abnormal gain of $1.1 million in 1999-00 relating to participation in a Commonwealth Government driver accreditation program. This was partly offset by an abnormal expense of $0.3 million relating to loss on the sale of obsolete stores.

ACTION reduced the level of debt in 1999-00, leading to an improvement in debt to equity and debt to total liabilities ratios. The lower level of debt reduced interest expenses by 11 per cent and resulted in an improvement in interest cover.

ACTION did not pay income tax or dividend payments over the reporting period.

ACTION entered into a contract in 1996-97 to meet community service obligations (CSOs). ACTION receives CSOs to provide reimbursement for offering fares below a commercial level, general route off-peak services, concessional travel for students and the provision of school services and special needs transport.[3] In order to meet its costs, ACTION also receives annual subsidies from the ACT Government.[4]

---

1 On 1 July 1998, most of ACTION's property, including bus shelters and interchanges, were transferred to the DUS as part of the implementation of the purchaser–provider governance arrangement. ACTION retained its Belconnen and Tuggeranong depots and associated offices including ACTION's head office.

2 The five year lease agreement commencing 28 June 1998 involved the lease of 25 buses. ACTION is required to make lease payments of $975 000 per year.

3 ACTION operates the special needs transport on a full cost recovery basis with revenue received from ACT Health Community Care, the ACT Department of Education and Canberra Hospital. ACTION reported $270 000 in foregone revenue for bus advertising for ACT Government and community organisations.

4 ACTION received subsidies of $3 million in 1996-97, $1 million in 1997-98, $2.3 million in 1998-99 and $5.2 million in 1999-00.

ACTION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	117	112	101	76	72
Total revenue	$M	65	65	56	57	67
Profitability						
Operating profit before tax (includes abnormals)	$'000	-1 660	-7 651	-11 015	-14 733	-4 342
Operating sales margin	%	7.9	-2.0	-13.5	-21.7	-3.3
Cost recovery	%	56.4	95.5	86.5	78.8	88.0
Return on assets	%	4.3	-1.1	-7.1	-13.9	-3.0
Return on equity	%	-3.3	-13.2	-17.6	-28.7	-10.2
Financial management						
Debt to equity	%	106.8	44.8	45.0	43.4	38.3
Debt to total assets	%	44.3	25.8	25.0	21.2	21.6
Total liabilities to equity	%	136.3	69.5	71.4	75.4	72.5
Interest cover	times	0.8	-0.2	-2.2	-5.1	-1.0
Current ratio	%	52.6	47.2	45.5	27.0	46.2
Leverage ratio	%	236.3	169.5	171.4	175.4	172.5
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0	0	0	0	0
Dividend payout ratio	%	0	0	0	0	0
Income tax expense	$'000	0	0	0	0	0
CSO funding	$'000	0	35 787	36 367	39 295	42 631

a The ACT Government extinguished all of ACTION's loans since self-government in 1989, converting debt of $23.9 million to equity. **b** Total revenue fell sharply between 1996-97 and 1997-98 resulting from declining fare revenue and reduced subsidy payments, and no revenue from asset disposals or recoveries from redundancies. **c** ACTION became liable for the payment of state and federal taxes and charges in 1998-99. On 1 July 1998, most of ACTION's property, including bus shelters and interchanges, were transferred to the DUS as part of the implementation of the purchaser–provider governance arrangement. ACTION retained its Belconnen and Tuggeranong depots and associated offices including ACTION's head office. **d** Includes an abnormal gain of $1.1 million relating to participation in a Commonwealth Government program. An abnormal expense of $0.3 million was incurred relating to loss on the sale of obsolete stores.

5 Railways

The financial performance of five rail Government Trading Enterprises (GTEs) is reviewed in this chapter — the NSW State Rail Authority (SRA), the Freight Rail Corporation of NSW (FreightCorp), Queensland Rail, Westrail and the National Rail Corporation (NRC) (see table 5.1). Westrail and Queensland Rail provide both passenger and freight services, FreightCorp and NRC provide only freight services, while the SRA provides passenger services.

Victoria's rail services are not included as they have been contracted to the private sector. TransAdelaide is reported on in chapter 4 because it only provides urban passenger services.

At the end of 1999-00, the five GTEs monitored controlled $16.3 billion of assets and generated $5.3 billion in revenues. Queensland Rail and the SRA are the largest operators, accounting for 48 per cent and 33 per cent of assets, and 40 per cent and 31 per cent of revenues respectively.

For a discussion of the data and the financial indicators used and some of the factors that should be considered when assessing performance see chapter 1.

5.1 Sector reforms

Reforms within the rail sector have been aimed at improving performance by subjecting operators to greater competitive pressures and introducing stronger financial disciplines.

Third party access regimes have been introduced, or are in the process of being introduced in each State and Territory, in accordance with National Competition Policy (NCP) agreements between the Commonwealth and State and Territory governments. Third party access to rail infrastructure (essentially the rail track) is seen as a means of increasing the scope for competition in rail services.

Table 5.1 **Monitored rail GTEs, 1995-96 to 1999-00[a]**

1995–96	*1996–97*	*1997–98*	*1998–99*	*1999-00*
New South Wales				
State Rail Authority	State Rail Authority			State Rail Authority
	Freight Rail Corporation			Freight Rail Corporation
	Rail Access Corporation[b]			Rail Access Corporation
	Rail Services Australia[b]			Rail Services Australia
Queensland				
Queensland Rail				Queensland Rail
Western Australia				
Westrail				Westrail[c]
Commonwealth				
National Rail Corporation				National Rail Corporation

a Victoria's rail services have been contracted to the private sector. TransAdelaide provides urban passenger services and is discussed in Chapter 4. **b** Not monitored. **c** On 30 May 2000, the Western Australia Government sought expressions of interest for the purchase of Westrail's freight operations. On 18 December 2000, the sale of the Westrail freight business to Australian Railroad Group (ARG) was finalised. ARG paid the State Government $585 million and committed to invest a further $400 million in the State's rail system over the next five years. The remaining parts of Westrail's activities will be operated by Western Australian Government Railways.

In NSW, the former SRA was divided into four independent business entities in July 1996 to form the SRA, the Rail Access Corporation (RAC), Rail Services Australia (RSA) and FreightCorp. These structural reforms were primarily aimed at facilitating competition through third party access to rail infrastructure.

The RAC, as the owner of rail infrastructure, was responsible for managing the State's rail infrastructure and for providing access to rail operators to the network. The RSA provided rail infrastructure maintenance services.[1]

FreightCorp provides freight services throughout NSW and owns and maintains its own rollingstock and locomotives.[2] The SRA provides city and country passenger services and owns and maintains its own rollingstock.

In contrast with NSW, the Queensland and Western Australian Governments retained their rail authorities as integrated entities, and set up internal business units that are responsible for third party access issues.

In Queensland, the Network Access Unit was established in 1995-96 within Queensland Rail to deal with access issues. It is responsible for all dealings and for negotiating access with third party operators and the development of network access provisions.[3]

In 1998-99, Westrail was restructured to separate its track functions from its train operating functions. Under the access regime, other operators may negotiate with the track owner for access. The framework for ensuring access arrangements will be overseen and monitored by the Western Australian Independent Rail Access Regulator.[4]

There has been some restructuring of interstate freight operations following the establishment of the NRC. In 1991-92, the NRC was formed by the Commonwealth and State governments to take over interstate freight traffic from the State rail

1 On 1 January 2001, Rail Services Australia and the Rail Access Corporation were merged to form the Rail Infrastructure Corporation.

2 In September 2000, the NSW Government announced its intention to sell FreightCorp to the private sector.

3 Queensland Rail has put in place accounting arrangements to separately identify network infrastructure and operating costs. These arrangements are designed to treat third party operators and internal business groups equally for the purposes of access pricing.

4 On 18 December 2000, the sale of the Westrail freight business to Australian Railroad Group (ARG), a private operator, was finalised. As part of the sale, ARG has been granted a 49 year lease of the freight rail network. As a result, other freight operators negotiate with ARG over access to the freight network. The remaining parts of Westrail's activities will be operated by Western Australian Government Railways.

systems and Australian National (Commonwealth). Establishment involved the transfer of business and assets associated with interstate freight to the NRC over much of the reporting period.[5]

Structural reforms that change the scope of a GTE's activities complicate the assessment of performance over time. Changes in the asset base, liability structure and revenue stream relativities that accompany such reforms result in inconsistencies in financial data over time. They also affect the financial ratios presented in the individual GTE performance reports.

Most rail GTEs have set about improving the operational performance of their business. Investment programs have been developed to upgrade and renew infrastructure. New services and initiatives aimed at improving system efficiencies and attracting and retaining customers have also been introduced.

Governments have restructured most rail GTEs into separate business units relating to their core services. Managers have also developed closer ties with the private sector, either through the contracting out of non-core activities or the formulation of joint ventures, such as Queensland Rail's joint venture with Sea Containers Ltd to establish the Great South Pacific Express.

The revenues and costs associated with operational restructuring, such as the sale of assets or redundancy costs, are included in the calculation of some financial ratios as abnormal revenues and expenses. Hence, in some cases, financial ratios may overstate or understate the extent of changes in GTE performance.

Over the reporting period, financial reforms have included financial restructuring, the revaluation of assets, the identification and direct funding of community service obligations (CSOs), the development of dividend policies and the introduction of tax-equivalent regimes. Many of these reforms were aimed at establishing competitive neutrality conditions agreed to under NCP.

Reforms that change the financial structure of a business will affect the financial ratios used to assess performance. Further, the consistency with which financial reforms are applied across GTEs has implications for performance comparisons.

5 In May 2000, NRC shareholders (Commonwealth, NSW and Victorian Governments) agreed to sell the NRC to the private sector.

5.2 Market environment

Rail GTEs have been operating in an increasingly competitive market environment. Rail transport has been largely displaced in many of its traditional markets by road transport, causing rail's share of the transport market to decline continually over the last 25 years.

The declines in market share have been most significant in the provision of non-urban passenger services and the interstate transport of non-bulk commodities. Alternative transport modes, including the car, plane and bus, have largely replaced rail in non-urban passenger services. Car transport is also capturing a greater share of the urban transport market.

In the interstate transport of containerised freight, the volume carried on road has been increasing at about three times the growth in rail volumes (Rail Projects Taskforce 1999). Rail has gone from being the dominant form of transport to, in most cases, a minor player in the transport of agricultural products, livestock, fertilisers and cement.

Rail has maintained a dominant role in the transport of bulk commodities, such as coal and iron ore, to ports. Rail is well suited to the transport of bulk commodities because it can handle the large volumes and heavy weights that are normally involved in their transport. However, the demand for rail transport has become susceptible to fluctuations in the demand for bulk commodities.

Revenue is also affected by demand and supply conditions in commodity markets, particularly coal and grain. Westrail and Queensland Rail have increased revenue in each of the past three years as coal and grain volumes have increased. However, FreightCorp's operating revenues have declined by 23 per cent since 1996-97.

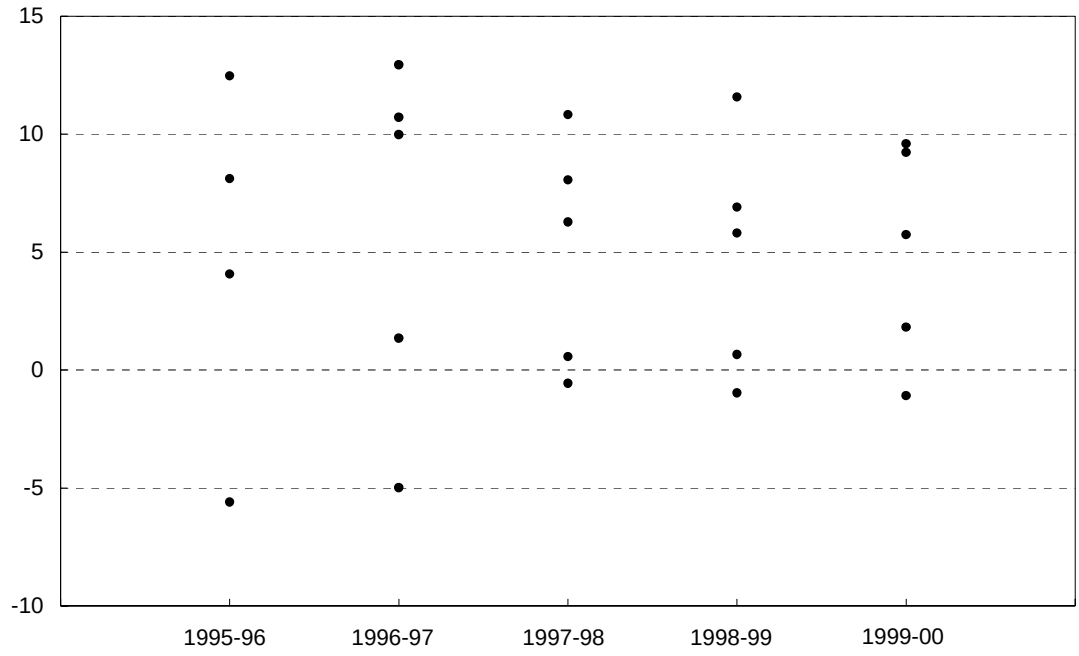
The implementation of access regimes increased the scope for competition from other rail operators, particularly private rail operators. For example, from 1997-98, FreightCorp faced competition from other rail operators for the transport of freight on the NSW rail system. Reductions in rail access charges have also led to reduced freight rates and resulted in a decline in revenue for some rail GTEs.

5.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings. For a more detailed discussion of profitability indicators see chapter 1.

Profitability, in terms of return on assets, has been mixed. The rail GTEs have had an average return on assets of around 5 per cent since 1995-96 (see figure 5.1).[6] Queensland Rail, Westrail and FreightCorp have consistently earned returns of between 5 and 15 per cent over the reporting period, although both Queensland Rail and FreightCorp's returns declined between 1996-97 and 1998-99. This performance compares favourably with private sector railways in the United States, where the average return on assets was around 5 per cent in 1999-00 (Troy 2000).

Figure 5.1 **Return on assets, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the return on assets ratio for a GTE in that financial year. Return on assets is the ratio of earnings before interest and tax (EBIT) to average total assets. EBIT is calculated by subtracting total expenses from total revenue (including abnormals) and adding back gross interest expense. Average total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period). Data points prior to 1996-97 include data for the former SRA, while data points after this date include data for both the SRA and FreightCorp.

The NRC's returns have declined continually over the period, with negative returns recorded in 1998-99 and 1999-00. The SRA recorded negative returns on assets over much of the reporting period. However, since the NSW rail industry was

6 Asset revaluations may have a significant influence on the return on assets ratio because of their impact on asset values and operating profit (through depreciation expense). Westrail, FreightCorp and Queensland Rail have revalued assets at some stage over the reporting period. In 1999-00, the accumulated balance of these revaluations was around $290 million. Queensland Rail accounted for over 80 per cent of this amount.

restructured in 1996-97, returns have improved with positive returns made since 1998-99.

In most cases, the trend for return on equity within the sector reflects the returns made on assets. One exception is Westrail, which was earning equity returns below zero early in the reporting period. However, from 1998-99 Westrail earned returns above 25 per cent on equity after financial restructuring.[7]

In some cases, the return on assets and equity reflect the impact of abnormal or other items on operating profit. For example, in 1999-00, FreightCorp's return on equity ratio rose, reflecting a negative tax-equivalent expense in anticipation of its sale to the private sector.[8] The SRA improved its profitability in 1998-99 as a direct result of abnormal revenue contributions of $52 million, relating to a transfer of assets from the NSW Department of Transport.

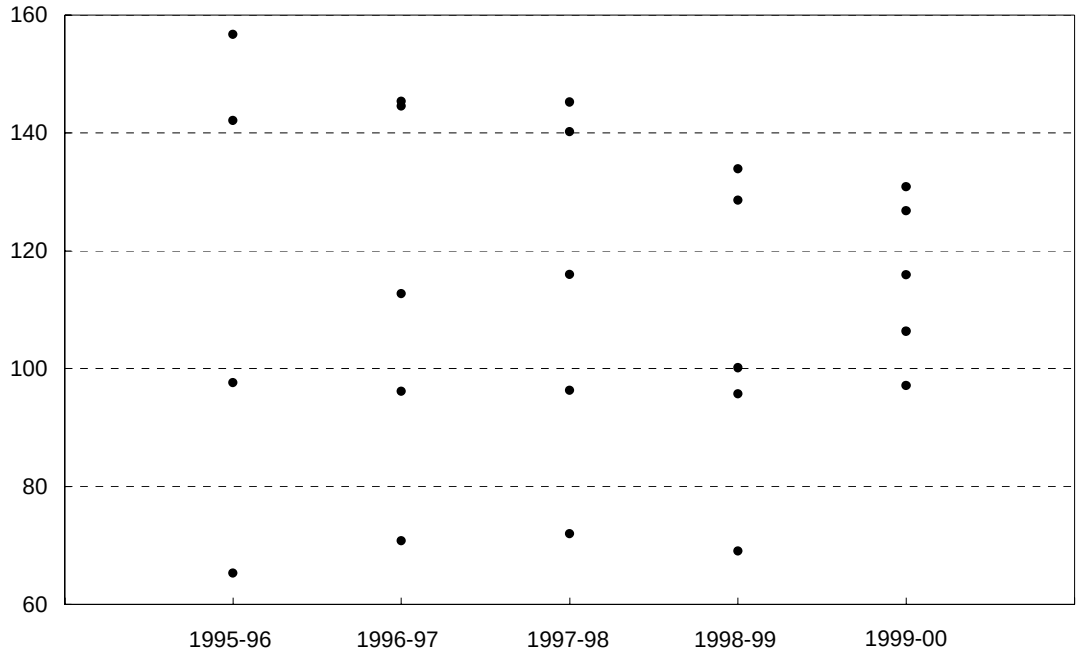
For much of the reporting period, three rail GTEs — Queensland Rail, Westrail and FreightCorp — have more than recovered their operating costs (see figure 5.2). In 1999-00, the SRA recorded a level of cost recovery over 100 per cent for the first time during the reporting period. Prior to this, the cost recovery level for the SRA was below 70 per cent.

The NRC is the only rail GTE not to have recovered operating costs in any year of the reporting period, maintaining a level of cost recovery of around 97 per cent.

7 Return on equity will be negative where a firm is making operating losses or where a firm has negative equity. Equity is negative when liabilities exceed assets.

8 Under accounting standards, future tax liabilities and benefits beyond 2000-01 would not be realisable with the sale of FreightCorp. As a result, tax-equivalent payments were reduced by $42 million for 1999-00 and led to the reporting of a negative tax-equivalent expense of $31 million. The return on equity ratio increases as the numerator used in its calculation is after tax profit.

Figure 5.2 **Cost recovery, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting abnormal revenue, investment income and receipts from governments to cover deficits on operations from total revenue. Expenses from operations are calculated by subtracting abnormal expenses and gross interest expense from total expenses. Data points prior to 1996-97 include data for the former SRA, while data points after this date include data for both the SRA and FreightCorp.

5.4 Financial management

Financial management indicators provide information about the capital structure of GTEs and their ability meet the cost of servicing debt and other liabilities as they fall due. For a more detailed discussion of financial management indicators see chapter 1.

Assessing the financial performance of the rail GTEs is complicated by the financial restructuring that has occurred within the sector. Financial restructuring introduces inconsistencies in the data across time, making comparison difficult.

In 1996-97, Westrail entered into a financial restructuring arrangement with the Western Australian Treasury. Under the agreement, State Treasury assumed responsibility for Westrail's unfunded superannuation liability, valued at around $725 million. Transferring the liability to State Treasury removed it from Westrail's

balance sheet and meant that it was no longer included in the calculation of Westrail's financial ratios in subsequent financial years.

Similarly, it is difficult to make a meaningful assessment of the NRC's financial management performance over this period. Between 1993 and 1996, the NRC received compensation payments from its shareholder governments to assist the NRC in rationalising inefficient functions transferred from State Governments. The compensation payments are included within the data used to calculate the NRC's financial ratios.

The remaining GTEs have not undertaken financial restructuring programs of this magnitude. However, some financial restructuring has occurred. In 1995-96 and 1997-98 respectively, Queensland Rail and FreightCorp changed the basis upon which their debt is valued to more closely reflect market values.[9] It is unclear what effect this had upon Queensland Rail's financial management position as it coincided with asset revaluations and corporatisation, and thus comparisons with the previous year are not possible.

In FreightCorp's case, the change in the measurement basis of borrowings resulted in abnormal losses and a corresponding increase in the carrying amount of borrowings in the balance sheet. Hence, changes in FreightCorp's financial management performance may not reflect a change in FreightCorp's reliance upon debt finance, but the impact of the debt revaluation.

At the end of 1999-00, FreightCorp, Queensland Rail and NRC were carrying debt levels equivalent to between 30 and 50 per cent of their total assets (see figure 5.3). These GTEs maintained this position over most of the reporting period. Westrail consistently maintained a debt to total assets ratio of around 80 per cent over the reporting period. In contrast, the SRA has had a debt to total assets ratio of around 4 per cent, reflecting the relatively low level of debt compared to other rail GTEs.

Most rail GTEs were operating with debt to equity ratios of between 60 and 160 per cent at the end of 1999-00. These GTEs have maintained this level over much of the reporting period. Westrail has reduced its exposure to debt in 1996-97 following financial restructuring. However, with a debt to equity ratio over 600 per cent, it remains substantially above the industry average.

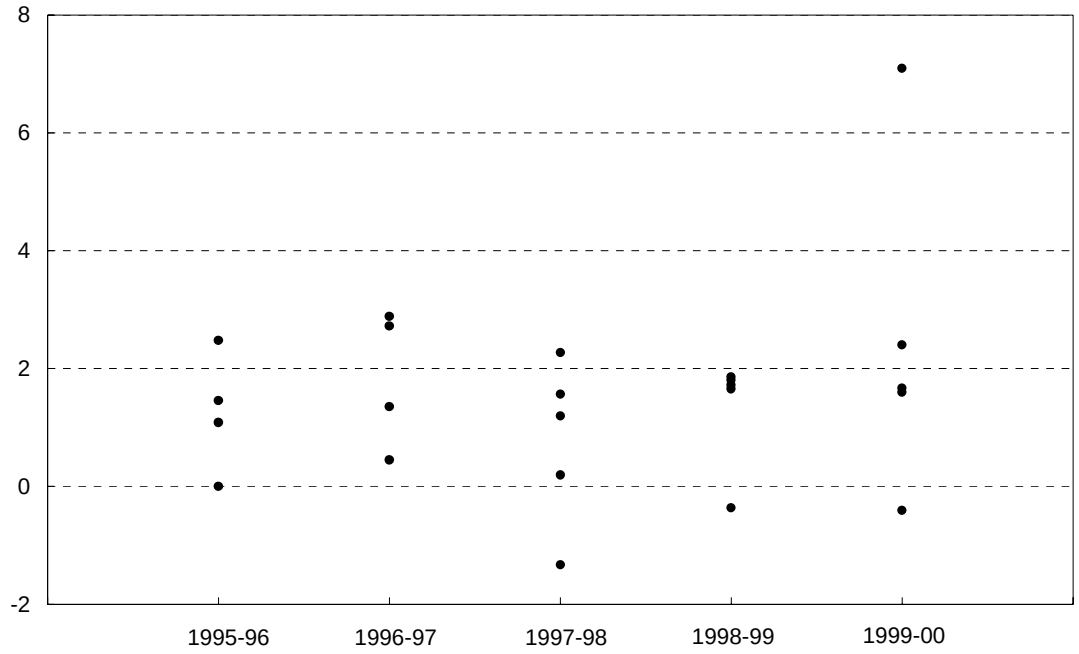
9 Prior to 1997-98, FreightCorp's debt was adjusted by amortising discounts or premiums over the term of the borrowings. Since 1997-98, FreightCorp's borrowings are recognised at the market value at the end of the financial year. Any increase or decrease in market values compared to the carrying amount is recognised as an expense or revenue in that period.

Figure 5.3 **Debt to total assets, 1995-96 to 1999-00 (per cent)**

Note Each data point represents the debt to total assets ratio for a GTE in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowing and finance leases. Total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events. They are measured as the average of the value of assets at the beginning and end of the reporting period. Data points prior to 1996-97 include data for the former SRA, while data points after this date include data for both the SRA and FreightCorp.

Sound financial management requires that profits are 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. At the end of 1999-00, three of the five rail GTEs had an interest cover ratio just under 2 times (see figure 5.4). This suggests that the GTE's profits may be vulnerable to interest rate increases. The SRA recorded the largest improvement in interest cover — from −19 times in 1996-97 to around 7 times in 1999-00. The NRC has had negative interest cover since 1997-98. Interest cover for rail operators in the United States averaged 1.6 times in 1999-00 (Troy 2000).

Figure 5.4 **Interest cover, 1995-96 to 1999-00 (times)**



Note Each data point represents the interest cover ratio for a GTE in that financial year. Interest cover is the ratio of earnings before interest and tax (EBIT) to gross interest expense. EBIT is calculated by subtracting total expenses from total revenue (including abnormals) and adding back gross interest expense. Gross interest expense includes finance charges on all finance leases and all debt related financial expenses. Data points prior to 1996-97 include data for the former SRA, while data points after this date include data for both the SRA and FreightCorp. Between 1995-96 and 1996-97, the SRA had a large negative interest cover, and so interest cover for these years is excluded.

5.5 Financial transactions

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 incentives similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles see chapter 1.

The SRA remained the only rail GTE not subject to a tax-equivalent regime by 1999-00. This may become an issue should the implementation of access regimes raise the possibility of direct competition from third party operators.

Governments act as the shareholder of rail GTEs on behalf of the community. Requiring dividend payments from GTEs is often justified as a return on shareholder funds. The SRA and the NRC are the only rail GTEs not yet subject to a dividend payment policy.

Queensland Rail has been required to make dividend payments since 1995-96 and Westrail and FreightCorp were required to make dividend payments from 1996-97. In 1999-00, these GTEs paid $185 million in dividends, with around 55 per cent distributed by Queensland Rail.

The level of tax-equivalent payments declined by $133 million in 1999-00 compared to 1998-99, when tax-equivalent payments were first made by some rail GTEs. Most of the decline was due to adjustments to future tax benefits and liabilities by GTEs following an announcement of a reduction in the company tax rate applying from 2000-01.[10] Queensland Rail accounted for around 80 per cent of the tax adjustment in the rail sector.

The announcement of the sale of FreightCorp by the NSW Government in September 2000 also led to an adjustment of future tax benefits and liabilities. This reduced FreightCorp's tax-equivalent payments for 1999-00 by $42 million.

Governments were also moving towards identifying, costing and explicitly funding the CSOs provided by rail GTEs. Most of the rail GTEs monitored provided CSOs over the reporting period. CSOs included concession fares to a specified a class of passenger and the provision for low volume freight services.

10 Tax-effect accounting leads to differences in how tax applies to income and the timing of tax payments. Future tax benefits and liabilities were adjusted in 1999-00, in accordance with accounting standards following the announcement of a reduction in the company tax rate. The value of this adjustment, which reduced future tax payable by around $55 million for GTEs in the rail sector, was offset against the value of tax that applied to taxable income in 1999-00.

5.6 GTE performance reports

State Rail Authority (NSW)
Freight Rail Corporation (NSW)
Queensland Rail (Qld)
Westrail (WA)
National Rail Corporation (C'wealth)

STATE RAIL AUTHORITY OF NSW NSW

Prior to 1996-97, the State Rail Authority of NSW (SRA) provided city and country passenger rail services and freight services throughout NSW as well as interstate passenger and freight services. On 1 July 1996, SRA was vertically and horizontally separated into four smaller entities — the SRA, the Rail Access Corporation (RAC), Rail Services Australia (RSA), and the Freight Rail Corporation (FreightCorp) — and some of its functions were transferred to these new entities.[1]

The SRA retained responsibility for the provision of city and country passenger rail services. Its first full year of operation as a separate entity was 1996-97. The SRA's assets declined in that year as some were transferred to the three new entities as part of the restructuring process.

Fares for travel on city rail services are regulated by the NSW Independent Pricing and Regulatory Tribunal (IPART). Fares for travel on country train services are set by the NSW Government.[2]

Increasing fares and patronage in 1999-00 resulted in revenue growth of 2 per cent compared to the previous year. A 2 per cent decline in expenses over the same period led to an improvement in profit (before tax, including abnormals) and other indicators such as the level of cost recovery — which exceeded 100 per cent for the first time over the reporting period.

Several items of capital expenditure for the SRA are largely funded by contributions from the NSW Government. In 1999-00, contributions for capital works and major periodic maintenance accounted for almost 20 per cent of total revenue. An adjustment to equity of $566.4 million was made in 1999-00 following the transfer of the Sydney airport line to the RAC.

The SRA is not required to make dividend or tax-equivalent payments to the NSW Government. It receives community service obligation funding for concession fares provided to specified classes of passengers and to meet revenue shortfalls resulting from the provision of services that are not commercially viable.

---

1 The RAC assumed ownership of rail infrastructure from SRA and is responsible for negotiating the use of the track by rail operators and funding the upkeep of the track. The RSA assumed responsibility for maintenance of the track under contract to the RAC and also provides construction and rollingstock overhaul and repair services. FreightCorp provides freight services throughout NSW.

2 Fares for country services increased by 8 per cent on 19 July 1999. Following an IPART determination in July 1999, fares for travel on city rail services increased by an average of 14 per cent from 1 August 1999.

STATE RAIL AUTHORITY OF NSW (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	12 466	4 622	4 528	5 450	5 356
Total revenue	$M	1 675	1 236	1 566	1 590	1 613
Profitability						
Operating profit before tax (includes abnormals)	$'000	-746 006	-448 796	-45 384	13 530	84 134
Operating sales margin	%	-42.0	-34.6	-1.8	1.8	6.0
Cost recovery	%	65.3	70.8	72.0	69.1	106.3
Return on assets	%	-5.6	-5.0	-0.6	0.6	1.8
Return on equity	%	-7.5	-6.7	-1.3	0.4	2.0
Financial management						
Debt to equity	%	6.7	5.6	5.8	4.5	4.8
Debt to total assets	%	5.4	2.2	4.2	3.8	3.7
Total liabilities to equity	%	25.2	35.6	35.3	29.3	30.5
Interest cover	times	-13.3	-19.0	-1.3	1.7	7.1
Current ratio	%	48.5	48.8	46.5	37.0	31.5
Leverage ratio	%	125.2	135.6	135.3	129.3	130.5
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0	0	0	0	0
Dividend payout ratio	%	0	0	0	0	0
Income tax expense	$'000	0	0	0	0	0
CSO funding[e]	$'000	421 052	507 501	495 525	483 650	478 900

a Fall in total assets due to asset divestiture associated with the restructure of SRA (State Rail Authority). **b** Higher revenues are the result of the sale of property, plant and equipment along with slightly higher passenger revenues. **c** Revenues increased due to asset disposal proceeds, higher passenger revenues, increases in NSW Government operating subsidies, interest received and other non-operating revenues. Operating profit is the result of a $51.6 million contribution from abnormal revenues. Abnormal revenues comprised a capital grant from the NSW Government for car parks, and bus and rail interchanges transferred from the Department of Transport. **d** In June 2000, the value of land was revalued upwards by $147 million and the value of buildings was revalued upwards by $304 million. Net assets to the value of $564 million were transferred to the Rail Access Corporation. **e** The SRA's community service obligations include concession fares to specified classes of passengers and revenue shortfalls resulting from providing services that are not commercially viable at the request of the NSW Government.

FREIGHT RAIL CORPORATION OF NSW NSW

The Freight Rail Corporation (FreightCorp) of NSW began operating in 1996-97 following the NSW Government's restructure of the State Rail Authority. FreightCorp is a statutory government-owned corporation undertaking 'above rail' freight operations.[1] It operates locomotives, wagons and other services. It purchases track services from the Rail Access Corporation for which it pays a charge.

Reductions in rail access charges that were passed on to customers contributed to a 5 per cent fall in revenue in 1999-00. The total volume of goods transported by FreightCorp in 1999-00 was similar to the previous year. The increase in profit (before tax, including abnormals) reflected a 10 per cent reduction in expenses.

FreightCorp has reduced its level of borrowings each year since 1996-97. The consequential reduction in the level of debt has led to improvements in debt to equity and debt to total assets over the reporting period.

FreightCorp is required to make tax-equivalent and dividend payments to the NSW Government. A write-back of deferred tax balances of $42 million resulted in FreightCorp reporting a negative tax-equivalent payment in 1999-00.[2]

Dividend payments to the NSW Government exceeded operating profit before tax (including abnormals) in 1997-98 and were 60 per cent of operating profits in 1998-99. In both years, dividend payments were met out of retained earnings from previous years.

FreightCorp has a community service obligation contract with the NSW Government to provide freight train services to regional areas at a non-commercial rate. The rates charged are determined by FreightCorp and are set at the level required to keep freight on rail.

1 'Above rail' refers to the services provided using locomotives, wagons, terminals and maintenance facilities. Below rail includes the track, stations, signalling and other infrastructure used for running train services.

2 The NSW Government announced its intention to sell FreightCorp in September 2000. Accounting standards require FreightCorp to write-back future tax liabilities and benefits that would not be realised.

FREIGHT RAIL CORPORATION OF NSW (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*
Size						
Total assets	$M	n.r.	1 075	959	985	951
Total revenue	$M	n.r.	832	772	690	642
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	106 304	14 158	33 660	55 466
Operating sales margin	%	n.r.	15.6	7.8	9.9	13.7
Cost recovery	%	n.r.	112.7	116.0	100.1	115.9
Return on assets	%	n.r.	12.9	6.3	6.9	9.1
Return on equity	%	n.r.	27.9	3.6	2.6	18.0
Financial management						
Debt to equity	%	n.r.	191.4	83.2	76.6	67.7
Debt to total assets	%	n.r.	56.8	37.3	37.4	34.4
Total liabilities to equity	%	n.r.	261.6	110.5	107.3	93.1
Interest cover	times	n.r.	2.9	1.2	1.8	2.4
Current ratio	%	n.r.	127.3	159.0	121.4	154.3
Leverage ratio	%	n.r.	138.2	190.5	193.2	207.4
Payments to and from government						
Dividends	$'000	n.r.	42 228	23 288	20 000	36 191
Dividend to equity ratio	%	n.r.	14.2	6.2	4.3	7.5
Dividend payout ratio	%	n.r.	51.0	171.6[d]	166.3[d]	41.5
Income tax expense	$'000	n.r.	23 494	590	21631	-31 762[e]
CSO funding	$'000	n.r.	60 618	90 000[f]	80 000	76 500

a FreightCorp began operating as a separate entity in 1996-97 following the restructure of State Rail Authority. **b** Operating profits declined as a result of abnormal expenses totalling $45.9 million. These expenses were related to restructuring costs associated with redundancies and debt. Redundancy costs include provision for severance payments. In previous years, debt had been valued at face value after deducting any unamortised discounts. FreightCorp changed the measurement of its borrowings to reflect market value. **c** Operating profits improved due to lower abnormal expenses of $13 million. **d** Dividend payouts have been funded by drawing upon retained earnings from previous years. **e** Includes a write-back of deferred tax balances of $42 million. A fall in the future company tax rate also reduced tax payable by $6.4 million. **f** The increase in community service obligation payments reflects a corresponding increase in access charges paid by FreightCorp in providing these services. **n.r.** Not relevant.

QUEENSLAND RAIL QUEENSLAND

Queensland Rail (QR) provides freight services throughout regional Queensland and operates passenger rail services in the Brisbane metropolitan area and between key regional centres. QR was corporatised in 1995.

Upon corporatisation, QR's fixed assets were revalued to reflect their market value and borrowings were brought to account at their market value. Total assets have increased over the reporting period as QR has undertaken a major capital works program, including new rollingstock and track.

Downward pressure on freight rates and an increase in the freight and passenger transport task over the reporting period have led to expenses increasing annually by 5.9 per cent, and revenue growing annually by 1.4 per cent since 1996-97. As a result, the level of profit in 1999-00 is around 45 per cent lower than the level recorded in 1996-97.

A higher level of payments from government and increases in coal and freight revenues underpinned an improvement in the level of profit (before tax, including abnormals) in 1999-00 compared to the previous year. QR entered into a cross-border lease transaction resulting in a profit on the sale of assets of $232 million. However, the asset values were simultaneously written-down by a corresponding amount, resulting in no impact on net profit.

The level of debt has increased from $1.5 billion to $1.9 billion over the reporting period, as a consequence of QR's capital works program. This is reflected in a rise in debt to equity and debt to total assets ratios and a decline in interest cover.

QR makes income tax-equivalent and dividend payments to the Queensland Government. The negative income tax expense reported in 1999-00 mainly reflects a reduction of $46.6 million due to a fall in the future company tax rate.

QR has service contracts with the Queensland Department of Transport. The Department makes payments for community services provided by QR for urban and intercity passenger services, low volume freight services and infrastructure. QR also received direct reimbursements from various State Government departments for concessions provided to senior citizens, pensioners and students.[1]

1 In 1999-00, QR received $27.1 million from the Queensland Department of Family, Youth and Community Services for senior pensioner concessions.

QUEENSLAND RAIL (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[a]	*1997-98*	*1998-99*	*1999-00*
Size						
Total assets	$M	5 846	6 487	7 031	7 609	7 796
Total revenue	$M	1 785	1 995	1 896	1 902	2 083
Profitability						
Operating profit before tax (includes abnormals)	$'000	315 895	389 020	304 609	167 886	176 817
Operating sales margin	%	29.6	30.8	28.7	22.2	21.1
Cost recovery	%	142.1	144.5	140.2	128.6	126.8
Return on assets	%	8.1	10.0	8.1	5.8	5.7
Return on equity	%	6.4	11.5	7.7	4.1	7.4
Financial management						
Debt to equity	%	105.0	108.5	116.5	126.9	158.8
Debt to total assets	%	36.3	41.1	43.3	44.6	48.0
Total liabilities to equity	%	158.9	177.6	180.3	195.6	234.6
Interest cover	times	2.5	2.7	2.3	1.7	1.7
Current ratio	%	81.2	77.7	106.7	134.0	87.1
Leverage ratio	%	258.9	277.6	280.3	295.6	334.6
Payments to and from government						
Dividends	$'000	160 611	240 345[b]	100 000	95 000	101 000
Dividend to equity ratio	%	5.1	10.5	4.1	3.7	4.1
Dividend payout ratio	%	80.0	91.3	53.4[c]	91.1	55.8
Income tax expense	$'000	115 246	125 893	117 301	63 656	-4 301[d]
CSO funding[e]	$'000	595 252	659 325	541 568[f]	533 417	670 826

a Does not include contributions from developers. **b** The 1996-97 dividend figure includes $36.7 million paid in that year, but which relates to the 1995-96 financial year. **c** Dividend payout ratio declined as the reduction in tax was not as great as the decline in operating profit. This is due to an under-provision for tax made in the previous financial year. **d** The negative income tax expense is largely the result of a decrease of $46.6 million due to a fall in the future company tax rate. **e** QR receives community service obligation payments from the Queensland Government for certain freight and passenger rail services. Contributions received in respect of passenger services are for Citytrain, Traveltrain and the Brisbane to border portion of interstate services. Contributions received in respect of freight services are for low volume routes and Q-Link operations. QR also receives amounts for reimbursement of concessions provided to senior citizens, pensioners and students. **f** Community service obligation funding was reduced following a decision by the Queensland Government.

WESTRAIL — WESTERN AUSTRALIA

Westrail is the trading name of the Western Australian Government Railways Commission. It provides urban and regional passenger and freight services throughout Western Australia. Westrail's country passenger services involve the operation of both trains and road coaches. The Perth metropolitan rail service is operated under contract to the Department of Transport.

On 30 May 2000, the Western Australian Government sought expressions of interest for the purchase of Westrail's freight operations.[1]

Revenue growth in 1999-00 reflected an increase in grain, mining and other freight services.[2] However, the decline in the operating sales margin and cost recovery ratio reflects an increase in expenses as a result of higher fuel and maintenance costs. Profit before tax (including abnormals) was enhanced due to abnormal gains of $42 million relating to land rationalisation ($25.9 million) and asset contributions ($16.1 million). This was partly offset by abnormal expenses relating to depreciation on a written-off asset ($7.2 million), freight rate adjustment ($0.9 million) and legal settlements ($0.5 million).

The growth in Westrail's assets in 1999-00 reflects capital expenditure of $127.4 million. Over 90 per cent of investment was for Westrail's freight operations. An increase in debt to equity and interest cover ratios reflects an increase in the level of borrowings by $69 million in 1999-00.

Westrail has been required to make dividend and tax-equivalent payments since 1996-97. Westrail receives funding for the provision of community service obligations relating to the provision of country rail and coach services and pensioner concessions.

1 On 18 December 2000, the sale of the Westrail freight business to Australian Railroad Group (ARG) was finalised. ARG paid the State Government $585 million and committed to invest a further $400 million in the State's rail system over the next five years. The remaining parts of Westrail's activities will be operated by Western Australian Government Railways.

2 Westrail's freight business accounts for over 60 per cent of total revenue.

WESTRAIL (continued)

Performance indicators 1995 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	1 060	1 137	1 244	1 337	1 407
Total revenue	$M	439	418	420	452	456
Profitability						
Operating profit before tax (includes abnormals)	$'000	41 127	30 684	46 554	69 023	49 020
Operating sales margin	%	29.8	28.0	30.5	33.0	28.8
Cost recovery	%	156.7	145.3	145.2	133.9	130.9
Return on assets	%	12.5	10.7	10.8	11.6	9.6
Return on equity	%	-6.3	-7.8	13.9	37.7	29.1
Financial management						
Debt to equity	%	-137.5	682.5	718.6	626.9	667.9
Debt to total assets	%	82.9	81.5	81.7	79.9	80.2
Total liabilities to equity	%	-266.5	766.5	819.3	712.7	754.0
Interest cover	times	1.5	1.4	1.6	1.9	1.6
Current ratio	%	40.1	44.2	34.9	28.5	39.3
Leverage ratio	%	-166.5	866.5	919.3	812.7	854.0
Payments to and from government						
Dividends	$'000	0	1 508	32 868	44 744	47 569
Dividend to equity ratio	%	0	-0.6	24.7	29.8	28.9
Dividend payout ratio	%	0	7.6	177.6	79.1	99.4
Income tax expense	$'000	0	10 926	28 043	12 437	1 180[e]
CSO funding	$'000	0	19 870	19 711	19 547	21 116

a Westrail incurred an abnormal expense totalling $11.8 million. State Treasury assumed Westrail's unfunded superannuation liability totalling $725 million. A financial restructuring package negotiated with State Treasury introduced direct funding of Westrail's community service obligations and the introduction of a tax-equivalent regime. **b** Includes abnormal revenue of $402 000. **c** Includes abnormal revenue of $48 million. **d** Includes abnormal revenue relating to land rationalisation ($25.9 million) and asset contributions ($16.1 million). This was partly offset by abnormal expenses relating to depreciation on a written-off asset ($7.2 million), freight rate adjustment ($0.9 million) and legal settlements ($0.5 million). **e** Tax-equivalent payments were reduced by $1.7 million as a result of a fall in the future company tax rate.

NATIONAL RAIL CORPORATION — COMMONWEALTH

The Commonwealth, New South Wales, Victorian, Queensland, South Australian and Western Australian Governments established the National Rail Corporation (NRC) in 1991, for the purpose of providing interstate rail freight transport services. The NRC began operations in 1993, focusing on creating a modern business by process re-engineering, upgrading, replacing key assets and systems, and improving relationships with customers in its first five years of operation.

In 1993, the NRC's three shareholders — the Commonwealth, New South Wales and Victorian Governments — agreed to underwrite the NRC's restructuring. The agreement committed each shareholder to cash equity injections, the transfer of selected nominated assets and the making of payments which were to compensate the NRC for any losses incurred from transferred functions. Compensation payments aimed to assist the NRC in restructuring and improving the productivity of inefficient functions, prior to the NRC assuming full responsibility for the business at the end of the transitional period in 1996.

NRC shareholders signed an agreement in May 2000 to sell 100 per cent of the company's shares to the private sector.

Assessing the NRC's financial performance over the reporting period is difficult because of the restructuring that was occurring. For example, profits over the first few years of the reporting period cannot be used as a measure of financial performance because of the payments being made by shareholder governments to the NRC.

The increase in revenue in 1999-00 was offset by a proportional rise in expenses due to higher fuel prices. As a result, operating profit (before tax, including abnormals) was similar to the previous year. A reduction in investments by $99 million led to a fall in the current ratio in 1999-00. The level of borrowings declined by $13 million but this did not significantly affect debt to equity or debt to total assets ratios.

NATIONAL RAIL CORPORATION (continued)

Performance indicators 1995 to 1999-00

	Units	*1995-96*[a]	*1996-97*[a]	*1997-98*[b]	*1998-99*	*1999-00*
Size						
Total assets	$M	846	862	897	825	767
Total revenue	$M	539	516	495	431	466
Profitability						
Operating profit before tax (includes abnormals)	$'000	1 917	-14 141	-20 406	- 31 556	- 30 063
Operating sales margin	%	-2.4	-2.1	-1.5	-4.2	-3.0
Cost recovery	%	97.6	96.1	96.3	95.7	97.1
Return on assets	%	4.1	1.3	0.6	-1.0	-1.1
Return on equity	%	0.3	-3.6	-2.3	-7.2	-7.3
Financial management						
Debt to equity	%	82.5	74.1	75.8	80.0	81.5
Debt to total assets	%	49.6	34.9	33.9	33.2	33.0
Total liabilities to equity	%	133.2	114.4	128.1	131.0	138.2
Interest cover	times	1.1	0.4	0.2	-0.4	-0.4
Current ratio	%	377.3	211.5	121.0	103.3	62.8
Leverage ratio	%	142.1	139.9	172.8	180.8	173.4
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0	0	0	0	0
Dividend payout ratio	%	0	0	0	0	0
Income tax expense	$'000	912	-285	-11 434	-4 480	-5 104
CSO funding	$'000	0	0	0	0	0

a Profits over the first few years of the reporting period cannot be used as a measure of financial performance because of the compensation payments being made by shareholder governments to the NRC. **b** Shareholder compensation payments were reduced by $25 million and ceased entirely in February 1998.

6 Ports

Fifteen port government trading enterprises (GTEs) are covered in this chapter. In 1999-00, these GTEs were responsible for assets valued at $3.2 billion and earned over $643 million in revenue.

These GTEs vary in size and the range of services they provide. The principal activities undertaken by these GTEs include the provision and maintenance of port infrastructure and port services such as mooring, stevedoring and pilotage.

Financial performance summaries including performance indicators for each GTE are presented after this introduction. The performance indicators are consistent across individual GTEs. However, when making comparisons, care should be taken to consider changes in market environments, and timing and valuation issues relating to chosen accounting methods.

For a discussion of the data and the performance indicators used and some of the factors that should be considered when assessing performance see chapter 1.

6.1 Sector reforms

Industry reforms within the ports sector have been aimed at improving the efficiency and financial performance of GTEs by making them more commercially focused. In general the reform process has been consistent with the recommendations set out in the 1993 Industry Commission report *Port Authority Services and Activities* (Meyrick and Associates 1998). Some of the major recommendations to come from the Commission's report included:

- 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 and pay dividends from after tax profits;
- the adoption, where cost efficient, of a landlord model of operation;[1] and

[1] The landlord model is characterised by the port authority concentrating on the supply of core activities only, with the more contestable waterfront services, such as stevedoring and pilotage supplied privately.

- where the landlord model is adopted, governments should identify and divest non-core activities and contract out, where cost affective, core activities.

The primary aim of these reforms has been to replicate market disciplines, including the establishment of clear objectives that eliminate any conflict between commercial and non-commercial objectives. Reform has also seen an increase in the scope for competition in the provision of port services, mainly through the competitive tendering and contracting out to private operators of activities such as stevedoring, pilotage, mooring, general maintenance and ship cleaning.

As a result of these reforms, individual GTEs experienced structural, institutional and commercial change during the reporting period (see table 6.1). The majority of restructuring occurred at the beginning of the reporting period. In 1995-96, three independent port corporations replaced the former Maritime Services Board of New South Wales.[2] In the same year, the Port of Melbourne Authority was divided into three separate entities.[3]

2 Newcastle Port Corporation, Port Kembla Port Corporation and Sydney Port Corporation were established.

3 Only two of these entities are monitored by this report, namely, the Melbourne Port Corporation and the Victorian Channels Authority.

Table 6.1 **Monitored port GTEs, 1995-96 to 1999-00**

1995-96	*1996-97*	*1997-98*	*1998-99*	*1999-00*
***New South Wales*[a]**				
Newcastle Port Corporation	→	→	→	Newcastle Port Corporation
Port Kembla Port Corporation	→	→	→	Port Kembla Port Corporation
Sydney Ports Corporation	→	→	→	Sydney Ports Corporation
***Victoria*[b]**				
Melbourne Port Corporation	→	→	→	Melbourne Port Corporation
Victorian Channels Authority	→	→	→	Victorian Channels Authority
Queensland				
Gladstone Port Authority	→	→	→	Gladstone Port Authority
Port of Brisbane Corporation	→	→	→	Port of Brisbane Corporation

[a] In 1995-96 the former the Maritime Services Board was dissolved and the Newcastle Port Corporation, Port Kembla Port Corporation and Sydney Ports Corporations were established. [b] In 1995-96 the former Port of Melbourne Authority was disaggregated into the Melbourne Port Corporation and the Victorian Channels Authority.

(Continued next page)

Table 6.1 (continued) **Monitored port GTEs, 1995-96 to 1999-00**

1995-96	*1996-97*	*1997-98*	*1998-99*	*1999-00*
Western Australia				
Fremantle Port Authority	→	→	→	Fremantle Port Authority
		Bunbury Port Authority[c] →	→	Bunbury Port Authority[d]
South Australia				
South Australian Ports Corporation	→	→	→	South Australian Ports Corporation
Tasmania				
Burnie Port Authority →	Burnie Port Corporation →	→	→	Burnie Port Corporation
Marine Board of Hobart →	Hobart Ports Corporation →	→	→	Hobart Ports Corporation
Port of Launceston →	Port of Launceston Pty Ltd →	→	→	Port of Launceston Pty Ltd
Port of Devonport Authority →	Port of Devonport Corporation →	→	→	Port of Devonport Corporation
Northern Territory				
Darwin Port Authority	→	→	→	Darwin Port Corporation[e]

[c] Bunbury Port Authority was not monitored prior to 1997-98. [d] Bunbury Port Authority was corporatised in 1999-00. [e] The Darwin Port Corporation was established in September 1999.

The operational models adopted by individual GTEs differ greatly. Some of the factors that may have influenced the choice of model are government objectives and the type and volume of trade throughput. This variation in operational models can blur the distinction between core and non-core port services and activities.

A number of reforms have led to improved pricing and allocative mechanisms being implemented over the reporting period. Consumption-based charging has been progressively introduced, resulting in port users incurring charges that relate to their individual service requirements, rather than the value of their cargo.

Despite the increasing use of consumption-based charges, inconsistencies remain in the types of charges levied across port GTEs for the provision of like services. Furthermore, the determination of port charges differs across jurisdictions. In some States, port charges are determined externally by independent pricing regulators, while in others, individual ports have more autonomy in setting charges. For example, the port charges of the Melbourne Port Corporation and the Victorian Channels Authority are determined by the Office of the Regulator-General (ORG), using incentive regulation.

6.2 Market environment

The level of revenue generated by port GTEs is strongly linked to trade throughput. Trade throughput is susceptible to changes in both domestic and international markets, particularly shifts in demand for key trade commodities. However, changing market environments do not impact on all GTEs uniformly because of differences in the composition and size of the markets served. The changes in market environment that can broadly be defined as common across all ports over the reporting period, include:

- an increase in the average total tonnage per ship visit resulting in a reduction in the number of ship visits and the unit cost of exchanging cargo;[1] and
- a fall in trade throughput resulting from a slump in demand, particularly from the Asian region. Trade throughput, for those ports monitored, recovered in 1999-00 with a 4.7 million increase in mass tonnes (AAPMA 2001).

Port specific changes in market environment have also affected the performance of particular ports. Examples of these changes include:

- the closure of BHP steel making facilities in Newcastle; and

1 Particularly towage and port authority tonnage charges.

- the cessation of general cargo shipping operated by Coastal Express Line at Port Launceston.

The market environment port GTEs face is dynamic. Port GTEs that have a diversified trade portfolio — both source and type of trade throughput — reduce the risk associated with changes in market environment. However, the extent to which a port GTE can diversify its operations depends on its size, location and government policy.

6.3 Profitability

Profitability indicators provide information on how GTEs are using the assets vested in them by shareholder governments to generate earnings. For a more detailed discussion of profitability indicators see chapter 1.

GTEs experienced substantial variation in their profitability indicators over the reporting period. This variation can largely be explained by abnormal items — either through their impact on operating profit, total assets or a combination of the two. In 1999-00, GTEs reported around $41 million in abnormal revenues and $94 million in abnormal expenses. This accounts for 6 per cent of total revenue and 18 per cent of total expenses.

Abnormal items include:

- Abnormal revenues — interest earned from superannuation reserves not previously accounted for, asset sales, subsidies from government that inflate operating profit before tax (including abnormals) and the return on assets ratio; and
- Abnormal expenses — downward revaluations of non-current assets, debt refinancing, redundancy payments, losses on disposal of assets and major cyclical asset maintenance (see box 6.1) that deflate operating profit before tax (including abnormals) and the return on assets ratio.

Box 6.1 **Major cyclical asset maintenance**

Issues relating to major non-current asset maintenance are significant to port GTEs for two reasons. First, the majority of Australian port channels require dredging at regular intervals to maintain channel depth. Second, past methods of accounting for major port maintenance involved adjustments to asset values or operating profit, thereby affecting measured performance.

Many port GTEs account for the continued deterioration in channels by making a charge to the profit and loss statement. This charge is calculated on the basis of the time expired since the last major maintenance cycle. In May 1999, the Urgent Issues Group of the Australian Accounting Research Foundation released Abstract 26: 'Accounting for Major Cyclical Maintenance'. The amended accounting treatment requires that provisions for future maintenance must not be recognised as a liability, or as accumulated depreciation, or as a reduction in the carrying value of an asset. As a result, charges to the profit and loss statement for the future removal of accumulated siltation in channels ceased.

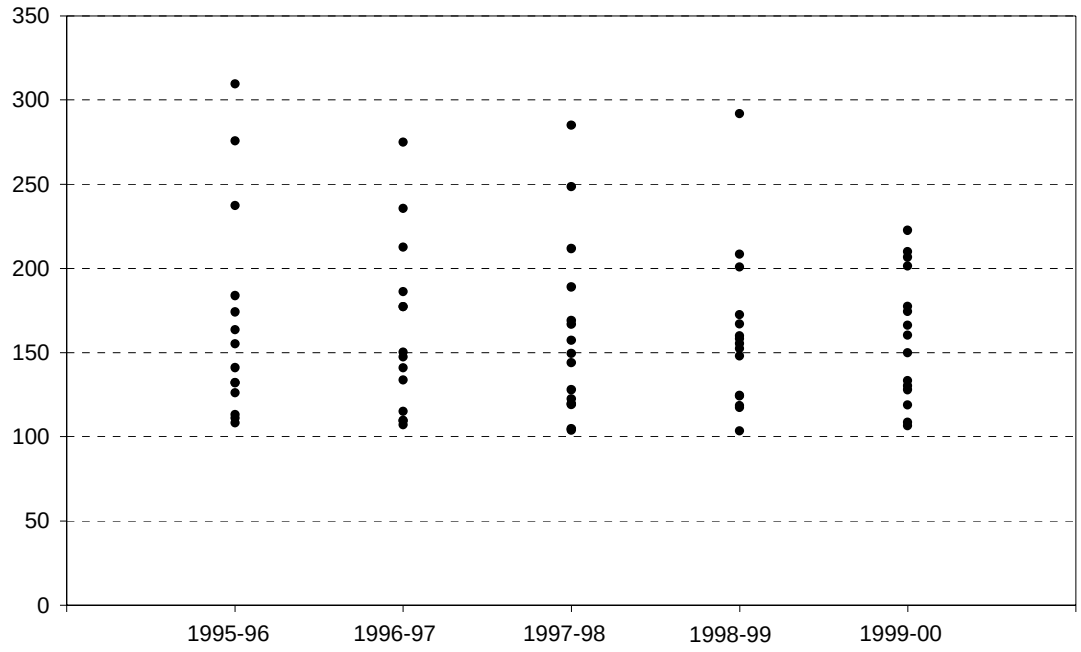
The change in accounting policy results in profits being overstated in the years until the next major maintenance dredging cycle. Thereafter, the cost of major non-current cyclical maintenance will be amortised over the next cycle with corresponding reductions in profits.

Abstract 26 applied to all port GTEs for reporting periods ending on or after 30 June 1999. Any adjustments arising from the application of Abstract 26 was adjusted against retained profits or accumulated losses as at 1 July 1998 — for example, the Port Kembla Port Corporation and Victorian Channels Authority annual reports for 1998-99.

Over the reporting period, the ports sector as a whole recorded an average annual growth rate for operating profit before tax (including abnormals) of 5.7 per cent. That said, the performance of individual GTEs has been more variable. Nearly all of this variability can be attributed to losses resulting from abnormal items, in particular write-downs on assets resulting from revaluations. For example, the Darwin Port Corporation recorded a loss in 1999-00 due to abnormal expense of $60.6 million attributable to the revaluation of assets.

Over the reporting period, all port GTEs recovered over 100 per cent of operating expenses (see figure 6.1). Although there is no clear industry trend in cost recovery over the period, the maintenance of cost recovery, despite reductions in port charges and a period of low demand for Australian exports from the Asian region, indicates an improvement in the recovery of costs.

Figure 6.1 **Cost recovery, 1995-96 to 1999-00 (per cent)**



Note Each data point represents the cost recovery ratio for a GTE in that financial year. Cost recovery is the ratio of revenue from operations to expenses from operations. Revenue from operations is calculated by subtracting abnormal revenue, investment income and receipts from governments to cover deficits on operations from total revenue. Expenses from operations are calculated by subtracting abnormal expenses and gross interest expense from total expenses.

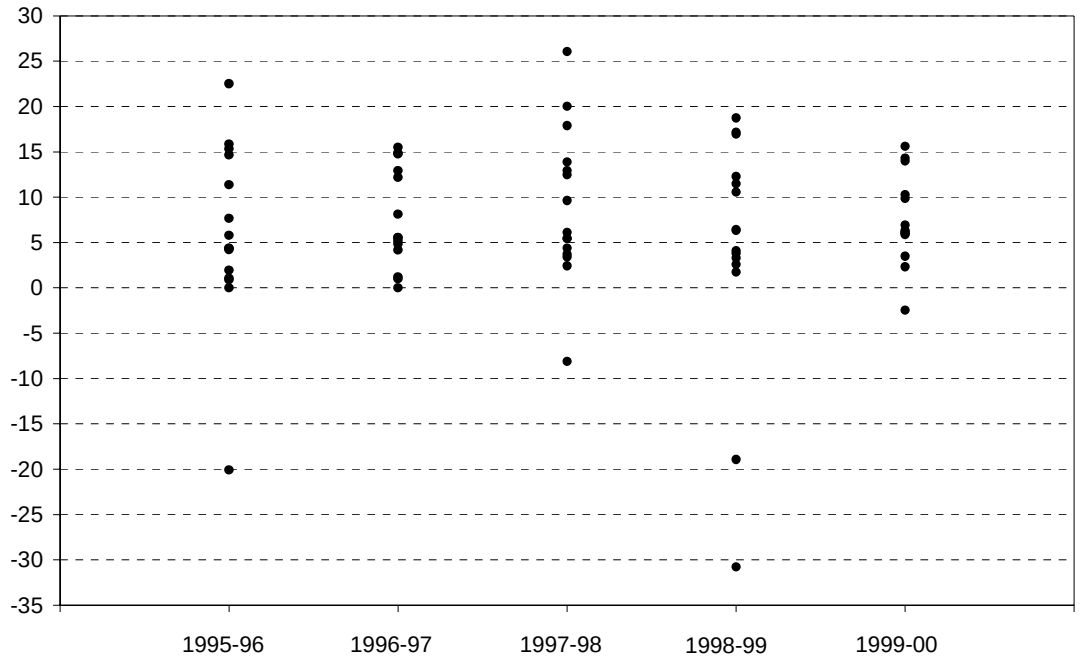
The average return on assets for the sector has fluctuated over the reporting period. The average in 1995-96 was 6.1 per cent, fell to 2.5 per cent in 1998-99 and was 6.1 per cent in 1999-00. This variability is mirrored in rates of return generated by individual GTEs (see figure 6.2).

The rate of return for the sector as a whole in 1999-00, was below that recorded for 10 year bonds.[2] After discounting the short-term positive effects on profits from the adoption of new accounting standards for cyclical maintenance, it is reasonable to expect that the appropriate return for these GTEs should be at least equal or above the long-term bond rate.

Asset revaluations account for the majority of the variation in the return on assets ratio over the reporting period. The largest downward asset revaluation occurred in 1999-00 at Darwin Port Corporation — assets were revalued downward by 52 per cent. Consequently, operating profit before tax (including abnormals) was negative, resulting in a negative return on assets. Gladstone Port Authority and Port Kembla Port Corporation experienced similar results in 1998-99.

2 The rate of return for 10 years bonds recorded at June 2000 was 6.6 per cent.

Figure 6.2 **Return on assets, 1995-96 to 1999-00 (per cent)**



Note Only positive return on assets ratios were included. 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 (includes abnormals) and adding back gross interest expense. Average total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period). This figure excludes two outlying data points. In 1996-97 the Victorian Channels Authority had a return on assets of 61 per cent and in 1999-00 the Darwin Port Corporation had a return of -46.9 per cent.

Significant upward revaluations have also occurred. For example, Sydney Ports Corporation's assets were revalued upward by 67 per cent in 1997-98. The largest increase in asset value occurred in 1999-00 when the value of the Victorian Channels Authority's assets increased by 175 per cent due to the recognition, as assets, of channels valued at $78 million.

The Burnie Port Corporation and Darwin Port Corporation earned negative returns on assets in 1999-00. These returns were the result of large downward asset revaluations culminating in operating losses before tax (including abnormals).

Another measure of profitability is return on equity — the rate of earnings on capital provided by shareholder governments. In the case of GTEs, returns on equity closely follow the returns on assets.

The ORG proposed benchmark return on equity of 7.3 per cent for Melbourne Port Corporation and 6.7 per cent for the Victorian Channels Authority (ORG 2000).

The studied GTEs appear to have performed poorly when compared to the ORG benchmark. In 1999-00, only five GTEs had a return on equity of above 7 per cent, a similar result to the six GTEs in the previous year.

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. For a more detailed discussion of financial management indicators see chapter 1.

Over the reporting period, port GTE debt to total asset ratios have not only been influenced by the acquisition and retirement of debt, but also through changes in the total value of port assets (see figure 6.3). Asset revaluations have a large impact on this ratio. For example, Sydney Ports Corporation's debt to total assets fell from 45 per cent to 28 per cent with no change in debt levels over the period 1996-97 to 1998-99.[3]

Apart from the impact of abnormal items on the debt to total assets ratio, improvements in some GTE's debt positions have been achieved through the retirement of debt. For example, Gladstone Port Authority achieved a 77 per cent reduction in debt levels over the reporting period and as a result debt to total assets fell from 11.1 per cent in 1995-96 to 3.1 per cent in 1999-00.

Another measure of financial management is interest cover. The sector average in 1999-00 was 3.3 times, which was an improvement over the previous year (1.3 times). A rule of thumb in financial analysis is that the minimum acceptable level lies between 3 to 4 times (Hoggett and Edwards 2000). In 1999-00, five GTEs achieved ratios below three times as compared to ten in 1998-99. Consequently, there has been a reduction in the risk that financial commitments may need to be met from sources of funds other than earnings from operations.

3 Sydney Ports Corporation's assets increased by 85 per cent in value terms between 1996-97 and 1998-99.

Figure 6.3 **Debt to total assets, 1995-96 to 1999-00 (per cent)**

Note Each data point represents the debt to total assets ratio for a GTE in that financial year. Debt is defined to include all repayable borrowings (interest bearing and non-interest bearing), interest bearing non-repayable borrowings and finance leases. Total assets are defined as the service potential or future economic benefits, controlled by the entity as a result of past transactions or other events (measured as the average of the value of assets at the beginning and end of the reporting period).

Abnormal items have a substantial impact on the interest cover ratio. For example, Port Kembla Port Corporation's interest cover increased from -6.4 times in 1998-99 to 2.8 times in 1999-00 due to abnormal expenses — in particular a $42.1 million downward asset revaluation in 1998-99.

The liquidity of some port GTEs has decreased over the reporting period. For example, the current ratio for the Hobart Ports Corporation has fallen from 594 per cent at the beginning of the reporting period to 147 per cent in 1999-00.

6.5 Financial transactions

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 incentives and regulations similar to those faced by private sector businesses. For a more detailed discussion of competitive neutrality principles see chapter 1.

Owner governments invariably require their GTEs to make tax-equivalent and dividend payments along with debt guarantee fees. These measures were designed

to encourage GTEs to act in a more commercial manner and have resulted in an increase in payments to governments.

The amount of dividend payable by each GTE depends on the dividend policy of the State or Territory government. In 1999-00, most GTE dividend payout ratios were 50 per cent or above. The Victorian Channels Authority had a ratio over 100 per cent which may indicate a decline in retained profits.

Income tax expense decreased in 1999-00 as a result of a reduction in the future company tax rate.[4] Until 1999-00, tax-equivalent payments were based on a company tax rate of 36 per cent. Due to timing differences and the adoption of tax-effect accounting, tax expense incurred in any given year may differ from the actual amount of tax payable. Changes in the company tax rate, effective from 2000-01, led to a restatement of future tax payments in 1999-00. Across the sector, this adjustment resulted in a one-off reduction in tax-equivalent payments of $11 million.

The reform process aimed to distinguish between commercial and non-commercial activities. Port GTEs required to undertake non-commercial activities should receive community service obligation (CSO) payments from shareholder governments equivalent to the cost of provision.

Darwin Port Corporation and Port Kembla Port Corporation are the only GTEs to receive CSO payments. Many other port GTEs are expected to undertake non-commercial activities, but do not receive CSO payments.

In 1999-00, Port Kembla received CSO funding valued at $4.5 million. The payment is provided as compensation for the shortfall to income generated by the NSW Rental Relief Scheme for the Port Kembla Coal Terminal. The Scheme is aimed at providing assistance to the coal industry through reducing the cost of coal loaded at Port Kembla by 70 cents per tonne.

4 The company tax rate will fall from 36 per cent in 1999-00 to 34 per cent for 2000-01 and then to 30 per cent from 2001-02.

6.5 GTE performance reports

Newcastle Port Corporation (NSW)
Port Kembla Port Corporation (NSW)
Sydney Ports Corporation (NSW)
Melbourne Port Corporation (Vic)
Victorian Channels Authority (Vic)
Gladstone Port Authority (QLD)
Port of Brisbane Corporation (QLD)
South Australian Ports Corporation (SA)
Fremantle Port Authority (WA)
Bunbury Port Authority (WA)
Burnie Port Corporation (Tas)
Hobart Ports Corporation (Tas)
Port of Devonport Corporation (Tas)
Port of Launceston Pty Ltd (Tas)
Darwin Port Corporation (NT)

NEWCASTLE PORT CORPORATION — New South Wales

The Newcastle Port Corporation (NPC) was created as a separate corporatised entity on 30 June 1995 with the passing of the *Ports Corporatisation and Waterways Management Act 1995*. The NPC is Australia's second largest port measured by mass tonnes with a total throughput of 72.7 million tonnes in 1999-00.

Total throughput fell by 5.3 million tonnes in 1999-00 as a result of a downturn in the coal industry and the closure of BHP's Newcastle steel making operations. Consequently, revenues generated by port management, wharfage, site occupation, navigation and pilotage decreased.[1]

Annual profits have in most years been around $12 to $13 million, but in 1997-98 and 1999-00 they were inflated by abnormal revenue. These revenues relate to superannuation interest earnings and a reduction in the member liability base. The increase in the cost recovery ratio during 1999-00 was caused by a fall in operating expenses, the most notable being a drop in 'repairs and services' expense of $1.8 million.

The value of equity significantly increased in 1996-97 and 1998-99 owing to:

- a reduction in borrowings from NSW Treasury Corporation and the transfer of two properties to the NPC in 1996-97;[2] and
- the 17 per cent upward revaluation of property, plant and equipment on 30 June 1999.

The 40 per cent fall in the NPC's borrowings combined with an increase in total assets led to a large drop in each of the debt to equity, debt to total asset, total liabilities to equity and leverage ratios during 1996-97.

The upward revaluation of the NPC's assets caused a sharp fall in the return on asset and return on equity ratios in 1998-99. However, the increase in total assets improves the NPC's debt to equity and debt to total asset ratios without any real change in debt levels or liabilities.

The NPC is required to make both tax-equivalent and dividend payments.

---

1 Port management income decreased by 5.8 per cent, wharfage income decreased by 11.4 per cent, income resulting from site occupation decreased by 13.7 per cent, navigational income dropped 6.4 per cent and pilotage income fell 4.5 per cent.

2 The NPC's borrowings fell from $50 million in 1995-96 to $30 million in 1996-97. Borrowings consist of NSW Treasury Corporation loans, secured by government guarantee and based upon instalment payments of interest only and repayment or rollover of principal at maturity. The two properties included the Australian Defence Industries and the Forgacs sites.

NEWCASTLE PORT CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	129	116	115	132	144
Total revenue	$M	34	38	47	40	38
Profitability						
Operating profit before tax (includes abnormals)	$'000	12 819	12 087	18 088	12 881	16 774
Operating sales margin	%	38.8	36.9	42.8	36.8	49.4
Cost recovery	%	163.5	150.3	157.3	158.2	177.4
Return on assets	%	11.3	12.2	17.9	12.3	14.0
Return on equity	%	13.4	12.1	17.3	10.8	14.1
Financial management						
Debt to equity	%	83.0	45.9	45.4	36.3	35.6
Debt to total assets	%	38.9	24.5	26.3	24.6	22.3
Total liabilities to equity	%	113.3	77.9	71.3	58.0	67.2
Interest cover	times	8.3	5.3	8.1	6.8	7.7
Current ratio	%	91.8	80.2	70.8	72.9	82.2
Leverage ratio	%	213.3	177.9	171.3	158.0	167.2
Payments to and from government						
Dividends	$'000	5 441	8 962	10 000	9 000	9 000
Dividend to equity ratio	%	9.0	14.3	15.1	12.0	10.6
Dividend payout ratio	%	67.3	118.1	87.5	111.3	75.3
Income tax expense	$'000	4 736	4 497	6 658	4 796	4 827
CSO funding	$'000	0	0	0	0	0

a The Newcastle Port Corporation (NPC) was incorporated on 1 July 1995. **b** The NPC's borrowings fell from $50 million in 1995-96 to $30 million in 1996-97. The decline in total assets in the 1996-97 financial year was due to a fall in current investments (current investments tend to be highly volatile and as such have been calculated by the NPC at a given point in time). **c** Total revenue and operating profit were inflated by abnormal revenue resulting from interest earned ($4.7 million) from superannuation reserves not previously accounted for. **d** A revaluation of property, plant and equipment was brought to account as at 30 June 1999. This resulted in an increase in the value of total assets and a consequent fall in the return on asset and return on equity ratios. **e** Includes abnormal revenue of $4.1 million relating to superannuation interest earnings and a reduction in member liability due to a review of actuarial assumptions.

PORT KEMBLA PORT CORPORATION — New South Wales

The Port Kembla Port Corporation (PKPC) was formed on 1 July 1995 as part of the corporatisation of NSW ports. The PKPC operates under the *Ports Corporatisation and Waterways Management Act 1995*.

The PKPC's total trade tonnage fell 12.6 per cent over the three year period to 1998-99. Reduced coal throughput accounted for 95 per cent of this fall. Trade further declined in 1999-00 as a result of a continuing reduction in coal related trade and income.

PKPC's total revenue has fallen 27 per cent between 1995-96 and 1999-00. The fall in total revenue was largely the result of a decline in port related rental associated with reduced coal throughput and the restructure of the PKPC's rental agreement with Port Kembla Coal Terminal on 1 July 1996.[1] To assist the local coal export industry the NSW State Government directed PKPC to reduce its tonnage fee at the coal terminal from $2.00 to $1.30, resulting in an $11.2 million fall in port management revenue during 1998-99.[2]

PKPC undertook a Recoverable Amounts Test (RAT) on 30 June 1999 to ensure that the carrying value of non-current assets did not exceed their recoverable amounts. The RAT revealed that property, plant and equipment were 36 per cent overvalued. As a result, assets were revalued downwards by $42.1 million and operating profit decreased in 1998-99 with the inclusion of the revaluation as an abnormal expense.

PKPC is required to make both income tax-equivalent and dividend payments. Income tax expense is reported as a negative amount in 1999-00 largely due to a benefit arising from deferred income tax provision.

In 1999-00 the PKPC received $4.5 million in community service obligation funding (CSO). The CSO addresses the difference between the actual amount of income received by the corporation under the NSW Government Rental Relief Scheme for the Port Kembla Coal Terminal and what would have been payable under the original lease scheme.

1 The 5 per cent reduction in scheduled charges to port users in 1996-97 may also have contributed to the fall in total revenue.

2 The Independent Pricing and Regulatory Tribunal recommended that $1.48 per tonne was a suitable rate to recover the value of the lease to the PKPC.

PORT KEMBLA PORT CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*	*1998-99*[c]	*1999-00*
Size						
Total assets	$M	196	186[c]	182	134	135
Total revenue	$M	44	38	39	28	32
Profitability						
Operating profit before tax (includes abnormals)	$'000	20 087	19 535	20 908	-34 633	8 302
Operating sales margin	%	67.7	63.6	64.5	-115.7	40.6
Cost recovery	%	309.5	275.0	285.0	172.5	201.4
Return on assets	%	15.3	12.9	13.9	-18.9	9.8
Return on equity	%	13.3	12.6	13.3	-49.1	23.7
Financial management						
Debt to equity	%	78.6	60.7	59.4	110.1	100.2
Debt to total assets	%	38.5	31.8	32.1	37.4	44.1
Total liabilities to equity	%	104.0	86.4	82.8	149.2	127.8
Interest cover	times	3.0	4.8	5.5	-6.4	2.7
Current ratio	%	63.0	68.3	97.9	51.4	91.9
Leverage ratio	%	204.0	186.4	182.8	249.2	227.8
Payments to and from government						
Dividends	$'000	7 982	8227	13 599	9 482	7 988
Dividend to equity ratio	%	8.3	8.4	13.6	12.4	14.2
Dividend payout ratio	%	62.5	66.8	102.4	-25.2	59.7
Income tax expense	$'000	7 321	7 214	7 622	2 995	-5 077[d]
CSO funding	$'000	0	0	0	0	4 490

a The Port Kembla Port Corporation (PKPC) commenced operations on 1 July 1995. **b** The fall in total assets resulted from the sale of short-term deposits ($4.5 million) and accumulated depreciation on the Port Kembla Coal Terminal ($4.6 million). The PKPC retired $15 million in borrowings partly through the sale of short-term deposits. **c** In June 1999, PKPC undertook a Recoverable Amounts Test that resulted in a $42.1 million downward asset revaluation. **d** Income tax expense decreased due to a reduction in the company tax rate from 36 per cent to 34 per cent in respect of 2000-01 and then to 30 per cent from 2001-02. Consequently, deferred tax balances have been remeasured using the appropriate new rates.

SYDNEY PORTS CORPORATION — New South Wales

The corporatisation of the ports of Sydney under the *Ports Corporatisation and Waterways Management Act 1995*, resulted in the establishment of Sydney Ports Corporation (SPC) on 1 July 1995. The SPC manages the commercial ports of Sydney Harbour and Botany Bay.

Increases in total revenue over the reporting period are largely due to growth in total container throughput.

The SPC delivered a 10 per cent reduction in total port charges over the two years following corporatisation. Furthermore, the SPC announced the abolition of the $10 wharfage charge on empty containers from 1 January 1999.[1] This represented $2 million of lost revenue to SPC in 1999-00.

SPC's rate of return on assets declined between 1995-96 and 1999-00, largely due to an increase in the value of total assets. The substantial rise in the value of assets reflects the revaluation of property, plant and equipment on 30 June 1998.[2] In addition to the asset revaluation, the SPC acquired land at Glebe Island and White Bay, purchased additional lots at Port Botany and incurred expenditure on road works. The asset revaluation resulted in a significant increase in equity that improved the SPC's debt to equity and total liabilities to equity ratios without any real change in debt levels or liabilities.

Total assets in 1999-00 include prepayments of superannuation ($20 million), a $10.5 million increase in prepayments due to an option to purchase land at Enfield and the capitalisation of a $10 million prepayment from the prior year for land at Botany Bay.

The SPC is required to make both tax-equivalent and dividend payments to the NSW Government. Dividend payments are determined in consultation with the Treasury. The SPC is not subject to any community service obligations.

1 The abolition of the container charge in 1999 follows a reduction from $25 to $10 in 1997. Furthermore, Sydney's pilotage charges were reduced 2.5 per cent in May 1999 as part of a three year contract between the SPC and Sydney Sea Pilots Pty Ltd. A further price reduction of 2.5 per cent took affect from 1 July 2000.

2 The SPC carried out a revaluation of 95 per cent of total assets using the deprival method. Assets not revalued were recorded at their historical cost.

SYDNEY PORTS CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*
Size						
Total assets	$M	334	337	524	544	581
Total revenue	$M	84	88	100	109	108
Profitability						
Operating profit before tax (includes abnormals)	$'000	42 901	38 370	40 858	49 469	45 059
Operating sales margin	%	57.9	57.6	52.8	55.2	52.2
Cost recovery	%	237.3	235.6	211.8	208.4	222.6
Return on assets	%	15.8	15.5	12.5	11.5	10.2
Return on equity	%	19.5	16.7	10.5	9.3	7.1
Financial management						
Debt to equity	%	109.3	102.9	44.4	42.1	40.9
Debt to total assets	%	47.7	44.9	35.0	28.2	27.0
Total liabilities to equity	%	143.3	130.1	54.5	52.0	56.6
Interest cover	%	7.2	3.8	4.2	5.2	4.6
Current ratio	%	26.2	101.5	185.9	99.5	124.7
Leverage ratio	%	243.3	230.1	154.5	152.0	156.6
Payments to and from government						
Dividends	$'000	15 142	14 558	12 749	13 639	13 030
Dividend to equity ratio	%	11.0	10.3	5.2	3.9	3.6
Dividend payout ratio	%	56.5	61.3	50.0	42.2	50.0
Income tax expense	$'000	16 080	14 619	15 359	17 177	19 001
CSO funding	$'000	0	0	0	0	0

a The fall in interest cover (and increase in the current ratio) resulted from a 96 per cent increase in gross interest expense. The SPC redirected short-term loans valued at $129 million (86 per cent of total borrowings in 1996-97) in favour of medium-term and long-term loan options. **b** The increase in total assets resulted largely from a revaluation of property, plant and equipment on 30 June 1998. Furthermore, the SPC purchased land at White Bay from the State Rail Authority and purchased lots 11, 12 and 13 at Port Botany from the Marine Ministerial Holding Corporation. **c** In 1998-99, the SPC purchased ten hectares of land at Port Botany. The SPC received a $7.1 million capital grant from the NSW Government for the construction of a new passenger terminal at Darling Harbour.

MELBOURNE PORT CORPORATION — Victoria

The Melbourne Port Corporation (MPC) commenced operations on 1 March 1996 under the *Ports Services Act 1995* (PSA). The MPC is responsible for managing port land, coordinating future developments and ensuring the availability of adequate land and infrastructure to port service providers.

The MPC is subject to an average revenue cap administered by the Office of the Regulator-General (ORG) in accordance with s. 50 of the PSA.[1] In meeting the revenue cap, the MPC was required to reduce wharfage charges by 20 per cent on 1 July 1996. In addition, MPC had to provide an average annual reduction in charges on prescribed services of 10 per cent (less CPI) over the period 1997-98 to 1999-00.[2] MPC estimated that this reduction has resulted in forgone revenue of approximately $26.7 million.

During 1999-00, the ORG extended the regulation of prescribed services for an additional five years. Commencing July 2000, MPC will be required to provide an annual 5.2 per cent average real reduction in charges for these services.

Operating profit before tax (including abnormals) under the revenue cap increased in each of the financial years to 1998-99.[3] This increase was achieved through a 32 per cent reduction in total expenses. However, a drop in wharfage charges of 18.2 per cent on average, coupled with an abnormal expense of $2.3 million, decreased profitability by 35 per cent in 1999-00 compared to the previous year.

The MPC's assets have been revalued twice over the reporting period. Revaluations in 1997-98 resulted in an increment of $50.7 million and a $69.7 million increment in 1999-00.

The MPC is required to make both tax-equivalent and dividend payments to the Victorian Government.[4]

---

1 The MPC was required to provide a 30 per cent real reduction in it's average revenue from prescribed services for the three year period prior to June 2000.

2 The MPC reduced charges on prescribed services by 8.5 per cent in 1997-98 and a further 6.2 per cent in 1998-99, MPC reduced its prescribed charges by 17 per cent in 1999-00. Prescribed services include the provision of berths, short-term storage and cargo marshalling services.

3 The financial statistics for 1995-96 only relate to the period 1 March 1996 to 30 June 1996.

4 The dividend is set at 33.3 per cent of operating profit after income tax.

MELBOURNE PORT CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	452	482	533	513	568
Total revenue	$M	30	81	81	83	75
Profitability						
Operating profit before tax (includes abnormals)	$'000	14 996	28 045	37 272	46 496	30 002
Operating sales margin	%	63.2	45.8	59.8	65.8	49.2
Cost recovery	%	275.8	212.5	248.5	291.8	209.9
Return on assets	%	4.2	8.1	9.6	10.5	6.9
Return on equity	%	3.1	4.7	6.6	8.2	4.1
Financial management						
Debt to equity	%	43.0	33.6	25.7	26.1	17.7
Debt to total assets	%	28.5	24.5	20.2	19.1	15.0
Total liabilities to equity	%	50.5	41.8	33.1	33.7	24.7
Interest cover	times	4.7	3.9	4.2	6.4	5.1
Current ratio	%	45.1	90.4	153.7	85.2[e]	40.8
Leverage ratio	%	150.5	141.8	133.1	133.7	124.7
Payments to and from government						
Dividends	$'000	3 185	4 227	7 987	34 074	8 644
Dividend to equity ratio	%	1.1	1.3	2.2	8.7	2.1
Dividend payout ratio	%	34.7	27.8	32.9	105.6	50.0
Income tax expense	$'000	5 822	12 842	13 012	14 224	12 713
CSO funding	$'000	0	0	0	0	0

a The Melbourne Port Corporation (MPC) commenced operations on 1 March 1996. Financial statistics for 1995-96 cover the period 1 March 1996 to 30 June 1996. **b** The increase in total assets largely resulted from an upward revaluation of the Corporation's land holdings ($50.7 million) and the retention of operating profits ($12.8 million). **c** Total assets fell as a result of a $26 million dividend payout from cash reserves, the depreciation of assets and the transfer of Station Pier to the Department of Infrastructure. **d** An abnormal expense of $2.3 million was incurred, resulting from the write-off of assets. **e** The large fall in the current ratio reflects the payment of a $26 million special dividend to the State Government coupled with an increase in current borrowings.

VICTORIAN CHANNELS AUTHORITY — Victoria

The Victorian Channels Authority (VCA) is a statutory authority established under the *Port Services Act 1995* (PSA). The VCA commenced operations on 1 March 1996 and is responsible for safe navigation of shipping in Port Phillip Melbourne and Geelong. The VCA is responsible for the provision and maintenance of navigational aids and commercial navigation channels. It is also required to coordinate pollution control and emergency response.

The VCA is subject to price regulation in the form of an average revenue cap on the provision of channel services. The VCA has discretion in determining its tariff structure. However, the Office of the Regulator-General (ORG) has the ability to reject prices if they do not comply with the average revenue cap. A pricing order placed on the VCA by the ORG in October 1996 required the VCA to reduce the standard channel fee charged to shipping by 12 per cent annually in real terms.[1] Consequently the standard channel rate has declined from 40 cents per gross ton in March 1996 to 26.1 cents in June 2000.

The presence of a revenue cap requires the VCA to reduce expenses if it is to maintain and increase profitability. The gradual decline in the cost recovery ratio reflects the VCA's inability to reduce expenses to compensate for the revenue cap.

The high return on asset and return on equity ratios achieved in 1996-97 arose because the value placed on channels was zero in the financial statements prior to 1997-98.[2] The rise in total assets during 1999-00 is the result of the inclusion in financial reporting of the value of channels transferred to the VCA from predecessor bodies ($78.1 million).[3] The inclusion of these assets has resulted in a $2 million increase in depreciation expense and a subsequent reduction in operating profit.

The VCA is subject to tax-equivalent payments under the *State Owned Enterprises Act 1992*. In addition, the VCA is required to pay dividends to the Victorian Government, as determined by the Treasurer.

1 A three year period commencing 1 July 1997 and ending 30 June 2000.

2 The determination of asset values for channels was resolved through the conversion of the total costs to capital associated with the Geelong channel improvement program in 1997-98, pursuant to s. 40(d) of the PSA.

3 Channels transferred from the former Port of Melbourne Authority (PMA) and the Port of Geelong Authority (PGA) have been recorded for the first time, effective 1 July 1999. The values are based on those previously held in the accounts of these authorities.

VICTORIAN CHANNELS AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	14	14	51	61	138
Total revenue	$M	7	22	21	25	19
Profitability						
Operating profit before tax (includes abnormals)	$'000	2 965	8 305	8 514	10 542	3 466
Operating sales margin	%	42.5	38.3	40.1	41.8	15.9
Cost recovery	%	174.0	177.3	166.8	148.0	118.9
Return on assets	%	22.5	61.0	26.1	18.7	3.5
Return on equity	%	34.9	77.9	4.1	8.2	1.0
Financial management						
Debt to equity	%	100.4	0	0	0	0
Debt to total assets	%	36.3	0	0	0	0
Total liabilities to equity	%	176.3	45.4	21.6	57.2	11.0
Interest cover	times	23.8	53.2	0	0	0
Current ratio	%	144.3	162.7	219.8	174.6	244.9
Leverage ratio	%	276.3	145.4	121.6	157.2	111.0
Payments to and from government						
Dividends	$'000	0[f]	1 035	3 130	3 271	1 000
Dividend to equity ratio	%	0	14.2	12.1	8.1	1.2
Dividend payout ratio	%	0	18.2	291.7	98.6	122.5
Income tax expense	$'000	1 228	2617	7 441	7 225	2 650
CSO funding	$'000	0	0	0	0	0

a The financial statistics for 1995-96 cover the period 1 January 1996 to 30 June 1996. **b** The Victorian Channels Authority (VCA) repaid total start-up debt ($5 million). **c** Assets rose largely as a result of the conversion of the total costs to capital associated with the Geelong channel improvement program. **d** Non-current assets increased resulting from additional costs associated with the dredging of the Port of Geelong ($4.3 million) and work in progress ($5.4 million). Operating profit was overstated due to a $3.4 million write-back in provisions for channel dredging. **e** The figures reported in 1999-00 are affected by the inclusion of the value of channels transferred to the VCA from predecessor bodies ($78.1 million). **f** The VCA was not required to make a dividend payment in 1995-96.

GLADSTONE PORT AUTHORITY — Queensland

The Gladstone Port Authority (GPA) was corporatised on 1 July 1994 under the *Government Owned Corporations Act 1993*. The GPA undertakes stevedoring activities, pilotage and the provision of infrastructure for bulk coal operations.

The GPA's total revenue increased steadily over the reporting period as a result of growth in total trade throughput. The slight decline in total revenue in 1997-98 reflects the cessation of the 'improved harbour charge' at the end of 1997.[1]

The GPA undertook a Recoverable Amounts Test on 30 June 1999 to ensure that the carrying value of non-current assets did not exceed their recoverable amounts. This resulted in a $139.2 million write-down of non-current assets. This write-down was recorded as an abnormal item resulting in a large operating loss before tax (including abnormals) in 1998-99. The impact of the loss is reflected in the negative return on asset, return on equity and interest cover ratios for 1998-99. The write-down largely related to user-funded assets, where port users provided the capital funding to construct the assets concerned.[2]

Increased operating profit in 1999-00 is in part due to a reduction in depreciation expense resulting from the abnormal write down of asset values in the previous year. Depreciation expense fell from $22.1 million in 1998-99 to $9.3 million in 1999-00.

The GPA has been committed to debt reduction, achieving a 77 per cent fall over the reporting period. As a consequence, the debt to equity, debt to total asset and total liabilities to equity ratios declined. In 1999-00, borrowings were further reduced by $6.3 million.

The GPA is required to make both tax-equivalent and dividend payments to the Queensland Government.

1 The improved harbour charge is an amount collected annually from coal shippers to cover interest and redemption of funds borrowed for Gladstone Harbour dredging in 1981.

2 User-funded assets did not generate sufficient cash flows to support their carrying values determined under the deprival value methodology and were consequently written-down.

GLADSTONE PORT AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*[a]	*1999-00*
Size						
Total assets	$M	438	452	464	358	369
Total revenue[b]	$M	77	83	81	82	86
Profitability						
Operating profit before tax (includes abnormals)	$'000	14 935	17 174	13 259	-127 700	21 548
Operating sales margin	%	24.3	25.2	18.4	-156.9	25.0
Cost recovery	%	132.2	133.6	122.5	117.4	133.2
Return on assets	%	4.4	4.8	3.4	-30.8	6.1
Return on equity	%	2.4	2.7	1.9	-21.8	2.6
Financial management						
Debt to equity	%	12.9	8.9	5.4	5.2	3.5
Debt to total assets	%	11.1	7.8	4.7	4.0	3.1
Total liabilities to equity	%	16.9	15.8	15.2	14.9	15.5
Interest cover	times	4.6	5.0	6.8	-108.8	37.0
Current ratio	%	69.2	109.2	110.9	118.2	141.5
Leverage ratio	%	116.9	115.8	115.2	114.9	115.5
Payments to and from government						
Dividends	$'000	2 602	2 571	3 087	0	3 938
Dividend to equity ratio	%	0.7	0.7	0.8	0	1.2
Dividend payout ratio	%	29.4	24.9	41.3	0	48.1
Income tax expense	$'000	6 076	6 856	5 787	-49 901	13 354
CSO funding	$'000	0	0	0	0	0

a The Gladstone Port Authority (GPA) undertook a Recoverable Amounts Test on 30 June 1999. This resulted in a $139.2 million write-down of non-current assets, and a commensurate fall in operating profit before tax (including abnormals), due to the increase in abnormal expenses. **b** The GPA's right to collect improved harbour charges under agreement with coal shippers ceased at the end of 1997. This placed significant constraints on the ability of the GPA to increase total revenue. Revenue from the improved harbour charge totalled $13.3 million in 1995-96, $14.6 million in 1996-97 and $5.8 million in 1997-98.

PORT OF BRISBANE CORPORATION — Queensland

The Port of Brisbane Corporation (PBC) was corporatised on 1 July 1994 under the provisions of the *Government Owned Corporations Act 1993*. The PBC manages the Port of Brisbane, Brisbane Multimodal Terminal, the boat harbours of Manly, Scarborough, Cabbage Tree Creek, Gardens Point and is a major shareholder in Brisbane Airport Corporation Limited (BACL).

The PBC's total revenue increased by 40 per cent (including abnormals) over the reporting period.[1] This growth was due to increased trade volumes. Total throughput in 1995-96 was 9 million tonnes compared to 23 million tonnes in 1999-00.

The PBC's total assets have increased over the reporting period by over 80 per cent. The major contributors to this growth are investment in the BACL and a number of upwards revaluations. Total asset growth due to revaluation increments over the reporting period is $62.9 million.[2]

The PBC invested in the BACL in 1996-97. The initial investment was entirely funded through borrowings from the Queensland Treasury Corporation. In 1999-00, the PBC increased its shareholding in the BACL to 37.6 per cent.[3] The debt incurred through investment in BACL has resulted in a sharp increase in the debt to equity, debt to total asset and total liabilities to equity ratios.

The PBC is required to make both tax-equivalent and dividend payments. The PBC was also subject to land tax and sales tax-equivalent payments from 1995-96.

1 Total revenue was inflated in 1997-98 as a result of a $4.8 million write-back of provisions for future repairs to various wharves and terminal pavings.

2 Over the reporting period, increases in the value of assets attributable to revaluations include $8.4 million in 1995-96, $13.3 million in 1996-97, $5.2 million in 1997-98, $5.3 million in 1998-99 and $35.9 million in 1999-00.

3 An additional investment of $20 million in BACL was made in 1999-00 as part of a rights issue by BACL. The investment was funded through increased debt.

PORT OF BRISBANE CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*
Size						
Total assets	$M	404	621	625	658	737
Total revenue	$M	60	68	82	78	84
Profitability						
Operating profit before tax (includes abnormals)[d]	$'000	22 593	27 470	16 568	26 341	26 205
Operating sales margin	%	35.8	39.7	32.5	52.2	51.6
Cost recovery	%	183.8	186.2	189.0	200.8	206.6
Return on assets	%	5.8	5.5	4.4	6.4	6.3
Return on equity	%	4.1	4.9	3.0	4.2	4.2
Financial management						
Debt to equity	%	0.1	48.4	46.5	48.9	52.2
Debt to total assets	%	0.1	37.7	30.7	31.8	34.2
Total liabilities to equity	%	7.6	55.5	51.9	57.8	61.0
Interest cover	times	1 130.7	32.9	2.6	2.8	2.3
Current ratio	%	126.6	101.6	81.3	81.0	94.0
Leverage ratio	%	107.6	155.5	151.9	157.8	161.0
Payments to and from government						
Dividends	$'000	5 831	7 126	4 780	15 805	17 580
Dividend to equity ratio	%	1.6	1.8	1.2	3.8	4.0
Dividend payout ratio	%	38.8	37.5	39.7	90.5	94.8
Income tax expense	$'000	7 563	8 454	4 514	8 884	7 667
CSO funding	$'000	0	0	0	0	0

a Increase in assets attributable to revaluations $8.4 million. Abnormal expenses deflated operating profit before tax (including abnormals) by $4.3 million. **b** Total assets increased due to a $193 million investment in the Brisbane Airport Corporation Ltd and a revaluation increment of $13.3 million. The investment was entirely funded through borrowings from the Queensland Treasury Corporation. Abnormal expenses deflated operating profit before tax (including abnormals) by $3.6 million. **c** Total revenue increased from a $4.9 million write-back of provisions for future repairs to various wharves and terminal pavings. Increase in assets attributable to revaluations by $5.2 million. Abnormal expenses deflated operating profit before tax (including abnormals) by $10.4 million. **d** Increase in assets attributable to revaluations by $5.3 million. Total revenue increased from a $3 million write-back of provisions for future repairs to various wharves and terminal pavings. Abnormal expenses deflated operating profit before tax (including abnormals) by $3 million.

SOUTH AUSTRALIAN PORTS CORPORATION South Australia

The South Australian Ports Corporation (SAPC) was established on 1 November 1995 under the provisions of the *Public Corporations Act 1993* and the *South Australian Ports Corporation Act 1994*. The SAPC is responsible for managing ten South Australian ports.[1]

As part of the corporatisation process, the SAPC revalued its non-current assets on 1 July 1995. Assets that had previously been valued at historic cost were revalued using the deprival method. The large downward revaluation of assets was recorded as an abnormal expense resulting in the SAPC incurring a large operating loss before tax (including abnormals) in 1995-96.

Total assets decreased in 1999-00 due principally to a reduction in cash holdings ($9.9 million). Cash reserves were utilised to retire debt, which subsequently fell by $12.1 million. These changes in assets and borrowings have improved the debt to equity, and total liabilities to equity ratios in 1999-00. Operating profit before tax (including abnormals) in 1999-00 fell largely as a result of a drop in revenue from port operations and services, in particular a reduction in grain exports and associated trade.

In 1996-97, the SAPC refinanced its debt with the South Australian Financing Authority, which separated the SAPC's debt from the Common Public Sector Interest Rate debt arrangement. The SAPC's debt to equity, debt to total asset, total liabilities to equity and leverage ratios have declined since 1995-96, which can in part be attributed to debt refinancing.

The SAPC is required to make tax-equivalent payments and dividend payments. In addition, SAPC is required to pay debt guarantee fees and land tax to the South Australian Government.[2] The SAPC also became liable for local council rates equivalent payments on 1 July 1998. On 7 April 1999, the South Australian Government announced an in principle decision to sell the SAPC.[3] The Department of Administrative and Information Services is the agency responsible for progressing the sale of the SAPC.

---

1 SAPC owns and manages the ports of Port Adelaide, Port Giles, Port Pirie, Port Lincoln, Klein Point, Wallaroo, Thevenard, Kingscote, Cape Jervis and Penneshaw.

2 There is a 0.75 per cent charge levied on all outstanding borrowings, in order to reflect the guarantee provided by the Government on these borrowings.

3 In May 2000 three Bills were introduced into the South Australian Parliament to facilitate the sale. The bills provide for the long-term lease of SAPC land and for the disposal of port infrastructure.

SOUTH AUSTRALIAN PORTS CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*	*1999-00*
Size						
Total assets	$M	126	109	102	103	94
Total revenue	$M	45	49	51	42	38
Profitability						
Operating profit before tax (includes abnormals)	$'000	-39 720	9 897	23 162	15 317	12 766
Operating sales margin	%	-77.9	31.4	49.9	40.9	36.1
Cost recovery	%	155.2	177.2	154.3	166.8	160.3
Return on assets	%	-20.1	14.8	24.5	17.0	14.3
Return on equity	%	-55.7	12.2	36.9	17.5	14.0
Financial management						
Debt to equity	%	133.0	87.6	63.7	48.6	26.8
Debt to total assets	%	41.2	38.3	33.2	28.2	17.2
Total liabilities to equity	%	156.9	111.5	85.7	72.7	49.0
Interest cover	times	-4.1	2.3	5.1	8.5	11.1
Current ratio	%	314.1	112.8	105.5	84.3	54.9
Leverage ratio	%	256.9	211.5	185.7	172.7	149.0
Payments to and from government						
Dividends	$'000	3 369	3 972	16 254[d]	5 506	4 971
Dividend to equity ratio	%	4.3	7.9	30.6	9.6	8.1
Dividend payout ratio	%	-7.8	64.6	82.8	54.9	58.1
Income tax expense	$'000	3 570	3 752	3 523	5 279	4 216
CSO funding	$'000	0	0	0	0	0

a The substantial fall in operating profit resulted from the write-down in the value of non-current assets at 1 July 1995 due to the adoption of the deprival method of asset valuation. **b** An abnormal expense of $5.7 million associated with debt refinancing arrangements with the South Australian Financing Authority reduced operating profit. The large decline in total assets resulted from a $15 million fall in current assets in the form of cash and receivables. **c** The higher level of revenue (and operating profit) is attributed to the sale of the Port's bulk loading plants. Property, plant and equipment fell 11 per cent during 1997-98 resulting from a downward valuation of land assets as at 30 June 1998 coupled with accumulated depreciation for the year. **d** The SAPC paid a final dividend to the South Australian Government on 30 June 1998. In addition, the Corporation paid a special capital dividend of $11.6 million.

FREMANTLE PORT AUTHORITY — Western Australia

The Fremantle Port Authority (FPA) was commercialised on 1 July 1996. The role of the port, as agreed by the Western Australian Government in November 1995, is 'to facilitate trade in an efficient and commercial manner'. The FPA provides and maintains port infrastructure and port services including ship scheduling, port communications and mooring. The FPA contracts out pilotage, stevedoring, towage, maintenance and fork lift training to the private sector.

Total port revenue increased over the reporting period as reductions in port charges were offset by increases in total throughput.[1] Weighted average prices have declined over the reporting period by 8.6 per cent. The improvement in the cost recovery ratio between 1995-96 and 1999-00, in the presence of falling prices, reflects a reduction in the unit cost of throughput.[2]

Between 1995-96 and 1999-00, the FPA achieved a high return on assets. Operating profit was used to retire debt and this is reflected in the improved debt to total assets ratio over the reporting period.[3] The FPA's return on equity, debt to equity and total liabilities to equity in 1996-97 improved with the transfer of employee entitlements (superannuation pension liabilities) to the Western Australia Government on 30 June 1997. During 1999-00, $7.5 million in debt was retired and $5.5 million of debt was restructured in order to reduce interest rate expense. Total assets increased in 1999-00 due mainly to a $4.9 million increase in bank bills and a $11.5 million increase in land assets.

The FPA is required to make both tax-equivalent and dividend payments to the Western Australian Government.

1 Total revenue was inflated in 1997-98 due to abnormal revenue resulting from a compensation receipt for costs incurred in regard to reclamation of Port Beach land and the lease surrender on 'A' Shed at Victoria Quay. Total trade in 1995-96 was 20.1 million tonnes while total trade in 1999-00 was 23.4 million tonnes.

2 For example cargo processed berth time has increased from 581 tonnes per hour in 1996-97 to 701 tonnes per hour during 1999-00.

3 The FPA's debt fell from $54.5 million in 1995-96 to $17.7 million in 1999-00.

FREMANTLE PORT AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*
Size						
Total assets	$M	104	108	112	114	120
Total revenue	$M	51	53	62	55	60
Profitability						
Operating profit before tax (includes abnormals)	$'000	8 340	10 620	17 894	13 824	14 768
Operating sales margin	%	27.1	29.0	34.6	34.3	29.2
Cost recovery	%	141.0	140.9	144.0	152.3	149.9
Return on assets	%	14.6	14.9	20.0	17.1	15.6
Return on equity	%	-102.6	22.7	27.4	14.5	12.4
Financial management						
Debt to equity	%	1 490.2	109.2	64.8	38.8	22.9
Debt to total assets	%	55.0	41.7	30.4	22.3	15.1
Total liabilities to equity	%	2 751.2	166.7	116.8	75.5	55.8
Interest cover	times	2.4	3.1	5.3	3.5	5.2
Current ratio	%	99.6	112.4	121.3	119.6	105.5
Leverage ratio	%	2 851.2	266.7	216.8	175.5	155.8
Payments to and from government						
Dividends	$'000	0	0	1262	845	1 750
Dividend to equity ratio	%	0	0	2.7	1.5	2.5
Dividend payout ratio	%	0	0	10.0	10.0	19.9
Income tax expense	$'000	0	5 616[d]	5 270	5 377	5 989
CSO funding	$'000	0	0	0	0	0

a A number of performance indicators improved in 1996-97 as a result of the transfer of the Fremantle Port Authority's (FPA's) $25.9 million superannuation pension liability to the Western Australian Government. **b** The FPA received $8.8 million from the Western Australian Government for costs incurred in regard to reclamation of Port Beach land and the lease surrender on 'A' Shed at Victoria Quay. **c** FPA was made subject to the *Port Authorities Act 1999*. **d** From 1 July 1996, the FPA was required to make tax-equivalent payments.

BUNBURY PORT AUTHORITY — Western Australia

The Bunbury Port Authority (BPA) was corporatised in August 1999 under the *Port Authorities Act 1999*. Bunbury is a bulk cargo handling port with alumina accounting for over 67 per cent of total throughput.[1]

In 1999, the authority undertook a restructuring program of port operations which resulted in the BPA exiting the direct provision of a range of port services. P&O Ports began exclusive provision of stevedoring, mooring, maintenance and other services in the port on 1 July 1999.

The fall in operating profit before tax (including abnormals) in 1998-99, was largely due to $1.4 million in redundancy payments. The payments resulted from the restructuring of the workforce to facilitate the outsourcing of services. The accompanying increase in the cost recovery ratio indicates that the BPA's underlying financial performance did not deteriorate following the outsourcing of services.

The increase in profitability during 1999-00 is attributable to a $2.5 million fall in total expenses. The decreased expenditure was the result of both workforce reduction and lower borrowing costs due to debt restructuring.[2]

The Authority is required to make dividend payments to the Western Australian Government. In addition, the BPA is required to pay income tax and sales tax-equivalents from 1 July 1999.[3]

1 Alumina trade through the port during 1999-00 was 6.8 million tonnes.

2 In July 1999, the BPA refinanced it's outstanding capital works debt facility. It transferred $13.6 million from Treasury to the WA Treasury Corporation in order to receive benefits from more competitive interest rates and principal repayment arrangements.

3 In January 1999 it was discovered that the BPA had been excluded from the Western Australian's Tax Equivalence Regime. Consequently Treasury advised the Authority that it was not liable to make tax-equivalent payments from 1 July 1996 to 30 June 1999.

BUNBURY PORT AUTHORITY (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*	*1997-98*	*1998-99*[a]	*1999-00*
Size						
Total assets	$M	n.r.	n.r.	75	91	94
Total revenue	$M	n.r.	n.r.	14	14	14
Profitability						
Operating profit before tax (includes abnormals)	$'000	n.r.	n.r.	2 890	1 870	4 400
Operating sales margin	%	n.r.	n.r.	31.8	22.8	37.2
Cost recovery	%	n.r.	n.r.	149.5	155.2	166.2
Return on assets	%	n.r.	n.r.	6.1	4.1	5.9
Return on equity	%	n.r.	n.r.	5.4	3.1	3.8
Financial management						
Debt to equity	%	n.r.	n.r.	32.0	24.5	24.1
Debt to total assets	%	n.r.	n.r.	22.9	20.2	19.2
Total liabilities to equity	%	n.r.	n.r.	39.8	33.6	27.1
Interest cover	times	n.r.	n.r.	2.7	2.2	5.3
Current ratio	%	n.r.	n.r.	359.4	239.1	204.1
Leverage ratio	%	n.r.	n.r.	139.8	133.6	127.1
Payments to and from government						
Dividends	$'000	n.r.	n.r.	332.0	190.0	951.0
Dividend to equity ratio	%	n.r.	n.r.	0.6	0.3	1.3
Dividend payout ratio	%	n.r.	n.r.	11.5	10.2	35.5
Income tax expense	$'000	n.r.	n.r.	0	0	1 720
CSO funding	$'000	n.r.	n.r.	0	0	0

a The increase in total assets resulted from the valuation of Crown land controlled by the Bunbury Port Authority that was previously valued at zero in the financial statements. Freehold land in Glen Iris was also revalued by the Valuer-General on the basis of unimproved value. Operating profit before tax (including abnormals) was deflated as a result of $1.4 million redundancy payments to workers as part of the restructuring process associated with outsourcing operations to P&O Ports. **n.r.** Not reported.

BURNIE PORT CORPORATION — Tasmania

The Burnie Port Corporation (BPC) commenced operations on 30 July 1997 pursuant to the *Ports Companies Act 1997*. It also manages the Burnie Airport.

Abnormal items affected the BPC's operating profit before tax (including abnormals) over the reporting period. BPC incurred an operating loss in 1999-00 due largely to a net abnormal expense of $4.7 million.[1] The BPC earned an operating profit before tax (including abnormals) in 1998-99, despite unforseen expenses associated with a violent storm in July 1998 and a $0.6 million increase in depreciation expenses, largely due to an increase in throughput.[2]

The BPC made a $2.5 million upward adjustment of retained profits on 1 July 1998 after the adoption of the principles set out in the Urgent Issues Group Abstract 26 'Accounting for Major Cyclical Maintenance'.[3] The amended accounting treatment resulted in the provision for runway resurfacing and seaport dredging being written-off, a separate asset being recognised for seaport dredging and a review of the useful lives of the respective assets.

In 1997-98, the BPC devalued non-current assets by 14 per cent. Despite this, total assets rose in 1997-98 with the consolidation of assets pertaining to the Burnie Airport in financial statements. In 1999-00, total assets fell as a result of a devaluation of $5.1 million due to the adoption of deprival valuation methodology.[4]

The BPC is required to make both tax-equivalent and dividend payments to the Tasmanian Government. There was no income tax expense or provision for income tax in 1999-00 due to the operating loss after abnormals and the existence of carried forward tax losses. The dividend distribution policy is determined by the directors in accordance with company rules. As a consequence of the 1998-99 and 1999-00 operating results, the Government agreed to waive dividend payments.

---

1 A $5.1 million abnormal expense was reported in 1999-00. The expense resulted from a devaluation and subsequent write-down of non-current assets. The abnormal expense was offset against a $474 720 abnormal revenue relating to a prior period sale and lease-back transaction.

2 The storm caused structural damage to the island and ocean breakwaters and No.5 and No.7 berth areas.

3 The amended accounting treatment requires that provisions for future maintenance must not be recognised as a liability, or as accumulated depreciation, or as a reduction in the carrying value of an asset. As a result, charges to the profit and loss statement for the future removal of accumulated siltation in channels ceased.

4 The devaluation was not made in conformity with a regular policy or revaluation.

BURNIE PORT CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	43	41	44	46	41
Total revenue	$M	12	12	16	13	15
Profitability						
Operating profit before tax (includes abnormals)	$'000	-1 506	-1 523	-5 393	948	-2 584
Operating sales margin	%	2.1	2.0	-23.7	19.7	-10.4
Cost recovery	%	111.0	109.3	127.9	124.3	130.2
Return on assets	%	1.0	1.0	-8.1	6.3	-2.5
Return on equity	%	-7.7	-7.8	-28.9	4.8	-12.8
Financial management						
Debt to equity	%	100.9	101.7	124.4	97.2	99.7
Debt to total assets	%	46.5	47.4	52.6	46.5	43.3
Total liabilities to equity	%	115.0	110.3	144.7	113.3	118.4
Interest cover	times	0.2	0.2	-1.8	1.5	-0.7
Current ratio	%	113.7	175.6	228.8	195.6	101.5
Leverage ratio	%	215.0	210.3	244.7	213.3	218.4
Payments to and from government						
Dividends	$'000	0	0	0	0	0
Dividend to equity ratio	%	0	0	0	0	0
Dividend payout ratio	%	0	0	0	0	0
Income tax expense	$'000	0	0	0	0	0
CSO funding	$'000	0	0	0	0	0

a Operating profit was deflated by a $0.8 million loss on the disposal of a slewing crane. **b** Covers the 11 month period to 30 June 1998. In 1997-98 property, plant and equipment relating to the Burnie Airport was consolidated in Burnie Port Corporation's (BPC's) financial statements. Operating profit was deflated with the adoption of the deprival method for the valuation of non-current assets. The BPC incurred numerous abnormal revenue items in 1997-98, including the amortisation of deferred revenue arising from prior period sale and lease buy back transactions, the write-back of seaport dredging and airport runway provisions, and contributions by external parties to capital improvements. Abnormal expenses included the capitalisation of finance leases, a loss due to obsolescence of the Tide Bridge, devaluation of assets and redundancy payments. **c** Operating profit was deflated, as abnormal revenue relating to the amortisation of deferred revenue arising from prior period sale and lease-buy-back transactions exceeded abnormal expenses resulting from the obsolescence of the Tide Bridge and redundancy payments to former stevedoring employees. **d** Includes abnormal expense of $5.1 million due to asset devaluation.

HOBART PORTS CORPORATION Tasmania

The Hobart Ports Corporation (HPC) was established on 30 July 1997 under the *Ports Companies Act 1997* with a statutory objective of facilitating trade for the benefit of Tasmania. King Island Ports Corporation is a wholly owned subsidiary of the HPC.

During the 1990s, the former Marine Board of Hobart diversified its activities into port-related property. The aim of diversification was to increase the returns on surplus wharves and cargo transit sheds that were being underutilised due to falling port throughput.[1]

Total revenue increased in 1998-99 due to the introduction of the HPC's stevedoring activities. Operating profit before tax (including abnormals) increased in 1999-00 due largely to revenue generated by an increase in stevedoring activities and an accompanying decrease in depreciation expense.[2]

Despite the changing composition of its revenue stream HPC has maintained a cost recovery ratio of over 100. This was achieved despite a loss of throughput and the move into new activities.

The dramatic fall in the current ratio in 1997-98 reflects a shift in the HPC's focus in favour of long-term returns on assets. HPC used cash deposits and an increase in current borrowings to finance the redevelopment of Elizabeth Street Pier into a hotel and convention centre and the purchase of a 49 per cent share in Hobart International Airport Pty Ltd.[3] The increase in the HPC's borrowings is reflected in the rise of the debt to equity, debt to total liabilities and total liabilities to equity ratios.

The HPC is required to make tax-equivalent payments to the Tasmanian Government under Part X(a) of the *Port Companies Act 1997*. Dividend payments were introduced as part of corporatisation in 1997-98. No income tax was payable in 1999-00 due to the existence of carried forward tax losses. Despite this, tax-equivalent expense is recorded as a credit of $37 000 reflecting the restatement of deferred tax balances due to a reduction in the future company tax rate.

1 An example of the development of port-related businesses is the Hobart Fish Handling Centre, which was opened on 1 January 2000. The centre handles all deep sea and market fish landed in Port Hobart and services the southern ocean and local market fish industry.

2 The fall in depreciation expenses reflects the impact of the valuation decrement for buildings as at 30 June 1999 which was brought to account in that year.

3 HPC's ownership interest in Hobart International Airport Pty Ltd grew in 1999-00 to 68 per cent.

HOBART PORTS CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*
Size						
Total assets	$M	49	51	61	61	64
Total revenue	$M	12	12	13	16	17
Profitability						
Operating profit before tax (includes abnormals)	$'000	328	1 763	1 709	371	765
Operating sales margin	%	-4.8	11.0	13.4	6.0	7.8
Cost recovery	%	108.2	109.6	103.9	103.5	108.5
Return on assets	%	0.9	4.2	3.7	1.7	2.3
Return on equity	%	0.7	2.7	3.5	1.0	1.7
Financial management						
Debt to equity	%	8.8	8.0	23.3	22.7	20.8
Debt to total assets	%	7.4	6.9	18.9	16.8	15.9
Total liabilities to equity	%	17.5	18.1	34.3	35.0	33.5
Interest cover	times	4.1	6.6	5.9	1.5	2.1
Current ratio	%	594.4	508.2	137.3	136.0	146.9
Leverage ratio	%	117.5	118.1	134.3	135.0	133.5
Payments to and from government						
Dividends	$'000	0	0	160	700	540
Dividend to equity ratio	%	0	0	0.4	1.5	1.2
Dividend payout ratio	%	0	0	10.5	148.1	67.4
Income tax expense	$'000	27	610	179	-102	-37
CSO funding	$'000	0	0	0	0	0

a A $1.3 million abnormal expense related to redundancies deflated operating profit. **b** Total revenue increased by $0.4 million as a result of a gain on the cancellation of a creditor. This gain was offset by an increase in redundancy expenses. **c** Includes abnormal revenue ($1.3 million) resulting from the transfer of title to land and buildings held by the Crown to the King Island Ports Corporation on 12 June 1998. Additional revenue was generated from the write-off of rental charges owing to the Tasmanian Treasury relating to King Island Ports facilities on 21 May 1998. Reporting period covers the 11 month period to 30 June 1998. The rise in total assets resulted from an increase in the value of property, plant and equipment. **d** Total revenue increased due to the sale of land ($0.4 million).

PORT OF DEVONPORT CORPORATION — Tasmania

The Port of Devonport Corporation (PDC), formerly the Port of Devonport Authority, was corporatised under the *Port Companies Act 1997*, effective from 30 July 1997. The PDC also manages the Devonport Airport.

In 1997-98, the PDC consolidated the financial results for the Devonport Airport in its financial statements.[1] Consolidation increased assets and improved PDC's debt to total asset, debt to equity and total liabilities to equity ratios. In addition, consolidation improved PDC's return on asset, return on equity and cost recovery ratios over and above that which would have occurred for the port operations alone.[2]

An increase in operating profit before tax (including abnormals) in 1999-00 was due to increased revenue from both seaport and airport operations. A $323 000 increase in seaport revenue resulted from a growth in throughput. Airport revenue grew by $220 000 as a result of increased passengers and an increase in landing and passenger charges. The cost recovery ratio was improved by a decrease in total expenses of $236 000.

The PDC is required to make both tax-equivalent and dividend payments. In 1998-99, the PDC paid a dividend to the Tasmanian Government representing 50 per cent of 1997-98 after tax profit. The 1999-00 dividend figure of $925 000 includes $304 000 paid in relation to the previous year and $621 000 provided for in relation to 1999-00.

1 The 1997-98 financial statistics cover the 11 month period to 30 June 1998.

2 Devonport Airport earned an operating profit in 1997-98 of $0.3 million.

PORT OF DEVONPORT CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*[c]	*1999-00*
Size						
Total assets	$M	29	29	43	45	46
Total revenue	$M	9	9	9	10	10
Profitability						
Operating profit before tax (includes abnormals)	$'000	1 622	1 018	1 446	453	2 069
Operating sales margin	%	19.5	13.1	16.0	6.5	21.8
Cost recovery	%	131.9	115.0	119.1	118.6	127.8
Return on assets	%	7.7	5.6	5.4	2.6	5.9
Return on equity	%	4.9	3.1	3.8	0.2	3.6
Financial management						
Debt to equity	%	34.6	30.2	23.8	25.3	22.2
Debt to total assets	%	25.3	21.5	21.0	19.5	16.7
Total liabilities to equity	%	43.9	42.0	34.0	33.4	33.5
Interest cover	times	4.3	2.7	3.8	1.7	4.3
Current ratio	%	470.3	455.0	480.9	454.6	322.7
Leverage ratio	%	143.9	142.0	134.0	133.4	133.5
Payments to and from government						
Dividends	$'000	0	0	0	440	925
Dividend to equity ratio	%	0	0	0	1.3	2.7
Dividend payout ratio	%	0	0	0	657.1	75.8
Income tax expense	$'000	665	374	442	386	849
CSO funding	$'000	0	0	0	0	0

a Total revenue includes $0.5 million from the sale a dredge. The increase in operating revenue associated with the sale of the dredge was offset by a special payment of $0.4 million to the Tasmanian Government pursuant to the *Port of Devonport Authority Bill 1996*. **b** In 1997-98, the Port of Devonport Corporation (PDC) consolidated Devonport Airport in its financial statements. 1997-98 covers the 11 month period to 30 June 1998. The increase in PDC's total assets in 1997-98 is largely attributable to the addition of Devonport Airport and all related investments. **c** Total assets increased due to harbour improvements associated with a capital dredging program. Abnormal expenses of $0.9 million relating to depreciation adjustments upon the reassessment of the useful life of non-current assets and the scrapping of fixed assets no longer held.

PORT OF LAUNCESTON PTY LTD — Tasmania

The Port of Launceston Pty Ltd was established on 30 July 1997 under the *Port Companies Act 1997*. Upon commencement of operations, the Port of Launceston acquired the Flinders Island Ports Company (formerly the Flinders Marine Board). The PLC consolidated Flinders Island Ports Corporation in its 1997-98 financial statements. Consolidation had a minimal impact on the Port's performance indicators.

Between 1995-96 and 1997-98, the Port of Launceston experienced operating losses before tax (including abnormals) due to the cessation of general cargo shipping operated by Coastal Express Line, coupled with rising expenses.[1] Unforseen expenses were incurred from the oil spill associated with the grounding of the Iron Baron and redundancy payments in 1995-96 and 1997-98. In 1998-99, the Port disposed of non-current assets, thus increasing operating profits. The increase in operating profit before tax (including abnormals) is attributable to abnormal revenue of $2 million relating to the settlement of a legal dispute in 1999-00.[2]

The Port's debt has remained relatively constant over the reporting period. Its debt to equity and debt to total asset ratios combined with low interest cover suggest the Port may be susceptible to increases in interest rates.

The Port of Launceston is required to make both tax-equivalent and dividend payments to the Tasmanian Government. The low income tax expense and income tax benefits incurred over the reporting period are attributable to both permanent and timing differences.

1 Prior to cessation, general cargo throughput accounted for 30 per cent of total port revenue.

2 The shipping company Coastal Express Line terminated a terminal lease, in June 1996, which was due to run until April 2001, as a result PLC entered into legal action against the company and others. A $2 million settlement was reached after mediation.

PORT OF LAUNCESTON PTY LTD (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*[c]	*1999-00*[d]
Size						
Total assets	$M	47	47	43	44	43
Total revenue	$M	9	7	7	8	10
Profitability						
Operating profit before tax (includes abnormals)	$'000	-438	-851	-290	220	1 476
Operating sales margin	%	7.5	5.2	13.3	19.8	25.0
Cost recovery	%	113.2	107.0	118.1	124.6	106.5
Return on assets	%	1.9	1.2	2.3	3.8	6.1
Return on equity	%	-1.4	-3.0	-3.6	2.1	4.9
Financial management						
Debt to equity	%	51.3	61.2	65.2	64.2	55.6
Debt to total assets	%	31.9	36.7	36.6	35.8	31.9
Total liabilities to equity	%	62.4	67.7	69.7	84.6	72.8
Interest cover	times	0.7	0.4	0.8	1.1	2.2
Current ratio	%	217.9	170.3	83.7	95.4	178.4
Leverage ratio	%	162.4	167.7	169.7	184.6	172.8
Payments to and from government						
Dividends	$'000	0	0	0	150	0[e]
Dividend to equity ratio	%	0	0	0	0.6	0
Dividend payout ratio	%	0	0	0	30.4	0
Income tax expense	$'000	-41	-288	-664	-274	268
CSO funding	$'000	0	0	0	0	0

a Operating profit in 1995-96 was deflated by $0.3 million resulting from the retrenchment of 15 employees, combined with increased expenses due to the grounding of the Iron Baron and the associated oil spill on 10 July 1995. **b** The Port of Launceston consolidated Flinders Island Ports Corporation in its financial statements from 1997-98. As a result of increased redundancy expenses operating profit was deflated by $0.2 million in 1997-98. **c** Both assets and liabilities increased in this year due to a change in the reporting treatment of future income tax benefit (non current asset) and the provision of deferred tax (non-current liabilities). Both total assets and total liabilities increased by $3.5 million. **d** Figures are influenced by $2 million of abnormal revenue — mainly the result of the settlement of a writ issued by the port against Coastal Express Line for the termination of a lease. **e** A dividend was payable in 1999-00 ($604 000), but was not declared within the reporting period. If included, dividend to equity is 2.4 per cent and the dividend payout ratio is 50 per cent.

DARWIN PORT CORPORATION — Northern Territory

The Darwin Port Corporation (DPC) was established under the *Darwin Port Corporation Act 1999*. The DPC, previously the Darwin Port Authority, began operating in September 1999 and is responsible for the management of port assets, including the East Arm Port facility and the provision of services such as reception facilities for cruise and naval vessels.

The growth in total revenue over the reporting period is attributable to community service obligation (CSO) funding and $20.5 million abnormal revenue generated by an asset sale in 1999-00.

The total value of assets decreased in 1999-00 by 50 per cent with a $60.6 million write-down in assets resulting from the revaluation of the East Arm Port facilities, using deprival methodology. The revaluation decrement, recorded as an abnormal item, adversely affects all profitability indicators. The exception is cost recovery, which excludes abnormal expenses in its calculation.

Profitability based on normal operating surplus (excluding abnormals) in 1999-00 increased by over 50 per cent.[1] Based on this growth and other things being equal, profitability indicators can be expected to improve on historical values in the forthcoming year.

During 1999-00, the DPC undertook debt restructuring. Debt levels were capped at $35 million — adjusted down from $56 million. The DPC was able to reduce its debt levels by transferring land and buildings valued at $20.5 million to the Government in exchange for the retirement of an equivalent level of debt. The decline in debt is reflected in the debt to total assets but is overshadowed in debt to equity, total liabilities to equity and interest cover ratios by the effects of the asset write-down.

The DPC received CSO funding to cover costs associated with the operation and management of the Stokes Hill wharf and precinct, the fishing harbour mooring basin and other wharf facilities. CSO funding was also received for the East Arm Port development.[2]

The DPC is required to make tax-equivalent and dividend payments to the Northern Territory Government. Dividend payments are set at 50 per cent of operating profit after tax. As a consequence, no dividend was paid in 1999-00.

---

1 In 1999-00 operating profit before abnormal items and income tax adjustment was $4.2 million compared to the 1998-99 profit of $2.7 million.

2 This CSO addressed debt servicing and costs incurred in the duplication of services. Funding associated with the East Arm Port development accounts for the majority of CSO payments since 1996-97.

DARWIN PORT CORPORATION (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*	*1996-97*[a]	*1997-98*	*1998-99*[b]	*1999-00*[c]
Size						
Total assets[d]	$M	67	111	135	136	68
Total revenue	$M	11	14	16	17	38
Profitability						
Operating profit before tax (includes abnormals)	$'000	1 438	-562	4 040	495	-47 685
Operating sales margin	%	20.7	0.4	40.F8	24.3	-117.5
Cost recovery	%	126.1	147.3	169.0	159.9	174.4
Return on assets	%	4.3	0.5	5.4	3.3	-43.4
Return on equity	%	4.5	-2.3	4.4	-1.0	-97.7
Financial management						
Debt to equity	%	102.2	113.6	78.9	76.6	132.4
Debt to total assets	%	57.1	65.0	47.1	41.8	34.2
Total liabilities to equity	%	104.9	118.4	83.7	83.6	158.3
Interest cover	times	2.3	4.8	2.5	1.1	-12.5
Current ratio	%	256.5	206.1	341.4	170.6	244.2
Leverage ratio	%	204.9	218.4	183.7	183.6	258.3
Payments to and from government						
Dividends	$'000	250	1 031	1 064	1 374	0
Dividend to equity ratio	%	0.8	2.5	1.7	1.9	0
Dividend payout ratio	%	17.4	-108.4	38.7	-178.2	0
Income tax expense	$'000	0	389	1 290	1 266	1 234
CSO funding	$'000	0	1 965	3 602	5 273	5 436

a In July 1996, the Darwin Port Corporation revalued its non-current assets using the deprival method, as a result, assets increased by $20 million. Operating profit before tax (including abnormals) was deflated by $4.2 million. This was the result of an abnormal expense concerning a downward adjustment to asset value due to revaluation. **b** Operating profit decreased due to a $2.2 million downward revaluation of assets.**c** Performance indicators, particularly profitability indicators, are influenced by the $60.6 million write-down of assets due to the application of deprival methodology to port infrastructure. **d** Capital works in progress relating to the East Arm Port increased total assets by $16.7 million in 1995-96, $28.9 million in 1996-97 and $20.9 million in 1997-98.

7 Commonwealth GTEs

Three Commonwealth government trading enterprises (GTEs) are covered in this chapter — Airservices Australia, Australia Post and Telstra. These GTEs vary significantly in size and in the range of services that they provide.

For a discussion of the data and the performance indicators used and some of the factors that should be considered when assessing performance see chapter 1.

AIRSERVICES AUSTRLIA — Commonwealth

Airservices Australia (ASA) was established in July 1995 under the *Air Services Act 1995*, and is responsible for providing and managing Australia's air navigation and air traffic services infrastructure.

Location specific pricing was introduced for fire fighting and rescue services in July 1997 and for terminal navigation in July 1998.[1] The aim of these pricing reforms was to price services more efficiently to reflect the cost of providing services at individual airports.

For most of the reporting period, net abnormal expenses have reduced ASA's operating profit. These expenses, which include downward revaluation of assets and provisions for redundancies associated with staff reductions, have resulted in the return on asset and return on equity ratios varying over the reporting period. Operating profit improved in 1999-00 with the inclusion of net abnormal revenue of $21.1 million due mainly to the write-back of legal provisions.

Despite having low or negative operating profit over the majority of the period, ASA has been generating adequate revenue to cover expenses. A number of non-commercial activities were provided by ASA over the reporting period, including a telephone complaints service regarding aircraft noise, aircraft noise and flight path monitoring, provision of environmental information and aviation search and rescue functions.[2] ASA does not receive direct funding for these activities.

ASA receives an $11 million Commonwealth Government subsidy aimed at enabling it to continue to cap prices at regional and General Aviation Airport Procedures airports.[3]

Airservices are required to make both tax-equivalent and dividend payments. Although no dividend payments were made in 1998-99, in 1999-00 there was a dividend of $13 million.

---

1 Terminal navigation charges are levied for the use of terminal navigation facilities and services for each landing, practice instrument approach or practice instrument approach immediately followed by a landing at an aerodrome with a control service for aircraft. These charges vary with maximum take-off weight of the aircraft, the time services are used and if the aerodrome is located in a capital city.

2 This function was transferred over to Australian Search and Rescue, which is managed by the Australian Maritime Safety Authority, in July 1997.

3 The subsidy is expected to cease during 2000-01.

AIRSERVICES AUSTRALIA (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*[c]	*1998-99*[d]	*1999-00*[e]
Size						
Total assets	$M	796	732	747	671	619
Total revenue	$M	580	619	607	605	636
Profitability						
Operating profit before tax (includes abnormals)	$'000	41 885	16 963	-48 012	-173 178	78 291
Operating sales margin	%	9.9	4.8	-6.1	-27.2	13.4
Cost recovery	%	110.7	107.3	107.0	108.0	110.0
Return on assets	%	7.1	4.0	-4.9	-23.1	13.3
Return on equity	%	4.0	1.9	-9.2	-44.8	15.9
Financial management						
Debt to equity	%	43.3	41.6	49.8	48.3	42.3
Debt to total assets	%	22.9	20.6	22.7	14.5	15.5
Total liabilities to equity	%	84.0	93.5	121.7	214.3	162.0
Interest cover	times	3.6	2.3	-3.1	-17.9	11.0
Current ratio	%	39.4	38.7	2.6	46.8	85.5
Leverage ratio	%	184.0	193.5	221.7	314.3	262.0
Payments to and from government						
Dividends	$'000	10 200	5 950	5 950	0	13 000
Dividend to equity ratio	%	2.4	1.5	1.7	0	5.8
Dividend payout ratio	%	59.9	76.7	-18.0	0	36.4
Income tax expense	$'000	24 849	9 205	-15 025	-49 815	42 544
CSO funding	$'000	0	0	0	0	0

a Abnormal expenses of $7.1 million from revaluation decrement on airways and general technical equipment, land and civil works. **b** Abnormal expenses of $34.9 million from revaluation decrement on land, buildings, and infrastructure. Plant and equipment revaluation decrement in 1997 of $7.3 million is related to the shortening of its useful life as a result of the Government's decision to auction the 1.8GHz spectrum. This figure also included allowances for changes to staff awards and redundancy payments arising from organisational restructure and staff termination payments arising from the transfer of the Search and Rescue (SAR) function to Australia Maritime Safety Authority (AMSA). **c** Abnormal expenses of $80.7 million from charges to profits for the provision for litigation, separation and redundancy payments and direct project costs arising from major organisational restructuring, provision for legal costs, revaluation decrement on infrastructure, plant and equipment, provision for early retirement benefits and staff termination payments arising from the transfer of the SAR function to AMSA. **d** Abnormal expenses of $228.2 million from separation and redundancy payments, devaluation of property, plant and equipment, Business Transformation Program costs, year 2000 direct project costs, Avgas refund and provisions for legal costs and litigation. **e**Abnormal revenue of $21.1 million generated by the write-back of legal provisions and asset sales. Successful outcomes in litigation enabled the write-back of legal provisions totalling $30.9 million relating to the Compass I, Compass II cases and Hughes litigation.

AUSTRALIA POST — Commonwealth

Australia Post was established in 1975 and corporatised in 1989 under the *Australian Postal Corporation Act 1989.* Its principal activities are letter delivery, parcel delivery, third party agency services (receiving bill payments for other companies) and the sale of postal products and merchandise. Australia Post holds a legislative monopoly for the processing and distribution of letters under 250 grams.

Over the reporting period, total assets and total revenue have increased steadily. A significant growth in revenue occurred in the 1999-00 reporting period and was attributed to a 6.5 per cent growth in mail volume. Year-to-year profit level fluctuations have been attributed to abnormal revenues increasing profits in 1995-96 and abnormal expenses decreasing profits in 1997-98.

Operating profit has fluctuated over the reporting period. Although there were no abnormal revenues recorded in 1999-00, there were one-off factors, which inflated demand and increased operating revenue. These include the introduction of the GST, the October constitutional referendum, an unusually high number of company floats and the Sydney Olympic Games.

A reversal in the upward trends of both the debt to equity and debt to total assets ratios occurred in 1999-00. This change is mainly the result of growth in total assets of $183.8 million.[1]

Australia Post is subject to all taxes and pays dividends to the Commonwealth Government. Dividend payments peaked over the reporting period at a high of $219.9 million in 1996-97.

Community service obligations (CSOs), as set out in s. 27 of the *Australian Postal Corporation Act 1989*, require that all Australians be provided with a letter service which reasonably meets their needs on an equitable basis and a domestic standard letter service at a uniform price. In addition, Australia Post must ensure that performance standards for the letter service reasonably meet the social, industrial and commercial needs of the Australian community. The uniform standard letter service has remained unchanged at 45 cents since January 1992.[2]

1 Growth in assets during 1999-00 is largely attributable to growth in receivables ($105.7 million), including bills of exchange, promissory notes, interest, and goods and services.

2 Australia Post receives no financial assistance from the Government to meet these CSOs. The cost of CSOs was estimated at $79 million for 1999-00.

AUSTRALIA POST (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*	*1997-98*[b]	*1998-99*	*1999-00*[c]
Size						
Total assets	$M	2 382	2 589	2 736	2 854	3 037
Total revenue	$M	2 944	3 155	3 300	3 468	3 743
Profitability						
Operating profit before tax (includes abnormals)	$'000	368 000	353 100	335 200	373 000	391 900
Operating sales margin	%	12.5	11.5	10.3	11.0	10.9
Cost recovery	%	113.4	112.9	113.0	112.5	113.5
Return on assets	%	17.0	15.1	13.4	14.2	14.4
Return on equity	%	27.3	26.9	26.3	27.1	25.0
Financial management						
Debt to equity	%	36.1	43.0	52.2	54.7	47.8
Debt to total assets	%	13.8	14.8	16.8	19.0	18.0
Total liabilities to equity	%	170.7	202.6	218.9	194.3	173.8
Interest cover	times	16.9	16.3	17.0	15.8	13.3
Current ratio	%	76.4	87.5	90.6	87.9	93.8
Leverage ratio	%	270.7	302.6	318.9	294.3	273.8
Payments to and from government						
Dividends	$'000	142 600	219 900	215 100	148 700	155 700
Dividend to equity ratio	%	16.4	25.3	25.1	16.3	15.0
Dividend payout ratio	%	60.0	94.3	95.6	60.0	60.0
Income tax expense	$'000	130 400	119 900	110 200	125 200	132 400
CSO funding	$'000	0	0	0	0	0

a Credit resulting from an adjustment to the provision for long service leave contributed to net abnormal revenue of $23.9 million. **b** Net abnormal expenses of $41.2 million came from charges resulting from year 2000 software modification costs, and charges resulting from a bond rate movement effect on employee entitlement provisions. **c** Net abnormal expenses of $34 million incurred for year 2000 compliance and GST implementation costs.

TELSTRA — Commonwealth

Telstra Corporation Limited was established in April 1993 and operates under the *Telecommunications Act 1997*. Telstra's principal activities include providing telephone exchange lines, local and long-distance phone services, international services, mobile telecommunication services, and a range of data, Internet and on-line services.

Revenue and operating profit increased steadily over the reporting period. Revenue growth has been mainly attributable to new product areas such as mobile services, data services, facsimile and ISDN services.[1] Increased operating profit within the 1999-00 financial period was driven by growth in non-traditional goods and services, increased inter-carrier revenue and asset sales worth $584 million.

The debt to equity and debt to total assets ratios rose in 1999-00. The increase was driven by a 31.5 per cent growth in borrowings, used to replenish working capital, after payment of the final dividend in October 1999. This payment included the special dividend of $2.1 billion.[2]

Telstra is subject to all taxes and pays dividends to its shareholders.[3] Some of the variability in the dividend payout ratio over the reporting period can be explained by special dividend payments, $3.2 billion in 1996-97 and $2.1 billion in 1998-99. Income tax expense in 1999-00 is lower due to a reduction in the company tax rate from 36 per cent to 34 per cent for 2000-01 and 30 per cent thereafter.

Telstra's Universal Service Obligation (USO) requires that standard telephone services, including services for the disabled, public payphones and prescribed carriage services, are reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on business. [4]

Telstra does not receive Government funding for the USO or DDO.[5]

---

1 During 1999-00, $656 million of the increased revenue was attributable to data text, Internet products and mobile services. Tradition revenues declined by $342 million.

2 Due to privatisation the company declared a special dividend of 16 cents per share, payable as part of the final dividend on 29 October 1999.

3 Telstra was first partially privatised in November 1997, when 33 per cent of the Corporation was floated. The second sell-off of 16 per cent occurred in October 1999.

4 Telstra is also subject to the Digital Data Obligation (DDO) — reasonable and equitable access on a 64kbps ISDN service or a broadly comparable satellite downlink service to at least 96 per cent of the Australian population.

5 The net cost of universal service provision in 1999-00 was shared among carriers based on proportion of eligible telecommunications revenue.

TELSTRA (continued)

Performance indicators 1995-96 to 1999-00

	Units	*1995-96*[a]	*1996-97*[b]	*1997-98*	*1998-99*	*1999-00*[c]
Size						
Total assets	$M	24 362	25 858	26 470	27 682	30 339
Total revenue	$M	15 239	15 983	17 302	18 218	19 840
Profitability						
Operating profit before tax (includes abnormals)	$'000	3 446 700	2 073 000	4 468 000	5 320 000	5 349 000
Operating sales margin	%	25.4	15.6	29.2	32.1	29.9
Cost recovery	%	131.7	136.1	141.3	147.4	148.7
Return on assets	%	16.4	10.3	19.5	21.8	20.6
Return on equity	%	18.9	14.2	31.0	32.6	33.5
Financial management						
Debt to equity	%	42.3	80.3	69.7	70.1	84.6
Debt to total assets	%	22.1	31.8	29.5	26.6	33.9
Total liabilities to equity	%	92.3	160.2	138.9	168.9	161.5
Interest cover	times	7.5	5.0	8.0	10.2	9.5
Current ratio	%	87.4	70.3	52.8	44.8	51.9
Leverage ratio	%	192.3	260.2	238.9	268.9	261.5
Payments to and from government						
Dividends	$'000	1 368 000	4 146 000[d]	1 802 000	4 247 000[e]	2 316 000[f]
Dividend to equity ratio	%	11.2	36.7	17.1	39.7	21.2
Dividend payout ratio	%	59.4	257.7	55.3	121.8	63.1
Income tax expense	$'000	1 144 600	464 000	1 211 000	1 832 000	1 676 000
CSO funding	$'000	0	0	0	0	0

a Abnormal revenue of $204.6 million received from a change in the depreciation methodology for communication assets. **b** Net abnormal expenses of $1.7 billion. This was attributable to provisions for broadband network rationalisation, loss on long-term construction contracts, the write-down of broadband network communication assets and most significantly, provisions for redundancy and restructuring which accounted for almost half of the abnormal expenses incurred in 1996-97. **c** Includes abnormal expense of $574 million for planned and actual redundancies. **d** As part of a restructuring of Telstra's capital base in preparation for privatisation, a special dividend payment of $3.2 billion was made to the Commonwealth Government. **e** Part of this would have been distributed to private shareholders. **f** Government equity in Telstra is 50.1 per cent therefore a proportion of these dividends would have gone to private shareholders.

A Participating enterprises

Table A.1 **Participating enterprises by jurisdiction, 1999-00**

GTE	*Industry Classification*
New South Wales	
Delta Electricity	Electricity
Macquarie Generation	Electricity
Pacific Power	Electricity
TransGrid	Electricity
Advance Energy	Electricity
Australian Inland Energy	Electricity
EnergyAustralia	Electricity
Great Southern Energy	Electricity
Integral Energy	Electricity
NorthPower	Electricity
Hunter Water Corporation	Water
Sydney Water Corporation	Water
Sydney Catchment Authority	Water
State Transit Authority	Urban Transport
State Rail Authority of NSW	Railways/Urban Transport
Freight Rail Corporation of NSW	Railways
Newcastle Port Corporation	Port Authorities
Port Kembla Port Corporation	Port Authorities
Sydney Ports Corporation	Port Authorities
Victoria	
Barwon Water	Water
City West Water	Water
Melbourne Water Corporation	Water
South East Water	Water
Yarra Valley Water	Water
Melbourne Port Corporation	Port Authorities
Victorian Channels Authority	Port Authorities

(Continued next page)

Table A.1 (continued) **Participating enterprises by jurisdiction, 1999-00**

GTE	*Industry Classification*
Queensland	
CS Energy	Electricity
Stanwell Corporation	Electricity
Tarong Energy	Electricity
Enertrade	Electricity
Powerlink	Electricity
Ergon Energy	Electricity
Energex	Electricity
Sun Water	Water
Queensland Rail	Railways/Urban Transport
Gladstone Port Authority	Port Authorities
Port of Brisbane Authority	Port Authorities
South Australia	
South Australian Water Corporation	Water
TransAdelaide	Urban Transport
South Australian Ports Corporation	Port Authorities
Western Australia	
Western Power	Electricity
Water Corporation	Water
Westrail	Railways/Urban Transport
Bunbury Port Authority	Port Authorities
Fremantle Port Authority	Port Authorities
Tasmania	
Hydro-Electric Corporation	Electricity
Aurora Energy	Electricity
Transend	Electricity
Hobart Regional Water Authority	Water
North West Water Authority	Water
Esk Water Authority	Water
Metro Tasmania Pty Ltd	Urban Transport
Burnie Port Corporation	Port Authorities
Hobart Port Corporation	Port Authorities
Port of Devonport Corporation	Port Authorities
Port of Launceston Pty Ltd	Port Authorities
Australian Capital Territory	
ACTION	Urban Transport

(Continued next page)

Table A.1 (continued) **Participating enterprises by jurisdiction, 1999-00**

GTE	*Industry Classification*
Northern Territory	
Darwin Port Authority	Port Authorities
Commonwealth	
Snowy Mountains Hydro-Electric Authority	Electricity
National Railway Corporation	Railways
Airservices Australia	Other Commonwealth
Australia Post	Other Commonwealth
Telstra Corporation	Other Commonwealth

B Definitions of Financial Performance Indicators

Table B.1 **Published financial performance indicators**

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

Table B.2 **Non-published financial performance indicators ($'000)**

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

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

(Continued next page)

Table B.2 (continued) **Non-published financial performance indicators ($'000)**

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

References

ABS (Australian Bureau of Statistics) 2000, *Government Financial Statistics*, Cat. no. 5512.0, ABS, Canberra.

—— 2001, Building Activity, Australia, Catalogue no. 8752.0, ABS, Canberra.

Association of Australian Ports and Marine Authorities 2001, *Total Throughput-Mass Tonnes*, http://www.aapma.org/aapma/trade/totalthroughput_9800.php3, (accessed 24 January 2001).

Australian Competition and Consumer Commission 1999, *NSW and ACT Transmission Network Revenue Caps 1999/00-2003/04*, Draft Decision, 12 May.

Bloomberg L.P. 2001, '*Dividend Paid by ASX Listed Companies 1999-00'*, New York, http://www.bloomberg.com (accessed 4 April 2001).

Cap Gemini Ernst and Young 2000, *Assessing the Long Run Marginal Costs of Generation in New South Wales*, Report for IPART, September 2000.

Chartered Accountants and Australian Society of CPAs 2000, *Accounting Handbook 2000*, Vol 1, Prentice Hall, Australia.

GSE (Great Southern Energy) 2001, *Electricity Market*, http://www.gsenergy.com.au/20_business/24_energy_market.htm, (accessed 11 April 2001).

Hey-Cunningham, D 1998, *Financial Statements Demystified*, 2nd edition, Allen and Unwin, NSW

Hoggett, J and L. Edwards 2000, *Accounting in Australia*, 5th edition, John Wiley and Sons, Brisbane.

Hulls, C. A and W. S Yeadon 1992, *Understanding business ratios and finances*, The Business Library, Melbourne.

IPART (Independent Pricing and Regulation Tribunal) 1998, *The Rate of Return for Electricity Distribution Networks*, Discussion Paper, November, Sydney.

—— 1999a, *Regulation of NSW Electricity Distribution Networks*, Determination and rules under the National Electricity Code, December, Sydney.

—— 1999b, *Aspects of the NSW Rail Access Regime*, Final Report, April, Sydney.

Meyrick and Associates and Tasman Asia Pacific 1998, *Measures to Promote Effective and Efficient Container Port Practices*, Final Report prepared for Marine and Ports Group of the Australian Transport Council.

National Electricity Market Management Company Limited (NEMMCO) 2001, Sydney, *Average Monthly Prices 1999-00*, http://www.nemmco.com.au/data/avg%20price%2099-00.htm, (accessed 15 March 2001).

ORG (Office of the Regulator-General, Victoria) 2000, *Victorian Ports Price Review: Melbourne Ports Corporation and Victorian Channels Authority*, May, Melbourne.

Productivity Commission 2000, *Financial performance of Government Trading Enterprises 1994-95 to 1998-99*, Performance Monitoring, Ausinfo, Canberra.

Queensland Competition Authority 2001, *Draft Decision on QR's Draft Undertaking*, http://www.qca.org.au/page.cfm?pageID=69&topmenuitem=rail, (accessed 9 May 2001).

Queensland Treasury 1997, *Recording and Valuation of Non-Current Physical Assets in the Queensland Public Sector*, http://www.treasury.qld.gov.au/pdfdocs/phyasset.pdf, (accessed 10 May 2001)

Rail Projects Taskforce 1999, *Revitalising Rail*, Department of Transport and Regional Services, Canberra.

SCNPMGTE (Steering Committee on National Performance Monitoring of Government Trading Enterprises) 1994, *Guidelines on Accounting Policy for Valuation of Assets of Government Trading Enterprises Using Current Valuation Methods*, October, Canberra.

—— 1997, *Government Trading Enterprises Performance Indicators 1991-92 to 195-96*, vol 1, May.

South Australian Department of Treasury & Finance 2001, *Uniform Financial Information South Australia 2000-2001*, http://www.treasury.sa.gov.au/budg2k1, (accessed 10 May 2001).

Troy 2000, *Almanac of Business and Industrial Financial Ratios*, Prentice Hall, Paramus.