Queensland Audit Office

Results of audit: Public non-financial corporations

Report 6: 2014–15

Queensland Audit Office

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Queensland Audit Office

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The Honourable F Simpson MP
Speaker of the Legislative Assembly
Parliament House
BRISBANE QLD 4000

Dear Madam Speaker

Report to Parliament

This report is prepared under Part 3 Division 3 of the *Auditor-General Act 2009*, and is titled *Results of audit: Public non-financial corporations* (Report 6: 2014–15)

In accordance with s.67 of the Act, would you please arrange for the report to be tabled in the Legislative Assembly.

Yours sincerely

Andrew Greaves
Auditor-General

Contents

Summary

Public sector entities are classified for financial reporting purposes into three groups:

- General government sector (GGS) entities—comprising departments and other largely budget-dependent bodies.
- Public financial corporations (PFC)—that provide insurance services and borrow and invest funds on behalf of government. These are WorkCover Queensland, the Queensland Treasury Corporation and QIC Limited.
- Public non-financial corporations (PNFC)—government owned corporations (GOCs) and statutory bodies that operate primarily across the energy, water, transport sectors.

Most PNFCs sell goods and services on commercial trading terms; they pay taxes and return dividends to the state government. By contrast, most GGS entities do not generate significant own-sourced revenue and rely primarily on annual budget appropriations to fund their activities and services.

While we continue to report on each entity and sector separately, this report also summarises the combined results for all PNFCs, to better understand how they affect the financial aggregates of the state in 2013–14. These results should however be understood in the context of the fact that PNFCs operate inherently different businesses, which limits comparisons of financial performance, position, and sustainability between entities and industry sectors.

Figure A lists the major PNFCs discussed in this report and how they fit into the state's energy, water and transport networks. PNFCs which were abolished or ceased to exist legally before 1 July 2013 have been excluded from any comparisons between entities and industries in this report.

As well as those listed in Figure A, six other entities were classified as PNFCs at 30 June 2014. Last year it was seven, but the Parklands Gold Coast Trust was abolished on 30 September 2013 and its assets and liabilities were transferred to the Department of National Parks, Recreation, Sport and Racing during the year.

Of these six other entities, the substantial PNFCs at 30 June 2014 were Stadiums Queensland and Queensland Treasury Holdings Pty Ltd (QTH):

- Stadiums Queensland manages, operates and promotes the use of major sporting and entertainment facilities on behalf of the Queensland Government. Stadiums Queensland is unlike other PNFCs. It does not recover the majority of the costs it incurs providing venues to hirers and tenants. It also does not pay income tax equivalents and dividends to government.
- QTH and its subsidiaries hold the state's interest in assets of strategic importance. These include the state's interest in shares and its residual holdings of land from government asset transactions.

Figure A
Major PNFCs by industry segment and purpose

Industry	Purpose	Entity	Type
Electricity	Generation	CS Energy Limited (CS Energy)	PNFC
		Stanwell Corporation Limited (Stanwell)	PNFC
	Transmission	Queensland Electricity Transmission Corporation Limited (trading as Powerlink)	PNFC
	Distribution	Ergon Energy Corporation Limited (Ergon)	PNFC
		Energex Limited (Energex)	PNFC
	Retailers	Ergon Energy Queensland Pty Ltd (Regional Queensland only)	PNFC
		Non-government entities	Private sector
Water	Combination of supply, storage and distribution	Queensland Bulk Water Supply Authority (trading as Seqwater)	PNFC
		SunWater Limited (SunWater)	PNFC
		Two 'category one' water boards (Gladstone Area Water Board and Mount Isa Water Board)	PNFC
		20 'category two' water boards	GGS
	Retailers	Central SEQ Distributor Retailer Authority (trading as Queensland Urban Utilities)	Local government (LG) sector
		Northern SEQ Distributor Retailer Authority (trading as Unitywater)	LG sector
		Municipal councils	LG sector
Transport	Rail	Queensland Rail Transit Authority (Queensland Rail)	PNFC
		Queensland Rail Limited	PNFC
		Non-government entity	Private sector
	Ports	Far North Queensland Ports Corporation Limited (trading as Ports North)	PNFC
		Gladstone Ports Corporation Limited	PNFC
		North Queensland Bulk Ports Corporation Limited	PNFC
		Port of Townsville Limited	PNFC
		Non-government entity	Private sector
	Roads	Department of Transport and Main Roads	GGS
		Municipal councils	LG sector

Source: Queensland Audit Office

Queensland Rail Limited became a fully integrated provider of rail services on 1 July 2010. As a result, any comparisons between rail and other PNFC industries include only four years of Queensland Rail Limited's results.

Audit opinions and conclusions

We issued 26 audit opinions on the financial reports of the PNFCs and the entities they control; and 25 audit opinions or conclusions on other engagements which are not ordinarily part of the audit of a financial report. An audit opinion provides a higher level of assurance, than a conclusion.

All opinions and conclusions were unqualified. This means that the financial reports complied with relevant Australian accounting standards and prescribed requirements; and for the other engagements, that the information presented was prepared in accordance with the basis of preparation set out within the report and was suitable for its intended users.

Figure B summarises the number of financial audits and other engagements by sector.

Figure B
Audit opinions and conclusions issued, by sector

Sector	Parent entities	Controlled entities	Other engagements
Energy	5	3	24*
Water	4	1	—
Port	4	—	—
Rail	1	1	1
Other	3	4	—

* Includes 12 opinions and 12 conclusions. All other reports were issued with an audit opinion.

Source: Queensland Audit Office

Emphases of matter

We included emphases of matter within 27 of the opinions and conclusions issued. Emphases of matter do not modify an opinion or conclusion. An emphasis of matter serves only to highlight an issue of which the auditor believes the users of the audited report need to be aware.

Figure C details the reasons why we included these emphases of matter.

Figure C
Summary: emphases of matter issued

Name of audit	Description of audit / review	Reason for emphasis of matter
Parklands Gold Coast Trust	General Purpose Financial Report audit for the period ending 30 September 2013	Highlights to the reader that the entity had been abolished and its assets, liabilities and operations transferred to the Department of National Parks, Recreation, Sport and Racing on 30 September 2013.
City North Infrastructure Pty Ltd	General Purpose Financial Report audit for the year ended 30 June 2014	Highlights to the reader that the entity was expected to be abolished in 2014–15.
12 x Regulatory Information Notice (RIN) engagements	Audit and review of information from Ergon and Energex as required by the Australian Energy Regulator (AER) across multiple years	Highlights to the reader that information in these reports were prepared on the basis of key assumptions as detailed within the basis of preparation section of these reports. These reports were also prepared for the purpose of fulfilling Ergon and Energex's reporting responsibilities to the AER.
Below Rail	Special Purpose Financial Report audit for the year ended 30 June 2013	Highlights to the reader that the financial report is a special purpose financial report prepared specifically to meet the information needs of the Queensland Competition Authority and those who may seek access to rail infrastructure for the purpose of operating trains.

Source: Queensland Audit Office

Timeliness and quality of financial reports

We certified and audited the financial reports for all 26 entities in this report by their legislative deadlines. Entities provide draft financial reports to us for audit on an agreed date. In 2013–14, 65 per cent of the 26 entities in this report provided their draft financial report to audit by the agreed time.

Government owned corporations and statutory bodies have their financial reports prepared and audited no later than 31 August each year. Exemptions can be granted but only by approval from the Treasurer for statutory bodies. No exemptions were requested in 2013–14.

Large public companies limited by shares must have their financial reports prepared and audited no later than 31 October each year.

Accuracy of financial report account balances

Draft financial reports provided for audit were generally satisfactory. In total, $422.3 million of material errors identified by management and audit required correction after the draft financial reports were provided to us for auditing.

These related to asset and tax balances within the draft financial reports of the Gladstone Ports Corporation totalling $407 million, and the Port of Townsville Limited totalling $15.3 million.

Adjustments to prior period balances within financial reports

Financial reports contain both current and prior year balances. The majority of changes to prior period balances within financial reports can result from errors not identified in previous years, better information becoming available, and changes in Australian accounting standards.

Changes were required to the prior period balances within the draft financial reports of North Queensland Bulk Ports Corporation Limited, Ergon, Energex and Stadiums Queensland in 2013–14, totalling $46.7 million.

Quality of financial report disclosures

The narrative disclosures within the notes to the draft financial reports were generally satisfactory. The majority of disclosure changes were the result of entities electing to improve the quality of disclosures within their financial reports.

Disclosure errors which required changes to the draft financial report related to entities' application of Australian Accounting Standard AASB 13 *Fair Value Measurement,* which came into effect for financial reporting periods commencing on or after 1 January 2013.

A number of disclosure changes were also required to the draft financial report of Queensland Rail due to its establishment as a statutory body on 3 May 2013.

Significant financial reporting issues

In forming our audit opinion, we must resolve any significant financial reporting issues we identify during an audit to ensure that the financial report is not materially misstated. The major issue we encountered related to the financial reporting of assets.

Financial reporting of property, plant and equipment

Valuation of assets

AASB 116 *Property, Plant and Equipment* prescribes the accounting treatment for property, plant and equipment so that users of a financial report can discern information about an entity’s investments in its property, plant and equipment and the changes in these investments. In the context of PNFCs, AASB 116 gives entities the choice of adopting either the cost or revaluation model when deciding how to value a class of assets for financial reporting purposes. The revaluation model is another way of describing assets recognised at their current fair values.

Where an entity decides to adopt the revaluation model for a class of assets, it is required to choose a valuation technique that will result in the valuation of those assets best approximating their fair values.

Figure D details the valuation model and technique adopted by the 15 PNFCs with material property, plant and equipment account balances in their financial reports.

Figure D
Valuation of property, plant and equipment

Model	Measurement/valuation technique	Number of entities
Cost	This is generally the fair value of assets/liabilities exchanged to acquire or construct the asset, with no subsequent change to these values to reflect cost, price or market movements.	4*
Revaluation	Income approach (present value technique that takes into account the future cash flows that a market participant would expect to receive)	7
	Replacement cost (valuation technique that reflects the amount that would be required currently to replace the service capacity of an asset)	4

* Queensland Rail and Queensland Rail Limited is taken to be one entity for the purposes of Figure D. Queensland Rail Limited controls significant property, plant and equipment and is consolidated into Queensland Rail for financial reporting purposes.

Source: Queensland Audit Office

Where entities decide to value their assets at fair value, AASB 13 *Fair Value Measurement* prescribes further accounting treatments relating to how fair value should be derived. AASB 13 became applicable for the first time in 2013–14. In this regard, the application of AASB 13 has affected the disclosures within the financial reports of entities which have elected to recognise their property, plant and equipment at fair value, but did not affect their valuations.

The valuation of assets is heavily predicated upon management assumptions and estimates. PNFCs' management teams were able to justify the assumptions and estimates they used in previous years against the principles of AASB 13.

Three of the four port corporations had significant fluctuations in the values of their assets over the past five years mostly due to asset revaluations and major asset disposals. A change in valuation technique from replacement cost to the income approach contributed to an uplift in the net value of Gladstone Ports Corporation Limited's and Port of Townsville Limited's assets by between 25 and 27 per cent. Significant changes were noted to the valuation of North Queensland Bulk Ports Corporation Limited's assets when it undertook a comprehensive revaluation exercise in 2011–12.

Impairment of assets

Australian Account Standard, AASB 136 *Impairment of Assets* requires these entities to assess certain assets for impairment each year. Where indicators of impairment exist, entities are required to write the value of impaired assets down to their recoverable amount in certain circumstances.

While having no effect this year, factors such as the impact of liquefied natural gas on the Queensland electricity market; changes to renewable energy targets; and the implementation of any new environmental / carbon measurements have the potential to affect the recoverable amount of assets held by Queensland's two electricity generators (CS Energy and Stanwell) in future years.

Other significant entity-specific financial reporting issues

Figure E summarises other significant entity-specific reporting issues that required resolution before we could issue an unqualified audit opinion.

Figure E
Significant entity-specific financial reporting issues

Industry	Issue
Energy (Chapter 2)	• Status of going concern issues relating to CS Energy, affecting its ongoing financial sustainability. • Ergon, Energex and Powerlink collectively held $1.48 billion in receivables as under recovery of revenues at 30 June 2014 (30 June 2012: $512.3 million). Time frames for recovery are subject to AER's annual pricing approval process.
Water (Chapter 3)	• The effect of the Queensland Competition Authority's review of Seqwater's bulk water prices from 1 July 2015 to 30 June 2018, and price monitoring investigation for the GAWB from 1 July 2015 to 30 June 2020, has historically affected prices that entities can charge for services they provide.
Ports (Chapter 4)	• Assets under construction (AUC) of nearly $87 million have been written off over the past five years. This has reduced profits made by port sector PNFCs by nine per cent, and reduced dividends to the government by $49 million across the same period.

Source: Queensland Audit Office

Financial performance, position and sustainability

When forming our audit opinion on the financial report of an entity, we must assess its ability to operate as a going concern. As part of this process, we assess its financial performance, position and sustainability, including its ability to:

- meet day to day operating expenses
- replace and augment assets to meet current and expected future service levels
- pay debts when they fall due.

Their current profitability and recent past performance means that, overall, PNFCs have been, and remain, financially sustainable in the short to medium term. The longer term financial sustainability of CS Energy, Seqwater, and Stadiums Queensland remains dependent on a number of pricing, funding and other business factors. Queensland Rail's declining capital replenishment ratios are also a leading indicator of future risks with the replacement of its stock of non-current assets, should this trend continue.

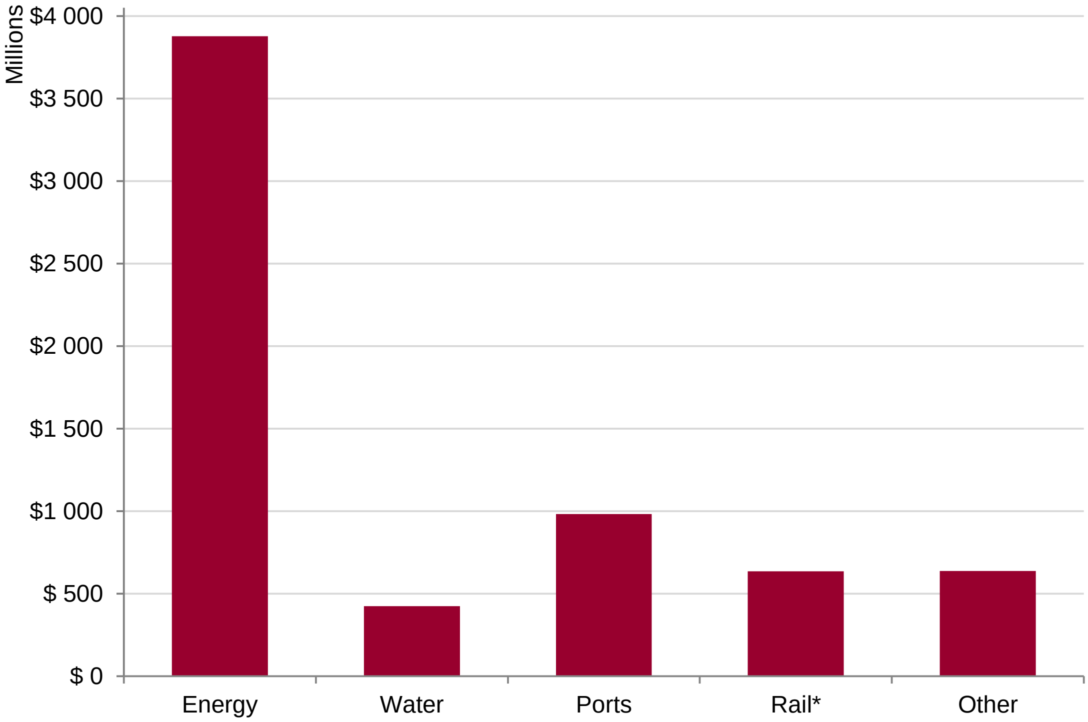
Financial performance and position

PNFCs in this report collectively earned after tax profits of $1.6 billion in 2013–14 ($6.6 billion for the five years to 30 June 2014). They generated income of $13.6 billion in 2013–14 ($57.3 billion for the past five years) and spent $11.1 billion in 2013–14 ($48.8 billion across the same five-year period).

Figure F compares the sum of profits after tax made by PNFCs within each of the industry sectors in the five years to 30 June 2014. PNFCs within the energy sector contributed 59 per cent of after tax profits.

PNFCs within the water sector earned $425.1 million. This result was largely due to $867.9 million in income tax credits that were brought to account by Seqwater over the past two years. PNFCs within the water sector in this report collectively made a loss of $385 million over the last five years before tax.

Figure F
Profits after tax by sector for the five years from 2009–10 to 2013–14



* Queensland Rail Limited became a fully integrated provider of rail services on 1 July 2010. As a result, this figure only includes the profits after tax of the PNFC rail sector in the four years to 30 June 2014.

Source: Queensland Audit Office

Property, plant and equipment (PPE) made up $54.6 billion (86 per cent) of the $63.8 billion in total assets held by PNFCs as at 30 June 2014. Their borrowings made up $31 billion (71 per cent) of the $43.9 in total liabilities at the same date.

Of the total property, plant and equipment held:

- entities within the energy sector recorded the highest value of assets—$32.7 billion (51 per cent of all PNFC assets)
- followed by entities within the water sector, which recorded $12.4 billion in assets (19 per cent of all PNFC assets).

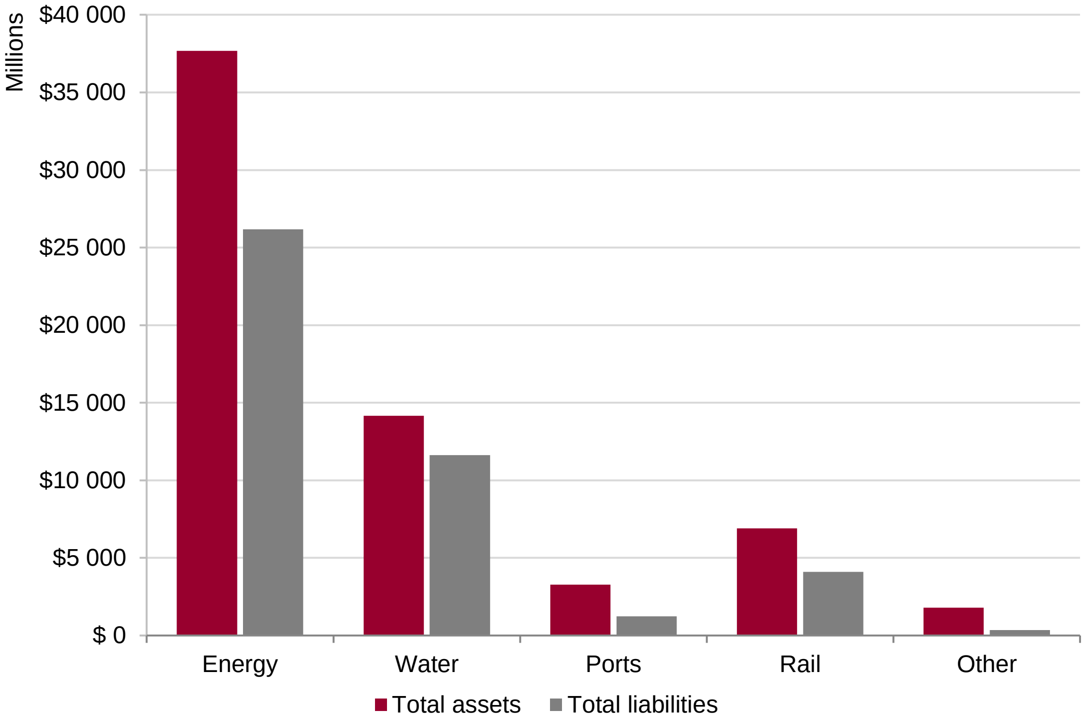
Of the total borrowings held:

- entities in the energy sector had the most debt at $17.1 billion (39 per cent of all PNFC liabilities)
- followed by entities within the water sector of $9.7 billion (22 per cent of all PNFC liabilities).

Borrowings by entities within the energy sector were mainly held by the network businesses of Powerlink, Energex and Ergon to fund their infrastructure programs. Borrowings of water sector PNFC entities were mainly held by Seqwater at 30 June 2014.

Figure G compares total assets and liabilities held by PNFCs within this report by industry sector at 30 June 2014.

Figure G
Assets and liabilities by industry sector at 30 June 2014



Source: Queensland Audit Office

Financial sustainability

Current year performance and position are important indicators of financial health. Recent past experiences are also leading indicators for identifying adverse trends and possible weaknesses that could affect future sustainability.

We use ratios derived from the published financial report to conduct this analysis:

- operating ratio
- capital replenishment ratio
- debt to revenue ratio.

When considered together, the five-year average results of these three ratios indicate that PNFCs are financially sustainable in the short to medium term. As a sector, PNFCs are generally generating sufficient income to pay their ongoing expenses; replace and add to their stock of assets at a rate faster than they are depreciating; and maintaining stable debt levels, when compared to revenue generated.

The longer term sustainability of four PNFCs, however, will continue to be influenced by the factors outlined in Figure H.

Figure H
Factors affecting longer term sustainability

Sector	Entity	Factors affecting financial sustainability
Energy	CS Energy	CS Energy's ability to meet its future expenditure and capital commitments is affected by the following factors: • onerous contract in place with third parties which have a negative effect on CS Energy's financial performance • coal supply issues to the Callide Power Station • future demand and electricity pricing.
Water	Seqwater	Seqwater's continuing long term financial sustainability is predicated on increases in bulk water prices to a point where the price of bulk water catches up with the cost of supplying this water. It is carrying significant debt because of past investments in water supply assets and the south-east Queensland water grid.
Rail	Queensland Rail	Queensland Rail's declining capital replenishment ratio and recent history of actual capital expenditure less than budgeted spend is a leading indicator of future risks relating to the replacement of its stock of non-current assets, should this trend continue. Spending by the Department of Transport and Main Roads on new generation rolling stock will help offset this declining trend.
Other	Stadiums Queensland	The financial sustainability of Stadiums Queensland depends on it receiving future funding from the government, as it historically receives less income from the services it provides than the cost of providing such services. It is also dependent on the limited market (sporting and entertainment) it operates in and the use of some venues are impacted by the seasonal nature of sports and other organisations which hire them.

Source: Queensland Audit Office

Queensland Treasury Holdings and its subsidiaries have been excluded from our assessment against these three ratios (operating, capital replenishment and debt to revenue) as these entities exist primarily to hold the residual assets from the state's investments and holdings in assets previously leased. The ability of QTH to continue as a going concern is instead influenced by other factors such as the decisions of government as its ultimate shareholder.

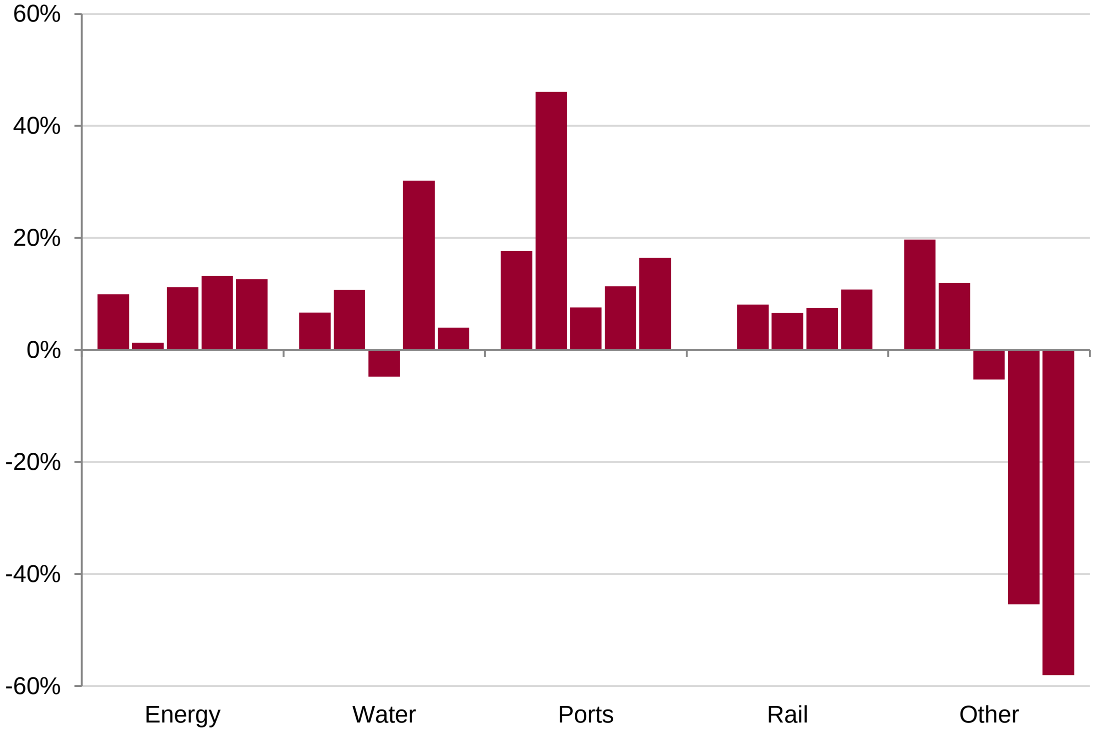
Operating ratio

This ratio is calculated as operating profit after tax, expressed as a proportion of total revenue. It should be positive over the medium to long term for the entity to remain financially sustainable. Ongoing negative ratios indicate net losses, which mean insufficient revenue is being generated to fund operating and future capital expenditure. This leads to the depletion of cash reserves and/or increased borrowings; this may compromise the ability of an entity to invest in new assets and/or maintain its service levels.

Combined PNFCs' profits after tax have averaged 11 per cent of their total operating revenues over the past five years. On average, they have collectively earned one dollar for every nine dollars of revenue generated.

This positive result is a leading indicator that PNFCs are generating sufficient revenues to fund both their operating and future capital expenditure. Figure I provides an overview of the operating ratios achieved by PNFCs in this report across each of the sectors over the last five years.

Figure I
Average operating ratios by sector for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

Energy sector entities, as a whole, averaged positive operating ratios of 10 per cent over the past five years. Average operating ratios achieved by PNFCs within the energy sector were characterised by the higher profitability of the three network businesses (Ergon, Energex and Powerlink) in comparison to the two electricity generators (CS Energy and Stanwell). Stanwell averaged lower levels of profits than the network businesses whilst CS Energy made losses after tax in each of the last five years. CS Energy's ability to pay its ongoing expenses has been partly supported by an equity injection of $300 million in 2011–12.

The operating ratios of water sector entities were influenced by large tax credits inherited by Seqwater when it merged with the former Queensland Bulk Water Transport Authority (QBWTA) on 1 January 2013. Under Australian accounting standards, prior year tax credits can only be brought to account for financial reporting purposes when specific conditions are met, such as an entity's ability to achieve future operating profits. The former QBWTA could not recognise these tax credits as it was unlikely to achieve any future operating profits. As Seqwater was able to satisfy the conditions for recognition of these tax credits under Australian accounting standards, it has progressively recognised QBWTA's large tax credits over the last two years. This resulted in an operating ratio of 4 per cent in 2013–14 (2012-13: 30 per cent).

The profits after tax of all four port corporations averaged around 21 per cent of combined total revenues over the past five years. The operating ratios of port corporations were affected by the long term lease of the Abbot Point coal terminal in 2010–11 for $1.8 billion, reducing revenue previously earned by the terminal, and resulting in a transfer of loans back to the state government.

Queensland Rail's operating ratios averaged 8 per cent over the past four years. Its income and therefore operating ratios depend on the transport services contract (TSC) that it holds with the Department of Transport and Main Roads.

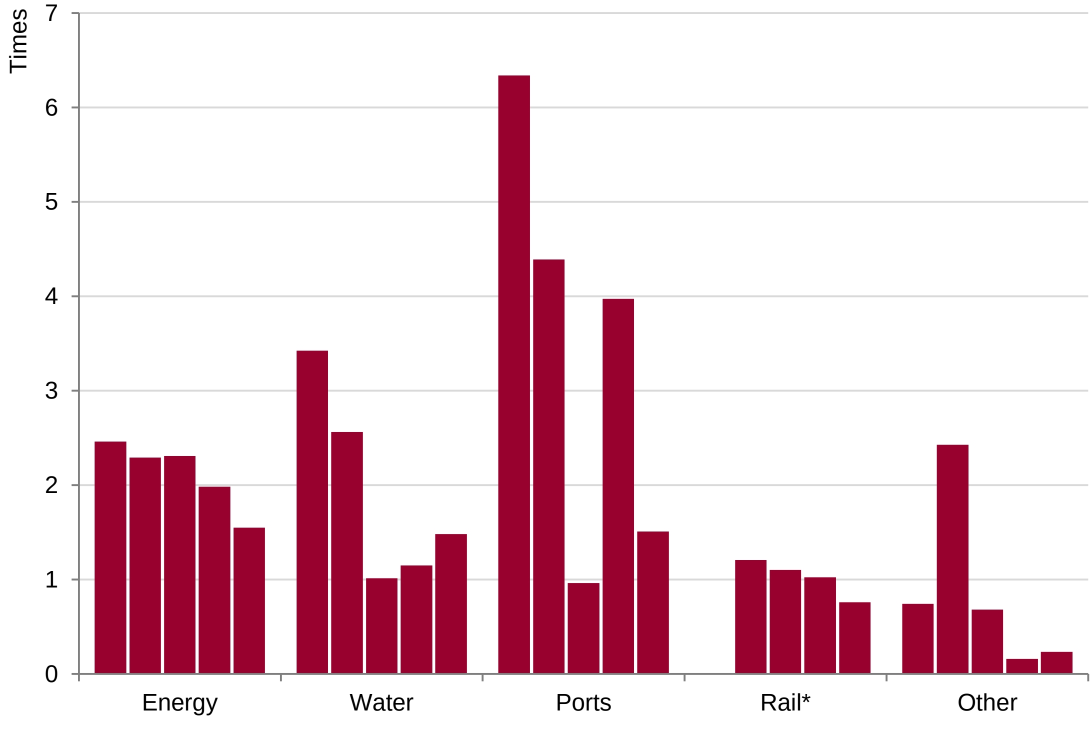
Stadiums Queensland's (other PNFCs) average losses equate to 15 per cent of its total revenues in each of the last five years. Its negative result over the last two years was mainly the result of reduced funding due to the cessation of the Community Investment Funding (CIF) servicing loan repayments, assets gifted to other government bodies and reduced grant funding from the state government. CIF loans were used for the redevelopment of Suncorp Stadium, Stage 6 of the Gabba redevelopment and the construction of the Cbus Super Stadium at Robina. Stadiums Queensland's future operating ratios depend on ongoing government grants as it does not generate sufficient income from the services it provides to pay its ongoing expenses.

Capital replenishment ratios

The capital replenishment ratio compares the annual net investment in non-current asset additions to the annual depreciation charge. An average ratio below one, over time, indicates that assets are being built or replaced below the rate that the non-current asset base is being depreciated.

As shown in Figure J, PNFCs have generally added to or replaced their stock of non-current assets over the past five years at a rate faster than their existing assets were being depreciated. On average, they spent $1.90 on new assets for every dollar of depreciation.

Figure J
Capital replenishment ratios for the five years from 2009–10 to 2013–14



As Queensland Rail Limited recognises its assets at cost, the fair value of its assets were recomputed and used for the purposes of calculating the capital replenishment ratio over the past four years to 30 June 2014.

Source: Queensland Audit Office

From the five groups of PNFCs in this report, only the 'Other PNFCs' recorded an average capital replenishment ratio of less than one over the past five years. As the only entity within the group of 'Other PNFCs' with significant non-current assets, Stadiums Queensland's average capital replenishment ratio over the past five years was 0.8. This is because Stadiums Queensland is not funded annually to replace its infrastructure assets. It is funded annually only to maintain its sporting facilities, and it occasionally receives funding to undertake specific infrastructure redevelopments.

The four PNFCs within the ports sector collectively had the highest capital replenishment ratio of the five sectors. These four entities recorded an average capital replenishment ratio of 3.4 over the past five years. The higher than normal capital replenishment rates were primarily the result of capital expenditure on the Abbot Point Capital Expansion project, Townsville Marine Precinct, Berth 10 upgrade, Berth 8 quayside extension, and the cruise terminal.

The sector with the next highest average capital replenishment ratio was the energy sector, which averaged 2.1 times annual depreciation over the last five years. The energy network businesses of Powerlink, Energex and Ergon have significantly higher capital replenishment rates than the electricity generation businesses of Stanwell and CS Energy, due mainly to their network replacement and augmentation requirements linked to their electricity demand forecasts.

Entities within the water sector had an average capital replenishment ratio of 1.9 over the same period. Some of the reasons for the higher capital replenishment rate were:

- construction work relating to Stage 3 of the Hinze Dam in 2009–10 and 2010–11
- completion of water supply assets on Curtis Island in 2011–12 and 2012–13
- completion of the majority of the works for the Woleebee Creek Pipeline Project in 2013–14.

Queensland Rail had an average capital replenishment ratio of 1.0 over the past four years which has declined from 1.2 to 0.8 during this period. The decline is partly the result of a decrease in scheduled capital spending, and a deliberate move to reduce the need for capital replenishment. Contributing factors, include a decline in labour resources, delays in project decisions and spending, as well as the transfer of management of the new generation rolling stock project to the Department of Transport and Main Roads. The new generation rollingstock project will replenish Queensland Rail's existing rail assets. The consideration of such capital expenditure in the context of the wider rail sector would have a positive impact on the capital replenishment ratio.

Debt to revenue ratios

The debt to revenue ratio compares total loans at a point in time with the total operating revenue generated over the year. This ratio shows the scale of debt compared to turnover, by indicating the extent to which operating revenues (including grants and subsidies) can cover an entity’s loans and other borrowings. Debt for the purposes of this ratio includes only borrowings through the Queensland Treasury Corporation (QTC) and does not include other liabilities such as trade creditors.

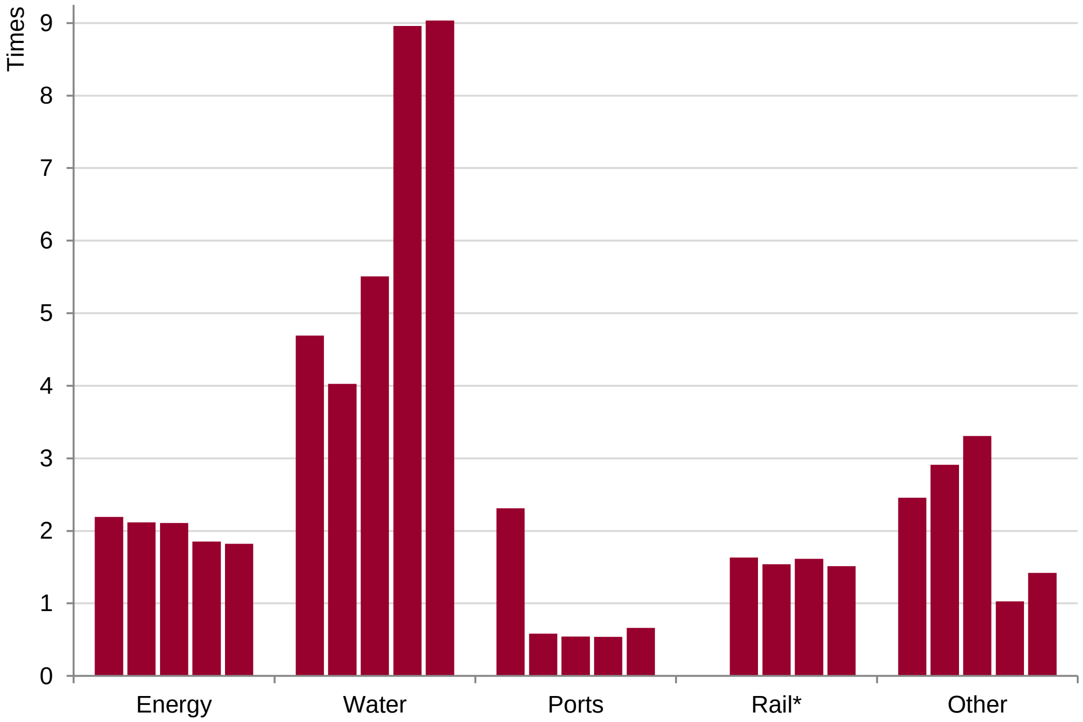
The value of debt held by all PNFCs as at 30 June 2014 was 2.3 times that of combined revenues earned by all PNFCs in 2013–14 as shown in Figure K. Debt to revenue ratios of PNFCs in this report averaged 2.2 at 30 June in each of the last five years. These ratios have proved to be sustainable as demonstrated by the fact that, as a sector, PNFCs have generally been able to fund their ongoing expenditure; and replace and grow their assets without incurring any significant increases in the level of debt they hold as a proportion of revenue they generate.

This means that PNFCs generally have been managing their debt levels effectively over the last five years. The exception being Seqwater, which inherited significant debt when it was combined into a single entity.

Figure K shows that the water sector had the highest average debt to revenue ratio of 6.4 over the last five years. This is largely because of the $9.2 billion of loans held by Seqwater to fund the construction of manufactured water assets, combined with borrowings it incurred because the bulk water prices it charges in south-east Queensland have been and continue to be less than the cost to supply such water. Seqwater's long term sustainability depends on increases in bulk water prices to a point where the price of bulk water catches up with the cost of supplying this water. Other factors such as operational cost reductions will help contain any future price increases.

Stadiums Queensland averaged a debt to revenue ratio of 2.2 over the past five years. The decrease in its debt to revenue ratio in 2012–13 was a result of the transfer of CIF loans of $306.6 million to Queensland Treasury and Trade through contributed equity.

Figure K
Debt to revenue ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

Energy PNFCs held $17.1 billion (56 per cent) of the PNFC total debt of $31 billion at 30 June 2014. Their debt balances have been on average twice that of the total income they generated in each of the last five years.

The energy network businesses of Powerlink, Energex and Ergon Energy hold $15.8 billion of the energy sector's $17.1 billion in borrowings and also have significantly higher debt to revenue ratios than the electricity generators of Stanwell and CS Energy. Notwithstanding this, the capital structures of the network businesses contain debt below the Australian Energy Regulator's benchmark debt levels, which is approximately 60 per cent of their regulated asset base.

Rail has averaged the second lowest debt to revenue ratio of the five PNFC groups in this report over the last four years. Total debt held by Queensland Rail averaged 1.6 times revenue earned over each of the past four years. Its total borrowings have remained relatively constant since it inherited $3 billion of debt on establishment in 2010–11. Queensland Rail has generated sufficient revenue to fund its expenses and has therefore not needed to borrow additional funds.

Port corporations averaged the lowest debt to revenue ratios of the five PNFC groups within this report. The total combined debt to revenue ratio of all four port corporations averaged 0.7 over the past five years. Combined debt of all four port corporations decreased to 0.6 times revenue generated in 2010–11 which, as for the operating ratio, was partly due to the long term lease of the Abbot Point coal terminal in 2010–11 which led to the subsequent transfer of related loans by North Queensland Bulk Ports Corporation Limited back to the state government that year.

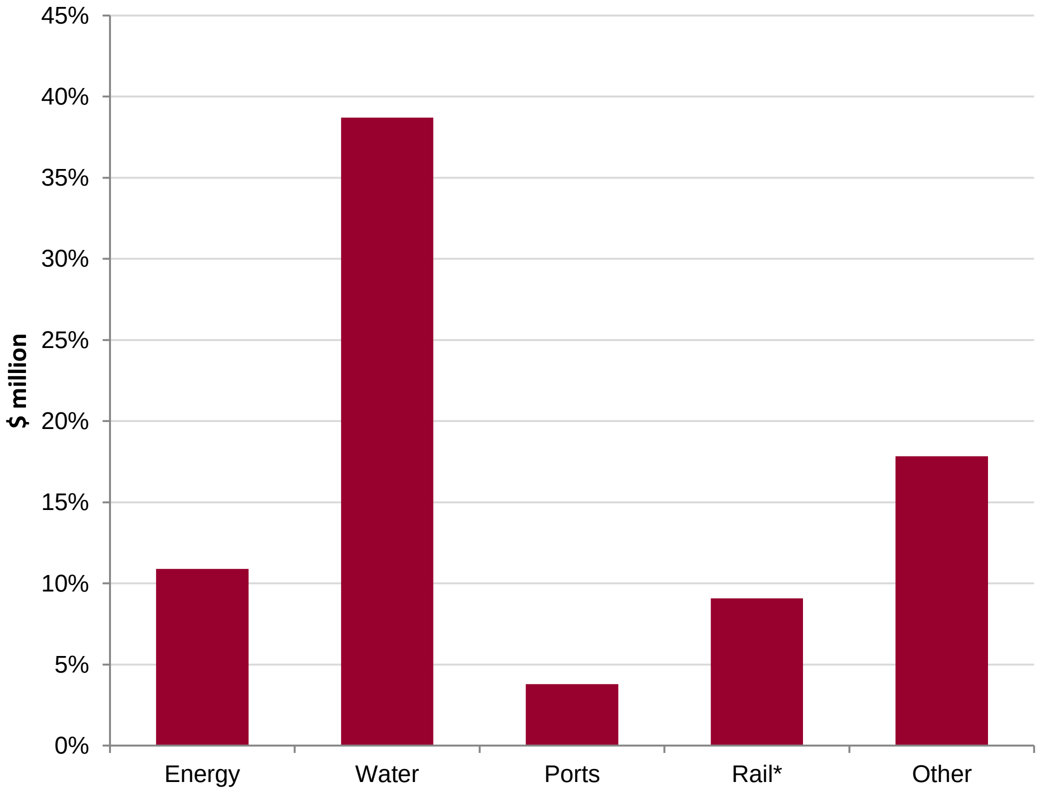
Interest 'bite'

A supplementary measure of debt sustainability relates to an entity's ability to service its debt obligations–to pay interest and to repay or refinance loans when they fall due. The interest expense ratio, 'interest bite' considers how much operating revenue is required to pay interest charges.

PNFCs recorded total interest expense on their borrowings of $1.7 billion in 2013–14 ($6.9 billion in the five years to 30 June 2014).

Total interest expense has averaged 12 per cent of revenues earned over the past five years; however, between the sectors, interest expense as a percentage of revenue varied significantly as shown in Figure L.

Figure L
Interest expense ratio over the past five years



Source: Queensland Audit Office

Interest expense of $1.68 billion averaged 39 per cent of total revenue earned by water sector entities over the past five years. This was primarily due to large borrowings held by Seqwater, which accounted for $9.2 billion of the $9.7 billion of borrowings held by PNFCs in the water sector at 30 June 2014. This would not be a sustainable position for a fully commercial entity.

Net cost of the PNFC sector to government

Flows to and from the government affect the ability of PNFCs to meet their expenditure commitments; replace and grow their asset bases; and repay debts.

PNFCs are required to pay dividends, income tax and competitive neutrality fees (CNFs) to the government; and receive community service obligation (CSO) payments, grants and net equity contributions from government for selected activities.

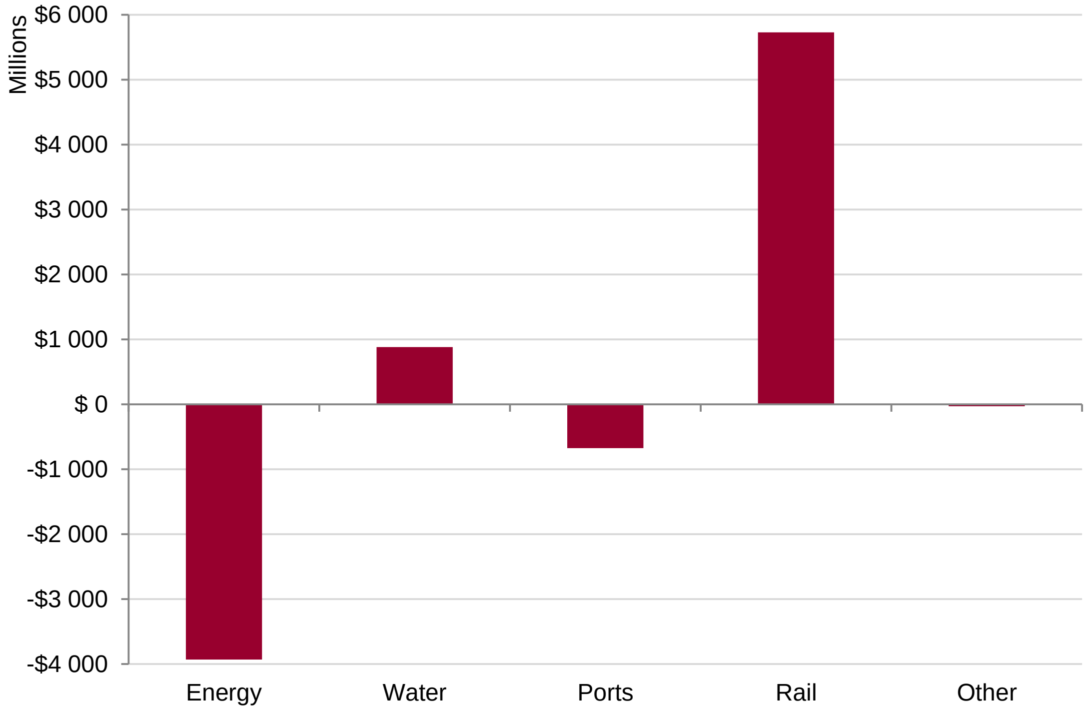
Over the last five years, $2.2 billion flowed from the government to PNFCs in net terms. Much of this is due to Seqwater's tax losses and funding provided to Queensland Rail.

PNFCs in the energy sector returned $3.9 billion of net flows to the government; entities within the ports sector returned $575.1 million of net flows over the same period.

In contrast, water sector entities received net flows from the government of $912.2 million due in part to significant tax losses recognised by Seqwater in the last two years. The rail sector also received $5.8 billion in net flows from the government over the past four years because Queensland Rail receives the majority of its ticketing and other revenue through government and not directly from the public. Queensland Rail also receives revenue to fund the development and maintenance of the rail network in Queensland.

Figure M shows combined flows from and (to) the government over the past five years.

Figure M
Net flows from and (to) government over the past five years



Source: Queensland Audit Office

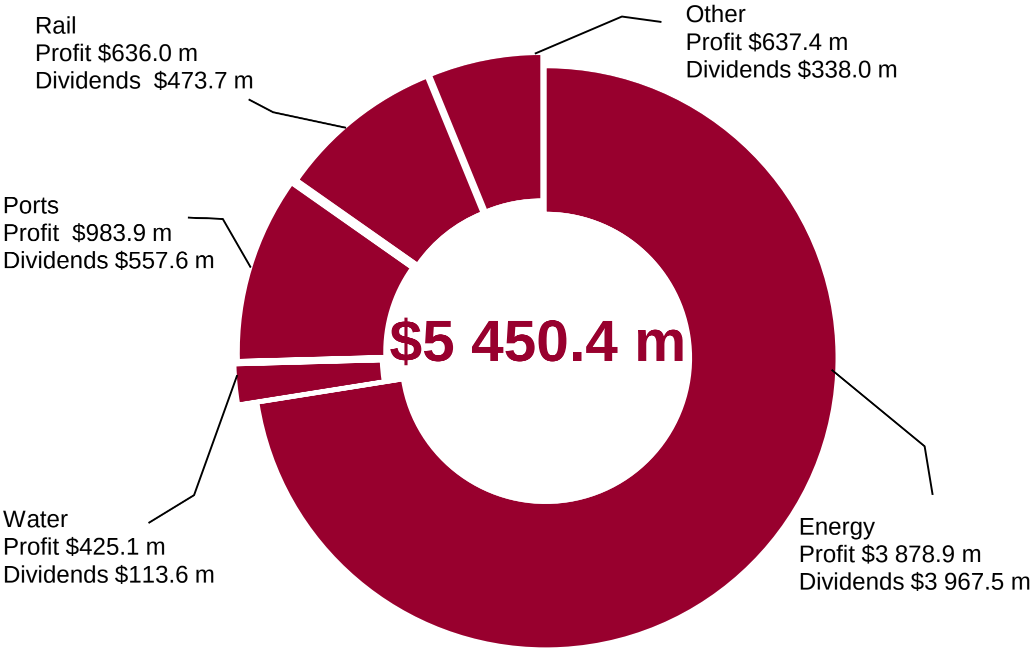
Outflows to the government

Dividends

Over the past five years, dividends declared by PNFCs to the government totalled $5.45 billion. Energy entities' combined dividends were $3.97 billion, and the four port corporations declared $557.6 million in dividends. The PNFCs in these two sectors contributed to 83 per cent of all dividends declared by PNFCs.

Figure N shows a breakdown of dividends declared by PNFCs within each sector over the last five years.

Figure N
Dividends declared by PNFCs over the past five years by sector



Source: Queensland Audit Office

Competitive neutrality fees

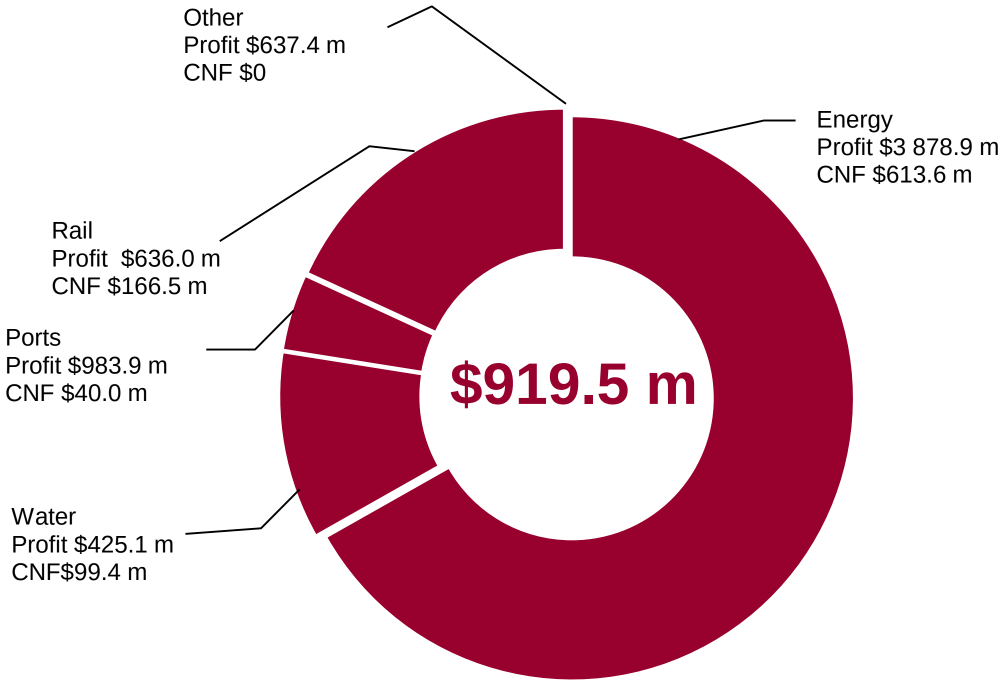
Competitive neutrality fees (CNFs) are designed to compensate for the net competitive advantage that government businesses enjoy over their competitors as a result of public sector ownership.

CNFs of $919.5 million were paid by PNFCs to government over the past five years. Energy PNFCs and Queensland Rail were the largest contributors of CNFs over the past five years, with energy entities contributing $613.6 million and Queensland Rail contributing $166.5 million over this period.

Queensland Rail pays CNFs because of its position as a monopoly provider of rail infrastructure and related services. Energy PNFCs pay CNFs to government because they borrow money at a rate that is lower than their private sector counterparts.

Figure O breaks up the CNFs recognised by PNFCs in each industry over the past five years.

Figure O
CNFs paid by PNFCs over the past five years by industry



Source: Queensland Audit Office

Tax equivalent payments

Section 24AM of the *Income Tax Assessment Act 1936* (ITAA 1936) states that income of a state body is exempt from income tax unless it is an excluded state body. Section 24AV(1) of the ITAA 1936 then enables state government jurisdictions to decide on its list of excluded state bodies.

In Queensland, certain government owned corporations and for-profit statutory bodies are subject to the national tax equivalents regime and must remit income tax to the state government instead of the Commonwealth government.

The net income tax recognised by PNFCs over the past five years was $1.45 billion. Net income tax recognised is calculated as the sum of income tax expense less any income tax credits that PNFCs may be eligible to.

The largest contributors of income tax were PNFCs in the energy industry, which recognised $1.59 billion of income tax over the past five years. This amount was offset by income tax credits of $867.9 million that were brought to account by Seqwater over the past two years. This means that Seqwater will not need to pay income tax for at least the next $2.9 billion in future profits, assuming that no further operating losses are made.

Inflows from the government

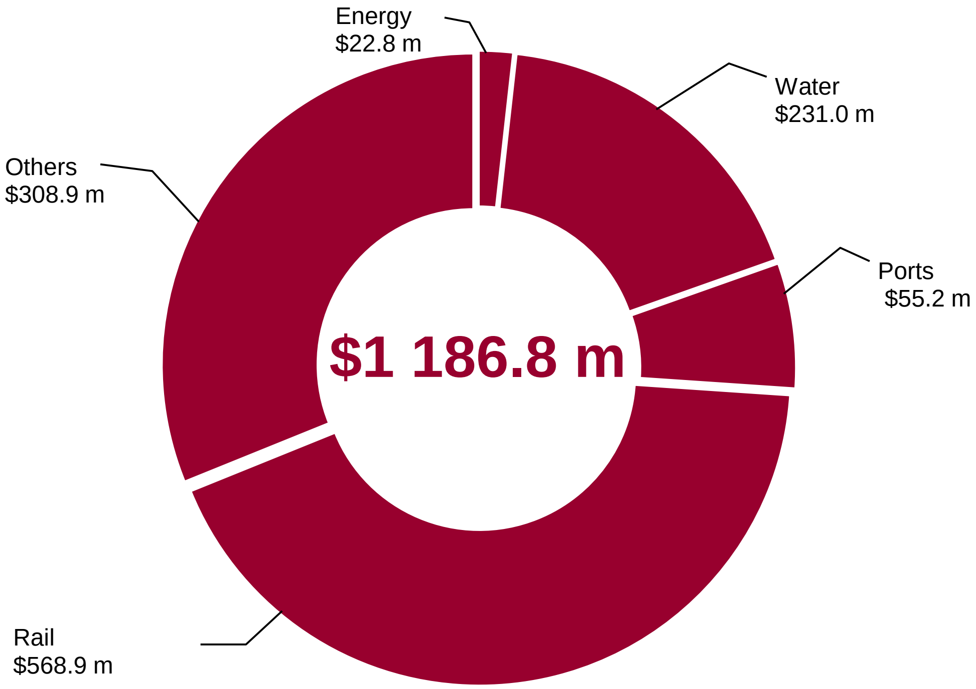
Net cash equity contributions to PNFC

Net cash equity contributions of $1.2 billion were paid to PNFCs over the five years. Net equity contributions are capital cash injections by government less any return of equity by those entities back to government.

The largest recipients of net cash equity contributions were Rail and Other PNFC entities which received $877.8 million in net equity contributions over the past five years. Of this, $568.9 million was injected into Queensland Rail Limited in 2010–11 and 2011–12 for the construction of rail projects in south-east Queensland. A further $306.6 million was injected into Stadiums Queensland effective 30 June 2013 in exchange for its CIF loans.

Figure P summarises the net equity contributions made to PNFCs by sector over the past five years.

Figure P
Net equity contributions made to PNFCs over the past five years by industry



Source: Queensland Audit Office

Community service obligations and other government funding

Community service obligations (CSOs) are monies received from government to fund non-commercial activities or services provided to the community at non-commercial prices. Government typically reimburses such entities for the revenue they would otherwise have earned had such services and activities being provided on commercial terms.

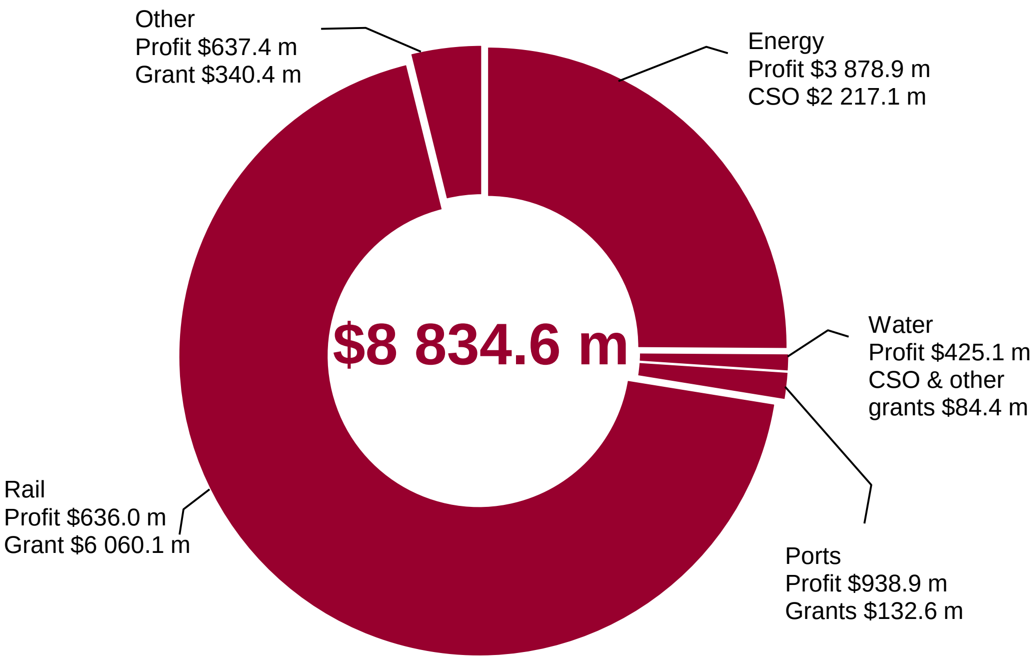
Queensland Rail and Stadiums Queensland also receive significant government funding as part of their normal business operations. To a lesser extent; all four Port Corporations also receive government funding from time to time. None of these three groups of entities disclosed CSOs within their financial reports.

CSOs received by PNFCs, and other funding (received by the four Port Corporations, Queensland Rail and Stadiums Queensland) totalled $8.8 billion in the five years to 30 June 2014. PNFCs within the energy industry and Queensland Rail received 94 per cent of this funding. CSOs paid to the energy sector were mainly made to Ergon Energy Queensland Pty Ltd as it was required to provide some regional customers with electricity at prices that were less than the cost of providing such services.

Government funding of $6.1 billion was provided to Queensland Rail over the past four years under arrangements within its transport services contract (TSC) with the Department of Transport and Main Roads.

Figure Q provides a breakdown of CSOs and other government funding received by PNFCs in this report.

Figure Q
CSOs and other government funds received by PNFCs over the past five years



Source: Queensland Audit Office

1 Context

1.1 Scope of report

The public non-financial corporation (PNFC) sector comprises bodies that provide non-regulatory, non-financial market goods and services. Sales to consumers finance PNFCs, while government subsidises community service obligations. PNFCs are legally distinct from the governments that own them.

Queensland Treasury and Trade determines the entities included in the PNFC sector.

This report does not include the results of PNFC entities which ceased to exist before 1 July 2013.

Entities in this report have different functions and regulatory requirements within the PNFC sector and the industries in which they operate. This limits the comparability of their financial performance and financial position.

Some accounting standards allow entities to choose between accounting treatments. The accounting policies entities choose may measure or report transactions and balances differently.

This report excludes the results of our audits of Queensland local governments, universities, grammar schools, Hospital and Health Services, general government sector entities, public financial corporations and the Queensland state government financial report, all of which we report separately to Parliament.

Our report on state public sector entities contains the results of our audits of the financial reports of 370 departments, statutory bodies and government owned corporations with a 30 June 2014 balance date. It also includes results of the audits of a further 116 entities which are not public sector entities.

1.2 Legislative framework

The Auditor-General of Queensland, supported by the Queensland Audit Office, provides Parliament with independent assurance on the financial statements of public sector entities to ensure public sector accountability. Our financial audits to form our audit opinions and our reports to Parliament on the results of our financial audits deliver this assurance.

This report to Parliament relates to the result of financial audits of 2013–14 public sector financial statements—specifically, state statutory bodies and government owned corporations within the PNFC sector and the entities that they control.

These public sector entities prepare their financial statements and annual reports under:

- the Financial and Performance Management Standard 2009—statutory bodies
- Government Owned Corporation Regulation 2004 (GOC Regulation)—government owned corporations
- *Corporations Act 2001* (Cth)—controlled entities that are public companies.

1.3 Legislated deadlines

The Financial and Performance Management Standard 2009 requires statutory bodies to have their financial statements finalised and audited no later than two months after the end of the financial year to which the statements relate; that is, by 31 August 2014. This is also the deadline for government owned corporations, as required by the GOC Regulation.

The appropriate Minister must table annual reports of statutory bodies in Parliament no later than three months after the end of the financial year. The Minister may extend the tabling period for the annual report by notice given to the department or the statutory body.

The *Corporations Act 2001* requires most controlled entities of statutory bodies and government owned corporations to issue their annual reports no later than four months after the end of the financial year.

Queensland Treasury and Trade requires annual reports of controlled entities of statutory bodies to be tabled in Parliament.

1.4 Audit responsibilities

Section 40 of the *Auditor-General Act 2009* requires the Auditor-General to audit the annual financial reports of all public non-financial corporation entities and to prepare an auditor's report. The auditor's report, which includes the audit opinion, provides assurance about the reliability of the financial reports, including compliance with legislative requirements.

The Auditor-General also performs other engagements over information not included in annual financial reports. For the purposes of this report, these other engagements include:

- audit of historical actual financial information
- review of historical estimated financial information
- review of historical non-financial information.

A combination of audit opinions and conclusions are issued for other information engagements. Audit opinions are issued over actual historical financial information based on an evaluation of the work performed by the auditor. A conclusion provides the reader with less assurance; and indicates whether anything has come to the attention of the auditor which users of the information should be made aware. The different types of audit opinions and review conclusions issued for annual financial reports and other information engagements are listed in Figure 1A.

Figure 1A
Types of audit opinions and conclusions issued

Type of information	Report issued	Auditing standard	Basis of opinion or conclusion
Annual financial report	Audit	Auditing Standard ASA 700—Forming an Opinion and Reporting on a Financial Report	Whether the report is prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework.
Other historical actual financial information	Audit	ASA 805 Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement	Whether information is presented fairly in accordance with requirements and the entity's basis of preparation.
Other historical estimated financial information	Review	ASRE 2405 Review of Historical Financial Information Other than a Financial Report	Whether or not anything has come to the auditor's attention that causes it to believe that the estimated financial information is not, in all material respects, presented fairly in accordance with the requirements and the entity's basis of preparation.
Non-financial actual and estimated information	Review	ASAE 3000 Assurance engagements other than audits or reviews of historical financial information	Whether or not anything has come to the auditor's attention that causes it to believe that the historical non-financial information is not, in all material respects, presented fairly in accordance with the requirements and the entity's basis of preparation.

Source: Queensland Audit Office

When issuing an audit opinion, we may report one or more of the audit opinion types outlined in Figure 1B.

Figure 1B
Audit opinions

Opinion	Description
Unqualified	We issue an unqualified opinion where the financial reports comply with relevant accounting standards and prescribed requirements.
Qualification	We issue a qualified opinion when the financial reports as a whole comply with relevant accounting standards and legislative requirements, but with particular exceptions.
Adverse	We issue an adverse opinion when the financial reports as a whole do not comply with relevant accounting standards and legislative requirements.
Disclaimer	We issue a disclaimer of opinion when we are unable to express an opinion as to whether the financial reports comply with relevant accounting standards and legislative requirements.

Source: Queensland Audit Office

We may include an *emphasis of matter* paragraph with an audit opinion to highlight an issue of which we believe the users need to be aware of. These paragraphs can also be included in review reports. The inclusion of an emphasis of matter paragraph does not modify the opinion or conclusion made.

For annual financial reports, after we issue the audit opinion, we are required under the *Auditor-General Act 2009* to provide a copy of the certified statements and the auditor's report to the Chief Executive Officer of the entity and the appropriate Minister. For other engagements, certified information is provided direct to the Chief Executive Officer.

The Act also requires the Auditor-General to prepare a report to Parliament on each audit. The report must state if the audit has been completed and the financial reports audited. It must also include details of significant deficiencies where financial management functions were not performed adequately or properly and any actions taken to improve deficiencies reported in previous reports.

1.5 Other reporting requirements

In addition to 30 June financial reports and whole of government reporting, energy generators and Ergon Energy submit financial reports to the Australian Securities and Investments Commission (ASIC) as part of maintaining their Australian financial services licences.

1.6 Reference to comments

In accordance with s.64 of the *Auditor-General Act 2009*, we provided sections of this report to relevant entities.

We provided sections of this report to the Minister for Energy and Water Supply; the Minister for Transport and Main Roads, the Minister for National Parks, Recreation, Sports and Racing, the Director-General, Department of Energy and Water Supply; the Director-General, Department of Transport and Main Roads; the Director-General, Department of National Parks, Recreation, Sports and Racing; and the Under Treasurer, Queensland Treasury and Trade for comment.

We provided copies of the report to the Premier, the Treasurer and Minister for Trade and the Director-General, Department of the Premier and Cabinet for information.

We have considered all comments received within 21 days and incorporated these in this report to the extent warranted. Comments received or a fair summary are included at Appendix A.

1.7 Report structure and cost

The report is structured as followed:

- Chapters 2 to 6 discuss the results of the each sector's audits for the reporting entities across energy (chapter 2), water (chapter 3), ports (chapter 4), rail (chapter 5) and other PNFCs (chapter 6), including the timeliness and quality of their draft financial reports, significant reporting issues and other matters we identified. We also analyse the financial performance and position of the major entities within each sector over the last five years, trends and issues affecting their financial sustainability and their position to meet their future financial obligations.
- Appendix A contains responses received.
- Appendix B describes the ratios we used to assess financial sustainability.
- Appendix C lists sector entities for which audit opinions will not be issued in 2013–14.
- Appendix D details revised AER guidelines and regulatory reporting requirements for energy GOCs, together with engagements we undertook during 2013–14.
- Appendix E summarises the price of bulk water compared to bulk water charges.

The cost of preparing this report was $220 000.

2 Energy sector

In brief

Background

In Queensland, a combination of government owned and privately owned generators contribute to the east coast national electricity grid.

The main suppliers are Stanwell Corporation Limited and CS Energy Limited. Queensland Electricity Transmission Corporation (trading as Powerlink) transports electricity at high voltage between generators and distributors who connect to businesses and households. In south-east Queensland, Energex Limited operates the distribution network.

Outside south-east Queensland, Ergon Energy Corporation Limited (EECL) operates the distribution network. The main interfaces between distributors and customers are retailers. In Queensland, all retailers are privately owned except for Ergon Energy Queensland Pty Ltd, a subsidiary of EECL which provides retail services outside south-east Queensland.

This chapter details the results of our audits and reviews of energy sector government owned corporations (GOCs) and the entities they control.

Conclusions

The financial reports of all energy GOCs and controlled entities were timely and of good quality. The low numbers of adjustments and disclosure changes management and audit identified between the first and final audited version of the financial reports reflect good financial reporting processes.

We assessed the financial sustainability of these entities in their ability to continue to operate as a going concern. Overall these entities are financially sustainable, except for CS Energy. Onerous contract with third parties, future demand, electricity pricing and coal supply issues to the Callide power station affect CS Energy's ability to meet its future expenditure and capital commitments.

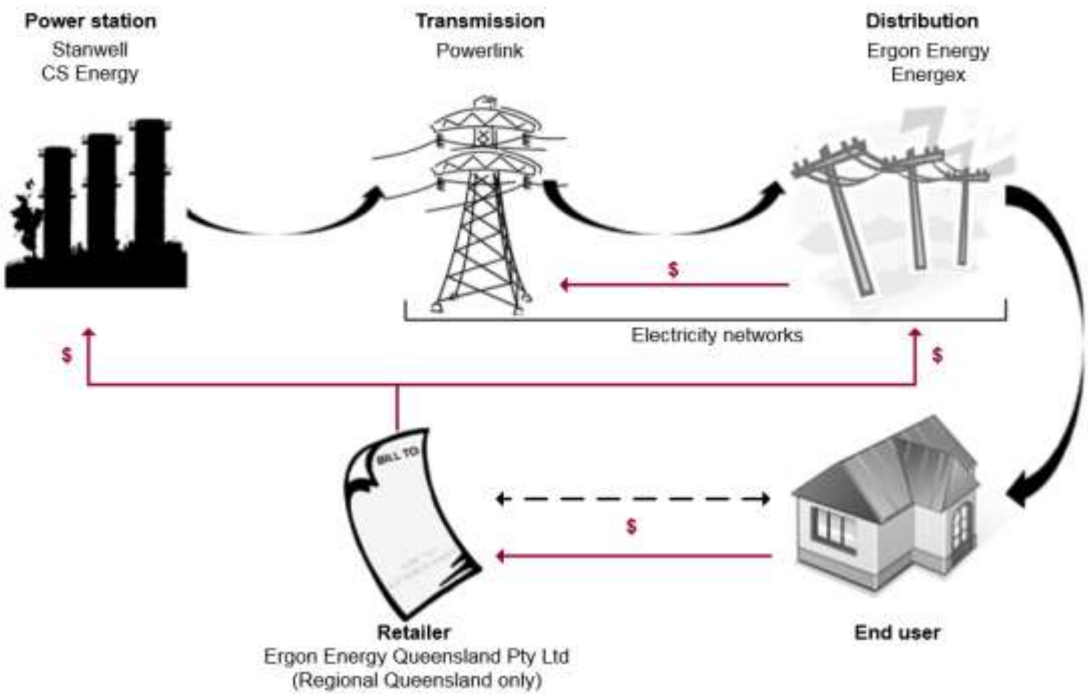
Key findings

- We completed all audits of financial reports within legislative deadlines. Three of eight entities did not provide their draft financial report for audit by agreed deadlines.
- We certified without qualification the audit and review of 12 regulatory information notices issued by the Australian Energy Regulator (AER) for Energex and Ergon.
- Hard close and 'shell' financial report processes continue to smooth year-end processes. No material changes were made to draft financial reports.
- Generators need to consider the eventual use of liquefied natural gas (LNG) and its impact on the Queensland electricity market, changes to renewable energy targets, and the implementation of any new environmental/carbon measurements in valuation of property, plant and equipment for generators in 2014–15.
- Network entities collectively held $1.48 billion in receivables as under recovery of revenues at 30 June 2014. Time frames for recovery are subject to AER's annual pricing approval process.
- Operating ratios are marginally above zero, except for CS Energy which continued to be in a negative position. This generator continues to record losses but forecasts a return to profitability in 2015–16. Its recognition as a going concern depends on continued access to undrawn debt facilities and ongoing government support.
- Capital replenishment ratios indicate assets are being built or refurbished faster than they are depreciating, but industry factors continue to affect decreasing capital investment significantly. Investment is primarily funded through debt.
- Debt sustainability ratios indicate that GOCs are continuing to meet their debt obligations.

2.1 Background

In Queensland, five government owned corporations (GOCs) are involved in generating, transmitting and distributing electricity. Figure 2A shows these five GOCs and how payments for electricity flow through the supply chain.

Figure 2A
Queensland electricity GOCS and payment flow through the supply chain



Source: Queensland Audit Office

By nature, the generator and network businesses have different revenue streams. Market forces drive generator revenue streams, while the Australian Energy Regulator (AER) determines network revenue in five-year periods. Thus, revenue streams are more predictable for network businesses.

Across the state, a combination of government owned electricity generators and privately owned electricity generators contribute to the east coast national electricity market (NEM). The main generators are the state-owned Stanwell Corporation Limited (Stanwell) and CS Energy Limited (CS Energy).

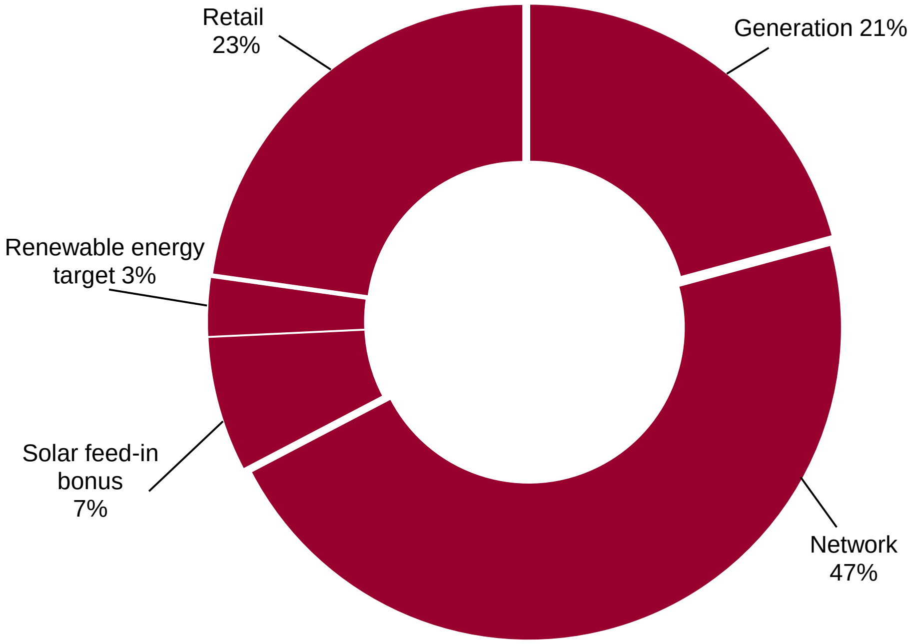
Once electricity has been generated and sold in the NEM, Queensland Electricity Transmission Corporation Limited (trading as Powerlink) transfers power around Queensland at high voltage between the generators and the lower voltage networks of Energex Limited (Energex) and Ergon Energy Corporation Limited (Ergon Energy) and some direct connect high voltage customers. For the purposes of this report, Powerlink, Energex and Ergon Energy are referred to as network businesses. These three state-owned entities do not have any competition from private sector operators in providing network services.

The main interface between the electricity industry and their customers, such as households and businesses, are the energy retailers. In Queensland, these retailers are privately owned, except for Ergon Energy Queensland Pty Ltd which services regional Queensland.

2.1.1 Electricity pricing

Energy bills include the wholesale cost of buying gas and electricity and transportation costs to deliver energy to customers and to provide retail services. Bills also include the cost of programs to save energy or support the development of renewable energy. Figure 2B shows the expected break up of costs for the average residential electricity bill, after the Australian Government repeals carbon pricing legislation from 1 July 2014.

Figure 2B
Break up of residential electricity bills post carbon repeal



Source: Queensland Competition Authority— fact sheet electricity prices from 1 July 2014 updated 24 July 2014.

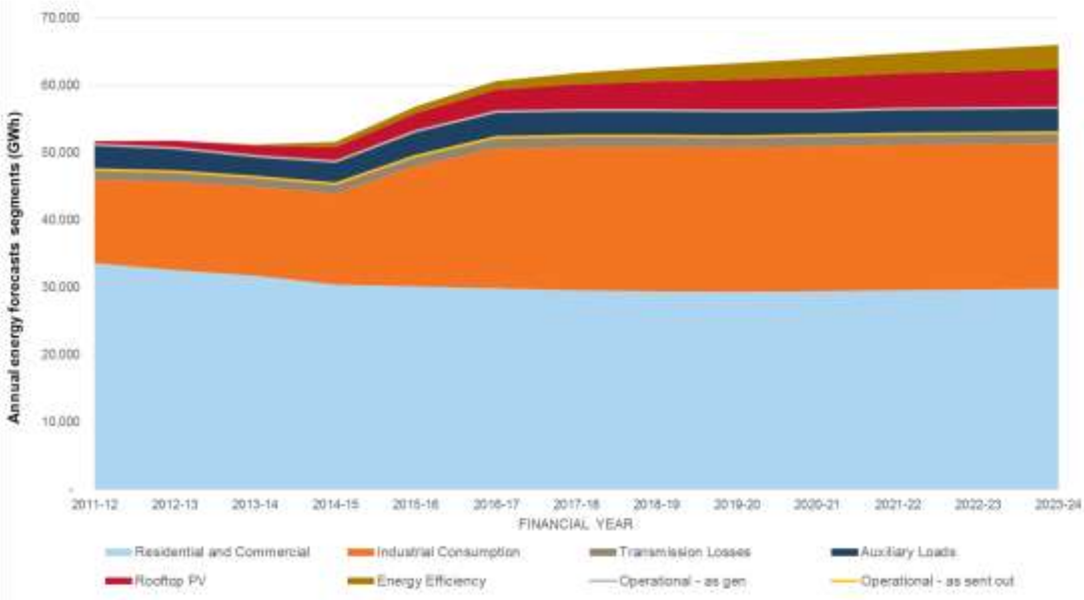
With the removal of carbon pricing, the generation cost component of the bill is similar to 2012–13. Network cost is now seven per cent lower than in 2012–13 and the retail cost component is relatively steady, compared to 2013–14. The Queensland Competition Authority estimates solar and renewable energy green costs will increase from 5 per cent in 2012–13 to 10 per cent in 2014–15. Increases reflect the historical take up of the solar bonus scheme and recovery of the scheme's cost from customers through retail charges.

To manage costs, some large customers opt to participate directly in the NEM wholesale market and manage their own contracts with the generators and network service providers. All other customers go through electricity retailers to supply their homes and businesses under either a market contract or a standard contract. Under a market contract, the retailer and customer negotiate prices and bonuses, like discounts. Under a standard contract, the Queensland Competition Authority (QCA) determines the prices that retailers charge, which are known as ‘regulated’ or ‘notified’ prices. The Minister for Energy and Water Supply delegates the power to set regulated electricity prices to the QCA.

2.1.2 Electricity demand

The Australian Energy Market Operator (AEMO) *National electricity forecasting report for the national energy market* (issued June 2014, updated August 2014) and Powerlink *Energy and Demand Forecast* report (issued February 2014) both anticipate significant reductions in annual energy consumption, compared to previous forecasts. Figure 2C shows the June 2014 AEMO annual energy forecasts for Queensland by segment.

Figure 2C
AEMO annual energy Queensland forecast outlook to 2023–24



Source: AEMO National electricity forecasting report for the national electricity market June 2014

The AEMO reported the short term annual energy forecast (to 2016–17) for Queensland is an average annual increase of 4.1 per cent. This is driven by a 16.4 per cent increase in large industrial consumption and a 2.0 per cent decrease in residential and commercial consumption.

Queensland's increased consumption reflects liquefied natural gas (LNG) projects coming online from 2014–15. Excluding LNG, large industrial is forecast to decline.

A decrease in residential and commercial electricity consumption is expected to offset the increase in industrial consumption. Increasing electricity prices, due to the solar bonus cost recovery scheme and the strongest growth in rooftop photovoltaic (PV) installations in the NEM by Queensland are driving the decrease in residential and commercial consumption. More PV energy generated requires less energy from the grid.

Historically the decline was primarily driven by sustained electricity price increases over the past five years, largely due to transmission and distribution network costs, and growth in rooftop PV and energy efficiency. In Queensland, federal energy saving programs drive total energy efficiency savings attributed to appliances, buildings, and industry. Increases in energy efficiency savings reduce the amount of operational electricity required from the grid, but network infrastructure still needs to be maintained to cater for peak demand.

2.1.3 Regulatory reform

A number of market and industry reviews could affect the GOCs' future revenues and market arrangements. The reviews at the national and state levels include:

- Queensland electricity sector review completed with 30-year electricity sector plan (PowerQ) released June 2014
- National Energy Customer Framework implementation deferral to July 2015
- review of enforcement regimes
- national approach to reliability standards
- Australian Energy Market Commission (AEMC) ongoing update of rules
- AER guidelines
- Senate inquiry into electricity network, prompted by gold plating allegations.

National level

Budget cuts, moves to do more with less and rationalisation of capital spending are affecting the way the industry does business. The Australian Government is considering substantial reform to the renewable energy target (RET) scheme.

In 2013–14, the AEMC and the AER issued draft reports for reliability standards and reliability settings to apply from 1 July 2016. AER also revised guidelines and increased regulatory reporting, as outlined in Appendix D of this report. Compliance with new regulatory requirements within tight implementation timeframes is a main concern for network GOCs.

The current focus for distributors is the 2015–20 revenue determination process. Effects on revenue will significantly influence the way these entities do business in coming years.

State level

On 20 May 2014, the Minister for Energy and Water Supply introduced:

- the Electricity Competition and Protection Legislation Amendment Bill 2014, which aims to remove retail price regulation in south-east Queensland and establish an effective market monitoring regime
- the National Energy Retail Law (Queensland) Bill 2014, which aims to complement the price reforms by strengthening consumer protections around the sale and supply of energy (electricity and natural gas) to consumers.

The Bills received assent on 26 September 2014. Consistent with actions outlined in *PowerQ: a 30-Year Electricity Strategy*, the new arrangements are expected to begin on 1 July 2015.

On 28 May 2014, the *Electricity and Other Legislation Amendment Act 2014* received assent. The Act:

- removes mandated feed-in arrangements for small customers in south-east Queensland when the eight cent a kilowatt hour feed-in tariff expired on 30 June 2014, enabling competition in the retail electricity market to determine the feed-in tariff rates available to small customers
- provides for the recovery of Queensland's portion of the cost of funding the AEMC by imposing a levy on electricity transmission and gas pipeline licence holders regulated under national energy laws.

The Queensland Government is considering options to improve the structure of regional subsidy arrangements, in parallel with reforms to Ergon Energy's retail business.

2.1.4 Changes to PNFCs in the public sector

On 7 October 2014, the state government released its *Final Plan: The Strongest & Smartest Choice —Queensland's Plan For Secure Finances And A Strong Economy* (the Final Plan), which details its plans for state assets after the 2015 state election. The plan proposes to offer for lease all energy sector assets.

Further details and the terms of proposed arrangements are not known at the time of preparing this report.

2.1.5 Entities covered in this chapter

The Queensland energy sector comprises five GOCs; one jointly controlled entity established to provide information and communications technology services to the electricity distributors; and 31 controlled entities. Due to reasons listed in Appendix C, only eight of these entities prepare financial reports.

The sector also includes seven joint venture interests and a foreign based entity, all audited by private sector firms.

All entities have a 30 June balance date.

This report does not include the results of other energy sector PNFCs which ceased to exist before 1 July 2013. Assets and business units previously held by Tarong Energy Corporation Limited before 1 July 2011 are not included in data for 2009–10 and 2010–11.

2.2 Conclusions

We certified unqualified audit opinions of all energy PNFCs included in this report. Readers can rely on the results in the audited financial reports of these entities.

The audits were completed within legislative deadlines and we received good quality draft financial reports as part of this process.

When forming an audit opinion on the financial report of an entity, we assess an entity's ability to operate as a going concern. We also assess the entity's financial performance, position and sustainability.

In 2013–14, network GOCs—Powerlink, Energex and Ergon—continue to dominate the supply chain, representing $28.52 billion (74 per cent) of revenue over five years. Networks supplied $3.67 billion (93 per cent) of dividends over the same period, held $29.06 billion (88 per cent) of property, plant and equipment and comprised $15.76 billion (92 per cent) of borrowings at 30 June 2014.

We assess an entity's financial sustainability in its ability to pay its ongoing expenses, replace and grow its assets and pay its debts as and when they fall due.

CS Energy's operating ratio continues to track below zero. Its future sustainability continues to depend on ongoing access to undrawn debt facilities with Queensland Treasury Corporation (QTC) and continued state government support. CS Energy's ability to meet its future expenditure and capital commitments is affected by:

- onerous contract in place with third parties which affect CS Energy's financial performance negatively
- future demand and electricity pricing
- coal supply issues to the Callide power station.

All other entities achieved financial results which indicate that they are sustainable.

2.3 Audit opinions and conclusions

Financial reports

Figure 2D summarises financial report results for energy sector audits during 2013–14.

Figure 2D
2013–14 financial report audit opinions issued

Audit	First draft financial report provided for audit	Financial reports signed	Opinion issued	Certified by deadline	Opinion
Government owned corporations and controlled entities					
Stanwell Corporation Limited	25.07.2014	26.08.2014	26.08.2014	Yes	Unqualified
CS Energy Limited	04.08.2014	28.08.2014	29.08.2014	Yes	Unqualified
Queensland Electricity Transmission Corporation Limited (Powerlink)	08.08.2014	22.08.2014	25.08.2014	Yes	Unqualified
Energex Limited	25.07.2014	25.08.2014	26.08.2014	Yes	Unqualified
Ergon Energy Corporation Limited	11.08.2014	29.08.2014	29.08.2014	Yes	Unqualified
Ergon Energy Queensland Pty Ltd	05.08.2014	29.08.2014	29.08.2014	Yes	Unqualified
Ergon Energy Telecommunications Pty Ltd	23.07.2014	29.08.2014	29.08.2014	Yes	Unqualified
Jointly controlled entities					
SPARQ Solutions Pty Ltd	17.07.2014	12.08.2014	14.08.2014	Yes	Unqualified

Source: Queensland Audit Office

We issued unqualified audit opinions for all five GOCs and the three reporting entities they control. This is consistent with 2012–13 and confirms financial reports have been prepared according to requirements of legislation and relevant accounting standards.

Regulatory information notices

Energex and Ergon engaged us in 2013–14 for regulatory work outlined in Appendix D.

This was because, for the first time, the AER requested information for the economic benchmarking, category analysis and revenue reset engagements. Not all information was readily available or recorded in the specified format. Where actual historic data could not be obtained from entity information systems, the data requested was estimated.

Across 12 engagements, 12 audit opinions and 12 conclusions were issued. Emphasis of matters were included in all opinions and conclusions to highlight the basis of preparation. This was key to understanding the assumptions we used to calculate the regulatory information notice (RIN) data. The emphasis of matter also highlighted the reports were only prepared to fulfil the entity's reporting responsibilities in accordance with the RIN. The information is not intended for other uses.

Australian financial service licences

Stanwell, CS Energy and Ergon Energy Queensland hold Australian financial service licences to trade financial products. ASIC issues and regulates licences under the requirements of the *Corporations Act 2001* (Cth).

We completed and certified all Australian financial service licences for 2012–13 and 2013-14, in conjunction with the engagements and without noting any issues.

2.4 Timeliness and quality of financial reports

Each entity should establish financial management systems that identify and manage financial risks, including risks to reliable and timely reporting. Entities must review the performance of financial management systems regularly.

Effective financial systems can produce timely and reliable financial information for management, directors and users of electricity services. An efficient system will integrate internal management reporting with external accountability reporting.

2.4.1 Timeliness

To show accountability in the use of public monies, entities should prepare and publish their financial information as soon as possible after the end of the financial year. The later entities produce and publish financial reports after their balance date, the less useful financial reporting is to stakeholders and for informed decision making.

Draft financial reports provided for audit

Five out of eight entities provided draft financial reports for audit by their agreed milestones.

Each entity agrees with us dates to provide draft financial reports for audit. This is usually through a client strategy document which we give to the entity at the end of our planning visit, confirmed with a letter to the entity before our final visit for the audit year.

Certification of financial reports by legislative deadline

Management and audit certified financial reports for all eight entities by their legislative deadlines.

GOCs must have their financial reports prepared and audited no later than 31 August each year.

2.4.2 Quality and accuracy

Financial report process

Most electricity GOCs have shell financial reports agreed by their external auditors and their audit committees each year. This practice helps detect qualitative errors before 30 June, reduces entities' workload at year-end and allows enough time to consider disclosure issues in a methodical and timely manner.

Financial results may still require adjustments to year-end disclosure. We raise errors reported in financial data with management; we require correction of material errors to issue an unqualified audit opinion. The entity may also change its draft financial reports after submitting them to audit, to correct or complete reported information or improve readability.

Material financial report and disclosure adjustments

Material disclosure adjustments include changes to reported amounts and commentary in financial reports made since the first substantially complete draft was provided to audit.

Entities did not make material changes to draft financial reports in 2013–14. Changes were made to reclassifications between line items to make the statements more readable. These did not affect the net operating result or net assets disclosed.

Most changes aimed to improve quality and understanding of the financial reports. Entities also made changes applying AASB 13 *Fair value measurement* for the first time in 2013–14.

Prior period adjustments

Entities made adjustments to 2012–13 figures disclosed in the 2013–14 financial reports, reflecting new Australian Accounting Standards, AASB 11 *Joint arrangements* and AASB 119 *Employee benefits*. Ergon adjusted prior period figures to incorporate better information recognising unbilled network charges.

Overall, prior period adjustments decreased net profit after tax reported in 2012–13 by $21 million and decreased net assets by $1 million.

2.5 Significant financial reporting issues

2.5.1 Going concern status—CS Energy

Our report *Results of audit: Energy sector entities 2012–13* (Report 9: 2013–14) details the ongoing issue of CS Energy's financial sustainability. CS Energy reported losses over the past four years totalling $761.5 million. Notably, $614.6 million comprised asset write-downs in 2010–11 associated with the carbon pricing scheme and generator business restructure.

CS Energy reported a net loss of $59.8 million in 2013–14 but forecasts a return to profitability in 2015–16. An onerous contract continues with the Gladstone Interconnection and Power Pooling Agreement. Continuing coal supply constraints at Callide also affect operations.

In preparing its 2013–14 financial report, CS Energy performed a going concern and solvency evaluation, analysing forecast cash flow, balance sheet, earnings and available debt facilities. Analysis excluded the non-cash effects of asset impairment, onerous contract and site rehabilitation adjustments.

CS Energy monitored its going concern, solvency and sustainability status, reporting monthly to the board of directors and shareholding Ministers. QTC continues to monitor this GOC as its going concern status depends on continuing access to undrawn debt facilities with QTC and ongoing government support.

2.5.2 Carbon pricing scheme effects

In 2013–14, carbon pricing continued to affect generators' total revenue and expenditure. Stanwell and CS Energy spent $564 million ($600 million in 2012–13) on carbon pricing and incurred $129.2 million ($159 million in 2012–13) in associated liabilities at 30 June 2014.

Generators seek to recover all carbon costs, but the amount is determined in reference to the average NEM intensity, which historically results in 80–90 per cent of this cost being actually recovered. The high carbon intensity of coal-fired generators prevents 100 per cent of carbon cost recovery through the pool and contract market.

Liabilities owing at 30 June 2014 will settle in 2014–15. The repeal of carbon legislation will remove a significant cost from the generator businesses in 2014–15.

2.5.3 Solar tariff rebates

The Queensland Solar Bonus Scheme is a government-mandated solar feed-in tariff (FIT) that pays eligible customers for the electricity eligible solar photovoltaic (PV) systems generate and export to the Queensland electricity grid.

Solar tariff rebates booked to distributor revenue and associated expenditure line items in 2013–14 totalled $354 million ($242.3 million in 2012–13) across 358 187 customers with solar panels connected to the grid (300 966 customers in 2012–13). These costs are included in the regulated revenue distributors receive so net effect over subsequent years on operating profit after tax is zero.

The receipt of the cash flow for these rebates is generally after two years, with approved pass-throughs advised to the QCA in year one, and price resets taking into account the recovery of these monies in year two.

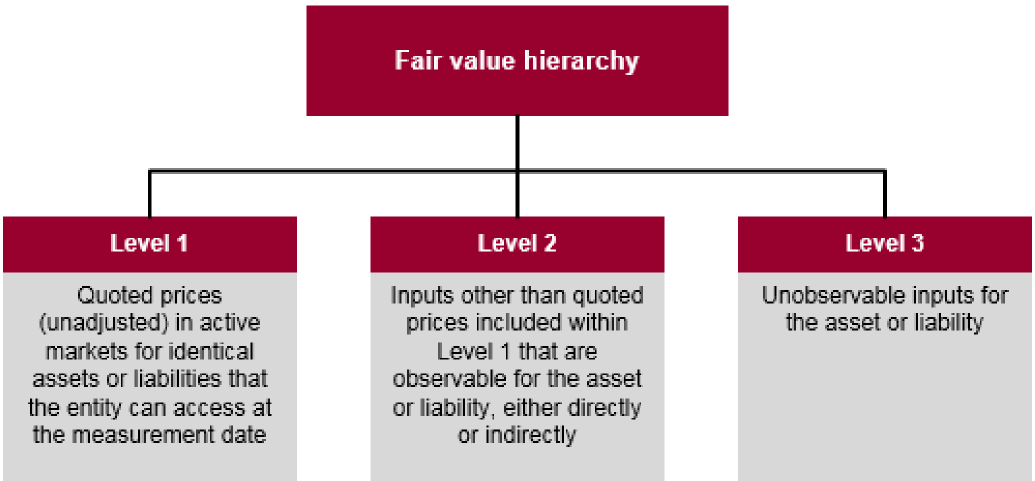
The scheme has changed over the past 12 months, with installations completed before 30 June 2013 now the only customers to retain a 44 cent FIT. The eight cent FIT ceases from 1 July 2014, so distributors will only administer the 44 cent solar rebate scheme. Distributors will settle the eight cent FIT receivables held at 30 June 2014 through the current process.

The state government announced on 12 October 2014 that it plans to restructure electricity bills so that the government would make up the costs of the scheme from a Strong Choices Electricity Price Relief Fund, should it be re-elected in 2015.

2.5.4 Impact of AASB 13—Fair Value Measurement

AASB 13 *Fair Value Measurement* applied for the first time in 2013–14, introducing a fair value hierarchy and new associated disclosure requirements. The fair value hierarchy looks at the degree to which valuation inputs are based on observable market evidence, as Figure 2E illustrates.

Figure 2E
AASB 13—fair value hierarchy



Source: Queensland Audit Office

The new requirements mainly affected the valuation and disclosure of derivative instruments, with some disclosure effects on property, plant and equipment balances.

Derivative valuations now need to take into account credit risk for the entity and counterparty in each transaction processed. The change in valuation methodology for derivative instruments did not materially change values reported, partially due to the state's credit position.

In some cases, disclosure changes affected the quality and timeliness of financial statement preparation.

2.5.5 Joint venture accounting

AASB 11 *Joint Arrangements* applied for the first time in 2013–14 to financial reporting periods beginning on or after 1 January 2013. The new standard replaces AASB131 *Interests in Joint Ventures*.

The SPARQ joint arrangement held by Energex and Ergon was proportionately consolidated into the accounts of both entities for the first time in 2013–14. Energex and Ergon have disclosed this change in their 2013–14 financial reports.

2.5.6 Ergon unbilled network charges

Network charges form part of the cost of distributing electricity. Distributors recover these costs from customers through their retailers, as electricity is consumed by business and households. As retailers progressively reading customer meters throughout the billing cycle, an estimate needs to be done at 30 June to calculate the charge for meters not yet read.

Historically, Queensland distributors have not reported unbilled network charges at 30 June where a subsidiary retail operation existed within the group. On consolidation, the network revenues and charges within the group are eliminated. However, on separation of the retail arm the retailer experiences issues in aligning its revenue and expenses.

In 2013–14, Ergon engaged external resources to build analytical capability and estimate unbilled network charges accurately on a consumption model. This led the Ergon parent entity to increase the 2012–13 net profit after tax by $3 million and its net assets by $105 million, disclosed in the 2013–14 financial report.

In the Ergon Energy Queensland Pty Ltd financial report, the 2012–13 net profit after tax was decreased by $3 million and the net assets decreased by $103 million.

Review of this matter in 2013–14 looked at the principles and accounting treatments for consistency with AASB 118 *Revenue* and AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. Both the Ergon consolidated group and Ergon Energy Queensland Pty Ltd made appropriate disclosures in the 30 June 2014 financial reports.

2.5.7 Under recovery of revenue balances at 30 June

In Queensland, network GOCs operate predominately under a revenue cap and record a receivable on the balance sheet when there is a difference between the amount of revenue they are allowed to collect and the amount of revenue they actually collect. This is known as an under recovery of revenue and is recorded as a receivable on the balance sheet of network GOCs at 30 June. The under recovery balance also includes:

- solar PV FIT pass-through
- service target performance incentive scheme (STPIS).

For distributors, solar PV FIT pass-through costs represent 42 per cent of the total under recovery balance at 30 June 2014. Regulated revenue represents 49 per cent and STPIS the remaining nine per cent.

At 30 June 2014, entities recognised a total of $1.48 billion as under recovery receivables across Powerlink, Energex and Ergon. As Figure 2F illustrates, this amount increased by $972 million (190 per cent) since 30 June 2012.

Figure 2F
Queensland transmission and distribution unrecovered revenue
30 June 2012 to 30 June 2014

Entity	30 June 2012 $ m	30 June 2013 $ m	30 June 2014 $ m
Powerlink	28.3	13.1	24.3
Energex	233.0	557.0	903.0
Ergon Energy	251.0	377.0	557.0
Total	**512.3**	**947.1**	**1 484.3**

Source: Queensland Audit Office

Key drivers for increased under recoveries in 2013–14 include:
- underestimating the solar panel rebate scheme at the time of AER determinations
- consumption when setting tariffs for 2013–14 being above actual consumption experienced during the 2013–14 year
- the escalation of prior period under recoveries at the weighted average cost of capital as determined by the AER.

A review of the under recoveries accounting treatment at 30 June 2014 found the treatment continues to meet the measurement and probability requirements of the accounting standards. The timeframe to recover this balance is subject to AER approval as part of the annual pricing approval process.

The International Accounting Standards Board has a project underway which may introduce a standard for rate-regulated industries. Entities will need to reassess how they recognise under recovery balances, should Queensland GOCs change the way they do business or the Board introduce a new revenue accounting standard.

2.5.8 Financial reporting of non-current assets

When applying AASB 116 *Property, Plant and Equipment,* GOCs can adopt either the cost model or the revaluation model for reporting an asset in the financial statements.

GOCs also apply AASB136 *Impairment of Assets* to assess any reduction in value where the amount to be recovered through use or sale of the asset is less than the reported value.

Figure 2G shows the current method of accounting energy GOCs use.

Figure 2G
Dominant asset valuation methodology

Entity	Model	Valuation technique (under AASB 13)
Stanwell	Cost, impaired to net realisable value using a combination of income based and sale values	N/A
CS Energy	Cost, and cost impaired to net realisable value using an income based approach	N/A
Powerlink	Fair value	Income approach
Energex	Fair value	Income approach
Ergon Energy	Fair value	Income approach

Note: Stanwell and CS Energy use an income approach to test impairment; for Stanwell asset Swanbank E, fair value less cost to sell was also used in 2013–14.

Source: Queensland Audit Office

In comparison to generators, which value assets at cost or a lower net realisable value, network businesses value their assets at fair value. Generators, which report their value at cost, will not account for any valuation increases resulting from discounted cash flows or estimated sale values, but will account for any valuation decreases resulting from those assessments. This means the balance sheet will not include the upside of current market assessments of sale values or increases in revenue earned.

For network businesses whose supply systems are at fair value, the discounted cash flow is the value recorded in the financial reports.

Overall, the net change in energy sector asset values resulting from revaluation and impairment reversals represented $526 million or 1.6 per cent change in asset values as shown in Figure 2H.

Figure 2H
2013–14 changes in asset values

Energy GOC	Net book value 30 June 2014 $ m	Revaluation 2013–14 $ m	Value of impairment reversal $ m
Energex	11 685	490 4.2%	0
Ergon	9 879	(449) (4.5%)	0
Powerlink	7 503	210 2.8%	0
Stanwell	2 169	0	0
CS Energy	1 450	0	275 19.0%
Total energy sector	**32 688**	**251**	**275**

Source: Queensland Audit Office

Valuation of generation assets

Generation assets are valued at either cost or recoverable amount. Recoverable amount is the higher of value in use, based on a discounted cash flow model, and fair value less costs to sell. This should represent the amount the asset could be sold for in an arm's length transaction.

The generation assets were impaired to their recoverable amount in 2010–11 by $1.02 billion, triggered by the proposed introduction of the federal government's carbon pricing regime. The value in use calculation used to value the assets contained significant judgements relating to:

- market factors—estimated demand from consumers, cost of fuel to operate the generation plant, estimated sale price of energy, generation capacity, derivatives and other risk management tools in place
- estimated cost of carbon and the effect of carbon pricing on these market factors
- discount rate incorporating the cost of equity and debt.

Australian accounting standards require management to make significant judgements when determining asset values and there may be a range of outcomes acceptable under those standards. Management discloses significant assumptions, both in valuation judgements and sensitivity of valuations to those judgements, in the financial report to help readers to interpret the resulting value.

Each year, management of GOCs must assess changes to the operating environment, including their key assumptions used to value assets, to determine if the assets should be written down further or adjusted back to cost.

For 2011–12 and 2012–13, management did not make further adjustments to the reported values.

In 2013–14, there were no indications that the generation plant had further reduced in value. The removal of the federal carbon pricing regime and higher internal valuation modelling led management to assess if the earlier impairment write-downs should be reversed and values of the assets increased.

Stanwell and CS Energy reached different conclusions on the reversal of previous write-downs due to the significant judgements made by management. We consider both results are reasonable and comply with Australian accounting standards. Management of the two generators have disclosed the judgements used in the financial statements.

Stanwell and CS Energy developed their own estimates of the future electricity market operation and price. This estimate was based on any publicly available market information (such as AEMO advice and updates) and management judgements on demand for energy; gas market operations; RET; reliability of economic information and the effect of LNG in Queensland; future environmental regulation; and other factors.

Management applied the estimate of market operations and prices, together with an estimate of future costs such as fuel, to individual pieces of generation plant. As a result, the value for individual plant within Stanwell and CS Energy differed significantly.

Stanwell concluded there is significant uncertainty in market factors influencing the management assumptions and the impairment should not be reversed in 2013–14.

CS Energy recorded a $275 million impairment loss reversal in 2013–14, partly reversing the significant impairment loss recorded in 2010–11. This represented a 19 per cent increase in value and resulted in a higher profit value. The reversal was based on changes to CS Energy's future cash flow assumptions (including market modelling of electricity prices) and the removal of carbon pricing from 1 July 2014. The main triggers were higher forecast electricity prices (excluding carbon), compared to those used in the 2011 model (which recorded the original impairment and reduced levels of entity-specific uncertainty, compared to 2012 and 2013). A reduced forecast in electricity demand in the Queensland market offset these factors.

In 2014–15, both GOCs should consider the eventuality and effect of LNG on the Queensland electricity market, RET changes and any new environmental/carbon measurements implemented. GOCs should analyse and assess the potential future reversal of impairments before the end of 2014–15.

Valuation of network assets

Regulated assets for transmission and distribution are measured at fair value on an income approach, recognising revaluation increments and decrements either in the statements of profit or loss or revaluation reserve.

Entities undertake valuations annually so an asset's carrying value does not differ materially from its fair value at the reporting date.

Fair value is determined by entities using an income approach—there is no market based evidence of fair value, due to the specialised nature of the regulated assets; and the items are rarely sold, except as part of a continuing business. Key assumptions of income approach valuations include:

- revenue cash flows for the remainder of the regulatory period, set by the regulator
- revenue cash flows for subsequent regulatory periods which management estimates, based on regulator guidelines
- operating and capital expenditure which management estimates
- discount rate incorporating the cost of equity and debt
- terminal value representing the value of the supply system at the end of the cash flow model, calculated as a multiple of the regulated asset base.

The reported net book value at 30 June 2014 for Powerlink, Energex and Ergon totalled $29.06 billion. This included an overall increase in revaluations using the income approach of $251 million or 0.9 per cent ($443.7 million in 2012–13). Revaluation of assets is processed through a reserve and does not affect net profit, except for changes in depreciation expense in future periods.

This net revaluation of $251 million includes a devaluation of $449 million (4.5 per cent) to Ergon's assets for 2013–14. The reduction in value was mostly due to management's decreased estimate of revenue to be earned in future regulatory periods and bringing forward the timing of estimated future capital expenditure.

Energex revalued assets upwards by $449 million (4.5 per cent), due to management's decreased estimate of future capital expenditure aligned with the Electricity Network Capital Program review and increased expected regulated revenue, offset by an increased discount rate.

GOCs management have considered valuation assumptions in light of current developments (status of AER regulatory determination negotiations and potential divestment of energy assets) and are satisfied valuations remain appropriate.

2.5.9 Valuation of CS Energy's onerous contract

There was a material adjustment to CS Energy's onerous contract in 2013–14. CS Energy's Gladstone interconnection and power pooling agreement is a liability on the balance sheet, as it is considered onerous. Management used a discounted cash flow model to calculate the value of the onerous contract and made key assumptions and estimates on the discount rate, future wholesale prices, generation, electricity supply and unavoidable contract costs.

In 2013–14, the onerous contract increased by $235 million to $388 million—a 125 per cent increase in value. Management reported this change as an expense and reduced net profit.

Management determined the onerous contract value using the same assumptions as the calculation of property, plant and equipment. The forecasts and assumptions management used are sensitive to changes in estimated revenue cash flows. In 2013–14, CS Energy estimated there would be less volatility in future prices, compared to prior period calculations. This increased exposure to the interconnection and power pooling agreement.

2.6 Financial performance, position and sustainability

When forming an audit opinion on the financial report, we must assess an entity’s ability to continue and operate as a going concern. We also assess an entity's financial performance, position and financial sustainability.

We assess an entity's financial sustainability in three key ratios—operating ratio; capital replenishment ratio; and debt to revenue ratio. These ratios demonstrate an entity's ability to pay its ongoing expenses; replace and grow its assets; and pay its debts as and when they fall due. We also assess flows between entities and the GGS.

By nature, generator and network businesses have different revenue streams. Generator businesses operate in a competitive National Electricity Market where their returns are subject to market forces of supply and demand. In comparison, network businesses have largely fixed returns determined by the Australian Energy Regulator (AER) in five-year periods. Revenue streams are more predictable for network businesses and this is reflected in the different capital structures used, compared to those used by generators. In effect the generators and networks operate inherently different businesses and this limits comparisons of financial performance, position, and sustainability between these entities.

2.6.1 Financial performance and position

Figure 2I details some significant account balances affecting the financial performance and position of the energy sector, using consolidated results from the five GOCs.

Figure 2I
Whole of energy sector—key financial information from 2009–10 to 2013–14

Financial information	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Factors affecting financial performance					
Revenue	5 869.80	6 675.54	7 462.83	9 029.16	9 380.86
Depreciation and amortisation	964.47	1 048.91	1 193.88	1 308.60	1 387.56
Net profit after tax	582.17	86.92	834.56	1 190.52	1 184.75
Factors affecting financial position					
Property, plant and equipment	24 463.14	26 009.47	29 424.22	31 312.40	32 688.62
Borrowings	12 878.65	14 138.94	15 738.50	16 743.51	17 093.58
Net assets	8 891.13	9 317.65	10 365.76	10 930.38	11 503.74

Source: Queensland Audit Office

The energy sector's financial performance and position has steadily improved over five years, despite generator restructure and asset impairment, due to the introduction of carbon pricing, decreasing the sector's net profit after tax in 2010–11.

Network GOCs Powerlink, Energex and Ergon continue to dominate the supply chain with a $28.52 billion share (74 per cent) of revenue over the five-year period. Networks also supplied $3.67 billion (93 per cent) of dividends over five years, held $29.06 billion (88 per cent) of property, plant and equipment and represented $15.76 billion (92 per cent) of borrowings at 30 June 2014.

The different supply chain functions and regulatory requirements of energy GOCs limits the ability to compare their financial performance and financial position. Some accounting standards also allow entities to choose from a selection of accounting treatments so similar transactions and balances may be measured and reported differently.

2.6.2 Financial sustainability

When forming an audit opinion on the financial report, we must assess each entity’s ability to continue and operate as a going concern. In this regard, an assessment is made also over an entity’s future financial sustainability. We have provided information on the financial sustainability ratios we used at Appendix B of this report.

2.6.3 Operating ratio

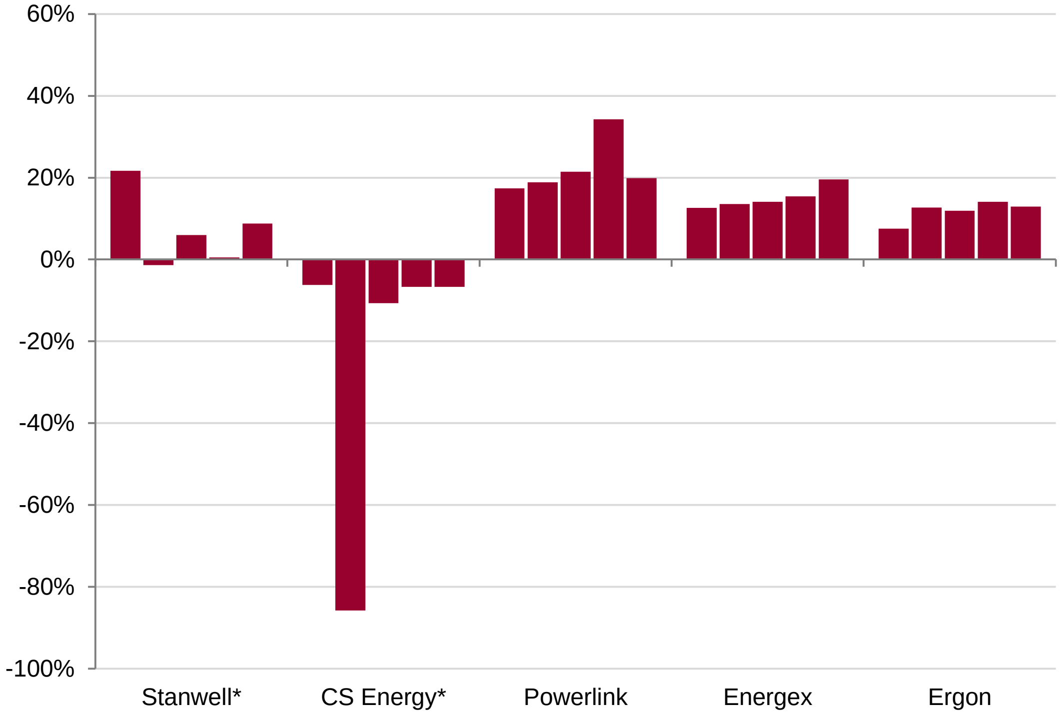
This ratio is the operating profit after tax, expressed as a proportion of total revenue. Operating profit after tax includes non-cash revenue and expenditure items. Unlike measures of absolute financial performance, comparing operating ratios allow readers to better understand the financial performance of entities relative to their size.

The operating ratio should be positive over the medium to long term for an entity to remain financially sustainable. Negative ratios indicate net losses, generating insufficient revenue to fund operating and future capital expenditure. This depletes cash reserves, increases borrowings and may compromise investment in new assets and service level maintenance.

Input costs, plant reliability and effective hedging against market positions drive generators. Network entities are driven by their ability to minimise disruption to electricity supply in accordance with industry standards. The industry has focused on decreasing costs in 2013-14.

Figure 2J summarises operating ratio results over the last five years for each GOC.

Figure 2J
Operating ratios for the five years from 2009–10 to 2013–14



* In 2010–11 the generator businesses were restructured. After the restructure, CS Energy and Stanwell were different in terms of staffing, level of debt and make up of the portfolios they hold which decreases the comparability of their businesses pre and post-restructure.

Note: The carbon scheme commenced in July 2012 which affects the ratio for generators in both the 2012–13 and 2013–14.

Source: Queensland Audit Office

Except for CS Energy, each entity averaged an operating ratio more than zero over five years. An average operating ratio of 10 per cent over five years means, across the sector, energy PNFCs were earning $1 for every $10 of revenue generated. Generator restructure meant the operating surplus ratios of Stanwell and CS Energy were negative in 2010–11, but CS Energy has had a negative ratio in all five years.

CS Energy has increased revenue over the last two consecutive years, but expenditure has increased correspondingly, resulting in an overall slight decline in the operating ratio. Decreases in revenue from electricity sales of $70.7 million since 2012–13 resulted from reduced generation and a decline in the time weighted average pool price. There was a 30 per cent reduction in generation at Callide Power Station due to coal supply issues. CS Energy's results for 2013–14 include a $238.4 million re-measurement expense for the Gladstone interconnection and power pooling agreement, which is treated as an onerous contract in the 2013-14 financial report. CS Energy booked an impairment reversal of $275 million after a change in the fair valuation of generation assets (a partial reversal of the significant impairment loss recorded in the year ended 30 June 2011) in 2013–14. CS Energy expects to return to profitability in 2015–16.

Stanwell has increased revenue over the last three consecutive years. Its coal revenue agreement continues as an element of profitability. Stanwell's operating ratio in 2013–14 has improved, due to its decreased total expenditure (seven per cent) on 2012–13. Although costs had been trending up over the five year period, an undertaking to improve commercial performance, measured as a reduction in operational expenditure has produced the 2013-14 result. The generator has not booked impairment reversals since its generation assets were valued in 2010–11 when the sector was restructured. Although carbon pricing has been repealed, other mitigating market factors pose significant uncertainty over the reversal of impairment for Stanwell assets at this point in time.

In 2012–13 Powerlink's divestment of its 41.1 per cent share in Electranet, for a pre-tax gain of $353.3 million, significantly increased its operating ratio in that year. Otherwise, Powerlink’s operating ratio has remained steady over the last three consecutive years. Excluding the divestment of Electranet, both revenue and expenditure rose over the past five years. However Powerlink achieved targets for operational efficiencies and cost reductions (both operating and capital expenditure) in response to shifting consumer expectations, regulatory reform and increased economic pressure.

The operating ratio of Energex has increased, driven by continued revenue increases and, in 2013–14, a five per cent decrease in expenditure compared to 2012–13. We noted increases in both regulated revenue and passed-through solar PV feed in tariffs. Expenditure was higher in 2012–13, due to the program to 'right size' the Energex group which reduced overall staff numbers. Energex achieved savings in ongoing network operating and support costs during 2013–14 as it reviewed work practices and organisational structure to align the business with actual trends in energy demand and consumption.

Ergon's operating ratio has decreased slightly on 2012–13. Revenue and expenditure is increasing but more slowly than in previous years. Like Energex, Ergon implemented efficiency measures, workforce reductions and a revised program of work to slow expenditure. Doing business costs Ergon more than Energex, because Ergon operates outside south-east Queensland. These costs are offset by community service obligation funds the Department of Energy and Water Supply provides.

Risk to future operating ratios

Demand and electricity pricing: Demand is falling: AEMO and Powerlink demand forecasts is tracking below 2012–13 levels. Queensland's high dependency on LNG projects is stimulating demand. High electricity pricing may cause some industrial participants to suspend or close operations, while domestic customers continue to look for ways to reduce consumption and reliance on grid power.

Profitability of core business assets: Generators are making core business assets more commercial. Stanwell and CS Energy must continue to improve gross margins to remain competitive in supply markets and minimise consumer price effects.

Cold storage of generator units: Stanwell has announced plans to bring back two of its Tarong units and put into cold storage the Swanbank power station, due to supply cost issues. Stanwell has contracts in place to sell the gas into the market rather than use it to generate electricity at the power station. Units in cold storage depreciate and incur overheads to remain serviceable for future use.

Coal revenue sharing agreement: Queensland's Commission of Audit recommended divesting non-core businesses, including Stanwell's coal export revenues. Had Stanwell operated without its coal revenue sharing agreement revenue in 2013–14, it would have recorded a net profit before tax of $67 million ($149.6 million net loss before tax in 2012–13), compared to 2013–14's profit before tax of $172.7 million ($8.3 million in 2012–13). Stanwell would have paid a far smaller dividend to government in both years.

Regulatory environment: Regulatory policy outcomes such as RET and carbon pricing, which federal and state governments set, significantly affect generator results.

Regulatory reporting: Network entities rely on revenue which the AER approves. The AER is increasing the amount of information it obtains for benchmarking purposes through regulatory reporting and it will increase its scrutiny of the revenue it allows networks to recover. Network businesses will emphasise efficient spending on building and maintaining assets to obtain funding through the AER process.

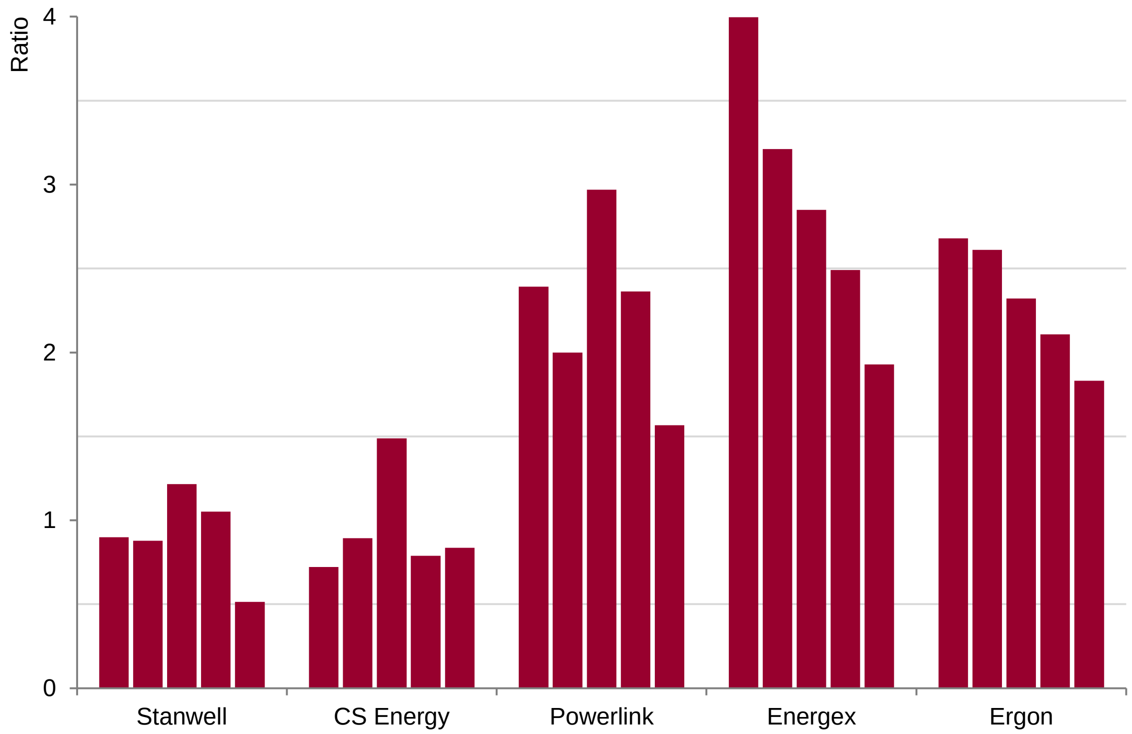
Market and tariff reform: Increasing solar PV system installation and tariff reform continue to affect network businesses in terms of maintaining current performance and aligning business with actual trends in energy demand and consumption.

2.6.4 Capital replenishment ratio

The capital replenishment ratio compares the annual net expenditure on non-current assets (predominantly property, plant and equipment) to annual depreciation. An average ratio below one, over time, indicates that assets are being built or replaced slower than the non-current asset base is depreciating.

Figure 2K summarises the results of capital replenishment ratios over the last five years for each GOC.

Figure 2K
Capital replenishment ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

On average over the past five years, the stock of non-current assets expanded or was replaced at a rate of $2.10 to every dollar assets depreciated.

All GOCs continue to record ratios close to one over five years; however, the generation companies are not spending money on new assets at the same rate as network companies.

Network GOCs have a high capital replenishment ratio, due to network replacement and augmentation requirements linked to electricity demand forecasts. Generator GOCs have a lower ratio, which is expected since they use capital to overhaul existing assets and are not constructing power stations. In the last two years a downward trend can be seen due to reduced augmentation requirements for network GOCs and lower than forecast electricity prices for generator GOCs which has resulted in generating units being placed in cold storage.

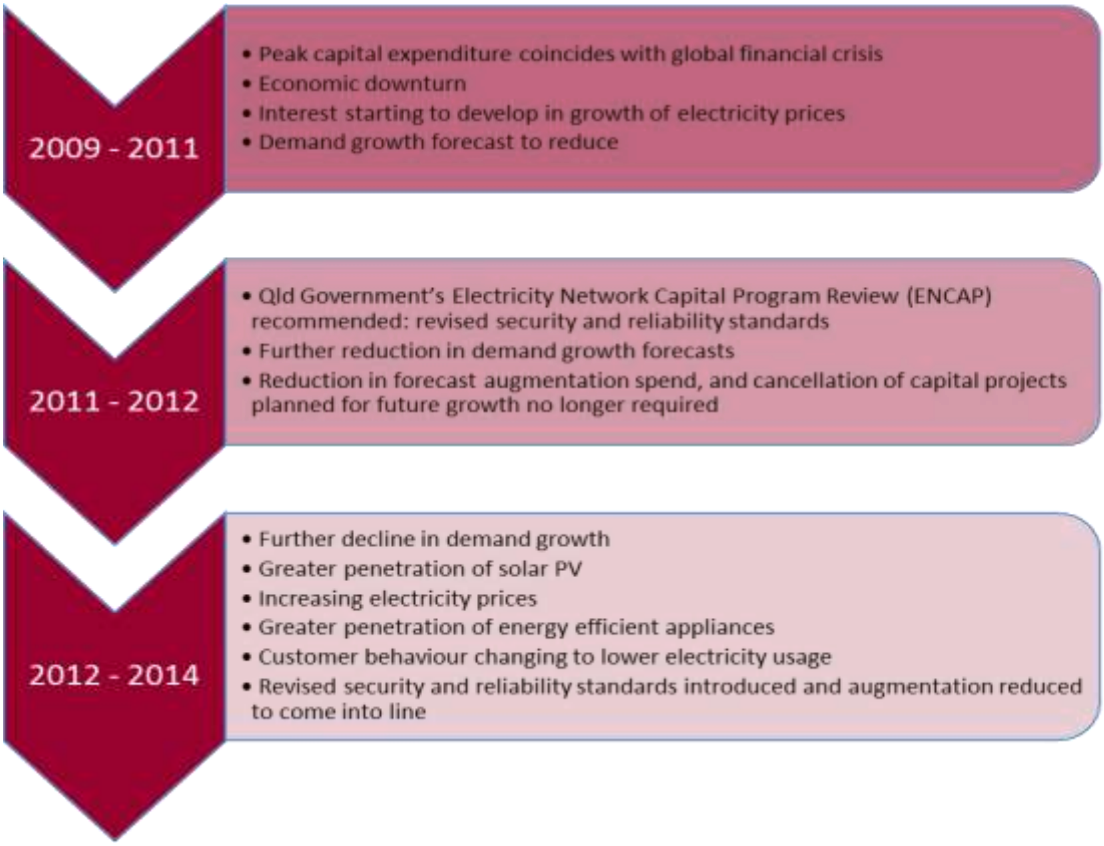
Assets under construction

Although some assets under construction have been written off, the drivers for decreased capital spend are:

- the cancellation of projects in advance of work commencing, where it has been determined that work is no longer required
- the deferment of projects not deemed necessary at this point in time
- reduced customer requested works.

Lower network demand and cold storage of generation assets have also driven changes in planned maintenance schedules across the industry. Figure 2L highlights industry factors which decreased capital spend over the last five years.

Figure 2L
Industry factors resulting in decreased capital spend



Source: Queensland Audit Office

Risks to future capital replenishment ratios

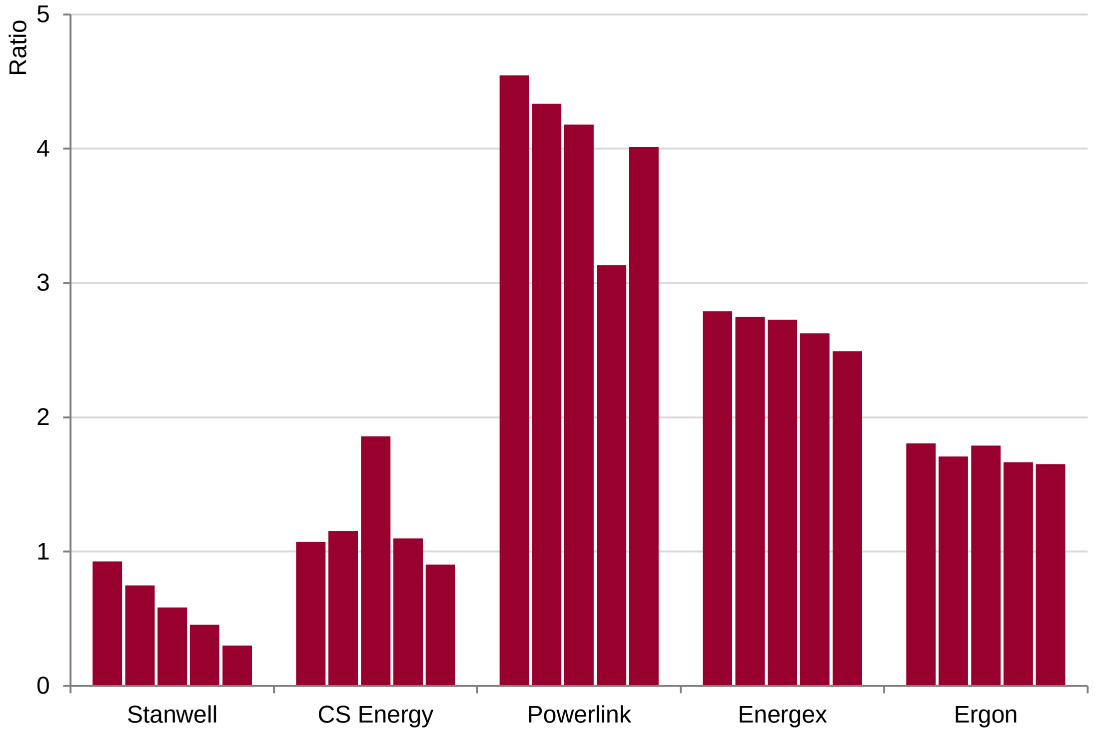
GOCs increased their asset bases over the past five years, but more slowly. Businesses are rationalising capital works programs, anticipating changes in expected demand, expenditure and efficiency. GOCs must source funds to replace and grow assets to meet customer requirements and remain sustainable.

2.6.5 Debt to revenue ratio

The debt to revenue ratio assesses an entity's ability to pay the principal and interest on borrowings when they fall due from the funds generated through the entity's operations. Debt in this ratio represents borrowings and does not include other liabilities such as trade creditors. Revenue includes both cash and non-cash items.

Figure 2M summarises results of the debt to revenue ratios over the last five years for each GOC.

Figure 2M
Debt to revenue ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

Energy PNFCs averaged a debt to revenue ratio of 1.97 over the past five years. In total, GOCs had $17.09 billion in long term borrowings at 30 June 2014 ($16.75 billion in 2012–13) against operating revenues of $8.86 billion ($9.1 billion in 2012–13). Ratio differences between generators and network entities depend on the nature of the business: generators maintain established plant while networks expand based on customer demand.

A move in the ratio for CS Energy from 1.09 to 0.90 in 2013–14 highlights the increased revenue booked from the reversal of asset impairment in 2013–14.

Stanwell borrowings decreased by $250 million in 2013–14, while revenue increased by $42 million, strengthening Stanwell's overall position.

The debt to revenue ratio for Powerlink continues to be higher than that of the distributors as distributor revenue includes charges Powerlink passes on and an overall higher level of revenue. The sale of Electranet Pty Ltd in 2012–13 moved Powerlink's ratio to 3.13 in 2012–13. In comparison to 2013–14, revenue was higher in 2012–13, even though debt levels were consistent across 2012–13 and 2013–14.

Energex and Ergon both recorded increased revenue and debt in 2013–14 compared to 2012–13, resulting in steady ratios in 2013–14.

We reported in *Results of audit: Energy sector entities 2012–13* (Report 9: 2013–14) the revenue streams of the generator and network businesses are different. Market forces drive generator revenues streams while the AER regulates network revenue in five-year periods. This makes revenue streams more predictable for network businesses.

As a result, the GOCs use different capital structures to operate their businesses. The capital structures of network GOCs contain debt below AER benchmark debt levels (as applied in the guidance related to determinations of the regulated rate of return) where 60 per cent of the regulated asset base is assumed to be funded by debt. This reflects the way businesses operate in that the costs of assets are spread across the life of those assets. Recovery of debt costs occurs through the regulated return on assets as set out in the revenue determinations by the AER.

Interest 'bite'

A supplementary measure of debt sustainability relates to an entity's ability to service its debt obligations—to pay interest and to repay or refinance loans when they fall due. The interest expense ratio—'interest bite'—considers how much operating revenue is required to pay interest charges.

Energy PNFCs recorded a total interest expense on their borrowings of $918.4 million in 2013–14 ($4.18 billion in the five years to 30 June 2014).

Total interest expense for the sector as a whole averaged 11 per cent of revenue earned across the five year period. However, interest expense as a percentage of revenue for generators averaged 4.8 per cent, compared to network entities which averaged 13.2 per cent over the same period. This is consistent with results for the debt to revenue ratio.

Risks to future debt ratios

GOCs will need to ensure capital structures continue to support long term sustainability.

Our *Results of audit: Energy sector entities 2012–13* Report to Parliament recommended that the Department of Energy and Water Supply (DEWS) and Queensland Treasury and Trade (QTT) include within performance reporting framework three measures of financial sustainability used. QTT has since decided to include the capital replenishment ratio in its monitoring activities of network GOCs. QTT indicated the other financial sustainability indicators we identified are already monitored as part of its performance monitoring framework, so no changes were needed.

2.6.6 Net flows to and from government

An entity's ability to meet its operating and capital expenditure commitments; replace and grow its asset base; and repay debt is also influenced by flows to and from government. PNFCs pay dividends, income tax and competitive neutrality fees to the government; and receive community service obligation receipts and equity contributions for selected activities. We assess the effect of these net flows on the financial results (financial performance, position and sustainability) of these entities.

Figure 2N outlines the net flows between the PNFCs within the energy industry and the government over the past five years.

Figure 2N
Whole of sector—net flows between government and energy sector
2009–10 to 2013–14

Financial information	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Flows from government					
Equity contributions	102.80	0.00	300.00	0.00	0.00
Community service obligations	251.60	399.30	415.20	632.00	519.00
Flows to government					
Dividends declared	(502.62)	(561.76)	(692.47)	(1 148.30)	(1 062.29)
Income tax expense	(238.37)	(9.53)	(356.97)	(496.40)	(489.62)
Competitive neutrality fees	(38.36)	(103.66)	(129.27)	(167.58)	(174.73)
Equity withdrawals	(380.00)	0.00	0.00	0.00	0.00
Net flows (to and) from the government					
Net flows	(804.95)	(275.65)	(463.51)	(1 180.28)	(1 207.64)

Source: Queensland Audit Office

Energy PNFCs recorded net flows to the government of $1.20 billion in 2013–14 and $3.93 billion in the five years to 30 June 2014.

Equity contributions and withdrawals

Equity contributions and withdrawals relate to equity movements in the form of cash to and from government entities. The energy sector has had negligible equity contributions and withdrawals over the past five years.

In 2009–10, Energex had a dividend reinvestment for B class shares movement of $102.8 million. In the same year, Stanwell had a capital repatriation of $380 million. This capital reduction was effected in accordance with a state government direction under s.115(3) of the *Government Owned Corporations Act 1993*.

The only other cash movement through equity in the sector occurred in 2011–12 when CS Energy received a capital injection for $300 million in response to an equity shortfall.

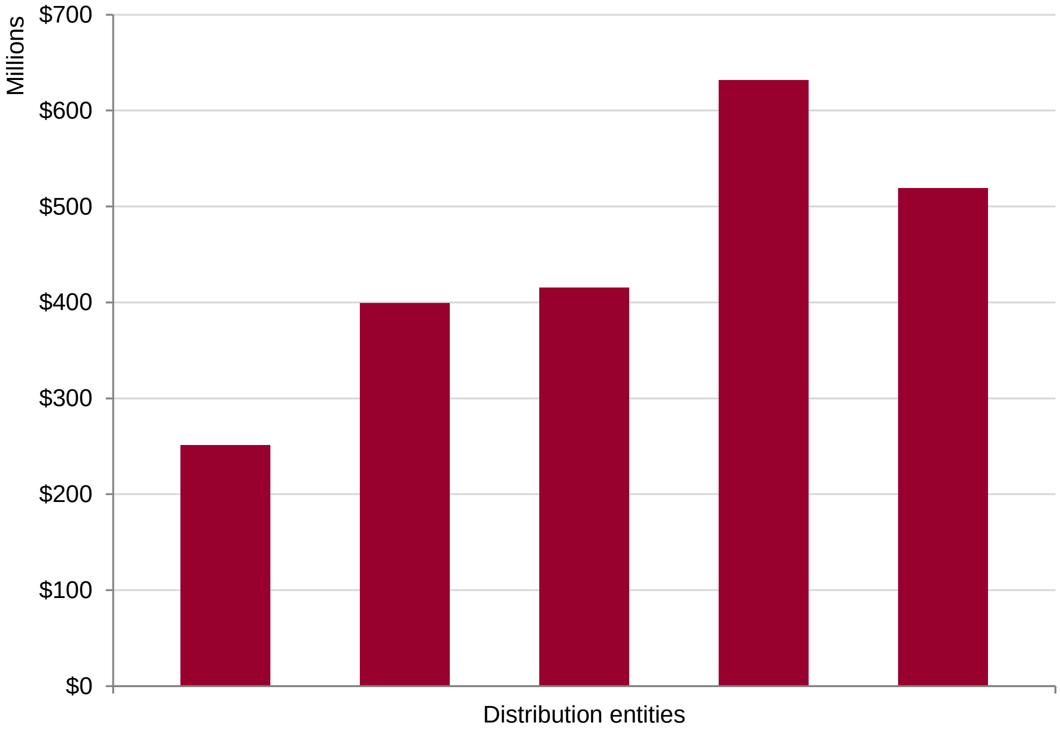
Community service obligations

The size of the network that the retail arm of Ergon Energy operates in regional Queensland make it unreasonable to recover operational and capital expenditures from customers. As a result, CSO payments from government form the second major portion of the consolidated group's revenue. Ergon received $519 million in 2013–14 and $2.18 billion in the five years to 30 June 2014. The CSO deed was renegotiated in 2013–14, with a new deed in place from 1 January 2014.

In 2012–13, Energex received a CSO payment of $35.8 million. Energex did not receive any further payments otherwise, during this five-year period

Figure 2O shows the level of CSO payments made to the consolidated Ergon group's distribution entities and Energex over the past five years.

Figure 2O
CSO payments to Ergon and Energex over the past five years



Note: In 2012–13 Energex received a CSO payment of $35.8 million. No further payments were received by Energex during this five-year period.

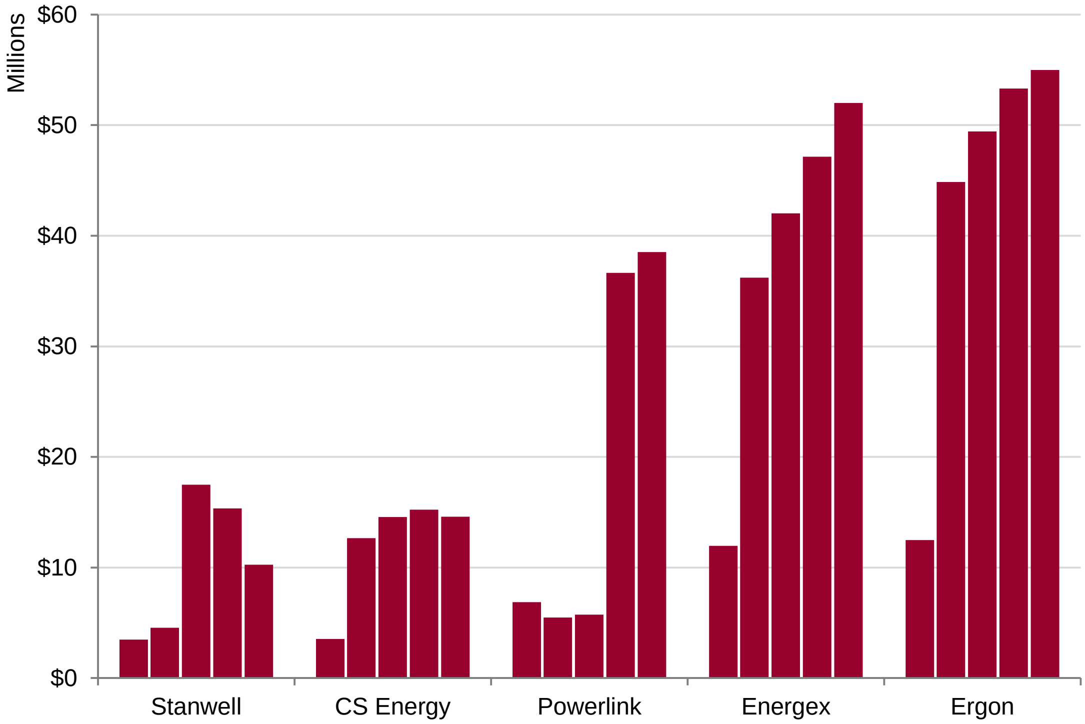
Source: Queensland Audit Office

Competitive neutrality fees

The purpose of establishing GOCs is to provide services to the community on a commercial basis, with the direct intention of making commercial returns that government can redistribute to meet other government objectives.

To ensure balance in the commercial environment, the government imposes competitive neutrality fees. Figure 2P shows the upward trend in the competitive neutrality fees charged to GOCs over the past five years in relation to their borrowings from QTC.

Figure 2P
Amount of competitive neutrality fees charged to GOCs over the past five years



Source: Queensland Audit Office

These fees remove the advantages that GOCs obtain being owned by the public sector. An example of this is where GOCs borrow monies from QTC at a rate lower than similar private sector entities could obtain in the private market.

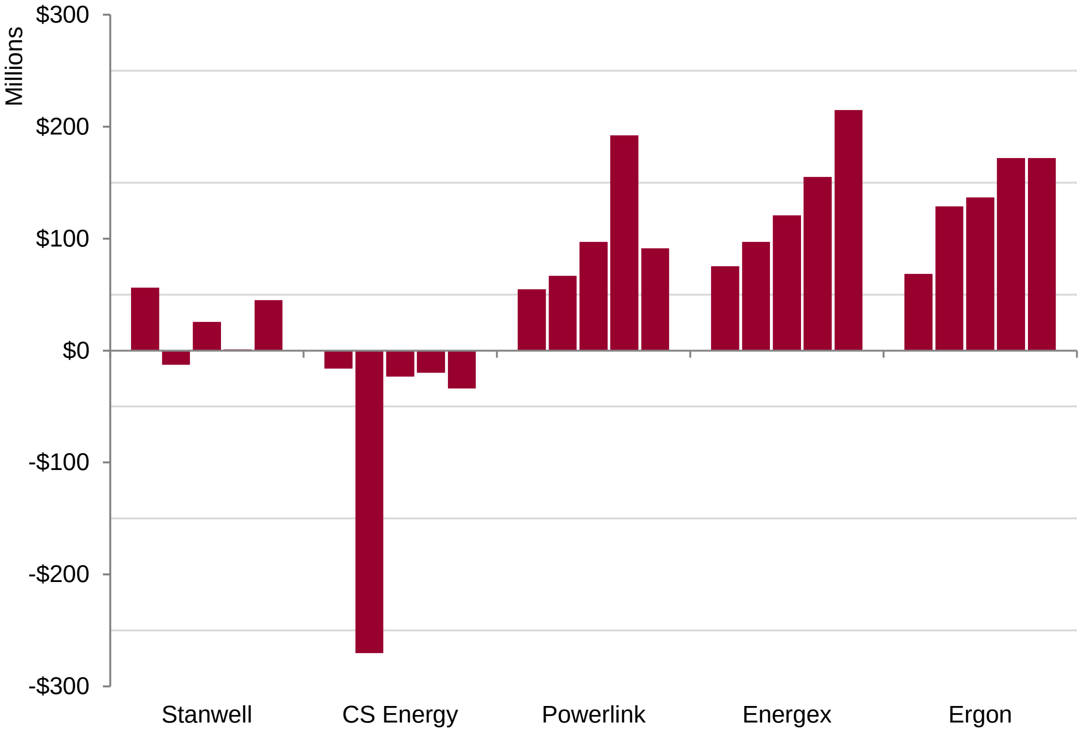
Income tax expense

Energy GOCs must make income tax equivalent payments on taxable income to the Queensland Government. This is in line with s.129(4) of the *Government Owned Corporations Act 1993*.

The Australian Taxation Office administers tax liabilities under the national tax equivalent regime (NTER). The NTER broadly uses the provisions of the *Income Tax Assessment Act 1936* (Cth), the *Income Tax Assessment Act 1997* (Cth) and associated legislation; the NTER manual; and other ATO rulings and pronouncements to determine the tax payable by the GOCs.

Figure 2Q shows the income tax expense of the energy GOCs over the past five years.

Figure 2Q
Income tax expense over the past five years



Source: Queensland Audit Office

Each GOC has implemented tax consolidation legislation and each is taxed as a single entity for group purposes. The GOCs, as 'head entities' in the tax consolidated groups, make income tax payments on behalf of their wholly owned subsidiaries.

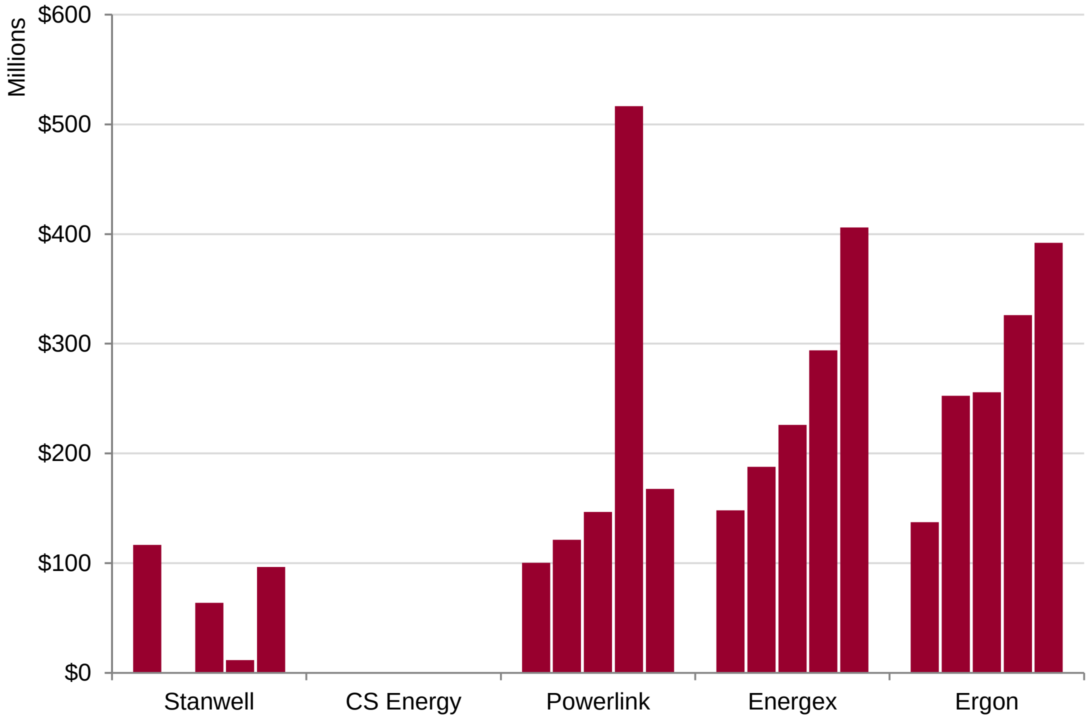
The tax consolidated groups have also entered into tax sharing and tax funding agreements. Tax funding agreements require each wholly owned controlled entity to pay to the parent GOC the current tax liability (asset) and any unused tax losses the parent GOC assumes. Tax sharing agreements set out the allocation of income tax liabilities amongst the entities, should the parent GOC default on its tax obligations; and the treatment of entities exiting the tax consolidated groups.

Dividends

The energy GOCs usually pay 80 per cent of their net profit after tax as a dividend to the Queensland Government. In 2013–14, GOCs declared dividends of $1.06 billion ($1.14 billion in 2012–13) for return to government. In 2012–13, Powerlink returned 90 per cent of its profit after tax to the Queensland Government. CS Energy did not return any dividends as it has declared a loss for the past five years.

Figure 2R highlights the amount paid out as dividends over the last five years for each level of the supply chain.

Figure 2R
Dividends declared over the past five years



Source: Queensland Audit Office

3 Water sector

In brief

Background

In Queensland, households, agriculture and industry are the primary users of water.

In south-east Queensland, the Queensland Bulk Water Supply Authority (trading as Seqwater) sells bulk water to distributor retailers and local government councils. Seqwater has a single controlled entity named the Australian Water Recycling Centre of Excellence Limited (AWRCEL). Its role is focused on research into water recycling technology. Outside south-east Queensland, the composition of the water supply chain is different with SunWater Limited (SunWater), local government councils and other entities sharing ownership of public sector surface water storage infrastructure (dams).

Changes to regional bulk water as recommended by the 30 April 2013 Queensland Commission of Audit Final Report were accepted in principle by the government. No final decision has been made by government at the date of this report.

This chapter details the results of our audit of Seqwater, AWRCEL, SunWater, Gladstone Area Water Board (GAWB) and Mount Isa Water Board (MIWB).

Conclusions

The financial reports of all five entities were audited by their statutory deadlines and unqualified audit opinions were issued for each of the entities covered in this chapter in 2013–14.

We considered the ability of Seqwater, SunWater, GAWB and MIWB to operate as a going concern in the context of their financial performance, position and sustainability. Overall, these entities are financially sustainable. Seqwater continues to be affected by interest charges on its loans and depreciation expenses on its assets.

Key findings

- We completed our audit of financial reports of all five entities by their legislative deadlines. One of five entities did not provide its draft financial report for audit by the agreed deadline.
- We found draft financial reports were generally of a satisfactory quality. We did not require material adjustments to the account balances within the draft financial reports provided for audit.
- Disclosure changes made to the draft financial reports provided for audit were primarily the result of entities electing to improve the quality of financial report disclosures rather than errors. Some disclosure errors were, however, identified as part of our audit process; these related mainly related to the application AASB 13 *Fair Value Measurement* and the applicability of new and emerging Australian accounting standards.
- Seqwater's debt at 30 June 2014 was more than 12 times its revenue in 2013–14, as a result of loans from its water supply assets. Significant tax losses carried over from its amalgamation with the SEQ Water Grid Manager on 1 January 2013 has influenced its recent financial performance. Seqwater's debt is guaranteed by the state, but it will rely primarily on future price increases and cost reductions to address its current adverse performance and position.
- MIWB's operating ratio has declined in 2013–14, due to decreased water sales to a single private sector mining company of $2.2 million; and increased expenditure resulting from the filtration costs after an outbreak of blue-green algae.
- SunWater's capital replenishment ratio has increased substantially from 2012–13 following the completion of the majority of new water supply assets at Woleebee Creek. GAWB's capital replenishment ratio also declined on completion of water supply assets on Curtis Island over the same period.

3.1 Background

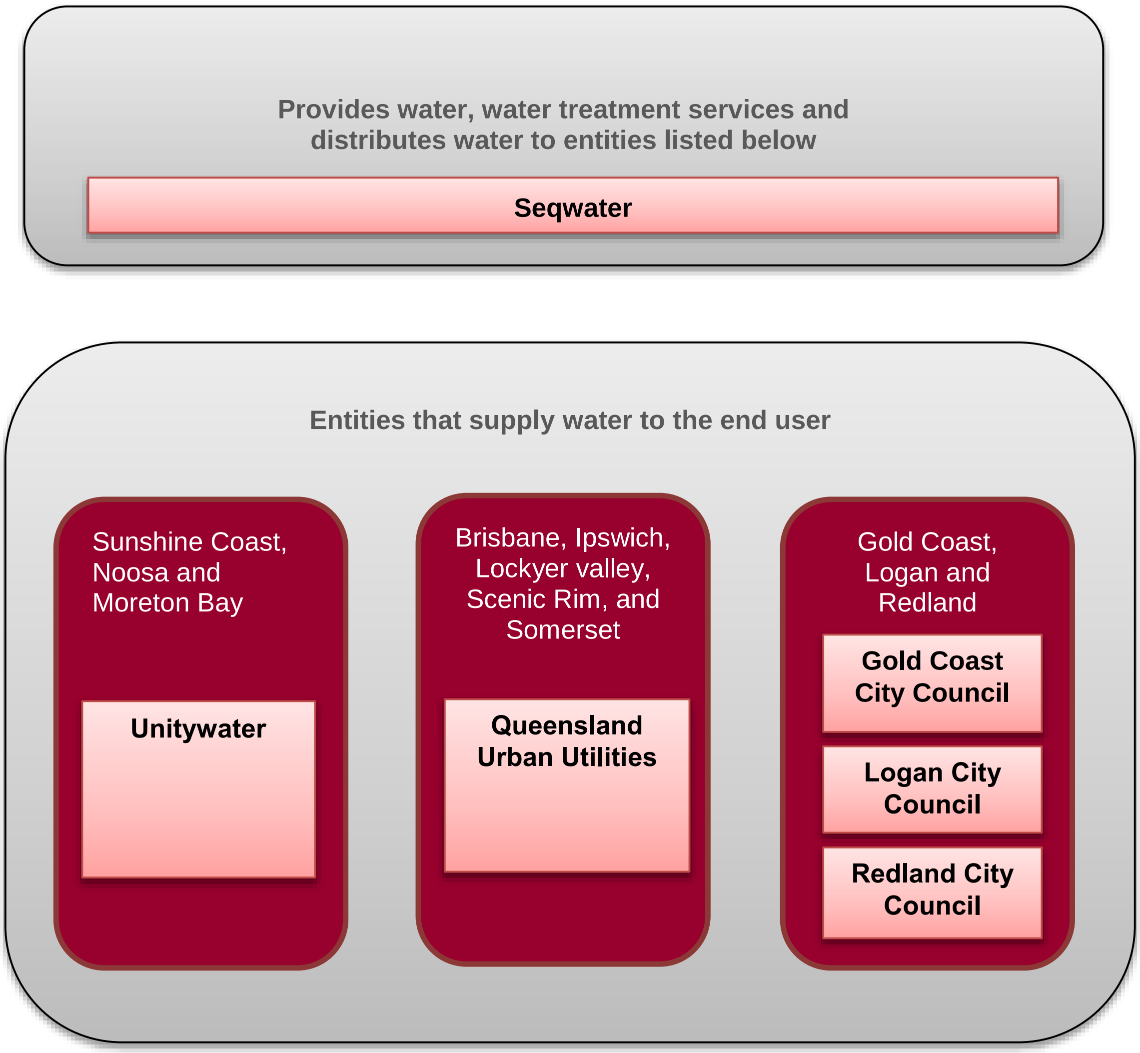
In Queensland, water is used primarily by households, agriculture and in the mining, electricity generation, tourism and manufacturing industries.

Direction and oversight of the water sector in Queensland is primarily provided through the Department of Energy and Water Supply (DEWS). A number of other government departments also have a strategic role in managing the supply of water throughout the state.

3.1.1 South-east Queensland

Within south-east Queensland, the Queensland Bulk Water Supply Authority (trading as Seqwater) sells and distributes bulk water to entities as described in Figure 3A using rules established under the Bulk Water Supply Code and Bulk Water Supply Agreements. Seqwater owns the infrastructure to manufacture, store, distribute and treat the water it sells.

Figure 3A
Water supply chain in south-east Queensland



Source: Queensland Audit Office

Central SEQ Distributor-Retailer Authority, trading as Queensland Urban Utilities (QUU); Northern SEQ Distributor-Retailer Authority, trading as Unitywater; and three local governments—Gold Coast, Logan and Redland City Councils—are responsible for distributing water purchased from Seqwater to water users in their respective local government areas.

QUU and Unitywater are known as distributor-retailers under the *South-East Queensland Water (Distribution and Retail Restructuring) Act 2009* (the Restructuring Act). The separation of Noosa from the Sunshine Coast Regional Council, and subsequent establishment of the Noosa Shire Council on 1 January 2014 has had minimal impact on the structure of the public sector water supply chain. There have been no other significant changes to the structure of this water supply chain since the Restructuring Act came into effect on 1 January 2013.

Figure 3B summarises some of the more significant changes to water sector entities in south-east Queensland over the last five years.

Figure 3B
Major restructures to south-east Queensland water entities

Date	Description	Enabling legislation
1 July 2010	QUU, Unitywater and the Southern SEQ Distributor-Retailer Authority (trading as AllConnex) is established to manage the water distribution and sewerage treatment responsibilities of 10 local government councils	*South-East Queensland Water (Distribution and Retail Restructuring) Act 2009*
1 July 2011	WaterSecure, the legal owner of manufactured water assets, amalgamates with Seqwater	South-East Queensland Water (Restructuring) Regulation 2011 made under the *South-East Queensland Water (Restructuring) Act 2007*
1 July 2012	AllConnex disbands, transferring functions back to Gold Coast, Logan and Redland councils	*South-East Queensland Water (Distribution and Retail Restructuring) Act 2009*
1 January 2013	Operations transfer from the Queensland Bulk Water Transport Authority (QBWTA) and SEQ Water Grid Manager to Seqwater	South-East Queensland Water (Restructuring) and Other Legislation Amendment Regulation (No.1) 2012
1 January 2013	Queensland Water Commission disbands and transfers functions mainly to DEWS and Seqwater	*South-East Queensland Water (Restructuring) and Other Legislation Amendment Act 2012*

Source: Queensland Audit Office

3.1.2 Outside south-east Queensland

Outside south-east Queensland, the composition of the water supply chain is different. SunWater Limited (SunWater), local government councils, water boards and other entities share ownership of public sector surface water storage infrastructure, irrigation channels and major pipelines to distribution points.

Outside the south-east corner, Queensland has no major manufactured water supply assets to provide water security in times of drought. There are also no major interconnecting pipelines to connect the state's dams and other assets. Instead, 22 water supply schemes operate by virtue of the *Water Supply Act 2000*. These schemes allocate water rights to local government councils, water boards and other entities from the state's surface and underground water sources.

Figure 3C summarises the composition of the water supply chain outside south-east Queensland.

Figure 3C
Stand alone public sector water entities that operate outside south-east Queensland

Entity	Purpose
SunWater	Owns and operates the infrastructure that stores and supplies water to irrigators, industrial customers and local government councils
Gladstone Area Water Board (GAWB)	Owns and operates infrastructure that stores and supplies water to the Gladstone Regional Council, industry and other customers in and around the greater Gladstone region
Mount Isa Water Board (MIWB)	Sources and sells water to the Mount Isa City Council and two private sector entities
Category 2 water boards	Smaller water boards that source and sell water primarily to irrigators in designated areas throughout the state
Local government councils	Local government councils source and sell water to their ratepayers from a number of surface and groundwater sources

Source: Queensland Audit Office

In comparison to south-east Queensland, drinking water provided to urban customers is primarily sourced and treated from local government owned infrastructure. Most local government councils outside south-east Queensland provide a combination of water distribution, treatment and other services to their ratepayers.

Two category 1 water boards (GAWB and MIWB) and 20 category 2 water boards store, treat, distribute and reticulate water for regional users. The two larger category 1 water boards operate in the Gladstone and Mount Isa regions. They are significantly larger than their category 2 water board counterparts and operate commercialised operations. Category 2 water boards are focused on the water supply needs of primarily irrigation customers in their designated areas.

SunWater provides infrastructure which supplies bulk water to irrigators and industrial customers. SunWater does not own all the rights to sell water contained in its dams and other infrastructure. Instead, other public and private sector entities purchase and sell water allocation entitlements between each other. This means the holder of the water allocation entitlement retains the risk of drought and other water shortages.

3.1.3 Changes to PNFC entities in the water sector

The Queensland Commission of Audit's final report in 2013 made four recommendations about regional bulk water. The state government accepted all four recommendations in its response, which was made publicly available on 30 April 2013.

Local management arrangements

The first recommendation involved moving SunWater's eight irrigation channel schemes to local management arrangements. If implemented, this will lead to the transfer of water distribution assets and the operational responsibilities for those assets to privately owned companies and/or cooperatives. The government has established an interim board for each of the eight irrigation channel schemes. These interim boards are supported by an independent project team established by DEWS. This project team has been involved in conducting strategic due diligence and supporting the interim boards prepare business proposals on how irrigator owned entities could manage these schemes.

The government is yet to make a final decision on moving the eight irrigation channel schemes to local management arrangements.

Other changes

The other three Commission of Audit recommendations relate to:

- the offer of SunWater's dedicated water supply infrastructure servicing commercial and industrial clients for private ownership and/or private operation, depending on the solution which provides the best value for money outcome for the government
- maintaining SunWater as a government owned corporation with its residual function to retain ownership and management of existing bulk water assets in regional Queensland
- the development of future bulk water storage facilities by the private sector, unless there is a compelling public good or market failure reasons not to do so.

The government has since released its *Final Plan: The Strongest & Smartest Choice — Queensland's Plan For Secure Finances And A Strong Economy* (the Final Plan), offering SunWater's commercial water pipelines (dedicated water supply infrastructure) for lease instead of sale. As part of the Final Plan, the government will not proceed with the leasing of these assets without first seeking a mandate at the next state election.

3.1.4 Entities covered in this chapter

We report on results of our audits of Seqwater, SunWater, GAWB and MIWB; and entities they control. Seqwater, SunWater, GAWB and MIWB make up the composition of PNFCs within the water sector for the purposes of this chapter. This report does not include the audit results of former PNFCs within the water sector which ceased to exist before 1 July 2013.

Seqwater has a single wholly owned subsidiary named The Australian Water Recycling Centre of Excellence Limited (AWRCEL). SunWater has three wholly owned subsidiaries; none of these were required to produce financial reports in 2013–14.

3.2 Conclusions

We issued unqualified audit opinions for all four PNFCs within the water sector and one controlled entity in 2013–14. An unqualified audit opinion means readers can rely upon the results in the audited financial reports of these entities.

We completed the audits of all entities by their legislative deadlines. One of the five entities did not provide its draft financial report for audit by the deadline agreed with us.

We were generally satisfied with the quality of draft financial reports provided to us for audit. No material changes were required to the account balances within the draft financial reports provided to us. Entities generally made disclosure adjustments to improve the quality of their draft financial reports.

Some errors and omissions to disclosures within the draft financial reports of PNFCs within this chapter were noted; these related to the application of Australian Accounting Standard AASB 13 *Fair Value Measurement* and the impact of new and future Australian accounting standards.

When forming an audit opinion on the financial report of an entity, we assess an entity's ability to operate as a going concern. We also assess an entity's financial performance, position and sustainability. Our assessment of an entity's financial sustainability includes assessing its ability to pay its ongoing expenses; to replace and grow its assets; and to pay its debts as and when they fall due.

Overall, these entities are financially sustainable, but the future sustainability of Seqwater continues to rely on achieving the indicative prices in the ministerial approved price path, which the Queensland Competition Authority (QCA) is reviewing. Future decreases in Seqwater's operating expenditure will also contain any future increases in the price of water.

Seqwater's financial sustainability continues to be affected by interest on its loans and depreciation charges on its water supply assets.

3.3 Audit opinions

We issued unqualified audit opinions on the financial reports of all five entities. We issue an unqualified audit opinion when the financial report complies with relevant accounting standards and legislative requirements relating to the establishment and keeping of accounts. An unqualified audit opinion assures the reader that the financial report is reliable and presents a true and fair view.

Figure 3D provides further detail on the audit opinions we issued for each entity covered in this chapter.

Figure 3D
2013–14 audit opinions issued

Audit	First draft financial report provided for audit	Financial statements signed	Opinion issued	Certified by deadline	Opinion
		Government owned corporation			
SunWater	08.08.2014	22.08.2014	28.08.2014	Yes	Unqualified
		Statutory bodies and subsidiary			
Seqwater	11.08.2014	28.08.2014	29.08.2014	Yes	Unqualified
AWRCEL	02.09.2014	30.09.2014	02.10.2014	Yes	Unqualified
GAWB	21.07.2014	28.08.2014	29.08.2014	Yes	Unqualified
MIWB	21.08.2014	28.08.2014	29.08.2014	Yes	Unqualified

Source: Queensland Audit Office

3.4 Timeliness and quality of financial reports

3.4.1 Timeliness

To show accountability in using public monies, entities should prepare and publish their financial reports as soon as possible after the end of the financial year. The later financial reports are produced and published after their balance date, the less useful they are to stakeholders and for informing decision making.

Each entity agrees with us on the dates to provide draft financial reports. This usually occurs at the conclusion of our planning visit and we confirm these dates with a letter to the entity later in the audit year.

Government owned corporations and statutory bodies must have their financial reports prepared and audited no later than 31 August each year. Only the Treasurer may approve exemptions for statutory bodies. No statutory bodies requested exemptions in 2013–14.

Large public companies limited by shares must have their financial reports prepared and audited no later than 31 October each year.

Four of the five entities (GAWB, SunWater, Seqwater and the AWRCEL) were able to provide us with a materially complete version of the draft financial report for audit by the agreed date. The financial reports of all five entities were certified by management and audit by their legislative deadlines.

3.4.2 Quality and accuracy

We were generally satisfied with the quality of the draft financial reports and supporting work papers provided to us for the purpose of conducting our audits. There were no material errors within the draft financial reports provided which required adjustments to the account balances in 2013–14.

We were generally satisfied with disclosures supporting account balances within draft financial reports. Most disclosure changes were the result of entities electing to improve the quality of disclosures in their financial reports.

Common disclosure errors identified across the entities were the result of entities not:

- fully complying with the disclosure requirements of AASB 13 which came into effect for financial reporting periods commencing on or after 1 January 2013
- adequately disclosing the impact of Australian accounting standards applicable in future reporting periods.

3.5 Significant financial reporting issues

Entities can choose to adopt either the cost or revaluation model when deciding how to value a class of assets for financial reporting purposes.

The revaluation model is another way of describing assets recognised at their fair values. Where an entity decides to adopt the revaluation model for a class of assets, entities must choose a valuation technique that best approximates fair value. These issues did not affect the AWRCEL significantly as it does not hold any property, plant and equipment.

Figure 3E outlines the valuation model and technique each of the four water PNFCs use.

Figure 3E
Asset valuation methodology

Model	Dominant Measurement/valuation technique	Entity
Cost	This is generally the fair value of assets/liabilities exchanged to acquire or construct the asset, with no subsequent change to these values to reflect cost, price or market movements	SunWater
Revaluation	Income approach (present value technique that takes into account the future cash flows that a market participant would expect to receive)	Seqwater GAWB
	Replacement cost (valuation technique that reflects the amount that would be required currently to replace the service capacity of an asset)	MIWB

Source: Queensland Audit Office

AASB 116 *Property, Plant and Equipment* prescribes the accounting treatment so users of the financial report can discern information about an entity's investment in its property, plant and equipment and the changes in the value of such investments. AASB 116 gives entities the option of valuing their assets at cost or fair value for financial reporting purposes.

Where entities decide to value their assets at fair value, AASB 13 prescribes further accounting treatments on deriving fair value. AASB 13 became applicable to Seqwater, GAWB and MIWB for the first time in 2013–14. This has affected the disclosures within the financial reports of these three entities but has not influenced the way in which these entities value their property, plant and equipment.

The valuation of assets in accordance with AASB 13 relies on management assumptions and estimates. We noted management could justify assumptions and estimates used in previous years to the principles within AASB 13. AASB 13 did not affect SunWater as it recognises property, plant and equipment under the cost model.

The Treasurer and Minister for Trade has directed the QCA to investigate and recommend bulk water prices to be charged by Seqwater between 1 July 2015 to 30 June 2018 and to conduct a price monitoring investigation for the GAWB for the period 1 July 2015 to 30 June 2020.

The outcome of these investigations may affect the prices charged and financial performance of Seqwater and GAWB in future years. Changes to the future prices these entities can charge may affect the valuation of certain assets because both entities value their assets under the revaluation model using the income approach.

3.6 Financial performance, position and sustainability

When forming an audit opinion on the financial report, we must assess the entity's ability to continue and operate as a going concern. We also assess its financial performance, position and financial sustainability.

We assess financial sustainability through three key ratios—operating ratio: capital replenishment ratio; and debt to revenue ratio. These ratios indicate an entity's ability to pay ongoing expenses; replace and grow assets; and pay debts as and when they fall due. We also assess flows to and from the state government as part of this assessment.

We found PNFCs in the water sector to be financially sustainable. Seqwater's longer term sustainability relies on increasing the price of bulk water to a point where it catches up with the cost of supply. Future cost savings by Seqwater will also contain the need for future price increases.

3.6.1 Financial performance and position

Figure 3F summarises the financial performance and position of PNFCs within this chapter over the past five years.

Figure 3F
Financial performance and position

Accounts	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Factors affecting financial performance					
Revenue	563.2	630.7	997.1	1 074.2	1 074.5
Expenses	511.2	533.8	1 062.3	1 225.5	1 391.5
Income tax	14.5	29.3	(17.5)	(476.0)	(360.0)
Profit after tax	37.5	67.6	(47.7)	324.7	42.9
Factors affecting financial position					
Assets	4 482.5	4 588.3	8 156.4	12 746.4	14 155.7
Liabilities	3 039.7	3 027.9	6 431.6	11 232.5	11 628.9
Equity	1 442.8	1 560.4	1 724.8	1 513.9	2 526.8

Source: Queensland Audit Office

Property, plant and equipment and borrowings dominate the overall financial position of PNFCs in the water sector. At 30 June 2014, Seqwater's borrowings accounted for 95 per cent of all borrowings, and 87 per cent of total property, plant and equipment held by the four PNFCs in this chapter.

The increases in revenue, expenses, assets and liabilities between 2010–11 and 2013–14 reflect the amalgamation of bulk water entities within south-east Queensland into Seqwater. Interest charges and depreciation expense associated with Seqwater's acquisition of significant water supply assets and loans from these entities mean expenses have exceeded revenue in recent years.

Collectively, these four PNFCs have recorded profits after tax in each of the past two years, due to the large income tax credits recorded by Seqwater in 2012–13 and 2013–14. The financial performance of SunWater and the two category 1 water authorities have been stronger than Seqwater. These entities were not affected by large borrowings from the construction of the state's manufactured water supply assets; and bulk water prices being less than the cost of supplying such water.

Water PNFCs made profits after tax of $42.9 million in 2013–14. Contributing to this were:

- Seqwater's after tax losses of $20.6 million (consisting of before tax losses of $400.2 million offset by income tax credits of $379.5 million)
- SunWater's after tax profits of $52.6 million
- GAWB's after tax profit of $10.6 million
- MIWB's after tax profit of $0.4 million.

3.6.2 Financial sustainability

Current year financial performance and position are important indicators of financial health. We also consider recent experiences to discern any trends that may be relate to future financial sustainability.

In assessing financial sustainability, we use three ratios from the results of published financial reports:

- operating ratio
- capital replenishment ratio
- debt to revenue.

Through these ratios, we found all four water PNFCs, except Seqwater, are operating financially sustainable operations. Seqwater's financial sustainability relies on a bulk water price path which QCA is reviewing and which the Minister approves. If unchanged, bulk water prices will increase between 12 per cent and 87 per cent, depending on the location of a water user's property. Appendix E provides further information about bulk water prices in south-east Queensland.

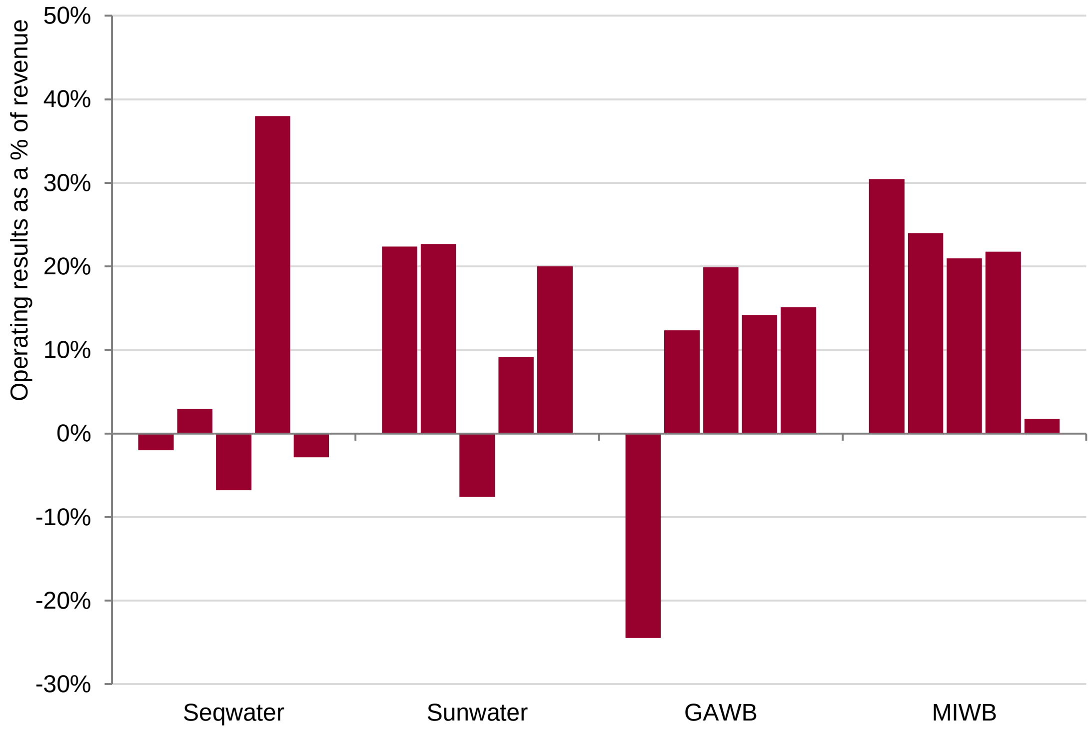
The AWRCEL has been excluded from this assessment as it relies significantly on a fixed amount of grant funding it received from the Australian Government to fund its principal activities. The AWRCEL currently has sufficient operational funding to continue as a going concern through to at least 30 June 2016.

3.6.3 Operating ratio

This ratio is calculated as operating profit after tax, expressed as a proportion of total revenue. It should be positive over the medium to long term for an entity to remain financially sustainable. Ongoing negative ratios indicate net losses, where revenue is insufficient to fund operating and future capital expenditure. This generally leads to a depletion of cash reserves, increases in borrowings and may compromise the ability of an entity to invest in new assets and/or maintain its service levels.

Figure 3G details the operating ratios of all four PNFCs in this chapter over the last five years.

Figure 3G
Operating ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

PNFCs within this chapter have averaged an operating ratio of nine per cent over the last five years, earning $1 for every $11 of revenue they generate. SunWater, GAWB and MIWB have been generating sufficient revenue to fund ongoing expenses.

Seqwater's ability to generate revenue to fund ongoing expenses has been significantly influenced by the recognition of $867.9 million in tax losses carried forward from its merger with the QBWTA on 1 January 2013. Seqwater would have reported negative operating ratios of -56 per cent in 2013–14 (2012–13: -26 per cent) had it not been for the recognition of these tax losses. These tax losses do not result in cash inflows from government but form the basis of income tax credits which can be used to offset income tax obligations arising from future profits. As at 30 June 2014, Seqwater had sufficient tax credits to not pay any income tax for the next $2.9 billion in profits at prevailing income tax rates.

SunWater's operating ratios have remained relatively strong in contrast to Seqwater. The 2011–12 negative result was due to write downs of $95.9 million primarily to the value of its irrigation assets. The value of these assets was written down because prices which irrigators could pay SunWater for the use of its assets up until 30 June 2017 were lower than SunWater initially expected. SunWater's operating ratios in 2012–13, lower than in other years, was affected by flood repair costs.

The operating ratios of GAWB have been relatively stable except in 2009–10. The improved results in 2010–11 were primarily due to the government's acceptance of new pricing arrangements from 1 July 2010 to 30 June 2015, as recommended by the QCA. The losses incurred in 2009–10 were influenced by a $6.3 million write down to the value of intangible assets connected with the construction of the lower Fitzroy Weirs and Gladstone to Fitzroy pipeline.

MIWB has historically achieved the greatest profit margins of the four PNFCs, except in 2013–14 due to:

- a review of contract prices charged to three major customers that transact with MIWB directly (Mount Isa City Council and two major private sector users)
- reduced water consumption from two of its three major customers
- increased expenditure from blue-green algae treatment and filtration costs.

Risk to future operating ratios

Distributor-retailer water pricing policies encouraging efficient water usage can also influence the future operating ratios of Seqwater if water users consume less water. This is because reduced water consumption also reduces revenue to fund the high fixed depreciation costs of the state's water supply assets and interest charges on its loans.

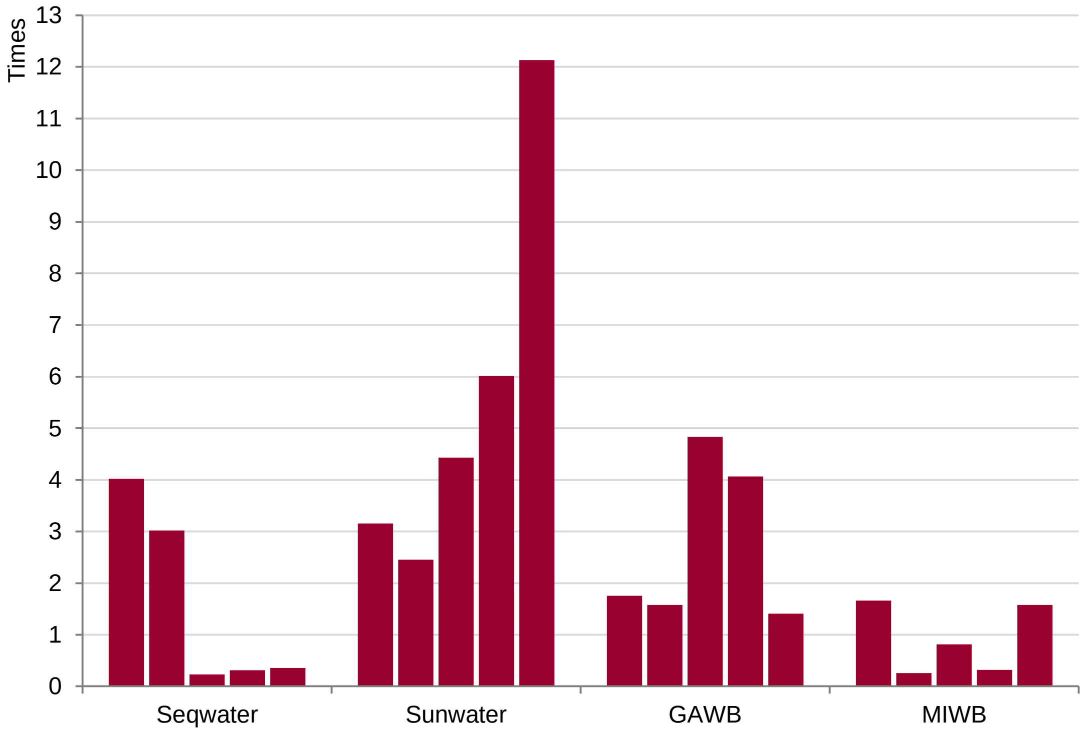
MIWB depends significantly on two private sector customers to provide more than 50 per cent of its revenue each year. The effect of this dependence was highlighted in 2013-14 when it received $2.2 million less from one of its two private sector customers than in 2012–13. The loss of one or both customers would affect MIWB's future operating ratios.

3.6.4 Capital replenishment ratio

The capital replenishment ratio compares the annual net expenditure on non-current assets to annual depreciation. An average ratio below one, over time, indicates assets are being built or replaced slower than the asset base is depreciating.

Figure 3H illustrates the results from our capital replenishment ratio analysis.

Figure 3H
Capital replenishment ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

Over the past five years, water PNFCs within this chapter were expanding or replacing their stock of non-current assets at a rate of $1.90 for every dollar of depreciation incurred through using these assets.

The large increases in Seqwater's asset base relate to the construction of stage 3 of the Hinze Dam between 2009–10 and 2010–11. As would be expected, the capital replenishment ratio of Seqwater has declined since the end of the 2001 to 2009 drought in south-east Queensland, upgrades to the Hinze Dam, and construction of other water supply infrastructure assets that were transferred to Seqwater over the past three years.

SunWater's capital replenishment rates increased substantially in 2013–14. The main reason for this relate to the completion of the majority of water supply assets at Woleebee Creek which resulted in asset additions of around $221 million. Capital replenishment rates of MIWB in 2013–14 increased because of capital works on Stage 3 of the Lake Moondarra Pipeline Upgrade and establishment of emergency filtration plant to address water quality issues associated with blue-green algae. The completion of water supply assets on Curtis Island by the GAWB has resulted in the decline of capital replenishment rates from the previous year.

Risks to future capital replenishment ratios

Residents in south-east Queensland (and some other regional parts of Queensland) experienced a drought from 2001 until 2009. The end of the drought resulted in increasing levels of stored water in south-east Queensland. Combined with the potential to further increase water supply to the south-east Queensland water grid through the state's manufactured water assets, these factors will mean that Seqwater is unlikely to significantly increase its bulk water asset supply base unless there are significant changes in water consumption and existing water supply.

Water supply and environmental issues relating to blue-green algae resulted in higher than usual capital expenditure in 2013–14 by the MIWB. These issues and other natural disasters can affect the future capital replenishment rates of all entities.

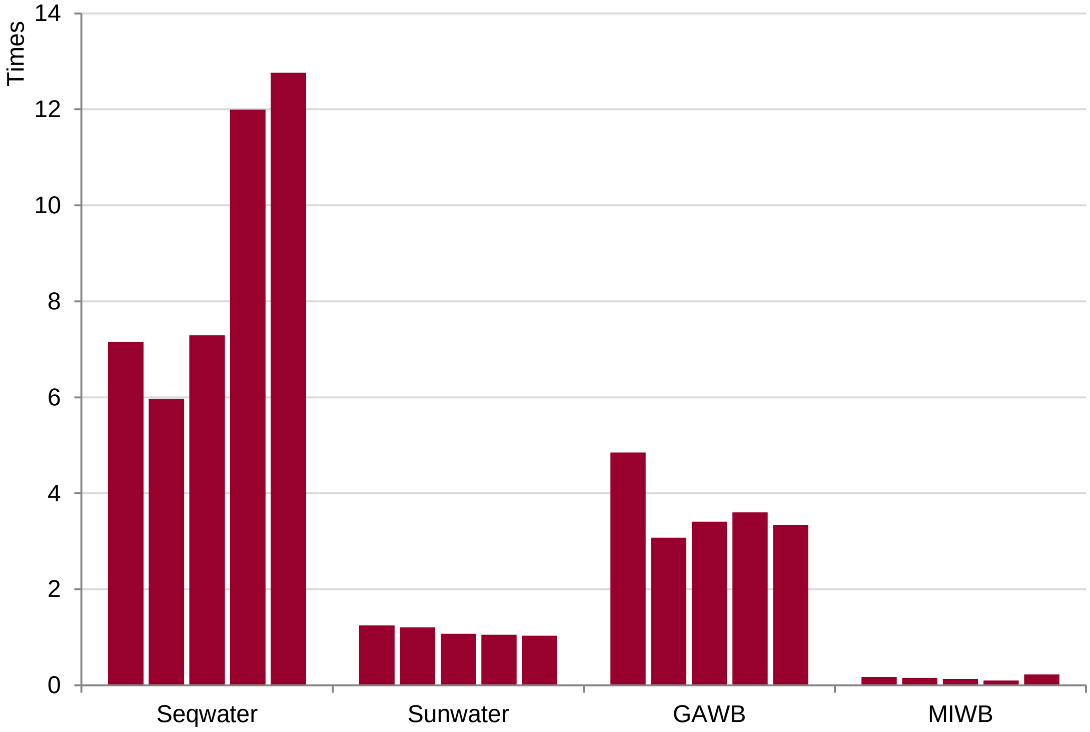
Future changes to the role of SunWater may result from the Commission of Audit's recommendation that future bulk water storage facilities be developed by the private sector unless there is a compelling public good or market failure reasons not to do so. This may influence the future capital replenishment rates of SunWater.

3.6.5 Debt to revenue ratio

The debt to revenue ratio assesses an entity's ability to pay the principal and interest on borrowings, when they fall due, from funds the entity generates. Debt is calculated as borrowings through the Queensland Treasury Corporation, measured at their book value, and does not include other liabilities such as trade creditors.

Figure 3I illustrates the debt to revenue ratios of the water PNFCs in this chapter over the past five years.

Figure 3I
Debt to revenue ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

Seqwater had higher debt to revenue ratios than SunWater, GAWB and MIWB in each of the last five years. As a sector, debt at 30 June 2014 was nine times revenue in 2013–14. PNFCs in this chapter averaged a debt to revenue ratio of 6.4 over the past five years.

The loans of Seqwater, GAWB, and MIWB with QTC are all secured by a shareholder guarantee. This means that the risk of entities not paying the principal and interest on their loans with QTC is held by the state. The loans of SunWater are not secured by the state.

Seqwater's loans at 30 June 2011 increased from 7.3 times revenue in 2011–12 to 12 times revenue in 2012–13 when it assumed responsibility for $4 billion in loans from the former SEQ Water Grid Manager and QBWTA on 1 January 2013. Seqwater's loans at 30 June 2014 have since increased to 12.8 times revenue in 2013–14 as the price it charges for bulk water continues to be less than the cost of supplying this water.

GAWB's debt to revenue position improved from 2010–11 following the announcement of higher prices from the previous year; it's debt to revenue ratios have been consistently lower than that of 2009–10 levels since then. GAWB has the second highest debt to revenue ratio of the four PNFCs. Its loans were primarily taken out to fund new water supply infrastructure assets in and around the Gladstone region.

Interest 'bite'

A supplementary measure of debt sustainability relates to an entity's ability to service its debt obligations–to pay interest and to repay or refinance loans when they fall due. The interest expense ratio, 'interest bite' considers how much operating revenue is required to pay interest charges.

PNFCs in this chapter recorded total interest expense on their borrowings of $567.2 million in 2013–14 ($1.68 billion in the five years to 30 June 2014).

These PNFCs averaged interest expenses of 39 per cent of revenue earned across the past five years. Seqwater averaged interest expense of 51 per cent of revenue earned across the same period. Its interest expense increased from 41 per cent of revenue in 2009–10 to 74 per cent in 2013–14 as a result of the loans it acquired from its merger with other bulk water entities.

By contrast, the interest expenses of other PNFCs (SunWater, GAWB and MIWB) averaged nine per cent of revenue over the same five year period.

Risks to future debt to revenue ratios

Loans across the four PNFCs totalled $9.7 billion at 30 June 2014. Seqwater held $9.2 billion of these loans. Most loans have variable interest rates. Notwithstanding a shareholder guarantee over payment of its loans in the event of default, interest rate movements can affect interest payments and future borrowings, if Seqwater is required to borrow to fund ongoing expenditure. Changes to levels of borrowings will affect the future debt to revenue ratios of Seqwater.

The past price of bulk water in south-east Queensland has been less than the cost of its supply. This difference was a primary factor resulting in the transfer of $1.8 billion in loans to Seqwater when it acquired the SEQ Water Grid Manager on 1 January 2013. The value of such loans totalled $296.1 million at 30 June 2009 and $1.9 billion at 30 June 2014. Seqwater's debt to revenue ratio will likely continue to deteriorate until the price of bulk water matches or exceeds the cost of its supply.

The outcome of QCA's price monitoring investigation of GAWB's planned pricing arrangements; and the investigation into bulk water prices Seqwater charges may affect the future debt to revenue ratios of both entities in future years.

Our report *Results of audit: Water sector entities 2012-13* (Report 7: 2013–14) recommended DEWS includes, within its annual performance reporting framework, three measures of financial sustainability we used (operating, capital replenishment and debt to revenue ratios).

DEWS has since updated its reporting framework to incorporate our recommendation. The reporting framework requires providers of drinking water and sewerage services to report industry metrics across water security, capacity to ensure continuity of supply, affordability, financial sustainability, industry and workforce capability, and customer service quality.

3.6.6 Net flows to and from the government

Flows to and from government affect an entity's ability to meet its expenditure commitments; replace and grow its asset base; and repay debt. PNFCs pay dividends, income tax and competitive neutrality fees to the government and receive community service obligation receipts, state government grants and equity contributions for selected activities. We assess the effect of net flows on the financial results (financial performance, position and sustainability) of these entities.

Flows from the state government have supported Seqwater's financial performance, position and sustainability through equity contributions it received and significant income tax credits it inherited from amalgamation with the QBWTA in the last five years. SunWater and the two category 1 water authorities (GAWB and MIWB) have contributed dividends, income tax and competitive neutrality fees to the state government across the same period.

PNFCs in the water sector recorded net flows from the government of $336.9 million in 2013–14 and $912.1 million in the five years to 30 June 2014. Figure 3J outlines the net flows between water PNFCs within this chapter and the government over the past five years.

Figure 3J
Flows from and (to) the government

Accounts	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Flows from the government					
Equity contributions	85.4	144.4	1.2	—	—
Community service obligations and other government funds	4.7	8.6	13.0	26.2	31.9
Flows (to) the government					
Dividends declared	(10.7)	(35.0)	(3.3)	(16.5)	(48.1)
Income tax (expense) credit	(14.4)	(29.3)	17.5	476.0	359.9
Competitive neutrality fees	(21.5)	(23.5)	(22.0)	(25.6)	(6.8)
Net flows (to) and from the government					
Net flows	43.5	65.2	6.4	460.1	336.9

Source: Queensland Audit Office

Income tax and dividends which GAWB and MIWB declared to the state government were remitted to the Gladstone Regional Council and Mount Isa City Council in its entirety before 2012–13. From 2012–13, all dividends and income tax paid by GAWB were retained by the state government. In the case of the MIWB, 50 per cent of dividends and income tax paid were retained by the state government and the rest were remitted to the Mount Isa City Council.

Equity contributions

Large cash contributions of equity by government reduces the amount of funds that PNFCs need to borrow to fund infrastructure and other developments. Equity injections of cash have the potential of improving the entity's operating, and debt to revenue ratios.

Cash equity contributions of $231 million were paid by government to Seqwater, SunWater and GAWB over the past five years.

Cash equity contributions of $138.5 million were made to partly fund stage three of the Hinze Dam and construction of the Wyaralong Dam. Cash contributions of $91.6 million were received by SunWater primarily to fund infrastructure programs such as the upgrade of spillway infrastructure at the Tinaroo dam.

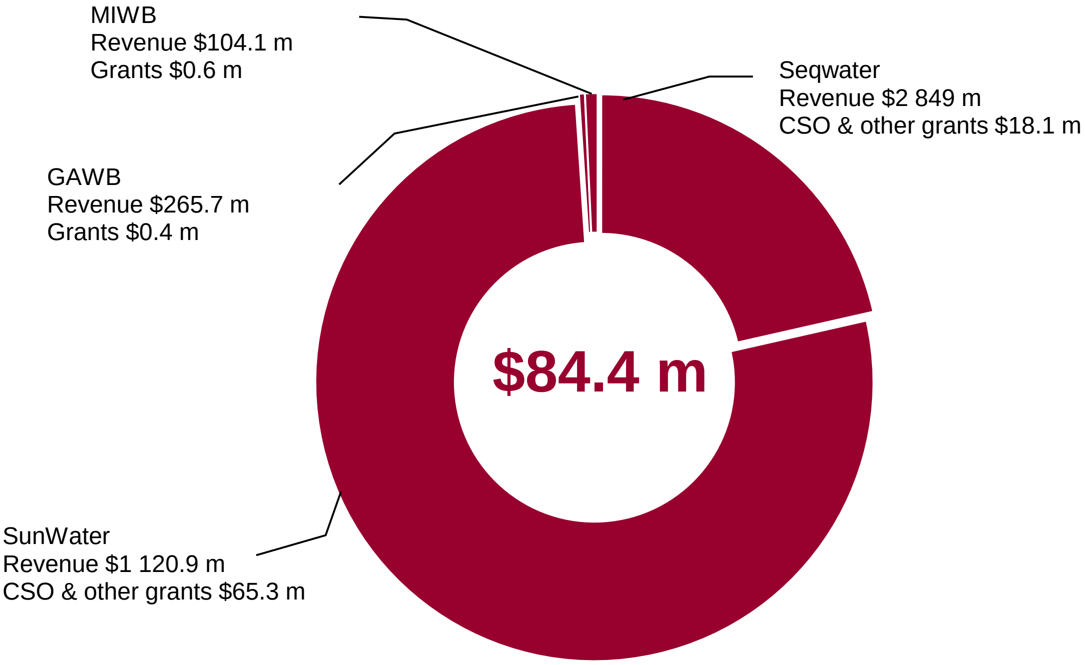
Cash equity contributions of $0.9 million paid to GAWB over the past five years have had a negligible effect on its financial performance, position and sustainability. MIWB did not receive any cash equity contributions across this period.

Community service obligations and other state government grants

The state government funds activities provided at non-commercial prices through community service obligation (CSO) revenue. The state government reimburses entities for revenue it would otherwise have earned to recover the costs of undertaking such activities. State government grants are also provided to PNFCs to fund specific projects.

CSO and grant funding from the state government has not had a significant impact on the total revenue earned of all four PNFCs in this chapter. Figure 3K provides an overview which compares CSOs and other grant funding to total revenue for each of the four PNFCs.

Figure 3K
CSO and state government grants received over the past five years



Source: Queensland Audit Office

Seqwater and SunWater received CSOs and grant funding of $83.4 million over the last five years. GAWB or MIWB did not receive CSOs but received a small amount of grant funding for specific purposes.

Seqwater and SunWater received CSO payments in recognition of the current rural water pricing policies that are applicable to irrigators. Water is provided by both Seqwater and SunWater to irrigation users at prices which are usually below the cost of providing such services. SunWater also receives CSO payments for the delivery of water to the Cloncurry Shire Council under a separate arrangement.

Competitive neutrality fees

Competitive neutrality fees (CNFs) are payments made by PNFCs because of competitive advantages they enjoy as a result of public sector ownership. From a financial reporting perspective, CNFs enable these entities to be better assessed on their true financial performance and position, had such benefits not been made available to them.

Figure 3L shows competitive neutrality fees paid by PNFCs when compared to profit after tax.

Figure 3L
CNFs as a percentage of profit after tax

Entity	CNF ($ m)	Profit after tax ($ m)	CNF as a percentage of profit after tax (%)
GAWB	15.6	29.8	52
Seqwater	72.6	247.8 *	29
SunWater	11.2	147.6	8
Total for the sector	**99.4**	**425.2**	**23**

* Only includes the profits after tax of Seqwater between 2009–10 and 2012–13 as CNFs were no longer paid to the government after that year.

Source: Queensland Audit Office

CNFs paid by Seqwater and GAWB have had a material impact on their overall profit after tax. The payment of CNFs has also affected the profits after tax of SunWater to a lesser extent.

Seqwater paid competitive neutrality fees of $72.6 million between 1 July 2009 and 31 December 2012 because of arrangements in place with the state government prior to its amalgamation with other bulk water entities on 1 January 2013.

GAWB paid $15.6 million and SunWater paid $11.2 million in the five years to 30 June 2014 because of their access to favourable interest rates. MIWB did not pay competitive neutrality fees to the state government in the past five years.

Income tax expense and credits

Section 24AM of the *Income Tax Assessment Act 1936* (ITAA 1936) states that income of a state body is exempt from income tax unless it is an excluded state body. Section 24AV(1) of the ITAA 1936 then enables state government jurisdictions to decide on its list of excluded state bodies.

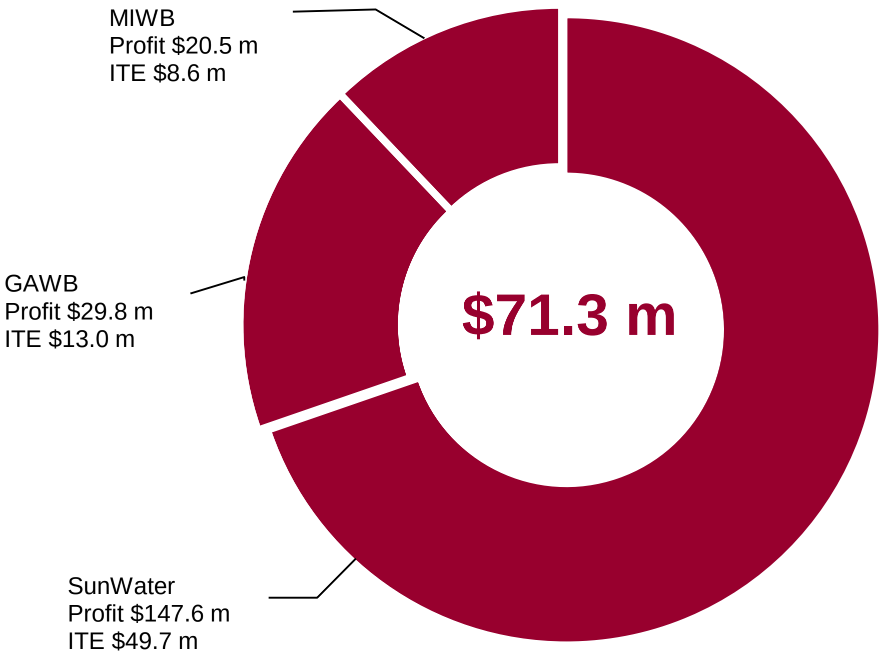
Queensland's four water sector PNFCs are required to account for and pay income tax to the state government, not the Australian Government, under the national tax equivalents regime.

SunWater, GAWB and MIWB have recorded net income tax expenses of $71.3 million over the past five years. The current applicable income tax rates have been set at 30 per cent but the actual rate of income tax paid by these three PNFCs will depend on the way taxation laws are applied.

By contrast, Seqwater recorded income tax credits of $885.5 million between 2011–12 and 2013–14. Income tax credits do not result in cash flows from the government but offset future income tax payments when a profit is eventually made.

Figure 3M compares the income tax expensed by each PNFC except Seqwater which recorded large net income tax credits over the past five years.

Figure 3M
Income tax as a comparison of profits after tax over the past five years



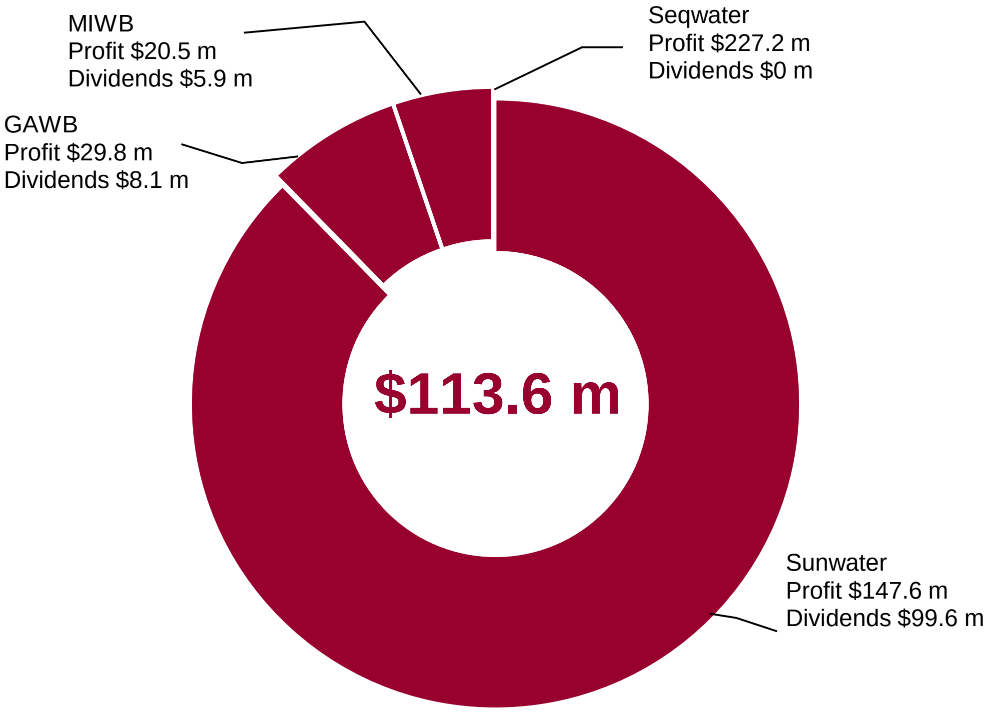
Source: Queensland Audit Office

Dividends

PNFCs paid $113.6 million in dividends to the state government over the past five years. Dividends paid averaged 67 per cent of SunWater's profit after tax; 27 per cent of GAWB's profit after tax; and 29 per cent of MIWB's profit after tax over the past five years.

Figure 3N provides a breakdown of dividends each PNFC paid over the past five years.

Figure 3N
Dividends declared by each entity over the past five years



Source: Queensland Audit Office

SunWater contributed to 88 per cent of total dividends declared by PNFCs in this chapter over the past five years. SunWater's profits are predominately earned through the supply of water from its dam and pipeline infrastructure to its customers.

4 Ports sector

In brief

Background

In Queensland, the government owned ports sector serves industry by delivering freight. Queensland has 14 busy trading ports, two community ports, and three smaller gazetted ports.

There were 279 million tonnes of goods and commodities transported through the state's ports in 2013–14, almost 12 per cent more than the previous year.

The 2013 Queensland Commission of Audit report recommended offering two of the larger government owned ports corporations for long term lease by private investors.

This chapter details the results of our 2013–14 audit of the four government owned ports corporations: Gladstone Ports Corporation Limited (GPCL), North Queensland Bulk Ports Corporation Limited (NQBP), Port of Townsville Limited (PoTL) and Far North Queensland Ports Corporation Limited (trading as Ports North).

Conclusions

We audited the financial reports of all ports entities by their statutory deadline and each received unqualified opinions.

Using pro formas would minimise ports' delays in presenting draft financial statements to audit and enable early agreement of account balances and note disclosures.

Ports continue to be financially sustainable, returning positive operating ratio results. The sector has achieved after tax profits of nearly $1 billion over the five-year period to 2013–14.

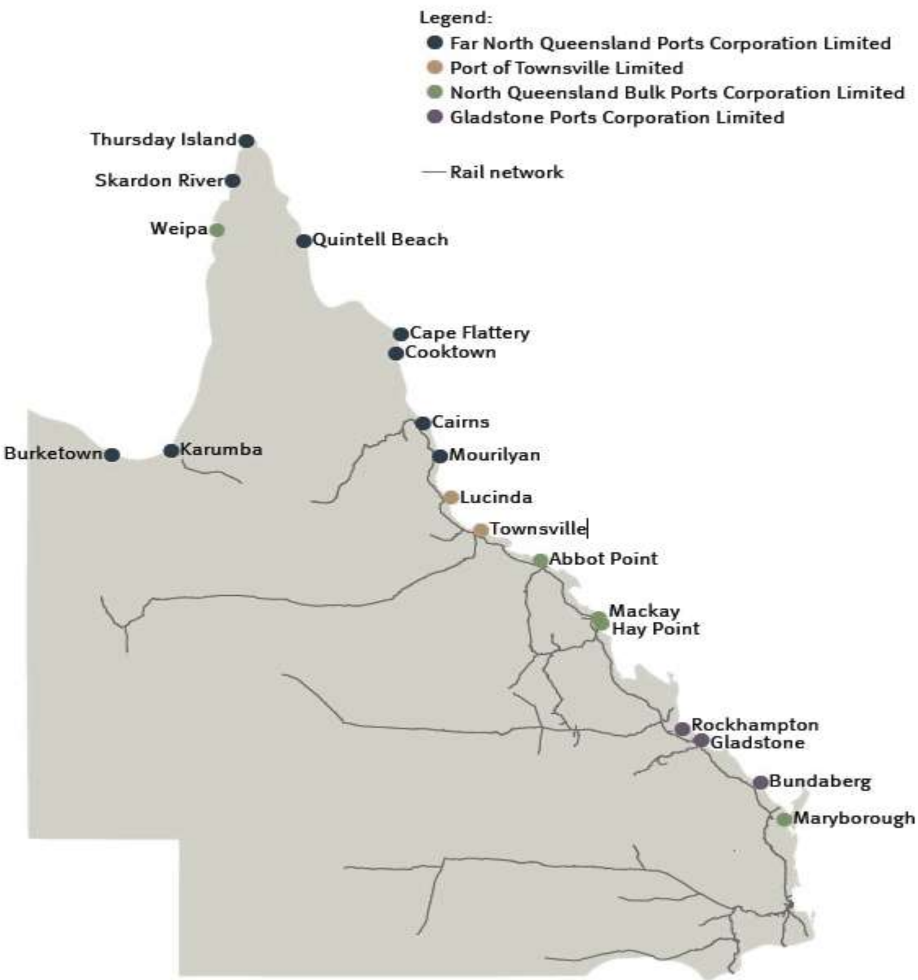
Key findings

- The audits of all PNFCs within the ports sector met their legislative deadlines. Some ports could improve quality further by introducing pro forma statements and early close considerations.
- Results in operating and debt to revenue ratios are good. Ports expect coal exports will continue to rise, with good levels of sales revenue expected to continue with Asia and India.
- Ports are currently achieving positive results in asset renewal, and there is no evidence of issues affecting the ability of ports to continue to replenish assets faster than they are depreciated. Ports assets are characterised by long lives and asset replenishment will be at risk for ports assets, if declining trends in capital investment continue for an extended period of the lives of these assets.
- Ports held $3.8 billion in borrowings or 36 per cent of net assets, which is comparatively low when compared to the energy sector. Most ports hold borrowings with Queensland Treasury Corporation (QTC) through non-current unsecured loans. QTC continues to apply competitive neutrality fees to represent the true stand alone cost of the debt.
- Ports have experienced significant cost write offs and impairment of assets under construction over the last five years, largely relating to discontinued projects and changes in project scope and timing.

4.1 Background

The Queensland ports sector comprises 19 ports (as Figure 4A shows) situated along the coastline of the state and varying from small sized community ports to larger coal export terminals. Ports activities include cargo handling and infrastructure, as well as maritime and pilotage services.

Figure 4A
State owned ports map



Source: Trade Statistics for Queensland Ports 2012–13 of Transport and Main Roads

The Department of Transport and Main Roads oversees four government-owned public non-financial corporations (PNFCs) managing the state's ports, as Figure 4B shows.

Figure 4B
State owned port corporations

Entity
Far North Queensland Ports Corporation Limited (trading as Ports North)
Gladstone Ports Corporation Limited (GPCL)
North Queensland Bulk Ports Corporation Limited (NQBP)
Port of Townsville Limited (PoTL)

Source: Queensland Audit Office

4.1.1 Activities of state government ports

State government ports operate under the *Government Owned Corporations Act 1993*. Each entity is required to operate on a commercial basis, establishing an independent board.

As Figure 4C shows, port operations can be grouped into three categories, referenced in the Queensland Commission of Audit report:

- high volume commercial—financially viable to operate as a stand alone facility
- low volume commercial—whilst expected to generate positive returns, these are not considered to be sufficient for the entity to operate on a stand alone basis
- non-commercial—normally non-trading or not expected to generate a positive return.

Figure 4C
Classification of port facilities

High volume commercial	Low volume commercial	Non-commercial
Port of Gladstone	Port of Cairns	Port of Bundaberg
Port of Townsville	Port of Mackay	Thursday Island
Port of Hay Point *	Port of Lucinda	Quintell Beach
Port of Abbot Point	Port Alma (Rockhampton)	Port of Maryborough
Port of Weipa	Mourilyan	Port of Cooktown
	Cape Flattery	Port of Burketown
	Karumba Port	
	Skardon River Port	

* NQBP manages port operations at Hay point terminal

Source: Queensland Commission of Audit

Figure 4D outlines the individual ports for which each port entity is responsible, including the key commodities transported through each facility.

Figure 4D
Port operations across the state

Entity	Ports
Ports North	Responsible for the ports of Cairns, Burketown, Cape Flattery, Cooktown, Karumba, Mourilyan, Port Kennedy (Thursday Island), Quintell Beach and Skardon River. These ports transport a diverse range of freight including agriculture, mining, tourism, sugar and fisheries. Also manages the Cairns cruise ship terminal.
GPCL	Responsible for the ports of Gladstone, Rockhampton (Port Alma) and Bundaberg. The port of Gladstone represents the state's largest multi-commodity port and exports to more than 30 different countries. Major exports include coal and alumina, while bauxite is the major imported commodity. Port of Bundaberg is used to export of sugar and molasses.
NQBP	Responsible for the ports of Abbot Point, Hay Point, Weipa, Mackay and Maryborough. Operates one of the largest coal terminals in the world at Hay Point, comprising two separate coal export terminals: the Dalrymple Bay Coal Terminal (DBCT) and the Hay Point Services Coal Terminal (HPSCT). Manages one of Australia's most northern coal terminals at Abbot Point, and exported a record 23 million tonnes of coal in 2013–14. The Port of Mackay exports a variety of products including sugar, molasses and grain, while its imports include petroleum and break bulk cargo. The Port of Weipa's main export is bauxite.
PoTL	Responsible for the ports of Townsville and Lucinda. The port of Townsville specialises in nickel ore, petroleum, oil, fertiliser and general cargo. The port recently completed a multi-million dollar berth upgrade and constructed Townsville's first cruise terminal, becoming operational in 2013-14. Lucinda is a dedicated port for the Ingham sugar industry.

Source: Queensland Audit Office

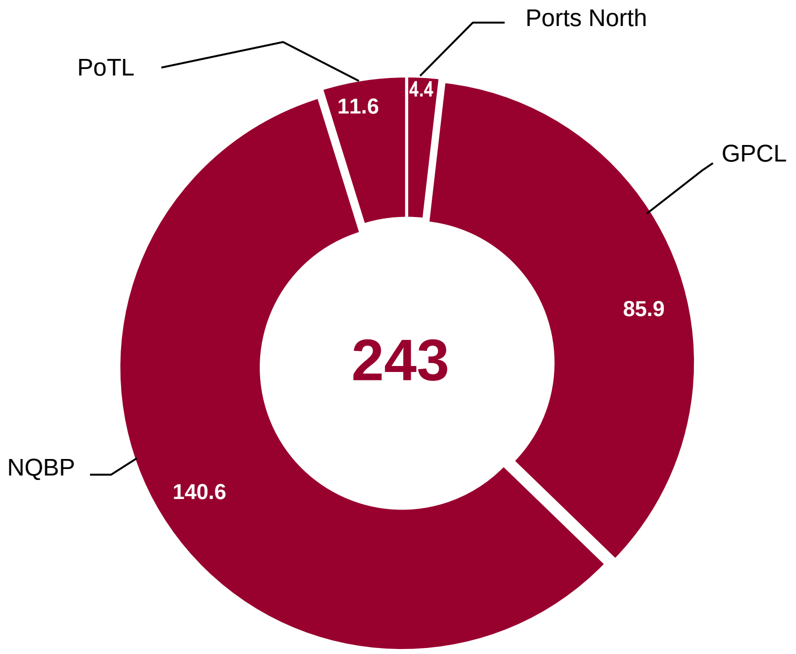
4.1.2 Commodities transported through the state's ports

The volume of freight moved throughout the state of Queensland has grown substantially over the past 25 years. Export volumes have increased almost five fold and import volumes have doubled.

Freight can be categorised as general freight or commodities moved in bulk. General freight comprises single items or grouped configurations; for example, wholesale/retail items, manufacture and building products. Commodities moved in bulk involve only single commodities such as sugar, coal, and grain.

As Figure 4E shows, Queensland's ports corporations transported around 243 million tonnes of freight each year over the past five years. Of this, NQBP and GPCL moved 226.5 million tonnes of commodities, or 93 per cent of all cargo travelling through Queensland government owned ports.

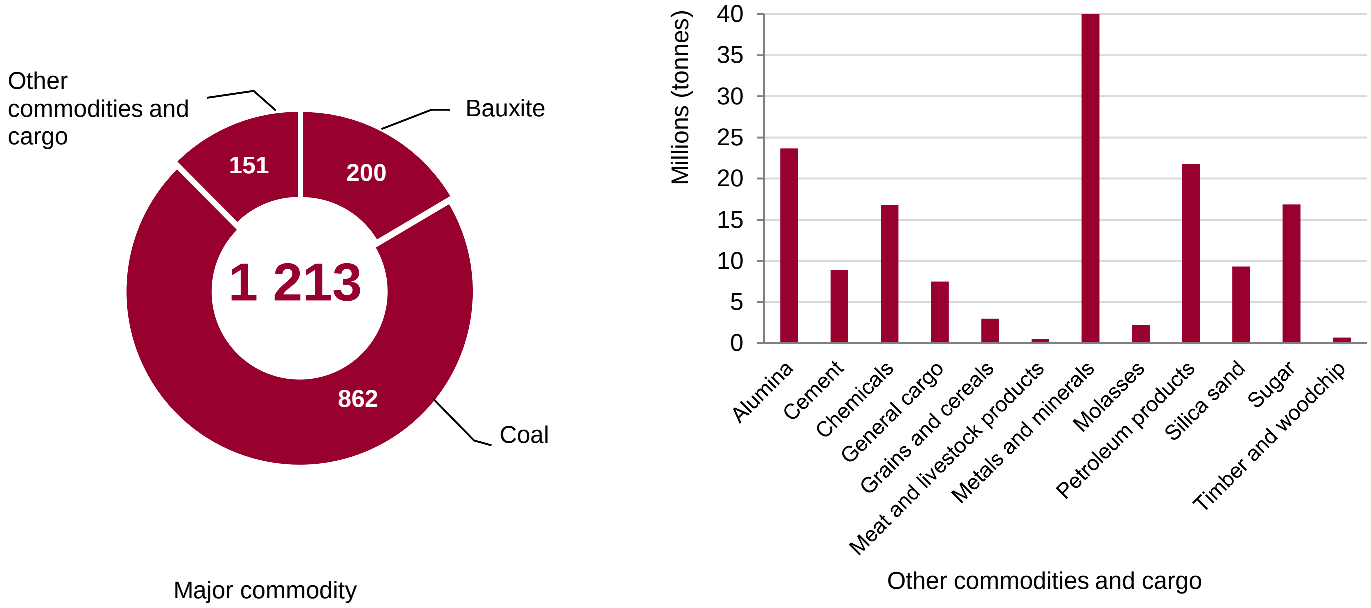
Figure 4E
Average yearly throughput (million tonnes) by ports corporations 2009–10 to 2013–14



Source: Department of Transport and Main Roads

Figure 4F shows a five-year summary of the major commodity groups Queensland Government owned ports transported. Ports transported 1 213 million tonnes of major commodities and cargo in the last five years—mostly coal (862 million tonnes or more than 70 per cent of all ports throughput) and bauxite (200 million tonnes or more than 16 per cent of all ports throughput). The category of 'other commodities and cargo' represents 151 million tonnes or 12 per cent of total throughput, of which ports transported 40 million tonnes of metals and minerals.

Figure 4F
Total throughput (million tonnes) for all ports 2009–10 to 2013–14

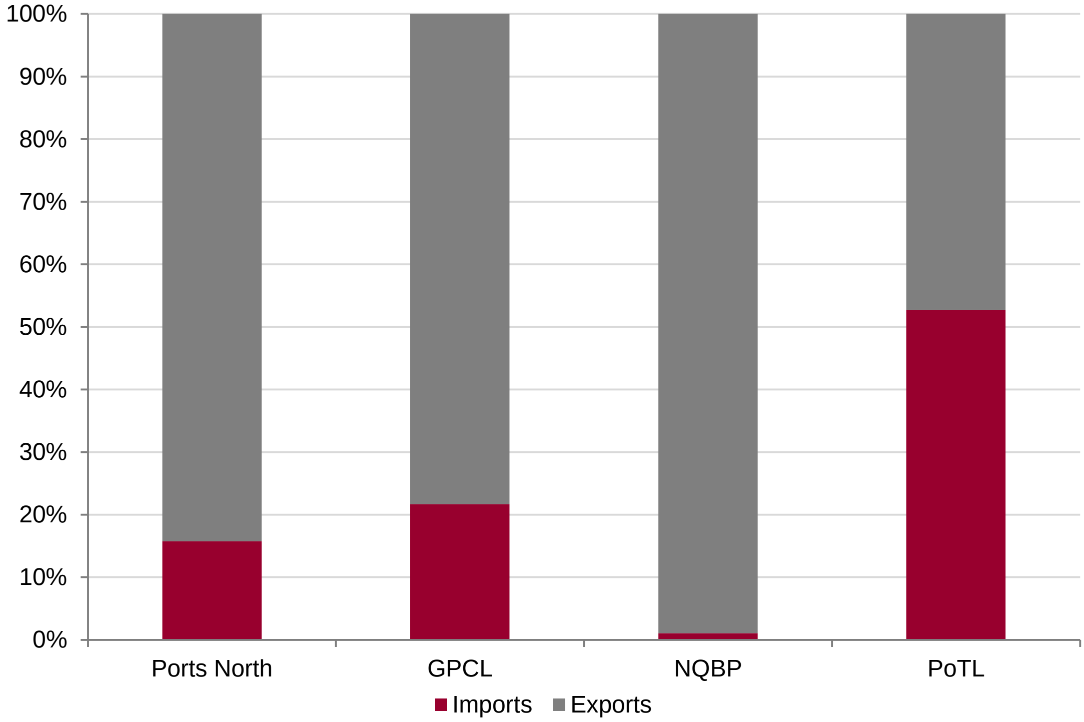


Source: Department of Transport and Main Roads

Imports and exports

Figure 4G illustrates the import/export profile of each of the ports over the last five years. Exports make up 88.9 per cent of total throughput while the volume of imports has consistently ranged between 10 per cent and 12 per cent of the total volume of goods transported.

Figure 4G
Commodity and cargo imports vs exports average across 2009–10 to 2013–14



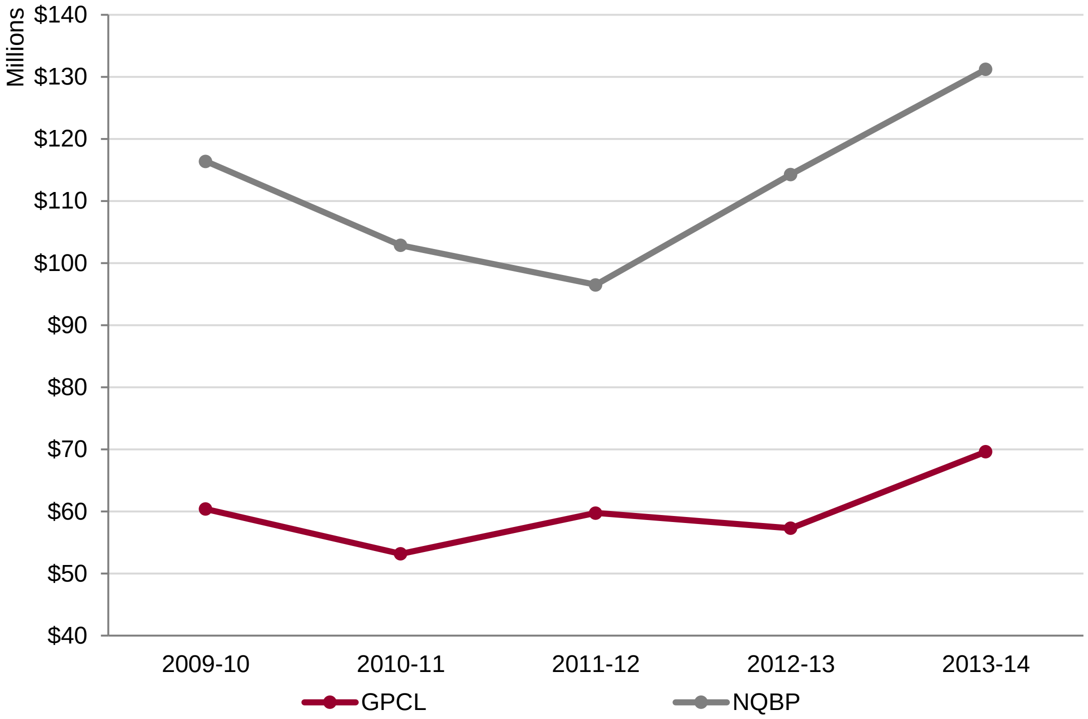
Source: Queensland Audit Office

Queensland largest export volume is in coal (over 62 per cent of the state's total exports), followed by bauxite exports.

Gladstone and Townsville ports process most imports, primarily bauxite, caustic soda, nickel ore and petroleum products. Queensland's large import volume is in bauxite, used for alumina production in Gladstone.

The success of the ports industry relies on the state's economic activity; this can be driven by world markets. Historically, coal export movements fluctuate, as Figure 4H shows.

Figure 4H
Five-year movement in coal exports through GPCL and NQBP



Source: Department of Transport and Main Roads

Although recent economic developments, including BMA's termination of 700 mining jobs in the Bowen Basin, have increased uncertainty around the growth of coal exports, the Treasurer's 2014–15 State Budget identified that, due to increased activity in China, coal exports grew substantially during 2013–14 and are expected to continue rising in 2014–15.

4.1.3 Changes to PNFCs in the public sector

The 2013 Queensland Commission of Audit report recommended the commercial operations of Gladstone Ports Corporation and Port of Townsville Limited (integrated with Mount Isa Line) be offered for lease to private operators. On 3 June, 2014, the Queensland Treasurer announced in the Draft Plan of action, "Strongest and Smartest Choice," with the State Budget that Gladstone Ports Corporation and Port of Townsville Limited (integrated with Mount Isa Line) were being considered for lease.

Further details and the terms of proposed arrangements are not known at this stage. We did not require adjustments to year-end balances due to the various proposals to sell or lease assets that were canvassed during and after the financial year.

4.1.4 Entities covered in this chapter

This chapter includes the results of our audit of PNFCs in the ports sector. Ports classified as PNFCs include GPCL, NQBP, PoTL and Ports North.

4.2 Conclusions

We issued an unqualified opinion for the financial statements of all four port entities. An unqualified audit opinion of a financial report means that the report complies with relevant Australian accounting standards and prescribed requirements.

Only two ports have controlled entities. NQBP controls the Ports Corporation of Queensland and Mackay Ports Limited, both dormant companies that do not trade. GPCL controls Gladstone Marine Pilot Service Pty Ltd and Gladstone WICET Operations Pty Ltd which are consolidated into GPCL's financial report.

None of the draft financial reports the ports provided met the agreed milestone. Three of the four ports provided an incomplete first draft, further delaying the process. First draft omissions included material note disclosures such as property, plant and equipment, investments, taxation, dividends and the statement of cash flows.

When forming an opinion on the financial report of an entity, we assess its ability to continue as a going concern by measuring its ability to pay ongoing expenses; replace and grow assets; and pay debts as and when they fall due. These factors indicate an entity's financial sustainability.

Each of the ports is performing well and is sustainable. There are no significant financial risks or uncertainties affecting their ability to continue operations in the future. The sector has achieved after tax profits of nearly $1 billion over the five-year period to 2013–14, with each port returning a positive operating result over the same period.

Results of capital replenishment ratios demonstrate each of the ports has achieved a positive financial position, meaning each entity is replacing its assets in a reasonable amount of time before assets are fully depreciated. Ports are currently returning ratios greater than one, and there are no indicators to suggest that port assets are not being replaced faster than they are depreciated. Although port assets are characterised by long lives, declining trends identified will pose a risk to asset replenishment if they continue into the medium term

Debt to revenue ratio calculations indicate that, over the last five years, the ports sector has been able to earn sufficient revenue to cover its debt commitments.

Figure 4I summarises the factors affecting the financial sustainability of the ports sector.

Figure 4I
Financial performance, position and sustainability of ports sector

Component	Description
Financial performance	Over the past five years, all ports collectively achieved net profits after tax of $983.9 million. User charges continue to dominate source revenue for each of the ports. With coal exports predicted to rise, it is expected that operating revenue will continue to increase in the future in spite of some uncertainty in the sector.
Financial position	The financial position for each of the ports remains positive, with only a small negative reported in the capital replenishment ratio calculated on GPCL for the 2011–12 financial year. The capital replenishment calculation does not include the proceeds from the Abbot Point Coal Terminal long term lease arrangement, received for the disposal of assets, so the results for that year do not incorrectly skew the results and report a negative financial position for the port. Borrowings are conservatively low across the ports sector compared to other PNFC sectors and ports earn sufficient revenue to meet debt commitments.
Financial sustainability	Each port continues to be financially sustainable, each returning positive operating results, demonstrating capital replenishment greater than one and earning sufficient revenue to meet debt commitments.

Source: Queensland Audit Office

4.3 Audit opinions

We issued unqualified audit opinions for all four ports, as we did in 2012–13; each port continues to prepare financial reports that comply with the requirements of relevant accounting standards, and legislative requirements. The audit opinions we issued provide assurance that each port has prepared financial reports that are reliable and present a true and fair view. Figure 4J provides further detail on the key milestones in the audit opinions we issued for ports entities in 2013–14.

Figure 4J
2013–14 audit opinions issued

Audit	Draft financial report provided for audit	Financial statements signed	Opinion issued	Certified by deadline	Opinion
Government owned corporation					
Ports North	13.08.2014	27.08.2014	28.08.2014	Yes	Unqualified
GPCL	13.08.2014	28.08.2014	29.08.2014	Yes	Unqualified
NQBP	20.08.2014	26.08.2014	29.08.2014	Yes	Unqualified
PoTL	29.07.2014	26.08.2014	26.08.2014	Yes	Unqualified

Source: Queensland Audit Office

4.4 Timeliness and quality of financial reports

4.4.1 Timeliness

To show accountability for the use of public monies, entities should prepare and publish their financial information as soon as possible after the end of the financial year. The later financial reports are produced and published after their balance date, the less useful they are for stakeholders and for informed decision making.

Draft financial reports provided for audit

Although each port agreed to provide final draft financial reports to us on an agreed date, all four ports corporations missed the agreed milestone, averaging a delay of 11 days. Ports North, GPCL and NQBP provided incomplete versions of the final draft financial report; for reasons that included: note disclosures such as property, plant, and equipment, investments, taxation, dividends and the statement of cash flows were yet to be finalised.

The agreed financial statement timetable with NQBP included the provision of a draft financial report without a completed statement of cash flows. Although NQBP met this milestone, the first complete set of financial statements provided to QAO was due on 5 August 2014 and we did not receive this until 20 August 2014.The main reason that NQBP was the only port to provide a near complete draft financial report by the due date, was its preparation of pro forma financial report. This helped management and audit discuss and agree early on accounting treatments, disclosures and appropriate action for significant issues identified before 30 June.

Entities prepare pro forma reports to assess accounting policy note disclosures and presentation of the financial report for quality, reliability and compliance with accounting standards before providing the year-end financial report to audit. Ports North, GPCL and PoTL did not provide us with pro forma accounts. These ports should consider preparing pro forma financial statements for 2014–15 to improve the timeliness of the process.

Certification of financial reports by legislative deadline

As government owned corporations, the ports are required by legislation to have their financial statements certified by 31 August.

We certified each of the ports' financial reports certified within the legislative time frame, but GPCL risked missing this milestone by making a late change in the technique it used to value its physical assets.

4.4.2 Quality and accuracy

We found the quality of the draft financial report and supporting work papers provided was satisfactory. We required some disclosure changes and material account balance adjustments to the draft financial reports.

Early closes

None of the four ports undertook early closes as part of the 2013–14 audit process.

An early close occurs when management prepares a financial report for audit before the end of the financial year. Early closes resolve financial reporting issues early and minimise the volume of changes required to the financial report at year-end. This approach encourages management and audit to consider the effects of issues well before the final audit so decisions are not rushed and both parties consider accounting treatments well. Early closes help meet the legislative time frame.

Port entities should consider implementing an early close process for 2014–15 to improve the quality and accuracy of the financial report, while satisfying legislative time frames.

Material financial report adjustments

Two of the four entities did not require any material management or audit initiated adjustments to their draft financial reports. PoTL and GPCL required material adjustments.

Material adjustments included amending late client journals for asset revaluation, impairment and taxation adjustments. PoTL made one material adjustment, writing back fully depreciated assets subject to obsolescence in the amount of $15.3 million. GPCL made multiple changes, amounting to $407 million, with the most significant being a channel asset revaluation adjustment of $281 million.

In aggregate, the client and audit initiated material adjustments made for the ports sector totalled $422.3 million.

Disclosure adjustments

We identified disclosure issues across ports in applying the new Australian Accounting Standard AASB 13 *Fair Value Measurement.*

These comprised:

- limited disclosure of key assumptions in property, plant and equipment asset valuation methodologies
- incomplete documentation of highest and best use considerations
- unspecified amounts in Level 1, 2 and 3 disclosures.

Across the four ports, we recommended changes to disclosures to improve the quality of writing and ease of understanding of the financial report.

Prior period errors

NQBP reported a prior period error in its 2013–14 financial report. The error related to the tax treatment adopted on acquisition of Ports Corporation of Queensland Limited and Mackay Ports Limited (subsidiaries of NQBP) in 2009. At the time, NQBP deleted deferred income tax equivalent assets associated with unrealised (tax) capital losses for specified property, plant and equipment, due to uncertainty over realising losses in the future. NQBP has determined that it is now probable that these losses will be realised and this conclusion could have been reached in prior years. The financial effect of correcting the error was to decrease deferred income tax equivalent liabilities by $22 million and increase retained earnings by the same amount.

4.5 Significant financial reporting issues

4.5.1 Effect of new accounting standards

A new Australian Accounting Standard AASB 13 *Fair Value Measurement* addresses inconsistencies in applying fair value methodologies to value and report assets in financial statements. The new standard focuses on the exit price (the price to sell the asset) when determining the asset's value and considers its 'highest and best use'. Calculating the asset's fair value relies on understanding its potential uses.

When determining the fair value of an asset or liability under AASB 13, entities must consider:

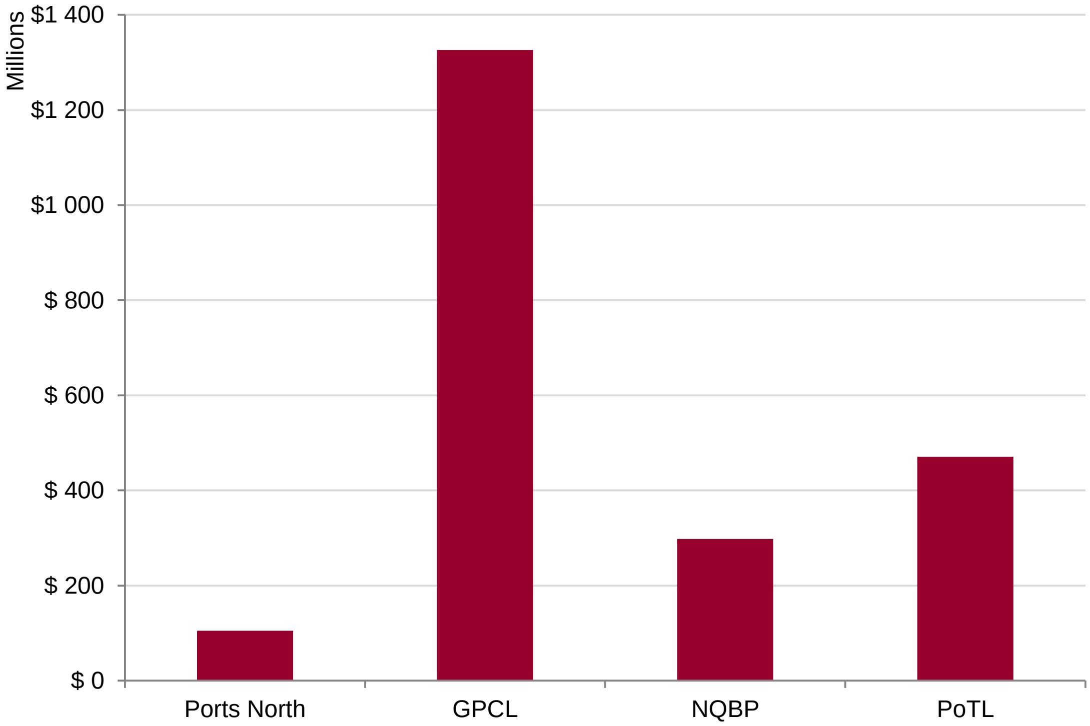
- the condition and location of the asset
- restrictions, if any, on the sale or use of the asset.

These aspects may influence the price a market participant is willing to pay.

Without evidence of better uses of an asset, the valuation methodology or fair value reported in most entities' financial statements are unlikely to change.

Figure 4K shows the reported values for property, plant and equipment of ports entities as at 30 June 2014.

Figure 4K
Total fair value of property, plant and equipment as at 30 June 2014



Source: Queensland Audit Office

Applying AASB 13 did not directly alter the reported values in 2013–14, but GPCL did change its valuation technique to estimate fair value for its port infrastructure assets. GPCL adopted the income based approach to value its port infrastructure, recognising the strong relationship between the revenue earned from certain groups of assets.

Implementing AASB 13 affected all ports, applying new level of disclosures for key valuation assumptions and estimates to calculate fair value. There is still room to improve existing disclosures:

- support estimates and assumptions applied to fair value assessment by calculations and external documentation
- demonstrate the current use of assets' values equate to highest and best use
- increase detail to support valuer assumptions and conclusions
- provide sufficient commentary on significant weather events and the effects on the condition of assets.

4.5.2 Asset valuation methodologies

Under AASB 116, port corporations can measure their property, plant and equipment assets using the cost or revaluation model. In 2013–14, ports valued their physical assets under the revaluation model to estimate fair value.

There are three common measurement techniques available under AASB 13 to estimate fair value:

- market value
- depreciated replacement cost
- income based approach.

The newly introduced AASB 13 requires the owner to assess the 'highest and best use' for the asset, from the perspective of the owner and of other market participants. The owner uses a valuation technique that reflects the characteristics and assumptions of the asset(s) and relevant observable and unobservable inputs. Even when external parties determine fair values, entities must assess if fair value has been determined correctly and if the methodology applied is reasonable, relevant and complete.

Figure 4L shows the methods the four ports used to estimate the fair value of their property, plant and equipment assets, following the cost or revaluation approach. AASB 116 *Property, Plant and Equipment* allows both valuation methods to estimate fair value, although Ports North and NQBP value their assets using depreciated replacement cost.

Figure 4L
Dominant valuation techniques used to estimate the fair value of property, plant and equipment

Port	Technique used to estimate fair value
Ports North	Depreciated replacement cost
GPCL	Income-based approach
NQBP	Depreciated replacement cost
PoTL	Income-based approach

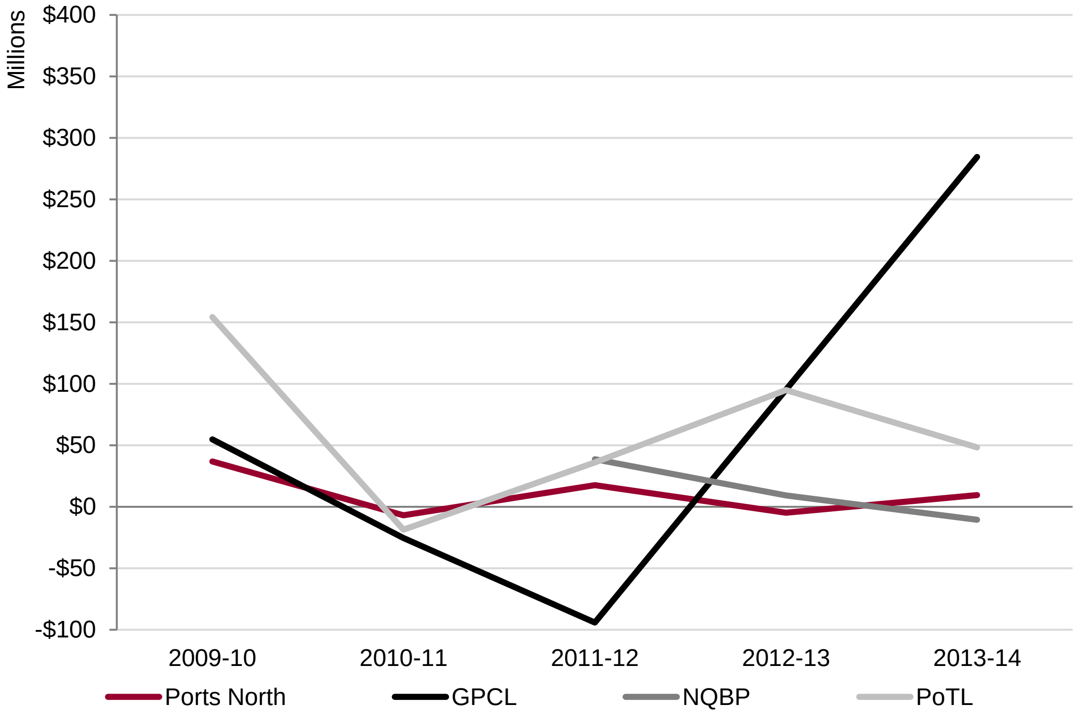
Source: Queensland Audit Office

Depreciated replacement cost reflects the cost to acquire the service potential embodied in an asset, adjusted to reflect the asset’s present condition/physical deterioration, functionality and technological and/or economic obsolescence. Revaluation recognises change in an asset's remaining service potential.

An income-based approach converts future amounts of cash flows or income and expenses to a single current amount, using discounted cash flows. The asset's owner determines the fair value measurement based on the value indicated by current market expectations about those future amounts.

Figure 4M shows the annual movements in the reported fair values of property, plant and equipment for all ports over the last five years.

Figure 4M
Annual movements in the reported value of property, plant and equipment—all ports over five years



Source: Queensland Audit Office

To avoid a distortion in Figure 4M we have excluded the movement in the value of NQBP's assets between 1 July 2009 and 30 June 2011 due to the significance of the value of the Abbot Point Terminal 1 asset that was sold under a 99-year lease). Movements in the reported values of property, plant and equipment arise from asset acquisitions, disposals, revaluations, depreciation and impairment. Significant fluctuations in asset revaluations arose where GPCL and PoTL changed valuation methodologies from depreciated replacement cost to income-based and in the year when NQBP performed a comprehensive valuation exercise.

Movements resulting from comprehensive valuations performed

In 2011–12, NQBP conducted a comprehensive exercise to value its channels, infrastructure and major plant and equipment asset classes, using the depreciated replacement cost technique. This increased reported values by $32 million: an uplift in depreciated replacement costs of $199 million reduced by $167 million in discounted cash flows that did not support the uplift.

In the same year, Ports North recorded an asset revaluation increment of $32 million, representing 35 per cent of the reported fair value at the beginning of the year.

When asset values are assessed, using depreciated replacement costs, up to five years apart, the volatility in movements of fair value of assets risks reducing the comparability of financial results from year to year.

Movements resulting from change in valuation methodology

AASB 116 *Property, Plant and Equipment* allows both income and depreciated replacement cost approaches to estimate fair value, and agencies must consider which method is most appropriate to their business.

When PoTL and GPCL changed their revaluation technique, from depreciated replacement cost to an income-based approach in 2011 and 2014 respectively, both entities reported material net revaluation increments of between 25 and 27 per cent in the year of making the change. This reflects the net revenue earned on those assets rather than the cost of replacing those assets.

Ports should adopt a valuation technique that best estimates the price to sell the asset under current market conditions. The income-based approach will generally be more relevant to assets where highest and best use is primarily dependent on their ability to generate cash inflows in a commercial environment. Depreciated replacement cost is typically suited to not for profit entities.

We recommended that Ports North and NQBP consider available valuation techniques. If they continue using depreciated replacement cost, there is scope for improvement in the quality and timing of valuation processes.

4.5.3 Impairment of assets under construction

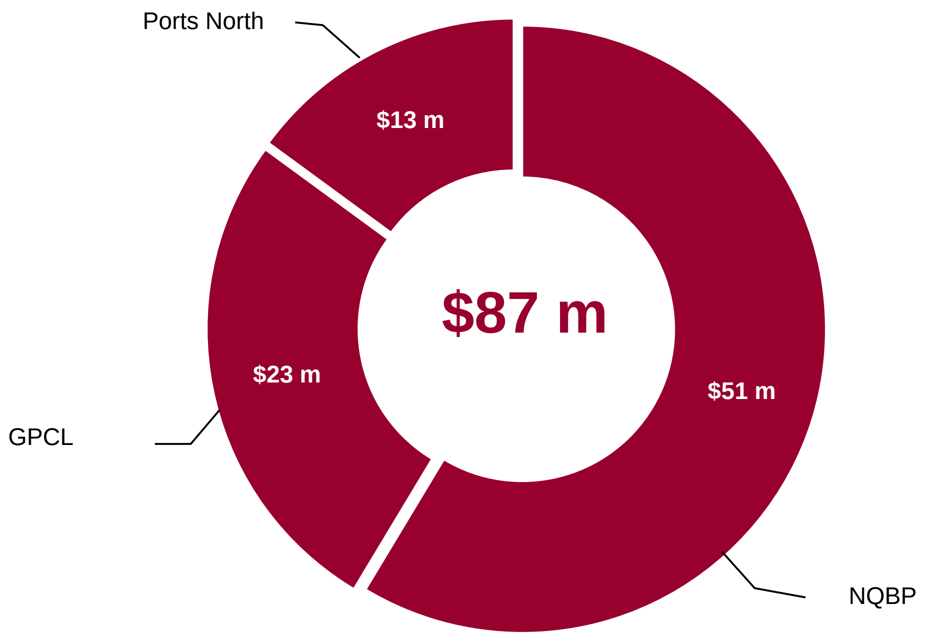
An asset is impaired when its market value or expected cash flows are less than the value reported on the entity’s balance sheet, resulting in a write down of the asset or asset class.

Government owned ports have incurred financial losses of nearly $40 million in the value of assets under construction in 2013–14. Ports asset write downs relate to discontinued projects, or changes in projects' scope and timing. Ports also expense community projects that do not generate a revenue stream (and which are thus not a port asset).

Ports can capitalise costs likely to contribute towards an asset's future economic benefits and meet the 'asset' definition. Ports expense costs arising from decisions to discontinue capital projects or where revenue does not support an asset's value. This results in in significant write downs and decreases ports' operating result.

Figure 4N shows ports have written off project costs of nearly $87 million over the past five years, with only Ports North, GPCL and NQBP reporting write-offs of project costs during this period This has reduced overall port sector profits by nine per cent and reduced dividends to government by $49 million.

Figure 4N
Value of assets under construction written off or impaired over the last five years—all ports



Source: Queensland Audit Office

GPCL impaired its Eastshores project to redevelop a waterpark recreational area that did not generate any income for the port. The impairment resulted in financial losses of just under $27 million incurred since the project's inception.

NQBP's most significant write down of assets under construction related to a multi-cargo facility deemed unsustainable, given a downturn in the mining industry and customer demand. As a result, NQBP wrote off cumulative project costs of $29 million.

The write down of assets under construction for these two projects alone represents 64 per cent of total write downs for the ports sector over the last five years.

4.5.4 Costs of dredging

Managing the state's ports involves continual dredging to manage sediment stirred by port traffic and water currents and so waterways are deep enough for safe mooring.

The four port corporations have spent $160.6 million in dredging activities over the past five years; that excludes the fee for service revenue and expenses for dredging GPCL undertook on the Western Basin for liquid natural gas proponents. Ports have expensed nearly half of all dredging costs in this five-year period. Such costs are not assets as they will not provide an economic benefit to a port for a period beyond one year.

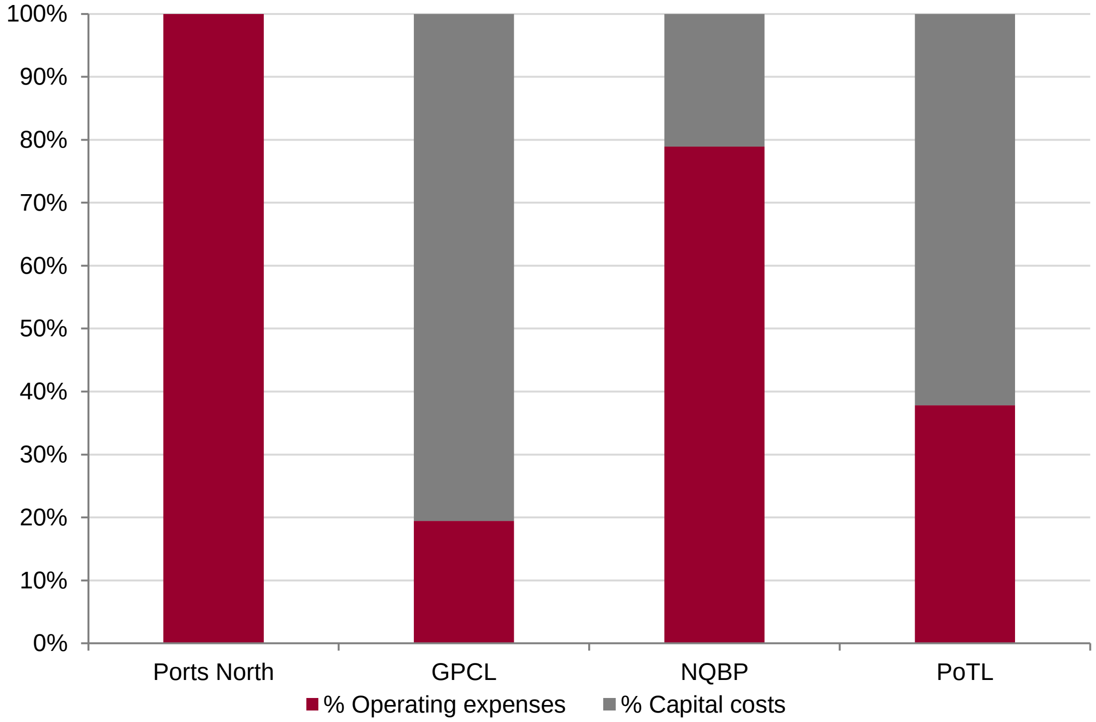
The costs of dredging can have one of two financial outcomes. Where costs are incurred to restore the channel to its original condition, or perform routine maintenance, these costs are normally classified as operating expenses. Conversely, dredging costs that are incurred to widen or deepen existing channels and harbours beyond their original condition, are generally capitalised. Whilst the frequency of dredging can impact if costs are capitalised, the determining factor should be if the nature of the dredging activity meets the recognition criteria of an asset.

Ultimately, assessing dredging costs as capital costs must satisfy Australian accounting standards:

- the agency must control the asset
- there was a past transaction or event which gave rise to the control
- future economic benefits must be expected to flow to the agency.

Often a subjective assessment, the basis to capitalise or expense dredging costs may be applied differently across the port sector, and is heavily influenced by the unique nature of each entity. The is demonstrated in Figure 4O where over the last five years each port has recognised a different proportion of capital versus non-capital dredging costs.

Figure 4O
Proportion of capital to non-capital dredging costs over the last five years



Source: Queensland Audit Office

Ports North has not capitalised any dredging costs in the last five years and undertook its last major dredging project to improve channels in 1990. Over the same period, NQBP capitalised dredging costs for channel improvements at Weipa in 2012–13; however, in 2013–14, it classified all dredging costs as maintenance expenses, whereas PoTL only capitalised dredging costs in 2012-13, expensing in other years. GPCL has expensed dredging costs over the last five years, capitalising from 2011-12, with the majority of costs capitalised in 2012-13.

Not inferring that one approach is more correct than the others, and recognising that the nature of activities at each port is a key point of difference, the graph highlights the importance of ensuring well-documented, formal policies are in place to provide clarity, consistency and greater awareness of what correctly constitutes and distinguishes between capital and operational expenditure. Clear and adequate guidance for classifying dredging costs can alleviate complex accounting issues, and mitigate the risk of inaccurate financial reporting.

4.6 Financial performance, position and sustainability

Figure 4P details some of the significant account balances affecting the financial performance and position of ports.

Figure 4P
Financial Performance and Position

Account	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Factors affecting financial performance					
Revenue	601.2	1 133.6	1 038.5	1 097.8	921.2
Expenses	453.3	652.8	910.4	920.3	707.2
Income tax	41.9	(41.8)	49.2	52.9	62.2
Profit after tax	106.0	522.6	78.9	124.6	151.8
Factors affecting financial position					
Assets	3 963.4	4 754.2	3 009.8	3 072.2	3 278.7
Liabilities	2 000.6	1 554.1	1 279.7	1 271.5	1 228.5
Equity	1 962.8	3 200.1	1 730.1	1 800.7	2 050.2

Source: Queensland Audit Office

4.6.1 Financial performance and position

The financial performance of the ports sector has remained steady over recent years, although the long term lease arrangement of Abbot Point Coal Terminal in 2010–11 caused fluctuations of revenue, expenses, income tax, and profit after tax. This transaction's disposal of assets directly affected each of these components and consequently skewed the results of these elements for that year.

Each of the ports continues to report a positive financial position, well supported by large asset bases. Infrastructure, channel and swing basin assets make up 65 per cent of total property, plant and equipment assets across the sector.

Borrowings represent a key source to fund capital projects. While PoTL has minimal borrowings, Ports North has none, relying mostly on internally generated funds. The borrowings of GPCL and NQBP total $3.8 billion, representing 95 per cent of total borrowings for the sector over the last five years. Both entities—and the sector as a whole—continue to return a positive financial position and can meet debt commitments.

4.6.2 Financial sustainability

Australian accounting standards require an entity to assess its ability to operate as a going concern and prepare its financial statements accordingly. The *Corporations Act 2001* (Cth) requires the directors of a company to make a formal statement of solvency (that the company can pay its debts as and when they fall due). This statement is included in the financial report this legislation requires and on which an audit opinion is expressed.

Assessment of going concern determines the financial sustainability of an entity or a sector. Ratios such as operating, capital replenishment and debt to revenue are critical in making this assessment.

Figure 4Q details a summary of the results of these ratios in financial sustainability for the ports sector.

Figure 4Q
Financial sustainability ratios for ports over the last five years

	2009–10	2010–11	2011–12	2012–13	2013–14
Operating ratio	17.7	46.1	7.6	11.4	16.5
Capital rep ratio	24.6	42.4	12.3	16.2	23.2
Debt to revenue	6.3	4.4	1.1	4.1	1.5

Source: Queensland Audit Office

- All ports have performed satisfactorily over the past five years, each reporting positive ratios. GPCL and Ports North have consistently reported lower ratios than the other port entities. Whilst Ports North has been the only port to report operating losses, this indicated asset impairment in 2010–11 and significant asset write downs in 2011–12, rather than cash depletion issues.
- The capital replenishment ratios of Ports North and NQBP declined, due to reduced asset purchases.
- All ports returned satisfactory debt to revenue results in 2013–14. Ports North has the lowest ratio. NQBP had the least satisfactory ratio in 2010, reporting more than seven times more debt than revenue. This was quickly resolved in the year to 30 June 2011 with the lease arrangement for Abbot Point.

Through these results, we can determine risks to the port's own assessment of going concern. We are satisfied each individual port can demonstrate adequately it is capable of meeting its present and future obligations.

We have identified risks to the financial sustainability of ports:

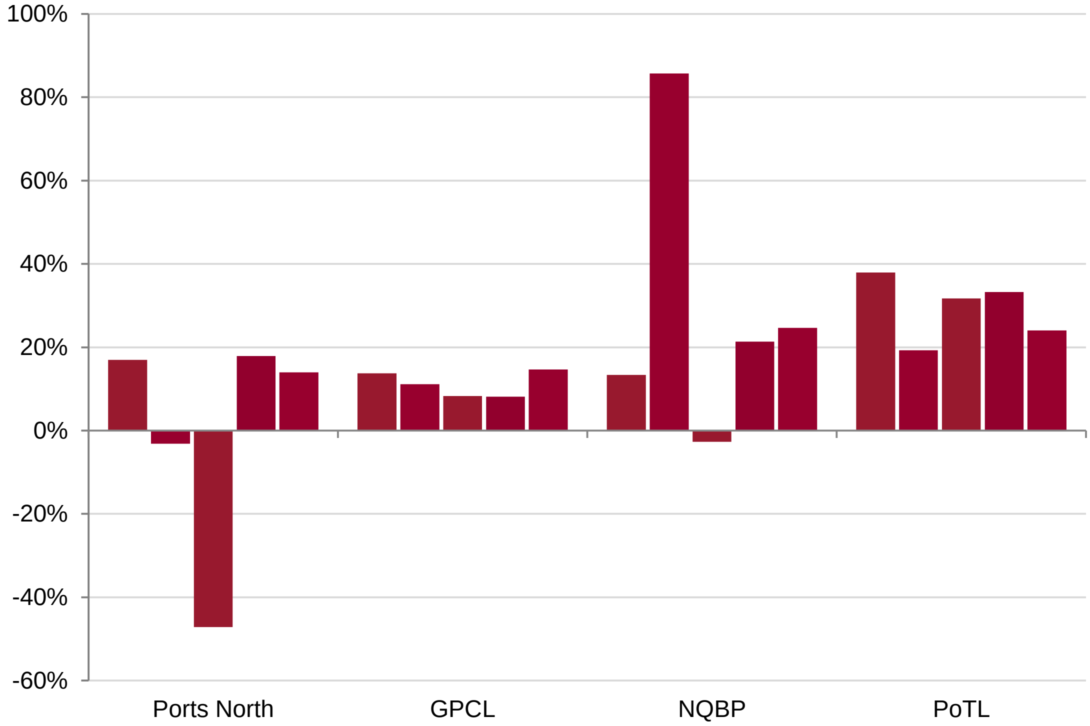
- Ports rely heavily on exports versus imports. Three of four ports export more than they import, with a strong focus on China and India.
- Environmental regulations limit all ports' ability to expand and operate effectively: in particular, to carry out dredging. Obtaining sea dumping permits is increasingly difficult.
- Ports face potential litigation by pressure groups. There is a cost associated with building strong community awareness: in particular, studies identifying the significant threats to the Great Barrier Reef.
- Ports are affected by commodity viability such as liquid natural gas at Gladstone.
- Ports depend heavily on coal markets.
- Mining companies may defer investment projects.

4.6.3 Operating ratio

This ratio is the operating profit before tax, expressed as a proportion of total revenue. It should be positive over the medium to long term for the entity to remain financially sustainable. Ongoing negative ratios indicate net losses, which mean revenue is insufficient to fund operating and future capital expenditure. This in turn depletes cash reserves and/or increases borrowings and may compromise investment in new assets and/or service levels.

Figure 4R shows the operating ratios across the ports entities over the last five years to 2013–14.

Figure 4R
Operating ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

Ports have mostly maintained positive ratios: all report a positive operating position since 2012–13. Over the last five years, ports averaged an operating ratio of 24 per cent.

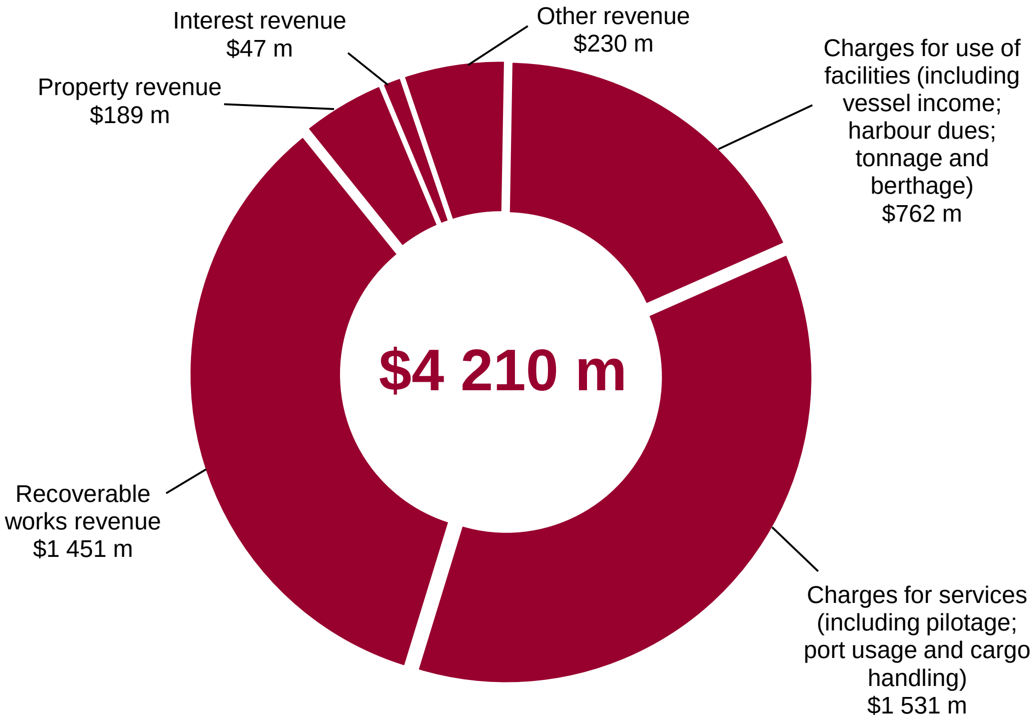
The ratio for both GPCL and NQBP increased since 2012–13, with revenue earnings increasing to meet operating costs. NQBP's significant increase in 2010–11 represents the long term lease arrangement with Abbot Point, whereas the decline in 2011–12 was due to a $22 million impairment of assets under construction.

The negative ratio Ports North reported in 2011–12 indicates a material impairment charge of $17.9 million for the Cairns cruise liner terminal completed in 2010–11 and significant asset write downs, and not early indications of cash management issues in financial sustainability of the port.

Revenue

Figure 4S shows the primary source of revenue for the ports continues to be charges for use of facilities and services, including harbour dues, tonnage rates, pilotage fees, shipping charges and handling charges.

Figure 4S
Composition of ports operating revenues for the last five years

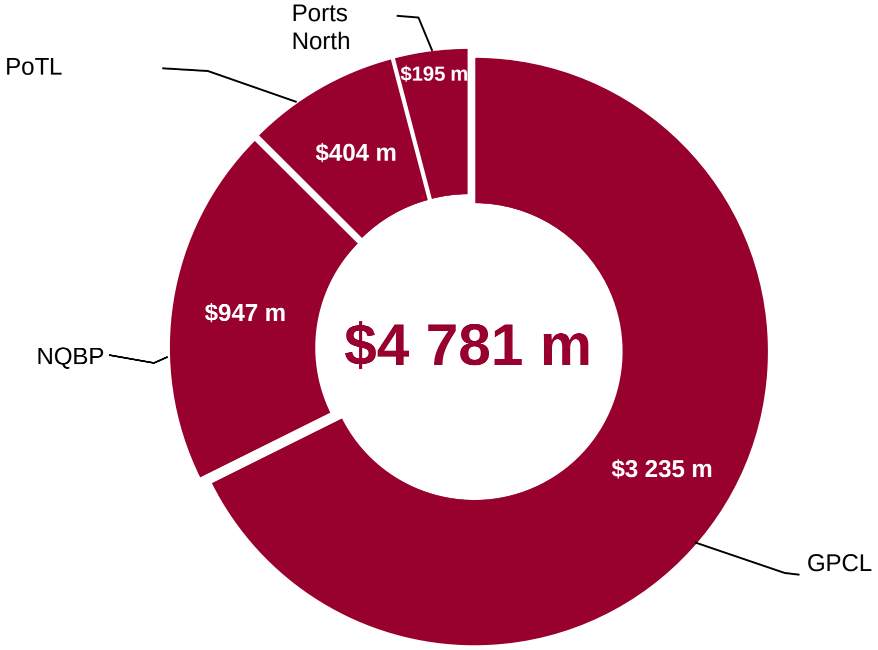


Source: Queensland Audit Office

GPCL has earned more than 38 per cent of its total revenue over the last five years from recoverable works revenue on behalf of other companies, including dredging and community projects.

Figure 4T shows revenue each port earned over the five years to 30 June 2014, excluding gains from sales of assets and increments from asset revaluations. GPCL and NQBP contribute nearly 87 per cent of the total revenue that the sector generates.

Figure 4T
Revenue by port entity—2009–10 to 2013–14



Source: Queensland Audit Office

Legacy arrangements by the state government can affect port entities. Such arrangements can severely restrict the capacity of ports to operate on a commercial basis and significantly reduce port charge-out rates, which affects revenue.

GPCL has been subject to long term legacy arrangements that may affect its operations and restrict its capacity to charge market rates for port charges:

- A 75-year long term lease arrangement, agreed in the 1960s, exists between the state government and a mineral resource project, where GPCL discounts its port charges to at least 88 per cent below the prevailing market rate.
- A 103-year agreement exists between the state and a private exporting company, where the company is not required to pay rent to the port. GPCL collects a reduced port charge well below the prevailing market rate.

Risks to future operating ratios

Global markets influence the operational sustainability of the state's ports sector. During 2013–14, increased trade activity in China increased Queensland coal exports and ports revenue. Expected rises in current trade activity promise revenue increases. Negative global events are just as likely to decrease revenues.

Ports' capital projects are at risk of future write offs.

Long term lease arrangements can restrict the amount of revenue that individual ports generate, constraining port charges well below the prevailing market interest rate.

Flows to government—payments for the competitive neutrality fee, dividends and income tax equivalents—can each significantly reduce a port's operating result. Representing a large proportion of a port's operating profit after tax, these compulsory outflows can restrict the level of profits a port can earn.

Natural or environmental disasters continue to be a risk.

Increasing environmental constraints and approvals placed upon the ports could endanger contracts with major suppliers. This could include delays in dredging programs essential for port performance.

Financial viability of some of Queensland ports is heavily reliant on one commodity: coal.

There is a risk of losing major business partners through insolvency.

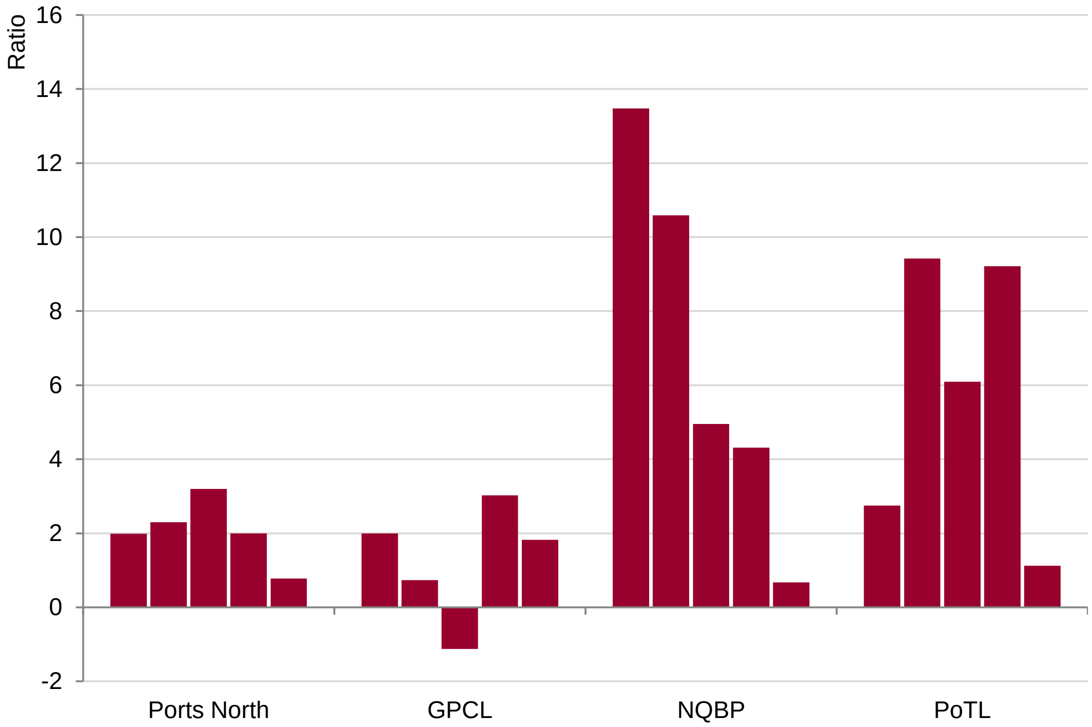
4.6.4 Capital replenishment ratio

The capital replenishment ratio compares the annual net expenditure on non-current assets to annual depreciation. An average ratio below one, over time, indicates assets are being built or replaced slower than depreciation. The ports industry is characterised by long-lived assets, with useful lives as high as 50 years in some cases. Recognising that the nature of these assets may contribute to a declining trend in asset replacement, it is still expected that average ratios will remain above one, and decreases are only incurred in the shorter term.

Over the last five years, the ports sector has averaged a ratio of 3.4, demonstrating the four ports are replacing or building assets faster than they are depreciated or amortised.

Figure 4U illustrates that the state's ports have been, on average, returning a positive ratio between one and 13 for the last five years. This means assets are being replaced in a reasonable time frame, before they are fully depreciated.

Figure 4U
Ports capital replenishment ratios from 2009–10 to 2013–14



Source: Queensland Audit Office

NQBP excluded the substantial proceeds it received in 2010–11 for the long term lease arrangement for the Abbot Point coal terminal from its capital replenishment ratio calculation. This was to avoid a negative result for that year that would incorrectly suggest NQBP was not replacing its assets effectively.

The only negative ratio result relates to GPCL in 2011–12, when the Queensland Government as a GPCL shareholder approved the sale of 160 hectares of land on Curtis Island to Shell CSG Australia for the Shell Australia liquid natural gas project.

PoTL and NQBP experienced significant fluctuations in capital replenishment ratios. We attribute PoTL's fluctuations to a record capital spend of $110 million, including government grants, for the Townsville marine precinct in 2010–11 and significant berth upgrades in excess of $120 million. Significant peaks for NQBP in 2009–10 and 2010–11 related to capital expenditure for the Abbot Point capital expansion project; despite being flagged for lease by 30 June 2011, NQBP incurred capital costs in related works to complete the asset.

Abbot Point terminal was a significant part of NQBP's business operations, and the long term lease of this asset has resulted in a reduction in capital spending and a declining trend in ratio since this time.

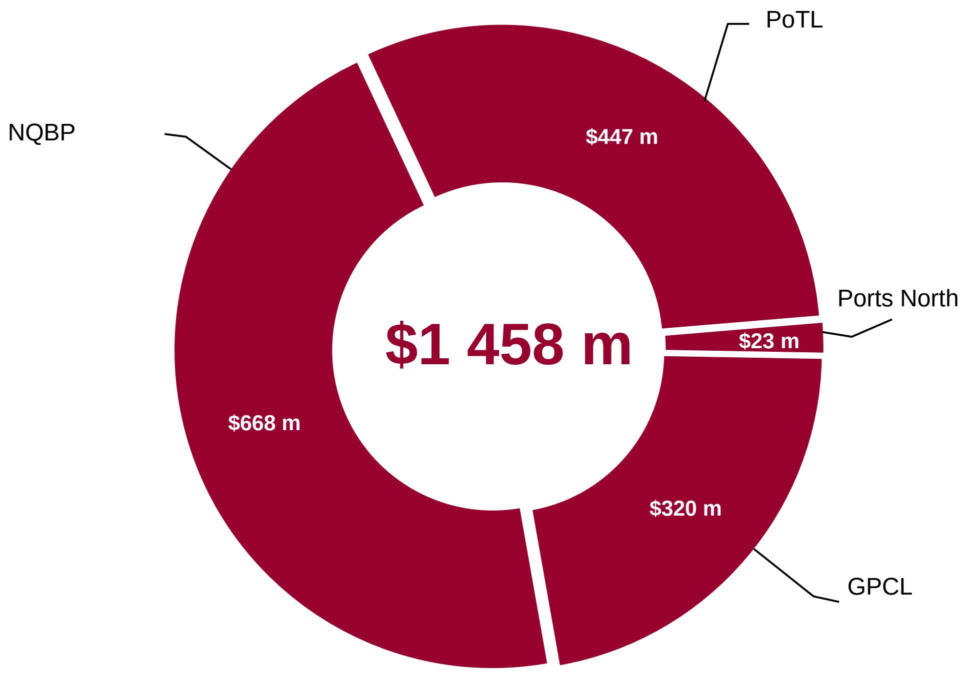
While ports returned positive results, the trend indicates each port's ratio has decreased from 2012–13. Over the last five years, there is no evidence of asset replenishment issues in the ports sector, indicating assets are being replaced faster than they are being depreciated. The risk to asset replenishment will only increase if capital investment continues to decline and reduces the results of the capital replenishment ratio below one for an extended period of the lives of these assets.

Budget versus actual capital spend

As demand for services and commodities increases, so too must the capacity of infrastructure assets the ports own. Capital expenditure includes the expansion of strategic port development facilities and essential capital dredging works.

As Figure 4V shows, NQBP spent $668 million on its capital program (46 per cent of total capital expenditure across the four ports) over the last five years. In 2009–10 and 2010–11 NQBP spent almost $588 million in capital expenditure; however, a long term lease on Abbot Point coal terminal assets reduced NQBP's asset portfolio by $1.4 billion in 2011.

Figure 4V
Total actual capital expenditure over the last five years

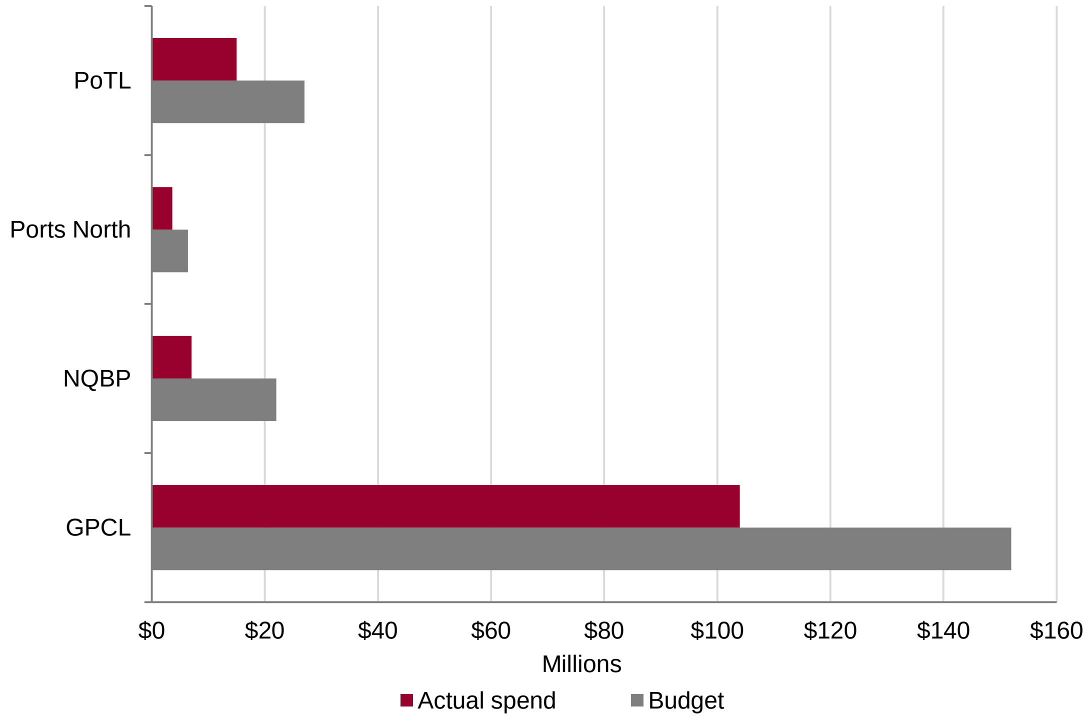


Source: Queensland Audit Office

Although there have been some peaks in capital expenditure over the last five years, capital expenditure within the Queensland ports industry has decreased over recent times. Ports spent $591.4 million in capital from 2011–12 to 2013–14, compared to $867.5 million spent between 2009–10 and 2010–11.

Figure 4W shows each of the four ports spent less on capital than was forecast in 2013–14. Ports spent just over half of the total forecast spend of $207 million on capital in 2013–14. Factors constraining capital programs included project delays, a lack of demand for investment properties and commodities, project underspends, and cancelled projects.

Figure 4W
Comparison of actual versus budgeted spend on capital in 2013–14



Source: Queensland Audit Office

Reducing capital expenditure can help a port retain cash reserves and maintain a positive cash position to help repay outstanding debts and borrowings. This may be a positive result for a port's financial position, but it can mean capital expenditure is merely delayed. This increases the risk projects will end up costing more than they would have cost if the project spend occurred as originally budgeted.

Risks to future capital replenishment ratios

Assets under construction may be written off or impaired when projects are discontinued; in 2013–14, GPCL, NQBP and Ports North reported financial losses for a range of capital projects.

Projects that are delayed or deferred can cost more to finalise.

Capital maintenance programs can be reduced if funds are not available.

Service delivery and related operations can be affected if assets are not replaced on a regular basis.

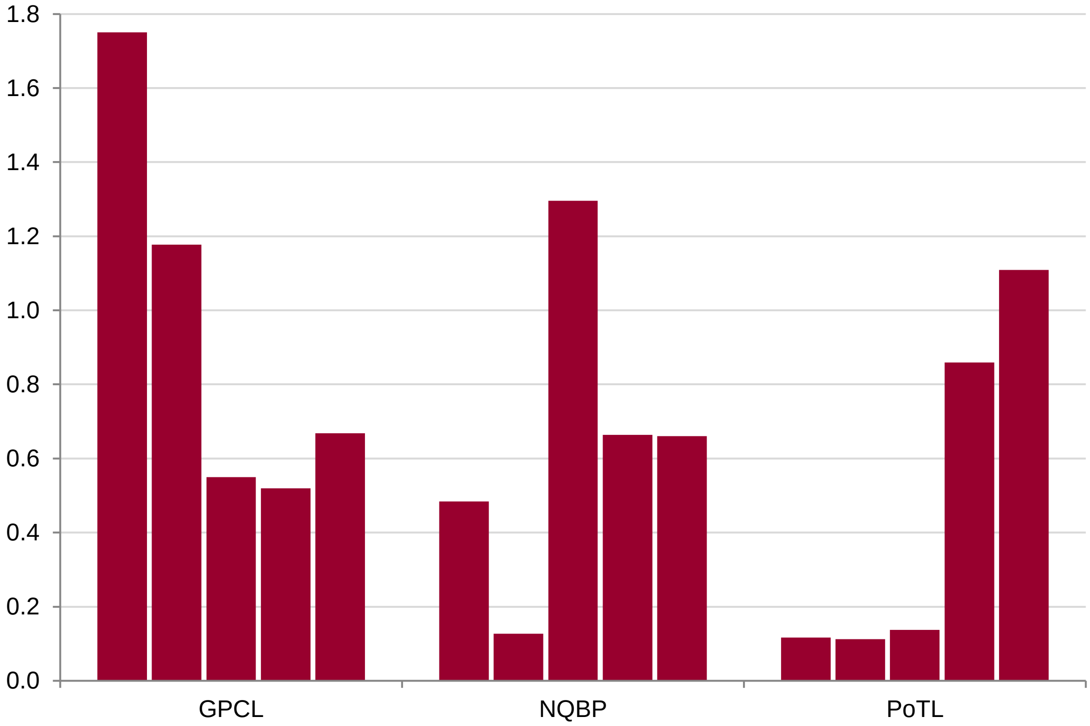
4.6.5 Debt to revenue ratio

The debt to revenue ratio assesses an entity's ability to pay the principal and interest on borrowings when they fall due from the funds generated through the entity's operations. In this ratio, debt is borrowings and does not include other liabilities such as trade creditors. It is used as a means to fund capital investment.

Ports, like other PNFCs, need to scrutinise borrowing arrangements so their capital programs can be funded while delivering on their financial performance.

Over the last five years, the ports sector averaged a debt to revenue ratio of 0.7. In 2013–14, total debt to revenue across three ports (Ports North is excluded because it did not receive any interest-bearing liabilities) demonstrates interest-bearing liabilities represent 70 per cent of total revenue. Total ports sector debt of $3.8 billion represented 36 per cent of total net assets for the sector, is relatively conservative, compared to other PNFC sectors such as Energy and, overall, ports are earning sufficient revenue to cover their debts. Figure 4X demonstrates debt to revenue ratio results for the past five years.

Figure 4X
Debt to revenue ratios for the five years from 2009–10 to 2013–14



Source: Queensland Audit Office

The sale and 99-year lease of Terminal 1 (X50) at Abbot Point, resulted in a transfer of NQBP's debt of $915 million to the state in 2010–11, resulting in fluctuations in the debt to revenue ratio until 2011–12. A decrease in 2012–13 was due to an increase in vessel income of $11.6 million; and receipt of $15 million for underwriting revenue in the form of project contributions.

PoTL maintained a fairly stable debt to revenue ratio for the three years from 2009–10. It incurred a significant increase in 2012–13, largely due to a decrease in the fair value gains for investments of $12 million and a substantial increase of $56 million in Queensland Treasury Corporation loans. PoTL's debt to revenue ratio continued to increase in 2013–14.

GPCL ratios have improved through $740 million in revenue it generated from recoverable works performed for its major customers over the last two years. While undertaking recoverable works is a feature of GPCL's business, it is not a constant or reliable source of revenue. Ports are not highly leveraged, largely due to increasing revenues and funding arrangements with private parties which fund maintenance and capital projects.

Interest 'bite'

Debt sustainability can be measured by an entity's ability to service its debt obligations—to pay interest and to repay or refinance loans when they fall due. The interest expense ratio—'interest bite'—considers how much operating revenue is required to pay interest charges.

Ports recorded total interest expense on their borrowings of $33.8 million in 2013–14 ($181.6 million in the five years to 30 June 2014).

The sector averaged total interest expense of four per cent of revenue earned in five years. The low percentage demonstrates the revenue the state's ports earn more than covers the interest on their borrowings, further demonstrating the ports sector is financially sustainable.

Risks to future debt to revenue ratio

Increasing environmental constraints and approvals placed upon the ports could lead to higher operating costs and loss of contracts with major suppliers; for example, this could delay dredging programs essential for port performance.

Reduced demand for commodities such as coal would affect revenue.

Natural disasters such as cyclones and floods are a risk.

Delays in investment in private sector resource projects due to market conditions and availability of finance are another risk.

GPCL has borrowings of more than $100 million. Interest rate movements could affect its capability to repay its debts.

Long term lease arrangements can restrict the amount of revenue individual ports can generate, constraining port charges well below the prevailing market interest rate.

4.6.6 Net flows to and from the government

The flows to and from the government can inhibit ports entities from meeting their present and future obligations—asset purchases and maintenance, debt repayment—while maintaining their financial sustainability. For the port sector, flows to the government have included dividends declared, income tax expense and competitive neutrality fees. Flows from the government related to equity injections. The government does not provide community service obligations to the port sector.

Net flows to government in 2013–14 for ports was $191.32 million.

Flows to and from government have been largely consistent over the last five years; however, during 2010–11, the ports sector declared a substantial dividend from a revenue increase of $395 million. This was due to NQBP's disposal of various assets, liabilities and other legal rights to the Abbot Point coal terminal to APCT #1 Pty Ltd.

Figure 4Y shows the flows of funds to and from the government over five years to 2013–14.

Figure 4Y
Flows from and (to) the government

Account	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Flows from the government					
Equity contributions	73.1	2.0	9.0	0	2.0
Community service obligations and other state government grants	80.4	37.6	14.6	0	0
Flows (to) the government					
Dividends declared	(56.6)	(262.4)	(53.4)	(93.9)	(91.4)
Income tax (expense) credit	(41.9)	33.4	(41.5)	(52.9)	(62.2)
Competitive neutrality fees	(5.6)	(10.4)	(7.5)	(7.8)	(8.7)
Equity withdrawals	0	0	0	0	(31.0)
Net flows (to) the government					
Net flows to and from government	49.4	(199.8)	(78.8)	(154.6)	(191.32)

Source: Queensland Audit Office

Equity contributions and withdrawals

Equity contributions have minimal effect on the financial sustainability of Queensland's four government owned ports, with Ports North and NQBP receiving $55 million and $157 million receiving net equity contributions over the last five years. None of the other ports has received or returned equity contributions over this period. PoTL received grants for Townsville Marine Precinct and cruise liner terminal and Berth 10 projects.

Ports North had an aggregate nil profit position over the last five years. The net equity flows of $55 million received over the same period funded capital expenditure for the cruise liner terminal, but largely related assets and liabilities transfer as part of the regional ports takeover.

Other ports fund their capital programs through debt borrowings.

Community service obligations and other state government grants

PoTL received state grants of $129.3 million from 2009–10 to 2011–12 to develop the Townsville Marine Precinct, the Berth 10 wharf, and cruise ship terminal.

None of the state's ports receive community service obligations.

Competitive neutrality fees

Each of three ports, excluding Ports North, has paid nearly $40 million in competitive neutrality fees on their borrowings over the last five years. Government charges these fees to allow for the competitive advantage government businesses have over their competitors.

Competitive neutrality fee payments only represent a small portion of after tax profits. Such payments have minimal effect, if any, on each port's operational sustainability.

GPCL incurred the highest percentage of competitive neutrality payments over the last five years—only seven per cent of the after tax profits GPCL earned over the same period.

Income tax expense and credits

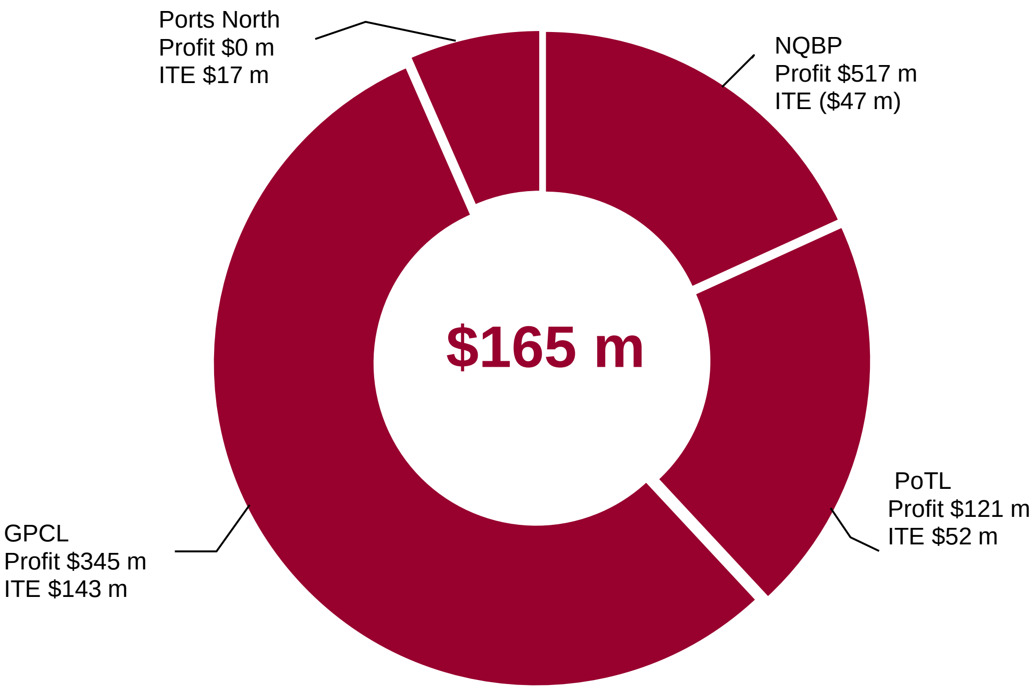
The effects of income tax payments on operational sustainability varies between the ports. The four ports paid income tax equivalent payments of $165 million over the last five years—17 per cent of the total profits the four ports earned after tax of $983 million.

Income tax equivalent payments represented a significant proportion of profits for GPCL (41 per cent) and PoTL (43 per cent). The effect on Ports North and NQBP is minor, even though NQBP paid almost the same amount in income tax as PoTL over the last five years.

Each port is exempt from income tax under s.23(d) of the *Income Tax Assessment Act 1936* (Cth*).* However, in accordance with Part 2 of the Queensland Treasurer's *Tax Equivalents Manual* and s.129 of the *Government Owned Corporations Act 1993*, each port must make income tax equivalent payments.

Figure 4Z shows the total income tax expense over the last five years for the four ports.

Figure 4Z
Income tax expense (ITE) as a comparison of net profits over the past five years



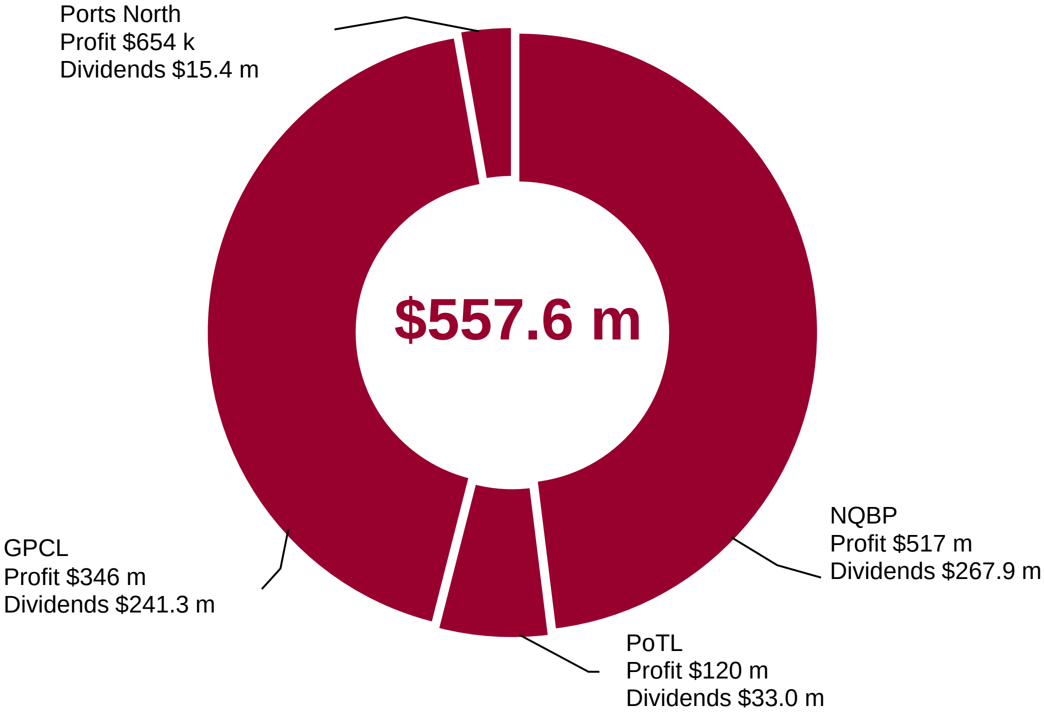
Source: Queensland Audit Office

Dividends

Port dividends are significant as a percentage of profits earned after tax and can affect their financial sustainability.

Figure 4AA demonstrates ports declared $557.6 million in dividends to the state government since 2009–10, representing 57 per cent of total after tax profits the four ports earned.

Figure 4AA
Five year net aggregate of after tax profits and dividends declared by entity



Source: Queensland Audit Office

5 Rail sector

In brief

Background

Queensland Rail (QR) fulfils the role of a railway manager and railway operator under the *Transport Infrastructure Act 1994,* serving the passenger, tourism, resources and freight customer markets.

QR carries more than 55 million passengers throughout the state each year and manages 6 754 kilometres of track. It was established as a statutory authority on 3 May 2013 with the passage of the *Queensland Rail Transit Authority Act 2013*.

QR Network's *QR Network's Access Undertaking (2008) June 2010,* which the Queensland Competition Authority (QCA) approved in June 2010, requires Queensland Rail Limited to prepare and publish financial reports for QR's below rail services. These reports are prepared in accordance with the *Costing Manual* the QCA approved.

This chapter details the results of our audit of QR, Queensland Rail Limited, On Track Insurance Pty Ltd and QR's below rail services.

Conclusions

We issued unqualified audit opinions to each entity for 2013–14.

Overall, these entities are financially sustainable. QR's future sustainability depends on:

- providing continued passenger rail services to the Department of Transport and Main Roads under a transport services contract
- undertaking reform in response to recommendations of the Queensland Commission of Audit, particularly those for QR to operate under future contestable service delivery arrangements
- delivering, maintaining, and managing rail networks throughout Queensland that provide an efficient, low cost option for rail operators to move large volumes of goods.

We provided an emphasis of matter in our audit opinion of the 2012–13 below rail services financial report to highlight the report is a special purpose report and may not be suitable for other purposes.

Key findings

- We completed audits of the financial reports of all public non-financial corporation entities within the QR group by their legislative deadlines.
- The QCA granted an extension for the 2012–13 below rail services financial report, due to a delay in finalising the 2012–13 QR statements.
- We found draft financial reports provided to audit in 2013–14 were of good quality. We did not require any material adjustments to the account balances within the draft financial reports provided for audit. We identified some disclosure omissions during our audit; these mostly related to Queensland Treasury and Trade's minimum reporting requirements.
- QR's operating ratio has increased primarily as a result of a three per cent increase in transport services contract revenue and a three per cent reduction in operating costs, including $44 million less in employee costs; consumable cost reductions of $45 million; and an offset of depreciation charges which increased $20 million.
- With reduced capital expenditure over the past four years, QR's capital replenishment ratio has been trending downwards. In 2013–14, QR invested $0.76 for each dollar of service potential of its non-current assets lost through depreciation and amortisation. The capital expenditure on the new generation rolling stock by the Department of Transport and Main Roads to replenish QR's existing rail assets will help in improving the ratio in the wider rail sector.
- Although QR's borrowings exceed its operating revenue by an average of 1.6 times over the last four years, the risk is low that QR would not able to pay its debts when they fall due as interest expense represented only nine per cent of total operating income over the same period. Queensland Rail's debt level has remained consistent over four years.

5.1 Background

The Queensland rail sector comprises Queensland Rail (QR), Queensland Rail Limited and On Track Insurance Pty Ltd which has a 30 June balance date.

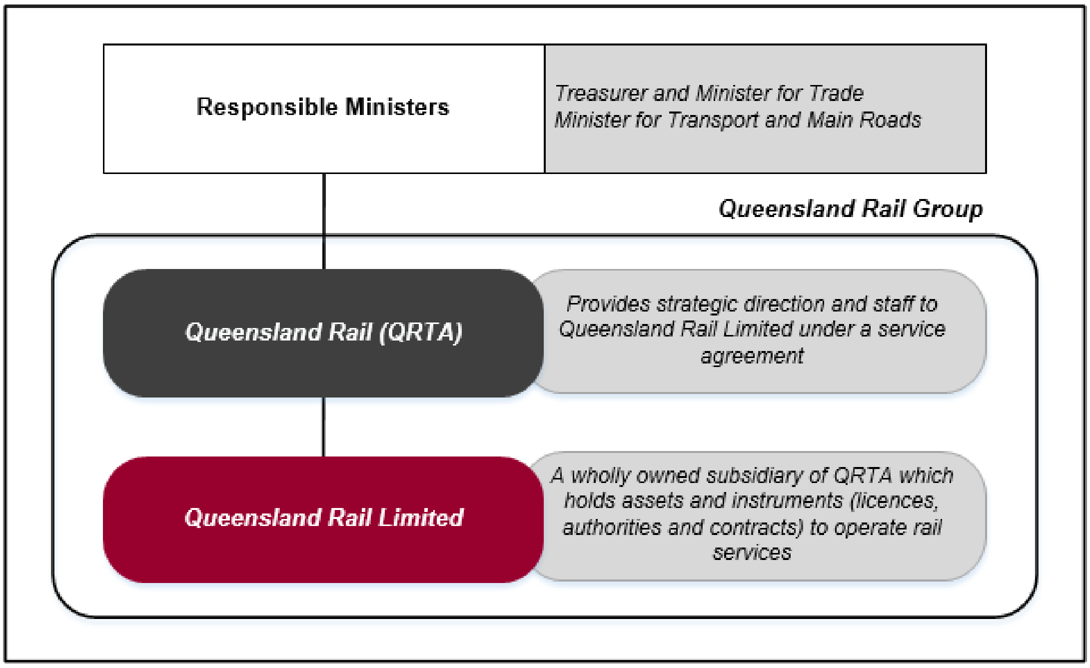
Before its name changed on 2 June 2013, QR was the former Queensland Rail Transit Authority established on 3 May 2013 under the *Queensland Rail Transit Authority Act 2013*. In accordance with this Act, shares in Queensland Rail Limited transferred to QR, thereby establishing Queensland Rail Limited as a wholly owned subsidiary of QR. All employees and their associated leave entitlements belonging to Queensland Rail Limited also transferred to QR.

Queensland Rail Limited changed its name from QR Passenger Pty Ltd on 11 June 2010 to anticipate the fundamental change to its operations when it became a fully integrated rail services provider on 1 July 2010. QR Passenger Pty Ltd had only operated metropolitan passenger trains, but Queensland Rail Limited significantly extended its operations. It owns all rail infrastructure in the metropolitan network and the non-coal regional rail network and is responsible for construction, maintenance and operation of those networks.

On Track Insurance Pty Ltd transferred from QR Limited (now known as Aurizon Holdings Limited) on 6 October 2010. On Track Insurance Pty Ltd remained a subsidiary of Queensland Rail Limited and its operating results are consolidated into financial reports of Queensland Rail Limited. The transfer was in accordance with the transfer notice enacted in line with the *Infrastructure Investment (Asset Restructuring and Disposal) Act 2009*. On Track Insurance Pty Ltd's principal objective is to insure and underwrite the risk of Queensland Rail Limited for events occurring up until 30 June 2010. External insurers cover events after 30 June 2010.

Figure 5A depicts the relationship between QR, Queensland Rail Limited and the responsible Ministers.

Figure 5A
Relationship between Queensland Rail group and responsible Ministers



Source: Queensland Audit Office

QR is an integrated rail operator that provides three primary products:

- SEQ Commuter (integrated above and below rail)
- Travel and Tourist train (above rail)
- Network (below rail).

5.1.1 SEQ Commuter

SEQ Commuter is a passenger and rail access service operating and maintaining 211 commuter rail car sets, 146 stations and 300 kilometres of track throughout south-east Queensland. Services extend from the centre of Brisbane, south to Beenleigh and Varsity Lakes on the Gold Coast; north to Ferny Grove, Shorncliffe, Doomben, Caboolture and Gympie; east to Cleveland; and west to Richlands, Ipswich, Rosewood and Springfield.

5.1.2 Travel and Tourist train

Travel and Tourist train provides train travel and holiday packages for international, interstate and intrastate tourists or holiday makers. It comprises QR's Travel network, heritage and tourist operations and travel centres.

Travel and Tourist train rail services extend along the Queensland coastline from Brisbane to Cairns, west to Charleville, Longreach and Mount Isa and include:

- Spirit of the Outback
- The Inlander
- The Westlander
- The Sunlander
- The Rockhampton tilt train
- The Cairns tilt train
- Kuranda Scenic Railway
- Gulflander.

QR also owns and operates specialist travel centres that offer holiday packages including air travel, car hire, travel and accommodation.

5.1.3 Network

QR's network covers the south-east Queensland network; and the Mount Isa, north coast, western, West Moreton, south western and central western rail lines. The network arm of the business focuses on 'below rail' management of QR's track and rail assets.

Third party operators access the network to deliver freight; the main freight customers are from the agricultural, mining, manufacturing, retail and tourism industries. Network access agreements contributed $217.5 million in revenue in 2013–14, with 23.4 million tonnes of freight transported across the network.

5.1.4 Changes to QR

Proposed divestment of Mount Isa line with Port of Townsville Limited

On 3 June 2014, the Queensland Treasurer announced in the State Budget that the Mount Isa line would be one of several government owned assets to be investigated for long term lease as part of the initiative to reduce the state's debt.

In line with the Queensland Commission of Audit's final report released in February 2013, and the government's response released in April 2013, the government will seek to combine the Mount Isa line with Port of Townsville Limited to create an integrated supply chain business.

The proposal would see a long term lease offered for the integrated asset of the Mount Isa line and Port of Townsville Limited, allowing the private sector to operate, maintain and expand the port and rail line for a term up to 99 years, in return for an upfront payment.

QR manages and maintains the Mount Isa line for freight services provided by private rail operators Aurizon Holdings Limited and Pacific National (QLD) Pty Limited. The region served by the line produces around 75 per cent of Queensland's non-coal mineral output; the line carries around five million tonnes of bulk freight annually.

Australian Rail Track Corporation review

On 25 February 2014, the Minister for Transport and Main Roads announced the federal government's Australian Rail Track Corporation Limited would review the viability of integrating Queensland's regional rail network with the national rail network.

The review is split into two phases—an initial exploratory phase followed by a due diligence process. The initial exploratory phase is nearly finished at the time of writing this report.

The Australian Rail Track Corporation Limited will submit its findings to the state and federal governments.

Once due diligence is complete, the federal and state governments will consider findings and decide whether to integrate the two networks.

Organisational restructure

QR has undergone major restructures in the last few years since separating from Queensland Rail Limited. The change of state government in March 2012 and the subsequent Queensland Commission of Audit provided further catalysts to increase efficiency and reduce costs of business.

High Court challenge

The High Court of Australia will hear a constitutional challenge by 11 unions in relation to whether Queensland Rail Statutory Authority is a constitutional corporation for the purposes of the Commonwealth Constitution and is therefore subject to the *Fair Work Act 2009* (Cth) rather than the state *Industrial Relations Act 1999.*

The enactment of the *Queensland Rail Transit Authority Act 2013* established Queensland Rail as a statutory authority and transferred existing employees of Queensland Rail Limited to the statutory authority. Those employees therefore became subject to the *Industrial Relations Act 1999 (Qld)* rather than the *Fair Work Act 2009* (Cth). The unions submit that the *Fair Work Act 2009* (Cth) applies to Queensland Rail and its employees on the basis that Queensland Rail is a constitutional corporation despite s.6(2) of the *Queensland Rail Transit Authority Act 2013* (which states that it is not a body corporate). The unions allege QR has several other attributes of a corporate entity and that it is a trading corporation on the basis that it was established to carry on a commercial enterprise, that its trading activities are significant and substantial, and that they are integral to its operations.

A successful unions' challenge may have significant industrial relations and corporate structure implications for QR. The case is still pending.

5.1.5 Entities covered in this chapter

This chapter includes the 2010–11 to 2013–14 results of our audits of rail sector PNFCs and the entities they control. QR was established on 3 May 2013 and became the parent entity of Queensland Rail Limited. Prior to this date, Queensland Rail Limited was the only PNFC entity within the rail sector in Queensland.

Queensland Rail Limited has a single, wholly owned subsidiary (On Track Insurance Pty Ltd, detailed in Appendix C of this report) which was not required to produce a financial report in 2013–14.

This report does not report on rail infrastructure projects such as Moreton Bay Rail Link and new generation rolling stock which the Department of Transport and Main Roads manages.

5.2 Conclusions

We issued QR and Queensland Rail Limited with unqualified audit opinions. We provided an emphasis of matter audit opinion to the 2012–13 below rail financial report to highlight the report is a special purpose report and may not be suitable for other purposes.

On Track Insurance Pty Ltd does not have to prepare financial statements, so we did not provide an independent audit opinion. We verified trial balance figures as part of our audit of Queensland Rail Limited's consolidated balances.

We completed audits of all entities by their legislative deadlines. The Queensland Competition Authority (QCA) extended the deadline for the below rail services financial statements, due to delay finalising QR's 2012–13 financial report.

We were satisfied with the quality and time frames of the draft financial reports provided for audit in accordance with agreed dates.

Since becoming a separate legal entity in 2010–11, QR (and before its establishment, Queensland Rail Limited) achieved positive operating results.

Its debt to revenue ratio over the past four years is high, with debt exceeding its operating revenue, due to a $3 billion loan it inherited in its capital structure when incorporated. We consider the risk of QR not being able to repay its debts as and when they fall due is low.

Overall, we consider QR and Queensland Rail Limited financially sustainable with continued government support.

5.3 Audit opinions

Financial reports

We issued unqualified audit opinions for QR and Queensland Rail Limited. This confirms the Queensland Rail group has prepared financial statements according to the requirements of legislation and relevant accounting standards. Figure 5B details the audit milestones leading to our audit opinion of the Queensland Rail group for 2013–14.

Figure 5B
2013–14 audit opinions issued

Audit	First draft financial report	Financial reports signed	Opinion issued	Certified by deadline	Opinion
		Statutory authority			
QR	25.07.2014	28.08.2014	29.08.2014	Yes	Unqualified
		Controlled entities			
Queensland Rail Limited	25.07.2014	28.08.2014	29.08.2014	Yes	Unqualified
On Track Insurance *	N/A	N/A	N/A	N/A	N/A
		Special purpose			
QR below rail services provided 2012–13	07.02.2014	28.03.2014	28.03.2014	Yes	Emphasis of matter
QR below rail services provided 2013–14**	TBA	TBA	TBA	TBA	TBA

* On Track Insurance Pty Ltd does not prepare financial statements
** The 2013–14 financial report of QR's below rail services is scheduled to commence in October 2014

Special purpose report

We provided an emphasis of matter audit opinion to the 2012–13 QR below rail services financial report to highlight the report is a special purpose report and may not be suitable for other purposes. The below rail services financial report represents a special purpose financial report prepared specifically to meet the information needs of the QCA and those who may seek access to rail infrastructure for the purpose of operating trains.

Sub clause 3.2.1 of the *Queensland Rail Access Undertaking* obligates Queensland Rail Limited to prepare financial statements for QR's below rail services; sub clause 3.2.2 requires statements to be audited within six months of the end of year to which the financial statements relate. The statements are to comply with the QCA's *Costing Manual*.

On 12 December 2013, the QCA extended the deadline for QR's below rail services 2012-13 financial report, due to delay finalising QR's financial statements. The 2013–14 audit of the below rail services statements is scheduled to begin in October 2014.

5.4 Timeliness and quality of financial reports

5.4.1 Timeliness

To show accountability for the use of public monies, entities should prepare and publish their financial reports as soon as possible after the end of the financial year. The later financial reports are produced and published after their balance date, the less useful they are for stakeholders and for informing decision making.

Management and audit certified the financial reports for QR and its controlled entity, Queensland Rail Limited, by the legislative deadline of 31 August 2014.

We agreed key milestones with management to manage the financial reporting process; QR met all obligations.

We received all draft financial reports in accordance with the agreed time frame.

5.4.2 Quality and accuracy

QR undertakes an 'early close' each year, preparing the financial report for audit purposes earlier in the financial year. Typically, QR prepares these reports as at 30 April and provides them to audit by 31 May each year. This means audit can verify most balances earlier in the financial year and reduce the volume of work at the end of the year.

We did not require either QR or Queensland Rail Limited to make material adjustments to draft financial reports.

Most of QR's disclosure adjustments were to comply with Queensland Treasury and Trade's financial reporting requirements for statutory bodies and improved financial report quality.

5.5 Significant financial reporting issues

5.5.1 Valuation of non-current assets

Under Queensland Treasury and Trade's non-current asset policies, QR can measure its buildings, infrastructure and, plant and equipment assets at fair value or cost. QR has chosen cost, so AASB 13 *Fair Value Measurement* has no effect when preparing its statutory accounts.

QR is required to apply the fair value principles when preparing its whole of government accounts. Fair value is the price received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. QR adopted the depreciated replacement cost approach to estimate the fair value of its infrastructure assets. As a result, the value of these assets reported at cost in its annual financial report is lower by $3.5 billion than the fair value for whole of government reporting purposes.

5.5.2 Onerous contract for office accommodation

On 30 June 2010, Queensland Rail Limited separated from its parent, QR Limited and, as part of the separation, lease arrangements were transferred to Queensland Rail Limited. After the transfer, Queensland Rail Limited staff relocated to Brisbane CBD office space originally intended for Aurizon staff. In early 2013–14, Queensland Rail Limited staff returned to 305 Edward Street, which QR owns.

This means most accommodation relating to lease arrangements is vacant; some floors are leased to tenants for two more years at most. Given an oversupply of office space in Brisbane's CBD, QR is endeavouring to lease its vacant CBD leased properties in the short to medium term.

QR's lease arrangement represents an onerous contract, where costs exceed economic benefits. QR recognised an expense in 2013–14 of $30 million, arising from this onerous contract. QR continues to seek opportunities to sub-lease accommodation; where opportunities are identified, QR will need to reverse the expense.

5.6 Financial performance, position and sustainability

When forming an audit opinion on the financial report of an entity, we assess its ability to continue to operate as a going concern. We assess an entity's financial performance, position and sustainability using three key ratios—operating, capital replenishment and debt to revenue ratios. We also assess flows to and from government.

5.6.1 Financial performance and position

QR's financial performance has improved over the last four years, with revenue increasing each year.

QR's employee benefits expense represents 41 per cent of the QR's expenses and inter-company transactions. Depreciation and amortisation expense and supplies and services constitute 45 per cent of Queensland Rail Limited's expenses.

Figure 5C provides more detail on significant account balances for the Queensland Rail group over four years.

Figure 5C
Financial Performance and Position

Accounts	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Factors affecting financial performance				
Revenue	1 839.5	1 946.0	1 930.6	1 983.6
Expenses	1 678.1	1 760.0	1 729.8	1 673.9
Income tax Expense	12.1	57.7	56.0	96.1
Profit after tax	149.3	128.3	144.8	213.6
Factors affecting financial position				
Assets	6 596.4	6 846.6	7 202.0	6 902.7
Liabilities	4 123.9	4 108.9	4 456.8	4 100.0
Equity	2 472.5	2 737.7	2 745.2	2 802.7

* For financial years 2010–11 to 2012–13, the balances were based on Queensland Rail Limited's financial performance, as Queensland Rail (the consolidated entity) only commenced operations on 5 May 2013 and operated for less than two months of 2012–13.

Source: Queensland Audit Office

Borrowings and property, plant and equipment dominate the overall performance and position of the PNFC rail sector. At 30 June 2014, Queensland Rail Limited's borrowings and property, plant and equipment accounted for 100 per cent within the sector. QR's assets and liabilities are limited to employee related provisions and intercompany balances.

5.6.2 Financial sustainability

Like all PNFCs, QR must be able to meet its current and future expenditure, as it falls due, to be considered financially sustainable.

QR was established on 3 May 2013; before that, Queensland Rail Limited was Queensland's sole integrated rail operator from 1 July 2010. To assist comparison, we have measured financial sustainability using the audited results of Queensland Rail Limited's financial reports since 2010–11.

We used results of three indicators of financial sustainability in financial reports. Based on the ratios, we assessed QR and its controlled entities as financially sustainable while the government continues to procure rail services under the transport services contract.

5.6.3 Operating ratio

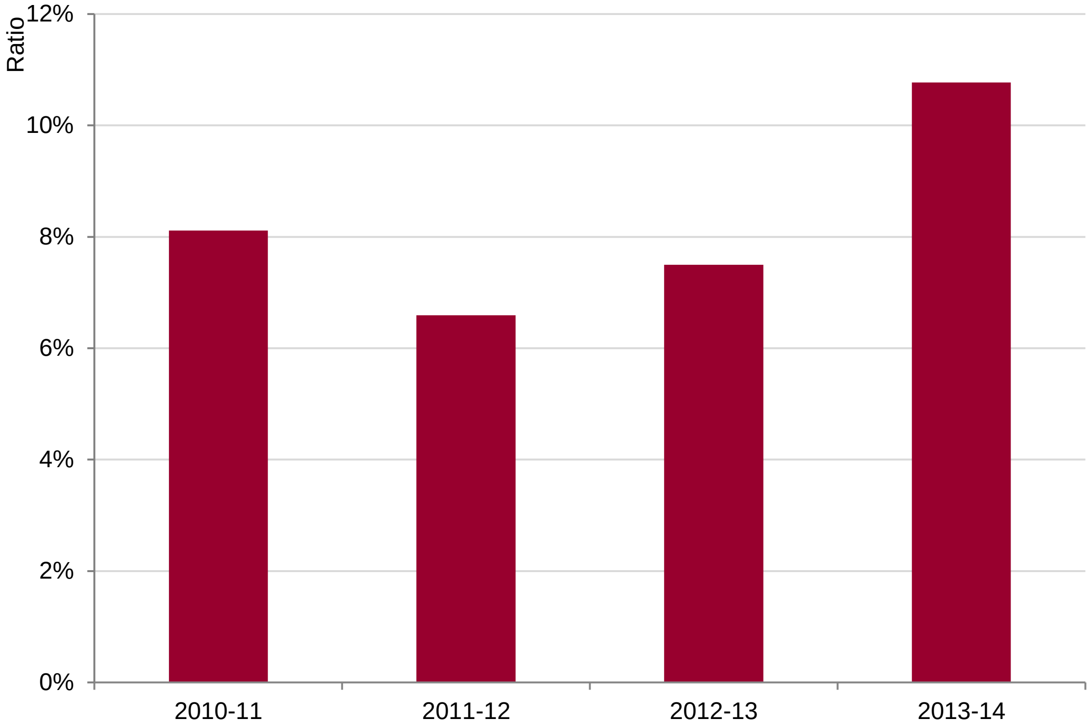
The operating ratio is operating profit after tax as a proportion of total revenue. It should be positive over the medium to long term for QR to remain financially sustainable. As QR derives most revenue from government funding, the ratio can measure QR's ability to control its recurrent operating and capital expenditure.

QR achieved an average operating ratio of eight per cent over the last four years.

As it continues its transformation to a more efficient and effective organisation, QR increased its revenue by $53 million and reduced its operating expenses by $56 million in 2013–14, resulting in a significantly higher 2013–14 operating ratio.

Figure 5D shows QR has improved its operating ratio in the last three years; it is unlikely its operating revenue would not meet its operating expenditure as it becomes due.

Figure 5D
Operating ratios from 2010–11 to 2013–2014



Source: Queensland Audit Office

Risk to future operating ratios

QR's transport services contract with the state government contributes approximately 80 per cent of QR's total revenue. If this contract revenue reduces, it will affect QR's future operating sustainability.

The 2014 State Budget recommended combining the Mount Isa rail line with Port of Townsville to create an integrated supply chain business. The proposal would offer a long term lease to the private sector to operate, maintain and expand the port and rail line up to 99 years for an upfront payment. The loss of the Mount Isa rail line will affect QR's revenue negatively.

Early retirement of existing city train rolling stock when new generation rolling stock fleet is commissioned will affect the state's operating ratio. Under the transport services contract, QR would expect the Department of Transport and Main Roads to compensate any financial loss QR incurred by retiring rolling stock before their design life expires.

The potential integration of QR's regional network with the national rail network is a risk. The Australian Rail Track Corporation will submit its findings to the state and federal governments. The governments' decision will affect QR's future operating performance.

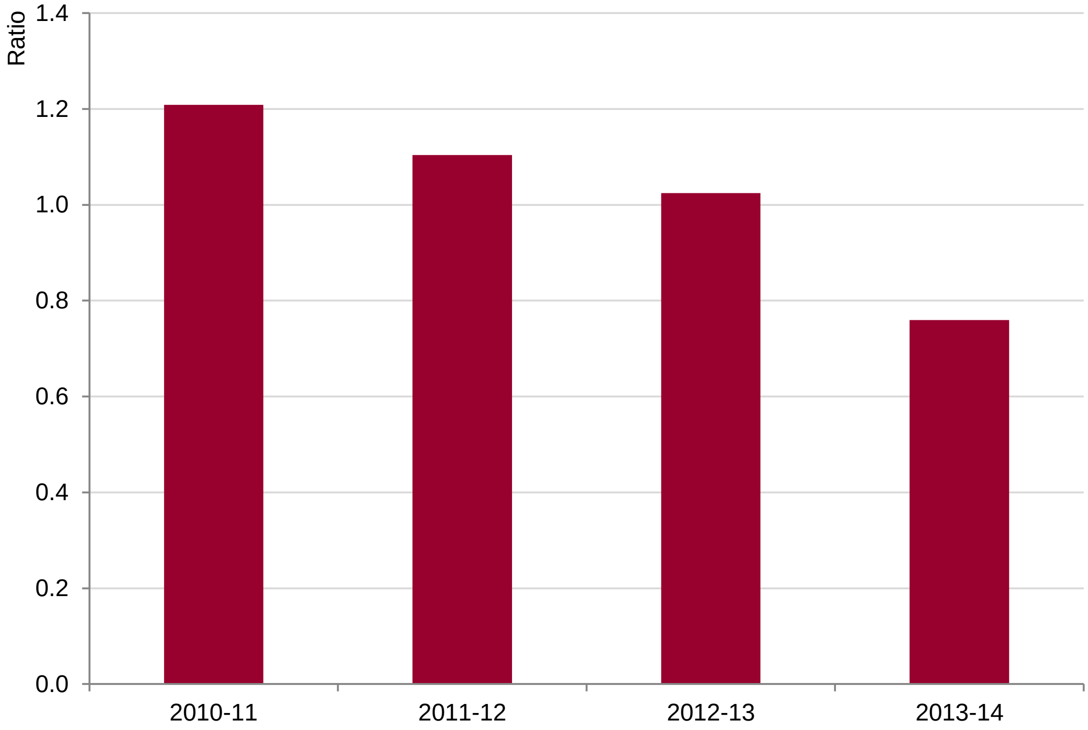
5.6.4 Capital replenishment ratio

This ratio compares the rate of net spending on non-current assets with its depreciation. A ratio less than one on an ongoing basis indicates capital expenditure is not being optimised so as to minimise whole of life cycle costs of assets or that assets may be deteriorating faster than they are being renewed or replaced.

The capital replenishment ratio compares the annual net expenditure on non-current assets to annual depreciation. An average ratio below one, over time, indicates assets are being built or replaced slower than depreciation.

We have used the depreciation expense on the current replacement cost of non-current assets to calculate the capital replenishment ratio. Figure 5E illustrates QR's capital replenishment ratio over the last four years.

Figure 5E
Capital replenishment ratios from 2010–11 to 2013–14



Source: Queensland Audit Office

QR achieved an average capital replenishment ratio of one over the last four years. This indicates QR has replenished its non-current assets to cover lost service potential. Although QR's assets are characterised by long-lived assets, with design lives as high as 100 years in some cases, QR's capital replenishment ratio is trending downwards. For the year ended 30 June 2014, QR did not adequately replace the service potential of its non-current assets lost through depreciation. This downward trend increases the risk that key operating assets will not be renewed when due.

QR's capital replenishment ratio does not account for capital spend in the wider rail sector on the new generation rolling stock public private partnership arrangement that the Department of Transport and Main Roads manages. Capital expenditure for this project will help replenish QR's existing rail assets and help offset the downward trend in the capital replenishment ratio.

Capital program

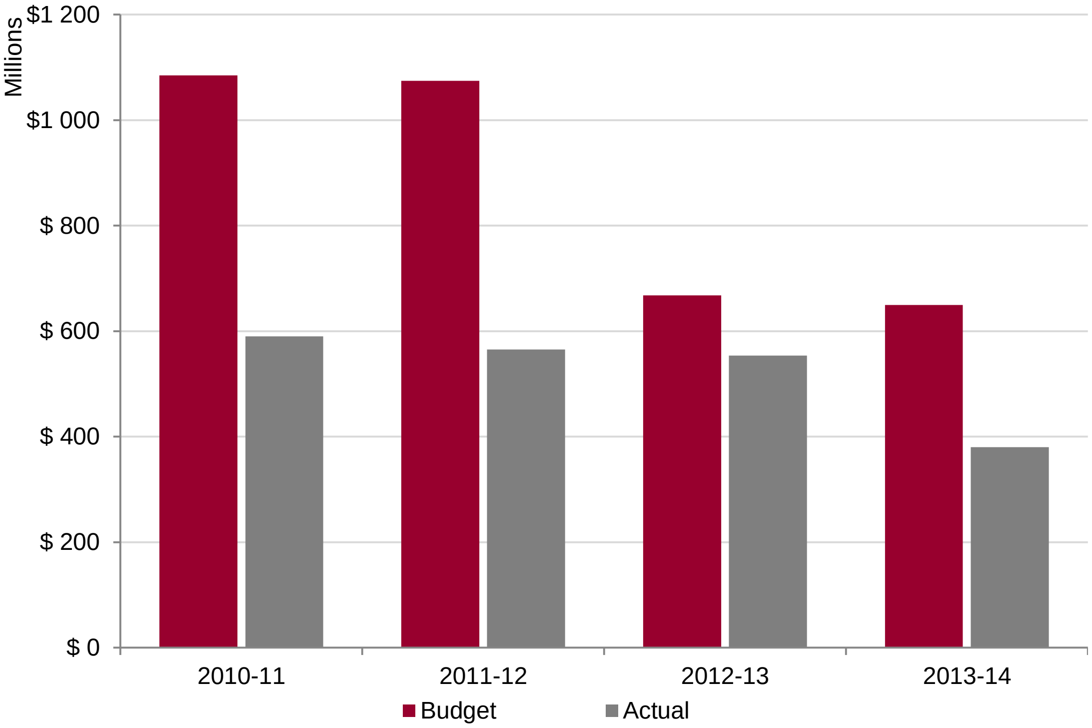
Construction and management of rail infrastructure in the metropolitan network and the non-coal regional rail network is significant in QR's operations. During 2013–14, QR completed projects with capital costs of more than $666 million. At 30 June 2014, 255 capital projects with combined costs of $245 million were in progress.

Investment in capital projects

QR has not met capital expenditure targets over the past four years. Reduced labour resources, a deliberate reduction in capital replenishment, delays in project decisions and spending, and the transfer of the new generation rollingstock project to the Department of Transport and Main Roads have all contributed to Queensland Rail not achieving their capital expenditure targets.

Figure 5F compares QR's budgeted and actual capital expenditure over the past four years.

Figure 5F
Comparison of budgeted and actual capital expenditure from 2010–11 to 2013–14



Source: Queensland Audit Office

On average, QR has reduced its capital investment on assets by 13 per cent each year and underspent its capital budget by 38 per cent each year. In 2013–14, QR spent 59 per cent of its forecast capital program.

Assets under construction expensed

We consider the capital replenishment ratio be read in the context of costs of assets under construction (AUC) expensed during the year. Expensing costs recorded as assets has affected QR's capital replenishment ratios in 2012–13 and 2013–14.

In 2012–13, QR expensed $54 million of AUC when de-scoping the Sunlander 14 project. Most of $37 million QR expensed in 2013–14 related to pre-feasibility expenditure on new generation rolling stock, which QR recovered from the state government when the project transferred to the Department of Transport and Main Roads.

Opening of Springfield rail line

QR's largest project completed in 2013–14 was the Springfield rail line for Springfield residents to travel directly to Brisbane's CBD by train for the first time. This $475 million project included a 9.5 kilometre dual track passenger rail line constructed between Richlands and Springfield; and two new stations at Springfield and Springfield Central. The project was delivered on time and within budget.

New generation rolling stock and early retirement of existing rolling stock

In January 2014, the government awarded a $5.4 billion (in nominal dollars) contract to the new generation rolling stock consortium to deliver 75 new six-car electric trains and construct a purpose-built centre to maintain these trains for 30 years.

Payments for maintenance represent nearly half of the total contract value. The contract includes Queensland Government funded capital contributions to the consortium of $720 million between June 2016 and December 2018.

Although the Department of Transport and Main Roads is managing the project, any early retirement of the current city train rolling stock will result in a net financial loss to the government and will affect the state's future operating ratios.

QR expects the Department of Transport and Main Roads to compensate any financial loss from QR retiring rolling stock early under the transport services contract. The Department of Transport and Main Roads and QR have not formalised the commissioning and replacement schedule for the proposed fleet.

Risks to future capital replenishment ratios

Rollout of new generation rolling stock and replacement of existing city network rolling stock in 2016 will increase depreciation if QR revises the useful lives of existing assets downwards.

QR's inability to achieve its capital investment targets could reduce capital funding from the government and impede QR's ability to replace its assets faster than depreciation.

Inadequate funding to replace the service potential of assets lost through depreciation could increase QR's risk of not replacing assets at the end of their design life.

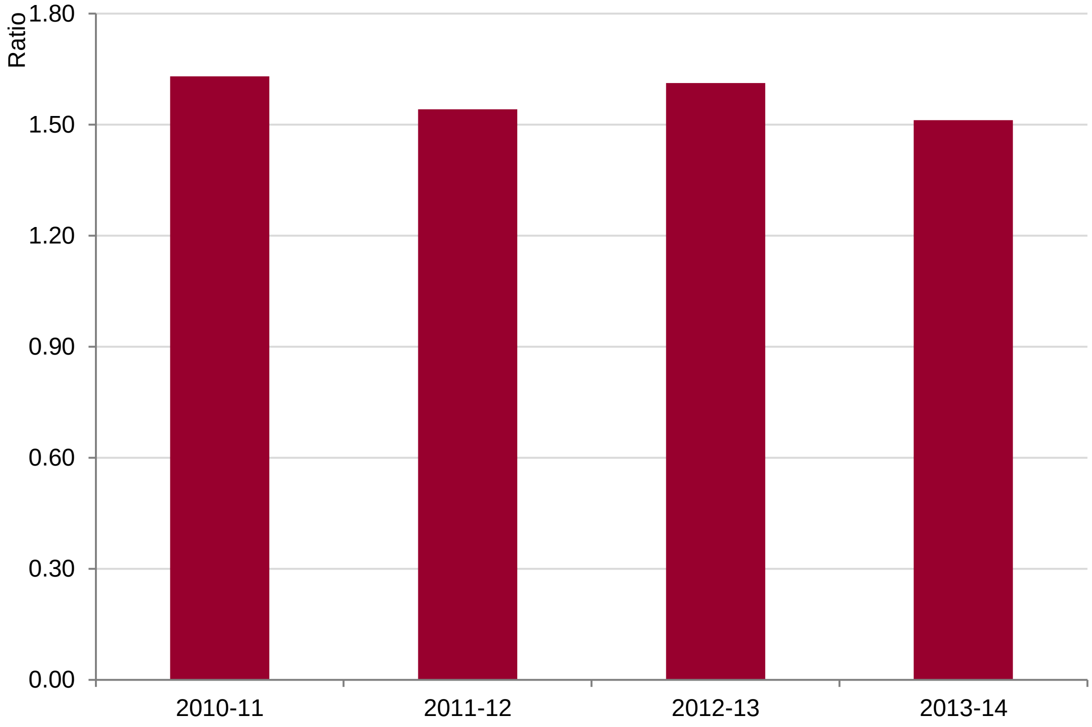
5.6.5 Debt to revenue ratio

QR's debt to revenue ratio has remained steady for four consecutive years. The ratio compares borrowings to revenue and measures the capacity of an organisation to repay debt and interest through its operations. A low ratio indicates financial stability and solvency, whereas a ratio of one and above indicates an organisation may have difficulties servicing its debts. Debt for the purposes of this ratio is borrowings and does not include other liabilities such as trade creditors.

Over the past four years, QR has been highly leveraged with borrowings exceeding its operating revenue. Contributing to this was borrowings of $3 billion Queensland Rail Limited inherited on separation from QR on 30 June 2010. This debt remains unpaid as at 30 June 2014.

Figure 5G shows QR's debt to revenue ratio over the last four years.

Figure 5G
Debt to revenue ratio from 2010–11 to 2013–14



Source: Queensland Audit Office

QR's debt to revenue ratio averaged 1.6 over the past four years. The increase in 2012–13 was due to the additional working capital loan of $100 million QR repaid in full in 2013–14. QR has not raised any significant funds from borrowings in the past four years to fund its operations, including its capital program.

Interest 'bite'

A supplementary measure of debt sustainability relates to an entity's ability to service its debt obligations—to pay interest and to repay or refinance loans when they fall due. The interest expense ratio—'interest bite'—considers the operating revenue required to pay interest charges.

QR recorded total interest expense of $152.8 million in 2013–14 ($699 million in the four years to 30 June 2014).

QR's total interest expense averaged nine per cent of revenue earned across the four-year period. This indicates QR has the financial capability to finance its debts as it uses $9 of every $100 of operating income to repay interest.

Risks to future debt ratios

Any significant reduction of transport services contract revenue will affect QR's future debt to revenue ratio with contractual revenue representing 80 per cent of total operating income.

Loss of network income as a result of operation restructure (such as the potential divestment of the Mt Isa rail line and integration of QR's regional network with the national rail network) present risks to QR's future debt to revenue ratio.

5.6.6 Net flows to and from the government

Figure 5H details net flows of funds between government and QR that significantly affect QR's financial performance and position.

Figure 5H
Flows of funds between government and QR

Accounts	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Flows from government				
Equity contributions	322.9	246.0	—	—
Transport services contract	1 436.5	1 530.3	1 526.6	1 566.7
Flows (to) government				
Dividends declared^	(84.4)	(102.6)	(115.8)	(170.9)
Income tax expense	(12.1)	(57.7)	(56.0)	(96.1)
Competitive neutrality fees	(40.0)	(41.0)	(41.3)	(44.2)
Net flows (to) and from government				
Net flows	1 622.9	1 575.0	1 313.5	1 255.5

^ Dividends declared in 2012–13 and 2013–14 relate to Queensland Rail

Source: Queensland Audit Office

Government provides a net inflow each year due to the transport services contract between QR and the Department of Transport and Main Roads. The contract operated annually for the first time in 2013–14. The contract covers funding for Queensland Rail Limited services associated with rail infrastructure, Citytrain and Traveltrain.

Equity contributions

The state government contributed $569 million to QR in 2010–11 and 2011–12 to construct rail projects under the South East Queensland Infrastructure Plan and Program (SEQIPP) 2010–2031 and other funded rail projects. The 2011–12 injection maintained QR's BBB credit rating. QR recorded non-cash injections of $314 million in 2010–11 as assets transferred from QR Limited as part of the separation.

Transport services contract

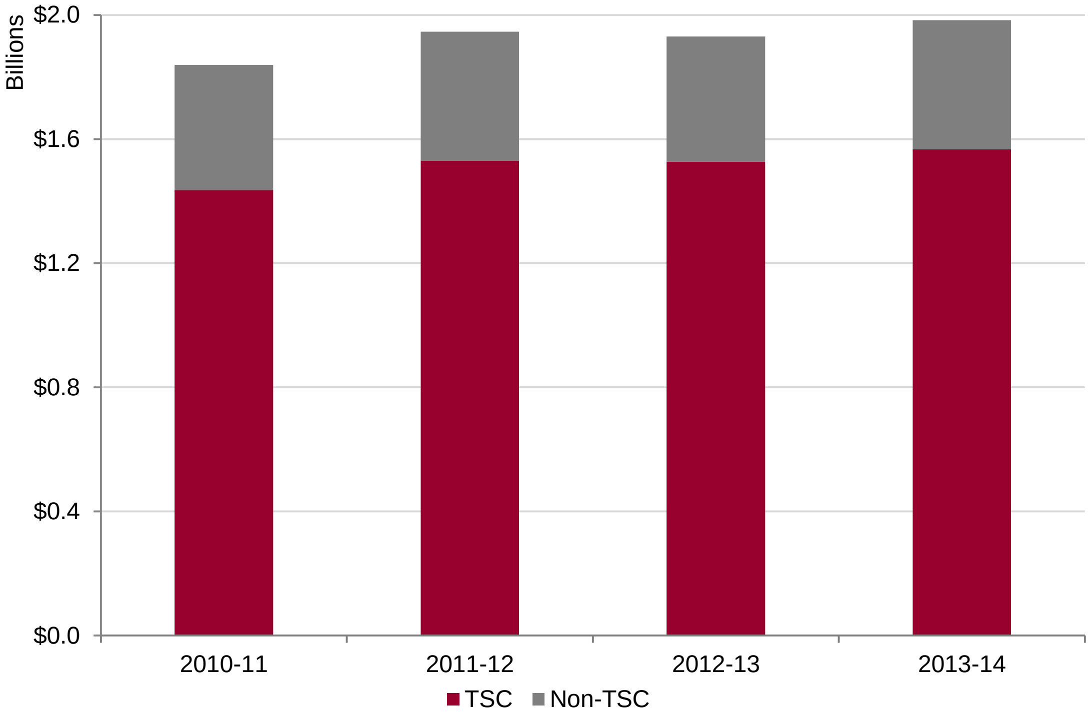
The transport services contract is a service contract for transport outcomes purchased by government under the *Transport Operations (Passenger Transport) Act 1994*.

The purpose of the transport services contract is to improve and sustain the operational performance of the Citytrain passenger rail service; to deliver long distance passenger rail services throughout Queensland; and to deliver the government's rail transport outcomes for rail infrastructure management.

Transport services contract may include community service obligations to deliver a product or service that would be commercially unviable without government compensation.

As Figure 5I shows, contractual revenue comprises nearly 80 per cent of all QR revenue over four years. Any significant decrease in this contribution will affect operating ratio.

Figure 5I
TSC and non-TSC revenue over the four year from 2010–11 to 2013–14



Source: Queensland Audit Office

Competitive neutrality fees

Competitive neutrality means that government businesses should not enjoy any net competitive advantage over their competitors simply as a result of their public sector ownership. QR is the sole operator of passenger train services in south-east Queensland; given QR's vast statewide rail network, the government has imposed competitive neutrality fees to ensure a level playing field between QR and its private sector competitors.

QR has been paying competitive neutrality fees of between $40 million to $45 million for the last four years. On average, the fee was approximately $42 million and, with an average net profit after tax of $159 million over the same period, these fees made up 26 per cent of its profit. Any increase in competitive neutrality fees will affect QR's operating ratio.

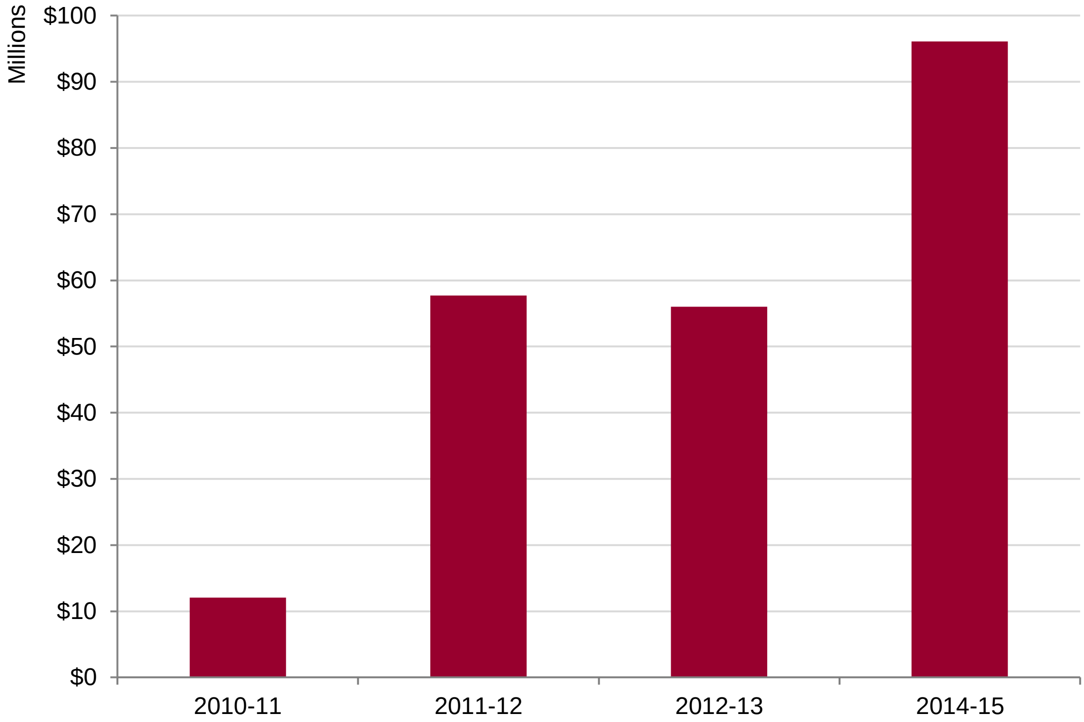
Income tax expense

The Queensland Rail group must make income tax equivalent payments to the Queensland Government on behalf of QR, Queensland Rail Limited and On Track Insurance Pty Ltd Payments are based on the value of benefits derived and rulings set out in the national tax equivalent regime which the Australian Tax Office administers.

These payments are made in line with the *Queensland Rail Transit Authority Act 2013* and instructions from the Treasurer. The national tax equivalent regime gives rise to obligations which reflect, in all material respects, those obligations for taxation which the *Income Tax Assessment Act 1936*, the *Income Tax Assessment Act 1997* and associated legislation would impose, as well as rulings and other Australian Taxation Office pronouncements to determine the tax payable by the group.

Figure 5J highlights the income tax expense the Queensland Rail group paid over four years.

Figure 5J
Income tax expense from 2010–11 to 2013–14



Source: Queensland Audit Office

The amount of income tax paid by the Queensland Rail group in 2010–11 was significantly lower than other years as this was the first year of separation from QR Limited. The national tax equivalent regime had approved the Queensland Rail group using revenue and capital tax losses not used by its former parent. The parent entity did not carry forward these losses when it was privatised in 2009–10. The significant increase in income tax expense in 2013-14 was mainly due to the increase of profit before tax of $109 million.

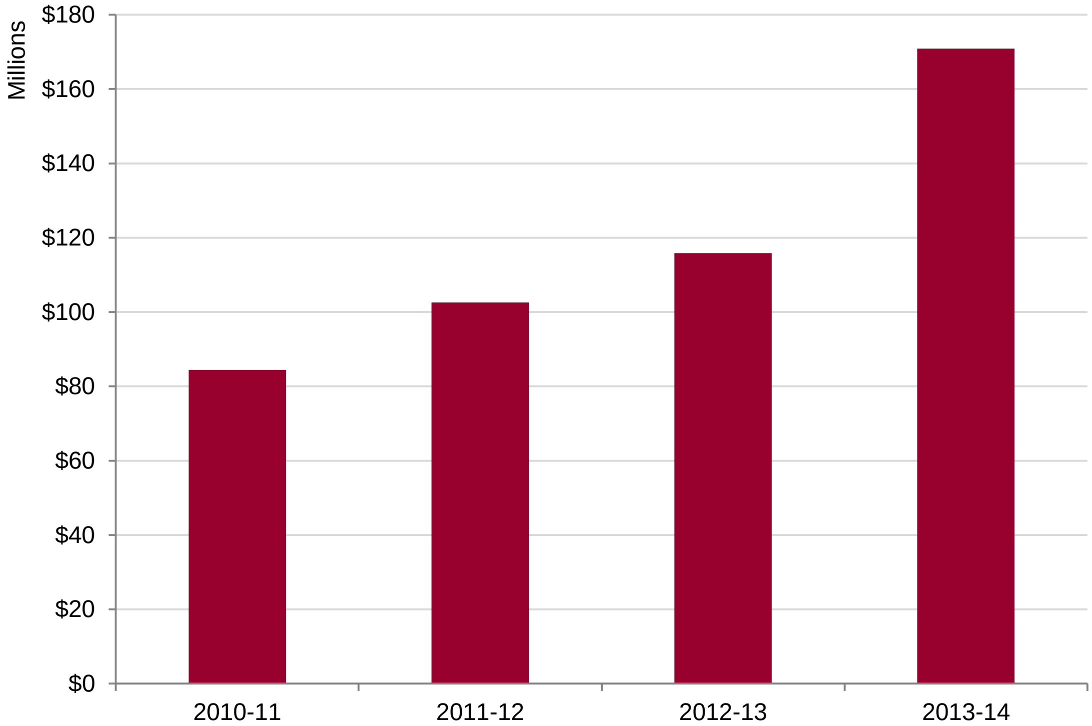
Dividends

QR pays 80 per cent of its net profit after tax as a dividend to the government. In 2013–14, the dividend QR declared to government was significantly higher than previous years, as operating results increased by $69 million. Figure 5K shows QR dividends over four years.

QR declared almost $474 million in dividends over the last four years—nearly $3 million more than estimated. In 2010–11, QR did not achieve its dividend target but it caught up in 2011–12.

The expensing of $54 million in Sunlander project costs was the main reason QR missed its dividend target in 2012–13. QR's continued effort to drive efficiency has provided the platform to exceed its target for the year ended 30 June 2014.

Figure 5K
Dividends provided over four years from 2010–11 to 2013–14



Source: Queensland Audit Office

6 Other public non-financial corporations

In brief

Background

This report scrutinises the financial practices of two other significant Queensland public sector entities classified as public non-financial corporations (PNFCs): Stadiums Queensland and Queensland Treasury Holdings Pty Ltd. Stadiums Queensland manages major sporting and entertainment facilities and Queensland Treasury Holdings Pty Ltd holds investments resulting from the state's privatisation of government assets.

We audited the financial statements of Stadiums Queensland, Queensland Treasury Holdings Pty Ltd and its controlled entities and Parklands Gold Coast Trust.

Conclusions

We issued unqualified audit opinions to each of these other PNFCs for 2013–14.

Stadiums Queensland's early preparation of draft financial reports statements avoided delays and enabled us to agree early on account balances and note disclosures.

The financial reports for Stadiums Queensland and Queensland Treasury Holdings Pty Ltd, including its wholly owned entities, were timely and of good quality.

We assessed the financial sustainability of Stadiums Queensland in terms of ability to operate as a going concern. Stadiums Queensland's future financial sustainability continues to rely on government to fund significant capital works, stadium redevelopment and asset replacement.

Key findings

- We completed audits of financial reports of all other PNFC entities by their legislative deadlines. Queensland Treasury Holdings Pty Ltd and its wholly owned entities did not prepare a draft pro forma financial report for either its Board or audit before 30 June but did produce pro formas for inclusion its parent's pro forma statements
- Parklands Gold Coast Trust ceased operations on 30 September 2013; its assets and liabilities transferred to the Department of National Parks, Recreation, Sport and Racing.
- We found draft financial reports were of good quality and did not require any material adjustments to account balances.
- Stadiums Queensland is financially sustainable while it is funded to pay some, though not all, of its operating commitments and some, but not all, of its short term capital expenditure commitments as and when they are due. Its lack of ability to replace and grow its non-current assets faster than depreciation challenges its financial sustainability. Without continued capital grants, Stadiums Queensland will not maintain or replace its stadium assets in the long term.
- Stadiums Queensland's operating ratio has declined. This is partly due to transfer of its loans from the community investment fund to Queensland Treasury and Trade in 2012–13.
- Stadiums Queensland would have reported positive operating ratios in 2012–13 and 2013–14, had it not recognised depreciation charges, which it is not funded for.

6.1 Background

Other significant Queensland public sector entities classified as public non-financial corporations (PNFCs) are Stadiums Queensland and Queensland Treasury Holdings Pty Ltd (QTH Pty Ltd).

Stadiums Queensland manages, operates and promotes the use of major sporting and entertainment facilities on behalf of the Queensland Government.

QTH Pty Ltd holds residual assets from the state's privatisations and other interests, including state government shares in Aurizon Holdings Ltd (formerly QR Limited).

Figure 6A shows QTH Pty Ltd's consolidated entity corporate structure.

Figure 6A
Queensland Treasury Holdings Pty Ltd consolidated entity structure

Company	Purpose
Parent entity	
Queensland Treasury Holdings (QTH)	QTH holds residual assets resulting from the state's lease of government assets. Queensland's Under Treasurer holds a 60 per cent interest and 76 per cent of the voting rights as trustee for the State of Queensland. Queensland Treasury Corporation holds a further 40 per cent interest and 24 per cent of the voting rights as a corporation sole constituted by the Under Treasurer.
Wholly owned subsidiaries of QTH	
Brisbane Port Holdings Pty Ltd (BPH)	BPH holds Port of Brisbane land assets, acting as port lessor of these leased assets under a long term leasing arrangement.
City North Infrastructure Pty Ltd (CNI)	CNI was established to manage the procurement of the Airport Link, Northern Busway and Airport Roundabout Upgrade projects. In 2013, the state transferred CNI's project and contract management responsibilities to QTH. CNI's remaining activities are to finalise administrative and corporate matters.
DBCT Holdings Pty Ltd (DBCTH)	DBCTH owns and leases Dalrymple Bay Coal Terminal assets.
Network Infrastructure Company Pty Ltd (NWI)	NWI is currently dormant and has not traded since its registration date.
Queensland Airport Holdings (Cairns) Pty Ltd (QAHC), and Queensland Airport Holdings (Mackay) Pty Ltd (QAHM)	The primary objective of both QAHC and QAHM is to hold land, zoned for use as an airport, on behalf of the state. Both entities were established to act as lessors for these leased assets under a long term leasing arrangement.
Queensland Lottery Corporation Pty Ltd (QLC)	On behalf of the state government, QLC holds the Queensland Lottery Licence and Golden Casket brands and trademarks which the Golden Casket Lottery Corporation licenses to Tattersall's Ltd.

Source: Queensland Treasury Holdings Consolidated Group 2013-14 Financial Reports

Parklands Gold Coast Trust ceased operations on 30 September 2013 to make way for site redevelopment of the 2018 Commonwealth Games village.

Excluding Parklands Gold Coast Trust, these other PNFCs have a 30 June balance date.

6.1.1 Entities covered in this chapter

We report the results of our audits of other PNFC entities and entities they control that we have not already reported in the results of audits of the water, energy, rail and ports sectors. Stadiums Queensland and QTH Pty Ltd are the only significant reporting entities we classify as other PNFCs.

QTH Pty Ltd has seven wholly owned subsidiaries. Four of these entities produced financial statements in 2013–14. Three wholly owned subsidiaries were not required to produce financial reports in 2013–14 as Appendix C of this report details.

We performed the final audit of the Parklands Gold Coast Trust as at 30 September 2013.

6.2 Conclusions

An unqualified audit opinion means readers can rely upon the results in the audited financial reports of these entities. We issued unqualified audit opinions of the financial statements of Stadiums Queensland, Parklands Gold Coast Trust, QTH Pty Ltd and four of QTH Pty Ltd's wholly owned subsidiaries: BPH, CNI, DBCTH and QLC.

Three of QTH Pty Ltd's wholly owned subsidiaries—NWI, QAHC and QAHM—were not required to produce financial reports in 2013–14 as Appendix C of this report details.

We included an emphasis of matter in our audit opinion on the financial report of Parklands Gold Coast Trust to highlight the revocation of trust operations and transfer of assets and liabilities on 30 September 2013.

We included an emphasis of matter in our audit opinion on the financial report of QTH Pty Ltd's subsidiary, CNI, to highlight the expected wind down of the company during 2014–15.

We completed audits of all entities by their legislative deadlines.

We concluded Stadiums Queensland's draft financial report was of good quality as it included the Australian Accounting Standard AASB 13 *Fair Value Measurement* disclosure adjustments arising from the review of the pro forma financial report. Applying AASB 13 did not result in any material adjustments to asset valuations.

Overall, these other PNFCs are financially sustainable, but Stadiums Queensland's future sustainability relies on continuing Queensland Government grant funding. QTH Pty Ltd and its wholly owned subsidiaries are financially sustainable: these entities continue to make profits on investment assets and can meet existing borrowing commitments.

Figure 6B provides more detail on significant milestones in our 2013–14 audit of the financial statements of other PNFCs.

6.3 Audit opinions

Figure 6B provides detail on the key milestones in the audit opinions we issued for other entities in 2013–14.

Figure 6B
2013–14 audit opinions issued

Audit	First draft financial report	Financial reports signed	Opinion issued	Certified by deadline	Opinion
Statutory body					
Stadiums Queensland	31.07.2014	26.08.2014	27.08.2014	Yes	Unqualified
Parklands Gold Coast Trust	26.11.2013	28.11.2013	28.11.2013	Yes	Unqualified with an emphasis of matter reference
Other public non-financial corporations and controlled entities					
QTH Pty Ltd	25.07.2014	05.08.2014	12.08.2014	Yes	Unqualified
BPH*	15.07.2014	05.08.2014	12.08.2014	Yes	Unqualified
QLC*	15.07.2014	04.08.2014	11.08.2014	Yes	Unqualified
DBCTH*	17.07.2014	05.08.2014	12.08.2014	Yes	Unqualified
CNI*	04.07.2014	20.08.2014	22.08.2014	Yes	Unqualified with an emphasis of matter reference

* Controlled entity of Queensland Treasury Holdings Pty Ltd
Three of QTH Pty Ltd's wholly owned subsidiaries—QTH, NWI and QAHC/QAHM—were not required to produce financial reports in 2013–14 as Appendix C of this report details.

Source: Queensland Audit Office

6.4 Timeliness and quality of financial reports

6.4.1 Timeliness

To show accountability for the use of public monies, entities should prepare and publish their financial reports as soon as possible after the end of the financial year. The later the financial reports are produced and published after their balance date, the less useful they are for stakeholders and for informing decision making.

Review of pro forma and draft financial reports

Management typically prepares pro forma financial reports for audit by 30 April each year to resolve issues early in the audit process.

Stadiums Queensland provided a pro forma financial report for us to audit on the agreed date of 6 June 2014. Stadiums Queensland applied AASB 13 *Fair Value Measurement* for the first time in 2013–14 and made disclosure adjustments to its draft pro forma financial report before completion. This did not require material adjustments to asset valuations.

QTH Pty Ltd produced pro forma statements for its parent highlighting key changes for 2013-14 for the purposes of consolidation and presentation the parent's pro forma financial statements to its audit committee.

We agree with each entity the due dates they provide draft financial reports for audit through a client strategy document, which we give the entity at the end of our planning visit, confirmed with a letter to the entity before our final visit for the audit year.

All reporting entities to whom we issued an unqualified opinion submitted draft financial reports to us by the agreed date.

Certification of financial reports by legislative deadline

Statutory bodies must have their financial reports prepared and audited no later than 31 August each year. Large public companies limited by shares are required to have their financial reports prepared and audited no later than 31 October each year.

Management and audit certified the financial reports for all seven entities required to produce financial reports in 2013–14 by their legislative deadlines.

6.4.2 Quality and accuracy

We found draft financial reports and supporting work papers was of good quality.

Material financial report adjustments

None of the seven entities required to produce financial reports in 2013–14 required any material management or audit initiated adjustments to their draft financial reports.

Prior period adjustments

Stadiums Queensland corrected a prior year error of $2.742 million in the statement of financial position relating to the incorrect recognition of a Queensland Treasury and Trade loan liability. Although the loan was provided at below market interest rates, it should have been recognised in the financial report at fair value on inception in accordance with *AASB 139 Financial Instruments: Recognition and Measurement.*

6.5 Significant financial reporting issues

Australian Accounting Standard AASB 13 *Fair Value Measurement* affects entities for reporting periods commencing on 1 January 2013. The requirements of AASB 13 affected the financial report of Stadiums Queensland.

AASB 13 refines the financial report requirements around measurement criteria of an asset measured on a fair value basis. It also introduces significant new disclosure requirements, depending on the observable and unobservable inputs used in the valuation process.

The valuation of assets under AASB 13 involves considering and quantifying management assumptions and estimates. Management's assumptions and estimates can affect final asset valuations significantly.

Although applying AASB 13 did not require Stadiums Queensland to make material adjustments to asset valuations, Stadiums Queensland disclosed additional information on the observable and unobservable inputs used in the valuation process.

6.6 Financial performance, position and sustainability

When forming an audit opinion on the financial report, we must assess the entity's ability to continue and operate as a going concern. We also assess its financial performance, position and financial sustainability.

Our assessment of their financial sustainability includes an assessment of three key ratios—operating, capital replenishment, and debt to revenue ratios. Taken together, these ratios indicate their ability to pay ongoing expenses, replace and grow assets, and pay debts as and when they fall due. We also assess flows to and from the government as part of this assessment.

Stadiums Queensland's financial sustainability depends on continued government funding.

We excluded QTH Pty Ltd and its subsidiaries from our financial sustainability assessment. These entities hold the residual assets from the state's investments and residual holdings in previously sold or leased assets and other factors, such as the decisions of government as the ultimate shareholder, influence the going concern nature of these entities.

We also excluded Parklands Gold Coast Trust as it ceased operating 30 September 2013.

6.6.1 Financial performance and position

Financial performance and position in any year are important indicators of an entity's overall financial health. We also consider recent experiences to discern any relevant trends.

Figures 6C and 6D provide overviews of the financial performances and positions of Stadiums Queensland and QTH Pty Ltd over the past five years.

Figure 6C
Financial performance and position —Stadiums Queensland

Accounts	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Factors affecting financial performance					
Revenue	178.75	162.26	136.08	113.02	78.36
Expenses	143.49	142.94	143.22	164.34	123.85
Profit/(Loss) after tax	35.26	19.33	(7.15)	(51.32)	(45.49)
Factors affecting financial position					
Assets	1 295.60	1 274.15	1 207.40	1 145.13	1 105.20
Liabilities	482.14	510.16	477.56	145.62	141.96
Equity	813.46	763.99	729.84	999.51	964.24

Source: Queensland Audit Office

Figure 6D
Financial performance and position—Queensland Treasury Holdings Pty Ltd

Accounts	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Factors affecting financial performance					
Revenue	1.04	697. 91	80.13	382.02	189.68
Expenses	0.09	71. 32	139.68	141.57	53. 35
Share of profit of equity accounted joint venture	0.18	0.59	-	-	-
Income tax expense/(credit)	0.02	187.98	(41.20)	70.56	41.41
Profit/(Loss) after tax	1.11	439. 21	(18.36)	169.89	94.92
Factors affecting financial position					
Assets	27.90	3 146.17	3 288.77	1 223.95	686.73
Liabilities	0.02	2 584.67	2 823. 63	588.92	216 .78
Equity	27.88	561. 50	465.14	635.03	469.95

Source: Queensland Audit Office

6.6.2 Financial sustainability

We assess financial sustainability through three key ratios—operating, capital replenishment and debt to revenue ratios. These ratios indicate an entity's ability to pay ongoing expenses; replace and grow assets; and pay debts as and when they fall due. We also assess flows to and from the government.

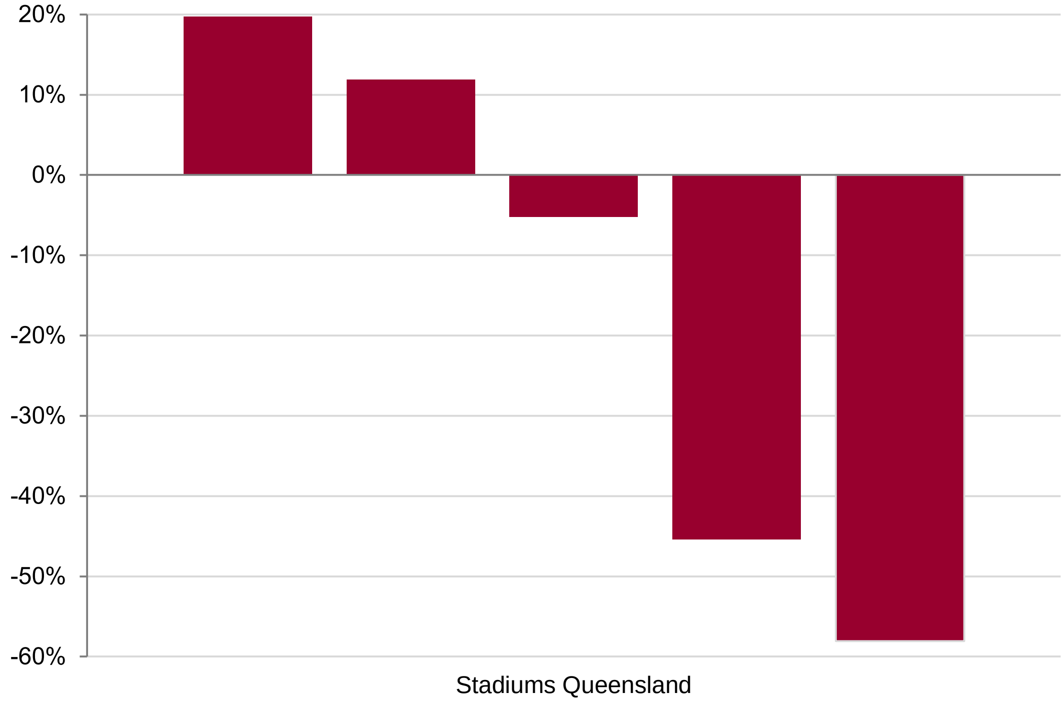
We assessed Stadiums Queensland as financially sustainable as long as government funding continues.

6.6.3 Operating ratio

The operating ratio represents operating profit after tax as a proportion of total revenue. It should be positive over the medium to long term for the entity to remain financially sustainable. Ongoing negative ratios indicate net losses, where revenue is insufficient to fund operating and future capital expenditure. This depletes cash reserves, increases borrowings and may compromise an entity's asset investment and service.

Figure 6E illustrates the operating ratios of Stadiums Queensland over five years.

Figure 6E
Stadiums Queensland operating ratios from 2009–10 to 2013–14



Source: Queensland Audit Office

Stadiums Queensland is not generating sufficient revenue to fund operating and future capital expenditure. Reduced government grant funding has influenced negative ratios reported in the past two years.

Stadiums Queensland's operating ratios have declined over the last five years.

Gifting of pedestrian access assets that Stadiums Queensland constructed for $10.6 million to the Department of Transport and Main Roads; reduced government funding; and the cessation of CIF funding for CIF loans which were transferred to Queensland Treasury and Trade on 30 June 2013, all contributed to the negative results in 2013–14.

The negative results in 2012–13 were due to reduced capital grant funding and the gifting to other government bodies of Stadiums Queensland's assets worth $27.9 million.

Stadiums Queensland achieved positive operating ratios in 2010–11 and 2009–10 through project specific funding.

Cumulative losses in these two years of $96.6 million approximate the unfunded depreciation charges of $102.2 million over the same period. Stadiums Queensland is not funded for depreciation charges.

Risk to future operating ratios

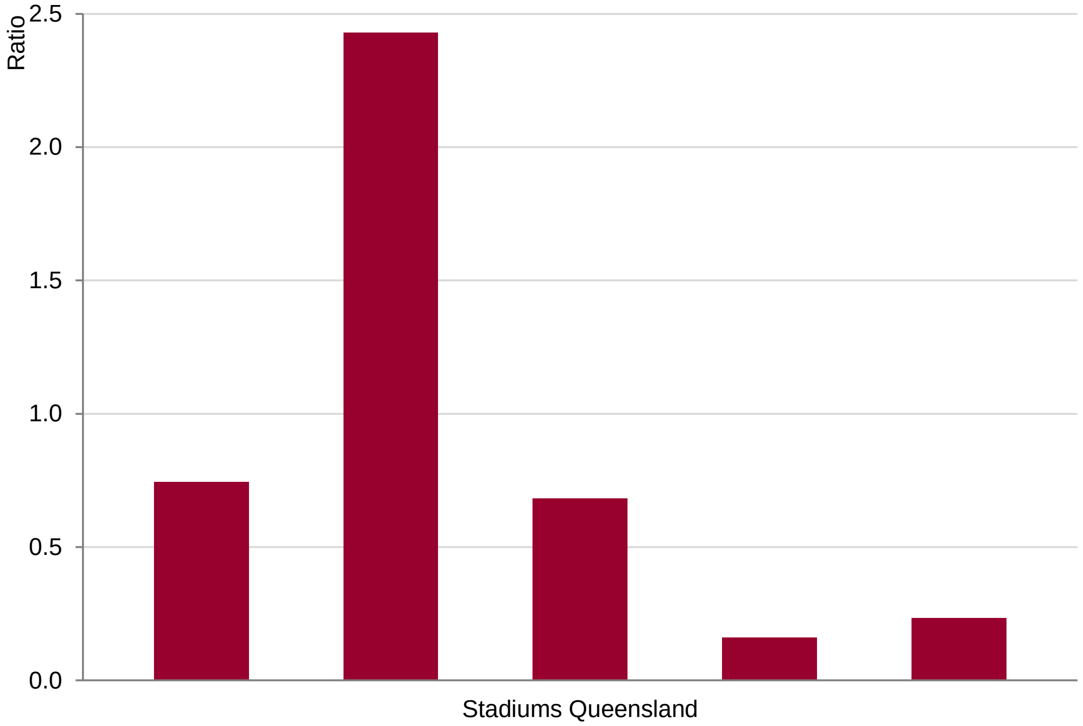
Stadiums Queensland relies on Queensland Government operating grants to meet venue maintenance costs, insurance and property costs as well as the cost of operating community use venues. Any changes to the funding arrangements may affect the future operating ratios of Stadiums Queensland.

6.6.4 Capital replenishment ratio

The capital replenishment ratio compares the annual net expenditure on non-current assets to annual depreciation. An average ratio below one, over time, indicates assets are being built or replaced slower than they are depreciating.

Figure 6F shows the results of our analysis of the capital replenishment ratio.

Figure 6F
Stadiums Queensland capital replenishment from 2009–10 to 2013–14



Source: Queensland Audit Office

Stadiums Queensland is not growing or replacing its stock of non-current assets faster than assets are depreciating, recording capital replenishment rates of less than one in most of the last five years.

Completion of the $144.2 million Metricon stadium at Carrara, Gold Coast affected the 2010-11 result.

In 2013–14, Stadiums Queensland gifted infrastructure assets to the Department of Transport and Main Roads of $10.7 million and, in 2012–13, gifted $27.9 million of pedestrian infrastructure assets to Brisbane City Council, Queensland Rail and the Department of State Development, Infrastructure and Planning.

The capital replenishment ratio should be read in the context of assets under construction Stadiums Queensland gifted, even though this had a negligible effect on Stadiums Queensland's capital replenishment ratios.

Risks to future capital replenishment ratios

Although Stadiums Queensland's capital replenishment ratio has declined to under one from 2011–12 year, it has strategies to mitigate the deteriorating capital replenishment ratio. These strategies focus on longer term asset protection to prolong the life of the assets and delay the need to build new replacement facilities.

Stadium Queensland conducts ongoing asset maintenance, refurbishments and upgrades.

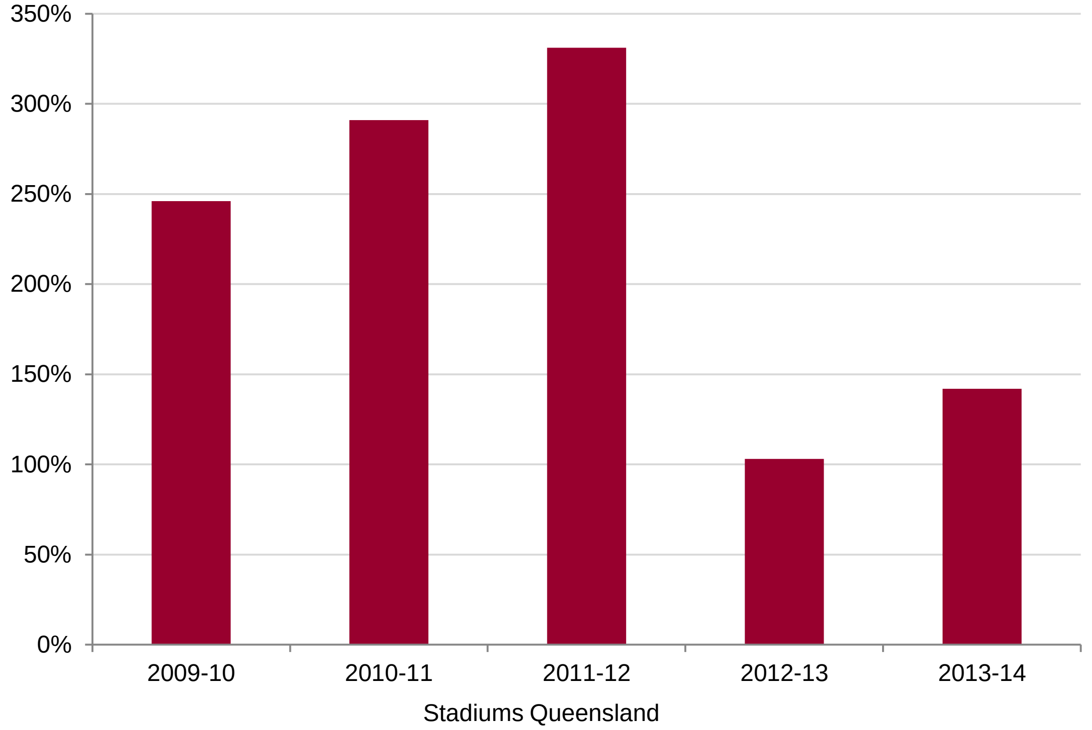
Stadiums Queensland insures assets to provide maximum coverage and mitigate asset management risks; for example, Stadium Queensland's insurance policy covered both Suncorp Stadium and Queensland Tennis Centre for repairs following the 2011 floods.

6.6.5 Debt to revenue ratio

The debt to revenue ratio assesses an entity’s ability to pay principal and interest on borrowings when they fall due from the funds the entity generates. Debt for the purposes of this ratio is borrowings and does not include other liabilities such as trade creditors.

Figure 6G shows Stadiums Queensland's debt to revenue ratio.

Figure 6G
Debt to revenue ratio—Stadiums Queensland



Source: Queensland Audit Office

Stadiums Queensland relies on Queensland Government grants to service its loans.

Interest 'bite'

Debt sustainability can be measured by an entity's ability to service its debt obligations—to pay interest and to repay or refinance loans when they fall due. The interest expense ratio—'interest bite'—considers the operating revenue required to pay interest charges.

Stadiums Queensland recorded interest expense on its borrowings of $7.3 million in 2013-14 ($119.3 million in the five years to 30 June 2014). When loans for the redevelopment of Suncorp Stadium, stage 6 of the Gabba redevelopment and construction of Cbus Super stadium of $306.6 million with the community investment fund transferred from Stadiums Queensland to Queensland Treasury and Trade in the calendar year of 2013, interest expense fell by 10 per cent to 6 per cent of Stadium Queensland's total operating costs in 2013–14.

Risks to future debt ratios

Stadiums Queensland has interest bearing loans of $111.2 million as at 30 June 2014: variable rate interest loans with Queensland Treasury Corporation and a fixed interest rate loan with Queensland Treasury and Trade.

Stadiums Queensland depends on Queensland Government operating grants to assist with servicing selected operational costs. Any changes to the funding arrangements may affect its ability to service future loan repayments.

6.6.6 Net flows to and from government

Flows to and from government affect an entity's ability to meet its expenditure commitments; replace and grow its asset base; and repay debt. PNFCs pay dividends, income tax and competitive neutrality fees to the government and receive government funding for certain activities and equity contributions that government invests in.

We assess the effects of these net flows on the entities' financial performance, position and sustainability.

Flows from the government support Stadiums Queensland's financial performance, position and sustainability through operating and capital grants received over the last five years.

QTH Pty Ltd has contributed equity, dividends, and income tax to the state government across the same period.

Other PNFCs in this sector recorded net flows from the government of $13.2 million in the five years to 30 June 2014.

Figure 6H outlines the flows between these other PNFCs and government over five years.

Figure 6H
Flows to and from the government 2009–10 to 2013–14

Accounts	2009–10 $ m	2010–11 $ m	2011–12 $ m	2012–13 $ m	2013–14 $ m
Flows from government—Stadiums Queensland					
Equity contributions	—	2.26	—	306.59	—
State government grants	84.86	82.95	74.62	65.81	32.14
Flows from / (to) government—QTH Pty Ltd					
Dividends declared	—	—	(78.00)	—	(260.00)
Income tax (expense) credit	(0.02)	(187.98)	41. 20	(70.56)	(41.41)
Net flows from / (to) government					
Net flows	84. 84	(102. 77)	37.82	301.84	(269.27)

Source: Queensland Audit Office

Equity contributions

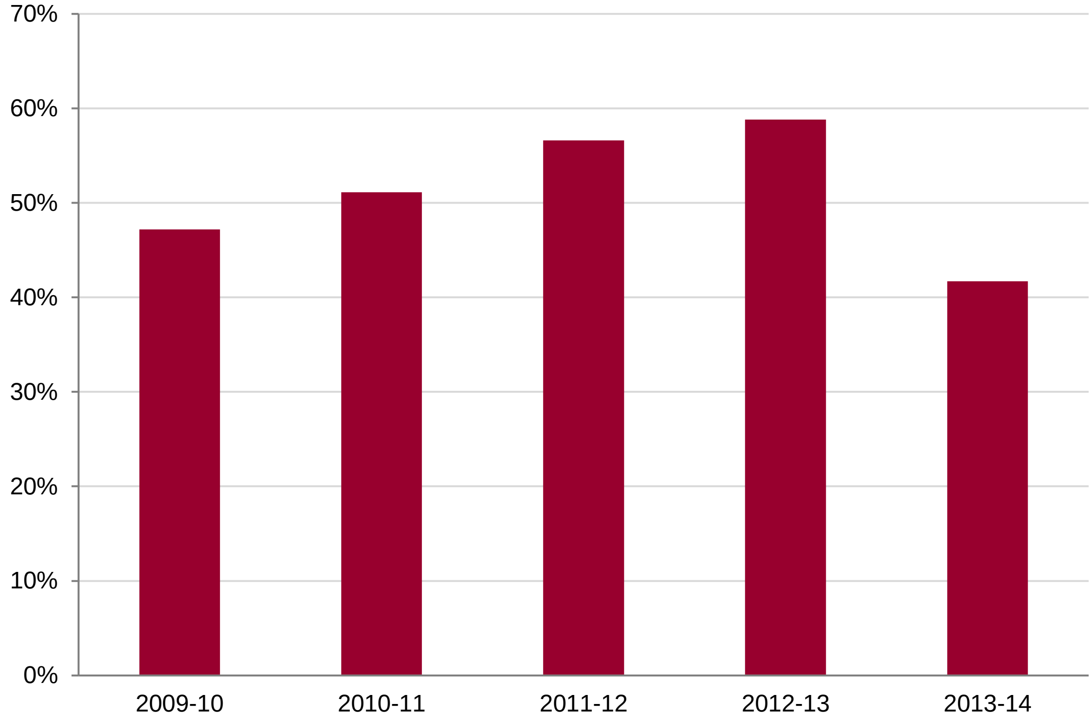
Stadiums Queensland received an equity contribution of $306.6 million on 18 June 2013 to account for a non-reciprocal transfer of its loans with the community investment fund to Queensland Treasury and Trade.

Otherwise, equity contributions have had negligible or no effect on the financial sustainability of Stadiums Queensland across the period.

State government grants to Stadiums Queensland

Government grant revenue has affected the operating ratios of Stadiums Queensland over the past five years. As Figure 6I shows, government grant revenue represents a significant a proportion of total revenue. The reduction in the level of government grant revenue by 2013-14 to $32 million reflects the reduced level of debt that Stadiums Queensland is now required to service.

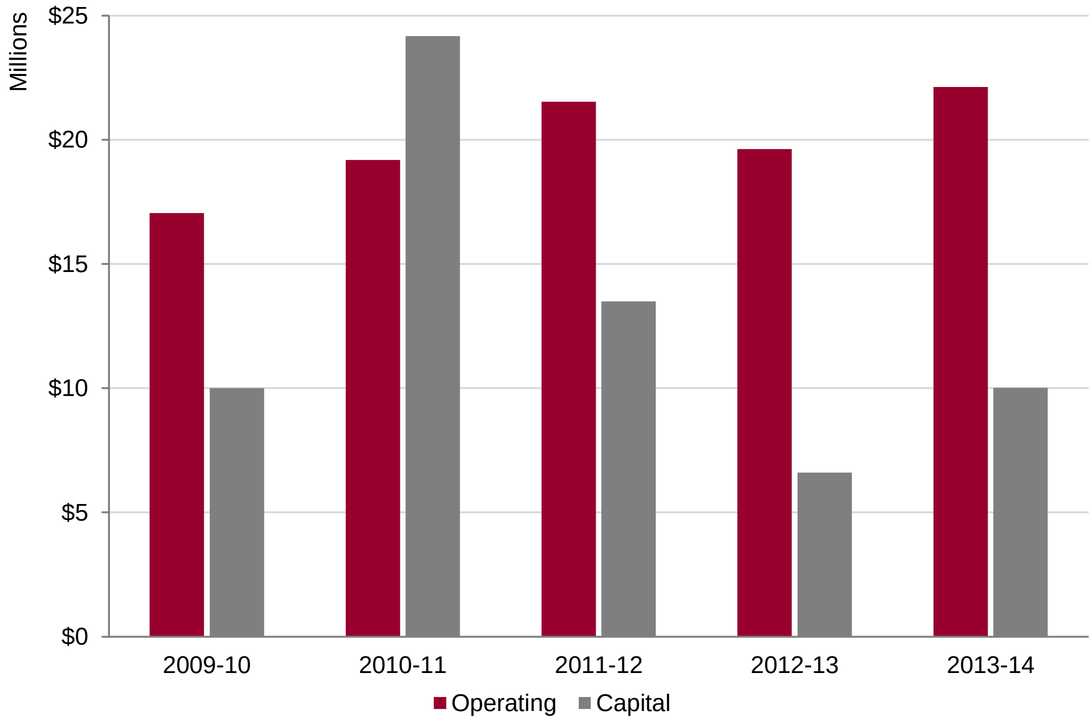
Figure 6I
Stadiums Queensland grant revenue as a percentage of total revenue for 2009–10 to 2013–14



Source: Queensland Audit Office

As Figure 6J shows, capital funding for Stadiums Queensland over five years has varied with projects, from a high of $24 million in 2010–11 to a low of $6.6 million in 2012–13. Although capital funding affects operating ratios, it also affects the capital replenishment ratio.

Figure 6J
Stadiums Queensland operating and capital grants for 2009–10 to 2013–14



*Source: Queensland Audit Office**

Competitive neutrality fees

Other PNFC entities did not pay competitive neutrality fees to government.

Income tax expense

QTH Pty Ltd is subject to the national tax equivalents regime and must pay income tax. Income tax equivalents can affect QTH Pty Ltd's financial sustainability.

QTH Pty Ltd paid income tax of $259 million to government over the last five years—38 per cent of net profits over the same period.

During 2013–14, QTH Pty Ltd sold 134.3 million shares in Aurizon Holdings Limited for gains of $305.2 million ($89.0 million in 2013–14 and $216.2 million from prior years). QTH Pty Ltd applied these net proceeds to repay its debt with Queensland Treasury Corporation and paid the remainder to the state through dividend and taxes.

Dividends

Dividends QTH Pty Ltd paid to the government have not affected its financial sustainability.

QTH Pty Ltd paid dividends of $338 million to government over the last five years—half of cumulative after tax profits it made over that time.

Appendices

Appendix A—Comments

In accordance with section 64 of the *Auditor-General Act 2009*, we provided a copy of this report or parts of this report to a number of entities and parties with a request for comment; the option of providing comments; and for their information.

We provided a copy of this report to the Minister for Energy and Water Supply; Minister for Transport and Main Roads; Minister for National Parks, Recreation, Sports and Racing with a request for comment.

We provided relevant parts of this report to the heads of the following entities / person with an option of providing a response:

- Stanwell Corporation Limited
- CS Energy Limited
- Queensland Electricity Transmission Corporation (trading as Powerlink)
- Ergon Energy Corporation Limited
- Energex Limited
- Queensland Bulk Water Supply Authority (trading as Seqwater)
- SunWater Limited
- Gladstone Area Water Board
- Mount Isa Water Board
- Far North Queensland Ports Corporation Limited (trading as Ports North)
- Gladstone Ports Corporation Limited
- North Queensland Bulk Ports Corporation Limited
- Port of Townsville Limited
- Queensland Rail
- Stadiums Queensland
- Queensland Treasury Holdings Pty Ltd
- Department of Transport and Main Roads
- Department of Energy and Water Supply
- Department of National Parks, Recreation, Sports and Racing
- Under Treasurer, Queensland Treasury and Trade

We provided a copy of this report to the Premier; the Treasurer and Minister for Trade; the Director-General, Department of the Premier and Cabinet; and the Chief Executive Officer, Queensland Competition Authority for their information.

We have considered all views provided to us in reaching our audit conclusions and these are represented to the extent relevant and warranted in preparing this report.

Responsibility for the accuracy, fairness and balance of the comments rests with the head of these agencies. Appendix A of this report includes comments we received within 21 days.

Comments received from Chairman, CS Energy

Ref B/D/14/33801
Letter No: 11128

18 November 2014

Mr A Greaves
Auditor-General
Queensland Audit Office
PO Box 15396
CITY EAST QLD 4002

Dear Mr Greaves

RE: Results of Audit: Public Non-Financial Corporations

Thank you for providing the draft report to Parliament on the *2013-14 Results of audit: Public non-financial corporations* for comment. CS Energy notes the substantial and important role the Auditor-General and its officers have in ensuring all public entities meet the standards expected of them in reporting and in the management of the funds entrusted to them by the taxpayers of Queensland.

CS Energy has been working with the Auditor-General's office to ensure that the report is a true and accurate representation, not only of its position individually, but also its position in relation to the other organisations to which CS Energy is compared in the report.

The report notes as an objective to assess the financial sustainability of the entities including an entity's ability to pay its ongoing expenses, replace and grow its assets, and pay its debts as and when they fall due. The report utilises three key ratios to assess corporation sustainability—operating ratio, capital replenishment ratio and the debt to revenue ratio. CS Energy notes the operating ratio and debt to revenue ratio utilises operating revenue as the denominator in the respective calculations.

One of the more problematic issues in the report is the inclusion of accounting adjustments in the operating revenue calculation. CS Energy is focused on delivering underlying business improvement. Underlying business improvement is normally measured on earnings performance, excluding the accounting adjustments; ie reflecting the cash generation capability of the organisation. Given the significant write-up of assets in FY2014, and the report's inclusion of these in operating revenue, large changes in ratios occur that are not reflective of the underlying performance, potentially distorting the true performance of the business.

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CS Energy Ltd ABN 54 078 848 745 www.csenergy.com.au

Comment received from Chairman, CS Energy

- 2 -

There are several other matters that make sensible comparison in the report difficult, and which CS Energy believes should be highlighted. Although the report recognises these issues in the commentary to varying extents, it is important to clarify CS Energy's position in relation to these matters, specifically:

1. The **lack of comparability of the periods prior to the Generator Restructure effected 1 July 2011 and the periods subsequent to this** – the restructure of the assets fundamentally changed the mix of assets held by CS Energy and included the transfer of large cash imposts to CS Energy such as the Gladstone Onerous Contract Arrangements. These periods, although presented in the same charts and diagrams, should not be compared to each other due to a number of material differences in the portfolios;

2. **Comparison of Generator and Network Business** - the generation businesses operate in a competitive National Electricity Market where the returns of the generators are subject to the market forces of demand and supply. The network business of Ergon, Energex and Powerlink are regulated monopoly businesses, which have largely fixed returns, as determined by the regulatory undertakings set by the Australian Energy Regulator. Network and Generation businesses have fundamentally different capital structures, reflecting the inherently different risk profiles of each type of business. This is not entirely obvious in the presentation of information throughout the report, and CS Energy believes it would have been more appropriate to completely separate the Network and Generation businesses in the report, rather than purporting to compare the two; and

3. **Carbon impact on operating revenue** during FY2013 and FY2014 – the introduction of the carbon tax resulted in an increase in the pool price and thus the operating revenues of the corporation. The cost for the carbon tax, which in CS Energy's case exceeded any revenue collected, is reflected in the operating expenses. Given the carbon uplift in the revenue is included in the operating revenue but not the costs, this results in an improvement in the Debt to revenue ratio which is not consistent with underlying performance. Given the uplift from carbon in the operating revenue line (which in fact resulted in negative financial performance) the QAO highlights improved ratios over the period. Comparing FY2013 and FY2014 to the other financial years is not valid for the debt to revenue ratio.

CS Energy believes that these issues potentially invite comparisons which are not appropriate, or may lead the reader to draw inaccurate conclusions on the performance of the business. These concerns have been expressed to QAO, who have sought to clarify some of these issues in the report.

Yours sincerely

Ross Rolfe
Chairman CS Energy

Comments received from Chairman, Ports North

Ports North

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RECEIVED
17 NOV 2014
QUEENSLAND AUDIT OFFICE

13 November 2014

Mr Andrew Greaves
Auditor General
Queensland Audit Office
PO Box 15396
CITY EAST QLD 4002

Dear Mr Greaves,

RESULTS OF AUDIT PUBLIC NON-FINANCIAL CORPORATIONS

Thank you for your letter of 24 October 2014 and the attached document. Taking into account the amendments confirmed by your staff in the email of 7 November 2014, Ports North's Board welcomes the report as a valuable contribution to improving the quality of financial reporting by Public Non-Financial Corporations. We have no specific issues to raise concerning the content of the report.

I would like to take the opportunity to thank the Queensland Audit Office (QAO), its staff and contractors for the professionalism displayed in the conduct of Ports North's annual audit and for the positive client engagement process you have undertaken in the preparation of this report.

If you wish to discuss further any of the above issues or require further information please contact our Chief Financial Officer, Nick Good, on the number below.

Yours sincerely

Brett Moller
CHAIRMAN

Enquiries: Nick Good, (07) 4052 3821
Email: nick.good@portsnorth.com.au

Cairns | Cape Flattery | Karumba | Mourilyan | Skardon River | Quintell Beach | Thursday Island | Burketown | Cooktown

Comments received from Chairman, Queensland Rail

QueenslandRail

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19 November 2014

CONFIDENTIAL

Mr Andrew Greaves
Auditor-General
Queensland Audit Office
PO Box 15396
City East QLD 4002

PROPOSED AUDITOR'S-GENERAL REPORT TO PARLIAMENT
RESULTS OF AUDIT PUBLIC NON-FINANCIAL CORPORATIONS – RAIL SECTOR

Dear Mr Greaves

Thank you for your updated proposed report in relation to the "Results of Audit: Public Non-Financial Corporations" (Draft Report) received on 19 November 2014.

We appreciate the engagement by the Queensland Audit Office ("QAO") and the consideration to our additional information provided to your office on 13 November 2014, as reflected in your amended Draft Report.

We maintain the view that Queensland Rail has been focused on optimising its capital investment by focusing on core operational deliverables and that the downward trend in the capital replenishment ratio is not a future risk to the replacement of non-current assets for the rail sector in Queensland. We understand that this is a Public Non-Financial Corporations Report and therefore excludes capital investment in the rail sector by the State through the Department of Transport and Main Roads for Moreton Bay Rail Link and New Generation Rollingstock. We note that your report now recognises that the capital expenditure for the NGR project will help replenish QR's existing rail assets and help offset the downward trend in the capital replenishment ratio.

The Board and senior management again thank you for considering our previous response to the initial Draft Report and reflecting some of our comments into the current Draft Report.

If you require further clarification in relation to any of the comments in this letter, please contact Helen Gluer, Chief Executive Officer, or Mark Hope, Chief Financial Officer.

Yours sincerely

Michael Klug AM
Chairman
Queensland Rail

The Queensland Rail Group including Queensland Rail (ABN 88 098 268 528) and Queensland Rail Limited (ABN 71 132 181 090)

Comments received from Chief Executive, Stadiums Queensland

Stadiums Queensland

Your ref: 2014-7451
Our ref: FIN-70-19

Stadiums Queensland
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Queensland 4102 Australia

Telephone +61 7 3008 6100
Facsimile +61 7 3008 6161

ABN 53 690 873 374

20 November 2014

Mr David Adams
Director of Audit
Queensland Audit Office
PO Box 15396
City East Qld 4001

Dear Mr Adams

In response to your e-mail of 20 November, 2014, please find below a concise response to the draft 2013-2014 Public non-financial corporations report:

> The financial sustainability of Stadiums Queensland (SQ) is no different to venue owners nationally and internationally. Sports stadia do not generate a profit because the costs of operating, maintaining and replacing assets exceed what can be derived from income due to the infrastructure being used on a weekly, fortnightly or seasonal basis rather than a daily basis. The inability to generate profit and achieve a return on capital is why so few stadia are owned by the private sector and why the Queensland Government provides both capital injections and grants to sustain the operation of these facilities. The Queensland Commission of Audit – Final Report, Part C Financial Management, C2.6 Major Stadiums states:
>
> *"Stadiums provide venues for sporting, cultural and community events. Public ownership of major stadiums is common around the world. At the very least, governments play a critical role in the funding of stadium developments.*
>
> *Historically, there has been little interest in private sector development and management of major stadiums around the world. Private investors rarely find major sports stadiums an attractive investment, because of the difficulty of earning an acceptable rate of return on the investment.*
>
> *In the absence of private sector interest, public development and ownership of sport and entertainment stadiums has been undertaken to achieve the following outcomes:*
>
> - *increasing tourism and consequential tourist dollars being spent in Queensland*
> - *major events attracting global and domestic awareness thereby leading to long-term position impacts for tourism*
> - *growth and development of business activity, investment and employment in local areas*
> - *development of community pride and providing greater choice in leisure activities."*

great venues. good times.

Comments received from Chief Executive, Stadiums Queensland

While SQ always seeks to increase the utilisation of its venues, there is a finite number of enterprises able to sustain the scale of events that require venues of the capacity of SQ's portfolio. They comprise major sports franchises or entertainment products specially designed for stadia such as high profile performers, motocross/motorcycle or monster truck events or major community festivals. As far as major sports franchisees are concerned many face the challenge to sustain themselves financially as it is. In relation to non-sport major events, the costs of production are so great that there is not a plethora of events for any venue to attract.

Further, two of the nine SQ venues are predominately community use venues (Queensland Sport and Athletics Centre and the Sleeman Sports Complex) which are used extensively for school sports carnivals, elite training and to foster participation in sport. There is little (if any) ability to attract events and users that provide a commercial return. The majority of the users participate in sport and recreation pursuits operated under the auspices of State Sporting Associations which are already heavily funded by government grants.

The cost of services for community use cannot be recovered in full due to the very nature of the services. SQ receives very minimal income and bears the full cost of community use. SQ does not receive and has never received Community Service Obligation (CSO) funding for those community use venues from the government.

SQ receives annual operating grants from the government to help meet the venue maintenance costs, insurance and property costs including Land Tax payments as well as the costs of operating the Sleeman Sports Complex and Queensland Sport and Athletics Centre. A specific operating grant is also provided to fund the loan repayments for the Metricon Stadium redevelopment.

The capital grant provided by the government assists SQ with asset replacements, refurbishments, upgrades and to maintain venues to the standard required to host international events and ensure compliance with legislative requirements. This funding does not offset SQ's annual depreciation charges. Therefore, it is anticipated future significant capital replacements, redevelopments and construction similar to Metricon Stadium, Suncorp Stadium and Gabba redevelopments will be funded by the government via special funding or loan facility.

The following table provides information on the Queensland Government funding for the last five years.

2

Comments received from Chief Executive, Stadiums Queensland

Queensland Government Grants to Stadiums Queensland and % of Total Revenue

	2009-10	2010-11	2011-12	2012-13	2013-14
	$000	$000	$000	$000	$000
Queensland Government Operating Garnts	17,046	19,183	21,534	19,631	22,128
Queensland Government Capital Grants	10,000	24,181	13,500	6,600	10,014
Community Investment Fund Receipts	57,818	39,583	39,583	39,583	-
Total Queensland Government Grants	84,864	82,947	74,617	65,814	32,142
Total Revenue	178,753	162,260	136,059	112,579	78,856
Queensland Government Grants as a % of Total Revenue	47%	51%	55%	58%	41%

SQ was required to borrow for the redevelopment and construction of Suncorp Stadium, The Gabba, Queensland Tennis Centre, Cbus Super Stadium and Metricon Stadium. The borrowings/ loans have been serviced from SQ operations, Community Investment Funds (CIF) and specific operating grants from the government.

On 1 July 2013, the CIF was abolished by the government and the Suncorp Stadium, Gabba and Cbus Super Stadium CIF loans of $306.6 million were transferred via contributed equity to Queensland Treasury and Trade on 30 June 2013.

SQ's total loans at 30 June 2014 amounted to $111.2 million. Approximately 49% of this debt is serviced by annual government grants of $5.4 million and the balance of the loans (51%) are serviced from revenue from venue operations.

Yours sincerely

Kevin Yearbury
Chief Executive

3

Appendix B—Financial sustainability measures

Figure B1 details the ratios we used to assess the financial sustainability of Public non-financial corporations covered in this report.

Figure B1
Financial sustainability measures

<table>
<tr><th>Measure</th><th>Formula</th><th>Description</th><th>Target range</th></tr>
<tr><td rowspan="2">Operating ratio</td><td>Net operating result after tax divided by total operating revenue.
Expressed as a percentage.</td><td>Indicates the extent to which operational revenues raised cover operational expenses.</td><td>Needs to be developed by individual entities and reported against at regular intervals.</td></tr>
<tr><td colspan="3">A negative result indicates an operating loss. The larger the negative percentage the worse the result. Operating losses cannot be sustained in the long term.
A positive percentage indicates that surplus revenue is available to support the funding of capital expenditure, or to be held in reserve to offset past or expected future operating losses.</td></tr>
<tr><td rowspan="2">Capital replenishment ratio</td><td>Annual net expenditure on non-current assets divided by depreciation expense.
Expressed as a number.</td><td>Comparison of the rate of net spending on assets with depreciation.</td><td>Needs to be developed by individual entities and reported against at regular intervals.</td></tr>
<tr><td colspan="3">A ratio greater than one means that an entity is replacing and/or growing its property, plant and equipment and intangible asset base at a rate faster than it is being depreciated and amortised.</td></tr>
<tr><td rowspan="2">Debt to revenue ratio</td><td>Total loans and borrowings at 30 June divided by total operating revenue that year.
Expressed as a percentage or number.</td><td>Indicates the extent to which its operating revenues (including grants and subsidies) can cover an entity's loans and other borrowings.</td><td>Needs to be developed by individual entities and reported against at regular intervals.</td></tr>
<tr><td colspan="3">Entities with a high debt to revenue percentage or number are generally most at risk of not being able to pay the principal and interest on borrowings as and when they fall due. For entities with a shareholder guarantee, a high debt to revenue ratio can impact an entity's ability to pay other operational expenses.</td></tr>
</table>

Source: Queensland Audit Office

Appendix C—Controlled entities for which audit opinions will not be issued

We will not issue 2013–14 audit opinions for some controlled entities in the energy sector, for the reasons Figure C1 lists.

Figure C1
Energy sector controlled entities for which no opinion will be issued for 2013–14

Entity	Parent entity	Reason
Controlled entities		
Mica Creek Pty Ltd	Stanwell	Deed of cross guarantee ASIC order
SCL North West Pty Ltd	Stanwell	Deed of cross guarantee ASIC order
Energy Portfolio 1 Pty Ltd	Stanwell	Dormant
Glen Wilga Coal Pty Ltd	Stanwell	Dormant
Goondi Energy Pty Ltd	Stanwell	Non-reporting
Tarong Energy Corporation Pty Ltd	Stanwell	Dormant
Tarong Fuel Pty Ltd	Stanwell	Deed of cross guarantee ASIC order
Tarong North Pty Ltd	Stanwell	Non-reporting
TEC Coal Pty Ltd	Stanwell	Deed of cross guarantee ASIC order
TN Power Pty Ltd	Stanwell	Deed of cross guarantee ASIC order
Aberdare Collieries Pty Ltd	CS Energy	Deed of cross guarantee ASIC order
Callide Energy Pty Ltd	CS Energy	Deed of cross guarantee ASIC order
CS Energy Group Holdings Pty Ltd	CS Energy	Dormant
CS Energy Group Operations Holdings Pty Ltd	CS Energy	Dormant
CS Kogan (Australia) Pty Ltd	CS Energy	Deed of cross guarantee ASIC order
CS Energy Kogan Creek Pty Ltd	CS Energy	Deed of cross guarantee ASIC order
CS Energy Oxyfuel Pty Ltd	CS Energy	Deed of cross guarantee ASIC order

Entity	Parent entity	Reason
Kogan Creek Power Pty Ltd	CS Energy	Deed of cross guarantee ASIC order
Kogan Creek Power Station Pty Ltd	CS Energy	Deed of cross guarantee ASIC order
Manzillo Insurance (PCC) Ltd- Cell Enmach	CS Energy	Overseas based entity
Harold Street Holdings Pty Ltd	Powerlink	Deed of cross guarantee ASIC order
Powerlink Transmission Services Pty Ltd	Powerlink	Deed of cross guarantee ASIC order
Energy Impact Pty Ltd	Energex	Deed of cross guarantee ASIC order
Metering Dynamics Business Support Pty Ltd	Energex	Non-reporting
Queensland Energy Services Team Pty Ltd	Energex	Non-reporting
Varnsdorf Pty Ltd	Energex	Deed of cross guarantee ASIC order
VH Energy Holdings Pty Ltd	Energex	Deed of cross guarantee ASIC order
VH Finance Pty Ltd	Energex	Deed of cross guarantee ASIC order
VH Operations Pty Ltd	Energex	Deed of cross guarantee ASIC order
Roames Asset Services Pty Ltd*	Ergon	Non-reporting

* The shares in Roames Asset Services Pty Ltd sold to a private sector entity on 1 March 2014.

Source: Queensland Audit Office

We will not issue 2013–14 audit opinions for some controlled entities in the water sector, for the reasons Figure C2 lists.

Figure C2
Water sector controlled entities for which no opinion will be issued for 2013–14

Entity	Parent entity	Reason
Controlled entities		
North West Queensland Water Pipeline Pty Ltd	SunWater	Non-reporting
Eungella Water Pipeline Pty Ltd	SunWater	Non-reporting
Burnett Water Pty Ltd	SunWater	Non-reporting

Source: Queensland Audit Office

We will not issue 2013–14 audit opinions for some controlled entities in the ports sector, for the reasons Figure C3 lists.

Figure C3
Ports sector controlled entities for which no opinion will be issued for 2013–14

Entity	Parent entity	Reason
Controlled entities		
Ports Corporation of Queensland	NQBP	Dormant
Mackay Ports Limited	NQBP	Dormant
Gladstone Marine Pilot Service Pty Ltd	GPCL	Non-reporting
Gladstone WICET Operations Pty Ltd	GPCL	Non-reporting

Source: Queensland Audit Office

We will not issue a 2013–14 audit opinion for the On Track Insurance Pty Ltd for the reason within Figure C4.

Figure C4
Rail sector controlled entity for which no opinion will be issued for 2013–14

Entity	Parent entity	Reason
Controlled entities		
On Track Insurance Pty Ltd	Queensland Rail Limited	Non-reporting

Source: Queensland Audit Office

Other Public non-financial corporations for which we will not issue audit opinions for and their reasons are detailed in Figure C5.

Figure C5
Other Public non-financial corporations for which no opinion will be issued for 2013–14

Entity	Parent entity	Reason
Controlled entities		
Queensland Airport Holdings (Cairns) Pty Ltd	QTH Pty Ltd	Dormant
Queensland Airport Holdings (Mackay) Pty Ltd	QTH Pty Ltd	Dormant
Network Infrastructure Company Pty Ltd	QTH Pty Ltd	Dormant

Source: Queensland Audit Office

Appendix D—Regulatory information notices

Revision of AER guidelines

In 2013 the Australian Energy Regulator (AER) began a better regulation program to improve its approach to network regulation. This included issuing a series of guidelines to promote the efficient investment in and use of energy services for the long term interests of consumers. The revised guidelines targeted regulation incentives, efficient spending and rates of return necessary to support efficient investment.

From September 2014, the AER will publish annual benchmarking reports which provide regular information on the relative efficiency of network businesses during the regulatory period. The AER has highlighted in its 'Overview of the Better Regulation reform package' that reports will identify areas the AER is likely to target when assessing future expenditure proposals. Benchmarking means inefficient networks may face cuts to their proposed expenditure.

The AER's rate of return guideline intends greater transparency of the key components of the rate of return (equity and debt) and their assessment. The AER will estimate returns on equity and debt for a hypothetical, benchmark-efficient business, rather than the actual costs of any particular network business. The aim is for network businesses to have incentives to finance their business as efficiently as possible, and to support continuing investment in safe and reliable energy networks without requiring consumers to pay for excessive returns to network businesses.

Move to increased reporting

Each year, the AER issues regulatory information notices (RINs) to network service providers.

The AER requires network businesses to provide, prepare and maintain information in the manner and form specified in each notice. Certain aspects of the information are subject to either audit or review. The information is split into both financial and non-financial, with the QAO undertaking only the financial information component of the regulatory information notices (RIN) engagements in prior years.

This year, the AER issued two additional RINs, requesting businesses to submit economic benchmarking templates by 30 April 2014 and category analysis templates by 31 May 2014. As the AER required network businesses to provide data in a new format responding to these RINs, these first data sets covered an initial five-year catch up period, from 2008–09 to 2012–13.

In August 2014, the AER issued another new RIN: to provide information similar to the economic benchmarking and category analysis but focusing on forecast information for revenue reset purposes for the initial period of 2008–09 to 2013–14. The new RIN replaces the 2013–14 category analysis RIN; data sets were due 31 October 2014.

With networks now required to submit three data sets under three separate RIN notices each year, increasing the flow of financial and non-financial information to the AER. This information may be used to forecast future efficient expenditure needs and assess future revenue proposals of network businesses.

Energex and Ergon engaged us in 2013–14 to conduct work over RINs as Figure D1 details.

Figure D1
Regulatory engagements we conducted in 2013–14

Engagement	Financial years covered	Type of information	Date reports certified	Type of report issued
Annual performance RIN—Ergon	2012–13	Financial	11.12.13	Audit (actual information)
Annual performance RIN—Energex	2012–13	Financial	19.11.13	Audit (actual information)
Annual performance RIN—Ergon	2013–14	Financial	30.10.14	Audit (actual information)
Annual performance RIN—Energex	2013–14	Financial	30.10.14	Audit (actual information)
Economic benchmarking	2008–09 to 2012–13	Financial	29.04.14	Audit (actual information) Review (estimated information)
Economic benchmarking	2013–14	Financial	30.10.14	Audit (actual information) Review (estimated information)
Category analysis	2008–09 to 2012–13	Financial and non-financial	02.06.14	Audit (actual information) Review (estimated information)
Reset RIN—Ergon	Reset RIN 2008–09 to 2013–14	Financial and non-financial	29.10.14	Audit (actual information) Review (estimated information)
Reset RIN—Energex	Reset RIN 2008–09 to 2013–14	Financial and non-financial	30.10.14	Audit (actual information) Review (estimated information)

Note: We certified economic benchmarking and category analysis RINs on the same day for Ergon and Energex.

Source: Queensland Audit Office

Appendix E—Bulk water price path

Figure E1 summarises the price of bulk water in 2013–14 and the price that will be charged to ratepayers and customers of local government council owned water businesses and distributor-retailers till the end of 2014–15. Bulk water prices from 2015–16 are indicative only at this stage and will be reviewed in 2015.

Figure E1
Bulk water price path

Council	2013–14	2014–15	2015–16	2016–17	2017–18	Increase per mega litre by dollar
Brisbane City	$2 302	$2 547	$2 792	$3 037	$3 217	$915
City of Gold Coast	$2 470	$2 715	$2 960	$3 139	$3 217	$747
Ipswich City	$2 238	$2 483	$2 728	$2 973	$3 217	$979
Lockyer Valley Regional	$2 495	$2 740	$2 985	$3 139	$3 217	$722
Logan City	$2 628	$2 873	$3 062	$3 139	$3 217	$589
Moreton Bay Regional	$2 437	$2 682	$2 927	$3 139	$3 217	$780
Redland City	$1 717	$1 962	$2 207	$2 452	$3 217	$1 500
Scenic Rim Regional	$2 602	$2 847	$3 062	$3 139	$3 217	$615
Somerset Regional	$2 872	$2 988	$3 062	$3 139	$3 217	$345
Sunshine Coast Regional	$1 855	$2 100	$2 345	$2 590	$3 217	$1 362

Source: Department of Energy and Water Supply and Queensland Audit Office

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Auditor-General Reports to Parliament

Reports tabled in 2014–15

Number	Title	Date tabled in Legislative Assembly
1.	Results of audit: Internal control systems 2013–14	July 2014
2.	Hospital infrastructure projects	October 2014
3.	Emergency department performance reporting	October 2014
4.	Results of audit: State public sector entities for 2013–14	November 2014
5.	Results of audit: Hospital and Health Service entities 2013–14	November 2014
6.	Results of audit: Public non-financial corporations	November 2014

Source: Queensland Audit Office