7 PUBLIC NON-FINANCIAL CORPORATIONS SECTOR

FEATURES

- **In 2013-14, Public Non-financial Corporations will continue to drive greater efficiencies across all activities and cut unnecessary expenditure in order to minimise the cost of delivering their services while maintaining reliable performance.**
- **In 2013-14, the Queensland Bulk Water Supply Authority (Seqwater) will further consolidate improved efficiencies of its bulk water operations and cost reductions expected from the 2012-13 merger of the three former bulk water entities.**
- **Queensland Rail will continue to implement revised governance arrangements during 2013-14 that respond to the new corporate structure announced on 3 May 2013.**
- **During 2013-14, a number of Government-owned corporations will work with Government on the implementation of the Queensland Government's response to the Independent Commission of Audit Final Report.**

CONTEXT

The entities comprising the Public Non-financial Corporations (PNFC) sector operate across a range of industries including energy, rail, port and water delivery services. A significant part of the PNFC sector is the State's Government-owned corporations (GOCs) declared by regulation to be GOCs under the *Government Owned Corporations Act 1993*. This sector does not incorporate QIC Limited as it forms part of the Public Financial Corporations sector. The PNFC sector also includes non-GOC entities including Seqwater, Queensland Rail and some local water boards. A full list of PNFC sector entities is available in Chapter 8.

Under the *Government Owned Corporations Act 1993*, GOCs are required to operate to realise commercial success and efficiency and are accountable for their performance. GOC business activities target needs identified within their relevant market sector.

Revenues generated by the PNFC sector are predominantly from the sale of services or basic commodities. In more limited cases, part of a PNFC's revenue may comprise Community Service Obligation payments from the Government. These payments subsidise the provision of a service or commodity supplied on a non-commercial basis in order to deliver the Government's broader policy objectives.

REFORM

In 2013-14, the Queensland Government will continue to focus the PNFC sector on driving value for money for Queensland taxpayers, maintaining effective accountability frameworks and the reliable delivery of essential services. This aims to build on the progress and achievements made in 2012-13.

Capital investment

GOCs and other major PNFC sector entities will focus on strategies that result in stronger profitability and greater asset efficiency in order to generate improved returns on the State's substantial equity investment in these businesses. In addition, their future capital programs will continue to be assessed to ensure efficient investment that balances reliability with the lowest long-run cost. The Government is already seeing benefits of this strategy with capital expenditure reducing over the forward estimates.

Water

In 2012, the Government began reform of the South East Queensland water entities with the objective of improving the efficiency of water operations and reducing the costs of the South East Queensland Water Grid. A key element of that reform was the merger of the three South East Queensland water entities into one.

On 1 January 2013, the Queensland Bulk Water Transport Authority (LinkWater) and the SEQ Water Grid Manager (WGM) were merged into the existing operations of the Queensland Bulk Water Supply Authority (Seqwater). From this date, Seqwater has taken over all the assets and operations of the three former SEQ water entities (including itself). LinkWater and the WGM ceased trading on 1 January 2013.

The new Seqwater board immediately identified savings of $80 million per annum from the new structure and after a review of the capital and operational budgets, identified a further reduction of $291 million in expenditure over 2013-14 to 2016-17. Overall there is a forecast improvement in the operating position of $333 million by the end of 2016-17 compared to the pre-merger position.

Reviews and reports

During 2012-13 the Government released a number of reports that significantly impact the PNFC entities, including the Independent Commission of Audit. Further details on how the Independent Commission's Final Report impacts the PNFC sector can be found later in this Chapter.

The Inter-Departmental Committee on Energy Sector Reform (IDC) was tasked with ensuring:

1. electricity in Queensland is delivered in a cost-effective manner for customers
2. Queensland has a viable, sustainable and competitive electricity industry
3. electricity is delivered in a financially sustainable manner from the Queensland Government's perspective.

The IDC has undertaken a substantial review of the electricity sector, in consultation with industry, with a view to developing a strategy for reform. Cabinet is yet to consider the IDC final report.

In 2013-14, Government will progress its review of ports' governance. This review will consider the most appropriate governance model for Queensland ports to ensure efficient and effective delivery of port services. The review will focus on determining an optimal governance model for Queensland ports, addressing improved productivity, minimisation of operational costs, maintaining service levels at the lowest cost and efficient and effective port services.

INDEPENDENT COMMISSION OF AUDIT

The Independent Commission of Audit's Final Report made a series of recommendations relevant to the PNFC sector.

It recommended, when market conditions are favourable, the Government divest its electricity generation assets. The Independent Commission identified a number of factors that would impact the optimal timing of divestment, including the uncertainty regarding the carbon tax and generation capacity in the National Electricity Market.

The Government does not currently have a policy to sell Government businesses, and remains fully committed to seeking a mandate from the Queensland people before divesting itself of any Government business. However, the Government believes such a proposal is worthy of an open and transparent community debate to establish its viability and to inform stakeholders of the costs and benefits of Government owning such businesses, noting these also come with significant financial risks in the context of a modern economy.

Regardless of any consideration of the merits of selling the assets, the Government's expectation of these operations is they are open for business as usual and the Government will adopt a prudent approach in ensuring decisions are not taken that could erode the value of these assets.

The Independent Commission also recommended the electricity distribution and transmission assets be divested. The Government has decided not to seek a mandate to do so at the next election. However, the Government believes that the Independent Commission's recommendation that residual retail electricity functions be divested warrants further consideration and debate with the community.

The Independent Commission also recommended that the electricity distribution and transmission businesses be required to achieve higher rates of return through increased efficiencies, better capital management and operational cost savings. It also recommends they divest themselves of non-core business where there are significant bring forward benefits for the State from doing so. The 2013-14 Budget reflects the adoption of these recommendations while at the same time ensuring impacts on prices, reliability and standards are minimised.

The Independent Commission made a number of recommendations directly relating to Queensland Rail and the port assets held by GOCs. Of these recommendations, the Government has accepted those relating to increased contestability and competition for services. The Government has also accepted in principle, in part, or for further consideration, a number of other recommendations, acknowledging that these matters will be reviewed as part of the ongoing reform activities being undertaken by the Department of Transport and Main Roads.

Specifically, the Independent Commission recommended that the commercial operations of the Gladstone Ports Corporation Limited (GPC) and Port of Townsville Limited (PoTL) be offered for long term lease to private operators. While the Government does not currently have a policy to sell Government businesses, it believes this proposal is worthy of an open and transparent community debate to establish its viability and to inform stakeholders of the costs and benefits involved. It should also be noted that the offering of a long-term lease for the operation of the commercial enterprises means the Government would still retain ownership of these ports. The Government commits to undertake further detailed investigation of this particular proposal to ensure that the debate is fully informed before making any decision.

The Government has accepted in principle the Independent Commission's recommendation that ownership and control of remaining government owned, low volume regional ports be offered to local authorities, in view of the significant role they play in their local communities. The Government notes that local authorities are an important stakeholder in ports and will consider each proposal on a case by case basis.

The Independent Commission's report recommended a number of initiatives regarding regional bulk water supply, including the transfer of SunWater Limited's (SunWater) irrigation channels to private irrigators and offering dedicated water supply infrastructure servicing commercial and industrial clients for private ownership and/or private operation, depending on which solution provides the best value for money outcome for the Government. The Independent Commission also recommended that while SunWater should retain ownership of regional bulk water assets, any new bulk water assets should be privately funded and owned (subject to compelling public benefit or market failure factors).

The Government has accepted the recommendations relating to SunWater, and has initiated an investigation into the divestment and transfer of the irrigation channels to irrigators under local management plans. The Government has also undertaken to evaluate proposals to divest dedicated water infrastructure servicing industrial and commercial clients.

The Government's response to the Independent Commission report recognised the benefits that flow from a number of recommendations and committed to further work on how to effectively and efficiently capture these benefits. In 2013-14, GOCs affected by these recommendations will work with the Government to ensure the businesses are positioned to meet the expectations of Government in this regard.

FINANCES AND PERFORMANCE

Earnings Before Interest and Tax

As outlined in Table 7.1, total forecast Public Non-financial Corporations sector earnings before interest and tax in 2013-14 are $3.7 billion.

Table 7.1
Earnings Before Interest and Tax[1]

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Energy Sector	2,249	2,625	2,733
Transport Sector	350	512	627
Other	89	522	350
Total PNFC sector Earnings Before Interest and Tax	**2,689**	**3,658**	**3,710**

Note:
1. Numbers may not add due to rounding.

Energy Sector

Generation

The Queensland region of the National Electricity Market (NEM) is currently characterised by oversupply of generation and lower than anticipated growth resulting in depressed contract and pool prices. Roof top solar generation capacity, currently estimated to be in excess of 500 megawatts (MW), also reduces demand for on-grid energy and suppresses price peaks on hot, sunny days.

The outlook for merchant generation in the Queensland region is uncertain. While recent demand growth in the Queensland region has been lower than forecast, it is the only region of the NEM forecast to experience some level of demand growth in the next decade. As this demand growth occurs, Queensland's spare generation capacity is expected to be absorbed, resulting in an increase in pool prices.

According to the Australian Energy Market Operator (AEMO) 2012 Electricity Statement of Opportunities Update (published in early 2013) and based on its medium growth scenario, no new base load generation capacity will be required in Queensland until 2020-21. Additional peaking capacity (open cycle gas turbine) of between 400MW and 500MW is expected to be required by 2015-16.

In late 2012, Stanwell Corporation Limited reduced availability at the Tarong Power Station from 1,400 MW to 700 MW. This reduced availability will be in place until after the summer of 2014-15. Stanwell's decision was in response to an over-supply in the energy market. The cold storage of the two units does not affect the security of electricity supply in Queensland.

The liquefied natural gas (LNG) industry will be important to any change to market fundamentals in the Queensland region. The LNG industry is expected to create additional base load demand and also move the domestic gas price towards international parity. In these circumstances the competitiveness of coal-fired generation, being the main type of generation within the Queensland government-owned generators, is expected to improve.

Networks

The financial positions of the network energy GOCs (Powerlink, Energex and Ergon) continue to reflect the significant amounts of deferred and/or delayed capital investment which have arisen as a result of estimates of ongoing low demand.

All three network entities are undertaking significant cost containment activities which are reflected in the 2013-14 Budget.

The only significant market based change is the completion of Powerlink's divestment of its equity interest in ElectraNet Pty Ltd, which primarily impacted returns in 2012-13. Although there have been limited changes in the market environment for network energy GOCs, significant risks remain which could impact the forecast outcomes of these entities, including:

- changes to the timing and profile of expected large load projects (such as LNG and other mining and infrastructure projects) which will influence energy growth
- significant changes to forecast electricity demand and volume growth profiles.

However, the most significant risk remains the commencement of the new regulatory period for Energex and Ergon which begins on 1 July 2015. The current regulatory environment presents some uncertainty due to expected significant rule changes and public focus on the decisions of the Australian Energy Regulator making it difficult to estimate the expected financial performance and position of Energex and Ergon post 2015-16.

Transport Sector

Queensland Rail

Queensland Rail (QR) is a provider of rail transport services which are predominantly supported by the Queensland Government through the provision of Community Service Obligation payments. QR maintains a focus on efficient and effective delivery of its services in order to improve its performance and reduce the overall cost of transport services.

The establishment of the QR efficiency program was a key initiative of the 2012-13 Budget. The efficiency program initially estimated a $42 million per annum reduction in consumable spending in addition to a management restructure and Voluntary Redundancy scheme. Total savings of approximately $60 million per annum are expected from these three initiatives. QR has successfully met the forecast cost reduction and continues to progress the efficiency program with further cost savings and efficiency measures identified for implementation in 2013-14.

In 2013-14, the Government will continue to improve the governance arrangements associated with the delivery of rail public transport services following from the recent institutional restructure in which a new statutory authority was created. This restructure is designed to provide an organisational platform for future reforms in rail service delivery. In addition, the contractual arrangements between the Department of Transport and Main Roads as purchaser, and QR as the service provider, are in the process of being renegotiated to ensure the best value outcome for rail commuters in Queensland.

Ports

Queensland's ports service a number of communities and regions and a multi-faceted industry base throughout the State. Other than the Port of Brisbane, all Queensland ports are owned by the Queensland Government with a mixture of both private and public ownership of terminals and berths.

Thermal and metallurgical coals are Queensland's largest export, and drive profitability at a number of Queensland ports. Nominal port capacity of up to 399 mt is expected by 2017-18 with completion of current and planned port expansion works, including the Wiggins Island Coal Export Terminal Stages 1 and 2 at the Port of Gladstone, Abbot Point Coal Terminal T0 and T3 expansions at the Port of Abbot Point and Hay Point Coal Terminal's Stage 3 expansion at the Port of Hay Point.

Water Infrastructure

SunWater

SunWater, in conjunction with the Department of Energy and Water Supply and irrigators, is investigating the viability of local management arrangements of channel irrigation schemes. A final decision is expected to occur in 2013-14.

Seqwater

On 1 January 2013, the two South East Queensland water statutory bodies of Queensland Bulk Water Transport Authority (LinkWater) and SEQ Water Grid Manager, were merged into the Queensland Bulk Water Supply Authority (Seqwater) to form one statutory body.

Seqwater has recently undertaken a major review and has improved its operating position by $333 million over its forward estimates compared to the pre-restructure position. This is largely a function of cost savings and from lower interest expenses arising from reduced borrowings. Seqwater's projected borrowings for 2013-14 reduce by $349 million compared to the pre-restructure position. This reduction is a result of reduced losses and the deferral of some capital works.

Borrowings

PNFC sector entities utilise debt financing as a source of funds for capital investments and to maintain an optimum capital structure.

PNFC sector entities are required to take a prudent and sound approach to the management of debt, including the establishment of borrowing arrangements which are appropriate to their business risk. These arrangements take into account the appropriateness of the proposed capital expenditure program and the implication of the borrowings for key financial and performance indicators.

As outlined in Table 7.2, total forecast Public Non-financial Corporation sector borrowings for 2013-14 are $30.9 billion. Over the period 2012-13 to 2015-16, net borrowings are $1.2 billion lower than forecast in the 2012-13 MYFER.

Table 7.2
Borrowings[1]

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Energy Sector	16,174	16,900	17,599
Transport Sector	3,585	3,566	3,515
Other	12,248	10,161	9,814
Total PNFC sector non-current borrowings	**32,007**	**30,626**	**30,928**

Note:
1. Numbers may not add due to rounding.

Returns to Government

PNFC sector entities provide returns to Government by way of dividends and current tax equivalent payments.

Dividends

A GOC's dividend policy is agreed with shareholding Ministers as part of the Statement of Corporate Intent. A Statement of Corporate Intent represents a performance contract between the shareholding Ministers and a GOC board, with the board being accountable to shareholding Ministers for meeting financial and non-financial performance targets. When establishing the dividend policy for the period, GOC boards are expected to ensure that the dividend policy takes into account the return shareholders expect on their investments and the levels of equity required to maintain an appropriate capital structure.

A GOC's dividend payment is determined in accordance with the agreed dividend policy and approved by shareholding Ministers on the recommendation of the GOC's board.

The dividend is paid out of profits, after the entity has met its commitments to operating and maintenance expenses.

At the time of the 2012-13 Budget, the forecast for ordinary dividends in 2012-13 was $971 million. It is now estimated dividends declared in 2012-13 will be $1 billion. As outlined in Table 7.3, total dividends in 2013-14 are estimated at $1.2 billion.

Table 7.3
Ordinary Dividends[1,2,3]

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Energy Sector	692	779	893
Transport Sector	163	232	280
Other	3	23	35
Total PNFC sector dividends	**859**	**1,034**	**1,208**

Notes:
1. Numbers may not add due to rounding.
2. Represents dividends declared in the period.
3. Will not match dividend numbers quoted in Chapter 3, as this table includes only dividends paid by PNFC sector entities.

Tax equivalent payments

Tax equivalent payments (TEPs) are paid by PNFC sector entities to recognise the benefits derived because they are not liable to pay Commonwealth tax. The primary objective of the payment is to promote competitive neutrality, through a uniform application of income tax laws, between the Government-owned entities and their privately held counterparts.

As outlined in Table 7.4, total current TEPs for 2013-14 are forecast to be $453 million. The substantial increase in TEPs between 2012-13 and 2013-14 is largely due to a change in the allowable tax treatment for capitalised labour affecting the electricity network sector, timing differences for tax accounting purposes when revenue recoveries are affected by electricity demand being below forecast and the lag in receipt of solar feed-in tariff revenue.

Table 7.4
Current Tax Equivalent Payments[1,2]

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Energy Sector	94	151	295
Transport Sector	87	131	149
Other	30	5	9
Total PNFC sector current TEPs	**211**	**287**	**453**

Notes:
1. Numbers may not add due to rounding.
2. Will not match tax equivalent payments revenues quoted in Chapter 3, as this table includes only tax equivalent payments from PNFC sector entities.

Community Service Obligation Payments

Community service obligations (CSOs) arise in situations where a commercial entity is required by Government to perform activities that on their own are not in the entity's commercial interests. In these situations Government will often provide CSO payments to compensate the entity for the cost of delivering the service.

As outlined in Table 7.5, in 2013-14 the Government is expecting to provide CSO payments to PNFC sector entities of $2.0 billion.

Table 7.5
Community Service Obligation Payments[1,2]

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Energy Sector	415	650	615
Transport Sector	1,356	1,411	1,416
Other	15	17	16
Total PNFC sector CSOs	**1,786**	**2,078**	**2,047**

Notes:
1. Numbers may not add due to rounding.
2. The numbers in this table will not match those in Table 4.3 due to ongoing contract negotiations.

In line with the Queensland Government's uniform electricity tariff policy, a CSO payment is provided to Ergon to compensate its retail subsidiary for the difference between the cost of retail supply to regional customers and the revenue received from uniform retail electricity tariff prices (regulated by the State). This subsidy is a key part of the uniform electricity tariff policy and is provided to ensure all Queenslanders, regardless of their geographic location, pay a reasonable price for their electricity.

The Government compensates SunWater for the shortfall in revenues generated by complying with the irrigation price path in SunWater managed irrigation schemes. The shortfall represents the difference between the efficient cost of supply of water to irrigators (lower bound cost) as determined by the Queensland Competition Authority, and the prices charged to irrigators as directed by the Government. Similarly, Seqwater receives a CSO from the Government for the provision of rural irrigation water to rural irrigators.

The Government compensates QR for the provision of non-commercial rail passenger and infrastructure services for the commuter and tourism markets.

These concessions are all detailed further in the Concessions Statement.

Taking into account the dividends and tax equivalent payments paid to the General Government sector, less the CSO payments to PNFC sector entities, the Government makes a substantial contribution to the PNFC sector on an annual basis, as indicated by the negative flows in Table 7.6. Competitive neutrality fees are also paid by some PNFC entities. These are paid prior to making dividend payments to Government. For more details, refer to Chapter 3.

Table 7.6
Net Flows to the General Government sector from PNFC Sector Entities

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Net Flows	(716)	(756)	(386)

Equity contributions

The levels and weightings of GOC debt and equity are managed by the Government to maintain an optimal and efficient capital structure. Corporations may have different target capital structures for different business entities or to support expected capital programs and projects.

As outlined in Table 7.7, estimated equity contributions to PNFC sector entities in 2012-13 and 2013-14 are $4 million and $77 million, respectively. The equity contribution in 2013-14 of $77 million is for Queensland Rail to support the New Generation Rolling Stock acquisition program.

Table 7.7
Equity Contributions[1]

	2011-12 Actual $ million	2012-13 Est. Act. $ million	2013-14 Budget $ million
Energy Sector	300	..	..
Transport Sector	255	4	77
Other	1	..	..
Total Equity Contributions	**556**	**4**	**77**

Note:
1. Numbers may not add due to rounding.