

FINANCIAL STATEMENTS

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DIRECTORS' REPORT

DIRECTORS

The directors of Melbourne Water Corporation in office at the date of this Report are:

C J Stewart (Chairman)
 B R Bayley (Managing Director)
 A A Browne
 RV Gilbert
 J M King
 B Solnordal

Particulars of the directors' qualifications, experience and special responsibilities are set out on page 37 of this Annual Report.

DIRECTORS' MEETINGS

During the financial period the Corporation held 12 meetings of directors. Attendance at meetings of the Board and its committees were:

	PRINCIPAL BOARD		AUDIT COMMITTEE		REMUNERATION COMMITTEE	
	<i>Attended</i>	<i>Maximum Possible</i>	<i>Attended</i>	<i>Maximum Possible</i>	<i>Attended</i>	<i>Maximum Possible</i>
C J STEWART	11	12	–	–	3	3
J E MORGAN *	7	7	2	2	3	3
A A BROWNE	11	12	4	4	–	–
RV GILBERT	11	12	–	–	–	–
J M KING	10	12	4	4	2	3
B SOLNORDAL	11	12	4	4	–	–

Note : B R Bayley was appointed as Managing Director on 28 July 1998.

* J E Morgan retired with effect 31 January 1998.

PRINCIPAL ACTIVITIES

The principal activities of the Corporation during the course of the financial year were to provide water and sewerage services on a wholesale basis to three retail companies: Yarra Valley Water Ltd, South East Water Ltd and City West Water Ltd. The Corporation also manages the main drainage network and waterways, providing flood protection and water quality improvement services for the greater Melbourne area.

OPERATING RESULTS AND DIVIDEND

The net profit for the Corporation after providing for income tax amounted to \$160.6 million.

Following negotiations with the Department of Treasury and Finance, a dividend of \$141.1 million has been proposed for the period. Of this amount \$76.2 million was paid as an interim dividend during 1997/98.

REVIEW OF OPERATIONS

The directors' review of the operations of the Corporation during the financial period ended 30 June 1998 and the results of those operations are set out in the Chairman's Report and the Managing Director's Overview on pages 6–9 of this Annual Report.

STATE OF AFFAIRS

On 1 January 1998, major reforms to water and sewerage in Melbourne were introduced by the State government. As part of the reform package wholesale water and sewerage prices have been reduced. It is estimated that revenue to Melbourne Water will be reduced by \$220 million on an annual basis by the reforms.

In addition to the pricing reforms, the Treasurer of Victoria approved the transfer of \$337 million (book value) of debt to the State. The debt transfer has been treated as a reduction in debt with an increase in equity (contributed capital) equal to the book value of the debt as at date of transfer. There has been a restructure of Melbourne Water's debt portfolio following the transfer. Refer to Notes 1.8 and 1.6.

There were no other significant changes in the state of affairs of the Corporation during the financial period ended 30 June 1998 not otherwise disclosed in this Report or the Financial Statements.

EVENTS SUBSEQUENT TO BALANCE DATE

Since the end of the financial year the directors are not aware of any matter or circumstance not otherwise dealt with in the Report or Financial Statements that, in the opinion of the directors has significantly affected or may significantly affect the operations of the Corporation, the results of those operations, or the state of affairs of the Corporation in subsequent future years.

STATUTORY INFORMATION – REPORT OF OPERATIONS

The following statutory information is provided elsewhere within the Annual Report:

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Particulars, functions and powers	40
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DIRECTORS' BENEFITS

No director has received or become entitled to receive a benefit (other than a benefit included in Notes 18 and 24 to the Financial Statements) because of a contract that the director, a firm of which the director is a member, or an entity in which the director has a substantial financial interest, has made (during the period ended 30 June 1998 or at any other time) with:

- (a) the Corporation; or
- (b) an entity that the Corporation controlled, or a body corporate that was related to the Corporation, when the contract was made or when the director received, or became entitled to receive, the benefit.

PROFIT AND LOSS STATEMENT

For year ended 30 June 1998

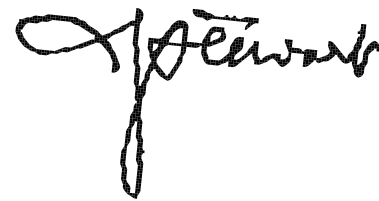
DIRECTORS' AND OFFICERS' LIABILITY INSURANCE

During the financial year the Corporation paid insurance premiums in respect of directors' and officers' liability insurance. The policies do not specify the premium for individual directors and officers.

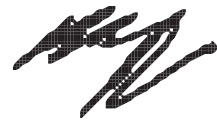
The directors' and officers' liability insurance provides cover against all costs and expenses involved in defending legal actions and any resulting payments arising from a liability to persons (other than the Corporation) incurred in their position as director or officer unless the conduct involves a wilful breach of duty or an improper use of information or position to gain advantage.

INTEREST IN CONTRACTS

No contracts involving directors' interests were entered into since the end of the previous financial year or existed at the end of the financial year other than the transactions detailed in Note 24 to the Financial Statements.



C J Stewart
(Chairman)



B R Bayley
(Managing Director)

	Note	1998 \$000	1997 \$000
Operating revenue	2	567,011	679,766
Operating profit before abnormal items and income tax	3.1	242,494	267,840
Abnormal items before income tax	3.2	–	4,443
Operating profit before income tax		242,494	263,397
Income tax attributable to operating profit	4	81,875	96,977
Operating profit after income tax		160,619	166,420
Retained profits at the beginning of the financial year		434,269	409,164
Total available for appropriation		594,888	575,584
Dividend provided for or paid	5	141,149	141,315
Retained profits at the end of the financial year		453,739	434,269

The accompanying notes form part of the Financial Statements.

BALANCE SHEET

At 30 June 1998

	Note	1998 \$000	1997 \$000
CURRENT ASSETS			
Cash	6	409	616
Receivables	7	21,794	26,075
Investments	8	5,003	10,003
Stores and livestock	9	9,536	9,009
Other	10	638	396
Total current assets		37,380	46,099
NON CURRENT ASSETS			
Property, plant and equipment	11	2,672,615	2,644,545
Other	12	11,369	23,607
Total non current assets		2,683,984	2,668,152
TOTAL ASSETS		2,721,364	2,714,251
CURRENT LIABILITIES			
Creditors	13	71,793	99,993
Borrowings	27.1	156,800	242,975
Provisions	14	89,278	111,626
Total current liabilities		317,871	454,594
NON CURRENT LIABILITIES			
Creditors		1,529	340
Borrowings	27.1	1,125,000	1,393,240
Provisions	15	219,189	171,354
Total non current liabilities		1,345,718	1,564,934
TOTAL LIABILITIES		1,663,589	2,019,528
NET ASSETS		1,057,775	694,723
EQUITY			
Contributed capital	16	604,036	260,454
Retained profits		453,739	434,269
TOTAL EQUITY		1,057,775	694,723

The accompanying notes form part of the Financial Statements.

STATEMENT OF CASH FLOWS

For year ended 30 June 1998

	Note	1998 \$000	1997 \$000
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers		550,796	658,453
Payments to suppliers and employees		(160,517)	(181,720)
Income Tax Equivalent Paid		(44,838)	-
Interest received		118	88
Interest and other costs of finance paid		(95,151)	(192,803)
Net cash provided by operating activities	23	250,408	284,018
CASH FLOWS FROM INVESTING ACTIVITIES			
Payment for property, plant, equipment and works in progress		(77,255)	(84,999)
Proceeds from sale of property, plant and equipment		18,629	23,590
Net cash used in investing activities		(58,626)	(61,409)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from borrowings		627,250	1,333,782
Repayment of borrowings		(686,424)	(1,421,143)
Dividend paid		(137,815)	(139,700)
Net cash used in financing activities		(196,989)	(227,061)
Net (decrease) in cash held		(5,207)	(4,452)
Cash at the beginning of the financial year		10,619	15,071
Cash at end of the financial year		5,412	10,619
Reconciliation of cash			
For the purposes of the statements of cash flows, cash represents cash on hand, at the bank and on short term deposit.			
Cash at bank and on hand	6	409	616
Deposits	8	5,003	10,003
		5,412	10,619

The accompanying notes form part of the Financial Statements.

NOTES TO THE ACCOUNTS

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1.1 General

These general purpose financial statements are prepared in accordance with the *Financial Management Act 1994*, Australian Accounting Standards, Urgent Issues Group Consensus Views and relevant statutory and other requirements. Where appropriate, the disclosure requirements of Corporations Law have also been followed, although there is no legal requirement to do so.

The financial statements have been prepared on the basis of historical cost and do not take into account changing money values or current valuations of non-current assets, except where stated.

Unless otherwise stated, amounts in the financial statements have been rounded to the nearest thousand dollars.

1.2 Income Tax

Under Section 88(1) of the *State Owned Enterprises Act 1992*, Melbourne Water became subject to the Victorian Income Tax Equivalent System from 1 July 1993. The tax equivalent rules are based on the *Income Tax Assessment Act 1936* (as amended). The essential difference between the State Equivalent Rules and the Commonwealth legislation is that the tax liability is to be paid to the State Government and not the Commonwealth Government.

Melbourne Water has adopted the liability method of Tax Effect Accounting in accordance with the requirements of Australian Accounting Standard AAS3 'Accounting for Income Tax (Tax Effect Accounting)'.

1.3 Valuation of Non Current Assets

Water Supply, Sewerage, Drainage and Other Fixed Assets are recorded at historical cost. Those assets acquired from external sources are valued either at values shown in the balance sheet of the acquired entity or at an estimated cost.

Crown land is valued using the 'market value adjacent site' method. The initial valuation was supplied by the Office of the Valuer General and subsequently indexed (refer to Note 11). Transfers and revaluations of Crown land are adjusted against contributed capital in accordance with formal approval by the Minister of Finance.

1.4 Recoverable Amount of Non Current Assets

To ensure compliance with the provisions of Australian Accounting Standard AAS10 'Accounting for the Revaluation of Non Current Assets' Melbourne Water undertook an internal business valuation in June 1998. Expected net cash flows at major asset grouping level were discounted to their present value to calculate the recoverable amount as prescribed in AAS10.

As the recoverable amount for each major asset group was in excess of the written down carrying value, a write down of 'in service' assets was not required.

1.5 Depreciation

Non Current Assets are depreciated on a straight line basis over the estimated useful lives of the assets. Depreciation commences in the month subsequent to the date where service can be obtained.

The estimated useful lives are as follows:

IT Equipment	3–5 years
Leasehold Improvements	5–20 years
Buildings	30–50 years
Other Plant & Equipment	50 years
Infrastructure Assets	50–100 years

NOTES TO THE ACCOUNTS

1.6 Receivables and Revenue Recognition

Trade Debtors

Drainage rate debtors – revenue is recognised on a monthly basis, derived from the total expected rates to be collected for the year. Rates are levied quarterly based on property valuations as at 30 June 1990. Settlement varies between 21 and 35 days (depending upon the billing cycle of the retail company). To secure the debtor, a lien is held over the property.

Water usage charges and sewage disposal charges - the charges comprise a variable metered component and a fixed fee. The metered usage revenue is recognised when the service has been used with settlement at 7 days. The fixed fee is recognised on a monthly basis with settlement at 14 days. Collateral is not obtained for this class of debtor.

Other Receivables

Interest received / receivable – income receivable is accrued in accordance with the terms and conditions of the underlying financial instrument or other contract.

Proceeds from sale of non current assets – property sales are recognised on signing of an unconditional contract of sale. Debtors are provided with commercial terms. However, in some cases this may extend to a maximum maturity of 120 days.

Other receivables are recognised at their carrying amount. Collateral is not normally obtained for other receivables.

Bad and Doubtful Debts

A provision for doubtful debts is based on a review of all amounts outstanding at balance date. Bad debts are written off in the period in which they are identified.

1.7 Creditors

Trade creditors and accruals - represent liabilities for goods / services and accrued interest on borrowings which are unpaid at 30 June 1998. The accrued interest on borrowings are unsecured and the Trade Creditors are usually paid within 30 days net of invoice.

Advances – represent security deposits and other advances paid by developers / land owners for the construction of drainage works. The amounts are unsecured and refunded to the developers at the completion of the project.

1.8 Borrowings

Borrowings are carried at their capital (book) values which represent the intrinsic present value of future cash flows discounted at the original issue yield. Any difference between the face value and capital value on issuance is recognised as a discount or premium and amortised over the term of the loan, using the effective yield method.

The capital value of CPI indexed bonds is adjusted to reflect changes in the appropriate CPI index. Any variation is charged to the Profit and Loss Statement.

All borrowings are required to be transacted through the Treasury Corporation of Victoria whose liabilities are guaranteed by the Government of Victoria.

On 1 January 1998, the Treasurer of Victoria approved the transfer of \$337 million (book value) of Melbourne Water debt to the State. The direction was made under section 9(1)(c) of the *State Owned Enterprises Act 1992*. The debt transfer has been treated as a reduction in debt with an increase in equity (contributed capital) equal to the book value of the debt as at date of transfer.

Since the debt restructure, all borrowings are now carried at their principal amount. Interest is accrued based on the applicable interest rate for each loan.

NOTES TO THE ACCOUNTS

1.9 Derivative Financial Instruments

Derivative financial instruments are utilised to manage financial risk and not for speculative or trading purposes. Transactions are undertaken to hedge interest rate risks associated with an underlying physical position, either to provide a desired debt profile and composition or to decrease specific exposure to interest rate risk. As such, the impact of derivative financial instruments on the profit and loss statement and market values quoted in Note 27.2 should not be viewed in isolation.

All derivative instruments are transacted through the Treasury Corporation of Victoria which has developed a suite of derivative products that have the characteristics of interest rate swaps, futures, forwards and options.

Derivatives are accounted for on a basis consistent with the underlying positions being hedged, with any gains and losses recorded on a deferral and amortisation basis. Derivative transactions are not recognised in the financial statements on inception.

As at 30 June 1998, Melbourne Water had no derivative positions and there were no additional positions in place to hedge future transactions.

Refer to Note 27 for additional details on financial instruments.

1.10 Employee Entitlements

Wages, Salaries and Annual Leave

Liabilities for wages, salaries and annual leave are recognised and measured as the amount unpaid at the reporting date at current pay rates in respect of employees' services up to that date. The liability for Annual Leave has been oncosted in accordance with the Australian Accounting Standard AAS30 'Accounting for Employee Entitlements'.

Sick Leave

Sick leave payments are made in accordance with relevant awards, determinations and Corporation policy. No provision is made in the financial statements for outstanding sick leave entitlements as these are not vested benefits.

Long Service Leave

A liability for long service leave is recognised and measured as the present value of expected future payments to be made in respect of services provided by employees up to reporting date. As prescribed by AAS30, expected future payments are discounted using interest rates attaching, as at reporting date, to Australian Government guaranteed securities with terms to maturity that match, as closely as possible, the estimated future cash outflows.

The current and non-current components of the liability are calculated based on the assumption that 10% of the total liability is taken within 12 months.

Superannuation

A liability in respect of defined benefit superannuation is recognised and measured as the difference between employees' vested benefits at the reporting date and the net market value of the superannuation funds' assets at that date, after allowing for the impact of the 15% tax on contributions.

Refer to Note 22 for further details on superannuation liability.

WorkCover

Melbourne Water is registered as a self-insurer for workers compensation and is liable to the workers or workers' dependants to pay compensation under the *Accident Compensation Act 1985*.

Based upon actuarial assessment, a provision of \$4.2 million (\$4.9 million in 1996/97) is made for outstanding claims incurred and not settled and for claims incurred but not reported. Other claims incurred and settled during the period are charged to the Profit and Loss Statement.

NOTES TO THE ACCOUNTS

Workers Compensation

Melbourne Water continues to be liable for workers compensation claims incurred prior to the introduction of WorkCare (now WorkCover). Based upon actuarial assessment, a provision of \$0.8 million is made for all outstanding workers compensation claims at 30 June 1998.

1.11 Stores and Livestock

Stores consist mainly of materials and supplies for asset construction, systems operation and general administration and are valued at cost.

Livestock includes cattle, sheep and horses held in connection with the operation of Werribee Agriculture. Livestock is stated at market price.

1.12 Year 2000 Expenditure

Costs relating to preparation for year 2000 readiness are charged as expenses when incurred. Refer Note 3.1.

2 OPERATING REVENUE

	1998	1997
	\$000	\$000
Sales Revenue		
Bulk water and sewerage charges	422,388	531,164
Drainage rates	91,707	89,952
	<hr/> 514,095	<hr/> 621,116
Other Revenue		
Interest received / receivable	117	80
Developer charges and contributions	17,045	15,592
Proceeds from sale of non-current assets	16,378	16,542
Miscellaneous	19,376	26,436
	<hr/> 52,916	<hr/> 58,650
Total operating revenue	<hr/> 567,011	<hr/> 679,766

NOTES TO THE ACCOUNTS

3 OPERATING PROFIT

	1998 \$000	1997 \$000
3.1 Operating profit before abnormal items and income tax is arrived at after crediting and charging the following specific items:		
Credits		
Interest received / receivable	117	80
Profit on sale of – non current assets	10,436	9,846
Charges		
Total interest paid / payable	118,717	199,085
Bad debts		
– trade	–	442
– other receivables	54	9
Loss on sale of non current assets	1,048	3,805
Rental expenses relating to operating leases	1,408	1,682
Depreciation		
– buildings	858	748
– plant and equipment	54,407	52,137
Transfers to / from doubtful debts provision		
– trade debtors	–	20
– other receivables	(188)	31
Labour and associated charges	39,644	44,386
Contract services	36,173	41,690
Year 2000 Expenditure	768	–
3.2 Operating profit after income tax is also arrived at after crediting and charging the following abnormal items.		
Credits		
Gross proceeds from sale of Streamline Australia	–	8,237
Charges		
Book value of Streamline Australia net assets sold	–	3,505
Change in accounting treatment for depreciation method	–	14,336
Change in accounting treatment for asset lives	–	(5,161)
Total abnormal items before income tax		4,443
Applicable income tax on abnormal items	–	1,599
Total abnormal items after income tax	–	2,844

NOTES TO THE ACCOUNTS

4 INCOME TAX

	1998 \$000	1997 \$000
The aggregate amount of income tax expense attributable to the financial year is reconciled to the prima facie tax payable on the operating profit as follows:		
Operating profit before income tax	242,494	263,397
Prima facie income tax calculated at 36%	87,298	94,823
Adjustment for the tax effect of permanent differences:		
Non deductible expenses	976	654
Net exempt income	(6,118)	(5,588)
Research and development concession	(286)	(204)
Other sundry items	–	1,308
Income tax adjusted for permanent differences	81,870	90,993
Adjustment for under provision in previous year	5	5,984
Income tax attributable to operating profit	81,875	96,977
5 DIVIDENDS		
Interim dividend paid during the year	76,200	79,700
Proposed final dividend paid / payable	64,949	61,615
Total dividend proposed for the period	141,149	141,315
6 CURRENT ASSETS – CASH		
Cash at bank and on hand	409	616
7 CURRENT ASSETS – RECEIVABLES		
Trade debtors	11,649	9,613
Other receivables	11,649	9,613
Less: Provision for doubtful debts	10,218	16,746
	73	284
	10,145	16,462
Total current assets – receivables	21,794	26,075

NOTES TO THE ACCOUNTS

8 CURRENT ASSETS - INVESTMENTS

	1998	1997
	\$000	\$000
Deposits	5,003	10,003
Total current assets - investments	5,003	10,003

9 CURRENT ASSETS - STORES AND LIVESTOCK

Stock in stores - valued at cost	1,745	1,961
Livestock - stated at market value	7,791	7,048
Total current assets - stores and livestock	9,536	9,009

10 CURRENT ASSETS - OTHER

Prepayments	421	250
Deferred expenses	217	146
Total current assets - other	638	396

NOTES TO THE ACCOUNTS

11 NON CURRENT ASSETS - PROPERTY, PLANT AND EQUIPMENT

	1998	1997
	\$000	\$000
Land and Buildings		
Crown land at valuation*	16,679	10,454
Freehold land and buildings at cost	28,741	19,597
Less: Accumulated depreciation - buildings	15,398	7,047
Total land and buildings	30,022	23,004
Plant and Equipment		
Plant and equipment at cost	3,169,358	2,974,711
Less: Accumulated depreciation	672,063	629,902
Total plant and equipment	2,497,295	2,344,809
Capital Works in Progress	145,298	276,732
Total non current assets - property, plant and equipment	2,672,615	2,644,545

* Crown Land

The Corporation controls 19,774 hectares of Crown land. The valuation was obtained from the Office of the Valuer General at 30 June 1993 (using the 'market value adjacent site' method) and was indexed using the 'all lands' index to a 30 June 1998 valuation.

Approximately 545 hectares of Crown land has been recognised in the financial records of Melbourne Water in 1997/98. The increase in non current assets of \$2.9 million has been adjusted against contributed capital. In 1996/97, approximately 62,120 hectares of Crown land (\$13.8 million) was divested from Melbourne Water. Refer to Notes 1.3 and 16.

State Digital Map Base

The Corporation has an interest in the State digital map base controlled by Geographic Data Victoria. The value of Melbourne Water's interest in the State digital map base is not considered material in the context of the Corporation's accounts and it is not included as an asset. In 1997/98 Melbourne Water received \$23,538 (\$12,000 in 1996/97) in royalties from this interest.

12 NON CURRENT ASSETS - OTHER

	1998	1997
	\$000	\$000
Other Receivables	180	-
Deferred Expenses	121	-
Future income tax benefit	11,068	23,607
Total non current assets - other	11,369	23,607

NOTES TO THE ACCOUNTS

13 CURRENT LIABILITIES – CREDITORS

	1998 \$000	1997 \$000
Trade creditors and accruals	71,353	99,834
Advances	440	159
Total current liabilities – creditors	71,793	99,993

14 CURRENT LIABILITIES – PROVISIONS

Employee entitlements	10,270	13,177
Dividend	64,949	61,615
Income tax	1,526	29,892
Insurance claims	478	942
Other provisions	12,055	6,000
Total current liabilities – provisions	89,278	111,626

15 NON CURRENT LIABILITIES – PROVISIONS

Employee entitlements	11,723	16,752
Deferred income tax	207,466	154,602
Total non current liabilities – provisions	219,189	171,354

16 CONTRIBUTED CAPITAL

Opening balance	260,454	24,267
Adjustment to Crown land #	6,225	(13,813)
Capital restructure *	337,357	250,000
Closing balance	604,036	260,454

Refer to Notes 1.3 and 11 for explanation of adjustments to Crown land.

* On 1 January 1998, debt with a book value of \$337M was transferred from the Corporation to the State, being part of the major reforms introduced by the State to water and sewerage pricing for Melbourne effective from that date. Refer to Note 1.8.

NOTES TO THE ACCOUNTS

17 AUDITORS' REMUNERATION

	1998 \$000	1997 \$000
Amounts received, or due and receivable, by the auditor for auditing the accounts of the Corporation.	87	90

18 DIRECTORS' REMUNERATION

Income received or due and receivable by directors	499	451
The number of directors of the Corporation included in these figures are shown below in their relevant income bands:		
Remuneration between	<i>Number</i>	<i>Number</i>
\$30,000 – \$39,999	4	4
\$60,000 – \$69,999	1	1
\$200,000 – \$209,999	–	1
\$250,000 – \$259,999	1	–

19 EXECUTIVES' REMUNERATION

Income received or due and receivable by executive officers whose income is more than \$100,000.	3,830	3,931
The number of executive officers whose income is more than \$100,000 are shown below in their relevant income bands:		
Remuneration between	<i>Number</i>	<i>Number</i>
\$100,000 – \$109,999	6	8
\$110,000 – \$119,999	7	11
\$120,000 – \$129,999	3	4
\$130,000 – \$139,999	1	3
\$140,000 – \$149,999	6	3
\$150,000 – \$159,999	2	1
\$160,000 – \$169,999	3	2
\$200,000 – \$209,999	1	–

NOTES TO THE ACCOUNTS

20 CONTINGENT LIABILITIES

	1998 \$000	1997 \$000
Details and estimates of maximum amounts of contingent liabilities for which no provision is included in the accounts, are as follows:		
Cross Border Lease		
Finance lease liability subject to a debt extinguishment arrangement.	–	503
The primary obligation to repay the finance lease principal and interest for the above arrangement has been 'in substance' assumed by third parties. The transaction has been arranged in such a manner so as to ensure that there is virtually no risk that Melbourne Water will be required to meet the lease commitments on maturity. The liability has therefore been excluded from the Balance Sheet in accordance with Australian Accounting Standard AAS23 'Set-off and Extinguishment of Debt'.		
The underlying obligation matured during 1997/98.		
Other Outstanding Claims		
Claims or possible claims against the Corporation arising out of various matters connected with the Corporation's business dealings.	801	1,239
Remediation Costs		
During the reporting period, the Corporation has provided for the remediation costs of some surplus sites. In future periods additional costs may be incurred for the remediation of sites prior to disposal.		

NOTES TO THE ACCOUNTS

21 COMMITMENTS

	1998 \$000	1997 \$000
Capital Commitments		
Total capital expenditure contracted for the construction of water, sewerage and drainage infrastructure at balance date but not provided for in the accounts.		
Not later than one year	21,175	35,771
Later than one year but not later than 2 years	1,092	5,510
Total capital commitments	22,267	41,281
Lease Commitments		
Total lease expenditure contracted for at balance date but not provided for in the accounts.		
Not later than one year	2,250	2,288
Later than one year but not later than 2 years	2,357	1,530
Later than 2 years but not later than 5 years	1,405	2,468
Later than 5 years	131	11
Total lease commitments	6,143	6,297
There are no commitments in relation to finance leases.		
Other Operating Commitments		
Total operating expenditure (excluding lease) contracted for at balance date but not provided for in the accounts.		
Not later than one year	19,141	20,326
Later than one year but not later than 2 years	15,803	16,140
Later than 2 years but not later than 5 years	20,045	28,135
Later than 5 years	46,159	50,447
Total other commitments	101,148	115,048

NOTES TO THE ACCOUNTS

22 EMPLOYEE ENTITLEMENTS

	1998 \$000	1997 \$000
Aggregate employee entitlements liability		
Accrued wages and salaries (part of Note 13)	829	805
Provision for employee entitlements current (Note 14)	10,270	13,177
Provision for employee entitlements non current (Note 15)	11,723	16,752
Total employee entitlements liability	22,822	30,734
<p>The aggregate employee entitlement liability includes amounts for annual leave, shift leave, long service leave, salaries and wages, WorkCover and unfunded superannuation.</p> <p>All employees of the Corporation are entitled to superannuation benefits upon retirement, disability or death through membership of the following funds:</p>		
Defined Benefits Fund		
<p>The Water Industry Superannuation Fund provides lump sum benefits based on length of service and final superannuable salary for employees engaged up until 31 December 1993. Employees contribute at rates between 0% to 7.5% of their salary. The Corporation contributes to the fund based upon an actuarial assessment rate of 13% of members' salaries.</p> <p>Actuarial assessment of the fund is made at yearly intervals. The last such assessment was made as at 30 June 1998 by William M. Mercer Pty Ltd.</p>		
Present value of employees' accrued benefits	45,200	46,400
Net market value of assets held by the fund	52,963	48,314
Excess of present value of employees' accrued benefits over assets held to meet future benefit payments	(7,763)	(1,914)
Vested benefits	56,500	58,000
<p>The unfunded superannuation liability (\$4.2 million for 1997/98) is measured as the difference between the Water Industry Superannuation Fund assets and the employees' vested benefits, after allowing for the impact of the 15% tax on contributions.</p>		
Vested benefits	56,500	58,000
Net market value of assets held by the fund	52,963	48,314
	3,537	9,686
Impact of contributions tax	624	1,709
Unfunded superannuation liability	4,161	11,395

NOTES TO THE ACCOUNTS

	1998 \$000	1997 \$000
Accumulation Funds		
<p>Employees engaged from 1 January 1994 are entitled to benefits under accumulation funds. The majority of these employees are covered by LASPLAN. Employees have the opportunity to contribute to the funds at a self-nominated rate or amount. The minimum employer contribution to the funds are pursuant to the Superannuation Guarantee Charge, which was 6.0% in 1997/98.</p>		
Employer Contributions		
Employer contributions to the funds	10,751	19,313
<p>The contributions in 1997/98 include additional contributions of \$1.8 million (\$5.1 million in 1996/97) to ensure that the funding level of the schemes did not deteriorate as a result of redundancies and cash injections to the Water Industry Superannuation Fund of \$6.0 million as part of a program to return the fund to a position where it is fully funded by September 1998.</p>		
Loans		
<p>There were no loans by the superannuation funds to Melbourne Water during 1997/98.</p>		
23 RECONCILIATION OF NET CASH PROVIDED BY OPERATING ACTIVITIES TO OPERATING PROFIT AFTER INCOME TAX		
	1998 \$000	1997 \$000
Operating profit after income tax	160,619	166,420
Depreciation	55,265	62,060
Adjustment to finance charges	952	(4,783)
Provision for doubtful debts	(211)	(388)
Profit on sale of assets	(10,830)	(14,578)
Loss on sale of assets	929	3,805
Value of works taken over from developers	(1,780)	(4,795)
Changes in assets and liabilities:		
Decrease in trade debtors	2,015	128
Decrease in other debtors	1	8
(Increase) in stores and livestock	(527)	(1,897)
(Increase) in prepayments	(171)	(252)
(Increase) in deferred expenses	(192)	-
Decrease in future income tax benefit	12,539	17,762
(Decrease)/increase in trade creditors	(13,013)	7,691
Increase/(decrease) in interest creditors	22,614	(9,264)
Increase in deferred revenue	45	-
(Decrease) in other provisions	(2,345)	(17,114)
(Decrease)/increase in provision for income tax	(28,366)	29,892
Increase in provision for deferred income tax	52,864	49,323
Net cash provided by operating activities	250,408	284,018

NOTES TO THE ACCOUNTS

24 RELATED PARTIES DISCLOSURE

Responsible persons

Persons who held office as a director of Melbourne Water Corporation at any time during the year ended 30 June 1998 are as follows: A A Browne, R V Gilbert, J M King, B Solnordal and C J Stewart.

J E Morgan retired from the Corporation with effect 31 January 1998.

B R Bayley was appointed as Chief Executive Officer of Melbourne Water Corporation from 1 February 1998.

The responsible Minister during the year ended 30 June 1998 was the Hon P McNamara, Minister for Agriculture and Resources.

Remuneration of responsible persons

Information on the remuneration of directors is disclosed in Note 18.

Loans to responsible persons

There were no loans to responsible persons at 30 June 1998.

Other transactions of responsible persons and their related parties

A director, A A Browne, is a partner in the firm Arthur Robinson & Hedderwicks, solicitors, which has provided legal services to Melbourne Water during the reporting period on normal commercial terms and conditions.

A director, J M King, was a director of MITS Ltd which has provided technology services to Melbourne Water during the reporting period. Services provided during the reporting period were on normal commercial terms and conditions.

The aggregate amount of each of the above types of other transactions with responsible persons and their related parties were as follows:

	1998 \$000	1997 \$000
Legal and professional fees	497	657
Technology services	4,564	4,671

25 ECONOMIC DEPENDENCY

The normal trading activities of the Corporation depend to a significant extent on the sale of bulk water and sewerage services to Yarra Valley Water Ltd, South East Water Ltd and City West Water Ltd. In addition, the Corporation depends on Yarra Valley Water Ltd, South East Water Ltd and City West Water Ltd for the provision of billing and collection services with respect to drainage rates.

26 EVENTS OCCURRING AFTER BALANCE DATE

No material events occurred after balance date.

NOTES TO THE ACCOUNTS

27 FINANCIAL INSTRUMENTS

27.1 Interest rate exposure

The Corporation's interest rate and the effective weighted average annual interest rate for each class of financial asset and liability is set out below.

30 June 1998	Weighted avg. annual effective interest rate	Floating interest rate	Fixed interest rate maturing			Non interest bearing	Total \$000
	%	\$000	1 year or less \$000	1 to 5 years \$000	over 5 years \$000	\$000	
FINANCIAL ASSETS							
Cash	4.84	409	-	-	-	-	409
Trade debtors		-	-	-	-	11,649	11,649
Other receivables		-	-	-	-	10,325	10,325
Deposits	5.07	-	5,003	-	-	-	5,003
Total financial assets		409	5,003	-	-	21,974	27,386
FINANCIAL LIABILITIES							
Trade creditors and accruals		-	-	-	-	72,882	72,882
Advances		-	-	-	-	440	440
Borrowings*	6.05	125,000	106,800	400,000	650,000	-	1,281,800
Total financial liabilities		125,000	106,800	400,000	650,000	73,322	1,355,122
NET FINANCIAL ASSETS (LIABILITIES)		(124,591)	(101,797)	(400,000)	(650,000)	(51,348)	(1,327,736)

30 June 1997

FINANCIAL ASSETS							
Cash	5.10	616	-	-	-	-	616
Trade debtors		-	-	-	-	9,613	9,613
Other receivables		-	-	-	-	16,462	16,462
Deposits	5.55	-	10,003	-	-	-	10,003
Total financial assets		616	10,003	-	-	26,075	36,694
FINANCIAL LIABILITIES							
Trade creditors and accruals		-	-	-	-	100,174	100,174
Advances		-	-	-	-	159	159
Borrowings	8.72	250,000	161,742	528,726	695,747	-	1,636,215
Interest rate swaps **	10.12	(135,000)	-	-	135,000	-	-
Total financial liabilities		115,000	161,742	528,726	830,747	100,333	1,736,548
NET FINANCIAL ASSETS (LIABILITIES)		(114,384)	(151,739)	(528,726)	(830,747)	(74,258)	(1,699,854)

* Of the total amount of borrowings at floating interest rate, \$50 million will mature within 12 months and the remaining \$75 million will mature in 1 to 3 years.

** During 1997/98, all interest swap positions were novated to the State of Victoria under a major debt restructuring initiative, implemented as part of the water industry pricing reforms. Refer to Note 1.8.

NOTES TO THE ACCOUNTS

27 FINANCIAL INSTRUMENTS

27.2 Market value

The book values and net market values of financial assets and liabilities at balance date are as follows.

	1998 Book value \$000	1998 Net market value* \$000	1997 Book value \$000	1997 Net market value* \$000
ON BALANCE SHEET				
Financial assets				
Cash	409	409	616	616
Trade debtors	11,649	11,649	9,613	9,613
Other receivables	10,325	10,325	16,462	16,462
Deposits	5,003	5,003	10,003	10,003
Total financial assets	27,386	27,386	36,694	36,694
Financial liabilities				
Trade creditors and accruals	72,882	72,882	100,174	100,174
Advances	440	440	159	159
Borrowings	1,281,800	1,306,812	1,636,215	1,755,450
Total financial liabilities	1,355,122	1,380,134	1,736,548	1,855,783
OFF BALANCE SHEET				
Financial liabilities				
Interest rate swaps	-	-	-	75,503
Total financial liabilities	-	-	-	75,503

* Net market values are capital amounts. The differences between book values and net market values relate principally to interest rate movements

Melbourne Water had no derivative positions as at 30 June 1998.

Net market values of financial instruments are determined on the following basis:

(a) On Balance Sheet

Cash, deposit investments, short term borrowings, cash equivalents and non interest bearing financial assets and liabilities (trade debtors and trade creditors) are valued at cost.

Other borrowings are estimated based on the present value of expected future cash flows discounted at current market interest rates quoted for securities issued by Treasury Corporation of Victoria (TCV).

Investments in securities, other financial assets and liabilities are estimates based on present value of expected future cash flows discounted at current market interest rates for assets and liabilities of similar risk and maturity structure.

(b) Off Balance Sheet

Interest rate swaps being the difference in net present values of the future cash flows, discounted at current market interest rates quoted for equivalent TCV swap positions.

NOTES TO THE ACCOUNTS

27.3 Credit Risk

The carrying amounts of financial assets included in the balance sheet represent the Corporation's exposure to credit risk in relation to those assets, net of any provisions for doubtful debts.

For off balance sheet derivative financial instruments, credit risk arises from the potential failure of counterparties to meet obligations under contract. Risk is quantified using the Reserve Bank's current exposure method, which at 30 June 1998 was nil.

Melbourne Water controls risk through credit ratings, limits and monitoring procedures consistent with Board approved policy. Collateral or other security is not required to support financial instruments.

All financial risk management instruments are transacted with the Treasury Corporation of Victoria (TCV), whose liabilities are guaranteed by the Government of Victoria. Melbourne Water potentially has a concentration of credit risk with TCV as the central borrowing authority of Victoria. The risk is considered minimal.

Melbourne Water does not have any significant trade credit exposure to an individual counterparty as at 30 June 1998.

27.4 Financing Arrangements

The capacity to borrow funds and manage the associated risks is subject to the provisions of the Borrowing and Investment Powers Act (1987). In accordance with this Act, the Victorian Treasurer issues annual approvals permitting new borrowings and the refinancing of all loan maturities for that year.

All funding is sourced from the Treasury Corporation of Victoria.

28 TRANSACTIONS WITH OTHER VICTORIAN GOVERNMENT ENTITIES

Material transactions under taken with other State Government controlled entities in the ordinary course of business

	1998 \$000	1997 \$000
Revenue	514,095	621,116
Liabilities	1,570,687	1,727,707
Expenses	341,594	327,499

Intra denotes entities within the same portfolio as Melbourne Water.
Inter denotes entities outside the portfolio.

STATEMENT BY DIRECTORS AND CHIEF FINANCE OFFICER

In the opinion of the directors of Melbourne Water Corporation:

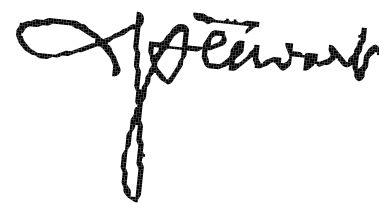
- (a) the accompanying financial statements are drawn up so as to present fairly the financial transactions of the Corporation for the year ended 30 June 1998 and the financial position of the Corporation as at that date; and
- (b) at the date of this statement there are reasonable grounds to believe that the Corporation will be able to pay its debts as and when they fall due.

We certify that the financial statements have been prepared in accordance with the requirements of the *Financial Management Act 1994* and applicable accounting standards.

We are not aware, at the date of this statement, of any circumstance which would render any particulars in the financial statements to be misleading or inaccurate.

Dated at Melbourne on this 21st day of August 1998.

On behalf of the Board:



C J Stewart
(Chairman)



B R Bayley
(Managing Director)



D J Corney
(Chief Finance Officer)

AUDITOR-GENERAL'S REPORT



AUDIT SCOPE

The accompanying financial statements of the Melbourne Water Corporation (trading as Melbourne Water) for the year ended 30 June 1998, comprising profit and loss account, balance sheet, statement of cash flows and notes to the accounts, have been audited. The members of the Corporation's Board are responsible for the preparation and presentation of the financial statements and the information they contain. An independent audit of the financial statements has been carried out in order to express an opinion on them as required by the *Audit Act 1994*.

The audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance as to whether the financial statements are free of material misstatement. The audit procedures included an examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with Australian Accounting Standards and other mandatory professional reporting requirements and comply with the requirements of the *Financial Management Act 1994*, so as to present a view which is consistent with my understanding of the financial position of the Melbourne Water Corporation and the results of its operations and its cash flows.

The audit does not provide any assurances that the Melbourne Water Corporation systems, or any other systems that the entity relies on in the conduct of its activities such as those of suppliers and service providers are year 2000 compliant, or whether plans and associated actions are adequate to address the year 2000 issue. The year 2000 issue has been addressed only in the context of existing audit responsibilities under Australian Auditing Standards to express an opinion on the financial statements.

The audit opinion expressed on the financial statements has been formed on the above basis.

AUDIT OPINION

In my opinion, the financial statements present fairly the financial position of the Melbourne Water Corporation as at 30 June 1998 and the results of its operations and its cash flows for the year ended on that date in accordance with Australian Accounting Standards and other mandatory professional reporting requirements and comply with the requirements of the *Financial Management Act 1994*.

Melbourne 21 / 8 / 1998



C A Baragwanath
Auditor-General

STATEMENT OF CORPORATE INTENT

1 July 1998 to 30 June 2001

INTRODUCTION

Melbourne Water Corporation is a statutory corporation wholly owned by the Victorian Government. The major functions are to:

- provide water and sewerage wholesale services to three retail water companies in Melbourne, viz Yarra Valley Water Ltd, South East Water Ltd and City West Water Ltd; and
- provide major drainage services, manage designated waterways and under take the operational functions of floodplain management (by Deed of Delegation from the Minister) to the greater Melbourne area.

PURPOSE

Melbourne Water Corporation exists to operate a successful commercial business which supplies safe water and removes sewage and stormwater at an acceptable cost and in an environmentally sensitive manner for the benefit of present and future Melburnians.

BUSINESS OBJECTIVES

Melbourne Water is committed to being a successful commercial business and places high priority on its responsibilities to the community, the environment and public health. The principal business objectives of the Corporation are to:

Commercial

- focus on the core businesses of water, sewerage and waterways and drainage
- ensure business risks are properly managed
- take a medium to long term view of the business and its assets to ensure ongoing viability based on increasing shareholder value

Customers

- maintain or improve the levels of service to customers
- foster effective relationships with the retail water companies
- ensure efficient and effective drainage services are provided to meet the needs of the land development industry
- ensure the implementation of Government policy in relation to land development activities impacting on flood plains

Environment and Public Health

- provide a low cost, reliable supply of safe high quality drinking water that consistently meets required standards
- dispose of sewage in an environmentally sensitive manner in accordance with Environment Protection Authority (EPA) requirements
- minimise the impact of stormwater on receiving waters thereby contributing to improved waterway water quality

Employees

- foster a work environment where people can perform to their full potential and understand and are committed to the achievement of the Corporation's goals.

COMMERCIAL ARRANGEMENTS

Scale of the Business

- Melbourne Water has total assets of approximately \$2.7 billion.
- An annual operating revenue of approximately \$438 million is derived mainly from bulk water and sewerage services to the retail water companies and from drainage services to the community.
- Approximately 474 gigalitres per annum of potable water is supplied to the retail water companies.
- Approximately 332 gigalitres per annum of sewage is collected from the retail water companies for treatment and disposal.
- Regional drainage services are provided within the greater Melbourne area covering approximately 7,800 square kilometres. (municipalities are responsible for local drainage systems).

Business Activities

Melbourne Water will under take the following principal business activities:

- management and operation of the bulk water, sewerage and drainage systems of Melbourne,
- enhancement of water quality in waterways and flood protection,
- maintenance of assets in good structural and hydraulic condition,
- management of infrastructure augmentation for improved service delivery, compliance with regulatory standards, urban growth and asset replacement, and
- undertaking of technology innovation through research and development to improve productivity and manage business risks.

Basis of Charges

Melbourne Water charges for its services to:

- ensure revenue adequacy to cover operations and maintenance costs, finance costs, capital investment, dividend, tax payments and debt retirement, and
- earn an appropriate commercial return on new investment having regard to the risk of the business.

The charges for bulk water and sewerage services are:

- based on recovering the total economic cost of service delivery, and
- structured so that approximately half of the costs are recovered through fixed charges and the remainder through variable charges based on the volume of water delivered and sewage treated.

Drainage charges are based on the rateable value of properties.

Capital Investment

Melbourne Water has made provision for significant capital investment to:

- meet the expected growth in demand from population increases,
- meet environmental standards,
- improve drinking water quality,
- improve water quality in Melbourne's waterways,
- maintain assets in serviceable condition, and
- improve flood protection.

The planned allocation of capital investment for 1998/99 is:

Growth	7 %
Compliance/Quality	32 %
Structural Condition	24 %
Business Systems	12 %
Flood Protection	16 %
Other	9 %

Dividend

The dividend to be paid to Government will be in accordance with the amount determined by the Victorian Treasurer after consultation with the Corporation's Board of Directors. Melbourne Water's dividend recommendation will be based on a review of its current financial position and longer term financial obligations.

STATUTORY REQUIREMENTS

Environmental / Health Regulations

Melbourne Water is committed to meeting statutory and other requirements. In particular, Melbourne Water is committed to:

- compliance with EPA discharge licences issued for the Eastern and Western Sewage Treatment Plants and other related agreements or understandings,
- achieving drinking water quality standards specified in the bulk water supply contracts between Melbourne Water and the retail water companies,
- undertaking improvement works in areas identified in contracts with the retail water companies to improve drinking water quality, and
- compliance with the Victorian *Occupational Health and Safety Act 1985* and regulations.

BUSINESS TARGETS	1997/98	1998/99	1999/00	2000/01
Operational Performance	Actual	Target	Target	Target
Drinking Water Quality (% compliance with quality requirements at wholesale/retail interface)	99.9%	100%	100%	100%
Effluent Discharge Quality to Water (% compliance with EPA Licence at Sewage Treatment Plants)	99.9%	100%	100%	100%
Waterways Alerts (% water quality alert levels reported to EPA)	100%	100%	100%	100%
Developer Offers Processed (% applications processed within 60 days)	96%	96%	97.5%	97.5%
Business Performance				
Return on average assets	13.3%*	8.6%	8.9%	9.0%
Return on average equity	18.3%*	9.7%	9.9%	10.2%
Gearing (interest bearing debt to total assets)	47.1%	47.2%	45.8%	44.2%
Funds from Operations Interest Cover (Times)	3.17	3.51	3.63	3.55
Capital Investment to Operating Revenue	14.1%	18.2%	22.8%	20.3%
Lost Time Injury Frequency Rate	5.6	0	0	0

* Ratios directly affected by water and sewerage pricing reform from 1 January 1998.

Performance Reporting

The operational and financial position of the Corporation will be reported to the Government as owner at the end of each financial year.

Melbourne Water will demonstrate its commitment to environmental and public health performance by annual public reporting on its regulatory and internal procedures and policies and performance against established benchmarks.

BUSINESS POLICIES

Human Resources

As a sound business practice and in recognition that employees are a valuable resource, Melbourne Water will give priority to the following initiatives:

- training that enables all individuals to fulfil their job requirements,
- market based remuneration system to reward and recognise superior performance,
- development of a teams based way of working across the Corporation,
- career and skill development planning for all employees,
- succession planning for management positions and key technical positions, and
- achieving the target of an injury free workplace.

Code of Conduct

Melbourne Water has adopted a Code of Conduct which outlines the standards expected of all employees. The Code covers ethics, responsibility to stakeholders, standards of behaviour, conflict of interest, confidential information, public statements, equal opportunity and occupational health and safety.

Public Health

Melbourne Water will ensure that public health is safeguarded through the:

- reliable supply of safe drinking water primarily using water harvested from protected water supply catchments,
- collection and treatment of sewage and disposal and storage of by-products in accordance with EPA requirements, and
- contribution to improvement of waterway water quality and minimisation of the impacts of stormwater on receiving waters.

Environmental Practices

Melbourne Water will work to improve its environmental management capabilities and ensure that its environmental management systems generally conform with guidelines adopted by the water industry in Australia.

Research and development programs will be conducted to enable the practical application of innovative low cost solutions in the delivery of environmental programs.

Community Responsibility

Melbourne Water is committed to the community. In particular, Melbourne Water will:

- participate in public debate on undertakings which impact on the environment or the standard of services that are to be provided,
- endeavour to understand the concerns and needs of local communities where Melbourne Water's operations potentially have impact, and
- continue to undertake community education and liaison programs on the water supply and sewerage systems, the impact of stormwater on the waterways of Melbourne and Port Phillip Bay and other major issues relevant to the community.

Risk Management

Melbourne Water will incorporate a risk management approach in conducting its business activities with the objective of understanding the nature of the risks involved and managing these in a cost effective way.

A framework, broadly based on the Australian standard for risk management, will be used that integrates risk management into existing procedures. The system will enable informed management decision making and the efficient allocation of resources to resolve issues.

Accounting Policies

The financial statements will be prepared in accordance with the *Financial Management Act 1994*, Australian Accounting Standards, Urgent Issues Group Consensus Views and relevant statutory and other requirements. Where appropriate, the disclosure requirements of Corporations Law will also be observed on a voluntary basis.

