

**Western Australian Treasury Corporation -**

Dr S.C. Thomas, Chairman.

Mr E.S. Ripper, Treasurer.

Mr M. Webb, Chief Executive Officer.

Mr M.A. Nunes, Deputy Chief Executive Officer.

Mr S.L. Luff, Manager, Finance and Administration.

**The CHAIRMAN:** This estimates committee will be reported by Hansard staff. The daily proof *Hansard* will be published at 9.00 am tomorrow.

Members may raise questions about matters relating to the operations and budget of the off-budget authority. Off-budget authority officers are recognised as ministerial advisers.

It is the intention of the Chairman to ensure that as many questions as possible are asked and answered and that both questions and answers are short and to the point.

The minister may agree to provide supplementary information to the committee, rather than asking that the question be put on notice for the next sitting week. For the purpose of following up the provision of this information, I ask the minister to clearly indicate to the committee which supplementary information he agrees to provide and I will then allocate a reference number. If supplementary information is to be provided, I seek the minister's cooperation in ensuring that it is delivered to the committee clerk by 8 June 2007, so that members may read it before the report and third reading stages. If the supplementary information cannot be provided within that time, written advice is required of the day by which the information will be made available. Details in relation to supplementary information have been provided to both members and advisers, and accordingly I ask the minister to cooperate with those requirements.

I caution members that if a minister asks that a matter be put on notice, it is up to the member to lodge the question on notice with the Clerk's office. Only supplementary information that the minister agrees to provide will be sought by 8 June 2007.

It will also greatly assist Hansard if, when referring to the program statements, volumes or the consolidated account estimates, members give the page number, item, program, amount in preface to their question.

**Mr E.S. RIPPER:** I might say that this is the first time Western Australian Treasury Corporation has appeared before the estimates committee, certainly in recent years.

**The CHAIRMAN:** The member for Vasse.

**Mr T. BUSWELL:** I am interested in perusing the budget papers, in particular the revenue to government from public corporations. The estimated dividend payment from Treasury Corporation for 2007-08 is almost \$2 million less than the dividend in 2006-07. That is a significant reduction. Can the Treasurer give an overview of why the expected dividend payment from Treasury Corporation has dropped by effectively 40 per cent? That is found in budget paper No 3, *Economic and Fiscal Outlook*. I am seeking some background information on Treasury Corporation.

**Mr E.S. RIPPER:** I will make some general comments. I am sure that the CEO can provide more detail. The profit and, therefore, the dividend payments of Treasury Corporation depend partly on the amount of borrowings that government agencies are involved in, and partly on the conditions in the various markets from which those funds are sourced. How those two matters are playing out in the profit figures, I think Mr Webb is better placed to explain.

**Mr M. Webb:** Certainly. Treasury Corporation's pricing policy is set to recover its total cost of operations from the provision of services to the Western Australian public sector. These costs are loosely broken down into what we refer to as administrative expenses, and generating a requisite commercially risk-adjusted return on the capital invested in the business. The estimates in the forward years reflect our base profit and loss forecasting. That is based on our estimates of borrowings outstanding in those forward years, growth in our administrative expenses, and also the necessary requisite return on capital invested in the business. The reduction of 40 per cent to which the member referred is a reflection of a year of over-performance by the corporation. The figures that are shown in the budget papers reflect the more normal return on capital invested in the business. Treasury Corporation has a fixed-dividend policy, which is 50 per cent of our after-tax profit. Therefore, the reduction would be a reduction in our after-tax profit, driven simply by a return to normal circumstances.

**Mr E.S. RIPPER:** I commend to members the quarterly reports of Western Australian Treasury Corporation, which are tabled in the house. Those reports contain an explanation of how Treasury Corporation benchmarks its administration costs, and the benefits that it delivers to agencies. That provides a very useful background. It

certainly convinces me, and I hope also the member, that Treasury Corporation is running a very good operation, as it should.

**Mr T. BUSWELL:** I endorse the Treasurer's comments. From all the information that I get from what I read and what I am told by people - which is not a lot, of course, being in opposition - Treasury Corporation is doing a very good job. This is just a good opportunity to ask a couple of questions.

**Mr E.S. RIPPER:** Sure.

**Mr T. BUSWELL:** I am interested to know what Treasury Corporation's target for return on capital is expected to be this financial year. I am interested to know that, firstly, so that I can understand how good Treasury Corporation's performance has been in generating a return on capital, and, secondly, so that I can understand how bad my performance has been in generating a return on my capital!

[12.40 pm]

**Mr E.S. RIPPER:** I will ask Mr Webb to respond to those matters. Unfortunately, he cannot deal with the member's capital management issues.

**Mr M. Webb:** I will deal with the forward period first; it is the easier question to answer. Our return on the capital benchmark that is set is essentially an outcome of an application of a capital asset pricing model. We use two factors for that. The first is a riskless rate of return, which, in the case of our application of the capital asset pricing model, is the commonwealth 10-year bond rate. On top of that is added an adjustment factor for the risk within the business. That adjustment factor is a combination of what we refer to in finance as being a beta for the firm applied against the market risk premium. The actual mechanism of the capital asset pricing model methodology is determined by international accounting firm KPMG and was last reviewed in April 2005. At this point I cannot say exactly what the required benchmark rate of return for business is in the forward year. That will be determined by the prevailing commonwealth bond rate on 1 July of the new financial year. For our current year's performance, I might defer to Mr Luff.

**Mr S.L. Luff:** The estimated return on capital that we are looking at for this year is 13.63 per cent.

**Mr T. BUSWELL:** That is obviously well above what I imagined the target was based on, given those other factors.

**Mr T.G. STEPHENS:** In reference to the Treasurer's supervision of Treasury Corporation, I note that his federal counterpart, in his supervision of the Future Fund, has allowed for the outsourcing of the custodial services for the Future Fund to go to an organisation called Northern Trust, closely associated with Enron and the collapse of Enron. Does the Western Australian government expose itself to the same level of risk that the federal government has now exposed itself to through the Future Fund by outsourcing to organisations such as the Northern Trust in the United States that have been caught up in the collapse of Enron?

**Mr E.S. RIPPER:** I have just been checking with the CEO as to who provides these types of services for Treasury Corporation. I am advised that the Commonwealth Bank of Australia provides the banking service.

**Mr T.G. STEPHENS:** Are all our custodial services done by that bank?

**Mr E.S. RIPPER:** I will ask Mr Webb to outline the various services and who provides them.

**Mr T.G. STEPHENS:** The Treasurer is not as risky as Mr Costello, I understand.

**Mr E.S. RIPPER:** Mr Webb will not comment on that.

**Mr M. Webb:** Our banking services are provided by the Commonwealth Bank of Australia under a government arrangement. Our registry services are provided through Austraclear, which is an owned subsidiary of the Sydney Futures Exchange, which in turn is a subsidiary of the Australian stock exchange, an Australian listed company. Our registry services, the services that maintain the register of all our lenders, are maintained by an Australian group known as Computershare International.

**Mr C.J. BARNETT:** My question relates to the loans through Treasury Corporation to each of the four electricity utilities. Does the Treasurer apply a different rate or risk premium to each of those utilities; if so, how would he rank them in terms of risk?

**Mr E.S. RIPPER:** That is a very good question; I will ask Mr Webb to answer it.

**Mr M. Webb:** In short, no. We would price debt to each of the entities based on prevailing Australian reference rates at the time of drawing. A common administrative margin is applied to each of those entities. The only form of adjustment is the Treasurer's guarantee that we charge to each of those entities, and that guarantee factor is common across the public sector.

**Mr C.J. BARNETT:** There is a government guarantee there but there is \$2 billion worth of debt attached to the net worth, which I would think is pretty secure. There is \$740 million worth of debt attached to Verve Energy. In the marketplace, I would think that that would be seen to necessitate having a risk premium attached to it.

**Mr E.S. RIPPER:** The member for Cottesloe raises an interesting issue. My understanding is that government trading enterprises trade under the umbrella of the state's AAA credit rating. If the member is interested in questions of competitive neutrality, he might then ask whether that should be the case for every government trading enterprise, including those competing with private sector competitors that do not have the capacity to take advantage of the government's AAA credit rating. We work hard to preserve the government's AAA credit rating and we have to take the rough with the smooth. If there is an organisation with more risk attached to it, that has to be offset against other entities in government that have less risk.

**Mr C.J. BARNETT:** The decision to apply the same rate is a policy decision. Regardless of risk, there is clearly a risk difference between a network and a power generator, particularly with old plant and equipment. To what extent do the real risks that attach to the real entities affect Treasury Corporation's ability when it goes into the market borrowing?

**Mr E.S. RIPPER:** I will ask Mr Webb to respond to that.

**Mr M. Webb:** Treasury Corporation does not access capital markets on the strength of its own balance sheet but by virtue of the explicit government guarantee on its liabilities.

**Mr C.J. BARNETT:** Do you think that will continue, though? We have seen situations internationally - I do not draw a comparison with Third World nations - in which the banks call it in effectively. That could happen. I would think the banks would be having a very careful look at South Australia, for instance. In this situation, Western Australia is strong but I do not think some of its entities are strong.

**Mr E.S. RIPPER:** The protection for this is the state's AAA credit rating. That is my understanding of how the system works. We have tried to persuade the ratings agencies to separate some of the trading enterprises in their consideration of the state's AAA credit rating. If we took a trading enterprise on its own, if it was a private company, it would not be trading at AAA; it would be trading at a lower credit rating because it would have more debt. In a sense our trading enterprises are arguably crimped by the requirement to have a AAA credit rating because the private sector competitors do not trade at AAA.

**Mr C.J. BARNETT:** I understand that point and it is a fair comment. Is the Treasurer detecting in the market that people are now starting to look at the actual assets behind a trading enterprise?

**Mr M. Webb:** No, by virtue of the fact that the rating agencies consider the gross government balance sheet position, which includes the net position of trading enterprises in their annual review. Western Australia is rated AAA and there is no talk of any other alternative rating at this point.

**Mr T. BUSWELL:** I am straying a little from the page in the budget papers but I do notice that in its last annual report, Treasury Corporation had an interesting foreign currency borrowing of \$NZ64 million. Could the Treasurer explain the background behind that borrowing of \$NZ64 million? It seems a little unusual to see borrowing in New Zealand dollars. Perhaps the Treasury could explain the genesis of that borrowing.

**Mr M. Webb:** The issue into New Zealand dollars was to meet the investment preferences of Japanese retail investors at the time. Japanese retail investors have an unusual position in that they prefer to chase absolute yield and take outright currency exposure in their investment decisions. At the time, commodity-backed currency, such as Australian dollars, New Zealand dollars and Canadian dollars, were the highest yielding currencies in the world and therefore Japanese retail funds float into those. Treasury Corporation responds to that and then hedges the foreign exchange risk through cross-currency swaps to produce effective Australian dollar cost funds that are lower than it could source domestically.

[12.50 pm]

**Mr C.J. BARNETT:** To what extent is Treasury Corporation's position affected by the recent appreciation of the Australian dollar?

**Mr M. Webb:** We have no net exposure to foreign exchange movements on the balance sheet.

**Mr C.J. BARNETT:** Does that include the old Western Power lines?

**Mr M. Webb:** Yes.

**Mr T. BUSWELL:** I am interested to understand the nature of advice, if any, provided by Treasury Corporation to the government on an issue that comes around at the end of each financial year regarding where a home is found for the government surplus.

**Mr E.S. RIPPER:** It is good to have a surplus to find a home for.

**Mr T. BUSWELL:** I am not arguing about that. I am arguing about the advice the Treasurer gets, if any, from Treasury Corporation. Does the Treasurer pop the cash in the bank and call it a repayment for the Perth-Mandurah railway project? That is basically a cash fund that I understand will be drawn down on slowly over the life of the project, as opposed to borrowings. Does Treasury Corporation provide the Treasurer with information to help the Treasurer make a sound financial decision about the destination of the end-of-year surplus? Does that include also comparing the benefits of using that surplus to retire debt instruments as opposed to ferreting it away for specific projects?

**Mr E.S. RIPPER:** I do not receive advice directly from Treasury Corporation on these issues; I receive advice from the Department of Treasury and Finance. It may be that on certain issues the Department of Treasury and Finance would consult Treasury Corporation. Mr Webb has just advised me that the Department of Treasury and Finance does take advice from Treasury Corporation on the investment of the public bank account balance. Late in the budget process the Department of Treasury and Finance usually gives me advice about the expected size of the cash surplus and presents me with a set of options for its use. Those options include the impact of various users of the surplus on different financial management aggregates and what happens when a certain parcel of debt is paid off and whether there is a premium for doing that, or whether there are any implications for the operating balance in future years if the superannuation liabilities are paid off. All those matters are considered as part of Treasury's discussions with me. On the basis of those discussions, I take a recommendation to the expenditure review committee and then to cabinet, where the matters are subject to further scrutiny.

**Mr T. BUSWELL:** Have any of the instrumentalities that have borrowed money through the corporations - they are listed in the back of the annual report - defaulted on any payments?

**Mr E.S. RIPPER:** I am unaware of any.

**Mr M. Webb:** We have never recorded a default on moneys advanced to an authority.

**Mr E.S. RIPPER:** An issue of major concern to the government and the Department of Treasury and Finance - it was not a default from a Treasury Corporation point of view - occurred when significant discussions took place between various government officers and the Shire of Cunderdin about the shire's financial position. The odd rogue local government is probably the biggest risk of default for Treasury Corporation.

**Mr R.C. KUCERA:** Were there any problems with the Shire of Busselton?

**Mr T. BUSWELL:** Despite its difficulties of governance, the Shire of Busselton's accounts are reasonably fiscally sound.

**Mr R.C. KUCERA:** I am not surprised; it is because of the value of properties there.

**The CHAIRMAN:** Do members have a substantive question?

**Mr E.S. RIPPER:** The finances of a shire are helped when someone increases the rates by 15 per cent in two years.

**Mr T. BUSWELL:** Yes, that did happen. The Treasurer is exactly right.

**The CHAIRMAN:** This banter is all very well, but can members get to a substantive question.

**Mr T. BUSWELL:** The Treasurer might be interested to know that in that instance, the CEO came to me with a proposition to either put up the rates by 20 per cent or go broke. I told the CEO that neither of those things would happen, and so we fixed the expenses.

I understand that the Financial Management Bill that was passed through the house gives the Treasurer more flexibility to invest in other instruments outside of those that have traditionally been defined. Is that accurate?

**Mr E.S. RIPPER:** My recollection is that those matters applied to the public bank account. There is always a trade-off between risk and reward. A conservative approach should be taken with the public bank account. Arguably, one could cut off one's nose to spite one's face by taking too conservative an approach.

**Mr T. BUSWELL:** I support the initiative because it is a good idea.

**Mr M. Webb:** Treasury Corporation is acting as an adviser to the Department of Treasury and Finance regarding the utilisation of the broader investment powers of the public bank account. We are working with the international firm Mercer's, which is an actuarial firm, to determine a new investment strategy for the public bank account. Needless to say, we would expect the net result to be conservative.

**Mr T. BUSWELL:** Are the directors of the public bank account paid a remuneration fee?

**Mr E.S. RIPPER:** Yes, they are. I do not have those figures in front of me. Perhaps Mr Webb has them.

**Mr M. Webb:** I do not have the figures with me, but they are paid. We can provide that information.

**The CHAIRMAN:** Is the member for Vasse seeking that as supplementary information?

**Mr T. BUSWELL:** It would be quite interesting. It could be the information that brings down the government!

**The CHAIRMAN:** Will the Treasurer confirm the information that he will supply?

**Mr E.S. RIPPER:** On that basis, no! Yes, I will provide information on the payments made to the directors of the public bank account.

*[Supplementary Information No A47.]*

**Mr E.S. RIPPER:** I thank all the officers who have provided information during this estimates committee process and also members opposite for their questions.

*Meeting suspended from 1.00 to 2.00 pm*