NZ TRANSPORT AGENCY
WAKA KOTAHI

General Circular Investment: Nº 14/03

Subject	**Change to terms of trade for June/July payments to approved organisations**
Circulation	Financial Managers (all Approved Organisations) Asset Managers (all Approved Organisations) Local Government New Zealand Office of the Auditor General
Circulated by	Bob Alkema – National Manager Investment
Date of Issue	28 October 2014

Purpose

This general circular advises a change to the NZ Transport Agency's terms of trade for the end-of-year claims paid in June/July to approved organisations, effective this financial year (2014/15), and sets out the Transport Agency's expectations of approved organisations claiming funding from the National Land Transport Fund.

The change to the terms of trade is that the Transport Agency reserves the right to defer the June/July payments of those approved organisations that claim in excess of their March quarter forecasts or exceed 15% of their annual expenditure in their June/July claims. Application of the revised terms of trade will take into account any special requests by the Transport Agency on specific approved organisations to make late claims.

The Transport Agency's expectations of approved organisations making claims on the National Land Transport Fund are that:

- approved organisations will make their claims on an accrual basis, that is they will claim on work completed in a month rather than wait until a supplier invoice is received before claiming;
- claims will be made regularly through each year as work progresses – for many programmed activities, e.g. public transport services, this means that accrued expenditure captured in the monthly claims will be reasonably evenly spread through the year;
- approved organisations will avoid holding off claims until the year end and will ensure that their June/July claims do not exceed 15% of their annual expenditure, ideally in each activity class;
- approved organisations will provide robust forecasts of their claims for the next 4 quarters and for the balance of the current NLTP, via the programme monitor module in Transport Investment Online, and will monitor their performance to improve their forecasts and claiming pattern.

Background and context

The Transport Agency is required under the Government Policy Statement on Land Transport to achieve value for money from the funding it provides for its own and approved organisation investment in the land transport network. A substantial part of achieving value for money is about investing in the right solution in the right place at the right time and at the right cost.

Part of the Transport Agency achieving value for money is also about how effectively it manages the National Land Transport Fund so that funds are used to the fullest extent possible each year in investments that create transport solutions for a thriving New Zealand. It is in this area of our business that approved organisations' forecasting and claiming performance has a profound impact on our ability to utilise the funding when it is available.

We seek your help to provide better forecasting and management of claims against forecast throughout the year. The more consistent the claims are against forecast throughout a financial year, the more promptly the claims are made on work completed and the more robust the forecasts that are provided, the better we can manage the National Land Transport Fund cash-flows and funding allocation.

Change to terms of trade

Historically, the claiming performance of many approved organisations has been irregular through each year, unrelated to the work progressed, and with substantial claims in the last two months of the year, commonly 18 to 24%. The resulting claims spike in July of each year, combined with less than robust forecasts, creates uncertainty for the Transport Agency and requires us to plan for a substantial cash-flow buffer in July, which ties up NLTF funds. In most years actual June/July claims undershoot the March quarter forecast and much of the buffer we hold is unnecessary. However, occasionally the year-end claim exceeds the forecast and we have difficulty in finding the cash to meet our terms of trade in respect of the end-of-year claims payments made in July.

We are committed to tighten up our cash-flow management and reduce the "just in case" buffer we hold for year-end claims. To enable this, we are changing the terms of trade so that, if we get into cash-flow difficulties around July of any year that threaten a breach of our short-term borrowing covenants with the government, we may choose to defer payments to those approved organisations that claim in excess of their March quarter forecasts or exceed 15% of their annual expenditure in their June/July claims. Application of the revised terms of trade will take into account any special requests by the Transport Agency on specific approved organisations to make late claims. In all other parts of the year, the current terms of trade of payment within 21 days of receipt of the verified claim will pertain.

The good news is that approved organisation claiming behaviour in 2012/13 was markedly better than for previous years, mostly led by the larger organisations. And the performance in 2013/14, while not as good as in 2012/13, was also an improvement on previous years. If this improvement can be sustained the deferral of payments may not need to be exercised.

Expectations of approved organisations making claims

Accrual based claims

The Transport Agency expects approved organisations to claim on an accrual basis - that is on the basis of an assessment of work completed rather than waiting for the supplier invoice before making a claim.

From the Transport Agency's perspective, this means that claims are tied to the work being undertaken, giving us a clearer view of actual expenditure through the year as well as increasing the certainty of the year end position. Our cash-flow management will improve as a result.

For an approved organisation, payment of claims on an accrual basis is efficient in terms of its cash-flow management, requiring less working capital to run the business and reducing interest costs. It should also give the approved organisation a clearer view of actual expenditure and improve the robustness of its forecasting.

Regular claiming

The Transport Agency expects regular monthly claims to be made by approved organisations. The more regular the claiming pattern, the better the view that both approved organisations and the Transport Agency have of actual expenditure through the year. For some programmed activities, such as public transport services, claims should be relatively evenly spread through the year, while for other activities, like road renewals, the claims should exhibit a seasonal pattern as the bulk of the works should be over the summer months.

Avoid leaving claims to year-end

The Transport Agency expects approved organisations to avoid leaving substantial claims to the end of each financial year and will ensure that their June/July claims are less than 15% of the annual expenditure. Ideally this should apply to each activity class. The more the claims are deferred to an end of year clean-up, the less visibility and certainty both approved organisations and the Transport Agency have of expenditure to date and the forecast year-end position, which makes efficient management of cash-flows and funding allocations very difficult.

Robust forecasting

The Transport Agency expects approved organisations to use the programme monitor module in TIO to provide robust forecasts of expected claims over the next four quarters and to the end of the current NLTP. We rely on forecasting to plan what debt we need to drawdown for cash-flow management and to allocate funding to fullest extent possible. Approved organisation forecasting is better than it used to be, but has a way to go before it could be considered robust. Collectively, we need to improve to provide more certainty so that the funding system performs as it should.

Enquiries

All enquiries relating to this circular should be directed to your local Transport Agency Planning and Investment Manager.

Bob Alkema
National Manager, Investment