CORRECTED TRANSCRIPT

PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

Inquiry into 2004–05 budget estimates

Melbourne – 19 May 2004

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Mr J. Brumby, Treasurer;

Mr I. Little, Secretary;

Mr S. Helgeby, deputy secretary, budget and financial management division; and

Ms H. Silver, deputy secretary, economic and financial policy division, Department of Treasury and Finance.

The CHAIR — We welcome our new witnesses from the Department of Treasury and Finance: Mr Ian Little, secretary; Mr Stein Helgeby, deputy secretary, budget and financial management division; Ms Helen Silver, deputy secretary, economic and financial policy division; and departmental officers. I call on the Treasurer to give a brief presentation on the more complex financial and performance information that relates to the 2004 budget estimates for the portfolio of the Treasurer.

Mr BRUMBY — Thank you, Chair. I will be very brief, because Ian Little will run through some of the slides from the department's perspective. I will very quickly run through some of the slides on the recent budget.

Overheads shown.

Mr BRUMBY — I think you are aware of these. Some of you may have seen these slides before.

The CHAIR — Yes, we had a very successful Department of Treasury and Finance breakfast.

Mr BRUMBY — I heard that was very good. Going to the next slide, I think you are aware of the surplus numbers — $545 million. We have average surpluses in excess of $500 million a year running forward, which is a good strong financial position. The next slide shows AAS31 and GFS figures. As I have explained before, GFS cash measures and also the budget are in surplus in each year in the forward estimates. Next, the debt curve shows debt paid down from close enough to $5 billion to just under $2 billion at the moment. So we have close enough to $2 billion of debt, with about $600 million over the forward estimates increasing up to about $2.7 billion or $2.8 billion and staying at about 1 per cent or 1.1 per cent of GDP, which is obviously very comfortably within the AAA rating.

Figures under the financial indicators continue to improve for us. Some of these are indicators that have been used in budget papers before and by the Auditor-General, and they are really an outstanding set of numbers about the fiscal strength of the state. On the tax side — I want to stress this, as I am sure I will get asked about tax today — I want to make the point that in this budget and from next year with debits tax there are significant tax reductions which are fully funded and in the forward estimates. That will result in Victoria's tax burden being below the national average by about 0.2 per cent and certainly now well below that of New South Wales. I will comment on that later if I have the opportunity.

We have a good set of growth numbers going forward — 3.25 to 3.5 per cent — and good employment growth. This slide shows business investment per capita. It is the same slide I have used every year in every budget presentation I have done, and it continues to show that Victoria is outperforming the average for Australia in business investment per capita. Unemployment is at a 14-year low. Again you see a very strong curve for the state. We have been below the national unemployment rate for 44 out of the last 45 months. It is a great outcome for Victoria.

I think you are aware we have been getting strong population growth from interstate. In the last year that growth rate has slowed a little, particularly as our property prices have moved up a bit closer to New South Wales, but it has been more than offset by a greater share of overseas migrants coming to Victoria. Victoria has about 25 per cent of the nation's population, as you know, and we have been getting about 28 per cent of the share of migrants, and as a consequence we are still getting population growth. If you look at the curve — the black line there which is Victorian population growth — in this last year our rate of growth actually exceeded the Australian rate of growth. If you look you will see that right back through the 1990s there was a huge gap there. That is quite an achievement for the state and one we are proud of.

You are familiar with the *Victoria — Leading the Way* statement: the main things there are the convention centre and the port vision. You are aware of the budget initiatives. We have had the debate in Parliament and the appropriation has been passed, so we are happy about that.

Mr FORWOOD — It has not been through the upper house yet.

Mr BRUMBY — I do not think you can block it any more. You never could.

Mr FORWOOD — The last time it was blocked, you guys did it.

Mr BRUMBY — On the slide showing record infrastructure investment you will see $2.9 billion — $10 billion over four years. Where is that going? It is going into schools, hospitals, economic infrastructure, roads and so on. We had a strong budget for provincial Victoria, and we make no apologies for this. Every budget we have delivered has been a positive one for provincial Victoria, and this continues our record. That is it from me. I think that was 3 minutes and 38 seconds!

The CHAIR — Am I game to correct the Treasurer?

Mr LITTLE — Good morning, Chair and members. I want to look at the impact of the budget on Treasury as a department, our objectives as a department, our new initiatives and, finally, what that means for our overall budget. Looking at the objectives, they have not changed from last year. There is one around sound financial management. The next is around provision of innovative police advice and the last is about service delivery.

Looking quickly at the new initiatives, government has provided ongoing funding of $2.8 million for the Victorian Competition and Efficiency Commission. This was announced in the economic statement *Victoria — Leading the Way*. It will be a statutory body reporting to the Treasurer supported by a secretariat based in DTF, and it will strengthen and incorporate the role previously played by the Office of Regulation Reform. The next initiative was a once-off $1.5 million increase in the department's budget to steward through when the changes to the Australian accounting framework are decided, which will be quite challenging and will involve this committee. In fact I would like to involve this committee if that is possible. The last is an ongoing funding item of $1 million for the State Revenue Office called the Land Rich Team. This is to ensure compliance with stamp duty legislation transactions involving land-rich trusts and companies.

On the asset initiatives side, the government increased the DTF budget to allow it to provide increased ICT — in fact renewed ICT infrastructure for both DTF and DPC over the next couple of years — for a total estimated investment (TEI) of $13 million. The next item allows the SRO to purchase over a two-year period land valuations from local councils. This is really an essential element of running the land tax system, but the government looks at the amount every two years. Lastly, the department will also administer the first-home home owners grant scheme which I am sure you all know about, the $5000 first home bonus. When you factor all those initiatives into DTF's base budget you see that our budget for 2004–05 increases from $178 million to $186 million, an increase of 4.1 per cent, and it is really those previous initiatives that I spoke about plus ongoing inflation-related increases. It does not change the trend of DTF's budget declining over time as we become more efficient at producing our outputs.

Breaking up that budget into our outputs, you can see there the eight output classifications which this year we have reduced to seven. The biggest move there is an increase of $14 million of strategic policy advice. That is our core business and we are increasingly reprioritising into that area. It also reflects some movements of outputs from some of those other output groups. That is the major change. I will leave it at that. Some of the questions about this slide may be more appropriately answered by the Minister for Finance or the Minister for WorkCover, but we will see how we go. That completes my discussion:

The CHAIR — Chapter 2 of budget paper 2, page 20, outlines the Victorian economic projections. Treasurer, could you explain how the Victorian Treasury economic forecast of 3.25 per cent compares with private sector forecasts and the recent commonwealth budget?

Mr BRUMBY — I can. The forecast numbers going forward, if you think back to that slide I put on before, 3.25 per cent for 2004–05 and 3.5 per cent in the out years, these are broadly consistent with private sector forecasts. You may have seen some comments recently in the media from some of the analysts in relation to that. The growth rate for the Victorian economy, looking over the last couple of years, last year was greater than that of New South Wales and South Australia combined. We have been the state which was most affected by the drought, and that drought is still in part working its way through the system. Taking all of those things into account — the fact that the dollar is a bit higher, interest rates, the world economy, a little bit of the drought still running through — 3.25 per cent is what we believe will be the growth for Victoria and, as I said, 3.5 per cent in the out years. In terms of employment growth, we are forecasting an unemployment rate of 5.5 per cent in both 2003–04 and 2004–05, the commonwealth is forecasting a national unemployment rate of 5.75 per cent for 2003–04 and 2004–05, so we are a little below the commonwealth on its estimates of growth but we are above the commonwealth on our estimates essentially of unemployment — we are below the commonwealth on our estimates of the employment rate.

Mr CLARK — My question relates to land tax. What indexation factor for 2005 did you assume was going to apply when you did the modelling for the land tax measures that you announced in the economic statement? What impact did you expect those changes would have on small-to-medium-sized businesses, and is it correct that with a 15 per cent increase in land value for land tax purposes, even after the package of changes, the holder of an $800 000 property would face a 55 per cent increase in their land tax for next year?

Mr BRUMBY — I am advised that the forecast is based on estimates of property price increases going forward over the valuation period. The estimate of that was around 15 per cent, but that figure is a DTF estimate and the true indexation factor for that period will not be known until the Valuer-General releases that information towards the end of 2004. So we are not able to give you that number until the Valuer-General makes that determination. What I can say about the land tax categorically is that obviously if you reduce the top rate from 5 per cent to 4 per cent it has a revenue impact. It is impossible to argue otherwise. If you then continue to reduce the top rate by a quarter of a per cent per annum over the next three years to reduce the rate to 3 per cent as is our target, these things have a significant cost to revenue; so the average cost to revenue of the land tax changes, which we announced, is around $200 million per annum. This is a very significant tax cut. One of my advisers might find me the page in the budget papers which has the tax table on those tax changes..

Mr CLARK — While you are waiting for that, Treasurer, you might also consider the aspect of the modelling for small-to-medium-sized businesses that you took into account when making your decision.

Mr BRUMBY — Land tax reform: the cost to budget in 2004–05, $124 million; in 2005–06, $197 million; in 2006–07, $222 million; and in 2007–08, $244 million. I am not sure why you would want to quibble with that.

Mr CLARK — I want to know why small businesses are facing a 55 per cent increase in land tax even after your package, and I want to know what modelling and information you were given about the impact on small-to-medium sized businesses before you made a decision.

Mr BRUMBY — I am not sure of the purpose of your question. The land tax system we inherited was your system. What we have done in government is continually improve it. When we were elected the tax-free threshold was $85 000; we have increased that to $125 000, then to $150 000, and to $175 000 in this latest package, taking tens of thousands of small investors and small businesses out of the system. We should be clear about that, Robert. Your threshold was $85 000.

Mr FORWOOD — There has been a slight increase in house prices.

Mr BRUMBY — Ours is $175 000, so we have more than doubled the tax-free threshold. We also have a land tax system where close to 97 per cent of all people who pay land tax in Victoria pay less than in New South Wales, but we have had one significant problem with it, which is its steep progressivity and the fact that it had a top rate of 5 per cent. If I might say, you would have acknowledged — in fact I know you have acknowledged it because I have seen some of your comments in *Hansard* when you were part of the former government — that the steep progressivity of the system was a problem. So we have sought to flatten that. What benefits does that bring? Firstly, it reduces the overall tax burden, but secondly, this has so many manifestations, whether it is major capital investment in our city, whether it is land development on the outer suburbs of Melbourne. Each time someone develops a block of land to sell in Craigieburn, the person owning that land is paying a holding tax of 5 per cent at this point in time. That is about $5000 a block for a first home buyer. As we reduce that down by 3 per cent in a competitive market that will reduce the price of land by about $2000 a block.

For superannuation funds, if you are an ordinary worker in the retail or manufacturing industries, you contribute superannuation which goes into the system, plus the 9 per cent contribution. Those funds invest in property and in Victoria they have been paying a 5 per cent rate of tax. So we are bringing that down. My view is that it is unambiguously positive in terms of investment, jobs and a fairer tax system, and the cuts themselves, as I have said, are close enough to $1 billion over five years. It does not matter how you cut it or it does not matter how you measure it — they are substantial reductions.

Finally, in terms of small business, you might wish to compare the sort of tax that a small business operator in Victoria would pay with land worth $500 000 compared with what they would pay in New South Wales. In Victoria the amount of tax they would pay on $500 000 would literally be a matter of hundreds of dollars. In New South Wales they are now paying thousands of dollars. We care about small business. We care about the progressivity of the system. We have taken $1 billion out of it. It is a better system; it is flatter. We have taken some of the extreme progressivity out of it, and so far as small business, self-funded retirees and investors go, it is the most generous at the lowest scales of anywhere in Australia.

Ms ROMANES — Chapter 1 of budget paper 2 outlines the government's financial policy objectives and strategy, and in particular objective 4, the government's commitment to a fair and efficient tax system. Could you outline recent taxation reforms in the budget and how these reforms position Victoria compared with other states?

Mr BRUMBY — I was just referring to the land tax cuts and the table on that is at page 37. I just want to make the point in answering that question in terms of building a fairer and a more efficient tax system, I have explained why we made changes to land tax. In addition in this budget, as you know, from 1 July we are also abolishing duty on mortgages. Why is that about building a fairer and more efficient system? It builds a fairer tax system because at the moment if you are a home buyer and you take out a loan of, say, $250 000 to buy a home, if you are a first home buyer you are paying about $1000 in mortgage duty. From 1 July that is removed. Why is it more efficient? If you are a business, typically a small business — again to go back to Robert Clark's question — and you are expanding, typically you put your house and your business in and take a second mortgage on that. Again the duty is removed on that primary mortgage, so that is a saving to business.

From 1 July 2005, as part of the intergovernmental agreement, we are also abolishing debits tax, which is again fairer because many people like pensioners use cheque accounts particularly and they will not pay that tax in the future, but also many businesses are paying debits tax. In all these ways we are building a fairer and more efficient tax system. If you go to the aggregate value of those tax cuts, if you look down the forward estimates period you will see by 2006–07 the value of the land tax reform tax cut is $222 million per annum; the mortgage duty is $200 million and the debits tax is $283 million per annum; so that is in total something like $700 million per annum of tax reduction. As I have said, it is building a fairer Victoria but also a more efficient economy. One thing which we want to do in a more difficult global environment is to make Victoria an attractive place for investment, to generate the jobs families want, and those reductions in tax will give us the competitive economy which we need to generate investment and jobs.

Mr CLARK — I return to the question of tax slugs on small business. Is it correct that one of the payroll tax changes that you announced in the budget will have the consequence that small to medium-sized businesses which are under the payroll tax threshold of $550 000 and who source workers through employment agencies, or labour hire firms as they are more commonly known, will in effect have to meet the cost of payroll tax on the wages of those workers, whereas under the current regime they do not have to do that?

Mr BRUMBY — I think you are referring to a press release that your federal counterpart may have issued the other day, is that right — Joe Hockey?

Mr CLARK — I am referring to your budget papers.

Mr BRUMBY — It sounds like you are referring to Joe Hockey's press release. I do not think that is particularly accurate. It is true that we will be making changes in that area, but the changes we will be making in Victoria are simply to bring our tax arrangements into line with those in other states. Far from penalising small business, what those arrangements will do is bring them into line with other states.

Mr CLARK — But they will still hit small business with the payroll tax cost that they do not bear at present and that New South Wales does not — —

Mr BRUMBY — That is not necessarily correct at the moment either. The arrangements will make the principal company responsible for the payment, I believe.

Mr LITTLE — If I can answer, it is not clear because there could be a range of ways in which the current payroll tax system impacts upon that small business, and it varies from case to case.

Mr CLARK — You are expecting to raise an extra $20 million from this measure.

Mr BRUMBY — But we raise $2.7 billion in payroll tax. The numbers jump around each year. But understand that the industry has been expecting this for some time. This is not a new matter. This is a matter which the State Revenue Office has been discussing with the industry for some time. All businesses that hire employees through national employment agencies will benefit because of the standardisation of the provisions with other states. We have had a set of provisions here which are out of line.

Mr CLARK — They are not standard with New South Wales even under what you are doing now.

Mr BRUMBY — I am not sure that is right. Smaller employment agencies with a payroll below the threshold of $550 000 will be able to avoid all payroll tax administration. They will not have to pay payroll tax or register, and there will be exemptions for several types of employment agencies and end users, including not-for-profit group training companies and employment agents where they on-hire workers to an organisation which is exempt from payroll tax, such as a public hospital or charity. There is nothing that I am aware of that is new in this. It is in line with what is happening interstate, and it is a matter which the State Revenue Office advises me it has been discussing with industry for some considerable time.

Mr MERLINO — Chapter 1 of budget paper 2 outlines the government's financial policy objectives and strategy. What are the financial settings that have been put in place to ensure prudent financial management and to maintain a AAA credit rating?

Mr BRUMBY — We have obviously put a number of strategies in place to do that. Every year that we have been in government we have produced a budget surplus. Every year that surplus has exceeded our minimum target of $100 million. We have delivered a surplus again for this year, as you have seen, where we have budgeted for strong surpluses going forward. In terms of the AAA credit rating, when I released the budget a couple of weeks ago Standard and Poor's issued the releases it normally releases at the time of the budget reinforcing the AAA rating.

Let me say about the AAA rating that only 10 states in the US have a AAA credit rating — that is, out of 50-or-so states in the US only 10 of them have a AAA credit rating. Outside the US only 16 per cent of economies around the world enjoy AAA credit ratings. So ours is a very strong fiscal position, and that benefits us in terms of making Australia, and Victoria in particular, a good place to invest. At the functions that I regularly attend with business, it has been important to them to know that there is sound financial management. That helps them with their investment decisions.

In other areas there are things like superannuation. When we were elected, for the first six months of the government I was the finance minister and Assistant Treasurer, so I was responsible for superannuation. One of the first decisions that we made was to bring forward the repayment of all of the unfunded superannuation liabilities from the target of 2040, which had been the policy of the former Kennett-Stockdale government, to 2035. If you look at various graphs in the budget papers you will see that they show that, so we are well and truly on track to achieve that. That is a big plus for the state. As you know, we are fully funded as we go now, unlike the commonwealth which only pays super at the time of retirement. So we are on schedule there. In fact page 61 of budget paper 4 shows that on present indications — if we brought it forward from 2040, the target was 2035 — and on present payment schedules those unfunded superannuation liabilities will be expunged by 2033. This is a very positive achievement for the state.

Mr CLARK — Can I take you to the issue of estimates and expected outcomes for fines and fees, in particular for police fines and other fines? You will know that for the current financial year, 2003-04, you were budgeting to collect $427.5 million in fines alone.

Mr BRUMBY — What page are you on?

Mr CLARK — I am referring to a spreadsheet, but it will be in the 2003-04 budget papers in the revenue estimates at the back of budget paper 3. It was $427.5 million budgeted for 2003-04. You are now expecting to get $233.5 million on your revised estimate for this year, and we are expecting to get $350 million in revenue for next year, 2004-05. Some of the reasons for the fall for this year against budget are fairly well known, but can you inform the committee what the factors are underlying the assumed increase in the police fines level between the 2003-04 outcome and 2004-05 budget figures?

Mr BRUMBY — Thank you for that. I will just see if I have the numbers here. The estimated numbers for 2004-05 you will find are not too different to 2002-03. I am after the 2002-03 number. We will just find that because I think it is instructive to look at that. What we have had is a system where, yes, there has been some growth in fines. We make no apology for that; it has been a key part of our road safety strategy. You saw some growth in that revenue through 2002-03. In 2003-04, for a variety of reasons of which we are all aware, including changed driver behaviour but also the problems with the Western Ring Road cameras, the revenue for this financial year has been significantly lower, and that is what you are referring to. When you then look at the estimate for 2004-05, in aggregate it is not too much different to what the total was in 2002-03. I am sure that between the number of advisers I have here today eventually, before 12.30 p.m., we will find that number for you.

Mr CLARK — Currently your figures are on page 133 of budget paper 4.

Mr BRUMBY — Yes, I have got those. I am just trying to find 2002-03 because I was asked specifically for these numbers.

Mr CLARK — While we are waiting, Treasurer, if the amount that has been involved with the fixed camera losses has been quantified — it is in the order of $13 million of revenue sacrificed, and I think a $6 million compensation fund. Assuming that the rest of the downturn in this year is due to modified driver behaviour the estimates appear to imply either that driver behaviour is expected to deteriorate again, or alternatively that there are going to be increased revenue-raising efforts that will contribute to the increase of $117-odd million between this year's revised and next year's budgeted figure?

Mr BRUMBY — In terms of this year in the ex gratia payments, which the Premier announced on Friday, there is $13.7 million ex gratia for refunds, $6 million for compensation, some of the remediation of the Western Ring Road, some outstanding payments from infringements — about $5 million, I think — and there is some cost for administration of the scheme. Those are all of those factors. Going forward, I was asked these questions on budget day. There is no change to the strategy which was outlined by the police minister and the transport minister two years ago. So there is a continuing rollout of cameras in this area, which I think were announced two years ago. There is no change to that strategy; there is nothing additional to it. And that is what you see reflected in the revenue numbers.

I will make one point if I can. This is a slide in the budget summary papers. The heading is 'Victorian road toll per 100 000 population: deaths and major-serious injuries per 100 000 population'. I want to highlight the impact that the range of government strategies are having on the road toll. Obviously these are matters which I am sure you will raise with the relevant ministers at the right time, but this slide shows a very substantial reduction in the rates of death and serious injuries per 100 000 population. There is a variety of factors contributing to that: speed cameras; the Arrive Alive program; the black spot program in the first four years of our government; and school crossing zones. This graph shows a huge reduction. Last year was the lowest road toll ever on record. Going forward, so far this year — that is, for the first five months of calendar year 2004 — we are tracking better than we did in 2004. We are tracking about 14 lives better. All of these deaths and major injuries are all cases of human tragedy, and, of course, economic cost. That is a massive reduction. That is a good news story for Victorians, and a good news story for things like the TAC.

Robert, could I go back to that question you raised before? I have the date, and I think it does confirm what I was saying. In 2002-03 our forecast on police fees and fines was $326 million — that was the forecast.

Mr CLARK — The revised forecast?

Mr BRUMBY — Yes. For 2004–05, two years later, we are predicting $350 million. It is a little bit more; it is $24 million more over two years off a base of $325 million, so it is probably a small increase in real terms. I have not got the exact increase there, but it is whatever that is — $25 million on $320 million over two years. It is less than 10 per cent over two years, about 9 per cent over two years, which is less than the nominal rate of GDP growth. This just goes to the point — what you have had, really, is 2003–04, for a variety of reasons that we have mentioned, was lower than anticipated. We revised down, and we are all aware of those issues. But for 2004–05 what we are predicting is basically the same sort of arrangements that occurred in 2002–03. As I said, it is a bit less than nominal GDP growth. Nominal GDP growth would be around 11 per cent; it is over two years, so it is a bit less than that, which I would hope reflects changes in driver behaviour. So we are seeing some changes in behaviour, and probably some significant changes because there is a continued rollout of cameras.

Ms GREEN — Treasurer, the 2004–05 state budget includes a number of projects which rely on commonwealth funding. Could you detail for the committee the implications of the recent commonwealth budget for the Victorian budget, particularly in relation to the range of projects that depend on commonwealth funding support?

Mr BRUMBY — The recent commonwealth budget did obviously disappoint us in a range of areas. We are particularly disappointed that no detail has been provided yet in relation to road funding and issues like the Deer Park bypass, the Calder Highway, the Geelong western bypass and the missing $21 million for the Pakenham bypass. Obviously we would want to see funding for all of these projects in Victoria, and I understand the Auslink white paper will be released in June. But I will just make this point about those projects. Victoria, as you know, is about 25 per cent of the nation's GDP. We pay a little over that in national fuel taxes. We have been getting back consistently over the last decade about 15 per cent or 16 per cent of national road funding. Really, this is an outrage for Victorians. There are as many people killed on the Calder Highway as there are on the Pacific Highway in New South Wales, yet still it does not attract federal funding. If we got just close to that 25 per cent — we would settle on 23 per cent or 24 per cent for the next four years — we would be able to undertake all of those projects I mentioned. So the Calder Highway, where we are after about $170 million from the commonwealth; the Geelong western bypass, which is $190 million; the Deer Park bypass, which is a national highway, about $250 million; the missing $21 million on Pakenham — you could do all of those and have a bit of change left over in the next four years. That is the extent to which this highway robbery is occurring. So we were disappointed there. There was nothing for the Wimmera–Mallee pipeline. Again we have $77 million in the forward estimates ready to go, ready to be spent, ready to save the Victorian and Australian water systems 83 000 megalitres of water per annum.

Mr FORWOOD — Why do you not start spending it?

Mr BRUMBY — Because we are waiting for commonwealth funding.

Mr CLARK — Waiting for the result of your own business case.

Mr FORWOOD — Why do you not spend it? You have the money in your forward estimates — spend it.

Mr BRUMBY — It would be a short pipeline, Bill.

Mr FORWOOD — It would be of great benefit, you know that. No matter where you start, it would be of benefit. You could spend that money and get a real effect now.

Mr BRUMBY — Come on, Bill!

The CHAIR — Back to the commonwealth budget, thank you.

Mr BRUMBY — If you want to water your backyard and you need 50 metres of hose, but you chop it to a third of its length, you cannot get there.

Mr FORWOOD — You know very well that — —

The CHAIR — This is Ms Green's question.

Mr BRUMBY — So there is the Wimmera–Mallee pipeline. But on other things, we would have liked to see a better share for Victoria in terms of higher education funding. We have got 10 000 more students now who are going to universities in Victoria who have qualified, but there have been no additional places since 1996. So there are all of these areas. I think you know that with AHCA, the health agreement, we are now paying 59 per cent compared with the commonwealth's 41 per cent.

The final point I want to make about the budget is on one area which I think should be of interest to the committee: that is that under the federal budget papers the federal budget is silent on national competition policy payments beyond 2005–06. It is just silent on it. There is no provision in the estimates for it. These payments are worth $200 million a year to Victoria — I think they are worth about $1 billion across Australia. We, as you know, have a very strong position on competition policy; we have been the national leader in it. The whole basis of national competition policy was that it would drive productive reforms, higher levels of production, and hence revenue in the Australian economy, and the whole purpose of these grants was to ensure that the states share in the additional 'cake', if you like, that is generated across Australia.

Let me make this point: these benefits flow on indefinitely; they do not just last one year and then stop. The benefits from competition reform and productivity growth flow on indefinitely, so the state of Victoria and the other states have a continuing, indefinite right to that flow of payments. That was the whole basis of national competition policy. But the federal budget is silent on it. There is nothing in the forward estimates, and needless to say, if this program were not continued it would have a very significant impact on all of the states. The federal Treasurer, Peter Costello, has referred this issue to the Productivity Commission for review. We will be making a submission to that, and we will be making it very clear that we believe this program should continue in the future, there is still more work to be done, and we believe the states must continue to enjoy their share of the growth benefits, the growth dividend, that flows from competition policy.

Mr CLARK — I want to follow up on the question of the Wimmera–Mallee pipeline and your remark that the state government's money was in the budget and ready to go. I want to refer you to page 94 of budget paper 2, 'Strategy and outlook', the centre section relating to the Wimmera–Mallee pipeline, and in particular to the statement that the state government funding is subject to 'confirmation of feasibility' and that the government is currently 'reviewing the interim business case' that has shown the revised estimated cost having risen from $301 million to $501 million. Does your answer mean that the business case has now been reviewed and that feasibility has been confirmed and that therefore the state has overcome those two obstacles?

Mr BRUMBY — The position is this: $77 million is in the forward estimates — I do not think you are questioning that — and it is available to be spent. The original cost of this project, as the Treasury papers note, was around $300 million for a saving of 80 000 to 90 000 megalitres of water. If you calculate the savings of water versus the cost of the project, at $300 million the cost per megalitre is still in the upper range of what governments and farmers would want to invest to save a megalitre of water. You can buy a megalitre of water in the market for under $1500 — for somewhere between $1000 and $1500 — so, if you are going to invest in water saving technology, you need to be somewhere in the ballpark. There are other benefits, of course, that come from investment in infrastructure — there is less waste, there are environmental benefits and all of those things — but you do not want to be too far outside of the range.

When you move up to a project cost of $500 million-plus to save 80 000 to 90 000 megalitres of water, your cost per megalitre is moving up to in excess of $5000 per megalitre. Frankly, at that sort of cost per megalitre saved, you have got to ask whether this project should proceed in that form or should it be re-examined and re-scoped to get it back closer to its original cost estimate. That is what the business case and the business assessment are looking at. It is not for me — I am not the minister responsible; John Thwaites is — and they will be examining that business case, but I think you would agree with me that this is a very good project for the state. There is huge water loss. You have heard me say this before: if you build a swimming pool from here to Darwin and run it halfway back and fill it up, that is 90 000 megalitres of water. It is a lot of water. If you were to fill up the Melbourne Cricket Ground twice a week — and of course you could not at the moment because it would all run out — but if you filled it up, that is the amount of water involved. It is a lot of water. But at $500 million–plus the cost per megalitre is excessive, so the business case is looking at how it is scoped and at newer pipeline technologies to try to get the cost down so that valuable project can proceed.

Mr CLARK — So it is fair to say that the problems confronting these issues at a state level are quite independent of the question of commonwealth government funding, and there is now a doubt about whether it is now feasible for it to proceed?

Mr BRUMBY — No, I would not say that. What I have said is that there is an examination of the cost base, which the project proponents have said recently is in excess of $500 million. We have said that needs to be re-examined, but we remain fully committed to the project. The point I made before is that the project, in reality, cannot proceed without some federal funding, and the reason for that is that you either have a short pipeline or the burden on property users is excessive. That is the equation. Either the state puts in a lot more or the burden on property users is excessive or the pipeline is much shorter than it needs to be. All of those things have been considered, but the key is whether the commonwealth contributes, and as you know a number of federal members of Parliament are very concerned, including the federal member for Mallee, John Forrest, who has staked his job on it. That is how strongly he feels about the merit of this project.

Mr DONNELLAN — Chapter 2 of budget paper 3 provides a report card on the implementation of the government's election commitments. Can you outline the extent to which the government has been able to deliver on the election commitments, both in terms of infrastructure and recurrent initiatives?

Mr BRUMBY — When we were elected in 1999 we made a number of election commitments which we called LFS — Labor's financial statement. Then in the run-up to the 2000 election we followed the same pattern and made specifically costed election commitments. They were for recurrent and capital initiatives — specific items such as additional teachers, home and community care — and there were 138 of them. What the budget papers show is that in last year's budget and now in this year's budget 100 per cent of those have been delivered. That is what the budget paper is all about. It is the report card on implementing that measure. Page 50 is the summary, which shows the number of initiatives and how they are funded. On the assets side we made a number of substantial asset commitments, and we said they would be progressively implemented over the four-year term. I am pleased to advise the Public Accounts and Estimates Committee today that following this budget — in other words, halfway through our term; two budgets in — 80 per cent of those capital commitments have been honoured. That means we are well ahead of schedule. You would expect it would be 50 per cent after two budgets, but we are well ahead of that, which means with absolute assurance that all of those projects to which we are committed will be approved and under construction by the time of the next election, which is what we promised.

Mr CLARK — My question relates to superannuation and goes back to the issues that you touched on earlier. I refer initially to the chart you also referred to on page 61 of budget paper 2. The chart shows the projected pay–off of unfunded superannuation liabilities by 2033 or thereabouts. You will see, Treasurer, that there is a bit of a kink in the chart over the early years — an initial dip from 2003–04, which would be largely due to the actuarial re–evaluation and the recovery in the stock market; you then see that the figure rises quite sharply over the next few years before the virtuous path of actually paying it off commences.

Mr BRUMBY — Sorry, I missed that last bit.

Mr CLARK — The virtuous bit of actually paying off the unfunded superannuation liabilities does not start until a few years down the track, and in the short term there is a sharp jump — —

Mr BRUMBY — No, that is not right. Do we have that graph — —

Mr CLARK — I will finish my question — —

Mr BRUMBY — No. Can we get a copy of the graph? We will get a photocopy brought over. It is a graph to go to your question, Robert, which shows that in terms of the net financial liabilities of the state, for the budget and next year and the year after and the year after that those liabilities are in all cases lower than what we anticipated in the 2003–04 budget, so in all cases we are ahead of schedule. We are better than we thought we would be at this stage last year in the 2003–04 budget.

The reason for the kink in the graph reflects two factors; firstly, that because of the stronger than anticipated budget position we have been able to prepay some superannuation, and I am sure you have picked that out of the budget documents. So we have actually, ahead of schedule, produced a dip in that curve because we have prepaid; and when you see the rise go back, it goes back to a point which is lower than we had anticipated it would be in this budget last year. So the kink reflects that factor, plus the secretary would advise me that it also reflects some of the movement in equity markets, moving from a weaker equity market to a stronger equity market, and then variations on that theme. But the key point is that if you look at the top of the curve, it was a smooth curve but because we paid out earlier and because of the movements in equity markets it shows a sharp downward reduction in real liabilities; but the top of the curve is still lower than where it was at this time last year. I am happy to show you, when we get this bar graph, that the net financial liability in this budget is about two $2 billion lower, so it is a very substantial reduction. It is paid out early, it is a good news story, but you get a kink because it has been such a significant reduction.

Mr CLARK — Thank you for that information, Treasurer, I will now finish my question. I accept that in relation to 2003–04 you have in fact paid down superannuation by about $1.2 billion in terms of unfunded superannuation liabilities. Over the whole of your term, on my figures expenses have exceeded cash payments to the tune of $777 million due to a big blow-out in 2001–02, but my question related primarily to what you provided for in the budget years 2004–05 and 2005–06 in terms of further contributions to paying off unfunded superannuation liability. I ask you to compare budget paper 4, page 8, with page 10. Page 8 shows the superannuation expense, page 10 shows the cash payment towards superannuation costs including unfunded superannuation liabilities, and you will see that there is a shortfall between expense and cash payment for 2004–05 of $667 million, and 2005–06 of $820 million. I put it to you that part of your budget strategy is to allow for this undercontribution towards unfunded superannuation liability in order to free up some of the cash flow that you need to meet some of the capital works commitments. Do you agree with that proposition?

Mr BRUMBY — Would you say there is something wrong with that?

Mr CLARK — No, I am asking you whether that is a correct analysis of how you are funding the capital works program in your budget.

Mr BRUMBY — I do not think it is correct to make that supposition. Let me make just a couple of points about the observations. You referred to a 'blow-out' in 2001–02. I am surprised you would use that expression because it is just not accurate and you would know that. There is no blow-out. What the superannuation expense reflects is the changes in equity markets, which you know well. When equity markets grow at less than 7 per cent, we have to expense the unfunded liability. In 2001–02, if my memory is correct, the unfunded liability because of changes in equity markets was around $1 billion. We had to bring that to book. You do not need cash to pay it. You know all this; I am just picking — —

Mr CLARK — The point I am making is that there are swings and roundabouts. You are 1.2 in front this year, you were 1.5 behind then and you are a net 777 behind.

Mr BRUMBY — I will answer the question, but I was just correcting you because you were disingenuous in using the word 'blow-out' because you know that is not the case. So you had shifts in equity markets of $1 billion. That is why expenses exceeded cash payments. In terms of your questions about 2004–05 and 2005–06, as I explained earlier, the strong budget position of the last couple of years has enabled us to essentially prepay some of the superannuation expense in future years. We make that decision at the end of the year. You would recall this. You come to the end of the financial year and until you get to 30 June you do not know what the final position will be. You get to 30 June, and let us say the economy has grown stronger than you thought and the cash surplus is a little larger than you thought it would be. The government then must make a decision about how it applies that available cash. We can use it to pay down debt or we can use it to pay down unfunded superannuation liabilities.

There are also some — although were they are no longer significant — minor tax advantages in prepaying some of that superannuation. Again, I think probably during the period that you were parliamentary secretary a prepayment was made which again attracted some tax advantages. There are still some tax advantages available to the state for prepayment of those liabilities. Last financial year, as we had more cash than we thought we would have at the end of the year, we used that to prepay some of those superannuation liabilities. In terms of this year we will also, subject to the cash position, prepay some of that liability going forward because the cash position is a little stronger than we thought it would be.

The consequence of that is that again, from the state's point of view, it is a good proposition. It is a very sensible use of cash surplus. It is paying down a super liability earlier than is required. It is picking up for the state a small, but nevertheless measurable, tax benefit, and it improves the financial position going forward as well. If you look at budget paper 2, chapter 4 page 60, the second last paragraph states:

> By 30 June ... the government will be around $1.8 billion ahead of the original payment schedule.

That goes to what I thought was your earlier question when I interrupted about the kink in the graph. That is because we are $1.8 billion ahead. So that is run down. We are actually ahead of schedule. That in turn answers some of your question about 2004–05 and 2005–06. The total cash contribution in super over the forward estimates period has not changed going forward but what we have done is changed the timing of it to better utilise the cash surpluses which we have experienced — which we have enjoyed — and we have used that to pay down debt. That is a 100 per cent good news story for the state. What it means is that we are ahead of the super payments. As I said, 2040 when we were elected; 2035; and now 2033. We are ahead of those. We are producing surpluses on AAS31 and GFS — government finance statistics — and we are also producing GFS cash surpluses every year going forward and funding a capital program in excess of $2 billion a year. So it does not matter how you cut and dice it, it is a good news story.

The CHAIR — In chapter 5 of budget paper 2, commonwealth-state financial relations, page 77 shows that Victoria's subsidy to other states and territories is now running at $1.7 billion. We have pushed in Victoria for a review of the current arrangements. Could you tell us what has been agreed in relation to that?

Mr BRUMBY — Thank you for that. It is fair to say that this is an issue which has been taken up by various governments in Victoria of different political persuasions because really in the last 20 or 30 years we have been getting a very poor deal. What we did manage to achieve this year at the treasurers conference was an agreement from the states which, I am pleased to say, I moved on behalf of Victoria and was agreed to by a majority of states and to which, therefore, the federal Treasurer must accede, that there will be — —

Mr FORWOOD — Which states did not agree?

Mr BRUMBY — Queensland, South Australia — for reasons best known to themselves — and the ACT, which has been a winner out of this as well. We got that review. As I said at the time, it is not as far reaching as we would have wanted, but we do have a review. The review will be conducted by heads of treasury of all Australian jurisdictions. It will include the examination of whether the present approach is appropriate and necessary, the size and trend of current redistributions, possible simplification and the reliability of the data used in the current system. Chair and members, I think you know the numbers here: $1.7 billion. That is the difference now between what Victoria pays in GST and what we get back. That is something like $350 for each Victorian — it is a huge amount — each year. It is just a huge amount of money.

Let me make this point, too, just more generally about these arrangements: in terms of untied funding, for 2004-05 Victoria will receive just 21 per cent — repeat, 21 per cent — of commonwealth untied funding. That essentially goes to the GST agreements. It means that for every $1 we pay we get back just 80 cents now — pay $1, get 80 cents back. In terms of special purpose payments — again these are matters which I hope provide some opportunities for this committee to focus on in the months and years ahead — we receive only 22 per cent for the current year. It does not matter how you look at this, we are carrying a lot of Australia and Victorian taxpayers pay for that. We have always said that we are very happy to support the needier states — Tasmania, the Northern Territory and South Australia. We think we have an obligation to do that to. But we draw the line at propping up Western Australia, Queensland and the ACT. As I have said before in relation to the ACT, the income per head there is 40 per cent higher than the national average. If you can just imagine a Victorian government putting a special tax on all Victorians to pay an annual Christmas bonus to the people of Brighton, that is what happens under this system with the ACT. It is a bizarre, outmoded, clapped-out system, and so we want to change it. In the last review, Queensland and Western Australia won — they got more money — every other state lost. So we are not happy with it. We are getting a review, and we hope we will get some progress from that.

Mr CLARK — I refer to the budget estimates for employee entitlement costs. On my calculations the employee entitlements for 2004–05 are expected to be about 9.2 per cent higher than what was budgeted for in 2003–04 — in other words, a fairly considerable increase, despite the government's wages policy. When the Premier was here yesterday he told the committee about the move to the new system and the inclusion of the provision for future wages growth in the departmental estimates. Trying to paraphrase him fairly, he said words to the effect that he was confident this would mean that wages estimates in this year's budget papers would not be exceeded. Can you comment, first of all, on the reasons for the continued apparent significant growth in employee entitlements; and secondly, do you share the Premier's confidence that the budget provision for employee entitlements for 2004–05 will not be exceeded?

Mr BRUMBY — I will make a general point about total operating expenses, because obviously in any budget it is possible to pick out some items that will have increases above the average going forward and some that will be below the average. The total increase in operating expenses in this budget is 4.2 per cent and nominal GDP will be around 5.5 per cent, so the rate of growth in expenses is significantly below the rate of growth in the economy.

Mr CLARK — But your increase this year is 7.9 per cent compared with what you budgeted for last year in total expenses.

Mr BRUMBY — I will come back to that in a moment, if I can. Employee benefits for 2004–05 are budgeted to increase by $643 million, which is a 6.25 per cent rise from the revised 2003–04 estimate, and that rise largely reflects the government's wages policy, obviously, plus additional expenditure as a result of higher staffing levels in health and education. We make no apologies for this. As I have said, nominal GDP will be around 5.5 per cent, so the total growth in employee entitlements will be a little above that, but that reflects wages policy, and it reflects the fact that we are putting more teachers in schools, more police on the streets and more nurses into hospitals. That is the job of a government, and if we are able to return the taxes that Victorians pay in the form of those service improvements, that is what Victorians want us to do. I would have thought there was abundant evidence of that, and that is what we are doing. And we are doing that all within the context of a budget that has a tax burden below the national average and a surplus running forward of around half a billion dollars a year.

The point is that if you can afford to put more teachers in schools and more nurses in hospitals and if you can get value-for-money outcomes from that, which we do in all of those areas, then that is what taxpayers want us to do, and that is precisely what we are doing. Over the remainder of the forward estimates period, employee benefits are budgeted to increase by a little over 3 per cent per year on average, and that is broadly consistent with the government's wages policy. There is a slide on total spend on GDP — total payments from operating activities. That is in the budget papers at page 202 of budget paper 4. This is looking at total payments from operating activities in real terms as a percentage of GDP. After we were elected, in the first couple of budgets there was an increase in spending, and since then as a share of GSP we are on a modest decline. In fact I will give you the percentage numbers on AAS31.

Mr FORWOOD — I will come back in 2007–08 and just see.

Mr BRUMBY — You can make that interjection.

Mr FORWOOD — Thank you.

Mr BRUMBY — But we have delivered five budgets, and you can see the curve.

Mr FORWOOD — You have delivered five budgets, and you have not once got your expenditure anywhere near your budget — not once!

Mr BRUMBY — That is a somewhat moot point.

Mr FORWOOD — They are your budget papers.

Mr BRUMBY — What this shows is that payments from operating activities as a share of GSP are trending down. So we are driving better value for money, we are paying down debt, we are producing budget surpluses, and we are treating more patients and doing a better job of educating children. They are the sorts of things that governments are expected to do.

Mr CLARK — Are you confident your government will come in within its entitlements estimates for 2004–05?

Mr BRUMBY — Yes.

Ms ROMANES — Treasurer, I refer to pages 56 to 58 in chapter 4 of budget paper 2, which outlines significant projects being delivered or under consideration as part of the Partnerships Victoria program. Could you outline the future directions of the Partnerships Victoria policy?

Mr BRUMBY — Thank you for the question. I know this has been a matter of interest to the Public Accounts and Estimates Committee. In June 2000 Victoria was the first state to formally release a partnerships policy. I was in Brisbane on Friday for the first national meeting of mainly treasurers but also ministers responsible for partnerships programs. Every state in Australia is now embarking on a public-private partnership program, and I think with one exception all the other states have used the material which has been generated out of Victoria, which is a credit to the department in terms of the quality of the material that has been produced.

We recently had a review of Partnerships Victoria which was conducted by Peter Fitzgerald. That was overwhelmingly a positive review and endorsement of the policy. He did make a number of recommendations going forward. Firstly, Peter recommended that we should apply PPPs to around 10 per cent of the total capital works spend. At the moment we are running a little below that. That is an important point to make. PPPs are a small but nevertheless important part of our capital works spend. Secondly, he recommended that generally the program should be applied to projects of $100 million or more, or those where there is maximum scope for innovation or the sort of one-off things that governments would not typically do. We have accepted those recommendations.

Peter Fitzgerald made further recommendations in relation to the discount rates; while we have noted his comments, we did not accept those recommendations. We have recently revised our discount rate policy — we did that late last year — so for projects with very low-risk transfer we use a rate of 5 per cent real, and for projects with a high-risk transfer it is around 7 or 8 per cent real, and that reflects the transfer of risk. A good example of the sort of transfer of risk is Spencer Street, which has been the subject of some commentary recently. The state has a contract with Civic Nexus, and the risk is borne by Civic Nexus. Leighton Contractors made some comments recently that it has had some difficulties in terms of the work it has been undertaking and that there may be a cost to it for that.

From the state's point of view, the state's position is fully protected, and that is really one of the great strengths of PPPs; you transfer the risk and we do not make payments until that project is delivered on time. So we have a number of projects; there have been 10 projects now which have reached contract execution — the County Court, Spencer Street, Docklands film and TV studios; Berwick community hospital, which is very nearly complete; waste water treatment upgrade projects at Echuca, Rochester, Wodonga and Altona; the mobile data network; correctional facilities; and metropolitan mobile radio. There are a further five projects in the market, including things like the showgrounds development, the Royal Women's Hospital and, of course, more recently the new Melbourne Convention Centre. So I think we have a good policy in place.

The underlying principle of it is value for money. It is not ideologically driven, it is not about how we report things in the books because any PPP we bring to book is about whether we achieve value for money. That is how we measure it. We now have a national PPP forum set up, and the purpose of that is to develop a national pipeline of projects because with a national pipeline and more consistency between the states you will get more competition, and more competition will mean better value for money and that is what we want to drive. So we had a very successful first meeting on Friday.

Mr CLARK — My question also relates to PPPs and in a sense follows on from the previous question. As you alluded to, one of the lynchpins of the PPP model is that you benchmark the private sector against the public sector equivalent through the public sector comparator and you have yourself in a position that if the private sector bid is inferior to the public sector comparator you leave open the capability of taking the project into the public sector on the basis of the public sector comparator. My question relates to the Scoresby freeway, where as I understand the government's position you cannot afford to do it through the public sector. In relation to the Scoresby, are you nonetheless having a public sector comparator prepared, and if bids do not meet up with the public sector comparator will you proceed to do the project as a public project in accordance with the Partnerships Victoria policy?

Mr BRUMBY — We made a decision more or less this time last year, or just before budget last year if I recall, that the Scoresby, or the Mitcham Frankston project, would be essentially a privately funded project. That decision has been made and, as you know, bids have been lodged and they are presently under consideration by government; so that project is proceeding as a private project. It falls within the umbrella of Partnerships Victoria because it is a piece of infrastructure which is privately financed, and Partnerships Victoria gives us the process and the policy approach to develop and implement it; but it is essentially a privately funded project and that is how it will proceed. It is very similar to CityLink, Robert, as you know. A decision will be made later this year on the successful tenderer. Work will start by the end of this calendar year. The total project capital costs are around $2 billion, as you are aware, and it is about 46 kilometres of freeways and tunnel. The economic benefits we expect to flow from it are very substantial.

Mr CLARK — Yes, but you are not doing a public sector comparison for it?

Mr BRUMBY — We have made a decision that it will be a privately funded road, and that decision is irrevocable.

Mr CLARK — So you have not done a public sector comparator?

Mr BRUMBY — One may have been undertaken, but obviously we took a decision to build it as a private road and that consideration therefore is no longer relevant.

Mr MERLINO — Treasurer, I refer you to page 37 of budget paper 3. Could you expand on the initiatives outlined in the recent budget which seek to ease the pressure on housing affordability?

Mr BRUMBY — Thank you for that. I think you are broadly aware of the initiatives that were announced in the budget, but let me simply make the point that no state has put in place the comprehensive range of measures to assist housing affordability as has Victoria. Other states have dabbled in this area, provided support for first home buyers, but no state has put in place the comprehensive range of measures which we put in place.

Firstly, they start with the $5000 grant; the first home bonus announced in the budget, which will assist something like 26 000 first home buyers over the next year. Secondly, there is the substantial reform of pensioner concessions, which now mean that a pensioner or an pensioner couple who have not claimed the benefit before will get a full stamp duty rebate of up to $250 000, phasing down to $350 000, at a cost to budget of $87 million over four years. This will more than double the number of pensioners who can get access to this program. Thirdly, there is the abolition of duty on mortgages. As I mentioned, a typical first home owner who borrows $250 000 will save just under $1000. A home buyer who borrows $500 000 will save closer to $2000. That is the trifecta, if you like, but there is also the fourth element of it, which is the changes to land tax. As I mentioned, if you talk to housing developers in the outer suburbs typically they acquire land and then they sell it to first home buyers. They have been paying land tax at a top marginal rate of 5 per cent per annum. In the future they will come down immediately to 4 per cent and over time to 3 per cent. As I said before, in a competitive market — and we are determined to ensure there will be a fully competitive market — those changes to land tax have the potential also to slice up to $2000 off the price of an average suburban block of land. No other state has tackled such a comprehensive range of measures — first home bonus, pensioner concessions, abolition of mortgage duty and land tax changes — and all of those will lead to substantial improvements in housing affordability.

Mr FORWOOD — Treasurer, I refer you to the modelling work done by Allan Consulting in relation to the Greenhouse Challenge for Energy, which shows that an emission trading system equivalent to $5 per tonne of CO_2 unambiguously lowers GDP and consumption for the duration of the policy shock period of 208 to 212, and that a further emissions intensity requirement equivalent to one in place in New South Wales would lead to a stranding of Victoria's coal assets and would increase wholesale electricity prices by well over 27 per cent. Has DTF done any modelling work on the effect of these policy options on the state budget, and if so can you advise the committee of what they say?

Mr BRUMBY — I am advised that no work has been done in terms of potential impact on the budget. I understand more generally this question may have been raised yesterday. I am advised that the project to which you refer is being managed jointly by the Department of Infrastructure and the Department of Sustainability and Environment. There has been an issues paper which was circulated in mid-2003 for public input, there is an interdepartmental committee (IDC) which has been established, Allan Consulting won a competitive tender to undertake this consultancy, including modelling of scenarios and policy options and consulting with industry. Allan Consulting is currently working towards completion of its final report, which will be available to government for its consideration, and the policy options and scenarios which are examined in the Allan Consulting report in no way imply government commitment to any particular scenario or policy option.

Mr FORWOOD — Thank you. Treasurer, are you on the IDC?

Mr BRUMBY — No, the IDC is departmental. I am not on it. The two departments, Department of Premier and Cabinet and Department of Treasury and Finance, are represented.

Ms GREEN — Chapter 1 of budget paper 3 refers to $2.9 million to establish and operate the Victorian Competition and Efficiency Commission. Could you briefly outline the role of this body and what the initial inquiries of the commission will focus on?

Mr BRUMBY — This was an initiative which the Premier and I announced in *Victoria — Leading the Way*. We are pretty excited about this. We are the first state to go down this route. The Victorian Competition and Efficiency Commission will be established from the new financial year, and its charter really is to oversee regulation reform. It subsumes the office of regulation reform, which is presently based in DIIRD. It will also take over or subsume the competitive neutrality unit, which is presently based in Treasury. Plus we will expand its function to give it real teeth to drive competition and efficiency reforms in the Victorian economy.

The reason for this, as committee members may be aware, is that last year I released a report called *Shaping Victoria's Future*, which was about the demographic and intergenerational changes occurring in Victoria and their budget impact. The reality is that our economy and demography are changing. There is a fiscal impact from that, and it is my view and Treasury's view that the best way for Victoria to tackle that is through continuous productivity improvement; Otherwise the only option for states, including ours, and the commonwealth is the old tax and spend, tax and spend. We think there is a better way, and that is through driving productivity improvement. To drive productivity improvement you need a more competitive, more efficient economy. We are establishing VCEC and, as I said, we are the first state to do that.

The first two inquiries I announced as part of the economic statement. The first one will be regulatory impediments to regional economic development, and the expected completion date of that is April 2005. This is really to look at: is there unnecessary regulation? Are there requirements which hold back investment in job growth? Is there overlap in federal, state and local governments? All those things will be examined. The second inquiry is the regulation of the housing construction sector. Again, this will be an interesting inquiry looking at: are there more efficient ways to deliver housing; are there unnecessary regulations there which are adding to the cost for home buyers or first home buyers? That report is due by June 2005. There will be independent commissioners. There will be a head commissioner called the chair and there will be two other part-time commissioners. There will be staff supporting it. These arrangements will be put in place shortly. I am particularly excited about this proposal and what it can mean for Victoria.

Mr CLARK — My question relates to the government's capital works program and budget. First of all, the table 'Purchase of fixed assets by department', which used to be table 1.2 of budget paper 3 under the old format, seems to have disappeared under the move to the new layout. Could you undertake to reinstate that in future budgets, or tell us where it is buried if we have missed it in this year's budget papers? More substantially, if you look at the expected outcome for 2003–04 in budget paper 4, page 222, looking at the line for 'Purchase of property, plant and equipment' you will see that the revised expected figure there is $1795.6 million compared with a budget of $2130 million. On my figuring $1795 million is about 0.9 per cent of GSP, which is approximately the same level of capital works expenditure as under the previous government in 1998–99. My question is: why has there been such a shortfall of about $330 million from the budgeted level of $2130 million in 2003–04?

Mr BRUMBY — There are a few questions there. We have a slide on capital works in the original presentation on the budget headed 'Record infrastructure investment'. The first issue, which is about what happened to the old table 1.2, if you look at budget paper 2, page 36, table 3.3, it is headed '2004–05 budget new asset funding by department'.

Mr CLARK — But that is not a full replacement of 1.2 because it only gives one year's worth and that gives new asset funding. The old 1.2 gave the expected capital expenditure by department for the budget and the forward estimates years, all capital works spending and not just new asset initiatives. They cover different things.

Mr BRUMBY — I am advised that further detail on all that is in budget paper 3, appendix A — that is individual initiatives. Can I take that on notice?

Mr CLARK — I am happy with for you to do that.

Mr BRUMBY — We have tried to provide more information, not less, with the new structure, and there is no reason why we could not provide that information to you, if I can take that on notice. We will do that. We thought this was a simpler format.

On the level of funding, the slide shows the levels going forward. My recollection, Robert, is that under the period of the Kennett government new fixed capital expenditure averaged 0.7 per cent of GSP. If I am wrong I am happy to be corrected, but that was the average. Ours has been averaging about 1.1 per cent of GSP. Again, if I am wrong on that I am happy to be corrected. The numbers on that slide are probably instructive: 1998–99 at about $1.1 million; 1999–2000 at about $1 billion; and thereafter you see the increase in spend. Obviously in 2000–01, 2001–02 and 2002–03, those amounts are actuals, so 2003–04 is a budgeted amount — we have not finished the financial year yet — and the other amounts going forward are budgeted. I will have some advice from Stein in about 5 seconds on the issue of any difference. I am advised that is largely a timing issue.

Mr HELGEBY — The cash flow forecasts in the 2003-04 budget have been revised relative to the actual progress of projects over the course of year.

Mr CLARK — That means some of the kick-up in 2004–05 figures is due to 2003–04 projects that have not been completed and have been rolled over into 2004–05.

Mr HELGEBY — Where the cash flow phasings have been different to that originally forecast in May 2003.

The CHAIR — I am interested in the Gateway project, which you outlined to the Public Accounts and Estimates Committee last year. Could you give the committee some indication of the achievements that have resulted from that Gateway project?

Mr BRUMBY — I can.

Mr FORWOOD — Only 5 minutes worth.

Mr BRUMBY — Gateway has been put in place. It is referred to in the budget papers and it has been very successful. I guess the origins of Gateway are this: particularly as we developed our Partnerships Victoria policy we put in place very rigorous arrangements for private sector investment in public infrastructure, and when we looked at those they were probably more rigorous than the arrangements which had been in place for traditional public sector capital works programs. As you know, the history of this state and the history of other state governments and the commonwealth is that capital programs typically in the past have gone over budget. The United Kingdom government did some work on this as well. It developed an index called the optimism bias, of which I think you are aware. In the UK it is about 45 per cent — that is, you announce a project is going to cost $100 million, and it ends up on average costing $145 million for a variety of reasons, such as changes of scope, inflation, all those sorts of things.

The whole purpose of the Gateway initiative is really about properly scrutinising all of the capital works programs, putting them through the different gates with an external panel to make sure that they really are driving value for money, that there is a strong business case and that they are being managed in the best way possible. All of the feedback which we have had — and Ian has just got some numbers for me here — show that to date we have had 25 reviews which have been completed on 19 projects across all departments. The feedback we have had from departments is that this has already resulted in short-term benefits to the quality of the projects being delivered across with, we believe, many more improvements to asset investment than we expected in future years. A further 27 reviews are currently scheduled to the end of September 2004. Essentially there are four or five processes. There is the Gateway review process itself, the project life-cycle guidance material, the multi-year strategy, which is where we look at 5 and 10 years going forward for possible rollout of capital works; and, of course, Gateway 2 addresses the issue of better reporting back as well.

We are pretty pleased with it. It is a bit like Partnerships Victoria too, where that material is being used by other states. We are finding that this initiative being developed in Victoria is now being looked at by other states, so that is positive. We have picked up this from some of the work they have done in the United Kingdom, so we are not claiming total originality or uniqueness here. We are applying it to our circumstances. We have developed that material, and my guess is that other states will pick it up and use it. It is a good news story, because it is about getting more timely delivery of projects, on time and on cost.

Mr FORWOOD — I wonder if you could explain to the committee the policy rationale behind the treatment, and the accounting of treatment, of the Alcoa decision for the $1.25 billion which the government has now taken on as an expense. How is this going to work in the years ahead? The SECV obviously still will need to pay the subsidy each year of around $80 million to $100 million for the life of the agreement with Alcoa through 2004 to 2016. What you have done, as I understand it, is put $1.25 billion in this year as an expense. Firstly, I am keen to hear the policy rationale, secondly, for you to explain how it works, and thirdly, you can talk to me about the accounting treatment.

Mr BRUMBY — The treatment of this is based on advice and the normal accounting standards under AAS31. We took the decision to terminate the smelter reduction amount, which was done from 1 July. As you know, in order to ensure the revenue position of the state going forward we extended land tax to electricity easements. The bookkeeping implications of that are that under accepted accounting practices we are required to essentially expense that liability, and to do that in the year in which the decision is made. That is the way in which we treated this matter under AAS31. So we created an account, an account that is technically known as an account payable, to the SECV of $1.25 billion, which resulted in a one-off expense in 2003-04. Needless to say, that accounting treatment has been signed off by the Auditor-General and it reflects a non-cash transaction.

That essentially writes down the 2003-04 budget position. I guess balancing that to this point in time this year we have had a strong equities market where you have seen growth above 7 per cent, and that is reflected in budget upside improvements. In addition an actuarial revaluation, which was completed in January or thereabouts, also added some hundreds of millions of dollars on budget upside. The net effect of those two totally unrelated transactions has been to virtually cancel themselves out in a bookkeeping sense. Going forward, which was the other part of your question, all it means is that now there is an extension of that land tax. Coincidentally raising that was not greatly dissimilar to the amount which was raised by the SRA, but because of the accounting treatment that land tax is actually added to budget forward estimates going forward, so it is included as revenue. The net effect has been an increase in expense under AAS31 for this financial year, and going forward indefinitely an amount of around $80 million a year in the forward estimates which improved both the AAS31 position and also the cash position of the budget.

Mr FORWOOD — In cash terms in the years ahead though, the government needs to pay the SECV $180 million a year, or thereabouts. Where do I find that in the budget papers?

Mr LITTLE — That will probably be in supplies and services, I guess. It will be a cash payment out of the budget sector to the non-budget sector, to the SECV. If I had to look at the dissection I think it would be in supplies and services.

Mr FORWOOD — Can you dig it out for us?

Mr BRUMBY — That amount has not changed. That amount remains unchanged. Going forward — —

Mr FORWOOD — We need to pay the amount under the agreement.

Mr BRUMBY — None of that has changed.

Mr CLARK — The amount which was going direct from VENCorp to the SECV — — Did not that amount go previously from VENCorp to the SECV rather than through the budget accounts?

Mr LITTLE - Yes.

Mr BRUMBY — Yes. But the total payment has not — —

You are asking questions about the payments to Alcoa. That payment does not change. That depends on world aluminium prices and all sorts of things.

Mr FORWOOD — I am interested in the system whereby that will happen, now that we have changed it.

Mr LITTLE — There will be a payment directly from the budget sector to the SECV when the SECV needs it. That will depend on aluminium prices and the state of its books. It could get revenues from other sources, but we would make an estimate and that puts SECV in a position to make the Alcoa payment.

Mr FORWOOD — Each year, and built into the forward estimates, some figure of around $80 million has been allocated. What I was told to do is track it down. You say, for instance, that it is services and supplies. If you can point it out for us that would be good.

Mr LITTLE — I will certainly tell you where it is. We have not disaggregated the amount. It does depend a little bit on what the SECV's financial position is each year. Some years, because of dividends it might get from Snowy Hydro, for instance, it may be in a position to make that payment itself. We will confirm where we have put our estimate. I am just saying that our estimate might vary from actuality from year to year.

The CHAIR — We have time for two more questions.

Mr DONNELLAN — The commonwealth indicated in its recent budget that it would be making amendments to the payment of the wine equalisation tax (WET). The Victorian government currently provides a 15 per cent cellar door rebate. What is the impact of this decision for Victoria?

Mr BRUMBY — Thank you for raising this. I know you are a — —

Mr FORWOOD — A wine drinker!

Mr BRUMBY — A strong supporter of the Victorian wine industry.

Mr FORWOOD — And the tobacco industry!

Mr BRUMBY — I was thinking more that in a policy sense he has been a strong supporter of the industry. This is an interesting issue and we are still in the process of getting further advice on this. We have been working very closely with the wine industry. As you are aware, after the introduction of the GST and the introduction of the WET arrangements, the effect of that was essentially to penalise the small and medium high-value wine producers. The big bulk producers of wine did very well out of it. You may have seen some doctors recently commenting on this — the AMA and others — saying it was an odd tax that did not tax by alcohol. The you could very large volumes of 11, 12 and 13 per cent alcohol by volume product that had a very low rate of tax.

The impact of the WET arrangements was essentially to penalise those small and medium-sized wineries with high valued wine. Most of those are located in Victoria. We tend not to be the huge, big, bulk producers, so we have been pushing for some time with the Victorian Wine Industry Association for a form of these arrangements, and I wrote to the federal Treasurer last year and said that if he would agree to reform those — and I think it was an amount of 600 000 litres — we would transfer to the commonwealth the payments that we currently make in terms of the cellar door rebate on the basis that those small and medium producers would be better off. On budget night the Treasurer announced new arrangements which generally were seen as a positive step forward in that he said there would be a wine equalisation tax rebate for wineries of up to $290 000 or $1 million in wholesale sales value. He wrote to me to say, 'Now I have done this, we would like you to give us the money you pay on the cellar door rebate'.

I have subsequently been advised by the VWIA that the new arrangements do not work as perhaps the federal Treasurer thought they might, and that they do not ensure that no winery will be worse off. In fact the VWIA estimates that the new federal arrangements deliver WET-free status to about 90 per cent of Victorian producers, but a number of the medium wineries with a high proportion of cellar door sales will, in fact, be worse off as a result of the proposed arrangements, combined with the current federal and state arrangements. The affected wineries, I understand, are what we describe as regional winery icons, and are large investors in regional winery tourism and employment. One example is All Saints Estate at Rutherglen. This business will be $103 000 worse off under the new arrangements compared to the current rebates on cellar door sales.

What the VWIA is therefore seeking is obviously a change to these arrangements. They want a retention of the state component of the current subsidy scheme, or alternatively they want 15 per cent of the 29 per cent of the WET paid on cellar door sales above the $290 000 federal rebate limit, to eliminate this disadvantage to those medium and large cellar door operators. It is an issue for those concerned. Generally the step that the commonwealth has taken is a step in the right direction so we are not interested in playing politics with this, but the advice the federal Treasurer got was not as accurate as it might have been, and there are unforeseen consequences. Therefore I will be writing to the federal Treasurer and saying that while we welcome this step in the right direction, there will be wineries worse off — not compared with the GST arrangement, but worse off than they are today, which would be quite counterproductive.

I am sure it was unintended , and I will be saying to the federal Treasurer that unless these intended consequences can be addressed we will not be in a position to offer up the cellar door rebate funding because it is offering that up that would make these wineries worse off. I hope we can achieve some constructive dialogue on that front, and reach a position where the small and medium–sized wineries are not disadvantaged and in fact are better off. That would be great for our industry. Finally, this year Victorian wine exports will be close to $350 million, and 10 years ago they were about $30 million. It has been a great success story for our state.

Mr CLARK — Can I come back to the issue of police fines and the information we discussed earlier at page 133 of budget paper 4? You referred in your previous answer to the various ex gratia payments being made as a result of the fixed speed camera issue. I assume they are being made out of a separate budget line, they are not being netted out of the fines revenue? My query is: we have a $94 million fall in expected revenue this year compared with last year, and then an expected jump of $117 million this year to next. The total amount involved in the fixed speed camera problems, I understand, is far smaller than that in terms of the amount of revenue that is being lost. Can you tell the committee how much revenue you estimate has been lost as a result of the fixed speed camera problems this year? Then, going forward to the $117 million increase, how much will come out of the fixed speed camera reinstatement and how much will come out of the extension of the red light speed cameras to control intersections, which is the other factor you referred to at page 133?

Mr BRUMBY — I will take that on notice, if I might. There are a number of questions contained in that question. To be fair, some of them rightly go to other ministers and portfolios and not to me, but I will take that on notice. I will give you as much information as I can. But just to reiterate the point, the actual numbers in 2002-03 were around $326 million, and we are forecasting $350 million for 2004-5, which is a growth a little lower than the nominal GDP. In 2003-04 the numbers are lower for a range of reasons which have been explained previously — the issues we have had with the cameras, the slower rollout of the speed camera program that was announced in 2002-3, and changes in driver behaviour. There has been a whole range of factors. You need to go to the Minister for Police and Emergency Services or the Minister for Transport on the full range of those factors, but in terms of any of the revenue matters, if I can get more information I will get that for you.

Mr CLARK — Just in that regard, Mr Little nodded to me in answer to the refunds coming out of — —

Mr BRUMBY — They will come out of the Treasurer's advance. Any of those unexpected payments come out of Treasurer's advance. They will not be netted off against revenue.

The CHAIR — Thank you very much, Treasurer. This concludes the estimates for the portfolios of Treasury, state and regional development and innovation. Thank you to your departmental officers in the second session from Treasury. We do appreciate your attendance. We thank Hansard also.

Mr BRUMBY — Sorry, can I just circulate that table I referred to earlier in answer to a question from Robert Clark? This was what I promised earlier. It reinforces the point I made about the superannuation liability that Robert was raising with me and the dip there. I am sorry it is not in colour, but it shows what the numbers were in last year's budget 2003-04 and what they are this year and you will see in all of the forward estimates the superannuation liability, and I can show you the same for net financial liabilities and for net debt. In all cases the numbers are better than we had anticipated last year.

The CHAIR — Thank you. We thank all those who have assisted with this morning's presentation. Copies of the Hansard transcript will be circulated to you within a week, along with follow-up questions from the secretariat.

Witnesses withdrew.