



**PARLIAMENT OF VICTORIA**  
Public Accounts and Estimates Committee

**Report on the 2015-16  
Budget Estimates**

Parliament of Victoria  
**Public Accounts and Estimates Committee**

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# Committee functions

The Public Accounts and Estimates Committee is a joint parliamentary committee constituted under the *Parliamentary Committees Act 2003*.

The Committee comprises nine members of Parliament drawn from both Houses of Parliament.

The Committee carries out investigations and reports to Parliament on matters associated with the financial management of the State. Its functions under the Act are to inquire into, consider and report to the Parliament on:

- any proposal, matter or thing concerned with public administration or public sector finances
- the annual estimates or receipts and payments and other budget papers and any supplementary estimates of receipts or payments presented to the Assembly and the Council
- any proposal, matter or thing that is relevant to its functions and has been referred to the Committee by resolution of the Council or the Assembly or by order of the Governor in Council published in the Government Gazette.

The Committee also has a number of statutory responsibilities in relation to the Office of the Auditor-General. The Committee is required to:

- recommend the appointment of the Auditor-General and the independent performance and financial auditors to review the Victorian Auditor-General's Office
- consider the budget estimates for the Victorian Auditor-General's Office
- review the Auditor-General's draft annual plan and, if necessary, provide comments on the plan to the Auditor-General prior to its finalisation and tabling in Parliament
- have a consultative role in determining the objectives and scope of performance audits by the Auditor-General and identifying any other particular issues that need to be addressed
- have a consultative role in determining performance audit priorities
- exempt, if ever deemed necessary, the Auditor-General from legislative requirements applicable to government agencies on staff employment conditions and financial reporting practices.

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This report is also available online at the Committee's website.

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# Acronyms and terms

<b>(Asset) investment through other sectors</b>	'Asset investment' funded through another sector (most commonly funded by the 'general government sector' and through the 'public non-financial corporations sector') for an asset that becomes part of that other sector. May be reported as gross inflows, gross outflows or net cash flows.
<b>Agency</b>	Government entities which generally receive their funding through 'departments' and for which 'departments' are responsible for reporting. Examples include Victoria Police, hospitals and TAFEs. Agencies, like 'departments', are directly accountable through one or more ministers to Parliament.
<b>Appropriation</b>	The authority to withdraw funds from the Consolidated Fund. This may be a once-off authority (as provided in the annual Appropriation acts) or a standing authority (a special appropriation provided by another act).
<b>Asset initiative</b>	A new program or project ('initiative') that delivers assets. See 'asset investment'.
<b>Asset investment</b>	Expenditure on assets (generally infrastructure such as roads or hospitals) as opposed to expenditure on the delivery of products and services ('outputs').
<b>Base funding</b>	The amount of funding received by a 'department' or 'agency' for the goods and services that it delivers every year. This is distinct from funding for time-limited 'initiatives'.
<b>Budget estimates</b>	Forecasts for future years made in the budget papers about matters such as revenue, expenditure, assets, liabilities and goods and services to be delivered.
<b>Budget papers</b>	The set of documents released with the annual budget. These normally include the Treasurer's speech and volumes on: strategy and outlook; service delivery; capital investment; and the estimated financial statements. The set also includes the annual financial report, published after the end of the budget period.
<b>Contingencies/contingency provisions</b>	Amounts included in a budget for expenses that have not been determined at the time of the budget. These provisions are for both predictable expenditure (such as dealing with population growth and initiatives to be released in future budgets) and unpredictable expenditure (such as unforeseen natural disasters).
<b>Department</b>	Large government entities. At 30 June 2015 there are seven departments in Victoria, plus Courts Victoria and the Parliamentary Departments. Funding for most 'agencies' is generally provided through departments and departments are required to report on the financial and performance results of the agencies for which they are responsible. Departments, like 'agencies', are directly accountable through one or more ministers to Parliament.

<b>Depreciation</b>	The amount of money it would require to keep the State's assets in the same condition as they were in last year. This amount is listed as an expense on the operating statement, and the cash equivalent to that amount is usually used to partially fund 'asset investment'.
<b>Direct (asset) investment</b>	'Asset investment' by the 'general government sector' managed by an 'entity' within that sector for an asset that becomes part of that sector.
<b>DTF</b>	Department of Treasury and Finance
<b>Entity</b>	Either a 'department' or an 'agency'.
<b>Expenditure reduction initiative</b>	Changes in the provision of 'outputs' that result in reductions to the cost of the 'output'. This may be done by reducing the services provided or providing the same services more efficiently. Savings initiatives are only one factor affecting 'output expenditure'. Thus, they may not reduce a department's total 'output expenditure' compared to the previous year if other factors (such as 'output initiatives') are greater in value. Savings initiatives are usually perpetual.
<b>Forward estimates period</b>	The period for which estimates are made in the budget papers. This includes the budget year and the following three financial years. The forward estimates period for the 2015-16 Budget is 2015-16 to 2018-19 inclusive.
<b>Funds outside the Public Account</b>	Funds held by entities that are in separate bank accounts and not in a 'Trust Fund' or the Consolidated Fund.
<b>General government sector</b>	Government 'entities' which provide services either with no charge to the user or with charges significantly below the cost of providing the services. This includes all 'departments' and many 'agencies'.
<b>General-purpose (GST) grants</b>	Grants from the Commonwealth Government to the State Government sourced from GST revenue. There are no restrictions imposed by the Commonwealth Government on how the funding can be spent.
<b>GFC</b>	Global Financial Crisis
<b>Gonski agreement</b>	The National Education Reform Agreement
<b>Government infrastructure investment</b>	A measure of 'general government sector' expenditure on infrastructure which includes 'direct asset investment', 'asset investment through other sectors' and some payments for 'public private partnerships' less proceeds from asset sales. Some Commonwealth-funded expenditure is excluded.
<b>Gross State Product (GSP)</b>	The total value of goods and services produced by the state in a year. This includes the goods and services delivered by the Government and the private sector.
<b>GST</b>	Goods and Services Tax
<b>HVHR</b>	High-Value, High-Risk
<b>ICT</b>	Information and Communications Technology

<b>Initiative</b>	A specific program or project detailed in the budget papers. Budget papers can include ‘asset initiatives’, ‘output initiatives’, ‘revenue initiatives’, ‘revenue foregone initiatives’ and ‘expenditure reduction initiatives’.
<b>Investments in financial assets for policy purposes</b>	See ‘investment through other sectors’.
<b>Liabilities</b>	Amounts that an organisation is obliged to pay in future years. Examples include borrowings and defined benefits superannuation plans.
<b>MICA</b>	Mobile Intensive Care Ambulance
<b>MOG</b>	Machinery-of-government
<b>NDIS</b>	National Disability Insurance Scheme
<b>Net borrowings</b>	New interest bearing liabilities raised from public borrowings during the year (less interest bearing liabilities repaid). Not to be confused with ‘Net lending/borrowing’.
<b>Net debt</b>	A calculation based on the difference between the value of selected categories of financial assets and financial liabilities. Essentially, the difference in value between what the Government owes and assets that it could easily convert to cash. Not all financial assets and liabilities are included.
<b>Net lending / borrowing</b>	A measure of financial performance in a year, calculated by adding economic flows (such as changes in the values of financial assets and liabilities) and ‘asset investment’ (net of asset funding) to ‘net result from transactions’.
<b>Net operating balance’</b>	See ‘operating surplus’.
<b>Net result</b>	A measure of an entity’s financial performance in a year which is calculated by taking the ‘net result from transactions’ and then adding other economic flows, such as changes in the values of financial assets and liabilities. The net result is different to the ‘net result from transactions’ (see below). ‘Asset investment’ is not included in either the net result or the ‘net result from transactions’.
<b>Net result from transactions</b>	See ‘operating surplus’.
<b>NHR</b>	National Health Reform Agreement
<b>Non-financial public sector (NFPS)</b>	The ‘general government sector’ and ‘public non-financial corporations sector’ consolidated together.
<b>Operating revenue</b>	See ‘revenue’.

<b>Operating surplus/balance</b>	A measure of a body's financial performance in a year which is calculated by subtracting an entity's expenses in the year from its income. Also known as the 'net result from transactions' or 'net operating balance'. 'Asset investment' is not included in the operating balance.
<b>Outcome</b>	The impact of an 'output' on the community, such as healthier people or a reduction in crime.
<b>Output</b>	An aggregate of goods and services (such as health care or policing services) delivered by a 'department' or its 'agencies'. Outputs are identified in the budget papers.
<b>Output expenditure</b>	Expenditure on 'outputs' (that is, goods and services). This is distinct from 'asset investment', although it includes some expenditure on 'public private partnerships'.
<b>Output initiative</b>	A new program or project ('initiative') that delivers goods and services (part of a department's 'outputs'). Output initiatives are usually for a limited period of time, although they are sometimes perpetual.
<b>PAEC</b>	Public Accounts and Estimates Committee
<b>PBU</b>	Pre-Election Budget Update
<b>PNFC</b>	Public non-financial corporation - see 'public non-financial corporations sector'.
<b>Present value</b>	The amount of money held today which is equivalent to a sum of money received in the future or stream of cash flows into the future given a specified rate of interest. For a loan, this is how much money would need to be held today to make all of the payments in the future, factoring in interest that would accrue to that money over time.
<b>PTV</b>	Public Transport Victoria
<b>Public Account</b>	The Government's principal bank account. The Public Account includes the Consolidated Fund and the 'Trust Fund'.
<b>Public financial corporations (PFC) sector</b>	Government 'agencies' which provide financial services, such as the Treasury Corporation of Victoria or the Transport Accident Commission.
<b>Public non-financial corporations (PNFC) sector</b>	Government 'agencies' which provide goods or services with charges that recover most of the cost of producing them, such as water authorities and trusts administering certain facilities. Does not include 'agencies' providing financial services (see 'public financial corporations sector').
<b>Public private partnership (PPP)</b>	An arrangement in which the private sector delivers an asset on behalf of the Government. Ownership of the asset usually passes to the Government after a defined period of time.
<b>Public sector as a whole</b>	The 'general government sector', 'public non-financial corporations sector' and 'public financial corporations sector' consolidated together. Referred to in the budget papers and Annual Financial Report as the 'State of Victoria'.

<b>Purchases of non-financial assets</b>	See 'direct investment'.
<b>Revenue</b>	Income received by the Government, mostly from State taxes and grants from the Commonwealth Government.
<b>Revenue foregone initiative</b>	Changes in policy which result in a decrease in 'revenue'. Examples include reducing a tax rate or increasing the number of people exempted from a tax. Like 'revenue initiatives', revenue foregone initiatives are usually perpetual.
<b>Revenue initiative</b>	Changes in policy which result in an increase in 'revenue'. Examples include new taxes or increasing existing taxes. Revenue initiatives are usually perpetual.
<b>Savings initiative</b>	Changes in the provision of 'outputs' that result in reductions to the cost of the 'output'. This may be done by reducing the services provided or providing the same services more efficiently. Savings initiatives are only one factor affecting 'output expenditure'. Thus, they may not reduce a department's total 'output expenditure' compared to the previous year if other factors (such as 'output initiatives') are greater in value. Savings initiatives are usually perpetual.
<b>Specific-purpose grants</b>	Grants from the Commonwealth Government to the State Government with restrictions on how the funding can be spent.
<b>State of Victoria</b>	See 'public sector as a whole'.
<b>TAC</b>	Transport Accident Commission
<b>TAFE</b>	Technical and Further Education
<b>TEI/Total estimated investment</b>	An estimate of the total amount of expenditure required to deliver an 'asset investment' project.
<b>Trust fund</b>	Part of the 'Public Account'. Trust accounts within the trust fund are set up to receive and distribute funds for specific purposes.
<b>VMIA</b>	Victorian Managed Insurance Authority

# Chair's foreword

I am pleased to present the *Report on the 2015-16 Budget Estimates* as part of the annual inquiry into the budget estimates by the Public Accounts and Estimates Committee. This report examines the assumptions, plans and estimates set out by the Government over the forward estimates period to 2018-19.

The report brings together the evidence presented to the Committee in relation to the 2015-16 Budget, including public hearings with ministers, departmental questionnaires and the budget papers.

The chapters included in this report examine the major aspects of the 2015-16 Budget, including the Government's plans regarding revenue, output expenditure, debt, liabilities and asset investment. The report also discusses the funding of the Government's election commitments, the changes to the key components of the performance measurement system for 2015-16 and the implementation of previous recommendations made by the former Committee.

One of the more important roles the Committee's reports plays is to assist members with their understanding of budgets and the processes by which they are created. Budgets can be intimidating documents, and cover a wide range of subjects, both financial and strategic.

In this report, the Committee has explained the information in five budget papers, five information papers and two budget updates. It has also addressed the Government's strategy and the wider implications of the budget for Victoria, in terms of revenue, expenses and how they relate to the State's debt position. I hope that the report will be some help to members in assisting their own constituents' understanding of this complicated subject.

The Committee is grateful to the many people who have contributed their time and effort to helping this inquiry. The Presiding Officers, Premier, Deputy Premier, Treasurer, Attorney-General, ministers, departmental secretaries and many of their staff have provided essential information in responding to questionnaires, attending public hearings, and answering questions on notice.

I would like to express my gratitude to the Committee's secretariat for their support throughout the inquiry. Their professionalism and the high quality of their work are greatly appreciated by myself and the Committee.

Finally, this is the first estimates report that has been produced by the Committee. I thank my fellow Committee members for their great efforts, their supportive approach, the inquisitiveness in their analysis and the spirit of co-operation in their deliberations on this report.



**Mr Danny Pearson MP**  
**CHAIR**

# Findings and recommendations

<b>1</b>	<b>Introduction</b>	<b>page</b>
	<b>FINDING 1:</b> The budget papers estimate that there will be a \$1.2 billion operating surplus in 2015-16, rising to \$1.8 billion in 2018-19. The 2015-16 Budget includes \$9.2 billion of new initiatives to deliver goods and services and \$19.0-22.0 billion of new asset investment projects. The budget papers predict that net debt will be reduced in 2015-16 and then rise between 2016 and 2019.	<b>2</b>
	<b>FINDING 2:</b> Previous budgets have consistently overestimated or underestimated a number of key items. These items include revenue, output expenses and the growth of gross state product. The budget papers do not discuss these variations, leaving readers of the budget papers unaware of the limitations in the Department of Treasury and Finance’s estimating methodology.	<b>5</b>
	<b>RECOMMENDATION 1:</b> Future budget papers include a discussion about the tendencies to underestimate or overestimate certain items in past budget estimates, including both financial statement items and key economic assumptions. This discussion should include:  (a) identifying the items which past budget papers have consistently underestimated or overestimated (considering the entire forward estimates period)  (b) quantifying the variations between the actual results and the estimates for these items (across all years of the relevant forward estimates periods).	<b>5</b>
	<b>RECOMMENDATION 2:</b> When future budget papers discuss the estimated future growth rates of items compared to past actual growth rates, the discussion clearly indicate if underestimation or overestimation of the estimates is likely to be a factor causing variances. This should apply to both financial statement items and key economic assumptions.	<b>5</b>
	<b>RECOMMENDATION 3:</b> The Department of Treasury and Finance consider including ‘fan charts’ in the budget papers, showing the likelihood of different outcomes for key budget estimates based on past variances between forecasts and actual results.	<b>5</b>
	<b>FINDING 3:</b> The 2015-16 budget papers provide more information in some areas than previous budgets. The disclosure in future budget papers could be enhanced by providing further details about the Government’s financial management objectives, sources of revenue, net debt targets and performance measurement.	<b>6</b>
	<b>FINDING 4:</b> The budget papers contain a large amount of information, spread across five core volumes. In some cases, connections between different parts of the budget papers could be improved to make the discussion of key topics more comprehensive.	<b>7</b>
	<b>RECOMMENDATION 4:</b> The Department of Treasury and Finance review the budget papers to identify areas where the discussion could be improved by making cross-references to other parts of the budget papers.	<b>7</b>



**FINDING 5:** A key function of the budget papers is to explain the basis for the estimated financial statements. The budget papers already contain much explanatory information, but the Committee has identified some areas where additional explanations would be helpful. The Committee considers that explaining variances between past actual growth rates and estimated future growth rates is particularly important. 8

**RECOMMENDATION 5:** Future budget papers include explanations for significant variances between past actual growth rates and estimated future growth rates for any item over \$100.0 million. A variance should be counted as significant when the future growth rate (between the budget year and the end of the forward estimates period) varies by greater than  $\pm 1$  percentage point from the growth rate across the last five years for which actual amounts are known. 8

## 2 Key aspects of the 2015-16 Budget page

**FINDING 6:** The budget papers estimate that an operating surplus of \$1.2 billion will be achieved in 2015-16. This is higher than the surplus of \$883.0 million estimated for 2014-15. The proposed lease of the Port of Melbourne's operations is also expected to facilitate a higher level of asset investment than the previous year and the first decrease in net debt since 2005-06. 17

**FINDING 7:** The Government has established four long-term financial management objectives, which are supported by three medium-term measures. However, the quantified targets for two of these measures are disclosed in a different budget paper to the discussion of the financial management objectives and measures. In addition, the medium-term measures do not reflect all of the long-term objectives. 22

**RECOMMENDATION 6:** In discussing the Government's financial objectives and measures in future Strategy and Outlook budget papers, the discussion clearly note the existence of any relevant quantified targets in other parts of the budget papers, including Note 1 to the financial statements. 22

**RECOMMENDATION 7:** The Government expand its financial management targets to provide specific targets for all four of its long-term objectives. 22

**FINDING 8:** Two of the key components of the performance measurement system are departmental objectives, which identify the intended impact of departmental activities on the community, and performance measures, which set the standards for the delivery of goods and services. The number of objectives has decreased from 46 to 35 since the last budget, while departments have proposed reducing the number of performance measures from 1,174 to 1,116. 24

**FINDING 9:** The Government states that 96 per cent of the output funding and 65 per cent of the asset funding promised in its election commitments have been included in the budget estimates. The budget estimates also include a number of initiatives that were not included as election commitments in *Labor's Financial Statement 2014*. 25

**FINDING 10:** The budget estimates predict an improvement in the sustainability of the general government sector's finances, with increasing operating surpluses and a net lending position in the last two years of the forward estimates period. 29

- FINDING 11:** The budget estimates for the public sector as a whole suggest improved financial performance across the forward estimates period. However, the public sector is expected to remain in an operating deficit throughout the forward estimates period and to be in a net borrowing position for all years except 2015-16. 30
- FINDING 12:** The Government has indicated that it is not always practicable for PNFC sector entities to recover all costs, including depreciation, through charges. The Government has indicated that additional funding can be provided from the general government sector. However, the levels of asset investment predicted for the PNFC sector are lower than the value of depreciation in some years of the forward estimates period. 31
- FINDING 13:** Large amounts of money are expected to flow between the different parts of the public sector. In 2015-16, both the PNFC and PFC sectors will receive more from the general government sector than they give. However, the current budget estimates predict that, in 2018-19, the PNFC sector will provide more money to the general government sector than it receives. This is largely driven by an expected drop in the value of services purchased by the general government sector from the PNFC sector. 33
- FINDING 14:** For the general government sector, the level of asset investment over the forward estimates period is expected to be more than required to maintain the infrastructure base. However, between 2016-17 and 2018-19, asset investment for the PNFC sector is expected to be less than required to maintain the asset base (as indicated by depreciation). 35
- FINDING 15:** Net debt for the general government sector is expected to reduce from \$21.2 to \$16.9 billion in 2015-16 following the proposed lease of the Port of Melbourne's operations. It is then expected to rise in each of the remaining years of the forward estimates period, reaching \$19.8 billion in 2019. However, as a proportion of gross state product, net debt will reduce between 2015 and 2019, in line with the Government's financial management target. 37
- FINDING 16:** For the PNFC sector, net debt is expected to increase in every year of the forward estimates period, from \$14.9 billion in 2015 to \$16.4 billion in 2019. 37
- FINDING 17:** The 2015-16 Budget releases new output initiatives with a total estimated cost of \$9.3 billion over five years. Over the forward estimates period, 71.8 per cent of the cost of these initiatives is expected to be funded through the reprioritisation of existing resources, the use of contingency allowances put aside in previous budget estimates and expenditure reduction initiatives. The remaining cost will increase output expenses compared to previous estimates. 40
- FINDING 18:** The 2015-16 Budget includes new asset initiatives with a total expected cost of \$19.0-22.0 billion. These, along with initiatives from previous budgets, will be funded by a mixture of cash resources and borrowings. The mixture was indicated in a chart in some previous budget papers, but this year is not indicated in this way. 41
- RECOMMENDATION 8:** The Department of Treasury and Finance include in future budget papers a chart indicating the proportion of each year's infrastructure investment expected to be funded by cash and the proportion expected to be funded by debt in recent years and across the forward estimates period. 41

**FINDING 19:** The core budget papers in 2015-16 are mostly structured in the same way as they were in 2014-15. Some additional details have been added which have increased transparency. However, some changes have decreased transparency in other areas. 44

### 3 Economic overview page

**FINDING 20:** Government activity in Victoria, measured by the expenses of the total public sector, is expected to account for 16.6 per cent of GSP in 2015-16 (\$63.7 billion) and 15.6 per cent in 2018-19 (\$69.8 billion). Similarly, public sector revenue is expected to change from 16.3 per cent of GSP (\$62.7 billion) in 2015-16 to 15.5 per cent in 2018-19 (\$69.6 billion). The decrease in revenue and expenses as a proportion of GSP reflects budget estimates that the Victorian economy will grow at a faster pace than public sector revenue and expenses. 48

**FINDING 21:** The Budget has been developed on estimates that gross state product will grow by 2.5 per cent (in real terms) in 2015-16 compared to the previous year and then by 2.75 per cent per year for the following three years. These are higher rates than have been seen in recent years. The 2015-16 budget papers indicate that economic growth over the next four years will be driven primarily by household consumption and dwelling investment. 52

**FINDING 22:** The budget papers each year do not provide quantified forecasts of the components of gross state product, making it difficult to assess the estimates of gross state product. 57

**RECOMMENDATION 9:** Future budget papers include a break-down of the forecasts of gross state product used in developing the budget estimates. This break-down should quantify the expected value of each of the main components of gross state product across the forward estimates period, including household consumption, dwelling investment, business investment and trade. 57

**FINDING 23:** The Department of Treasury and Finance discloses six key economic forecasts in the budget papers each year. However, there are additional significant factors for which the Department does not disclose its forecasts. Without disclosure of the forecasts used in producing the budget estimates, it is difficult to assess the risks to the budget estimates that may come from variations to the forecasts. 58

**RECOMMENDATION 10:** Future budget papers publish the forecasts for the budget year and forward estimates period for any variable included in the sensitivity analysis for which a 1 percentage point variance would impact on the operating surplus or net debt by more than \$100.0 million over the forward estimates period. For any variable where this is not appropriate, the budget papers should state the reasons why the forecasts for this variable have not been published in the budget papers. 58

**FINDING 24:** Not all of the key economic assumptions on which the budget estimates have been based are included in the sensitivity analysis in the budget paper each year. 58

- RECOMMENDATION 11:** The sensitivity analysis in future budget papers include all variables listed in Note 1 to the financial statements as key economic assumptions (including population growth and the unemployment rate). For any variable where this is not appropriate, the budget papers should state the reasons why this variable has not been included in the sensitivity analysis. 59
- FINDING 25:** The 2015-16 budget papers identify a number of risks to the economic outlook. If they eventuate they would have a negative effect on the economy and consequently on the budget estimates. Only two of these risks are quantified in the sensitivity analysis in the budget papers. 61
- RECOMMENDATION 12:** Future budget papers quantify the impact of the main risks to the Victorian economy identified in the discussion in Budget Paper No.2 by including all of the identified risks in the sensitivity analysis. For any risk where this is not appropriate, the budget papers should state the reasons why this risk has not been included in the sensitivity analysis. 61
- FINDING 26:** The Government anticipates a more positive outlook for the labour market over the forward estimates period. It expects to positively influence the labour market over the next four years through funding a number of initiatives in the labour market, education and training areas. The Government has set a target of creating 100,000 jobs and provides forecasts for the employment and unemployment rates. However, it has not quantified the expected impact on other key measures of employment. 65
- RECOMMENDATION 13:** The Department of Treasury and Finance release forecasts and publish targets for the underemployment rate, underutilisation rate, the total number of hours worked and the youth unemployment rate. 65
- RECOMMENDATION 14:** The Government release regular reports to assess the progress and efficacy of the Government's programs to stimulate employment. 65
- FINDING 27:** Forecasts produced by the Department of Treasury and Finance have shown mixed success between 2007-08 and 2013-14, with 47.6 per cent of recent estimates for the budget-year within 0.5 percentage points of the actual result. However, the growth in real gross state product has been consistently overestimated and population growth has been consistently underestimated. 69
- RECOMMENDATION 15:** The Department of Treasury and Finance review its methodology for forecasting growth in real gross state product (in the light of the regular overestimation in previous budgets) and population growth (in the light of regular underestimation). 69
- FINDING 28:** Forecasts for most of the key economic variables for 2017-18 and 2018-19 are based on past average growth rates over different periods of time. These periods range from nine years (in the case of population growth) to 37 years (in the case of employment growth). The budget papers and the Department of Treasury and Finance's *Method for Making Forecasts of Macro-Economic Indicators* provide very limited details about how forecasts of the last two years of the forward estimates period are calculated. 70

**RECOMMENDATION 16:** Future budget papers include additional details about the methodology used in making economic forecasts across the forward estimates period, including the period of time considered when calculating trends where appropriate. 71

**RECOMMENDATION 17:** The Department of Treasury and Finance update the *Method for Making Forecasts of Macro-Economic Indicators* to provide more detailed descriptions of the methods used to produce forecasts for the last two years of the forward estimates period. 71

## 4 Revenue page

**FINDING 29:** Revenue is expected to rise to \$55.5 billion in 2015-16. It is then forecast to rise to \$61.2 billion over the forward estimates period, an average growth rate of 3.3 per cent per year. The growth rate for revenue anticipated over the forward estimates period is significantly lower than historical rates. Though there is a strong relationship between gross state product (GSP) and taxation revenue, the budget estimates suggest that taxation revenue will grow more slowly than GSP over the forward estimates period. 76

**RECOMMENDATION 18:** Future budget papers include an explanation of how the estimates for GSP have influenced the estimates of different components of revenue. In cases where GSP growth rates differ significantly from revenue growth rates, these explanations should identify the factors which have caused the difference in growth rates, and discuss how each factor has influenced the estimate. 76

**RECOMMENDATION 19:** The Auditor-General assess whether the factors used by the Department of Treasury and Finance in constructing revenue estimates are adequately described in the budget papers. This assessment should include the way GSP estimates, and any other relevant factors, have been taken into account. As part of this, the Auditor-General should examine why the taxation estimates in the 2015-16 Budget increase at a slower rate than has occurred in recent years at the same time that the GSP estimates increase at a faster rate. 77

**FINDING 30:** The budget estimates predict that revenue will grow at a slower rate over the forward estimate period than in recent years. This may be a result of a forecasting methodology that includes conservative estimates and omits elements of revenue where the amount to be received is uncertain. 79

**FINDING 31:** Revenue is expected to be \$9,172 per Victorian in 2015-16. By 2018-19, revenue is expected to have decreased to \$8,880 per Victorian (in 2015-16 terms), as population and inflation are expected to grow at a faster rate than the revenue estimates. 80

**FINDING 32:** The value of revenue and revenue foregone initiatives released in the 2015-16 budget papers is significantly less than the value of initiatives released in the last four budgets. 86

**FINDING 33:** The *Stamp Duty Exemption on Mobile Plant Registration* initiative and the *Car Registration Discounts for Trade Apprentices* initiative are both intended to forego revenue to achieve policy objectives. However, the former has been listed in the budget papers as a revenue initiative, while the latter has been included as an output initiative. 87

<b>RECOMMENDATION 20:</b> Future budget papers include information in the revenue measures section on all initiatives whose main effect is to lower revenue. This can be achieved either by:	
(a) including all such initiatives in the revenue measures section of the budget papers as revenue initiatives or	
(b) including a cross-reference in the revenue measures section of the budget papers to relevant initiatives in other sections of the budget papers.	87
<b>FINDING 34:</b> Additional orientation information describing a number of revenue items was included in previous budget papers but has not appeared in the 2015-16 budget papers.	90
<b>RECOMMENDATION 21:</b> The budget papers reinstate the practice of including background information on the major components of revenue, including, where relevant, the component's purpose, how it is calculated and relevant concessions and exemptions. This information may be included in the discussion of each revenue item or in another section in the budget papers.	90
<b>FINDING 35:</b> Sales of goods and services are expected to total \$6.8 billion in 2015-16, rising further to \$7.0 billion in 2017-18 and 2018-19. This is a much slower growth rate than occurred in recent years.	91
<b>FINDING 36:</b> Surpluses accumulated over the forward estimates period by WorkSafe are intended to be used to decrease premiums and to fund programs to benefit the Victorian workforce. Surpluses from other enterprises are intended to be passed to the Government as dividends. The Auditor-General has noted an increase in borrowings by water authorities to finance the construction of infrastructure assets at the same time that dividends have been taken by the general government sector.	96
<b>RECOMMENDATION 22:</b> The Government publish a detailed explanation of its dividend policy, identifying the factors considered in determining when it is best to leave profits with entities and when it is best to take them as dividends.	96
<b>RECOMMENDATION 23:</b> Future budget papers provide more detailed discussion about the estimated dividend payments included in the forward estimates. This discussion should explain why those amounts are considered appropriate and indicate the expected impact of dividend payments on the financial sustainability of paying entities. This should include a discussion of the effects on paying entities' abilities to carry out their infrastructure investment plans while meeting required dividend payments.	96
<b>FINDING 37:</b> The Government anticipates that income tax equivalent revenue will be \$287.1 million in 2015-16 and increase to \$463.8 million by 2018-19. It is expected to increase by 67.5 per cent in the last year of the forward estimates period. This change is not explained in the budget papers.	97
<b>FINDING 38:</b> The Government expects that general-purpose (GST) grants from the Commonwealth Government will rise to \$12.8 billion in 2015-16, before rising further to \$15.8 billion by 2018-19. This is driven by expectations of increased GST pool size and a more favourable GST relativity.	98

**FINDING 39:** Specific-purpose grants are expected to be \$12.7 billion in 2015-16. The budget estimates assume no growth over the forward estimates period, despite a long-term trend of growth. The budget papers attribute this to the transfer of some aged care expenditure to the Commonwealth, changes in agreements for indexing grants and expiring fixed-term programs. The Department of Treasury and Finance's methodology for estimating specific-purpose grants may also have underestimated the value of grants over the forward estimates period. 101

## 5 Parliamentary control over departmental revenue page

**FINDING 40:** The budgetary appropriations system provides the Government with a number of methods to access public money. Some of these methods require direct Parliamentary authority, while others are determined by the Treasurer or Minister for Finance. The proportion of total income for departments that is not determined directly by the Parliament has increased from between 11 and 14 per cent to around 21 per cent due to changes in health funding from the Commonwealth Government. The budget papers have not discussed this change. 106

**RECOMMENDATION 24:** Future budget papers note the proportion of revenue that comes from annual and special appropriations compared to other sources and explain any significant changes in this proportion from previous years. 106

**FINDING 41:** Annual appropriations are well disclosed, both before and after the financial year. The uses for which special appropriations are intended are not fully disclosed in either the budget papers or departments' annual reports. 107

**RECOMMENDATION 25:** Future budget papers specify how much of each special appropriation is intended to fund:

- (a) the provision of outputs
- (b) additions to the net asset base
- (c) payments made on behalf of the State. 108

**RECOMMENDATION 26:** The Department of Treasury and Finance require departments, in annual reports, to disclose the amounts received in special appropriations that are used in:

- (a) the provision of outputs
- (b) additions to the net asset base
- (c) payments made on behalf of the State.

Any variances between the purpose set out in the budget papers and the actual use should be identified and explained. 108

**FINDING 42:** In contrast to annual appropriations and special appropriations, the contributions of funds received and held outside the Public Account and the Trust Fund to the operating statement are not disclosed in the budget papers. 108

**RECOMMENDATION 27:** Future budget papers specify the anticipated contributions from funds received and held outside the Public Account and the Trust Fund to departments' operating statements. 108

**FINDING 43:** As in previous years, the budget papers do not disclose the amounts expected to flow from individual trust accounts to departments or the intended purpose of funding appropriated from trust accounts. Annual reports do not specify the uses that funding from trust accounts were put to. 109

**RECOMMENDATION 28:** Future budget papers specify the amounts expected from each trust account for each department. 109

**RECOMMENDATION 29:** Future budget papers specify the intended purpose (provision of outputs, additions to the net asset base, or payments on behalf of the State) of money received by departments from trust accounts. 109

**RECOMMENDATION 30:** The Department of Treasury and Finance require departments, in their annual reports, to disclose their income from the Trust Fund, broken down into the provision of outputs, additions to the net asset base and payments made on behalf of the State. Any variances between the initial budget estimates and the actual amounts should be identified and explained. 109

**FINDING 44:** The contribution from funds received and held outside the Public Account is not separately disclosed in either the budget papers or in departments' annual reports. 110

**RECOMMENDATION 31:** Future budget papers separately detail the income expected from funds held outside the Public Account for each department, broken down into the provision of outputs, additions to the net asset base and payments made on behalf of the State. 110

**RECOMMENDATION 32:** The Department of Treasury and Finance require departments, in their annual reports, to disclose their income from funds held outside the Public Account, broken down into the provision of outputs, additions to the net asset base and payments made on behalf of the State. Any variances between the initial budget estimates and the actual amounts should be identified and explained. 110

**FINDING 45:** When the cost of delivering an output in a year is lower than the price agreed with the Government, the unspent portion of the agreed price may be spent by the department in the future, with the permission of the Treasurer. Departments have consistently accumulated these amounts over the last decade, with 'applied appropriations unspent' totalling \$5.1 billion at 30 June 2014. 113

**RECOMMENDATION 33:** In future budget papers, the Department of Treasury and Finance:

- (a) note the total value of accumulated applied appropriations unspent, broken down into the major components (including payables, accruals related to employee entitlements, prior years' surpluses and depreciation equivalent revenue)
- (b) indicate the estimated change to these values over the forward estimates period
- (c) indicate the reasons for the anticipated changes for each component. 113



<b>6</b>	<b>Borrowings, debt and liabilities</b>	<b>page</b>
	<b>FINDING 46:</b> The Government has set a target of reducing net debt as a proportion of gross state product for the general government sector. However, the Government has not set a target for net debt in the public non-financial corporations sector, although that sector's net debt is also a significant amount. The Government's plans for net debt are therefore not comprehensively disclosed.	117
	<b>RECOMMENDATION 34:</b> Future budget papers include a target for net debt in the public non-financial corporations sector.	117
	<b>FINDING 47:</b> The Government expects that the proposed Port of Melbourne lease will result in general government sector borrowings decreasing to \$29.2 billion and net debt decreasing to \$16.9 billion by June 2016. After this, borrowings and net debt are expected to rise, reaching \$33.5 billion and \$19.8 billion respectively by June 2019.	118
	<b>FINDING 48:</b> The budget papers anticipate that borrowings and net debt for the public non-financial corporations sector will continue to increase over the forward estimates period. Net debt for the PNFC sector is estimated to increase from \$14.9 billion to \$16.4 billion between 2015 and 2019.	120
	<b>FINDING 49:</b> Melbourne Water Corporation and the three urban water authorities are expected to make up around 85 per cent of the net debt in the public non-financial corporations sector in June 2015. These entities are all expected to increase debt levels over the forward estimates period.	120
	<b>FINDING 50:</b> The Government plans to decrease its unfunded superannuation liability to zero by 2035. The liability is expected to decrease gradually but consistently over the forward estimates period as plan assets increase. However, the budget papers do not include interim goals towards the Government's 2035 target. Without such goals, it is not possible to determine whether the unfunded liability is on track to be zero by 2035.	123
	<b>RECOMMENDATION 35:</b> The budget papers reinstate the practice of including a diagram showing the expected level of unfunded superannuation liability in each year between the budget year and 2035, similar to the disclosure in earlier budget papers. Commentary should also be provided on the achievement of interim goals.	123
	<b>FINDING 51:</b> In comparison to the 2014 Pre-Election Budget Update, the 2015-16 budget papers estimate that less cash will be available over the forward estimates period from operating surpluses to fund asset investment. However, the 2015-16 Budget estimates that this will be partly offset by cash inflows from investment through other sectors. The Budget also estimates that less borrowing will be required for infrastructure investment and public private partnerships. As a result, the 2015-16 Budget estimates that net debt will decrease by \$148.4 million more between 2014 and 2018 than was estimated in the 2014 Pre-Election Budget Update.	126
	<b>FINDING 52:</b> The 'reconciliation of estimates' table in the budget papers provides useful information on what has driven changes between current and previous estimates of operating surpluses. There is no equivalent reconciliation of estimates table for net debt estimates.	126

**RECOMMENDATION 36:** Future budget papers include an additional table reconciling the information given in the ‘application of cash resources’ table between current and previous estimates, similar to ‘reconciliation of estimates’ table produced for operating surpluses. This table would include changes to estimates for:

- (a) net cash flows from operating activities
- (b) direct investment (purchases of non-financial assets)
- (c) investment through other sectors (net cash flows from investments in financial assets for policy purposes)
- (d) proceeds from asset sales
- (e) finance lease liabilities
- (f) changes in net debt. 127

**RECOMMENDATION 37:** Accompanying the table reconciling estimates of net debt, the Department of Treasury and Finance provide discussion of the factors that have driven the changes between budgets. 127

## 7 **Output expenses** page

**FINDING 53:** The Government has stated an intention to improve public services and to increase output expenses at a faster rate than the previous government planned. However, this growth will need to be limited to achieve the Government’s other goals of maintaining the State’s triple-A credit rating and growing infrastructure while maintaining debt levels. In the 2015-16 Budget, the higher estimated growth rate for operating expenses is anticipated to be largely offset by cash inflows from the proposed lease of the Port of Melbourne and from the public financial corporations sector. 131

**FINDING 54:** The budget papers estimate that output expenses will grow at an average of 3.0 per cent per year over the forward estimates period. This is a much lower rate than the actual growth in recent years, which has averaged 6.2 per cent. However, previous budgets have consistently underestimated the growth in output expenses by significant amounts, suggesting that the forward estimates in this budget may be understated. 132

**FINDING 55:** The budget estimates suggest that output expenses will decline over the forward estimates period when adjusted for population growth and inflation. However, this may be a result of the forward estimates being underestimated. 133

**FINDING 56:** The majority of output expenses relate to health and education, followed by the categories ‘transport and communications’ and ‘public order and safety’. The forward estimates suggest that future spending will be relatively similar. However, the budget estimates do indicate a decrease in the proportion of expenses for housing and community amenities. 136

**FINDING 57:** The estimated growth in output expenses is largely driven by expected increases in employee expenses and grants to the private and not-for-profit sectors. Purchases of services are expected to decrease as a result of the transfer of some responsibilities to the Commonwealth Government as part of the National Disability Insurance Scheme. 137

- FINDING 58:** The estimates for output expenses between 2015-16 and 2017-18 have been revised upwards by approximately \$2 billion per year since the 2014 Pre-Election Budget Update. This has been driven by new output initiatives, changes to specific-purpose grants and administrative variations. 140
- FINDING 59:** The format of the 'reconciliation of estimates' table has been modified in the 2015-16 budget papers. Generally, this has made the information easier to understand. However, this table no longer separately discloses the impact of variations in specific-purpose grants on revenue and expenses. 140
- RECOMMENDATION 38:** 'Reconciliation of estimates' tables in future budget papers separately disclose the impact on revenue and expenses of variations in specific-purpose grants. Differences between the impact on revenue and the impact on expenses should be discussed when the differences exceed \$100 million. 140
- FINDING 60:** Machinery-of-government changes affected six departments during 2014-15. Departments indicated that the expected costs of these changes in 2014-15 ranged from zero to \$2.0 million. 142
- RECOMMENDATION 39:** The Department of Treasury and Finance update the Model Report to require all departments to report any costs and benefits in a year as a result of machinery-of-government changes in their annual reports. The updated report should include guidance so that the data in annual reports are provided on a consistent basis across departments. 142
- FINDING 61:** Some departments indicated that the machinery-of-government changes may result in reduced expenses in future years through efficiencies. 143
- FINDING 62:** The budget papers refer to 'base funding' for ongoing programs. However, the concept of base funding was not clear to departments when questioned, suggesting that there may be a difference between the way that the funding process is described and actual practice. 145
- RECOMMENDATION 40:** Future budget papers clarify what is meant by 'base funding' and explain the relationship between base funding, initiative funding and output prices. 145
- RECOMMENDATION 41:** The Department of Treasury and Finance clarify the Budget and Financial Management Guidances to include a definition of 'base output price' and how the escalation of this relates to the budget estimates. 145
- RECOMMENDATION 42:** The Auditor-General conduct an audit of whether the way that output prices are calculated is clearly and accurately articulated by the Department of Treasury and Finance in its Budget and Financial Management Guidances and other documentation. 145
- FINDING 63:** The 2015-16 Budget provides funding for \$9.3 billion of new output initiatives. The largest new initiatives relate to health and education. Other large initiatives also relate to social and community services and boosting jobs and the economy. 149

**FINDING 64:** The budget papers estimate that new expenditure reduction initiatives will reduce expenses by \$334.5 million over four years. Departments have generally indicated that they expect this to be achieved without any impacts on service delivery. However, there is no reporting structure in place to assess whether or not these expectations will turn out to be accurate. 151

**RECOMMENDATION 43:** The Department of Treasury and Finance update the Model Report to require all departments to list expenditure reduction targets set for the relevant year and how these targets were met. This should include details of any impacts on service delivery, including quantification of the impacts where possible. 151

**FINDING 65:** The budget papers indicate that \$1.5 billion of the cost of new initiatives will be met by reprioritising funding previously provided to departments. The budget papers do not include details of which programs have been affected by the reprioritisation. 152

**RECOMMENDATION 44:** Future budget papers include details of the programs from which funding has been reprioritised, including:

- (a) the name of the program, initiative or project from which funding has been reprioritised
- (b) the amount reprioritised from each year of the forward estimates period
- (c) the budget in which the initiative was released (where relevant). 152

**RECOMMENDATION 45:** The Department of Treasury and Finance update the Model Report to require departments to report on the actual amounts of money reprioritised during the year, including:

- (a) the name of the program, initiative or project from which funding has been reprioritised
- (b) the amount reprioritised in the year
- (c) the budget in which the initiative was released (where relevant). 153

**FINDING 66:** The Government has used \$4.8 billion of the contingency allowance put aside in previous budget estimates to offset the cost of its new output initiatives. The Government has also put additional money into contingencies. As a result, the contingencies in this budget's forward estimates period are larger than in other recent budgets, providing scope for funding a larger value of new initiatives in future budgets without impacting on the estimates for total output expenses. 154

**FINDING 67:** Departments identified 91 initiatives that lapsed in 2014-15, representing over \$281.3 million of expenditure in 2014-15. Other initiatives apparently due to lapse in 2014-15 may not have done so because the funding was ongoing or because subsequent initiatives provided further funding. However, this is not always clearly stated in the budget papers, making it difficult to know what has happened with an initiative. 155

**RECOMMENDATION 46:** Future budget papers clearly state in the description of a new initiative if the initiative:

- (a) provides ongoing funding
- (b) provides additional funding for a previously released initiative. 155

**FINDING 68:** Key risks to the expenses estimates identified by the Government include salary increases and demand for services being higher than expected. Departments indicated that measures were in place to mitigate these and other key risks. 157

## 8 Asset investment page

**FINDING 69:** The Government's long-term financial management objectives contain references to infrastructure delivery. However, the 2015-16 Budget does not set a quantified target for asset investment over the medium term. 161

**RECOMMENDATION 47:** Future budget papers include a quantified target for infrastructure investment over the medium term. 161

**FINDING 70:** The High-Value and High-Risk Framework indicates that asset projects which are judged to be of high value and high risk should be subject to greater levels of oversight. Previous budget papers listed the projects that had been classified as high-value and high-risk. However, no equivalent list was included in the 2015-16 budget papers. 163

**RECOMMENDATION 48:** Future budget papers re-introduce the practice of listing all asset projects classified as high-value and high-risk. 163

**FINDING 71:** The Government expects to obtain additional resources in the future as part of the *Asset Recycling Initiative*. From 2015-16, these additional resources are expected to be obtained through the proposed lease of operations of the Port of Melbourne. 164

**FINDING 72:** The budget papers estimate that government infrastructure investment will peak in 2016-17 at \$6.5 billion and then be less in the last two years of the forward estimates period. Government infrastructure investment is expected to average \$5.3 billion per year between 2015-16 and 2018-19, which is slightly higher than the annual average of \$5.1 billion from 2007-08 to 2014-15. 165

**FINDING 73:** Asset investment has been overestimated in four of the six budgets between 2008-09 and 2013-14. The average variation between budget year estimates and actual expenditure has been an overestimation of \$499.9 million. 165

**FINDING 74:** The Government expects direct investment by departments and general government sector agencies to peak at \$6.2 billion in 2016-17, before declining to \$5.2 billion in 2018-19. As in previous years, the budget papers do not provide commentary explaining the year-to-year variations. 167

**RECOMMENDATION 49:** Future budget papers explain variations between individual years of the forward estimates period for direct investment ('purchases of non-financial assets') by the general government sector. 167

**FINDING 75:** Investment through other sectors ('net cash flows from investments in financial assets for policy purposes') is expected to decrease over the next four years in comparison to the investment made from 2007-08 to 2014-15. In two years of the forward estimates period, cash inflows are expected to exceed cash flowing out. In 2015-16, this is due to the proposed lease of the Port of Melbourne's operations. The budget papers do not explain the expected cash inflow of \$1.1 billion in 2017-18. 170

- RECOMMENDATION 50:** Future budget papers provide a detailed explanation for variances to any item of the budget estimates where the variance from one year to the next or from previous estimates is:
- (a) close to or over \$1.0 billion or
  - (b) more than 50 per cent for any item with a value over \$200.0 million. 170
- FINDING 76:** In contrast to earlier budget papers, this year's budget papers do not provide details of the projects being funded through this method. The budget papers do not distinguish between cash outflows and inflows for this line item, making it difficult to understand what the Government is providing to other sectors in some years. 170
- RECOMMENDATION 51:** Future budget papers re-instate the practice of disclosing the major projects funded by the general government sector through 'net cash flows from investments in financial assets for policy purposes', as was undertaken in past budgets. 170
- RECOMMENDATION 52:** Future budget papers disaggregate 'net cash flows from investments in financial assets for policy purposes' to specify cash outflows and cash inflows, as was undertaken in the *2013-14 Financial Report*. 170
- FINDING 77:** Estimates of expenditure by the private sector on the construction of public private partnership projects in 2016-17 and 2017-18 have been revised downwards since the last budget. This is primarily a result of the Government's decision to discontinue projects such as the *East West Link* and *Cranbourne-Pakenham Rail Corridor*. Explanations for changes in PPP infrastructure investment estimates are not provided in the budget papers each year, making it difficult for the Parliament and the community to understand changes to the estimates from one budget to the next. 173
- RECOMMENDATION 53:** Future budget papers include a reconciliation of 'public private partnerships infrastructure investment and other' estimates between the current and previous budgets, including explanations for any variances. 173
- FINDING 78:** Payments to service PPP projects are an important constraint that must be factored into the budget estimates. Government payments for PPP projects are expected to total approximately \$1.5 billion per year across the forward estimates period, except for 2016-17. These amounts are not disclosed in the budget papers each year. 175
- RECOMMENDATION 54:** Future budget papers disclose details of the expected Government payments on public partnerships projects over the forward estimates period and beyond, as reported by the Victorian Auditor-General's Office. 175
- FINDING 79:** Net direct investment for the public non-financial corporations sector is expected to be \$2.5 billion in 2014-15, with lower amounts across the forward estimates period. As with the general government sector, the budget papers each year do not provide explanations for variations in this line item across the forward estimates period for the public non-financial corporations sector. 176

- RECOMMENDATION 55:** Future budget papers explain variations between individual years of the forward estimates period for direct investment (‘purchases of non-financial assets’) by the public non-financial corporations sector. 176
- FINDING 80:** Government infrastructure investment adjusted for inflation and population growth is expected to decrease from \$858 per Victorian in 2015-16 to \$742 in 2018-19, though with a spike at \$1,031 in 2016-17. 177
- FINDING 81:** Government infrastructure investment figures have been revised downwards since the 2014-15 Budget for most years of the forward estimates period. According to the Department of Treasury and Finance, this is primarily driven by changes to major projects such as the cancellation of the *East West Link* and the *Cranbourne-Pakenham Rail Corridor* projects, and adjustments made to the proposed lease of the Port of Melbourne’s operations. 178
- FINDING 82:** The value of new asset initiatives released in each budget has been significantly higher in the last three budgets than in earlier budgets. This has been primarily a result of several particularly large projects. However, the largest projects released in the 2013-14 and 2014-15 budgets were discontinued with the 2015-16 Budget. 180
- FINDING 83:** Four new asset initiatives released in the 2015-16 Budget do not include full details of their total estimated investment or their expected expenditure in some years of the forward estimates period. In one case, no explanation is provided. 181
- RECOMMENDATION 56:** Future budget papers include explanations for all asset investment projects for which any details of the anticipated expenditure (including the total estimated investment) are marked ‘tbc’. 181
- RECOMMENDATION 57:** At the earliest opportunity, future budget papers provide details of the anticipated expenditure over the forward estimates period for any asset initiative from a previous budget where the anticipated expenditure in some future years was listed as ‘tbc’. 181
- FINDING 84:** Three transport-related projects make up the bulk of the new asset initiatives released in the 2015-16 Budget: the *Melbourne Metro Rail Project*, the *Level Crossing Removal Program* and *High-Capacity Metro Trains*. These three projects have a total estimated investment of between \$15.3 and \$18.3 billion. Each project replaces a similar project of the previous government. 185
- FINDING 85:** The 2015-16 Budget estimates include increased cash resources available to fund its asset investment without borrowings over the next four years. The increase is primarily a result of larger operating surpluses over the forward estimates period and cash inflows from investment through other sectors (as a result of the proposed lease of operations of the Port of Melbourne and expected receipts from the public financial corporations sector). 187
- FINDING 86:** Six asset projects were discontinued prior to the 2015-16 Budget. In some cases, alternative projects have been funded in the 2015-16 Budget. 189

<b>9</b>	<b>The Government's election commitments</b>	<b>page</b>
	<b>FINDING 87:</b> Of the 100 output commitments in <i>Labor's Financial Statement 2014</i> , at least 85 received funding in the 2014-15 Budget Update or the 2015-16 Budget. Of these, 79 commitments (totalling \$3.0 billion over five years) were fully funded and one commitment (for \$25.4 million over five years) has been partly funded. Five commitments (for \$174.3 million) have been funded, but the extent of the funding is not clear. Additional initiatives state that they provide funding for election commitments but it is not clear which, if any, of the commitments in <i>Labor's Financial Statement 2014</i> these relate to. The budget papers do not provide a clear connection between commitments made in <i>Labor's Financial Statement 2014</i> and the initiatives released in the budget papers in some cases.	196
	<b>RECOMMENDATION 58:</b> Future budget papers include a report forming part of the election commitments section of budget papers that shows:	
	(a) which election commitments (including output, asset and expenditure reduction commitments) have been funded to date	
	(b) which budget initiatives each election commitment has been funded through	
	(c) how much funding has been provided for each election commitment to date	
	(d) for commitments that have been partly or not yet funded, whether the Government intends to further fund the commitments and when further funding will be provided.	197
	<b>FINDING 88:</b> <i>Labor's Financial Statement 2014</i> indicates that \$1.9 billion of funding will come from expenditure reduction initiatives, the reprioritisation of existing resources and the use of existing funds. The budget papers state that \$1.5 billion has been provided from these sources in existing forward estimates. However, the budget papers do not provide further details.	199
	<b>FINDING 89:</b> Of the 61 asset commitments in <i>Labor's Financial Statement 2014</i> , 36 (with a TEI of \$3.6-4.0 billion) have been fully funded and 16 (with a TEI of \$2.4-2.6 billion) have been partly funded. The remaining nine commitments (with a TEI of \$175.4 million) have not yet received funding.	202
	<b>FINDING 90:</b> The funded commitments from <i>Labor's Financial Statement 2014</i> have not resulted in an increase in anticipated investment expenditure compared to the estimates in the 2014 Pre-Election Budget Update. Net expenditure on assets was expected to be \$10.8 billion between 2015-16 and 2017-18 in the 2014 Pre-Election Budget Update, while the 2015-16 Budget expects net expenditure to be \$7.5 billion over the same period, a reduction of \$3.3 billion.	203
	<b>FINDING 91:</b> The Government's election commitments included guarantees for a minimum of \$2.0 billion funding over eight years for roads in rural and outer suburban areas. This includes \$1.0 billion to be spent over the forward estimates period. The budget papers do not indicate progress towards compliance with the guarantees.	204
	<b>RECOMMENDATION 59:</b> Future budget papers include a list of the initiatives that contribute to the guaranteed minimum funding levels for:	
	(a) roads in Melbourne's outer suburban and interface communities	
	(b) roads and level crossings in rural and regional communities.	204



<b>10</b>	<b>Performance measurement</b>	<b>page</b>
	<b>FINDING 92:</b> All departments have indicated that they are currently developing corporate plans. The Department of Treasury and Finance’s guidance on long-term planning is currently under review and the development of long-term plans has therefore been paused.	210
	<b>FINDING 93:</b> There are 35 departmental objectives in the 2015-16 budget papers. This is a decrease of 11 objectives compared to the 2014-15 budget papers and 17 fewer than the 2011-12 budget papers (when objectives were first introduced). Only the Department of Environment, Land, Water and Planning noted the changes and provided explanations in the budget papers.	212
	<b>RECOMMENDATION 60:</b> Future budget papers include explanations for all modifications to departmental objectives, following the model of the Department of Environment, Land, Water and Planning in the 2015-16 budget papers.	212
	<b>FINDING 94:</b> There are 35 departmental objectives in the 2015-16 budget papers. This is a decrease of 11 objectives compared to the 2014-15 budget papers and 17 fewer than the 2011-12 budget papers (when objectives were first introduced). Only the Department of Environment, Land, Water and Planning noted the changes and provided explanations in the budget papers.	214
	<b>RECOMMENDATION 61:</b> Future budget papers include explanations for all modifications to departmental objective indicators.	214
	<b>FINDING 95:</b> The total number of outputs decreased by 17.9 per cent between 2009-10 and 2015-16, while the total cost of delivering outputs increased by 26.3 per cent. The Government has stated its intention to review outputs and performance measures.	216
	<b>FINDING 96:</b> Most outputs in the 2015-16 budget papers had at least one quality measure. However, there were eight outputs with no quality measures. These outputs have a total funding of \$531.8 million.	218
	<b>RECOMMENDATION 62:</b> The Department of Treasury and Finance ensure that all outputs from all departments in future budget papers include quality measures.	219
	<b>FINDING 97:</b> Quantity measures represent 45.2 per cent of the performance measures in 2015-16. However, there are five outputs without any quantity measures in the 2015-16 Budget. This includes four outputs from the Department of Treasury and Finance.	220
	<b>RECOMMENDATION 63:</b> The Department of Treasury and Finance ensure that all outputs from all departments in future budget papers include quantity measures. These quantity measures should relate to the same goods and services that are reported on by the other measures in the output.	221
	<b>RECOMMENDATION 64:</b> As part of the review of the performance measurement framework indicated by the Minister for Finance, the Department of Treasury and Finance establish guidelines to ensure that each output has an appropriate mix of quality, quantity, timeliness and cost performance measures.	221

**FINDING 98:** For many new initiatives, departments were able to detail the performance measures which will reflect the impact of the initiative in future years. For 41 new initiatives worth at least \$20 million (both output and asset initiatives), departments were unable to identify any associated performance measures other than output costs in the 2015-16 budget papers. 224

**RECOMMENDATION 65:** The Department of Treasury and Finance ensure that all initiatives (worth above \$20 million) in future budget papers have at least one associated performance measure other than output cost. 224

**FINDING 99:** The Government proposed discontinuing 258 non-cost performance measures with the 2015-16 Budget. The Committee has reviewed these performance measures and considers that 45 of these measures should be retained. 228

**RECOMMENDATION 66:** The Government not discontinue the measures listed in Table 10.4 of this report. 228

## 11 The Government's responses to the former committee's *Report on the 2014-15 Budget Estimates* page

**FINDING 100:** Of the six recommendations from the *Report on the 2014-15 Budget Estimates* that were supported or supported in principle, the Committee considers that three have been fully implemented, one has been partially implemented and one has not been implemented. It is too soon to tell whether or not one recommendation has been implemented. The one that has not been implemented related to the definitions included in Budget Paper No.4. 231

**RECOMMENDATION 67:** The Department of Treasury and Finance review previous recommendations made by the Public Accounts and Estimates Committee about the glossary in Budget Paper No.4 (*State Capital Program*) and improve the definitions. This should include not providing different definitions for terms that are used interchangeably. 231

**FINDING 101:** The current guidelines for responses to parliamentary inquiries date from 2002. The previous government intended to review the guidelines but this review appears not to have been completed. The former Public Accounts and Estimates Committee made a number of recommendations regarding matters that could be considered as part of the review. 232

**RECOMMENDATION 68:** The Government complete the review and update of the *Guidelines for Submissions and Responses to Inquiries*. As part of this review, the Government consider the recommendations of the previous Public Accounts and Estimates Committee outlined in Appendix A11.1 of this report. 232

## 1.1 Background

The Government introduced the 2015-16 appropriation bills into Parliament on 5 May 2015, seeking authority to release money for the 2015-16 financial year. The bills were passed by the Legislative Council on 25 June 2015.

Along with the appropriation bills, the Government tabled five budget papers, an overview document and four budget information papers. These documents detail the estimated finances for the next four years, along with the Government's intentions, strategies, economic assumptions and forecasts. The Department of Treasury and Finance also made available a series of online data sets with additional information.<sup>1</sup>

The *Parliamentary Committees Act 2003* requires the Public Accounts and Estimates Committee to inquire into the annual estimates in the budget papers each year.<sup>2</sup> This inquiry aims to:

- assist members of Parliament in their deliberation on the appropriation bills
- make recommendations which promote clear and full disclosure of the information contained in the budget papers
- provide members of Parliament with an improved understanding of the budget
- provide feedback on the performance measures that the Government has proposed discontinuing for 2015-16
- encourage economical, efficient and effective government administration.

In May, the Committee tabled an alert report that notified members of Parliament about the public hearings undertaken as part of this inquiry. This was intended to assist members in their deliberation on the appropriation bills.

This report presents the findings and recommendations of the Committee resulting from the Committee's examination of the 2015-16 budget papers.

## 1.2 Key findings and recommendations

This section identifies some of the key themes of the report, including several issues which appear in multiple chapters. These issues are discussed further in the relevant chapters.

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1 Department of Treasury and Finance, *Financial Data Sets 2015-16* (2015). Available at <[www.dtf.vic.gov.au/Victorias-Economy/Economic-indicators-and-statistics/Financial-data-sets](http://www.dtf.vic.gov.au/Victorias-Economy/Economic-indicators-and-statistics/Financial-data-sets)>, viewed 14 August 2015.

2 *Parliamentary Committees Act 2003* (Vic), s.14.

In some cases, recommendations have been included in this section. These recommendations are more general in nature and affect multiple areas of the budget papers. In other cases, more specific recommendations addressing the issues noted in this chapter appear in later chapters.

Links to the other chapters are provided in this section to help readers find more details on any particular issue.

## 1.2.1 The Budget at a glance

The budget papers estimate that the Government<sup>3</sup> will receive \$55.5 billion in revenue in 2015-16 and will spend \$54.3 billion delivering goods and services. This will leave it with a \$1.2 billion operating surplus in 2015-16.<sup>4</sup>

Between 2015-16 and 2018-19, the Government expects both revenue and expenses to grow. The budget papers estimate that revenue will grow faster than expenses, increasing the operating surplus to \$1.8 billion in 2018-19.<sup>5</sup>

The 2015-16 Budget announces 256 new initiatives to deliver goods and services, which are expected to cost \$9.2 billion over five years.<sup>6</sup>

The budget papers predict that asset investment will average \$5.3 billion per year over the next four years.<sup>7</sup> The budget announces new asset projects expected to cost between \$19.0 and \$22.0 billion to construct or acquire.<sup>8</sup> These include the *Melbourne Metro Rail Project*, the *Level Crossing Removal Program* and the *High-Capacity Metro Trains* initiative.<sup>9</sup>

According to the budget estimates, net debt will reduce from \$21.2 to \$16.9 billion during 2015-16, driven by the proposed lease of the Port of Melbourne's operations. The budget papers estimate that debt will increase in the following years, reaching \$19.8 billion in June 2019.<sup>10</sup>

All of these matters are discussed in more detail through this report.

**FINDING 1:** The budget papers estimate that there will be a \$1.2 billion operating surplus in 2015-16, rising to \$1.8 billion in 2018-19. The 2015-16 Budget includes \$9.2 billion of new initiatives to deliver goods and services and \$19.0-22.0 billion of new asset investment projects. The budget papers predict that net debt will be reduced in 2015-16 and then rise between 2016 and 2019.

<sup>3</sup> As represented by the general government sector – that is, departments and those agencies which do not fully recover costs (see further discussion in Section 2.2).

<sup>4</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.49.

<sup>5</sup> *ibid.*

<sup>6</sup> *ibid.*, p.57; Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

<sup>7</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.47.

<sup>8</sup> *ibid.*, p.60.

<sup>9</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), pp.36, 41-2.

<sup>10</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.61-2.

## 1.2.2 Limitations to the budget estimates

One key theme noted through the report is that, for a number of key budget items and economic variables, there have historically been regular variations between what is estimated in the budget papers and what actually occurs. These include:

- growth in the gross state product (adjusted for inflation), which has been consistently overestimated in past budgets (Section 3.5.2)
- population growth, which has been consistently underestimated (Section 3.5.2)
- the growth rate of revenue, which has been consistently underestimated (Section 4.3.2)
- the growth rate of output expenses (that is, the delivery of goods and services), which has been consistently underestimated (Section 7.3.1)
- the amount of asset investment in the budget year, which has been generally overestimated in previous budgets (Section 8.3).

In the case of revenue, evidence from departments indicated that the methodology used to make estimates may be partly responsible for the consistent underestimation. This methodology includes making conservative estimates and assuming zero for items where the amount to be received is uncertain (see Section 4.3.2).

Many factors are difficult to predict when preparing budget estimates. Practices such as conservative estimation may be prudent from a budget management perspective. The Committee does not have a view on whether or not the methodology adopted by the Department of Treasury and Finance is appropriate. The Committee notes that the Auditor-General reviews the budget estimates each year, including the methodology used to create them.<sup>11</sup>

However, the Committee considers that the inherent limitations of the budget estimates process should be more clearly disclosed. The budget papers each year do not include any discussion of the fact that key figures like revenue and expenses are consistently underestimated or that asset investment is generally overestimated. As a result, readers of the budget papers may misunderstand the nature of budget estimates, believing them to be accurate predictions of what will occur over the forward estimates period.

The Committee considers that known biases should be clearly stated and explained. In particular, where estimated future growth rates are compared to past actual growth rates, the budget papers should clearly indicate if the estimated growth rates for the item are generally underestimated or overestimated.

<sup>11</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.4-5.

As part of clarifying the limitations to the estimates, the Department of Treasury and Finance should consider the use of ‘fan charts’. In the United Kingdom, these have been used by institutions such as the Bank of England and the Office for Budget Responsibility to illustrate the level of uncertainty associated with forecasts.<sup>12</sup>

Fan charts are based on variations between past forecasts and actual figures. The variations are used to create ‘probability bands’, which show the likelihood of different degrees of variation.

The Office for Budget Responsibility indicates that:<sup>13</sup>

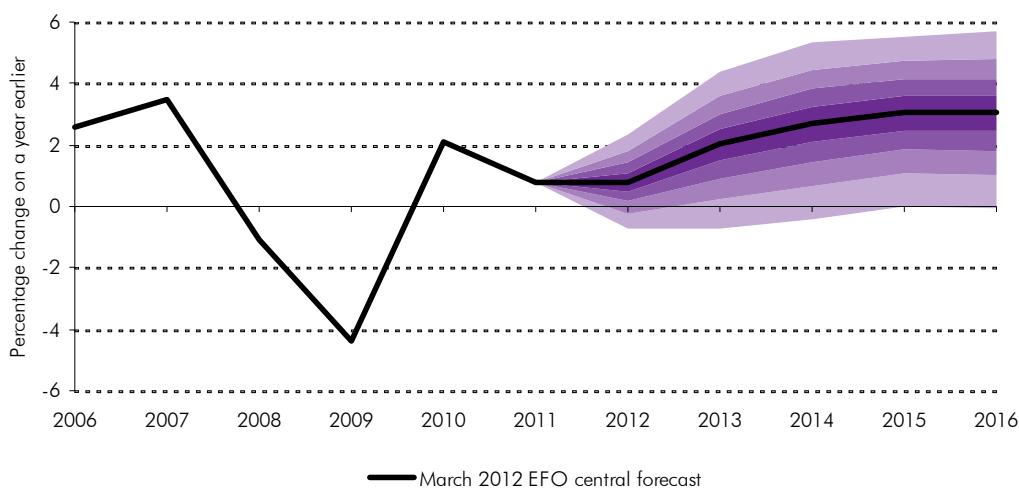
The uncertainty about the outcome of a variable – for example GDP growth or public sector net borrowing – can be represented by a probability distribution, which attaches weights to the likelihood of a range of different outcomes. Fan charts bring together a series of these distributions, each relating to a particular period of time.

...

The final fan charts do not represent our assessment of specific risks to the central forecast. Neither can they fully capture the extreme range of potential outcomes. We would usually expect forecast errors to fall within a reasonable band around our central forecasts, and the fan charts capture this general degree of uncertainty reasonably well.

Figure 1.1 shows an example of a fan chart for growth estimates of gross domestic product.

**Figure 1.1** Fan chart example (growth of gross domestic product)



Source: Reproduced from Office for Budget Responsibility, *Briefing Paper No.4: How We Present Uncertainty* (2012), p.10.

<sup>12</sup> House of Commons, *Economic Indicators, February 2015, Research Paper 15/06* (2015), pp.iv-v.

<sup>13</sup> Office for Budget Responsibility, *Briefing Paper No.4: How We Present Uncertainty* (2012), p.3.

The Office for Budget Responsibility explains that ‘the chart suggests, purely based on the evidence of past forecast errors, that there is only a 20 per cent probability of growth being between ½ and 1 per cent in 2012 or between 1½ and 2½ per cent in 2013’.<sup>14</sup>

Introducing fan charts into the Victorian budget papers would be one way for the Department of Treasury and Finance to more clearly indicate the level of certainty around key estimates in the budget papers.

**FINDING 2:** Previous budgets have consistently overestimated or underestimated a number of key items. These items include revenue, output expenses and the growth of gross state product. The budget papers do not discuss these variations, leaving readers of the budget papers unaware of the limitations in the Department of Treasury and Finance’s estimating methodology.

**RECOMMENDATION 1:** Future budget papers include a discussion about the tendencies to underestimate or overestimate certain items in past budget estimates, including both financial statement items and key economic assumptions. This discussion should include:

- (a) identifying the items which past budget papers have consistently underestimated or overestimated (considering the entire forward estimates period)
- (b) quantifying the variations between the actual results and the estimates for these items (across all years of the relevant forward estimates periods).

**RECOMMENDATION 2:** When future budget papers discuss the estimated future growth rates of items compared to past actual growth rates, the discussion clearly indicate if underestimation or overestimation of the estimates is likely to be a factor causing variances. This should apply to both financial statement items and key economic assumptions.

**RECOMMENDATION 3:** The Department of Treasury and Finance consider including ‘fan charts’ in the budget papers, showing the likelihood of different outcomes for key budget estimates based on past variances between forecasts and actual results.

### 1.2.3 Reporting comprehensively

The budget papers are an opportunity for the Government to set out its plans for the upcoming year, including its goals and how it intends to achieve them. This disclosure is important for the Parliament in considering the appropriation bills. It also informs the community about how the Government intends to spend public money.

At the end of the financial year, the information set out in the budget papers is essential for assessing the Government’s performance, as the actual results can be compared to the goals set in the budget papers.

<sup>14</sup> *ibid.*, p.10.

To fulfil these purposes, it is important for the information in the budget papers to fully and clearly describe what the Government intends to do. The Committee notes a number of areas where additional information is supplied in this year's budget papers compared to the previous year (see Section 2.6). This report also identifies a number of areas where the budget papers could be more comprehensive, including:

- of the four long-term financial management objectives, one is supported by medium-term targets while the others are not (Sections 2.3.2 and 8.2.1)
- varying levels of detail are provided about the different sources of government revenue, including differing details about the amounts expected, the intended purposes, the actual amounts received and the actual ways that the funding is used (Section 5.4)
- while the Government has provided a target for net debt in the general government sector, it has not provided an equivalent target for the public non-financial corporations sector, though that sector also has a significant level of debt (Section 6.3.1)
- in some instances, the specifications of the goods and services to be delivered do not include quantity or quality measures, making it difficult to fully assess performance (Section 10.3.4)
- for 41 major initiatives, no performance measures have been included in the budget papers to assess the success of the initiatives (Section 10.4).

Improving reporting in these areas would enhance the transparency of the Government's plans and facilitate accountability at the end of the year.

**FINDING 3:** The 2015-16 budget papers provide more information in some areas than previous budgets. The disclosure in future budget papers could be enhanced by providing further details about the Government's financial management objectives, sources of revenue, net debt targets and performance measurement.

#### 1.2.4 Connecting different parts of the budget papers

In total, the core budget papers contain over 900 pages of information spread across five volumes. A number of topics appear in more than one section, as different aspects of the topics are discussed, the topics are analysed in different ways or the topics are considered in a different context.

In many cases, there are clear links between these sections. However, there are some areas where connections could be improved. Similarly, there are cases where related topics are discussed in different places and it would be useful for the budget papers to make connections between the topics. Improving these sorts of connections is important for comprehensively discussing topics and helping readers to fully understand the information in the budget papers. The Committee recommends:

- linking the description of the medium-term financial management measures to the quantified targets for these measures (Section 2.3.2)



- disclosing the forecasts used in preparing the budget papers for all the items which the sensitivity analysis identifies as significant (Section 3.3.1)
- including all the key economic variables noted in the budget papers in the sensitivity analysis (Sections 3.3.1 and 3.3.2)
- discussing the relationship between the estimates of gross state product and the estimates of revenue (Section 4.3.1)
- in the discussion of revenue initiatives, noting any initiatives in other sections whose main effect is to lower revenue (Section 4.4.3).

The report also identifies ways that the linkage between the election commitments published in *Labor's Financial Statement 2014* and the initiatives in the budget papers could be made clearer (Section 9.2.7).

**FINDING 4:** The budget papers contain a large amount of information, spread across five core volumes. In some cases, connections between different parts of the budget papers could be improved to make the discussion of key topics more comprehensive.

**RECOMMENDATION 4:** The Department of Treasury and Finance review the budget papers to identify areas where the discussion could be improved by making cross-references to other parts of the budget papers.

## 1.2.5 Further explanation for changes

In addition to providing estimated financial statements, a key function of the budget papers is to explain how the estimates have been made and what they mean for Victorians. One of the Committee's main roles in examining the budget estimates is to identify areas where more explanation is needed. This report recommends that future budget papers include explanations for:

- variations between past actual growth rates and estimated future growth rates (Sections 4.3.1 and 7.3.1)
- significant variations between different years of the forward estimates period (Sections 4.5.3, 8.3.1 and 8.3.2)
- changes to the level of appropriations coming from annual and special appropriations compared to previous budgets (Section 5.3)
- variations to the estimates for net debt and asset investment between budgets (Sections 6.4.1 and 8.4)
- why some expenditure estimates cannot be provided for particular asset initiatives (Section 8.5.2)
- changes to departmental objectives and departmental objective indicators since the last budget (Sections 10.3.1 and 10.3.2).

The Committee considers that variations between past actual growth rates and estimated future growth rates are particularly important as these can reveal changes in policy, changes in the environment or limitations to the estimates

(see Section 1.2.2). The Committee considers that, wherever the estimated growth rate for an item varies from the past actual growth rate by more than 1 percentage point, this should be explained.

The Committee also notes that the budget estimates include over \$1.1 billion of cash being transferred between sectors in 2017-18. This had not been expected in earlier budget papers. No explanation for this transfer is included in the budget papers (see Section 8.3.1 of this report). The Committee considers that, as a rule, changes of this magnitude should be explained.

**FINDING 5:** A key function of the budget papers is to explain the basis for the estimated financial statements. The budget papers already contain much explanatory information, but the Committee has identified some areas where additional explanations would be helpful. The Committee considers that explaining variances between past actual growth rates and estimated future growth rates is particularly important.

**RECOMMENDATION 5:** Future budget papers include explanations for significant variances between past actual growth rates and estimated future growth rates for any item over \$100.0 million. A variance should be counted as significant when the future growth rate (between the budget year and the end of the forward estimates period) varies by greater than  $\pm 1$  percentage point from the growth rate across the last five years for which actual amounts are known.

## 1.3 The inquiry process

### 1.3.1 Questionnaires

The Committee sent two questionnaires to departments as part of this inquiry.

A general questionnaire (that is, a questionnaire containing a standard set of questions) was sent to all departments in May 2015. The questions related to:

- departmental strategic priorities
- the bases on which the budget was prepared
- spending plans
- expenditure reduction initiatives
- output and asset initiative funding
- public private partnership expenditure
- revenue, including Commonwealth Government grants
- performance measures
- staffing matters.

Departmental responses to this questionnaire were due on 12 June 2015.

A second questionnaire was sent to selected departments in July 2015. This included questions specific to each department arising from the budget papers. Departmental responses to this specific questionnaire were due on 7 August 2015.

The responses to both questionnaires can be found on the Committee's website ([www.parliament.vic.gov.au/paec](http://www.parliament.vic.gov.au/paec)).

### **1.3.2 Public hearings**

The Committee held public hearings from 8-22 May 2015 with all ministers and the Parliament's Presiding Officers. In total, the hearings lasted for 55 hours. The aim of the hearings was to provide an opportunity for ministers to present overviews of their portfolios and for the Committee to ask questions on the estimates for each portfolio.

As part of the inquiry process, the Committee tabled an alert report in May 2015 to assist members of Parliament to find information gathered during these hearings.<sup>15</sup>

Transcripts of the public hearings, slide shows of ministers' presentations and documents tabled in the hearings can be found on the Committee's website ([www.parliament.vic.gov.au/paec](http://www.parliament.vic.gov.au/paec)).

### **1.3.3 Questions on notice**

Ministers took questions on notice at the hearings for 24 portfolios (see Appendix A1.3). Ministers' responses can be found on the Committee's website.

### **1.3.4 Timeliness of responses**

Departments' and ministers' responses to the Committee's questionnaires and questions on notice are important sources of information for the Committee's analysis. It is therefore important that the responses are received early enough for the Committee to consider the content for the preparation of this report.

Appendix A1.1 lists the dates on which responses to the general questionnaire were received.

Appendix A1.2 lists the dates on which responses to the specific questionnaire were received.

Appendix A1.3 lists the dates on which responses to the questions on notice were received.

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15 Public Accounts and Estimates Committee, *2015-16 Budget Estimates Hearings Alert Report* (2015).

## 1.4 Machinery-of-government changes

A significant number of machinery-of-government changes took place after the election in November 2014. Changes were also made to ministerial portfolios and departmental structures.

### 1.4.1 Changes to portfolios

A number of ministerial portfolios were modified for 2015-16. The modifications included renaming, amending, adding, amalgamating, splitting and discontinuing portfolios. The resulting impact was a reduction from 49 portfolios at the time of the 2014-15 Budget to 40 with the 2015-16 Budget.

Appendix A1.4 compares the portfolios at the time of the 2014-15 and 2015-16 budgets.

### 1.4.2 Changes to departments

Figure 1.2 below compares the activities delivered by each department in the 2015-16 Budget and the 2014-15 Budget, based on the movement of performance measures for each department.

Other changes that are not reflected in the performance measures include the movement of CenITex from the former Department of State Development, Business and Innovation to the Department of Treasury and Finance,<sup>16</sup> and the creation of Emergency Management Victoria in 2014, with some responsibilities transferred to it from Victoria Police.<sup>17</sup>

## 1.5 Acknowledgement

The Committee acknowledges the contributions to this inquiry, including attendance at the public hearings, made by the Presiding Officers, Premier, Deputy Premier, Treasurer, Attorney-General, Ministers, Departmental Secretaries, heads of agencies and staff. The Committee thanks everyone involved for their effort in preparing responses to the questionnaires, attending the public hearings and responding to questions on notice.

## 1.6 Cost

The cost of this inquiry was approximately \$145,000.

<sup>16</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.130.

<sup>17</sup> Department of Treasury and Finance, *Budget Paper No.3: Service Delivery* (2015), p.382.

**Figure 1.2** Movement of responsibilities, 2014-15 Budget compared to 2015-16 Budget

OLD DEPARTMENT	NEW DEPARTMENT(S)			
Education and Early Childhood Development	Education and Training			
Environment and Primary Industries	Economic Development, Jobs, Transport and Resources	Environment, Land, Water and Planning		
Human Services	Health and Human Services	Premier and Cabinet		
Health	Health and Human Services			
Justice	Justice and Regulation	Premier and Cabinet		
Premier and Cabinet	Premier and Cabinet	Economic Development, Jobs, Transport and Resources		
State Development, Business and Innovation	Economic Development, Jobs, Transport and Resources	Health and Human Services	Premier and Cabinet	
Transport, Planning and Local Infrastructure	Economic Development, Jobs, Transport and Resources	Environment, Land, Water and Planning	Health and Human Services	Premier and Cabinet
Treasury and Finance	Treasury and Finance	Economic Development, Jobs, Transport and Resources	Premier and Cabinet	
Parliament	Parliament			
Courts	Courts			

Source: Public Accounts and Estimates Committee, based on performance measures as disclosed in Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2014-15 and 2015-16.



## 2.1 Introduction

This chapter provides an overview of the 2015-16 Budget. It examines the following questions:

- What are the key components of the Budget for 2015-16? (Section 2.2)
- What is the economic and political context for this year's budget? (Section 2.3)
- What are the budget estimates for the next four years? What do the key financial indicators show? (Section 2.4)
- What is the expected cost of new initiatives announced in this year's budget and how have they been funded? (Section 2.5)
- How are the budget papers structured? What has changed since last year? (Section 2.6)

Most of the topics in this chapter are discussed in more detail in the later chapters of this report.

## 2.2 Key components of the 2015-16 Budget

The public sector as a whole is divided into three parts:<sup>18</sup>

- the **general government sector**, which includes all departments and those government agencies that provide services with no charges or charges significantly below costs
- the **public non-financial corporations sector**, which consists of government-owned agencies that recover most of their costs through charges (such as water authorities)
- the **public financial corporations sector**, which includes government-owned agencies that provide insurance or financial services.

### 2.2.1 General government sector

The general government sector is the largest sector and the main focus of the budget papers.

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<sup>18</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), pp.210, 214, 245.

Figure 2.1 below illustrates the key components of the Budget for the general government sector in 2015-16 and how money flows from one component to another. Table 2.1 provides further details of the amounts and compares them to the previous year.

As the figure and table show, the **REVENUE** for the general government sector is expected to total \$55.5 billion in 2015-16, with 45.8 per cent of it coming from Commonwealth Government grants. The remainder comes from the State's own sources, such as payroll tax, land transfer duty and charges for services.

Most of this revenue is spent delivering goods and services, referred to in this report as **OUTPUT EXPENSES**.<sup>19</sup> These are expected to total \$54.3 billion in 2015-16.

The **OPERATING SURPLUS**<sup>20</sup> is the amount of revenue left after output expenses have been deducted. The operating surplus is expected to be \$1.2 billion in 2015-16, higher than the \$883.0 million estimated for 2014-15.<sup>21</sup>

The operating surplus is one source of cash which can be used for asset investment or for the repayment of borrowings. A number of other sources also provide cash for these purposes.

Some amounts are included in output expenses for accounting reasons but do not involve any transfer of cash (referred to as '**DEPRECIATION AND SIMILAR**' in this report<sup>22</sup>). As there is no transfer of cash, these amounts are still available from the total revenue to be spent by the Government. The budget estimates include \$2.5 billion of depreciation and similar within the output expenses for 2015-16.

Proceeds from **ASSET SALES**<sup>23</sup> also provide cash, with \$322.0 million expected in 2015-16.

In addition, the Government expects to receive \$6.5 billion from its **INVESTMENT THROUGH OTHER SECTORS**<sup>24</sup> in 2015-16, primarily from the proposed lease of the Port of Melbourne's operations.<sup>25</sup>

The Government expects these four sources of cash (the operating surplus, depreciation and similar, asset sales and investment through other sectors) to provide a total of \$10.6 billion in 2015-16. This is considerably more than the \$4.0 billion estimated for 2014-15, with the increase largely reflecting the proposed lease of the Port of Melbourne.

19 Referred to as 'expenses', 'operating expenses' or 'expenses from transactions' in the budget papers.

20 Referred to as 'operating surplus', 'net result from transactions' or 'net result from transactions - net operating balance' in the budget papers.

21 Actual figures for 2014-15 are not available at this time.

22 Referred to as 'non-cash revenue and expenses (net)' in the budget papers.

23 Referred to as 'proceeds from asset sales' or 'sales of non-financial assets' in the budget papers.

24 Referred to as 'net cash flows from investments in financial assets for policy purposes' in the budget papers.

25 This is a net figure for investment through other sectors. Cash outflows from the general government sector to other sectors for investment through other sectors have been subtracted from the cash inflows. In contrast to 2015-16, more cash usually flows outwards from the general government sector than inwards, making this a source of expenditure rather than cash in most years.



Figure 2.1 Key components of the 2015-16 Budget for the general government sector



(a) Includes some expenditure by the private sector on the construction of public private partnership projects.

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 10, 29; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.44, 59.

Some of this will be used to fund asset investment. The '**GOVERNMENT INFRASTRUCTURE INVESTMENT**' indicator measures the total expenditure by the general government sector on asset investment,<sup>26</sup> along with expenditure by the private sector on behalf of the government through the construction of public private partnership projects. The budget papers estimate that government infrastructure investment will be \$5.2 billion in 2015-16.

Some of the cash that remains after asset investment has been funded will be used to reduce the debt of the general government sector. The **DECREASE IN NET DEBT** is expected to be \$4.3 billion in 2015-16. This is the first time that net debt for the general government sector has decreased since 2005-06.<sup>27</sup>

**Table 2.1** Key components of the 2015-16 Budget for the general government sector, comparison to 2014-15

	2014-15 revised estimate	2015-16 Budget	Variance	Variance
	(\$ million)	(\$ million)	(\$ million)	(per cent)
<b>REVENUE</b>				
State-sourced	29,081.2	30,100.6	1,019.4	3.5
Commonwealth Government grants	24,461.2	25,428.1	966.9	4.0
Total revenue	53,542.4	55,528.7	1,986.3	3.7
<b>EXPENSES</b>				
Output expenses	52,659.4	54,309.8	1,650.4	3.1
<b>CASH RESOURCES</b>				
Operating surplus	883.0	1,218.9	335.9	38.0
Depreciation and similar	3,469.1	2,536.0	-933.1	-26.9
Asset sales	360.0	322.0	-38.0	-10.6
Investment through other sectors (net)	-719.5 <sup>(a)</sup>	6,510.8	7,230.4	-1,004.9
Total cash resources	3,992.6	10,587.7	6,595.2	165.2
<b>ANNUAL ASSET INVESTMENT</b>				
Government infrastructure investment	4,164.5	5,190.9	1,026.4	24.6
<b>REPAYMENT OF BORROWINGS</b>				
Decrease in net debt	-65.4 <sup>(b)</sup>	4,342.2	4,407.6	-6,739.4

(a) Negative amount indicates that more cash flowed from the general government sector to other sectors (to fund asset investment) than was received from those sectors.

(b) Negative amount indicates that net debt increased.

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 9, 10, 171, 225, 228, 247; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.44, 59; Department of Treasury and Finance, *Net Infrastructure Investment* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates)>, viewed 30 September 2015.

26 Including direct investment and investment through other sectors, less proceeds from asset sales and cash inflows from investment through other sectors (except for the Port of Melbourne).

27 Department of Treasury and Finance, *Consolidated Balance Sheet – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015.

As noted in Section 1.2.1 of this report, however, past budgets have consistently underestimated revenue and output expenses and generally overestimated infrastructure investment in the budget year. Past results suggest that there are likely to be significant variations between these estimates and the actual results.

**FINDING 6:** The budget papers estimate that an operating surplus of \$1.2 billion will be achieved in 2015-16. This is higher than the surplus of \$883.0 million estimated for 2014-15. The proposed lease of the Port of Melbourne's operations is also expected to facilitate a higher level of asset investment than the previous year and the first decrease in net debt since 2005-06.

## 2.2.2 Public non-financial corporations sector

As can be seen in Table 2.2, the public non-financial corporations (PNFC) sector is estimated to have revenue of \$9.6 billion in 2015-16 and expenses of \$10.1 billion. This leaves the sector with an operating deficit of \$523.4 million. This is part of a longer trend of this sector running a deficit, which is discussed further in Section 2.4.1 of this chapter.

**Table 2.2** Key components of the 2015-16 Budget for the public non-financial corporations sector, comparison to 2014-15

	2014-15 revised estimate	2015-16 Budget	Variance	Variance
	(\$ million)	(\$ million)	(\$ million)	(per cent)
Revenue	9,309.0	9,581.5	272.5	2.9
Output expenses	9,691.7	10,104.9	413.2	4.3
Operating surplus/deficit	-382.7	-523.4	-140.7	36.8
Net debt	14,908.2	15,559.6	651.4	4.4

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.49-51.

The PNFC sector also undertakes a significant asset investment program each year. The figures for this are not separately disclosed in the 2015-16 financial statements 'due to commercial sensitivities'<sup>28</sup> (which the Committee understands to be a reference to the proposed lease of the Port of Melbourne). Budget Paper No.4 identifies \$3.4 billion of expenditure on asset investment in 2015-16, compared to \$4.2 billion budgeted in 2014-15.<sup>29</sup>

Although the proposed lease will provide a significant cash inflow to the PNFC sector, this will be passed to the general government sector. Consequently, the sector's net debt is expected to increase in 2015-16 by 4.4 per cent to \$15.6 billion (see Table 2.2).

<sup>28</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.53.

<sup>29</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.16; Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), p.19. These figures are calculated on a different basis to the figures in the financial statements.

### 2.2.3 Public financial corporations sector

Table 2.3 presents the major estimates for the public financial corporations (PFC) sector. The PFC sector undertakes little asset investment and most of the debt it carries is on behalf of the other sectors, so those indicators have not been included.

**Table 2.3** Key components of the 2015-16 Budget for the public financial corporations sector, comparison to 2014-15

	2014-15 revised estimate	2015-16 Budget	Variance	Variance
	(\$ million)	(\$ million)	(\$ million)	(per cent)
Revenue	7,054.6	7,580.7	526.1	7.5
Output expenses	8,026.2	8,476.4	450.2	5.6
Operating surplus/deficit	-971.6	-895.7	75.9	-7.8
Net result	-882.6	586.9	1,469.5	-166.5

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.65.

The PFC sector is expected to have an operating deficit in both 2014-15 and 2015-16. However, the sector relies to a considerable degree on income from investments, which are not included in revenue or the operating surplus/deficit. These are factored into the net result, which is also included in Table 2.3. The PFC sector is expected to move from a negative to a positive net result between 2014-15 and 2015-16.

## 2.3 Budget setting and strategic directions

In his budget speech, the Treasurer indicated that the 2015-16 Budget was about 'jobs, schools, hospitals and transport'.<sup>30</sup> The Treasurer explained the Government's financial strategy to the Committee:<sup>31</sup>

Firstly, we have rebalanced the state's expenditure to ensure that all Victorians continue to ensure high-quality services, around health and education in particular. That is critical to addressing that shortfall in funding for services that we inherited. The pre-election budget update forecast that we would see expenses grow by just 2.5 per cent. We did not see that as sustainable and we moved necessarily to make appropriate adjustments. The budget begins to correct for that shortfall. We are moving up our operating expenses to 3 per cent.

<sup>30</sup> Department of Treasury and Finance, *Budget Paper No.1: 2015-16 Treasurer's Speech* (2015), p.1.

<sup>31</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.16.

The second part of the strategy is that we have continued to invest in historically high levels of infrastructure right across the state. The major projects agenda will sensibly invest in projects – the right projects at the right time, we like to say – and it will ensure that we improve those linkages between Victorians. Our general infrastructure spend is expected to average about \$5.3 billion over the budget forward estimates period, and that is well above the 10-year average of 4.9 billion. The budget, as you know, announced \$22 billion in terms of expenditure.

The third proposition is that we deliver surpluses of at least \$1 billion every year of the budget and forward estimates. Strong surpluses provide the cash required to invest in our services and pay down our debt.

Fourthly, we have funded 96 per cent of our 2014 output election commitments, and, fifthly, we are delivering low and declining net debt, consistent with maintaining our AAA credit rating. Solid financial fundamentals in the budget will place our budget estimates in a strong position for 19-20 and for 20-21 and going forward.

In summary, our finances are basically in a sound position. We are increasing investment in core services. We are investing in infrastructure at historically high levels. We are maintaining operating surpluses at about a billion dollars across the budget and forward estimates – over a billion dollars – and we are projecting net debt to decrease to 4.4 per cent by June 2019, the lowest for some time.

### 2.3.1 Economic context

The Government has indicated that it expects the Victorian economy to improve over the forward estimates period:<sup>32</sup>

- Positive signs for Victoria's economy have recently emerged as the national economy transitions to more balanced growth, assisted by low interest rates and a depreciated Australian dollar. Victoria's traditional growth drivers of household consumption and dwelling construction are strengthening, although labour income growth remains weak.
- Other structural shifts are presenting challenges for some industries as well as growth opportunities in new and emerging sectors. Victoria's industry structure is diverse and able to adapt to these changes. Structural adjustment is a long-standing characteristic of the Victorian economy.

In line with these expectations, the Budget has been based on assumptions that the economy<sup>33</sup> will grow at a faster rate than it has in recent years and that the unemployment rate will go down.<sup>34</sup>

Further discussion of the economic context of this year's budget and the accuracy of assumptions used in the budget papers can be found in Chapter 3 of this report.

<sup>32</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.17.

<sup>33</sup> As measured by gross state product (that is, the total value of goods and services produced by Victoria in a year) in real terms (that is, adjusted for inflation).

<sup>34</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.19-20.

### 2.3.2 Financial management objectives and targets

The Strategy and Outlook budget paper includes two sets of financial management goals:<sup>35</sup>

- long-term priorities
- medium-term measures.

The previous government similarly had long-term objectives and a medium-term strategy.<sup>36</sup> There are several elements in common but also a number of differences. The budget papers explain that, ‘The Government has reviewed the fiscal strategy to more closely align with its priorities to provide services and infrastructure for all Victorians in a fiscally responsible manner’.<sup>37</sup>

Table 2.4 compares the long-term priorities and objectives in the 2015-16 Budget with the objectives of the previous government.

**Table 2.4** Long-term financial management priorities and objectives, 2014-15 Budget and 2015-16 Budget

2014-15 Budget	2015-16 Budget
<p><b>Managing responsibly</b></p> <p>Victoria’s state finances will be managed responsibly to enhance the wellbeing of Victorians.</p>	<p><b>Sound financial management</b></p> <p>Victoria’s finances will be managed in a responsible manner to provide capacity to fund services and infrastructure at levels consistent with maintaining a triple-A credit rating.</p>
<p><b>Improving services</b></p> <p>Victoria’s public services will improve over time through enhanced efficiency and through a growing capacity of the Victorian economy to fund those services.</p>	<p><b>Improving services</b></p> <p>Public services will improve over time.</p>
-	<p><b>Building infrastructure</b></p> <p>Public infrastructure will grow steadily over time to meet the needs of a growing population.</p>
<p><b>Maximising community benefit</b></p> <p>Public sector resources will be allocated to those activities which generate maximum community benefit.</p>	<p><b>Efficient use of public resources</b></p> <p>Public sector resources will be invested in services and infrastructure to maximise the economic, social and environmental benefits.</p>
<p><b>Looking after the future</b></p> <p>The endowment of public sector wealth bequeathed by the current generation of Victorians to the next will be no less than the current generation inherited from the previous generation.</p>	-
<p><b>Managing the unexpected</b></p> <p>The State’s financial position will be robust enough to absorb and recover from unanticipated events, and to absorb the volatility inherent in revenues and expenses.</p>	-

Sources: Department of Treasury and Finance, *Budget Paper No.2: 2014-15 Strategy and Outlook* (2014), p.8; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

<sup>35</sup> *ibid.*, p.14.

<sup>36</sup> Department of Treasury and Finance, *Budget Paper No.2: 2014-15 Strategy and Outlook* (2014), pp.8-9.

<sup>37</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.13.

In both the 2014-15 and 2015-16 budgets, these high-level objectives were supported by shorter-term measures and targets (see Table 2.5).

**Table 2.5** Financial measures and targets, 2014-15 Budget and 2015-16 Budget

2014-15 Budget	2015-16 Budget
<p><b>Net debt</b></p> <p>General government net debt reduced as a percentage of GSP over the decade to 2022.</p>	<p><b>Net debt</b></p> <p>General government net debt as a percentage of GSP to be maintained at a sustainable level over the medium-term.</p>
<p><b>Superannuation liabilities</b></p> <p>Fully fund the unfunded superannuation liability by 2035.</p>	<p><b>Superannuation liabilities</b></p> <p>Fully fund the unfunded superannuation liability by 2035.</p>
<p><b>Operating surplus</b></p> <p>A net operating surplus of at least \$100 million and consistent with the infrastructure and debt parameters.</p>	<p><b>Operating surplus</b></p> <p>A net operating surplus consistent with maintaining general government net debt at a sustainable level over the medium term.</p>
<p><b>Infrastructure investment</b></p> <p>Infrastructure investment of 1.3 per cent of GSP (calculated as a rolling five-year average).</p>	-

Sources: Department of Treasury and Finance, *Budget Paper No.2: 2014-15 Strategy and Outlook* (2014), p.9; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

With the exception of the infrastructure measure, the measures are broadly similar between the two budgets. However, the Committee notes that the net debt and operating surplus targets are described in less precise terms than previously. Phrases such as ‘a sustainable level’ and ‘the medium term’ are open to multiple interpretations.

The targets are further specified in the Statement of Finances budget paper, which indicates that:<sup>38</sup>

- the target for net debt is ‘net debt as a percentage of GSP reducing from the commencement of the budget year to the end of the forward estimates period’
- the target for operating surpluses is ‘net operating surpluses in each year over the budget and forward estimates period’.

These targets are clear and measurable. However, they are included in a different budget paper to the financial objectives and measures. There is no mention in the discussion of the financial measures that further details about the targets can be found elsewhere. Moreover, their location is in a note to the financial statements that few people would look at. As a result, the Committee considers that most readers of the budget papers would not be aware of these quantified targets. Disclosure of these targets could be improved in future budget papers.

<sup>38</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.20.

Regarding the superannuation liabilities measure, the Committee notes that the target is to fully fund the unfunded portion of this liability by 2035. With no intermediate targets, it will be difficult in the medium term to understand whether or not the Government is on track to achieve its goal. Further discussion of this can be found in Section 6.3.2 of this report.

The discontinuation of the infrastructure target is discussed in Section 8.2.1.

The Committee also notes that the medium-term targets primarily relate to the 'sound financial management' long-term priority and not the other three long-term priorities. Greater clarity about the Government's intentions would come from introducing targets relating to the other priorities. This would also provide for greater accountability, as it would facilitate assessing the Government's performance compared to its objectives at the end of each financial year.

**FINDING 7:** The Government has established four long-term financial management objectives, which are supported by three medium-term measures. However, the quantified targets for two of these measures are disclosed in a different budget paper to the discussion of the financial management objectives and measures. In addition, the medium-term measures do not reflect all of the long-term objectives.

**RECOMMENDATION 6:** In discussing the Government's financial objectives and measures in future Strategy and Outlook budget papers, the discussion clearly note the existence of any relevant quantified targets in other parts of the budget papers, including Note 1 to the financial statements.

**RECOMMENDATION 7:** The Government expand its financial management targets to provide specific targets for all four of its long-term objectives.

### 2.3.3 Service delivery objectives and targets

Each year, Budget Paper No.3 provides details of the outcomes that the Government intends to achieve with its expenditure and how it intends to achieve them. This includes:

- departmental objectives identifying the impacts that the Government expects to have on the community
- performance measures establishing the quantity, quality, timeliness and cost of the goods and services that the Government expects departments to deliver to achieve the objectives.

These departmental objectives and performance measures are key means for the Government to communicate its intentions in a budget. They are also a key element of accountability, as departments are required to report each year on their actual performance compared to the targets and to explain significant variations.



Each year, changes are made to the objectives, indicators, performance measures and targets. These may reflect changes to government programs and priorities, administrative variations and refinements of the system.

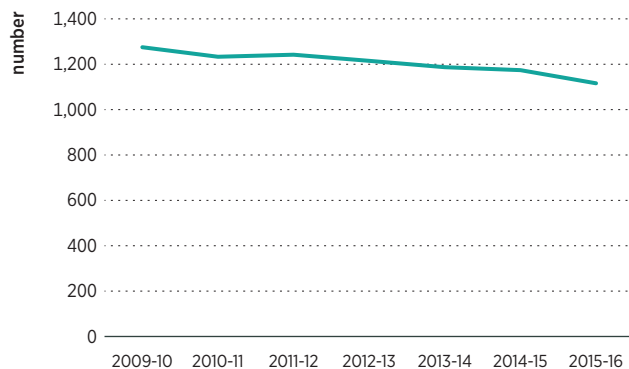
The 2015-16 budget includes a reduction in the number of departmental objectives from 46 to 35. Only 17 objectives remained unchanged between 2014-15 and 2015-16, with the rest modified, rearranged or discontinued. One new measure was introduced. The overall reduction continues a general tendency to reduce the number of objectives since they were introduced in the 2011-12 budget papers. Those budget papers included 52 departmental objectives. The budget papers do not explain the reasons for the changes in most cases.<sup>39</sup>

The changes to objectives are discussed in more detail in Section 10.3.1 of this report.

In relation to performance measures, this budget proposes discontinuing 285 of the 1,174 from 2014-15 (24.3 per cent). This is a larger discontinuation than previous budgets (over the previous four budgets, the number ranged from 92 to 225).<sup>40</sup>

A total of 227 new measures were created with the budget, leading to an overall proposed reduction of 58 measures (4.9 per cent).<sup>41</sup> This continues a trend of reducing the number of performance measures each year, which has been occurring for several years (see Figure 2.2).

**Figure 2.2** Number of performance measures applicable to each year, 2009-10 to 2015-16



Notes: Includes measures added in budget updates. Does not include measures recommended by the Committee for continuation in Chapter 10 of this report.

Source: Committee calculations based on Budget Paper No.3 each year and the relevant budget updates.

While welcoming a number of improvements that have been made to the performance measures with the 2015-16 Budget, the Committee has concerns about the discontinuation of some measures. These concerns and other issues related to performance measurement are discussed in Chapter 10 of this report.

<sup>39</sup> Committee calculations based on Budget Paper No.3 for relevant years.

<sup>40</sup> Committee calculations based on Budget Paper No.3 and Budget Updates for relevant years.

<sup>41</sup> *ibid.*

The Committee notes that the Minister for Finance has indicated that the Government intends to review the performance measurement system.<sup>42</sup> This is discussed further in Sections 10.3.3 and 10.3.4.

**FINDING 8:** Two of the key components of the performance measurement system are departmental objectives, which identify the intended impact of departmental activities on the community, and performance measures, which set the standards for the delivery of goods and services. The number of objectives has decreased from 46 to 35 since the last budget, while departments have proposed reducing the number of performance measures from 1,174 to 1,116.

### 2.3.4 Election commitments

As the 2015-16 Budget is the first budget released since the change of government in 2014, election commitments are a major theme. The budget papers include a report on the Government's progress at implementing its election commitments. It compares the funding provided in the 2014-15 Budget Update and the 2015-16 Budget to the commitments set out in *Labor's Financial Statement 2014*, which was published shortly before the 2014 State election (see Table 2.6).

**Table 2.6** Funding of *Labor's Financial Statement 2014* commitments

	Total value of commitments	Initiatives released in budgets to date <sup>(a)</sup>	Proportion of committed funding released in budgets
	(\$ billion)	(\$ billion)	(per cent)
Output initiatives	3.3	3.2	96
Expenditure offsets <sup>(b)</sup>	1.8	1.5	83
Asset initiatives	6.8	4.4	65

(a) Includes the 2014-15 Budget Update and the 2015-16 Budget.

(b) Includes expenditure reduction initiatives, reprioritisation of existing funding and the use of existing funds (such as the *Regional Growth Fund*).

Note: Various other qualifications are noted in Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.108.

Source: Adapted from Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.108.

The table indicates that most of the funding for output commitments has now been included in the budget estimates. The budget papers state that funding has been allocated for all of the initiatives scheduled to commence in 2014-15 or 2015-16.<sup>43</sup>

<sup>42</sup> Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.2.

<sup>43</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.108.

A smaller portion of asset investment funding has been provided to date. However, the budget estimates include significant amounts in the estimates for future years which could be used for these projects.<sup>44</sup> The budget papers state that, ‘The budget fully funds projects ready for implementation and work is under way to deliver the remainder of the Government’s election commitments’.<sup>45</sup>

*Labor’s Financial Statement 2014* indicated that funding the election commitments would have no impact on the operating surplus.<sup>46</sup> However, as discussed in Section 2.4.1 of this chapter, the operating surplus estimates in the 2015-16 Budget are significantly lower than had been predicted before the change of government.

This is because the election commitments make up only a small proportion of the new output and asset initiatives in the 2014-15 Budget Update and 2015-16 Budget (see Table 2.7).

**Table 2.7** Election commitments as proportion of new output and asset initiatives

	New initiatives released in 2014-15 Budget Update and 2015-16 Budget <sup>(a)</sup>	Election commitments released in budgets to date <sup>(a)(b)</sup>	Proportion of initiatives that are election commitments
	(\$ billion)	(\$ billion)	(per cent)
Output initiatives	9.7	3.2	33
Asset initiatives	19.0–22.0	4.4	20–23

(a) Five-year totals for output initiatives and total estimated investment for asset initiatives.

(b) Includes the 2014-15 Budget Update and the 2015-16 Budget.

Source: Committee calculations based on Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), Appendix A; Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.60.

New output and asset initiatives are discussed further in Section 2.5 of this chapter and in Chapters 7 and 8 of this report. The Government’s election commitments are further discussed in Chapter 9.

**FINDING 9:** The Government states that 96 per cent of the output funding and 65 per cent of the asset funding promised in its election commitments have been included in the budget estimates. The budget estimates also include a number of initiatives that were not included as election commitments in *Labor’s Financial Statement 2014*.

<sup>44</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.35.

<sup>45</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.1.

<sup>46</sup> Victorian Labor, *Labor’s Financial Statement 2014* (2014), p.6.

## 2.4 The forward estimates, 2015-16 to 2018-19

### 2.4.1 Revenue and expenses

Table 2.8 shows the budget estimates for revenue and expenses for the general government sector and the PNFC sector across the forward estimates period. The operating revenue and expenses of the PFC sector have not been included, as these are a poor indicator of its performance. The PFC sector relies heavily on returns on investments, which are not included in operating revenue.

The Committee notes that estimates of revenue and expenses in the budget papers tend to be underestimated (see Sections 4.3.2 and 7.3.1) and that this effect tends to become more pronounced in the later years of the forward estimates period.

**Table 2.8** Revenue and expenses, general government and PNFC sectors, 2014-15 to 2018-19

	2014-15 revised estimate (\$ million)	2015-16 Budget (\$ million)	2016-17 estimate (\$ million)	2017-18 estimate (\$ million)	2018-19 estimate (\$ million)
<b>GENERAL GOVERNMENT SECTOR</b>					
Revenue	53,542.4	55,528.7	56,893.9	59,036.6	61,179.1
Output expenses	52,659.4	54,309.8	55,497.4	57,671.0	59,350.7
Operating surplus/deficit	883.0	1,218.9	1,396.5	1,365.6	1,828.4
<b>PNFC SECTOR</b>					
Revenue	9,309.0	9,581.5	9,603.1	9,842.9	10,165.0
Output expenses	9,691.7	10,104.9	10,082.7	10,223.7	10,535.7
Operating surplus/deficit	-382.7	-523.4	-479.5	-380.8	-370.7

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 49, 225.

For both sectors, revenue and expenses are forecast to grow over the forward estimates period and the operating surplus/deficit is generally expected to improve. However, the PNFC sector will remain in deficit throughout the forward estimates period.

The growth in revenue for both sectors is slower between 2015-16 and 2016-17 compared to the other years. For the general government sector, this is largely driven by Commonwealth Government grants, where reductions in some areas have occurred due to the transfer of some responsibilities to the Commonwealth Government as part of the National Disability Insurance Scheme.<sup>47</sup> For the

<sup>47</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.52; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.163; Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, pp.5-6.

PNFC sector, this is predominantly a result of the proposed lease of the Port of Melbourne's operations, as the revenue from the sales of goods and services by the Corporation are no longer included in the PNFC sector statement.<sup>48</sup>

Expenses for both sectors are similarly expected to grow by smaller amounts between 2015-16 and 2016-17 than between other years of the forward estimates period. In fact, for the PNFC sector, the budget estimates indicate lower expenses in 2016-17 than the previous year. This is also primarily a result of the proposed lease of the Port of Melbourne.<sup>49</sup>

The estimates suggest that the Government will meet its target of general government sector surpluses in every year (see Section 2.3.2).

The Committee notes that the estimated operating surpluses for the general government sector are significantly lower than the estimates included in the *2014 Victorian Pre-Election Budget Update* (the last estimates made before the change of government in 2014). The reduced estimates are largely a result of increased estimates for output expenses. The Treasurer explained to the Committee:<sup>50</sup>

The higher operating surpluses the previous government forecast were only achievable by restricting our expenditure growth to just 2.5 per cent on average a year. Taking into account inflation and population growth, this could not have been delivered without an appreciable impact upon the service delivery that Victorians need and require and I think deserve. A more sustainable level of expenditure growth at 3 per cent remains under our revenue growth of 3.4 per cent and delivers on our election commitments while ensuring essential services are not compromised.

The revision of output expenses is discussed further in Section 7.4.1 of this report.

### **Expenditure sustainability – general government sector**

Figure 2.3 illustrates two measures of expenditure sustainability:

- the operating surplus/deficit, which compares the amount of operating revenue<sup>51</sup> to the cost of delivering goods and services
- net lending/borrowing, which compares the amount of revenue to the cost of delivering services and some asset investment costs.<sup>52</sup>

48 Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.5.

49 *ibid.*

50 Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.2; cf. Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.45.

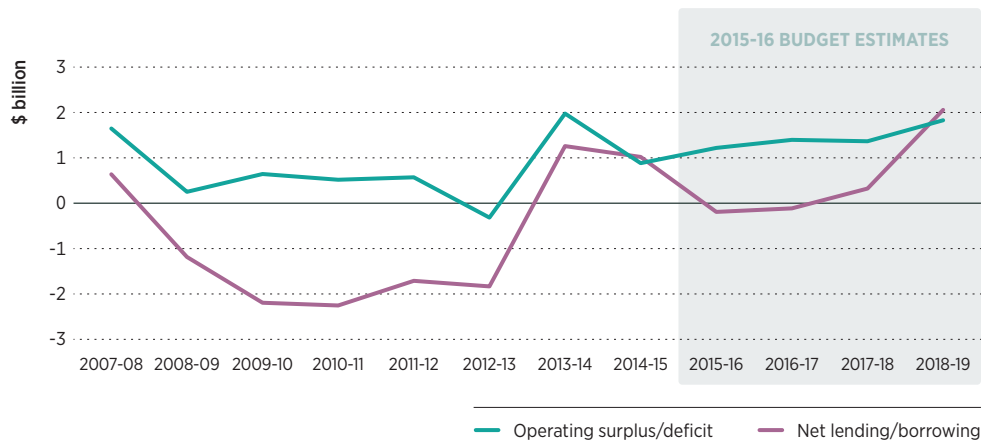
51 Operating revenue does not include some cash inflows, such as sales of assets.

52 Proceeds from asset sales and the full cost of direct asset investment in each year are included in net lending/borrowing, but not in the operating surplus/deficit. The total liability for each public private partnership project is included in net lending/borrowing in the year in which it is commissioned, even though actual payments will take place over a number of years. Cash inflows and outflows for investment through other sectors are not included in either the operating surplus/deficit or the net lending/borrowing.

The operating surplus/deficit is one of the Government’s financial measures (see Section 2.3.2). Net lending/borrowing is an indicator developed by the Australian Bureau of Statistics which is used by Moody’s Investors Service in analysing the Budget.<sup>53</sup>

Figure 2.3 places the forward estimates for both of these indicators for the general government sector in historic context.

**Figure 2.3** Operating surplus/deficit and net lending/borrowing, general government sector, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015.

Figure 2.3 shows that the forecast operating surpluses are higher than all years since the global financial crisis (2008) except for 2013-14 (when the surplus was inflated by the early receipt of Commonwealth grant payments, including for *East West Link*<sup>54</sup>).

Net lending/borrowing provides a better measure of whether the Government’s total expenditure can be funded by its revenue. Broadly speaking, a result above zero indicates that the Government has more revenue than it requires to fund expenditure (including asset investment) in that year. This is referred to as a ‘net lending’ position. A result below zero indicates that revenue without borrowings is not sufficient (referred to as a ‘net borrowing’ position).

Figure 2.3 also shows that the general government sector is expected to be a net borrower for the first two years of the forward estimates period and a net lender in the last two years. This change is driven by decreasing asset investment in the last

53 Moody’s Investor Service, *Announcement: Moody’s Comments on Victoria’s 2015/16 Budget* (2015).

54 Department of Treasury and Finance, *2013-14 Financial Report* (2014), pp.6, 140.

two years accompanied by increasing cash resources available.<sup>55</sup> Unlike the other years of the forward estimates, there is also no commissioning of public private partnerships included in the estimates for 2018-19.<sup>56</sup>

Asset investment and funding are discussed further in Chapter 8, while borrowings are discussed in Chapter 6.

**FINDING 10:** The budget estimates predict an improvement in the sustainability of the general government sector's finances, with increasing operating surpluses and a net lending position in the last two years of the forward estimates period.

### Expenditure sustainability – public sector as a whole

Figure 2.4 looks at the same indicators, but for the public sector as a whole<sup>57</sup> (which includes the general government sector, the PNFC sector and PFC sector). The operating surplus/deficit for the public sector as a whole follows a similar pattern to the general government sector, with a peak in 2013-14 followed by a decrease in 2014-15 and then an increase over the forward estimates period.

**Figure 2.4** Operating surplus/deficit and net lending/borrowing, public sector as a whole, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – Whole of State* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015.

However, the public sector as a whole is expected to be in deficit throughout the forward estimates period, in contrast to the general government sector. This is a result of the estimates for the PNFC and PFC sectors both being operating

<sup>55</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.8, 36; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>56</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>57</sup> Referred to as the 'State of Victoria' in the budget papers.

deficits throughout the forward estimates period.<sup>58</sup> In the case of the PFC sector, the Committee notes that its deficits will be more than offset by returns on investments, which are a major source of funds for that sector.<sup>59</sup>

The net lending/borrowing indicator for the public sector as a whole follows a similar pattern, but with large variations in 2012-13 and 2015-16. These reflect the commissioning of the Victorian Desalination Plant (in 2012-13) and the expected proceeds from the proposed lease of the Port of Melbourne's operations in 2015-16.

**FINDING 11:** The budget estimates for the public sector as a whole suggest improved financial performance across the forward estimates period. However, the public sector is expected to remain in an operating deficit throughout the forward estimates period and to be in a net borrowing position for all years except 2015-16.

### The impact of PNFC sector deficits

Looking at the operating deficit and other sustainability indicators for a number of self-funded entities, the Auditor-General has recently stated:<sup>60</sup>

A review of state entities that have been rated as high risk for each of the past five years indicates that many may not be able to set their fees and charges at a level that would enable them to generate enough revenue to meet their obligations as they fall due and ensure the long-term maintenance of their assets. In many cases, if these entities were to set their prices at a point that would allow them to do this, the community may not use the services available.

If these entities are to be financially sustainable over the long term, the underlying pricing model used to generate revenue may need amendment, another funding source may need to be found or additional government support may be required. The Department of Treasury and Finance should work with self-funded entities to try to find an appropriate balance between the fee-setting model and their ability to improve their long-term financial sustainability.

In response, the Government indicated:<sup>61</sup>

Often the pricing model, either for commercial or policy reasons, does not always allow these entities to fully recover depreciation. While operating commercially, most are sufficiently self-funding to cover direct cash operating costs but not sufficiently self-funding to fully provide for asset replacement or upgrading.

Fully or partially funding the depreciation costs would result in potentially large cash reserves being held for many years.

<sup>58</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.49, 65.

<sup>59</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.65.

<sup>60</sup> Victorian Auditor-General's Office, *Portfolio Departments and Associated Entities: Results of the 2013-14 Audits* (2015), p.20.

<sup>61</sup> *ibid.*, p.135.



Decisions on whether and when the State wishes to fund asset replacement or upgrading or new asset acquisition for these entities is a future policy decision, which the State should make at the time the assets are required to be replaced or upgraded. Entities can seek funding as part of the annual budget process in the context of whole of government asset management and service delivery objectives and priorities.

In relation to the 2015-16 Budget, the budget papers note that most PNFC sector entities are expected to have operating surpluses across the forward estimates period. The budget papers indicate that the overall operating deficit for the sector is largely a result of VicTrack, which is expected to have an average deficit of \$460 million over the forward estimates period. According to the budget papers, the Government considers that VicTrack is sustainable excluding depreciation.<sup>62</sup>

The Committee notes that, overall, the budget estimates for the PNFC sector would be an operating surplus throughout the forward estimates period if depreciation costs were excluded.<sup>63</sup> Moreover, the general government sector is expected to make sufficient surpluses to more than cover the PNFC sector's deficits,<sup>64</sup> meaning that the general government sector would be able to fund the shortfalls if it wished to do so.

However, as discussed in Section 2.4.3 of this chapter, asset investment by the PNFC sector is expected to drop over the forward estimates period. In fact, the current estimates are lower than depreciation between 2016-17 and 2018-19, indicating that the level of expenditure may not be sufficient to maintain infrastructure at the same level as in the past. This is a potential concern which may suggest that there are difficulties with the existing system.

This is an area that the Committee will be watching through the forward estimates period.

**FINDING 12:** The Government has indicated that it is not always practicable for PNFC sector entities to recover all costs, including depreciation, through charges. The Government has indicated that additional funding can be provided from the general government sector. However, the levels of asset investment predicted for the PNFC sector are lower than the value of depreciation in some years of the forward estimates period.

## 2.4.2 Transactions between sectors

Considerable amounts of money flow between the three different sectors each year. In response to the Committee's questionnaire, the Department of Treasury and Finance provided details about the flows that occur through the operating statement, which have been included in Appendices A2.1 and A2.2 and are summarised in Table 2.9.

<sup>62</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.69.

<sup>63</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.49.

<sup>64</sup> See the operating statement for the non-financial public sector, which consolidates both sectors – Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.57.

**Table 2.9 Transactions between sectors, 2015-16**

	To/from PNFC sector (\$ million)	To/from PFC sector (\$ million)
Amount going from the general government sector	3,291.3	1,727.8
Amount coming to the general government sector	3,143.6	1,298.3
Net amount going to other sectors	147.7	429.5

Source: Committee calculations based on Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.45-6.

### The PNFC sector and the general government sector

As Appendix A2.1 shows, it is anticipated that \$3,291.3 million will flow from the general government sector to the PNFC sector through operating expenses, mostly through grants and other transfers (\$2,943.0 million). This makes up 34.4 per cent of the PNFC sector's revenue estimates in 2015-16.<sup>65</sup>

In the same year, \$3,143.6 million is estimated to flow from the PNFC sector back to the general government sector. The majority of this (\$1,751.8 million) comes through the inter-sector capital assets charge. This is a charge based on 8.0 per cent of the written-down value of assets held by agencies.<sup>66</sup> The charge is intended to help agencies be more aware of the capital tied up in their assets and to encourage the sale of under-utilised assets by representing the opportunity cost of holding onto assets.<sup>67</sup> A further \$610.0 million is expected to flow from the PNFC sector to the general government sector through taxation, dividends, income tax equivalent revenue and local government rate equivalent revenue. These taxes and charges thus effectively recoup \$2,361.8 million, or 80.3 per cent of the funding passed to the PNFC sector as grants.<sup>68</sup>

However, the individual entities receiving grants may not be the same as the entities paying the taxes and charges. An important function of the system can be to redistribute money from some entities to others.

The other years of the forward estimates period are generally similar to the estimates for 2015-16 except for the purchase of services between the sectors. Both the provision of services to the PNFC sector and the purchase of services from the PNFC sector are estimated to decline substantially over the forward estimates period (see Appendix A2.1).

<sup>65</sup> Committee calculations based on Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.45-6; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.49.

<sup>66</sup> Department of Treasury and Finance, *BFMG - 12 Capital Assets Charge* (2009), p.68.

<sup>67</sup> *ibid.*, pp.68, 70.

<sup>68</sup> Committee calculations based on Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.45-6.

Primarily as a result of this, the budget estimates indicate that \$51.3 million more will flow from the PNFC sector to the general government sector than from the general government sector to the PNFC sector in 2018-19 (see Appendix A2.1). If this eventuates, it may place additional pressure on the PNFC sector's finances.

### The PFC sector and the general government sector

Appendix A2.2 shows that \$1,727.8 million is estimated to flow from the general government sector to the PFC sector in 2015-16. The majority of this (\$1,237.6 million) is interest payments, with the remainder (\$490.2 million) coming from the purchase of services.<sup>69</sup>

In 2015-16, \$1,298.3 million is estimated to flow from the PFC sector back to the general government sector. Taxation, dividends, income tax equivalent and rate equivalent revenue is expected to account for \$845.8 million of this. The remainder comes from interest and charges for services provided by the general government sector to the PFC sector.

The budget estimates assume that the amounts flowing between the PFC sector and general government sector will remain relatively stable across the forward estimates period. The largest change relates to a substantial reduction in dividends from the PFC sector (see further discussion in Section 4.5.3 of this report).

**FINDING 13:** Large amounts of money are expected to flow between the different parts of the public sector. In 2015-16, both the PNFC and PFC sectors will receive more from the general government sector than they give. However, the current budget estimates predict that, in 2018-19, the PNFC sector will provide more money to the general government sector than it receives. This is largely driven by an expected drop in the value of services purchased by the general government sector from the PNFC sector.

### 2.4.3 Asset investment

Table 2.10 shows the level of direct asset investment (less asset sales) for the general government sector and the PNFC sector across the forward estimates period. The 2015-16 figure for the PNFC sector primarily reflects estimated revenue from the proposed lease of the Port of Melbourne's operations rather than asset investment.

<sup>69</sup> Interest payments are a result of loans made on behalf of the general government sector by the PFC sector, for which the general government sector pays interest to the PFC sector, which then passes much of the money on to third parties. The purchase of services relates to the payments for services provided by the PFC sector to departments or agencies in the general government sector.

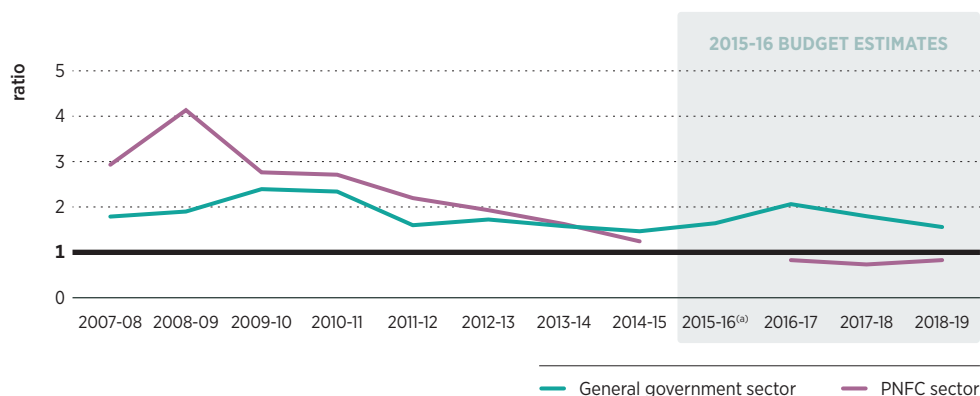
**Table 2.10** Direct asset investment less asset sales, general government and PNFC sectors, 2014-15 to 2018-19

	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
General government sector	3,658.1	4,229.7	5,612.7	5,173.2	4,900.3
PNFC sector	2,456.7	-4,423.6 <sup>(a)</sup>	1,851.3	1,654.9	1,959.6

(a) This primarily reflects proceeds from the proposed lease of the Port of Melbourne rather than spending on infrastructure.

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.10, 52, 228.

Figure 2.5 compares the estimated level of expenditure on assets to the amount required to maintain the current asset base (as indicated by depreciation). A ratio above 1 indicates that the Government is increasing the State's infrastructure. This is important to cater for Victoria's growing population and to provide up-to-date infrastructure. Additional infrastructure can also provide social and economic benefits to Victorians. A ratio below 1 means that new asset investment is not keeping up with the decline in the value of existing assets.

**Figure 2.5** Ratio of asset creation to asset use, general government and PNFC sectors, 2007-08 to 2018-19

(a) The 2015-16 figure for the PNFC sector has not been included, as it primarily reflects proceeds from the proposed lease of the Port of Melbourne's operations rather than spending on infrastructure.

Source: Committee calculations based on Department of Treasury and Finance, *Consolidated Cash Flow Statement – General Government Sector* and *Consolidated Balance Sheet – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.49, 52; Department of Treasury and Finance, *Financial Report, 2008-09 to 2013-14*.

Figure 2.5 shows that the ratio is expected to be above 1 throughout the forward estimates period for the general government sector. However, for the PNFC sector, the ratio is estimated at less than 1 between 2016-17 and 2018-19. The Committee notes that this is consistent with declining asset investment by the PNFC sector.

As discussed in Section 1.2.2, some budget estimates are not particularly reliable and underestimation may be a contributing factor in this instance. Nonetheless, this is a potential concern and the Committee will be watching the actual expenditure in future years. Possible difficulties with the PNFC funding model have been noted in Section 2.4.1 of this chapter.

As shown in Table 2.10 and Figure 2.5, asset investment for the general government sector is expected to peak in 2016-17. This is largely a result of estimated expenditure on health and transport projects. The budget papers indicate that expenditure in these areas is expected to rise between 2015-16 and 2016-17 and then drop off in the later years of the forward estimates period.<sup>70</sup> The budget papers do not indicate which particular projects this reflects (see further discussion in Section 8.3 of ways to improve disclosure).

**FINDING 14:** For the general government sector, the level of asset investment over the forward estimates period is expected to be more than required to maintain the infrastructure base. However, between 2016-17 and 2018-19, asset investment for the PNFC sector is expected to be less than required to maintain the asset base (as indicated by depreciation).

#### 2.4.4 Net debt

The forward estimates for the net debt of the general government sector and PNFC sector can be seen in Table 2.11.

**Table 2.11** Net debt, general government and PNFC sectors, 30 June, 2015 to 2019

	2015 revised estimate	2016 Budget	2017 estimate	2018 estimate	2019 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
General government sector	21,240.0	16,897.8	19,259.0	19,450.2	19,834.7
PNFC sector	14,908.2	15,559.6	15,972.6	16,082.7	16,391.5

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.9, 51.

As noted in Section 2.2.1, as a result of the proposed lease of the Port of Melbourne's operations, the Government intends to repay borrowings during 2015-16. This contributes to net debt declining from \$21.2 billion to \$16.9 billion during that year. Net debt is expected to increase to \$19.3 billion in the following year and then increase at a slower rate over the next two years, reaching \$19.8 billion in 2019.<sup>71</sup> This pattern reflects the budget assumptions that asset investment will peak in 2016-17 and that, in the following two years, asset

<sup>70</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.39.

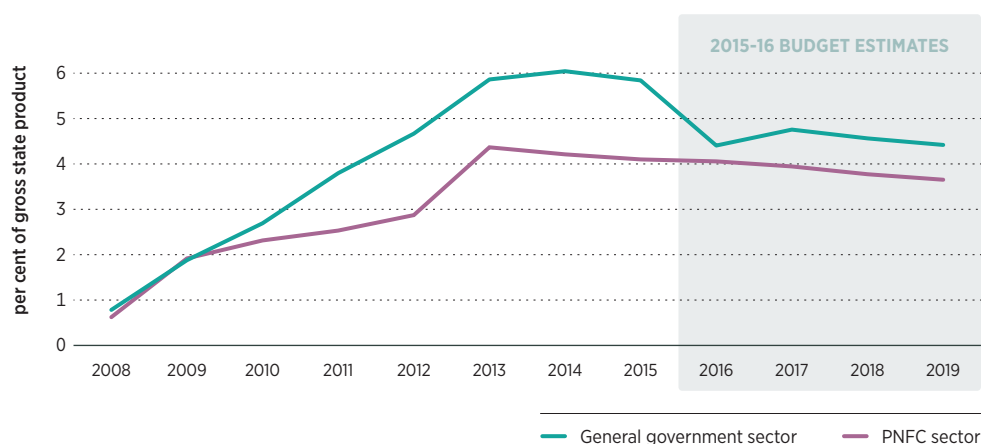
<sup>71</sup> *ibid.*, p.9.

investment will be less while cash resources will be greater (see Section 8.6 of this report).<sup>72</sup> It is also partly a result of plans to increase the balance of ‘cash and deposits’ over the forward estimates period.<sup>73</sup>

For the PNFC sector, net debt is expected to increase in each year of the forward estimates period, from \$14.9 billion in 2015 to \$16.4 billion in 2019.<sup>74</sup>

Figure 2.6 places the estimates in context by providing a longer time frame and comparing the net debt estimates to gross state product (GSP), that is, the total value of goods and services produced by Victoria in the year.

**Figure 2.6** Net debt as a proportion of gross state product, general government and PNFC sectors, 30 June, 2008 to 2019



Source: Committee calculations based on Department of Treasury and Finance, *Consolidated Balance Sheet – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015; Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 21 May 2015; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.51; Department of Treasury and Finance, *Financial Report, 2008-09 to 2013-14*.

Although net debt for the PNFC sector is expected to rise in dollar terms across the forward estimates period, it is expected to decline as a proportion of GSP. This is driven by estimates that, although both debt and GSP will grow, GSP will grow at a faster rate.

Similarly with the general government sector, the growth in GSP means that net debt will be 4.4 per cent of GSP in both 2016 and 2019,<sup>75</sup> despite increasing from \$16.9 to \$19.8 billion (see Table 2.11). The estimates indicate that the Government will meet its target of reducing net debt as a proportion of GSP between the start and the end of the forward estimates period (see Section 2.3.2), with net debt estimated to drop from 5.8 per cent of GSP in 2015 to 4.4 per cent in 2019.<sup>76</sup>

<sup>72</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>73</sup> *ibid.*, p.62.

<sup>74</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.51.

<sup>75</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.44.

<sup>76</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.62.

As Section 3.5.2 of this report discusses, however, previous budget estimates for GSP growth in real terms (that is, adjusted for inflation) have tended to be optimistic. If the current budget estimates are similarly optimistic, the decline in net debt as a proportion of GSP as indicated in Figure 2.6 may not be as rapid as indicated.

Debt and borrowings are discussed further in Chapter 6.

**FINDING 15:** Net debt for the general government sector is expected to reduce from \$21.2 to \$16.9 billion in 2015-16 following the proposed lease of the Port of Melbourne's operations. It is then expected to rise in each of the remaining years of the forward estimates period, reaching \$19.8 billion in 2019. However, as a proportion of gross state product, net debt will reduce between 2015 and 2019, in line with the Government's financial management target.

**FINDING 16:** For the PNFC sector, net debt is expected to increase in every year of the forward estimates period, from \$14.9 billion in 2015 to \$16.4 billion in 2019.

### 2.4.5 Assessments by the rating agencies

Victoria relies on two independent agencies for the State's credit rating: Standard & Poor's Financial Services and Moody's Investor Service. Both gave Victoria a triple-A credit rating at their most recent assessments (though Moody's last report was prior to the 2015-16 Budget).

In August 2015, after consideration of the 2015-16 Budget and other factors, Standard & Poor's re-affirmed its 'AAA/A-1+' rating with a stable outlook for Victoria.<sup>77</sup> This was based on:<sup>78</sup>

... the extremely predictable and supportive institutional framework benefiting state governments in Australia, plus the state's very strong financial management and economy, and its exceptional liquidity. The ratings also reflect Victoria's strong budgetary performance and low contingent liabilities. Victoria's average budgetary flexibility and its moderate debt burden partially offset these strengths.

Regarding the budget estimates, Standard & Poor's noted that:<sup>79</sup>

Although it is in a strong position, the 2015-2016 budget forecasts higher cash operating expenditure (3.8% higher from 2016-2018) than previously, reflecting the state government's election commitments to increase service delivery including higher staffing expenses (2.5% higher), which tend to be relatively inflexible and difficult to reduce, if needed. If costs are not controlled, it could put pressure on the state's budgetary performance and creditworthiness in the long run. Supporting this

<sup>77</sup> Standard & Poor's Ratings Services, *Research Update: Ratings On Australian State of Victoria Affirmed At "AAA/A-1+"; Outlook Remains Stable* (2015).

<sup>78</sup> *ibid.*, p.2.

<sup>79</sup> *ibid.*, p.3.

strong position are its small after-capital account deficits of 0.2% of total revenues over the same period,<sup>80</sup> and benefit from additional revenue following the long-term lease of the Port of Melbourne Corp.

Standard & Poor's also noted the Government's 'prudent approach to debt and liquidity management' but expressed its view that, 'the state's financial objectives and targets are not particularly onerous'.<sup>81</sup>

Moody's has not issued a ratings assessment since the Budget was tabled, but did publish some comments on the Budget. Moody's noted that the estimates for output expenses in the 2015-16 Budget were higher than previous estimates (see Section 2.4.1) and commented that:<sup>82</sup>

The lower [cash] operating balances provide less of a cushion should tax or GST-backed Commonwealth grants be less robust than forecast and the higher current spending base will prove more inflexible if reductions are required in future years. Given Victoria's ambitious capital improvement program – including significant investments in rail and road projects – the availability of operating surpluses will be critical to the state's ability to fund a greater portion of capital expenditures internally and for the achievement of projected targets for easing its debt burden.

However, Moody's also noted that, 'the higher spending rate also incorporates the setting aside of greater contingencies, an approach which is fiscally prudent'.<sup>83</sup>

## 2.5 Budget initiatives and their impact

Most of the Government's output expenses cover ongoing service delivery, such as schools, hospitals and the police. Each budget also includes a number of output initiatives, which are new projects or programs (or the continuation of previous initiatives for which funding has run out). Output initiatives are usually funded for a fixed period of time, between one and five years.

The new output initiatives released in this year's budget account for \$2.2 billion of expenses in 2015-16, or 4.1 per cent of the total output expenses.<sup>84</sup>

<sup>80</sup> Calculation based on figures developed by Standard and Poor's which are adjusted relative to the figures in the budget papers. These figures are on a cash basis, include capital expenditure as well as operating expenses and include both the general government sector and public non-financial corporations sector. The adjusted figures are published in Standard & Poor's Ratings Services, *Research Update: Ratings On Australian State of Victoria Affirmed At "AAA/A-1+"; Outlook Remains Stable* (2015), pp.5-6.

<sup>81</sup> Standard & Poor's Ratings Services, *Research Update: Ratings On Australian State of Victoria Affirmed At "AAA/A-1+"; Outlook Remains Stable* (2015), p.3.

<sup>82</sup> Moody's Investor Service, *Announcement: Moody's Comments on Victoria's 2015/16 Budget* (2015).

<sup>83</sup> *ibid.*

<sup>84</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.49, 58.



Budgets also include asset initiatives, which provide funding for new infrastructure projects. The projects released in this year's budget are expected to have a total cost of between \$19.0 and \$22.0 billion, with \$1.2 billion to be spent in 2015-16.<sup>85</sup>

These new initiatives are detailed in Budget Paper No.3.

### 2.5.1 New output initiatives

The 2015-16 Budget includes 256 output initiatives, with a total cost of \$9.3 billion across five years.<sup>86</sup> This is higher than recent budgets. This figure is in addition to \$367.5 million of initiatives released in the 2014-15 Budget Update (shortly after the change of government).<sup>87</sup>

The highest value new initiatives mostly relate to schools, TAFEs, hospitals, supporting the economy (including employment) and support for people with disabilities. Further details of the new initiatives can be found in Section 7.6 of this report.

Although the new output initiatives are expected to cost \$9.3 billion (of which \$9.1 billion is expected to be spent between 2015-16 and 2018-19),<sup>88</sup> it is not anticipated that expenses will increase by this much. The cost is expected to be offset by funding from:<sup>89</sup>

- reprioritisation of existing resources (which draws on funding previously allocated to departments, such as for other programs)
- the use of provisions included in previous estimates of the forward estimates period for expenses that had not been identified at the time those previous estimates were made (referred to in the budget papers as 'contingencies')
- expenditure reduction initiatives (new programs to reduce expenses, either by delivering services more efficiently or reducing the services delivered).

The impact of these measures is set out in Table 2.12.

As the table shows, most of the new expenditure in each year is funded from these sources. Overall, 71.8 per cent of the cost of the new initiatives is expected to be funded through these means across the forward estimates period.<sup>90</sup> The remainder of the cost, however, (the 'net impact') will increase expenses compared to the estimates made in previous budgets.

<sup>85</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.60.

<sup>86</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

<sup>87</sup> Committee calculations based on Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), Appendix A.

<sup>88</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

<sup>89</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

<sup>90</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

**Table 2.12** Impact of the new output initiatives in the 2015-16 Budget, 2015-16 to 2018-19

	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)
Cost of new output initiatives	2,231	2,176	2,358	2,359
Funded by				
• reprioritisation of existing resources	-490	-371	-332	-257
• use of contingencies <sup>(a)</sup>	-709	-951	-1,416	-1,689
• expenditure reduction initiatives	-72	-84	-91	-88
Net impact	960	770	520	325

(a) Contingencies are allowances made in previous budget estimates for the cost of initiatives which are funded in future budgets. New initiatives can be funded without impacting on the total expenses estimates by reducing the amount of contingencies. This figure includes amounts listed as 'adjustments' and 'contingency offset for new policy' in the budget papers.

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

Additional details about these funding sources can be found in Section 7.7 of this report.

**FINDING 17:** The 2015-16 Budget releases new output initiatives with a total estimated cost of \$9.3 billion over five years. Over the forward estimates period, 71.8 per cent of the cost of these initiatives is expected to be funded through the reprioritisation of existing resources, the use of contingency allowances put aside in previous budget estimates and expenditure reduction initiatives. The remaining cost will increase output expenses compared to previous estimates.

## 2.5.2 New asset initiatives

The 2015-16 Budget provides funding for 91 new asset investment projects. The total estimated cost for the entire construction or acquisition of these projects is between \$19.0 and \$22.0 billion.<sup>91</sup> This includes \$9.0-11.0 billion for the *Melbourne Metro Rail Project*, \$5.0-6.0 billion for the *Level Crossing Removal Program* and \$1.3 billion for *High-Capacity Metro Trains*.<sup>92</sup>

The new initiatives make up \$1.2 billion<sup>93</sup> of the \$5.2 billion estimated to be spent by the general government sector on asset investment in 2015-16.<sup>94</sup> The remaining \$4.0 billion includes projects released in previous budgets, upgrades, the replacement of operating assets and other asset investment that is not detailed in the budget papers.<sup>95</sup>

<sup>91</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.60.

<sup>92</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.36.

<sup>93</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.60.

<sup>94</sup> As measured by the 'government infrastructure investment' indicator – see Section 2.2.1 of this report.

<sup>95</sup> See Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.12 and Chapter 2.

As noted in Section 2.2.1, asset investment can be funded by the operating surplus, depreciation and similar, asset sales, cash inflows from ‘investment through other sectors’ and borrowings. Debt estimates are discussed in Section 2.4.4 and Chapter 6. More details about the funding of new and existing asset investment can be found in Section 8.6.

The Committee notes that the 2012-13 and 2014-15 budget papers included charts indicating the proportion of asset investment to be funded through cash and the proportion to be funded by debt.<sup>96</sup> The 2015-16 budget papers do not include an equivalent break-down in the chart indicating estimated asset investment.<sup>97</sup> The Committee considers that the break-down of how each year was expected to be funded in the 2012-13 budget papers<sup>98</sup> was useful and should be re-introduced in future budget papers.

**FINDING 18:** The 2015-16 Budget includes new asset initiatives with a total expected cost of \$19.0-22.0 billion. These, along with initiatives from previous budgets, will be funded by a mixture of cash resources and borrowings. The mixture was indicated in a chart in some previous budget papers, but this year is not indicated in this way.

**RECOMMENDATION 8:** The Department of Treasury and Finance include in future budget papers a chart indicating the proportion of each year’s infrastructure investment expected to be funded by cash and the proportion expected to be funded by debt in recent years and across the forward estimates period.

## 2.6 Structure of the 2015-16 budget papers

The Department of Treasury and Finance informed the Committee that the 2015-16 budget papers ‘are structured in a similar manner to the 2014-15 papers’.<sup>99</sup> As with the 2014-15 Budget, there are five core budget papers in 2015-16:

- the Treasurer’s speech (Budget Paper No.1)
- an outline of the budget strategy and outlook (Budget Paper No.2)
- details of new initiatives released in this budget; details of each department’s mission statement, objectives, outputs and performance measures; and a discussion of local government financial relations (Budget Paper No.3)
- information about infrastructure and other asset projects currently underway in the public sector, including both new and existing projects (Budget Paper No.4)

<sup>96</sup> Department of Treasury and Finance, *Budget Paper No.2: 2014-15 Strategy and Outlook* (2014), p.50; Department of Treasury and Finance, *Budget Paper No.2: 2012-13 Strategy and Outlook* (2012), p.37.

<sup>97</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.48.

<sup>98</sup> The Committee notes that the 2012-13 budget papers provided details for each year of the forward estimates period, while the 2014-15 budget papers only provided an average for the last three years of the forward estimates period. The Committee considers the year-by-year break-down to be preferable.

<sup>99</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.42.

- estimated financial statements with detailed notes for the general government sector; financial statements for the other sectors and for departments; and details of a variety of aspects of the State's finances (Budget Paper No.5).

There is also a Budget Overview document and four budget information papers, which bring together information from different parts of the core budget papers. Additional data are provided online in a number of spreadsheets, along with a video which 'provides an overview of the key initiatives'.<sup>100</sup>

In response to the Committee's questionnaire, the Department expressed its view that, 'There are no significant changes to the suite of core budget papers'.<sup>101</sup> The Committee conducted its own assessment of changes to the budget papers, which can be seen in Table 2.13.

The changes identified in that table do not include changes to the content as a result of changes in policy or the machinery of government.

**Table 2.13** Changes to the structure of the budget papers between 2014-15 and 2015-16

Chapter	Type of change	Details
<i>Budget Paper No.2: 2015-16 Strategy and Outlook</i>		
Chapter 2	Removal	The discussion of Victorian economic conditions no longer includes a short section on regional economies.
Chapter 3	Restructure	The chapter this year is focused on employment. Last year it discussed the economy more broadly.
Chapter 4	Restructure	The infrastructure investment chart now displays government infrastructure investment rather than net infrastructure investment. Each year of the forward estimates is now displayed separately rather than the last three years being averaged. The total amount of infrastructure investment is no longer broken down into the proportion funded by cash and the proportion funded by debt.
	Restructure	The reconciliation of estimates to the previous budget update has been restructured to provide the impact of each factor on the operating surplus rather than separately detailing the impact on revenue and expenses. Some items previously specified are no longer separately listed.
Chapter 5	Addition	In contrast to earlier years, last year's 'Application of Cash Resources for the Non-Financial Public Sector' table provided only aggregated information for 'net investment in fixed assets'. This year, the figure has been disaggregated in line with earlier years.
Appendix A	Addition	Charts have now been added for some variables, graphically displaying the impact on the operating surplus/deficit and net debt.

<sup>100</sup> *ibid.*

<sup>101</sup> *ibid.*

Chapter	Type of change	Details
<b>Budget Paper No.3: 2015-16 Service Delivery</b>		
Chapter 1	Removal	The 2014-15 budget papers, within the departmental tables of output initiatives, indicated for each department: <ul style="list-style-type: none"> <li>• the amount of funding for new initiatives to come from existing resources</li> <li>• the department's share of whole-of-government initiatives.</li> </ul> Although totals for these are still provided, the departmental break-downs are no longer supplied.
	Addition	Details have been added about asset election commitments which were not included as initiatives in the 2015-16 Budget but for which funding is held in contingency in the forward estimates.
<b>Budget Paper No.4: 2015-16 State Capital Program</b>		
Chapter 1	Removal	The previous budget papers included a list of the major projects classified as 'high-value and high-risk'. There is no equivalent in the 2015-16 budget papers.
	Addition	The table reconciling the 'government infrastructure investment' figure with other asset investment figures has been extended from only covering the budget year to including the full four years of the forward estimates period.
	Removal	This budget paper no longer lists the major projects contributing to asset investment through other sectors and the expenditure on each project in the budget year.
Definitions and Style Conventions	Addition	Extra terms have been added to the definitions.
<b>Budget Paper No.5: 2015-16 Statement of Finances</b>		
Chapter 1	Addition	Additional notes to the financial statements have been provided relating to: <ul style="list-style-type: none"> <li>• contingencies for output expenses and asset investment</li> <li>• break-downs of the 'other non-financial assets' and 'payables' balances.</li> </ul>
Chapter 2	Removal	The number of years of data has been reduced in the financial statements in Chapter 2, which no longer includes the last year for which actual figures are available.
Chapter 4	Removal	In discussing state taxation, last year's budget paper included descriptions of each major category of tax. This has not been repeated in 2015-16.
	Addition	Several boxes have been added discussing the longer-term context of various items of revenue.
	Addition	A new chart (Chart 4.3) has been added illustrating the contribution of the three major variables to the growth in GST revenue.
Chapter 5	Restructure	Table 5.3, comparing tax expenditure and tax revenue for the major categories of taxation, now refers to the budget year, whereas it was previously based on the year before the budget year.
	Addition	Additional detail has been added about changes to concession amounts and descriptions of key concession categories.
Appendix A	Removal	Within the table of Consolidated Fund receipts, 'cash inflows from investing and financing' have not been disaggregated this year.
Appendix B	Addition	Additional notes have been added to the revised estimates for 2014-15 and results for the first three quarters of 2014-15 detailing: <ul style="list-style-type: none"> <li>• a break-down of dividends received, indicating each paying entity and the amount paid</li> <li>• a break-down of the 'payables' balance</li> <li>• the 'application of cash resources' (that is, the impact of asset investment on net debt).</li> </ul>

Chapter	Type of change	Details
<b>Budget Overview</b>		
All	Restructure	The content has been considerably modified in line with changes to Government programs, projects and priorities. The overall length of the document has increased from 16 to 32 pages, though there is less text on most pages compared to last year.
<b>Budget Information Papers</b>		
All	Restructure	This year there are four budget information papers, compared to two last year, with new papers provided on 'putting people first' and 'suburban growth'. The structure and content of the papers has been changed considerably, with shorter budget papers with less text on the page compared to last year.

Source: Public Accounts and Estimates Committee.

The Committee considers that many of these changes are improvements. However, it believes that some of the changes have reduced transparency. These are discussed in more detail in the relevant chapters of this report.

**FINDING 19:** The core budget papers in 2015-16 are mostly structured in the same way as they were in 2014-15. Some additional details have been added which have increased transparency. However, some changes have decreased transparency in other areas.

# 3

## Economic overview

### 3.1 Introduction

The performance of Victoria's economy is one of the main determinants of how much money the Government collects from taxes, the level of expenditure on services, the level of asset investment and the amount of borrowings.

The 2015-16 Budget is based on economic forecasts relating to several elements of Victoria's economy, the national economy and the global economic outlook. These forecasts contain numerous assumptions about how the economy will develop over the next four years. The levels of revenue and expenditure in the budget year and forward estimates period are based on these assumptions. Any significant variations from these assumptions may result in changes to the State's forecast fiscal position. An understanding of these assumptions is therefore important for assessing the reliability of the budget estimates and the risks to those estimates.

In addition to the overall economy affecting the Government's budget, Government policies also impact on the economy. The Government has stated that it 'is acting immediately to implement its election commitments to rebuild a strong economy, improve economic growth and create jobs'.<sup>102</sup>

The 2015-16 budget papers contain a new chapter addressing the overall outlook of the Victorian labour market ('The Jobs Challenge')<sup>103</sup> and a number of Government policies and initiatives are designed to lift overall economic activity to support job creation.<sup>104</sup>

This chapter will discuss the following:

- What are the key economic variables influencing the budget estimates? What role does the Government play in the economy? (Section 3.2)
- What is the current economic outlook for Victoria? What is the current national and international outlook? (Section 3.3.1)
- What risks does the Victorian economy currently face? (Section 3.3.2)
- What are the prospects for the labour market in Victoria? (Section 3.4)
- How reliable are the Department of Treasury and Finance's forecasts? (Section 3.5)

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<sup>102</sup> Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), p.1.

<sup>103</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.27-41.

<sup>104</sup> *ibid.*, p.39.

## 3.2 Key economic variables

The Department of Treasury and Finance indicated to the Committee that a number of key economic variables impact on Government revenue (see Table 3.1).

**Table 3.1** Relationship between main economic variables and major revenue items in the budget

Economic variable	Impacted revenue items
Gross State Product (GSP)	All taxes are influenced by GSP
State final demand <sup>(a)</sup>	Insurance taxes
Household consumption	Gambling taxes; GST (national consumption)
Employment Growth	Payroll tax, gambling taxes
Consumer Price Index	GST, motor vehicle taxes, gambling and insurance taxes.
Wages Growth	Payroll tax, land transfer duty and gambling taxes
Housing prices	Land transfer duty
Interest rates	Land transfer duty
Population	All taxes are influenced by population

(a) A broad measure of the demand for goods and services in the economy.

Source: Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.32.

Based on predictions for these and other factors, the Budget anticipates that \$62.7 billion of revenue will flow into the Victorian public sector as a whole in 2015-16 (including Commonwealth grants).<sup>105</sup> This is equivalent to 16.3 per cent of the gross state product (GSP),<sup>106</sup> that is, the total value of goods and services produced in the year. The budget papers estimate that public sector revenue will increase in dollar terms to \$69.6 billion in 2018-19,<sup>107</sup> but decrease as a proportion of GSP, declining to 15.5 per cent.<sup>108</sup>

A similar pattern is expected for public sector expenses. These are expected to increase over the forward estimates period in dollar terms, from \$63.7 billion in 2015-16 to \$69.8 billion in 2018-19.<sup>109</sup> However, expenses are expected to decline as a proportion of GSP from 16.6 per cent in 2015-16 to 15.6 per cent in 2018-19.<sup>110</sup>

Figures 3.1 and 3.2 show the estimated trends for Victorian public sector revenue and expenses.

<sup>105</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.73.

<sup>106</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.20, 73.

<sup>107</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.73.

<sup>108</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.20, 73.

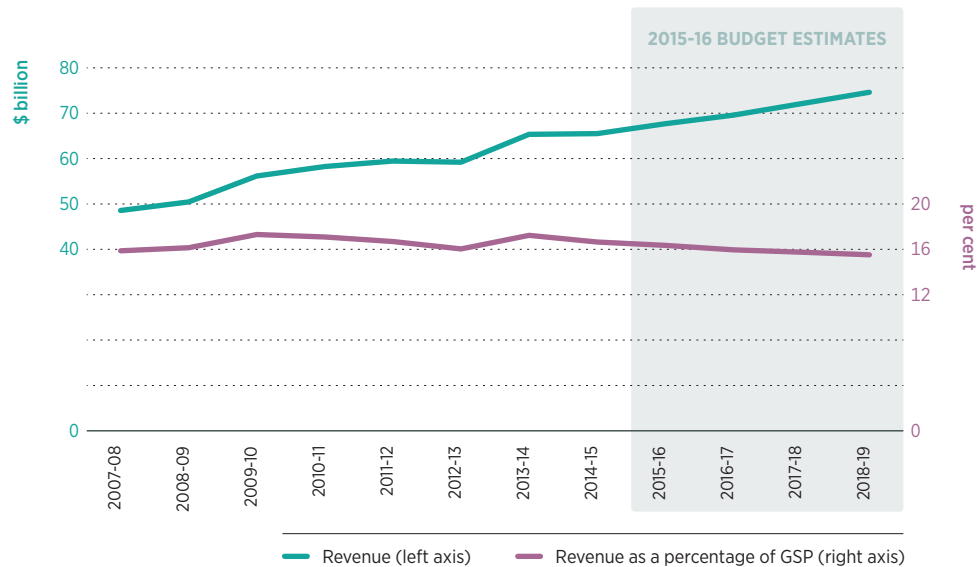
<sup>109</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.73.

<sup>110</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.20, 73.



The anticipated decrease of both revenue and expenses as proportions of GSP reflects the fact that the budget estimates assume that the economy will grow at a faster pace than revenue and expenses.

**Figure 3.1** Victorian public sector revenue<sup>(a)</sup> in dollars and as a proportion of GSP, 2007-08 to 2018-19



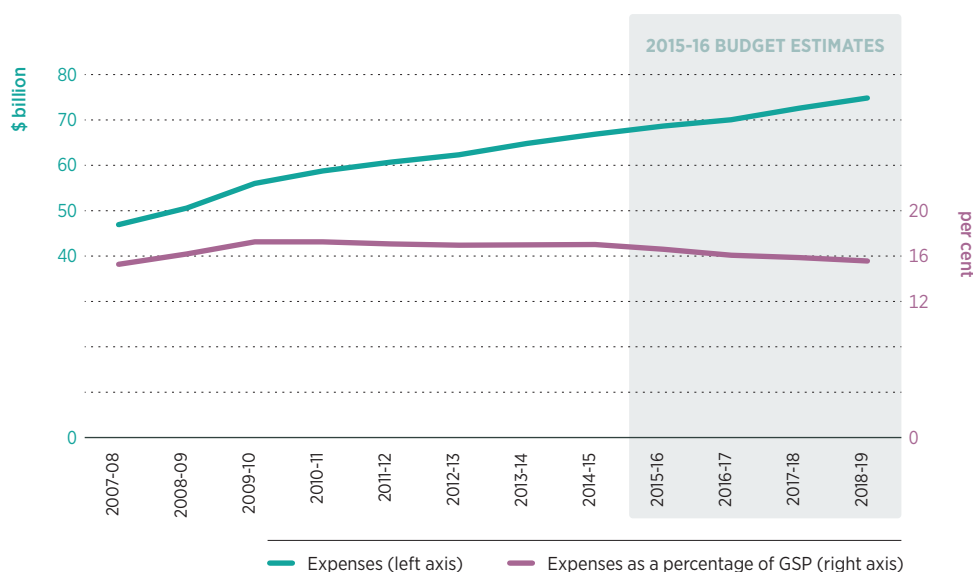
(a) Refers to the public sector as a whole (which includes the general government sector, the public non-financial corporations sector and the public financial corporations sector).

Source: Committee calculations based on Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 15 May 2015; Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement - Whole of State* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 15 May 2015.

The Committee notes, however, that figures for revenue and expenses have been consistently underestimated by past budgets (see Sections 4.3.2 and 7.3.1 of this report), while growth rates for GSP have been overestimated (see Section 3.5). The figures in this budget for revenue and expenses as a proportion of GSP may therefore be understated.

Factors impacting on revenue estimates are discussed further in Chapter 4 of this report and factors impacting on the estimates of output expenses are discussed in Chapter 7.

**Figure 3.2** Victorian public sector expenses<sup>(a)</sup> in dollars and as a proportion of GSP, 2007-08 to 2018-19



(a) Refers to the public sector as a whole (which includes the general government sector, the public non-financial corporations sector and the public financial corporations sector). Excludes infrastructure spending beyond the value of depreciation.

Source: Committee calculations based on Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 15 May 2015; Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – Whole of State* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 15 May 2015.

**FINDING 20:** Government activity in Victoria, measured by the expenses of the total public sector, is expected to account for 16.6 per cent of GSP in 2015-16 (\$63.7 billion) and 15.6 per cent in 2018-19 (\$69.8 billion). Similarly, public sector revenue is expected to change from 16.3 per cent of GSP (\$62.7 billion) in 2015-16 to 15.5 per cent in 2018-19 (\$69.6 billion). The decrease in revenue and expenses as a proportion of GSP reflects budget estimates that the Victorian economy will grow at a faster pace than public sector revenue and expenses.

### 3.3 Victorian economic outlook

The economic assumptions that go into the Budget aim to provide the Government with an outlook as accurate as possible to make informed decisions. As noted in Section 3.2, the budget estimates for revenue are influenced by a range of economic variables. The level of expenses, asset investment and debt are also influenced by these assumptions. If the economic assumptions turn out not to be correct, the likelihood of the budget estimates being inaccurate increases accordingly.

Within this context, a reasonable degree of accuracy for these assumptions is expected. Knowing these assumptions helps the Parliament and the community understand the reasonableness of the budget estimates and potential areas of risk where the estimated figures may be subject to higher variability.

### 3.3.1 The economic forecasts in the budget papers

The Government indicated in the 2014-15 Budget Update that it anticipated economic growth to remain below trend, primarily weakened by ‘the absence of a pick-up in business investment’.<sup>111</sup> The Government further explained that:<sup>112</sup>

The [Victorian] economy has experienced a period of subdued growth. Gross State Product [GSP] per capita has been effectively flat since the global financial crisis. The unemployment rate has reached 6.8 per cent, and total hours worked in the economy have remained virtually unchanged.

...

Since the 2014 Pre-Election Budget Update, forecast GSP growth for 2014-15 and 2015-16 has been downgraded, reflecting recent economic data which suggests that the transition back toward trend growth rates will be slower than previously forecast. This reflects relatively flat business investment, and modest growth in household consumption. In addition, the unemployment rate forecast has been increased in 2014-15 and in each year across the forward estimates.

The Government also indicated the challenges that the Victorian economy faces:<sup>113</sup>

Australia’s transition away from mining investment to other drivers of growth in the Australian economy could be slower than currently anticipated. Given the interstate trade links through the provision of goods and services, this could also reduce Victoria’s growth prospects. Victorian employment growth has been weak over the past two years, with the unemployment rate rising steadily to 6.8 per cent as more people look for work. Business investment has also been at relatively low levels as a share of GSP, as businesses defer investment pending signs of sustained growth in demand.

Following the 2014-15 Budget Update, the 2015-16 budget papers predict an overall positive economic environment for Victoria. This is primarily driven by low interest rates, a weaker Australian dollar and high population growth.<sup>114</sup> Nonetheless, similar to the 2014-15 Budget Update, the 2015-16 budget papers also signal current economic challenges, such as structural changes in the economy, heightened job security concerns, weak consumer expectations and a weak labour market.<sup>115</sup>

Table 3.2 shows the Victorian economic forecasts on which the 2015-16 Budget is based.

<sup>111</sup> Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), p.7.

<sup>112</sup> *ibid.*, p.1.

<sup>113</sup> *ibid.*, p.7.

<sup>114</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.18.

<sup>115</sup> *ibid.*

The budget papers explain that ‘the key assumptions underlying the economic forecasts include: interest rates that follow movements in market expectations in the short term, and stabilise thereafter; a trade-weighted index<sup>116</sup> of 64.5; and oil prices that follow the path suggested by oil futures’.<sup>117</sup>

**Table 3.2** Victorian economic forecasts (annual percentage change)<sup>(a)</sup> used in the 2015-16 budget papers

	2013-14 actual	2014-15 forecast	2015-16 forecast	2016-17 forecast	2017-18 projection <sup>(f)</sup>	2018-19 projection
Real gross state product	1.7	2.25	2.50	2.75	2.75	2.75
Employment	0.6	2.00	1.50	1.50	1.50	1.50
Unemployment rate <sup>(b)</sup>	6.2	6.50	6.25	6.25	6.00	5.75
Consumer price index <sup>(c)</sup>	2.8	1.50	2.75	2.75	2.50	2.50
Wage price index <sup>(d)</sup>	2.7	2.75	3.25	3.50	3.50	3.50
Population <sup>(e)</sup>	1.9	1.8	1.8	1.8	1.8	1.8

(a) Per cent change in year-average compared with previous year, except for the unemployment rate and population.

(b) Year-average rate.

(c) Melbourne consumer price index.

(d) Total hourly rates are used, excluding bonuses.

(e) Per cent change over the year to 30 June. Forecasts are rounded to the nearest 0.1 percentage point.

(f) On the difference between forecasts and projections, see further discussion in Section 3.5.2 of this chapter.

Source: Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.19; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.20.

The Committee notes that the Budget predicts stable growth for the economy as a whole: between 2.50 per cent and 2.75 per cent each year. The unemployment rate is expected to gradually decrease from 6.25 per cent in 2015-16 to 5.75 per cent in 2018-19. The consumer price index is expected to stabilise around 2.50 per cent over the forward estimates period.

Budget Paper No.2 includes a sensitivity analysis which discusses the expected impact of some of these and other economic indicators being 1 percentage point higher than expected. The analysis indicates the impact on the Government’s revenue, expenses and debt levels.<sup>118</sup> For instance, if consumer prices increase by 1 percentage point more than expected between 2014-15 and 2015-16, revenue and output expenses in 2015-16 would increase by an additional \$219 million and \$71 million respectively.<sup>119</sup>

<sup>116</sup> This index reflects the importance of Australia’s major trading partners to Australian trade. It includes the average of the exchange rates of the Australian dollar with the major trading partners’ currencies.

<sup>117</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.19.

<sup>118</sup> *ibid.*, pp.77-88.

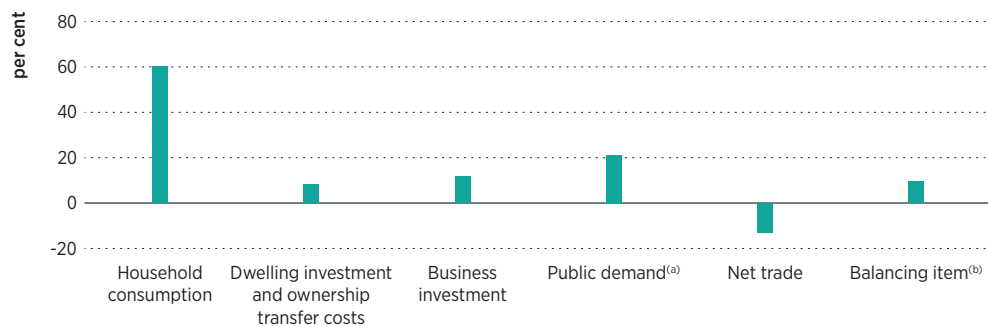
<sup>119</sup> *ibid.*, p.78.

According to the sensitivity analysis, variations in interest rates would have the largest impact on income from transactions in 2015-16 (\$227 million of additional revenue if interest rates are 1 percentage point higher than expected).<sup>120</sup> The Committee notes, however, that interest rate forecasts are not published in the budget papers (see further discussion later in this section).

### Real gross state product

Real gross state product (GSP) is a standard indicator to measure economic growth. GSP primarily consists of the sum of household consumption, dwelling investment and ownership transfer costs, business investment, government expenditure and the trade balance (the difference between the State's exports and its imports).<sup>121</sup> Figure 3.3 shows the proportions of these components. GSP in real terms refers to GSP adjusted to account for inflation.

**Figure 3.3** Share of GSP, 2013-14



(a) Includes public consumption and investment for all levels of government (that is, national, state and local).

(b) Includes net interstate trade in goods and services, changes in inventories and other miscellaneous components.

Source: Based on Department of Treasury and Finance, *State Budget Briefing* (2015). Available at <[www.vic.ipaa.org.au/news/latest-news/2015-state-budget-briefing](http://www.vic.ipaa.org.au/news/latest-news/2015-state-budget-briefing)>, viewed 24 July 2015; Australian Bureau of Statistics, *Australian National Accounts: State Accounts, 2013-14, cat. no.5220.0*. Available at <[www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/5220.02013-14?OpenDocument](http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/5220.02013-14?OpenDocument)>, viewed 24 July 2015.

The 2015-16 budget papers predict that the Victorian economy, measured by real GSP, will grow by 2.50 per cent in 2015-16. This compares to 1.70 per cent growth in 2013-14 and an estimated growth of 2.25 per cent for 2014-15.<sup>122</sup>

According to the 2015-16 budget papers, economic growth in Victoria will be driven primarily by household consumption and dwelling investment, which comprise approximately two-thirds of Victoria's GSP.<sup>123</sup>

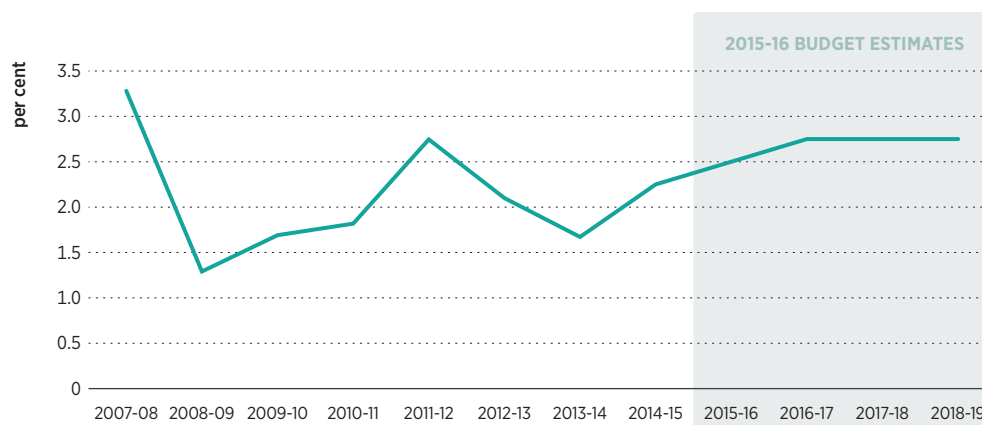
Figure 3.4 compares the current budget's forecasts for real GSP growth rates to the actual growth rates between 2007-08 and 2013-14.

<sup>120</sup> *ibid.*

<sup>121</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.2.

<sup>122</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.19.

<sup>123</sup> *ibid.*, p.18.

**Figure 3.4** Change in real gross state product (GSP),<sup>(a)</sup> 2007-08 to 2018-19

(a) Annual percentage change compared with the previous year.

Source: Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 13 May 2015.

The Committee notes that the budget estimates are framed around real GSP growth estimates that are larger than recent years. The budget papers predict an annual average growth rate of 2.7 per cent from 2015-16 to 2018-19, while the actual annual average growth rate from 2007-08 to 2014-15 has been 2.1 per cent (or 1.9 per cent if the particularly high growth rate in 2007-08 is excluded).<sup>124</sup>

**FINDING 21:** The Budget has been developed on estimates that gross state product will grow by 2.5 per cent (in real terms) in 2015-16 compared to the previous year and then by 2.75 per cent per year for the following three years. These are higher rates than have been seen in recent years. The 2015-16 budget papers indicate that economic growth over the next four years will be driven primarily by household consumption and dwelling investment.

The following sections examine the main components of GSP and their drivers.

### Employment

There are a number of ways to measure employment levels. The Department of Treasury and Finance forecasts employment levels by focusing on:<sup>125</sup>

- the labour market (that is, the demand and supply of labour)
- the number of employed people, which considers all the working population (aged 15 and over) who are employed for more than one hour a week<sup>126</sup>
- the unemployment rate, defined as the number of unemployed people as a proportion of the labour force<sup>127</sup>

<sup>124</sup> Committee calculations based on Department of Treasury and Finance, *Macroeconomic indicators* (2015), <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 13 May 2015.

<sup>125</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.9.

<sup>126</sup> Australian Bureau of Statistics, *Labour Force Australia, March 2015, cat. no. 6202.0*. Available at <[www.abs.gov.au/AUSSTATS/abs@.nsf/allprimarymainfeatures/4EA28ABBE8AFE477CA257E3D001197FB?opendocument](http://www.abs.gov.au/AUSSTATS/abs@.nsf/allprimarymainfeatures/4EA28ABBE8AFE477CA257E3D001197FB?opendocument)>, viewed 22 October 2015.

<sup>127</sup> The sum of people who work or are actively seeking work.

- the participation rate, which refers to the labour force as a proportion of the working age population.<sup>128</sup>

The Government predicts that labour market conditions will stabilise in 2015-16 and 2016-17. At the time of the 2015-16 Budget (May 2015), the Government indicated:<sup>129</sup>

Victorian labour market conditions have been weak over the past four years. The unemployment rate has risen and broader measures of spare capacity are at 20-year highs.

...

Since late 2014, the labour market has shown tentative signs of improvement. Employment growth has lifted markedly and the unemployment rate has edged lower, although it remains elevated.

...

The unemployment rate is expected to stabilise around its current level across 2015-16 and 2016-17 and is projected to ease thereafter as employment grows at trend and the participation rate moves lower.

The labour market is an area where the Government is seeking to have an impact through its policies. These are discussed in more detail in Section 3.4 of this chapter.

The Committee notes that the budget papers provide estimates for the unemployment rate and the number of employed people,<sup>130</sup> but not other labour market factors such as the underemployment rate, the underutilisation rate, the total numbers of hours worked and the youth unemployment rate. This is also discussed further in Section 3.4.

### Inflation and wages

The budget papers estimate that inflation will remain within the Reserve Bank's national target of 2.0-3.0 per cent over the forward estimates period. This expectation is primarily driven by an anticipated lower Australian dollar (compared to levels seen in recent years), improving conditions in the labour market and growing household consumption.<sup>131</sup> The annual inflation rate is expected to increase to 2.75 per cent in 2015-16, significantly higher than the 1.5 per cent estimated for 2014-15 in this year's budget papers.<sup>132</sup> The Government explains the change as influenced by the repeal of the carbon tax and low international oil prices.<sup>133</sup>

<sup>128</sup> Australian Bureau of Statistics, *Labour Force Australia, March 2015, cat. no. 6202.0*. Available at <[www.abs.gov.au/AUSSTATS/abs@.nsf/allprimarymainfeatures/4EA28ABBE8AFE477CA257E3D001197FB?opendocument](http://www.abs.gov.au/AUSSTATS/abs@.nsf/allprimarymainfeatures/4EA28ABBE8AFE477CA257E3D001197FB?opendocument)>, viewed 22 October 2015.

<sup>129</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.20.

<sup>130</sup> *ibid.*, p.19.

<sup>131</sup> *ibid.*, p.21.

<sup>132</sup> *ibid.*, p.19.

<sup>133</sup> *ibid.*, p.21.

In relation to wages growth, the budget papers assume that this will stabilise around an annual growth rate of 3.5 per cent over the forward estimates period.<sup>134</sup> The budget papers state that ‘annual wages growth has been historically low given elevated unemployment and constrained bargaining power of employees in seeking additional wage increases’.<sup>135</sup>

### Household consumption and dwelling investment

Household consumption is the amount spent by households on goods and services. It is primarily driven by labour income and household wealth as well as interest rates.<sup>136</sup> This component is expected to account for about 60 per cent of GSP in 2013-14.<sup>137</sup>

Dwelling investment includes the value of new dwellings and home improvements. The main factors influencing dwelling investment are the demand for new houses, population growth, interest rates and prices.<sup>138</sup> Dwelling investment accounted for around 6.2 per cent of Victorian GSP in 2013-14.<sup>139</sup>

The 2015-16 budget papers predict a positive outlook for both household consumption and dwelling investment, primarily driven by an expected stronger labour income (which would increase household wealth and consumption).<sup>140</sup>

The 2015-16 budget papers further indicate that:<sup>141</sup>

Positive signs have emerged in the State’s traditional growth drivers of household consumption and dwelling investment as the national economy shifts from growth led by mining investment to broader-based drivers. These are responding to low interest rates and strong asset price growth ...

...

Low interest rates, combined with high population growth, have increased demand in Victoria’s residential property market. Strong price growth among established dwellings is encouraging further residential construction.

Reduced interest payments and rising asset prices have strengthened household financial positions and supported consumer spending. In addition, lower petrol prices have bolstered household expenditure by allowing disposable income to be redirected towards other goods and services. However, the pick-up in consumption has come amid stalled growth in employee income, a result of subdued growth in wages and flat aggregate hours worked in the Victorian economy.

<sup>134</sup> *ibid.*, p.19.

<sup>135</sup> *ibid.*, p.21.

<sup>136</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.2.

<sup>137</sup> *ibid.*

<sup>138</sup> *ibid.*, p.3.

<sup>139</sup> *ibid.*

<sup>140</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.18.

<sup>141</sup> *ibid.*



The budget papers expect dwelling investment ‘to grow solidly in the short term, in line with recent strength in the established property market and supported by a surge in construction of multi-unit dwellings’.<sup>142</sup>

### Business investment

Business investment refers to activities related to investment by business in machinery, construction, intellectual property goods, raised livestock and agriculture.<sup>143</sup>

Business investment accounted for approximately 11.8 per cent of GSP in 2013-14.<sup>144</sup> It is driven mainly by interest rates, past business investment and the lending margin (that is, the cost of borrowing).<sup>145</sup>

The Government anticipates a favourable outlook for business investment over the forward estimates period after a period of stagnation since the global financial crisis. The budget papers indicate that:<sup>146</sup>

Despite improved business conditions, firms have been reluctant to invest. However, given low borrowing costs and a more favourable exchange rate, firms are predicted to increase their capital expenditure as consumer spending improves and exports strengthen.

### Government expenditure

The Department of Treasury and Finance defines government expenditure as the ‘activity generated by various levels of government (Commonwealth, state and local) within the economy through its consumption of goods and services and gross fixed capital formation (i.e. investment)’.<sup>147</sup> For forecasting purposes, the Department indicates that:<sup>148</sup>

[Government expenditure] is forecast by consideration of information affecting government revenue and expenditure. This may include, but is not limited to, policy announcements, election commitments, industry intelligence and financial information conveyed in both Commonwealth and state budget documents.

Other variables included in modelling government expenditure are population, employment in the public sector and the 10-year Commonwealth bond yield.<sup>149</sup>

<sup>142</sup> *ibid.*, p.20.

<sup>143</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.5.

<sup>144</sup> Committee calculation based on Australian Bureau of Statistics, *Australian National Accounts: State Accounts, 2013-14, cat. no.5220.0*. Available at <[www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/5220.02013-14?OpenDocument](http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/5220.02013-14?OpenDocument)>, viewed 24 July 2015.

<sup>145</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2014), p.5.

<sup>146</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.20.

<sup>147</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.6.

<sup>148</sup> *ibid.*, p.6.

<sup>149</sup> *ibid.*

The contribution of Victorian public sector expenditure to gross state product is discussed in Section 3.3.1 of this chapter. Output expenses are discussed in more detail in Chapter 7 and asset investment is discussed in Chapter 8.

### Trade balance

The difference between what is exported and what is imported is known as the trade balance. Exports and imports include both goods (for example, manufactured goods, food and minerals) and services (for example, education, tourism and financial services delivered in Australia to non-Australians).

According to the Commonwealth Department of Foreign Affairs and Trade, most of Victoria's exports of goods in 2013-14 came from food and fibre products and manufactured goods.<sup>150</sup> The Department of Treasury and Finance identifies the exchange rate and changes in relative prices (of exports to domestic sales) as the main factors influencing goods exports.<sup>151</sup> In the case of services, education and personal travel were the main exports in 2013-14.<sup>152</sup> Both services are consumed in Victoria, by people arriving in the State to study or for holidays.

In the case of imports, the largest categories of imported goods in Victoria are crude petroleum and passenger motor vehicles.<sup>153</sup> Variations are largely explained by global prices, the exchange rate and the relative cost of producing the goods domestically.<sup>154</sup> For services, the main service imported to Victoria is personal travel.<sup>155</sup>

Victoria's net trade balance was a deficit of \$38.2 billion in 2013-14.<sup>156</sup> The 2015-16 budget papers indicate that:<sup>157</sup>

Victoria's trade deficit is predicted to widen more slowly than over the previous decade. Exporters will benefit from the Australian dollar depreciating as well as accelerating demand for Victorian products from Asia. Imported goods and services, such as outbound tourism, will become relatively more expensive due to the lower exchange rate but growth is expected to rise broadly in line with state final demand.

<sup>150</sup> Based on Department of Foreign Affairs and Trade STARS database and ABS catalogues 3101.0, 5220.0, 5368.0, 5368.0.55.003 and 6291.0.55.001.

<sup>151</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.7.

<sup>152</sup> Based on Department of Foreign Affairs and Trade STARS database and ABS catalogues 3101.0, 5220.0, 5368.0, 5368.0.55.003 and 6291.0.55.001.

<sup>153</sup> *ibid.*

<sup>154</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.7.

<sup>155</sup> Based on Department of Foreign Affairs and Trade STARS database and ABS catalogues 3101.0, 5220.0, 5368.0, 5368.0.55.003 and 6291.0.55.001.

<sup>156</sup> *ibid.*

<sup>157</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.20.

### Disclosure of the assumptions in the budget papers

As previously noted, the GSP estimates in aggregate are disclosed in the budget papers. Additionally, the budget papers provide general commentary on the expected trends of the main GSP components over the forward estimates period. However, the budget papers each year do not provide any quantified forecasts of the main GSP components.

Given the relevance and potential impact of these variables and their assumptions within the budgetary process, the Committee considers that it would be informative for future budgets to provide forecasts for each of the GSP components. This would enable the reader to gain a better understanding of the assumptions underpinning the budget and to assess the reasonableness of these estimates.

**FINDING 22:** The budget papers each year do not provide quantified forecasts of the components of gross state product, making it difficult to assess the estimates of gross state product.

**RECOMMENDATION 9:** Future budget papers include a break-down of the forecasts of gross state product used in developing the budget estimates. This break-down should quantify the expected value of each of the main components of gross state product across the forward estimates period, including household consumption, dwelling investment, business investment and trade.

Other economic forecasts also play a significant role in determining the budget estimates. In response to the Committee's questionnaire, the Department of Treasury and Finance listed the factors that had the most significant impacts on revenue estimates (see Table 3.1 of this report).

The Department of Treasury and Finance's forecasts for some of these factors are disclosed in the budget papers but not all are disclosed. In particular, forecasts are not disclosed for:

- household consumption
- property prices
- interest rates.

Property prices and interest rates are also included in the sensitivity analysis in the budget papers. The sensitivity analysis estimates that a 1 percentage point variation from the forecasts for property prices would have a \$378 million impact on the operating surplus and a \$390 million impact on net debt over the forward estimates period. A similar variation from the estimates of interest rates would have a \$588 million impact on the operating surplus and an \$881 million impact on net debt over the forward estimates period.<sup>158</sup>

<sup>158</sup> *ibid.*, pp.78-9.

The Committee considers that these impacts are significant. However, without the Department of Treasury and Finance's forecasts for these factors being revealed, it is difficult for the Parliament and the community to assess whether or not these impacts are likely to occur.

The sensitivity analysis also identifies two other factors for which the forecasts are not revealed but where a 1 percentage point variation from the budget estimates would impact on the forward estimates period by more than \$100 million: property volumes and enterprise bargaining agreements.<sup>159</sup>

The Committee considers that the Department's forecasts should be disclosed for all factors for which variations may have a significant impact on the budget estimates. This would enable the Parliament and the community to assess the forecasts and develop informed views about the likelihood of variations from the forecasts occurring. A threshold to decide which economic variables have a significant impact on the budget estimates would be whether or not a 1 percentage point variance would impact on the operating surplus or net debt by more than \$100.0 million over the forward estimates period. If there is any variable meeting the threshold for which it is not appropriate to publish the forecasts, the reasons for this should be clearly explained in the budget papers.

**FINDING 23:** The Department of Treasury and Finance discloses six key economic forecasts in the budget papers each year. However, there are additional significant factors for which the Department does not disclose its forecasts. Without disclosure of the forecasts used in producing the budget estimates, it is difficult to assess the risks to the budget estimates that may come from variations in the forecasts.

**RECOMMENDATION 10:** Future budget papers publish the forecasts for the budget year and forward estimates period for any variable included in the sensitivity analysis for which a 1 percentage point variance would impact on the operating surplus or net debt by more than \$100.0 million over the forward estimates period. For any variable where this is not appropriate, the budget papers should state the reasons why the forecasts for this variable have not been published in the budget papers.

The Committee also notes that population growth and the unemployment rate appear in the budget papers as key economic assumptions on which the budget estimates have been based (see Table 3.2). However, the potential impact of variations from the forecasts in the budget papers is not discussed in the sensitivity analysis. As a general principle, the Committee considers that the sensitivity analysis should include all factors identified by the Department of Treasury and Finance as key economic assumptions, where appropriate. Alternatively, the budget papers should indicate the reasons why any key economic assumptions have not been included in the sensitivity analysis.

**FINDING 24:** Not all of the key economic assumptions on which the budget estimates have been based are included in the sensitivity analysis in the budget papers each year.

<sup>159</sup> *ibid.*

**RECOMMENDATION 11:** The sensitivity analysis in future budget papers include all variables listed in Note 1 to the financial statements as key economic assumptions (including population growth and the unemployment rate). For any variable where this is not appropriate, the budget papers should state the reasons why this variable has not been included in the sensitivity analysis.

### National and international economic outlook

The 2015-16 budget papers also include the following assumptions about the national economy:<sup>160</sup>

- improving economic growth, with an annual growth rate (in nominal terms) for gross domestic product of 2.6 per cent in 2014-15 and 3.1 per cent in 2015-16
- falling terms of trade (the ratio of export prices to import prices), lowering national income and potentially constraining consumer spending
- low interest rates stimulating the national property market, particularly in Sydney and Melbourne
- a low exchange rate (which could potentially increase the competitiveness of Victorian businesses<sup>161</sup>)
- the national labour market continuing to under-perform in the near term (particularly for the mining states).

In relation to the international economic outlook, the 2015-16 budget papers assume improving economic conditions in the United States, modest economic growth in China, a gradual recovery in the Japanese economy, a solid economic outlook for New Zealand, and modest economic growth in the eurozone.<sup>162</sup>

The Treasurer further explained to the Committee that:<sup>163</sup>

... the global economic outlook has moderated since the 2014-15 budget update due in no small part to the weaker growth prospects for the emerging economies, including China, Russia and Brazil ...

The IMF predicts global growth will rise marginally in 2015 and 2016. There are numerous risks to the global outlook – a prolonged downturn for the Chinese economy and the Chinese property market would limit construction growth and probably reduce demand for Australia’s mineral resources, leading to further declines in commodity prices and therefore an impact on terms of trade. A more rapid transition to consumer-led growth in China would likely boost Victoria’s exports. The risk of Greece exiting the eurozone I think resurfaced in early 2015, with management of the nation’s debt subject to ongoing deliberations. An exit would clearly unsettle equity markets and confidence, so that, together with the geopolitical tension in Ukraine and instability in the Middle East as well – the possibility that that might escalate all has an impact. A faster than expected recovery and a lift in interest

<sup>160</sup> *ibid.*, pp.22-4.

<sup>161</sup> *ibid.*, p.18.

<sup>162</sup> *ibid.*, p.25.

<sup>163</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, pp.27-8.

rates, particularly in the US, could lead to a further depreciation of the Australian dollar. This would more than deliver additional support for Victoria's trade-exposed industries and businesses and would likely see a more pronounced shift in household spending towards domestically produced goods and services. Prolonged weaknesses in global oil prices would, I think, keep petrol prices low, placing downward pressure on inflation and supporting Victoria's household consumption.

### 3.3.2 Economic outlook risks

Table 3.3 shows some of the economic risks which are discussed in the budget papers.

**Table 3.3 Risks to the economic outlook, 2015-16 Budget**

Risks	Potential impact on the Victorian economy	Impact of a one percentage point variance between estimates and actuals on the Budget <sup>(a)</sup>
Stronger-than-expected Australian dollar	Negative impact on: <ul style="list-style-type: none"> <li>Victorian business competitiveness</li> <li>business investment</li> <li>exports growth</li> </ul>	Not quantified
Lower-than-expected employment	Negative impact on: <ul style="list-style-type: none"> <li>labour income</li> <li>household consumption</li> <li>business investment</li> </ul>	Income from transactions: -\$62 million Expenses from transactions: \$2 million
Longer-than-expected period of low interest rates	Increase in: <ul style="list-style-type: none"> <li>asset prices</li> <li>household consumption</li> </ul>	Income from transactions: -\$227 million Expenses from transactions: -\$2 million
Lower-than-expected Chinese property market	Negative impact on: <ul style="list-style-type: none"> <li>mining exports growth for Australia</li> <li>commodity prices</li> <li>terms of trade</li> </ul>	Not quantified
Negative economic situation in Europe and increased geopolitical tensions around the world (for example, in the Ukraine and in the Middle East)	<ul style="list-style-type: none"> <li>financial market instability</li> </ul>	Not quantified
Rapid increase in global oil prices	<ul style="list-style-type: none"> <li>higher inflation</li> <li>lower household consumption growth</li> </ul>	Not quantified

(a) Based on the sensitivity analysis in Budget Paper No.2. Estimates in the sensitivity analysis indicate the impact of the particular variable being one percentage point higher than estimated. The budget papers indicate that in most cases the impact of the outcome being one percentage point lower than expected would be the opposite. Therefore, the Committee has reversed the impact shown in the sensitivity analysis to approximate the impact of these risks being realised.

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.26, 78.

The Committee notes that the 2015-16 budget papers also contain a brief discussion on the likely impact of the risks identified in Table 3.3 for some revenue items such as land transfer duty, land tax and payroll tax.<sup>164</sup> However, the discussion does not provide any quantified estimates of the potential impact of these risks on the Victorian economy or Government revenue. The Committee notes that only two of the identified risks are included in the sensitivity analysis in Budget Paper No.2.<sup>165</sup> The Committee considers that including those risks in the sensitivity analysis, where appropriate, would be valuable for understanding the potential impact of the risks that the Victorian economy currently faces.

**FINDING 25:** The 2015-16 budget papers identify a number of risks to the economic outlook. If they eventuate they would have a negative effect on the economy and consequently on the budget estimates. Only two of these risks are quantified in the sensitivity analysis in the budget papers.

**RECOMMENDATION 12:** Future budget papers quantify the impact of the main risks to the Victorian economy identified in the discussion in Budget Paper No.2 by including all of the identified risks in the sensitivity analysis. For any risk where this is not appropriate, the budget papers should state the reasons why this risk has not been included in the sensitivity analysis.

## 3.4 The labour market

As noted above, the Government has identified the labour market as a key area of the economy where it is seeking to make changes.

In relation to the current labour market outlook for Victoria, the Minister for Employment indicated to the Committee that:<sup>166</sup>

Over the past four years we have seen in Victoria a rise in the statewide unemployment rate from 4.9 per cent to 6.8 per cent, and there was a rise in the three-month average regional unemployment rate from 5.8 per cent to 6.6 per cent over that same four-year period.

...

Also troubling is this graph on youth unemployment and the rise in the youth unemployment rate over that similar period from 12 to 14.5 per cent.

According to the 2015-16 budget papers, the labour market in Victoria is 'constantly undergoing structural change as well as cyclical fluctuations'.<sup>167</sup> Recent trends show a change in the composition of employment from full-time jobs to part-time jobs. According to the Government, part-time jobs now represent

<sup>164</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.164, 166-9.

<sup>165</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.77-88.

<sup>166</sup> Hon. Jacinta Allan MP, Minister for Employment, *2015-16 Budget Estimates Transcript of Evidence*, 15 May 2015, p.3.

<sup>167</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.28.

one-third of total employment.<sup>168</sup> The budget papers state that ‘this reflects the level of full-time employment remaining broadly flat over the past four years’,<sup>169</sup> while the proportion of part-time jobs has increased.<sup>170</sup>

The 2015-16 budget papers discuss a number of labour market indicators, including:<sup>171</sup>

- the total number of hours worked by all workers (see Figure 3.5)
- the underemployment rate, which measures the number of people who have a job but are willing to work more hours (see Figure 3.6)
- the labour force underutilisation rate, which is defined as the sum of the unemployment and underemployment rates (see Figure 3.6).

**Figure 3.5** Annual hours worked in Victoria, 1980 to 2015



Source: Reproduced from Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.30.

Figure 3.5 shows that the total number of hours worked has fallen in recent years. The budget papers indicate that trends have differed across different industries, with negative trends for several industries in Victoria.<sup>172</sup> The impact on employment numbers and the participation rate has been mitigated by the shift to a larger proportion of part-time jobs.

<sup>168</sup> *ibid.*

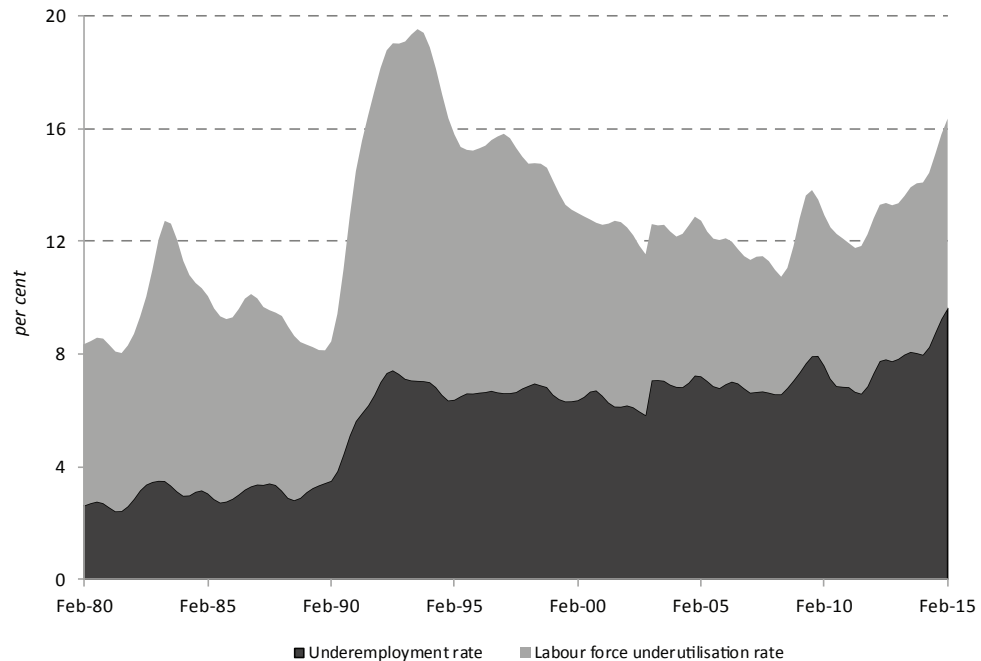
<sup>169</sup> *ibid.*

<sup>170</sup> *ibid.*

<sup>171</sup> *ibid.*, pp.30-2.

<sup>172</sup> *ibid.*, pp.31-2.



**Figure 3.6** Underemployment and underutilisation rates in Victoria, 1980 to 2015

Source: Reproduced from Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.32.

However, as can be seen from the underemployment rate, there are many employed people who would like to work more hours. The 2015-16 budget papers state that ‘Victoria’s underemployment rate (a measure of people who have a job and would like to work additional hours) rose to 9.6 per cent in February 2015’.<sup>173</sup>

Additionally, the 2015-16 budget papers also indicate the following trends for labour market indicators:<sup>174</sup>

- ‘Victoria’s unemployment rate rose to 6.9 per cent in July 2014, the highest recorded since October 2001 ...’
- ‘The labour force underutilisation rate (the sum of the unemployment and underemployment rates) increased to 16.4 per cent in February 2015, its highest level in over 20 years.’

The budget papers note that the youth employment rate has also decreased significantly since March 2012.<sup>175</sup>

The Minister for Employment indicated that another challenge for the labour market is the evolution of the economy. The Minister pointed out that:<sup>176</sup>

... not only do we have those challenges of an increasing unemployment rate, but there is also the issue of the transitioning of the economy. We have heard this a lot, workers have heard this a lot and businesses have heard this a lot. We do see the

<sup>173</sup> *ibid.*, p.32.

<sup>174</sup> *ibid.*, pp.29, 33.

<sup>175</sup> *ibid.*, p.33.

<sup>176</sup> Hon. Jacinta Allan MP, Minister for Employment, *2015-16 Budget Estimates Transcript of Evidence*, 15 May 2015, p.3.

reality of the fact that the nature and composition of the workforce is changing. We are taking an approach ... that we believe government has a role to play in not just being a commentator in the transition of the economy but in ensuring that the jobs of the future are there and that people have the skills to fill those jobs and the pathways to find those jobs.

Furthermore, the budget papers indicate that:<sup>177</sup>

... the Government is taking a series of actions that are geared towards lifting overall economic activity to support job creation by boosting confidence, encouraging new business formation, undertaking regulatory reform and improving linkages between people and jobs.

The 2015-16 budget papers contain the Government's response to the labour market situation. This includes the following programs:<sup>178</sup>

- the *Back to Work Scheme*, a \$100.0 million package delivered over two years providing 'financial assistance to businesses hiring those at risk of extended periods of unemployment, including young people and retrenched workers'
- the *Future Industries Fund*, with \$200.0 million delivered over four years to develop six growth industries identified by the Government (medical technology and pharmaceuticals, new energy technology, food and fibre, transport, defence and construction technology, international education and professional services)
- the Premier's Jobs and Investment Panel (an independent body of senior business and industry leaders), which 'will provide direct advice to the Premier on the allocation of \$508 million over five years for jobs and investment'
- the \$200 million *Regional Jobs Fund*, which will support job-creating projects in Regional Victoria.

As a result of these initiatives, the Government expects to help create 100,000 jobs over two years.<sup>179</sup> The Minister for Employment has stated that:<sup>180</sup>

We have set a target of creating 100,000 jobs. That is a very strong target. In particular you can see in the budget papers it does forecast some modest employment growth over the forward estimates. We recognise this, that there are those challenges that are forecast in employment rates, and how we need to pedal even harder – whether it is through our policy approaches or the program implementation in the *Back to Work* plan – to achieve job creation in the state.

177 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.39.

178 *ibid.*, p.40.

179 *ibid.*, p.27.

180 Hon. Jacinta Allan MP, Minister for Employment, *2015-16 Budget Estimates Transcript of Evidence*, 15 May 2015, p.3.

The budget papers also indicate that the Government is implementing policies in relation to the education and training system.<sup>181</sup> The actions described in the budget papers include:<sup>182</sup>

- investing significantly in education and skills, including a focus on reskilling workers;
- providing \$300 million to complete the \$320 million TAFE Rescue Fund, helping campuses across the state reopen closed buildings, upgrade workshops and classrooms and become more financially sustainable;
- providing young people and displaced workers with opportunities to develop the skills they need to get a job in the industries that will drive Victoria's future prosperity; and
- delivering community service obligations and enhancing the regulation of training providers.

The Committee notes that the labour market is only discussed from a retrospective point of view in the 2015-16 budget papers, except for the forecasts for the unemployment rate and employment growth. The Committee considers that it would be informative, as part of the Government's policy to improve labour market conditions, if forecasts and targets were published for each labour market indicator discussed in Chapter 3 of Budget Paper No.2 (that is, youth unemployment, the underemployment rate, the underutilisation rate and the number of hours worked). This information would provide the Parliament and the Victorian community with an understanding of the expected impact of the Government's policies on the labour market. In addition, these disclosures would be valuable for understanding the link between the labour market estimates and payroll tax estimates (see Section 4.4.2 of this report).

**FINDING 26:** The Government anticipates a more positive outlook for the labour market over the forward estimates period. It expects to positively influence the labour market over the next four years through funding a number of initiatives in the labour market, education and training areas. The Government has set a target of creating 100,000 jobs and provides forecasts for the employment and unemployment rates. However, it has not quantified the expected impact on other key measures of employment.

**RECOMMENDATION 13:** The Department of Treasury and Finance release forecasts and publish targets for the underemployment rate, underutilisation rate, the total number of hours worked and the youth unemployment rate.

**RECOMMENDATION 14:** The Government release regular reports to assess the progress and efficacy of the Government's programs to stimulate employment.

<sup>181</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.39.

<sup>182</sup> *ibid.*, p.40.

## 3.5 Economic forecasts

Economic forecasts are an important input into the Government's tax and spending policies. Inaccurate forecasts could potentially lead to misguided decisions with unfavourable results for the economy, the community and public sector finances.

### 3.5.1 The Department of Treasury and Finance's methodology

In Victoria, the Department of Treasury and Finance (DTF) is responsible for monitoring the State's economy and for delivering economic forecasts to the Government. The Committee notes that the Department has recently developed a working paper which enables a better understanding of its forecasting methodology. This document is the result of recommendations made in the *Review of Treasury Macroeconomic and Revenue Forecasting*.<sup>183</sup> Its purpose is to 'enable the reader to understand the broad method used to undertake macro-economic forecasts'.<sup>184</sup>

Furthermore, the Department explains that:<sup>185</sup>

This paper is a further step in DTF's policy of increasing the transparency of its operations. The paper will assist readers in understanding how DTF's forecasts are made and will increase confidence in the forecasts.

The Committee welcomes the disclosure of the forecasting process and will follow the Department's further steps in increasing the transparency of its operations.

In relation to the forecasting process, the Department has indicated that:<sup>186</sup>

A number of methods and sources of information are employed to generate macro-economic forecasts. These include consideration of recent and current recorded values, formal econometric modelling, trends suggested by leading indicators, economic theory, industry and business liaison, insights provided by other forecasts, and the experience and the intuition of DTF forecasters.

The Department uses a wide range of data sources including the Australian Bureau of Statistics, Reserve Bank of Australia, Treasury Corporation of Victoria, International Monetary Fund, departmental data and private institutions (for example, ANZ, National Australia Bank and Deloitte Access Economics).<sup>187</sup>

<sup>183</sup> Commonwealth of Australia, The Treasury, *Review of Treasury Macroeconomic and Revenue Forecasting* (2012).

<sup>184</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), p.1.

<sup>185</sup> *ibid.*

<sup>186</sup> *ibid.*

<sup>187</sup> *ibid.*, pp.13-15.

The Department publishes economic forecasts twice a year (which are included in the Budget and Budget Update) and the forecasting methodology is reviewed before the release of each document (in May for the Budget and in December for the Budget Update).<sup>188</sup>

### 3.5.2 The accuracy of the Department of Treasury and Finance's forecasts

The Committee notes that the relevant task of the Department of Treasury and Finance is to provide economic forecasts as accurately as possible to assist the Government and the Parliament to make informed decisions. As discussed above, these forecasts ultimately shape the budget estimates. Any deviations from these assumptions will have an effect on the State's financial outcomes.

The Committee understands that economic forecasting is a challenging task. There are a number of variables that are impossible to predict accurately and none of the variables is entirely within the Department's control. The success of a forecast relies on multiple factors, such as considering the full range of accurate information and the ability to utilise the appropriate modelling and statistical techniques.

The Committee has assessed the accuracy of the Department's forecasts for real GSP growth, employment, the unemployment rate, the consumer price index, the wage price index and population growth, by comparing the actual results to the estimates contained in previous budgets.

Tables showing forecasts and actual figures for those variables can be found in Appendices A3.1 to A3.6. The tables show varying levels of accuracy across different years and different variables. Overall, across the seven years examined by the Committee, 47.6 per cent of budget year estimates were within half a percentage point of the actual result.<sup>189</sup> Real GSP growth and employment growth have been the most difficult variables to predict accurately.

The Committee notes that the outcomes for two indicators, real GSP growth and population growth, show a consistent deviation in one direction (see Figures 3.7 and 3.8 below).

Real GSP growth has been consistently overestimated in previous budgets, with an average overestimation of 0.38 percentage points for estimates of the budget year and an average overestimation of 1.13 percentage points when comparing the earliest estimate to the actual outcome (see Appendix A3.1). For illustrative purposes, the Committee notes that 1 per cent of lower-than-expected GSP would be equivalent to \$160 million less revenue for the Government in 2015-16.<sup>190</sup>

<sup>188</sup> *ibid.*, pp.1-2.

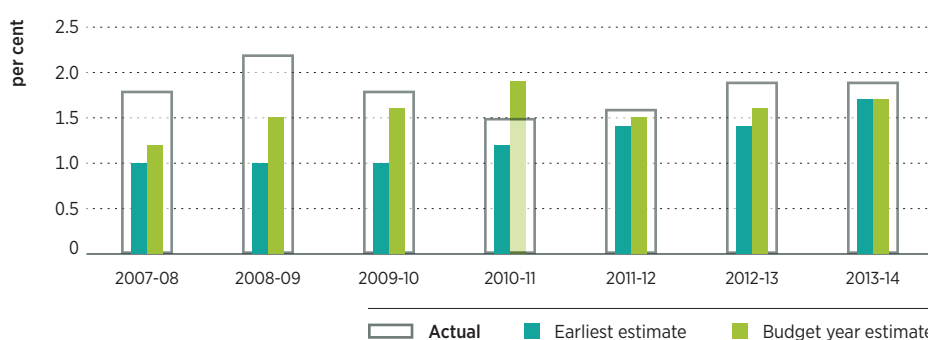
<sup>189</sup> Committee calculations based on Appendices A3.1-A3.6.

<sup>190</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.78.

**Figure 3.7** Real GSP estimated and actual growth rates, 2004–05 to 2013–14 budgets

Note: The earliest estimate refers to the first time that a forecast for the relevant year appeared in the budget papers (that is, four years in advance).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

**Figure 3.8** Population estimated and actual growth rates, 2004–05 to 2013–14 budgets

Note: The earliest estimate refers to the first time that a forecast for the relevant year appeared in the budget papers (that is, four years in advance).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

In relation to population growth, the Committee notes that this variable has been consistently underestimated in previous budgets, with an average underestimation of 0.24 percentage points for the budget year and an average variation of 0.57 percentage points comparing the actual outcome to the earliest estimate (see Appendix A3.2). The budget papers do not estimate the impact of forecast errors for population growth on the revenue, expenses or net debt estimates.

Consistent forecast errors in one direction can be an indication that there is scope to improve the methodology. The Committee therefore considers that the Department of Treasury and Finance may benefit from reviewing its methodology for these variables.

Regarding these and the other economic variables, the Committee also considers that disclosure could be improved in the budget papers. A better understanding of the budget estimates would be provided by more clearly indicating the reliability of the estimates. This is further discussed in Section 1.2.2 of this report.

**FINDING 27:** Forecasts produced by the Department of Treasury and Finance have shown mixed success between 2007-08 and 2013-14, with 47.6 per cent of recent estimates for the budget-year within 0.5 percentage points of the actual result. However, the growth in real gross state product has been consistently overestimated and population growth has been consistently underestimated.

**RECOMMENDATION 15:** The Department of Treasury and Finance review its methodology for forecasting growth in real gross state product (in the light of the regular overestimation in previous budgets) and population growth (in the light of regular underestimation).

### The use of trends for economic forecasting

The budget papers indicate that the economic forecasts for the last two years of the forward estimates period are calculated in a different way to the first two years. In relation to the economic forecasts for the last two years, the budget papers specify that:<sup>191</sup>

Projections for 2017-18 and 2018-19 represent trend rates, except for the unemployment rate which shows a path towards trend.

The Committee sought further details from the Department of Treasury and Finance about how these forecasts were calculated. Table 3.4 below shows the response provided by the Department.

The Department's explanation indicates that, in most cases, the forecasts have been made by calculating the past annual average growth rate (also referred to as 'long-run average growth rate'). The Committee notes that the periods of time used in these calculations vary significantly, from nine years to 37 years. The Committee considers that disclosing the periods of time in the budget papers would provide the Parliament and the community with a better understanding of the basis of the budget estimates.

The Committee considers that this would be particularly important as there are multiple ways to produce forecasts of economic variables. Some people may not consider calculating averages based on past performance, sometimes over long periods, to be the most appropriate methodology for calculating economic forecasts. Publishing details of the methodology in the budget papers would enable readers to make their own assessments about the appropriateness of the economic forecasts used in calculating the budget estimates.

The Committee also notes that the methodology used for calculating the forecasts of the last two years of the forward estimates period is set out more clearly in Table 3.4 than in the Department's document *Method for Making Forecasts of*

<sup>191</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.19.

*Macro-Economic Indicators*<sup>192</sup> (discussed in Section 3.5.1 of this chapter). The Committee considers that this document should be updated to more clearly reflect the methodology used to calculate all forecasts.

**Table 3.4** Trends used to produce economic forecasts for 2017-18 and 2018-19 in the 2015-16 Budget

Economic variable	Assumed trend (rounded)	Period of trend analysis	Actual 'trend' using analysis period (unrounded)	Comment
Real gross state product <sup>(a)</sup>	2.75	Since 1989-90	2.79	Annual average growth since series began in 1989-90.
Employment <sup>(a)</sup>	1.50	Since June Quarter 1978	1.58	Equal to the long-run average growth rate since series began.
Unemployment rate <sup>(b)</sup>	Falling to 5.75	Since December Quarter 1983	6.87	Simple average of past values is not used. Estimate of the 'equilibrium' unemployment rate derived from econometric modelling of the natural rate of unemployment and non-accelerating inflation rate of unemployment (NAIRU), to which the projections converge by the end of the forward estimates period (This value is 5.73%).
Consumer price index <sup>(a)</sup>	2.50	Since September Quarter 1993	2.51	The trend of 2.50% was chosen because it is the mid-point of the RBA's inflation target band. This coincides with the average rate since inflation targeting commenced in mid-1993.
Wage price index <sup>(a)</sup>	3.50	Since mid-1998 when WPI series started	3.41	The average growth rate since mid-1998 (beginning of the WPI series). The trend of 3.50% is consistent with a trend growth for inflation of 2.50% and the labour share of productivity of 1.00%.
Population <sup>(c)</sup>	1.8	Since mid-2006	1.79	Represents the average growth since mid-2006 (8 years), rather than since 1980s when the series began. The average growth between 1981 and 2005 was 1.0%, and since 2006 the growth rate has never been below 1.4%.

(a) Per cent change in year-average compared with previous year.

(b) Year-average rate (per cent)

(c) Per cent change over the year to 30 June.

Source: Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.4.

**FINDING 28:** Forecasts for most of the key economic variables for 2017-18 and 2018-19 are based on past average growth rates over different periods of time. These periods range from nine years (in the case of population growth) to 37 years (in the case of employment growth). The budget papers and the Department of Treasury and Finance's *Method for Making Forecasts of Macro-Economic Indicators* provide very limited details about how forecasts of the last two years of the forward estimates period are calculated.

<sup>192</sup> Macroeconomic and Revenue Forecasting Group, Department of Treasury and Finance, *Method for Making Forecasts of Macro-Economic Indicators* (2015), pp.1-2.



**RECOMMENDATION 16:** Future budget papers include additional details about the methodology used in making economic forecasts across the forward estimates period, including the period of time considered when calculating trends where appropriate.

**RECOMMENDATION 17:** The Department of Treasury and Finance update the *Method for Making Forecasts of Macro-Economic Indicators* to provide more detailed descriptions of the methods used to produce forecasts for the last two years of the forward estimates period.

### 3.5.3 Economic forecast quality assurance

The Committee notes that the Department of Treasury and Finance has performance measures in place to assess the accuracy of its forecasts for two main economic variables: ‘Accuracy of estimating the employment growth rate in the State budget’ and ‘Accuracy of estimating the gross state product growth rate in the State budget’.<sup>193</sup> In the 2015-16 budget papers, these two performance measures have replaced a former performance measure which measured the forecast accuracy of both variables.<sup>194</sup> The Department indicated that, ‘the measure has been split to allow clear reporting of the economic metrics and to improve the clarity of the data presented’.<sup>195</sup> The Committee welcomes the introduction of these two new performance measures. However, the Committee has some concerns about the broadness of the targets for these measures.

The Committee sought further details on what mechanisms the Department of Treasury and Finance has put in place to assess previous economic forecasts compared to actual results. The Department explained that:<sup>196</sup>

- Accuracy of forecasts is a key output deliverable; macroeconomic (GSP and employment growth within one percentage point of actual) and revenue (forecast aggregate own source tax revenue to be within five percent of actual) targets are output reporting requirements that ensure comparison between actuals and forecasts. All forecasts for the main macroeconomic variables as well as revenue are reported in the on-line database and are available for public scrutiny;
- DTF forecasting methodologies are scrutinised by the Victorian Auditor-General as part of the process of providing an independent assurance report published in Budget Paper 5 Statement of Finances;
- DTF undertakes its own annual schedule of internal audit of activities. In recent years audits have been undertaken on Economic forecasting and modelling (2012-13) and Land Transfer Duty forecasting and modelling (2013-14). In addition DTF subscribes to ISO (International Organization for Standardization) accreditation which also undertakes regular reviews of forecasting methodologies and associated processes;

<sup>193</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.326.

<sup>194</sup> ‘Accuracy of estimating gross state product and employment in the State Budget’ (Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.296).

<sup>195</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.326.

<sup>196</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.32-3.

- DTF utilises best practice in undertaking its forecasts. This includes continual reviews of methodologies updating and refreshment of econometric tools that support forecasts (at least twice a year after budget and budget updates). Models are compared to best practice. The general outline is described and published as part of the on-line database.

Furthermore:<sup>197</sup>

Methodologies employed include guidance from economic theory and econometric modelling where appropriate, review of forward indicators, consideration of market conditions and commentary including intelligence gathered through business liaison, consideration of contemporaneous developments, attention to risk and other mitigating circumstances and all forecasts are subject to review by ascending levels of scrutiny within the Department. Comparisons are always made with other public forecasts made by the Commonwealth Treasury, the Reserve Bank of Australia, other state and territory treasuries and private sector forecasters (primarily banks) to affirm storylines and may lead to modification of forecasts.

The Committee is pleased to see that these measures are in place. The Committee hopes that continued quality assurance and consideration of past estimates will enable the Department to further refine its methodologies and improve its forecasts.

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197 *ibid.*, p.33.

# 4 Revenue

## 4.1 Introduction

The Government expects that the total revenue for the general government sector will be \$55.5 billion in 2015-16. Over the forward estimates, it is forecast to rise to \$61.2 billion (see Table 4.1).

**Table 4.1** General government sector revenue, 2014-15 to 2018-19

	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
Total revenue (\$ million)	53,542.4	55,528.7	56,893.9	59,036.6	61,179.1
Annual growth					
• (\$ million)	1,177.8	1,986.3	1,365.2	2,142.7	2,142.5
• (per cent)	2.2	3.7	2.5	3.8	3.6
Average annual growth rate (2015-16 to 2018-19) (per cent) <sup>(a)</sup>			3.3		

(a) Compound annual growth rate. Calculated by the Committee.

Source: Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.49; Committee calculations based on Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015.

This revenue comes from a range of sources. Slightly more than half (54.2 per cent in 2015-16) is expected from the State's own sources, such as taxes, fees, fines and dividends. The balance comes from the Commonwealth Government in grants.

This chapter will examine the following aspects of the budget estimates for revenue:

- What is the Government's strategy for revenue? (Section 4.2)
- What are the forecast trends in revenue and what do these mean for Victoria? (Section 4.3)
- How do the latest estimates compare with those from previous budgets? (Section 4.4)
- What are the main components of revenue and how are they expected to change between 2015-16 and 2018-19? (Sections 4.5 and 4.6)

## 4.2 Government strategy for revenue

The budget papers set out financial measures and targets for the 2015-16 Budget (see Section 2.3.2 of this report). These include:<sup>198</sup>

A net operating surplus consistent with maintaining general government net debt at a sustainable level over the medium term.

To achieve this target, revenue growth will need to keep pace with the growth in output expenses and asset investment. Estimates of the operating surplus are discussed further in Section 2.4.1 of this report.

Specific initiatives affecting revenue growth in the 2015-16 Budget are discussed in Section 4.4.3.

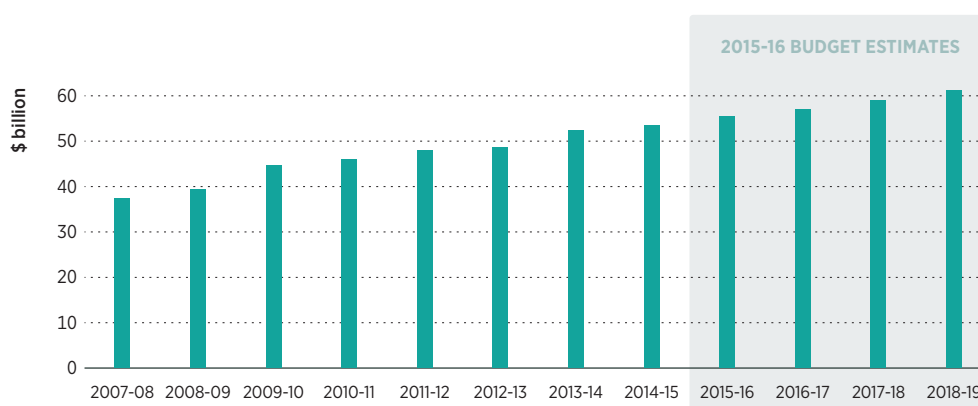
## 4.3 Revenue estimates

### 4.3.1 Expected growth over the forward estimates period

As mentioned in Section 4.1, the budget estimates predict that the total revenue of the general government sector will rise to \$55.5 billion in 2015-16 from an estimated \$53.5 billion in 2014-15. It is then anticipated to climb to \$61.2 billion over the forward estimates period.<sup>199</sup>

Figure 4.1 shows the revenue for each year since 2007-08, including the forward estimates period.

**Figure 4.1** Total revenue, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 1 June 2015.

<sup>198</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

<sup>199</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.163.

Table 4.2 shows that, for most items of revenue, the forecast growth rates in the 2015-16 Budget are significantly lower than the actual rates seen in past results. Consequently, the forecast growth rate for revenue as a whole is also lower than past actual rates. Further detail is given in Appendix A4.1.

**Table 4.2** Past actual and forecast growth rates, selected revenue components

Revenue component	Past actual growth rates <sup>(a)</sup>	Forecast growth rates <sup>(b)</sup>
Taxation revenue	4.7	3.9
Sales of goods and services	7.0	1.2
Other revenue <sup>(c)</sup>	7.5	1.6
Dividends and similar revenue	-8.5	-2.8
Grant revenue	6.5	3.8
Total revenue	5.8	3.3

(a) Compound annual growth rate, 2007-08 to 2013-14.

(b) Compound annual growth rate, 2015-16 to 2018-19.

(c) Includes interest, other contributions and grants.

Source: Committee calculations based on Department of Treasury and Finance, *State Taxation Revenue - Annual* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue)>, viewed 27 May 2015; Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement - General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 1 June 2015.

The budget papers do not normally compare the growth rate estimates for revenue components with past actual growth rates. However, the Committee considers that the budget papers would be improved if significant variances between estimated future growth rates and past actual growth rates were explained, as this would make the assumptions underlying the budget estimates clearer. This is discussed further, along with a recommendation, in Section 1.2.5 of this report.

Table 4.3 compares the actual and estimated growth rates for taxation revenue and gross state product (GSP).

**Table 4.3** Past actual and forecast growth rates, taxation revenue and gross state product

	Past actual growth rate <sup>(a)</sup>	Growth rate over forward estimates period <sup>(b)</sup>
	(per cent)	(per cent)
Taxation revenue	4.7	3.9
Gross state product	4.1	5.4

(a) Compound annual growth rate between 2007-08 and 2013-14.

(b) Compound annual growth rate between 2015-16 and 2018-19.

Source: Committee calculations based on Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement - General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 3 June 2015; Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 3 June 2015.

There is generally a strong relationship between growth in the broader economy and growth in taxation revenue. For example, as the Commonwealth Parliamentary Budget Office recently stated (in relation to the Commonwealth Government):<sup>200</sup>

... over the past 30 years, growth in the nominal economy has been the main driver of receipts, as revenue collections are highly dependent on the size and growth of the economy, profits and income.

The Victorian budget papers also note that:<sup>201</sup>

... higher than expected economic activity or inflation will tend to lead to higher taxation revenue.

Given this relationship between the broader economy (which is measured by GSP) and taxation revenue, one would expect that a higher GSP growth rate would cause a higher taxation growth rate. However, as Table 4.3 shows, the budget papers estimate that something quite different will happen. The budget papers predict that the rate of GSP growth will increase, while the rate of taxation growth will decrease.

There are a number of possible reasons for this, such as: the influence of factors other than GSP on taxation estimates; an expected change in the relationship between taxation revenue and GSP; or issues with the Department of Treasury and Finance's methodology. The budget papers usually provide only limited explanations of the relationship between economic variables and the revenue estimates, making it impossible to tell what the Department of Treasury and Finance is expecting that has led to these estimates. The Committee considers that future budget papers would be improved by discussing the relationship between economic variables and revenue estimates in more detail, so that the Parliament and the community could better understand the basis of the estimates.

**FINDING 29:** Revenue is expected to rise to \$55.5 billion in 2015-16. It is then forecast to rise to \$61.2 billion over the forward estimates period, an average growth rate of 3.3 per cent per year. The growth rate for revenue anticipated over the forward estimates period is significantly lower than historical rates. Though there is a strong relationship between gross state product (GSP) and taxation revenue, the budget estimates suggest that taxation revenue will grow more slowly than GSP over the forward estimates period.

**RECOMMENDATION 18:** Future budget papers include an explanation of how the estimates for GSP have influenced the estimates of different components of revenue. In cases where GSP growth rates differ significantly from revenue growth rates, these explanations should identify the factors which have caused the difference in growth rates, and discuss how each factor has influenced the estimate.

<sup>200</sup> Parliament of Australia, Parliamentary Budget Office, *The Sensitivity of Budget Projections to Changes in Economic Parameters* (2014), p.2.

<sup>201</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.63.

**RECOMMENDATION 19:** The Auditor-General assess whether the factors used by the Department of Treasury and Finance in constructing revenue estimates are adequately described in the budget papers. This assessment should include the way GSP estimates, and any other relevant factors, have been taken into account. As part of this, the Auditor-General should examine why the taxation estimates in the 2015-16 Budget increase at a slower rate than has occurred in recent years at the same time that the GSP estimates increase at a faster rate.

### 4.3.2 Underestimation in the budget estimates

One factor that may partly explain the lower estimated growth rate for revenue is that the estimates may be understated. Table 4.4 looks at the revenue growth estimates across forward estimates periods in previous budgets.<sup>202</sup> By comparing the estimated growth with what actually occurred, it can be seen that revenue growth has been consistently underestimated.

**Table 4.4** Estimated and actual growth rates for total revenue, rolling forward estimates periods

	Estimated growth rate across the relevant forward estimates period <sup>(a)(b)</sup>	Actual growth rate <sup>(a)</sup>
2005-06 Budget	3.0	7.1
2006-07 Budget	3.0	8.5
2007-08 Budget	3.2	7.2
2008-09 Budget	4.1	6.8
2009-10 Budget	1.5	2.9
2010-11 Budget	3.3	4.4

(a) All growth rates are compound annual growth rates between the relevant budget year and the end of the relevant forward estimates period.

(b) Calculation of estimated growth rates in each budget is shown in Appendix A4.4

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2005-06 to 2010-11; Department of Treasury and Finance, *Financial Report*, 2006-07 to 2013-14.

The average annual growth rate predicted in the budgets listed in Table 4.4 was 3.0 per cent, with the highest predicted growth rate being 4.1 per cent. The actual growth rate over the whole period (2005-06 to 2013-14) was 6.4 per cent, and the growth predicted in each budget was less than actually occurred.

The underestimation can also be seen by comparing the revenue estimate for the budget year to the actual amount of revenue received. For every budget that the Committee examined (2005-06 to 2013-14<sup>203</sup>), the revenue estimate was lower than the actual amount (see Appendix A4.2). The average underestimation over this period was \$1.5 billion.<sup>204</sup>

<sup>202</sup> The 2010-11 Budget is the last one included, as it is the last year for which actual data are available for all years of the budget's forward estimates period.

<sup>203</sup> 2013-14 is the last year for which actual amounts have been published to date.

<sup>204</sup> Committee calculations based on Appendix A4.4.

The consistent underestimation may be partly a result of the methodology used to make the budget estimates. The Department of Health and Human Services advised the Committee that:<sup>205</sup>

Conservative price and volume assumptions have been used to ameliorate the income risks associated with National Health Reform and other fee for service revenue. Commonwealth funding arising from National Partnership Agreements has only been included in budget papers where negotiations with the Commonwealth have concluded.

Other departments also indicated that a policy had been adopted of forecasting income as zero where the amount is difficult to accurately estimate, even though it is likely that some revenue will be received.<sup>206</sup>

This can be seen with specific-purpose grants from the Commonwealth Government. The Commonwealth budget is presented after the Victorian budget, meaning that not all funding decisions are known to the Victorian Government when preparing the State budget. The Department of Treasury and Finance indicated to the Committee that its methodology for estimating specific-purpose grants is conservative, explaining that its estimates are:<sup>207</sup>

... based on the latest advice from the Commonwealth, primarily from Commonwealth budget publications, direct and specific advice from the Commonwealth, or conservative interpretations of the funding conditions for national partnership agreements. The Victorian Government does not attempt to anticipate future policy decisions of the Commonwealth.

The Department also advised the Committee that ‘the Victorian budget does not contain contingencies for specific-purpose grants that have yet to be announced’.<sup>208</sup>

As a result, for a number of specific-purpose grants whose future was uncertain at the time of the Victorian budget, the Victorian budget estimates included no income in 2015-16 (see Appendix A4.3). In three cases, subsequent decisions by the Commonwealth Government mean that funding will be provided:

- the National Partnership Agreement on Homelessness includes \$22.8 million for Victoria in 2015-16<sup>209</sup>
- the National Partnership on the National Quality Agenda on Early Childhood Education and Care includes a total payment of \$19.1 million to the states in 2015-16, including a yet-to-be determined share to Victoria<sup>210</sup>

<sup>205</sup> Department of Health and Human Services, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 26 June 2015, p.9.

<sup>206</sup> For example, Department of Justice and Regulation, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 11 June 2015, p.15; Parliamentary Departments, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.5.

<sup>207</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.2.

<sup>208</sup> *ibid.*

<sup>209</sup> Commonwealth of Australia, *Budget Paper No.3: Federal Financial Relations 2015-16* (2015), p.48.

<sup>210</sup> *ibid.*, p.32.



- the National Partnership on Treating More Public Dental Patients has been replaced by a new National Partnership on Adult Public Dental Services, including an anticipated payment to Victoria of \$38.5 million in 2015-16.<sup>211</sup>

The Committee notes that this may no longer be an issue if the State budget is tabled after the Commonwealth budget. The Government has informed the Committee that it is considering a later date, and:<sup>212</sup>

... will continue to investigate implementation options for a future year, subject to the preservation of Constitutional protection around budget passage.

The Committee notes that the practice of making conservative estimates and estimating zero for items about which there is uncertainty is a regular accounting practice. The Committee also notes that the Auditor-General has indicated that:<sup>213</sup>

... the estimated financial statements have been properly prepared on the basis of the assumptions contained in Note 1 [and that] the methodologies used to determine those assumptions are reasonable.

However, these practices can lead to underestimation of revenue. The Committee considers that current and recent budget papers have not clearly explained the likelihood that the revenue estimates are understated. For example, the budget papers discuss risks associated with grants from the Commonwealth Government. However, they do not disclose that the Department of Treasury and Finance's methodology<sup>214</sup> means it is most likely that grant revenue will be higher than predicted in the budget papers.

Recommendations relating to this issue have been made in Section 1.2.2 of this report.

**FINDING 30:** The budget estimates predict that revenue will grow at a slower rate over the forward estimate period than in recent years. This may be a result of a forecasting methodology that includes conservative estimates and omits elements of revenue where the amount to be received is uncertain.

### 4.3.3 Revenue per Victorian

As noted in Section 4.3.1, revenue is expected to increase each year, but at a slower rate than in previous years.

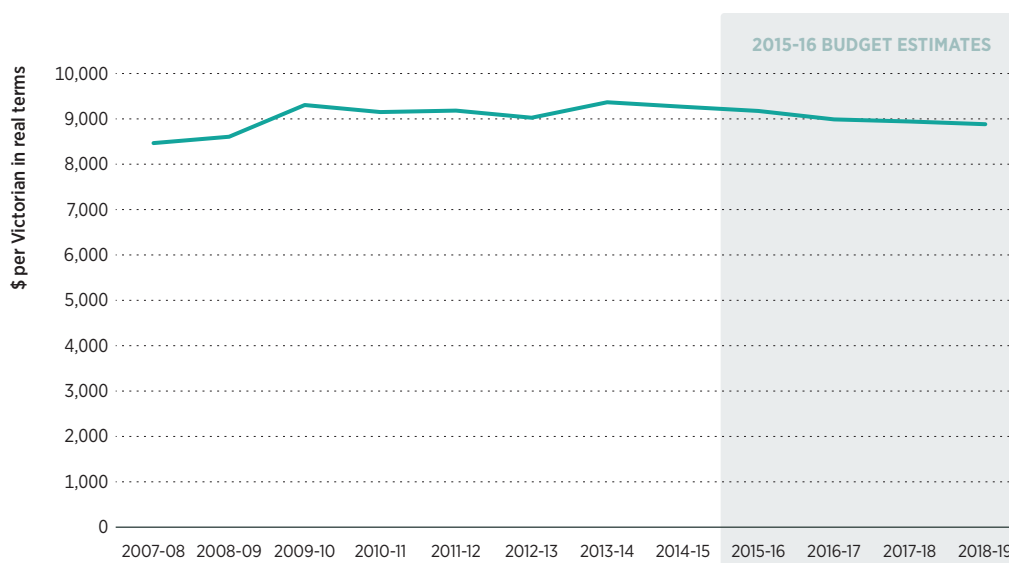
Figure 4.2 below adjusts the revenue estimates to show what they would mean per person, and in real terms (that is, removing the effects of inflation).

<sup>211</sup> *ibid.*, p.26.

<sup>212</sup> Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 120<sup>th</sup> Report to Parliament – Report on the 2014-15 Budget Estimates – Part Two*, tabled 15 April 2015, p.2.

<sup>213</sup> Victorian Auditor-General, quoted in Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.5.

<sup>214</sup> Such as making conservative estimates and not including any estimates of future new grants.

**Figure 4.2** Revenue per Victorian in real terms,<sup>(a)</sup> 2007-08 to 2018-19

(a) Expressed in 2015-16 prices.

Source: Committee calculations based on Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 3 June 2015; Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 3 June 2015.

Revenue is expected to be \$9,172 per person in 2015-16. The Government anticipates that this will decrease to \$8,880 (in 2015-16 prices) in 2018-19.

Figure 4.2 shows that revenue in real terms per Victorian is expected to follow a broad downward trend after peaking in 2013-14. While revenue is increasing in dollar terms (see Figure 4.1), population growth and inflation are expected to combine to outweigh this growth.

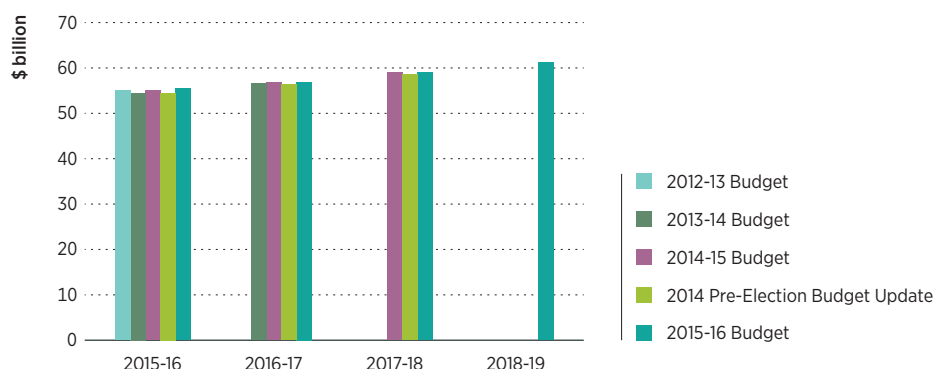
If this trend were to occur, it would put pressure on the Government's ability to deliver the same level of services to Victorians.

**FINDING 31:** Revenue is expected to be \$9,172 per Victorian in 2015-16. By 2018-19, revenue is expected to have decreased to \$8,880 per Victorian (in 2015-16 terms), as population and inflation are expected to grow at a faster rate than the revenue estimates.

## 4.4 Comparison to previous estimates

At the time of each budget, the Government produces new estimates (including revenue estimates) for the relevant forward estimates period. Figure 4.3 compares the latest revenue estimates to past estimates, including those from the 2014 Pre-Election Budget Update (issued by the Department of Treasury and Finance shortly before the election in 2014).

Figure 4.3 shows that, since the 2014 Pre-Election Budget Update, estimates for every year between 2015-16 and 2017-18 have been revised upwards, by a total of \$2.1 billion.

**Figure 4.3** Comparison of revenue estimates in the 2015-16 Budget to previous estimates

Source: Department of Treasury and Finance, *Budget Paper No.5: Statement of Finances*, 2012-13 to 2015-16; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.27.

However, the forward estimates had been revised downwards in the 2014 Pre-Election Budget Update compared to the previous budget. The Pre-Election Budget Update stated that this was principally a result of adjustments to the scheduling of specific-purpose grants from the Commonwealth Government for the *East West Link*.<sup>215</sup> This involved two separate changes: a prepayment of \$1 billion in 2013-14 (increasing grants for 2013-14 and correspondingly lowering those for 2014-15 to 2016-17); and a \$500 million deferral, decreasing expected revenue in 2017-18 and increasing it in 2018-19.<sup>216</sup>

As noted above, estimates made in the 2015-16 budget papers are consistently higher than those made in the 2014 Pre-Election Budget Update. Table 4.5 illustrates what has driven the changes.

**Table 4.5** Variations in estimates for revenue between the 2014 Pre-Election Budget Update and the 2015-16 Budget

	2015-16	2016-17	2017-18
<b>Revenue estimates in the 2014 Pre-Election Budget Update</b>	<b>54,482.3</b>	<b>56,346.1</b>	<b>58,524.6</b>
State Government policy decision variations	+49.0	+76.0	+91.0
Taxation	+283.2	+66.0	-175.0
Investment income	+257.0	+115.0	-118.0
General-purpose grants	+228.3	-113.8	-704.7
Specific-purpose grants	+212.3	+245.3	+1,198.4
Other <sup>(a)</sup>	+16.6	+159.3	+220.3
<b>Revenue estimates in the 2015-16 Budget</b>	<b>55,528.7</b>	<b>56,893.9</b>	<b>59,036.6</b>

(a) Calculated by elimination.

Source: Committee calculations based on Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.27; Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), p.20; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.55; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.7.

<sup>215</sup> Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.17.

<sup>216</sup> *ibid.*

The largest revision is a result of the ‘rescheduling to 2017-18 of expected revenues under the asset recycling initiative’<sup>217</sup> (see Section 8.2.3 for more details of that initiative). This accounts for the increase in specific-purpose grants in 2017-18. A number of other factors also contributed smaller amounts to the revision.

#### 4.4.1 Commonwealth Government grants

Table 4.5 shows that the increase in the revenue estimates is primarily a result of changes to the scheduling of specific-purpose grants from the Commonwealth Government. The estimates for specific-purpose grant revenue between 2015-16 and 2017-18<sup>218</sup> increased by \$1.7 billion between the 2014 Pre-Election Budget Update and the 2015-16 Budget, predominantly in 2017-18.

The budget papers identify two factors that have contributed to this:

- ‘additional funding for government and non-government schools announced in the Commonwealth’s 2014-15 Mid-Year Economic and Fiscal Outlook’<sup>219</sup>
- ‘the rescheduling to 2017-18 of expected revenues under the asset recycling initiative’.<sup>220</sup>

General-purpose (GST) grants from the Commonwealth Government in 2015-16 are also expected to be higher than previously forecast. The budget papers note that this ‘reflects growth in the GST pool and an improvement to Victoria’s GST relativity as recommended by the Commonwealth Grants Commission (CGC) in their methodology review’.<sup>221</sup> However, less is now expected through general-purpose grants in 2016-17 and 2017-18 than was previously expected. The large write-down for 2017-18 is due to a lowering of the estimated GST relativity for the State.<sup>222</sup> The Department of Treasury and Finance advised the Committee that this is ‘due mostly to lower iron ore prices increasing Western Australia’s share of the national GST pool’.<sup>223</sup>

#### 4.4.2 State taxation and investment income

Estimates for taxation have been revised upward for 2015-16 and 2016-17, but downward in 2017-18. The Department of Treasury and Finance advised the Committee that the upward revision for 2015-16 was driven by land transfer

217 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.57.

218 The years common to both estimates.

219 Department of Treasury and Finance, *2014-15 Budget Update* (2014), p.21.

220 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.57.

221 *ibid.*

222 *ibid.*

223 Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.48.

duty 'due to the property market being stronger than originally forecast'.<sup>224</sup> The budget papers note that that the downward revision in 2017-18 is a result of the increased risk of a downturn later in the forward estimates period.<sup>225</sup>

This is partly mitigated by payroll tax. Estimates for payroll tax are lower in 2015-16 than previously predicted, as a result of a 'divergence between aggregate hours worked and total employment [which] means payroll tax revenue has not kept pace with recent gains in employment'.<sup>226</sup> This divergence is illustrated in a graph in the budget papers.<sup>227</sup> The budget papers also note that 'aggregate hours worked are expected to improve in line with the forecast period of sustained employment growth',<sup>228</sup> restoring the payroll tax revenue to that of previous estimates from 2016-17 onwards.

The Committee recommends in Section 3.4 of this report that, in the future, the Department of Treasury and Finance release its forecasts for the number of hours worked. This would help readers to understand the expected effects of this on payroll tax.

These estimates are particularly interesting in the light of the Government's strategies to create jobs and grow the economy, such as the *Plan for Jobs and Growth* (see further discussion in Section 3.4 of this report).

Section 4.5.1 discusses taxation in greater detail.

The estimates for dividends and similar revenue have been increased in 2015-16 and 2016-17 but decreased in 2017-18. These changes are mostly a result of changes in the value of dividends expected from various government business enterprises. Dividend revenue has been adjusted in a complex manner, with expected dividends from some enterprises increased while others have been decreased.<sup>229</sup>

In particular, the Government has raised the amount of dividends expected from the Transport Accident Corporation (TAC) between 2015-16 and 2017-18,<sup>230</sup> and imposed dividends on the Victorian Managed Insurance Authority for the first time.<sup>231</sup> However, it has also decided not to take dividends from WorkSafe Victoria (the Victorian WorkCover Authority) over the whole of the forward estimates period.<sup>232</sup> Previously the authority was expected to provide \$535.1 million between 2015-16 and 2017-18.<sup>233</sup> See Section 4.5.3 for more detail.

<sup>224</sup> This is offset by lower revenue from land tax and motor vehicle taxes (Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.36).

<sup>225</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.56.

<sup>226</sup> *ibid.*

<sup>227</sup> *ibid.*, p.21; also discussed on pp.30-3 as 'underemployment'.

<sup>228</sup> *ibid.*, p.56.

<sup>229</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28.

<sup>230</sup> *ibid.*; Department of Treasury and Finance, *Budget Paper No.5: 2014-15 Statement of Finances* (2014), p.23.

<sup>231</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28.

<sup>232</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.56.

<sup>233</sup> Calculation based on Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.44.

The budget papers state that the lower-than-previously-expected investment income in 2017-18 'largely reflects lower income tax equivalent payments by TAC due to reduced investment income and the impact of bond rate movements on claim costs'.<sup>234</sup>

### 4.4.3 2015-16 Budget initiatives

The estimates are also influenced by revenue and revenue foregone initiatives. These are new decisions to increase or decrease revenue which are released with each budget and budget update.

The 2015-16 Budget released revenue initiatives intended to increase revenue by \$333.1 million over four years (see Table 4.6) and one revenue foregone initiative intended to decrease revenue by \$11.4 million over four years.

**Table 4.6** New revenue initiatives, 2015-16 Budget

Initiative	Net impact over the forward estimates period <sup>(a)</sup> (\$ million)
<i>Absentee Landowner Surcharge</i>	53.5
<i>Land Transfer Duty Surcharge on Foreign Buyers of Residential Property</i>	279.6
<b>TOTAL</b>	<b>333.1</b>

(a) 2015-16 to 2018-19.

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

The most significant of these initiatives is a decision by the Government to add a 3.0 per cent surcharge to the land transfer duty payable on sales or transfers of residential property to foreign buyers.<sup>235</sup> This is expected to raise land transfer revenue by \$279.6 million over the next four years. The Department of Treasury and Finance informed the Committee that 'the purchaser will have an opportunity to declare whether they are a "foreign purchaser" at the time of making a purchase or relevant acquisition',<sup>236</sup> although the Department of Treasury and Finance also advised the Committee that, 'The Treasurer may exercise discretion to provide an exemption to foreign developers that add to the supply of housing stock in Victoria'.<sup>237</sup>

The Committee notes that the Parliament's Standing Committee on the Economy and Infrastructure conducted an inquiry into the State Taxation Acts Amendment Bill 2015, which brings this initiative into law. Though the budget papers estimate

<sup>234</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.56.

<sup>235</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

<sup>236</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.20.

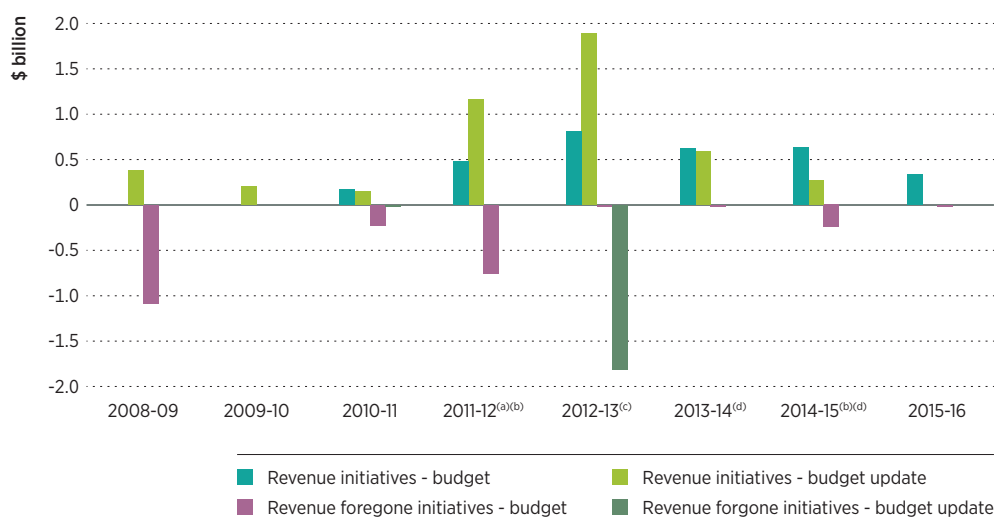
<sup>237</sup> *ibid.*

that revenue will flow to the Government as a result of this initiative from 2015-16,<sup>238</sup> the Economy and Infrastructure Committee found that the full impact of the surcharge may not be realised for several years.<sup>239</sup>

One revenue foregone initiative was introduced in the 2015-16 Budget, decreasing revenue over the forward estimates period by \$11.4 million by reducing stamp duty on the registration of mobile plant and other special-purpose vehicles.<sup>240</sup> This is discussed further in Section 4.5.1.

Figure 4.4 compares the impact of revenue and revenue foregone initiatives from the 2015-16 Budget with initiatives from past budgets.

**Figure 4.4** New revenue and revenue foregone initiatives, current and previous budgets (five-year totals), 2008-09 to 2015-16



- (a) Initiatives included in previous budget updates have been removed from the totals given in Budget Paper No.3 prior to 2010-11 to avoid double counting.
- (b) Budget Update initiatives for 2010-11 and 2014-15 are from Budget Updates and Pre-Election Budget Updates.
- (c) These large amounts reflect primarily the discontinuation of previous mechanisms for gathering fire-related contributions and their replacement by the Fire Services Property Levy.
- (d) A Casino Electronic Gaming Machine Levy was introduced in the 2013-14 Budget Update, but estimates were removed from the 2014-15 Budget, as mutual agreement between the Government and the Casino operator had not been achieved by the time of the Budget (Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.78). This initiative has been excluded from the figure above.
- Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery, 2008-09 to 2015-16*; Department of Treasury and Finance, *Victorian Budget Update, 2008-09 to 2014-15*; Department of Treasury and Finance, *Victorian Pre-Election Budget Update, 2010 and 2014*.

<sup>238</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

<sup>239</sup> Economy and Infrastructure Committee, *Inquiry Into the State Taxation Acts Amendment Bill 2015* (2015), p.4.

<sup>240</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

Figure 4.4 shows that revenue initiatives in the 2015-16 Budget have been smaller than those released in the past four years. Revenue to be raised through these initiatives is estimated at \$333.1 million over four years.<sup>241</sup> Over the previous four budgets, the average estimated additional revenue through revenue initiatives was \$637.5 million.<sup>242</sup>

Similarly, the total revenue forgone over the next four years from new initiatives in the 2015-16 Budget (\$11.4 million<sup>243</sup>) is lower than the average (\$255.7 million<sup>244</sup>) of the previous four budgets.

**FINDING 32:** The value of revenue and revenue foregone initiatives released in the 2015-16 budget papers is significantly less than the value of initiatives released in the last four budgets.

### Disclosure of revenue initiatives

The budget papers include a number of initiatives whose principal purpose is to lower revenue flowing to the Government in order to achieve specific policy objectives. The Committee notes that the budget papers do not treat two of these initiatives in a consistent manner.

The *Stamp Duty Exemption on Mobile Plant Registration* initiative is intended to reduce running costs for businesses by exempting vehicles classified as ‘mobile plant’ or ‘plant-based special purpose vehicles’ from stamp duty. This initiative is classified as a revenue measure in the budget papers.<sup>245</sup>

The *Car Registration Discounts for Trade Apprentices* initiative provides a 50 per cent discount on registration charges for some trade apprentices. In contrast to the *Stamp Duty Exemption on Mobile Plant Registration* initiative, this initiative is classified as an output initiative.<sup>246</sup> There is no mention of this initiative in the revenue measures section of the budget papers.

Both initiatives have similar impacts on the revenue estimates.

One of the main roles of the budget papers is to communicate the Government’s policies and how they will be achieved. The Committee considers that interested users should be able to find a complete list of initiatives whose primary purpose is to forego revenue in one place. This can be achieved either by listing all such initiatives as revenue initiatives or by cross-referencing relevant initiatives in other sections from the revenue measures section of the budget papers.

<sup>241</sup> *ibid.*

<sup>242</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2011-12 to 2014-15.

<sup>243</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

<sup>244</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2011-12 to 2014-15.

<sup>245</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

<sup>246</sup> *ibid.*, pp.20, 32.



**FINDING 33:** The *Stamp Duty Exemption on Mobile Plant Registration* initiative and the *Car Registration Discounts for Trade Apprentices* initiative are both intended to forego revenue to achieve policy objectives. However, the former has been listed in the budget papers as a revenue initiative, while the latter has been included as an output initiative.

**RECOMMENDATION 20:** Future budget papers include information in the revenue measures section on all initiatives whose main effect is to lower revenue. This can be achieved either by:

- (a) including all such initiatives in the revenue measures section of the budget papers as revenue initiatives or
- (b) including a cross-reference in the revenue measures section of the budget papers to relevant initiatives in other sections of the budget papers.

## 4.5 State-sourced revenue

Overall, the budget estimates for State-sourced revenue increase to \$30.1 billion (a 3.5 per cent growth) in 2015-16, before rising to \$32.7 billion in 2018-19.<sup>247</sup>

The three largest categories of State-sourced revenue in Victoria are:

- taxation revenue
- sales of goods and services
- dividends and similar.

### 4.5.1 Taxation revenue

The estimates for taxation revenue are \$19.0 billion in 2015-16.<sup>248</sup> This is an increase of \$750.6 million over the revised estimate for 2014-15.<sup>249</sup> Over the forward estimates period it is anticipated to rise to \$21.3 billion.<sup>250</sup>

The State receives taxation revenue through a large number of streams. This section will discuss the five most significant streams. Together, these cover around 85 per cent of total taxation revenue.

Figure 4.5 (and Appendix A4.1) show that payroll tax is expected to increase at a higher rate than has been observed in the past (an average of 5.9 per cent per year compared to an historic average of 4.3 per cent). The budget papers note that ‘as demand recovers this should boost full time employment and drive a recovery in payroll tax’.<sup>251</sup> This is in line with the Government’s plan to stimulate

<sup>247</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 29.

<sup>248</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.165.

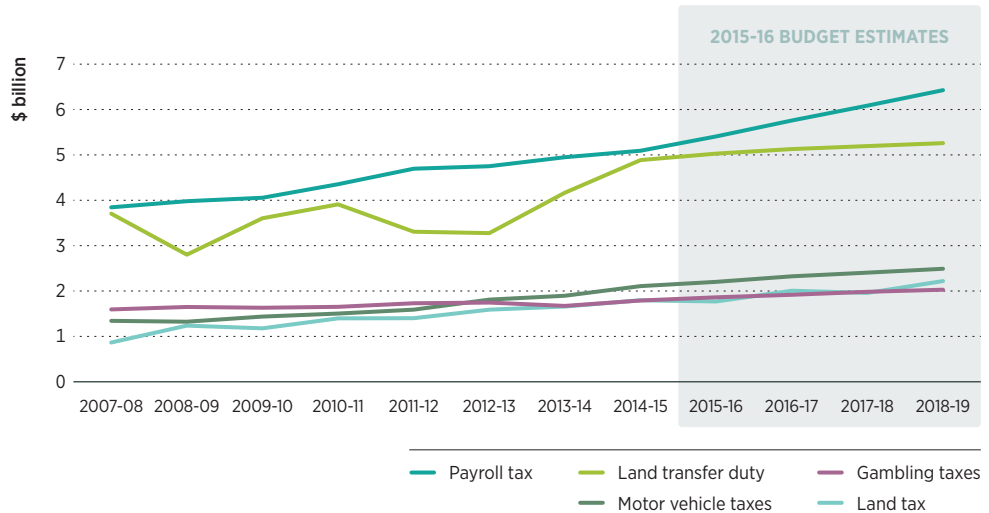
<sup>249</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.165. Payroll tax and land transfer duty were significant contributors to this growth.

<sup>250</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.165.

<sup>251</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.51.

the labour market through its *Back to Work Plan* and the budget forecasts that unemployment will stabilise over 2015-16 and 2016-17 before declining in 2018-19. See Section 3.4 of this report for further details.

**Figure 4.5** Major components of taxation revenue, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *State Taxation Revenue - Annual* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue)>, viewed 27 May 2015.

Land transfer duty is expected to increase to \$5.0 billion in 2015-16,<sup>252</sup> after having increased from \$4.2 billion to \$4.9 billion between 2013-14 and 2014-15.<sup>253</sup> Appendix A4.1 shows that, after this point, land transfer duty is forecast to grow not only at a rate slower than it has in the past (1.5 per cent per year compared to 2.0 per cent in the past), but also slower than other major tax components. This is despite the addition of a revenue initiative that adds a surcharge to land transfers to foreign buyers of residential property.<sup>254</sup>

The budget papers note that the property market is cyclical, with periods of growth interspersed by periods of stagnation.<sup>255</sup> When prices rise, sellers have an incentive to sell, but when prices stop rising, sellers tend to wait. This means that transaction numbers and prices tend to move together. Because revenue from land transfer duty is a product of both the price of the land sold and the number of transactions, this synchronisation can cause severe fluctuations in revenue (as shown in Figure 4.5).

<sup>252</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.165.

<sup>253</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.76; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.165.

<sup>254</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

<sup>255</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.166.

The budget papers also note that strong growth in the market can be an indication that the cycle may be ending, which increases the likelihood of a ‘correction’ in land transfer revenue.<sup>256</sup> Because ‘historically, a period of more subdued growth has followed periods of strong growth in land transfer duty’,<sup>257</sup> the Government has adopted a forecast of slower but positive growth from 2015-16 onwards.

Land tax is determined by land value rather than sales. Revaluations of land are performed every two years, which is why the revenue stream has a ‘stepped’ appearance in Figure 4.5. Overall, the growth rate of this component is expected to be lower than historic levels (with forecast growth of 7.8 per cent per year compared with past growth of 11.5 per cent per year). However, the growth rate is underpinned by the expectation of more land being subject to land tax.<sup>258</sup> In addition, ‘greater compliance activity by the State Revenue Office to ensure only genuine owner-occupiers receive the land tax primary place of residence exemption’<sup>259</sup> will contribute to revenue growth. This compliance activity is related to a revenue initiative included in the 2014 Pre-Election Budget Update.<sup>260</sup>

Motor vehicle tax revenue is expected to grow at 4.2 per cent per year over the forward estimates period. Revenue from motor vehicle taxes is expected to be reduced by \$11.4 million over four years by a Government revenue foregone initiative (*Stamp Duty Exemption on Mobile Plant Registrations*).<sup>261</sup> In addition, an output initiative, *Car Registration Discounts for Trade Apprentices*,<sup>262</sup> is anticipated to reduce revenue by a further \$7.6 million over the forward estimates period.<sup>263</sup> Appendix A4.1 shows that the forecast growth rate of motor vehicle tax revenue (4.2 per cent per year) is slower than has been observed over past actual results (5.9 per cent per year).<sup>264</sup> The Department of Treasury and Finance, however, describes the growth over the forward estimates period as ‘broadly in line with its trend growth rate’.<sup>265</sup>

Gambling tax revenue is expected to rise at an average rate of 2.9 per cent per year over the forward estimates period.<sup>266</sup> The budget papers note that ‘the growth in gambling tax revenue reflects general weakness in nominal consumption expenditure’.<sup>267</sup> However, Appendix A4.1 shows that this is a significant increase over past actual growth rates (which have averaged 0.8 per cent per year).<sup>268</sup>

256 ‘As upward momentum of the current cycle builds, so does the likelihood of a correction, as has been the case in past property cycles’ (Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.166).

257 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.50.

258 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.168.

259 *ibid.*

260 Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), pp.75-6.

261 Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.104.

262 *ibid.*, pp.20, 32.

263 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.191.

264 Committee calculations based on Department of Treasury and Finance, *State Taxation Revenue - Annual* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue)>, viewed 27 May 2015.

265 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.170; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.51.

266 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.170.

267 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.51.

268 This is not noted in the budget papers.

The Committee considers that the roll-out of the voluntary pre-commitment scheme<sup>269</sup> may limit growth in gambling tax revenue. In addition, in giving evidence to the Committee, the Minister for Consumer Affairs commented that:<sup>270</sup>

Between 2008-09 and 2013-14 gaming machine player loss declined in real terms by 18.3 per cent, and in that same period gaming machine expenditure as a proportion of household final consumption expenditure declined by 25 per cent.

The budget papers similarly indicate the expectation that ‘gambling expenditure will continue to decline as a share of household consumption, weighing on revenue growth’.<sup>271</sup>

The Committee notes that the budget papers previously included introductory paragraphs that described each component of tax revenue. This included relevant information such as the purpose of the item, how it is calculated or exemptions or concessions for the item. With some exceptions, these paragraphs have been removed from the 2015-16 budget papers. The budget papers have an important role in communicating the Government’s plans, and orienting readers is part of this role. The continued inclusion of this information would improve the clarity of future budget papers.

**FINDING 34:** Additional orientation information describing a number of revenue items was included in previous budget papers but has not appeared in the 2015-16 budget papers.

**RECOMMENDATION 21:** The budget papers reinstate the practice of including background information on the major components of revenue, including, where relevant, the component’s purpose, how it is calculated and relevant concessions and exemptions. This information may be included in the discussion of each revenue item or in another section in the budget papers.

## 4.5.2 Sales of goods and services

The Government receives revenue from the sale of goods and services such as regulatory fees, user charges and public transport fares. This component of revenue also includes income from property rent and the inter-sector capital asset charge, which is imposed by the Government on public sector bodies. This charge is set at 8.0 per cent of the total written-down value of assets held by the body, and is intended to encourage the disposal of assets that are not in active use.<sup>272</sup>

<sup>269</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.85.

<sup>270</sup> Hon. Jane Garrett MP, Minister for Consumer Affairs, Gaming and Liquor Regulation, *2015-16 Budget Estimates Transcript of Evidence*, 20 May 2015, p.6.

<sup>271</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.51.

<sup>272</sup> Department of Treasury and Finance, *BFMG - 12: Capital Assets Charge* (2009), p.68.

Sales of goods and services are expected to rise by 3.9 per cent to \$6.8 billion in 2015-16 before rising further to \$7.0 billion in 2017-18 and 2018-19.<sup>273</sup> This is an average annual growth rate of 1.2 per cent over the forward estimates period. As can be seen in Appendix A4.1, this is a significantly lower growth rate than has been seen in recent years (7.0 per cent).

The budget papers state that the increase in sales of goods and services in 2015-16 is 'largely driven by an increase in the capital asset charge from VicTrack reflecting an increase in the capital asset base'.<sup>274</sup> The Committee notes that a similar increase in the inter-sector capital asset charge is anticipated in 2016-17, although this is not discussed in the budget papers.<sup>275</sup> Specific commentary in this section of the budget papers covers events in the budget year, and only provides a general discussion of the rest of the forward estimates.

The largest contributor to sales of goods and services is the provision of services by the general government sector. This component is expected to decrease in 2016-17 and 2018-19 compared to the previous years. The Department of Treasury and Finance advised the Committee that:<sup>276</sup>

The reduction in provision of services revenue in 2016-17 is primarily driven by the cessation of revenue for the administration of the *Advanced Lignite Demonstration Program*, which is managed by the State on behalf of both the State and the Commonwealth. This reduction is partially offset by an estimated increase in farebox revenue (revenue from fares). The reduction in revenue in 2018-19 relates to the expected reduction in revenue for the *CarbonNet* project in that year, relative to 2017-18.

**FINDING 35:** Sales of goods and services are expected to total \$6.8 billion in 2015-16, rising further to \$7.0 billion in 2017-18 and 2018-19. This is a much slower growth rate than occurred in recent years.

### 4.5.3 Dividends and similar revenue

This revenue item includes:

- dividends, which are payments made by government business enterprises in the public financial corporations (PFC) sector and public non-financial corporations (PNFC) sector to the general government sector, based on profits achieved by the enterprise
- payments equivalent to income tax and local government rates (intended to ensure that the enterprises, which are not subject to normal taxes and rates, do not have an unfair advantage over private sector companies).

<sup>273</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.7.

<sup>274</sup> *ibid.*, p.184.

<sup>275</sup> *ibid.*

<sup>276</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.6.

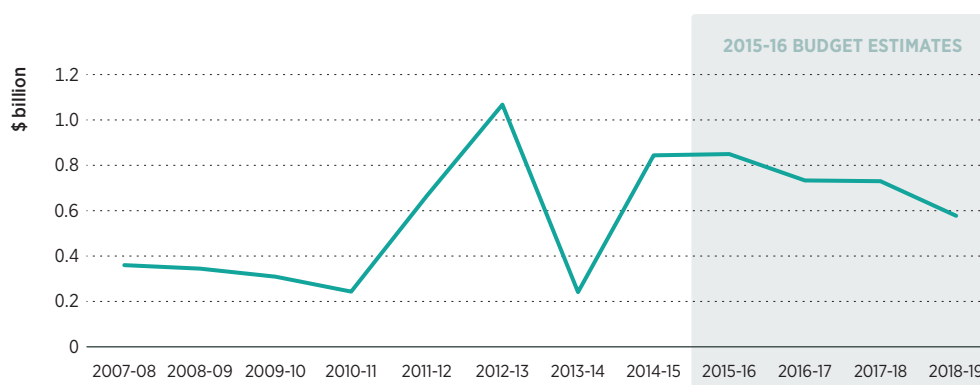
Dividends and similar are expected to provide \$1.14 billion in 2015-16 before falling slightly over the forward estimates to \$1.05 billion in 2017-18.<sup>277</sup>

## Dividends

Dividends are paid by some of the enterprises outside the general government sector. They reflect the Government's role as owner of these enterprises. The entities that pay dividends are predominantly water authorities and state-owned financial and insurance enterprises.<sup>278</sup> These entities raise most of their own revenue by charging clients for their services.

Figure 4.6 shows the level of dividends received by the general government sector from other sectors.

**Figure 4.6** Dividends, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.28, 237; Department of Treasury and Finance, *Financial Report*, 2009-10 to 2013-14.

Dividends have fluctuated from year to year in the past. However, the estimates in the budget papers are a more stable level, averaging \$722.6 million over the four years to 2018-19.<sup>279</sup> Figure 4.6 shows that dividends estimates over the forward estimates period are higher than all past years' payments since 2007-08 apart from 2012-13.

Over the forward estimates period, the two most significant contributors to dividends revenue are the Transport Accident Commission (TAC) and the Victorian Managed Insurance Authority (VMIA). Together, these entities are anticipated to provide two-thirds of the total dividends revenue.

<sup>277</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.7.

<sup>278</sup> Major entities that pay dividends are listed in the budget papers (Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28).

<sup>279</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28.

The level of dividends to be paid by an enterprise is determined twice each year based on a number of factors, including the enterprise's capacity to pay, considering factors such as profit and retained earnings. The Government's financial position is also considered when determining dividend payments.<sup>280</sup>

The Minister for Finance indicated that an 'economic funding ratio' was used to determine the capacity of entities to pay dividends in this budget. He explained that this is in addition to the 'accounting funding ratio', which:<sup>281</sup>

... is used as the standard, including in reporting, which includes the requirement of the Auditor-General to report based on the accounting standards.

Explaining the difference between the two ratios, the Minister commented that:<sup>282</sup>

The accounting funding ratio is determined based on the commonwealth bond yield used as a discount rate, which is at historic lows, while the economic funding ratio allows for the expected investment returns on scheme assets to determine the discount rate. Therefore the economic funding ratio is a more realistic indicator of the scheme's financial strength, particularly in times when we have got such low bond rates.

Informed by both funding ratios, the 2015-16 budget estimates include \$1.4 billion over four years in dividends from the Transport Accident Commission (TAC).<sup>283</sup> This is in addition to \$253.2 million from the TAC for 2014-15.<sup>284</sup>

The Minister expressed his view that the TAC was able to make these payments, commenting that:<sup>285</sup>

The TAC is also in a strong financial position, with a performance from insurance operations of \$325 million. The TAC's accounting funding ratio at 30 June 2014 was 91 per cent, and the economic funding ratio was 145.7 per cent.

The Minister further noted that charges for clients of the TAC are not expected to increase as a result of the expected dividends, stating that:<sup>286</sup>

... the increased dividends from the TAC will not result in increased charges to motorists.

The Committee notes that dividend payments from the TAC in 2016-17 and 2018-19 are expected to decrease.<sup>287</sup> This contributes to an overall downward trend in dividend revenue in the later part of the forward estimates.

<sup>280</sup> Department of Treasury and Finance, *Corporate Planning and Performance Reporting Requirements - Government Business Enterprises* (2009), section 7.1.1. Note that two versions of this document exist with identical text but different formatting.

<sup>281</sup> Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.6.

<sup>282</sup> *ibid.*, p.3.

<sup>283</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28.

<sup>284</sup> *ibid.*, p.237.

<sup>285</sup> Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.3.

<sup>286</sup> *ibid.*, p.7.

<sup>287</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28.

The budget estimates also include \$420.0 million in dividends from the Victorian Managed Insurance Authority (VMIA).<sup>288</sup> The Minister noted that this was the first time the VMIA had been required to pay a dividend, and that ‘this will bring the VMIA in line with other public financial corporations’.<sup>289</sup>

The Minister also commented that the agency had the capacity to pay the dividends, as it was:<sup>290</sup>

... in a strong financial position. The accounting funding ratio as at 30 June 2014 was 108 per cent and the economic funding ratio was 174 per cent.

The Government claims that there will be no impact of these dividends on clients of the VMIA. The Minister indicated that the issue had been raised in the Legislative Council.<sup>291</sup> The Minister for Training and Skills had remarked there that:<sup>292</sup>

The payment of dividends by VMIA will not result in any increase in premiums for VMIA’s clients. VMIA premiums are based on the estimated costs of claims incurred in the coming year. The payment of dividends has no impact on this.

In giving his evidence, the Minister for Finance noted that, in contrast to the TAC and the VMIA:<sup>293</sup>

Consistent with our election commitment, WorkSafe will not pay dividends in this budget.

The Committee notes that this policy differs from the previous government’s plans. As discussed in Section 4.4.2, previous budget estimates anticipated that WorkSafe (the Victorian WorkCover Authority) would pay dividends of \$535.1 million between 2015-16 and 2017-18.<sup>294</sup> The budget papers note that:<sup>295</sup>

Instead, the surplus accumulated will be used to fund improvements to benefits and access to benefits for injured workers, lower WorkCover premiums for Victorian businesses and programs to improve workplace safety and the health of the Victorian workforce.

The Government has a right to take dividends from PNFC and PFC entities because it is the owner of the entities. The money that comes to the Government from dividends contributes to the general government sector’s total revenue and may be used to fund service provision or may pass through the surplus to fund asset investment (see Figure 2.1). In addition, the Department of Treasury and

288 *ibid.*

289 Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.6.

290 *ibid.*, p.3.

291 *ibid.*, p.7.

292 *Victorian Parliamentary Debates*, Legislative Council, 7 May 2015, p.1342 (Hon. Steve Herbert MLC).

293 Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.3.

294 Calculations based on Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update (2014)*, p.44.

295 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook (2015)*, p.51.



Finance has stated that, 'Dividends/distributions to government are intended to reinforce the commercial focus of GBEs [government business enterprises] and ensure that GBEs operate with an optimal and efficient capital structure.'<sup>296</sup>

Whether or not an entity pays dividends, and how much it pays, is determined by the Government. The decision about whether or not to take dividends can have a major impact on the paying entity. As the revenue for these PNFC and PFC entities largely comes from charges to consumers, the decision about whether or not to take dividends can also have an impact on consumers.

For example, the Government expects that leaving profits with WorkSafe across the forward estimates period will provide a range of benefits for workers and businesses, as discussed above.

In some cases, dividend payments may have negative effects on some paying entities. Water authorities in particular require capital to fund renewals of infrastructure systems and new infrastructure to cope with population growth. If the payment of dividends leaves an enterprise without sufficient capital to fund its required asset investment, it may be required to find funding from other sources. While the general government sector may provide funding (see Section 2.4.1 of this report), the Auditor-General noted that there has been a:<sup>297</sup>

... correlation between the increase in borrowings to finance the construction of infrastructure assets and payment of dividends over the last five years.

The debt level of the PNFC sector is discussed further in Section 6.3.1 of this report.

In addition, the Auditor-General has commented, for State-controlled entities, that:<sup>298</sup>

... it appears that a sufficiently robust assessment of an entity's ability to pay dividends may not have been completed.

The Department of Treasury and Finance indicates that consideration is given to the circumstances of the paying entity as well as the Government's budget position when determining dividends.<sup>299</sup> The Department has listed a number of the factors which are considered<sup>300</sup> but the Committee considers that there is scope for more detailed disclosure around the Government's dividend policy. In particular, the Committee considers that there would be benefits from:

- a more detailed explanation of the framework used to determine dividends

<sup>296</sup> Department of Treasury and Finance, *Corporate Planning and Performance Reporting Requirements: Government Business Enterprises* (2009), section 7.

<sup>297</sup> Victorian Auditor-General's Office, *Water Entities: Results of the 2013-14 Audits* (2015), p.37.

<sup>298</sup> Victorian Auditor-General's Office, *Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2013-14* (2014), p.17.

<sup>299</sup> Department of Treasury and Finance, *Corporate Planning and Performance Reporting Requirements: Government Business Enterprises* (2009), section 7.1.1.

<sup>300</sup> Department of Treasury and Finance, *Corporate Planning and Performance Reporting Requirements: Government Business Enterprises* (2009), section 7.1.1; Department of Treasury and Finance, *FRD 03A: Accounting for Dividends* (2005), p.2.

- additional discussion of the basis for the Government's dividend decisions in any particular budget, including a discussion of the impact of dividend payments on the financial sustainability of paying entities.

This additional disclosure may help to address the Auditor-General's concerns and would provide the Parliament and the community with a clearer understanding of the Government's decisions. It may also provide more clarity for government-owned entities.

**FINDING 36:** Surpluses accumulated over the forward estimates period by WorkSafe are intended to be used to decrease premiums and to fund programs to benefit the Victorian workforce. Surpluses from other enterprises are intended to be passed to the Government as dividends. The Auditor-General has noted an increase in borrowings by water authorities to finance the construction of infrastructure assets at the same time that dividends have been taken by the general government sector.

**RECOMMENDATION 22:** The Government publish a detailed explanation of its dividend policy, identifying the factors considered in determining when it is best to leave profits with entities and when it is best to take them as dividends.

**RECOMMENDATION 23:** Future budget papers provide more detailed discussion about the estimated dividend payments included in the forward estimates. This discussion should explain why those amounts are considered appropriate and indicate the expected impact of dividend payments on the financial sustainability of paying entities. This should include a discussion of the effects on paying entities' abilities to carry out their infrastructure investment plans while meeting required dividend payments.

### Income tax equivalent payments

After dividends, the majority of 'dividends and similar revenue' is made up of income tax equivalent revenue.

Income tax equivalent payments are anticipated to be \$287.1 million in 2015-16, an increase of \$112.0 million from 2014-15.<sup>301</sup> This is expected to decrease between 2015-16 and 2016-17 and then grow over the remainder of the forward estimates period, reaching \$463.8 million by 2018-19.<sup>302</sup>

Income tax equivalent revenue is expected to increase by \$186.9 million (67.5 per cent) between 2017-18 and 2018-19. The Department of Treasury and Finance has previously commented that:<sup>303</sup>

<sup>301</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.28, 237.

<sup>302</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.28.

<sup>303</sup> Department of Treasury and Finance, *Response to the Committee's 2011-12 Financial and Performance Outcomes Questionnaire on the Annual Report*, received 28 February 2013, p.5.

The Government does not have discretion over the ITE revenue. The ATO administers the national tax equivalent regime in line with a memorandum of understanding with state and territory governments. The underlying tax paid by a government business enterprise will depend on their taxable profit.

The Committee notes that, consistent with previous years, the budget papers do not discuss the increase in revenue, or reveal assumptions on the taxable profits of government business enterprises for later years of the forward estimates period.

**FINDING 37:** The Government anticipates that income tax equivalent revenue will be \$287.1 million in 2015-16 and increase to \$463.8 million by 2018-19. It is expected to increase by 67.5 per cent in the last year of the forward estimates period. This change is not explained in the budget papers.

## 4.6 Grants from the Commonwealth Government

Revenue from Commonwealth Government grants is estimated to make up 45.8 per cent of Victorian general government sector revenue in 2015-16. This equates to \$25.4 billion (4.0 per cent more than in 2014-15). Commonwealth Government grants are expected to increase to \$28.5 billion in 2018-19.<sup>304</sup>

These grants are made up of:

- general-purpose (GST) grants, which represent Victoria's share of revenue from the goods and services tax collected and distributed by the Commonwealth Government (these may be spent in any manner chosen by the Victorian Government)
- specific-purpose grants, which are 'tied' in varying degrees to purposes determined by the Commonwealth Government.

### 4.6.1 General-purpose (GST) grants

General-purpose grants are expected to rise from \$12.0 billion in 2014-15 to \$12.8 billion in 2015-16.<sup>305</sup> They are then forecast to rise to \$15.8 billion by 2018-19.<sup>306</sup>

General-purpose grants are funded by GST revenues. These are collected by the Commonwealth Government in a central pool. Each year the Commonwealth Grants Commission calculates 'relativities' for each state, which are intended to reflect the states' abilities to raise their own revenue and provide required services. Together with population estimates, these relativities determine the share of the total pool that is distributed to each state.

<sup>304</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.171.

<sup>305</sup> *ibid.*

<sup>306</sup> *ibid.*

The principal factors that determine the value of general-purpose grants allocated to the State are therefore:

- the overall size of the GST pool
- Victoria's population (as a proportion of Australia's population)
- variations in Victoria's relativity.

The budget papers include a useful graph showing the relative contributions of these factors to the growth in Victoria's estimated GST grants revenue.<sup>307</sup> Factors used in calculating the 2015-16 budget estimates are shown in Table 4.7 below.

**Table 4.7** Calculation of Victoria's GST revenue estimates, 2014-15 to 2018-19

	2014-15	2015-16	2016-17	2017-18	2018-19
Pool size (\$ billion) <sup>(a)</sup>	54.6	57.3	60.4	63.7	67.4
GST relativity for Victoria	0.88282	0.89254	0.88362	0.90272	0.94133
Victoria's population share (per cent)	24.9	24.9	24.9	24.9	25.0
General-purpose grants for Victoria (\$ billion)	12.0	12.8	13.4	14.4	15.8

(a) Calculated by the Committee.

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.171-2.

Table 4.7 shows that the anticipated growth in general-purpose grants is primarily a result of growth in pool size and a more advantageous relativity for the State.

The budget papers list factors that have led the Department of Treasury and Finance to make these estimates, including an increase in income and consumption, short-term growth in dwelling investment and longer-term growth in export quantities for the mining states.<sup>308</sup>

Forecasts of Victoria's relativities take into account recent changes in the methodology of calculating shares for states. The budget papers note that the main impact of these changes for Victoria are the recognition of additional costs for urban infrastructure and a more consistent treatment of transport infrastructure payments from the Commonwealth Government to the states.<sup>309</sup>

**FINDING 38:** The Government expects that general-purpose (GST) grants from the Commonwealth Government will rise to \$12.8 billion in 2015-16, before rising further to \$15.8 billion by 2018-19. This is driven by expectations of increased GST pool size and a more favourable GST relativity.

<sup>307</sup> *ibid.*, p.173.

<sup>308</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.52.

<sup>309</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.172; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.15.

## 4.6.2 Specific-purpose grants

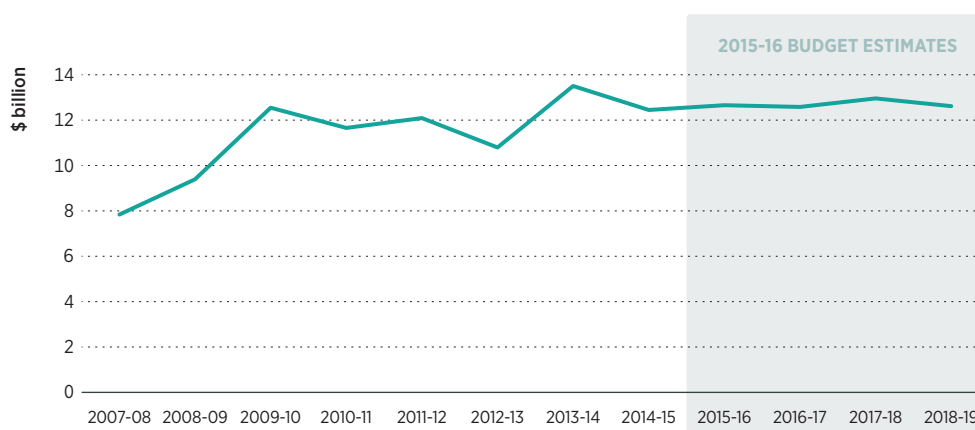
Revenue from specific-purpose grants is anticipated to rise to \$12.7 billion for 2015-16. This is an increase of \$209.9 million (1.7 per cent) over the revised estimate for 2014-15.

The Committee notes that this includes \$300.0 million expected to be paid by the Commonwealth Government in 2015-16 which was initially intended for the cancelled *East West Link* project.<sup>310</sup> The budget papers note that, ‘Negotiations are in progress with the Commonwealth Government on the allocation of the funding to other infrastructure projects’.<sup>311</sup> The budget papers also note that this and other funding for the *East West Link* has not been recognised as a liability in the Victorian budget papers.<sup>312</sup> In contrast, the Commonwealth Government assumed that it would not be paying the \$300.0 million in its 2015-16 Budget, though it indicated that it will supply the money if the project proceeds and is willing to consider investing in other infrastructure projects in Victoria.<sup>313</sup>

Although the Victorian budget papers indicate that negotiations are in progress regarding this funding, they do not specify what the money will be spent on if the negotiations are successful nor what the impact would be on the budget estimates if negotiations are unsuccessful.

Overall, the budget estimates assume no growth in specific-purpose grants over the forward estimates period, with revenue forecast to fall slightly to \$12.6 billion in 2018-19 (see Figure 4.7).<sup>314</sup>

**Figure 4.7** Specific-purpose grants, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.171; Department of Treasury and Finance, *Financial Report, 2007-08 to 2013-14*.

<sup>310</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.47.

<sup>311</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.182.

<sup>312</sup> *ibid.*, p.21.

<sup>313</sup> Commonwealth of Australia, *Budget Paper No.2: Budget Measures 2015-16* (2015), p.133

<sup>314</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.171.

Figure 4.7 shows that revenue from specific-purpose grants has shown an upward trend since 2007-08. However, over the forecast period, the budget papers indicate a flatter trend.

The budget papers note that a number of factors have contributed to this assumption.<sup>315</sup>

The budget papers indicate that specific-purpose grants are expected to decrease between 2015-16 and 2016-17 with the roll-out of the National Disability Insurance Scheme.<sup>316</sup>

... primarily due to the agreed transfer of responsibilities under the Home and Community Care National Partnership from Victoria to the Commonwealth.

With regard to health-related grants, the Commonwealth Government budget papers note that:<sup>317</sup>

From 1 July 2017, the Commonwealth will index its contribution for public hospitals funding by the Consumer Price Index and population growth. This approach ensures public hospitals funding growth is more sustainable.

This is a change from the current system whereby the increase in grants was determined by activity levels in public hospitals and an independently determined 'national efficient price'.<sup>318</sup>

Regarding schools, the 2014-15 Commonwealth Government Budget included an amount that provided for increased funding over time. However, it noted that:<sup>319</sup>

From the 2018 school year onwards, total school funding will be indexed by the Consumer Price Index, with an allowance for changes in enrolments.

This is a change from the model used for funding prior to 2018. Under the National Education Reform Agreement (referred to as the Gonski Agreement), a specific amount was provided for each school student, with a series of additional amounts for schools and students meeting specific criteria.<sup>320</sup>

The effect of this change has been to reduce the anticipated rate of growth of amounts paid to the State after 2016-17. According to the Minister for Education:<sup>321</sup>

<sup>315</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.163.

<sup>316</sup> *ibid.*, p.163. This transfer of responsibilities is also noted in the Commonwealth Government budget papers (Commonwealth of Australia, *Budget Paper No.3: Federal Financial Relations 2015-16* (2015), p.42) and Department of Treasury and Finance, *Response to the Committee's Budget Estimates Specific Questionnaire*, received 19 August 2015, p.6.

<sup>317</sup> Commonwealth of Australia, *Budget Paper No.3: Federal Financial Relations 2015-16* (2015), p.12.

<sup>318</sup> *ibid.*

<sup>319</sup> Commonwealth of Australia, *Budget Paper No.2: Budget Measures 2014-15* (2014), p.91.

<sup>320</sup> Commonwealth of Australia, *Budget Paper No.3: Federal Financial Relations 2013-14* (2013), p.53.

<sup>321</sup> Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015, p.5.

There will be money that will flow through from the commonwealth in those years – 2018, 19 – but at a much lower rate, so there will be a level of indexation. The difference between what the commonwealth has now put on the table and what was agreed to under the Gonski national agreement – the difference over 18-19 – is around \$1 billion for Victorian schools.

However, the Commonwealth budget papers note that:<sup>322</sup>

... final allocations from the 2018 school year onwards are subject to formal negotiations between the Commonwealth, the states and the non-government sector.

The Committee considers that the flatter trend forecast for specific-purpose grants as a whole may also be a result of forecasting methods used by the Department of Treasury and Finance. Specific-purpose grants regularly change, with some grants expiring in a year and new ones being released by the Commonwealth Government. As discussed in Section 4.3.2, the budget estimates factor in the expiration of grants but do not include any amounts for the value of new grants. As a result, the actual value of specific-purpose grants received by Victoria across the forward estimates period is likely to be higher than the budget estimates.

**FINDING 39:** Specific-purpose grants are expected to be \$12.7 billion in 2015-16. The budget estimates assume no growth over the forward estimates period, despite a long-term trend of growth. The budget papers attribute this to the transfer of some aged care expenditure to the Commonwealth, changes in agreements for indexing grants and expiring fixed-term programs. The Department of Treasury and Finance’s methodology for estimating specific-purpose grants may also have underestimated the value of grants over the forward estimates period.

<sup>322</sup> Commonwealth of Australia, *Budget Paper No.3: Federal Financial Relations 2015-16* (2015), p.30.





# 5

## Parliamentary control over departmental revenue

### 5.1 Introduction

The Victorian Parliament has ultimate authority in determining how public money is spent. The Parliament exercises this authority mainly through the annual appropriation bills, which give the Government the authority to spend the money during the year. The Parliament also delegates authority to others, such as the Treasurer and the Minister for Finance, to authorise some payments.<sup>323</sup> The authorisation of the Government to spend public money is referred to as appropriations.

This chapter examines the appropriations system, looking at:

- How are the Government and its departments able to access funding, and to what extent are the intended uses specified? (Section 5.2)
- To what extent does the Parliament control the resources available to the Government, and how has this changed over time? (Section 5.3)
- How well are the uses of funding specified in the budget papers and annual reports? (Section 5.4)
- What happens when goods and services are provided by departments to the satisfaction of the Government, but the actual cost of delivering those goods and services was less than agreed? (Section 5.5)

It should be noted that the appropriations system describes the State's finances in a different way to the financial statements, which are the basis for most other chapters of this report. The connections between the appropriations system, the budget papers and the reporting framework are explored through this chapter.

### 5.2 Sources of funding

Government money is held in three different places. The first two of these are:

- the Consolidated Fund, from which departments receive money through annual appropriations<sup>324</sup> (in the appropriations acts each year) and special appropriations (authorised in various other acts)
- the Trust Fund, which holds money that is intended for specific purposes.

<sup>323</sup> Such as Treasurer's Advances, payments from the Trust Fund and payments from outside the Public Account.

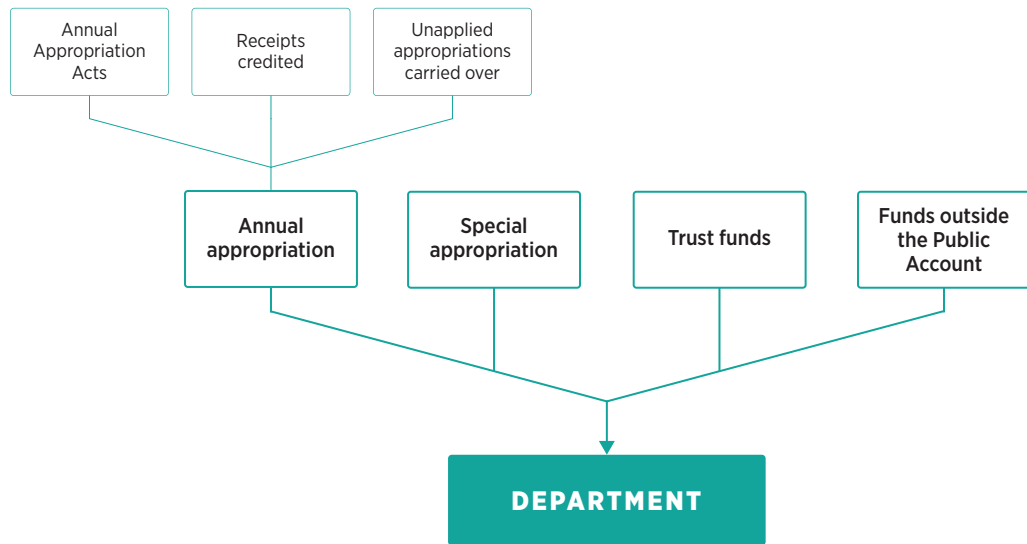
<sup>324</sup> Annual appropriations also include 'receipts credited to appropriations' (revenue that is received from an external source and that the Treasurer has agreed that the department may retain) as well as unapplied appropriations that have been carried over from the previous year.

Taken together, the Consolidated Fund and the Trust Fund are known as the Public Account.<sup>325</sup> In addition, government money is also held in:

- funds outside the Public Account.

These sources are illustrated in Figure 5.1.

**Figure 5.1** Sources of funds for a department under the appropriations system



Source: Public Accounts and Estimates Committee.

Only annual appropriations and special appropriations require the agreement of the Parliament in acts. The Minister for Finance or the Treasurer has the authority to provide funding from the other sources to departments (see Appendix A5.1 for details). These appropriations, under delegated authority from the Parliament, do not require the Government to apply to the Parliament for authority in each case. In this way, they provide the Government with a significant level of autonomy and flexibility.

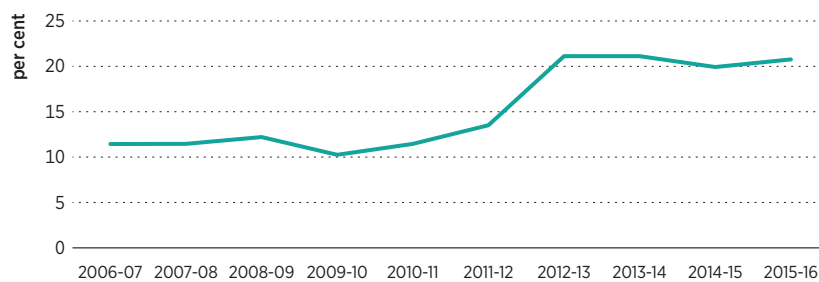
After the budget, departments may find that they require more money to carry out their tasks than initially anticipated. The Treasurer has further resources that may be distributed without having to ask the Parliament for approval. This provides the Government further flexibility in a range of circumstances (see Appendix A5.2).

325 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.205.

### 5.3 The level of parliamentary control

Section 5.2 notes that some departmental funding is made under the direct authority of the Parliament. Other funding is provided by the Treasurer or Minister for Finance under the delegated authority of the Parliament. The share of funding provided to departments through this second, more flexible, group has nearly doubled over the past decade. This is shown in Figure 5.2.

**Figure 5.2** Proportion of total income from transactions for departments not provided through annual or special appropriations, 2006-07 to 2015-16



Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2006-07 to 2015-16.

The figure shows that, before 2012-13, departments typically received between 11 and 14 per cent of their funding from these more flexible sources. However, since 2012-13, this share has risen to around 21 per cent, and is expected to remain at this level in 2015-16.<sup>326</sup>

The Department of Treasury and Finance explained to the Committee that this shift is mostly due to a changed model for health funding.<sup>327</sup>

Prior to 2012-13, payments from [the] Commonwealth for National Health Care Specific Purpose Payment (SPP) were paid into the State's consolidated fund and then appropriated to Department of Health as annual appropriation. From 2012-13, National Health Care SPP ceased and the National Health Reform commenced and funds were paid directly into a Health Funding Pool administered by the Department of Health, as per the new agreement. This resulted in a reduction in appropriation revenue to the Department of Health but a commensurate increase in grants income.

The Committee considers that an explanation of the increase should have appeared in the budget papers. This would assist members of Parliament with their consideration of the appropriation bills. It would also enhance transparency, explaining the Government's strategy and options.

<sup>326</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), pp.125, 172, 198, 223, 270, 298, 319, 335, 344.

<sup>327</sup> Department of Treasury and Finance, *Response to the Committee's Budget Estimates 2015-16 Specific Questionnaire*, received 19 August 2015, p.7.

**FINDING 40:** The budgetary appropriations system provides the Government with a number of methods to access public money. Some of these methods require direct Parliamentary authority, while others are determined by the Treasurer or Minister for Finance. The proportion of total income for departments that is not determined directly by the Parliament has increased from between 11 and 14 per cent to around 21 per cent due to changes in health funding from the Commonwealth Government. The budget papers have not discussed this change.

**RECOMMENDATION 24:** Future budget papers note the proportion of revenue that comes from annual and special appropriations compared to other sources and explain any significant changes in this proportion from previous years.

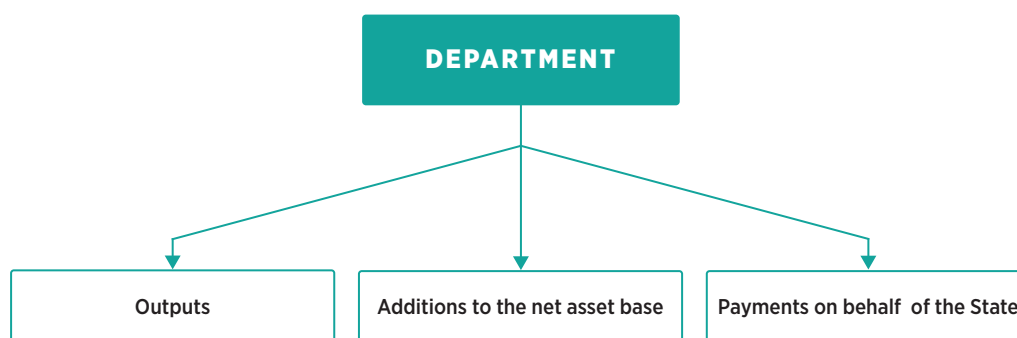
## 5.4 Specifying how departments use funding

In the appropriations context, money is allocated to departments for one of three purposes:<sup>328</sup>

- the provision of outputs (that is, the delivery of services)
- additions to the net asset base (asset investment)
- payments on behalf of the state (funding passed on to other bodies).

These are illustrated in Figure 5.3.

**Figure 5.3** Uses of funds for a department under the appropriations system



Source: Public Accounts and Estimates Committee.

As mentioned in Section 5.1, this represents a different view of the State's expenses to other parts of the budget papers.<sup>329</sup>

The extent to which these uses are specified and reported on differs between the different methods of funding.

<sup>328</sup> Department of Treasury and Finance, *BFMG - 19: Appropriations (2007)*, p.20.

<sup>329</sup> Which classify expenses into wage costs, grants, depreciation, etc.

### 5.4.1 Annual and special appropriations

Annual appropriations are the main source of funding for most departments. The value of each department's annual appropriation is determined by the Parliament every year in the appropriation acts. Special appropriations are authorised by the Parliament through other acts. These acts may authorise appropriations to a department over a number of years.

The Committee considers there to be good mechanisms in place for describing the intended and actual uses of annual appropriations.

Before the start of the year, the budget papers set out the intended uses for annual appropriations.<sup>330</sup> The portion intended for output provision is included as a line item in each department's operating statement.<sup>331</sup> At the end of the year, departments' annual reports set out the way the funding was used, including any changes that were made after the budget. Variances between the adjusted estimates and the amounts 'applied' (that is, actually paid to the departments) are also disclosed and explained.<sup>332</sup>

Because of this, the Committee considers that annual appropriations are highly transparent. The Parliament and the community are able to understand the initial intentions for the funding, how the intentions changed through the year, and why any differences occurred.

The same level of detail is not provided for special appropriations. Budget Paper No.5 includes a list of all special appropriations, showing the various acts under which the appropriations are made, and the amount of each individual appropriation.<sup>333</sup> Special appropriations for output provision are included as a line item in departments' operating statements. However, special appropriations are not broken down into the three potential uses in the same way as annual appropriations.

Annual reports are required to quantify special appropriations that were applied during the year.<sup>334</sup> However, while a general description of the purpose is required, no indication is required as to whether these were for the provision of outputs, additions to the net asset base or payments on behalf of the State.

The Committee considers that enhancing the disclosure of special appropriations to match annual appropriations would provide for improved transparency in this area.

**FINDING 41:** Annual appropriations are well disclosed, both before and after the financial year. The uses for which special appropriations are intended are not fully disclosed in either the budget papers or departments' annual reports.

<sup>330</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.215-7.

<sup>331</sup> For example, Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.88.

<sup>332</sup> Department of Treasury and Finance, *FRD 13: Disclosure of Parliamentary Appropriations* (2003), p.2.

<sup>333</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.211-4.

<sup>334</sup> Department of Treasury and Finance, *FRD 13: Disclosure of Parliamentary Appropriations* (2003), p.2.

**RECOMMENDATION 25:** Future budget papers specify how much of each special appropriation is intended to fund:

- (a) the provision of outputs
- (b) additions to the net asset base
- (c) payments made on behalf of the State.

**RECOMMENDATION 26:** The Department of Treasury and Finance require departments, in annual reports, to disclose the amounts received in special appropriations that are used in:

- (a) the provision of outputs
- (b) additions to the net asset base
- (c) payments made on behalf of the State.

Any variances between the purpose set out in the budget papers and the actual use should be identified and explained.

#### 5.4.2 The Trust Fund and funds outside the Public Account

As discussed in Section 5.2, a share of departments' income comes from the Trust Fund and funds received and held outside the Public Account. The Committee notes in Section 5.3 that these sources are increasing as a proportion of departmental income. However, the amounts contributed by each of these sources to departments' operating revenue are not separately disclosed in the budget papers each year. The Committee considers that linking the funding from these sources to the operating statements would provide a clearer understanding to the Parliament and the community of how departments are being funded.

**FINDING 42:** In contrast to annual appropriations and special appropriations, the contributions of funds received and held outside the Public Account and the Trust Fund to the operating statement are not disclosed in the budget papers.

**RECOMMENDATION 27:** Future budget papers specify the anticipated contributions from funds received and held outside the Public Account and the Trust Fund to departments' operating statements.

#### The Trust Fund

The Trust Fund is made up of individual trust accounts, established for different purposes as needed. In many cases, trust accounts are established to receive money from external sources, such as Commonwealth Government grants or clients of a department. The Department of Treasury and Finance listed 88 trust accounts in September 2015.<sup>335</sup>

<sup>335</sup> Correspondence from the Department of Treasury and Finance, received 9 September 2015.

As has been the case in past budgets, this year's budget papers indicate the aggregate amounts that each department is authorised to spend from trust accounts.<sup>336</sup> However, the intended uses<sup>337</sup> for these amounts are not specified. In addition, the budget papers do not break down the aggregate amount into the individual accounts.

In annual reports, like the budget papers, there is no requirement that departments specify how they used revenue from the trust accounts. Departments are required to report total receipts and payments for individual trust accounts.<sup>338</sup> However, as the budget papers do not specify the amount of funding expected from individual accounts before the start of the year, the Parliament and the community are not able to compare the actual amounts to what was anticipated at the time of the budget.

The Committee considers that, for transparency and accountability, variances between expected and actual results for each account should be compared and reasons for the variances explained. This requires a system that discloses expected results at the time of the budget and corresponding reporting at the end of the year.

**FINDING 43:** As in previous years, the budget papers do not disclose the amounts expected to flow from individual trust accounts to departments or the intended purpose of funding appropriated from trust accounts. Annual reports do not specify the uses that funding from trust accounts were put to.

**RECOMMENDATION 28:** Future budget papers specify the amounts expected from each trust account for each department.

**RECOMMENDATION 29:** Future budget papers specify the intended purpose (provision of outputs, additions to the net asset base, or payments on behalf of the State) of money received by departments from trust accounts.

**RECOMMENDATION 30:** The Department of Treasury and Finance require departments, in their annual reports, to disclose their income from the Trust Fund, broken down into the provision of outputs, additions to the net asset base and payments made on behalf of the State. Any variances between the initial budget estimates and the actual amounts should be identified and explained.

### Funds outside the Public Account

The Department of Treasury and Finance notes that departments also receive income from funds received and held outside the Public Account,<sup>339</sup> such as State school bank accounts.<sup>340</sup>

<sup>336</sup> For example, Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.198.

<sup>337</sup> That is: provision of outputs; additions to the net asset base; or payments on behalf of the state.

<sup>338</sup> Department of Treasury and Finance, *2014-15 Model Report for Victorian Government Departments* (2015), pp.290-1.

<sup>339</sup> Department of Treasury and Finance, *BFMG - 19: Appropriations* (2007), p.21.

<sup>340</sup> Victorian Auditor-General's Office, *Parliamentary Control and Management of Appropriations* (2003), p.23.

Historically, the contribution from funds received and held outside the Public Account has not been separately disclosed in either the budget papers or in departments' annual reports. Rather, it contributes unknown amounts to a number of other line items. The Financial Report for the State does disclose the balance of funds held outside the Public Account at the end of the year, but not the amounts flowing into and out of these accounts.<sup>341</sup> Simply put, there is no indication given anywhere as to how much money flows to departments from outside the Public Account.

The Committee considers that an understanding of the amounts flowing to departments from funds held outside the Public Account is a critical part of departmental transparency and accountability.

**FINDING 44:** The contribution from funds received and held outside the Public Account is not separately disclosed in either the budget papers or in departments' annual reports.

**RECOMMENDATION 31:** Future budget papers separately detail the income expected from funds held outside the Public Account for each department, broken down into the provision of outputs, additions to the net asset base and payments made on behalf of the State.

**RECOMMENDATION 32:** The Department of Treasury and Finance require departments, in their annual reports, to disclose their income from funds held outside the Public Account, broken down into the provision of outputs, additions to the net asset base and payments made on behalf of the State. Any variances between the initial budget estimates and the actual amounts should be identified and explained.

## 5.5 Applied appropriations unspent

Since 1998-99, the State's financial management system has been based on the 'funder-purchaser-provider' model.<sup>342</sup> The Government acts as the funder, deciding what 'outputs' (goods and services) it wishes to have delivered and providing funding. In addition to their role as part of the Government, Ministers also act with departmental secretaries and departments as 'purchasers', and are tasked with managing the provision of the outputs in the most efficient and effective manner. This may involve departments or other government entities delivering the outputs or it may involve paying the private sector to deliver them. The bodies that actually deliver the outputs are classified as 'providers'.

<sup>341</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.186.

<sup>342</sup> Department of Treasury and Finance, *Reform of the Budget Sector: Elements of Financial Management* (1997), pp.10-11.



Under this model, the Government and the purchaser agree on the price<sup>343</sup> to be paid for the goods and services in advance of their delivery. When the Government is satisfied that the outputs have been delivered, the agreed amounts are paid to the department.<sup>344</sup> These amounts are referred to as ‘applied appropriations’.<sup>345</sup>

Departments can often deliver the outputs for less than the price agreed with the Government. There are a number of reasons for this. Some costs included in the output price (such as depreciation) may not have associated expenditure in a particular year. Departments may also find cheaper ways to deliver outputs.

In these cases, the agreed amount is still ‘applied’, meaning the department receives the full payment. The difference between the amount paid and the amount spent in a year is referred to as ‘applied appropriations unspent’. The Department of Treasury and Finance indicated that the major components of this include:<sup>346</sup>

... payables and accruals related to employee entitlements and other liabilities; as well as accumulated prior years’ surpluses and depreciation equivalent revenue.

With the permission of the Treasurer, the applied appropriations unspent may be used by the department to fund projects in the future.<sup>347</sup> The Auditor-General discussed this in a past report, noting that:<sup>348</sup>

These funds are available, without further parliamentary approval, for application towards the payment of creditors and other liabilities, the financing of asset replacements (reinvesting to maintain asset capacity as reflected in depreciation expenses), or the delivery of additional outputs – where surpluses are available from previous service delivery.

The Auditor-General noted in 2003 that the accumulated amount of applied appropriations unspent had been increasing, and at that time had reached \$1.6 billion.<sup>349</sup> As a result, the Auditor-General recommended the establishment of an upper limit on surpluses retained by departments.<sup>350</sup>

Figure 5.4 shows that applied appropriations unspent have continued to rise since the Auditor-General’s comments, consistently increasing over the past decade. At 30 June 2014, applied appropriations unspent totalled \$5.1 billion.<sup>351</sup>

<sup>343</sup> As well as other specifications of the output in terms of quantity, quality and timeliness of delivery.

<sup>344</sup> Department of Treasury and Finance, *BFMG - 19: Appropriations* (2007), p.23. It should be noted that this transfer does not remove the funds from the Consolidated Fund.

<sup>345</sup> Department of Treasury and Finance, *BFMG - 19: Appropriations* (2007), p.23.

<sup>346</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.6.

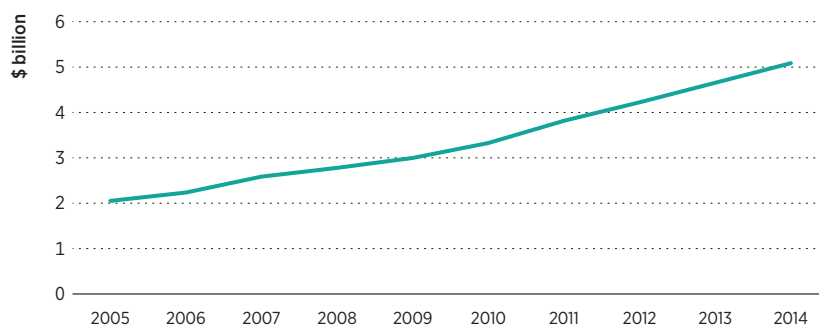
<sup>347</sup> Department of Treasury and Finance, *BFMG - 39: Departmental Surpluses/Deficits* (2009), pp.182-3.

<sup>348</sup> Victorian Auditor-General’s Office, *Parliamentary Control and Management of Appropriations* (2003), p.40.

<sup>349</sup> Victorian Auditor-General’s Office, *Parliamentary Control and Management of Appropriations* (2003), p.40; Department of Treasury and Finance, *2001-02 Financial Report for the State of Victoria* (2002), p.115.

<sup>350</sup> Victorian Auditor-General’s Office, *Parliamentary Control and Management of Appropriations* (2003), pp.40-1.

<sup>351</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.183.

**Figure 5.4** Applied appropriations unspent, 2005 to 2014<sup>(a)</sup>

(a) Balances at 30 June each year.

Source: Department of Treasury and Finance, *Financial Report 2004-05 to 2013-14*.

When asked about the strategy behind growing this balance, including the intended use of the funds, the Department of Treasury and Finance informed the Committee that:<sup>352</sup>

Balances for employee entitlements are a large contributor to growth over time. These are expected to grow annually consistent with increases in the value of employee entitlements due to wages and service growth; and accumulating long service leave provisions, which typically augment at a value greater than is paid out each year. These liabilities are paid out as employees leave the workforce, or otherwise draw on their leave entitlements.

Other payables, particularly related to the capital program, can also contribute to year-end SAU balances. These are generally a matter of timing, and will be progressively paid out as the payables fall due.

Amounts related to accumulated surpluses and depreciation equivalent revenue will be available as a potential funding source for future budget decisions, consistent with the financial management framework.

This response explains the growth and intended use of the employee entitlements and payables components. However, the extent to which the other components are growing and the reasons for that growth remain unclear.

The Committee notes that this is a potentially large source of income for departments but is not discussed in the budget papers. The Committee considers that future budget papers would be improved by indicating the value of funding available from this source, indicating how it is expected to change over the forward estimates period and explain why those changes are planned.

The Committee notes that the value of applied appropriations unspent grew by an average of 10.6 per cent per year between 2005 and 2014.<sup>353</sup> This is a rapid rate of growth compared to many other variables in the State's finances, which the Committee considers should be explained.

<sup>352</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.6.

<sup>353</sup> Committee calculation based on Department of Treasury and Finance, *2004-05 Financial Report* (2005), p.128; Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.183.

**FINDING 45:** When the cost of delivering an output in a year is lower than the price agreed with the Government, the unspent portion of the agreed price may be spent by the department in the future, with the permission of the Treasurer. Departments have consistently accumulated these amounts over the last decade, with ‘applied appropriations unspent’ totalling \$5.1 billion at 30 June 2014.

**RECOMMENDATION 33:** In future budget papers, the Department of Treasury and Finance:

- (a) note the total value of accumulated applied appropriations unspent, broken down into the major components (including payables, accruals related to employee entitlements, prior years’ surpluses and depreciation equivalent revenue)
- (b) indicate the estimated change to these values over the forward estimates period
- (c) indicate the reasons for the anticipated changes for each component.



# 6 Borrowings, debt and liabilities

## 6.1 Introduction

As discussed in Section 2.2.1, the Government's operating surplus is a source of cash for its asset investment program. This is supplemented by the cash available through non-cash allowances such as depreciation, proceeds from asset sales and cash inflows from investment through other sectors. However, if the Government requires a higher level of asset investment than the amount of cash available, it must cover the difference by borrowing.

When the Government commences payments for public private partnership (PPP) projects, future payments are also added to borrowings.<sup>354</sup>

Borrowing (and associated debt) can be a useful way of expanding assets beyond the amount allowed by operating cash. However, debt must not only be repaid, but interest on the debt must also be paid. Many factors go into deciding the appropriate level of debt at any point in time.

The Committee does not have a view on the appropriate level of debt. However, it notes that the Government has set targets for what it considers to be appropriate (see Section 6.2).

Table 6.1 sets out the levels of net debt<sup>355</sup> that the budget papers anticipate over the forward estimates period. Net debt is expected to decline by \$4.3 billion in 2015-16 following the proposed lease of the Port of Melbourne's operations. It is then expected to increase by \$2.4 billion in 2016-17 and by smaller amounts in the two following years. This is further discussed in Section 6.3.1.

This chapter will examine the following aspects of borrowings, debt and other liabilities:

- What are the Government's strategies for debt and liabilities? (Section 6.2)
- What are the expected levels of debt and borrowings over the forward estimates period? (Section 6.3.1)
- What are the Government's plans for the unfunded superannuation liability? (Section 6.3.2)
- How do the latest estimates compare with those from previous budgets? (Section 6.4)

<sup>354</sup> The value of these payments is reduced to the 'present value', that is, an estimate of how much money would need to be held today to make all of the payments in the future, factoring in interest that would accrue to that money over the term of the lease.

<sup>355</sup> Net debt is the value of financial liabilities less the value of assets that are readily convertible to cash, or 'the sum of deposits held, advances received and borrowings less the sum of cash, deposits, advances paid and investments, loans and placements' (Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.62).

**Table 6.1** General government sector net debt, 2015 to 2019<sup>(a)</sup>

	2015 revised estimate	2016 Budget	2017 estimate	2018 estimate	2019 estimate
Net debt (\$ million)	21,240.0	16,897.8	19,259.0	19,450.2	19,834.7
Annual growth					
• (\$ million)	65.4	-4,342.2	2,361.2	191.2	384.5
• (per cent)	0.3	-20.4	14.0	1.0	2.0
Average annual growth rate (June 2016 to June 2019) (per cent) <sup>(b)</sup>			5.5		

(a) Balances at 30 June each year.

(b) Compound annual growth rate. Calculated by the Committee.

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.9, 227.

The primary focus of this chapter will be borrowings and net debt for the general government sector. It will also discuss borrowings and net debt for the public non-financial corporations (PNFC) sector, as this sector carries a significant amount of debt. However, the chapter will not examine the public financial corporations (PFC) sector. The PFC sector largely acts as a financial vehicle or intermediary in the financial markets for the other two sectors, so results in this sector are a reflection of the other sectors.

## 6.2 The Government's strategy

The budget papers provide a way for the Government to communicate and explain its fiscal strategy for the upcoming years. This assists the Parliament to understand details of the Government's plans. As described in Section 2.3.2, this includes a series of financial management targets, including:<sup>356</sup>

- reducing general government sector net debt as a proportion of gross state product between 2015 and 2019 (see Section 6.3.1)
- fully funding the unfunded superannuation liability by 2035 (see Section 6.3.2).

The financial management target for net debt relates exclusively to general government sector debt. However, the Committee notes that net debt for the PNFC sector for June 2015 is expected to be \$14.9 billion, which is only \$6.3 billion (or 29.8 per cent) less than the net debt for the general government sector.<sup>357</sup> Despite this, the budget papers do not include a target for PNFC net debt. This means that the Government has not indicated what its plans are for a large proportion of the debt held by the State.

<sup>356</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.20.

<sup>357</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.9, 51.

The Committee considers that the introduction of a target for net debt in the PNFC sector would therefore be beneficial. Such a target and associated discussion in the budget papers would allow the Parliament and the community to understand whether the debt level in the sector was considered high or low, as well as the Government's intentions over the medium term.

**FINDING 46:** The Government has set a target of reducing net debt as a proportion of gross state product for the general government sector. However, the Government has not set a target for net debt in the public non-financial corporations sector, although that sector's net debt is also a significant amount. The Government's plans for net debt are therefore not comprehensively disclosed.

**RECOMMENDATION 34:** Future budget papers include a target for net debt in the public non-financial corporations sector.

## 6.3 Estimates for debt and liabilities

### 6.3.1 Borrowings and net debt

As described in Section 2.4.4, the budget papers anticipate that net debt for the general government sector will fall by June 2016, but will then rise in each of the following years of the forward estimates period. In contrast, estimates for the PNFC sector show net debt rising over the whole of the period to June 2019.

#### General government sector

The budget papers forecast that general government sector net debt as a proportion of gross state product (GSP) will decrease to 4.4 per cent in June 2016 (from a revised estimate of 5.8 per cent for June 2015). Over the following two years, the budget papers anticipate that this proportion will increase, but will return to 4.4 per cent by June 2019.<sup>358</sup> This is in line with the Government's target (see Section 6.2).<sup>359</sup> This is discussed further in Section 2.4.4.

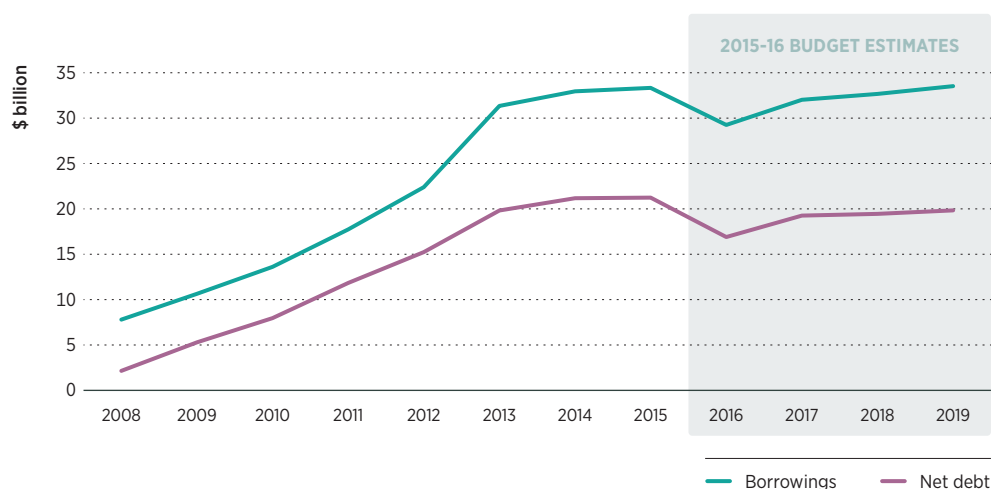
Figure 6.1 shows borrowings and net debt for the general government sector in dollar terms rather than as a proportion of GSP. The figure shows that net debt has been increasing steadily since 2008. The 2015-16 budget papers include a revised estimate for net debt for June 2015 of \$21.2 billion, with borrowings estimated at \$33.3 billion.<sup>360</sup> As a result of this level of borrowings, interest expense for 2015-16 is estimated to be \$2.1 billion.<sup>361</sup>

<sup>358</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.13, 44.

<sup>359</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.20.

<sup>360</sup> *ibid.*, p.9.

<sup>361</sup> *ibid.*, p.7.

**Figure 6.1** Borrowings and net debt, general government sector, 2008 to 2019<sup>(a)</sup>

(a) Balances at 30 June each year.

Source: Department of Treasury and Finance, *Financial Report, 2008-09 to 2013-14*; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances (2015)*, pp.9, 51.

The Government intends to decrease net debt through the proposed lease of the Port of Melbourne's operations (see Section 8.2.3). As a result of the lease, the Government expects to pay back some of its borrowings during 2015-16. By June 2016, borrowings are anticipated to have fallen to \$29.2 billion, with net debt at \$16.9 billion.<sup>362</sup>

However, after this, net debt is expected to rise, as cash flows anticipated from operating activities are insufficient to provide for planned net asset investment and PPP commissioning so that increased borrowings are necessary.<sup>363</sup> By June 2019, net debt is anticipated to be \$19.8 billion, with borrowings at \$33.5 billion.<sup>364</sup>

The Committee notes that, while the level of net debt expected for the general government sector in 2019 is lower than its expected 2015 level, the level of borrowings in 2019 is higher than that anticipated for 2016.

**FINDING 47:** The Government expects that the proposed Port of Melbourne lease will result in general government sector borrowings decreasing to \$29.2 billion and net debt decreasing to \$16.9 billion by June 2016. After this, borrowings and net debt are expected to rise, reaching \$33.5 billion and \$19.8 billion respectively by June 2019.

### Public non-financial corporations sector

As noted above, the Government's published strategy for net debt is confined to the general government sector. However, the PNFC sector also holds a significant amount of net debt.<sup>365</sup>

<sup>362</sup> *ibid.*, p.9.

<sup>363</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook (2015)*, p.59.

<sup>364</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances (2015)*, p.9.

<sup>365</sup> *ibid.*, p.51.



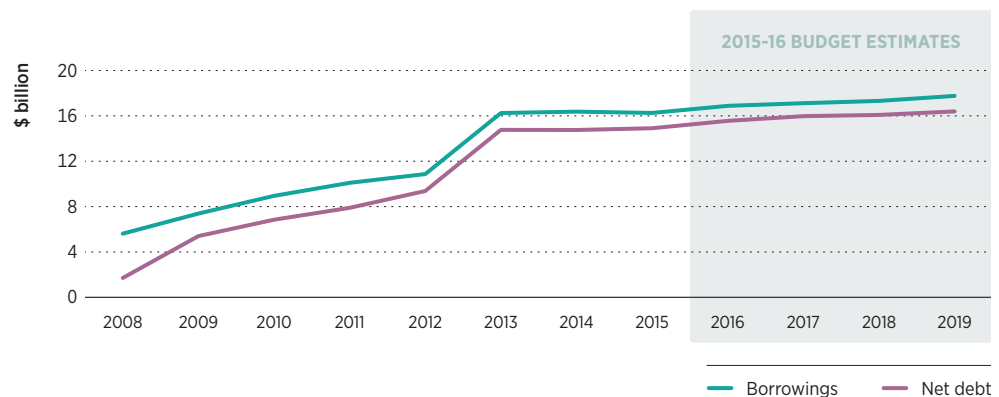
In contrast to the general government sector, borrowings and net debt in the PNFC sector are not expected to decrease in 2015-16, with net debt forecast to rise from \$14.9 billion to \$15.6 billion.<sup>366</sup> Although the proposed Port of Melbourne lease will result in funds flowing into the sector, these funds will flow out to the general government sector in the same period, with no significant impact on PNFC sector debt.<sup>367</sup>

The budget papers estimate that, as a result, the interest expense for the sector will be \$1.1 billion for 2015-16.<sup>368</sup>

Urban and regional Water entities are anticipated to hold around 92 per cent of the net debt for the sector in June 2015.<sup>369</sup> The Auditor-General has noted that a key challenge for these entities will be 'servicing growing debt, and repaying the debt in the future'.<sup>370</sup>

After 2016, the budget papers anticipate that PNFC borrowings will continue to increase, reaching \$17.8 billion by June 2019.<sup>371</sup> Similarly, net debt is expected to rise to \$16.4 billion by June 2019.<sup>372</sup>

**Figure 6.2** Borrowings and net debt, public non-financial corporations sector, 2008 to 2019<sup>(a)</sup>



(a) Balances at 30 June each year.

Source: Department of Treasury and Finance, *Financial Report*, 2008-09 to 2013-14; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.51.

Figure 6.2 shows borrowings and net debt for the sector since 2008. The figure shows that the growth rates for borrowings and net debt over the forward estimates period are estimated to be less than past growth rates. This is because past asset expenditure by the PNFC sector has been greater than the cash available for it. In more recent years, and over the forward estimates period, investment levels are expected to be closer to cash availability.

<sup>366</sup> *ibid.*

<sup>367</sup> *ibid.*, p.52.

<sup>368</sup> *ibid.*, p.49.

<sup>369</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.49.

<sup>370</sup> Victorian Auditor-General's Office, *Water Entities: Results of the 2013-14 Audits* (2015), p.42.

<sup>371</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015 16 Statement of Finances* (2015), p.51.

<sup>372</sup> *ibid.*

The effect of the continued increase in net debt on the sector will be felt in continued interest expenditure. As noted in Section 6.2, the Government has not set a target for net debt in this sector.

**FINDING 48:** The budget papers anticipate that borrowings and net debt for the public non-financial corporations sector will continue to increase over the forward estimates period. Net debt for the PNFC sector is estimated to increase from \$14.9 billion to \$16.4 billion between 2015 and 2019.

The main entities that contribute to PNFC net debt are listed in Appendix A6.1. The Committee notes that \$12.7 billion (around 85 per cent) of the PNFC sector's net debt is held by Melbourne Water Corporation and the three metropolitan urban water authorities.<sup>373</sup> Approximately \$5.1 billion of Melbourne Water Corporation's debt is a result of the Victorian Desalination Plant.<sup>374</sup> Appendix A6.1 shows that these four entities are expected to increase debt levels over the next four years.

The increased debt held by the four water authorities provides the majority of the expected rise in PNFC net debt over the forward estimates period.<sup>375</sup>

Figures provided by the Department of Treasury and Finance show that three PNFC entities (Victorian Rail Track, Coliban Region Water Corporation and Places Victoria) are anticipated to have lower net debt in June 2019 than in June 2015.<sup>376</sup>

**FINDING 49:** Melbourne Water Corporation and the three urban water authorities are expected to make up around 85 per cent of the net debt in the public non-financial corporations sector in June 2015. These entities are all expected to increase debt levels over the forward estimates period.

### 6.3.2 Superannuation liability

Most staff now employed in the Victorian public sector have defined contributions superannuation schemes. With this type of fund, set amounts are paid into a superannuation account for each employee with each pay. When the employees retire, their superannuation benefits are determined by the amount contributed, along with any capital growth.

However, earlier superannuation schemes for the public sector were of the 'defined benefits' type.<sup>377</sup> On retirement, these schemes provided beneficiaries with an indexed pension for the rest of their lives, with the payment being a set proportion of their final salary. In contrast to a defined contributions scheme, there is no guarantee that what the Government will be required to pay

<sup>373</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.49.

<sup>374</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.168.

<sup>375</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.51.

<sup>376</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.49.

<sup>377</sup> For a small number of staff, these schemes are still available.

the retirees will be covered by ‘plan assets’ (that is, the amount that has been put aside plus capital growth). This shortfall is therefore a future liability for the Government.

As noted in Section 6.2, the Government’s financial management strategy includes fully funding this superannuation liability by 2035.<sup>378</sup> This has been the strategy of a number of successive governments.

During his hearing, the Treasurer remarked that:<sup>379</sup>

Steady progress towards fully funding the state’s unfunded superannuation liability has, I think, been a longstanding commitment of governments, and the aim is to get to a point of having it funded by 2035.

The budget papers anticipate that the plan assets will increase from \$21.0 billion in June 2016 to \$22.4 billion in June 2019.<sup>380</sup> As a result, the unfunded superannuation liability is expected to decrease gradually but consistently over the forward estimates period.<sup>381</sup>

In his estimates hearing, the Treasurer noted that:<sup>382</sup>

The general government superannuation funding ratio – the proportion of our liabilities of the former state superannuation fund, which is backed by superannuation plan investments – is projected to increase from 46 per cent to 48.9 per cent over the next four years. The numbers are looking good there.

However, contributions to the asset base are only one factor that will determine whether the funds will be able to cover their obligations.

An actuarial assessment is carried out every three years to update assumptions about the number of beneficiaries. The last assessment was conducted in 2012. Changes to assumptions as a result of these assessments may impact on the estimated value of the unfunded superannuation liability.

In addition, in calculating the superannuation liability, the estimated future payments are discounted to a ‘present value’.<sup>383</sup> The discounting is ‘based on a long-term fixed interest Commonwealth Government bond rate’, which is currently 2.7 per cent per year.<sup>384</sup> The Minister for Finance noted in his hearing that:<sup>385</sup>

... changes in bond rates can lead to very large changes in the superannuation liability.

<sup>378</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

<sup>379</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.28.

<sup>380</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.31.

<sup>381</sup> *ibid.*, p.9.

<sup>382</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.28.

<sup>383</sup> That is, an estimate of how much money would need to be held today to make all of the payments in the future, factoring in interest that would accrue to that money over time.

<sup>384</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.25.

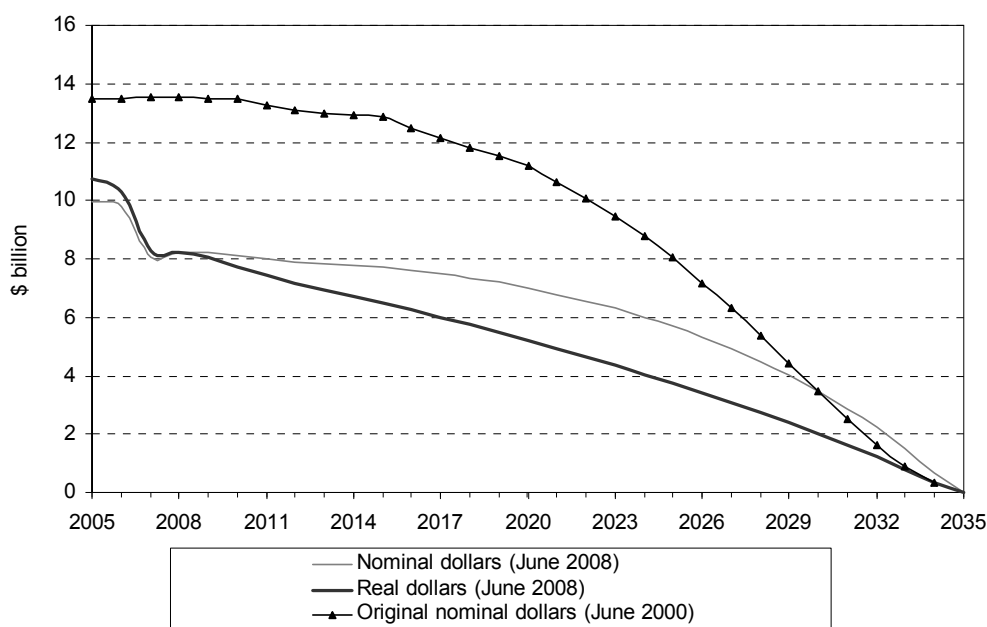
<sup>385</sup> Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.6.

For example, between June 2011 and June 2012, primarily as a result of changes in the bond rate, the unfunded superannuation liability rose from \$22.8 billion to \$32.6 billion. In the next year, further changes to the bond rate led to the liability falling to \$25.1 billion.<sup>386</sup>

As a result of these fluctuations, it is very difficult in any one year to assess whether the Government is on track to achieve its target that the outstanding liability will be zero by 2035.

The Committee notes that past budget papers included a diagram showing a realistic path that the unfunded liability could take to decrease to zero in 2035. This was last included in the 2008-09 budget papers, and is reproduced in Figure 6.3 below.

**Figure 6.3** General government sector unfunded superannuation liability – long-term projections, 2008-09 Budget



Source: Reproduced from Department of Treasury and Finance, *Budget Paper No.2: 2008-09 Strategy and Outlook* (2008), p.55.

Figure 6.3 shows the long-term goal and all years between. With this information, readers were able to understand how annual progress towards the 2035 goal was planned, and therefore whether the liability was decreasing at the appropriate rate.

The Committee considers that including a similar figure in future budget papers would indicate the interim goals that support the Government’s long-term strategy. This would demonstrate whether the Government is setting aside funds at an appropriate rate to achieve its goal.

<sup>386</sup> Department of Treasury and Finance, *2012-13 Financial Report* (2013), p.27.

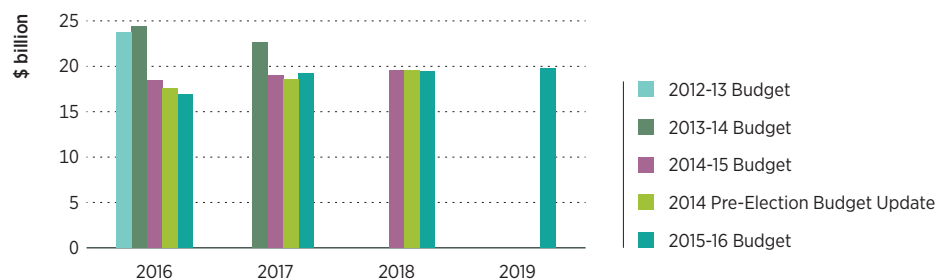
**FINDING 50:** The Government plans to decrease its unfunded superannuation liability to zero by 2035. The liability is expected to decrease gradually but consistently over the forward estimates period as plan assets increase. However, the budget papers do not include interim goals towards the Government's 2035 target. Without such goals, it is not possible to determine whether the unfunded liability is on track to be zero by 2035.

**RECOMMENDATION 35:** The budget papers reinstate the practice of including a diagram showing the expected level of unfunded superannuation liability in each year between the budget year and 2035, similar to the disclosure in earlier budget papers. Commentary should also be provided on the achievement of interim goals.

## 6.4 Comparison to previous estimates

Figure 6.4 shows the estimates for net debt given in the last four budgets (and the 2014 Pre-Election Budget Update, issued just before the change of government in 2014).

**Figure 6.4** Comparison of general government sector net debt estimates in the 2015-16 Budget to previous estimates



Note: Balances at 30 June each year.

Source: Department of Treasury and Finance, *Budget Paper No.5: Statement of Finances*, 2012-13 to 2015-16; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.29.

The most significant adjustment that has been made to the estimates of net debt was a result of the proposed lease of the Port of Melbourne's operations. This was decided at the time of the 2014-15 Budget and caused net debt predictions to be reduced across the forward estimates.

### 6.4.1 Comparison to the Pre-Election Budget Update

Table 6.2 shows that anticipated net debt for June 2018 is relatively unchanged from the estimate in the 2014 Pre-Election Budget Update. However, the estimates for intervening years are significantly different.

Although the debt estimate for 2018 is relatively unchanged, the factors contributing to this result have changed considerably. Table 6.3 shows the cumulative impact of these changes to the estimates between 2014 and 2018.

**Table 6.2** Estimates of general government sector net debt between 2015 and 2019<sup>(a)</sup>, 2014 Pre-Election Budget Update and 2015-16 Budget

	2015 (\$ million)	2016 (\$ million)	2017 (\$ million)	2018 (\$ million)	2019 (\$ million)
2014 Pre-Election Budget Update	21,768.8	17,564.3	18,609.9	19,597.5	n/a
2015-16 Budget	21,240.0	16,897.8	19,259.0	19,450.2	19,834.7
<b>Change in net debt estimates</b>	<b>-528.8</b>	<b>-666.5</b>	<b>649.1</b>	<b>-147.3</b>	<b>n/a</b>

(a) Balances at 30 June in each year.

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 State of Finances* (2015), p.9; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.29.

**Table 6.3** Expected change in general government sector net debt between 2014 and 2018, 2014 Pre-Election Budget Update estimates compared with 2015-16 Budget

	2014 PEBU (\$ million)	2015-16 Budget (\$ million)	Difference (\$ million)
Cash available between 2014-15 and 2017-18 from:			
• operating surpluses	9,031.6	4,864.0	-4,167.6
• depreciation and similar; and asset sales	12,613.5	13,395.8	782.3
• net cash inflows from investments in other sectors <sup>(a)</sup>	5,002.2	7,621.6	2,619.4
<b>Total cash resources</b>	<b>26,647.3</b>	<b>25,881.4</b>	<b>-765.9</b>
Cash needed between 2014-15 and 2017-18 for:			
• infrastructure investment <sup>(b)</sup>	21,899.0	21,269.8	-629.2
• PPPs and other finance leases	3,015.6	2,157.0	-858.6
• other movements	155.5	729.0	573.5
<b>Total cash needed</b>	<b>25,070.1</b>	<b>24,155.8</b>	<b>-914.3</b>
<b>Cash available for paying off net debt between 2014 and 2018<sup>(c)</sup></b>	<b>1,577.1</b>	<b>1,724.4</b>	<b>147.3</b>

(a) Only years with a net cash inflow have been included in this figure.

(b) Includes both direct investment (including contingency) and net cash outflows for investment through other sectors.

(c) Totals may not add due to rounding.

Source: Committee calculations based on Department of Treasury and Finance, *2013-14 Financial Report* (2014), pp.31-3; Department of Treasury and Finance, *2014 Pre-Election Budget Update* (2014), pp.11, 19, 29, 30; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p. 59; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 10, 225, 228.

Part of the Government's strategy has been to increase expenditure on services (see Section 2.3 and 7.4).<sup>387</sup> As a result of this, forecasts for the operating surpluses between 2014-15 and 2017-18 have been decreased by \$4.2 billion compared to previous estimates, leading to lower cash resources available from this source for asset investment.<sup>388</sup>

<sup>387</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.45.

<sup>388</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.7; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.27.

The Government has mitigated the impact of this by increasing the amount it is expecting in cash inflows from investments in other sectors.

The Government has increased the amount it expects to receive from the proposed Port of Melbourne lease primarily by proposing to extend the term of the lease<sup>389</sup> (see Section 8.6). This has increased the anticipated net inflow from other sectors for 2015-16 from \$5.0 billion<sup>390</sup> to \$6.5 billion.<sup>391</sup> The Government also anticipates a net cash inflow of \$1.1 billion from the public financial corporations sector during 2017-18 which had not been anticipated at the time of the Pre-Election Budget Update.<sup>392</sup> This is not fully explained in the budget papers (see Section 8.3.1)

Table 6.3 shows that changes to the estimates of depreciation and similar costs, together with planned asset sales, have added \$782.3 million more than previously estimated to the amount available for investment. This is a result of multiple relatively small revisions to several line items since the 2014 Pre-Election Budget Update.<sup>393</sup>

The total impact of these three factors is that \$765.9 million less cash is available from these sources for asset investment across the four years.

The impact of the reduced estimates of cash resources has been offset by the Government lowering the amount it expects to spend in direct asset investment over the forward estimates period, and adjusting the amount it expects to invest through other sectors. Over the forward estimates period, this investment is forecast to be \$629.2 million less than previously forecast.

In addition, the Government has scaled back its PPP investment program, replacing the *Cranbourne-Pakenham Rail Corridor* project<sup>394</sup> with parts of several direct investment projects (see Section 8.7). The Government has added a *New Schools* PPP project, but the overall liability for new PPP projects has decreased.<sup>395</sup> PPP projects are described in further detail in Section 8.3.1. As a result of these changes, \$858.6 million less in PPP liabilities is expected to be added to borrowings between 2014 and 2018.

<sup>389</sup> Specified as 50 years in the Delivering Victorian Infrastructure (Port of Melbourne Lease Transaction) Bill 2015 (Vic), s.11(2)(a). The previously planned lease term was specified as 'medium-term', which the Committee understands to have been 40 years.

<sup>390</sup> Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.30.

<sup>391</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.10.

<sup>392</sup> The item 'net cash flows from investments in financial assets for policy purposes' for 2017-18 having been adjusted from an outflow of \$163.5 million (Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.30) to an inflow of \$1,110.8 million (Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.10).

<sup>393</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.228; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.30.

<sup>394</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.13; Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.23.

<sup>395</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

In contrast, the estimated cost of 'other movements' has increased by \$573.5 million. The Department of Treasury and Finance advised the Committee that this includes \$420 million in negotiated payments following the cancellation of the *East West Link* project.<sup>396</sup>

The net result of these changes is that the estimated level of net debt for June 2018 is relatively unchanged. The overall decrease in net debt between 2014 and 2018 is now estimated at \$1.7 billion, compared to the \$1.6 billion estimated in the 2014 Pre-Election Budget Update (see Table 6.3).

After June 2018, the Government anticipates that net debt will rise during the last year of the forward estimates period. As described in Section 6.3.1, this is a result of the planned level of asset investment being greater than the expected cash resources available for 2018-19.<sup>397</sup>

**FINDING 51:** In comparison to the 2014 Pre-Election Budget Update, the 2015-16 budget papers estimate that less cash will be available over the forward estimates period from operating surpluses to fund asset investment. However, the 2015-16 Budget estimates that this will be partly offset by cash inflows from investment through other sectors. The Budget also estimates that less borrowing will be required for infrastructure investment and public private partnerships. As a result, the 2015-16 Budget estimates that net debt will decrease by \$147.3 million more between 2014 and 2018 than was estimated in the 2014 Pre-Election Budget Update.

The Committee notes that the budget papers include a 'reconciliation of estimates' table for the operating surplus.<sup>398</sup> This shows what has driven changes between current and previous estimates for the operating surplus by showing the impact of key factors on revenue and expenses. The Committee considers this a particularly useful tool for understanding changes to the operating surplus.

Like the operating surplus, net debt is a key budget component which is specified in the Government's fiscal strategy (see Section 6.2 of this report). However, neither previous budget papers nor this year's papers have included an equivalent reconciliation of estimates table for changes in net debt. The budget papers do contain an 'application of cash resources' table that highlights factors that contribute to net debt. However, this is not accompanied by an explanation for changes to the estimates since previous budgets.

The Committee considers that the addition of a table comparing application of cash resources tables between budgets would highlight factors that had driven changes to net debt estimates. Discussion of these factors would provide readers with an important understanding of changes between budgets.

<sup>396</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.3.

<sup>397</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>398</sup> *ibid.*, p.55.



**FINDING 52:** The ‘reconciliation of estimates’ table in the budget papers provides useful information on what has driven changes between current and previous estimates of operating surpluses. There is no equivalent reconciliation of estimates table for net debt estimates.

**RECOMMENDATION 36:** Future budget papers include an additional table reconciling the information given in the ‘application of cash resources’ table between current and previous estimates, similar to ‘reconciliation of estimates’ table produced for operating surpluses. This table would include changes to estimates for:

- (a) net cash flows from operating activities
- (b) direct investment (purchases of non-financial assets)
- (c) investment through other sectors (net cash flows from investments in financial assets for policy purposes)
- (d) proceeds from asset sales
- (e) finance lease liabilities
- (f) changes in net debt.

**RECOMMENDATION 37:** Accompanying the table reconciling estimates of net debt, the Department of Treasury and Finance provide discussion of the factors that have driven the changes between budgets.



# 7 Output expenses

## 7.1 Introduction

The majority of the Government's revenue each year goes to output expenses. Output expenses mostly relate to the delivery of services by the Government, such as health care, education and policing.<sup>399</sup> The relationship between output expenses and other items of the budget is further discussed in Section 2.2.1 of this report.

Output expenses are expected to grow over the forward estimates period, as indicated in Table 7.1 below.

**Table 7.1** General government sector output expenses, 2014-15 to 2018-19

	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
Total output expenses (\$ million)	52,659.4	54,309.8	55,497.4	57,671.0	59,350.7
Annual growth					
• (\$ million)	2,271.0	1,650.4	1,187.6	2,173.6	1,679.7
• (per cent)	4.5	3.1	2.2	3.9	2.9
Average annual growth rate (2015-16 to 2018-19) (per cent) <sup>(a)</sup>			3.0		

(a) Compound annual growth rate. Calculated by the Committee.

Sources: Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.49; Committee calculations based on Department of Treasury and Finance, Consolidated Comprehensive Operating Statement – General Government Sector (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015.

This chapter examines the following questions:

- What is the Government's strategy for output expenses? (Section 7.2)
- What factors are causing the growth over the forward estimates period? How reliable are the estimates? What services will be provided? (Section 7.3)
- How and why have these estimates changed since previous budgets? (Section 7.4)
- What do we know about departments' base funding? (Section 7.5)
- What new output initiatives were released in the 2015-16 budget papers? (Section 7.6)
- How have these initiatives been funded? (Section 7.7)

<sup>399</sup> Depreciation is also included within output expenses, reflecting the decline in value of infrastructure and other assets associated with the service delivery. The cash equivalent to depreciation partly funds asset investment (see Section 2.2.1).

- What programs have been discontinued or have lapsed since the previous budget? (Section 7.8)
- What are the major risks to the estimates for output expenses? (Section 7.9)

This chapter will focus on the general government sector, which delivers most of the services provided by the public sector. The general government sector generally delivers services free of charge or at charges significantly below cost.<sup>400</sup>

## 7.2 The Government's strategy

As noted above, output expenses fund service delivery. Service delivery features prominently in the Government's long-term financial management objectives (see Section 2.3.2). These objectives include improving public services and investing in services that 'maximise the economic, social and environmental benefits'.<sup>401</sup>

As part of the 2015-16 Budget, the Government intends to increase output expenses at a faster rate than had been planned by the previous government.<sup>402</sup>

The Government's financial goals also include maintaining a triple-A credit rating and growing infrastructure while maintaining debt 'at a sustainable level'.<sup>403</sup> To achieve these goals, it will be necessary for the Government to limit the increase in output expenses so that operating surpluses are achieved. Operating surpluses are important components of funding infrastructure without increasing debt (see Section 2.2.1) and maintaining a triple-A credit rating.

The impact of increasing the growth rate of operating expenses compared to previous estimates is to reduce the operating surpluses relative to previous estimates. However, as discussed in Section 6.4.1 of this report, this is anticipated to be largely offset by greater cash inflows from the proposed lease of the Port of Melbourne's operations and from the public financial corporations sector (see Section 8.6). A reduction to the anticipated scale of the asset investment program between 2014-15 and 2017-18 has also reduced the amount of cash resources required for asset investment. As a result, as noted in the budget papers, the increased growth in operating expenses compared to previous estimates 'does not add to the State's debt burden'.<sup>404</sup>

<sup>400</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.210.

<sup>401</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

<sup>402</sup> *ibid.*, p.45; Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, pp.2, 13.

<sup>403</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

<sup>404</sup> *ibid.*, p.45.

**FINDING 53:** The Government has stated an intention to improve public services and to increase output expenses at a faster rate than the previous government planned. However, this growth will need to be limited to achieve the Government's other goals of maintaining the State's triple-A credit rating and growing infrastructure while maintaining debt levels. In the 2015-16 Budget, the higher estimated growth rate for operating expenses is anticipated to be largely offset by cash inflows from the proposed lease of the Port of Melbourne and from the public financial corporations sector.

## 7.3 Estimates for output expenses

### 7.3.1 Underestimation in the budget estimates

As shown in Table 7.1, the budget estimates suggest that output expenses will grow at an average rate of 3.0 per cent per year across the forward estimates period. However, it needs to be understood that previous budget papers have significantly underestimated the growth of output expenses across the relevant forward estimates periods. Table 7.2 compares the forward estimates in previous budget papers to the actual growth rates in those periods.<sup>405</sup>

**Table 7.2** Estimated and actual growth rates for output expenses, rolling forward estimates periods

	Estimated growth rate across the relevant forward estimates period <sup>(a)</sup>	Actual growth rate <sup>(a)</sup>
2005-06 Budget	2.9	7.8
2006-07 Budget	3.1	9.4
2007-08 Budget	3.1	8.4
2008-09 Budget	4.1	6.6
2009-10 Budget	1.3	3.6
2010-11 Budget	2.9	3.5

(a) All growth rates are compound annual growth rates between the relevant budget year and the end of the relevant forward estimates period.

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2005-06 to 2010-11; Department of Treasury and Finance, *Financial Report*, 2006-07 to 2013-14.

The average annual growth rate across the entire period covered by those budgets (2005-06 to 2013-14) was 6.2 per cent. Most of the estimates in these budgets predicted growth rates around 3.0 per cent, as does the 2015-16 Budget. In every case, the actual growth rate was higher than estimated.

<sup>405</sup> The 2010-11 Budget is the last one included, as it is the last year for which actual data are available for all years of the budget's forward estimates period.

Similarly, Appendix A7.1 shows that expenses in the budget year have been underestimated in every budget that the Committee examined (2005-06 to 2013-14<sup>406</sup>). This underestimation averaged \$1.1 billion per year during this period.<sup>407</sup>

As discussed in Section 4.3.2, past budgets have similarly underestimated revenue. As a result, the higher-than-expected expenses have not necessarily led to the operating surpluses being lower than expected. As both revenue and expenses have been underestimated by different amounts in different years, the impact on the surplus has varied.

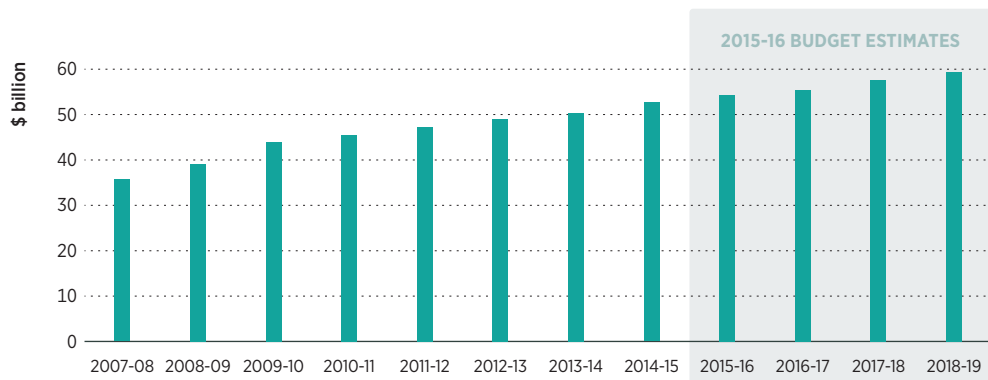
However, the current budget estimates need to be understood in this context. The pattern of repeated underestimation suggests that the latest budget estimates may be conservative and that the actual expenses across the forward estimates period may be higher than predicted.

**FINDING 54:** The budget papers estimate that output expenses will grow at an average of 3.0 per cent per year over the forward estimates period. This is a much lower rate than the actual growth in recent years, which has averaged 6.2 per cent. However, previous budgets have consistently underestimated the growth in output expenses by significant amounts, suggesting that the forward estimates in this budget may be understated.

### 7.3.2 The forward estimates

The forward estimates for output expenses are compared to previous actual amounts in Figure 7.1.

**Figure 7.1** General government sector output expenses, 2007-08 to 2018-19



Source: Department of Treasury and Finance, Consolidated Comprehensive Operating Statement – General Government Sector (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015.

<sup>406</sup> 2013-14 is the last year for which actual amounts have been published to date.

<sup>407</sup> Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2005-06 to 2013-14; Department of Treasury and Finance, *Financial Report*, 2006-07 to 2013-14.

The estimates show output expenses growing by 3.1 per cent between 2014-15 and the budget year and then by an average of 3.0 per cent between 2015-16 and 2018-19.<sup>408</sup>

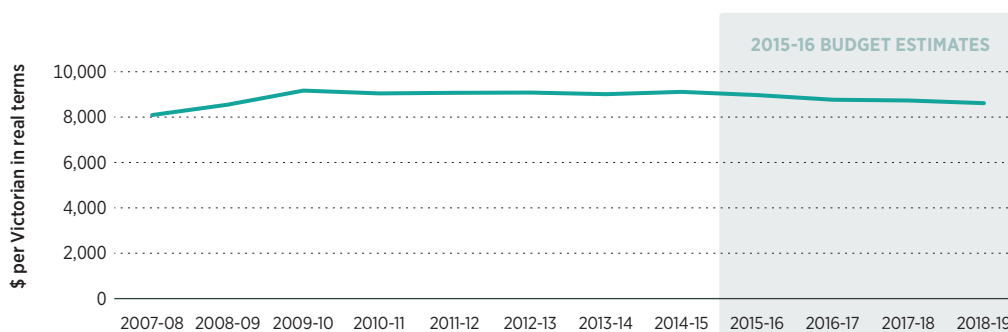
As noted in Section 7.2 of this chapter, the Government has increased the estimated growth rate for output expenses relative to previous budget estimates (see further discussion in Section 7.4). The budget papers indicate that population growth and inflation were considerations in this decision.<sup>409</sup>

Figure 7.2 adjusts the forward estimates and past actual expenses to account for inflation and population growth. The figure shows that, after a relatively stable period between 2009-10 and 2014-15, the budget estimates for expenses per Victorian in real terms (that is, adjusted for inflation) will decrease over the forward estimates period, by an average of 1.3 per cent per year. Although the 2015-16 budget estimates increase the growth rate for output expenses, they still do not keep pace with expected population growth combined with inflation.

If this situation were to eventuate, the Government would need to achieve significant efficiencies in order to deliver the same levels of service to every Victorian.

However, the estimated decline may be a result of the underestimation of the forward estimates (see Section 7.3.1 of this report).

**Figure 7.2** General government sector output expenses in real terms per Victorian,<sup>(a)</sup> 2007-08 to 2018-19



(a) Expressed in 2015-16 prices.

Source: Committee calculations based on Department of Treasury and Finance, Consolidated Comprehensive Operating Statement – General Government Sector (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 21 May 2015; Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 21 May 2015.

**FINDING 55:** The budget estimates suggest that output expenses will decline over the forward estimates period when adjusted for population growth and inflation. However, this may be a result of the forward estimates being underestimated.

<sup>408</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.49.

<sup>409</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.45.

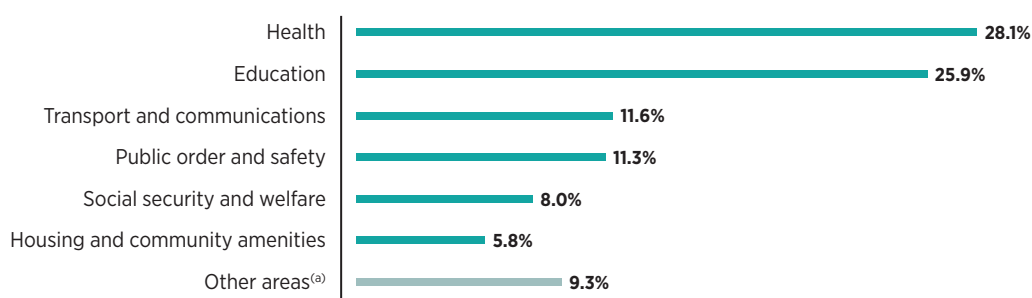
### 7.3.3 What the money will be spent on

The estimates can be broken down in a number of different ways to understand what is driving the growth over the forward estimates period. This includes the purpose of the expenses and the types of expense expected.

#### The purposes of the expenses

The 'government purpose classification' is a system developed by the Australian Bureau of Statistics for categorising government expenditure.<sup>410</sup> Figure 7.3 breaks down the estimated expenses for 2015-16 according to the largest categories.

**Figure 7.3** Expenses by government purpose classification, 2015-16



(a) Includes the categories 'general public services', 'recreation and culture', 'fuel and energy', 'agriculture, forestry, fishing and hunting', 'mining, manufacturing and construction', 'other economic affairs' and 'other purposes'.

Source: Department of Treasury and Finance, *Consolidated Government Purpose Classification Data (2015)*. Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 20 July 2015.

Health and education are the main areas of expenditure, together accounting for 54.0 per cent of output expenses in 2015-16. The next largest categories are services connected with transport and communications (such as road maintenance and public transport) and with public order and safety (such as emergency services and courts).

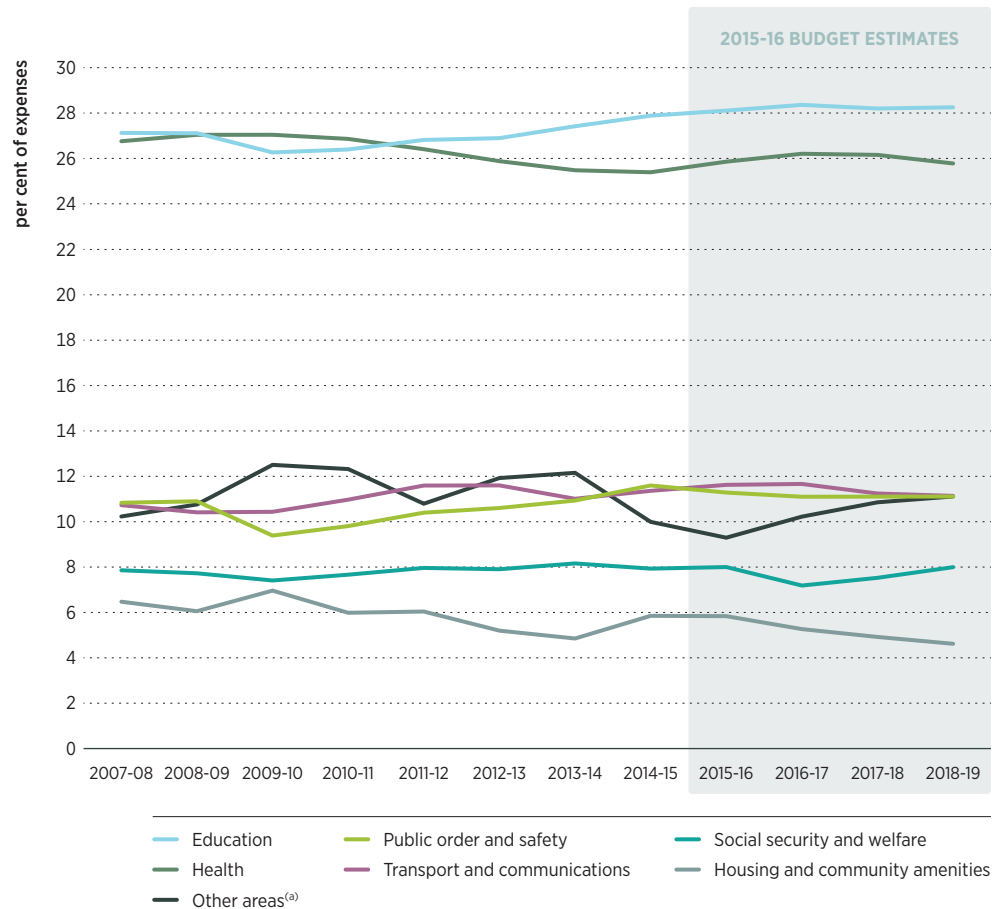
Figure 7.4 below compares the 2015-16 break down to earlier years and the forward estimates.

No major shifts are expected for the largest categories of expenses. Health spending is expected to become a slightly larger share of output expenses across the forward estimates period, rising from 28.1 to 28.3 per cent between 2015-16 and 2018-19. Education expenses have been declining as a proportion of the total in recent years, reaching an estimated 25.4 per cent in 2014-15. The budget estimates see it stabilise around 26.0 per cent, though it is expected to remain a smaller portion than it was prior to 2012-13.<sup>411</sup>

<sup>410</sup> For an explanation of the categories, see Department of Treasury and Finance, *2013-14 Financial Report (2014)*, pp.216-7.

<sup>411</sup> Committee calculations based on Department of Treasury and Finance, *Consolidated Government Purpose Classification Data (2015)*. Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 20 July 2015.



**Figure 7.4** Proportions of expenses by government purpose classification, 2007-08 to 2018-19

(a) Includes the categories 'general public services', 'recreation and culture', 'fuel and energy', 'agriculture, forestry, fishing and hunting', 'mining, manufacturing and construction', 'other economic affairs' and 'other purposes'.

Source: Department of Treasury and Finance, *Consolidated Government Purpose Classification Data* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 20 July 2015.

Expenses associated with social security and welfare are estimated to decline between 2015-16 and 2016-17 both as a proportion of total expenses and in dollar terms. They are then expected to increase in the later years of the forward estimates period.<sup>412</sup> In relation to this, the budget papers explain:<sup>413</sup>

From July 2016, the Commonwealth will be responsible for home support services for people aged over 65 years... The State's contribution to the National Disability Insurance Scheme commences from 2016-17 and increases thereafter as more clients transition into the scheme.

<sup>412</sup> Committee calculations based on Department of Treasury and Finance *Consolidated Government Purpose Classification Data* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 20 July 2015; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.34.

<sup>413</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.34.

Expenses in the ‘housing and community amenities’ category are expected to decline across the forward estimates period, both in dollar terms and proportionately.<sup>414</sup> The budget papers indicate:<sup>415</sup>

The downward movement from 2015-16 relates to sun setting initiatives and movements in funding across years for various initiatives.

The budget papers do not provide details about which areas of service delivery within the ‘housing and community amenities’ category will be affected.

**FINDING 56:** The majority of output expenses relate to health and education, followed by the categories ‘transport and communications’ and ‘public order and safety’. The forward estimates suggest that future spending will be relatively similar. However, the budget estimates do indicate a decrease in the proportion of expenses for housing and community amenities.

### The types of expenses

Expenses are also broken down according to the type of expense. The three largest categories are:

- employee expenses, which cover the salaries paid to employees in the general government sector
- grant expenses, which primarily consist of money given to other sectors of government and bodies outside the State public sector
- ‘other operating expenses’, which largely consist of purchases of supplies, consumables and services from outside the general government sector.

Employee expenses are the largest category of output expenses. Employee expenses are expected to increase by \$1,425.1 million between 2014-15 and the budget year, then by an average of \$814.2 million per year over the forward estimates period.<sup>416</sup> The budget papers explain that employee expenses, including superannuation, are:<sup>417</sup>

... projected to grow by 7.1 per cent to \$23 billion in 2015-16 and by 3.4 per cent a year on average over the forward estimates. The growth in 2015-16 is driven by annual growth in wages, growth in staffing numbers associated with growing patient demand and increased investment in the education sector ...

The estimates suggest that grant expenses will be the second largest driver of the growth in expenses. This includes Commonwealth Government grants to non-government schools and local governments which are passed through

<sup>414</sup> Committee calculations based on Department of Treasury and Finance, *Consolidated Government Purpose Classification Data* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 20 July 2015; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.34.

<sup>415</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.34.

<sup>416</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 225.

<sup>417</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.53; cf. Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.11.

the Victorian Government. The estimates for grants increase by \$467.0 million (5.7 per cent) between 2014-15 and 2015-16 and then by an average of \$387.5 million (4.3 per cent) per year over the next three years.<sup>418</sup>

The budget papers explain that, ‘This increase primarily reflects growth in capital asset payments to VicTrack’.<sup>419</sup> The Committee understands this to be a reference to the increased grants provided by the general government sector to VicTrack to cover its increased capital asset charges<sup>420</sup> (see Section 2.4.2 of this report on the capital asset charge). However, the Committee notes that most of the growth is in grants to the private sector and not-for-profit sector (such as non-government schools).<sup>421</sup>

In contrast to employee expenses and grant expenses, ‘other operating expenses’ are expected to increase at a much lower rate. The budget estimates indicate that this item will decrease by 2.2 per cent between 2014-15 and 2015-16 and then increase at an average of 1.6 per cent per year over the forward estimates period.<sup>422</sup> This is largely driven by an estimated decrease in one component of this category: the purchase of services by the general government sector.<sup>423</sup> The Department of Treasury and Finance explained that:<sup>424</sup>

The 2015-16 figure for purchase of services by the general government sector includes the final year of State Government expenditure on Home and Community Care (HACC), prior to transferring the responsibility and funding for people aged over 65 years for this service to the Commonwealth, as agreed under the National Disability Insurance Scheme (NDIS). Purchase of services estimates from 2016-17 onwards are lower primarily due to the transfer of this age cohort.

The HACC transfer of responsibility was agreed in May 2013 as part of the NDIS. Discussions on a transition date for HACC are ongoing but are expected to be agreed and in place prior to the start of the 2016-17 financial year.

**FINDING 57:** The estimated growth in output expenses is largely driven by expected increases in employee expenses and grants to the private and not-for-profit sectors. Purchases of services are expected to decrease as a result of the transfer of some responsibilities to the Commonwealth Government as part of the National Disability Insurance Scheme.

418 Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.7, 225; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.53.

419 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.53.

420 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.184; the budget papers note that the increased charge is a result of an increased capital asset base (ibid.).

421 ibid., p.33.

422 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.53.

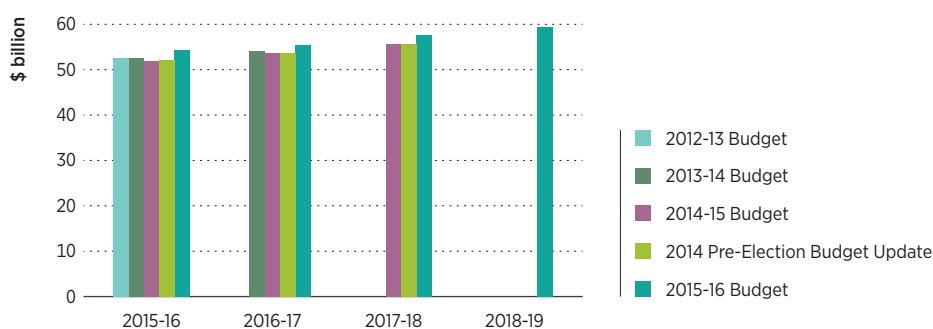
423 Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.33.

424 Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, pp.5-6.

## 7.4 Comparison to previous estimates

Each budget and budget update revises the forward estimates for expenses in the light of new decisions by the Government and changing external circumstances (such as population growth and Commonwealth Government funding). Figure 7.5 compares the estimates for 2015-16 to 2017-18 made in the current budget with the estimates from previous years.

**Figure 7.5** Comparison of output expenses estimates in the 2015-16 Budget to previous estimates



Sources: Department of Treasury and Finance, *Budget Paper No.5: Statement of Finances*, 2012-13 to 2015-16; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014).

Figure 7.5 shows that the estimates in the 2015-16 Budget are approximately \$2 billion higher in each year than the estimates made in previous budgets. This is in line with the Government's strategy to grow output expenses at a faster rate than previously estimated (see Section 2.3 and 7.2 of this report).

### 7.4.1 Factors increasing the estimates

Table 7.3 below indicates what has driven the increase in the estimates since the 2014 Pre-Election Budget Update (which was issued shortly before the change of government in 2014).

The largest driver of growth has been the new output initiatives released in the 2014-15 Budget Update and 2015-16 Budget. These new initiatives are a mixture of election commitments, other new programs and the continuation of lapsing programs. These are discussed further in Section 7.6 of this report. Changes in specific-purpose grants have also added significant amounts, especially in 2015-16.

These additional expenses have been partly offset by:

- expenditure reduction initiatives, which reduce expenditure through efficiencies or by reducing the services provided
- the reprioritisation of existing resources, which includes funding previously allocated to departments for other purposes
- the release of 'contingencies', that is, allowances put aside in previous budget estimates for future allocation to departments.

These are discussed further in Section 7.7 of this report.

**Table 7.3** Variations in estimates for output expenses between the 2014 Pre-Election Budget Update and the 2015-16 Budget

	2015-16	2016-17	2017-18
	(\$ million)	(\$ million)	(\$ million)
Output expenses estimated in the 2014 Pre-Election Budget Update	52,188	53,667	55,559
New output initiatives	+2,363	+2,292	+2,426
Changes as a result of specific-purpose grants	+742	+254	+287
Expenditure reduction initiatives	-72	-84	-91
Reprioritisation of existing resources	-490	-371	-332
Release of contingencies <sup>(a)</sup>	-715	-965	-1,330
Other administrative variations <sup>(b)</sup>	+293	+704	+1,150
Net impact	+2,122	+1,831	+2,111
Output expenses estimated in the 2015-16 Budget	54,310	55,497	57,671

(a) May include some reprioritisation of existing resources decided in the 2014-15 Budget Update. This figure includes the line items 'adjustments' and 'contingency offset for new policy' from the budget papers and is the net release of contingency, factoring in increases to contingencies.

(b) Reflects the impact on expenses, whereas the line item with the same name in the 2015-16 budget papers reflects the net impact on the operating surplus.

Source: Committee calculations based on Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), pp.27, 45; Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), pp.20, 121-5; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), pp.29, 49, 55, 58; Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.43.

The changes to specific-purpose grants have also resulted in additional revenue from the Commonwealth Government. While the expenses related to specific-purpose grants are estimated to increase by \$1.3 billion across the three years, revenue for specific-purpose grants is estimated to increase by \$1.7 billion (see Section 4.4).<sup>425</sup> The budget papers note 'the rescheduling to 2017-18 of expected revenues under the asset recycling initiative' as a major factor.<sup>426</sup>

There have also been a number of changes described as 'other administrative variations' increasing output expenses. The budget papers indicate that these variations largely reflect:<sup>427</sup>

- prudent provisioning for future budgets to meet the Government's service delivery priorities;
- higher than expected payments for the tail of the *First Home Owners Grant* scheme; and

<sup>425</sup> The Committee notes that the timing of the increased revenue does not correspond with the timing of the increased expenses (compare Table 4.5 to Table 7.3). The estimates suggest that the additional expenses will exceed the additional revenue in 2015-16. However, the additional revenue will exceed the additional expenses in 2017-18.

<sup>426</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.57.

<sup>427</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.57; cf. Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), p.22.

- additional depreciation averaging \$41 million due to a change in accounting policy for measuring the fair value of school buildings.

The Committee understands a large portion of this to be additions to the contingencies to fund future initiatives (see Section 7.7.3 of this chapter).

**FINDING 58:** The estimates for output expenses between 2015-16 and 2017-18 have been revised upwards by approximately \$2 billion per year since the 2014 Pre-Election Budget Update. This has been driven by new output initiatives, changes to specific-purpose grants and administrative variations.

Table 7.3 is largely based on the ‘reconciliation of estimates’ table, which is produced with each budget and budget update.<sup>428</sup> The Committee notes that the format of this table was substantially changed with the 2015-16 Budget. A number of smaller line items are no longer separately disclosed. In addition, whereas the impacts of each item on revenue estimates and expenses estimates were separately detailed previously, only the net impact on the operating surplus is indicated this year for some items.

The Committee considers that the new format is generally an improvement, as it provides the information in a clearer, more succinct manner. However, the Committee considers that future budget papers should disaggregate the impact of specific-purpose grants variations to separately indicate the impact on revenue and expenses. The revenue and expenses impacts can be quite different and the Committee considers that clearly disclosing and discussing these differences would assist readers of the budget papers to understand the context of the Budget.

**FINDING 59:** The format of the ‘reconciliation of estimates’ table has been modified in the 2015-16 budget papers. Generally, this has made the information easier to understand. However, this table no longer separately discloses the impact of variations in specific-purpose grants on revenue and expenses.

**RECOMMENDATION 38:** ‘Reconciliation of estimates’ tables in future budget papers separately disclose the impact on revenue and expenses of variations in specific-purpose grants. Differences between the impact on revenue and the impact on expenses should be discussed when the differences exceed \$100 million.

## 7.4.2 Machinery-of-government changes

As detailed in Section 1.4 of this report, considerable machinery-of-government changes occurred following the change of government in 2014. The Committee sought information through its questionnaire about what impact these changes had on departments’ output expenses.

In relation to costs, the six departments affected by machinery-of-government changes provided the following responses:

<sup>428</sup> e.g. Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.55.

- the Department of Treasury and Finance stated that no costs were incurred<sup>429</sup>
- the Department of Justice and Regulation responded that, ‘There were no costs to the department (excluding staff costs)’<sup>430</sup>
- the Department of Health and Human Services indicated that the total cost was anticipated to be approximately \$150,000<sup>431</sup>
- the Department of Economic Development, Jobs, Transport and Resources indicated that costs would be between \$1.5 and \$2.0 million in 2014-15, with further costs expected in 2015-16 and 2016-17<sup>432</sup>
- the Department of Environment, Land, Water and Planning explained that it ‘does not track costs associated with machinery-of-government changes’ but noted that changes to ‘signage and other related material has cost approximately \$70,000’<sup>433</sup>
- the Department of Premier and Cabinet did not provide details, simply indicating that, ‘Costs involved in implementing changes are absorbed within existing budgets’.<sup>434</sup>

However, in a later response to an inquiry conducted by the Legislative Council’s Legal and Social Issues Committee, the Government provided updated figures about direct costs incurred up to 31 May 2015 (see Table 7.4 below). These do not include staff time.

The Government’s submission to that inquiry notes the difference between these figures and the figures earlier provided to the Public Accounts and Estimates Committee, with a number of explanations for the differences provided.<sup>435</sup>

All but one of the departments indicated to the Public Accounts and Estimates Committee that there would not be reductions in staff numbers as a result of the machinery-of-government changes. The other department (the Department of Economic Development, Jobs, Transport and Resources) indicated that it was undertaking ‘an extensive organisational design process’. However, the

429 Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.2.

430 Department of Justice and Regulation, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 11 June 2015, p.2.

431 Department of Health and Human Services, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 26 June 2015, p.3.

432 Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.2.

433 Department of Environment, Land, Water and Planning, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 22 June 2015, p.2.

434 Department of Premier and Cabinet, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.3.

435 Victorian Government, *Whole of Victorian Government Submission on Costs Associated with the Machinery of Government Changes*, submission to the Legal And Social Issues Committee’s Inquiry into Machinery of Government Changes (2015).

Department noted, ‘The focus of the redesign is not on cost reduction but on ensuring the Department has an appropriate capability mix and has its resources deployed in the right areas’.<sup>436</sup>

**Table 7.4** Direct costs associated with machinery-of-government changes, 30 November 2014 to 31 May 2015

Department	Direct costs (\$)
Economic Development, Jobs, Transport and Resources	1,302,507
Education and Training	10,200 <sup>(a)</sup>
Environment, Land, Water and Planning	770,568
Health and Human Services	618,000
Justice and Regulation	0
Premier and Cabinet	341,430
Treasury and Finance	23,000
<b>Total</b>	<b>3,065,705</b>

(a) Reflects costs incurred as a result of the change to the department's name.

Source: Victorian Government, *Whole of Victorian Government Submission on Costs Associated with the Machinery of Government Changes*, submission to the Legal and Social Issues Committee's Inquiry into Machinery of Government Changes (2015), pp.2-5.

As some of the responses to this Committee and the Legal and Social Issues Committee indicate, the costs of machinery-of-government can be significant. The Public Accounts and Estimates Committee believes that there would be public interest in understanding what these costs are and therefore considers that departments should monitor and report on the costs of implementing machinery-of-government changes, as well as the benefits achieved through the changes. This could be achieved by updating the Department of Treasury and Finance's Model Report, which provides guidance to departments on how annual reports should be prepared.

**FINDING 60:** Machinery-of-government changes affected six departments during 2014-15. Departments indicated that the expected costs of these changes in 2014-15 ranged from zero to \$2.0 million.

**RECOMMENDATION 39:** The Department of Treasury and Finance update the Model Report to require all departments to report any costs and benefits in a year as a result of machinery-of-government changes in their annual reports. The updated report should include guidance so that the data in annual reports are provided on a consistent basis across departments.

<sup>436</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.3



The Committee also sought details about the anticipated benefits of the machinery-of-government changes. Departments indicated that the main expected benefits related to improved service delivery rather than cost reductions. However, some departments indicated that they expected some reductions in expenses in the long-term as a result of the machinery-of-government changes. The Department of Economic Development, Jobs, Transport and Resources explained that it is currently relocating staff in central Melbourne to consolidate and co-locate business groups.<sup>437</sup> The Department also noted that it ‘expects to realise efficiencies through scale, for example in relation to procurement and accommodation, which will be realised fully in future financial years’.<sup>438</sup>

The Department of Health and Human Services similarly noted that the changes ‘will, over time, result in administrative efficiencies, with a consolidated shared services approach to corporate functions – including human resources, information technology, legal and financial services’.<sup>439</sup> The Department also indicated that ‘There are not expected to be redeployments, contract non-renewals or other means of reducing staff numbers relied upon as a result of machinery of government changes’.<sup>440</sup> The Department did not provide further details about how the efficiencies will be achieved without redeployments or other means of reducing staff.

**FINDING 61:** Some departments indicated that the machinery-of-government changes may result in reduced expenses in future years through efficiencies.

## 7.5 Base funding

The budget papers distinguish two strands of funding for departments:<sup>441</sup>

- ‘base funding departments receive for ongoing programs’
- new initiatives.

New initiatives are generally time-limited, providing funding for between one and five years. However, some initiatives are described as ‘ongoing’, in which case the Committee understands that this funding is added to future base funding.

Ongoing programs and new initiatives are both part of the output prices that departments charge the Government for the delivery of goods and services (see Section 5.5 of this report).

<sup>437</sup> *ibid.*, p.3.

<sup>438</sup> *ibid.*, p.2.

<sup>439</sup> Department of Health and Human Services, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 26 June 2015, p.2.

<sup>440</sup> *ibid.*, p.3.

<sup>441</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.113.

'Base output prices' are referred to in the Department of Treasury and Finance's Budget and Financial Management Guidances, a series of documents providing details about the State's fiscal system. The Guidances note that these prices are increased each year 'to maintain alignment with movements in the rate of inflation. This ensures departments' ability to deliver services is not eroded over time by inflation'.<sup>442</sup> However, the term is not defined and it is not clear whether this refers to 'base funding departments receive for ongoing programs' or to something else.

The value of new initiatives is clearly disclosed in the budget papers. However, as in previous budget papers, the value of base funding is not revealed. The Committee sought details from each department as part of the Budget Estimates General Questionnaire. Departments provided a variety of responses:<sup>443</sup>

- three departments referred to the 'original base year for 2014-15' as something created four or five years ago and did not provide any quantified numbers
- two departments provided figures for output appropriations based on the appropriation bills
- the four remaining departments provided other figures, though these included fixed-term initiatives in some cases, apparently contradicting the concept of base funding as ongoing programs.

These variations suggest that there is no common understanding of what base funding is. Given that base funding is referred to in the budget papers (and base output prices are referred to in the Budget and Financial Management Guidances), the Committee considers that this concept should be more clearly articulated.

The lack of clarity around base funding may also be an indicator that the budget estimates are not calculated by escalating the cost of ongoing programs and adding the cost of time-limited initiatives. In this case, additional clarity should be provided relating to:

- how the funding for new initiatives listed in Budget Paper No.3 each year impacts on departmental revenue and output prices
- what is escalated in line with inflation according to the Budget and Financial Management Guidances.

The Committee considers that additional clarification and disclosure by the Department of Treasury and Finance in this area would be beneficial. The Committee also considers that there would be benefit in an independent review by the Auditor-General of whether the way that output prices are calculated is clearly and accurately explained.

<sup>442</sup> Department of Treasury and Finance, *BFMG - 06 Departmental Funding Model - Output Pricing* (2007), p.133. The Guidances note a number of circumstances in which funding escalation may not be in line with the inflation.

<sup>443</sup> Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire, question 15.

**FINDING 62:** The budget papers refer to ‘base funding’ for ongoing programs. However, the concept of base funding was not clear to departments when questioned, suggesting that there may be a difference between the way that the funding process is described and actual practice.

**RECOMMENDATION 40:** Future budget papers clarify what is meant by ‘base funding’ and explain the relationship between base funding, initiative funding and output prices.

**RECOMMENDATION 41:** The Department of Treasury and Finance clarify the Budget and Financial Management Guidances to include a definition of ‘base output price’ and how the escalation of this relates to the budget estimates.

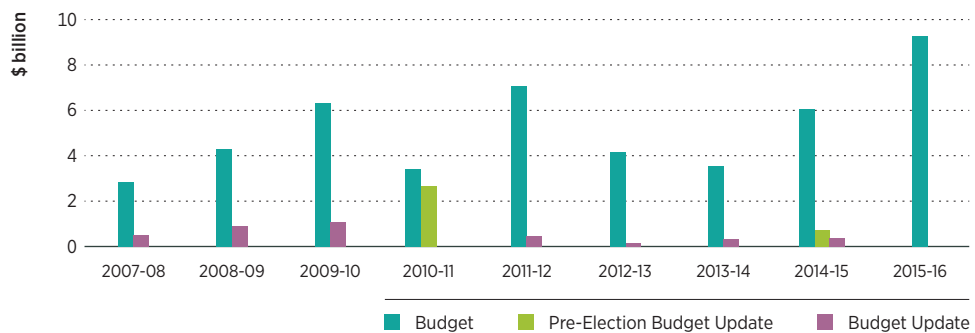
**RECOMMENDATION 42:** The Auditor-General conduct an audit of whether the way that output prices are calculated is clearly and accurately articulated by the Department of Treasury and Finance in its Budget and Financial Management Guidances and other documentation.

## 7.6 New initiatives

The 2015-16 budget papers include new output initiatives with a total value (over five years) of \$9.3 billion.<sup>444</sup> This includes election commitments (see Section 9.2 of this report), the continuation of lapsing initiatives (see Section 7.8) and other new programs.

As can be seen from Figure 7.6, this is a larger amount than has been seen in recent budgets.

**Figure 7.6** New output initiatives, current and previous budgets (five-year totals), 2007-08 to 2015-16



Note: Initiatives included in previous budget updates have been removed from the totals given in Budget Paper No.3 prior to 2010-11 to avoid double counting.

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2008-09 to 2015-16; Department of Treasury and Finance, *Victorian Budget Update*, 2008-09 to 2014-15; Department of Treasury and Finance, *Victorian Pre-Election Budget Update*, 2010 and 2014.

<sup>444</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

## 7.6.1 Main initiatives

The ten largest new initiatives (based on the five-year totals of expenses) are listed in Table 7.5.

**Table 7.5** Largest new output initiatives, 2015-16 Budget

	Funding (five-year total) (\$ million)
<i>Education State</i>	1,424.3
<i>School Enrolment Based Funding</i>	1,137.5
<i>Meeting Hospital Services Demand</i>	970.0
<i>Social and Community Services Equal Remuneration Order</i>	889.0
<i>Premier's Jobs and Investment Fund (including the 'start-up' initiative)</i>	508.0
<i>Regional Jobs and Infrastructure Fund</i>	500.0
<i>TAFE Rescue Fund</i>	200.0
<i>Future Industries Fund (including New Energy Jobs Fund)</i>	200.0
<i>Hospital Beds Rescue Fund</i>	200.0
<i>More Support for People with Disabilities and Their Families</i>	151.1

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

Together, these ten initiatives account for \$6.2 billion (66.5 per cent of the total new initiative funding).

### Education State

The Minister for Education provided details about a number of issues connected with the *Education State* initiative as part of the budget estimates hearings.<sup>445</sup> He explained:<sup>446</sup>

In terms of the education state, \$1.4 billion over five years has been set aside to implement the first phase of the education state strategy. This funding will be directed into initiatives that the evidence shows will improve the outcomes of Victorian school students. As a government we are committed to addressing student disadvantage and ensuring that funding is directed to the areas that need it most. This is consistent with our commitment to the Gonski agreement. There is an unacceptable link between low achievement and student disadvantage. We are focused on breaking this link and ensuring that all students, regardless of their background, have the skills to shape their future. The government will consult with stakeholders, including schools and school leaders, on the development of new school initiatives and proposed delivery models. Announcements for these new initiatives to support the education state will be made in the coming months.

<sup>445</sup> Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015.

<sup>446</sup> *ibid.*, pp.3-4.

The Minister stated that this funding acquits the State's commitment to the National Education Reform Agreement (referred to as the 'Gonski agreement') in the 2015, 2016 and 2017 school years.<sup>447</sup> Under this agreement, school funding is determined by a base rate per student with additional funding in particular circumstances which create disadvantage.<sup>448</sup>

As noted in Section 4.6.2 of this report, the Commonwealth Government has indicated that it will provide school funding using a different methodology from the 2018 school year onwards.<sup>449</sup> In terms of funding from the Victorian Government in 2018 and onwards, the Minister for Education indicated that this had not yet been finalised.<sup>450</sup> Part of the *Education State* initiative funds 'a review of Victorian education funding and how it is allocated' to be conducted by the Hon. Steve Bracks AC.<sup>451</sup> The Minister for Education indicated that this review:<sup>452</sup>

... will consider how government school funding is currently allocated and used; commonwealth contributions to government school funding in Victoria; how the student resource package is calculated, constructed and distributed; and how to make sure the system is clear and transparent for principals and school communities on school funding and how it is determined. The review will be completed by the end of 2015. There will be recommendations to me on how to deliver a funding system that supports schools to achieve the best results for Victorian students.

The Minister also informed the Committee that there would be transparency in the future around the additional Gonski-related funding:<sup>453</sup>

Each and every school will have a specific line item in their indicative budgets in September outlining the additional Gonski-related funding, so the education state funding, which is the Gonski national agreement funding – the additional funding that we have allocated for [20]16 and 17 in full. When schools receive their indicative budgets, they will see that in complete transparency.

The Minister noted that the Government will publish details of how the individual schools' portions of the funding have been calculated.<sup>454</sup>

The Committee welcomes these commitments to disclosure.

The National Education Reform Agreement includes a number of performance indicators to assess whether the funding is being spent effectively.<sup>455</sup> The Committee may examine the results as part of future inquiries.

<sup>447</sup> *ibid.*, p.3; cf. Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.50.

<sup>448</sup> Council of Australian Governments, *National Education Reform Agreement* (2013), pp.17-18.

<sup>449</sup> Commonwealth of Australia, *Budget Paper No.2: Budget Measures 2014-15* (2014), p.91; cf. Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015, p.5.

<sup>450</sup> Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015, p.5.

<sup>451</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.50.

<sup>452</sup> Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015, p.23.

<sup>453</sup> *ibid.*, p.15.

<sup>454</sup> *ibid.*, p.16.

<sup>455</sup> Council of Australian Governments, *National Education Reform Agreement* (2013), pp.7-8.

## School Enrolment Based Funding

Negligible details are provided in the budget papers about the *School Enrolment Based Funding* initiative. The budget papers simply note that, ‘Additional and ongoing funding is provided for government and non-government schools to meet forecast student enrolments up to the end of the 2017 school year’.<sup>456</sup>

Enrolment-based funding is a regular component of the funding for education institutes, with the funding based on pupil numbers.<sup>457</sup> In 2012, the Auditor-General noted that budget estimates for school enrolment-based funding had been insufficient for three years in a row (2009-10 to 2011-12) and had been supplemented through Treasurer’s Advances<sup>458</sup> (that is, funding provided in the appropriation bills for the Treasurer to allocate to departments through the year for ‘urgent claims’). The Committee notes that school enrolment-based funding was also supplemented through a Treasurer’s Advance in 2012-13<sup>459</sup> and possibly through a payment from advances in 2013-14.<sup>460</sup>

The Auditor-General noted that ‘The year on year requirement to source additional funds through TAs [Treasurer’s Advances] raises concerns with the method for calculating the budget figures.’ The Auditor-General also suggested that this may not be an appropriate use of Treasurer’s Advances.<sup>461</sup>

The Committee hopes that the additional funding budgeted through the *School Enrolment Based Funding* initiative will remove the need to draw on Treasurer’s Advances in future years and will watch to see if it is successful.

## Meeting Hospital Services Demand

The budget papers provide the following details about the *Meeting Hospital Services Demand* initiative:<sup>462</sup>

Additional funding will enable health services to respond to growing patient demand across Victoria. Services targeted include emergency department presentations, intensive care, maternity admissions, elective surgery, specialist clinics, palliative care, chemotherapy, radiotherapy, dialysis, sub-acute care and Victoria’s contribution to National Blood Products.

At the budget estimates hearings, the Minister for Health estimated that the extra funding would enable hospitals to admit an additional 60,000 patients and treat an additional 40,000 people per year in emergency departments.<sup>463</sup>

<sup>456</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.51.

<sup>457</sup> Victorian Auditor-General’s Office, *Portfolio Departments and Associated Entities: Results of the 2011-12 Audits* (2012), p.29.

<sup>458</sup> *ibid.*

<sup>459</sup> Department of Treasury and Finance, *2012-13 Financial Report* (2013), p.170.

<sup>460</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.193 - the report notes that a payment was made to the Department of Education and Early Childhood Development for ‘enrolment based funding’ but does not specify whether this was for schools, kindergartens, TAFEs or other education institutions.

<sup>461</sup> Victorian Auditor-General’s Office, *Portfolio Departments and Associated Entities: Results of the 2011-12 Audits* (2012), pp.28-30.

<sup>462</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.66.

<sup>463</sup> Hon. Jill Hennessy MP, Minister for Health, *2015-16 Budget Estimates Transcript of Evidence*, 13 May 2015, pp.2, 7.

The budget papers note that the funding estimates for this initiative include a contribution from the Commonwealth Government.<sup>464</sup>

**FINDING 63:** The 2015-16 Budget provides funding for \$9.3 billion of new output initiatives. The largest new initiatives relate to health and education. Other large initiatives also relate to social and community services and boosting jobs and the economy.

## 7.7 Funding the new initiatives

As noted in Section 7.4.1 of this chapter, the cost of these new initiatives has been partially offset by:

- expenditure reduction initiatives, which reduce departments' expenses by either finding more efficient ways to deliver services or by reducing the services delivered
- the reprioritisation of funding from existing programs and other departmental sources
- the use of 'contingencies' set aside in previous budget estimates.

### 7.7.1 Expenditure reduction initiatives

The 2015-16 budget papers include nine expenditure reduction initiatives,<sup>465</sup> intended to reduce expenses by \$334.5 million over four years.<sup>466</sup> These are all reflections of the Labor Party's election commitments, as discussed in Section 9.2.8 of this report.

Figure 7.7 below compares the value of these initiatives to expenditure reduction initiatives in previous budgets. The figure shows that the value of new initiatives in this budget is higher than the 2014-15 Budget but significantly smaller than was seen between 2011-12 and 2013-14.

The largest initiative is *Abolish Taxpayer Funded Political Advertising*, which is expected to save \$38.4 million per year.<sup>467</sup> The budget papers note that work is being undertaken to develop a final implementation plan for this initiative.<sup>468</sup>

The other initiatives primarily relate to machinery-of-government changes and administrative efficiencies. Two initiatives also relate to the workforce - *Reduce the Number of Executive Officers* and *Reduce the Use of Labour Hire Firms*.

<sup>464</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.65.

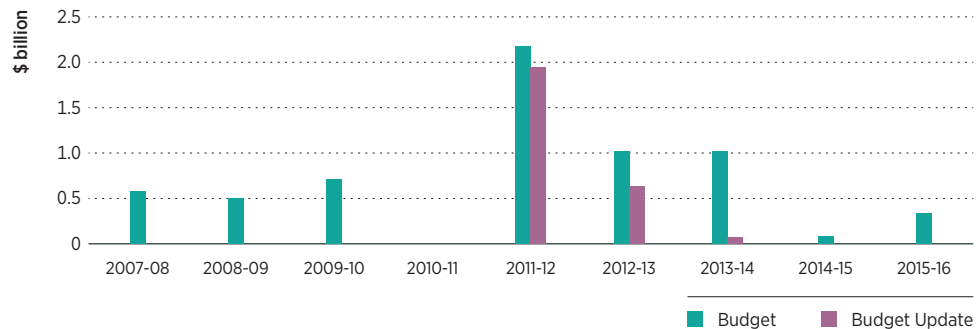
<sup>465</sup> Referred to in the budget papers as 'efficiency and expenditure reduction measures', 'output efficiencies' and 'savings'.

<sup>466</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.105.

<sup>467</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.105.

<sup>468</sup> *ibid.*

**Figure 7.7** New expenditure reduction initiatives, current and previous budgets (five-year totals)



Note: No expenditure reduction initiatives were included in the 2010 or 2014 Pre-Election Budget Updates.

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2008-09 to 2015-16; Department of Treasury and Finance, *Victorian Budget Update*, 2008-09 to 2014-15; Department of Treasury and Finance, *Victorian Pre-Election Budget Update*, 2010 and 2014.

The Committee sought details in its questionnaire about the impact of expenditure reduction initiatives on departments. In relation to the new initiatives in the 2015-16 Budget:

- five departments indicated that they expected no impact or negligible impact on service delivery<sup>469</sup>
- the Department of Treasury and Finance responded that it 'is committed to finding efficiencies while continuing to deliver services through its allocated resources'<sup>470</sup>
- the Department of Justice and Regulation indicated that it had not yet developed an implementation plan as it was expecting 'further savings to be allocated from the LFS [*Labor's Financial Statement 2014*] which are yet to be quantified'<sup>471</sup>
- the Parliamentary Departments and Court Services Victoria stated that they were not affected by expenditure reduction initiatives in the 2015-16 Budget.<sup>472</sup>

During the 57<sup>th</sup> Parliament, the former Public Accounts and Estimates Committee raised some concerns about the way that expenditure reduction initiatives were implemented and reported. The budget papers often specified the ways in

<sup>469</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.20; Department of Education and Training, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 16 June 2015, p.16; Department of Environment, Land, Water and Planning, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 22 June 2015, p.12; Department of Health and Human Services, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 26 June 2015, p.16; Department of Premier and Cabinet, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.12.

<sup>470</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.14.

<sup>471</sup> Department of Justice and Regulation, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 11 June 2015, p.24.

<sup>472</sup> Parliamentary Departments, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.10; Court Services Victoria, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 11 June 2015, p.12.



which the Government expected expenditure to be reduced (such as reducing advertising or the use of consultants). In practice, though, departments determined how their expenditure was reduced and could choose to reduce expenditure in ways that varied from the Government's stated intentions. No mechanisms were put in place to indicate whether or not the implementation of expenditure reductions by departments had impacted on service delivery.<sup>473</sup>

The Committee notes that these concerns have not been addressed and believes that there is scope for improvement to reporting in this area. The Department of Treasury and Finance's Model Report (which sets out the requirements for departments in preparing their annual reports) could be updated to enhance disclosure in this area.

**FINDING 64:** The budget papers estimate that new expenditure reduction initiatives will reduce expenses by \$334.5 million over four years. Departments have generally indicated that they expect this to be achieved without any impacts on service delivery. However, there is no reporting structure in place to assess whether or not these expectations will turn out to be accurate.

**RECOMMENDATION 43:** The Department of Treasury and Finance update the Model Report to require all departments to list expenditure reduction targets set for the relevant year and how these targets were met. This should include details of any impacts on service delivery, including quantification of the impacts where possible.

## 7.7.2 Reprioritisation of existing funding

The cost of the new initiatives has also been partly offset through the reprioritisation of existing funding. This includes reducing the funding previously allocated to particular programs so that this funding can be used for the new initiatives. The budget papers indicate that \$1.5 billion of funding was expected to come from reprioritisation over the forward estimates period.<sup>474</sup>

Prior to the 2014 Victorian election, the Labor Party released *Labor's Financial Statement 2014*, a document detailing the election commitments expected to be implemented between 2014 and 2018. This included \$804.5 million of reprioritisations between 2014-15 and 2018-19. The bulk of this (\$608.0 million) was expected to come from 'reform[ing] industry and innovation policy'.<sup>475</sup>

For the remaining \$196.5 million, *Labor's Financial Statement 2014* lists the programs from which funding would be reprioritised, the amount reprioritised from each program and the budget or budget update in which the program was announced.<sup>476</sup>

<sup>473</sup> Public Accounts and Estimates Committee, *Report on the 2013-14 Budget Estimates - Part Two* (2013), pp.122-4; Public Accounts and Estimates Committee, *Report on the 2011-12 Financial and Performance Outcomes* (2013), pp.56-7.

<sup>474</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

<sup>475</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), p.10.

<sup>476</sup> *ibid.*, p.11.

However, the Committee notes that there is no equivalent reporting in the budget papers, which simply list the total amounts to be reprioritised from each year.<sup>477</sup> The Committee sought further details from departments through its questionnaire. The responses can be seen in Appendix A7.2.

These responses identify a number of programs from which funding has been reprioritised. They also indicate that, in some cases, funding has been reprioritised from base funding. The programs identified by departments totalled \$1.2 billion, representing most of the \$1.5 billion identified in the budget papers. Departments' responses indicate that the bulk of the reprioritised funding comes from two areas:

- the *Regional Growth Fund* (providing \$500.0 million over four years), which is being replaced by the *Regional Jobs and Infrastructure Fund* (also \$500.0 million over four years)<sup>478</sup>
- the reform of industry and innovation policy (providing \$470.0 million over four years). The Department of Economic Development, Jobs, Transport and Resources explained, 'The Government is reforming its approach towards driving economic growth, jobs and innovation in Victoria. A number of programs are being assessed as to whether they are suitable for the reformed approach'.<sup>479</sup>

The Committee considers that the break-down in *Labor's Financial Statement 2014* (excluding the reform of industry and innovation policy) was a clear and effective means of communicating what was intended to be reprioritised and that future budget papers should produce similar information. This would assist the Parliament and the community to better understand what programs have been affected by reprioritisation decisions in the budget.

**FINDING 65:** The budget papers indicate that \$1.5 billion of the cost of new initiatives will be met by reprioritising funding previously provided to departments. The budget papers do not include details of which programs have been affected by the reprioritisation.

**RECOMMENDATION 44:** Future budget papers include details of the programs from which funding has been reprioritised, including:

- (a) the name of the program, initiative or project from which funding has been reprioritised
- (b) the amount reprioritised from each year of the forward estimates period
- (c) the budget in which the initiative was released (where relevant).

<sup>477</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

<sup>478</sup> Hon. Jaala Pulford MLC, Minister for Regional Development, *2015-16 Budget Estimates Transcript of Evidence*, 18 May 2015, p.4.

<sup>479</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.20.

**RECOMMENDATION 45:** The Department of Treasury and Finance update the Model Report to require departments to report on the actual amounts of money reprioritised during the year, including:

- (a) the name of the program, initiative or project from which funding has been reprioritised
- (b) the amount reprioritised in the year
- (c) the budget in which the initiative was released (where relevant).

### 7.7.3 Funding from contingencies

In each budget, the estimates for output expenses across the forward estimates period include an allowance for initiatives that will be released in future budgets. These amounts are referred to as ‘contingencies’ in the budget papers. When new initiatives are released in later budgets, the cost of these new initiatives can be offset by reducing the contingency. The effect of this is to fund the new initiatives without increasing the total output expenses compared to the previous budget estimates.

At the budget estimates hearings, the Treasurer informed the Committee that:<sup>480</sup>

The contingencies represent a very important part of the budget because they allow us as a government to allow for future spending, including might I say on unanticipated events and new initiatives in future budgets, without impacting upon our fiscal aggregates. A budget without adequate contingencies runs the risk of actual expenses exceeding estimated expenses, which may ultimately result in not achieving projected operating results.

The budget papers indicate that contingencies were reduced by \$4.8 billion over the forward estimates period to offset the cost of the new output initiatives.<sup>481</sup> However, as discussed in Section 7.4.1, additional money was also put into contingencies for the funding of future initiatives.

Table 7.6 compares the contingencies in the 2015-16 budget estimates to the 2014 Pre-Election Budget Update. It shows that the amount of contingencies has dropped in each year between 2015-16 and 2017-18, though by relatively small amounts in the last two years.

**Table 7.6** Output contingencies, 2014 Pre-Election Budget Update and 2015-16 Budget

	2014-15 (\$ million)	2015-16 (\$ million)	2016-17 (\$ million)	2017-18 (\$ million)	2018-19 (\$ million)
2014 Pre-Election Budget Update	177.9	872.9	1,755.9	2,948.7	n/a
2015-16 Budget	n/a	517.6	1,636.3	2,923.6	4,193.5

Sources: Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.52; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.35.

<sup>480</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.23.

<sup>481</sup> Committee calculation based on the sum of ‘adjustments’ and ‘contingency offset for new policy’ in Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

The total included across the forward estimates period, however, is significantly more than has been typically included in previous budgets for their forward estimates periods. The total output contingencies from the previous three budgets, for example, varied between \$4.2 and \$5.8 billion.<sup>482</sup> This contrasts with the \$9.3 billion included in the 2015-16 Budget. The Treasurer explained:<sup>483</sup>

So our existing contingencies at the 2014-15 budget update we utilised to fund the government's election commitments, consistent with our LFS [*Labor's Financial Statement 2014*] statement released during the election campaign, so that they had no impact on the budget bottom line. It is also our intent to keep our commitments within the envelope available at the 2014 election budget update, and I am pleased to note that this was in fact achieved in the context of the budget papers that we brought forward.

... contingencies are projected to total about \$9.3 billion over the budget and forward estimates. That represents a significant increase from the 2014 pre-election budget update, where total output contingencies came to \$5.8 billion over the four-year forward estimates period. So a considerably larger and expanded sum.

... [We have chosen] to put in higher levels of contingency in order to acquit future opportunities, future decisions that governments will have to make in the future.

The Treasurer also pointed out that Moody's Investors Services noted the greater contingencies, describing it as a 'fiscally prudent' approach.<sup>484</sup>

The effect of these higher contingencies is that a larger value of new initiatives can be funded in future budgets without increasing the estimates for output expenses.

**FINDING 66:** The Government has used \$4.8 billion of the contingency allowance put aside in previous budget estimates to offset the cost of its new output initiatives. The Government has also put additional money into contingencies. As a result, the contingencies in this budget's forward estimates period are larger than in other recent budgets, providing scope for funding a larger value of new initiatives in future budgets without impacting on the estimates for total output expenses.

## 7.8 Lapsing and discontinued programs

As noted earlier in this chapter, a portion of departmental funding comes from time-limited initiatives. At the conclusion of the period for which these initiatives are funded, they are said to 'lapse'. When funding for a program lapses, the program may be:

- funded for an additional period through a new budget initiative

<sup>482</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: Statement of Finances, 2012-13 to 2014-15*.

<sup>483</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, pp.23-4.

<sup>484</sup> Moody's Investors Services, *Announcement: Moody's Comments on Victoria's 2015/16 Budget (2015)*; cf. Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, pp.19, 24.

- continued by the department using its own funding
- discontinued, especially where its goals have been achieved or where the Government's priorities have changed.

The budget papers do not provide any information about lapsing programs, other than noting the final year of funding at the time that a new initiative is released. The Committee sought details through its Budget Estimates Questionnaire.

Departments identified 91 programs as lapsing in 2014-15, with a total expenditure exceeding \$281.3 million in their last year.<sup>485</sup> The list can be seen in Appendix A7.3, with further details in the questionnaire responses on the Committee's website ([www.parliament.vic.gov.au/paec](http://www.parliament.vic.gov.au/paec)). In many cases, departments indicated that new initiatives provided similar community benefits or that the lapsing initiative would continue to be funded through other means.

However, the Committee notes that the 91 identified initiatives are a small portion of the number of initiatives initially expected to lapse in 2014-15. The budget papers between 2011-12 and 2014-15 listed 280 initiatives for which the last year of funding was 2014-15. At least some of the discrepancy between these figures is a result of:

- budget initiatives being ongoing (that is, not time-limited) without this being identified in the budget papers
- new initiatives providing further funding for previous initiatives without mentioning the original initiatives.

However, it is often difficult to track these changes, as the initiative descriptions in budget papers do not always clearly identify whether funding is ongoing or is a supplement to a previous initiative. The Committee considers that the clarity of funding decisions in the budget papers would be improved by consistently noting these situations.

**FINDING 67:** Departments identified 91 initiatives that lapsed in 2014-15, representing over \$281.3 million of expenditure in 2014-15. Other initiatives apparently due to lapse in 2014-15 may not have done so because the funding was ongoing or because subsequent initiatives provided further funding. However, this is not always clearly stated in the budget papers, making it difficult to know what has happened with an initiative.

**RECOMMENDATION 46:** Future budget papers clearly state in the description of a new initiative if the initiative:

- provides ongoing funding
- provides additional funding for a previously released initiative.

<sup>485</sup> The Department of Environment, Land, Water and Planning identified five lapsing programs for which it did not include expenditure in 2014-15.

Where the Government's priorities change, programs may also be terminated earlier than originally intended. In addition to lapsing programs, the departments identified the following output programs as curtailed, deferred or discontinued as a result of changes to strategic priorities:<sup>486</sup>

- industry and innovation policy programs
- *Jobs in the 21<sup>st</sup> Century* initiatives
- *CenITex Transformation* (Project Atlas), which was 'on pause' at the time of the questionnaires and has subsequently been discontinued<sup>487</sup>
- the Construction Code Compliance Unit.

## 7.9 Risks to the budget estimates

In discussing risks to the output expenses estimates, the budget papers note that employee expenses are the largest expense.<sup>488</sup> The budget estimates are made based on currently agreed enterprise bargaining agreements, with an assumption that they will be unchanged over the forward estimates period.<sup>489</sup> The sensitivity analysis in the budget papers estimates that, if all government enterprise bargaining agreements were 1 percentage point higher than assumed, the expenses would increase by an average of \$262 million per year across the forward estimates period.<sup>490</sup>

The budget papers also indicate that:<sup>491</sup>

Another key risk is growth in demand for government services exceeding current projections. This can occur, for example, as a result of higher than forecast population growth or expenditure in response to unforeseen events such as natural disasters, including bushfires and floods.

The estimates incorporate contingency provisions to mitigate the impact of expenditure risks, which may be realised during the budget and forward estimates. The contingency provisions are designed to address the likely growth in Victoria's population and consequent derived demand for government services.

<sup>486</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.5; Department of Premier and Cabinet, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.4; Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.3.

<sup>487</sup> CenITex, *About CenITex* <[www.cenitex.vic.gov.au/web33/home.nsf/Web+Pages/8419EFE34BFCE424CA25755C0015B29B?Open&Expand=2.1](http://www.cenitex.vic.gov.au/web33/home.nsf/Web+Pages/8419EFE34BFCE424CA25755C0015B29B?Open&Expand=2.1)>, viewed 22 September 2015.

<sup>488</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.64.

<sup>489</sup> *ibid.*, p.84; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.22; for further details of the Government's wages policy, see Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, pp.12-13.

<sup>490</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.78.

<sup>491</sup> *ibid.*, p.64.

In response to the Budget Estimates Questionnaire, some departments also identified risks that were specific to each department. These are all included in Appendix A7.4. Salary risks and demand risks were identified by several departments. Other concerns included:

- the costs of inputs being higher than expected
- actual growth in expenses being more than the growth in funding
- Commonwealth-State arrangements that are yet to be finalised
- ageing assets.

All departments which identified risks indicated that they had measures in place to mitigate these risks. The Committee will examine whether these measures have been sufficient as part of its Inquiry into the 2015-16 Financial and Performance Outcomes.

**FINDING 68:** Key risks to the expenses estimates identified by the Government include salary increases and demand for services being higher than expected. Departments indicated that measures were in place to mitigate these and other key risks.





# 8 Asset investment

## 8.1 Introduction

The Government plans to invest \$21.3 billion on infrastructure and other physical assets over the next four years (see Table 8.1). This includes projects released in past budgets, new asset initiatives announced in the 2015-16 Budget and an allowance for the funding of future projects.

**Table 8.1** Government infrastructure investment<sup>(a)</sup>, 2014-15 to 2018-19

	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
Government infrastructure investment (\$ million)	4,164.5	5,190.9	6,528.8	4,484.0	5,112.1
Annual growth					
• (\$ million)	-1,374.1	1,026.4	1,337.9	-2,044.8	628.1
• (per cent)	-24.8	24.6	25.8	-31.3	14.0
Average annual growth rate (2015-16 to 2018-19) (per cent) <sup>(b)</sup>			-0.5		

(a) This measure reflects the total direct asset investment made by the general government sector, general government sector funding for projects delivered through other sectors and expenditure by the private sector on construction of PPPs on behalf of the general government sector, less the proceeds from asset sales.

(b) Compound annual growth rate. Calculated by the Committee.

Source: Department of Treasury and Finance, *Net Infrastructure Investment* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates)>, viewed 4 June 2015.

More details about this expenditure can be found in the later sections of this chapter.

In terms of new projects, the 2015-16 budget papers announced 91 new asset initiatives, with a total estimated investment across the life of the projects between \$19.0 and \$22.0 billion.<sup>492</sup> This includes the *Melbourne Metro Rail Project*, the *Level Crossing Removal Program* and the purchase of 37 high-capacity metro trains for deployment on the Cranbourne-Pakenham rail corridor.<sup>493</sup> These projects are discussed further in Section 8.5.3 of this chapter.

In analysing the Government's asset investment plans, this chapter will examine the following:

- What is the Government's strategy for asset investment? (Section 8.2)
- What are the estimates for the different components of asset investment over the next four years? (Section 8.3.1-2)

<sup>492</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.60.

<sup>493</sup> *ibid.*, p.10.

- What do these estimates mean for Victorians? (Section 8.3.3)
- How do these estimates compare with previous estimates? (Section 8.4)
- What new initiatives are in the 2015-16 Budget? (Section 8.5)
- How will the Government fund asset investment over the forward estimates period? (Section 8.6)
- Which projects have been discontinued since the last budget? (Section 8.7)

## 8.2 The Government's asset investment strategy

### 8.2.1 The Government's goals for asset investment

As discussed in Section 2.3.2 of this report, the Government's long-term financial management objectives include growing infrastructure to meet the needs of a growing population and using infrastructure to achieve economic, social and environmental benefits (see Table 8.2).

**Table 8.2** Long-term financial management objectives

Priority	Objective
Sound financial management	Victoria's finances will be managed in a responsible manner to provide capacity to fund services and infrastructure at levels consistent with maintaining a triple-A credit rating.
Improving services	Public services will improve over time.
Building infrastructure	Public infrastructure will grow steadily over time to meet the needs of a growing population.
Efficient use of public resources	Public sector resources will be invested in services and infrastructure to maximise the economic, social and environmental benefits.

Source: Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.14.

As noted in Section 2.3.2, the long-term financial management objectives are supported by three medium-term targets. However, none of these specifically relates to infrastructure.

The previous government had a specific target related to infrastructure: 'Infrastructure investment of 1.3 per cent of GSP [gross state product] (calculated as a rolling five-year average)'.<sup>494</sup> The Committee notes that the 2015-16 Budget does not include this target for infrastructure and no substitute target has been provided.

<sup>494</sup> Department of Treasury and Finance, *Budget Paper No.2: 2014-15 Strategy and Outlook* (2014), p.9.

The Committee sought details from the Department of Treasury and Finance as to why a specific target for infrastructure is not included in the 2015-16 budget papers. In response, the Department stated that, ‘the Government revised its fiscal strategy (and measures) as part of the 2015-16 Budget to more closely align with its fiscal policies and priorities.’<sup>495</sup>

As infrastructure features in the financial management objectives, it is not clear to the Committee why removing the target more closely aligns the fiscal strategy and measures with the fiscal policies and priorities. The Committee considers that having a measureable target for infrastructure delivery is important for understanding and assessing the Government’s infrastructure investment plans. Given the importance of infrastructure in the long-term financial management objectives, the Committee considers a measure and target to be important for understanding how the long-term objectives will translate into action in the shorter term.

**FINDING 69:** The Government’s long-term financial management objectives contain references to infrastructure delivery. However, the 2015-16 Budget does not set a quantified target for asset investment over the medium term.

**RECOMMENDATION 47:** Future budget papers include a quantified target for infrastructure investment over the medium term.

## 8.2.2 Delivery bodies and processes

The 2014-15 Budget Update and 2015-16 Budget provide funding for two new infrastructure bodies: Infrastructure Victoria and Projects Victoria.<sup>496</sup> According to the budget papers, ‘these bodies will ensure that transport and infrastructure investments are strategically planned and efficiently delivered’.<sup>497</sup>

The budget papers indicate that Infrastructure Victoria ‘will provide independent and transparent advice to Government on infrastructure priorities and set a long term strategy for infrastructure investment that endures beyond election cycles’.<sup>498</sup>

The Special Minister of State further explained to the Committee:<sup>499</sup>

... \$40 million has been allocated to Infrastructure Victoria – \$10 million each year over the forward estimates – to try to ensure that we have the capability of identifying Victoria’s current and future infrastructure needs in terms of the significance they play both in the domestic Victorian economy but also within the Australian nationally significant infrastructure.

<sup>495</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.5.

<sup>496</sup> Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2015), p.123; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.10.

<sup>497</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.10.

<sup>498</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.313.

<sup>499</sup> Hon. Gavin Jennings MP, Special Minister of State, *2015-16 Budget Estimates Transcript of Evidence*, 21 May 2015, p.3.

In regard to Projects Victoria, the budget papers explain that it ‘will oversee the delivery of all major projects, research and develop appropriate project delivery models, and review and improve capability in project development and delivery’.<sup>500</sup>

The Special Minister of State further stated that:<sup>501</sup>

We are establishing Projects Victoria with a \$10 million allocation over the next four years to assist in making sure that we have a knowledge base and an understanding of how we keep those projects on track once they commence.

The Committee sought further details regarding the expected relationship between these two new infrastructure bodies and the current functions undertaken by Major Projects Victoria. The Department of Treasury and Finance indicated that:<sup>502</sup>

Infrastructure Victoria will be required to perform its legislative functions – independent, long term infrastructure planning, research and advice – in collaboration with all government departments and agencies, including Major Projects Victoria. Projects Victoria will work cooperatively with other government departments and agencies (including Major Projects Victoria) to oversee major project delivery and improve capability in project development and delivery.

Infrastructure Victoria will produce and regularly update a 30 year state infrastructure strategy and provide the Government with independent, expert advice on a range of infrastructure-related matters ... These roles will inform any decisions relating to the role of Major Projects Victoria.

The Infrastructure Victoria Bill 2015 to establish Infrastructure Victoria received Royal Assent on 8 September 2015.

### High-value and high-risk process

The Department of Treasury and Finance’s high-value and high-risk process identifies capital projects (including infrastructure and Information and Communication Technology projects) as high-value and high-risk if:<sup>503</sup>

- total estimated investment is > \$100 million, regardless of funding source; and/or
- the investment is identified as ‘high risk’ using a risk assessment tool; or
- Government identifies the investment as warranting extra rigour.

Identified projects are subject to higher levels of oversight. The Department of Treasury and Finance has stated that:<sup>504</sup>

<sup>500</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.93.

<sup>501</sup> Hon. Gavin Jennings MP, Special Minister of State, *2015-16 Budget Estimates Transcript of Evidence*, 21 May 2015, p.3.

<sup>502</sup> Department of Premier and Cabinet, *Response to the Committee’s 2015-16 Budget Estimates Specific Questionnaire*, received 17 August 2015, p.1.

<sup>503</sup> Department of Treasury and Finance, *HVHR Investment Framework* (2014), p.1.

<sup>504</sup> *ibid.*

Greater rigour in HVHR [high-value and high-risk] investment development, approval and oversight will increase confidence in project delivery according to forecast cost, time and benefits.

This process was first outlined in the 2011-12 budget papers. Starting in 2011-12, each year's budget papers included a list of the projects classified as high-value and high-risk.<sup>505</sup> The Committee notes that the 2015-16 budget papers do not include this list or any other discussion of such projects. The Committee considers that the identification of high-value and high-risk projects in the budget papers added to the transparency and accountability of large-scale projects in the State and that this should be re-introduced in future budget papers.

**FINDING 70:** The High-Value and High-Risk Framework indicates that asset projects which are judged to be of high value and high risk should be subject to greater levels of oversight. Previous budget papers listed the projects that had been classified as high-value and high-risk. However, no equivalent list was included in the 2015-16 budget papers.

**RECOMMENDATION 48:** Future budget papers re-introduce the practice of listing all asset projects classified as high-value and high-risk.

### 8.2.3 Asset investment funding – *Asset Recycling Initiative*

The *Asset Recycling Initiative* was announced by the Commonwealth Government in 2014. It provides grants to the states of up to 15 per cent of the value of asset sales (referred to as 'divestments') as long as the proceeds are spent on infrastructure investments.<sup>506</sup>

The Commonwealth Government's 2015-16 budget papers further indicate that:<sup>507</sup>

[The *Asset Recycling Initiative*] creates an incentive for the states to unlock funds from existing state-owned assets to invest in additional infrastructure that will support economic growth and enhance productivity.

The Victorian Government has stated its intention to further explore possible asset sale opportunities. In relation to this, the 2015-16 budget papers indicate that:<sup>508</sup>

Where it is in the community's interest, capital currently tied up in mature businesses can be recycled to build new assets for the benefit of the community, which would not otherwise have been affordable. The Government will consider the potential for future asset recycling opportunities.

505 For example, Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), pp.3-5.

506 Commonwealth of Australia, *Building Australia's Infrastructure* (2014), p.5.

507 Commonwealth of Australia, *Budget Paper No.3: Federal Financial Relations 2015-16* (2015), p.1.

508 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.12.

The main divestment expected in Victoria across the forward estimates period is the proposed lease of the Port of Melbourne’s operations from 2015-16 (see Section 8.6 of this report).

The divestment of the Rural Finance Corporation in 2014 is another example of this strategy. The Government has indicated that the proceeds from this ‘will facilitate investment in new productive economic infrastructure in rural and regional Victoria, including the *Murray Basin Rail Project*’.<sup>509</sup>

**FINDING 71:** The Government expects to obtain additional resources in the future as part of the *Asset Recycling Initiative*. From 2015-16, these additional resources are expected to be obtained through the proposed lease of operations of the Port of Melbourne.

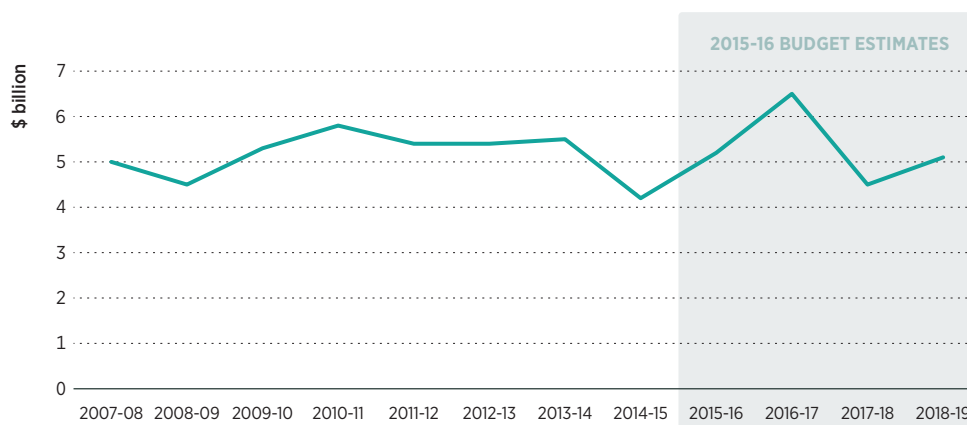
### 8.3 Estimates for asset investment

The budget papers utilise the ‘government infrastructure investment’ measure as an overall figure for asset investment.<sup>510</sup> It includes the three main modes of asset investment in Victoria (see Section 8.3.1 of this chapter).

Government infrastructure investment is forecast to be \$5.2 billion in 2015-16. This is \$1.0 billion more than the latest estimate for 2014-15 (\$4.2 billion).<sup>511</sup>

Figure 8.1 compares the government infrastructure investment estimates over the next four years to the amounts between 2007-08 and 2014-15.

**Figure 8.1** Government infrastructure investment, 2007-08 to 2018-19



Note: Excludes some one-off payments from the Commonwealth.

Source: Department of Treasury and Finance, *Net Infrastructure Investment* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates)>, viewed 4 June 2015.

<sup>509</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.6.

<sup>510</sup> This measure reflects the total direct asset investment made by the general government sector, general government sector funding for projects delivered through other sectors and expenditure by the private sector on construction of PPPs on behalf of the general government sector, less the proceeds from asset sales.

<sup>511</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.13.

Government infrastructure investment is expected to increase in 2016-17 to \$6.5 billion and then to be lower in the last two years of the forward estimates period. The Government expects government infrastructure investment to average \$5.3 billion per year from 2015-16 to 2018-19. This average is slightly higher than the expected average of \$5.1 billion per year between 2007-08 and 2014-15 (though funding from the Commonwealth Government in response to the global financial crisis is not included in the earlier figures).

**FINDING 72:** The budget papers estimate that government infrastructure investment will peak in 2016-17 at \$6.5 billion and then be less in the last two years of the forward estimates period. Government infrastructure investment is expected to average \$5.3 billion per year between 2015-16 and 2018-19, which is slightly higher than the annual average of \$5.1 billion from 2007-08 to 2014-15.

### Accuracy of asset investment estimates

The Committee has assessed the accuracy of past asset investment estimates by comparing the budget year estimates for 'net investment in fixed assets'<sup>512</sup> to the actual figures (see Table 8.3).

**Table 8.3** Estimated and actual figures for 'net investment in fixed assets', 2008-09 to 2013-14

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
Budget year estimate	3,938.4	6,960.6	6,369.5	6,143.4	5,794.3	5,826.0
Actual	4,047.1	5,710.5	6,639.6	5,228.9	5,202.0	5,204.7
Variance	108.7	-1,250.1	270.1	-914.5	-592.3	-621.3

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2008-09 to 2015-16.

The Committee notes that asset investment has proven difficult to accurately estimate in past budgets. As Table 8.3 shows, between 2008-09 and 2013-14, four of the six budgets overestimated asset investment for the budget year. In addition, when the expenditure has been overestimated, the variance has been much greater than the variance in years with an underestimation. As a result, the average variance for asset investment estimates has been an overestimation of \$499.9 million.

This tendency to overestimate asset investment is not discussed in the current or previous budget papers. This matter is further explored in Section 1.2.2 of this report.

**FINDING 73:** Asset investment has been overestimated in four of the six budgets between 2008-09 and 2013-14. The average variation between budget year estimates and actual expenditure has been an overestimation of \$499.9 million.

<sup>512</sup> This figure includes direct investment and investment through other sectors less proceeds from asset sales. See Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

### 8.3.1 Components of general government sector asset investment

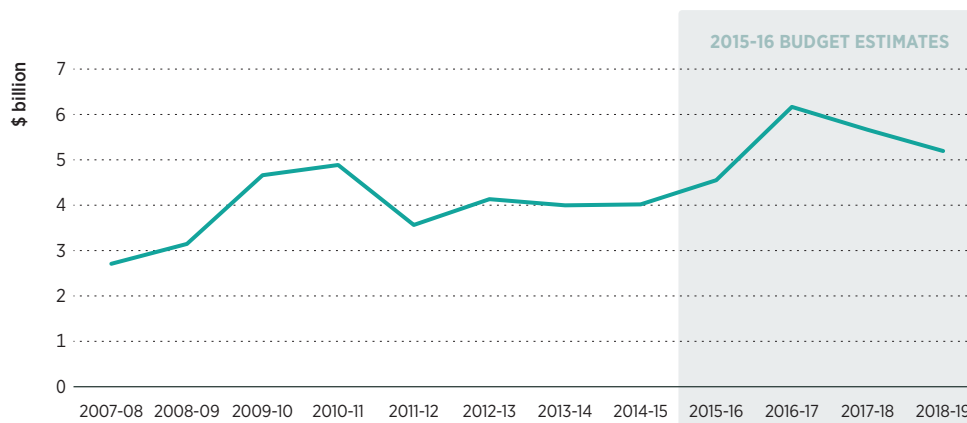
The Government delivers assets in three ways:

- direct investment<sup>513</sup> (that is, the traditional method), where general government sector bodies directly manage the construction or acquisition of assets
- investment through other sectors,<sup>514</sup> where the Government provides funds to other sectors, mainly the public non-financial corporations (PNFC) sector, to deliver asset investment projects in support of Government policy
- public private partnerships (PPPs), where the Government enters into an agreement with the private sector to finance and construct assets on behalf of the Government. The private sector operates and maintains the assets for a period of time established in the contract and then usually passes the ownership to the Government.

#### Direct investment

Direct investment consists of the acquisition or construction of asset projects by the general government sector through the departments or other general government sector agencies. Figure 8.2 shows the expected trend for direct asset investment from 2007-08 to 2018-19.

**Figure 8.2** Direct asset investment, general government sector, 2007-08 to 2018-19



Source: Department of Treasury and Finance, *Consolidated Cash Flow Statement – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 9 June 2015.

Direct investment estimates include both projects released in the 2015-16 Budget and continuing projects released in past budgets. They also include allowances for projects that are expected to be released in future budgets (known in the budget papers as ‘contingencies not allocated to departments’).<sup>515</sup>

<sup>513</sup> Referred to in the budget papers as ‘purchases of non-financial assets’.

<sup>514</sup> Referred to in the budget papers as ‘net cash flows from investments in financial assets for policy purposes’.

<sup>515</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.40.



The Committee sought further details in relation to the methodology used to quantify the ‘contingencies not allocated to departments’. The Department of Treasury and Finances indicated that:<sup>516</sup>

This item comprises two types of contingencies:

1. contingencies for government policy decisions made but not yet allocated, which includes provisions for election commitments to be funded in future budgets and asset policy decisions for which funding has yet to be allocated to departments; and
2. funding not allocated to specific purposes which is an unallocated provision available for future government asset investment decisions.

The Government expects direct investment to be \$4.6 billion in 2015-16 and then peak at \$6.2 billion in 2016-17, primarily driven by substantially higher contingencies related to ‘decisions made but not yet allocated’.<sup>517</sup> These contingencies are expected to increase from \$478.1 million in 2015-16 to \$2.0 billion in 2016-17.<sup>518</sup> Direct investment is expected to decline in the last two years of the forward estimates period, to \$5.7 billion in 2017-18 and \$5.2 billion in 2018-19.<sup>519</sup> The budget papers each year do not provide explanations for variations between individual years across the forward estimates period for direct investment. The Committee considers that this information would be valuable in understanding the Government’s future plans for asset investment.

In relation to ‘contingencies not allocated to departments’, the Committee notes that the 2015-16 budget papers provide a break-down of this item for the first time into ‘decisions made but not yet allocated’ and ‘funding not allocated to specific purposes’.<sup>520</sup> The Committee welcomes this disclosure and considers that it adds transparency to the role of contingencies in developing the budget estimates.

**FINDING 74:** The Government expects direct investment by departments and general government sector agencies to peak at \$6.2 billion in 2016-17, before declining to \$5.2 billion in 2018-19. As in previous years, the budget papers do not provide commentary explaining the year-to-year variations.

**RECOMMENDATION 49:** Future budget papers explain variations between individual years of the forward estimates period for direct investment (‘purchases of non-financial assets’) by the general government sector.

<sup>516</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.34-5.

<sup>517</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.40.

<sup>518</sup> *ibid.*

<sup>519</sup> *ibid.*

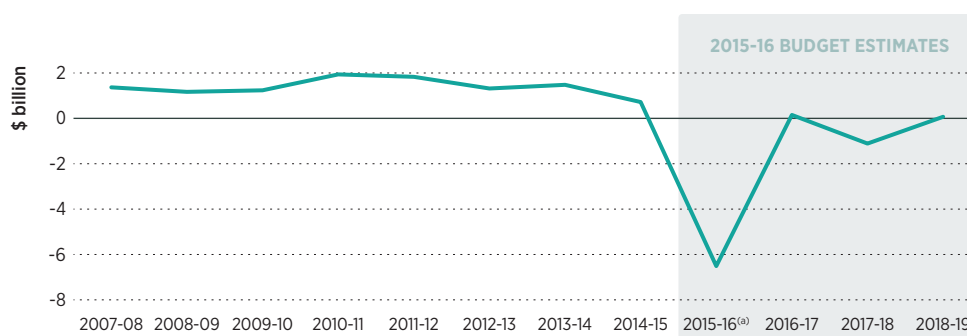
<sup>520</sup> *ibid.*

### Investment through other sectors

The Government also funds projects that are subsequently owned and operated by other sectors, particularly the public non-financial corporations (PNFC) sector. This type of investment is referred to in the budget papers as 'net cash flows from investments in financial assets for policy purposes'.<sup>521</sup> This line item in the budget papers includes both cash flows to other sectors for asset investment and cash flowing back from other sectors. The *2013-14 Financial Report* separately reported cash inflows and outflows.<sup>522</sup> However, the budget papers only provide net figures. This makes it difficult to understand how much is being provided to other sectors in years where there are significant amounts of cash flowing back.

Figure 8.3 shows the budget estimates for investment through other sectors from 2007-08 to 2018-19.

**Figure 8.3** Investment through other sectors, 2007-08 to 2018-19



(a) The estimate for 2015-16 primarily reflects the cash inflow to the general government sector as a result of the proposed lease of operations of the Port of Melbourne.

Source: Department of Treasury and Finance, *Consolidated Cash Flow Statement – General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 9 June 2015.

The Committee notes that investment through other sectors is expected to account for a smaller portion of the Government's asset investment over the forward estimates period in comparison to recent years. This partly reflects the completion in 2014-15 of the largest project funded in this way in recent years, the *Regional Rail Link*.

In two years of the forward estimates period, the budget estimates indicate that more cash will flow in from the other sectors than will flow out. The expected cash inflow of \$6.5 billion into the general government sector for 2015-16 reflects the proposed lease of the Port of Melbourne's operations (see Section 8.6 of this report).

<sup>521</sup> For example, Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.10.

<sup>522</sup> Department of Treasury and Finance, *2013-14 Financial Report* (2014), p.33.

A cash inflow to the general government sector of \$1.1 billion is also expected in 2017-18.<sup>523</sup> This inflow had not been anticipated in the 2014 Pre-Election Budget Update or the 2014-15 Budget Update,<sup>524</sup> indicating that a recent change in policy or external circumstances has led to this inflow. The budget papers do not provide any explanation for the matter, so the Committee sought details from the Department of Treasury and Finance. The Department responded that:<sup>525</sup>

... the movement between 2014 Pre-Election Budget Update and 2015-16 Budget in 2017-18 largely relates to increased capital receipts from the State's Public Financial Corporations.

It is not clear to the Committee what these receipts relate to, why they are expected or what changed between previous budget updates and this year's budget.

Similarly, there is a significant change between the 2014-15 Budget Update and the 2015-16 Budget in relation to line item 'other movements in non-financial assets'. At the time of the 2014-15 Budget Update, this item was estimated at \$318.5 million in 2016-17 and \$275.0 million in 2017-18.<sup>526</sup> In contrast, in the 2015-16 Budget, it is estimated at -\$1,381.0 million in 2016-17 and -\$1,250.6 million in 2017-18.<sup>527</sup> In response to the Committee's questionnaire, the Department of Treasury and Finance explained that this was a result of transfers of assets from the general government sector to the PNFC sector.<sup>528</sup> As with the above, the Committee considers that further explanation is required to understand the specific drivers of these updated estimates.

The former Committee recommended that budget papers should explain variations from one year to the next or from previous estimates for any component of the budget estimates where the variation is:

- close to or over \$1.0 billion or
- more than 50 per cent for any item with a value over \$200.0 million.<sup>529</sup>

The Department of Treasury and Finance supported the recommendation.<sup>530</sup> The current Committee reiterates that recommendation. The Committee considers that the consistent implementation of this recommendation would enable the Parliament and the community to better understand the budget estimates over the forward estimates period.

<sup>523</sup> Department of Treasury and Finance, *Budget Paper No.5: 2014-15 Statement of Finances* (2015), p.10.

<sup>524</sup> Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), p.40; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.30.

<sup>525</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.2.

<sup>526</sup> Department of Treasury and Finance, *2014-15 Victorian Budget Update* (2014), p.63.

<sup>527</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.36.

<sup>528</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.3.

<sup>529</sup> Public Accounts and Estimates Committee, *Report on the 2013-14 Budget Estimates – Part Two* (2013), Recommendation 2, p.3.

<sup>530</sup> Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 116<sup>th</sup> Report to Parliament – Report on the 2013-14 Budget Estimates – Part Two*, tabled 16 April 2014, p.2.

In past budget papers, the Government identified the major projects funded by asset investment through other sectors.<sup>531</sup> The Committee notes that this information does not appear in the 2015-16 budget papers. The Committee understands that this may be due to commercial sensitivity related to the proposed lease of the Port of Melbourne's operations from 2015-16. However, the Committee considers that this information is important for understanding the Government's planned asset investment delivery. Without this information, there are no details in the budget papers of what projects are funded through this source. The Committee therefore considers that this information should be reinstated from the 2016-17 budget papers.

**FINDING 75:** Investment through other sectors ('net cash flows from investments in financial assets for policy purposes') is expected to decrease over the next four years in comparison to the investment made from 2007-08 to 2014-15. In two years of the forward estimates period, cash inflows are expected to exceed cash flowing out. In 2015-16, this is due to the proposed lease of the Port of Melbourne's operations. The budget papers do not explain the expected cash inflow of \$1.1 billion in 2017-18.

**RECOMMENDATION 50:** Future budget papers provide a detailed explanation for variances to any item of the budget estimates where the variance from one year to the next or from previous estimates is:

- (a) close to or over \$1.0 billion or
- (b) more than 50 per cent for any item with a value over \$200.0 million.

**FINDING 76:** In contrast to earlier budget papers, this year's budget papers do not provide details of the projects being funded through this method. The budget papers do not distinguish between cash outflows and inflows for this line item, making it difficult to understand what the Government is providing to other sectors in some years.

**RECOMMENDATION 51:** Future budget papers re-instate the practice of disclosing the major projects funded by the general government sector through 'net cash flows from investments in financial assets for policy purposes', as was undertaken in past budgets.

**RECOMMENDATION 52:** Future budget papers disaggregate 'net cash flows from investments in financial assets for policy purposes' to specify cash outflows and cash inflows, as was undertaken in the *2013-14 Financial Report*.

### Public private partnerships

Public private partnerships (PPPs) are projects delivered by the private sector on behalf of the Government. Generally, the private sector finances, builds, operates and maintains an asset for the Government for a fixed period of time. The Government makes payments over that period of time or allows the private

531 Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), p.16.

sector to operate the asset and collect revenue. At the conclusion of that period, the ownership of the asset is usually transferred to the Government. The 2015-16 budget papers explain that:<sup>532</sup>

The Government uses PPPs to contract with the private sector to provide infrastructure and related services. Private finance does not represent an additional funding source. The majority of PPP projects are government funded through availability payments, financed by the private sector and recognised as a finance lease in the government's accounts.

The Government has also stated that it 'will continue to procure infrastructure and services through public private partnerships (PPPs) where such partnerships achieve value for money for Victorian taxpayers'.<sup>533</sup>

According to the budget papers, there are currently a total of 25 PPP projects, which includes 18 in operation, five under construction (*Bendigo Hospital, CityLink-Tulla Widening, Hopkins Correctional Centre, Ravenhall Prison and Victorian Comprehensive Cancer Centre*) and two in the procurement stage (*New Schools PPP Project and High-Capacity Metro Trains*).<sup>534</sup> Additionally, the budget papers indicate that the Government 'is actively exploring other opportunities to partner with the private sector for the delivery of government services'.<sup>535</sup>

When a PPP project starts operating, the full value of payments across the life of the project is added to the relevant sector's borrowings, though reduced to the present value.<sup>536</sup>

### Private sector expenditure on public private partnership projects

The budget papers provide estimates for the expenditure by the private sector on the construction of PPP projects for the Government. This is referred to as 'PPP infrastructure investment'. Table 8.4 provides the estimates for 'PPP infrastructure investment and other' expenditure ('other' refers to other commercially sensitive items) over the next four years as well as actual expenditure from 2011-12 to 2013-14 and the revised figure for 2014-15.

The figure for 2015-16 mostly relates to the proposed lease of operations of the Port of Melbourne, as the proceeds have been included in this figure.

<sup>532</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.8.

<sup>533</sup> *ibid.*

<sup>534</sup> *ibid.*

<sup>535</sup> *ibid.*

<sup>536</sup> An estimate of how much money would need to be held today to make all of the payments in the future, factoring in interest that would accrue to that money over the term of the lease.

**Table 8.4** PPP infrastructure investment and other<sup>(a)</sup>, 2011-12 to 2018-19

	2011-12 actual	2012-13 actual	2013-14 actual	2014-15 revised	2015-16 estimate	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
PPP infrastructure investment and other	496.1	238.7	334.0	-213.1 <sup>(b)</sup>	7,472.0 <sup>(c)</sup>	765.6	421.6	142.6

(a) Includes PPP infrastructure investment and other commercially sensitive items.

(b) The negative figure reflects the discontinuation of the *East West Link* and *Cranbourne Pakenham Rail Corridor* projects and adjustments associated to the proposed lease of operations of the Port of Melbourne.

(c) Includes proceeds from the proposed lease of the Port of Melbourne's operations.

Sources: Department of Treasury and Finance, *Response to the Committee's 2014-15 Budget Estimates Questionnaire*, received 8 May 2014, p.21; Response to questions on notice from the Hon. Michael O'Brien MP, Treasurer, to Chair, Victorian Parliament Public Accounts and Estimates Committee, received 9 July 2013, p.4; Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.44.

The Government expects that the private sector will carry out \$1.3 billion of work on PPPs from 2016-17 to 2018-19. The anticipated decreasing amount of private sector expenditure on PPPs is a result of expectations that the construction of a number of projects will be completed over the next four years while only one PPP is categorised as an upcoming procurement.<sup>537</sup>

Table 8.5 compares 'PPP infrastructure investment and other' estimates provided at the time of the 2014-15 budget papers and the 2015-16 budget papers.

**Table 8.5** PPP infrastructure investment and other<sup>(a)</sup>, 2011-12 to 2018-19

	2014-15 revised	2015-16 estimate	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
2014-15 Budget	1,854	nfp <sup>(b)</sup>	968	808	n/a
2015-16 Budget	-213.1	7,472	766	422	143

(a) Includes PPP infrastructure investment and other commercially sensitive items.

(b) Not for publication.

Source: Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.44.

The Department of Treasury and Finance explained the reasons for the variance between the estimates:<sup>538</sup>

The 2014-15 reduction primarily reflects the Government's decision to not proceed with the *East West Link* and *Cranbourne-Pakenham Rail Corridor* projects and adjustments associated with the medium-term lease of the Port of Melbourne Corporation.

<sup>537</sup> The *Victorian Comprehensive Cancer Centre*, the *Bendigo Hospital* redevelopment (Stage 1 and 2), the *New Schools PPP* (Tranche 1 and 2) and the *Ravenhall Prison* are all expected to be completed during the forward estimates period. See Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.8; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>538</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.44.

The 2016-17 and 2017-18 reductions are mainly due to reduced finance leases associated with the *Cranbourne-Pakenham Rail Corridor* project.

The Committee acknowledges the relevance of this information and notes that explanations for the variances between the current budget estimates and previous budget estimates are not readily available for ‘PPP infrastructure investment and other’ in the budget papers each year. The Committee considers that noting changes to the estimates and the reasons for any variances compared to the last budget in future budget papers would provide a better understanding of what is driving the PPP expenditure estimates.

**FINDING 77:** Estimates of expenditure by the private sector on the construction of public private partnership projects in 2016-17 and 2017-18 have been revised downwards since the last budget. This is primarily a result of the Government’s decision to discontinue projects such as the *East West Link* and *Cranbourne-Pakenham Rail Corridor*. Explanations for changes in PPP infrastructure investment estimates are not provided in the budget papers each year, making it difficult for the Parliament and the community to understand changes to the estimates from one budget to the next.

**RECOMMENDATION 53:** Future budget papers include a reconciliation of ‘public private partnerships infrastructure investment and other’ estimates between the current and previous budgets, including explanations for any variances.

### Government payments for public private partnerships projects

As noted above, there are currently 18 PPP projects in operation. The Government currently makes payments each year to the private sector as part of these projects. Four additional PPP projects are expected to start operating (referred to as ‘commissioning’) during the forward estimates period: the *Victorian Comprehensive Cancer Centre* in 2015-16, the *Bendigo Hospital* redevelopment (Stage 1) and the *New Schools PPP Project* (Tranche 1) in 2016-17, and the *Bendigo Hospital* redevelopment (Stage 2), the *Ravenhall Prison* and the *New Schools PPP Project* (Tranche 2) in 2017-18.<sup>539</sup> As each project starts operating, the Government starts making payments.

The Committee sought details from departments about the amount of expenditure they are expecting to incur on commissioned PPP projects in the budget year and over the forward estimates period, as well as the revised figure for 2014-15.

Five departments provided quantified responses.<sup>540</sup> Table 8.6 provides the expected total impact on departments’ operating statements and Appendix A8.1 provides a break-down by department.

<sup>539</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>540</sup> The Department of Economic Development, Jobs, Transport and Resources, the Department of Environment, Land, Water and Planning, the Department of Health and Human Services, the Department of Justice and Regulation and Courts.

**Table 8.6** PPP payments made by departments<sup>(a)</sup>, 2014-15 to 2018-19

	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
PPP payments made by departments	377.3	458.0	464.9	457.9	519.7

(a) These figures only include payments registered as part of the departments' operating statements. In addition, the departments reported payments registered in the 'statement of cash flows' totalling \$1,456.5 million (five-year total) and in the 'administered items statement' totalling \$3,766.5 million.

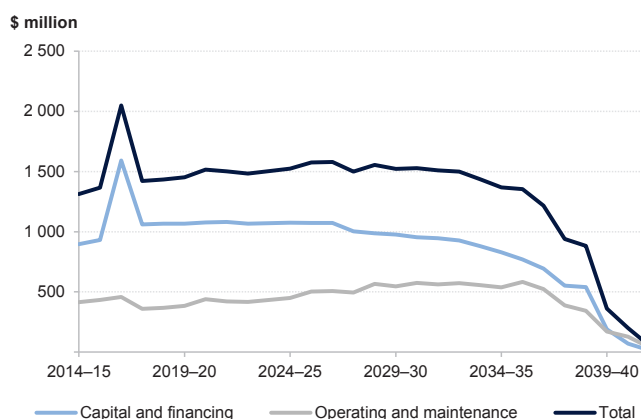
Sources: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.

The Department of Education and Training indicated that:<sup>541</sup>

The figures relating to the *Partnerships Victoria in Schools Project* and *New Schools PPP Project* cannot be disaggregated and disclosed, as this would reveal commercially sensitive information relating to the current tender process for the *New Schools PPP Project* for which proposals are due in June 2015.

Three departments indicated that they were not engaged in any commissioned PPP projects or that the question was not applicable to them.<sup>542</sup>

The Victorian Auditor-General's Office recently sought similar information. Figure 8.4 shows the total expected cost each year of payments for PPPs identified by the Victorian Auditor-General's Office (for the PPP projects that operated in Victoria at 30 June 2014). It shows larger figures than Table 8.6 as it includes all payments, including those not included in the operating statements. The estimated Government payments for PPP projects are approximately \$1.5 billion per year over the forward estimates period, except for 2016-17.

**Figure 8.4** Total annual payments for public private partnerships

Note: Nominal dollar amounts.

Source: Reproduced from Victorian Auditor-General, *Portfolio Departments and Associated Entities: Results of the 2013-14 Audits* (2015), p.77.

541 Department of Education and Training, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 16 June 2015, p.19.

542 The Department of Premier and Cabinet, the Parliamentary Departments and the Department of Treasury and Finance.



This information has not been disclosed before and is not currently published by the Government. The Committee considers that this information is particularly important for understanding the budget estimates, as the future payments are constraints that must be factored into the budget. Therefore, the Committee considers that this information should be disclosed in future budget papers.

**FINDING 78:** Payments to service PPP projects are an important constraint that must be factored into the budget estimates. Government payments for PPP projects are expected to total approximately \$1.5 billion per year across the forward estimates period, except for 2016-17. These amounts are not disclosed in the budget papers each year.

**RECOMMENDATION 54:** Future budget papers disclose details of the expected Government payments on public partnerships projects over the forward estimates period and beyond, as reported by the Victorian Auditor-General's Office.

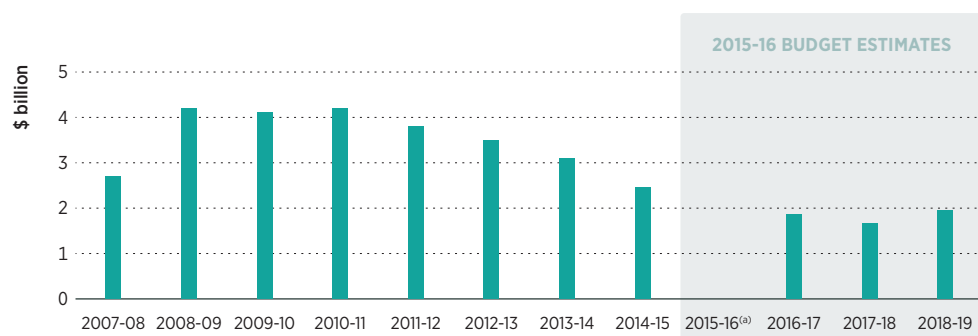
### 8.3.2 Public non-financial corporations sector direct investment

The budget papers note that the public non-financial corporations (PNFC) sector 'largely funds its investment in new infrastructure through operating cash flows, borrowings, revenue from asset sales and State and Commonwealth Government funding and grants'.<sup>543</sup>

Direct asset investment for the PNFC sector in the 2015-16 budget papers appears as a net figure (that is, the budget papers only disclose direct investment less proceeds from asset sales) due to commercial sensitivity related to the proposed lease of the Port of Melbourne's operations.

Figure 8.5 shows the expected trend for net direct asset investment from 2007-08 to 2018-19.

**Figure 8.5** Net direct investment, public non-financial corporations sector, 2007-08 to 2018-19



(a) The 2015-16 figure for the PNFC sector has not been included as this primarily reflects revenue from the proposed lease of the Port of Melbourne rather than asset investment.

Sources: Department of Treasury and Finance, *Financial Report*, 2008-09 to 2013-14; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.52.

543 Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.13.

The budget papers anticipate that net direct investment for the PNFC sector will be \$2.5 billion in 2014-15 and then decrease to \$1.9 billion in 2016-17 and \$1.7 billion in 2017-18 before increasing to \$2.0 billion in the last year of the forward estimates period.<sup>544</sup> The estimate for 2015-16 has not been included in Figure 8.5 as it primarily reflects proceeds from the proposed lease of the Port of Melbourne's operations.

As with the general government sector, the budget papers each year do not provide any explanation for variations from one year to the next of the forward estimates period. The Committee considers that providing this explanation would allow the Parliament and the community to better understand what is planned for investment within the PNFC sector.

**FINDING 79:** Net direct investment for the public non-financial corporations sector is expected to be \$2.5 billion in 2014-15, with lower amounts across the forward estimates period. As with the general government sector, the budget papers each year do not provide explanations for variations in this line item across the forward estimates period for the public non-financial corporations sector.

**RECOMMENDATION 55:** Future budget papers explain variations between individual years of the forward estimates period for direct investment ('purchases of non-financial assets') by the public non-financial corporations sector.

### 8.3.3 Asset investment indicators

The Committee examined two indicators to understand the level of asset investment in Victoria:

- direct investment compared to depreciation, which compares the expenditure on assets to an estimate of the amount of money that would be required to maintain the same level of assets
- the level of government infrastructure investment per Victorian in real terms (that is, adjusted for inflation and changes in population).

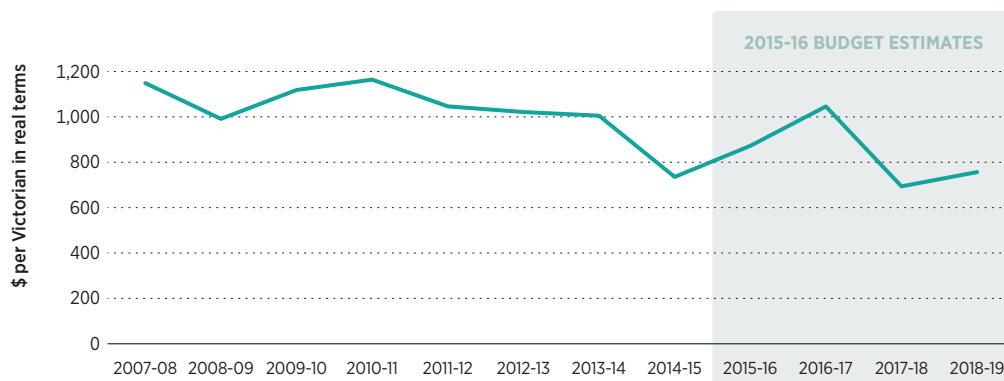
The first of those indicators is discussed in Section 2.4.3 of this report. It shows that the level of asset investment is expected to remain greater than depreciation across the forward estimates period for the general government sector.

#### Government infrastructure investment per Victorian in real terms

Figure 8.6 shows the expected trend for government infrastructure investment per Victorian in real terms between 2007-08 and 2018-19.

<sup>544</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.52.

**Figure 8.6** Government infrastructure investment per Victorian in real terms,<sup>(a)</sup> 2007-08 to 2018-19



(a) Expressed in 2015-16 prices.

Source: Committee calculations based on Department of Treasury and Finance, *Net Infrastructure Investment* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Other-financial-aggregates)>, viewed 4 June 2015; Department of Treasury and Finance, *Macroeconomic Indicators* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators)>, viewed 4 June 2015.

The Committee notes that the amount of money spent on infrastructure per Victorian is expected to increase in real terms from \$721 in 2014-15 to \$858 in 2015-16. Expenditure is then expected to rise to \$1,031 in 2016-17 before decreasing to \$679 in 2017-18 and increasing again to \$742 in 2018-19. This follows a longer-term trend of decline since 2008.

Government infrastructure investment per Victorian in real terms is lower in most years of the forward estimates period than it was in 2013-14 and earlier. This is a result of the reduction in the total government infrastructure investment (see Section 8.3) combined with inflation and population growth.

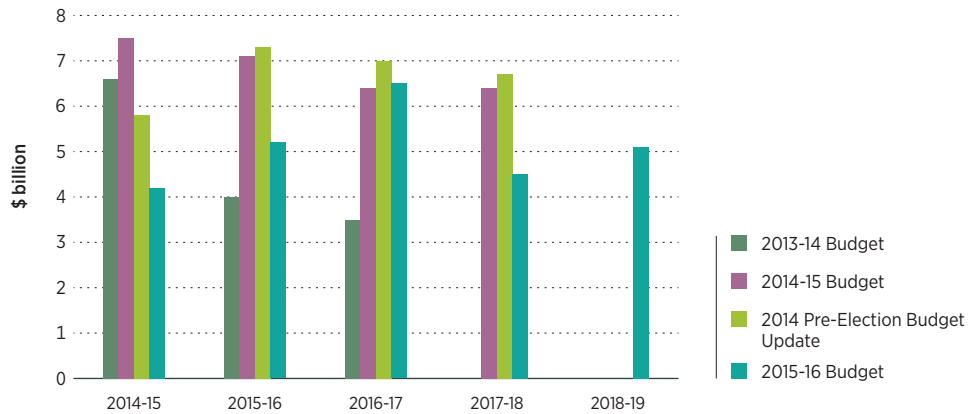
**FINDING 80:** Government infrastructure investment adjusted for inflation and population growth is expected to decrease from \$858 per Victorian in 2015-16 to \$742 in 2018-19, though with a spike at \$1,031 in 2016-17.

## 8.4 Comparison to previous estimates

Figure 8.7 below compares government infrastructure investment estimates from the 2013-14 Budget, 2014-15 Budget, the 2014 Pre-Election Budget Update and the 2015-16 Budget.

Government infrastructure investment forecasts have generally been revised downwards in the 2015-16 Budget compared to the past two budgets. For 2015-16, the 2014-15 Budget anticipated that government infrastructure investment would be \$7.1 billion. This was revised to \$7.3 billion at the time of the Pre-Election Budget Update and down to \$5.2 billion in the 2015-16 Budget.

**Figure 8.7** Government infrastructure investment, comparison with previous estimates, 2014-15 to 2018-19



Note: Estimates from the 2012-13 Budget and earlier are not included as the methodology used to calculate government infrastructure investment was different.

Sources: Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2013-14 to 2015-16; Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.10.

In relation to 2014-15, the Pre-Election Budget Update indicated that:<sup>545</sup>

Compared with the 2014-15 Budget, government infrastructure investment has been revised down by around \$1.7 billion in 2014-15. This reflects cash receipts from the sale of the Rural Finance Corporation (which is netted off against infrastructure investment) being received in 2014-15 rather than 2013-14 and revised cash flow estimates for various road and rail projects.

The Department of Treasury and Finance explained that much of the change to the 2014-15 estimate following the Pre-Election Budget Update related to the decision not to proceed with the *East West Link* and the *Cranbourne-Pakenham Rail Corridor* PPPs, along with adjustments associated with the proposed lease of the Port of Melbourne’s operations.<sup>546</sup>

**FINDING 81:** Government infrastructure investment figures have been revised downwards since the 2014-15 Budget for most years of the forward estimates period. According to the Department of Treasury and Finance, this is primarily driven by changes to major projects such as the cancellation of the *East West Link* and the *Cranbourne-Pakenham Rail Corridor* projects, and adjustments made to the proposed lease of the Port of Melbourne’s operations.

<sup>545</sup> Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.10.

<sup>546</sup> Department of Treasury and Finance, *Response to the Committee’s 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.44.

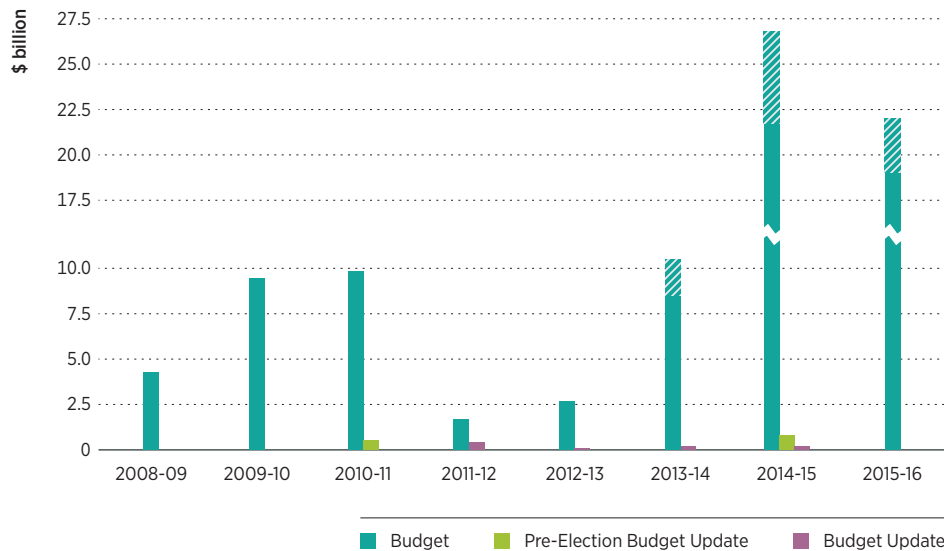
## 8.5 New initiatives

### 8.5.1 Total estimated investment of new asset investment projects

The total estimated investment (TEI) of an asset project is the total cost of delivering or acquiring it. This often includes expenditure across multiple years, including years beyond the forward estimates period.

Figure 8.8 compares the TEI of new asset initiatives released in the 2015-16 Budget to the TEI of initiatives in previous budgets. This includes expenditure for all components of asset investment (that is, direct investment, investment through other sectors and PPPs).<sup>547</sup>

**Figure 8.8** New asset investment initiatives, current and previous budgets (total estimated investment), 2007-08 to 2015-16



Note: Where values have been expressed as a range in the budget papers, the range has been indicated by hatched areas.

Sources: Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2007-08 to 2015-16; Department of Treasury and Finance, *Victorian Budget Update*, 2011-12 to 2014-15; Department of Treasury and Finance, *Victorian Pre-Election Budget Update*, 2010 and 2014.

The Committee notes that the value of new asset initiatives was significantly higher in the 2013-14, 2014-15 and 2015-16 budgets compared to earlier budgets. This is explained by the inclusion of a number of very large projects in these budgets.

The 2013-14 Budget figure includes funding for the *East West Link – Stage 1* (\$6.0-8.0 billion). The 2014-15 Budget figure includes the *Melbourne Rail Link* (\$8.5-11.0 billion) and the *East West Link – Western Section* (\$8.0-10.0 billion). The Committee notes that these three asset initiatives have been discontinued in the 2015-16 Budget (see Section 8.7 of this report).

<sup>547</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.60.

In 2015-16, the value of asset initiatives is primarily driven by the *Melbourne Metro Rail Project* and (\$9.0-11.0 billion) and *the Level Crossing Removal Program* (\$5.0-6.0 billion). These and other major new initiatives are discussed further in Section 8.5.3.

Some funding related to asset investment has also been released as part of output initiatives. For example, the \$500.0 million *Regional Jobs and Infrastructure Fund* is an initiative established to ‘support regional development in Victoria’.<sup>548</sup> It includes funding for asset investment such as the *Ballarat Station Redevelopment*, the *Eureka Stadium* and other Ballarat sporting infrastructure as well as the *Ararat Arts Precinct Development*.<sup>549</sup>

**FINDING 82:** The value of new asset initiatives released in each budget has been significantly higher in the last three budgets than in earlier budgets. This has been primarily a result of several particularly large projects. However, the largest projects released in the 2013-14 and 2014-15 budgets were discontinued with the 2015-16 Budget.

## 8.5.2 Projects with details still to be confirmed

For four new asset initiatives, the 2015-16 budget papers do not provide the same level of detail about the expected expenditure as is provided for other initiatives. In two cases, both the TEIs and the expected expenditure in each year of the forward estimates period are marked as ‘tbc’ (that is, ‘to be confirmed’):<sup>550</sup>

- *Melbourne Exhibition Centre – Stage 2 Development*
- *Maintaining Ocean Access for Gippsland Lakes.*

For two projects, the TEI has been provided and the expected expenditure in some years has been detailed, but the expenditure in other years has been listed as ‘tbc’:<sup>551</sup>

- *Level Crossing Removal Program*
- *Casey Hospital expansion.*

The budget papers indicate in two cases that details are not available until further planning is done. In one case, details have not been provided ‘due to commercial sensitivities’.<sup>552</sup> The Committee accepts that these are valid reasons. However, no explanation as to why details have not been disclosed for the *Melbourne Exhibition Centre – Stage 2 Development* project is provided. The Committee considers that explanations should be provided in future cases.

<sup>548</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.26.

<sup>549</sup> *ibid.*

<sup>550</sup> *ibid.*, p.36.

<sup>551</sup> *ibid.*, pp.36, 76.

<sup>552</sup> *ibid.*, p.37.

The Committee notes that projects with expected expenditure marked as ‘tbc’ have appeared in previous budgets. In the 2014-15 budget papers, for example, there was one project where the expected expenditure for some years was marked as ‘tbc’ and in the 2013-14 budget papers there were five projects for which some or all details were ‘tbc’ (including the TEI in four cases).<sup>553</sup>

The TEI of asset investment projects is noted each year in Budget Paper No.4. The TEI of these new initiatives may therefore be revealed in future budget papers. However, Budget Paper No.3 of the year in which the initiative is released is the only place where anticipated expenditure patterns across multiple years are revealed. The Committee notes that some of the projects are substantial, especially the *Level Crossing Removal Program*, which has a TEI of \$5.0-6.0 billion, of which only \$3.0 million has been allocated to particular years.<sup>554</sup>

The Committee therefore considers that, when ‘tbc’ is initially provided for the anticipated expenditure in some years of the forward estimates period, the details should be supplied when possible in future budget papers.

**FINDING 83:** Four new asset initiatives released in the 2015-16 Budget do not include full details of their total estimated investment or their expected expenditure in some years of the forward estimates period. In one case, no explanation is provided.

**RECOMMENDATION 56:** Future budget papers include explanations for all asset investment projects for which any details of the anticipated expenditure (including the total estimated investment) are marked ‘tbc’.

**RECOMMENDATION 57:** At the earliest opportunity, future budget papers provide details of the anticipated expenditure over the forward estimates period for any asset initiative from a previous budget where the anticipated expenditure in some future years was listed as ‘tbc’.

### 8.5.3 Main initiatives

Table 8.7 below identifies the ten largest initiatives (based on TEI) released in the 2015-16 budget papers. The Committee notes that these ten initiatives account for 90.8 per cent of the total value of new asset initiatives released in the 2015-16 Budget. Most of these initiatives relate to transport infrastructure.

The 2015-16 Budget also provides funding of \$40 million<sup>555</sup> (\$1.6 million released as an output initiative<sup>556</sup> and \$38.5 released as an asset initiative<sup>557</sup>) for the first stage of the *West Gate Distributor*, the Government’s alternative to the *East West Link* project proposed by the former government. This stage

553 Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.64; Department of Treasury and Finance, *Budget Paper No.3: 2013-14 Service Delivery* (2013), pp.21, 52

554 Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.36

555 Department of Treasury and Finance, *Budget Information Paper: Getting on With It* (2015), p.11.

556 Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.21.

557 *ibid.*, p.37.

includes ‘the widening of Whitehall Street to provide an upgraded connection to Footscray Road, and the strengthening and widening of Shepherd Bridge over the Maribyrnong River’.<sup>558</sup> This is expected to be the first stage of a much larger project.

**Table 8.7** Main new asset initiatives, 2015-16 Budget

Asset initiative	Total estimated investment (\$ million)
<i>Melbourne Metro Rail Project</i>	9,000.0-11,000.0
<i>Level Crossing Removal Program</i>	5,000.0-6,000.0
<i>High-Capacity Metro Trains</i>	1,301.0
<i>Conventional Signalling Upgrade – Caulfield to Dandenong</i>	360.0
<i>School Modernisations</i>	324.6
<i>New E-Class Trams</i>	294.8
<i>New VLocity Carriages for the Regional Network</i>	257.1
<i>Western Women's and Children's Hospital</i>	200.0
<i>M80 Upgrade – EJ Whitten Bridge to Sunshine Avenue</i>	150.0
<i>Delivering New Schools</i>	111.1

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

### Melbourne Metro Rail Project

The *Melbourne Metro Rail Project* consists of a new rail tunnel with five train stations linking the Sunbury line and the Cranbourne-Pakenham line via the Melbourne CBD.<sup>559</sup> The construction of the project is expected to commence in 2018<sup>560</sup> and be completed in 2026.<sup>561</sup>

The budget papers indicate that:<sup>562</sup>

Melbourne Metro will increase public transport passenger capacity and reliability across the network, improve access to employment, education and other opportunities, and support urban development.

<sup>558</sup> *ibid.*, p.45.

<sup>559</sup> *ibid.*, p.42.

<sup>560</sup> *ibid.*, p.3.

<sup>561</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.98.

<sup>562</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.42.



According to the Minister for Public Transport:<sup>563</sup>

[the *Melbourne Metro Rail Project* is] at the centre of our transport infrastructure agenda... because it is the project that will unlock the capacity of the system in the centre of Melbourne to enable additional services to be run from the suburbs of Melbourne and from regional Victoria as well.

The Government anticipates that this project will cost between \$9.0 and \$11.0 billion. This includes funding of \$1.5 billion over the next four years for planning, design and construction.<sup>564</sup> Funding for the remaining years will be detailed in future budget papers.

At the budget estimates hearings, the Treasurer indicated that the funding sources for this project were still to be determined. He stated that:<sup>565</sup>

... it will principally be funded out of federal and state allocations. Now, the federal government, in its current complexion and with its current predilection, does not believe it has an obligation in respect of funding these arrangements. It would be unfortunate if the state of Victoria ultimately has to carry the load on its own ... but nonetheless, if we have to, we will.

The Treasurer also noted an intention to 'engage the community about how it will be funded and financed.'<sup>566</sup>

This project replaces the previous government's *Melbourne Rail Link*, which was discontinued following the change of government.<sup>567</sup> Both projects consisted of rail tunnels designed to increase the capacity of the rail network. The previous project also incorporated the construction of the *Airport Rail Link* connecting Southern Cross Station and Melbourne Airport.<sup>568</sup> This is not part of the *Melbourne Metro Rail Project*.

### Level Crossing Removal Program

The 2015-16 Budget provides funding of between \$5.0 and \$6.0 billion for the removal of 50 level crossings over eight years that 'will reduce road congestion, train delays and improve safety'.<sup>569</sup>

According to the budget papers, the expected benefits of this project are that it:<sup>570</sup>

- Reduces congestion. Level crossings make up almost half of the RACV's traffic hotspots in Melbourne. Boom gates can stay down for up to 80 minutes over the morning peak.

<sup>563</sup> Hon. Jacinta Allan MP, Minister for Public Transport, *2015-16 Budget Estimates Transcript of Evidence*, 15 May 2015, p.3.

<sup>564</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.1; Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.36.

<sup>565</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.9.

<sup>566</sup> *ibid.*

<sup>567</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.101.

<sup>568</sup> Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.2.

<sup>569</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.1.

<sup>570</sup> Department of Treasury and Finance, *Budget Overview* (2015), p.16.

- Means more trains can run on every line. At present, the addition of services on major train lines would cause traffic chaos on surrounding streets.
- Helps reduce the road toll. There were over 240 crashes at level crossings over the decade to 2013. That's not good enough in the road safety capital.

Procurement and construction for this project are expected to commence in 2015-16<sup>571</sup> and the program is expected to be completed by the end of 2022.<sup>572</sup> The Minister for Public Transport informed the Committee that 20 level crossings are expected to be removed by 2018, including 17 which have already been identified and announced.<sup>573</sup>

A total of \$3.0 million was expected to be spent by 30 June 2015. At the time of the Budget, the remaining expenditure had not yet been allocated over the next few years.<sup>574</sup> The budget papers indicate that 'funding will be released progressively as planning for packages of work is completed and projects released to market for tender'<sup>575</sup> (see further discussion in Section 8.5.2 of this chapter).

Funding for this project includes previous funding related to the *Metro Level Crossing Blitz*, an asset initiative released in the 2013-14 Budget.

### High-Capacity Metro Trains

The 2015-16 Budget has allocated \$1.3 billion to acquire 37 high-capacity metro trains for deployment on the Cranbourne-Pakenham corridor and an associated infrastructure upgrade.<sup>576</sup>

This initiative also funds the construction of a new maintenance depot.<sup>577</sup> Both the procurement of the new trains and the construction of the new maintenance depot will be delivered through PPPs.<sup>578</sup>

According to the budget papers, 'This will upgrade and transform Melbourne's busiest train line, and free up existing trains to meet demand on other lines'.<sup>579</sup>

This project is estimated to cost \$21.9 million in 2015-16, with a total of \$247.9 million to be spent between 2016-17 and 2018-19. The remaining \$1,031.2 million is expected to be spent beyond the forward estimates period.<sup>580</sup>

571 Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.2.

572 *ibid.*

573 Hon. Jacinta Allan MP, Minister for Public Transport, *2015-16 Budget Estimates Transcript of Evidence*, 15 May 2015, pp.4, 16.

574 Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.17.

575 *ibid.*, p.18.

576 Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.3.

577 *ibid.*

578 Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.8.

579 Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.3.

580 *ibid.*, p.36.

The project replaces the high-capacity trains element of the former Government's *Cranbourne-Pakenham Rail Corridor* project, which included 25 high-capacity trains<sup>581</sup> (see Section 8.7 of this chapter for further discussion of the former project).

**FINDING 84:** Three transport-related projects make up the bulk of the new asset initiatives released in the 2015-16 Budget: the *Melbourne Metro Rail Project*, the *Level Crossing Removal Program* and *High-Capacity Metro Trains*. These three projects have a total estimated investment of between \$15.3 and \$18.3 billion. Each project replaces a similar project of the previous government.

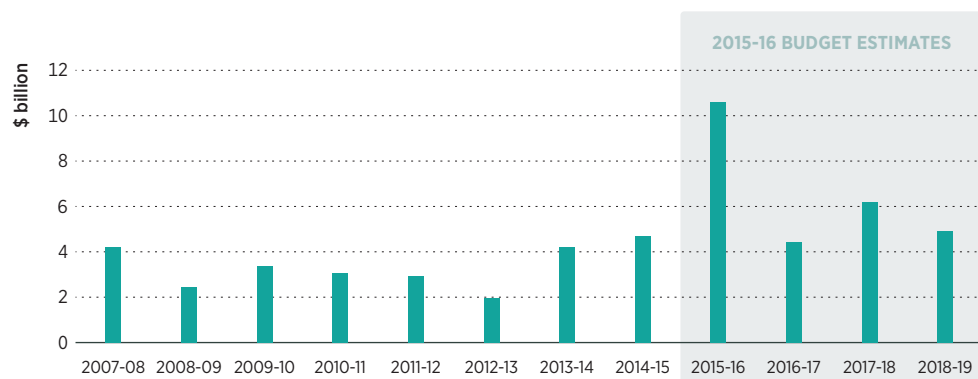
## 8.6 Sources of funding

As discussed in Section 2.2.1 of this report, the Government funds its asset investment from five main sources:

- the operating surplus (which includes Commonwealth grants)
- depreciation and similar
- asset sales
- inflows from investment through other sectors
- borrowings.

Figure 8.9 shows the expected amounts of cash resources, excluding borrowings, available for annual asset investment from 2007-08 to 2018-19.

**Figure 8.9** Total cash resources available for asset investment, 2007-08 to 2018-19



Sources: Committee calculations based on Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement – General Government Sector (2015)*. <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 4 June 2015; Department of Treasury and Finance, *Consolidated Cash Flow Statement – General Government Sector (2015)*. Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 4 June 2015.

581 Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.67.

Cash resources available for asset investment are expected to be substantially higher over the forward estimates period than in recent years. The average annual amount of cash resources from 2015-16 to 2017-18 is expected to be \$6.5 billion, primarily driven by larger operating surpluses in each of the next four years (see Section 2.4.1 of this report) and larger amounts of money received from investment through other sectors in 2015-16 and 2017-18.

The higher levels of cash resources are expected to reduce the amount of new borrowings required over the forward estimates period compared to recent years (see Section 6.3.1 of this report).

A key source of cash in the 2015-16 Budget is cash inflows from investments through other sectors (included in the budget papers line item 'net cash flows from investment in financial assets for policy purposes'). See further discussion of this item in Section 8.3.1 of this report. The budget estimates include two years (2015-16 and 2017-18) in which large cash inflows from this source will significantly increase the level of cash resources.

The Government expects a cash inflow to the general government sector of \$6.5 billion in 2015-16, primarily from the proposed lease of the Port of Melbourne's operations.<sup>582</sup> The 2015-16 budget papers indicate that proceeds from the proposed lease:<sup>583</sup>

... will be used to fund investment in new transport-related capital projects through the establishment of the Victorian Transport Building Fund.

The fund<sup>584</sup> is expected to provide funding for the Government's main asset initiatives such as the *Melbourne Metro Rail Project*, the removal of 50 level crossings and the *West Gate Distributor*.<sup>585</sup>

In May 2015, the proposed lease period for the operations of the Port of Melbourne was 50 years, with an option for the Government of the day to extend the lease by up to an additional 20 years.<sup>586</sup> In relation to the proposed lease arrangement, the Government has explained that:<sup>587</sup>

Only the port's commercial operations will be leased. The Victorian and Commonwealth Governments will retain responsibility for regulating the port's safety, security and environmental functions.

The leaseholder will be responsible for maintaining and improving the port's operations, delivering efficiencies, boosting competitiveness and ensuring future port development is not compromised.

<sup>582</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.59.

<sup>583</sup> *ibid.*, p.11.

<sup>584</sup> Referred to in the Delivering Victorian Infrastructure (Port of Melbourne Lease Transaction) Bill 2015 as the 'Victorian Transport Fund'.

<sup>585</sup> Hon. Daniel Andrews MP, Premier, *Lease The Port, Remove The Crossings, Create 5000 New Jobs* (Media release, 27 May 2015).

<sup>586</sup> Delivering Victorian Infrastructure (Port of Melbourne Lease Transaction) Bill 2015, s.11.

<sup>587</sup> Hon. Daniel Andrews MP, Premier, *Lease The Port, Remove The Crossings, Create 5000 New Jobs* (Media release, 27 May 2015).

As noted in Section 8.3.1 of this report, the Government is also expecting a \$1.1 billion cash inflow from the public financial corporations sector in 2017-18, which will add to the cash available for asset investment in that year.

An additional factor increasing the amount available for asset investment is the funding carried over from the previous financial year. The Committee sought further details from departments in relation to the amount of money that they expected to carry over from 2014-15. The total amount reported by the departments is \$189.0 million.<sup>588</sup> A departmental break-down for this figure can be found in Appendix A8.2.

**FINDING 85:** The 2015-16 Budget estimates include increased cash resources available to fund its asset investment without borrowings over the next four years. The increase is primarily a result of larger operating surpluses over the forward estimates period and cash inflows from investment through other sectors (as a result of the proposed lease of operations of the Port of Melbourne and expected receipts from the public financial corporations sector).

## 8.7 Discontinued projects

Following the change of government in 2014, six projects were discontinued:<sup>589</sup>

- *East West Link – Western Section*
- *East West Link – Eastern Section*
- *Cranbourne-Pakenham Rail Corridor*
- *Port of Hastings Development*
- *Melbourne Rail Link*
- *VicRoads Registration and Licensing System.*

### East West Link (western and eastern sections)

The *East West Link – Stage 1* (eastern section) was a new asset initiative released in the 2013-14 Budget. The project aimed to provide a road link, mostly as a tunnel, between the end of the Eastern Freeway in Clifton Hill and the CityLink at Parkville.<sup>590</sup> The total TEI for this project was estimated at \$6.0-8.0 billion<sup>591</sup> and it was expected to be delivered as a PPP.<sup>592</sup>

<sup>588</sup> Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.

<sup>589</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), pp.23, 89, 101.

<sup>590</sup> Department of Treasury and Finance, *Budget Paper No.3: 2013-14 Service Delivery* (2013), p.55; Department of Treasury and Finance, *Budget Information Paper No.2: 2013-14 Infrastructure Investment* (2013), p.10.

<sup>591</sup> Department of Treasury and Finance, *Budget Paper No.3: 2013-14 Service Delivery* (2013), p.52.

<sup>592</sup> Department of Treasury and Finance, *Budget Paper No.4: 2013-14 State Capital Program* (2013), p.7; Department of Treasury and Finance, *Budget Information Paper No.2: 2013-14 Infrastructure Investment* (2013), p.10.

The *East West Link – Stage 2* (western section) was released in the 2014-15 Budget. The project was expected to commence in late 2015 with a TEI of \$8.0-10.0 billion,<sup>593</sup> which included \$1.5 billion of funding from the Commonwealth.<sup>594</sup>

The 2015-16 budget papers indicate that:<sup>595</sup>

On 15 April 2015, the Government announced that it had negotiated an agreement with the East West Link consortium. Under the agreement, the State will purchase the companies in the consortium (EWL Project Co) for one dollar. All assets owned by EWL Project Co will transfer to the State.

Net costs of \$339 million had already been drawn down and paid to the consortium for the bid process, design and pre-construction. These costs have already been incurred and cannot be retrieved. They will be retained by the consortium subject to a certification process between it and the State.

A further \$81 million of fees were incurred to establish the EWL Project Co credit facility of \$3 billion. The State intends to negotiate with the banks to take over that facility to contribute to funding for the Melbourne Metro Rail Project and will receive value for those fees. All rates, fees, swaps and obligations related to the credit facility will now be worked through between the financiers and the State.

....

The majority of these [already incurred] costs relate to land and property acquisitions, which the Government has already announced will now be sold, with the proceeds to offset these costs.

The remaining costs relate to planning, procurement and the former Government reimbursing costs incurred by the unsuccessful bidders.

The new *West Gate Distributor* project has been commenced as an alternative (see Section 8.5.3).

### **Cranbourne-Pakenham Rail Corridor**

This project was included as a new asset initiative in the 2014-15 Budget. It was intended to improve rail connections through the south-east corridor.<sup>596</sup> The TEI for this project was expected to be between \$2.0 and \$2.5 billion<sup>597</sup> and the construction was expected to begin in 2015.<sup>598</sup>

The 2015-16 budget papers indicate that this project ‘has ceased and been replaced by the *Conventional Signalling Upgrade – Caulfield to Dandenong*, *Level Crossing Removal Program*, and *High-Capacity Metro Trains* projects’.<sup>599</sup>

<sup>593</sup> Department of Treasury and Finance, *Budget Information Paper: Infrastructure Investment* (2014), p.12; Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.64.

<sup>594</sup> Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), pp.48-9.

<sup>595</sup> Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.47.

<sup>596</sup> Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.67.

<sup>597</sup> Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), p.48.

<sup>598</sup> Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.67.

<sup>599</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.23.

## Port of Hastings Development

The *Port of Hastings Development* project was released in the 2013-14 Budget with initial funding of \$110.0 million (four-year total) for planning for a new container port at Hastings.<sup>600</sup> The project aimed to increase the container capacity to meet the State's needs after the Port of Melbourne reaches its capacity.<sup>601</sup> The current government has indicated that the Port of Hastings may still be developed in the future, stating that, 'Infrastructure Victoria will provide independent advice to Government on the most appropriate site for a second container port, including assessing locations at Hastings and Bay West'.<sup>602</sup>

## Melbourne Rail Link

As seen in Section 8.5.3, this project planned the construction of an underground tunnel between Southern Cross and South Yarra stations, two new stations, and a rail link to Tullamarine Airport with a total TEI of between \$8.5 and \$11.0 billion.<sup>603</sup> Packages within the project were expected to be delivered as a PPP project.<sup>604</sup> The new *Melbourne Metro Rail Project* has been released in this budget as an alternative (see Section 8.5.3)

## VicRoads Registration and Licensing System.

This project was a new asset initiative released in the 2011-12 Budget Update with a TEI of \$121.6 million (three-year total, from 2011-12 to 2013-14), with no reported expected completion date. The aim of this system was to 'substantially improve upon the capability, reliability and efficiency of the existing system... [and to] provide greater flexibility to update the system in response to regulatory or policy changes'.<sup>605</sup>

In the 2014-15 Budget, the project appeared with a remaining expenditure of \$46.1 million with expected completion date 'tbc' (that is, 'to be confirmed') as the project had been paused 'to reassess customer expectations of future services needs and how they impact on systems requirements'.<sup>606</sup> The 2015-16 budget papers note that the project has now been discontinued.<sup>607</sup> No further details are supplied.

**FINDING 86:** Six asset projects were discontinued prior to the 2015-16 Budget. In some cases, alternative projects have been funded in the 2015-16 Budget.

<sup>600</sup> Department of Treasury and Finance, *Budget Paper No.3: 2013-14 Service Delivery* (2013), pp.52, 57.

<sup>601</sup> Hon. David Hodgett MP, Minister for Ports, *2013-14 Budget Estimates Transcript of Evidence*, 14 May 2013, p.7.

<sup>602</sup> Department of Treasury and Finance, *Frequently Asked Questions*. Available at <[www.dtf.vic.gov.au/Infrastructure-Delivery/Leasing-the-Port-of-Melbourne/Frequently-asked-questions](http://www.dtf.vic.gov.au/Infrastructure-Delivery/Leasing-the-Port-of-Melbourne/Frequently-asked-questions)>, viewed 8 October 2015.

<sup>603</sup> Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), p.115.

<sup>604</sup> *ibid.*, p.11.

<sup>605</sup> Department of Treasury and Finance, *2011-12 Victorian Budget Update* (2011), p.119.

<sup>606</sup> Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), pp.51-2.

<sup>607</sup> Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.23.





# 9

## The Government's election commitments

### 9.1 Introduction

Prior to the November 2014 election, the Labor Party set out a series of election commitments in *Labor's Financial Statement 2014* (LFS). The intentions of these commitments included 'creating jobs, supporting skills, investing in industries and maintaining a steady pipeline of projects'.<sup>608</sup> Since the 2014 election, the new government has presented the 2014-15 Budget Update and the 2015-16 Budget, both of which have included output, expenditure reduction and asset initiatives related to the election commitments.

The LFS indicated the financial impact expected between 2014-15 and 2018-19 as a result of the election commitments. The LFS included 100 output commitments, with expenses totalling \$3.4 billion<sup>609</sup> over the five years.<sup>610</sup> It also included commitments to 61 asset investment projects with a total estimated investment (TEI) of \$6.2-6.8 billion.<sup>611</sup> The Committee notes that some of these commitments will incur additional costs beyond the forward estimates period, as further components of some projects are expected to be funded later. These additional costs are not included in the LFS.

The aim of this Chapter is to assess:

- To what extent have the output and expenditure reduction commitments in the LFS been funded? (Section 9.2)
- To what extent have the asset commitments in the LFS been funded? (Section 9.3)

This Chapter also identifies the potential for improved disclosure about the funding of election commitments (Section 9.2.7).

It should be noted that this Chapter is not intended to assess whether the LFS commitments have been implemented.<sup>612</sup> This may be done as part of future inquiries into financial and performance outcomes. This Chapter is restricted to looking at whether or not funding for the commitments has been included in the budget estimates to date.

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<sup>608</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), p.1.

<sup>609</sup> \$3.3 billion of this will be funded by the general government sector, with the Transport Accident Commission providing \$85.2 million.

<sup>610</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), pp.7-10.

<sup>611</sup> *ibid.*, pp.12-13.

<sup>612</sup> For example, whether the intended number of CFA fire trucks has been provided.

## 9.2 Output expenses

The LFS includes 100 output commitments.<sup>613</sup> Of these, 82 projects were expected to start in 2014-15 or 2015-16, with the remaining 18 to start in later years. The projects starting in 2014-15 or 2015-16 were estimated to require \$3.2 billion (over five years) including \$734.9 million in 2015-16.<sup>614</sup>

Table 9.1 summarises the output commitments, along with the measures expected to partially offset the expenses.

**Table 9.1** Summary of output commitments from *Labor's Financial Statement 2014*

	Number of commitments	Total impact over five years (\$ million)
Commitments to be funded by the general government sector	94	3,309.1
Commitments to be funded by the Transport Accident Commission	6	85.2
<b>Total commitments</b>	<b>100</b>	<b>3,394.3</b>
LESS:		
Expenditure reduction initiatives	9	334.5
Reprioritisation of existing resources	n/a <sup>(a)</sup>	804.5
Use of existing funds	4	713.0
<b>Total offset</b>		<b>1,852.0</b>
<b>Net impact<sup>(b)</sup></b>		<b>1,457.1</b>

(a) *Labor's Financial Statement 2014* includes five groups of reprioritisations, with specific initiatives from past budget papers identified for four groups.

(b) Impact on the general government sector; excludes commitments to be funded by the Transport Accident Commission (which is part of the public financial corporations sector).

Source: Adapted from Victorian Labor, *Labor's Financial Statement 2014* (2014), p.6.

Figure 9.1 below shows the extent to which the Committee considers the Government has funded the 100 output commitments included in the LFS.

The budget papers state that funding for all 82 commitments listed in the LFS as beginning in 2014-15 or 2015-16 has been provided in the 2015-16 Budget. In terms of value, the budget papers state that, of the \$3.3 billion committed (for the general government sector) funding for \$3.2 billion had been provided.<sup>615</sup>

<sup>613</sup> Referred to in the LFS as 'recurrent funding commitments' (Victorian Labor, *Labor's Financial Statement 2014* (2014), pp.7-10).

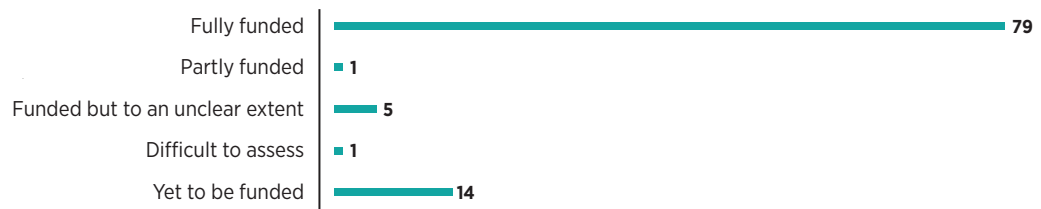
<sup>614</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), pp.7-10.

<sup>615</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.108.

The Committee's assessment identified:

- 79 commitments (worth \$3.0 billion over five years) which were clearly fully funded
- one commitment (for \$25.4 million over five years) which was partly funded
- five commitments (totalling \$174.3 million over five years) which have been funded, but the extent to which they have been funded is not clear
- one commitment (for \$4.0 million over five years) which is more difficult to assess
- 14 commitments (worth \$182.2 million) which do not yet appear to be funded.

**Figure 9.1** Output commitments from *Labor's Financial Statement 2014* funded in the budget papers (number of commitments)



Source: Committee calculations based on Department of Treasury and Finance, *2014-15 Budget Update* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1; Victorian Labor, *Labor's Financial Statement 2014* (2014).

However, the Committee notes that there are six initiatives which are marked in the budget papers as fulfilling election commitments where it is not clear what commitments they relate to (see Section 9.2.6). These may relate to some of the 14 commitments identified as 'yet to be funded'.

### 9.2.1 Commitments yet to be funded

Of the 100 commitments included in the LFS, 14 (with a total commitment of \$182.0 million) do not appear to be included in the 2014-15 Budget Update or the 2015-16 Budget. These projects are not expected to start until 2016-17 or later. Therefore no delay has come about as a result of not funding these projects to date.

These commitments are listed in Appendix A9.1.

The budget papers state that, 'Funding has been provisioned in this budget for these future allocations'.<sup>616</sup> The Committee notes that the allowance held for 'decisions made but not yet allocated' in the forward estimates is greater than the

<sup>616</sup> *ibid.*

total commitment for these projects.<sup>617</sup> This allowance is therefore sufficient to provide funds for these 14 commitments in future budgets without affecting the current estimates for output expenses over the forward estimates period.

### 9.2.2 Fully funded commitments

The 2014-15 Budget Update and the 2015-16 Budget have fully funded 79 commitments, totalling \$3.0 billion over five years. This includes:<sup>618</sup>

- 61 commitments that have been allocated funding as set out in the election commitments
- 11 commitments<sup>619</sup> where the overall amounts allocated were the same as the amounts committed, but the schedules of expenditure varied (see Appendix A9.2)
- five commitments<sup>620</sup> where greater amounts of funding (totalling an additional \$23.1 million over five years<sup>621</sup>) were allocated than committed in the LFS<sup>622</sup> (see Appendix A9.2)
- two commitments for the provision of new public holidays,<sup>623</sup> which are not mentioned in the budget papers, although ministers indicated to the Committee that adjustments for these public holidays have been factored into departments' budgets.<sup>624</sup>

### 9.2.3 Partly funded commitments

Funding for one commitment, *Tech Schools – Program Component*, has been partially provided in the 2015-16 Budget.<sup>625</sup> The Minister for Education stated that further funding will be allocated in future budgets.<sup>626</sup>

<sup>617</sup> Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.35.

<sup>618</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1; and Victorian Labor, *Labor's Financial Statement 2014* (2014).

<sup>619</sup> Including two commitments, *Newstead Solar* and *Macedon Solar*, which appear to have been funded in the budget papers as a single initiative, *Newstead/Woodend Renewable Energy Grants*.

<sup>620</sup> Including two which were fully funded, but with a different mix of asset and output funding to what had been listed in the LFS.

<sup>621</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), pp.20, 83, 92; Victorian Labor, *Labor's Financial Statement 2014* (2014), pp.7-8.

<sup>622</sup> For one of these commitments, *Young Farmer Scholarships*, the discrepancy may be explained as a rounding error.

<sup>623</sup> *Make Grand Final Friday a Public Holiday* and *Make Easter Sunday a Public Holiday*.

<sup>624</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.26 (cf. Hon. Jenny Mikakos MLC, Minister for Families and Children, *2015-16 Budget Estimates Transcript of Evidence*, 20 May 2015, p.8).

<sup>625</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.47.

<sup>626</sup> Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015, p.4.

## 9.2.4 Funded, but to an unclear extent

For five commitments, some funding has been provided in the 2015-16 Budget. However, it is not clear whether this is for part or the whole of the commitment:

- two commitments, *Beth Weizmann Centre Security Enhancements* and *Indian Cultural Precinct*, have been funded through the *Community Infrastructure and Cultural Precincts Fund* initiative,<sup>627</sup> but the budget papers do not specify whether the whole or part of each commitment has been provided as part of the initiative
- the budget papers indicate that a component of the *Expanding Public Transport Concessions for Veterans* commitment will be funded by the Transport Accident Commission rather than the general government sector,<sup>628</sup> although the amount to be provided by the Commission is not specified in the budget papers
- the commitment for *450 New Fire Fighters* does not appear as an initiative in the budget papers, but is noted as contributing to an increase in the cost of the *Emergency Capability* output (without being quantified),<sup>629</sup> and, while the Treasurer remarked that 'we are on the way towards employing 450 extra firefighters',<sup>630</sup> he did not indicate how much funding has been provided
- the cost of one initiative, *Car Registration Discounts for Trades Apprentices*,<sup>631</sup> is less than estimated in the LFS,<sup>632</sup> although the budget papers do not specify whether this is because the estimated cost of fully implementing the initiative has been revised, the scope has changed or some other factor.

## 9.2.5 Commitments where the funding status is difficult to assess

There is no initiative in the budget papers that clearly corresponds to the *Multicultural Grants (Including School Security)* commitment. It may have been funded as part of another initiative, the *Community Infrastructure and Cultural Precincts Fund*.<sup>633</sup> This initiative is relevant in subject, provides sufficient resources to fund the commitment and is noted in the budget papers as contributing to an election commitment.<sup>634</sup> However, there is nothing explicitly linking this initiative to this specific commitment.

<sup>627</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.94.

<sup>628</sup> *ibid.*, pp.20-1.

<sup>629</sup> *ibid.*, pp.269, 288.

<sup>630</sup> Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.12.

<sup>631</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), pp.20-1.

<sup>632</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), p.7.

<sup>633</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.92.

<sup>634</sup> *ibid.*, p.94.

### 9.2.6 Additional initiatives funding election commitments

A further six initiatives in the budget papers are marked as fulfilling election commitments where it is not clear which LFS commitments the initiatives relate to. These have not been counted towards any commitment in the above analysis. These are listed in Appendix A9.3, along with the *Community Infrastructure and Cultural Precincts Fund* discussed in Section 9.2.5.

In some cases, the initiative descriptions explicitly indicate that the initiative fulfils a commitment in the LFS. However, the titles and descriptions of the initiatives do not clearly relate to any of the LFS commitments. The Committee is therefore unable to identify which LFS commitments have been funded by these initiatives or whether these initiatives fully or partially fund those commitments.

These initiatives may fund part of the 14 commitments noted as 'yet to be funded'. This lack of clarity would be resolved by the adoption of a clearer reporting framework in future budget papers as recommended in Section 9.2.7.

### 9.2.7 A clearer reporting framework

As can be seen from the above discussion, it is not easy to reconcile the budget papers and the LFS. The inclusion of an additional report in the election commitments section of budget papers would improve transparency. The report could show:

- which commitments have been funded to date
- which initiatives relate to which commitments
- how much funding has been provided to date for each election commitment
- which commitments have been partly funded or not yet funded, whether the Government intends to fully fund these commitments and when further funding will be provided.

Previous governments have included similar reports in past budget papers.<sup>635</sup>

**FINDING 87:** Of the 100 output commitments in *Labor's Financial Statement 2014*, at least 85 received funding in the 2014-15 Budget Update or the 2015-16 Budget. Of these, 79 commitments (totalling \$3.0 billion over five years) were fully funded and one commitment (for \$25.4 million over five years) has been partly funded. Five commitments (for \$174.3 million) have been funded, but the extent of the funding is not clear. Additional initiatives state that they provide funding for election commitments but it is not clear which, if any, of the commitments in *Labor's Financial Statement 2014* these relate to. The budget papers do not provide a clear connection between commitments made in *Labor's Financial Statement 2014* and the initiatives released in the budget papers in some cases.

<sup>635</sup> For example, Department of Treasury and Finance, *Budget Paper No.3: 2010-11 Service Delivery* (2010), Chapter 4.

**RECOMMENDATION 58:** Future budget papers include a report forming part of the election commitments section of budget papers that shows:

- (a) which election commitments (including output, asset and expenditure reduction commitments) have been funded to date
- (b) which budget initiatives each election commitment has been funded through
- (c) how much funding has been provided for each election commitment to date
- (d) for commitments that have been partly or not yet funded, whether the Government intends to further fund the commitments and when further funding will be provided.

## 9.2.8 Funding methods

As shown in Table 9.1, the Government intends to partly offset the costs of its output commitments in three ways:

- expenditure reduction initiatives
- the reprioritisation of existing resources
- the use of existing funds.

The budget papers indicate that the Government intends to use \$1.8 billion<sup>636</sup> from these sources to fund the output election commitments. The budget papers state that \$1.5 billion of this has been provided in the 2014-15 Budget Update or the 2015-16 Budget.<sup>637</sup>

### Expenditure reduction initiatives

In the LFS, the Labor Party indicated that it would introduce initiatives to reduce output expenses by \$334.5 million over the five years to 2018-19.<sup>638</sup> This involves nine expenditure reduction methods.

The budget papers included all of these methods as expenditure reduction initiatives (see Section 7.7.1 of this report), with the same expected total expenditure reduction.

One commitment, *Cease Producing Hard-Copy Government Reports for Tabling in Parliament*,<sup>639</sup> has been renamed *Reduce Hard Copy Reports Tabled in Parliament*.<sup>640</sup> However, the Committee notes that the estimated amount of expenditure reduced by this initiative is unchanged.

These expenditure reduction initiatives are further discussed in Section 7.7.1.

<sup>636</sup> The LFS indicates that \$1,859.0 million will offset its output initiatives through 'savings and efficiencies, reprioritisations and existing funds in forward estimates' (Victorian Labor, *Labor's Financial Statement 2014* (2014), p.6). The budget papers do not explain why this is represented in the budget papers as \$1.8 billion.

<sup>637</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.108.

<sup>638</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), pp.6, 10.

<sup>639</sup> *ibid.*, p.10.

<sup>640</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.105.

### Reprioritisation of existing resources

The LFS identifies a number of areas from which funding is to be reprioritised to fund the Government's commitments (see Table 9.2).<sup>641</sup>

**Table 9.2** Reprioritisations planned to fund output commitments

Source	Funds freed for output initiatives <sup>(a)</sup> (\$ million)
Reform industry and innovation policy	608.0
2014 Pre-Election Budget Update initiatives being replaced by alternative Labor policy	34.0
Reprioritise 2014 Pre-Election Budget Update initiatives	124.6
Reprioritise 2014-15 Budget initiatives	37.9
<b>Total</b>	<b>804.5</b>

(a) Five-year total.

Source: Adapted from Victorian Labor, *Labor's Financial Statement 2014* (2014), p.10.

The LFS also includes a more detailed list of how the reprioritisations from the 2014-15 Budget and the 2014 Pre-Election Budget Update would be achieved, including the specific initiatives replaced or discontinued.<sup>642</sup>

The 2015-16 Budget states that \$1.5 billion will be reprioritised from existing resources over five years.<sup>643</sup> This amount is greater than the \$804.5 million proposed in the LFS.<sup>644</sup> However, the budget papers do not indicate whether the programs from which the money has been reprioritised in the budget papers are the same as those detailed in the LFS.

The Committee asked departments about initiatives from which funding has been reprioritised. In response, the Department of Economic Development, Jobs, Transport and Resources reported that it had reprioritised \$41.1 million under the *Jobs in the 21<sup>st</sup> Century* program (part of the 2014 Pre-Election Budget Update initiatives identified in the LFS for reprioritisation) and \$470.0 million through reforms of industry and innovation policy.<sup>645</sup>

<sup>641</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), p.10.

<sup>642</sup> *ibid.*, p.11.

<sup>643</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58.

<sup>644</sup> The Committee also notes that reprioritisation identified in each year of the forward estimates period in the budget papers is greater than that identified for each year in the LFS (Victorian Labor, *Labor's Financial Statement 2014* (2014), p.10; Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.58).

<sup>645</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.20.



The Department of Health and Human Services also responded that it had reprioritised \$21.1 million under two initiatives<sup>646</sup> that had been identified in the LFS for reprioritisation.<sup>647</sup>

Other departments provided information on reprioritised programs or initiatives (see Appendix A7.2). However, these initiatives were not those identified for reprioritisation in the LFS.

### Use of existing funds

The LFS also identified four funds that are to be used for election output commitments (see Table 9.3).

**Table 9.3** Existing funds planned to be used for output commitments

Source	Funds freed for output initiatives <sup>(a)</sup> (\$ million)
Regional Growth Fund	500.0
Victorian Property Fund	57.0
Recreational Fishing Licence Fund	10.0
Community Support Fund	146.0
<b>Total</b>	<b>713.0</b>

(a) Five-year total.

Source: Adapted from Victorian Labor, *Labor's Financial Statement 2014* (2014), p.10.

The budget papers do not provide any details about whether or not these sources have been used to fund the election commitments.

The Department of Economic Development, Jobs, Transport and Resources indicated to the Committee that the Regional Growth Fund has been reprioritised.<sup>648</sup>

**FINDING 88:** *Labor's Financial Statement 2014* indicates that \$1.9 billion of funding will come from expenditure reduction initiatives, the reprioritisation of existing resources and the use of existing funds. The budget papers state that \$1.5 billion has been provided from these sources in existing forward estimates. However, the budget papers do not provide further details.

<sup>646</sup> \$18.0 million from the *Strategic sporting infrastructure program* (Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.56) and \$3.8 million from the *Flexible post-crisis responses for women and children* initiative (Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.77).

<sup>647</sup> Department of Health and Human Services, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, resubmitted 7 October 2015, p.18.

<sup>648</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.20.

### 9.3 Asset investment

The LFS includes 61 asset commitments,<sup>649</sup> with a total estimated investment (TEI) for the construction or acquisition of the assets of \$6.2-6.8 billion.<sup>650</sup> Scheduling of this expenditure is not specified in the document, suggesting that the expected commencement date for each project may be any time over the period 2015-16 to 2018-19. Two commitments, with a TEI of \$60.1 million, are intended to be funded by the Transport Accident Commission.

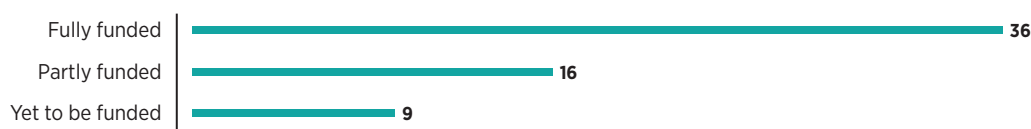
**Table 9.4** Summary of asset commitments from *Labor's Financial Statement 2014*

Asset commitments	Number of commitments	Total estimated investment (\$ million)
Commitments funded by the general government sector	57	3,778.1
Commitments funded by the Transport Accident Commission	2	60.9
Rail enhancement priorities	2	2,400.0-3,000.0
<b>Total</b>	<b>61</b>	<b>6,239.0-6,839.0</b>

Source: Adapted from Victorian Labor, *Labor's Financial Statement 2014* (2014), p.6.

Figure 9.2 shows the Committee's assessment of how many of the 61 asset commitments in the LFS have been funded in the 2014-15 Budget Update or the 2015-16 Budget.

**Figure 9.2** Asset commitments from *Labor's Financial Statement 2014* funded in the budget papers to date (number of commitments)



Source: Committee calculations based on Department of Treasury and Finance, *2014-15 Budget Update* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1; Victorian Labor, *Labor's Financial Statement 2014* (2014).

The budget papers state that, of the \$6.8 billion committed, funding for \$4.4 billion had been provided.<sup>651</sup> The Committee's assessment shows that 36 commitments (worth \$3.6-4.0 billion) have been fully funded. A further 16 commitments for \$2.4-2.6 billion have been partly fulfilled. The remaining nine commitments are yet to be funded.

<sup>649</sup> Referred to in the LFS as 'capital funding commitments'.

<sup>650</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), pp.12-13.

<sup>651</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.108.

### 9.3.1 Commitments yet to be funded

Of the commitments listed in the LFS, nine (with a total TEI of \$175.4 million) did not have funding included in the budget papers. These are listed in Appendix A9.4.

There are a range of reasons why these have not been funded to date. The Government has listed a number of explanations, including the need for:<sup>652</sup>

- negotiations with other parties, such as the Commonwealth Government, a health agency and a local government
- the identification of suitable sites
- planning and business case development.

The budget papers note that:<sup>653</sup>

Funding is being held in contingency for the full cost of delivering these asset initiatives ...

However, the budget papers also indicate that funding for one project (*Aikenhead Biomedical Engineering*) is 'contingent on the Commonwealth matching funding'.<sup>654</sup> In August 2015, the Commonwealth Government had still not made a commitment to the project.<sup>655</sup>

### 9.3.2 Fully funded commitments

Of the asset commitments included in the LFS, 36 (with a total TEI of \$3.6-4.0 billion) are fully funded in the 2015-16 Budget. Of these:

- 22 commitments<sup>656</sup> have been included as asset initiatives unchanged from the LFS
- six commitments have been included in the 2015-16 Budget with TEI estimates increased to \$15.7-18.7 billion, either because the scope of the initiative has changed since the commitment, the commitment was fulfilled as part of a larger project, or because the initiative includes extra funding from other sources (see Appendix A9.5)
- six commitments were funded, but with a different mix of asset and output expenditure to the mix specified in the LFS<sup>657</sup> (see Appendix A9.5)

<sup>652</sup> *ibid.*, pp.109-11; cf. Hon. Tim Pallas MP, Treasurer, *2015-16 Budget Estimates Transcript of Evidence*, 8 May 2015, p.8.

<sup>653</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.109.

<sup>654</sup> *ibid.*

<sup>655</sup> Hon. Jill Hennessy MP, Minister for Health, *Federal Government Urged to Support New Medical Research Centre* (Media release, 17 August 2015).

<sup>656</sup> Including two projects to be funded by the TAC.

<sup>657</sup> For one of these, *Police Communications Upgrade*, output funding for the initiative was made up of savings from the existing project, reprioritisation of funding and new funding of \$11.5 million (Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.84), which is \$1.5 million more than the LFS commitment.

- the components of two commitments<sup>658</sup> were rearranged and funded as a different two initiatives.<sup>659</sup>

### 9.3.3 Partly funded commitments

A further 16 asset commitments (with a TEI of \$2.4-2.6 billion) have been partly funded in the 2015-16 Budget, with funding of \$179.4 million provided through asset initiatives (see Appendix A9.6).<sup>660</sup>

Twelve projects are clearly funded in the budget papers as asset initiatives with TEIs lower than the commitments in the LFS. In nine cases, the budget papers specify that further funding will be allocated in future budgets. There are no comments about future funding in the other three cases.<sup>661</sup>

Early works, including planning and business case preparation, have been funded through output initiatives for two other projects, *Bolton St Eltham Upgrade* and *Streamlining Hoddle St*.<sup>662</sup> The budget papers note that the 'balance of election commitment [is] to be delivered in future budgets'.<sup>663</sup>

For two commitments, the *School Capital Package* and *Extra School Capital* commitments, which had a total TEI of \$530.0 million, the budget papers do not clearly indicate whether the commitments have been funded. However, in his budget estimates hearing, the Minister for Education remarked that:<sup>664</sup>

Of the \$530 million TEI committed for new and existing government school capital programs, \$497.5 million has been acquitted.

The Minister did not specify which initiatives in the budget papers included this funding and no combination of initiatives for the Department of Education and Training totals that amount.

In Section 9.2.5, the Committee has made a recommendation that is intended to clarify situations like these.

**FINDING 89:** Of the 61 asset commitments in *Labor's Financial Statement 2014*, 36 (with a TEI of \$3.6-4.0 billion) have been fully funded and 16 (with a TEI of \$2.4-2.6 billion) have been partly funded. The remaining nine commitments (with a TEI of \$175.4 million) have not yet received funding.

<sup>658</sup> *Huntly Fire Station and CFA and SES Capital Grants*.

<sup>659</sup> *Country Fire Authority Stations Program and Expansion of Bellarine Victorian State Emergency Services Headquarters*.

<sup>660</sup> Committee calculation based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), pp.36-7, 53; Victorian Labor, *Labor's Financial Statement 2014* (2014).

<sup>661</sup> *Orygen Youth Mental Health, Victorian Heart Hospital and West Gate Distributor*.

<sup>662</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), pp.31, 35.

<sup>663</sup> *ibid.*, pp.20-1.

<sup>664</sup> Hon. James Merlino MP, Minister for Education, *2015-16 Budget Estimates Transcript of Evidence*, 12 May 2015, p.4.

### 9.3.4 Funding asset commitments

As part of the LFS, an external assessor stated that:<sup>665</sup>

... the capital policy commitments are capable of being accommodated within the available asset contingencies as disclosed in the Pre-Election Budget Update.

That is, funding the asset commitments will not increase the total estimates for asset investment compared to the estimates included in the 2014 Pre-Election Budget Update.

For the three years which are common to the 2014 Pre-Election Budget Update and the 2015-16 Budget (that is, 2015-16 to 2017-18), the net expenditure on assets is estimated at \$7.5 billion in the 2015-16 Budget,<sup>666</sup> less than the \$10.8 billion estimated in the 2014 Pre-Election Budget Update.<sup>667</sup> Further discussion of asset investment funding can be found in Section 8.6 of this report.

**FINDING 90:** The funded commitments from *Labor's Financial Statement 2014* have not resulted in an increase in anticipated investment expenditure compared to the estimates in the 2014 Pre-Election Budget Update. Net expenditure on assets was expected to be \$10.8 billion between 2015-16 and 2017-18 in the 2014 Pre-Election Budget Update, while the 2015-16 Budget expects net expenditure to be \$7.5 billion over the same period, a reduction of \$3.3 billion.

### 9.3.5 Road funding

As part of its election commitments, the Labor Party indicated that a total of \$2 billion will be allocated to rural and outer suburban areas to improve roads:<sup>668</sup>

- A minimum of \$1 billion over eight years will be allocated to repair and upgrade roads in Melbourne's outer suburban and interface communities.
- A minimum of \$1 billion over eight years will be allocated to repair and upgrade roads and level crossings in rural and regional communities.

These commitments are represented in the LFS as two guarantees of \$500.0 million each (over the four years covered by the LFS): *Regional Roads Fund – Stage 1* and *Outer-Suburban Roads Fund – Stage 1*.<sup>669</sup>

<sup>665</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), p.3.

<sup>666</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.10.

<sup>667</sup> Committee calculations based on Department of Treasury and Finance, *2014 Victorian Pre-Election Budget Update* (2014), p.30.

<sup>668</sup> Victorian Labor, *Project 10,000* (2014), p.34.

<sup>669</sup> Victorian Labor, *Labor's Financial Statement 2014* (2014), p.13.

The Committee understands that these guarantees are met through a number of projects in the LFS and the budget papers. However, neither the LFS nor the budget papers specify which projects should be counted towards the \$500.0 million totals. The budget papers reiterate the commitment,<sup>670</sup> but do not indicate progress towards meeting the guarantees.

The Committee considers that the budget papers could more clearly demonstrate the progress to date at implementing these guarantees by specifying the particular projects that the Government considers should be counted towards these guarantees.

**FINDING 91:** The Government's election commitments included guarantees for a minimum of \$2.0 billion funding over eight years for roads in rural and outer suburban areas. This includes \$1.0 billion to be spent over the forward estimates period. The budget papers do not indicate progress towards compliance with the guarantees.

**RECOMMENDATION 59:** Future budget papers include a list of the initiatives that contribute to the guaranteed minimum funding levels for:

- (a) roads in Melbourne's outer suburban and interface communities
- (b) roads and level crossings in rural and regional communities.

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670 Department of Treasury and Finance, *Budget Paper No.2: 2015-16 Strategy and Outlook* (2015), p.41.

# 10 Performance measurement

## 10.1 Introduction

The performance measurement system is an essential part of the way the Government communicates its intended policies and its desired impact on the community. It also forms the basis for departmental reporting about actual achievements at the end of the year, making it a key element of transparency for the spending of public money. In addition, performance measurement can be a management tool to improve the efficiency and effectiveness of departments' service delivery.

Since its introduction in 1998-99, the performance measurement system has evolved, with the aim of increasing its quality and usefulness, as well as enhancing the transparency and accountability of departments' activities.

The former Public Accounts and Estimates Committee undertook a detailed analysis of the performance measurement system in 2014 in its *Review of the Performance Measurement and Reporting System*.<sup>671</sup> In this report, the former Committee assessed the different components of the system for each department and identified examples of good practice, as well as areas for improvement. Recommendations were made to individual departments and to central agencies. Many recommendations were accepted by the previous government in its response to the report.<sup>672</sup>

The Victorian Auditor-General's Office also conducted an audit in 2014 of how the performance measurement and reporting system was applied by three departments<sup>673</sup> and how it is overseen by the Department of Treasury and Finance.<sup>674</sup>

The Committee is conscious that these reports were released in 2014 and that there has not yet been sufficient time to fully implement the recommendations from the former Committee and the Victorian Auditor-General's Office.

At the budget estimates hearings in May 2015, the Minister for Finance indicated that the Government intends to undertake a review of the performance reporting framework, including outputs and performance measures.<sup>675</sup>

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671 Public Accounts and Estimates Committee, *Review of the Performance Measurement and Reporting System* (2014).

672 Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 118<sup>th</sup> Report to Parliament – Review of the Performance Measurement and Reporting System*, tabled 18 September 2014.

673 The Department of Premier and Cabinet, the former Department of Health and the former Department of Transport, Planning and Local Infrastructure.

674 Victorian Auditor-General's Office, *Public Sector Measurement and Reporting* (2014).

675 Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.2.

As a result of these factors, the Committee expects the performance measurement system to change in the near future. The aim of this chapter therefore is not to comprehensively assess the performance measurement system at this time. Rather, this chapter aims to provide an overview of the changes to the performance measurement system in the 2015-16 budget papers through the following questions:

- How does the performance measurement system operate in Victoria? (Section 10.2)
- What changes have been made to the key components of the performance measurement system for 2015-16? (Section 10.3)
- How are initiatives released in the 2015-16 budget assessed by performance measures? (Section 10.4)
- Are there any performance measures that have been proposed for discontinuation that are still valuable for measuring performance? (Section 10.5)

The Committee intends to examine the performance measurement system in more detail at a later date.

## 10.2 Background

The performance measurement system currently includes six key components (see Figure 10.1):

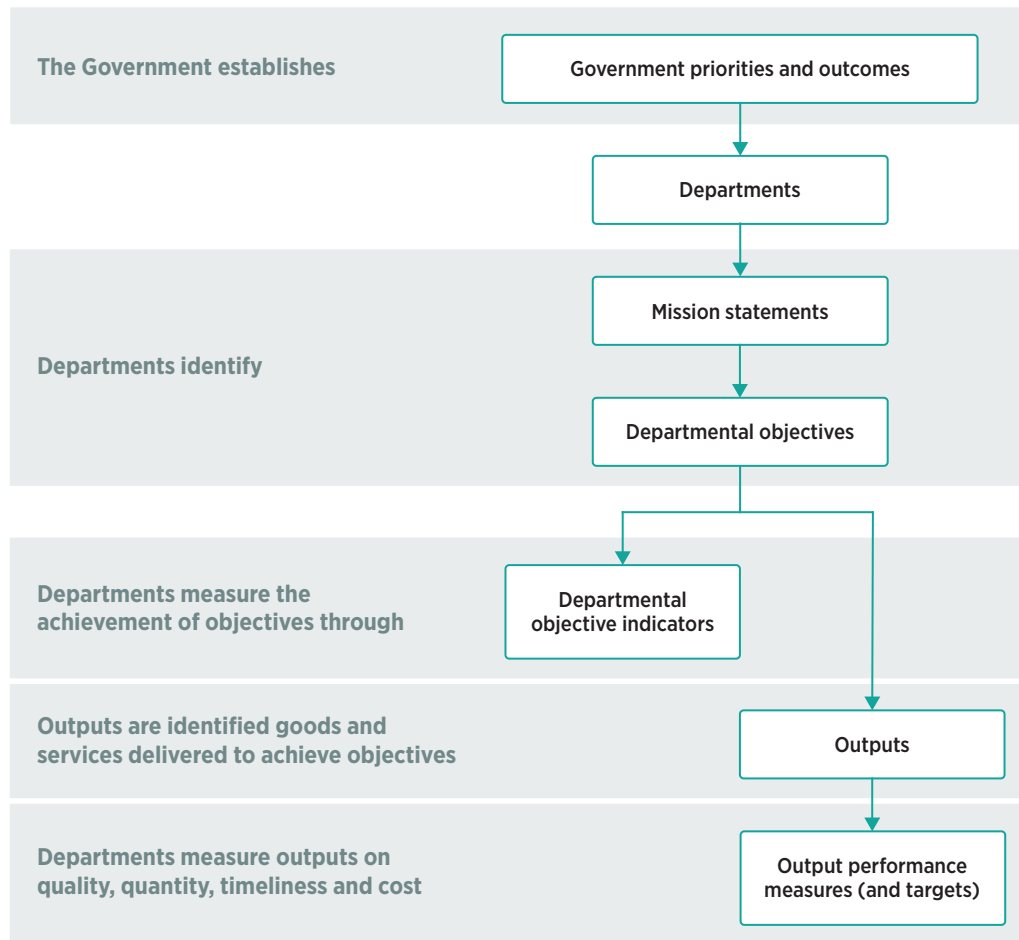
- the Government's priorities and intended outcomes, which reflect the desired impact of its policies on the community
- mission statements identified by departments to support the Government's priorities and intended outcomes
- departmental objectives, which describe the departments' intended impact on the community through their delivery of goods and services
- departmental objective indicators to assess progress towards departmental objectives
- output descriptions, which summarise the goods and services that a department plans to deliver
- output performance measures and targets, which measure and report on the quantity, quality, timeliness and cost of the goods and services (that is, outputs) delivered.

The components of the system are discussed in more detail in the former Committee's report on the performance measurement system.<sup>676</sup>

<sup>676</sup> Public Accounts and Estimates Committee, *Review of the Performance Measurement and Reporting System* (2014), Chapter 2.



**Figure 10.1** The Victorian performance measurement system



Source: Compiled by the Committee based on Department of Treasury and Finance, *A Guide to Corporate and Long Term Planning* (2013), p.14; Department of Treasury and Finance, *BFMG-02: Performance Management Framework* (2012), pp.97-8.

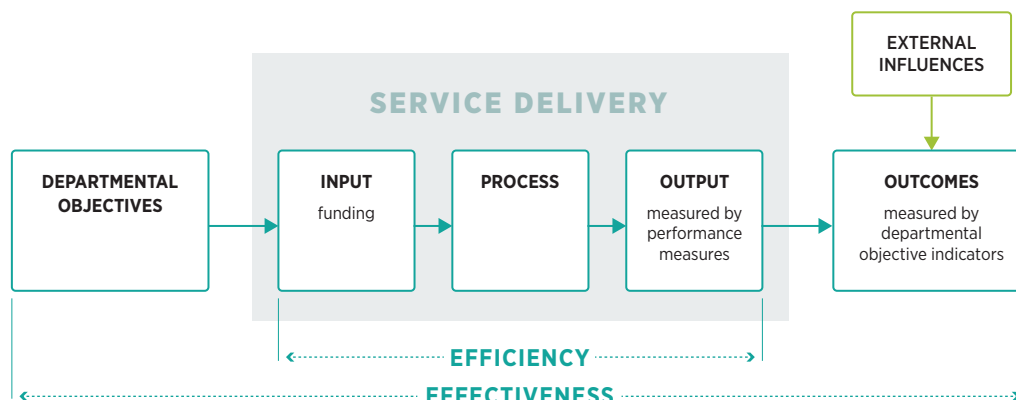
### 10.2.1 Measuring effectiveness and efficiency

A key purpose of the performance measurement system is to assess the effectiveness and efficiency of the delivery of goods and services.<sup>677</sup> Within the performance measurement framework, efficiency can be quantified by comparing the inputs (that is, funding) to the outputs delivered.<sup>678</sup> Effectiveness is measured by comparing departmental objectives to the impact on the community achieved (that is, outcomes). Figure 10.2 illustrates this process.

<sup>677</sup> Department of Treasury and Finance, *BFMG - 09: Output Specification and Performance Measures* (2012), p.109.

<sup>678</sup> *ibid.*

**Figure 10.2** Effectiveness and efficiency measurement within the performance measurement system



Source: Public Accounts and Estimates Committee, based on Victorian Auditor-General's Office, *Environment and Sustainability Sector: Performance Reporting* (2013), p.2.

### 10.2.2 Reporting performance measurement

The public reporting cycle in Victoria includes each department reporting on its expected performance as part of the budget papers, and on its actual performance as part of its annual report (see Figure 10.3).

**Figure 10.3** Reporting cycle in Victoria



Source: Public Accounts and Estimates Committee.

Departmental performance statements are published in the budget papers in May, before the start of the financial year. These statements include descriptions of all key components of the performance measurement system related to departments, including targets (that is, expected results for the financial year). The actual results are published in departments' annual reports along with explanations for significant variances from targets.

Additionally, departments report to the Department of Treasury and Finance on their performance against targets twice a year (in December<sup>679</sup> and at the end of the financial year<sup>680</sup>). This is supposed to be a consideration in determining whether or not departments receive their funding for output delivery.<sup>681</sup>

<sup>679</sup> Department of Treasury and Finance, *BFMG - 50: Output Revenue Certification* (2007), p.81.

<sup>680</sup> Department of Treasury and Finance, *BFMG - 51: Output Revenue Certification - Year End* (2007), p.83.

<sup>681</sup> Department of Treasury and Finance, *BFMG - 48: Performance Reporting* (2007), p.78.

### 10.2.3 Departmental planning

Performance measures and their targets relate specifically to the budget year. Departmental objectives and their indicators are intended to relate to the medium term.<sup>682</sup>

In relation to the longer term, the Department of Treasury and Finance undertook some work during the 57<sup>th</sup> Parliament to establish a system of long-term planning. The Department indicated that:<sup>683</sup>

The objective of long-term planning is to give clear direction to government concerning future output and service delivery trajectories, challenges and reform opportunities over a long term planning horizon (10 years), in the context of the expected economic and fiscal environment.

Each department was to develop a ten-year long-term plan and a four-year corporate plan.

The Victorian Auditor-General's Office assessed the development of three departments' corporate and long-term plans in 2014. The Office's report indicated that:<sup>684</sup>

The progress towards developing corporate and long-term plans that fully address government's requirements has been slow. The latest draft plans for Department of Health, Department of Transport, Planning and Local Infrastructure and Department of Premier and Cabinet fall well short of the government's minimum requirements and the rate of progress does not suggest that agencies are close to addressing this shortfall.

...

Across all departments, the depth and quality of corporate plans improved after minimum requirements were introduced in 2011. However, the corporate plans of the audited departments do not adequately address government's requirements.

The preparation of long-term plans was paused after departments submitted their first versions to government in March 2013 because of their inconsistent quality and poor timeliness in submitting plans to the Department of Treasury and Finance (DTF).

The fiscal and performance challenges facing Victoria mean effective long-term planning is critical if government is to be prepared to meet these challenges.

The Committee sought details from departments in the 2015-16 Budget Estimates General Questionnaire regarding the current status of their corporate and long-term plans. All departments noted that the development of their corporate

<sup>682</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.113.

<sup>683</sup> Department of Treasury and Finance, *A Guide to Corporate and Long-Term Planning* (2014), p.11.

<sup>684</sup> Victorian Auditor-General's Office, *Public Sector Performance Measurement and Reporting* (2014), p.25.

plans is underway and that, at present, the development of a long-term plan is not a Government requirement. The Department of Economic Development, Jobs, Transport and Resources informed the Committee that:<sup>685</sup>

The Department of Treasury and Finance (DTF) has advised it is developing new guidelines for corporate, 'long-term' and asset management planning and completion of these plans should be deferred until new guidelines are issued by the Minister for Finance.

The Committee looks forward to seeing these new guidelines completed and implemented, as it considers corporate and long-term planning to be important components of an effective performance measurement system.

**FINDING 92:** All departments have indicated that they are currently developing corporate plans. The Department of Treasury and Finance's guidance on long-term planning is currently under review and the development of long-term plans has therefore been paused.

## 10.3 Changes to the performance measurement system in the 2015-16 Budget

### 10.3.1 Departmental objectives

According to the Department of Treasury and Finance's guidance, departmental objectives must be designed to identify the impact on the community (that is, they should be outcomes-based)<sup>686</sup> and should be clearly linked to the goods and services the department delivers.<sup>687</sup>

There were 35 departmental objectives across the government departments in the 2015-16 budget papers.<sup>688</sup> This is a decrease of 11 objectives compared to the 2014-15 Budget and 17 objectives fewer than the 2011-12 Budget, the first year in which departmental objectives appeared in the budget papers (see Figure 10.4 below).

The Committee notes that 17 objectives across departments remained unchanged between 2014-15 and 2015-16. Additionally, changes in the departmental objectives for 2015-16 include:<sup>689</sup>

- the discontinuation of three departmental objectives

<sup>685</sup> Department of Economic Development, Jobs, Transport and Resources, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 15 June 2015, p.10.

<sup>686</sup> Department of Treasury and Finance, *BFMG - 02: Performance Management Framework* (2012), p.98.

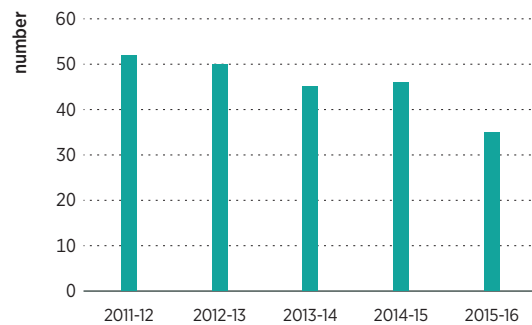
<sup>687</sup> Department of Treasury and Finance, *BFMG - 08: Departmental Objectives and Departmental Objective Indicators* (2013), p.103.

<sup>688</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2. Excludes the Victorian Auditor-General's Office and Parliament, which provided aims instead of outcomes-based objectives.

<sup>689</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2; Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), Chapter 2.

- the addition of one new departmental objective ('Increase Victoria's competitiveness and productivity: Support the delivery of policy and projects that enables increased productivity and competitiveness in Victoria')
- the rearrangement of 18 departmental objectives into nine
- the modification of eight departmental objectives (ranging from minor wording changes to a change in focus on the same topics).

**Figure 10.4** Number of departmental objectives, 2011-12 to 2015-16 budgets



Note: Excludes objectives listed by the Victorian Auditor-General's Office and Parliament, as they provided aims instead of outcomes-based objectives.

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2011-12 Service Delivery* (2011), Chapter 3; Department of Treasury and Finance, *Budget Paper No.3: Service Delivery, 2012-13 to 2015-16*, Chapter 2.

The discontinued objectives are:

- 'Assist businesses in accessing skilled workers to align with Victoria's industry needs'.
- 'Safer transport services and infrastructure: Make safety improvements to transport infrastructure and systems, improve security management and implement programs to promote safer transport user behaviour'.
- 'Facilitate strategic investment in State and local infrastructure: Develop proposals for State and local infrastructure projects, including sporting facilities, to stimulate growth, boost competitiveness, support population growth and build on Victoria's outstanding reputation for hosting major sporting events at world-class facilities'.

The Department of Environment, Land, Water and Planning was the only department to note the changes to its departmental objectives and provide explanations in the 2015-16 budget papers. The Department's stated reason for changes was 'to better reflect the focus and direction of the Department following machinery of government changes which came into effect on 1 January 2015'.<sup>690</sup> The Committee welcomes the inclusion of explanations and encourages the other departments to follow this practice in future budget papers.

<sup>690</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.194.

The Department of Premier and Cabinet indicated to the Committee that:<sup>691</sup>

New departmental objectives and objective indicators were established as a result of the 2014 State election, subsequent machinery of government changes and departmental restructure.

The changes included:

- wording changes to the department's objectives to create stronger links to outputs
- reducing the overall number of performance measures to improve clarity around output delivery, and ensure measures demonstrate effectiveness and efficiency
- rebalancing the quantity, quality and timeliness measures within each output.

Taking these factors into account, the department has proposed a number of measures for discontinuation that did not provide efficiency or effectiveness performance information suggesting these performance measures provide minimal value in explaining departmental performance.

**FINDING 93:** There are 35 departmental objectives in the 2015-16 budget papers. This is a decrease of 11 objectives compared to the 2014-15 budget papers and 17 fewer than the 2011-12 budget papers (when objectives were first introduced). Only the Department of Environment, Land, Water and Planning noted the changes and provided explanations in the budget papers.

**RECOMMENDATION 60:** Future budget papers include explanations for all modifications to departmental objectives, following the model of the Department of Environment, Land, Water and Planning in the 2015-16 budget papers.

### 10.3.2 Departmental objective indicators

Departmental objective indicators were introduced for the first time in the 2013-14 Budget.<sup>692</sup> These were defined by the Department of Treasury and Finance as 'a piece of data that demonstrates progress towards the achievement of a department's objectives'.<sup>693</sup> Similar to departmental objectives, departmental objective indicators must be outcomes-focused by identifying 'what is to be achieved rather than what outputs are delivered or what processes are followed'.<sup>694</sup>

In addition, departmental objective indicators should be indicative of changes to government priorities. The Government's guidance states that 'departmental objective indicators help Government, Ministers, the Department, Parliament and the community to assess how effective a department has been in delivering the Government's agenda over the medium term'.<sup>695</sup>

<sup>691</sup> Department of Premier and Cabinet, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 17 August 2015, p.1.

<sup>692</sup> Department of Treasury and Finance, *Budget Paper No.3: 2013-14 Service Delivery* (2013), Chapter 2.

<sup>693</sup> Department of Treasury and Finance, *BFGM - 08: Departmental Objectives and Departmental Objective Indicators* (2013), p.103.

<sup>694</sup> *ibid.*, p.107.

<sup>695</sup> *ibid.*, p.106.

There were 120 objective indicators across the government departments in the 2015-16 budget papers.<sup>696</sup> A total of 77 objective indicators remained unchanged since the previous budget. Changes between 2014-15 and 2015-16 consisted of:

- the discontinuation of 22 objective indicators
- the addition of 22 new objective indicators
- the rearrangement of six objective indicators into three
- the modification of 18 objective indicators (ranging from minor wording changes to a change in focus on the same topics).

The discontinued indicators are listed in Appendix A10.1 and the new indicators are listed in Appendix A10.2.

The overall result of these changes is a reduction by three compared to the 2014-15 Budget.

Some of the rearrangements are a result of a department's internal assessment of objective indicators. For example, the Department of Premier and Cabinet reduced its number of departmental objective indicators from 12 in 2014-15 to six in 2015-16. As previously noted, the Department indicated that these changes are a result of the 2014 State election, and a subsequent departmental review to reflect machinery-of-government changes, as well as efforts to address recommendations made by the Victorian Auditor-General's Office in 2014.<sup>697</sup>

The Committee notes that, although indicators were changed in seven departments, only three departments included comments in the budget papers explaining the changes.<sup>698</sup> These comments indicate that the changes have been driven by a changed focus following machinery-of-government changes,<sup>699</sup> changes in government strategies,<sup>700</sup> a desire to increase clarity<sup>701</sup> and the replacement of old measures with new measures believed to better evaluate the department's performance.<sup>702</sup>

The Committee notes, however, that not all explanations provided sufficient details to understand the reasons for changes to objective indicators. For example, the notes explain that the indicators 'Reduce regulatory burden by 25 per cent by 2014' and 'Reduce the costs and barriers to doing business in Victoria'<sup>703</sup> were amalgamated into 'Reduce the costs and barriers to doing

<sup>696</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2.

<sup>697</sup> Department of Premier and Cabinet, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 17 August 2015, p.1.

<sup>698</sup> The Department of Environment, Land, Water and Planning, the Department of Justice and Regulation, and the Department of Treasury and Finance.

<sup>699</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.194.

<sup>700</sup> *ibid.*, pp.316-7.

<sup>701</sup> *ibid.*, pp.194, 267.

<sup>702</sup> *ibid.*, pp.316-7.

<sup>703</sup> Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), p.277.

business in Victoria, including reducing the regulatory burden'.<sup>704</sup> However, the notes do not indicate why these were amalgamated or why the specific target of 25 per cent was removed.

The Committee sought further details from the Department of Treasury and Finance, specifically asking why the quantitative component of this indicator was removed (that is, the '25 per cent'). The Department responded that:<sup>705</sup>

Two previous indicators 'Reduce the Costs and barriers to doing business in Victoria' and 'Reduce regulatory burden by 25 per cent by 2014' were combined into one new indicator 'Reduce the costs and barriers to doing business in Victoria, including reducing the regulatory burden'. This is noted in the footnotes (d) and (f) on pp 316-17 of Budget Paper No.3.

The Committee considers that explanations provided by the departments to changes in objective indicators should include a level of detail that would enable the reader to understand the reasons for these adjustments.

As with departmental objectives, the Committee welcomes the inclusion of comments and detailed explanations provided by departments. The Committee encourages the other departments to follow this practice in future budget papers.

**FINDING 94:** There are 35 departmental objectives in the 2015-16 budget papers. This is a decrease of 11 objectives compared to the 2014-15 budget papers and 17 fewer than the 2011-12 budget papers (when objectives were first introduced). Only the Department of Environment, Land, Water and Planning noted the changes and provided explanations in the budget papers.

**RECOMMENDATION 61:** Future budget papers include explanations for all modifications to departmental objective indicators.

### 10.3.3 Outputs

Outputs are the groups of goods and services delivered by departments or entities on behalf of the State.<sup>706</sup> The Government's guidance indicates that outputs 'should be measurable in terms of their efficiency and effectiveness, i.e. the impact they are designed to have on the achievement of departmental objectives'.<sup>707</sup>

According to the Department of Treasury and Finance, outputs should be specified at a level which will:<sup>708</sup>

- assist the Government to determine the outputs it will purchase;

<sup>704</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.316.

<sup>705</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates Specific Questionnaire*, received 19 August 2015, p.1.

<sup>706</sup> They also include goods and services delivered to other government departments. See Department of Treasury and Finance, *BFMG - 09 Output Specification and Performance Measures* (2012), p.109.

<sup>707</sup> Department of Treasury and Finance, *BFMG - 09: Output Specification and Performance Measures* (2012), p.109.

<sup>708</sup> *ibid.*, p.110.

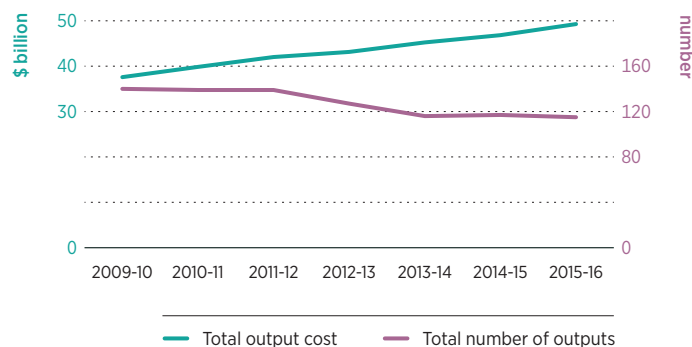


- best inform the department's own internal management decision making; and
- provide effective reporting to Parliament and stakeholders (for example Ministers, Cabinet and the public).

Departmental outputs may vary from year to year as a result of changes in the Government's priorities, machinery-of-government changes or departments' efforts to improve the performance measurement system.

There are 115 outputs in the 2015-16 budget papers. This is a reduction of two outputs compared to the 2014-15 Budget, although there have been significant changes to many outputs as a result of the machinery-of-government changes during 2014-15. Figure 10.5 shows the trend for the number of outputs from 2009-10 to 2015-16.

**Figure 10.5** Number and cost of outputs, 2009-10 to 2015-16 budgets



Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2009-10 to 2015-16.

The Committee notes that the total number of outputs decreased by 17.9 per cent between 2009-10 and 2015-16 (from 140 to 115 outputs). At the same time, the total output cost has increased by 26.3 per cent (from \$37.6 billion in 2009-10 to \$49.3 billion in 2015-16).<sup>709</sup>

In relation to this trend, the Minister for Finance indicated that:<sup>710</sup>

The capacity to make resource allocation decisions and hold departments to account is being reduced by poor specification of outputs and a gradual aggregation of activities into larger outputs ... There were about 350 outputs when Victoria first introduced output budgeting in 1997-98, appropriation has grown almost fourfold and the number of outputs reduced by more than half. The average value of an output is now \$351 million<sup>711</sup> compared to \$39 million in 1997-98. The Andrews government will review the service delivery and performance reporting framework to ensure outputs and performance measures are meaningful to the Parliament and the community.

<sup>709</sup> Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2009-10 to 2015-16.

<sup>710</sup> Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.2.

<sup>711</sup> This figure has been calculated by using the total appropriation figure (\$41,071.0 million) from the Appropriation (2014-2015) Bill 2014 and a total of 117 outputs delivered in 2014-15.

The Committee looks forward to the review indicated by the Minister for Finance. The Committee considers that this review has the potential to increase the transparency and accountability of the performance measurement system.

**FINDING 95:** The total number of outputs decreased by 17.9 per cent between 2009-10 and 2015-16, while the total cost of delivering outputs increased by 26.3 per cent. The Government has stated its intention to review outputs and performance measures.

### 10.3.4 Performance measures and targets

Performance measures and their targets specify what the Government expects departments to deliver each year.<sup>712</sup> They also form the basis of departmental reporting at the end of the year. As seen in Section 10.2.1, performance measures can also be used to assess the level of efficiency with which outputs are delivered by departments. In accordance with the Government's guidance, performance measures and their targets seek to measure four main aspects of departmental performance:

- the quantity of goods and services delivered
- the quality of goods and services delivered
- the timeliness of their delivery
- the cost of their delivery.

The Department of Treasury and Finance's guidance indicates that 'the mix of quality, quantity, timeliness and cost measures for each output should give a balanced and complete performance picture of what the output is trying to achieve and how the delivery of the output will be measured'.<sup>713</sup>

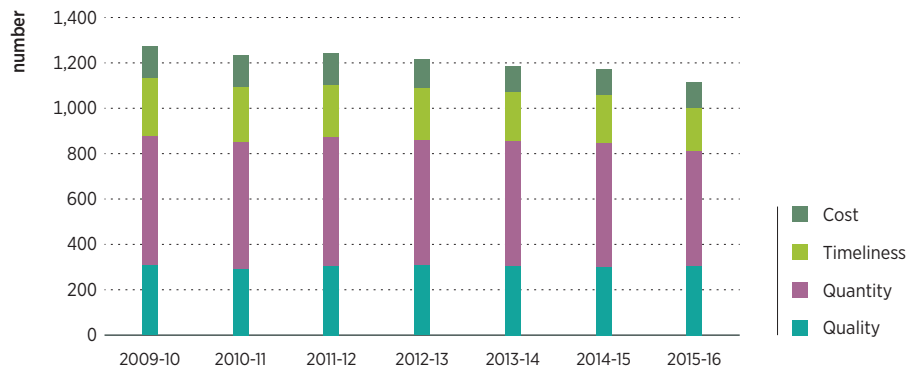
Government departments are required to review their performance measures to ensure that they remain relevant to departmental objectives (if they are not, they must be replaced or discontinued – see Section 10.5 of this chapter).<sup>714</sup> As with other key components of the performance measurement system, changes to performance measures are also made due to machinery-of-government changes, the establishment of different government priorities, changes to programs, and refinements and improvements to the system itself. While these changes are important, it is also desirable that performance measures keep some degree of consistency to ensure comparability over time.

The budget papers propose a total of 1,116 performance measures for 2015-16. Figure 10.6 shows the number of performance measures in each year from 2009-10 to 2015-16, including the composition of quantity, quality, timeliness and cost. Appendices A10.3-4 provide the composition of performance measures for each department in 2015-16.

712 Department of Treasury and Finance, *BFMG – 09: Output Specification and Performance Measures* (2012), p.113.

713 *ibid.*, p.114.

714 *ibid.*, p.110.

**Figure 10.6** Number of performance measures, 2009-10 to 2015-16

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: Service Delivery*, 2009-10 to 2015-16.

The Government has asked the Committee to assess the quality, quantity and timeliness measures proposed for discontinuation. The Committee agrees that most of the measures should be discontinued. However, the Committee considers that 45 of the proposed measures should not be discontinued (see Section 10.5 of this report).

If all of the proposed discontinuations occur, the total number of performance measures will have decreased by 12.5 per cent between 2009-10 and 2015-16 (from 1,275 to 1,116). During the same period, there has also been a shift in the proportions of the different types of measure, with the proportion of timeliness measures decreasing and the proportion of quality measures increasing.

As noted in Section 10.1, the Minister for Finance indicated that the Government will undertake a review of the performance measurement reporting framework. The Minister stated that:<sup>715</sup>

One of my key responsibilities is output performance measures. There is a need to review output measures ...

The Andrews government will review the service delivery and performance reporting framework to ensure outputs and performance measures are meaningful to the Parliament and the community.

The Committee looks forward to the results of this review.

### Quality performance measures

Quality performance measures are intended to ‘describe whether output delivery has been up to the expected standard of performance ... or if output delivery has met comparable better practice benchmarks associated with key objectives and intended results of services’.<sup>716</sup>

<sup>715</sup> Hon. Robin Scott MP, Minister for Finance, *2015-16 Budget Estimates Transcript of Evidence*, 14 May 2015, p.2.

<sup>716</sup> Department of Treasury and Finance, *BFMG - 09: Output Specification and Performance Measures* (2012), p.114.

Measuring the quality with which goods and services are delivered can be a tool to help departments achieve the desired impact on the community and can provide assurance to the Parliament and community about the standards of departmental performance. Therefore, the Committee believes that it is important for all outputs to have at least one measure that assesses whether the expected quality of the output has been met.

This issue was raised by the former Committee during the 57<sup>th</sup> Parliament<sup>717</sup> and the government of the day committed to having at least one quality measure in each output at that time.<sup>718</sup>

The Committee has identified eight outputs without any quality measures in the 2015-16 Budget (see Table 10.1).

**Table 10.1** Outputs without quality measures, 2015-16 Budget

Department	Outputs
Economic Development, Jobs, Transport and Resources	Tourism, Major Events and International Education
Health and Human Services	Acute Training and Development
	Aged Care Assessment
	Public Health Development, Research and Support
	Small Rural Services – Home and Community Care Services
	Small Rural Services – Primary Health
Premier and Cabinet	Business Environment Policy Advice
	Public Sector ICT and Digital Government

Source: Department of Treasury and Finance, *Budget Paper No.3: Service Delivery* (2015), Chapter 2.

The Committee notes that all of the outputs listed above for the Department of Health and Human Services were identified by the former Committee in earlier budgets as having no quality measures.<sup>719</sup> The other three outputs had quality measures in previous budgets but the departments have sought to discontinue them this year (see further discussion in Section 10.5).

These outputs represent \$531.8 million of funding in 2015-16. The Committee therefore considers it important that the quality of goods and services delivered through these outputs be measured and reported.

**FINDING 96:** Most outputs in the 2015-16 budget papers had at least one quality measure. However, there were eight outputs with no quality measures. These outputs have a total funding of \$531.8 million.

<sup>717</sup> Public Accounts and Estimates Committee, *Report on the 2011-12 Budget Estimates – Part Two* (2012), pp.19-21.

<sup>718</sup> Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 102<sup>nd</sup> Report on the 2011-12 Budget Estimates – Part Two*, tabled 7 February 2012, p.4.

<sup>719</sup> Public Accounts and Estimates Committee, *Report on the 2013-14 Budget Estimates – Part Two* (2013), p.143.

**RECOMMENDATION 62:** The Department of Treasury and Finance ensure that all outputs from all departments in future budget papers include quality measures.

### Quantity performance measures

Quantity performance measures ‘describe outputs in terms of how much, or how many’.<sup>720</sup> They are the most common type of measure, representing 45.2 per cent of all measures in 2015-16.<sup>721</sup> This type of performance measure allows the Parliament and community to understand the number of goods and services that the Government expects a department to deliver during the financial year.

Quantity measures often reflect the workload undertaken by a department. When looking at actual results, quantity measures can provide important contextual information for interpreting other measures. For example, if there are changes to the quality or timeliness with which services are delivered, understanding whether the quantity of services delivered increased or decreased can help the Parliament and community to understand the results.

Where quantity measures are provided for the same services that quality or timeliness measures report on, the performance measures may indicate if a department has improved the quality of its service delivery by reducing the number of services delivered. Alternatively, the performance measures may reveal that a drop in timeliness is a result of a higher demand than anticipated. Quantity measures may also indicate whether a department consistently underestimates or overestimates demand, which may be important in determining the appropriate level of funding in the future. However, without quantity measures, it would be difficult to see these scenarios.

As shown in Figure 10.2, performance measures can be used to assess departments’ efficiency by comparing the amount of funding to the service levels delivered. The quantity of goods and services delivered can be a key piece of information for this sort of assessment.

The Committee is disappointed to see that, with the 2015-16 Budget, the Department of Treasury and Finance has proposed discontinuing all quantity measures from four outputs. In addition, a new output has been created in the Department of Economic Development, Jobs, Transport and Resources with no quantity measures. As a result, there are five outputs that do not have any quantity measures in the 2015-16 budget papers (see Table 10.2). The total funding for these outputs in 2015-16 is \$46.5 million.

<sup>720</sup> Department of Treasury and Finance, *BFMG – 09: Output Specification and Performance Measures* (2012), p.114.

<sup>721</sup> Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2.

**Table 10.2** Outputs without quantity measures, 2015-16 Budget

Department	Outputs
Economic Development, Jobs, Transport and Resources	Industrial Relations
Treasury and Finance	Economic and Financial Policy
	Budget and Financial Policy Advice
	Financial and Resource Management Frameworks Maintenance and Support
	Financial Reporting

Source: Department of Treasury and Finance, *Budget Paper No.3: Service Delivery* (2015), Chapter 2.

The Department of Treasury and Finance indicated to the Committee that its reasons for proposing the discontinuation of measures were based on:<sup>722</sup>

... two main themes:

- Counting advice to Government is not a useful measure of the worth of that advice, and assessing it as part of an objective indicator is a better approach; and
- Timeliness or quality measures for a specific quantity of outputs imply the same information as a quantity measure.

The Committee acknowledges that there are limitations to quantity measures and that quality and timeliness measures are also very important. However, the Committee considers that quantity measures provide important information that is not provided by other types of measure. As discussed above, quantity measures are particularly useful for assessing the efficiency of output delivery and providing contextual information. The Committee therefore considers that all outputs should have at least one associated quantity measure.

As part of its review of the performance measures (see Section 10.5 of this chapter), the Committee has not agreed with the discontinuation of the quantity measures for these outputs for the Department of Treasury and Finance. Though the Committee acknowledges that there are deficiencies with a number of the measures proposed for discontinuation by the Department, the Committee does not consider that having no measures of the workload for these outputs is an appropriate solution. The Committee has therefore recommended that these measures be retained until more appropriate measures are developed.

As part of the review of performance measures noted by the Minister for Finance, the Department of Treasury and Finance may wish to consider guidance and rules relating to the appropriate mix of performance measures types in outputs.

**FINDING 97:** Quantity measures represent 45.2 per cent of the performance measures in 2015-16. However, there are five outputs without any quantity measures in the 2015-16 Budget. This includes four outputs from the Department of Treasury and Finance.

<sup>722</sup> Correspondence from David Martine, Secretary, Department of Treasury and Finance, to Chair, Public Accounts and Estimates Committee, received 1 September 2015.

**RECOMMENDATION 63:** The Department of Treasury and Finance ensure that all outputs from all departments in future budget papers include quantity measures. These quantity measures should relate to the same goods and services that are reported on by the other measures in the output.

**RECOMMENDATION 64:** As part of the review of the performance measurement framework indicated by the Minister for Finance, the Department of Treasury and Finance establish guidelines to ensure that each output has an appropriate mix of quality, quantity, timeliness and cost performance measures.

### Demand measures

As noted above, quantity measures often reflect the amount of work being undertaken by a department. In some cases, a department's or agency's workload may be heavily influenced by external demand (such as the number of patients presenting at a hospital or the number of court cases).

Some departments have expressed concern about having performance measures that are not within the department's control. For example, Courts Services Victoria indicated to the Committee:<sup>723</sup>

The revenue certification process includes an assessment by DTF [the Department of Treasury and Finance] of whether the agreed outputs have been delivered and agreed targets specified in the budget papers have been met. It is not considered appropriate to set disposal targets for the jurisdictions in an environment where they do not control demand. Setting a target figure for the number of disposals conceptually suggests that the jurisdictions should seek out additional cases if demand declines, which is clearly inappropriate and I am sure not reflective of the intention of the Parliament or the Committee.

The Department of Premier and Cabinet similarly sought to discontinue some of its performance measures because they reflected factors outside its control. For example, the Department's explanations for discontinuing some measures include:<sup>724</sup>

- The number of requests varies according to the legislative program, as well as government and departments' priorities therefore the office does not have the control over the number of requests...
- The number of Statutory Rules made and Bills prepared and introduced by departments into Parliament is set by the legislative program, as well as government and department priorities...
- The Ombudsman has no control over the number of complaints it receives, which is closely linked to the number of complaints it finalises...

<sup>723</sup> Correspondence from Michael Carroll, Acting Chief Executive Officer, Courts Services Victoria, to Chair, received 31 August 2015.

<sup>724</sup> Correspondence from Chris Eccles, Secretary, Department of Premier and Cabinet, to Chair, received 10 September 2015.

The Committee acknowledges that the Department of Treasury and Finance's guidance states the performance measures should only relate to things primarily within departments' control.<sup>725</sup> However, in practice, there are many performance measures which primarily reflect external demand and are not under the departments' control. This has been the case for many years.

The Committee considers that these measures are valuable, as they often supply important information about a department's workload. As discussed earlier in this section, that information can be valuable in a number of ways. During the 57<sup>th</sup> Parliament, the former Committee recommended that a separate category of performance indicator, to be called 'demand measures', should be introduced to the performance measurement and reporting system to explicitly allow for this type of measure.<sup>726</sup> At the last update, this recommendation was 'under review'.<sup>727</sup>

The current committee confirms its support for this new category of measure. By establishing these measures as a separate type, it would be easy for the Department of Treasury and Finance to exclude this category of measure from the revenue certification process. This would meet the concerns of Court Services Victoria quoted above.

## 10.4 Performance reporting for new initiatives

The Department of Treasury and Finance indicates that 'changes, such as new initiatives and new funding, must be reflected by changes in performance measures and/or targets'.<sup>728</sup> Previous guidance from the Department has required performance measures for every major new initiative released in a budget.<sup>729</sup>

The Committee sought details from departments on performance measures that were affected by new initiatives (both output and asset initiatives) worth \$20 million or more in the 2015-16 Budget.

In most cases, departments were able to demonstrate appropriate performance measures related to the new initiatives. Table 10.3 below shows some examples of these connections.

The Department of Premier and Cabinet indicated that all of its new initiatives have performance measures associated with them.<sup>730</sup> The Department of Justice and Regulation indicated that all but one initiative have performance measures

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- 725 Department of Treasury and Finance, *BFMG - 09 Output Specification and Performance Measures* (2012), p.115.
- 726 Public Accounts and Estimates Committee, *Review of the Performance Measurement and Reporting System* (2014), Recommendation 24, p.53.
- 727 Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 118<sup>th</sup> Report to Parliament - Review of the Performance Measurement and Reporting System*, tabled 18 September 2014, p.11.
- 728 Department of Treasury and Finance, *BFMG - 09: Output Specification and Performance Measures* (2012), p.117.
- 729 Department of Treasury and Finance, *Budget Papers Guidance - General Government Sector (Budget Papers and Estimates Update)*, n.d., p.3; Department of Treasury and Finance, *Information Request No.11-23: 2012-13 Departmental Performance Statements for Publication in the Budget Papers* (2011), p.3.
- 730 Department of Premier and Cabinet, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.19.



associated with them. For the remaining initiative, the Department noted that it was 'not possible to identify specific performance measures that [the] initiative contributes to'.<sup>731</sup> Three departments indicated that the query was not applicable to them.<sup>732</sup>

**Table 10.3** Performance measures related to new initiatives released in the 2015-16 Budget

Department	Initiative	Related performance measures
Department of Premier and Cabinet	Promoting social cohesion and community harmony (\$20.7 million over four years)	<ul style="list-style-type: none"> <li>• Consultations with culturally and linguistically diverse (CALD) communities</li> <li>• Attendance at Cultural Diversity Week flagship event, Viva Victoria</li> <li>• Proportion of grants approved which are provided to organisations in regional/rural areas</li> <li>• Event briefs completed within the required timeframe</li> </ul>
Department of Justice and Regulation	Expanding Community Correctional Services to meet demand	<ul style="list-style-type: none"> <li>• Average daily offenders under community based supervision</li> <li>• Community work hours performed</li> <li>• Offenders with a supervised order that has been successfully completed (note this was subsequently disaggregated)</li> <li>• Offenders with a treatment or personal development program condition who have been appropriately referred to a program within set time frames</li> </ul>
Department of Economic Development, Jobs, Transport and Resources	Future Industries Fund (including New Energy Jobs Fund)	<ul style="list-style-type: none"> <li>• Companies supported by Future Industries Fund</li> <li>• Future industry sector strategies delivered</li> <li>• Industry roundtables and engagement forums</li> <li>• Proportion of all international students studying in Victoria</li> </ul>
	Regional Jobs and Infrastructure Fund	<ul style="list-style-type: none"> <li>• Actual export sales generated for regional businesses as a result of participation in government programs</li> <li>• Economic development and service delivery projects supported</li> <li>• Employment in regional Victoria resulting from government investment facilitation services and assistance</li> <li>• New investment in regional Victoria resulting from government facilitation services and assistance</li> <li>• Participant satisfaction with implementation of Regional Development Victoria programs</li> <li>• Access to diverse range of supported projects: regional Touring Victoria destinations</li> <li>• Diverse range of product, producers and cultural venues supported: organisations recurrently funded</li> <li>• Diverse range of product, producers and cultural venues supported: regionally based organisations recurrently funded</li> <li>• Diverse range of product, producers and cultural venues supported: project companies and artists funded</li> <li>• Diverse range of product, producers and cultural venues supported: project companies and artists funded which are regionally based</li> </ul>

Source: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.

<sup>731</sup> Department of Justice and Regulation, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 11 July 2015, p.38.

<sup>732</sup> The Department of Treasury and Finance, the Parliamentary Departments and Courts Services Victoria.

The remaining four departments<sup>733</sup> reported that a total of 40 new initiatives worth more than \$20 million each were released as part of the 2015-16 Budget with no associated performance measures other than output costs (see Appendix A10.5).

The Committee believes that major new initiatives should have performance measures (either new or existing measures) associated with them to reflect the initiatives' desired outcomes and to allow the Parliament and the community to assess the initiatives' progress over time.

**FINDING 98:** For many new initiatives, departments were able to detail the performance measures which will reflect the impact of the initiative in future years. For 41 new initiatives worth at least \$20 million (both output and asset initiatives), departments were unable to identify any associated performance measures other than output costs in the 2015-16 budget papers.

**RECOMMENDATION 65:** The Department of Treasury and Finance ensure that all initiatives (worth above \$20 million) in future budget papers have at least one associated performance measure other than output cost.

## 10.5 Discontinued performance measures

Since 2011, the Committee has been asked to comment each year on the non-cost measures proposed for discontinuation in the Budget. As the 2015-16 budget papers state, 'performance measures are assessed annually by the Public Accounts and Estimates Committee for their continuing relevance and robustness'.<sup>734</sup>

The Government has identified five criteria which indicate when it is appropriate to substantially change or discontinue a performance measure:<sup>735</sup>

- where a current measure can be replaced by a more appropriate measure and the new measure will provide significantly more meaningful information to the Parliament and the public;
- it is no longer relevant due to a change in Government policy or priorities and/or departmental objectives;
- milestones, projects or programs have been completed, substantially changed, or discontinued;
- funding is not provided in the current budget for the continuation of the initiative; and
- Parliament and the public can judge the success of output delivery without the measure.

<sup>733</sup> The Department of Economic Development, Jobs, Transport and Resources, the Department of Environment, Land, Water and Planning, the Department of Education and Training, and the Department of Health and Human Services.

<sup>734</sup> Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.353.

<sup>735</sup> Department of Treasury and Finance, *BFMG - 09: Output Specification and Performance Measures* (2012), pp.117-18.

The Committee accepts these as good general principles and has used these in making its assessment.

The 2015-16 Budget proposes discontinuing 258 non-cost performance measures (24.4 per cent).<sup>736</sup> This is larger than previous budgets (over the last four budgets, the number has ranged from 86 to 194).

Two departments proposed particularly large reductions in 2015-16:

- the Department of Premier and Cabinet proposed discontinuing 76 non-cost measures and introducing 32 new measures, taking its total from 109 to 65 (a 40.4 per cent reduction)
- the Department of Treasury and Finance proposed discontinuing 33 non-cost measures, while only introducing 5 new measures, taking its total from 80 to 52 (a 35.0 per cent reduction).

A total of 202 new non-cost measures were created with the budget, leading to an overall reduction of non-cost measures by 56 (5.3 per cent). This continues a trend which has occurred for some time to reduce the number of performance measures each year (see Section 2.3.3).

### 10.5.1 Committee's review

The Committee recommends that measures should be re-instated where:

- the activity assessed by the performance measure is in the public interest and not measured by other measures
- the new measures are less clear than the measures proposed for discontinuation
- the removal of the performance measures would lead to a less comprehensive measurement of the departments' activities (by no longer providing information about certain activities)
- removing the proposed measures would leave the output with no quality measures
- removing the proposed measures would leave the output with no quantity measures
- the measures provide information about the workload of the department, which is important contextual information for understanding the department's performance and its level of efficiency.

Some of the concerns underlying this approach are discussed in more detail in Section 10.3.4 of this chapter.

<sup>736</sup> In addition, 27 cost measures have been discontinued, taking the total number of discontinued measures to 285. The Committee has not been asked to comment on the cost performance measures.

## Results of the review

The Committee assessed the 258 non-cost performance measures proposed to be discontinued and sought further clarification details in relation to 61 of these measures.

After assessing the information in the budget papers and the further details provided by departments, the Committee considers that 45 of the proposed measures should be retained (see Table 10.4). The Committee's reasons for retaining these measures are detailed in Appendix A10.6.

**Table 10.4** Performance measures proposed to be discontinued in the 2015-16 Budget which the Committee considers should be retained

Output	Performance measure
<b>DEPARTMENT OF ECONOMIC DEVELOPMENT, JOBS, TRANSPORT AND RESOURCES</b>	
Industry and Enterprise Innovation	Number of major research and evaluation projects completed
Tourism, Major Events and International Education	Value of media coverage generated: domestic
	Value of media coverage generated: international
	Victoria's share of domestic tourism advertising awareness among target markets: interstate
	Victoria's share of domestic tourism advertising awareness among target markets: intrastate
Transport Safety, Security and Emergency Management	Transport safety regulation: rail safety audits/compliance inspections conducted in accordance with legislative requirements
Sustainably Manage Fish, Game and Forest Resources	Minimum number of uniformed fisheries officers maintaining operational coverage for priority fishing activity periods, as defined by the Compliance Strategic Assessment
Taxi and Hire Vehicle Services	Taxis and hire vehicles conform to safety and quality standards
<b>DEPARTMENT OF JUSTICE AND REGULATION</b>	
Gambling and Liquor Regulation and Racing Industry Development	Liquor and gambling compliance inspection outcomes provided within set timeframes (VCGLR)
<b>DEPARTMENT OF PREMIER AND CABINET</b>	
Arts Portfolio Agencies	Public Record Office Victoria: Records transferred
	Public Record Office Victoria: digital records preserved
Anti-Corruption and Public Sector Integrity	Corruption prevention initiatives delivered by IBAC
Chief Parliamentary Counsel Services	Advice given on legislation in response to written requests
	Statutory Rules made and Bills prepared and introduced into Parliament
Freedom of Information (FOI) Commissioner	Education and training activities delivered by FOI Commissioner
Ombudsman services	Jurisdictional complaints finalised (VO)
	Proportion of jurisdictional complaints where the original outcome is set aside by a review undertaken in accordance with the Ombudsman's internal review policy

<b>Output</b>	<b>Performance measure</b>
Aboriginal Community and Cultural Development	Clients service contacts for members of the Stolen Generations with Connecting Home Limited
	Client service contacts for members of the Stolen Generations with the Victorian Koorie Family History Service
Multicultural Affairs and Citizenship	Grants approved
Office of Women's Affairs	Number of women participating in funded programs, projects and events
<b>DEPARTMENT OF TREASURY AND FINANCE</b>	
Budget and Financial Policy Advice	Budget and financial policy advice through Ministerial briefs, Budget and Expenditure Review Committee and Cabinet Sub-Committee briefs
	Cost control and efficiency reviews
Financial Reporting	Estimates reporting – Budget, Budget Update and Pre-Election Budget Update
	Financial Reporting – Annual Financial Report, Mid-Year Financial Report and Quarterly Financial Reports
Financial and Resource Management Frameworks Maintenance and Support	Annual review of whole of government compliance framework
	Delivery of updates, guides and newsletters
	Review of major resource management policies
Economic and Financial Policy	Briefings on Cabinet submissions
	Written Ministerial briefs
	Long-term research projects completed
	Long-term research projects managed within agreed timeframes
GBE Performance Monitoring and Financial Risk Management	Annual performance and compliance review of registered housing agencies
	Corporate plans reviewed and assessed and quarterly performance reports
	Provide financial policy advice on borrowings, investments, insurance, and superannuation issues and prudential supervision
<b>COURTS</b>	
Courts	Civil matters disposed in the Supreme Court
	Civil matters disposed in the County Court
	Civil matters disposed in the Magistrates' Court
	Civil matters disposed in the Victorian Civil and Administrative Tribunal
	Child protection matters disposed in the Children's Court
	Coronial matters disposed in the Coroner's Court
	Criminal matters disposed in the Supreme Court
	Criminal matters disposed in the County Court
	Criminal matters disposed in the Magistrates' Court
	Criminal matters disposed in the Children's Court

Source: Public Accounts and Estimates Committee.

The Committee acknowledges that there are limitations to some of the performance measures that it has recommended be retained. In these cases, the Committee has disagreed with the proposed discontinuation because no equivalent new measure has been created. The Committee considers that the performance measurement system should be improved by replacing such measures with better ones, rather than simply eliminating the measures and no longer reporting on those aspects of service delivery.

The Committee would be willing to support the discontinuation of these measures in the future if new, better measures of those aspects of service delivery were introduced. This has been indicated in the comments in Appendix A10.6.

**FINDING 99:** The Government proposed discontinuing 258 non-cost performance measures with the 2015-16 Budget. The Committee has reviewed these performance measures and considers that 45 of these measures should be retained.

**RECOMMENDATION 66:** The Government not discontinue the measures listed in Table 10.4 of this report.

# 11 The Government's responses to the former Committee's *Report on the 2014-15 Budget Estimates*

## 11.1 Introduction

The Public Accounts and Estimates Committee of the 57<sup>th</sup> Parliament tabled its *Report on the 2014-15 Budget Estimates* in two parts during 2014. The report included seven recommendations.

The Government responded to these recommendations in October 2014 and April 2015.<sup>737</sup>

This chapter explores:

- How did the Government respond to the recommendations? (Section 11.2)
- What progress has been made at implementing the recommendations to date? (Section 11.3)

This chapter also looks at the *Guidelines for Submissions and Responses to Inquiries*. These guidelines date from 2002 and the former Committee made a number of recommendations about ways that these could be improved. Section 11.4 discusses this issue further, noting that the guidelines have not yet been updated.

## 11.2 Responses to the recommendations

Of the seven recommendations in the *Report on the 2014-15 Budget Estimates*, the Government:

- supported four
- supported two 'in principle'
- indicated that it was 'awaiting PAEC response' for one.

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<sup>737</sup> Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 120<sup>th</sup> Report to Parliament – Report on the 2014-15 Budget Estimates – Part One*, tabled 15 October 2014; Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 120<sup>th</sup> Report to Parliament – Report on the 2014-15 Budget Estimates – Part Two*, tabled 15 April 2015.

The Government was awaiting the Committee's response regarding a recommendation about performance measures. Further correspondence between the Committee and the Government has taken place since that time and the Government is still considering the latest advice from the Committee.

### 11.3 Implementation of the recommendations

The Committee asked the Department of Treasury and Finance about its progress at implementing the recommendations that were supported or supported in principle. The Department indicated that all six had been implemented.<sup>738</sup>

The Committee also conducted its own assessment. The Committee considers that:

- three recommendations have been implemented
- one has been partially implemented
- one has not been implemented
- it is too soon to tell with one.

The recommendation that has been partially implemented was to publish historical figures for the item 'public private partnership (PPP) infrastructure investment'. In explaining why the Department of Treasury and Finance considers that recommendation to be implemented, the Department noted that historical figures for 'government infrastructure investment', which includes PPP infrastructure investment, have been published.<sup>739</sup> The Committee acknowledges that this would give a knowledgeable reader of the budget papers some indication of the value of PPP infrastructure investment. However, as government infrastructure investment also includes an amount representing 'other commercially sensitive items',<sup>740</sup> it would be impossible to calculate an exact figure for PPP infrastructure investment based on the data in the budget papers. The Committee notes that the Government's support for this recommendation was only 'in principle'.<sup>741</sup>

The recommendation that has not been implemented related to the glossary included in Budget Paper No.4. The former Committee made a number of recommendations in various inquiries about that glossary. Several of these recommendations relate to the use of a wide variety of terms for asset investment in the budget papers. Some of these terms are used interchangeably, while

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738 Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.29-31.

739 *Ibid.*, p.30.

740 Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), p.12.

741 Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 120<sup>th</sup> Report to Parliament – Report on the 2014-15 Budget Estimates – Part Two*, tabled 15 April 2015, p.2.



some have distinct meanings. However, for several terms which are used interchangeably, the glossary in Budget Paper No.4 defines the terms in different ways, suggesting that different meanings are intended when they are not.<sup>742</sup>

Recommendation 6 in the *Report on the 2014-15 Budget Estimates* was that:<sup>743</sup>

The Department of Treasury and Finance continue to refine the definitions in Budget Paper No.4 (State Capital Program) to ensure that terms which are used interchangeably are not defined differently.

The Department of Treasury and Finance indicated that this had been implemented, stating that, 'The required information was included in the 2015-16 Budget Papers'.<sup>744</sup> However, apart from the addition of two extra terms, the definitions in Budget Paper No.4 were exactly the same in the 2015-16 budget papers as they were in the previous year.<sup>745</sup> The concerns expressed by the Committee of the last Parliament have not been addressed in any way.

The Committee considers that it is too soon to confirm whether or not one recommendation has been implemented, as it relates to the Financial Report for the State, which has not yet been tabled. The Department of Treasury and Finance indicated that, 'The next Annual Financial Report due for release in October 2015 will demonstrate implementation.'<sup>746</sup> The Committee will reassess the status of this recommendation following the tabling of the Financial Report.

**FINDING 100:** Of the six recommendations from the *Report on the 2014-15 Budget Estimates* that were supported or supported in principle, the Committee considers that three have been fully implemented, one has been partially implemented and one has not been implemented. It is too soon to tell whether or not one recommendation has been implemented. The one that has not been implemented related to the definitions included in Budget Paper No.4.

**RECOMMENDATION 67:** The Department of Treasury and Finance review previous recommendations made by the Public Accounts and Estimates Committee about the glossary in Budget Paper No.4 (*State Capital Program*) and improve the definitions. This should include not providing different definitions for terms that are used interchangeably.

<sup>742</sup> Public Accounts and Estimates Committee, *Report on the 2013-14 Budget Estimates – Part Two* (2013), p.172.

<sup>743</sup> Public Accounts and Estimates Committee, *Report on the 2014-15 Budget Estimates – Part Two* (2014), Recommendation 6, p.110.

<sup>744</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.31.

<sup>745</sup> Department of Treasury and Finance, *Budget Paper No.4: 2014-15 State Capital Program* (2014), p.137; Department of Treasury and Finance, *Budget Paper No.4: 2015-16 State Capital Program* (2015), pp.119-20.

<sup>746</sup> Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.29.

## 11.4 The review of the guidelines for responses to inquiries

In 2002, the Department of Premier and Cabinet issued *Guidelines for Submissions and Responses to Inquiries*. These were 'designed to aid officials who are considering preparing a submission or response to a parliamentary inquiry or other statutory or non-statutory inquiry'.<sup>747</sup> In 2013, the Government of the day indicated that it intended to review these guidelines. As part of this review, the Government indicated that it would consider providing more detailed guidance about responding to parliamentary committees and establishing guidelines related to the implementation of recommendations.<sup>748</sup>

The former Committee made a number of recommendations that could be considered as part of this review (see Appendix A11.1).

The Department of Premier and Cabinet indicated in May 2014 that the review was in progress and was expected to be completed in late 2014.<sup>749</sup>

The Committee notes that the 2002 guidelines remain on the Department of Premier and Cabinet's website and no updated version appears to have been issued. The Committee considers that responding to committee recommendations and reporting on the implementation of recommendations are important from a transparency and accountability perspective. As the previous Committee identified, updating the guidelines has the potential to enhance the operation of the parliamentary committees system.

**FINDING 101:** The current guidelines for responses to parliamentary inquiries date from 2002. The previous government intended to review the guidelines but this review appears not to have been completed. The former Public Accounts and Estimates Committee made a number of recommendations regarding matters that could be considered as part of the review.

**RECOMMENDATION 68:** The Government complete the review and update of the *Guidelines for Submissions and Responses to Inquiries*. As part of this review, the Government consider the recommendations of the previous Public Accounts and Estimates Committee outlined in Appendix A11.1 of this report.

<sup>747</sup> Department of Premier and Cabinet, *Guidelines for Submissions and Responses to Inquiries* (2002), p.6.

<sup>748</sup> Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 111<sup>th</sup> Report to Parliament – Report on the 2012-13 Budget Estimates – Part Two*, tabled 12 March 2013, pp.24-5; Victorian Government, *Government Responses to the Recommendations of Public Accounts and Estimates Committee's 116<sup>th</sup> Report to Parliament – Report on the 2013-14 Budget Estimates – Part Two*, tabled 16 April 2014, pp.13-14.

<sup>749</sup> Department of Premier and Cabinet, *Response to the Committee's 2014-15 Budget Estimates General Questionnaire*, received 7 May 2014, p.23.

# Appendix 1

## Introduction

### A1.1 Return dates of the 2015-16 Budget Estimates General Questionnaire (distributed on 5 May 2015)

Department	Due date	Extension granted until	Received
Economic Development, Jobs, Transport and Resources	12 June 2015	-	15 June 2015
Education and Training	12 June 2015	-	16 June 2015 <sup>(a)</sup>
Environment, Land, Water and Planning	12 June 2015	22 June 2015	22 June 2015
Health and Human Services	12 June 2015	26 June 2015	26 June 2015 <sup>(b)</sup>
Justice and Regulation	12 June 2015	-	11 June 2015
Premier and Cabinet	12 June 2015	-	12 June 2015
Treasury and Finance	12 June 2015	-	12 June 2015
Parliament	12 June 2015	-	12 June 2015
Courts	12 June 2015	-	11 June 2015

(a) Resubmitted with minor amendments on 7 August 2015.

(b) Resubmitted with minor amendments on 7 October 2015.

Source: Public Accounts and Estimates Committee.

### A1.2 Return dates of the 2015-16 Budget Estimates Specific Questionnaire (distributed on 3 July 2015)

Department	Due date	Extension granted until	Received
Economic Development, Jobs, Transport and Resources	7 August 2015	-	6 August 2015
Environment, Land, Water and Planning	7 August 2015	-	12 August 2015
Health and Human Services	7 August 2015	-	7 August 2015
Premier and Cabinet	7 August 2015	-	17 August 2015
Treasury and Finance	7 August 2015	-	19 August 2015
Parliament	7 August 2015	-	4 August 2015

Source: Public Accounts and Estimates Committee.

## A1.3 Return dates of questions on notice from the 2015-16 budget estimates hearings (distributed on 17 June 2015)

Portfolio	Due date	Extension granted until	Received
Aboriginal Affairs	8 July 2015		13 July 2015
Ambulance Services	8 July 2015	7 August	5 August 2015
Corrections	8 July 2015		8 July 2015
Education	8 July 2015		9 July 2015
Employment	8 July 2015		10 July 2015
Environment, Climate Change and Water	8 July 2015		22 July 2015
Families and Children	8 July 2015		8 July 2015
Finance	8 July 2015		6 July 2015
Health	8 July 2015	7 August	5 August 2015
Housing, Disability and Ageing	8 July 2015		10 July 2015
Industrial Relations	8 July 2015		13 July 2015
Industry	8 July 2015		13 July 2015
Mental Health	8 July 2015		10 July 2015
Multicultural Affairs	8 July 2015		6 July 2015
Police	8 July 2015		8 July 2015
Premier	8 July 2015		1 July 2015
Prevention of Family Violence	8 July 2015	20 July 2015	17 July 2015
Public Transport	8 July 2015		10 July 2015
Regional Development	8 July 2015		7 July 2015
Small Business, Innovation and Trade	8 July 2015		1 July 2015
Training and Skills	8 July 2015		29 June 2015
Treasurer	8 July 2015		25 June 2015
Tourism and Major Events	8 July 2015		2 September 2015
Veterans	8 July 2015		26 June 2015

Source: Public Accounts and Estimates Committee.

## A1.4 Changes to portfolios

Portfolios at the 2014-15 Budget	Portfolios at the 2015-16 Budget
Aboriginal Affairs	Aboriginal Affairs
Ageing	Agriculture
Agriculture and Food Security	Ambulance Services
Assistant Treasurer	Attorney-General
Attorney-General	Consumer Affairs, Gaming and Liquor Regulation
Aviation Industry	Corrections
Bushfire Response	Creative Industries
Children and Early Childhood Development	Education
Community Services	Emergency Services
Consumer Affairs	Employment
Corrections	Energy and Resources
Crime Prevention	Environment, Climate Change and Water
Disability Services and Reform	Equality
Education	Families and Children
Employment and Trade	Finance
Energy and Resources	Health
Environment and Climate Change	Housing, Disability and Ageing
Finance	Industrial Relations
Health	Industry
Higher Education and Skills	Local Government
Housing	Mental Health
Industrial Relations	Multicultural Affairs
Innovation	Planning
Liquor and Gaming Regulation	Police
Local Government	Ports
Major Projects	Premier
Manufacturing	Prevention of Family Violence
Mental Health	Public Transport
Multicultural Affairs and Citizenship	Racing
Planning	Regional Development
Police and Emergency Services	Roads and Road Safety
Ports	Small Business, Innovation and Trade
Premier	Special Minister of State
Public Transport	Sport
Racing	Tourism and Major Events
Regional and Rural Development	Training and Skills
Regional Cities	Treasurer
Roads	Veterans
Small Business	Women
Sport and Recreation	Youth Affairs
State Development	
Technology	
The Arts	
Tourism and Major Events	
Treasurer	
Veterans' Affairs	
Water	
Women's Affairs	
Youth Affairs	

Source: Public Accounts and Estimates Committee.



# Appendix 2

## Key aspects of the 2015-16 Budget

### A2.1 Components of the general government sector operating statement going to or coming from the PNFC sector

	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)
<b>General government sector revenue coming from the PNFC sector</b>				
Taxation revenue	243.8	209.8	212.1	230.4
Interest revenue	472.8	468.8	465.0	460.5
Dividends	215.6	195.6	182.7	216.6
Income tax equivalent and local government rate equivalent revenue	150.6	125.9	162.2	186.5
Grants	5.3	2.3	2.3	2.3
Sales of goods and services – inter-sector capital assets charge	1,751.8	1,901.6	1,949.2	1,971.2
Sales of goods and services – provision of services	303.7	228.9	194.2	195.6
<b>Total revenue from the PNFC sector</b>	<b>3,143.6</b>	<b>3,132.9</b>	<b>3,167.7</b>	<b>3,263.1</b>
<b>General government sector expenses going to the PNFC sector</b>				
Grants and other transfers	2,943.0	3,041.7	3,107.0	3,110.8
Other operating expenses – purchase of supplies and consumables	0.2	0.3	0.3	0.2
Other operating expenses – purchase of services	348.1	294.2	193.6	100.8
<b>Total expenses going to PNFC sector</b>	<b>3,291.3</b>	<b>3,336.2</b>	<b>3,300.9</b>	<b>3,211.8</b>
<b>Net flow from the general government sector to the PNFC sector</b>	<b>147.7</b>	<b>203.3</b>	<b>133.2</b>	<b>-51.3</b>

Source: Adapted from Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.45-6.

## A2.2 Components of the general government sector operating statement going to or coming from the PFC sector

	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)
<b>General government sector revenue coming from the PFC sector</b>				
Taxation revenue	18.8	19.2	19.6	20.1
Interest revenue	111.4	121.9	134.1	134.2
Dividends	619.5	522.2	530.7	343.9
Income tax equivalent and local government rate equivalent revenue	207.5	238.1	252.1	236.3
Sales of goods and services – provision of services	341.1	341.0	342.8	348.3
<b>Total revenue from the PFC sector</b>	<b>1,298.3</b>	<b>1,242.4</b>	<b>1,279.3</b>	<b>1,082.8</b>
<b>General government sector expenses going to the PFC sector</b>				
Interest expense	1,237.6	1,117.2	1,144.4	1,102.2
Other operating expenses – purchase of services	490.2	520.5	552.3	585.3
<b>Total expenses going to PFC sector</b>	<b>1,727.8</b>	<b>1,637.7</b>	<b>1,696.7</b>	<b>1,687.5</b>
<b>Net flow from the general government sector to the PFC sector</b>	<b>429.5</b>	<b>395.3</b>	<b>417.4</b>	<b>604.7</b>

Source: Adapted from Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, pp.45-6.



# Appendix 3

## Economic overview

### A3.1 Estimated and actual growth rates for real gross state product,<sup>(a)</sup> 2004-05 to 2013-14 budgets

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Budget year estimate <sup>(b)</sup>	3.25	3.00	0.25	3.25	3.00	1.75	2.25
Actual	3.20	0.80	2.00	2.50	2.30	1.60	1.70
Variation between budget year estimate and actual	-0.05	-2.20	1.75	-0.75	-0.70	-0.15	-0.55
Average variation between budget year estimate and actual				-0.38			
Earliest budget estimate <sup>(c)</sup>	3.50	3.25	3.25	3.00	3.00	3.00	3.00
Actual	3.20	0.80	2.00	2.50	2.30	1.60	1.70
Variation between earliest estimate and actual	-0.30	-2.45	-1.25	-0.50	-0.70	-1.40	-1.30
Average variation between earliest estimate and actual				-1.13			

(a) Annual percentage change compared with the previous year.

(b) That is, the estimate made in the budget immediately preceding the start of the financial year (the estimate in the 2007-08 budget papers for 2007-08, the estimate in the 2008-09 budget papers for 2008-09 and so on).

(c) That is, the estimate made three years in advance (the estimate in the 2004-05 budget papers for 2007-08, the estimate in the 2005-06 budget papers for 2008-09 and so on).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

### A3.2 Estimated and actual growth rates for population,<sup>(a)</sup> 2004-05 to 2013-14 budgets

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Budget year estimate <sup>(b)</sup>	1.20	1.50	1.60	1.90	1.50	1.60	1.70
Actual	1.80	2.20	1.80	1.50	1.60	1.90	1.90
Variation between budget year estimate and actual	0.60	0.70	0.20	-0.40	0.10	0.30	0.20
Average variation between budget year estimate and actual				0.24			
Earliest budget estimate <sup>(c)</sup>	1.00	1.00	1.00	1.20	1.40	1.40	1.70
Actual	1.80	2.20	1.80	1.50	1.60	1.90	1.90
Variation between earliest estimate and actual	0.80	1.20	0.80	0.30	0.20	0.50	0.20
Average variation between earliest estimate and actual				0.57			

(a) Percentage change over the year to 30 June.

(b) That is, the estimate made in the budget immediately preceding the start of the financial year (the estimate in the 2007-08 budget papers for 2007-08, the estimate in the 2008-09 budget papers for 2008-09 and so on).

(c) That is, the estimate made three years in advance (the estimate in the 2004-05 budget papers for 2007-08, the estimate in the 2005-06 budget papers for 2008-09 and so on).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

### A3.3 Estimated and actual growth rates for employment,<sup>(a)</sup> 2004-05 to 2013-14 budgets

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Budget year estimate <sup>(b)</sup>	1.25	1.50	-1.00	2.00	1.75	0.25	1.5
Actual	2.70	0.20	2.80	3.50	0.80	0.80	0.60
Variation between budget year estimate and actual	1.45	-1.30	3.80	1.50	-0.95	0.55	-0.90
Average variation between budget year estimate and actual				0.59			
Earliest budget estimate <sup>(c)</sup>	1.50	1.25	1.25	1.25	1.50	1.50	1.75
Actual	2.70	0.20	2.80	3.50	0.80	0.80	0.60
Variation between earliest estimate and actual	1.20	-1.05	1.55	2.25	-0.70	-0.70	-1.15
Average variation between earliest estimate and actual				0.20			

(a) Annual percentage change compared with the previous year.

(b) That is, the estimate made in the budget immediately preceding the start of the financial year (the estimate in the 2007-08 budget papers for 2007-08, the estimate in the 2008-09 budget papers for 2008-09 and so on).

(c) That is, the estimate made three years in advance (the estimate in the 2004-05 budget papers for 2007-08, the estimate in the 2005-06 budget papers for 2008-09 and so on).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

### A3.4 Estimated and actual unemployment rates,<sup>(a)</sup> 2004-05 to 2013-14 budgets

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Budget year estimate <sup>(b)</sup>	5.00	4.75	7.00	5.50	5.00	5.75	5.50
Actual	4.50	5.10	5.50	5.10	5.40	5.70	6.20
Variation between budget year estimate and actual	-0.50	0.35	-1.50	-0.40	0.40	-0.05	0.70
Average variation between budget year estimate and actual				-0.14			
Earliest budget estimate <sup>(c)</sup>	5.25	5.25	5.25	5.00	4.75	7.75	5.25
Actual	4.50	5.10	5.50	5.10	5.40	5.70	6.20
Variation between earliest estimate and actual	-0.75	-0.15	0.25	0.10	0.65	-2.05	0.95
Average variation between earliest estimate and actual				-0.14			

(a) Year-average rate.

(b) That is, the estimate made in the budget immediately preceding the start of the financial year (the estimate in the 2007-08 budget papers for 2007-08, the estimate in the 2008-09 budget papers for 2008-09 and so on).

(c) That is, the estimate made three years in advance (the estimate in the 2004-05 budget papers for 2007-08, the estimate in the 2005-06 budget papers for 2008-09 and so on).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

### A3.5 Estimated and actual growth rates for the consumer price index,<sup>(a)</sup> 2004-05 to 2013-14 budgets

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Budget year estimate <sup>(b)</sup>	2.50	3.00	2.00	2.25	2.75	2.75	2.50
Actual	3.60	2.80	2.10	3.30	2.30	2.20	2.80
Variation between budget year estimate and actual	1.10	-0.20	0.10	1.05	-0.45	-0.55	0.30
Average variation between budget year estimate and actual				0.19			
Earliest budget estimate <sup>(c)</sup>	2.50	2.50	2.50	2.50	2.50	2.50	2.50
Actual	3.60	2.80	2.10	3.30	2.30	2.20	2.80
Variation between earliest estimate and actual	1.10	0.30	-0.40	0.80	-0.20	-0.30	0.30
Average variation between earliest estimate and actual				0.23			

(a) Annual percentage change compared with the previous year.

(b) That is, the estimate made in the budget immediately preceding the start of the financial year (the estimate in the 2007-08 budget papers for 2007-08, the estimate in the 2008-09 budget papers for 2008-09 and so on).

(c) That is, the estimate made three years in advance (the estimate in the 2004-05 budget papers for 2007-08, the estimate in the 2005-06 budget papers for 2008-09 and so on).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

### A3.6 Estimated and actual growth rates for the wage price index,<sup>(a)</sup> 2004-05 to 2013-14 budgets

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Budget year estimate <sup>(b)</sup>	3.50	3.75	3.75	3.25	3.75	3.00	3.50
Actual	3.80	4.00	2.80	3.80	3.50	3.30	2.70
Variation between budget year estimate and actual	0.30	0.25	-0.95	0.55	-0.25	0.30	-0.80
Average variation between budget year estimate and actual				-0.09			
Earliest budget estimate <sup>(c)</sup>	3.50	3.50	3.50	3.50	3.50	3.50	3.50
Actual	3.80	4.00	2.80	3.80	3.50	3.30	2.70
Variation between earliest estimate and actual	0.30	0.50	-0.70	0.30	0.00	-0.20	-0.80
Average variation between earliest estimate and actual				-0.09			

(a) Annual percentage change compared with the previous year.

(b) That is, the estimate made in the budget immediately preceding the start of the financial year (the estimate in the 2007-08 budget papers for 2007-08, the estimate in the 2008-09 budget papers for 2008-09 and so on).

(c) That is, the estimate made three years in advance (the estimate in the 2004-05 budget papers for 2007-08, the estimate in the 2005-06 budget papers for 2008-09 and so on).

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.2: Strategy and Outlook*, 2004-05 to 2015-16.

# Appendix 4

## Revenue

### A4.1 Past actual growth rates and forecast growth rates for components of revenue

	Past actual growth rate (per cent) <sup>(a)</sup>	Forecast future growth rate in 2015-16 Budget (per cent) <sup>(b)</sup>	Variance between past and forecast growth rates (percentage points)
<b>Taxation revenue</b>			
Payroll tax	4.3	5.9	1.6
Land transfer duty	2.0	1.5	-0.5
Gambling taxes	0.8	2.9	2.1
Motor vehicle taxes	5.9	4.2	-1.7
Land tax	11.5	7.8	-3.6
Other taxes <sup>(c)</sup>	9.2	1.9	-7.3
<b>Total taxation revenue</b>	<b>4.7</b>	<b>3.9</b>	<b>-0.8</b>
Dividends and income tax equivalent and rate equivalent revenue	-8.5	-2.8	5.7
Sales of goods and services	7.0	1.2	-5.8
Other revenue <sup>(d)</sup>	7.5	1.6	-5.9
<b>State-sourced revenue</b>	<b>5.1</b>	<b>2.8</b>	<b>-2.3</b>
General-purpose (GST) grants	3.7	7.5	3.8
Specific-purpose grants	9.5	-0.1	-9.6
<b>Grants from the Commonwealth Government</b>	<b>6.5</b>	<b>3.8</b>	<b>-2.7</b>
<b>Total revenue from transactions</b>	<b>5.8</b>	<b>3.3</b>	<b>-2.5</b>

(a) Compound annual growth rate, 2007-08 to 2013-14.

(b) Compound annual growth rate, 2015-16 to 2018-19.

(c) Includes insurance taxes and Fire Services Property Levy.

(d) Includes interest, other contributions and grants.

Sources: Department of Treasury and Finance, *State Taxation Revenue* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/State-taxation-revenue)>, viewed 27 May 2015; Department of Treasury and Finance, *Consolidated Comprehensive Operating Statement - General Government Sector* (2015). Available at <[www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements](http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Aggregate-financial-statements)>, viewed 1 June 2015; Committee calculations.

## A4.2 Estimated and actual amounts of revenue received in the budget year

	Revenue estimate for budget year (\$ million)	Actual revenue for budget year (\$ million)	Variance (\$ million)
2005-06 Budget	30,623.6	31,972.0	1,348.4
2006-07 Budget	32,442.1	34,885.7	2,443.6
2007-08 Budget	34,269.2	37,340.3	3,071.1
2008-09 Budget	37,810.0	39,284.8	1,474.8
2009-10 Budget	42,388.3	44,585.3	2,197.0
2010-11 Budget	45,759.3	46,026.9	267.6
2011-12 Budget	47,439.2	47,882.3	443.1
2012-13 Budget	48,356.7	48,612.9	256.2
2013-14 Budget	50,327.5	52,364.7	2,037.2

Sources: Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2005-06 to 2013-14; Department of Treasury and Finance, *Financial Report*, 2006-07 to 2013-14.

## A4.3 Grants from the Commonwealth Government expected by the Victorian budget papers to expire in 2014-15

Grant name	Revenue expected in 2014-15 (\$ million)
Transitional National Partnership Agreement on Homelessness	22.8
Remote Indigenous Housing	15.0
More Support for Students with Disabilities	14.3
National Quality Agenda on Early Childhood Education and Care	6.9
Treating More Public Dental Patients	31.9
Regional Rail Link	331.0
<b>Total</b>	<b>421.9</b>

Source: Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), pp.177-83.

## A4.4 Total revenue, forward estimates and forecast growth rates from past budgets

	Budget year (\$ million)	Second year (\$ million)	Third year (\$ million)	Fourth year (\$ million)	Average growth rate <sup>(a)</sup> (per cent)
2005-06 Budget	30,623.6	31,454.5	32,257.0	33,502.4	3.0
2006-07 Budget	32,442.1	33,462.9	34,594.7	35,499.8	3.0
2007-08 Budget	34,269.2	35,420.5	36,381.0	37,676.0	3.2
2008-09 Budget	37,810.0	39,320.8	41,116.8	42,646.4	4.1
2009-10 Budget	42,388.3	42,602.1	43,269.3	44,390.0	1.5
2010-11 Budget	45,759.3	46,595.5	49,169.1	50,400.1	3.3

(a) Compound annual growth rate from budget year to fourth year of the forward estimates period calculated by the Committee.

Sources: Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2005-06 to 2010-11.

# Appendix 5

## Parliamentary control over departmental revenue

### A5.1 Methods of adding to or changing resources available to departments – in the budget

Type	Authority	Who decides	Guidance document
Annual appropriations	Appropriations Act	Parliament	BFMG – 19
Special appropriations	Various acts	Parliament	BFMG – 19
Annotated receipts	FMA s.29	Treasurer and minister	BFMG – 19
Funds received and held outside the Public Account	FMA s.15	Minister for Finance	BFMG – 19
Funds received through trust funds	FMA s.9	Minister for Finance / Treasurer	BFMG – 18, BFMG – 19
Carryover of unapplied funds	FMA s.32	Treasurer	BFMG – 40
Treasurer's advances <sup>(a)</sup>	Appropriations Act schedule 1	Parliament	BFMG – 19, BFMG – 42
Accumulated surplus – previously applied appropriation	BFMG – 39	Treasurer	BFMG – 39

(a) The total value of Treasurer's advances is determined in the budget, but not its uses.

Source: Public Accounts and Estimates Committee.

### A5.2 Methods of adding to or changing resources available to departments – after the budget

Type	Authority	Who decides	Guidance document
Temporary advances	FMA s.35	Treasurer	BFMG – 19, BFMG – 42
Transfers between items of departmental appropriation	FMA ss.30, 31	Treasurer or presiding officers	BFMG – 19
Draw-down of accrual-based appropriations in future years	FMA s.33	Treasurer	BFMG – 42
Advances to cover salary and related cost increases	Section 3(2) of Appropriations Acts	Treasurer	FRD – 13
Appropriation of additional Commonwealth grants	FMA s.10	Treasurer and Governor-in-Council	BFMG – 18
Borrowing against future appropriations	FMA s.28	Treasurer and Governor-in-Council	BFMG – 19
Carryover of unapplied funds	FMA s.32	Treasurer	BFMG – 40
Treasurer's advances <sup>(a)</sup>	Appropriations Act schedule 1	Treasurer	BFMG – 19, BFMG – 42

(a) The amounts from the Treasurer's advances provided to departments are determined during the year as circumstances require.

Source: Public Accounts and Estimates Committee.





# Appendix 6

## Borrowings

### A6.1 Public non-financial corporations sector net debt, June 2015 to June 2019

PNFC entity	2015 revised estimate	2016 Budget	2017 estimate	2018 estimate	2019 estimate
	(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
Melbourne Water Corporation	8,223.9	8,299.4	8,315.7	8,491.0	8,608.4
Yarra Valley Water Corporation	2,079.8	2,314.7	2,496.8	2,648.1	2,859.5
South East Water Corporation	1,317.8	1,386.2	1,419.5	1,440.2	1,442.0
City West Water Corporation	1,091.6	1,158.2	1,208.3	1,258.4	1,382.9
Victorian Rail Track	735.2	647.2	556.7	371.9	351.7
Barwon Region Water Corporation	578.3	608.4	604.5	578.5	588.8
Coliban Region Water Corporation	468.9	476.0	458.6	441.9	419.5
Urban Renewal Authority Victoria (Places Victoria)	275.5	302.4	287.4	256.1	255.6
Other PNFCs <sup>(a)</sup>	137.2	367.1	625.1	596.6	483.1
<b>Total PNFC net debt</b>	<b>14,908.2</b>	<b>15,559.6</b>	<b>15,972.6</b>	<b>16,082.7</b>	<b>16,391.5</b>

(a) Calculated by the Committee based on the difference between the entities listed above and the total.

Sources: Department of Treasury and Finance, *Response to the Committee's 2015-16 Budget Estimates General Questionnaire*, received 12 June 2015, p.49; Department of Treasury and Finance, *Budget Paper No.5: 2015-16 Statement of Finances* (2015), p.51.



# Appendix 7

## Output expenses

### A7.1 Estimated and actual amounts of expenses in the budget year

	Expenses estimate for budget year (\$ million)	Actual expenses for budget year (\$ million)	Variance (\$ million)
2005-06 Budget	30,258.9	31,147.5	888.6
2006-07 Budget	32,125.3	33,551.2	1,425.9
2007-08 Budget	33,944.9	35,693.8	1,748.9
2008-09 Budget	36,982.4	39,033.7	2,051.3
2009-10 Budget	42,223.2	43,941.7	1,718.5
2010-11 Budget	44,887.4	45,509.6	622.2
2011-12 Budget	47,298.8	47,311.0	12.2
2012-13 Budget	48,201.8	48,929.4	727.6
2013-14 Budget	50,103.0	50,388.5	285.5

Sources: Department of Treasury and Finance, *Budget Paper No.4/5: Statement of Finances*, 2005-06 to 2013-14; Department of Treasury and Finance, *Financial Report*, 2006-07 to 2013-14

## A7.2 Initiatives, programs and projects from which \$2.0 million or more of funding was reprioritised in the 2015-16 Budget

Department	Initiative, program or project	2015-16 (\$ million)	2016-17 (\$ million)	2017-18 (\$ million)	2018-19 (\$ million)
Economic Development, Jobs, Transport and Resources	<i>Regional Growth Fund (RGF)</i>	125.0	125.0	125.0	125.0
	General Recurrent	8.4	3.2	2.9	0.6
	Reform of industry and innovation policy reprioritisation	199.9	131.2	103.0	35.9
	<ul style="list-style-type: none"> <li>The Government is reforming its approach towards driving economic growth, jobs and innovation in Victoria. A number of programs are being assessed as to whether they are suitable for the reformed approach.</li> </ul>				
	<i>Jobs for the 21<sup>st</sup> Century</i>	12.1	14.5	14.5	-
Education and Training	Local Learning and Employment Networks	8.0	8.0	8.0	8.0
	<ul style="list-style-type: none"> <li>This funding is for the continuation of the Local Learning and Employment Networks program.</li> </ul>				
Environment, Land, Water and Planning	none				
Health and Human Services	Funding for the Community Sports Infrastructure Fund was reprioritised from the Strategic Sporting Infrastructure Fund (see LFS, page 11)	18.0	0.0	0.0	0.0
	Funding for the Homelessness innovation action projects is drawn from the State budget commitment to the National Partnership Agreement on Homelessness	5.7	5.9	6.2	0.0
	Funding for the Proton beam therapy centre has been reprioritised from the Department's existing budget	2.0	0.0	0.0	0.0
	Funding for the WOVG Family Violence Response (DHHS component) was reprioritised from flexible post-crisis responses for women and children (see LFS, page 11)	3.8	0.0	0.0	0.0

Department	Initiative, program or project	2015-16 (\$ million)	2016-17 (\$ million)	2017-18 (\$ million)	2018-19 (\$ million)
Justice and Regulation <i>(including Victoria Police, the Melbourne Fire and Emergency Services Board and the Country Fire Authority)</i>	Women's Prison Expansion Strategy to Meet Demand	17.7	2.3	2.3	2.3
	<ul style="list-style-type: none"> <li>Reprioritisation from funding originally provided for the Marngoneet Annex which has experienced construction delays and redirected funding from existing women's prison initiatives.</li> </ul>				
	Police Communications Upgrade	2.8	3.2	8.9	8.9
	<ul style="list-style-type: none"> <li>Reprioritisation of existing police projects including the retirement of the legacy analogue service.</li> </ul>				
	Working with Children Check	4.8	4.7	0.0	0.0
	<ul style="list-style-type: none"> <li>Reprioritisation from efficiencies and savings from within Infringement Management and Enforcement Services.</li> </ul>				
	Family Violence	2.6	1.0	0.0	0.0
	<ul style="list-style-type: none"> <li>Reprioritisation from previously approved funding for Family Violence initiatives.</li> </ul>				
Victoria Police StateNet Mobile Radio service payments	0.0	0.0	7.5	7.5	
CFA Emergency Medical Response Program	0.2	0.2	0.2	0.2	
<ul style="list-style-type: none"> <li>Reprioritisation from CFA's base Budget used to fund EMR pilot program.</li> </ul>					
Firefighter Training (Hazelwood)	1.7	0.2	0.3	0.3	
<ul style="list-style-type: none"> <li>Reprioritisation from CFA and MFESB Base Budget.</li> </ul>					
Premier and Cabinet	Victorian Aboriginal Cultural Heritage Strategy	0.6	1.2	1.2	1.2
	Office of the Public Access Counsellor	3.7	3.7	3.7	3.7
	Office of the Chief Parliamentary Counsel	0.6	0.6	0.6	0.6
Treasury and Finance	none	-	-	-	-
Parliament	none	-	-	-	-
Courts	none	-	-	-	-
<b>Total</b>		<b>417.7</b>	<b>305.1</b>	<b>284.3</b>	<b>194.3</b>

Sources: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.

### A7.3 Lapsing programs<sup>(a)</sup> in 2014-15, as identified by departments

Department	Program or initiative	Expenditure in 2014-15 (\$ million)
Economic Development, Jobs, Transport and Resources	Support for the Victorian College of the Arts	6.0
	Victorian Sculpture Initiative	0.3
	Melbourne Recital Centre SummerSalt	1.0
	Victorian Screen Fellowships	0.1
	Victoria - Leader in Learning	0.4
	Transition to a Global Future	0.1
	Building Innovative Small Manufacturers	2.8
	Specialist Manufacturing Service	1.6
	Automotive New Markets Program	1.0
	Supporting the Aviation Industry	3.2
	Regional Blueprint: Industry Capability Network	1.3
	Industry Capability Network - Whole of Government	1.5
	Local Area Capital Improvements	1.0
	Information & Communications Technology	5.2
	Export Victoria	2.3
	International Markets	2.0
	Development projects along the Richmond to Footscray rail corridor	4.9
	Victoriaworks for Indigenous Jobseekers Program	1.3
	CALD Jobs Bank Registry	0.1
	Victorian Employment Solutions	2.7
	Opening unused Railway Station buildings to community and sporting groups	1.3
	Preserve W Class Trams	2.0
	Inter Capital High-Speed Rail Planning Unit	1.0
	Establish Public Transport Development Authority	2.5
	Country Roads and Bridges	40.0
	Smoke Taint in Australian Vineyards	1.0
	Taxi Services Commission	0.3
	Recreational Fishing Opportunities in Regional Victoria	4.2
	NICTA (World Class R&D)	8.5
	Victorian Biotechnology Advisory Council	0.4
	Driving Business Innovation	5.6
	Veski Fellowships and School Mentoring	0.7
	Australian Open Tennis	3.2
	Les Misérables 2014	0.2
	Bicycle Ferry - Port Punt	0.4
	Regional Victoria Living Expo	0.5
	Edgars Road - Development	0.5
	Red Tape Commissioner	0.4
	Farmers Markets Support Program	1.0

Department	Program or initiative	Expenditure in 2014-15 (\$ million)
Economic Development, Jobs, Transport and Resources (continued)	Regional Blueprint: Sustainable Small Towns Program	12.0
	Regional Blueprint: Planning for Tomorrow	1.3
	Regional Blueprint: Frameworks for the Future	1.1
	Regional Blueprint: The Good Life in Provincial Victoria	2.5
	Community Support Grants	3.1
	Revitalising Regional Towns/Advancing Country Towns	0.1
	Modernising Farm Services	21.7
Education and Training <sup>(b)</sup>	Early Years Workforce Support	7.5
	Early Childhood Intervention Service (ECIS) Improvement Project	1.0
	Parenting Support Strategy	0.6
	Education Maintenance Allowance replacement funding for non-government schools	11.0
	Combat Bullying	1.0
	Safe Schools – Professional Development for Teachers	0.5
	Science, Maths, and Entrepreneurship – Collaborative Network	0.1
	Languages Teaching Scholarships	2.0
Department of Environment, Land, Water and Planning	Water efficiency rebates	10.0
	Frankston Activities Area revitalisation	0.8
	Planning for Melbourne and regional Victoria	0.2
	Victorian Adaptation Sustainability Partnership	-(c)
	ResourceSmart Schools	-(c)
	ResourceSmart Business	-(c)
	Communities for Nature	-(c)
Victoria Environment Partnerships Program	-(c)	
Health and Human Services	Services Connect – Extension of Client Support Trials in Dandenong, Geelong and Portland and expansion of existing sites' capacity	3.1
	Initiatives under the Youth Action Strategy (Shape It!) – the Exchange; Change It Up and Shape It! grants	0.2
	Neighbourhood Renewal at Flemington and Maryborough	1.0
	Kids Under Cover	1.1
	Enhance and redevelop community-based mental health infrastructure (Stage 2)	2.0
	Headspace communities of Youth Services	1.0
	Improved housing access for people with a severe mental illness – improved housing access	0.2
	Active Sports Partnership Program	0.2
	Integrity in Sport	0.3
	Melbourne to Warrnambool Cycling Classic	0.1
	Motorcycle Paramedic Unit	1.0
	Abolish 'not ready for care'	0.1
	Bush Nursing Support	0.6
	First On – First Off rule	-
	Health Condition Support & Self Help Group Grants	1.0
	Health Innovation & Reform Council Board Fees	0.1

Department	Program or initiative	Expenditure in 2014-15 (\$ million)
Health and Human Services <i>(continued)</i>	Health services winter demand capacity enhancement	60.0
	Hospital Improvement Commission	0.1
	Infection prevention	2.5
	Informing consumers about maternity care	0.2
	Open Access Board Meetings	0.0
	Patient focussed work practices	0.1
	ANZAC Centenary 'Lest we forget' grants	0.2
	Bowel cancer screening	0.5
	National Partnership Agreement on Preventive Health - Chronic Disease Prevention (Healthy Together Victoria)	12.5
Justice and Regulation	Step Back Think	0.2
	Fire Services Levy Monitor	2.3
	Electronic Monitoring	1.8
Premier and Cabinet	Women's Economic Participation Strategy	0.5
Treasury and Finance	none	-
Parliament	none	-
Courts	none	-
<b>Total</b>		<b>281.3</b>

- (a) Names of programs or initiatives are as received in departmental responses and may differ from the budget papers.
- (b) The Department of Education and Training noted: 'All numbers are estimated based on budget allocation, with the exception of Education Maintenance Allowance - as the program ceased at the end of 2014, actual expenditure is shown'.
- (c) No details supplied by the Department.

Sources: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.



## A7.4 Major areas of risk relating to output expenses estimates

Department	Response
Economic Development, Jobs, Transport and Resources	The major area of risk to the Department's expenditure estimates is primarily related to unexpected changes to input costs for services and construction of infrastructure.
Education and Training	n/a
Environment, Land, Water and Planning	The major risk for the Department in relation to expense estimates would be any unexpected costs associated with emergency response.
Health and Human Services	<p>The portfolio expenses for 2015-16 include estimated employee costs of \$9,804 million as would be usual practice the renewal of Enterprise Bargaining Agreements across the sector over the next four years presents for risk over the forward estimates period because of the inherent nature of negotiated outcomes.</p> <p>The transition of Home and Aged Care (HACC) services for people aged 65 and over to the Commonwealth and the introduction of the National Disability Insurance Scheme will affect the residual disability scheme provided by the Department. The policy parameters for the residual disability scheme have not been finalised, so costs may vary from those incorporated in the forward estimates.</p>
Justice and Regulation	<p><b>Department of Justice and Regulation</b></p> <p>The major areas of risk identified by the Department for its expense estimates are:</p> <ul style="list-style-type: none"> <li>• The incremental impact of the General Efficiency Dividend savings announced by the previous government and the risk of not achieving efficiency targets in the forward estimates without compromising service delivery.</li> <li>• Greater than anticipated increases in the number of prisoners and offenders (both men and women) following recent legislative changes, including the abolition of suspended sentences.</li> <li>• Growth in security related costs due to the increased domestic terror threat level.</li> <li>• Higher than anticipated emergency response related costs due to bushfire, floods, storms, etc.</li> </ul> <p><b>Victoria Police</b></p> <p>The major risks for Victoria Police expenditure estimates relate to:</p> <ul style="list-style-type: none"> <li>• Responding to the increasing security threat levels. <ul style="list-style-type: none"> <li>- Responding to the increasing threat levels against police and the broader community is generating significant challenges for Victoria Police given the size of the entity, the complexities of service delivery and the Victorian community's expectations. The current security level is likely to be in place for some time, and will involve additional measures to protect the community and maintain the safety of police personnel and staff.</li> </ul> </li> <li>• Commuted Overtime. <ul style="list-style-type: none"> <li>- As a result of a Fair Work Australia decision, a significant number of back-pay claims have been received whereby employees are now seeking the allowance for duties they have performed in the past that was similar to detective work. To date, 1600 claims have been received, and as at 31 March 2015 Victoria Police has raised a \$15 million provision for such claims in order to meet current accounting requirements. The value of the claims recognised is based on management assessments and it is possible that further claims may be received by affected Sworn employees</li> </ul> </li> <li>• Outcomes of EBA negotiations <ul style="list-style-type: none"> <li>- Over the forward estimates period, both the Sworn and VPS EBAs will be subject to renewal. Any salary increase beyond Government wages policy (not offset by productivity savings) will place pressure on Victoria Police's expenditure estimates.</li> </ul> </li> </ul>

Department	Response
Justice and Regulation <i>(continued)</i>	<p><b>Metropolitan Fire and Emergency Services Board</b></p> <p>The financial risks for MFB are:</p> <ul style="list-style-type: none"> <li>• that the 2.5% funding increase (Departmental Funding Model (DFM) rate) may be insufficient to cover the entire cost of running the new Victorian Emergency Management Training Centre (VEMTC) at Craigieburn – work is ongoing to determine an appropriate cost model for multi-agency usage to mitigate this risk</li> <li>• the forecast running costs to provide Marine Response is predictive as there is limited historical data to draw on. Therefore forecast revisions may be required.</li> <li>• the forthcoming Operational EBA may result in higher costs being incurred by the MFB than is currently funded for (including the DFM increase).</li> </ul> <hr/> <p><b>Country Fire Authority</b></p> <p>Fire season activity related expenditure.</p>
Premier and Cabinet	No risks identified.
Treasury and Finance	<p>The major component of DTF’s expenses are staffing costs which are generally stable and predictable. DTF will achieve its allocated savings target by finding efficiencies while continuing to deliver services through its allocated resources.</p> <p>The major areas of risk for CenITex are an ageing asset base and platforms, and the potential impairment of assets upon transition to cloud technologies.</p>
Parliament	Increase in electorate office and precinct rents and utilities, increase in electorate officer salary and on-costs, relocation of electorate offices impacted by the redistribution of electoral boundaries and operation of Legislative Council Standing Committees for which no staff salary and on-costs funding was approved by 2015-16 ERSC.
Courts	<p>CSV expenses are forecast to grow faster than increases to its appropriation. Major expense risks for CSV primarily relate to the growth of salary expenses and insufficient funding to resource demand pressures created by upstream or downstream policy impacts.</p> <p>In addition aging IT and poor quality court buildings and facilities pose significant expense risk and are points of potential critical failure for the Courts.</p>

Sources: Departmental responses to the Committee’s 2015-16 Budget Estimates General Questionnaire.

# Appendix 8

## Asset investment

### A8.1 PPP payments made by departments, 2014-15 to 2015-16

Department	Payment	2014-15 revised estimate (\$ million)	2015-16 Budget (\$ million)	2016-17 estimate (\$ million)	2017-18 estimate (\$ million)	2018-19 estimate (\$ million)
Economic Development, Jobs, Transport and Resources	<b>Peninsula Link Project – Operating statement</b>					
	Interest expense	44.6	88.0	85.1	82.9	82.9
	Other operating expenses	4.8	8.3	9.6	9.0	9.0
	<b>Total</b>	<b>49.4</b>	<b>96.3</b>	<b>94.7</b>	<b>91.9</b>	<b>91.9</b>
	<b>Biosciences Research Centre Project – Operating statement</b>					
	Employee benefits	0.1				
	Interest expense	8.8	17.6	17.3	17.2	16.9
	Other operating expenses	6.8	10.3	10.7	10.3	11.6
	<b>Total</b>	<b>15.7</b>	<b>27.9</b>	<b>28.0</b>	<b>27.5</b>	<b>28.5</b>
	<b>Showgrounds Redevelopment – Operating statement</b>					
	Employee benefits	0.1	0.1	0.1	0.1	0.1
	Interest expense	3.0	3.6	2.9	0.0	0.0
	Other operating expenses	0.2	0.2	0.2	0.2	0.2
Net gain/(loss) on financial instruments and statutory receivables/payments	0.0	0.0	0.0	2.3	1.6	
<b>Total</b>	<b>3.3</b>	<b>3.9</b>	<b>3.2</b>	<b>2.6</b>	<b>1.9</b>	
<b>Melbourne Convention and Exhibition Centre – Administered items statement</b>						
Expenses on behalf of the State	16.7	17.0	18.1	19.1	19.4	
<b>Melbourne Convention and Exhibition Centre – Operating statement</b>						
Grants and other transfers	5.1	5.2	5.4	5.5	5.5	
Interest expense	40.7	40.5	40.3	40.0	42.5	
<b>Total</b>	<b>45.8</b>	<b>45.7</b>	<b>45.7</b>	<b>45.5</b>	<b>48.0</b>	

Department	Payment	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
		(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
Environment, Land, Water and Planning	Payments made on behalf of the State – Victorian Desalination <b>Project finance lease liability</b> – Administered items	40.4	44.3	33.2	40.4	45.7
	Payments made on behalf of the State – Victorian Desalination <b>Project finance lease Interest</b> – Administered items	467.0	462.9	458.8	454.9	450.4
	Payments made on behalf of the State – Victorian Desalination <b>Project Contractor cost</b> – Administered items	123.7	112.8	116.0	120.7	131.9
	<b>Total</b>	<b>631.1</b>	<b>620.0</b>	<b>608.0</b>	<b>616.0</b>	<b>628.0</b>
Health and Human Services	<b>Operating statement</b>					
	Other operating expenses	121.2	135.4	139.4	138.8	145.2
	<b>Cash flow statement</b>					
	Repayment of finance leases	12.4	12.4	12.4	12.4	12.4
Justice and Regulation	<b>Operating statement</b>					
	Interest expense	21.2	20.6	19.9	49.8	64.7
	Other operating expenses	144.8	150.2	153.4	124.2	164.1
	<b>Total</b>	<b>166.0</b>	<b>170.8</b>	<b>173.3</b>	<b>174.0</b>	<b>228.8</b>
	<b>Cash flow statement</b>					
	Interest and other cost of finance	21.2	20.6	19.9	49.8	64.7
	Payments to suppliers and employees	144.8	150.2	153.4	124.2	164.1
	Repayment of finance leases	11.9	13.3	12.7	320.9	12.5
	Payment for non-financial assets	8.2	8.0	8.3	5.0	0.0
<b>Total</b>	<b>186.1</b>	<b>192.1</b>	<b>194.3</b>	<b>499.9</b>	<b>241.3</b>	

Department	Payment	2014-15 revised estimate	2015-16 Budget	2016-17 estimate	2017-18 estimate	2018-19 estimate
		(\$ million)	(\$ million)	(\$ million)	(\$ million)	(\$ million)
Courts	<b>Operating statement</b>					
	Depreciation	5.7	5.7	5.7	5.7	5.7
	Other operating expenses	16.1	18.0	20.6	19.7	19.3
	<b>Total</b>	<b>21.8</b>	<b>23.7</b>	<b>26.3</b>	<b>25.4</b>	<b>25.0</b>
	<b>Cash flow statement</b>					
	Repayment of finance leases	4.8	4.8	4.8	4.8	4.8
	Interest and other finance costs paid	11.4	11.4	11.4	11.4	11.4
	<b>Total</b>	<b>16.2</b>	<b>16.2</b>	<b>16.2</b>	<b>16.2</b>	<b>16.2</b>

Sources: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.

## A8.2 Carried over funds from 2014-15 by departments

Department	2015-16 (\$ million)
Economic Development, Jobs, Transport and Resources	26.2
Environment, Land, Water and Planning	0.1
Education and Training	0.0
Health and Human Services	118.4
Justice and Regulation	42.8
Premier and Cabinet	1.5
Treasury and Finance	0.0
Parliament	0.0
Courts	0.0
<b>Total</b>	<b>189.0</b>

Sources: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.



# Appendix 9

## The Government's election commitments

### A9.1 Output commitments yet to be funded

Commitment	Funds committed in <i>Labor's Financial Statement 2014</i> <sup>(a)</sup> (\$ million)
Active Transport Victoria	3.3
Doctors in Schools	24.6
Geelong Ring Road extension – Planning	4.0
Grant for VTA Logistics Cadetship Program	1.0
Grant to Country Women's Association	0.1
Homes for Homes	0.5
Parliamentary Budget Office	11.0
Presumptive Rights for Fire Fighters	40.0
Response Time Rescue Fund – New Program Funding	60.0
Rolling Stock – Stage 1 – Operating Component	20.4
Romsey Intersection – Planning	0.2
Rooming House Upgrade Program	10.0
TAC International	0.5
WorkSafe Package	6.5
<b>Total</b>	<b>182.0</b>

(a) Total funding is committed between 2016-17 and 2018-19.

Source: Committee calculations based on Victorian Labor, *Labor's Financial Statement 2014* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

## A9.2 Output commitments fully funded but with a different schedule to the LFS

Commitment	Funds committed in <i>Labor's Financial Statement 2014</i> <sup>(a)</sup> (\$ million)
Additional Police Resources – Operating Component	138.6
China and India Scholarship Program	1.0
Community Sports Infrastructure Fund (including Female Facilities)	100.0
Engaging With the Mining Sector	1.0
Ethical Clothing	2.0
Future Industries Fund (including New Energy Jobs Fund)	200.0
Melbourne's North Innovation and Investment Fund	10.5
Premier's Jobs and Investment Panel (Including Start-Up Victoria)	508.0
Simonds Stadium – Operational Costs	4.8
Newstead Solar <sup>(b)</sup>	0.2
Macedon Solar <sup>(b)</sup>	0.1
<b>More funding provided than committed</b>	
Emergency Medical Response Expansion	5.0
Office of the Public Access Commissioner	12.0
Phase out Commercial Netting in the Bay (First Four Years)	10.0
SunSmart – New Program Funding	5.0
Young Farmer Scholarships	0.5

(a) Total funding is committed between 2014-15 and 2018-19.

(b) These two projects were amalgamated and funded as a single initiative, *Newstead/Woodend Renewable Energy Grants*.

Source: Committee calculations based on Victorian Labor, *Labor's Financial Statement 2014* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

## A9.3 Output initiatives noted as fulfilling election commitments where it is not clear what commitments they relate to

Initiative name	Funds provided in 2015-16 Budget <sup>(a)</sup> (\$ million)
Community Infrastructure and Cultural Precincts Fund	11.1
Community Capacity and Participation	13.2
Firefighter Training (Hazelwood)	1.7
House of World Cultures Feasibility Study	0.2
Life Saving Victoria Clubhouse Redevelopments – Ocean Grove and South Melbourne	4.7
Promoting Social Cohesion and Community Harmony	20.7
Victorian Small Business Commission	10.4

(a) Total funding is provided between 2014-15 and 2018-19.

Source: Committee calculations based on Victorian Labor, *Labor's Financial Statement 2014* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.



## A9.4 Asset commitments yet to be funded

Commitment	TEI in <i>Labor's Financial Statement 2014</i> (\$ million)
Aikenhead Biomedical Engineering	60.0
Chinese Aged Care Land Bank	2.5
Contemporary Music Hub	10.0
Doctors in Schools	18.0
Golf Centre of Excellence	10.0
Maroondah Breast Cancer Centre	10.0
O'Herns Rd Upgrade – State Contribution	40.7
Railway Station Car Parking Fund	20.0
Save Sunvale Primary Site	4.2

Source: Committee calculations based on Victorian Labor, *Labor's Financial Statement 2014* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), p.109.

## A9.5 Asset commitments funded differently to the way indicated in the LFS

Commitment (from LFS)	
CFA trucks	Scope increased from 50 to 70 trucks
Level Crossing Removal Program – Stage 1	Commitment fulfilled as part of a larger initiative
Melbourne Metro – Planning and Early Works	Commitment fulfilled as part of a larger initiative
Metro Rolling Stock – Stage 1	Commitment fulfilled as part of a larger initiative
Regional Rolling Stock – Stage 1	Commitment fulfilled as part of a larger initiative
State Library Redevelopment	Initiative includes additional funding from other sources
Better Fishing Facilities	Fully funded through an output initiative
Canadian State Park	Fully funded, but the majority of funds were provided through an output initiative
Inner City Netball	Fully funded through an output initiative
Police Communications Upgrade	Fully funded through an output initiative. The existing project was rearranged, including \$11.5 million in new funding, which is \$1.5 million more than had been committed.
Save the Palais	Fully funded through an output initiative
SunSmart – Capital Component	Fully funded, but with a different mix of asset and output funding to what was specified in the LFS

Source: Committee calculations based on Victorian Labor, *Labor's Financial Statement 2014* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

## A9.6 Partly funded asset commitments

Commitment (from LFS)	TEI in <i>Labor's Financial Statement 2014</i> (\$ million)	TEI in budget papers (\$ million)	Variance (\$ million)
Bolton St Eltham Upgrade	10.5	0.0 <sup>(a)</sup>	-10.5
Drysdale Bypass Construction	109.0	2.0	-107.0
Extra School Capital	20.0	n/a <sup>(b)</sup>	-
Frankston Station Precinct Redevelopment	50.0	13.1	-36.9
Mernda Rail Extension	400.0–600.0	9.0	-391.0–591.0
Napier St Bendigo Upgrade	17.2	0.6	-16.6
Orygen Youth Mental Health	60.0	1.0	-59.0
Road and Rail Minor Works Fund	80.0	43.8 <sup>(a)</sup>	-36.2
School Asbestos Removal Program	100.0	27.0 <sup>(a)</sup>	-73.0
School Capital Package	510.0	n/a <sup>(b)</sup>	-
Streamlining Hoddle St	60.0	0.0 <sup>(a)</sup>	-60.0
Tech Schools – Capital Component	100.0	8.0	-92.0
Thompsons Rd duplication	175.0	20.5	-154.5
Victorian Heart Hospital	150.0	15.0	-135
West Gate Distributor	500.0	38.5 <sup>(a)</sup>	-461.5
Yan Yean Rd Duplication	95.0	0.9	-94.1

(a) Some funding provided through output initiatives.

(b) Funding has been allocated to these commitments, including *School Improvement Program*, but the amount allocated to specific programs cannot be determined.

Source: Committee calculations based on Victorian Labor, *Labor's Financial Statement 2014* (2014); Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 1.

# Appendix 10

## Performance measurement

### A10.1 Discontinued departmental objective indicators, 2014-15 to 2015-16

Department	Objective indicator
Environment and Primary Industries	Number of effective responses to biosecurity events, incursions and emergencies
	Number of fisheries and levels of timber stocks maintained within sustainable limits
Justice	Proportion of voters enrolled out of total eligible
	Anti-corruption and Freedom of Information (FOI) education activities (FOI and IBAC)
Premier and Cabinet	Victoria's reputation as an international centre for arts and culture is enhanced
	Access to arts and cultural programs is improved, particularly for school children, youth, families and regional communities
	Victoria's cultural venues and state owned facilities are maintained to provide continuously improving services to Victorians
	The Governor is supported effectively in the exercising of his functions and powers
	A centre for excellence that fosters an efficient, ethical and responsible public sector
	Services provided to the State relating to the development, drafting, publication and implementation of legislation are comprehensive, integrated and of a high quality
	Capacity building activities undertaken with traditional owner groups: cultural heritage management
State Development and Business Innovation	Level of participation in ANZAC commemoration and visits to Shrine of Remembrance
	Business skills needs assisted
	Collaborations assisted
Transport, Planning and Local Infrastructure	Market outcomes, industry and consumer confidence strengthened
	Public transport patronage
	Total investment dollars leveraged, by type, for committed infrastructure projects
	The vision for Victoria is reflected in the State Planning System
Treasury and Finance	The quality of the built environment has significant cultural and public value contributing to an enriched sense of place for all Victorians
	Satisfaction of key stakeholders with State Planning Strategies
	Ensure approved Public Sector EBAs comply with wages policy and support improvements to productivity and workplace reform
	Increased engagement with industry to enable improved compliance and productivity in the Victorian construction industry

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2; Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), Chapter 2.

## A10.2 New departmental objective indicators, 2014-15 to 2015-16

Department	Objective indicator
Economic Development, Jobs, Transport and Resources	Attendance at creative and cultural events and experiences
	Creative organisations and projects supported
	Visitor satisfaction at creative and cultural events, and state owned cultural facilities
	Major projects delivered
	Relative share of Victorian energy sourced from renewables
	Value of Victorian earth resources production
	Transport projects delivery complies with agreed scope, timeframes and budget
Environment, Land, Water and Planning	Efficient provision of timely and authoritative information on population growth and change
	Public participation in planning, building and heritage initiatives
Health and Human Services	Incidence/prevalence of selected potentially preventable health conditions is reduced
	Percentage of patients seen within clinically recommended times
	The Victorian public health system has a sustainable workforce
	Reduced rate of hospital admissions for ambulatory care sensitive conditions
	Services provided to patients are safe and of high quality
	Victoria has a framework for sustainable infrastructure and fabric
Premier and Cabinet	Quality infrastructure drives economic activity in Victoria
	The development and effective use of technology supports productivity and competitiveness
	The costs and barriers associated with doing business in Victoria are reduced
Treasury and Finance	Provide high quality, timely and relevant advice on the State's finances and budget, borrowings, investments, insurance, superannuation issues and prudential supervision, as assessed by feedback from our key clients
	Provide high quality, timely and relevant advice on economic policy, forecasts, legislation and frameworks as assessed by feedback from our key clients
	Provide high quality, timely and relevant advice on asset management, the delivery of infrastructure and management of government land as assessed by feedback from our key clients
	Provide high quality, timely and relevant advice on services to Government as assessed by feedback from our key clients

Source: Public Accounts and Estimates Committee, based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2; Department of Treasury and Finance, *Budget Paper No.3: 2014-15 Service Delivery* (2014), Chapter 2.

### A10.3 Performance measures by department, type of performance measure (proportion), 2015-16 Budget

Department	Quality (per cent)	Quantity (per cent)	Timeliness (per cent)	Cost (per cent)	Total (per cent)
Economic Development, Jobs, Transport and Resources	22.0	53.6	16.9	7.5	100.0
Education and Training	51.7	39.3	1.1	7.9	100.0
Environment, Land, Water and Planning	24.3	43.7	22.3	9.7	100.0
Health and Human Services	28.0	47.1	13.1	11.8	100.0
Justice and Regulation	26.0	47.2	17.9	8.9	100.0
Premier and Cabinet	22.5	32.5	26.3	18.8	100.0
Treasury and Finance	36.1	24.6	24.6	14.8	100.0
Parliament	31.0	26.2	28.6	14.3	100.0
Courts	8.8	58.8	29.4	2.9	100.0
<b>Total</b>	<b>27.3</b>	<b>45.2</b>	<b>17.2</b>	<b>10.3</b>	<b>100.0</b>

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2.

### A10.4 Performance measures by department, type of performance measure, 2015-16 Budget

Department	Quality (number)	Quantity (number)	Timeliness (number)	Cost (number)	Total (number)
Economic Development, Jobs, Transport and Resources	65	158	50	22	295
Education and Training	46	35	1	7	89
Environment, Land, Water and Planning	25	45	23	10	103
Health and Human Services	81	136	38	34	289
Justice and Regulation	32	58	22	11	123
Premier and Cabinet	18	26	21	15	80
Treasury and Finance	22	15	15	9	61
Parliament	13	11	12	6	42
Courts	3	20	10	1	34
<b>Total</b>	<b>305</b>	<b>504</b>	<b>192</b>	<b>115</b>	<b>1,116</b>

Source: Committee calculations based on Department of Treasury and Finance, *Budget Paper No.3: 2015-16 Service Delivery* (2015), Chapter 2.

## A10.5 New initiatives<sup>(a)</sup> worth \$20 million or more without any associated performance measures other than output cost, 2015-16 Budget

Department	Initiative
Economic Development, Jobs, Transport and Resources	Premier's Jobs and Investment Fund (including the 'Start Up' initiative)
	Home Safe - 24 hour public transport on weekends
	Securing Service Improvements on Victoria's public transport network
	Crash and Trauma Education Centre (Asset and Output)
	High-Capacity Metro Trains
	Practical driver training for year 10s
	Optimising transport network performance congestion
	Conventional signalling upgrade Caulfield and Dandenong
	Trial of high capacity signalling - stage 1
	Xtrapolis Trains - Five six car sets
	Chandler Highway Bridge duplication
	Life Extension of Comeng Trains
	M80 Upgrade - EJ Whitten bridge to Sunshine avenue
	West Gate Distributor - Northern Section
Education and Training	Asbestos removal program
	Building new schools
	Land acquisition
	Relocatable Classroom Program
	Modernisations and upgrades
	TAFE Rescue Fund (capital component)
	Build and upgrade kindergartens
	Education State funding - allocation of \$1.4 billion
	School enrolment based funding
School Maintenance Fund	
Environment, Land, Water and Planning	Interface Councils Infrastructure Fund
Health and Human Services	Meeting ambulance services demand and responsiveness
	Super Pharmacies
	Genomic testing
	Angliss Hospital intensive care unit and short stay unit
	Casey Hospital expansion
	Engineering infrastructure replacement program
	Health service violence prevention fund
	Medical equipment replacement program
	Werribee Mercy Hospital - acute expansion
	Western Women's and Children's Hospital
	Ambulance station upgrades
	Ambulance vehicles and equipment
	Expansion of intensive placement prevention and family re-unification service
	Improving financial support for carers
	Springboard
Justice and Regulation	Social and Community Services equal remuneration order

(a) Names of initiatives are as received in departmental responses and may differ from the budget papers.

Source: Departmental responses to the Committee's 2015-16 Budget Estimates General Questionnaire.

## A10.6 Performance measures proposed to be discontinued in the 2015-16 Budget which the Committee considers should be retained

### Department of Economic Development, Jobs, Transport and Resources

Output	Measure	Explanation given in the budget papers	Committee comment
Industry and Enterprise Innovation	Number of major research and evaluation projects completed	This performance measure is proposed to be discontinued as it only measures operational activities and does not contribute to outputs.	The Department further indicated that 'The number of research and evaluation projects undertaken in one policy area represents an input that supports the Department's core business of program and policy development. The current measure is an input activity rather than an output that is aligned with the Department's service delivery needs'. <sup>(a)</sup>  The Committee notes that the former Department of Business and Innovation proposed discontinuing this measure with the 2012-13 Budget for similar reasons. The Committee at the time recommended it not be discontinued, based on a belief that stakeholders would have an interest in this measure and that it was an appropriate matter to report on. The current Committee supports that view.
Sustainably Manage Fish, Game and Forest Resources	Minimum number of uniformed fisheries officers maintaining operational coverage for priority fishing activity periods, as defined by the Compliance Strategic Assessment	This performance measure is proposed to be discontinued as it has been replaced by the 2015-16 performance measure 'Proportion of uniformed fisheries officers maintaining operational coverage for priority fishing activity periods, as defined by the Compliance Strategic Assessment'. The new measure uses proportion as the revised methodology to more accurately measure activity. (p.358)	The Department further indicated that it will reinstate this performance measure. <sup>(d)</sup>
	The unit of measure has been amended from a number to a proportion of total uniformed fisheries officers rostered for out of hours coverage. This more accurately defines the relative level of resourcing assigned to this education and enforcement strategic priority. (p.147)		

Output	Measure	Explanation given in the budget papers	Committee comment
Taxi and Hire Vehicle Services	Taxis and hire vehicles conform to safety and quality standards	This performance measure is proposed to be discontinued as it has been replaced by the 2015-16 performance measure, 'Average safety and quality rating for metropolitan taxi vehicles' which utilises a new and more robust methodology to measure the safety and quality standards of a large sample of metropolitan taxis. The safety and quality of hire vehicles is determined by improved competition under the Government's reforms rather than ongoing compliance and enforcement activity.	<p>The Minister for Finance further indicated that 'Implementation of the Government's reforms of hire vehicles have increased competition by reducing the number of operating zones in Victoria to two, lowered licence prices for new entrants and allowed for hire vehicles which are not required to meet the luxury vehicle tax threshold. With increased competition and customer choice in the market, hire vehicle licence holders and operators will need to continue to improve on and maintain high safety and quality vehicle standards in order to meet customer demands for safe, clean and comfortable point-to-point transport services ... Narrowing the reporting focus through the State Budget on taxi safety and quality will ensure that PAEC is informed on the source of most significant risk'.<sup>(e)</sup></p> <p>The Committee does not support the discontinuation of this performance measure. The Committee considers that narrowing the report focus by removing the assessment of hire vehicles and focusing only on the metropolitan taxi vehicles will provide less information to the Parliament and the community. The Committee believes that increased competition and customer choice in the market does not necessarily ensure that hire vehicles would meet expected safety and quality standards. Therefore, the Committee recommends this measure be retained.</p>
Tourism, Major Events and International Education	Value of media coverage generated: domestic	The performance measure is proposed to be discontinued as it is no longer an effective measure and has been replaced by the 2015-16 performance measures 'Links from Tourism Victoria consumer sites' and 'Visitors to Tourism Victoria consumer websites' to reflect the significance of digital communications in positioning Victoria as a leisure tourism destination. <sup>(b)</sup>	<p>The Department sought to discontinue these measures in the 2012-13 Budget for similar reasons. At that time, the Committee accepted the limitations of the measures and recommended that the Department develop new measures of social media to supplement these measures, modify its survey instruments or develop new, more comprehensive measures.</p> <p>The Committee welcomes the Department's new measures related to its websites. However, these measures do not provide any indication of the effectiveness of the Department's efforts to penetrate traditional media.</p> <p>The Committee considers that it is important for traditional media to be measured so long as the Department is still using traditional media to promote Victoria to tourists. If these performance measures are not effective or specific, the Department should develop more appropriate measures of traditional media. Until that is done, the Committee does not consider it appropriate to discontinue these measures.</p> <p>The Committee also notes that the removal of these measures leaves the output with no quality measures. The Committee considers that every output should have at least one measure of the quality of its service delivery.</p>
	Value of media coverage generated: international	The performance measure is proposed to be discontinued as it is no longer an effective measure and has been replaced by the 2015-16 performance measures 'Links from Tourism Victoria consumer sites' and 'Visitors to Tourism Victoria consumer websites' to reflect the significance of digital communications in positioning Victoria as a leisure tourism destination. <sup>(b)</sup>	
	Victoria's share of domestic tourism advertising awareness among target markets: interstate	This performance measure is proposed to be discontinued as it is no longer relevant. The performance measure does not accurately measure awareness of tourism advertising linked directly to government programs. <sup>(c)</sup>	
	Victoria's share of domestic tourism advertising awareness among target markets: intrastate	This performance measure is proposed to be discontinued as it is no longer relevant. The performance measure does not accurately measure awareness of tourism advertising linked directly to government programs. <sup>(c)</sup>	



Output	Measure	Explanation given in the budget papers	Committee comment
Transport Safety, Security and Emergency Management	Transport safety regulation: rail safety audits/compliance inspections conducted in accordance with legislative requirements	This performance measure is proposed to be discontinued as it has been replaced by the 2015-16 performance measure 'Rail safety audits, compliance inspections and investigations conducted in accordance with State and National legislative requirements and timelines' to better reflect State and National agreements.	The Department further indicated that the Department/Public Transport Safety Victoria now also has regulatory obligations under the Office of the National Rail Safety Regulator (ONRSR) as well as the existing obligations. The ONRSR sets deliverables and determines regulatory efforts and this is not covered in the scope of the original measure. <sup>(c)</sup>  The Committee notes that where the measure proposed for discontinuation identified the number of audits and inspections conducted, the new measure tracks the proportion of audits, inspections and investigations that meet legislative requirements and timelines. The Committee considers that meeting legislative requirements is a basic requirement for a department and that, in most cases, departmental performance measures should be setting higher standards. As such, the Committee considers that the old measure, which indicated the number of audits/inspections, is more informative, as it gives some indication of the scale of activities. If the Department wishes to set a quality measure, it should set targets that are more ambitious than simply meeting the minimum standards of legislation.  The Department may wish to indicate what regulatory and compliance obligations have been met, including both responsibilities under the ONRSR and others.
(a)	Correspondence from Richard Bolt, Secretary, Department of Economic Development, Jobs, Transport and Resources to Chair, Public Accounts and Estimates Committee, received 18 September 2015.	(c)	The Department further indicated that this performance measure and the measure 'Victoria's share of domestic tourism advertising awareness among target markets: intrastate' no longer accurately measures awareness of tourism advertising linked to government programs. The syndicated research tool used for this indicator is owned by Roy Morgan Research and paid for by Tourism Victoria. It measures the share of awareness of tourism advertising for Victoria as a whole which includes Tourism Victoria's activities and other advertising, for example, this tool also measures awareness of advertising by Jetstar, Crown, etc. The tool does not have the capacity to identify Tourism Victoria's independent contribution to advertising awareness. Furthermore, the results generated by this research tool are influenced more by traditional forms of media (free to air TV, mainstream print media), whereas Tourism Victoria's activities are increasingly directed towards generating awareness through advertisements in digital and social media and segment-focused magazines (i.e. food and wine publications) (Correspondence from Richard Bolt, Secretary, Department of Economic Development, Jobs, Transport and Resources to Chair, Public Accounts and Estimates Committee, received 18 September 2015).
(b)	The Department further indicated that when this measure and the 'value of media coverage generated: international' were introduced, 'value of media generated reflected only the traditional public relations and media familiarisations activities undertaken by Tourism Victoria. This indicator measures the dollar value of media generated by these activities by calculating the cost of this media; if it were purchased for advertising (known as Advertising Value Equivalency (AVE)). AVE is best used for traditional media, although it is able to be measured for digital media where there is a valid print or other traditional equivalent. At this stage, there is no commercial standard for measuring the AVE of non-traditional digital media, such as blogs or social media. While activities engaging traditional media are continuing, Tourism Victoria's activities are increasingly directed towards digital media (website, blogs and social media). A key digital tool is the consumer-facing website visitvictoria.com. The measure that is proposed to be discontinued does not cover these key digital media tools, including the visitvictoria.com website' (Correspondence from Richard Bolt, Secretary, Department of Economic Development, Jobs, Transport and Resources to Chair, Public Accounts and Estimates Committee, received 18 September 2015).	(d)	Correspondence from Richard Bolt, Secretary, Department of Economic Development, Jobs, Transport and Resources, to Chair, Public Accounts and Estimates Committee, received 13 October 2015.
		(e)	Correspondence from the Hon. Robin Scott MP, Minister for Finance, to Chair, Public Accounts and Estimates Committee, received 24 June 2015.
		(f)	Correspondence from Richard Bolt, Secretary, Department of Economic Development, Jobs, Transport and Resources, to Chair, Public Accounts and Estimates Committee, received 18 September 2015.

### Department of Justice and Regulation

Output	Measure	Explanation given in the budget papers	Committee comment
Gambling and Liquor Regulation and Racing Industry Development	Liquor and gambling compliance inspection outcomes provided within set timeframes (VCGLR)	This performance measure is proposed to be discontinued as it has been replaced in 2015-16 with the performance measure 'Liquor and gambling inspections completed within set time (VCGLR)'. The new performance measure is a more accurate reflection of the services provided by VCGLR and aligns with the new quantity based performance measures 'Liquor and gambling inspections completed: metropolitan' and 'Liquor and gambling inspections completed: regional'.  On p.291, Budget Paper No.3 indicates that the measure has been replaced by 'Liquor and gambling approvals, licence, permit applications and variations completed within set time (VCGLR)'.	The new measure 'Liquor and gambling inspections completed within set time (VCGLR)' does not appear in the budget papers. The measure 'Liquor and gambling approvals, licence, permit applications and variations completed within set time (VCGLR)' does not cover the same activities, according to the details provided in the budget papers. Therefore, the Committee recommends this measure be retained.

### Department of Premier and Cabinet

Output	Measure	Explanation given in the budget papers	Committee comment
Arts Portfolio Agencies	Public Record Office Victoria: records transferred	This performance measure is proposed to be discontinued as it has been consolidated into the 2015-16 performance measure 'Collection Usage: utilisation of physical and digital records held by PROV'.	The Department further indicated that this aspect of service delivery will be reported through 'Collection usage: utilisation of physical and digital records held by PROV' and that both measures will still be measured internally and reported through the annual report. <sup>(a)</sup>
	Public Record Office Victoria: digital records preserved	This performance measure is proposed to be discontinued as it has been consolidated into the 2015-16 performance measure 'Collection Usage: utilisation of physical and digital records held by PROV'.	The Committee welcomes the addition of the new performance measure. However, it understands that there is a significant volume of material kept which is not accessed in any year. The Committee considers that this should still be measured as part of the Department's activities. If the measures are still considered by the Department to be sufficiently meaningful to measure and report as part of the Department's annual report, the Committee considers it appropriate to continue reporting this activity as part of the Department's performance measures.
Anti-Corruption and Public Sector Integrity	Corruption prevention initiatives delivered by IBAC	This performance measure is proposed to be discontinued as a result of a departmental review to improve clarity around its output delivery and ensure measures demonstrate output efficiency and effectiveness. Retained measures in relation to IBAC include: 'Proportion of Independent Broad-Based Anti-Corruption Commissions investigations completed within 12 months', 'Satisfaction rating with IBAC's prevention and education initiatives delivered to stakeholders', and 'Complaints or notifications assessed by IBAC within 45 days'.	The Department further indicated that this measure is no longer relevant as IBAC has now developed a strategy which has matured IBAC's approach to corruption prevention. <sup>(a)</sup>  The Committee considers that, if this measure is discontinued, there would be no measure indicating the scale of corruption prevention activities as part of IBAC's Corruption Prevention Strategy. The Committee recommends this measure be retained until a new measure related to IBAC's prevention activities is introduced.

Output	Measure	Explanation given in the budget papers	Committee comment
Chief Parliamentary Counsel Services	Advice given on legislation in response to written requests	This performance measure is proposed to be discontinued as it is no longer relevant because it reflects activity that is not influenced by the Chief Parliamentary Counsel Services. The Chief Parliamentary Counsel will continue to provide advice on legislation in response to written requests.	The Department further indicated that, for both of these measures, variables measured are not within the Department's control. In the case of the measure 'Advice given on legislation in response to written requests', the Department has indicated that the Office will always respond to requests for information. For the measure 'Statutory rules made and bills prepared and introduced into Parliament', the Department has indicated that the measure takes no account of the complexity of the work undertaken. <sup>(a)</sup>
	Statutory rules made and bills prepared and introduced into Parliament	This performance measure is proposed to be discontinued as it is no longer relevant because it reflects activity that is not influenced by the Chief Parliamentary Counsel Services. The Chief Parliamentary Counsel will continue to prepare and introduce into Parliament Statutory Rules made and Bills.	The Committee understands the demand-driven nature of these performance measures. However, it considers that, without measures of workload, it would be difficult to assess the efficiency of services provided. Alternatively, new measures reflecting this workload could be introduced. The Committee recommends these measures be retained until new measures reflecting the Chief Parliamentary Counsel's workload are introduced.
Freedom of Information (FOI) Commissioner	Education and training activities delivered by FOI Commissioner	This performance measure is proposed to be discontinued as a result of a departmental review to improve clarity around its output delivery and ensure measures demonstrate output efficiency and effectiveness.	The Department further indicated that this measure is no longer relevant in alignment with the maturity of the organisation and that it does not capture the full extent of related activities being undertaken. However, the performance measure will still be published in the annual report. <sup>(a)</sup>
Ombudsman services	Jurisdictional complaints finalised (VO)	This performance measure is proposed to be discontinued as it has been consolidated into the 2015-16 performance measure 'Proportion of jurisdictional complaints independently investigated by Victorian Ombudsman'.	The Committee recommends this measure be retained until new measures are introduced measuring the Commissioner's education and training activities, as this is a matter of public interest. Additionally, if the measure is still considered by the Department to be sufficiently meaningful to measure and report as part of the Department's annual report, the Committee considers it appropriate to continue reporting this activity as part of the Department's performance measures.
	Proportion of jurisdictional complaints where the original outcome is set aside by a review undertaken in accordance with the Ombudsman's internal review policy	This performance measure is proposed to be discontinued as it has been consolidated into the 2015-16 performance measure 'Proportion of jurisdictional complaints independently investigated by the Victorian Ombudsman'.	The Department further indicated that the Ombudsman has no control over the number of complaints it receives and that the replacement measure provides a greater indicator of effectiveness and efficiency. <sup>(a)</sup>
			The Committee understands the demand-driven nature of this performance measure. However, this measure provides useful information about the workload that the Office faces, which the new measure does not. Without this information, it is difficult to assess the efficiency of services. It is therefore recommended that this measure be retained or other measures indicating the workload of the Office be introduced.
			The Committee considers that the remaining quality measure for this output does not provide as meaningful and independent a test of the quality of the Ombudsman's investigations. Additionally, the quantity measure previously stated by the Department does not seem to be equivalent to the proposed discontinued quality measure.

Output	Measure	Explanation given in the budget papers	Committee comment
Aboriginal Community and Cultural Development	Client service contacts for members of the Stolen Generations with Connecting Home Limited  Client service contacts for members of the Stolen Generations with the Victorian Koorie Family History Service	These performance measures are proposed to be discontinued as a result of a department review to improve clarity around its output delivery and ensure measures demonstrate output efficiency and effectiveness.	The Department further indicated that for both of these measures it is difficult to capture an accurate picture of client numbers on an annual basis due to the complex nature of this type of service delivery as cases may remain open but clients may not utilise the service for extended periods. <sup>(a)</sup>  The Committee understands the complex nature of measuring these activities as indicated by the Department. However, the Committee considers that the removal of these measures would lead to a less comprehensive measurement of the Department's activities by no longer providing any information related to these activities. Therefore, the Committee recommends these performance measures be retained until new measures related to this matter of public interest are introduced.
Multicultural Affairs and Citizenship	Grants approved	This performance measure is proposed to be discontinued as a result of a department review to improve clarity around its output delivery and ensure measures demonstrate output efficiency and effectiveness.	The Department further indicated that this measure was first introduced to indicate the number of community organisations and that the measure now incorporates five grants programs and does not provide information on the effect of the grants. This measure is proposed to be replaced by the new measure 'Proportion of grants approved which are provided to organisations in regional/rural areas'. <sup>(a)</sup>  The Committee considers that a quantity measure is also important, so that changes to the scale of these activities over time can be understood. Therefore, it recommends this performance measure be retained.
Office of Women's Affairs	Number of women participating in funded programs, projects and events	This performance measure is proposed to be discontinued as it does not accurately reflect Government priorities regarding policy and programs for Women.	The Department further indicated that 'in reviewing the remaining funding agreements it was considered that new measures of success were required as the measure of numbers alone did not provide information about the quality of the interaction or engagement or whether women engaged in more than one activity'. <sup>(a)</sup>  The Committee notes that the description of the Department's new output (Women and Equality Policy and Programs) indicates that it includes 'deliver[ing] initiatives that support the economic, social and civic participation of Victorians', which is similar to the description of the former Office of Women's Affairs output. However, the proposed measures for the new output only relate to actions in relation to 'Women and the Prevention of Family Violence' and policy analysis and papers. The Committee considers that in its current form, the measure does not accurately reflect the ends of the Department's output. However, of the discontinued measures from the former Office of Women's Affairs output, this is the only one which the Department indicates is likely to reflect ongoing activities (its 2015-16 target is 1,450 women). As this appears to be the only measure that might capture activities for women other than prevention of family violence and policy analysis and papers, the Committee considers that it should be retained or new measures capturing the other work undertaken within the output be introduced.

(a) Correspondence from Chris Eccles, Secretary, Department of Premier and Cabinet, to Chair, Public Accounts and Estimates Committee, received 10 September 2015.

## Department of Treasury and Finance

Output	Measure	Explanation given in the budget papers	Committee comment
Budget and Financial Policy Advice <sup>(a)</sup>	Budget and financial policy advice through ministerial briefs, Budget and Expenditure Review Committee and Cabinet Sub Committee briefs	This performance measure is proposed to be discontinued as evaluation of the Department's policy advice for this output will be included in the objective indicator for the 'Sound financial management of Victoria's fiscal resources' objective.	The Committee agrees that some of these measures are not ideal and a number of them were highlighted by the previous Committee in its report on the performance measurement system. However, if all of these measures were discontinued, there would be no quantity measures for these outputs. Quantity measures (in combination with cost measures) are important for assessing the efficiency with which outputs are delivered, which is one of the purposes of the performance measurement system. The Committee recommends that either these measures be retained or other, more comprehensive measures indicating the quantity of work undertaken in these outputs be established.
Financial Reporting	Estimates reporting - Budget, Budget Update and Pre-Election Budget Update	This performance measure is proposed to be discontinued as the work described by this measure is adequately addressed in the measure 'Delivery of Cost Control and Efficiency Review reports within agreed timeframes'.	
	Financial performance reporting - Annual Financial Report, Mid-Year Financial Report and Quarterly Financial Reports	This performance measure is proposed to be discontinued as the work described by this measure is adequately addressed in the measures 'Annual Budget published by date agreed by Treasurer' and 'Budget Update, Financial Report for the State of Victoria, Mid-Year Financial Report, and Quarterly Financial Reports are transmitted by legislated timeline'.	
Financial and Resource Management Frameworks	Annual review of whole of government compliance framework	This performance measure is proposed to be discontinued as the work described by this measure is adequately addressed in the measure 'Budget Update, Financial Report for the State of Victoria, Mid-Year Financial Report, and Quarterly Financial Reports are transmitted by legislated timeline'.	
Maintenance and Support	Delivery of updates, guides and newsletters	This performance measure is proposed to be discontinued as the work described by this measure is adequately addressed in the measure 'YPS stakeholder feedback indicates delivery of advice and information sessions supported the VPS to understand the financial management framework'. <sup>(c)</sup>	
	Review of major resource management policies	This performance measure is proposed to be discontinued as the work described by this measure is adequately addressed in the measure 'Annual financial management compliance report for the previous financial year is submitted to the Minister for Finance'.	

Output	Measure	Explanation given in the budget papers	Committee comment
Economic and Financial Policy <sup>(d)</sup>	Briefings on Cabinet submissions	This performance measure is proposed to be discontinued as evaluation of the Department's policy advice for this output will be included in the objective indicator for the 'Guide Government actions to increase Victoria's productivity and competitiveness' objective.	
	Written ministerial briefs	This performance measure is proposed to be discontinued as evaluation of the Department's policy advice for this output will be included in the objective indicator for the 'Guide Government actions to increase Victoria's productivity and competitiveness' objective.	
	Long-term research projects completed	This performance measure is proposed to be discontinued as it is no longer relevant. <sup>(e)</sup>	
	Long-term research projects managed within agreed timeframes	This performance measure is proposed to be discontinued as it is no longer relevant. <sup>(e)</sup>	
	Annual performance and compliance review of registered housing agencies	This performance measure is proposed to be discontinued as it has been replaced by the 2015-16 performance measure 'Registered housing agencies that are annually reviewed'. The new measure is a quality performance measure.	
GBE Performance Monitoring and Financial Risk Management <sup>(f)</sup>	Corporate plans reviewed and assessed and quarterly performance reports	This performance measure is proposed to be discontinued as the work described by this measure is adequately addressed in the measure 'Analysis and review of corporate plans within two months of receipt'.	
	Provide financial policy advice on borrowings, investments, insurance, and superannuation issues and prudential supervision	This performance measure is proposed to be discontinued as evaluation of the Department's policy advice for this output will be included in the objective indicator for the 'Sound financial management of Victoria's fiscal resources' objective.	
(a)	The Department has further indicated that it will provide qualitative data for its policy advice objective indicators in the 2015-16 annual report (Correspondence from David Martine, Secretary, Department of Treasury and Finance, to Chair, Public Accounts and Estimates Committee, received 2 September 2015).		(d) The Department has further indicated that it will provide qualitative data for this output in the objective indicator 'Guide Government actions to increase Victoria's productivity and competitiveness' objective in the 2015-16 annual report (Correspondence from David Martine, Secretary, Department of Treasury and Finance, to Chair, Public Accounts and Estimates Committee, received 2 September 2015).
(b)	The Department has further indicated that 'the nature of this review has changed and this quantity measure no longer accurately reflects the work of the output' (Correspondence from David Martine, Secretary, Department of Treasury and Finance, to Chair, Public Accounts and Estimates Committee, received 2 September 2015).		(e) The Department has further indicated that it will 'continue to undertake long-term economic research to underpin advice on a broad range of policy issues. However, it is no longer appropriate to include a performance measure that arbitrarily defines a discrete number of projects for the purposes of reporting'. (Correspondence from the Hon. Robin Scott MP, Minister for Finance, to Chair, Public Accounts and Estimates Committee, received 24 June 2015, p.2).
(c)	The Department has further indicated that 'a count of the communications with Government agencies does not evaluate the effectiveness of the information conveyed [and that] The measure is better evaluated by the quality measure VPS stakeholder feedback indicates that delivery of guidelines, newsletters, information sessions and training has improved the VPS awareness and understanding of accounting policy and financial management' (Correspondence from David Martine, Secretary, Department of Treasury and Finance, to Chair, Public Accounts and Estimates Committee, received 2 September 2015).		(f) The Department has further indicated that it will provide qualitative data for this output in the objective indicator 'Sound financial management of Victoria's fiscal resources' objective in the 2015-16 annual report (Correspondence from David Martine, Secretary, Department of Treasury and Finance, to Chair, Public Accounts and Estimates Committee, received 2 September 2015).

## Courts

Output	Measure	Explanation given in the budget papers	Committee comment
Courts	Civil matters disposed in the Supreme Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Civil matters disposed in the Supreme Court’.	Courts Services Victoria further explained: <sup>(a)</sup> The discontinuation of the measures is proposed as part of an overarching shift to provide more meaningful and appropriate measures which align with the International Framework for Court Excellence (IFCE).
	Civil matters disposed in the County Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Civil matters disposed in the County Court’.	...
	Civil matters disposed in the Magistrates’ Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Civil matters disposed in the Magistrates’ Court’.	The new case clearance rate measure reflects one of the eleven Global Measures of Court Performance under the IFCE. Case clearance rate is considered to be a superior performance measure to matters disposed.
	Civil matters disposed in the Victorian Civil and Administrative Tribunal	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Civil matters disposed in the Victorian Civil and Administrative Tribunal’.	...
	Child protection matters disposed in the Children’s Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Child protection matters disposed in the Children’s Court’.	An individual case may be disposed of with minimal work being undertaken by a court (a simple debt recovery matter disposed of by a default judgment), or it can consume a vast amount of time and resources (a long running complex trial). A jurisdiction may experience a spike in filings in debt recovery proceedings with minimal impact on workload but this will show up as a significant increase in disposals. A jurisdiction may experience only a small increase in the number of cases but a significant increase in workload due to the complexity of the cases. This is reflected in disposal figures. Resolution of a single matter may resolve thousands of individual claims, or even avoid many proceedings being brought to court at all; disposal figures cannot reflect this and can distort the real picture.
	Coronial matters disposed in the Coroner’s Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Coronial matters disposed in the Coroners’ Court’.	...
	Criminal matters disposed in the Supreme Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Criminal matters disposed in the Supreme Court’.	The revenue certification process includes an assessment by DTF of whether the agreed outputs have been delivered and agreed targets specified in the budget papers have been met. It is not considered appropriate to set disposal targets for the jurisdictions in an environment where they do not control demand. Setting a target figure for the number of disposals conceptually suggests that the jurisdictions should seek out additional cases if demand declines, which is clearly inappropriate and I am sure not reflective of the intention of the Parliament or the Committee.
	Criminal matters disposed in the County Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Criminal matters disposed in the County Court’.	The Committee understands the demand-driven nature and limitations of these performance measures. However, it considers that it is important for there to be measures which reflect the workload that CSV faces. Without measures of workload, it would be difficult to assess the efficiency of services provided. The Committee would consider it appropriate for new measures of workload to be introduced. However, the Committee recommends these measures be retained until new measures reflecting workload for this area are introduced.
	Criminal matters disposed in the Magistrates’ Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Criminal matters disposed in the Magistrates’ Court’.	
	Criminal matters disposed in the Children’s Court	This performance measure is proposed to be discontinued as it has been replaced by the 2015–16 performance measure ‘Case clearance rate – Criminal matters disposed in the Children’s Court’.	

(a) Correspondence from Michael Carroll, Acting Chief Executive Officer, Courts Services Victoria, to Chair, Public Accounts and Estimates Committee, received 31 August 2015. Source: Department of Treasury and Finance, *Budget Paper No.3: Service Delivery 2015-16* (2015), Appendix A.





# Appendix 11

## The Government's Responses to the Former Committee's Report on the 2014-15 Budget Estimates

### A11.1 Recommendations of the former Public Accounts and Estimates Committee relating to the review of the *Guidelines for Submissions and Responses to Inquiries*

Report	Recommendation
<i>Report on the 2011-12 Budget Estimates – Part Three, Recommendation 84, p.234</i>	In future responses to the Committee's recommendations, the Government indicate in the response column whether a Recommendation is fully or only partly supported.
<i>Report on the 2011-12 Budget Estimates – Part Three, Recommendation 85, p.236</i>	In future responses to the Committee's recommendations, the Government specify a timeframe by which a decision will be reached for each Recommendation classified as 'under review'.
<i>Report on the 2011-12 Budget Estimates – Part Three, Recommendation 86, p.236</i>	In future responses to the Committee's recommendations, the Government commit to updating the Public Accounts and Estimates Committee within three months of determining what action will be taken for each Recommendation classified as 'under review'.
<i>Report on the 2011-12 Budget Estimates – Part Three, Recommendation 87, p.237</i>	In future responses to the Committee's recommendations, for all recommendations with further action planned, the Government provide timelines by which it expects the actions to be completed.
<i>Report on the 2011-12 Budget Estimates – Part Three, Recommendation 88, p.237</i>	The Department of Treasury and Finance clarify for the Government the differences between the classification 'under review' and 'support'.
<i>Report on the 2011-12 Budget Estimates – Part Three, Recommendation 90, p.241</i>	In future responses to the Committee's recommendations, in describing any further actions planned, the Government specify: <ul style="list-style-type: none"> <li>(a) whether those actions will definitely include what the Committee has recommended; and</li> <li>(b) whether the planned actions will fully or partly implement the recommendation.</li> </ul>
<i>Report on the 2012-13 Budget Estimates – Part Two, Recommendation 50, p.156</i>	The Government establish and publish guidelines for the implementation of Parliamentary Committee recommendations. These guidelines should include: <ul style="list-style-type: none"> <li>(a) a mechanism for assigning responsibility for the implementation of recommendations;</li> <li>(b) processes for monitoring the implementation of positively received recommendations; and</li> <li>(c) a system for reporting on the implementation of positively received recommendations.</li> </ul>
<i>Report on the 2012-13 Budget Estimates – Part Two, Recommendation 51, p.157</i>	In the development of guidelines for the implementation of Parliamentary Committee recommendations, the Government consider as a model the Australian Capital Territory's Guidelines for Responding to Reports by the Auditor-General.

Report	Recommendation
<i>Report on the 2012-13 Budget Estimates – Part Two</i> , Recommendation 52, p.162	The Government establish and publish processes and guidance for responses to Parliamentary Committee recommendations to ensure: <ul style="list-style-type: none"> <li>(a) decisions about whether or not to support recommendations are based on current and accurate information;</li> <li>(b) responses clearly address the recommendations' substance as well as intent;</li> <li>(c) responses are classified in a way that enables consistent interpretation of the Government's intent; and</li> <li>(d) the expectations associated with a particular response type are explicit.</li> </ul>
<i>Report on the 2012-13 Budget Estimates – Part Two</i> , Recommendation 53, p.163	The Government assign the Department of Premier and Cabinet or the Department of Treasury and Finance responsibility for the quality assurance of responses to Parliamentary Committee recommendations. This should include ensuring that each response meets defined criteria for clearly and consistently representing the Government's intentions in relation to the recommendations.
<i>Report on the 2011-12 Financial and Performance Outcomes</i> , Recommendation 18, p.91	In future responses to Committee recommendations, where the Government's view of the cause of a problem differs from that expressed in the Committee's report in support of a recommendation, the Government should indicate why it does not accept the Committee's view.
<i>Report on the 2013-14 Budget Estimates – Part Two</i> , Recommendation 39, p.181	As part of its review of guidelines for responding to inquiries, the Department of Premier and Cabinet provide a clear definition of the conditions under which a Recommendation should be considered to be implemented.
<i>Report on the 2013-14 Budget Estimates – Part Two</i> , Recommendation 40, p.181	Following its investigation, the Department of Treasury and Finance implement a system to inform committees about the ultimate decisions on all recommendations initially classified as 'under review'.
<i>Report on the 2013-14 Budget Estimates – Part Two</i> , Recommendation 41, p.182	The Department of Premier and Cabinet liaise with the Department of Treasury and Finance to ensure that any new guidelines for responding to inquiries incorporate any system developed by the Department of Treasury and Finance to inform the Committee about recommendations initially responded to as 'under review'.
<i>Report on the 2013-14 Budget Estimates – Part Two</i> , Recommendation 42, p.182	As part of its review of guidelines for responding to inquiries, the Department of Premier and Cabinet develop a procedure to inform committees when the Government changes its response to a Recommendation prior to implementation.
<i>Report on the 2012-13 Financial and Performance Outcomes</i> , Recommendation 10, p.118	Government responses supporting the Committee's recommendations that cite proposed review action include, to the extent possible, specific details of the planned reviews and their associated timelines. This approach would assist the Parliament's consideration of the responses.

A11

# Extract from the minutes of proceedings

## Report on the 2015-16 Budget Estimates Consideration and adoption of draft report for tabling

**Monday 19 October 2015**

**No. 1. Chapter 4: Revenue plus Appendix**

Question – That Chapter 4: Revenue plus Appendix be agreed to.

*The Committee divided.*

**Ayes**

Danny Pearson MP  
Harriet Shing MLC  
Steve Dimopoulos MP  
Dr Rachel Carling-Jenkins MLC  
Sue Pennicuik MLC

**Noes**

David Morris MP  
Danny O'Brien MP

*Resolved in the affirmative.*

**No. 2. Report and Appendices**

Question – That subject to minor amendments the whole of the Report on the 2015-16 Budget Estimates Inquiry plus Appendices be agreed to.

*The Committee divided.*

**Ayes**

Danny Pearson MP  
Harriet Shing MLC  
Steve Dimopoulos MP  
Dr Rachel Carling-Jenkins MLC  
Sue Pennicuik MLC

**Noes**

David Morris MP  
Danny O'Brien MP

*Resolved in the affirmative.*



**PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE**

**INQUIRY INTO THE BUDGET ESTIMATES 2015-16**

**MINORITY REPORT**

**Submitted by**

**David Morris MP – Deputy Chair**

**Danny O’Brien MP**

**Tim Smith MP**

## 1. Introduction

The Parliamentary Committees Act 2003 requires the Public Accounts and Estimates Committee to inquire into and report upon:

*the annual estimates or receipts and payments and other Budget papers and any supplementary estimates of receipts or payments presented to the Assembly and the Council<sup>1</sup>*

The Committee has completed that task for the 2015-16 financial year, and the accompanying majority report represents the findings of the inquiry.

## 2. Minority Findings

**The Minority make the following findings:**

### **Finding 1**

**The Andrews Government has failed to meet its election commitment to reform the conduct of the Public Accounts and Estimates Committee Estimates Hearings. (Section 4)**

### **Finding 2**

**The actions of the Andrews Government in failing to appoint the Public Accounts and Estimates Committee in a timely manner, and the Government's failure to respond to Committee Questionnaires in an appropriate time frame have been a significant impediment to the conduct of this Inquiry. (Section 5)**

### **Finding 3**

**The failure of the Andrews Government to appropriately account for the \$1.5 billion advanced to Victoria as the Commonwealth's contribution to the construction of the East West Link Stage 1 has resulted in the alleged \$1.2 billion operating surplus being overstated by that amount.**

**Had those funds been appropriately accounted for, the claimed operating surplus would in fact have been a deficit of \$300 million. (Section 6)**

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<sup>1</sup> Parliamentary Committees Act 2003 S14(1) (ii)

### **3. Limitations of the Committee Report.**

Minority members accept that the Committee has completed the inquiry to the extent possible, while noting the limitations placed on it by the less than transparent manner in which financial information is presented to the Parliament in the current format of the budget papers.

In particular the Minority notes:

- The lack of information provided to the Parliament and the public regarding all recurrent spending not the subject of new or on-going initiatives – often referred to as ‘base funding’. While it is possible to calculate the quantum of base funding, detailed reporting of programs and initiatives contained within the base is not disclosed in the budget papers.
- The budget papers provide little information on the re-allocation and re-prioritisation of funds.
- The section of the report devoted to consideration of Government revenue (Chapter 4) was not agreed. Minority concerns are addressed below.

### **4. Failure of the Andrews Government to Honour Election Commitments with regard to the conduct of the Estimates Hearings.**

In May 2014 the then Opposition issued a media release headed “More Government Scrutiny under Labor Reform Plan”. The release included the following:

*“Key Facts*

*Labor’s plan will:*

- *Introduce one day of hearings per Department.*
- *Allow Committee members to ask questions of relevant senior departmental officials.*
- *Allow Committee members to ask a series of questions about a single, serious issue.*
- *Ensure Ministers are not asked so-called ‘Dorothy Dixier’ questions with rehearsed answers.*
- *Enforce an equal number of Government and non-government members on the Committee”.*<sup>2</sup>

The Minority notes:

- No ‘Reform Plan’ was implemented for the 2015-16 Estimates Hearings, nor has any plan been considered since the hearings were completed.
- Committee members were not permitted to directly question senior department officials, despite their presence at the witness table.

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<sup>2</sup> ALP Media Release 21 May 2014

- Committee members were not permitted to ask a series of questions about a single, serious issue.
- In accordance with Legislative Assembly Sessional Orders, Members were permitted only to ask a substantive question, followed by a supplementary.
- A large number of ‘Dorothy Dix’ questions were asked, and answered, during the course of the hearings.

**Finding:**

**The Andrews Government has failed to meet its election commitment to reform the conduct of the Public Accounts and Estimates Committee Estimates Hearings.**

## 5. Government Failings.

The Minority notes:

- The Government failed to appoint a Public Accounts and Estimates Committee until 16 April 2015, less than three weeks prior to the introduction of the 2015 State Budget.
- The Committee of the 57<sup>th</sup> Parliament was appointed on the 10<sup>th</sup> February 2011, almost three months prior to the introduction of that years State Budget.
- As a consequence of the Government’s failure to appoint a Committee in a timely manner, department questionnaires were not issued by the Committee in sufficient time for a response to be received prior to the hearings.
- The absence of the information normally available to the Committee via the questionnaires was a significant impediment to the inquiry.
- Because the information was not received prior to the conclusion of the hearings, Committee Members were unable to seek further information, by way of oral questions or questions on notice, on any matters raised by the contents of the questionnaires.
- The delayed receipt of the questionnaires was exacerbated by significant delays on the part of some Departments in responding to the Committee’s requests for information.
- In the most extreme case a complete response from the Department of Health and Human Services was not received by the Committee until October 2015, more than four months after the estimates hearings, and three months after the commencement of the current financial year.



**Finding:**

**The actions of the Andrews Government in failing to appoint the Public Accounts and Estimates Committee in a timely manner, and the Government's failure to respond to Committee Questionnaires in an appropriate time frame have been a significant impediment to the conduct of this Inquiry.**

**6. Specific Purpose Revenue – East West Link Stage 1.**

Prior to the 2014 State Election, Victoria received a Commonwealth grant of \$1.5 billion, representing the Commonwealth contribution towards the construction of the proposed East West Link Stage 1.

Upon coming to office the Andrews Government abandoned the project, at significant cost to Victorian taxpayers. Despite cancelling the project, the Government failed to return the \$1.5 billion provided by the Commonwealth specifically for that purpose.

Nor was provision made in the 2015-16 Budget Papers for the return of these funds.

The Commonwealth budget, brought down on 12<sup>th</sup> May 2015, anticipated the return of the \$1.5 billion held by the State. The Herald Sun reported the following day:

*“VICTORIA must repay within 14 months the \$1.5 billion it received for the dumped East West Link project, according to Federal Budget papers. Repayment of the money, which was claimed yesterday by Treasurer Joe Hockey as a major boost to the Commonwealth bottom line, would hammer Victoria’s Budget and send it into deficit.”<sup>3</sup>*

On 14<sup>th</sup> May 2015 the Secretary of the Department of Treasury and Finance made his first appearance at the Estimates Hearings following the release of the Commonwealth Budget. As the following excerpt from the Hansard record of the hearing shows, the Government refused to allow members to directly question the Secretary on this issue:

***Mr MORRIS**—On a point of order, since Mr Martine, the secretary of DTF, last appeared the federal budget has been brought down, and if media reports are correct, at least one announcement has been made which may have a significant negative impact on the budget, to the tune of \$1.5 billion, on the set of estimates we are currently considering. That is clearly a matter for this department but perhaps not for this minister. I was wondering whether the Chair would allow a question directly to Mr Martine.*

***The CHAIR**—Thank you for your point of order. As has been agreed prior to these hearings, we are adopting the previous practice of PAEC, whereby questions are directed to ministers and ministers have the call in terms of whether they choose to refer a question on to a departmental representative. Obviously as we look at future years—perhaps next year and the year after—when we adopt more of a Senate-style approach, then that will be more likely to occur as a matter of course. But as we discussed before these hearings commenced, we will adhere to standard practice. It is up to the minister to determine whether he will hand a question from any member of the committee on to the department to answer.*

<sup>3</sup> Herald Sun ‘Show us East West Money’ 13 May 2014

*Mr SCOTT—I am happy to answer a question.*

*Mr MORRIS—It is entirely outside your portfolio. That is why I have raised it with the Chair, with the intention of seeking an answer from the secretary.*

*Ms WARD—The ruling has been made, so I suspect we are up to your question.*

*The CHAIR—I have ruled. It is up to the minister to determine whether he will pass a question any member of the committee raises to a departmental representative to answer.*<sup>4</sup>

The Minister refused to allow the Secretary to respond directly to the Committee.

In the period between the hearings and the finalisation of this inquiry a series of media reports have suggested a number of alternative projects to which the Commonwealth may be prepared to reallocate funds.

Negotiations are ongoing, with the Commonwealth Treasurer telling 3AW on 28<sup>th</sup> October:

*“No we haven’t arrived at a final agreement yet but we are in very good faith discussions between Tim Pallas and I. I mean the \$1.5 billion was given by the Prime Minister Tony Abbott at the time and Joe Hockey to build the East West Link. It wasn’t a gift voucher for anything people wanted to think about and dream up. It was for the East West Link”.*<sup>5</sup>

The Minority notes that while subsequent discussions may well result in a change of Commonwealth policy regarding repayment of the funds (a change of policy the minority would welcome) the Budget Papers do not accurately reflect the true financial position of the State of Victoria.

**Finding:**

**The failure of the Andrews Government to appropriately account for the \$1.5 billion advanced to Victoria as the Commonwealth’s contribution to the construction of the East West Link Stage 1 has resulted in the alleged \$1.2 billion operating surplus being overstated by that amount.**

**Had those funds been appropriately accounted for the claimed operating surplus would in fact have been a deficit of \$300 million.**

David Morris MP, Deputy Chair  
Danny O’Brien MP  
Tim Smith MP

Melbourne 28<sup>th</sup> October 2015

<sup>4</sup> Hansard: Public Accounts and Estimates Committee – Finance Page 4 14<sup>th</sup> May 2015

<sup>5</sup> Hon Scott Morrison Interview with Neil Mitchell 3AW 28 October 2015

# 120 years of scrutiny

## Australia's first Committee of Public Accounts was established in Victoria in 1895.

From the beginning, the Committee has sought to improve the accessibility of the Government's public accounts. In examining the financial statements of the time, the very first report noted that, 'The form in which the information is prepared does not appear to enable the public to easily understand the accounts.'



**William Shiels**  
First Chair of the Committee  
of Public Accounts (and  
16<sup>th</sup> Premier of Victoria).

Successive committees since then have kept pressure on the Government to be more transparent, accountable and responsible for how it spends public money. The scope of the Committee's activities has grown since 1895 and it now reviews budgets, departments' performance and the activities of the Auditor-General, along with various specific issues.

The Committee continues to recommend improvements, advocates best practice and identifies areas where reporting could be improved.

*This is the 301<sup>st</sup> report released by the Public Accounts and Estimates Committee or its predecessors since 1895.*

