VERIFIED VERSION

PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

Inquiry into budget estimates 2015–16

Melbourne — 8 May 2015

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Mr David Martine, Secretary,

Ms Melissa Skilbeck, Deputy Secretary, Budget and Finance,

Mr David Webster, Deputy Secretary, Commercial, and

Mr Michael Brennan, Deputy Secretary, Economic, Department of Treasury and Finance.

The CHAIR — I declare open the public hearings for the Public Accounts and Estimates Committee inquiry into the 2015–16 budget estimates. All mobile telephones should now be turned to silent.

I would like to welcome to the hearing the Treasurer of Victoria, the Honourable Tim Pallas, MP; Mr David Martine, Secretary of the Department of Treasury and Finance; Ms Melissa Skilbeck, Deputy Secretary, Budget and Finance, Department of Treasury and Finance; Mr David Webster, Deputy Secretary, Commercial, Department of Treasury and Finance; and Mr Michael Brennan, Deputy Secretary, Economic.

All evidence is taken by this committee under the provisions of the Parliamentary Committees Act, attracts parliamentary privilege and is protected from judicial review. Any comments made outside the hearing, including on social media, are not afforded such privilege. The committee does not require witnesses to be sworn, but questions must be answered fully, accurately and truthfully. Witnesses found to be giving false or misleading evidence may be in contempt of Parliament and subject to penalty.

All evidence given today is being recorded by Hansard. You will be provided with proof versions of the transcripts for verification as soon as available. Verified transcripts, PowerPoint presentations and handouts will be placed on the committee's website as soon as possible.

Departmental officers may approach the table during the hearing to provide information to the witnesses if requested, by leave of myself. However, written communication to witnesses can only be provided via officers of the PAEC secretariat. Members of the public gallery cannot participate in the committee's proceedings in any way.

Members of the media are to observe the following guidelines: cameras must remain focused only on the persons speaking; operators must not pan the public gallery, the committee or witnesses; and filming and recording must cease immediately at the completion of the hearing.

I invite the witness to make a very brief opening statement of no more than 10 minutes. This will be followed by questions from the committee.

Mr PALLAS — Thanks very much, Chair. It gives me great pleasure to be here this morning and address you about the 2015–16 Victorian budget, a budget that in one word is about delivering. This budget gets on with the projects that our state needs and it puts people first. The budget delivers on 96 per cent of the commitments that the government took to the people of Victoria at the last election, and we are doing what we said we would do. It is the biggest ever education budget, it includes a massive boost to health, it commits record funding for public transport and it supports the creation of 100 000 jobs.

We are delivering a $1.2 billion operating surplus in 2015–16, growing that to $1.8 billion in 2018–19, and our projected surpluses are almost double the operating results actually achieved by the previous government when in office. 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. We are reducing net debt from its June 2014 peak of 6 per cent of GSP to 4.4 per cent by June of 2019. This is a responsible level of net debt, and it is lower than estimated by the previous government.

This budget funds an extensive infrastructure program, with $5.2 billion in capital expenditure this year, and $6.5 billion in capital expenditure next year. This is well above the average $4.9 billion delivered over the previous 10 years. More than $17 billion will be invested in roads and public transport projects to ease congestion, to stimulate the economy, to create jobs and to enable people to move in and around Melbourne and Victoria.

This government believes that a good education for kids gives them the best start in life. This government believes that all jobs start with skills, and we know that all skills start at school. That is why this budget invests $3.9 billion in education and skills over four years, making it the biggest education budget in Victoria's history. Two point nine billion of this is for schools, the biggest cash injection into our school system ever made. This budget invests $350 million in TAFE; $59 million for kinders; and $568 million for new and upgraded schools, including money to refurbish 67 schools, rebuild 9 schools and remove asbestos in classrooms right across the state. And we will provide $12 million to support and establish tech schools across the state. For the first time, Gonski funding levels will be met to the end of the 2017 school year. The previous government tore apart those TAFE systems in the middle of a youth unemployment crisis, and in stark contrast this government has included a $350 million injection to save our struggling TAFE system.

We believe everyone should have the care they need, not the care that they can afford, and our budget invests $2.1 billion in Victoria's health system, including $200 million to increase hospital capacity and $60 million for an elective surgery boost to cut waiting lists. With this funding hospitals can admit an extra 60 000 patients and treat an extra 40 000 emergency patients. Our growing population means that we require more hospitals. The budget provides over $560 million to hospitals in fast-growing areas across Victoria: Western Women's and Children's Hospital, Casey Hospital, Werribee Mercy Hospital and Angliss Hospital.

This government is getting on with projects our state needs so people can get home to their families safer and faster. It delivers record investment in public transport, with a 41 per cent increase over the 14–15 year budget. Two to $2.5 billion over four years will commence the removal of 50 of our most dangerous and congested level crossings. This is vital to addressing both safety and of course reducing congestion, vital to allowing more trains to run on every line, and also vital to reducing the road toll. Our budget makes the biggest investment in public transport in the history of our state. The government has committed $1.5 billion over the current forward estimates period to deliver the 9 to 11 billion dollar Melbourne Metro rail project. This is the right project at the right time. This investment relieves train congestion in the city loop. It will create space for more trains right across the network.

We are also investing over $600 million to fix the congestion Victorians face getting to work, getting home and also getting around the community safely. That will include $150 million in the next stage of the M80 upgrade from Sunshine Avenue to the EJ Whitten Bridge, $110 million to duplicate the Chandler Highway bridge and $90 million for smart investment in intelligent transport systems. In addition we are providing $273 million towards widening CityLink and the Tullamarine Freeway and $40 million to deliver works this year to widen Whitehall Street and strengthen and widen Shepherd Bridge in Footscray.

In summary this budget delivers the commitments the government took to the people of Victoria at the last election. We are doing what we said we would do. This budget gets the balance right. We are restoring services, prioritising those things that are important to families — health, education and the protection of the vulnerable — and we are delivering the right infrastructure projects at the right time. This budget of course continues the Labor tradition of building on strong financial management. We are delivering a strong operating surplus, low net debt and sustainable and resilient expenditure growth. The budget delivers on longstanding Labor values in a modern and responsible way.

The CHAIR — I will kick off. In the context of your role as Treasurer, can you tell the committee how this budget acquits *Labor's Financial Statement*?

Mr PALLAS — It gives me great pleasure to say that *Labor's Financial Statement* of 2014, which was effectively our commitment to the Victorian people of not only the things we were going to do but how we were going to fund them, detailed the Andrews Labor government's plan to fix Victoria and also to support our families while making sure that Victoria's finances are healthy and stable. It was published in November 2014, prior to the state election, and it laid out detailed financial information on the now government's election commitments. Through the delivery of these commitments, the government plans to lift the state's economic performance and also to improve the quality of Victorians' lives.

The 2015–16 budget also delivers on the commitments we took to the last election whilst maintaining healthy prudent surpluses, preserving our AAA credit rating and also creating more jobs for Victorians. These are our commitments writ large, in effect. These are the things that we value and the things that we intend to make a diligent and consistent part of the way that the government intends to operate going forward. The commitments set out in that statement and the commitments we took to Victoria at the last election were fully costed. They were affordable and they were achievable. I might say they were oversighted not only by a substantial firm in Moore Stephens but also by John Howard's and Jeff Kennett's commissioner of audit, Professor Bob Officer.

Our financial statement identified recurrent initiatives of $3.3 billion over four years. The 15–16 budget provides $3.2 billion for these output initiatives, which is 96 per cent of the funds that were outlined in our financial statement. As you can see, there is a high degree of proximity between what we said and what we are delivering. Labor's plan covered a range of recurrent funding commitments across all fields affecting the lives of all Victorians: skills and knowledge, jobs and growth, health and wellbeing, world-class transport, a safe and just society, sustainable and livable communities, and initiatives to back rural and regional Victoria.

Key recurrent initiatives that are funded in the 2015–16 budget include the Camps, Sports and Excursions Fund, which will assist disadvantaged families to cover the cost of school trips and excursions. Eligible primary school students will receive an annual school credit of $125; secondary school students will receive an annual school credit of $225. There is the $100 million Back to Work scheme through which the government will provide financial assistance to businesses hiring those at risk of an extended period of unemployment. There is $508 million for the Premier's Jobs and Investment Fund, including $60 million for a start-up initiative. There is $200 million for the Future Industries Fund, which will be established to support the transition of the Victorian economy through targeted strategies to grow the state.

We did identify before the election, and we remain committed to, those six high-growth sectors that were incorporated in that statement. I will not labour the point by taking you through them, but we are identifying those areas of growth that historically can give us some degree of certainty going forward that there will be continuing employment generation in the Victorian economy. The Hospital Beds Rescue Fund, which is funded in the budget, will enable additional hospital beds to be opened across Victoria, providing capacity to deliver more hospitals and services, as was recommended by the previous Travis review.

Chair, I am conscious that I do not want to take up all the time in this answer. I can go on, so you just give me the wind-up when you think I have gone on too long. I can see from one side of the table that I have gone on too long already.

The CHAIR — Perhaps you might like to briefly summarise.

Mr PALLAS — The government has committed in the budget to get on with the construction of the Melbourne Metro rail project. That will include of course a new rail tunnel with five new stations linking with the Sunbury line and the Cranbourne-Pakenham line via the Melbourne CBD. We are also committed to a very substantial package of works around the removal of our 50 most dangerous and congested level crossings, and our commitment really is that we will deliver for our community. The things we said we would do are of course the minimum requirement of any government: you honour your promises. That is what we will do, but more importantly what we are saying is that we will rebalance the way that the budget is addressed. We will make sure that we are putting more money into services and that we put money into the capital spend in order to build the right projects at the right time.

Mr MORRIS — Good morning, Treasurer. Welcome back to PAEC after what I think is an absence of five years.

Mr PALLAS — It is.

Mr MORRIS — You really do not know what you were missing here!

Mr PALLAS — It is good to be back.

Mr MORRIS — I am sure it is. I also note that despite assurances to the contrary, the tradition of Dorothy Dixers at PAEC is alive and well, and we start the hearings with a broken promise. That is not a good way to start. To move to the more substantive issues, Treasurer, I refer you to budget paper 5, page 200, and in particular the reference to the east–west link, eastern section, which is down the bottom of the page. In particular there is the debt facility, and you have already spent some $81 million purchasing this $3 billion debt facility. Can you advise the committee what the weekly or monthly fees are for maintaining that facility, and can you let us know what the additional cost of using this approach is compared with perhaps more traditional means, like raising the funds through Treasury Corporation of Victoria?

Mr PALLAS — Sure. I suppose by way of background the first thing is to make the point that we formed the view, and we formed the view very clearly and quite directly to the Victorian people, that we would not proceed with this project if we were elected. We have gone through quite a diligent process in negotiations with the east–west consortium in order to extract ourselves from what we saw as being an entirely inappropriate set of contractual arrangements. Nonetheless, we dealt respectfully with the consortium, and we have come to a mutually agreed arrangement.

Those mutually agreed arrangements, of course, the contents of the heads of agreement — the non-binding heads of agreement — have been made public. They effectively indicate that the state, which we announced on 15 April, had negotiated an agreement with the east–west consortium. Under the agreement the state will purchase the companies in the consortium, the East–West Link Project Co for $1. All assets owned by Project Co will transfer to the state. We are currently going through a process identified in that heads of agreement that will enable us now to move to a formal contractual arrangement, and our expectation is that those processes will be concluded within three months of the initial announcement and the initial signing of the heads of agreement. The full content of those arrangements will therefore need necessarily to be held until we have got to that point where full commercial and contractual close has occurred.

I am prepared to take you through the arrangements. Effectively they are in two parts. There will be an arrangement struck between, as it were, the constructors and the financiers of these arrangements. So $339 million of net costs have been drawn down and paid to the consortium for the bid process and the design and preconstruction. These costs have already been incurred — I want to stress that point — and they cannot be retrieved. They will be retained by the consortium subject to a certification process, which is in place — that is, we want to satisfy ourselves. We have made it very clear to the consortium that we expect a demonstration that these are real dollars that have gone out the door for real purposes, and a further $81 million of fees were incurred to establish the Project Co credit facility of about $3 billion.

The state intends to negotiate with the banks to take over that facility, to contribute to the funding of the Melbourne Metro rail link project, and we expect to receive value for those fees. All rates or fees, swaps and obligations related to the credit facility will now be worked through between the financiers and the states. I might say that the financiers are a very large group, and whether all the financiers seek to stay in those recast, repurposed arrangements will ultimately be a matter for them, but we have no doubt that we will be able to get to the level of the facility that we see as being desirable.

The 2014–15 budget disclosed 6 to 8 billion dollars in terms of total estimated investment for the east–west link section, 8 to 10 billion dollars for the western section, and of this, the project-incurred costs under the former government were over 2013–14 and 2014–15. The majority of those incurred costs, might I say, do relate to land and property acquisitions, which the government has already announced will now be sold, with the proceeds used to offset those costs. The remaining costs around the incurred costs really relate to planning and procurement — the sort of work that government does day-to-day as it thinks about projects, as it proceeds to develop projects, whether they proceed or not. It is an inherent cost in the business of planning for the future.

The government, and I think it is an important point for the committee to appreciate, having successfully negotiated a heads of agreement, and of course with every expectation that it will get to a closed contractual arrangement, the remaining allocated funding — that is, the funding that the previous government allocated to this project of around about $7 billion across the budget and the forward estimates — is now available. It is available to the state of Victoria to repurpose and to apply to other more critical priorities.

Mr MORRIS — So, Treasurer, you cannot tell us what it is going to cost the people of Victoria? That is not particularly satisfactory, I must say, from a committee point of view, but that point aside, I understand that the consortium had obligations to draw down particular finances. Are those obligations transferred to the state? This is outside the $339 million you have already referred to. Are those obligations to draw down finances transferred to the state, and if they are, what are they?

Mr PALLAS — I am not trying to be disingenuous with you here, David, but the reality is that we are going through a negotiation with both the financial institutions and the construction companies. We would expect, of course, that there would be a much greater level of clarity once we have finally concluded those contractual arrangements, and we understand our obligation to the people of Victoria to be clear about what has occurred here. Whether or not I want to be particularly open and transparent in this committee, you can take it from me that the Auditor-General is going to be looking into these matters with, I understand, a fair degree of interest and animation. We understand our obligations to acquit our responsibilities in regard to these negotiations. We have not yet concluded contractual arrangements, as I said. We expect that they will be concluded — —

Mr MORRIS — You must have had an idea of the costs to prepare the budget, though. We are simply trying to get a handle on that.

Ms WARD — Are we doing supplementary questions?

Mr PALLAS — I am happy to have a bit of back and forward. I think the truth is, in this process we are going through a negotiation. I hope that you are not asking me to in any way compromise the state's negotiating position by starting to put a figure around where this comes. But, David, let me assure you all of this will be clear and transparent in the context of what has been finally agreed once those arrangements have been struck.

Our expectation is as I have put it to you, that we have incurred liabilities — in fact amounts of $339 million of net costs have been drawn down and $81 million of fees have been incurred, and we hope to re-purpose those fees. I will be able to give you a greater acquittal of those matters once these arrangements have been finally concluded.

Ms WARD — Good morning, Treasurer; nice to see you. I am pretty interested in discussing a bit further on east–west link. Could you please expand on how the government is protecting the interests of Victorian taxpayers in dealing with east–west link?

Mr PALLAS — The first point I would make is east–west link from our perspective was a flawed project — flawed from its inception — and in many ways it was a project that was out of sequence, out of time, and had not been properly worked through, and importantly the transparency that subsequently became apparent has demonstrated why Victoria in effect dodged a bullet with this infrastructure being delivered.

We know that the project was shrouded in secrecy. We kept seeking that the business case be made public, and upon coming to government we did produce that business case and it has been effectively out there for the purposes of public scrutiny. The reason why I think the light of public scrutiny was so important is because it did demonstrate that this was a very, very bad investment for Victoria. The Andrews government committed to release the business case, and we did. We committed to release the contractual terms, and we did.

The original business case, of course, we all know now had a benefit-cost ratio on traditional BCR allocation arrangements — before we start getting into the complexities of agglomeration economics — and it had an original and legitimate BCR of about 0.45, which is 45 cents in the dollar, which is a loss-making venture of 55 cents in the dollar. Not many people would get involved in that, and I hope that in future what we see from governments is greater transparency around the production of some satisfaction that what governments are doing are actually and properly accounted for before we commit substantial sums of money to them.

The previous government overtly decided to not submit these arrangements to Infrastructure Australia because they recognised that it would effectively destroy their case for getting federal funding. In fact there is an elegant excerpt in one of the documents from the consideration by the previous government's relevant cabinet subcommittee where they actually say, 'We'd better not show this to the federal government, otherwise it might compromise our capacity to get federal funds'. We have got to wonder why Tony Abbott in those circumstances, a Prime Minister, would consistently have sought to pursue and support these arrangements, given that he was effectively being used in the process.

So the project was flawed. We knew 9 in 10 drivers would be worse off. Victorian taxpayers were also going to have to pay billions and billions of dollars in availability payments over the next 25 years, and I do not think that is a thing that many people have really appreciated. It would have sucked the life out of Victoria's future.

It was a completely false claim that the road would only cost Victorians $2 billion. The business case is clear on this; the contractual arrangements make it even more clear. Effectively what we had was a hiding from independent scrutiny that would only have increased Victorian taxpayers costs — not only by $1.5 billion of federal tax funds but a much bigger sum than that. If you look at the true costs of this project, the previous government declared them as $6.8 billion before the last election, but we now know that the true cost is $10.7 billion.

The current federal leader, of course, called the election a referendum on east–west; Victorians delivered on this referendum and they expressed a pretty clear view. We see it as part of our mandate. The side letter, I think, really did demonstrate how insecure the government were around the legal footing under which they were entering into it, and it really did. In many ways the fact that it was not made public before the last election was a great impediment upon the state's capacity to negotiate our way through these arrangements. But I am pleased to say that we did do so.

Mr D. O'BRIEN — You said the contract was not worth the paper it was written on.

Mr T. SMITH — Not one dollar.

Ms SHING — I think we were hearing about a side letter, weren't we?

Mr PALLAS — I suppose the obvious thing is that we have an obscene side letter that was not in the public domain, and it goes directly to the way that the government of the day conducted itself, because the government of the day did not know that there was a guarantee in writing from the previous Treasurer. Now the current Treasurer — —

Mr MORRIS — The Treasurer is here to speak about what is happening in 2015, not what may have happened in previous governments.

Mr PALLAS — David, this goes directly to the obligations that attach to the state of Victoria. So essentially what we are able to tell you is that we had a guarantee from the state of Victoria to the east–west corporation that even illegal actions by the state were guaranteed by the state. If you say that you are somewhat aghast that consequently the state has incurred costs — —

Mr MORRIS — Standard commercial practice.

Mr PALLAS — No, it is not standard commercial practice.

Mr MORRIS — It is standard; ask the gentleman sitting on your right.

Mr PALLAS — I defy you to show any such similar arrangements, because we could not find any relating to state government arrangements. Quite frankly, we have disclosed that we believe these arrangements have been properly and fairly relieved from the state and the state gets substantial funds going forward — $7 billion going forward as a consequence. That has effectively reduced the state's exposure to a bad project, and it will also ensure that Victoria has the capacity to invest in the right projects.

Dr CARLING-JENKINS — Thank you, Treasurer, and I thank you for your budget presentation and for being the first person to answer questions in this forum. I note that in your opening statement you said that 96 per cent of Labor's election commitments were covered in this budget. Can you please describe for the committee which commitments you are unable to accommodate in this budget, and why?

Mr PALLAS — Thanks very much, Rachel, for your question. I suppose the first point I would make is that the government was very clear in its pre-election position in that things we said we would do we would go about and actually deliver to Victorians. So the important thing from our perspective in making those commitments is also acquitting them. We spent a lot of time looking at problems that governments in the past have incurred. If you essentially only implement 20 per cent of your capital agenda in your first budget, I think there is a fair level of community scepticism about your real and continuing commitment to the government's broad agenda.

We did say 96 per cent of our projects would be implemented and have been implemented in this budget. On page 109 of budget paper 3, you will see that there is a page that deals with outstanding capital commitments. Let me put this in context. What we said is that 96 per cent of our commitments have been paid for. I am sure we will at some point get into a process of where is the money, because it is not expressly allocated. I had a bit of fun during question time during the week over that issue. But let me assure you that the projects that are identified in the express allocated funding sources also have appropriate allocations put aside for them in order to acquit our election commitments. That is contained in our unallocated capital, which is the subject of decisions, and ultimately to acquit our election commitments. I will take you through those in due course.

The outstanding capital commitments, which deal with those areas that have yet to be fully acquitted — and, might I say, some of those were because we did not give a start of electoral cycle commencement date for those matters. All of the things that we said that we would acquit in the first budget have been acquitted — and, might I say, more than we said we would do. Importantly that there are some — if you look at table 1.26 on page 109 of budget paper 3, you see 'Aikenhead biomedical engineering' at 60 million TEI, 'Chinese aged care land bank' at 2.5 million, 'Contemporary music hub' at 10, 'Doctors in schools' at 18, 'Golf centre of excellence' at 10, 'Maroondah breast cancer centre' at 10, 'O'Herns road interchange' at 10.7 — might I say that is part of an initiative that we need to acquit with the federal government. We are seeking what we understand could well be a contribution from the federal government to that. Did I say that is 40.7? Did I get that wrong? 'Railway station car parking fund' at 20 million and 'Save Sunvale primary site' at 4.2 million. So all up there is about $175.4 million in the context of the capital allocations identified that I have already taken you through in my presentation. This is a very small amount, but might I assure you that where there are cash flows that do not fully acquit the TEI of projects that we have identified, but have commenced, they have been fully provided for in our appropriate allocations.

Dr CARLING-JENKINS — Thank you for your answer and for providing context to your earlier comments. Can you let the committee know when you will be able to deliver on these commitments?

Mr PALLAS — I think if you went to each and every one of them, I suppose they all have differing considerations attaching to them. Some might, for example, have a consideration around, 'Well, what contribution are we going to get from the federal government?'. Aikenhead may well have that same arrangement. There are also questions of other financial inputs, including from the hospitals and other areas, so those are subject to negotiation. I can assure you they are all things that we committed to at the last election and therefore seek to have well underway before the next election.

Mr T. SMITH — Treasurer, I refer to page 42 of budget paper 3 regarding Melbourne Metro. The question is: how are you going to pay for this? Will you allow any increases to the cost of train and tram fares, CBD parking, rating on properties, road toll premiums or other taxes, charges and fees to pay for the 9.5 billion black hole in this project?

Mr PALLAS — It is a little rich to describe it as a black hole.

Mr T. SMITH — How are you going to pay for it?

Mr PALLAS — The first point I would make — —

Mr T. SMITH — It is going to cost 11 billion, so how — —

Ms SHING — It would be nice if you let the Treasurer answer the question.

Mr T. SMITH — It would be nice if he could answer it succinctly.

Mr PALLAS — So, Tim, I will try to answer it succinctly.

Mr T. SMITH — Thank you.

Mr PALLAS — So we have committed 1.5 billion over four years, and we expect that this project will come to something in the vicinity of about $11 billion — up to $11 billion. The first point I would make is that we expect this to be a very substantial contribution towards unblocking the city loop. It will free up the capacity of something like 20 000 extra passengers every hour who will be able to make their way on our metro system; that is something like about 19 trains extra. So how do we fund it? The first issue is that there was a business case provided to the previous government that was subsequently made public only recently, I note. It is fortuitous that these things find their way into the public domain at certain times. What I would say is that it put a number of ideas forward that included the suggestion that there would be increased car parking charges, increased train fares — can I just say the ideas that were contemplated in that business case, in large measure, do not get us anywhere near where you would want to get in respect of being able to fund and finance this project.

Let us be frank, it will require a very substantial public sector contribution, and the state will obviously, through its capital allocations into the future, make continuing contributions. But, Tim, let me assure you, I could not get more than $1.5 billion out the door on this project over the next four years; I just could not do it physically. With the planning, the design, the tendering processes that would be required and the land acquisition issues that need to be taken into account, we just could not do it, and I accept that the community would expect to have a clear appreciation of how the state will fund and finance this project when contracts are signed and then work begins.

But I think equally and fairly we should be given the right to design it and to engage the community about how it will be funded and financed. But for issues such as car parking I think, to be honest, we have built that just about as much as we can. The previous government increased the revenue take from the congestion levy by a factor of 3 when they came to government to when they completed their term in government. I do not think we can keep going back to that source. I do not think milking the fare box actually helps us in the long term in terms of the size of the contribution that we are contemplating here. It will in many cases require a priority in terms of our capital spend going forward.

Mr T. SMITH — So how does your answer reconcile with some of the comments of the Premier, who says that we will not be doing any of that? I just do not get a picture about where the money is coming from for this project.

Mr PALLAS — I do not know, Tim. The Premier said he had no plans to do this, and I think on a different radio station — maybe a competitor — I said we had no plans to implement any of those things.

Mr T. SMITH — You have not said how you are going to pay for this. We do not know.

Mr PALLAS — No, what I have said to you is when we enter into contracts, when we are at a point where the community will see that this project is actually physically occurring — —

Mr T. SMITH — So it is 'Just wait and trust us'?

Mr PALLAS — But if you want to know where the principal amount of funds will come from, 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. I might say we are used to it, in terms of the federal allocations that we get, but nonetheless, if we have to, we will. Remembering that there will be a very substantial amount of unallocated capital going forward that can be tasked to this project over a responsible and long-term period, that will be the core of the funding base going forward.

Ms PENNICUIK — Treasurer, welcome to the PAEC. Good to see you here again.

Mr PALLAS — Thank you.

Ms PENNICUIK — You mentioned in your opening remarks that the budget has allocated around $567 million for 67 school refurbishments. The Greens were very concerned when the Auditor-General released the annual financial report of the state of Victoria last year in that it was a qualified audit opinion and that the auditor did not agree with the state's decision to write down almost $1.6 billion of taxpayer investments in school buildings:

> The state did this writedown on the basis that it believed that seven out of every 10 Victorian schools are partly economically obsolete. However those schools are continuing to deliver educational outcomes for the citizens of Victoria.

The auditor also notes that in view of the practices applied across other Australian jurisdictions he found that Victoria is alone in its approach to this matter. He also stated that it is of concern that the state has written down schools that had recently received significant funds from the commonwealth and the state with regard to their upgrades and that some schools had current capital work programs and new schools in growth areas under PPPs.

My question to you, Treasurer, is: what attention are you paying to this issue with regard to more public funds — hundreds of millions of dollars — going into school refurbishments and a situation where we had the qualified report issued by the auditor and concerns raised about that particular practice, which was unprecedented and does not happen anywhere else in Australia?

Mr PALLAS — Thanks, Sue. We share your concerns, and we shared them in opposition. I am pleased to say that the qualified opinion issued by the Auditor-General on the Department of Education and Training 13–14 financial statement and the 13–14 financial report for the state of Victoria and the valuation of its school building assets has been resolved. The qualification related to the interpretation and the application of economic obsolescence in deriving fair value issues to school buildings under the Australian accounting standard's fair value measurement. I will not bore you with the accounting standard measure. That measure, however — —

Ms PENNICUIK — Do bore us with it.

Mr PALLAS — AASB 13; and that standard provides definitive guidance about what are diverse views regarding the application of economic obsolescence in regard to the public sector. The state has made a change in our accounting practices and policy for the valuation of school building assets going forward. There is no adjustment — can I make you that much more comfortable — for economic obsolescence; it is made for assets still in use, and this change means that the matter is now resolved.

The state has made those changes during the 14–15 financial year. I am sure that the Auditor-General himself will clarify his views in respect of this matter. It is not for me to speak on behalf of him, but we believe that these arrangements now fully acquit the concerns that have been put in place and certainly the qualifications that have been stated.

Ms PENNICUIK — During the auditor's report he put some recommendations such as that DTF develop an appropriate and consistent accounting policy that is consistent with the requirements of the Australian accounting standards, and the department did not accept that recommendation. So are you saying that the department is now accepting that recommendation?

Mr PALLAS — Yes, I am. I am saying that we have now acquitted the concerns that the Auditor has raised. If you go to page 17 of budget paper 5, there is some content that basically explains exactly what has happened here, that we have changed our accounting principles to discard the previous arrangement of incorporating the concept of economic obsolescence in regard to school valuations. The Auditor-General can speak for himself, but we believe that essentially we have acquitted his concerns in that respect.

Mr DIMOPOULOS — Good morning, Treasurer. Thank you for your time and your affable disposition. I refer you to budget paper 3, page 1, where it talks about the government delivering its election commitments. Of course some of these commitments were already underway before the delivery of this budget on Tuesday. Do you mind updating the committee on the progress to date? We have got some of those commitments.

Mr PALLAS — Sure. The 14–15 budget update provided immediate funding for a number of key election commitments to commence ahead of the 15–16 budget. The key ones I suppose in summary are the family violence royal commission. Basically we have made it clear that to us there is no greater commitment that a government should make than to family violence and safety in the home, the protection of women and children.

We know that of course the leading form of death amongst women between the ages of 15 to 44 years is a result of domestic violence, so it is a very substantial problem and it is one that we believe needs to be confronted in very substantive terms. That is why the family violence royal commission and funding it early was so important to us. We moved quickly to commit funding of $40 million over two years and to allocate this in the budget update. That was only a matter of weeks after coming to government, I might note, so that the royal commission could be established without delay.

In February 2015 the Royal Commission into Family Violence was established, I am pleased to say, and it is due to deliver its recommendations in early 2016. We are in a position where we are moving into the budget cycle of course. We will have a clearer appreciation of what is further required, and there will be more that will be required from government, make no mistake, in this space.

The budget update also announced funding of $1.5 million for reopening the inquiry into the Hazelwood mine fire, to look into the reported increase in deaths in the Latrobe Valley and also to consider options for the rehabilitation of the mine. The inquiry is set to reopen this month and will help the community get to the bottom of concerns that quite genuinely affect that community and to make sure that we learn the lessons of these issues and also get on with the job of the long-term rehabilitation of the mine.

One hundred million dollars on the Back to Work scheme. That was important in the sense that the way the scheme will operate is that there is effectively a three-month qualification period, so putting that money in early allowed employers from 1 April of this year to start the process, and come 1 July effectively money would be available to be paid forthwith for those employers who qualified — that is, met the qualification criteria and also met the employment period criteria.

The community service obligations for TAFE of course were important to us. We put a very substantial amount of money into TAFEs — an initial allocation of $20 million to fund the full TAFE rescue component as part of the 15–16 budget; $200 million in the 15–16 budget for output funding and $100 million for capital.

The commencement of transport infrastructure policies, in addition to the budget update, included $166 million in capital funding to advance key transport infrastructure priorities in two key projects: the level crossing program and the West Gate distributor early works. That of course was facilitated and, as you know, we have continued the process around those early work capital programs in order to ensure that we had sufficient capacity for those departments who were ready and able to get going in order to generate sufficient infrastructure works while the government was getting on with the business of delivering its substantial infrastructure package that was contained in this budget.

Mr D. O'BRIEN — Treasurer, my question goes to wages policy. I refer to budget paper 2, page 64, 'Employee expenses'. Can you please advise the committee of the specifics of your public sector wages policy in relation to wage increases and any productivity offsets?

Mr PALLAS — Certainly our position in respect of wages policy is that we do not take the view that we should be constantly at war with our workforce and our employees. That does not mean that as a government we should nonetheless be anything other than prudent in terms of the allocations that we make for staff, because obviously the more that you spend in terms of your current expenditure on your staffing costs and the more that you put in on your existing staffing costs, it does have a capacity and prohibits the amount of actual and more staff we can take on, so it is about getting that mix right.

One of the things that I have been really anxious to impress upon people in the context of this budget is we are trying to rebalance our allocation. It is a Labor budget — unashamedly a Labor budget. We are winding back the level of capital allocation in the first year, we are putting more funding into services, and we are also putting more funding into the commitments that we think were critically important going forward.

I know there has been a fair bit of talk around employee growth projections. I think it was identified that there would be increases of 7.1 per cent in 15–16 in terms of employee growth. That, might I say, is up from the 5 per cent of employee growth projections in the 2014–15 pre-election budget update, so it was 5 per cent moving to 7.1 percent. Not all of that — in fact none of that, quite frankly — is around further or higher wage increases. They would be absolutely minimal in the context that they are principally related to more staff being employed.

Overall, that 7.1 per cent is broadly driven by both price and volume — that is, factors contributing to price growth: the 2.5 per cent indexation policy on wages policy; the profiling of major enterprise agreements, the costs of some of those major agreements, for example, teachers being back-ended. There is growth in employee expenses. In a pre-election budget update the previous government's employee spend, which the previous government identified at about 5 per cent, was the result of both indexation of 2.5 per cent of frontline services, increased education enrolment funding and increased investment in corrections, police and protective services officers. So growth from the 5 to the 7.1, which I suppose is really the key of your question, goes to 15–16 and it reflects our commitment to meet more demand from a growing community, a community that actually expects that they get quality services and for a government to actually make that investment in those quality services.

It is critical to our core service deliveries, including health and education. Key programs that I can direct you to that will demonstrate where that growth is happening — there is new funding to meet hospital and health service demands, there is expanded child protection and family services, there is funding to meet growth in school enrolments and there is new funding for police and emergency services. To give you an illustration of the sorts of things we have said we will do in terms of additional staff, we are on the way towards employing 450 extra firefighters, 111 extra child protective services workers. We are putting in place police custody workers, who are freeing up police — 400 effectively, to free up police — so that they can go about their jobs on the frontline.

So yes, we are making an investment, and our wage profile — not our wages cost profile, but our wage profile — in terms of the overall cost into services is expanding. Overall, over the forward estimates period what the growth is projected is both moderate and average at around about 3.4 per cent.

Mr D. O'BRIEN — Of wages?

Mr PALLAS — Of expenses.

Mr D. O'BRIEN — Okay, sorry. Yes.

Mr PALLAS — Wage expenses — can I put it that way. It is not a wage outcome in an enterprise bargaining sense, if I can put it that way. But to the extent, Danny, that your question went to, 'What's your wages policy?', our wages policy is similar to but not the same as the previous government's. Our view is that of course there should be a guaranteed base rate of wage increase at around about 2.5 per cent.

We take a much more flexible view around productivity; we think the previous government was too hard. They had a component of about 0.5 per cent around productivity, some of which was really quite frankly ludicrous. Some of the logic was tortuous that went into the enterprise bargaining agreements that sought to justify when the government felt that they had a political agenda or imperative to meet those costs. Quite frankly we think that our workforce should be able to get access to that extra half of a per cent in circumstances where they show that they are improving service delivery, where they are improving the efficient provision of services and that they partner with the state going forward.

So we will be more flexible. I mean, we will recognise the collective bargaining rights of our representative organisations. That is the Labor way; we are a Labor government. But we are not going to be irresponsible in terms of wages costs. You will find wages costs broadly, in our expectation, will be — in terms of enterprise bargaining outcomes — broadly in the same ballpark as those identified by the previous government.

Mr D. O'BRIEN — Thank you, Treasurer. You sort of half got around to answering my question, which was about what the actual wages policy is. You said then that it is similar but not the same as the coalition's. You then talked about it should be a base of 2.5 per cent. Then I think you said that the public service should have access to the extra half a per cent where relevant but you will be flexible. What I am really trying to get at is the budget paper actually says, 'Wages policy sets the framework': what is the wages policy, given that we have got the growth in public sector wages, given that we have got a number of EBA negotiations. And can you guarantee that you will stick to a policy, rather than just saying, 'We'll be flexible'? I really would like to get to the percentage if I could.

Mr PALLAS — I could make the glib observation that the definition of what constituted productivity under the previous government was a very flexible concept based on the imperative to settle the disputes that they were involved in. So look, the truth is we are serious about making sure that we can keep — —

Mr T. SMITH — What's the percentage?

Mr PALLAS — Well, I have already told you.

Mr T. SMITH — No, you did not.

Mr PALLAS — The percentage that the government has put in place in terms of wages policy is 2.5 per cent as a base outcome, and we acknowledge that there will be capacity in the order of 0.5 per cent for improved efficiency, not being productivity. I want to be very clear about this. We recognise and regard that there will be occasions when governments see a need to do more than that in individual circumstances. There will, for example, be circumstances where workers have had deflated wage outcomes for a considerable period of time through no fault of their own, through a deflated capacity in the bargaining processes. We would see them as being few, but nonetheless we are not going to get constrained into an ideological straitjacket on this. We see wages policy as an important tool to drive the outcome of all enterprise agreements and also to moderate employee expenses growth. It is critically important that we take a responsible line in respect to that. It is also, as I understand, important, given that we have a low period of inflation, that therefore the expectations of our workforce are moderate, modest and should be respected in that context.

Mr D. O'BRIEN — So 2.5 per cent plus 0.5 per cent, but there will be some that might get a bit more.

Ms SHING — 'In the order of', I think, was what the Treasurer said.

Mr PALLAS — Yes, in the order of, and, look, our view is this is a total wages cost outcome and they will vary. They will vary across departments. For example, we might not be satisfied. Just as the previous government was not satisfied that they were getting productivity, we may not be satisfied that we are getting the requisite levels of efficiency.

We may be more than satisfied that we are getting a better outcome, and we will pay effectively for that better outcome. I have to say as a government we put a considerable amount of value in and around the idea that this is a cooperative approach that we will adopt with the union movement. That means that if we can drive improved service delivery and then if we can improve the quality of the services that we are providing to the Victorian community within the overall wage cost parameters that we have set in the budget, then we will value that and we will reward it, because we accept and acknowledge that our workforce do a wonderful job. But if you want to know broadly where we are talking, I am using the same sort of language as the previous government did with a couple of notable exceptions: 2.5 per cent will be assured as a base increase on wages and there will be a further provision for 0.5 per cent, provided there is efficiency and the provision of efficiency. Effectively we are looking at a capacity for the state to enter into negotiations in a meaningful way to improve our services.

Mr D. O'BRIEN — That is across government?

Mr PALLAS — Yes. And as I say, the overall estimates period identifies growth, which is broadly proximate with where it has been over a considerable period of time, regardless of the government of the day, at around about 3.4 per cent.

Ms SHING — Good morning, Treasurer; good morning, departmental heads. I would like to take you to page 45 of BP2, if I may, which sets out the government's budget strategy. I would welcome an explanation from you, Treasurer, to the committee as to context and rationale for the fiscal strategy that has been adopted in this year's budget.

Mr PALLAS — The strategy that the government has adopted to address the shortfall in funding for services that we inherited is effectively about getting that balance right. We have said it over and over again. We do recognise that there is value in building the right infrastructure at the right time, but there is not much point building that infrastructure if effectively what you are left with is — as we were and had to make provision for — prisons that have been built but not populated with staff. At the 2014 pre-election budget update, expenses were forecast to grow by an average of just 2.5 per cent a year, as I have previously indicated, over the four years to 2017–18. That is over a period when population growth was expected to grow by 1.8 per cent and inflation by 2.6 per cent, so there was a disconnect and a disparity between how the government was actually going to equip their budgetary settings. They were essentially talking about keeping to within a straitjacket of 2.5 per cent in expenditure growth in circumstances where there was no clear or apparent way that they were going to be able to do that.

I do have a handout for you, which will give you a brief illustration of that. The previous government strategy to constrain expenses growth would have resulted, I think, in an unsustainable shortfall in the levels of expenditure required to meet the growing demand in core services for families, including on health, education and front-line social services. To ensure that we could get all Victorians to continue to enjoy high-quality economic and social infrastructure, what the budget seeks to do is to restore funding to critical core services. So we are delivering $9.2 billion in terms of new output initiatives. That includes a progressive social agenda in investing in key services across health, disability, community services and responding to social challenges, including $250 million for child protection and family services, $81 million for family violence and $30 million for the ice action proposals, so that all Victorians can enjoy and can share in an improved standard of living.

An education state commitment, of course, as I have said, is $2.9 billion of funding going forward in output for schools to include the commitment to funding levels for the Gonski agreement to the 2016–17 school years. In tackling job creation there are the initiatives that complement the jobs that will be created through the government's major projects agenda. Essentially what we are looking at in the 15–16 budget is $22 billion TEI — total estimated investment — in new asset initiatives of $22 billion to honour our election commitments to remove those 50 level crossings at 5 to 6 billion. You have also got the 9 to 11 billion dollars of Melbourne Metro. And of course that is all provided in terms of our broad forward estimates appreciation and costs going forward.

The government is delivering on those high-quality services and infrastructure in a fiscally responsible manner. We take our fiscal responsibilities very seriously, and it is consistent with maintaining a AAA credit rating. I might say the double-rated AAA credit rating was achieved by a Labor government and maintained for 11 years by a Labor government.

Mr T. SMITH — Almost bankrupted us 20 years ago.

Mr PALLAS — How old were you then, Tim? He has got a collective memory. Underpinning those strong surpluses are operating expenses, which are projected to grow by around about 3 per cent a year over the budget period. So the second chart, that hopefully has been distributed, is appropriately higher than the unsustainably low levels that had been projected by the previous government, but low by contemporary standards. So to give you an illustration, 6 per cent a year over the decade to 2014–15 and below the equivalent rate of growth in revenue at 3.4 per cent a year, so we are not spending more than we are earning.

Mr MORRIS — Treasurer, if I can go back to the earlier subject — the reference is BP5, page 200 — the debt facility, and I will try again. On 15 April you paid an $81 million credit card fee, effectively, on behalf of the state of Victoria. You have now got a $3 billion credit limit on that card. You have not made your minimum monthly payment — let alone paid it in full — and as a consequence you are incurring costs on behalf of the state. You may be negotiating the final repayment plan, but at the moment there is money going out the door. There is money going out the door every week or every month. It is a pretty simple question: how much money is going out the door every week or every month? If you do not know, perhaps Mr Martine can answer it for you.

Mr PALLAS — I was tracking it. I am more than happy to have my public servants answer questions here today as well, but I am answering it for you, David, on the basis that I assume it is me that you want to, and I will.

Mr MORRIS — Treasurer, we just want an answer.

The CHAIR — Treasurer, I ask you to refer to the Deputy Chair as Deputy Chair, please.

Mr PALLAS — Sorry; Deputy Chair. The point that I would make is that in the arrangements that we struck for the debt facility which you are referring to — there was $81 million of costs incurred to establish that debt facility — we are in the process of renegotiating with the consortium around those arrangements. We have struck an agreement, so the good news for you is that there is a commitment for no further drawdowns on that debt facility by the financiers while the negotiations are occurring. Consequently whatever it is that we have inherited is what we are trying to manage, Deputy Chair. Certainly our aim and objective here is to make sure that the Victorian people get value for that debt facility.

I am not going to pre-empt where these negotiations might end. The answers will be clear and apparent once we have gone through the negotiation and we have made the terms of settlement clear, apparent and public.

The point I do make is that I assume that you are not asking us to go to a point of outlining what we would expect to pay, but I can assure you that in terms of debt drawdown, no further debt drawdown has occurred against those facilities since the heads of agreement were struck. Indeed, as the secretary of my department draws to my attention, in budget paper 5, chapter 6, page 201, there is a quote that says:

> Under the heads of agreement with EWC, the state's obligation for the novation of debt is capped (excluding the novation of any interest rate hedging related to the project).

So effectively we have restricted liability to those amounts that we have publicly acquitted and accounted for.

Mr MORRIS — Treasurer, I thank you for answering my supplementary from my last question, but I was not asking about drawdown of further debt; I was asking what this facility is costing us each week or each month. I understand there are costs. I am simply asking you what they are. What is this costing us every week?

Mr PALLAS — I think I might be able to answer this question.

Mr MORRIS — That would be helpful.

Mr PALLAS — Let me just consult with my colleagues. What we are in the process of doing, Deputy Chair, is effectively trying to repurpose an existing debt facility, and in going through that process what we are seeking to do is to repurpose it and leave it there as a facility that the state may seek to draw down on in future, bearing in mind that any liabilities and costs that have been incurred in regard to the debt facility to this point that have either been or are continuing to be drawn are borne by the consortium of financiers or are consistent with the terms of the heads of agreement. So the moment that we formally enter into new arrangements, the state will acquire the debt facility, and with the exception of any repurposing or establishment fees that might be incurred, only in those circumstances when we start to draw down on that new facility will there be additional costs incurred.

Mr MORRIS — So you are saying the meter is running but the charges are to be paid by someone else at the moment? Anything up to the final — —

Mr PALLAS — No, I am saying exactly the opposite. The liability to the state is capped. It was capped at the numbers that we made clear at the time of the heads of agreement — $339 million, and $81 million of fees incurred for the establishment of the debt facility. Over and above that there may be additional fees — there may be — and I have yet to complete a negotiation around these issues, but there may be additional costs should we seek to repurpose and reapply this facility. But it will only be at the point that we conclude those arrangements and it will only be at the point that we tell the people of Victoria what those arrangements are. But in terms of adding debt drawdown, and any consequence of that drawdown on the new facility, that will only occur when we start to draw down, which could be some years from now because it will be applied to the allocations for Melbourne Metro.

As we have said, we have got $1.5 billion in the budget for Melbourne Metro. I do not anticipate that we will draw down above and beyond those numbers in this term of government.

Mr MORRIS — So the meter is running but we do not know what the fare structure is effectively; thank you.

Mr PALLAS — You just cannot verbal me like that, David. It is not an accurate reflection of what I just said.

Ms SHING — You have been given an answer. If you are not happy with that, that is not the Treasurer’s concern.

Mr D. O’BRIEN — Did you not just say, though, that any costs at the moment are currently being borne by the consortium?

Mr PALLAS — The costs that the state has incurred are capped at $339 million. Together, and over above that, are issues around how the facility itself is managed at $81 million. That can be seen, Danny, as a sunk fee, as a sunk cost to the state, and we could walk away tomorrow. Alternatively we can say, ‘Let’s see if we can put that to good use, repurpose it for some value and apply it to a project that Victorians voted for’.

Mr D. O’BRIEN — But is that facility costing us now?

Mr PALLAS — The costs to the state are capped. Can I be clear about that? The costs to the state are capped. They will only become greater if we enter into new arrangements that will have to be public and publicly disclosed. Those arrangements would only effectively have an impact on the debt facility itself when we draw down against the debt facility. But there may be some additional costs associated with the renegotiation of the debt facility itself, the repurposing of that debt facility.

Ms WARD — I draw your attention to page 13 of budget paper 2. I note that there is a net debt profile declining to 4.4 per cent of gross state product over the forward estimates period. Can you tell me how that compares with the net debt projections published in previous budget documents?

Mr PALLAS — The net debt of 4.4 per cent of gross state product compares very favourably with the figures on net debt. It has not been this low since 2011, and it is lower than the projections the former government had set in terms of their forward estimates period. So the estimate for net debt at June 2018 shown in the 2014 pre-election budget update was 4.5 per cent of gross state product. We have bettered that. Not only is net debt projected to be 4.4 per cent of gross state product by June 2019, its trajectory is headed in the right direction, and I think that is important. It is not simply that you jump up and down, because of course the possibility of assets coming on and off the balance sheet has an impact on how our numbers look, but the practical outcome is that this debt profile, the projections, are heading in the right direction.

Net debt is expected to be 4.8 per cent in 2017, largely due to the cash flow profile of major asset investments, and it reduces consistently thereafter. Net debt as a proportion of GSP is expected to be 4.6 per cent by June 2018 and also, as discussed, coming down to 4.4 in June 2019. The levels of trajectory of debt so far are no accident. They are the result of a clear, a deliberate and a fundamentally sound financial strategy. I will take you just briefly through this.

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.

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.

Mr D. O'BRIEN — I take you to the issue of contingencies. You mentioned you have had a bit of fun with that this week so you should be all over it. Budget paper 5, page 202, refers to the current Tabcorp litigation, which was a consequence of the then Minister for Gaming and now Premier. That is set down for a special leave application on 15 May — next week, I think. We note that there is $686.8 million plus interest at stake on this one. Does your contingency specifically set aside paying out this judgement should it go against the state?

Mr PALLAS — There is an allocation of contingency, but if the question is, 'Is this figure expressly part of a contingent allocation?', the answer is no.

Mr D. O'BRIEN — It is not specifically part of a contingent allocation?

Mr PALLAS — No.

Mr D. O'BRIEN — Okay. If this judgement were to go against the state, given you have already halved the budget surplus, would this not halve the budget surplus again, and more?

Mr PALLAS — We could spend our life in pursuit of what may be. Essentially we have an outcome in a court that we are defending that effectively puts us in a very strong position. Our expectation is that we will successfully defend a decision that has already been made, but I want to draw to your attention the level of general government output contingency not allocated to departments that we have provided for. Funding has been put aside for a general contingency. That is set up at page 35.

Mr D. O'BRIEN — Of BP — —?

Mr PALLAS — Budget paper 5. Obviously if decisions are averse to the state's interest that has an impact on the state's bottom line. I do not think there is much doubt about that. But the advice that we have, the expectation that we have, the way that we have conducted ourselves, and certainly the fact that we are defending this action rigorously, is a clear illustration that we believe that the acquitting of responsibilities in those court cases to date has been appropriately managed.

I might say that I understand there are also counterclaims in respect of other litigation that essentially the state might get an upside on. So the point I make is if I made contingency for only the worst possible outcome in the contingency allocations, Danny, we would have a lot of contingency and not much action happening. So what we have tried to do is make sure that we have a responsible, reasonable assessment of how contingency should be managed, based on a reasonable expectation of liability that the state wears.

Dr CARLING-JENKINS — Treasurer, there have been many issues around transparency and contracts raised over the past four months, and today I note that you described the east–west link as an example that was shrouded in secrecy. This budget now contains a number of large infrastructure projects, detailed in budget paper 3, including, most significantly in terms of cost, the level crossing removal program and the Melbourne Metro rail project, which was an election commitment of your government. Will you rule out accepting an unsolicited bid for these infrastructure projects and guarantee a considered, open tender process?

Mr PALLAS — I can guarantee you, Rachel, that there will be no unsolicited bids received because it no longer exists as a policy of this government. What we have is a market-led proposal strategy and process, and we do see that there is value to be received from the private sector coming up with ideas. We are very proud of the idea that we can actually go to the private sector and say to them, 'Look, we are interested in your ideas. Tell us how better we can get value for the state, how essentially we can get a much better outcome for the state by you telling us how the state can better acquit its commitments to the people of Victoria'. This idea that the state, the government, the politicians are the sole repository of wisdom I think is a really dangerous one, and I think it actually gets us to a point where we need to have a much more substantial engagement with the community.

But I do think you are right to say that unsolicited bids, as they were previously applied and structured by the government, got us to a point where you saw arrangements sought to be entered into that had not even been in the public domain. One of the reasons, for example, why the western distributor — the Transurban proposal — is in the public domain is that we changed the arrangements to place an obligation on the government to tell the world that we had received it and had reached a certain stage of maturity in terms of our assessment and deliberations around it that the public had a right to know about it. Would it have been more comfortable for governments to have simply sat back and waited until they had acquitted themselves and got to a point where we had absolute certainty around the value of these arrangements? Absolutely it would have. But would it have been the right thing to do by the Victorian public? I do not think so.

So we have taken the view that we do need to continue an engagement with the private sector to recognise that they can be very substantial contributors both to ideas and to add value to our infrastructure proposal. Quite the contrary, Rachel. I am open for business, the government is open for business. We will be looking for market-led proposals in respect of our capital spend — we will encourage it — but we will also give the community some confidence that what we are going to do is also make sure that when the private sector comes forward with proposals, they offer the best value for Victorians. The revised guidelines and the new market-led proposals put in a much more transparent and rigorous process that we believe is probably the most transparent and rigorous in the country.

The market-led proposals should be innovative, and they should be focused on community priorities. So one of the things we are going to do is instead of saying 'under unsolicited bids' — and there is a big difference, really, if you just look at the terminology applied. Unsolicited bids are things that just seem to rain down on you from the private sector. We are saying market-led proposals because here are our areas of interest. We will tell the community, we will tell the public, 'Here is where the state wants its effort and its capital capacity applied — —

Mr D. O'BRIEN — How does the western distributor fit into that?

Mr PALLAS — Well, it is a — —

Mr D. O'BRIEN — Because you said you did not want it.

Mr PALLAS — I am really looking forward to taking some questions about the western suburbs and road connectivity, but the very real thing, the real point we make is that we recognise that there are ways that the private sector can improve our offering to the public. I mean, if we get to the ridiculous position where essentially all governments do is say, 'We had a policy before the last election that is immutable. All the things that we said' — because in opposition we were the sole repository of information and that therefore the things that we said we would do — 'absolutely are immutable', then you are putting yourself on a collision course with excluding a great wealth of information from the private sector, and from the public sector as well, might I add.

So our clear view was, yes, the West Gate distributor is a great project, and an unsolicited bid may well have hidden from the community's eyes and mine exactly what more could be done. But a market-led proposal could well open up an engagement with the community about what looks like a very worthwhile proposal that augments, that improves, the offerings that the previous government put to the last election. So we do intend making sure that we will look at the Transurban proposal under the guidelines that we put out and we are now publicly engaging the community around. The proposal expands the capacity of the West Gate Freeway — it provides a new connection with the West Gate Freeway to CityLink. It has intrinsic merit. But are we at a point where we think that the government will own it and commit to it? We are not, because I want to protect the taxpayers interests. I also want the taxpayer to think that they have actually got some ownership in the processes that are happening — they are not happening behind closed doors; they are happening in the context that, 'This is what is before us; we are considering it'.

I am really pleased to say that we have announced recently that we have appointed Barry O'Farrell's commissioner of audit, Kerry Schott, and Tony Canavan from Ernst & Young, to oversight the process, to make sure the project is stacking up and that this is not just another example of governments heading too far ahead of themselves and signing up to things that ultimately they and the community will regret.

Openness, accountability and transparency within the context of the government's priority for allocations, that is essentially what we are trying to do here, Rachel. I think the community will profit by it, I think the private sector will help us profit by it and hopefully they too will see these things as good for their businesses.

Dr CARLING-JENKINS — From your answer I find it very encouraging that you are talking about openness, transparency and accountability. Can I just ask you to confirm that you will be opening up your tender processes or market-led proposals which are accepted and contracts, once signed, to public scrutiny?

Mr PALLAS — Certainly we have taken the view that will be more open and transparent around the release of material that we have entered into. Whether they are business cases — on contractual arrangements, I think we have to tread a little bit warily. What we have said is that we will take advice from Infrastructure Victoria, once it is established, about what can and appropriately should be released in contractual terms. I do not mean to be coy around this, Rachel, but I have to be very careful too, because if I give an unqualified commitment about what we will release, we could well be in a position where I frighten the market off. Some of them see that there is some inherent intellectual property attaching to the contracts that they signed.

To give you an illustration of that — and we protected it — with the east–west consortium, they were very concerned that the state not release the schedule of availability payments incorporated within the contracts that they had entered into with the previous government. We were aware of that, and we think that was a reasonable thing to do. We found another way around giving the community an appreciation of what the real cost of those availability payments was. I produced a letter from the secretary, who gave an all-up cost and the life of the arrangements rather than showing how they financed the year-on-year contributions. So we are going to try to be as open and transparent as we can, recognising that there are some really serious implications if we get it wrong. Infrastructure Victoria will be a really invaluable addition to that.

Can I also just reinforce that the changes to the guidelines that we are putting in place should give you some confidence that we will be augmenting the openness and transparency. The new guidelines in the market-led proposals include greater transparency and disclosure details. Headline details of the proposals will be released at the end of stage 2, and that is of course why the West Gate upgrade was made public. And a description of the proposal will be publicly disclosed at the end of stage 3. Value-for-money tests are all strengthened for all proposals. Assessment processes now include a formal requirement to consider competitive processes for the delivery of the proposal, and probity arrangements are improved and were independently assessed as robust.

I must say when the Transurban proposal came we took the view, 'Well, we do not have Infrastructure Victoria in place. We could either sit back and wait for an Infrastructure Victoria process to be established, or alternatively we could create a quasi-Infrastructure Victoria process to oversight and to guide our consideration around the value of this process. That is why Dr Kerry Schott and Tony Canavan from Ernst & Young have been advising us as we have gone along, in order to tell us that there is real value in pursuing this project, and I might say that that is in fact their advice.

Mr DIMOPOULOS — Treasurer, I bring your attention to your speech, in budget paper 1, page 2. I know you have referred to the AAA credit rating a number of times, but I am particularly interested in it in relation to a big investment in this budget and how we protect the AAA credit rating in the context of the rest of the country in terms of other jurisdictions, perhaps.

Mr PALLAS — Thanks very much, Steve. It is actually a really interesting topic at the moment, because our AAA credit rating is critically important to the state. It is important not only because of the optics but because of the discipline it puts in place around the way that the government conducts itself. We are of course AAA credit rated by both Standard & Poor's and Moody's Investors Service. I think we are one of about nine sub-sovereign jurisdictions in the world that actually fall into that category. It is the highest possible rating for independent ratings agencies, and it has been achieved through governments' responsible financial management. It is something that governments of all persuasions have been committed to over the last few decades. The ratings methodologies of Standard & Poor's and Moody's do differ, and they both focus on a number of key areas, whether it is economic fundamentals, financial performance, debt burden, financial management and the level of liquidity. So the key financial ratios used by Moody's and Standard & Poor's to assess financial performance and debt burden are the ratios of operating cash flows to revenue and the ratio of debt to revenue. They are the keys.

The fundamental government sector operating surplus is estimated to be around $1.2 billion in 2015–16, and it will grow to $1.8 billion in 2018–19. This drives an improvement in the ratio of operating cashflow to revenues from 7.2 per cent in 2014–15 to 8.2 per cent in 2018–19, and a reduction in the debt to revenue ratio from 81.4 per cent to 74.2 per cent over that same period. The government has achieved these through solid financial management, recognising that these are solid financial outcomes, maintaining our infrastructure investment at historically high levels. We have estimated our investment in the budget and forward estimates period, as I say, at about $5.3 billion. Historically it has been around about 4.9 billion. GSP, as I say, is projected to be — net debt to GSP is around about 4.4 per cent. This is lower than the last published estimates of the previous government. There has been some commentary by the ratings agencies around our budget.

To put it in context, it is them assessing the budget — good, bad and ugly in terms of their overall assessment. Basically Standard & Poor's have indicated that the government's budgetary performance is likely to remain broadly consistent with its recent history by achieving operating surpluses at the non-financial public sector level, and they consider the level of debt to be consistent with a AAA rating for the state. Moody's said:

> … in addition to the cost of providing enhanced levels of services, the higher spending rate also incorporates the setting aside of greater contingencies, an approach which is fiscally prudent.

Both ratings agencies are going to obviously now have an in-depth analysis of the budget, so I do not think we can consider these to be the final views, but there is cause for some optimism in that certainly the actions that we have taken have met with broadly positive assessments. They are going to release their ratings opinions later in the year after completing a full review of the budget.

Mr T. SMITH — Treasurer, referring to budget paper 3, page 42, what is the benefit-cost ratio of the Melbourne Metro rail project?

Mr PALLAS — This project actually has been the subject of a benefit-cost ratio, a business case, but one that I think in fairness to the community we have to acknowledge requires now to be reassessed in the context of the changes to the nature of the project and also making sure that it is contemporaneous. We committed $11 billion to realise the Melbourne Metro rail project, which will include $1.5 billion over the forward estimates period.

I think there is increasing consensus. I even understand that the opposition are now indicating that they support the project, and I am pleased, I might say, for that. I think it is important for the state that to the extent that we can — and we might not always get to that point, but to the extent that we can — consensus around large infrastructure projects is important. From now until 2018 the Melbourne Metro authority will be progressing land acquisition, developing tender and contract documentation, and delivering significant early work such as tram rerouting and service relocations.

On the business case expressly, it is currently being updated, and it will be released in due course after the government and Infrastructure Victoria have had the opportunity to consider it. But I do want to make a couple of points about business cases. We said before the last election — and we meant it — that business cases should be a contingent part of the process of governments moving forward with large infrastructure projects. What that does not mean is that when assessments have occurred in the past we cannot be guided and assisted by that work. So if we go back to business cases that were produced in 2009, 2010 — business cases, I might say, that the previous government as late as 2013 were advocating in support of to Infrastructure Australia for Melbourne Metro — those business cases do need to be updated because, as I say, they need to be contemporaneous with the planning and they need to pick up any alterations in terms of the overall engineering process, plus I think people need to have some certainty that we are getting closer to a degree of specificity around cost and financing and funding options.

But the business case was so developed, so substantial back then that not only did the previous government endorse it and support in their advocacy to Infrastructure Australia but Infrastructure Australia rated as one of the most important infrastructure projects in the nation. It is unfortunate of course that we are in this argument about what level of contribution, if any, the federal government would make to a project of this nature, but I think the fundamentals of a business case are about saying, 'Are you investing your money to get a good outcome?'.

Mr T. SMITH — What is the current status — do you not have one?

Mr PALLAS — Well, the status of the business case is that it is being updated, and obviously when it is updated it will be in the public domain, but that is not to say that we were removed or without information to guide us. In fact the level of work that had gone into this project is literally years and years of research, effort, analysis from consultants, engineers, so much so that it was considered to be, as I say, the most worthwhile major public transport infrastructure project in the nation, one that the previous government advocated for as late as 2013 to Infrastructure Australia in their submission.

So the point I make is yes of course we have got to update them and yes of course we need to be guided by the advice and the guidance that they incorporate within them, but we should get to the point of saying, 'While we are constantly updating' — and we will — 'the business case, we should do nothing more and we should wait for all the thinking to have effectively occurred'. We need to plan first, and then we need to build, but essentially we are at a level of confidence in the quality of this project that we can have some clear understanding that moving forward there is sufficient specificity around the previous business case and we will be guided by the work in the new business case. I believe the Premier has indicated that it is likely that business case will be available by the end of the year.

Mr T. SMITH — On a supplementary, when did the revised business case process begin, Treasurer?

Mr PALLAS — I think you would probably need to direct specifically your inquiry to the public transport minister as they are the minister responsible and — —

Mr T. SMITH — So you do not know?

Mr PALLAS — Let me see. I might see if I can find it. We cannot give you any greater specificity. If you would like, we will try and give you a date outside of the session — —

Mr T. SMITH — It would be appreciated.

Mr PALLAS — I am more than happy to tell you when. My secretary of the department tells me he assumes it started after 29 November. I do not think that would satisfy you, so we will see if we can get some dates and that information for you.

Mr T. SMITH — It would be greatly appreciated. Thank you, Treasurer.

Ms PENNICUIK — Treasurer, I would like to return to the subject that you and I discussed in the past in one of your previous roles. The budget papers talk about the long-term asset recycling and possible long-term lease of the port of Melbourne. It talks about the proceeds of that — in budget paper 2, page 11 — being put into a Victorian transport building fund. But on page 61 the paper also talks about net debt as a proportion of GSP falling, largely reflecting receipt of proceeds from the medium-term lease of the port.

Treasurer, the Legislative Council has called for the release of the scoping study for the privatisation of the port of Melbourne by KPMG last year, and that has not been released, despite your government's claims of openness and transparency. So the public knows little about what the plans are. If I refer to the port of Melbourne's annual report from last year, the net assets of the port are $1.7 billion and it returned a total dividend of $43, nearly 44, million. It does that every single year, and if you project that out 20 years, you would probably get around $1 billion in dividends from the port, thereabouts, probably more. So this is a significant issue for the people of Victoria to dispose of this asset, because even a long-term lease is a sale in any other terminology. The question is: what regulation will be put in place prior to the offer of the sale or lease to govern prices, rents, fees and competitive behaviour by a proposed private port operator, and when will the Parliament and the public see details of that regulatory model?

Mr PALLAS — Can I say that the reason we are not releasing the KPMG report is that it is a document that went to cabinet-in-confidence protection under the previous government. If the previous government, the opposition, agrees to the release of that document, I think there is one element that goes to actual price — expectations around price for the port, the sale of the long-term lease — but in all other respects we would be happy pretty much well to release it. So it is essentially a question for those parties who are part of the process of actually asking for the release of these documents to give the appropriate waivers around documents of previous governments. Try not to blame us for what the Liberal Party might be saying about what should or should not be released.

In a broader sense what we have said of course is we are committed to the sale or the longer term lease of the port of Melbourne. We are very much of the view that you have got to make sure that what we are producing here is something of value in the long term for the state. So the asset recycling strategies should not just be a standard operating procedure of government, but we should look at the value we are getting from our assets. Can they be applied to better purpose? Will the state benefit from the recycling? So the $40 million dividend that you are proposing does have to be weighed up. It is an amount that comes off our operating budget each and every year, but on the flipside of that, can that money be put to better use in capital terms in the short term? I certainly am of the view that that is the case, and my party is certainly of that view.

The sort of things we are looking to do, if you are looking for the question as to what would the regulatory environment look like for the sale of the port — I think I have to be a little bit circumspect, because the Parliament has not yet been given the opportunity to scrutinise the legislation, which will, I can assure you, be introduced very shortly into the Parliament. We accept that we will have to have a process of engagement with all parties around its content and terms, but we will be making sure that a number of preconditions are very clearly outlined to ensure that the regulation around the port of Melbourne is in place to ensure that it continues to operate competitively and efficiently to support Victoria's freight logistics network.

We will require that the transaction delivers optimal overall long-term economic benefit to Victoria and Victorian businesses. We will be treating employees fairly and equitably, and there will be guarantees as to continuing employment in that respect for port employees over a period of time. We will be maximising the financial return to the state from the transaction within the overall policy settings that will be apparent from the legislative framework and of course any public statements that the government has made while minimising the ongoing financial risks and liabilities to the state. We will also be ensuring that the appropriate residual activities of the port — and some of those are quite important, whether they are marine, environmental and safety functions — remain with the state and are managed in an efficient manner. We will be completing the transaction efficiently with appropriate probity, transparency and accountability standards, and we will be looking to secure Victoria's continued role and place as the freight and logistics capital of the nation.

Ms PENNICUIK — Thank you Treasurer. It is interesting that you agree that the port as it stands is a public asset which, as I said, according to its own report has $1.7 billion of assets and returns a substantial dividend to the state every year and provides a whole lot of other services, which you just outlined yourself. So in terms of trading that asset off against other assets, it is a very significant decision on behalf of the state of Victoria, particularly when you are talking about an asset that delivers a dividend as opposed to trading that off for assets that may or may not deliver a dividend or an equal dividend or benefit to the people of Victoria.

I take the answer you have given me about the regulatory proposals that may come forward, but also the ACCC has already been asked to intervene over the currently proposed rent rises at the port of Melbourne. Has your government discussed these with the ACCC in the context of the proposed sale or lease, and do you agree that such arrangements will impact on the proceeds you may get from the lease?

Mr PALLAS — On the introductory comments, Sue — I will come back to the question of the ACCC — the reason we are going down this path, let me be very clear, is because we told the people of Victoria that this is what we were going to do if elected to government. I might say there was a level of consensus around this on both sides of politics, we believe.

Ms PENNICUIK — Not from all sides.

Mr PALLAS — Not from all sides, no, Sue; I understand that. My view is that in public life you have to do what you said you were going to do. That is a key part of what this budget is all about: delivering on our commitments. If we were unable to implement the sale of the port, that would put a considerable impediment upon the capacity for us to deliver. It would take the anticipated value of that sale out. You have quite rightly identified that the government, in opposition, under its policy Project 10 000 committed to putting funds into a transport infrastructure building fund, and we will. The principal use of those funds will be for the level crossing removals that we identified and also for other infrastructure projects identified in our Project 10 000 policy that we took to the election.

On the issue of the ACCC's observations around the rental negotiations, I just want to put this into context. What is happening here is DP World, which is one of the two stevedores at the port of Melbourne, is in the process of a biennial market rent review under the terms of its lease with the port of Melbourne. This is a business-as-usual review by the port itself. The port, following the recent third operator leasehold arrangements, was confronted with a valuation proposal that put a considerable increase on the rent of stevedoring facilities for the port. It had nothing to do with the context of the port sale. This was an annual review process that was put in place and activated by the port itself. Essentially all it did was apply the rate that the new third operator put to rental space for stevedoring facilities at Webb Dock. Understandably there was a substantial level of concern expressed by DP World.

Ms PENNICUIK — Treasurer, you are aware, too, that concerns have been raised by other producers and by the Tasmanian government as well?

Mr PALLAS — Other?

Ms PENNICUIK — By producers that use the port and by the Tasmanian government.

Mr PALLAS — I have been in direct contact with the Tasmanian government. Rather than go too far on a tangent about the issue of who is concerned and who is not, let me take you through the process. You have asked a question about the process that is going on, and I am more than happy to answer any additional questions you might have about impact and effect of these processes. We have got, in effect, a process whereby there is a rent review every two years, which is a standardised process going through with DP World. It resulted in a higher rental rate as a consequence of a third port operator being brought in by the previous government. DP World objects to that — it takes the view that it is not a fair market reflection — and there is now a process of independent valuation going on by an independent third valuer, which is effectively trying to work out whether or not there is merit to DP World's concerns. We have got one operator that is paying these rents but we have got two existing operators that do not like the suggestion that they should be. We understand that these matters are of concern. The port has agreed to temporarily suspend its right under the contract to immediately charge 80 per cent of the proposed market rate rent within 60 days of the matter being issued. It has stepped back and is now going through a process of review.

The CHAIR — I ask the Treasurer to conclude his answer.

Mr PALLAS — DP World has delayed this engagement. The market rent review was not triggered by the port lease transaction; it is an entirely separate process managed by the port, not by me. Effectively an independent valuation is now underway. We will find out what the real appropriate market rate to be charged in this context is, and as I understand it that may well form the context of a negotiated outcome that could ultimately get to a settlement of these issues.

Ms PENNICUIK — Chair, I just want to say that my question about the ACCC and its call for an undertaking has not been answered.

Mr PALLAS — Sorry. On the ACCC, I will be brief and say that we take the view, with respect to the ACCC, that these matters are about market regulation and market pricing, so it is passingly strange to hear the ACCC express a view about seeking to impose market rigour on what was historically a duopoly. We take our responsibilities in managing the port seriously. We have got an independent valuation process going on, and we have got a process that is essentially being managed by the port, and our view is that the fact that there are market rates going in place is an appropriate mechanism to work out whether or not the valuation on that land is appropriate.

Ms SHING — Treasurer, I take you to BP5, pages 35 and 40. They set out output and asset contingencies not allocated to departments at (c). I am wanting to know if you can explain why it was important to rebuild these contingencies as part of the budget process.

Mr PALLAS — Thank you very much, Harriet, for your question. 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. An example of the sorts of things that might be funded from contingency are costs associated with a natural disaster, for example — having sufficient put aside for bushfires. These costs will be incurred whether or not there are provisions for them. It is something that governments have to do. The community expects us to do it, and prudent governments make adequate contingency arrangements for them.

So if we had not made allowances for these costs, they would be reflected in weaker budget outcomes than had previously been forecast. So our existing contingencies at the 2014–15 budget update we utilised to fund the government's election commitments, consistent with our LFS 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.

DTF's assessment noted that the aggregate impact of the government's election commitments on net debt, once available contingencies and identified savings and efficiencies are applied, is broadly cost neutral by the end of the forward estimates period of 2018–19. I think that is a pretty clear positive endorsement of the rigorous process that we went through before the last election, and it has provided us with the room to make the decisions that we have made. We have applied much of the existing contingency to offset the cost of election commitments, and it shows that the output 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.

Of course we could have delivered even stronger fiscal outlooks if we had chosen to do that in the sense that the representation in the 15–16 budget had lower levels of contingency. We have therefore assessed to put in higher levels of contingency in order to acquit future opportunities, future decisions that governments will have to make in the future. And it would appear that the credit rating agencies agree with that strategy. Moody's in its post-budget press release noted:

> … in addition to the cost of providing enhanced levels of services, the higher spending rate also incorporates the setting aside of greater contingencies, an approach which is fiscally prudent.

I see that as an endorsement of the strategy that basically says, 'Leave capacity for the future. Leave capacity for future decisions'. So a suggestion that, for example, there is lower than the previous government's capital spend I think can be well and truly countered with an argument that there is more than sufficient capacity to deal with the unforeseen and for future decisions.

Mr MORRIS — Treasurer, can I refer you to BP5, page 188, in particular the fire services property levy. Given your promise of no new taxes or tax increases beyond CPI, can you guarantee that no property owners will pay a real increase in their fire services property levy in 2015–16?

Mr PALLAS — A real increase?

Mr MORRIS — Beyond CPI.

Mr PALLAS — Beyond the mechanisms that you established in the fire services property levy surely?

Mr MORRIS — You gave a guarantee that there would be no new taxes and no tax increases beyond CPI. I am asking you if the fire services property levy is going to exceed the limits that you placed on it.

Mr PALLAS — We gave a commitment at the last election and we are very serious about implementing it, and the commitment of course is very clear about making sure that we recognise the burdens that Victorian families operated under. The fire services property levy revenue estimate for the 2015–16 budget is about the same as the 14–15 revenue estimate in that budget. Consistent with our promises to the Victorian people to fully fund our election commitments without the need for tax increases, investments in fire services in *Labor's Financial Statement* have not been funded — can I just enforce this point: not been funded — through the fire services property levy. The actual amount of FSPL revenue collected in 2014–15 will be published in the 2014–15 financial report for the state of Victoria.

But, Deputy Chair, the government has been very clear. We have decided, consistent with our commitments, not to apply the FSPL to election commitments outlined. Of course the FSPL, the tax, remains as it was set by the previous government. It is a tax that has a base rate and has a capital improved value component. That tax remains and will not be adjusted for the purposes of funding these improved services.

Mr MORRIS — I appreciate the Treasurer's advice on that and also his reference to the aggregates, even though I did not ask about the aggregates. But given that he has referred to that, and given that CPI in Melbourne is currently sitting at about 1 per cent, Treasurer, how can you justify increasing fees and charges by 2.75 per cent in the coming year?

Mr PALLAS — It is a supplementary question on an entirely different issue, but — —

Mr MORRIS — On an issue that you raised in your answer to the substantive question.

Mr PALLAS — I fail to see that I did. But nonetheless, our position is the position of the previous government — that is, there is a methodology that has been put in place for the adjustment of fees and fines and charges of the state. Those adjustment processes have been simply preserved and maintained. And might I say, we said before the last election, we incorporated it into our *Labor's Financial Statement* and the statements that I made at the time that we released it, that there would be no adjustment to the methodology that was put in place for the adjustment of fees and fines. We were very clear about that, Deputy Chair. Fees and fines for the 2015–16 period are expected to be slightly higher than the 2014–15 period in terms of revenue. Primarily it is due to a higher volume of regulatory fees being collected, such as Infringements Court lodgement fees from local councils, largely for parking violations, and an estimated increase in fees on police-issued fines such as penalty reminder fees.

Fine revenue for 2015 is expected to be, as I say, largely consistent with 14–15, with growth in line with indexation — the indexation methodologies that have been consistently applied. Over the forward estimates fees and fine revenue growth is broadly consistent — that is, over the forward estimates period proper. The 15–16 budget estimate for that year is $8 million lower than the 2014–15 budget estimate for 2014–15, primarily due to the impacts of roadworks, improved driver behaviour and mobile camera placement in outer metropolitan and regional locations being the subject of greater deployment, and these were reflected in the *2014 Victorian Economic and Financial Update*.

Ms WARD — I draw your attention to chapter 3 of budget paper 2, which is entitled 'The jobs challenge'. This is something of particular interest to my electorate. Why are jobs such a major focus of the government's 2015–16 budget, and what budget initiatives are designed to meet this challenge?

Mr PALLAS — The government's position is that we believe that everyone in the state deserves the dignity and security, might I say, of a stable job in a growing industry. That is why in the 2015–16 budget we place considerable emphasis on jobs and getting the Victorian economy moving. Victoria has a number of competitive strengths. We have a skilled workforce, we have a diverse industry base, we have livable cities and regions and strong transport linkages. The budget builds on those strengths, and it does that by making responsible investments that will prepare this generation and generations to come to be able to compete in the global economy.

The government recognises the challenges. Our labour market conditions have been weak over the last four years; I think that is no surprise to anybody. The unemployment rate has risen, and there are broader measures for spare capacity — that is, people who are either unemployed or in their own view underemployed. It is at a 20-year high. Young people have been particularly affected, with youth employment falling sharply in recent years. Some workers are also vulnerable to industry structural change, including of course the upcoming closure of the automotive manufacturing industry in Victoria.

Since 2014 the labour market has shown some tentative signs of improvement. The 2015–16 budget is focused on creating jobs and also investing in education and skills to provide employment opportunities for all Victorians. Victoria's Back to Work strategy will help to provide 100 000 jobs, giving young people the skills they need for the jobs they want. The government has delivered our biggest ever education budget. We see education as basically being an investment in our most valuable resource — our people — and therefore in terms of future generations education will be resourced to ensure that we can skill our future workforce to be able to compete in an increasingly more competitive global community.

The government is also providing $12 million to establish tech schools right across the state, and the schools will open up to students from years 7 to 12. They will learn skills alongside a comprehensive secondary education. That is on top of our investment in schools and the TAFE sector, which is receiving additional funds to complete the TAFE rescue arrangements. There is $300 million to complete the TAFE Rescue Fund, and $50 million is being provided for the TAFE Back to Work Fund. The government understands that many young people are in a situation where they need greater advice around work so they can get themselves into a position where they identify the skills they need.

The government is making a major investment in creating jobs now and into the future. That is why the $100 million Back to Work scheme is important. It is also why the recasting of our industry systems is so important. There is the Premier's Jobs and Investment Panel at $508 million and a start-up initiative at $60 million. The government's $200 million Regional Jobs Fund will play a critical role in collectively assisting in the identification of where the growth areas are that are coming through in the Victorian economy that the government should be putting its effort and emphasis into. We see them as medical technology and pharmaceuticals, new energy technology, food and fibre, transport, defence and construction technology, international education, and professional services. Those moneys, together with $200 million for the Future Industries Fund, are about identifying those growth areas, skilling up the workforce and making prudent investments, getting behind those industries that are growing into the future.

Mr D. O'BRIEN — It is a nice segue on jobs into my question, which is related to the public holiday decisions. As a regional MP I know that many of our regional businesses are concerned about this, and I want to share with you aspects of an email I got this week from a businessperson in my electorate:

> Just want to voice my concern over the grand final day public holiday I will be closed Friday not much point in opening … mate it's hard enough now to make a bob Dan reckons he's going to create all these jobs how when everyone is closed …

In relation to employee expenses, given the significant public sector wage crisis, can you inform us of the additional costs that will be imposed on the budget as a result of the grand final eve holiday?

Mr PALLAS — I suppose the — —

Ms SHING — On a point of order — sorry, Chair — can we get a budget paper reference from you, Mr O'Brien?

Mr D. O'BRIEN — Budget paper 5, page 22.

Mr PALLAS — The first thing I would say is that the government was pretty clear before the last election that these were part of the mandate we sought from the Victorian people. We put it out there publicly. It is because we believe that Victorians work hard and do deserve recognition for their work. They should be appropriately paid for working on public holidays, and they should also be entitled to public holidays — additional public holidays — and we said we would do it, and we are going ahead and doing it. It was an election commitment, and we will deliver it. The government will continue to talk to a range of stakeholders about programs, initiatives and election commitments — an in-depth consultation with a broad range of stakeholders — which will also inform this part of the analysis as part of a regulatory impact statement that the government is currently undertaking.

Funding is required to deliver this election commitment, which has been dealt with as a part of the budget process. Wage costs are a normal part of the base funding for departments. We have made appropriate adjustments in base funding from time to time to reflect changes in cost structures. The total cost of public holidays varies each year of course. You get differing public holidays — —

Mr D. O'BRIEN — Can you tell us what the total additional cost of this one is?

Mr PALLAS — What I can tell you is that we effectively fund departments for their employment costs. We do not disaggregate them, nor do I concern myself with the disaggregation of what those costs are. We expect departments to be able to identify what their projected costs are going to be. We make provision for those costs, and we have appropriately made provision for those costs in the budget. Essentially that is incorporated within the departmental allocations.

Mr D. O'BRIEN — But if you have incorporated it, you must know what the additional costs are.

Mr PALLAS — Is this the third supplementary?

Mr D. O'BRIEN — It is the same — I am trying to get an answer to the first question.

Mr PALLAS — I have just given you the answer. We pay — —

Mr D. O'BRIEN — No. You have said you have accounted for it, but you have not said how much it is.

Mr PALLAS — Because it is picked up in a broad allocation to the departments. We effectively fund departments for the delivery of services. Those services are pre-empted upon their staffing costs in part. We effectively say to the departments, 'Tell us what you need in terms of your capacity to continue to deliver services and to grow those services consistent with the allocations that the government has made'. They give us a figure, and we make provision for it. It is essentially a global figure that is provided for, because we effectively provide for service delivery and outcomes. That is what we have made provision for.

The CHAIR — Mr O'Brien, on a supplementary question.

Members interjecting

Mr D. O'BRIEN — I am sorry, but we are having to ask the question again and again because we are not getting an answer to the first question. I take up your point in the answer you gave about the departments. In respect of the departments, the minister responsible, the Minister for Small Business, Innovation and Trade, has in fact three times in Parliament said he does not know and that it is a matter for the Treasurer. He has failed to disclose the cost of these new public holidays. He does not know. Is it a fact now that you do not know either?

Ms SHING — On a point of order, Chair, again, asked and answered. On that basis I cannot see how the supplementary seeks to extract any additional information. The Treasurer has indicated very clearly it is — —

Mr MORRIS — There was no information provided in the first answer.

Ms SHING — The information may not have been what you wanted to hear, but the Treasurer has said clearly it is a global figure. It is up to the departments to spend that money as they see fit on the employee costs associated with their payroll.

Mr D. O'BRIEN — On the point of order, Chair, the Treasurer said that it is up to departments. I referred to one of the department's ministers, in fact the minister responsible for this decision, who has said three times in Parliament he does not know; it is a matter for the Treasurer.

The CHAIR — Does the Treasurer wish to respond?

Mr PALLAS — I am more than happy to respond. I am not sure that I am going to do much more than simply endorse that what the minister said in the context of his contributions in the upper house was exactly right. He was going through a budget process.

Mr MORRIS — He does not know.

Mr PALLAS — He was going through a budget process in terms of the forward estimates and the government's liabilities. Wages costs are a normal part of the base funding for departments. His department presumably was going through a process of identifying what its base funding requirements would be. They have subsequently put in their base funding. We fund for the delivery of services. That is the point of actually funding departments — their employee costs and all other associated issues. Those costs have now been fully acquitted, and they are provided for in the budget.

Mr D. O'BRIEN — But they are not — —

The CHAIR — Mr O'Brien, you have asked your supplementary question, and the Treasurer has answered it. The next question is from Mr Dimopoulos.

Mr DIMOPOULOS — Treasurer, I refer you to budget paper 2 and the sections that refer to the international economic context on pages 24 and 25 and the risks to the outlook on page 26. You have touched on the fact that the government cannot necessarily anticipate every eventuality — natural disasters and other things. But to the extent that it is possible, what mitigation measures are in this budget in relation to protecting Victoria's ongoing financial viability should the world turn upside down?

Mr PALLAS — I suppose volatility in Victoria's revenue base since the global financial crisis really does serve as a pretty stark illustration that our economy and our state's finances are inextricably bound to the global economy. We know 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, and the sharp fall in oil prices as a result of subdued global markets and also increased supply, which is negatively affecting oil exporters but benefiting net oil importers, including most advanced economies.

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 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.

Against that backdrop of global economic uncertainty the government has delivered a fiscally strong, responsible budget; operating surpluses of at least $1 billion each year going forward; substantial output and asset provision for future budgets, which I think is important and gives us capacity in the event of unforeseen events; and net debt declining to 4.4 per cent of GSP by the end of the forward estimates. It is all about providing us with investment in the important things, whether they are services or key infrastructure — the right infrastructure at the right time — but also making sure that we have capacity in adverse circumstances where the state's resources are called upon to deal with economic uncertainty and deterioration in international markets.

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 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. Net financial liability is declining to 12.1 per cent of GSP by June 2019 — the lowest since 2008–09.

Mr T. SMITH — Treasurer, have you ever received any acting or drama classes from Mr — —

The CHAIR — Mr Smith, this does not relate to the budget papers.

Mr T. SMITH — I refer you to page 22 of budget paper 3. How many sessions did you have, and what was the cost, if indeed this occurred?

Mr PALLAS — I can tell you that when it comes to acting classes I am beyond all help. What you see is what you get. I am not going to confirm or engage in any discussion around what assistance I have had in being able to perform my role. I simply say that it is a normal part of the process of government that government ministers, might I even say previous government ministers, are provided with support and assistance in being able to manage their functions. I have been provided with that support and assistance. It has been very good support and assistance. Today it has served me well. I have not had to wax lyrical or even call upon my thespian allusions. I simply say this: the support that I have received has been appropriate.

The CHAIR — Mr Smith, I will allow you a supplementary, but I will be very interested to see where this goes.

Mr T. SMITH — My supplementary question is: who made the decision to hire Mr West and why? Again, I refer you to budget paper 3, page 22.

Mr PALLAS — 'I do not know' is the answer. I am in a position where essentially I am more than happy to take offers of free assistance for my performance. I will take free advice from those opposite about how well I have performed today, but most importantly I have to tell you that I do take this job seriously. It does require us to look at serious issues, and quite frankly the support that ministers get to perform their jobs — to provide the community with confidence that we are across our briefs and managing our portfolios seriously and professionally — is a key part of the job. Assistance of the nature that you have described is appropriate.

The CHAIR — That concludes this morning's hearings. I would like to thank the Treasurer of Victoria, the Honourable Tim Pallas, MP, for attending, as well as Mr Martine, Ms Skilbeck, Mr Webster and Mr Brennan and representatives of the Treasurer's staff.

Witnesses withdrew.