VERIFIED VERSION

PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

Inquiry into 2013–14 and 2014–15 Financial and Performance Outcomes

Melbourne — 16 February 2016

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Mr David Webster, Deputy Secretary, Commercial,

Mr Mark Johnstone, Acting Deputy Secretary, Economic, and

Ms Gayle Porthouse, Deputy Secretary, Corporate and Government Services, Department of Treasury and Finance.

The CHAIR — I declare open the public hearings for the Public Accounts and Estimates Committee inquiry into the 2014–15 financial and performance outcomes. All mobile telephones should now be turned to silent. I would like to welcome Mr David Martine, Secretary of the Department of Treasury and Finance; Ms Melissa Skilbeck, deputy secretary, budget and financial management; Mr David Webster, deputy secretary, commercial; Mr Mark Johnstone, acting deputy secretary, economic; and Ms Gayle Porthouse, deputy secretary, corporate and government services.

I would also like to welcome all witnesses sitting in the gallery. Any witness who is called from the gallery during this hearing must clearly state their name, position and relevant department for the record.

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 transcript for verification as soon as available. Verified transcripts, any PowerPoint presentations and handouts will be placed on the committee's website as soon as possible.

Witness advisers 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 must remain focused only on the persons speaking. Any filming and recording must cease immediately at the completion of the hearing.

I now give the witnesses the opportunity to make a brief opening statement of no more than 10 minutes. This will be followed by questions from the committee.

Mr MARTINE — Thank you, Chair. I was not planning to make a lengthy opening statement, but I might just make a couple of very brief comments, which is really around just providing the committee with a little bit of information about what the Department of Treasury and Finance does. Essentially I am quoting page 12 of our annual report and just briefly running through the four objectives that the department has. Firstly, 'sound financial management of Victoria's fiscal resources'. Essentially the department has a central role in shaping Victoria's economic, social and fiscal policy.

The second objective is 'guide government actions to increase Victoria's productivity and competitiveness'. The department, in that regard, provides advice to the government of the day on economic and financial issues, including longer term economic development, regulation, financial strategy and taxation policy.

The third objective is 'drive improvement in public sector asset management and the delivery of infrastructure'. In that regard the department develops and applies prudent commercial principles and practices to influence the delivery of government policies. And the fourth objective for the department is to 'deliver efficient whole-of-government common services to the Victorian public sector'.

That is quite a simple summary of the four objectives that the department has. Three of those essentially are providing advice to the government of the day — financial, commercial, economic and policy advice — and the fourth one is providing a number of services across government. So that is essentially the functions. I have with me my four deputies, so those four functions are split across the four of those. With that very brief statement, I am more than happy to take the committee's questions.

The CHAIR — Sure. I might commence, and it is wonderful to have you here before us today for this session.

Ms SHING — Arguably there has never been a more exciting time to be appearing before PAEC.

The CHAIR — Thank you, Ms Shing.

Mr MARTINE — We share that excitement.

Mr T. SMITH — It just starts, doesn't it!

Mr MARTINE — We will withhold our enthusiasm.

The CHAIR — Thank you, Secretary. I just refer to page 40 of the questionnaire which you provided to the PAEC secretariat where you indicated that the goal for infrastructure investment is 1.3 per cent of GSP, calculated as a rolling five-year average, and that the 13–14 result was 1.69 per cent and the 14 result was 1.58 per cent. I was just wondering whether you could advise whether there is a desirable figure, just not looking at our jurisdiction but jurisdictions elsewhere, with our level of population growth — growing between 1000 and 1500 people per week in terms of Melbourne, let alone what is happening in country Victoria. From your perspective, is there a range that is desirable in terms of infrastructure spend to cater for and to respond to that growth in population?

Mr MARTINE — Thank you for the question, and I am assuming, Chair, you are referring to page 40 of the response?

The CHAIR — Yes, that is right.

Mr MARTINE — As you have identified, particularly with population growth here in Victoria, we are actually the fastest growing state. Our population growth is forecast to grow roughly around the 1.8 per cent across each of the years, so that does impact on particular infrastructure needs for the state. It is certainly an important priority for governments here in Victoria to ensure that adequate investment is provided, in particular infrastructure.

One of the keys of ensuring that an infrastructure program can be rolled out to meet those population needs is to actually maintain a strong fiscal position. One of the key priorities there, and it is articulated in the budget papers — both the current government but former governments have had very similar fiscal objectives — is what I kind of describe as living within your means. So that if you effectively can run budget surpluses — so operating surpluses — it frees up that capacity to ensure that appropriate investment can be made on the infrastructure needs.

It is very hard to put a particular figure on the exact amount, because a lot of the infrastructure spends are long term. Projects that you start planning for now and investing in, a lot of those benefits flow — might be 5, 6, 10 years time. It is very difficult to sort of say that 1.69 per cent or 1.6 per cent is actually the right figure. I think probably the best way to answer that particular part of the question is really to say that if you maintain good finances within the state, it gives the opportunity then for the government of the day to undertake those appropriate investments. It frees up the cash and you are not essentially using borrowings for funding recurrent, which is actually the important thing. It ensures that those borrowings can then be solely used for investment in productivity-enhancing infrastructure projects.

Mr MORRIS — Picking up on your point, there were, as we know, some changes in terms of the government's fiscal objectives between 2014–15 and 15–16. Can you indicate to us whether the objectives that were applied to the assessment of the 14–15 financial year were those that there were set out in the budget for that year or whether they are in fact those outlined in the 15–16 budget — or something else again, given that there was a change midyear.

Mr MARTINE — Thanks for the question. Page 13 of our department's annual report, and I will make that reference; I am not sure whether you have that with you. Effectively we report on that page against the original objectives that the year started with, but we do make the comment, in the paragraphs under those objective indicators, the change that occurred under the new government. Just to clarify those: the objective indicators are outlined on page 13. There are three of them:

1. Demonstrate strong fiscal discipline by maintaining an annual budget surplus of at least $100 million

2 General government net debt reduced as a percentage of GSP over the decade to 2022.

3 Effective financial risk management and prudential supervision of public financial corporations and public non-financial corporations.

Those three objectives were essentially the objectives as articulated by the former government in the lead-up to or the beginning of 14–15. The new government's objectives were outlined in the budget earlier this year, and essentially, once again, the three objectives and in the same order for the upgrade in surplus:

> A net operating surplus consistent with maintaining general government net debt at a sustainable level over the medium term.

In terms of net debt the target or objective being:

> General government net debt as a percentage of GSP to be maintained at sustainable level over the medium term.

Then with respect to superannuation liabilities:

> Fully fund the unfunded superannuation liability by 2035.

On page 13 of our annual report we have that discussion where we kind of reconcile — reconcile is perhaps not the right word — but we mention both the objectives. We certainly started the financial year with the former government's three objectives.

Mr MORRIS — By way of supplementary, if I could, and I guess coming out of that, in your view what is a sustainable level of government debt?

Mr MARTINE — That is a very good question to have a discussion on. As the committee would no doubt be aware, we have here in Victoria a AAA credit rating by both Standard & Poors and Moody's. Our debt profile at the moment: roughly about 6 per cent in 14–15, dropping down to 4.4, which was outlined in the budget update to the end of the forward estimates, so we have got that trajectory downwards. In the assessments undertaken by the two ratings agencies, they are very positive about the state's finances, and they have been positive for a number of years. Quite a bit of that comes down to what I mentioned in my answer to the earlier question about, in a sense, the state living within its means and maintaining budget surpluses.

I guess without making too many comments about what happens in other jurisdictions, that is one of the issues at the commonwealth level. Their net debt as a proportion of GDP is going to peak in that 18 to 19 per cent range, which internationally is not incredibly high. But their big challenge is they are still running budget deficits, so that adds that complexity to them.

The comments that we get from Standard & Poors and Moody's about the state finances, which reinforce our AAA, are very positive: 'a very strong financial management', 'strong budget performance', 'very strong liquidity'. I guess one of the important points they draw out in both of their comments is the strong and diverse economy we have here in Victoria. Unlike some of the mining states, where through the mining boom there was clearly very strong economic growth in WA and Queensland, as the mining boom drops off they have got some significant challenges, and we saw that with some of the down-writing of their revenue forecasts in December — a quite significant writing down.

Overall our state finances: I would describe them as strong. Six per cent debt to GSP has been assessed by the ratings agencies as fine and sustainable at a AAA credit rating. We are currently projecting by the end of the forward estimates for the budget update in December down to 4.4, which obviously we will be updating as part of the budget parameters in early May.

Mr DIMOPOULOS — Further on your point about the revenue in the mining states, can you discuss some of the underlying revenue trends for Victoria in terms of 14–15?

Mr MARTINE — Thanks for the question. Perhaps if I start with a little bit of context about revenue in the state — and I am drawing on data in the 2014 annual financial report — essentially we receive revenue in the order of $54 billion. The rough metrics on that are state taxes account for about 18 billion of that. The bulk of the remaining money comes from the commonwealth, and a large proportion of that is GST revenue. That sits at about 11, and then there are grants from the commonwealth, either special-purpose payments for health and education or national partnerships. I think we had a discussion a month or two ago about that relationship with the commonwealth. So they are kind of the rough metrics: overall, about 53 billion of revenue; state taxes account for about 18 of those.

Our biggest tax bases: we have got two that contribute most — or not most — but the largest two tax bases are payroll tax and land transfer duty. Payroll tax grows — or we are forecasting as part of the budget update — at about 5 per cent. The long-run average — well, the average for the last five years is at 4.8. It is a reasonably stable tax base. The other big one is land transfer duty, or stamp duty on property transactions. That accounts for 5.4 billion of that. That one in particular is very hard to forecast. Just as an example, in 13–14 land transfer duty grew by 27 per cent; in 11–12 it fell by 15 per cent. So it is not an easy tax base to forecast. That is where quite a bit of the volatility occurs in terms of our taxes.

Most of the other tax bases we have here in Victoria are reasonably kind of stable. The other one on the revenue side that can be quite variable is, of course, the GST. That is where what we receive here in Victoria is dependent on, in a sense, what happens nationally and also what happens in other states. So as their economies grow at a slower rate and their own revenue falls, that can impact on us here in Victoria in potentially a material sort of way. So our relativity, which is in a sense our share per capita, sits at about 0.89, so we are not quite getting our population share. As the other states' economies vary, their claim on the pool will change, and as they potentially get more, we potentially get less.

The other key driver on the GST, of course, is what happens with consumption spending. That drives kind of the size of the pie that we all fight over to get cut up. At the moment national consumption is probably growing a little bit below trend nationally. We are not too bad here in Victoria, but of course it is really driven by what is happening nationally.

In a sense that is kind of a brief sort of snapshot of state revenue: 54 billion. About 18 we kind of control ourselves, and then a couple of those, the more significant, are payroll tax and land transfer duty.

Mr D. O'BRIEN — Secretary, if you just go to page 14 of the questionnaire responses, it refers to the proceeds from the sale of the Rural Finance Corporation. You will see in the table there the estimated cash flow for 14–15 was 119 million but the actual was 1.45 billion. What is the difference there? How has that come about, and what does that mean for the net value of the sale of RFC?

Mr MARTINE — I might just ask Mr Webster to provide a little bit of detail.

Mr WEBSTER — Rural Finance has two elements in their capital structure, effectively equity from the state and loans from TCV. I believe the 1.4 billion is the equity return plus the repayment of the TCV loan, but I will take that on notice and confirm that.

Mr D. O'BRIEN — Why was there such a significant difference, though, between the estimated and the actual? You surely would have known what that — —

Mr MARTINE — Perhaps during the course of this morning, because we have got 3 hours, we might endeavour just to try and get that simple explanation of the difference between the estimated and the actual, because as you pointed out there is quite a significant difference. I suspect the answer, hopefully, will be quite a simple one.

Mr D. O'BRIEN — I suspect it is an accounting one, not that we suddenly have got a billion dollars more than we thought we were going to get.

Mr MARTINE — Without turning around, I will task my people sitting behind me to endeavour to try and get an answer in the next hour so we can provide that to you.

Mr D. O'BRIEN — That would be great. Thank you.

Ms SHING — Thank you everyone for coming along today. I would like to — following up on the question from the Deputy Chair and your comment in relation to debt — look at the effect of employment growth on payroll tax revenue and to ask for general comments in relation to that impact across the board.

Mr MARTINE — Thank you for the question. As I indicated in one of my earlier answers, payroll tax that we raise in the state: for 15–16 in the budget update, forecasting about 5.4 billion, growing at about 5 per cent. The average for the last five years has been 4.8 per cent. So it is a reasonably stable tax base. It is obviously affected by a number of factors. Levels of employment is important, but likewise composition of employment is important as well. Essentially what impacts on payroll tax is average hours worked, so the composition between full time and part time can be a factor and also the sorts of jobs that are created. There is a threshold on payroll tax of $550 000, so for example, if we observe growth in employment coming from very small businesses that are sitting below the threshold, then obviously we will not see that applying to the payroll tax estimates. So the composition of employment is quite important.

We are seeing here in Victoria at the moment that our labour market is not too bad. Unemployment is trending down a bit. The data we do get out of the ABS on unemployment, it is probably fair to say, is quite volatile. Some months we do get some large changes. We had one of those late last year, where we dropped down to 5.6. It was actually a little bit less, but it has now been revised back to 5.6. We are currently sitting at 5.9. Even though we do have that volatility, it is driving down and we are seeing reasonably strong employment growth as well. The actual employment growth in 14–15 was 2.1 per cent, so reasonably solid employment growth.

Just in terms of the other point on payroll tax, I might just mention a section of the budget papers which we probably do not talk about enough — I do not think so anyway — but it is also reflected in the budget update as well, and that is the sensitivity analysis towards the back of the budget papers. What we try and do in that — and we produce it also in the budget in May — is give the reader a sense of, if there was a change in some of the economic parameters, what that would mean for the financial position of the state. There are a lot of caveats outlined in the document, because what we try and do is isolate one change and try and work out what that might mean for the finances, and of course when those changes occur you do not see them in isolation. The economy is far more complex than just changing one of the particular parameters.

So we sort of walk our way through various scenarios there, and there is a section, which we reproduce in the budget papers as well, on what higher employment actually does to payroll tax revenue. It kind of states the obvious, which is as employment rises, payroll tax receipts do rise.

What we also try and do is, given the complexities and the caveats around that analysis, a couple of case studies on how our forecasts stood up to particular shocks in the economy. One of those that I might mention is 2006–07, where there was actually quite strong economic growth that exceeded our expectations and what that meant for some of the key finances, including revenue, payroll tax and land transfer duty. What we saw in that particular scenario in 2006–07 is consistent with what I mentioned in the earlier part of my answer — that even though the economy grew more strongly than expected, we did not see a significant change in payroll tax, because of that composition question of where the jobs are created. If they are small business below that threshold, you do not get the benefit of the payroll tax increase.

I just wanted to mention that section of the budget papers because there is some quite useful information. I have just reminded the committee that we do try and work out some of those sensitivities of changes in some of those economic variables to the state's finances.

Ms SHING — Thank you for that answer. Just by way of a brief supplementary, if I may, in response to the questionnaire on employment growth, you indicated that the ABS has also indicated that some Victorian labour force statistics may have been affected by variations in the sample characteristics of the groups rotating in and out of the survey. Could one of you flesh that out a little more in terms of what that actually means?

Mr MARTINE — I can give you perhaps a high-level kind of answer, and we are happy to supplement that with a more detailed, technical answer, but essentially there is a rolling survey — I think it is nine cohorts — and each month a cohort drops out and a new cohort is added. You have this sort of rolling survey. Sometimes you get a month where particular characteristics of the cohort that drops out of the survey and the cohort that is added to the survey may lead to some strange numbers.

As I mentioned earlier, and I will just give as an example, the unemployment rate here in Victoria in September 2015 was 6.3 per cent, then in October it came in at 5.6 per cent — that is a very, very significant reduction — and then in November we jumped back up to 6.1. So we do at time see a bit of volatility. We have had discussions with the Australian Bureau of Statistics on this very point, particularly through the heads of Treasury meeting, which is chaired by the secretary of the commonwealth Treasury and has my counterparts from around the country. We have had some lengthy discussions and we have had some presentations by the head of the ABS. They themselves are doing quite a bit of work to try and come up with some more robust employment numbers, because it is very important, particularly in designing policy, to ensure that you have got the right sort of data.

My take on the employment numbers and the unemployment numbers is I tend to look at the overall trends. Some months will be down and then sure enough, if we have a large reduction, it is not surprising to see a bit of a bounce back the following month. So you generally try and look at a number of months in sequence and see if you can measure a bit of a trend, but certainly the ABS is doing quite a bit of work to try and deal with that sampling problem.

Ms SHING — Is that sort of smoothing what other jurisdictions do as well in the context of those ABS figures and variations?

Mr MARTINE — We do not do any smoothing ourselves; we take the ABS numbers. They produce a number for Victoria — they produce a number for every state — and then they produce a national number, and they are the numbers that get reported in the press. We do not do any smoothing. In terms of what that may mean for the state of Victoria and what that may mean for government policy we would take a longer term view than just one month's data, because of the volatility.

Mr T. SMITH — Secretary, I refer you to page 31 of the questionnaire. It refers to an increase of around 1.5 billion from budget to actuals for the general public service because of, inter alia, costs to the state from the finalisation of the agreement with the east–west link consortium. Could you provide the committee with a breakdown of the additional 1.5 billion in expenditure on that line item there in the questionnaire?

Mr MARTINE — Thanks for the question. So there are a number of elements to the change between the 891 and the 2.4. So in the text there are references to superannuation, but your question was very much around east–west —

Mr T. SMITH — Yes.

Mr MARTINE — so I am more than happy to talk about east–west. As the government outlined, earlier in 2015 there was an agreement struck with the consortium to settle the east–west matter. As outlined in a number of press releases through the course of April through to June, there were two elements to the costs with the consortium. There was 339 million of net costs, which effectively had already been drawn down by the consortium prior to the termination of the project, and then there was a further 81 million with respect to fees to establish the credit facility that was established by the consortium. So they are essentially the east–west costs.

I am not quite sure what the superannuation element is to that number, but we can certainly try and endeavour to provide that to the committee if that is of use.

Mr T. SMITH — It would be very helpful because from what you are saying there is 800 million give or take, probably more.

Mr MARTINE — Yes. We will endeavour to see what further info we can find on that, but certainly the settlement with the consortium on east–west is as outlined by the government in the press releases.

Mr T. SMITH — So you will come back to us with regard to what that specifically pertains to and the breakdown of it?

Mr MARTINE — Yes, we will see what further details we can find out about particularly the superannuation component, because that may be quite significant.

Dr CARLING-JENKINS — Thank you for coming this morning; I really appreciate it Mr Martine.

I am just grappling with the machinery of government changes, and I know this is something that you probably expected to ask. It is something we have all been grappling with, and I know that this has also been investigated by the Legislative Council's legal and social committee, which you have spoken to. I note that when you spoke to that committee you indicated that the machinery of government costs were not substantial and were absorbed within existing budgets. That committee, when it gave its interim report, noted some concern that:

> … the central agency approach that costs are 'absorbed' may lead to a failure by departments to identify and track costs transparently.

They recommended a clear machinery of government change reporting framework, possibly based on the Whitehall system, where expenditure is reported by each department according to accommodation, HR systems, integration, IT investment and so on. Further to this they also noted and supported the recommendation made by this committee, recommendation 39 of the PAEC report on the 2015–16 budget estimates. That recommendation states:

> The Department of Treasury and Finance update the model report to require all departments to report any costs and benefits in a year as a result of machinery of government changes in their annual reports. The updated report should include guidance so that the data in annual reports are provided on a consistent basis across departments.

So my question is simply: is the department planning to make changes to the model report as per the recommendation this committee has made, and if so, what form do you anticipate these changes taking?

Mr MARTINE — Okay. Thanks for the question. I do remember the discussion I had with the committee on machinery of government changes. As you outlined in your question, they have effectively been managed by each department and no department received additional funding to manage any particular costs, but likewise no department had their budgets reduced as a result of efficiencies that can occur through a machinery of government change. So it is important, I guess, to think about both sides of the particular issue.

We did move from nine departments to seven departments, so by definition, for example, there are two less secretaries. Some might say that is a good thing; I do not know. But there are efficiencies to be had by merging departments. So just as no-one received some extra funding, no-one had their budgets reduced.

Certainly in terms of reporting, particularly on an annual basis, they are matters that ultimately need to be decided by government and the issues that have been raised about how one goes about reporting particularly machinery of government changes. I guess all I can really say is that there has been no firm decision that I am aware of at the moment about that. I can certainly follow up on that.

Dr CARLING-JENKINS — Sure. That would be great, just to know when a firm decision might be made. Thank you.

Ms PENNICUIK — Thank you, Chair, and I do apologise for running a little bit late today; I was unavoidably detained. Mr Martine, I apologise if anyone has already asked this question, but Mr Smith referred to a variance on page 31, but on page 30 there is one at the top of the page within general public services of an initial budget of 361 million and the actual being just over 1 billion. The reason for this is stated as:

> … the different methodology used for expenses since the 2013-14 original budget … is relevant to more departments than anticipated in the 2013–14 budget papers.

I wonder if you could expand on that because it is quite a large variance of around $700 million.

Mr MARTINE — Okay. I can give you a very high-level answer. Essentially the breakdown of spending that you observe on pages 30, 31 and 32 is what we call by classification, and those classifications are driven by ABS requirements. They are not departmental outputs, so it is a different kind of way of classifying total spending in the budget. In terms of that particular one, similar to I guess the earlier question, I am just trying to think off the top of my head what might be driving that. The best thing might be trying during the course of our discussion this morning just to see if we can get the simple answer to that, but I suspect it is sort of a classification kind of change driven by the Australian Bureau of Statistics, otherwise you would see — —

Ms SKILBECK — As David said, the general purpose classification system is driven by the ABS, and its purpose is to allow comparisons across states of particular types of expenditure. Like anything that is nationally consistent, it involves a whole lot of rounding and adjustments, so it does not map exactly from the outputs the way in which Victoria describes its own expenditure to the ABS versions.

The general public services category is the most general, as described in the title, so all the other specific categories are easier to map. The general public services category becomes the rest. We had significant inconsistencies between years in these classifications, 13–14 in particular, and subsequently we have done a lot of work to ensure that we are mapping consistently year on year from our outputs to the ABS classification. It has been an issue across a number of jurisdictions. But they do vary significantly because of the particular descriptions used for each of those classifications that the ABS settles in order to enable that comparison across states. So it has limited value when it has that sort of variation, which is why we have done a lot of work to try to make sure it is vastly less going forward.

Ms PENNICUIK — Yes. When I originally looked at this I thought, 'It raises a few questions, such as what is the different methodology — what actually is that? — and the other one about 'relevant to more departments than anticipated', in what way?'. I feel like, hearing your answer, I have got more questions. I suppose it is more about whether you are able to provide after the briefing or maybe during — —

Ms SKILBECK — I think it will be after the session. It would involve us going back to the — —

Ms PENNICUIK — Some more definition, more details.

Ms SKILBECK — Basically it was an improved mapping approach, so it would be going back and seeing what the differences were in the two, between the old mapping approach and the new one.

Mr MARTINE — But we can certainly endeavour to do that.

The CHAIR — Secretary, in your earlier comments talking about debt, you mentioned the fact that Victoria is trending down from 6 per cent debt of GSP in 13–14 down to I think about 4 per cent in 18–19, and that is aided by the fact that we have got significant budget surpluses as well. So you have got the capacity to make further investments and you have got more flexibility, I suppose, in your budgetary position. You are contrasting that with the commonwealth position just as a case in point, where they have got debt trending up and they have got budget deficits. I am just wondering: how does Victoria compare to, say, the OECD average? Clearly with the OECD there are outliers there in terms of Japan and the United States in terms of their level of public sector debt, but I am just wondering how Victoria would compare in a broad and general sense to the OECD average.

Mr MARTINE — Thank you, Chair. I do not have the figures with me, but I am very confident to say we are significantly less than the OECD average — 6 per cent falling to 4.4 per cent in terms of the size of our economy is low. As I mentioned to you in my earlier answer, the commonwealth debt as a proportion of GDP is going to peak at sort of around perhaps 18 or 19 per cent. We do see some countries — you mentioned Japan, the US — the UK, most countries are actually even higher than we are nationally at sort of 18 to 19 per cent, so I am very confident to say here in Victoria we are significantly less than the OECD average. Hence we maintain that AAA credit rating from both jurisdictions — sorry, both rating agencies — and we are only one of two jurisdictions here in Australia that actually have AAA credit ratings from both Standard & Poor's and Moody's, and New South Wales is the other one. Although, just to talk up Victoria for a minute, we are the only state that has maintained both of those AAA credit ratings since the GFC, which I think is an important one as well.

The CHAIR — Thank you. The Deputy Chair.

Mr MORRIS — Thanks, Chair. This is obviously an issue of interest to both of us, because I am on the same subject. Mr Martine, in Standard & Poor's August 2015 ratings report, coming back to the amended fiscal objectives, in their commentary they said:

> We consider the state's financial objectives and targets are not particularly onerous and their qualitative nature makes measuring success challenging.

Can you give me your thoughts on that comment?

Mr MARTINE — Thank you for the question. We have been doing it for many years now: we sit down with both rating agencies a few weeks after the budget and we actually have very long sessions with them just to talk through the state's finances and make sure that they have a full understanding of the metrics, what is happening with debt, liquidity, the state of the Victorian economy et cetera, what some of the fiscal risks are. In the discussions that we have had with both Standard & Poor's and Moody's — and it is picked up in their reports — they are very positive, and have been for a number of years, about the state's finances. Your question is, I guess, picking up on an element of the fiscal parameters, which is essentially maintaining the operating surpluses that are consistent with a sustainable level of debt.

Our view in the department is that 6 per cent is very sustainable, and it has been reinforced by the commentary from the rating agencies, and their reports, both in September from S & P and in Moody's report — their last full report was February last year, but their next one is due out shortly — did reconfirm their views after the budget. So certainly in terms of sustainability our view in the department, which we conveyed to the rating agencies, is that we think maintaining the surpluses that were outlined in the budget and the budget update — all of those were above 1 billion and 6 per cent debt to GSP — are sustainable finances.

Mr MORRIS — Just going on from that, if I may, again referring to that August report, S & P said that they expected Victoria's debt burden to fall over the period to 2018, which is consistent with your comments this morning — and the published figures as well, of course — yet a couple of days before their report was published the Treasurer was reported in the *Age* as saying in Sydney that he was throwing out the political playbook and that 'it would be irresponsible not to consider increasing borrowing'. The annual financial report produced a figure of net debt in 2014–15 of $22.327 billion. The budget published less than two months before had a forecast figure of 21.2, so there was an increase there of $1.1 billion in a couple of months. Given that there is a conflict between what Standard & Poor's are saying is their understanding of the direction and the Treasurer was in Sydney saying he is going to look at borrowings, where does that leave our AAA if in fact the direction is contrary to their published understanding?

Mr MARTINE — Let me perhaps just give a bit of background and context. We are currently sitting at roughly 6 per cent of GSP, and as you indicated, the estimates outlined in the budget update in December have us falling to 4.4.

Essentially the forward estimates are based on current government policy, which is the longstanding convention, so if you extended those out you would actually still see the trajectory downwards. The Treasurer, as you indicated, did make a speech in August 2015, and he has made some public comment since about the issue of investing in infrastructure and using debt to fund infrastructure investment. What he has said, which is consistent with Standard & Poor's, and I will come back to some of their commentary, is that essentially as that debt profile falls across the forward estimates, and even beyond, governments — and I use the plural term — should be seriously looking at appropriate borrowings for what I describe as productivity-enhancing infrastructure.

So coming back to one of my earlier comments, you do not really want to be in a position to be increasing debt to fund your recurrent, which is why maintaining operating surpluses is really important. But if you are maintaining operating surpluses and you have a profile of debt, which is currently 6 per cent endorsed by two ratings agencies at AAA, and it is projected to fall, the point the Treasurer has raised is about engaging in a public discussion about, in a sense — I would kind of describe it as — filling that wedge with borrowings for productivity-enhancing infrastructure.

Standard & Poor's — I am just trying to remember the date; it was probably in the middle of 2015 — put in a submission to a commonwealth Senate inquiry on infrastructure. It should be on one of the commonwealth websites, but they actually raised that issue about states borrowing for infrastructure. It is interesting that their commentary is in a sense consistent with the comments that the Treasurer made, which is that states do need to have a look at what they describe as prudent, sustainable borrowings because of the infrastructure needs that we are all facing, not just here in Victoria, but all jurisdictions have similar problems. With the population growing at it is we really need to be investing in infrastructure. It is interesting that Standard & Poor's itself recognises that that is a significant need.

We invest a lot more at the state level on infrastructure than the commonwealth does. Most of their infrastructure contributions, as you would be aware, is really money provided to the states for funding infrastructure. So certainly at the state level Standard & Poor's, in their submission to the commonwealth Senate inquiry, were not inconsistent with the Treasurer's comments about engaging in a sensible discussion about borrowing in a sustainable way for financing what we would describe as productivity-enhancing infrastructure — in a sense, grow the state to improve the state's productivity.

Mr MORRIS — I am just trying to reconcile the two. We have got S & P saying that if the forecasts fall — that is our understanding of how it is going to happen — we are fine maintaining the AAA stable. We have got the Treasurer — with you filling in the gaps, as I understand it — basically saying, 'We've got the room there to maintain borrowings at 6 per cent'. Are you saying that is not going to affect the AAA, or is there a point where it is, given that there seems to be a fundamental mismatch between what S & P are saying is the basis of their forecast and what the Treasurer and now you are telling us?

Mr MARTINE — There are couple of points I will make. I do not think there is a mismatch. The Treasurer has not publicly stated a particular figure, but we are currently at around 6 per cent. We are forecasting it to fall to 4.4 per cent by the end of the forward estimates in the budget update, and clearly in the budget we then add another year. Based on current government policy settings, that debt profile will just continue trending downwards because effectively the estimates reflect current government decisions.

So what the Treasurer is talking about is the wedge that starts getting created by the debt profile falling over the forward estimates, engaging in a public discussion about using some of that wedge in a sustainable prudent way to borrow for long-term productivity-enhancing infrastructure, not to borrow for recurrent. The government has been quite clear publicly around the importance of maintaining budget surpluses. But if you can borrow in a way that is fiscally sustainable — and given we are sitting at about 6 per cent, we have got both rating agencies comfortable with the current state's finances; they are comfortable with the fact that we are running surpluses, the Victorian economy is strong and diverse and the diversity is a really important point for rating agencies because it helps minimise the risk — then there is headroom in terms of extended borrowings.

What I cannot do today or tomorrow or any day is say that debt at X means you lose AAA. The rating agencies' metrics are far more complex than that. They take the financials and they run some metrics, but a lot of it is qualitative as well. A lot of it comes down to what the government of the day's commitment is to fiscal sustainability and what its commitment might be to making hard decisions if, for example, there is a hit to the revenue base and they see the operating balance fall or even go into deficit. They are kind of looking for that commitment of the government of the day to take that remedial action to cut spending or raise taxes. So a lot of it is actually qualitative, not just the financial metrics.

We have over an extended period had quite positive comments from both S & P and Moody's around a lot of those qualitative factors as well. If you look at some of the metrics in some of the other jurisdictions, on the face of it it kind of looks like debt to GSP is sort of less, but when you scratch away, a lot of it has to do with that commitment, particularly around operating, or a lack of commitment to making hard decisions if revenue, for example, starts falling.

Mr D. O'BRIEN — Out of interest, do they share with you what those matrixes and metrics are?

Mr MARTINE — They do. Probably a couple of weeks after the budget we have a full day — me and my esteemed colleagues here — with S & P and then we have another full day with Moody's, and we run through in a lot of detail, starting with the state of the Victorian economy all the way through to the financials. We help them understand the metrics. They are very open with us in terms of how the metrics might look, and we have built this up over many years. We actually have a very good understanding of how they calculate their metrics. But as I indicated, their views are formed not just by the metrics. In fact the metrics are just, in a sense, one small element. A lot of it comes down to the commitment of the government of the day to stand behind strong financial management, but we certainly have a good understanding of how they do calculate the metrics.

Mr D. O'BRIEN — So they do not say, 'Twenty-five per cent of GSP would be a — —

Mr MARTINE — You will never get a rating agency to say to you that, if you go above X, you have lost AAA, but as I said, it is just one component of their overall assessment. Just as a rating agency will not provide that, I and my department are therefore very cautious about providing that as well, so we never would say to the government of the day, 'You could go to X per cent and not lose AAA'. We just cannot kind of do that.

Ms WARD — Good morning, everyone. Sorry I was not here earlier to welcome you all. I will continue on with my colleagues' conversation around the Standard & Poor's report, and I note that it says that Victoria's economy is very strong compared with its peers and that:

> Growth has been subdued over the past few years with real GSP growth of 1.7 per cent in 2014 and 1.6 per cent in 2013, but is expected to pick up to about 2.25 per cent in the year ended 30 June 2015 …

What I am interested in is that Victoria only gets around 9 per cent of commonwealth infrastructure spend, which equates to around $91 per person, and that is compared with states like New South Wales, where it is $281, and Western Australia, where it is $320 per person. With that in mind and your comments around a sensible discussion around how Victoria may increase its borrowings or what Victoria may do in getting much-needed money towards increasing our infrastructure investment, can you have a conversation with us around how increased infrastructure investment can actually help or play a role in our GSP?

Mr MARTINE — Thank you for your question. There are probably a few elements to my answer. Firstly, I might just touch on the issue of commonwealth-state relations and the metrics that you mentioned. You are quite right, at the moment Victoria's share of the infrastructure pie on average over a number of years is sitting at about 9 per cent. When you think about the fact that Victoria's population share is around 25 per cent, it is quite clear that there is an issue with respect to how the commonwealth decides to split up that funding. This has been an issue which certainly is not just under this government — it predates. It has been going for a number of years that successive governments have been having those vigorous debates with Canberra about appropriate infrastructure funding. So before we even get to the point of thinking about borrowing for infrastructure, certainly there is an important debate that we need to have, which we are having as we speak with the commonwealth with respect to how much funding they are providing the state of Victoria to help fund some of the major infrastructure projects. Certainly we are pleased that the new Prime Minister is more receptive to funding public transport projects than the former Prime Minister was, and that is an important one for us here in Victoria. But that is certainly our no. 1 priority to help fund some of our infrastructure needs.

I will make the observation that, unfortunately, given the state of the commonwealth's finances at the moment, those discussions with the commonwealth are not easy in terms of trying to get a greater contribution from them. So that is a really important part to it. Then, I guess, coming back to my earlier answer, the question that governments then need to consider is — beyond what we can get out of Canberra — what is then the best way to fund those, keeping in mind the importance of maintaining strong fiscal discipline but also ensuring that we can meet the infrastructure needs for the state, and with the state growing at 1.8 per cent and Melbourne itself just continuing to expand, there are significant infrastructure needs moving forward that we do need to address.

Hopefully, I suspect over the long term or even medium term it is potentially a combination of both some additional funding from the commonwealth — hopefully they are listening today — along with, as the Treasurer indicated late last year, having that discussion around some prudent funding through debt for some of these infrastructure needs.

Ms WARD — Thank you.

Mr D. O'BRIEN — Secretary, on page 4 of the questionnaire, at the very bottom there, it refers to a Treasurer's advance of 18.34 million for the negotiation of the lease of the port of Melbourne. I had better wait until you just get it there. I am just wondering if we could get a breakdown of what those costs were and when they were actually incurred, and whether it includes any success fee for the joint financial advisers as well.

Mr MARTINE — Thanks for the question. So that would relate to essentially the fees for the joint financial advisers that are assisting us on the port of Melbourne lease, and the two main ones there are Morgan Stanley and Flagstaff. We do provide — I think this is on our website — a list of contractors and consultants, and on the last page of that particular document we provide some information on the total that covers all of the contractors for that.

Mr D. O'BRIEN — Sorry, that is for that project?

Mr MARTINE — For the port lease.

Mr D. O'BRIEN — Yes.

Mr MARTINE — But importantly the reason I am referring to that is the footnote. We received — and I will just read out the footnote to that particular table:

> For 2014–15, a partial reporting exemption has been granted for the port of Melbourne lease transaction consultancy expenditure. Transaction consultancy expenditure will be disclosed in full on transaction completion.

What that effectively means is we provide the aggregate figure for not just Morgan Stanley, Flagstaff, Minter Ellison and PwC — there are probably about 12 to 15 companies listed there — but for commercial reasons we aggregate that up and, as the footnote indicates, once the transaction is complete we will be able to provide publicly and to the committee an exact breakdown of what has been provided to each of those. So, the Treasurer's advance reference on page 4 essentially relates to fees to contractors for the port lease.

Mr D. O'BRIEN — Would that have been expended or, again, would that be something that, until the actual lease has been finalised — —

Mr MARTINE — No, there has been spending along the way to the financial advisers and the other legal advice et cetera.

Mr D. O'BRIEN — But not fully at this stage, or — —

Mr MARTINE — No, it has not been. I mean, as the committee would be aware the lease transaction issue is continuing. So there have been costs incurred and there will be some future costs as well.

Mr D. O'BRIEN — A supplementary if I may, Chair. On a related matter, page 13 of the questionnaire again refers to actual cash outflow of 652 million for Port of Melbourne Corporation debt repayment. Was that made in the expectation that the port of Melbourne lease would be done in 15–16? Or what was the reason for that debt payment?

Mr MARTINE — Sorry, what was the page reference?

Mr D. O'BRIEN — Page 13, question 7, at the very bottom of the table.

Mr MARTINE — I think from memory that is repayment of the debt.

Mr WEBSTER — Typically when you sell these assets you sell them on a debt-free, cash-free basis, so this is preparing the corporation for sale.

Mr D. O'BRIEN — Is that cash outflow of the state paying back Port of Melbourne debt?

Mr WEBSTER — Effectively the Port of Melbourne had a loan from TCV, so it is the state putting an equity injection into the Port of Melbourne to allow them to pay TCV back.

Mr D. O'BRIEN — So effectively it will be zero debt by the time of the sale.

Mr WEBSTER — Yes, correct.

Mr D. O'BRIEN — Okay, thank you.

Mr DIMOPOULOS — Getting back to the objectives you outlined for your department at the beginning. In relation to whole-of-government procurement and the savings I imagine and the other efficiencies that could be achieved, can you give us a progress report on the department's work on that element of your objectives over the last financial year?

Mr MARTINE — Okay, thanks for the question. If you just let me get the right reference. I might just get Ms Porthouse to provide you with a bit more detail.

Ms PORTHOUSE — DTF actually manages 18 separate categories for state purchasing contracts on behalf of government. On page 25 of the annual report we had a target of 5 per cent, which we exceeded. The managed spend is 6.6 per cent in 2014–15 against a performance target of 5 per cent.

Mr DIMOPOULOS — Where is that — which page number?

Ms PORTHOUSE — It is on page 25.

Mr MARTINE — Page 25.

Ms PORTHOUSE — About halfway down, under quality. As I said, we manage these 18 separate categories. The value of the savings for 2014–15 was 50 million against a managed spend of 760 million. The savings were predominantly achieved through reduced cost and cost avoidance, so really it is around the negotiations for a major spend being able to get the best outcome for the people of Victoria by negotiating lower costs for those particular services. The sorts of categories that are managed are motor vehicles, staffing services, fuel and associated products, security services, energy — those kinds of things.

Typically a reduced cost is generally either results from a reduction in the supplier's price from a previous baseline or a change in specification for a good or service. Cost avoidance is generally either an avoidance of increasing supplier's price — that is, the removal of the CPI increase might be negotiated — or other costs for a reduction in operational or reputational risk. I suppose overall we go for 5 per cent decrease; 6.6 was achieved mainly through negotiation on, you know, total spend across government through having such a major spend.

An example — 13 million of savings or 5 per cent were achieved under the motor vehicle state purchase contract on a managed spend of 264 million.

Mr DIMOPOULOS — Are the figures based on the previous year's expenses?

Ms PORTHOUSE — Yes, and those savings were distributed across departments, and the benefits calculated by using the difference between prices paid by government and the fleet benchmark pricing in the private sector.

Mr DIMOPOULOS — So obviously the pure power of bulk purchase is probably the biggest factor, but do you feel that there is a lack of, or maybe a glass half full — is there more talent in DTF to understand pricing structures, the market, than individual departments would have?

Ms PORTHOUSE — Yes. I think that is absolutely right. What we have been able to do is consolidate that capability within our department. We will go to the market to help us with some of those categories, but in the main we have the category managers that have very specific knowledge around that particular buy. It is better than doing it disaggregated across departments where you are going to get not only the bulk buy, as you say, but also a differential in the way those things are negotiated.

Mr T. SMITH — I refer you to your 2014–15 annual report, page 9. You talk about future challenges being the sale of the port and also projected surpluses over the forward estimates of some 5.8 billion. Are those projections with regards to the surpluses predicated on the successful lease of the port?

Mr MARTINE — No. The port proceeds do not in a material way affect the operating balance. What it does is affect debt. There is a slight variance in terms of what it might do to the annual interest bill, which does flow through to the operating balance. But in terms of the profile of surpluses you observe — for example, in the budget update — they are not affected by the lease of the port. What is affected is the levels of the net debt. So the budget update — and I have discussed this, I think, with the relevant committee on the port transaction — assumes proceeds from the lease, which are embedded in the numbers, and that essentially flows through to the net debt numbers but does not affect the operating surpluses.

Ms SHING — Following on from the question from my colleague Mr Smith in relation to the port of Melbourne and that particular lease, we have indicated that surpluses are not affected by the port lease or by the timing of the port lease. Would that be a fair extension of that view that you have expressed?

Mr MARTINE — Only in a marginal way in terms of the annual interest bill —

Ms SHING — Okay. Taking you then to — —

Mr MARTINE — and just a minor impact on dividends. Obviously the longer the port is in state hands, then there are dividends that flow in, so effectively there is kind of a net effect of a slightly higher interest cost because you have not got the proceeds to pay down debt. But likewise, you get some dividends out of the entity for a slightly longer period.

Ms SHING — Offset, perhaps, by fluctuations in the market caused by timing?

Mr MARTINE — No. But in terms of the valuation, that does not flow through to the operating balance.

Ms SHING — To that end I would like to take you then to the expenses incurred in relation to progressing the lease of the port of Melbourne. We have the 18.34 additional funding by way of the Treasurer's Advance, which Mr O'Brien referred to in his earlier question, and in addition to that the actual cash outflow made in anticipation of the lease at page 13. To what extent is the work continuing to revise those figures, given the progress of the lease negotiations to date and in the context of, in particular, the submission and the details set out in what DTF provided to the select committee for the port of Melbourne?

Mr MARTINE — Thanks for the question. I might perhaps refer to the document that I referenced in an earlier answer, which is essentially the list of consultants and contractors for 2014–15, which is supplementary information to our annual report, which is up on our website. I have a page reference, but it may not be the one on the screen — my page reference is 11. In that document what it effectively states is that the total approved project fee, which is the fee for all of the advisers, is 22.871 million, and expenditure in 2014–15 is 15.929 million. That is effectively what has been spent during the course of 14–15. Obviously we will be continuing the engagement of advisers to the extent that we need to, subject to the timing of the lease transaction and what plays out through the Parliament, so we will be continuing those until there is resolution, I guess, or a government decision to do otherwise.

Ms SHING — So as it stands there will be revisions to the aggregates as they are incurred in achieving the outcome of the lease of the port of Melbourne over time?

Mr MARTINE — There is a series of matters here. There is the cost of advisers, which is the numbers I have indicated.

Ms SHING — Yes.

Mr MARTINE — We will certainly be revising those. In terms of the bigger impact — which is essentially that we booked in our estimates proceeds from the lease transaction — obviously in the lead-up to the budget in May we will need to sit down and have a close look at those in terms of timing and I guess in terms of ultimately what may or may not be agreed in Parliament in terms of what that might do to the valuation of the port. We will be, over the course of the next month or two, having a close look at those estimates. But as I indicated, apart from the minor dividend and interest issue, none of that affects the size of the operating surplus; it is really just the timing of and quantum of the pay down of debt.

Ms SHING — And to the extent that is relevant, the submission that was made to the select committee in relation to the components of the transaction as proposed?

Mr MARTINE — Sorry?

Ms SHING — The submission that was made by DTF in relation to the Port of Melbourne Select Committee as far as the regulatory impact and financial impact to the state as a consequence of the lease proceeding?

Mr MARTINE — Yes. We will need to have a close look at all of those estimates over the coming months, depending on where the matter gets to through Parliament and other processes.

Ms SHING — Great. Thank you for your answer.

Mr D. O'BRIEN — Thank you for those figures. The 22.1 million was the total allocated?

Mr MARTINE — Sorry?

Mr D. O'BRIEN — You mentioned 22.1 million allocated for the cost.

Mr MARTINE — Yes; 22.9 total approved project fee excluding GST, so that is in the document on our website, the list of contractors, and then the expenditure in 14–15 in that same document is 15.9.

Ms PENNICUIK — Just following on, I suppose, from the theme of the port of Melbourne, I understand that DTF would have been doing preparation for not only the sale or lease of the port of Melbourne but also the Westconnect toll road. What I would like to know is whether you could give some advice as to whether proceeding with the tunnel as well as the proposed rail shuttle — which is also designed to get trucks off freeways and off roads, major concerns to the communities around the port of Melbourne — whether both would be still viable to proceed at the same time, I mean not one or the other but both?

Mr MARTINE — Thanks for the question. I assume you mean the western distributor project not the Westconnect or — —

Ms PENNICUIK — The tunnel.

Mr MARTINE — Yes, the tunnel. We are involved to the extent of providing advice to government particularly around some of the commercial and financial matters. In terms of the detailed planning of the particular project, essentially a lot of that is being managed by DEDJTR, who pick up the transport responsibilities. Our involvement is certainly advising government on the commercial aspects of that. As the government has indicated in December, they have decided to move to what we call stage 4, which is negotiations with Transurban, and those discussions are obviously continuing, and we have got some involvement in that particular aspect of the project. I might ask Mr Webster to add a few comments on that.

Mr WEBSTER — In terms of your actual question, there is no conflict in terms going ahead with one project does not make the other one technically unfeasible. Whether you wish to have two projects happening in parallel, I think you would need to ask the question to DEDJTR, but there is no technical issue that one precludes the other.

Ms PENNICUIK — So no legal, design, economic impediments to proceeding with both projects?

Mr WEBSTER — Not as far as I am aware.

Mr MARTINE — I would not have thought so.

Dr CARLING-JENKINS — I think I might go on a different track and give you a bit of a rest from port of Melbourne questions.

Ms SHING — We were just getting started.

Dr CARLING-JENKINS — Unless anyone else wants to jump in with that.

Ms SHING — We have got all week.

Dr CARLING-JENKINS — Yes, we do. We are here all week.

I would like to — as I said, a completely different subject — just explore the impact of swapping asset and output expenditure on the budget surplus. Each year it is my understanding that costs are shifted by departments between operating expenditure and capital expenditure. I apologise if this is a bit simplistic, but broadly speaking it is my understanding that capital expenditure creates assets while operating expenditure does not, and operating expenses affect the surplus while capital expenditure does not.

But departments explain the number of variances as being due to the reclassification between these two costs that we refer to as a section 30 adjustment. These changes do not only affect output performance measures but can affect departmental and state expenditure and following this obviously the surplus as it shifts expenditure from above the line to below the line. I am just wondering if you can speak to this issue around why costs are moved around under these section 30 transfers, and what is considered when making these transfers?

Mr MARTINE — That is a very interesting question you have asked. Your brief summary is correct, but they are not changes that departments can just unilaterally make. We are all governed by the accounting standards, in which there are quite clear definitions around what is an expense and what is capital but essentially, as you have described, an output affects the budget surplus; an asset does not affect the budget surplus but affects net debt. But likewise an output also affects net debt. So anything on the output and assets side feeds through to the net debt numbers I mentioned, but only outputs affect the size of the budget surplus.

Without knowing specifics, there could be a whole range of reasons why something has moved from output to asset or from asset to output, but all of those changes are governed by the accounting standards. At the end of the year that particular classification change would be looked at by the Auditor-General in their sign-off of that particular department's accounts. So if there were some issue around misclassification between output and assets, then it would be picked up in that context. So they are not unilateral changes that either departments or we make, but it could be for a whole range of different reasons. It could be simply that there might be a particular government decision to implement something in a certain way and then as it has been progressed and the implementation has been developed the decision might be made that there is a slightly different way of rolling out that particular program, which might affect the original split between asset and outputs. So it can be a whole range of reasons on that.

The CHAIR — We might use this pause as an opportunity to have a brief break.

Secretary, I have got a question for you in relation to inclusion programs. I note that the National Australia Bank has had a very successful partnership with Jesuit Social Services in relation to the African-Australian Inclusion Program, which basically looks at getting very bright young people from the Horn of Africa, who are young, who are educated, and they get a rotation through the NAB. It has been a quite successful program; I think their retention rate is around about 85 per cent. It is particularly important because a lot of these people might live on public housing estates and it is an opportunity for them to get access into practical work experience, get off welfare, get into work. So I was just wondering whether the Department of Treasury and Finance has any inclusion programs or has thought or considered looking at having inclusion programs for specific disadvantaged cohorts?

Mr MARTINE — Thank you for your question. I might just make a couple of brief comments on that particular point. We have been doing quite a bit of work over the last 12 months within the department about the question of diversity, and that is not just a gender balance issue but in terms of diversity more generally. We are in the process of putting together a diversity action plan, which is going to be considered by the department's executive board I think within the next month.

Ms PORTHOUSE — Next month.

Mr MARTINE — It is something that is quite important to us. It is probably fair to say that we are not too different to a number of treasuries around the country, which is not particularly diverse in our background. Our gender balance — just some metrics — in aggregate does not look too bad. It is 51:48, but of course as you look at particularly the more senior levels, we do have some work to do, and we are actively looking to do that.

One initiative that we did implement — I think it was early last year, so it would have been for 2015 — is that we consciously made a decision to actively recruit some graduates who identified as coming from an Indigenous background. We have our normal graduate program and we take 12 to 15 graduates each year, but to supplement that we specifically targeted in a separate program some graduates that had specifically identified as coming from an Indigenous background. I am pleased to report to the committee that we actually picked up three graduates to come to the department, which was a fantastic outcome, because up to that point there was only one DTF employee who had identified themselves as coming from an Indigenous background, so that is 1 out of nearly 500 people. So it was something that as a board we were conscious to try and address. I think we made the three offers and they were all accepted. It is a really good way of just helping to create a bit more of a diverse background. So they are kind of some of the initiatives that we are looking to implement in the department.

The CHAIR — Thank you, Secretary.

Mr MARTINE — Chair, can I just briefly try and provide an answer to one of the earlier questions?

The CHAIR — Of course.

Mr MARTINE — I cannot quite remember who specifically asked the question, but it was the question relating to page 31, 'General public services'. It was a question in relation to the movement from the initial budget estimate for 2014 from 891 to the actual of 2428.

Ms SHING — Mr Smith, I believe.

Mr T. SMITH — Yes.

Mr MARTINE — So the answer to the question is that embedded in the 2.4 is about 1.9 relating to superannuation. You might see in the explanation there is a reference to a movement from 'other purposes output to the general public services output'. If you turn the page to page 32, you will see that there is a reduction under 'Other purposes'. So effectively there was a change in classification for the superannuation component and embedded in that 2.4 is the revised 1.9. That change in superannuation classification came about from a change to accounting standard AASB 119, which changed the way in which defined benefit superannuation expenses are presented in a comprehensive operating statement. That was first reflected in the 2013–14 financial report, which would have been released towards the end of 2014. So effectively a large proportion of that change — we have spoken, I think, about the east–west element — relates to the movement between the 'General public services' line and the 'Other purposes' line on page 32.

Mr T. SMITH — Thank you.

Mr MORRIS — Just on the timing on that, was AASB 119 in operation after the introduction of the budget but before the production of the AFR for 13–14?

Mr MARTINE — I think that is the case. It was first reflected in the AFR in 13–14, so that would have been released in October 2014. The initial budget estimate for 14–15 would have been released in May of 2014, so it would have been kind of prepared several months leading up to that.

Mr MORRIS — So the explanation is that it was prior to — —

Mr MARTINE — Yes. So the initial budget estimate would have been — —

Mr MORRIS — the operation of 119?

Mr MARTINE — Yes.

Mr MORRIS — It is just that I remember the events; I just do not remember the chronology.

The CHAIR — That is what they all say.

Mr MORRIS — On an entirely different matter, the DTF annual report at page 18 relates to the financial reporting output. One of the performance measures is the number of Auditor-General qualifications relating to material weaknesses in financial reporting systems. The target is zero and the reported actual is zero. When we go to the AFR for 14–15, net result from transactions, net operating balance, surplus — $1.214 billion. Then of course we have the Auditor-General's report, which qualifies the accounts, including that failure to recognise a liability and an expense means that expenses from transactions are understated for the state of Victoria and the general government sector. I am not quoting exactly but just picking out the highlights. The net result from transactions are overstated for the state of Victoria and the general government sector by $1.5 billion. The comprehensive results are also overstated by the same amount. Other provisions and total liabilities are both understated for the state of Victoria and the Victorian general government sector by 1.5 billion, and the accumulated surplus and net assets for the state of Victoria and the Victorian general government sector are overstated by $1.5 billion.

Clearly there is a disagreement between the government and the Auditor-General on this issue, but presumably, having said in the department's annual report that there were no qualifications, you must have formed an opinion on the validity of the Auditor-General's claims. Would you care to comment?

Mr MARTINE — There are a couple of elements to your question. Essentially the qualification you refer to does actually manifest itself in the DTF accounts. The DTF accounts are qualified. The whole-of-government accounts are essentially the sum of all of the departments' accounts. The Auditor-General, similar to language you have conveyed, qualified the departments' accounts. I sign off the departments' accounts, along with my CFO and my independent audit committee, and our view is that a liability and expense was not required to be recorded in 14–15.

Essentially — and I am happy to run through the explanation for that — there was an agreement between the former government here in Victoria and the commonwealth in relation to funding for the east–west project. That was dated 28 June 2014, and that had a schedule of payments to the state of Victoria. Part of that schedule of payments had the 1.5 billion that the Auditor-General is talking about, and that was received into the state's accounts in 13–14. It was actually in June 2014 that the 1.5 came in.

As a result of the change of government, the new government made a clear decision not to proceed with the project, so the other funding in the MOU, which was another 1.5 which was forward looking, was immediately off the table, so the issue we are obviously talking about is the 1.5 that the state physically received. Effectively the new government made a policy decision to not proceed with the project, and in a sense the agreement between the state of Victoria and the commonwealth then became a void agreement.

These agreements between jurisdictions are not legally enforceable, and from time to time parties to those agreements do step away. I guess a good example of the commonwealth doing something similar relates to their decision in May of 2014 to walk away from the health agreement and the education agreement. They made that decision unilaterally in 2014, in a sense effectively tearing up those particular agreements. The then government — the former government — and the new government and DTF itself have been advocating ever since that this is unsustainable, but the fact is that the commonwealth walked away from that agreement, and at that particular point in time in a sense there was no agreement. As much as we think we are being hard done by, there is no agreement, so we take out the revenue that would have flowed from that particular agreement.

With this particular issue on the east–west project, the Victorian government made a decision not to proceed with the project and at that point in time there was no longer an agreement with the commonwealth. To help form our view we obtained some independent legal and accounting advice on the matter, and I, my CFO and my external audit committee then satisfied ourselves that, because in a sense there is no longer an agreement with the commonwealth, there is no requirement to book an expense and a liability to return the funds. The commonwealth may take different action. They may seek to recover that money in a different way. They have made no decision on that. But the view we took in finalising our accounts was that in the absence of an actual agreement, which is now no longer valid because the Victorian government has walked away, there is therefore no liability and expense that needs to be recorded.

Obviously the acting Auditor-General had a different view — that happens from time to time — but the qualification is certainly in the DTF accounts and, because the annual financial report is in a sense the sum of all of the departments' accounts, that qualification then translates up to the whole-of-government accounts. The explanation provided, I think, in the Treasurer's statement, from memory, in the annual financial report is very similar to the statement that I made in my department's accounts. The rationale is essentially the same.

Mr MORRIS — I think there are a couple of points there. The first point I made is that the DTF annual report records that there were no qualifications.

Mr MARTINE — If I can look at the right page again — —

Mr MORRIS — Page 18.

Mr MARTINE — If you look at the wording of the performance measure, it talks about weaknesses in systems and processes. We would take the view that on this particular matter there is no weakness in a system or process. There is clearly a different view and interpretation of accounting standards between us and the acting Auditor-General — there is no debate about that. The acting Auditor-General took a view that an expense and a liability should be recorded. The view we took in the department is that it is not required, because there is in effect no agreement with the commonwealth. We are not trying to hide the fact here that there is not a qualification. It is very clear in the department's annual report that our accounts were qualified by the Auditor-General and hence flowed up to the AFR. It is essentially a qualification relating to a different opinion and interpretation of accounting standards.

Mr MORRIS — I think, with respect, that is probably a very good example of the problems that many parliamentarians have with our performance measures — that there has been a qualification, but this is because of the get-out clauses written into it. I am not having a personal shot, but there is simply enough latitude in there, shall we say, to record it as 'no qualification' when in fact a qualification has occurred.

Mr MARTINE — It is certainly not the intent to try and avoid the fact that the accounts were qualified, because it is very transparent and clear in the DTF — —

Ms SHING — Absolutely, in plain sight.

Mr MORRIS — I guess the other point, though — and I certainly agree with you that any new government has the absolute right to not proceed with an agreement — is that whatever the commonwealth may have done in 2014 the state has not paid money to the commonwealth. The commonwealth simply said, 'From now on as a newly elected government we are not going to continue commitments that are alleged to have been made over the forward estimates period by our predecessors'. I do not argue about their right to do that, and I do not argue about the right of the current state government to not proceed with the agreement, but the Auditor-General's report also talks about — and obviously I am not a practising accountant and I am not totally familiar with all the AASBs — in the paragraph above the points I was quoting earlier:

> The state has not recorded a liability in the consolidated balance sheet or an expense in the consolidated comprehensive operating statement to account for the requirement to return the funds.

You are saying there is no requirement to return the funds. He says:

> This is a departure from AASB 1004 contributions, which require that a liability and an expense be recognised because clearly the conditions of the grant will not be met and the funds are required to be returned, and consequently a departure from AASB 137 provisions contingent liabilities and contingent assets.

Can we have a little more detail about how this decision is not a departure from AASB 1004?

Mr MARTINE — I think the important point comes back to my comment around the status of the agreement, and the advice we received, which I am very comfortable with, is that at the point that the new government terminated the project — in a sense walked away from the agreement — there were no conditions to be met under the agreement because the agreement did not exist, and if an agreement does not exist, you cannot have a requirement for a liability and expense. That is in essence the legal and accounting advice, and that is really the debate.

Obviously the acting Auditor-General took a different view, but essentially it comes down to a view as to whether when an agreement is torn up you still believe that that agreement exists, and I guess, similar to my comparator with the health and education agreements, yes, you are right that jurisdictions can walk away and you are correct that that is not money that we have actually received — it was forward-looking money — but at that point in time, back in 2014, we immediately took out those future projections. We did not take a view that the commonwealth was still required under that agreement to provide that funding to the state, and therefore we do not pretend we are going to receive it in the forward estimates, because there is no longer now an agreement between the commonwealth and the state that covers that bit of funding for health and education.

So it all comes down to the question of whether an agreement existed as of 30 June 2015, and our view is based on the legal and accounting advice, as I said that I am very comfortable with, that at that point in time there was no agreement. Therefore, if there was no agreement, there was no obligation or requirements that had not been met. Obviously the acting Auditor-General took a different view — that as of 30 June in his view there was still an agreement — and that is really in a sense the whole debate. That is what it comes down to.

Mr MORRIS — So essentially what you are saying is that a government can enter into an agreement with another government to do certain things, receive funding for that and, then having received the funding for it, say, 'Look, we've decided not to proceed, but we'll keep the funds'.

Mr MARTINE — These agreements between jurisdictions are not legally enforceable, so technically that can happen. The jurisdiction that has provided that funding can obviously take different action, and the commonwealth may take action to recover the 1.5 in a different way, but the current government here in Victoria has made a clear statement that it is not returning the funds — that it does not have an obligation to return those funds, because essentially as of 30 June when the accounts were finalised there was no valid agreement that existed at that point between the commonwealth and the state of Victoria. That really comes down to the whole debate around then the interpretation of the accounting standards.

Mr D. O'BRIEN — If there was no valid agreement, you would not have had the 1.5 billion, so the natural conclusion to that may be that you need to give it back.

Mr MARTINE — At the point in time that the state received the 1.5 billion, which was June 2014, there was an agreement in place that both jurisdictions still were honouring. Then there was a change of government, and the new government made a decision to terminate the project, and at that point the agreement was no longer valid, and when we hit 30 June to finalise the accounts, at that point in time, if there was no agreement then between the commonwealth and the state that governed the payment of the 1.5 and the requirements and the conditions that had to be met, then our view is that an expense and a liability were therefore not required to be booked in the accounts. The 1.5 that we are yet to receive under that agreement — clearly we have taken that out of the budget forward estimates, because if there is no agreement, that is not going to flow from the commonwealth —

Mr MORRIS — I would hope so!

Mr MARTINE — so that has gone, and that was very similar to what was undertaken just after May 2014 when the commonwealth effectively tore up the health and education agreements. That future funding was then removed out of the estimates. There was no point pretending — —

Ms SHING — It was the referendum; the election was the referendum on the east–west link.

The CHAIR — Order!

Mr MORRIS — The difference is that no money had been paid and no moral obligation incurred.

Ms SHING — Are you asking for an opinion, Deputy Chair?

Mr MORRIS — The morals rest entirely with the government, not the witnesses this morning, but it is a matter of the moral position — and the moral position stinks, frankly.

Mr D. O'BRIEN — I would love to borrow money from Treasury, because then I would say, 'Oh, sorry, I've decided not to go ahead with that but I'm keeping the money'!

Ms SHING — Only if you had written a side letter that actually gave you all of the entitlements — —

The CHAIR — Order! Mr O'Brien, we can come back to you if you have another question about this.

Ms WARD — I want to ask a question about private-public partnerships, but before I do I just want to get something clear in my head. Like my colleague, I am not an accountant either; more of a community worker, I would say. I am interested in this idea around infrastructure money and the money that comes to the state. With the money that Mr Morris is referring to, does that fall into the 9 per cent of funding that we get from the commonwealth?

Mr MARTINE — That is correct, and there is a very good point to be made there. If the Victorian government returns that 1.5 billion or the commonwealth took that 1.5 billion back from Victoria in a different way, then that 9 per cent actually drops quite a bit. I think from memory it is something like 4.5 per cent, something like that.

Ms WARD — So we would actually end up with less than $50 per Victorian.

Mr MARTINE — So it would be, I am not quite sure the metrics per capita but it would continue to fall, so it does have quite a material effect on our share of that pot, remembering my earlier comment that per capita we are about 25 per cent, so generally you would kind of expect Victoria to receive in that order of magnitude. Particularly with very strong population growth at 1.8 per cent, there is actually a valid argument that we should have with the commonwealth, which we have raised with them, that we should actually be receiving more than 25 per cent given the strong population growth. At the moment we are roughly 9 and if we lost the 1.5 billion, it does drop to something like 4.5 per cent roughly.

Ms WARD — Which is quite paltry, really. So going to private-public partnerships, we know about estimates for public-private partnerships that have been under construction, but if I can turn your mind to 2014–15 and how much was spent in completed public-private partnership infrastructure investment projects, was the amount higher or lower than the budget estimates of 1.854 million, and what factors resulted in any difference?

Mr MARTINE — Sorry, are you referring to a particular answer in our response, or — —

Ms WARD — I do not have a reference to your response, sorry.

Mr MARTINE — We might just need to find — —

Ms WARD — Just interested. So we know the figures of the starting point but I do not think we know the end point of what happens at the end of PPPs.

Mr MARTINE — There is note 34.

Mr WEBSTER — Excuse me, I am not fully understanding the question.

Ms WARD — That is okay.

Mr WEBSTER — Note 34 —

Mr MARTINE — And this is of the annual financial report.

Ms WARD — Okay, yes.

Mr WEBSTER — outlines the commitments in present value terms of effectively the principal amount of the availability payments going forward, so what is in the forward estimates for PPP projects which are during procurement is an estimate of what the finance lease liability will be at financial close. What happens while it is underway is the state is taking interest rate risk, so the interest rate is only fixed on the date that the contract is signed or pretty soon thereafter and the actual interest rate will determine what the actual lease liability, if it is booked, is. Once the lease liability is booked, when the contract is signed, it then does not change or it changes for an accounting amortisations. Does that answer the question?

Ms WARD — No, I go back to the earlier comment: I am not an accountant! The crux of it is that you estimate what PPPs will cost.

Mr WEBSTER — Correct.

Ms WARD — What we do not know is, at the very end of the project, what it has actually cost. Is there a way of you explaining that to us or of us getting that information?

Mr WEBSTER — It does come through two lines, so effectively the finance lease liability which is booked at the start of the project is what is called the net present value of the future payments, so it is effectively saying your home loan is 100. You may pay more than 100 in principal and interest through time over the 20 years but the 100 is, if you paid it off now, what the value of the loan is. So in terms of totting up the payments through time, you have to look at the principal payments, which come through reductions in the commitment line in note 34. There are two other lines, which is the interest on the lease liability, which is the interest component on that, and then there is separately in another note the other commitments note that I believe details what is paid to PPP companies for the operational elements of the PPP, so the total payments come through three different lines in the annual financial report.

Ms WARD — Okay. So if I can get you to go to budget paper 4, page 15. Bear with me because I do not have a copy, I am sorry. There is a figure of $1.8545 million that talks about initial expenditure, I think, but it is not clear what happens next.

Mr WEBSTER — So this is budget paper 4?

Ms WARD — Yes, budget paper 4, page 15.

Mr WEBSTER — Note 15?

Mr D. O'BRIEN — No, page 15.

Mr MARTINE — We are just trying to track down the budget paper. Page 15?

Mr WEBSTER — Yes. This is an adjustment we do to actually show the gross amount of government infrastructure investments, so the 1.854 is effectively the actual construction costs of PPP assets. What we would previously be concerned about is the 5.6 figure, which had previously been reported as the government infrastructure headline spend, which effectively excluded PPPs because they were accounted for differently. We thought that was misleading so to put out a number which included all of the infrastructure spend, the government infrastructure investment adds to the traditional spend the actual construction costs or the estimated construction costs of PPP, to better reflect what actual construction costs are that are spent on infrastructure in the state.

Ms PENNICUIK — Chair, given we are having a little conversation, I was wondering if I do have a quick follow-up to that on the same subject? It is not a substantive question — —

The CHAIR — If you could be succinct, Ms Pennicuik, that would be appreciated.

Ms PENNICUIK — I will be very succinct. If I could refer you to question 6 on page 12 of the questionnaire. I am interested in this area as well because PPPs are notoriously opaque to the community. There is a table there asking for the amount including the following line items, and the amount is nil to all of those line items. It is just a follow-up to that. Is it that in terms of the PPP none of these things such as interest expenses or operating expenses et cetera down that table apply? Can you explain that?

Mr WEBSTER — There are no PPPs in the DTF accounts; they are all in other departments.

Mr MARTINE — Most of them would be in transport.

Mr WEBSTER — Transport, health.

Mr MARTINE — Yes. So generally their answer to question 6 should be populated with some quite large numbers.

Ms PENNICUIK — From other departments.

Mr MARTINE — But in terms of the DTF's own accounts, we do not have any PPPs.

Ms PENNICUIK — Yes. Thank you. You can see how it was just a follow-up.

The CHAIR — Yes, that is fine, Ms Pennicuik.

Mr D. O'BRIEN — Likewise just a clarification, if I may, on the 1.5 we were talking about a moment ago. I believe you said, Secretary, the other 1.5 that had not been received as yet was excluded from the forward estimates.

Mr MARTINE — Yes.

Mr D. O'BRIEN — When was that done? Was it in the 15–16 budget or in an update at some stage?

Mr MARTINE — The government changed in late November. I would need to double check. I think it would have been taken out in the budget update released a month after the election, in December 2014.

Mr D. O'BRIEN — If you could just confirm that for us at some stage, that would be great.

Mr MARTINE — Yes. It was effectively 1.5 billion spread over five years up to 2018–19.

Mr D. O'BRIEN — Sorry, Chair, my substantive question is on a different issue altogether. Enterprise bargaining agreement increases — page 44 of the survey response shows a 1.3 per cent increase from 13–14 to 14–15. But on page 46 — sorry, I am going to jump around a little bit here — the initial estimate for EBA increases is 1.9 per cent but the actual was 4.6 per cent — a 2.7 per cent variance. Then if we go to page 49, that highlights that is about a $391 million difference. I am a bit confused about whether that is a result of a change of government. The explanation refers to unexpected demand growth in hospital and health services, but this is actually EBA increases, so it is not employee expenses per se. I am just wondering if you could give a clear explanation of that increase. Was it a result of the change of government? Was it a change of policy?

Ms SKILBECK — No, neither.

Mr MARTINE — No. I am just trying to interpret our response. This question has come up before in a slightly different way in terms of growth in employee expenses for 14–15. We can come back to you on the actual specifics in the response, but I guess the important point I would not mind making is — I am referring to the year 14–15 — the data I have with me is the employee expenses in the pre-election update were forecast to grow in 14–15 by 2.5 per cent. Employee expenses are driven by quantity and price, so an EBA outcome may affect the price. Quantity can be affected by a whole range of factors.

The government in its very first budget did talk about providing additional funding, particularly in areas of health and some of the social service areas — in fact providing additional funding to, in a sense, increase quantity. So that affected the growth in total employee expenses figure in the 15–16 budget, but also the actual in 14–15. I do not think I have the actual figure there.

I would need to go back, though, and probably take on notice the specifics in terms of the EBA metrics there, because at the time of the government's first budget there were, from memory, very few — if any — —

Ms SKILBECK — No major EBAs.

Mr MARTINE — No major EBAs had been concluded by the new government.

Mr D. O'BRIEN — I guess that is why I am asking.

Mr MARTINE — So there was no kind of price impact flowing through. There was certainly a quantity impact discussed and disclosed in the government's first budget. The price impact was minimal. As I said, there were, I think from memory, a couple of very minor EBAs that had been concluded prior to the government's first budget.

Ms SKILBECK — More specifically, there were no new major EBAs. So the price impacts will generally come from the old EBAs — the existing EBAs — and the increases embedded in those. For different workforces in the service things like progression rates — the rate at which people increase and move into a higher wage bracket — increases price, and the composition of the workforce and the make-up, as opposed to the pure quantity of employees in any area. So they are the general sources in a year. For the 14–15 year there were no major EBAs settled so there was no change in the settings of price for any particular large workforce.

Mr D. O'BRIEN — Yes, so I would be pleased if you could give me a clearer answer because this does — it is enterprise bargaining agreement increases — so it relates to the price. The explanation is largely about the number, which is a different thing.

Mr MARTINE — I understand your question.

Ms SKILBECK — You are quite right; the terminology is not clear.

Mr D. O'BRIEN — And just to clarify, is the current government's policy also 2.5 plus productivity, plus 0.5?

Mr MARTINE — Yes, 0.5.

Ms SKILBECK — The terminology is service delivery improvements for an additional 0.5.

Mr D. O'BRIEN — Okay, thank you.

Mr DIMOPOULOS — Thank you. In the budget update on page 9 you talk about, and I quote:

> Government infrastructure investment remains high. Estimated government infrastructure investment over the budget and forward estimates averages $5.3 billion a year compared with the historical average of $4.9 billion a year over the decade to 2014–15.

I just want to see if you could unpack that for us a bit more. What is inherent in that figure? And also, in light of the positive remarks made by the Prime Minister and Infrastructure Australia in relation to public transport infrastructure spending, how does that figure relate in that context?

Mr MARTINE — I am referring to page 9 of the most recent budget update, which was released in December 2015. If you look on the previous page, page 8, it gives a bit of an indication of government infrastructure investment looking forward for the next four years. We have 5.0 billion in 15–16, 6.3 billion in 16–17, 4.5 and then 5.2. These estimates reflect government decisions at the time that they are put together. That is the general approach we obviously take on estimates. Included in that would be all of the government's announcements on infrastructure spends that they have made clear decisions to proceed with.

For example, grade separation removals and a number of other election commitments would be embedded in that number. Mr Webster has already in an earlier answer talked a bit about the adjustments we make for PPPs to kind of better reflect the total quantum of that investment and, importantly, to try to get a sense of the impact that that may have on the Victorian economy, whereas if we exclude the PPPs, it can give a slightly misleading number because the more PPPs you do, and if you do not include them, it kinds of look like the government of the day is not really investing much in infrastructure. It is just a different way of financing the particular project.

Those numbers reflect government decisions as of publication with all of their major projects that have been agreed and announced, particularly around election commitments. Obviously, moving forward, those numbers will then be updated for the budget where, if the government makes further decisions on infrastructure spending, they will then get reflected in those numbers moving forward. As outlined in your question and on page 6, at the moment it averages slightly above the historical average of 2014.

Coming back to one of my very early answers with respect to the level of infrastructure investment and what it should be — it is always a very hard thing to answer — but I will make the observation that with population growing at 1.8 per cent, with the city of Melbourne expanding rapidly and with some real infrastructure needs in regional Victoria, future governments are going to have to have a very serious look at the quantum of infrastructure spending. Given the long lead times — because with a lot of these projects you start now with planning, particularly the big ones, and it can take up to 10 years before the benefits are actually there — you do need to have that very forward-looking agenda, particularly on infrastructure.

Mr DIMOPOULOS — So yes, the government's commitments are reflected in the budget, in the forward estimates, and you have talked about grade separation. Is, for example, the rolling stock order in those figures?

Mr MARTINE — All decisions — —

Mr DIMOPOULOS — Just before you go on, so I do not interrupt you again, I imagine that in public transport infrastructure spending state governments are sovereign to an extent; however, they have got to read the signals from Canberra in terms of the bidding for federal funds at some point. How do you see that relationship with the change of Prime Minister and the more positive remarks in relation to public transport?

Mr MARTINE — Certainly, as I mentioned earlier, all of our estimates include all government decisions at the time of publication. Most of those decisions, particularly for a budget update, would have already been announced publicly by the government of the day. It is reasonably rare for a government to use a budget update to actually announce a new project. Sometimes it may happen in an actual budget, but generally they are announced beforehand. So everything included here would reflect both election commitments that the government is implementing and other decisions it would have made in its first 12 months.

Coming to the point of our relationship with Canberra, obviously, as I have outlined in some my earlier answers, it is a very important relationship, particularly on infrastructure, because at 9 per cent of the size of the pot it is very low compared to our population. As I have mentioned, we are certainly encouraged by the more positive commentary out of the current Prime Minister, particularly around public transport, because some of the infrastructure needs that we are currently trying to address are on public transport. It kind of always, I guess, puzzled us a bit here in Victoria the distinction that was being drawn between funding for roads versus funding for rail in particular, because the whole infrastructure program needs to be complementary. You cannot just have roads versus rail; you actually need to spend in both areas. So we are continuing that advocacy role. We meet quite regularly as treasuries, and the Treasurer is also, as you would expect, conveying the strong message from Victoria about the need to ensure that we get our fair share out of Canberra for total infrastructure funding.

Mr T. SMITH — Secretary, I refer you to page 9 of your 2014–15 annual report, and you have got a significant project this year in supporting a review into housing affordability. I was wondering if you could advise us who is conducting the review in the government, what the terms of reference are and when it will conclude?

Mr MARTINE — Thanks for your questions. I am assuming you are referring to my report of operations in the annual report.

Mr T. SMITH — Yes.

Mr MARTINE — I think the Treasurer has made a few statements about housing and housing affordability. In the department we are supporting government in looking at those issues on housing affordability, what can be done with respect to affordability. It is a real issue, I guess not just here in Victoria but it is certainly a national issue. But here in Victoria, with the population growth, the expansion of the city of Melbourne, it is an issue which the government is committed to and has made some announcements to have a look at. The reference there is effectively reflecting our role in supporting government by providing advice to the government through the Treasurer on issues around housing affordability. The government has not made, as of today, any particular decisions or announcements, so I cannot really pre-empt any of that.

Mr T. SMITH — You cannot tell me who is running the review?

Mr MARTINE — We are providing, I guess, sort of a support function to government.

Mr T. SMITH — You are essentially the secretariat. Is there an outsider who is running the review or is it within the department or — —

Mr MARTINE — I will probably have to — actually I hate to do this — just take it on notice in terms of what further information and details that I can provide, but certainly the reference here reflects the support that we provide government on issues.

Mr T. SMITH — So you will provide that in writing to the committee?

Mr MARTINE — Sorry?

Ms SHING — He just indicated that that would be the case.

Mr MARTINE — Yes.

Mr T. SMITH — Okay, so you cannot tell me who is leading this thing. Can you tell me: is it assessing the continuation of first home owner grants, stamp duty concessions, the first homebuyers? Are they on the table as part of this review?

Mr MARTINE — Probably the best way to explain what we are looking at is: I guess, like any market, demand and supply factors affect any market, so demand and supply affects price, which is central, I guess, to housing affordability. In looking at the issues and in advising government we are essentially looking at, in a sense, both sides of the issue. So what can one do to increase supply with both land and I guess affordable housing? Like any market, the more supply you provide, that puts some downward pressure on price.

Likewise, on the demand side what can be done with respect to demand? In a sense, some of the tightening that has come through lending institutions, particularly to investors, has actually helped to reduce some of that demand pressure. The banks are becoming a bit more strict on the loans that they are providing investors, so we are actually seeing a bit of a flattening of the investor market. That helps put some downward pressure on pricing, so in a sense we are kind of looking at the full suite. But coming back to my earlier answer — —

Mr T. SMITH — So it is. They are all on the table.

Mr MARTINE — The government has not made any kind of announcements in terms of where it wants to head on anything.

Mr T. SMITH — Just to clarify: in terms of the terms of reference, everything is on the table.

Mr MARTINE — That is the bit I will need to take on notice in terms of the articulation of what is on the table or not. I am always very conscious of making public statements around ruling things in or ruling things out, so all I can say as the head of the Treasury and as a bureaucrat is that we are providing advice to the government on the important issue of housing affordability. It will be a comprehensive, fulsome advice, and then the government will make some decisions and no doubt some announcements on what it is looking to do.

Mr T. SMITH — If you could come back in writing on these facts, that would be greatly appreciated. Just one further question: are you in discussions with the department of planning with regards to their role in terms of housing affordability?

Mr MARTINE — Well certainly planning — and that is a good point, actually. Planning is an important issue with respect to the whole issue of supply-side issues on housing affordability, so how the planning system works, the speed with which decisions can be made. There are a whole range of things.

Mr T. SMITH — Height restrictions in the central city, perhaps.

Mr MARTINE — We have been talking across all of government on what are some of the issues that just help, as I said, that whole demand-supply equation. I am more than happy to take on notice and come back to you with what we can.

Mr T. SMITH — Greatly appreciated.

Ms SHING — I would be interested in moving to the shared service provider role that DTF has begun to acquit across government agencies that it supports, and I am interested in hearing from you and from all witnesses, in fact, where that is relevant and necessary for the purposes of your responses to the questionnaire as a whole.

Mr MARTINE — I might ask Ms Porthouse just to run through some of the work that the shared services provider has been providing, and I think in particular there are some good metrics we can talk about in terms of accommodation.

Ms SHING — The metrics is exactly what I would then like to go into, so feel free to just go from there.

Ms PORTHOUSE — So DTF, through the DTF shared service provider — one of the key metrics is reducing our footprint — reduced vacant government accommodation space in the CBD and fringe areas by 3280 square metres. That equated to a total saving in 14–15 of $1.2 million. Also, 1.5 per cent of managed government office accommodation was vacant, and that is compared with 2.2 per cent the year before and compared with the market averages across the CBD of 9.1 per cent — so doing quite well there.

What we continue to do, and so it gets harder and harder to meet and exceed these targets, is to work closely with government agencies around how they can best use their footprint and how they can move their people around so that they are getting the best productivity outcome but at the same time reducing the space that they are utilising. We continue to do that; that is part of our strategic advice across government around them working on their strategic accommodation plans.

Also we have reduced workspace ratios; that is the other factor that we use. We have gone from 15.2 per cent in 2013 — this is space per person — to 14.3 per cent, so we have exceeded that particular target by 4.2 per cent. They are the ratios. We are doing quite well on them; we can do better. It is really just a continuing conversation around how best we can utilise the space that we have, particularly in the CBD because that is obviously the most expensive space that we occupy. A number of other key projects that we are working with departments on are DJR, for example, on their Community Correctional Services Accommodation Expansion Program and that kind of stuff. But basically we are doing okay.

Ms SHING — Beyond the CBD, in terms of the decentralised provision of government services in and around Melbourne in suburban and peri-urban areas?

Ms PORTHOUSE — It is pretty static. There is not a lot of movement in terms of the space that we occupy. What we do do is on behalf of government obviously negotiate as hard as we can around the rental costs, if that answers your question.

Ms SHING — Yes, thank you. And just a supplementary if I may: to what extent does the improved ratio occur as a consequence of consultation with affected agencies and work areas?

Ms PORTHOUSE — Very much so. It is paramount that we get them to buy in to us meeting these targets, so the stakeholder engagement is critical with the government's accommodation persons for us to be able to deliver on these outcomes. Is that what you meant?

Ms SHING — Yes, thank you. That is very helpful.

Ms PENNICUIK — If I could refer you to page 30 again of the questionnaire, which is question 21, with regard to the variances. On page 30, with regard to education, the variance of the estimate and the actual is $1.1 billion, and the explanation is:

> The main reason for this variance relates to the different methodology —

again —

> used for expenses since the 2013–14 original budget as noted above. $147 million relates to a reduction in employee expenses driven by the deconsolidation of dual sector entity TAFEs ($100 million) and the winding down of the Voluntary Departure Packages ($40 million) —

so that comes to 147 million. But that leaves really sort of around 900 million. There is not detail of why that is. I just wondered if you have any more information there.

Mr MARTINE — Yes. Thanks for the question, because I think it perhaps highlights an issue on which it might be worth us, as a department, providing some more material to the committee. If you look at a lot of the explanations on page 30, as Ms Skilbeck indicated in a much earlier answer, a lot of them are being driven by changes in the methodology in how some of these things get classified under the framework that is released by the ABS. They are not really changes driven by changes in policy or changes in service delivery. Particularly on page 30, but I notice it comes up in a few answers to the questions, quite a few of them do make reference to different methodologies et cetera — —

Ms PENNICUIK — Quite a lot of them do, so obviously — —

Mr MARTINE — Yes, so I am just wondering whether, perhaps not dobbing in too much work for my department, the committee might find it useful that we try and provide perhaps a bit more of an answer on this question that tries to draw a bit of a distinction between methodology changes. So the answer to that question on the bottom of page 31, for example, about general public services that Mr Smith asked was all about a change in methodology — something is moving from one line to another. It has just struck me that a number of these questions, particularly in this couple of pages, are really driven by just purely methodology changes. Perhaps if we just take that on notice and think about a way to try to break that down a bit to assist the committee to try to understand what is just moving from one line to another versus what is actually a real change. We will have a look at that.

Ms PENNICUIK — A supplementary, thanks, Chair. There are two things I would like to follow that up with. One is $900 million, to me, seems a lot to attribute to a change in methodology, and when you came back after the break I got excited and thought you were going to respond to my question about the general purposes at the top of page 31, which again was 700 million, and the answer was about the methodology. I note that you are going to provide some information on notice, but I wonder if you could — for the benefit of everyone here who may not see the answer taken on notice later, because we are having a discussion about it now and because even just the two that I have highlighted is about $1.6 billion attributed to changes in methodology and there is even more, as you have said yourself in that answer to question 21, where the answer is changes to methodology — maybe make some general outline as to what that actually means. What was the methodology? What is the methodology now, and how does that result in these changes?

Mr MARTINE — So the language 'different methodology' is for expenses. What that effectively means is an expense has moved from one of these lines to another. It is not as if there is a change in methodology that has increased expenses overall or reduced expenses overall. Essentially what has happened is, with the ABS framework and as Ms Skilbeck indicated earlier, there has been some work undertaken to better map departmental outputs through to this particular classification which is used nationally so that comparisons can be made between jurisdictions.

All of these changes in terms of methodology are all about something moving from one classification to another classification. I suspect we probably need to provide the committee with a much better explanation on what that actually means and where some of these big ones are going — so it is going from, for example, general public services to education. We will endeavour to try and provide that because it has obviously raised a number of questions through the course of the morning. But, as you note, in most of the answers it does talk about the different methodology.

If one is interested in what each of the departments is spending in terms of their annual expenditure for 13–14, their output statements are probably the key focus. They will be outlined in their annual reports. This methodology — this government purpose classification which comes out of the ABS — is really to help do some comparisons between jurisdictions, and they are not easy things to do. But certainly none of those methodology changes relate to changing the overall quantum of expenses either up or down.

Ms PENNICUIK — Thank you. Can I have one brief supplementary?

The CHAIR — It can be very brief, Ms Pennicuik.

Ms PENNICUIK — I think this is a very interesting and important issue. I understand that it is very important of course to be able to compare across jurisdictions and then also to compare across time from what was happening before and what is happening now. Your answer was to provide the committee with more information, but I suppose just following on from all this, it is fine for DTF to talk about this, and they understand the lingo — you know, the vernacular — but perhaps there are different levels of understanding of that in the committee, and there are far different levels of understanding of it in the community. For the community to be able to make sense of all this, I think it does need more explanation as to what is happening.

Mr MARTINE — Perhaps if I can just add to my answer, because you are touching on a very important issue here, this framework has essentially been established to help do comparisons between jurisdictions. I would not necessarily say it is the right framework to assist within a jurisdiction and within a parliamentary committee, for example, in assessing output spending by departments — in a sense that kind of tension is there. So we will certainly have a look at how we can provide the committee with a bit more explanation of the methodology changes. But, as I said, they are all kind of self-contained within that one table — X is moving from Y to Z.

Dr CARLING-JENKINS — In 2012 it is my understanding that the former committee recommended that DTF require departments to publish more information around performance measures, such as how these are calculated, and discuss what they mean in line with the UK model. It is a few years on, and we on this committee still struggle a little bit with some of the performance measures provided. They continue to at times lack some clarity, meaningfulness and even some robustness at times. The response to the former committee was that that would be taken under consideration. I would just like to follow up on that. Will your department consider directing other departments to include supporting information that explains the basis of performance measures included in annual reports, and, if so, can we expect to see greater clarity in performance measures in this coming year?

Mr MARTINE — I might just make a few general comments before passing across to Ms Skilbeck. Performance measures are a very important part of the transparency and accountability framework. The ones obviously I am most familiar with are my own department's performance measures. Certainly in looking through those there are a number, particularly some of the quantitative measures, that to me actually do not make a lot of sense, and the ones that we are actually looking to remove relate to things such as the quantity of briefs we prepare. We have traditionally set targets that we will prepare 300 briefs for the Treasurer of the day, and some years we might be 280 and some years we might be 350. To me, it begs the question: is it good to be below 300 or is it good to be above 300?

Dr CARLING-JENKINS — It lacks a bit of meaningfulness, doesn't it?

Mr MARTINE — That is right. So I am always very cautious actually that a quantitative measure is not necessarily better than just a qualitative measure. Sometimes a quantitative measure may lead to misinformation or even a perverse outcome. Maybe we wrote 350 briefs because our first briefs were so poor that the Treasurer of the day could not understand them and we had to follow it up — who knows? It is a good indicator on workload, but it does not really provide useful information on performance. We have been having a look at our own, and I guess my general observation before I pass to Ms Skilbeck is that I suspect we are kind of the tip of the iceberg in terms of the performance measures across government in some quite important areas of spending to help track what is actually being delivered in those. I kind of struggle with some of my own, and we are doing a bit of work on that. I might pass across to Ms Skilbeck for some other observations.

Ms SKILBECK — More broadly we are, starting with our own department, focused on improving the performance measures generally in substance as opposed to explaining the ones that we have currently. Like so many useful policy reforms, it is a balancing act between the amount of change one generates and the consistency of information that this committee and the Parliament receives, so we do need to balance that. The other key balancing act is the accountability needs to be with the department for whom the performance relates and the ministers and not something we impose, so it needs to be a conversation, but with some clear parameters around what is a good measure and what is not.

I particularly support the comment the secretary made about some of the artificiality around having a quantitative measure rather than a qualitative one when the nature of the work can only really be observed qualitatively. So we are well and truly in that process discussing with departments. We have had some delays in that work with some of the machinery of government, the natural consequences of accounting for reconfiguration of outputs and departments and therefore the measures related to the outputs, so our energy now is being spent more directly on improving those performance measures, and in some cases that may mean fewer of them than more.

Certainly I will take on notice and take on board in terms of the work we do the need to explain both any changes we make but the measure ongoing when it is used. We do endeavour to do that, but it can get to be quite a detailed and lengthy budget paper 3 if there is a lot of commentary for every single measure, so it is a balancing act. But, yes, we are very, very focused on improving the usability and the significance of the performance measures and reducing some of the spurious effort that is put into us counting our number of briefs and the equivalent in more significant service areas around government so that we can focus on some key measures.

Mr MARTINE — And for the record, our briefs are of a very high quality.

Ms SKILBECK — It is genuinely difficult to explain.

Mr T. SMITH — So can we see some of them, then?

Ms SHING — Are you advising that on the basis of a brief that you received, Secretary?

Mr MARTINE — I will take that on notice.

The CHAIR — One question from me: Mr O'Brien made mention of this earlier in relation to the fees paid to consultants in relation to the proposed long-term lease of the Port of Melbourne Authority. I suppose that leads to a broader question as to governments deciding to go out and spend money on consultancies. I think it has been a well-established practice for decades that governments of all different persuasions do not necessarily have the requisite skills within the VPS and go out and procure specific key personnel to provide a specific form of work or goods or services — invariably, professional services — for a specific task. I am just wondering, in terms of the broader Treasury perspective, how does the amount expended in the 14–15 financial year for consultants tally with previous years under previous administrations?

Mr MARTINE — Thanks for the question, and I will refer back to the document I was referencing earlier, which is the document on our website on contractors and consultants for 2014–15. I do not have in front of me the history of what was spent in the department, but I am, I suspect, pretty safe to conclude that this level of expenditure — a total approved of 29.8, so that picks up the 22.9 that we spoke about on the port, plus everything else — would be certainly much higher than it has been, but that is very much because we have engaged experts to assist us with the Port of Melbourne lease, which takes up 22.9 of the 29.8. As a general observation, certainly within DTF, we try and ensure that we are only buying in expertise where we really have a gap. Obviously with a major asset sale, effectively — the Port of Melbourne lease — it is not unusual in any jurisdiction to spend the necessary money to get the appropriate legal and commercial advice, and that is effectively what we have done. So I suspect, yes, we are higher than we have been for a number of years, but I think if you stripped out the port lease, my guess — but it would only be a guess — is that I suspect it would probably not be too different within DTF.

The CHAIR — But it would broadly be consistent with what, for example, was spent with Troughton Swier in the 90s in relation to the privatisation of the SECV, broadly.

Mr MARTINE — That could be. From my experience looking at some of these things in other jurisdictions, I do not think what we are spending for the port lease is significantly different to what you would expect in a major divestment such as the Port of Melbourne. What was spent by the department or the state back in the 90s, I am not too sure about.

The CHAIR — I seem to recall many FOI documents floating around at that stage and being quite impressed with the amount of money that was paid, but it was value for money.

Mr MORRIS — A quick clarification first, if I could, just going back to the EBA question. I was actually looking at something else but I was listening to the answer, and I thought someone said that there had not been any new EBAs commenced in that period.

Ms SKILBECK — In the 14–15 year there were no new major EBAs, and we define 'major' as wages bills of more than a billion dollars.

Mr MORRIS — My understanding was the ambulance EBA commenced in May 15. Does that fall below that threshold, or is that not accurate?

Ms SKILBECK — It would have been post-budget numbers. I would have to take on notice whether the wages bill falls underneath. It is actually a small number of employees in the workforce relative to nurses or teachers.

Mr MORRIS — Yes. If you could, that would be terrific. I wanted to turn to the issue of the gambling litigation. There was a reference in the budget to a hearing in May, and then in the AFR there was a reference to being listed for hearing in the High Court on 10 and 11 November. I am just wondering if you can give us an update on where that is at.

Mr MARTINE — Thanks, Deputy Chair. I guess we are, in a sense, all waiting for the outcome of the High Court. I think if we have any greater intelligence — which is not unusual, because it is hard to extract information out of the High Court at times, and there were the hearings in November, I think it was — it would be good, certainly from a budgeting point of view, to have it resolved pretty quickly so that we get a sense of what it means for the state, because things can go either way and there are two cases and the amounts are quite significant, and either one can fall either way. They may both go the way of the state, and there is a very significant upside, or they may go the other way. We just do not have any kind of intelligence on the thinking of the High Court or timing at the moment. So as I said, I am hoping that it will be resolved, and I suspect, like a lot of these actions, we will probably just get a notification that next week there will be an announcement.

Mr MORRIS — By way of a supplementary, on exactly that point, I am just wondering whether the department has quantified the liability to the state, should each of those succeed and, if so, what the number might be.

Mr MARTINE — Okay, so I am looking at note 35, page 153, of the annual financial report. It does talk about the Tabcorp proceeding and the amount claimed plus interest, and there is a reference to another matter. There are two cases that have been actually linked in the High Court. But we have published those numbers I am pretty sure in documents somewhere. I am just trying to remember where they are. Unfortunately you do get to lose some of your memory on where these numbers appear, but they are there somewhere. So we will endeavour to try and track them down and provide them to the committee, unless Mr Johnstone can instantaneously find them.

Ms SHING — No pressure, though.

Mr JOHNSTONE— Not quite.

Ms SHING — That is okay. We can take them later.

Mr MARTINE — They are there somewhere. We will endeavour to provide that to the committee.

Mr MORRIS — Yes, and if perchance they are not published, if we can have them in any case — —

Mr MARTINE — Okay, we will take that on notice.

Mr MORRIS — I am sure they are, but if they are not, we can have them anyway.

Mr MARTINE — I can give perhaps a partial answer. We will take it on notice to provide it for the committee, but the Tabcorp issue amounts to $686 million plus interest, and the Tatts — —

Look, we will take it on notice. As I said, they are there somewhere.

Mr MORRIS — And those figures represent the anticipated liability, not just the — —

Mr MARTINE — The state did make a payment. I am trying to remember what year it was. It must have been 2014.

Mr JOHNSTONE — Yes. This one here.

Mr MARTINE — Yes, so in terms of the Tatts claim, which the state lost at that point, we actually paid out, including interest, on 27 June 2014, $540 million. We will certainly come back to you in writing, but the rough orders of magnitude then are that the Tatts issue on the table is 540, so if we win that, we get 540 plus interest back, and the Tabcorp was the 680-odd plus interest, so if we lose that, we would have to pay that. They are kind of the orders of magnitude.

Mr MORRIS — That is useful. Thank you.

Mr D. O'BRIEN — Sorry, was that the 15–16 budget paper?

Mr MARTINE — That is the budget update released in late last year.

The CHAIR — I am conscious of time. I would like to thank the witnesses for their attendance. Thank you Mr Martine, Ms Skilbeck, Mr Webster, Mr Johnstone and Ms Porthouse.

Mr D. O'BRIEN — On a point of order, sorry, if I may, you said you were going to try and get the Rural Finance answer before the end of the hearing. Did you have any luck on that one?

Mr MARTINE — I think we have got an answer, which hopefully will provide the information you are after.

Mr WEBSTER — The 119.7 million represents business as usual, which was the expectation if the business had not been sold, and it represented advances that would have come back to the government. The actual amount is the total amount of the sale, which includes the equity and the sale of the loan book.

Mr D. O'BRIEN — Right. So it is the — —

Mr MARTINE — It is announced at 1.4.

Mr D. O'BRIEN — It is the book as well, so it is really just an accounting measure. It is not an actual — —

Mr WEBSTER — It is not the profit on the sale. Effectively on the total proceeds we pay back the loan. The equity portion is what is left after the loan from TCV to Rural Finance being repaid.

Mr D. O'BRIEN — Thank you.

The CHAIR — The committee will follow up with you on questions taken on notice. A written response should be provided within 21 days of that request. Thank you.

Witnesses withdrew.