2005-06 Budget Update

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Presented by the Honourable John Brumby MP,
Treasurer of the State of Victoria

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Budget Paper No. 2 – Strategy and Outlook
Budget Paper No. 3 – Service Delivery
Budget Paper No. 4 – Statement of Finances (incorporating Quarterly Financial Report No. 3)
Budget Overview

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Front cover images ■ The Peace Tower (2003), artist Suesy Circosta in collaboration with residents of the Collingwood housing estate 'Work for the Dole' participants and volunteers from the City of Yarra ■ The Voices of Atherton Gardens Choral Group photographed by Angela Bailey 2004

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For the information of Honourable Members

This Budget Update refers to the general government sector throughout, except where specifically stated.

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HIGHLIGHTS

The *Budget Update* contains a mid-cycle review of the state of the annual Budget, which is presented in Parliament each May. The update provides revised estimated financial statements, which includes the projected outcome for the end of the current financial year, as well as an update on the State's economy and the underlying parameters used for the Budget.

- The *2005-06 Budget Update* demonstrates that the Government continues to achieve its commitment to maintaining its $100 million budget surplus target, ensuring that businesses and families in Victoria have a stable financial environment in which to invest and plan for their futures.
- In May 2005, the Government announced that its primary operating target would be measured against the net result from transactions, using the Australian equivalents to International Financial Reporting Standards (A-IFRS). The revised estimate of the 2005-06 general government operating surplus (net result from transactions) is $331 million, slightly lower than the $365 million May 2005 Budget estimate. Over the following three year period, the net result from transactions is now projected to average $416 million a year.
- Including the non-cash impact of actuarial adjustments and revaluations, the 2005-06 net result is projected to be $1 502 million, which is higher than the original budget estimate and reflects higher than expected superannuation gains associated with strong equity market performance, together with an increase in the discount rate applied to the accrued liability.
- The Government continues to improve quality, access and equity in service delivery to all Victorians:
  - included in the *2005-06 Budget Update* is significant funding for the *Moving Forward* statement, which builds on existing strengths in regional economies and communities to enhance growth in provincial Victoria; and
  - net infrastructure investment spending is expected to average $2.8 billion a year over the four years to 2008-09.

- Victoria is maintaining modest and sustainable levels of net financial liabilities, consistent with its triple-A rating. The Government is using its strong balance sheet to fund key investment projects that generate long-term benefits:
  - net debt is projected to increase from $1.5 billion as at 30 June 2005 to $5.4 billion as at 30 June 2009, but nevertheless remains around 2.0 per cent of gross state product (GSP), down from 3.2 per cent of GSP in 1999 and 16.3 per cent of GSP in 1995; and
  - net financial liabilities are projected to increase from $16.8 billion (7.7 per cent of GSP) as at 30 June 2005 (after allowing for A-IFRS methodology changes) to $20.5 billion (7.7 per cent of GSP) as at 30 June 2009.
- The Government is committed to providing a fair and efficient tax system to Victorian businesses and households that is competitive with other states. After allowing for known future tax policy changes in all states, Victoria's taxes are set to be around the Australian average.
- The forecast for Victorian gross state product (GSP) growth for 2005-06 is unchanged at 3.0 per cent. The outlook for 2006-07 is also unchanged at 3.5 per cent. The mix of expected growth drivers has shifted marginally towards stronger business investment and net exports, and away from consumer spending.
- Victoria's economy grew by 2.3 per cent in 2004-05, below the budget estimate of 2.75 per cent and equal to the growth rate for Australia as a whole. Over the past four years, the Victorian economy has grown at an average annual rate of 3.6 per cent, above the national rate of 3.3 per cent.
- Victoria's labour market has continued to perform well, with strong employment growth combining with higher labour force participation. The forecast for employment growth has been revised up to 2.0 per cent in 2005-06.
- Reflecting further rises to oil prices since the 2005-06 Budget, CPI inflation has been revised higher to 3.0 per cent in 2005-06. The forecast for 2006-07 is unchanged at 2.5 per cent.

CHAPTER 1: FINANCIAL POLICY OBJECTIVES AND STRATEGY

- The Government is committed to maintaining its $100 million budget surplus target, ensuring that businesses and families in Victoria have a stable financial environment in which to invest and plan for their future.
- The revised estimate of the 2005-06 general government operating surplus (net result from transactions) is $331 million, slightly lower than the $365 million May 2005 Budget estimate. Over the following three year period, the net result from transactions is now projected to average $416 million a year.
- The adoption of the new Australian equivalents to International Financial Reporting Standards (A-IFRS) has further enhanced the transparency and accountability of Victoria's financial and resource management.
- The Government is helping to create greater capacity for economic growth through significant investments in infrastructure projects. In line with this goal, general government net infrastructure investment spending is expected to average $2.8 billion a year over the four years to 2008-09.
- The Government continues to improve quality, access and equity in service delivery to all Victorians. Included in the *2005-06 Budget Update* is significant funding for the *Moving Forward* statement, which builds on existing strengths in regional economies and communities to enhance growth in provincial Victoria.
- The Government is committed to providing a fair and efficient tax system to Victorian businesses and households that is competitive with other states. After allowing for known future tax policy changes in all states, Victoria's taxes are set to be around the Australian average.
- Victoria is maintaining modest and sustainable levels of net financial liabilities, consistent with its triple-A rating. The Government is using its strong balance sheet to fund key investment projects that generate long-term benefit.

FINANCIAL STRATEGY

The Government's financial policy objectives and strategies are set out in the *Financial Management (Financial Responsibility) Act* 2000. The Act includes a set of sound financial management principles. These are to:

- manage financial risks faced by the State prudently, taking into consideration economic circumstances;
- pursue spending and taxation policies that are consistent with a reasonable degree of stability and predictability in the level of the tax burden;
- maintain the integrity of the Victorian tax system;
- ensure that government policy decisions have regard to their effects on future generations; and
- provide full, accurate and timely disclosure of financial information relating to the activities of the Government and its agencies.

These financial management principles underpin the Government's financial policy objectives and strategies.

With the broad strategic priority of providing a sound and stable financial basis from which growth can be promoted across the whole State, the Government will continue to deliver world-class infrastructure to drive economic growth, and improve quality, access and equity in key services to all Victorians, while maintaining a sound financial position.

The Government's financial responsibility legislation requires a statement of its short and long-term financial objectives. These objectives are summarised in Table 1.1.

Table 1.1: 2005-06 Financial objectives

Long-term	*Short-term*
Maintain a substantial budget operating surplus	Operating surplus of at least $100 million in each year
Deliver world-class infrastructure to maximise economic, social and environmental benefits	Implement strategic infrastructure projects
Provide improved service delivery to all Victorians	Complete the implementation of the 2002 election commitments
Provide a fair and efficient tax system that is competitive with other states	Implement reforms to Victoria's business taxation system
Maintain state government net financial liabilities at prudent levels	Maintain a triple-A credit rating

Objective one: Operating surplus

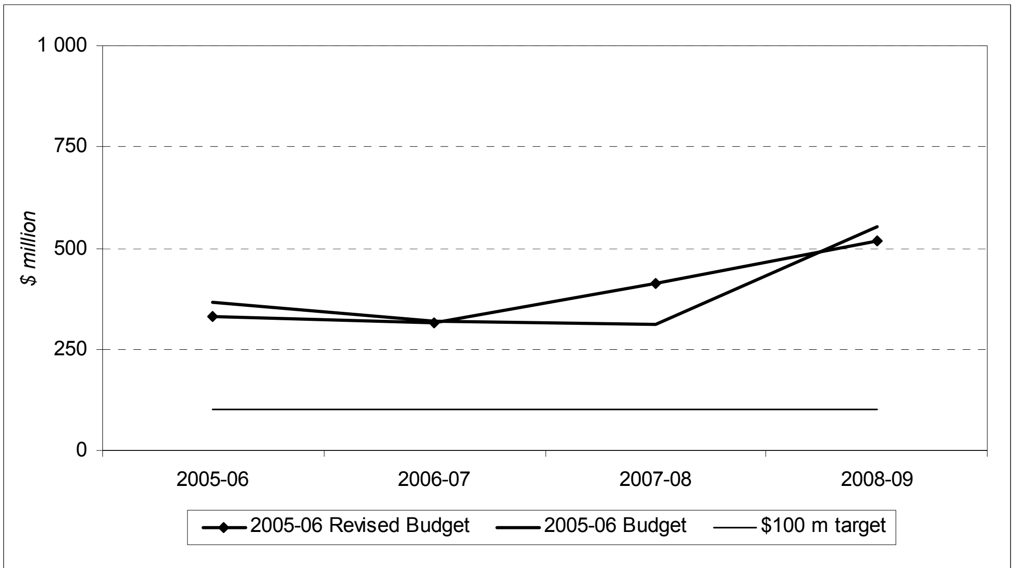
The Government's long-term objective is to maintain a substantial budget operating surplus. In the short term, the Government's key financial objective is to maintain an operating surplus of at least $100 million in each year.

As part of the implementation of the Australian equivalents to International Financial Reporting Standards (A-IFRS), the Government reviewed the financial measure against which the $100 million operating surplus is to be achieved, and determined that the A-IFRS net result from transactions is the most robust measure of the Government's financial management under the new standards.

The revised outlook for the budget surplus remains consistent with this objective, as can be seen in Chart 1.1. The net result from transactions is forecast to be $331 million in 2005-06 and to average $416 million a year over the following three years.

Chapter 3, *Budget Position and Outlook,* provides further detail, including alternative measures of the Government's operating performance.

Chart 1.1: General government sector net result from transactions

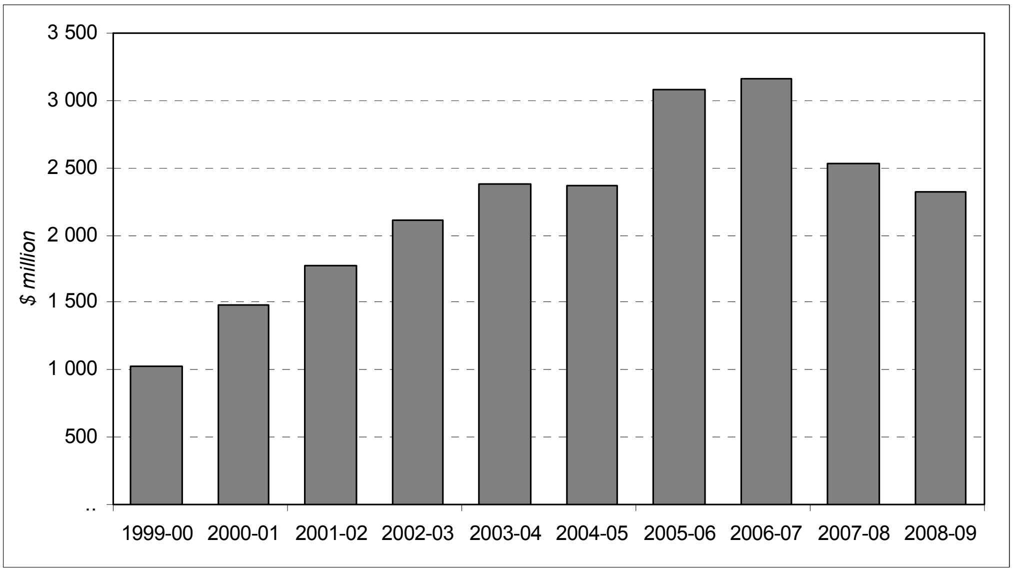


Source: Department of Treasury and Finance

Objective two: Infrastructure

The Government is committed to delivering world-class infrastructure to enhance social, economic and environmental benefits across the State. Over the period 2005-06 to 2008-09, general government net infrastructure investment is expected to average $2.8 billion a year (see Chart 1.2). The Government has invested more than $11 billion since 1999-2000, almost double the infrastructure spending in the preceding six years.

Chart 1.2: General government sector net infrastructure investment[(a)]



Source: Department of Treasury and Finance

Note:
(a) Includes purchases of property, plant and equipment and net contributions to other sectors of government less proceeds from sale of property, plant and equipment.

The significant boost to Victoria's infrastructure has been made possible by Victoria's strong financial position. The forecast strong net result from transactions over the forward estimates period, coupled with the strength of the balance sheet, enables the Government to continue its major program of building, upgrading and modernising infrastructure.

Objective three: Service delivery

The Government is continuing to improve quality, access and equity in service delivery to all Victorians through the implementation of the Government's 2002 election commitments and its 2005-06 Budget initiatives.

Also included in the *2005-06 Budget Update* is significant funding for the *Moving Forward* statement, which builds on existing strengths in regional economies and communities to enhance growth in provincial Victoria. Funding is committed until 2009-10, and includes a $200 million extension of the Regional Infrastructure Development Fund and a new $100 million Provincial Victoria Growth Fund.

Objective four: Taxation

The Government has a commitment to a fair and efficient tax system that is competitive with other states.

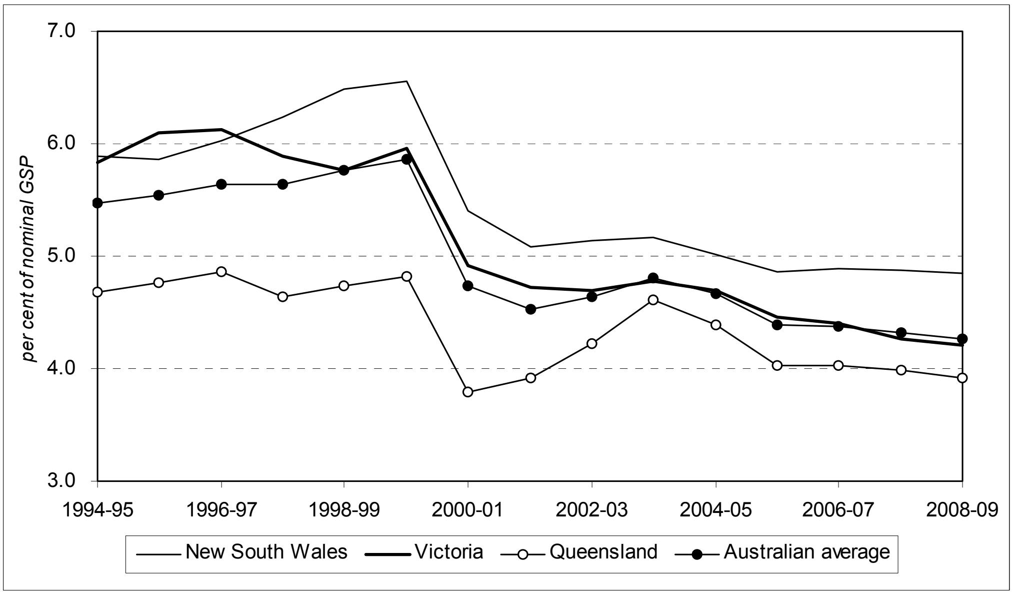
The competitiveness of Victoria's tax regime plays an important role in underpinning economic growth and investment. Consistent with the Government's strategic priority of promoting growth across the whole of the State, the Government aims to ensure that Victoria's taxes remain competitive with the Australian average.

Victoria's preferred measure of tax competitiveness is state taxation expressed as a share of nominal gross state product (GSP). This measure relates the level of taxation revenue to economic capacity. Taxation revenue as a share of nominal GSP for Victoria, New South Wales, Queensland and the Australian average is shown in Chart 1.3.

The tax competitiveness estimates are based on the *2005-06 Budget Update* taxation estimates for Victoria combined with the 2005-06 Budget estimates of all other jurisdictions, apart from Queensland where the estimates in the October 2005 *Special Fiscal and Economic Statement* were used.

Victoria's tax burden in 2005-06, using the budget update estimates, is set to be 4.46 percentage points of nominal GSP. Victoria is set to be around 0.40 percentage points ($935 million) below New South Wales and around the Australian average. Over the forward estimates period, Victoria's taxation as a share of GSP is forecast to decline to 4.21 per cent of nominal GSP in 2008-09.

Chart 1.3: Taxation revenue as a share of nominal GSP



Source: Australian Bureau of Statistics, Department of Treasury and Finance, 2005-06 Budgets of all jurisdictions (except Queensland) and Queensland's Special Fiscal and Economic Statement (October 2005).

Objective five: Net financial liabilities

The Government's commitment to sound financial management includes maintaining the State's net financial position at prudent levels in order to achieve its short-term objective of maintaining Victoria's triple-A credit rating. The international credit rating agencies focus on both net debt and net financial liabilities of the general government sector and the non-financial public sector as measures of overall indebtedness.

Victoria's triple-A long-term local currency and foreign currency debt ratings were re-affirmed by Standard and Poor's and Moody's Investors Service in October 2005. Both rating agencies cited low debt levels and a strong track record in prudent fiscal management as key reasons behind their affirmations.

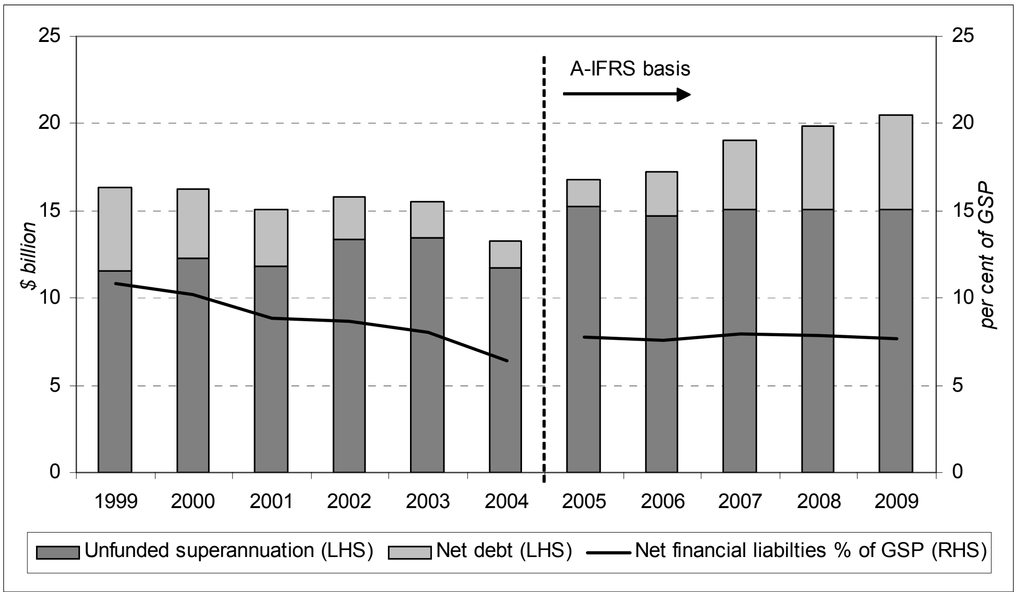
The 2005-06 revised budget projections reinforce these positive factors as:

- strong net result from transactions are projected for 2005-06 ($331 million) and the remainder of the forward estimates period ($416 million average);
- the nominal value of net debt is projected to increase from $1.5 billion (0.7 per cent of GSP) as at 30 June 2005 to $5.4 billion (2.0 per cent of GSP) as at 30 June 2009. These levels of debt are relatively low by international standards and well below historical levels of 3.2 per cent of GSP in 1999 and 16.3 per cent in 1995; and

- general government net financial liabilities are projected to increase in nominal terms from $16.8 billion (7.7 per cent of GSP) as at 30 June 2005 (after allowing for A-IFRS methodology changes to the unfunded superannuation liability) to $20.5 billion (7.7 per cent of GSP) as at 30 June 2009. This nominal increase is in line with the growth of the Victorian economy, and reinforces the Government's commitment to maintaining financial liabilities at prudent and manageable levels.

Chart 1.4 shows the nominal level of net debt and unfunded superannuation, and total net financial liabilities as a share of GSP. The break in the series reflects the A-IFRS methodology change to the value of unfunded superannuation. For 2006, this methodology change added around $4.8 billion (2.1 per cent of GSP) to the level of unfunded superannuation.

Chart 1.4: General government net financial liabilities, as at 30 June[(a)(b)]



Source: Department of Treasury and Finance

Notes:
(a) General government net financial liabilities are calculated as the sum of the net debt and unfunded superannuation liabilities.
(b) Net debt is calculated as gross debt less liquid financial assets. For the years relevant, Growing Victoria investments are excluded as an offset to gross debt on the grounds that these investments were earmarked for infrastructure projects and were therefore not available to redeem gross debt.

CHAPTER 2: ECONOMIC CONDITIONS AND OUTLOOK

- Solid world economic growth is expected to continue to support the Victorian and Australian economies.
- The forecast for Victorian gross state product (GSP) growth for 2005-06 is unchanged at 3.0 per cent. The mix of expected growth drivers has shifted marginally towards stronger business investment and net exports, and away from consumer spending.
- The outlook for economic growth in 2006-07 is unchanged at 3.5 per cent.
- Victoria's economy grew by 2.3 per cent in 2004-05, below the budget estimate of 2.75 per cent and equal to the growth rate for Australia as a whole. Over the past four years, the Victorian economy has grown at an average annual rate of 3.6 percent, above the national rate of 3.3 per cent.
- Victoria's labour market has continued to perform well, with strong employment growth combining with higher labour force participation. The forecast for employment growth has been revised up to 2.0 per cent in 2005-06.
- Reflecting further rises to oil prices since the 2005-06 Budget, CPI inflation has been revised higher to 3.0 per cent in 2005-06. The forecast for 2006-07 is unchanged at 2.5 per cent.

THE ECONOMY SINCE BUDGET

World economic conditions

Since the 2005-06 Budget, the world economy has continued to grow at a solid rate, driven by continued strength in China and the United States and new stimulus from Japan and the rest of Asia. Europe continues to lag behind the world economy.

The overall outlook for world economic growth remains solid. The latest Consensus Economics survey (November 2005) forecasts remain largely unchanged since budget time, with world economic growth expected to be 3.1 per cent in 2005 and 2006.

A major development for the world economy has been the continued upward trend of oil prices. In contrast to previous oil price shocks, the current high oil prices are the result of strong world demand and, despite recent hurricane-related supply disruptions, are not expected to have a contractionary impact on the global economy. The impact of higher oil prices has, however, been reflected in higher headline inflation. Importantly, there is currently little evidence of significant second round inflationary impacts in the major economies.

The US economy has continued its solid growth into 2005, with a recovery in the labour market and gains to house prices supporting consumer spending. Significant rises in corporate profits are also combining with high business sentiment to support strong business investment. Hurricanes Rita and Katrina have resulted in only minor short-term weakness in the economy, which is expected to record solid growth in the remainder of the year and into 2006. This is despite higher headline inflation as a result of higher oil prices.

China's economy has performed even more strongly than expected at budget time. Consensus Economics growth forecasts have been revised up from 8.6 per cent to 9.4 per cent in 2005. The strong growth in China is combining with further signs of a recovery in Japan, where there has been a pick-up in business investment, and stronger consumer spending with an improving labour market. The outlook for the rest of Asia has also improved with the region benefiting from an emerging recovery in global information technology and communications demand.

European economic growth has continued to be weak, with domestic demand hindered by high unemployment and poor consumer and business sentiment. Since the 2005-06 Budget, the outlook for the United Kingdom, Germany and France has been downgraded, with Consensus Economics now expecting economic growth in the European Union to be 1.6 per cent in 2005 (downgraded from a forecast of 1.9 per cent in April).

Victoria

Victoria's economy grew by 2.3 per cent in 2004-05, equal to the growth rate for Australia as a whole. This compares with the budget estimate of 2.75 per cent and represents a slowdown on the revised growth estimate of 5.3 per cent for 2003-04. This is consistent with trends for Australia as a whole, and reflects a mild downturn in housing construction and continued negative impact of net exports.

Solid world economic growth has continued to support the Australian economy, with strong demand for commodities resulting in large gains in resource exports. As noted in the 2005-06 Budget, Victoria's relative lack of mineral resources compared with other major states has affected its export performance. In addition, a high exchange rate and enduring impacts of drought have continued to adversely affect Victoria's manufacturing and agricultural sectors. As a result, net exports have continued to be weak and detracted from economic growth in 2004-05.

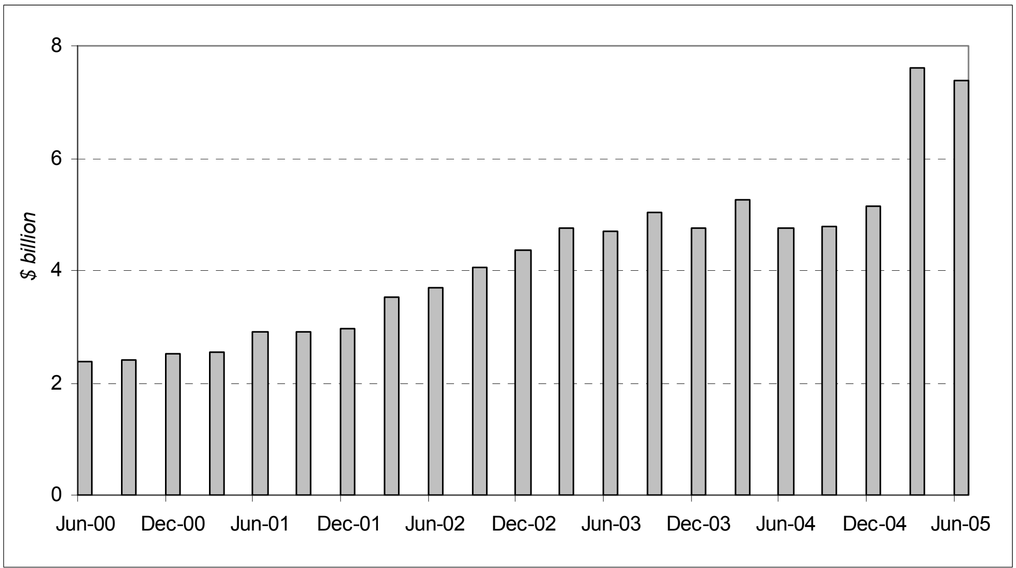
Aggregate demand grew by a solid 4.2 per cent in 2004-05, slightly higher than originally forecast at budget time, with business investment and consumer spending stronger than expected.

Consumer spending has remained strong, with growth of 4.8 per cent in 2004-05, which is higher than that expected at budget time. Growth has been driven by spending on clothing and footwear, furnishing and other household equipment, communications and hotels, cafes and restaurants. Consumer spending is likely to be more subdued in the coming year, with a slight slowing in employment growth combining with weaker house prices and continued rebalancing of household balance sheets.

As expected, Victoria experienced a relatively mild downturn in housing construction, with a decline of 3.9 per cent in 2004-05. The soft landing in part reflects Victoria's continued solid population growth and employment growth. The decline follows three years of strong growth in housing activity. Some continued weakness in housing construction is expected in the short-term, followed by a return to trend growth rates.

Business investment has been a major strength of the Victorian economy, growing by 10.2 per cent in 2004-05. This represents the seventh consecutive yearly rise, and was broadly based across machinery and equipment, non-dwelling investment, intangibles and livestock during the year. Business investment is expected to continue to be a key driver of the State's economy, and the non-residential building and engineering construction pipeline is at record levels (see Chart 2.1).

Chart 2.1 Business investment pipeline, Victoria[(a)]



Source: Australian Bureau of Statistics

Note:
(a) Sum of the value of non-residential building work yet to be done and engineering construction work yet to be done. Quarterly original data, current prices.

Victoria experienced strong employment growth in 2004-05, recording a rise of 3.3 per cent. This was above the budget forecast of 3.0 per cent. Nearly two-thirds of net jobs created have been full-time, with the biggest contributors to growth coming from the health and community services, retail trade, and transport and storage sectors. The strong growth in employment throughout the year has also continued to encourage more Victorians into the workforce, with the labour force participation rate rising by 1.1 percentage points in 2004-05.

ECONOMIC OUTLOOK

Revised projections for the Victorian economy are presented in Table 2.1.

Table 2.1: Economic projections[(a)]

(Projections in 2005-06 Budget, where different, are in parentheses)

	2004-05 Actual	*2005-06 Forecast*	*2006-07 Forecast*
Gross state product	2.3	3.0	3.5
	(2.75)		
Employment	3.3	2.0	1.25
	(3.0)	*(1.0)*	
Unemployment rate [(b)]	5.7	5.5	5.5
	(5.75)		*(5.25)*
Consumer price index	2.0	3.0	2.5
		(2.75)	
Wage cost index [(c)]	3.9	4.0	3.5
	(3.75)	*(3.75)*	

Sources: Australian Bureau of Statistics; Department of Treasury and Finance

Notes:
(a) Per cent change on proceeding year unless otherwise indicated. All projections are rounded to the nearest 0.25 percentage point.
(b) Year average level, per cent.
(c) Total hourly rate, excluding bonuses.

Continued solid world economic growth is expected to support the Victorian and Australian economies, as the domestic drivers of housing construction and consumer spending slow.

The forecast for Victorian GSP growth for 2005-06 is unchanged at 3.0 per cent. Economic growth of 3.5 per cent is expected in 2006-07. Although the growth forecast for 2005-06 is unchanged, the mix of expected growth drivers has shifted marginally towards stronger business investment and net exports, and away from consumer spending.

Stronger business investment is expected, with firms choosing to boost capacity in a climate of continued solid demand. The outlook is also supported by a business investment pipeline at record levels, including major infrastructure projects such as EastLink having just commenced.

Net exports are expected to recover, with stronger export growth the result of some improvement in agricultural conditions and solid world economic growth. Import growth is likely to slow as consumer spending moderates from the rapid growth rates seen in recent years.

The forecast for employment growth has been revised to 2.0 per cent in 2005-06, up from 1.0 per cent at budget time, but below the 3.3 per cent in 2004-05. The upward revision reflects the continued strong growth recorded since the Budget. The unemployment rate is expected to remain steady at around 5.5 per cent into 2005-06, with employment growth being matched by further increases in labour force participation.

The CPI inflation forecast has been revised higher to 3.0 per cent in 2005-06, due to a further rise in oil prices since the Budget. CPI headline inflation is currently at the top of the Reserve Bank of Australia's target band, which presents the possibility of future interest rate rises if oil prices flow through into sustained increases in prices and wages.

Economy-wide wage pressures are expected to continue to be moderate, although the 2005-06 forecast has been revised up marginally to reflect the current tightness in the labour market.

ECONOMIC RISKS

The Victorian economic projections are sensitive to a number of risks. The major risks include higher interest rates, rising oil prices and movements in the Australian dollar. These issues are discussed in Chapter 5, *Statement of Risks.*

CHAPTER 3: BUDGET POSITION AND OUTLOOK

- The revised 2005-06 general government net result from transactions surplus is $331 million, slightly lower than the $365 million May 2005 budget estimate. Over the forward estimates period, these surpluses are now projected to average $416 million a year.
  - Including the non-cash impact of actuarial adjustments and revaluations, the 2005-06 net result is projected to be $1 502 million, which is higher than the original budget estimate and reflects a higher than expected superannuation gain associated with strong equity market performance, together with an increase in the discount rate applied to the accrued liability.
- Net infrastructure investment spending is expected to average $2.8 billion a year over the four years to 2008-09.
- Net debt is projected to increase from $1.5 billion as at 30 June 2005 to $5.4 billion as at 30 June 2009, but nevertheless remains around 2.0 per cent of GSP, down from 3.2 per cent of GSP in 1999 and 16.3 per cent of GSP in 1995.
- Net financial liabilities are projected to increase from $16.8 billion (7.7 per cent of GSP) as at 30 June 2005 (after allowing for Australian equivalents to International Financial Reporting Standards (A-IFRS) methodology changes) to $20.5 billion (7.7 per cent of GSP) as at 30 June 2009.

This chapter provides an overview of the projected budget position for the period 2005-06 to 2008-09 for the general government sector, and a reconciliation of movements in income and expenses since the 2005-06 Budget released in May 2005 (referred to as 'original budget').

The budget and forward estimates years are based on the economic projections outlined in Chapter 2, *Economic Conditions and Outlook*, and reflect the accounting policies and assumptions documented in Chapter 6, *Estimated Financial Statements and Notes*. The estimates take into account the financial impacts of all policy decisions announced by the Victorian Government, as well as Commonwealth Government funding revisions and other factors as at 30 November 2005 that affect the projected general government sector financial statements. Specific policy decisions taken since the 2005-06 Budget that have an effect on the budget position are summarised in Appendix A, *Specific Policy Initiatives Affecting the Budget Position*.

The State's budget (2005-06) and forward estimates years (2006-07 to 2008-09) represent planning projections based on unchanged policy and other assumptions. Outcomes could differ from these projections for many reasons, including realisation of the risks described in Chapter 5, *Statement of Risks*.

The estimates from 2005-06 (detailed in Chapter 6, *Estimated Financial Statements and Notes*) are formulated in accordance with the Australian equivalents to International Financial Reporting Standards (A-IFRS), which are applicable for reporting periods commencing on or after 1 January 2005.

2005-06 TO 2008-09 OUTLOOK

Table 3.1 sets out the projected aggregate outlook over the budget and forward estimates period. A more detailed statement of financial performance is provided in Chapter 6, *Estimated Financial Statements and Notes*.

Table 3.1: Summary operating statement 2005-06 to 2008-09[(a)]

($ million)

	2005-06 Budget	*2005-06 Revised*	*2006-07 Estimate*	*2007-08 Estimate*	*2008-09 Estimate*
Taxation	10 306.2	10 452.9	10 880.6	11 132.0	11 556.4
Investment income	1 397.9	1 310.4	1 137.6	1 210.3	1 152.1
Grants	14 262.1	14 340.0	14 868.2	15 421.6	16 042.7
Sales of goods and services	2 397.1	2 496.9	2 531.8	2 577.2	2 620.6
Other income [(b)]	2 260.2	2 271.2	2 393.0	2 381.2	2 533.7
Total income from transactions	**30 623.6**	**30 871.4**	**31 811.2**	**32 722.4**	**33 905.5**
% change			3.0%	2.9%	3.6%
Employee benefits	11 201.5	11 346.6	11 670.5	12 008.4	12 352.2
Superannuation	1 759.3	1 754.9	1 772.3	1 773.1	1 764.0
Depreciation and amortisation	1 235.1	1 221.7	1 285.4	1 371.5	1 439.5
Financing costs	492.1	477.7	484.6	490.2	506.9
Supplies and services	9 991.2	10 044.1	10 651.9	11 071.7	11 758.3
Other expenses [(c)]	5 579.7	5 695.2	5 629.8	5 594.5	5 566.3
Total expenses from transactions	**30 258.9**	**30 540.3**	**31 494.5**	**32 309.4**	**33 387.2**
% change			3.1%	2.6%	3.3%
Net result from transactions	**364.7**	**331.1**	**316.6**	**413.0**	**518.3**
Net gains - disposal of physical assets	25.7	29.7	22.9	10.6	11.2
Other income - other economic flows	8.5	8.5	8.5	8.5	8.5
Actuarial gains on superannuation	..	1 203.5	..	..	..
Other expenses - other economic flows	(74.8)	(70.8)	(66.9)	(56.3)	(52.5)
Net result from other economic flows	**(40.6)**	**1 170.9**	**(35.5)**	**(37.1)**	**(32.8)**
Net result	**324.1**	**1 502.0**	**281.1**	**375.8**	**485.5**

Source: Department of Treasury and Finance

Notes:

(a) *This is an abbreviated operating statement. The full statement is shown in Chapter 6, Estimated Financial Statements and Notes.*

(b) *Comprises regulatory fees and fines, fair value of assets received free of charge, capital asset charge and other miscellaneous income.*

(c) *Includes grants and transfer payments.*

As highlighted in Chapter 1, *Financial Policy Objectives and Strategy*, the Government has committed to achieving operating surpluses of at least $100 million a year on a net result from transactions basis. Table 3.1 shows that the Government is forecast to achieve this financial objective. The net result from transactions is budgeted to be $331 million in 2005-06, before averaging $416 million a year over the following three years.

These strong forecast net result from transactions surpluses demonstrate the Government's solid performance in continuing to responsibly manage the State's finances. Furthermore, these strong surpluses are an important funding source for the Government's substantial capital investment program, thereby limiting the call on debt to finance needed infrastructure (see *Cash Flows* below).

As discussed below in *Other economic flows*, the revised 2005-06 net result of $1 502 million is higher than the revised net result from transactions, largely due to the non-cash impact on the unfunded superannuation liability of movements in share markets and the long-term bond rate.

Alternative measures of financial performance

Alternative measures of financial performance are set out in Table 3.2. This includes Government Finance Statistics (GFS) measures used by the Australian Bureau of Statistics and the net result.

Table 3.2: A-IFRS and GFS budget measures

($ million)

	2005-06 Budget	*2005-06 Revised*	*2006-07 Estimate*	*2007-08 Estimate*	*2008-09 Estimate*
A-IFRS Net result from transactions	364.7	331.1	316.6	413.0	518.3
A-IFRS Net result	324.1	1 502.0	281.1	375.8	485.5
GFS net operating balance	364.7	331.1	316.6	413.0	518.3
GFS net lending/(borrowing)	(1 433.1)	(1 523.9)	(853.7)	(421.7)	(398.0)
GFS cash surplus/(deficit) [(a)]	183.2	229.2	(713.8)	(495.6)	(557.9)

Source: Department of Treasury and Finance

Note:

(a) International Monetary Fund/GFS cash surplus/deficit equals the net cash flows from operating activities less investments in non-financial assets, and excludes acquisitions under financial leases.

Unlike the Government's net result from transactions target measure, the net result includes various revaluation gains and losses on assets and liabilities and provision for doubtful debts. In particular, the non-cash impact of revaluation gains and losses on superannuation liabilities in the current financial year adds substantial volatility to the A-IFRS net result through movements in factors such as interest rates or share markets.

The revised 2005-06 net result is $1 502 million (refer to Table 3.2), significantly higher than the $324 million original budget estimate. As discussed below in *Other economic flows*, this is mainly due to better than expected investment performance of superannuation schemes, together with a reduction in the accrued superannuation liability due to a 0.21 percentage point increase in the discount rate.

Chapter 5, *Statement of Risks,* estimates that a 1 per cent increase in interest rates would bring about a $2.9 billion increase in the A-IFRS net result in the current financial year. In addition, the day-to-day valuation of unrealised capital gains on equities held by Victoria's superannuation funds impacts on the A-IFRS net result.

Given such volatility is beyond the control of governments, this is the primary reason why the A-IFRS net result from transactions is a more appropriate measure of the Government's financial management.

The GFS net operating balance is identical to the net result from transactions. Both measures exclude the effects of revaluation (holding gains or losses) arising from changes in the market prices and other changes in the volume of assets. The GFS net operating balance is the conceptual basis of most state budgets, and provides comparability with other states.

The GFS net lending/borrowing result is equal to the GFS net operating balance less net acquisitions of non-financial assets. As net lending/borrowing takes into account total spending on fixed assets during the period, rather than just the current year's expense (through depreciation), it is lower than the GFS net operating balance and the A-IFRS net result from transactions over the forward estimates.

The GFS cash surplus/deficit result is equal to net cash flows from operating activities less net cash investment in non-financial assets. Although both net lending and the cash surplus include the immediate impact of expenditure on fixed assets, the cash surplus removes non-cash revenues and expenses (including the superannuation interest cost), and allows for cash contributions made to the unfunded superannuation liability. The projected general government sector GFS cash surplus is $229 million in 2005-06. Over the forward estimates period, general government sector GFS cash deficits are projected to be $589 million a year on average.

Income from transactions

Total income from transactions is projected to increase by 3.2 per cent a year on average over the forward estimates period, driven by growth in taxation and Commonwealth grants.

Over the forward estimates period, taxation is projected to grow by 3.4 per cent a year on average, generally reflecting the positive impact of continuing strength in employment and overall economic growth, as well as the flow through of property value growth. The growth in taxation has been moderated by a number of factors, including:

- modest growth in land tax (1.5 per cent a year on average) reflecting the impact of the program of tax rate reductions announced in the 2005-06 Budget;
- land transfer revenue is expected to increase by only 1.6 per cent a year on average with modest growth in the number of land transfer transactions (in line with increases in the number of households) and mild house price growth;
- the abolition of rental business duty from 1 January 2007 following a review under the 1999 *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*; and
- the implementation of a complete smoking ban within enclosed licensed premises (with some exceptions) from 1 July 2007, which will impact on gambling taxation revenue from 2007-08.

Investment income is projected to fall slightly over the forward estimates period, as dividend income is projected to return to long-term trends beyond 2005-06.

Grants income is expected to grow at an average rate of 3.8 per cent a year over the forward estimates period. This reflects several factors, including:

- continued growth in GST grants due to increases in the national GST pool (which in turn is driven by moderate rises in consumption and dwelling investment) and an assumed gradual rise in Victoria's share; and
- growth in specific purpose operating and capital grants, largely comprising grants for education and health related services.

Expenses from transactions

Total expenses from transactions are projected to increase by 3.0 per cent a year on average over the forward estimates period. This is slightly below expected price inflation plus Victorian population growth.

Reflecting expected inflation and the Government's continuing commitment to improve services such as health, education and community safety, employee benefits are expected to grow by 2.9 per cent a year on average over the forward estimates period, with purchases of supplies and services, grants and 'other' expenses expected to rise by 3.3 per cent a year on average.

This growth partly reflects the impact of the recent decisions announced by Government in the *Moving Forward* statement (released in November 2005), which provides significant funding to build on existing strengths in regional economies and communities to enhance growth in provincial Victoria.

Depreciation and amortisation expense is expected to increase by 5.6 per cent a year on average, reflecting growth in the capital stock as a result of the Government's continuing substantial infrastructure investment program and revaluations of physical assets.

Other economic flows

Differences between the net result from transactions and the net result are due to other economic flows. This includes actuarial adjustments, gains and losses on disposal of physical assets and other income and expenses from other economic flows.

Other economic flows are expected to improve the net result for the general government sector by $1 171 million in 2005-06. This is largely due to the following non-cash revaluation gains:

- better than expected investment returns on superannuation scheme assets increasing superannuation gains by $649 million. This was primarily caused by better than expected equity market performance resulting in the State Superannuation Fund earning 6.75 per cent compared to a budgeted return of 1.88 per cent; and
- a reduction in the value of the accrued superannuation liability which also increased superannuation gains by $554 million, primarily due to an increase in the ten year Commonwealth bond rate (effective annualised rate) from 5.22 per cent at 30 June 2005 to 5.43 per cent.

Over the forward estimates period, other economic flows are expected to reduce the net result by $35 million a year on average, largely reflecting expenses relating to the provision for doubtful debts.

RECONCILIATION OF FORWARD ESTIMATES TO PREVIOUSLY PUBLISHED ESTIMATES

Table 3.3 compares the revised outlook for the net result from transactions measure for the period 2005-06 to 2008-09 to the estimates published in the 2005-06 Budget.

The projected revised 2005-06 net result from transactions is $331 million, a decrease of approximately $34 million from the result estimated at the time of the 2005-06 Budget. Over the forward estimates period, net result from transactions surpluses are expected to be higher on average relative to original budget estimates.

Table 3.3: Reconciliation of estimates to 2005-06 Budget[(a)]

($ million)

	2005-06 Revised	*2006-07 Estimate*	*2007-08 Estimate*	*2008-09 Estimate*
Net result from transactions - 2005-06 Budget	**364.7**	**319.3**	**313.0**	**550.8**
Plus: Variations in income from transactions since 2005-06 Budget				
Policy decision variations	**(19.1)**	**37.7**	**53.0**	**57.4**
Economic/demographic variations				
Taxation	166.7	168.8	131.6	128.5
Investment income	(55.0)	(78.2)	38.4	84.2
Total economic/demographic variations	**111.7**	**90.6**	**170.0**	**212.8**
Commonwealth grant variations				
General purpose grants	37.0	86.5	155.7	214.9
Specific purpose payment grants	25.3	43.3	(2.5)	(164.2)
Total Commonwealth grant variations	**62.3**	**129.8**	**153.2**	**50.7**
Increase in own-source revenue	**129.5**	**120.5**	**135.0**	**154.6**
Administrative variations	**(36.6)**	**(21.9)**	**(45.8)**	**(72.3)**
Total variation in income from transactions since 2005-06 Budget	**247.8**	**356.7**	**465.5**	**403.1**
Less: Variations in expenses from transactions since 2005-06 Budget				
Policy decision variations [(b)]	**113.5**	**194.3**	**219.7**	**196.7**
Commonwealth variations	**33.2**	**(54.5)**	**(100.3)**	**(152.1)**
Variations due to changes in own-source revenue	**134.4**	**118.8**	**129.5**	**153.9**
Administrative variations				
Superannuation variations	(11.9)	(19.6)	(26.2)	(58.2)
Other administrative variations	12.2	120.4	142.8	295.3
Total administrative variations	**0.3**	**100.8**	**116.6**	**237.1**
Total variation in expenses from transactions since 2005-06 Budget	**281.5**	**359.3**	**365.5**	**435.7**
Revised net result from transactions	**331.1**	**316.6**	**413.0**	**518.3**

Source: Department of Treasury and Finance

Notes:

(a) Totals may not add due to rounding.

(b) Output policy decisions reflect the total cost of decisions. The total expenditure for each year may differ to Appendix A, Specific Policy Initiatives Affecting the Budget Position, for certain initiatives due to Treasurer's contingency funding being offset against expenditure in 'other' administrative variations and due to departmental reprioritisations being included in Appendix A.

Variations to income from transactions

Income from transactions in 2005-06 is expected to be $248 million higher than the 2005-06 Budget estimate and is projected to be $408 million a year higher on average over the forward estimates period.

Policy decisions have decreased income by $19 million in 2005-06, but increased income by $49 million a year on average over the next three years, largely as a result of:

- reduced taxation revenue from 2005-06 associated with the Government’s decision to revise the policy announced in the 2005-06 Budget that reforms land tax on trusts; and
- the introduction of a Development Contribution from 2006-07, which requires developers in Melbourne’s five designated growth areas to contribute to the cost of a range of infrastructure projects, including transport, environmental and community facilities. This Development Contribution is a key mechanism supporting the Government's Plan for Melbourne’s Growth Areas, which seeks to provide infrastructure as growth areas develop.

Economic and demographic factors have caused taxation estimates to be revised upwards by $149 million a year on average from 2005-06 to 2008-09, with major changes including:

- an upward revision in payroll tax estimates (up $91 million a year on average) due to a higher 2004-05 revenue base reflecting stronger than expected employment and wages growth in 2004-05, combined with growth biased towards larger firms. Economic forecasts for employment and wages growth in 2005-06 have also been revised upwards reflecting continuing strong economic growth in 2005-06;
- an increase in the forecasts for land transfer revenue of $133 million in 2005-06, $102 million in 2006-07, and $59 million a year on average over the next two years. The upward revisions are largely due to a smaller than expected fall-off in the number of land transfer transactions. The stronger than expected volumes are partly due to the continued strong first homebuyer activity and, while investor demand has eased, owner occupier activity has continued to be solid; and
- a reduction in land tax estimates (down $25 million a year on average) due to a slightly lower 2004-05 revenue base and the impact of a High Court decision on land tax.

Investment income as a result of economic and demographic factors has been revised downwards by $67 million a year on average in 2005-06 and 2006-07, before rising to be $84 million higher by 2008-09. Major changes include:

- a reduction in income tax equivalent payments from the public financial corporations sector in 2005-06 and 2006-07. As a result of the transition to A-IFRS, the methodology used to calculate the outstanding insurance claims liability has increased the valuation of the liabilities. This increase is an allowable deduction for the purpose of calculating national tax equivalent payments;
- an upward revision to dividends and income tax equivalent payments from the public financial corporations sector from 2007-08, reflecting increased investment earnings from a higher asset base as a result of better investment performance in 2004-05, partly offset in 2007-08 by the impact of an improved benefits package for injured workers; and
- a minor downward revision to dividends received from the water authorities over the four years from 2005-06, due to lower than expected profits in 2004-05 and over the forward estimates period.

Commonwealth general purpose grants income, (GST grants) have been revised upwards by $37 million in 2005-06, rising to be $215 million higher by 2008-09. The increase in 2005-06 estimated income reflects revised growth in the GST revenue pool as disclosed by the Commonwealth in its 2005-06 Budget, while the growth over the forward estimates period is primarily due to a change in the methodology used to forecast Victoria's share of the national GST pool.

Commonwealth specific purpose payments have been revised upward by $34 million a year on average in 2005-06 and 2006-07, before falling to be $164 million lower in 2008-09. The decrease over the forward estimates period is mainly driven by a decrease in Commonwealth funding for government and non-government schools, reflecting a decrease in the Average Government School Recurrent Costs index in 2005. Funding was reduced by $42 million in 2005-06 before falling to be $236 million lower by 2008-09. The impact of this downward revision has been mitigated by a number of increased grants, including:

- an upward revision in capital grants reflecting additional funding for a number of new *AusLink* rail projects, together with revised cash flows for a number of road projects based on the 2005-06 Commonwealth Budget;
- an increase in the Commonwealth's commitment to provide $167 million to the Wimmera-Mallee Pipeline project;
- an increase in grants to the health and community services sector, including programs relating to disability services and funding to meet the cost of specialised medicines; and
- an increase in Exceptional Circumstances funding from the Commonwealth in 2005-06 for drought-affected areas, as well as an increase in its level of subsidy for drought-affected farmers in existing areas.

Own-source revenue has been revised upwards by $135 million a year on average, mainly due to updated projections in the TAFE and school sectors based on improved performance and growth over recent years, together with higher than expected donations, bequests and grants to hospitals from the private sector, and increased revenue estimates for the Environmental Protection Fund.

Administrative variations have resulted in a downward revision of $44 million a year on average, reflecting a number of factors, including a reduction in interest revenue over the four years to 2008-09 as a result of the Government continuing to utilise its financial assets to fund its strong commitment to infrastructure spending and service delivery.

Variations to expenses from transactions

Expenses from transactions in 2005-06 are expected to be $282 million higher than the 2005-06 Budget estimate and are projected to be $387 million a year higher on average over the forward estimates period.

Since the 2005-06 Budget, policy decisions account for additional expenses of $114 million in 2005-06 (with the impact on expenses from transactions partly offset by contingency funding) and $204 million a year on average over the forward estimates period. This includes funding to:

- implement a range of initiatives as part of the *Moving Forward* statement (released in November 2005), to build on existing strengths in regional economies and communities to enhance growth in provincial Victoria. In particular, this funding will renew the Regional Infrastructure Development Fund; create a new Provincial Victoria Growth Fund; and fund regional ports, transport and tourism;
- manage increased demand and complexities for services provided to government school students with special education needs under the Program for Students with Disabilities;
- build on existing reforms in child protection services and provide additional child protection workers and grants to community service organisations; and
- upgrade the fixed safety camera system to ensure ongoing compliance with road safety measures by Victorian drivers.

Specific policy decisions since the 2005-06 Budget are summarised in Appendix A, *Specific Policy Initiatives Affecting the Budget Position*.

Changes to Commonwealth grants have had a negative impact on expenses, on average, over the budget and forward estimates period compared with the original budget. This was primarily driven by a reduction in expenditure as a result of the decrease in Commonwealth grants for government and non-government schools, partly offset by an increase in expenditure relating to health and community services, together with an increase in Exceptional Circumstances funding in 2005-06.

Expenditure associated with an increase in own-source revenue (as discussed above) has increased by $134 million a year on average. This primarily relates to TAFEs and schools, hospitals, and waste-management programs and Sustainability Fund initiatives. Minor variances in expenditure from revenue earned reflects timing differences, and some expenditure on capital (which does not impact on the operating statement).

Administrative variations are expected to increase expenses above the original budget estimates by $101 million in 2006-07, growing to be $237 million higher by 2008-09. This variation reflects a number of factors, including:

- a downwards revision to superannuation expense over the forward estimates period, largely reflecting the flow-on impact of better than expected investment returns;
- increased expenses over the forward estimates associated with a non-cash adjustment relating to the employee entitlements of former National Express employees that the State assumed responsibility for as part of the re-franchising of the former National Express franchise; and
- an upward revision in 2008-09 to the contingency held for concluding initiatives, reflecting further analysis of relevant initiatives (refer to Chapter 5, *Statement of Risks,* for further details).

CASH FLOWS

The net result from transactions is an important funding source for the Government's substantial capital investment program. Table 3.4 provides a summary of cash generated through the operations of Victorian Government departments and other general government sector agencies, and how that cash is applied to infrastructure investment, together with any requirements for additional cash through financing activities.

Table 3.4: Application of cash resources

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Net result from transactions	**364.7**	**331.1**	**316.6**	**413.0**	**518.3**
Add back: Non-cash income and expenses (net) [(a)]	2 213.9	2 349.9	1 424.6	1 296.9	1 164.5
Net cash flows from operating activities	**2 578.6**	**2 680.9**	**1 741.2**	**1 709.9**	**1 682.8**
Less:					
Net investment in fixed assets					
Expenditure on approved projects	3 098.9	3 215.5	2 909.8	1 630.6	876.0
Unallocated provision for future allocation	..	..	399.5	1 109.4	1 567.0
Proceeds from asset sales	(134.0)	(138.0)	(144.0)	(210.3)	(121.3)
Total net investment in fixed assets	**2 965.0**	**3 077.5**	**3 165.3**	**2 529.6**	**2 321.7**
Finance leases	615.1	615.1	..	..	..
Other investment activities (net)	15.6	17.1	4.4	0.9	17.3
Decrease/(increase) in net debt	**(1 017.0)**	**(1 028.7)**	**(1 428.5)**	**(820.6)**	**(656.1)**

Source: Department of Treasury and Finance

Note:
(a) Includes depreciation and non cash movements in liabilities such as unfunded superannuation and employee benefits.

Table 3.4 shows an expected net result from transactions for 2005-06 of $331 million, and averaging $416 million a year over the forward estimates. Adjusting for a number of expense and income items that do not require or provide cash resources during the year (principally depreciation, but also including growth in unfunded superannuation liabilities and employee benefit liabilities) yields a projected net cash inflow from operating activities for 2005-06 of $2.7 billion, and an average of $1.7 billion a year from 2006-07.

This cash surplus from operating activities is a significant source of financing for the Government's infrastructure investment program, funding around 70 per cent of the net $2.8 billion a year on average to be spent on fixed assets over the four years to 2008-09. The Government is utilising its strong balance sheet to fund the remainder of its infrastructure program, through an increase in net debt of $984 million a year on average over the forward estimates period.

Around $3 billion of the planned infrastructure spending from 2006-07 represents the provision of a contingency to allow for future government capital spending. This allocation is in accordance with previous budget practice to ensure realistic forward projections of asset investment consistent with the Government's desire to ensure that an appropriate asset base exists to support ongoing service delivery. As part of the annual budget process, funds from this provision will be allocated to specific capital projects.

Of the $1.0 billion increase in net debt in 2005-06, $615 million is due to the recognition of new finance lease arrangements, with an equivalent increase in fixed assets, following the expected completion and handover of the Spencer Street Station redevelopment and the completion of two new prisons in Ravenhall and Lara. These projects are being delivered under the *Partnerships Victoria* model.

FINANCIAL POSITION

Table 3.5 provides a summary of the general government sector statement of financial position. A more detailed statement of financial position is provided in Chapter 6, *Estimated Financial Statements and Notes*.

Table 3.5: General government summary balance sheet as at 30 June

($ million)

	2005 Actual [(a)]	2006 Revised	2007 Estimate	2008 Estimate	2009 Estimate
Assets					
Capital stock [(b)]	52 886.7	57 017.8	60 647.8	64 109.2	67 869.2
Financial assets [(c)]	4 432.9	4 045.6	2 630.0	2 106.9	1 960.1
Other assets	2 620.7	2 267.4	2 472.1	2 582.4	2 724.8
Total assets	**59 940.3**	**63 330.8**	**65 749.8**	**68 798.4**	**72 554.1**
Liabilities					
Superannuation	15 287.8	14 721.7	15 063.1	15 109.3	15 042.5
Borrowings	5 560.0	6 194.8	6 198.2	6 486.3	6 984.5
Other liabilities	7 910.1	8 089.4	8 132.8	8 148.0	8 197.1
Total liabilities	**28 757.9**	**29 005.9**	**29 394.0**	**29 743.6**	**30 224.2**
Net assets	**31 182.4**	**34 324.9**	**36 355.8**	**39 054.8**	**42 330.0**

Source: Department of Treasury and Finance

Notes:
(a) Balances as at 30 June 2005 have been adjusted due to the adoption of A-IFRS. This includes a change in methodology used to value the unfunded superannuation liability.
(b) Capital stock includes land and buildings, plant and equipment, roads and earthworks, cultural and other assets.
(c) Financial assets include cash assets, investments, loans and placements.

General government sector net assets are expected to increase from $31.2 billion as at 30 June 2005 to $42.3 billion at 30 June 2009. This growth is largely due to an expected increase in the value of the capital stock, primarily driven by the significant levels of capital expenditure by the Government over the budget and forward estimates period, together with upwards revaluations of assets.

This increase is partly offset by growth in the value of the unfunded superannuation liability over the forward estimates, which is in line with the profile as set by the fund actuary to enable the Government to achieve its target of full funding by 2035.

With net assets rising, the balance sheet illustrates the Government's commitment to sound financial management through a strong, stable and flexible financial position for the State.

NET DEBT AND NET FINANCIAL LIABILITIES

While the preceding analysis is predominately on an Australian accounting standards basis, the analysis of net financial liabilities and net debt are based on the Government Finance Statistics (GFS) economic framework (see Chapter 7, *Accrual Uniform Presentation of Government Finance Statistics*).

The Government's commitment to sound financial management includes maintaining the State's net financial liabilities at prudent levels in order to achieve its short-term objective of maintaining Victoria's triple-A credit rating. The key measures of financial position are the GFS measures of net debt and net financial liabilities. The international credit rating agencies focus on both net debt and net financial liabilities of the general government sector and the non-financial public sector as measures of overall indebtedness. Table 3.6 highlights these key measures for the general government sector.

Victoria's triple-A long-term local currency and foreign currency debt ratings were re-affirmed by Standard and Poor's and Moody's Investors Service in October 2005. Both rating agencies cited low debt levels and a strong track record in prudent fiscal management as key reasons behind their affirmations. As presented in Table 3.6, the levels of general government net debt and net financial liabilities from 2004-05 reinforce these positive trends.

Table 3.6: General government net financial liabilities as at 30 June

($ million)

	2005 *Actual* [(a)]	2006 *Revised*	2007 *Estimate*	2008 *Estimate*	2009 *Estimate*
Financial assets					
Cash and deposits	1 803.2	1 788.7	1 473.7	1 058.7	943.7
Advances paid	95.9	95.3	92.3	89.3	86.2
Investments, loans and placements	2 625.5	2 252.7	1 152.1	1 044.1	1 012.3
Total financial assets	**4 524.6**	**4 136.7**	**2 718.1**	**2 192.0**	**2 042.1**
Financial liabilities					
Deposits held	449.9	455.9	462.4	468.7	476.7
Advances received and borrowings	5 558.8	6 193.6	6 197.0	6 485.1	6 983.4
Net debt	**1 484.1**	**2 512.8**	**3 941.3**	**4 761.9**	**5 417.9**
Unfunded superannuation	15 287.8	14 721.7	15 063.1	15 109.3	15 042.5
Net financial liabilities	**16 771.9**	**17 234.5**	**19 004.4**	**19 871.2**	**20 460.4**

Source: Department of Treasury and Finance

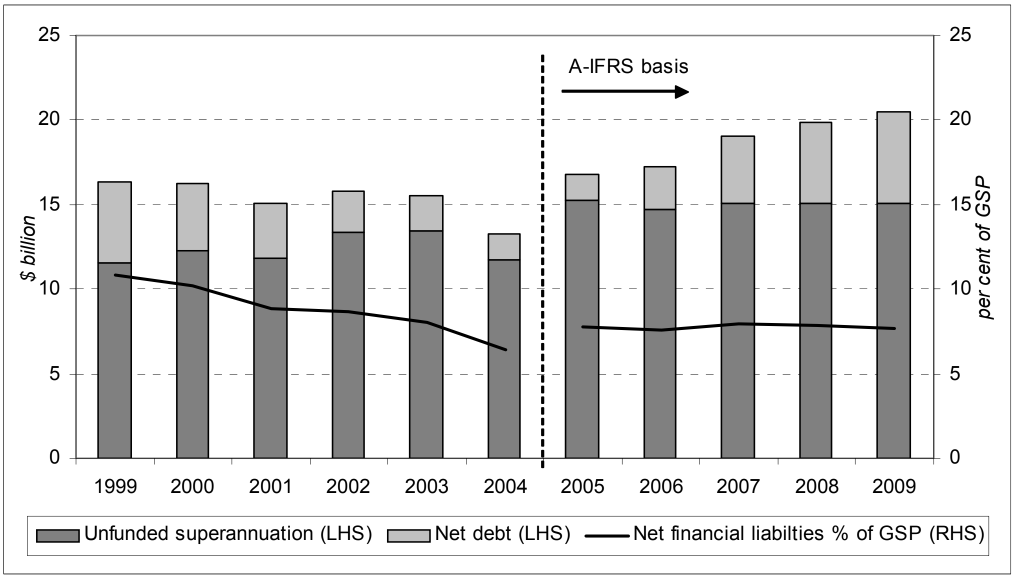
Note:

(a) Balances as at 30 June 2005 have been adjusted due to the adoption of A-IFRS. This includes a change in methodology used to value the unfunded superannuation liability.

Net debt, which is the standard measure used to assess general government indebtedness, is determined by deducting liquid financial assets from gross debt. The rationale for deducting liquid financial assets is that, in a period of financial difficulty, liquid assets would be readily available to redeem debt. Table 3.6 shows net debt is projected to increase from $1.5 billion (0.7 per cent of GSP) as at 30 June 2005 to $5.4 billion (2.0 per cent of GSP) as at 30 June 2009.

These levels of debt are relatively low by international standards and well below historical levels of 3.2 per cent of GSP in 1999 and 16.3 per cent in 1995.

Chart 3.1: General government net financial liabilities, as at 30 June(a)(b)(c)



Source: Department of Treasury and Finance

Notes:

(a) General government net financial liabilities are calculated as the sum of the net debt and unfunded superannuation liabilities.

(b) Net debt is calculated as gross debt less liquid financial assets. For the years relevant, Growing Victoria investments are excluded as an offset to gross debt on the grounds that these investments were earmarked for infrastructure projects and were therefore not available to redeem gross debt.

(c) Balances as at 30 June 2005 have been adjusted due to the adoption of A-IFRS. This includes a change in methodology used to value the unfunded superannuation liability.

Net financial liabilities are the sum of unfunded superannuation liabilities and net debt. General government net financial liabilities are projected to increase from $16.8 billion (7.7 per cent of GSP) as at 30 June 2005 to $20.5 billion (7.7 per cent of GSP) as at 30 June 2009. As presented in Chart 3.1, the 30 June 2005 closing balances have been adjusted to reflect the impact of the A-IFRS methodology change on the value of the unfunded superannuation liability. This methodology change added around $4.8 billion (2.1 per cent of GSP) to the level of the unfunded superannuation liability compared with the methodology used in the previous financial year (although with no change to the amount of cash required to finance the superannuation liability).

This increase is in line with the growth of the Victorian economy, and reinforces the Government's commitment to maintaining financial liabilities at prudent and manageable levels.

Major impacts of A-IFRS

On 15 July 2004, the Australian Accounting Standards Board (AASB) approved the A-IFRS to come into effect for reporting periods commencing on or after 1 January 2005.

Under A-IFRS, the unfunded superannuation liability and associated expense are affected by changes in the long-term bond rate as well as the investment returns on the superannuation schemes' assets. It is important to note that these movements will not impact on the net result from transactions, which is the Government's measure of operating surplus. This measure will not be distorted by movements in the unfunded superannuation liability that arise due to changing financial market conditions. These movements are recorded as other economic flows.

For the revised 2005-06 estimate, the movement in other economic flows of $1 171 million primarily reflects the impact on the unfunded superannuation liability of movements in share markets and the long-term bond rate.

Table 3.7 below shows the main balance sheet impacts of adopting A-IFRS, which indicates that the main variations occur to opening balances as at 1 July 2005 for property, plant and equipment, and superannuation.

The decreases in property, plant and equipment are a result of the impact of the new requirements relating to the deemed cost revaluation of assets (AASB 1), the transfer of property, plant and equipment to non-current assets for resale (AASB 5), changes in finance and operating leases (AASB 117) and the impairment of assets (AASB 136).

However, the more material change is in relation to the measurement of superannuation. AASB 119 requires the liabilities of the State's defined benefit superannuation schemes to be measured using a long-term bond rate, rather than the assumed long-term earning rate on the schemes' assets. The State is using the annualised ten-year Commonwealth bond rate to measure its liabilities. The large movement shown in the table is the transitional impact. In 2000, the Government adopted a funding framework aimed at fully funding these liabilities by 2035. The increase in the reported unfunded superannuation liability that arises under A-IFRS is due to a change in valuation methodology, and the amount of cash required to finance the superannuation liability is unchanged.

Table 3.7: Transitional impact of adopting A-IFRS on the Balance Sheet

($ million)

	2005
Total assets at 30 June 2005 - GAAP basis	**60 623.3**
A-IFRS impact on assets	
Receivables	180.9
Assets held for sale	59.2
Inventories	(24.7)
Property plant and equipment	(881.2)
Roads and earthworks	(19.9)
Other differences	2.7
Total A-IFRS impact on assets	**(683.0)**
Total assets at 1 July 2005 - A-IFRS	**59 940.3**
Total liabilities at 30 June 2005 - GAAP basis	**23 774.3**
A-IFRS impacts on liabilities	
Payables	141.5
Interest-bearing liabilities	29.7
Superannuation	4 794.3
Other differences	18.0
Total A-IFRS impact on liabilities	**4 983.5**
Total liabilities at 1 July 2005 - A-IFRS	**28 757.9**
Total equity at 30 June 2005 - GAAP basis	**36 848.9**
A-IFRS impacts on equity	
Accumulated funds	(4 461.2)
Reserves	(1 205.3)
Total A-IFRS impact on equity	**(5 666.5)**
Total equity at 1 July 2005 - A-IFRS	**31 182.4**

Source: Department of Treasury and Finance

CHAPTER 4: ECONOMIC REFORM

- Continued economic reform is needed to maintain and improve standards of living and meet the challenges of population ageing, globalisation and a decline in the dividend from past reform.
- Victoria has strong economic reform credentials, and has shown leadership in the debate over the nature and extent of a national approach to the next wave of reform, developing a plan for a 'third wave' of reform in the key areas of infrastructure, regulation, health, education and training and work incentives.
- Victoria continues to advocate cooperation and partnership with the other States and Territories and the Commonwealth in the pursuit of reform.
- Victoria considers the Council of Australian Governments (COAG) meeting in early 2006 presents as the next opportunity for other jurisdictions to commit to national economic reform.

Past reforms

Reforms in the early 1980s led to a dramatic change in the Australian and Victorian economies. Whereas Australia and Victoria had been relatively insulated from world developments, reforms such as the floating of the dollar, deregulation of financial markets and the reduction in trade barriers led to productivity increases, as local businesses responded to the threat or actuality of international competition. Opening the economy facilitated an expansion of the traded sector. Greater integration with the world economy created the pressure and the opportunity for enhanced competition and productivity.

The development of the traded sector led, in turn, to pressure on the non-traded sector and the impetus for a second wave of reform in the mid 1990s. A national program of microeconomic reform followed, which focused on increased competition and improving the efficiency of infrastructure services. National Competition Policy (NCP) extended competition law to areas owned or regulated by the State (including all government businesses and the professions) and required all legislative restrictions on competition to be reviewed, and where appropriate, reformed. It provided the incentive for state and the Commonwealth governments to improve the structure of services provided by utilities.

The previous two waves of reform have led to substantial economic growth and associated improvements in wellbeing. Measured by gross domestic product (GDP) per capita, standards of living have increased by a third since 1990 for the average Australian (and for the average Victorian). This is the longest period of sustained growth on record and stronger than the average for all countries of the Organisation of Economic Cooperation and Development (OECD), a common benchmark for Australian economic performance.

Current and prospective challenges

A number of factors threaten the continued superior performance of the Victorian economy. Demographic change over the next quarter century will place increased pressure on the workforce.

Over the next four decades, the proportion of Victorians aged over 65 is projected to double from around 13 per cent to 25 per cent. Over the same period, if current participation rates for men and women at each age level stay as they are, aggregate participation would fall from about 65 per cent to 56 per cent. That is, the proportion of people over the age of 15 who are working would fall by about 9 percentage points. Around approximately one-third of this fall will occur within the next decade. In this circumstance, sustaining the government supplied support services for those not in paid work would require considerably increased taxation.

The recent emergence of the so-called BRIC economies of Brazil, Russia, India and China presents threats and opportunities; while at the same time the dividend from earlier reforms is declining.

China has had one of the fastest growing economies over the last decade. With a current population of over 1.3 billion, China presents some very great opportunities for Victorian producers. However, the size and growth of the Chinese economy has the potential to impose powerful competitive pressures on Victorian producers. India is also a very large economy with a high growth rate and the potential to have a very significant impact on the Victorian economy. Together, the impact of growth of these two countries alone is likely to significantly change the industrial structure and consequently the demand for skills in Victoria.

The reforms of the mid 1980s and 1990s enabled the Victorian economy to adapt quickly and to grow. The growth increased average standards of living. However, recent measures of productivity suggest that the dividends from these earlier reforms are petering out. Future growth and consequent capacity to raise living standards for all Victorians will require a new round of reforms.

Development of the reform agenda

The looming prospect of population ageing, and a growing awareness of its longer term economic and fiscal implications, have been major drivers behind the development of a third wave of reform. The Commonwealth Government's

Intergenerational Report, an attachment to the 2002-03 Commonwealth Budget, suggested that, unless policies were introduced to meet the consequences of the ageing of the population, the Commonwealth Government would face a budget deficit in the order of 5 per cent by 2041-42. The *Intergenerational Report* was followed by *Shaping a Prosperous Future*, a complementary analysis by the Victorian Department of Treasury and Finance of the prospects for the Victorian Government as a consequence of the ageing of the population. *Shaping a Prosperous Future* indicated that the Victorian Government could face a government budget deficit of up to 4 per cent by 2041-42 as a result of population ageing.

The interaction of State and Commonwealth jurisdictions and their exposure to deficits as a consequence of ageing was further examined by the Victorian Government it its submission to a research inquiry of the Productivity Commission. The Victorian submission, entitled *Preparing for Victoria's Future: Challenges and Opportunities in an Ageing Population,* indicated a potential combined state and Commonwealth deficit of around 7 per cent, with the shares between the jurisdictions dependent on the extent of Commonwealth Government provision of specific purpose payments. The Victorian findings were subsequently confirmed by the Productivity Commission (*Economic Implications of an Ageing Population*, March 2005).

The Victorian studies into the challenges arising from population ageing led to the development of a reform agenda based on the demonstrated importance of an agenda to improve productivity and at least maintain participation rates.

Victoria further pursued a leadership role in the development of a reform agenda at the June 2005 meeting of the Council of Australian Governments (COAG). The Victorian proposals, later outlined in *A Third Wave of National Reform: A New National Reform Initiative for COAG,* call on the Commonwealth, State and Territory leaders to develop and agree to an ambitious reform agenda.

The reforms proposed can be classified into two broad areas. The first area concerns continuing effort to build competitiveness of our businesses, and includes reforms to do with regulation and infrastructure. The second area concerns building the capabilities of our people, and includes reforms in health, education and training and work incentives.

Preliminary modelling by the Department of Treasury and Finance suggests that reforms in relation to the business environment can deliver potentially large gains. For instance, further enhancing and developing the reforms of the NCP to enable a more integrated electricity market, a more efficient land transport system, more effective and active markets in water, and reductions in compliance burden could lead to a 1.5 per cent increase in GDP by 2015. However, greater gains may be achieved by extending the scope to the development of human capital. This preliminary modelling indicates that a broad agenda could raise GDP by 6.1 per cent by 2015. About two-thirds of this growth is estimated to arise from maintaining the participation rate as the population ages, with productivity improvement contributing the remainder.

VICTORIA'S REFORM AGENDA

Continuing to promote business competitiveness

Under the NCP, Victoria has made, and is continuing to make, substantial reforms to promote business competitiveness. There are two main areas of further work: reduction of costs to business from government regulation, and improvements from 'Third Wave' government infrastructure prioritisation and investment.

Regulation

While regulation is a useful tool to achieve government policy, in many instances there may be unintended consequences. Regulations involve compliance costs, can reduce productivity by distorting consumption and investment decisions or by locking in inefficient production processes, and can constrain labour force participation.

Monitoring and checking the effects of regulations is an important role of government. In July 2004, the Victorian Government established the Victorian Competition and Efficiency Commission to undertake this role. The Victorian Competition and Efficiency Commission advises the Government on business regulation reform and identifies opportunities to improve Victoria's competitive position. It has three avenues of activity: the review of regulatory impact statements and provision of advice on the economic impact of new legislation; undertaking inquiries referred to it by the Victorian Government; and operating Victoria's competitive neutrality unit.

While the rigorous assessment of regulatory proposals will reduce the unintended consequences of government regulation, there remains scope for further regulatory reform. Victoria has advocated a systematic approach towards measuring the costs of existing and new regulation, with the aim of reducing those costs. Victoria has called on governments to agree to a target for red tape reduction.

Infrastructure

Efficient provision and use of public infrastructure are critical to sustaining business competitiveness. Appropriate and timely public investment in the transport system, water, energy and communications is needed to sustain and develop the competitiveness of the private sector. In addition, improvements in provision of these services to households directly increases standards of living. The challenge for government is to balance competing demands for infrastructure spending.

Lack of clarity in regard to jurisdictional boundaries between the states, the Commonwealth and local government has hindered development in many areas of public infrastructure. To improve infrastructure, governments must work together to:

- reach agreement on a set of national corridor priorities;
- broaden *AusLink* to encompass gateway to gateway corridors;

- address the gaps in energy and water pricing agendas;
- improve resource use efficiency;
- facilitate efficient financing of infrastructure; and
- develop timely and efficient approval processes.

Building human capital

Earlier waves of economic reform may be characterised as changes to institutional arrangements and their structures, whereas a large part of the new wave of reform is focused on retaining and building on the past reforms, while building the skills and capabilities of people our human capital.

In this context, the proposed broad reform agenda Victoria is advocating comprises:

- further developing the competitiveness of Australian businesses by completing legislative reviews, reducing red tape and building world-class economic infrastructure. This will support our businesses to participate and succeed in the global economy;
- giving focus to our health system to improve its efficiency and effectiveness, while at the same time improving the health and wellbeing of the population;
- encouraging and supporting people of all ages to achieve more educationally in ways now needed to more fully participate in the economy; and
- removing disincentives and barriers to labour force participation, thereby encouraging all people to make the best use of their capabilities.

Health

In health, the greatest opportunities to deliver improvements in outcomes are through a focus on reducing the incidence of chronic disease. The most effective approach in the in the medium to long term is through a greater focus on prevention; patient centred care; and improved productivity and efficiency of the health system.

The Department of Human Services has estimated that some $1 billion of income is lost by 25–64 year old Victorians per year due to poor health associated with smoking, obesity and high blood pressure. This demonstrates the potentially large benefits from a focus on reducing risk factors associated with chronic disease and cancer.

Achieving a more integrated, seamless and rational delivery and funding of health care with a focus on patients, offers an important opportunity to improve health outcomes, while at the same time contributing greatly to the agenda of improved productivity and participation.

Improving the efficiency of health resources may be achieved by improving the incentive structure in which health services are delivered. Reforms include measures to provide incentives for consumers to recognise the resource costs of their decisions; reforms which aim to reduce duplication of services between the States and the Commonwealth; a national scheme for health practitioner regulation; and greater integration across health service providers, though the better use of e-health to improve quality care.

Education and training

Over recent decades, there have been large increases in the average length of formal education and increases in the level of qualification required to obtain high paid work. Studies show that increasing years of formal education at school, at university and in the vocational education and training (VET) sector all produce large rates of return to students and society. Economic growth has also been closely associated with increases in formal education.

A systematic approach to education requires a more adaptable environment associated with appropriate community attitudes towards life-long learning. Reform is required for the very young, those of school age, those contemplating post-school education, and those in the workforce.

School-based education should entrench a capacity and propensity to learn, and every young person should be offered better choices to support a successful transition from school to work or further study. The negative labour market consequences of leaving school early are both immediate and persistent.

While Victorian retention rates to year 12 or equivalent have risen dramatically in recent decades, and are currently the highest among the States, completion rates for some groups are discernibly lower. These groups include students from low socio-economic backgrounds, boys, students in rural and remote areas and Indigenous Victorians. These outcomes are confirmed by international comparative tests which show that, while Victorian students perform well on average, there is a large variation in performance.

Current low rates of unemployment and a strong economy have led to an emerging skills shortage. The VET system has the potential to meet any skills gap and to provide life-long learning opportunities for those seeking them. However, the responsiveness of the VET system could be improved, for example by better aligning private and public costs and benefits. More broadly, the VET system needs to accommodate a more diverse student base by providing a wider range of pathways connecting schools with higher education and work. Training also needs to be delivered in the style and at the time and place that suit students and business.

Work incentives

Raising age and gender specific participation rates is likely to become a major priority for governments over the next decade. Victorian participation rates for older workers, sole parents and those with low skills are below those of leading OECD countries. Cultural norms are important determinants of participation rates, but a key factor under the influence of government is the incentives facing potential workers.

Work incentives are shaped by the interaction of the wages and conditions on offer, the tax and welfare system, and the disincentives created by regulatory and other barriers to work. The interaction of the personal income tax and welfare systems fails to encourage and reward work. Incentives should apply both to getting a job and to increasing hours of work for those who do.

While the major tool of influence, the tax and transfer system, is in the control of the Commonwealth Government, state governments have a very important role in shaping the work environment. This is achieved through development of the regulatory environment, by promoting appropriate attitudes to work and the interaction with family and other responsibilities, and through its role as an exemplary employer.

IMPLEMENTING REFORM

The Victorian Government is implementing its proposals for a third wave of reform on two fronts. First, it is undertaking reforms in its own jurisdiction and, second, it is seeking a national approach for reform with the Commonwealth and the other State and Territory governments.

The Victorian Government's recent record on reform is outlined in the Economic Reform chapter of its 2005-06 Budget Papers (see Budget Paper No. 2 *Strategy and Outlook*). Most notably, Victorian reform has included a leading role in developing competition and regulation policy, large reductions in business costs, and a dramatic increase in infrastructure investment including the development of public-private partnerships.

The national approach is being pursued through the processes of COAG. As an equal partnership of Australian governments, COAG will have primary responsibility for the strategic direction of the new national reform initiative. COAG will further consider the approach proposed by Victoria in the lead-up to its next meeting in February 2006.

The success of the reform proposal will depend on governments agreeing to a common set of objectives, the establishment of transparent processes for monitoring progress, and appropriate financial incentives for all governments to actively pursue reform.

CHAPTER 5: STATEMENT OF RISKS

- The budget projections are sensitive to a number of upside and downside risks (both economic and fiscal) and contingent assets and liabilities.
- The major risks to the Victorian economic projections include higher interest rates, rising oil prices and movements in the Australian dollar.
- Contingency provisions within the budget provide general protection against fiscal risks, including increased demand for government services.
- A number of contingent assets and liabilities have been identified, in particular relating to the public transport rail agreements.

This chapter provides a discussion of the risks to Victoria's budget position. These risks include economic risks, incorporating an analysis of the sensitivity of the budget operating surplus to macroeconomic shocks, and fiscal risks.

ECONOMIC RISKS

The main risks to the Victorian economic projections stem from prospective financial market developments, including movements in interest rates, the Australian dollar and the price of crude oil. In addition, a strong labour market, and reports of skilled labour shortages, have the potential to contribute to higher wages and interest rates.

Interest rates were last changed in March 2005, when the Reserve Bank increased the cash rate to 5.5 per cent. Despite earlier signals that policy would be tightened again, rates have remained steady, as a slowing in demand growth has helped offset pressures from other sources such as rising oil and raw materials prices. Nevertheless, with oil and commodity prices at persistently high levels, and wages edging higher, financial markets expect that a further modest increase in interest rates is likely. A larger adjustment would place some pressure on the medium-term growth forecasts.

The price of crude oil has increased further over the past six months, due to strong global demand for oil and bulk commodities more generally. Financial markets expect the oil price to remain broadly steady over the coming year. The spike in oil prices has already produced an increase in producer and consumer inflation, although underlying inflation pressures are contained at present. If the oil price rises further, this could have some effect on both the growth and inflation projections.

The United States economy is continuing to grow at a solid pace, although higher interest rates are likely to contribute to more moderate growth outcomes over the coming year. A key risk to the US outlook is emerging inflation pressures, due largely to rising oil prices. If these pressures result in higher interest rates in the US than are currently anticipated, this could have implications for the global economic outlook. Weaker growth in Victoria's major trading partners would affect the projections for exports and economic growth.

The Australian labour market remains fairly strong; the unemployment rate is around a 30-year low; and there are reports of skilled labour shortages in certain industries. There is a risk that the tight labour market could result in increased pressure on wages, which are already edging higher. Such a scenario could put some upward pressure on interest rates, which would have negative implications for the growth forecasts.

The Australian dollar continues to trade at high levels, although the currency is well below the peaks (approaching US$0.80) recorded earlier this year. The strength in the currency reflects Australia's rising terms of trade and relatively high interest rates, although the differential between Australian and US cash rates has narrowed sharply over the past year. While a positive for inflation, the high exchange rate has put pressure on the State's exporters and those firms exposed to import competition. If the currency were to renew its upward trend, these pressures would be exacerbated. In contrast, if interest rate differentials were to narrow further than expected, and if commodity prices begin to weaken, the Australian dollar would likely depreciate. This would provide some support to the State's exporters, although it could potentially place some pressure on the estimates for inflation.

Sensitivity analysis

The sensitivity analysis indicates the risk associated with forecasts or projections of selected economic and financial variables by estimating the impact on revenue, expenses and the net result from transactions. The major variables that affect Victoria's net result from transactions are economic growth, employment, prices, wages, interest rates and volatility in asset markets.

To assess sensitivity to change, the level of the economic indicator in each case is permanently increased by one percentage point in the first year above the forecast growth rate and then allowed to grow at the forecast rate. It is assumed during the analysis of each indicator that all other indicators follow their forecast growth rates.

Table 5.1: Impact on the general government net result from transactions of a one percentage point increase in selected economic indicators in 2005-06[(a)(b)]

($ million)

	2005-06 Estimate	*2006-07 Estimate*	*2007-08 Estimate*	*2008-09 Estimate*
GSP				
Taxes, regulatory fees and fines	34	36	36	38
Other income [(c)]	99	111	123	135
Superannuation expenses	..	..	..	..
Other expenses	..	1	1	2
Net result from transactions	**133**	**146**	**158**	**172**
Superannuation - actuarial gains (losses)	..	..	..	..
Net result	**133**	**146**	**158**	**172**
Employment				
Taxes, regulatory fees and fines	33	34	36	38
Other income [(c)]	1	3	5	7
Superannuation expenses	..	..	..	..
Other expenses	..	..	..	..
Net result from transactions	**34**	**37**	**41**	**44**
Superannuation - actuarial gains (losses)	..	..	..	..
Net result	**34**	**37**	**41**	**44**
Consumer prices				
Taxes, regulatory fees and fines	44	46	47	49
Other income [(c)]	163	175	179	187
Superannuation expenses	..	6	6	8
Other expenses	39	184	190	195
Net result from transactions	**168**	**31**	**30**	**33**
Superannuation - actuarial gains (losses)	-120	..	..	..
Net result	**48**	**31**	**30**	**33**
Average weekly earnings				
Taxes, regulatory fees and fines	33	34	36	37
Other income [(c)]	-14	-12	3	5
Superannuation expenses	..	18	18	19
Other expenses[(d)]	..	..	..	..
Net result from transactions	**19**	**4**	**21**	**23**
Superannuation - actuarial gains (losses)	-167	..	..	..
Net result	**-148**	**4**	**21**	**23**
Domestic share prices				
Taxes, regulatory fees and fines	..	..	..	..
Other income [(c)]	5	5	1	1
Superannuation expenses	..	-3	-3	-3
Other expenses	..	..	..	..
Net result from transactions	**5**	**8**	**4**	**4**
Superannuation - actuarial gains (losses)	52	..	..	..
Net result	**57**	**8**	**4**	**4**

Table 5.1: Impact on the general government net result from transactions of a one percentage point increase in selected economic indicators in 2005-06[(a)(b)] (continued)

($ million)

	2005-06 Estimate	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Overseas share prices [(f)]				
Taxes, regulatory fees and fines	..	..	..	..
Other income [(c)]	4	4	..	..
Superannuation expenses	..	-2	-2	-2
Other expenses	..	..	..	..
Net result from transactions	**4**	**6**	**3**	**3**
Superannuation - actuarial gains (losses)	33	..	..	..
Net result	**36**	**6**	**3**	**3**
Property prices				
Taxes, regulatory fees and fines	31	31	46	47
Other income [(c)]	2	3	5	8
Superannuation expenses	..	-1	-1	-1
Other expenses	..	..	..	..
Net result from transactions	**33**	**35**	**52**	**56**
Superannuation - actuarial gains (losses)	9	..	..	..
Net result	**42**	**35**	**52**	**56**
Property volumes				
Taxes, regulatory fees and fines	22	22	23	23
Other income [(c)]	2	3	3	5
Superannuation expenses	..	..	..	..
Other expenses	..	..	..	..
Net result from transactions	**24**	**25**	**26**	**28**
Superannuation - actuarial gains (losses)	..	..	..	..
Net result	**24**	**25**	**26**	**28**
Interest rates [(e)]				
Taxes, regulatory fees and fines	..	..	..	..
Other income [(c)]	78	80	40	43
Superannuation expenses	..	5	17	29
Other expenses	1	5	9	13
Net result from transactions	**77**	**70**	**16**	**1**
Superannuation - actuarial gains (losses)	2 856	..	..	..
Net result	**2 933**	**70**	**16**	**1**

Source: Department of Treasury and Finance

Notes:

(a) A positive number for taxes, regulatory fees and fines, and other income denotes an increase in revenue. A positive number for superannuation expenses and other expenses denotes an increase in expenses (and hence a reduction in the net result from transactions and net result). A positive number for the net result from transactions and net result denotes an improvement. Numbers may not balance due to rounding.

(b) An equivalent one percentage point decrease in each indicator would have an opposite impact to that shown.

Notes (continued):

(c) Other income includes general and specific purpose grants, including grants for on-passing, as well as changes in dividends and income tax equivalent payments from public authorities. Dividends and income tax equivalent payments are based on an estimated dividend payout ratio. However, dividends paid by government business enterprises are determined by the Treasurer having regard to relevant commercial considerations, including reported profit/loss, operating cash flow, gearing and interest cover, capital requirements and the views of the Board and the portfolio Minister. Therefore, the actual impact on this revenue source is dependent on the current circumstances of the relevant public authority.

(d) Following the implementation of the departmental funding model, employee entitlements, included as part of other expenses, are now sensitive to changes in prices, whereas in previous years these impacts would have been identified under average weekly earnings.

(e) Assumes a one percentage point increase in the cash rate over the entire forward estimates period, resulting in a one percentage point increase in the term structure.

(f) The increase in the estimated impact of movements in overseas share prices on the net result and the net result from transactions, relative to that published in the 2005-06 Budget, reflects the correction of a spreadsheet error which had resulted in an underestimation of the value of overseas shares held by the state superannuation funds.

The Government's fiscal target, the net result from transactions, is most sensitive to economic growth and property markets. The net result (which also takes into account the impact of other economic flows) is also sensitive to interest rates and share markets.

The sensitivity analysis presented in Table 5.1 presents the sensitivity of both the net result from transactions and the net result to selected economic and financial indicators.

Sensitivity to economic growth

A 1 per cent increase in gross state product (GSP) would improve both the net result from transactions and the net result by $133 million in 2005-06, rising to $172 million in 2008-09. This primarily reflects higher GST grant revenue and taxation revenue.

Sensitivity to prices

A 1 per cent increase in consumer prices is expected to increase the net result from transactions by $168 million in 2005-06. This is the result of higher GST and other Commonwealth revenue, as well as higher taxation revenue. The higher revenue is partly offset by a higher cost of supplies and services, and some increases in outlays on grants and transfers.

The increase in consumer prices would also result in an actuarial-based increase in superannuation liabilities of $120 million in 2005-06. This would reduce the improvement in the net result to $48 million in 2005-06. The higher superannuation liabilities will increase the superannuation expense in the remaining forward years. In accordance with the departmental funding model, while higher prices will have no impact in the budget year, they will flow through into increased output funding for departmental expenses in the forward years, resulting in an impact on the net result from transactions and the net result of $33 million by 2008-09.

Sensitivity to domestic and overseas share prices

An increase in domestic share prices of 1 per cent would lead to an improvement in the net result from transactions of $5 million in 2005-06 through increased Transport Accident Commission dividends. The net result will increase by $57 million with an associated increase in superannuation fund assets. Over the remaining forward estimates, the net result from transactions and net result will improve by approximately $4 million with additional Transport Accident Commission dividends combining with a reduction in superannuation expenses. Similarly, an increase in overseas share prices will increase the net result from transactions by $4 million in 2005-06, with a gain on superannuation fund assets increasing the net result by $36 million. In the remaining forward years, there will be a small improvement in the net result from transactions and net result of around $1 million.

Sensitivity to property prices

A 1 per cent increase in property prices is expected to result in a $33 million increase in the net result from transactions in 2005-06, primarily reflecting additional conveyancing duty. A gain on superannuation fund assets held as property will result in a total improvement in the net result of $42 million. As higher property prices flow through to higher land tax collections in later years, the improvement in the net result from transactions and the net result would rise by $56 million by 2008-09.

Sensitivity to interest rates

A 1 per cent increase in interest rates would result in higher public authority income and interest receipts, resulting in an improvement in the net result from transactions of $77 million in 2005-06. At the same time, the increase in interest rates generates a revaluation of superannuation fund liabilities of $2.86 billion in 2005-06, improving the net result by $2.93 billion. As the higher public authority income ceases after the first two years, and superannuation expenses grow over subsequent forward years, the improvement in both the net result from transactions and the net result declines to $1 million by 2008-09.

FISCAL RISKS

Expenditure risks

Following the introduction of the departmental funding model from 2004-05, departments now need to plan for, and manage, all costs associated with delivering services. There are, however, several general risks such as unforeseen changes in the size and structure of the Victorian population, which can affect the expenditure and revenue outlook. These risks can be classified into those affecting all government departments and those that are department specific.

The main risks to specific departmental expenditures relate to growth in demand for key services, the modernisation of assets, and government responses to unforeseen events. Examples of these types of impacts could include pressures related to the maintenance of assets, such as government schools and TAFE institutes, and funding required in relation to natural disaster relief.

The 2005-06 Budget and forward estimates include a contingency provision to allow for the likelihood that some of these department-specific and government-wide expenditure risks will be realised during the budget year or over the course of the forward years. The contingency provision includes a general allowance for:

- growth in Victoria's population, and consequent derived demand for government services;
- an allowance for depreciation expenditure that would be associated with new asset investments funded from the unallocated capital provision (subject to government approval); and
- other expenditure risks, which are unforeseen or not able to be quantified at the time of construction of the budget estimates.

In addition, the budget estimates include a contingency from 2007-08 that acknowledges funding for a number of initiatives will conclude in 2006-07 or following years. A provision is provided on the basis that the Government may endorse a number of these initiatives to continue or be replaced to meet service delivery priorities.

The inclusion of an operating contingency provision in the budget estimates mitigates the potential impact of expenditure risks on the overall budget position. Realised expenditure risks will only impact on total expenditure and the annual budget position to the extent that they cannot be accommodated within the contingency provision built into the budget estimates.

In addition to the operating contingency, the budget estimates include an unallocated capital provision to provide capacity for future asset investment funding requirements. With a capital program the size of that funded by the Government, there are always likely to be variations in actual costs for individual asset investment projects against budget. However, the forward estimates assume that capital cost pressures are managed within the existing forward estimates with no budget impact. Management of capital cost pressures may occur in one of three ways:

- the reallocation of resourcing within departments' global capital budgets (reflecting the likelihood that cost over-runs on some projects will be offset by cost under-runs in other areas);
- re-scoping a project to fit within funding parameters (subject to government approval); and/or
- funding from the unallocated capital funding set aside in the forward estimates (subject to government approval).

Significant events that could represent a call on the operating contingency or unallocated capital funding and/or impact on total budget expenditure forecasts are detailed below.

Insurance exposures

The availability and affordability of commercial insurance has improved during the past year, although difficulties remain for particular clients and risks, particularly professional indemnity insurance for some highly specialised professions. Apart from heritage and tourist railways, which are covered under the State's broad Government Rail Insurance Program, the State no longer provides cover for tourism ventures, which have reverted to commercial insurance.

Pressures on private sector medical indemnity premiums have also eased, but there is still a risk that increasing medical costs and lack of availability of private doctors in some regions may result in the State assuming larger numbers of high risk medical procedures. The possibility of such movement, together with the impact of claims that arise from current levels of public medical services, means that there is a continuing need to monitor closely the State's medical indemnity liabilities and expenses.

As set out in the contingent liabilities section, as the insurer for the Victorian general government sector, the Victorian Managed Insurance Authority (VMIA) insures any additional risks assumed by the general government sector. It does so either explicitly through indemnities provided to non-government bodies, or implicitly through transfer of activities from private sector to general government sector service providers. However, the State continues to bear directly the risks of losses arising from events for which VMIA does not provide insurance, such as terrorist attacks.

Revenue risks

Commonwealth grants

Commonwealth grants are a major source of revenue for the Victorian Government, worth approximately $13.5 billion in 2004-05. Commonwealth grants include general purpose grants (GST grants and National Competition Policy payments) and specific purpose payments (SPPs).

The level of SPPs is determined by the policies of the Commonwealth Government, and is published on an annual basis in the Commonwealth Budget Papers. The level of general purpose grants, and in particular GST grants, is affected by the general level of activity in the Australian economy and the GST revenue sharing relativities calculated by the Commonwealth Grants Commission (CGC).

The Commonwealth has indicated that it will release its *2005-06 Mid-year Economic and Fiscal Outlook* by the end of December 2005. This will outline the Commonwealth Government's expectations on Australia-wide economic activity, and will include any revisions to the expected level of GST grants throughout the forward estimates period. The CGC provides annual updates of its GST revenue sharing relativities in February, which are subject to the approval of the Commonwealth Treasurer at the Ministerial Council for Commonwealth-State Financial Relations in March.

Legal dispute between the Valuer-General and the Port of Melbourne

The Valuer-General is currently in dispute with the Port of Melbourne regarding the interpretation of the term 'works relating to a port' in the *Valuation of Land Act* 1960. Because the Act excludes works relating to a port from the valuation of port land, it has the potential to reduce the land tax payable by the Port of Melbourne if the term is interpreted in its broadest possible sense. The matter remains before the Supreme Court.

CONTINGENT ASSETS AND LIABILITIES

Contingent assets

Contingent assets are either:

- possible assets that arise from past events where the probability of existence of a possible asset is considered higher than remote, but which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
- assets that fail either or both of the criteria for recognition as assets. These are:
  - assets for which it is not probable that the future economic benefits embodied in them will eventuate; and/or
  - assets that do not possess a cost or other value that can be measured reliably.

These can be classified into either quantifiable, where the potential economic benefit is known, or non-quantifiable.

Quantifiable contingent assets

Table 5.2: Quantifiable contingent assets

($ million)

	As at June 2004	*Estimate for June 2005* [(a)]
Guarantees, Indemnities	0.5	1.4
Potential early termination of contractual arrangements [(b)]	100.0	100.0
Legal proceedings and disputes	0.1	1.4
Other [(c)]	65.1	134.2
Total contingent assets	**165.7**	**237.0**

Source: Department of Treasury and Finance

Notes:

(a) There have been no material changes to quantifiable contingent assets since last reported in the 2004-05 Financial Report for the State of Victoria.

(b) Included under 'potential early termination of contractual arrangements' are any additional costs arising to the Director of Public Transport on early termination or expiry of the public transport partnership agreements. The Franchisee must indemnify the Director for any losses, damages or costs incurred by him as a result of the termination. If the Franchisee does not do so, the Director has the right to draw on the Franchisee's performance bonds totalling $100 million for the amount of losses, damages or costs.

(c) 'Other' includes Transurban City Link Limited and EastLink project as described below.

Transurban City Link

A dispute exists between Transurban City Link Limited and the Australian Taxation Office (ATO) in respect of the deductibility for taxation purposes of concession fees payable by Transurban to the Victorian Government. The amount in dispute is $39.2 million. The Federal Court had previously found against Transurban in this matter; however, a recent appeal by Transurban to the full bench of the Federal Court was determined in its favour in October 2004. The ATO has recently announced that it is seeking leave to appeal.

The nominal value of concession fee notes held by the Victorian Government as at 30 June 2005 is $586.4 million (assuming Transurban is successful and the tax deduction is allowed) or $547.2 million (if the ATO is successful and the tax deduction is not allowed).

EastLink

On 14 October 2004, the State entered into a concession deed with ConnectEast to design, construct, finance and operate EastLink (formerly known as the Mitcham Frankston Project). Various performance bonds provided under the concession deed can be drawn by the State in circumstances where the concessionaire (ConnectEast) or one of its contractors fails to meet its obligations. These bonds include a construction bond ($87 million) and an operation phase bond ($5 million).

Non-quantifiable contingent assets

Public transport partnership agreements

On 19 February 2004, the Director of Public Transport, on behalf of the Crown, entered into contractual arrangements with Connex and Yarra Trams to operate rail transport services in the State. The following paragraphs summarise the major contingent assets arising from those arrangements.

Profit sharing: The Director is entitled to receive payment from Connex and Yarra Trams should Franchisee profits exceed defined thresholds.

Operational performance regime: The operational performance regime entitles the Director to receive penalty payments if Connex and Yarra Trams fail to meet set punctuality and reliability performance targets.

Special event payments: The Director is entitled to receive payments at a set rate for special event kilometres short of a defined contractual limit.

Newport Depot: The annual 'Franchise Sum' payable to Connex is to be reduced by the value of the Newport lease rental at the expiry or early surrender of the lease.

OneLink Service Contract: The Director will be paid all compensation payments under the OneLink Service Contract for failure to meet required performance standards.

Employee entitlements: Connex and Yarra Trams are required to manage employee entitlements to agreed forecast amounts.

The Director is entitled to receive payments where the provision for employee entitlements (excluding long service leave) is greater than an agreed forecast amount, and actual long service leave payments are less than an agreed forecast amount.

Adjustment event: The Director is obliged to decrease the fixed monthly 'Franchise Sum' payable as a result of a defined adjustment event occurring, which has a fundamental impact.

Compensable enhancement claim for improving the flow on the Westgate Freeway

The Melbourne City Link Concession Deed contains compensable enhancement provisions that enable the Victorian Government to claim 50 per cent of additional revenue derived by City Melbourne Link Limited as a result of certain events that particularly benefit City Link including changes to the adjoining road network.

On 20 May 2005, the Victorian Government lodged a compensable enhancement claim relating to works to improve the traffic flow on the West Gate Freeway between Lorimer and Montague Streets.

EastLink

As indicated above, on 14 October 2004, the State entered into a concession deed with ConnectEast to design, construct, finance and operate EastLink. The following paragraphs summarise the major non-quantifiable contingent assets arising from the concession deed.

Additional lease rental

The concession deed sets out circumstances where the State is entitled to receive, by way of increased lease rentals, a share of revenue that the concessionaire receives over an agreed base sum. The concessionaire's ability to make these payments also depends on other cash flow criteria at the time.

Compensable enhancements

The concession deed sets out circumstances where the State may receive compensation for providing a measurable benefit to the concessionaire by the taking of certain actions. Primarily, these are enhancements to the road network that generate incremental traffic for the concessionaire over and above those road network enhancements which have already been identified in the concession deed and which have been factored in to the current tolling structure. Any compensation receivable would be net of any negative impacts caused by the State by the taking of certain actions (e.g. negative impact on traffic levels).

Refinance benefits

In the event that the concessionaire is able to achieve future incremental refinancing benefits, over and above the refinancing assumptions included in the final bid, over the course of the concession, the State would share in any gain subject to certain conditions.

Contingent liabilities

Contingent liabilities are either:

- possible liabilities that arise from past events where the probability of existence of a possible liability is considered higher than remote, but which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
- provisions that fail either or both of the criteria for recognition as liabilities. These are:
  - provisions for which it is not probable that the future sacrifice of economic benefits will be required; and/or
  - provisions the amount of which cannot be measured reliably.

As with contingent assets, contingent liabilities are also classified as either quantifiable or non-quantifiable.

Quantifiable contingent liabilities

Table 5.3: Quantifiable contingent liabilities

($ million)

	As at June 2004	Estimate for June 2005 [(a)]
Guarantees, Indemnities	272.5	400.6
Potential early termination of contractual arrangements [(b)]	622.4	633.7
Legal proceedings and disputes	212.2	281.7
Other	12.6	26.0
Non-general government debt [(c)]	2881.4	3115.2
Total contingent liabilities	**4001.1**	**4457.2**

Source: Department of Treasury and Finance

Notes:

(a) There have been no material changes to quantifiable contingent liabilities since last reported in the 2004-05 Financial Report for the State of Victoria.

(b) Under 'potential early termination of contractual arrangements' is a contractual agreement of $633.7 million ($622.4 million for 2004) relating to the cost of correctional services beyond the current contract period. The State has the option to retender for the provision of correctional services every three years, after the initial five year period for each contract.

(c) Represents guarantees for loans made by the general government sector to agencies in the public non-financial corporations sector, primarily the water entities and other non-general government sector entities.

Non-quantifiable contingent liabilities

A number of potential obligations, which are non-quantifiable at this time, have been recognised by the Government arising from:

- indemnities provided in relation to transactions, including financial arrangements and consultancy services, as well as for directors and administrators;
- performance guarantees, warranties, letters of comfort, and the like;
- deeds in respect of certain obligations; and
- unclaimed moneys which may be subject to future claims by the general public against the State.

Asset sales

Potential exposures are associated with the sale of a number of assets and services where the purchaser was provided with various indemnities and warranties.

Royal Melbourne Showgrounds

A contingent liability exists relative to any claims which may be made against the Showgrounds Nominees Pty Ltd arising from joint venture dealings as outlined in the Development and Operations Agreement for the Royal Melbourne Showgrounds.

An undertaking has been given by the joint venture parties to meet the unindexed service fees payable to the Concessionaire (Developer) under the Development and Operations Agreement as and when they fall due.

Under the State Support Deed – Core Land, the State undertakes to ensure the performance of the payment obligations in favour of the Concessionaire and the performance of the joint venture financial obligations in favour of the security trustee.

Under the State Commitment to Royal Agricultural Society (RAS), the State has agreed to support certain obligations of RAS that may arise out of the Joint Venture Agreement. In accordance with the terms, in the State Commitment to RAS, the State will pay (in the form of a loan) the amount requested by RAS. If any outstanding loan amount remains unpaid at the date, which is 25 years after the commencement of the operation term under the Development and Operation Agreement, RAS will be obliged to satisfy and discharge each such outstanding loan amount. This may take the form of the transfer to the State of the whole of the RAS' participating interest in the joint venture.

Melbourne Cricket Ground redevelopment

On 15 August 2002, the State entered into agreements to support the redevelopment of the Melbourne Cricket Ground (MCG) for the Melbourne 2006 Commonwealth Games. This is in addition to a commitment to provide grants of $77 million towards the capital cost of the redevelopment, and a guarantee of up to $360 million in respect of a Treasury Corporation of Victoria loan facility to the Melbourne Cricket Club (MCC).

These agreements include:

- indemnities to the MCG Trust and the MCC in the event that there should be insufficient trading surpluses to meet scheduled debt servicing and repayments, or if the total project construction cost exceeds $450 million;
- agreement for compensation to the Australian Football League (AFL) as a result of the hosting of the Melbourne 2006 Commonwealth Games. The amount of compensation will be finalised following the completion of the 2006 AFL draw. All compensation claims will be calculated in accordance with an agreed compensation formula; and
- previously provided indemnities to the MCC and MCG Trust in the context of the 1990 Great Southern Stand development, which have been reincorporated into the contractual arrangements of the Northern Stand redevelopment, under greater accountability and responsibility of the MCC to the MCG Trust.

Public transport rail partnership agreements

The Director of Public Transport, on behalf of the Crown, entered into new partnership contractual arrangements with franchisees to operate rail transport services in the State, operative from 18 April 2004. The following summarises the major contingent liabilities arising from those arrangements.

Contingent liabilities arising during the agreement period

There are a number of contingent liabilities arising from the new Partnership Agreements between the Director of Public Transport and Connex and Yarra Trams, which were signed on 19 February 2004.

These possible liabilities refer to payments to be made by the Director of Public Transport to Connex and Yarra Trams should certain events occur:

Operational performance regime: The operational performance regime obliges the Director to make incentive payments for franchisees exceeding set punctuality and reliability performance targets.

Special event payments: The Director is obliged to make payments at a set rate for special event kilometres operated above a defined contractual limit.

Farebox risk sharing: The Director is obliged to make payments should farebox receipts fall below defined thresholds.

Service growth incentive: The Director is obliged to make payment for certain additional services introduced to meet service standards.

Commonwealth Games revenue guarantee payments: The Director is obliged to make a top-up payment should, as a result of Commonwealth Games, farebox fall below a projected amount based on the prior period's farebox and patronage growth.

Commonwealth Games kilometre payment: The Director is obliged to make payments for additional service kilometres operated above the Master Timetable Requirements in respect of the Commonwealth Games.

New ticketing revenue guarantee payment: Franchisees have an option to elect to permanently move to a revenue guarantee payment regime should implementation matters or new ticket fare structures associated with the introduction of the new ticketing system cause a real reduction in the farebox.

The revenue guarantee payment will be based on the prior period's farebox, including an estimate for patronage growth and inflation. Under the above arrangement, the Director is liable for the difference between actual farebox received and the guaranteed revenue amount.

New ticketing system start-up: The State is obliged to pay any additional labour costs associated with training and deployment of staff in relation to the establishment of the new ticketing system.

Employee entitlements: Franchisees are required to manage employee entitlements to agreed forecast amounts. The Director is obliged to make payments where the provision for employee entitlements (excluding long service leave) is less than an agreed forecast amount, and actual long service leave payments are greater than an agreed forecast amount.

Access charge adjustment: Should the access charge regime for train rail access be reset, then the Director is obliged to make payment to the franchisee in respect of any increased cost as a result of the reset. The Director is also required to reimburse the franchisee's reasonable costs incurred in renegotiating the access charges.

Regional Fast Rail: The Director is required to meet the incremental costs incurred by Connex associated with the introduction of Regional Fast Rail.

Connex and Mainco indemnity

The Department has indemnified Connex and Mainco (including agents and contractors) against any loss caused by Regional Rail Link whilst undertaking Regional Fast Rail within the Connex network.

VicTrack and Spencer Street Station Authority indemnity: The Director indemnifies VicTrack and the Spencer Street Station Authority from any claim brought by the franchisees under the Infrastructure Lease.

Adjustment event: The Director is obliged to increase the fixed monthly franchise sum as a result of any other defined adjustment event occurring, which has a fundamental impact.

Contingent liabilities on early termination or expiry of franchise agreement

Franchise assets: To maintain continuity of services, the Director at early termination or expiry of the franchise agreement will:

- for new rolling stock – either acquire the new rolling stock at predetermined values, or have the lease payment obligations transferred to the Director or a successor franchise; and
- for franchise assets – either purchase the assets or have the assets transferred to the successor.

Unfunded superannuation: At the early termination or expiry of the contract, the Director will assume any unfunded superannuation amounts (apart from contributions the franchisee is required to pay over the contract term) to the extent that the State becomes the successor operator.

Contingent liabilities arising from potential changes to existing conditions

Change in Victorian law: Franchisees may make a claim against the Director for any net losses incurred as a result of a change in Victorian law which directly relates to the franchise business.

Pre-existing contamination: The Director is responsible for all costs associated with pre-existing contamination clean up. The Director also indemnifies the franchisee from and against all losses, damages, actions suits, claims, demands, costs and expenses associated with pre existing contamination.

Native Title: The Director is liable for payments of any valid compensation claim to Native Title holders made under any Native Title law in respect of the land defined in the infrastructure leases entered into with franchisees.

National Express receivership

In December 2002, the Government appointed receivers and managers to the National Express train and tram franchises, in order to protect government interest, ensure continuation of services up to the commencement of new franchise agreements, and deal with any subsequent termination issues.

The Treasurer, under the Receivership Deed of Indemnity, has agreed to indemnify the receivers for debts properly incurred by them in the course of receivership. The Treasurer has also agreed to remunerate the receivers in accordance with the rates set out in the deed.

Country Train Safety Systems

Country Train Safety Systems is the project under which the Train Protection and Warning System is being installed. The Director of Public Transport undertakes to reimburse Pacific National (Victoria) Limited (previously Freight Victoria Limited) reasonable costs and expenses related to the installation, testing and rectification and repair of the Train Protection Warning System and will indemnity Pacific National (Victoria) Limited for any loss, or cost, or liability it suffers arising from the Director's installation.

Melbourne City Link

An outstanding claim exists from Transurban City Link Limited pursuant to the Melbourne City Link Concession Deed, relating to an alleged Material Adverse Effect in respect of the construction of Wurundjeri Way. Expert determination found in favour of the State; however, the claim has now been appealed to arbitration, which is yet to proceed. VicRoads is defending this claim and is unable to assess the likelihood of success at this time.

EastLink

On 14 October 2004, the State entered into a Concession Deed with ConnectEast to design, construct, finance and operate EastLink. The major non-quantifiable contingent liability arising from the concession deed relates to the Key Risk Management Regime. The Regime relates to the occurrence of certain circumstances that may have a detrimental impact on the concessionaire's ability to achieve its forecast returns. It identifies the areas that enable the concessionaire to claim redress from the State. These may include acts of prevention, failure to support a principal road interface, changes in state law, Native Title and the environmental effects statement.

Native Title

A number of claims have been filed with the Federal Court under the *Native Title Act* 1993 that affect Victoria. While many such claims are being processed through the legal system, the Government has committed itself to resolving claims through mediation, where possible. It is not feasible at this time to quantify any future liability.

HIH Insurance

The State's quantifiable direct exposures arising from the collapse of the HIH Insurance Group are included in the liabilities shown in the financial statements of the agencies directly responsible for them (such as the Victorian WorkCover Authority and the VMIA), and are consolidated in the financial statements of the State.

The State's obligations in respect of its builders' warranty insurance rescue package are direct liabilities of the State itself. They do not form part of the liabilities of Housing Guarantee Fund Limited, which manages claims on behalf of the State.

The State also retains some unquantifiable contingent exposures arising from the collapse of the HIH Insurance Group. These contingent exposures arise primarily through the possibility that the State may be involved in litigation in which it would be entitled to recover damages from third parties. If these third parties were insured by HIH, recovery in full may not be possible.

Smelter Reduction Amount

The State Electricity Commission of Victoria (SECV) is the first defendant in a matter before the High Court of Australia commenced by summons dated 5 June 2003 in which the Australian Steel Company (Operations) Pty Ltd is the plaintiff. The plaintiff has claimed that Schedule 9A2 of the National Electricity Code, amongst other legislation, imposing a charge known as the Smelter Reduction Amount, is invalid. The plaintiff seeks reimbursement of Smelter Reduction Amounts previously paid together with interest and costs. Origin Energy Electricity Limited is a second defendant in this matter and has filed and served consequential cross claims against the SECV.

The Government discontinued the collection of the Smelter Reduction Amount from 30 June 2004.

The State of Victoria has entered into an agreement with SECV, whereby the State has fully indemnified the SECV in respect of all legal costs and any other moneys payable by the SECV in the matter. The interests of the SECV are being managed by the State of Victoria.

Melbourne 2006 Commonwealth Games

In winning the bid to host the Melbourne 2006 Commonwealth Games, the State entered into two contracts:

- the Endorsement Contract with the Australian Commonwealth Games Association; and
- the Host City Contract with the Commonwealth Games Federation.

The Organising Committee for the Commonwealth Games is the Melbourne 2006 Commonwealth Games Corporation (M2006), a statutory corporation.

Under the Endorsement Contract, the State is obliged to underwrite any shortfall between revenue and expenditure of M2006 for the organisation of the Games. Also under this contract, any remaining surplus resulting from the Games, after M2006 has discharged all financial commitments and other obligations, is to be transferred to the Association. This surplus is, in turn, required to be paid to the State to be used for the benefit of sport in Victoria.

The Host City Contract specifies the rights and obligations of M2006 in relation to organising the Games. The contract includes the commitment the State outlined in its bid document to offer travel grants to competitors and team officials attending the Games.

Ticketmaster7

On 15 July 2005, the State agreed to indemnify Ticketmaster7 for any losses, damages, costs and expenses associated with the early release of moneys associated with ticket sales for the Melbourne 2006 Commonwealth Games. The early release of moneys ensures that Melbourne 2006, the organising body of the Games, can pay costs incurred in preparation for the Games. The ordinary practice is for moneys from ticket sales to be kept in trust until the completion of the event, in case the event is cancelled, and moneys need to be refunded. Under the Indemnity, the maximum exposure is approximately $45 million, the total amount of ticket sales. As the entire Melbourne 2006 Commonwealth Games would need to be cancelled to reach this exposure, the probability of this risk occurring is very low.

Land remediation – environmental concerns

A number of Victorian government properties have been identified as potentially contaminated sites. The State does not admit any liability in respect of these sites. However, remedial expenditure may be incurred to restore the sites to an acceptable environmental standard in the event of future developments taking place.

Victorian Managed Insurance Authority – property and public liability

The VMIA was established in 1996 as a captive insurer for departments and participating bodies, predominantly in the general government sector. VMIA provides its client bodies with a range of insurance cover, including for property, public and products liability, professional indemnity and contract works. VMIA reinsures in the private market for losses above $50 million arising out of any one event, up to a maximum for each type of cover (e.g. $1 500 million for property and $750 million for public liability). The risk of losses above these reinsured levels and below $50 million is borne by the State.

Victorian Managed Insurance Authority – public healthcare insurances

VMIA insures the public health care system for a range of insurances, including medical indemnity risks. The Government has indemnified VMIA for losses on its public sector medical indemnity portfolio that exceed 120 per cent of claims estimated to be incurred in any one policy year.

Gambling/gaming licences

In 1994, the State sold a wagering licence and a gaming licence to TABCORP Holdings Limited (TABCORP) for $597 million. The *Gambling Regulation Act* 2003 requires the State to provide a refund to TABCORP in 2012 of an amount equal to the licence value of the former licences or the premium payment paid by the new licensee, whichever is the lesser. While this creates an obligation on the State to refund the licence value to TABCORP, it will be offset by the premium payment from the issue of any new licences. In 1992, a gaming operator's licence was issued to the Trustees of the Will and Estate of the late George Adams (the licensee). The *Gambling Regulation Act* 2003 entitles the licensee to be paid, at the end of its current licence period in 2012, an amount equal to the value of its current licence or the premium payment paid by the new licensee, whichever is the lesser. This entitlement is contingent on the licensee not being granted a new licence.

Builders' warranty

The builders' warranty insurance market, like other insurance markets, was affected by the 11 September 2001 terrorist attacks in the United States and adverse claims experience. In mid-April 2002, the State agreed to provide temporary (to 30 June 2002) reinsurance support to builders' warranty insurance provider Dexta Corporation, following the withdrawal of some of its commercial reinsurance support. This support was subsequently extended to 30 September 2002. The Government determined that there would be no further extension.

The State received reinsurance premiums for this participation and is required to contribute to payment of reinsured claims, as well as paying management fees. The precise timing and value of claims related payments is uncertain, as claims may be made by home owners for up to six and a half years after the arrangement ceased.

Based on Dexta's previous levels of activity, the central estimate of the State's gross exposure (i.e. before premium receipts) is not more than $6 million. While the State expects, along with the commercial reinsurers who are party to the agreement, to at least break even on these arrangements, the State retains an non-quantifiable contingent liability that claims may exceed the central estimate.

On 13 March 2002, Victoria and New South Wales jointly announced a series of reforms to builders' warranty insurance arrangements. This announcement included a commitment to provide a catastrophe fund capable of supporting claims above $10 million. Since builders' warranty insurance commenced, there have been no losses exceeding this amount by an insurer to any one builder. To meet this commitment, the two States offered reinsurance arrangements to all builders' warranty insurers covering claims in respect of any one builder exceeding $10 million, with each of the two States reinsuring claims relating to properties in that State. A reinsurance agreement giving effect to these arrangements was concluded in December 2002 (effective from 1 January 2003) with one insurer. South Australia became a party to this agreement with effect from 31 December 2004. This agreement requires the insurer to pay reinsurance premiums to the three States that are estimated to be sufficient for the States to at least break even on these arrangements. However, the State retains an non-quantifiable contingent liability for additional claims.

CHAPTER 6: ESTIMATED FINANCIAL STATEMENTS AND NOTES

The Estimated Financial Statements have been prepared in accordance with the provisions of the *Financial Management Act* 1994. This Act requires the Estimated Financial Statements to be consistent with the Financial Policy Objectives and Strategies Statement (see Chapter 1, *Financial Policy Objectives and Strategy*), and to be prepared in a manner and form determined by the Minister. Consistent with the form of the Estimated Financial Statements presented in the 2005-06 Budget Papers, these revised statements are based on Australian equivalents to International Financial Reporting Standards (A-IFRS).

The purpose of the Estimated Financial Statements is to provide updated information on the forecast financial results for the general government sector. Given the prospective nature of these statements, they reflect a number of professional judgements about the most likely operating and financial conditions for the Victorian general government sector. International developments and other risks to the national economy, from which Victoria would not be immune, may cause the general government actual result to differ from the projections.

The accompanying notes to the statements provide revised details of the material economic and other assumptions. In addition, only those specific forecast assumptions that have changed since the 2005-06 Budget have been included. A number of these assumptions are subject to inherent uncertainties, which are outside the control of the Government.

Compared with the balance sheet estimates published in the 2005-06 Budget, the opening balances as at 30 June 2005 and consequent forecast closing balances have been adjusted to reflect actual audited balances as at 30 June 2005, and have been further adjusted to reflect the adoption of A-IFRS. The original estimates were based on audited values at 30 June 2004 adjusted for estimated movements during 2004-05.

Estimated Financial Statements for the Victorian General Government Sector

Table 6.1: Estimated operating statement for the financial year ending 30 June

($ million)

	Notes	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Income from transactions						
Taxation	2	10 306.2	10 452.9	10 880.6	11 132.0	11 556.4
Fines and regulatory fees		726.9	727.1	778.2	766.8	770.1
Investment income	3	1 397.9	1 310.4	1 137.6	1 210.3	1 152.1
Grants income	4	14 262.1	14 340.0	14 868.2	15 421.6	16 042.7
Sales of goods and services		2 397.1	2 496.9	2 531.8	2 577.2	2 620.6
Fair value of assets received free of charge or for nominal consideration		22.0	22.0	..	..	160.0
Inter-sector capital asset charge		778.8	778.8	777.7	768.7	755.6
Other income		732.6	743.4	837.1	845.7	848.0
Total income from transactions		**30 623.6**	**30 871.4**	**31 811.2**	**32 722.4**	**33 905.5**
Expenses from transactions						
Employee benefits		11 201.5	11 346.6	11 670.5	12 008.4	12 352.2
Superannuation	5	1 759.3	1 754.9	1 772.3	1 773.1	1 764.0
Depreciation and amortisation	6	1 235.1	1 221.7	1 285.4	1 371.5	1 439.5
Financing costs	7	492.1	477.7	484.6	490.2	506.9
Grants and transfer payments	8	5 579.3	5 694.9	5 629.5	5 594.1	5 565.9
Supplies and services		9 991.2	10 044.1	10 651.9	11 071.7	11 758.3
Other expenses		0.4	0.4	0.4	0.4	0.4
Total expenses from transactions	**9**	**30 258.9**	**30 540.3**	**31 494.5**	**32 309.4**	**33 387.2**
Net result from transactions		**364.7**	**331.1**	**316.6**	**413.0**	**518.3**
Income/(expenses) from other economic flows						
Net gain/(loss) from disposal of physical assets		25.7	29.7	22.9	10.6	11.2
Other income from other economic flows	3	8.5	8.5	8.5	8.5	8.5
Actuarial gains/(losses) on superannuation defined benefit plans	5, 9	..	1 203.5	..	..	..
Other expenses from other economic flows	6, 9	(74.8)	(70.8)	(66.9)	(56.3)	(52.5)
Net result from other economic flows		**(40.6)**	**1 170.9**	**(35.5)**	**(37.1)**	**(32.8)**
Net result		**324.1**	**1 502.0**	**281.1**	**375.8**	**485.5**
Gain/(loss) on revaluation of properties		2 276.0	2 316.2	2 460.1	2 647.2	2 870.5
Total changes in equity other than contributions to other sectors by the State in its capacity as owner		**2 600.1**	**3 818.2**	**2 741.2**	**3 023.1**	**3 356.0**

The accompanying notes form part of these Estimated Financial Statements.

Table 6.2: Estimated balance sheet as at 30 June

	($ million) *Notes*	*2006 Revised*	*2007 Estimate*	*2008 Estimate*	*2009 Estimate*
Current assets					
Cash and cash equivalents	*16*	1 788.7	1 473.7	1 058.7	943.7
Other financial assets		1 726.7	653.8	622.0	646.0
Receivables		1 693.1	1 882.7	1 966.3	2 083.1
Prepayments		67.3	67.8	68.0	68.2
Inventories		101.9	102.5	103.1	103.6
Assets held for sale		77.8	78.8	79.8	80.8
Total current assets		**5 455.4**	**4 259.4**	**3 897.9**	**3 925.3**
Non-current assets					
Other financial assets		530.2	502.5	426.2	370.5
Receivables		327.3	340.2	365.2	389.1
Property, plant and equipment and infrastructure systems	*10, 12*	35 317.2	37 782.9	40 308.0	43 222.3
Road networks	*11, 12*	17 735.0	18 864.3	19 753.6	20 567.4
Other assets	*13*	3 965.6	4 000.6	4 047.6	4 079.5
Total non-current assets		**57 875.4**	**61 490.5**	**64 900.6**	**68 628.8**
Total assets		**63 330.8**	**65 749.8**	**68 798.4**	**72 554.1**
Current liabilities					
Payables		2 212.6	2 233.0	2 261.5	2 319.6
Interest bearing liabilities		276.9	283.0	288.2	289.5
Employee benefits	*14*	1 002.8	1 049.1	1 096.0	1 142.3
Superannuation	*5*	285.1	556.1	644.0	806.0
Other provisions		184.4	183.3	182.9	182.8
Other liabilities		345.4	351.3	357.5	363.5
Total current liabilities		**4 307.1**	**4 655.8**	**4 830.2**	**5 103.8**
Non-current liabilities					
Payables		1 080.6	962.9	844.8	730.4
Interest bearing liabilities		5 917.9	5 915.2	6 198.0	6 695.0
Employee benefits	*14*	2 451.5	2 570.8	2 647.6	2 724.9
Superannuation	*5*	14 436.7	14 507.0	14 465.3	14 236.5
Other provisions		577.5	560.6	548.8	537.8
Other liabilities		234.6	221.7	208.8	195.9
Total non-current liabilities		**24 698.8**	**24 738.2**	**24 913.4**	**25 120.4**
Total liabilities		**29 005.9**	**29 394.0**	**29 743.6**	**30 224.2**
Net assets		**34 324.9**	**36 355.8**	**39 054.8**	**42 330.0**

The accompanying notes form part of these Estimated Financial Statements.

Table 6.3: Estimated statement of cash flows for the financial year ending 30 June

($ million)

	Notes	*2005-06 Budget*	*2005-06 Revised*	*2006-07 Estimate*	*2007-08 Estimate*	*2008-09 Estimate*
Cash flows from operating activities						
Receipts						
Taxation		10 386.5	10 533.2	10 910.8	11 103.5	11 528.8
Fines and regulatory fees		628.5	636.7	685.5	684.1	692.4
Grants		14 262.1	14 340.0	14 868.5	15 421.9	16 043.0
Sale of goods and services		2 390.3	2 478.7	2 531.4	2 575.9	2 614.9
Interest received		361.6	339.6	300.7	257.4	250.8
Dividends received		699.9	723.1	514.9	553.7	463.0
Capital asset charge received		778.8	778.8	777.7	768.7	755.6
Other receipts		1 218.7	1 289.2	936.1	1 188.6	1 201.1
Total receipts		**30 726.3**	**31 119.2**	**31 525.5**	**32 553.9**	**33 549.7**
Payments						
Employee benefits		(10 955.3)	(11 100.0)	(11 504.8)	(11 884.7)	(12 228.7)
Superannuation		(1 109.9)	(1 117.4)	(1 431.0)	(1 726.9)	(1 830.8)
Interest paid		(439.0)	(432.4)	(437.4)	(443.6)	(458.2)
Grants and transfer payments		(5 649.3)	(5 764.8)	(5 702.2)	(5 681.2)	(5 652.9)
Supplies and services		(9 994.1)	(10 023.6)	(10 708.9)	(11 107.6)	(11 696.2)
Total payments		**(28 147.6)**	**(28 438.3)**	**(29 784.3)**	**(30 843.9)**	**(31 866.8)**
Net cash flows from operating activities	*15*	**2 578.6**	**2 680.9**	**1 741.2**	**1 709.9**	**1 682.8**
Cash flows from investing activities						
Purchase of property, plant and equipment	*17*	(2 529.4)	(2 589.7)	(2 599.0)	(2 415.9)	(2 362.1)
Proceeds from sale of property, plant and equipment		134.0	138.0	144.0	210.3	121.3
Net (purchase)/disposal of investments		370.2	372.9	1 100.7	108.2	31.9
Net customer loans (granted)/repaid		0.6	0.6	3.0	3.0	3.1
Net contribution to other sectors of government		(569.6)	(625.7)	(710.3)	(324.1)	(80.9)
Net cash flows from investing activities		**(2 594.2)**	**(2 704.0)**	**(2 061.6)**	**(2 418.4)**	**(2 286.7)**
Cash flows from financing activities						
Net borrowings		8.2	8.5	5.4	293.5	488.9
Net cash flows from financing activities		**8.2**	**8.5**	**5.4**	**293.5**	**488.9**
Net increase in cash and deposits held		**(7.3)**	**(14.5)**	**(315.0)**	**(415.0)**	**(115.0)**
Cash and deposits at beginning of reporting period		1 799.0	1 799.0	1 784.4	1 469.4	1 054.4
Cash and deposits at end of reporting period	*16*	**1 791.7**	**1 784.4**	**1 469.4**	**1 054.4**	**939.4**

The accompanying notes form part of these Estimated Financial Statements.

Notes to the Estimated Financial Statements

Due to the possibility that circumstances or events outlined in the Estimated Financial Statements may not occur as expected, actual results may differ from those forecast and the difference may be material. Accordingly, no guarantee is given that the financial results will be achieved. However, the best professional judgement has been applied in preparing the Estimated Financial Statements.

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Assumptions

The Estimated Financial Statements have been prepared using the material economic and other assumptions listed below.

Material economic and other assumptions[(a)]

	(per cent change)			
	2005-06	*2006-07*	*2007-08*	*2008-09*
Gross state product	3.00	3.50	3.50	3.25
Employment	2.00	1.25	1.50	1.25
Consumer price index [(b)]	3.00	2.50	2.50	2.50
Wage cost index [(c)]	4.00	3.50	3.50	3.50
Population [(d)]	1.10	1.00	1.00	1.00

Source: Australian Bureau of Statistics, Department of Treasury and Finance

Notes:

(a) Year-average per cent change on previous year unless otherwise indicated. All projections apart from population are rounded to the nearest 0.25 percentage points. Projections of population are rounded to the nearest 0.1 percentage points.

(b) Departmental output revenue for the budget year, that is subject to indexation under the departmental funding model, is indexed by the consumer price index forecast at the time of the Budget Update (2.5 per cent). This may differ from the updated forecast consumer price index as disclosed.

(c) Total hourly rate excluding bonuses.

(d) June quarter, per cent change on previous June quarter.

Note 1: Statement of significant accounting policies and forecast assumptions

The following summary sets out the significant accounting policies and forecast assumptions that have been adopted in preparing and presenting this update of the Estimated Financial Statements for the forecast period (which includes the budget year and the estimates for the three subsequent years).

The accounting policies and assumptions applied, other than the assumptions for defined benefit superannuation expense and liability, are consistent with those of the Estimated Financial Statements as published in the 2005-06 Budget Paper No. 4, *Statement of Finances* which should be read in conjunction with this update.

(A) Compliance framework

This *Budget Update* is a specific purpose financial report for the general government sector comprising Estimated Financial Statements for the 2005-06 Budget year and subsequent forecast years as required by section 23L of the *Financial Management Act* 1994. It has not been subject to audit review.

These Estimated Financial Statements have been prepared in accordance with Australian equivalents to International Financial Reporting Standards (A-IFRS), other authoritative pronouncements of the Australian Accounting Standards Board, Urgent Issues Group Interpretations and the *Financial Management Act* 1994. Their presentation is based on New Zealand Financial Reporting Standard *Prospective Financial Information* (modified to achieve consistency in the presentation of the Estimated Financial Statements with the format expected to be used in the future for reporting historically orientated Victorian general government financial reports and to be consistent with A-IFRS) because there are no specific Australian authoritative pronouncements which prescribe the preparation and presentation of prospective financial statements. The information presented in the Estimated Financial Statements takes into account government decisions and other circumstances that may have a material effect on the statements.

(B) Basis of accounting and measurement

The accrual basis of accounting has been employed in the preparation of the Estimated Financial Statements whereby assets, liabilities, income, expenses and equity are recognised in the reporting period to which they relate, regardless of when cash is received or paid.

The opening balances of 1 July 2005 are based on the most recent audited financial reports of consolidated entities adjusted for the adoption of A-IFRS.

(C) Reporting entity

The Victorian general government sector includes all government departments, agencies and other bodies engaged in providing public services free of charge or at prices significantly below their cost of production. The services provided by these entities are financed mainly through taxes, other compulsory levies and user charges. The general government sector is not a separate entity but represents the budget sector within the State of Victoria whole-of-government reporting entity.

(D) Basis of consolidation

The Estimated Financial Statements incorporate assets and liabilities of all reporting entities within the Victorian general government sector and their income and expenses for the respective period.

Details of the entities included in the general government sector are shown in Note 18 to the financial statements.

In the process of reporting the general government sector as a single economic entity, all material transactions and balances between entities within the sector are eliminated.

(E) Developments in financial reporting standards

The AASB has issued for comment a proposed accounting standard for *Financial Reporting of General Government Sectors by Governments*. This proposed standard is intended to harmonise the requirements of Government Finance Statistics (GFS) and Generally Accepted Accounting Principles (GAAP) to produce one set of financial reports. The final outcome of this proposal and when it will be effective is uncertain. However, the presentation format used in this update is not inconsistent with A-IFRS, and is intended to transitionally address the needs of all users pending finalisation and introduction of a new reporting standard for government. The effect of any changes to recognition or measurement requirements as a result of this proposed new standard is not expected to be significant.

The AASB has also advised its intention to withdraw the accounting standards specific to Government Departments (AAS 29) and Government (AAS 31) and replace them where required by topic-specific financial reporting standards. The final outcome and timing of this project is uncertain, but there is not expected to be a significant effect on the results or financial position of the general government sector.

The AASB also continues to make new and revise existing financial reporting standards, including the July 2004 'stable platform of A-IFRS'. These changes result from both the AASB's own activities and changes made to International Financial Reporting Standards. The impact that may occur as a result of these changes is unknown and is not accounted for in the Estimated Financial Statements.

(F) Revised forecast assumptions

All forecast assumptions are as published in the 2005-06 Budget Paper No. 4, *Statement of Finances* except for the following.

Superannuation expenses from transactions

Forecast assumptions

Future defined contribution superannuation expenses are based on assumptions regarding future salaries and legislated contribution rates.

Future defined benefit superannuation expenses are based on the estimated value of benefits that are expected to accrue to members during the reporting period and forecast investment returns and bond rates. The relevant forecast assumptions are determined and applied in accordance with the requirements of current accounting standards. Refer below for the forecast assumptions for the State's net defined benefit superannuation liabilities.

Superannuation liabilities

The liability for employee superannuation benefits is the responsibility of the State's public sector superannuation schemes. These schemes are not consolidated in the Estimated Financial Statements as they are not controlled by the State. However, the major proportion of unfunded superannuation liabilities is the responsibility of the State and is recognised accordingly.

Forecast assumptions

The State's superannuation liabilities at future balance dates are estimated based on projections provided by the actuaries of the various defined benefit schemes. These projections are based on demographic and financial assumptions which include, in particular, an expected return on the assets of the defined benefit schemes and a discount rate for determining the present value of accrued benefits. Consistent with the long-term actuarial assumptions detailed below, the expected return on assets is assumed to remain constant across the budget and forecast periods. The discount rates used are based, in accordance with the requirements for reporting under A-IFRS, on prevailing Commonwealth bond rates and are also assumed to remain constant across the forward estimates period. Actual experience may vary significantly from the assumptions used, resulting in significant changes in the value of the State's superannuation liabilities which flow through to the operating statement, primarily as other economic flows.

Set out below are the disclosures required by AASB 119 *Employee Benefits,* regarding the forecast assumptions for the budget and forward years for each relevant defined benefit scheme.

Superannuation assumptions

Victorian statutory superannuation schemes	*Assumptions*	*Per cent [(a)]*
State Superannuation Fund/Emergency Services Superannuation Scheme	Expected return on assets[(b)]	7.50
	Discount rate[(c)(d)]	5.43
	Wages growth	4.00
	Inflation rate	2.50
Constitutionally Protected Schemes	Discount rate[(c)]	5.47
	Wages growth	4.00
	Inflation rate	n.a.
Parliamentary Contributory Superannuation Scheme [(e)]	Expected return on assets[(b)]	7.60
	Discount rate[(c)]	5.47
	Wages growth	4.00
	Inflation rate	n.a.
Health Super Fund	Expected return on assets[(b)]	7.00
	Discount rate[(c)]	5.47
	Wages growth	4.00
	Inflation rate	2.50

Notes:
(a) Wages growth in this table are actuarial assumptions and do not reflect the Government's wages policy.
(b) The expected return on assets stated is gross of tax. This rate is adjusted in the calculation process to reflect the assumed rate of tax payable by each scheme. For the period to 30 June 2005, further adjustment was made in the calculation process to allow for the actual investment performance of each scheme, as available at that time.
(c) In accordance with accounting standards, the discount rate is based on the ten-year Commonwealth Government bond rate. The rate stated above is an annual effective rate, gross of tax.
(d) This rate was updated as part of the Budget Update to reflect the bond rate at that time.
(e) Parliamentary salaries are determined by reference to equivalent salaries in the Commonwealth Parliament.

(G) Rounding

All amounts in the Estimated Financial Statements have been rounded to the nearest hundred thousand dollars unless otherwise stated. Figures in the Estimated Financial Statements may not add due to rounding.

Note 2: Taxation

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Payroll tax	**3 179.2**	**3 257.7**	**3 415.9**	**3 582.4**	**3 752.2**
Taxes on immovable property					
Land tax	824.1	771.7	810.6	799.4	807.8
Congestion levy	19.4	19.4	38.8	39.7	40.6
Metropolitan improvement levy	92.1	92.1	95.1	98.2	101.4
Property owner contributions to fire brigades	34.9	34.9	35.6	36.4	38.0
Total taxes on immovable property	**970.5**	**918.1**	**980.1**	**973.7**	**987.8**
Financial and capital transactions					
Land transfers	2 075.6	2 208.8	2 211.1	2 224.9	2 314.5
Rental business stamp duty	57.5	57.5	43.4	..	..
Other property stamp duty	11.1	8.9	9.4	9.9	10.4
Debits tax [(a)]	21.5	21.5	..	..	..
Financial accommodation levy	10.2	10.2	14.1	16.6	16.8
Total financial and capital transactions	**2 175.9**	**2 306.9**	**2 278.0**	**2 251.4**	**2 341.7**
Levies on statutory corporations	**60.4**	**60.4**	**60.4**	**61.6**	**..**
Gambling taxes					
Private lotteries	314.7	307.9	320.0	320.6	327.7
Electronic gaming machines	931.0	930.1	984.9	947.2	1 000.2
Casino	113.5	111.8	120.4	129.9	141.0
Racing	116.5	116.8	120.6	118.4	122.2
Other	3.3	3.5	3.7	3.9	4.1
Total gambling taxes	**1 479.0**	**1 470.1**	**1 549.6**	**1 520.0**	**1 595.2**
Taxes on insurance	**1 061.2**	**1 063.6**	**1 121.0**	**1 182.6**	**1 237.3**
Motor vehicle taxes					
Vehicle registration fees	711.4	710.9	770.1	814.1	860.3
Stamp duty on vehicle transfers	594.9	585.2	620.0	657.3	696.4
Total motor vehicle taxes	**1 306.3**	**1 296.1**	**1 390.1**	**1 471.4**	**1 556.7**
Other taxes	**73.7**	**80.1**	**85.5**	**89.0**	**85.6**
Total taxation revenue	**10 306.2**	**10 452.9**	**10 880.6**	**11 132.0**	**11 556.4**

Note:

(a) *Debits tax was abolished on 1 July 2005. Revenue in 2005-06 represents carryover amounts from the previous year.*

Note 3: Investment revenue

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Investment income from transactions					
Dividends	699.9	723.1	514.9	553.7	440.1
Income tax and rate equivalent revenue	203.6	113.7	177.3	253.7	314.7
Interest	361.7	339.7	300.9	257.6	251.0
Royalties	55.7	55.7	65.0	65.4	65.9
Rents	15.3	15.3	15.4	15.6	15.7
Other	61.6	62.7	64.0	64.3	64.7
Total investment income from transactions	**1 397.9**	**1 310.4**	**1 137.6**	**1 210.3**	**1 152.1**
Investment income from other economic flows					
Gain on investments [(a)]	0.1	0.1	0.1	0.1	0.1
Total investment income from other economic flows	**0.1**	**0.1**	**0.1**	**0.1**	**0.1**
Total investment income	**1 398.0**	**1 310.5**	**1 137.7**	**1 210.4**	**1 152.2**

Note:

(a) Gain on investments is a component of 'other income from other economic flows' on the operating statement.

Note 4: Grants

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Operating grants					
General purpose grants	8 050.4	8 087.4	8 347.7	8 851.5	9 362.3
Specific purpose grants for on-passing	1 686.3	1 663.6	1 740.2	1 798.3	1 858.7
Other specific purpose grants	3 971.1	4 010.6	4 013.0	4 173.7	4 343.7
Total operating grants	**13 707.7**	**13 761.6**	**14 100.9**	**14 823.5**	**15 564.8**
Capital grants					
Specific purpose grants for on-passing	132.3	132.5	136.4	137.1	137.9
Other specific purpose grants	422.0	446.0	630.9	461.0	340.1
Total capital grants	**554.3**	**578.5**	**767.3**	**598.2**	**477.9**
Total grants income	**14 262.1**	**14 340.0**	**14 868.2**	**15 421.6**	**16 042.7**

Note 5: Superannuation

(a) Superannuation expense recognised in the operating statement

($ million)

	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Defined benefit plans					
Current service cost [(a)]	634.5	732.0	700.0	668.0	643.0
Interest cost [(a)]	1 401.7	1 484.0	1 526.3	1 552.5	1 573.5
Expected return on plan assets (net of expenses) [(a)]	(958.8)	(1 076.5)	(1 107.9)	(1 133.4)	(1 157.2)
Amortisation of past service cost [(a)]	(12.0)	(15.0)	(15.0)	(15.0)	(15.0)
Actuarial (gains)/losses [(b)]	..	(1 203.5)	..	..	..
Total expense recognised in respect of defined benefit plans	**1 065.4**	**(79.1)**	**1 103.5**	**1 072.1**	**1 044.4**
Defined contribution plans					
Employer contributions to defined contribution plans [(a)]	655.2	591.7	628.6	659.1	676.1
Other (including pensions) [(a)]	38.7	38.7	40.3	41.9	43.5
Total expense recognised in respect of defined contribution plans	**693.9**	**630.4**	**668.9**	**701.0**	**719.6**
Total superannuation expense recognised in operating statement	**1 759.3**	**551.4**	**1 772.3**	**1 773.1**	**1 764.0**

Notes:
(a) Superannuation expense from transactions.
(b) Superannuation expense from other economic flows.

(b) Reconciliation of the present value of the defined benefit obligation

($ million)

	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Opening balance of defined benefit obligation	30 137.7	30 198.7	30 721.4	31 044.7
Current service cost	732.0	700.0	668.0	643.0
Interest cost	1 484.0	1 526.3	1 552.5	1 573.5
Contributions by plan participants	213.2	207.2	198.4	190.0
Actuarial (gains)/losses	(554.2)	..	..	..
Benefits paid	(1 814.1)	(1 910.8)	(2 095.7)	(2 193.4)
Closing balance of defined benefit obligation	**30 198.7**	**30 721.4**	**31 044.7**	**31 257.8**

(c) Reconciliation of the fair value of superannuation plan assets

($ million)

	2005-06 *Revised*	2006-07 *Estimate*	2007-08 *Estimate*	2008-09 *Estimate*
Opening balance of plan assets	14 865.7	15 529.7	15 696.0	15 957.9
Expected return on plan assets	1 076.5	1 107.9	1 133.4	1 157.2
Actuarial gains/(losses)	649.4	..	..	..
Employer contributions	487.5	762.3	1 026.2	1 111.1
Contributions by plan participants	213.2	207.2	198.4	190.0
Benefits paid (including tax paid)	(1 762.6)	(1 911.1)	(2 096.0)	(2 192.5)
Closing balance of plan assets	**15 529.7**	**15 696.0**	**15 957.9**	**16 223.8**

(d) Reconciliation of the assets and liabilities recognised in the balance sheet

($ million)

	2005-06 *Revised*	2006-07 *Estimate*	2007-08 *Estimate*	2008-09 *Estimate*
State Superannuation Fund				
Defined benefit obligation	24 513.7	24 997.9	25 300.8	25 490.1
Plan assets	(9 969.2)	(10 010.8)	(10 154.2)	(10 284.2)
Net liability/(asset)	**14 544.5**	**14 987.2**	**15 146.6**	**15 205.9**
Other funds [(a)]				
Defined benefit obligation	5 685.0	5 723.5	5 743.9	5 767.7
Plan assets	(5 560.5)	(5 685.2)	(5 803.8)	(5 939.5)
Unrecognised past service cost	52.7	37.7	22.6	8.4
Net liability/(asset)	**177.2**	**76.0**	**(37.3)**	**(163.4)**
Total unfunded superannuation				
Defined benefit obligation	30 198.7	30 721.4	31 044.7	31 257.8
Plan assets	(15 529.7)	(15 696.0)	(15 957.9)	(16 223.8)
Unrecognised past service cost	52.7	37.7	22.6	8.4
Unfunded superannuation liability	**14 721.7**	**15 063.1**	**15 109.3**	**15 042.5**
Represented by:				
Current liability	285.1	556.1	644.0	806.0
Non-current liability	14 436.7	14 507.0	14 465.3	14 236.5

Note:

(a) Other consists of Emergency Services Superannuation Scheme, constitutionally protected schemes, Parliamentary Contributory Superannuation Fund, HealthSuper Fund and the general government element of Vision Super.

Note 6: Depreciation and amortisation

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Depreciation from transactions					
Plant, equipment and infrastructure systems	540.0	547.0	579.3	604.0	608.6
Buildings [(a)]	338.5	329.8	357.9	410.1	464.3
Road networks	302.3	290.9	299.6	308.6	317.8
Other assets	11.9	11.9	8.4	8.3	8.3
Total depreciation from transactions	**1 192.6**	**1 179.6**	**1 245.2**	**1 330.9**	**1 399.0**
Amortisation from transactions					
Leased plant and equipment	13.3	14.7	11.4	12.0	12.1
Leasehold buildings	21.8	20.1	22.4	22.5	22.5
Intangible produced assets	7.4	7.4	6.4	5.9	5.9
Total amortisation from transactions	**42.5**	**42.2**	**40.2**	**40.5**	**40.6**
Total depreciation and amortisation from transactions	**1 235.1**	**1 221.7**	**1 285.4**	**1 371.5**	**1 439.5**
Amortisation from other economic flows					
Intangible non-produced assets [(b)]	8.4	8.4	9.6	8.9	10.2
Total amortisation from other economic flows	**8.4**	**8.4**	**9.6**	**8.9**	**10.2**
Total depreciation and amortisation	**1 243.5**	**1 230.1**	**1 294.9**	**1 380.4**	**1 449.7**

Notes:

(a) Includes estimated depreciation on amounts not yet allocated to projects in 2006-07 to 2008-09.

(b) Amortisation of intangible non-produced assets is a component of 'other expenses from other economic flows' on the operating statement.

Note 7: Financing costs

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Interest on long-term interest bearing liabilities	356.4	354.6	347.1	349.8	363.7
Interest on short-term interest bearing liabilities	23.1	23.1	26.1	26.4	26.3
Finance charges on finance leases	25.6	25.6	41.4	42.0	42.5
Discount interest	59.0	49.7	45.1	41.5	40.9
Other financing costs	28.1	24.7	24.8	30.5	33.5
Total financing costs	**492.1**	**477.7**	**484.6**	**490.2**	**506.9**

Note 8: Grants and transfer payments

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Commonwealth	53.7	57.7	59.4	61.2	63.0
Local government	493.7	505.3	536.9	529.8	530.3
Private sector	3 428.7	3 474.9	3 405.8	3 335.2	3 337.5
Grants within Victorian Government	1 599.6	1 653.3	1 625.5	1 667.4	1 634.6
Grants to other state governments	3.7	3.7	1.8	0.5	0.5
Total grants and transfer payments	**5 579.3**	**5 694.9**	**5 629.5**	**5 594.1**	**5 565.9**

Note 9: Total expenses by departments

($ million)

	2005-06 Budget	2005-06 Revised [d]	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Expenses from transactions					
Parliament	107.7	108.1	111.2	113.1	114.2
Education and Training	8 973.4	9 064.7	9 357.6	9 474.4	9 699.6
Human Services	11 433.2	11 489.8	11 797.1	12 107.6	12 351.2
Infrastructure	3 505.8	3 553.7	3 661.8	3 689.0	3 736.3
Innovation, Industry and Regional Development	276.9	392.7	371.0	355.3	285.5
Justice	2 789.8	2 816.6	2 858.6	2 954.9	3 041.3
Premier and Cabinet	482.1	486.6	491.8	505.4	561.0
Primary Industries	351.8	411.0	346.2	315.7	321.5
Sustainability and Environment	950.7	996.4	978.6	972.9	1 009.2
Treasury and Finance	1 978.0	1 966.1	1 985.7	1 972.8	1 955.6
Victorian Communities	1 064.5	1 112.8	782.4	717.4	733.4
Contingencies not allocated to departments [a]	9.7	(164.0)	429.9	880.5	1 264.9
Regulatory bodies and other part budget funded agencies [b]	1 039.3	1 039.3	1 075.7	1 106.9	1 126.5
Total	**32 962.7**	**33 273.8**	**34 247.8**	**35 166.0**	**36 200.2**
Less eliminations [c]	(2 703.8)	(2 733.5)	(2 753.3)	(2 856.6)	(2 813.0)
Total expenses from transactions	**30 258.9**	**30 540.3**	**31 494.5**	**32 309.4**	**33 387.2**
Expenses from other economic flows					
Treasury and Finance	..	(1 203.5)	..	..	..
Other	74.8	70.8	66.9	56.3	52.5
Total expenses from other economic flows	**74.8**	**(1 132.8)**	**66.9**	**56.2**	**52.5**

Notes:

(a) This contingency includes a provision for programs lapsing in 2006-07 or later years, future demand growth, and an allowance for departmental underspending in 2005-06 which may be subject to carryover into 2006-07 including Treasurer's Advance. Under the departmental funding model, since 1 July 2004, departments have been required to manage all costs within their departmental budgets.

(b) Other general government sector agencies, which receive less that 50 per cent of their revenue from appropriations and therefore are not allocated to departments.

(c) Comprising payroll tax, capital asset charge and inter-departmental transfers.

(d) 2005-06 revised departmental estimates are inclusive of carryover.

Note 10: Property, plant and equipment and infrastructure systems

($ million)

	2006 *Revised*	2007 *Estimate*	2008 *Estimate*	2009 *Estimate*
Land, national parks and other land only holdings	**18 769.4**	**19 904.3**	**21 077.0**	**22 365.2**
Buildings [(a)]	14 782.7	16 512.7	18 448.6	20 741.7
Less: Accumulated depreciation	*(1 114.7)*	*(1 483.7)*	*(1 905.7)*	*(2 382.4)*
Buildings (written down value)	**13 668.0**	**15 029.1**	**16 542.9**	**18 359.2**
Infrastructure systems	990.7	1 127.7	1 252.6	1 349.7
Less: Accumulated depreciation	*(47.6)*	*(69.0)*	*(92.3)*	*(117.8)*
Infrastructure systems (written down value)	**943.1**	**1 058.6**	**1 160.3**	**1 231.8**
Plant, equipment and vehicles	4 695.9	5 026.4	5 274.3	5 515.8
Less: Accumulated depreciation	*(2 795.9)*	*(3 259.8)*	*(3 755.4)*	*(4 255.5)*
Plant, equipment and vehicles (written down value)	**1 900.0**	**1 766.6**	**1 518.9**	**1 260.3**
Leased plant, equipment and vehicles	68.3	53.7	34.7	34.7
Less: Accumulated depreciation	*(31.6)*	*(29.4)*	*(25.7)*	*(28.9)*
Leased plant, equipment and vehicles (written down value)	**36.7**	**24.3**	**8.9**	**5.7**
Total property, plant and equipment and infrastructure systems	**35 317.2**	**37 782.9**	**40 308.0**	**43 222.3**

Note:
(a) Includes amounts not yet allocated to projects in 2006-07 to 2008-09.

Note 11: Road networks

($ million)

	2006 *Revised*	2007 *Estimate*	2008 *Estimate*	2009 *Estimate*
Roads	15 438.6	16 655.1	17 612.9	18 448.1
Accumulated depreciation	*(5 462.4)*	*(5 700.4)*	*(5 945.4)*	*(6 197.8)*
Road Infrastructure	4 871.6	5 084.0	5 324.0	5 620.5
Accumulated depreciation	*(1 702.5)*	*(1 764.2)*	*(1 827.7)*	*(1 893.1)*
Roads (written down value)	**13 145.2**	**14 274.5**	**15 163.8**	**15 977.6**
Earthworks	4 589.8	4 589.8	4 589.8	4 589.8
Total road networks	**17 735.0**	**18 864.3**	**19 753.6**	**20 567.4**

Note 12: Reconciliation of movements in fixed assets

($ million)

	2006 Revised	2007 Estimate	2008 Estimate	2009 Estimate
Carrying amount at the start of the year [(a)]	48 990.9	53 052.2	56 647.2	60 061.6
Additions [(b)]	3 193.8	2 586.1	2 404.8	2 349.8
Disposals at written down value	(140.2)	(113.7)	(211.8)	(110.1)
Revaluations increments	2 252.1	2 394.2	2 579.6	2 800.2
Assets transferred	(42.0)	(1.0)	(1.0)	113.5
Depreciation/amortisation expense	(1 202.5)	(1 270.6)	(1 357.2)	(1 425.3)
Carrying amount at the end of the year	**53 052.2**	**56 647.2**	**60 061.6**	**63 789.7**

Notes:

(a) Fixed assets comprise land and buildings, infrastructure systems, plant, equipment, vehicles and road networks. Excludes movements in other assets in Note 13 below.

(b) Includes assets acquired under finance lease arrangements.

Note 13: Other assets

($ million)

	2006 Revised	2007 Estimate	2008 Estimate	2009 Estimate
Natural resources reserves at valuation	87.3	95.7	104.1	112.5
Other assets - including works of art, museum collection, rare book collections and intangibles	4 063.5	4 113.8	4 176.2	4 223.6
Less: Accumulated depreciation/amortisation	*(185.2)*	*(208.9)*	*(232.8)*	*(256.6)*
Total other assets	**3 965.6**	**4 000.6**	**4 047.6**	**4 079.5**

Note 14: Employee benefits

($ million)

	2006 Revised	2007 Estimate	2008 Estimate	2009 Estimate
Current				
Accrued salaries and wages [(a)]	761.8	781.6	802.0	821.8
Long service leave	241.0	267.6	294.0	320.4
Total current employee benefits	**1 002.8**	**1 049.1**	**1 096.0**	**1 142.3**
Non-current				
Accrued salaries and wages [(a)]	135.6	135.6	135.6	135.6
Long service leave	2 315.9	2 435.2	2 512.0	2 589.2
Total non-current employee benefits	**2 451.5**	**2 570.8**	**2 647.6**	**2 724.9**
Total employee benefits	**3 454.3**	**3 619.9**	**3 743.6**	**3 867.1**

Note:

(a) Includes accrued annual leave, payroll tax and other similar on-costs.

Note 15: Reconciliation of net result to net cash flows from operating activities

($ million)

	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Net result	1 502.0	281.1	375.8	485.5
Non-cash movements				
Depreciation and amortisation	1 230.1	1 294.9	1 380.4	1 449.7
Revaluation of investments	(0.1)	(0.1)	(0.1)	(0.1)
Assets received/given free of charge	(9.4)	..	..	(114.5)
Revaluation of assets	(8.4)	(8.4)	(8.4)	(8.4)
Discount/premium on other financial assets/interest bearing liabilities	6.3	5.9	4.9	7.5
Movements included in investing and financing activities				
Net revenue from sale of property, plant and equipment	(29.7)	(22.9)	(10.6)	(11.2)
Movements in assets and liabilities				
Increase/(decrease) in provision of doubtful debts	61.7	57.0	47.0	41.9
Increase/(decrease) in payables	(14.2)	(101.5)	(89.6)	(56.3)
Increase/(decrease) in employee benefits	246.6	165.6	123.7	123.5
Increase/(decrease) in superannuation	(566.0)	341.3	46.3	(66.9)
Increase/(decrease) in other provisions	(0.2)	(17.9)	(12.2)	(11.2)
Increase/(decrease) in other liabilities	(63.3)	(6.9)	(6.7)	(6.9)
(Increase)/decrease in receivables	338.5	(273.8)	(156.7)	(183.8)
(Increase)/decrease in other assets	(13.0)	26.8	16.1	33.9
Net cash flows from operating activities	**2 680.9**	**1 741.2**	**1 709.9**	**1 682.8**

Note 16: Reconciliation of cash

($ million)

	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Cash	598.5	612.8	628.7	643.2
Deposits at call	1 190.2	860.8	429.9	300.4
Cash and deposits	**1 788.7**	**1 473.7**	**1 058.7**	**943.7**
Bank overdraft	(4.2)	(4.2)	(4.2)	(4.2)
Cash and deposits held as at 30 June	**1 784.4**	**1 469.4**	**1 054.4**	**939.4**

Note 17: Purchase of property, plant and equipment by departments

($ million)

	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Parliament	6.1	6.1	5.1	6.7	2.2
Education and Training	555.7	562.2	396.5	200.8	202.3
Human Services [(a)]	773.7	812.7	550.3	285.0	117.3
Infrastructure	661.7	591.6	735.9	456.3	158.2
Innovation, Industry and Regional Development	48.9	55.1	11.6	11.7	11.7
Justice	194.1	206.9	138.5	87.6	74.0
Premier and Cabinet	81.8	106.0	75.2	34.0	19.2
Primary Industries	4.9	6.0	5.1	5.2	5.2
Sustainability and Environment	131.9	204.8	126.7	114.0	99.8
Treasury and Finance [(b)]	65.8	72.9	28.7	14.0	13.9
Victorian Communities	24.2	45.0	7.3	6.3	6.2
Regulatory bodies and other part budget funded agencies	105.4	105.4	118.5	84.9	85.2
Not allocated to departments [(c)]	(125.0)	(185.0)	399.5	1 109.4	1 567.0
Total purchase of property, plant and equipment	**2 529.4**	**2 589.7**	**2 599.0**	**2 415.9**	**2 362.1**

Notes:

(a) On 28 November, the Government announced the redevelopment of the Royal Children's Hospital with a total estimated investment of $847.4 million. However, the annual cash flows are yet to be determined and as such are not included in the Human Services estimates. Once finalised these cash flows will reduce the amount available to be allocated to specific Departments and increase Human Services estimates.

(b) Includes amounts under the vehicle fleet leasing facility not allocated to departments.

(c) Amount available to be allocated to specific departments and projects in future budgets. This includes an allowance for departmental underspending in 2005-06 which may be subject to carryover in 2006-07.

Note 18: General government sector entities

The following is a list of general government sector entities which have been consolidated for the purposes of the Estimated Financial Statements. For further details on consolidation policy, refer to Note 1 (D) 'Basis of consolidation' in the statement of significant accounting policies and forecast assumptions.

General government sector entities
Department of Education and Training
Adult Community and Further Education Board
Adult Multicultural Education Services
Centre for Adult Education
TAFEs including:
Bendigo Regional Institute of TAFE
Box Hill Institute of TAFE
Central Gippsland Institute of TAFE
Chisholm Institute of TAFE
Driver Education Centre of Australia Ltd
East Gippsland Institute of TAFE
Gordon Institute of TAFE
Goulburn Ovens Institute of TAFE
Holmesglen Institute of TAFE
Institute of Land and Food Resources (TAFE Division)
International Fibre Centre Limited
Kangan Batman Institute of TAFE
Northern Melbourne Institute of TAFE
Royal Melbourne Institute of Technology (TAFE Division)
South West Institute of TAFE
Sunraysia Institute of TAFE
Swinburne University of Technology (TAFE Division)
University of Ballarat (TAFE Division)
Victoria University of Technology (TAFE Division)
William Angliss Institute of TAFE
Wodonga Institute of TAFE
Victorian Curriculum and Assessment Authority
Victorian Institute of Teaching
Victorian Learning and Employment Skills Commission
Victorian Qualifications Authority
Department of Human Services
Health Purchasing Victoria
Hospitals, Health and Ambulance Services including:
Alexandra District Ambulance Service
Alexandra District Hospital
Alpine Health
Ambulance Service Victoria Metropolitan Region
Austin Health
Bairnsdale Regional Health Service
Ballarat Health Services
Barwon Health
Bass Coast Regional Health
Bayside Health
Beaufort and Skipton Health Service

General government sector entities (continued)
Beechworth Health Service
Benalla and District Memorial Hospital
Bendigo Health Care Group
Boort District Hospital
Casterton Memorial Hospital
Central Gippsland Health Service
Cobram District Hospital
Cohuna District Hospital
Colac Area Health
Dental Health Services Victoria
Djerriwarrh Health Services
Dunmunkle Health Services
East Grampians Health Service
East Wimmera Health Service
Eastern Health
Echuca Regional Health
Edenhope and District Memorial Hospital
Gippsland Southern Health Service
Goulburn Valley Health
Hepburn Health Service
Hesse Rural Health Service
Heywood Rural Health
Inglewood and District Health Service
Kerang and District Hospital
Kooweerup Regional Health Service
Kyabram and District Health Services
Kyneton District Health Service
Latrobe Regional Hospital
Lorne Community Hospital
Maldon Hospital
Mallee Track Health and Community Services
Manangatang and District Hospital
Mansfield District Hospital
Maryborough District Health Service
McIvor Health and Community Services
Melbourne Health
Moyne Health Services
Mt Alexander Hospital
Nathalia District Hospital
Northeast Health Wangaratta
Northern Health
Numurkah District Health Service
Omeo District Health
Orbost Regional Health
Otway Health and Community Services
Peninsula Health
Peter MacCallum Cancer Institute
Portland District Health
Robinvale District Health Services
Rochester and Elmore District Health Service
Rural Ambulance Victoria
Rural Northwest Health
Seymour District Memorial Hospital

General government sector entities (continued)
South Gippsland Hospital
South West Healthcare
Southern Health
Stawell Regional Health
Swan Hill District Hospital
Tallangatta Health Service
Terang and Mortlake Health Service
The Kilmore and District Hospital
The Queen Elizabeth Centre
The Royal Children's Hospital
The Royal Victorian Eye and Ear Hospital
The Royal Women's Hospital
Timboon and District Health Care Service
Tweddle Child and Family Health Service
Upper Murray Health and Community Services
Victorian Institute of Forensic Mental Health
West Gippsland Health Care Group
West Wimmera Health Service
Western District Health Service (formerly Western District Health Service and the Coleraine District Health Services) (a)
Western Health
Wimmera Health Care Group
Wodonga Regional Health Service
Yarram and District Health Service
Yarrawonga District Health Service
Yea and District Memorial Hospital
Infertility Treatment Authority
Mental Health Review Board
Psychosurgery Review Board
Registration Boards including:
Chinese Medicine Registration Board of Victoria
Chiropractors Registration Board of Victoria
Dental Practice Board of Victoria
Medical Practitioners Board of Victoria
Nurses Board of Victoria
Optometrists Registration Board of Victoria
Osteopaths Registration Board of Victoria
Pharmacy Board of Victoria
Physiotherapists Registration Board of Victoria
Podiatrists Registration Board of Victoria
Psychologists Registration Board of Victoria
Victorian Health Promotion Foundation
Victorian Relief Committee

Department of Infrastructure
Energy Safe Victoria (formerly Office of Gas Safety and the Office of the Chief Electrical Inspector) (a)
Roads Corporation
Southern and Eastern Integrated Transport Authority
Spencer Street Station Authority

General government sector entities (continued)
Department of Innovation Industry and Regional Development
Prince Henry’s Institute of Medical Research
Regional Development Victoria
Tourism Victoria
Department of Justice
Country Fire Authority
Domestic Building (HIH) Indemnity Fund
Emergency Services Telecommunications Authority (formerly Emergency Communications Victoria) [(a)]
Equal Opportunity Commission
Judicial College of Victoria
Legal Practice Board
Liquor Licensing Panel
Metropolitan Fire and Emergency Services Board
Office of Public Prosecutions
Office of the Legal Ombudsman
Office of the Public Advocate
Office of the Victorian Privacy Commissioner
Sentencing Advisory Council
Victoria Legal Aid
Victoria Police (Office of the Chief Commissioner of Police)
Victoria State Emergency Service Authority [(a)]
Victorian Commission for Gambling Regulation
Victorian Electoral Commission
Victorian Institute of Forensic Medicine
Victorian Law Reform Commission
Department of Premier and Cabinet
Australian Centre for the Moving Image
Film Victoria
Library Board of Victoria
Museums Board of Victoria
National Gallery of Victoria, Council of Trustees
Office of Police Integrity
Office of the Ombudsman
State Services Authority (incorporates former Office of Public Employment)
Department of Primary Industries
Veterinary Practitioners Registration Board of Victoria
Department of Sustainability and Environment
Architects Registration Board of Victoria
Building Commission
Catchment Management Authorities including:
Corangamite Catchment Management Authority
East Gippsland Catchment Management Authority
Glenelg Hopkins Catchment Management Authority
Goulburn Broken Catchment Management Authority
Mallee Catchment Management Authority
North Central Catchment Management Authority
North East Catchment Management Authority

General government sector entities (continued)
Port Phillip and Westernport Catchment Management Authority
West Gippsland Catchment Management Authority
Wimmera Catchment Management Authority
Environment Protection Authority
Heritage Council
Office of the Commissioner for Environmental Sustainability
Parks Victoria
Plumbing Industry Commission
Royal Botanic Gardens Board
Surveyors Registration Board of Victoria (formerly Surveyors Board) [(a)]
Sustainability Victoria (formerly Sustainability Energy Authority and Eco Recycle Victoria) [(a)]
Trust for Nature (Victoria)

Department of Treasury and Finance
Essential Services Commission
Victorian Competition and Efficiency Commission

Department for Victorian Communities
2007 World Swimming Championships Corporation
Shrine of Remembrance Trustees (formerly under Department of Sustainability and Environment)
Victorian Institute of Sport Limited
Victorian Institute of Sport Trust

Parliament of Victoria
Victorian Auditor-General's Office

Note:
(a) New entities in 2005-06.

CHAPTER 7: ACCRUAL UNIFORM PRESENTATION OF GOVERNMENT FINANCE STATISTICS

THE ACCRUAL GFS PRESENTATION

The Government Finance Statistics (GFS) system employed by the Australian Bureau of Statistics (ABS) is designed to provide statistics relating to all Australian public sector entities. The statistics show consolidated transactions of the various institutional sectors of government from an economic viewpoint, providing details of the revenue, expenses, payments, receipts, assets and liabilities. It includes only those transactions over which a government exercises control under its legislative or policy framework, and excludes from the calculation of net operating balance both revaluations (holding gains or losses) arising from a change in market prices, and other changes in the volume of assets resulting from discoveries, depletion and destruction of assets.

GAAP/GFS HARMONISATION

The Australian Accounting Standards Board has issued for comment a proposed accounting standard for *Financial Reporting of General Government Sectors by Governments*. This proposed standard is intended to harmonise the requirements of GFS and Generally Accepted Accounting Principles (GAAP) to produce one set of financial reports. The final outcome of this proposal and when it will be effective are uncertain.

Operating statement

The operating statement is designed to capture the composition of GFS revenues and GFS expenses and the net cost of a government's activities within a financial year. It shows the full cost of resources consumed by government in achieving its objectives, and how these costs are met from various revenue sources.

The GFS operating statement reports two major fiscal measures – the GFS net operating balance and GFS net lending. The GFS net operating balance is calculated as GFS revenue minus GFS expenses. GFS net lending, or fiscal balance, includes net capital expenditure but excludes depreciation, thereby giving a measure of a jurisdiction's call on financial markets.

Previously, differences arose between the GFS and accounting frameworks, particularly in the operating statement. With the introduction of the Australian equivalents to the International Financial Reporting Standards (A-IFRS), the net result from transactions is identical to the GFS net operating balance. Both measures exclude the effects of revaluation (holding gains or losses) arising from changes in the market prices and other changes in the volume of assets.

Balance sheet

The balance sheet records a government's stocks of financial and non-financial assets and liabilities and discloses the resources over which a government maintains control. The GFS balance sheet differs from the standard accounting presentation in that it provides information on financial and non-financial assets, and does not distinguish between current and non-current assets and liabilities.

Compared with the balance sheet estimates published in the 2005-06 Budget Paper No. 4, *Statement of Finances*, the opening balances as at 30 June 2005 and consequent forecast closing balances have been adjusted to reflect actual audited balances as at 30 June 2005 and restated based on A-IFRS. The original estimates were based on audited values at 30 June 2004 adjusted for estimated movements during 2004-05.

Cash flow statement

The cash flow statement records a government's cash receipts and payments and shows how a government obtains and expends cash.

The GFS cash flow statement reports two major fiscal measures – the net increase in cash held and the cash surplus. Net increase in cash held is the sum of net cash flows from all operating, investing and financing activities. The cash surplus comprises only net cash received from operating activities, and from sales and purchases of non-financial assets, minus distributions paid (in the case of public financial corporations and public non-financial corporations), minus finance leases and similar arrangements.

INSTITUTIONAL SECTORS

General government sector

The general government sector comprises all government departments, offices and other bodies engaged in providing services free of charge or at prices significantly below their cost of production. General government services include those which are mainly non-market in nature, those which are largely for collective consumption by the community, and those which involve the transfer or redistribution of income. These services are financed mainly through taxes, other compulsory levies and user charges.

Public non-financial corporations sector

The public non-financial corporations sector was formerly known as the public trading enterprises sector. It comprises bodies mainly engaged in the production of goods and services (of a non-financial nature) for sale in the market place at prices that aim to recover most of the costs involved (e.g. water and port authorities). In general, public non-financial corporations are legally distinguishable from the governments which own them.

Non-financial public sector

The non-financial public sector represents the consolidated transactions and assets and liabilities of the general government and public non-financial corporations sectors. In compiling statistics for the non-financial public sector, transactions and debtor-creditor relationships between sub-sectors are eliminated to avoid double counting.

Table 7.1: General government sector operating statement

($ million)	*2005-06 Budget*	*2005-06 Revised*	*2006-07 Estimate*	*2007-08 Estimate*	*2008-09 Estimate*
GFS revenue					
Taxation revenue	10 306	10 453	10 881	11 132	11 556
Current grants and subsidies	13 708	13 762	14 101	14 823	15 565
Capital grants	554	578	767	598	478
Sales of goods and services	3 604	3 711	3 738	3 764	3 798
Interest income	362	340	301	258	251
Other	2 090	2 028	2 023	2 148	2 257
Total revenue	**30 624**	**30 871**	**31 811**	**32 722**	**33 905**
GFS expenses					
Employee expenses	12 723	12 908	13 243	13 586	13 925
Depreciation	1 235	1 222	1 285	1 371	1 440
Other operating expenses	9 809	9 836	10 452	10 874	11 514
Nominal superannuation interest expense	443	408	418	419	416
Other interest expense	469	459	466	465	481
Other property expenses	..	..	..	..	..
Current transfers	5 254	5 370	5 420	5 459	5 451
Capital transfers	325	337	210	135	160
Total expenses	**30 259**	**30 540**	**31 495**	**32 309**	**33 387**
GFS net operating balance	**365**	**331**	**317**	**413**	**518**
Less: Net acquisition of non-financial assets					
Purchases of non-financial assets	2 529	2 590	2 599	2 416	2 362
Sales of non-financial assets	- 134	- 138	- 144	- 210	- 121
Less: Depreciation	1 235	1 222	1 285	1 371	1 440
Plus: Change in inventories	..	..	1	1	1
Plus: Other movements in non-financial assets	637	624	..	..	115
Total net acquisition of non-financial assets	**1 798**	**1 855**	**1 170**	**835**	**916**
GFS net lending (+) / borrowing (-)	**-1 433**	**-1 524**	**- 854**	**- 422**	**- 398**

Source: Department of Treasury and Finance

Table 7.2: Public non-financial corporations sector operating statement

($ million)	2005-06 Budget	2005-06 Revised	2006-07 Estimate
GFS revenue			
Sales of goods and services	3 403	3 387	3 455
Current grants and subsidies	1 335	1 391	1 428
Capital grants	259	289	200
Interest income	113	138	114
Other	466	382	382
Total revenue	**5 575**	**5 586**	**5 579**
GFS expenses			
Employee expenses	618	656	637
Depreciation	839	828	858
Other operating expenses	3 183	3 239	3 127
Property expenses	882	863	868
Current transfers	176	155	125
Capital transfers	5	9	11
Total expenses	**5 703**	**5 750**	**5 627**
GFS net operating balance	**- 128**	**- 164**	**- 48**
Less: Net acquisition of non-financial assets			
Purchases of non-financial assets	1 870	1 704	2 044
Sales of non-financial assets	- 78	- 72	- 67
Less: Depreciation	839	828	858
Plus: Change in inventories	2	..	4
Plus: Other movements in non-financial assets	164	136	133
Total net acquisition of non-financial assets	**1 118**	**940**	**1 255**
GFS net lending (+) / borrowing (-)	**-1 246**	**-1 104**	**-1 303**

Source: Department of Treasury and Finance

Table 7.3: Non-financial public sector operating statement

($ million)	2005-06 *Budget*	2005-06 *Revised*	2006-07 *Estimate*
GFS revenue			
Taxation revenue	10 161	10 320	10 743
Current grants and subsidies	13 710	13 762	14 101
Capital grants	555	579	767
Sales of goods and services	6 190	6 281	6 378
Interest income	415	428	370
Other	2 023	1 918	1 943
Total revenue	**33 054**	**33 288**	**34 302**
GFS expenses			
Employee expenses	13 342	13 564	13 880
Depreciation	2 075	2 049	2 144
Other operating expenses	12 026	12 102	12 611
Nominal superannuation interest expense	443	408	418
Other interest expense	754	775	807
Other property expenses	..	..	..
Current transfers	3 780	3 853	3 866
Capital transfers	329	345	220
Total expenses	**32 748**	**33 096**	**33 947**
GFS net operating balance	**306**	**192**	**355**
Less: Net acquisition of non-financial assets			
Purchases of non-financial assets	4 399	4 294	4 643
Sales of non-financial assets	- 212	- 210	- 211
Less: Depreciation	2 075	2 049	2 144
Plus: Change in inventories	2	..	4
Plus: Other movements in non-financial assets [(a)]	801	760	133
Total net acquisition of non-financial assets	**2 916**	**2 796**	**2 425**
GFS net lending (+) / borrowing (-)	**-2 610**	**-2 603**	**-2 071**

Source: Department of Treasury and Finance

Note:

(a) Alterations to 2005-06 Budget - due to the discovery of a compilation error in the originally published 2005-06 figure for other movements in non-financial assets in the table above, the previously reported $186 million has been amended to $801 million. As a consequence, the total net acquisition of non-financial assets (previously $2 301 million) and GFS net lending/borrowing (previously -$1 995 million) have also been corrected. No other figures or tables are affected by this alteration.

Table 7.4: General government sector balance sheet

($ million)						
as at 30 June	*2005 (a) Opening*	*2006 Budget*	*2006 Revised*	*2007 Estimate*	*2008 Estimate*	*2009 Estimate*
Assets						
Financial assets						
Cash and deposits	1 803	1 796	1 789	1 474	1 059	944
Advances paid	96	95	95	92	89	86
Investments, loans and placements	2 626	2 255	2 253	1 152	1 044	1 012
Other non-equity assets	2 673	2 586	2 380	2 643	2 801	2 987
Equity	36 811	37 492	37 459	38 336	39 093	39 548
Total financial assets	**44 009**	**44 225**	**43 976**	**43 697**	**44 086**	**44 577**
Non-financial assets						
Land and fixed assets	50 988	55 016	55 117	58 785	62 274	66 079
Other non-financial assets	2 144	2 148	2 148	2 112	2 086	2 043
Total non-financial assets	**53 132**	**57 163**	**57 265**	**60 897**	**64 360**	**68 122**
Total assets	**97 141**	**101 388**	**101 241**	**104 594**	**108 446**	**112 699**
Liabilities						
Deposits held	450	456	456	462	469	477
Advances received	9	9	9	8	7	7
Borrowing	5 550	6 183	6 185	6 189	6 478	6 977
Superannuation liability	15 288	15 937	14 722	15 063	15 109	15 042
Other employee entitlements and provisions	3 975	4 207	4 221	4 369	4 480	4 593
Other non-equity liabilities	3 487	3 487	3 413	3 303	3 200	3 129
Total liabilities	**28 758**	**30 279**	**29 006**	**29 394**	**29 744**	**30 224**
Net worth	**68 383**	**71 109**	**72 235**	**75 200**	**78 703**	**82 475**
Net financial worth (b)	**15 251**	**13 946**	**14 970**	**14 303**	**14 343**	**14 353**
Net debt (c)	**1 484**	**2 501**	**2 513**	**3 941**	**4 762**	**5 418**

Source: Department of Treasury and Finance

Notes:

(a) *The opening balances of 1 July 2005 are based on the most recent audited financial reports of consolidated entities adjusted for the adoption of A-IFRS.*

(b) *Net financial worth equals total financial assets minus total liabilities.*

(c) *Net debt equals the sum of deposits held, advances received and borrowings, minus the sum of cash and deposits, advances paid, and investments, loans and placements.*

Table 7.5: Public non-financial corporations sector balance sheet

($ million)				
as at 30 June	*2005 [(a)] Opening*	*2006 Budget*	*2006 Revised*	*2007 Estimate*
Assets				
Financial assets				
Cash and deposits	518	522	423	304
Advances paid	159	134	134	117
Investments, loans and placements	1 115	847	835	782
Other non-equity assets	1 566	1 510	1 474	1 412
Equity	..	..	..	..
Total financial assets	**3 357**	**3 012**	**2 866**	**2 615**
Non-financial assets				
Land and fixed assets	38 148	39 579	39 172	40 627
Other non-financial assets	196	179	280	326
Total non-financial assets	**38 344**	**39 758**	**39 451**	**40 953**
Total assets	**41 702**	**42 770**	**42 317**	**43 567**
Liabilities				
Deposits held	87	83	69	50
Advances received	11	9	7	5
Borrowing	4 181	4 506	4 257	4 604
Superannuation liability	57	57	58	57
Other employee entitlements and provisions	2 682	2 731	2 716	2 743
Other non-equity liabilities	745	765	623	644
Total liabilities	**7 763**	**8 151**	**7 730**	**8 104**
Shares and other contributed capital	**33 939**	**34 619**	**34 587**	**35 464**
Net worth	**..**	**..**	**..**	**..**
Net financial worth [(b)]	**-38 344**	**-39 758**	**-39 451**	**-40 953**
Net debt [(c)]	**2 487**	**3 095**	**2 941**	**3 456**

Source: Department of Treasury and Finance

Notes:

(a) *The opening balances of 1 July 2005 are based on the most recent audited financial reports of consolidated entities adjusted for the adoption of A-IFRS.*

(b) *Net financial worth equals total financial assets minus total liabilities minus shares and other contributed capital.*

(c) *Net debt equals the sum of deposits held, advances received and borrowings, minus the sum of cash and deposits, advances paid, and investments, loans and placements.*

Table 7.6: Non-financial public sector balance sheet

($ million)				
as at 30 June	*2005 (a) Opening*	*2006 Budget*	*2006 Revised*	*2007 Estimate*
Assets				
Financial assets				
Cash and deposits	2 322	2 317	2 211	1 778
Advances paid	254	228	228	210
Investments, loans and placements	3 740	3 102	3 088	1 934
Other non-equity assets	3 041	2 974	2 702	2 969
Equity	2 872	2 872	2 872	2 872
Total financial assets	**12 229**	**11 494**	**11 101**	**9 764**
Non-financial assets				
Land and fixed assets	89 136	94 595	94 288	99 411
Other non-financial assets	2 312	2 299	2 381	2 380
Total non-financial assets	**91 448**	**96 894**	**96 669**	**101 791**
Total assets	**103 676**	**108 389**	**107 770**	**111 555**
Liabilities				
Deposits held	537	539	525	512
Advances received	20	17	15	13
Borrowing	9 730	10 688	10 441	10 791
Superannuation liability	15 345	15 994	14 779	15 120
Other employee entitlements and provisions	5 677	5 899	5 892	5 973
Other non-equity liabilities	3 043	3 131	2 916	2 891
Total liabilities	**34 352**	**36 268**	**34 568**	**35 302**
Net worth	**69 325**	**72 120**	**73 202**	**76 253**
Net financial worth (b)	**-22 123**	**-24 774**	**-23 467**	**-25 538**
Net debt (c)	**3 971**	**5 596**	**5 454**	**7 394**

Source: Department of Treasury and Finance

Notes:

(a) The opening balances of 1 July 2005 are based on the most recent audited financial reports of consolidated entities adjusted for the adoption of A-IFRS.

(b) Net financial worth equals total financial assets minus total liabilities.

(c) Net debt equals the sum of deposits held, advances received and borrowings, minus the sum of cash and deposits, advances paid, and investments, loans and placements.

Table 7.7: General government sector cash flow statement

($ million)

	2005-06 [(a)] Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Cash receipts from operating activities					
Taxes received	10 386	10 533	10 911	11 103	11 529
Receipts from sales of goods and services	3 529	3 568	3 674	3 708	3 743
Grants/subsidies received	14 262	14 340	14 869	15 422	16 043
Other receipts	2 554	2 684	2 078	2 325	2 240
Total receipts	**30 731**	**31 124**	**31 531**	**32 559**	**33 555**
Cash payments from operating activities					
Payment for goods and services	-22 037	-22 233	-23 659	-24 729	-25 784
Grants and subsidies paid	-5 058	-5 174	-5 053	-5 038	-4 996
Interest paid	- 416	- 414	- 418	- 418	- 432
Other payments	- 641	- 623	- 659	- 665	- 659
Total payments	**-28 153**	**-28 444**	**-29 789**	**-30 849**	**-31 872**
Net cash flows from operating activities	**2 579**	**2 681**	**1 741**	**1 710**	**1 683**
Net cash flows from investing in non-financial assets					
Sales of non-financial assets	134	138	144	210	121
Purchases of non-financial assets	-2 529	-2 590	-2 599	-2 416	-2 362
Total cash flows - non-financial assets	**-2 395**	**-2 452**	**-2 455**	**-2 206**	**-2 241**
Net cash flows from investments in financial assets for policy purposes	**- 569**	**- 625**	**- 707**	**- 321**	**- 78**
Net cash flows from investments in financial assets for liquidity	**370**	**373**	**1 101**	**108**	**32**
Net cash flows from financing activities					
Advances received (net)	- 1	- 1	- 1	- 1	- 1
Borrowings (net)	9	9	6	294	490
Deposits received (net)	..	..	..	..	..
Other financing (net)	..	..	..	..	..
Net cash flows from financing activities	**8**	**9**	**5**	**293**	**489**
Net increase in cash held	**- 7**	**- 15**	**- 315**	**- 415**	**- 115**
Surplus (+) /deficit (-) excluding acquisitions under finance leases [(b)]	**183**	**229**	**- 714**	**- 496**	**- 558**
Acquisitions under finance leases	615	615	..	..	..
Surplus (+) /deficit (-) including finance leases	**- 432**	**- 386**	**- 714**	**- 496**	**- 558**

Source: Department of Treasury and Finance

Notes:
(a) The 2005-06 Budget have been adjusted to reflect changes in GFS classifications.
(b) Net cash flows from operating activities less investments in non-financial assets.

Table 7.8: Public non-financial corporations sector cash flow statement

($ million)

	2005-06 [(a)] Budget	*2005-06 Revised*	*2006-07 Estimate*
Cash receipts from operating activities			
Receipts from sales of goods and services	3 346	3 345	3 443
Grants/subsidies received	1 668	1 788	1 766
Other receipts	408	307	293
Total receipts	**5 422**	**5 440**	**5 502**
Cash payments from operating activities			
Payment for goods and services	-2 878	-2 987	-2 862
Grants and subsidies paid	- 166	- 199	- 179
Interest paid	- 328	- 302	- 337
Other payments	- 946	- 952	- 978
Total payments	**-4 318**	**-4 440**	**-4 356**
Net cash flows from operating activities	**1 104**	**1 000**	**1 146**
Net cash flows from investing in non-financial assets			
Sales of non-financial assets	78	72	67
Purchases of non-financial assets	-1 870	-1 704	-2 044
Total cash flows from investing in non-financial assets	**-1 792**	**-1 633**	**-1 977**
Net cash flows from investments in financial assets for policy purposes	**575**	**632**	**711**
Net cash flows from investments in financial assets for liquidity purposes	**267**	**280**	**53**
Net cash flows from financing activities			
Advances received (net)	- 2	- 4	- 1
Borrowings (net)	328	80	350
Deposits received (net)	..	..	..
Distributions paid	- 477	- 450	- 400
Other Financing (net)	..	..	..
Total net cash flows from financing activities	**- 151**	**- 375**	**- 51**
Net increase in cash held	**3**	**- 95**	**- 119**
Surplus (+) /deficit (-) excluding acquisitions under finance leases [(b)]	**-1 165**	**-1 082**	**-1 231**
Acquisition of assets under finance leases and similar arrangements	..	..	..
Surplus (+) /deficit (-) including finance leases	**-1 165**	**-1 082**	**-1 231**

Source: Department of Treasury and Finance

Notes:

(a) The 2005-06 Budget have been adjusted to reflect changes in GFS classifications.

(b) Net cash flows from operating activities less investments in non-financial assets and distributions paid.

Table 7.9: Non-financial public sector cash flow statement

($ million)

	2005-06 [(a)] Budget	2005-06 Revised	2006-07 Estimate
Cash receipts from operating activities			
Taxes received	10 242	10 401	10 773
Receipts from sales of goods and services	6 058	6 096	6 301
Grants/subsidies received	14 264	14 368	14 888
Other receipts	2 369	2 486	1 915
Total receipts	**32 933**	**33 351**	**33 877**
Cash payments from operating activities			
Payment for goods and services	-24 863	-25 146	-26 453
Grants and subsidies paid	-3 509	-3 644	-3 503
Interest paid	- 744	- 715	- 755
Other payments	- 612	- 614	- 675
Total payments	**-29 727**	**-30 120**	**-31 387**
Net cash flows from operating activities	**3 206**	**3 231**	**2 490**
Net cash flows from investing in non-financial assets			
Sales of non-financial assets	212	210	211
Purchases of non-financial assets	-4 399	-4 294	-4 643
Total cash flows from investing in non-financial assets	**-4 187**	**-4 084**	**-4 432**
Net cash flows from investments in financial assets for policy purposes	**6**	**7**	**1**
Net cash flows from investments in financial assets for liquidity purposes	**638**	**653**	**1 153**
Net cash flows from financing activities			
Advances received (net)	- 3	- 5	- 2
Borrowings (net)	337	89	356
Deposits received (net)	..	..	..
Other financing (net)	**..**	**..**	**..**
Total net cash flows from financing activities	**334**	**84**	**354**
Net increase in cash held	**- 4**	**- 109**	**- 434**
Surplus (+) /deficit (-) excluding acquisitions under finance leases [(b)]	**- 982**	**- 853**	**-1 942**
Acquisition of assets under finance leases and similar arrangements	615	615	..
Surplus (+) /deficit (-) including finance leases	**-1 597**	**-1 468**	**-1 942**

Source: Department of Treasury and Finance

Notes:

(a) The 2005-06 Budget have been adjusted to reflect changes in GFS classifications.

(b) Net cash flows from operating activities less investments in non-financial assets.

Table 7.10: General government AAS 31 net result reconciled to GFS measures

($ million)

	2005-06 Budget	2005-06 Revised	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
General government net result from transactions	**365**	**331**	**317**	**413**	**518**
equals: **General government net operating balance (GFS)**					
Less: Gross fixed capital formation	3 032	3 076	2 455	2 206	2 355
Plus: Depreciation	1 235	1 222	1 285	1 371	1 440
Less: Change in inventories	..	..	1	1	1
GFS net lending(+)/borrowing(-)	**-1 433**	**-1 524**	**- 854**	**- 422**	**- 398**
Plus:					
Superannuation expense (difference between operating statement, including nominal interest, and cash flow statement)	649	638	341	46	- 67
Acquisitions under finance leases	615	615	..	..	..
Other non-cash items	- 263	- 115	- 201	- 120	- 93
GFS cash surplus(+)/deficit(-)	**- 432**	**- 386**	**- 714**	**- 496**	**- 558**
Less: Net contributions to other sectors of government	569	625	707	321	78
Other non-cash items	16	18	7	4	20
Decrease in general government net debt	**-1 017**	**-1 029**	**-1 429**	**- 821**	**- 656**

Source: Department of Treasury and Finance

Victoria's 2005–06 Loan Council Allocation

As required under the Uniform Presentation Framework, Victoria is required to publish the Loan Council Allocation (LCA) estimates. The LCA is a measure of each government's net call on financial markets in a given financial year to meet its budget obligations. The method of public release is the responsibility of each individual jurisdiction. Victoria discloses its LCA information through the Financial Report for the State of Victoria, Budget Paper No. 4, *Statement of Finances* and Budget Update.

Table 7.11 compares Victoria's 2005-06 LCA as approved by Loan Council in March 2005 with the revised LCA based on *2005-06 Budget Update* estimates.

Table 7.11: Loan Council Allocation 2005–06

($ million)

	2005-06 Nomination [(a)]	*2005-06 Revised*
General government sector cash (+) deficit / (-) surplus	- 46	386
Public non-financial corporation sector cash (+) deficit / (-) surplus	761	1 082
Non-financial public sector cash (+) deficit / (-) surplus [(b)]	715	1 468
Less: Net cash flows from investments in financial assets for policy purposes [(c)]	9	7
Plus: Memorandum items [(d)]	440	117
Loan Council Allocation	**1 146**	**1 578**
Tolerance limit (2 per cent of non-financial public sector cash receipts from operating activities) [(e)]	642	642

Source: Department of Treasury and Finance

Notes:

(a) *2005-06 Budget Paper No 4, Statement of Finances.*

(b) *The sum of the surplus/deficit of the general government and public non-financial corporation sector does not directly equal the non-financial public sector surplus due to intersectoral transfers, which are netted out in the calculation of the non-financial public sector figure. Surplus (+)/deficit(-) includes finance lease acquisitions.*

(c) *The non-financial public sector surplus/deficit relating to 2005-06 includes net cash flows from investments in financial assets for policy purposes.*

(d) *Memorandum items are used to adjust the ABS deficit to include in LCAs certain transactions, such as operating leases, that have many of the characteristics of public sector borrowings but do not constitute formal borrowings. They are also used, where appropriate, to deduct from the ABS deficit certain transactions that Loan Council has agreed should not be included in LCAs (e.g. the over/under funding of employers' emerging costs under public sector superannuation schemes, or borrowings by entities such as statutory marketing authorities).*

(e) *A tolerance limit equal to 2 per cent of 'total non-financial public sector cash receipts from operating activities' (2004-05 Budget Update) applies to jurisdictions' LCA nomination and revised LCA at budget time, and between the budget time LCA and LCA outcome. The tolerance limit applying to Victoria in 2005-06 is $642 million (2 per cent of $32 094 million – sourced from 2004-05 Budget Update).*

As part of the Loan Council arrangements, Loan Council has agreed that if at any time a jurisdiction finds that it is likely to exceed its tolerance limit, in either direction, it is required to provide an explanation to Loan Council and, in line with the emphasis of increased transparency, to make the explanation public. The 2005-06 revised LCA (deficit of $1 578 million) remained within the tolerance limit. The change of $432 million in the LCA between *2005-06 nomination and 2005-06 revised* is mainly due to:

- a revision in the general government sector cash position from $46 million surplus to $386 million deficit primarily due to a significant increase in capital expenditures arising from Government initiatives announced in the 2005-06 Budget and the completion of two new prisons;
- an increase in the public non-financial corporations sector cash deficit of $321 million is due to:
  - an increase in payments for goods and services across the public non-financial corporations sector, partially offset by grants and subsidies received to fund other operating expenses of the sector; and
  - an increase in capital expenditures primarily to fund additional rolling stock, rail infrastructure, a new transport ticketing system and capital works on new housing estates;
- partially offset by a reduction in memorandum items of $323 million. The reduction in memorandum items is driven by a reduction in borrowing requirements of universities and a reduction in the operating lease commitments across the general government sector.

Infrastructure projects

In the interests of transparency, the State is required to disclose the details of infrastructure projects with private sector involvement and to report full contingent exposure, if any. Exposure is to be measured by the Government's termination liabilities in a case of private sector default and disclosed as a footnote to, rather than a component of, LCAs.

Listed below are details of Melbourne Convention Centre redevelopment, Central Highlands Water – Ballarat North Water Reclamation and Barwon Water – Biosolids Management, which are expected to be contracted in the 2005-06 financial year.

Melbourne Convention Centre redevelopment

This redevelopment will be the largest of its kind in Australia. The redevelopment will integrate a convention centre, which will include a 5 000 seat plenary hall, with the existing exhibition centre and broader Southbank site.

The Government allocated $367 million to the Melbourne Convention Centre redevelopment in the 2004-05 Budget process.

The project contract is expected to include an obligation for the Government to make a payment to the contractor should Government terminate the contract for default. The quantum of the payment is not expected to exceed the remaining balance of the approved project funding at any time.

Central Highlands Water – Ballarat North Water reclamation

Central Highlands Water is seeking to implement a wastewater treatment re-use project in order to comply with licence conditions set by the Environment Protection Authority for the Ballarat North wastewater treatment plant.

The project is being procured on a Design-Build-Operate basis, and it is therefore not expected that there will be any significant termination payment payable by the Government on contractor default.

Barwon Water – Biosolids Management

The objective of this project is to manage the biosolids removed during the sewage treatment process at Black Rock Sewage Treatment Plant and other treatment plants in the Barwon Water region. Management of biosolids includes a treatment process to ensure that the final product is suitable for beneficial re-use in accordance with EPA requirements.

The project contract is expected to include an obligation for the Government to make a payment to the contractor should the Government terminate the contract for default. The quantum of the payment is not expected to exceed the remaining balance of the approved project funding at any time.

APPENDIX A: SPECIFIC POLICY INITIATIVES AFFECTING THE BUDGET POSITION

Appendix A outlines output, asset investment and revenue initiatives since the 2005-06 Budget.

The following tables provide details of output and asset initiatives in relation to:

- *Moving Forward – Making Provincial Victoria the Best Place to Live, Work and Invest*; and
- Other department specific initiatives.

Revenue initiatives are at the end of this appendix. Except where specified, figures indicate the total cost of initiatives. Funding from reprioritisation, contingencies and other existing funding sources has not been deducted from the total cost of the initiatives.

MOVING FORWARD – MAKING PROVINCIAL VICTORIA THE BEST PLACE TO LIVE, WORK AND INVEST

Forming a key part of the *2005-06 Budget Update* are the initiatives announced in *Moving Forward*. This statement, released on 14 November 2005, will build on the strength of regional economies and communities, and unlock the potential for future growth in provincial Victoria. For further detail on these initiatives, refer to the *Moving Forward* statement.

Education and Training

Output initiatives

($ million)					
	2005-06	*2006-07*	*2007-08*	*2008-09*	*2009-10*
New training opportunities in areas of high regional demand	..	1.8	4.5	4.3	4.8
Total output initiatives	**..**	**1.8**	**4.5**	**4.3**	**4.8**

Source: Department of Treasury and Finance

New training opportunities in areas of high regional demand

This initiative will provide additional training to existing workers, apprenticeships and traineeships, pre-apprenticeships and pre-vocational training in areas of high demand.

Infrastructure

Output initiatives

($ million)					
	2005-06	*2006-07*	*2007-08*	*2008-09*	*2009-10*
A new provincial unit within VicUrban	..	0.7	0.7	0.7	0.7
Creating new bus and transport connections	2.3	5.9	8.2	8.2	8.2
Refitting V/Line's regional train fleet	..	3.3	3.3	3.3	3.3
Total output initiatives	**2.3**	**9.9**	**12.2**	**12.2**	**12.2**

Source: Department of Treasury and Finance

A new provincial unit within VicUrban

Funding is provided to establish a provincial unit within VicUrban. The unit will identify potential sites for new commercial housing in regional areas, form partnerships with local councils to facilitate new housing developments, provide technical advice and information and conduct research into issues with an impact on commercial housing in provincial Victoria.

Creating new bus and transport connections

Funding is provided for new and enhanced bus services in regional towns and cities experiencing strong population growth, such as Ballarat, Bendigo, Geelong, Shepparton, Mildura, Yarrawonga, Wodonga, Hamilton, Warnambool, Echuca, Wangaratta, Wallan and Kilmore. Improved bus services will also be provided to connect small towns in remote regions, as well as new bus services that connect to the revitalised rail network such as Marshall station to Torquay, Jan Juc, Ocean Grove, Barwon Heads and Warun Ponds. These services will support access to work, education, community services and recreation.

Refitting V/Line's regional train fleet

Funding is provided to refit V/Line's regional fleet of locomotive-hauled carriages and Sprinter cars. Trains will be refurbished with new soft furnishings, upgraded toilets and washrooms and exterior livery. The refurbishment will ensure the locomotive hauled and sprinter fleet has a similar standard of presentation and comfort to the new V'Locity trains.

Asset initiatives

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*	*TEI*
Creating new bus and transport connections	..	2.0	3.0	..	5.0
Total asset investment	**..**	**2.0**	**3.0**	**..**	**5.0**

Source: Department of Treasury and Finance

Creating new bus and transport connections

New Park and Ride facilities will be provided at key commuter locations for inter-urban rail travel to Melbourne, offering secure parking and improved passenger facilities at existing stations.

Innovation, Industry and Regional Development

Output initiatives

($ million)	*2005-06*	*2006-07*	*2007-08*	*2008-09*	*2009-10*
Creating a new Provincial Victoria Growth Fund	6.5	18.5	25.0	25.0	25.0
Cooperative Research Centre for innovative dairy products	..	0.1	0.1	0.1	..
Centre for Energy and Greenhouse Technologies	7.0	5.0	3.0	..	..
Renewing the Regional Infrastructure Development Fund	25.0	37.0	36.0	41.0	61.0
Four seasons energy pilots	..	0.5	0.5	..	..
Total output initiatives	**38.5**	**61.1**	**64.6**	**66.1**	**86.0**

Source: Department of Treasury and Finance

Creating a new Provincial Victoria Growth Fund

The Government will provide funding to establish a new Provincial Victoria Growth Fund to deliver increased support to: help regional councils, business and communities; market and promote provincial Victoria; identify and capture new business and investment opportunities; tackle skills shortages; and manage and plan for growth and change.

Cooperative Research Centre for innovative dairy products

The Cooperative Research Centre (CRC) undertakes important research in genetics, reproductive technologies and resistance to disease. The Government will provide funding to support the work of the CRC – in particular to work with local companies to establish a commercially-focused project in bioactive products.

Centre for Energy and Greenhouse Technologies

The Government will provide funding to support the work of the Centre for Energy and Greenhouse Technologies, which aims to facilitate investment in new sustainable energy and greenhouse gas reduction technologies.

Renewing the Regional Infrastructure Development Fund

Funding is provided to assist in developing economic, tourism and community infrastructure in regional Victoria by extending the Regional Infrastructure Development Fund (RIDF). The extension to RIDF will include a funding boost to and broadening of the Small Towns Development Fund, a new intermodal freight program, provincial pathways, support for the dairy industry and new regional ports infrastructure.

Four seasons energy pilots

Funding is provided to establish a two-year pilot program to demonstrate alternative heating and cooling sources of energy for regional communities.

Premier and Cabinet

Output initiatives

	($ million)				
	2005-06	*2006-07*	*2007-08*	*2008-09*	*2009-10*
Growing regional arts	..	2.0	2.0	2.0	2.0
Total output initiatives	**..**	**2.0**	**2.0**	**2.0**	**2.0**

Source: Department of Treasury and Finance

Growing regional arts

This initiative will provide funding for: professional/programming infrastructure for performing art centres and galleries; regional student access programs for regional cultural facilities; and promotion of provincial locations to film and television production companies. This initiative will also enable mainstream shows selected from major metropolitan institutions and companies to tour in provincial Victoria.

Primary Industries

Output initiatives

	($ million)				
	2005-06	*2006-07*	*2007-08*	*2008-09*	*2009-10*
Establishing a Sustainable Timber Industry Council	..	0.1	0.1	0.1	0.1
Developing gold undercover	..	3.0	3.0	3.0	..
Developing the Latrobe Valley's resources future	..	0.5	0.5	0.5	..
Developing streamlined property management systems	..	1.3	1.3	1.4	1.0
Services and information for new land managers	..	0.8	0.8	0.8	0.8
Tackling weeds and pests in high risk rural areas	..	1.0	1.5	2.7	1.0
Total output initiatives	**..**	**6.6**	**7.1**	**8.4**	**2.8**

Source: Department of Treasury and Finance

Establishing a Sustainable Timber Industry Council

Funding of $250 000 over 4 years is provided to establish a Sustainable Timber Industry Council, providing advice to the Minister for Agriculture on broad strategic issues affecting the forest and timber industries dependent on public and private forest resources. The Council will be a non-statutory advisory body drawing on high-level forestry and timber industry expertise.

Developing gold undercover

Funding is provided to attract greater investment for gold exploration to Victoria and open up new exploration in areas adjacent to the State's 'golden triangle', where limited or no exploration has taken place. A key part of this initiative will be the expansion and further development of geoscience data and the online delivery mechanisms to supply information to potential investors quickly and efficiently.

Developing the Latrobe Valley's resources future

Funding is provided to support and encourage new brown coal based investment in the Latrobe Valley. The project effectively implements the recommendations arising from the Latrobe Valley 2100 Coal Resource Project, and will include producing a strategic plan to develop the Latrobe Valley's resources, creating new investment opportunities for downstream coal products and preparing commercialisation strategies arising from the coal research and development program.

Developing streamlined property management systems

Funding is provided to streamline property management systems and reduce environmental and planning 'red tape' for Victorian farmers. The project will assist Victoria to participate in current national discussions on Environmental Management Systems (EMS) certification, strengthen capacity of Victorian farmers to implement sustainable farming systems and support industry-driven uptake of EMS.

Services and information for new land managers

Funding is provided to engage new land managers more effectively on their expectations of living in rural Victoria and ensure that they are aware of appropriate land management practices and their obligations as land managers.

Tackling weeds and pests in high risk rural areas

Funding is provided to tackle weeds and pests in regions with growing urban environments and higher-density housing. The project will include investigating and assessing high-value interface areas in provincial Victoria, providing education and awareness programs, increasing support to landcare groups and improving access to bait for pest animal management.

Sustainability and Environment

Output initiatives

($ million)	2005-06	2006-07	2007-08	2008-09	2009-10
Keeping the Port of Lakes Entrance open	..	5.9	7.5	3.8	6.2
Total output initiatives	**..**	**5.9**	**7.5**	**3.8**	**6.2**

Source: Department of Treasury and Finance

Keeping the Port of Lakes Entrance open

As part of the *Moving Forward* Statement, the Government has provided $31.5 million over six years (output and asset funding) to install a comprehensive sand management system, including a sand bypassing system, to keep the Port of Lakes Entrance open. The project will also establish a monitoring regime for sand movements inside and outside the port entrance, improve existing sand management in the adjacent Gippsland Lakes, replace the Sandpiper dredge, and trial a dredge hopper for the future phase out of the April Hamer dredge.

Asset initiatives

($ million)	2005-06	2006-07	2007-08	2008-09	TEI
A new deal for regional local ports [(a)]	..	7.5	7.5	7.5	30.0
Keeping the Port of Lakes Entrance open	3.0	..	..	0.5	4.4
Total asset investment	**3.0**	**7.5**	**7.5**	**8.0**	**34.4**

Source: Department of Treasury and Finance

Note:
(a) This includes allocations sourced from Regional Infrastructure Development Fund.

A New Deal for regional local ports

As part of the *Moving Forward* Statement, funding of $30 million has been provided to maintain and upgrade port assets to enhance access and safety, improve the delivery of services to local communities and support local fishing and tourism. Ports likely to benefit from this program are Port Fairy, Warrnambool, Apollo Bay, Mallacoota, Gippsland Lakes, Portarlington, Anderson Inlet, Snowy River, Port Campbell and Port Albert.

Victorian Communities

Output initiatives

($ million)	*2005-06*	*2006-07*	*2007-08*	*2008-09*	*2009-10*
Skills and jobs for disadvantaged workers	..	1.1	1.1	1.1	0.0
Extending the country football and netball program	..	1.5	1.5	1.5	1.5
Total output initiatives	**..**	**2.6**	**2.6**	**2.6**	**1.5**

Source: Department of Treasury and Finance

Skills and jobs for disadvantaged workers

This initiative will skill up and secure work for disadvantaged job seekers in regional areas. The program will assist the transport and distribution industry in the North East and manufacturing industry in Western Victoria by providing services which may include transport, mentoring, counselling and/or housing assistance to employers, councils, unions and others to tackle skilled labour shortages and fill vacancies in these industry areas.

Extending the country football and netball program

This initiative seeks to increase the level of support for country sporting organisations through the provision of improved playing surfaces and the upgrade of shared community, club and social facilities for football and netball clubs across provincial Victoria.

DEPARTMENTAL OUTPUT AND ASSET INITIATIVES

Education and Training

Output initiatives

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*
Services to students with disabilities	35.4	54.9	75.5	25.0
Drought assistance to families	0.2	0.2	..	..
Total output initiatives	**35.6**	**55.1**	**75.5**	**25.0**

Source: Department of Treasury and Finance

Services to students with disabilities

Additional funding is provided to the Program for Students with Disabilities to manage increased demand for services provided to government school students with special education needs.

Drought assistance to families

Additional funding is provided to help schools provide additional support for students in drought affected areas.

Human Services

Output initiatives

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*
Safety of children in care	6.9	14.6	16.3	17.8
Total output initiatives	**6.9**	**14.6**	**16.3**	**17.8**

Source: Department of Treasury and Finance

Safety of children in care

This initiative builds on existing reforms in child protection services and provides additional child protection workers and grants to community service organisations to strengthen the protection of children in care. Funding will also enable the implementation of additional support strategies for foster carers and training for child protection workers to ensure improved standards in child protection practice and promote healthy development of vulnerable children.

Asset initiatives

($ million)	2005-06	2006-07	2007-08	2008-09	TEI
Alfred Hospital Intensive Care Unit redevelopment	0.7	11.0	8.5	..	20.2
Royal Children's Hospital	n.a.	n.a.	n.a.	n.a.	847.4
Total asset investment	**0.7**	**11.0**	**8.5**	**..**	**867.6**

Source: Department of Treasury and Finance

Alfred Hospital Intensive Care Unit redevelopment

This initiative will enable the redevelopment and upgrade of the Alfred Hospital Intensive Care Unit. This funding will enable the Alfred Hospital to continue to provide high quality medical services to patients requiring intensive care in the best practice clinical environment.

Royal Children's Hospital

Funding is provided to re-build the Royal Children's Hospital (RCH) to the west of the existing site. The existing hospital buildings will be demolished with the exception of two modern buildings on the site, the front entry building and the ten storey research centre, which will be retained as part of the new hospital. The remainder of the existing site will be returned to parkland. The new RCH will have the capacity to treat an extra 35 000 patients a year with improved accommodation and facilities such as more single rooms, neonatal cots and operating theatres with parking for 2 000 cars in a new underground carpark. The project will be constructed under the *Partnerships Victoria* model with a private sector consortium building and maintaining the hospital for 25 years with the Government owning and operating the RCH.

Infrastructure

Output initiatives

($ million)	2005-06	2006-07	2007-08	2008-09
Additional public transport to Mildura	2.0	6.1	6.3	6.5
'World class Victoria' infrastructure campaign	3.0	..	..	..
Major projects stakeholder program	2.0	..	..	..
Motorcycle safety	3.2	4.2	1.1	..
New ticketing system [(a)]	..	..	..	..
Vehicle impoundment [(b)]	..	0.2	0.2	0.2
Total output initiatives	**10.2**	**10.5**	**7.6**	**6.7**

Source: Department of Treasury and Finance

Notes:
(a) Project output funding will be finalised as part of the 2006-07 Budget.
(b) Refer to Department of Justice Vehicle impoundment output initiative for description of this initiative.

Additional public transport to Mildura

Funding is provided for additional public transport services between Melbourne and Mildura. An extra train and coach service will operate daily, providing a more convenient connection to Mildura.

'World class Victoria' infrastructure campaign

Funding is provided to develop a high-level public information campaign that will maximise understanding of the contribution that infrastructure investments make to the economic strengths and competitive advantages of Victoria. By highlighting key infrastructure investments across all portfolios of government, the campaign is intended to maximise awareness and understanding among business decision makers, the general public and other key local and external audiences. The campaign will integrate with the broader 'World class Victoria' campaign.

Major projects stakeholder program

Funding is provided to develop a targeted program of events and activities throughout 2005-06 that are designed to promote strong relationships with key stakeholders in the major projects industry across Victoria.

Motorcycle safety

The Transport Accident Commission motor cycle safety fund has been extended for two years and will continue to invest in various programs aimed at improving road safety for motorcyclists. Funding will continue to support the Motorcycle Blackspot Program, and improvements in motorcycle education, training, and engineering technologies.

New ticketing system

Funding is provided for the design, development and implementation of a new ticketing system, based on re-usable Smartcard technology, to be rolled out in 2007. The new Smartcard will work across metropolitan trains, trams and buses, and V/Line coach and major regional bus services. It will deliver faster, easier, smoother and safer travel for Victoria's public transport customers.

Asset initiatives

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*	*TEI*
Central Pier	3.6	..	..	..	3.6
New ticketing system	63.8	121.8	87.8	0.8	290.0
Vehicle impoundment [(a)]	0.4	..	..	..	0.4
Total asset investment	**67.8**	**121.8**	**87.8**	**0.8**	**294.0**

Source: Department of Treasury and Finance

Note:
(a) Refer to Department of Justice Vehicle impoundment output initiative for description of this initiative.

Central Pier

Funding is provided to improve the appearance and condition of Central Pier in Docklands to allow public access ahead of the Volvo Ocean Race and Commonwealth Games in early 2006.

New ticketing system

Refer to the output initiative for a description of this initiative.

Innovation, Industry and Regional Development

Output initiatives

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*
Business development and manufacturing industries stakeholder program	0.5	..	..	..
'World class Victoria' business investment campaign	3.0	..	..	..
Walter and Eliza Hall Institute Expansion	30.0	5.0	5.0	5.0
Total output initiatives	**33.5**	**5.0**	**5.0**	**5.0**

Source: Department of Treasury and Finance

Business development and manufacturing industries stakeholder program

Funding is provided to develop industry development programs and initiatives to promote investment in consultation with industry. The programs aim to engage key industry sectors, general public and business groups.

'World class Victoria' business investment campaign

To leverage off the investment opportunities presented by the Commonwealth Games funding is provided to develop a high-level public information campaign that will encourage widespread awareness of Victoria's economic strengths and competitive advantages, especially among business decision makers. By highlighting successful businesses and individuals, the campaign is intended to acknowledge the contribution that business makes to Victoria as well as to encourage traffic to the new *business.vic.gov.au* website and the Victorian Business Line. The campaign will introduce the campaign theme 'World class Victoria'.

Walter and Eliza Hall Institute expansion

Funding is provided to support the building of a new seven storey western wing at Walter and Eliza Hall Institute's Parkville laboratories. Expanding Walter and Eliza Hall Institute will enable this world leading research centre to undertake new research activities, invest in new technology, develop future research leaders and generate new health benefits from its research for the community.

Justice

Output initiatives

($ million)	2005-06	2006-07	2007-08	2008-09
Vehicle impoundment	0.9	3.3	3.4	3.5
Crime Prevention Victoria	2.0	..	..	..
Road safety cameras	..	12.1	12.5	12.7
Total output initiatives	**2.9**	**15.4**	**15.9**	**16.2**

Source: Department of Treasury and Finance

Vehicle impoundment

Funding has been provided to support legislation enabling Victoria Police to better respond to reckless drivers. Funding will cover the costs of impounding vehicles, employing a new magistrate and an additional senior police constable. Impoundment costs will be recovered from offenders who will need to pay impoundment costs before their vehicle is released.

Crime Prevention Victoria

Funding has been provided for an education campaign to improve Victorian's confidence in their safety, with the focus on feeling secure at home.

Road safety cameras

Funding has been provided for the maintenance of the fixed safety camera system to ensure ongoing compliance with road safety measures by Victorian drivers.

Premier and Cabinet

Output initiatives

($ million)	2005-06	2006-07	2007-08	2008-09
State Architect	0.6	1.3	1.3	1.3
National Gallery of Victoria – Insurance	1.0	0.4	1.1	1.2
Total output initiatives	**1.6**	**1.7**	**2.4**	**2.5**

Source: Department of Treasury and Finance

State Architect

Funding is provided for the establishment and the ongoing operation of the State Architect. Funding of $25 000 per year will also be provided for minor capital items associated with this initiative.

National Gallery of Victoria – Insurance

Additional funding is provided for insurance for the State collection at National Gallery of Victoria.

Asset initiatives

($ million)	2005-06	2006-07	2007-08	2008-09	TEI
Spotswood	7.0	..	..	..	7.0
Total asset investment	**7.0**	**..**	**..**	**..**	**7.0**

Source: Department of Treasury and Finance

Spotswood

Funding is provided for the purchase of land and the development of a carpark for Museum Victoria's Scienceworks campus at Spotswood.

Primary Industries

Output initiatives

($ million)	2005-06	2006-07	2007-08	2008-09
Farming family shire rate assistance	5.6	4.4	..	..
Total output initiatives	**5.6**	**4.4**	**..**	**..**

Source: Department of Treasury and Finance

Farming family shire rate assistance

Funding is provided to ensure additional support for farming families affected by the prolonged drought. This additional assistance will come through the farming family shire rate assistance package and be available to those in Commonwealth declared exceptional circumstances drought-affected areas of the State.

Sustainability and Environment

Asset initiatives

	($ million)				
	2005-06	*2006-07*	*2007-08*	*2008-09*	*TEI*
Additional funding for Piping the System - Wimmera Mallee (state component)	..	..	..	..	42.0
Development contribution infrastructure initiatives [(a)]	..	53.0	66.0	68.0	n.a.
Gippsland Water Factory	25.0	..	..	..	25.0
Mt Buller water recycling	1.0	..	..	..	1.0
Mt Hotham wastewater reuse and water conservation	4.2	..	..	..	4.2
Total asset investment [(a)]	**30.2**	**53.0**	**66.0**	**68.0**	**72.2**

Source: Department of Treasury and Finance

Note:
(a) Total estimated investment (TEI) not specified as this is an ongoing program.

Additional funding for Piping the System – Wimmera Mallee (State component)

The Victorian Government has committed, subject to new matching funding from the Commonwealth, additional funding of $42 million to provide for the replacement of the existing 17 500 kilometres of open channels with a new pipeline in the Wimmera Mallee region. This funding is in addition to the $125 million already committed by the Victorian Government.

Development contribution for infrastructure initiatives

Revenue from the development contribution will assist in the more timely provision of a range of transport, environmental and community infrastructure to service new communities in Melbourne's growth areas. The specific infrastructure projects to be funded will be determined through the preparation of growth area-specific development contribution plans. The final expenditure pattern will be influenced by the timing of planning requirements and the nature of infrastructure projects specified in these plans, and estimates are therefore likely to vary. The expenditure profile across different growth areas is also expected to vary for similar reasons.

Gippsland Water Factory

Through this $120 million initiative, wastewater treatment facilities between Morwell and Dutson Downs, including the central Gippsland Regional Outfall Sewer, will be upgraded. A key aspect of this project will be the construction of a wastewater treatment plant at Morwell. This initiative will enable the provision of additional treated water for industry.

In addition to the $25 million sourced from the second tranche of Victorian Water Trust allocations, the State Government will provide a further $25 million from the RIDF, bringing its total contribution to $50 million.

Mt Buller water recycling

Through this $3.4 million initiative, the Mt Buller and Mt Stirling Alpine Resort Management Board will undertake capital works to improve the quality and increase the quantity of recycled water for snowmaking and other non-potable purposes. These capital works will contribute to the protection of the high country streams and rivers, by reducing the amount of water withdrawn from Boggy Creek by the Mt Buller Alpine Village. The State Government will contribute $1.0 million to help deliver this initiative.

Mt Hotham wastewater reuse and water conservation

Through this $8.4 million initiative, the Mt Hotham Alpine Resort Management Board, in conjunction with private operators, will implement water conservation measures across the resort, reduce wastewater point discharges and use recycled water to expand the snowmaking capacity across the resort. As part of the initiative, the Mt Hotham Alpine Resort Management Board has agreed to return 110 megalitres per year of water to the environment. The State Government will contribute $4.2 million to help deliver this initiative.

Revenue initiatives

Justice

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*
Vehicle impoundment	0.9	2.7	2.8	2.9
Total revenue initiatives	**0.9**	**2.7**	**2.8**	**2.9**

Source: Department of Treasury and Finance

Vehicle impoundment

Funding is provided to establish the vehicle impoundment system. Impoundment costs will be recovered from offenders who will need to pay impoundment costs before their vehicle is released.

Sustainability and Environment

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*
Development contribution	..	53.0	66.0	68.0
Total revenue initiatives	**..**	**53.0**	**66.0**	**68.0**

Source: Department of Treasury and Finance

Development contribution

The development contribution initiative requires developers in Melbourne’s five designated growth areas to fund a proportion of the cost of a range of infrastructure projects including transport, environmental and community facilities. The development contribution is a key mechanism supporting the Government's Plan for Melbourne’s Growth Areas, and aims to ensure more timely provision of infrastructure as growth areas develop. The estimates shown above reflect both cash or in-kind support expected to flow to the State. Revenue is expected to be influenced by the timing of planning requirements, and estimates are therefore likely to vary.

Treasury and Finance

($ million)

	2005-06	*2006-07*	*2007-08*	*2008-09*
Land Tax on Trusts	-20.0	-18.0	-15.8	-13.5
Total revenue initiatives	**-20.0**	**-18.0**	**-15.8**	**-13.5**

Source: Department of Treasury and Finance

Land tax on trusts

The Government announced during the 2005-06 Budget its plan to reform the area of land tax on trusts to ensure landowners have a reduced incentive to artificially minimise their obligations through the use of multiple trusts. The new arrangements will ensure greater clarity as well as providing a simpler, fairer and more equitable tax system.

After consulting with key industry and taxpayer groups, the Government agreed to a surcharge of 0.375 per cent, which lead to lower rates than in the original model. It was also agreed to allow existing trusts up until 31 December 2005 to nominate a beneficiary of a trust, and they will be assessed at ordinary land tax rates. Estimated revenue from the surcharge has substantially reduced as a result of these changes.

APPENDIX B: TAX EXPENDITURES AND CONCESSIONS

TAX EXPENDITURES

Part of the higher level of disclosure required under the *Financial Management Act* 1994 is an overview of tax expenditures.

Tax expenditures are tax concessions granted to certain taxpayers, activities or assets, which are a deviation from the normal taxation treatment. This includes tax-free thresholds and can also take the form of exempting or applying a lower rate, deduction or rebate of a tax for a certain class of taxpayer, activity or asset (this excludes generally applying marginal tax rates).

Table B.1 shows aggregate tax expenditures by the main categories of tax for the period 2004-05 to 2008-09. The 2005-06 Budget estimate for total estimated tax expenditures for 2005-06 was $2 243 million, $90 million lower than the current estimate of $2 333 million. The variations from the forecast estimates published in the 2005-06 Budget are mainly associated with:

- a single large exemption for corporate reconstruction (shown under 'other stamp duties') in the September quarter 2005; and
- the introduction of the congestion levy.

Congestion levy tax expenditures did not appear in the 2005-06 Budget as the impact was still being assessed. The congestion levy will be applied to long-stay car parking spaces within a boundary that includes the CBD grid and adjacent highly congested areas such as Southbank, Docklands and St Kilda Road precincts. Congestion levy tax expenditures relate to exemptions within the boundary and are expected to be $25 million in 2005-06 and $50 million in the forward years.

Table B.1: Aggregate tax expenditures (excluding thresholds) by type of tax

($ million)

Description	2004-05 Estimate	2005-06 Estimate	2006-07 Estimate	2007-08 Estimate	2008-09 Estimate
Land tax	1 309	1 259	1 293	1 278	1 293
Payroll tax [(a)]	623	665	688	712	739
Gambling tax	68	72	76	73	78
Other stamp duties	63	246	137	138	138
Motor vehicle taxes	66	68	69	73	76
Congestion levy	..	25	50	50	50
Total estimated tax expenditures	**2 129**	**2 333**	**2 313**	**2 324**	**2 373**

Source: Department of Treasury and Finance and State Revenue Office

Note:

(a) Part of the revision to payroll tax expenditures since the 2005-06 Budget reflects a correction to an error in the tax expenditure calculation methodology as applied to public hospitals and non-profit, non-public schools. This correction accounts for a reduction in the estimated payroll tax expenditures by $55 million in 2004-05 rising to $64 million in 2008-09.

CONCESSIONS

This is the second year that concessions have been reported on by the Victorian Government. The aim was to improve transparency of an important and growing component of state assistance to disadvantaged Victorians. This enhanced reporting of concessions formed part of the broader reform of concession programs in the 2005-06 Budget.

Concessions are a direct budget outlay or reduction in government charges that have the effect of reducing the price of a good or service for particular groups. Certain characteristics of the consumer, such as possession of a Commonwealth pensioner card or a health care card, are the basis for entitlement. Concessions allow certain groups in the community to access and/or purchase important amenities like energy, education, health and transportation at a cheaper rate or zero cost.

Table B.2 classifies the major concessions provided by the Victorian Government by the various categories. The current estimated total value of concession for 2005-06 is $921 million, down marginally from the $932 million estimated in the 2005-06 Budget.

Table B.2: Estimated concessions by category[(a)(b)]

($ million)

Description	*2003-04 Estimate*	*2004-05 Estimate*	*2005-06 Estimate*
Energy, municipal rates, water and sewerage	227	248	249
Education	96	110	119
Health	286	291	298
Hardship assistance	15	15	15
Transport	207	220	240
Total for items estimated	**831**	**885**	**921**

Source: Department of Treasury and Finance and Department of Human Services Concessions Unit Annual Report

Notes:

(a) These figures include the cost of administration.

(b) Department of Treasury and Finance estimates have been used for some of the 2004-05 and 2005-06 figures.

APPENDIX C: REQUIREMENTS OF THE *FINANCIAL MANAGEMENT ACT* 1994

The *Financial Management Act* 1994 (the Act) requires the Minister to prepare a budget update for tabling in Parliament each financial year. The provisions of the Act have been complied with in the *2005-06 Budget Update*.

Table C.1 details the statements required to be included in this document under the provisions of the Act together with appropriate chapter references.

Table C.1: Statements required by the *Financial Management Act* 1994 and their location in the *2005-06 Budget Update*

Relevant section of the Act and corresponding requirement	*Location*
(Sections 23 E-G of the *Financial Management Act* 1994)	
Statement of financial policy objectives and strategies for the year.	Chapter 1, *Financial Policy Objectives and Strategies*
(Sections 23 H-N of the *Financial Management Act* 1994)	
Estimated financial statements for the year comprising: – an estimated statement of financial performance over the year; – an estimated statement of financial position at the end of the year; – an estimated statement of cash flows for the year; and – a statement of the accounting policies on which these statements are based and explanatory notes.	Chapter 6, *Estimated Financial Statements and Notes*
Accompanying statement to estimated financial statements which: – outlines the material economic assumptions used in preparation of the estimated financial statements;	Chapter 2*, Economic Conditions and Outlook* and Chapter 6, *Estimated Financial Statements and Notes*

Table C.1: Statements required by the *Financial Management Act* 1994 and their location in *2005-06 Budget Update* (continued)

Relevant section of the Act and corresponding requirement	*Location*
– discusses the sensitivity of the estimated financial statements to changes in these assumptions;	Chapter 5, *Statement of Risks*
– provides an overview of estimated tax expenditures in the budget; and	Appendix B, *Tax Expenditures and Concessions*
– provides a statement of the risks that may have a material effect on the estimated financial statements.	Chapter 5, *Statement of Risks*

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