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Government
of South Australia

Report

of the

Auditor-General

Annual Report

for the

year ended 30 June 2013

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Part C: State finances and related matters

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Part C

Table of contents

Page

State finances and related matters

Part C

Table of contents

Page

Part C

Table of contents

Page

Part C

Table of contents

Page

Part C

Table of contents

Page

Appendix

State finances and related matters

1 Introduction

The 2013-14 South Australian Budget was tabled in Parliament in June 2013. This commentary provides Audit observations and comments on aspects of the State's finances. In particular:

- an overview of matters currently relevant to the State's public finances
- the reporting frameworks that exist for reporting on the State's finances. There are three separate reporting requirements involving statutory and conventional accounting, each providing a different perspective
- a brief analysis of the financial performance of the State for the year, based on the three different reporting frameworks used in the public sector. This primarily involves an examination of the results for the past year, and the Budget and forward projections included in the Budget Papers
- a review of the financial position of the State, including understanding some of the major assets and liabilities, and the impact that they have on the State's finances.

Limitation on audit analysis

Most of the audit analysis in this Report is based on data provided in the Budget Papers, particularly for the 2013-14 Budget, supplemented with information provided by DTF.

There are some limitations associated with the data when analysing results. These limitations include the following:

- The Audit commentary in this Report is based on a review of the Budget material and related information. It is not an audit in the same sense as work conducted to provide an audit opinion on financial statements. The Budget data are estimates and are unaudited.
- This review considers the estimated result for 2012-13. Past experience is that actual results have varied, sometimes substantially, from the estimated result.
- Classification changes occur from year to year in revenue and expense definitions that can affect the comparability of individual items across the time series. Such changes do not generally affect the net lending (borrowing) result. Budget Papers explain structural breaks in time series.

In Audit's view, these limitations are reasonable and do not invalidate the overall trend analysis from the Budget data.

2 Overview of State finances

2.1 Overview

This section provides a broad overview of matters that are, in my opinion, currently relevant to the State's public finances. Further commentary and details follow in later sections. Specific terms are used in reporting on public finances. The main terms and their meanings are provided in Chapters 3 and 4 of this Report. References to the Budget are to Budget Paper 3 'Budget Statement', unless otherwise stated.

2.2 Fiscal strategy

The Government sets out its fiscal strategy in each budget and its broader fiscal targets, together with performance against those targets.

Prior to the 2011-12 MYBR a common fiscal target of the budgets post the global financial crisis was the achievement of sustainable surpluses. Some of the key elements of these past budgets were:

- 2009-10 Budget – Declining revenues, combined with higher infrastructure and operating spending, led to an operating deficit in 2008-09, the first in six years, and previously unbudgeted growth in net debt. An operating deficit of $304 million was budgeted for 2009-10. The announced fiscal strategy was to return the State to sustainable surpluses in the medium-term.

- 2010-11 Budget – The fiscal strategy for the 2010-11 Budget was to establish and maintain sustainable surpluses. An operating deficit was budgeted for 2010-11 with a return to initially small but growing surpluses from 2011-12. The Budget detailed significant budget improvement measures adopted from the then Sustainable Budget Commission's recommendations.

- 2011-12 Budget – The 2011-12 Budget reported that taxation and GST revenues remained significantly below estimates made prior to the global financial crisis, and those estimated in the 2010-11 Budget. A key fiscal strategy was to re-establish and maintain sustainable operating surpluses. An operating deficit was budgeted for 2011-12 and operating surpluses were projected from 2012-13, although at lower levels than in the previous Budget.

The 2011-12 MYBR noted that global economic uncertainty had intensified beyond any expectations and had precipitated ongoing softness in the domestic economy, particularly the property and retail sectors. This resulted in significant deterioration in the budget position after the 2011-12 Budget was released. Over the forward estimates, revenue was revised down by $1.1 billion and the net operating balance was not forecast to return to surplus until 2014-15, two years later than forecast in the 2011-12 Budget.

Given the global economic uncertainty and the significant impact on revenues, new fiscal targets were set by the Government as part of the 2011-12 MYBR. Two key targets were:

- a net operating surplus by the end of the forward estimates
- a maximum ratio of general government net debt to revenue of 50%.

The 2012-13 Budget reinforced the adverse effect of ongoing weaker than expected economic conditions, particularly constrained household consumption and a very subdued property market. As a result, tax and GST revenue growth were revised downward significantly from the projections in the 2011-12 Budget. For the period 2011-12 to 2014-15 taxation revenue was revised downward by $1.551 billion and GST revenue was revised downwards by $1.276 billion. The 2012-13 Budget projected a return to a net operating surplus in 2015-16 ($512 million). Deficits were expected for each of the three years 2012-13 to 2014-15. The cumulative net operating deficit over the four years of the 2012-13 Budget was $1.148 billion.

2.2.1 Net operating balance target

Since the 2011-12 MYBR the Government has had a fiscal target of a net operating surplus by the end of the forward estimates. The 2013-14 Budget expects deficits for the years 2013-14 and 2014-15 before returning to a net operating surplus in 2015-16.

Further, the 2013-14 Budget projects net lending deficits for the years 2013-14 to 2015-16 before an expected net lending surplus in 2016-17. The cumulative net lending deficit over the four years of the 2013-14 Budget is $3.135 billion.

2.2.2 Debt fiscal target

Since the 2011-12 MYBR the Government's debt fiscal target is a maximum ratio of general government net debt to revenue of 50%. This differs from a broader measure in previous years of net financial liabilities to revenue. Net financial liabilities include the present value of the unfunded superannuation liability, which can fluctuate significantly from year to year depending on the discount rate required to be used to calculate the liability.

Net debt is expected to increase from $5.611 billion as at 2012-13 to $8.751 billion as at 2016-17. Net debt peaks in 2015-16 at $9.446 billion. Expressed as a percentage of revenue, net debt increases from 36.8% as at 2012-13 to 47.4% as at 2016-17. As at 2015-16 the net debt to revenue ratio is expected to be 54.2%, which exceeds the debt fiscal target of a maximum ratio of 50%.

The net debt increase is significantly impacted on by the recognition of the new Royal Adelaide Hospital ($2.8 billion) in 2015-16.

2.2.3 The State credit rating

Securing and maintaining a triple-A credit rating for the State has been used by the State Government as another target measure (indicator) of prudent management of risks to State finances.

South Australia's credit rating from Standard & Poor's was downgraded from AAA to AA+ following the release of the 2012-13 Budget in May 2012. In early September 2012, Moody's also downgraded South Australia's credit rating.

Prior to this downgrade, South Australia had maintained a triple-A credit rating since 2004.

In late September 2012 Standard & Poor's further downgraded South Australia's credit rating from AA+ to AA with a stable outlook.

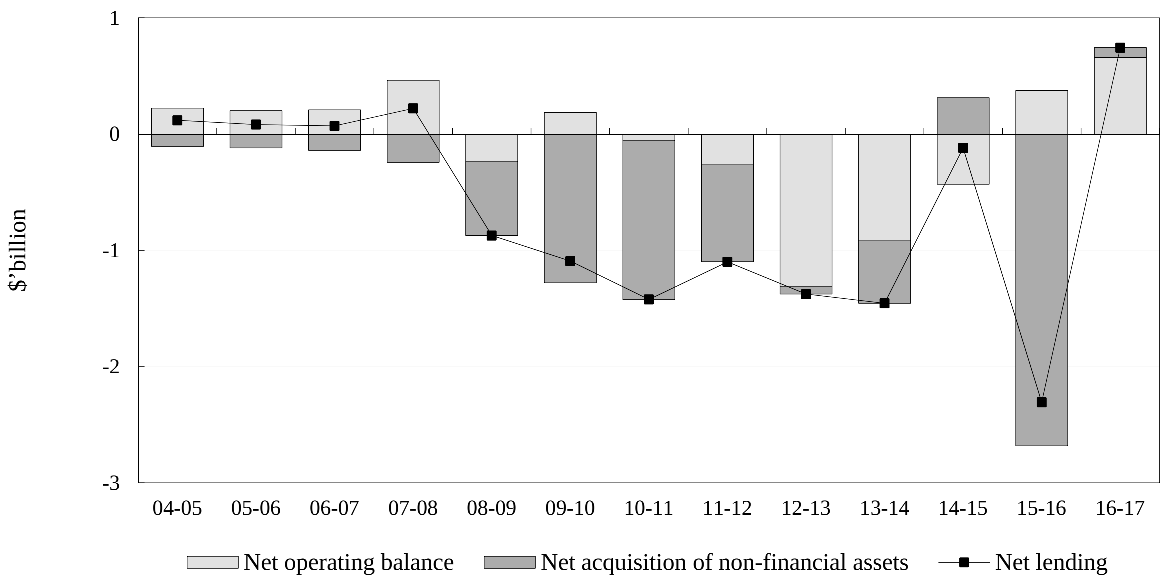
At the time of the release of the 2013-14 State Budget, Standard & Poor's commented that its current credit rating of the State of South Australia is not immediately affected by the State's Budget. Standard & Poor's indicated that their assessment of the strong institutional framework supporting Commonwealth-State relations in Australia, and the State's wealthy economy in an international context, underpin the ratings on South Australia. They also noted that constraining the ratings are the State's weak budgetary performance, rising debt burden, and modest budgetary flexibility.

At the same time Moody's commented that risks to budget improvements include the potential for weaker than anticipated revenues. Moody's indicated that the State is counting on robust growth in property related conveyancing duties, payroll tax and GST-backed grants to drive an average annual 4.9% rise in revenue over the next four years. Moody's also indicated that the State's ability to achieve the forecast low 1.8% annual average rise in expenditures will be challenged by demands for improved services and the wage expectations of public sector workers.

2.3 Changing financial position

The following chart demonstrates the trend in net lending since 2004-05 and expected trend over the forward estimates.

Chart 2.1 – General government sector net operating balance, net acquisition of non-financial assets[(a)] and net lending



(a) Net acquisition of non-financial assets included as negative amounts

Chart 2.1 shows the increased frequency of net lending deficits (where revenues are less than operating and net investment expenditure) since 2008-09 reflecting:

- a significant capital expenditure program since 2008-09 (net acquisition of non-financial assets)
- actual or expected significant net operating deficits for the period 2011-12 to 2014-15
- the recognition of the new Royal Adelaide Hospital asset in 2015-16.

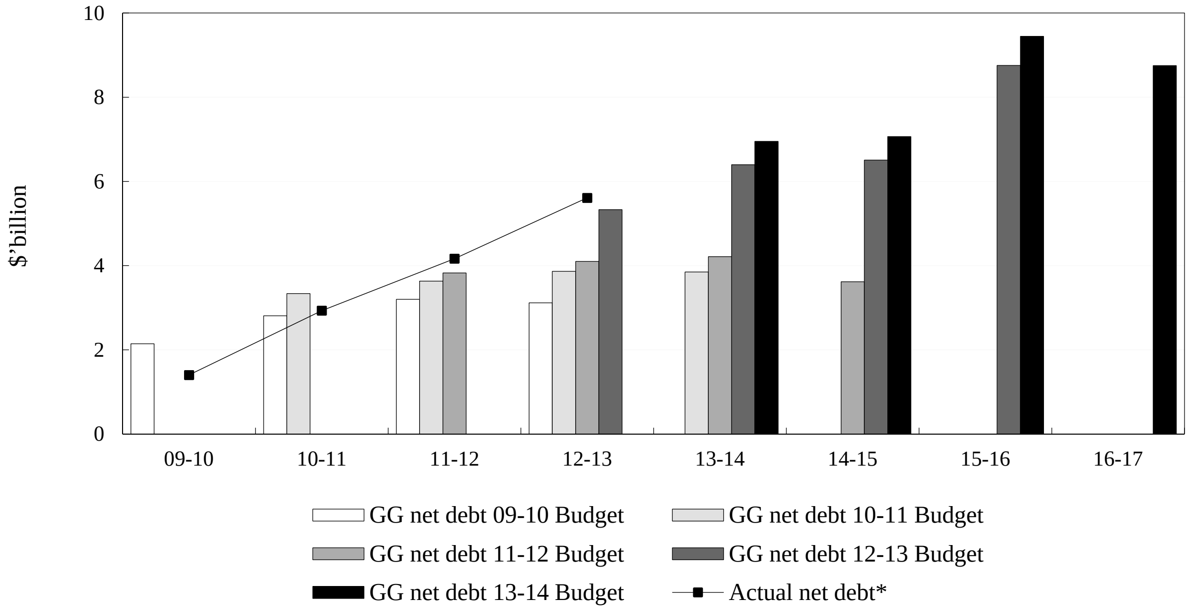
The chart highlights the seven year period from 2008-09 to 2014-15 where net operating deficits occurred or are expected for each year other than 2009-10. This reflects the impact of the global financial crisis and the ongoing global economic uncertainty and the budget policy dimensions for revenue and expense management set over recent years. A return to net operating surplus is projected in 2015-16, on the basis of strengthening revenue growth rates and expenditure restraint through realisation of savings targets.

Net lending deficits also occur or are projected for each of the years 2008-09 to 2015-16. As a consequence, net debt rises from a surplus cash position of $276 million as at 2007-08 to peak at $9.4 billion as at 2015-16, before reducing to $8.8 billion as at 2016-17. The 2015-16 year includes recognition of the new Royal Adelaide Hospital ($2.8 billion).

Net lending deficits are significantly influenced by capital investment spending decisions. Over $7 billion is spent or estimated to be spent on net acquisition of non-financial assets for the period 2008-09 to 2016-17. This includes $2.8 billion in 2015-16 associated with the recognition of the new Royal Adelaide Hospital.

The following chart shows how general government sector net debt estimates have changed subsequent to the 2008-09 Budget.

Chart 2.2 – Comparison of general government sector (GG) net debt between budgets



* 2012-13 is estimated net debt

Chart 2.2 highlights the significant increase in net debt estimates over successive budgets since 2009-10. This increase reflects the maintenance of a significant capital expenditure program over a period where there were major write-downs in revenue estimates over successive budgets. These downward revisions in revenue estimates (mainly taxation and GST revenue grants) have placed significant pressure on the Budget.

For the period 2009-10 to 2016-17 the total of actual and estimated purchases of non-financial assets is almost $16 billion. Over this same period, actual and estimated sales of non-financial assets amount to $2.4 billion. Capital payments are discussed further at section 2.6.7 of this Report.

The Budget states that the net lending deficits until 2015-16 reflect the Government's significant capital expenditure, to both stimulate the economy and to rebuild the State's infrastructure management. If the impact of the new Royal Adelaide Hospital is excluded it is also evident that there is an easing in the level of infrastructure investment across the period of the 2013-14 Budget.

2.4 Operating Statement

2.4.1 Estimated results for 2012-13

The 2013-14 Budget estimates a net operating balance deficit of $1314 million for 2012-13 compared to the budgeted deficit of $867 million. The difference between the budgeted and estimated result was mainly due to an increase in employee expenses and a reduction in some current grants from the Commonwealth.

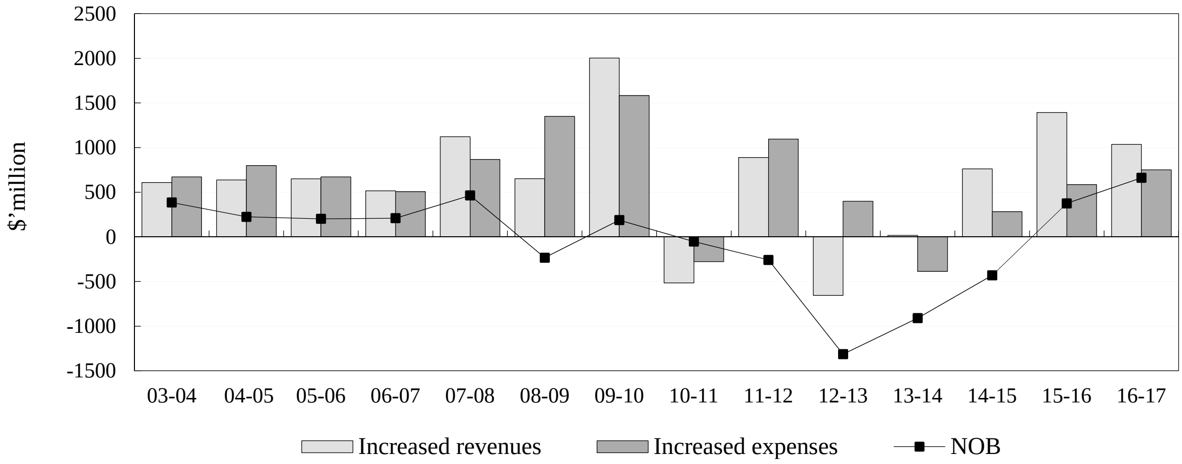
The net lending deficit is estimated to be $1376 million, compared to the budgeted amount of $1901 million. The difference between the budgeted and estimated deficit is mainly due to the Forestry and Lotteries sale proceeds totalling $1 billion (excluding stamp duty) being included in the general government sector sales of non-financial assets for the estimated result.

The general government sector is estimated to have net debt of $5611 million at the end of 2012-13.

2.4.2 Budget forecasts 2013-14 to 2016-17

Chart 2.3 shows annual increases in revenues and expenses since 2003-04 compared to annual changes estimated for the four years of the 2013-14 Budget together with each year's net operating balance.

Chart 2.3 – Annual change in general government sector revenue, expenses and net operating balance (NOB)[(a)]



(a) 2009-10 and 2010-11 are influenced by Commonwealth stimulus grants

For the five years to 2007-08, annual increases in revenues and expenses were reasonably consistent and the net operating surpluses were achieved over the period. The global financial crisis affected 2008-09 and a net operating deficit was incurred. The annual movements from 2008-09 to 2011-12 are influenced by changes in Commonwealth funding, including stimulus grants, which peaked in 2009-10. Funding from the Commonwealth's Nation Building - Economic Stimulus Plan concluded in 2011-12.

The chart shows that revenues are estimated to improve significantly in the last three years of the 2013-14 Budget. These revenue increases reflect expectations of a return to normal historical growth trends (see chart 2.8 in this Chapter) and come off a base of significant revenue write-downs in previous budgets. Significant increases are expected in both GST revenue grants and taxation revenue. In 2015-16, when the Budget expects to return to a net operating surplus, taxation revenue is expected to increase by $334.1 million and grant revenue is expected to increase by $916.4 million (including GST revenue grants increase of $400 million, recurrent specific purpose grants increase of $143.4 million and capital grants from the Commonwealth increase of $292.5 million).

Chart 2.3 also highlights the expenditure restraint anticipated over those four years compared to earlier years. The projected net operating surplus for 2016-17 of $661 million is the highest of any year on the chart.

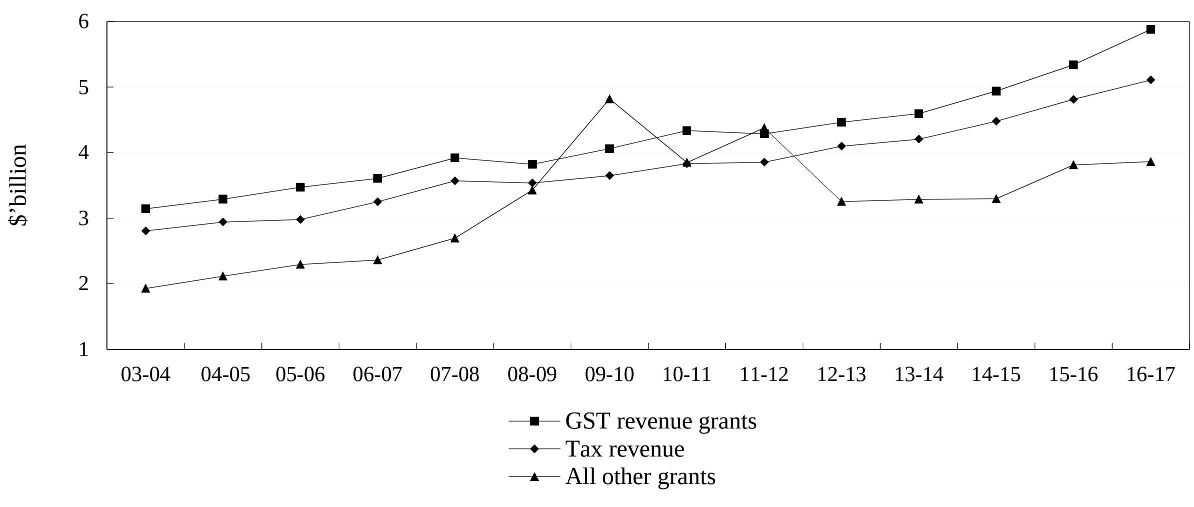
2.4.3 Revenue forecasts 2013-14 to 2016-17

There were significant temporary compositional changes in revenues following the global financial crisis. Immediate and large reductions in GST revenue grants and taxation revenue were offset by Commonwealth economic stimulus and other nation building funding to the states. Further, the crisis coincided with major changes in the Commonwealth's financial relations with the states. This resulted in other changes in the timing and composition of Commonwealth revenues.

Expected reductions in GST revenue grants and taxation revenue in the 2012-13 Budget were far more significant than what was expected in previous budgets. This has had a major impact on the net operating balance and net debt projections. Further, these reductions are not offset by Commonwealth economic stimulus funding, as was the case in the wake of the 2008-09 global financial crisis. The 2013-14 Budget has revised GST revenue grants and taxation revenue down a further $722 million over the four years from 2012-13 since the 2012-13 Budget.

Chart 2.4 shows expected trends for the major revenue items in the 2013-14 Budget against the experience of the ten years to 2012-13.

Chart 2.4 – General government sector Commonwealth grants and taxation revenue



The chart highlights the impact of the global financial crisis and ongoing global economic uncertainty over the period 2008-09 to 2011-12. Over this period there were two breaks in trend where:

- GST revenue grants and taxation revenue fell in 2008-09
- GST revenue grants fell in 2011-12 and taxation revenue increased marginally.

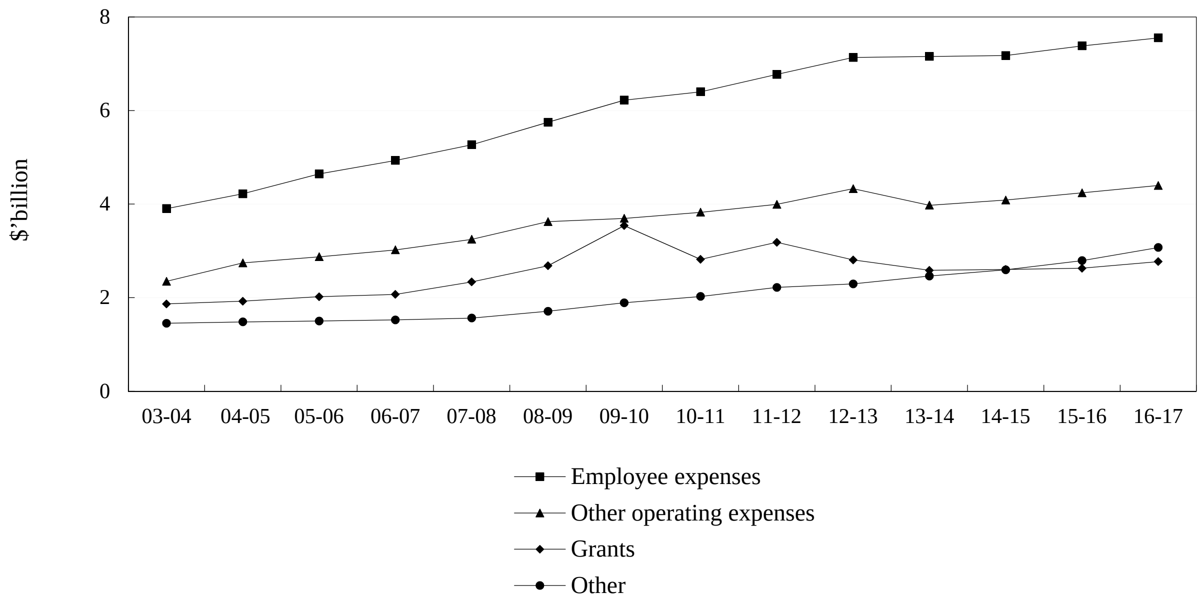
Both GST revenue grants and taxation revenue streams are expected to experience stronger growth from 2013-14 on the basis of an improved economic outlook, relatively low interest rates, more positive labour market conditions and improved household confidence. Given that there is still a degree of economic and financial uncertainty, a risk remains that this revenue growth is not achieved and revenue pressures reappear. An analysis of these revenue streams against the historical average growth rates is provided later in this Chapter under section 2.6.1 (see in particular chart 2.8 in this Chapter).

All other grants, principally other Commonwealth grants, increased markedly in the period 2008-09 to 2010-11 mainly due to the Commonwealth Government's Nation Building - Economic Stimulus Plan and Nation Building Plan for the Future capital grants. Grants remained high in 2011-12 mainly reflecting the timing of Commonwealth capital grants for major water, road and rail infrastructure projects. Other Commonwealth grants reduced in 2012-13 reflecting payment profiles agreed with the Commonwealth. Importantly, these monies are required to be spent on projects and are not available as general purpose revenue. Some of these grants are on-passed to recipients as grant expenses or are used for specific capital spending programs.

2.4.4 Expense forecasts 2013-14 to 2016-17

Chart 2.5 shows trends expected for total expenses in the 2013-14 Budget split into four main categories, against the experience of recent years.

Chart 2.5 – General government sector expenses



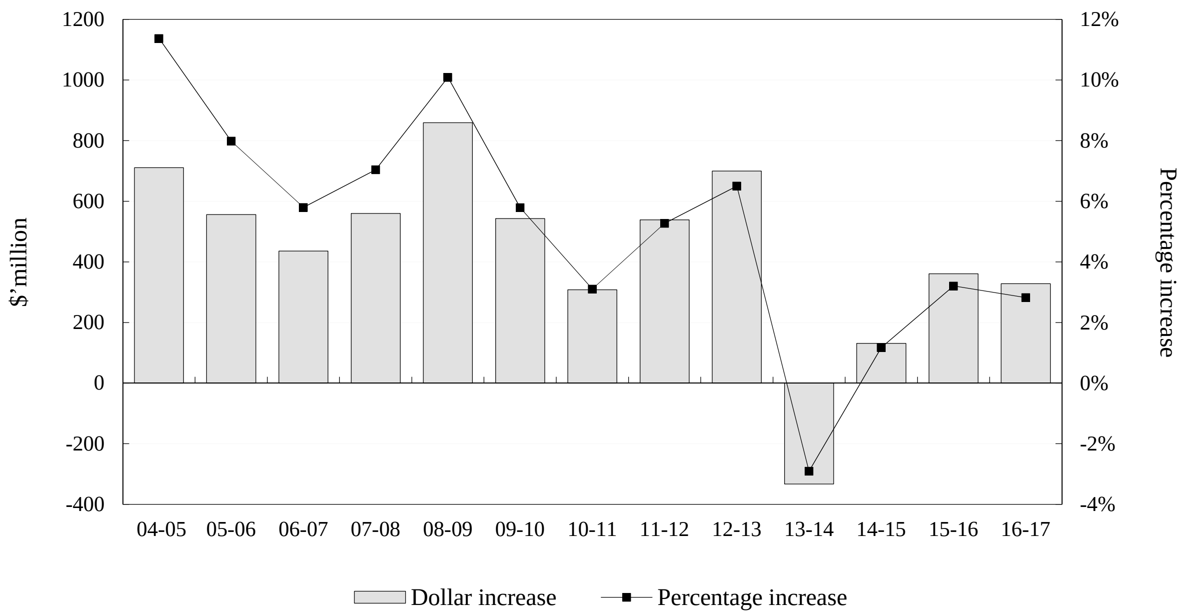
All categories of expenses, except grants, are estimated to increase in 2012-13 and beyond. The decrease in grant expenses is largely associated with Commonwealth grant revenues discussed above. These grant expenses reduce in line with related grant revenues.

Other operating expenses increased in 2012-13 due to relief of $320 million debt on the South Australian Housing Trust balance sheet following relief of the same amount of South Australia's public housing payments due to the Commonwealth.

The challenging dimension of expenditure restraint underlying the 2013-14 Budget is illustrated by the estimated annual movements in the two main expenditure items of the Budget, employee expenses and other operating expenses. These two items combined represent 69% of expenses for 2013-14, a proportion that is consistent with most years.

Chart 2.6 shows that the annual movements projected for employee expenses and other operating expenses for the four years to 2016-17 are below all of the previous nine years' experience other than 2010-11.

Chart 2.6 – Annual change in employee and other operating expenses



Integral to the expenditure restraint is achieving savings initiatives built into the forward estimates from both previous budgets and the current Budget. As commented previously, achieving these expenditure targets is a major task and therefore another risk to the current budget strategy.

2.4.5 Net acquisition of non-financial assets

For 2012-13 net acquisition of non-financial assets (the balance of purchases of non-financial assets less sales of non-financial assets and depreciation) is estimated to be $62 million, which is $972 million less than the budgeted amount of $1.034 billion. The difference is mainly due to the Forestry and Lotteries sale proceeds being included in the general government sector sales of non-financial assets for the estimated result.

Net acquisition of non-financial assets for 2013-14 is budgeted at $544 million.

Purchases of non-financial assets in 2013-14 are expected to be $1.9 billion and this reduces to $912 million in 2014-15. Purchases increase significantly in 2015-16 due to the recognition of $2.8 billion associated with the new Royal Adelaide Hospital.

For the general government sector, sales of non-financial assets peaked at $1.2 billion in 2012-13. Sales include proceeds from the forward sale of the State's Green Triangle forest plantations ($635.1 million) and proceeds from the appointment of Tatts Lotteries SA Pty Ltd as exclusive Master Agent to operate the SA Lotteries' brands and products for a term of 40 years ($402.8 million). These amounts are exclusive of stamp duty.

Sales are expected to be $419 million in 2013-14 and reduce to $4 million by 2016-17.

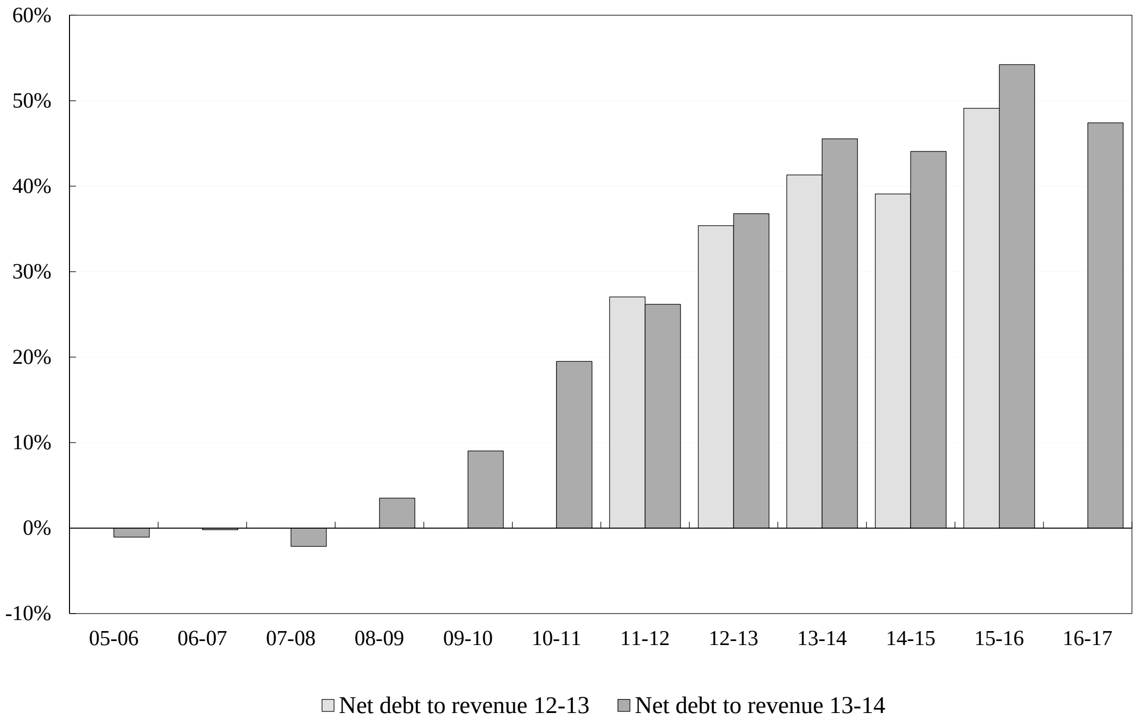
2.4.6 Ratios of net debt to revenue

As highlighted earlier, one of the Government's fiscal targets is to achieve a level of general government net debt that remains affordable over the forward estimates - equating to a maximum ratio of net debt to revenue of 50%.

The Government previously had a fiscal target to achieve net lending outcomes that ensure the ratio of net financial liabilities to revenue continues to decline towards that of other triple-A rated states. However, this was replaced as part of the 2011-12 MYBR with a more specific net debt to revenue measure due to the volatility of the present value of the unfunded superannuation liability, which formed part of net financial liabilities. The broader net financial liabilities to revenue ratio is further discussed in section 10.3.1 of Chapter 10 of this Report.

Chart 2.7 shows the ratio of net debt to revenue for recent years and for the 2012-13 and 2013-14 Budgets.

Chart 2.7 – General government sector ratio of net debt to revenue Budget comparisons



The 2013-14 Budget projects that net debt will rise higher than was previously estimated in the 2012-13 Budget. Consequently the ratio of net debt to revenue is higher than previously budgeted. The ratio peaks in 2015-16 at 54.2% as a consequence of the recognition of the new Royal Adelaide Hospital. The ratio falls back to 47.4% in 2016-17 on the basis of expected revenue growth of $1 billion, a net operating surplus projection of $661 million and reduced estimated purchases of non-financial assets.

The 2015-16 projected ratio exceeds the maximum of 50% established by the Government's fiscal target.

2.4.7 Interstate comparison

Section 10 of this Report includes comment on 2013-14 Budget comparisons for key budget aggregates across jurisdictions. In 2013-14, South Australia, New South Wales, Tasmania and Queensland are forecasting general government sector net operating balance deficits. Victoria and Western Australia have budgeted net operating surpluses. Tasmania, Western Australia and New South Wales expect net lending deficits for all estimate years. The other states expect to return to net lending surpluses in 2015-16 or 2016-17. Most jurisdictions are budgeting to invest significant funds into infrastructure projects.

2.5 Non-financial public sector Balance Sheet[1]

The State's Balance Sheet is expected to strengthen modestly over the four years of the 2013-14 Budget as measured by net worth. This is the combined effect of a rise in the value of non-financial assets, due to projected valuation increases and asset acquisitions, offset by increases in net financial liabilities.

Net financial worth deteriorates over the forward estimates by over $4 billion due primarily to the growth in borrowings.

Net worth is estimated to add $1.3 billion over the forward estimates to reach $39.8 billion by 2016-17.

2.5.1 Assets

Total assets are expected to increase over the forward estimates from $66.1 billion in 2012-13 to $71 billion by 2016-17. There is a large increase in 2015-16 due to the recognition of the new Royal Adelaide Hospital ($2.8 billion).

Net acquisitions (purchases less depreciation and asset sales) increase non-financial assets by $2.7 billion through to 2016-17. Revaluations in the PNFC sector are also estimated to add substantially to non-financial assets.

Total financial assets are expected to be $2.7 billion in 2012-13, falling to $2.1 billion in 2016-17. This reduction is primarily due to the movement in investments in other public sector entities under the equity category of financial assets.

1 Balance Sheet data is for the NFPS unless otherwise stated due to the high value of non-financial assets in PNFCs.

Investments in other public sector entities represent the value of the Government's interest in PFCs including WorkCoverSA and the Motor Accident Commission (MAC).

WorkCoverSA reported a comprehensive profit result of $23 million in 2012-13. This compares to a comprehensive loss result of $437 million in 2011-12. The improvement in the comprehensive profit was mainly due to a reduction in the cost of claims (due to a smaller increase in the outstanding claims liability) and an increase in investment profit. This contributed to an improvement in its funding ratio to 63.7% from 59.2%, compared to its approved target funding range of 90% to 110%. As at 30 June 2013 WorkCoverSA had a net liability position of $1366 million ($1389 million).

MAC reported a comprehensive profit result for 2012-13 of $371 million, compared to a comprehensive loss result of $34 million in 2011-12. This was primarily due to a reduction in claims expense (due to only a marginal increase in the outstanding claims liability) and increased revenue from investment activities. MAC's statutory solvency level, calculated in accordance with a formula determined by the Treasurer, improved to 111.9% (100.8%) of the target level of solvency. As at 30 June 2013 MAC had net assets of $768 million ($397 million).

2.5.1.1 Motor Accident Commission - $100 million contribution to the Budget

The 2013-14 Budget presented in June 2013 includes an amount of $100 million to be received from MAC to fund future road improvement and safety initiatives.

The $100 million contribution was the subject of correspondence between the Chair of the Board of MAC and the Premier and Treasurer in May 2013. Subsequently the Board of MAC on 31 May 2013 considered the correspondence of the Chair and Premier and Treasurer. The Board noted positive benefits to the CTP Fund from a contribution that would address key road safety initiatives and agreed that any payment should not impact on future premium and sufficient solvency levels.

In early August 2013 Audit sought, through written communication to MAC, a specific understanding of the nature of the proposed contribution relevant to the provisions of the *Motor Accident Commission Act 1992* (MAC Act) and for consideration of financial reporting treatment and disclosure.

The Board of MAC on 30 August 2013 considered the audit communication. The Board formally agreed a contribution of $100 million from the MAC CTP Fund as required by the Treasurer pursuant to section 25(5)(d) of the MAC Act for road safety initiatives initially with a focus on the treatment of black spots in accordance with its functions and objectives under section 14(1)(d) of the MAC Act. In addition the proposed contribution has been disclosed as a commitment in the 2012-13 financial statements of MAC.

2.5.2 Liabilities

Borrowing is a major component of liabilities over the period of the forward estimates. Net debt, mainly borrowings less cash and deposits, is estimated to rise from $9.5 billion at 30 June 2013 to $13.1 billion as at 2016-17. The general government sector net debt is estimated to increase to $5.6 billion at 30 June 2013 rising to $8.8 billion as at 2016-17. In 2015-16 net debt will include the effect of accounting for the new Royal Adelaide Hospital discussed further in section 2.6.7.1.

The other major component of liabilities, unfunded superannuation liabilities, is estimated to be $11.9 billion for the year to 30 June 2013. Unfunded superannuation liabilities are valued at points in time by discounting future superannuation benefit payments by a discount rate that reflects the risk-free interest rate consistent with the requirement of prevailing AASs. A discount rate of 3.7% was used for the estimate as at the 2013-14 Budget, compared with 4% for the 2012-13 Budget. A 1% reduction in the discount rate is estimated to increase the superannuation liability by $2.6 billion.

The unfunded superannuation liability is a long-term liability to current and past members of closed defined benefit superannuation schemes. The Budget records that while financial market volatility in the recent past has resulted in multi-billion dollar revisions to the value of the liability recorded on the Balance Sheet, there has been no material change in the actual expected payments to beneficiaries underlying the liability.

The Government reports that it remains committed to fully fund the superannuation liability by 2034. Table 4.8 of 2013-14 Budget Paper 3 'Budget Statement' (page 81) itemises expected past service superannuation liability cash payments for 2012-13 and the four years of the Budget.

2.6 Risks and management tasks for the 2013-14 Budget

As mentioned earlier, the stated fiscal strategy of the 2013-14 Budget is to achieve a net operating surplus by the end of the forward estimates. Key elements to the success of the 2013-14 Budget will be achieving estimated real growth in major revenue items and realising expenditure restraint arising from previously announced and current budget improvement measures.

Consistent with prior years, Audit sought DTF's view of which areas of the Budget are considered to be the highest risks and any specific monitoring measures. DTF responded that the major risks to the fiscal outlook are set out in Chapter 6 of the 2013-14 Budget Paper 3 'Budget Statement'. These include: the impact of economic activity on household spending patterns and demand for housing, which impact on GST and property taxation; expenditure risks such as higher than expected wage increases, cost escalations on capital projects and activity growth in hospitals and schools; and changes in Commonwealth policy.

This section discusses some of the risks to achieving the Budget estimates. The values ascribed to some risks are from the Budget Papers[2] which explain and illustrate the effect of many of the budget risks.

Integral to any budget is the quality of data, which by its nature is based on estimates, assumptions and targets. Processes supporting the data preparation are a vital element in the integrity of the Budget.

Audit requested confirmation from DTF that the 2013-14 Budget estimates are based on data submitted by agencies and details of the processes adopted by DTF to ensure the integrity and reasonableness of this data for use in the preparation of the Budget. DTF responded that the data for all lines is maintained in the Budget and Monitoring System and then is only amended with specific approvals through the following processes:

- Cabinet decisions

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[2] 2013-14 Budget Paper 3 'Budget Statement', Chapter 6.

- carryovers
- impacting and non-impacting data adjustments
- mid-year review adjustments
- 2013-14 Budget measures.

Agencies submit data to DTF via DTF's Budget and Monitoring System to update their budget estimates. This data is subject to a range of integrity checks to ensure the correct application of accounting principles and that it is consistent with the relevant decisions of government. Quality assurance reports have been developed to aid in the detection of common problems associated with the data provided.

The forward estimates figures are calculated by consolidating approved budgets for individual government agencies. These incorporate government policy decisions and parameter variations relating to the operations of agencies, such as the quantity of services provided. In estimating revenue items, DTF applies a range of assumptions. These assumptions are outlined in Chapter 3 of 2013-14 Budget Paper 3 'Budget Statement'.

2.6.1 Net operating balance

The 2013-14 Budget estimates net operating deficits for the General government sector for the period 2012-13 to 2014-15. The budget is expected to return to a surplus of $375 million in 2015-16.

Table 2.1 shows the impact of the global financial crisis and the Government response to ongoing global economic uncertainty by tracking how net operating result estimates for the general government sector have changed since the 2008-09 Budget, which was presented before the crisis.

Table 2.1 – Comparison of estimated net operating results between budgets

	2008-09 $'million	2009-10 $'million	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million	2014-15 $'million	2015-16 $'million	2016-17 $'million
NOB 2008-09 Budget	160	356	434	424					
NOB 2009-10 Budget	*(233)	(304)	78	96	304				
NOB 2010-11 Budget		*187	(389)	55	216	370			
NOB 2011-12 Budget			*(53)	(263)	114	80	655		
NOB 2012-13 Budget				*(258)	(867)	(778)	(15)	512	
NOB 2013-14 Budget					*(1 314)	(911)	(431)	375	661

* Actual or estimated result

The actual net operating surplus result for 2009-10 of $187 million was heavily influenced by Commonwealth funding in response to the global financial crisis and other changes.

The changes since the estimated surpluses of the 2008-09 Budget (before the global financial crisis) represent a $1.7 billion unfavourable turnaround over the four years to 2011-12 in the changed economic environment.

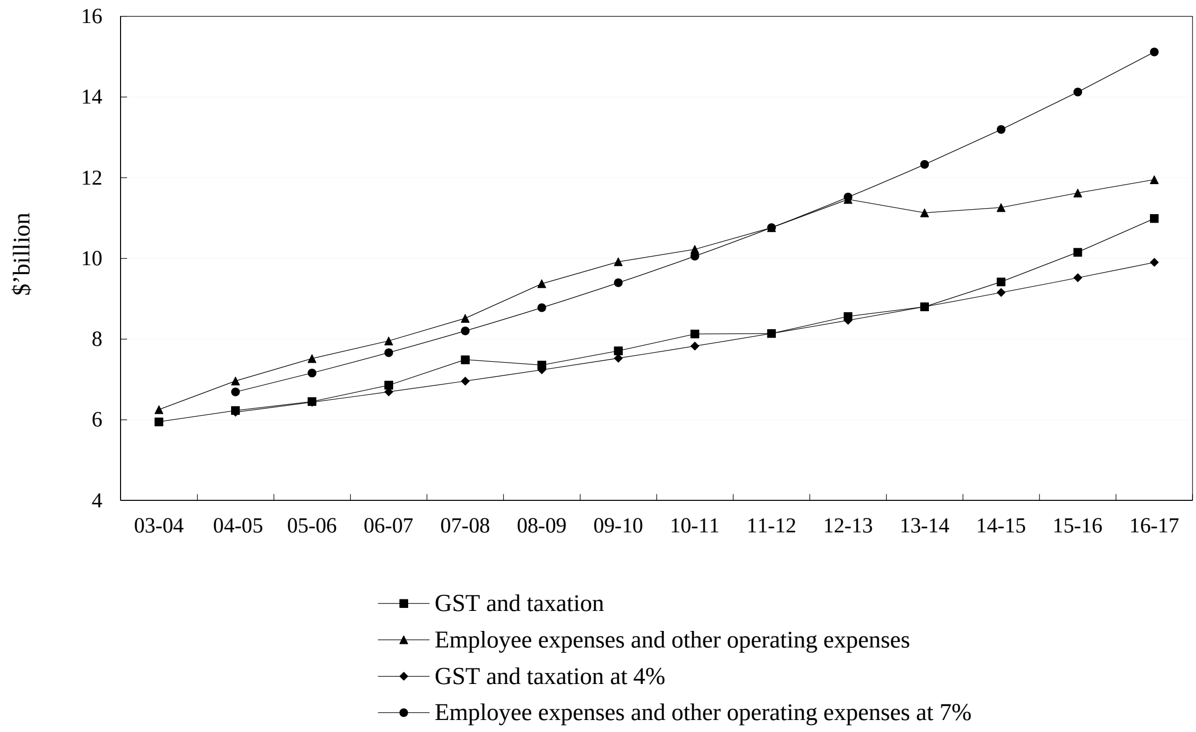
Table 2.1 also demonstrates the ongoing impact on the estimates for the years 2012-13 to 2015-16. For these estimate years successive Budgets have lowered the estimated net operating result from the previous Budget. This has had a marked effect as expected surpluses in the 2011-12 Budget become estimated deficits in the 2012-13 Budget. The cumulative unfavourable expected turnaround in the net operating surplus over this period amounts to $2.5 billion. The 2013-14 Budget revised the net operating surpluses down by a further cumulative amount of $1.1 billion. This mainly reflects the deterioration of GST and taxation revenue estimates over this period and the present level of expenditure projections.

The 2013-14 Budget expects a significant improvement in the net operating balance back to surpluses in 2015-16 and 2016-17. The Budget projects an improvement in the net operating balance in 2015-16 of $806 million. Prior to this period flexibility is limited to contingencies or policy changes to buffer against unfavourable influences and events that may affect outcomes.

Buffers are built into the Budget through contingency provisions including headroom. These amounts are provided for unexpected events or for expenditure that is subject to further approvals. The 2013-14 Budget includes contingency buffers to a similar extent as previous years. Beyond this, and in the absence of other changes in spending or taxation policies, unfavourable outcomes will flow to the net operating result and, in the event of deficits, to net debt.

The net operating result is at risk from both revenue and expense outcomes. Chart 2.8 compares trends for some previously discussed key revenue and expenses items in the Budget, namely GST and taxation revenue and employee expenses and other operating expenses.

Chart 2.8 – Comparison of GST and taxation revenue and employee expenses and other operating expenses



In chart 2.8, the GST and taxation revenue line tracks actual revenues up to 2011-12 and estimated revenues from 2012-13 to 2016-17. For the nine years to 2011-12, these two combined items grew on average annually by about 4%. Applying this average growth rate from 2003-04 through to 2016-17 creates the GST and taxation revenue at 4% line. It can be seen by the closeness of the two lines that the 2013-14 Budget estimates are consistent over most of the estimate years with that past average experience. A gap between past experience and Budget estimates is evident in 2016-17. Further comments on operating revenue risks are provided in section 2.6.2 below.

For the nine years to 2011-12 combined employee expenses and other operating expenses grew on average annually by about 7%. Applying this average growth rate from 2003-04 through to 2016-17 creates the employee expenses and other operating expenses at 7% line. Comparing the trend of this line to the estimated expenses for the 2013-14 Budget shows a diverging difference between the two lines. This difference highlights the significance of the expenditure restraint required from the 2013-14 Budget.

2.6.2 Operating revenues

The estimated result for 2012-13 expects GST revenue to be marginally less than budgeted and taxation revenue to increase marginally. Over the forward estimates both these revenue lines are expected to grow in real terms. This improvement in taxation and GST revenues is based on the expected improvement in domestic economic conditions. GST revenue has now shown to be highly sensitive to household spending patterns. State taxation also varies with economic activity and demand for housing.

The 2013-14 Budget comments that the ongoing softness in the property market and domestic consumption has resulted in taxation and GST revenue grants being revised down by $722 million over the four years from 2012-13 since the 2012-13 Budget.

GST revenue in 2012-13 is estimated at $4.5 billion, representing 29% of total revenue. South Australia’s GST revenue grants are expected to increase at rates that vary from estimated growth in the GST pool. Factors contributing to changes to South Australia’s share of the GST pool include a declining population share and movements in South Australia’s projected relativities which are particularly affected by different state taxation and royalties revenue growth rates compared to other states and changes to the distribution of Commonwealth National Partnership Agreement funding to the State.

The two main elements of state taxation are payroll tax and conveyance duty. Growth in payroll tax is based on expected stronger growth in employment from 2013-14. For conveyance duty, property market conditions are expected to improve, returning to their long-term trend level over the medium-term. Strong growth in conveyance duty is expected from 2014-15, with transactions expected to return to long-term trend levels by 2016-17 and property prices estimated to grow in line with long-term property price growth projections.

The Budget comments that the difficulty in predicting trends in property market values and activity levels in recent years makes forecasting of property taxes, especially conveyance duty, difficult. Since 1995-96 the annual growth in conveyance duty revenue has ranged from negative 21% to positive 42%. The difference in volatility of the two main sources of taxation revenue is represented in the following chart, which shows actual annual nominal percentage changes from 2002-03 and expected changes over the forward estimates.

Chart 2.9 – Annual percentage change in payroll tax and conveyance duty

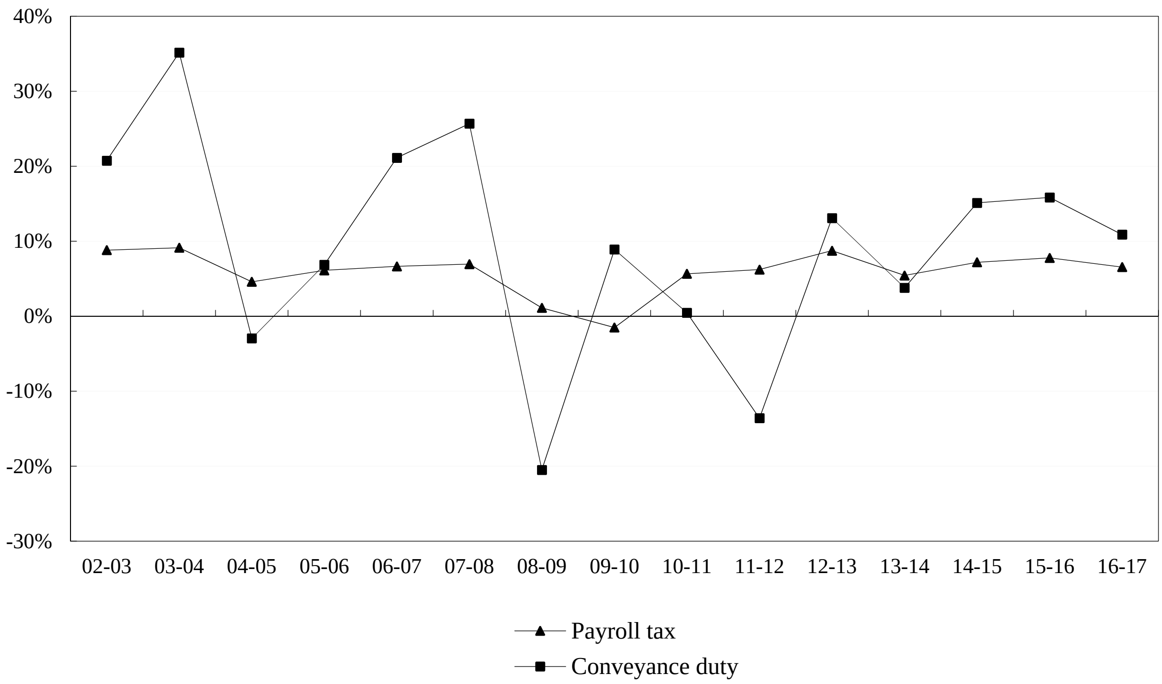


Chart 2.9 shows the relative stability of payroll tax growth over the period in comparison to the significant fluctuations in conveyance duty. Conveyance duties are a volatile revenue stream that is sensitive to both transaction levels and transaction prices. The chart also demonstrates that, over the forward estimates, conveyance duty is expected to increase each year. The increase in 2013-14 is modest (3.8%), with stronger growth above 10% expected in the years 2014-15 to 2016-17.

The 2013-14 Budget reports that there is a risk that property prices and/or activity levels will be lower than estimated, particularly if relatively soft employment conditions remain or structural changes in the economy causes employment uncertainty. Risk analysis in the Budget Papers notes that:

- a 1% change in GST pool growth has a revenue impact for South Australia of about $44 million p.a.
- a variance of 1% in state taxation revenue equates to about $42 million p.a.
- a 1% variation in property values equates to about $8 million in conveyance duty revenue
- a 1% variation in transactions equates to about $7 million in conveyance duty revenue.

2.6.3 Operating expenses

Consistent with recent past Budgets, the 2013-14 Budget expects significant restraint in spending. The Budget Papers provide summary details of parameter and policy changes that occur between budgets that typically have added hundreds of millions to spending commitments.

Parameter effects usually include adjustments for enterprise bargaining outcomes, the carryover of expenditure from the previous year, revised timing of expenditure, expenditure associated with additional Commonwealth revenues and changes to interest expenses. Some expenses are covered by using contingency provisions set aside in the annual budget.

Parameter effects since the 2012-13 Budget have reduced operating expenses by $26 million (before provisions) over the four years to 2015-16.

Salaries and wages remains the main public sector operating cost. The Budget records that enterprise bargaining negotiations are progressing for a number of major workforce groups. Budget commentary states that the outcomes of future wage negotiations will be crucial in determining whether expenditure forward estimates in this Budget can be achieved, and the level of government services that can be delivered in light of the current challenging economic conditions.

The Budget records that if public sector-wide wage outcomes for new enterprise agreements vary by 1% p.a. from allowances in the forward estimates, the Budget impact is estimated to be approximately $240 million in 2016-17. Further, comment is made that if real wage restraint cannot be achieved, further FTE reductions and savings may be required in future Budgets to maintain the fiscal position.

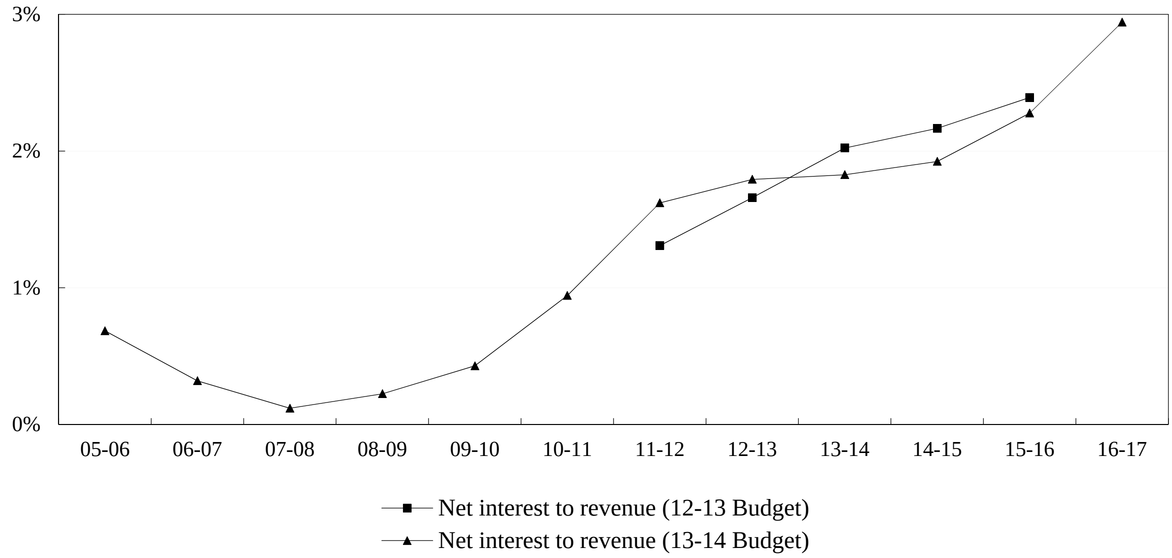
The 2013-14 Budget reports that policy decisions since the 2012-13 Budget have added $944 million (before provisions) to operating expenses over four years to 2015-16. The ongoing practice of approving expenditure commitments between Budgets, while a practical necessity for many reasons, is an area that warrants a high degree of government management discipline given the present budget challenges to achieve savings targets and achieve revenue growth.

Subsequent to the release of the 2013-14 Budget the SA Government signed the National Education Reform Agreement (NERA) with the Commonwealth Government. This agreement will increase public funding to South Australian schools by around $1.1 billion between 2013 and 2019. DTF has advised that the 2013-14 Budget does not incorporate funding arrangements for the delivery of the NERA. Further, while negotiations are still ongoing with the Commonwealth as to the final profile of additional State and Commonwealth NERA funding, the current estimate of additional contributions by the State for the period 2014 to 2019 is $229.9 million. The additional Commonwealth contribution for this same period is estimated to be $427 million.

2.6.4 Ratio of interest to revenue

In the 2013-14 Budget, interest expenses are expected to decline in 2013-14 primarily due to a lower interest rate applicable to government debt. Interest expenses then increase over the forward estimates reflecting a rise in interest rates and a higher level of borrowings up to 2015-16. Chart 2.10 shows the outcomes for the general government sector ratio of net interest expense to revenue for recent years and as estimated in the 2012-13 and 2013-14 Budgets.

Chart 2.10 – General government sector interest to revenue ratio



This chart shows the ratio of net interest to revenue rising significantly from 2009-10 to 2016-17. The 2015-16 year includes interest payments on the finance lease for the new Royal Adelaide Hospital for a part of that year ($70.6 million) while 2016-17 includes the first full year of interest costs on this finance lease ($211.4 million).

Exposure to rising interest rates is heightened through the increase in net debt. The Budget notes that a 1% increase in the average interest rate applying to general government sector debt would increase net interest expense by approximately $67 million in 2013-14 rising to $76 million in 2016-17.

2.6.5 Savings initiatives

Savings initiatives have been a major element of recent Budgets. The 2010-11 Budget consolidated savings announced in earlier Budgets (of over $700 million p.a. by 2013-14) into new savings which totalled $1.5 billion over a four year period arising from the recommendations of the Sustainable Budget Commission. These were additional to cost recovery and revenue measures ($478.6 million) and some retained savings included in agencies from previous Budgets.

The 2010-11 Budget Papers itemised the new savings initiatives in Budget Paper 6 '2010-11 Budget Measures Statement'. This provided a reference for monitoring progress of those initiatives. The Budget Papers did not restate initiatives scheduled to commence in 2010-11, or that were not fully implemented, from previous Budgets.

Since the 2010-11 Budget subsequent budgets have introduced additional significant savings initiatives, including the following:

- The 2012-13 Budget introduced new savings initiatives totalling $430.7 million over the four years of the forward estimates. The two main measures were an increase in the efficiency dividend from 0.25% to 1% of employee expenses and the reduction of a further 1000 FTE staff over the forward estimates.

- The 2012-13 MYBR introduced $227.2 million of savings initiatives through introduction of an additional efficiency dividend of 1% p.a. reduction in the net cost of services and a reduction in costs in specifically identified portfolio areas.

- The 2013-14 Budget introduces savings measures of $140 million through the extension of the 1% p.a. efficiency dividend to 2016-17, the bringing forward of 2015-16 savings measures and reducing the maximum TVSP payout.

Previous Reports have emphasised that the savings task falls on all portfolios of government and, in the past, the Health and Ageing portfolio has not been able to achieve savings targets or has experienced other service demands that have necessitated additional funding.

The Budget notes that, with the exception of Health and Ageing, agency savings budgeted to commence prior to or in 2012-13 and across the forward estimates are substantially on track. The Health and Ageing savings task was reassessed as part of the 2012-13 MYBR. This included revising the level and timing of budget improvements it expected to be delivered across the forward estimates. Table 8.8 in Chapter 8 of this Report provides a summary of the reductions in the Health and Ageing savings task.

There remain significant new savings to be achieved for the last year (2013-14) of the 2010-11 Budget initiatives. In addition, subsequent budgets have identified additional savings of $797.9 million over the forward estimates.

Table 8.4 in this Report provides details of savings by portfolio for the 2010-11 Budget initiatives. Table 6.1 of 2013-14 Budget Paper 3 'Budget Statement' (page 113) provides details of the delivery of savings and revenue measures since the 2008-09 MYBR.

Another major savings area is the shared services initiative which, since its inception in 2007, has not met its original savings targets. Shared Services SA activities are discussed in Part A of this Report.

As previous Reports have highlighted, an inherent risk of the saving strategy of government is its sheer size and breadth. Achieving the task requires significant discipline and, as noted earlier, Health and Ageing has experienced difficulties meeting savings targets. Further, the introduction of additional savings targets subsequent to the 2010-11 Budget presents ongoing risks including industrial action, public demand to maintain services and ineffective and inefficient administrative performance.

It is also noted that the efficiency dividend increase in recent budgets is a broad savings measure that does not identify specific areas of government activity where savings are expected to be realised. The increase in the efficiency dividend and the broad nature of this savings initiative adds an additional element of flexibility and hence budget management oversight complexity to the overall savings task.

2.6.6 Full-time equivalents reduction management strategy

A key part of the 2010-11 savings strategy involved further reduction in public sector FTEs by 3743 FTEs, excluding increases from other initiatives. The 2012-13 Budget introduced a savings initiative to reduce a further 1000 FTE staff over the forward estimates, starting in 2013-14 with savings of $25 million and increasing to $86.6 million in 2015-16. The 2013-14 Budget brought forward the 2015-16 FTE reductions into the 2014-15 year.

To assist agencies to achieve the 2010-11 savings target, the Government introduced an enhanced redeployment process to match excess employees with suitable vacant roles. The Government considered that successful redeployment of excess employees into funded vacancies would significantly reduce the potential cost of reducing the workforce. The Government also approved further targeted voluntary separation program arrangements. A key condition is that TVSP offers are only to be made to employees who were declared excess to requirements because their positions have been or are to be abolished.

DTF advised that TVSPs are currently planned to continue to be available over the forward estimates. The 2013-14 Budget notes that, from 1 July 2014, the maximum TVSP payout will be reduced from 116 weeks pay to 52 weeks pay.

The 2013-14 Budget states that FTE reductions can also be achieved in other ways (for example, natural attrition) and that the Government will honour its pledge of a ‘no forced redundancy’ policy for the remainder of this electoral term. After 30 June 2014, a public sector employee who has been identified by their agency as having been excess for longer than 12 months (and during that time has been assisted to find alternative public sector employment) would be able to be separated with an appropriate financial package having regard to the *Public Sector Act 2009* or other applicable legislation, and applicable industrial provisions.

DTF has advised Audit that between 1 November 2010 and 30 June 2013 1502.1 FTE reductions were achieved through TVSP payments (excluding executive reductions) as reported to DTF. Table 8.7 and related commentary in Chapter 8 of this Report provide further details.

For 2012-13 Audit sought an update of FTE monitoring arrangements and data as at 30 June 2013. DTF’s response, based on data received from major agencies, showed overall, that agencies were estimating they would be 437 FTEs below their budgeted FTE levels as at 30 June 2013. The overall position comprised various agencies being over and under their cap. For example:

- the Department of Health and Ageing has reported that actual FTEs were 296 FTEs above its cap primarily due to difficulties in specifying the FTE cap for the health regions
- the Department of Planning Transport and Infrastructure reported actual FTEs of 160 FTEs below its cap mainly due to vacancies and ongoing positions that are being filled by contractors
- South Australia Police reported actual FTEs of 172 FTEs below its cap mainly due to vacancies in unsworn officers.

Table 8.6 and related commentary in Chapter 8 of this Report provide further details.

2.6.7 Capital payments

For the period 2009-10 to 2012-13 the State has achieved capital expenditure exceeding $2 billion annually in every year except 2011-12 ($1.9 billion). As in past years, carryover adjustments were made for delays where expenditure will now be incurred in later years. As part of the budget carryover process, investing carryovers from 2012-13 to 2013-14 and future years are $74 million.

As reported in previous years the significance of the capital outlays and activity introduces a heightened risk to the proper management and control of capital projects. This situation remains, with purchases of non-financial assets estimated to be $1.9 billion in 2013-14. The budget includes a slippage allowance for 2013-14 of $210 million, compared to $300 million in the previous year.

The capital program also comprises large projects with inherent complexities and risks. Over the four years to 2016-17 capital spending includes $522.5 million on major rail projects, $833.4 million on road projects, $542.8 million on the redevelopment of major metropolitan and regional hospitals and $131.9 million for the redevelopment of Adelaide Oval.

2.6.7.1 New Royal Adelaide Hospital - Public Private Partnership project

In June 2011 the Government announced financial close on a contract with SAHP to build, operate and maintain the new Royal Adelaide Hospital under a PPP arrangement. The Government agreed on a fixed price for the design, construction, risk management and running and maintenance costs of the new hospital. The total capital cost of the new hospital at contractual close was $2.09 billion comprising SAHP's contracted design and construction cost of $1.85 billion and $244.7 million for state works including clinical equipment.

The new Royal Adelaide Hospital is recognised as an asset and a finance lease liability of $2.8 billion in the 2015-16 forward estimate year. This accounts for the large increase in net debt in 2015-16. The amount represents the net present value of design and construction costs, lifecycle payments, interest and other project costs.

Annual service payments are also budgeted to commence in 2015-16, with $126.9 million included for that year. This amount only represents a part year payment based on the expected opening date of the new Royal Adelaide Hospital. DTF has advised that for the 2016-17 full year the total annual payment is estimated to be $395.3 million.

Only part of this annual payment amount will be expensed each year as it includes cash payments that are applied to the reduction in the lease liability, which DTF has advised in a full year will be $111.7 million. The remainder of the payment is reflected as an expense, including finance charges on the lease and operating expenditure.

DTF also advised that an annual expense of $73 million is expected relating to the amortisation of the asset on the balance sheet.

2.6.7.2 Asset sales

Sales of non-financial assets are netted from purchases of non-financial assets when determining total net acquisition of non-financial assets. Total asset sales for the general government sector over the four years to 2016-17 are estimated to be $741 million.

Sales of non-financial assets peaked in 2012-13 at $1.2 billion as a result of the finalisation of two significant sale processes in 2012-13: proceeds from the forward sale of the State's Green Triangle forest plantations ($635.1 million) and proceeds from the appointment of Tatts Lotteries SA Pty Ltd as exclusive Master Agent to operate the SA Lotteries' brands and products for a term of 40 years ($402.8 million). These amounts are exclusive of stamp duty.

These sale amounts have flowed through to the net lending result and net debt. For further discussion on these two sale processes please refer to Part A of this Report.

2.6.8 Budget monitoring

The critical importance of strong monitoring of budget progress has been continually emphasised in previous Reports. DTF has advised Audit of specific measures in place. They include monthly monitoring of financial performance and quarterly monitoring of capital projects, savings measures and FTEs. Further, monitoring reports continue to be provided to the SBCC based on information supplied by agencies and analysis prepared by DTF.

Given the magnitude of the Budget improvement measures introduced in the 2010-11 Budget and the importance to the fiscal outlook of the achievement of these measures, DTF introduced an enhanced monitoring process in 2010-11 to monitor agency progress in achieving the measures and FTE reductions. This monitoring regime continues in 2013-14. Specific processes concluded or introduced since 2010-11 are described in section 8.4.8 of Chapter 8 of this Report.

2.6.8.1 Department for Health and Ageing

At the time of the 2012-13 Budget, the Department for Health and Ageing was projected to overspend its 2011-12 Budget by $122 million. A provision was made in the Budget for this projected overspend. In addition, the 2012-13 Budget included new operating initiatives totalling $167 million in 2012-13 and 2013-14 to re-profile the Department for Health and Ageing’s budget savings task. The aim was to provide the Department with additional resources for a more even annual build up of savings to enable it to achieve its aggregate savings target by 2014-15.

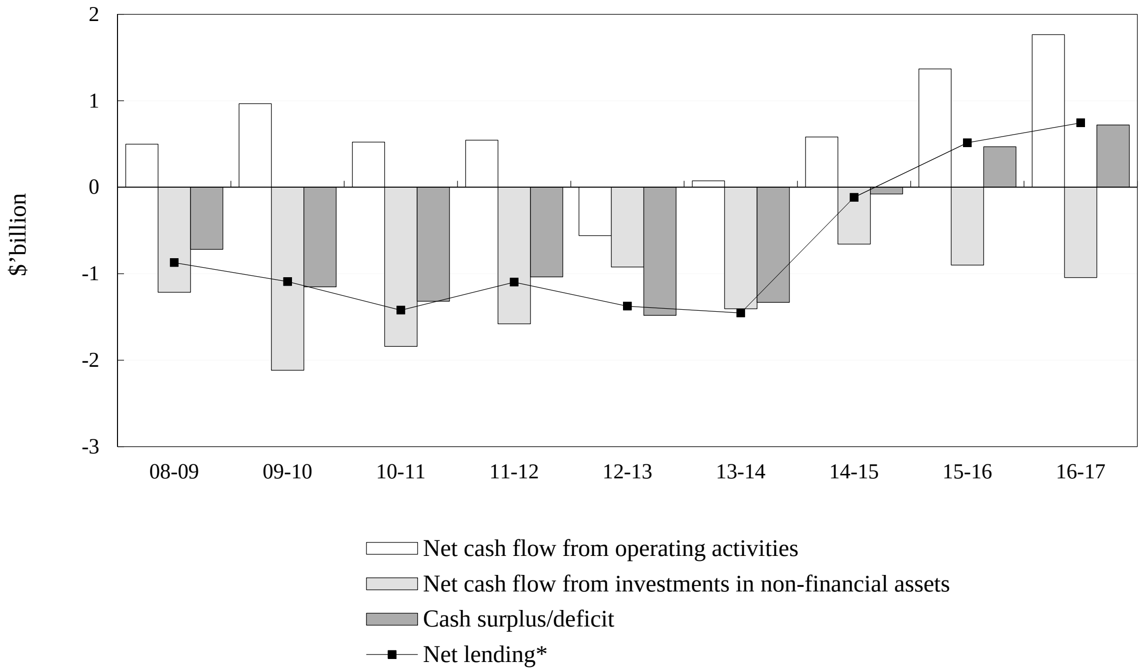
DTF has advised that the 2011-12 overspend of $122 million and the $167 million in operating initiatives in the 2012-13 Budget have been factored into the Health and Ageing savings targets as reprofile in subsequent years.

The Government has re-assessed the level and timing of budget improvement it considered the Department could deliver across the forward estimates. This resulted in a reduction, totalling $523.2 million, to the Department’s budget savings target over the forward estimates in the 2012-13 MYBR. Section 8.4.8.1 of Chapter 8 of this Report provides further details on the Health and Ageing savings task, including a summary of the revised savings measures and initiatives.

2.6.9 General government sector cash flow

Net lending indicates the expected borrowing requirements each year. There is a close relationship between this figure and the cash surplus/deficit as reported in the general government sector cash flow statement. Positive operating cash flows contribute to the capital expenditure program and reduce the reliance on debt to finance these asset acquisitions. The following chart shows the actual cash flow position for the general government sector for recent years, the estimated cash flow as at 30 June 2013 and the expected cash flow over the four years of the 2013-14 Budget.

Chart 2.11 – General government sector cash flow



* For the purposes of this cash flow analysis the impact of the new Royal Adelaide Hospital is excluded from net lending in 2015-16

The chart demonstrates an estimated deterioration in net operating cash flows in 2012-13 before a significant expected improvement in these cash flows in the last two years of the 2013-14 Budget, resulting in overall cash surpluses. These expected cash surpluses are critical in ensuring operating cash flows cover the net cash outflows associated with investments in non-financial assets and contribute to reducing net debt.

2.7 Concluding observations

The Government has stated that the 2013-14 Budget provides the fiscal underpinning for the Government's economic plan by controlling spending and debt, whilst ensuring strategic objectives are progressed. The Government notes that the 2013-14 Budget seeks, as far as possible, to insulate the general public from the national impacts of recent international developments whilst providing a sound fiscal platform as the economy and markets recover.

The Budget reports that, across the budget forward estimate period, the South Australian economy is expected to return to long-term average growth rates supported by government infrastructure spending and improved consumer sentiment.

In the general government sector, the Budget contains new operating initiatives totalling $475.9 million and new investing initiatives totalling $833.4 million. These significant initiatives have been offset by new operating and investing savings, revenues from external sources associated with the initiatives and the use of provisions made in earlier budgets.

The general government sector net debt is expected to increase from $5.6 billion as at 2012-13 to $8.8 billion as at 2016-17. Expressed as a percentage of revenue, this increases net debt from 36.8% in 2012-13 to 47.4% as at 2016-17. As at 2015-16 the net debt to revenue ratio is expected to be 54.2%, which exceeds the debt fiscal target of a maximum ratio of

50%. The net debt increase is significantly impacted on by the recognition of the new Royal Adelaide Hospital ($2.8 billion) in 2015-16.

There have been significant increases in net debt estimates over successive budgets since 2009-10. This increase reflects the maintenance of a significant capital expenditure program over a period where there were major write-downs in revenue estimates over successive budgets. These downward revisions in revenue estimates (mainly taxation and GST revenue grants) have placed significant pressure on the Budget.

Revenues are estimated to improve significantly in the last three years of the 2013-14 Budget. These revenue increases reflect expectations of a return to normal historical growth trends and come off a base of significant revenue write-downs in previous budgets.

Comparison with past experience shows that the 2013-14 Budget estimates for key revenue lines are mostly consistent with past average experience but revenue performance is sensitive to economic activity. GST revenue has now shown to be highly sensitive to household spending patterns. State taxation also varies with economic activity and demand for housing. In particular, conveyance duties are a volatile revenue stream that is sensitive to both transaction levels and transaction prices.

Comparing the trend of key estimated expenses for the 2013-14 Budget with past average experience shows a diverging difference. This difference highlights the significance of the expenditure restraint required in the 2013-14 Budget.

Salaries and wages remains the main public sector operating cost. Budget commentary states that the outcomes of future wage negotiations will be crucial in determining whether expenditure forward estimates in this Budget can be achieved, and the level of government services that can be delivered in light of the current challenging economic conditions.

There are significant new savings to be achieved for the last year (2013-14) of the 2010-11 Budget initiative. In addition, subsequent budgets have identified additional savings of $797.9 million over the forward estimates. The Budget notes that, with the exception of Health and Ageing, agency savings budgeted to commence prior to or in 2012-13 and across the forward estimates are substantially on track. The Health and Ageing savings task was reassessed as part of the 2012-13 MYBR. This included revising the level and timing of budget improvements it expected to be delivered across the forward estimates.

The 2013-14 Budget continues a significant capital spending program with purchases of non-financial assets estimated to be $1.9 billion in 2013-14 and presents a continuing heightened risk to the proper management and control of capital projects.

For the general government sector, sales of non-financial assets peaked at $1.2 billion in 2012-13. Sales in 2012-13 include proceeds from the Forestry and Lotteries sale processes of $1 billion. These asset sale proceeds flowed through as a once-off opportunity for debt reduction. The sale of these assets means that the Government no longer bears the risk of annual variable expense and revenue flows from these activities. This also means that the net annual revenue flows and opportunities from these activities are also foregone.

The 2013-14 Budget is the fifth Budget since the onset of the global financial crisis. These Budgets have been set against the background of economic and financial uncertainty and volatility and this has translated into considerable deterioration of the key indicators across the forward estimates. Successive Budgets have revised down the estimated net operating result, primarily due to major deterioration of taxation and GST revenue estimates over this period. This has had a consequent impact on net lending and net debt over a period where a major capital expenditure program has been maintained.

The 2013-14 Budget projects a return to a net operating balance surplus in the penultimate year of the forward estimates (2015-16) and a return to net lending surplus in the final year of the forward estimates (2016-17). Consistent with recent past budgets the proposed outcomes are based on revenue growth (through an improved economy) and the achievement of a significant savings program. As with those budgets, a continuation of difficult economic conditions will translate into a very difficult and challenging task of achieving the stated 2013-14 Budget outcomes, including out year surplus results.

3 Reporting framework

3.1 Introduction

Three reporting frameworks are used for reporting on the State's finances, namely the:

- Uniform Presentation Framework
- AASs
- Treasurer's Statements pursuant to the PFAA.

The following sections provide a brief overview of each of the frameworks.

3.2 Uniform Presentation Framework

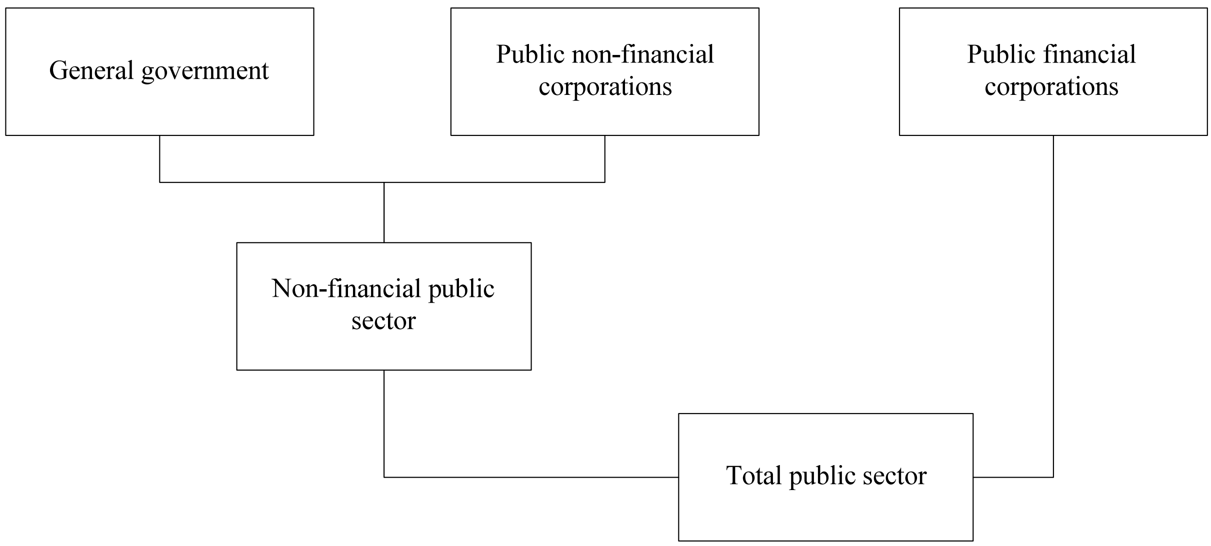
3.2.1 Background

By agreement between the Commonwealth, states and territories, each jurisdiction presents their Budget Papers and mid-year budget update on a Uniform Presentation Framework basis.

The Uniform Presentation Framework is a reporting standard based on the ABS's accrual based GFS framework. The primary objective of the Uniform Presentation Framework is to ensure that Commonwealth, state and territory governments provide a common core of financial information in Budget Papers to enable direct comparisons amongst jurisdictions.

In South Australia, the Budget is prepared using the GFS framework. The GFS framework excludes revaluations from the GFS net operating balance, as they are not transactions for the purposes of the GFS framework.

Three sectors (which are then consolidated into two additional sectors) of government activity are used in the GFS framework recognising that State Government responsibilities cover a wide range of activities. They are:



A description of the makeup of the three primary sectors is as follows.

General government **–** all budget dependent departments and agencies providing services free of charge or at prices below their cost of production or service cost. These are the services that tend to be financed mainly through taxes and other charges, and for this reason this sector tends to be the focus of fiscal targets.

PNFCs **–** trading enterprises mainly engaged in the production of goods and services for sale in the marketplace at prices that aim to recover most or all of the costs involved. In South Australia the sector includes the South Australian Housing Trust and the South Australian Water Corporation (SA Water). The consolidation of the general government and PNFCs represents the NFPS.

PFCs **–** bodies primarily engaged in the provision of financial services. This includes financial institutions such as SAFA, HomeStart Finance and the Superannuation Funds Management Corporation of South Australia (Funds SA).

The Budget Papers include the following GFS financial statements:

- general government sector Operating Statement and Balance Sheet
- PNFC sector Operating Statement and Balance Sheet
- NFPS Operating Statement and Balance Sheet
- cash flow statements for these sectors.

The PFC sector data is not published in the Budget Papers.

3.2.1.1 Key Government Financial Statistics headline amounts

When analysing GFS financial statements, the key GFS headline amounts are as follows:

- ***GFS net operating balance*** **–** the excess of GFS revenues over GFS expenses.

- ***GFS net lending/borrowing*** **–** the net operating balance less net acquisition of non-financial assets. It indicates the extent to which accruing operating expenses and net capital investment expenditure is funded by revenues.

- ***Net worth*** **–** a financial position measure that comprises total assets (financial and non-financial) less total liabilities less any contributed capital. This measure includes non-current physical assets (land and fixed assets) and employee entitlements such as unfunded superannuation and employee leave balances.

- ***Net financial liabilities*** **–** comprises total liabilities less financial assets (net financial worth), but excludes equity investments (net worth) in the other sectors of the jurisdiction.

- ***Net debt*** **–** comprises certain financial liabilities less financial assets. The items included in this measure are discussed in depth in the Budget Papers.[3]

[3] Net debt equals the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements as defined in the GFS framework.

3.2.2 Scope of audit review of Government Financial Statistics financial statements

This Report primarily covers commentary on GFS based information. Although Audit seeks to have a sound understanding of the Budget preparation process, the data and assumptions are not subject to audit. Work performed on the 2013-14 Budget year's GFS data has included some analytical procedures to ensure that the amounts presented are reasonably supported and where trends in data materially differ, that they can be adequately explained.

Accordingly, no opinion is provided on the accuracy of either the historic or prospective figures presented.

3.3 Australian Accounting Standards

The AASs framework is the basis for agency (budget and actual) and whole-of-government (actuals only) reporting.

3.3.1 Agency financial reports

The statutory financial reports that are prepared by individual agencies and subject to audit are compiled using AASs.

3.3.2 AASB 1049 Whole of Government and General Government Sector Financial Reporting

A summary of information prepared on this basis is provided in Chapter 12 of this Report.

The whole-of-government/general government CFR has been prepared pursuant to accounting standard AASB 1049. AASB 1049 specifies requirements for whole-of-government financial reports and general government sector financial reports of each government. The standard requires compliance with other applicable AASs except as specified in the standard and disclosure of additional information such as reconciliations to key fiscal aggregates determined in accordance with the ABS 'Australian System of Government Financial Statistics: Concepts, Sources and Methods'.

3.3.3 Convergence of Government Financial Statistics and Australian Accounting Standards

The AASB has been working towards the objective of harmonising generally accepted accounting principles and the GFS to achieve a single standard to produce comparable government budgets and financial statements that are auditable and comparable. Some elements of this project were undertaken in response to a direction from the Financial Reporting Council.

The AASB has previously released two exposure drafts in relation to this matter: ED 174 in 2009 and ED 212 in 2011. The AASB considered feedback resulting from both of these exposure drafts and decided, in December 2012, that it would not proceed with a standard consistent with these exposure drafts as a whole.

The AASB informed the Financial Reporting Council of the decision not to proceed with a standard as a result of ED 212 as a whole. Reasons behind this decision included:

- enabling entities within the general government sector to select accounting policies available to public sector entities outside of the general government sector
- the costs of implementing GFS-aligned measurement policies
- the divided views expressed by those commenting on ED 212 regarding the benefits of the proposals.

The Financial Reporting Council, at its March 2013 meeting, agreed to withdraw the directive to the AASB regarding generally accepted accounting principles/GFS harmonisation.

While the AASB decided not to proceed with a standard based on ED 212 as a whole, the AASB concluded that there was merit in proceeding with a standard requiring not-for-profit entities within the general government sector to report original budgeted information and explanations of major variations from budget.

As a result the AASB issued two standards in March 2013: AASB 1055 Budgetary Reporting and AASB 2013-1 Amendments to AASB 1049 Relocation of Budgetary Reporting Requirements.

AASB 1055, which applies to reporting periods beginning on or after 1 July 2014, will require not-for-profit entities within the general government sector whose budget is presented to Parliament, the general government sector and the whole-of-government financial statements to disclose, in their financial statements:

- original budget information, presented and classified on a basis which is consistent with the financial statements prepared in accordance with AASs
- explanations of major variances between the budget and actual amounts (which may include reference to revised budgets presented to Parliament).

These disclosure requirements will apply to both the controlled and administered items of an entity where budget information for both is presented to Parliament.

3.4 Treasurer's Statements – *Public Finance and Audit Act 1987*

The Treasurer's Statements are prepared pursuant to the requirements of the PFAA and reported as the appendix in Volume 6 of Part B of this Report.

A summary of information prepared on this basis is provided in Chapter 11 of this Report.

4 Summary of key fiscal measures and targets

4.1 South Australian fiscal targets

The 2013-14 Budget Papers[4] indicate that the Government is committed to the following fiscal targets:

Target 1: *A net operating surplus by the end of the forward estimates.*

Target 2: *Once surplus is achieved, operating expenditure growth will be limited to trend growth in household income.*

Target 3: *Achieve a level of general government net debt that remains affordable over the forward estimates – a maximum ratio of net debt to revenue of 50%.*

Underpinning the general government debt target the Government continues its commitments that:

- consistent with the Government's obligations under the Competition Principles Agreement, operations of public corporations that cannot be paid for from their own revenue streams will be funded from the budget
- the defined benefit unfunded superannuation liability will be fully funded by 2034.

4.1.1 General government net operating balance

A net operating surplus means that revenues will cover expenses, including interest and depreciation. South Australia is forecasting a return to net a operating surplus of $375 million in 2015-16 with deficits expected in both of the preceding two years of the 2013-14 Budget.

In the 2011-12 Budget the Government had targeted at least a net operating surplus in the general government sector every year.

The net operating deficit position continues to be impacted by adverse revenue movements in state taxation and expected GST receipts.

4.1.2 General government net debt to revenue

The Government's fiscal target of net debt is set at a maximum ratio of net debt to revenue of 50%. General government sector net debt is expected to increase from $5.6 billion as at 30 June 2013 to $8.8 billion as at 30 June 2017. The estimated increase in net debt incorporates the recognition of the financial obligations for the new Royal Adelaide Hospital on the State's balance sheet in 2015-16, which increases net debt by $2.8 billion. As at 2015-16 the ratio is 54.2%, which exceeds the debt fiscal target of a maximum ratio of 50%. By 30 June 2017 the ratio of net debt to revenue is expected to fall to 47.4%.

4 2013-14 Budget Paper 3 'Budget Statement', page 7.

4.2 Fiscal measures in other jurisdictions

In considering the State's fiscal strategy, it is useful to note the current practice across Australian jurisdictions. This is set out below.

Jurisdiction	Budget fiscal objective/strategy[(a)(b)]
Commonwealth	Achieving a budget cash surplus, on average, over the medium-term. Keeping taxation as a share of gross domestic product below the level for 2007-08 (23.7% of gross domestic product) on average. Improving the Government's net financial worth over the medium-term.
NSW	Maintain operating balances and debt positions that are consistent with the State's triple-A credit rating. Hold expense growth below long-run revenue growth. Total state sector unfunded superannuation liabilities eliminated by 30 June 2030.
Vic	Infrastructure investment of 1.3% of GSP (as a five year rolling average). General government net debt reduced as a percentage of GSP over the decade to 2022. Fully fund the unfunded superannuation liability by 2035. A net operating surplus of at least $100 million and consistent with the infrastructure and debt parameters.
Qld	Stabilise then significantly reduce debt (NFPS). Achieve and maintain a general government sector fiscal balance by 2014-15. Target full funding of long-term liabilities such as superannuation in accordance with actuarial advice. Maintain a competitive tax environment for business.
WA	Ensure general government sector annual expense growth does not exceed revenue growth. Maintain a cash surplus from operating activities for the general government sector of at least 50% of infrastructure spend per year.. Maintain the total non-financial public sector net debt to revenue ratio at or below 55%. Maintain a cash operating surplus for the total non-financial public sector of at least 5% of operating cash receipts. Provide a fair and efficient taxation system that is competitive with other states.
ACT	Achieve a general government sector net operating surplus. Maintain the territory's AAA credit rating. Manage debt prudently and maintain net financial liabilities within the range of all AAA rated jurisdictions. To fully fund the Territory's unfunded superannuation liability by 2030. Maintain operating cash surpluses. Maintain quality services and infrastructure. Make targeted investments to achieve strategic objectives of economic growth, reducing future costs and addressing chronic disadvantage. Maintain taxation revenues at sustainable levels. Deliver more efficient and productive public services, within tight financial constraints. Build a more productive and competitive economy.

Jurisdiction	Budget fiscal objective/strategy[(a)(b)]
Tas	Achieve a net operating balance greater than $50 million by 2014-15 and $200 million by 2022-23. Ensure recurrent services can be fully funded from recurrent revenue. Align expenditure growth and the need for infrastructure renewal and development with long-term growth in revenue.
NT	Eliminate the fiscal imbalance in the Territory's non-financial public sector by 2017-18. Achieve a net operating surplus for the Territory's general government sector by 2016-17. Taxation effort in the Territory's general government sector is more on par with the average effort of the states by 2016-17. The Territory's government owned corporation is moving towards commercial rates of return on capital employed by 2016-17. The Territory's non-financial public sector net debt as a percentage of revenue is returning towards 60% by 2020.

(a) Unless otherwise stated, all fiscal measures relate to the ABS defined general government sector.

(b) Other targets may also be used in relation to such areas as debt, taxes, expenses, net worth, superannuation, infrastructure and risk.

4.3 Some audit observations on the fiscal measures

Consistent with the prior year, the majority of jurisdictions continue to have a medium-term focus. Like South Australia, other jurisdictions have framed budgets working towards achieving budget surplus and reducing debt.

Like South Australia, other jurisdictions have framed budgets working towards funding unfunded superannuation liabilities in the long term. Many jurisdictions have targeted strategies to maintain or improve competitive taxation regimes.

5 Estimated results for 2012-13

5.1 Overview

The following section summarises the estimated operating results for 2012-13.

5.2 2012-13 estimated results

5.2.1 General government sector

The estimated result for the year was a net operating deficit of $1314 million (budget $867 million deficit) and net lending deficit (borrowing) of $1376 million (budget $1901 million). The following table shows 2011-12 financial year data and differences between the estimated result and budget for 2012-13.

Table 5.1 – General government budget comparisons 2011-12 to 2012-13

Revenue:	2011-12 Actual $'million	2012-13 Budget $'million	2012-13 Estimated result $'million	Difference to budget $'million	Difference to budget %
Taxation revenue	3 854	4 057	4 099	42	1
Grants:					
Current	7 465	7 498	7 404	(94)	(1)
Capital	1 204	373	313	(60)	(16)
Sale of goods and services	2 015	2 006	2 045	39	2
Interest income	172	167	133	(34)	(20)
Dividend and income tax equivalent income	385	349	399	50	14
Other	811	608	856	248	41
Total revenue	15 905	15 059	15 249	190	1
Less: **Expenses:**					
Employee expenses	6 770	6 930	7 134	204	3
Superannuation expenses:					
Superannuation interest cost	407	340	314	(26)	(8)
Other superannuation expenses	666	742	746	4	1
Depreciation and amortisation	718	822	830	8	1
Interest expenses	427	414	404	(10)	(2)
Other operating expenses	3 993	3 987	4 329	343	9
Grants	3 183	2 692	2 806	115	4
Total expenses	16 164	15 926	16 563	637	4
Net operating balance	(258)	(867)	(1 314)	(447)	52
Less: **Net acquisition of non-financial assets**					
Purchases of non-financial assets	1 876	2 147	2 092	(55)	(3)
Less: Sales of non-financial assets	322	291	1 200	909	312
Less: Depreciation	718	822	830	8	1
Plus: Change in inventory	3	-	-	-	-
Plus: Other movements in non-financial assets	-	-	-	-	-
Total net acquisition of non-financial assets	839	1 034	62	(972)	(94)
Net lending (borrowing)	(1 098)	(1 901)	(1 376)	525	(28)

Note: Totals may not add due to rounding.

As shown in the table, when compared to the net operating deficit of $258 million in 2011-12, the 2012-13 Budget anticipated a net operating deficit of $867 million. This anticipated deficit increase of $609 million is due mainly to overall budgeted decreases in revenue totalling $846 million offset by overall budget decreases in expenditure totalling $238 million.

The decrease in the revenue budget is primarily caused by an $831 million decrease in capital grants revenue, with a $203 million decrease in other revenue offset by a similar increase in taxation revenue. The decrease in the 2012-13 expenditure budget is due mainly to a $491 million decrease in grants expense, offset by increases of $160 million in employee expenses and $104 million in depreciation.

The estimated result for 2012-13 shows a $447 million deterioration from budget, leading to a net operating deficit of $1314 million. Almost half of this deterioration from budget is impacted by the estimated $204 million increase in employee expenses. Increases compared to budget in other operating expenses ($343 million) and grants expense ($115 million) are partly offset by a $248 million increase in other revenue.

5.2.1.1 Net acquisition of non-financial assets

The 2012-13 estimated result for purchases of non-financial assets of $2092 million is $55 million below the 2012-13 Budget.

Table 5.2 shows that consistent with the high value of capital spending, some large adjustments were made in the course of 2012-13. The original Budget was increased predominately by carryovers from 2011-12 totalling $253 million.

The estimated result for 2012-13 allows for mid-year budget adjustments and carryovers beyond the year. Carryovers into 2013-14 and beyond of $74 million include deferral of $41 million for the Adelaide Oval redevelopment. The estimated result is also influenced by the adjustment of the slippage allowance reflecting the reduced uncertainty of projections.

Table 5.2 – Comparison of purchases of non-financial assets budget to 2012-13 estimated result

		$'million	$'million
2012-13 Budget			2 147
Add:	Policy decisions	4	
	Carryovers from 2011-12[a]	253	
	Adjustment to capital slippage provision (Net adjustment from MYBR and Budget)	70	327
Less:	Carryovers into 2013-14 and forward years	(74)	
	Significant project reprofiles	(218)	
	Use of provisions set aside in the 2012-13 Budget and the 2012-13 MYBR	(4)	
	Other (includes reclassifications to operating and contingency adjustments)	(86)	(382)
2012-13 estimated result			2 092

Note: Totals may not add due to rounding.

[a] Carryovers from 2011-12 published in the 2012-13 MYBR include a $30 million carryover of asset sales

5.2.2 Non-financial public sector

The NFPS (consolidating the general government and PNFC sectors) estimated result for the year was a net lending deficit (borrowing) of $1295 million, which is $122 million more than budget for the year.

The following table summarises the position.

Table 5.3 – NFPS Budget comparisons 2011-12 to 2012-13

	2011-12 Actual $'million	**2012-13 Budget $'million**	**2012-13 Estimated result $'million**	Difference to budget $'million	Difference to budget %
Revenue	16 866	16 168	16 377	209	1
Less: **Expenses**	16 908	17 068	17 689	621	4
Net operating balance	(41)	(901)	(1,313)	(412)	46
Less: **Net acquisition of non-financial assets**	1 383	272	(17)	(289)	(106)
Net lending (borrowing)	(1 424)	(1 173)	(1 295)	(122)	10

Note: Totals may not add due to rounding.

The increase in the net lending deficit (borrowing) by $122 million comprises the deterioration in the PNFC sector's result by $648 million and the improvement in the general government result by $525 million.

The deterioration in the PNFC sector's[5] net lending deficit (borrowing) from budget is due mainly to a decrease in sales of non-financial assets, reflecting the fact that the 2012-13 budget included an expectation that ForestrySA assets would be sold by a PNFC rather than general government.

5 2013-14 Budget Paper 3 'Budget Statement' , table A.2.

6 Budget 2013-14 overview

6.1 Overview

The following commentary focuses on the trends arising from the 2013-14 Budget. It provides an overview of:

- the Budget for 2013-14 having regard to the estimated result for 2012-13
- a longer term view of the forecast results going forward to 2016-17.

The analysis deals only with the accrual based GFS framework.

6.1.1 Matters of significance to the 2013-14 Budget

Net operating deficits are expected through to 2014–15 with the 2013-14 Budget projecting a return to a net operating surplus of $375 million for 2015-16.

While this is a $137 million deterioration on the 2015-16 net operating surplus previously predicted in the 2012-13 Budget, a key reason for this decline is the financial impact arising from a change in the accounting standard relating to the calculation of the nominal superannuation interest expense.

The net operating position continues to be impacted by adverse revenue movements, particularly reductions in GST revenue grants, which have been revised down by $522 million over the four years from 2012-13.

A net operating surplus of $661 million is estimated for 2016-17.

The 2013-14 Budget projects net lending deficits for the next three years, with a cumulative amount of $3879 million. This amount is impacted by the recognition of the new Royal Adelaide Hospital ($2.8 billion) in 2015-16.

Other specific items to note in the 2013-14 Budget estimates years are:

- new operating and investing initiatives totalling $1309 million over the next four years[6], including the use of $484 million of 'specific provisions' held as contingency provisions in previous budgets

- targeted savings, revenue offsets and reductions in capital programs totalling $724 million over four years[7]

- expenditure restraint compared to revenue growth is projected to lift the net operating balance to $661 million by 2016-17

- general government sector net debt increasing by $3140 million to $8751 million by June 2017.

Budgeted total revenues and expenses for 2013-14 are both lower than was previously estimated in the 2012-13 Budget.

6 2013-14 Budget Paper 3 'Budget Statement', table 2.1.
7 2013-14 Budget Paper 3 'Budget Statement', table 2.1.

As a consequence of these changes a net operating balance deficit of $911 million is now budgeted, a deterioration from the estimated $778 million deficit projected for 2013-14 in the 2012-13 Budget.

6.2 General government sector – Operating Statement

Table 6.1 sets out the differences between the 2013-14 Budget and the estimated results for 2012-13.

Table 6.1 – GFS – General government sector budget comparison of 2012-13 estimate results and 2013-14 Budget

Revenue:	**2012-13 Estimated Result $'million**	**2013-14 Budget $'million**	Difference $'million	Difference %
Taxation revenue	4 099	4 206	107	3
Grants:				
Current grants	7 404	7 590	186	3
Capital grants	313	293	(20)	(6)
Sale of goods and services	2 045	2 077	32	2
Interest income	133	102	(31)	(23)
Dividend and income tax equivalent income	399	328	(71)	(18)
Other	856	669	(187)	(22)
Total revenue	15 249	15 265	16	-
Less: **Expenses:**				
Employee expenses	7 134	7 155	21	-
Superannuation expenses:				
Superannuation interest cost	314	434	120	38
Other superannuation expenses	746	754	8	1
Depreciation and amortisation	830	895	65	8
Interest expenses	404	379	(25)	(6)
Other operating expenses	4 329	3 975	(354)	(8)
Grants	2 806	2 585	(221)	(8)
Total expenses	16 563	16 176	(387)	(2)
Net operating balance	(1 314)	(911)	403	(31)
Less: **Net acquisition of non-financial assets**				
Purchase of non-financial assets	2 092	1 858	(234)	(11)
Less: Sales of non-financial assets	1 200	419	(781)	(65)
Less: Depreciation	830	895	65	8
Total net acquisition of non-financial assets	62	544	482	777
Net lending (borrowing)	(1 376)	(1 455)	(79)	6

Note: Totals may not add due to rounding.

The major differences for the 2013-14 year are:

- an increase in current grants due mainly to increases in GST revenue grants and other contributions and grants, offset by a net reduction in other Commonwealth grants
- a $187 million decrease in other revenue due mainly to the once-off relief of South Australia's public housing loan payments to the Commonwealth in 2012-13, offset by an increase in royalty revenue
- a $354 million decrease in other operating expenses largely reflecting the once-off expense associated with the writing off of South Australian Housing Trust debt to the Treasurer in 2012-13

- a decrease in other grant expenses of $221 million reflecting the bring forward of payments for grants to local government from 2013-14, final payments for the on-passing of Commonwealth grants for the Adelaide desalination plant in 2012-13 and a reduction in annual grants to the South Australian Housing Trust associated with relief of $320 million on its balance sheet.

More detail of the factors influencing the 2013-14 Budget is considered in the context of the longer term trends discussed later in this Report.

6.2.1 Reconciliation of variations since 2012-13 Budget

Each year a reconciliation is included in the Budget Papers of the current budget estimates with the corresponding estimates for the previous year. This explains differences between budgets arising from what the Government categorises as parameter and policy changes.

'Parameter changes' are those that flow from other than policy choices. Revenue includes taxation changes from economic activity and Commonwealth revenue. Expenses include carryovers between years from timing effects, reclassifications and corrections.

'Policy changes' are the decisions made by the Government to increase or decrease taxation and spending.

The following table summarises all parameter and policy changes made since the 2012-13 Budget that affect the net operating balance and provisions used to offset some of those changes.[8]

Table 6.2 – Reconciliation of general government sector net operating balance

	2012-13 Estimated result $'million	2013-14 Budget $'million	2014-15 Estimate $'million	2015-16 Estimate $'million
2012-13 Budget	(867)	(778)	(15)	512
Parameter and other variations:				
Revenue - taxation	42	(49)	(106)	(125)
Revenue - other	99	(434)	(673)	(482)
Operating expenses	(515)	263	161	117
Net effect of parameter and other variations	(373)	(220)	(618)	(489)
Policy measures:				
Revenue - taxation	-	(11)	18	30
Revenue - other	(11)	37	6	18
Revenue - offsets	60	237	130	154
Operating expenses	(352)	(399)	(144)	(49)
Net effect of policy measures	(303)	(135)	11	153
Use of provisions set aside in the 2012-13 Budget and the 2012-13 MYBR:				
Operating expenses	229	223	191	199
2013-14 Budget	(1 314)	(911)	(431)	375

Note: Totals may not add due to rounding. Brackets mean an unfavourable change.

[8] 2013-14 Budget Paper 3 'Budget Statement', table 1.7.

6.2.1.1 Revenue variations

Table 6.2 highlights the expected downward revision of state taxation revenue and other revenue across the forward estimates. The decrease in other revenue includes parameter changes in the receipt of Commonwealth GST grants.

The following table shows the components of revenue parameter changes.[9]

Table 6.3 – Revenue parameter changes

	2012-13 Estimated result $'million	2013-14 Budget $'million	2014-15 Estimate $'million	2015-16 Estimate $'million
Commonwealth Specific Purpose and National Partnership grants:				
Special Purpose	(91)	(208)	(215)	(241)
National Partnership	(67)	(124)	(160)	109
Commonwealth contributions	-	-	-	-
GST revenue grants and transitional assistance	(48)	(47)	(187)	(239)
Property related taxes	79	(22)	(48)	(69)
Other State taxes	(37)	(27)	(58)	(56)
Dividends and income tax equivalents	50	(36)	(41)	(44)
Interest income	(35)	(53)	(40)	(17)
Other	290	34	(30)	(50)
Total	141	(483)	(779)	(607)

Note: Totals may not add due to rounding.

In particular table 6.3 shows the downward revisions since the 2012-13 Budget in GST distributions from the Commonwealth and State taxes across the forward estimates.

Commonwealth specific purpose and National Partnership grants have been revised to reflect the latest estimates included in the Commonwealth's 2013-14 Budget.

6.2.1.2 Operating expense variations

Table 6.2 shows that parameter effects are estimated to reduce operating expenses by $26 million over the four years to 2015-16.

Policy spending decisions since the 2012-13 Budget, however, add a further $944 million to operating expenses over the four year period of which $352 million is for 2012-13.[10] The following table shows the value of policy measures taken in each of the past five years after presentation of the Budget for the year.

Table 6.4 – Policy spending decisions

	2008-09 $'million	2009-10 $'million	2010-11 $'million	2011-12 $'million	2012-13 $'million
Policy measure operating expenses	296	344	125	199	352

[9] 2013-14 Budget Paper 3 'Budget Statement', table 1.9 and 2012-13 MYBR, table 1.5.
[10] 2013-14 Budget Paper 3 'Budget Statement', table 1.7.

Table 6.4 shows that $1316 million was added to spending for the past five years. This increase reflects established practice of discretionary expenditure decisions being taken after Budgets are announced.

As shown in table 6.2, policy expense adjustments since the 2012-13 Budget are only partially offset by revenue variations, contributing to the deterioration in the estimated net operating deficit for 2012-13 to $1314 million.

6.3 Public non-financial corporation sector – Operating Statement

A net operating deficit of $237 million is budgeted in 2013-14, a deterioration from the estimated result for 2012-13.

Net lending is budgeted to weaken to $316 million in 2013-14 due mainly to a net operating deficit of $237 million. The differences between the two years are set out in the following table.

Table 6.5 – GFS – PNFC budget comparison 2012-13 and 2013-14

	2012-13 Estimated result $'million	**2013-14 Budget $'million**	Difference $'million	Difference %
Revenue:				
Sale of goods and services	1 859	1 710	(149)	(8)
Other	1 094	615	(479)	(44)
Total revenue	2 952	2 324	(628)	(21)
Less: **Expenses:**				
Employee expenses	210	202	(8)	(4)
Superannuation expenses	24	24	-	-
Depreciation and amortisation	406	445	39	10
Interest expenses	246	236	(10)	(4)
Other property expenses	349	285	(64)	(18)
Other operating expenses	1 350	1 205	(145)	(11)
Other expenses	366	164	(202)	(55)
Total expenses	2 950	2 561	(389)	(13)
Net operating balance	2	(237)	(239)	-
Less: **Net acquisition of non-financial assets:**				
Purchase of non-financial assets	762	729	(33)	(4)
Less: Sales of non-financial assets	461	247	(214)	(46)
Depreciation	406	445	39	10
Add: Change in inventories	27	42	15	56
Total net acquisition of non-financial assets	(79)	79	158	(200)
Net lending (borrowing)	81	(316)	(397)	(490)

Note: Totals may not add due to rounding.

6.4 Non-financial public sector – Operating Statement

The 2013-14 budgeted result for the NFPS is a net operating deficit of $1148 million, an improvement of $165 million from the 2012-13 estimated result.

6.5 A longer term perspective of financial performance

The following sections provide additional details in an historical perspective.

6.5.1 General government sector Operating Statement time series

Table 6.6 provides a 10 year time series for those individual elements that contribute to the budget result.

Table 6.6 – GFS - General government sector Operating Statement - time series

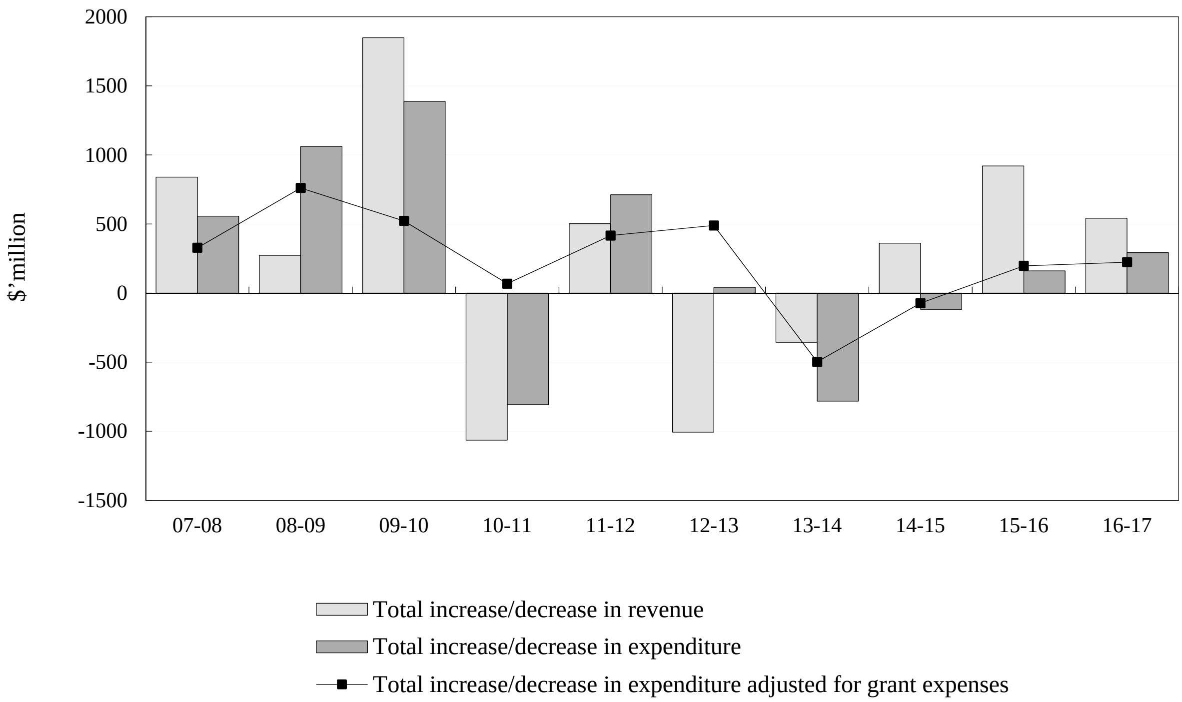
	2007-08 Actual	2008-09 Actual	2009-10 Actual	2010-11 Actual	2011-12 Actual	2012-13 Est. result	2013-14 Budget	2014-15 Estimate	2015-16 Estimate	2016-17 Estimate
Revenue:	**$'million**	**$'million**	**$'million**	**$'million**	**$'million**	**$'million**	**$'million**	**$'million**	**$'million**	**$'million**
Taxation revenue	3 570	3 537	3 649	3 831	3 854	4 099	4 206	4 479	4 813	5 109
Grants:										
Current	6 294	6 651	7 039	7 109	7 465	7 404	7 590	7 976	8 599	9 345
Capital	322	598	1 841	1 076	1 204	313	293	260	553	398
Sales of goods and services	1 572	1 697	1 936	1 879	2 015	2 045	2 077	2 150	2 228	2 323
Interest income	203	150	138	168	172	133	102	124	163	205
Dividend and income tax equivalent income	429	382	433	403	385	399	328	370	376	378
Other	490	517	497	550	811	856	669	669	687	696
Total revenue	12 879	13 531	15 534	15 017	15 905	15 249	15 265	16 027	17 419	18 454
Less: **Expenses:**										
Employee expenses	5 268	5 749	6 221	6 400	6 770	7 134	7 155	7 175	7 382	7 553
Superannuation expenses:										
Superannuation interest cost	276	383	455	427	407	314	434	429	422	415
Other superannuation expenses	546	580	600	621	666	746	754	760	772	784
Depreciation and amortisation	525	566	633	670	718	830	895	974	1 041	1 130
Interest expenses	218	180	204	308	427	404	379	430	556	742
Other operating expenses	3 246	3 624	3 695	3 824	3 993	4 329	3 975	4 086	4 240	4 397
Grants	2 337	2 682	3 540	2 819	3 183	2 806	2 585	2 603	2 629	2 771
Total expenses	12 414	13 764	15 347	15 069	16 164	16 563	16 176	16 458	17 043	17 793
Net operating balance	464	(233)	187	(53)	(258)	(1 314)	(911)	(431)	375	661
Less: **Net acquisition of non-financial assets**										
Purchases of non-financial assets	875	1 305	2 144	2 122	1 876	2 092	1 858	912	3 790	1 051
Less: Sales of non-financial assets	108	108	29	82	322	1 200	419	251	67	4
Less: Depreciation	525	566	633	670	718	830	895	974	1 041	1 130
Add: Change in inventories	-	7	3	-	3	-	-	-	-	-
Add: Other movements in non-financial assets	-	-	(206)	-	-	-	-	-	-	-
Total net acquisition of non-financial assets	242	639	1 279	1 370	839	62	544	(313)	2 682	(83)
Net lending (borrowing)	222	(872)	(1 092)	(1 422)	(1 098)	(1 376)	(1 455)	(118)	(2 306)	744

Note: Totals may not add due to rounding.

6.5.2 Net operating balance influences

The following chart shows the increase or decrease, in real terms, of total revenue and total expenses to the previous year for the 11 years to 2016-17.

Chart 6.1 – Increase/Decrease of total revenue and total expenses to previous year[(a)(b)]



(a) Estimated June 2013 values
(b) 2009-10 and 2010-11 are influenced by Commonwealth stimulus grants

Chart 6.1 starkly demonstrates the short and medium-term responses to the global financial crisis. 2009-10 shows the highest growth in revenues over the period due to additional Commonwealth stimulus money.

Revenue is affected by the very large Commonwealth stimulus grants wind-down. Part of the decrease in expenses in 2010-11 is the matching fall in related grant expenses. The line adjusted to exclude grant expenses shows the significance of movements in grant expenses over the three years to 2010-11.

The decrease in revenues for 2012-13 reflect the timing of Commonwealth National Partnership payments.

Real revenue increases are forecast for 2014-15 to 2016-17 due mainly to budgeted increases in Commonwealth GST grants and state taxation revenue.

7 Revenue

Trend data in charts in this section is in real terms at estimated June 2013 values unless otherwise stated.

7.1 Revenue overview

The expected reductions in GST revenue grants and taxation revenue in the 2012-13 Budget were far more significant than what was expected in previous budgets. This has had a major impact on the net operating balance and net debt projections. These reductions are not offset by Commonwealth economic stimulus funding, as was the case in the wake of the global financial crisis.

The 2013-14 Budget has revised GST revenue grants and taxation revenue down a further $722 million since the 2012-13 Budget and highlights how government revenues are impacted by property market conditions and household consumption.

Total general government sector revenues are estimated to be $15.3 billion in 2013-14, an increase of $16 million from the previous year's estimated result, and a real decrease of $356 million or 2.3%. In real terms total revenue is expected to increase by 9.6% by 2016-17.

The components of total revenue and trends in real terms are illustrated in the following chart.

Chart 7.1 – General government sector total revenue (real)

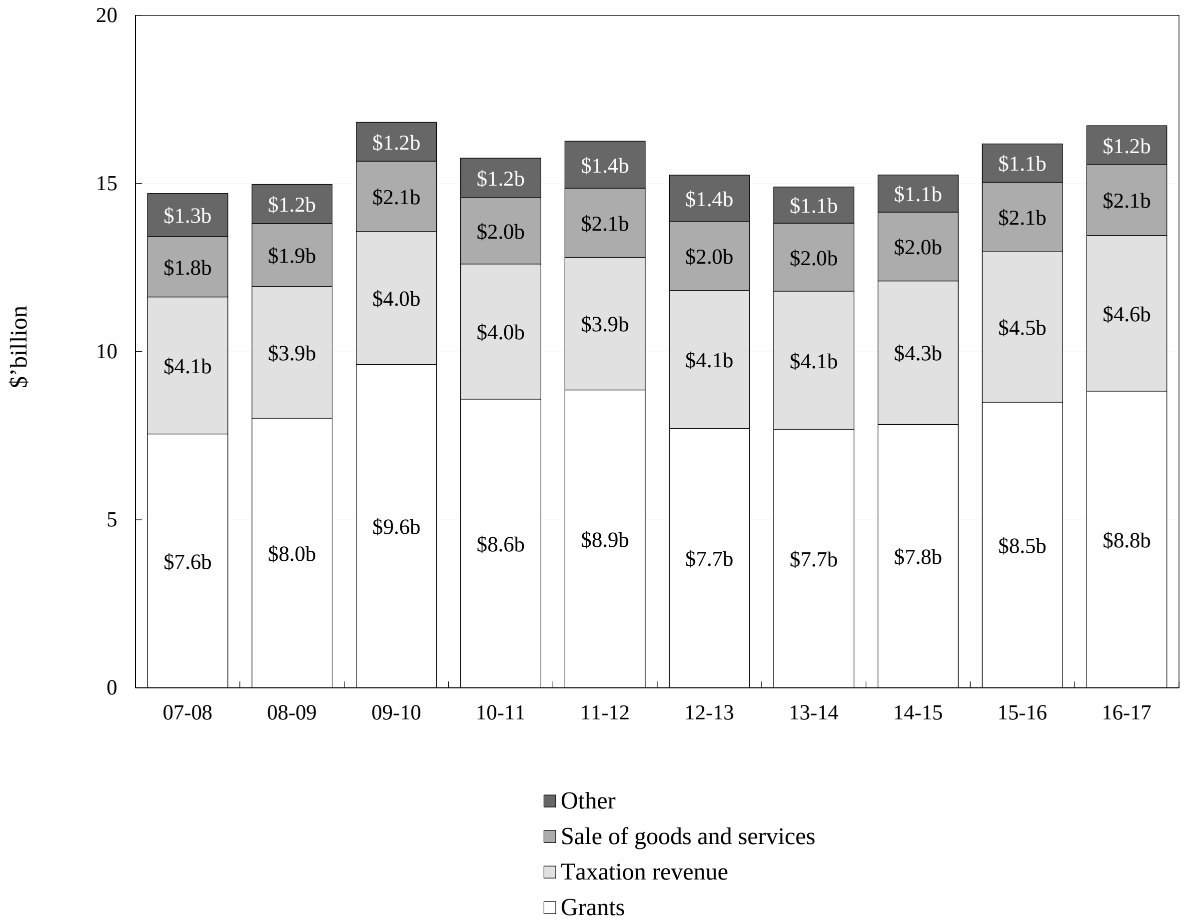


Chart 7.1 highlights the importance of Commonwealth grants to the State's revenues. Over most years Commonwealth grants represent about 50% of total revenue. During the period 2008-09 to 2011-12 Commonwealth revenue increased as a proportion of total State revenue, peaking at 55.9% in 2009-10. This increase was mainly due to temporary stimulus funding following the global financial crisis.

This percentage declines to 49.5% by 2012-13, a return to historical trends. While a relatively small change in percentage terms, this represents some hundreds of millions of dollars when total revenues are in the order of $15.2 billion (2012-13 nominal) and supports significant spending activity in targeted areas.

The following commentary provides some additional analysis of the main revenue areas. Detailed commentary is provided in Chapter 3 of the 2013-14 Budget Paper 3 'Budget Statement'.

7.2 Commonwealth grants

The Intergovernmental Agreement on Federal Financial Relations provides the framework for the Commonwealth's financial relations with the states and territories.

While Commonwealth funding is the foundation of State finances, it is not controllable by the State.

The following table outlines estimated Commonwealth grants for the five years to 2016-17 and demonstrates a 27% increase (nominal) over that period.

Table 7.1 – Commonwealth grants 2012-13 to 2016-17 (nominal)

	2012-13 $'million	2013-14 $'million	2014-15 $'million	2015-16 $'million	2016-17 $'million
Current grant revenue	7 250.9	7 342.8	7 830.2	8 452.6	9 197.9
Capital grant revenue	293.8	268.4	243.6	536.1	380.9
Total grants	7 544.7	7 611.2	8 073.8	8 988.7	9 578.8

The increase in current grants is due mainly to budgeted increases in GST revenue grants.

7.2.1 GST revenue grants

GST revenue grants for 2012-13 are expected to be $49 million lower than the original budget estimate, reflecting a decrease in the national GST pool estimated by the Commonwealth Treasury. The total GST pool is expected to increase by around 3.6% in 2012-13, compared to the Commonwealth's original budget estimate of growth of 5.7%.

GST revenue grants are distributed according to the principle of horizontal fiscal equalisation. The principle of horizontal fiscal equalisation is based on ensuring that each state has the capacity to provide public services at a similar standard and level of efficiency as the other states for a comparable revenue-raising effort.

In March 2013 the Commonwealth Grants Commission released its Report on GST Revenue Sharing Relativities – 2013 Update of per capita relativities for the distribution of GST revenue grants to the states in 2013-14.

The Commonwealth Grants Commission recommended a decreased relativity for South Australia, which will receive 9.1% of the GST pool in 2013-14. This represents a decline of around 0.3 of a percentage point compared to 2012-13.

Over the forward estimates, South Australia's GST revenue grants are expected to grow by 7.5% in 2014-15, 8.1% in 2015-16 and 10.1% in 2016-17.

7.2.2 Specific purpose payments

SPPs are provided under section 96 of the *Constitution* for both recurrent and capital expenditure purposes. States are required to spend the funding received under each national SPP in the relevant sector but have the flexibility to allocate funds within that sector to meet agreed objectives.

For 2013-14, with the exception of National Health Reform funding and the National Disability SPP, each state and territory will receive a share of each national SPP funding pool with 20% based on historical allocation and 80% based on population share. The allocation of National Health Reform funding and National Disability SPP for 2013-14 is solely based on population share.

The Commonwealth will eventually distribute all national SPPs between the states on a purely per capita basis according to ABS's population estimates. The Commonwealth started phasing in the per capita arrangements from 2009-10, with the timing varying between agreements.

National Health Reform and National Education and Early Childhood funding represents over 88% of South Australia's allocation of SPP funding of $2324 million for 2013-14. National Education and Early Childhood SPP grants include grants provided to the states for on-passing, mainly for non-government schools and local government. For 2013-14 SPP grants for on-passing total $731 million.

Estimates for the National Schools SPP do not incorporate additional funding proposed by the Commonwealth as part of national education reforms. While negotiations with the Commonwealth over these reforms were ongoing at the time of preparing the 2013-14 Budget, the current estimate of additional contributions by the State for the period 2014 to 2019 is $229.9 million. The additional Commonwealth contribution for this same period is estimated to be $427 million.

Over the forward estimates, SPPs are expected to increase from $2294 million in 2012-13 to $2652 million (real) in 2016-17, a real increase of $358 million. This growth in national SPPs reflects indexation arrangements specified in the Intergovernmental Agreement on Federal Financial Relations.

7.2.3 National Partnership Commonwealth grants

National Partnerships are a form of time limited payment under the Federal-State funding arrangements to fund specific projects and to facilitate and/or reward states that deliver on nationally significant reforms.

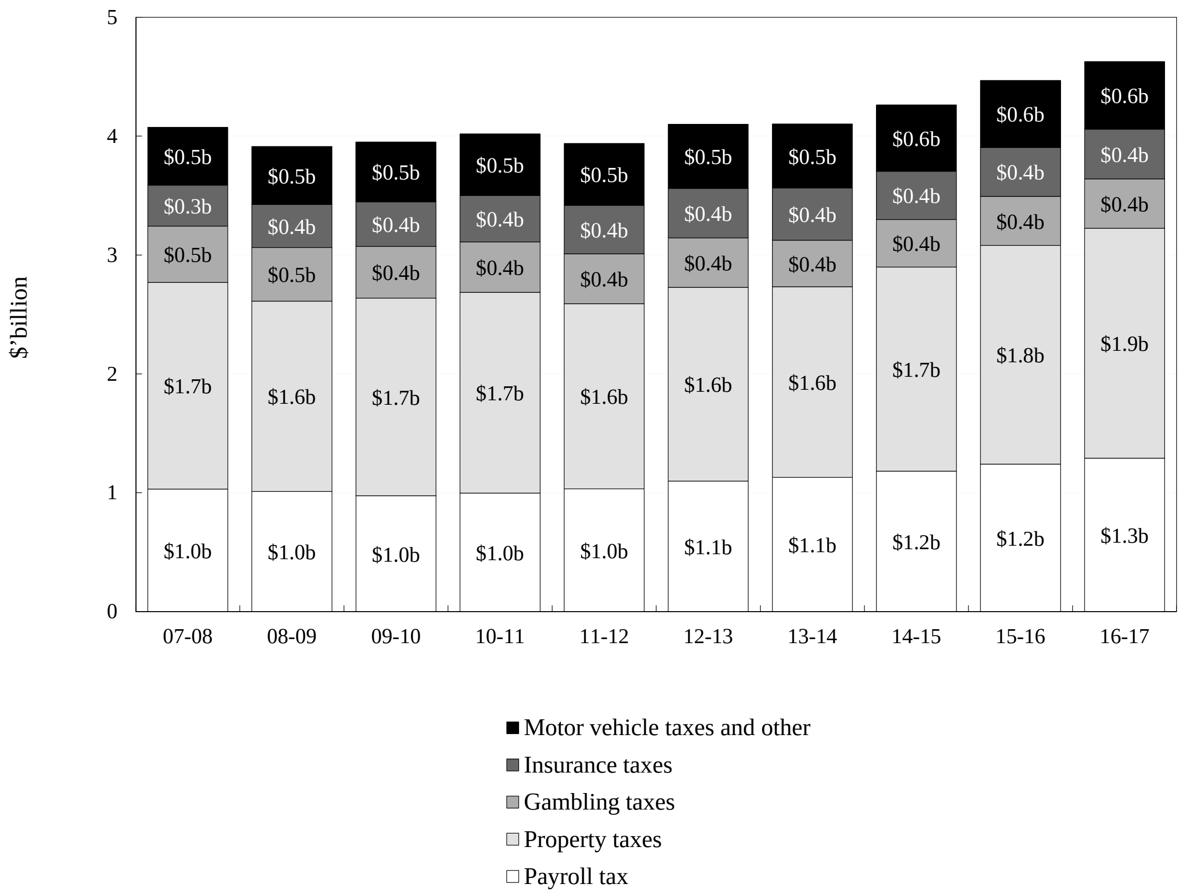
In 2013-14, South Australia will receive an estimated $554 million of National Partnerships funding for recurrent purposes. This is a decrease of 12% from the $626 million estimated for 2012-13. This decrease reflects changes in the timing of the Commonwealth's funding allocations.

7.3 Taxation revenue

Taxation revenue is the second largest source of revenue to the State and represents about 27% of revenues in 2012-13. It comprises a diverse range of activities, including payroll, property, motor vehicles and gambling.

The following chart examines the trend in the components of taxation receipts (in real terms) over the 10 year period to 2016-17.

Chart 7.2 – Taxation revenue (real)



Total taxes, in real terms, increase marginally in 2012-13 before rising over the last three years of the forward estimates. Chart 7.2 demonstrates that throughout this time series, variations in taxation revenue are primarily attributable to property taxes.

Taxation revenue for 2013-14 is estimated to be $4206 million (nominal), an increase of $107 million over the estimated result for 2012-13. It is expected to be $5109 million (nominal) in 2016-17, a real increase of $528 million compared to 2012-13.

7.3.1 Property taxes

Property taxes include land tax, stamp duty (including on the conveyance of property and transfers of non-quoted marketable securities), the Emergency Services levy on fixed property, the Save the River Murray levy, regional natural resources management levies and guarantee fees.

From 2014-15 property taxes also include a transport development levy, introduced in the 2012-13 MYBR. The levy will be set at $750 p.a. per car park space (excluding residential car parking and other non-chargeable privately owned car parks), indexed annually to movements in the CPI. The levy is estimated to generate $26 million in 2014-15 and is intended to encourage the use of public transport.

Property taxes for 2013-14 are estimated to be $1643 million (nominal), a real decrease of $27 million from the estimated result for 2012-13. They are expected to be $2135 million (nominal) in 2016-17, a real increase of $304 million compared to 2012-13. Chart 7.3 shows the trend in property taxes (in real terms).

Chart 7.3 – Taxes on property (real)

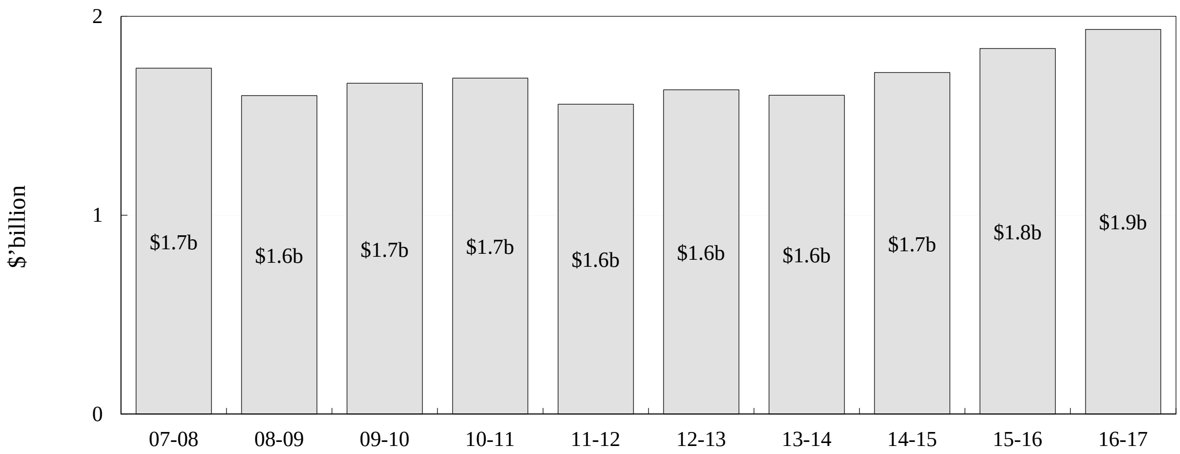
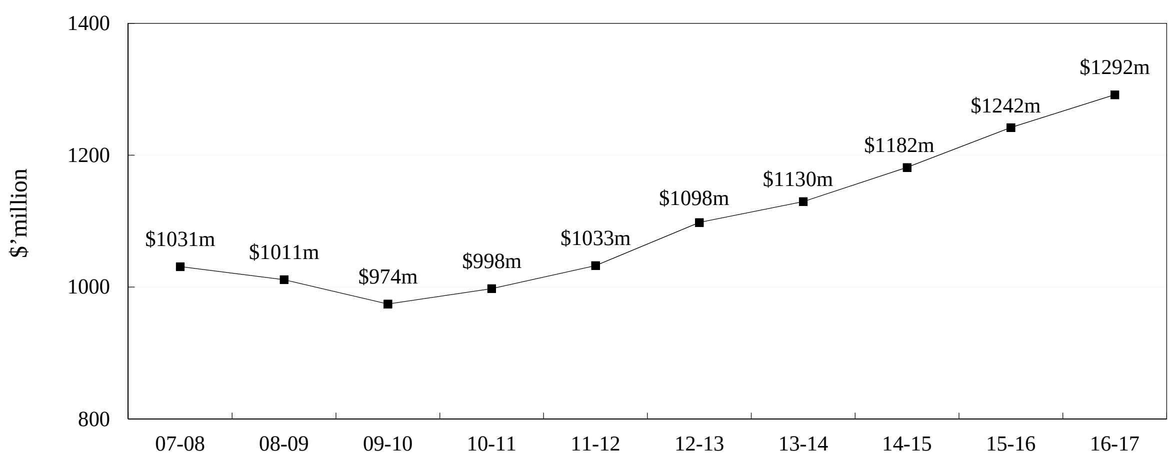


Chart 7.3 highlights the estimated increase in property taxes over the forward estimates, which is attributable to estimated growth in the number of property transactions, from the 25 year low level recorded in 2011-12, and annual real growth in property prices from 2014-15.

7.3.2 Payroll tax

Payroll tax is a principal source of taxation revenue. Chart 7.4 shows payroll tax revenue is anticipated to increase in real terms over the forward estimates.

Chart 7.4 – Employer payroll tax (real)



Payroll taxes for 2013-14 are estimated to be $1158 million (nominal), a real increase of $32 million from the estimated result for 2012-13. The payroll tax threshold remained at $600 000 on 1 July 2012. In addition, the payroll tax rate also remained at 4.95%.

Payroll tax is expected to be $1426 million (nominal) in 2016-17, a real increase of $194 million compared to 2012-13.

7.3.3 Gambling taxes

Gambling taxes for 2013-14 are estimated to be $402 million (nominal), a real decrease of $24 million from the estimated result for 2012-13. Gambling taxes are not expected to return to the 2012-13 estimated results (in real terms) until the end of the forward estimates. The following chart shows the trend in gambling taxes.

Chart 7.5 – Gambling taxes (real)

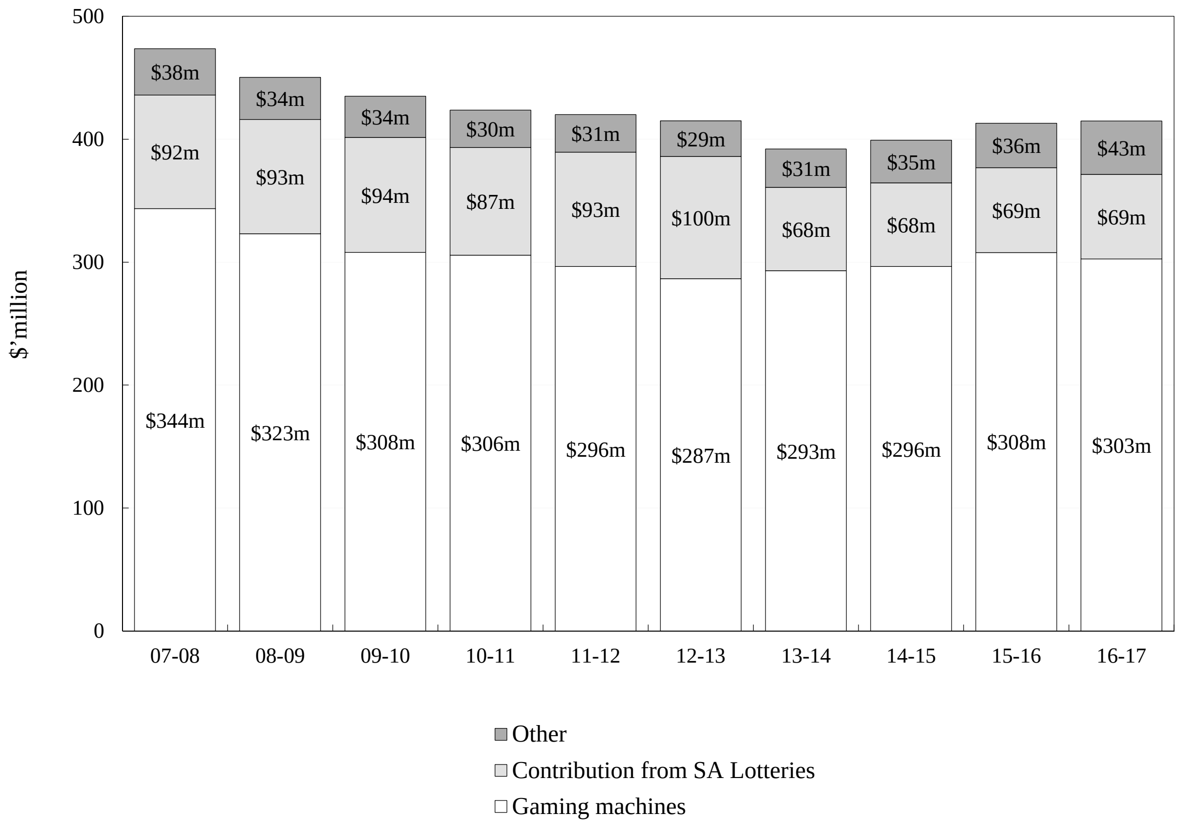


Chart 7.5 demonstrates the downward trend in total gambling revenue over the six years to 2012-13, particularly in revenue from gaming machines in hotels and clubs. Gaming machine revenue is expected to grow modestly over the forward estimates.

Tatts Lotteries SA Pty Ltd was appointed as the Master Agent of SA Lotteries in December 2012 and will manage SA Lotteries' brands and products. Prior to this arrangement the Government's distributions from SA Lotteries comprised a tax on net gambling revenue and a dividend. Both contributions were classified as gambling tax revenue in accordance with ABS conventions. Tatts Lotteries SA Pty Ltd appointment as Master Agent will mean that the Government will no longer receive a dividend from SA Lotteries, which is the main reason for the reduction in contributions from SA Lotteries from 2013-14.

7.4 Sales of goods and services

Revenue from sales of goods and services represented 13% of estimated total revenues in 2012-13. Sales of goods and services by the general government sector include government fees and charges most of which will have increased by 3% from 1 July 2013 reflecting the annual indexation of fees.

Revenue from sales of goods and services are expected to be $2323 million (nominal) in 2016-17, a real increase of $59 million compared to 2012-13.

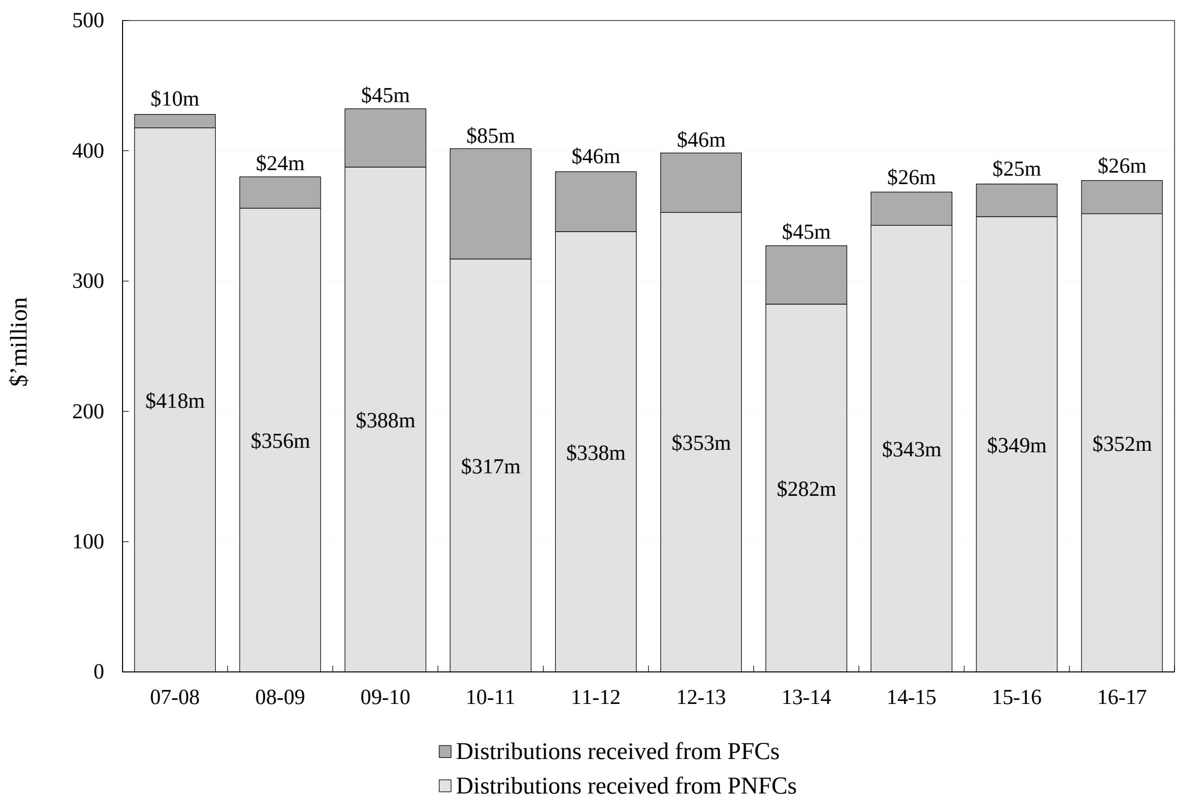
7.5 Dividend and income tax equivalent income

Dividend and income tax equivalent income are the distributions received from PNFCs and PFCs. They include returns of accumulated capital.

As the distributions come from two other GFS sectors, on a consolidated financial reporting basis, these distributions are internal transfers and have no effect on the whole-of-government consolidated operating result. On the GFS sector basis, transfers are recorded as revenue in the general government sector.

Chart 7.6 shows the trend in distributions received from PNFCs and PFCs for the 10 years to 2016-17.

Chart 7.6 – Distributions received by the general government sector (nominal)



Total distributions for 2012-13 are estimated at $399 million, $50 million higher than expected due to improved distributions from ForestrySA, SA Water and SAFA offset by reduced estimates from Renewal SA.

Distributions from SA Water represent the single largest component of this revenue source, comprising 79% of estimated total distributions for 2012-13.

Distributions from ForestrySA are estimated to be $28.5 million above budget in 2012-13 due to the once-off distribution associated with the completion of the forward sale of the Green Triangle forest plantations. From 2013-14 distributions from ForestrySA are expected to cease, reflecting ForestrySA's new role as operational manager of the Green Triangle plantations.

7.6 Other revenue

Other revenue mainly comprises royalties, fines and penalties and schools fundraising revenue. Other revenue is expected to be $696 million (nominal) in 2016-17, a real decrease of 26% compared to 2012-13. This decrease reflects the once-off relief of $320 million in South Australia's public housing debt by the Commonwealth in 2012-13. This gain is offset by a recognised expense for the general government sector associated with the subsequent relief of the South Australian Housing Trust's obligations to the Treasurer.

7.7 Risks to revenue

The Budget Papers provide detailed explanations of various risks to the amount and the flexibility of the revenue budget. Included in the risk analysis is:

- ***Taxation*** **–** a variance of 1% in taxation revenue, not including GST revenues, equates to about $42 million p.a. The Budget Papers provide a more detailed analysis, but highlight that price and activity trends in the property market have a greater impact on the short-term volatility of state taxation revenues than does the broader economy. This is because of the significant share of taxation revenues derived from property based taxes.

- ***GST revenue grants*** **–** a variance of 1% in GST revenue growth has a revenue impact of $44 million p.a. Revised Commonwealth Government estimates of the GST pool in 2012-13 are 1% below the estimate of the GST pool made at the time of the Commonwealth's 2012-13 Budget.

  Commonwealth general purpose payments are the vehicle for horizontal fiscal equalisation. The methodology and data underlying the horizontal fiscal equalisation process is determined by the Commonwealth Grants Commission. Methodology changes may impact on the State, either positively or adversely. A 0.01 change in South Australia's relativity results in a change in GST revenue grants of about $36 million.

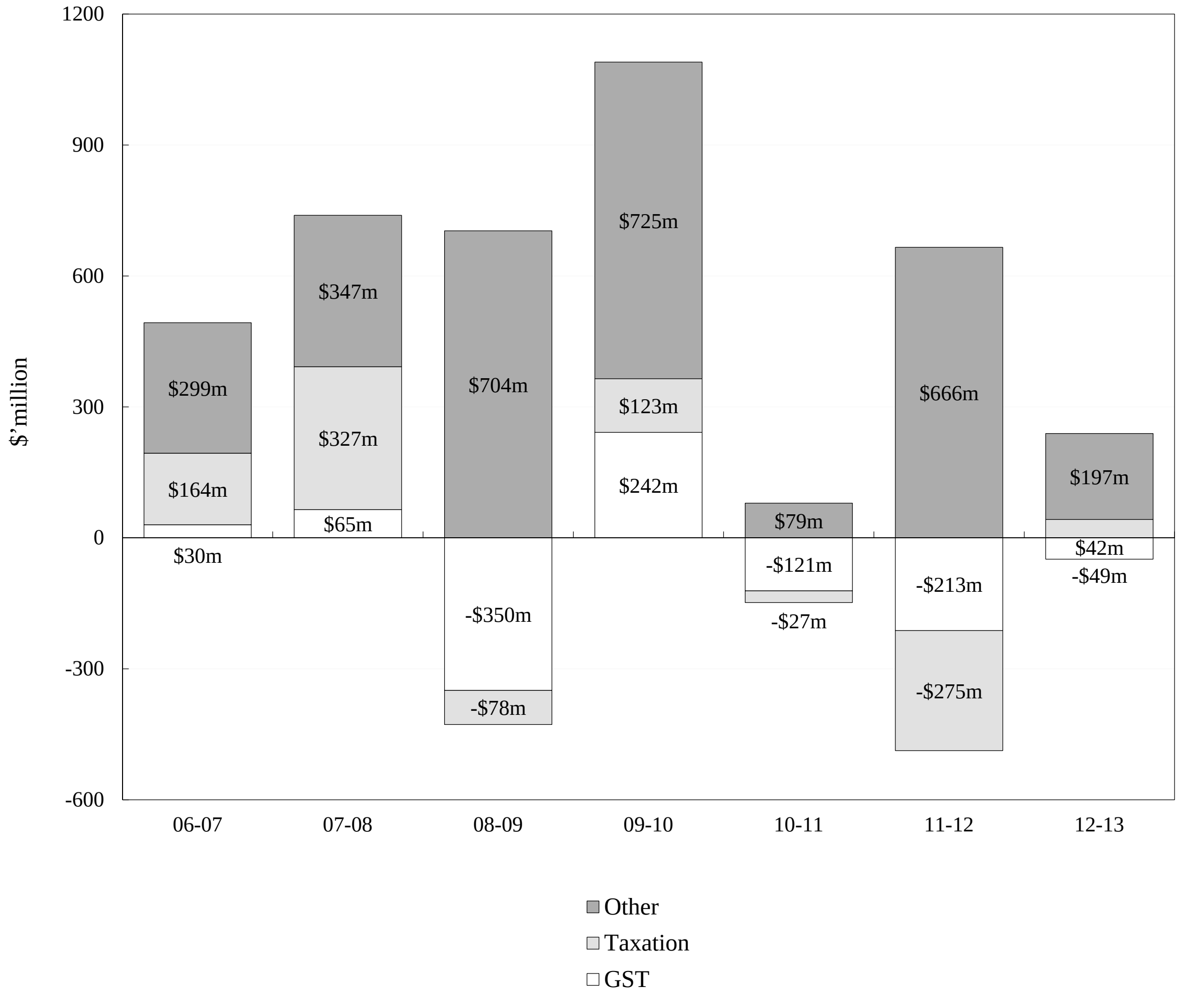
- ***Commonwealth specific purpose and National Partnership grants*** **–** payments for specific purposes and National Partnerships from the Commonwealth account for about 20% of State Government revenues. Variations in their level or the conditions applying to these payments pose a risk to the budget.

Refer 2013-14 Budget Paper 3 'Budget Statement', Chapter 6 for the full details of these risks.

7.7.1 Past revenue outcomes

Notwithstanding the risks to the revenue budget, to provide a recent historic context, the following chart shows the difference between budgeted and actual revenues for the past seven years.

Chart 7.7 – Difference between budget and actual revenues (nominal)[(a)(b)]



(a) 2009-10 is influenced by Commonwealth stimulus grants
(b) 2012-13 is the difference between budget and estimated results

The chart highlights the very large favourable variations from budget that were enjoyed up to 2007-08, prior to the unfavourable variations in GST and taxation revenue noted in 2008-09 mainly attributable to the global financial crisis. In 2009-10 a return to a favourable variation to budgeted revenue was noted.

Results for 2011-12 showed a favourable variation in other revenue (predominately Commonwealth National Partnerships grants), partially offset by decreases in GST and taxation revenue.

Estimated results for 2012-13 anticipate a decrease in GST, partially offset by an increase in taxation revenue, with a $197 million favourable variation in other revenue. The favourable variation in other revenue is due mainly from the $320 million relief from Commonwealth debt, partially offset by decreases in royalties, fines and penalties.

8 Expenses

8.1 Expenses overview

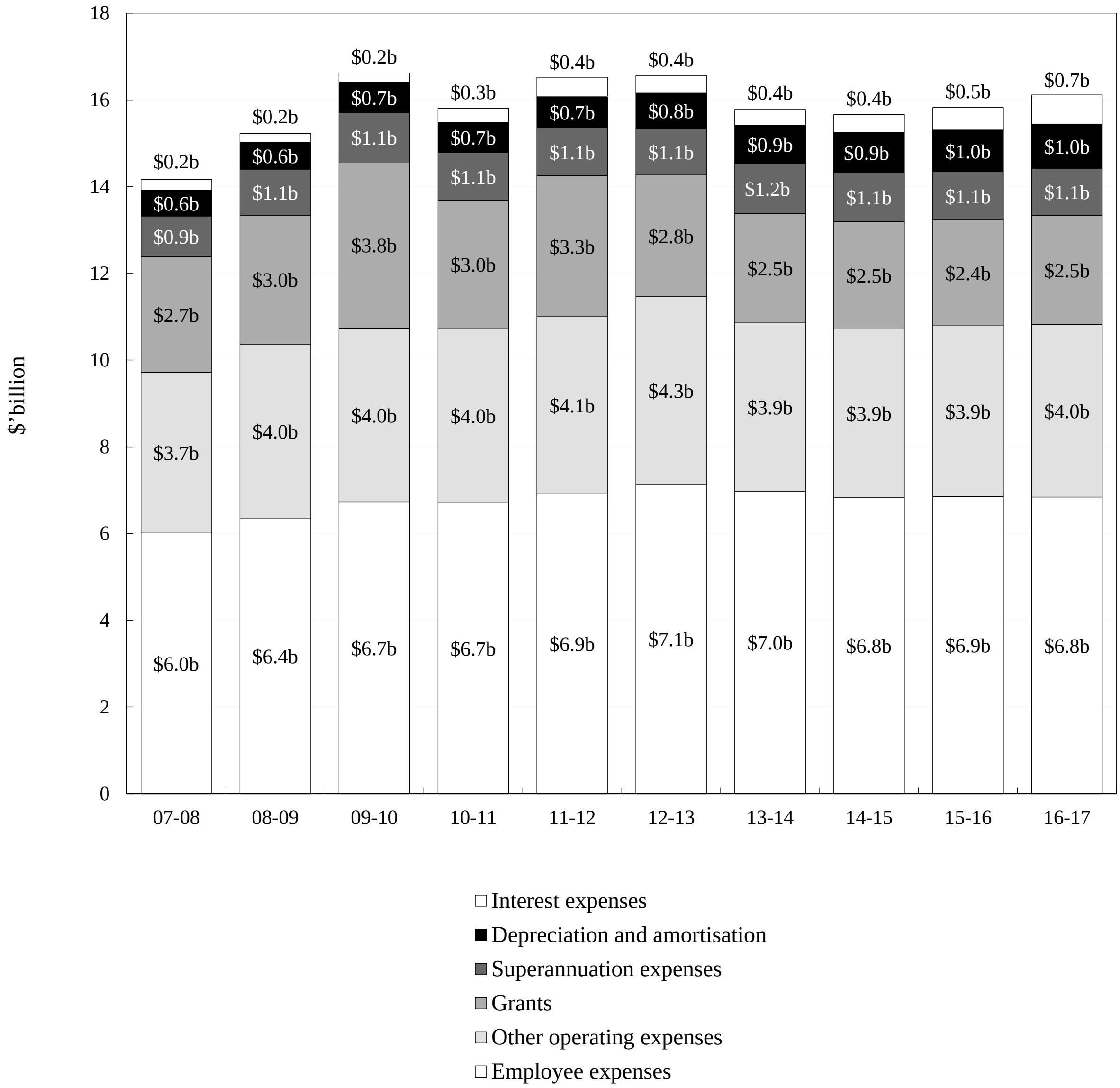
In the absence of better than budgeted revenue outcomes, the key to achieving the budget operating result targets is to control expenses. Consistent with recent past Budgets, the 2013-14 Budget expects significant restraint in spending.

For 2012-13 estimated expenses total $16.6 billion and exceed budget by $637 million or 4%.

Total expenses for 2013-14 are budgeted to be $16.2 billion, $387 million or 2.3% lower than 2012-13 and grow to $17.8 billion in 2016-17.

The following chart highlights the trends in expenses (in real terms) that have emerged since 2007-08.

Chart 8.1 – General government sector – expenses (real)



The chart shows expenses grow annually from 2007-08 to a peak of $16.6 billion (real) in 2009-10, with a marked drop in 2010-11 resulting from a drop in grant expenses. Total expenses then reach $16.6 billion (real) in 2012-13, with the 2013-14 Budget forecasting total expenses to remain steady over the period of the forward estimates.

The following discussion focuses on some of the major components that make up expenses. Detailed comments on expenditure are provided in the 2013-14 Budget Paper 3 'Budget Statement', Chapter 2.

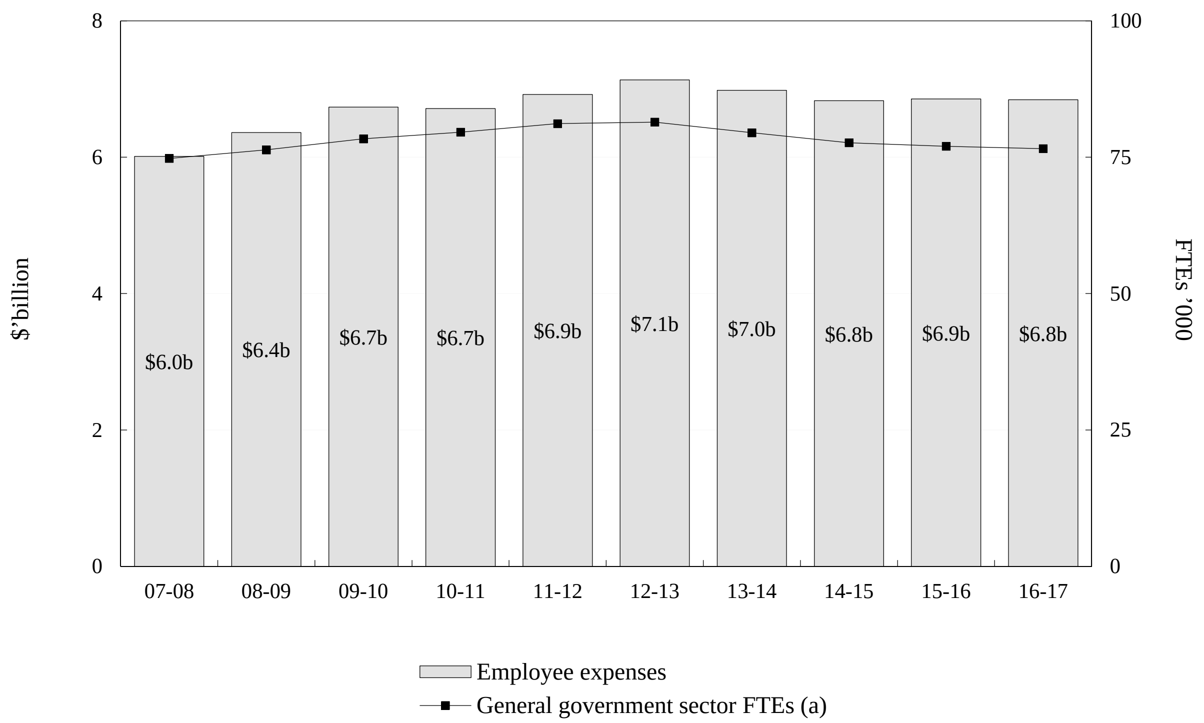
8.2 Expenses by type

8.2.1 Employee expenses

Employee expenses (an estimated $7134 million in 2012-13) represent the highest proportion (43%) of total expenses. They are estimated to increase by less than 1% in 2013-14 and then on average by 1.8% per year to 2016-17.

The following chart shows employee expenses in real terms and available FTE data from DTF estimates.

Chart 8.2 – General government sector – employee expenses (real) and FTEs



(a) DTF estimates

The chart highlights the actual growth in real terms of employee expenses through to 2012-13. This growth is consistent with FTE numbers. Employee expenses are expected to decline modestly in 2013-14 and 2014-15, remaining constant over the final two years of the forward estimates.

Real terms growth in employee expenses is generally a combination of any award increases above CPI and the increase in FTEs.

In the five years to 2012-13 employee expenses grew, in real terms, by an average of 3.5% per year. The 2013-14 Budget shows employee expenses decreasing in real terms by 2.2% for the 2013-14 year. This is partly because, for presentation purposes, the employee expenses line in the forward estimates does not include full estimates for enterprise agreements to be renegotiated or finalised in 2013-14. A proportion of the salaries and wages contingency allowance is included in other operating expenses.

The 2013-14 Budget provides for anticipated public sector wage increases over the forward estimates period, both in individual agency budgets, and in the total of the contingency items in the 'Administered Items for Department of Treasury and Finance' to cover future enterprise agreement outcomes.

A major risk to the Budget, and in particular the forward estimates, is the outcomes from enterprise agreements and control of FTE numbers.

At the time of the presentation of the 2013-14 Budget the main enterprise agreements currently under negotiation or expected to commence negotiation during the next 12 months include salaried medical officers and clinical academics, nurses and midwives, firefighters, the building metal and plumbing trades and police.

Examples of recent annual outcomes (excluding non-wage items) within agreements are:

- *SA Public Sector Wages Parity Enterprise Agreement: Salaried 2012:* annual salary increases of 3% from 1 October 2012 and 1 October 2013

- *SA Health Visiting Medical Specialists Enterprise Agreement 2012:* annual salary increases of 2.5% from 1 January 2013, 2014 and 2015, together with annual salary increases of 1% from 30 November 2013 and 2014

- *South Australian School and Preschool Education Staff Enterprise Agreement 2012:* annual salary increases of 3% from 1 October 2012, 1 October 2013 and 1 October 2014

- *TAFE SA Educational Staff Enterprise Agreement 2012:* Annual salary increases of 3% from 1 October 2012, 1 October 2013 and 1 October 2014.

The Government has indicated that future wage outcomes will be crucial in determining whether it can achieve the expenditure forward estimates in the 2013-14 Budget.

8.2.2 Other operating expenses

Other operating expenses include general purchases of goods and services.

These expenses are estimated to be $4 billion for 2013-14, a decrease of $354 million or 8% in nominal terms from 2012-13. The projection for the forward years to 2016-17 is for a real terms decline of 8%.

The Budget Papers state that under the forward estimates indexation policy, agencies are required to absorb any cost increases within their existing budget allocations unless the specific price increase has a material effect on the agency budget. The materiality test applied is that a price change experienced has altered agency costs by more than 0.5 percentage points above or below the standard indexation provided for in agency budgets.

8.2.3 Contingency provisions

Contingency amounts are incorporated into the Budget to provide flexibility if additional expenditure is required to be made by the Government. The following table shows the composition of contingency provisions for 2012-13 and 2013-14.

Table 8.1 – Contingency provisions

	2012-13 Budget $'million	2012-13 Estimated result $'million	2013-14 Budget $'million
Employee entitlements	151	358	145
Investing contingencies	87	17	18
Supplies and services	160	126	132
	397	**501**	**295**

The 2013-14 Budget includes contingency amounts totalling $295 million, $206 million less than the estimated outcome for 2012-13. Investing contingencies of $18 million for 2013-14 are budgeted at their lowest level since 2008-09.

While allocating sums to each of the categories for presentation purposes, contingency funds may also be transferred from other lines where available. The total value of budgeted contingencies for 2013-14 is consistent with figures presented in previous budgets.

8.2.4 Grants

Grants expense from the general government sector represents payments to other sectors of government and the private sector. These payments include:

- grants to non-government schools, local government and industry
- payments to the South Australian Housing Trust
- community service obligation payments to SA Water and ForestrySA.

Over the period 2008-09 to 2012-13 grants expense is influenced by the flowthrough of Commonwealth grant revenue. Table 6.6 shows the changes in grants expense over the forward estimates. Grants are estimated to be $2806 million for 2012-13, $114 million or 4% over budget predictions.

Grants are budgeted to decrease by $221 million to $2585 million in 2013-14 largely due to an estimated $79 million p.a. reduction in grants to the South Australian Housing Trust following the relief of $320 million in Commonwealth housing debt.

8.2.5 Superannuation expenses

8.2.5.1 Superannuation interest cost

In 2013-14 and across the forward estimates, superannuation interest cost is expected to be higher than estimated in the 2012-13 Budget, in the order of $110 million each year. This increase arises largely as a result in a change to the accounting standard relating to the calculation of nominal superannuation interest expense. The revised accounting standard limits the return that can be assumed from fund assets to the Commonwealth bond rate (currently assumed at 3.7%). This rate is less than the 7% assumed in the 2012-13 Budget, and results in an increase in the nominal superannuation interest expense.

The actual return on superannuation fund assets impacts on superannuation interest costs. The Budget Papers note that a 1% lower than expected return on superannuation assets invested by Funds SA would increase estimated unfunded superannuation liabilities by around $50 million. An increase in unfunded superannuation liabilities of this magnitude would increase superannuation interest cost, decreasing the net operating balance result by around $3 million p.a.

8.2.5.2 Other superannuation expenses

Other superannuation expenses are employer superannuation contributions incurred by government agencies during the reporting period and include superannuation contributions on salaries and wages. It also includes superannuation on-cost on accrued leave. Estimated other superannuation expenses were $746 million in 2012-13 and are projected to increase to $784 million in 2016-17, a real decrease of 4.8%.

8.2.6 Depreciation and amortisation

Estimated depreciation and amortisation expenses were $830 million in 2012-13 and are projected to increase by 36% to $1130 million in 2016-17. The increase reflects the growth in the value of fixed assets through purchases and revaluations. Building projects that the Government expects to complete over the forward estimates include the Flinders Medical Centre Redevelopment, Glenside Campus Redevelopment, The Queen Elizabeth Hospital Stage 2 Redevelopment and the redevelopment of the Adelaide Oval.

Amortisation of the finance lease for the new Royal Adelaide Hospital will also commence in the second half of 2015-16, with the first full year of amortisation occurring in 2016-17.

8.2.7 Interest expense

Interest expenses comprise interest paid by the Treasurer on government borrowings and interest expenses of agencies related to finance leases.

Estimated interest expense in 2012-13 was $404 million and is projected to increase by 84% to $742 million in 2016-17, reflecting a higher level of borrowings up to 2016-17. Interest payments on the financial lease for the new Royal Adelaide Hospital will start in the second half of 2015-16. The first full year interest expense associated with the new Royal Adelaide Hospital will occur in 2016-17.

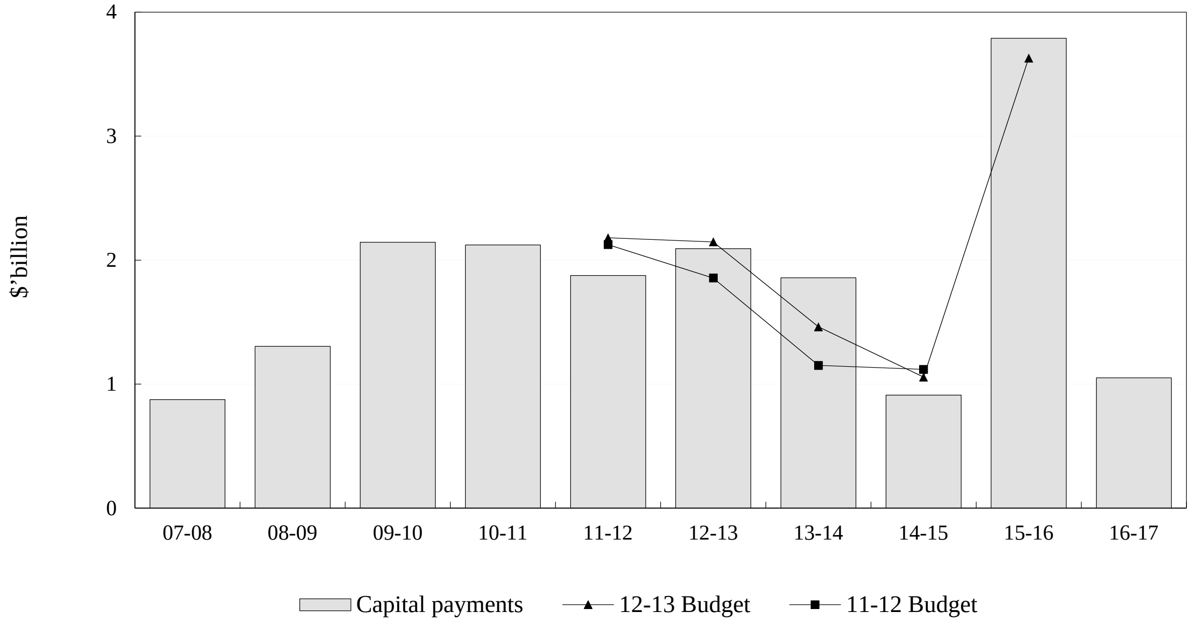
Further discussion in relation to debt movements is provided in section 9.6 of this Report.

8.2.8 Capital payments

Capital project payments are represented by the value of purchases of non-financial assets in the general government sector Operating Statement.

The following chart shows the purchase of non-financial assets over the 10 year period to 2016-17, overlayed with budgeted purchases from the 2011-12 and 2012-13 Budgets.

Chart 8.3 – General government sector purchase of non-financial assets (nominal)



In the 2009-10 Budget, the combined influence of State and Commonwealth spending initiatives, elevated general government sector capital spending estimates to high levels. Capital payments exceeded $2000 million in 2009-10 and 2010-11.

This level of capital spending is estimated again for 2012-13, before reducing through to 2014-15. The large increase in the purchase of non-financial assets in 2015-16 represents the recognition of the new Royal Adelaide Hospital.

Although there will be components of future expenditure that have effectively been committed, the forward years contain funds contingent on approvals. The investing contingency provision for 2013-14 is $18.4 million.

Major projects carry high inherent risks including cost estimating, escalations and timeliness of completion. Sustained higher capital outlays than have been made in past years, need support from appropriate project management expertise, information systems and controls.

As in past years, carryover adjustments are made where appropriate if delays occur in budgeted project expenditure in the year but which will now be incurred in later years. The 2013-14 Budget included investing carryovers from prior years into 2013-14 and future years of $74 million.

The 2012-13 Budget outlined investing project suspensions and deferrals totalling $444.2 million[11] across the forward estimates period. A summary of investing suspensions and deferrals for each agency was provided in table 2.5 of Budget Paper 3 ‘Budget Statement’ for that year. The more financially significant projects affected were Rail Network Electrification Upgrades, the Queen Elizabeth Hospital Redevelopment (Stage 3A) and the Modbury Hospital Redevelopment. Estimates for these large projects remain in the forward estimates of the 2013-14 Budget.

[11] 2012-13 Budget Paper 3 ‘Budget Statement’, page 28.

8.2.9 *Public Private Partnerships*

The major PPP in progress is the new Royal Adelaide Hospital project.

In June 2011 the Government announced financial close on a contract with SAHP to build, operate and maintain the new Royal Adelaide Hospital under a PPP arrangement. The Government agreed on a fixed price for the design, construction, risk management and running and maintenance costs of the new hospital.

The total capital cost of the new hospital at contractual close was $2.09 billion comprising SAHP's contracted design and construction cost of $1.85 billion and $244.7 million for state works including clinical equipment.

The new Royal Adelaide Hospital is included as an asset and a finance lease liability of $2.8 billion in the 2015-16 forward estimate year. This accounts for the large increase in net debt in 2015-16. The amount represents the net present value of design and construction costs, lifecycle payments, interest and other project costs.

Annual service payments are also budgeted to commence in 2015-16, with $126.9 million included for that year. This amount only represents a part year payment based on the expected opening date of the new Royal Adelaide Hospital. DTF has advised that, in a full year, the total annual payment is estimated to be $395.3 million.

Only part of this annual payment amount will be expensed each year as it includes cash payments that are applied to the reduction in the lease liability, which DTF has advised in a full year will be $111.7 million. The remainder of the payment is reflected as an expense, including finance charges on the lease and operating expenditure.

DTF also advised that an annual expense of $73 million is expected relating to the amortisation of the asset on the balance sheet.

The liability for the new hospital is in addition to the estimate in the 2013-14 Budget of $222.9 million of state investing expenditure (inclusive of road works managed by the Department of Planning, Transport and Infrastructure) on key clinical equipment, state project management and other site works.

8.2.9.1 Financial reporting of Public Private Partnership projects

Depending on the terms of contracts, PPPs may, through their contractual arrangements and assignment of risks and benefits under current accounting standards, be classified as, or have elements of, either:

- a finance lease that transfers substantially all the risks and rewards incidental to ownership of an asset
- an operating lease that does not transfer substantially all the risks and rewards incidental to ownership and is excluded from the State Balance Sheet (may be off-Balance Sheet). In this case lease payments are recognised as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

Under AASs whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:

- the lease transfers ownership of the asset to the lessee by the end of the lease term
- the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised
- the lease term is for the major part of the economic life of the asset even if title is not transferred
- at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset
- the leased assets are of such a specialised nature that only the lessee can use them without major modifications.

As mentioned previously, the capital component of the PPP arrangement for the new Royal Adelaide Hospital is to be recognised as a finance lease in the Balance Sheet, and consequently have an impact on net debt and net financial liabilities. As the State is the lessee, at the commencement of the lease term, lessees recognise finance leases as assets and liabilities in the Statement of Financial Position at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. Any initial direct costs of the lessee are added to the amount recognised as an asset. Subsequently, minimum lease payments are apportioned between a finance charge and reducing the outstanding liability.

8.2.10 Asset sales

Sales of non-financial assets are taken into account in calculating the annual net lending result. They are netted from purchases of non-financial assets when determining total net acquisition of non-financial assets.

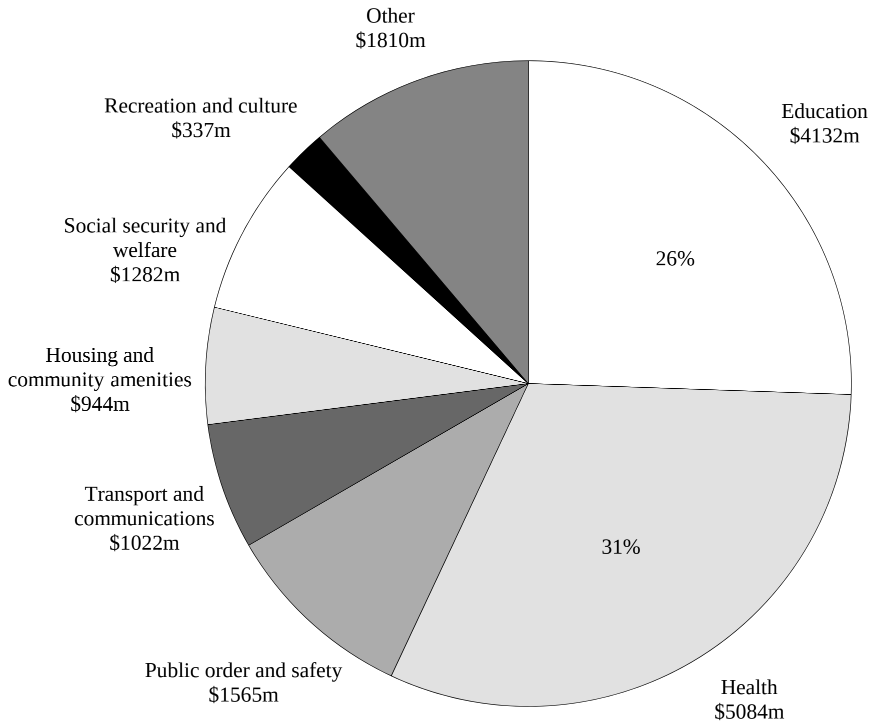
The sale of non-financial assets is estimated to total $1200 million for 2012-13. This amount is largely attributable to the proceeds from the forward sale of the State’s Green Triangle forest plantations ($635.1 million), and proceeds from the appointment of Tatts Lotteries SA Pty Ltd as exclusive Master Agent to operate SA Lotteries’ brands and products for a term of 40 years ($402.8 million). These amounts are exclusive of stamp duty.

For the 2013-14 Budget sales of non-financial assets are forecast to total a further $741 million. Of this amount, $670 million is anticipated over the first two years of the 2013-14 Budget.

8.3 Expenses by function

The GFS reporting framework also provides information on expenditure (excluding capital payments) by function for the general government sector. The following charts the 2013-14 Budget expenses and demonstrates the extent to which the health and education sectors dominate the overall expenditure by the State.

Chart 8.4 – General government sector expenses by function[12]



8.4 Risks to expenses

8.4.1 Overview

As with revenue, the 2013-14 Budget provides detailed consideration of various risks to the expenditure budget and acknowledges the management task for achieving budgeted outcomes.[13]

Some of the key risks reported are:

- ***Wages and salaries*** – an increase of 1% p.a. above the amounts factored into the Budget would have an adverse impact of approximately $240 million in 2016-17.
- ***Interest rates*** – a 1% increase in the average interest rate applying to general government sector net debt would increase net interest expense by about $67 million in 2013-14 rising to $76 million in 2016-17.
- ***Capital investment pressures*** – a number of departments have large capital investment programs over the forward estimates period. Large capital programs increase the risk of cost escalation compared with original projections.

  If cost escalations exceed the amounts included in the capital investment program, annual net lending outcomes will be impacted. A 1% increase in costs for the capital program in the general government sector will increase expenditure by approximately $19 million in 2013-14.

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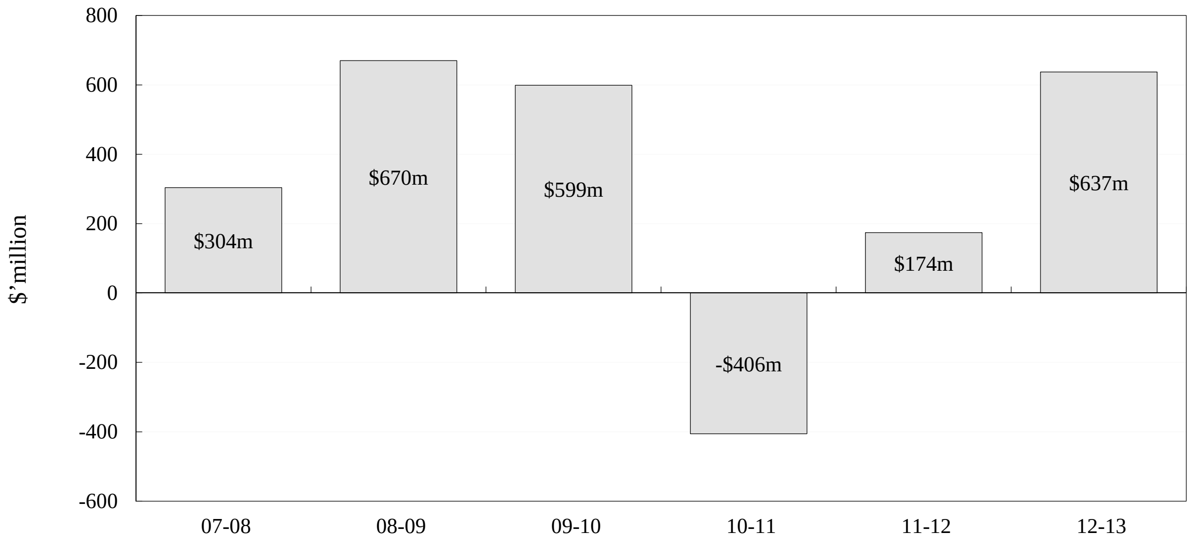
12 2013-14 Budget Paper 3 'Budget Statement', table 2.22
13 2013-14 Budget Paper 3 'Budget Statement', page 111

- ***Hospital expenditure growth*** – Hospital expenditure has consistently exceeded budget in recent years. While the Government is implementing a number of strategies to manage this expenditure growth, a 1% growth in excess of the amounts included in the 2013-14 Budget will increase expenditure by $51 million p.a.

To provide a recent historical context, the following chart shows actual outcomes against estimates for expenses for the past six years.

Chart 8.5 – Difference between budget and actual expenses[(a)(b)]



(a) 2012-13 is the difference between budget and the estimated result
(b) 2008-09 and 2009-10 are influenced by Commonwealth stimulus grants

Expenses exceeded budget in 2008-09 and 2009-10 due mainly to additional Commonwealth economic stimulus grants provided in response to the global financial crisis.

For 2010-11 total expenses are $406 million less than budgeted, largely arising from decreases in grant and other operating expenses.

Total expenditure for 2012-13 is estimated to exceed budget by $637 million. This variance from budget is due largely to increases in employee expenses and other operating expenses.

8.4.2 Savings and revenue offsets

For a number of years large value savings targets have featured as an essential element of fiscal strategy. A range of savings initiatives announced since the 2008-09 Budget were consolidated in the 2010-11 Budget after the Government had considered budget improvement measures recommended by the then Sustainable Budget Commission.

8.4.3 Savings strategy 2010-11

The 2010-11 Budget consolidated savings announced in earlier Budgets (of over $700 million p.a. by 2013-14) into new savings which totalled $1.5 billion over a four year period arising from the recommendations of the Sustainable Budget Commission. These were additional to cost recovery and revenue measures ($478.6 million) and some retained savings included in agencies from previous Budgets.

The following table sets out the total savings incorporated in the 2010-11 Budget. Revenue measures are excluded.

Table 8.2 – Summary of 2010-11 Budget new and existing operating savings

	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million	4 year total $'million
New budget improvement savings					
Expenditure savings	99.0	254.1	389.8	474.6	1 217.5
Across government initiatives	25.8	73.1	101.4	108.1	308.5
Total new budget improvement savings	124.8	327.2	491.2	582.7	1 525.9
Existing saving measures and interest savings:					
FTE savings (2008-09 MYBR)	28.0	45.0	56.0	59.0	188.6
Indexation (2009-10 Budget)	27.0	47.0	46.0	47.0	166.2
Efficiency dividend (2006-07 Budget)	-	11.0	27.0	44.0	82.5
Interest savings	-	7.0	35.0	80.0	122.0
Total existing saving measures and interest savings	56.1	110.0	163.3	230.0	559.3
Total new and existing savings	180.9	437.2	654.5	812.7	2 085.2

Note: Totals may not add due to rounding

Since the 2010-11 Budget the Government has announced changes to these savings measures. The following table, based on information provided by DTF, sets out the total adjustments made to the savings measures announced in the 2010-11 Budget.

Table 8.3 – Summary of adjustments to 2010-11 Budget operating savings measures

2010-11 Savings measures	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million
2010-11 MYBR				
Parks Community Centre (improving service delivery)	-1.3	-1.9	-4.2	-4.8
Procurement governance - reform	-	-1.4	-1.4	-1.4
2011-12 Budget				
Disability Client Trust Management	-	-0.7	-	-
Court awarded costs against police - introduce cap	-	-1.6	-	-
Public sector employee recreation leave loading - reversal of 2010-11 Budget saving	-	-	-22.0	-22.2
2011-12 MYBR				
Family and Community Development Program - grant prioritisation	-	-	-1.0	-2.0
2012-13 Budget				
Facilities management - efficiencies	-	-	-2.4	-
Disability Client Trust Management	-	-	-1.0	-1.1
2012-13 Mid Year Budget Review				
Facilities management - efficiencies	-	-	-3.2	-
Court awarded costs against police - introduce cap	-	-	-	-1.6
Total adjustments	-1.3	-5.8	-35.1	-33.1

Note: Totals may not add due to rounding

Health savings measures not achieved or deferred are not included in Table 8.3 as DTF has advised that they may include savings measures announced before or after the 2010-11 Budget. Notwithstanding, the 2012-13 MYBR reprofiled Health's total savings requirement, including 2010-11 savings measures. DTF advised that the 2012-13 MYBR savings adjustment addressed Health's total savings requirement and identified a quantum of savings, rather than a list of measures, that was considered achievable in the context of Health's budget pressures.

The 2012-13 MYBR reduced Health's savings measures by $122.9 million for 2012-13 and by $128.3 million for 2013-14. Further, DTF advised that Health savings not achieved for 2010-11 were $24.3 million and not achieved in 2011-12 were $54.5 million.

The following table identifies the 2010-11 savings measures remaining as at the time of the 2013-14 Budget, summarised at the agency level. The table excludes Health and Ageing savings because of the reprofiling of their total savings measures. Section 8.4.8.1 of this Chapter provides a more detailed analysis of the Department for Health and Ageing's savings task.

Table 8.4 – Summary of adjusted 2010-11 Budget savings measures

Agency	Revised 2010-11 $'million	Revised 2011-12 $'million	Revised 2012-13 $'million	Revised 2013-14 $'million
Attorney-General	1.7	10.0	18.4	20.6
Communities and Social Inclusion	1.6	10.1	18.6	18.9
Correctional Services	1.1	1.6	2.0	2.0
Courts Administration Authority	—	0.3	0.6	0.6
Defence SA	0.6	0.7	1.6	1.5
Education and Child Development	8.9	28.9	49.9	60.4
Emergency Services	1.1	3.1	4.4	5.2
Environment, Water and Natural Resources	8.2	14.5	25.6	32.6
Environment Protection Authority	0.1	0.4	0.8	1.1
Further Education, Employment, Science and Technology	11.6	21.9	30.0	38.0
Manufacturing, Innovation, Trade, Resources and Energy	13.2	22.9	28.4	33.4
Planning, Transport and Infrastructure	7.1	31.7	32.5	44.3
Premier and Cabinet	1.8	5.6	12.1	20.2
Primary Industries and Regions	14.3	18.7	22.9	26.2
South Australia Police	0.8	2.4	4.5	3.0
State Emergency Service	0.3	0.3	0.6	0.6
Tourism	1.1	3.0	4.0	4.6
Treasury and Finance	31.3	53.5	62.4	68.0
Whole-of-government	0.2	28.7	30.9	33.4
Zero Waste	0.4	0.5	0.4	0.4
Total savings measures announced in the 2010-11 Budget remaining in the 2013-14 Budget	105.3	258.6	350.4	415.0

Note: Totals may not add due to rounding

The 2013-14 Budget notes that, with the exception of Health and Ageing, agency savings budgeted to commence prior to or in 2012-13 and across the forward estimates are substantially on track.

8.4.4 Savings identified since the 2010-11 Budget

Since the 2010-11 Budget subsequent budgets have introduced additional significant savings initiatives, including the following:

- The 2012-13 Budget introduced new savings initiatives totalling $430.7 million over the four years of the forward estimates. The two main measures were an increase in the efficiency dividend from 0.25% to 1% of employee expenses and the reduction of a further 1000 FTE staff over the forward estimates.
- The 2012-13 MYBR introduced $227.2 million of savings initiatives through introduction of an additional efficiency dividend of 1% p.a. reduction in the net cost of services and a reduction in costs in specifically identified portfolio areas.
- The 2013-14 Budget introduced savings measures of $140 million through the extension of the 1% p.a. efficiency dividend to 2016-17, the bringing forward of 2015-16 savings measures and reducing the maximum TVSP payout.

Table 6.1 of 2013-14 Budget Paper 3 ‘Budget Statement’ (page 113) provides details of the delivery of savings and revenue measures since the 2008-09 MYBR.

8.4.5 Nature of savings initiatives

As previous Reports have highlighted, an inherent risk of the saving strategy of government is its sheer size and breadth. Achieving the task requires significant discipline and, as noted earlier, Health and Ageing has experienced difficulties meeting savings targets. Further, the introduction of additional savings targets subsequent to the 2010-11 Budget presents ongoing risks including industrial action, public demand to maintain services and ineffective and inefficient administrative performance.

It is also noted that the efficiency dividend increase in recent budgets is a broad savings measure that does not identify specific areas of government activity where savings are expected to be realised. The increase in the efficiency dividend and the broad nature of this savings initiative adds an additional element of flexibility and hence budget management oversight complexity to the overall savings task.

8.4.6 Reduction of full-time equivalents

A key part of the 2010-11 savings strategy involved further reduction in public sector FTEs by 3743 FTEs, excluding increases from other initiatives. The 2012-13 Budget introduced a savings initiative to reduce a further 1000 FTE staff over the forward estimates, starting in 2013-14 with savings of $25 million and increasing to $86.6 million in 2015-16. The 2013-14 Budget brought forward the 2015-16 FTE reductions into the 2014-15 year.

Table 8.5 summarises DTF’s advice on all general government budgeted FTE reductions associated with specific savings measures since the 2008-09 Budget.

Table 8.5 - Full-time equivalent employees as at 30 June

	2010	2011	2012	2013	2014	2015	2016	2017	Total
2008-09 MYBR	1 200	200	200	-	-	-	-	-	1 600
2010-11 Budget	-	608	954	742	369	-	-	-	2 673
2011-12 Budget	-	-	26	200	202	2	-	-	430
2011-12 MYBR	-	-	18	16	3	-	-	-	37
2012-13 Budget	-	-	-	7	309	350	350	-	1 016
2012-13 MYBR	-	-	-	-	202	65	393	-	660
2013-14 Budget[(a)]	-	-	-	-	-	-	-	-	-
Originally budgeted FTE reduction	1 200	808	1 198	965	1 084	417	743	-	6 416

(a) No new specific FTE savings measures are included in the 2013-14 Budget

Savings measures to reduce FTE levels are offset by expenditure initiatives that increase FTE numbers. The 2013-14 Budget outlines that FTEs in the general government sector are estimated to decrease by 4882 between 30 June 2013 and 30 June 2017[14].

DTF has advised that this reduction of 4882 FTEs is the net effect of all budget adjustments that have been processed for each year. This includes new expenditure and revenue measures (including efficiency dividends) introduced in recent budgets and MYBRs, as well as parameter and other variations.

The following table reflects information provided by agencies and compares the approved FTE cap to the actual level of FTEs (as at the last pay period in June) for key general government sector agencies (excluding a number of small agencies). The FTE caps reflect agency profiling of the cap as at the end of June 2013.

Table 8.6 – Actual and cap FTEs by portfolio as at 30 June 2013

Agency	Actual FTEs	Approved CAP FTEs	Variance FTEs	Variance %
Attorney-General	1 094	1 148	(54)	(4.7)
Communities and Social Inclusion	3 647	3 659	(12)	(0.3)
Correctional Services	1 645	1 686	(41)	(2.4)
Courts	717	721	(4)	(0.6)
Defence SA	28	30	(2)	(7.9)
Education and Child Development	22 929	22 954	(25)	(0.1)
Electoral Commission of SA	19	22	(3)	(14.2)
Emergency Services	1 189	1 182	8	0.7
Environment Protection Authority	211	216	(5)	(2.3)
Environment, Water and Natural Resources	1 687	1 790	(104)	(5.8)
Further Education, Employment, Science and Technology	3 251	3 255	(5)	(0.1)
Health and Ageing	30 625	30 330	296	1.0
Manufacturing, Innovation, Trade, Resources and Energy	470	446	24	5.5
Planning, Transport and Infrastructure	3 446	3 606	(160)	(4.4)
Premier and Cabinet	2 021	2 057	(36)	(1.8)

[14] 2013-14 Budget Paper 3 'Budget Statement', page 30

Table 8.6 – Actual and cap FTEs by portfolio as at 30 June 2013 (continued)

Agency	Actual FTEs	Approved CAP FTEs	Variance FTEs	Variance %
Primary Industries and Regions	867	961	(93)	(9.7)
South Australia Police	5 592	5 764	(172)	(3.0)
Tourism	109	127	(17)	(13.6)
Treasury and Finance	500	532	(32)	(6.0)
Total	80 047	80 485	(437)	(0.5)

Note: Actual and approved FTE cap figures provided by DTF. Positive variances indicate over FTE cap.
Totals may not add due to rounding

The 2013-14 estimate of FTEs for the general government sector as at 30 June 2013 was 81 436[15]. FTE monitoring is limited to key agencies representing the majority of the general government sector.

Explanations, provided by agencies, for the key variances as at the end of June are as follows.

Portfolios above the cap:

- Health and Ageing (296 FTEs) – primarily due to difficulties in specifying the FTE cap for the Health Regions, which are currently showing underspending on employee expenses but an over-cap result of 323 FTE

- Manufacturing, Innovation, Trade, Resources and Energy (24 FTEs) – advised that its FTE cap required correction following recent machinery of government changes

- Emergency Services (8 FTEs) – largely a result of staff employed under grant funded arrangements and timing of employee separations, partially offset by vacancies across the emergency services entities.

The majority of agencies with large variances below the FTE cap reported that they were the result of vacancies, with Primary Industries and Regions reporting that it was 93 FTEs below the cap due mainly to delays in establishing and finalising contracts with external parties, continued uncertainty of funding from research and development corporations and early achievement of future savings requirements.

8.4.7 Targeted voluntary separation program

To assist agencies to achieve the 2010-11 savings target, the Government introduced an enhanced redeployment process to match excess employees with suitable vacant roles. The Government considered that successful redeployment of excess employees into funded vacancies would significantly reduce the potential cost of reducing the workforce.

The Government also approved further targeted voluntary separation program arrangements. A key condition is that TVSP offers are only to be made to employees who were declared excess to requirements because their positions have been or are to be abolished. TVSPs became available from November 2010.

[15] 2013-14 Budget Paper 3 'Budget Statement', page 30.

DTF advised that TVSPs are currently planned to continue to be available over the forward estimates.

Audit sought from DTF a summary of TVSPs since November 2010, as it is responsible for coordinating aspects of the program. Table 8.7 sets out a summary of FTE reductions achieved through TVSP payments (excluding executive reductions) as reported to DTF during the period 1 November 2010 to 30 June 2013.

Table 8.7 – FTE reductions from TVSPs reported by agencies 1 November 2010 to 30 June 2013

	FTE reductions from TVSPs
Arts SA	2.0
Attorney-General's	64.1
Communities and Social Inclusion[(2)]	62.8
Correctional Services	9.0
Defence SA	1.0
Education and Child Development[(3)]	194.3
Environment, Water and Natural Resources[(4)]	146.7
Environment Protection Authority	7.2
Further Education, Employment, Science and Technology	173.7
Health and Ageing	442.7
Manufacturing, Innovation, Trade, Resources and Energy[(5)]	50.0
Premier and Cabinet	48.0
Primary Industries and Regions[(6)]	100.8
Planning, Transport and Infrastructure[(7)]	103.6
SAFECOM	15.0
South Australia Police	4.0
SA Ambulance Service Inc	10.0
South Australian Metropolitan Fire Service	3.0
South Australian Tourism Commission	18.6
Treasury and Finance	38.7
ForestrySA (non-general government sector)	4.0
Lotteries Commission of South Australia	3.0
Total	1 502.1

Note:
(1) Totals may not add due to rounding
(2) Formerly Families and Communities
(3) Formerly Education and Children's Services
(4) Formerly Environment and Natural Resources and incorporating Water
(5) Formerly Trade and Economic Development
(6) Formerly Primary Industries and Resources
(7) Formerly Transport, Energy and Infrastructure incorporating Planning and Local Government

Agencies are centrally reimbursed for TVSP payments made to achieve savings measures announced in the 2010-11 Budget and subsequent budget initiatives.

The 2010-11 Budget provided for $353.8 million over four years for the cost of TVSP payments in support of employee separations. This cost was based on the provision of 3000 TVSPs over the four year period[16]. The 2012-13 Budget[17] states that an additional

16 2010-11 Budget Paper 6 'Budget Statement', page 13.
17 2012-13 Budget Paper 3 'Budget Statement', page 27.

$60.4 million has been provided over three years for targeted TVSP payments associated with the savings measure in that budget to reduce an additional 1000 FTEs. While the TVSP arrangements continue through 2013-14, from 1 July 2014 the maximum TVSP payout will be reduced to 52 weeks pay (calculated as 10 weeks base plus two weeks per year of service).

The 2013-14 Budget states that FTE reductions can also be achieved in other ways (for example, natural attrition) and that the Government will honour its pledge of a 'no forced redundancy' policy for the remainder of the current electoral term. After 30 June 2014, a public sector employee who has been identified by their agency as having been excess for longer than 12 months (and during that time has been assisted to find alternative public sector employment) would be able to be separated with an appropriate financial package having regard to the *Public Sector Act 2009* or other applicable legislation, and applicable industrial provisions.

At 30 June 2013 DPC advised there were 177 excess employees on the redeployment list.

8.4.8 Budget monitoring and reporting

Monitoring progress against Budget targets to enable a timely response to any significant issues arising is a vital element in managing budget risk.

The critical importance of strong monitoring of budget progress has been continually emphasised in previous Reports. DTF has advised Audit of specific measures in place. They include monthly monitoring of financial performance and quarterly monitoring of capital projects, budget initiatives and FTEs. Further, monitoring reports continue to be provided to the SBCC based on information supplied by agencies and analysis prepared by DTF.

DTF advised that the major risks to the fiscal outlook are set out in Chapter 6 of the 2013-14 Budget Paper 3 'Budget Statement'. These include the impact of economic activity on household spending patterns and demand for housing, which impact on GST and property taxation; expenditure risks such as higher than expected wage increases, cost escalations on capital projects and activity growth in hospitals and schools; and changes in Commonwealth policy.

Given the magnitude of the Budget improvement measures introduced in the 2010-11 Budget and the importance to the fiscal outlook of the achievement of these measures, DTF introduced an enhanced monitoring process in 2010-11 to monitor agency progress in achieving the measures and FTE reductions. This monitoring regime continues in 2013-14. Processes concluded or introduced since 2010-11 include the following:

- Early 2011 – monitoring focus was on agency progress in delivering 2010-11 savings and was discussed at the 2011-12 Budget bilateral meetings between the Treasurer and Ministers.

- July/August 2011 – monitoring considered agency progress in delivering savings measures commencing in 2011-12 and plans for delivering measures commencing in 2012-13 and beyond. The Treasurer met with Chief Executives to discuss progress on savings implementation and presented an enhanced monitoring report to the SBCC.

- Early 2012 – focused on progress against 2011-12 savings targets and identifying issues in achievement of future savings measures. This information was discussed in 2012-13 Budget bilateral meetings between the Treasurer and Ministers.

- July 2012 – focused on verifying achievement of measures budgeted to be implemented in 2011-12, confirming that measures beginning in 2012-13 are on track and ensuring the development of plans to deliver measures beginning in 2013-14 and beyond. The Minister for Finance met with Chief Executives to work through plans and consider agency progress in achieving savings and will present a report to SBCC.

- In 2012-13 the Minister for Finance was delegated responsibility by SBCC for monitoring the implementation and delivery of savings by agencies. Regular monitoring of savings measures was incorporated into quarterly processes and a savings section added to quarterly monitoring reports to SBCC.

- Existing regime continues in 2013-14 with monthly monitoring of financial performance and quarterly monitoring of capital projects, savings measures and FTEs. Monitoring reports will continue to be provided to SBCC.

8.4.8.1 Department for Health and Ageing savings task

Last year DTF advised that, at the time of the 2012-13 Budget, the Department for Health and Ageing (the Department) was projected to overspend its 2011-12 Budget by $122 million. Funding was provided to offset projected overspends (in prison health, mental health and the post-acute care program) and unachieved revenue and savings targets.

The 2012-13 Budget included new operating initiatives totalling $167 million in 2012-13 and 2013-14 which included a reprofile of the Department's budget savings task. This aimed to provide the Department with additional resources for a more even annual build-up of savings to achieve its aggregate savings target by 2014-15. The 2011-12 overspend of $122 million and the $167 million in operating initiatives in the 2012-13 Budget have been factored into the Department's savings targets as reprofiled in subsequent years. The Department's savings requirement to meet its budget was $169 million in 2012-13 increasing to $503.8 million by 2015-16.

In the past, the Department has not been able to achieve savings targets or has experienced other service demands that have necessitated additional funding. Given that savings measures required of agencies will continue together with requirements to further reduce expenditure, the Department implemented the following strategies:

- Following Cabinet approval in November 2011, the Office for Business Review and Implementation (OBRI) was established within the Department to support the delivery of improved financial management and savings measures. Further commentary on the activities of OBRI is provided below.

- In 2012 the Department commissioned the hospital budget performance and remediation reviews of the three main Local Health Networks.

In July 2012 and October 2012 the Government approved the implementation of specific efficiency strategies identified in the hospital budget performance and remediation reviews and additional measures required to meet forward budget estimates. On both occasions the Government was advised the savings measures proposed were still insufficient for the Department to meet the Government's budget targets by 2015-16.

The Government re-assessed the level and timing of the budget improvement measures it considered the Department could deliver across the forward estimates. This resulted in a reduction, totalling $523.2 million, to the Department's budget savings target over the forward estimates in the 2012-13 MYBR.

The following table provides the revised savings measures since the 2012-13 Budget and a breakdown of the Department's savings initiatives.

Table 8.8 - Summary of revised savings measures and initiatives

	2012-13 $'million	2013-14 $'million	2014-15 $'million	2015-16 $'million
Revised savings target[1]				
Aggregate budget improvement required	-169.0	-351.3	-448.4	-503.8
2012-13 MYBR reduction in savings measures	122.9	128.3	148.7	123.3
2012-13 Post MYBR revised savings measures	-46.1	-223.0	-299.7	-380.5
2013-14 Budget savings measures	-	16.1	-5	-5.1
2013-14 Budget revised savings measures	**-46.1**	**-206.9**	**-304.7**	**-385.6**
Savings initiatives[2]				
Hospital budget performance and remediation reviews	21.8	58.7	70.1	70.4
Existing savings	16	87	106.7	107.1
New savings to be implemented	4.3	15.4	17.4	20.3
Potential savings requiring further analysis	4	45.8	110.5	187.8
	46.1	206.9	304.7	385.6

(1) Revised savings target figures provided by DTF.
(2) Savings initiatives figures provided by the Department for Health and Ageing.

There is a significant growth in savings targets of $160.8 million in 2013-14, $97.8 million in 2014-15 and $80.9 million in 2015-16. This will present an enormous challenge for the Department to deliver the future savings measures. Table 8.8 demonstrates that a major component of the savings initiatives is potential savings requiring further analysis and refinement. A number of these savings initiatives will be subject to separate Cabinet approval.

Office for Business Review and Implementation

OBRI was operational from February 2012 to support the delivery of improved financial management and savings measures. OBRI's developments and milestones include:

- executive support to the Business Review and Implementation Steering Committee (BRISC) which was established in early 2012 and includes DTF representation. BRISC's role is to oversee and provide governance to improve financial management and risk management of savings measures. OBRI reports monthly to BRISC on the status of implementation of savings initiatives

- regular meetings with Local Health Networks and business units to discuss and assist with the implementation of the efficiency savings measures approved by Government and monitoring progress against planned milestones

- OBRI commissioned consultants to undertake a hospital budget and performance efficiency review of the three main metropolitan Local Health Networks in 2012. The resulting reports and recommendations were considered by Cabinet in October 2012 and the Government response to the reviews was released in October 2012. The efficiency opportunities accepted by Government have been monitored and reported to BRISC by OBRI during 2012-13

- engaged a consultant to undertake a hospital budget performance review of the Women's and Children's Health Network. A report was provided in June 2013 and made available for public consultation, with responses submitted by early August 2013. SA Health released the Cabinet approved response in September 2013

- developed a financial management framework which has been promulgated across SA Health and made training available to staff

- developed a project management framework which has been promulgated across SA Health to assist with the management of savings projects. The project management framework includes the development of implementation plans for each efficiency savings initiative and project status reporting requirements which are assessed by OBRI

- finalising guidelines for measuring savings.

- in July 2013 OBRI implemented a web enabled project management application to enhance project management, monitoring and reporting of savings implementation across SA Health

- increased focus on further developing efficiency opportunities in system and business reform

9 Balance Sheet

9.1 Introduction

The Balance Sheet sets out the assets, liabilities and net worth (difference between assets and liabilities) of the State. This section provides some commentary of trends and influences in the State public sector financial position.

The information relates principally to data for both the general government sector and also the NFPS, which consolidates the general government and PNFCs sectors (including SA Water and ForestrySA).[18]

9.2 Overview of the State's financial position

The following summarises the financial position information for South Australia for the general government and NFPSs.

9.2.1 General government sector financial position

The following table provides time series data for the general government sector.

Table 9.1 – General government sector financial position (nominal terms)

	2009-10 Actual $'million	2010-11 Actual $'million	2011-12 Actual $'million	2012-13 Estimated result $'million	2013-14 Estimate $'million	2014-15 Estimate $'million	2015-16 Estimate $'million	2016-17 Estimate $'million
Financial assets	25 363	27 516	24 912	24 383	24 727	25 139	25 553	26 018
Non-financial assets	29 680	33 658	35 785	37 380	37 997	37 731	40 454	40 413
Total assets	55 043	61 175	60 698	61 763	62 724	62 870	66 007	66 430
Total liabilities	18 811	20 217	23 499	23 301	24 835	25 012	27 345	26 646
Net worth	36 231	40 958	37 199	38 463	37 888	37 858	38 662	39 784
Net financial worth	6 551	7 299	1 413	1 083	(108)	127	(1 792)	(628)
Net debt	1 402	2 930	4 165	5 611	6 951	7 064	9 446	8 751

Note: Totals may not add due to rounding.

Of note is the expectation that:

- financial assets increase by $1635 million across the forward estimates. This is due mainly to investments in other public sector entities, up $1368 million
- non-financial assets increase by $3033 million over the forward estimates. This is due mainly to the purchase of buildings and improvements, including the recognition of the new Royal Adelaide Hospital in 2015-16 ($2.8 billion)
- net worth (assets less liabilities) is estimated to increase to $39 784 million by 30 June 2017

[18] 2013-14 Budget Paper 3 'Budget Statement', appendix D details agencies within the respective sectors.

- net debt is expected to peak at $9446 million in 2015-16 due mainly to increased borrowing, including finance lease obligations associated with the new Royal Adelaide Hospital, to fund major capital investment programs.

9.2.2 Non-financial public sector financial position

The following table provides time series data for the NFPS.

Table 9.2 – Non-financial public sector financial position (nominal terms)

	2009-10 Actual $'million	2010-11 Actual $'million	2011-12 Actual $'million	2012-13 Estimated result $'million	2013-14 Estimate $'million	2014-15 Estimate $'million	2015-16 Estimate $'million	2016-17 Estimate $'million
Financial assets	5 143	5 638	2 543	2 738	2 479	2 323	2 203	2 079
Non-financial assets	53 228	59 359	62 322	63 396	64 709	65 068	68 318	68 877
Total assets	58 371	64 997	64 866	66 134	67 188	67 392	70 521	70 955
Total liabilities	22 140	24 040	27 667	27 671	29 299	29 534	31 858	31 171
Net worth	36 231	40 958	37 199	38 463	37 888	37 858	38 662	39 784
Net financial worth	(16 997)	(18 402)	(25 123)	(24 933)	(26 820)	(27 211)	(29 655)	(29 092)
Net debt	4 487	6 541	7 996	9 478	11 128	11 348	13 746	13 123

This table highlights that:

- non-financial assets dominate the financial position
- the value of non-financial assets is estimated to increase over the forward estimates by $5481 million by 2016-17. This increase mainly arises from investment and revaluation in health, transport and water related infrastructure
- net financial worth is negative as liabilities exceed financial assets. The negative balance generally increases over the forward estimates period
- net debt is estimated to increase across the forward estimates by $3645 million. The recognition of the new Royal Adelaide Hospital impacts on the increase in 2015-16 ($2.8 billion).

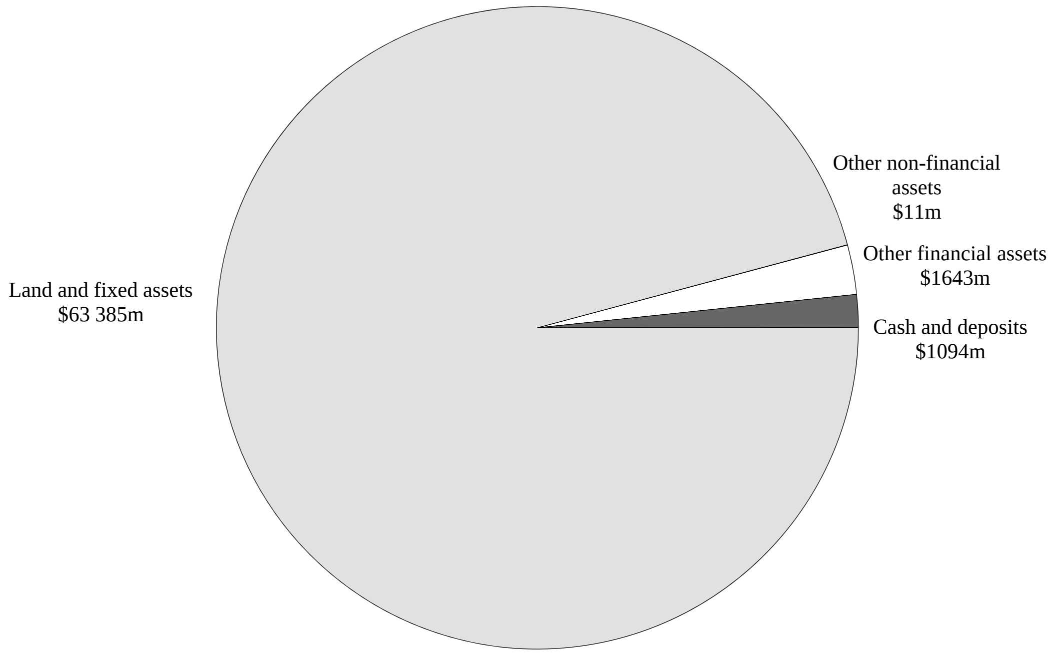
9.3 Assets

Table 9.2 shows that the State's asset position is growing from year to year because of major asset acquisitions.

9.3.1 Non-financial public sector assets

The following chart shows the estimated composition of assets under the control of the State as at 30 June 2013 for the NFPS.

Chart 9.1 – Non-financial public sector assets at 30 June 2013



Other financial assets include equity of $421 million. This comprises $846 million in other investments offset by a negative $425 million equity investment in other public sector agencies.

Non-financial assets represent the vast majority of State assets being 96% of the total. The State's non-financial or physical assets comprise mainly plant, equipment and infrastructure (including roads and water infrastructure) and land and improvements. These assets are divided between the general government and PNFC sectors.

In accordance with the Treasurer's Accounting Policy Statements, major assets are subject to regular revaluation. Valuation of public sector assets, particularly general government sector assets, is a subjective process. Valuations will reflect the specific circumstances of individual government entity operations. The general purpose is to provide users of financial reports with an understanding of the extent of assets employed by government agencies in their operations. Most assets are not realisable.

9.3.1.1 Revaluation of non-financial assets

Revaluations of non-financial assets will generally have the most influence on the improvement of the State's net worth. To illustrate, the following chart summarises actual asset value changes over the four year period 2009-10 to 2012-13 for the major agencies in the general government and PNFC sectors.

Table 9.3 – Revaluation of non-financial assets (actuals)

	2009-10 $'million	2010-11 $'million	2011-12 $'million	2012-13 $'million	Total $'million
General government	9 702	387	715	683	11 487
PNFCs	1 170	1 460	353	(545)	2 438
Total	10 872	1 847	1 068	138	13 925

Revaluation of the assets of the major agencies added $13.9 billion to the total value of non-financial assets over the four year period to 2012-13. Asset revaluations by the Department of Planning, Transport and Infrastructure account for 80% of total non-financial asset revaluations over the four year period covered in table 9.3.

The $545 million revaluation decrement for the PNFC sector in 2012-13 reflects a $403 million decrease in the valuation of freehold land and buildings owned by the South Australian Housing Trust.

During 2009-10 the value of the State's road network increased by $9.1 billion and reflects an internal revaluation undertaken by the Department of Planning, Transport and Infrastructure. A key assumption of the revaluation model adopted by the Department of Planning, Transport and Infrastructure is that the road network would be replaced by a modern equivalent asset rather than replacing the existing 'as constructed' network.

9.3.2 Financial assets

Total financial assets are expected to be $2.7 billion in 2012-13, falling to $2.1 billion in 2016-17. This reduction is primarily due to the movement in investments in other public sector entities under the equity category of financial assets.

Investments in other public sector entities represent the value of the Government's interest in PFCs including WorkCoverSA and the Motor Accident Commission (MAC).

In addition, Funds SA holds significant funds on behalf of other government agencies, including PFCs and government superannuation funds. This includes funds of MAC and funds held to back SAFA's insurance liabilities. The following table shows Funds SA's holdings of investment assets as at 30 June 2012 and 30 June 2013:

Table 9.4 – Funds SA's investments (actuals) [(a)] [(b)]

	Domestic equities $'million	International equities $'million	Fixed interest $'million	Other investments $'million	Total $'million
2012-13	4 449	4 831	1 806	9 599	20 685
2011-12	3 698	3 631	1 938	8 507	17 774

(a) Market values have been used in determining the above amounts.
(b) Excludes WorkCoverSA

As shown above, a large proportion of the State's investment assets are placed in both domestic and international equities. Investments of this type and nature are managed through the development of agency specific investment strategies, which are ratified by the relevant agencies' boards. International and domestic equity investments are subsequently managed by external fund managers on behalf of Funds SA.

Funds SA incurred a net gain from investing activities in 2012-13 of $2634 million reflecting the ongoing recovery of financial markets during the year. As the majority of managed funds are superannuation assets, much of this gain is reflected in an improvement in the unfunded superannuation liability.

Small increases in the outstanding claims liability compared to prior years and the reduction in revenue from investing activities has contributed to an increase in MAC's statutory solvency level, calculated in accordance with a formula determined by the Treasurer. As at 30 June 2013 MAC had net assets of $768 million, $371 million higher than 2012. The assets of the Compulsory Third Party Fund as at 30 June 2013 were 111.9% of the target level of solvency compared to 100.8% in the previous year.

WorkCoverSA reported a comprehensive profit result of $23 million in 2012-13. This compares to a comprehensive loss result of $437 million in 2011-12. The $460 million improvement in the comprehensive result was due mainly to an increase in net investment profit of $157 million coupled with a $286 million lower deterioration in the underwriting result caused mainly by a lower increase in the net outstanding claims liability.

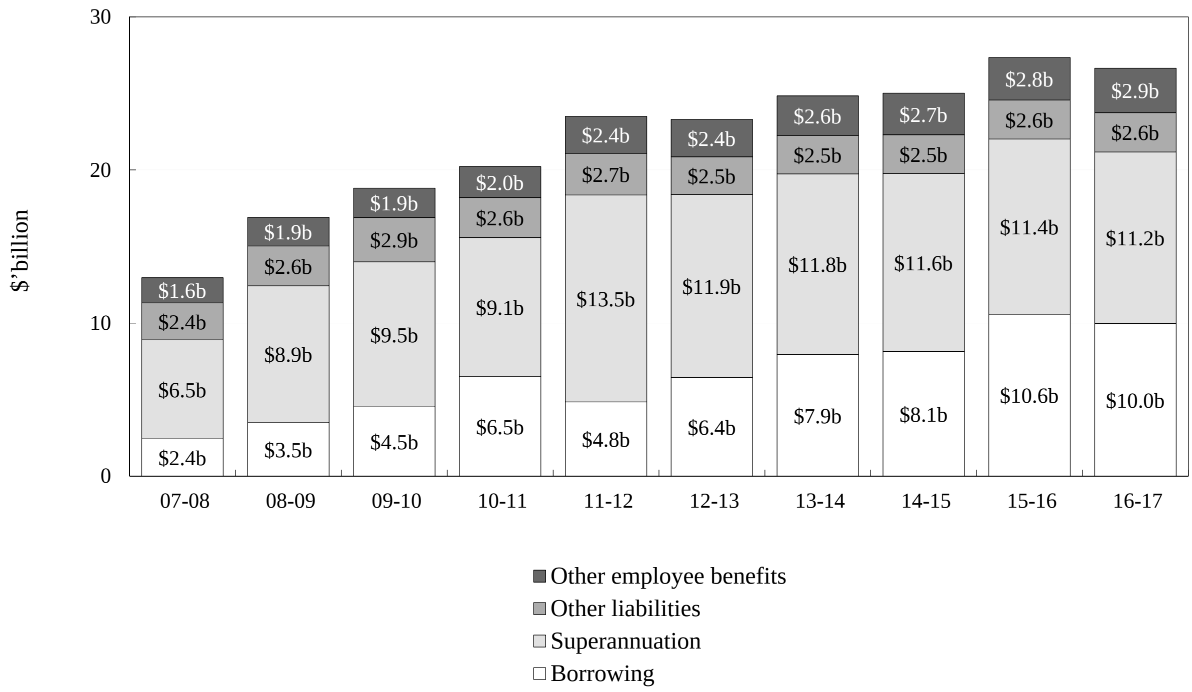
Further commentary is included under 'Motor Accident Commission', 'South Australian Government Financing Authority', 'Superannuation Funds Management Corporation of South Australia' and 'WorkCover Corporation of South Australia' in Part B of this Report.

9.4 Liabilities

9.4.1 General government sector liabilities

The following chart shows trends in the main elements of total liabilities for the 10 years to 2016-17.

Chart 9.2 – General government sector liabilities (nominal terms)



There was a structural break in 2011-12 – from 2011-12 borrowings are presented net of the Treasurer's deposits with SAFA

Total liabilities are estimated to decrease by $198 million to $23.3 billion in 2012-13. This is due mainly to decreases in the unfunded superannuation liability partially offset by an increase in borrowings. The variability in the unfunded superannuation liability in the five years to 2012-13 is due mainly to movements in earnings, actuarial assumptions and the discount rate used to estimate the value of the liability.

Total liabilities are expected to increase by $3345 million or 14.4% to $26.65 billion over the period of the forward estimates. This is due mainly to expected increases in borrowings, up $5118 million offset by unfunded superannuation liability reduction of $2314 million over the five years to 2016-17.

9.4.2 Non-financial public sector liabilities

The trends and composition of liabilities for the NFPS are consistent with those of the general government sector.

Total liabilities are expected to increase by $3500 million or 12.6% to $31.2 billion over the period of the forward estimates. In 2012-13 only a minor increase of $4 million in total liabilities is estimated, with higher borrowings offset by a reduced unfunded superannuation liability and advances received. Borrowings have increased due mainly to ongoing capital expenditure in the general government and PNFC sectors.

9.5 Unfunded superannuation

9.5.1 Background to unfunded superannuation liabilities

The unfunded superannuation liabilities are calculated in accordance with AASs as the net difference between the estimated value of accrued defined benefit superannuation obligations and the value of assets set aside to meet these obligations.

Superannuation liabilities are determined on long-term estimates of total liabilities. This is a liability to current and past members of closed defined benefit superannuation schemes. They are not liabilities that will be called on in total in the immediate future - thus there is the ability to seek to fund them over many years. The State has a long-term funding strategy in place.

In estimating the liabilities, a range of variable factors and assumptions are taken into account. Also important are the scheduled past service contributions by the Government. The superannuation liability may change periodically as assumptions and earnings experience change and, because of discounting, as the Government bond rate changes and the period of settlement approaches. This is an accepted fact for this type of liability.

9.5.2 Estimated unfunded superannuation liability at 30 June 2013

Unfunded superannuation liabilities are estimated to decrease by $1581 million to $11 941 million as at 30 June 2013 compared to the value at 30 June 2012. This decrease is explained in table 9.5 and includes the impact of an increase in the discount rate used to measure the liability of $771 million, higher than expected returns on investments of $733 million and other movements of $77 million.

A discount rate of 3.7% (effective annual rate) was used to calculate the 30 June 2013 estimate compared with 3.4% to estimate the actual liability at 30 June 2012. This increase in the discount rate resulted in a $771 million decrease in the liability over the year compared to the estimate as at 30 June 2012 and highlights the sensitivity of the valuation of the superannuation liability to movements in the discount rate. Should interest rates decrease in the future, the value of the liability will increase as discussed later.

The following table sets out the major elements that comprise the movement from the estimated unfunded superannuation liabilities at 30 June 2012 to the 30 June 2013 estimated liability.

Table 9.5 – Estimated unfunded superannuation liabilities as at 30 June 2013

	$'million	$'million
Estimated unfunded liability 30 June 2012 (2012-13 Budget)		11 908
Add: Difference between actual and expected returns	182	
Movement in discount rate	1 449	
Other	(16)	
Total changes		1 615
Actual at 30 June 2012		13 523
Add: Higher than expected returns on investments	(733)	
Movement in discount rate	(771)	
Other movements	(77)	
Total changes		(1 581)
Estimated closing balance June 2013		11 941

Note: Totals may not add due to rounding.

9.5.2.1 Superannuation discount rate

As required by AASs, the unfunded superannuation liability is estimated at a point in time by discounting future superannuation benefit payments by a discount rate that reflects the risk-free interest rate. The reference rate used is the longest dated Commonwealth Government nominal bond. Due to the high value of the expected payments to beneficiaries and the long-term nature of the liabilities, valuation of the superannuation liability is sensitive to movements in the discount rate. The following table provides examples of the possible values by varying the discount rate from the current rate of 3.7%.

Table 9.6 – Sensitivity analysis of unfunded superannuation liabilities to discount rate movements as at 30 June 2013

Discount rate %	Unfunded superannuation liability $'billion	Increase (Decrease) $'billion
4.7	9 841	(2 100)
3.7	11 941	-
2.7	14 541	2 600

Table 9.6 shows how significantly the value of the liability can change with movements in interest rates alone. For example, should the longest dated Commonwealth Government nominal bond rate increase to 4.7%, the value of the unfunded liability will reduce by $2.6 billion. The Budget records that while financial market volatility in the recent past has resulted in multibillion dollar revisions to the value of the liability recorded on the Balance Sheet, there has been no material change in the actual expected payments to beneficiaries underlying the liability.

9.5.2.2 Superannuation funding

DTF advised that total superannuation funding (including the fully funded Southern State Superannuation Scheme) is expected to be $1341 million in 2013-14, up $15.2 million on the estimated funding for 2012-13. Payments comprise amounts paid from agencies as contributions to current employment for new service and contributions reflecting a catch-up for the lack of funding for employment in previous years (past service contributions) prior to the full funding policy.

The past service superannuation liability cash payments are affected by a number of factors including the long-term earning rate on superannuation assets. Where investment performance exceeds the assumed rate, it is possible to reduce the level of past service payments required to fully fund superannuation liabilities by 2034. Additional funding contributions are required, however, to compensate for reduced earnings to remain on target.

The past service superannuation liability cash payment for 2013-14 is estimated to be $422 million.[19]

9.5.2.3 Earnings

Funds SA is responsible for managing the investment of superannuation assets. Investment earnings on superannuation assets are highly susceptible to economic conditions, financial markets and Funds SA's investment strategy. Further detail on investment performance is provided under 'Superannuation Funds Management Corporation of South Australia' in Part B of this Report.

An earnings rate of 19.6% was estimated for 2012-13 at the time of the 2013-14 Budget.

9.5.3 Long-term funding of superannuation liabilities

The commitment to fully fund unfunded liabilities was reaffirmed by the Government in the 2013-14 Budget, with the position as at 30 June 2013 remaining consistent with the plan to eliminate unfunded superannuation liabilities by 2034.

Past service superannuation liability cash payments increase over that period, in line with the Government's expectations of salary inflation. Assuming no change in the discount rate and a return to long-term earnings, unfunded liabilities are expected to have peaked in 2011-12. It is estimated that benefit payments will peak in 2026-27.

The Government's target to fully fund superannuation liabilities by 2034 is on track based on these estimates. Based on current data and estimates, in 2034 the liability will be fully funded by equivalent assets of $8.3 billion.

[19] 2013-14 Budget Paper 3 'Budget Statement', table 4.8.

9.6 Net debt

The restructuring of the State's finances over a number of years reduced net debt to historically low levels to the point that the general government sector had net financial assets rather than net debt for the three years to 2007-08.

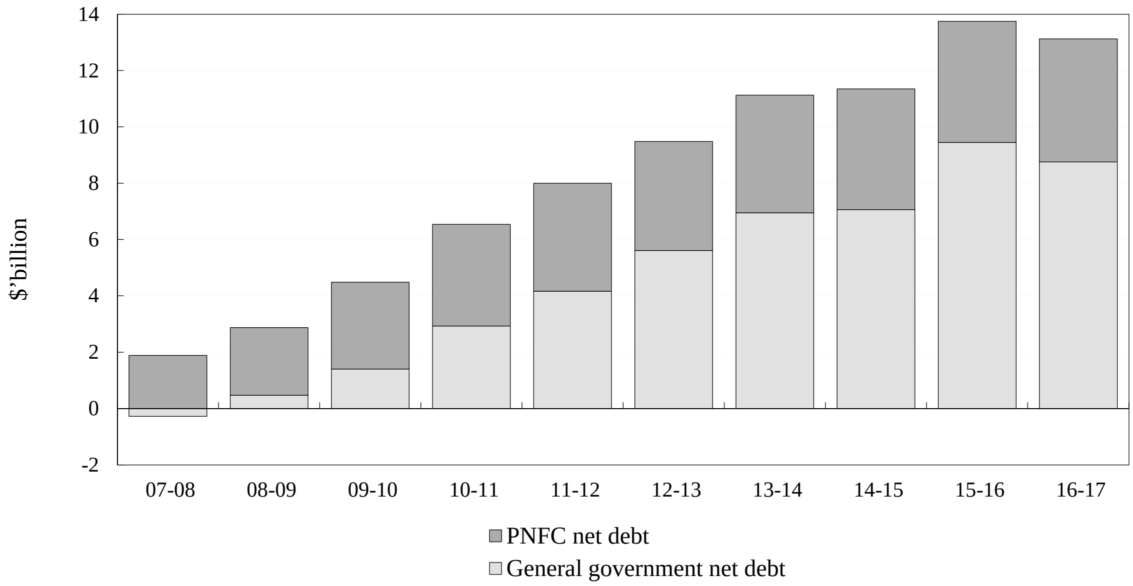
9.6.1 Definition of net debt

Net debt[20] equals certain financial liabilities (the sum of deposits held, advances received and borrowing) minus financial assets (the sum of cash and deposits, advances paid, and investments, loans and placements) as defined in the GFS framework.

9.6.2 Longer term trends in the level of debt

The following chart shows data on a long-term basis to the end of the forward estimates. Total net debt has increased by $6385 million to $7996 million (8.7% of South Australia's GSP) in the period 2007-08 to 2011-12, with general government net debt increasing by 106% over this period. In 2012-13 net debt is expected to increase by $1482 million to $9478 million (10% of South Australia's GSP). Forward estimates show that net debt is projected to rise to $13 123 million by 30 June 2017 (11.4% of South Australia's GSP).

Chart 9.3 – South Australian non-financial public sector net indebtedness 2007-08 to 2016-17



The general government sector is estimated to have net debt of $5611 million at the end of 2012-13. Over the forward estimates net debt increases in this sector by $3140 million to $8751 million. The increase in general government debt is mainly due to the Government's significant investment program, including the new Royal Adelaide Hospital, resulting in a net lending deficit until 2015-16.

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20 The indebtedness of the Treasurer, published in the Treasurer's Statements, represents the amount the Treasurer has borrowed from SAFA. This amount may be linked with the GFS accrual numbers, but a change in the GFS net lending position is not necessarily reflected by a change in the indebtedness of the Treasurer.

Net debt of the PNFCs increases by $505 million over the same period to $4372 million.

Chart 9.3 highlights that in 2011-12 debt in the general government sector increased to levels consistent with that found in the PNFC sector. From 2012-13 debt in the general government sector is estimated to grow at a higher rate than the PNFC sector.

The main holder of debt in the PNFC sector is SA Water. SA Water is a commercial business servicing its debt from business revenues.

SA Water's debt is mainly attributable to water treatment and security projects and includes progressive release of retention payments for the Adelaide desalination plant of $1824 million. In 2012-13, SA Water will account for around 93% of the total PNFC sector net debt. SA Water's net debt is forecast to steadily increase over the forward estimates to $3772 million in 2016-17.

The 2013-14 Budget Papers state that the PPP (capital component) arrangement for the new Royal Adelaide Hospital is to be recognised as a finance lease in the Balance Sheet and consequently have an impact on net debt and net financial liabilities. Further detail is provided in section 8.2.9 of this Report.

Table 9.7 explains the expected movements in net debt for the general government sector at the time of the 2012-13 Budget.

Table 9.7 – Reconciliation of movements in general government net debt as at the 2012-13 Budget

	2012-13 Estimated result $'million	2013-14 Budget $'million	2014-15 Budget $'million	2015-16 Budget $'million	2016-17 Budget $'million
Opening general government net debt	**4 165**	**5 611**	**6 951**	**7 064**	**9 446**
General government cash surplus/deficit	-1 482	-1 332	-77	-466	719
Add: Net cash flows from equity transactions	60	-10	-39	-30	-26
Finance lease acquisitions	-	-	-	2 820	-
Less:					
Other movements	25	-3	-3	-2	1
Improvement/Deterioration to general government net debt	**-1 447**	**- 1 339**	**- 113**	**- 2 382**	**695**
Closing general government net debt	**5 611**	**6 951**	**7 064**	**9 446**	**8 751**

Note: Table may not add due to rounding

9.6.3 Debt affordability and servicing

Chart 9.3 highlights the increase in public sector net debt over the period 2011-12 to 2016-17. At the end of 2012-13 total NFPS net debt is estimated to represent 10% of GSP compared to 11.4% in 2016-17.

The Budget records that the net debt increase includes the financial obligations for the new Royal Adelaide Hospital lease liability, which will appear on the general government Balance Sheet for the first time in 2015-16. This is estimated to add $2.8 billion to net debt at that time.

9.6.4 *Debt management policy*

SAFA has been delegated the responsibility for managing the debt of the South Australian Treasurer.

A portion of this debt is actively managed within limits authorised by the Treasurer, while other debt (CPI indexed debt and Commonwealth-State Housing debt) is managed on a passive basis. Any losses or gains made on the settlement of these transactions is to the Treasurer’s account, resulting in either an increase or decrease in the amount owed by the Treasurer. SAFA’s debt management performance is measured against benchmarks approved by the Treasurer.

The Treasurer’s approved policy for benchmark duration applied during the 2012-13 financial year is between one to 1.5 years. Lower duration benchmarks offer lower average interest costs over the long-term but with possible higher short-term budget volatility.

During 2012-13 SAFA’s funding task, after the budget and MYBR, was forecast at $6.4 billion comprising:

- $1.7 billion for the SA public sector
- $4.6 billion to refinance existing debt
- $0.1 billion in pre-funding/liquidity

During 2012-13 SAFA issued two new Select Lines, effectively lengthening the State’s refinancing profile. In September 2012 SAFA issued $0.75 billion of a new December 2012 Select Line and in February 2013 SAFA issued $2 billion of a new May 2016 Select Line. Both of these new lines were issued as floating rate notes. These new lines were predominately used to fund loans to the Treasurer and SA Water.

Additional commentary on the maturity profile of SAFA’s Select Lines is included under the heading ‘Further commentary on operations’ in the section titled ‘South Australian Government Financing Authority’ in Part B of this Report.

9.7 Other non-financial public sector liabilities

Other NFPS liabilities estimated as at 30 June 2013 comprise other employee benefits ($2520 million), payables ($1173 million), other liabilities ($1134 million), advances received ($232 million) and deposits ($178 million).

Other employee benefits include long service leave provisions ($1796 million estimated result for 2012-13), annual leave liabilities ($519 million estimated result for 2012-13) and salaries and wages liability ($140 million estimated result for 2012-13).

Significant individual balances in liabilities include amounts that are subject to estimation processes similar to that applying to the estimation of superannuation liabilities. They include:

- estimated long service leave provisions amounting to $1796 million as at 30 June 2013 and budgeted to increase to $1890 million by 30 June 2014. Long service leave is calculated by an estimation process in accordance with AASs

- estimated workers compensation provisions totalling $456 million are estimated as at 30 June 2013, increasing to $468 million at 30 June 2014.

9.8 Contingent liabilities

As reported in the Budget Papers[21] contingent liabilities are those that have not been recognised in the Balance Sheet, but rather are disclosed in notes to the accounts.

Reasons for this are:

- there is significant uncertainty as to whether a sacrifice of future economic benefits will be required
- the amount of the liability cannot be measured reliably
- there is significant uncertainty as to whether an obligation presently exists.

Contingent liabilities of the Government can arise from:

- legislative provisions requiring the Government to guarantee the liabilities of public sector organisations, eg financial institutions
- the ordinary activities of the Government might give rise to disputes and litigation that remain unresolved at any given balance date.

Guarantees and contingent liabilities of the Government of South Australia as at 30 June 2012 were valued at $896 million ($848 million as at 30 June 2011). Guarantees are valued at nominal values without adjustment for the probability of actual liabilities occurring.

9.8.1 Service risks and contingent liabilities

Agencies must continue to properly manage against incurring long-term liabilities arising from the inherent risks in the delivery of public services such as health, welfare, education, corrections, public housing and how duty of care responsibilities are exercised. Matters that have arisen over a number of years highlight the importance of public sector entities understanding the nature of risk in their circumstances and having relevant controls and processes in place to mitigate and monitor identified risks.

[21] 2013-14 Budget Paper 3 ‘Budget Statement’, pages 116-117 provides a summary of contingent liabilities.

10 Comparison with other states

10.1 Some observations

The purpose of this analysis is to draw attention to trends for this State over time and the relative differences between jurisdictions. No suggestions are made as to what is regarded as optimal. However, significant variations or negative trends would warrant consideration as to the related implications.

Across jurisdictions these indicators are influenced by varying valuation approaches for both assets and liabilities, differences in the type and level of infrastructure, as well as higher state debt levels. Infrastructure can also be provided through the private sector and therefore not be included in government data.

Prior to forming conclusions it is critical that any assessment made incorporates a sound understanding of the prevailing, specific circumstances in each state. Audit has not sought to provide all of the relevant information in this Report. Rather the opportunity is taken to show what each state is forecasting through to 2016-17.

The following table shows 2013-14 budgeted total revenue for each State.

Table 10.1 – 2013-14 budgeted general government total revenue by state

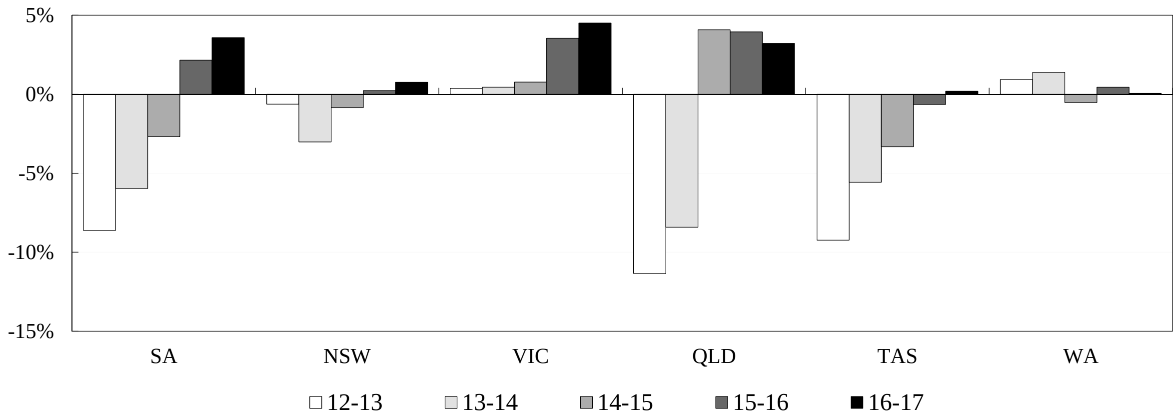
State	NSW	Vic	Qld	WA	SA	Tas
	$'million	$'million	$'million	$'million	$'million	$'million
Total revenue	62 573	50 328	44 677	27 978	15 265	4 792

Given the relative differences in size and level of financial activity of each state, comparisons that follow are given as proportions of total revenue in each state.

10.2 Operating Statement

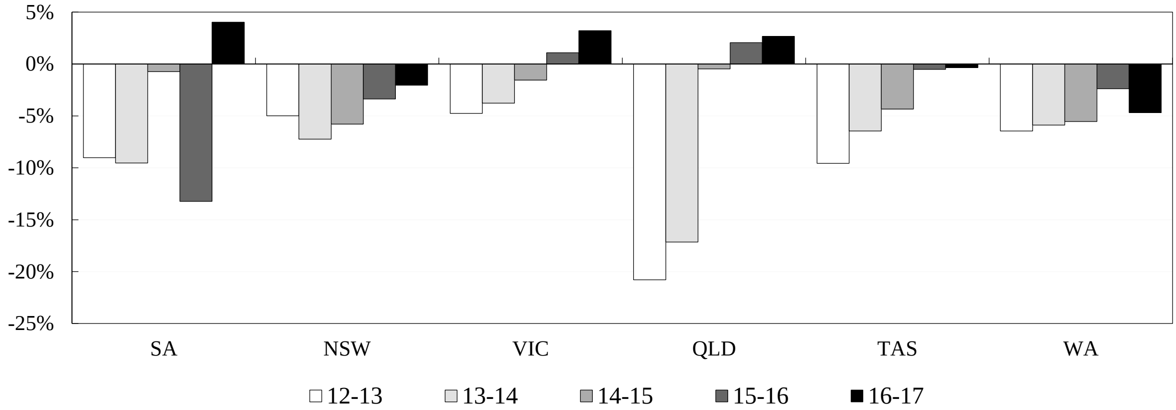
The following charts compare some trends in the GFS information with other states using 2013-14 Budget data.

Chart 10.1 – General government sector net operating balance as a proportion of total revenue



All states except Victoria and Western Australia have projected negative ratios for the 2013-14 financial year. Chart 10.1 also shows that all states except Victoria and Western Australia have net operating deficits budgeted for 2013-14. Across the forward estimates operating results vary widely between jurisdictions.

Chart 10.2 – General government sector net lending (borrowing) as a proportion of total revenue



As detailed in chart 10.2, all states are estimating net lending deficits up to and including 2014-15, with New South Wales, Tasmania and Western Australia showing deficits continuing to 2016-17. South Australia's forecast net lending deficit of $2306 million in 2015-16 reflects the impact of the new Royal Adelaide Hospital. Financial reporting for the new Royal Adelaide Hospital is commented on in section 8.2.9.1 of this Report.

Chart 10.2 shows that, with the exception of 2016-17, the trend in South Australia's net borrowing as a proportion of total revenues is reasonably consistent with other states over the four years.

10.3 Balance Sheet

10.3.1 Ratio of net financial liabilities to revenue

Net financial liabilities include the present value of the unfunded superannuation liability, which can fluctuate significantly from year to year depending on the discount rate used to calculate the liability. The rate used by each State in presenting their Budget varies, making direct comparison problematic.

The following chart plots the ratio of net financial liabilities to revenue for each of the states.

Chart 10.3 – Ratio of net financial liabilities to revenue

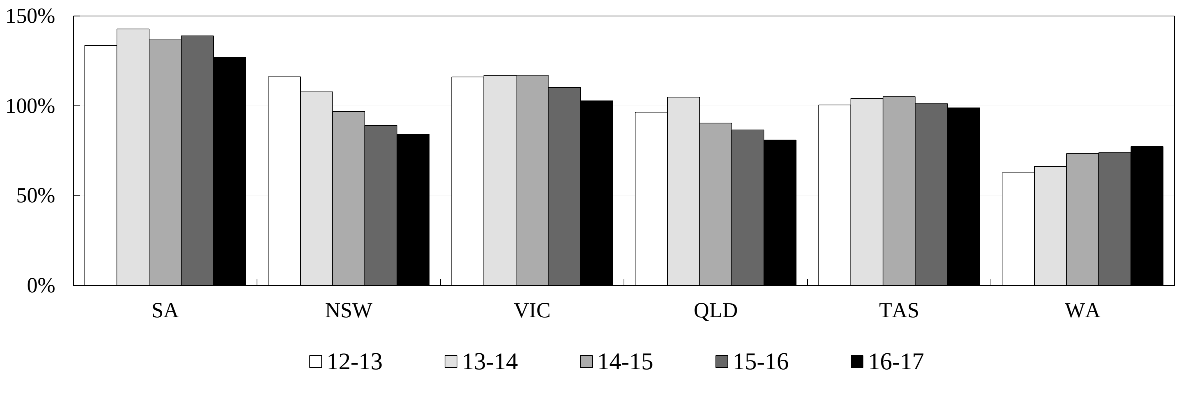


Chart 10.3 shows the 2012-13 Budget settings result in the ratio for South Australia fluctuating slightly over the next four financial years to 2016-17. It is evident that New South Wales, Victoria and Queensland are showing a general decline over the forward estimates to 2016-17.

11 Treasurer's Statements

11.1 Treasurer's Statements – *Public Finance and Audit Act 1987*

The Treasurer's Financial Statements are prepared pursuant to the PFAA to report on transactions and balances in the public accounts.

The main public accounts are the Consolidated Account, special deposit accounts and deposit accounts established pursuant to the PFAA.

A high proportion of, but not all, public monies are received and expended through the Consolidated Account. The main receipts to the Consolidated Account are state taxation and Commonwealth general purpose grants to the State.

Special deposit accounts and deposit accounts are used by almost all agencies as their main operating account. The Treasurer's financial statements report only the closing balances of these accounts. Detail of agency transactions are in the individual general purpose financial statements of agencies.

The Treasurer's financial statements set out the appropriation authority available from various sources for the financial year including the annual *Appropriation Act*, the Governor's Appropriation Fund, and specific appropriations authorised under various Acts. Also set out are the purpose and amount of payments from the Consolidated Account (that is, the use of that appropriation).

The Treasurer's financial statements are reported, in full, in the Appendix to Part B of this Report.

11.2 Scope of audit of the Treasurer's Statements

Audit reviewed the controls exercised by the Government Accounting, Reporting and Procurement branch surrounding the appropriation and disbursement of monies through the public accounts. This included the:

- testing of appropriation disbursements pursuant to the annual *Appropriation Act*, the Governor's Appropriation Fund, Contingency Funds and other Acts
- establishment and changes to Treasurer's special deposit accounts, imprest accounts and deposit accounts
- updating and recording of the Treasurer's loans and guarantees
- maintenance of the central general ledger.

The results of audit work undertaken identified certain areas where improvements could be made. Review findings are provided under the 'Audit findings and comments' heading in the section titled 'Department of Treasury and Finance' in Part B of this Report.

11.3 The Consolidated Account outcome

The following table sets out total appropriation authority and actual payments for the Consolidated Account in 2012-13.

Table 11.1 – 2012-13 appropriation authority and payments

	Appropriation authority $'million	Actual payments $'million
Appropriation Act 2012	12 280.7	12 226.7
PFAA, section 15	83.2	83.2
Governor's Appropriation Fund	382.2	188.1
Specific appropriations authorised in various Acts	121.0	121.0
Total	12 867.1	12 619.0

The result on the Consolidated Account and variations from budget for 2012-13 were as follows.

Table 11.2 – 2012-13 Consolidated Account result

	2011-12 Budget $'million	2011-12 Actual $'million	Variation $'million
Total receipts	10 124.1	11 504.2	1 380.1
Total payments	12 401.7	12 619.5	217.8
Consolidated Account financing requirement	(2 277.6)	(1 115.3)	1 162.3

The deficit of $1115.3 million ($1474.7 million deficit in 2011-12) is reflected as an increase in net debt serviced from the Consolidated Account as shown in Statement J of the Treasurer's Statements.

The key differences between actual and budgeted amounts were:

- ***Receipts*** – main items exceeding budgetary expectations (increase against budget) included greater than anticipated taxation receipts (increase $63.787 million), the return of cash to Consolidated Account – cash alignment policy ($192.301 million from a zero estimate), proceeds from the SA Lotteries Master Agent agreement ($402.771 million from a zero estimate) and proceeds from the sale of the State's Green Triangle forest plantations ($635.077 million from a zero estimate)

- ***Payments*** – higher than anticipated budgeted expenditure noted for the Department of Planning, Transport and Infrastructure ($135.2 million or 14.2%) and administered items for DTF ($91.347 million or 5%).

Consistent with the previous year, in 2012-13 significant amounts were appropriated to agencies as equity. The main equity contributions were to the Department of Planning, Transport and Infrastructure ($683.2 million), the Department for Health and Ageing ($314.4 million) and the Department of Further Education, Employment, Science and Technology ($112.5 million). Equity funding is credited directly to an agency's Statement of Financial Position, not through the Statement of Comprehensive Income. For further comment see section 11.6 of this Report. Details of the budget and actual data are presented in Statement A – Comparative Statement of the Estimated and Actual Payments from the Consolidated Account of the Government of South Australia.

11.4 Appropriation flexibility

Flexibility in appropriation authority arises from the provision of sources of funds for additional/new initiatives or unforeseen cost pressures that can be used without a requirement to return to Parliament for additional appropriation authority. This flexibility is provided by a combination of legislative provisions and budget practices.

The following table sets out relevant items for 2012-13.

Table 11.3 – Appropriation flexibility

	Authority/ Budget $'million	Actual payments $'million
Governor's Appropriation Fund	382.2	188.1
Contingency provisions in administered items for DTF	396.9	372.8
PFAA, section 15	83.2	83.2
Total flexibility	862.3	644.1

Use of these provisions requires the Treasurer's approval. Use of contingency provisions does not affect the Budget result as they are already included in that result.

11.4.1 Governor's Appropriation Fund and contingency provisions

Section 12 of the PFAA provides for the Governor's Appropriation Fund. Generally the Governor's Appropriation Fund is used to fund new Government initiatives or to meet unexpected expenditure needs.

Details of the purpose of appropriations from the Governor's Appropriation Fund are provided in Statement K – Governor's Appropriation Fund of the Treasurer's Statements. The main items were as follows.

Table 11.4 – Main Governor's Appropriation Fund payments

Agency	Purposes	Actual payments $'million
Department of Planning, Transport and Infrastructure	Additional appropriation being amounts received to ensure the Operating Account did not become overdrawn and funds required for the Adelaide Oval redevelopment.	$135.216
Department for Communities and Social Inclusion	Additional appropriation being amounts required for the National Partnership Agreement on Transitioning Responsibilities for aged care and disability services.	$11.462
Administered Items for the Department of Treasury and Finance	Additional appropriation being amounts received to fund unbudgeted payments to Parliamentary Superannuation Fund and Judges Pension Scheme.	$8.1

11.4.2 Contingency provisions

Contingency provisions for employee entitlements, supplies and services and plant and equipment are included in the total of the appropriation purpose ‘Administered Items for Department of Treasury and Finance’ in Statement A of the Treasurer’s Statements. These amounts are included within the total appropriation (and budgeted expenses) but may not be committed to a specific purpose at the time of the Budget. They are provided for potential budget impacts or for expenditure that is subject to further Cabinet or Ministerial approval.

Details of payments from the contingency funds are provided in Statement L – Statement of Other Transfers from the Administered Items for the Department of Treasury and Finance. Payments are transfers of additional funding to agencies.

The main items were as follows.

Table 11.5 – Main contingency provision payments

Agency	Total payments $’million
Department for Health and Ageing	178.461
Department of Education and Child Development	48.059
Department of Treasury and Finance	24.987
Department of Planning, Transport and Infrastructure	21.922
Department of Further Education, Employment, Science and Technology	18.849
Administered Items – Attorney-General’s Department	17.368

11.4.3 Appropriation by the Treasurer for additional salaries, wages etc

Section 15 of the PFAA provides that the Treasurer may appropriate from the Consolidated Account an amount sufficient to cover increases in public sector salaries, wages, allowances, payroll tax or superannuation contributions arising by reason of the award, order or determination of a court, tribunal or other body empowered to fix salaries, wages or allowances.

As with the Governor’s Appropriation Fund, use of this provision adds to the amount appropriated by Parliament each year and may affect the Budget result where these are unbudgeted expenses.

In 2012-13 $83.2 million was appropriated by the Treasurer pursuant to section 15 of the PFAA. This amount was added to the line ‘Administered Items for Department of Treasury and Finance’. Payments are reflected against that line. In 2011-12 the amount appropriated by the Treasurer was $42 million.

11.4.4 Appropriation transfers

In addition to the preceding provisions, appropriation can be transferred between agencies. Section 13 of the PFAA provides authority where excess funds exist for one agency and are necessary for another. Section 5 of the *Appropriation Act* provides authority where restructuring of an agency occurs so that appropriation related to transferring functions may in turn be transferred.

No section 13 transfers occurred in 2012-13. Section 5 transfers are detailed in Statement A of the Treasurer's Statements.

11.5 Special deposit accounts and deposit accounts

Most appropriation from the Consolidated Account is transferred to special deposit accounts and deposit accounts established pursuant to the PFAA. Under related provisions, monies credited to those accounts can be spent without further appropriation from Parliament. This is of significance in that monies appropriated in one year and transferred to a deposit account need not actually be expended in that year, that is, they may be carried over into the next year unless required by the Treasurer to be paid to the Consolidated Account.[22]

Table 11.6 shows that over $3371 million is held in special deposit accounts and deposit accounts as at 30 June 2013.

Table 11.6 – Special deposit accounts and deposit accounts

	2011-12 $'million	2012-13 $'million	Increase (Decrease) $'million
Special deposit accounts	2 686.7	2 757.9	71.2
Deposit accounts	684.1	613.1	(71.0)
Total	3 370.8	3 371	0.2

Such unspent balances do come under the scrutiny of Parliament as they are reported in the financial positions of agencies, in the Budget Papers and the balances are also reported in Treasurer's Statements F, F(1), F(2) and G.

The largest balances at 30 June 2013 were:

- ***Special deposit accounts*** – Accrual Appropriation Excess Funds ($433 million), Highways Fund ($311 million), Treasury and Finance Administered Items ($263 million), Health and Ageing ($177 million) and Treasury and Finance Administered Items – Intergovernmental Agreement on Federal Financial Relations ($177 million)

- ***Deposit accounts*** – South Australian Housing Trust ($61 million), Agents Indemnity Fund ($60 million), Rail Transport Facilitation Fund ($48 million), SAFA ($45 million) and Waste to Resources Fund ($44 million).

Account balances are subject to the Treasurer's cash alignment policy that aims to minimise balances as discussed below.

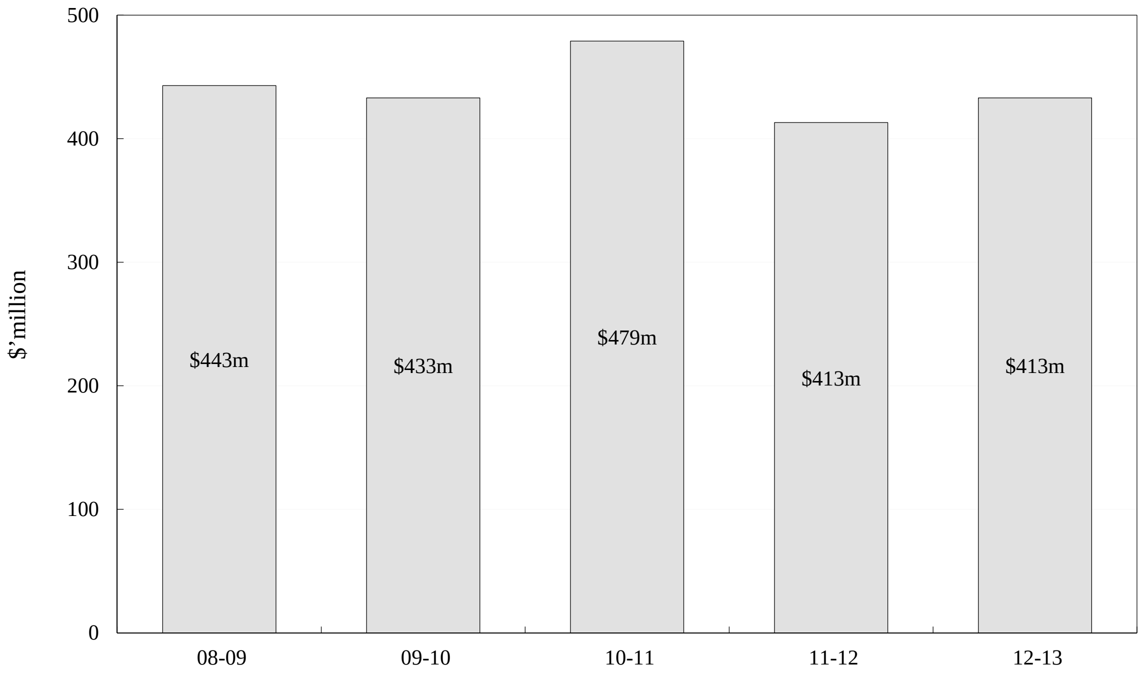
11.5.1 Accrual Appropriation Excess Funds Account

The approved purpose of the Accrual Appropriation Excess Funds Account is to record all receipts and payments associated with surplus cash balances generated in agencies by the shift to accrual appropriations.

[22] PFAA section 8(5) - any surplus of income over expenditure standing to the credit of a special deposit account must, at the direction of the Treasurer, be credited to the Consolidated Account.

Accrual appropriations are made to agencies for accruing leave liabilities (the value of the leave entitlement accruing to employees for the year rather than just the amount paid to employees taking leave in the year) and depreciation expenses.

Chart 11.1 – Accrual Appropriation Excess Funds Account



11.5.2 Treasury and Finance Administered Items – Intergovernmental Agreement on Federal Financial Relations Account

The approved purpose of the Treasury and Finance Administered Items – Intergovernmental Agreement on Federal Financial Relations Account (the Account) is to receive and disburse money paid to the State pursuant to the Intergovernmental Agreement on Federal Financial Relations for the national SPP purposes listed in Schedule F of that agreement and for the NPP payments for the purposes listed in Schedule G of that agreement.

The operations of the Account are included in the DTF administered financial statements, which are included in Part B of this Report. The balance in the Account at 30 June 2013 was $176.8 million. This entire balance is committed to various SA Government agencies to fulfil requirements under the Intergovernmental Agreement on Federal Financial Relations agreements.

11.5.3 Cash alignment policy

The Government has a cash alignment policy to align agency cash balances with appropriation and expenditure authority. Pursuant to the policy, payments are required to be made to return surplus cash to the Consolidated Account. All special deposit accounts are reviewed at least annually to determine whether there was surplus cash in an account. The policy supports the Treasurer's discretionary power to require surplus funds in special deposit accounts to be paid to the Consolidated Account.

A total of $192.301 million ($346.523 million in 2011-12) of surplus cash was returned to the Consolidated Account during 2012-13. The amounts were as follows.

Table 11.7 – Cash alignment policy repayments

Agency	**Total payments $'million**
Department of Treasury and Finance – Administered Items	150
Department of Communities and Social Inclusion – Administered Items	14.3
South Australia Police	12.3
Department of the Premier and Cabinet	9.7
Department of Primary Industries and Regions	4.1
Environment Protection Authority	1
Electoral Office	0.9

11.6 Equity contributions

Equity contributions to agencies are provided based on a DTF policy that provides guidance on budgeting for employee entitlements, depreciation, investing payments and appropriation, and for the operation of the Accrual Appropriation Excess Funds Account (AAEFA). Under the policy, agencies are provided with sufficient operating appropriation to fund their net operating expenses, including depreciation and employee entitlements.

Most investing payments are funded out of the appropriation provided to agencies for depreciation. In cases where net investing payments are less than the appropriation provided for depreciation, the surplus appropriation will be deposited into the AAEFA for future use. If the net cash requirement for investing payments exceeds depreciation, the cash shortfall is funded from the AAEFA or via an equity contribution if the balance in the AAEFA is not sufficient.

Treasurer's Instruction 3 'Appropriation' provides that where the First Schedule to the *Appropriation Act* requires that money be appropriated to a public authority as a contribution of equity, as a loan or for program funding, the Treasurer acquires a financial interest in the net assets of the public authority concerned. Monies issued or applied from the Consolidated Account pursuant to this instruction are not to be reported by the public authority as revenues in the period in which they are received, but are to be shown separately in the public authority's Statement of Financial Position, as a contribution of equity by the Government of South Australia.

Total equity contributions as at 30 June 2013 were $4470 million. Details of equity contributions provided to agencies are set out in the Treasurer's Statements – Statement I – Indebtedness of the Treasurer.

12 Whole-of-government/General government consolidated financial report

AASB 1049 Whole of Government and General Government Sector Financial Reporting requires the preparation of both whole-of-government (WhOG) and general government sector financial reports. Accordingly, both WhOG and general government sector financial reports form one CFR and is usually presented at the same time as the final budget outcome by DTF.

At present there is no requirement under the PFAA or other South Australian legislation to provide an independent audit opinion on the preparation of WhOG or general government sector financial reports.

Due to the timing of the preparation of the CFR, the last completed report relates to the year ended 30 June 2012, therefore the following commentary has been kept purposely brief.

12.1 AASB 1049 key concepts

As specified, the South Australian CFR is prepared by DTF pursuant to AASB 1049.

The CFR is not a general purpose financial statement. As such it is unique, and is influenced by two significant matters that affect the form and content of the report. Firstly, it is a requirement to prepare a financial report for the general government sector. Secondly, AASB 1049 requires use of a different accounting framework than that used by agencies when preparing their general purpose financial statements.

AASB 1049 requires financial reports to be prepared consistent with the principles and rules in the ABS publication 'Australian System of Government Financial Statistics: Concepts, Sources and Methods'.

12.2 AASB 1049 and the reporting entity concept

The reporting entity adopted is reflective of the 'enterprise unit' concept, where a reporting entity is an enterprise unit which can comprise one or more legal bodies. The WhOG reporting entity includes government departments (general government sector), non-financial corporations, financial corporations and other government-controlled entities. The general government sector reports from only one perspective, detailing that sector's transactions with non-financial corporations, financial corporations, and non-South Australian sector entities.

12.3 Scope of consolidated financial report audit

Consistent with previous years there is presently no requirement under the PFAA or other legislation to provide an independent audit opinion on the preparation of the CFR. Therefore, unless relevant legislative provisions are passed, I will not issue a formal independent audit opinion on the CFR.

Although there is no mandate for the Auditor-General to issue a formal independent audit opinion in respect of such information, I consider it both valuable, and within the ambit of wider public expectation, that such financial information should be subject to some form of independent review regarding its credibility and validity. Consequently, sufficient work has been undertaken in order to provide observations to DTF with respect to the CFR annually since 1999.

The key features of the CFR audit include a review of:

- the principles adopted in defining the economic entity for CFR purposes
- controls and procedures within DTF for evaluating the reliability and validity of data forwarded by agencies
- the adequacy and reliability of the Hyperion database as a medium for the preparation of the CFR
- processes for the preparation of the CFR
- compliance with appropriate legislation and accounting frameworks, in particular AASs, Urgent Issue Group Consensus Views, Treasurer's Instructions, and other professional reporting requirements in Australia.

Limitations still exist with the current reporting process. Notwithstanding these limitations, the usefulness and importance of the report in providing an understanding of the broad structure of the State's financial position is recognised as a key reporting tool of the Government.

12.3.1 Audit findings and comments

Following the audit review of the financial report for 2011-12, a management letter was forwarded to DTF in December 2012 that contained reporting and operational improvements. The audit management letter was reproduced in full in the CFR report published by DTF.[23]

The matters raised included:

- no review was performed of data provided by agencies against audited financial statements
- identified errors in the CFR were not tracked
- government to government transactions were not fully eliminated
- non-disclosure compliance with key AASB standards, some of which were associated with material balances reported within the CFR
- overstatement of the Treasurer's cash and cash equivalents
- incorrect classification of operating lease commitments with SAFA as general government.

Departmental response

DTF responded to Audit's comments with the following:

- checking procedures over data provided by agencies have been reviewed with a final review to be performed against audited financial statements for material agencies

[23] Government of South Australia, CFR for the year ended 30 June 2012.

- DTF will collate a list of known variances to agency financial statements
- government to government transactions will be fully eliminated
- disclosure to comply with key AASB standards will be made where relevant and material
- the Treasurer's cash and cash equivalents balance will not be overstated in future CFRs
- classification of operating lease commitments with SAFA will be corrected.

12.4 Consolidated financial report financial performance

The following discusses the financial performance for the WhOG as detailed in the CFR as at 30 June 2012. As previously discussed, data for the current year (due to the time needed for preparation) is not available at the time of this Report. The data below provides the opportunity to observe the financial result of the Government using a full accrual accounting basis, and the consolidation of all sectors. The consolidation process means that all inter-sector transactions are eliminated.

The following table summarises the WhOG financial performance per the CFR for the year ended 30 June 2012, with comparative amounts included for the prior year only. This table reflects the reporting and presentation requirements of AASB 1049.

Table 12.1 – CFR financial performance

	2012 $'million	2011 $'million
Revenue from transactions		
Taxation revenues	**3 483**	3 478
Grant revenue	**9 046**	8 524
Charges for goods and services	**4 651**	4 366
Interest income	**785**	854
Dividends and income tax equivalents	**37**	42
Other revenues	**898**	673
Total revenues from transactions	**18 900**	17 937
Expenses from transactions		
Employee expenses	**6 859**	6 534
Superannuation interest cost	**407**	427
Other superannuation expenses	**695**	653
Depreciation and amortisation	**1 131**	1 077
Use of goods and services	**4 555**	4 288
Interest expenses	**1 168**	1 036
Grant expenses	**2 479**	2 359
Other operating expenses	**1 642**	1 478
Total expenses from transactions	**18 936**	17 851
Net result from transactions - Net operating balance	**(36)**	86

Table 12.1 – CFR financial performance (continued)

	2012 $'million	2011 $'million
Other economic flows - included in net result		
Net foreign exchange gains	**53**	409
Net gain/loss on sale of non-financial assets	**(11)**	25
Net gain/loss on financial assets or liabilities at fair value	**8**	(117)
Net actuarial gains (losses) of superannuation defined benefit plans	**(4 429)**	403
Other net actuarial gains (losses)	**(1 049)**	(305)
Other economic flows	**(75)**	(68)
Total economic flows included in net result	**(5 503)**	347
Net result	**(5 539)**	433
Other economic flows - other non-owner movements in equity		
Changes in property, plant and equipment ARR	**1 695**	2 411
Net gain on financial assets at fair value	**(5)**	5
Prior period adjustments	**39**	62
Total other economic flows - non-owner movements in equity	**1 729**	2 478
Comprehensive result - change in net worth	**(3 810)**	2 911
Total change in net worth	**(3 810)**	2 911

Key fiscal aggregates		
Net operating balance	**(36)**	86
Less: Net acquisition of non-financial assets	**1 361**	1 904
Net lending/borrowing	**(1 397)**	(1 818)

The main variations in revenues in 2011-12 were as follows:

- ***Grant revenue*** – increased by 6.1% or $522 million. This decrease was mainly driven by an increase in both current and capital Commonwealth National Partnership grants of $280 million and $188 million respectively. There was also an increase in current Commonwealth specific purpose grants for on-passing of $96 million. Offsets included a $28 million decrease in other capital Commonwealth grant receipts, as well as a $37 million decrease in other capital grant and contributions receipts

- ***Charges for goods and services*** – increased by 6.5% or $285 million. The increase was mainly driven by an increase in SA Water rates and charges for water services of $152 million as well as an increase in fees and levies received of $137 million

- ***Interest income*** – decreased by 8.1% or $69 million. The increase was mainly driven by lower interest returns generated by SAFA ($55 million) as well as agency interest earnings principally from bank deposits ($25 million)

  Other revenues – increased by 33.4% or $225 million. The increase was largely due to the recognition of contributed assets associated with the Adelaide Oval redevelopment.

The main variations in expenses in 2011-12 were as follows:

- ***Employee expenses*** – increased by $325 million or 5%. This increase was due mainly to rising salary and wages costs of $295 million, an increase in TVSPs payments of $24 million and an increase in other employee related expenses of $28 million offset by a reduction in LSL expenses of $32 million

- ***Use of goods and services*** – increased by $267 million or 6.2%. This increase was due mainly to rising contract service expense costs of $123 million, other use of goods and services payments of $94 million and computing and communication expense payments of $43 million

- ***Interest expenses*** – increased by $132 million or 12.7%. This increase was due to an increase in borrowings interest of $115 million and finance charges on finance leases of $17 million

- ***Grant expenses*** – increased by $120 million or 5.1%. This increase was due to rising recurrent grants of $98 million, an increase in capital grant payments of $85 million and an increase in other current transfer payments of $80 million offset by a reduction in other capital transfer payments of $106 million and subsidies payments of $37 million

- ***Other operating expenses*** – increased by $164 million or 11.1%. This increase was mainly due to an increase in both self-insurance claims ($182 million) and gambling prizes/dividends ($22 million). Offsets included a $32 million decrease in other expenses, as well as a $28 million decrease in income/capital and redemption related workers compensation payments.

12.5 Consolidated financial report financial position

The following table summarises the WhOG financial position result per the CFR for the year ended 30 June 2012, with a comparative amount included for the prior year only. This table reflects the reporting and presentation requirements of AASB 1049.

Table 12.2 – CFR financial position

	2012 $'million	2011 $'million
Assets		
Financial assets		
Cash and deposits	**946**	838
Receivables	**2 027**	2 099
Advances paid	**2 484**	2 212
Investments, loans and placements	**8 608**	7 097
Investments - other	**14 894**	14 729
Interest in joint venture	**799**	706
Total financial assets	**29 758**	27 683

Table 12.2 – CFR financial position (continued)

	2012 $'million	2011 $'million
Non-financial assets		
Produced assets:		
Inventories	**673**	432
Machinery and equipment	**3 214**	2 525
Buildings and structures	**43 954**	42 156
Heritage assets	**1 111**	1 129
Biological assets	**84**	723
Intangibles	**103**	134
Non-financial assets held for sale or distribution	**608**	55
Other non-financial assets	**134**	166
Non-produced assets:		
Land	**12 321**	12 449
Intangibles	**341**	158
Non-financial assets held for sale or distribution	**509**	109
Total non-financial assets	**63 051**	60 036
Total assets	**92 809**	87 718
Liabilities		
Deposits held	**237**	248
Borrowing	**14 907**	12 331
Payables	**2 078**	2 415
Employee benefits	**2 506**	2 110
Superannuation	**13 523**	9 096
Superannuation fund deposits	**15 142**	14 303
Provisions (other than employee benefits)	**6 590**	5 572
Liabilities from non-financial assets held for sale or distribution	**24**	-
Other liabilities	**843**	874
Total liabilities	**55 850**	46 949
Net assets (liabilities)	**36 960**	40 770
Equity		
Retained earnings	**(467)**	4 763
Reserves:		
Asset revaluation reserve	**36 708**	35 238
Other reserves	**702**	747
Financial assets available for sale reserve	**16**	21
Total equity (Net worth)	**36 960**	40 770

The main variations in assets in 2011-12 were as follows:

- ***Advances paid*** – increased by $272 million or 12%. This was driven by an increase in loan advances of $300 million offset by a decrease in Treasurer's loans of $28 million

- ***Investments, loans and placements*** – increased by $1511 million or 21%. This increase is due to an increase in marketable debt securities of $1290 million and other investments of $281 million offset by a decrease in non-marketable debt securities of $61 million

- ***Machinery and equipment*** **–** increased by $689 million or 27%. This increase is due mainly to additions of $726 million in 2012-13 and $159 million of capitalised expenditure offset by depreciation charges of $241 million

- ***Buildings and structures*** **–** increased by $1798 million or 4%. This increase is due mainly to additions of $237 million in 2012-13, $1491 million of capitalised expenditure and $995 revaluation increments offset by depreciation charges of $853 million

- ***Biological assets*** **–** decreased by $639 million or 88%. This decrease is due mainly to the reclassification of standing timber as non-financial assets held for distribution as a result of the Government's decision to sell the State's Green Triangle forest plantations

- ***Non-financial assets held for sale or distribution*** **–** increased by $953 million due mainly to the reclassification of standing timber and plantation land, which during 2012-13 was transferred to the Treasurer in advance of the forward sale of the State's Green Triangle forest plantations.

The main variations in liabilities in 2011-12 were as follows:

- ***Borrowing*** **–** increased by $2576 million or 21%. This increase is due mainly to an increase in debt security holdings of $2580 million offset by a decrease in lease liabilities of $9 million

- ***Payables*** **–** decreased by $337 million or 14%. This decrease is due mainly to a decrease in derivatives payable - SAFA foreign exchange swaps of $395 million offset by an increase in accruals of $60 million and other payables of $8 million

- ***Employee benefits*** **–** increased by $396 million or 19%. This increase is due mainly to an increase in annual leave liabilities of $29 million, long service leave of $313 million and other employee benefit liabilities of $56 million

- ***Superannuation*** **–** increased by $4427 million or 49%. This increase is due mainly to a $4390 million increase in the State's defined benefit obligation. The increase in the defined benefit obligation was impacted by the decrease in the long-term Commonwealth bond rate, which is a key determinant of the actuarial calculation

- ***Superannuation fund deposit liabilities*** – increased by $839 million or 6%. This reflects an increase in the liability of Funds SA to all superannuation plans

  Provisions (other than employee benefits) **–** increased by $1018 million or 18%. This increase is due mainly to an increase in WorkCover provisions of $681 million, Motor Accident Commission motor vehicle compensation insurance claim provisions of $277 million, SAICORP insurance and risk management fund (SAGIRM) provisions of $35 million.

Acronyms used in this Report

Acronym	Description
AAS	Australian Accounting Standard[1]
AASB	Australian Accounting Standards Board
ABS	Australian Bureau of Statistics
CFR	Consolidated financial report
CPI	Consumer price index
DTF	Department of Treasury and Finance
FTE	Full-time equivalent
GFS	Government Financial Statistics
GSP	Gross state product
GST	Goods and services tax
MYBR	Mid-year budget review
NFPS	Non-financial public sector
PFAA	*Public Finance and Audit Act 1987*
PFC	Public financial corporation
PNFC	Public non-financial corporation
PPP	Public Private Partnership
SAFA	South Australian Government Financing Authority
SBCC	Sustainable Budget Cabinet Committee
SPP	Specific purpose current and capital payment
TVSP	Targeted voluntary separation package
WorkCoverSA	WorkCover Corporation of South Australia

[1] 'Australian Accounting Standards' means accounting standards issued by the Australian Accounting Standards Board that are in force in relation to the reporting period to which the financial report relates.