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Government
of South Australia

Report

of the

Auditor-General

Annual Report

for the

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Part C: State finances and related matters

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State finances and related matters

1 Introduction

The 2014-15 South Australian Budget was tabled in Parliament in June 2014. 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 2014-15 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 2013-14. 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 of this Report. 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.

After the global financial crisis in 2008-09 a common fiscal target was the achievement of sustainable surpluses. Some of the key elements of 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 – This 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 resulting 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. 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 (2014-15)
- a maximum ratio of general government net debt to revenue of 50%.

The 2014-15 Budget maintains the target of a net operating surplus by the end of the forward estimates but changes the target of a maximum ratio of general government net debt to revenue of 50% to a maximum of 35%. This is in response to a reduction in general government sector net debt of $2.7 billion, arising from the Government's decision to change the gearing level (level of debt as a percentage of assets) arrangements of the South Australian Water Corporation (SA Water) from 2014-15. Section 2.3 of this Chapter discusses this further.

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 reinforced the adverse effect of ongoing weaker than expected economic conditions and projected a return to net operating surplus in 2015-16. The 2014-15 Budget expects a deficit for the 2014-15 year before returning to net operating surpluses in 2015-16 and subsequent years.

2.2.2 Debt fiscal target

Since the 2011-12 MYBR the Government's debt fiscal target has been based on the ratio of general government net debt to revenue. 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. Prior to the 2014-15 Budget the target ratio was a maximum of 50%. The 2014-15 Budget has changed the target to a maximum of 35% in response to the change in gearing level of SA Water.

Net debt is expected to decrease from $6.887 billion as at 2013-14 to $5.269 billion as at 2017-18. Net debt peaks in 2015-16 at $7.146 billion. Expressed as a percentage of revenue, net debt is forecast to decrease from 45.1% as at 2013-14 to 28.2% as at 2017-18. As at 2015-16 the net debt to revenue ratio is expected to be 41.4%, which exceeds the new debt fiscal target of a maximum ratio of 35%. The net debt increase in 2015-16 is due to the expected recognition of the new Royal Adelaide Hospital ($2.8 billion) in that year.

2.2.3 The State credit rating

Securing and maintaining a triple-A credit rating for the State has been used in the past 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.

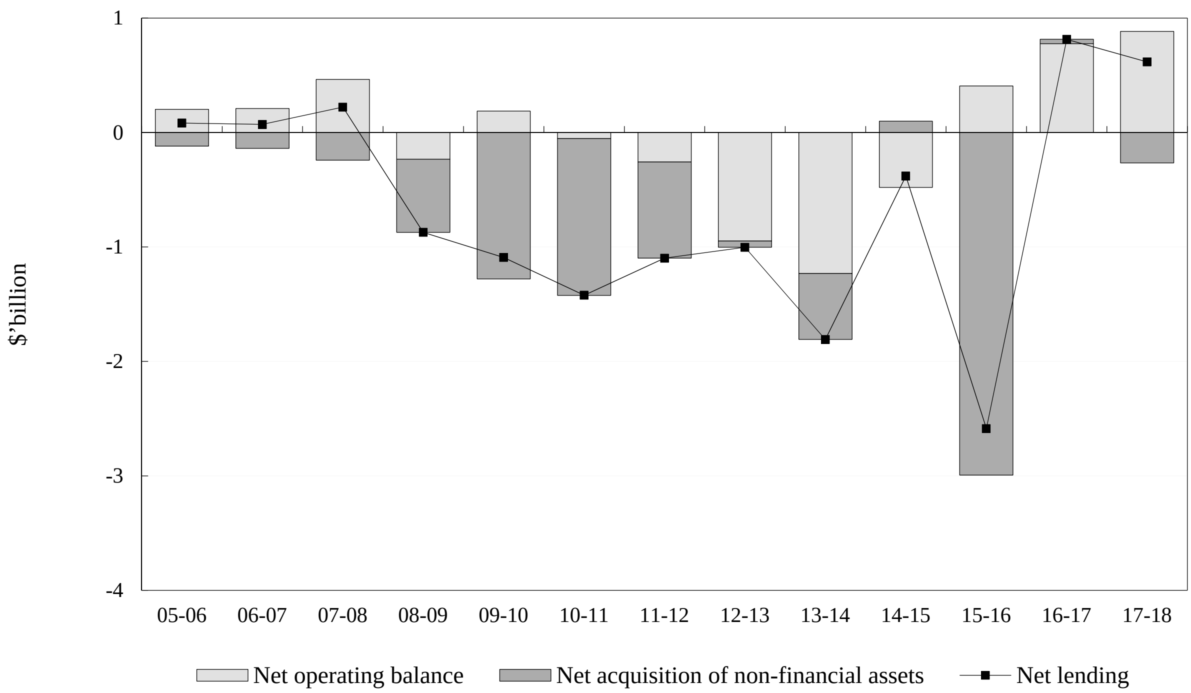
At the time of the release of the 2014-15 State Budget, Standard and Poor's commented that its current credit rating of the State of South Australia of AA with a stable outlook is not immediately affected by the State's Budget.

Moody's commented on the 2014-15 Budget that the potential for weaker than anticipated revenue growth remains a risk for budget outcomes. It noted that the State is counting on conveyancing duties rising 9.6% annually and payroll tax by 6.3% to drive the 5.2% annual rise in revenues through to 2017-18, which could be optimistic. Moody's also observed that the State's ability to achieve the forecast low 1.9% annual average increase in current expenditure over the same period – largely supported by only a 1% rise in employee costs – will be challenging.

2.3 Changing financial position

The following chart demonstrates the trend in net lending since 2005-06 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.

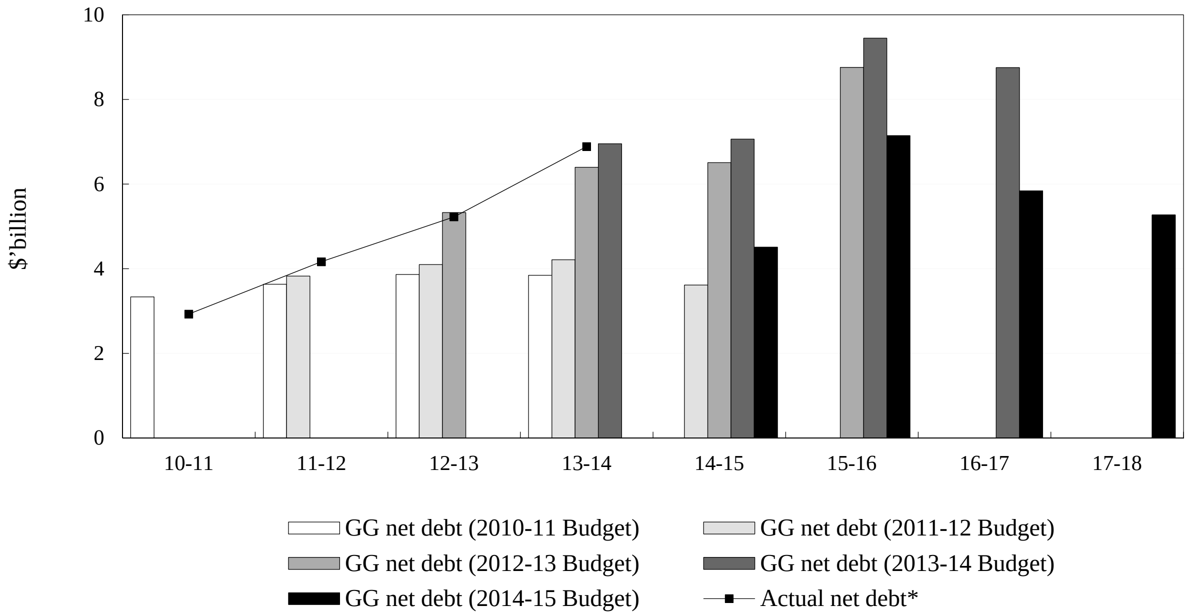
For the seven year period from 2008-09 to 2014-15 net operating deficits result for each year other than 2009-10. This reflects the impact of the global financial crisis and the ongoing global economic uncertainty, and the budget policy dimensions and decisions for revenue and expense management set over recent years. A return to net operating surplus is projected in 2015-16, on the basis of anticipated strengthening revenue growth rates and significant expenditure restraint.

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 $7.1 billion as at 2015-16, before reducing to $5.3 billion as at 2017-18. 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 2017-18. 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 over recent budgets.

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



* 2013-14 is estimated net debt.

Chart 2.2 highlights the significant increase in net debt estimates in the 2012-13 and 2013-14 Budgets. The increases reflect 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.

The 2014-15 Budget net debt estimates are significantly lower than in the 2013-14 Budget as a result of the proposed increase in the SA Water debt level by $2.7 billion. The effect of this adjustment on net debt is to move $2.7 billion of debt from the general government sector balance sheet to the PNFC balance sheet in 2014-15. The Government indicated that this adjustment will be made to ensure that the SA Water balance sheet is consistent with that of other government-owned utilities interstate. Page 74 of 2014-15 Budget Paper 3 'Budget Statement' discusses this changed debt arrangement further. This explains the significant reduction in general government sector net debt projections in the 2014-15 Budget.

It is important to note that the SA Water debt adjustment arrangement does not change the overall level of net debt expected for the NFPS (combined general government and PNFC sectors) which remains consistent between the 2013-14 Budget and the 2014-15 Budget. For example, the 2014-15 Budget projects net debt to be $11.497 billion in the NFPS in 2014-15 and the projection for the same year in the 2013-14 Budget was $11.348 billion.

Net debt is also expected to reduce in 2016-17 due to a Motor Accident Commission (MAC) contribution of $500 million resulting from a government decision to open the provision of Compulsory Third Party (CTP) insurance to the private sector from 1 July 2016.

2.4 Operating statement

2.4.1 Estimated results for 2013-14

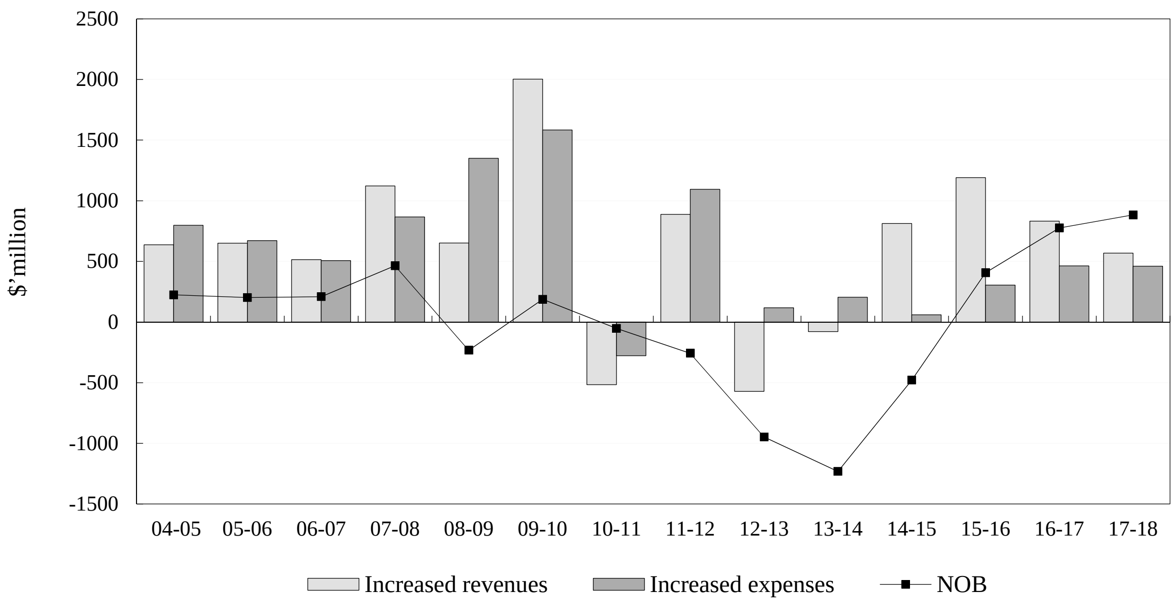
The 2014-15 Budget estimates a net operating balance deficit of $1232 million for 2013-14 compared to the budgeted deficit of $911 million. The difference between the budgeted and estimated result is mainly due to employee expenses increasing by $103 million and other operating expenses increasing by $235 million.

The net lending deficit is estimated to be $1808 million, compared to the budgeted amount of $1455 million. The difference between the budgeted and estimated deficit is mainly due to deterioration in the net operating balance estimate in 2013-14.

2.4.2 Budget forecasts 2014-15 to 2017-18

Chart 2.3 shows annual increases in revenues and expenses since 2004-05 compared to annual changes estimated for the four years of the 2014-15 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 four years to 2007-08, annual increases in revenues and expenses were reasonably consistent and net operating surpluses were achieved over the period. The global financial crisis affected 2008-09 and a net operating deficit resulted. 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.

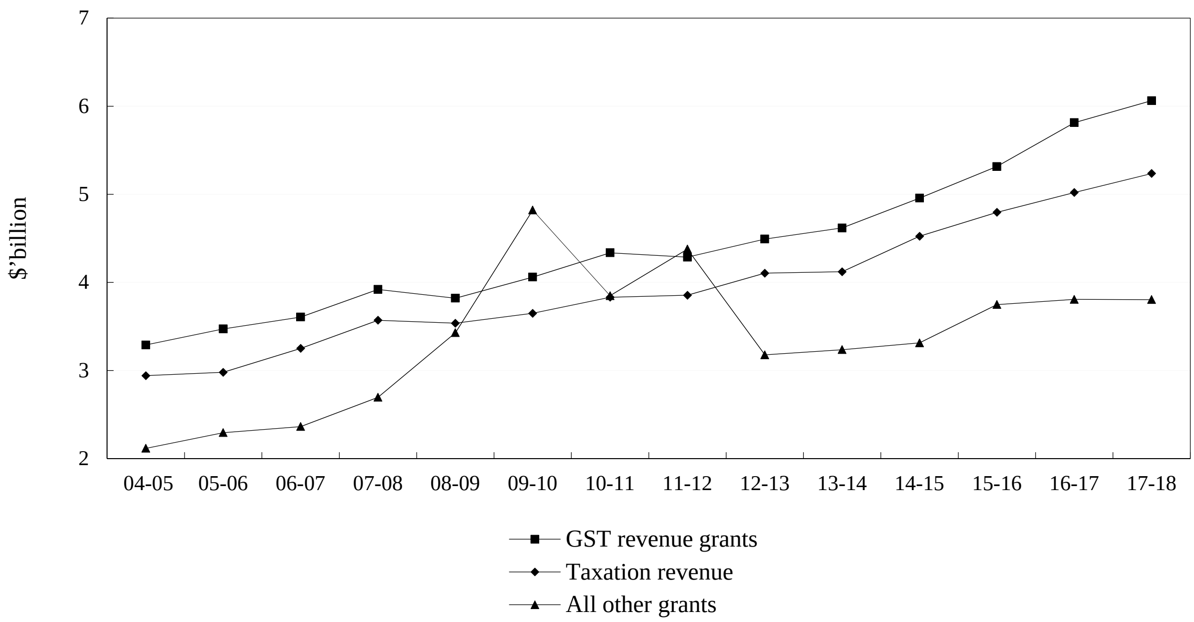
The chart shows that revenues are estimated to improve consistently over the four years of the 2014-15 Budget. In 2015-16, when the Budget expects to return to a net operating surplus, taxation revenue is expected to increase by $271.4 million and grant revenue is expected to increase by $793.8 million (including a GST revenue grants increase of $358.9 million, recurrent specific purpose grants increase of $116.2 million and capital grants from the Commonwealth increase of $306.6 million).

Chart 2.3 also highlights that the projected net operating surpluses for 2016-17 and 2017-18 are the two highest of any year on the chart.

2.4.3 Revenue forecasts 2014-15 to 2017-18

Chart 2.4 shows expected trends for the major revenue items in the 2014-15 Budget against the experience of the ten years to 2013-14.

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.

Further, 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. Specifically, chart 2.4 shows that the category all other grants (principally other Commonwealth grants) increased markedly in the period 2008-09 to 2010-11. This was 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.

Both GST revenue grants and taxation revenue streams are expected to experience consistent growth over the four years of the 2014-15 Budget, on the basis of projected increases in the State's share of the national GST pool and an expected continued recovery in revenues from property taxes. Given that there is still an environment 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).

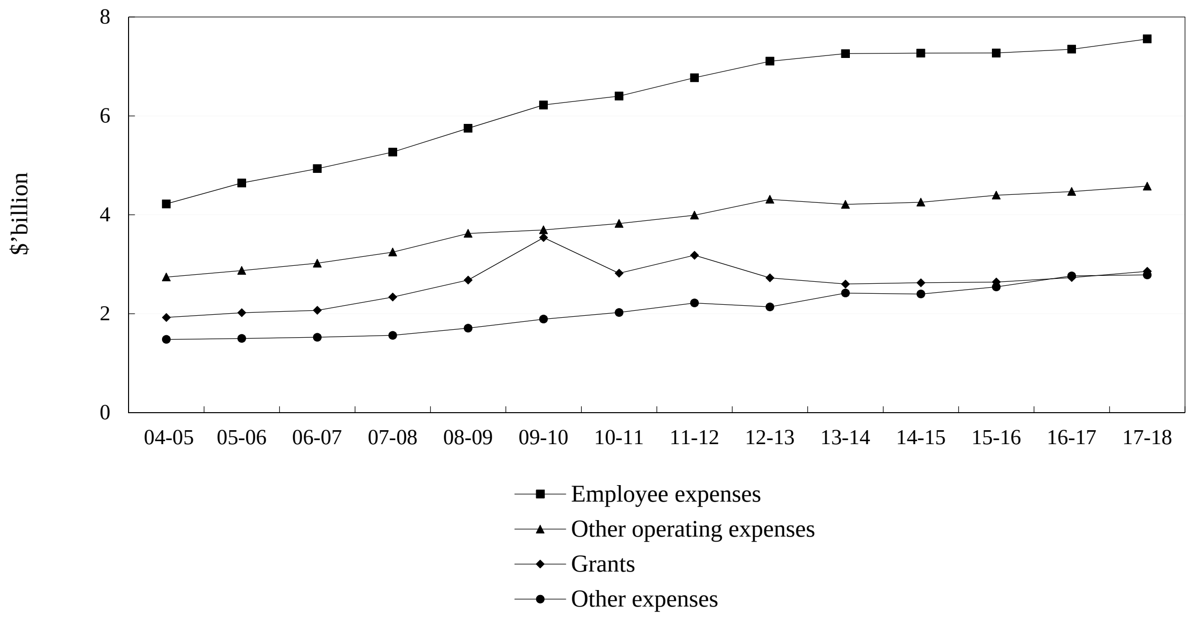
The 2014-15 Budget also contains a taxation measure that removes the general remissions provided on the fixed and mobile property Emergency Services levy. Over the four years of the 2014-15 Budget this measure increases the Emergency Services levy collected by $355.8 million.

The Budget indicates that the 2014-15 Commonwealth Budget implemented significant decreases in Commonwealth funding in the main areas of Commonwealth specific purpose payments and National Partnership payments. Table 1.3 of 2014-15 Budget Paper 3 'Budget Statement' outlines the specific areas where reductions were made, including estimated reductions in the 2017-18 year. This is further discussed in section 7.2 of Chapter 7 of this Report.

2.4.4 Expense forecasts 2014-15 to 2017-18

Chart 2.5 shows trends expected for total expenses in the 2014-15 Budget split into four main categories, against the experience of recent years.

Chart 2.5 – General government sector expenses



Employee expenses are estimated to increase in 2013-14 and beyond but at significantly lower rates than the experience in earlier years. This reflects the expected reductions in employment numbers over the forward estimates.

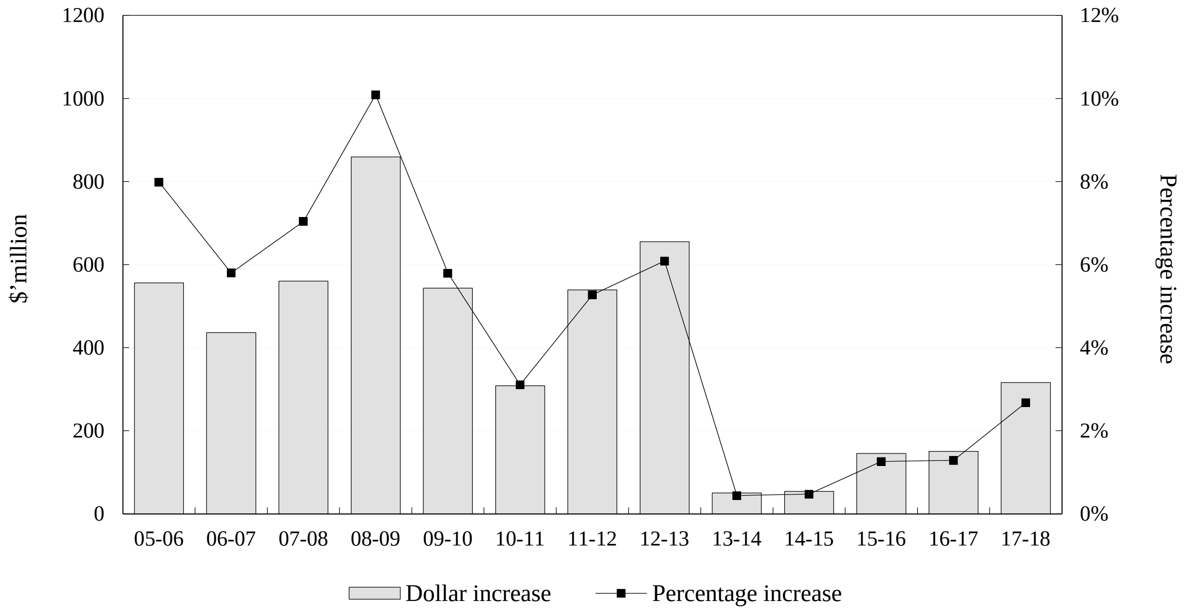
Other operating expenses show consistent gradual increases, other than in 2012-13 when the additional increase was due to relief of $320 million debt on the South Australian Housing Trust balance sheet following relief of the same amount of South Australia's public housing payments due to the Commonwealth.

The fluctuation in grant expenses is mainly associated with fluctuations in Commonwealth grant revenues discussed above in section 2.4.3.

The challenging dimension of expenditure restraint underlying the 2014-15 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 70% of expenses for 2014-15, a proportion that is consistent with most years.

Chart 2.6 shows that the annual movements estimated or projected for employee expenses and other operating expenses for the period 2013-14 to 2017-18 are below all of the previous eight years' experience, other than 2010-11.

Chart 2.6 – Annual change in employee and other operating expenses



Integral to the expenditure restraint is achieving significant savings initiatives built into the forward estimates from previous Budgets and the current Budget. 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 2013-14 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 $576 million, which is in line with the budgeted amount of $544 million.

Purchases of non-financial assets in 2014-15 are expected to be $1.2 billion and are projected to be above $1 billion for each year of the forward estimates. Purchases increase significantly in 2015-16 due to the recognition of $2.8 billion for the new Royal Adelaide Hospital.

For the general government sector, sales of non-financial assets peaked at $1.2 billion in 2012-13. Sales included 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 $389 million in 2014-15 and reduce to less than $100 million for the remaining three years of the forward estimates.

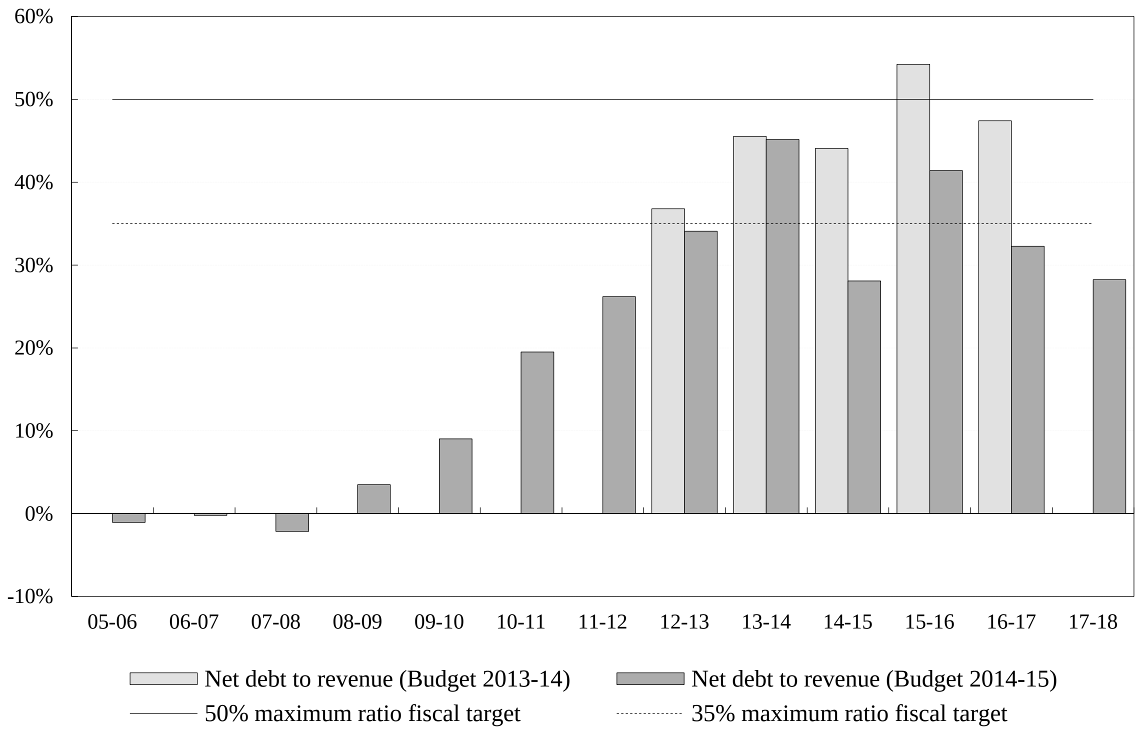
2.4.6 Ratios of net debt to revenue

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 35%.

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 forms 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 2013-14 and 2014-15 Budgets.

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



The 2014-15 Budget projects that net debt will be at lower levels than was previously estimated in the 2013-14 Budget. This is primarily due to the adjustment to the SA Water debt level and the resultant reduction in general government sector net debt of $2.7 billion in 2014-15. Consequently, the ratio of net debt to revenue falls below the 35% maximum set by the Government's fiscal target in 2014-15. The ratio peaks in 2015-16 at 41.4% as a consequence of the recognition of the new Royal Adelaide Hospital. The ratio falls back below 35% in 2016-17 and 2017-18 on the basis of expected significant revenue growth and net operating surplus projections of $776 million in 2016-17 and $883 million in 2017-18.

Net debt is also reduced in 2016-17 by an expected MAC contribution of $500 million from a government decision to open the provision of CTP insurance to the private sector from 1 July 2016.

The 2015-16 projected ratio exceeds the maximum of 35% established by the Government's fiscal target due to the recognition of the new Royal Adelaide Hospital, and then falls below this maximum for the final two years of the 2014-15 Budget.

2.4.7 Interstate comparison

Section 10 of this Report includes comment on 2014-15 Budget comparisons for key budget aggregates across jurisdictions. In 2014-15, South Australia, New South Wales and Tasmania are forecasting general government sector net operating balance deficits. Tasmania, Western Australia and New South Wales expect net lending deficits for all estimate years. Victoria is expecting a net lending surplus in 2014-15 while the remaining States expect to return to net lending surpluses over the forward estimates. 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 over the four years of the 2014-15 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 $2 billion due primarily to the growth in borrowings.

Net worth is estimated to add $3.6 billion over the forward estimates to reach $42.9 billion by 2016-17.

2.5.1 Assets

Total assets are expected to increase over the forward estimates from $67.2 billion as at 2013-14 to $72.5 billion as at 2017-18. 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 $3.1 billion for the four years through to 2017-18. Revaluations in the PNFC sector are also estimated to add substantially to non-financial assets.

Total financial assets are expected to be $3.4 billion in 2013-14, falling to $3 billion in 2017-18. 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 MAC.

WorkCoverSA reported a comprehensive profit result of $235 million in 2013-14. This compares to a comprehensive profit result of $23 million in 2012-13. The improvement in the comprehensive profit was mainly due to a reduction in the cost of claims (due to a smaller

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

increase in the outstanding claims liability). This contributed to an improvement in its funding ratio from 63.7% to 71%, compared to its approved target funding range of 90% to 110%. As at 30 June 2014 WorkCoverSA had a net liability position of $1131 million ($1366 million).

MAC reported a comprehensive profit result for 2013-14 of $483 million, compared to a comprehensive profit result of $371 million in 2012-13. MAC's statutory solvency level, calculated in accordance with a formula determined by the Treasurer, increased to 132.1% (111.9%) of the target level of solvency. As at 30 June 2014 MAC had net assets of $1251 million ($768 million).

2.5.1.1 Compulsory Third Party insurance changes

The Government has decided to open the provision of CTP insurance to the private sector in South Australia from 1 July 2016.

As a consequence of this decision, MAC will end its role as the sole provider of CTP insurance in South Australia. This will allow MAC to cease writing new CTP insurance policies and to run off its claims against policies issued up to and including 30 June 2016.

This will allow MAC to pay an estimated $500 million in 2016-17 from its surplus net assets to the Government. This will also reduce general government sector net debt by $500 million in 2016-17.

DTF advised that the estimate of $500 million was based on the net asset position of MAC as at 30 June 2013 of $767.7 million and a preliminary value of net assets as at March 2014 of $886.9 million. As noted above the net asset position of MAC as at 30 June 2014 was $1251 million.

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 $10.9 billion as at 30 June 2014 to $12.5 billion as at 2017-18. The general government sector net debt is estimated to increase to $6.9 billion at 30 June 2014, falling to $5.3 billion as at 2017-18. In 2015-16 net debt rises to $7.1 billion as it includes the effect of accounting for the new Royal Adelaide Hospital (discussed further in section 2.6.7.1 of this Chapter). The reduction in net debt in the general government sector is attributable to the SA Water debt restructure of $2.7 billion in 2014-15.

The other major component of liabilities, unfunded superannuation liabilities, is estimated to be $10.5 billion for the year to 30 June 2014. 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 4.3% was used for the estimate in the 2014-15 Budget, compared with 3.7% for the 2013-14 Budget. A 1% increase in the discount rate is estimated to decrease the superannuation liability by $2.3 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 4.6 of 2014-15 Budget Paper 3 ‘Budget Statement’ itemises expected past service superannuation liability cash payments for 2013-14 and the four years of the Budget.

2.6 Risks and management tasks for the 2014-15 Budget

The stated fiscal strategy of the 2014-15 Budget is to achieve a net operating surplus by the end of the forward estimates. Consistent with recent past years, key elements to the success of the 2014-15 Budget will be achieving estimated real growth in major revenue items and realising expenditure restraint arising from previously announced and current budget improvement measures.

As in past years, Audit sought DTF’s view of areas of the Budget considered to be the highest risks and the nature of specific monitoring measures. DTF responded that the major risks to the fiscal outlook are set out in Chapter 6 of 2014-15 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 2014-15 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 process undertaken for the 2014-15 Budget was the same as for 2013-14. Data for all lines is maintained in DTF’s Budget and Monitoring System and then is only amended with specific approvals through the following processes:

- Cabinet decisions
- carryovers
- impacting and non-impacting data adjustments
- mid-year review adjustments
- 2014-15 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 consistency 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. In estimating revenue items, DTF applies a range of assumptions. These assumptions are outlined in Chapter 3 of 2014-15 Budget Paper 3 ‘Budget Statement’.

[2] 2014-15 Budget Paper 3 ‘Budget Statement’, Chapter 6.

2.6.1 Net operating balance

The 2014-15 Budget estimates net operating deficits for the general government sector for 2013-14 and 2014-15. The budget is expected to return to a surplus of $406 million in 2015-16 and the surplus is expected to grow to $883 million by 2017-18.

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					*(948)	(911)	(431)	375	661
NOB 2014-15 Budget						*(1 232)	(479)	406	776

* 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.

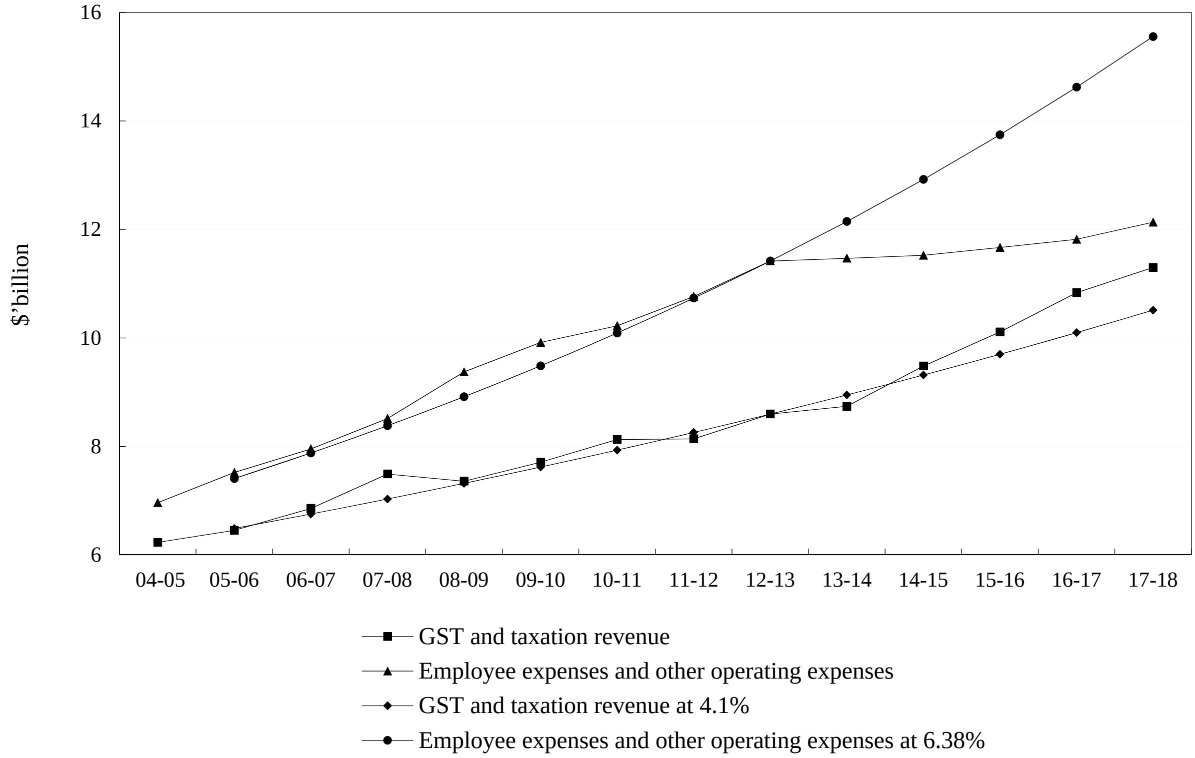
Table 2.1 also demonstrates the ongoing impact on the estimates for the years 2012-13 to 2015-16. For these estimate years successive Budgets have lowered the estimated net operating result from the previous Budget. This has had a marked effect as expected surpluses in the 2011-12 Budget became estimated deficits in the 2012-13 Budget. The cumulative unfavourable expected turnaround in the net operating surplus between these two Budgets amounts to $2.5 billion. The 2013-14 Budget revised the net operating surpluses down by a further cumulative amount of $767 million. This mainly reflects the deterioration of GST and taxation revenue estimates over this period and the present level of expenditure projections.

The 2014-15 Budget (consistent with the previous two years' Budgets) expects a return to net operating surpluses in 2015-16, where an improvement of $885 million in the net operating balance is projected.

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 2014-15 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 expense items in the 2014-15 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 2012-13 and estimated revenues from 2013-14 to 2017-18. For the nine years to 2012-13, these two combined items grew on average annually by about 4.1%. Applying this average growth rate from 2004-05 through to 2017-18 creates the GST and taxation revenue at 4.1% line. While these two lines are reasonably close, a gap between past experience and Budget estimates emerges in 2015-16 and is sustained over the final two estimate years. Further comments on operating revenue risks are provided in section 2.6.2 below.

For the nine years to 2012-13 combined employee expenses and other operating expenses grew on average annually by about 6.38%. Applying this average growth rate from 2004-05 through to 2017-18 creates the employee expenses and other operating expenses at 6.38% line. Comparing the trend of this line to the estimated expenses for the 2014-15 Budget shows a diverging difference between the two lines. This difference highlights the significance of the expenditure restraint required from the 2014-15 Budget. The 2014-15 Budget estimates over the four years contain significant savings initiatives that have been introduced in this Budget and previous Budgets. New savings introduced since the $1.5 billion Sustainable Budget Commission savings in the 2010-11 Budget include:

- $430.7 million in the 2012-13 Budget
- $227.2 million in the 2012-13 MYBR
- $140 million in the 2013-14 Budget
- $1.5 billion in the 2014-15 Budget.

2.6.2 Operating revenues

The estimated result for 2013-14 expects GST revenue to be marginally more than budgeted and taxation revenue to decrease marginally. Over the forward estimates both these revenue lines are expected to grow in real terms. GST revenue has now shown to be highly sensitive to household spending patterns. State taxation also varies with economic activity and demand for housing.

GST revenue in 2013-14 is estimated at $4.6 billion, representing 30% 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 growth in State taxation and royalties revenue relative to other States and the distribution of Commonwealth National Partnership Agreement funding amongst the States.

The two main elements of State taxation are payroll tax and conveyance duty. Growth in payroll tax is based on the outlook for employment and wages growth. For conveyance duty, the level of property transfers is expected to return to their long-term trend levels by 2016-17 and property prices are expected to grow modestly each year.

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 1996-97 the annual growth in conveyance duty revenue has ranged from negative 20% 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 2003-04 and expected changes over the forward estimates.

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

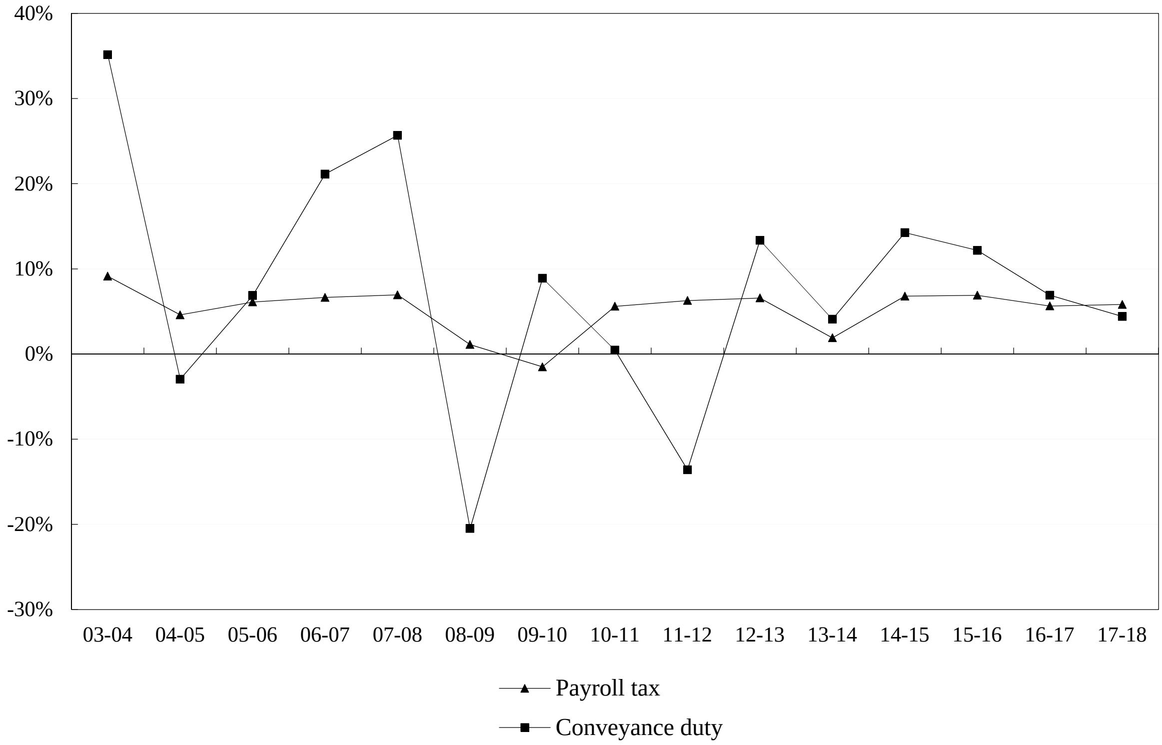


Chart 2.9 shows the relative stability of payroll tax growth over the period in comparison to the significant fluctuations in conveyance duty. Conveyance duties are a volatile revenue stream that is sensitive to both transaction levels and transaction prices. The chart also demonstrates that, over the forward estimates, conveyance duty is expected to increase each year. Strong growth is expected in 2014-15 and 2015-16 of 14.3% and 12.2% respectively, with lower levels of growth in the final two estimate years.

The 2014-15 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 change 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 $50 million p.a.
- a variance of 1% in State taxation revenue equates to about $45 million p.a.
- a 1% variation in property values equates to about $10 million in conveyance duty revenue
- a 1% variation in transactions equates to about $8 million in conveyance duty revenue.

2.6.3 Operating expenses

Consistent with recent past Budgets, the 2014-15 Budget expects significant restraint in spending. Nominal growth in employee expenses is expected to be virtually zero in both 2014-15 and 2015-16, and contained to 1% and 2.8% in 2016-17 and 2017-18.

Salaries and wages remain the main public sector operating cost. The Budget records that enterprise bargaining negotiations have been completed or 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 $260 million in 2017-18. The Budget states that the Government will limit future wages growth to 2.5% p.a. and if real wage restraint cannot be achieved, further FTE reductions and savings may be required in future Budgets to maintain the fiscal position.

The Budget Papers provide summary details of parameter and policy changes that occur between Budgets. 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.

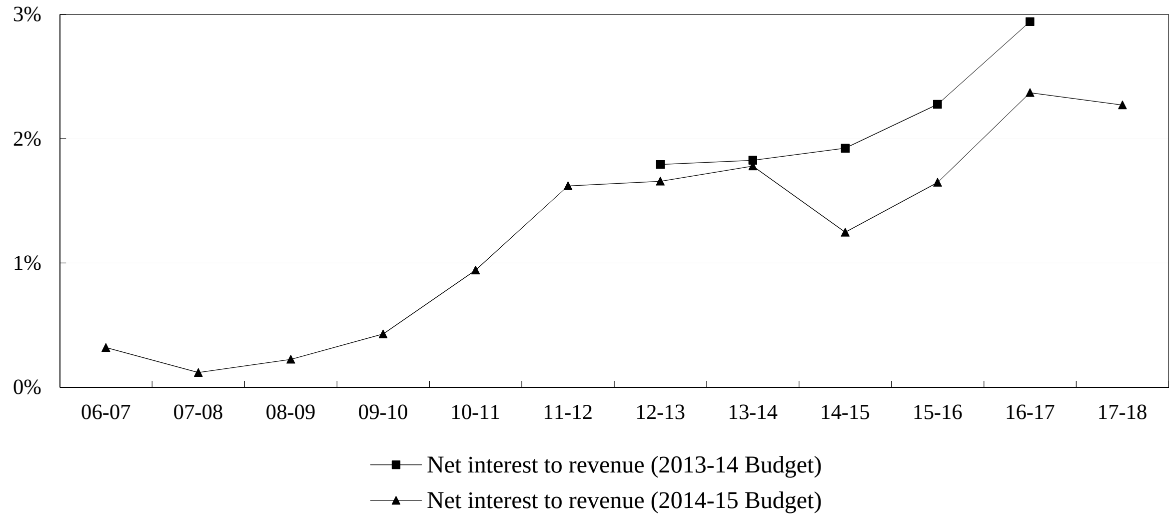
Parameter effects since the 2013-14 Budget have reduced operating expenses by $751 million (before provisions) over the four years to 2016-17. This reduction is primarily due to a reduction in interest expense due to the change in SA Water gearing level from 2014-15 reducing general government sector net debt in 2014-15. The reduction in interest expense over the three years from 2014-15 is $749 million.

The 2014-15 Budget reports that policy decisions since the 2013-14 Budget have added $518 million (before provisions) to operating expenses over the four years to 2016-17. 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.

2.6.4 Ratio of interest to revenue

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 2013-14 and 2014-15 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 through to 2013-14.

The differences in the ratio between the 2013-14 Budget and the 2014-15 Budget are primarily due to the SA Water gearing change, which will reduce general government debt by $2.7 billion in 2014-15.

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).

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 $45 million in 2014-15, rising to $53 million in 2017-18.

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.

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 a 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.

- The 2014-15 Budget introduces a return to major savings measures amounting to $1.5 billion over the four years of the Budget. This is made up of operating savings of $1.2 billion and investing savings of $290 million.

I note that the 2014-15 Budget savings include an initiative to save $189 million over three years by reforming procurement arrangements undertaken by agencies. The Budget indicates that this saving is to be allocated to agencies during 2014-15. I intend, as part of the 2014-15 audit coverage, to review the nature of the procurement reform, including the realisation strategies to be implemented and savings allocation methodology to be adopted.

Savings introduced since the 2010-11 Budget now exceed the significant savings initiatives set in that Budget arising from the work of the Sustainable Budget Commission. The details of savings by individual agency and individual savings measures introduced in the 2014-15 Budget are provided in 2014-15 Budget Paper 6 ‘Budget Measures Statement’.

Table 8.4 in Chapter 8 of this Report provides details of savings by portfolio for the 2010-11 Budget initiatives.

Previous Reports have emphasised that 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 2014-15 Budget introduces significant additional savings for this portfolio. Table 2.4 of 2014-15 Budget Paper 3 ‘Budget Statement’ identifies additional total operating savings of $532.7 million for Health and Ageing. This includes $332 million specifically identified for reduction in hospital beds or other health service reductions.

The Budget notes that, with the exception of Health and Ageing, agencies have delivered budgeted savings and agency savings budgeted to commence in 2013-14 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 MYBR also made some adjustments to the savings targets. Table 8.8 in Chapter 8 of this Report provides a summary of the Health and Ageing savings task, including adjustments made to savings targets.

I have commented in previous Reports that an inherent risk of the saving strategy of government is its sheer size and breadth. This risk is still applicable and even heightened given a number of factors, including:

- the growth in the savings ask of agencies since the 2010-11 Budget – the 2014-15 Budget alone introduces $1.5 billion in additional savings
- in the past Health and Ageing has not met its full quota of savings targets and the 2014-15 Budget introduces significant additional savings for this portfolio. The achievement of the current level of Health and Ageing savings presents a very difficult challenge and poses a significant risk to achieving the Budget strategy
- some new savings strategies are subject to further analysis and refinement, including the method of savings allocation.

Achieving the savings task requires significant discipline and presents ongoing risks including industrial action, public demand to maintain services, unsatisfactory administrative performance and budget management oversight complexity.

2.6.6 Full-time equivalents reduction management strategy

A key part of the savings strategy in budgets since 2010-11 has involved reduction in public sector FTEs. For example, the 2010-11 Budget included a reduction of 3743 FTEs, excluding increases from other initiatives, and the 2012-13 Budget introduced a savings initiative to reduce a further 1000 FTE staff.

The 2014-15 Budget notes that FTEs in the general government sector are estimated to decrease by 4080 between 30 June 2014 and 30 June 2018, reflecting the cumulative impact of savings measures partially offset by new expenditure measures.

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 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 the TVSP scheme remains available for workforce reductions associated with specific measures. The 2013-14 Budget noted that, from 1 July 2014, the maximum TVSP payout will be reduced from 116 weeks pay to 52 weeks pay.

The 2014-15 Budget states that FTE reductions can also be achieved in other ways (eg natural attrition, not filling vacancies and not renewing contracts). Further, the Budget notes that after 30 June 2014, a public sector employee who has been identified by their agency as excess and who has been unsuccessful in finding alternative public sector employment, will be able to be separated with an appropriate financial package, having regard to applicable legislation and industrial provisions.

DTF has advised Audit that between 1 November 2010 and 30 June 2014 2866.6 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 2013-14 Audit sought an update of FTE monitoring arrangements and data as at 30 June 2014. DTF's response, based on data received from major agencies, showed that overall agencies were estimating they would be 842 FTEs below their budgeted FTE levels as at 30 June 2014. The overall position comprised various agencies being over and under their cap. For example:

- the Department for Health and Ageing has reported that actual FTEs were 75 FTEs above its cap primarily due to a slightly higher than cap result in the health units
- the Department of Further Education, Employment, Science and Technology reported actual FTEs of 237 FTEs below its cap mainly due to earlier than budgeted separation of employees in TAFE SA
- South Australia Police reported actual FTEs of 129 FTEs below its cap mainly due to delays in recruitment of sworn officers and the timing of recruitment of sworn officers and cadets.

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

Comment is made in 2014-15 Budget Paper 3 'Budget Statement' that an adjustment was made to the Department for Health and Ageing's FTE cap reflecting improved information on staffing levels. DTF advised that the adjustment includes two components. Firstly, FTE reductions associated with savings measures in Health and Ageing have historically been based on the agency's ratio of total employee expenses to total budget at average salary level. The adjustment to the FTE cap during 2013-14 reflects the replacement of historically calculated FTE reductions with specific FTE savings measures now being implemented for Health and Ageing. The adjustment reflects that fewer savings have applied to frontline service areas than would have been implicit in the initial estimate. Secondly, the adjustment includes re-alignment of the FTE cap to the approved expenditure budget for employee entitlements across the portfolio. I intend, as part of the 2014-15 audit coverage, to gain an understanding of the reasonableness of the basis of the FTE cap adjustment.

2.6.7 Capital payments

For the period 2009-10 to 2012-13 the State has achieved capital expenditure in the general government sector exceeding $2 billion annually in every year except 2011-12 ($1.9 billion). The estimated level of capital expenditure for 2013-14 is $1.6 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 2013-14 to 2014-15 and future years are $254 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. Purchases of non-financial assets are projected to be over $1 billion for all four years of the 2014-15 Budget. The Budget includes a slippage allowance for 2014-15 of $160 million, compared to $210 million in the previous year.

The capital program also comprises large projects with inherent complexities and risks. Over the four years to 2017-18 capital spending includes $1.3 billion on road projects, $295.7 million on major public transport projects, $283.1 million on the redevelopment of major metropolitan and regional hospitals and $166.3 million on education projects.

2.6.7.1 New Royal Adelaide Hospital - Public Private Partnership project

In June 2011 the Government announced financial close on a contract with the SA Health Partnership (SAHP) consortium 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 2017-18 are estimated to be $597 million.

The majority of the sales of non-financial assets are expected in 2014-15 ($389 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.

2.6.8 Budget monitoring

The critical importance of strong monitoring of budget progress has been continually emphasised in previous Reports. DTF advised Audit of specific measures in place for 2013-14. They were consistent with 2012-13 and include monthly monitoring of financial performance and quarterly monitoring of capital projects, savings measures and FTEs.

Further, monitoring reports continued to be provided to the BRCC (formerly the SBCC) based on information supplied by agencies and analysis prepared by DTF.

DTF advised that the existing monitoring regime will continue in 2014-15, with monitoring reports provided to the Senior Management Council and the BRCC.

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.

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 reprofile the Department for Health and Ageing's budget savings task. The aim was to provide Health and Ageing with additional resources for a more even annual build-up of savings to enable it to achieve its aggregate savings target by 2014-15.

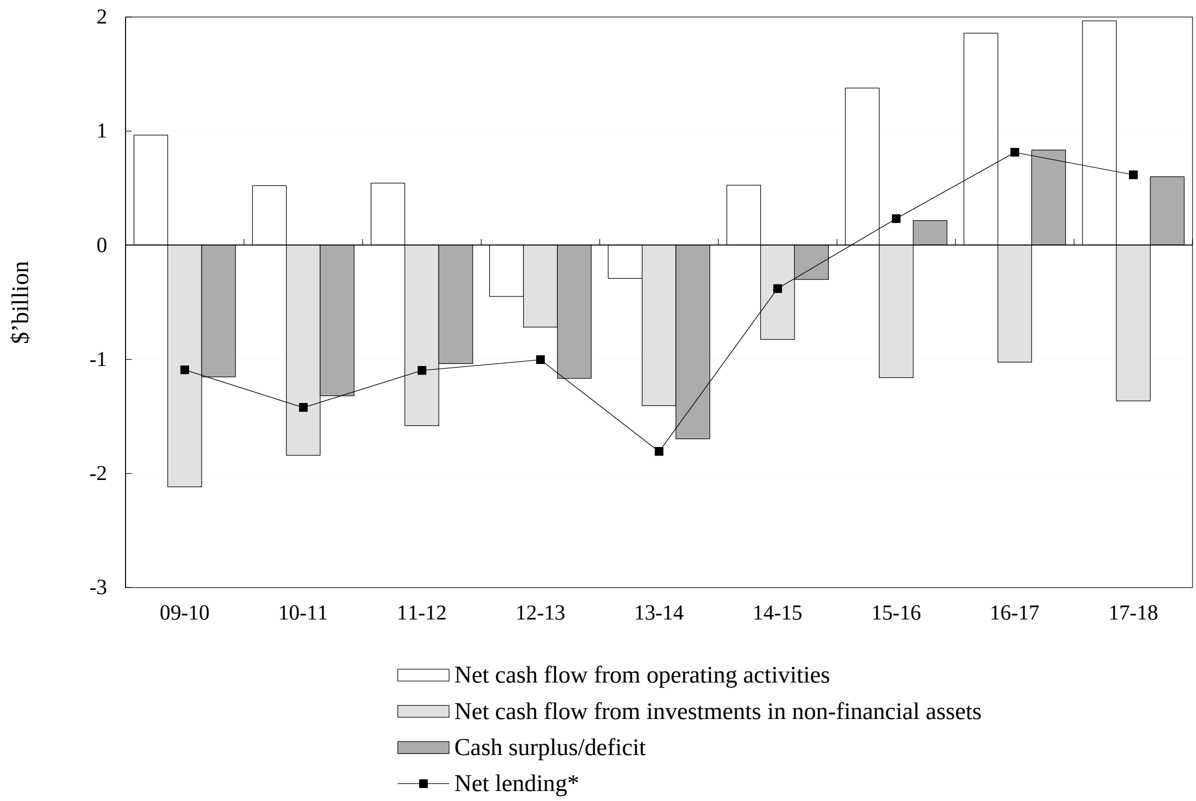
The Government reassessed the level and timing of budget improvement it considered Health and Ageing could deliver across the forward estimates. This resulted in a reduction, totalling $523.2 million, to the Health and Ageing's budget savings target over the forward estimates in the 2012-13 MYBR. The 2014-15 Budget introduced additional savings of $532.7 million for the Health and Ageing portfolio.

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. Table 8.8 in Chapter 8 demonstrates that the annual savings task for Health and Ageing is subject to significant annual growth, reaching a cumulative annual savings amount of $766.2 million in 2017-18. This will present an enormous challenge to deliver the future savings. A major component of the targeted savings is potential savings requiring further analysis and refinement. A number of these savings measures may be subject to separate Cabinet approval.

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 2014 and the expected cash flow over the four years of the 2014-15 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 actual or estimated negative net operating cash flows in 2012-13 and 2013-14 before a return to expected positive cash flows in 2014-15 and subsequent years of the 2014-15 Budget. This improvement results in cash surpluses from 2015-16. 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 2014-15 Budget states that it has been framed in the context of the challenge of ongoing domestic and international fluctuations and a need to respond to the fiscal challenge posed by Commonwealth Budget reductions. The Budget also notes that the impending closure of manufacturing operations by GM Holden Ltd and Toyota Motor Corporation will impact South Australia’s economy and employment. Some key elements of the 2014-15 Budget include:

- new expenditure savings initiatives of $1.5 billion
- removal of Emergency Services levy remissions realising $355.8 million in revenue
- realisation of proceeds of $500 million from MAC from opening the provision of CTP insurance to the private sector from 1 July 2016

- suspension of three hospital capital expenditure projects
- changes to the capital structure of SA Water in 2014-15, resulting in decreased general government sector net debt of $2.7 billion.

In the general government sector, the Budget contains new operating initiatives totalling $471.4 million and new investing initiatives totalling $985.1 million. These significant initiatives have been offset by new operating and investing savings, revenues from external sources associated with the new initiatives and the use of provisions made in earlier Budgets.

The general government sector net debt is estimated to increase to $6.9 billion at 30 June 2014, falling to $5.3 billion as at 2017-18. In 2015-16 net debt rises to $7.1 billion as it includes the effect of accounting for the new Royal Adelaide Hospital. The reduction in net debt in the general government sector in 2014-15 is attributable to the SA Water debt restructure of $2.7 billion.

Revenues are estimated to improve consistently over the four years of the 2014-15 Budget. Audit analysis indicates that a deteriorating gap between past average experience and the 2014-15 Budget estimates for key revenue lines emerges in 2015-16 and is sustained over the final two estimate years. GST revenue has 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.

Audit analysis of the trend of key estimated expenses for the 2014-15 Budget with past average experience shows a diverging difference. The trend of these expenses based on past average experience is significantly above the 2014-15 Budget estimated expenses. This difference highlights the significance of the expenditure restraint required in the 2014-15 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.

Savings introduced since the 2010-11 Budget now exceed the significant savings initiatives set in that Budget arising from the work of the Sustainable Budget Commission. Previous Reports have emphasised that 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 2014-15 Budget introduces significant additional savings for this portfolio of $532.7 million, including $332 million specifically identified for reduction in hospital beds or other health service reductions.

The 2014-15 Budget estimates purchases of non-financial assets to be $1.2 billion in 2014-15. Purchases are expected to be over $1 billion for each of the three remaining years of the forward estimates. This presents a continuing heightened risk to the proper management and control of capital projects.

In summary, since the global financial crisis in 2008-09, successive budgets have made significant downward revisions to key revenue items (GST revenue and State taxation revenue). Since this time the Government has responded by identifying major saving initiatives, including $1.5 billion in the 2010-11 Budget and $1.5 billion in the 2014-15 Budget.

Recent Budgets have also responded to the budget situation through the realisation of proceeds from the sale of significant government assets such as ForestrySA ($635.1 million) and SA Lotteries ($402.8 million). The 2014-15 Budget includes an initiative to realise $500 million from MAC.

The 2014-15 Budget projects a return to a net operating surplus of $406 million in 2015-16 and a return to a net lending surplus of $814 million in 2016-17. Further, the Budget expects significant net operating surpluses in 2016-17 and 2017-18. This improvement is based on expected growth in GST and State taxation revenue and achievement of a significantly increased savings program. The risk remains that economic uncertainty will see revenue pressures re-emerge in key areas. Further, past experience indicates that the Health and Ageing portfolio will face significant challenges in achieving its increased savings targets, a significant component of the overall government savings measures.

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 issued pursuant to the PFAA.

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

3.2 Uniform presentation framework

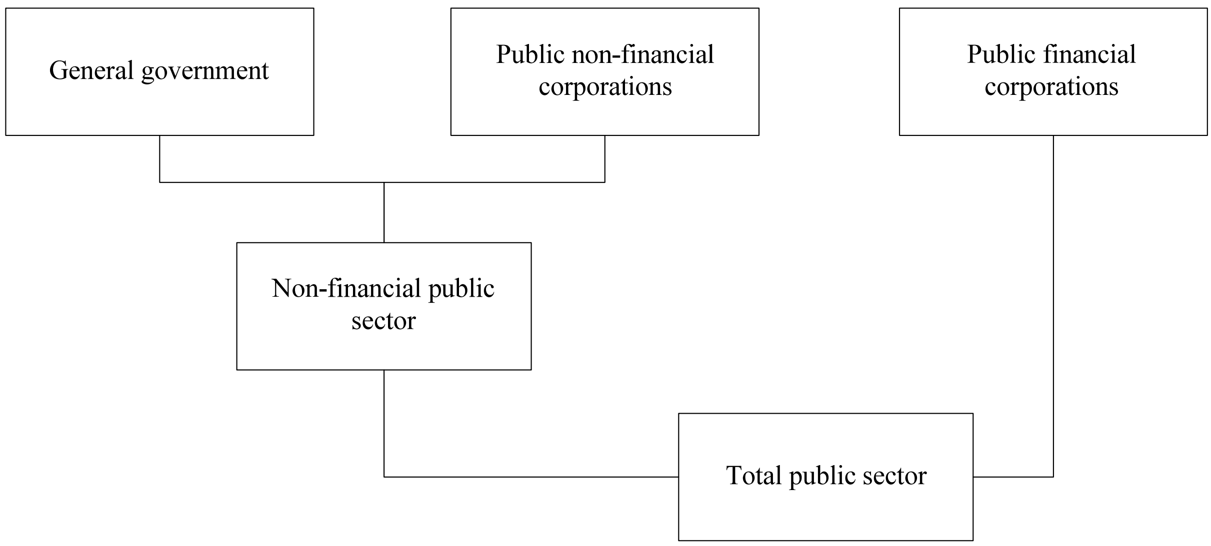
3.2.1 Background

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 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.

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.

- ***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]

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[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 2014-15 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 historical 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 Budgetary reporting in general purpose financial statements

Over a number of years, the AASB worked towards the objective of harmonising generally accepted accounting principles and the GFS. This project, which was developed in phases, aimed to develop requirements for a single set of financial reports that are auditable, comparable between jurisdictions, and in which the outcome statements are directly comparable with the relevant budget statements. The project was undertaken in response to a direction from the Financial Reporting Council.

The Financial Reporting Council subsequently withdrew its direction to harmonise generally accepted accounting principles and GFS for entities within the general government sector. However, the AASB concluded that there was still merit in 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 AASB 1055 Budgetary Reporting in 2013. This standard applies to reporting periods beginning on or after 1 July 2014. AASB 1055 requires not-for-profit entities within the general government sector whose budgeted financial statements are presented to Parliament to disclose:

- original budgeted amounts, presented and classified on a basis that is consistent with the financial statements prepared in accordance with AASs
- explanations of major variances between the original 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 such budget information is presented to Parliament.

These requirements in AASB 1055 will also apply to the general government sector financial statements and the whole-of-government financial statements, replacing budgetary reporting requirements previously held in AASB 1049.

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 2014-15 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 35%.

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 a net operating surplus of $406 million in 2015-16, with deficits expected in the preceding two years.

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 35%. General government sector net debt is expected to decrease from $6.9 billion as at 30 June 2014 to $5.3 billion as at 30 June 2018. The estimated decrease in net debt is a result of transferring debt to the PNFC sector (SA Water) from the general government sector. As at 2015-16 the ratio is 41.4%, which exceeds the debt fiscal target of a maximum ratio of 35%. This is largely due to the increase in debt associated with the new Royal Adelaide Hospital which will be recognised in the State's balance sheet in 2015-16. By 30 June 2018 the ratio of net debt to revenue is expected to fall to 28.2%.

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. Deliver budget surpluses building to at least 1% of GDP by 2023-24. Improving the Government's net financial worth over the medium-term.

4 2014-15 Budget Paper 3 'Budget Statement', page 9.

Jurisdiction	Budget fiscal objective/strategy[(a)(b)]
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. Achieve and maintain a general government sector fiscal balance. 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 net operating surpluses over the medium term. Prudently manage the ACT's balance sheet. Make targeted investments to achieve economic growth. Maintain taxation revenues at sustainable levels. Continue to plan for the delivery of high quality services to meet the needs of the ACT community. Fully fund the Territory's unfunded superannuation liability by 2030. Maintain a AAA credit rating.
Tas	Redirect government spending to investments that boost productivity and participation. Reduce the Government's share of the economy over time. Strengthen the Government's balance sheet over time to be able to respond to any future external shocks.
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 2013-14

5.1 Overview

The following section summarises the estimated operating results for 2013-14.

5.2 2013-14 estimated results

5.2.1 General government sector

The estimated result for the year is a net operating deficit of $1232 million (budget $911 million deficit) and net lending deficit (borrowing) of $1808 million (budget $1455 million). The following table shows 2012-13 financial year data and differences between the estimated result and budget for 2013-14.

Table 5.1 – General government budget comparisons 2012-13 to 2013-14

Revenue:	2012-13 Actual $'million	2013-14 Budget $'million	2013-14 Estimated result $'million	Difference to budget $'million	Difference to budget %
Taxation revenue	4 104	4 206	4 121	(85)	(2)
Grants:					
Current	7 354	7 590	7 642	52	1
Capital	315	293	213	(81)	(27)
Sale of goods and services	2 115	2 077	2 199	122	6
Interest income	134	102	33	(69)	(68)
Dividend and income tax equivalent income	446	328	375	47	14
Other	865	669	673	4	1
Total revenue	15 333	15 265	15 254	(11)	-
Less: **Expenses:**					
Employee expenses	7 105	7 155	7 258	103	1
Superannuation expenses:					
Superannuation interest cost	314	434	468	34	8
Other superannuation expenses	675	754	781	27	4
Depreciation and amortisation	762	895	864	(31)	(3)
Interest expenses	386	379	304	(75)	(20)
Other operating expenses	4 313	3 975	4 210	235	6
Grants	2 726	2 585	2 601	16	1
Total expenses	16 282	16 176	16 487	311	2
Net operating balance	(948)	(911)	(1 232)	(321)	35
Less: **Net acquisition of non-financial assets:**					
Purchases of non-financial assets	2 008	1 858	1 567	(291)	(16)
Less: Sales of non-financial assets	1 197	419	127	(292)	(70)
Less: Depreciation	762	895	864	(31)	(3)
Plus: Change in inventory	7	-	-	-	-
Plus: Other movements in non-financial assets	-	-	-	-	-
Total net acquisition of non-financial assets	55	544	576	32	6
Net lending (borrowing)	(1 003)	(1 455)	(1 808)	(353)	24

Note: Totals may not add due to rounding.

The 2013-14 Budget anticipated a net operating deficit of $911 million for 2013-14, a marginal improvement on the net operating deficit of $948 million experienced in 2012-13.

The estimated result for 2013-14 shows a $321 million deterioration from budget, leading to a net operating deficit of $1232 million. This deterioration from budget is impacted by the estimated $103 million increase in employee expenses and $235 million increase in other operating expenses. Explanations for these movements are provided in 2014-15 Budget Paper 3 'Budget Statement', page 30.

Total revenue, while impacted by decreases in taxation and interest revenue, remains largely on budget due to improvements compared to budget in revenue from the sale of goods and services and dividend revenue from PNFCs and PFCs.

5.2.1.1 Net acquisition of non-financial assets

The 2013-14 estimated result for purchases of non-financial assets of $1567 million is $291 million below the 2013-14 Budget.

Table 5.2 shows that, consistent with the high value of capital spending, some large adjustments were made in the course of 2013-14. The original Budget was increased predominately by carryovers from 2012-13 totalling $174 million.

The estimated result for 2013-14 allows for mid-year budget adjustments and carryovers beyond the year. Carryovers into 2014-15 and beyond of $254 million include $84 million for road and rail infrastructure programs. 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 2013-14 estimated result

	$'million	$'million
2013-14 Budget		1 858
Policy decisions		(20)
Parameter variations:		
Carryovers from 2012-13	174	
Adjustment to capital slippage provision (Net adjustment from MYBR and Budget)	(110)	
Carryovers into 2014-15 and forward years	(254)	
Significant project reprofiles	(150)	
Use of provisions set aside in the 2013-14 Budget and the 2013-14 MYBR	(1)	
Other (includes reclassifications to operating and contingency adjustments)	70	(271)
2013-14 estimated result		1 567

Note: Totals may not add due to rounding.

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 $2100 million, which is $329 million more than budget for the year.

The following table summarises the position.

Table 5.3 – NFPS Budget comparisons 2012-13 to 2013-14

	2012-13 Actual $'million	**2013-14 Budget $'million**	**2013-14 Estimated result $'million**	Difference to budget $'million	Difference to budget %
Revenue	16 494	16 367	16 328	(39)	-
Less: **Expenses**	17 152	17 515	17 784	269	2
Net operating balance	(657)	(1 148)	(1 457)	(309)	27
Less: **Net acquisition of non-financial assets**	64	623	643	20	3
Net lending (borrowing)	(721)	(1 771)	(2 100)	(329)	19

Note: Totals may not add due to rounding.

The increase in the net lending deficit (borrowing) of $329 million is largely driven by the deterioration in the general government sector's result (refer table 5.1 in this Chapter).

6 Budget 2014-15 overview

6.1 Overview

The following commentary focuses on the trends arising from the 2014-15 Budget. It provides an overview of:

- the Budget for 2014-15 having regard to the estimated result for 2013-14
- a longer term view of the forecast results going forward to 2017-18.

6.1.1 Matters of significance to the 2014-15 Budget

A net operating deficit of $1232 million is expected in 2013-14. This represents a $321 million decline from the position estimated in the 2013-14 Budget, due largely to upward revisions in operating expenses of $329 million.

A net operating deficit is also expected in 2014-15, with the 2014-15 Budget projecting a return to a net operating surplus of $406 million for 2015-16. This is a $31 million improvement on the 2015-16 net operating surplus previously predicted in the 2013-14 Budget.

Net lending deficits are projected for the next two years, peaking at $2587 million in 2015-16. 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 2014-15 Budget estimates years are:

- new operating and investing initiatives totalling $1457 million over the next four years[5], including the use of $118 million of specific provisions held as contingency provisions in previous Budgets

- targeted savings, revenue offsets and reductions in capital programs totalling $1494 million over four years[6]

- expenditure restraint compared to revenue growth projected to lift the net operating balance to $883 million by 2017-18

- general government sector net debt decreasing by $1618 million to $5269 million by June 2018. This decrease is largely driven by the decision to change the capital structure of SA Water.

Budgeted total revenues and expenses for 2014-15 are both consistent with the estimates in the 2013-14 Budget.

6.2 General government sector – Operating statement

Table 6.1 below sets out the differences between the 2014-15 Budget and the estimated results for 2013-14.

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5 2014-15 Budget Paper 3 ‘Budget Statement’, table 2.1.
6 2014-15 Budget Paper 3 ‘Budget Statement’, table 2.1.

Table 6.1 – GFS – General government sector budget comparison of 2013-14 estimate results and 2014-15 Budget

Revenue:	2013-14 Estimated result $'million	2014-15 Budget $'million	Difference $'million	Difference %
Taxation revenue	4 121	4 524	403	10
Grants:				
Current grants	7 642	8 000	358	5
Capital grants	213	269	57	27
Sale of goods and services	2 199	2 282	83	4
Interest income	33	32	(1)	(3)
Dividend and income tax equivalent income	375	256	(119)	(32)
Other	673	704	31	5
Total revenue	15 254	16 067	813	5
Less: **Expenses:**				
Employee expenses	7 258	7 268	10	-
Superannuation expenses:				
Superannuation interest cost	468	443	(25)	(5)
Other superannuation expenses	781	796	15	2
Depreciation and amortisation	864	927	63	7
Interest expenses	304	232	(72)	(24)
Other operating expenses	4 210	4 254	44	1
Grants	2 601	2 626	25	1
Total expenses	16 487	16 547	59	-
Net operating balance	(1 232)	(479)	754	(61)
Less: **Net acquisition of non-financial assets:**				
Purchase of non-financial assets	1 567	1 217	(350)	(22)
Less: Sales of non-financial assets	127	389	262	206
Less: Depreciation	864	927	63	7
Total net acquisition of non-financial assets	576	(99)	(675)	(117)
Net lending (borrowing)	(1 808)	(380)	1 429	(79)

Note: Totals may not add due to rounding.

The major differences for the 2014-15 year are:

- an increase in State taxation revenue of $403 million, due mainly to a $279 million increase in property related taxes
- a $358 million increase in revenue from current grants, predominately GST revenue grants from the Commonwealth
- a $119 million decrease in dividends and income tax equivalent income, from other State entities outside the general government sector, largely reflecting an estimated reduction in distributions from SA Water
- a decrease in interest expenses of $72 million, reflecting the SA Water gearing change that will reduce general government net debt by $2.7 billion
- a decrease in the purchase of non-financial assets reflecting the decline in general government investing expenditure as a number of significant projects near completion.

More detail of the factors influencing the 2014-15 Budget is considered in the context of the longer term trends discussed later in this Report.

6.2.1 Reconciliation of variations since 2013-14 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 2013-14 Budget that affect the net operating balance and provisions used to offset some of those changes.[7]

Table 6.2 – Reconciliation of general government sector net operating balance

	2013-14 Estimated result $'million	2014-15 Budget $'million	2015-16 Estimate $'million	2016-17 Estimate $'million
2013-14 Budget	(911)	(431)	375	661
Parameter and other variations:				
Revenue - taxation	(85)	(46)	(103)	(174)
Revenue - other	79	(35)	(189)	(299)
Operating expenses	(103)	208	268	378
Net effect of parameter and other variations	**(109)**	**127**	**(24)**	**(95)**
Policy measures:				
Revenue - taxation	-	92	86	86
Revenue - other	(22)	(93)	(149)	(211)
Revenue - offsets	16	125	194	234
Operating expenses	(226)	(305)	(81)	94
Net effect of policy measures	**(232)**	**(181)**	**50**	**203**
Use of provisions set aside in the 2013-14 Budget and the 2013-14 MYBR:				
Operating expenses	18	8	5	6
2014-15 Budget	**(1 232)**	**(479)**	**406**	**776**

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

6.2.1.1 Revenue variations

Table 6.2 includes the expected reduction in Commonwealth funding announced in the 2014-15 Commonwealth Budget. The Commonwealth reductions form the major part of the total $475 million reduction in revenue policy (other) variations over the four years to 2016-17. Further details on these reductions are provided in 2014-15 Budget Paper 3 'Budget Statement', table 3.2.

Table 6.2 also identifies 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.

[7] 2014-15 Budget Paper 3 'Budget Statement', table 1.12.

The following table shows the components of revenue parameter changes.[8]

Table 6.3 – Revenue parameter changes

	2013-14 Estimated result $'million	2014-15 Budget $'million	2015-16 Estimate $'million	2016-17 Estimate $'million
Commonwealth specific purpose and National Partnership grants:				
Special purpose	(2)	10	6	(14)
National Partnership	(39)	(5)	(94)	(46)
GST revenue grants and transitional assistance	23	17	(25)	(66)
Property related taxes	(7)	24	(7)	(59)
Other State taxes	(77)	(70)	(94)	(115)
Dividends and income tax equivalents	45	(116)	(79)	(120)
Interest income	(69)	(94)	(130)	(170)
Other	123	153	133	118
Total	(6)	(81)	(292)	(473)

Note: Totals may not add due to rounding.

In particular table 6.3 shows the downward revisions, since the 2013-14 Budget, in State taxes, dividends and income tax equivalents and interest income.

The downward revision in other State taxes is due mainly to revisions in the anticipated level of payroll tax, reflecting revisions in the expected growth of both employment and wages.

The downward revision in interest income across the forward estimates reflects the impact of netting off of interest received from the Treasurer's funds deposited with SAFA against interest payable on the Treasurer's borrowings.

The downward revision across the forward estimates for dividends and income tax equivalents largely reflects the decrease in SA Water's budgeted profit as a result of additional interest and guarantee fees expense, following the $2.7 million increase in its debt profile. Distributions across the forward estimates are also expected to reduce arising from changes in the forecast timing of proposed land and commercial property sales by the Urban Renewal Authority (Renewal SA).

6.2.1.2 Operating expense variations

Table 6.2 shows that parameter effects are estimated to reduce operating expenses by $751 million over the four years to 2016-17.

Policy spending decisions since the 2013-14 Budget, however, add a further $518 million to operating expenses over the same period, $226 million of which is for 2013-14.[9] 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

	2009-10 $'million	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million
Policy measure operating expenses	344	125	199	352	226

[8] 2014-15 Budget Paper 3 'Budget Statement', table 1.14 and 2013-14 MYBR, table 1.6.
[9] 2014-15 Budget Paper 3 'Budget Statement', table 1.12.

Table 6.4 shows that $1246 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, the policy expense adjustments of $226 million since the 2013-14 Budget significantly contribute to the deterioration in the estimated net operating deficit for 2013-14 to $1232 million.

6.3 Public non-financial corporation sector – Operating statement

A net operating deficit of $208 million is budgeted in 2014-15, a slight improvement from the estimated result for 2013-14.

The net lending deficit is budgeted to marginally improve to $280 million in 2014-15, due mainly to this net operating deficit. The differences between the two years are set out in the following table.

Table 6.5 – GFS – PNFC budget comparison 2013-14 and 2014-15

Revenue:	2013-14 Estimated result $'million	2014-15 Budget $'million	Difference $'million	Difference %
Sale of goods and services	1 667	1 805	138	8
Other	644	614	(30)	(5)
Total revenue	2 311	2 419	108	5
Less: **Expenses:**				
Employee expenses	193	200	7	4
Superannuation expenses	24	25	1	4
Depreciation and amortisation	429	439	10	2
Interest expenses	220	328	108	49
Other property expenses	300	222	(78)	(26)
Other operating expenses	1 226	1 273	47	4
Other expenses	144	140	(4)	(3)
Total expenses	2 536	2 627	91	3
Net operating balance	(224)	(208)	17	(8)
Less: **Net acquisition of non-financial assets:**				
Purchase of non-financial assets	653	658	5	1
Less: Sales of non-financial assets	218	194	(24)	(11)
Depreciation	429	439	10	2
Add: Change in inventories	61	47	(14)	(23)
Total net acquisition of non-financial assets	67	72	5	8
Net lending (borrowing)	(292)	(280)	12	(4)

Note: Totals may not add due to rounding.

6.4 Non-financial public sector – Operating statement

The 2014-15 budgeted result for the NFPS is a net operating deficit of $686 million, an improvement of $770 million from the 2013-14 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

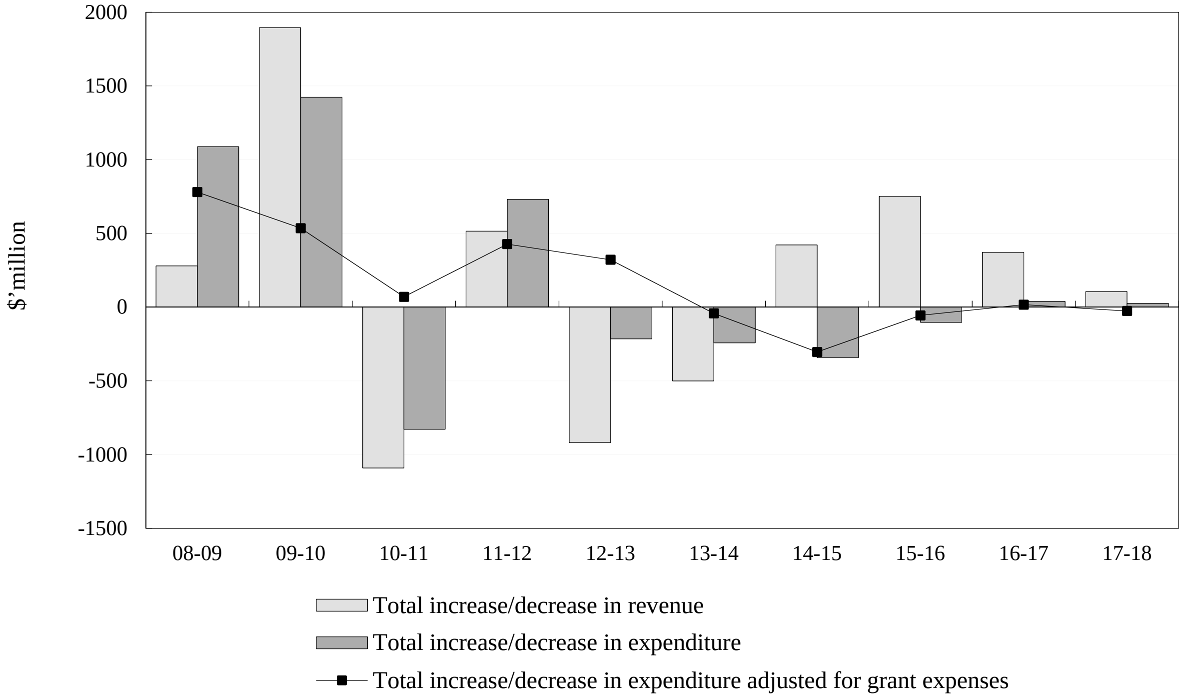
	2008-09 Actual $'million	2009-10 Actual $'million	2010-11 Actual $'million	2011-12 Actual $'million	2012-13 Actual $'million	2013-14 Est. result $'million	2014-15 Budget $'million	2015-16 Estimate $'million	2016-17 Estimate $'million	2017-18 Estimate $'million
Revenue:										
Taxation revenue	3 537	3 649	3 831	3 854	4 104	4 121	4 524	4 795	5 020	5 236
Grants:										
Current	6 651	7 039	7 109	7 465	7 354	7 642	8 000	8 487	9 165	9 442
Capital	598	1 841	1 076	1 204	315	213	269	577	455	425
Sales of goods and services	1 697	1 936	1 879	2 015	2 115	2 199	2 282	2 353	2 441	2 513
Interest income	150	138	168	172	134	33	32	35	37	39
Dividend and income tax equivalent income	382	433	403	385	446	375	256	298	261	271
Other	517	497	550	811	865	673	704	713	711	732
Total revenue	13 531	15 534	15 017	15 905	15 333	15 254	16 067	17 258	18 090	18 659
Less: **Expenses:**										
Employee expenses	5 749	6 221	6 400	6 770	7 105	7 258	7 268	7 271	7 347	7 554
Superannuation expenses:										
Superannuation interest cost	383	455	427	407	314	468	443	436	429	420
Other superannuation expenses	580	600	621	666	675	781	796	798	807	820
Depreciation and amortisation	566	633	670	718	762	864	927	990	1 065	1 084
Interest expenses	180	204	308	427	386	304	232	319	465	462
Other operating expenses	3 624	3 695	3 824	3 993	4 313	4 210	4 254	4 396	4 470	4 579
Grants	2 682	3 540	2 819	3 183	2 726	2 601	2 626	2 642	2 732	2 858
Total expenses	13 764	15 347	15 069	16 164	16 282	16 487	16 547	16 852	17 315	17 776
Net operating balance	(233)	187	(53)	(258)	(948)	(1 232)	(479)	406	776	883
Less: **Net acquisition of non-financial assets:**										
Purchases of non-financial assets	1 305	2 144	2 122	1 876	2 008	1 567	1 217	4 067	1 125	1 374
Less: Sales of non-financial assets	108	29	82	322	1 197	127	389	84	99	25
Less: Depreciation	566	633	670	718	762	864	927	990	1 065	1 084
Add: Change in inventories	7	3	0	3	7	0	0	0	0	0
Add: Other movements in non-financial assets	0	(206)	0	0	0	0	0	0	0	0
Total net acquisition of non-financial assets	639	1 279	1 370	839	55	576	(99)	2 993	(39)	266
Net lending (borrowing)	(872)	(1 092)	(1 422)	(1 098)	(1 003)	(1 808)	(380)	(2 587)	814	617

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 10 years to 2017-18.

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



(a) Estimated June 2014 values.
(b) 2009-10 and 2010-11 are influenced by Commonwealth stimulus grants.

Chart 6.1 demonstrates the responses to the global financial crisis, with 2009-10 showing the highest growth in revenues over the period due to additional Commonwealth stimulus money.

Revenue for 2010-11 was affected by the very large Commonwealth stimulus grants wind-down, with part of the decrease in expenses in 2010-11 showing the matching fall in related grant expenses. The decrease in revenues for 2012-13 reflected the timing of Commonwealth National Partnership payments.

Decreases in real revenue and expenses are estimated for 2013-14. Real revenue increases forecast for 2014-15 to 2017-18 are due mainly to forecast real increases in GST revenue grants and State taxation.

7 Revenue

Trend data in charts in this section is in real terms at estimated June 2014 values unless otherwise stated.

7.1 Revenue overview

Total general government sector revenues are estimated to be $15.3 billion in 2013-14, a decrease of $79 million from the previous year's result, and a real decrease of $499 million or 3.2%. In real terms total revenue is expected to increase by 11% by 2017-18.

While total revenue is estimated to increase over the forward estimates, the 2014-15 Budget highlights the significant decrease, relative to the 2013-14 Budget, in Commonwealth specific purpose payments and National Partnership funding. These reductions were announced in the Commonwealth Government's 2014-15 Budget.

State taxation revenue, while revised down since the 2013-14 Budget, is expected to increase by 15.1% by 2017-18 in real terms. This increase is due mainly to estimated increases in property taxes, driven by increases in conveyance duty, the removal of general remissions on the Emergency Services levy and the introduction of the new transport development levy from 2014-15.

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)

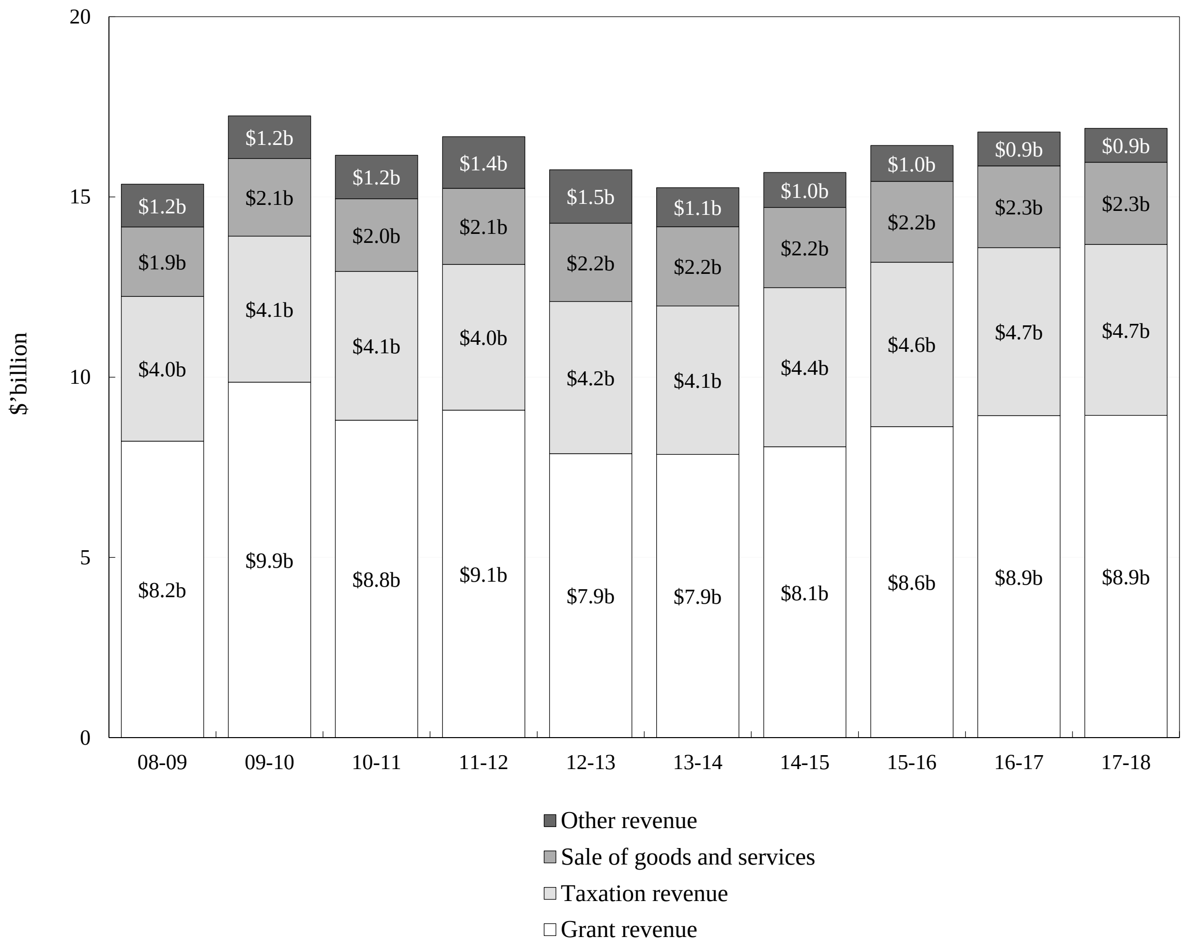


Chart 7.1 highlights the importance of Commonwealth grants to the State's revenues. Over most years Commonwealth grants represent about 50% of total revenue. During the period 2008-09 to 2011-12 Commonwealth revenue increased as a proportion of total State revenue, peaking at 55.9% in 2009-10. This increase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

This percentage declines to 49.2% 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 $15.3 billion (2013-14 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 2014-15 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 2017-18 and demonstrates a 28% increase (nominal) over that period.

Table 7.1 – Commonwealth grants 2013-14 to 2017-18 (nominal)

	2013-14 Est. result $'million	2014-15 Budget $'million	2015-16 Budget $'million	2016-17 Budget $'million	2017-18 Budget $'million
Current grant revenue					
GST revenue	4 618.2	4 956.3	5 315.2	5 813.6	6 062.9
National Partnership	450.1	346.0	312.7	320.3	212.0
National Partnership (on-passing)	113.4	155.6	154.0	153.2	158.9
Special purpose	1 485.7	1 636.4	1 752.6	1 875.2	1 965.1
Special purpose (on-passing)	729.6	764.3	811.1	861.2	901.3
Total current grant revenue	**7 397.0**	**7 858.6**	**8 345.6**	**9 023.5**	**9 300.2**
Capital grant revenue					
National Partnership	68.8	154.9	462.5	341.5	310.8
Special purpose	103.6	91.6	92.4	93.3	94.3
Special purpose (on-passing)	11.4	0.0	0.0	0.0	0.0
Other Commonwealth grants	4.2	4.9	3.1	3.1	3.1
Total capital grant revenue	**188.0**	**251.4**	**558.0**	**438.0**	**408.2**
Total Commonwealth grants	**7 585.0**	**8 110.0**	**8 903.6**	**9 461.5**	**9 708.4**

The 2014-15 Budget notes the reduced funding outcomes for South Australia arising from the Commonwealth Government's 2014-15 Budget, as compared to the information published in the Commonwealth Government's 2013-14 Mid-year Economic and Fiscal Outlook (MYEFO). The 2014-15 Commonwealth Budget comments that it will achieve savings of

$1.8 billion over four years from 2014-15 by ceasing the funding guarantees under the National Health Reform Agreement 2011 and revising Commonwealth public hospital funding arrangements from 1 July 2017. From 2017-18 the Commonwealth will index its contribution to hospitals funding by a combination of the CPI and population growth.

Table 3.1 of 2014-15 Budget Paper 3 'Budget Statement' identifies the Commonwealth reductions made to this funding and other areas as part of the 2014-15 Commonwealth Budget. The figures in the table for the years 2013-14 to 2016-17 have been determined by comparing funding amounts budgeted in the 2013-14 Commonwealth Government MYEFO with amounts budgeted in the 2014-15 Commonwealth Budget.

The 2017-18 figures in table 3.1 were calculated on the basis of applying indexation rates applicable at the time of the 2013-14 Commonwealth MYEFO to budgeted 2016-17 grant amounts. These were then compared to the 2017-18 amounts identified in the 2014-15 Commonwealth Budget to determine the impact of the change in Commonwealth policy.

7.2.1 GST revenue grants

GST revenue grants for 2013-14 are expected to be $23 million higher than the original budget estimate, reflecting an increase in the national GST pool estimated by the Commonwealth Treasury. The total GST pool is expected to increase by around 5.5% in 2013-14, compared to the Commonwealth's original budget estimate of growth of 5.3%.

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 2014 the Commonwealth Grants Commission released its 'Report on GST Revenue Sharing Relativities - 2014 Update' of per capita relativities for the distribution of GST revenue grants to the States in 2014-15.

The Commonwealth Grants Commission recommended an increased relativity for South Australia, which will receive 9.2% of the GST pool in 2014-15. This represents an increase of around 0.1 of a percentage point compared to 2013-14.

Over the forward estimates, South Australia's GST revenue grants are expected to grow by 7.2% in 2015-16, 9.4% in 2016-17 and 4.3% in 2017-18.

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.

In its original form the Intergovernmental Agreement on Federal Financial Relations provided for five national SPPs covering health, schools, disability, housing and skills and workforce development. From 1 July 2014 funding for national SPPs will be distributed on a per capita basis according to population estimates.

Two former SPPs have now been superseded. The National Health Reform funding replaced the National Healthcare SPP from 1 July 2012, while the National Schools SPP was replaced by the Students First program from 1 January 2014.

Since the 2013-14 Budget, SPP funding for the period 2013-14 to 2016-17 has reduced by $144 million. This decrease is largely attributable to announcements included in the Commonwealth Government's 2014-15 Budget, particularly with regard to the National Health Reform funding arrangements.

The $144 million accumulated decrease across the four years to 2016-17 incorporates a $254 million reduction in health funding and a $38 million decrease in funding for disability services, partially offset by a $154 million increase in funding for education and early childhood.

From 1 July 2017 funding will no longer be provided under the National Health Reform Agreement. Instead the Commonwealth Government will provide funding for public hospitals, and index its contribution by the CPI and adjust for population growth. The 2014-15 Budget comments that changes to the National Health Reform funding from 2018 will decrease Commonwealth funding by a further $217 million in 2017-18.[10]

Changes in the quantum of funding under the Students First program will also occur from the 2018 school year onwards. Under the revised arrangements total recurrent funding for schools will be indexed by the CPI with an allowance for changes in enrolments.

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 2014-15, South Australia will receive an estimated $502 million of National Partnerships funding for recurrent purposes (including grants for on-passing). This is a decrease of 11% from the $564 million estimated for 2013-14. These grants decline by a further 26%, to $371 million by 2017-18. These decreases reflect funding decisions of the Commonwealth Government. The 2014-15 Budget identifies the State programs most impacted by these decisions[11].

National Partnership funding for capital purposes is anticipated to increase by $86 million in 2014-15, with a further $308 million increase in 2015-16. Significant capital funding continues across the forward estimates.

7.3 Taxation revenue

Taxation revenue is the second largest source of revenue to the State and represents about 27% of revenues in 2013-14. It comprises a diverse range of activities, including payroll, property, motor vehicles and gambling.

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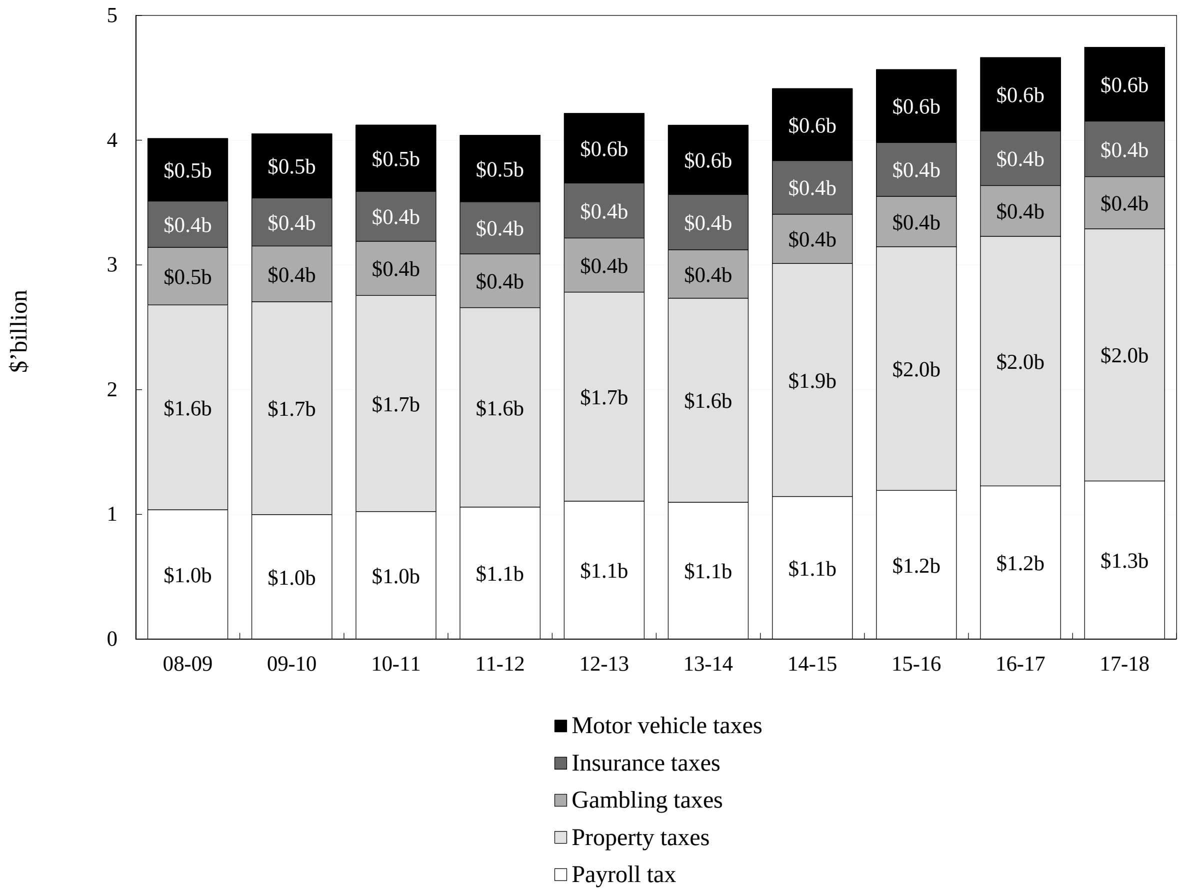
[10] 2014-15 Budget Paper 3 'Budget Statement', page 59.
[11] 2014-15 Budget Paper 3 'Budget Statement', page 60.

The following chart examines the trend in the components of taxation receipts (in real terms) over the 10 year period to 2017-18.

Chart 7.2 – Taxation revenue (real)



Total taxes, in real terms, decrease marginally in 2013-14 before rising in 2014-15 and 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 and payroll tax.

Taxation revenue for 2014-15 is estimated to be $4524 million (nominal), an increase of $403 million over the estimated result for 2013-14. It is expected to be $5236 million (nominal) in 2017-18, a real increase of $624 million compared to 2013-14.

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 $29 million in 2014-15.

Property taxes for 2014-15 are estimated to be $1915 million (nominal), a real increase of $232 million from the estimated result for 2013-14. They are expected to be $2231 million (nominal) in 2017-18, a real increase of $385 million compared to 2013-14. Chart 7.3 shows the trend in property taxes (in real terms).

Chart 7.3 – Taxes on property (real)

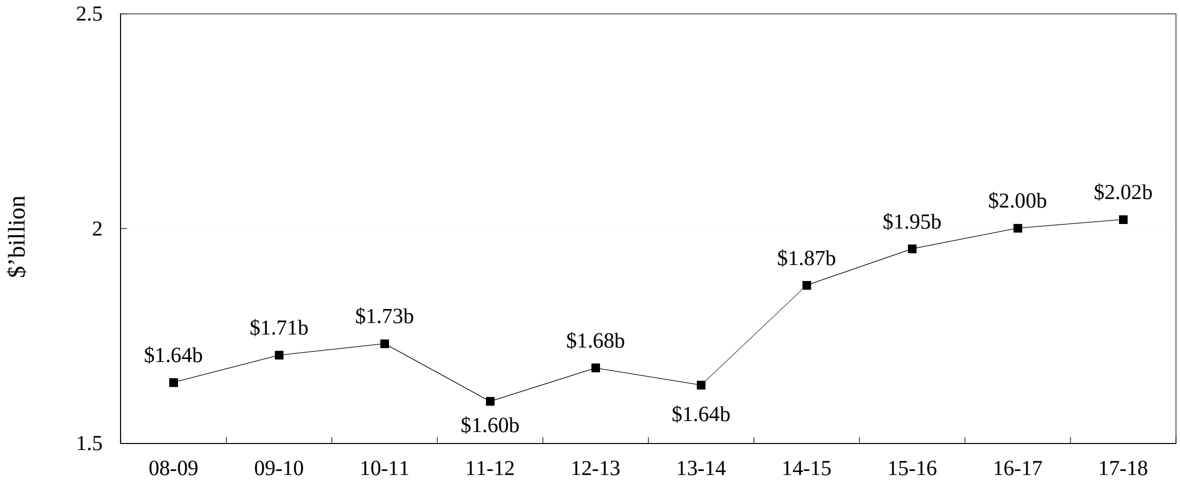
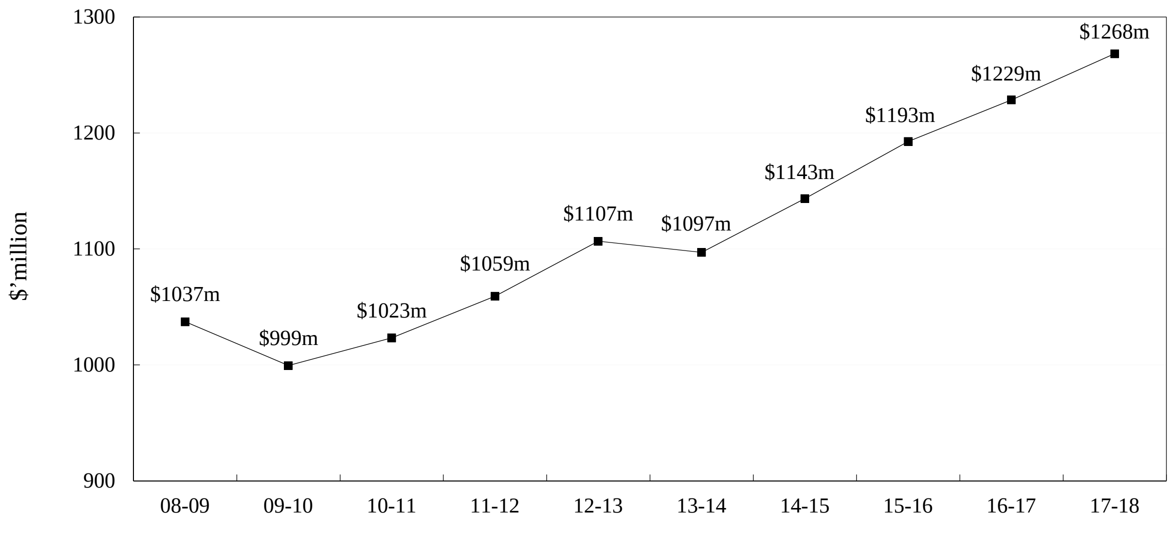


Chart 7.3 highlights the estimated increase in property taxes over the forward estimates. The increase in property taxes for 2014-15 is due mainly to a forecast increase in conveyance duty, the removal of Emergency Services levy remissions from 1 July 2014 and the commencement of the transport development levy. The annual increases for 2015-16 and thereafter are largely attributable to expected increases in conveyance duty driven by estimated growth in the number of property transactions and annual real growth in property prices.

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 2014-15 are estimated to be $1172 million (nominal), a real increase of $46 million from the estimated result for 2013-14. The payroll tax threshold remained at $600 000 on 1 July 2013. In addition, the payroll tax rate also remained at 4.95%.

Payroll tax is expected to be $1400 million (nominal) in 2017-18, a real increase of $171 million compared to 2013-14.

7.3.3 Gambling taxes

Gambling taxes for 2014-15 are estimated to be $404 million (nominal), which is broadly consistent with the result for 2013-14 (in real teams).

Chart 7.5 – Gambling taxes (real)

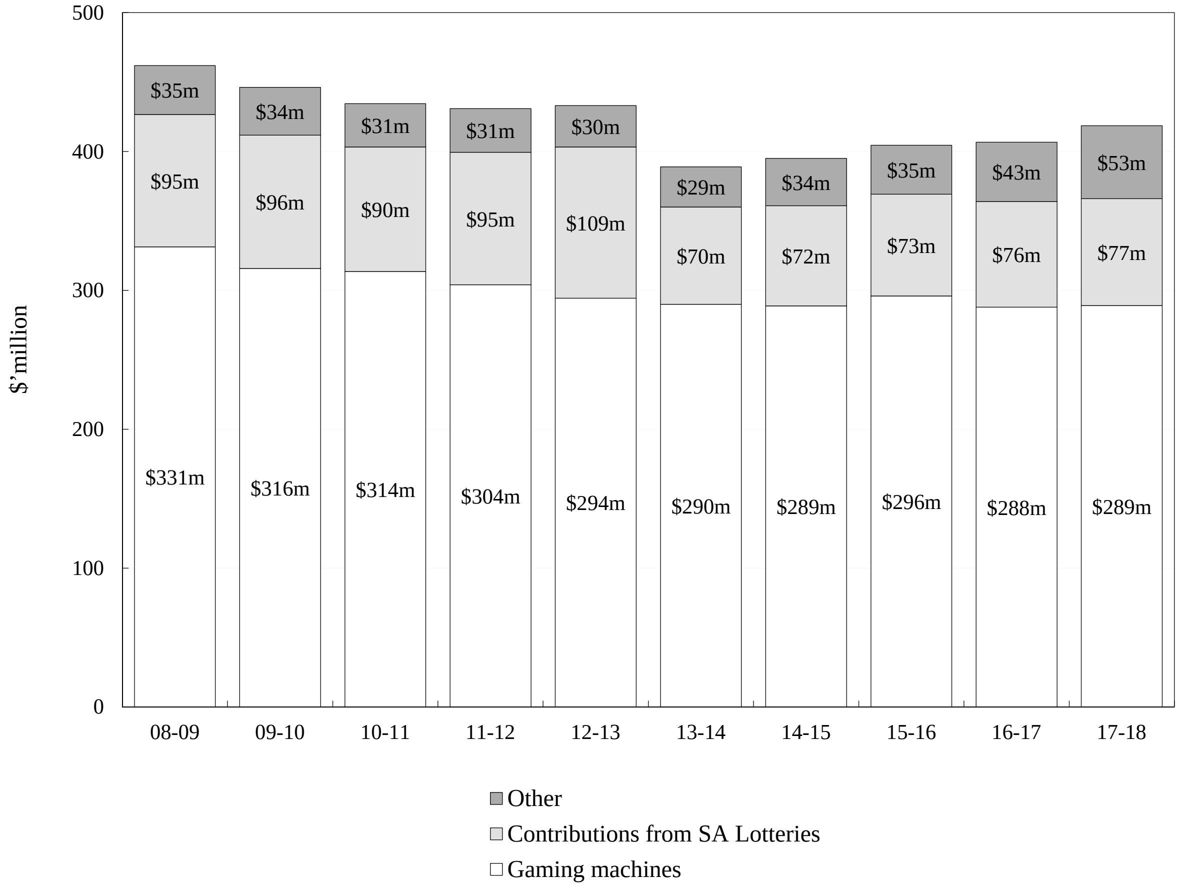


Chart 7.5 demonstrates the downward trend in total gambling revenue over the six years to 2013-14, particularly in revenue from gaming machines in hotels and clubs.

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 14% of estimated total revenues in 2013-14. Sales of goods and services by the general government sector include government fees and charges, most of which will have increased by 2.7% from 1 July 2014 reflecting the annual indexation of fees.

Revenue from sales of goods and services are expected to be $2513 million (nominal) in 2017-18, a real increase of $78 million compared to 2013-14.

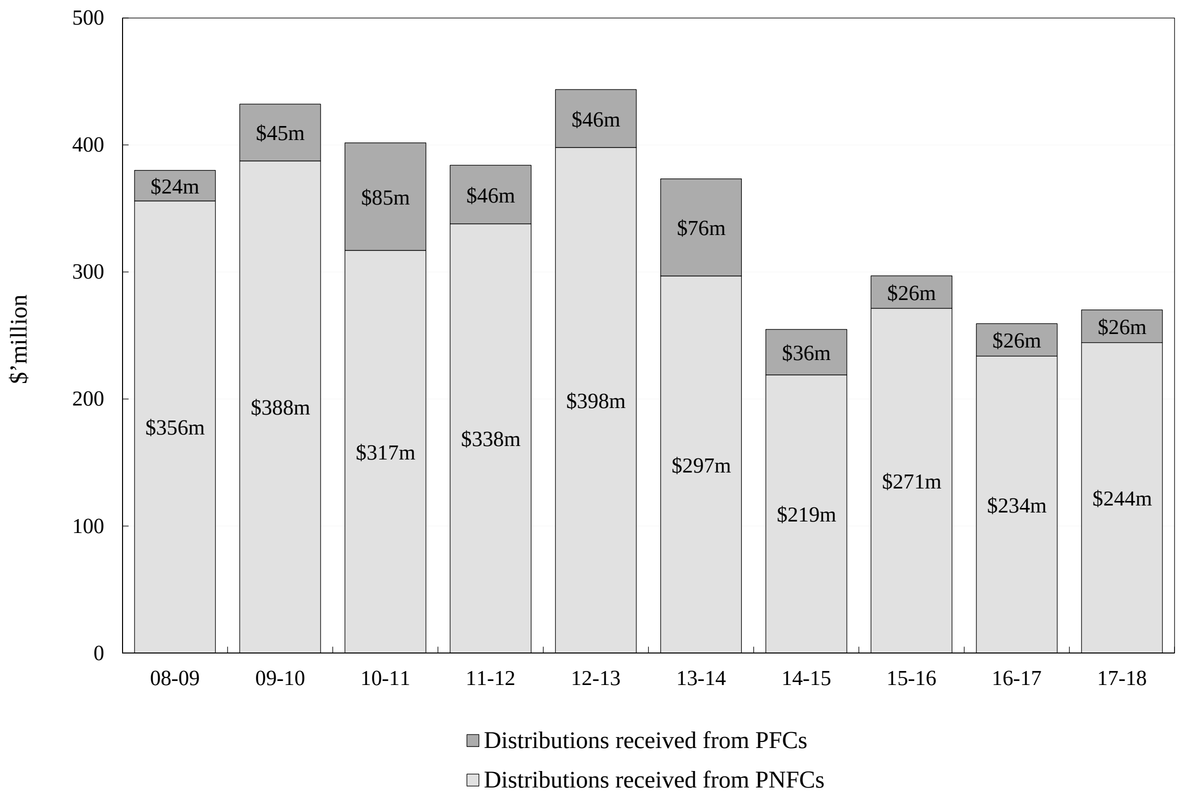
7.5 Dividend and income tax equivalent income

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 2017-18.

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



Total distributions for 2013-14 are estimated at $375 million, $46 million higher than expected due to improved distributions from 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 78% of estimated total distributions for 2013-14.

Distributions from SA Water are estimated to decrease in 2014-15 as SA Water incurs additional costs due to additional interest and guarantee fee expenses associated with its $2.7 billion increase in debt. Distributions increase again in 2015-16, due mainly to the recognition of revenue following the completion of a significant project in the Yorke Peninsula and the cumulative effect of efficiency gains.

7.6 Other revenue

Other revenue mainly comprises royalties, fines and penalties and schools fundraising revenue. The 2013-14 estimated result of $673 million is broadly in line with the 2013-14 Budget. In real terms other revenue is expected to fall marginally across the forward estimates.

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 $45 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 $50 million p.a. Revised Commonwealth Government estimates of the GST pool in 2013-14 are 0.9% higher than the estimate of the GST pool made at the time of the Commonwealth's 2013-14 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 $38 million.

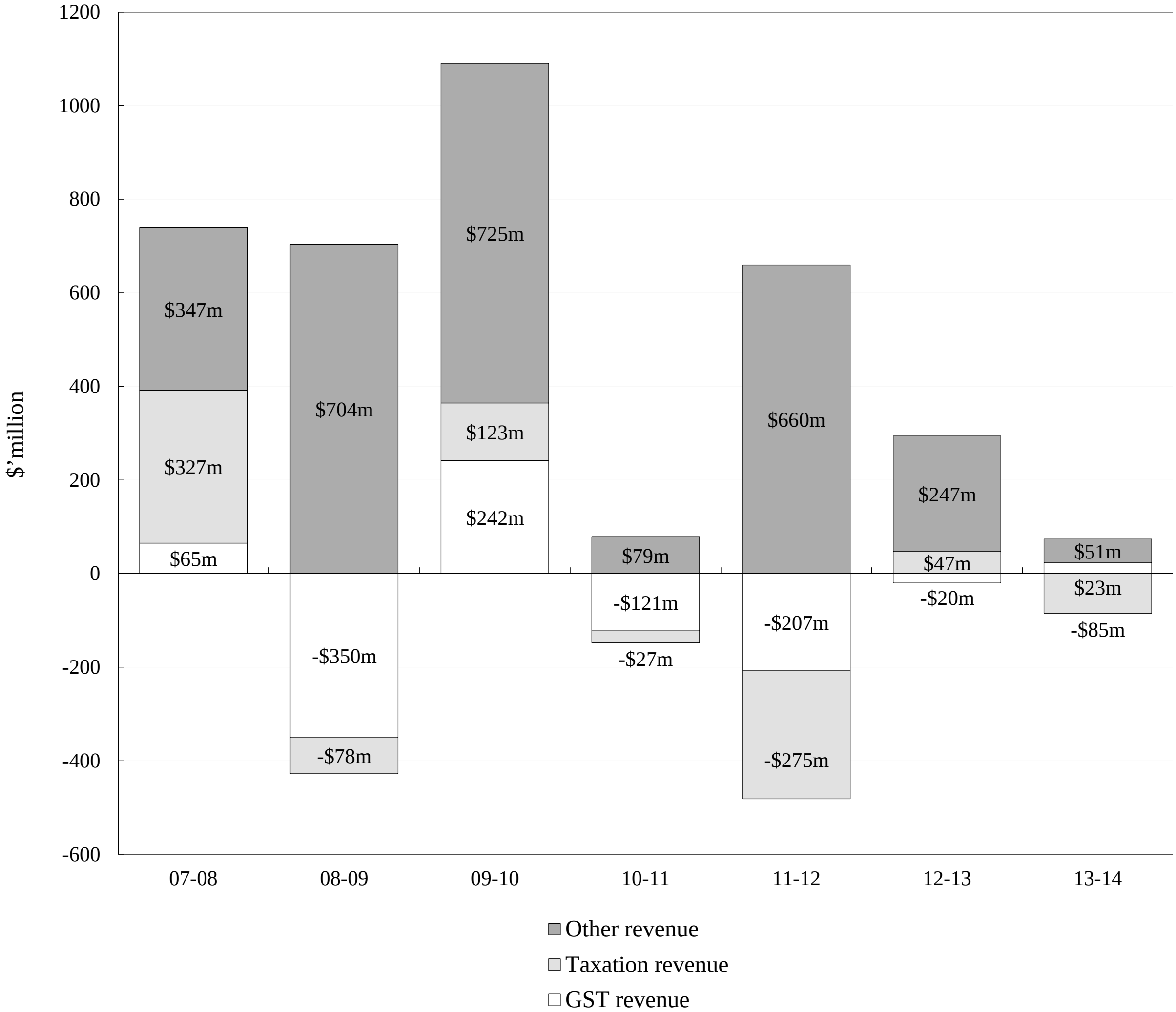
- ***Commonwealth specific purpose and National Partnership grants*** – payments for specific purposes and National Partnerships from the Commonwealth account for about 20% of State Government revenues. Variations in their level or the conditions applying to these payments pose a risk to the budget.

Refer 2014-15 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 historical 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) 2013-14 is the difference between budget and estimated results.

The chart highlights the very large favourable variations from budget that were enjoyed in 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 2013-14 anticipate an unfavourable result for taxation revenue, largely offset by favourable variations in GST and other revenue.

8 Expenses

8.1 Expenses overview

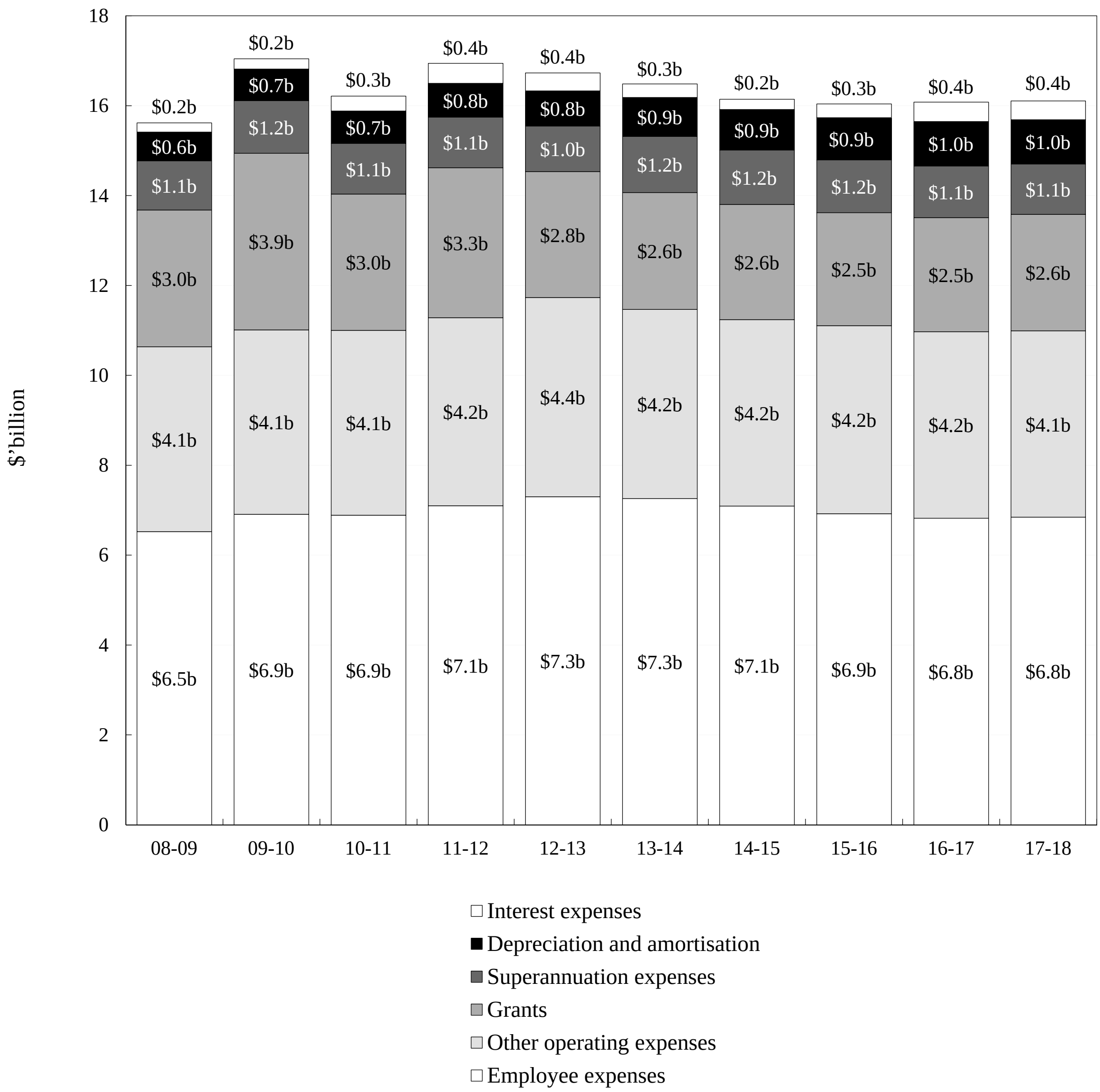
In the absence of better than budgeted revenue outcomes, the key to achieving the budget operating result targets is to control expenses. Consistent with recent past Budgets, the 2014-15 Budget expects significant restraint in spending.

For 2013-14 estimated expenses total $16.5 billion and exceed budget by $311 million or 2%.

Total expenses for 2014-15 are budgeted to be $16.5 billion, $60 million or a marginal 0.4% increase on the 2013-14 estimated result. Total expenses are expected to grow by 8% to $17.8 billion in 2017-18.

The following chart highlights the trends in expenses (in real terms) that have emerged since 2008-09.

Chart 8.1 – General government sector – expenses (real)



The chart shows the impact that movements in grant expenses have on total expenses over the period 2008-09 to 2012-13. Total expenses rise to $17 billion (real) in 2009-10 and $16.9 billion (real) in 2011-12, before dropping in the subsequent year. These movements were predominately impacted by the timing of grant expenditure.

For 2013-14 total expenses are expected to decrease to $16.5 billion (real), due mainly to decreases in grants and other operating expenses, partially offset by increases in the remaining expense categories.

The chart also demonstrates the level of expenditure restraint forecast over 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 2014-15 Budget Paper 3 'Budget Statement', Chapter 2.

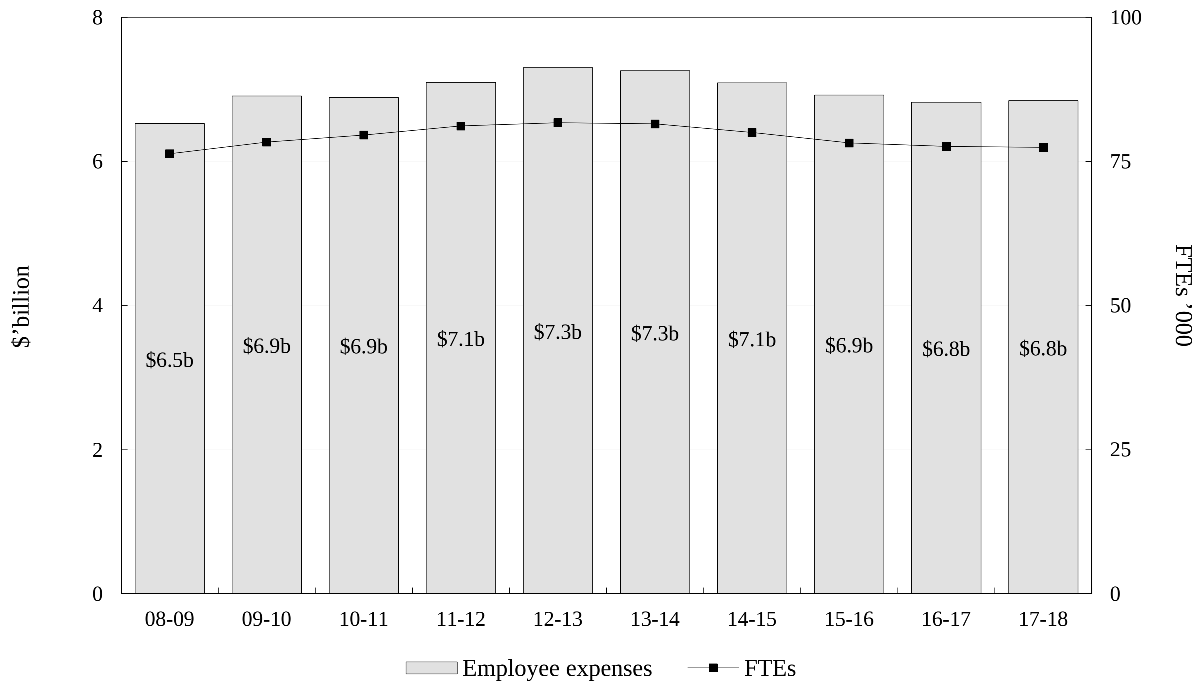
8.2 Expenses by type

8.2.1 Employee expenses

Employee expenses (an estimated $7258 million in 2013-14) represent the highest proportion (44%) of total expenses. They are estimated to increase by less than 0.2% in 2014-15 and then on average by 1.3% p.a. to 2017-18. In real terms the 2014-15 Budget anticipates employee expenses to decrease by 5.7% by 2017-18.

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)]



(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 each year between 2014-15 and 2016-17, remaining relatively constant in 2017-18.

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 2013-14 employee expenses grew, in real terms, by an average of 2.2% per year. The 2014-15 Budget shows employee expenses decreasing in real terms by 2.3% for the 2014-15 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 2014-15. A proportion of the salaries and wages contingency allowance is included in other operating expenses.

The 2014-15 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, are the outcomes from enterprise agreements and control of FTE numbers.

At the time of the presentation of the 2014-15 Budget the main enterprise agreements currently under negotiation or expected to commence negotiation during the next 12 months include the building metal and plumbing trades, police and the wages parity salaried group.

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

- *SA Public Sector Wages Parity Enterprise Agreement: Weekly paid 2013:* $30 per week from 1 October 2012, with an annual 3% increase from 1 October 2012 and 1 October 2013.

- *Nursing/Midwifery Enterprise Agreement 2013:* Annual salary increases of 3% from 1 October 2013, 1 October 2014 and 1 October 2015.

- *SA Health Salaried Medical Officers Enterprise Agreement 2013:* Annual salary increase of 9% from 14 April 2013, annual salary increases of 3% from 14 April 2014 and 14 April 2015, and 2.5% increase from 14 April 2016.

- *South Australian Metropolitan Fire Service Enterprise Agreement 2014:* Annual salary increases of 3% from 1 January 2015 and 1 January 2016, a 1% annual salary increase from 1 July 2016 and a 3% salary increase from 1 January 2017.

The Government has indicated that future wage outcomes will be crucial in determining whether it can achieve the expenditure forward estimates in the 2014-15 Budget, and also the level of government services that can be delivered in light of existing economic conditions.

8.2.2 Other operating expenses

Other operating expenses include general purchases of goods and services and are estimated to represent 26% of total expenses for 2013-14.

Other operating expenses are estimated to be $4.3 billion for 2014-15, an increase of $44 million or 1% in nominal terms from 2013-14. The projection for the forward years to 2017-18 is for a real terms decline of 1.5%.

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 2013-14 and 2014-15.

Table 8.1 – Contingency provisions

	2013-14 Budget $'million	2013-14 Estimated result $'million	2014-15 Budget $'million
Employee entitlements	145	284	66
Investing contingencies	18	11	23
Supplies and services	132	29	139
	295	324	228

While allocating sums to each of the categories for presentation purposes, contingency funds may also be transferred from other lines where available. The 2014-15 Budget includes contingency amounts totalling $228 million, $95 million less than the estimated outcome for 2013-14 and $144 million less than the actual outcome for 2012-13.

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 was influenced by the flowthrough of Commonwealth grant revenue. Table 6.6 of Chapter 6 of this Report shows the changes in grants expense over the forward estimates. Grants are estimated to be $2601 million for 2013-14, $16 million over budget predictions.

Grants are budgeted to increase by $25 million to $2626 million in 2014-15 largely due to an increase in grants associated with the South Australian River Murray Sustainability program for water recovery and industry assistance.

Grants are budgeted to increase by a further $232 million to $2858 million in 2017-18, due mainly to the anticipated growth in Communities and Social Inclusion grants, reflecting an increase in grants to the South Australian Housing Trust budgeted in 2017-18.

8.2.5 Superannuation expenses

8.2.5.1 Superannuation interest cost

The superannuation interest expense represents the increase during the year in the defined benefit superannuation obligations due to these being one year closer to settlement, less the expected earnings on superannuation assets. The superannuation interest expense is calculated based on the unfunded superannuation liability at the end of the preceding financial year.

The superannuation interest expense for 2013-14 is estimated at $468 million, $34 million higher than the estimate in the 2013-14 Budget but consistent with estimates in the 2013-14 MYBR. The increase in the superannuation interest expense reflects revised assumptions and investment returns.

The superannuation interest expense is expected to decrease over the period of the forward estimates, reflecting existing assumptions for the calculation of the defined benefit superannuation obligations and investment returns.

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-costs on accrued leave. Estimated other superannuation expenses were $781 million in 2013-14 and are projected to increase to $820 million in 2017-18, a real decrease of 4.9%.

8.2.6 Depreciation and amortisation

Estimated depreciation and amortisation expenses were $864 million in 2013-14 and are projected to increase by 26% to $1084 million in 2017-18. 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 period from 2013-14 to 2016-17 include the Glenside Campus redevelopment, Lyell McEwin Hospital Stage C redevelopment and the redevelopment of the Adelaide Oval.

The completion of road network projects, including the South Road Superway and duplication of the Southern Expressway, also contribute to the increase in depreciation over the forward estimates.

Amortisation of the asset under 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 ($73 million).

8.2.7 Interest expense

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

Estimated interest expense in 2013-14 was $304 million, $75 million lower than forecast in the 2013-14 Budget. This decrease reflects the impact of netting the interest received on the Treasurer's funds held on deposit with SAFA against interest paid on Treasurer's borrowings.

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 ($111.7 million). The commencement of the Royal Adelaide Hospital finance lease agreement is the main driver of a projected increase in interest expense from 2016-17.

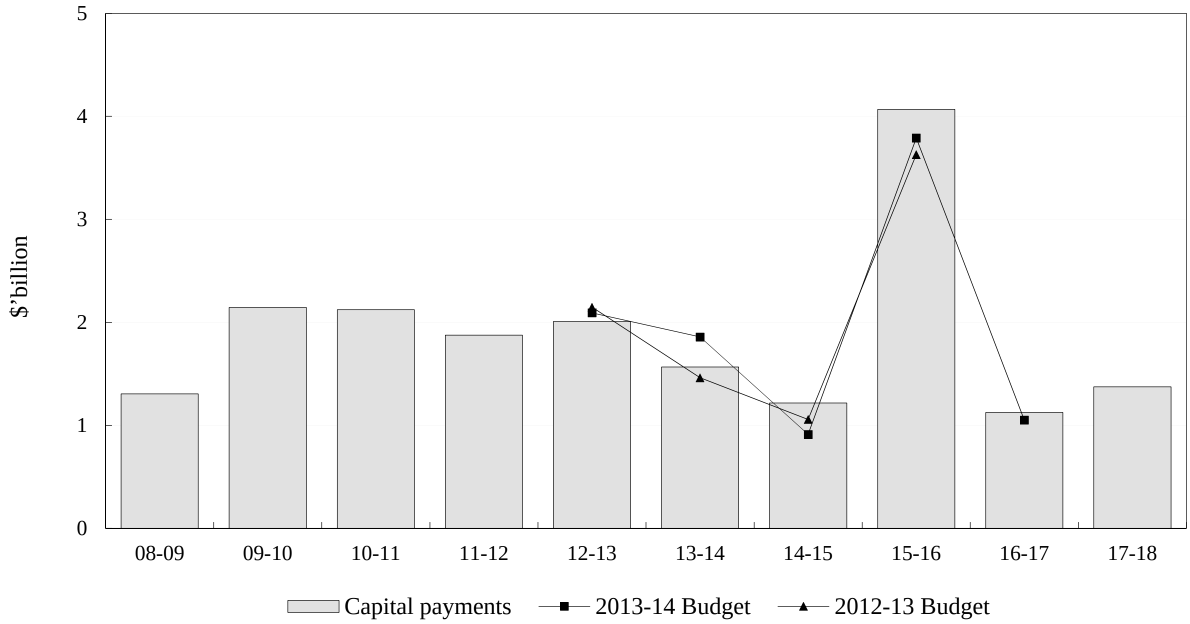
Further discussion in relation to debt movements is provided in section 9.6 of Chapter 9 of this Report.

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 2017-18, overlayed with budgeted purchases from the 2012-13 and 2013-14 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 $2 billion in 2009-10 and 2010-11.

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.

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

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 2014-15 Budget included investing carryovers from prior years into 2014-15 and future years of $254 million.

The 2012-13 Budget outlined investing project suspensions and deferrals totalling $444.2 million[12] 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 deferred in the 2012-13 Budget included the Queen Elizabeth Hospital redevelopment (Stage 3A) and the Modbury Hospital redevelopment. The 2014-15 Budget comments that these large projects have now been suspended in response to the Government's response to the 2014-15 Commonwealth Budget.[13]

The funding previously allocated to these projects, together with funding to redevelop the Flinders Medical Centre announced in the 2014-15 State election have been redirected to a Health Capital Reconfiguration Fund, which is included in investing contingencies over the forward estimates.

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.

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[12] 2012-13 Budget Paper 3 'Budget Statement', page 28.

[13] 2014-15 Budget Paper 3 'Budget Statement', page 7.

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

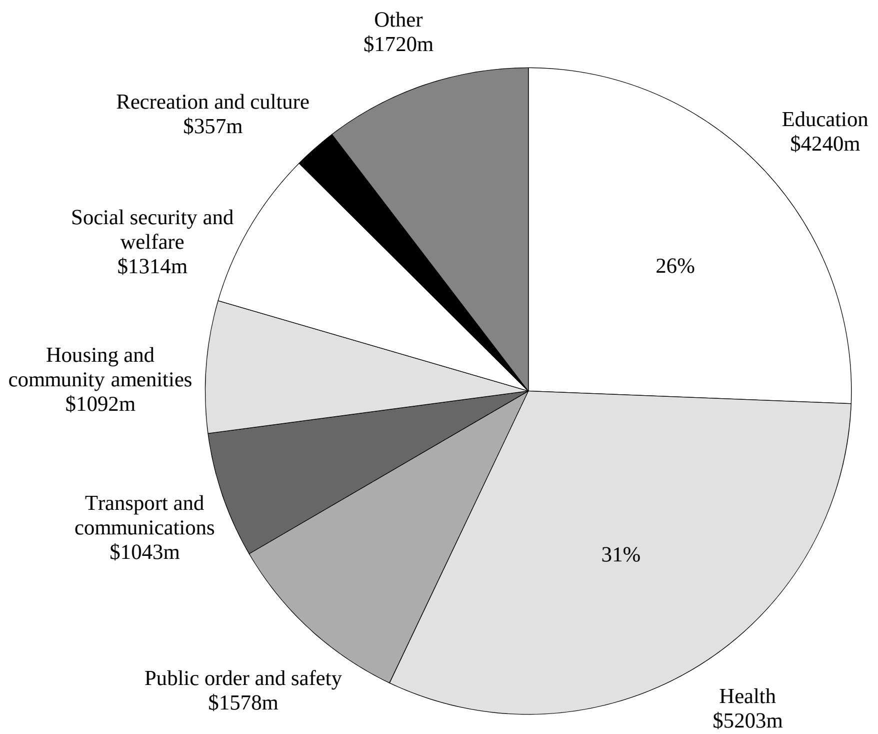
Sales of non-financial assets are taken into account in calculating the annual net lending result. They are netted from purchases of non-financial assets when determining total net acquisition of non-financial assets.

Total asset sales for the general government sector over the four years to 2017-18 are estimated to be $597 million, including $389 million anticipated in 2014-15.

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 2014-15 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[14]



8.4 Risks to expenses

8.4.1 Overview

As with revenue, the 2014-15 Budget provides detailed consideration of various risks to the expenditure budget and acknowledges the management task for achieving budgeted outcomes.[15]

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 $260 million in 2017-18.
- ***Interest rates*** – a 1.0 percentage point increase in the average interest rate applying to general government sector net debt would increase net interest expense by about $45 million in 2014-15 rising to $53 million in 2017-18.

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[14] 2014-15 Budget Paper 3 'Budget Statement', table 2.22
[15] 2014-15 Budget Paper 3 'Budget Statement', page 107

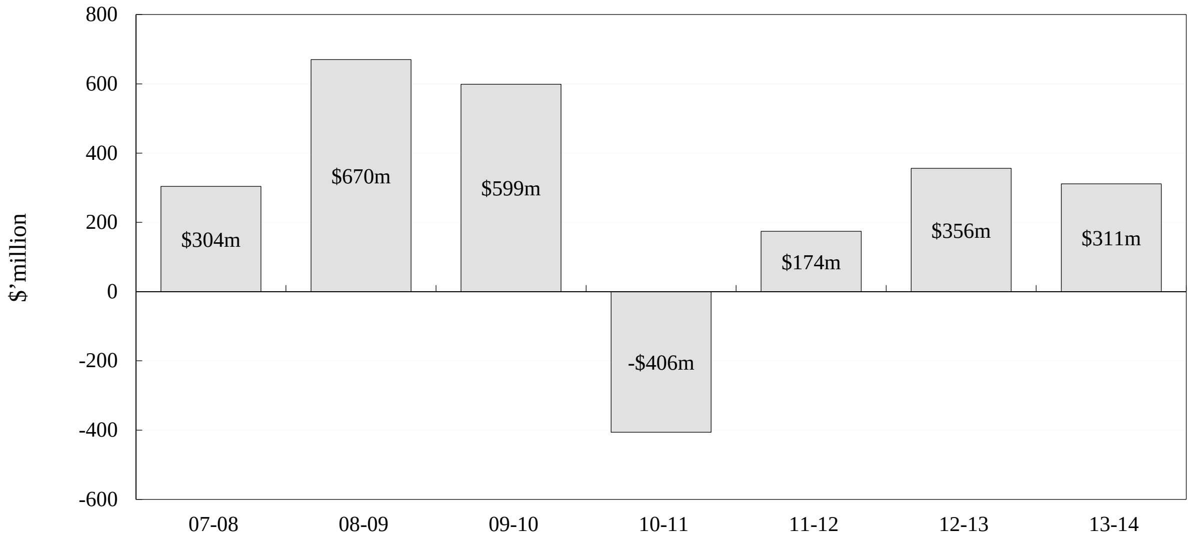
- ***Capital investment pressures*** **–** a number of departments have large capital investment programs over the forward estimates period. Large capital programs increase the risk of cost escalation compared with original projections.

  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 $12 million in 2014-15.

- ***Hospital expenditure growth*** **–** Hospital expenditure has consistently exceeded budget in recent years. While strategies are being implemented to manage this expenditure growth, a 1% growth in excess of the amounts included in the 2014-15 Budget will increase expenditure by $46 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) 2013-14 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 were $406 million less than budgeted, largely arising from decreases in grant and other operating expenses.

Total expenditure for 2013-14 is estimated to exceed budget by $311 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

2010-11 savings measures (continued)	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million
2012-13 Budget				
Facilities management - efficiencies	-	-	-2.4	-
Disability Client Trust Management	-	-	-1.0	-1.1
2012-13 MYBR				
Facilities management - efficiencies	-	-	-3.2	-
Court awarded costs against police - introduce cap	-	-	-	-1.6
2013-14 MYBR				
Biosecurity animal health-cost recovery	-	-	-	-0.5
Total adjustments	-1.3	-5.8	-35.1	-33.6

Note: Totals may not add due to rounding.

As conveyed in last year's Report Health and Ageing savings measures not achieved or deferred are not included in table 8.3, as DTF advised that they may include savings measures announced before or after the 2010-11 Budget. Notwithstanding, the 2012-13 MYBR reprofiled Health and Ageing's total savings requirement, including 2010-11 savings measures. DTF advised that the 2012-13 MYBR savings adjustment addressed Health and Ageing'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 and Ageing's budget pressures.

The 2012-13 MYBR reduced Health and Ageing's savings measures by $122.9 million for 2012-13 and by $128.3 million for 2013-14. Further, DTF advised that Health and Ageing 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 2014-15 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 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

Agency (continued)	Revised 2010-11 $'million	Revised 2011-12 $'million	Revised 2012-13 $'million	Revised 2013-14 $'million
Premier and Cabinet	1.8	5.6	12.1	20.2
Primary Industries and Regions	14.3	18.7	22.9	25.7
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 SA	0.4	0.5	0.4	0.4
Total savings measures announced in the 2010-11 Budget remaining in the 2014-15 Budget	105.3	258.6	350.4	414.5

Note: Totals may not add due to rounding

The 2014-15 Budget notes that, with the exception of Health and Ageing, agencies have delivered budgeted savings and agency savings budgeted to commence in 2013-14 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.

- The 2014-15 Budget introduces major savings measures amounting to $1.5 billion. This amount is made up of operating savings of $1.2 billion and investing savings of $290 million.

Savings introduced since the 2010-11 Budget now exceed the significant savings initiatives set in that Budget arising from the work of the Sustainable Budget Commission. The detail of savings by individual agency and individual savings measures introduced in the 2014-15 Budget are provided in 2014-15 Budget Paper 6, 'Budget Measures Statement'. A summary of these savings is discussed at pages 25 and 26 of 2014-15 Budget Paper 3 'Budget Statement'. Tables 2.4 and 2.5 at pages 27 and 28 itemise savings by agency.

8.4.5 *Nature of savings initiatives*

I have commented in previous Reports that an inherent risk of the savings 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, unsatisfactory administrative performance and budget management oversight complexity.

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.

The 2014-15 Budget includes savings initiatives for reductions of a further 308 FTEs from specific measures, including 200 FTEs identified as a result of the reductions announced in the 2014-15 Commonwealth Budget.

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)]	-	-	-	-	-	-	-	-	-
2013-14 MYBR[(a)]	-	-	-	-	-	-	-	-	-
2014-15 Budget	-	-	-	-	-	70	68	170	308
Originally budgeted FTE reduction	1 200	808	1 198	965	1 084	487	811	170	6 724

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

The 2014-15 Budget notes that FTEs in the general government sector are estimated to decrease by 4080 between 30 June 2014 and 30 June 2018.[16] This reduction reflects the cumulative impact of savings measures partially offset by new expenditure measures.

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 2014.

[16] 2014-15 Budget Paper 3 'Budget Statement', page 33

Table 8.6 – Actual and cap FTEs by portfolio as at 30 June 2014

Agency	Actual FTEs	Approved CAP FTEs	Variance FTEs	%
Attorney-General	1 133	1 190	(57)	(4.8)
Communities and Social Inclusion	3 737	3 836	(99)	(2.6)
Correctional Services	1 697	1 651	46	2.8
Courts	618	644	(26)	(4.0)
Defence SA	31	31	-	-
Education and Child Development	23 150	23 083	67	0.3
Electoral Commission of SA	20	22	(2)	(9.1)
Emergency Services	1 171	1 177	(6)	(0.5)
Environment Protection Authority	220	217	3	1.4
Environment, Water and Natural Resources	1 513	1 586	(73)	(4.6)
Further Educ, Employ, Science and Tech.	2 894	3 131	(237)	(7.6)
Health and Ageing	30 763	30 688	75	0.2
Manufacturing, Innov, Trade, Res and Energy	477	482	(5)	(1.0)
Planning, Transport and Infrastructure	3 351	3 425	(74)	(2.2)
Premier and Cabinet	1 944	2 083	(139)	(6.7)
Primary Industries and Regions	834	898	(64)	(7.1)
SA Police	5 645	5 774	(129)	(2.2)
Tourism	95	106	(11)	(10.4)
Treasury and Finance	356	467	(111)	(23.8)
Total	79 649	80 491	(842)	(1.0)

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

The 2014-15 estimate of FTEs for the general government sector as at 30 June 2014 was 81 516.[17] 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 (75 FTEs) – primarily due to slightly higher than cap results in health units.
- Education and Child Development (67 FTEs) – due mainly to additional FTEs relating to the National Education Reform Agreement, partially offset by recruitment delays.
- Correctional Services (46 FTEs) – largely reflecting that the Correctional Services' FTE cap under-represents the size of the custodial workforce.

The majority of agencies with large variances below the FTE cap reported that the variances were either the result of earlier than budgeted separation of employees or the result of vacancies. Primary Industries and Regions reported that it was 64 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.

[17] 2014-15 Budget Paper 3 'Budget Statement', page 33.

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.

DTF advised that the TVSP scheme remains available for workforce reductions associated with specific measures. The 2013-14 Budget noted that, from 1 July 2014, the maximum TVSP payout will be reduced from 116 weeks pay to 52 weeks pay.

Audit sought from DTF a summary of TVSPs since November 2010, as DTF 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 2014.

Table 8.7 – FTE reductions from TVSPs reported by agencies
1 November 2010 to 30 June 2014

General government sector	FTE reductions from TVSPs
Arts SA	3.0
Attorney-General’s	124.5
Correctional Services	21.0
Courts Administration Authority	6.0
Communities and Social Inclusion(2)	164.3
Defence SA	1.0
Education and Child Development(3)	270.9
Environment, Water and Natural Resources(4)	309.9
Environment Protection Authority	7.2
Further Education, Employment, Science and Technology	199.0
Health and Ageing	646.5
Manufacturing, Innovation, Trade, Resources and Energy(5)	74.7
Premier and Cabinet	130.5
Primary Industries and Regions(6)	138.2
Planning, Transport and Infrastructure(7)	203.5
SACA Board of SA	1.0
SA Country Fire Service	0.0
SA Fire and Emergency Services Commission	15.0
SA Lotteries(8)	37.3
SA Police	4.0
SA Ambulance Service	10.0
SA Metropolitan Fire Service	3.0
SA State Emergency Service	1.0
TAFE SA	333.9

General government sector (continued)	FTE reductions from TVSPs
Tourism	24.4
Treasury and Finance	64.5
Zero Waste SA	8.0
Public non-financial corporations sector	
Forestry SA	64.5
Total	2866.6

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.
(8) Moved to the General Government sector in 2013-14.

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

DTF has advised that for the period from 1 November 2010 to 30 June 2014 centrally reimbursed TVSP payments to staff totalled $343.2 million. A further $16.7 million in TVSP payments were funded by agencies. These figures exclude fees paid to Shared Services SA for administering the scheme, payroll tax, employee assistance and executive termination payments.

The 2014-15 Budget states that FTE reductions can also be achieved in other ways (eg natural attrition, not filling vacancies and not renewing contracts). Further, the Budget notes that after 30 June 2014, a public sector employee who has been identified by their agency as having been excess and has been unsuccessful in finding alternative public sector employment will be able to be separated with an appropriate financial package having regard to applicable legislation and industrial provisions.

At 30 June 2014 DPC advised there were 150 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 continued to be provided to the BRCC (formerly the SBCC) based on information supplied by agencies and analysis prepared by DTF.

DTF advised that the existing monitoring regime will continue in 2014-15, with monitoring reports provided to the Senior Management Council and the BRCC.

DTF also advised that the major risks to the fiscal outlook are set out in Chapter 6 of 2014-15 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 2014-15. 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 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 continued in 2013-14 with monthly monitoring of financial performance and quarterly monitoring of capital projects, savings measures and FTEs. Monitoring reports to be provided to the BRCC (formerly the SBCC). In addition, during the year copies of monitoring reports were provided for discussion at Senior Management Council.

8.4.8.1 Health and Ageing portfolio savings task

The 2012-13 Budget included new operating initiatives totalling $167 million in 2012-13 and 2013-14 to reprofile the Health and Ageing portfolio budget savings task. This aimed to provide Health and Ageing with additional resources for a more even annual build-up of savings to achieve its aggregate savings target by 2014-15. Health and Ageing's savings requirement to meet its budget was $169 million in 2012-13 increasing to $503.8 million by 2015-16.

In the past, Health and Ageing 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, Health and Ageing implemented the following strategies:

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

- In 2012 Health and Ageing 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 Health and Ageing to meet the Government's budget targets by 2015-16.

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

The 2014-15 Budget introduced significant additional savings of $532.7 million for the Health and Ageing portfolio. This includes identification of reductions in hospital beds or other health service reductions to save $332 million over the forward estimates.

The following table provides the revised savings measures since the 2012-13 Budget and a breakdown of the Health and Ageing'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	2016-17 $'million	2017-18 $'million
Revised savings target(1)						
Aggregate budget improvement required	-169.0	-351.3	-448.4	-503.8	-535.2	-568.6
2012-13 MYBR reduction in savings measures	122.9	128.3	148.7	123.3	83.9	73.4
2012-13 post-MYBR revised savings measures	-46.1	-223.0	-299.7	-380.5	-451.3	-495.2
2013-14 Budget savings measures	-	16.1	-5.0	-5.1	-5.3	-5.4
2013-14 Budget revised savings measures	**-46.1**	**-206.9**	**-304.7**	**-385.6**	**-456.6**	**-500.6**
2013-14 MYBR savings adjustments		43.8	40.3	15.3	-1.8	-1.8
2014-15 Budget savings measures			-17.6	-94.5	-157.3	-263.7
2014-15 Budget revised savings		**-163.1**	**-282.0**	**-464.8**	**-615.7**	**-766.2**
Annual growth in savings task			-118.9	-182.8	-150.8	-150.5

	2012-13 $'million	2013-14 $'million	2014-15 $'million	2015-16 $'million	2016-17 $'million	2017-18 $'million
Savings initiatives(2)						
Hospital budget performance and remediation reviews			26.8	46.7	46.7	46.7
Established measures			67.3	101.2	108.8	108.9
Operational efficiency measures			24.8	30.0	30.0	30.0
Potential savings requiring further analysis			-	123.8	267.0	417.4
			118.9	**301.7**	**452.5**	**603.0**

(1) Revised savings target figures provided by DTF.
(2) Savings initiatives figures provided by the Department for Health and Ageing for savings starting in 2014-15 and subsequent years.
(3) Totals may not add due to rounding.

The table demonstrates that the annual savings task for Health and Ageing is subject to significant annual growth, reaching a cumulative annual savings amount of $766.2 million in 2017-18. This will present an enormous challenge 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 may 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

- consultants commissioned 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

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

- a financial governance framework developed that has been promulgated across Health and Ageing, together with financial management training made available to staff

- a project management framework developed that has been promulgated across Health and Ageing 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

- establishment of consistent 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 Health and Ageing

- in May 2014, OBRI engaged consultants to undertake a budget performance review of SA Pathology and SA Medical Imaging. Final reports are expected in September 2014 at which time the Department for Health and Ageing will prepare a submission to Cabinet outlining the findings and recommendations for consideration and approval.

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 chapter provides commentary on trends and influences noted for the State public sector financial position.

The information principally relates to data for the general government sector and also the NFPS, which consolidates the general government and PNFC sectors.[18]

9.2 Overview of the State's financial position

The following summarises financial position information for the general government and non-financial public sectors of the State.

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)

	2010-11 Actual $'million	2011-12 Actual $'million	2012-13 Actual $'million	2013-14 Est'd result $'million	2014-15 Estimate $'million	2015-16 Estimate $'million	2016-17 Estimate $'million	2017-18 Estimate $'million
Financial assets	27 516	24 912	23 954	24 415	22 112	22 552	22 567	23 164
Non-financial assets	33 658	35 785	37 621	38 222	38 166	41 208	41 215	41 524
Total assets	61 175	60 698	61 575	62 638	60 277	63 760	63 783	64 688
Total liabilities	20 217	23 499	22 212	23 430	21 154	23 757	22 440	21 832
Net worth	40 958	37 199	39 363	39 208	39 124	40 003	41 343	42 856
Net financial worth	7 299	1 413	1 742	986	958	(1 205)	128	1 332
Net debt	2 930	4 165	5 227	6 887	4 511	7 146	5839	5 269

Note: Totals may not add due to rounding.

Of note is the expectation that:

- financial assets decrease by $1251 million across the forward estimates. This is impacted by changes in SA Water's debt to asset gearing ratio (refer point four below) and consequent reduction in equity

- non-financial assets increase by $3302 million over the forward estimates. This is mainly due 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 $42 856 million by 30 June 2018

[18] 2014-15 Budget Paper 3 'Budget Statement', appendix D details agencies within the respective sectors.

- Net debt is expected to decrease over the forward estimates from $6887 million as at 30 June 2014 to $5269 million as at 30 June 2018. The decrease in net debt largely reflects the change in gearing for SA Water.

  Specifically, the 2014-15 Budget provided measures to change SA Water's debt to asset gearing ratio. This will be achieved through a $2.7 billion increase in SA Water's debt, and therefore a corresponding reduction in general government sector net debt by the same amount.[19]

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)

	2010-11 Actual $'million	2011-12 Actual $'million	2012-13 Actual $'million	2013-14 Est'd result $'million	2014-15 Estimate $'million	2015-16 Estimate $'million	2016-17 Estimate $'million	2017-18 Estimate $'million
Financial assets	5 638	2 543	3 394	3 412	3 342	3 375	2 936	3 009
Non-financial assets	59 359	62 322	62 586	63 834	64 424	68 034	68 618	69 504
Total assets	64 997	64 866	65 981	67 247	67 766	71 409	71 553	72 512
Total liabilities	24 040	27 667	26 617	28 039	28 642	31 405	30 210	26 656
Net worth	40 958	37 199	39 363	39 208	39 124	40 003	41 343	42 856
Net financial worth	(18 402)	(25 123)	(23 223)	(24 627)	(25 300)	(28 031)	(27 275)	(26 647)
Net debt	6 541	7 996	8 949	10 931	11 497	14 266	13 075	12 545

Note: Totals may not add due to rounding.

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 $5670 million by 2017-18. This increase mainly arises from investment in, and revaluation of, health, transport and water related infrastructure
- net financial worth is predicted to marginally decrease over the forward estimates.
- net debt is also estimated to increase across the forward estimates by $1614 million with the recognition of the new Royal Adelaide Hospital principally contributing to the spiked increase in 2015-16 ($2.8 billion).

9.3 Assets

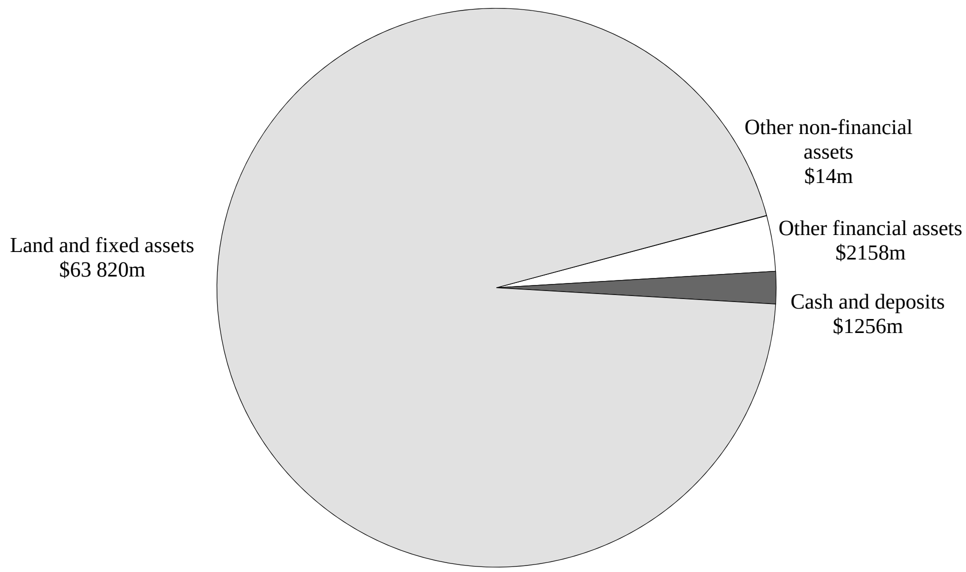
Table 9.2 above shows the State's asset position principally growing year to year because of ongoing asset acquisitions.

[19] 2014-15 Budget Paper 3 'Budget Statement', Chapter 4, 'Managing the State's Assets and Liabilities', page 73

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 2014 for the NFPS.

Chart 9.1 – Non-financial public sector assets at 30 June 2014



Other financial assets include equity of $958 million and receivables of $819 million. Equity comprises $848 million in other investments as well as $110 million of equity investments in other public sector agencies.

Non-financial assets represent the vast majority of State assets – 95% of the total. The State's non-financial or physical assets mainly comprise plant, equipment and infrastructure (including roads and water infrastructure) as well as 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 financial report users with an understanding of the extent and type of assets operationally managed by government agencies. Most assets are not realisable.

9.3.1.1 Revaluation of non-financial assets

Revaluations of non-financial assets, together with acquisitions, 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 2010-11 to 2013-14 for the major agencies in the general government and PNFC sectors.

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

	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million	Total $'million
General government	387	658	730	324	11 801
PNFCs	1 460	353	(545)	333	2 771
Total	1 847	1 011	185	657	14 572

Note: 2013-14 PNFC revaluation amounts exclude ForestrySA

Revaluation of the assets of the major agencies added $14 600 million to the total value of non-financial assets over the four year period to 2013-14. Asset revaluations by the Department of Planning, Transport and Infrastructure account for 52% of total non-financial asset revaluations over the four year period covered in table 9.3.

The $333 million increment for the PNFC sector in 2013-14 reflects a $348 million revaluation gain on infrastructure, plant and equipment recorded by SA Water offset by a $15 million decrement in freehold land and buildings recorded by the South Australian Housing Trust.

9.3.2 Financial assets

Total financial assets are expected to be $3412 million in 2013-14, falling to $3009 million in 2017-18. This reduction is primarily due to anticipated negative movements in 'investments in other public sector entities' under the financial asset equity category for both 2016-17 and 2017-18.

Investments in other public sector entities represent the value of the Government's interest in PFCs including WorkCover SA and MAC.

Additionally, Superannuation Funds Management Corporation of South Australia (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 2013 and 30 June 2014:

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

	Domestic equities $'million	International equities $'million	Fixed interest $'million	Other investments $'million	Total $'million
2013-14	5 026	5 641	2 017	11 151	23 835
2012-13	4 449	4 831	1 806	9 599	20 685

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

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 respective agency 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 2013-14 of $2839 million reflecting stable growth in 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.

As at 30 June 2014 MAC had net assets of $1252 million ($768 million in 2012-13). The assets of the CTP Fund as at 30 June 2014 were 132.1% of the statutory target solvency level, compared to 111.9% in 2012-13 and 100.8% in 2011-12. As demonstrated, in recent years there has been significant movement in MAC's solvency which demonstrates the potential, annual volatility of the CTP Fund and its dependence on strong market investment returns to achieve and maintain target levels of sufficient solvency.

WorkCoverSA reported a total comprehensive profit of $235 million in 2013-14 ($23 million in 2012-13). The $212 million improvement in comprehensive result was mainly attributable to reductions in the cost of claims of $211 million which significantly contributed to improvements in WorkCoverSA's reported underwriting result.

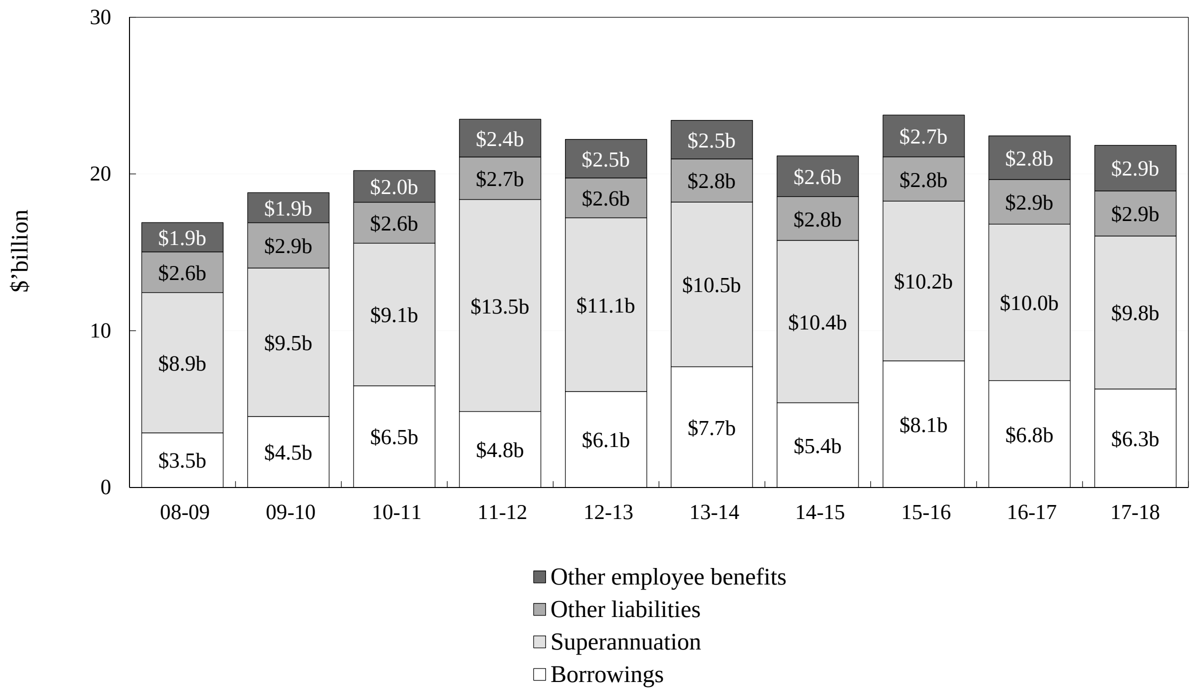
Further commentary is included in the sections titled 'Motor Accident Commission', 'South Australian Government Financing Authority', 'Superannuation Funds Management Corporation of South Australia' and 'WorkCover Corporation of South Australia' in Part B of this Report.

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 2017-18.

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 increase by $1218 million to $23 430 million in 2013-14, due mainly to increased borrowings partially offset by a decrease in the unfunded superannuation liability. The variability in the unfunded superannuation liability in the five years to 2013-14 is mainly due to movements in earnings, actuarial assumptions and the discount rate used to estimate the value of the liability.

Total liabilities are expected to decrease by $1598 million or 6.8% to $21 832 million over the forward estimate period. This is mainly due to expected decreases in both borrowings, down $1424 million, and the unfunded superannuation liability reducing by $744 million over the five years to 2017-18.

9.4.2 Non-financial public sector liabilities

Total liabilities are expected to increase by $1617 million or 5.8% to $29 656 million over the forward estimate period. In 2013-14 an increase of $1422 million in total liabilities is estimated, with higher borrowings offset by a reduced unfunded superannuation liability.

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 2014

Unfunded superannuation liabilities are estimated to decrease by $1435 million to $10 506 million at 30 June 2014, from the estimated liability as at 30 June 2013 detailed in the 2013-14 Budget. This decrease is explained in table 9.5 and principally reflects the increase in the discount rate used to estimate the liability, the impact of higher than expected returns on investments and other movements.

The following table sets out the major elements comprising the movement from the estimated unfunded superannuation liabilities at 30 June 2013 to 30 June 2014.

Table 9.5 – Estimated unfunded superannuation liabilities as at 30 June 2014

		$'million	$'million
Estimated unfunded liability 30 June 2013 (2013-14 Budget)			11 941
Add:	Difference between actual and expected returns	322	
	Movement in discount rate	(1 364)	
	Other	169	
	Adjustments to align with AASB 119	17	
	Total changes		(856)
Actual at 30 June 2013			11 085
Add:	Higher than expected returns on investments	(1 016)	
	Movement in discount rate	4	
	Other movements	433	
	Total changes		(579)
Estimated closing balance 30 June 2014 (2014-15 Budget)			10 506

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 rate that reflects the average maturity on the liability. 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 upwards from the current rate of 4.3%.

Table 9.6 – Sensitivity analysis of unfunded superannuation liabilities to discount rate movements as at 30 June 2014

Discount rate %	Unfunded superannuation liability $'billion	Increase (Decrease) $'billion
4.3	10 506	-
6.0	7505	(3 001)
7.5	5 558	(4 948)

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 7.5%, the value of the unfunded liability will reduce by $4.948 billion. 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.

9.5.2.2 Superannuation funding

DTF advised that total superannuation funding (including the fully funded Southern State

Superannuation Scheme) is expected to be $1461 million in 2014-15, up $64 million on the estimated funding for 2013-14. Payments comprise amounts paid from agencies as contributions to current employees for new service and contributions. This reflects 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 earnings 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 however required to compensate for reduced earnings to remain on target.

The past service superannuation liability cash payment for 2014-15 is estimated to be $417 million.[20]

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 14.1% was estimated for 2013-14 at the time of the 2014-15 budget.

9.5.3 Long-term funding of superannuation liabilities

The commitment to fully fund unfunded liabilities was reaffirmed by the Government in the 2014-15 Budget, with the position as at 30 June 2014 remaining consistent with the plan to eliminate unfunded superannuation liabilities by 2034.

Past service superannuation liability cash payments are estimated to 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 estimated to have already peaked (2011-12). It is estimated that benefit payments will peak in 2026-27 ($787 million).

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 $7.518 billion.

9.6 Net debt

The Government's decision to restructure its balance sheet in 2014–15 by transferring debt to the public non-financial corporation (PNFC) sector (SA Water) from the general government sector, will have a significant impact on the general government net debt position in 2014-15. There is no impact from this change on total non-financial public sector (NFPS) net debt, however general government sector net debt reduces by $2.7 billion.

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[20] 2014-15 Budget Paper 3 'Budget Statement', table 4.6.

9.6.1 Definition of net debt

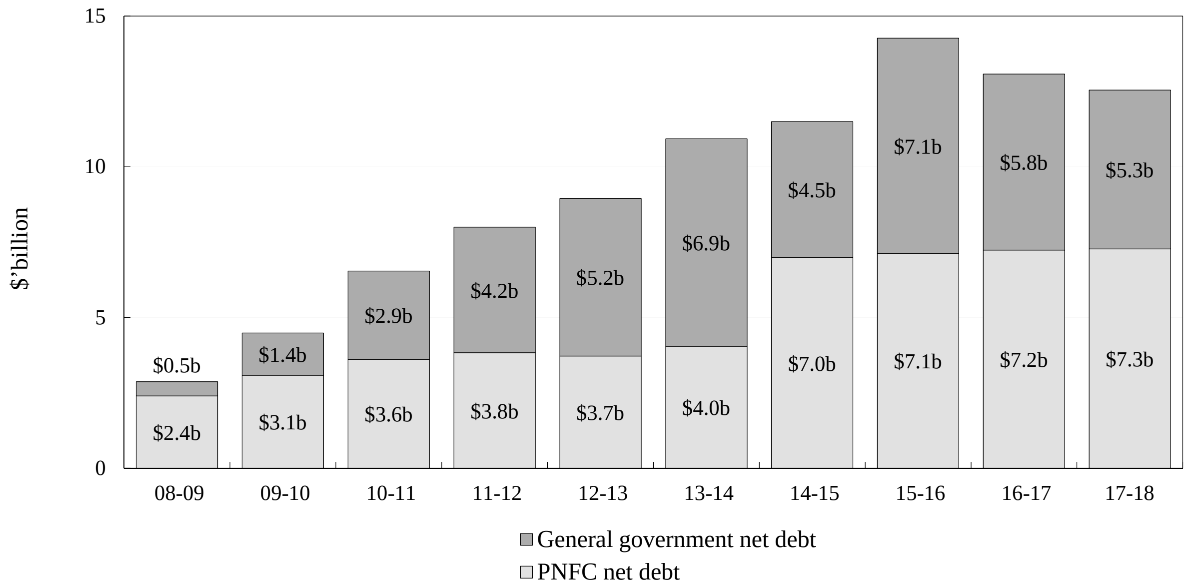
Net debt[21], comprises the stock of selected gross financial liabilities less financial assets. Net debt is reported in the balance sheet and is the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, investments, loans and placements.

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 NFPS net debt has increased by $6077 million to $8949 million (9.4% of South Australia's GSP) in the period 2008-09 to 2012-13, with general government net debt increasing from $475 million to $5227 million over this period.

In 2013-14 total NFPS net debt is expected to increase by $1982 million to $10 931 million (11% of South Australia's GSP). Forward estimates show that net debt is projected to rise to $12 545 million by 30 June 2018 (10.5% of South Australia's GSP).

Chart 9.3 – South Australian non-financial public sector net indebtedness 2008-09 to 2017-18



Over the forward estimates general government net debt is estimated to decrease by $1618 million to $5269 million.

The decrease in general government debt is mainly due to the change in SA Water's debt to asset gearing ratio – refer section 9.2.1 of this chapter. Conversely, net debt of the PNFCs increases by $3232 million over the same period to $7276 million for the same reason.

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

21 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.

In 2013-14 SA Water will account for approximately 92.4% of the total PNFC sector net debt. As a consequence of debt to asset gearing ratio changes, SA Water's net debt is forecast to increase over the forward estimates to $6726 million.

The 2014-15 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 in 2015-16. Consequently, this will have an impact on net debt and net financial liabilities moving forward. 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 2013-14 Budget.

Table 9.7 – Reconciliation of movements in general government net debt as at the 2013-14 Budget

	2013-14 Estimated result $'million	2014-15 Budget $'million	2015-16 Budget $'million	2016-17 Budget $'million	2017-18 Budget $'million
Opening general government net debt	**5 227**	**6 887**	**4 511**	**7 146**	**5 839**
General government cash surplus/deficit	-1 696	-300	217	835	601
Add: Net cash flows from equity transactions	11	2 675	-30	474	-27
Less:					
Assets acquisition under finance leases and similar arrangements	-	-	-2 820	-	-
Other movements	26	1	-1	-1	-3
Improvement/Deterioration to general government net debt	**-1 660**	**2 376**	**-2 635**	**1 307**	**570**
Closing general government net debt	**6 887**	**4 511**	**7 146**	**5 839**	**5 269**

Note: Table may not add due to rounding.

9.6.3 Debt affordability and servicing

At the end of 2013-14 total NFPS net debt is estimated to represent 11.1% of GSP compared to 10.5% in 2017-18.

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 Agreement 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 2013-14 financial year is between 1 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 2013-14 SAFA's funding task, after the budget and MYBR, was forecast at $6.1 billion comprising:[22]

- $1.5 billion for the South Australian public sector
- $4.6 billion to refinance existing debt.

SAFA is projecting a gross 2014-15 funding requirement of $5.8 billion. Anticipated drivers for this requirement are forecast to be the Treasurer and PNFCs including SA Water, HomeStart and the Adelaide Convention Centre. These new client borrowings will be funded by the expected issuance of circa $3.9 billion of Select Lines (term debt). SAFA anticipates this funding will primarily be sourced from domestic markets and most notably Authorised Deposit-taking Institutions operating in Australia.

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 2014 comprise superannuation liabilities ($10 506 million), other employee benefits ($2538 million), other liabilities ($1296 million), payables ($1164 million), advances received ($239 million) and deposits ($173 million).

Other employee benefits include long service leave provisions ($1758 million estimated result for 2013-14), annual leave liabilities ($541 million estimated result for 2013-14), salaries and wages liability ($165 million estimated result for 2013-14) and retention leave ($32 million estimated result for 2013-14).

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

- estimated long service leave provisions amounting to $1758 million as at 30 June 2014 and budgeted to increase to $1864 million by 30 June 2015. Long service leave is calculated by an estimation process in accordance with AASs

- estimated workers compensation provisions totalling $493 million are estimated as at 30 June 2014, increasing to $503 million at 30 June 2015.

9.8 Contingent liabilities

As reported in the Budget Papers[23] contingent liabilities are those that have not been recognised in the balance sheet, but rather are disclosed in notes to the accounts.

[22] SAFA Advisory Board Paper # 1267 – Funding Strategy – Annual Funding Task (May 2014)
[23] 2014-15 Budget Paper 3 'Budget Statement', pp. 111-112 provides a summary of contingent liabilities.

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 reliably measured
- 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 2013 were valued at $951 million ($896 million as at 30 June 2012). 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.

10 Comparison with other States

10.1 Observations

This chapter highlights trends for this State over the forward estimates to 2017-18 as well as relative differences between jurisdictions. Whilst no suggestions are made regarding what is considered optimal, significant variations or negative trends would warrant consideration as to the related implications.

Across jurisdictions economic indicators are influenced by varying valuation approaches for assets and liabilities, differences in the type and level of infrastructure, as well as higher State debt levels. Infrastructure can also be provided through private sector investment and therefore be excluded from 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 over the next four financial years.

The following table shows 2014-15 budgeted total revenue for each State.

Table 10.1 – 2014-15 budgeted general government total revenue by State

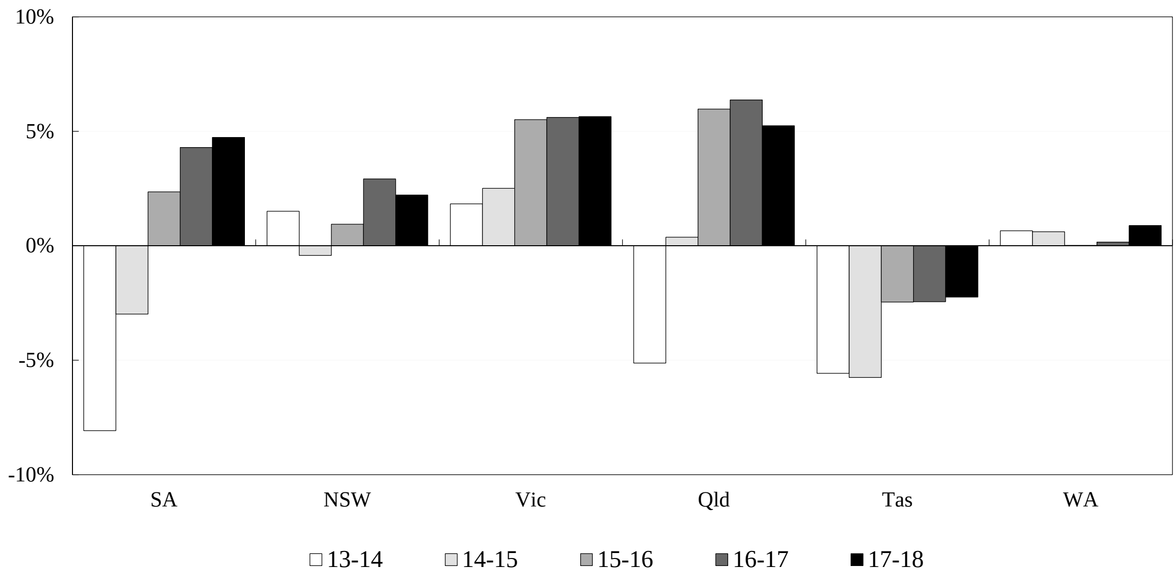
State	NSW	Vic	Qld	WA	SA	Tas
	$'million	$'million	$'million	$'million	$'million	$'million
Total revenue	67 113	52 902	50 120	28 683	16 067	4 964

Given the relative differences in state size and financial activity levels, the following comparisons are given as proportions of total revenue in each State.

10.2 Operating statement

The following charts compare trends in the GFS information with other States using 2014-15 Budget data.

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



All States except South Australia, New South Wales and Tasmania have projected positive ratios for the 2014-15 financial year. Chart 10.1 also shows that South Australia, Queensland and Tasmania have net operating deficits estimated for 2013-14. Across the forward estimates operating results broadly vary between jurisdictions.

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

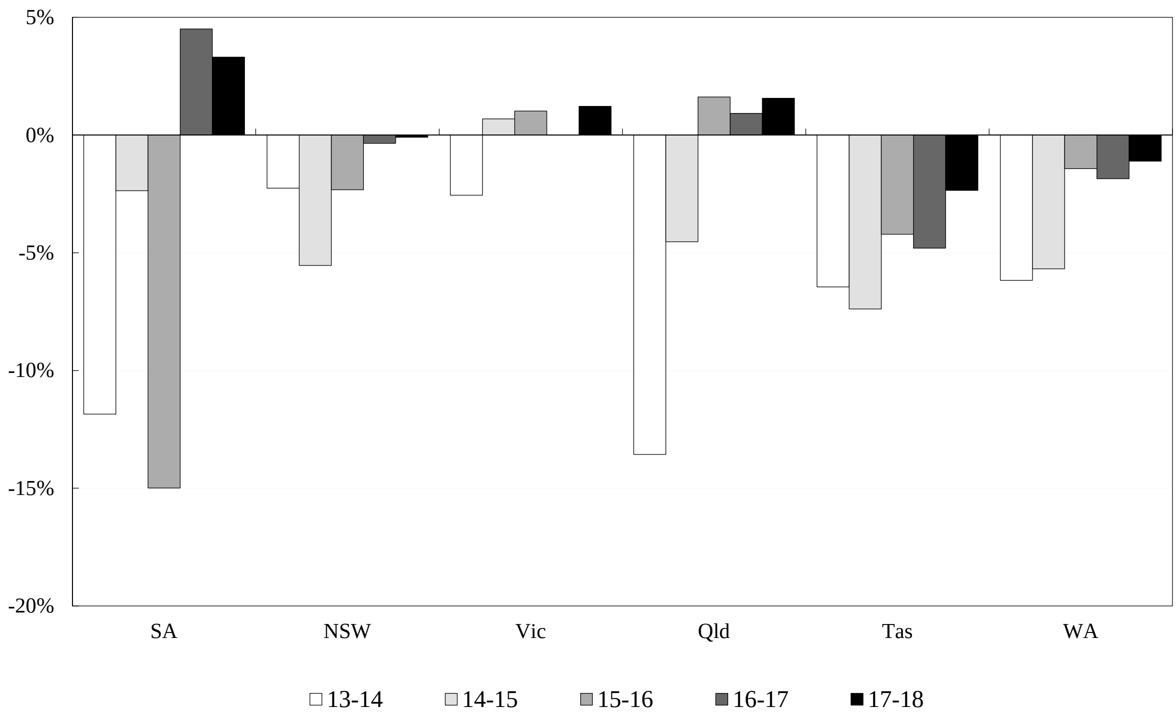


Chart 10.2 indicates all States except Victoria and Queensland are estimating net lending deficits up to and including 2015-16 with New South Wales, Tasmania and Western Australia showing deficits continuing to 2017-18. South Australia's forecast net lending deficit of $2587 million in 2015-16 reflects 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 also shows that for the period 2013-14 to 2015-16, the negative trend in South Australia's net borrowing as a proportion of total revenues is reasonably consistent with other States over the same time frame.

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 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 comparisons 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

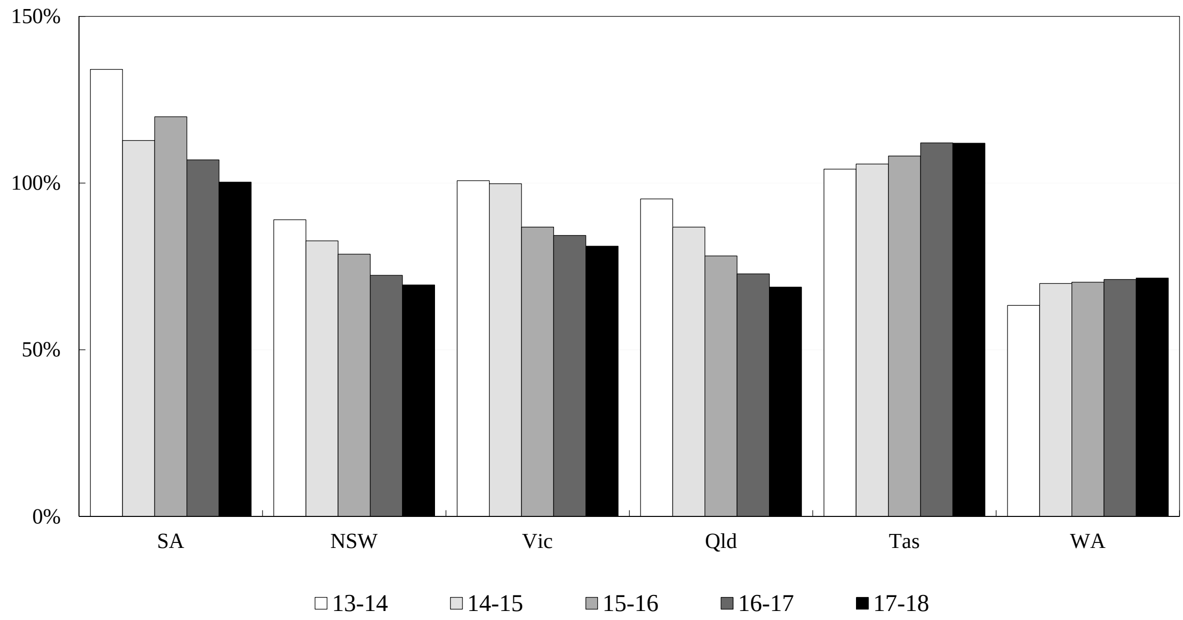


Chart 10.3 shows the 2013-14 Budget settings result in the ratio for South Australia generally declining over the forward estimates to 2017-18. This is consistent with New South Wales, Victoria and Queensland which are also predicting general declines over the same time period.

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 Audit scope 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 audit work 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 2013-14.

Table 11.1 – 2013-14 appropriation authority and payments

	Appropriation authority $'million	Actual payments $'million
Appropriation Act 2013	12 245.3	12 087.2
PFAA, section 15	71.0	71.0
Governor's Appropriation Fund	368.4	192.1
Specific appropriations authorised in various Acts	132.1	139.5
Total	12 816.8	12 489.8

The result on the Consolidated Account and variations from budget for 2013-14 were as follows.

Table 11.2 – 2013-14 Consolidated Account result

	2013-14 Budget $'million	2013-14 Actual $'million	Variation $'million
Total receipts	10 393.2	10 949.3	556.1
Total payments	12 377.5	12 489.8	112.3
Consolidated Account financing requirement	(1 984.3)	(1 540.5)	443.8

The deficit of $1540.5 million ($1115.2 million deficit in 2012-13) 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 repayment of advances from the South Australian Housing Trust (increase $98.2 million), GST revenue grants (increase $51.8 million), Commonwealth SPPs (increase $29.2 million), Commonwealth National Partnership payments (increase $15.4 million), the return of cash to Consolidated Account – cash alignment policy ($303.2 million from a zero estimate) and SA Water income tax equivalent (increase $49.9 million)

- ***Payments*** – higher than anticipated budgeted expenditure noted for the Department of Further Education, Employment, Science and Technology ($43.3 million or 8.9%), Department of Planning, Transport and Infrastructure ($50.2 million or 6.7%) and administered items for DTF ($78.3 million or 4.6%).

Consistent with the previous year, in 2013-14 significant amounts were appropriated to agencies as equity. The main equity contributions were to the Department of Planning, Transport and Infrastructure ($483.6 million), the Department for Health and Ageing ($99.1 million) and the Department of Further Education, Employment, Science and Technology ($61 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 2013-14.

Table 11.3 – Appropriation flexibility

	Authority/ Budget $'million	Actual payments $'million
Governor's Appropriation Fund	368.4	192.1
Contingency provisions in administered items for DTF	295.3	280.2
PFAA, section 15	71.0	71.0
Total flexibility	734.7	543.3

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	Primarily to ensure the Department's Operating Account did not become overdrawn	$50.2
Department of Further Education, Employment, Science and Technology	Primarily to ensure the Department's Operating Account did not become overdrawn	$43.3

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	115.911
TAFE SA	29.734
Department of Planning, Transport and Infrastructure	22.081
Department of Primary Industries and Regions	20.445
Department of Education and Child Development	19.404
Department of Environment, Water and Natural Resources	15.496

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 2013-14 $71 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 2012-13 the amount appropriated by the Treasurer was $83.2 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 2013-14. 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.[24]

Table 11.6 shows that over $3061 million is held in special deposit accounts and deposit accounts as at 30 June 2014.

Table 11.6 – Special deposit accounts and deposit accounts

	2012-13 $'million	2013-14 $'million	Increase (Decrease) $'million
Special deposit accounts	2 757.9	2 406.2	(351.7)
Deposit accounts	613.1	655.3	42.2
Total	3 371	3 061.5	(309.5)

Such unspent balances do come under the scrutiny of Parliament as they are reported in the financial positions of agencies and 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 2014 were:

- ***Special deposit accounts*** – Accrual Appropriation Excess Funds ($535 million), Highways Fund ($233 million), Treasury and Finance Administered Items ($149 million) and Health and Ageing ($147 million)

- ***Deposit accounts*** – South Australian Housing Trust ($72 million), Agents Indemnity Fund ($66 million), Waste to Resources Fund ($54 million), Rail Transport Facilitation Fund ($51 million) and SAFA ($46 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.

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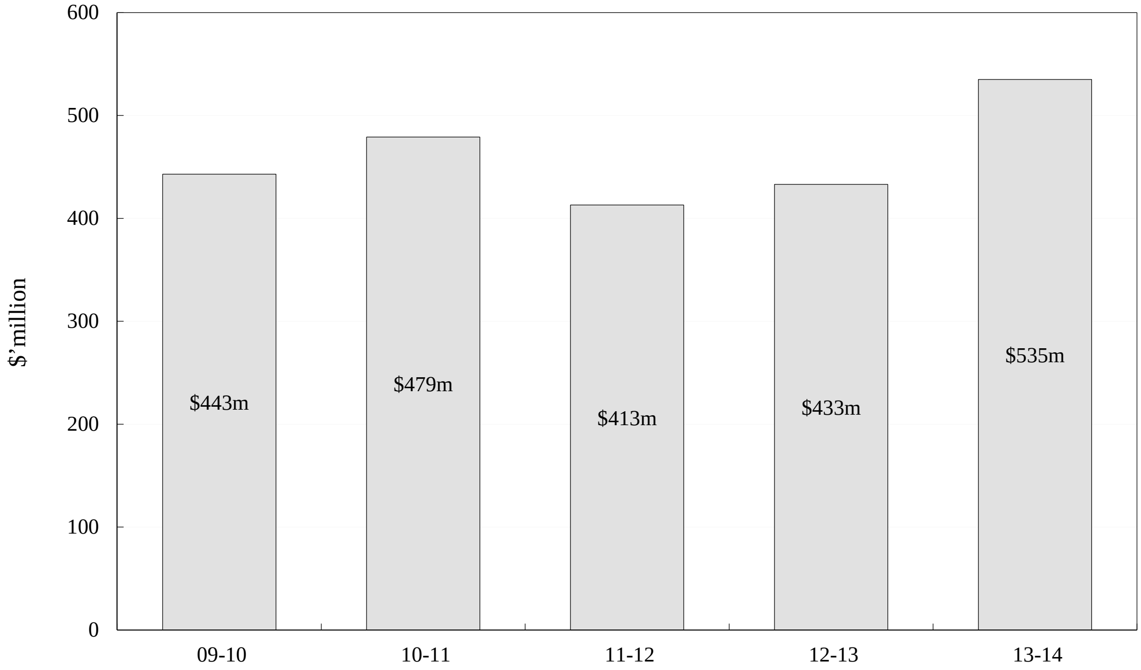
24 PFAA section 8(5) – any surplus of income over expenditure standing to the credit of a special deposit account must, at the direction of the Treasurer, be credited to the Consolidated Account.

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 2014 was $73.6 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 $303.23 million ($192.301 million in 2012-13) of surplus cash was returned to the Consolidated Account during 2013-14. The amounts were as follows.

Table 11.7 – Cash alignment policy repayments

Agency	**Total payments $'million**
Department of Treasury and Finance – Administered Items	213.6
Education and Child Development	45.6
South Australia Police	14.3
Defence SA	13.7
Treasury and Finance	6.1
Environment Protection Authority	5.4
Correctional Services	2.4
Manufacturing, Innovation, Trade, Resources and Energy	1.1
Auditor-General's	1.0

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 Schedule 1 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 SA Government.

Total equity contributions as at 30 June 2014 were $5164 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 the whole-of-government (WhOG) and general government sector financial reports. Accordingly, the 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 2013, therefore the following commentary has been kept purposely brief.

12.1 AASB 1049 key concepts

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
- 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 2012-13, a management letter was forwarded to DTF in December 2013 that contained reporting and operational improvements. The audit management letter was reproduced in full in the CFR report published by DTF.[25]

The matters raised included:

- non-compliance with AASB 1049 which requires explanations of major variances between the general government sector results and corresponding original budget amounts
- non-compliance with AASB 1023 General Insurance Contracts
- misclassification of asset transfers from the Department of Planning, Transport and Infrastructure to Renewal SA
- overstatement of the cash and cash equivalents.

Departmental response

DTF responded to Audit's comments with the following:

- the final budget outcome provides a detailed explanation of variance between the last revised budget and actual results. DTF notes that further disclosure of variations on a different basis in the CFR does not add valuable information for users
- appropriate summary disclosure as required by AASB 1023 will be identified and implemented in the 2013-14 CFR.

The misstatement of cash and cash equivalents and misclassification of the asset transfers were noted.

[25] Government of South Australia, CFR for the year ended 30 June 2013.

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 2013. 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 2013, 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

	2013 $'million	**2012 $'million**
Revenue from transactions		
Taxation revenues	**3 712**	3 483
Grant revenue	**8 119**	9 046
Charges for goods and services	**5 049**	4 651
Interest income	**821**	785
Dividends and income tax equivalents	**47**	37
Other revenues	**1 100**	898
Total revenues from transactions	**18 849**	18 900
Expenses from transactions		
Employee expenses	**7 190**	6 859
Superannuation interest cost	**314**	407
Other superannuation expenses	**705**	695
Depreciation and amortisation	**1 216**	1 131
Use of goods and services	**4 609**	4 555
Interest expenses	**1 159**	1 168
Grant expenses	**2 315**	2 479
Other operating expenses	**1 478**	1 642
Total expenses from transactions	**18 985**	18 936
Net result from transactions - Net operating balance	**(136)**	(36)
Other economic flows - included in net result		
Net foreign exchange gains	**114**	53
Net gain/(loss) on sale of non-financial assets	**(42)**	(11)
Net gain/(loss) on financial assets or liabilities at fair value	**127**	8
Net actuarial gains/(losses) of superannuation defined benefit plans	**2 314**	(4 429)
Other net actuarial gains/(losses)	**(411)**	(1 049)
Other economic flows	**(65)**	(75)
Total economic flows included in net result	**2 036**	(5 503)
Net result	**1 900**	(5 539)

Table 12.1 – CFR financial performance (continued)

	2013 $'million	2012 $'million
Other economic flows - other non-owner movements in equity		
Changes in property, plant and equipment ARR	**258**	1 695
Net gain/(loss) on financial assets at fair value	**10**	(5)
Prior period adjustments	**2**	39
Total other economic flows - non-owner movements in equity	**270**	1 729
Comprehensive result - change in net worth	**2 169**	(3 810)
Total change in net worth	**2 169**	(3 810)
Key fiscal aggregates		
Net operating balance	**(136)**	(36)
Less: Net acquisition of non-financial assets	**319**	1 361
Net lending/borrowing	**(456)**	(1 397)

The main variations in revenues in 2012-13 were as follows:

- ***Taxation revenues*** – increased by 6.6% or $229 million. This increase was mainly driven by an increase in payroll tax of $68 million, increase in stamp duties on property of $113 million and increase in motor vehicle registration taxes of $34 million.
- ***Grant revenue*** – decreased by 10.2% or $927 million. This decrease was mainly driven by a decrease in current and capital Commonwealth National Partnership grants of $322 million and $884 million respectively. These decreases were partially offset by an increase in current Commonwealth general purpose grants of $206 million
- ***Charges for goods and services*** – increased by 8.6% or $398 million. The increase was mainly driven by an increase in SA Water rates and charges for water services of $208 million as well as an increase in fees and levies received of $67 million

The main variations in expenses in 2012-13 were as follows:

- ***Employee expenses*** – increased by $332 million or 4.8%. This increase was due mainly to rising salary and wages costs of $294 million, an increase in TVSPs payments of $12 million and recognition of retention leave expenses of $33 million, all partially offset by a reduction in other employee related expenses of $31 million
- ***Grant expenses*** – decreased by $164 million or 6.6%. This decrease was due to declining recurrent grants of $133 million, a decrease in capital grant payments of $85 million and a decrease in other current transfer payments of $14 million, partially offset by an increase in subsidies payments of $49 million
- ***Other operating expenses*** – decreased by $164 million or 10%. This decrease was mainly due to a decrease in self-insurance claims of $247 million, partially offset by increases in workers compensation payments of $43 million, gambling prizes/dividends of $22 million and other expenses of $25 million

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 2013, 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

	2013 $'million	2012 $'million
Assets		
Financial assets		
Cash and deposits	**1 331**	946
Receivables	**1 267**	2 027
Advances paid	**2 584**	2 484
Investments, loans and placements	**8 082**	8 608
Investments - other	**18 422**	14 894
Interest in joint venture	**801**	799
Total financial assets	**32 486**	29 758
Non-financial assets		
Produced assets:		
Inventories	**560**	673
Machinery and equipment	**3 960**	3 214
Buildings and structures	**45 025**	43 954
Heritage assets	**1 128**	1 111
Biological assets	**74**	84
Intangibles	**94**	103
Non-financial assets held for sale or distribution	**6**	608
Other non-financial assets	**86**	134
Non-produced assets:		
Land	**12 091**	12 321
Intangibles	**349**	341
Non-financial assets held for sale or distribution	**140**	509
Total non-financial assets	**65 512**	63 051
Total assets	**95 998**	92 809
Liabilities		
Deposits held	**183**	237
Borrowing	**16 022**	14 907
Payables	**1 225**	2 078
Employee benefits	**2 547**	2 506
Superannuation	**11 085**	13 523
Superannuation fund deposits	**17 867**	15 142
Provisions (other than employee benefits)	**6 888**	6 590
Liabilities from non-financial assets held for sale or distribution	**-**	24
Other liabilities	**1 052**	843
Total liabilities	**56 869**	55 850
Net assets (liabilities)	**39 129**	36 960

Table 12.2 – CFR financial position (continued)

	2013 $'million	2012 $'million
Equity		
Retained earnings	**2 582**	(467)
Reserves:		
Asset revaluation reserve	**36 424**	36 708
Other reserves	**96**	702
Financial assets available for sale reserve	**27**	16
Total equity (net worth)	**39 129**	36 960

The main variations in assets in 2012-13 were as follows:

- ***Cash and deposits*** – increased by $385 million or 41%. This was mainly driven by an increase in SAFA short-term money market deposits
- ***Receivables*** – decreased by $760 million or 37%. This was mainly due to a decrease in derivatives receivable - SAFA foreign exchange swaps of $836 million and SAFA interest rate swaps of $68 million, offset by an increase in charges for goods and services of $271 million
- ***Investments - other*** – increased by $3529 million or 24%. This increase is due to an increase in equity investments held by Funds SA, WorkCoverSA and MAC
- ***Inventories*** **–** decreased by $113 million or 17%. This decrease is mainly due to a decrease of land held for resale of $87 million
- ***Machinery and equipment*** – increased by $746 million or 23%. This increase is due mainly to additions of $1178 million in 2012-13 and $73 million of capitalised expenditure offset by depreciation charges of $242 million
- ***Non-financial assets held for sale or distribution*** – decreased by $971 million due mainly to the sale of standing timber under the Treasurer's Implementation Deed with One-Forty-One and transfer of land held for sale to the Treasurer.

The main variations in liabilities in 2012-13 were as follows:

- ***Borrowing*** – increased by $1115 million or 7%. This increase is due to an increase in debt security holdings of $1114 million
- ***Payables*** – decreased by $853 million or 41%. This decrease is due mainly to a decrease in derivatives payable - SAFA foreign exchange swaps of $841 million
- ***Superannuation*** – decreased by $2438 million or 18%. This decrease is due mainly to a decrease in the State's defined benefit obligation. The decrease in the defined benefit obligation was impacted by the increase in the long-term Commonwealth bond rate, which is a key determinant of the actuarial calculation
- ***Superannuation fund deposit liabilities*** – increased by $2725 million or 18%. This reflects an increase in the liability of Funds SA to all superannuation plans.

Acronyms used in this Report

Acronym	Description
AAS	Australian Accounting Standard[1]
AASB	Australian Accounting Standards Board
ABS	Australian Bureau of Statistics
BRCC	Budget Review Cabinet Committee
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.