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Government
of South Australia

Report

of the

Auditor-General

Annual Report

for the

year ended 30 June 2011

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State finances and related matters

1 Introduction

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 2011-12 Budget, supplemented with information provided by the Department of Treasury and Finance (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 2010-11. Past experience is that actual results have varied, sometimes substantially, from the estimated result.
- Classification changes occur from year to year in revenue and expense definitions that can affect the comparability of individual items across the time series. Such changes do not generally affect the net lending (borrowing) result. Budget Papers explain structural breaks in time series.

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

2 Overview of State finances

2.1 Overview

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

2.2 Fiscal strategy

Each budget the Government sets out its fiscal strategy and its broader fiscal targets, together with performance against those targets. The 2009-10 Budget was set against the backdrop of uncertainty as economies emerged from the worst of the global financial crisis. The crisis had a striking effect on the State's finances. 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. The announced fiscal strategy was to return the State to sustainable surpluses in the medium-term. The 2009-10 Budget built on earlier savings measures and contained a range of budget improvement targets for which specific measures were to be identified in the 2010-11 Budget.

The fiscal strategy for the 2010-11 Budget was to establish and maintain sustainable surpluses. An operating deficit of $389 million was budgeted for 2010-11 with a return to initially small but growing surpluses. The budget detailed significant budget improvement measures adopted from the then Sustainable Budget Commission's recommendations. These measures and a moderation in infrastructure spending were anticipated to return the Budget to surplus on both an operating and net lending basis by 2013-14.

The 2011-12 Budget Statement (Budget Paper 3) reports the Budget was prepared in an environment of deteriorating revenues, with taxation and GST revenues remaining significantly below estimates made prior to the global financial crisis, and those estimated in the 2010-11 Budget. A key fiscal strategy of the 2011-12 Budget is to re-establish and maintain sustainable operating surpluses. The estimated result for 2010-11, a deficit of $427 million, is in line with the 2010-11 Budget. An operating deficit of $263 million is now budgeted for 2011-12 compared to a surplus of $55 million estimated at the time of the 2010-11 Budget. Operating surpluses are projected from 2012-13 although at lower levels than in the previous budget. The budget also is not projected to return to net lending surplus until 2014-15, a year later than previously forecast.

The Budget introduces modest revenue and savings measures compared to the previous two budgets but included the announcement that the Government was considering creating a new lotteries licence for the Lotteries Commission of South Australia (SA Lotteries). Success in meeting the Budget targets is dependent on achieving both these and previously announced improvement measures in 2011-12 and following years.

Of the Government's broader fiscal targets, two are not expected to be achieved in part of the four year period of the 2011-12 Budget namely:

- at least a net operating balance in the general government sector in every year. A net operating deficit of $263 million is budgeted for 2011-12.

- net lending outcomes that ensure the ratio of net financial liabilities to revenue continues to decline towards that of other triple-A rated states. The ratio is forecast to increase across the forward estimates peaking in 2013-14 before declining in 2014-15. Trends for other states are shown in chart 10.3 in this Report.

2.2.1 The State credit rating

Another of the fiscal targets is to ensure that risks to state finances are managed prudently to maintain a triple-A credit rating.

South Australia has had a triple-A credit rating since September 2004. When the 2011-12 Budget was released, credit rating agencies including Moody's and Standard & Poor's announced the State's rating was unlikely to change. Factors influencing their views included:

- Australia's strong institutional framework and demonstrated fiscal discipline continue to support South Australia's rating
- the expectation that the State's savings measures will partly mitigate the impact of lower revenues
- the expectation that South Australia will continue to manage its finances prudently over the next two years.

Standard & Poor's noted that a return to surplus will depend partly on a decrease in operating expenditure they regarded as ambitious. Moody's noted that continued progress in carrying out recommendations of the State's 'Sustainable Budget Commission' will be of key importance in bringing the general government back into balance. Moody's commented that greater exercise of expenditure constraints will be particularly important as the Budget redress relies upon a very slow pace of expenditure growth. Moody's also noted that this is likely to be challenged by wage outcomes and ongoing pressures on health care and other services.

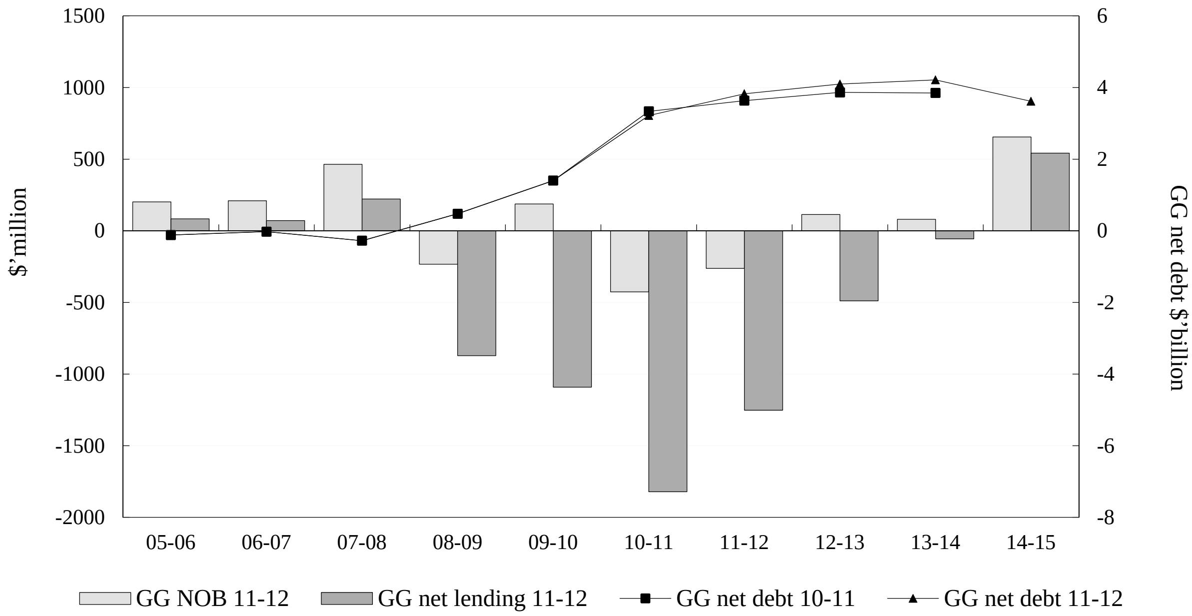
In late September 2011, Standard & Poor's issued a statement confirming the triple A rating but revising its outlook on the State to negative, from stable. Standard & Poor's stated the outlook revision reflects their concerns that the Government will not achieve its ambitious savings measures, and that its budgetary position will not improve as forecast over the medium term. They also stated that further weighing on the rating, was the State exceeding the non-financial public sector net financial liabilities ratio of 80 percent to 90 percent of operating revenues, as set by Standard & Poor's. They noted a decline back into this range in 2015 is dependent on the delivery of the ambitious savings measures. Pressure could also be placed on the ratings if WorkCoverSA's liability continues to grow unabated.

Standard & Poor's concluded that a return to a stable outlook is possible if the Government reaches its targets or alternatively, slippage in the delivery of the savings targets may result in a ratings downgrade.

2.3 Changing financial position

The following chart shows changes occurring or anticipated in some of the key financial indicators over a 10 year period to 2014-15 for the general government sector.

Chart 2.1 – General government sector net operating balance (NOB), net lending and net debt



The chart highlights the six year period from 2008-09 to 2013-14 where net operating deficits or small surpluses occurred or are expected. Net lending deficits (where revenues are less than operating and investment expenditure) are also incurred or projected for each of the six years. As a consequence, net debt rises from a surplus cash position of $276 million in 2007-08 to peak at $4.2 billion in 2013-14.

While the operating results for the six year period are influenced by the global financial crisis, the net lending deficits are mainly influenced by capital investment spending decisions. Over $5 billion is spent or estimated to be spent on net acquisition of non-financial assets for the six year period from 2008-09 to 2013-14.

The Government adopted a strategy of net operating balance surpluses and net lending deficits (borrowing to finance higher capital spending) in the 2006-07 Budget. The budgeted net lending deficits would, in turn and if realised, lead to rising net debt. The strategy was maintained through to the 2008-09 Budget but with net lending deficits and net debt expected to increase with each budget in response to escalating capital programs.

The general government net debt 2010-11 line illustrates what was anticipated in the 2010-11 Budget. Since the global financial crisis, the State has incurred operating deficits in 2008-09 and 2010-11 which, together with higher capital spending, leads to higher than previously projected net borrowing for the three years 2011-12 to 2013-14.

As occurred in the 2010-11 Budget, the 2011-12 Budget projects net operating results lower than previously budgeted and net lending deficits that are higher than previously budgeted. Consequently, it is anticipated net debt will increase more than previously projected and is now expected to reach $4.2 billion (previously estimated at $3.8 billion) in 2013-14.

Chart 2.1 highlights how the settings of the 2011-12 Budget, which build on initiatives and announcements since the 2008-09 MYBR, are expected to lead to improved results reaching a targeted operating surplus of $655 million (previously projected at $840 million) and net lending surplus of $542 million (previously projected at $689 million) in 2014-15. The estimated net lending surplus in 2014-15 in turn reduces net debt.

The chart also highlights that from 2011-12 to 2013-14, there is little room for unfavourable outcomes without increasing the risk of achieving longer term targets.

2.4 Operating Statement

2.4.1 Estimated results for 2010-11

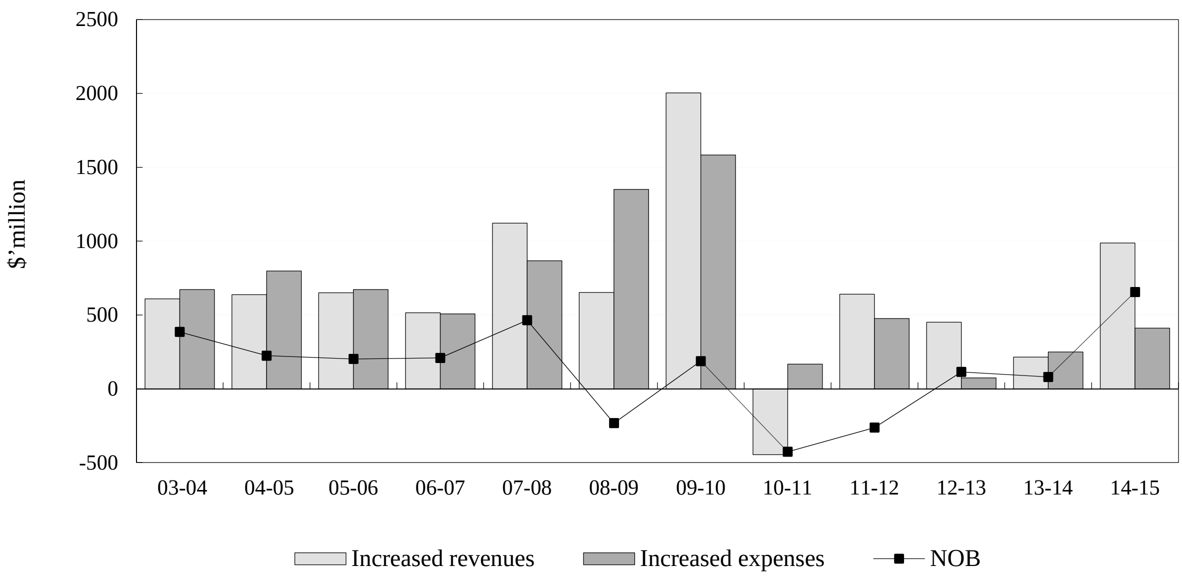
The 2011-12 Budget Papers show the operating result for 2010-11 is estimated as a net operating balance deficit of $427 million compared to the budgeted deficit of $389 million. The variation is principally due to lower than budgeted grant revenues and higher than estimated interest expenses.

The net lending deficit is estimated to be $1821 million, compared to the budgeted $1791 million, the difference being due to the decline in the net operating balance result. The general government sector is estimated to have net debt of $3217 million at the end of 2010-11, $118 million lower than was budgeted. The improved position is due to a better than anticipated opening balance of net debt as at 1 July 2010. At the time of the 2010-11 Budget, net debt at 30 June 2010 was estimated at $1.6 billion. The actual position at 30 June 2010 was $1.4 billion.

2.4.2 Budget forecasts 2011-12 to 2014-15

Chart 2.2 shows annual increases in revenues and expenses since 2003-04 compared to annual changes estimated for the four years of the 2011-12 Budget together with each year's net operating balance.

Chart 2.2 – 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.

As shown, in the five years to 2007-08, annual increases in revenues and expenses were reasonably consistent and the net operating surpluses were achieved over the period. The global financial crisis affected 2008-09 and a net operating deficit was incurred. The annual movements from 2008-09 to 2010-11 are influenced by changes in Commonwealth funding including stimulus grants which peaked in 2009-10.

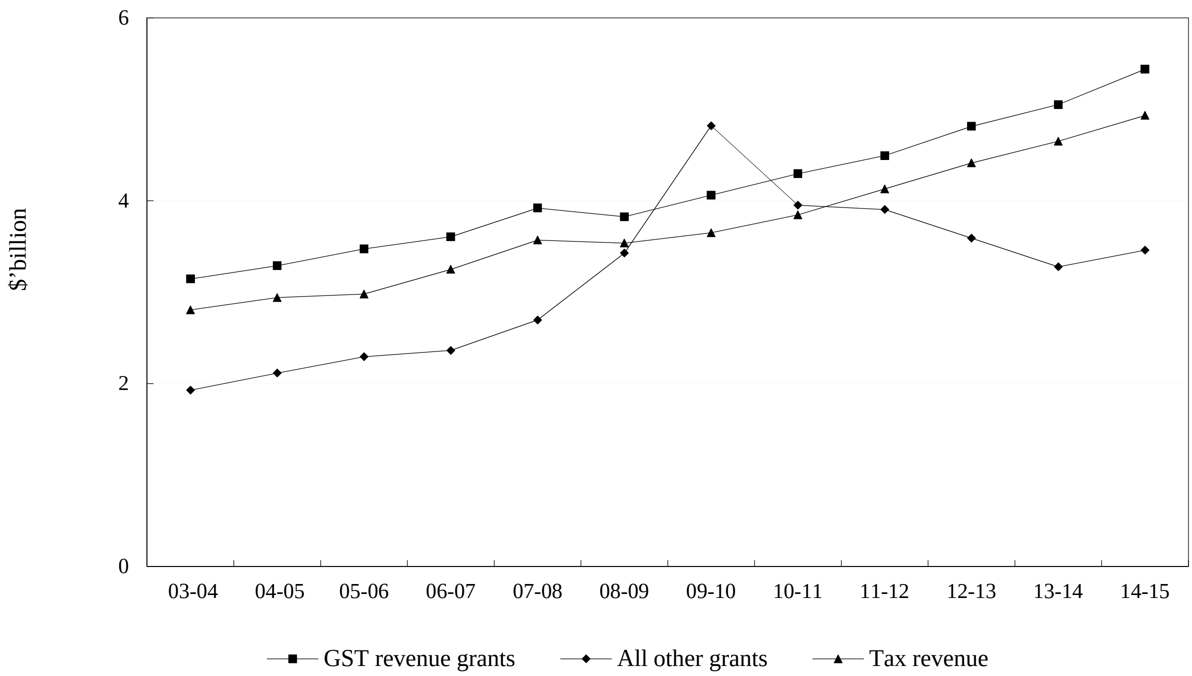
The chart shows that for the four years of the 2011-12 Budget revenues are estimated to grow annually, particularly in 2014-15. It also highlights the expenditure restraint anticipated over those four years compared to earlier years. The projected net operating surplus for 2014-15 of $655 million is the highest of any year on the chart.

2.4.3 Revenue forecasts 2011-12 to 2014-15

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

Chart 2.3 shows expected trends for the major revenue items in the 2011-12 Budget against the experience of the eight years to 2010-11.

Chart 2.3 – General government sector Commonwealth grants and taxation revenue



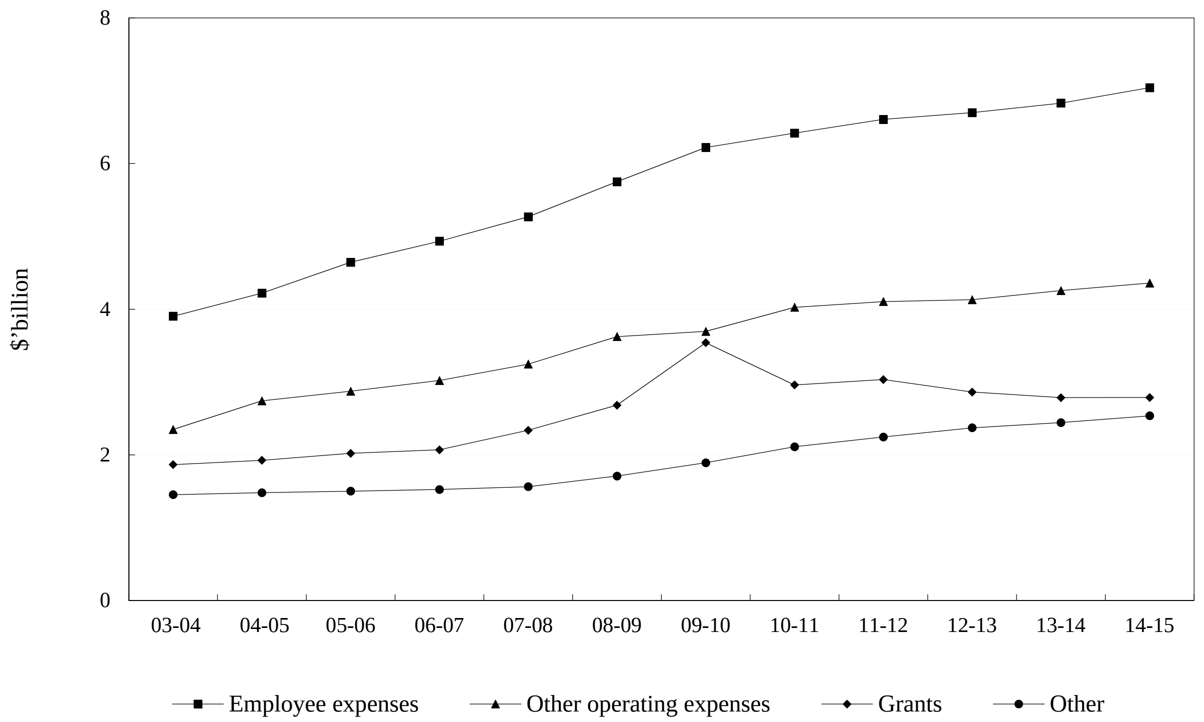
The chart highlights the break in trend when GST revenue grants and taxation revenue fell in 2008-09 with the onset of the global financial crisis. Both revenue streams have increased since 2008-09 and are, now estimated to grow annually, in real terms, over the forward estimates on the assumption that economic growth will improve over the forward estimates period. The trends shown in the chart suggest that the revenue projections from 2011-12 to 2014-15 are consistent with past years with the exception of 2008-09.

All other grants, principally other Commonwealth grants, increased markedly in 2008-09 and 2009-10 mainly due to the Commonwealth Government's Nation Building – Economic Stimulus Plan and Nation Building Plan for the Future capital grants. Other Commonwealth grants reduce after 2009-10 reflecting payment profiles agreed with the Commonwealth including the cessation of some agreements. Importantly, these monies are required to be spent on projects and are not available as general purpose revenue. The grants are mainly on-passed to recipients as grant expenses or are used for specific capital spending programs.

2.4.4 Expense forecasts 2011-12 to 2014-15

Chart 2.4 shows trends expected for total expenses in the 2011-12 Budget split into four main categories, against the experience of recent years.

Chart 2.4 – General government sector expenses

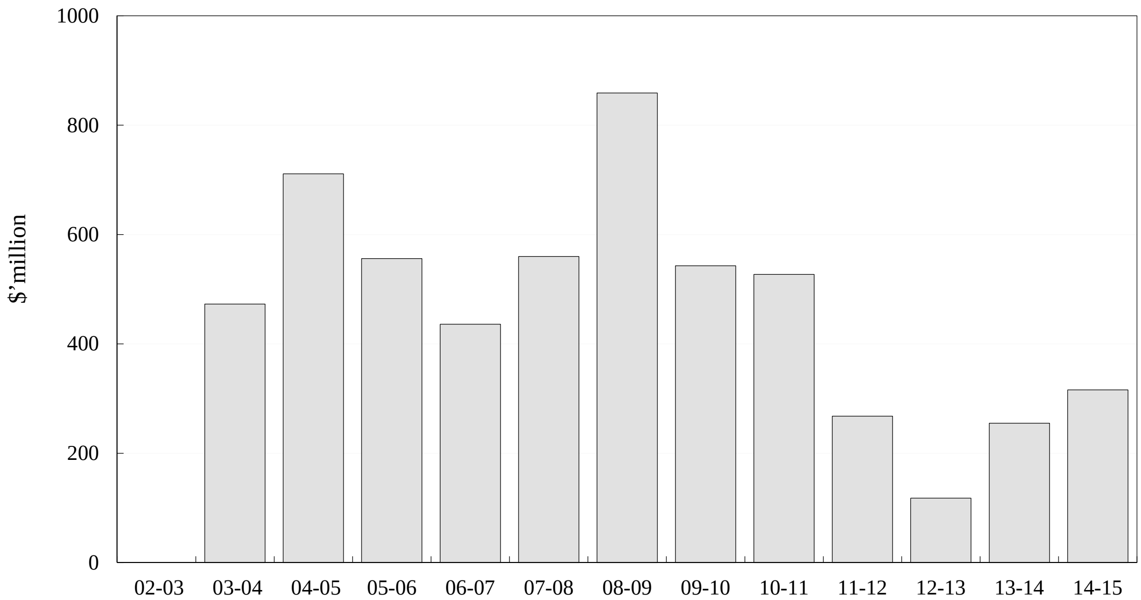


All categories of expenses except grants are estimated to increase in 2010-11 and beyond. The decrease in grant expenses is largely associated with Commonwealth grant revenues discussed above. These grant expenses reduce in line with related grant revenues.

The challenging dimension of expenditure restraint underlying the 2011-12 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 sixty-seven precent of expenses for 2011-12, a proportion that is consistent with most years.

Chart 2.5 shows the annual movements projected for employee expenses and other operating expenses for the four years to 2014-15 are below all of the previous eight years' experience.

Chart 2.5 – Annual change in employee and other operating expenses



Integral to the expenditure restraint is achieving savings initiatives built into the forward estimates in the previous three budgets. As commented last year, achieving these expenditure targets is a major task and therefore a risk to the current budget strategy.

2.4.5 Net acquisition of non-financial assets

Net acquisition of non-financial assets, the balance of purchases of non-financial assets less sales of non-financial assets and depreciation, for 2010-11 is estimated to be $1.4 billion, in line with budget. In arriving at this result, both purchases of non-financial assets and sales of non-financial assets were about $100 million under budget.

Net acquisition of non-financial assets for 2011-12 is budgeted at $988 million. While purchases of non-financial assets remain at $2.1 billion, sales of non-financial assets of $369 million are up $267 million from the previous year. Purchases of non-financial assets reduce across the four years to $1.1 billion in 2014-15. Sales of non-financial assets are estimated to reach $418 million in 2012-13 and reduce to $45 million in 2014-15.

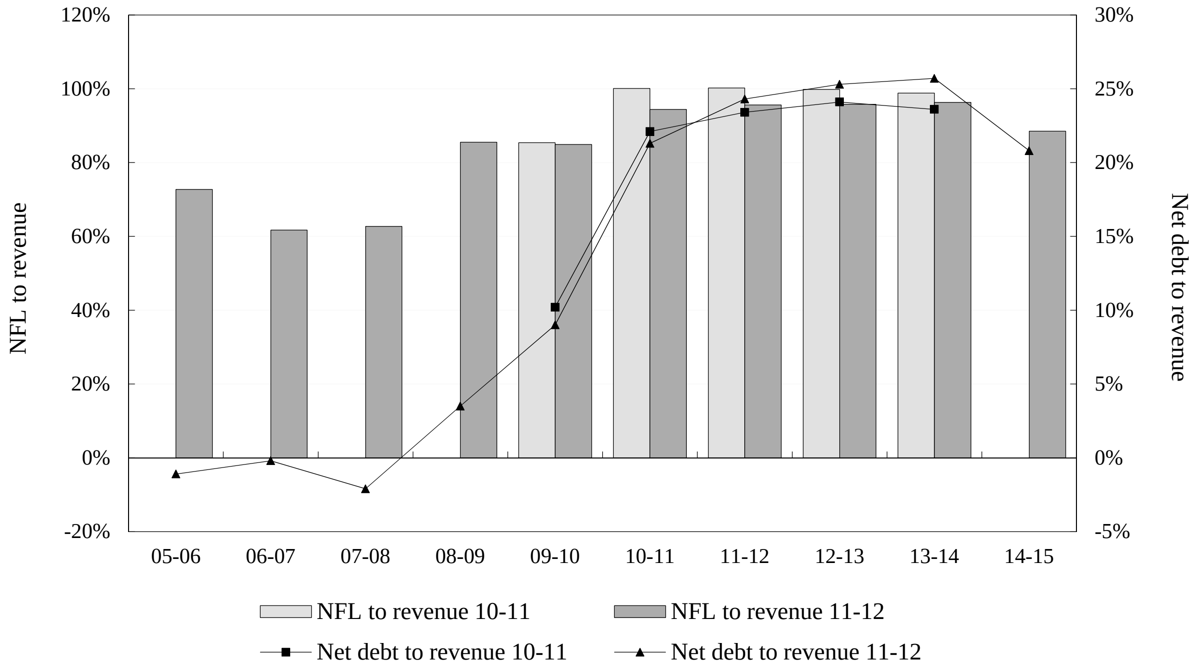
The estimated sales in the forward estimates for the non-financial public sector include proceeds from the forward sale of up to three harvest rotations for ForestrySA plantations and a proposed sub-licence giving the right to operate the SA Lotteries' brands and business for a defined period of time. These are discussed in section 2.6.7.2 Asset sales.

2.4.6 Ratios of net financial liabilities to revenue and net debt to revenue

One of the Government's fiscal targets is 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. Another of its key general government budget indicators is the ratio of net debt to revenue.

Chart 2.6 shows the ratios of net financial liabilities and net debt to revenue for recent years and for the 2010-11 and 2011-12 Budgets.

Chart 2.6 – General government sector ratios of net financial liabilities to revenue and net debt to revenue Budget comparisons



The chart shows that both the ratios of net financial liabilities to revenue and net debt to revenue were projected to increase in the 2010-11 Budget, peaking in 2011-12 and 2012-13 respectively. This outcome is not consistent with its related fiscal target, but the ratio declines in 2014-15 when the net lending position returns to surplus. Movements in the ratio reflect the operating deficits expected and the capital expenditure program, financed in part by borrowings. Net financial liabilities are also influenced by changes in the value of unfunded superannuation liabilities.

The ratio of net financial liabilities to revenue is lower across the forward estimates than previously budgeted due to the lower estimated value of unfunded superannuation liabilities. This in turn reflects the higher discount rate assumptions in this budget. Chart 10.3 in section 10 of this Report sets out the five year estimates to 2014-15 including for other states. It shows the similarity of estimates for this ratio between South Australia and New South Wales and Victoria.

The 2011-12 Budget projects that net debt will rise higher than was previously estimated in the 2010-11 Budget. Consequently the ratio of net debt to revenue is higher than previously budgeted. The ratio peaks in 2013-14.

2.4.7 Interstate comparison

Section 10 of this Report includes comment on 2011-12 Budget comparisons for key budget aggregates across jurisdictions. In 2011-12, South Australia, New South Wales, Tasmania, and Queensland are forecasting general government net operating balance deficits. Victoria and Western Australia have budgeted net operating surpluses. All other jurisdictions are predicting net lending deficits (borrowing) up to 2014-15 except Victoria in 2013-14 and South Australia in 2014-15. 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 2011-12 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 up to 2013-14 due to the growth of financial liabilities and improves in 2014-15 when borrowings are estimated to reduce.

Net worth is estimated to add $3.3 billion over the forward estimates to reach $40.7 billion by 2014-15.

2.5.1 Assets

Total assets are estimated to increase by $251 million in 2010-11 to over $58 billion and are expected to continue to rise over the forward estimates to $63 billion by 2014-15. Net acquisitions (purchases less depreciation and asset sales) increase non-financial assets by $2 billion in 2010-11 and add a further $1.3 billion through to 2014-15. Revaluations are also estimated to add substantially to non-financial assets. Rising property values have had a marked positive influence on the Balance Sheet over a number of years, particularly from growth in the value of rental properties of the South Australian Housing Trust.

Total financial assets are expected to be $2.9 billion in 2010-11, rising to $3.3 billion in 2014-15.

Included in financial assets is the value of the Government's interest in Public Financial Corporations including the Motor Accident Commission and WorkCover Corporation of South Australia (WorkCoverSA). Investment market conditions through 2010-11 contributed to increases in the market value of investment assets. The Superannuation Funds Management Corporation of South Australia (Funds SA), which manages the majority of the Government's financial assets, reported net income of $1.6 billion compared to $1.5 billion in 2009-10. As the managed funds include superannuation assets, this result will contribute to managing the unfunded superannuation liability.

Positive market returns and an improved underwriting result contributed to the Motor Accident Commission reporting a comprehensive profit result for the year of $193 million, up from $168 million. The Commission's statutory solvency level, calculated in accordance with a formula determined by the Treasurer, improved to 103.6 percent (97.1 percent) of the target level of solvency. As at 30 June 2011 the Commission had net assets of $431 million ($239 million). WorkCoverSA, which manages its own investments, also reported a profit in 2010-11. The comprehensive result for the year was a profit of $30 million ($77 million). This contributed to an improvement in its funding ratio to 64.8 percent from 61.5 percent, compared to its approved target funding range of 90 to 110 percent. As at 30 June 2011 WorkCoverSA had a net liability position of $952 million ($982 million).

[1] Balance Sheet data is for the non-financial public sector unless otherwise stated due to the high value of non-financial assets in public non-financial corporations.

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 by $2.4 billion to $6.9 billion at 30 June 2011 and to $7.6 billion by 2014-15. The general government sector net debt is estimated to increase to $3.2 billion at 30 June 2011 rising to $4.2 billion in 2013-14 and then decrease to $3.6 billion by 2014-15. In 2015-16 net debt will include the effect of accounting for the new Royal Adelaide Hospital discussed further in section 2.6.7.1 Public private partnership projects.

The other major component of liabilities, unfunded superannuation liabilities, are estimated to be $8.7 billion for the year to 30 June 2011, an improvement on the 2010-11 budgeted expectation of $9.4 billion. The improvement is mainly due to the following:

- 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 Australian Accounting Standards. A discount rate of 5.6 percent was used for the estimate as at the 2011-12 Budget, compared with 5.3 percent for the 2010-11 Budget. A 1 percent rise in the discount rate is estimated to decrease the superannuation liability by $1.5 billion.

- Improvement in actual returns from investment markets. The assumed earnings rate for 2010-11 of 12.9 percent compares to the long term assumption of 7 percent. The actual earnings rate in 2009-10 was negative 17.6 percent. A 1 percentage point higher than expected return would reduce the estimated unfunded superannuation liabilities by around $46 million.

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 multibillion dollar revisions to the value of the liability recorded on the Balance Sheet, there has been no material change in the actual expected payments to beneficiaries underlying the liability.

The Government reports that it remains committed to fully fund the superannuation liability by 2034.

2.6 Risks and management tasks for the 2011-12 Budget

As noted, the stated fiscal strategy of the 2011-12 Budget is to re-establish and maintain sustainable operating surpluses. Key elements to the success of the Budget will be achieving estimated real growth in major revenue items, realising expenditure restraint arising from previously announced budget measures and achieving the estimated value of proposed asset sales.

Audit sought DTF's view of which areas of the Budget are considered to be the highest risks and any specific monitoring measures. DTF responded that the major risks to the fiscal outlook are set out in Chapter 6 of the 2011-12 Budget Statement (Budget Paper 3). These include the impact of economic activity on household spending patterns and demand for housing, which impact on GST and property taxation, and expenditure risks such as higher than expected wage increases, cost escalations on capital projects and activity growth in hospitals.

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 2011-12 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 2011-12 Budget estimates are based upon information submitted by agencies throughout the year relating to the following processes:

- Cabinet decisions
- carryovers
- impacting data adjustments
- mid-year review adjustments
- 2011-12 Budget measures.

Agencies submit journals to DTF via the DTF's Budget and Monitoring System to update their budget estimates. These journals are subject to a range of integrity checks to ensure the correct application of accounting principles and that they are consistent with the relevant decisions of Government. DTF establishes and maintains detailed process guidelines which are communicated to agencies at the start of each budget process. These guidelines establish timeframes not only for agencies but also for account management teams within the DTF Finance Branch, whose fundamental role is to ensure the quality and reasonableness of the financial data submitted by agencies.

During this period account managers ensure that all fields on coversheets, which form the primary source of information about a proposal, are completed appropriately and that the financial data in journals is accurate and have full accounting integrity. DTF liaises with agencies at this stage to seek additional supporting information if required or to resolve any inconsistencies in the data provided. Quality assurance reports have been developed to aid in the detection of common problems associated with coversheets and journals.

Audit also sought details of the key assumptions and adjustments made in quantifying the forward estimates figures for 2012-13 to 2014-15. DTF responded that the forward estimates figures are calculated by consolidating approved budgets for individual government agencies. These incorporate government policy decisions and parameter variations relating to the operations of agencies, such as the quantity of services provided.

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2 Budget Statement 2010-11, Budget Paper 3, Chapter 6.

In estimating revenue items, DTF may apply some assumptions. These assumptions are outlined in Chapter 3 of the Budget Statement, Budget Paper 3.

2.6.1 Net operating balance

As noted, one of the Government's broader fiscal targets is to achieve at least a net operating balance in the general government sector in every year. This means there are sufficient revenues to meet expenses every year. The 2011-12 Budget estimates net operating deficits for 2010-11 and 2011-12 meaning that since 2008-09, net operating deficits are incurred in three of the four year period to 2011-12. The cumulative value of the operating deficits is $923 million.

Table 2.1 shows the impact of the global financial crisis by tracking how net operating result estimates 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
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			*(427)	(263)	114	80	655

* 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.

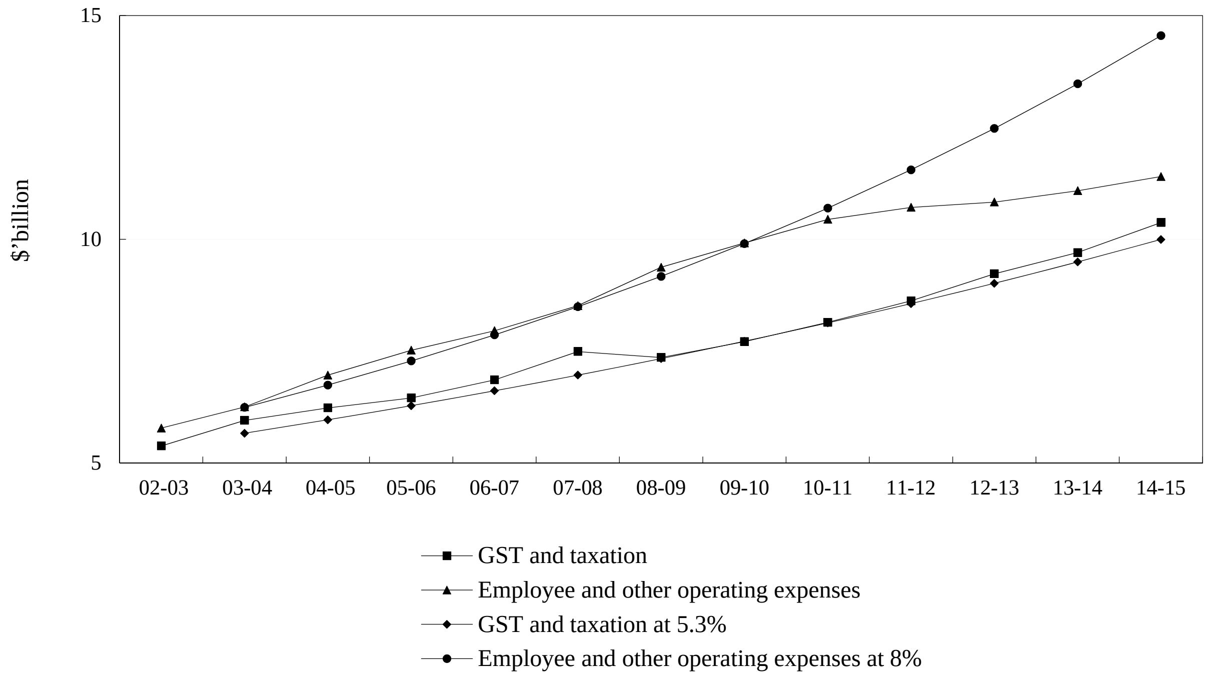
Notably, for the estimates for the years 2010-11 to 2014-15, successive budgets have lowered the estimated net operating result from the previous budget with 2010-11 and 2011-12 becoming estimated deficits. The changes since the estimated surpluses of the 2008-09 Budget, before the global financial crisis, represent a $2.2 billion unfavourable turnaround over the four years to 2011-12 in the changed economic environment. As discussed later in this Report, there remains a high degree of uncertainty in the global economic environment.

The net operating surpluses estimated for 2012-13 and 2013-14 provide some flexibility and buffer against unfavourable influences and events that may affect outcomes.

Buffers are also 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 2011-12 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 2.7 compares trends for some previously discussed key revenue and expenses items in the Budget namely GST and taxation revenue and employee expenses and other operating expenses.

Chart 2.7 – Comparison of GST and taxation revenue and employee expenses and other operating expenses



In chart 2.7, the GST and taxation revenue line tracks actual revenues up to 2009-10 and estimated revenues from 2010-11 to 2014-15. For the seven years to 2009-10, these combined two items grew on average annually by about 5.3 percent. Applying this average growth rate from 2002-03 through to 2014-15 creates the GST and taxation revenue at 5.3 percent line. It can be seen by the closeness of the two lines that the 2011-12 Budget estimates are consistent with that past average experience. Further comments on operating revenue risks follow in the section 2.6.2 Operating revenues.

For the seven years to 2009-10 combined employee expenses and other operating expenses grew on average annually by about 8 percent. Applying this average growth rate from 2002-03 through to 2014-15 creates the employee expenses and other operating expenses at 8 percent line. Comparing the trend of this line to the estimated expenses for the 2011-12 Budget shows a diverging difference between the two lines. This difference highlights the significance of the expenditure restraint required from the 2011-12 Budget.

2.6.2 Operating revenues

As mentioned, the estimated result for 2010-11 is that the main revenue lines, GST and taxation revenue, are less than budgeted. Even so, both revenue lines grew in real terms for 2010-11 and are projected to do so for the next four years. GST revenue has now shown to be highly sensitive to household spending patterns. State taxation also varies with economic activity and demand for housing.

Internationally, there remain risks since the global financial crisis, including the sovereign debt issues of some European Union nations, the United States of America's fiscal position and the speed and strength of the Japanese recovery. The continuing volatility of international equity markets evidences the uncertainty associated with these and other risks.

In September 2011 the Governor of the Reserve Bank of Australia in a statement on the month's monetary policy decision, stated that the outlook for the global economy is less clear than it was earlier in the year. He noted that uncertainty and financial volatility is reducing confidence and may result in more cautious behaviour by firms and households in major countries and that a number of forecasters have scaled back their global growth estimates over the past couple of months. Domestically he stated that overall, the near-term growth outlook continues to look somewhat weaker than was expected a few months ago. Beyond the near term, growth is still likely to be at trend or higher, unless the world economic outlook continues to deteriorate.

In late September 2011, the International Monetary Fund (IMF) in a briefing on the world economic outlook, revised down its forecast for world growth. It noted that recovery in the global economy had weakened considerably, and downside risks had increased sharply. The IMF stated that strong policies were needed both to improve the outlook and to reduce the risks.

GST revenue in 2010-11 is estimated at $4.3 billion, representing 28 percent 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 the timing of Commonwealth specific purpose and National Partnership grant funding to the State over the period 2009-10 to 2012-13. They are also impacted by revised assessment methods for the treatment of jurisdictions' capital needs.

In August 2011 the Commonwealth and all state and territory governments finalised a new national health agreement. The State Government announced that the new agreement meant additional funding would be available to the State from 2014-15. While not included in the 2011-12 Budget, the new agreement should benefit longer term revenues.

The two main elements of state taxation are payroll tax and conveyance duty. Growth in payroll tax is based on expected continuing solid employment growth. For conveyance duty, property market conditions are expected to improve, returning to their long-term trend level by the end of the forward estimates period.

Risk analysis in the Budget Papers notes that:

- a 1 percent change in GST pool growth has a revenue impact for South Australia of about $42 million per annum

- a variance of 1 percent in state taxation revenue, not including GST revenues, equates to about $41 million per annum.

2.6.3 Operating expenses

In the absence of better than budgeted revenue outcomes, the key to achieving the Budget operating result targets is to control expenses. The 2011-12 Budget expects significant restraint in spending. Past Auditor-General's Reports have included commentary on operating expense variations. The Budget Papers provide summary details of parameter and policy changes that occur between budgets that typically have added hundreds of millions to spending commitments.

Parameter effects 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. Audit notes that parameter effects since the 2010-11 Budget have added $897 million (before provisions) to operating expenses over four years to 2013-14.

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

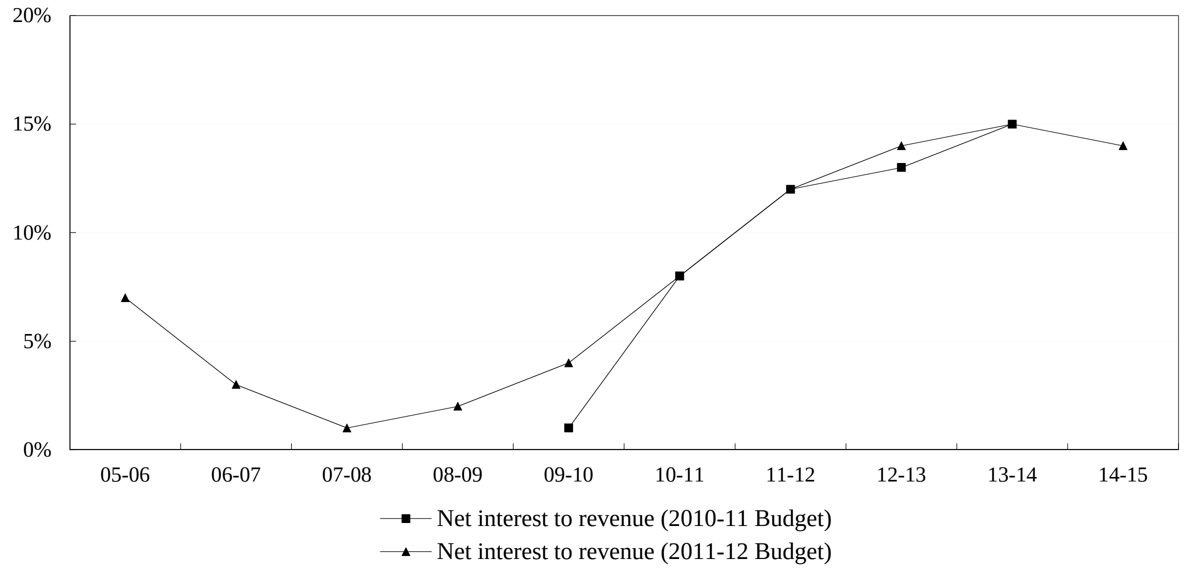
The Budget records that if public sector wide wage outcomes for new enterprise agreements vary by 1 percent per annum from allowances in the forward estimates, the Budget impact will be approximately $225 million in 2014-15.

The 2011-12 Budget reports that policy decisions since the 2010-11 Budget have added $461 million (before provisions) to operating expenses over four years to 2013-14. 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 2011-12 Budget settings.

2.6.4 Ratio of interest to revenue

In the 2011-12 Budget, interest expenses are expected to rise over the forward estimates reflecting a higher level of borrowings up to 2013-14, as a consequence of the net lending deficits and an expectation that interest rates applicable to government debt will rise moderately across the forward estimates. Chart 2.8 shows the outcomes for the general government ratio of net interest expense to revenue for recent years and as estimated in the 2010-11 and 2011-12 Budgets.

Chart 2.8 – General government sector interest to revenue ratio



This chart shows the ratio of net interest to revenue rising steeply from 2009-10 to 2013-14. On current projections this ratio is in line over the forward years, other than 2012-13, with what was estimated for the 2010-11 Budget. As mentioned, net debt rises over the period of the forward estimates higher than was budgeted for 2010-11.

Exposure to rising interest rates is heightened through the increase in net debt. The Budget notes that a 1 percent increase in the average interest rate applying to general government sector debt would increase net interest expense by approximately $33 million in 2011-12 rising to $39 million in 2014-15.

2.6.5 Savings initiatives

Setting large savings targets is a feature of past Budgets. The 2010-11 Budget consolidated savings announced in earlier budgets (of over $700 million per annum by 2013-14) and new savings totalling $1.5 billion over the next four years arising from the recommendations of the Sustainable Budget Commission. These were additional to cost recovery and revenue measures ($478.6 million) and some retained savings included in agencies from previous budgets. The 2010-11 Budget papers itemised the new savings initiatives in Budget Paper 6 '2010-11 Budget Measures Statement'. This provided a reference for monitoring progress of those initiatives. The Budget Papers did not restate initiatives scheduled to commence in 2010-11, or that were not fully implemented, from previous Budgets.

The savings task falls on all portfolios of Government. There has been mixed success in previous years in meeting savings targets. It is well known that health and, to a lesser but nonetheless substantial degree, families and community service areas, have either found savings targets difficult to meet over time or have other service demands that have necessitated additional funding.

In response to Audit inquiries about progress with the operating savings for 2010-11, DTF advised that generally, agencies achieved their allocated savings targets. In some cases where agencies did not achieve the specific saving (eg for timing reasons) they found a replacement saving to meet the overall target. Audit notes that methods vary across agencies. One method of achieving savings in the period was to hold vacant positions to offset budget pressures while others managed through reductions in other expenditure lines rather than FTE numbers. The largest exception was in Health which had a $10.9 million shortfall relating to an unachieved outpatient services reforms measure.

DTF also confirmed reductions to the new savings targets of $62 million for the three years 2011-12 to 2013-14. The main reduction arose from the Government's decision not to proceed with the measure that was to replace the recreation leave loading provision for specified public sector employees with an additional recreation leave entitlement of two days per annum. This resulted in an adverse impact on the Budget of around $23 million per annum commencing from 2012-13.

There remains in excess of $1.3 billion of new savings to be achieved for the three years to 2013-14. The Department of Health has the largest individual agency savings target with savings for the three years of $298 million. Table 8.4 in this Report provides details of savings by portfolio.

Another major savings area is the shared services initiative. In Part A of this Annual Report to Parliament, I reported that various factors have meant that up to 2009-10, the shared services initiative has not met its original savings targets, falling $42.8 million short of the original budgeted savings of $130 million. A discussion of Shared Services SA activities is in Part A of this Report.

I refer to these various instances as examples to demonstrate the difficult nature and extent of the savings task and risks to be mitigated in managing the achievement of the 2011-12 Budget outcomes.

I noted last year that an inherent risk of the saving strategy is its sheer size and breadth. Achieving the task will require significant discipline. Agencies have developed experience with implementing savings strategies over recent years but the savings targets are not always achievable by all agencies. The remaining savings task is of a much greater scale. It presents risks including industrial action and public demand to maintain services. Implementing savings tends to be directed at administrative and support areas for services. As the remaining savings targets are pursued, care needs to be taken that where this occurs, relevant changes to systems and procedures within a risk management context is addressed, to ensure the public interest is continually served by efficient and effective administrative performance and failures avoided.

2.6.6 Full-time equivalents reduction management strategy

A key part of the 2010-11 savings strategy is to further reduce public sector full-time equivalents (FTEs) by 3743 FTEs excluding increases from other initiatives. At an average savings of $70 000 per year per FTE, this measure is expected to achieve savings of $262 million per annum if fully implemented by 2013-14. To assist agencies to achieve this 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 (TVSP) 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.

The TVSP scheme is planned to be available until 2013-14. It is also structured to encourage acceptance of an offer within six months of it being made but offers may be accepted beyond that time frame for a lesser amount. Given this timeframe and structure, it may be some time before it is clear what impact the scheme has had in providing incentive for reducing FTE numbers and meeting targeted savings. The Government indicated an initial target of 1011 FTE reductions for 2010-11.

The 2011-12 Budget states that FTE reductions can also be achieved in other ways (for example, natural attrition) and that the Government will honour its pledge of a ‘no forced redundancy’ policy for the remainder of this electoral term. Commencing in 2014, a process will be introduced whereby a public sector employee who has been a long-term redeployee would be able to be separated with appropriate financial severance and in accordance with the *Public Sector Act 2009*.

DTF have advised Audit that between 1 November 2010 and 30 June 2011 381.1 FTE reductions were achieved through TVSP payments (excluding executive reductions) as reported to DTF. Table 8.8 and related commentary in this Report provides further details. The 2011-12 Budget also states that an additional provision for TVSP payments of $29.9 million over the period 2011-12 to 2013-14 was established to support the extension of the public sector workforce reduction strategy.

For 2010-11 Audit sought an update of FTE monitoring arrangements and data as at 30 June 2011. DTF's response, based on data received from major agencies, showed total FTEs of 77 808 which is within the total cap of 78 596 as at 30 June 2011. The overall position comprised various agencies being over and under their cap. For example Health has reported that actual FTEs were 118 FTEs above its cap, largely attributed by Health to activity growth while Families and Communities was 157 FTEs below its cap, primarily due to vacancies held to achieve overall budget management strategies. Table 8.7 and related commentary in this Report provides further details.

2.6.7 Capital payments

For 2009-10 and 2010-11 the State has achieved budgeted capital expenditure exceeding $2 billion annually. Even so, as in past years, carryover adjustments were made for delays where expenditure will now be incurred in later years. Investing carryovers from 2010-11 to 2011-12 and future years are $205 million.

I have previously reported that the significant increase in capital outlays and activity may introduce a heightened risk to the proper management and control of capital project management. This situation remains, with purchases of non-financial assets estimated to be $2.1 billion in 2011-12. The budget includes a slippage allowance of $300 million, the same as the previous year. The capital program also comprises large projects with inherent complexities and risks. Over the four years to 2014-15 capital spending includes $1.2 billion on major rail projects, $1.1 billion on road projects and $669 million on the redevelopment of major metropolitan and regional hospitals.

2.6.7.1 Public private partnership projects

Public private partnership (PPP) projects form a part of the annual capital program. Two major PPPs in progress in 2010-11 are the Education Works New Schools PPP project and the new Royal Adelaide Hospital project, the largest PPP to date.

Total estimated investing expenditure on the Education Works - Stage 1 up to 2010-11 is $200 million including capitalisation of leased assets and equipment. For the 2011-12 Budget, operating costs are estimated at $33.8 million in 2011-12 and $26.6 million annually through to 2014-15

In June 2011 the Government announced financial close on a contract with SA Health Partnership (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 current forward estimates to 2014-15 do not recognise the completion of the new RAH and the commencement of annual service payments as they are scheduled to occur in 2015-16. The Government has indicated it will then pay an average $397 million a year for 30 years to SAHP who will be responsible for the non-clinical costs of running and maintaining the hospital. DTF has advised that this payment will need to be recognised when the new hospital begins operating noting that only part of this amount will be expensed as it includes cash payments associated with the lease liability. The details of the Budget impacts for 2015-16 are still being finalised.

DTF has advised Audit that the PPP contract will be recorded as a finance lease liability in 2015-16 when the RAH becomes available for use by the State. DTF currently estimates the value of the lease liability is $2.8 billion. This will add substantially to net debt from 2015-16.

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. Asset sales for the general government sector are projected to increase in 2011-12 and peak at $418 million in 2012-13. Total asset sales over the four years to 2014-15 are estimated to be $966 million.

When combined with the public non-financial corporations, total budgeted asset sales for non-financial public sector are $1319 million in 2011-12, well in excess of total asset sales in recent years. Further asset sales of $871 million are estimated for 2012-13 making asset sales a significant element to the estimated net debt projections for the four years of the 2011-12 Budget.

The estimated sales in the forward estimates include proceeds from the forward sale of up to three harvest rotations for ForestrySA plantations (announced in the 2008-09 MYBR) and a recently proposed sub-licence giving the right to operate the SA Lotteries' brands and business for a defined period of time. Proceeds from these initiatives and other asset sales have not been separately disclosed in the Budget so as to avoid prejudicing processes, but they are substantial to the estimated net lending results within the four years of the 2011-12 Budget. The budget notes that reductions in interest costs in the Budget arising from debt retirement may be at risk if the Government is unable to achieve the value estimated for divestment of ForestrySA harvest rotations, the new SA Lotteries sub-licence and selected government owned properties.

The Government announced it would proceed with the forward sale of three forest rotations in May 2011. In July 2011 the Government advised on progress with the South East Forestry Industry Roundtable. The members of the Roundtable are to advise the Government on what conditions should be attached to the forward sale.

In response to Audit inquiries about the process that will be used to issue the lotteries licence, DTF advised that appropriate project governance will be established in consultation with relevant parts of Government in order to implement the proposal. A Steering Committee for the project has also been established that reports to the Treasurer through the Deputy Under Treasurer.

2.6.8 Budget monitoring

Past Audit Reports have consistently emphasised the need for strong monitoring of budget progress. In response to Audit inquiries of specific monitoring measures for the 2011-12

Budget, DTF advised there was a regular monitoring regime, coordinated by DTF, including monthly monitoring of financial performance against approved budget, and monitoring of capital projects, budget initiatives and FTEs on a quarterly basis. Each aspect of the monitoring regime, based on information supplied by agencies and an analysis prepared by DTF was provided to the Sustainable Budget Cabinet Committee (SBCC).

DTF also advised that given the magnitude of the Budget improvement measures and the importance to the fiscal outlook of the achievement of these measures, an enhanced monitoring process was also introduced in 2010-11 to monitor the progress of agencies in achieving their budget improvement measures and FTE reductions. Both regular and enhanced monitoring processes will continue in 2011-12.

Monitoring in July/August 2011 was to focus on those savings measures commencing or significantly increasing in 2011-12 to ensure agencies are on track to deliver the required savings during 2011-12 and ensuring that plans are in place to deliver those measures that commence in 2012-13 and beyond. The Treasurer met with Chief Executives in August 2011 for an overview of their progress in achieving the savings task and to work through their implementation plans. The Treasurer will report to SBCC on the outcomes of the process, with individual Chief Executives required to meet with the full SBCC if significant issues impacting the achievement of savings or revenue measures are identified. FTE reduction monitoring (originally a component of the enhanced monitoring process) will now be incorporated into the quarterly monitoring process.

For 2010-11, DTF advised that at the time of the 2011-12 Budget, Health was projected to overspend its budget by $66.7 million. A provision was made and held centrally (ie contingencies in DTF administered items) for this projected overspend. The components of the overspend included an increase in the cost of service delivery, a reduction in revenue associated with the Pharmaceutical Benefits Scheme and other revenue sources, timing of implementing hospital savings strategies and fee for service additional costs in Country Health SA.

Audit intends to review the outcomes of the monitoring process reported to the SBCC in early 2011-12.

2.7 Concluding observations

The fiscal strategy of the 2011-12 Budget is to re-establish and maintain sustainable operating surpluses. An operating deficit of $263 million is now budgeted for 2011-12 compared to a surplus of $55 million expected at the time of the 2010-11 Budget. Operating surpluses are projected from 2012-13 although at lower levels than in the previous budget. The budget also is not projected to return to net lending until 2014-15, a year later than previously forecast. Revisions in the 2011-12 Budget highlight the ongoing uncertainty of economic events. Notably, in successive budgets since 2008-09, projected net operating results for the years 2010-11 to 2014-15 have lowered from the previous budget with 2010-11 and 2011-12 becoming estimated deficits.

The general government sector net debt is estimated to increase to $3.2 billion at 30 June 2011, lower than previously budgeted but rising to $4.2 billion in 2013-14 and then decrease to $3.6 billion by 2014-15. Notably, the increase in net debt to 2010-11 primarily reflects capital spending. In the three years since 2007-08, at which time the State had net financial assets rather than debt, operating results cumulatively total a deficit of $473 million while net asset acquisitions are $3.3 billion.

The essential elements of the Budget are estimated real growth in major revenue items, realise expenditure restraint from previously announced budget measures, manage the continuing large capital program and achieve the estimated value of proposed asset sales.

Comparison with past experience shows that the 2011-12 Budget estimates for key revenue lines are consistent with past average experience but revenue performance is sensitive to economic activity. I note the statement by the Governor of the Reserve Bank of Australia in September 2011. He noted that domestically, near-term growth outlook continues to look somewhat weaker than was expected a few months ago. Beyond the near term, growth is still likely to be at trend or higher, unless the world economic outlook continues to deteriorate. Further, the IMF revised down its forecast for world growth in late September 2011.

Comparing the trend of key estimated expenses for the 2011-12 Budget with past average experience shows a diverging difference. This difference highlights the significance of the expenditure restraint required in the 2011-12 Budget.

There remains in excess of $1.3 billion of new savings to be achieved for the three years to 2013-14 in addition to other remaining savings. Agencies now have some experience with implementing savings programs but the savings targets are not always achievable by all agencies. For 2010-11, agencies were collectively within the established FTE cap as at 30 June 2011. I note that some achieved this by managing staff vacancies. Agencies have also availed themselves of the TVSP scheme set up to support FTE reduction. DTF report that generally, savings for 2010-11 were achieved. The largest exception was in Health which had a $10.9 million shortfall relating to an unachieved outpatient services reforms measure. The Department of Health's savings target for the next three years is $298 million. The Health portfolio has experienced difficulty in meeting savings targets in the past and is continually under service demand pressure.

Implementing savings tends to be directed at administrative and support areas for services. Care needs to be taken that where this occurs, relevant changes to systems and procedures within a risk management context is addressed, to ensure the public interest is continually served by efficient and effective administrative performance and failures avoided.

The 2011-12 Budget continues a large capital spending program with purchases of non-financial assets estimated to be $2.1 billion in 2011-12. This presents a continuing heightened risk to the proper management and control of capital projects. In addition to this program, the Government has also committed grant expenditure of $535 million to redevelop the Adelaide Oval.

Total budgeted asset sales for the non-financial public sector are $1319 million in 2011-12, well in excess of total asset sales in recent years. Further asset sales of $871 million are estimated for 2012-13. The budget now incorporates two significant asset realisation processes for the forward sale of up to three harvest rotations for ForestrySA plantations and a proposed sub-licence giving the right to operate the SA Lotteries' brands and business for a defined period of time. Appropriate competitive sales process incorporating relevant expertise will be vital to maximising the realisable value of these public assets.

If the aims of this budget are achieved the estimated result for 2014-15 is an operating surplus of $655 million, the highest result reported since the GFS budget methodology was adopted in 2002-03. The budget records that the significant operating surplus forecast for 2014-15 provides an essential buffer for the impact of 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.

Given the context of this Budget, Audit considered both its method of preparation and the monitoring processes. Importantly, any budget process is by its nature, inherently a matter of estimations and assumptions. Noting that qualification, the Budget preparation process incorporates a range of quality assurance techniques. For monitoring, DTF advised that given the magnitude of the Budget improvement measures and the importance to the fiscal outlook of the achievement of these measures, it introduced an enhanced monitoring process in 2010-11. Monitoring processes cover agencies' progress in achieving their budget improvement measures and FTE reductions.

The prevailing climate of economic uncertainty emphasises the importance of a high degree of government management discipline facilitated by effective reporting and monitoring. Audit will review aspects of the Budget monitoring process in 2011-12.

3 Reporting framework

3.1 Introduction

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

- Uniform Presentation Framework (UPF)
- Australian Accounting Standards (AASB)
- Treasurer's Statements pursuant to the *Public Finance and Audit Act 1987*.

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

3.2 Uniform Presentation Framework

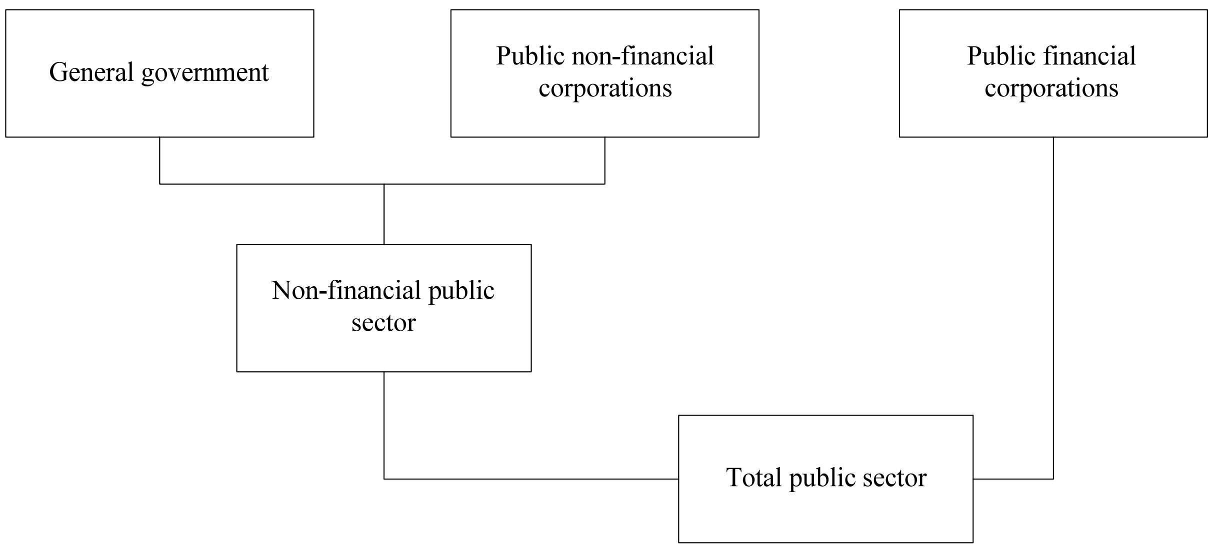
3.2.1 Background

By agreement between the Commonwealth, states and territories, each jurisdiction presents their budget papers, mid-year budget update outcome reporting on a UPF basis.

The UPF is a reporting standard based on the Australian Bureau of Statistics' accrual based Government Financial Statistics (GFS) framework. The primary objective of the UPF 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 make up 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.

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

Public financial corporations – bodies primarily engaged in the provision of financial services. This includes financial institutions such as the South Australian Government Financing Authority (SAFA), South Australian Asset Management Corporation (SAAMC), HomeStart Finance and Funds SA.

The Budget Papers include the following GFS financial statements:

- general government sector Operating Statement and Balance Sheet
- public non-financial corporation sector Operating Statement and Balance Sheet
- non-financial public sector Operating Statement and Balance Sheet
- cash flow statements for these sectors.

The public financial corporations sector data is not published in the Budget Papers.

3.2.1.1 Key government financial statistics headline amounts

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

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

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

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

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

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

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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 2011-12 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.

No opinion is, therefore, provided on the accuracy of both historic and prospective figures presented.

3.3 Australian Accounting Standards

The Australian Accounting Standards 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 Australian Accounting Standards (AASB).

3.3.2 AASB whole-of-government/general government consolidated financial report

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

Whole-of-government financial reports for South Australia up to 2007-08 were prepared by DTF pursuant to accounting standard AAS 31 'Financial Reporting by Governments'.

Since 2008-09, the whole-of-government/general government consolidated financial report (CFR) has been prepared pursuant to accounting standard AASB 1049 'Whole of Government and General Government Sector Financial Reporting'. 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 AASBs except as specified in the standard and disclosure of additional information such as reconciliations to key fiscal aggregates determined in accordance with the ABS GFS Manual.

3.3.3 Convergence of Government Financial Statistics and Australian Accounting Standards

The objective of harmonising generally accepted accounting principles and the GFS is to achieve a single standard to produce comparable government budgets and financial statements that are auditable and comparable.

The Australian Accounting Standards Board (the Board) issued ED 174 'Amendments to Australian Accounting Standards to facilitate GAAP/GFS Harmonisation for Entities within the general government sector [AASB 101, 107 and 1052]' in January 2009. ED 174 was issued as part of the second, and final, phase of the Board's implementation of the Financial Reporting Council's GAAP/GFS harmonisation broad strategic direction.

At its June 2009 meeting, the Board discussed the responses to ED 174. As a result, the Board expressed a preference not to proceed with Phase 2 of the project on the grounds that imposing GAAP/GFS harmonisation requirements in the manner proposed in ED 174 would not meet the needs of a broad range of users.

At its February 2010 meeting the Board considered alternative approaches that might overcome its reservations about issuing a Standard based on the proposals in ED 174. The Board decided to issue proposals for a mandatory Standard that takes a different approach to that proposed in ED 174. This revised approach provides that the Board's focus should be improved financial reporting for entities within the general government sector, rather than exclusively GAAP/GFS harmonisation. This approach would have regard to improvements that might arise from adopting aspects of harmonisation.

In June 2011 the Board issued ED 212 'Not-for-Profit Entities within the General Government Sector'. Comments in response to this ED are due by 31 October 2011. In particular, the Board is interested in assessing whether the benefits of a new Standard would outweigh the cost of implementing it.

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

The Treasurer's Statements are prepared pursuant to the requirements of the *Public Finance and Audit Act 1987* and reported as an Appendix in Part B of the Auditor-General's Annual Report to Parliament.

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

4 Summary of key fiscal measures and targets

4.1 South Australian fiscal targets

The 2011-12 Budget Papers[4] indicate that the Government is committed to the following fiscal targets:

Net operating balance	*To achieve at least a net operating balance in the general government sector in every year.*
Net lending	*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.*
Taxes	*To ensure the State has an effective tax regime having regard to the Government's social and economic objectives.*
Services	*To provide value for money community services and economic infrastructure within available means.*
Superannuation	*To fully fund accruing superannuation liabilities and progressively fund past service superannuation liabilities.*
Risk	*To ensure that risks to State finances are managed prudently to maintain a triple-A rating.*
PNFCs borrowing	*To ensure public non-financial corporations (PNFCs) will only be able to borrow where they can demonstrate that investment programs are consistent with commercial returns (including budget funding).*

4.1.1 General government net operating balance

One of the Government's fiscal targets is to achieve net operating balances every year. This means that revenues are covering expenses, including interest and depreciation.

The Government states in the 2011-12 Budget Papers that a key fiscal target is to achieve net operating balances every year. This means that revenues are covering expenses, including interest and depreciation. South Australia is forecasting a net operating deficit in 2011-12 before returning to a surplus in 2012-13.

4.1.2 General government ratio of net financial liabilities to revenue

Another of the Government's fiscal targets is 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. Net financial liabilities is a broader measure than net debt as it includes significant liabilities other than borrowings, such as unfunded superannuation and long service leave entitlements.

4 Budget Statement 2011-12, Budget Paper 3, Table 1.3.

The ratio is forecast to peak in 2013-14 and decline to below current levels by 30 June 2015. This reflects both an improvement in the net operating balance and an easing of the level of infrastructure investment across the period.

It is evident that a similar situation exists for New South Wales and Victoria whilst Tasmania, Queensland and Western Australia show a steady ratio incline.

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 in the following table.

Jurisdiction	Budget fiscal objective/strategy [(a) (b)]
Commonwealth	Achieving a budget surplus, on average, over the medium term. Keeping taxation as a share of GDP below the level for 2007-08 (23.5 percent of GDP) on average. Improving the Government's net financial worth over the medium term.
NSW	General government sector net financial liabilities at or below 6 percent of GSP by June 2015. Total state sector unfunded superannuation liabilities eliminated by June 30 2030.
Vic	Target operating surplus of at least $100 million in each year, with surpluses averaging $164 million over the forward estimates. Constraint in expenditure growth, including the delivery of a $2.2 billion five year package of efficiency savings. Emphasising the importance of the Government's policy of having no wage policy outcomes greater than 2.5 percent, unless they are funded from productivity gains.
Qld	In the general government sector, meet all operating expenses from operating revenue (where operating revenue is defined as total revenue from transactions and operating expenses are defined as total expenses from transactions less depreciation). Achieve a general government net operating surplus as soon as possible, but not later than 2015-16.
WA	Achieve operating surpluses for the general government sector. Ensure that real per capita own-purpose general government expenses do not increase.
Tas	By 2014-15 achieve a net operating surplus greater than $50 million.
ACT	Achieve a general government sector net operating surplus. Maintain the territory's AAA credit rating. Maintain operating cash surpluses.
NT	Expenditure growth not to exceed revenue growth, excluding tied Commonwealth funding.

(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

The most prevalent position is to target net operating surpluses in the general government sector, based on the GFS accrual method as is the position in this State. New South Wales is the only other state to give specific focus to net financial liabilities.

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

5 Estimated results for 2010-11

5.1 Overview

The following section summarises the estimated operating results for 2010-11.

5.2 2010-11 estimated results

5.2.1 General government sector

The estimated result for the year was a net operating deficit of $427 million (budget $389 million deficit) and net lending deficit (borrowing) of $1821 million (budget $1791 million). The following table shows 2009-10 financial year data and differences between the estimated result and budget for 2010-11.

Table 5.1 – General government budget comparisons 2009-10 to 2010-11

Revenue:	2009-10 Actual $'million	2010-11 Budget $'million	2010-11 Estimated Result $'million	Difference to budget $'million	Difference to budget Percent
Taxation revenue	3 649	3 858	3 845	(13)	-
Grants:					
Current	7 039	7 257	7 176	(81)	(1)
Capital	1 841	1 063	1 072	9	1
Sale of goods and services	1 936	1 877	1 885	8	-
Interest income	138	143	184	41	29
Dividend and income tax equivalent income	433	353	408	55	16
Other	497	536	518	(18)	(3)
Total revenue	15 534	15 086	15 087	1	-
Less: **Expenses:**					
Employee expenses	6 221	6 379	6 417	38	1
Superannuation expenses					
Superannuation interest cost	455	427	427	-	-
Other superannuation expenses	600	676	684	8	1
Depreciation and amortisation	633	681	693	12	2
Interest expenses	204	255	307	52	20
Other operating expenses	3 695	3 983	4 026	43	1
Grants	3 540	3 073	2 960	(113)	(4)
Total expenses	15 347	15 475	15 514	39	-
Net operating balance	187	(389)	(427)	(38)	10
Less: **Net acquisition of non-financial assets**					
Purchases of non-financial assets	2 144	2 283	2 189	(94)	(4)
Less: Sales of non-financial assets	29	201	102	(99)	(49)
Less: Depreciation	633	681	693	12	2
Plus: Change in Inventory	3	-	-	-	-
Plus: Other movements in non- financial assets	(206)	-	-	-	-
Total net acquisition of non-financial assets	1 279	1 402	1 394	5	-
Net lending (borrowing)	(1 092)	(1 791)	(1 821)	(30)	2

Note: Totals may not add due to rounding.

As shown in the table, when compared to the net operating surplus of $187 million in 2009-10, the 2010-11 Budget anticipated a net operating deficit of $389 million. This movement of $576 million was due mainly from a reduction in capital grants from the Commonwealth partially offset by decreased grant expenditure. The reduction in grant activity reflects the anticipated wind down of the Commonwealth government’s economic stimulus plan.

The estimated result for 2010-11 shows a $38 million deterioration from budget, leading to a net operating deficit of $427 million. This increase in the estimated net operating deficit principally results from decreased Commonwealth grants partially offset by increased distributions from PNFCs and marginal increases in employee expenses and operating expenses offset by decrease in grant expenses.

5.2.1.1 Net acquisition of non-financial assets

The 2010-11 estimated result for purchases of non-financial assets is down $94 million from budget. The majority of under expenditure qualifies for carryover into future budgets. Investing carryovers from 2010-11 to 2011-12 and future years are $205 million.[5] The largest of these carryovers are associated with the revitalisation of the State’s rail network.

The 2010-11 budget of $2283 million for purchases of non-financial assets, included a slippage allowance of $300 million to allow for likely project delays. Table 5.2 shows that consistent with the high value of capital spending, some large adjustments were made in the course of 2010-11. The original budget was increased by policy decisions and carryovers from 2009-10. The estimated result for 2010-11 allows for mid-year budget adjustments and carryovers beyond the year. Finally, the estimated result is influenced by the removal of the slippage allowance reflecting the reduced uncertainty of projections.

Table 5.2 – Purchases of non-financial assets budget to estimated result comparison 2010-11

		$’million	$’million
2010-11 Budget			2 283
Add:	Policy decisions	4	
	Carryover from 2009-10	36	
			40
Less:	MYBR adjustments	(78)	
	Approved budget time carryovers	(205)	
	Cabinet approved re-profiles	(62)	
	Other	10	(335)
Add back:	Capital slippage reversal		200
2010-11 Estimated result			2 189

Note: Totals may not add due to rounding.

5.2.2 Non-financial public sector

The non-financial public sector (consolidating the general government and public non-financial corporations sectors) estimated result for the year was a net lending deficit (borrowing) of $2402 million, which is $101 million more than budget for the year.

[5] Budget Statement 2011-12, Budget Paper 3, Table 1.8.

The following table summarises the position.

Table 5.3 – NFPS Budget comparisons 2009-10 to 2010-11

	2009-10 Actual $'million	**2010-11 Budget $'million**	**2010-11 Estimated result $'million**	Difference to budget $'million	Difference to budget Percent
Revenue	16 315	16 101	15 949	(152)	(1)
Less: **Expenses**	15 679	16 515	16 375	(140)	(1)
Net operating balance	636	(414)	(426)	(12)	3
Less: **Net acquisition of non-financial assets**	2 361	1 887	1 976	89	5
Net lending (borrowing)	(1 725)	(2 301)	(2 402)	(101)	4

Note: Totals may not add due to rounding.

The increase in the net lending deficit (borrowing) by $101 million comprises the deterioration in the general government result by $30 million and the public non-financial corporations sector's result by $71 million.

The public non-financial corporations sector's[6] net operating balance is estimated to improve $26 million from budget to a surplus of $1 million. Total net acquisition of non-financial assets increases by $97 million compared to budget due to a $253 million decrease in the estimated sales of non-financial assets compared to budget, primarily from deferred asset sales, partially offset by a $196 million decrease in the purchase of non-financial assets compared to budget. The combination of these results causes an increase of $71 million in the net lending deficit (borrowing) to $582 million.

[6] Budget Statement 2011-12, Budget Paper 3, Table A.2.

6 Budget 2011-12 overview

6.1 Overview

The following commentary focuses on the trends arising from the 2011-12 Budget tabled in Parliament in June 2011. It provides an overview of:

- the Budget for 2011-12 having regard to the estimated result for 2010-11
- a longer term view of the forecast results going forward to 2014-15.

The analysis deals only with the accrual based GFS framework.

6.1.1 Matters of significance to the 2011-12 Budget

The 2011-12 Budget was prepared in an environment of deteriorating taxation and GST revenues, which highlights the need for continued expenditure restraint. The Budget states that expenditure on new expenditure initiatives across the forward estimates is the lowest budgeted net spending on new initiatives since 2003-04.

Despite this focus on expenditure restraint, the 2011-12 Budget does not anticipate a net operating surplus until 2012-13. To support the net operating deficits for 2010-11 and 2011-12, and to fund the Government's capital investment program across the forward estimates, net debt (mainly borrowings less cash and deposits) is budgeted to climb to $4213 million by 2013-14, before reducing in 2014-15.

Some specific items to note in the 2011-12 Budget estimates years are:

- new operating and investing initiatives totalling $516 million over the next four years[7]
- targeted savings and revenue offsets totalling $150 million over four years[8]
- expenditure restraint compared to revenue growth is projected to lift the net operating balance to $655 million by 2014-15
- higher capital investment leads to general government sector net debt increasing by $398 million to $3615 million by June 2015.

Budgeted total revenues and expenses for 2011-12 are higher than was previously estimated in the 2010-11 Budget.

Total revenue for 2011-12 is now budgeted at $15.7 billion, $200 million or 1.3 percent more than was estimated for 2011-12 in the previous, 2010-11 Budget. Expenses for 2011-12 are now budgeted at $16.0 billion, $518 million or 3.3 percent higher than was estimated at the time of the 2010-11 Budget.

As a consequence of these changes, a net operating balance deficit of $263 million is now budgeted, down from the estimated $55 million 2011-12 surplus result projected in the 2010-11 Budget and not achieving the fiscal objective of at least a net operating balance for the general government sector.

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[7] Budget Statement 2011-12, Budget Paper 3, Table 1.1.
[8] Budget Statement 2011-12, Budget Paper 3, Table 2.1.

6.2 General government sector – Operating Statement

Table 6.1 sets out the differences between the 2011-12 Budget and the estimated results for 2010-11.

Table 6.1 – GFS - General government sector budget comparison of 2010-11 estimate results and 2011-12 Budget

Revenue:	**2010-11 Estimated result $'million**	**2011-12 Budget $'million**	Difference $'million	Difference Percent
Taxation revenue	3 845	4 129	284	7
Grants:				
Current grants	7 176	7 666	490	7
Capital grants	1 072	730	(342)	(32)
Sale of goods and services	1 885	2 054	169	9
Interest income	184	172	(12)	(7)
Dividend and income tax equivalent income	408	371	(37)	(9)
Other	518	605	87	17
Total revenue	15 087	15 727	640	4
Less: **Expenses:**				
Employee expenses	6 417	6 606	189	3
Superannuation expenses				
Superannuation interest cost	427	412	(15)	(4)
Other superannuation expenses	684	701	17	2
Depreciation and amortisation	693	768	75	11
Interest expenses	307	366	59	19
Other operating expenses	4 026	4 105	79	2
Grants	2 960	3 034	74	3
Total expenses	15 514	15 990	476	3
Net operating balance	(427)	(263)	164	(38)
Less: **Net acquisition of non-financial assets**				
Purchase of non-financial assets	2 189	2 125	(64)	(3)
Less: Sales of non-financial assets	102	369	267	262
Less: Depreciation	693	768	75	11
Total net acquisition of non-financial assets	1 394	988	(406)	(29)
Net lending (borrowing)	(1 821)	(1 252)	569	(31)

Note: Totals may not add due to rounding.

As shown, the differences for the 2011-12 year are due mainly to:

- increased taxation revenue arising from projected increases in property taxes (especially conveyance duty and guarantee fees) and payroll tax
- increased current grants income due mainly to a $197 million estimated increase in GST revenue grants from the Commonwealth and a $221 million increase in Commonwealth National Partnership grants
- a $342 million decrease in capital grants income, principally Commonwealth National Partnership grants. This large decrease reflects the continued winding back of payments under the Commonwealth's Nation Building - Economic Stimulus Plan
- increased revenue from the sales of goods and services due mainly to increased revenue from regulatory fees ($75 million), drivers' licence fees ($30 million) and other user charges ($39 million)

- increased employee expenses (including targeted separation costs).

More detail of the factors influencing the 2011-12 Budget is considered in the context of the longer-term trends discussed later in this Report.

6.2.1 Reconciliation of variations since 2010-11 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 categorise 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 2010-11 Budget that affect the net operating balance and provisions used to offset some of those changes.[9]

Table 6.2 – Reconciliation of general government sector net operating balance

	2010-11 Estimated result $'million	2011-12 Budget $'million	2012-13 Estimate $'million	2013-14 Estimate $'million
2010-11 Budget	(389)	55	216	370
Parameter and other variations:				
Revenue - taxation	(13)	(61)	(12)	(8)
Revenue - other	24	228	122	58
Operating expenses	50	(391)	(181)	(375)
Net effect of parameter and other variations	61	(224)	(71)	(325)
Policy measures:				
Revenue - taxation	-	2	2	2
Revenue - other	(9)	31	63	47
Operating expenses	(125)	(162)	(127)	(47)
Net effect of policy measures	(134)	(129)	(62)	2
Use of provisions set aside in the 2010-11 Budget and the 2010-11 MYBR:				
Operating expenses	34	35	34	34
2011-12 Budget	(427)	(263)	114	80

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

6.2.1.1 Revenue variations

The table highlights the expected downward revision of taxation revenue across the forward estimates and increases in other revenues primarily from Commonwealth funding changes since the 2010-11 Budget.

[9] Budget Statement 2011-12, Budget Paper 3, Table 1.6.

The following table shows the components of revenue parameter changes.[10]

Table 6.3 – Revenue parameter changes

	2010-11 Estimated result $'million	2011-12 Budget $'million	2012-13 Estimate $'million	2013-14 Estimate $'million
Commonwealth Specific Purpose and National Partnership grants:				
Capital	8	90	(34)	(1)
Current	30	155	94	151
Commonwealth contributions	9	14	-	-
GST revenue grants and transitional assistance	(163)	(89)	(3)	5
Property related taxes	(48)	(82)	(64)	(20)
Dividends and income tax equivalents	55	(17)	(14)	(141)
Interest income	41	45	44	19
Other	77	50	89	37
Total	9	166	112	50

Table 6.3 shows the downward revisions, since the 2010-11 Budget, in GST distributions from the Commonwealth for 2010-11 and 2011-12, and downward revisions to property related taxes (particularly conveyance duty) over the period to 2013-14.

Current grants have been revised up due to revisions to specific purpose grants from the Commonwealth for non-government schools and National Partnership payments for aged care and education.

6.2.1.2 Operating expense variations

Table 6.2 shows that parameter effects are estimated to add $897 million to operating expenses over the four years to 2013-14.

Policy spending decisions add a further $461 million to operating expenses over the four year period of which $125 million is for 2010-11.[11] 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

	2006-07 $'million	2007-08 $'million	2008-09 $'million	2009-10 $'million	2010-11 $'million
Policy measure operating expenses	163	274	296	344	125

Table 6.4 shows that $1202 million was added to spending for the past five years. In past years, increases reflected an established practice of discretionary expenditure decisions being taken after Budgets were announced. This was generally enabled by favourable revenue outcomes. By comparison to past years, policy expense adjustments since the 2010-11 budget, as shown in table 6.2, are only partially offset by revenue variations, contributing to a deterioration in the estimated net operating deficit to $427 million.

[10] Budget Statement 2011-12, Budget Paper 3, Table 1.8 and 2010-11 Mid-year budget review, Table 1.5.
[11] Budget Statement 2011-12, Budget Paper 3, Table 1.6.

6.3 Public non-financial corporation sector – Operating Statement

A net operating deficit of $13 million is budgeted in 2011-12. This minor deterioration from the estimated result for 2010-11 is due to an increase in the sales of goods and services offset by increases in other operating expenses, depreciation and amortisation and interest expenses. Net lending is budgeted to improve to $177 million in 2011-12 due to a $691 million increase in the budgeted sales of non-financial assets. The differences between the two years are set out in the following table.

Table 6.5 – GFS - PNFC budget comparison 2010-11 and 2011-12

Revenue:	**2010-11 Estimated result $'million**	**2011-12 Budget $'million**	Difference $'million	Difference Percent
Sale of goods and services	1 636	1 965	329	20
Other	982	977	(5)	(1)
Total revenue	2 619	2 942	323	12
Less: **Expenses:**				
Employee expenses	237	242	5	2
Depreciation and amortisation	332	386	54	16
Interest expenses	225	249	24	11
Other property expenses	322	327	5	2
Other operating expenses	1 376	1 638	262	19
Other expenses	126	114	(12)	(10)
Total expenses	2 618	2 955	337	13
Net operating balance	1	(13)	(14)	-
Less: **Net acquisition of non-financial assets**				
Purchase of non-financial assets	1 165	1 244	79	7
Less: Sales of non-financial assets	259	950	691	267
Depreciation	332	386	54	16
Add: Change in inventories	8	(98)	(106)	-
Total net acquisition of non-financial assets	582	(190)	(772)	(133)
Net lending (borrowing)	(582)	177	759	(130)

Note: Totals may not add due to rounding.

6.4 Non-financial public sector – Operating Statement

The 2011-12 budgeted result for the non-financial public sector is a net lending deficit (borrowing) of $1075 million, an improvement of $1327 million from the 2010-11 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

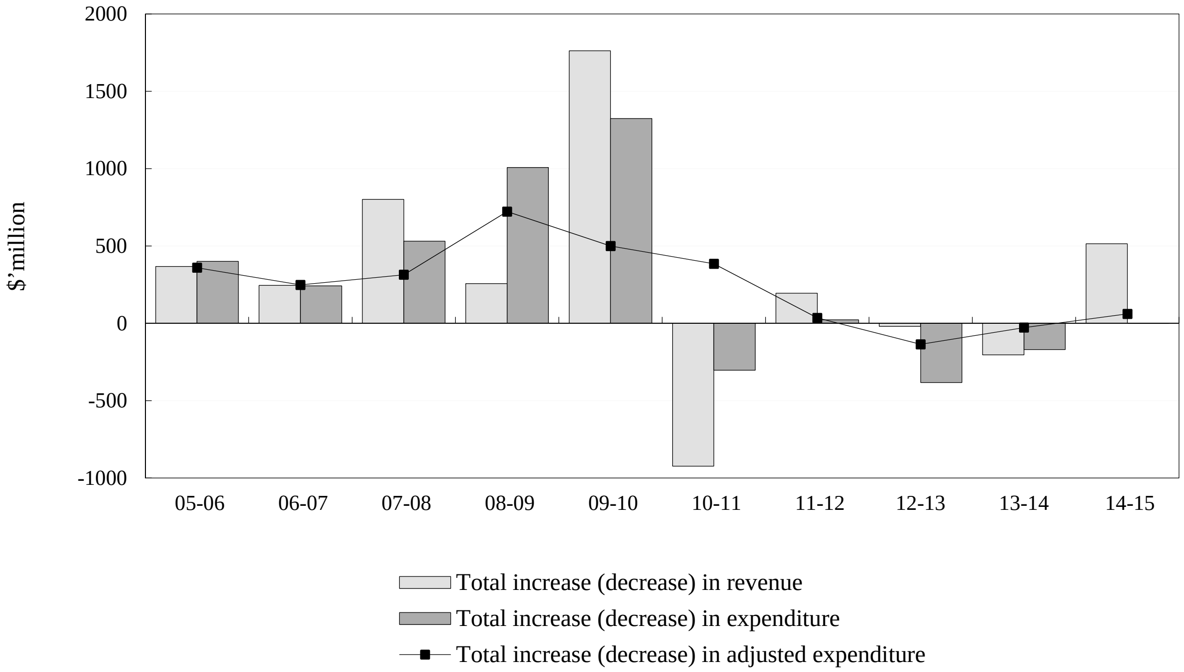
Revenue:	2005-06 Actual $'million	2006-07 Actual $'million	2007-08 Actual $'million	2008-09 Actual $'million	2009-10 Actual $'million	2010-11 Est. result $'million	2011-12 Budget $'million	2012-13 Estimate $'million	2013-14 Estimate $'million	2014-15 Estimate $'million
Taxation revenue	2 979	3 250	3 570	3 537	3 649	3 845	4 129	4 413	4 650	4 933
Grants:										
Current	5 556	5 715	6 294	6 651	7 039	7 176	7 666	7 905	8 080	8 515
Capital	210	254	322	598	1 841	1 072	730	500	248	383
Sales of goods and services	1 333	1 464	1 572	1 697	1 936	1 885	2 054	2 123	2 167	2 243
Interest income	147	167	203	150	138	184	172	196	192	199
Dividend and income tax equivalent income	575	450	429	382	433	408	371	406	408	410
Other	441	456	490	517	497	518	605	635	647	695
Total revenue	11 242	11 757	12 879	13 531	15 534	15 087	15 727	16 178	16 392	17 379
Less: **Expenses:**										
Employee expenses	4 644	4 933	5 268	5 749	6 221	6 417	6 606	6 699	6 829	7 041
Superannuation expenses:										
Superannuation interest cost	344	316	276	383	455	427	412	410	407	403
Other superannuation expenses	480	506	546	580	600	684	701	707	715	729
Depreciation and amortisation	454	498	525	566	633	693	768	835	881	961
Interest expenses	223	204	218	180	204	307	366	420	441	444
Other operating expenses	2 874	3 021	3 246	3 624	3 695	4 026	4 105	4 130	4 255	4 359
Grants	2 021	2 069	2 337	2 682	3 540	2 960	3 034	2 863	2 786	2 788
Total expenses	11 040	11 547	12 414	13 764	15 347	15 514	15 990	16 064	16 313	16 724
Net operating balance	202	209	464	(233)	187	(427)	(263)	114	80	655
Less: **Net acquisition of non-financial Assets**										
Purchases of non-financial assets	717	771	875	1 305	2 144	2 189	2 125	1 856	1 151	1 119
Less: Sales of non-financial assets	144	134	108	108	29	102	369	418	134	45
Less: Depreciation	454	498	525	566	633	693	768	835	881	961
Add: Change in inventories	0	0	0	7	3	0	0	0	0	0
Add: Other movements in non-financial assets	0	0	0	0	(206)	0	0	0	0	0
Total net acquisition of non-financial Assets	119	139	242	639	1 279	1 394	988	603	136	113
Net lending (borrowing)	83	71	222	(872)	(1 092)	(1 821)	(1 252)	(489)	(56)	542

Note: Totals may not add due to rounding.

6.5.2 Net operating balance influences

Achieving at least a net operating balance in every year is a fiscal target. 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 2014-15.

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



(a) Estimated June 2011 values.
(b) 2009-10 and 2010-11 are influenced by Commonwealth stimulus grants.

Chart 6.1 starkly demonstrates the short and medium term responses to the global financial crisis. 2009-10 shows the highest growth in revenues over the period due to additional Commonwealth stimulus money. On current projection, in 2010-11 revenues and expenses fall in real terms.

Revenue is affected by the very large Commonwealth stimulus grants wind down. Part of the decrease in expenses is the matching fall in related grant expenses in 2010-11 and 2011-12. The line adjusted to exclude grant expenses shows the significance of movements in grant expenses over the three years to 2010-11. For 2011-12 and across the forward estimates the impact of grant expenses is significantly reduced.

Expenses, excluding grants, also decrease or are constrained from proposed savings strategies and general expenditure control. It can be seen that expenditure projections from 2011-12, even after allowing for grant expenses, are lower than actual results over the period 2005-06 to 2009-10. Expenses budgeted for 2010-11 are lower than, in real terms, the lowest actual results experienced over the preceding six years. While the circumstances in the previous years differed, the task of decreasing spending remains a challenge.

7 Revenue

Trend data in charts in this section is in real terms at estimated June 2011 values unless otherwise stated.

7.1 Revenue overview

The global financial crisis combined with changes to Commonwealth and states' financial arrangements has caused a temporary change in the composition of total revenue over the period 2008-09 to 2011-12.

Total general government sector revenues are estimated to be $15.7 billion in 2011-12, an increase of $640 million (4.2 percent) over the previous year's estimated result, and a real increase of $194 million or 1.3 percent.

In real terms total revenue is expected to increase by 3.2 percent by 2014-15.

The makeup of total revenue and trends in real terms are illustrated in the following chart:

Chart 7.1 – General government sector total revenue (real)

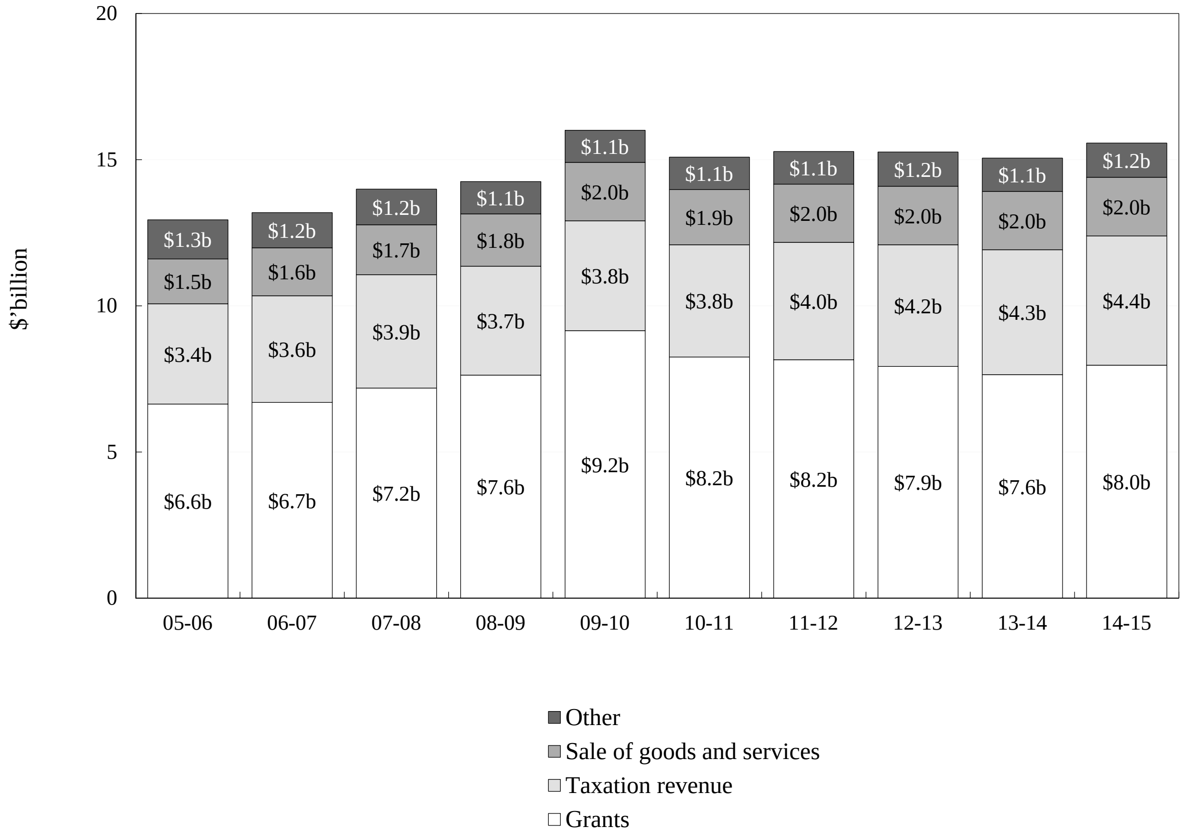


Chart 7.1 highlights the importance of Commonwealth grants to the State's revenues. Over most years Commonwealth grants represent about 50 percent of total revenue. During the period 2008-09 to 2011-12 Commonwealth revenue increased as a proportion of total State revenue, peaking at 55.9 percent (nominal)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

This percentage declines over the forward estimates to 50.2 percent (nominal) in 2014-15 which is in line with historical trends. While a relatively small change in percentage terms, this represents some hundreds of millions when total revenues are in the order of $15.7 billion (2010-11 nominal) and supports significant spending activity in targeted areas.

The following commentary provides some additional analysis of the main revenue areas. Detailed commentary is provided in Chapter 3 of the Budget Statement 2011-12.

7.2 Commonwealth grants

The 'Intergovernmental Agreement on Federal Financial Relations' (IGA) 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 2014-15 and demonstrates a 9 percent increase (nominal) over that period.

Table 7.1 – Commonwealth grants 2010-11 to 2014-15 (nominal)

	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million	2014-15 $'million
Current grant revenue	7 011.4	7 507.9	7 746.7	7 923.2	8 358.3
Capital grant revenue	1 029.5	711.6	484.00	232.0	366.8
Total grants	8 040.9	8 219.5	8 230.7	8 155.2	8 725.1

Table 7.1 highlights an anticipated decline in large Commonwealth capital grants over the forward estimates, more than offset by an increase in current grants to $8358 million in 2014-15.

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

7.2.1 GST revenue grants

GST revenue grants for 2010-11 are expected to be $162 million lower than the original budget estimate, reflecting a weaker recovery from the global financial crisis than originally estimated by the Commonwealth Treasury. The total GST pool is expected to grow by around 3.2 percent in 2010-11, compared to the Commonwealth's original budget estimate of growth of 7.5 percent.

GST revenue grants are distributed according to the principle of horizontal fiscal equalisation (HFE). The principle of HFE 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.

Over the forward estimates, South Australia's GST revenue grants are expected to grow by 7.2 percent in 2012-13, 4.9 percent in 2013-14 and 7.7 percent in 2014-15.

7.2.2 Specific purpose payments

Specific purpose current and capital payments (SPPs) are provided under section 96 of the *Constitution* for both recurrent and capital expenditure purposes. Reform of Federal financial relations in 2008-09 resulted in a significant rationalisation in the number of SPPs, effective from 1 January 2009. Previously, the allocation of Commonwealth payments for specific purposes among the states was based on many approaches including Commonwealth discretion, historical allocation and formula based allocation. Under the revised IGA arrangements, national SPPs will eventually be distributed between the states on a purely per capita basis based on Australian Bureau of Statistics' population estimates. This is being phased in over five years from 2009-10.

In August 2011 the Council of Australian Governments (COAG) agreed to a new National Health Reform Agreement to deliver reforms to the organisation, funding and delivery of health and aged care. From 1 July 2012 the National Health Care SPP will be replaced by National Health Reform funding which will comprise base funding equivalent to the National Healthcare SPP and, from 1 July 2014, efficient growth funding.

For more details on National Health Reform refer Chapter 3 of Budget Paper 3, Budget Statement 2011-12.

Over the forward estimates, SPPs are expected to increase from $2286 million (real) in 2011-12 to $2294 million in 2014-15, a real increase of $22 million from 2010-11. Over the forward estimates, growth in national SPPs reflects indexation arrangements specified in the IGA partially offset by the phasing-in of per capita distribution.

7.2.3 National Partnership Commonwealth grants

National Partnership current and capital payments (NPP) are a form of time limited payment under the new Federal-state funding arrangements to fund specific projects and to facilitate and/or reward states that deliver on nationally significant reforms.

In 2011-12, South Australia will receive an estimated $793 million of NPP funding for recurrent purposes. This is an increase of 38.7 percent compared to the $572 million estimated for 2010-11. This increase reflects increased funding for education programs, increased funding under the National Health Reform agenda and the aggregated impact of a range of other Commonwealth funded initiatives.

7.2.4 Monitoring of specific purpose funding

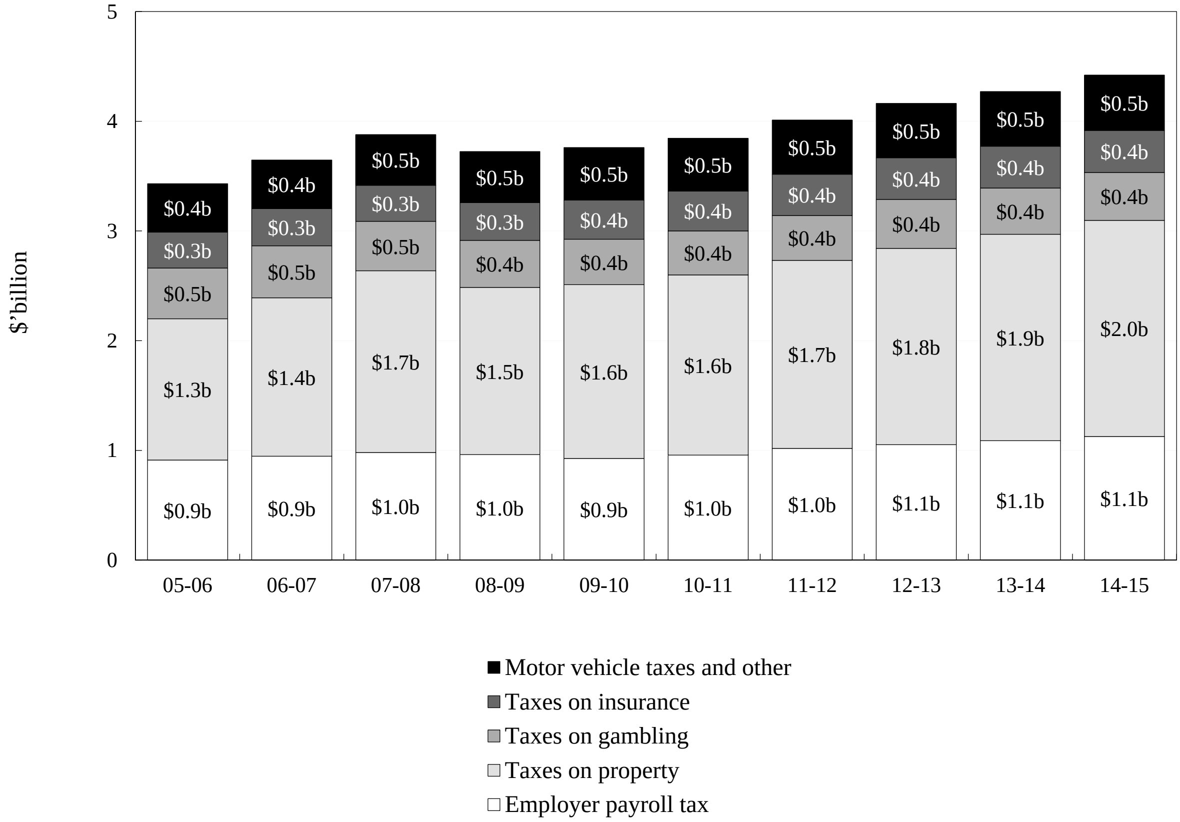
Under Commonwealth-State financial arrangements, SPPs and NPPs will be reviewed by Treasurers not less than every five years, to ensure that funding is adequate to meet expenditure demands. The reporting of outcomes will also be monitored to identify issues that might trigger earlier consideration of funding adequacy.

7.3 Taxation revenue

Taxation revenue is the second largest source of revenue to the State and represents about 25.5 percent of revenues in 2010-11. It comprises a diverse range of activities, including payroll, property, motor vehicles and gambling activities.

The Government has a fiscal strategy to ensure the State has an effective tax regime having regard to the Government's social and economic objectives. Considerations for the State's capacity to raise taxation revenue include the capacity of taxpayers to pay and the State's relative tax effort compared to other States and Territories.[12] The following chart examines the trend in the components of taxation receipts (in real terms) over the 10 year period to 2014-15.

Chart 7.2 – Taxation revenue (real)



Total taxes, in real terms, remain steady over 2009-10 before rising over the remaining forward estimate periods. Chart 7.2 demonstrates that throughout this time series, variations in taxation revenue are primarily attributable to property taxes.

Taxation revenue for 2011-12 is estimated to be $4129 million (nominal) an increase of $284 million over the estimated result for 2010-11. It is expected to be $4934 million (nominal) in 2014-15, a real increase of $575 million compared to 2010-11.

7.3.1 Property taxes

Property taxes include land tax, stamp duty on conveyances, mortgages, shares, rental, Emergency Services levy (ESL) on fixed property, the Save the River Murray Levy, regional natural resources management levies and guarantee fees.

Property taxes for 2011-12 are estimated to be $1763 million (nominal), a real increase of $72 million from the estimated result for 2010-11. They are expected to be $2198 million

[12] Budget Statement 2011-12, Budget Paper 3 pp 44 discusses South Australia's relative taxation effort.

(nominal) in 2014-15, a real increase of $328 million compared to 2010-11. Chart 7.3 shows the trend in property taxes (in real terms).

Chart 7.3 – Taxes on property (real)

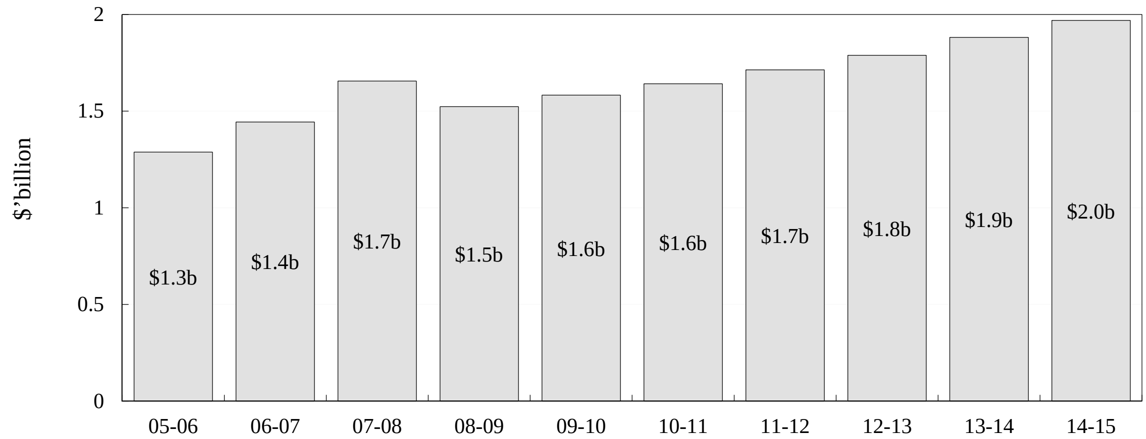


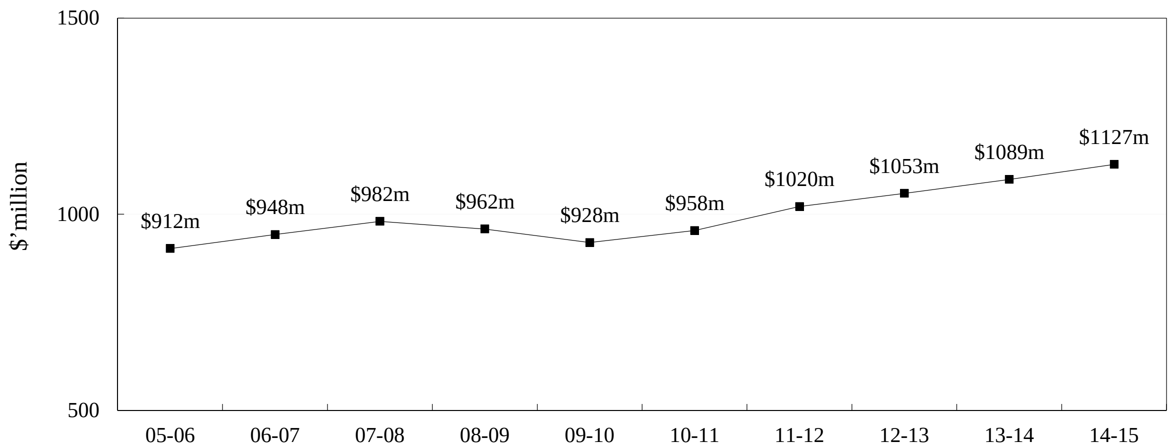
Chart 7.3 reflects the expected growth in property taxes over the forward estimates attributable to the adoption of strong medium-term property value assumptions.

The Budget Papers note that property tax revenues are affected by IGA tax policy reforms as well as revenue policy measures. The IGA reforms affect property tax growth in 2012-13 when stamp duty on non-quoted marketable securities and non-real property transfers is abolished. The introduction of a landholder model from 1 July 2011 and the introduction of land tax relief measures in 2010-11 also affect revenue levels.

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)



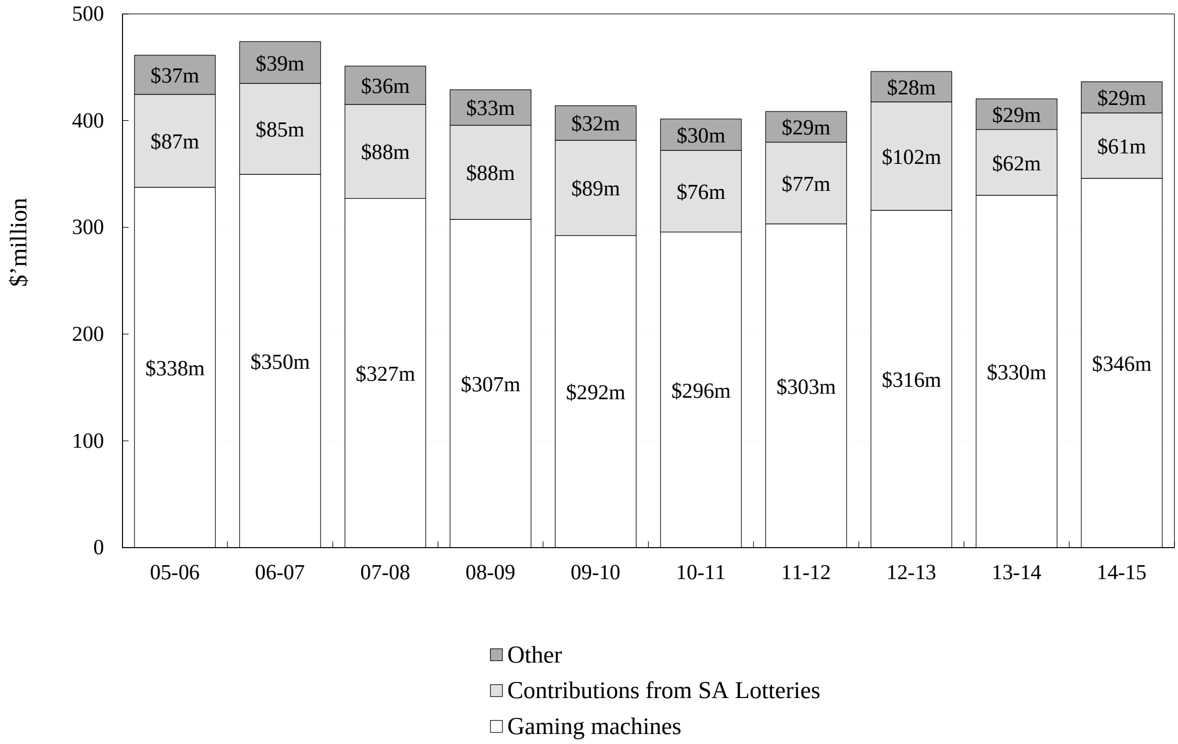
Payroll taxes for 2011-12 are estimated to be $1049 million (nominal), a real decrease of $61 million from the estimated result for 2010-11. The payroll tax threshold remained at $600 000 on 1 July 2010. In addition, the payroll tax rate also remained at 4.95 percent.

Payroll tax is expected to be $1258 million (nominal) in 2014-15, a real increase of $169 million compared to 2010-11.

7.3.3 Gambling taxes

Gambling taxes for 2011-12 are estimated to be $421 million (nominal), a real increase of $7 million from the estimated result for 2010-11. Gambling taxes are expected to be $487 million (nominal) in 2014-15, a real increase of $35 million compared to 2010-11. The following chart shows the trend in gambling taxes.

Chart 7.5 – Gambling Taxes (real)



The real decrease in gaming machine revenue for 2009-10 and 2010-11 is as a result of lower expenditure on gaming machines in hotels and clubs. For 2010-11 the decrease is also impacted by lower than expected tax revenue from the Casino. From 2011-12 net gaming revenue is expected to grow broadly in line with household consumption expenditure.

Contributions from SA Lotteries in 2012-13 are boosted by the expected return of reserves in line with the Government's planned creation of a new lotteries licence.

7.4 Sales of goods and services

Revenue from sales of goods and services represented 12.5 percent of estimated total revenues in 2010-11. Sales of goods and services by the general government sector include government fees and charges most of which will have increased by 2.9 percent from 1 July 2011 reflecting the annual indexation of fees.

Revenue from sales of goods and services are expected to be $2243 million (nominal) in 2014-15, a real increase of $125 million compared to 2010-11.

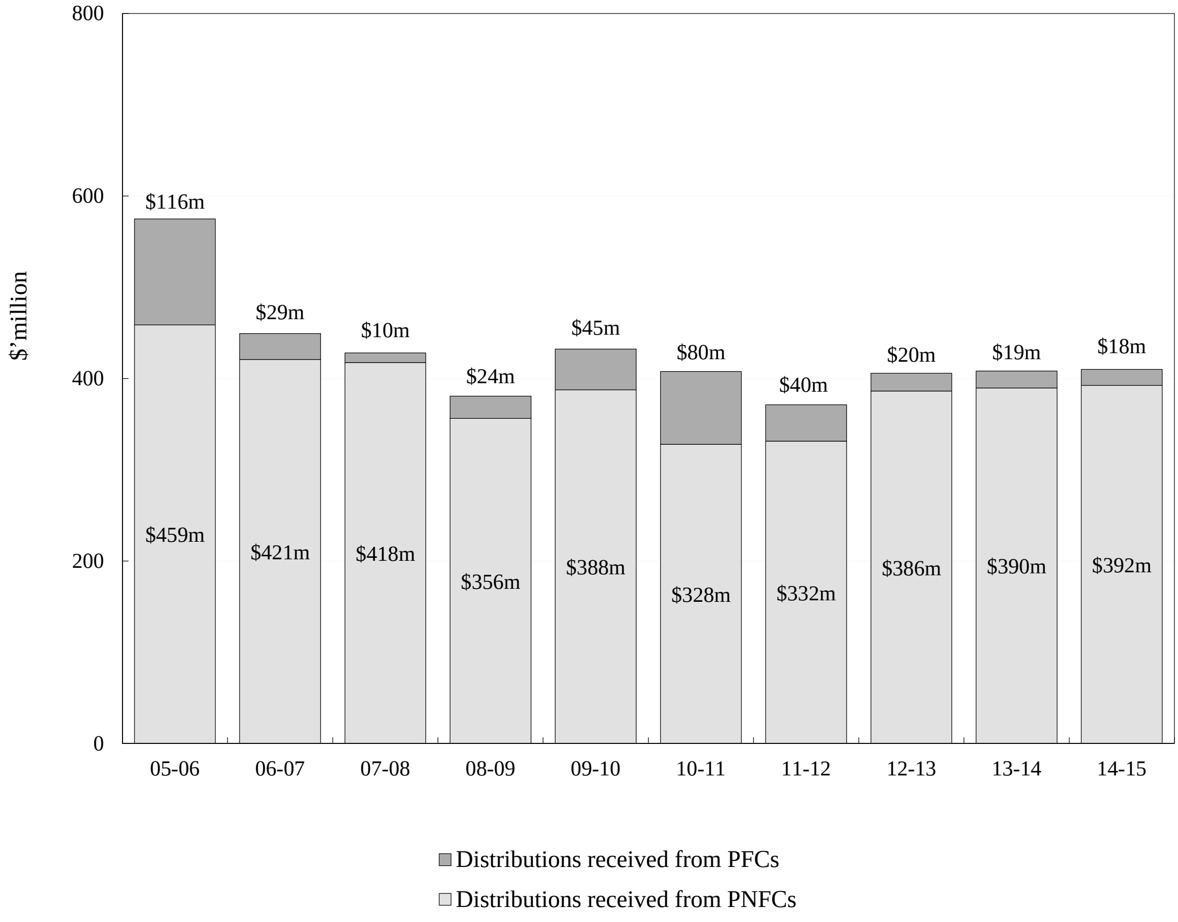
7.5 Dividend and income tax equivalent income

Dividend and income tax equivalent income are the distributions received from public non-financial corporations (PNFCs) and public financial corporations (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 2014-15.

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



Total distributions for 2010-11 are estimated at $408 million, $55 million higher than expected due to improved distributions from SA Water partially offset by reduced estimates from the Land Management Corporation and HomeStart Finance.

Chart 7.6 highlights that distributions for 2010-11 were maintained at long term trend levels by higher than normal PFC distributions. $50 million was received from SAFA in 2010-11 as a return of excess capital from its treasury operations. SAFA's capital at 30 June 2011 was $249.1 million ($257.5 million).

For 2010-11, the distributions from SA Water were revised upwards due mainly to decreased expenses associated with the delay of the delivery of water for the Adelaide Desalination Plant and delays in a number of smaller infrastructure projects. Distributions from the Land Management Corporation were revised down in 2010-11 due mainly to lower than forecast sales revenue and the deferral of commercial property sales to 2011-12.

The chart shows that total distributions in 2011-12 are estimated to be the lowest for the 10 years covered.

7.6 Other revenue

Other revenue mainly comprises royalties, fines and penalties and schools fundraising revenue. Other revenue is expected to be $695 million (nominal) in 2014-15, a real increase of 20.3 percent compared to 2010-11.

7.7 Risks to revenue

The Budget Papers provide quite 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 percent in taxation revenue, not including GST revenues, equates to about $41 million per annum.

- ***GST revenue grants*** – a variance of 1 percent in GST revenue growth has a revenue impact of $42 million per annum. Revised Commonwealth Government estimates of the GST pool in 2010-11 are 5.2 percent below the estimate of the GST pool made at the time of the Commonwealth's 2010-11 Budget.

  Commonwealth General Purpose Payments are the vehicle for horizontal fiscal equalisation (HFE). The methodology and data underlying the HFE process is determined by the Commonwealth Grants Commission (CGC). Methodology changes may impact on the State, either positively or adversely. A 0.01 percent change in South Australia's relativity results in a change in GST revenue grants of about $32 million.

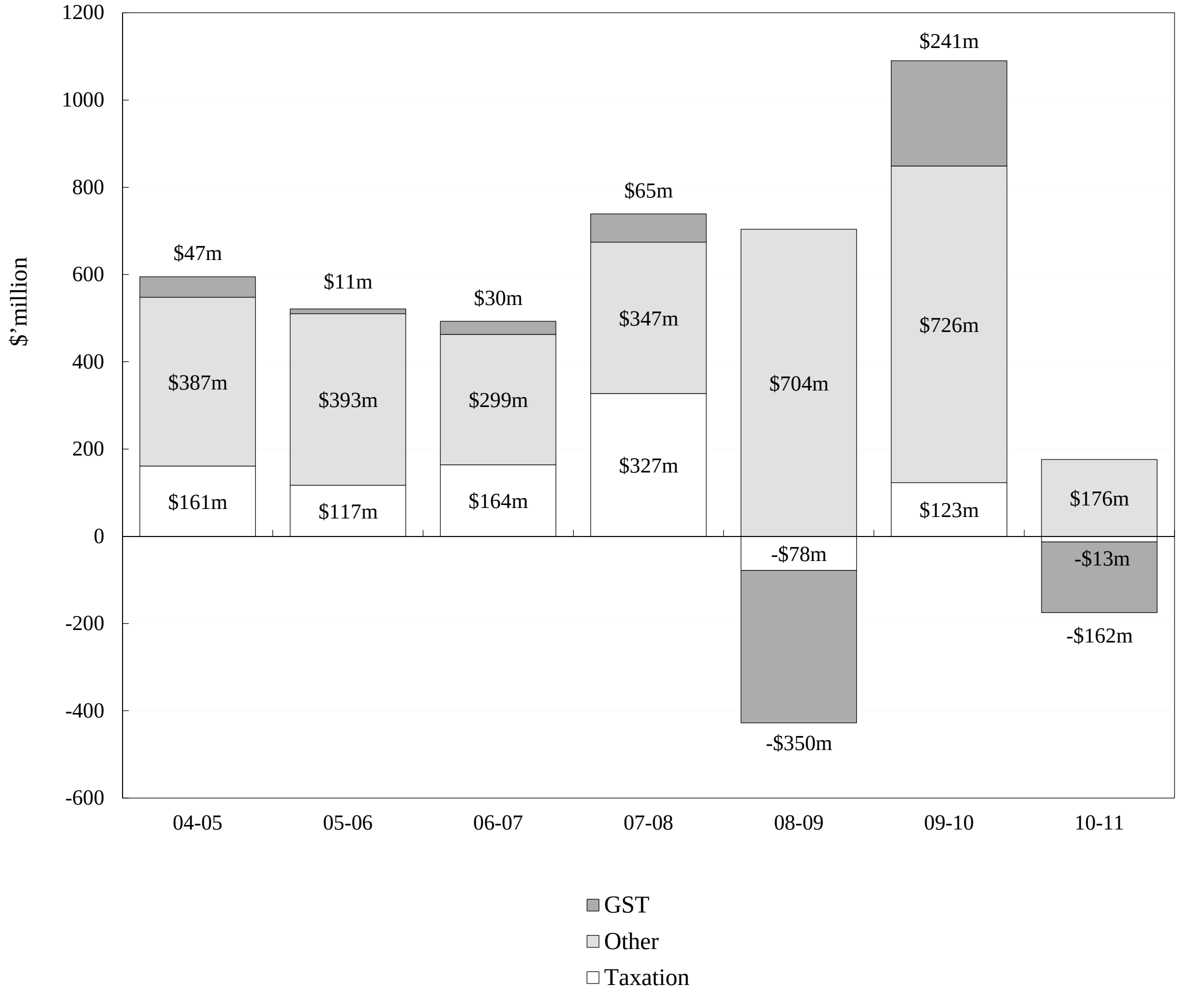
- ***Commonwealth specific purpose grants*** – payments for specific purposes from the Commonwealth account for about 24 percent of state government revenues. Variations in their level or the conditions applying to these payments pose a risk to the Budget.

Readers are referred to the Budget Statement 2011-12, Budget Paper 3, Chapter 6 for the full details.

7.7.1 Past revenue outcomes

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

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



(a) 2009-10 is influenced by Commonwealth stimulus grants

The chart highlights the very large favourable variations from budget that were enjoyed up to 2007-08, prior to the unfavourable variations in GST and taxation revenue noted in 2008-09 mainly attributable to the global financial crisis. In 2009-10 a return to a favourable variation to budgeted revenue is noted, reflected by a net $1090 million improvement mainly from additional NPPs.

Estimated results for 2010-11 anticipate that revenues are on budget, with favourable variations in other revenues of $176 million (mainly distributions from PFCs and PNFCs), offset by an unfavourable variation in GST revenues of $162 million and taxation of $13 million.

8 Expenses

8.1 Expenses overview

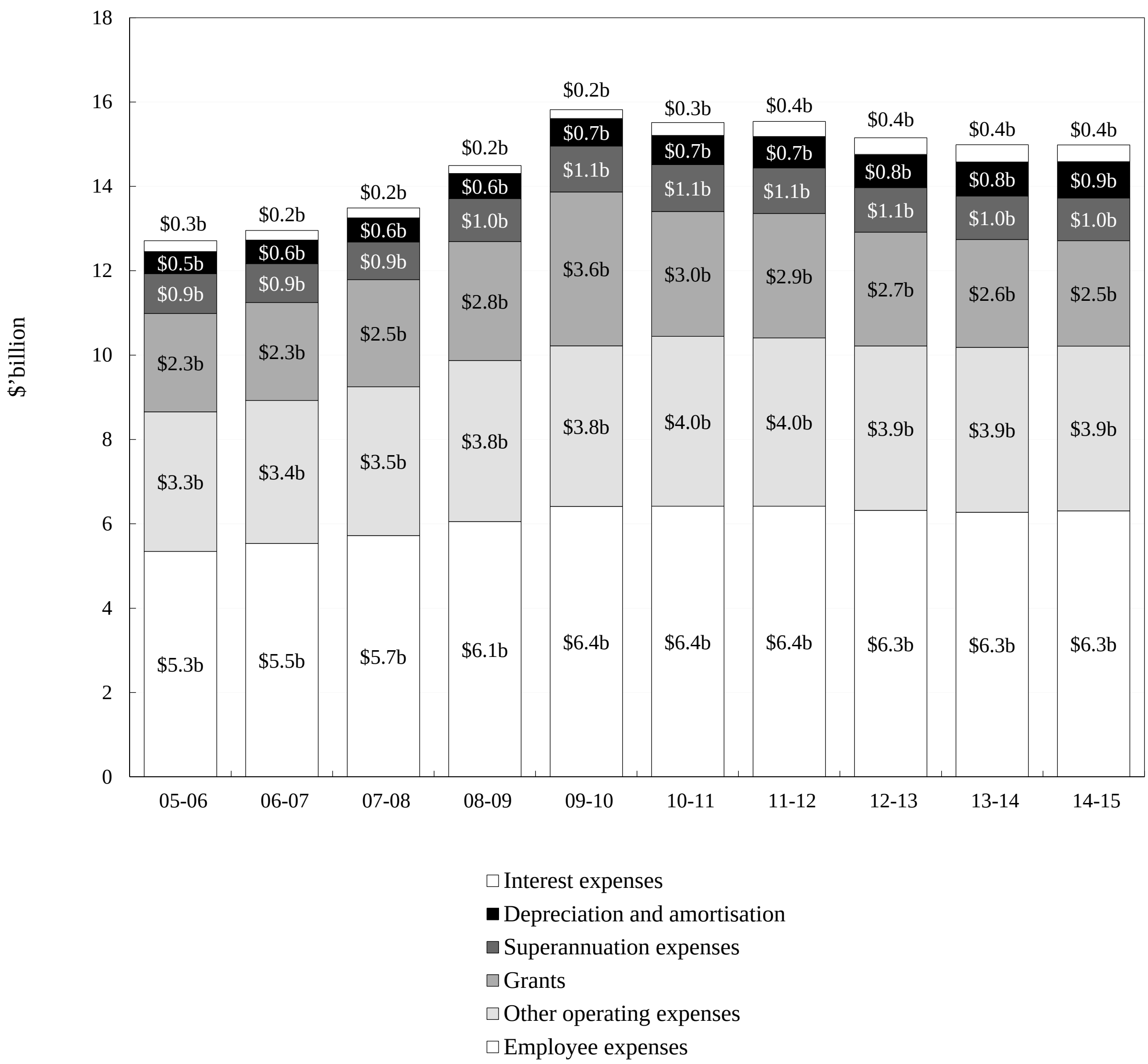
As with revenue, the global financial crisis combined with changes to Commonwealth and state financial arrangements caused a change in the composition of total expenses over the period 2008-09 to 2012-13 as grants expense is influenced by the flow through of Commonwealth grant revenue.

For 2010-11 estimated expenses total $15.5 billion and exceed budget by $39 million or 0.3 percent.

Total expenses for 2011-12 are budgeted to be $16 billion, $476 million or 3.1 percent higher than 2010-11 and grow to $16.7 billion in 2014-15.

The following chart highlights the trends in expenses (in real terms) that have emerged since 2005-06.

Chart 8.1 – General government sector - expenses (real)



The chart shows expenses grow annually from 2005-06 to 2009-10, trending downwards thereafter.

The following discussion focuses on some of the major components that make up expenses. Detailed comments on expenditure are provided in Budget Statement 2011-12, Budget Paper 3, Chapter 2.

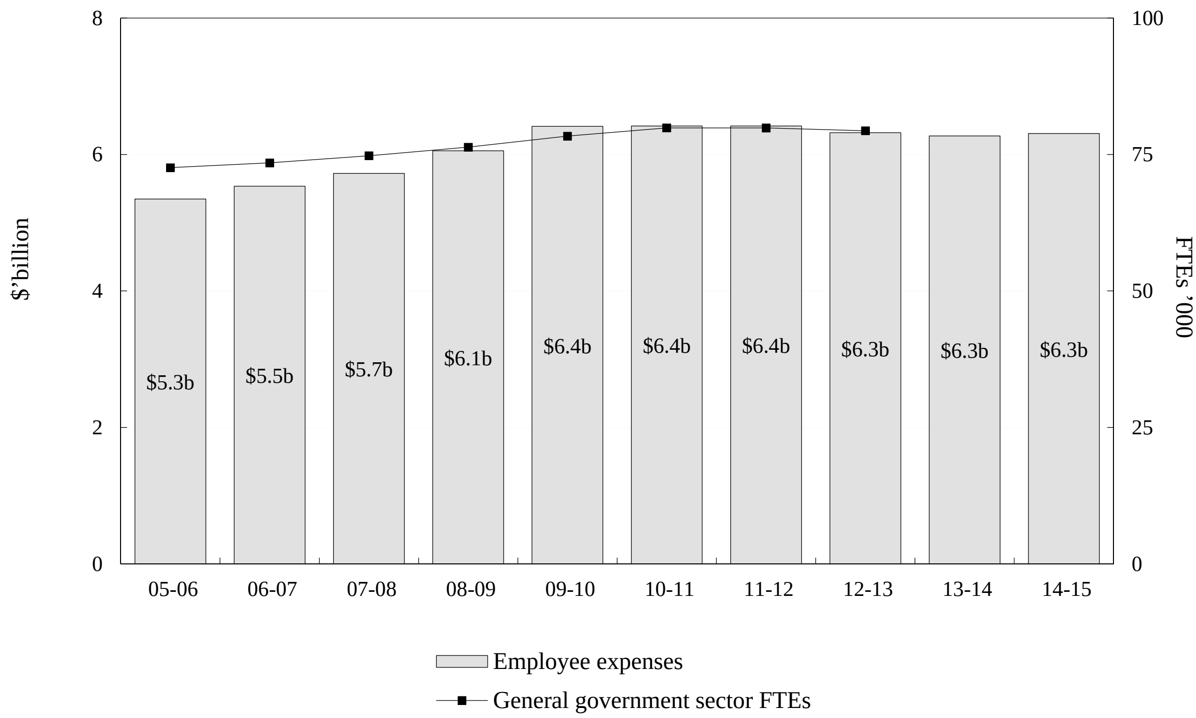
8.2 Expenses by type

8.2.1 Employee expenses

Employee expenses (an estimated $6417 million in 2010-11) represent the highest proportion (41 percent) of total expenses. They are estimated to increase by 2.9 percent in 2011-12 and about 2.2 percent per year to 2014-15.

The following chart shows employee expenses in real terms and available FTE data from the Office of Public Employment (OPE) and DTF estimates.

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



(i) 2005-06 and 2006-07 are actual FTEs provided by OPE.
(ii) 2007-08 to 2012-13 are DTF estimates

The chart highlights the real terms growth in employee expenses until 2009-10. This growth is consistent with FTE numbers. Employee expenses remain generally constant for 2010-11 and 2011-12 and are projected slightly downwards thereafter.

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

In the four years to 2010-11 employee expenses grew by an average of 6.8 percent per year. The 2011-12 Budget shows employee expenses decreasing in real terms on an average of 0.4 percent. This is mainly 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 2011-12. A proportion of the salaries and wages contingency allowance is included in other operating expenses.

The 2011-12 Budget provides for anticipated public sector wage increases over the forward estimates period, both in individual agency budgets, and in the total of the contingency items in the 'Administered Items for Department of Treasury and Finance' to cover future enterprise agreement outcomes.

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

At the time of the presentation of the 2011-12 Budget the main enterprise agreements currently under negotiation or expected to commence negotiation during the next 12 months include:

- SA Ambulance Service employees
- wages parity (building, metal and plumbing trades)
- SA Metropolitan Fire Service (fire fighters)
- salaried medical officers, clinical academics and visiting medical specialists
- wages parity salaried group
- school and preschool employees and TAFE lecturers.

The Government has indicated it will continue to negotiate wage outcomes consistent with ensuring sustainability of the State's finances. Enterprise agreements generally extend over three years with annual increases/outcomes within agreement sometimes differing from year to year. Outcomes in recent years, while in strong economic times, have in some periods been within this limit but generally exceed the Government's current target, with some sectors receiving much more.

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

- Police – 1 July 2010 and 1 July 2011 – 3.5 percent; 1 July 2013 – 3 percent.
- Nurses/midwives – 1 October 2010, 1 December 2011 and 1 October 2012 – 2.5 percent.
- Wages parity (weekly paid) – $25 per week effective 1 October 2009, 1 October 2010 and 1 October 2011.
- Assistants to members of Parliament – 1 October 2009, 1 October 2010 and 1 October 2011 – 2.5 percent.
- Fire fighters – 1 January 2009 – 8.2 percent.
- Salaried medical officers and clinical academics – 14 April 2008 – 14.7 percent, 14 April 2009 and 2010 – 3.5 percent.
- Pre-school and school sector education classifications – 1 October 2009, 2010 and 2011 – 4 percent.

- TAFE sector lecturers – 1 October 2009, 2010 and 2011 – 3.5 percent.
- Wages parity (salaried group) – 1 October 2009 – 2.5 percent.
- Visiting medical specialists – 1 January 2010 – 3.5 percent, 1 January 2011 and 2012 – 4 percent.

Circumstances for the respective groups naturally differ, but many of these examples were beyond the Government's current target and vary across groups.

8.2.2 Other operating expenses

Other operating expenses include general purchases of goods and services.

These expenses are estimated to be $4.1 billion for 2011-12, an increase of $79 million or 2 percent in nominal terms from 2010-11. The projection for the forward years to 2014-15 is for a real terms decrease of 3 percent.

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 two years to 2011-12.

Table 8.1 – Contingency provisions

	2010-11 Budget $'million	2010-11 Estimated result $'million	2011-12 Budget $'million
Employee entitlements	156	167	161
Investing contingencies	64	97	131
Supplies and services	269	53	279
	489	317	571

The 2011-12 Budget includes contingency amounts totalling $571 million, $82 million more than the previous Budget and $254 million more than the estimated outcome for 2010-11. While allocating sums to each of the categories for presentation purposes, contingency funds may also be transferred from other lines where available.

The inclusion of contingencies is a consistent approach to previous Budgets.

8.2.4 Grants

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

- grants to non-government schools, local government and industry

- appropriations for the South Australian Housing Trust
- community service obligation payments to SA Water and the South Australian Forestry Corporation.

As mentioned, over the period 2008-09 to 2012-13 grants expense is influenced by the flow through of Commonwealth grant revenue. Table 6.6 shows the changes in grants expense over the forward estimates. Grants are estimated to be $2960 million for 2010-11 or $113 million (3.7 percent) under budget.

Grants are budgeted to increase by $74 million to $3034 million in 2011-12 largely due to the transfer of Commonwealth grants to SA Water for the Adelaide Desalination Plant and grant payments for the redevelopment of the Adelaide Oval, partially offset by reductions in payment of Commonwealth stimulus funding.

8.2.5 Superannuation expenses

8.2.5.1 Superannuation interest cost

In 2011-12 and across the forward estimates, superannuation interest cost is expected to be marginally lower than estimated in the 2010-11 Budget, in the order of $7 million each year.

The Budget Papers note that a 1 percent lower than expected return on superannuation assets invested by Funds SA would increase estimated unfunded superannuation liabilities by around $46 million. An increase in unfunded superannuation liabilities of this magnitude would increase superannuation interest cost, decreasing the net operating balance result by around $3 million per annum.

8.2.5.2 Other superannuation expenses

Other superannuation expenses are employer superannuation contributions incurred by government agencies during the reporting period and include superannuation contributions on salaries and wages. It also includes superannuation on-cost on accrued leave. Estimated other superannuation expenses were $684 million in 2010-11 and are projected to increase to $729 million in 2014-15, a real decrease of 4.5 percent.

8.2.6 Depreciation and amortisation

Estimated depreciation and amortisation expenses were $693 million in 2010-11 and are projected to increase by 39 percent to $961 million in 2014-15. The increase reflects the growth in the value of fixed assets through purchases and revaluations.

8.2.7 Interest expense

Estimated interest expense in 2010-11 was $307 million and is projected to increase by 45 percent to $444 million in 2014-15 as a result of projected increased borrowing to fund capital programs and moderate rises in interest rates across the forward estimates.

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

8.2.8 Capital payments

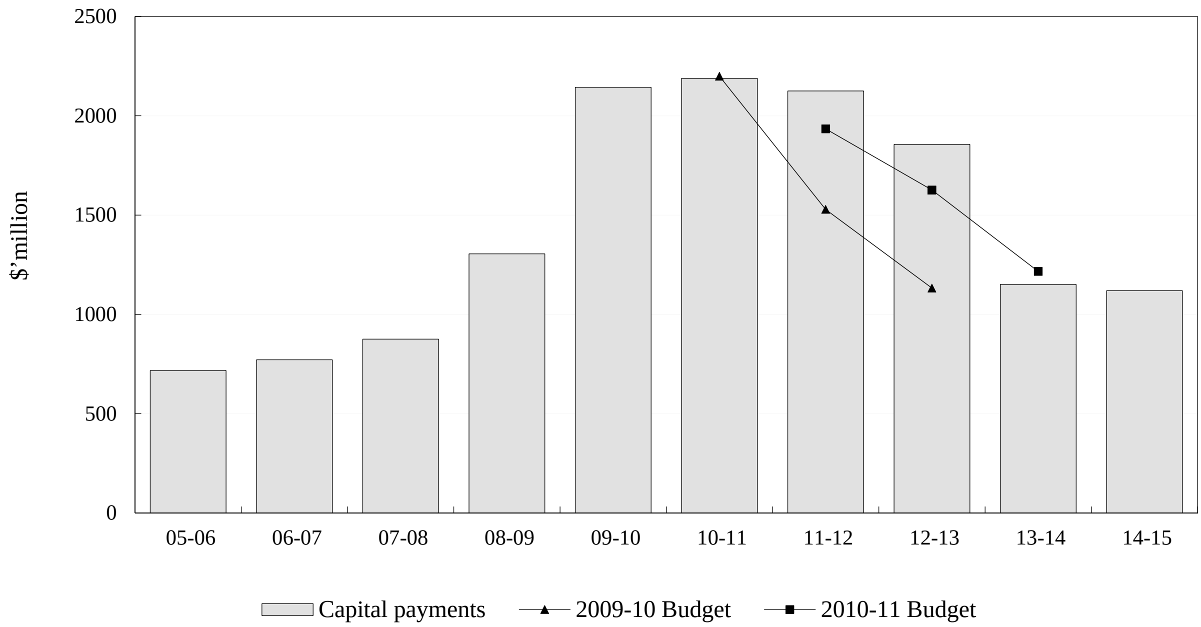
Capital project payments are represented by the value of purchases of non-financial assets in the General Government Sector Operating Statement.

In the 2009-10 Budget, the combined influence of state and Commonwealth spending initiatives, elevated general government sector capital spending estimates to extraordinarily high levels. The estimated result for 2009-10 purchases of non-financial assets is $2.2 billion, $94 million less than budget for the year but the peak in capital spending based on recent past outcomes and future estimates.

Purchases of non-financial assets are estimated to be $2.1 billion in 2011-12. The budget includes a slippage allowance of $300 million, the same as the previous year. The slippage allowance is based on the established tendency for projects to slip behind schedule.

The following chart shows the purchase of non-financial assets over the 10 year period to 2014-15, overlayed with budgeted purchases from the 2009-10 and 2010-11 Budgets.

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



The chart shows the variability of the expenditure, both historically and in the forward estimates and the increases since the 2009-10 Budget. Although there will be components of future expenditure that have effectively been committed, the forward years contain funds contingent on approvals. The investing contingency provision for 2011-12 is $130.7 million.

Major projects carry high inherent risks including cost estimating, escalations and timeliness of completion. Sustained higher capital outlays than have been made in past years, need support from appropriate project management expertise, information systems and controls. For 2009-10 and 2010-11 the State has achieved budgeted capital expenditure exceeding $2 billion annually. As in past years, carryover adjustments are made where appropriate if delays occur in budgeted project expenditure in the year but which will now be incurred in later years. Investing carryovers from 2010-11 to 2011-12 and future years are $205 million.

8.2.9 Public private partnerships

Public private partnership (PPP) projects form a part of the annual capital program.

Two major PPPs in progress are the Education Works New Schools PPP project and the new Royal Adelaide Hospital project.

Contractual close of the Education Works New Schools PPP project was achieved in early July 2009. At that time, the net present value cost of the contract arrangement was $323 million including the cost of construction, management and maintenance of the schools and equipment provision and replacement over a 30 year period. Total estimated investing expenditure on the Education Works – Stage 1 up to 2010-11 is $200 million including capitalisation of leased assets and equipment. For the 2011-12 Budget, operating costs are estimated at $33.8 million in 2011-12 and $26.6 million annually through to 2014-15.

In June 2011 the Government announced financial close on a contract with SA Health Partnership (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 Government advised that the total capital cost was higher than first estimated as previous capital cost estimates did not make a full allowance for risk. The hospital will also be larger and have an improved ICT system than was first proposed.

The current forward estimates to 2014-15 do not recognise the completion of the new RAH and the commencement of annual service payments as they are scheduled to occur in 2015-16. The Government has indicated it will then pay an average $397 million a year for 30 years to SAHP who will be responsible for the non-clinical costs of running and maintaining the hospital

8.2.9.1 Financial reporting of public private partnership projects

Depending on the terms of contracts, PPP 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 a 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 State Balance Sheets (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 Australian accounting standards 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.

The Government has a PPP arrangement for police stations and some court facilities. These arrangements are accounted for as an operating lease. Lease payments in 2010-11 were $5.2 million.

DTF have advised that capital components of PPPs arrangements for schools and the new hospital are to be recognised as finance leases 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.

The Portfolio Statements Budget Paper 4 Volume 3 for Education and Children's Services records an increase in total assets partly due to recognising an asset for the finance lease associated with the establishment of the new schools as per Education Works – Stage 1 PPP arrangement ($178 million). An increase in total liabilities is due mainly to the recognition of a liability for the finance lease for the PPP ($178 million).

As indicated, the current forward estimates do not recognise the completion of the new RAH and the commencement of annual service payments as they are scheduled to occur in 2015-16. The current forward estimates end in 2014-15. DTF has advised that the PPP contract will be recorded as a finance lease liability in 2015-16 when the RAH becomes available for use by the State. DTF currently estimates the value of the lease liability at $2.8 billion. This will add substantially to net debt from 2015-16.

This liability is in addition to the estimate of $244.7 million of state investing expenditure (inclusive of road works managed by Department for Transport, Energy and Infrastructure) on the upgrade and connection of utilities, key clinical equipment, state project management and other site works.

As noted, the average full year service payment will be $397 million, varying slightly each year with lifecycle costs. DTF has advised that this payment will need to be recognised when the new hospital begins operating noting that only part of this amount will be expensed as it includes cash payments associated with the lease liability. The details of the Budget impacts for 2015-16 were still being finalised. In addition to the service fee payout, other issues include:

- any offsetting reductions in running costs for the current RAH site
- depreciation impacts
- timing and part year issues in 2015-16 as the first full year operation of the new RAH will be 2016-17.

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.

Sales of assets for 2010-11 are estimated to be $102 million, $99 million less than targeted in the 2010-11 Budget. Asset sales are projected to increase over the forward estimates, peaking at $418 million in 2012-13.

The estimated sales in the forward estimates for the non-financial public sector include proceeds from the forward sale of up to three harvest rotations for ForestrySA plantations (announced in the 2008-09 MYBR) and a recently proposed sub-licence giving the right to operate the SA Lotteries' brands and business for a defined period of time. Proceeds from these initiatives and other asset sales have not been separately disclosed in the Budget so as to avoid prejudicing processes, but they are substantial to the estimated net debt projections within the four years of the 2011-12 Budget. The Budget notes that reductions in interest costs in the Budget arising from debt retirement may be at risk if the Government is unable to achieve the value estimated for divestment of ForestrySA harvest rotations, the new SA Lotteries sub-licence and selected government owned properties.

Processes for the sale of the South Australian Forestry Corporation's assets progressed through 2010-11. Audit was previously advised the sales process would include scoping studies, due diligence and marketing to obtain the best possible price.

The proposal to create a new SA Lotteries licence was announced in the 2011-12 Budget. Audit asked DTF to indicate the process that will be used to issue the lotteries licence.

DTF responded that the new licence, along with the SA Lotteries' corporate product brands, will continue to be owned by the State, with a sub-licence giving the right to a private party to operate the SA Lotteries' brands and business for a defined period of time. The indicative program for the State to create the new sub-licence and allocate it to the private sector, subject to further development and change, is as follows:

- prepare SA Lotteries new sub-licence for sale including developing transition plans for policy issues and due diligence
- marketing/expressions of interest
- indicative bids

- final bids
- Cabinet approval to execute the new sub-licence.

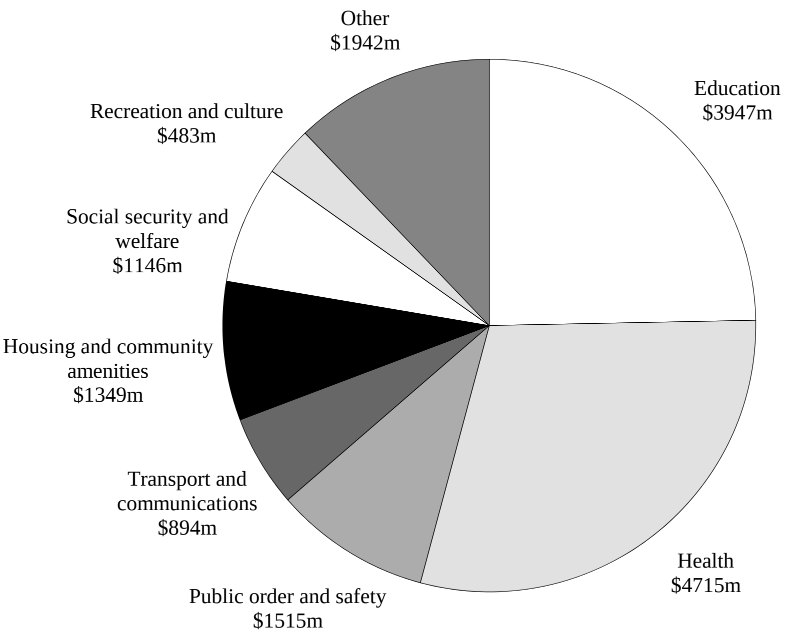
DTF also advised that appropriate project governance will be established in consultation with relevant parts of Government in order to implement the proposal. A Steering Committee for the project has been established that will report to the Treasurer through the Deputy Under Treasurer.

Implementation of any approved transaction will be done by the Government Enterprises and Market Projects Branch in DTF and led by a Project Director. A number of specialist advisors and consultants will be engaged to assist in the implementation of the proposal.

8.3 Expenses by function

The GFS reporting framework also provides information on expenditure (excluding capital payments) by its function for the general government sector. The following charts the 2011-12 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[13]



8.4 Risks to expenses

8.4.1 Overview

As with revenue, the 2011-12 Budget provides detailed consideration of various risks to the expenditure budget and acknowledges the management task for achieving budgeted outcomes.[14]

[13] Budget Statement 2011-12, Budget Paper 3, Table 2.16
[14] Budget Statement 2011-12, Budget Paper 3, p 94

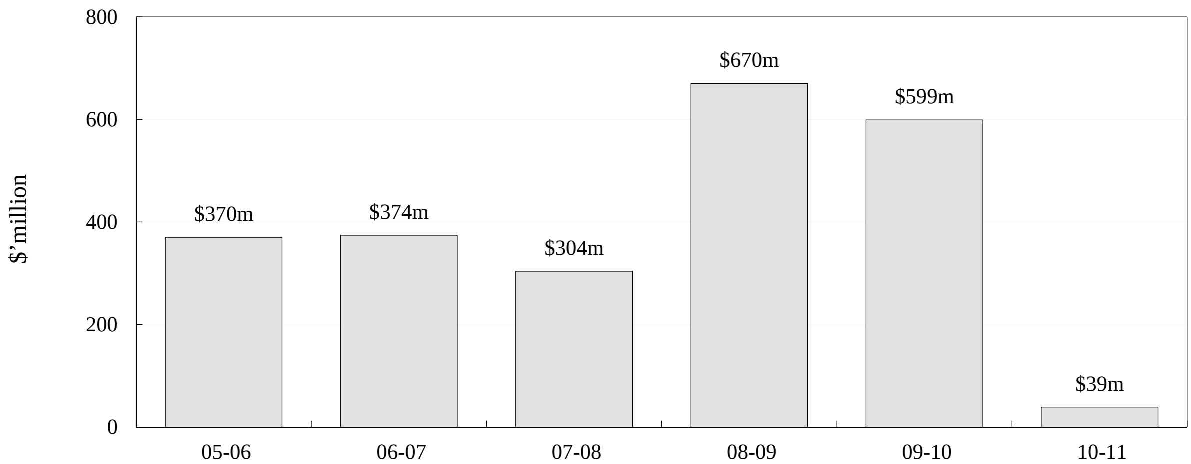
Some of the key risks reported are:

- ***Wages and salaries*** – an increase of 1 percent per annum above the amounts factored into the Budget would have an adverse impact of approximately $225 million in 2014-15.
- ***Capital investment pressures*** – a number of departments including Transport, Energy and Infrastructure and Health have large capital investment programs over the forward estimates period. Historically there has been considerable 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 percent increase in costs for the capital program in the general government sector will increase expenditure by approximately $21 million in 2011-12.

To provide a recent historic 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) 2010-11 is the difference between budget and the estimated result.
(b) 2008-09 and 2009-10 are influenced by Commonwealth stimulus grants.

The chart highlights that, notwithstanding classification changes, expenses consistently exceeded original budget expense targets in the three years to 2007-08 due to parameter variations and policy measures.

While 2008-09 and 2009-10 also exceeded budget, for the various reasons explained in this report, mainly to do with the global financial crisis, much of this increase was funded by Commonwealth stimulus grants.

When compared to variances experienced over the previous five years, total expenditure for 2010-11 is estimated to exceed budget by a relatively minimal $39 million.

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 Sustainable Budget Commission.

8.4.3 Savings strategy 2010-11

The Sustainable Budget Commission reported to the Government and the 2010-11 Budget included savings measures that addressed and consolidated past savings with new savings. The Government stated that specific measures announced in the 2010-11 Budget achieved remaining unspecified savings of over $700 million per annum by 2013-14. The 2010-11 Budget also included new operating savings totalling $1526 million over the next four years.

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

Audit requested advice from DTF of any changes to the 2010-11 announced new savings measures including:

(a) information (by agency or portfolio) which details the achievement of the 2010-11 budget savings announced in the 2010-11 Budget ($124.8 million)

(b) a reconciliation, by agency or portfolio, of the operating initiatives for 2011-12 and beyond announced in the 2010-11 Budget ($1.4 billion) with those remaining in the 2011-12 Budget.

The following table sets out adjustments made to the 2010-11 announced savings measures.

Table 8.3 – Summary of adjustments to 2010-11 budget new operating savings

	2011-12 $'million	2012-13 $'million	2013-14 $'million	total $'million
Parks Community Centre	-1.9	-4.2	-4.8	-10.9
Procurement efficiencies	-1.4	-1.4	-1.4	-4.2
Disability Client Trust Management	-0.7	-	-	-0.7
Reform of public sector recreation leave loading arrangements	-	-22.8	-23.7	-46.5
Total savings measures reversed or delayed	-4.0	-28.4	-29.9	-62.3

The following table is provided at the portfolio level consistent with the format of table 2.4 in the 2010-11 Budget Statement. Revenue measures are excluded.

Table 8.4 – Summary of adjusted 2010-11 new budget operating savings

Portfolio	Budget 2010-11 $'million	Revised 2011-12 $'million	Revised 2012-13 $'million	Revised 2013-14 $'million	3 year total $'million
Premier and Cabinet	3.8	8.6	17.0	25.0	50.6
Trade and Economic Development/ Defence SA	14.0	23.5	29.9	34.9	88.3
Treasury and Finance	5.4	11.4	16.4	18.5	46.3
Planning and Local Government	0.5	0.9	1.9	1.9	4.7
Justice	4.8	18.4	29.2	32.2	79.8
Primary Industries and Resources	14.2	18.2	22.4	25.6	66.2
Transport, Energy and Infrastructure	6.9	31.2	37.2	43.4	111.8
Health	17.6	61.8	103.8	132.7	298.3
Education and Children's Services	8.7	28.3	49.1	59.6	137.0
Families and Communities	2.2	8.8	18.2	19.6	46.6
Environment	6.0	11.5	22.3	29.8	63.6
Water	2.5	3.2	3.6	3.4	10.2
Tourism	1.1	3.0	4.0	4.6	11.6
Further Education, Employment, Science and Technology	11.4	21.4	29.1	37.2	87.7
Across Government Initiatives					
Reform of long service leave arrangements	-	28.7	30.1	31.8	90.6
Reform of recreation leave loading arrangements	-	-	-	-	-
Improved motor vehicle fleet utilisation	-	2.5	5.0	7.4	14.9
Motor vehicle fleet mix improvements	-	2.2	4.4	6.8	13.4
Ministerial office budgets reduction	-	2.6	2.9	3.4	8.9
First Home Owners Bonus Scheme reform	17.1	20.9	20.0	18.9	59.8
Introduction of First Home Owners Grant Property Value Cap	1.5	2.0	2.0	2.0	6.0
Removal of petroleum subsidy scheme	7.2	14.3	14.2	14.1	42.6
Total savings announced in 2010-11 Budget remaining in the 2011-12 Budget	124.8	323.3	462.8	552.8	1 338.9

DTF advised that generally, agencies had achieved their allocated savings targets for 2010-11. There would be a number of cases where agencies did not achieve the specific saving (eg for timing reasons) but found a replacement saving to ensure the overall target was achieved. This is evidenced by the fact that they have not overspent their total budget. There are several exceptions:

- Health had an $11.6 million shortfall from not achieving an Outpatient Services reforms measure ($10.9 million) and a delay in achieving some of the savings associated with the Corporate Services reform measure ($700 000).

- Savings associated with the petroleum subsidy scheme savings measure (across government measure held in DTF Administered Items) were lower than budget by $1.4 million as while the scheme closed on 1 January as planned, due to a month lag in subsidy claims the saving was the equivalent of five months not the six months budgeted.

- A $1.3 million shortfall in the Department for Families and Communities due to Cabinet's decision to reverse the 2010-11 Budget decision to close the Parks Community Centre.

Audit also requested advice from DTF on the achievement of the existing savings measures of $56.1 million in 2010-11. DTF advised that, as for the new savings there were a number of cases where agencies did not achieve the specific saving but found a replacement saving to ensure the overall savings target was met. Against the existing savings measures reflected in the $56.1 million, agencies were not reporting any shortfalls against the indexation measure, indicating that they are being managed, and only Health has reported a shortfall against the 2008-09 MYBR FTE reduction measure amounting to $1.5 million in 2010-11.

8.4.4 Nature of savings initiatives

Table 8.4 shows that the savings task for 2010-11 was $124.8 million. Table 8.4 also shows that the savings target increases annually being $323 million in 2011-12 and rising to $553 million in 2013-14.

The savings task falls on all portfolios of Government.[15] Details of the new savings initiatives announced in the 2010-11 Budget are included in Budget Paper 6 '2010-11 Budget Measures Statement'. This provides a reference for monitoring progress of the new savings program. Given the size of the savings target, individual measures encompass a broad range of activities. To illustrate, the nature of savings and some values where directly reported, include:

- reducing the number of public servants
- savings from efficiency dividends
- departmental efficiencies
- motor vehicle fleet reform - $31.7 million
- public sector long service leave arrangements reform - $90.7 million over three years
- public sector employee recreation leave loading alternative arrangements - $46.6 million over two years
- reducing government advertising - $18 million over four years
- facilities management savings - $31.5 million.

A number of issues arise that are relevant to achieving future savings.

Audit review of savings in this and past years shows that some areas of savings are more difficult to achieve than originally estimated. It is well known that health and, to a lesser but nonetheless substantial degree, families and community service areas, have had continuing budget pressure in recent years. The Department of Health is an agency that has found savings targets difficult to meet and, as noted, this again occurred in 2010-11. I have also reported that various factors have meant that savings from the shared services initiative may be lower than originally factored into the Budget.

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15 Budget Statement 2010-11, Budget Paper 3, Table 2.4.

The shared services initiative is also an area where savings have lagged behind the budgeted schedule. Progress with the shared services initiative is discussed in Part A of this Annual Report to Parliament.

I noted last year that an inherent risk of the overall savings strategy is its sheer size and breadth. Achieving the task will require significant discipline. Agencies have developed experience with implementing savings strategies over recent years but the savings targets are not always achievable by all agencies. As indicated, DTF have reported agencies achieved most of the 2010-11 targets. The remaining saving task is of a much greater scale. It presents risks including industrial action and public demand to maintain services. Implementing savings tends to be directed at administrative and support areas for services. Care needs to be taken that where this occurs, relevant changes to systems and procedures within a risk management context is addressed, to ensure the public interest is continually served by efficient and effective administrative performance and failures avoided.

8.4.5 Reduction of full-time equivalents

A key part of the savings strategy is to further reduce the number of FTEs. The combined savings measures announced in the 2010-11 Budget were estimated to result in the reduction of 3743 FTEs from the public sector by 2013-14. This reduction will be partially offset by an additional FTEs resulting from 2010 election commitments and other expenditure initiatives in the 2010-11 Budget. The net reduction of 1762 FTEs is around 2 percent of the general government sector workforce.

Table 8.5 – Full-time equivalent impacts of new initiatives in 2013-14

	Savings initiatives	Expenditure initiatives	Total
Health	(957)	1 277	320
Education and Children’s Services	(350)	66	(284)
Transport, Energy and Infrastructure	(213)	-	(213)
Justice	(206)	349	142
Primary Industries and Resources	(186)	7	(179)
Further Education, Employment, Science and Technology	(183)	127	(56)
Families and Communities	(108)	140	32
Others	(470)	15	(454)
Total 2010-11 initiative FTEs	(2 673)	1 981	(692)
Previously announced savings requirements			
2009-10 Budget indexation requirements	(342)		
Efficiency dividend	(328)		
FTE reduction target in 2008-09 MYBR	(400)		
Total previously announced savings requirements			(1 070)
			(1 762)

The 1070 FTE savings requirements were allocated to agencies in previous budgets and the 2008-09 MYBR. DTF advise that the FTE savings requirement associated with the 2009-10 Budget Indexation Savings and Efficiency Dividend is indicative only, being based on a standard distribution of the total budget savings between employee expenses and supplies and services. Agencies may implement savings strategies to achieve these measures that results in different FTE outcomes. The 400 FTEs in table 8.5 is the last two years of the FTE reduction target announced in the 2008-09 MYBR.

The timetable for achieving the FTE reductions or value equivalent is set out in the following table.

Table 8.6 – Full-time equivalent reduction 2010-11 to 2013-14

	2010-11	2011-12	2012-13	2013-14	Total
Total FTE reductions	(1 011)	(1 373)	(862)	(497)	(3 743)

For 2010-11 Audit sought an update of FTE monitoring arrangements including a copy of the data as at 30 June 2011 and the latest available reports used for FTE monitoring, including variance explanations and any action taken on variances. Audit also sought advice of any changes in monitoring systems or processes for the 2011-12 Budget.

DTF responded that FTE monitoring data for 30 June 2011 was received from major agencies on 11 July 2011.

The following table reflects information provided by the 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 agencies (excluding a number of small agencies). The FTE caps reflect agency profiling of the cap as at the end of June 2011.

Table 8.7 – Actual and cap FTEs by portfolio as at 30 June 2011

Portfolio	Actual FTEs	Approved CAP FTEs	Variance FTEs	Variance Percent
Health	29 975	29 856	118	0.4
Families and Communities	4 885	5 042	(157)	(3.1)
Education and Children's Services	20 731	20 764	(33)	(0.2)
Further Education, Employment, Science and Technology	3 342	3 303	39	1.2
Transport, Energy and Infrastructure	2 980	2 997	(17)	(0.6)
Justice	10 407	10 757	(350)	(3.3)
Primary Industries and Resources	1 220	1 321	(102)	(7.7)
Trade and Economic Development	125	124	1	0.5
Defence SA	39	44	(6)	(12.6)
Environment and Natural Resources	1 098	1 160	(62)	(5.3)
Water	373	410	(37)	(9.1)
Environment Protection Authority	216	212	4	2.0
Treasury and Finance	1 290	1 404	(115)	(8.2)
Premier and Cabinet	821	853	(32)	(3.8)
Tourism	144	169	(25)	(14.7)
Planning and Local Government	163	179	(16)	(9.0)
Total	77 808	78 596	(788)	(1.0)

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

Portfolios above the cap:

- Health has reported that actual FTEs were 118 FTEs above its cap as at 30 June. This comprises 151 FTEs above the cap in the Health Units, associated with above budgeted expenditure, offset by below cap projections for the Department of Health (18 FTEs) and SA Ambulance Service (15 FTEs). A central contingency provision of 147 FTEs was established for 2010-11 (as part of the 2011-12 Budget deliberations) to meet increases in the cost of service delivery.

- Department of Further Education, Employment, Science and Technology has reported that actual FTEs were 39 FTEs above its cap at 30 June, primarily due to savings measures being managed through reductions in other expenditure lines rather than FTE numbers.

Portfolios below the cap:

- Justice was 350 FTEs below its cap, primarily due to:
  - South Australia Police (167 FTEs) mainly from unsworn vacancies (74 FTEs), reduced recruit intake (85 FTEs) and reduced community constables (12 FTEs)
  - Attorney-General's Department (111 FTEs) from across-department vacancies mainly within the Office of Consumer and Business Affairs and Office of Recreation and Sport
  - Department for Correctional Services (37 FTEs) mainly from vacancies due to difficulties in recruiting correctional officers.
- Department for Families and Communities was 157 FTEs below its cap, primarily due to vacancies held in Families SA (43 FTEs), vacancies in Disability SA that are being managed through increased use of overtime (46 FTEs) and vacancies in Domiciliary Care SA reflecting an increase in the number of agency staff as a strategy to reduce costs (39 FTEs).
- Department of Treasury and Finance was 115 FTEs under its cap, primarily due to vacancies within Shared Services SA (72 FTEs), Corporate Services (12 FTEs) and RevenueSA (14 FTEs).
- Department of Primary Industries and Resources was 101 FTEs below its cap, primarily due to vacancies resulting from uncertainty of external funding from research and development corporations and the decision to hold vacancies in order to achieve savings strategies.
- Department of Environment and Natural Resources (62 FTE) and Department for Water (37 FTE) were both below their caps primarily due to the earlier than budgeted completion of seasonal and/or externally funded projects.

DTF further advised that the Under Treasurer will write to the relevant Chief Executive where there are particular issues relating to the FTE cap data or reporting of FTE actuals for an agency. Issues will also be identified and reported to SBCC through the 2010-11 year-end review process. There are no additional FTE reporting requirements in 2011-12.

8.4.6 Targeted voluntary separation program

To support its savings target strategies, the Government has approved a targeted voluntary separation package (TVSP) scheme for employees who are or become excess to requirements as a consequence of savings measures or organisational changes and who are not assigned to other public sector employment. An offer of a TVSP can only be made to an employee who an agency has decided is excess to requirements because their assigned duties/role or position has or is to be abolished.

TVSPs became available from November 2010. The 2010-11 Budget contained various initiatives including ongoing savings requirements which are scheduled to occur progressively over the next four years. The Government anticipated that separation packages will be available until 2013-14.

Audit sought a summary of TVSP payments for 2010-11 from DTF as it is responsible for coordinating aspects of the program.

DTF clarified the current status of the program and provided a summary of FTE reductions achieved in 2010-11. DTF advised that, as announced in the 2010-11 and 2011-12 Budgets, agencies are required to make significant savings by 2013-14, which will necessitate reductions in staff numbers. Agencies do not have a specific budget for TVSPs. The number of TVSP payments made is influenced by the extent to which FTE reductions are achieved through other means such as not renewing employment contracts, not filling vacancies as they occur and redeployment of employees within the South Australian public sector, as well as the rate of uptake of TVSPs by those employees who have been made an offer.

Table 8.8 sets out a summary of FTE reductions achieved through TVSP payments (excluding executive reductions) as reported to the DTF during the period 1 November 2010 to 30 June 2011.

Table 8.8 – FTE reductions from TVSPs reported by agencies 1 November 2010 to 30 June 2011

	FTE reductions From TVSPs
Attorney-General’s	19.6
Correctional Services	2.0
Education and Children’s Services	5.0
Environment and Natural Resources	39.3
Families and Communities	41.2
Further Education, Employment, Science and Technology	34.3
Health	70.3
Planning and Local Development	9.0
Premier and Cabinet	20.4
Primary Industries	30.8
SAFECOM	4.0
SA Ambulance Service	4.0
SA Police	4.0
SA Metropolitan Fire Service	3.0
SA Tourism Commission	5.0
Trade and Economic Development	45.4
Transport, Energy and Infrastructure	20.5
Treasury and Finance	19.3
ForestrySA (non-general government sector)	4.0
Total	381.1

Agencies are centrally reimbursed for TVSP payments made to achieve savings measures announced in the 2010-11 Budget, existing savings measures, and TVSPs made to existing redeployees.

Funding provided and the estimated timetable for the scheme is provided in the following table.

Table 8.9 – TVSP scheme costs

	2010-11 $'million	2011-12 $'million	2012-13 $'million	2013-14 $'million	Total $'million
Operating expenses	94.9	86.7	123.9	48.3	353.8

This initiative provides $353.8 million over four years for the cost of TVSP payments in support of employee separations underpinning savings initiatives contained in the 2010-11 Budget. This cost is based on the provision of 3000 TVSPs over the four year period.

To encourage early success of offers, an enhanced package operates where acceptance occurs within six months of an offer being made. A non-executive employee to whom an offer of a TVSP is made will be eligible to have a separation payment, calculated at the rate of 20 weeks pay, plus an additional three weeks pay for each completed year of service, up to a maximum of 116 weeks (equivalent to 32 completed years of service).

After six months from the date of the first offer of a TVSP, separation payments will be calculated at the rate of 10 weeks, plus an additional three weeks pay for each completed year of service, up to a maximum of 88 weeks (equivalent to 26 years of service).

Actual reimbursements up to 31 May 2011 totalled $31.8 million.[16]

8.4.7 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. Past Audit Reports have consistently emphasised the need for strong monitoring of budget progress and provided details of processes that applied in those years. As in previous years, following the release of the Budget, I asked DTF for details of any changes to capital, operating expenditure and saving/revenue monitoring processes for 2011-12. I also sought advice of which areas of the Budget DTF considered to be the highest risks and any specific monitoring measures.

DTF advised that the major risks to the fiscal outlook are set out in Chapter 6 of the 2011-12 Budget Statement (Budget Paper 3). These include the impact of economic activity on household spending patterns and demand for housing, which impact on GST and property taxation, and expenditure risks such as higher than expected wage increases, cost escalations on capital projects and activity growth in hospitals and schools.

The regular monitoring regime, coordinated by the DTF, includes monthly monitoring of financial performance against approved budget, and monitoring of capital projects, budget initiatives and FTEs on a quarterly basis. Reports on each aspect of the monitoring regime, based on information supplied by agencies and an analysis prepared by the DTF are provided to the Sustainable Budget Cabinet Committee (SBCC).

[16] As reimbursement requests occur in the month after the actual separation of the employees, reimbursements for TVSPs paid by agencies in June 2011 were processed by DTF in the 2011-12 year.

Given the magnitude of the Budget improvement measures introduced in the 2010-11 Budget ($2 billion over four years), and the importance to the fiscal outlook of the achievement of these measures, an enhanced monitoring process was also introduced in 2010-11 to monitor the progress of agencies in achieving their budget improvement measures and FTE reductions. Both regular and enhanced monitoring processes will continue in 2011-12.

The first round of enhanced monitoring, undertaken in early 2011, concentrated on agency progress in delivering the 2010-11 savings. This information was included in the documents discussed between the Treasurer and Ministers at the 2011-12 Budget bilateral meetings.

The second round of enhanced monitoring, being undertaken in July/August 2011, will focus on those savings measures commencing or significantly increasing in 2011-12 to ensure agencies are on track to deliver the required savings during 2011-12 and ensuring that plans are in place to deliver those measures that commence in 2012-13 and beyond. The Treasurer met with Chief Executives in August 2011 to obtain an overview of their progress in achieving the savings task and work through their implementation plans. The Treasurer will report to SBCC on the outcomes of the process, with individual Chief Executives required to meet with the full SBCC if significant issues impacting the achievement of savings or revenue measures are identified.

FTE reduction monitoring (originally a component of the enhanced monitoring process) will now be incorporated into the quarterly monitoring process.

For 2010-11, DTF advised that at the time of the 2011-12 Budget, Health were projected to overspend its budget by $66.7 million. A provision was made and held centrally (ie contingencies in DTF administered items) for this projected overspend. The components of the overspend included an increase in the cost of service delivery, a reduction in revenue associated with the Pharmaceutical Benefits Scheme and other revenue sources, timing of implementing hospital savings strategies and fee for service additional costs in Country Health SA.

9 Balance Sheet

9.1 Introduction

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

The information relates principally to data for both the general government sector and also the non-financial public sector, which consolidates the general government and public non-financial corporations (including SA Water and the South Australian Forestry Corporation).[17]

9.2 Overview of the State's financial position

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

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)

	2007-08 Actual $'million	2008-09 Actual $'million	2009-10 Actual $'million	2010-11 Estimated result $'million	2011-12 Estimate $'million	2012-13 Estimate $'million	2013-14 Estimate $'million	2014-15 Estimate $'million
Financial assets	20 539	22 449	25 363	23 760	23 604	24 339	25 047	25 632
Non-financial assets	16 161	18 595	29 680	31 088	32 134	32 818	33 046	33 201
Total assets	36 700	41 045	55 043	54 849	55 738	57 157	58 092	58 834
Total liabilities	12 959	16 898	18 811	17 393	18 025	18 366	18 580	18 091
Net worth	23 741	24 146	36 231	37 456	37 713	38 791	39 512	40 743
Net financial worth	7 580	5 551	6 551	6 368	5 578	5 973	6 467	7 541
Net debt	(276)	475	1 402	3 217	3 825	4 098	4 213	3 615

Note: Totals may not add due to rounding.

Of note is the expectation that:

- financial assets increase by $1872 million across the forward estimates. This is due mainly to investments in other public sector entities, up $2317 million partly off-set by a decrease in advances paid of $404 million
- non-financial assets increase by $2113 million over the forward estimates. This is mainly from the purchase of land and fixed assets

[17] Budget Statement 2011-12, Budget Paper 3, Appendix D details agencies within the respective sectors.

- net worth (assets less liabilities) increases across the forward estimates. This is due to asset growth

- net debt increases across the forward estimates to $4213 million in 2013-14 then decreases to $3615 million in 2014-15 due mainly to increased borrowing to fund major capital investment programs.

9.2.2 Non-financial public sector financial position

The following table provides time series data for the non-financial public sector.

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

	2007-08 Actual	2008-09 Actual	2009-10 Actual	2010-11 Estimated result	2011-12 Estimate	2012-13 Estimate	2013-14 Estimate	2014-15 Estimate
Financial assets	4 259	4 316	5 143	2 882	2 883	2 927	3 103	3 260
Non-financial assets	34 227	39 067	53 228	55 740	57 093	58 373	59 094	59 739
Total assets	38 486	43 384	58 371	58 622	59 976	61 300	62 196	62 999
Total liabilities	14 745	19 237	22 140	21 166	22 264	22 509	22 684	22 256
Net worth	23 741	24 146	36 231	37 456	37 713	38 791	39 512	40 743
Net financial worth	(10 487)	(14 921)	(16 997)	(18 284)	(19 381)	(19 583)	(19 581)	(18 996)
Net debt	1 611	2 872	4 487	6 872	7 922	8 175	8 170	7 553

This table highlights that:

- non-financial assets dominate the financial position

- the value of non-financial assets are estimated to increase by $2512 million in 2010-11 to $55.74 billion. The value of non-financial assets is estimated to increase by $3999 million by 2014-15. This increase mainly arises from the purchase of new assets and to a lesser extent asset revaluations, offset by asset sales and depreciation

- net financial worth is negative as financial liabilities exceed financial assets and is estimated to generally deteriorate over the forward estimates period

- net debt is estimated to increase over the forward estimates period.

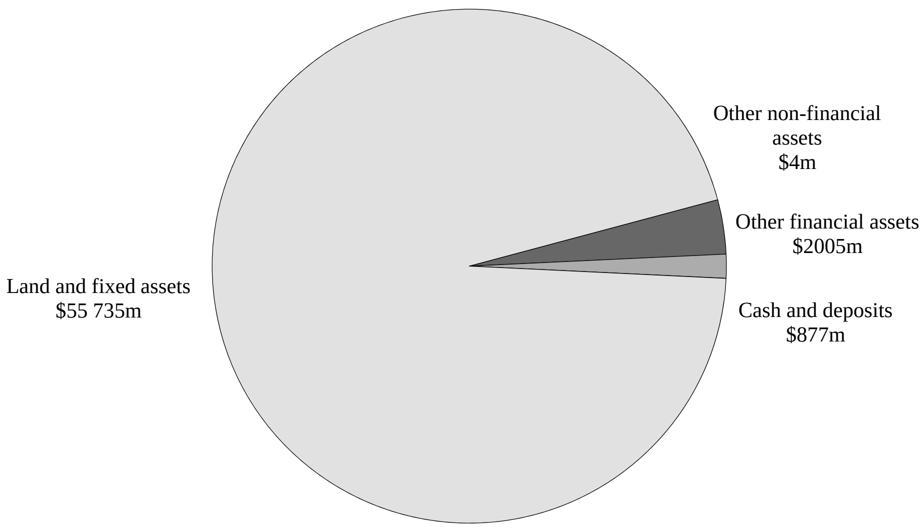
9.3 Assets

Table 9.2 shows that the State's asset position is growing from year to year because of major asset acquisitions or revaluations. This position is similar to interstate jurisdictions, where similar trends are noted.

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 2011 for the non-financial public sector.

Chart 9.1 – Non-financial public sector assets at 30 June 2011



Other financial assets include equity of $754 million. This comprises $764 million in other investments offset by a negative $10 million equity investment in other public sector agencies.

Non-financial assets clearly represent the vast majority of State assets being 95 percent of the total. The State's non-financial or physical assets comprise mainly plant, equipment and infrastructure (including roads and water infrastructure) and land and improvements. These assets are divided between the general government and public non-financial corporations sectors.

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

9.3.1.1 Revaluation of non-financial assets

Revaluations of non-financial assets will generally have the most influence in the improvement of the State's net worth. To illustrate, the following chart summarises actual asset value changes over the four year period 2007-08 to 2010-11 for the major agencies in the general government and public non-financial corporations sectors.

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

	2007-08 $'million	2008-09 $'million	2009-10 $'million	2010-11 $'million	Total $'million
General government	961	1 142	9 702	365	12 170
Public non-financial corporations	863	1 729	1 178	1 460	5 216
Total	1 824	2 871	10 880	1 825	17 386

Revaluation of the assets of the major agencies added $17.4 billion to the total value of non-financial assets over the four year period to 2010-11.

During 2009-10 the value of the State's road network increased by $9.1 billion and reflects an internal revaluation undertaken by the Department for Transport, Energy and Infrastructure. A key assumption of the revaluation model adopted by the Department is that the road network would be replaced by a modern equivalent asset rather than replacing the existing 'as constructed' network. Further commentary is included under 'Department for Transport, Energy and Infrastructure' in Part B of this Annual Report to Parliament.

9.3.2 Public financial corporations financial assets

The majority of the Government's financial assets are held by Funds SA. This includes funds of the Motor Accident Commission and SAFA. The following table shows Funds SA's holdings of investment assets as at 30 June 2010 and 30 June 2011:

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

	Domestic equities $'million	International equities $'million	Fixed interest $'million	Other investments $'million	Total $'million
2010-11	4 413	3 640	1 924	6 897	16 874
2009-10	3 798	3 267	1 509	6 196	14 770

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

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

Funds SA incurred a net gain from investing activities in 2010-11 of $1628 million reflecting the ongoing recovery of financial markets during the year. As the majority of managed funds are superannuation assets, much of this gain is reflected in an improvement in the unfunded superannuation liability. This net gain builds on the prior year net gain of $1516 million.

The positive market returns contributed to an improvement in the Motor Accident Commission's statutory solvency level, calculated in accordance with a formula determined by the Treasurer. As at 30 June 2011 the Commission had net assets of $431.1 million. The assets of the compulsory third party fund as at that date were 103.6 percent of the target level of solvency compared to 97.1 percent the previous year.

WorkCoverSA also incurred a gain on investments that contributed to an improvement in its net liability position to $951.7 million.

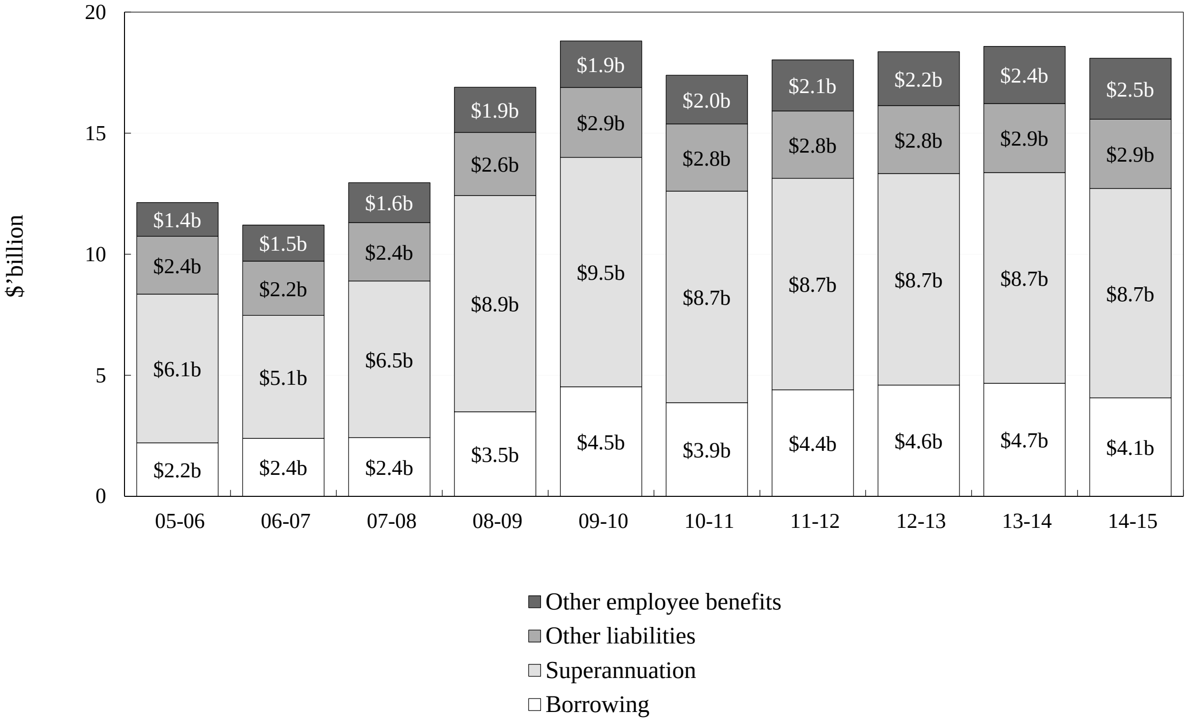
Further commentary is included under 'Motor Accident Commission', 'South Australian Government Financing Authority', 'Superannuation Funds Management Corporation of South Australia' and 'WorkCover Corporation of South Australia' in Part B of this Annual Report to Parliament.

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 2014-15.

Chart 9.2 – General government sector liabilities (nominal terms)



Total liabilities are estimated to decrease by $1419 million or 7.5 percent to $17.4 billion in 2010-11. This is due mainly to decreases in the unfunded superannuation liability and borrowings. The variability in the unfunded superannuation liability in the five years to 2010-11 is due mainly to movements in earnings, actuarial assumptions and the discount rate used to estimate the value of the liability.

Total liabilities are expected to increase by $701 million or 4 percent to $18.09 billion over the period of the forward estimates. This is due mainly to increases in borrowings, up $196 million and other employee benefits, up $513 million, over the four years to 2014-15.

9.4.2 Non-financial public sector liabilities

The trends and composition of liabilities for the non-financial public sector are consistent with those of the general government sector.

Total liabilities are expected to increase $1090 million or 5.1 percent to $22.3 billion over the period of the forward estimates. A $973 million or 4.4 percent decrease in total liabilities in 2010-11 is due to an decrease in borrowings, down $211 million or 2.8 percent, superannuation liabilities, down $744 million or 7.8 percent and other liabilities $105 million or 3.4 percent.

9.5 Unfunded superannuation

9.5.1 Background to unfunded superannuation liabilities

The unfunded superannuation liabilities are the net difference between the estimated value of accrued superannuation liabilities and the value of assets set aside to meet the liabilities.

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. This 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 2011

Unfunded superannuation liabilities are estimated to decrease by $743 million to $8734 million as at 30 June 2011 compared to the value at 30 June 2010. This decrease is explained in table 9.5 and includes the effect of past service superannuation payments of $407 million, higher than expected returns on investment of $275 million and the impact of an increase in the discount rate used to measure the liability.

A discount rate of 5.6 percent (effective annual rate) was used for the 2011-12 Budget compared with 5.3 percent for the 2010-11 Budget. This marginal increase in the discount rate resulted in a $515 million decrease in the liability over the year compared to the estimate as at 30 June 2010 and highlights the sensitivity of the valuation of the superannuation liability to movements in the discount rate. Should interest rates decrease in the future, the value of the liability will increase as discussed later.

The following table sets out the major elements that comprise the movement from the estimated unfunded superannuation liabilities at 30 June 2010 to the 30 June 2011 estimated liability.

Table 9.5 – Estimated unfunded superannuation liabilities as at 30 June 2011

	$'million	$'million
Estimated unfunded liability 30 June 2010 (2010-11 Budget)		9 476
Add: adjustments	2	
Total charges		2
Actual at 30 June 2010		9 478
Add: Superannuation interest cost	427	
Past service superannuation payments	(407)	
Higher than expected returns on investments	(275)	
Movement in discount rate	(515)	
Effect of actuarial review on the SA Superannuation Scheme	46	
Increase in short-term CPI assumptions	117	
Variance between actual and expected experience	(151)	
Other movements	15	
Total charges		(743)
Estimated closing balance June 2011		8 734

Note: Totals may not add due to rounding.

9.5.2.1 *Superannuation discount rate*

As required by Australian Accounting Standards, the unfunded superannuation liability is estimated at a point in time by discounting future superannuation benefit payments by a discount rate that reflects the risk-free interest rate. The reference rate used is the longest dated Commonwealth Government nominal bond. Due to the high value of the expected payments to beneficiaries and the long term nature of the liabilities, valuation of the superannuation liability is sensitive to movements in the discount rate. The following table provides examples of the possible values by varying the discount rate from the current rate of 5.6 percent.

Table 9.6 – Sensitivity analysis of unfunded superannuation liabilities to discount rate movements as at 30 June 2011

Discount rate Percent	Unfunded superannuation liability $'billion	Increase (Decrease) $'billion
6.6	7 264	(1 500)
5.6	8 734	-
4.6	10 534	1 800

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 6.6 percent, the value of the unfunded liability will reduce by $1.5 billion. The Budget records that while financial market volatility in the recent past has resulted in multibillion dollar revisions to the value of the liability recorded on the Balance Sheet, there has been no material change in the actual expected payments to beneficiaries underlying the liability.

9.5.2.2 Superannuation funding

In 2011-12, total superannuation funding is budgeted to be $1206 million (up $20.5 million on 2010-11). It is a significant part of cash outlays. Payments comprise amounts paid from agencies as contributions to current employment for new service and contributions reflecting lack of funding for current employment in previous years ('past service' contributions) prior to the full funding policy.

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

The past service superannuation liability cash payment for 2011-12 is estimated to be $409 million.[18] This estimate is similar to that included in the 2010-11 Budget.

9.5.2.3 Earnings

Funds SA is responsible for managing the investment of superannuation assets. Investment earnings on superannuation assets are very much 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 Annual Report to Parliament.

An earnings rate of 11.5 percent was estimated for 2010-11. Previous years have benefited from higher outcomes than the assumed earnings rate.

9.5.3 Long-term funding of superannuation liabilities

The commitment to fully fund unfunded liabilities was reaffirmed by the Government in the 2011-12 Budget, with the position as at 30 June 2011 remaining consistent with the plan to eliminate unfunded superannuation liabilities by 2034.

Due to the improved investment performance in 2010-11 and the increase in the discount rate, reduced past service superannuation liability cash payments are forecast until 2034 compared to the 2010-11 Budget. Assuming no change in the discount rate and a return to long term earnings, unfunded liabilities are expected to increase, peaking around the 2011-12 period. It is estimated that benefit payments will peak in 2023-24.

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18 Budget Statement 2011-12, Budget Paper 3, Table 4.7.

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, estimated at $6.4 billion will be fully funded by equivalent assets of $6.4 billion.

9.6 Net debt

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

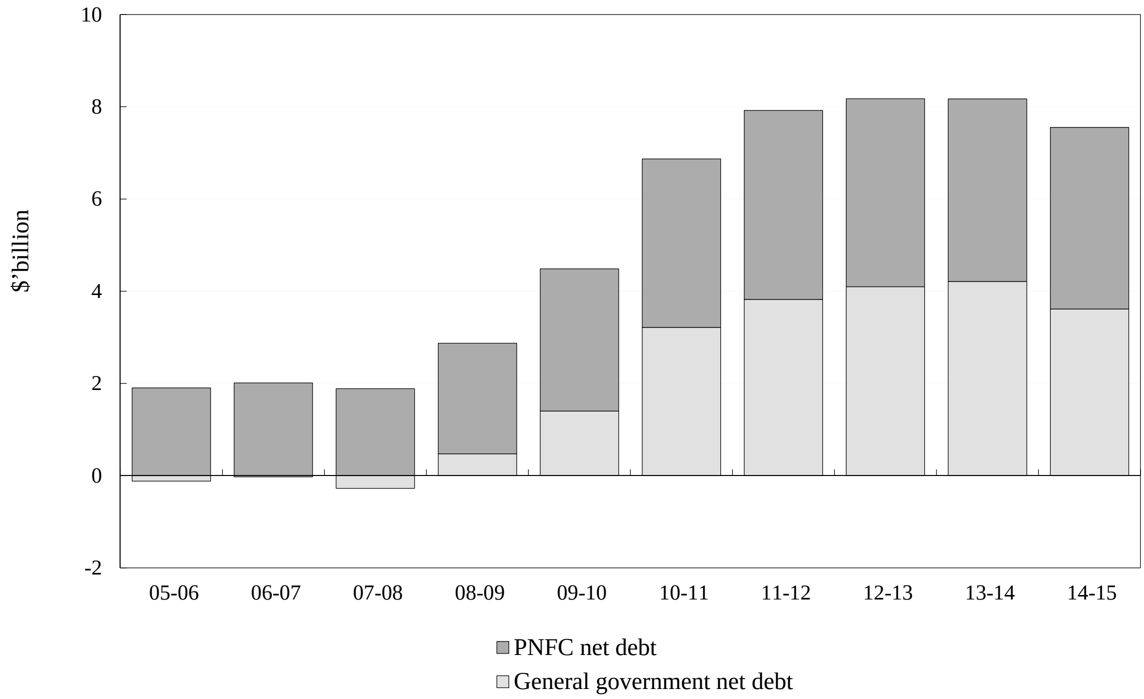
9.6.1 Definition of net debt

Net debt[19] equals certain financial liabilities (the sum of deposits held, advances received and borrowing) minus financial assets (the sum of cash and deposits, advances paid, and investments, loans and placements) as defined in the GFS framework.

9.6.2 Longer term trends in the level of debt

The following chart shows data on a long-term basis to the end of the forward estimates. Public sector net debt has increased by $2701 million to $4487 million (5.6 percent of South Australia's Gross State Product) in the period 2005-06 to 2009-10. In 2010-11 net debt has increased by $2385 million to $6872 million (8 percent of South Australia's Gross State Product). Forward estimates show that net debt is projected to rise to $7553 million in 2014-15 (7.2 percent of South Australia's Gross State Product).

Chart 9.3 – South Australian public sector net indebtedness 2005-06 to 2014-15



19 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.

General government sector is estimated to have net debt of $3217 million at the end of 2010-11. Over the forward estimates net debt increases in this sector by $398 million to $3615 million. The estimated increase in net debt primarily reflects an increase in external borrowing, resulting from net lending deficits until 2013-14.

Net debt of the public non-financial corporations increases by $283 million over the same period to $3938 million.

The chart highlights that from 2011-12, debt in the general government sector is expected to increase to levels consistent with that found in the public non-financial corporations sector. The main holder of debt in the public non-financial corporations sector is SA Water. SA Water is a commercial business servicing its debt from business revenues.

The increase in SA Water's debt is mainly attributable to water security projects including the building of the $1824 million Adelaide Desalination Plant (ADP) and the $403 million North-South Interconnection System. In 2011-12, SA Water will account for around 90.7 percent of the total PNFC sector net debt. From 2011-12, SA Water's net debt is forecast to decline across the forward estimates.

The 2011-12 Budget Papers state that Public Private Partnerships (PPPs) (capital component) arrangements for hospitals and schools are to be recognised as finance leases in the Balance Sheet and consequently have an impact on net debt and net financial liabilities. Further detail is provided in sections 8.2.9 and 9.6.3 of this Report.

Table 9.7 explains the expected movements in net debt for the general government sector at the time of the 2010-11 Budget.

Table 9.7 – Reconciliation of movements in general government net debt as at the 2010-11 Budget

	2010-11 Estimated result $'million	2011-12 Budget $'million	2012-13 Budget $'million	2013-14 Budget $'million	2014-15 Budget $'million
Opening general government net debt	**1 402**	**3 217**	**3 825**	**4 098**	**4 213**
Net lending	**-1 821**	**-1 252**	**- 489**	**- 56**	**542**
Add back:					
Accrued expenses	(3)	63	70	59	64
Assets acquired under finance leases/capitalisation of service rights	196	-	-	-	-
Less: Accrued revenue	17	(7)	2	6	(2)
General government cash surplus/deficit	**-1 645**	**-1 182**	**- 421**	**- 3**	**608**
Add: Net cash flows from equity transactions	8	579	162	(103)	1
Less:					
Assets acquisition under finance leases	178	-	-	-	-
Other adjustments	1	5	14	9	11
Improvement/deterioration to general government net debt	**-1 815**	**- 608**	**- 273**	**- 115**	**598**
Closing general government net debt	**3 217**	**3 825**	**4 098**	**4 213**	**3 615**

Note: Table may not add due to rounding

9.6.3 Debt affordability and servicing

Chart 9.3 highlights the increase in public sector net debt over the period 2010-11 to 2013-14 before declining in 2014-15. At the end of 2010-11 total public sector net debt is estimated to represent 8 percent of Gross State Product compared to 7.2 percent in 2014-15.

The reduction in net debt in 2014-15 is dependent on achieving results throughout the four years of the 2011-12 budget culminating in an operating surplus of $655 million in 2014-15 for the general government sector.

The budget records that the significant 2014-15 operating surplus provides an essential buffer for the impact of the new Royal Adelaide hospital (PPP) lease liability which will appear on the general government Balance Sheet for the first time in 2015-16. This is estimated to add $2.8 billion to net debt at that time.

9.6.4 Debt management policy

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

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

The Treasurer’s approved policy for benchmark duration applied during the 2010-11 financial year is between one to 1.5 years. Lower duration benchmarks offer lower average interest costs over the long-term but with possible higher short-term budget volatility.

During 2010-11 SAFA’s funding task, after the September budget and mid-year budget review was forecast at $5.6 billion comprising:

- $2.3 billion for the SA public sector
- $4.3 billion to refinance existing debt
- $(1.0) billion run down in excess liquidity.

During 2010-11, SAFA refinanced $2 billion of its June 2011 select lines and issued $1.35 billion of a June 2014 select line in late March 2011. SAFA’s projected funding requirement over the next few years is estimated to be lower than previous years. This reflects a projected return to operating surplus in the general government sector, the reduced funding needs of SA Water as the desalination plant construction is completed and SAFA’s refinancing profile which has no maturity until May 2013.

For further details on SAFA refer to the section ‘South Australian Government Financing Authority’ in Part B of this Annual Report to Parliament.

9.7 Other non-financial public sector liabilities

Other non-financial public sector liabilities estimated as at 30 June 2011 comprise other employee benefits ($2090 million), payables ($1220 million), other liabilities ($963 million), advances received ($591 million) and deposits ($196 million).

Other employee benefits include long service leave provisions ($1446 million estimate result for 2010-11), annual leave liabilities ($489 million estimate result for 2010-11) and salaries and wages liability ($142 million).

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

- estimated long service leave provisions amounting to $1446 million as at 30 June 2011 and budgeted to increase to $1539 million by 30 June 2012. Long service leave is calculated by an estimation process in accordance with AASBs.
- estimated workers compensation totalling $384 million are estimated as at 30 June 2011, increasing to $396 million at 30 June 2012.
- actual outstanding insurance claims payable to entities external to SAFA amount to $301 million for 2009-10 and $336 million in 2010-11. Details of SAFA's insurance operations are included in Part B of this Annual Report to Parliament.

9.8 Contingent liabilities

As reported in the Budget Papers[20] contingent liabilities are those that have not been recognised in the Balance Sheet, but rather are disclosed in notes to the accounts.

Reasons for this are:

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

Contingent liabilities of the Government can arise from:

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

[20] Budget Statement 2011-12, Budget Paper 3, pp 97-98 provides a summary of contingent liabilities.

Guarantees and contingent liabilities of the Government of South Australia as at 30 June 2010 were valued at $842 million ($717 million as at 30 June 2009). Guarantees are valued at nominal values without adjustment for the probability of actual liabilities occurring.

The $125 million increase is due mainly to an $88 million increase in the indemnified loans and liabilities of the Local Government Financing Authority (LGFA).

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 recent 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.

9.9 Natural Disaster Relief and Recovery Arrangements

The Australian Government provides funding to states and territories through the Natural Disaster Relief and Recovery Arrangements (NDRRA) to help pay for natural disaster relief and recovery costs. The amount of NDRRA reimbursement for natural disaster costs for each State or Territory is dependent on set thresholds.

These arrangements apply to the following natural disasters:

- bushfire
- earthquake
- flood
- storm
- cyclone
- storm surge
- landslide
- tsunami
- meteorite strike
- tornado.

The NDRRA do not apply to drought, frost, heatwave, epidemic or events resulting from poor environmental planning, commercial development or personal intervention.

The NDRRA are based on terms and conditions in the NDRRA Determination.

During 2010-11 the Australian Government amended these arrangements, introducing a requirement for each state and territory government to have regular, independent assessments of their insurance arrangements and provide these assessments to the Commonwealth for review. All states must have their first independent assessment completed by 30 September 2011.

The Commonwealth's review of a state's independent assessment is guided by the following principles:

1. A state has responsibility to put in place insurance arrangements which are cost effective for both the state and the Commonwealth.

2. The financial exposure borne by taxpayers (at both levels of government) should be minimised.

3. The onus is on a state to explore a range of insurance options in the marketplace and assess available options on a cost-benefit basis.

The Commonwealth may, as a result of its review, recommend changes to a state's insurance arrangements. If a state fails to take appropriate action in response to those recommendations, the Commonwealth may reduce the amount of any reimbursement available to a state in the event of a natural disaster.

SAFA have engaged a consultant to perform the first independent assessment of its insurance arrangements. A draft report is expected by mid-September 2011.

10 Comparison with other states

10.1 Some observations

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

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

Importantly before drawing conclusions, any assessment needs a sound understanding of the specific circumstances prevailing in different states. I have not sought to provide all of the relevant information in this Report. Rather I take the opportunity to show what each State is forecasting through to 2015.

The following table shows 2011-12 budgeted total revenue for each State.

Table 10.1 – 2011-12 Budgeted general government total revenue by State

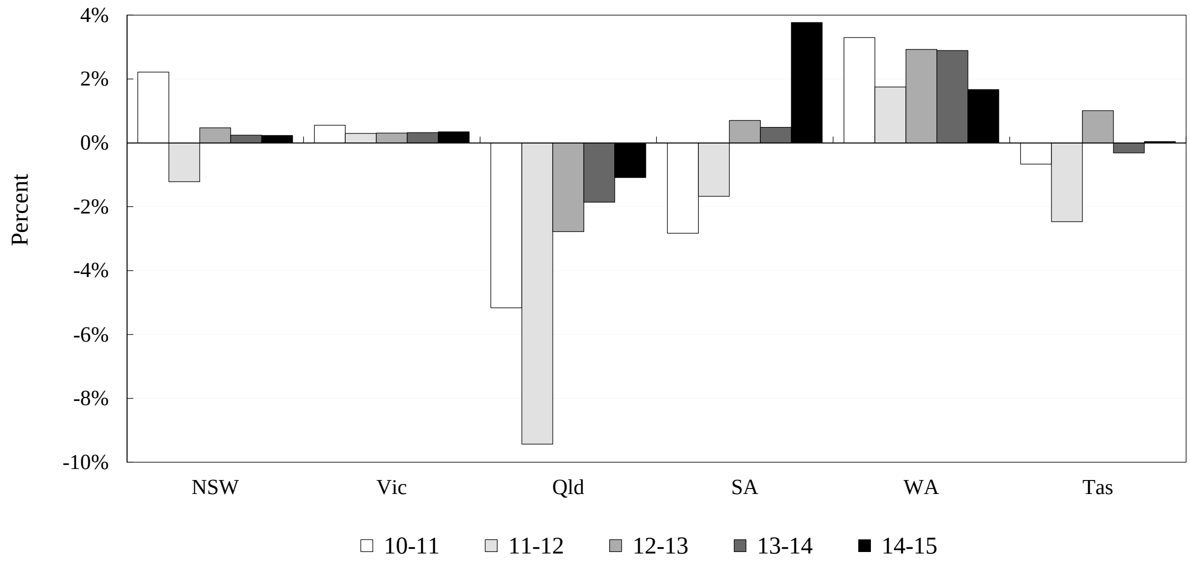
State	NSW	Vic	Qld	WA	SA	Tas
	$'million	$'million	$'million	$'million	$'million	$'million
Total revenue	59 026	47 439	43 007	25 233	15 727	4 618

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

10.2 Operating Statement

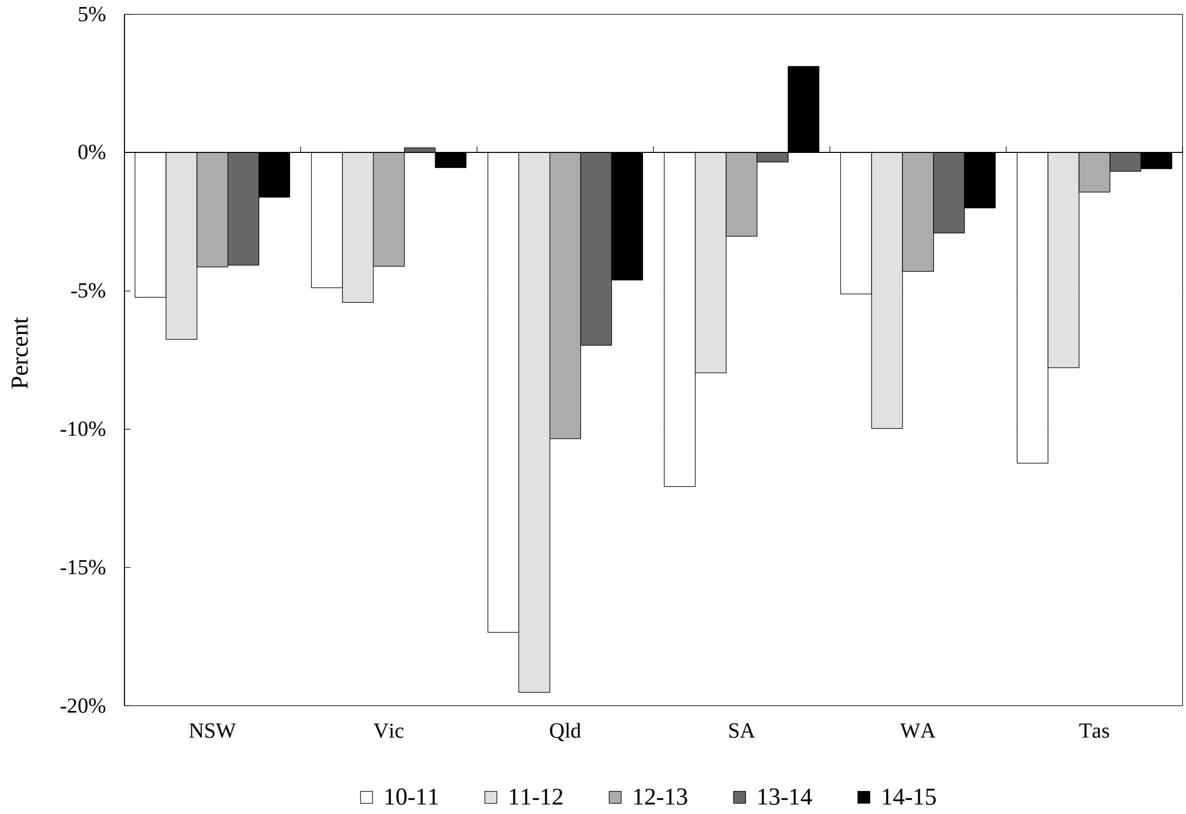
The following charts compare some trends in the GFS information with other states using 2011-12 budget data.

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



South Australia, Queensland and Tasmania each have projected negative ratios for the 2011-12 financial year. Chart 10.1 shows that South Australia, New South Wales, Queensland and Tasmania have net operating deficits budgeted for 2011-12. Across the forward estimates operating results vary widely between jurisdictions.

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



As detailed in chart 10.2, all states (except for Victoria in 2013-14 and South Australia in 2014-15) are estimating net lending deficits (borrowing) outcomes for the four years to 2014-15.

Chart 10.2 shows that South Australia's net borrowing as a proportion of total revenues is generally consistent with other states in terms of trend over the four years.

10.3 Balance Sheet

10.3.1 Ratio of net financial liabilities to revenue

The fiscal targets include a measure - the ratio of net financial liabilities to revenue. This measure is broader than net debt as it includes significant liabilities other than borrowings, such as unfunded superannuation and long service leave entitlements. This ratio is sensitive to the interest rate used to value unfunded superannuation liabilities. The rate used by each State varies.

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

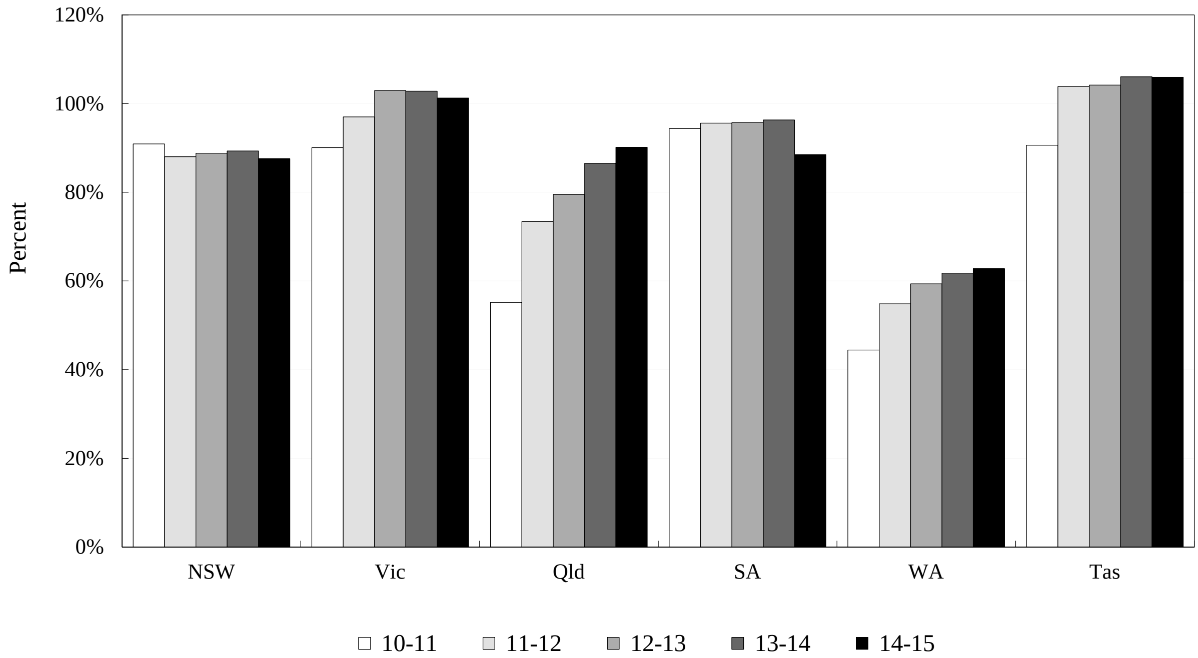


Chart 10.3 shows the 2011-12 budget settings result in the ratio for South Australia rising slightly over the next three financial years until decreasing in 2014-15. It is evident that a similar situation exists for New South Wales, Victoria and Tasmania.

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 *Public Finance and Audit Act 1987* to report on transactions and balances in the public accounts.

The main public accounts are the Consolidated Account and special deposit accounts and deposit accounts established pursuant to the *Public Finance and Audit Act 1987*.

A high proportion, but not all, of 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 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 Annual Report to Parliament.

11.2 Scope of audit of the Treasurer’s Statements

Audit reviewed the internal controls surrounding the appropriation and disbursement of monies through the public accounts. This included the:

- testing of appropriations from the Governor’s Appropriation Fund, Contingency Funds and other payments
- establishment and changes to Treasurer’s Special Deposit Accounts and Deposit Accounts
- updating and recording of the Treasurer’s loans
- maintenance of the central general ledger.

11.2.1 Audit findings and comments

The results of audit work undertaken identified a number of areas where improvements could be made. Review findings are provided under the Audit Findings and Comments heading for the Department of Treasury and Finance in Part B of this Annual Report to Parliament.

11.3 The Consolidated Account outcome

The following table sets out total appropriation authority and actual payments for the Consolidated Account in 2010-11.

Table 11.1 – 2010-11 appropriation authority and payments

	Appropriation authority $'million	Actual payments $'million
Appropriation Act 2010	12 482.3	12 288.4
Public Finance and Audit Act 1987, section 15	28.6	28.6
Governor's Appropriation Fund	347.0	3.6
Specific appropriations authorised in various Acts	110.0	110.0
Total	12 967.9	12 430.6

The result on the Consolidated Account and variations from budget for 2010-11 was as follows.

Table 11.2 – 2010-11 Consolidated Account result

	2010-11 Budget $'million	2010-11 Actual $'million	Variation $'million
Total receipts	10 961.2	10 651.1	310.1
Total payments	12 614.3	12 430.5	183.8
Consolidated Account financing requirement	(1 653.1)	(1 779.4)	126.3

The deficit of $1779 million ($1252 million deficit in 2009-10) is reflected in 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 included the return of cash to Consolidated Account – Cash Alignment Policy ($96.5 million), SA Water dividend ($64.5 million or 38.2 percent), payroll tax receipts ($12.2 million or 1.1 percent), Department for Transport, Energy and Infrastructure equity contribution repayment ($15.77 million). These were offset by lower than anticipated stamp duties ($100.5 million or 7.61 percent), Land Management Corporation dividend ($36.8 million) and gaming machines tax ($13.7 million or 4.71 percent).

- ***Payments*** – lower than budgeted expenditure noted for Defence SA ($16.4 million or 25.8 percent), Department for Transport, Energy and Infrastructure ($22.4 million or 3.6 percent) and Department of Further Education, Employment, Science and Technology ($50.8 million or 11.5 percent). These were offset by higher than anticipated expenditure amounts for the administered items for the Department of Treasury and Finance ($28.5 million or 1.7 percent) and administered items for the Department of Environment and Natural Resources ($2 million or 15.6 percent).

Consistent with the prior year, in 2010-11 significant amounts were appropriated to agencies as equity. The main items were the Department for Transport, Energy and Infrastructure ($431.4 million), Department of Health ($252.6 million) and South Australia Police ($58.5 million). Equity funding is credited directly to an agency's Statement of Financial Position, not through the Statement of Comprehensive Income. For further comment see 11.6 'Equity contributions'. 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 2010-11.

Table 11.3 – Appropriation flexibility

	Authority/ budget $'million	Actual payments $'million
Governor's Appropriation Fund	347.0	3.6
Contingency provisions in administered items for DTF	489.0	222.5
Public Finance and Audit Act 1987, section 15	28.5	28.5
Total flexibility	864.5	254.6

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

11.4.1 Governor's Appropriation Fund and contingency provisions

Section 12 of the *Public Finance and Audit Act 1987* provides for the Governor's Appropriation Fund (GAF). Generally the GAF is used to fund new Government initiatives or to meet unexpected expenditure needs.

Details of the purpose of appropriations from the GAF 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 $'000
South Australian Tourism Commission	New classic Adelaide rally	125
Department of Environment and Natural Resources administered items	To support $2 million of funding brought forward for Royal Zoological Society of South Australia	1 997
Courts Administration Authority	Required to support various funding programs and meet additional charges	358
Department of Planning and Local Government	Cost recovery for the investigation of Burnside Council	901
Joint Parliamentary Services	Transfer from the House of Assembly	180

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 of Health	110.0
Department of Education and Children’s Services	19.9
Administered items for Attorney-Generals Department	16.2
South Australia Police	13.4
Department for Transport, Energy and Infrastructure	11.7
Department for Families and Communities	10.7

11.4.3 Appropriation by the Treasurer for additional salaries, wages etc

Section 15 of the *Public Finance and Audit Act 1987* 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 2010-11 $28.5 million was appropriated by the Treasurer pursuant to section 15. This amount was added to the line ‘Administered Items for Department of Treasury and Finance’. Payments are reflected against that line. In 2009-10 the amount appropriated by the Treasurer was $70.3 million.

11.4.4 Appropriation transfers

In addition to the preceding provisions, appropriation can be transferred between agencies. Section 13 of the *Public Finance and Audit Act 1987* 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 2010-11. 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 *Public Finance and Audit Act 1987*. 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.[21]

Table 11.6 shows that over $2919 million are held in Special Deposit Accounts and Deposit Accounts as at 30 June 2011, up $152 million from the previous year.

Table 11.6 – Special Deposit Accounts and Deposit Accounts

	2009-10 $'million	2010-11 $'million	Increase/ (decrease) $'million
Special Deposit Accounts	2 151.4	2 324.6	173.2
Deposit Accounts	614.8	593.8	(21.0)
Total	2 766.2	2 918.4	152.2

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

The largest balances at 30 June 2011 were:

- ***Special Deposit Accounts*** – Accrual Appropriation Excess Funds ($479 million), Highways Fund ($314 million), Treasury and Finance Administered Items Account ($255 million) and Treasury and Finance administered Items – Intergovernmental Agreement on Federal Finance Relations ($210 million).

- ***Deposit Accounts*** – South Australian Housing Trust ($114 million), Agents Indemnity Fund ($45 million), SAFECOM Operating Account ($42 million) and Rail Transport Facilitation Fund ($41 million).

Account balances are subject to the Treasurer's Cash Alignment Policy that aims to minimise balances as discussed below.

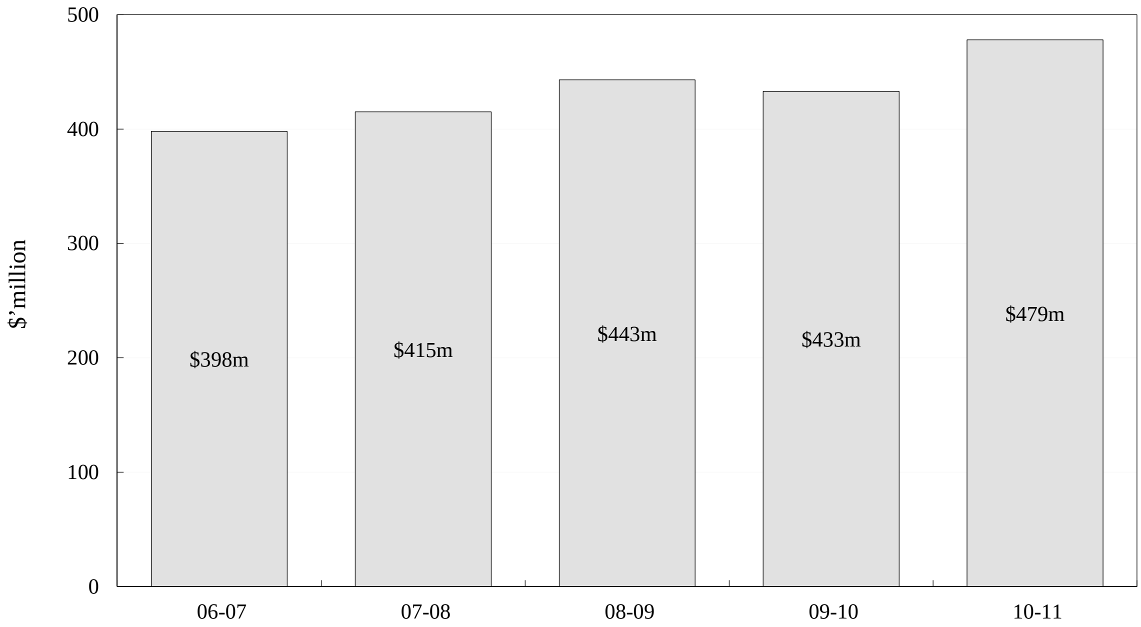
11.5.1 Accrual Appropriation Excess Funds Account

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

[21] *Public Finance and Audit Act 1987* subsection 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 DTF administered financial statements, which are included in Part B of this Annual Report to Parliament. The balance in the Account at 30 June 2011 was $210 million. This entire balance is committed to various South Australian 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 $96.6 million ($143.9 million in 2009-10) of surplus cash was returned to the Consolidated Account during 2010-11. The main amounts were as follows.

Table 11.7 – Cash alignment policy repayments

Agency	Total payments $'million
Department of Treasury and Finance Administered Items Special Deposit Account	62.7
Department of Families and Communities Administered Items	7.6
Department of Further Education, Employment, Science and Technology	11.2
Defence SA	6.0
Department of Primary Industries and Resources	4.7
Department of Trade and Economic Development	2.9
Department for Correctional Services	1.4

11.6 Equity contributions

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

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

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

Total equity contributions as at 30 June 2011 were $2851 million. Details of equity contributions provided to agencies are set out in Statement I Indebtedness of the Treasurer of the Treasurer's Statements.

During 2010-11 Audit identified misstatements in the reported balance of equity contributions in Treasurer's Statement I. The Department of Treasury and Finance has corrected these misstatements in the Treasurer's Statements for 2010-11.

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

AASB 1049 'Whole of Government and General Government Sector Financial Reporting' requires the preparation of both Whole-of-Government (WHOG) and General Government (GG) sector financial reports. Accordingly, both WHOG and GG sector financial reports form one financial report and are required to be issued at the same time as the Final Budget Outcome (FBO) by DTF.

At present there is no requirement under the *Public Finance and Audit Act 1987* or other South Australian legislation to provide an independent audit opinion on the preparation of WHOG or GG sector financial reports.

Due to the timing of the preparation of the CFR, the last completed report relates to the year ended 30 June 2010, therefore the following commentary has been kept purposely brief.

12.1 AASB 1049 key concepts

As specified, the South Australian CFR is prepared by the Government Accounting, Reporting and Procurement Branch (GARP) of 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 GG 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 Australian Bureau of Statistics (ABS) publication 'Australian System of Government Financial Statistics: Concepts, Sources and Methods' (GFS Manual).

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 GG 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 *Public Finance and Audit Act 1987* 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 report 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. As a result, sufficient work has been undertaken to be able to provide observations in respect to the financial report for each year since 1999.

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

- the principles adopted in defining of the economic entity for CFR purposes
- the adequacy and reliability of the Hyperion database as a medium for the preparation of the CFR
- processes for the preparation of the CFR
- compliance with appropriate legislation and accounting frameworks, in particular Australian Accounting Standards, 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 2009-10, a management letter was forwarded to DTF in December 2010 that contained reporting and operational considerations that would need to be addressed in order to provide an unqualified audit opinion for the CFR. This would, of course, require legislation changes requiring such an opinion to be issued. The Audit management letter was reproduced in full in the CFR report published by DTF.[22]

The matters raised included:

- completeness and accuracy of CFR items
- the use of unaudited data in the preparation of the CFR
- recognising a relevant value for land under roads controlled by the South Australian Government.

Departmental response

DTF responded to Audit's comments specifying that they would review them to determine whether they could include the required disclosures in the 2010-11 CFR.

12.4 Consolidated financial report financial performance

The following discusses the financial performance for the WHOG as detailed per the CFR as at 30 June 2010. 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.

[22] Government of South Australia, Consolidated Financial Report for the year ended 30 June 2010.

The following table summarises the WHOG financial performance per the CFR for the year ending 30 June 2010, with a comparative amount included for the prior year only. This table reflects the reporting and presentation requirements of AASB 1049.

Table 12.1 – CFR financial performance

	2010 $'million	2009 $'million
Revenue from transactions		
Taxation revenues	**3 335**	3 253
Grant revenue	**9 224**	7 503
Charges for goods and services	**4 274**	4 135
Interest income	**613**	620
Dividends and income tax equivalents	**44**	32
Other revenues	**602**	624
Total revenues from transactions	**18 092**	16 166
Expenses from transactions		
Employee expenses	**6 345**	5 869
Superannuation interest cost	**455**	383
Other superannuation expenses	**631**	608
Depreciation and amortisation	**1 009**	853
Use of goods and services	**4 112**	4 146
Interest expenses	**784**	701
Grant expenses	**2 659**	2 189
Other operating expenses	**1 409**	1 791
Total expenses from transactions	**17 404**	16 539
Net result from transactions - Net operating balance	**688**	(373)
Other economic flows - included in net result		
Net foreign exchange gains	**428**	(473)
Net gain/loss on sale of non-financial assets	**39**	36
Net gain/loss on financial assets or liabilities at fair value	**(2)**	310
Net actuarial gains (losses) of superannuation defined benefit plans	**(490)**	(2 379)
Other net actuarial gains (losses)	**(194)**	(95)
Other economic flows	**(52)**	(87)
Total economic flows included in net result	**(271)**	(2 688)
Net result	**416**	(3 061)
Other economic flows - other non-owner movements in equity		
Changes in property, plant and equipment	**11 592**	3 562
asset revaluation reserve	**12**	(12)
Net gain on financial assets at fair value	**-**	67
Total other economic flows - non-owner movements in equity	**11 605**	3 618
Comprehensive result - change in net worth	**12 021**	557
Total change in net worth	**12 021**	557

Key fiscal aggregates		
Net operating balance	**688**	(373)
Less: Net acquisition of non-financial assets	**2 584**	1 234
Net lending/borrowing	**(1 896)**	(1 607)

The main variations in revenues in 2009-10 were as follows:

- ***Grant revenue*** – increased by 22.9 percent or $1721 million. This increase was mainly driven by a $1731 million rise in Commonwealth national partnership grants. A further $241 million increase in current general purpose grants was off-set by a $397 million reduction in Commonwealth specific purpose grants.

- ***Charges for goods and services*** – increased by $139 million or 3.4 percent due mainly to increases in water related charges ($66 million), compulsory third party premiums ($41 million) and other goods charges ($91 million). Off-sets included a $115 million reduction in other service charges and slight declines in gambling and workers compensation levies.

The main variations in expenses in 2009-10 were as follows:

- ***Employee expenses*** – increased $476 million or 8.1 percent. This increase was due mainly to rising salary and wages costs of $294 million and the payment of Targeted Voluntary Separation Packages (TVSPs) in 2009-10 of $127 million.

- ***Grant expenses*** – increased $470 million or 21.5 percent. This increase was due mainly to a significant rise in recurrent grants ($162 million) and other capital transfer payments ($273 million).

- ***Other operating expenses*** – decreased $382 million or 21.3 percent. The decrease was due mainly to declines in self-insurance claims ($121 million), income/capital and redemption related workers compensation payments ($85 million) and other expenses ($170 million).

12.5 Consolidated financial report financial position

The following table summarises the WHOG financial position result per the CFR for the year ending 30 June 2010, 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

	2010 $'million	2009 $'million
Assets		
Financial assets		
Cash and deposits	**583**	576
Receivables	**862**	768
Advances paid	**1 842**	1 447
Investments, loans and placements	**9 512**	6 759
Investments - other	**12 698**	10 571
Interest in joint venture	**727**	681
Total financial assets	**26 223**	20 802
Non-financial assets		
Produced assets:		
Inventories	**429**	411
Machinery and equipment	**2 711**	2 087
Buildings and structures	**38 847**	26 166
Heritage assets	**864**	860
Biological assets	**769**	689

	2010 $'million	2009 $'million
Intangibles	**117**	102
Non-financial assets held for sale	**43**	16
Other non-financial assets	**132**	122
Non-produced assets:		
Land	**9 703**	8 975
Intangibles	**111**	51
Non-financial assets held for sale	**46**	29
Total non-financial assets	**53 772**	39 508
Total assets	**79 995**	60 310
Liabilities		
Deposits held	**275**	382
Borrowing	**12 287**	7 427
Payables	**1 313**	1 187
Employee benefits	**2 007**	1 947
Superannuation	**9 478**	8 939
Superannuation fund deposits	**12 405**	10 544
Provisions (other than employee benefits)	**5 270**	5 126
Other liabilities	**1 366**	1 186
Total liabilities	**44 401**	36 738
Net assets (liabilities)	**35 594**	23 573
Equity		
Retained earnings	**3 053**	2 577
Reserves:		
Asset revaluation reserve	**31 679**	20 221
Other reserves	**843**	769
Financial assets available for sale reserve	**18**	6
Total equity (Net worth)	**35 594**	23 573

The main variations in assets in 2009-10 were as follows:

- ***Investments, loans and placements*** – increased $2753 million or 41 percent. This increase is due mainly to a rise in marketable debt security holdings of $2725 million or 69.9 percent.

- ***Investments – other*** – increased $2127 million or 20 percent. This increase is due mainly to a rise in government equity holdings in listed and unlisted entities of $1366 million and $761 million respectively.

- ***Buildings and structures*** – increased $12 681 million or 48 percent. This increase is due mainly to increases in road network, bus and rail tracks assets of $9370 million and water, sewerage and drainage assets of $2143 million.

The main variations in liabilities in 2009-10 were as follows:

- ***Borrowing*** – increased $4860 million or 65 percent. This increase is due mainly to an increase in debt security holdings $4830 million.

- ***Superannuation fund deposit liabilities*** – increased $1861 million or 18 percent. This reflects an increase in the liability of Funds SA to all superannuation plans.