LEGISLATIVE ASSEMBLY FOR THE AUSTRALIAN CAPITAL TERRITORY

# REVIEW OF AUDITOR-GENERAL'S REPORT NUMBER 3, 1997

***1995-96 Territory Operating Loss***

STANDING COMMITTEE ON PUBLIC ACCOUNTS
Report Number 28

August 1997

## RESOLUTION OF APPOINTMENT

The Standing Committee on Public Accounts was appointed by the Legislative Assembly on 9 March 1995 with the following terms of reference:

(a) examine:

  (i) the accounts of the receipts and expenditure of the Australian Capital Territory;

  (ii) the financial affairs of authorities of the Australian Capital Territory; and

  (iii) all reports of the Auditor-General which have been laid before the Assembly;

(b) report to the Assembly, with such comments as it thinks fit, any items or matters in those accounts, statements and reports, or any circumstances connected with them, to which the Committee is of the opinion that the attention of the Assembly should be directed;

(c) inquire into any question in connection with the public accounts which is referred to it by the Assembly and to report to the Assembly on that question; and

(d) inquire into and report on the implementation of the *Public Sector Management Act 1994* with particular reference to:

  (i) the public interest; and

  (ii) any other related matter.

## MEMBERSHIP OF THE COMMITTEE

Mr Andrew Whitecross MLA (From 18 February 1997. Elected Committee Chair 19 February 1997)

Ms Louise Littlewood MLA (From 18 February 1997. Elected Deputy Committee Chair 19 February 1997)

Ms Lucy Horodny MLA

Mr Bill Wood MLA (From 26 March 1996 to 18 February 1997. Former Committee Chair)

Mr Trevor Kaine MLA (To 18 February 1997. Former Deputy Committee Chair)

Ms Rosemary Follett MLA (To 26 March 1996. Former Committee Chair)

Secretary: Bill Symington

# 1. INTRODUCTION

1.1. Auditor-General's Report No 3, 1997 was presented to the Assembly on 26 February 1997.

1.2. The audit presents the results of an analysis of the adequacy of Government income to meet the full costs of programs based upon "Whole of Government" financial statements which had been prepared to a state whereby an analysis could be made at the time of the audit.

1.3. The audit noted that completion of the "Whole of Government" financial statements by the Office of Financial Management (OFM) might produce figures different from those mentioned by the audit, but observed that the available figures were sufficiently accurate to support the audit's general conclusions.[1]

# 2. AUDIT CONCLUSIONS AND COMMITTEE APPROACH

2.1. The audit report did not contain findings, rather it addressed a range of matters and drew conclusions. The committee sought from the Chief Minister, and received, a co-ordinated response on the audit conclusions.[2]

2.2. The audit conclusions and comments provided by the Chief Minister are provided in this section under appropriate headings.

***Territory 1995-96 operating loss***

2.3. **The audit concluded that the accrual operating loss incurred by the ACT from all its operations in 1995-96 was $349m. This comprised $347m loss on General Government Sector operations and $2m from Public Trading Enterprises after adjusting for dividends and tax equivalents payable to the Government by the Public Trading Enterprises.**[3]

2.4. The Chief Minister advised that of the $344m final loss, an amount of $91m was a one-off abnormal adjustment of the accumulated liability for superannuation based on the employee profile of the ACT. That adjustment, relating to prior years, was accounted for as an abnormal expense.

2.5. The committee was further advised that the audit analysed the result by separating the General Government Sector (GGS) from the Public Trading Enterprise (PTE) Sector, and advised that the GGS comprises the activities of Government traditionally dependent on budget support, whilst PTEs include the

[1] Audit report, p2
[2] Submission to the committee from the Chief Minister dated 17 June 1997
[3] Audit report, p2

commercial trading enterprises which have the aim of recovering all, or a significant part, of production costs from individual consumers. It was pointed out that PTEs can vary in their degree of commerciality and may receive subsidies from government including for community service obligations.

2.6. The Chief Minister advised that the PTE result before dividends and tax equivalent payments to Government was given as a $35m surplus, reflecting the contribution of the businesses to the total Government position. The committee was advised that the audit did not disclose this result, but disclosed an operating loss of $2m after deducting dividends and tax equivalents, which put the sector into a poorer light than was warranted. The committee was advised that the audited position of ACTEW, for instance, showed an operating profit of $46.270m before income tax equivalents and $29.756m after income tax equivalents.[4]

2.7. The committee considers the Government has ignored the basic audit opinion that the PTE sector recorded a loss after payments to Government were taken into account, a situation exacerbated in the 1997-98 budget where the Government extracted an extraordinary dividend from ACTEW.[5]

*The operating loss in perspective*

2.8. **The audit gave a perspective of the magnitude of the overall Territory loss in 1995-96 and compared the loss with the 1996-97 loss projected in the 1996-97 budget papers. The audit noted that for 1995-96 the loss was $349m representing about $3,000 per household compared with $231m budgeted in 1996-97 at about $2,000 per household.[6]**

2.9. The Chief Minister advised that for strategic decision making purposes the most useful comparison is with the 1995-96 actual which was $253m (at about $2,200 per household) excluding abnormal items. The committee was also advised that the estimated outcome in the 1997-98 budget papers for 1996-97 was for an operating loss of $162m before abnormal items (at about $1,404 per household).[7] However, the committee notes that the budgeted operating loss for 1997-98 is estimated to rise again to $236m (at about $2040 per household).[8]

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[4] Chief Minister, op cit, p2
[5] ACT Budget Paper No 4 1997-98, p669
[6] Audit report, p3
[7] Chief Minister, op cit, p3
[8] ACT Budget Paper No 3, 1997-98, p222 (Consolidated Total Territory Operating Statement)

2.10. **The audit noted that the budget forward estimates forecast large losses continuing through to the limit of the forecasts (year 2000), that these losses will increase the amounts to be met by future generations of taxpayers, and that the size of the losses are sufficient to create the potential for the future standard of living of ACT residents to be significantly affected.**[8]

2.11. The Chief Minister advised that the forward projections in the 1997-98 budget reflect continuing high losses, albeit significantly improved over the 1995-96 position, but that there has been shown to be a quite dramatic improvement in the 1996-97 performance over what was forecast at the time of the 1996-97 budget.[9]

2.12. Nevertheless, the Chief Minister warned that the 1995-96 results should be of concern and, in this regard, the committee noted comment by the audit that the emergence of the loss has not been a product of the immediate short term but that since the introduction of self-government revenue from the Commonwealth has been progressively reduced. The audit noted that transitional Commonwealth funding to the ACT has declined from $83.3m in 1991-92 to an expected $8.6m in 1997-98, representing a reduction of $244 per capita over the period.[10]

2.13. The audit also commented that the level of adjustment which has been required by the ACT is probably beyond any that has been asked for, or achieved by, any other Australian jurisdiction.[11] In this regard, the committee noted that the ACT's administration has evolved from 14 separate Commonwealth Departments in the space of 8 to 9 years, that functions were still in the process of transfer from the Commonwealth to the ACT as late as 1991-92, and that comparisons in the audit have been made with State and Territory jurisdictions which have been operating for considerably longer periods than the ACT.[12]

2.14. The committee was advised that from 1991-92 to 1997-98 total general revenue assistance to the States and Territories increased from $13.704 billion to $16.830 billion, an increase of 22.8% or $27.98 per capita per year. Over the same period general revenue assistance for the ACT declined by $21.9m per year or $70.71 per capita per year.[13]

2.15. The committee was advised that this level of adjustment has been beyond any that has been asked for, or achieved by, any other state or Territory and that it has not been possible for the adjustment to be fully absorbed through expenditure constraint. The Chief Minister advised that reductions in Commonwealth

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[8] Audit report, p3
[9] Chief Minister, p3
[10] Audit report, p13
[11] ibid, p14
[12] ibid, p13 and Chief Minister, op cit, p4
[13] Chief Minister, op cit, p4

assistance to the ACT have also been absorbed through a combination of ACT sourced revenue initiatives, a reduction in reserves, increases in general government net debt, and increases in unfunded liabilities, mainly superannuation.[14]

2.16. The audit further noted that with the current economic difficulties which both the ACT Government and the ACT business community are encountering, the present time may not be appropriate for revenues and costs to be balanced.[15]

***Responses to the serious financial operating position***

2.17. **The audit commented that the 1996-97 Budget papers did not reveal any planned major initiatives to rein in the (operating loss) deficiency to significantly lower levels.[16]**

2.14 In response the Chief Minister acknowledged that the current budgeted operating loss, if sustained in the longer term, may inhibit the future financial well being of the Canberra community. However, the Chief Minister advised that efforts in achieving efficiencies and structural improvements were already evident.[17]

2.18. In this regard, it was pointed out that the audit report noted significant progress made with some of the initiatives currently being undertaken to redress this position, and that these included:[18]

- reductions in travel costs
- reductions in Workers' Compensation premiums
- savings in accommodation costs
- savings in the car fleet
- establishment of InTACT to deliver recurrent savings in information technology
- savings in telecommunication costs with the establishment of ACTNET
- productivity savings through the enterprise agreements
- recent success in gaining Commonwealth assistance for obtaining increases in cross-border payments for Health from NSW.

2.19. The Chief Minister advised that the level of annual savings to be achieved through these measures is estimated to be in the order of $13m although these alone would not fix the loss problem.[19] The audit, in essence, acknowledged this

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[14] ibid
[15] Audit report, p14
[16] ibid, p16
[17] Chief Minister, op cit, p5
[18] ibid and Audit report, p17
[19] Chief Minister, op cit, p5

position noting that potential cost reductions appeared insufficient to make a major impression on the operating losses.[20]

2.20. The committee was advised that strategies being developed to further assist the position include an Asset Management Strategy to co-ordinate total major asset management, extension of competitive tendering to ensure that every effort is made to realise potential for cost savings, and actively searching for opportunities to outsource economic development activities.[21]

2.21. The audit noted that the Government's strategic plan *"Canberra: A Capital Future"*, released in December 1996, although significant, could not be seen as directly producing large reductions in the operating losses, although if the expansion of the revenue base occurred as a result of implementing the strategic plan then some improvements in the loss position would be generated.[22]

2.22. The Chief Minister disagreed with the audit view advising the committee that it understated the potential of the plan. The Chief Minister put the view that it should be recognised that the plan had as a focus the promotion and encouragement of a sustainable future for the ACT by setting direction for the Government's corporate and budget planning over the next three to five years, improved capital works planning such as for schools, roads, and community centres over the next five to ten years, and major urban redevelopment planning for Canberra's growth and redevelopment for the next ten to fifteen years.[23]

2.23. The strategic plan was debated, but not adopted by, the Assembly. The committee notes that Members were concerned that the strategy did not have sufficient regard for the needs of the community over the needs of business.[24]

2.24. It was put to the committee that increases in the rate of taxation as a revenue measure would result in the ACT not being competitive against NSW and Victoria and would result in business migration from the ACT. The committee was advised that the key is to expand the revenue base by encouraging economic growth rather than to increase the rate of revenue applicable.

2.25. The Chief Minister advised that a summary of current negotiations associated with increasing private sector investment in the ACT through the ACT Business Incentive Scheme (ACTBIS) program showed that assistance had already been approved which will result in additional employment and investment in the ACT over a three year period of 700 positions and $37m, with the 1997-98 budget providing an additional $4.5m directly targeting the unemployed and generating new jobs.

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[20] Audit report, p17
[21] Chief Minister, op cit, p5
[22] Audit report, p18 and p20
[23] Chief Minister, op cit, p6
[24] Assembly Debates, 10 December 1996, p4624 etseq

2.26. In addition, the committee was advised that significant projects currently being investigated with the private sector have the potential to generate a further 2,000 positions and over $180m in new investment and that these initiatives have a significant capacity to expand the revenue base of the ACT and assist in addressing the operating result without the need to increase revenue rates. The committee was also advised that structural reforms have been implemented to improve the relative efficiency of public sector administration in the ACT through streamlining the planning and approval process and a reduction in 'red tape'.[25]

2.27. The Chief Minister proffered the view that the audit understated the magnitude of the adjustment task faced by the ACT and was silent on initiatives pursued by the Government in the context of Commonwealth/State financial relations. These included submissions to the Commonwealth Grants Commission (CGC) Review of Methodology arguing that the ACT is not being fairly compensated for cross border or national capital issues, and seeking an extension of transitional funding in recognition of the implementation of self-government and the difficult operating environment imposed on the ACT by the application of Federal industrial relations and worker's compensation legislation.[26]

2.28. The Chief Minister advised that at the 1997 Premiers' Conference, the Commonwealth agreed to provide $10m in additional transitional allowances for 1997-98 and a further $5m in 1998-99.[27]

2.29. The committee notes the importance of the Grants Commission review of methodology and other transitional factors but considers these to be marginal, with the underlying operating loss primarily a matter for the ACT Government and that additional transitional allocations must be kept in perspective.

### *Comparison with other governments, capital cities and local authorities*

2.30. **The audit compared the ACT unfavourably with the Commonwealth, NSW and WA. A comparison with other capital cities and larger NSW Local Government Councils was also unfavourable, finding that they generally operated with sound 1995-96 surpluses in contrast to the ACT's loss.**[28]

2.31. In response, the Chief Minister noted that the audit when dealing with the detailed analysis of both sets of comparisons contained some appropriate qualifications and warnings, and claimed that comparisons with either State

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[25] Chief Minister, op cit, p6
ibid
[26] ibid, p7
[27] ibid
[28] Audit report, p4

government, local government and other major cities were invalid because of the fundamentally different nature of the ACT to any of the comparison groups.

2.32. The committee notes that the 1996-97 budget papers revealed a profit on the main municipal accounts which put the ACT in the middle of the range of local authorities included in the audit comparison.[29] This suggests that the areas contributing most to the overall operating loss are State type functions.

2.33. The 1997-98 budget papers do not include municipal accounts and, as a consequence, it is not possible to compare the ACT's financial performance on municipal functions. The committee considers future budgets should present a set of municipal accounts.

2.34. The audit did acknowledge that, when considering the Commonwealth and NSW position, it needed to be recognised that their revenue raising capacities are much greater and more flexible than those of the ACT.[30] The Chief Minister reminded the committee that the larger States have significant industrial bases and populations, that the ACT has consistently maintained that the Commonwealth contribution to the additional cost burden which results from the ACT being the National Capital has been significantly inadequate, and that the recent submission to the CGC detailed where these inequities occur.[31]

2.35. The Chief Minister noted the audit comment that NSW has used asset sales in a significant manner to improve its financial results, and advised that the ACT has moved to release some of its tied resources through sale and leaseback of some properties in the same manner as other jurisdictions have done, although the scope of the opportunity in the ACT is very much more limited.[32]

2.36. The Chief Minister further noted that the audit recognised that comparisons with other capital cities cannot be made without reservations because the ACT is a city/state model providing expensive services such as health, education, police or transport which has no counterpart elsewhere in Australia.[33]

2.37. The committee considers that interstate comparisons of the kind attempted by the audit are important but given the relatively crude nature of the comparisons, caution is required in dealing with them.

***The general government sector loss dissected***

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[29] 1996-97 Budget paper No 3, p169
[30] Audit report, p11
[31] Chief Minister, op cit, p8
[32] ibid
[33] Audit report, p12

**2.38. The audit indicated that the General Government Sector (GGS) was responsible for $347m (or $256m after excluding abnormal items of $91m) of the total 1995-96 Territory operating loss. The health and education functions were identified as the major contributors to the GGS portion and, within these, employee costs account for 61 per cent and 72 per cent respectively. The audit concluded that these are the areas which need to be addressed if major savings are to be made.**[34]

2.39. The committee was advised that while the audit may have been correct in identifying the major areas where savings could be achieved, the conclusion does not necessarily follow from the analysis.[35] It was noted that the audit made reference to a number of adjustments to the audited financial statements of departments, and that in preparing the consolidated whole-of-Territory statements, the Chief Minister's Department identified some inconsistencies in accounting treatment.[36]

2.40. The committee was advised that for the consolidation purposes adjustments were made to departmental results and that, in the most extreme case, this resulted in an extraordinary expense item being moved above the line and treated as a normal expense because on a whole of government basis the transaction was not extraordinary. The committee was advised that in this context care must be taken when analysing departmental adjusted statements because of the different implications able to be drawn between the audited departmental and the adjusted results. For the purpose of analysing results at a departmental level, the committee was advised that it is more appropriate to use the audited financial statements of the departments.

2.41. The Chief Minister advised that by effectively reversing the treatment of superannuation liability the audit assumed it would have removed misleading results, but the Chief Minister claimed that the treatment used in this matter was consistent with accounting standards. The committee was advised that in identifying the major cost activities of government the audit analysis was fair but it was not useful as an efficiency indicator and was not necessarily indicative of over servicing, but simply identified the larger spending departments.[37]

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[34] ibid, pp25,27,30
[35] Chief Minister, op cit, p9
[36] Audit report, p23
[37] Chief Minister, op cit, p9

2.42. In addressing the major contributors to the GGS loss the Chief Minister advised that the value of Department of Urban Services revenues generated through land sales, licence and various statutory fees was unrelated to the efficiency of the Department or the costs of its operations. However, the Chief Minister noted that the audit largely excluded the Department from attention as a source of remedy for the GGS operating loss because of its revenues and because depreciation expenses on infrastructure assets are largely seen as fixed.[38] The Chief Minister advised that it is not correct to refer to the adjusted results as the departmental results without careful qualification as to how the information was generated and how it is being used. Thus, the difficulty with the approach used by the audit was that the adjusted results do not indicate inefficiency, which may be inferred, or community priorities.[39]

2.43. The Chief Minister advised that while health and education are major components of the total Territory cost picture, the Government maintained the view that major savings, or major improvements to revenue, are potentially available throughout the ACT public sector and that there are significant levels of expense in functions of government besides health and education where there may be opportunities for savings or efficiencies.[40]

2.44. The Committee was advised that health and education are both people-based industries and that the Department of Health and Community Care, for example, has limited opportunities to increase revenue as it cannot force people to have, or elect to use, private insurance, while the Medicare Agreement requires that public patients receive free treatment.[41]

2.45. The health, education and urban services functions contribute some 67 per cent of the overall operating loss for the Territory, and the committee was advised that the Government will include all agencies and outputs in the search for efficiencies and for redundant and non-core business to find savings and revenue options.[42]

2.46. The Chief Minister advised that the analysis available under the management reform model as proposed by the Government includes both analysis of management performance by department and broader analysis of the overall functions of government. By using the full accrual output funding model (expected

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[38] ibid, p10
[39] ibid
[40] ibid
[41] ibid
[42] ibid, p14

in the 1998-99 budget), a result other than break-even would, prima facie, reflect on management performance. Prices for outputs would be based on a full cost, market tested price level and failure to break-even would then clearly signal less efficient services.[43]

2.47. It was pointed out to the committee that the framework now in place for 1996-97 and to be continued for 1997-98 does not extend to output prices covering full costs because the Auditor General holds some concerns with the full model. The clear performance signals to be gained from variations from break-even are not available and hence results will need to be carefully interpreted until the full model is implemented.[44]

2.48. The committee was advised that the analysis intended by the Australian Accounting Standards and reflected in current ACT policy isolates Territory items (those items over which a department has little discretion) and where it is acting on behalf of the Territory. Managers are thus held accountable only for those areas where they have discretion.[45]

2.49. The Chief Minister claimed that the audit gave little attention to the private trading enterprise (PTE) sector, that in contrast to statements in the audit the PTEs were self supporting, contributing an overall profit of $37m in 1995-96, and that there may be further opportunities to improve that position significantly so that the PTEs become significant net contributors to the overall position.[46]

### *Chief Minister's Department - superannuation liability*

**2.50. The audit noted that the Chief Minister's Department with a loss of $286m included the majority of superannuation costs incurred by other agencies because these are recognised as a whole of government cost rather than costs incurred by each agency. The audit noted that while this is allowable as an alternative by the relevant Australian Accounting Standard (AAS) it has resulted in most agency losses being significantly understated and the Chief Minister's Department losses being correspondingly overstated.**[47]

2.51. The Chief Minister advised that the AAS provides for treatment under two circumstances - where superannuation is centrally managed and where it is not. Neither is mandatory because both management arrangements are used in practice and considered to be acceptable, thus the 1995-96 presentation is consistent with

[43] ibid
[44] ibid
[45] ibid, p11
[46] ibid
[47] Audit report, p24

the standard accounting for centralised management of the Territory's superannuation liability.

2.52. The Chief Minister further advised that it is also consistent with the management framework under which the ACT has operated from 1 July 1996 and will allow comparability with the 1996-97 budget and subsequent reporting.[48]

2.53. The Chief Minister noted that as from 1 July 1996 departments have been providing services for a price. That price, under the model developed by the Government, is based on full costs of providing their services, and superannuation as a cost component would be recovered along with other input costs as part of the price for outputs.

*Borrowing and leaseback arrangements as a source of funds*

**2.54. The audit noted that sale and leaseback or other financing type arrangements to meet Territory liabilities are similar in financial terms to borrowing and that in any evaluation of the ACT's current financial position they should be treated the same as borrowing. The audit noted that substantial increases in these types of arrangements would be contrary to a low debt policy.**[49]

2.55. The Chief Minister proffered the view that owning property involves substantial investment of resources at a time when the Territory is reassessing the need for such investment. Asset sales release these investment funds, remove the associated depreciation expenses and property management costs, as well as the burden of refurbishing and selling older buildings at the end of their useful lives. In the meantime the sales permit a lower level of borrowing which reduces interest costs.[50]

2.56. The Chief Minister acknowledged that leaseback commits the Territory to future rental payments, or paying rental for accommodation and other services as the services are received by the Territory. However, the Government has considered the options and has entered into these arrangements in the belief that they will deliver the better long term outcomes for the ACT.[51]

2.57. The committee concurs with the audit view that leaseback arrangements are similar (or essentially the same) in financial terms to borrowing.

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[48] Chief Minister, op cit, p12
[49] Audit report, p21
[50] Chief Minister, op cit, p11
[51] ibid

*Chief Minister's Department-as central banker*

**2.58. The audit noted that the banker responsibility of the Chief Minister's Department generated a loss of some $70m as the cash inflows from Commonwealth grants and own cash sources fell short of the operating cash outflows.**[52]

2.59. The committee was advised that the banker role financed $74m of the Territory loss through an increase in borrowings and through reducing investments, but that the audit comment was misleading. The Chief Minister advised that the banker function (the former ACT Borrowing and Investment Trust) generated a $2m profit during the year.

2.60. The Chief Minister's Department Territorial audited cash flows was given as showing a net outflow of $16m, made up of operating cash flows (net outflow $106m), investing cash flows (net inflow $ 15m) and financing cash flows (net inflow $74m).[53]

*Superannuation costs*

**2.61. The audit identified the ACT Government's unfunded liability for employee superannuation as the most significant deferred cost. This deferred cost allowed the ACT to carry a large operating loss into the future. The audit noted that the ageing profile of ACT emplyees means that many will soon reach retirement age and the deferred superannuation costs for these employees will need to be met in cash. It was estimated that payments of $175m will need to be made in the years from 2001 to 2005 after which date payments will escalate.**[54]

2.62. Unfunded superannuation liabilities over the three years 1993-94 to 1995-96 were put by the audit as having risen from about $316m representing 68 per cent of total liabilities to some $601m representing 73.3 per cent of total liabilities and for which funding would need to be obtained from future revenues.[55]

2.63. The committee was advised that the Government has adopted a policy of seeking to fully fund the annual superannuation expense and that funding of the balance of the unfunded liability will be addressed after the annual expense target is achieved. It was put to the committee that managing the rate of growth of the liability in the future could be by reducing staff or introducing new superannuation schemes for new staff. To fully fund superannuation before a balanced budget is

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[52] Audit report, p27
[53] Chief Minister, opcit, p13
[54] Audit report, pp6,7 and p31
[55] ibid

achieved would require increased borrowing, probably at a cost in excess of interest earned on investment, until the cash is needed.[56]

2.64. The committee noted modelling undertaken by the Office of Financial Management on options for meeting the unfunded liability.[57] This modelling showed that the growth in emerging costs to around the year 2030 relates to existing staff with existing superannuation entitlements particularly for those in the Commonwealth Superannuation Scheme which is now closed to new entrants.

2.65. The Chief Minister advised that the superannuation expense cannot be reasonably and equitably distributed without detailed actuarial analysis to determine to which agencies the adjustment is attributable. The committee was advised that as the non contributing agencies did not accurately reflect the increase in their liability, agencies that made contributions to the Superannuation Provision Account (SPA) did not fully extinguish their liability as the contribution rates used were lower than those the actuarial review subsequently revealed should have been paid. To redistribute to the non-contributing agencies the contributing agencies' portion of the movement in the liability would further distort the operating results of the non-contributing agencies.[58]

2.66. The committee was advised that agencies calculate the superannuation expense by applying an actuarially determined percentage to superannuable salaries and wages. That percentage is calculated as if the agency were an employer making a contribution to a fully-funded superannuation fund. In calculating the increase in total accrued liabilities for the SPA, the actuary recognises that SPA assets represent only partial funding of the liabilities, that is, the investment earnings from a fully funded situation are not available to offset the growth in annual liabilities.

2.67. The Chief Minister advised that the additional annual amount arising from the partial funding is not distributed to the expenses of agencies as it is seen as a consequence of a whole-of-government decision on funding levels rather than a matter within the control of individual agencies. Another factor is that contribution rates for agencies which make cash payments to the SPA are not reviewed annually.

2.68. The actuary's calculation of an estimated rate generally applies for three years (in the past this period has been extended) and may include a plus or minus adjustment related to actual experience over the years to which the previous rate

[56] Chief Minister, op cit, p14
[57] Select Committee on Estimates, 1997-98, trans, p 35 et seq
[58] Chief Minister, op cit, p14

applied.[59] The results of a review of rates completed during 1 996-97 are outlined in Attachment 1.

*Improvement to agencies' operating statement presentation*

**2.69. The audit report outlined an alternative accounting treatment for superannuation expenses and prepared a suggested format. The audit commented that the current presentational method for superannuation costs in agencies financial statements involves the amount of the superannuation cost brought to account as expenses being fully offset by a notional revenue item titled "Liabilities Assumed by Government". As a consequence of this treatment the superannuation cost has no effect on agencies' operating results and this could present a potentially misleading representation of the result to readers of the statements.**

**2.70. The audit then commented that a relatively minor change can be made to eliminate the existing possibility an incorrect view of agencies' operating results could be gained. The change would involve treating the "Assumption of Superannuation Liabilities" item as allocations to the agencies' accumulated funds in their operating statements rather than as a revenue item.[60]**

2.71. The Chief Minister was unable to agree with the accounting treatment and presentation suggested by the audit report, advising that the accounting policy issued by the Government in relation to this matter is consistent with Australian Accounting Standard 29 (AAS 29) "Financial Reporting by Government Departments" and noting that the Auditor-General had previously agreed with the accounting treatment employed.

2.72. The committee was advised that where the liability for superannuation is held centrally, that is through the SPA rather than by individual departments, the appropriate accounting treatment under the standards is to recognise the notional revenue item as part of the journal transferring the liability to the centre.

2.73. The Chief Minister advised that AAS 29 gives an illustration of an acceptable presentation and that it indicates that notional revenue is to be recognised as a revenue alongside other revenues. The Chief Minister advised that the ACT management framework employs an operating result approach, which is sanctioned by AAS 29, and which indicates that the assumption of liabilities

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[59] ibid, pp14,15
[60] Audit report, pp35,36

revenue should be disclosed as part of revenues from Government, and further commented that the Auditor General's preferred treatment of this item as a capital adjustment rather than a revenue is inconsistent with AAS 29.[61]

## 3. COMMITTEE COMMENT

3.1. The audit report is particularly welcome in providing an overview of the accounts of the ACT on a "Whole of Government" accrual reporting basis.

3.2. While the committee accepts that the audit analysis was based upon incomplete financial statements at the time of its preparation, it notes there was sufficient data available to enable the analysis to reach valid conclusions about the level of the ACT's financial operations and the structural factors which have contributed to the operating loss.

3.3. The audit is also welcome by most members of the committee because it has obliged the Government to provide the committee with a substantive response to matters raised by the audit and its conclusions. The submission, while basically defensive of the Government's approach to the management of the accounts of the General Government Sector, is nevertheless a detailed explanation of the Government's approach to management of the GGS debt.

3.4. There is no question that the ACT faces a considerable GGS debt burden for the foreseeable future and that the operating losses are being facilitated to a large extent by the ability to defer to the future the payments for a significant part of the costs incurred through contributions to employee superannuation.

3.5. The Government's submission to the committee indicates a disagreement with the audit in a number of key areas.

3.6. The Government took issue with the audit for commenting that the Government's strategic plan titled *"Canberra: A Capital Future"* could not directly facilitate large reductions in the operating losses. The Government asserted that the strategic plan would have brought a focus on the promotion and encouragement of a sustainable future for the ACT. The committee observes that the Assembly when it considered the plan earlier this year was not convinced that its claimed benefits would be enjoyed by the greater ACT community.

3.7. The Government was also at odds with the audit in the treatment of superannuation liability by departments and in identifying the areas where savings could be achieved. These matters are discussed earlier in this report, but the committee sees the issues as essentially differences of approach in relation to the interpretation of the relevant accounting standards.

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[61] Chief Minister op cit, p17

3.8. The committee notes that while the Government accepts that leaseback arrangements as a source of funds permits a lower of level of borrowing, it appeared reluctant to fully acknowledge the audit view that these arrangements should be treated the same as borrowing. Most members of the committee, however, reaffirm their support of the audit view on this matter.

3.9. The Territory unfunded superannuation liability is, in fact, the Government's fastest growing liability and is identified by the audit as a major concern for the ACT's economic situation. This matter was addressed by the 1996-97 Estimates Committee which recommended the Government present to the Assembly a statement on medium and long-term strategies for superannuation and an analysis of emerging costs and an analysis of accrued liability. The 1997-98 Estimates Committee recommended that the Government develop, and inform the Assembly on, the outline of an appropriate superannuation scheme for new entrants to the ACT Public Service and which includes the estimated costs per year on the basis of a desirable funding option compared to a similar funding option for the present Public Sector Superannuation Scheme.

3.10. The Estimates Committee recommendation has been agreed in principle by the Government which has advised that it will consider options for the development of an effective long term solution to superannuation financing. However, the Government has also advised that the financial impact of a new scheme would take some time to emerge although it would have a significant effect in the longer term on the employer costs to be borne by future budgets.[62]

3.11. The growth in emerging costs to around the year 2030 in relation to existing staff with existing superannuation entitlements will need to be met out of ACT revenues and, without offsetting adjustments, will lead to a significant increase in the operating loss overthe next 30 years or so. This will occur regardless of any changes to superannuation arrangements for new entrants to the ACT public service.

3.12. The committee will request the Auditor-General to undertake a similar audit on the final accounts of the 1996-97 year.

## 4. RECOMMENDATION

**4.1. The committee recommends that the Government:**

**(i) present a table of municipal accounts for the current budget year (1997-98) and that such a table be presented in all future budgets;**

**(ii) report to the Assembly on short and long-term options for addressing the emerging and accruing costs of superannuation taking account of the relevant recommendations of the 1996-97 and 1997-98 Estimates Committee reports; and**

[62] Government Response to the Select Committee on estimates 1997-98, pp4,5

**(iii) seek to reach agreement with the Auditor-General on interpretations of the accounting standards and advise the Assembly during the December 1997 sittings of the Assembly on the outcome.**

Andrew Whitecross

Andrew Whitecross MLA
Chair

ATTACHMENT 1

## PROJECTED ANNUAL SUPERANNUATION EXPENSE RATE

The following rates have been supplied by the consulting actuary for the purpose of calculating employer superannuation expense. All rates are expressed as a percentage of superannuable salary and exclude the EPSC (3%) payments made to ComSuper.

### A. - Entities which have not been allocated a specific employer contribution rate

In most cases the rates shown below will replace current rates of 20% for the CSS and 12.4% for the PSS.

| Financial Year | CSS | PSS | Total |
|---|---|---|---|
| | % | % | % |
| 1996-97 | 25.6 | 10.4 | 17.1 |
| 1997-98 | 25.0 | 10.5 | 16.7 |
| 1998-99 | 25.0 | 10.5 | 16.4 |
| 1999-00 | 25.1 | 10.5 | 16.1 |
| 2000-01 | 24.3 | 10.5 | 15.6 |
| 2001-02 | 24.3 | 10.5 | 15.3 |

### B. - Entities for which the actuary has calculated a specific rate

This rate will be used in respect of 1997-98 and the forward years.

| Agency | CSS | PSS | Total |
|---|---|---|---|
| | % | % | % |
| ACTEW | 22.1 | 11.5 | 15.8 |
| ACTION | 24.1 | 13.7 | 19.2 |

### C. - Entities for which the actuary has calculated a group rate

The listed agencies will apply the rates in the following table for 1997-98 and the forward years

| CSS | PSS | Total |
|---|---|---|
| % | % | % |
| 21.7 | 11.6 | 15.6 |

ACT Milk Authority
ACTTAB
Central Financing Unit
CIT

| | |
|---|---|
| Exhibition Park | Forestry |
| Agents Board | ACT Housing |
| AIHS | Legal Aid Commission |
| Auditor-General's Office | Construction Industry Long Service Leave Board |
| Bruce Stadium | Public Trustee |
| Canberra Theatre Trust | Registrar of Financial Institutions |
| Casino Surveillance Authority | Rental Bond Board |
| Cemeteries Trust | |
| Totalcare | |

Source: Chief Minister, submission to the committee dated 17 June 1997

## DISSENTING COMMENT

By

Mrs L Littlewood MLA

*Territory 1995-96 Operating Loss*

The committee's comment in paragraph 2.7 that the extraordinary dividend from ACTEW in the 1997-98 budget will exacerbate the PTE sector loss after payments to Government is not correct as the dividend payment will be paid after a profit or loss is declared.

*Committee Comment*

I disgaree with the thrust of paragraph 3.3, my view being that the value of the audit was enhanced by the Government providing the committee with a substantive response to matters raised by the audit and its conclusions. The submission provides a detailed explanation of the Government's approach to management of the GGS debt.

The Territory unfunded superannuation liability referred to in paragraph 3.9 is, in fact, the community's rather than the Government's fastest growing liability. In other words, the liability will be borne by the whole the community.

Louise Littlewoood MLA