

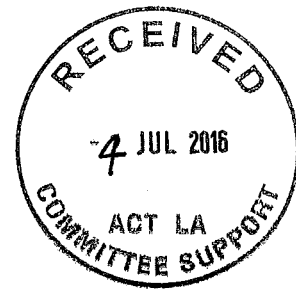


**ANDREW BARR** MLA  
CHIEF MINISTER OF THE AUSTRALIAN CAPITAL TERRITORY

Treasurer  
Minister for Economic Development  
Minister for Urban Renewal  
Minister for Tourism and Events

Member for Molonglo

Mr Brendan Smyth MLA  
Chair  
Select Committee on Estimates 2016-17  
Legislative Assembly  
London Circuit  
CANBERRA ACT 2601




Dear Mr ~~Smyth~~ <sup>Brendan</sup>

**Government Response to the Specialist Budget Advisor (Pegasus Economics) Report on the 2016-17 Budget**

The Select Committee on Estimates 2016-17 (the Committee) engaged Pegasus Economics to review and advise on the contents of the Territory's 2016-17 Budget. I would like to acknowledge the effort and time undertaken by Pegasus Economics in providing this independent assessment of the ACT Budget.

At the Select Committee's hearings on 20 June 2016, I undertook to formally respond to the matters raised by Pegasus Economics in its Report. The Government's response to that Report is attached for the Committee's information.

Yours sincerely


  
Andrew Barr MLA  
Treasurer


- 4 JUL 2016

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**Government Response**  
**to the Pegasus Economics report**  
***Review of the ACT Budget 2016-17***

***Andrew Barr MLA***  
***Treasurer***  
***July 2016***

## **Introduction**

In its *Inquiry into the Appropriation Bill 2016-2017 and the Appropriation (Office of the Legislative Assembly) Bill 2016-2017*, the Select Committee on Estimates 2016-17 (the Committee) commissioned Pegasus Economics (Pegasus) to review the 2016-17 ACT Budget, consistent with the Committee's Terms of Reference. Pegasus has subsequently produced the *Review of the ACT Budget 2016-17* (the Pegasus Report) for the Committee's consideration.

The Pegasus Report is necessarily broad reaching in scope, and provides a range of factual assessments regarding the 2016-17 Budget. As stated by Pegasus (page 2), "...the report seeks to explicate elements of the Budget and points to areas that the Committee may wish to explore or to seek further information in its consideration of the Budget." A copy of the report can be found on the Legislative Assembly website:

[http://www.parliament.act.gov.au/in-committees/select\\_committees/template5/inquiry-into-appropriation-bill-2016-2017-and-the-appropriation-office-of-the-legislative-assembly-bill-2016-2017/specialist-budget-advisor-report?inquiry=871094](http://www.parliament.act.gov.au/in-committees/select_committees/template5/inquiry-into-appropriation-bill-2016-2017-and-the-appropriation-office-of-the-legislative-assembly-bill-2016-2017/specialist-budget-advisor-report?inquiry=871094).

In its deliberations on the 2016-17 Budget, the Committee requested that the Government provide a response to the Pegasus report to assist it in understanding more fully the issues and features of the Budget.

The Government remains committed to open, transparent and accountable practices in its management of the Territory's public finances, ensuring that sustainable taxation revenues are closely aligned with service delivery levels that meet community standards. The independent review of the 2016-17 Budget undertaken by Pegasus provides a number of important observations regarding these activities. These observations are welcomed and, in turn, the Government wishes to present this response to the matters raised by Pegasus' assessment for the Committee's consideration.

## Economic Forecasts

### **1. ACT Final Demand and Wage Price Index**

(Pegasus Report, section 3.1, page 3 and section 3.6, page 6)

The Government notes the Pegasus commentary in relation to the validity of the projection of ACT final demand returning to its long-term trend rate of 4 per cent in the outyears, with Pegasus suggesting that ACT final demand projections of around 2.5 per cent would be more realistic. In addition, the Pegasus Report stated that the Wage Price Index projected growth rate of 3.5 per cent may be optimistic given the constrained public sector wage growth in the Commonwealth.

**Response:** The Government's methodology of projecting, rather than forecasting, economic parameters in the outyears is consistent with both past practice and standard forecasting methodology. Budget Paper 3, page 27 states:

*"In keeping with the projection methodology – economic parameters revert to their trend growth rates in the projection years."*

The projection of a return to trend is not unreasonable, given the observed tendency of economic parameters to return to their long-run average. It is important to note that long-run trend projections can also underestimate outcomes.

### **2. Efficiency Dividend**

(Pegasus Report, footnote, page 6)

The Government notes the Pegasus commentary in relation to the \$500 million "discrepancy" between the Commonwealth's efficiency dividend measure announced in its May Budget, and the measure referred to by the ACT Government.

**Response:** The 2016-17 Commonwealth Budget included an increase to the efficiency dividend to which the Australian Public Service is subject:

*"The Government will achieve efficiencies in the operation of the Australian Public Service by increasing the standard annual efficiency dividend by 1.5 per cent in 2017-18, 1.0 per cent in 2018-19 and 0.5 per cent in 2019-20." (Commonwealth Budget Paper 2, page 71)*

*"The new efficiency profile will generate savings of approximately \$1.924 billion above previous baseline estimates for the Budget out years." (Commonwealth Budget Paper 4, page 131)*

Within this \$1.924 billion saving, the Commonwealth Government committed to hypothecate \$500 million of these savings to 'public service improvement' programs. However, it remains unclear what form these programs will take.

## Fiscal outlook

### **3. Superannuation Return Adjustment**

(Pegasus Report, section 4.2, page 9)

The Government notes the Pegasus commentary on the Superannuation Return Adjustment, the long-term investment return objective of Consumer Price Index plus 5 per cent, and the use of this rate by the actuary in determining the appropriate employer contribution rates or in the calculation of the superannuation liability valuation estimates.

**Response:** The Government is seeking to extinguish the Territory's unfunded defined benefit superannuation liability to the Commonwealth by accumulating financial assets in the Superannuation Provision Account (SPA). These superannuation liabilities relate to current and past ACT employees who are members of Commonwealth defined benefit superannuation schemes (CSS/PSS), which are now closed to new entrants.

The investment earnings on these financial assets include interest, dividends, distributions and capital growth. Under the Government Finance Statistics reporting framework, capital growth on financial assets is not included as revenue in the Net Operating Balance. This approach understates the expected investment revenue and overstates the net superannuation expense related to the superannuation liabilities.

The superannuation return adjustment, together with interest, distribution and dividend revenues, provides for the expected overall return of the Consumer Price Index plus 5 per cent per annum, the long-term target annual return of the SPA. While investment earning outcomes are volatile from year to year, over the past twenty years the portfolio has achieved the long-term target investment return objective of the Consumer Price Index plus 5 per cent.

It is important to note that the CSS and PSS are Commonwealth superannuation schemes and the SPA financial assets are not superannuation plan assets. Additionally, the Government does not operate a superannuation fund for employees. Given this, the long-term investment return assumption on these financial assets is not related to the discount rate or employee crediting rate assumptions utilised by the actuary in determining the appropriate employer contribution rates or in the calculation of the superannuation liability valuation estimates.

The actuary applies financial and demographic assumptions relevant to the liabilities that are in accordance with the professional actuarial and Australian Accounting Standard requirements.

The actuary has utilised a reduced employee crediting rate and discount rate assumption for the 2016-17 Budget of 3.2 per cent for the calculation of the superannuation liability valuation as at 30 June 2016 and superannuation expense for the 2016-17 financial year.

#### **4. Superannuation Liability Valuation**

(Pegasus Report, section 4.2, pages 9-10)

The Government notes the Pegasus commentary on the Government's use of a discount rate other than 6 per cent to calculate the superannuation liabilities in financial statements.

**Response:** The Australian Accounting Standards require the financial year end superannuation liability valuation to reference the yield on a suitable Commonwealth Government bond (a risk free rate) as the appropriate discount rate to estimate the present value of the superannuation liabilities – this is not a fixed 6 per cent discount rate.

The 2016-17 Budget has utilised an estimate of 3.2 per cent for the 30 June 2016 superannuation liability valuation, which was referenced to the yield on the Commonwealth's 2039 bond as at 31 March 2016. The forward year estimates continue to utilise a long-term discount rate assumption of 6 per cent. While rates are low at the moment, interest rates have been much higher in the past and may be higher again in the future. As defined benefit superannuation liabilities are necessarily very long-dated, it is appropriate to use a long-term discount rate.

For example, the average 10-year Commonwealth interest rate over the last 25 years has been around 5.9 per cent. It is projected that the Territory will have these superannuation liabilities until beyond 2070 with the liabilities projected to peak in 2033 (Figure 8.2.1 on page 296 of Budget Paper 3 refers).

It is also of note that the long-term discount rate assumption of 6 per cent is also currently utilised by the Commonwealth Government in estimating its CSS/PSS defined benefit superannuation liabilities.

The long-term discount rate assumption is subject to ongoing consideration by the actuary, as are all other financial and demographic assumptions.

The financial impacts from a discount rate that is different to the long-term assumption are normally incorporated into the annual Budget Reviews.

#### **5. Treatment of the Light Rail**

(Pegasus Report, section 4.2, page 10)

The Government notes the Pegasus commentary in relation to the presentation of payments and expenses related to the Light Rail project. The Government also notes that Pegasus considers that "the Light Rail project will not have significant impacts on the Budget from 2018-19" (page 26).

**Response:** In preparing the Budget Papers, the Government has fully reflected all expenses relating to the Light Rail Network in the budget estimates. Some of the payments for the Light Rail Network project are capital in nature and are therefore included on the balance sheet and cash flow statement, and not in the operating statement.

The capital payments not included in the operating statement are as follows:

- A capital contribution of \$375 million in 2018-19.
- A component of the service payment:
  - \$0.3 million in 2018-19; and
  - \$8.8 million in 2019-20.

## **6. Return to surplus**

(Pegasus Report, section 4.4, page 11)

The Government notes the Pegasus commentary in relation to the Government achieving a planned operating surplus in the outyears.

**Response:** Budgets necessarily rely on assumptions as they are framed around circumstances existing at the time of publication, as well as predictions of future movements in a broad number of variables. The estimates in the ACT Budget cover a broad range of circumstances, including economic and fiscal assumptions, and Commonwealth grants revenue as recently published in the 2016-17 Commonwealth Budget. These assumptions as well as changed circumstances will be reviewed at future estimates updates and the estimates will be amended as necessary.

In recent years, the ACT Budget has been framed in an uncertain economic environment and it has been subject to significant financial pressures such as the global financial crisis, cuts to Commonwealth spending as well as employment, reductions in Commonwealth revenue in relation to health and GST, and the Loose-Fill Asbestos Insulation Eradication Scheme (the Asbestos Eradication Scheme). The Government chose not to cut services to the ACT community but opted to go into deficit on a temporary basis.

As there has been a succession of such events, the Government has continued to adopt that approach and it is only now – in the 2016-17 Budget – that the Government has improved its forecasts in all years since the 2015-16 Budget Review. This anticipated improvement is shown in Figure 5 of the Pegasus Report and is reflective of the recent improvement in economic activity and optimism in the ACT economy. The lack of any new economic shocks will result in a return to a balanced budget in 2017-18, ahead of the Government's previous schedule.

## **Revenue**

### **7. Vertical fiscal imbalance**

(Pegasus Report, section 5.1, page 14)

The Government notes the Pegasus commentary in relation to the extent of vertical fiscal imbalance (VFI) in the ACT Budget.

**Response:** The rationale for raising the perceived inequity with the Commonwealth Government providing 41 per cent of the ACT's revenue in 2016-17 and 32 per cent coming from ACT own source taxation receipts is to attribute a sense of lack of scrutiny and fiscal discipline in major areas of service delivery when compared to other jurisdictions.

This is incorrect for two reasons:

- 1) The VFI framework underpins the Australian federal system, and the assertion in the Pegasus Report does not consider the full context of that system.
  - a) Importantly, Pegasus fails to place VFI in the context of the offsetting application of the horizontal fiscal equalisation (HFE) principle, which partially offsets the disparity in revenue raising capacity between State-level jurisdictions.
    - i) The ACT's high share of GST is driven mainly by its relatively lower revenue raising capacity compared with other States, with GST representing a higher proportion of the ACT's total Commonwealth revenue than for four other States. This is because a significant proportion of economic activity, ie the Commonwealth Government is exempt from Territory taxation.
  - b) As reported in the Budget papers, on average, States and Territories are estimated to receive 46.2 per cent of their funding from the Commonwealth in 2016-17.
  - c) At 41 percent, the ACT is the jurisdiction which is second least reliant on Commonwealth revenue.
  - d) In per capita terms, the ACT ranks in the middle of States in its reliance on Commonwealth revenue.
- 2) The 2016-17 ACT Budget setting in relation to federal funding (in trend terms) is not out of the ordinary. It must be expected that federal-funded reform programs fluctuate, and this is illustrated throughout the Budget papers in relation to major service delivery programs such as the National Disability Insurance Scheme; Health; Education; and the time-limited National Partnership Payments.

On the issue of hard or soft budget constraints, the level of Commonwealth grants is not under State/Territory control, and the ACT necessarily relies on the Commonwealth's estimates of these payments in its own forward estimates. Marginal decisions about the level of own-source taxation are the responsibility of the Territory Government, for which it is fully accountable.

#### **8. Tax reform**

(Pegasus Report, section 5.2, page 15)

The Government notes Pegasus' commentary about the benefits of tax reform that replaces inefficient taxes with efficient taxes. The Government also notes the Pegasus commentary in relation to the inefficiency and other adverse effects of motor vehicle transfer duties (which are estimated to raise \$30.6 million in 2016-17).

**Response:** While the Government is mindful of these concerns, it is worth noting that motor vehicle transfers in 2016-17 are a minor part of revenue compared with both total revenue (0.6 per cent), and own-source taxation (1.9 per cent). Compared with the property conveyance duties, this distortion is minor. Further, as a jurisdiction with responsibility for both State-level and municipal functions, the ACT has limited options of other taxes which could be used to replace this revenue. The ACT's most efficient tax base – the broad-based taxation of land through general rates – is already increasing in order to replace revenue from conveyance and insurance duties.

The Government has a well established history of eliminating inefficient taxes and replacing them with more equitable ones, with 2012-13 seeing the introduction of the Government's 20-year program of reform for the Territory's taxation system.

Future reforms will cut unfair and inefficient transaction taxes, and result in significant economic gains in the wider economy through increased productivity. While the Government's tax reforms will make the ACT tax system fairer and more sustainable, the Government also recognises the need to provide support to families and individuals who need a helping hand – the Government will continue to provide concessions to households most in need of support.

Additional details regarding the Government's plan to increase the efficiency of the Territory's taxation base can be found in the Taxation Reform budget booklet (released in conjunction with the 2016-17 Budget) at:  
[http://apps.treasury.act.gov.au/data/assets/pdf\\_file/0010/870292/Taxation-Reform.pdf](http://apps.treasury.act.gov.au/data/assets/pdf_file/0010/870292/Taxation-Reform.pdf)

## **9. Raising the threshold for payroll tax**

(Pegasus Report, section 5.3, page 17)

The Government notes the Pegasus commentary in relation to the impact of the increase of the payroll tax free threshold on the Government's tax base.

**Response:** In relation to the Government's decision to increase the payroll tax threshold (and, in Pegasus' opinion, eroding one of the Territory's taxation bases in so doing), the rationale behind this decision is straightforward; as required and, as historically demonstrated, the Government will act as necessary to support businesses in the ACT. The combined effect of the increases in the threshold since 2012-13 result in savings for local businesses of up to \$34,250 per year, and, as noted in the 2016-17 Budget Papers, the increase in the threshold will result in approximately 40 businesses in the ACT becoming exempt from payroll tax in 2016-17.

It is worth noting also that although payroll taxes are relatively less inefficient than the alternatives, including transaction taxes such as property conveyances, they are not as efficient as taxation levied through general rates.

## **10. Safer Families Initiative – Hypothecated taxes**

(Pegasus Report, section 5.4, page 17)

The Government notes the Report's commentary in relation to the hypothecation of taxes, with particular reference to the Safer Families Levy.

**Response:** The Safer Families Levy will be applied to all residential and rural properties as a whole-of-community response to domestic and family violence. The application of the Levy aligns with that employed for other levies (such as the Fire and Emergency Services Levy) where annual rates are determined via a disallowable instrument and updated if and when required. Accordingly, the Levy represents a legislated and sustainable revenue source that will bind future governments to fund family violence prevention programs over the long term.

## **11. Dividends**

(Pegasus Report, section 5.5, page 18)

The Government notes the Pegasus commentary in relation to the timing and levels of Public Trading Enterprise (PTE) dividends.

### **Response:**

#### *Icon Water*

In the budget and forward years, Icon Water Limited's (Icon's) dividend payment is set as 100 per cent of net profit excluding gifted assets. The main reason for the movement in the dividend payment in 2016-17 is disclosed in Budget Paper 3 (page 245) as a reduced distribution from the ActewAGL joint venture. Further information on reasons for changes in Icon's operating profit can be obtained from the variance explanations in the notes to its budget statements (namely Budget Statement B, page 228:

[http://apps.treasury.act.gov.au/data/assets/pdf\\_file/0010/869977/B-CMTEDD-Budget-Statements.pdf](http://apps.treasury.act.gov.au/data/assets/pdf_file/0010/869977/B-CMTEDD-Budget-Statements.pdf)).

There are two main drivers of the increases in revenue in 2018-19 and 2019-20. Icon has forecast an increase in water revenue in 2018-19, in anticipation of the next price determination, which includes an allowance for recovery of 3 gegalitres (not recovered during the current pricing period). Icon has also allowed for an expected increase in energy revenues in 2019-20 for the next regulatory price period.

The level of estimated dividends is agreed each year between the Board and the Voting Shareholders as part of the Statement of Corporate Intent (SCI) consultation process. This is negotiated based on the business plans and financial forecasts reflected in the SCI, including Icon's debt servicing capacity.

The dividend policy for Icon maintains its gearing ratio at sustainable levels, increasing marginally from 55 per cent in the 2016-17 Budget to 57 per cent by 2019-20. The Voting Shareholders have the discretion to reconsider the 100 per cent dividend payout ratio to maintain a sustainable capital structure, for working capital requirements, or to provide funding for capital expenditure or contingency purposes.

#### *Land Development Agency*

The Pegasus Report is correct in noting that the increase in dividends from the Land Development Agency is primarily driven by increased sales activity.

## *Other*

In response to commentary on page 19 of the Pegasus Report, the Government confirms that dividends and other capital returns from PTEs are driven by the capital and investment requirements of the business, not by short-term budgetary considerations.

## **Expenditure**

### **12. Health**

(Pegasus Report, section 6.3, page 21)

The Government notes the Pegasus commentary in relation to health funding, including statements regarding efficiency, staffing and outputs.

#### **Response:**

The Government has provided \$6.4 billion over the next four years to ACT Health, comprising the Health Directorate and the Local Hospital Network. This amount includes the Health Central Provision (a total of \$0.186 billion over four years), which will be used to fund future expense initiatives to be determined by the Government.

In terms of efficiency, there are valid reasons why ACT Health services cost more, on average, than other jurisdictions. ACT Health provides some low-volume, high-cost services (such as open heart surgery, bone marrow transplantation and intensive care for babies) but the ACT does not have the economies of scale to manage these services in a manner as efficient as in larger jurisdictions. Moreover, the ACT retains a legacy superannuation cost from Commonwealth defined benefit schemes.

Notwithstanding this, the Government notes that there is scope to improve the level of efficiency of our services while improving patient outcomes. The Government is investing in a range of activities through the ACT Health System Innovation Program to reduce costs relative to the national average, and reduce growth in health costs.

Additionally, the decision to reinvest efficiencies within the health system provides the opportunity to establish new ways of providing services as well as introducing new technology.

In relation to staffing levels, ACT Health has historically invested in growing its workforce to meet the needs of the community. The Government is not seeking to reduce staff numbers but to redirect resources as efficiencies are made and innovative systems and processes are introduced to maximise the health outcomes of our community.

In terms of outputs, ACT Health is introducing activity-based funding processes to demonstrate the average cost of services (outputs) in a more transparent manner. This will provide clearer identification of cost drivers as well as highlighting variations between the ACT and other service jurisdictions.

This process will assist in improving the efficiency of the health system and provide for reinvestment in services that will also improve health outcomes.

The outcomes of this process will also identify the relative benefits of providing services in different environments and in a more integrated manner to both support people in managing health conditions, while also supporting the entire community by maximising the efficiency of services.

Canberra's public hospitals service more than just the local population. They provide emergency, specialist, trauma and acute care to people beyond the ACT borders, especially the surrounding regions of NSW. A wide range of services are delivered locally, including acute inpatient and day services, outpatient services, women's and children's services, paediatrics and pathology services.

The ACT is a small jurisdiction and attracts a mobile workforce as well as many visitors who contribute to economic activity through ties with political and diplomatic services, through engagement in high quality education and research, and through our own tourist and nearby tourist destinations. While not achieving the economies of scale in delivering health services for larger jurisdictions, the ACT Government has been committed to developing and providing services that caters to community needs and development, and that offer appropriate treatment when it is most needed.

### **13. Asbestos Eradication Scheme**

(Pegasus Report, section 6.5, page 27)

The Government notes the Pegasus commentary in relation to the payments towards the Loose-fill Asbestos Insulation Eradication Scheme (the Asbestos Eradication Scheme).

**Response:** The 2016-17 Budget estimated the cash payments for the Asbestos Eradication Scheme at \$929 million, \$39 million lower than the 2015-16 Budget estimate of \$968 million. This is predominantly due to decreases of \$40.5 million in expected house and land purchase costs, and \$3.6 million in demolition and remediation costs (partially offset by higher Asbestos Taskforce costs of \$5 million).

The 2016-17 Budget estimates assume that 50 properties will opt out of the Scheme (as at 20 May 2016, owners of 23 properties had decided not to participate). At the time of the 2015-16 Budget, it was assumed that all affected properties would participate.

### **14. Capital Works Program**

(Pegasus Report, section 6.6, page 28)

The Pegasus Report notes a "...dramatic decline" in the forward estimates for the Territory's capital works expenditure in 2019-20.

**Response:** The reduction in capital expenditure in 2019-20 reflects the completion of a number of significant projects, including Light Rail – Stage 1 and the ACT Law Courts Facilities. Investment in 2019-20 will be subject to future decisions by the Government, and these impacts will be reflected in subsequent budgets.

## 15. Savings and offsets

(Pegasus Report, section 6.7, page 29)

The Government notes the Pegasus commentary in relation to the offsets included in the Budget Papers.

**Response:** Additional details regarding the nature of the offsets included in the 2016-17 Budget Papers are provided at [Attachment A](#).

## Assets and Liabilities

### 16. Overview

(Pegasus Report, section 7.1, page 32)

The Government notes the Pegasus commentary that the Territory's balance sheet is healthy, with a positive net worth rising from \$17.1 billion to \$17.7 billion over the budget and forward estimates. It also notes that net debt and net financial liabilities are also forecast to rise over that period.

**Response:** A number of factors in recent years have impacted on net debt and net worth in different ways. One example relates to the Asbestos Eradication Scheme – in particular, while the full cost of borrowing for the Asbestos Eradication Scheme is included in net debt and net worth, the value of the assets purchased (ie contaminated properties) is less than the purchase cost, reducing net worth.

### 17. Net Financial Liabilities

(Pegasus Report, section 7.2, page 33)

The Government notes the Pegasus commentary in relation to the possibility of future revaluations of the superannuation liability in the outyears.

**Response:** The Government periodically reviews the suitability of all discount rates and ensures that all estimates and projections reflect the relevant economic circumstances. Accordingly, if the current low interest rate environment continues, similar future financial adjustments may be required. It should be noted that the financial impact adjustment is normally reflected in the annual Budget Review.

### 18. Superannuation

(Pegasus Report, section 7.4, page 34)

The Government notes the Pegasus commentary in relation to the sensitivity of the unfunded superannuation liability estimate compared to the rate used to measure the present value of superannuation payment in the outyears.

**Response:** The discount rate assumption does impact on the present value estimate of the superannuation liabilities, or what the Government estimates the future benefit payments to be worth today – so using a lower discount rate results in an increase in the estimated value of the future liability in current dollar terms, all else being equal. However, lower discount rates would tend to be associated with lower rates of salary growth and rate of inflation which would tend to lower the superannuation liability.

## Fiscal sustainability

### **19. Other indicators**

(Pegasus Report, section 8.3, page 37)

The Government notes the Pegasus commentary in relation to the inclusion of alternative indicators of fiscal sustainability to those contained in the Budget Papers.

**Response:** The Government monitors the relationship between the costs of borrowings and revenue and total financial assets on an ongoing basis as they are utilised by Standard & Poor's (S&P) when assessing the ACT's credit rating and credit worthiness. The ACT's S&P credit rating is currently AAA Stable, which is S&P's highest credit rating.

## Risks

### **20. Overview**

(Pegasus Report, section 9.1, page 39)

The Government notes the Pegasus commentary in relation to the Government's ability to return to surplus in the event that unexpected adverse events occur.

**Response:** The Government's fiscal strategy commits to achieving an operating balance over time. There have been a number of shocks to the ACT in the past few years – the global financial crisis, cuts to both Commonwealth spending and jobs, reductions in Commonwealth grants in relation to health and GST, and the Asbestos Eradication Scheme. The Government has taken the approach that it would not cut services to the ACT but would temporarily go into deficit to support the ACT economy. The Government was able to take such action as a result of its strong balance sheet and its AAA credit rating, and the 2016-17 Budget forecasts demonstrate that this approach has been successful.

The risk of incurring deficits does limit the Government's capacity to deal with unanticipated adverse external shocks somewhat. However, this does not mean that the Government cannot respond in the event of an external shock.

As the Government: (a) has supported the ACT economy, notwithstanding a number of large financial impacts and is now forecasting a return to a balanced budget earlier than was anticipated; and (b) has retained its AAA credit rating, this is testament to the effectiveness of this strategy. Should there be further external shocks, the Government considers that it is well placed to respond, based on its track record and the continued strength of its balance sheet.

### **21. Fiscal Risks**

(Pegasus Report, section 9.3, page 40)

The Government notes the Pegasus commentary in relation to the risk that accrued liability for defined benefit superannuation schemes pose to the Territory's fiscal position.

**Response:** The ongoing risks associated with the superannuation liability estimates are acknowledged in the Budget Papers. As these liabilities will not be extinguished until well into the future, long-term actuarial assumptions must be made. These assumptions are reviewed on an ongoing basis by the actuary and adjusted when required.

## **22. Program and Other Risks – Asbestos Eradication Scheme**

(Pegasus Report, section 9.4, page 40)

The Government notes the Pegasus commentary in relation to the risk that the sales phase of the Asbestos Eradication Scheme poses to the Territory achieving the estimates presented in the 2016-17 Budget Papers.

**Response:** At the commencement of the Asbestos Eradication Scheme, the Government necessarily had to make a number of assumptions about the variables affecting the Scheme and reflect these in the relevant budget estimates. For example, the estimate in the 2015-16 Budget was an average purchase price for houses of \$717,000 per house. The outcome achieved to date has been an average of \$722,000.

The estimate in the 2015-16 Budget was an average sale price of remediated blocks of \$601,000 per remediated block. This has not been adjusted in the 2016-17 Budget. This estimate is based on an overall uplift 38 per cent.

As at 20 May 2016, seven properties had sold under the hammer and two were sold shortly after auction. Sales prices were close to the estimate included in the 2015-16 Budget Review.

The average uplift above the unimproved value for these nine blocks was 38 per cent, consistent with the revised target.

## **23. Program and Other Risks – Workers' Compensation Scheme**

(Pegasus Report, section 9.4, page 41)

The Government notes the Pegasus commentary in relation to the increased cost of the workers' compensation scheme insurance premiums for a number of agencies.

**Response:** The Government has applied a \$7.5 million offset to reduce the overall cost of supplementation provided in 2016-17 to agencies in response to higher than anticipated insurance premiums. The offset arose from successful appeals against Comcare premium pricing, and the resulting refund of past year premium payments.

## 24. Savings Offsets

(Pegasus Report, section 9.4, page 41)

The Government notes the Pegasus commentary in relation to the offsets identified in the Budget Papers and provides further information in Table A.1 (expense initiatives) and Table A.2 (capital initiatives).

**Response:** The following tables detail the nature of the expense and capital offsets included in the calculation of the Budget estimates.

**Table A.1 – Offsets/savings associated with Expense initiatives**

Agency	Initiative Title	2016-17 Budget \$'000	2017-18 Estimate \$'000	2018-19 Estimate \$'000	2019-20 Estimate \$'000	Total \$'000	Nature of Offset
ACTPCA	Better Services – Extension to Woden Cemetery – Stage 1 <sup>1,2</sup>	0	31	46	49	126	This project will be funded from the ACT Public Cemeteries Authority's existing resources.
CMTEDD	Digital Canberra – Support for the Chief Digital Officer to improve government services	500	0	0	0	500	This initiative will be partially offset over time by savings achieved through the implementation of more efficient ICT systems across government.
CMTEDD	Healthy Weight Initiative – Healthy Canberra	200	110	110	110	530	This initiative will be partially offset by Health as a result of the cessation of funding provided for the <i>Active Kids Challenge</i> program.
CMTEDD	Sport and Recreation – Asset Repair and Maintenance Scheme – Year four	904	0	0	0	904	This initiative will be partially offset by surplus funds remaining from the 2015 Asian Cup matches hosted by the ACT.
CMTEDD	Supporting Aboriginal and Torres Strait Islander Peoples – Indigenous Enterprise Development	100	100	0	0	200	This initiative will be met from within the Chief Minister, Treasury and Economic Development Directorate's existing resources.
CMTEDD	Supporting Affordable Housing – Homes for Homes <sup>3</sup>	50	50	0	0	100	This initiative will be met from within the Chief Minister, Treasury and Economic Development Directorate's existing resources.
CMTEDD	Workers' Compensation – Supplementing agency costs	7,487	0	0	0	7,487	This initiative will be partially offset as a result of successful appeals against Comcare premium pricing as well as refunds from past year premium payments.
Education	Better Schools – Enhancing quality assurance of schools	300	300	300	300	1,200	This initiative will be funded from within the Education Directorate's existing resources.

Agency	Initiative Title	2016-17 Budget \$'000	2017-18 Estimate \$'000	2018-19 Estimate \$'000	2019-20 Estimate \$'000	Total \$'000	Nature of Offset
Education	Better Schools – Improving teacher quality – Scholarships for teachers	100	100	100	0	300	This initiative will be funded from within the Education Directorate's existing resources.
Education	Better Schools – Schools for All	4,350	2,443	1,738	754	9,285	This initiative will be partially funded from within the Education Directorate's existing resources.
Education	Better Schools – Strengthening and promoting Ngunnawal culture and history	150	150	0	0	300	This initiative will be funded from within the Education Directorate's existing resources.
Education	Safer Families – Trauma Understanding and Sensitive Teaching (TRUST) Project	60	60	0	0	120	This initiative will be funded from within the Education Directorate's existing resources.
EPD	Leading Australia in responding to climate change – Reducing energy use in ACT Government buildings	350	350	350	350	1,400	This initiative will be funded from contributions from affected ACT Government agencies.
JACSD	ACT Corrective Services – Information management <sup>1</sup>	1,055	479	23	23	1,580	The offset arises from savings in a related tender process.
JACSD	Reforming Emergency Services – Aero-medical services and hangar upgrade	25	103	105	108	341	Investment in this initiative will increase the amenity of the hangar and, in turn, there will be an increase in rent collected by the Government.
JACSD	Reforming Emergency Services – Improving emergency responses – Website and emergency warning system upgrades	79	81	83	85	328	This initiative will be partially offset through savings gained from retiring the current system arrangements.
TCCSD	Better Public Transport – Trial of electric buses <sup>1</sup>	300	0	0	0	300	This project will be partially funded from within Transport Canberra and City Services Directorate's existing resources.
TCCSD	Better Public Transport for Woden and Weston Creek – New Woden bus depot <sup>1</sup>	0	0	0	2,700	2,700	The MRCagney review of ACTION forecast savings of \$2.7 million per year by improving the efficiency of the bus network and reducing dead running.
TCCSD	Better Services – Improved asset management <sup>1</sup>	0	0	300	550	850	This initiative will be offset through repairs and maintenance savings resulting from improved business processes that will result from the new system being implemented.
TCCSD	Better Services – Improving libraries – Self-service check out and improved access <sup>1</sup>	0	0	143	318	461	The offset against this initiative arises from efficiencies gained through the new system, reducing resources currently required by Libraries ACT.

Agency	Initiative Title	2016-17 Budget \$'000	2017-18 Estimate \$'000	2018-19 Estimate \$'000	2019-20 Estimate \$'000	Total \$'000	Nature of Offset
TCCSD	Improving Our City – Gateway to Canberra – Landscaping of Pialligo Avenue	310	0	0	0	310	This project will be funded from within the Transport Canberra and City Services Directorate's existing resources.
<b>TOTAL EXPENSE OFFSETS</b>		<b>16,320</b>	<b>4,357</b>	<b>3,298</b>	<b>5,347</b>	<b>29,322</b>	

**Notes:**

1. This is a capital initiative with an associated expense offset/saving.
2. This initiative also includes an associated capital offset, see Table A.2.
3. This initiative will be delivered by Housing ACT and fully offset by the Chief Minister, Treasury and Economic Development Directorate.

**Table A.2 – Offsets/savings associated with Capital initiatives**

Agency	Initiative Title	2016-17	2017-18	2018-19	2019-20	Total	Nature of Offset
		Budget	Estimate	Estimate	Estimate		
		\$'000	\$'000	\$'000	\$'000		
ACTPCA	Better Services – Extension to Woden Cemetery – Stage 1 <sup>1</sup>	392	166	0	0	558	This initiative will be funded from within the ACT Public Cemeteries Authority's existing resources.
Education	Better Schools – ACT Board of Secondary Studies database upgrade	176	0	0	0	176	This initiative will be partially funded from within the Education Directorate's existing resources.
Education	Better Schools – Investment in Gungahlin school infrastructure	4,340	0	0	0	4,340	This initiative will be partially offset by savings realised through the efficient management of the Charles Weston School project.
Education	Better Schools – IT upgrade for school administration	3,812	3,791	2,397	0	10,000	This upgrade will be funded from within the Education Directorate's existing resources.
EPD	Caring for our Environment – Water Quality Improvement – Contributions to the Basin Priority Project	27,000	30,000	17,671	0	74,671	The capital offset against this initiative is associated with the unwinding of a capital provision established in the 2015-16 Budget to undertake this work.
<b>TOTAL CAPITAL OFFSETS</b>		<b>35,720</b>	<b>33,957</b>	<b>20,068</b>	<b>0</b>	<b>89,745</b>	

**Note:**

1. This initiative also includes an associated expense offset – see Table A.1.