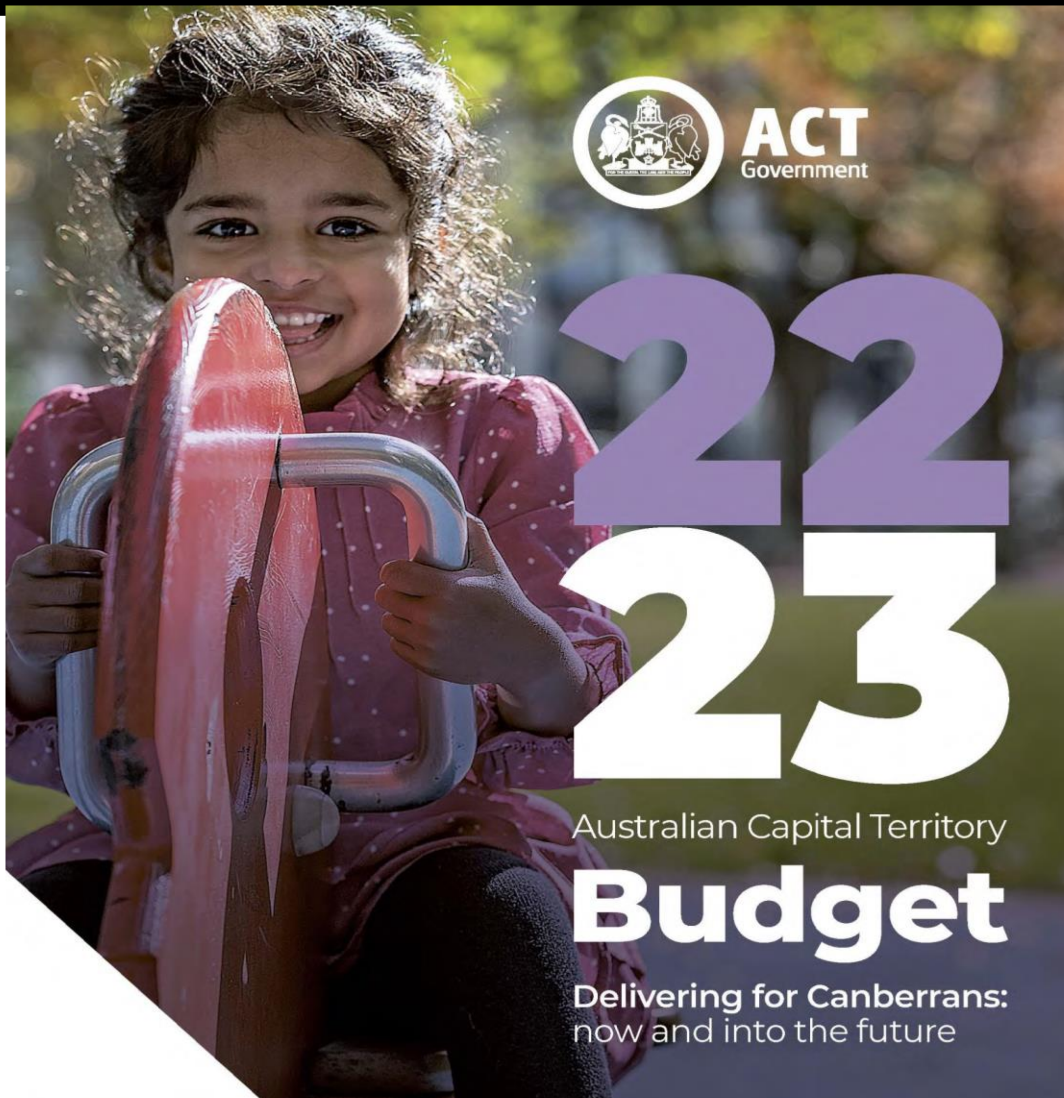
2022

Review of the ACT Budget 2022-23



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Pegasus Economics is a boutique economics and public policy consultancy firm that specialises in strategy and policy advice, economic analysis, trade practices, competition policy, regulatory instruments, accounting, financial management and organisation development.

This report has been commissioned by the ACT Legislative Assembly's Select Committee on Estimates 2022-2023 to assist the Committee in its deliberations in relation to the 2022-23 ACT Budget.

The views and opinions expressed in this report are those of the authors.

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Photograph on the front cover is taken from the front cover of *Australian Capital Territory Budget 2022-23: – Budget Outlook* from the 2022-23 ACT Budget.

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Executive Summary

Overview

This report has been prepared by Pegasus Economics to assist the ACT Legislative Assembly's Select Committee on Estimates 2022-2023 in its consideration and review of the 2022-23 ACT Budget. The draft report was required to be produced within a week of the presentation of the Budget to the Legislative Assembly. It is based on a desk-top review of the available documentation.

The 2022-23 Budget has an investment focus. Additional capital spending on infrastructure across the Budget and forward years will be largely financed through increased borrowings.

Most of the ACT Budget economic forecasts for 2022-23 appear reasonable, with exceptions in relation to the consumer price index (CPI) and population growth.

If the Reserve Bank's and Commonwealth Government's most recent forecast for the CPI in 2022-23 are in the ballpark then it is highly likely the ACT Government forecast for the Canberra CPI in 2022-23 is too low.

The ACT Government is forecasting and projecting accelerating population growth. However, the outlook for population growth presented by the ACT Government is quite optimistic compared to forecasts prepared by the Centre for Population that suggest slightly more modest population growth for the ACT.

The aggregate Budget forecasts are more favourable than in either of the past two years, which were adversely impacted by the effects of COVID-19.

The stronger than anticipated economic recovery in 2021-22 has flowed through into higher-than-expected revenue arising from own-source revenue and grants from the Commonwealth (ACT Government, 2022a, p. 223). Revenue is now expected to be $537 million higher in 2022-23 than previously forecast at the time of the 2021-22 Budget.

Under stage 3 of tax reform it appears that the reduction in revenue from commercial and residential conveyances will far exceed the increase in general rates as an overall percentage of ACT Government own-source taxation revenue.

Based on the forward revenue estimates in the 2022-23 ACT Budget, the expected increases in general rates by 2025-26 will only make up less than one third of the shortfall in revenue from reductions in commercial and residential conveyance revenue, in turn suggesting the ACT Government is not seeking to replace revenue lost from phasing out reductions in commercial and residential conveyances entirely from increases in general rates.

Growth in expenses across the Budget and forward years is modest by historical standards and is lower than expected inflation and population growth.

The Budget includes a substantial major projects, infrastructure and capital works program across the Budget and forward years. The ACT Government will invest $1.4 billion in infrastructure and capital in the ACT in 2022-23 and approximately $7 billion over the next five years. $1.8 billion of the proposed program over the five years is in provisions, with detailed estimates not for publication.

The key projects for 2022-23 include investments in health, new schools in Gungahlin and Molonglo, the big battery, road and bridge works in Molonglo, a new CIT campus and Transport Interchange for Woden, new public housing and public housing renewal and Light Rail expansion.

The ACT has a strong balance sheet and key balance sheet measures are within the range reported by other States and Territories, but all of the Territory's key balance sheet measures are expected to deteriorate over the Budget and forward estimates period.

Unfunded superannuation liabilities are by far the largest financial liability on the Territory's balance sheet. Successive ACT Governments have maintained a commitment to the target of achieving full coverage of the Territory's unfunded defined benefit superannuation liabilities by 2030. On current forecasts, the prospect of extinguishing the unfunded liability by 2030 appears remote.

While the ACT Government will have no difficulty in meeting its immediate obligations over the Budget and forward estimates, the current fiscal trajectory is not sustainable over the long-term.

Affordable Housing

Many people in the ACT are experiencing difficulties in accessing housing in the ACT. Budget settings have contributed to this problem.

Distortions in the income tax system have contributed to increased prices for houses and units across most of Australia. There is also evidence to suggest that demand for land in the ACT vastly exceeds supply, adding to the pressure on prices arising from the income tax system.

The ACT land tax regime has had the effect of increasing the price of rental properties. Canberra now has the highest rental prices in the country and it is arguably the case that people on lower incomes can no longer afford to reside in the ACT.

The ACT Government has introduced several programs to improve the supply of affordable housing for lower income groups and those suffering from socioeconomic disadvantage. These include some $141 million of housing measures in the 2022-23 Budget. However, the scale of these programs is small and they are unlikely to have a significant impact on improving the supply of affordable housing for lower income groups.

The ACT Government is a beneficiary of high land prices through proceeds from land sales, dividends from the Suburban Land Agency and income from general rates and land tax.

The stock of public housing in the ACT has not kept pace with population and has remained largely stagnant over the past decade, reducing affordable housing options for those from lower income groups wanting to reside in the ACT.

1. Introduction

1.1 Purpose

This report has been produced to assist the Select Committee on Estimates 2022-2023 in its consideration of the 2022-23 Budget.

The purpose of the report is to identify major features of the Budget that the Committee may wish to explore in its consideration of the Budget. The report does not express any judgement on the appropriateness of individual decisions reflected in the document. The focus of the report is on reasonableness of assumptions used in construction of the Budget and the consistency and transparency of the presentation of the Budget aggregates.

Additional comment has been provided in the report on issues specifically identified by the Committee, including on housing and Wellbeing.

1.2 Approach

The report is based on a desk-top review of the ACT Budget documentation presented to the Assembly on Tuesday 2 August 2022. We have also consulted other documentation in the public domain including Commonwealth Government Budget Papers and economic statements, previous ACT Budget documents, reports of the ACT Auditor-General, various Ministerial statements, Departmental reports and other research literature.

1.3 Limitation of Scope

In preparing advice for the Select Committee, Pegasus has relied on details contained in the Budget Papers, our independent research and analysis and other public sources. Pegasus did not have access to Treasury working papers or other internal documentation. Work was undertaken within a week of the presentation of the Budget to the Legislative Assembly.

These matters have limited Pegasus' ability to perform a full and complete review.

2. Economic Forecasts

Most of the ACT Budget economic forecasts for 2022-23 appear reasonable, with exceptions in relation to the consumer price index (CPI) and population growth.

If the Reserve Bank's and Commonwealth Government's most recent forecast for the CPI in 2022-23 are in the ballpark then it is highly likely the ACT Government forecast for the Canberra CPI in 2022-23 is too low.

The ACT Government is forecasting and projecting accelerating population growth. However, the outlook for population growth presented by the ACT Government is quite optimistic compared to forecasts prepared by the Centre for Population that suggest slightly more modest population growth for the ACT.

2.1 Overview

A summary of current economic trends alongside the economic estimates and forecasts contained in the 2022-23 ACT Budget are provided in Table 1 below.

Table 1: Current outcomes and economic estimates and forecasts in the 2022-23 ACT Budget, percentage change

Indicator	Current outcomes	2021-22 Estimates and Outcomes	**2022-23 Budget**	2023-24 Forecasts	2024-25 Projections	2025-26 Projections
Gross State Product[1]		3	3	3	3	3
State Final Demand[1,2]	3	2¼	2½	2¼	2½	2½
Employment[3,4]		0.1	2	1¾	1¾	1¾
Wage Price Index[2,3]	2.8	2¾	3¼	3½	3½	3½
Consumer Price Index[4]		6.3	3¾	3	2½	2½
Population[3,5]	0.4	½	1½	1¾	2	2

1. In year average terms.
2. Outcome to the end of March 2022.
3. Through the year.
4. Outcome for 2021-22.
5. Outcome to the end of December 2021.

Sources: ACT Government (2022a), Australian Bureau of Statistics (ABS) (2022, 2022a, 2022d, 2022d, 2022f).

2.2 ACT Gross State Product and Final Demand

Gross domestic product (GDP) measures the value of goods and services that an economy produces in a period (Li & Gao, 2021, p. 2). Gross state product (GSP) is the equivalent of GDP for a region of a national economy (Australian Bureau of Statistics, 2021b). This measure can be produced for a

region of any size whether a state, territory, or district. In the Australian context, it is compiled for the six states and two territories.

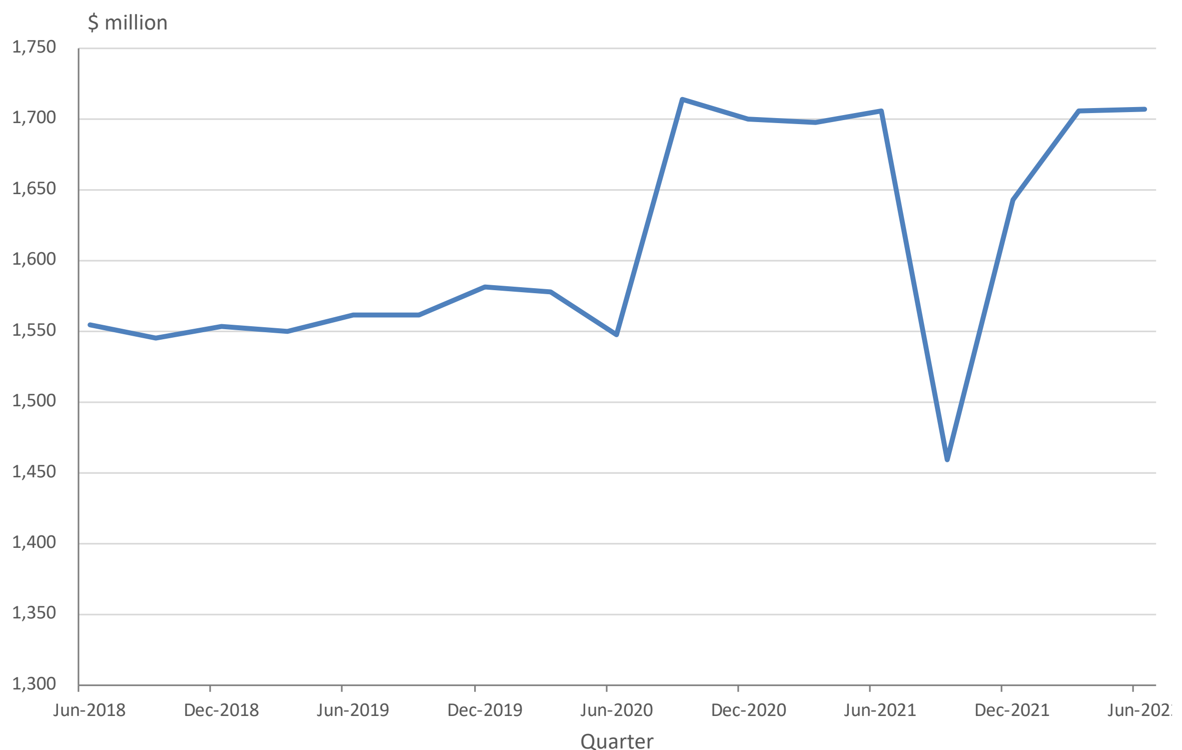
The Australian Bureau of Statistics (ABS) publishes the Australian GDP quarterly but GSP is only available annually (Li & Gao, 2021, p. 2). Also, estimates of GSP are only published annually with a significant time delay following the end of the financial year. The best and most immediate indicator of economic activity within the ACT is final demand. Final demand contains most of the components of GSP and is highly correlated with GSP.

The most recent national accounts released by the ABS (2022) relates to the March quarter 2022. ACT final demand grew by 1.7% in the March quarter 2022. Household consumption appears to have almost finally recovered from the September quarter 2021 when parts of the economy were shut down due to the COVID-19 pandemic, driving a 10.8% fall in household consumption. Household consumption bounced back to grow by 8.9% in the December quarter 2021 and by 3.0% in the March quarter 2022.

Growth in final demand for the year ending March 2022 was 3.1%, which is somewhat higher than the Budget estimate for an increase in ACT final demand of 2¼% for 2021-22, although not incompatible.

Household consumption in the ACT has now recovered from its COVID-19 pandemic induced slump in the September quarter 2021. Retail trade (which makes up around a third of household consumption) has now grown for three consecutive quarters. Retail trade for the ACT economy is outlined in Figure 1 below.

Figure 1: Retail Turnover for the ACT Economy, March Quarter 2019 to the September Quarter 2020 ($ million, constant 2020-21 dollars)

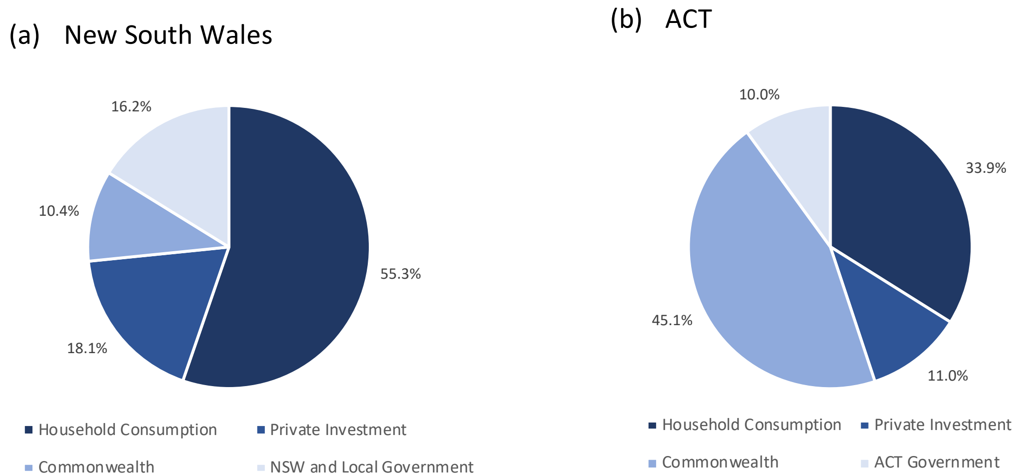


Source: ABS (2022e).

Pegasus has no reason to query the forecasts of ACT final demand of growth of 2½% in 2022-23, 2¼% in 2023-24, with projections of 2½% growth in the out-years. Nor do we question forecasts and projects for 3% growth in GSP in 2022-23 and the out-years.

As the seat of the Commonwealth Government, the ACT is heavily dependent on the consumption and investment decisions of the Commonwealth Government. This can be seen in Figure 2 below, which compares the four main components of the New South Wales (NSW) and ACT economies.

Figure 2: Components of Final Demand for the New South Wales and ACT economies, year ended March 2022

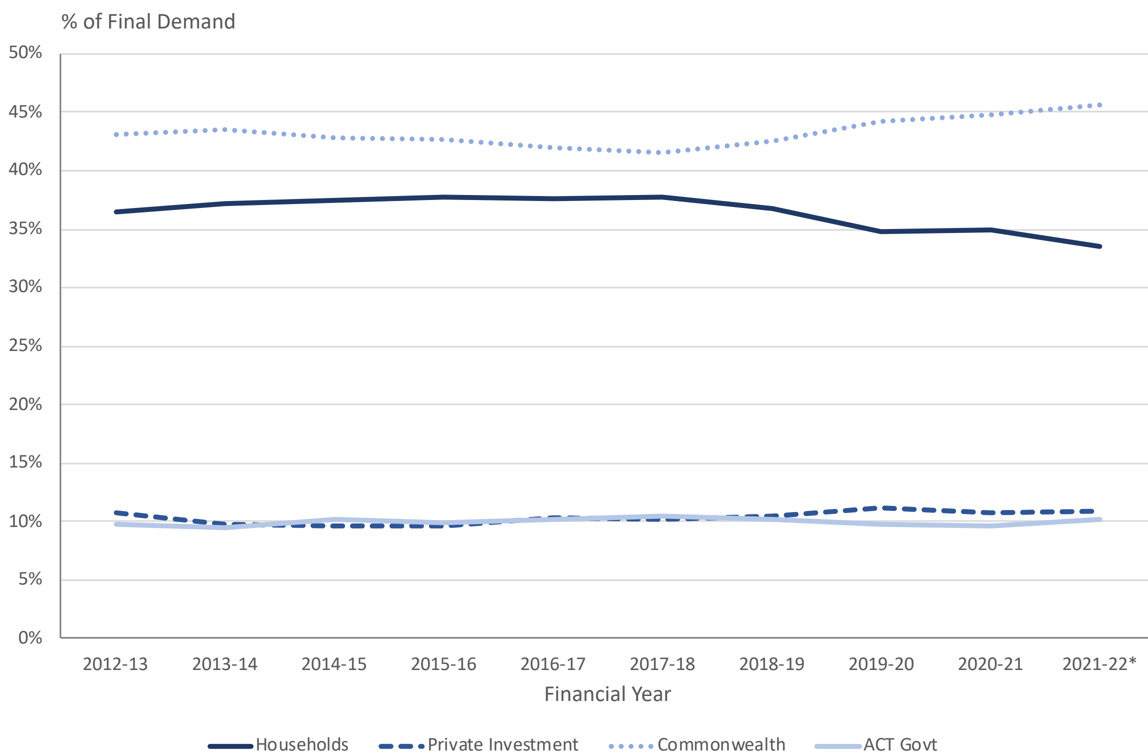


Source: ABS (2022) .

In the year to the end of March 2022, the Commonwealth represented 45.1% of total demand in the ACT economy while household consumption represented 33.9%, private investment 11.0%, and 10.0% for the ACT Government.

The historical relative shares of ACT final demand are provided in Figure 3 below.

Figure 3: Relative shares of ACT Final Demand – 2012-13 to 2021-22*



Source: ABS (2022).
* 2021-22 only includes the September and December quarters 2021, and the March quarter 2022.

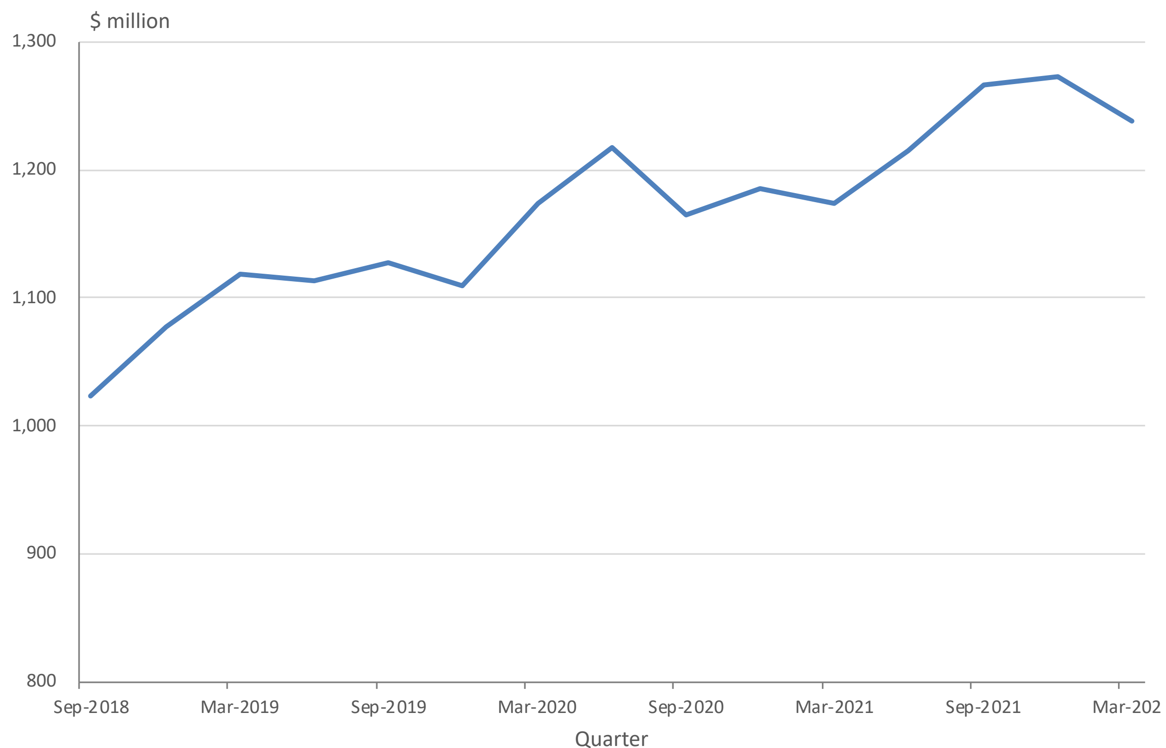
Since 2019-20 a contraction in the household consumption share of final demand has been offset by an expansion in the Commonwealth Government share. The contribution of the ACT Government to final demand has been hovering at around 10% on average over the past decade, while private investment has averaged slightly higher at 10.3% over the same period.

Since the onset of economic disruption caused by the COVID-19 pandemic, the ACT economy has become less diverse and more dependent on the public sector, with the Commonwealth and ACT governments' now accounting for more than 54% of final demand.

2.2.1 ACT Economy Public Sector Fiscal Stimulus During the COVID-19 Pandemic

The national accounts show that the ACT Government increased its spending to support the ACT economy during the second half of 2021. ACT Government consumption expenditure recorded an all-time high in the September and December quarters of 2021 as set out in Figure 4 below. This is probably related to the 11,000 businesses that received the COVID-19 Business Support Grants and eligible workers in the ACT who were able to receive the Commonwealth's Pandemic Disaster Leave Payment from 20 August 2021 (ACT Government, 2022a, p. 17).

Figure 4: ACT Government Consumption Expenditure – September 2018 to March 2022 ($ million, constant 2019-20 dollars)



Source: ABS (2022).

2.3 Employment

Employment growth through the year on a quarterly basis to the end of June 2022 for the ACT was running at 0.1% in seasonally adjusted terms (Australian Bureau of Statistics, 2022b). While the ACT lost almost 13,000 jobs during September and October 2021 at the height of the second wave of the COVID-19 pandemic, the available evidence suggests those jobs have now been recovered.

In the 2022-23 ACT Budget, the ACT Government is estimating employment growth of 2% in 2022-23, moderating slightly to grow by 1¾% in 2023-24, with projections for growth1¾% in the out-years.

A rebound in employment growth from the pandemic affected 2021-22 levels does not appear unreasonable.

2.4 Wage price index

The Wage Price Index (WPI) is currently running at 2.8% through the year to the end of the March quarter 2022 (Australian Bureau of Statistics, 2022f), which is consistent with the ACT Budget estimate of 2¾% for 2021-22.

In the 2022-23 ACT Budget, the ACT Government is estimating growth in the WPI of 3¼% in 2022-23, with the forecast for 2023-24 and projections for the out-years rising to 3½%. The forecast for 2022-23 is consistent with the Commonwealth Government's most recent forecast for the WPI for the nation and broadly consistent with the forecasts and projections in the out-years.[1]

On this basis, forecasts and projections for wages growth appear reasonable.

2.5 Consumer price index

We have some reservations about the Consumer Price Index (CPI) assumptions in the Budget.

The percentage change for 2022-23 for Canberra was 6.3% (Australian Bureau of Statistics, 2022a). The ACT Government is forecasting CPI growth of 3¾% through the year to the end of June 2023, 3% in 2023-24, and 2½% in the out-years. By contrast, the Reserve Bank of Australia (RBA) (2022, p. 59) is forecasting CPI growth of 6¼% in 2022-23 while the Commonwealth Government is forecasting CPI growth of 5¼% in 2022-23 across the eight capital cities (Chalmers, 2022). The ACT Budget is therefore based on an assumption that CPI growth in the ACT will be 1½ to 2½% lower than the national average. The annual percentage increase in the national CPI each financial year has been highly correlated with the ACT CPI, and an annual difference of the magnitude suggested by the most recent RBA and Commonwealth forecasts as compared to the ACT government forecast is unprecedented in over 20 years.

The ACT Government (2022a, p. 30) has argued that the ACT's contractual arrangements for the supply of green energy will mean that the ACT will be somewhat insulated from further CPI rises associated increased energy prices in other jurisdictions. According to the ACT Independent Pricing and Regulatory Commission (2022), ActewAGL's regulated (standing offer) tariffs will decrease, on average, by at least 1.25% as from 1 July 2022.

This is unlikely to result in a large discrepancy between the CPI in Canberra and the national result.

At present, electricity prices make up only 2.5% of the CPI basket for Canberra (Australian Bureau of Statistics, 2021). Also, gas and other household fuels (presumably largely consisting of natural gas), make up only 1.9% of the CPI basket for the ACT, suggesting ACT residents are relatively the largest per capita consumers of natural gas in country.[2] Any benefit ACT residents are likely to receive from lower electricity prices arising from green energy supply arrangements are likely to be partially offset from higher natural gas prices flowing through to consumers from recent gas price rises.

If the Reserve Bank's and Commonwealth Government's most recent forecast for the CPI in 2022-23 are in the ballpark then it is highly likely the ACT forecast for the Canberra CPI in 2022-23 is too low.

As the ACT budget forecast for the CPI in 2023-24 for growth of 3%, and projections of moderating growth of 2½% growth in the out-years is consistent with the most recent Commonwealth

[1] See Chalmers (2022).

[2] The CPI basket nationally has a weighting of 0.97% for gas and other households, while the CPI basket for Melbourne has a weighting of 1.74% for gas and other households, the second largest across all capital cities after Canberra.

Government national CPI forecasts, the forecast and projections for the out-years appear reasonable.

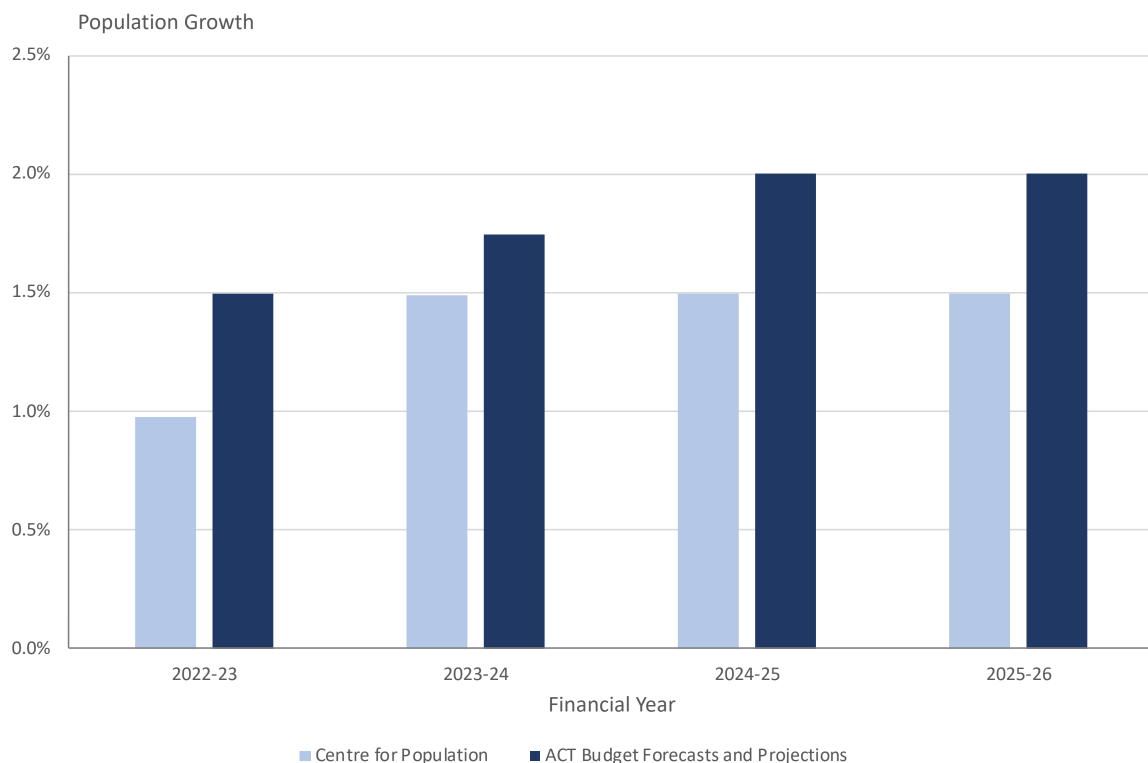
2.6 Population growth

Population growth for the ACT is currently running at 0.4% through the year to the end of December 2021 (Australian Bureau of Statistics, 2022d), which is consistent with the ACT Government (2022a) budget forecast of 0.5% growth in 2021-22.

The ACT Government (2022a) is projecting accelerating population growth, with forecast growth of 1½% in 2022-23, increasing to 1¾% in 2023-24, and projections of 2% growth in the out-years. The ACT Government (2022a, p. 27) contends the ACT's population growth rate is expected to progressively return to its pre-pandemic rate, reaching 2% by 2024-25. However, the outlook for population growth presented by the ACT Government is optimistic compared to forecasts prepared by the Centre for Population (2022, p. 6) that suggest more modest population growth for the ACT. While the Centre for Population is forecasting ACT population growth will increase following the pandemic, it is not expected to return to its pre-pandemic levels.

The difference between ACT Government and the Centre for Population ACT population growth forecasts is outlined in Figure 5 below.

Figure 5: ACT Government and Centre for Population ACT Population Growth Forecasts: 2022-23 to 2025-26



Sources: ACT Government (2022a) and Centre for Population (2022, p. 6).

3. Housing Market Issues

Many people in the ACT are experiencing difficulties in accessing housing in the ACT. Budget settings have contributed to this problem.

Distortions in the income tax system have contributed to increased prices for houses and units across most of Australia. There is also evidence to suggest that demand for land in the ACT vastly exceeds supply, adding to the pressure on prices arising from the income tax system.

The ACT land tax regime has had the effect of increasing the price of rental properties. Canberra now has the highest rental prices in the country and it is arguably the case that people on lower incomes can no longer afford to reside in the ACT.

The ACT Government has introduced several programs to improve the supply of affordable housing for lower income groups and those suffering from socioeconomic disadvantage. These include some $141 million of housing measures in the 2022-23 Budget. However, the scale of these programs is small and they are unlikely to have a significant impact on improving the supply of affordable housing for lower income groups.

The ACT Government is a beneficiary of high land prices through proceeds from land sales, dividends from the Suburban Land Agency and income from general rates and land tax.

The stock of public housing in the ACT has not kept pace with population and has remained largely stagnant over the past decade, reducing affordable housing options for those from lower income groups wanting to reside in the ACT.

3.1 Introduction

In a meeting between members of the ACT Legislative Assembly's Select Committee on Estimates 2022-2023 and Pegasus consultants on 27 July 2022, it was requested that Pegasus examine issues related to housing inequality issues. This section of the report responds to that request.

3.2 House and Rental Prices in the ACT

During the 2020-21 financial year, Canberra became the second most expensive capital city to purchase a house behind Sydney, overtaking Melbourne median house prices by recording year-on-year median house price growth of 36.6% (Domain, 2021). In 2020-21, Canberra's median house price rose to in excess of $1 million. The weighting in the consumer price index (CPI) suggests the amount spent on new dwelling purchases in Canberra is the highest in the country across all capital cities as a proportion of household expenditure (Australian Bureau of Statistics, 2021). In the CPI 'basket' for Canberra, new dwelling purchase currently has a weighting of 10.34%, compared to the national average of 8.67% and Sydney at 9.47%.

The price of land in the ACT is unlikely to abate any time soon, with the ACT Government (2022a, p. 244) attributing a $96.1 million increase in dividends expected to paid by the Suburban Land Agency

in 2023-24 over what is forecast in 2022-23 to “a general increase in the value of land scheduled for settlement compared to the 2022-23 financial year.”

Importantly for many low-income earners, or transfer recipients, higher house prices reduce rental affordability, as rents need to increase if investors are to maintain their rental yield (Henry, Harmer, Piggott, Ridout, & Smith, 2009b, p. 413).

Continuous increases in rentals for houses and units has seen Canberra become the most expensive capital city to rent in Australia, a title held in relation to houses for the past four years and units for almost two years (Domain, 2022a). In the year to the end of June 2022, the median rental price for houses rose by 11.3% and for units by 10%.

The 2021 Rental Affordability Index reveals that Canberra is the least affordable capital city for low-income households (SGS Economics and Planning Pty Ltd, 2021, p. 11). In the ACT, rents are pushed up by the overall high-income earning workforce, pricing many low-income households out of the market.

The ACT Government (2022a, p. 24) contends that housing remains affordable in the ACT given the relatively high income levels. This statement is factually correct as the ACT enjoys the highest level of average weekly ordinary time earnings for adults working full time across all states and territories.[3] However, it is also arguably the case that people on lower incomes, often suffering from socio-economic disadvantage, can no longer afford to reside in the ACT.

Exacerbating affordability problems in relation to rental properties in the ACT is the ACT Government’s land tax applied to investor-owned dwellings. The potential problem arising from the application of land tax on rental properties in the ACT is that most of the impost is likely to be passed through to prospective renters in the form of higher rental prices. As John Mungoven (2021) wrote in *The Canberra Times* in February 2021:

> *I doubt most ACT residents are aware that when an average ACT house is rented, and the residential rates are, say, $2750 a year, the government charges the home owner/landlord about an additional $4000 a year as land tax.*
>
> *Guess who those costs are passed onto in rent? The tenant of course. That is the main reason rents are so high here.*

According to Michael Yardney, the chief executive of Metropole Property Strategists, the biggest challenge in the ACT for property investors is land tax:

> *Canberra property has consistently done well over the long term and it’s not as volatile as other states but the high rates for all home owners and the disproportionately high level of land tax over stamp duty means investors shouldn’t be tempted to buy there.*
>
> *It’s a great place to buy if you’re going to live there as you don’t have to pay land tax on a principal place of residence or below a certain land value threshold, but investors should be wary. (Williams, 2022)*

According to Property Investment Professionals of Australia chairwoman Nicola McDougall, the ACT is probably more of a home-owner market rather than an investor one, and that the land tax requirements make it less appealing for investors (Williams, 2022).

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[3] Australian Bureau of Statistics (2022a).

The Budget Papers acknowledge community concerns about access to housing. The Budget Outlook includes the following statement:

> *During consultations on the 2022-23 Budget, participants identified the challenges associated with housing affordability and supply and their disproportionate effect on the more vulnerable members of the ACT community. The community indicated a need for greater access to safe and secure public housing, more support for homelessness and better access to short-term emergency accommodation. Community input also demonstrated a need for more affordable housing for low-to-medium income households. (ACT Government, 2022a, p. 71).*

While the Budget Papers include a number of indicators of Wellbeing in the ACT, and 'Housing and home' is identified as one of the Wellbeing domains that has informed the development of policies in the Budget, the Budget Papers do not provide any specific indicators of Wellbeing in this domain.

3.3 Demand Side Income Tax Issues

Commonwealth taxation policies are contributing to problems with housing affordability in the ACT.

Capital gains tax policies have encouraged investment in real estate that have driven up housing costs.

The Henry Tax Review (Henry, Harmer, Piggott, Ridout, & Smith, 2009, p. xxiii) made an oblique reference to the CGT exemption in relation to owner-occupied housing and the widespread community support that it enjoys:

> *While the overall demand for housing is increased by favourable tax and transfer provisions particularly for owner-occupied housing, these provisions are of very long standing and have deep community support.*

Most of the benefits of this tax break are enjoyed by people wealthy enough to invest in housing while the costs of higher rent are paid by low income households.

An efficient tax is one that does not unduly interfere with the operation of the market economy (Evans, 1998, p. 296). According to Waincymer (1993, p. 27):

> *[a] system of taxation in a free market economy ought to minimise any undesirable disruption to the market mechanism… The government aims to raise the revenue it requires, but as far as possible allow the decisions of individuals to remain as they would have been in the absence of the tax. If a system of taxation encourages people to shift resources between sectors, it operates against the market system and is hence inefficient in economic terms.*

In this manner, the tax system should be neutral between investment and consumption decisions. However, favourable tax treatment of owner-occupied housing compared to other asset classes can create distortions in the economy. According to a report from the Australia Institute (Grudnoff, 2016, p. iii):

> *Reducing the concession is likely to have a positive economic impact by reducing distortions in the economy. At present the exemption encourages over capitalisation in main residences since any increase in their value is tax free. This has the effect of pushing up the value of housing and therefore making that housing less affordable. It also reduces investment in other areas.*
>
> *Capital gain is less productive for the economy than other forms of income. Earning an income from a capital gain does not require the production of*

something but instead means holding an asset while its value increases. So from an economics perspective this is a less useful form of income.

The Organisation for Economic Co-operation and Development (OECD) (2022, p. 9) has recently observed that:

The majority of countries fully exempt capital gains on main residences, and while there may be justification for such an approach, an uncapped exemption provides vastly greater benefits to the wealthiest households and further distorts the allocation of savings in favour of owner-occupied housing.

In the Australian context, the Australia Institute (Grudnoff, 2016) has published research findings suggesting that low income households (those in the bottom 30%) get almost no benefit from this tax break. In contrast, almost 90% of the benefit goes to the top half of income earners while the bottom half get only 11%, with high income households (those in the top 20%) receiving more than half of the benefit (55%).

While investment in residential property is subject to the CGT, the concessional treatment enjoyed by property investors through the application of a 50% discount on realised capital gains as compared to rental income (subject to no discount), means that investment returns in the Australian residential housing market are likely driven by capital gains rather than by rental yield (Henry, Harmer, Piggott, Ridout, & Smith, 2009b, p. 418). The CGT concessional treatment enjoyed by property investors is amplified when investments are geared (Henry, Harmer, Piggott, Ridout, & Smith, 2009b, p. 417).

While this distortion applies equally across the entire country, the impacts are arguably greater in markets like the ACT where imbalances between demand and supply mean that greater capital gains can be anticipated.

3.4 Supply Side Issues

The Budget Papers state that the estimates reflect a steady schedule of land releases to meet forecast demand, "reflecting the upgrades to population growth" (ACT Government , p.374). It is difficult to reconcile this claim with the population growth assumptions in the Budget and land revenue for ACT Government PTEs and the ACT General Government sector dividends from land sales in the financial statements.

Nothwithstanding these claims, there is some evidence that the supply of land for residential property development in the ACT is inadequate.

In February 2022 the first release of fixed price blocks offered by ballot for the new Canberra suburb of Macnamara attracted significant interest, with 12,300 registrations received for the 71 blocks available (Starmer, 2022). A second ballot of fixed price blocks by ballot saw 7400 buyers register for 51 blocks of land (Levinson, 2022).

According to the selling agent, Linda Lockwood of Belle Property Canberra, land in Canberra's Inner South is scarce (Taulaga, 2022). Ms Lockwood further contended:

Land is a rare commodity and demand is much greater than supply. [The ACT government] just isn't releasing as much anymore.

The executive director of the Housing Industry Association (HIA) in the ACT, Greg Weller has said he doesn't believe the ACT Government is distributing land in a way that is helping to control accelerating prices (Twyford, 2022). He described their current method of ballots as 'drip-feeding' land.

[We have] a situation in which a lot of people are chasing a small number of blocks and that invariably puts price pressure onto new homes … making it more expensive and less attractive to build a new home.

Mr Weller said if enough land was available for people to buy, a significant number of housing problems would be solved and that, ultimately, more land will have to be released (Twyford, 2022). He also pointed to increasing medium-density housing in the suburbs and changing planning laws to allow more subdivisions in developed suburbs as key levers the ACT Government can pull to ease the pressure on the market.

In this regard, the Productivity Commission (2004, p. XXV) has previously observed in relation to State and Territory governments:

Most governments have sought to limit the outward expansion of their capital cities, in order to reduce infrastructure costs and protect the environment. In doing so, the scarcity value of land in those cities will inevitably rise. Unless there are offsetting increases in housing density, affordability will be adversely affected.

ACT Opposition Leader Elizabeth Lee has accused the ACT Government of "deliberately restricting the release of land in the ACT" (Levinson, 2022). On the other hand, Chief Minister Andrew Barr has argued the release of new land constitutes less than 2% of the total housing market, so it could not possibly affect the price of houses in established suburbs in inner Canberra or even Belconnen (Twyford, 2022).[4]

A residential dwelling provides a bundle of goods and services for house owners. In the case of owner-occupied housing, the services provided include shelter, financial security and a tax effective savings vehicle (Henry, Harmer, Piggott, Ridout, & Smith, 2009b, p. 410). Two goods provided by a residential dwelling are residential land and a dwelling (residential building), both of which feed into the price of residential property in the ACT. While residential land by itself is an imperfect substitute for a residential property due to the absence of a dwelling, nonetheless the price of residential property by itself is a major input into the price of residential property. The Productivity Commission (2004, p. 6) has previously observed the price of a 'house' represents the combined value of dwelling and the land on which it is situated.

If the supply of residential land is constrained resulting in relative scarcity, this in turn will put upward price pressure on residential land. As a major input into the price of residential property, relative scarcity in the supply of residential land can also be expected to feed into higher residential property prices.

ACT Government agencies benefit from the high land prices generated by the mismatch between supply and demand. In 2023-24, ACT Government PTEs expect to earn $72 million from market gains on land sales (ACT Government, 2022a, p. 335).

3.5 ACT Government Policies to Address Affordable Housing

The ACT Government has in recent years introduced a number of policies and programs to respond to community concerns about housing pressures.

The ACT Government provides land tax exemptions for landlords whose investment properties are managed through a community housing provider (Taulaga, 2021), under the Affordable Community Housing Land Tax Exemption. Landlords signed up to the scheme are exempt from paying land tax if they rent their properties at less than 75% market rates.

[4] It is not entirely clear whether Mr Barr is referring to the stock of housing or to the flow of housing.

The scheme was introduced in 2019, and initially, 100 properties were eligible for the exemption, that was increased to 125 in 2020 (Taulaga, 2021). The ACT Government increased the number of properties eligible under the scheme to 250 in 2021, despite only 54 landlords signing up to the scheme. Given the low take-up of the scheme, it is unlikely that it has had a significant impact in alleviating affordability issues for renters.

The ACT Government also has a number of other programs to assist those on low incomes and those suffering from socio-economic disadvantage find affordable housing. These include:

- Affordable Home Purchase Scheme, which assists low-to-moderate income households by providing homes for purchase at affordable prices (ACT Government, 2022a, p. 74)
- A commitment for the provision of 600 affordable rental dwellings through promoting Build-to-Rent opportunities
- Dedicating at least 15% of the Indicative Land Release Program to affordable, community and public housing (ACT Government, 2022a, p. 75).

New housing initiatives in the 2022-23 Budget total some $141 million over 4 four years, as set out in Table 2 below.

Table 2: Housing initiatives included in the 2022-23 Budget ($'000)

Initiative Name	2022-23	2023-24	2024-25	2025-26
Delivering more affordable housing				
expense	0	0	0	0
Expanding specialist homelessness service				
expense	1879	2872	2534	0
Lease variation Build-to-Rent				
expense	0	0	2500	2500
Phasing out stamp duty				
expense	10100	10000	9800	10100
Securing high quality public housing				
expense	500	0	0	0
capital	57262	0	0	0
Turner Build-to-Rent pilot				
expense	321	326	0	0
Vulnerable Household Energy Support Scheme				
expense	6000	815	563	1098
capital	-11860	-5602	-2267	12653
Year four Growth and Renewal Program				
capital	7900	8400	13500	0
Total	**72102**	**16811**	**26630**	**26351**

Source: ACT Government (2022a).

There are questions about the likely effectiveness of these programs in moderating housing pressures. The OECD (2022, p. 110) has warned that evidence suggests that measures promoting homeownership may be limited in their effectiveness and can contribute to increased house prices where there are housing supply constraints.

The ACT Auditor-General (ACT Audit Office, 2020, pp. 75-76) has noted that despite land being released for affordable housing purposes, there has been poor take-up of this land to date by the ACT community and a mismatch in relation to the market preferences of tenants:

> *Only 16 of the of the 86 affordable housing dwellings offered to the market so far have proceeded to purchase. This is likely to be a reflection of affordable housing land releases thus far being primarily 1 or 2 bedroom units, while the majority of eligible purchasers are seeking 3 bedroom dwellings and single houses on compact blocks. The supply of affordable housing dwellings through the Affordable Home Purchase Program has not met the market's preferences.*

Regardless of their effectiveness, the scale and timing of the new measures is unlikely to have a significant impact on equitable access to housing in the ACT. The chief executive of the Real Estate Institute ACT, Michelle Tynan, has said that while the build-to-rent initiatives would help with rental affordability in the long-run, "without any major projects advanced or even 'shovel ready', it will be years before this strategy will assist" (Garrity, 2022). She went on to say that the delivery of 75 to 150 affordable homes outlined in the Budget will not adequately address the waiting list of over 3,000 registrations for affordable and social housing in the ACT.

3.6 Provision of Public Housing in the ACT

The ACT Government (2022, p. 8) Growing and Renewing Public Housing program aims to increase the supply of quality public housing for members of the Canberra community most in need. According to the ACT Government, this will require some tenants to relocate to alternative public housing where a property has been identified for sale or redevelopment or for safety reasons. One effect of this program will be to increase the amount of public housing where there are currently low holdings (in the outer suburbs) and decrease the amount of public housing where there are high holdings (in the inner suburbs where land values are higher).

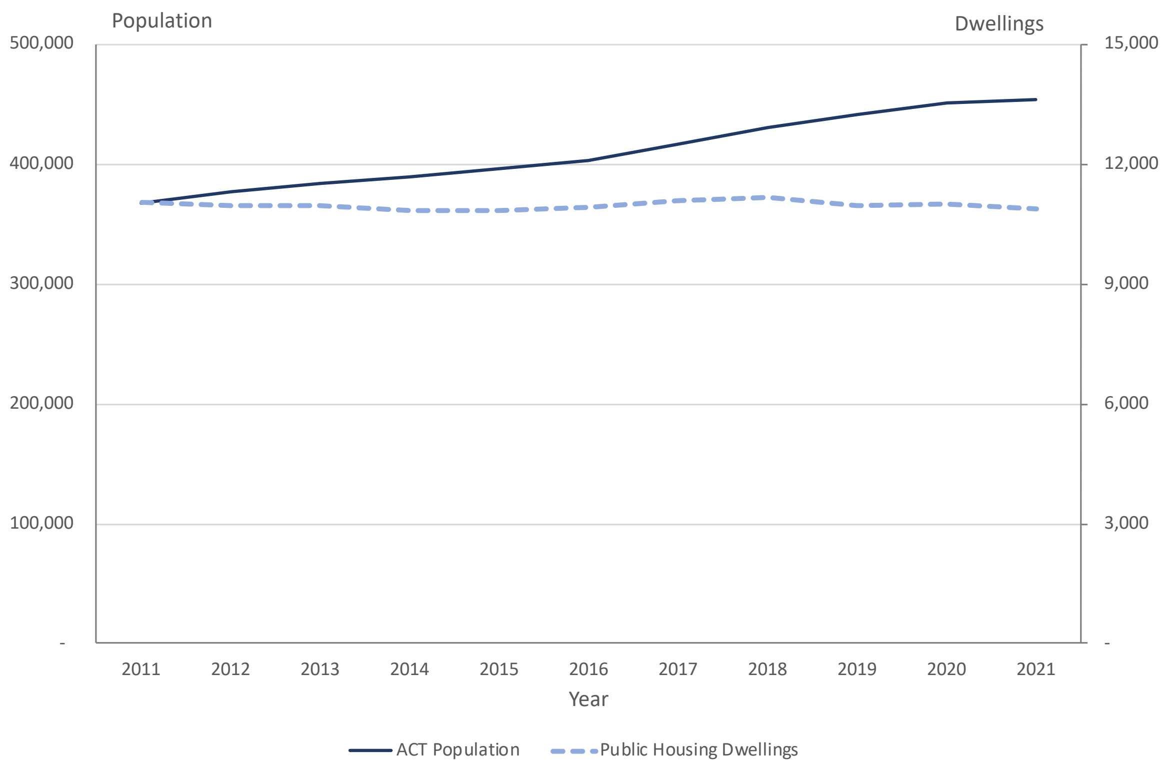
The Growing and Renewing Public Housing Program has been criticised by the CEO of the ACT Council of Social Service (ACTCOSS), Dr Emma Campbell, as "incredibly callous and cruel" (Halter, 2022). According to ACTCOSS (2022) back in early March 2022, over 300 ACT Housing tenants – including older people, people with chronic health issues and people with disability – had received letters informing them that they will need to vacate their properties. Dr Campbell has complained in relation to the relocation that:

> *The fact that properties are built on high value land that the ACT Government wishes to sell should not be a reason to order public housing tenants out of their homes.*
>
> *Many of the individuals involved are highly vulnerable, including people with dementia or complex mental health issues.*

This is not the first time the ACT Government has imposed relocation on a significant number of public housing tenants. The ACT Government sold around 1,300 public housing units in the path of light rail stage 1, involving the eventual displacement of 1,900 tenants to either existing purchased dwellings or newly constructed units (Lawson, Pawson, Troy, van den Nouwelant, & Hamilton, 2018, p. 12n).

The available evidence suggests the stock of public housing has not kept pace with ACT population growth, and has remained stagnant at around 11,000 dwellings since 2011 while the ACT resident population has grown by just over 23% between 2011 and 2021. This is illustrated in Figure 6.

Figure 6: ACT Population and the Provision of ACT Public Housing Dwellings – 2011-2021



Sources: Productivity Commission (2022) and ABS (2022d).

4. Fiscal Position

The aggregate Budget forecasts are more favourable than in either of the past two years, which were adversely impacted by the effects of COVID-19.

Growth in expense across the Budget and forward years is modest by historical standards and is lower than inflation and population growth. With a stronger than anticipated economic recovery in 2021-22, revenue collections are now expected to be stronger than previously expected.

The ACT has a strong balance sheet but that position is deteriorating over time. All of the Territory's key balance sheet measures are expected to deteriorate over the Budget and forward estimates period.

The ACT Government will be able to meet its immediate obligations over the Budget and forward estimates but the current fiscal trajectory is not sustainable over the long-term.

4.1 Operating Statement - Headline Operating Balance

The Budget Papers present a headline net operating deficit of $483.0 million in 2022-23, reducing each year to a deficit of $229.4 million by 2025-26.

Table 3: General Government Sector Headline Net Operating Balance

	2021-22 Est. outcome	2022-23 Budget	2023-24 Estimate	2024-25 Estimate	2025-26 Estimate
	$m	$m	$m	$m	$m
Revenue	7,012.8	7,079.1	7,538.3	7,525.3	7,854.1
Expenses	7,806.6	7,780.2	7,938.2	8,076.5	8,353.8
Superannuation return adjustment	213.4	218.1	234.3	251.6	270.3
HEADLINE NET OPERATING BALANCE	**-580.4**	**-483.0**	**-344.9**	**-299.5**	**-229.4**

Source: ACT Government (2022a, p. 52).

The aggregate Budget forecasts are more favorable than in either of the past two years, which were adversely impacted by the effects of COVID-19.

Although still in deficit, the Headline Net Operating Balance has improved for each of the Budget and forward years relative to the forecasts for those years announced in the 2021-22 Budget. Compared to the 2020-21 Budget, the Headline Net Operating Balance is only slightly lower for 2023-24, but shows a stronger profile in the out-years.

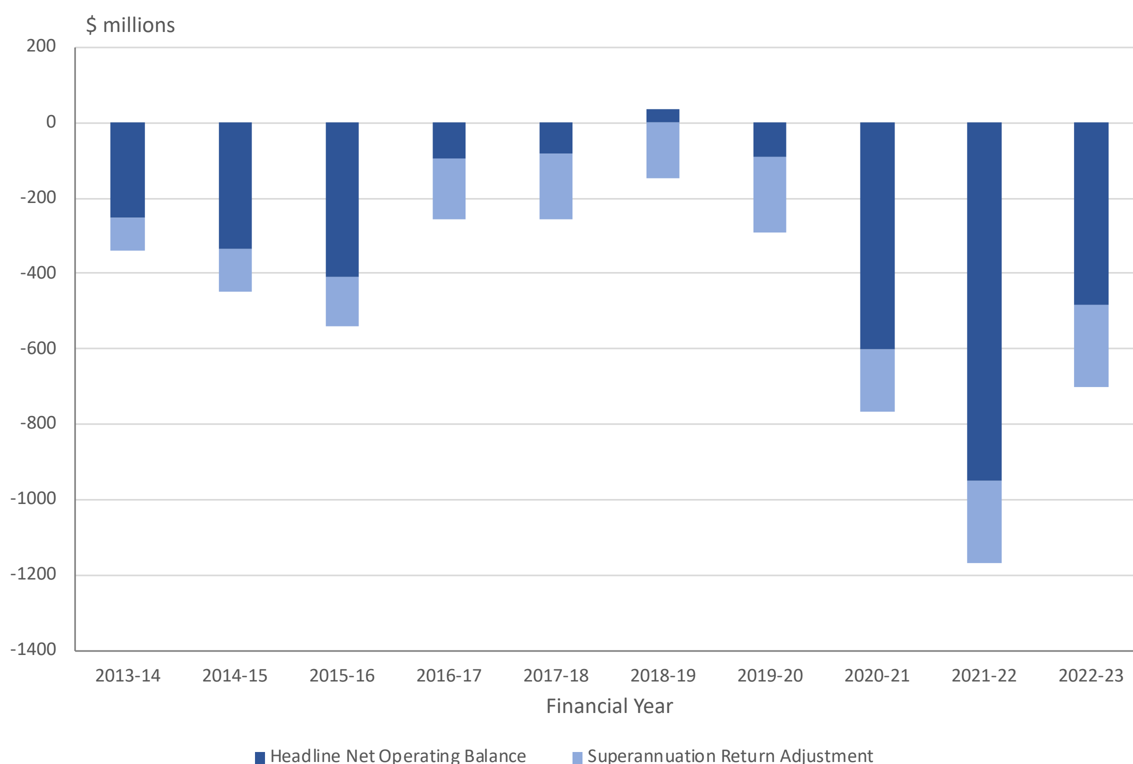
Growth in expense across the Budget and forward years is modest by historical standards and is roughly in pace with inflation and population growth. ACT revenue is forecast to be some $416 million higher in 2021-22 than in the 2021-22 Budget. In turn, revenue is now expected to be $537

million higher in 2022-23 than previously forecast at the time of the 2021-22 Budget. In the three years to 2024-25, revenue is now expected to be almost $1.8 billion higher than was previously forecast at the time of the 2021-22 Budget.

There are questions, however, about how the reported fiscal position has been constructed. While the ACT Government states that the financial statements included in the Budget papers are consistent with the requirements of the Uniform Presentation Framework agreed by the Heads of Treasury (ACT Government, 2021, p.6), discretion has been exercised in the adoption of some assumptions and inclusion of certain transactions in the reported fiscal position.

As in previous years, the reported deficit is reduced by a sizeable superannuation adjustment. The impact of the superannuation return adjustment on the reported Headline Operating Balance is shown in Figure 7 below.

Figure 7: Contribution of Superannuation Return Adjustment to Headline Net Operating Balance ($ million)



Sources: ACT Government (2013, 2014, 2015, 2016, 2017, 2018a, 2019, 2021, 2021a, 2022a).

While the superannuation return adjustment has an impact on the reported headline operating balance for 2022-23, the underlying deficits are so large that the adjustment does not shift the deficit to balance or close to balance as it did in the years between 2016-17 and 2019-20. The adjustment is however some $115 million larger than it might otherwise have been as a consequence of the use of the projected long-term investment return rather than the valuation discount rate in calculating the superannuation return adjustment.

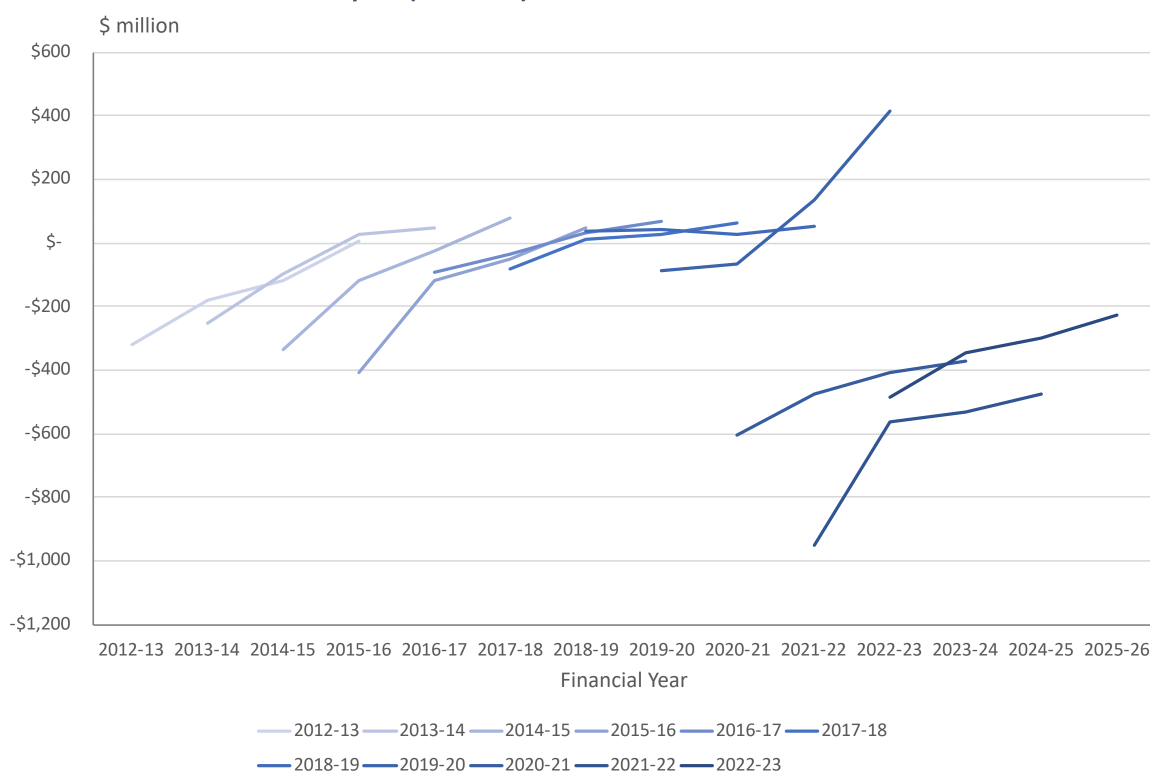
A discussion of accounting and classification issues in the Budget is provided at section 9 of this report.

4.2 Medium term forecasts

The medium-term outlook is better than forecast in either of the past two Budgets.

This represents a positive reversal of the trends historically seen in ACT Budgets. The long-term trend in the ACT has been for successive Budgets to set out progressively worse forecasts. Figure 8 below shows the Budget and forward estimates published in each year between 2012-13 and 2022-23. As can be seen, promised improvements in the budget position over the forward years have rarely materialised. In almost all cases, the Budget estimate in any year is worse than had been forecast in previous years.

Figure 8: Forecast returns to surplus ($ million)



Sources: ACT Government (2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018a, 2019, 2021, 2021a, 2022a).

The 2022-23 Budget reverses that trend. However, as the past few years have shown, Government Budgets are vulnerable to external events and unexpected shocks. The ACT Budget is particularly dependent on Commonwealth funding and growth in the Australian Public Service. A return to surplus for the ACT Government will require favourable economic circumstances and considerable fiscal discipline over a long period of time.

4.3 Measures of the ACT Government's financial position

The ACT has a strong balance sheet, but that position is deteriorating over time.

The strength of the Government's finances over the medium term can be assessed in terms of reported levels of net debt, net financial liabilities and net worth.[5] Table 4 below presents movements in these measures for the Budget and forward years.

[5] Definitions and further discussion of the application of these measures are provided in section 8 of this report.

Table 4: General Government Sector Key Balance Sheet Measures

	2021-22 Est. outcome $m	2022-23 Budget $m	2023-24 Estimate $m	2024-25 Estimate $m	2025-26 Estimate $m
Net debt (excluding super)	4,995.8	6,524.9	7,457.8	8,659.3	9,882.5
Net financial liabilities	12,146.8	11,415.7	12,212.2	13,224.8	14,226.6
Net worth	17,482.7	18,991.9	18,702.2	18,256.2	18,200.8

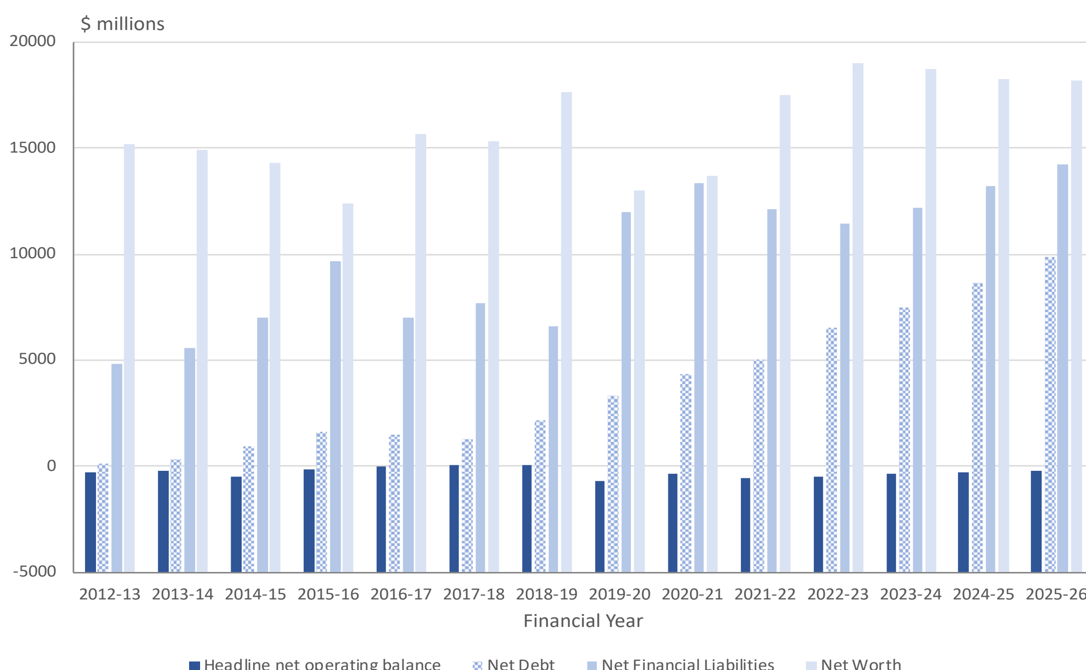
Source: ACT Government (2022a, pp. 52, 285, 286).

Table 4 shows a weakening of the Territory's financial position over the Budget and forward years. Net debt is forecast to almost double over the Budget and forward years compared to the expected 2021-22 outcome. After a period of improvement between 2019 and 2021, net financial liabilities are expected to grow over the Budget and forward years. Net worth, which is the broadest measure of the Territory's financial position, is expected to grow in 2022-23 and then fall slightly in absolute terms over the forward estimates period.

These metrics have improved in 2022-23 and all out-years relative to the 2021-22 Budget. However, 2021-22 is a poor year for comparison as forecasts for net debt and net financial liabilities in the 2021-22 Budget were adversely affected by the COVID pandemic. The fact remains that over the Budget and forward years net debt and net financial liabilities are growing while net worth is falling slightly in absolute terms.

While the key balance sheet measures can vary from year to year with changes in underlying assumptions, the long-term trend shows a deterioration in the Territory's indebtedness and financial obligations. This is illustrated in the Figure 9 below.

Figure 9: Key balance sheet measures since 2012-13 ($ million)



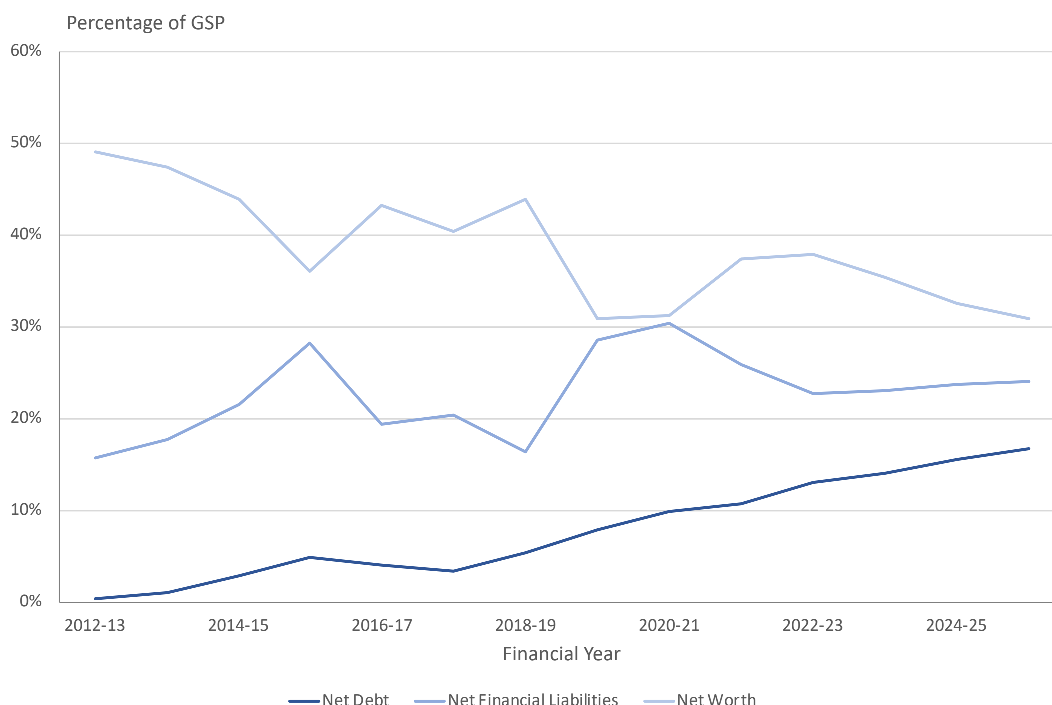
Source: ACT Government (2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018a, 2019, 2021, 2021a, 2022a).

Note: From 2019-20, net debt includes the impact of accounting changes in relation to the treatment of leases. The ACT Government has indicated that for this reason net debt from 2019-20 is not directrly comparable to prior years.

Figure 9 shows that net financial liabilities have more than doubled since 2012-13 and will have almost tripled by 2025-26. Over the same time, net debt will have grown from around $100 million in 2012-13 to more than $5 billion currently and almost $10 billion by the end of the forecast period. Net worth has grown in absolute terms over this period but at a much slower rate.

When expressed as a proportion of Gross State Product, all of the Territory's key balance sheet measures are expected to deteriorate over the Budget and forward estimates period, as shown in Figure 10.

Figure 10: Key balance sheet measures as a proportion of Gross State Product



Source: ABS (2021a), ACT Government (2022a, 285-286).

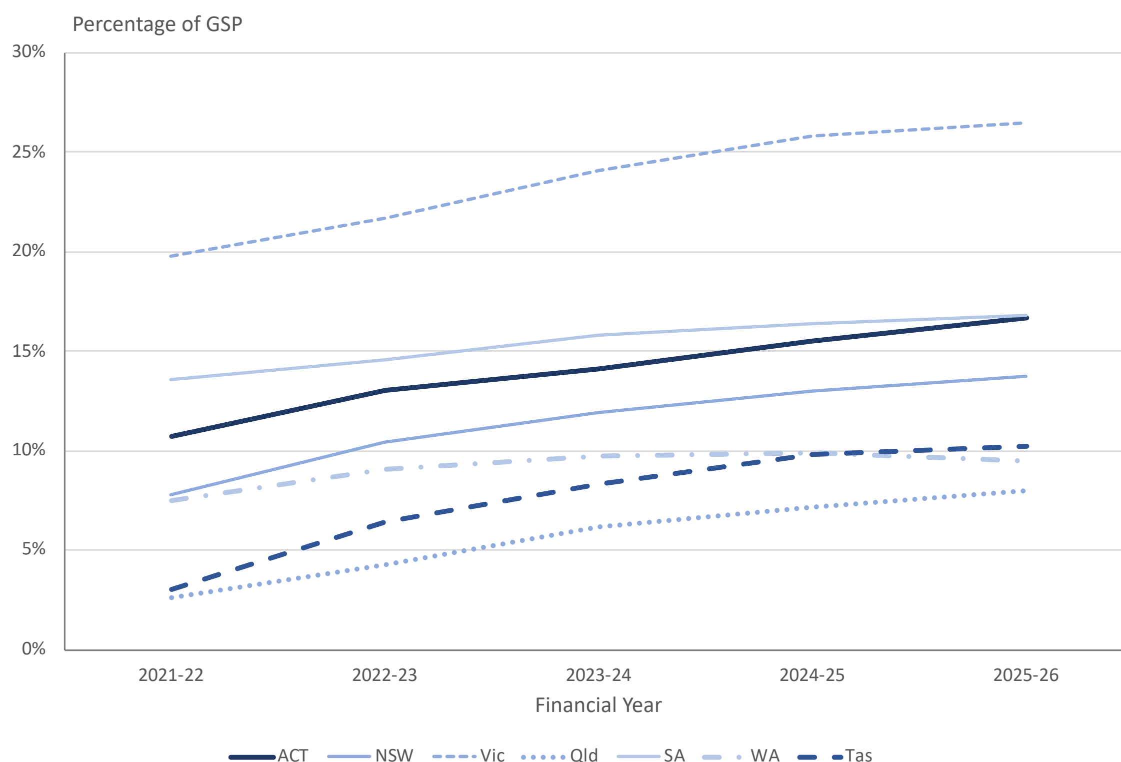
Taken together, these trends suggest a weakening over time of the ACT Government's balance sheet.

4.4 Comparisons with other States and Territories

All Australian jurisdictions reported a decline in their fiscal positions during the COVID pandemic, and the relative deterioration in the ACT Government's position was within the range of expected outcomes reported by other governments (ACT Government, 2021, pp.201-204). This continues to be the case.

Figure 11 shows a comparison of net debt as a proportion of GSP for the Australian States and Territories.

Figure 11: Net debt comparison across jurisdictions (% of GSP)



Source: 2022-23 State and Territory Budget papers, ABS (2021a).

Figure 11 shows that the ACT level of net debt as a proportion of GSP is within the range reported by other State and Territory governments, albeit at the higher end of that range. However, the chart also shows that other States and Territories apart from Victoria have begun a process of budget consolidation as their economies emerge from the pandemic.

Estimates of net financial liabilities and net worth for each jurisdiction are set out in Table 5. Table 5 below shows that the level of net financial liabilities and net worth for the ACT are in the range of outcomes for all States and Territories.

Table 5: Net financial liabilities and net worth comparison across jurisdictions as a percentage of GSP, 2021-22 (est. outcome)

	Net fin. Liabilities	Net worth
ACT	25.9	37.3
NSW	26.6	39.6
Vic	28.7	27.3
Qld	13.8	47.9
SA	31.9	37.5
WA	7.1	31.1
Tas	28.3	29.2
NT	42.2	38.6

Source: State government 2022-23 Budget papers.

The credit rating of all State and Territory debt is assessed from time to time by ratings agencies. The ACT currently enjoys a Standard & Poors rating of AAA on its long-term debt and a rating of A-1+

on its short-term obligations. This means that the ratings agency considers that the ACT has an extremely strong capacity to meet its long and short-term financial commitments.

Table 6 below sets out the credit ratings on long-term debt for all States and Territories. The table shows that the ACT has a level of creditworthiness that is better than or comparable to that enjoyed by other States.

Table 6: Long-term credit rating as reported by States and Territories, 2022-23

	Moody's	S&P
ACT	-	AAA (Negative)
NSW	Aaa (Stable)	AA+ (Stable)
Vic	Aa1 (Negative)	AA (Stable)
Qld	Aa1 (Stable)	AA+ (Stable)
SA	Aa1 (Stable)	AA+ (Negative)
WA	Aa1 (Stable)	AA+ (Positive)
Tas	Aa2 (Stable)	AA+ (Stable)
NT	Aa3 (Stable)	-

Source: State government 2022-23 Budget Papers and State treasury websites.

Overall, the ACT's financial position is very strong and is within the range reported by other States and Territories.

4.4 Other measures of sustainability

Additional measures of the sustainability of Territory's financial position are also available.

In financial audits, the ACT Auditor-General has employed measures such as:

- Assets to liabilities coverage;
- Short term assets to short term liabilities coverage; and
- Financial assets to liabilities coverage.

The benefit of these measures is that they provide an indication of the Territory's capacity to meet its obligations over the short and medium-term.

As part of this review, Pegasus undertook analysis of the capacity of the General Government sector to meets its financial obligations using similar ratios.

The coverage of assets to liabilities falls over the Budget and forward years from about 1.8 times in 2022-23 to about 1.6 times in 2025-26.

The ratio of short-term assets to short term liabilities also deteriorates over the Budget and forward years.

Financial assets are forecast to exceed net financial liabilities by approximately 2.0 times in 2022-23 to approximately 1.7 times in 2025-26.

This analysis reinforces the suggestion that the ACT Government's financial position is deteriorating over the medium term.

Cash flows from operating activities and investments for policy purposes are forecast to be negative in all but one of the Budget and forward years.

An overall General Government cash deficit of $1.2 billion and negative net cash from operations of $92.5 million have been forecast for 2022-23.

These positions generally improve over the forward years, with the cash deficit reducing across each of the forward years. Similarly, net cash from operations is forecast to be positive across each of the out years.

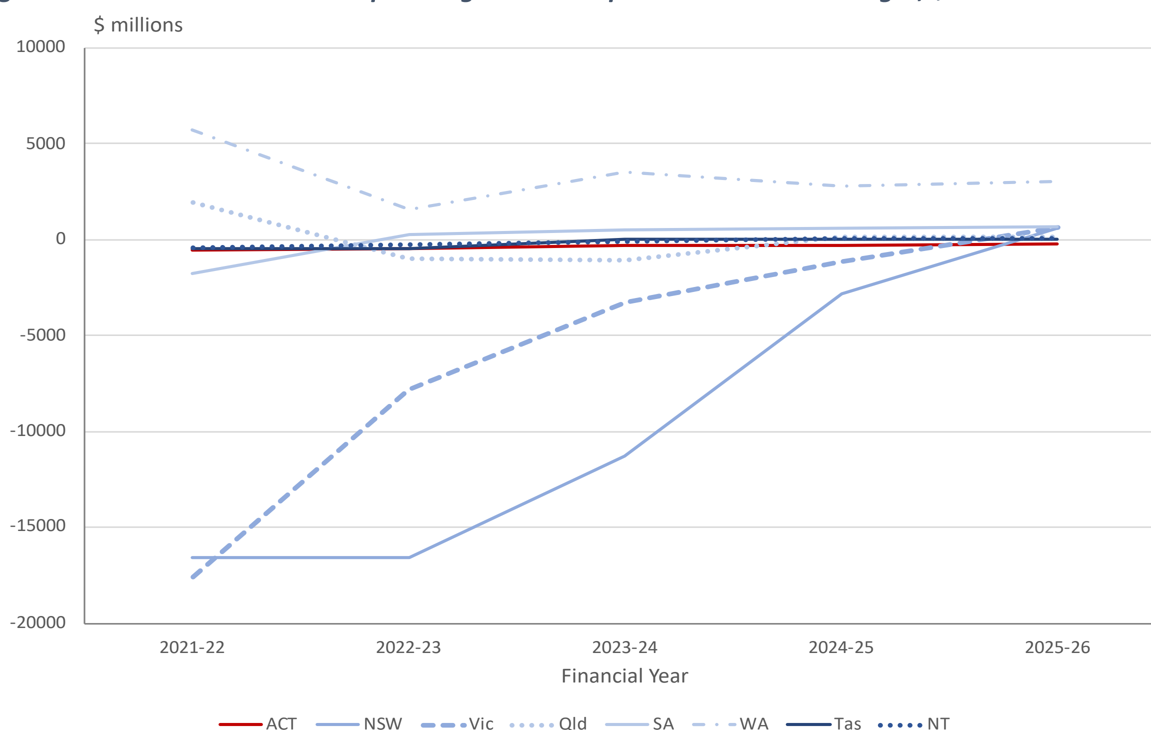
The ACT Government will be able to meet its immediate obligations over the Budget and forward estimates but the current fiscal trajectory is not sustainable over the long-term.

4.5 Strategies for fiscal recovery

The ACT Government has previously indicated that it recognises the importance of restoring public finances and reducing net debt and has stated that it would systematically reduce debt over the long term (ACT Government, 2021, pp. 52). The Government also indicated at that time that this should be deferred until the COVID pandemic had passed (ACT Government, 2021, p.53).

Other States and Territories have commenced a process of fiscal consolidation, with large forecast reductions in operating balances over the forward estimates, as shown in Figure 12.

Figure 12: Movements in State operating balance reported in 2022-23 Budget, $million



Sources: 2022-23 State and Territory Budget papers.

Of most relevance to the ACT, the Commonwealth Government has indicated that it proposes to commence a period of budget repair. As noted in the Budget papers, this represents a risk for the Territory's financial position as 38.2 percent of the Australian Public Service is located in the ACT (ACT Government 2022a, p.36). Budget repair by the Commonwealth will require complementary adjustments to the ACT Budgets if the Territory's fiscal position is not to deteriorate further.

The ACT Government (2022a, p. 48) has indicated in the Budget Outlook that the path back to a balanced budget will continue to be a focus for the Government over the medium-term. However, we could however find no evidence in the Budget Papers of any articulated strategy for reducing the Territory's debt burden or a timeframe for the return to surplus.

5. Revenue

ACT revenue is forecast to be some $416 million higher in 2021-22 than in the 2021-22 Budget. In turn, revenue is now expected to be $537 million higher in 2022-23 than previously forecast at the time of the 2021-22 Budget. In the three years to 2024-25, revenue is now expected to be almost $1.8 billion higher than was previously forecast at the time of the 2021-22 Budget.

In the 2012-13 Budget, the ACT Government committed itself to rebalancing its tax base by reducing and eventually eliminating stamp duty over a 20-year period and replacing the shortfall through an increase in the general rates system.

The phasing out of stamp duties and the phasing in of the new general rates system over the course of 20 years is being implemented through a series of four separate stages. We are currently up to stage 3 of the tax reform that commenced in 2021-22 and will go until 2025-26.

However, under stage 3 of tax reform it appears that the reduction in revenue from commercial and residential conveyances will far exceed the increase in general rates as an overall percentage of ACT Government own-source taxation revenue.

Based on the forward revenue estimates in the 2022-23 ACT Budget, the expected increases in general rates by 2025-26 will only make up less than one third of the shortfall in revenue from reductions in commercial and residential conveyance revenue, in turn suggesting the ACT Government is not seeking to replace revenue lost from phasing out reductions in commercial and residential conveyances entirely from increases in general rates.

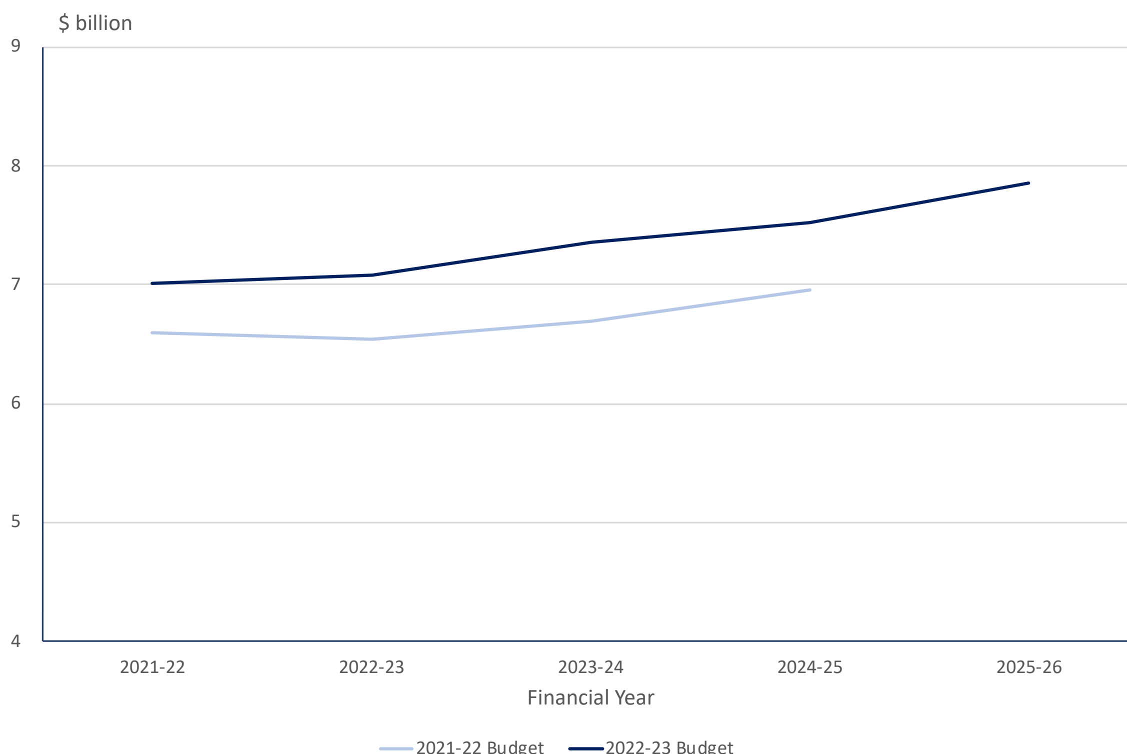
Payroll tax is expected to increase by more than the shortfall in both nominal dollars and as a percentage of total own-source revenue. Other own-source revenue, in aggregate, is forecast to remain roughly constant as a percentage of own-source revenue.

5.1 Overview

ACT revenue is forecast to be some $416 million higher in 2021-22 than previously forecast in the 2021-22 Budget (ACT Government, 2022a, p. 255; 2021a, p. 239). The stronger than anticipated economic recovery in 2021-22 has flowed through into higher-than-expected revenue arising from both own-source revenue and grants from the Commonwealth (ACT Government, 2022a, p. 223).

In turn, revenue is now expected to be $537 million higher in 2022-23 than previously forecast at the time of the 2021-22 Budget. In the three years to 2024-25, revenue is now expected to be almost $1.8 billion higher than was previously forecast at the time of the 2021-22 Budget. This is shown in Figure 13 below.

Figure 13: Forecast ACT Budget Revenue in the 2021-22 ACT Budget and the 2022-22 ACT Budget – 2021-22 to 2025-26 ($ billion)



Source: ACT Government (2022a, p. 255; 2021a, p. 239).

The largest contributors to the increase in revenue in 2021-22 have come from:

- a $179.8 million increase in own-source taxation
- a $129.3 million increase in GST revenue
- a $99.4 million increase in Commonwealth grants
- a $78.9 million increase in gains from contributed assets
- a $76.5 million increase in dividends and tax equivalent payments.

In 2022-23, revenue is expected to increase by $66.3 million over the expected outcome for 2021-22. The largest contributors to the increase in revenue over the expected outcome in 2021-22 will come from:

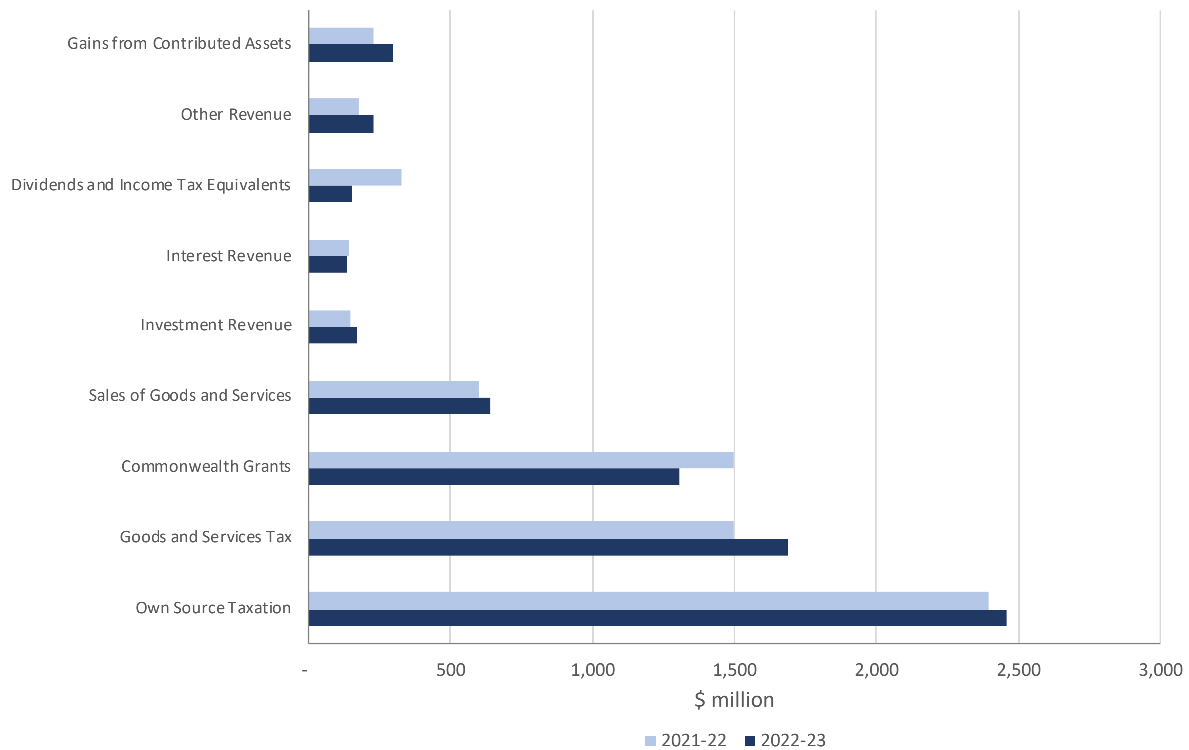
- a $189.9 million increase in GST revenue
- a $61.9 increase in own-source revenue
- a $72.9 million increase in gains from contributed assets
- a $50.2 million increase in other revenue.

These increases in revenue are expected to be partially offset by lower revenue from:

- a $194.3 million reduction in Commonwealth grants
- a $173.1 million reduction in dividends and tax equivalent payments.

A comparison of the revenue forecast outcome for 2021-22 and the revenue forecast for 2022-23 is provided in Figure 14 below.

Figure 14: Revenue Forecast Outcome for 2021-22 and the Revenue Forecast for 2022-23 ($ million)



Source: ACT Government (2022a, p. 225).

5.2 Tax reform and Own Source Revenue

In the 2012-13 Budget, the ACT Government committed itself to rebalancing its tax base through a process of gradually reducing and eventually eliminating various taxes on conveyances (sometimes referred to as stamp duty on the sale of land for residential and commercial purposes) over a 20-year period and replacing the shortfall through an increase in the general rates system. In relation to Conveyance Duty the ACT Government (2012, p. 46) commented at the time:

> *The Government will abolish Conveyance Duty over a 20-year period. Over the next five years, tax rates will be progressively reduced to phase out Conveyance Duty in the longer term.*
>
> *The reduction in the marginal tax rate will focus on the lower tax brackets. …*
>
> *The tax brackets and reduced tax rates will be applicable to both residential and commercial sector transactions.*

In relation to general rates, the ACT Government (2012, p. 47) commented at the time:

> *The Government will improve the progressivity of the General Rates system with the introduction of a number of tax brackets and increasing marginal tax rates.*

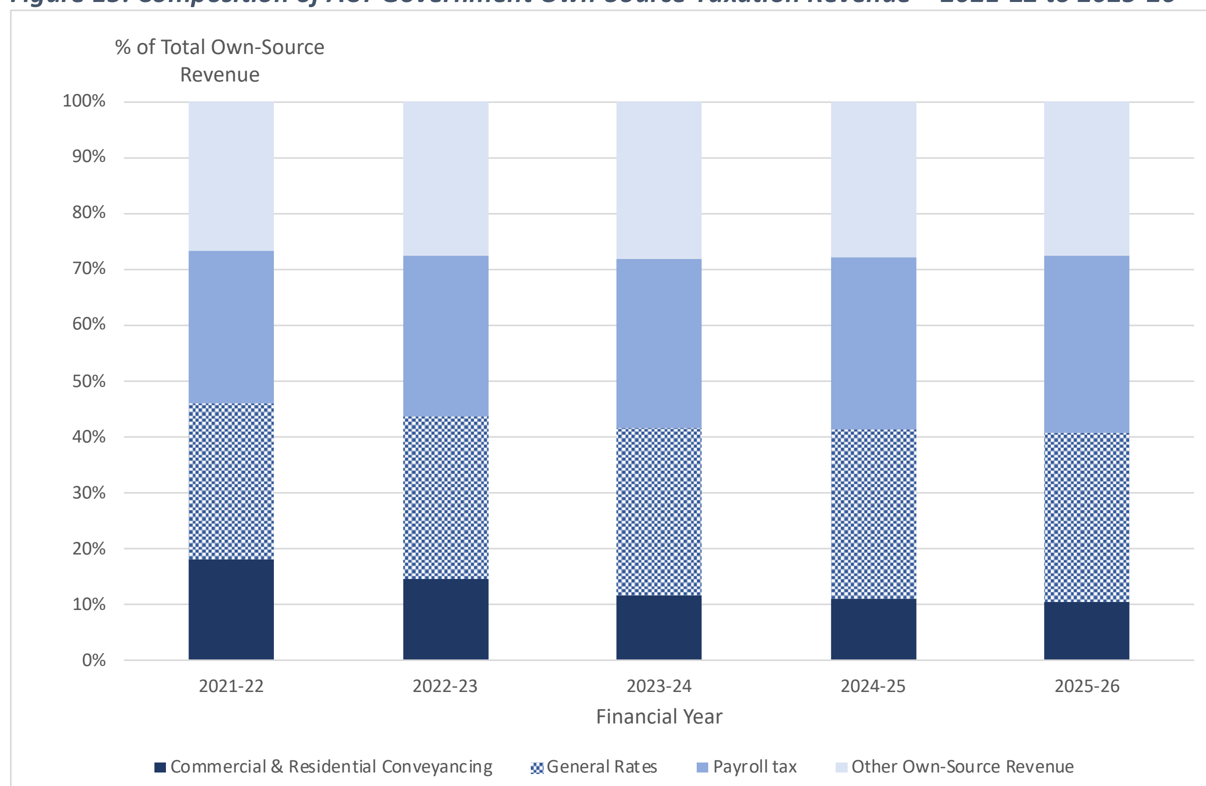
The phasing out of stamp duties and the phasing in of the new general rates system over the course of 20 years is being implemented in four stages to avoid a shock to the property market and to enable the change to be revenue neutral (Reardon & Hopkins, 2018, p. 4). Under stage 3, which commenced in 2021-22 and will run until 2025-26, rates are expected to increase on average by 3.75% per annum (ACT Government, 2021, p. 141).

Consistent with the objectives of the tax reform, the Budget shows own-source taxation revenue from general rates increasing over future years while revenue from commercial and residential

conveyances is contracting. In nominal dollars, the increase in rates exceeds the decline in stamp duties. However, this ignores the growth that could have been expected in both revenue sources over the period without the change in policy. Total own-source revenue is projected to grow by 4.1% per annum over the three forward years and were this rate of increase to apply to revenue from rates they would grow to $805 million in 2025-26 implying an increase of only $32 million when compared with the Budget forecast. Conversely, stamp duties would have been expected to grow to $405 million in 2025-26, so the projected outcome would represent a decline of $116 million once expected growth is taken account.

As a result, when expressed as a percentage of total own-source revenue, the increase in rates is less than the decline in stamp duties as shown in Figure 15 below. Payroll tax is expected to increase by more than the shortfall in both nominal dollars and as a percentage of total own-source revenue. Other own-source revenue, in aggregate, is forecast to remain roughly constant as a percentage of own-source revenue.

Figure 15: Composition of ACT Government Own-Source Taxation Revenue – 2021-22 to 2025-26



Source: ACT Government (2022a, p. 226).

In other words, general rates are not rising quickly enough to replace the amount of revenue lost from changes in commercial and residential conveyance thresholds and rates.

According to the ACT Government (2022a, p. 225), from 2023-24 payroll tax is expected to overtake general rates as the largest source of own-source taxation revenue due to the strength in the labour market and wages growth. By 2025-26, payroll tax is expected to account for 31.7% of own-source taxation revenue, while general rates will account for 30.3%.

Revenue from payroll tax will increase from 27.3% of ACT Government own-source taxation revenue in 2021-22 to 31.7% by 2025-26 – an overall increase of 4.4 percentage points. This is around twice the increase in the percentage of ACT Government own-source taxation revenue collected from general rates over the same period.

Payroll tax is levied on employers. The application of payroll in the ACT, along with all other Australian sub-national jurisdictions, is selective in that it only applies to businesses with a payroll

above a certain threshold. In the ACT, that threshold is $2 million per annum. For firms subject to payroll tax, a flat rate of 6.85% applies in the ACT.

The exemptions in current payroll taxes distort the choices of business structure, organisation and employment, thereby distorting the productive allocation of labour in the economy (Freebairn, Stewart, & Liu, 2015, p. 14). Thresholds exert a downward bias on firm sizes and significant dead-weight losses may arise from these threshold-induced reductions in firm size.

Because payroll taxes are generally levied on all components of employee remuneration, they are designed to tax the value-added from labour (Henry, Harmer, Piggott, Ridout, & Smith, 2009a, p. 293). As such, payroll taxes are similar to the labour component of Australia's personal income tax as well as the goods and services tax — they all generate revenue by reducing the real return from working.

Business organisations often assert that payroll tax is an impost on business rather than a payment by workers (Freebairn, Stewart, & Liu, 2015, p. 14). However, the long-term incidence and distributional effects of a selective payroll tax are very different to the statutory incidence. Large businesses pay the tax to government. The adjustment of the wage cost and of employment mean that most of the tax in a long run equilibrium is passed back to employees of both large and small businesses as a lower market wage than otherwise (or lower rate of wage increase over time). That is, all employees, including those employed by small business, bear most of the payroll tax levied on large business.

5.3 Budget Impact on Cost of Living

The ACT Government (2022a, p. 207) indexes most of its taxes and fees each year in line with the expected wage price index (WPI) outcome for the previous financial year. The ACT Government contends this ensures taxes and fees keep pace with the cost of providing Government services, while remaining affordable. One notable exception to this is increases in general rates that are part of the tax reform discussed above and are set to grow by 3.75% per annum under stage 3.

As a measure of consumer inflation, the CPI for Canberra was running at 6.3% through the year to the end of June 2022, while the WPI is only forecast to increase by 2¾% through the year to the end of June 2022. As the CPI for Canberra has been running significantly higher than the expected increase in the WPI for the ACT, then the ACT Government's tax burden imposed on ACT residents is actually being reduced during 2022-23 in real terms (or inflation adjusted terms). Based on the ACT Government's economic forecasts, this is likely to continue into 2023-24 (even though Pegasus contends the ACT Government's forecast for the Canberra CPI is probably too low).

However, this situation is expected to turnaround in 2024-25 when the WPI for the ACT is expected to exceed the Canberra CPI based on the ACT Government's economic projections. While on average, ACT residents in the workforce should be able to offset ACT Government tax increases indexed to the ACT WPI through wage and salary increases, ACT residents whose primary source of income are social security benefits indexed to the national CPI could be relatively worse-off in real terms. Potentially offsetting this additional impost upon such ACT residents is ACT Government (2022a, p. 203) support for vulnerable households with cost-of-living pressures through the provision of a wide range of concessions to assist with living expenses, including general rates, utility bills, driver licence fees, motor vehicle registration fees, and public transport fares.

5.4 Dividends and Income Tax Equivalents

Total dividends in 2022-23 are expected to be $103.5.0 million, a decrease of $68.4 million from the 2021-22 Budget. Dividends are expected to increase in 2023-24 to $223.7 million, decrease to $195.8 million in 2024-25, and then increase to $227.1 million in 2025-26. The movements in dividends across the years is largely the result of the deferral of land sale settlements from 2020-21

and a bring forward of land sale settlements from future years. In addition, Icon Water dividends are less than expected due to lower water usage and ActewAGL profits are lower due Feed-in-Tariff pricing volatility. Further details of these transactions are provided in Table 7 below.

Table 7: Dividends from ACT Public Trading Enterprises

	2021-22 Est. Outcome $'000	2022-23 Budget $'000	2023-24 Estimate $'000	2024-25 Estimate $'000	2025-26 Estimate $'000
Dividends					
Dividends – Icon Water	37,822	15,559	39,690	53,436	55,842
Dividends – CIT Solutions	500	500	500	500	500
Dividends – City Renewal Authority and Suburban Land Agency	175,057	87,449	183,553	141,889	170,748
Total Dividends	**213,379**	**103,508**	**223,743**	**195,825**	**227,090**

Source: ACT Government (2022a, p. 244).

Tax equivalent revenue is forecast in 2022-23 to be $52.4 million, a decrease of $63.2 million compared to the updated forecast for 2021-22. It is noted that the forecasts increase significantly for 2023-24, taper off for 2024-25 but increase significantly again in 2025-26.

The major driver in relation to dividends and income tax equivalent payments across the out-years is the surge in dividends from the Suburban Land Agency as well as an increase in tax equivalent payments from this same public authority. Specifically, the increases relate to a general increase in the value of land scheduled for settlement and the estimated increase in land sales in Gungahlin and Molonglo.

Generally, there is a case for greater transparency in the presentation and explanation of the flows expected from dividends. In this regard, the ACT Government’s policy in respect to dividends is unclear.

6. Expenditure

Forecast expenses for 2022-23 of $7.8 billion have been held at about the same level as the expected 2021-22 outcome. The forecasts show growth over the period of 7.0% on the estimated outcome for 2021-22, or an annual growth rate of 1.75%. This is a very modest increase given the assumptions for population growth and inflation in the Budget. Expenses are expected to fall as a proportion of GSP over the Budget and forward estimates period.

The Budget Papers set out over $1 billion new spending over four years on Wellbeing initiatives in net terms, including $141 million on housing.

6.1 Overview

Forecast expenses for 2022-23 of $7.8 billion have been held at about the same level as the expected 2021-22 outcome. Expenses are expected to grow to $8.4 billion by 2025-26.

Table 8 sets out the forecasts for aggregate expenses for the budget and forward years.

Table 8: Budget and forecast expenses

	2021-22	2022-23	2023-24	2024-25	2025-26
	Est. Outcome	Budget	Estimate	Estimate	Estimate
	$m	$m	$m	$m	$m
Expenses	**7,806.6**	**7,780.2**	**7,938.2**	**8,076.5**	**8,353.8**

Source: ACT Government (2022a, p. 52).

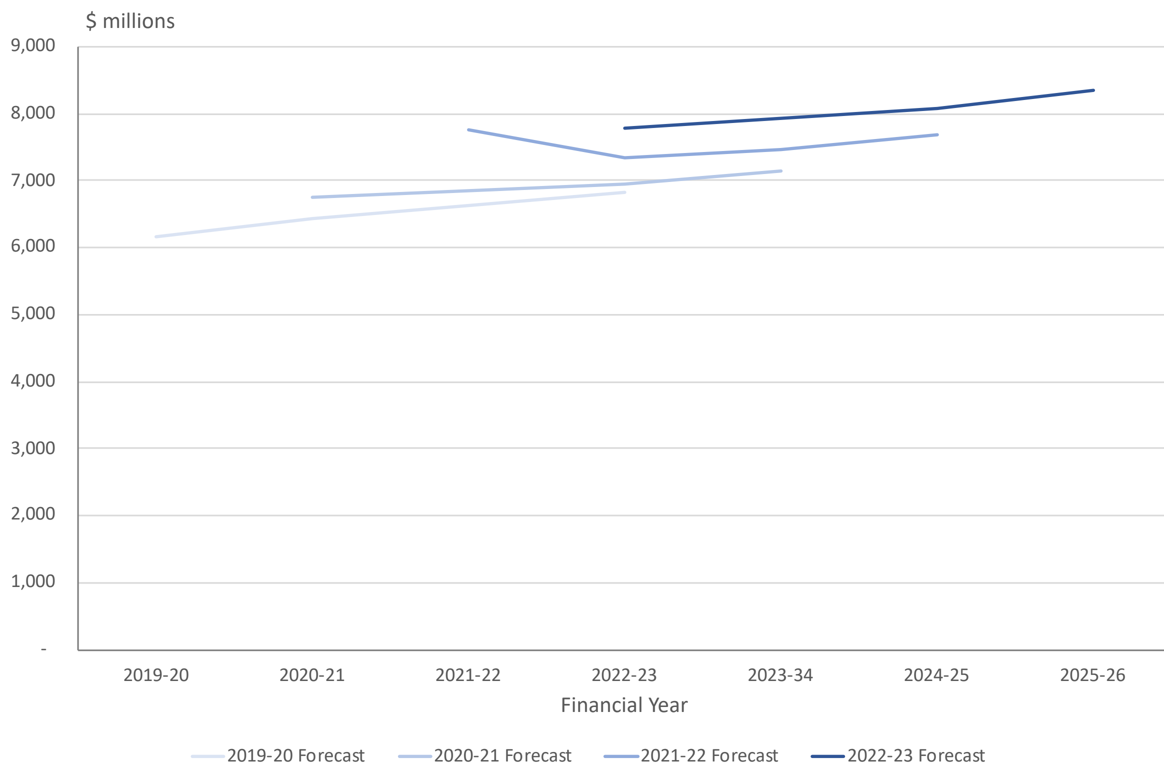
The forecasts show growth over the period of 7.0% on the estimated outcome for 2021-22, or an annual growth rate of 1.75%. This is a very modest increase given the assumptions for population growth and inflation in the Budget. It continues a period of relative restraint on expenses since the 2019-20 Budget, which was interrupted by a peak in 2021-22 related to additional pandemic measures (ACT Government 2022a, p.216).

It remains the case however that expenses in all years are forecast to be higher than set out in the 2021-22 Budget. The main reasons for the change in the forecast level of expenses relative to the last Budget include the effect of changes of new initiatives and changes in underlying volume and price parameters. The main reasons for these changes include:

- Additional funding of $161.9 million ($361 million over three years) for new Wellbeing initiatives in 2022-23
- An increase of $57.3 million in expenses associated with large-scale generation certificates ($184 million over three years)
- An increase of $51.2 million in the superannuation liability expense in 2022-23 ($112 million over three years)
- Higher interest expenses of $17.9 million in 2022-23 ($130 million over three years) due to the impact of higher rates on borrowings (ACT Government 2022a, p.55).

In previous years the ACT Budget had also forecast relatively modest forecasts for expenses that have increased in subsequent Budgets. This is shown in the following chart in which the forecast series shifts upward in each successive year.

Figure 16: Expense forecasts – 2019-20 to 2022-23 Budgets ($ million)



Sources: ACT Government (2019, 2021, 2021a, 2022a).

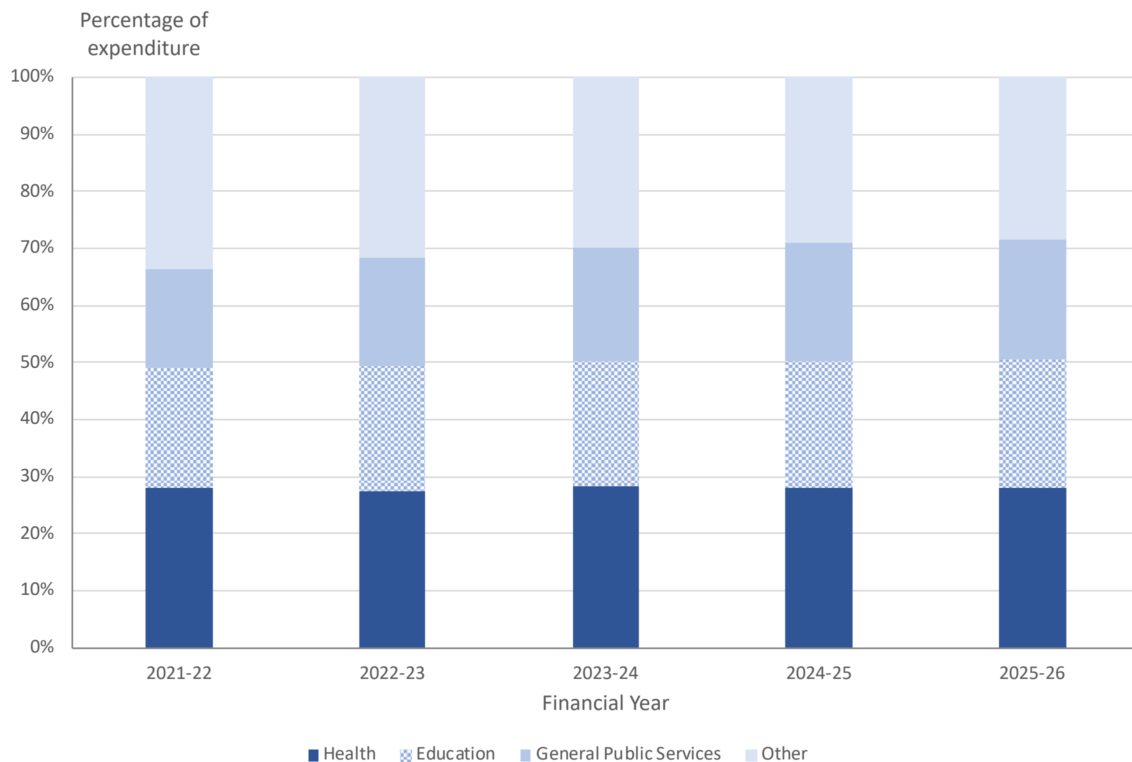
Based on the experience of previous years, the estimates for expenses in the forward years might be expected to be higher in future Budgets.

6.2 Expenses by function

The Budget Papers include at Table 3.4.1 a classification of expenses by the functions through which general governments aim to achieve their socio-economic objectives (ACT Government 2022a, p.217). This classification is widely employed in international systems of Government Finance Statistics and is intended to allow trends in government outlays on functions or purposes to be examined over time (International Monetary Fund, p. 75).

In the ACT, General Government Sector expenses are dominated by spending on health, general public services and education.

Figure 17: Expenses by function – 2021-22 to 2025-26 (per cent)



Source: ACT Government (2022a).

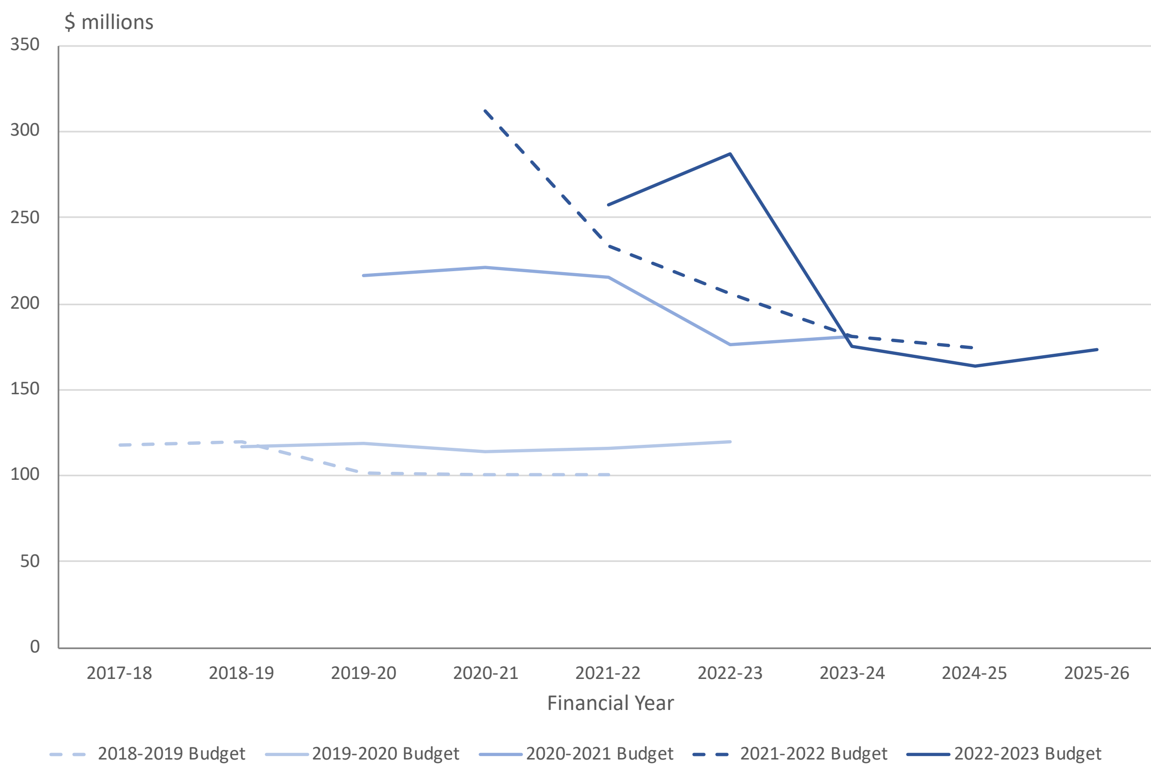
Together, these functions account for around 68% of all government expenses in the 2022-23 Budget. This is consistent with traditional patterns of spending in the ACT.

The major contributions to the growth in expenses across the forward estimates period are in general public services, health and education. Spending on recreation, culture and religion are forecast to be relatively stable.

Forecasts for the environment protection function may justify some further explanation. The Budget Papers show an increase in spending from the estimated 2021-22 outcome to $287.5 million in 2022-23 falling across the forward years to $173.5 million in 2025-26. The forecast decline of over $100 million over the forward years is difficult to understand in terms of the Government's commitment to the environment and the prominence of the environment in the Wellbeing domains.

Figure 18 below sets out the estimated outcomes and forecasts for the environment function for each Budget since 2018-19 (environmental protection was not reported as a separate function prior to 2018-19).

Figure 18: Expenses for Environment Protection function– 2017-18 to 2025-26 ($ million)



Sources: ACT Government (2017, 2018a, 2019, 2021, 2021a, 2022a).

The chart shows declining levels of expenditure in forecasts for the function across all years other than 2019-20. However, the chart also shows that it is usual for successive Budgets to spend more on the function than forecast in the preceding Budget and, in all but one year, to promise more in the Budget year than the previous year's estimated outcome.

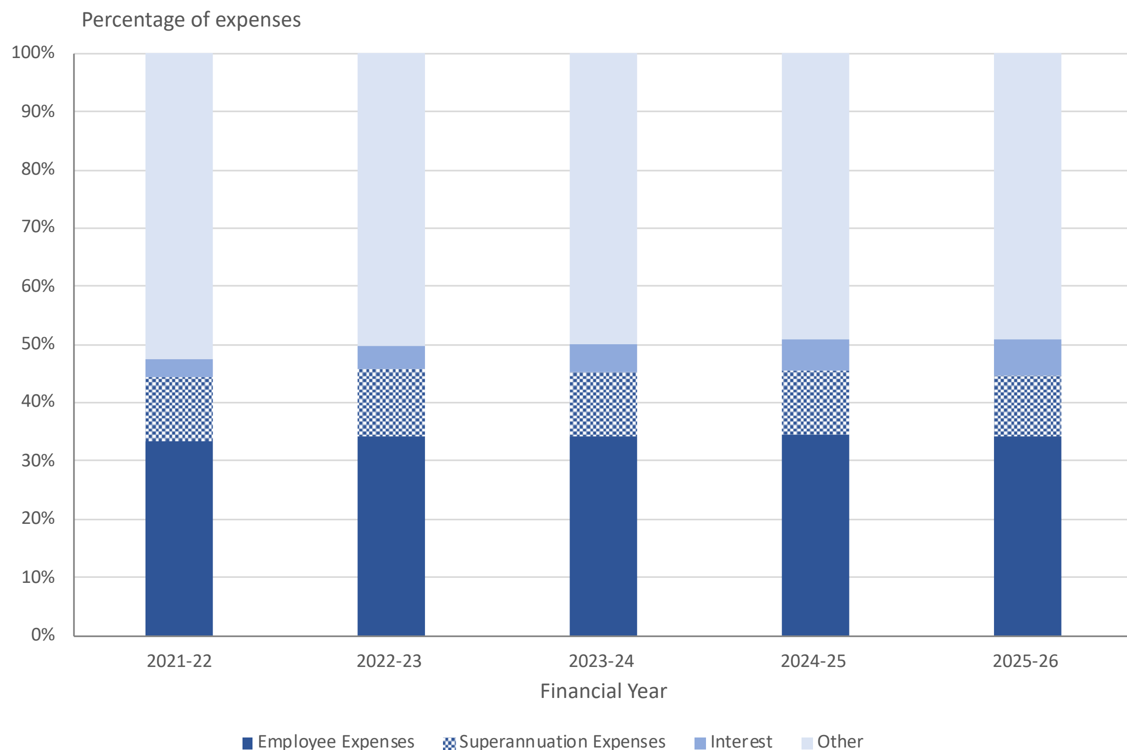
This pattern of spending invites a question as to whether the ACT Government expects to spend less on environment protection in 2023-24 to 2025-26 than any year since 2019 or whether, consistent with the importance attached to environment protection in the Government's priorities and the Wellbeing Framework, expenditure can be expected to increase in future years beyond the forecast levels.

6.3 Operating Expenses

Expenses can also be described in terms of the economic type or purpose of the payment, as shown in Table 3.4.2 (ACT Government 2022, p.218).

Expenses for the ACT Government are dominated by salaries, superannuation and other employee related expenses.

Figure 19: Expenses by economic type – 2021-22 to 2025-26 (per cent)



Source: ACT Government (2022a).

As in previous years, almost half of the expenses relate to employee wages and superannuation (ACT Government, 2022a, p. 217). Salaries and employee expenses are forecast to grow by 2.2% in 2022-23 over the expected outcome for 2021-22 and by around 2.4% per annum on average over the Budget and forward years.

Interest expenses are the cost of borrowing on public debt. Interest expenses are expected to increase by $61.5 million in the 2022-23 Budget from the estimated 2021-22 outcome and to roughly double over the Budget and forward years, from $257.7 million in 2021-22 to $501.7 million in 2025-26. The growth in interest payments reflects the impact of higher interest rates on a higher level of borrowing and is a direct consequence of the Territory's deficit budgeting. In the last year in which the ACT Budget was in surplus, the interest expense was less than $200 million.

The forecast reduction in supplies and services does not account for the recent renewal of the *National Partnership on COVD-19 Response*. Additional revenue and expenses associated with the extension will need to be reflected in the 2022-23 Budget review.

The presentation of expenses by economic type illustrates the extent of the challenges in shifting the budget aggregates. Many of the ACT Government's expenses are "locked in" to the extent that they are made up of payments which are to a large extent not discretionary. Employee related expenses represent half of total expenses. These costs are difficult to move in the short to medium-term. Depreciation and amortisation expenses represent another 7% of the total. Interest expenses on the Territory's borrowings are expected to rise to 6 percent of expenses by 2025-26. These payments are a first call for government spending because if a government does not meet these payments as they fall due it will lose the confidence of financial markets.

Other categories of expenditure are discretionary in a technical sense but as they are more directly related to the level of services provided to the community, there are practical constraints on the

extent to which payments can be reduced in the short to medium term. The amount of lock-in limits the scope for governments to influence the level of public expenditure and the broader fiscal position in the short to medium term.

6.4 Well-being initiatives

The ACT Government is working to embed a Wellbeing Framework within the Budget. Wellbeing concepts are being studied closely by bodies such as the OECD as a means of broadening the measure of community outcomes beyond economic indicators of wealth such as GDP. New Zealand adopted a Wellbeing Budget in 2019. However, the ACT is one of the few administrations to incorporate a Wellbeing Framework into its annual budget.

As part of this process, the 2022-23 ACT Budget presents new spending initiatives in terms of the prime areas (or domains) within the Wellbeing Framework that will be impacted by each initiative.

The Wellbeing Framework has the potential to help target Government investments towards areas of concern to the community and provide additional information on the success of Government activities in contributing to positive social and economic outcomes. However, in its current form, the Wellbeing presentation employed in the Budget is difficult to follow or to reconcile against reporting on Government activities. The Government has provided at page 61 a summary indication of how its priorities and investments map across six categories that are broadly aligned to the Wellbeing domains (ACT Government 2022a, p.61). However, this does not provide a precise reconciliation between the Government's priority areas and the Wellbeing domains.

In some cases, the domains align reasonably closely to the Functions reported in Table 3.4.1 and to existing Government Directorates. In other cases, the domains cut across Functions and several Directorates or agencies may be contributing to different domains. The Budget Papers acknowledge that in practice many initiatives will contribute to multiple Wellbeing domains.

At this stage the Budget documents only allocate new expenditure initiatives to these domains. It is not possible from the Budget documents to determine how much of the Territory's ongoing base funding contributes to each of the domains. Nor is it possible to identify the impact of the Territory's revenue settings on the Wellbeing domains.

The Budget Papers set out over $1 billion new spending on Wellbeing initiatives, net of savings and off-sets. Table 9 below sets out a summary of the new spending initiatives allocated in the Budget Papers to each domain.

Table 9: New initiatives Budget and forecast expenses ($000)

Wellbeing Domain	2022-23	2023-24	2024-25	2025-26
Access and connectivity	-1315	18084	6362	4936
Economy	11669	10701	-2296	-3946
Education and life-long learning	37039	64591	73790	61395
Environment and climate	9378	24324	5540	3094
Governance and institutions	32298	14035	7446	4775
Health	113066	65448	56519	31404
Housing and home	72102	16811	26630	26351
Identity and belonging	12524	42170	23835	19313
Living Standards	1560	0	0	0
Safety	43439	42328	31254	31541
Social connection	4699	10262	1493	1243
Time	4257	2911	5144	5400
Total	**340716**	**311665**	**235717**	**185506**

Source: ACT Government (2022a, pp. 109-200).

Consistent with the general pattern of ACT Government expenditure, the major areas for new investment include Health and Education and life-long learning. However, the Budget Papers also show significant new investments in the Housing and home and Safety domains.

Significant new investments in these domains include:

- Upgrading Canberra Hospital
- Investing in Digital health Record infrastructure
- Development of the Whitlam Primary School and modernisation of Majura Primary School
- Capital investments in new and renewed public housing
- Measures to modernise and upgrade emergency services.

The announced initiatives include some $401 million of savings and offsets, including off-sets of $170 million over four years within the Health Funding Envelope (2022-23 Budget Outlook, Table 3.2.1, page 97).

7. Capital Works and Infrastructure

The Budget includes a substantial major projects, infrastructure and capital works program across the Budget and forward years. It should be noted the Investment Program is over 5 years, out to 2026-27, as distinct to the remaining Budget being over 4 years. The ACT Government will invest $1.4 billion in infrastructure and capital in the ACT in 2022-23 and approximately $7 billion over the next five years. $1.8 billion of the proposed program over the five years is in provisions, with detailed estimates not for publication.

The key projects for 2022-23 include investments in health, new schools in Gungahlin and Molonglo, the big battery, road and bridge works in Molonglo, a new CIT campus and Transport Interchange for Woden, new public housing and public housing renewal and Light Rail expansion. The peak years for infrastructure spending are $1.7 billion in 2023-24 and $1.5 billion in 2024-25, falling to $1.1 billion in 2026-27. Experience suggests that some new capital projects may be deferred and new projects brought on stream in future Budgets.

7.1 Overview

The Budget Papers indicate that the ACT Government (2022a, p. 269) intends to invest $7 billion in infrastructure in the ACT over the next five years to 2026-27.

Table 10 below summarises the infrastructure, capital works and investment program.

Table 10: Summary of investment and capital works program – 2022-23 to 2026-27

	2022-23 Allocation $'000	2023-24 Allocation $'000	2024-25 Allocation $'000	2025-26 Allocation $'000	2026-27 Allocation $'000
New Capital Works	237,406	204,190	163,176	77,984	7,390
Works-in-Progress	891,890	1,034,156	463,280	119,902 74,614	22,633
TOTAL (Including Provisions)	1,274, 385	1,644,425	1,142,736	684,812 229,591	629,608
Infrastructure Investment Provisions	**67,525**	**329,967**	**436,423**	**405224**	**524,680**
Better Infrastructure Fund	**77,564**	**76,112**	**79,857**	**81,702**	**74,905**
TOTAL INFRASTRUCTURE INVESTMENT INCLUDING PROVISIONS	1,358,993	1,654,154	1,527,360	1,372,560	1,110,630

Source: ACT Government. (2022a, p. 269)

7.2 Capital Works Program

The Capital Works Program forms the largest component of the Infrastructure Investment Program, with funding of $974 million in 2022-23 and $5.4 billion over the five years to 2026-27. This includes:

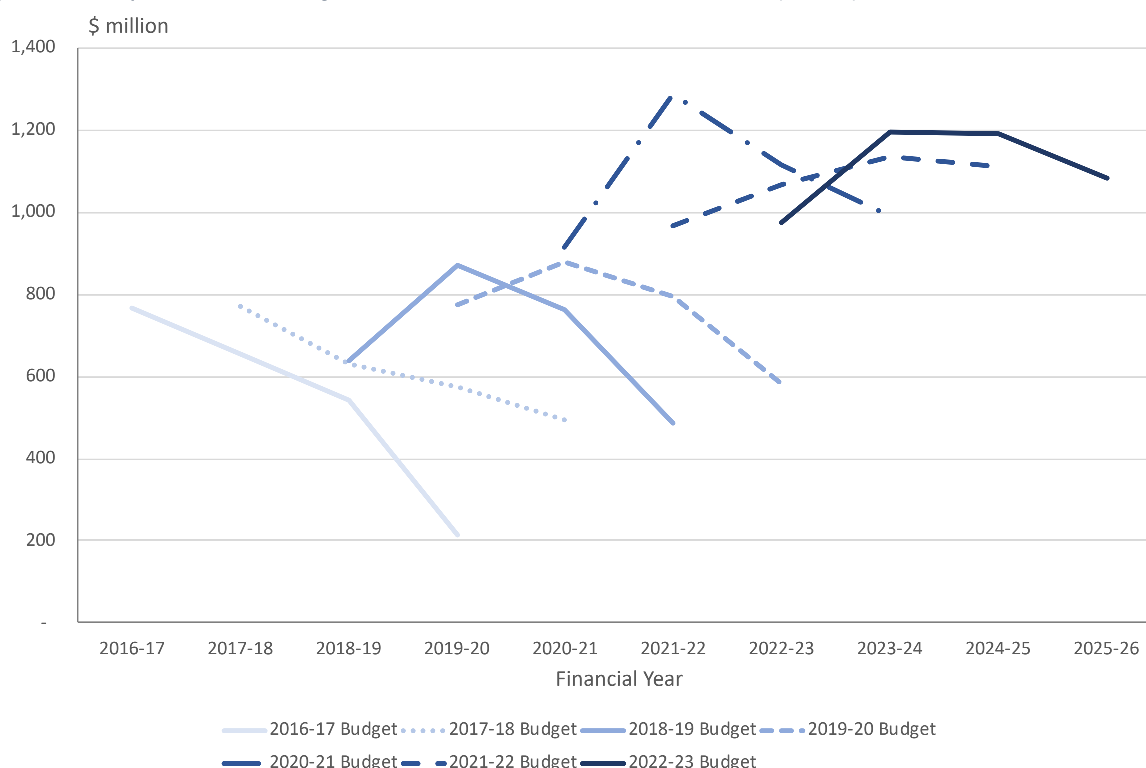
- $237 million in 2022-23 and $690 million over five years for new capital works
- $892 million in 2022-23 and $2.5 billion over five years for works-in-progress
- $78 million in 2022-23 and $390 million over five years for the Better Infrastructure Fund
- $1.8 billion over five years for Central Capital Provisions.

These allocations include; $585 million for health, education and skills infrastructure, $500 million for transport investments, and $200 million for city services infrastructure.

The Capital Delivery Provision has a net zero impact over the five years to 2026-27.

This Budget reflects a significant increase in the capital works program, with a total funding envelope of $5.4 billion over the five years. It is noted, however, the funding tappers off across the last two out years. The ratcheting up of the capital works program forecasts in the last five ACT Budgets is outlined in Figure 20 below.

Figure 20: Capital Works Program Forecasts – 2016-17 to 2023-24 ($'000)



Source: ACT Government (2016, p. 210; 2017, p. 194; 2018a, p. 202; 2019, p. 197; 2021. p. 177; 2021a, p. 280; 2022a, p. 269).

It would appear from the Budget papers that some of the initiatives have been brought forward from previous years, such as the Canberra Hospital Master Plan and John Gorton drive, Molonglo. One consistent pattern in the forward estimates for capital works program forecasts is the eventual decrease in spending across the forward years that is never actually realised. The Committee might wish to inquire of officials how far into the future the planning timeframe for the capital works program extends.

It should be noted, however, the Infrastructure Provisions increases substantially across the four forward years with a total funding envelope of $1.8 billion (Central Capital Provisions). The Central Capital Provisions sets aside funding for significant capital works projects for which budgets are yet to be settle, or which are commercially sensitive. The Capital Delivery Provisions re-profile approximately 24% of the 2022-23 and approximately 27% of the 2023-24 Capital Works Program to the last three out-years.

The key elements of the Capital Works Program for 2023-24 are (Chapter 3.2, ACT Government, 2022a):

Health

- Canberra Hospital Master Plan implementation, $52.4 million
- Digital Health, $50.8 million
- Canberra Hospital Campus, clinical equipment, beds and building services, $37.4 million
- Southside hydrotherapy pool, $8.5 million.

Education

- New public primary school and early childhood care centre, Whitlam (Molonglo), $84.4 million
- Majura Primary School upgrade, $40.5 million
- Margaret Hendry School expansion and a new public high school in Taylor, $33.1 million
- Modern Learning Centres, $8.5 million.

Housing

- Additional public housing repairs and maintenance, $57.3 million
- 140 public housing dwellings, $29.8 million
- Specialist homelessness programs, $7.3 million.

Emergency Services

- New joint services station in Molonglo, $24 million
- Upgrades to ICT network, $$2.6 million.

Transport

- Five intersection upgrades, $7.6 million
- Boboyan Road upgrade, $6.7 million
- Partnership projects with the Commonwealth, $6.2 million
- Umbagong Park bridge replacements, $4.3 million.

Climate

- Progress the Big Canberra Battery, 90 electric buses and environmental friendly appliances under the Vulnerable Household Energy Support Scheme, $95 million.

Communities

- Water retardation at Narrabundah playfields, $11.8 million
- Public swimming pools operations, $11.1 million.

Arts and Culture

- Canberra Theatre expansion and re-development, $62 million.

Most of this funding is allocated across the Budget and three forward years.

7.3 Better Infrastructure Fund

The Better Infrastructure Fund provides Government agencies with an annual funding pool for works that extend the useful life or improve service delivery capacity of infrastructure assets. For 2022-23, the Budget provides $77.4 million for projects. In summary, key allocations include (Appendix B, ACT Government, 2022a):

- Health, $12.5 million
- CIT, $2.99 million
- Cultural, $450 thousand
- Community Service, $447 thousand
- Education, $25.9 million
- Justice, $2.0 million
- Environment, $1.1 million
- Transport, $25.3 million.

7.4 Works-In-Progress

A total of $$895 million is allocated for 2022-23. In summary, key components include (Appendix C, ACT Government, 2022a, pp 323 – 332):

- Health, $56.5 million
- Chief Minister, Treasury and Economic Development, $56.2 million
- City Renewal, $7.1 million
- Education, $125.4 million
- Environment, $12.3 million
- Housing, $23.2 million
- Justice, $37.0 million
- Major Projects Canberra, $332.2 million
- Transport, $164.8 million.

In summary, key projects include; Light Rail phases 2A and 2B, CIT Woden Campus and Interchange, combustible cladding rectification, Canberra Hospital expansion, Northside hospital development and the Canberra Theatre Centre redevelopment, (ACT Government, 2022b, p. 17).

7.5 Major Projects

Major Projects Canberra is responsible for delivering major infrastructure projects and to support other Government agencies deliver infrastructure work programs. For 2022-23 the total Infrastructure investment is $346.4 million, including Work-In-Progress of $332.2 million. Over 2022-23 and the out-years, the key projects include those indicated above in section 6.4 (ACT Government, 2022b, p. 9)

Other major projects include; new primary schools in Molonglo, new high schools in Gungahlin, additional public housing, upgrading existing public housing, planning for build-to-rent affordable accommodation in Gungahlin, completing John Gorton drive Molonglo, duplication of William Hovell drive, upgrading the Monaro highway, delivering the Home of Football in Throsby, delivering the big Canberra Battery, new and improvements to existing emergency services facilities, and updating arts and cultural facilities (ACTGovernment, 2022a, p. 267).

7.6 Light Rail Stages 2A and 2B

The infrastructure program outlined in the Budget includes capital components of the ACT's Light Rail Stages 2A, Raising London Circuit and 2B, Light Rail to Woden.

The investment associated with these projects is set out in the Table 11 below.

Table 11: Public Private Partnerships – Light Rail Stage 2A and 2B – Capital Expenditure Schedule

Project	2022-23 Forecast $'000	2023-24 Forecast $'000	2024-25 Forecast $'000	2025-26 Forecast $'000	Total $'000
Light Rail Stage 2A	**36,899**	**37,027**	**0**	**0**	**73,926**
Light Rail Stage 2B	**50,038**	**0**	**0**	**0**	**50,038**
Total	86,937	37,027	0	0	123,964

Source: ACT Government. (2022b, p. 17)

The infrastructure program includes the capital components (Work-in-Progress) of the ACT's major ongoing public private partnership; Light Rail Stages 2 and 2A. The Light Rail Stage 1 project has been completed. Consequently, it should be noted that Light Rail Stage 1 has been transferred from General Government to the Public Trading Enterprises sector.

It should also be noted that the total project value is identified as "NFP". Pegasus assumes this is because confidential negotiations are underway with the consortia.

Comments on the accounting treatment of the Territory's Light Rail arrangements are provided in section 9.

7.7 ACT Roads

The capital works program provides for a range of planned or work-in-progress road projects.

Capital injections are being provided for projects such as Springvale drive, Owen Dixon drive Southern Cross drive, and road safety improvements and works. Further, the 2022-23 Infrastructure Program includes work-in-progress funding for projects such as, Athllon drive, William Slim duplication, Gundaroo drive duplication, and Monaro highway upgrades.

The Committee asked Pegasus to provide advice on the split between capital funding and maintenance for ACT road funding in the Budget. The Budget papers do not provide a separate focus on road works and projects. In addition, the Budget papers do not separately identify what provision has been made in the Budget or forward years for maintenance of existing and new roads.

7.8 Capital Works Reserve

In 2019 the ACT Government amended the *Financial Management Act 1996* to introduce a new mechanism, the Capital Works Reserve, to allow agencies with multi-year allocations to manage their capital program by advancing funds during the financial year should their capital appropriation be exceeded. Funds drawn from the Reserve will be deducted from the forward estimates for the project(s) concerned in later years. The 2022-23 Budget has allocated $250 million for this Reserve, with unused funds lapsing at the end of the financial year. The Treasurer has to provide the Legislative Assembly with a reconciliation of any amounts approved for payment from the Reserve (under section 26 of the *Financial Management Act 1996*).

As consistent with our previous recommendation, the Committee may wish to investigate the operation, including processes for reporting usage of the reserve. In particular, given this arrangement is an appropriation mechanism, normal arrangements would provide the Assembly with a level of control and assurance over the proper use of this mechanism to ensure appropriate accountability and transparency over the use of funds. In this regard, Pegasus suggests it explores with the ACT Government and officials:

- Criteria established to assess claims on the reserve
- Authority to approve such claims

- Assurance over the usage of the appropriation.

In regard to the latter, the Committee may wish to approach the Auditor-General to review the usage of the Reserve.

8. Assets and Liabilities

8.1 Overview

The Budget Papers indicate a broad continuation of existing trends. While the 2022-23 Budget notes that the Territory's fiscal position is stronger across all key measures than had been projected in 2021-22, forecast trends suggest a general deterioration of the balance sheet over the medium term.

8.2 Net Debt

Net debt is a key balance sheet measure in the Government Finance Statistics framework and in the Uniform Presentation Framework agreed by Treasurers in all Australian jurisdictions as the standard for presentation of information in budget papers.

It represents the sum of deposits held, advances received and borrowings less the sum of cash and deposits, advances paid, investments, loans and placements.[6] The measure of net debt employed by the ACT Budget Papers excludes super liabilities.

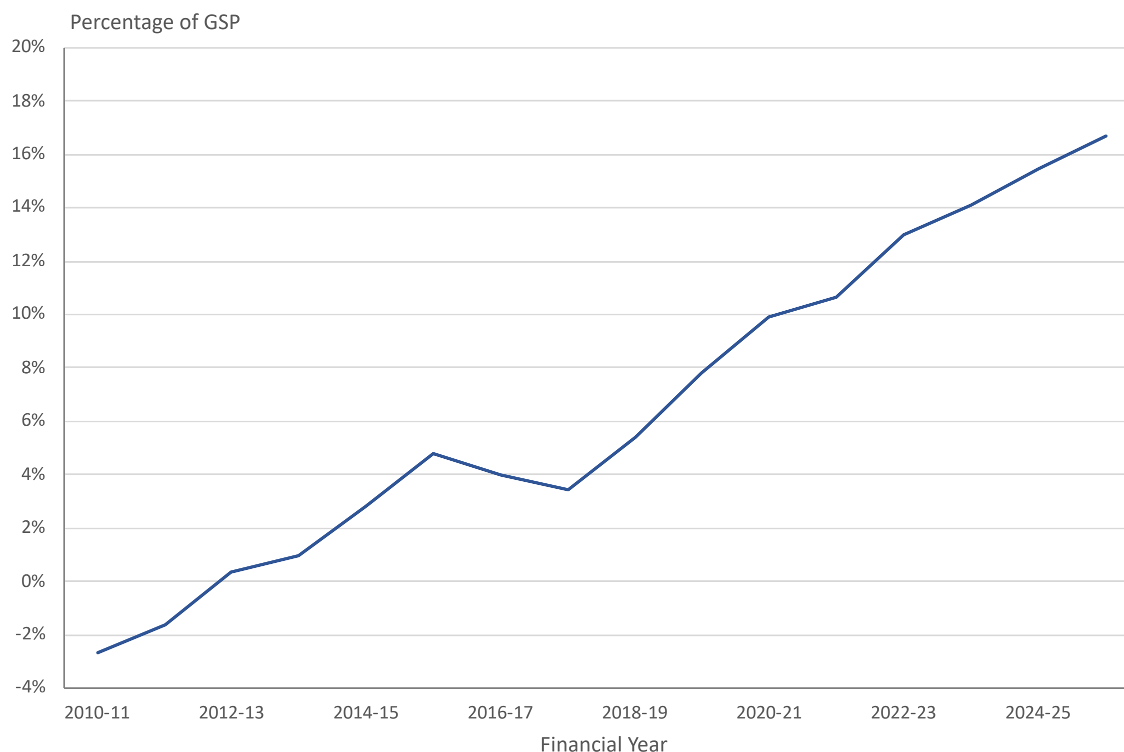
In both absolute and relative terms, the ACT's net debt in 2022-23 is lower than had been forecast in the 2021-22 Budget, but the trend remains persistently upwards: in absolute terms, net debt at the close of the 2025-26 fiscal year is forecast to be nearly double that of the estimated debt for 2021-22.

The ratio of net debt to GSP is a broad indicator of a jurisdiction's ability to meet its debt obligations and its medium-term financial sustainability. The Budget Papers forecast steady growth in the ratio of net debt to GSP in line with the trend since 2017-2018, rising six percentage points to 16.7% by 2025-26, from an estimated value of 10.7% in 2021-22.

Figure 21 illustrates the growth in net debt since 2010-11 as a percentage of the Gross State Product (GSP).

[6] Net debt takes account of gross debt liabilities, which include market and Commonwealth borrowings, and liabilities such as those associated with the impact of public private partnerships such as the Light Rail project, as well as financial assets, such as cash, deposits and investments.

Figure 21: Net debt as a proportion of Gross State Product – 2010-11 to 2025-26 (per cent)



Sources: ABS (2021a), ACT Government (2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018a, 2019, 2021, 2021a, 2022a).

Note: From 2019-20, net debt includes the impact of accounting changes in relation to the treatment of leases. The ACT Government has indicated that for this reason net debt from 2019-20 is not directrly comparable to prior years.

As shown in Figure 21, the ACT Government's net debt has grown steadily over the past decade as a proportion of the Territory's economy, and the ACT has gone from being a net creditor to carrying a substantial debt burden.

The large increase in net debt to GSP in 2015-16 was related to the loan provided by the Commonwealth to support the Asbestos Eradication Scheme and a provision for the Light Rail Stage 1 project. The subsequent reduction in net debt reflected the effect of decisions to procure the Light Rail through a PPP, which removed the requirement to debt fund the capital cost of the project (ACT Government, 2015, p. 251; ACT Government, 2016, p. 288).

However, apart from that adjustment, the ratio of net debt to GSP has consistently increased at a rate of 1-2% a year and is expected to continue to grow up to 2025-26 (Budget 2023. p 285).

The ACT Government's net debt is only partially a consequence of its response to the COVID-19 pandemic: as Figure 21 shows, the change in debt to GSP ratio over the period 2019-2022 is well in line with both prior and projected trends.

A short-term increase in net debt can be a sensible response to adverse economic shocks. However, high levels of continuing debt are undesirable as they impose debt servicing costs and can reduce future budget flexibility.

Australian interest rates are rising. As interest rates continue to rise, the ACT will be faced with higher public debt interest bills.

The Budget Papers do not indicate any long-term strategy for paying down the stock of accumulated debt.

8.3 Net financial liabilities

Net financial liabilities provide a broad measure of the General Government sector's financial obligations to others.

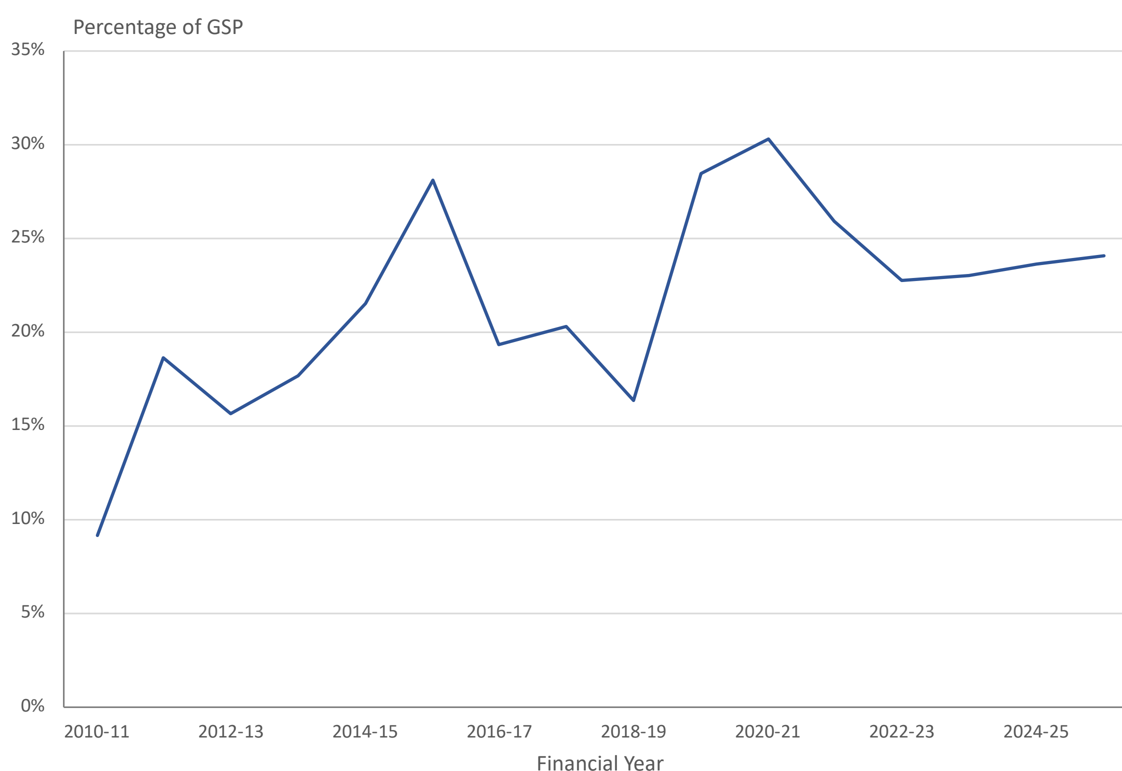
Net financial liabilities are calculated as total liabilities (including net debt and superannuation liabilities) less financial assets (such as cash reserves and investments), excluding the value of equity held by the General Government sector in public corporations. Changes in net financial liabilities are therefore influenced by variations in the net debt figures discussed in the previous section.

The Territory's net financial liabilities have reduced since the 2021-22 Budget but are projected to increase slightly into the out-years. Net financial liabilities for 2022-23 are estimated at $11.4 billion, a reduction of $731 million since 2021-22, and $1.3 billion lower than had been projected for 2022-23 in the previous budget, all significant improvements in balance sheet position. This figure, however, is expected to rise to $14.2 billion by 2025-26.

Relative to GSP, following a sharp drop from 2021-22 to 2022-23, the level of net financial liabilities is forecast to rise gradually into the out-years. The Budget Papers suggest that forecast growth in the ratio of net financial liabilities to GSP over the forward years are related to inflationary trends and changes in the assumptions relating to the discount rate for measuring the superannuation liability.

Figure 22 below illustrates the growth in net financial liabilities since 2010-11 as a proportion of GSP.

Figure 22: Net financial liabilities as a proportion of Gross State Product – 2010-11 to 2025-26 (per cent)



Sources: ABS (2021a), ACT Government (2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018a, 2019, 2021,2021a, 2022a).

Figure 22 shows that while there has been some fluctuation in the ratio of net financial liabilities to GSP over time, the overall trend since 2010 has been upwards.

A spike in 2015-16 was related to a higher forecast superannuation liability and capital provisions to account for some capital projects that were subsequently procured through a PPP (ACT Government,

2016, p. 289). A second spike in 2019-20 largely reflected growth in the superannuation liability, higher borrowings and changes in the accounting treatment of operating leases (ACT Government, 2019, p.295).

Continued growth in the ratio of net financial liabilities to GSP is not desirable in terms of the sustainability of the ACT Government's debt. The ACT Government has in the past argued that its borrowings should be looked at in the context of a growing economy and budget, rather than as absolute figures in isolation (ACT Government, 2019, p.295). Considering rising interest rates and the steady growth in net financial liabilities to GSP shown in Figure 22, this may not be sustainable into the medium and longer term.

8.4 Net worth

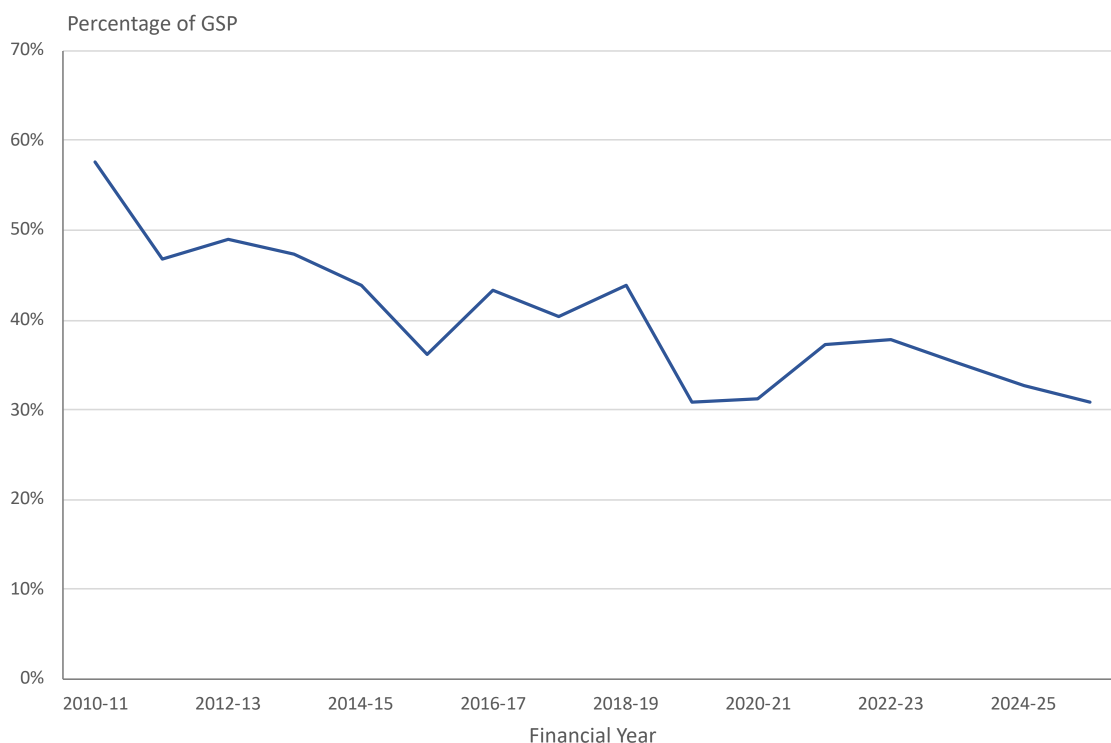
Net worth is an economic measure of wealth that reflects the value of all financial and non-financial assets (such as land, plant and equipment) less liabilities, including superannuation liabilities.

This indicator is often regarded as the best measure of the sustainability and inter-generational equity of a jurisdiction's fiscal position (e.g. Rowles, 1992; AARF, 1995; JCPA, 1995a; Mellor, 1996, cited in Robinson, 1996).

The ACT Government's net worth is positive, and has improved in both absolute and relative terms since 2019-2021. It is, however, projected to decrease into the future.

Figure 23 illustrates the change in net worth as a proportion of GSP since 2010-11.

Figure 23: Net worth as a proportion of Gross State Product – 2010-11 to 2025-26 (per cent)



Sources: ABS (2021a), ACT Government (2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018a, 2019, 2021, 2022).

Figure 23 shows a fairly consistent long-term decline in the ACT Government's net worth expressed as a proportion of GSP. The ACT Government's net worth has fallen from almost 60% of GSP in 2010-11 to 38% in 2022-23 and is forecast to fall to 30.8% by 2025-26.

The Territory's absolute net worth remains high: it was $15.9 billion in 2010-11, is estimated at $19.0 billion for 2022-23, and is only predicted to fall slightly to $18.2 by 2025-2026.

While the Territory maintains a strong net worth in absolute terms, there has been a long-term decline in net worth as a proportion of GSP. In the absence of corrective measures to improve the value of the ACT Government's assets or reduce liabilities, that trend is likely to continue.

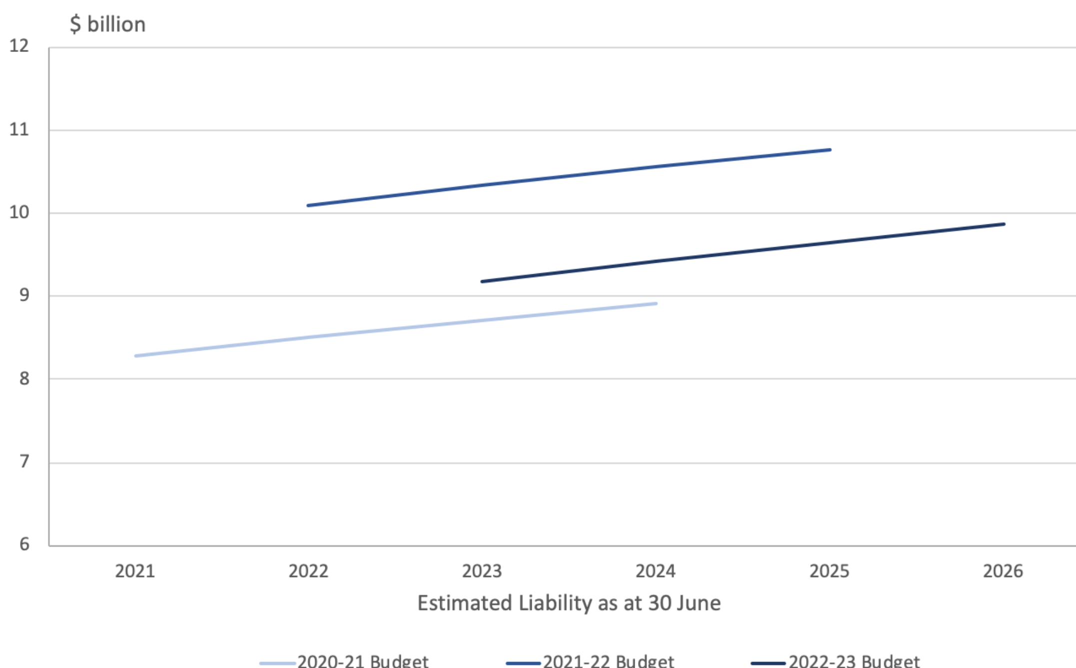
8.5 Superannuation

For new employees since 2005, the Government has made fortnightly payments to each employee's designated superannuation fund under a defined contribution arrangement. There are no associated unfunded liabilities for these employees. However, the ACT continues to carry a significant liability associated with the superannuation entitlements of past and present employees who are members of the Commonwealth defined benefit superannuation schemes, the Commonwealth Superannuation Scheme (CSS) and the Public Sector Superannuation Scheme (PSS).

Approximately 6,000 current employees are members of these schemes. In addition, the ACT has liabilities in the two schemes in relation to a further 29,000 former ACT Government employees, including around 16,000 pensioners. Both the CSS and PSS schemes are closed to new members.

The Territory's estimated defined benefit superannuation liability depends critically upon the discount rate used to calculate the present value of superannuation payments in future years and its relativity to the other financial assumptions regarding future salary growth, pension indexation and crediting rates. Demographic assumptions regarding exit rates and mortality will also impact on the estimated liability. For financial statement reporting, the discount rate is prescribed under the accounting standards (AASB 119) to be the market yield on Government bonds on the reporting date. This changes from year to year and leads to volatility in the estimated liability. For forward estimates, long term financial assumptions are typically adopted to remove this source of volatility. However, different long-term assumptions have been used in each of the last three Budgets resulting in significant changes in the estimated liability, as shown in Figure 24.

Figure 24: Estimated Defined Benefit Superannuation Liabilities



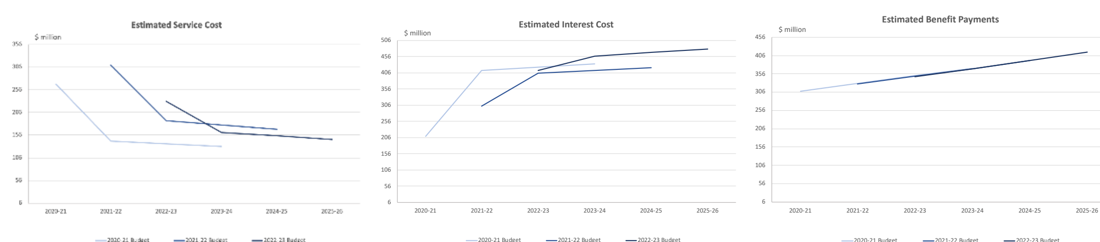
Source: ACT Government (2021, 2021a, 2022a).

This makes it impossible to discern the impact of changes in other assumptions or experience. For example, the most recent actuarial valuation of the CSS and PSS found that redundancies and higher pension take-up rates in the PSS had led to a $3 billion increase in the Commonwealth's estimated

liability as at 30 June 2020 (Mercer Consulting (Australia) Pty Ltd, 2021, p. 16). It is not possible to determine the corresponding effect for the Territory's liability. If the long-term financial assumptions are to be changed from one Budget to the next, it would aid transparency and allow the impact of other changes to be identified if the liabilities were reported both on the new basis and the previous basis. This is particularly important in the current environment where higher than anticipated inflation will impact on actual indexation of pensions and result in an increase in the estimated liability.

The projected service cost (associated with the accrual of employee benefits) and interest cost (due to the unwinding of the discount rate as accrued benefits come closer to payment) are also sensitive to the financial assumptions and have been similarly volatile over the last three Budgets. Projected benefits, however, are expected to change only slowly as experience emerges and assumptions are updated at a triennial actuarial review. This is evident in the three charts shown in Figure 25.

Figure 25: Estimated Defined Benefit Superannuation Flows



Source: ACT Government (2021, 2021a, 2022a).

The large change between the first two points in each of the service cost and interest cost series reflects the difference between the discount rate prescribed for financial reporting and the long-term discount rate. A lower discount rate increases the service cost, as future benefit payments are not as heavily discounted, and reduces the interest cost, as the opening liability is unwound using that lower rate.

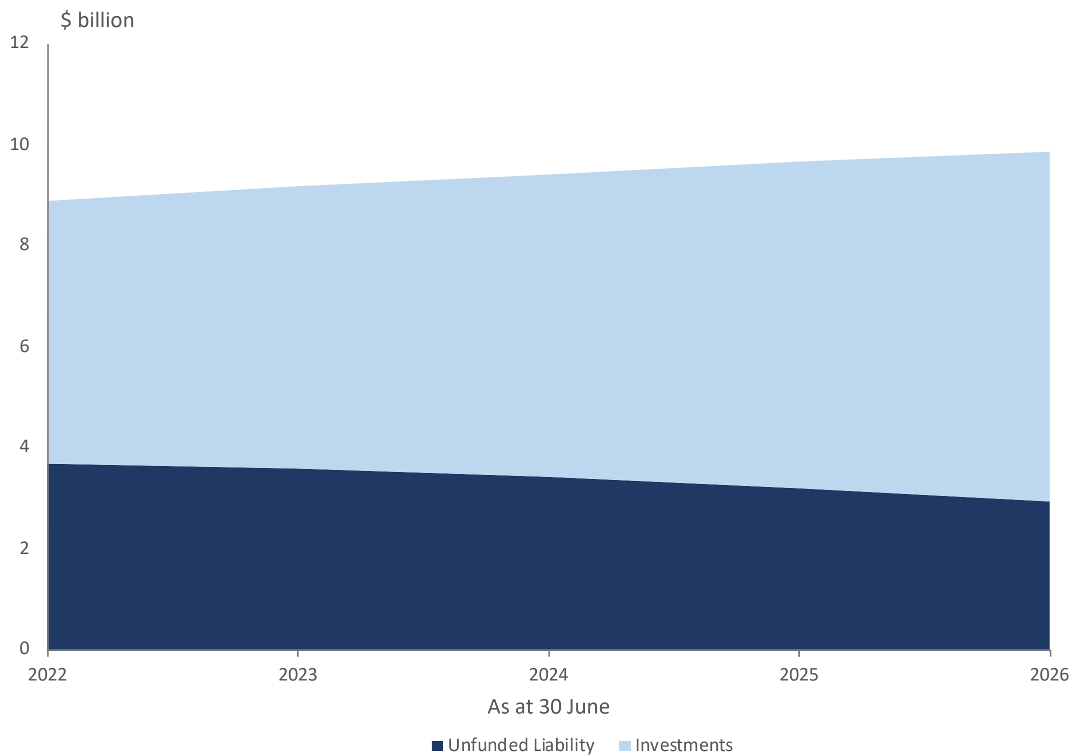
The ACT Government established a Superannuation Provision Account in 1991 as a vehicle for accumulating funds to meet the Territory's unfunded defined benefit superannuation liability. Successive Governments have maintained a commitment to the target of achieving full coverage of liabilities by 2030. In Pegasus to the Legislative Assembly on the 2020-21 Budget (Davey, Fisher, Antcliff, & Kaufmann, 2021), we noted that "without a significant increase in investment returns or additional contributions, the ACT Government seems unlikely to achieve its goal of full funding of the superannuation liability by 2030". Our concerns in this regard remain. The Government now appears to be conscious of this risk, with the meagre investment return achieved in 2021-2022 leading the Government to observe that:

> *Any negative impacts to both future investment earnings and the superannuation liability valuation will increase the likelihood that the timeframe to extinguish the Territory's unfunded superannuation liability will need to be extended. (ACT Government 2022a, p 372)*

Based on the estimate of defined benefit liabilities and the assets in the Superannuation Provision Account as at 30 June 2022 and in the absence of any further contributions, the Account would need to achieve total investment returns of CPI plus 8.2 percentage points over the next eight years to meet the goal of full funding. This compares with the target rate of return of CPI plus 4.75 percentage points and an achieved return of CPI plus 5.2 percentage points over the past 26 financial years. In these circumstances, the prospect of extinguishing the unfunded liability by 2030 appears remote.

If the target rate of return of CPI plus 4.75 percentage points were to be consistently achieved, progress towards full funding would be expected to continue, as shown in Figure 26 ,and we estimate that assets would be sufficient to cover the unfunded liability (estimated using the long-term financial assumptions) in around 13 years. At the same time, we note that the target investment return is above the midpoint of the range mandated for the Commonwealth Government's Future Fund and, given the risks in the Australian and global economic environment in the short to medium term, may not be achieved.

Figure 26: Defined Benefit Superannuation Unfunded Liability and Investment Assets



Source: (ACT Government, 2022a, p. 288 for figures used to estimate the total defined benefit liability as at 30 June 2022 on the long term discount rate, p. 290 for all other estimates).

Despite these reservations, there is no indication that the ACT will have any difficulties in meeting its unfunded superannuation obligations, which will emerge as a requirement to meet benefit payments over a period of more than 50 years. The projections of benefit payments are virtually unchanged from the 2021-22 Budget.

9. Budget accounting, classification and valuation issues

9.1 Overview

The 2022-23 Budget reflects decisions on a number of accounting, classification and valuation issues.

The following sections provide comment on the budget accounting and classification issues that have material impacts on the Budget aggregates and how they are presented.

9.2 Disclosure of Key Accounting Policies

The Budget financial statements, including the budget deficit, and associated tables, are presented in Chapter 4 of the principal Budget Paper (ACT Budget 2023). Section 4.1 relates to the General Government Sector (GGS) and Appendix D includes the financial statements for the ACT's Public Trading Enterprises. Appendix E includes the Total Territory Consolidated Financial Statements, reflecting an accounting consolidation of the GGS and the Public Trading Enterprises. The GGS statements are titled "GFS/GAAP FINANCIAL STATEMENTS" suggesting that Australian Accounting Standards Board (2012) accounting standard AASB 1049 *Whole of Government and General Government Sector Financial Reporting* has been adopted as the key basis for the preparation of the statements. The presentation format of the statements suggests this is the case. AASB 1049, which forms the basis for the Australian Heads of Treasuries Uniform Presentation Framework, requires compliance with all other applicable accounting standards in the preparation of the statements.

In accordance with generally accepted budget reporting principles, Section 4.2 sets out revenues and expenses by function. These tables provide details and a level of granularity of the ACT's revenue streams and expenses across the ACT's key directorate functions.

Appendix D – "Basis of financial statement preparation", (2023, pp. 355- 354) sets out the key accounting bases adopted in the preparation of the Budget financial statements. This section confirms the financial statements have been prepared in accordance with AASB 1049, the Heads of Treasuries Uniform Presentation Framework, which is based on AASB 1049, and where applicable, the ABS Government Finance Statistics framework.

Unlike several other Australian jurisdictions, including the Commonwealth, other than key accounting policies and assumptions adopted in preparing the statements, except in respect to Service Concession Arrangements and Concessional Loans, Appendix G, key underlying accounting policies and assumptions have not been disclosed. In addition, and whilst key revenue streams and key expenses are detailed at sub-section 4.1, as indicated above, there is no disclosure of key assets such as investments and loans, investments in other public sector entities, and produced and non-produced property plant and equipment, nor key liabilities such as advances received, borrowings, superannuation and employee compensation.

Although some of these items, such as liabilities associated with Service Concession Arrangements, are described elsewhere in the Budget Papers, typically the financial statements would be accompanied by a series of notes, describing the accounting policies and assumptions adopted and providing a breakdown of key financial statement items. By way of comparison, some other jurisdictions include a statement of the basis of accounting adopted, significant accounting policies and forecast assumptions and include disclosure of the likely impact of new or amended accounting standards applicable in the future.

Such an approach enhances accountability and transparency for the user/s of the statements.

The Committee may wish to explore with officials a number of issues in relation to the non-disclosure of key accounting policies and assumptions and key balance sheet items, including:

- Why, unlike other Australian jurisdictions, are the bases of accounting, key accounting policies and a disaggregation of key assets and liabilities not disclosed in notes accompanying the financial statement?

9.3 Superannuation return adjustment

As has been the case since 2006-07, the presentation of the headline net operating balance for 2022-23 includes an adjustment for long-term expected superannuation investment earnings.

The Government has argued that a superannuation return adjustment is necessary because, although the Government Finance Statistics (GFS) reporting framework requires the inclusion of superannuation interest costs and other superannuation expenses in the operating balance, it only allows for interest income and dividends to be included as a transactional revenue item in the net operating balance, ignoring the capital growth on the assets in the Superannuation Provision Account (ACT Government, 2016, p. 42).

There is an argument for allowing an offset to the reported interest cost to recognise the fact that the Government is holding assets in the Superannuation Provision Account to meet superannuation liabilities. The combination of an unfunded liability partially offset by assets in the Account can be considered analogous to a partially funded superannuation scheme. In reporting the interest costs for a partially funded superannuation scheme, the assets of the scheme would be netted off the gross liability and the interest cost would arise only on the unfunded component of the liability. This effectively allows for fund assets to earn a rate of return equal to the discount rate.

In the context of the ACT arrangements, the assets in the Account do not directly reduce the unfunded superannuation liability and the ACT Government must report the interest cost on the total unfunded liability, without any recognition of the assets that are held against this liability. In calculating the superannuation return adjustment, however, the ACT Government uses a projected total investment return that is greater than the discount rate used to value the liability. This has the effect of improving the Headline Net Operating Balance beyond the position that would be reported for a partially funded superannuation scheme with the same level of funding. In the Budget year, the use of the projected long-term investment return rather than the long-term valuation discount rate of 5% per annum reduces the headline net operating balance by around $115 million.

In the past we have noted that the return assumption in this adjustment has the potential to materially shift the budget aggregates. In 2018-19, for example, the net operating balance before allowance for the superannuation return adjustment was a deficit of $109 million and the inclusion of a return adjustment of $146 million resulted in a reported surplus in the Headline Net Operating Balance of $37 million. In the current environment, where the Government is running substantial deficits, the superannuation return adjustment acts to reduce the Headline Net Operating Balance, from $794 million to $580 million.

Our report on the 2020-21 Budget commented on the inconsistency in assumptions used in calculating the anticipated returns and the superannuation return adjustment. We note that the current Budget has adopted consistent return assumptions. However, it remains our view that, if a superannuation return adjustment is to be included, it should be calculated on a basis that would effectively replicate the position of a partially funded superannuation scheme. This would mean calculating the adjustment on an assumption that the total return on the assets of the Superannuation Provision Account is identical to the long-term discount rate used in valuing the liability.

9.4 Superannuation liability valuation and service costs

The discount rate used to calculate the present value of the Territory's superannuation liability has a significant impact on the estimated value of the superannuation liability and related superannuation expenses.

It is also important to note that the Budget forecasts for the superannuation liability and associated expenses are calculated using a different discount rate from that used in reporting for the Territory's financial statements. The Budget forecasts use a long-term discount rate while for financial reporting the prevailing Government bond rate is used.

The long-term discount rate utilised in the 2021-22 Budget was 4% per annum, 1 percentage point lower than the rate of 5% per annum which has been used by the Commonwealth Government in the two most recent triennial actuarial reviews (as at 30 June 2017 and 30 June 2020) of the defined benefit schemes giving rise to the Territory's liability. The 2020-21 Budget had used a long-term discount rate of 5% per annum, consistent with the actuarial reviews, but had adopted a lower inflation assumption of 2 % per annum rather than 2.5% per annum. For the 2022-23 Budget, the forecasts have reverted to 5% per annum long term discount rate and have also adopted the inflation assumption used for the triennial actuarial reviews.

Reporting at the end of the financial year in the financial statements is required under the Australian Accounting Standards (AASB 119) to be prepared on the basis of the yield on a suitable Commonwealth Government bond. The liability valuation at 30 June 2022 utilised a discount rate assumption of 3.75% (ACT Government, 2022a, p. 288).

Commonwealth Government bond rates have increased in 2022 but at 3.2% per annum at the time of writing remain well below the valuation discount rate of 5% per annum. It would, therefore, be expected that the reported superannuation liability as at 30 June 2023 will, as in 2022, be higher than the figure forecast in the Budget Papers.

Table J.6 in the Appendices to the Budget Outlook indicates that a 1% decrease in the discount rate from the long-term budget assumption of 5% would increase the estimated liability by almost $1.6 billion.

Table 12: Impact of a 1 percentage point decrease in the discount rate on superannuation liability

	2022-23	2023-24	2024-25	2025-26
	$'000	$'000	$'000	$'000
Superannuation Liability	**+1,595,079**	**+1,612,031**	**+1,624,162**	**+1,631,553**

Source: (ACT Government, 2022a, p. 381)

The lower discount rate will also have an impact on the service cost, which would be expected to be somewhat higher, with an offsetting reduction in the interest cost. Based on the figures reported in the Budget Outlook (ACT Government, 2022, p. 381), the net effect of these adjustments to the service and interest costs is a small increase in the superannuation expense as shown in Table 13 below. The changes in the superannuation expense are not material in the context of the overall liability.

Table 13: Impact of a 1 percentage point decrease in the discount rate on superannuation expense

	2022-23	2023-24	2024-25	2025-26
	$'000	$'000	$'000	$'000
Superannuation Expense	**+22,095**	**+17,164**	**+12,551**	**+8,077**

Source: (ACT Government, 2022a, p. 381)

The application of a higher discount rate to the Budget estimate of the Territory's superannuation liabilities will generally have the effect of decreasing the estimate of the superannuation liability and service costs. There is thus a trade-off between achieving consistency between budget and forward year figures and the need for a subsequent revision of the estimates when the final outcome for the year is known.

9.5 Public Private Partnerships – Service Concession Arrangements

The ACT Government (2022a, pp. 356-357) is currently engaged in two Public Private Partnerships (PPP) projects: Light Rail Stage 1 and the ACT Housing Asset Assistance Program (HAAP).

Pegasus (Davey, Fisher, Antcliff, & Kaufmann, 2021) has previously commented on the accounting treatment of these items in the ACT Budget.

Since the 2020-21 Budget, the ACT Government has adopted the applicable accounting standard, AASB 1059 *Service Concession Arrangements: Grantors*.

AASB 1059 does not treat PPP arrangements as leases, but instead, requires the assets and liabilities to be recognised in the balance sheet and valued at current replacement cost, when the government gains control of these assets and liabilities, generally taken to be when the project becomes operational. Any intangible assets such as intellectual property rights, must be included in the aggregate of project assets. At the end of the construction contracts, the infrastructure will become ACT assets. This is taken to mean that once the projects are operational, the infrastructure is owned by the Territory. It is noted that Light Rail – Stage 1 became operational in April 2019.

Appendix G indicates that in respect to Light Rail – Stage 1 that although the Government will make service payments over the life of the long-term contracts with the consortia, the infrastructure will only become ACT assets at the end of these contracts. It is unclear to Pegasus as to the length of term of these contracts and the schedule for taking these assets and liabilities on to the balance sheets.

It is unclear therefore, as to whether the assets and liabilities associated with Light Rail – Stage 1 have been recognised in the General Government and Consolidated Balance Sheets.

The Committee may wish to explore with officials a number of issues in relation to the accounting treatment in the Budget for Service Concession Arrangements. These include:

- Have the assets and liabilities associated with Light Rail – Stage 1 been recognized?
- If not, what would be the impact on the Budget balances had they been so?

The Committee should note these are complex issues and Pegasus is available should clarification in private, be required.

9.6 Light Rail – Stage 2A Raising London Circuit and Stage 2B To Woden

Reference is made to Budget Statements I, Major Projects Canberra (ACT Government, 2022b, pp. 15-17). It appears there is currently no service concession arrangements associated with these projects, noting funds are being expended.

9.7 Technical Adjustments

The suite of Budget Papers include technical adjustments, which appear to indicate changes to previous decisions relating to the funding of programs and projects. The adjustments appear to move funding across years as well as changes to appropriations across years.

Whilst this is not unusual in other jurisdictions, for instance, the re-phasing of appropriations and the movement of previous decision to out years, the level of adjustments appears substantial.

The Committee may wish to explore with officials:

- The reasons for the substantial number of adjustments; and
- The impact of these adjustments on the out years.

9.8 Discount Rates

Whilst a number of public sector and corporate entities issue bonds as a form of debt financing, the key Australian bond market reference is the Australian Government Bond issuance program. Domestically, and unlike the United States, Europe and the United Kingdom, Australia does not have a deep embedded corporate bond market for the purposes of debt financing. Accordingly, the Australian Accounting Standards require the relevant Australian Government Bond spot rate to prevail as the discount rate valuing long term liabilities, for financial statement purposes. For the forward years, there is more flexibility about the choice of discount rate. As noted in the discussion of superannuation liabilities, the value assigned to the liability depends upon the relativities between the discount rate, assumed wage growth, inflation and fund crediting rates. For the purposes of transparency, it would be helpful if the assumptions adopted in relation to all these variables were disclosed.

It is unclear from the Budget Papers as to what discount rate has been applied to the long-term service concession contracts liabilities, noting as discussed above, it appears no such liabilities have been brought to account.

The Committee may wish to explore what discount rates have been applied as a budget parameter.

9.9 Concessional Loans

Concessional loans are arrangements where a lender, typically a government, provides a loan facility on terms and conditions more favorable than the prevailing market. Concessions can include lower or zero interest rates, interest free periods, and/or an extended maturity term. Appendix G indicates the ACT Government (2022a, pp. 357-358) is providing concessional loans pursuant to its Sustainable Household Scheme and to remediate cladding on private buildings.

The accounting treatment outlined accords with the applicable accounting standard *AASB 9, Financial Instruments*.[7]

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[7] See Australian Accounting Standards Board (2010).

10. Gender Equity in Relation to Expenses and Capital Works

10.1 Introduction

In a meeting between members of the ACT Legislative Assembly's Select Committee on Estimates 2022-2023 and Pegasus consultants on 27 July 2022, it was requested that Pegasus examine issues related to gender equity issues. This section of the report responds to that request.

10.2 Gender Equity in Relation to ACT Government Expenses and Infrastructure Investment Program

Based on detailed data from the labour force survey (Australian Bureau of Statistics, 2022c), Pegasus has identified two major areas of ACT Government expenses where females make up the majority of the workforces (healthcare and social assistance, and preschool and secondary education), and one major area of the infrastructure investment program where males make up the majority of the workforce (construction). This is outlined in Table 14 below.

Table 14: Average Female, Male and Total Employment Levels in the ACT Healthcare and Social Assistance, Preschool and Secondary Education, and Construction Sectors – August 2021 to May 2022

Sector	Female Employment ('000)	Male Employment ('000)	Total Employment ('000)	Percentage Female Employment (%)
Healthcare & Social Assistance	21.8	9.8	31.6	69.0%
Preschool Education	2.0	0.0	2.0	100.0%
Secondary Education	5.9	2.5	8.4	70.4%
Construction	1.4	11.7	13.1	10.6%

Source: ABS (2022c).

The female dominated workforce sectors of health and education are estimated to make up approximately 49.2% of total ACT Government expenses in 2022-23 (ACT Government, 2022a, p. 217). Health is expected to make up 27.4% of total ACT Government expenses in 2022-23 (expenses of $2.1 billion), while education is expected to make up 21.9% of ACT Government expenses in 2022-23 (expenses of $1.7 billion).[8] On the other hand, the male dominated construction is expected to see ACT Government (2022a, p. 269) infrastructure investment program spending of approximately $1.4 billion in 2022-23.[9]

The Women's Budget Statement 2022-23 sets out initiatives in the Budget that support women and girls in the ACT.[10]

[8] Minor discrepancies in the quoted figures are due to rounding.

[9] Composed of an aggregate of construction expenditure in relation to new capital works, works in progress and central capital provisions.

[10] See https://www.treasury.act.gov.au/__data/assets/pdf_file/0003/2051328/Womens-Budget-Statement.pdf.

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