

PART 1

FISCAL STRATEGY AND BUDGET PRIORITIES

This part provides an overview of the fiscal and economic outlook, describes the government's fiscal strategy and outlines the key budget priorities.

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STATEMENT 1: FISCAL STRATEGY AND BUDGET PRIORITIES

Australia's strong economic performance and fiscal management continues to be amongst the best in the developed world. The 2005-06 Budget puts in place major initiatives to sustain this performance, including further income tax cuts and welfare to work reforms, while maintaining strong budget surpluses over the next four years. These initiatives will boost participation in the workforce and increase the productive capacity of the economy over time, thereby enhancing Australia's growth prospects and its capacity to deal with future demographic pressures in a sustainable way.

In this budget the Government will introduce personal income tax cuts worth \$21.7 billion over four years, improving the incentives for all Australian taxpayers to participate in the workforce. The superannuation surcharge will be abolished at a cost of \$2.5 billion over four years, increasing incentives to save and boosting retirement incomes.

Substantive reform of the income support system for people of workforce age will encourage greater workforce participation by those with capacity to work. Obligations to look for work will be applied to a wider range of people, the payment structure will be altered to encourage participation and extra services will be provided to help people to prepare for and stay in work.

The Government will abolish the Tariff Concession Scheme, at a cost of \$1.25 billion over four years, as well as provide other business tax relief aimed at enhancing business investment and Australia's international competitiveness.

This budget also includes measures to address the fiscal sustainability of the health system, particularly through changes to the Medicare Safety Net and the Pharmaceutical Benefits Scheme.

The Australian economy is forecast to continue to grow solidly, with GDP growth forecast to strengthen from around 2 per cent in 2004-05 to 3 per cent in 2005-06. With unemployment at a 28-year low, the economy is set to deliver sustained improvements in Australia's economic wellbeing.

Having met the need for spending in priority areas, an underlying cash surplus of \$8.9 billion is expected in 2005-06, with further surpluses projected for the 3 years following.

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STATEMENT 1: FISCAL STRATEGY AND BUDGET PRIORITIES

FISCAL OUTLOOK

The fiscal outlook for Australia remains very strong, with the Government forecasting its eighth budget surplus. Australia is in a much stronger fiscal position than most comparable economies.

The 2005-06 Budget puts in place a series of major initiatives aimed at sustaining Australia's economic performance, including income tax cuts and the abolition of the Tariff Concession Scheme. The budget also introduces welfare to work reforms which will boost participation in the workforce, increase the productive capacity of the economy and strengthen Australia's fiscal position in preparation for the ageing of the population. The budget outlines arrangements for a Future Fund to make a provision for unfunded liabilities the nation faces, easing the cost of future demographic change.

An underlying cash surplus of \$8.9 billion is expected in 2005-06 compared with an estimated surplus of \$4.5 billion at the *Mid Year Economic and Fiscal Outlook 2004-05* (MYEFO). Underlying cash surpluses continue to be projected across the forward estimates.

Table 1: Budget aggregates

| | Actual | Estimates | | Projections | | |
|---|------------|------------|------------|-------------|------------|------------|
| | 2003-04 | 2004-05 | 2005-06 | 2006-07 | 2007-08 | 2008-09 |
| Underlying cash balance (\$b)(a) | 8.0 | 9.2 | 8.9 | 7.9 | 8.5 | 9.3 |
| Per cent of GDP | 1.0 | 1.1 | 1.0 | 0.8 | 0.8 | 0.9 |
| Fiscal balance (\$b) | 4.8 | 7.0 | 7.4 | 7.5 | 8.0 | 9.0 |
| Per cent of GDP | 0.6 | 0.8 | 0.8 | 0.8 | 0.8 | 0.9 |

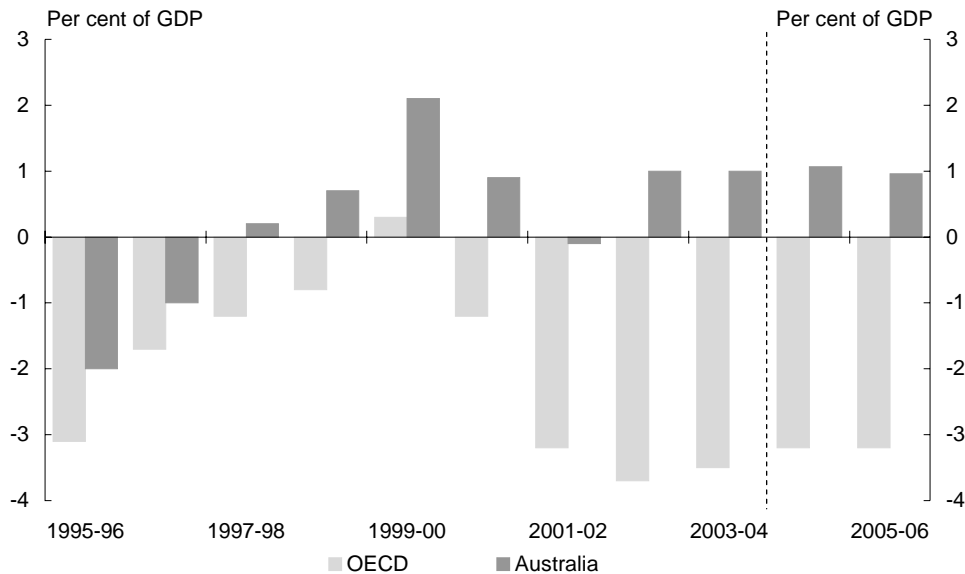
(a) Excludes expected Future Fund earnings from 2005-06 onwards. For further explanation refer to Statement 2 Box 1 and Statement 8.

Expected Future Fund earnings are excluded from the underlying cash balance. This recognises that these resources are not available for recurrent spending, instead being pre-committed to fund existing liabilities. This represents a tightening of fiscal policy.

In accrual terms, a fiscal surplus of \$7.4 billion is now expected for 2005-06 compared to a surplus of \$3.5 billion estimated at MYEFO.

Australia's very strong fiscal position compared to OECD countries is highlighted in Chart 1. The fiscal position amongst OECD countries, on average, is expected to remain in deficit in 2005-06 and 2006-07, notwithstanding strong global growth.

Chart 1: International comparison of budget balances



Source: OECD Economic Outlook 76 November 2004 and Budget Paper No. 1, *Budget Strategy and Outlook 2005-06*.

ECONOMIC OUTLOOK

The outlook for the Australian economy is for solid output growth, low unemployment and moderate inflation. In year-average terms, GDP growth is forecast to strengthen from around 2 per cent in 2004-05 to 3 per cent in 2005-06. Australia will continue to benefit from higher terms of trade in 2005-06. Strong world demand has resulted in substantial increases in contract prices for some of Australia's bulk commodity exports. These high export prices will result in strong growth in national income through 2005-06.

The combination of solid output growth, moderate inflation and a 28-year low in unemployment provides a sound platform for further sustained improvement in Australia's economic wellbeing.

Table 2: Major economic parameters (percentage change from previous year)

| | Forecasts | | Projections | | |
|---------------|-----------|---------|-------------|---------|---------|
| | 2004-05 | 2005-06 | 2006-07 | 2007-08 | 2008-09 |
| Real GDP | 2 | 3 | 3 1/2 | 3 1/2 | 3 1/4 |
| Employment(a) | 2 3/4 | 1 3/4 | 1 1/2 | 1 1/2 | 1 1/4 |
| Wages(b) | 3 3/4 | 4 | 3 3/4 | 3 3/4 | 4 |
| CPI | 2 1/2 | 2 3/4 | 2 1/2 | 2 1/2 | 2 1/2 |

(a) Labour Force Survey.

(b) Wage Price Index.

Source: Australian Bureau of Statistics (ABS) Cat. No 5206.0, 6202.0, 6401.0, 6345.0 and Treasury.

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Table 2 presents the major economic parameters used in preparing the budget. The parameters for 2004-05 and 2005-06 are forecasts while those for 2006-07, 2007-08 and 2008-09 are projections.

Projections for 2008-09 incorporate an employment growth assumption that has been adjusted down by $\frac{1}{4}$ of a percentage point. This reflects, for the first time, the anticipated decline in labour market participation as the population ages and some 'baby boomers' start to retire. The downward adjustment to employment brings projected GDP growth down to $3\frac{1}{4}$ per cent in 2008-09. Real GDP projections and updated analysis of labour force projections from the Intergenerational Report 2002-03 are discussed in Box 6 of Statement 3.

The nominal GDP projections incorporate a technical assumption that commodity prices will return progressively to their long-run average level. This technical assumption recognises the probability that present historically high commodity prices will not persist as world supply expands. The technical assumption has the effect of reducing nominal GDP growth in 2006-07 and 2007-08. Real GDP growth projections for these years are unchanged. The assumptions underlying the nominal GDP projections are discussed in more detail in Box 7 of Statement 3.

FISCAL STRATEGY

The Government's medium-term fiscal strategy is an integral part of the economic management framework designed to deliver sustainable economic growth, rising employment and higher living standards.

A medium-term approach to fiscal policy

The primary objective of the medium-term fiscal strategy is to maintain budget balance, on average, over the course of the economic cycle. This helps deliver macroeconomic stability, encourages private investment in a low interest rate environment, entrenches low public debt and ensures that, over time, the current account reflects private saving and investment decisions.

The Government's medium-term fiscal strategy has a number of supplementary objectives, including: maintaining budget surpluses over the forward estimates period while growth prospects are sound; not increasing the overall tax burden from 1996-97 levels; and improving the Australian Government's net worth position over the medium to longer-term. The supplementary objective of no increase in the overall tax burden means that the Government achieves budget balance over the cycle through a disciplined and prioritised approach to spending and not by recourse to increased taxation.

Central to the Government's objective of improving net worth is the establishment of the Future Fund, dedicated to funding the public sector superannuation liability – the largest liability on the balance sheet, currently valued at \$91 billion. To ensure that

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government saving will grow sufficiently to meet future superannuation payments, expected Fund earnings are excluded from the underlying cash balance. This means that the Fund's earnings are not available for recurrent spending and will contribute to improving the Government's net worth over time.

Consistent with the Government's fiscal strategy, this budget delivers another substantial surplus in 2005-06 and further surpluses over the medium term. This will help contain inflationary pressures in the economy, thus supporting a low interest rate environment, and will add to national savings.

The surplus in 2005-06 is larger than envisaged at the time of MYEFO, supported by recent unexpected increases in commodity export prices. Larger surpluses mean that the Government is saving some of the additional income Australia is earning from the rest of the world.

A decade of sound economic management has enabled Australia to make the most of its opportunities in the global economy. The Government remains committed to ensuring strong economic outcomes are sustained. It is appropriate that the Government take a prudent approach to fiscal policy, particularly as national income is currently being boosted as a result of higher commodity prices which are not expected to be permanent. This prudent approach ensures public finances will be well-positioned to meet future challenges, including those flowing from demographic change and the increasing demand for high-quality health care.

The Government has a strong record of fiscal sustainability, having already delivered a major reduction in the level of general government net debt. Australia now has one of the lowest levels of net debt in the OECD (Chart 2).

Chart 2: General government net debt levels in selected countries (1997 to 2006)



Source: International data are sourced from OECD Economic Outlook 76 December 2004. Australian data are sourced from Statement 12. All data are for the total general government sector.

BUDGET STRATEGY AND PRIORITIES

The Government's budget strategy seeks to foster a prosperous and secure environment where all members of society have opportunities to contribute to the community and to share in the rewards of responsible economic management.

To ensure the Australian economy can continue to deliver sustainable economic growth, rising employment and higher living standards, this budget focuses on:

- continued responsible economic management, including strong surpluses in each of the next four years and measures to prevent costly burdens being placed on future generations (ensuring fiscal sustainability);
- increasing incentives to work and save and addressing impediments that prevent people who are capable of working from engaging in the labour market (increasing workforce participation); and
- implementing policies that increase the productive capacity of the economy (enhancing productivity).

Income tax cuts and increased funding on major health and aged care priorities will improve the wellbeing of Australians today. However, this budget also addresses the challenges to Australia's prosperity over the decades ahead.

The Government's *Intergenerational Report 2002-03* discussed how, over the next 40 years, the proportion of our population aged 65 or more will double while the population of workforce age will grow by just 14 per cent. The *Intergenerational Report 2002-03* noted that pressures in key areas of government spending – notably health, aged care and pensions – could give rise to a 'fiscal gap' of around 5 per cent of GDP in the absence of policy change.

The recent Productivity Commission report on *Economic Implications of an Ageing Australia* (March 2005) reinforced the findings of the *Intergenerational Report 2002-03*, noting that fiscal pressures arising from an ageing population will fall predominantly in areas of Australian Government, rather than State Government, responsibility. Policy responses will need to focus on enhancing both workforce participation and productivity in order to generate the economic growth needed to meet these fiscal pressures, without raising taxes as a proportion of GDP.

The demographic pressures identified in the *Intergenerational Report 2002-03* are starting to be felt during this budget period. Economic growth projections for 2008-09 have been adjusted down by one quarter of a percentage point as a result of the ageing of the population.

Further steps need to be taken now to address the demographic challenge to Australia's growth prospects. This budget makes an important contribution to

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preparing Australia to meet the demographic pressures we face. It does so within a continued framework of responsible fiscal management, delivering this Government's eighth budget surplus.

This budget demonstrates the Government's commitment to facilitating jobs growth, through welfare to work reforms, work incentives through tax relief for individuals and Australian businesses and funding to further build Australia's vocational skill base.

These measures build on the substantial reforms in the 2004-05 Budget which boosted retirement savings, provided substantial assistance to families, delivered tax cuts to improve the rewards from work, and made substantial investments to build longer-term capacity through support for science and innovation and investment in land transport infrastructure.

Personal income tax reform and family assistance

The Government is introducing personal income tax cuts worth \$21.7 billion over four years. The tax cuts will improve the incentives for all Australian taxpayers to participate in the workforce. They will also improve the international competitiveness of Australia's personal income tax system by substantially raising the thresholds for the top two marginal tax rates.

From 1 July 2005, the following changes will be made to the personal income tax scale:

- the lowest marginal tax rate will be reduced from 17 per cent to 15 per cent; and
- the 42 per cent threshold will increase to \$63,001 and the 47 per cent threshold will increase to \$95,001.

From 1 July 2006, further reductions in personal income tax will be provided as follows:

- the 42 per cent threshold will increase to \$70,001 and the 47 per cent threshold will increase to \$125,001.

Table 3: New personal tax rates

| Current tax thresholds | Tax rate | New tax threshold from 1 July 2005 | Tax rate | New tax thresholds from 1 July 2006 | Tax rate |
|------------------------|----------|---------------------------------------|-----------|--|-----------|
| Income range (\$) | % | Income range (\$) | % | Income range (\$) | % |
| 0 - 6,000 | 0 | 0 - 6,000 | 0 | 0 - 6,000 | 0 |
| 6,001 - 21,600 | 17 | 6,001 - 21,600 | 15 | 6,001 - 21,600 | 15 |
| 21,601 - 58,000 | 30 | 21,601 - 63,000 | 30 | 21,601 - 70,000 | 30 |
| 58,001 - 70,000 | 42 | 63,001 - 95,000 | 42 | 70,001 - 125,000 | 42 |
| 70,001 + | 47 | 95,001 + | 47 | 125,001 + | 47 |

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The reduction in the 17 per cent marginal tax rate to 15 per cent will improve the rewards from participating in the workforce for lower income earners. Moving the 42 per cent threshold up to \$70,001 means more than 80 per cent of taxpayers will face a top marginal tax rate of 30 per cent or lower over the forward estimates period.

Senior Australians will also benefit. At present, senior Australians eligible for the Senior Australians Tax Offset and the low income tax offset pay no tax up to an annual income of \$20,500 for singles and up to \$33,612 for couples (depending on the income earned by each member of the couple). The tax cuts will lift these income levels up to \$21,968 for singles and \$36,494 for couples, and the Government will ensure that the offset will only phase out once income exceeds the effective tax free threshold for each single person or member of a couple. The Medicare levy thresholds that apply to senior Australians will also be increased to ensure that they do not pay the Medicare levy until they begin to incur an income tax liability.

These benefits to senior Australians are in addition to the Mature Age Worker Tax Offset announced since last budget, which provides a tax offset of up to \$500 to workers 55 years of age and older, at a cost of \$1.9 billion over four years from 2005-06.

These tax cuts build on the reforms delivered through *The New Tax System* (July 2000), and in the 2003-04 and 2004-05 Budgets. The combined effect of these tax reforms has been to deliver significant reductions in tax for all Australian taxpayers.

- Taxpayers earning \$25,000 paid \$4,521 in income tax prior to *The New Tax System* (excluding the Medicare levy) whereas taxpayers on that income will, from 1 July 2005, only pay \$3,261; a reduction of around 28 per cent.
- Taxpayers on \$60,000 paid \$18,801 in tax prior to *The New Tax System* (excluding the Medicare levy), compared with \$13,860, from 1 July 2005; a reduction of around 26 per cent.
- Taxpayers on \$90,000 paid \$32,902 in tax prior to *The New Tax System* (excluding the Medicare levy), whereas from 1 July 2006 they will pay only \$25,260, a reduction of around 23 per cent.

Chart 3 below shows the percentage reductions in tax that have been delivered by the Government, over a range of taxable incomes.

Chart 3: Income tax savings since *The New Tax System*

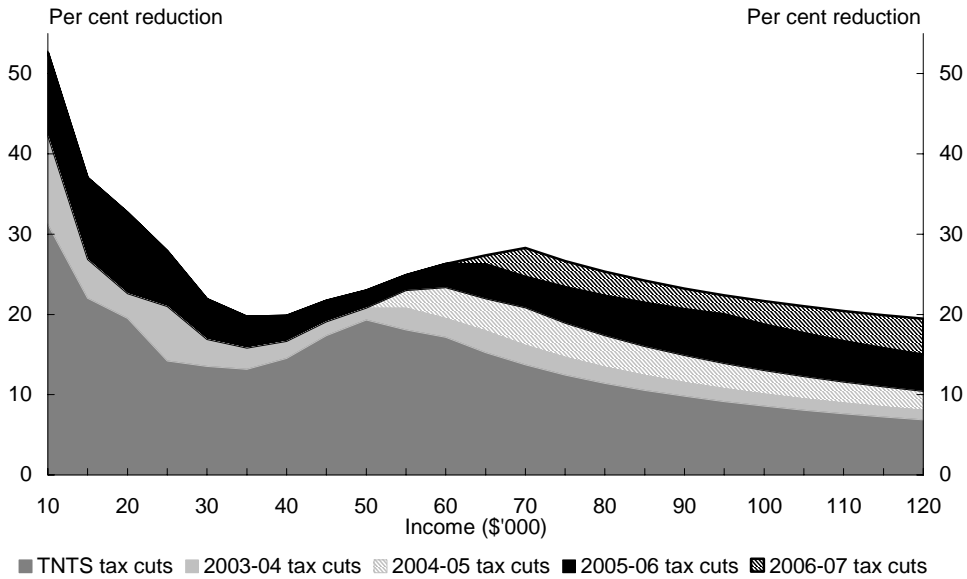
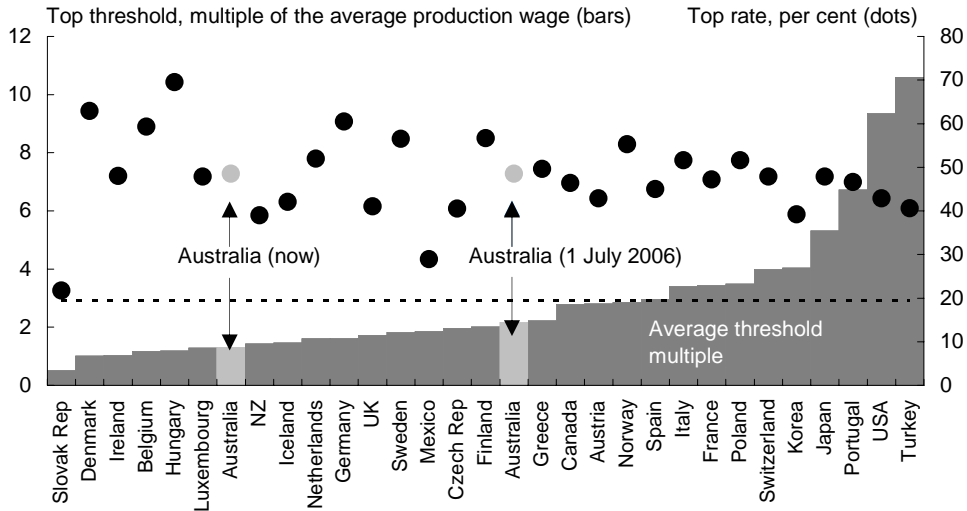


Chart 4 below shows how Australia's top income tax threshold will rise to more than twice the average production wage (a means of comparing earnings on an international basis). The substantial increase in the top threshold significantly improves Australia's position amongst the OECD countries.

Chart 4: Comparison of top tax rates and thresholds across the OECD^(a)



(b) The average production wage is the full-time wage of a worker in the manufacturing sector.
Source: Based on OECD data.

From 1 July 2006, taxpayers will not face the top marginal tax rate until they earn over \$125,000. This means that the top marginal tax rate will apply to only 3 per cent of taxpayers from 2006-07.

Increased assistance for families and carers

This budget also provides extra assistance for Australian families.

From 1 July 2006, the level of family income allowed before Family Tax Benefit Part A starts to be withdrawn will be increased to \$37,500 a year. This will assist over 400,000 families, providing increased assistance of up to \$12.55 a week.

This measure builds on the substantial increases in family assistance provided in the last budget, as well as further enhancements announced since last budget through a \$300 increase in the maximum rate of Family Tax Benefit Part B, and the introduction of the 30 per cent Child Care Tax Rebate.

The Government will provide \$317 million for a one-off carer bonus to be paid to eligible carers in June 2005 in recognition of their role of carer for a person with a disability. Recipients of Carer Payment will receive a \$1,000 bonus payment. Recipients of Carer Allowance will receive a \$600 bonus payment for each eligible care receiver. The bonus will be tax free and not treated as income when calculating social security payments.

Improving retirement incomes

The Government assists people to improve their retirement income by encouraging them to make additional voluntary superannuation contributions. In the 2004-05 Budget, the Government significantly increased the co-contribution matching rate from 100 to 150 per cent and raised the qualifying income threshold. More people are now eligible for a co-contribution. This measure has particularly benefited low and middle income earners. The maximum superannuation surcharge rate has also been gradually reduced from its original 15 per cent.

As part of this budget the superannuation surcharge will be abolished for superannuation contributions made from 1 July 2005. This will increase retirement savings for people affected by the surcharge and increase incentives to make additional contributions, at a cost of \$2.5 billion over four years.

A more sustainable welfare system

This budget incorporates a comprehensive rebalancing of Australia's welfare system to make it more sustainable and to encourage increased workforce participation for those with the capacity to work. The changes recognise the importance of paid employment, whether full-time or part-time, to Australia's prosperity and each individual's own wellbeing.

More people required to look for work, and enhanced Newstart Allowance

Parents receiving Parenting Payment prior to 1 July 2006 will be able to remain on that payment under the current entitlement; that is, until their youngest child turns 16. This group of parents will have a year to seek work voluntarily from the later of 1 July 2006 or when their youngest child turns six. After that they will become subject to an obligation to seek part-time work of at least 15 hours per week.

Parents applying for Parenting Payment on or after 1 July 2006 will receive Parenting Payment while their youngest child is less than six years old. When their youngest child turns 6, this group of parents will receive enhanced Newstart and be subject to an obligation to seek part-time work of at least 15 hours per week.

The new payment and obligations arrangements

| Income support recipient | | Obligation | Payment |
|--|---|--------------------------|---|
| Parent, youngest child aged under 6 | Existing recipient (on 30 June 2006) | None | Parenting Payment (single or partnered) |
| | New applicant ^(a) (from 1 July 2006) | None | Parenting Payment (single or partnered) |
| Parent, youngest child aged 6 or over | Existing recipient (on 30 June 2006) | Part-time ^(b) | Parenting Payment (single or partnered) |
| | New applicant (from 1 July 2006) | Part-time | Enhanced Newstart Allowance |
| Person with disabilities, capable of working 15-29 hours per week | Existing recipient (on 10 May 2005) | None | Disability Support Pension |
| | New applicant (11 May 2005 to 30 June 2006) | None ^(c) | Disability Support Pension ^(c) |
| | New applicant (from 1 July 2006) | Part-time | Enhanced Newstart Allowance |

(a) When the youngest child turns 6, a part-time obligation and enhanced Newstart apply.

(b) Existing recipients of Parenting Payment have a 12 month grace period before new obligations commence, starting from the later of 1 July 2007 or their youngest child's seventh birthday.

(c) New applicants for the Disability Support Pension between 11 May 2005 and 30 June 2006 will be reassessed after 1 July 2006. If the reassessment indicates they can work 15-29 hours per week they will be placed on enhanced Newstart Allowance and have a part-time work obligation.

People in receipt of the Disability Support Pension prior to 1 July 2006 will remain on that payment with no part-time work obligation. They will be subject to the normal periodic review process for Disability Support Pension, usually every two or five years, which will apply the existing eligibility criteria (which is broadly whether that person is capable of 30 hours work per week at award wages).

People seeking to go on Disability Support Pension on or after 1 July 2006 will face new eligibility criteria. They will receive Disability Support Pension if they are assessed as being incapable of 15 hours work a week at award wages. If they are assessed as being capable of 15-29 hours work per week at award wages they will receive enhanced Newstart and be subject to an obligation to seek part-time work of at least 15 hours per week.

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People applying for Disability Support Pension between 11 May 2005 and 30 June 2006 will be assessed for eligibility under the existing test; that is whether they are able to work 30 hours per week at award wages. However, their ongoing eligibility will be reassessed in periodic reviews, usually every two or five years, against the new 15-29 hours per week at award wages test, after 1 July 2006. If they are assessed as being capable of 15 hours work per week at award wages they will have an obligation to undertake part-time work and will receive enhanced Newstart.

From 1 July 2006 the Government will increase Mobility Allowance to \$100 per fortnight for people with disabilities who have a part-time obligation to look for work. Disability Support Pensioners who are working 15 or more hours per week may also be eligible.

The Government will also enhance Newstart Allowance. This will support increased participation by improving the returns to part-time work. The maximum withdrawal rate will be reduced from 70 to 60 cents in the dollar. In addition, the income at which this rate commences will be increased to \$250 per fortnight, up from \$142 for Newstart currently. Both these changes will benefit recipients of Newstart Allowance, as well as recipients of Youth Allowance (Other), Mature Age Allowance, Widow Allowance, Sickness Allowance and Partner Allowance. Recipients of Youth Allowance (Student), Austudy and Abstudy will benefit from a reduction in the withdrawal rate from 70 cents to 60 cents in the dollar.

New and expanded services to help people get jobs

The Government will ensure that those who are obliged to look for work receive appropriate assistance to help them find work. This budget includes over \$2 billion in new and expanded services to help people get jobs.

- Parents will benefit from a new \$48 million Employment Preparation service, which will allow Job Network providers to purchase skills training and assessments. Employment Preparation will replace the current Transition to Work Programme.
- People with disabilities will benefit from a new \$80 million Pre-Vocational Participation Account to provide limited short interventions that allow them to become job-ready quickly. Services that this will fund include pain management, work conditioning and short-term mental health interventions.
- A new Wage Assist Programme will allow Job Network providers to provide wage subsidies to employers who hire long-term unemployed people who have been making a genuine effort to find work. Wage assistance will be payable for between 13 and 26 weeks.
- A comprehensive work capacity assessment will assess all new Disability Support Pension applicants to determine whether they can work between 15 and 29 hours per week at award wages.

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- An extra \$266 million over four years to increase the number of child care places, including 84,300 Outside School Hours Care places.
- Other existing services will also expand. The Government will provide additional funding of: \$170 million over three years for the Disability Open Employment Service programme; \$178 million over three years for rehabilitation services; and \$43 million over three years for additional Vocational Education and Training places.

A new compliance framework

The new obligations to look for work will be supported by an improved compliance framework incorporating payment suspension, rather than payment reduction. This will provide greater incentives for people to meet their obligations.

Bolstering the national skills pool

With unemployment at 5.1 per cent, its lowest level in a generation, it is not unexpected that skills shortages are emerging in some places and some sectors of the economy, particularly those benefiting from the strong terms of trade that Australia is experiencing. This budget introduces a range of initiatives in education, training and skilled migration to bolster the national skills pool.

These measures are underpinned by two longer-term drivers:

- to increase productivity by enhancing workforce skills and the capacity to apply new technologies; and
- to bolster participation, which depends vitally on educational attainment. Some 81 per cent of those of working age who have post-school qualifications are employed compared to only 61 per cent of those without such qualifications.

The Government is increasing vocational education and training (VET) places, and taking measures to attract more Australians to the rewards of a career in the trades. This budget will create 4,500 pre-vocational training places for people interested in a career in a traditional trade, at a cost of \$20 million, and provide an additional 7,000 School-Based New Apprenticeships, at a cost of \$26 million, so more students can begin their apprenticeships while continuing their school studies.

This budget also implements other policies announced in the recent election. Youth Allowance (as well as Austudy and Abstudy for over 25 year olds) will be extended to apprentices. 24 Australian Technical Colleges, located in areas of skill shortage and linked to industry needs will be established to provide 7,200 year 11 and 12 students with an academic and a vocational education. 20,000 New Apprenticeship Access Programme places will assist job seekers in areas of skill shortage who want a New Apprenticeship but need additional skills before they commence. Scholarships will be provided for apprentices, as well as toolkits for apprentices in skill shortage disciplines.

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Through the Commonwealth-State Training Funding Agreement, over 2005 to 2008, the Government will invest a further \$5 billion and deliver extra reforms which include: providing more training places in areas of skill shortage; removing impediments to user choice, so employers and employees have more freedom to choose the training organisation that best suits their needs; ensuring the system is industry-led and responds flexibly to industry needs; and providing greater access to training places and recognition of prior learning for mature workers.

The Government will continue to invest strongly in Australian schools, which underpin Australia's long-term skilled labour supply. As announced in the recent election, the Government will implement its election commitment, A Billion Dollar Investment in Our School Infrastructure. This budget also sees the Government continue the Australian Government Quality Teacher Programme at a cost of \$140 million. Overall, the Government will provide \$33 billion to Australian schools over 2005-2008, some \$9.5 billion more than in the previous four year period.

The Government is committed to ensuring young Australians receive the guidance they need to assist them in navigating key transitions at school and the move on to further study and work. This budget will provide \$143 million to deliver an Australian Network of Industry Career Advisers.

To supplement the national skills pool, the Government will increase skilled migration places by 20,000 in 2005-06 to 97,500, up from 24,100 in 1995-96, and take a range of initiatives to ensure Australia takes migrants with skills currently in short supply. In addition, it will establish a new trade skills training visa to enable overseas students to undertake apprenticeships in regional Australia on a full-fee paying basis.

The Government will also exempt temporary residents from Australian tax on most of their foreign source income for up to four years. This will provide tax relief of \$105 million over 2007-08 and 2008-09, making it easier for Australian businesses to attract skilled workers to fill short-term vacancies, and help to ease cost pressures from employing foreign workers.

The Future Fund

With net debt dramatically reduced by this Government through continued surpluses and the use of asset sale proceeds to retire debt, the Government has made a further commitment to long-term fiscal sustainability by establishing a Future Fund to meet its unfunded superannuation liabilities, which currently amount to \$91 billion.

The Future Fund will strengthen Australia's long-term financial position and ensure we are better able to meet the challenges of the future. Funding superannuation now will reduce future pressures on the budget at a time when the Government will need to face the spending challenges of an ageing population.

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The Future Fund aims to accumulate sufficient financial assets to offset the Government's unfunded superannuation liabilities by 2020. The Government will commit accumulated surpluses of around \$16 billion to the Fund as seed capital, once the 2004-05 Budget surplus is realised. These funds will be invested in a range of financial assets.

To ensure the Future Fund grows over time, the Government will reinvest its investment earnings in the Fund, which will be quarantined from the rest of the budget. The Government intends to invest future budget surpluses in the Fund. Legislation will be introduced to establish the Fund, which is to be managed by an independent statutory agency governed by an appropriately qualified board. The Government will set out an investment mandate to guide the board in managing the Fund. This legislation will prevent drawdowns from the Fund until the superannuation liability is considered by actuarial assessment to be fully funded. The Government will only be able to draw down the Fund to meet superannuation payments.

Supporting business in Australia

Providing tax and tariff relief for business

The Government will provide \$1.8 billion in tax and tariff relief to business through a range of initiatives aimed at reducing cost pressures on business and supporting efficient and sustainable investment. The measures will help sustain high rates of productivity growth and increase the competitiveness of Australian business. Changes to international taxation arrangements will enhance Australia's attractiveness to foreign investors and as a location for regional headquarters, and will remove impediments to Australian firms investing overseas.

- The Government will remove the 3 per cent concessional tariff on business inputs that applies when there are no substitutable goods manufactured in Australia. The removal of the tariff will reduce business input costs by \$1.25 billion over four years, helping to increase the international competitiveness of Australian business and encourage investment in efficient industries, so enhancing productivity.
- The Government will introduce a systematic treatment for 'blackhole' expenditures which will allow business to deduct a range of these expenses, including pre-business costs, which currently are not deductible for taxation purposes. 'Blackhole' expenditures are expenses which, currently, are not recognised under tax law. In addition, there will be increased scope for business to include expenditures in the cost base of an asset for capital gains tax purposes. The initiative will provide tax relief of \$205 million over 2006-07 to 2008-09.
- The Government will make changes to align Australia's capital gains tax (CGT) regime for non-residents more closely with international norms, at a cost of \$230 million over four years. These changes will narrow the operation of the CGT

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for non-residents by limiting its application to non-resident direct or indirect holdings of Australian real property (and similar assets, such as mining rights) and non-residents holding assets of a permanent establishment in Australia (branch assets). Bringing Australia into line with international practice will improve Australia's attractiveness as an investment destination.

- The foreign loss and foreign tax credit quarantining rules will be abolished. This will benefit Australian multinationals, regional headquarters operations in Australia, managed funds and small Australian businesses expanding offshore, at a cost of \$50 million over 2007-08 to 2008-09. This budget also delivers the Government's election commitment to remove loss quarantining provisions that apply to film income.
- The Government will enhance the operation of the Petroleum Resource Rent Tax (PRRT) and the associated Gas Transfer Price Regulations to reduce industry compliance costs and improve administration. The changes will cost \$23 million between 2006-07 and 2008-09, mainly due to changes to the timing of PRRT payments from allowing transferable exploration expenditure to be taken into account in calculating quarterly instalments of PRRT.

These measures build on previous tax initiatives for business, announced since the last budget, which provide targeted tax relief to small business, including the entrepreneur's tax offset (costing \$1.2 billion over 2006-07 to 2008-09) and improved access to the simplified tax system (costing \$361 million over four years).

This budget also provides a further \$74 million to support small business through the continuation of the successful Small Business Assistance Programme, the Small Business Mentoring and Succession Programme, and the Business Entry Point website. The continuation of these programmes is recognition of the contribution the small business sector makes to the Australian economy and demonstrates the Government's commitment to supporting the entrepreneurial spirit of Australia's small businesses.

The Government will provide \$12 million over four years to assist small businesses and their employees to form Australian Workplace Agreements, and provide a Workplace Dispute Settlement Pilot Programme to resolve disputes in a less formal and less costly way.

Investing in health and aged care

In 2005-06 the Government will spend \$45 billion on health and aged care, up from \$20 billion in the Government's first budget in 1996-97.

Targeting health priorities and investing in health promotion

This budget targets key health priorities and invests in health promotion, prevention and detection activities as part of a strategy to enhance the long-term health of Australians. Healthy individuals are more likely to enjoy opportunities to participate

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in the labour force and in society more generally, while minimising the growth of health costs.

This budget provides:

- \$321 million over five years, including measures announced last year, to make dementia a National Health Priority and invest in early intervention, additional care services and carer training to significantly improve the quality of life for people with dementia;
- \$208 million over five years to assist carers of senior Australians with more financial help and better access to respite care;
- \$196 million over five years, including measures announced last year, through the Strengthening Cancer Care initiative to introduce coordinated measures that tackle prevention, treatment, research and support for cancer patients and their families and carers;
- \$139 million over four years to fund new vaccines for chickenpox and polio, continuing the Government's strong commitment to child immunisation programmes;
- \$79 million over four years to improve access to health services for veterans;
- \$25 million over four years to implement a new National Tobacco Youth Campaign to help discourage young Australians from taking up smoking; and
- \$22 million over four years in additional prevention, treatment and communication programmes as part of the National Illicit Drugs Strategy, which has received approximately \$1 billion of Government funding since its introduction in 1997.

These initiatives build on the recently concluded Public Health Outcome Funding Agreements with the states and territories, which will provide \$812 million funding over five years for public health initiatives, and on the Government's \$116 million Building a Healthy, Active Australia package announced in 2004.

Creating a sustainable health system

However, Australia faces significant long-term pressures on health expenditure. Consistent with the requirements of responsible management, the Government is taking the necessary policy decisions to ensure the long-term viability of the health system. Failure to make changes today will put key government programmes at risk in the future.

The Government is raising the Medicare Safety Net thresholds to \$500 for concession card holders and Family Tax Benefit Part A recipients and to \$1000 for all other individuals and families. These threshold levels are those the Government originally

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proposed to the Senate. Setting the thresholds at these levels will save \$499 million over four years, helping ensure the sustainability of this important government initiative.

The Medicare Safety Net will remain a generous protection against high medical expenses, with over \$1.1 billion in benefits expected to be paid over the next four years. It also needs to be considered in the context of the Government's significant investment in Medicare, including the 100 per cent Medicare initiative, which has made GP services more affordable.

The Pharmaceutical Benefits Scheme (PBS) is the fastest growing component of health expenditure. The Government is committed to ensuring the sustainability of the PBS so all Australians can continue to have affordable access to necessary medicines, including through the listing of new innovative drugs as they become available.

In this budget, the Government is phasing in a moderate increase in the PBS Safety Net thresholds to further improve the balance of Government and consumer contributions. This measure builds on the 12.5 per cent mandatory price reduction for new generic drugs which will save an estimated \$1 billion over five years.

The Government is pursuing needed reforms in the distribution and retailing of PBS medicines to contain the escalating costs. Through the next Community Pharmacy Agreement, the Government will ensure pharmacies are rewarded for the services they provide, without this placing an unfair burden on taxpayers. The Government will be seeking significant savings in this area in the next five-year Agreement, as well as substantial further savings over time.

A new approach to family law

The Government has a continuing strong commitment to Australian families.

This budget provides \$398 million for reforms to the family law system focusing on families and their needs before, during and after separation. Increased services will help prevent separation and, where parents do separate, will allow a less adversarial path to separation through:

- A network of 65 community-based Family Relationship Centres at a cost of \$199 million over four years. These will underpin a fresh approach to the family law system, putting the emphasis on reaching agreement on child custody arrangements at a much earlier stage in the separation process, outside and before formal court proceedings. As part of this initiative, \$10 million will be provided to Rural Outreach Services;
- \$137 million over four years to maintain the increased funding to family relationship services provided in 2004-05 and for a significant expansion of

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pre-marriage education, early intervention services for families and Men's Line; and

- \$54 million over four years to expand the successful Contact Orders Programme, children's contact services, dispute resolution counselling, mediation and similar services.

Assistance for Indigenous Australians

This budget provides substantial extra assistance for Indigenous Australians.

- \$86 million will be provided over four years to continue to develop and implement Shared Responsibility Agreements. A key priority in this process will be further fostering community engagement in goal setting and decision making processes.
- In employment and business development, the Community Development Employment Projects (CDEP) programme will be reformed to give more outcome-focused funding agreements, and an Indigenous Economic Development Strategy will be implemented to identify and foster entrepreneurs.
- In health, the Government will provide \$102 million over four years to improve the health of Indigenous babies and children, through targeted activities in maternal and child health and chronic disease. An additional \$40 million will be provided to the Primary Health Care Access Programme to further improve access to health services by establishing new primary health sites and increasing the capacity of existing clinics. Some \$10 million will increase access to hearing services for Indigenous adults, and \$18 million will help to address substance misuse.
- In housing, the Government will invest \$103 million over four years to continue and expand the Healthy Indigenous Housing initiative to meet, more efficiently and effectively, the housing needs of Indigenous communities.

Providing for Australia's Security

National security remains a priority for the Government.

The Government continues to increase resources for Australia's security agencies to meet the higher demands placed on them. As part of its integrated national security strategy, the Government supports cooperation between national and international agencies, and links to business and the community.

In each budget since 11 September 2001, the Government has invested significantly to improve national security. In total, it has committed \$5.6 billion over eight years from 2001-02 to foster safety and security in Australia and our region.

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This budget provides \$1.1 billion over four years for protective security enhancements, border security, intelligence, regional security initiatives and incident response capacity. The *Providing for Australia's Security* package includes:

- \$522 million for protective security enhancements, including for Defence personnel and facilities and Australia's overseas missions, such as enhanced emergency communications and relocation of some missions;
- \$226 million for border protection, including a significant investment in new biometric technologies, incorporating ePassports, to help border authorities to verify travellers' identities quickly and reliably;
- \$239 million to strengthen Australia's intelligence capabilities, including for counter-terrorism investigations and language skills development;
- \$60 million for regional security initiatives, including cooperation and knowledge sharing and counter-terrorism assistance measures; and
- \$26 million to build Australia's incident response capability, including resources for counter-terrorism prosecutions.

Enhancing quarantine and protecting Southern Ocean fisheries

The Government is committed to maintaining the integrity of Australia's borders.

Australia's quarantine regime provides a strong forward defence against exotic diseases, protecting Australia's unique biodiversity and maintaining the market advantage associated with the Australian agriculture sector's 'clean and green' image. In this budget, the Government commits \$580 million over four years to maintain and enhance our quarantine inspection regime. This includes:

- \$391 million for maintaining Australia's commitment to manage quarantine risk and protect our borders;
- \$144 million for continuing the Government's 40 per cent contribution to quarantine inspection fees and charges, to help Australian agricultural exports to be more price competitive in overseas markets;
- \$39 million for enabling Biosecurity Australia to conduct import risk assessments and promote Australia's quarantine system internationally; and
- \$6 million for enhancing border controls at Australia's airports in response to the increased risk of avian influenza to both humans and animals in our region.

This budget also provides \$181 million over four years from 2006-07 to continue armed patrols of Australia's exclusive economic zone in the Southern Ocean. These patrols

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aim to suppress the activities of vessels engaged in illegal fishing, as well as protect Australia's sovereign interests in, and the environmental values of, the Southern Ocean.

International engagement

The future wellbeing of Australians depends on our ability to gain from trade and other links with the rest of the world, while limiting exposure to external risks. Australia has a clear interest in promoting sustainable development in our region and globally. The Government is pursuing an active, practical and multilayered strategy to meet these challenges. Key instruments include providing bilateral assistance and actively participating in global and regional institutions and forums.

Providing bilateral assistance

The Government has committed \$1 billion over five years to help Indonesia recover from the devastating human and economic damage caused by the Boxing Day tsunami. These funds will be divided equally between grant assistance and highly concessional loans. Combined with Australia's existing development cooperation programme, this brings Australia's commitment to Indonesia to a total of \$1.8 billion over five years.

The Government will provide funding of \$69 million over the next four years to develop a tsunami warning system which will provide 24 hour surveillance for accurate and early detection and warning in the event of a tsunami threatening the west or east coast of Australia, or South West Pacific nations.

This budget continues funding to the Regional Assistance Mission to the Solomon Islands at a cost of \$841 million over four years. The Government will also continue its substantial commitments of personnel to strengthen capacity in Papua New Guinea and, on a smaller scale, Nauru.

Australia has a strong interest in a stable and developing Iraq. This budget provides \$466 million over four years to continue the Australian Defence Force's contribution to stabilisation and reconstruction activities. This includes \$240 million over four years for Defence deployments in the Al Muthanna Province in southern Iraq, and \$226 million over three years to continue Operation CATALYST. Additional funding of \$45 million over two years will assist Iraq's economic development and democratic transition.

The Government is maintaining its strong support for the World Bank's Heavily Indebted Poor Countries (HIPC) Initiative, which aims to reduce the excessive debt burdens of the world's poorest nations. This budget provides an additional \$35 million over three years to the HIPC Initiative. The effect of Australia's increased aid commitments will be to raise official development assistance (ODA) by \$518 million from 2003-04 to 2005-06. This will increase the ratio of ODA to gross national income from 0.25 in 2003-04 to 0.28 in 2005-06.

