STATEMENT 4: FINANCIAL OUTLOOK

Contents

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Overview

The introduction of accrual budgeting with an output and outcomes framework further intensifies the Commonwealth's focus on responsible financial management and accountability. Consolidated financial statement projections for the general government sector are presented for the first time in the 1999-2000 Budget.

Operating result

The Commonwealth's operating result before abnormals is expected to improve further in 1999-2000 (see Chart 1). The estimated operating result for 1999-2000 is a surplus of $5.7 billion, an improvement of $2.5 billion from the operating surplus of $3.2 billion expected in 1998-99. This improvement reflects a 6.2 per cent increase in revenue, partly offset by a 4.6 per cent increase in expenses.

After including abnormal and extraordinary items, an operating surplus of $16.7 billion is expected in 1999-2000. Movements in abnormal items over the forward estimates period are largely due to the Government's asset sales programme, particularly the proposed sale of the Government's remaining share in Telstra.

Statement 5 contains detailed descriptions of expenses and Statement 6 contains detailed descriptions of revenues. *Budget Paper No. 2* contains detailed descriptions of individual budget measures.

Chart 1: Operating Result

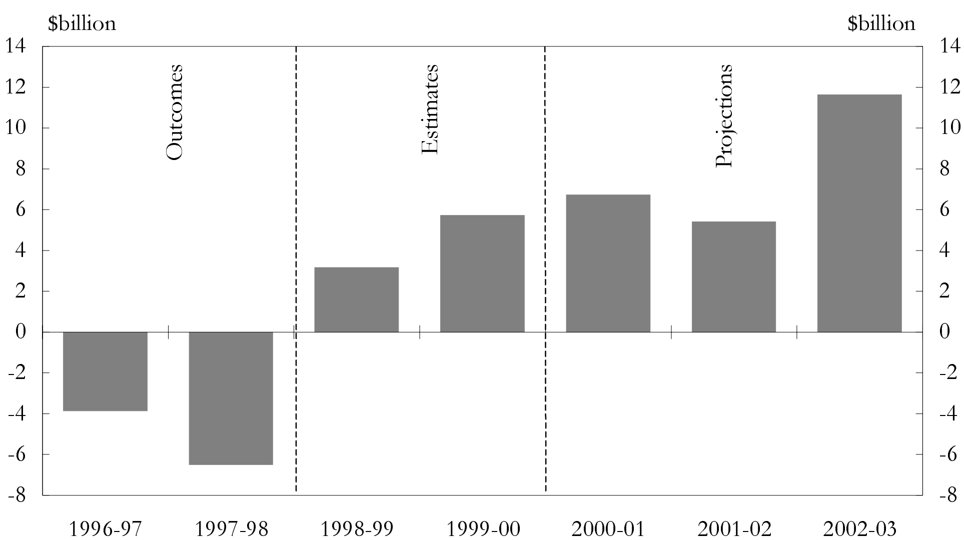


Table 1: Operating Result Estimates

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Revenue					
Total taxation	140847	147779	139223	142465	150723
Total non-taxation	12502	15050	11271	11294	12343
Total	153349	162828	150494	153759	163065
Expenses	150183	157111	143776	148357	151432
Operating result	**3166**	**5717**	**6718**	**5402**	**11633**

Net Assets

The consolidated financial position of the general government sector is expected to improve in 1999-2000 with an increase in net assets of $16.8 billion, or 20.8 per cent, relative to the expected outcome for 1998-99. This improvement will reduce the excess of liabilities over assets to $63.8 billion by 30 June 2000. Unlike private profit making enterprises, governments are able to record negative net asset positions as they have access to a guaranteed stream of revenue to service current and future liabilities.

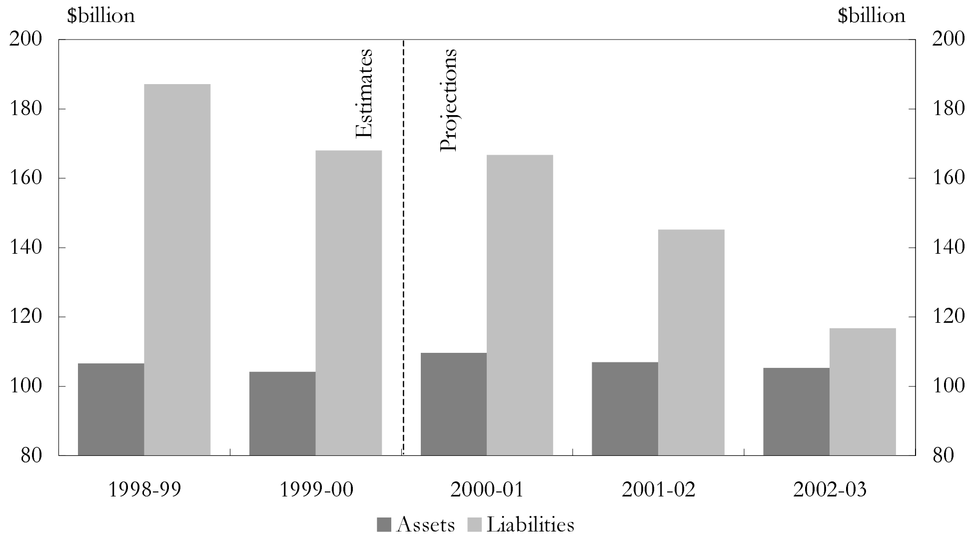
The Commonwealth's net asset position is expected to improve substantially over the budget and forward estimates period (see Chart 2). It is expected that the negative net assets position will be further reduced to $11.5 billion, or 1.6 per cent of GDP, by 2002-03.

Table 2: Balance Sheet Estimates

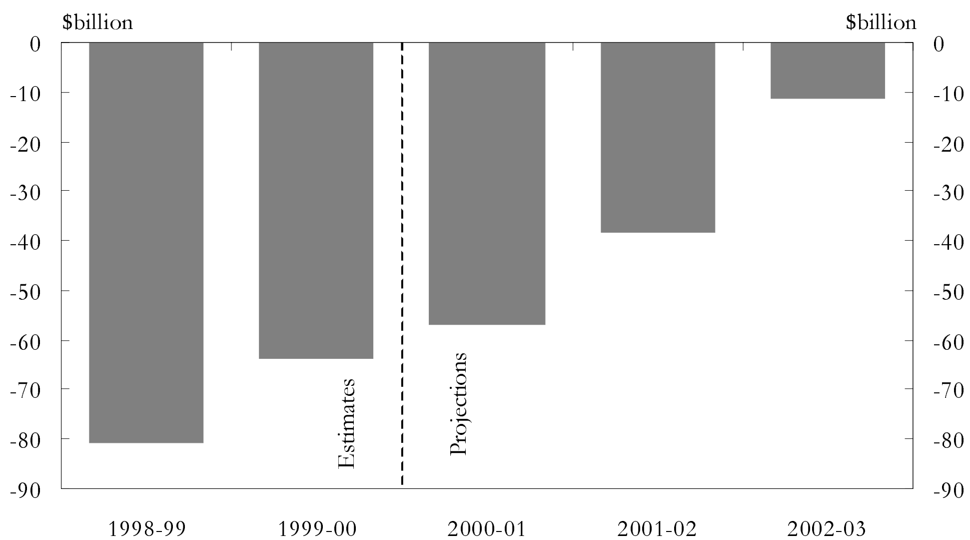
	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Assets					
Financial	52958	49248	53794	50180	47537
Non-financial	53520	54889	55789	56662	57666
Total assets	106478	104137	109583	106842	105203
Liabilities					
Debt	96688	75651	73960	51403	22009
Provisions and payables	90342	92273	92664	93708	94670
Total liabilities	187030	167924	166624	145111	116679
Net assets	**-80551**	**-63787**	**-57041**	**-38269**	**-11476**
Equity	**-80551**	**-63787**	**-57041**	**-38269**	**-11476**

Chart 2: Balance Sheet Aggregates

Panel A: Assets and Liabilities



Panel B: Net Assets



New Agency Banking Arrangements

As part of the introduction of an accrual framework, the Department of Finance and Administration is introducing agency banking arrangements which will apply from 1 July 1999. These apply to agencies covered by the *Financial Management and Accountability Act 1997* (ie Departments of State, Parliamentary Departments and prescribed FMA agencies) and will allow agencies to manage departmental resources, including cash, in a more business-like manner. To encourage better cash management agencies will receive the benefit of being able to retain interest on departmental account balances. Agencies will be responsible for establishing their own bank accounts, processing their payments and receipts, maintaining detailed transactional records and meeting bank fees and charges associated with operating their bank accounts.

Primary Financial Statements

Statement of Revenue and Expenses for the Commonwealth General Government Sector

	Note	Estimates		Projections		
		1998-99	1999-00	2000-01	2001-02	2002-03
		$m	$m	$m	$m	$m
Revenues						
Taxation						
Income tax		104060	109950	111080	114200	121160
Indirect tax	2	30902	31979	22122	21960	23060
Other taxes fees and fines		5885	5849	6021	6305	6503
Total taxation revenue		140847	147779	139223	142465	150723
Non-taxation						
Sales of goods and services		2505	2496	2562	2537	2494
Interest and dividends	3	6502	8844	5535	5605	6694
Net foreign exchange gains		360	0	0	0	0
Net gains from sales of assets		27	9	2	2	2
Other sources of non-tax revenue	4	3107	3700	3173	3150	3153
Total non-tax revenue		12502	15050	11271	11294	12343
Total revenue		153349	162828	150494	153759	163065
Expenses						
Goods and services						
Employees	5	15033	15016	14843	14912	15002
Suppliers	6	11670	13670	12198	12073	11700
Depreciation and amortisation	7	2308	2477	2776	2956	3169
Net write down of assets		1497	1431	1341	1277	1294
Net foreign exchange losses		-140	2	2	2	2
Net losses from the sale of assets		25	43	15	24	13
Other goods and services expenses		4899	5246	4913	5046	5292
Total goods and services		35292	37885	36089	36289	36472
Subsidies benefits and grants						
Personal benefits		59105	61939	68851	71682	75956
Subsidies		3508	3824	4215	4540	4734
Grants	8	43013	44602	26607	28724	27760
Total subsidies benefits and grants		105626	110366	99674	10495	108449
Interest and other						
Interest and other financing costs		9265	8860	8012	7122	6511
Total Interest and other		9265	8860	8012	7122	6511
Total expenses		**150183**	**157111**	**143776**	**148357**	**151432**
Operating result		**3166**	**5717**	**6718**	**5402**	**11633**
Abnormal and extraordinary items		**624**	**10990**	**0**	**13293**	**15131**
Operating result after abnormal items		**3790**	**16707**	**6718**	**18695**	**26764**

Balance Sheet for the Commonwealth General Government Sector

	Note	Estimates		Projections		
		1998-99	1999-00	2000-01	2001-02	2002-03
		$m	$m	$m	$m	$m
Assets						
Financial assets						
Cash		1875	2006	1755	1581	1307
Receivables		20125	19964	24355	21942	20646
Investments	12	29319	25328	25491	24142	22720
Accrued revenue		385	423	399	447	522
Other financial assets		1254	1527	1795	2069	2342
Total financial assets		52958	49248	53794	50180	47537
Non-financial assets						
Land and buildings		14448	14152	13895	13482	13526
Infrastructure		33955	35628	36947	38318	39431
Intangibles		601	740	709	616	528
Inventories		2902	2746	2639	2646	2584
Other non-financial assets	9	1615	1624	1599	1600	1597
Total non-financial assets		**53520**	**54889**	**55789**	**56662**	**57666**
Total assets		**106478**	**104137**	**109583**	**106842**	**105203**
Liabilities						
Debt						
Government securities	12	87322	64143	62541	38429	9257
Loans		5607	7455	7392	9330	9265
Leases		216	191	236	223	210
Deposits		559	632	705	778	851
Overdrafts		2	2	2	2	2
Other debt		2984	3228	3085	2642	2425
Total debt		**96688**	**75651**	**73960**	**51403**	**22009**
Provisions and payables						
Employees	10	74710	75864	76881	77636	78351
Suppliers		2011	1851	1855	1844	1831
Personal benefits payable		1096	2261	2459	2639	2904
Subsidies payable		72	71	69	68	67
Grants payable	11	8147	8123	8162	8256	8089
Other provisions and payables		4305	4103	3239	3265	3428
Total provisions and payables		**90342**	**92273**	**92664**	**93708**	**94670**
Total liabilities		**187030**	**167924**	**166624**	**145111**	**116679**
Net assets		**-80551**	**-63787**	**-57041**	**-38269**	**-11476**
Equity						
Accumulated results		-104822	-86603	-79870	-59679	-31274
Reserves		24271	22817	22829	21410	19798
Total equity		**-80551**	**-63787**	**-57041**	**-38269**	**-11476**

Statement of Cash Flows for the Commonwealth General Government Sector

	Note	Estimates		Projections		
		1998-99	1999-00	2000-01	2001-02	2002-03
		$m	$m	$m	$m	$m
Operating activities						
Cash received						
Taxes fees and fines	13	139202	145411	134086	142894	150882
Sales of goods and services		3003	2811	2752	2584	2826
Interest		2158	2704	2662	2729	4135
Dividends		4258	6065	2915	2756	2393
Other		3043	3646	3078	3115	2655
Total operating cash received		151664	160637	145493	154078	162891
Cash used						
Payments to employees		15574	13862	13826	14156	14287
Payments to suppliers		11244	13473	11796	11652	11304
Subsidies paid		3635	3826	4217	4541	4735
Personal benefits		58402	60774	68653	71503	75690
Grant payments		41666	44627	26569	28630	27927
Interest and other financing costs		9265	8860	8012	7122	6511
Other		5354	5449	5779	5021	5130
Total operating cash used		145141	150871	138854	142625	145585
Net cash from operating activities		**6523**	**9766**	**6639**	**11453**	**17306**
Investing activities						
Cash received						
Proceeds from asset sales program		5511	15828	-	15658	16698
Proceeds from sales of property, plant and equipment and intangibles		701	810	725	699	553
Other		170	3	25	-	-
Total investing cash received		6382	16641	750	16356	17251
Cash used						
Purchase of property, plant and equipment and intangibles		4579	4989	4838	5055	4967
Net advance receipts		-	-	923	-	-
Other	12	783	248	187	372	458
Total investing cash used		5362	5237	5949	5427	5425
Net cash from investing activities		**1020**	**11404**	**-5199**	**10930**	**11826**

	Note	Estimates		Projections		
		1998-99	1999-00	2000-01	2001-02	2002-03
		$m	$m	$m	$m	$m
Financing activities						
Cash received						
Other		630	317	118	73	73
Total cash received		630	317	118	73	73
Cash used						
Net repayments of borrowings	12	6288	21330	1666	22174	29249
Other		995	25	143	456	230
Total cash used		7283	21355	1809	22629	29479
Net cash to/from financing activities		**-6653**	**-21038**	**-1691**	**-22556**	**-29406**
Net increase/decrease in cash held		**890**	**131**	**-251**	**-174**	**-274**

Appendix A — Statistics, Concepts and Notes to the Financial Statements

Note 1: External Reporting Standards

The *Charter of Budget Honesty Act 1998* requires that the budget is based on external reporting standards and that departures from applicable external reporting standards are identified.

The 1999-2000 Budget financial statements have been prepared on an accrual basis in accordance with applicable Australian accounting standards, including Australian Accounting Standard No. 31 'Financial Reporting by Governments' (AAS31). AAS31 is the relevant accounting standard for financial reporting by governments.

AAS31 requires the adoption of a full accrual basis of accounting. This means that assets, liabilities, revenues and expenses are recorded in financial statements when they have their economic impact, rather than when the cash flows associated with these transactions occur. Consistent with AAS31, an operating statement, a statement of financial position and a statement of cash flows have been prepared using estimates for the current year, budget year and the three forward years.

The accounting policies in this budget document are consistent with the accounting policies in AAS31. While the scope for financial reporting recommended in AAS31 is the whole-of-government (that is, the Commonwealth public sector), the 1999-2000 Budget financial estimates cover the general government sector only. However, a whole-of-government approach for reporting financial outcomes is adopted in the Commonwealth's Consolidated Financial Statements.

In relation to revenue, AAS31 suggests revenue be recognised at the time the income (or economic activity) giving rise to a tax liability occurs, where this can be measured *reliably*. The Commonwealth does not consider its revenues can be reliably forecast on this basis. Revenue in the budget is therefore recognised at the time the relevant tax law indicates the existence of a requirement to pay an amount in tax or when a tax assessment is raised by the Australian Taxation Office (ATO) and the Australian Customs Service (ACS). That is, revenue is only recognised when the taxpayer makes a self-assessment or the ATO/ACS issues an assessment. This differs from the method used for recording taxation revenue in previous accrual outcome reports.

In order to ensure that all dividends are reported on a consistent basis, in the Budget Financial Statements for the forecast years, dividends are recorded in the year that they are declared, rather than the year in which the income was earned. For the RBA dividend this treatment differs from that applied in the 1997-98 Consolidated Financial Statements.

The Commonwealth collects a number of taxes on an agency basis for the States and Territories, principally Revenue Replacement Taxes (which replaced business franchise fees), mirror taxes on Commonwealth places and from 1 July 2000, the goods and services tax. The revenue from these taxes is passed to State and Territory Governments (with an adjustment for administration costs in the case of Revenue Replacement taxes). AAS31 and other relevant accounting standards would suggest the gross amount of these taxes be included in the Commonwealth's financial statements. However, given the Commonwealth's agency role in the collection of these taxes, the accrued revenues and associated payments to the States and Territories are not recorded in the budget estimates.

Note 2: Indirect Tax

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Sales tax	16080	16710	2050	870	890
Of which Revenue Replacement	*1000*	*1054*	*88*	*0*	*0*
Less transfers to States and Territories in relation to revenue replacement	997	1052	88	0	0
Sales tax revenue	**15083**	**15659**	**1962**	**870**	**890**
Excise duty	17640	18200	16470	16730	17310
Of which Revenue replacement	*5469*	*5528*	*257*	*0*	*0*
Less transfers to States and Territories in relation to revenue replacement	5463	5523	256	0	0
Excise duty revenue	**12177**	**12677**	**16214**	**16730**	**17310**
Customs duty	3820	3820	3950	4360	4860
Of which Revenue replacement	*178*	*176*	*4*	*0*	*0*
Less transfers to States and Territories in relation to revenue replacement	177	176	4	0	0
Customs duty revenue	**3643**	**3644**	**3946**	**4360**	**4860**
GST revenue			27409	32290	33259
Less transfers to States and Territories in relation to GST revenue			27409	32290	33259
GST revenue			**0**	**0**	**0**
Mirror taxes	123	127	111	115	120
Less transfers to States and Territories in relation to mirror revenue	123	127	111	115	120
Mirror tax revenue	**0**	**0**	**0**	**0**	**0**
Indirect tax revenue	**30902**	**31979**	**22122**	**21960**	**23060**

Note 3: Interest and Dividends

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Interest					
Interest from other governments					
State and Territory debt	226	194	114	76	69
Housing agreements	224	175	172	169	166
Total interest from other governments	449	369	286	245	235
Interest from other sources					
Swap interest	1515	1690	1428	1491	1710
Advances	34	39	44	49	53
Deposits	6	20	23	26	28
Bills receivable	6	6	6	6	6
Bank deposits	86	100	106	116	126
Other	154	554	726	916	2144
Total interest from other sources	1801	2410	2334	2604	4066
Total interest	**2250**	**2779**	**2620**	**2849**	**4301**
Dividends					
Dividends from associated entities	4126	5958	2819	2650	2283
Other dividends	126	108	96	106	110
Total dividends	**4252**	**6065**	**2915**	**2756**	**2393**
Total interest and dividends	**6502**	**8844**	**5535**	**5605**	**6694**

Note 4: Other Sources of Non-taxation Revenues

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Industry contributions	179	144	133	135	132
Indexation of HECS receivable and AUSTUDY loans	79	144	143	175	166
International Monetary Fund related revenue	57	69	69	69	69
Other	2791	3343	2827	2771	2785
Total other sources of non-taxation revenues	**3107**	**3700**	**3173**	**3150**	**3153**

Note 5: Employees

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Salaries and wages	9384	9419	9305	9422	9352
Superannuation[1]	2788	2801	2821	2827	2823
Leave and other entitlements	285	271	258	278	282
Separations and redundancies	135	63	29	24	26
Workers compensation premiums	35	34	34	34	34
Other	2407	2428	2397	2326	2484
Total employees	**15033**	**15016**	**14843**	**14912**	**15002**

Note 6: Suppliers

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Supply of goods and services	8845	10623	9117	9055	8698
Operating lease rental expenses	961	926	918	930	943
Other	1864	2121	2164	2088	2059
Total suppliers	**11670**	**13670**	**12198**	**12073**	**11700**

Note 7: Depreciation and Amortisation

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Depreciation					
Specialist military equipment	1036	1124	1317	1463	1655
Buildings	437	444	437	436	440
Other infrastructure, plant and equipment	708	768	857	880	886
Total depreciation	2181	2336	2611	2779	2981
Total amortisation	127	140	165	177	188
Total depreciation and amortisation	**2308**	**2477**	**2776**	**2956**	**3169**

[1] The amounts contained in this note do not reflect the Commonwealth's total superannuation expense. That can be obtained from the GFS operating statement (superannuation expense and superannuation interest) in Statement 9.

Note 8: Grants

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
State and Territory Governments	32524	33687	15794	17742	17402
Non-profit organisations	1120	1106	1110	1106	1118
Overseas	533	229	450	496	223
Private sector	-26	558	262	252	101
Local governments	7	188	202	206	200
Other	8855	8835	8790	8922	8715
Total grants	**43013**	**44602**	**26607**	**28724**	**27760**

Note 9: Other Non-financial Assets

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Prepayments	837	835	835	838	838
Other	778	788	764	762	760
Total other non-financial assets	**1615**	**1624**	**1599**	**1600**	**1597**

Note 10: Employee Liabilities

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Superannuation	69088	70174	71136	71811	72421
Leave and other entitlements	2945	3022	3099	3194	3294
Accrued salaries and wages	575	631	651	677	713
Workers compensation claims	2021	1972	1927	1886	1854
Separations and redundancies	30	16	15	13	14
Workers compensation premiums	0	0	0	0	0
Other	51	49	52	55	55
Total employee entitlements	**74710**	**75864**	**76881**	**77636**	**78351**

Note 11: Grants Payable

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
State and Territory Governments	2331	2542	2616	2713	2783
Non-profit organisations	30	10	9	8	8
Private sector	7	6	5	5	2
Overseas	1373	1110	1090	1111	865
Local governments	2	2	2	2	2
Other	4403	4453	4439	4416	4428
Total grants payable	**8147**	**8123**	**8162**	**8256**	**8089**

Note 12: Government Securities

Transactions relating to government securities and financial assets acquired for debt management purposes have been netted in the statements of financial position and cash flows. In the statement of financial position, the financial assets — investments category excludes financial assets acquired for debt management purposes, while the debt — government securities category is shown net of financial assets acquired for debt management purposes. Likewise, in the statement of cash flows, the investing activities — cash used — other category excludes cash used to acquire financial assets for debt management purposes while the financing activities — cash used — repayment of borrowings category includes cash used to acquire financial assets for debt management purposes.

This netting treatment has been applied because of the considerable uncertainty associated with the split between government securities and financial assets acquired for debt management purposes. Debt management strategies in respect of government securities and financial assets are highly dependent on prevailing market conditions and other factors. The balance to be struck between gross debt retirement and financial asset acquisition cannot be accurately estimated in advance.

Note 13: Taxes Fees and Fines

	Estimates		Projections		
	1998-99	1999-00	2000-01	2001-02	2002-03
	$m	$m	$m	$m	$m
Total taxes fees and fines	145840	152530	161954	175299	184261
Less payments to States and Territories in relation to revenue replacement	6638	6751	348	0	0
Less payments to States and Territories in relation to GST revenue	0	0	27409	32290	33259
Less payments to States and Territories in relation to mirror tax revenue	0	368	111	115	120
Taxes fees and fines	**139202**	**145411**	**134086**	**142894**	**150882**

Appendix B: Sensitivity of Fiscal Aggregates to Economic Developments

Table B1 provides a guide to the sensitivity of the forward estimates of expenses and revenue to variations in economic parameters in 1999-2000. It is important to recognise that the estimates presented in the table provide only a 'rule of thumb' indication of the impact on the budget of changes in economic and other parameters.

Table B1: Sensitivity of Financial Aggregates to Changes in Economic Parameters

	1999-00 $m	2000-01 $m	2001-02 $m	2002-03 $m
Expenses				
Prices	270	310	640	480
Wages	80	310	360	370
Unemployment Benefit Recipients	300	300	300	300
Safety Net Adjustment	60	180	310	390
Revenue				
Prices	70	240	250	260
Wages	1100	1020	1080	1180
Employment	720	670	700	760
Private Final Demand	340	270	280	280

EXPENSES

On the expenses side, the sensitivity analysis of the estimates provides for the following assumptions about changes to four broad groups of parameters:

- prices — all price deflators are assumed to increase by one percentage point at the start of the September quarter 1999, with wage deflators left unchanged;

- wages — all wage and salary rates are assumed to increase by one percentage point from the beginning of the September quarter 1999, with price deflators left unchanged;

- unemployment benefit recipients (includes Newstart Allowance and unemployed Youth Allowance recipients) — the total number of recipients is assumed to increase by 5 per cent from the beginning of the September quarter 1999; and

- Safety Net Adjustment — the Safety Net Adjustment (SNA) determined by the Australian Industrial Relations Commission (AIRC) is assumed to increase by $2 per week in the budget and forward years from the 1998-99 financial year. The SNA is used in the calculation of Wage Cost Indexes. Changing the SNA in the 1998-99 year will produce a full year impact in the budget year (1999-2000).

In addition, about $28 billion of expenses, comprising agency departmental expenses, other Commonwealth Own Purpose Expenses of a departmental expense nature and Specific Purpose Payments to the States of a departmental expense nature, are indexed to weighted averages of movements in underlying inflation and the SNA determined by the AIRC.

The profile of the prices sensitivity has changed when compared to previous analysis. This is primarily due to the introduction of *A New Tax System* and its interaction with financial assistance grants to the States. This has the most impact during the transition period in 2000-01 and 2001-02. There are also flow-on effects to other accounts (other than expenses) which are not included in the above analysis.

The number of unemployment benefit recipients, and therefore the total spending on benefits, is affected by economic growth and employment growth. However, the relationship between GDP growth and unemployment benefit recipients is highly variable and difficult to quantify. For this reason, Table B1 only includes the impact of changes in the number of unemployment benefit recipients (ie Newstart Allowance and unemployed Youth Allowance recipients) on the estimates.

REVENUE

The assumptions underlying the sensitivity of the revenue estimates to changes in prices and wages are identical to those used for expenses. In each case, the analysis presents the estimated effects of change in one economic variable only, and does not attempt to capture the linkages between economic variables that characterise changes in the economy more broadly.

The revenue effects of changes in employment and private final demand show the effect of the following assumptions:

- employment — if the level of employment is assumed to increase by one per cent from the beginning of the September quarter 1999, with no change in the composition of demand; and

- private final demand (consumption plus investment) — if the level of private final demand is assumed to increase by one per cent from the beginning of the September quarter 1999, with no change in the composition of demand.

Changes in prices affect revenue through changes in excise revenue. Changes to arrangements relating to business franchise fee replacement taxes announced in *A New Tax System* result in larger changes in excise revenue for a given change in prices from 2000-01 onwards.

Changes in wages and employment feed through quickly into tax revenue largely through increases in PAYE tax collections. The personal income tax cuts, which come into effect from 2000-01, cause some reduction in the sensitivity of revenue to changes in wages and employment.

Changes in private final demand affect revenue predominantly through changes in sales tax and excise collections. The abolition of Wholesale Sales Tax from 2000-01 means that changes in private final demand have a much lower impact on the revenue from that year.

Appendix C: Statement of Risks

OVERVIEW

The forward estimates of revenue and expenses in the 1999-2000 Budget incorporate assumptions and judgements based on information available at the time of publication. A range of factors may influence the actual budget outcome in future years. The *Charter of Budget Honesty Act 1998* requires these to be disclosed in a Statement of Risks in each Economic and Fiscal Outlook Report. The purpose of this disclosure is to increase the transparency of the fiscal projections.

Events which could affect fiscal outcomes include:

- changes in economic and other parameters;
- matters which have not been included in the fiscal forecasts because of uncertainty about their timing, magnitude or whether they will eventuate; and
- the realisation of contingent liabilities.

Economic and Other Parameters

Some degree of uncertainty is attached to budget time and forward estimates for both revenues and expenses. For example, past experience indicates that the actual revenue outcome could vary from the initial estimate by about 2¼ per cent on average for the budget year.

The major factor influencing expected expenses and revenues in any year is typically changes in forecasts of economic and non-economic parameters. Over time, differences between the economic parameter forecasts and outcomes have not caused any clear bias toward understatement or overstatement of expenses and revenue — and therefore the budget balance. The sensitivity of the estimates to major economic parameters (but not other parameters) is discussed in Appendix B.

Differences in non-economic (programme-specific) parameter forecasts and outcomes have been biased towards an understatement of expenses in recent years. This year, considerable effort has been made to reduce the extent of this bias. Programme-specific parameters are assumptions underpinning some particular programme estimates, eg client numbers and/or average rates payable on family payments, family tax payments and disability support pension programmes. The Contingency Reserve contains an allowance for this conservative bias.

Fiscal Risks

Fiscal risks are general developments or specific events which may have an effect on the fiscal outlook. In some cases, the events will simply raise the possibility of some fiscal impact. In other cases, some fiscal impact will be reasonably certain, but it will not be included in the forward estimates because the timing or magnitude is not known. Fiscal risks may affect expenses and/or revenue and may be positive or negative.

Specific sources of fiscal risk include:

- litigation currently before the courts; and
- possible Senate rejection or amendment of budget measures or other legislation before the Parliament.

Some fiscal risks are reflected in the Contingency Reserve and are therefore included in the aggregate expenses figuring. The Contingency Reserve is an allowance included in aggregate expenses to reflect anticipated events which cannot be assigned to individual programmes at budget time. These items are also not included in the Statement of Risks. Fiscal risks in the Contingency Reserve include expected running costs carryovers from 1998-99 to 1999-2000, and allowances for the established tendency for estimates of some programme expenditure to be overstated in the budget year and understated in the forward years.

Matters that are not currently under active consideration by Government, or pressure from interests outside the Government for changes in spending levels, are not treated as fiscal risks.

Contingent Liabilities

Contingent liabilities differ from fiscal risks in that they are generally more readily quantifiable and clearly defined.

Contingent liabilities are defined as costs the Government will have to face if a particular event occurs. They include loan guarantees, non-loan guarantees, warranties, indemnities, uncalled capital and letters of comfort.

The Commonwealth's major exposure to contingent liabilities arises out of legislation providing guarantees over certain liabilities of Commonwealth controlled financial institutions (ie the Reserve Bank of Australia (RBA) and the Export Finance and Insurance Corporation) and the now fully privatised Commonwealth Bank of Australia. Other substantial non-loan guarantees include guaranteed payments from Telstra Corporation Ltd to the Telstra Superannuation Scheme.

The strategies for managing these exposures are aimed at ensuring the underlying strength and viability of the entities, so that the guarantees are not triggered. Similar strategies apply to entities not subject to explicit guarantees.

Other arrangements are in place to govern the entering into, and monitoring of, contingent liabilities such as indemnities and uncalled capital. Uncalled capital is primarily associated with international financial institutions such as the International Bank for Reconstruction and Development, the Asian Development Bank and the European Bank for Reconstruction and Development. Arrangements for capital contributions, including contingent liabilities, are approved by Parliament and reports on the institutions are provided annually by the Government to Parliament.

Consistent with Australian Bureau of Statistics (ABS) standards, transactions concerned with the management of international reserves and the monetary system are classified as financing transactions (and do not impact on the fiscal or operating balance). Therefore, contingent liabilities (and assets) with the International Monetary Fund (IMF) are not shown below.

Details of Fiscal Risks and Contingent Liabilities

Fiscal risks and contingent liabilities with a possible impact on the forward estimates greater than $20 million in any one year, or $40 million over the forward estimates period, are listed below. Information on fiscal risks takes account of decisions of Parliament and other developments up to the close of parliamentary business on 30 April 1999. In general, information on contingent liabilities is based on information provided by departments and agencies and is current to 31 March 1999 (or a later date as indicated where that information is available). However, for the guarantees under the *Commonwealth Bank Sale Act 1995* and the Telstra Corporation Ltd superannuation guarantee, the latest reliable information available on the balance of guarantees outstanding was at the end of June 1998.

Information on contingent liabilities is provided in annual financial statements of departments and non-budget entities.

Fiscal Risks — Revenue

Revenue forecasts, like all forecasts, are subject to a margin of error. Over the previous ten years, the average absolute error in the forecast of revenue in the budget year has been in the order of 2¼ per cent.

The average forecast error, measured relative to the tax base being forecast, is even higher for some components of the tax base. This is particularly evident for the ‘Company’ and ‘Other Individuals’ tax bases, partly reflecting the reaction of these payers to tax changes, and the way capital losses or gains are realised so as to minimise tax payments.

An implication of the degree of uncertainty surrounding the revenue forecasts is that, while many of the forecasts are reported to the nearest ten million dollars for budget accounting purposes, they should not be interpreted as implying an equivalent level of forecast precision.

The various risks influencing the accuracy of the revenue forecasts are outlined below.

Tax Reform

On 13 August 1998, the Government announced its taxation reform package, *A New Tax System*. The reforms encompass both expense and revenue measures. Key revenue measures include: lower personal income tax rates; abolition of Wholesale Sales Tax (WST); abolition of nine State and Territory taxes; introduction of a Goods and Services Tax (GST); and reform of business taxes.

The forward estimates fully incorporate the revenue effects of the taxation reform package. To the extent that the implementation of the Government's package varies from that announced there may be an impact on future revenue collections.

Indirect Tax Changes

A key element of tax reform is the introduction of a GST which will enable the abolition of WST and a series of State and Territory taxes. Rejection of the legislation or significant amendments would jeorpardise the proposal and could amount to a serious fiscal risk.

Review of Business Taxation

The *Review of Business Taxation* is due to report to the Government no later than 30 June 1999. Its terms of reference require a revenue neutral package. There will be an impact on revenue collections if the package of measures implemented is not revenue neutral either in aggregate or in individual years.

Taxpayer Behaviour

The estimates of revenue make an allowance for changes in taxpayer behaviour in the period before the full implementation of tax reform. It is, however, very difficult to quantify the extent to which taxpayers will manage their affairs to take advantage of opportunities to minimise tax over this period. To the extent that taxpayers are able to reduce tax beyond the forecast allowance, revenue will be reduced.

General Risks

The forward estimates of revenue are subject to a number of general pressures which can result in risks to revenue collections. These general pressures include: tax minimisation and avoidance, including the exploitation of tax expenditures; financial innovation; internationalisation; developments in communications technology and workplace arrangements; and court decisions. These pressures may result in a shift in the composition of revenue collected from the various tax bases and/or a change in the size of the tax base. The revenue forecasts make what is believed to be an appropriate allowance for these factors, given the data available.

Tax minimisation and avoidance involves the use of provisions and 'loopholes' in the tax law which were not intended by policymakers. In the absence of closing these off, the revenue base will shrink relative to that projected in the forward estimates. The Government is committed to addressing these problems by way of a fundamental tax reform programme that has, as one of its aims, the formation of a simpler and fairer tax system. At the same time, the Government will continue to take legislative action to close off such schemes as they are identified. In addition, the Australian Taxation Office (ATO) will continue to undertake extensive compliance enforcement work, including pursuing matters through the courts, to maintain the integrity of the tax system.

Financial innovation has increased dramatically during the past two decades and the tax system has generally not kept pace with these innovations. Consequently, uncertainty has arisen over the application of existing laws to new and often complex financial arrangements. Also, the scope for tax minimisation and avoidance through the application of financial engineering has expanded. An Issues Paper on the taxation of financial arrangements was released by Treasury and the ATO in December 1996. Consultations have continued between officials and taxpayers as to an appropriate basis for any reforms in this area. This subject is being considered by the *Review of Business Taxation*.

The **internationalisation** of the Australian economy also introduces a general risk to the forward estimates of revenue. Income tax collections from capital are subject to increasing downward pressure due to increasing 'tax competition' among jurisdictions and 'profit shifting' in the context of the relatively free international flow of capital. The ATO is undertaking a series of compliance improvement measures to ensure that Australian companies deal with their international parties at 'arms length'. Income tax collections from labour are also coming under increasing downward pressure as a rising proportion of labour becomes more internationally mobile and subject to tax competition. The further integration of economies also means the integrity of each country's tax system will increasingly rely on international co-operation on tax matters.

Developments in **communications technology**, such as the Internet, also raise a general risk to the forward estimates of revenue. Such developments may allow the purchase or sale of an increasing number of goods and services — including the provision of labour services — in a way which could render traditional tax collection mechanisms unworkable, posing a major challenge for tax system design. The OECD is developing a taxation framework to apply to electronic commerce which will include 'place of taxation' rules for consumption taxes and measures to strengthen international co-operation in tax administration and collection. Australia is contributing actively to this work. The ATO has sought to raise awareness of the issue in its publication *Tax and the Internet*.

Developments in workplace arrangements may also affect taxation collections. Australia's tax system is characterised by a progressive system of personal income tax rates, combined with a flat company tax rate. Typically, the top marginal tax rate has been higher than the company tax rate. The divergence between the rates of personal and company tax provides an opportunity for some individual taxpayers, who would otherwise be subject to higher rates of personal income tax, to derive income through a corporate structure to take advantage of features of the corporate tax regime (for example, the lower company tax rate). In response to such activity (termed 'alienation of personal services income'), the Commissioner of Taxation is taking appropriate steps to safeguard the intended operation of the law, including testing the law in the courts.

Court decisions also increase the risk that revenue will be lower or higher than anticipated. Court decisions can affect the interpretation of tax legislation and, in the absence of Government action, can significantly change the level of revenue collected under that legislation.

Tax expenditures are often at risk of being exploited in an unexpected manner, which can also have a significant effect on the forward estimates of revenue. The Government receives a steady stream of calls for new tax expenditures to be granted. As a general proposition, the granting of further tax expenditures will lead to the downward adjustment of the forward estimates of revenue. Equally, the winding back of existing tax expenditures will generally require the upward adjustment of the forward estimates of revenue. As a result of a decision in the 1996-97 Budget, all tax expenditures will be subject to ongoing monitoring and evaluation to determine whether they remain relevant to meeting the Government's priorities.

Apart from the abovementioned general risks, which could have a cumulative impact over time, there are general risks to the forward estimates which could have a significant effect in any one-year, but not necessarily a cumulative effect over time. In any one year, revenue will be influenced by a number of factors, including for example, the degree to which companies and individuals realise losses and capital gains, the valuation of stocks, the utilisation of specific tax expenditures and taxpayer behavioural responses to revenue measures. Such factors can have a particularly significant effect on company tax collections and the revenue forgone through tax expenditures. Generally, such factors are not, by their nature, able to be forecast with a high degree of certainty.

Specific Risks

There are also a number of specific risks to revenue that are currently the subject of ongoing analysis and evaluation by the Treasury and the ATO. Such risks include, for example, specific tax minimisation and avoidance schemes. Early detection and government response to such risks is desirable. It would be inappropriate to explicitly identify such current specific risks until the Government is in a position to respond to the risks. To do so may compromise the Government's policy response and magnify the downside risks to the forward estimates of revenue.

The Government has announced a number of measures to date that have already been factored into the forward estimates of revenue but are yet to be passed by Parliament. Should the passage of legislation relating to these measures be delayed, amended or rejected, the forward estimates would need to be adjusted.

Review of 'Nuisance Tariffs'

On 24 July 1998 the then Minister for Industry, Science and Tourism announced a review of all tariffs less than five per cent and which raise less than $100,000 in revenue in a year ('nuisance tariffs'). Industry has been consulted on all tariff items that raise little revenue and provide little or no protective benefit to Australian industry. The review has been completed and is currently under government consideration.

Review of the General Tariff Rate

Under the 1994 Bogor Declaration, Asia-Pacific Economic Cooperation members committed to 'free and open' trade and investment in the region by 2010 for developed economies and 2020 for industrialising economies. As part of Australia's Individual Action Plan the general tariff rate (currently at five per cent) is scheduled to be reviewed by the end of the year 2000.

Sale of Radio Frequency Spectrum Licenses

The Commonwealth has announced the release of spectrum licenses for sale. The estimates of the proceeds from the sale of spectrum licenses are based on current market information. However, the actual amount realised will also depend on market conditions. Further sales are expected to occur in 1999-2000 and may be deferred if market conditions prove unfavourable.

Fiscal Risks — Expenses

Agriculture, Fisheries and Forestry

Exceptional circumstances

Additional expenditure on exceptional circumstances relief is subject to climate variability which cannot be predicted with any degree of certainty. The number of Exceptional Circumstances Relief Payment recipients and exceptional circumstances interest rate subsidies approved will vary significantly each year, depending on the severity of drought and other exceptional circumstances.

Attorney-General's

Native Title cost sharing

The Commonwealth has previously offered to assist States and Territories (hereafter States) in meeting compensation costs associated with their validation of past acts under legislation complementary to the *Native Title Act 1993*. Following the High Court's *Wik* decision, the Commonwealth's offer has been extended to cover intermediate period acts and certain specified future acts.

The extent of Commonwealth payments to the States pursuant to this offer will depend on the terms of the final financial assistance agreements with the States and the level of compensation liabilities arising from actions by the States to acquire native title rights. Those liabilities cannot be quantified due to uncertainty about future acts by the States and the extent and valuation of surviving native title. The Commonwealth has also offered to assist States and Territories with the costs of bodies established under State alternative provisions approved by the Commonwealth Minister to deal with native title claims, and to hear and determine objections to proposed future acts. The extent of this assistance will depend on decisions to establish such bodies, the timing of their recognition and the extent of their use.

Communications, Information Technology and the Arts

Digitisation strategy of the Australian Broadcasting Corporation

The Government has agreed to cover, at the end of the five-year conversion period (i.e. until 2002-03), outstanding debt in relation to Phase 1 of the Australian Broadcasting Corporation's plans for the conversion to digital broadcasting. That debt is currently estimated to be $31 million.

Sale of Telstra

The *Telstra (Transition to Full Private Ownership) Bill 1998* includes provision for a social bonus totalling $351 million over five years for improved communications, particularly in rural and regional areas. This funding could be placed at risk if the Bill does not pass Parliament.

Defence

Litigation cases in train — Department of Defence

The Department of Defence is involved in several cases covering a wide range of litigation where either the cases have not been heard, or damages and costs have yet to be awarded. The litigation involves Common Law liability and claims before the Human Rights and Equal Opportunity Commission, claims relating to HMAS Stalwart, HMAS Voyager, HMAS Melbourne, asbestos litigation, and alleged defective administration by the Department. In total there are some 513 claims with a value of $92 million.

Education, Training and Youth Affairs

NSW University superannuation supplementation

The NSW Government has passed amendments to legislation which offer current contributing members of the State Superannuation Scheme the opportunity to transfer from an emerging cost pension scheme to a fully funded one which provides lump sum benefits in 2000-01. Some employees of universities are members of the State Superannuation Scheme. If the offer is extended to these employees and some accept the offer, it may bring forward into 2000-01 superannuation commitments which would not otherwise have fallen due until future years. It is not possible, at this stage, to quantify the level of take-up of the offer nor its financial impact, but it is expected to be minimal.

Family and Community Services

Applying the newly arrived resident's waiting period to agreement countries

The 1998-99 Budget contained the social security measure 'Applying the Newly Arrived Resident's Waiting Period to Agreement Countries', which required New Zealand citizens to wait two years before claiming Australian income support payments. Savings of about $42 million over four years were estimated. Relevant legislation was introduced in the Autumn Sittings 1999. Even assuming passage of the legislation, the postponement of implementation (and therefore savings) could mean that the forward estimates require variation.

Modified treatment of non-economic loss compensation payments

This 1998-99 Budget measure sought to include lump-sum non-economic loss compensation payments in the income test for determining income support payments. This would remove the existing incentive for income support recipients of non-economic loss compensation payments to take lump sums in preference to on-going income support.

Legislation for this measure was introduced in the Autumn Sittings 1999, with a commencement date to be fixed by proclamation. If this measure does not pass the Senate, estimated expenditure would increase by some $50 million over the budget and forward estimates period.

Possible Social Security Agreements

The Government is continuing negotiations with a number of countries regarding possible revisions to, or new, social security agreements which would cover those people who have lived part of their working lives in both countries. Depending on their terms, individual agreements could have financial implications ranging from net savings to costs of up to $25 million a year.

Finance and Administration

Asset sales

The major asset sale provided for in the 1999-2000 Budget figuring was the sale of a further 16 per cent of the Commonwealth's remaining equity in Telstra Corporation.

The revised estimates include the effect of the sale of the remainder of Telstra, noting that the level of proceeds will depend, *inter alia*, on the prevailing levels of world equity markets at the time of the sale. The first stage of the sale will leave majority control in Government hands. Revenue from the sale could be placed at risk if the *Telstra (Transition to Full Private Ownership) Bill 1998* does not pass Parliament.

While the sale of Telstra does not impact on the operating result, any profit on the sale of Telstra would be classified as an abnormal item and impact on the adjusted operating result.

Australia Post — notional account surplus

The employer payments made by Australia Post for its past and present employees who are members of the Commonwealth Superannuation Scheme (CSS) are in excess of the payments required to fund past and future liabilities for these members. The adequacy of these payments is tracked through an actuarial assessment of Australia Post's notional account.

Every three years an actuarial review of the notional account is undertaken. The review revalues the notional account taking into consideration demographic and financial changes since the previous review. A review of Australia Post's notional account is currently being undertaken based on data as at 30 June 1998. It is expected that the surplus will increase, however, it is not possible at this time to quantify the amount.

Member choice and Commonwealth Superannuation Arrangements

New superannuation arrangements for Commonwealth employees have been provided for in the budget and forward estimates although the arrangements are subject to the passage of legislation currently before the Parliament. These new arrangements involve the closure to new entrants of the Public Sector Superannuation Scheme (PSS) from 1 July 1999 and the choice for new employees of either a complying superannuation fund or a Retirement Savings Account offered by their employer. Existing employees will have a similar choice from 1 July 2000 if they wish to cease their membership of the PSS or the Commonwealth Superannuation Scheme. Incorporation of the new superannuation arrangements in the Budget has increased expected superannuation payments by $12 million in 1999-2000, $265 million in 2000-01, and $295 million in 2001-02 without increasing the superannuation costs to employers. These amounts are a bringing forward of future cash payments (ie. discharge of liability) and therefore represent no additional expense to the Budget.

Health and Aged Care

Australian Health Care Agreements

The Commonwealth and all States and Territories, except Western Australia and Tasmania, signed five-year Australian Health Care Agreements (AHCA), commencing 1 July 1998. Western Australia accepted the AHCA proposal in-principle on 3 August 1998, and Tasmania did likewise on 1 April 1999. The Agreements incorporate a risk sharing arrangement for changes in the private health insurance participation rate. Under this formula, a nationally consistent rise of one percentage point in the participation rate above a point midway between the March 1998 and June 1995 levels will reduce Commonwealth grants to the States and Territories by approximately $82 million a year from 1999-2000. Commonwealth grants will be increased by a similar amount from 1999-2000 if the participation rate falls by one percentage point below the December 1998 level (based on current estimates of movements in population, the hospital output cost index, and assuming those leaving private health insurance have the same age/sex profile as those remaining).

The AHCA funding formula applies the hospital output cost index to total funding. However discussions with the States on specification of the index in 1999-2000 and beyond have not been completed. For every one percentage point change in hospital output costs (relative to the budget assumption of a 0.5 per cent increase), grants to the States and Territories will change in aggregate by approximately $60 million a year.

Immunisation funding mechanism

Future vaccine technology will result in new vaccines substituting for ones already in use (eg multivalent vaccines which combine several vaccines into one) and, as a consequence, could result in higher unit costs of vaccine within the routine schedule. Given the nature of current vaccine technology, and the possible introduction of new vaccines, specific vaccine costs cannot be precisely quantified at this stage. The inclusion of new essential vaccines within the routine schedule has the potential to increase Commonwealth outlays by up to $120 million in total over the next four years.

Litigation cases in train — Department of Health and Aged Care

The Department is presently involved in 61 cases which could result in some financial liability for the Commonwealth. These cases cover a wide range of litigation, where either the cases have not been heard or damages and costs have yet to be awarded. The litigation now involves Creutsfeldt-Jacob disease, Acquired Immune Deficiency Syndrome, Hepatitis C, defective products, personal injuries, the Department as an employer, and a variety of other claims against the Commonwealth. It is not possible to quantify the liability arising from these cases.

Major new listings — Pharmaceutical Benefits Scheme and Medicare Benefits Scheme

From time to time new items are added to the Medicare Benefits Scheme and Pharmaceutical Benefits Scheme schedules. To a certain extent the existing forward estimates take account of these additions. However, major new developments in medicines or medical procedures could result in increases in expenses which exceed the provision in the forward estimates. It is not possible to quantify the fiscal risk arising from such potential developments.

Immigration and Multicultural Affairs

Temporary safe have in Australia for displaced Kosovars

The Government's decision on 1 May 1999 to activate plans to provide temporary safe haven in Australia for 4,000 displaced Kosovars will result in some financial impact in both 1998-99 and in 1999-2000. Whilst extensive preparations were under way in Australia, the uncertainty at the time of finalising the 1999-2000 Budget was such that the resource implications were not included in the budget estimates.

Industry, Science and Resources

Repayment of Snowy Mountains Hydro-electric Scheme debt

The expected corporatisation of the Scheme in 1999-2000 will involve the refinancing and early repayment of debt to the Commonwealth. The estimated market value of the debt is in the order of $900 million. Detailed arrangements are to be finalised between the Commonwealth and NSW and Victorian Governments, as shareholders in the new company. The exact timing and level of payments may be influenced by electricity and financial markets at the time of corporatisation.

Prime Minister and Cabinet

Hindmarsh Island bridge damages claim

Developers of a marina associated with the proposed Hindmarsh Island bridge have brought a substantial damages claim against the Commonwealth and other parties involved in the decision by the previous Minister for Aboriginal and Torres Strait Islander Affairs, pursuant to the *Aboriginal and Torres Strait Islander Heritage Protection Act 1984*, to ban construction of the bridge. The plaintiffs are claiming damages of $20 million.

Separation of Aboriginal children from their families in the Northern Territory

Earlier laws, policies and practices led to the separation of many Aboriginal and Torres Strait Islander children from their families. Some 2,200 claims for damages are underway against the Commonwealth in relation to alleged forced separations. If the applicants in the two test cases proceeding in 1999 are successful, the Commonwealth may be liable for substantial payments in relation to these and other claims, which could amount to hundreds of millions of dollars.

Investment incentives

In the December 1997 *Investing for Growth* industry statement, the Government announced its willingness to consider the provision of incentives, in limited and special circumstances, for major strategic investment projects. Such incentives could be in the form of expense (grants) or revenue (taxation concession) measures.

Transport and Regional Services

Compensation claims — finalisation of acquisition of properties for the Second Sydney Airport at Badgerys Creek

Compensation claims under the *Lands Acquisitions Act 1989* relating to the compulsory acquisition of properties for the proposed Second Sydney Airport at Badgerys Creek, give rise to an estimated risk of $30 million.

Maritime Industry Reform

On 18 August 1998 the Commonwealth provided a guarantee to cover borrowings made by the Maritime Industry Finance Company (MIFCo) to finance redundancy related payments in the stevedoring and maritime industries. MIFCo's borrowing facility, negotiated with its bankers, is presently $155 million. This facility is expected to be increased to meet the larger than originally anticipated redundancy costs in the stevedoring industry. Amendments will be introduced as part of the 1999-2000 Budget to increase the expenditure cap in the *Stevedoring Levy (Collection) Act 1998* from $250 million to $350 million.

Treasury

Australia's involvement in the International Monetary Fund (IMF) assistance to Thailand, Indonesia and the Republic of Korea

In response to instability in regional financial markets and economies, Australia offered to provide bilateral financing in support of IMF programmes in Thailand, Indonesia and the Republic of Korea. In the case of Thailand, this has taken the form of a currency swap between the Reserve Bank of Australia (RBA) and the Bank of Thailand for $US1 billion which is being drawn down over a three-year period. In the event of default, the ability of the RBA to maintain the dividend stream projected in the forward estimates may be affected.

Australia has offered to provide supplementary financing or 'second tier' financing of up to $US1 billion for each of Indonesia and Korea. This financing would be provided via a loan on a non-concessional basis. With subsequent improvement in economic conditions in Korea, no payment is now expected to be required. Negotiations for the provision of up to $US300 million to Indonesia are proceeding.

Contingent Liabilities — Quantifiable

Agriculture, Fisheries and Forestry

Australian Wheat Board (AWB)/AWB Ltd

Under the *Wheat Marketing Act 1989*, the Commonwealth underwrites borrowings by the AWB and AWB Ltd that fund advance and related payments from open wheat pools up to a maximum of $3,018 million as at 22 March 1999. Borrowings are repaid as the wheat is sold. The Commonwealth's responsibility for the underwriting of borrowings will cease after the 1998-99 season and previous season's pools are finalised by AWB Ltd.

Queensland Fisheries Management Authority

The Commonwealth guaranteed a loan of up to a maximum of $40.9 million to encourage the restructuring of the Northern Prawn Fishery. As at 31 March 1999, the amount outstanding on the loan was $3.5 million, which is to be paid off within one year. The loan was taken out by the Queensland Fisheries Management Authority on behalf of the Commonwealth to buy back surplus boat units from the fishery with repayment to be made by the industry through levies.

Wool International

Under Section 53(7) of the *Wool International Act 1993*, the Commonwealth underwrites borrowings of Wool International for the management of the wool stockpile. The contingent liability for borrowings by Wool International totalled $235 million as at 31 March 1999.

Communications, Information Technology and the Arts

Australian Broadcasting Corporation

The Commonwealth has guaranteed loans by the Australian Broadcasting Corporation. The principal amount covered by the guarantee as at 31 March 1999 was $155 million. These loans were largely used to meet costs relating to the construction of premises for the Corporation at Southbank (Melbourne) and Ultimo (Sydney).

Special Broadcasting Service

The Commonwealth has guaranteed loans taken out by the Special Broadcasting Service. The principal amount covered by the guarantee as at 31 March 1999 was $39 million. These loans were used to pay for the refurbishment and enhancement of the Service's premises at Artarmon in Sydney.

Telstra Corporation Ltd — Loan Guarantee

The Commonwealth has guaranteed loans taken out by Telstra Corporation Ltd. The principal amount covered by the guarantee as at 31 March 1999 was $41.25 million. The loan was originally issued prior to July 1989 when most of Telstra's borrowings were guaranteed by the Commonwealth. The loan will be fully repaid on 15 November 1999.

Telstra Corporation Ltd — Superannuation Guarantee

Telstra Corporation Ltd has agreed to make additional employer contributions to the Telstra Superannuation Scheme. The Commonwealth has guaranteed that it will cover any outstanding additional employer contributions in the event that Telstra becomes insolvent. The net present value of the contingent liability in respect of the guaranteed stream of payments for the Telstra Superannuation Scheme as at 30 June 1998 was $1.1 billion.

Art Indemnity Australia

The amount indemnified for artworks on loan to galleries participating in exhibitions under the Scheme has decreased to $19.4 million as at 31 March 1999. The decrease is due to only one exhibition being covered by the program at that date.

Defence

Defence Housing Authority

Private sector borrowing by the Defence Housing Authority is explicitly guaranteed by the Commonwealth under section 38 of the *Defence Housing Authority Act 1987*. The value of loans guaranteed at 30 April 1999 was $40 million.

Military Compensation

Contingent liabilities exist in relation to military compensation claims to the value of some $27.9 million. This amount relates to outstanding claims for non-economic loss as a consequence of the Federal Court decision in *Schlenert v the Australian and Overseas Telephone Corporation 1995*.

Education, Training and Youth Affairs

Commonwealth Loan Guarantees — Group Training

The Minister for Education, Training and Youth Affairs is authorised to issue Commonwealth guarantees on a limited number of loans made to Commonwealth endorsed Group Training companies by commercial lenders in the period 18 February 1999 to 30 June 2001. These guarantees assist Group Training Companies to gain access to additional working capital required to expand the number of apprentices and trainees that may be employed through Group Training companies. The maximum guarantee of each loan is $175,000 with the total value of all guarantees capped at $30 million.

Commonwealth Loan Guarantees — ABSTUDY Financial Supplement Loan Scheme

The ABSTUDY Financial Supplement Loan Scheme provides tertiary students with the option of obtaining additional living and educational expenses while studying. Loans are made to students through an arrangement with the Commonwealth Bank of Australia (CBA) and the Commonwealth purchases the loans on 31 May in the fifth year after the loan was taken out. The Commonwealth commences recovery action when a student's income reaches the pre-determined threshold.

In the 1998-99 Budget there was an ABSTUDY Loan Supplement contingent liability of $146 million, relating to loans which had not been purchased back from the CBA. As at 16 April 1999, the value of loan guarantees outstanding for ABSTUDY Supplement recipients was in the order of $175 million.

Finance and Administration

Telstra Corporation Ltd — Notional Account Surplus

The employer payments made by Telstra for its past and present employees who are members of the Commonwealth Superannuation Scheme (CSS) are in excess of the payments required to fund past and future liabilities for these members. The adequacy of these payments is tracked through an actuarial assessment of Telstra's notional account.

A review of Telstra's notional account was completed earlier this financial year. The total surplus was determined at $1,428 million as at the valuation date of 30 June 1997. This surplus will be paid to Telstra Superannuation Scheme either by way of a schedule of instalments or by way of a lump sum.

Foreign Affairs and Trade

Export Finance and Insurance Corporation (EFIC)

The Commonwealth guarantees the due payment by EFIC of money that is, or may at any time become, payable by EFIC to any person other than the Commonwealth. As at March 1999, the contingent liability totals $7,681.3 million, comprising contracts of insurance and guarantees ($3,606.1 million), liabilities ($965.7 million) and national interest provisions ($3,109.5 million).

Assistance for East Timor

The Government has made clear that Australia will provide substantial assistance to an autonomous or independent East Timor. Assistance during and after the transition process will be crucial to peace and stability, and the longer-term development of East Timor. Australia has already pledged $20 million in 1998-99 to assist the UN consultation process that will allow the East Timorese people determine their future. This is in addition to the $7 million provided in 1998-99 through our aid program to Indonesia. An expansion of the aid program to East Timor is planned for 1999-2000. Decisions on the level and nature of this assistance will be taken once the outcome is clearer. Some financial provision for support for East Timor has been allowed for in the Contingency Reserve for the 1999-2000 Budget.

Industry, Science and Resources

Australian Industry Development Corporation (AIDC)

As at 1 November 1998, the Corporation's contingent liabilities were $206.5 million in respect of guarantees and credit risk facilities. The Corporation's other guaranteed borrowings, which totalled $1,793 million as at 1 November 1998, have been offset by holdings in Commonwealth Government securities and certain hedging instruments guaranteed by Warburg Dillon Read (formerly known as UBS Australia Ltd).

Australian Industry Development Corporation (AIDC) in relation to the Australian Submarine Corporation

On 16 December 1998, the Department of Defence (Defence) accepted a Commonwealth guarantee for $26.6 million in relation to the Commonwealth's interest in the Australian Submarine Corporation (ASC). The Commonwealth through the Australian Industry Development Corporation (AIDC) holds a substantial but minority interest in the ASC.

The Commonwealth provided the guarantee to cover the AIDC's obligations under an agreement with the Westpac Banking Corporation in which the bank provides an extended performance guarantee to Defence in respect to the Collins class submarines. The termination date of the guarantee is 31 December 2001.

The Commonwealth has also agreed to indemnify the AIDC in relation to its obligations under the performance guarantee agreement.

Snowy Mountains Hydro-electric Authority (SMHEA)

The *Snowy Mountains Hydro-electric Power Act 1949* provides that borrowings by SMHEA may be guaranteed by the Commonwealth. The Authority has issued inscribed stock at a discount to finance capital works of the Scheme. The borrowings are subject to explicit Commonwealth guarantees. The face value of guaranteed borrowings is $181.5 million with the net amount guaranteed (excluding the unamortised discount on the issue of inscribed stock) being $98.2 million.

Transport and Regional Services

Federal Airports Corporation (FAC) — Wind Up

On 24 September 1998 the Commonwealth assumed responsibility for all remaining assets, liabilities and contracts of the FAC on the wind-up of the Corporation. Unpresented cheques of $2 million have been identified and provided for. There is no basis for quantifying any potential claims beyond this amount.

Treasury

Guarantees under the Commonwealth Bank Sale Act 1995

Under the terms of the *Commonwealth Bank Sale Act 1995,* the Commonwealth has guaranteed various liabilities of the Commonwealth Bank of Australia, the Commonwealth Bank Officers' Superannuation Corporation (CBOSC) and the Commonwealth Development Bank.

The guarantee for the Commonwealth Bank of Australia relates to both on and off-balance sheet liabilities. Of the existing contingent liability, 34 per cent involves off-balance sheet liabilities. As at 30 June 1998, the balance of the guarantee was $99,745.9 million, a reduction of $4,428.2 million on the previous year.

The guarantee for CBOSC covers the due payments of any amount that is payable to or from the Fund, by CBOSC or by the Bank, in respect of a person who was a member, retired member or beneficiary of the Fund immediately before 19 July 1996. Total accrued benefits at 30 June 1998 have been valued at $3,743 million following an actuarial review. The outstanding value subject to the guarantee is estimated to be $3,737 million.

As of 1 July 1996, the Commonwealth Development Bank ceased to write new business and no additional liabilities are being incurred. The existing contingent liability will gradually decline with the retirement of existing loans and exposures. The revised estimate for the balance of this guarantee was $472.5 million as at June 1998.

Reserve Bank of Australia (RBA) guarantee

This contingent liability relates to the Commonwealth's guarantee of the liabilities of the RBA. The major component of RBA liabilities relates to Notes (ie currency) on Issue. This treatment of Notes largely relates to the historical convention of the convertibility of

Notes to gold — coins are not treated as a liability in the Commonwealth's accounts. At 7 April 1999, Notes on Issue totalled $23,697 million.

The other major liability consists of deposits with the RBA by the banking sector. At 7 April 1999, these deposits amounted to $5,928 million. In total, the guarantee for the Reserve Bank was $37,916 million as at 7 April 1999.

Uncalled Capital Subscriptions — international financial institutions

The liability relates to the value of the uncalled portion of the Commonwealth's shares in the International Bank for Reconstruction and Development ($US2,769.5 million — estimated value $A4,496.7 million at 31 December 1998), the Asian Development Bank ($US2,477.5 million — estimated value $A4,022.6 million), and the European Bank for Reconstruction and Development ($US71,220 million — estimated value $A115,635.7 million).

Contingent Liabilities — Unquantifiable

Attorney-General's

Australian Federal Police Adjustment Scheme (AFPAS)

Under section 30(2) of the *Australian Federal Police Act 1979*, all Australian Federal Police (AFP) appointees who complete a fixed term appointment are entitled to a payment upon separation from the organisation. Funding has been provided for the costs expected to be incurred over the next two years, but actual expenditure is subject to the number of staff separations. In 1999, the Government will consider proposals to extinguish the Australian Federal Police Adjustment Scheme liabilities.

Communications, Information Technology and the Arts

Year 2000 compliance

The Commonwealth provided $120 million to agencies to upgrade their systems during 1998-99 for redeveloping or replacing non-compliant software and hardware, and developing contingency plans to permit business operations to continue should systems fail on 1 January 2000. Progress by agencies in ensuring that their systems are Year 2000 compliant is monitored by quarterly reporting to Government, with the results of these reports being published. The exact costs of the Year 2000 compliance program will not become apparent until some time after 1 January 2000.

Defence

HMAS Melbourne compensation

The decision in the *Mewett v Commonwealth* case may be used as a precedent by up to 900 crewmen of HMAS Melbourne, in relation to the Voyager incident, to lodge claims against the Commonwealth. Some 95 claims have been lodged to date (noted in *Fiscal Risks–Expenses*) however there is no basis for quantifying further claims.

Employment, Workplace Relations and Small Business

Possible increased workers' compensation costs to the Commonwealth

The decision in *Australian Postal Corporation v Burch* handed down by the Full Federal Court on 5 August 1998 may increase workers' compensation costs for the Commonwealth.

Finance and Administration

Australian Law Reform Commission (ALRC) employees

Notice of potential claims under the Commonwealth Funds Management (CFM) share sale agreement has been received from the Commonwealth Bank in relation to an action brought against CFM (among others) as successor to the former Superannuation Fund Investment Trust by certain employees of the Australian Law Reform Commission in respect of their superannuation entitlements. The Commonwealth has exercised its right to take over the defence of the action. The financial effect of this claim cannot be quantified at this stage.

Commonwealth Civilian Superannuation Liability

Every three years an actuarial review of the Commonwealth's unfunded liability in respect of the Public Sector Superannuation Scheme (PSS) and the Commonwealth Superannuation Scheme (CSS) is undertaken. The next review, due by 30 June 2000, will be based on data as at 30 June 1999. The review revalues the unfunded liability to take account of demographic and financial changes since the previous review. It is not possible at this time to quantify the net change in the unfunded liabilities.

Commonwealth shareholding in the Australian Submarine Corporation

An indemnity was issued to Barry AC Hilson and BACH Pty Limited in relation to liabilities arising from assistance provided to the Commonwealth during the conduct of a review of the Commonwealth's shareholding in the Australian Submarine Corporation. This indemnity is ongoing.

Macquarie Bank — DASFLEET

Macquarie Fleet Leasing Pty Ltd, as purchaser of DASFLEET, have disputed the valuation methodology adopted by the Commonwealth in the Completion Asset and Liability Statement in relation to the vehicle fleet. This matter is subject to arbitration.

The Commonwealth is also in dispute with Macquarie Fleet Leasing on matters associated with the Tied Contract.

New Commonwealth Insurable Risk Managed Fund (Comcover)

From 1 July 1998, the Government has progressively replaced the previous non-insurance policy with one of self-insurance via a managed fund (Comcover). The managed fund will produce better risk management and therefore reduce costs over time.

Comcover is also progressively covering the insurable risks of bodies under the *Commonwealth Authorities and Companies* (CAC) *Act 1997* within the general government sector. Premiums are being charged by the fund to cover the long-term cost of risk and associated administrative costs.

A reinsurance programme has been put in place to reduce the likelihood of significant impacts on the Budget from CAC body and FMA agency exposures.

Superannuation Act 1976 and the Public Sector Superannuation Scheme (PSS)

Under the *Superannuation Act 1976* (for the Commonwealth Superannuation Scheme (CSS)) and the PSS Trust Deed and Rules and determinations made under them, the Commonwealth guarantees payment of the amounts of members' contributions and productivity contributions with interest allocated to those amounts by respective Boards of Trustees.

The CSS and the PSS guarantee the accrued contributions and interest so there cannot be a negative credit rating on invested funds. The Commonwealth has not had to make a payment in relation to this guarantee.

Indemnities for the Reserve Bank of Australia (RBA)

The Commonwealth has indemnified the RBA against loss and damage arising from the acceptance of certain Commonwealth cheques bearing a facsimile signature having been impressed thereon without the authority of the Commonwealth and other aspects of banking services provided by the Bank.

Sale of Australian River Co. Limited (formerly ANL Limited)

The sale of Australian River Co.'s businesses has been completed. The sale terms provide for certain contingent liabilities related to warranties, indemnities and employee matters. The limit on warranty claims is purchase price with a minimum and aggregate claim and a time period of 21 months from December 1998. In relation to employee matters, the Sale Deed provides for the Commonwealth to reimburse redundancy payments that are capped at a maximum of $11 million.

Sale of the National Transmission Network

The National Transmission Company Pty Ltd was established by the Commonwealth to effect the sale of the National Transmission Network. An indemnity was provided to the person appointed as the sole director, secretary and public officer of the Company pending the sale of the shares. The indemnity covers all costs, losses, expenses or liabilities incurred as an officer of the Company, and was issued on 16 February 1999.

Privatisation of Wool International

Indemnities were issued to the Members of Wool International indemnifying them against all actions, suits, claims demands or proceedings and costs, arising from, or as a consequence of providing information and assistance for the purposes of the privatisation. The indemnities cover assistance given in accordance with a Ministerial Direction and the Memorandum of Understanding (between the Commonwealth and the Members of Wool International). The indemnity is a continuing indemnity in respect of any liability that arises from assistance prior to completion of the project.

Indemnities relating to other Asset Sales

Indemnities have been given in respect of a range of other asset sales. Details of these indemnities have been provided in previous Budget and MYEFO papers, for example see pages 100-103 in the 1998-99 MYEFO.

Health and Aged Care

CSL Ltd

CSL Ltd is indemnified against claims made by persons who contract specified infections from specified products and against employees contracting asbestos related injuries. CSL Ltd has unlimited cover for most events that occurred before the sale of CSL Ltd on 1 January 1994, but has more limited cover for a specified range of events that might occur during the period of the current contract. Given the open-ended nature of some of the indemnities, damages and risk cannot be quantified.

Transport and Regional Services

Civil Aviation Safety Authority (CASA) — indemnity to officers of the Authority administering the Carrier's liability insurance requirements

An indemnity has been given to those officers of CASA who administer the carrier's liability insurance requirements under Part IVA of the *Civil Aviation (Carrier's Liability) Act 1959* and complementary state legislation. This indemnity was revoked with effect from 29 August 1998 as CASA has obtained commercial insurance covering the risks specified in the indemnity. The indemnity will still apply in relation to liabilities associated with acts or omissions that occurred before the date of revocation.

Federal Airports Corporation (FAC) — transfer of former contingent liabilities to the Commonwealth

As part of the wind-up of the FAC, the Commonwealth assumed responsibility on 1 July 1998 for a contingent liability of the Corporation which relates to debtors of the FAC who are challenging the validity of network charges made under the *Federal Airports Corporation Act 1986*. If the network charging approach is found to be invalid, this raises the prospect of further claims from other airport users who have previously paid network based charges to the Corporation. There is no basis for quantifying potential claims.

Tripartite Deed relating to the Core Regulated Airports

Tripartite Deeds apply to the 12 Core Regulated Airports (Sydney, Melbourne, Brisbane, Perth, Canberra, Coolangatta, Townsville, Adelaide, Hobart, Launceston, Darwin and Alice Springs). The Tripartite Deeds between the Commonwealth of Australia, airport lessees and lessees' financiers provide for the Commonwealth to 'step-in' as airport operator in defined circumstances. The potential liability of the Commonwealth would vary considerably with the specific factors leading to such an action. If the Commonwealth entered into possession of an airport site it could seek to recover its costs from a number of sources, including airport revenues.

Maritime Industry Finance Company Ltd (MIFCo) — board members' indemnity

Indemnities for MIFCo board members have been provided to protect against civil claims relating to employment and conduct as directors of MIFCo. These indemnities are unquantifiable and no expiry date has been set.

Stevedoring Industry Finance Committee (SIFC)

The Stevedoring Industry Finance Committee (SIFC) has 18 claims for asbestos related damage awaiting High Court decision. These claims were inherited from the Australian Stevedoring Industry Authority. Costs that may arise from these claims can not be determined and are therefore unquantifiable. Any future claims made resulting from the High Court's decision are also unquantifiable.

Treasury

Changes in the net principal value of cross currency swaps and foreign currency denominated debt resulting from changes in the nominal exchange rate

Significant net foreign exchange gains or losses may be recorded in the operating statement if there is a significant change in the nominal exchange rate. This is because a change in the nominal exchange rate results in a change in the net principal value of cross currency swaps and foreign currency denominated debt. The direction of movement in the exchange rate will determine whether there is a net foreign exchange gain or a loss. A gain is a positive risk to the operating result, while a loss is a negative risk. Net foreign exchange gains or losses do not have any impact on the fiscal balance.

Veterans' Affairs

Vietnam Veterans' Health Study

A clear commitment on the part of the Government has been made to fund the results of the Vietnam Veterans Health Study. Finalisation will occur as soon as the results are validated. This is expected in the latter part of 1999.