Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2008–09

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Victorian Auditor-General's Office

Auditing in the Public Interest

The Hon. Robert Smith MLC
President
Legislative Council
Parliament House
Melbourne

The Hon. Jenny Lindell MP
Speaker
Legislative Assembly
Parliament House
Melbourne

Dear Presiding Officers

Under the provisions of section 16AB of the *Audit Act 1994*, I transmit the *Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2008–09.*

Yours faithfully

D D R PEARSON
Auditor-General

24 November 2009

Contents

Audit summary

This is the third of six reports to Parliament scheduled for 2009–10 covering the results of the annual financial report audits of the Victorian state and local government sectors. This report provides the results of the audit of the Annual Financial Report (AFR) of the State of Victoria.

The key conclusion from this audit is that Parliament can have confidence in the Annual Financial Report of the State of Victoria.

Our external audit provides authoritative independent assurance that the Treasurer and the Minister for Finance, WorkCover and the Transport Accident Commission have prepared the AFR consistent with the provisions of the *Financial Management Act 1994* (FMA) and applicable accounting standards.

The AFR details the state's cost of operations, revenue, impacts of market re-measurement on the value of assets and liabilities, the value of what it owns and what it owes. In the AFR, information is provided at the:

- state level which aggregates the three sectors of government, the general government sector (GGS), the public non-financial corporations (PNFC) and the public financial corporations (PFC) to present a whole-of-government perspective, and
- GGS level separated out to provide a perspective of the operations of the budget funded sector of government.

A clear audit opinion on the 2008–09 AFR was issued on 29 September 2009 and included in Chapter four of the Financial Report that was tabled in Parliament on 14 October 2009 in line with the timing required by legislation.

However, the AFR preparation timetable was not achieved due to the late provision of certified financial data by 34 (79 per cent) material entities and lengthy considerations regarding the recognition and measurement of land under roads and the measurement of infrastructure assets at fair value.

Financial performance and position of the state

In 2008–09 the net result, including transactions and other economic flows, for the state was a deficit of $13 088.8 million (deficit of $3 165.9 million, 2007–08) largely reflecting the second year of actuarial losses by the state's defined benefit superannuation plans combined with realised and unrealised losses on financial instruments due to financial market conditions.

The net result from transactions for the state was a deficit of $62.9 million in 2008–09 (a surplus of $1 638.6 million, 2007–08) again largely reflecting the impact of the global financial crisis. The general government sector (GGS) net result from transactions was a surplus of $251.2 million in 2008–09 ($1 646.6 million, 2007–08) which exceeded the revised key financial objective of a net result from transactions of at least $100 million. The achievement of this target was primarily due to the recognition of fiscal stimulus funding from the Commonwealth and higher sales of goods and services and other revenue.

The state's net worth for the year increased by $26 412.8 million (29 per cent) to $118 003.6 million ($91 590.8 million in 2007–08). Notwithstanding the investment losses of $4 022.2 million, revaluation of non-financial assets of $20 263.5 million and the recognition of land under roads of $18 682.5 million more than offset the losses. These factors improved the state's net asset position.

Borrowings, provisions for insurance claims and the superannuation liability are the major obligations of the state. Total state liabilities increased during the year by $18 141.8 million (31.2 per cent) to $76 250.4 million ($58 108.6 million in 2007–08). This increase mainly reflected the impact of adverse financial market conditions, and the part funding of the State's infrastructure program from borrowings. The state's triple-A credit rating was re-affirmed by Standard & Poor's in September 2009.

While the net result from transactions for the GGS is an indicator of the government's financial performance, the financial sustainability of the state requires consideration of the state's net result. When looking at this 'bottom line' and by taking into account other economic flows, the deficits in the 2007–08 and 2008–09 net results clearly demonstrate the state's exposure to financial markets and economic conditions. These and other factors can put at risk longer-term financial sustainability and will need to be closely monitored, so that revenue and expenditure policy settings remain sustainable.

Risks to the financial performance and condition

There are a number of external factors which need to be continually monitored in managing short and long term sustainability.

External factors that could impact the state's future financial performance and condition include:

- the performance of the national economy and the policy directions and decisions of the Commonwealth Government, which significantly influence the level of Commonwealth grants to the state
- volatility in the performance of the Australian and international financial and equity markets, significantly influencing the investment revenues in the short term and superannuation expenses of the state
- demographic trends, including the ageing population, expected to affect the level and nature of services provided by the government

- the public sector workforce pressures for wage and salary growth, and the need to maintain sustainable full time equivalent (FTE) whilst meeting increased demands on government service delivery
- the implementation of any Australian emissions trading scheme and climate change.

Quality of reporting

DTF prepares the AFR in accordance with the requirements of the FMA and applicable Australian accounting standards and interpretations. Australian Accounting Standard AASB 1049 *Whole of Government and General Government Sector Financial Reporting* has particular relevance.

The quality of the AFR depends upon the accuracy of financial data submitted to DTF by public sector entities and DTF's quality assurance processes in preparing the consolidated accounts.

A direct measure of accuracy is the incidence and magnitude of the errors in the financial data submissions and the draft financial reports requiring adjustments.

In 2008–09 errors in the financial data submissions of 31 material entities (28 in 2008) were detected, indicating deficiencies in quality assurance processes of both reporting entities and DTF.

Material error was also identified in the draft disclosure notes to the AFR for commitments and contingencies. Initially the amounts disclosed in the AFR did not agree to the audited balances included in the individual entities financial reports. All these material errors were corrected in the AFR before issue of the clear audit opinion.

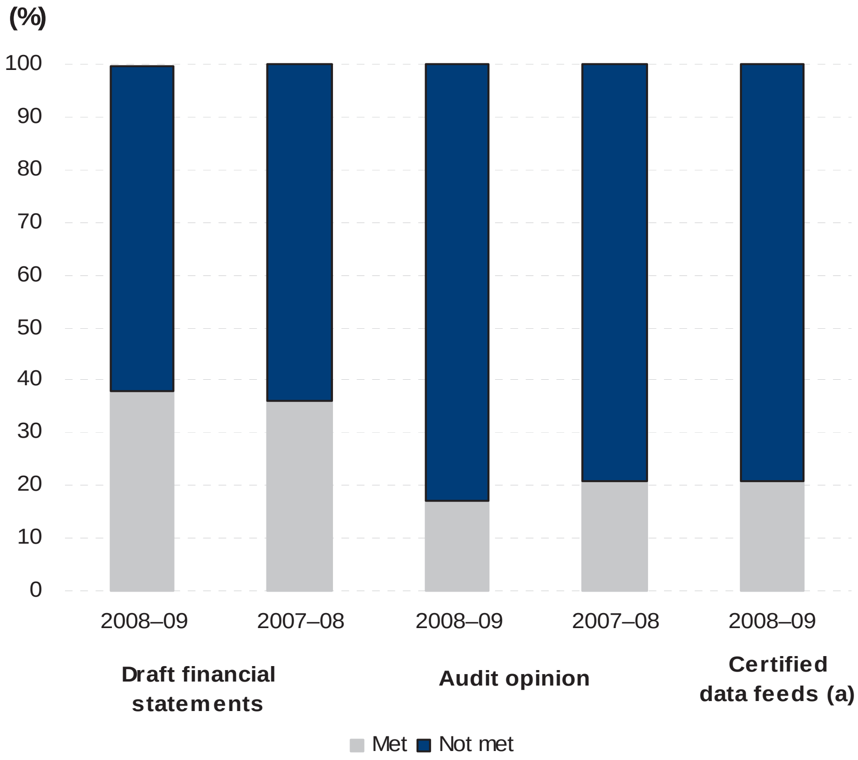
Timeliness of reporting

The timely preparation and audit of the AFR depends on the consolidated entities meeting the established AFR preparation timetable and the early identification and resolution of significant accounting, recognition, measurement, presentation and disclosure matters. The individual financial operations of these material entities are significant in the reporting of the consolidated finances of the state and collectively comprise more than 90 per cent of the state's assets, liabilities, revenue and expenditure.

Responding to last year's audit recommendation, DTF released the AFR timetable in February 2009. This timetable included earlier reporting milestone dates than the FMA legislative time frames to enable the AFR 15 October tabling date to be met.

Notwithstanding the earlier consultations and issue of the AFR timetable, fewer material entities met the time lines as summarised below.

Figure A
Timeliness of reporting for material entities 2008–09 and 2007–08



Note: (a) Comparative data not available for certified data feeds.
Source: Victorian Auditor-General's Office.

This situation highlights the ongoing need to improve processes and to better focus efforts to deliver reliable financial reports within the established time frames.

Current issues

It is important for the AFR and consolidated entities to apply consistent accounting policies so the utility and comparability of financial reports can be optimised.

The 2008–09 AFR is the first to be prepared in accordance with AASB 1049, this resulted in:

- water, rail and port infrastructure assets being measured at fair value resulting in a $15 300 million increment being reported in the AFR. However, the majority of water, rail and port entities record infrastructure assets at cost in their individual entity financial reports. This is in accordance with accounting standards and FRD 121 *Infrastructure Assets (Water/Rail)*. However, FRD 121 also requires the entities concerned to move to recording the applicable assets at fair value in their individual entity financial reports to commence either in 2009–10 or 2010–11 years.
- the recognition of $18 682.5 million of land under roads in the AFR. However, Vic Roads did not recognise land under roads in their financial report in accordance with options available in AASB 1051 *Land Under Roads* to not recognise land under roads acquired prior to 1 July 2008.

There will continue to be a variance between valuations in the AFR and the financial reports of the water and rail entities until these entities are required to implement fair valuation of infrastructure assets in their financial reports.

Assuming current revenue levels, this change in accounting policy would result in higher depreciation charges, lower net results and affect the tax related balances for these entities. These inconsistencies at 30 June 2009 highlight the need for a concerted effort to treat like transactions and events consistently to achieve optimal utility and comparability.

Significant developments

Victorian Bushfire Appeal Trust Fund

The Victorian Bushfire Appeal Trust Fund, up to 25 October 2009 had received $382 million, an increase of $9.1 million since 30 June 2009 with payments of $78.2 million being distributed to individuals and communities since 30 June. The $169.1 million ($238.2 million at 30 June 2009) balance of the fund is to be utilised to make further distributions to individuals and communities.

Post-balance date events

Victorian Desalination Plant

Construction, operation and maintenance of the Victorian Desalination Plant is to be delivered by Aquasure via a public private partnership model for the state government. Construction commenced in October 2009 with estimated construction costs of $3 500 million to be borne by Aquasure. The future financial implications of this project are not yet quantifiable because final negotiations and syndication had not been completed at 30 September 2009. The state government has provided a Treasurer's Guarantee over a portion of the plant debt, as a lender of last resort in the case that the syndication process is not successful.

Rail franchise

Operation and maintenance contracts for Melbourne's passenger train and tram networks for the eight years ending November 2017 were completed in August 2009. The train contract with United Group Limited for Metro Trains Melbourne is expected to cost the state an average of $474 million per year and the tram contract with Keolis Downer EDI an average of $97 million per year.

Other developments

Channel Deepening Project

This project is scheduled for completion by 31 December 2009 and is expected to come in ahead of schedule and under the original budget.

Food Bowl Modernisation Project

Project works have recently commenced with estimated costs for the project of $2 004.5 million. $168.1 million of this project had been spent at 30 June 2009.

Northern Sewerage Project

This project commenced in August 2007 and is on schedule for completion in mid 2012. The $650 million estimated costs for this project are to be funded by Melbourne Water Corporation and Yarra Valley Water Limited.

Myki

Myki is now operating in town buses in Ballarat, Bendigo, Geelong, Seymour, Warragul and the Latrobe Valley. It is expected that Melbourne operations will begin in late 2009. Total capital costs are forecast at $454 million, with $261.4 million of capital costs incurred at 30 June 2009. Operating costs to 30 June 2009 were $201.6 million with committed operating costs totalling $367.4 million projected over ten years commencing in 2009–10. Further capital and operating costs of $393.6 million are also forecast however these have not been contracted for at 30 June 2009.

New Melbourne Convention Centre

The new Melbourne Convention Centre was officially opened on 5 June 2009. A private sector consortium is to operate the Melbourne Exhibition and Convention Centre (MECC) for a period of 25 years which commenced on 31 March 2009. The state's total estimated costs for the MECC is $1 734 million.

Melbourne Central City Studios

The state paid $6 million for Melbourne Central City Studios in November 2008. The net assets of the studios were subsequently written down to $0.5 million and the studios continue to have a high financial viability risk.

Commonwealth Games Athlete's Village

The state's estimated cost for the Commonwealth Games Athletes Village has increased from the 2006 reported cost of $41 million to $59.1 million due to lower than expected forecast revenue. This is a result of reducing the number of apartments to be built from 650 to 632. The estimated average return for each apartment has also been reduced from $70 000 to $45 500.

Recommendations

Number	Recommendation	Page
1.	DTF should, in consultation with material entities: • develop improved processes, to achieve the required time frames, and • improve their quality assurance processes.	17
2.	Public sector entities should more rigorously align their financial reporting timetable, including audit committee and board meeting dates, to the AFR timetable.	17
3.	DTF should lead the adoption of consistent recognition and measurement policies across the Victorian public sector.	17

General

The total cost of preparing and printing this report was $160 000.

Audit Act 1994 section 16—submissions and comments

Introduction

In accordance with section 16(3) of the *Audit Act 1994,* a copy of this report, or relevant extracts from the report, was provided to all relevant agencies with a request for comments or submissions.

The comments and submissions provided are not subject to audit nor the evidentiary standards required to reach an audit conclusion. Responsibility for the accuracy, fairness and balance of those comments rests solely with the agency head.

Submissions and comments received

RESPONSE provided by the Treasurer

I welcome the Auditor-General's report, which forms an important part of the state's parliamentary accountability framework over public finances.

The report concludes that Parliament can have confidence in the AFR, which demonstrates the state's continued prudent financial management of public finances during 2008–09 and affirms the government has continued to achieve its key financial objectives, including delivering a net result from transactions (operating surplus) of at least $100 million, maintaining net financial liabilities at appropriate levels and delivering world class infrastructure to maximise economic, social and environment benefits.

The report further complements the government's assessment in the AFR of the economic and other risks impacting on the state's finances over future periods. As the AFR demonstrates, the state is well positioned to respond to these risks.

The report acknowledges the continued improvement of processes for the production of the AFR over the previous twelve months, while noting further scope to improve the timeliness and quality of input to the AFR from public sector agencies, and the related quality assurance processes. In this regard, the Department of Treasury and Finance (DTF) will continue to work closely with agencies to identify and support improvement opportunities, particularly focusing on the provision of timely advice on complex and contentious accounting policy issues, and on data submission requirements. In addition, internal quality assurance processes will continue to be refined in order to meet continuous improvement outcomes and to identify and reduce the impact of external factors on the production of the AFR.

RESPONSE provided by the Treasurer – continued

The need for public sector financial reports to present information consistently to ensure optimal utility and comparability is also acknowledged. To this end, DTF will continue to support and facilitate the adoption of consistent asset recognition and measurement policies across the Victorian public sector.

Finally, I would like to thank your audit team for conducting a professional and timely audit, which added value to the quality of the AFR.

RESPONSE provided by Melbourne City Studios Pty Ltd

Response to the Report on Balance Sheet

In the Figure 3J Summary of the financial position of the acquired studios, the 'Balance Sheet June 2008' on the first column is based on actual audited Melbourne Central City Studios Pty Ltd (MCCS) financial reports. The "Revised June Balance Sheet" on the second column is not adopted by MCCS, but is an illustrative balance sheet that is retrospectively developed by Auditor-General.

As at 19 November 2008 the Directors commissioned a valuation of company buildings. The values determined the increment in replacement cost over and above the historic cost recorded in the MCCS's asset register was $14.2 million. This valuation was similar to the 2006 revaluation and the $11.2 million write down is mainly attributed to the change in the assumed remaining estimated useful lives of the administration building and the warehouse to 5 years and 10 years respectively from 40 years in earlier valuation. While this is accepted by the MCCS at the moment, it is still subject to revision in the future. The Department is currently reviewing the business direction of MCCS which could potentially extend the useful life of the key assets, hence reversing the write down and subsequently increase the assets carrying value of the assets.

RESPONSE provided by Melbourne City Studios Pty Ltd – continued

Response to the Report on Operating Loss 2008–09

The loss of $6.81 million includes two items which could not be properly attributed to trading performance: (1) a $2.03 million write-off of Deferred Tax Asset which is no longer applicable and (2) an imputed expense of $1.15 million write-down in asset value due to the revaluation after acquisition. Excluding both items, the operating loss stands at $3.63 million. This is due to significant fall in revenue to $1.27 million compared to $4.54 million in previous year. Financial year 2007–08 was an exceptionally good year while financial year 2008–09 was a difficult year affected by the global economic crisis, a high value of Australian dollar and the Writers Guild of America strike.

It is important to note that MCCS's key performance indicators include both commercial and broader economic outcomes. MCCS remains focused on the studios' key objectives to develop the industry and generate broader economic benefit for Victoria. Since its opening in 2004, MCCS has hosted local and international productions with an estimated contribution to the Victorian economy of more than $470 million. As part of the critical infrastructure for Victoria's film and TV industry, MCCS will continue to play its critical role in fostering a vibrant creative industry in Victoria.

Response to the Report on Financial Health and Sustainability

The Government is currently reviewing options for MCCS and while it notes that to-date it has not met its commercial KPIs it has been successful in creating over $470 million in economic activity in Victoria.

1 Results of audit

At a glance

Background

The *Financial Management Act 1994* and AASB 1049 *Whole of Government and General Government Sector Financial Reporting,* requires a Victorian whole-of-government and general government sector (GGS) Annual Financial Report (AFR) audited by the Auditor-General, to be tabled in Parliament. The AFR is contained within the *Financial Report for the State of Victoria 2008–09* (the Financial Report), and is a key document in acquitting the government's stewardship of the state's finances to Parliament.

The Department of Treasury and Finance (DTF) prepares the AFR. It consolidates the financial results of more than 300 public sector entities, each of which is separately audited by the Auditor-General. In 2008–09, 47 of these entities were regarded as material entities, as the magnitude of their individual financial operations are significant in the reporting of the consolidated finances of the state.

Findings

- A clear audit opinion on the 2008–09 AFR was issued on 29 September 2009 and included in Chapter 4 of the Financial Report that was tabled in Parliament on 14 October 2009 in line with the timing required by legislation.
- However, the AFR preparation timetable was not achieved due to the late provision of certified financial data by 34 (79 per cent) material entities and lengthy considerations regarding the recognition and measurement of land under roads and the measurement of infrastructure assets at fair value.

At a glance – *continued*

Recommendations

- DTF should, in consultation with material entities:
  - develop improved processes, to achieve the required timeframes, and
  - improve their quality assurance processes.
- Public sector entities should more rigorously align their financial reporting timetable, including audit committee and board meeting dates, to the AFR timetable.
- DTF should lead the adoption of consistent recognition and measurement policies across the Victorian public sector.

1.1 Introduction

This is the third of six reports to Parliament scheduled for 2009–10 covering the results of our audits of public sector financial reports. The reports in the series are outlined in Figure 1A.

The purpose of this report is to:

- set out the results of the audit of the AFR
- discuss the financial performance and the financial position of the state and highlight matters of significance for the state's long-term ability to sustain operations and respond to changing community expectations
- provide observations on the status and financial implications of significant developments.

Figure 1A
VAGO reports on the results of audits

Reports	Description
Local Government: Results of the 2008–09 Audits	The **first** report, tabled in Parliament on 11 November 2009, contains the results of the annual audit of 79 councils, 12 entities they control and 12 regional library corporations.
Public Hospitals: Results of the 2008–09 Audits	The **second** report, tabled in Parliament on 11 November 2009, contains the results of the annual audit of 88 public hospitals, 22 entities they control and four associated entities.
Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2008–09	The **third** report, to be tabled in Parliament on 24 November 2009 contains the results of the audit of the State's Annual Financial Report.
Water Entities: Results of the 2008–09 Audits	The **fourth** report, to be tabled contains the results of the annual audit of 19 entities, comprising 16 water corporations and three retail distribution companies.
Portfolio Departments and Associated Entities: Results of the 2008–09 Audits	The **fifth** report, to be tabled provides a summary of the results of the annual audit of financial reports of the 10 portfolio departments and 198 associated entities with 30 June 2009 balance dates.
Results of Audits for Entities with other than 30 June 2009 Balance Dates	The **sixth** of these reports, to be tabled by mid 2010 provides the results of the annual audit of financial reports of 120 entities in Victoria's public sector, which have a financial year other than 30 June 2009. These entities principally comprise 76 higher education entities, 34 vocational training entities and Victoria's five alpine resorts.

Source: Victorian Auditor-General's Office.

1.2 Financial audit framework

The financial audit framework applied in the conduct of the 2008–09 audits of the consolidated entities and the AFR is outlined in Figure 1B.

Figure 1B
Financial audit framework

Planning

Planning is not a discrete phase of a financial audit, rather it continues throughout the engagement. However, initial audit planning is conducted at two levels:

- At a high or entity level, planning involves obtaining an understanding of the entity and its environment, including its internal controls. The auditor identifies and assesses: the key risks facing the entity; the entity's risk mitigation strategies; any significant recent developments; and the entity's governance and management control framework.
- At a low or financial statements line item level, planning involves the identification, documentation and initial assessment of processes and controls over management, accounting and information technology systems.

The output from the initial audit planning process is a detailed audit plan and a client strategy document, which outlines the proposed approach to the audit. This strategy document is issued to the client after initial audit planning and includes an estimate of the audit fee.

Conduct

The conduct phase involves the performance of audit procedures aimed at testing whether or not financial statement balances and transactions are free of material error. There are two types of tests undertaken during this phase:

- Tests of controls, which determine whether controls identified during planning were effective throughout the period of the audit and can be relied upon to reduce the risk of material error.
- Substantive tests, which involve: detailed examination of balances and underlying transactions; assessment of the reasonableness of balances using analytical procedures; and a review of the presentation and disclosure in the financial statements, for compliance with the applicable reporting framework.

The output from this phase is a final (and possibly an interim) management letter which details significant findings along with value-adding recommendations on improving controls and processes. These documents are issued to the client after any interim audit work and during the reporting phase.

Reporting

The reporting phase involves the formal presentation and discussion of audit findings with the client management, and / or the audit committee. The key outputs from this process are:

- A signed audit opinion, which is presented in the client's annual report alongside the certified financial statements.
- A report to the minister responsible for the entity of significant findings identified during the audit
- A report to Parliament on significant issues arising from audits either for the individual entity or for the sector as a whole.

Source: Victorian Auditor-General's Office.

1.3 Scope

Section 9A of the *Audit Act 1994* requires the Auditor-General to provide an audit opinion on the AFR.

Section 16A of the *Audit Act 1994* requires the Auditor-General to prepare and table a report on the audit of the AFR.

1.4 The financial reporting framework

The *Financial Management Act 1994* (the FMA) sets the framework for the administration of public finances in Victoria. The FMA requires the annual preparation of a consolidated financial report of the state with transactions, balances and disclosures reported at:

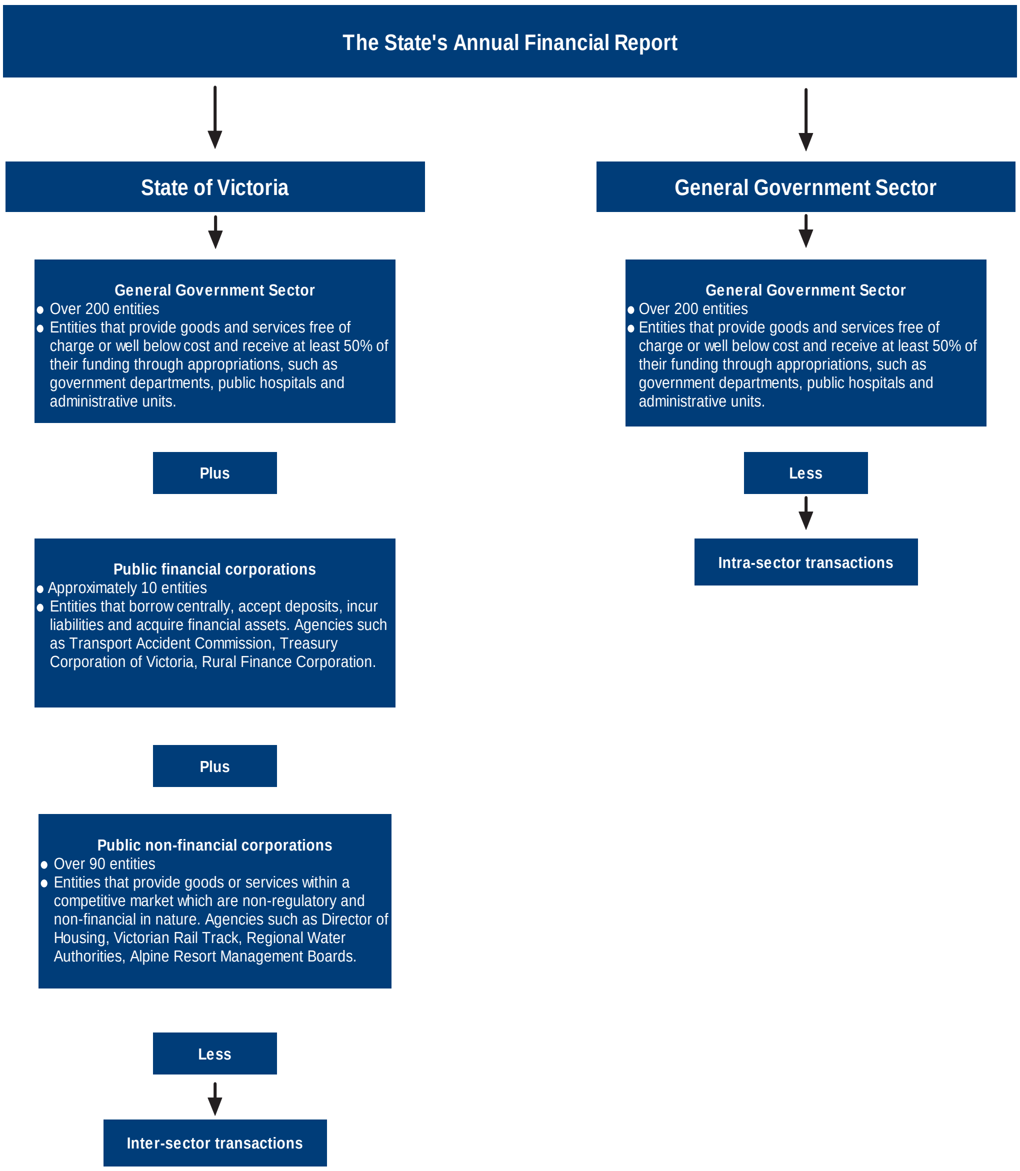
- state level which aggregates the three sectors of government: the general government sector (GGS), the public non-financial corporations (PNFC) and the public financial corporations (PFC) to present a whole-of-government perspective
- GGS level separated out to provide a perspective of the operations of the budget funded sector of government.

These financial reports are referred to in the FMA as the Annual Financial Report (AFR). The AFR is a key document which acquits the government's stewardship of the state's finances to Parliament. The AFR is incorporated into a narrative report, the Financial Report for the State of Victoria 2008–09 (the Financial Report).

The AFR details the government's cost of operations, revenue, impacts of market re-measurement on the value of assets and liabilities, and the value of what it owns and what it owes. In the AFR, the government provides this information for the State of Victoria and the GGS.

Figure 1C outlines the financial report coverage included in the AFR.

Figure 1C
Entities included in the 2008–09 AFR



Source: Victorian Auditor-General's Office.

Consolidated financial reports for the state are the combined financial results of all entities in each sector; except for inter and intra sector transactions between entities in these groups which are netted out to avoid double counting where they are internal transactions e.g. payroll tax paid by a department is netted out in the results for the state.

In accordance with Australian accounting standards, only entities controlled by the state are included in the consolidated financial report. The state controls entities where it has the power to direct the activities of, and benefit from, that entity. Controlled entities include the portfolio departments and state-owned enterprises. Figure 1D details the entities that are not controlled by the state and the justification for this in accordance with Australian accounting standards.

Figure 1D
Entities not controlled by the state

Entity	Justification
Local government	Local government is a separate tier of government with councils elected and accountable to their constituents.
Universities	Universities are primarily funded by the Commonwealth with the state only directly appointing a small minority of the members to the University councils.
Denominational hospitals	Denominational hospitals are private providers of public health services and have their own governance arrangements.
Superannuation funds	The net assets of the funds themselves are the property of the members with any shortfall in entitlements related to defined benefit schemes being recorded as a liability of the state and consolidated via the financial report of the Department of Treasury and Finance.

Source: Victorian Auditor-General's Office.

The consolidated financial results are also disaggregated to report the transactions and balances into the three sectors of government in Note 2 to the AFR.

The AFR is the responsibility of the Treasurer and the Minister for Finance, WorkCover and the Transport Accident Commission. DTF prepares the AFR in accordance with section 24 of the FMA and applicable Australian accounting standards and interpretations. Australian Accounting Standard *AASB 1049 Whole of Government and General Government Sector Financial Reporting* however has particular relevance. The FMA requires the AFR itself to be audited by the Auditor-General, and tabled in Parliament by 15 October each year.

The 2008–09 AFR is the first to be prepared in accordance with this standard which resulted in:

- the measurement of all infrastructure, plant and equipment assets at fair value, previously recorded at historical cost, which resulted in a revaluation increment of $15 349.9 million
- the recognition of $18 682.5 million of land under roads acquired prior to 1 July 2008
- the recognition in the GGS of government equity of $60 634.8 million in the public financial corporations (PFC) and public non financial corporations (PNFC) on the balance sheet
- changes to the classification of a number of transactions and balances, for example, fines are no longer disclosed separately on the comprehensive operating statement, they are now classified in other current revenue
- additional disclosure requirements, including analysis of the significant differences between actual results and the original budget.

1.5 Results of the audit of the 2008–09 AFR

The independent audit opinion adds credibility to the financial report, providing assurance that the information in the financial report is reliable.

A clear audit opinion on the 2008–09 AFR was issued on 29 September 2009 and included in Chapter four of the Financial Report that was tabled in Parliament on 14 October 2009. In the prior year, a clear audit opinion on the AFR was issued on 24 September 2008 and was tabled in Parliament on 14 October 2008.

A clear audit opinion indicates that the AFR has been prepared in accordance with the requirements of the FMA and Australian accounting standards.

1.6 Preparation of the AFR

DTF consolidates the financial results of more than 300 public sector entities controlled by the state in terms of Australian accounting standards.

Of the controlled public sector entities, 47 were deemed material entities for 2008–09. A material entity is a public sector entity whose individual financial operations are significant in the reporting of the consolidated finances of the state. These entities collectively comprise more than 90 per cent of the state's assets, liabilities, revenue and expenditure.

Material entities are listed in Appendix A. Note 40 to the AFR lists the controlled public sector entities included in the AFR.

To facilitate preparation of the AFR, public sector entities transmit financial data via electronic data feeds into DTF's Business Management System (BMS), a web based reporting facility based upon:

- their audited financial reports, and
- separately audited data, where data required for the AFR differed to data reported in the financial reports of consolidated entities.

Data feeds are verified by audit with reference to the entities' audited financial reports or results of the audits of the fair valuation of assets.

1.6.1 Quality of draft financial reports

The quality of the draft AFR depends upon the accuracy of financial data submitted to DTF by public sector entities and DTF's quality assurance processes in preparing the consolidated accounts. In 2008–09 errors in the financial data submissions of 31 material entities (28 in 2008) were detected, indicating deficiencies in quality assurance processes of both reporting entities and DTF.

Material error was also identified in the draft disclosure notes to the AFR for commitments and contingencies which were sourced from entity data feeds to DTF. Initially the amounts disclosed in the AFR did not agree with the audited balances included in the final individual entities financial reports. Material errors detected were:

- **commitments disclosed at nominal value**—understated by $2 436.9 million by 11 entities and overstated by $3 854.2 million by 12 entities
- **commitments disclosed at net present value**—understated by $313.2 million by four entities and overstated by $1014.2 million by three entities
- **quantifiable contingencies**—understated by $39.1 million by six entities and overstated by $491.4 million by 13 entities.

In addition, further errors detected were:

- **mis-classification of commitments**—totalling $1 737.9 million by 10 entities
- **omission of non-quantifiable contingencies**—by 10 entities.

All these material errors were corrected in the AFR before issue of the clear audit opinion.

1.6.2 Timeliness of AFR preparation

The timely preparation and audit of the AFR depends on the consolidated entities meeting the established AFR preparation timetable and the early identification and resolution of significant accounting, recognition, measurement, presentation and disclosure matters.

Responding to last year's audit recommendation, DTF released the AFR timetable in February 2009. DTF essentially requires the following from material entities:

- complete draft financial reports for audit by 24 July 2009 (25 July in 2008)
- audited sign-off to the DTF by 12 August for GGS entities (14 August in 2008) and 14 August 2009 for PNFC's and PFC's (18 August in 2008).

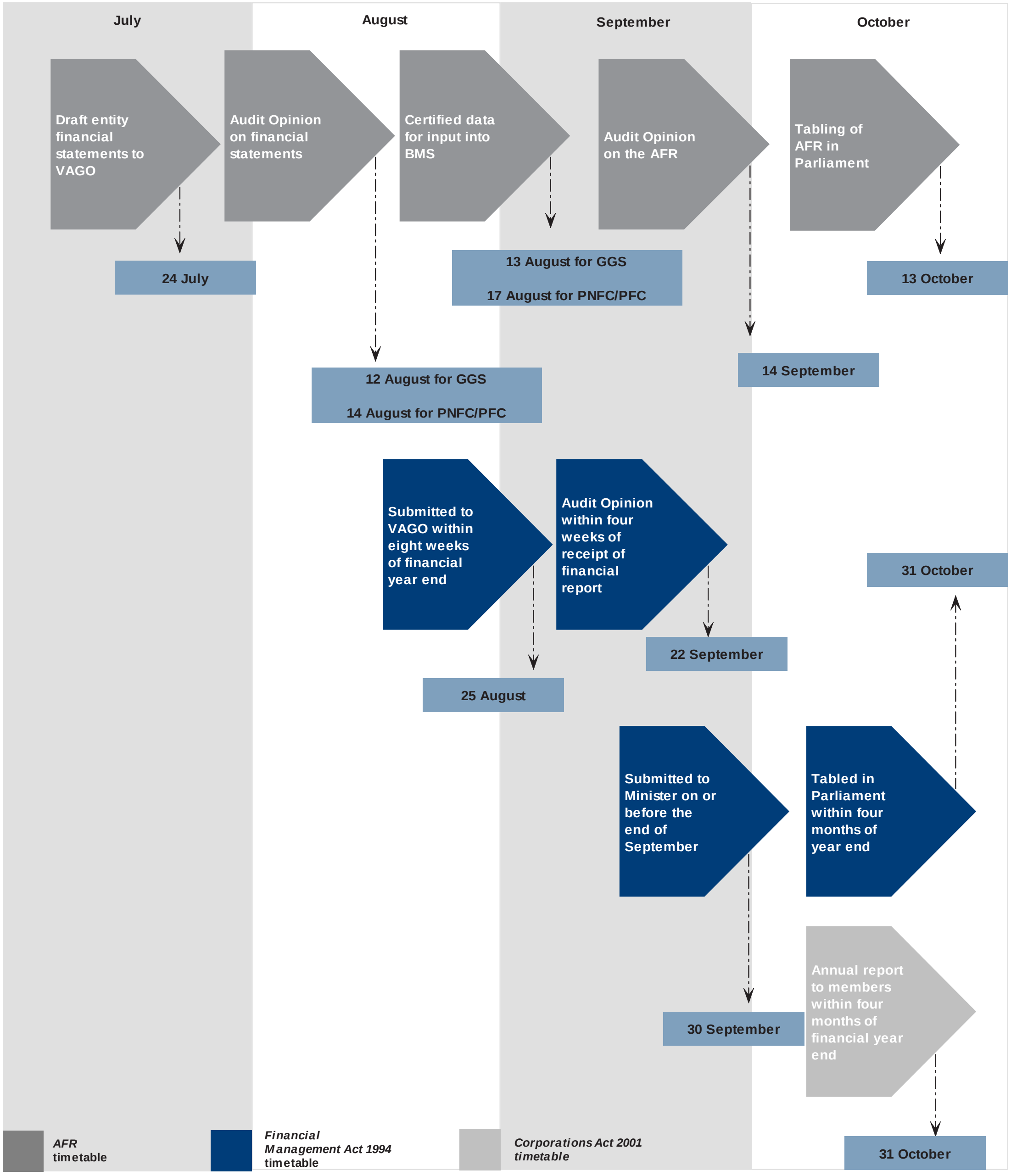
In addition, DTF requires CFO certified data feeds to the DTF by 13 August 2009 for GGS entities (14 August in 2008) and 17 August 2009 for PNFC's and PFC's (18 August in 2008) for 43 of the 47 material entities. Four entities are not required to provide full feeds to the DTF due to the nature of their consolidation.

DTF requires from the non-material entities CFO certified data feeds to the DTF by 13 August 2009 for GGS entities (14 August in 2008) and 17 August 2009 for PNFC's and PFC's (18 August in 2008).

This timetable included earlier reporting milestone dates than the legislative timeframes imposed on reporting entities included in the AFR. The FMA requires entities to submit annual reports to the relevant minister. These reports should be tabled in Parliament within four months of the end of the financial year, and include financial reports for both the entity and any controlled entities which must be prepared and audited within 12 weeks. The remaining entities, reporting under the *Corporations Act 2001,* are required to report to their members within four months of the end of the financial year.

Key milestone dates in the AFR timetable are contrasted to legislative reporting requirements in Figure 1E.

Figure 1E
Reporting time frames and the key milestone dates included in the AFR timetable



Source: Victorian Auditor-General's Office.

Notwithstanding the earlier consultations and issue of the AFR timetable, fewer material entities met the timelines as summarised below. This delayed the preparation and audit of the AFR.

In response to DTF required milestones:

- 18 material entities or 38 per cent (17 material entities or 36 percent in 2008) provided complete draft financial reports to audit by the required milestone date
- eight material entities or 17 per cent (10 material entities or 21 per cent in 2008) had audited financial reports completed by the required milestone date
- nine material entities or 21 per cent of the reporting entities provided certified financial data to DTF by the required milestone date.

Figure 1F provides the results of material entities against DTF AFR milestones dates.

This situation highlights the need to improve processes and to better focus efforts to deliver reliable financial reports within the established timeframes.

Figure 1F
Results of material entities against DTF milestone dates

	Draft financial reports		Audit opinion		Certified data feed	
Material entity	**Met**	**Not met**	**Met**	**Not met**	**Met**	**Not met**
General government sector	**24 July 2009**		**12 August 2009**		**13 August 2009**	
Austin Health		●		●		●
Alfred Health		●		●		●
Barwon Health		●		●		●
Country Fire Authority	●		●		●	
Department of Education and Early Childhood Development		●		●		●
Department of Human Services		●		●		●
Department of Innovation, Industry and Regional Development		●		●		●
Department of Justice	●			●		●
Department of Planning and Community Development		●		●		●
Department of Premier and Cabinet		●		●		●
Department of Primary Industries	●			●		●
Department of Sustainability and Environment	●			●		●
Department of Transport		●		●		●
Department of Treasury and Finance		●		●		●
Eastern Health	●		●			●
Melbourne Health	●		●			●
Metropolitan Fire and Emergency Services Board	●			●		●
National Gallery of Victoria		●		●		●
Office of the Chief Commissioner of Police (Victoria Police)		●		●		●
Parks Victoria		●		●	●	

Figure 1F
Results of material entities against DTF milestone dates – *continued*

	Draft financial reports		Audit opinion		Certified data feed	
Material entity	**Met**	**Not met**	**Met**	**Not met**	**Met**	**Not met**
General government sector – *continued*	**24 July 2009**		**14 August 2009**		**17August 2009**	
Roads Corporation (Vic Roads)		●		●		●
Royal Children's Hospital		●		●		●
Southern Health	●		●			●
Victorian Commission for Gambling Regulation	●			●		●
Victorian Skills Commission		●		●		●
Western Health	●		●			●
Public non-financial and public financial corporations	**24 July 2009**		**14 August 2009**		**17August 2009**	
Barwon Region Water Corporation		●	●		●	
City West Water Limited	●			●	●	
Goulburn-Murray Rural Water Corporation		●		●		●
Melbourne Water Corporation	●			●		●
Port of Melbourne Corporation	●			●		●
Rural Finance Corporation	●		●		●	
South East Water Limited		●		●		●
State Electricity Commission of Victoria		●		●	●	
Transport Accident Commission (TAC)		●		●		●
Treasury Corporation of Victoria		●		●	●	
V/Line Passenger Corporation		●		●	●	
Victorian Energy Networks Corporation (VENCorp)		●		●		●
Victorian Managed Insurance Authority		●		●		●

Figure 1F
Results of material entities against DTF milestone dates – *continued*

	Draft financial reports		Audit opinion		Certified data feed	
Material entity	**Met**	**Not met**	**Met**	**Not met**	**Met**	**Not met**
Public non-financial and public financial corporations – *continued*	**24 July 2009**		**14 August 2009**		**17 August 2009**	
Victorian Rail Track		●		●		●
Victorian Urban Development Authority (VicUrban)	●		●		●	
Victorian WorkCover Authority		●		●		●
Yarra Valley Water Limited	●			●		●
Other	**24 July 2009**		**14 August 2009**		**Not applicable**	
Emergency Services Superannuation Scheme		●		●		
Residential Tenancies Bond Authority	●			●		
Senior Master of the Supreme Court		●		●		
State Trustees Limited	●			●		
2008–09	**18**	**29**	**8**	**39**	**9**	**34**
Per cent	38	62	17	83	21	79
2007–08	**17**	**30**	**10**	**37**	**n/a**	**n/a**
Per cent	36	64	21	79	n/a	n/a

Source: Victorian Auditor-General's Office.

1.7 Inconsistent recognition and measurement of assets

The 2008–09 AFR is the first to be prepared in accordance with AASB 1049. This resulted in:

- Water, rail and port infrastructure assets being measured at fair value resulting in a $15 300 million increment being reported in the AFR. However, the majority of water, rail and port entities record infrastructure assets at cost in their individual financial reports. This is in accordance with FRD 121 *Infrastructure Assets (Water/Rail)* and the relevant Australian accounting standards. However, FRD 121 also requires the entities concerned to move to recording the applicable assets at fair value in their individual entity financial reports within the next two years. Figure 1G provides a summary of infrastructure asset valuation methods.
- The recognition of $18 682.5 million of land under roads in the AFR. However, VicRoads did not recognise land under roads in their individual financial report in accordance with the options available under AASB 1051 *Land Under Roads* to not recognise land under roads acquired prior to 1 July 2008.

Figure 1G
Reporting entity infrastructure asset valuation methods

	Infrastructure valuation methodology	
	Cost	Fair value
AFR		✓
Port entities		
Port of Melbourne Corporation	✓	
Port of Hastings Corporation		✓
Victorian Regional Channels Authority		✓
Rail entities		
Victorian Rail Track	✓	
Water entities		
Barwon Region Water Corporation	✓	
Central Gippsland Region Water Corporation	✓	
Central Highlands Region Water Corporation	✓	
City West Water Limited	✓	
Coliban Region Water Corporation	✓	
East Gippsland Region Water Corporation	✓	
Gippsland and Southern Rural Water Corporation	✓	
Goulburn-Murray Rural Water Corporation	✓	
Goulburn Valley Region Water Corporation	✓	
Grampians Wimmera Mallee Water Corporation	✓	
Melbourne Water Corporation	✓	
Lower Murray Urban and Rural Water Corporation	✓	
North East Region Water Corporation	✓	
South East Water Limited	✓	
South Gippsland Region Water Corporation	✓	
Wannon Region Water Corporation	✓	
Western Region Water Corporation	✓	
Westernport Region Water Corporation	✓	
Yarra Valley Water Limited	✓	

Source: Victorian Auditor-General's Office.

There will continue to be a variance between valuations in the AFR and the financial reports of the water and rail entities until DTF, under the direction of the minister, requires these entities to implement fair valuation of infrastructure assets in their financial reports.

Assuming current revenue levels, this change in accounting policy would result in higher depreciation charges, lower net results and impact on tax-related balances for these entities.

In addition to inconsistency between the AFR and individual reporting entities, there is inconsistency in the measurement of assets by ports. In 2008–09, ports were required to measure infrastructure assets at fair value in their financial reports. The Port of Hastings Corporation and the Victorian Regional Channels Authority complied with this requirement. The Minister for Finance subsequently provided the Port of Melbourne Corporation with an exemption from recording these assets at fair value on 19 August 2009. The corporation advised that a fair valuation could not be provided with sufficient rigor for inclusion in its statutory report.

These ongoing inconsistencies at 30 June 2009 highlight the need for a concerted effort to treat like transactions and events consistently to achieve optimal utility and comparability.

Whilst not significant for the AFR, for future statutory financial reports:

- Victorian Rail Track needs to improve the quality of its asset information to assure materially accurate valuations for the fair valuation of trains, trams and associated infrastructure assets.
- Port of Melbourne Corporation needs to finalise its fair valuation methodology.
- Vic Roads should, consistent with the AFR, recognise land under roads.

Recommendations

1. DTF should, in consultation with material entities:
   - develop improved processes, to achieve the required timeframes, and
   - improve their quality assurance processes.

2. Public sector entities should more rigorously align their financial reporting timetable, including audit committee and board meeting dates, to the AFR timetable.

3. DTF should lead the adoption of consistent recognition and measurement policies across the Victorian public sector.

2 The state's financial result

At a glance

Findings

- In 2008–09 the net result, including transactions and other economic flows, for the state was a deficit of $13 088.8 million (deficit of $3 165.9 million, 2007-08) largely reflecting the second year of actuarial losses by the state's defined benefit superannuation plans combined with realised and unrealised losses on financial instruments due to financial market conditions.
- The net result from transactions for the state was a deficit of $62.9 million in 2008–09 (a surplus of $1 638.6 million, 2007–08) again largely reflecting the impact of the global financial crisis. The GGS net result from transactions was a surplus of $251.2 million in 2008–09 ($1 646.6 million, 2007–08) which exceeded the revised key financial objective of $100 million.
- A number of external factors need to be monitored in managing short and long-term sustainability.

2.1 Introduction

This chapter provides analysis of significant results and balances for the state.

To assist readers to make assessments about the state's financial performance and position, we:

- provide an overview of the state's financial results for the period 2004–05 to 2008–09
- overview the general government sector (GGS) net result from transactions
- highlight financial management challenges faced by the state.

2.2 Financial results

Every year the State of Victoria tables in Parliament two key financial documents – the Statement of Finances (incorporating Quarterly Financial Report No. 3) Budget Paper No. 4, and the Annual Financial Report (incorporating Quarterly Financial Report No. 4) (AFR).

The Statement of Finances includes the state's estimated financial statements for the GGS (the original budget).

The AFR details the state's cost of operations, revenue, impacts of market re-measurement on the value of assets and liabilities, and the value of what it owns and what it owes. In the AFR, this information is provided for the State of Victoria and the GGS.

2.2.1 Financial performance

Two key measures of financial performance and sustainability are provided in the AFR: the net result from transactions and the net result. The net result from transactions is revenue less expenditures that can be directly attributed to government policy. The net result is derived by adding the net result from transactions to the total of other economic flows. Other economic flows represent changes in the values of assets and liabilities due to market re-measurements that are not directly attributable to government policy including actuarial gains and losses that primarily reflect the valuation movement in the state's superannuation liability.

Net result

Figure 2A shows the net results for the state and the GGS (including transactions and economic flows) for the last five financial years.

Figure 2A
Net results—State of Victoria and general government sector

Source: Victorian Auditor-General's Office.

The 2008–09 net result of the state (including transactions and other economic flows) was a deficit of $13 088.8 million (deficit of $3 165.9 million, 2007–08). For the GGS, the net result was a deficit of $8 372.8 million (deficit of $1 934.8 million, 2007–08).

The deficit result is primarily attributed to:

- actuarial losses by the state's defined benefit superannuation plans of $7 572.5 million ($3 398 million, 2007–08)
- losses on financial instruments measured at fair value totalling $4 022.2 million ($1 452.0 million, 2007–08).

The actuarial loss of $7 572.5 million ($3 398 million, 2007–08) includes the impact of lower than expected returns on superannuation plan assets of $3 693.5 million ($3 005.3 million, 2007–08), and a $3 879.0 million decline ($411.0 million, 2007–08) due to the impact of the reduction in the Commonwealth Government bond rate used in the measurement of the liability.

Each year, an actuarial gain or loss on the state's superannuation liability is recognised in the net result to reflect the impact of variations between assumptions and actual experience as well as the impact of changes in actuarial assumptions. Apart from the impact of investment returns, a small change in key assumptions can cause large variations in the liability and associated actuarial gain or loss. For example, a 0.01 per cent change in the Commonwealth Government bond rate (which underpins the discount rate that is used to measure the superannuation liability) is estimated to change the value of the superannuation liability, which gives rise to actuarial gains or losses, of approximately $30.0 million. Consequently, actuarial gains and losses on superannuation can have a significant impact on the net result.

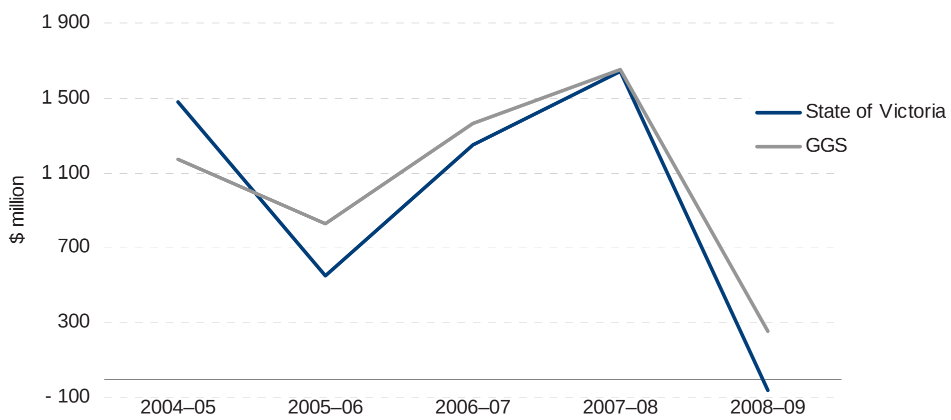
The loss on financial instruments measured at fair value comprises realised losses of $1 228.0 million, ($379.0 million, 2007–08), unrealised losses of $1 708.4 million ($1 073.0 million, 2007–08) and losses on the derivative financial instruments for the State Electricity Commission of Victoria (SECV) onerous contract of $1 091.8 million (gain of $800.9 million, 2007–08) as a result of a significant decrease in the aluminium price (2008–09 US$1 645, 2007–08 US$3 030) used to measure the derivative financial instruments. The onerous contract is recognised in accordance with AASB 137 *Provisions, Contingent Liabilities and Contingent Assets,*

These losses are directly related to the decline in asset values in the financial markets. Under the requirements of Australian accounting standards, the state's equities and managed investments, debt securities and derivative financial instruments have to be re-measured at fair value each balance date. The revaluation is shown as a gain or loss on revaluation of financial assets. While the state benefited from a strong economy during 2005–06 and 2006–07, the downturn in financial markets since 2007–08, has resulted in these fair value losses.

Net result from transactions

Figure 2B shows the State of Victoria and GGS net result from transactions for the last five financial years.

Figure 2B
Net results from transactions—State of Victoria and general government sector



Source: Victorian Auditor-General's Office.

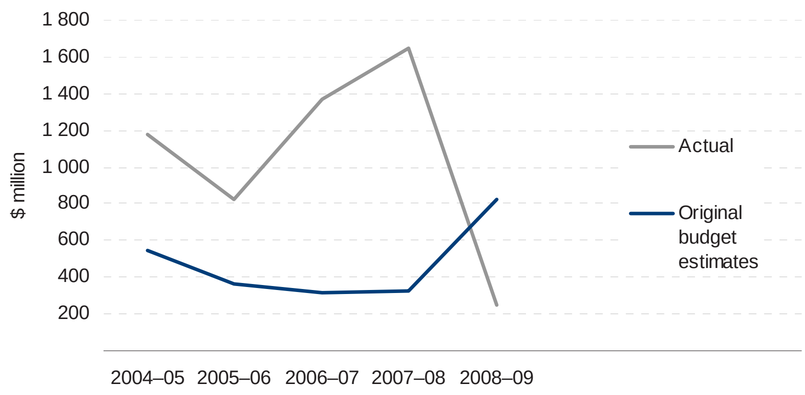
The comprehensive operating statement for 2008–09 shows that the consolidated net result from transactions for the state was a deficit of $62.9 million (a surplus of $1 638.6 million, 2007–08). The net result from transactions for the GGS was a surplus of $251.2 million ($1646.6 million, 2007–08) which exceeded the revised key financial objective of a net result from transactions of at least $100 million. The achievement of this target was primarily due to the recognition of fiscal stimulus funding from the Commonwealth and higher sales of goods and services revenue and other revenue.

The net result from transactions for the GGS is the state’s key measure of short-term financial performance.

For the period 2005–06 to 2007–08 the state’s key financial objective was to achieve a net result from transactions of at least $100 million for the GGS. In the 2008–09 budget this target was revised to maintaining a substantial net result from transactions for the budget sector of at least one per cent of revenue in each year. Due to the global financial crisis the state reverted to a net result from transactions of at least $100 million, though it is committed to returning to a budgeted operating surplus of at least one per cent of revenue in the future.

Figure 2C shows the GGS net result from transactions in comparison with the original budget estimates for the last five financial years.

Figure 2C
Net results from transactions—general government sector



Source: Victorian Auditor-General's Office.

The original budgeted net result from transactions was $827.5 million whereas the actual net result from transactions for the GGS was $251.2 million (2007–08 original budget of $324.3 million compared to an actual result of $1 646.6 million). The actual result of $251.2 million compared to a revised budget estimate of $242.5 million (2007– 08 actual result of $1 646.6 million compared to a revised budget of $996 million).

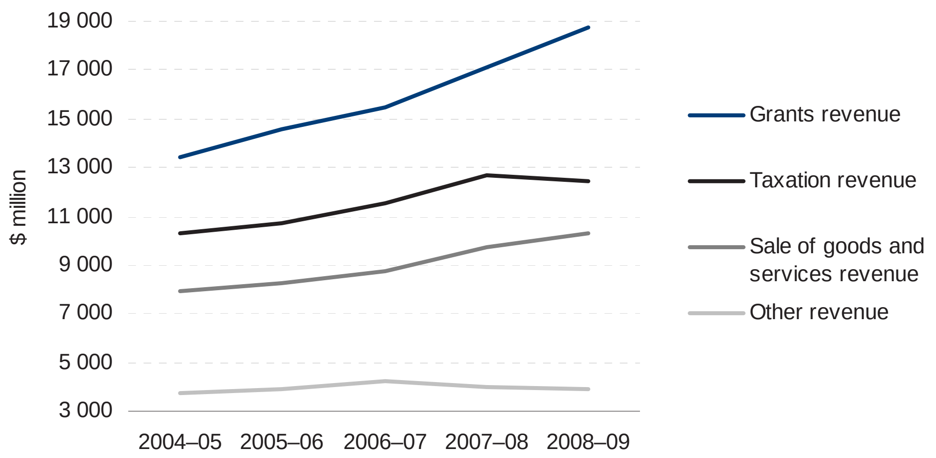
There are inherent uncertainties in determining budgets, both in developing estimates themselves and anticipating future events. The final outcomes also reflect the impact of new policy decisions since the original budget.

Revenue

Commonwealth grants, state taxation and the sale of goods and services are the primary sources of revenue for the state. Total revenue has risen from $35 296.0 million in 2004–05 to $45 432.0 million in 2008–09, an increase of 28.7 per cent. During 2008–09, the impact of the global financial crisis resulted in lower levels of total taxation receipts, however, additional Commonwealth Government fiscal stimulus funding of approximately $430.0 million and the changes to the Commonwealth funding for states resulted in significant growth in grant revenue.

Figure 2D shows the major sources of revenue for the state for the last five financial years.

Figure 2D
Total revenue from transactions—State of Victoria



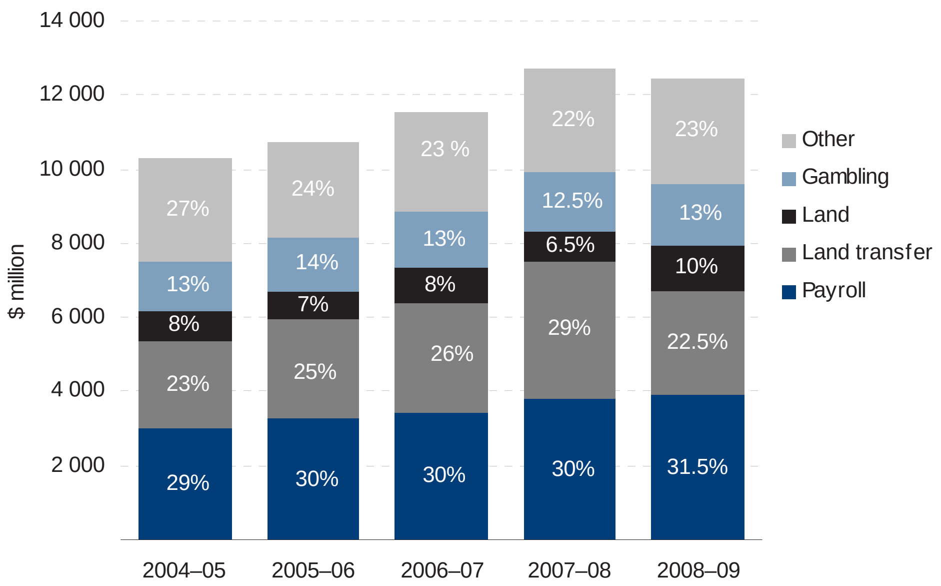
Source: Victorian Auditor-General's Office.

Commonwealth grants have increased by 39.8 per cent, from $13 394 million in 2004-05 to $18 722.6 million in 2008–09. In 2008–09, grant revenue represented 41.2 per cent of the state's total revenue from transactions. The state is highly dependent on Commonwealth funding which includes goods and services tax (GST) revenue and national specific purpose and partnership payments. The performance of the national economy, individual state economies and policy decisions of the Commonwealth government impacts on the level of funding provided to the state.

Taxation revenue reported for the state is derived from taxation reported for the GGS less taxes paid by consolidated entities, including payroll tax. In 2004–05 the state earned taxation revenue of $10 282.3 million, increasing by 21 per cent to $12 443.6 million in 2008–09.

The major sources of taxation revenue are payroll tax, land transfer duty, gambling taxes, land tax and other taxes primarily comprising motor vehicle and insurance taxes. Figure 2E provides a breakdown of the components of taxation revenue for the last five financial years.

Figure 2E
Taxation revenue—State of Victoria



Source: Victorian Auditor-General's Office.

Total taxation receipts had grown each year until 30 June 2008. Lower levels of taxation in 2008–09 reflected slower economic growth. In 2008–09 taxes from land transfer duty declined because of declines in the value of property prices and the number of property sales, while land tax increased, primarily due to the application of revised property valuations. The state's relative dependency on any one source of taxation changed in 2008–09 with increased reliance on land tax and payroll. The state forecasts ongoing growth in taxation revenue from 2009–10.

Taxation revenue as a share of nominal Gross State Product (GSP) was 4.70 per cent in 2008–09. During the period from 2004–05 to 2008–09, taxation revenue has ranged between 4.61 per cent and 4.84 per cent of nominal GSP.

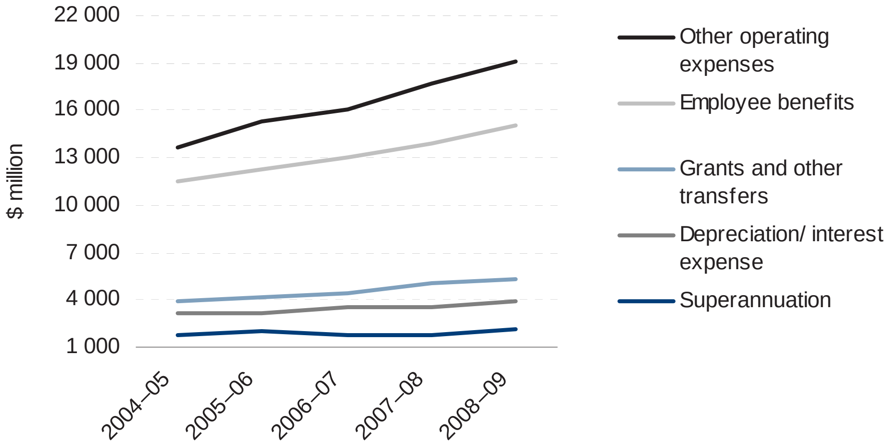
The state's estimates for taxation revenue for the period 2009–10 to 2012–13 are based on real economic growth forecasts of 0.25 per cent in the 2009–10 year increasing to 2.25 per cent in the 2010–11 year and 3 per cent in the following two years to 2012–13 and inflation forecasts of 2 per cent in 2009–10 increasing to 2.5 per cent by 2012–13. These forecasts are subject to review as part of the annual mid–year budget update process.

Sales of goods and services revenue has increased by 31.0 per cent, from $7 882.4 million in 2004–05 to $10 326.9 million in 2008–09. In 2008–09, sales of goods and services revenue represented 22.7 per cent of the state's total revenue from transactions, an increase of $574.7 million from 2007–08. In 2008–09, the growth in sales of goods and services revenue primarily reflects the one-off effect of the Commonwealth government reimbursing the state for costs associated with the 2009 Victorian bushfires of $266 million, increased water and sewerage usage charges across the three metropolitan water retailers of $167 million as a result of increased water prices between 14 per cent and 19 per cent, and increased TAFE student fee revenue of approximately $60 million from on-shore and off-shore international students, reflecting higher student enrolments.

Expenditure

Total expenditure for the state rose from $33 817.3 million in 2004–05 to $45 494.9 million in 2008–09, an increase of 34.5 per cent. This reflects increased levels of service provision and the impact of inflation on expenditure. Figure 2F shows the major types of expenditure for the state for the last five financial years. Employee benefits, other operating expenses and grants and other transfers are the primary costs incurred by the state, together making up 86.6 per cent of total expenditure in 2008–09.

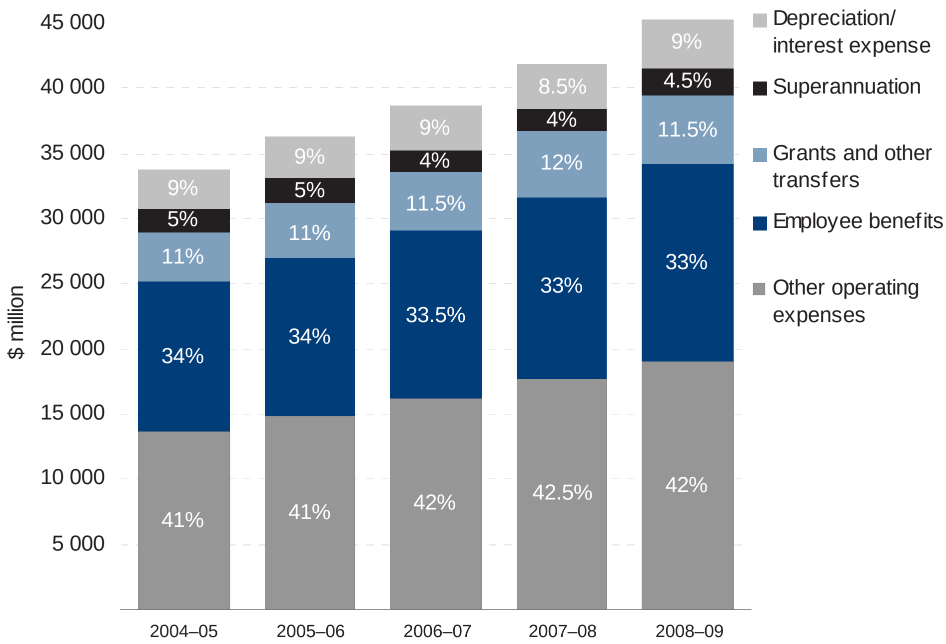
Figure 2F
Total expenses from transactions—State of Victoria



Source: Victorian Auditor-General's Office.

Figure 2G provides a breakdown of state expenditure for the last five financial years.

Figure 2G
Total expenses from transactions—State of Victoria



Source: Victorian Auditor-General's Office.

Employee costs

The state's total employee costs (excluding superannuation expenses) have increased from $11 448.7 million in 2004–05 to $15 037.0 million in 2008–09, an average annual increase of around 7.1 per cent for the period 2004–05 to 2008–09.

Increased employee costs for the state from 2007–08 to 2008–09 are primarily attributed to an increase in wage outcomes under enterprise bargaining agreements and increased service delivery supporting an increase in the public sector workforce and increased wages and overtime. Analysis of the material entities, which include 78.9 per cent of the employee costs for the state, shows that:

- employee numbers measured in terms of full-time equivalents (FTE) for these entities grew by 3.45 per cent, from 145 970 last year to 151 017 this year which includes an increase in FTE numbers for Department of Education and Early Childhood Development of 1 099, Southern Health of 505, Department of Justice of 404, Vic Roads of 342, Victoria Police of 218, the Department of Sustainability and Environment of 150, the Department of Planning and Community Development of 247, and Barwon Health of 239
- average employment costs per FTE increased by 5.20 per cent, above Victoria's average wage growth of 4.0 per cent.[1]

[1] *Source:* 2008–09 Annual Financial Report (incorporating Quarterly Financial Report No 4).

- The increase above Victoria's average wage growth was influenced by the following factors:
  - Enterprise Bargaining Agreement (EBA) increase of 4.9 per cent in May 2008 and 2.71 per cent in January 2009 for government school teachers. In addition, lump sum payments were made in 2008–09 of $2,000 to principals, $1 500 to leading teachers and $1 000 to classroom teachers.
  - Public hospital doctors salaries increased by between 5 and 7.5 per cent, backdated to December 2008.
  - EBA increase of 3 per cent for police.
  - EBA increase of 3 per cent for CFA staff members.
  - EBA increase of 3.25 per cent for nurses.
  - overtime and additional salary costs for:
    - police and CFA staff as a result of the Victorian Bushfires in February 2009
    - health workers resulting from the swine flu epidemic in 2009.

A major component of the state's employee costs are the costs of the public sector employees in the GGS. In 2008–09 the GGS employee costs, have increased from $13 239.4 million to $14 296.9 million, an increase of 8 per cent from the prior year. Employee costs for the GGS are estimated to reach $17 247.1 million (39 per cent of total expenditure) by 2012–13.

2.3 Financial position of the state

The consolidated balance sheet in the AFR contains information about the value and composition of the state's assets and liabilities. The notes to the AFR contain further information about financial commitments, and contingent assets and liabilities that are not reflected in the consolidated balance sheet.

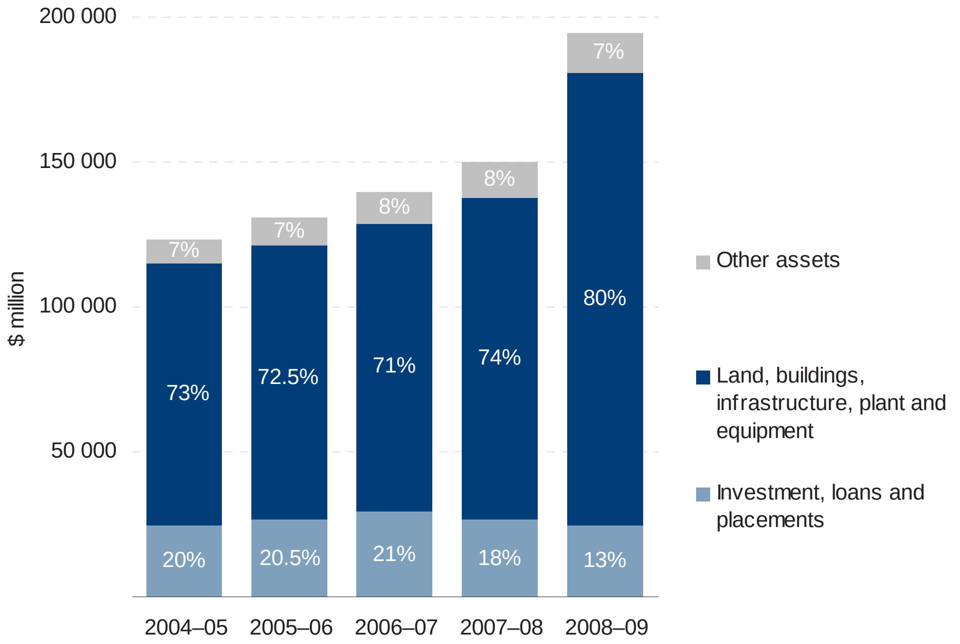
The state's net worth for the year increased by $26 412.8 million (or 29 per cent) to $118 003.6 million ($91 590.8 million in 2007–08). Notwithstanding the investment losses of $4 022.2 million, revaluation of non-financial assets of $20 263.5 million and the recognition of land under roads of $18 682.5 million more than offset investment losses and overall has improved the state's net asset position.

2.3.1 Assets

Investments, loans and placements are the major financial assets of the state. Land, buildings, infrastructure, plant and equipment are the major non-financial assets of the state.

Figure 2H shows the major assets for the state for the last five financial years.

Figure 2H
Total assets—State of Victoria



Source: Victorian Auditor-General's Office.

Total state assets increased from $123 092.6 million in 2004–05 to $194 254.0 million in 2008–09, an increase of $71 116.4 million (or 57.8 per cent) over the five year period.

In 2008–09 the increase in assets was predominantly attributed to significant increases in land, buildings, infrastructure, plant and equipment as explained below:

- Revaluation of $20 500 million for the following asset classes-land and buildings of $4 800 million for scheduled revaluations in the health sector; and infrastructure assets of $15 300 million primarily in the rail and water sectors as a result of the requirement to fair value all infrastructure assets in accordance with AASB 1049.
- Recognition of land under roads of $18 682.5 million as a result of the first time recognition of land under roads in accordance with AASB 1051.
- Asset additions of $9 283.3 million as a result of the following significant additions:
  - $1 096.6 million for capitalisation of part or full completion of various rail related projects, including new trains under construction
  - $1 089.2 million for capitalisation of part or full completion of water infrastructure within Melbourne Water Corporation, primarily relating to the Desalination Plant, Sugarloaf Pipeline and Northern Sewer Project.

- $861.4 million for capitalisation of part or full completion of the major roads and associated infrastructure: Deer Park Bypass, Monash West Gate Freeway Upgrade, Calder Corridor and Geelong Ring Road.
- Recognition of the states share of assets in the Murray Darling Basin joint venture of $809.7 million.
- Various other water infrastructure projects of approximately $760 million across other material water sector entities.
- $545.7 million primarily relating to land and school building additions under the state's Better Schools Today program, School regeneration program and the School modernisation program.
- Melbourne Convention Centre and associated land–$539.2 million
- $369.4 million additions of new land and buildings relating to the provision of community housing.
- Various projects of approximately $350 million across the eight material hospitals.
- $333 million for construction in progress at Port of Melbourne Corporation, primarily relating to the Channel Deepening Project.
- Land for the Rectangular Stadium –$96.4 million, and associated plant and equipment $105.9 million.

2.3.2 Infrastructure renewal

The state's public infrastructure, primarily road and intrastate rail networks, ports and water assets was valued at $55 984.1 million at 30 June 2009[2]. It grew by $18 875.4 million (50.1 per cent) from 2007–08 to 2008–09. This growth related to:

- Major asset additions such as the Deer Park Bypass, Monash West Gate Freeway Upgrade, Calder Corridor, Geelong Ring Road, and recognition of the states share in the Murray Darling Basin.
- The revaluation of significant infrastructure assets of $15 300 million in the rail and water sectors as a result of the requirement to fair value all infrastructure assets in accordance with AASB 1049.

A significant challenge for the state is to maintain existing infrastructure and to provide for the new infrastructure required to achieve the state's social, economic and environmental objectives.

One indicator of the state's financial performance in relation to infrastructure maintenance is the difference between the rate at which existing infrastructure is being used up and the rate at which it is being replaced. This can be measured by comparing the amount spent investing in renewal of assets with the annual depreciation charge on these assets. A renewal ratio higher than 1:1 indicates that infrastructure expenditure exceeds depreciation.

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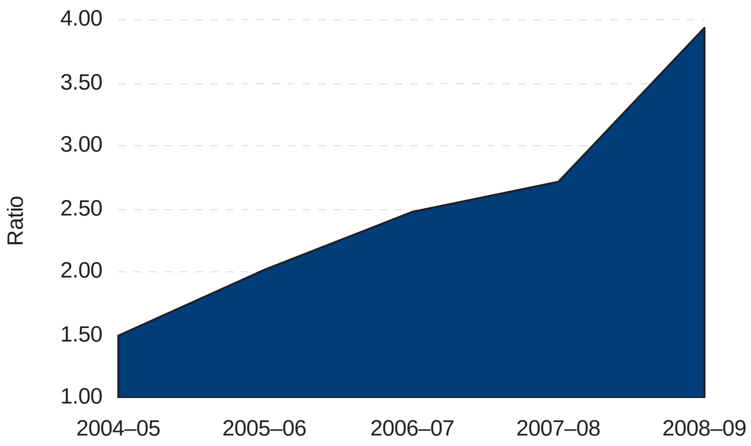
[2] This excludes infrastructure subject to certain public private partnership (service concession) arrangements such as Citylink and Eastlink.

Figure 2I shows the results calculated for infrastructure replacement for the financial periods 2004–05 to 2008–09.

Figure 2I
Plant, equipment, vehicles and infrastructure systems replacement analysis



Source: Victorian Auditor-General's Office.

Based on reported balances the infrastructure replacement ratio for the state increased from 1.5:1 in 2004–05 to 3.9:1 in 2008–09. This indicates prima facie that the state is investing in infrastructure at a rate faster than its service potential is being consumed.

However, caution is required in interpreting these results as:

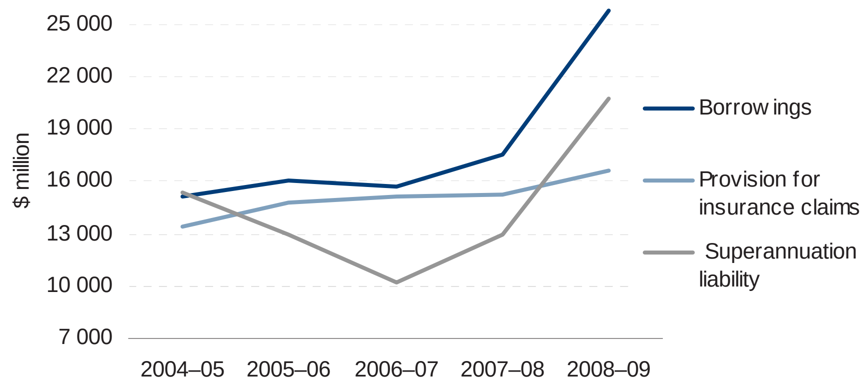
- major infrastructure assets, including water storage, supply systems, rail, ports and channels were measured at their fair value for the first time at 30 June 2009. Annual depreciation expense resulting from this revaluation will be recognised in the comprehensive operating statement from 1 July 2009 in accordance with accounting standards
- annual expenditure on infrastructure includes both upgrade of existing assets and acquisition of new assets. However at this point it is not possible to be conclusive as to what extent asset upgrades alone are keeping pace with consumption (depreciation expense) of those assets.

2.3.3 Liabilities

Borrowings, provisions for insurance claims and the superannuation liability are the major obligations of the state. Total state liabilities increased from $53 614 million in 2004–05 to $76 250.4 million in 2008–09, an increase of $22 636.4 million (or 42.2 per cent) over the five-year period.

Figure 2J shows the major liabilities for the state for the last five financial years.

Figure 2J
Borrowings, provision for insurance claims and superannuation liability—State of Victoria



Source: Victorian Auditor-General's Office.

The state's borrowings increased by $7 769.8 million to $25 795.8 million at 30 June 2009 from $18 026.0 million at 30 June 2008. Borrowings include public sector borrowings of $20 314.5 million, derivative financial instruments of $2 784.0 million and finance leases of $2 697.3 million entered into by public sector entities. Public sector borrowings predominately are raised through the Treasury Corporation of Victoria.

The $7 769.8 million increase in borrowings included:

- $2 241.8 million in derivative financial instruments entered into to hedge risks relating to the foreign currency borrowings
- domestic and foreign currency borrowings of $5,047.3 million to primarily fund:
  - capital projects such as education renewal, water infrastructure, transport infrastructure, and health capital projects
  - the cost of dividends paid to the DTF of $154 million by the four metropolitan water bodies at lending rates of approximately 3 per cent.

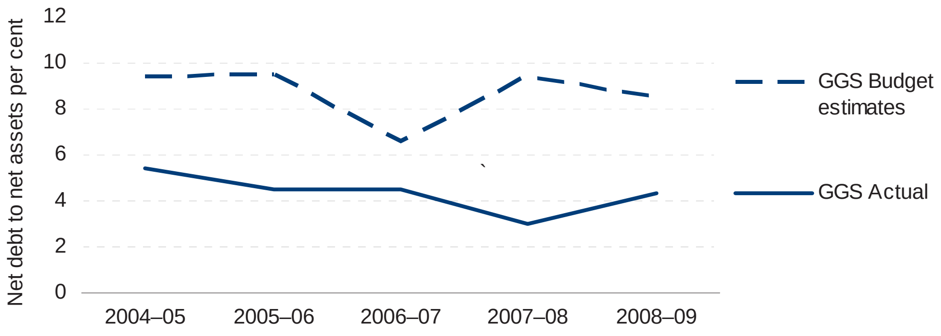
While the state projects surpluses for the GGS for the period 2009–10 to 2012–13, it also projects increased net debt. Net debt for the GGS is projected to increase from $5 291.7 million at 30 June 2009 to $16 005.8 million at 30 June 2013.

Gearing is a key measure of the extent of the state's reliance on borrowings to fund asset acquisition and growth. The ratio is calculated by net debt (borrowings, advances received and deposits held less cash and deposits, advances paid and investments, loans and placements) over net worth. A lower ratio indicates less reliance on debt to fund assets and lower exposure to rising finance costs associated with increased interest rates.

Figure 2K shows the GGS's gearing ratio for the last five financial years.

In 2008–09, the gearing ratio for the GGS has moved slightly upwards, indicating that the state's debt levels have increased during the course of 2008–09 relative to the state's asset base. This is consistent with the government decision to increase the infrastructure programs.

Figure 2K
Gearing—general government sector



Source: Victorian Auditor-General's Office.

2.3.4 Debt sustainability

Sustainable debt is the level of debt that can be paid back, principal and interest, given economic growth, interest rates and the future surplus generating capacity of the state. The measurement of debt sustainability is difficult as debt is generally repaid over a significant period where these factors are not able to be reliably forecast.

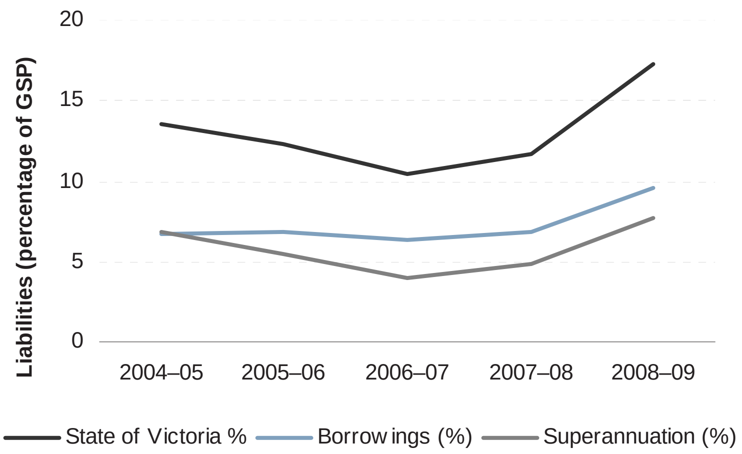
An indicator of debt sustainability is the ratio of borrowings and the superannuation liability to GSP. A lower ratio indicates that the state is better able to service its debt obligations.

Reduced levels of gross state debt resulted in a reduction of this ratio over the financial periods 2005–06 to 2007–08. In the year ended 2008–09, the ratio increased from 11.5 per cent to 17.31 per cent for the state made up of the PNFC sector from 2.1 per cent to 2.9 per cent, the PFC sector from 6.2 per cent to 8.7 per cent and for the GGS from 7.7 percent to 11.6 per cent.

By comparison the equivalent ratios of net debt plus superannuation to GSP in the year ended 2008–09 increased from –0.4 per cent to 6.09 per cent for the state, made up of the PNFC sector from 0.65 per cent to 2.04 per cent, the PFC sector from -3.5 per cent to –0.69 per cent and for the GGS from 5.6 percent to 9.7 per cent.

Figure 2L shows the state's debt sustainability for the last five financial years.

Figure 2L
Debt sustainability—State of Victoria



Source: Victorian Auditor-General's Office.

The increased debt levels reflect the commitment to growing the state's infrastructure, represented through an increased capital program.

2.3.5 Superannuation liability

The AFR includes superannuation liabilities of the state which are managed in the Emergency Services and State Super (ESSSuper), Constitutionally Protected Schemes, Parliamentary Contributory Superannuation Fund and Health Super Fund.

The schemes are not consolidated by the state as they are not controlled: however the superannuation liabilities of the state are recognised.

The Emergency Services Superannuation Scheme, which incorporates the former State Superannuation Fund, represents 96.3 per cent of the state's superannuation liability. Members of the funds include government employees under plans that are now closed. The fund pays benefits as a lump sum based on salary, period of membership, age and contribution rates during membership as these are defined benefit plans. Benefits are payable on retirement, resignation, retrenchment, death and disability. ESSSuper fund is also responsible for the trusteeship and administration of the State Superannuation Fund.

The superannuation liability represents the difference between the present value of superannuation benefits accrued to date and the value of superannuation plan assets. The liability exists due to the plan assets of the superannuation funds being insufficient to cover the accrued benefit liability to pay plan members.

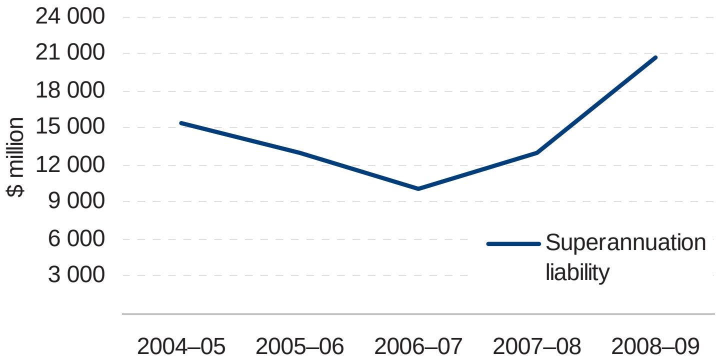
The state's superannuation liability increased from $15 345 million in 2004–05 to $20 755.1 million in 2008–09. Prior to 2007–08 the liability had been reducing. This reduction was attributed to strong returns on superannuation plan assets and the adoption, in 2000, of a funding framework aimed at fully funding the liabilities in the State Superannuation Fund by 2035.

The state's superannuation liability increased by $7 796.3 million for the 12 months ended 30 June 2009, an increase of 60.2 per cent. The increase is primarily attributed to:

- An increase of $3 693.5 million due to declining global economic conditions resulting in lower than expected investment returns on superannuation plan assets. The lower than expected returns were primarily attributed to negative performance in the international and australian equity markets of approximately 25 per cent in 2008–09 due to the global financial crisis.
- An increase of $3 879 million due to the impact of the reduction in the Commonwealth Government bond rate from 6.54 per cent to 5.7 per cent used to value the liability.

Figure 2M shows the year on year changes in the balance of the state's superannuation liability over the five year period to 2008–09.

Figure 2M
Superannuation liability—State of Victoria



Source: Victorian Auditor-General's Office.

The ESSSuper fund's expected long-term investment return on the assets invested is 8 per cent[3]. In 2008–09, ESSSuper's investment return was negative 15.1 per cent. The average investment return for ESSSuper over the period 2004–05 to 2008–09 was a positive investment return of 3.4 per cent. The volatility of the investment market continues to be a risk for the state.

3 *Annual Financial Report of the State of Victoria 2008–09.*

The prior four year average investment return was above the state's long-term expected return.

The state has confirmed its long-term strategy to fully fund the State Superannuation Fund by 2035. In accordance with the intentions to fully fund the liability, the 2009–10 Statement of Finances disclosed the following contributions included in Figure 2N:

Figure 2N
State contributions to superannuation liability

Financial year	Estimated contribution ($mil)
2009–10	535
2010–11	544
2011–12	560
2012–13	750

Source: 2009–10 statement of finances.

2.3.6 Provision for insurance claims

The AFR includes a provision for insurance claims relating primarily to the Victorian WorkCover Authority, the Transport Accident Commission and the Victorian Managed Insurance Authority. The provisions for insurance claims are independently assessed by actuaries and represent the estimated amounts payable at 30 June in respect of claims reported but not yet paid, claims incurred but not reported and the anticipated direct and indirect costs of settling those claims.

The provision for insurance claims increased from $15 228.9 million in 2007–08 to $16 625.9 million in 2008–09, an increase of $1 396.7 million (9 per cent). This increase is primarily attributed to:

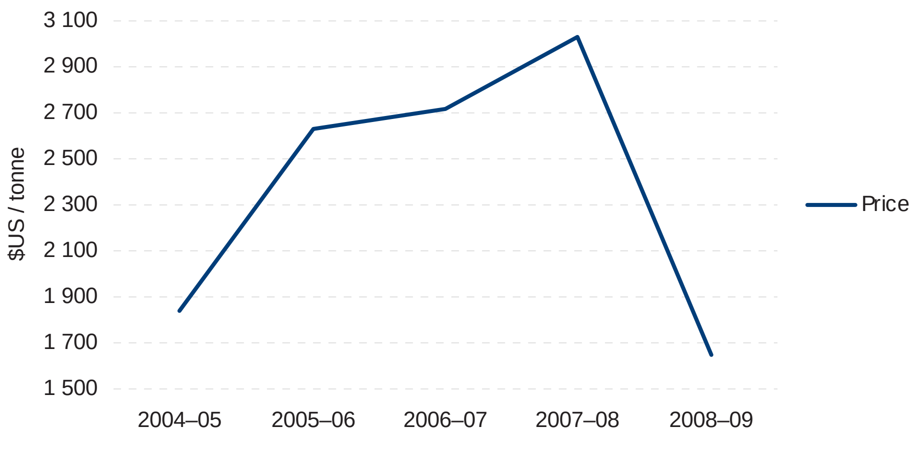
- changes in economic assumptions used in the actuarial calculation to measure the liability of approximately $400 million. In particular, the discount rate used to measure the liability decreased significantly as a result of decreases in interest rates
- an allowance for expected increase in claims of $730 million
- an increase in medical indemnity claims of approximately $115 million.

2.3.7 Onerous contract provision

The State Electricity Commission of Victoria (SECV) recognises an onerous contract provision at the end of each financial year in accordance with the *AASB 137 Provisions, Contingent Liabilities and Contingent Assets*. This provision represents obligations under low flexible tariff electricity arrangements entered into by the state in 1984 to attract investment in the Point Henry and Portland aluminium smelters. The tariff arrangements require the state, through the SECV, to subsidise the lower electricity prices charged to the smelters. The SECV is responsible for the future liabilities arising from the tariff arrangements until the smelter contracts expire in 2014 (Point Henry) and 2016 (Portland). In 2004 the Treasurer executed an agreement and Deed of Indemnity with the SECV. Under the Deed of Indemnity, the state is obliged to fund the shortfall relating to SECV's obligations under these electricity supply agreements.

The value of the SECV's obligations are assessed at the end of each financial year, taking into account changes in the electricity market and predicted future changes in aluminium and electricity prices, foreign exchange rates, discount rates and the consumer price index. During 2008–09, aluminium prices decreased significantly as a result of the Global Financial Crisis (GFC). Figure 2O shows the movements in the average aluminium prices for the period 2004–05 to 2008–09.

Figure 2O
Aluminium prices 2005–2009



Source: Victorian Auditor-General's Office.

This decline in aluminium prices resulted in SECV's net smelter contract provision changing from a positive $580 million in 2007–08, with no state Government indemnity, to a net negative $600 million in 2008–09. This shortfall resulted in the reinstatement of the state government indemnity of $536 million at 30 June 2009 representing future payments to be made to the SECV to fund the shortfall under the electricity supply agreements with the aluminium smelters.

2.3.8 Risks to financial performance and condition

There are a number of external factors which need to be continually monitored by the state in managing its short and long-term fiscal sustainability.

External factors that could impact the state's future financial performance and condition include:

- the performance of the national economy and the policy directions and decisions of the Commonwealth Government, which significantly influence the level of Commonwealth grants to the state
- volatility in the performance of the Australian and international financial and equity markets, significantly influencing the investment revenues and superannuation expenses of the state
- demographic trends expected to impact on the level and nature of services provided by the government
- the public sector workforce pressures for wage and salary growth, and the need to maintain sustainable FTE whilst meeting increased demands on service delivery
- the implementation of any Australian emissions trading scheme and climate change.

2.4 Conclusion

While the net result from transactions for the GGS is an indicator of financial performance, the financial sustainability of the state requires consideration of the state's net result. When looking at this 'bottom line' by taking into account other economic flows, the deficits in the 2007–08 and 2008–09 net results clearly demonstrates the state's exposure to financial markets and economic conditions. These factors can put at risk longer-term financial sustainability and will need to be closely monitored, so that revenue and expenditure policy settings remain sustainable.

3 Significant developments

At a glance

Background

This section includes observations on the status and financial implications of significant developments which occurred during 2008–09 and events subsequent to year end.

Findings

Victorian Bushfire Appeal Trust Fund

- The Victorian Bushfire Appeal Trust Fund had received $382 million up to 25 October 2009, an increase of $9.1 million since 30 June 2009 with payments of $78.2 million being distributed to individuals and communities since 30 June. The $169.1 million ($238.2 million at 30 June 2009) balance of the fund is to be utilised to make further distributions.

Post-balance date events

- The state government has provided a Treasurer's Guarantee over a portion of the Victorian Desalination Plant project debt, as a lender of last resort in the case that the syndication process is not successful.
- Status of the Rail Franchise is provided.

Other developments

- The channel deepening project is expected to come in ahead of schedule and under the original budget.
- The state paid $6 million for Melbourne Central City Studios in November 2008. Net assets were subsequently written down to $0.5 million and the studios continue to have a high financial viability risk.
- The state's cost for the Commonwealth Games Athletes Village has increased from the reported cost of $41 million in 2006 to $59.1 million due to lower than expected revenue as a result of reducing the number of apartments to be built (from 650 to 632). The estimated average return from each apartment has also reduced from $70 000 to $45 500.
- Status of the Food Bowl Modernisation Project, Northern Sewerage Project, Myki, and the New Melbourne Convention Centre are provided.

3.1 Introduction

This section includes observations on the status and financial implications of significant issues and developments which occurred during 2008–09 and subsequent to year end.

3.2 Victorian Bushfire Appeal Trust Fund

In line with the relevant accounting framework, the Victorian Bushfire Appeal Funds were assessed as held in trust for the beneficiaries, which included the individuals and communities affected by the bushfires. These funds are not controlled for the benefit of the Victorian Government. Accordingly, the appeal funds are not presented as assets or income of the state or the Department of Human Services (DHS). The DHS 2008–09 annual report has appropriately disclosed the appeal funds as third party funds under management. Disclosure of the fund is included in Note 35 Funds under management in the AFR.

Establishment of the Victorian Bushfire Appeal Trust Fund

Over 78 towns and communities across Victoria were devastated by the bushfire disaster in February 2009. This presented the state with exceptional circumstances within which to provide emergency assistance to the affected communities, families and individuals. On 8 February 2009, the Victorian Government, in partnership with the Commonwealth Government and the Australian Red Cross Society (Red Cross), approved the establishment of the 2009 Victorian Bushfire Appeal Trust Fund under section 19(1) of the *Financial Management Act 1994*.

The purpose of the trust fund is for the receipt of donations and other contributions, and their disbursement to assist individuals and communities in towns and rural areas affected by the bushfires.

Monies from the fund are distributed to individuals and communities through DHS at the direction of an Independent Advisory Panel. Members of the Advisory Panel were appointed jointly by the Red Cross and the Victorian Government, including a senior nominee from the Red Cross and a senior representative of DHS.

The Advisory Panel was required to set rules and criteria for the making of payments from the trust fund. The Advisory Panel's responsibilities are to guide, account for and report on the disbursement of monies from the trust fund.

Supporting the Advisory Panel is a Secretariat, and an Implementation Unit, operated by DHS. The Secretariat's role includes policy development for the different types of payments, liaison and managing stakeholder relationships. The Implementation Unit is responsible for assessing applications, making payments and working with DHS's case managers to assist bushfire affected people.

Probity and auditing arrangements established for the trust fund

On 17 February 2009, an independent probity auditor was appointed by DHS to review the establishment and operation of the Victorian Bushfire Appeal Trust Fund. The scope of the appointment did not extend to the Red Cross's collection activities as they were separately controlled and audited.

Overall, the probity auditor assessed that the control framework put in place by DHS has, with some minor exceptions, been reliable. Subsequent to the probity auditor's initial findings, key recommendations were promptly responded to by DHS.

Figure 3A shows that up to 25 October 2009, $382 million in donations and contributions had been received, with payments of $217.3 million being distributed to individuals and communities. The balance of the Trust Fund at 25 October 2009 is $169.1 million.

The Victorian Bushfire Appeal Fund Secretariat advised that the balance of the funds is to be utilised to:

- pay outstanding eligible recipients. At 25 October 2009, DHS were processing over 500 applications from bushfire affected victims. DHS has estimated that these applications amount to approximately $3 million
- assist in community rebuilding. Up to 25 per cent of the total trust funds collected are to be utilised for bushfire affected community infrastructure initiatives
- fund claims that are yet to be received
- fund any other initiatives as determined by the Advisory Panel.

Figure 3A
Victorian Bushfire Appeal Trust account receipts and payments to 25 October 2009

Item	30 June 2009 ($mil	25 October 2009 ($mil) (unaudited)	Total receipts and payments
Opening balance	–	238.2	
Donations and other contributions	375.1	6.9	382
Interest earned	2.2	2.2	4.4
Total receipts	**377.3**	**9.1**	**386.4**
Less payments to individuals and communities	139.1	78.2	217.3
Balance of fund	**238.2**	**169.1**	

Source: Victorian Auditor-General's Office.

3.3 Post-balance date events

Victorian Desalination Plant

The Department of Sustainability and Environment's Capital Projects Division is responsible for the delivery of the $3.500 million Victorian Desalination Project on behalf of the state government. The project is a key part of the Victorian Government's Water Plan released on 19 June 2007 *Our Water Our Future: The Next Stage of the Government's Water Plan*.

The project comprises the delivery of a reverse osmosis desalination plant producing 150 GL per annum of drinking water, long marine inlet and outlet tunnels to protect the coast and the marine areas, an 84 km transfer pipeline to connect to the Melbourne water network near Berwick, an 87 km underground power supply, and the delivery of renewable energy to fully offset the electricity used by the plant and transfer pipeline during operation.

The project is being delivered as a Public-Private Partnership under the *Partnerships Victoria* Policy. On 30 July 2009, the state government announced the AquaSure consortium as the successful bidder for the project. The consortium will finance, design, construct, operate and maintain the desalination plant and associated water transfer infrastructure. The power supply infrastructure will be returned to a new owner after commissioning.

The project reached contract close on 30 July 2009 and financial close on 2 September 2009. Construction commenced on the plant site on 30 September 2009. The contract has a 30-year term, with the project scheduled to deliver water by the end of 2011.

The State Government has provided a Treasurer's Guarantee over a portion of the project debt, as a lender of last resort in the case that the syndication process is not successful. The Department of Sustainability and Environment (DSE), Department of Treasury and Finance and the Treasury Corporation of Victoria (TCV) are all involved in the transaction arrangements, with any financial support required via the Guarantee to be through TCV on behalf of the State Government.

The desalination plant project team within the Capital Projects Division of DSE has been involved from June 2007 in the following activities in preparation for the construction of the plant:

- obtaining all key planning and State/Commonwealth environmental approvals
- community consultation and landowner liaison
- developing a reference design
- carrying out a range of preconstruction activities and studies
- preparation of a Partnerships Victoria business case
- plant site land acquisition, and landowner liaison on pipe and power routes
- commissioning a seawater sampling facility on the plant site
- developing tender documentation
- short-listing of two bidding consortia via an expressions of interest process

- tender evaluation and assessments of commercial, legal, financial, technical, social and environmental matters
- concluded negotiations with bidders, culminating in the award of the contract to AquaSure.

During the period 2009 to 2011, DSE will undertake in the following activities in the delivery phase of the plant:

- managing and administering the contract with AquaSure
- managing the independent reviewer and environmental auditor contract
- transfer pipeline and power supply easement land acquisition and compensation
- managing the progress of the debt syndication process
- overseeing AquaSure undertaking the design and construction of the project
- reviewing design packages prepared by AquaSure's design and construct contractor, Thiess Degremont
- managing community engagement including through the community liaison group.

Construction of the plant commenced in October 2009.

Details on the actual costs and future expected costs for DSE as at 30 June 2009 are provided in Figure 3B.

Figure 3B
Actual and expected costs for DSE

DSE actual cost to 30 June 2009 ($mil)	DSE future expected costs ($mil)
159.5	162.3

Source: Victorian Auditor-General's Office.

The $3.5 billion construction cost is to be borne by AquaSure. Water is to be ordered from AquaSure on an annual basis, three months ahead of the commencement of each financial year. Water can be ordered in block increments of 0, 50, 75, 100, 125 or 150GL. AquaSure will be paid monthly via a two part payment mechanism. A water security payment will be made provided AquaSure is capable of delivering the required quantity of water at the required quality. A separate water usage payment will be made based on the volume of water ordered. This will be for the supply of the required quantity of water to the state's water quality requirements, and includes the required renewable energy to ensure one hundred percent offsetting. The payments to AquaSure will be subject to a series of abatement tests.

The 2008–09 AFR note 36, includes disclosure of this post balance date event. As the syndication process has not been completed as at 30 September 2009, the financial impacts of this project will be included in the 2009–10 Auditor-General's Report on the AFR.

Rail franchise

The 2008–09 AFR, note 36, includes disclosure of this post balance date event. As disclosed in the AFR, on 31 August 2009 the state completed contracts with Metro Trains Melbourne (MTM) to operate and maintain Melbourne's passenger train network from 30 November 2009 for an eight year period with an extension option of a further seven years. It is estimated that MTM will receive an average of $474 million per year and will be liable for fines of up to $1 million per month for poor reliability and punctuality performance of the train network.

There is also a commitment by the state to spend a total of $1 800 million on the maintenance of the train network over the duration of the contract which includes $500 million committed to secure the reliability of the train network.

On 31 August 2009, the contract for the tram operations and maintenance was finalised with Keolis Downer EDI (KDR) appointed for an eight year period with an extension option of a further seven years. It is estimated that KDR will receive an average of $97 million per year and will be liable to fines of up to $0.5 million per month for poor reliability and punctuality performance of the tram network.

Analysis of the financial impacts of this project will be included in the 2009–10 Auditor-General's Report on the AFR.

3.4 Significant developments

Channel Deepening Project

The Port of Melbourne Corporation (the corporation) was established to promote sustainable trade growth by providing effective port services and managing sea channels for vessels to access these services. The corporation is responsible for the Channel Deepening Project (CDP) to allow larger ships, with up to a 14-metre draught, to use the port at all tides.

The CDP is a high priority for the corporation because it expects the container trade to more than treble by 2035, with trend towards using larger, more efficient vessels. Failure to provide additional channel depth is expected to force shipping companies to work around this constraint, resulting in increased shipping costs for Melbourne cargo.

The project started in February 2008. The corporation has announced that all dredging within Port Phillip Bay was completed by 31 August 2009, technical completion of dredging of the Entrance on 1 October 2009 and that the entire project is planned for completion by 31 December 2009.

Details on the budget, costs and future committed costs at 30 June 2009 are provided in Figure 3C.

Figure 3C
Budget and associated financial implications

Original budget ($mil)	Actual cost to 30 June 2009 ($mil)	Future committed cost ($mil)
969	561.6	108.8

Source: Victorian Auditor-General's Office.

Future committed costs represent contractual commitments at 30 June 2009 and do not include all future expected project costs.

The following contingent liability was reported with regard to the CDP at 30 June 2009:

- On 14 December 2007, the Minister for Environment and Climate Change approved the Channel Deepening Project under the Coastal Management Act 1995 (Vic). One of the three main conditions of the approval is a requirement on the Corporation to provide a $100 million environmental performance bond in favour of the Minister for Environment and Climate Change, to be used for any remedial action or post dredging recovery works (Recovery) as agreed with the Minister for Roads and Ports. The remedial actions must be attributable to the impacts of the Channel Deepening Project and result from:
  - a breach of the Environmental Management Plan or other terms of approval for the Channel Deepening Project; and/or
  - impacts not anticipated in the Environmental Management Plan and/or the Supplementary Environment Effects Statement.

This contingent liability continues until the earlier of:

- TCV receiving a notice from the Minister for Environment and Climate Change that the guarantee is no longer required
- the $100 million has been paid in full; or
- 5 December 2012.

When the project is completed in 2009–10 the corporation will need to assess the fair value of channel assets, and the useful lives of the channel assets for the calculation of the annual depreciation charge.

The CDP is expected to come in ahead of schedule and under the original budget.

Food Bowl Modernisation

The State Owned Enterprise for Irrigation Modernisation in Northern Victoria trading as the Northern Victoria Irrigation Renewal Project (NVIRP) was established in December 2007 to deliver the $2 000 million Food Bowl Modernisation irrigation system on behalf of the state government. The project was established as part of the *Our Water Our Future – The Next Stage of the Government's Water Plan.* The project is to be delivered in two stages.

The project aims to provide the Goulburn Murray Irrigation District with an irrigation delivery system that will reduce water losses and assist with the region's economic viability. It will aim to recover approximately 225 gigalitres of water (long-term average) which is currently lost to the system, water savings will then be shared equally by irrigators in the region, the environment and Melbourne via the Sugarloaf Pipeline.

The objectives of stage one are:

- implement water distribution and delivery efficiency improvements to deliver annual water savings within the established project cost
- deliver an improved standard and efficiency of a water delivery service with modernised connections, and
- provide a catalyst for regional economic development opportunities and improved productivity.

The NVIRP is required to undertake the following activities in Stage one of the project:

- modernisation of the larger carrier and trunk channels which will form the core backbone of the irrigation system
- replacement, rationalisation of meter outlets with new accurate meters, and
- creating new direct connections to the system for those customers who are currently connected to the distribution and spur channels.

Ownership and responsibility for the operation of the infrastructure will transfer to the Goulburn-Murray Rural Water Corporation (G-MW) as discrete portions of the capital works are completed.

Stage One project works have commenced and are structured around the upgrade of manually operated channels and control systems to automated irrigation delivery systems to be delivered by 31 December 2012. This will allow better measurement of water flows enabling channel repairs to be undertaken where the worst seepage and leakage losses exist.

Stage Two, the further modernisation of irrigation infrastructure in the Goulburn Murray Irrigation District is to be funded by the Commonwealth Government. The Commonwealth has agreed in-principle to contribute up to 90 per cent of the project costs up to $1 000 million which is expected to deliver a further 200GL of water savings.

Figure 3D provides the budget, costs and future commitments and quantifiable contingencies as at 30 June 2009.

Figure 3D
Budget, cost and future commitments

Stage	Original budget ($mil)	Actual cost to 30 June ($mil)	Future committed cost ($mil)
Stage 1	1 004.5	168.1	836.4
Stage 2	1 000	–	–

Source: Victorian Auditor-General's Office.

Figure 3E provides details on entities funding stage 1 and the contribution for each entity.

Figure 3E
Budgeted, actual and outstanding contributions

Entity	Original budget contribution ($mil)	Contributions made to date	Outstanding contributions
Department of Sustainability and Environment	604.5	167.4	437.1
City West Water Limited	100	15	85
South East Water Limited	100	15	85
Yarra Valley Water Limited	100	15	85
Goulburn-Murray Rural Water Corporation	100	–	100
Total	**1 004.5**	**212.4**	**792.1**

Source: Victorian Auditor-General's Office.

During 2008–09 it was decided the Melbourne Water Corporation would no longer be required to make a $300 million contribution. The three retail distribution companies will now contribute $100 million each to the project. The retailers have made the contributions on the basis that two new bulk water entitlements (BWE’s) will be finalised, approved and issued by the State Government during November and December 2009 following parliamentary approval.

Analysis of the financial impacts of this project will be included in the 2009–10 Auditor-General’s Report on the AFR.

Northern Sewerage Project

Announced in 2004 under the Victorian State Government's Yarra River Action plan, the Northern Sewerage Project (NSP) involves the construction of 12.5 km of new sewer from Reservoir to Pascoe Vale that will:

- increase the capacity of the sewerage system for Melbourne's growing northern suburbs
- help protect the Merri and Moonee Ponds Creeks from the damaging impact of sewage overflows that can occur after heavy rain as well as preventing damage to private property and help to improve the health of our waterways flowing into the Yarra River.

The NSP is a joint project being undertaken by Melbourne Water Corporation and Yarra Valley Water Limited. Total project costs are estimated at $650 million.

The project commenced in August 2007 and is on schedule for completion and commissioning in mid 2012.

Details on the budget, costs and future commitments and contingencies as at 30 June 2009 are provided in Figure 3F.

Figure 3F
Budget and associated financial implications

	Original budget ($mil)	Actual cost to 30 June 2009 ($mil)	Future committed cost ($mil)
Melbourne Water Corporation as at 30 June 2009	422.1	172.9	253.6
Yarra Valley Water Limited as at 30 June 2009	228	71.9	156.1

Source: Victorian Auditor-General's Office.

Analysis of the financial impacts of this project will be included in the 2009–10 Auditor-General's Report on the AFR.

Myki

Myki is Victoria's new ticketing system that will replace the Metcard and V/line ticketing systems and paper tickets on regional buses, providing one integrated ticketing solution for all modes of transport within the state. The myki smartcards allow commuters to credit the card's balance online, via the phone or on the transport system itself.

The Transport Ticketing Authority (TTA) was established in June 2003 as a state body to oversee the current public transport ticketing system and to procure and manage the new myki ticketing system for Victoria.

The decision to replace the Metcard ticketing system with a new smartcard system was announced in 2004. In 2005 a contract for the development, installation and operation of the new ticketing system was awarded to Keane Australia Micropayment Consortium Pty Ltd (Kamco) for a total of $494 million. In addition to the Kamco contract, $505 million was budgeted for on-going operating costs to run the existing Metcard system until 2008 and development and running of the new replacement system until 2017, bringing the total budget to $999 million.

In 2008, an additional $352 million was allocated to the project, $79 million to operate the existing Metlink system for a further 18 months and $271 million in capital funding for extra myki machines and additional system functionality. The total revised budget is now $1 351 million.

Myki is now operating on town buses in Ballarat, Bendigo, Geelong, Seymour, Warragul and Latrobe Valley (covering Moe, Morwell and Traralgon). Progressive implementation is scheduled throughout 2009–10 for Melbourne with 485 trams, 2219 buses and 217 train stations fitted out with the new myki equipment, with the expectation that operations will begin in late 2009. It is expected that both the myki and Metcard systems will operate in parallel throughout the 2009–10 financial year.

Details on the budget, costs and future commitments at 30 June 2009 are provided in Figure 3G.

Figure 3G
Budget, costs and future commitments

Budget ($mil)	Total expenditure to 30 June 2009 ($mil)	Future committed cost ($mil)
Capital: 454	Capital 261.4	Capital: 120
Operating: 897	Operating 201.6	Operating: 367.4
1 351	**463**	**487.4**

Source: Victorian Auditor-General's Office.

The capital spend from 17 June 2003 to 30 June 2009 totalled $261.4 million, acquiring the following significant assets for the new ticketing system:

- hardware $145.3 million
- software $97.6 million
- devices $14.1 million
- other assets to support the operation of the authority total $4.4 million.

The operating spend from 17 June 2003 to 30 June 2009 totalled $201.6 million. This included $95.7 million to the operator of the existing ticketing system for the period 1 March 2007 to 30 June 2009. The balance of operating expenditure comprised:

- service charges – Kamco $36.7 million
- employee benefits $22.4 million
- decommissioning existing system $4.4 million
- access payments to transport operators $4.4 million

- depreciation $2.9 million
- other more general operating costs to 30 June 2009 were $35.1 million.

The committed operating costs of $367.4 million are for a 10 year period from 1 July 2009 to 30 June 2019. In 2009–10 and 2010–11 committed operating costs are $92.4 million and $73.3 million respectively. From 2011–12 to 2018–19 the average committed operating cost drops to $25.3 million. Higher committed operating costs throughout 2009 to 2011 are due to establishment of the system.

Additional capital and operating costs of $393.6 million are forecast, however, these have not been contracted for at 30 June 2009.

The existing Metcard system is owned and operated by a private company and therefore responsibility for generating ticketing revenue currently sits outside of the state. The state's role to distribute the revenue to the private operators, once collected, will remain unchanged. In 2009–10, the state will need to gain assurance that adequate controls have been designed to capture, record and monitor the estimated $800 million per annum in ticketing revenue.

New Melbourne Convention Centre

As part of its 2004 *Economic Statement Victoria: Leading the Way*, the state government announced its support of the development of a new Melbourne Convention Centre adjacent to the Melbourne Exhibition Centre. The new Convention Centre includes a 5 000 seat plenary hall and integrated commercial development of the surrounding south wharf precinct. The development would give Melbourne a versatile and advanced Convention Centre, the largest of its kind in Australia.

In February 2006, a consortium was selected, to deliver the project under the public private partnership project model as per the Partnerships Victoria framework. The project agreement was finalised in May 2006 and established two distinct phases for the project; the design and construction phase in which the private sector consortium led by Plenary Group was responsible for the design, construction and financing of the new convention centre and the 25 year operating phase which commenced on 1 January 2009.

In the operating phase, the consortium is to provide various contracted operating services in return for a quarterly service payment from the state. At the end of the operating phase the asset will transfer to the state.

The new Convention Centre was officially opened on 5 June 2009.

This arrangement has been classified as a finance lease in accordance with AASB 117 *Leases* and AASB Interpretation 4 – *Determining whether an arrangement contains a lease*. The Department of Innovation, Industry and Regional Development (DIIRD) and the AFR included an asset and finance lease liability of $455.4 million and quarterly service payments which are split between service and lifecycle costs, finance costs and capital repayments over the term of the lease.

The Melbourne Convention and Exhibition Trust (MCET) is responsible for marketing and operating the new facility. DIIRD, on behalf of the state, entered into a loan agreement with MCET under which MCET undertakes to repay the state's 50 per cent or $227.5 million of the value of the asset ($455 million) over the 25 year lease period.

Figure 3H provides the nominal value of the total cash outflows of the new arrangement. The service and lifecycle costs are for maintenance of the existing exhibition centre and the new convention centre.

Figure 3H
Estimated commitments of new facility at start of the lease

Total value of estimated commitments	$'000
Cost outflows	
Service and life-cycle costs	547 826
Finance costs	823 997
Principal repayment	455 421
Total cash payments over the term of the lease	**1 827 244**
Revenue inflows	
Sale of land	–13 000
Rights to car parking revenue for 25 years	–43 000
Commercial development lease agreement paid in advance for 99 years	–37 000
Total cost to the state	**1 734 244**

Source: Department of Innovation, Industry and Regional Development Annual Report 2008–09.

Details on the budget and future commitments for the MECC as at 30 June 2009 are provided in Figure 3I.

Figure 3I
Original budget and future commitments for the MECC

State's original budget contribution ($mil)	State's actual contribution ($mil)	Future committed cost ($mil)
370.0		Operating 544.8
	370.0	Capital and finance costs –1 269.2

Source: Victorian Auditor-General's Office.

Melbourne Central City Studios

In 2002 the state entered into an agreement with a developer to build and operate film and television studios at Melbourne's Docklands precinct. The government loaned the developer $31.5 million to build the studios.

To assist the developer to be more competitive in the global film and television market the original contract was altered in 2004. The state:

- guaranteed $14.5 million of the developer’s borrowings
- deferred the repayment of the state’s loan to February 2008 with interest to be accrued and added to the loan principal
- suspended lease payments to the state for the studio site for the first 3 years of the new arrangements
- funded improved perimeter fences for the studios
- charged a peppercorn rent for the use of certain crown land and transferred ownership of a warehouse on the land to the developer.

In June 2008, the operator of the film and television studios requested the State to buy the operating company. Following negotiations, the state then purchased all the shares in the holding company operating the film and television studios for $6 million in November 2008.

At the date of purchase, the net assets were recorded in the company’s financial report at $11.7 million. Subsequent to the purchase a valuation of the assets conducted by the state resulted in a write down of $11.2 million leaving net assets of $0.5 million. A summary of the financial position of the acquired studios is provided in Figure 3J.

Figure 3J
Summary of the financial position of the acquired studios

	Balance sheet June 2008 ($mil)	Revised June balance sheet ($mil)
Assets	61.3	50.1
Liabilities	49.6	49.6
Net assets	**11.7**	**0.5**
Issued capital	4.6	4.6
Asset revaluation reserve	17.8	6.6
Retained earnings	–10.7	–10.7
Equity	**11.7**	**0.5**
Purchase price	**6**	**6**

Source: Victorian Auditor-General's Office.

In 2008–09:

- the studio recorded a net loss of $6.8 million
- the studio’s trading cashflows were not sufficient to meet rental, loan interest and principal obligations. The state has granted the studios a further exemption from making rental, loan and interest repayments until 30 June 2009.

The studios are assessed as having a high financial viability risk due to their current year losses while 30 June 2010 operating cash flow forecasts are also uncertain. An assessment of key indicators of financial health and business forecasts for the studios indicates high financial viability risk. The future plans and forecasts for the studios are sensitive to the global economy and are therefore uncertain. Forecasted revenue for the studios is dependent on US film production. As the Australian dollar strengthens against the United States dollar, American film companies are withdrawing from film production in Australia.

Figure 3K provides key indicators of financial sustainability for the studios.

Figure 3K
Indicators of financial health for the studios

	30 June 2008 ($mil)	30 June 2009 ($mil)
Net operating cash flows	1.680	–0.756
Cash reserves	1.752	0.687
Current asset ratio	0.95:1	2.80:1

Source: Source: Victorian Auditor-General's Office.

The Commonwealth Games Athletes Village

To meet the accommodation requirements of the 6 000 athletes and officials of the 2006 Commonwealth Games, the state entered into an agreement with the Village Park Consortium to build an athletes' village in inner Melbourne.

The intention of the agreement was that housing for the athletes' village would form part of a larger, integrated private and social housing development now known as Parkville Gardens. The housing estate was expected to be completed by 31 December 2011, and was estimated to provide $82.9 million in revenue back to the state. This figure was calculated in 2006 using a projected build mix of 650 apartments and 168 houses.

The project development agreement allows the developer to determine the final product mix of the site and offers a number of completion date options: the latest of which could be 31 December 2018. This means that the carrying value of the expected revenue stream may continue to fluctuate.

Figure 3L shows the financial implications for the Commonwealth Games Athletes Village at 30 June 2009.

Figure 3L
Financial Implications for the Commonwealth Games Athletes Village at 30 June 2009

Estimated revenue to the state 30 June 2006 ($mil)	Revised estimated revenue to the state 30 June 2009 ($mil)	Actual revenue received to date 30 June 2009 ($mil)
82.9	64.8	37.3

Source: Victorian Auditor-General's Office.

The decrease in the revised estimated revenue is as a result of reducing the number of apartments to be built (from 650 to 632). The estimated average return from each apartment has also reduced from $70 000 to $45 500. The present value of the revenue expected to be received in future financial years from the sale of the uncompleted apartments was estimated to be $27.5 million at 30 June 2009.

These revised revenue forecasts reduced the expected original return to the state. The state's costs for the Village increased from the reported cost of $41.0 million in 2006 to $59.1 million as shown in figure 3M.

Figure 3M
Total contribution made to the village by the state.

Item	Estimated figures 30 June 2006 ($mil)	Revised figures 30 June 2009 ($mil)
Contributions by the state to the village project		
Land	46.6	
Cash	52.3	
Scope changes	43.3	
Social housing	35.1	
Project management	14.2	
Environmental works	15.6	
Total outflows	**207.1**	**207.1**
Revenue from sales	82.9	64.8
Use of the games village	3.9	
Social housing	43.8	
Environment works	15.6	
Land	19.9	
Total inflows	**–166.1**	**–148**
Net contribution by the state	**–41**	**–59.1**

Source: Victorian-Auditor General's Office, based on the information from the OCGC and additional analysis.

Appendix A. Material entities

A.1 Material entities for 2008–09 financial year

General government sector

Entity
Austin Health
Alfred Health (formally known as Bayside Health)
Barwon Health
Country Fire Authority
Department of Education and Early Childhood Development
Department of Human Services
Department of Innovation, Industry and Regional Development
Department of Justice
Department of Planning and Community Development
Department of Premier and Cabinet
Department of Primary Industries
Department of Sustainability and Environment
Department of Transport
Department of Treasury and Finance
Eastern Health
Melbourne Health
Metropolitan Fire and Emergency Services Board
National Gallery of Victoria
Office of the Chief Commissioner of Police (Victoria Police)
Parks Victoria
Roads Corporation (Vic Roads)
Royal Children's Hospital
Southern Health
Victorian Commission for Gambling Regulation
Victorian Skills Commission
Western Health

Public non-financial corporations

Entity
Barwon Region Water Corporation
City West Water Limited
Goulburn-Murray Rural Water Corporation
Melbourne Water Corporation
Port of Melbourne Corporation
South East Water Limited
State Electricity Commission of Victoria
V/Line Passenger Corporation
Victorian Energy Networks Corporation (VENCorp)
Victorian Rail Track
Victorian Urban Development Authority (VicUrban)
Yarra Valley Water Limited

Public financial corporations

Entity
Rural Finance Corporation
Transport Accident Commission (TAC)
Treasury Corporation of Victoria
Victorian Managed Insurance Authority
Victorian WorkCover Authority

Other entities

The following entities are also deemed material entities that required certification of a particular balance in their financial statements

Entity	Certification required for:
Emergency Services Superannuation Scheme	Unfunded superannuation liability
Residential Tenancies Bond Authority	Monies held in trust
Senior Master of the Supreme Court	Monies held in trust
State Trustees Limited*	Monies held in trust

Appendix B. Acronyms and glossary

B.1 Acronyms

AASB	Australian Accounting Standards Board
AAS	Australian Accounting Standards and Interpretations
ABS	Australian Bureau of Statistics
ABS GFS	Australian Bureau of Statistics Government Finance Statistics
A-IFRS	Australian Equivalents to International Financial Reporting Standards
AFR	Annual Financial Report
A-GAAP	Australian Generally Accepted Accounting Principles
BMS	Business Management System
DTF	Department of Treasury and Finance
EBA	Enterprise Bargaining Agreement
ESSS	Emergency Services and State Super Fund
FMA	Financial Management Act 1994
FRD	Financial Reporting Direction
FTE	Full-time equivalent
GDP	Gross Domestic Product
GFC	Global Financial Crisis
GGS	General Government Sector
GSP	Gross State Product
PFC	Public Financial Corporation
PNFC	Public Non-Financial Corporation
SECV	State Electricity Commission of Victoria
VAGO	Victorian Auditor-General's Office.

B.2 Glossary

Actuarial gain/loss

Unrealised gain or loss experienced due to fair value movements of a superannuation liability between specific periods of time.

Acquisition

Acquisition, in relation to assets, means establishing control over the asset, undertaking the risks, and receiving the rights to future benefits, as would be conferred with ownership, in exchange for a cost of acquisition.

Asset

A resource controlled by an entity as a result of past events, and from which future economic benefits are expected to flow to the entity.

Asset's useful life

An asset's useful life is the period over which it is expected to provide the entity with service. Depending on the nature of the asset, useful life can be expressed in terms of time or output.

Auditor's opinion

Positive written expression within a specified framework indicating the auditor's overall conclusion on the financial report based on audit evidence obtained. A clear opinion indicates that the financial report has been prepared in accordance with the requirements of relevant legislation and Australian accounting standards.

Audit Act 1994

The *Audit Act 1994* establishes the operating powers and responsibilities of the Auditor-General. This includes the operations of his office – the Victorian Auditor-General's Office (VAGO) as well as the nature and scope of audits conducted by VAGO. The Act also addresses the relationship of the Auditor-General with the Committee as the representative body of Parliament and the Auditor-General's accountability to Parliament for discharge of the position's responsibilities.

Capital expenditure

Amount capitalised to the balance sheet for contributions by a public sector entity to major assets owned by the entity, including expenditure on:

- capital renewal of existing assets that returns the service potential or the life of the asset to that which it had originally
- capital expansion which extends an existing asset at the same standard to a new group of users.

Commitments

Commitments include those operating, capital and other outsourcing commitments arising from non cancellable contractual or statutory sources.

Comprehensive result

The net result of all items of income and expense recognised for the period. It is the aggregate of operating result and other movements in equity.

Consolidation

The process of adjusting and combining financial information from the individual entities in each government sector to prepare the consolidated financial statements and present financial information for the State as a whole.

Contingent asset

A possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one, or more uncertain future events, not wholly within the control of the entity.

Contingent liability

- A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
- a present obligation that arises from past events but is not recognised because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii)the amount of the obligation cannot be measured with sufficient reliability.

Debt securities

Securities representing money borrowed by an issuer that must be paid back at a specific date. The security pays interest or is purchased at a discount to face value.

Debt sustainability

Debt sustainability is the ratio of borrowings and the superannuation liability to GSP and is a key measure of the state’s ability to support and finance its debt. A lower ratio indicates that the state is better able to service its debt obligations.

Deficit

A shortfall; an excess of expenditure over revenue.

Depreciation

The systematic apportionment of an asset’s capital value as an expense over its estimated useful life to take account of normal usage, obsolescence, or the passage of time.

Derivative financial instrument

A financial contract that derives its value from changes in underlying assets or indices.

Entity

Is a body whether corporated or unincorporated that has a public function to exercise on behalf of the state or is wholly owned by the state, including: departments, statutory authorities, statutory corporations and government business enterprises.

Fair value

The amount for which an asset (financial or non financial) could be exchanged between knowledgeable, willing parties in an arm's length transaction.

Financial assets

A financial asset is any asset that is

- cash
- an equity instrument of another entity
- a contractual right
  - to receive cash or another financial asset from another entity, or to exchange financial assets or;
  - financial liabilities with another entity under conditions that are potentially favourable to the entity
- a contract that will or may b settled in the entity's own equity instruments and is:
  - a non derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments or;
  - a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments.

Financial instruments

A contract that represents a financial asset of one party and a financial liability or equity instrument of another party.

Financial Management Act 1994

The *Financial Management Act 1994* was developed to improve financial administration and accountability and provide for annual reporting to the Parliament by all Victorian public sector agencies.

Financial reporting direction

Financial reports are prepared in accordance with Australian Accounting Standards and Interpretations (AASs) as issued by the Australian Accounting Standards Board (AASB). Where a AASB standard provides accounting treatment options, the Department of Treasury and Finance issues Financial Reporting Directions (FRDs) to ensure consistent application of accounting treatment across the Victorian public sector in compliance with that particular standard.

Financial sustainability

An entity's ability to manage financial resources so it can meet spending commitments, both at present and into the future.

Financial year

The period of 12 months from which a financial report is prepared ending on 30 June each year.

Fiscal stimulus funding

Government funding provided through grants in an attempt to stimulate the economy.

General government sector

The GG sector comprises all government departments, offices and other bodies engaged in providing services free of charge or at prices significantly below their cost of production. General government services include those which are mainly non market in nature, those which are largely for collective consumption by the community, and those which involve the transfer or redistribution of income. These services are financed mainly through taxes, other compulsory levies and user charges. A listing of all entities comprising the GG sector is included in Appendix A.

Government finance statistics

Government Finance Statistics (GFS) enables policy makers and analysts to study developments in the financial operations, financial position and liquidity situation of the Government. More details about the GFS can be found in the Australian Bureau of Statistics (ABS) GFS Manual *Australian System of Government Finance Statistics: Concepts, Sources and Methods 2005.*

Grants and other transfers

Transactions in which one unit provides goods, services, assets (or extinguishes a liability) or labour to another unit without receiving approximately equal value in return. Grants can either be of a current or capital nature.

Gross state product (GSP)

The measurement of economic output for the state. It is the sum of all value added by industries within the state and serves as a counterpart to the gross domestic product (GDP) for a nation.

Infrastructure

Fixed capital assets, such as schools and hospitals, which support the provision for services. Infrastructure can also refer to a network of reticulated services such as roads, energy services, rail, airports etc.

Internal control

A process affected by an entity's structure, work and authority flows, people and management information systems, designed to assist the entity accomplish specific goals and objectives. Internal control is a means by which an entity's resources are directed, monitored and measured. It plays an important role in preventing and detecting fraud and protecting the entity's resources.

Inter-sector transactions

Transactions that occur between Victorian public sector entities within one sector, which are eliminated upon consolidation.

Joint venture

A contractual agreement joining two or more parties, for the purpose of executing a particular business undertaking. All parties agree to share in the profits and losses of the enterprise.

Liability

A present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

Managed investments

A unit trust which allows investors to pool their money with that of other investors so that the fund can buy a wide range of investments. These investments are primarily managed in Government by the Victorian Funds Management Corporation who makes the investment decisions.

Materiality

Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial report. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatement. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have if it is to be useful.

Material entity

Material entities represent those entities which are collectively deemed to have a significant effect on the transactions and balances reported in the state's annual report. The selection of these entities follows a detailed analysis of the financial operations of all controlled entities and takes into account any major risk factors that are attached to specific entities or portfolios.

Net Debt

Net debt equals sum of deposits held, advances received, government securities, loans and other borrowings less the sum of cash and deposits, advances paid and investments, loans and placements, and investment in GG sector entities using the equity method.

Net present value

The total present value of a time series of cash flows. It is a standard method for using the time value of money to appraise long-term projects.

Net result

Net result is a measure of financial performance of the operations for the period. It is the net result of items of revenue, gains and expenses (including losses) recognised for the period, excluding those that are classified as 'other non owner movements in equity'.

Net result from transactions

Net result from transactions is a key fiscal aggregate and is revenue from transactions minus expenses from transactions. It is a summary measure of the ongoing sustainability of operations. It excludes gains and losses resulting from changes in price levels and other changes in the volume of assets. It is the component of the change in net worth that is due to transactions and can be attributed directly to government policies.

Net worth

Assets less liabilities, It is an economic measure of wealth and reflects the contribution of jurisdictions to the wealth of Australia.

Nominal value

The total value of a commitment.

Non financial assets

Non financial assets are all assets that are not financial assets. It includes inventories, land, buildings, infrastructure, road networks, land under roads, plant and equipment, cultural and heritage assets, intangibles and biological assets such as commercial forest.

Onerous contract

A type of contract where the costs involved with fulfilling the terms and conditions of the contract are higher than the amount of economic benefit received.

Other economic flows

Other economic flows are changes in the value or value of an asset or liability that do not result from transactions. It includes gains and losses from disposals, revaluations and impairments of non current physical and intangible assets; actuarial gains and losses arising from defined benefit superannuation plans; fair value changes in financial instruments and agricultural assets; and depletion of natural assets (non produced) from their use or removal. In simple terms, other economic flows are changes arising from market remeasurements.

Public financial corporations sector (PFC)

PFC's are bodies primarily engaged in the provision of financial intermediation services or auxiliary financial services. They are able to incur financial liabilities on their own account (e.g. taking deposits, issuing securities or providing insurance services). A listing of all entities comprising the PFC sector is included in Appendix A.

Public non-financial corporations sector (PNFC)

The PNFC sector comprises bodies mainly engaged in the production of goods and services (of a non financial nature) for sale in the market place at prices that aim to recover most of the costs involved (e.g. water and port authorities). In general, PNFCs are legally distinguishable from the governments which own them; A listing of all entities comprising the PNFC sector is included in Appendix A.

Return on superannuation plan assets

Interest, dividends and other revenue derived from superannuation plan assets, together with realised and unrealised gains or losses on the assets, less any costs of administering the superannuation plan and less any tax payable by the superannuation plan itself.

Revaluation

The act of recognising a reassessment of values for non-current assets at a particular point in time.

Risk

The chance of a negative impact on the objectives, outputs or outcomes of the entity.

Sale of goods and services

Refers to revenue from the direct provision of goods and services and includes fees and charges for services rendered, sale of goods and services, fees from regulatory services, work done as an agent for private enterprises. It is also rental income under operating leases and on produced assets such as buildings and entertainment, but excludes rent income from the use of non produced assets such as land. User charges includes sale of goods and services revenue.

Surplus

Total revenue exceeds total expenditure resulting in a profit.

Auditor-General’s reports

Reports tabled during 2009–10

Report title	Date tabled
Local Government: Results of the 2008–09 Audits (2009–10:1)	November 2009
Public Hospitals: Results of the 2008–09 Audits (2009–10:2)	November 2009
Towards a ‘smart grid’—*the roll-out of Advanced Metering Infrastructure* (2009–10:3)	November 2009
Responding to Mental Health Crises in the Community (2009–10:4)	November 2009
Management of the Community Support Fund (2009–10:5)	November 2009

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