VAGO
Victorian Auditor-General's Office

Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2023–24

November 2024

Victorian Auditor-General's Report 2024–25:5

This report is printed on Monza Recycled paper. Monza Recycled is certified Carbon Neutral by The Carbon Reduction Institute (CRI) in accordance with the global Greenhouse Gas Protocol and ISO 14040 framework. The Lifecycle Analysis for Monza Recycled is cradle to grave including Scopes 1, 2 and 3. It has FSC Mix Certification combined with 99% recycled content.

ISBN 978-1-921060-93-9

VAGO

Victorian Auditor-General's Office

Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2023–24

Independent assurance report to Parliament

Published by order, or under the authority, of the Parliament of Victoria

November 2024

VAGO

Victorian Auditor-General's Office

Hon Shaun Leane MLC
President
Legislative Council
Parliament House
Melbourne

The Hon Maree Edwards MP
Speaker
Legislative Assembly
Parliament House
Melbourne

Dear Presiding Officers

Under the provisions of the *Audit Act 1994*, I transmit my report *Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2023–24*.

Yours faithfully

[redacted]

Andrew Greaves
Auditor-General
22 November 2024

The Victorian Auditor-General's Office (VAGO) acknowledges the Traditional Custodians of the lands and waters throughout Victoria. We pay our respects to Aboriginal and Torres Strait Islander communities, their continuing culture, and to Elders past and present.

Contents

Report snapshot

About this report	In this report, we share outcomes of our audit on the state's financial report and our independent perspective on the state's financial outcomes and risks to fiscal sustainability.

Audit outcomes (Section 2)

The 2023–24 Annual Financial Report of the State of Victoria (AFR) is free from material error and we issued an unmodified (clear) audit opinion on it.

We issued clear opinions on 28 of the 30 material entities' financial reports.

We were unable to express an opinion on whether the distracted driver fines income reported by the Department of Justice and Community Safety (DJCS) was complete and therefore issued a modified opinion on its financial report.

We also continued to modify our audit opinion on the financial report of Victorian Rail Track (VicTrack) because of how it accounts for assets it leases to the Department of Transport and Planning (DTP).

These modifications did not impact our opinion on the AFR because:

- for DJCS, the matter was not material to the state's financial report
- for VicTrack, the Department of Treasury and Finance (DTF) made a central adjustment on consolidation of the state's financial report to correct the issue.

Financial outcomes for the general government sector and risks to fiscal sustainability (Section 3)

The general government sector (GGS) incurred another operating loss this year of $4.2 billion. This brings accumulated losses over the last 5 years to $48 billion. The government attributes $31.5 billion of these losses to its COVID-19 response and $16.5 billion to providing ongoing public services:

- Revenue was $8.4 billion higher compared to 2022–23 because of greater tax receipts from the COVID debt levy and improved economic conditions. The Transport Accident Commission (TAC) also paid the government a $1.1 billion dividend and the Australian Government paid $1.7 billion more in grant funding.
- Operating expenses increased by $3.7 billion compared to 2022–23 because of higher public sector employee costs and other operating expenses. Interest expenses on debt also increased by $1.7 billion due to new or refinanced borrowings at higher interest rates. The interest expense now makes up 6.1 per cent of the GGS operating revenue and is expected to increase to 8.8 per cent by 2027–28.

This year's GGS operating cash surplus of $2.6 billion included an unexpected $0.7 billion pass-through grant from the Australian Government for local councils, paid at the end of the financial year. The pass-through grant was not paid out within the financial year.

The GGS fiscal cash deficit of $14.4 billion is expected to continue to 2027–28. This means the government's combined cash outlays on operating activities and its investment in capital projects remained greater than its operating cash inflows, which is a continuation of the last 8 years.

Prolonged operating losses and ongoing fiscal cash deficits are not financially sustainable, largely because they lead to higher debt levels than otherwise and indicate underlying structural risks.

The value of cumulative cost saving initiatives announced from 2019–20 to 2027–28 is now $9.0 billion, with $4.9 billion to be achieved over the next 4 years. Achieving these savings and maintaining current service levels will be challenging given several emerging financial risks.

GGS gross debt rose again this year at a pace faster than revenue and economic growth to $168.8 billion. It is projected to grow to $228.2 billion by 30 June 2028. The government's present strategy is to manage debt levels relative to the state's economy. In this regard, the government has committed to start reducing net debt to gross state product (GSP) in 2027–28.

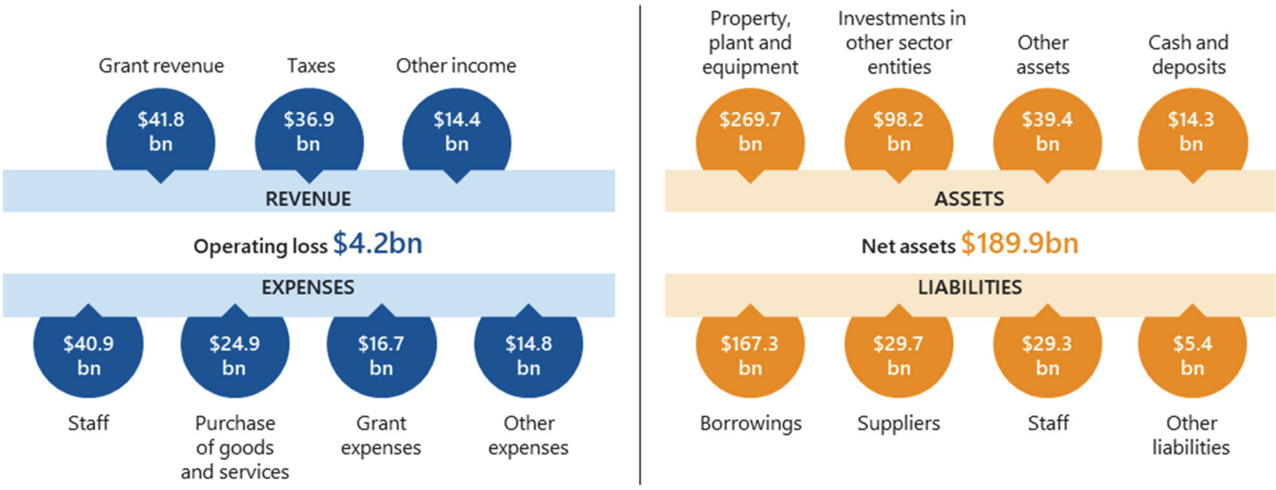
Sound financial management is foundational to fiscal sustainability. A clear and well defined long-term financial plan is required and integral to a robust and mature financial management framework.

Key matters arising from our audits of material entities (Section 4)

We identified financial control weaknesses at some material entities that impact the reliability and usefulness of their financial reports.

We also continued to find significant weaknesses in information technology (IT) system controls across many material entities. Disappointingly, a number of prior-year IT control deficiencies remain unresolved, reflecting ongoing weaknesses in their control environments.

Key numbers: general government sector



Note: Numbers are rounded.
Source: VAGO.

Our recommendations

We consulted with the audited agencies and considered their views when reaching our conclusions. The agencies' full responses are in Appendix A.

This year's recommendations

Recommendations			**Agency response(s)**
Department of Treasury and Finance	**1**	Work with the government to: • better articulate its longer-term financial plan that prioritises the management of existing and emerging financial risks • use this long-term plan as a framework to anchor government decision-making in the allocation of public resources to emphasise alignment with financial and economic strategies • transparently report this plan and ongoing progress against the plan to Parliament and the public (see Section 3).	Noted
	2	Enhance its public reporting to demonstrate progress against saving initiatives and efficiency dividends outlined in the state Budgets and the realisation of their benefits (see Section 3).	Noted
Department of Premier and Cabinet	**3**	Undertake a post-implementation review of the 2022 machinery-of-government changes, including: • working together with impacted departments to understand collective experiences • sharing findings and lessons learnt with the government to improve planning, implementing and operationalising future machinery-of-government changes (see Section 4).	Accepted

Several material entities	**4**	Extending from our recommendation last year, we recommend relevant material entity chief financial officers:
		• develop and implement robust quality assurance processes over the financial information provided to the Department of Treasury and Finance
		• ensure:
		  • internal processes are documented well enough to enable a new starter to understand what submission processes and obligations are required by the Department of Treasury and Finance, how these processes are to be done and by when
		  • adequate training and knowledge transfer occurs for all key finance staff to support the process (see Section 2).
			–

Follow-up on prior-year recommendations

Recommendations			Agency response(s)	2023–24 update
Department of Treasury and Finance	**1**	Consider why quality issues with information provided by material entities arise and determine whether further training and guidance are required.	Accepted	Quality issues with financial information continue to exist. Refer to Section 2 of the report for an extended recommendation on this.
	2	Work with the government to set specific targets and precise timing of achieving its key financial measures and targets of net debt to gross state product and interest expense to revenue.	Noted	–
	3	Work with the government to outline its debt management strategy including when and how the state will be able to start to pay down the debt that it has and plans to accumulate.	Noted	The government's present strategy is to manage debt levels relative to the state's economy. In this regard the government has committed to reduce net debt to gross state product from 25.2 to 25.1 per cent by 2027–28. Refer to Section 3 of the report.
Relevant material entities	**4**	Develop and implement a robust quality assurance process over financial information provided to Department of Treasury and Finance for Annual Financial Report of the State of Victoria purposes.	–	Quality issues with financial information continue to exist. An extended recommendation is provided in this year's recommendations above.
	5	Prioritise the resolution of information technology control deficiencies that pose a risk to achieving complete and accurate financial reporting, business objectives or compliance with legislation.	–	Information technology deficiencies continue to exist. Refer to Section 4 of the report.
Department of Premier and Cabinet	**6**	Work with the government, departments and state-controlled entities to reconsider the tabling schedule of annual reports, to reduce the information burden on Parliamentarians and the Victorian community, of tabling high volumes at the same time.	Not accepted	Tabling of annual reports remains delayed. Refer to Section 2 of the report.

Recommendations			Agency response(s)	2023–24 update
Department of Jobs, Skills, Industry and Regions	**7**	Appoint an independent evaluator to assess and report on the effectiveness of the Business Costs Assistance Program and Licensed Hospitality Venue Fund grants programs and whether value for money was achieved. The evaluation should identify lessons learnt and make recommendations for future programs.	Accepted	In progress. Refer to Section 4 for further details.

1. Why we do this report and what we look at

In this report, we share outcomes of our audit on the state's financial report and share our independent perspective on the state's financial outcomes and risks to fiscal sustainability.

We also share the audit outcomes of state-controlled material entities that make up significant components of the state's finances.

Our audit opinions provide confidence that the financial reports of the state and material entities are reliable to use and inform decision-making.

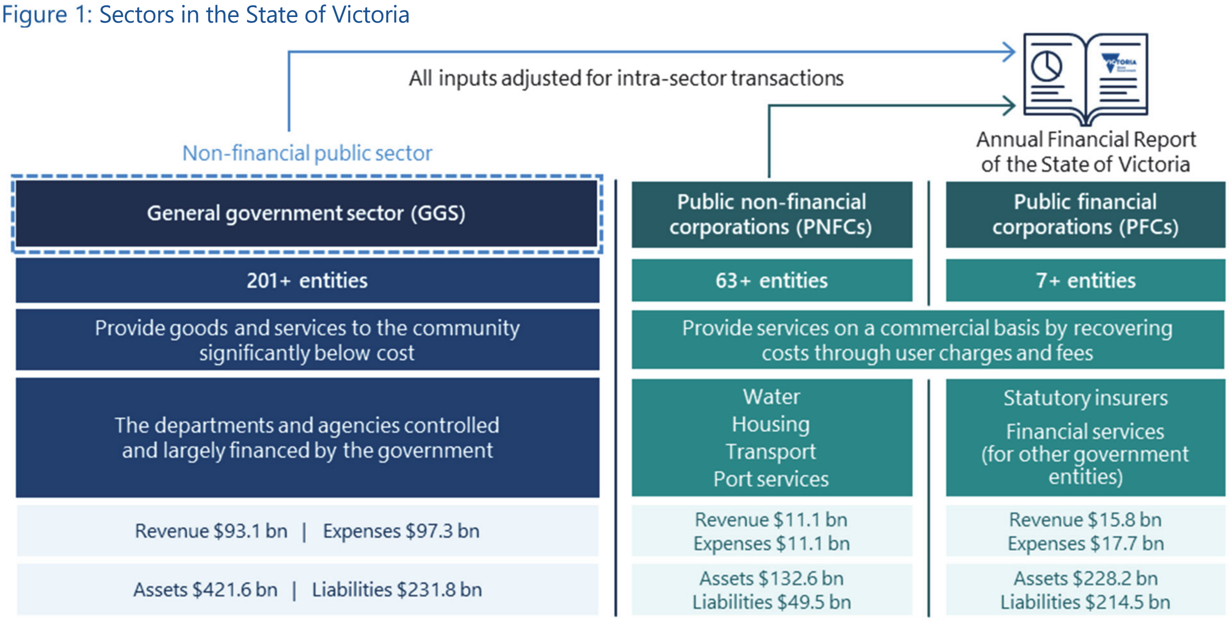
The AFR

DTF prepares the AFR. This is the state's consolidated financial report and is also known as the Financial Report (Incorporating Quarterly Financial Report No. 4).

The AFR shows the consolidated financial results for the State of Victoria for a given reporting period. Figure 1 outlines the 3 sectors within the state, which include over 271 state-controlled entities that contribute to the consolidated financial results.

We issue an audit opinion on the AFR. Our opinion provides assurance that the published financial outcomes of the state are reliable. This means Parliament and the Victorian community can confidently use the information in the AFR to better understand the state's financial outcomes and, when relevant, make informed decisions.

Figure 1: Sectors in the State of Victoria



Source: VAGO.

Entities excluded from the AFR

The AFR only includes state-controlled entities. Other public sector entities that we audit are excluded from the AFR because the state does not control them for financial reporting purposes.

The AFR excludes ...	Because ...
local government	it is a separate tier of government. Councils are elected by and accountable to their communities.
universities	they are mainly funded by the Australian Government. The state appoints a minority of university council members.
denominational hospitals	they are private providers of public health services and have their own governance arrangements.
state superannuation funds	their net assets are members' property. However, any net asset shortfalls related to certain defined benefit scheme entitlements are a state obligation and are reported as a liability in the AFR.
registered community health centres and aged-care providers	they have various funding streams, including from the Australian Government and owned-source revenue, with their own governance arrangements.

These entities prepare separate financial reports and have them audited.

Material entities in the AFR

Each year we audit and provide separate audit opinions on the financial reports of the state-controlled entities that are consolidated into the AFR.

In 2023–24, there were 30 material entities that accounted for most of the state's assets, liabilities, revenue and expenses. We therefore consider these entities to be significant components in the AFR.

We primarily focus on the financial transactions and balances of these material entities when forming our opinion on the AFR.

Reporting our insights on the state's finances

This report is the only report to Parliament that we must make under section 57(1) of the *Audit Act 1994*. The Act provides that we may comment on and make recommendations about the:

- effective and efficient management of public resources
- proper accounts and records.

We use this report to provide our independent perspective on the state's finances.

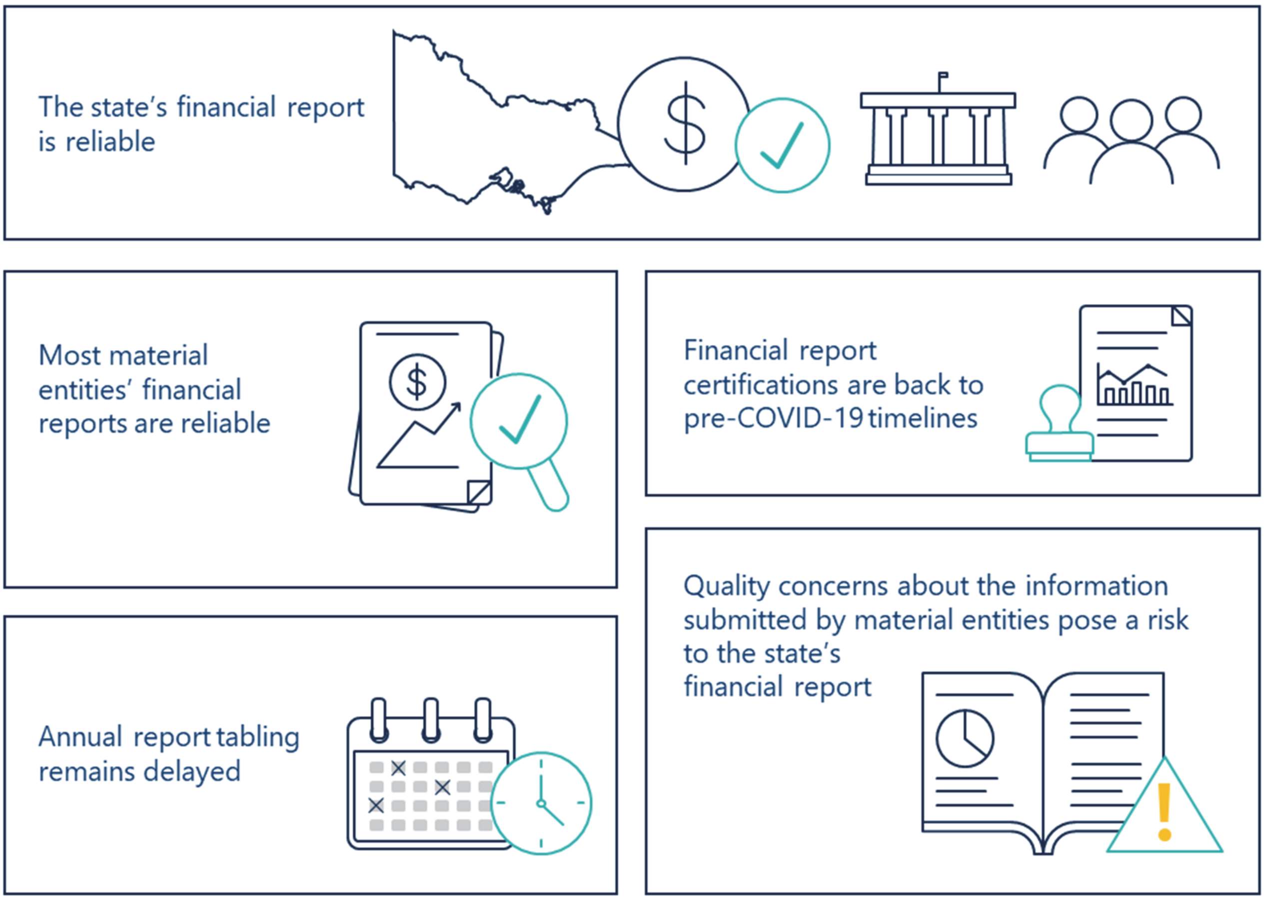
We also prepare a dashboard as a companion product to this report. It brings together current and historical financial information for the Victorian GGS reported in past state Budgets and AFRs. You can find this dashboard on our website.

Further information

See Appendix B for more information about our audit approach, independence and our costs.

2. Audit outcomes

Snapshot



Conclusion

We provided a clear audit opinion for the 2023–24 AFR.

Our clear opinion provides reasonable assurance that the financial performance and position of the State of Victoria, and within that the GGS, as reported in the 2023–24 AFR is reliable.

The separate financial reports of 28 of the 30 material entities are also reliable. We issued modified audit opinions on the DJCS's and VicTrack's financial reports. These matters were not material to the AFR.

The state's financial report is reliable

Audit opinion on the AFR

We provided a clear audit opinion on the 2023–24 AFR. Our clear opinion provides reasonable assurance that the financial performance and position of the State of Victoria, and within it the GGS, as reported in the AFR is free from material error.

Key audit matters

Auditors may include a description of key audit matters in the auditor's report, as described under the Australian Auditing Standards. We include such matters in the AFR and material entity audit reports where appropriate.

Key audit matters are those we identify as most significant to an audit and their inclusion in the audit report provides transparency and insight into the audit process.

We reported the following key audit matters for the AFR:

- recognition and measurement of transport assets
- recognition and measurement of service concession assets, liabilities and commitments
- valuation of defined benefit superannuation liability
- valuation of the provision for insurance claims.

A copy of our audit report is in Appendix C.

Most material entities' financial reports are reliable

Material entity audit outcomes

We issued clear opinions on 28 of the 30 material entities' financial reports at the time we issued our opinion on the AFR.

We issued modified opinions on 2 material entities – VicTrack and DJCS. We signed our audit opinion on DJCS after the AFR.

These modifications did not impact our opinion on the AFR because:

- for DJCS, the matter was not material to the state's financial report
- for VicTrack, DTF made a central adjustment on consolidation of the state's financial report to correct the issue.

Appendix D lists the material entities and summarises their financial results and our audit opinions.

Our qualified opinion for DJCS

DJCS is responsible for the road safety camera program, which includes the distracted driver and seatbelt offence detection system. The system detects drivers who are using portable devices while driving or who are not wearing their seatbelt correctly.

DJCS began issuing infringement notices relating to the distracted driver and seatbelt offence detection system on 1 July 2023. Income relating to those offences is recognised as fines income in its financial report.

DJCS outsources the operation of camera technology, information systems and processes used to detect, record and verify data for those offences. For the 2023–24 reporting period, DJCS did not ensure the outsourced provider maintained appropriate controls, accounts and records over these systems and processes.

As a result, we were unable to express an opinion on whether the fines income reported in DJCS's financial report is complete. Accordingly, we issued a qualified opinion.

See Section 4 for more information about how we came to this conclusion.

Our adverse opinion for VicTrack

We have continued to issue an adverse opinion on VicTrack's financial report. This means that its financial report does not accurately reflect its financial performance and position.

VicTrack has continued to account for assets it leases to DTP as operating leases. VicTrack asserts that it substantially holds all the risks and rewards incidental to ownership of the operational transport assets.

We disagree. VicTrack's incorrect accounting is material and pervasive to its financial report.

Our view is that DTP is responsible for the operation of the transport network as a whole and that in this regard DTP:

- directs the use of transport assets by setting the timetables and operating conditions for all modes of transport with no significant input from VicTrack
- substantially holds the risks and rewards of ownership of the operational transport assets.

This is why we formed the view that it is a finance lease. VicTrack continues to incorrectly recognise these leased assets and associated transactions that should be accounted for by DTP.

In the AFR, DTF made a central adjustment on consolidation to correct this inconsistent accounting treatment. This means the fair value of the underlying assets and associated transactions were correctly reinstated at the State-of-Victoria level.

Appendix E further explains the accounting for the lease arrangements of operational transport assets.

Adverse opinion

We make an adverse opinion when an entity's financial reports are misrepresented, misstated or do not accurately reflect the entity's financial health.

Financial report certifications are back to pre-COVID-19 timelines

Legislated timelines

DTF and the state-controlled entities must complete financial reporting tasks by the dates set in the *Financial Management Act 1994*. Entities are required to provide financial reports to us within 8 weeks of the balance date (30 June), which is 25 August.

The *Audit Act 1994* requires us to provide the entity with an audit opinion within 4 weeks of receiving its financial report. That means we should provide audit opinions by 22 September.

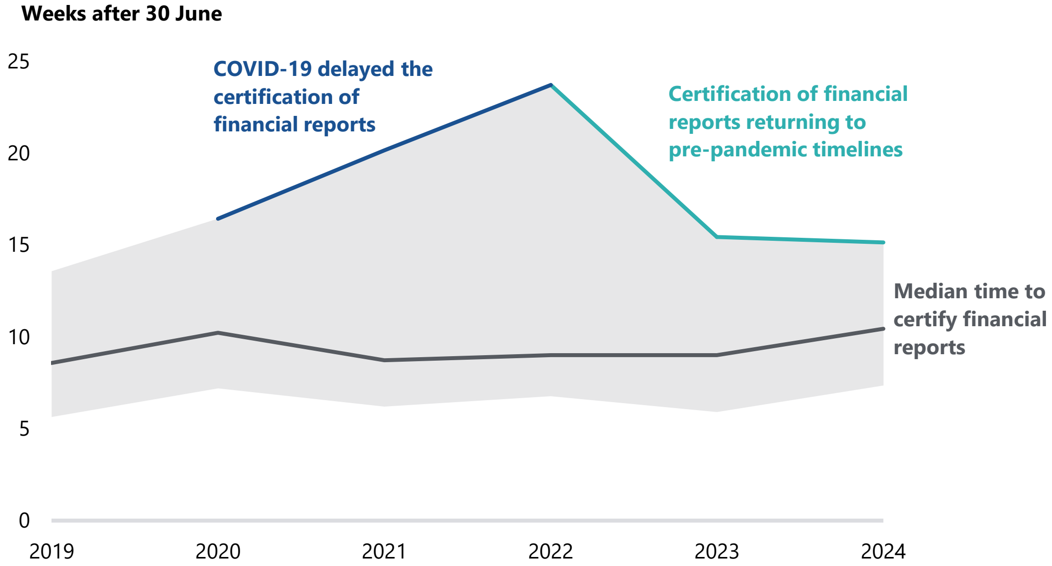
To meet their legislative timelines, DTF and VAGO rely on entities providing complete and accurate financial information on time. Delays impact the timeliness of our audit opinions as well as the preparation and tabling of the material entities' financial reports and the AFR in Parliament.

Timely financial reports for material entities

There was a significant improvement in the timing of financial reports this year.

As shown in Figure 2, the median time for material entities to certify financial reports has remained stable at around 9 weeks after 30 June. The pandemic caused significant delays, with the last material entity certifying its financial report 24 weeks after the balance date in 2021–22. This has largely returned to pre-pandemic timelines over the last 2 years.

Figure 2: Timeliness of financial report certifications from 2019 to 2024



Source: VAGO.

This year, one material entity certified its financial report and a further 25 provided draft financial reports by the due date of 25 August. We were then able to provide:

- 20 of the 30 material entities with an audit opinion by the due date of 22 September
- a further 9 material entities with an audit opinion before we gave the Treasurer our audit opinion on the AFR.

Annual report tabling remains delayed

Annual reports are important accountability documents

Annual reports of public sector entities promote transparency and accountability. These reports provide an overview of an entity's activities, financial performance and use of public resources, including the audited financial report. They also ensure accountability by detailing how funds have been spent and outcomes achieved.

As required by the *Financial Management Act 1994*, state-controlled entities have until 31 October to table their annual reports. They must also table their annual reports when Parliament is sitting. If they do not meet this date, responsible ministers must:

- report this to Parliament, along with the reasons for the delay
- ensure the annual reports are tabled as soon as possible after they are received.

We have an obligation under the Australian Auditing Standards to consider whether financial information in annual reports is consistent with the audited financial report. If we identify an inconsistency, it may indicate a material misstatement in either the financial report or financial information of the annual report. This consistency check is done before we release our audit opinion if the annual report is available by the agency.

Delayed tabling of annual reports

By 31 October 2024, we had issued audit reports on 235 state-controlled entity financial reports. This includes audit reports of both parent and subsidiary entity financial reports. Of these:

- 124 state-controlled entity annual reports were tabled by 31 October 2024.
- 111 state-controlled entity annual reports were not tabled by 31 October 2024.

On 30 October 2024, the Assistant Treasurer, on behalf of the responsible ministers, informed Parliament that the annual reports of 131 public bodies would be delayed because the ministers had not received them in time. There was no explanation for these delays, as required by the *Financial Management Act 1994*.

Quality concerns with financial information submitted by material entities pose a risk to the state's financial report

Quality of information requires improvement

DTF relies on state-controlled entities providing it with timely, complete and accurate financial information so it can prepare and publish the AFR.

DTF requested …	To provide their trial balance by …	And supplementary information for disclosures by …
GGS entities	24 July 2024	7 August 2024.
public financial corporation (PFC) and public non-financial corporation (PNFC) entities	1 August 2024	

Each entity's chief financial officer (CFO) must certify that the information provided to DTF is complete and accurate.

In our *Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2022–23,* we recommended that material entities develop and implement robust quality assurance processes on financial information provided to DTF.

This year, we continued to identify challenges with the quality of information provided. More specifically, we noted:

- delays in the provision of information
- significant errors in the information, including incorrect classification of liabilities, cashflows from investing activities and overstatements in service concession arrangement commitments
- changes to key finance staff and responsibilities, leading to a loss of knowledge on the submission processes and obligations required by DTF.

Delays and poor-quality financial information submitted puts pressure on DTF's quality assurance processes, increasing the risk of undetected material errors. This may lead to inaccurate financial reporting, which can negatively impact decision-making by the government, Parliament and the Victorian community.

Recommendations

Relevant material entities

Extending from our recommendation last year, we recommend relevant material entity CFOs:

- develop and implement robust quality assurance processes over the financial information provided to DTF
- ensure:
    - internal processes are documented well enough to enable a new starter to understand what submission processes and obligations are required by DTF, how these processes are to be done and by when

	• adequate training and knowledge transfer occurs for all key finance staff to support the process.
Department of Treasury and Finance	In our 2022–23 report, we recommended DTF investigates key drivers for the quality issues with financial information submitted and consider whether any further training or guidance may be required to support material entities and reduce the risk of inaccurate financial reporting.

3.

Financial outcomes for the GGS and risks to fiscal sustainability

Snapshot

Long-term focus to fiscal management is required, prioritising management of existing and emerging financial risks

The Victorian GGS reported another net operating loss of **$4.2 billion** this year, bringing total losses over the last 5 years to **$48 billion**

The GGS achieved a **$2.6 billion** operating cash surplus with higher tax revenue, dividends and more Australian Government grants

Prolonged fiscal cash deficit is a challenge to ongoing financial sustainability, and is set to continue

The GGS's gross debt grew by **$24.9 billion** to **$168.8 billion**, faster than revenue and economic growth

Conclusion

The GGS achieved an operating cash surplus this year, but it incurred another accrual operating loss, bringing accumulated losses over the last 5 years to $48 billion. It also reported a fiscal cash deficit as it has for the last 8 years.

Ongoing operating losses and fiscal cash deficits are indicators of structural issues with underlying revenue and expenditure policy settings that create risks to financial sustainability.

The government has announced further planned savings of $4.9 billion over the next 4 years to manage costs. Achieving these savings and maintaining current service levels will be a challenge given the current financial pressures and several emerging financial risks.

The GGS's gross debt rose again this year at a pace faster than revenue and economic growth. The government's present strategy is to manage debt levels relative to the state's economy. In this regard, the government has committed to start reducing net debt to GSP in 2027–28.

Sound financial management underpins fiscal sustainability. A clear and well defined longer-term financial plan is an important part of this. Developing this longer-term plan will provide a clear framework against which government decision-making can be anchored.

Long-term focus to fiscal management is required, prioritising management of existing and emerging financial risks

Fiscal sustainability

What is fiscal sustainability?

To remain fiscally sustainable, the state must meet current and future expenditure requirements from revenue earned, absorb foreseeable changes and materialising risks and manage the impact from these factors to changing revenue and expenditure requirements.

Fiscal sustainability

Fiscal sustainability is the ability of the government to maintain public finances at a credible and serviceable position now and into the future. Ensuring long-term fiscal sustainability requires governments to engage in ongoing monitoring and strategic forecasting of future revenue and expenditure, environmental factors and socioeconomic trends to remain financially resilient.

Fiscal strategy

Fiscal strategy outlines the government's fiscal strategies and objectives

The state Budget sets out the Victorian Government’s long-term financial management objectives for the GGS along with short-term objectives and key financial measures and targets for achieving the government's fiscal strategy.

The state’s long-term financial management objectives, as outlined in the 2024–25 state Budget, are:

- sound financial management

- improved services
- building infrastructure
- efficient use of public resources
- a resilient economy.

The government acknowledges that sound fiscal management requires a realignment of revenue and expenditure, coupled with a strategy to fund the government's infrastructure program.

Accordingly, the government developed a 4-step fiscal strategy aligned with its key financial measures and sustainability objectives in the 2020–21 state Budget. This strategy involved 4 steps:

- step 1: creating jobs, reducing unemployment and restoring economic growth
- step 2: returning to an operating cash surplus
- step 3: returning to operating surpluses
- step 4: stabilising debt levels.

In the 2024–25 state Budget, the government added a fifth step to this fiscal strategy – reducing net debt as a proportion of GSP by the end of its forward estimate period.

Fiscal strategy

A fiscal strategy is a clear statement of the government's fiscal objectives and targets over a defined period. It sets out the government's short term and long-term fiscal strategies and objectives for managing its finances and existing and emerging risks. It also demonstrates how planned government policies will contribute to fiscal sustainability and macro-economic stability.

Short-term financial sustainability objectives

State's finances were impacted by the COVID-19 pandemic, rising debt and structural issues

The government has also developed short-term financial sustainability objectives given the fiscal position has been impacted by past underlying structural issues, the COVID-19 pandemic and borrowings to support its large infrastructure program.

Figure 3 shows these objectives as set out in the last 4 Budgets.

Figure 3: GGS short-term financial sustainability objectives

Budget year	Operating cash surplus	Net operating balance	Net debt to GSP
2024–25	Operating cash surplus will be achieved by 2022–23 and maintained over the Budget and forward estimates period.	Net operating balance will return to a surplus by 2025–26.	Net debt to GSP will stabilise and begin to decline by the end of the forward estimates period.
2023–24	Operating cash surplus will be achieved by 2022–23 and maintained over the Budget and forward estimates period.	Net operating balance will return to a surplus by 2025–26.	–
2022–23	Operating cash surplus will be achieved by 2022–23.	Net operating balance will return to a surplus by the end of the forward estimates period.	–
2021–22	Operating cash surplus will be achieved before the end of the forward estimates period.	–	–

Source: VAGO, based on the AFR and state Budget.

Financial measures and targets

Financial measures and targets are less defined and may undermine discipline in use of public resources

To support these objectives, the state has set key financial measures and targets. Figure 4 outlines the government's key financial measures and targets for the GGS set out in respective state Budgets along with the actual outcomes reported for the last 2 years.

The measures and targets are qualitative, except for one: fully funding the unfunded superannuation liability by 2035.

Figure 4: GGS key financial measures, targets and results

Financial measure	Target	2022–23 actual	2023–24 Budget	2023–24 actual
Operating cash surplus/deficit[(a)]	A net operating cash surplus consistent with maintaining GGS net debt at a sustainable level	$4.3 billion net operating cash surplus	$0.8 billion net operating cash surplus	$2.6 billion net operating cash surplus
Net debt to GSP[(b)]	GGS net debt as a percentage of GSP to stabilise in the medium term	20.3%	22.6%	21.9%
Interest expense to revenue	GGS interest expense as a percentage of revenue to stabilise in the medium term	4.7%	6.2%	6.1%
Superannuation liabilities (contribution to the State Superannuation Fund)	Fully fund the unfunded superannuation liability by 2035	$0.6 billion	$0.3 billion	$0.1 billion

Note: [(a)]These are the net cashflows from operating activities as disclosed in the consolidated cashflow statement.
[(b)]Net debt is gross debt less liquid financial assets. It is the sum of deposits held, advances received, government securities, loans and other borrowings less the sum of cash and deposits, advances paid, investments, loans and placements.
Source: VAGO, based on data from the state Budget, the AFR and a publicly announced policy costing.

Financial measures and targets have been progressively revised over the last 12 years from quantifiable targets to ones that are less defined, which can be seen in Appendix F. With the exception of fully funding the superannuation liability, these measures lack specific targets and clear timelines for achieving them.

The measures and targets were amended in 2020–21 to reflect the uncertain economic and fiscal environment and the government's focus on economic recovery after the pandemic. For example, the 'operating surplus' target was removed and the 'operating cash surplus' and 'interest expense to revenue' targets were introduced. These new targets had no specific measures other than to achieve the outcome.

COVID debt repayment plan

In the 2023–24 state Budget, the government also introduced a temporary plan to reduce the cost of servicing the debt from its response to the COVID-19 pandemic of $31.5 billion. This plan is for a 10-year period to 2033 and has 3 parts:

- introduction of a temporary COVID debt levy on land and payroll tax
- rebalancing the public service through further savings and efficiency initiatives across the government, including reductions in corporate and back-office functions, labour hire and consultancy expenses. An estimated saving of $2.1 billion was included in the 2023–24 Budget for a 4-year period ending 30 June 2027
- establishing the Victorian Future Fund (VFF), where the $7.9 billion proceeds received in 2022–23 from outsourcing licensing, registration and custom plate services through the VicRoads modernisation joint venture arrangement will be invested.

The government took on COVID-19-related debt when interest rates were historically low. Given the current low cost of servicing this debt and its long repayment timeline, the government does not plan to pay it off immediately. Instead, funds from the COVID debt levies and savings and efficiency initiatives mean the government expects to borrow less than planned for the state's infrastructure program.

The VFF has been established as an offset account, where investments and their returns will be used to offset pandemic borrowings, lowering the cost of servicing debt.

The government has not publicly reported how it progressed with this plan during 2023–24, including realisation of benefits from saving and efficiency initiatives.

Our observations

Long-term fiscal focus needed

While strategies and objectives are in place, the state has not articulated a clear plan for long-term fiscal management. Current strategies are short term, reactive and do not address both the existing financial challenges and emerging financial risks that we comment on further in this section. A more comprehensive approach is needed to ensure long-term fiscal sustainability and proactive management of the state's finances.

Developing a well-defined, long-term plan will provide a clear framework for which government decision-making can be anchored to ensure the allocation of public resources are prioritised not only based on policy intent but align with the financial and economic strategies and constraints to maintain financial health. It will also enable ongoing monitoring and assessment, helping the government uncover risks to financial health and adapt accordingly.

The government can also use the plan to transparently report its progress, remaining accountable to managing fiscal sustainability of the state.

3.1 Financial outcomes for the GGS

Our analysis focuses on the GGS because movements between years in the GGS's results explain most of the movements in the state's consolidated results, with some notable exceptions.

The GGS reported another net operating loss of $4.2 billion this year, bringing accumulated losses over the last 5 years to $48 billion

What is the operating result and why is it important?

The net operating result is a key measure of the GGS's financial performance and fiscal sustainability. A positive operating result reflects the state’s capacity to earn revenue and effectively manage expenses, resulting in a surplus that can be used for future needs.

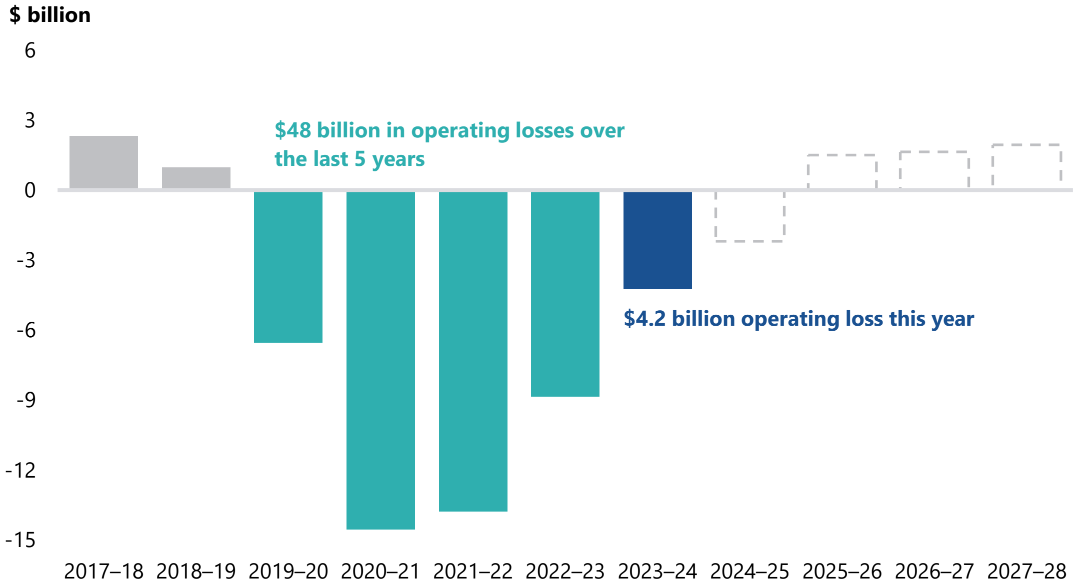
The GGS reported another net operating loss this year of $4.2 billion, as shown in Figure 5. This is an improvement of $4.6 billion compared with last year, however, more than the $4.0 billion estimated in the 2023–24 state Budget.

This result brings the state's total accumulated losses over the last 5 years to $48 billion. The government attributes approximately:

- $31.5 billion of these cumulative operating losses to its COVID-19 response from 2019–20 to 2022–23
- $16.5 billion of these cumulative operating losses to providing ongoing public services.

These operating losses deplete cash reserves, increase debt, and diminish the state's financial resilience and ability to respond to future shocks.

Figure 5: GGS net operating result



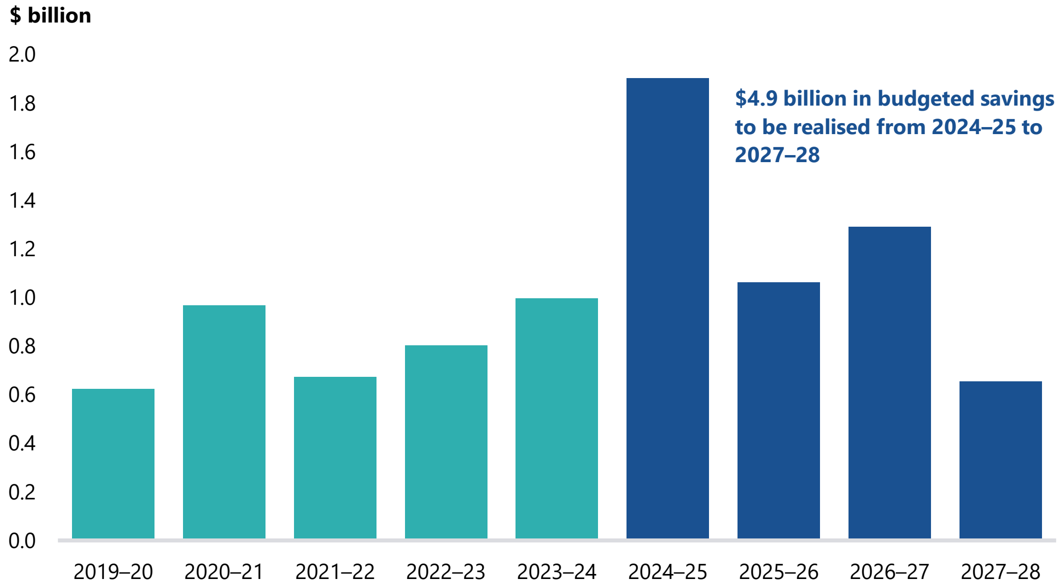
Source: VAGO, based on the AFR and state Budget.

The GGS is forecast to incur a further net operating loss of $2.2 billion in 2024–25 before expecting to return to a net operating surplus from 2025–26. This will bring the cumulative operating losses over 6 years to 2024–25 to $50.1 billion.

Of the $50.1 billion, $18.6 billion of losses are attributable to providing ongoing public services. The operating surpluses forecast from 2025–26 to 2027–28 in the 2024–25 state Budget only allow for recovery of $5.1 billion of the accumulated losses by 2027–28. The government will need to make significant surpluses beyond current budgetary forecasts to restore the financial resilience eroded by these losses.

The government has announced various saving initiatives and efficiency dividends to manage these weaker financial outcomes in the state Budget. Figure 6 shows the value of cumulative savings announced from 2019–20 to 2027–28 of $9.0 billion, with $4.9 billion to be realised from 2024–25 to 2027–28.

Figure 6: Cumulative saving initiatives announced in the state Budget



Source: VAGO, based on the state Budget.

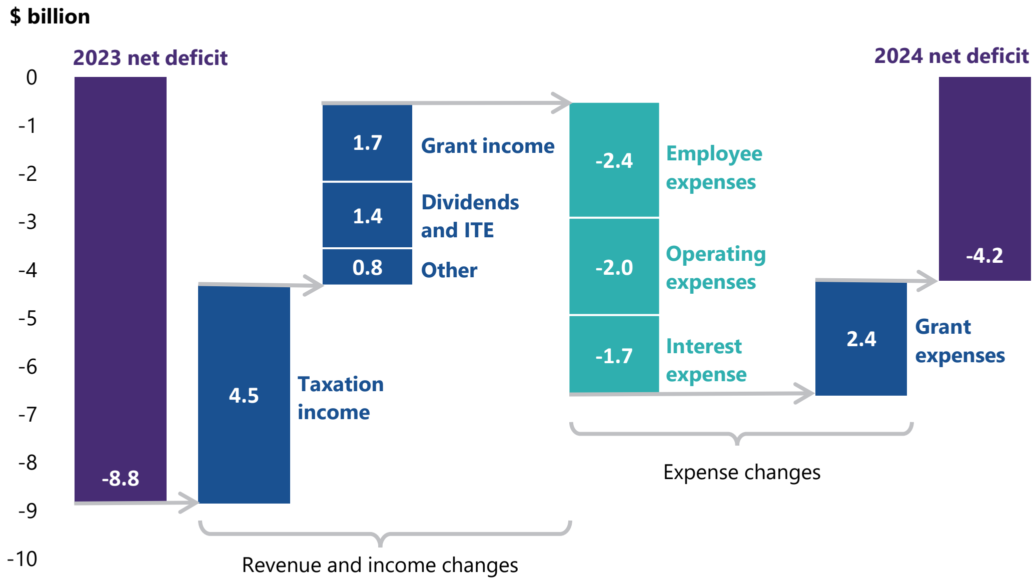
Achieving these savings and maintaining current service levels will be difficult given the financial pressures faced, including the current financial outcomes, growing employee costs, interest expenses from servicing debt, inflation and demand for services due to the growing population.

These risks are discussed further in our emerging risks section. The government must manage these emerging risks closely if it is to achieve the forecast operating surplus in 2025–26.

How the operating deficit was achieved

Figure 7 shows the key contributors of this year's improvement in operating results compared with last year.

Figure 7: Changes in the GGS net operating result from 2023 to 2024



Note: Numbers have been rounded. ITE stands for income tax equivalents.
Source: VAGO, based on the AFR and state Budget.

This improved result is driven by operating revenue growing more than operating expenses.

Operating revenue rose by $8.4 billion, or 9.9 per cent, increasing from $84.7 billion in 2023 to $93.1 billion in 2024, mainly driven by higher:

- taxation income of $4.5 billion due to the COVID debt levy applied on payroll and land holdings and stronger economic conditions in property and labour markets
- grants received from the Australian Government of $1.7 billion mainly due to growth in the national GST pool, supported by elevated inflation and a resilient labour market
- dividends and income tax equivalents (ITE) of $1.4 billion, largely due a $1.1 billion dividend payment from the TAC due to its improved profitability in recent years from lower claims.

Operating expenses increased by $3.7 billion, or 4.0 per cent, from $93.6 billion in 2023 to $97.3 billion in 2024, mainly driven by:

- employee expenses of $2.4 billion from higher full-time employee (FTE) and wage growth
- interest expense of $1.7 billion due to new borrowings or refinanced borrowings at higher interest rates
- other operating expenses of $2.0 billion, including a $380 million payment for the withdrawal from the 2026 Commonwealth Games and $248 million for higher concession payments mainly relating to energy bill relief payments – additionally, a general increase in expenses due to inflationary pressures and government activity

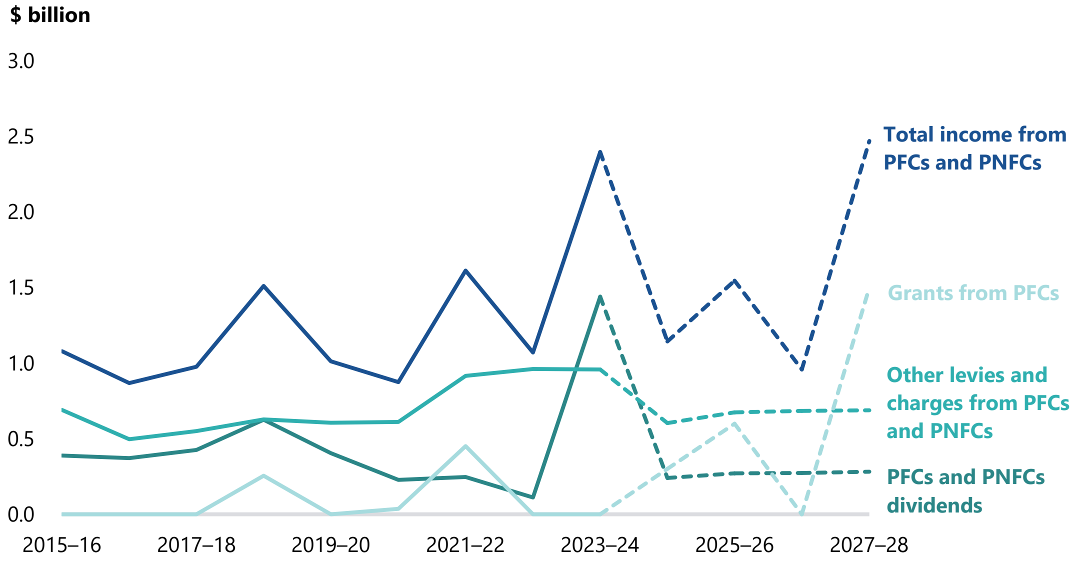
- an offset of $2.4 billion reduction of grant expenses for on-passing local government grants and private sector and not-for-profit grants.

Funding from the Australian Government, increases in taxation income and income sourced from public corporations have continued to make a substantial contribution to the GGS's operating result.

Income sourced from public corporations comprise dividends, statutory fees and charges, financial accommodation levy, environmental contribution levy, grants and ITE receipts. The receipts of $2.4 billion have contributed to a reduction in the GGS's operating deficit and achieving positive operating cashflows in 2023–24.

Figure 8 shows income and revenue sourced from public corporations over the last 10 years together with the forecast from 2024–25 to 2027–28.

Figure 8: Income and revenue sourced from PFCs and PNFCs



Source: VAGO, based on the AFR and state Budget.

Income and revenue sourced from public corporations have fluctuated over the years. However, they saw a substantial increase this year, rising to $2.4 billion from $1.1 billion in 2022–23. This increase was primarily driven by one-off dividends of $1.1 billion from the TAC.

Public corporations

Public corporations are state-owned entities or statutory authorities established under legislation. They include:

- PNFCs that provide a wide range of goods and services while meeting commercial principles through cost recovery via user fees and charges
- PFCs that deal with financial aspects of the state. They have the power to borrow, accept deposits and acquire financial assets.

The GGS achieved a $2.6 billion operating cash surplus through higher tax income, dividends and more Australian Government funding

What is the operating cash result and why is it important?

The operating cash surplus is the extra money left over for the government in a financial year after paying for its operations and running expenses, such as employee salaries, supplier expenses, interest costs and utilities.

The state achieved an operating cash surplus of $2.6 billion this year. This is $1.8 billion higher than the forecast in the 2023–24 Budget of $0.8 billion. However, it is $1.6 billion less than last year's operating cash surplus of $4.2 billion.

Last year's operating cash surplus included $7.9 billion of proceeds received from VicRoads modernisation joint venture arrangement.

Achieving the operating cash surplus this year was possible because of:

- the increase in taxation income of $4.5 billion explained previously
- the one-off dividend payment of $1.1 billion from the TAC
- local government financial assistance grants of $0.7 billion received from the Australian Government before the year end and paid out to councils post year end.

Prolonged fiscal cash deficit is a challenge to ongoing fiscal sustainability and is set to continue

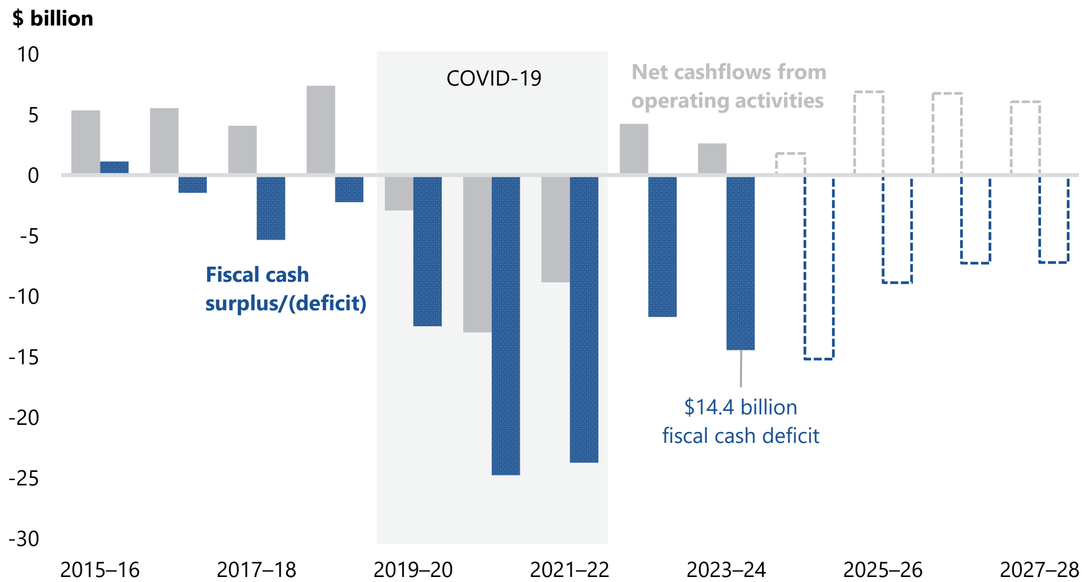
Fiscal net cash deficit outcome for a further year

A key indicator of financial sustainability is the fiscal cash surplus/deficit outcome. A fiscal cash surplus means the state's cash inflows from operations exceed its recurrent and capital outlays.

A fiscal cash surplus is a sign of good financial health because it means there is available cash for the state to invest in public services, pay down debt or build financial resilience for future uncertainties. A fiscal cash deficit means the state has to borrow to cover its net investments in non-financial assets used to provide public services.

Figure 9 shows the fiscal cash surplus/deficit of the GGS since 2015–16, in addition to the projected outcome for the Budget and forecast years from 2024–25 to 2027–28.

Figure 9: Fiscal cash surplus/deficit



Source: VAGO, based on the AFR and state Budget.

The GGS made a fiscal cash deficit of $14.4 billion in 2023–24. It has not made a fiscal cash surplus for last 8 years, with this trend expected to continue over the next 4 years. This prolonged period of fiscal cash deficits demonstrates why the state has relied so heavily on borrowings to fund capital needs, which is a challenge to its financial sustainability.

Fiscal cash surplus/deficit

The cash surplus/deficit is calculated by:

- net cashflows received from operating activities, which are the sum of cash received from sources, such as taxes and government grants, offset by cash spent on operating expenses, such as employee costs
- plus net cashflows from investment in non-financial assets, being the sum of cash earned from investment activities, such as the sale of land and buildings, offset by cash spent on capital projects
- less dividends received from public corporations.

GGS gross debt rose by $24.9 billion to $168.8 billion, faster than revenue and economic growth

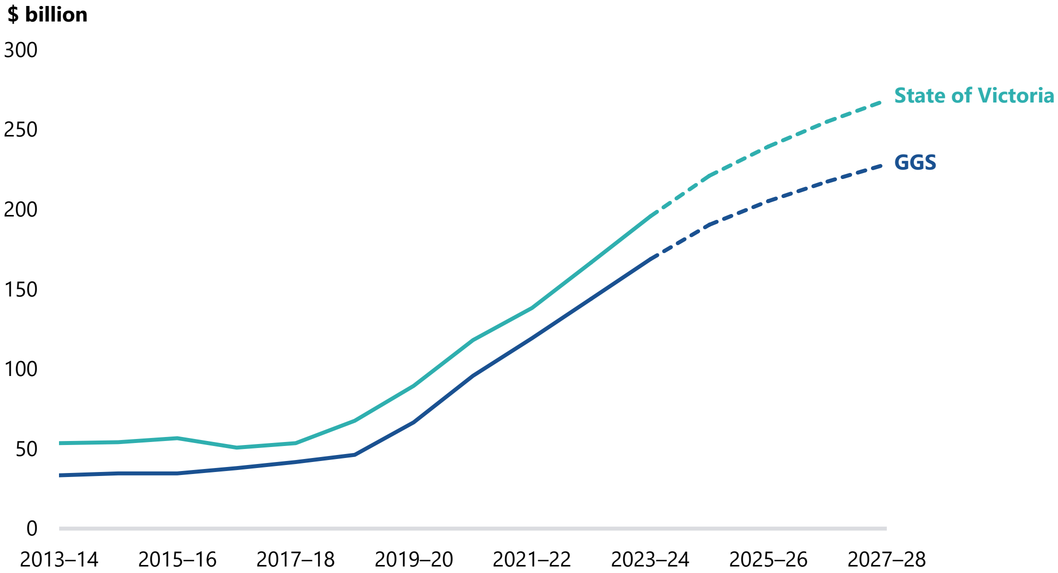
Victoria's debt is at a record high and projected to grow further

Victorian state debt is historically high and expected to grow as the government continues to borrow to fund its significant planned infrastructure program.

In Victoria, there is a total of $208 billion in new and existing capital projects underway. The state Budget committed to investing $132 billion in capital projects from the 2024–25 financial year and beyond. The majority of this investment is expected to be debt funded.

Figure 10 shows the growth of Victoria's gross debt since 2013–14 and forecast growth over the forward estimates to 2027–28.

Figure 10: Growth of Victoria's gross debt



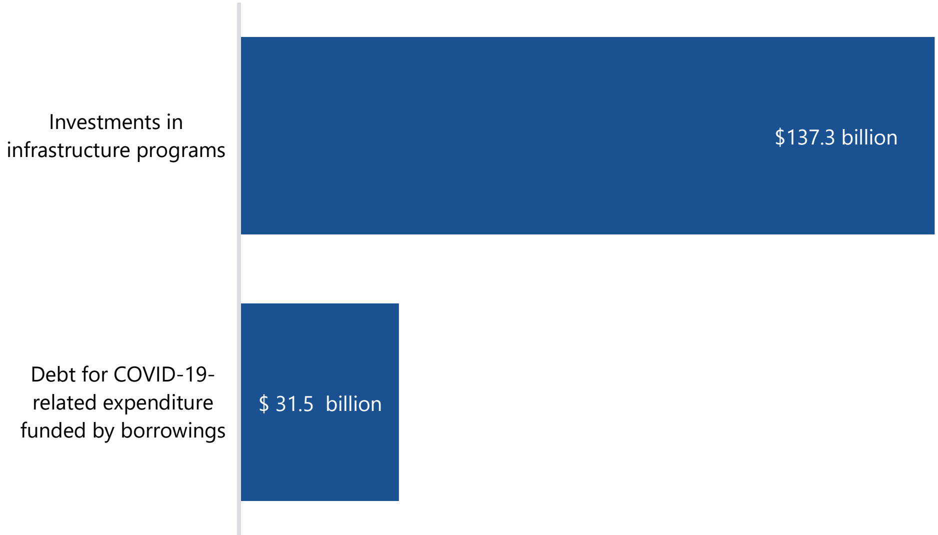
Source: VAGO, based on the AFR and state Budget.

The GGS's gross debt rose from $33.4 billion at 30 June 2014 to $168.8 billion at 30 June 2024. In particular, rapid growth of 154 per cent was experienced since 2019–20, when debt was $66.5 billion.

GGS gross debt is projected to grow to $228.2 billion by 30 June 2028. The state's gross debt follows a similar growth pattern. It was $195.7 billion as at 30 June 2024 and is expected to grow to $268.4 billion by 30 June 2028.

The growth in debt was in part used to fund the state's operating deficit in response to the COVID-19 pandemic, and in part to fund planned infrastructure programs and unplanned cost overruns of existing infrastructure projects, with this breakdown in Figure 11.

Figure 11: GGS gross debt profile by its purpose and use



Source: VAGO, based on the AFR and state Budget.

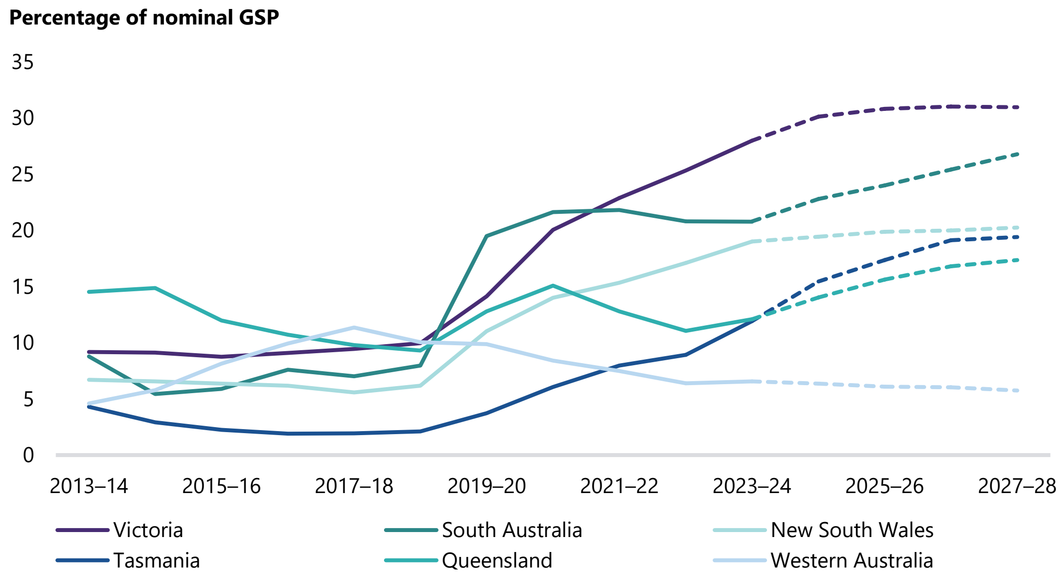
The state took on $31.5 billion debt in responding to the pandemic, more than 18.7 per cent of the government's current outstanding debt.

Using debt to fund investment in intergenerational infrastructure is common. It enables the government to allocate resources and invest in long-term projects that the taxpayers might not otherwise afford today. However, a higher and unsustainable level of public debt can pose a significant risk to future prosperity and economic stability. If not managed in a fiscally sustainable and responsible manner, debt imposes a direct cost on taxpayers both now and in the future.

Victoria's debt has been growing faster than other states

Figure 12 shows GGS total gross debt of all Australian states as a percentage of nominal GSP for each state. This is a common measure used across jurisdictions to understand their relative indebtedness. Victoria's debt to GSP ratio was comparable to other states prior to the pandemic. Since then, it has diverged significantly. This trend is forecast to continue to 2027–28.

Figure 12: Gross debt of Australian GGS by state



Source: VAGO, based on each state Budget.

3.2 GGS emerging risks

Achieving fiscal sustainability requires close attention and management of several emerging risks

Risks to fiscal sustainability currently remain elevated

Achieving the current fiscal strategy is critical for the financial sustainability of the state.

The government aims to maintain the operating cash surplus achieved last year over the forward estimates to achieve a net operating surplus by 2025–26 and to stabilise and reduce debt as a proportion of GSP by 2027–28.

There are several emerging risks that require close attention and management if the government is to achieve its fiscal strategy and ensure fiscal sustainability over the medium and long term.

They include:

- growing indebtedness of the state
- rising interest costs of new and refinanced debt
- rising employee costs taking up a large portion of the GGS's revenue and income
- managing operating expenses growth amid rising service demand and high inflation
- limitations to new revenue and income streams
- unplanned and significant cost escalations of major infrastructure projects.

These risks are discussed below.

Growing indebtedness of the state

Managing debt at a sustainable level is an important requirement for fiscal sustainability

Managing debt at a sustainable level ensures that the government can access debt markets while keeping the cost of debt low, is able to respond to future crises and can ensure intergenerational equity.

Several measures of fiscal sustainability indicate that Victoria's debt burden has increased and the state's ability to service these debts has decreased.

The state Budget and fiscal strategy contain several measures aimed at achieving fiscal sustainability. The government assesses the sustainability of the debt by applying the following financial measures:

- net debt to GSP
- interest expense to revenue.

We also consider the following to be appropriate measures:

- gross debt to GSP
- gross debt to revenue (indebtedness) – gross debt as a proportion of operating revenue
- interest expense relative to the portfolio of debt – considering new and refinanced (rolled over) debt and the maturity profile.

The impact of rising debt and interest expense on these debt sustainability measures are discussed further below.

Intergenerational equity

Intergenerational equity means fairly sharing economic costs and benefits of the government's fiscal policy decisions, such as taxation, public spending and borrowing across different generations.

Gross debt as a proportion of GSP continues to increase

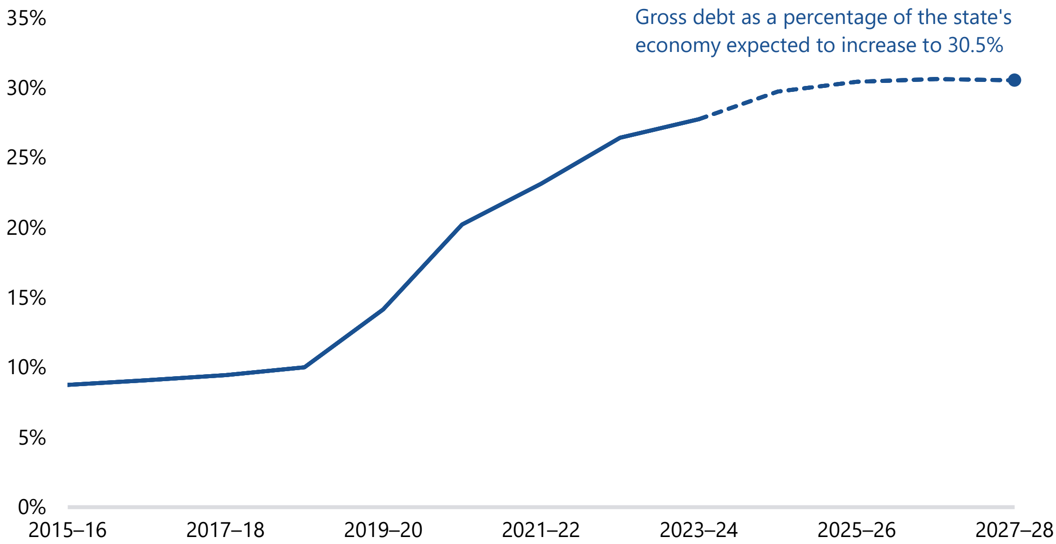
Gross debt to GSP is a key financial measure of the GGS and an indicator of the size of the state's debt in relation to the size of the economy.

The higher this ratio, the more difficult it is for the state to pay back its debt.

An increasing ratio means that state debt is growing faster than the economy. This scenario puts additional pressure on debt service costs and consequently the net operating result, which makes it harder to repay debt.

Figure 13 shows that gross debt as a percentage of GSP has rapidly grown. The 2024–25 state Budget forecasts that debt will stabilise as a proportion of GSP by 2027–28.

Figure 13: GGS gross debt as a percentage of GSP



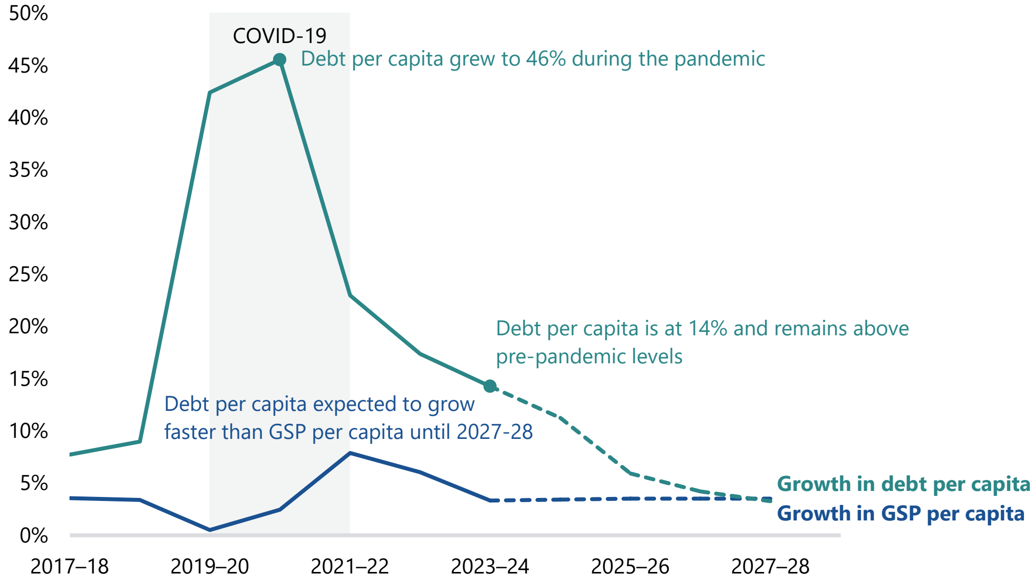
Source: VAGO, based on the AFR and state Budget.

Average growth of GGS gross debt from 2015–16 to 2018–19 was 7.6 per cent per year. GGS gross debt grew by an average rate of 33.3 per cent per year from 2019–20 to 2022–23 due to significant investment in infrastructure programs and pandemic-related expenses.

Gross debt is forecast to increase from 27.7 per cent in 2023–24 to 30.5 per cent of GSP in 2027–28, growing at an average rate of 7.9 per cent per year during that period, well above the growth in GSP and GGS revenue.

Figure 14 shows that while the growth rate of per capita debt growth is projected to slow, it will still outpace revenue growth through to 2027–28 thereby increasing the debt burden on Victorians.

Figure 14: Annual growth in per capita GSP and per capita gross debt of the GGS



Source: VAGO, based on the AFR and state Budget.

Steps 4 and 5 of the government's fiscal strategy aim to stabilise and reduce net debt as a proportion of GSP by 2027–28. The government has committed to reduce net debt to GSP from 25.2 to 25.1 per cent by 2027–28. However, the government has not established a long-term specific target for net debt to GSP ratio or ceiling on the quantum of debt it plans to take on.

Achieving consistent and higher nominal economic growth is key to achieving steps 4 and 5 of the fiscal strategy. However, it may not address the sustainability risks associated with growing debt.

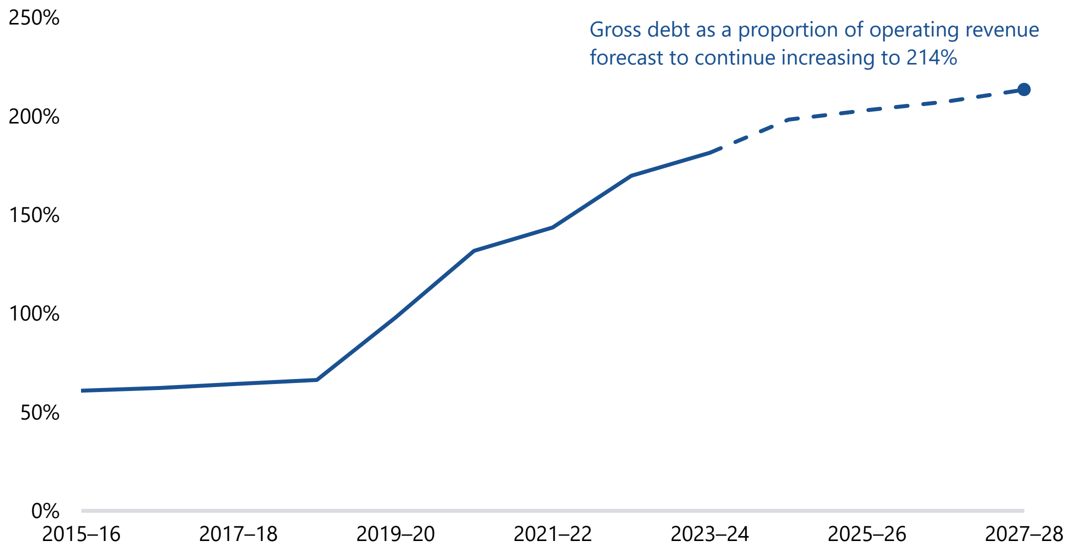
Gross debt as a proportion of revenue is projected to rise over 200 per cent in 2024–25

While governments commonly use net debt as a proportion of GSP as a measure, gross debt to public sector operating revenue is also a useful measure of fiscal sustainability. This can be particularly informative:

- if the growth in state revenue uncouples from economic growth
- in a higher interest rate environment, especially where the interest rate is higher than annual GSP growth and the government's revenue growth.

Figure 15 shows that gross debt as a proportion of operating revenue is continuing to increase.

Figure 15: GGS gross debt as a proportion of operating revenue



Source: VAGO, based on the AFR and state Budget.

In this scenario, debt servicing and allocating money to essential services can be problematic because interest repayments take a greater bite from operating revenue.

Rising interest costs for new and refinanced debt

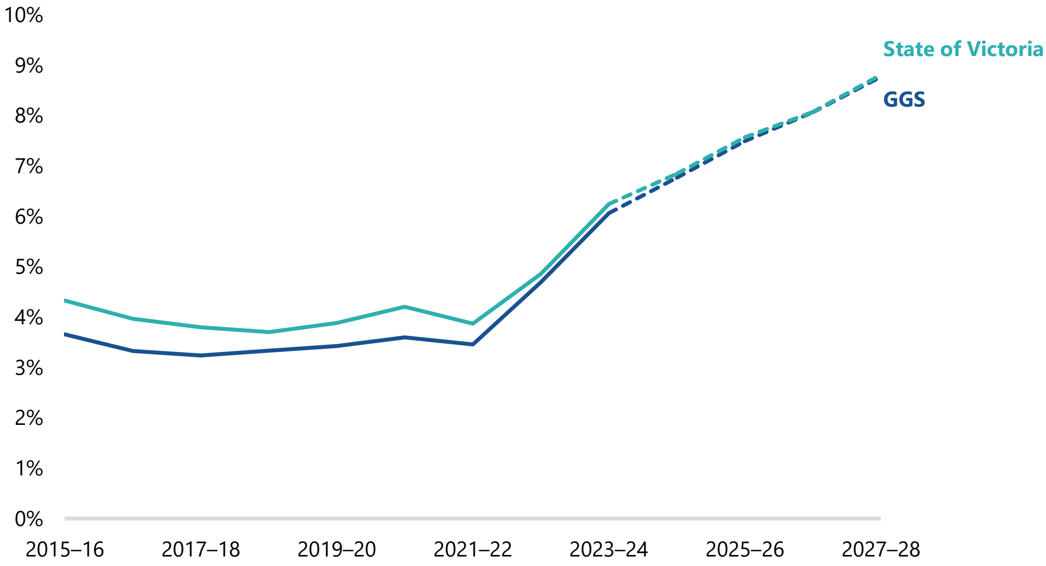
Interest expense is rising faster than revenue – interest bite

Stabilising GGS interest expense as a percentage of revenue in the medium term is one of the government's financial measures and targets. As the state's debt increases, and interest rates remain elevated, so does the interest expense incurred to service the debt.

Comparing interest expense to operating revenue provides information on the share of revenue devoted to servicing debt costs (the interest bite).

Figure 16 shows that the interest bite will increase significantly over the next 4 financial years. In 2023–24, 6.1 per cent of the GGS operating revenue, or $5.6 billion, was needed to service debt costs compared to 3.4 per cent, or $2.3 billion, in 2019–20. This is estimated to increase to 8.8 per cent, or $9.4 billion, by 2027–28.

Figure 16: Interest expense as a percentage of revenue



Source: VAGO, based on the AFR and state Budget.

Although the government aims to stabilise interest expense to revenue in the medium term, it has not set a specific and measurable target or the year it expects to achieve this measure.

When the government spends more money on interest payments, there will be less money available for public services.

The move from low to high interest rates significantly increase the interest bite

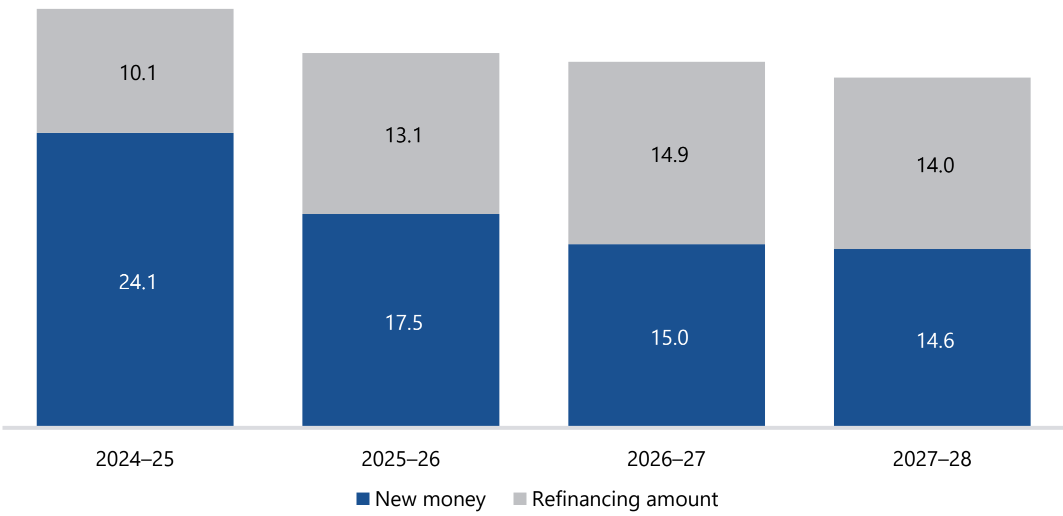
The transition from a low interest rate to higher interest rate environment post COVID-19 has and will continue to increase the cost of borrowing, leading to the proportion of interest costs from new and refinanced debt becoming larger.

The Treasury Corporation of Victoria (TCV) facilitates the raising of debt for the state by issuing bonds to both the domestic and international capital markets. It then lends this (on-lends) to DTF or other government entities. Approximately 90 per cent of TCV's lending is to the GGS via DTF. DTF uses the amounts borrowed to fund the government's initiatives.

TCV has projected to borrow a further $71.2 billion over the next 4 years to 30 June 2028 as seen in Figure 17 for on-lending to the GGS and other government entities.

The 2024–25 state Budget estimates GGS gross debt to be $228.2 billion by 30 June 2028.

Figure 17: Total financing required by the state by origin over the next 4 years ($ billions)



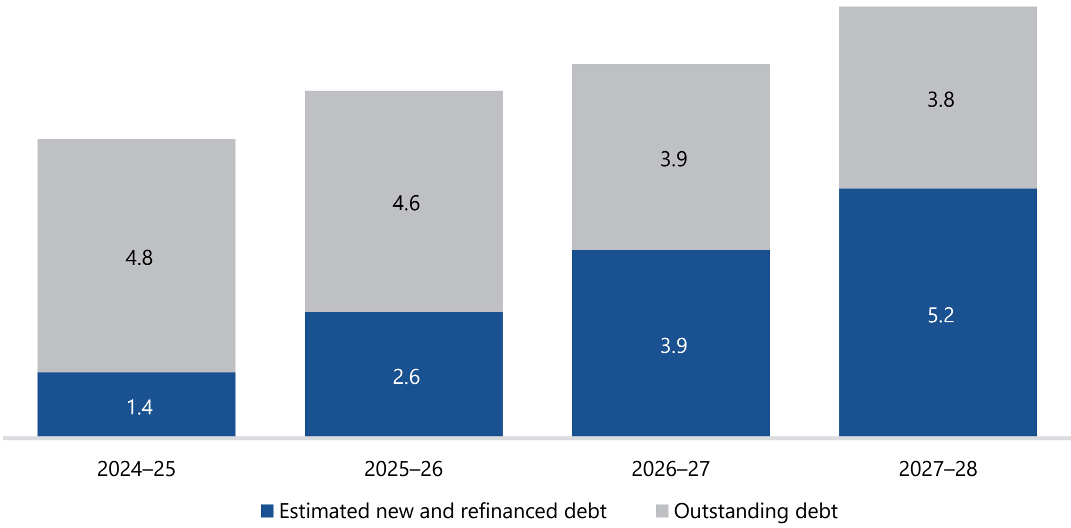
Note: New money refers to the funds required to finance new capital projects and operational needs.
Refinancing refers to the replacement of an existing debt obligation with another debt obligation under different terms. It is usually performed to extend the original debt over a longer period of time, to change fees or interest rates or to move from a fixed to variable interest rate.
Source: VAGO, based on TCV.

In addition, TCV projects to refinance $52.1 billion of existing debt. This debt was originally entered into in a lower interest rate environment during the pandemic. In the current high-interest rate environment it is likely these refinanced borrowings will come at higher interest rates, as will any new borrowings entered into. This presents a significant financial sustainability challenge because it reduces the proportion of revenue and income earned for use on public service delivery.

At 30 September 2024, the 10-year TCV government bond rate was 4.8 per cent, which is significantly higher than the average interest rate of around 3.6 per cent on TCV existing debt.

As currently issued TCV debt matures between 2025 and 2028, interest paid on it will decrease approximately from $4.8 billion to $3.8 billion. However, as this debt is refinanced and new funding requirements are financed, total new financing interest expenses are projected to rise approximately from $1.4 billion to over $5.2 billion over the same period as seen in Figure 18. This therefore means that the overall increase in interest expense for the period is projected to be approximately an increase of $2.8 billion.

Figure 18: Expected interest cost on TCV debt including new and refinanced debt ($ billion)



Source: VAGO, based on TCV.

Government bond

A government bond is a loan for a specified period with regular interest payments with repayment of face value in full at the maturity.

Rising employee costs consuming more revenue and income

Managing employee expense growth

Employees are the state's largest single operating expense.

In 2023–24, the GGS paid its employees $36.0 billion, which represents 37.0 per cent of its total expenses, compared to 35.9 per cent in 2022–23.

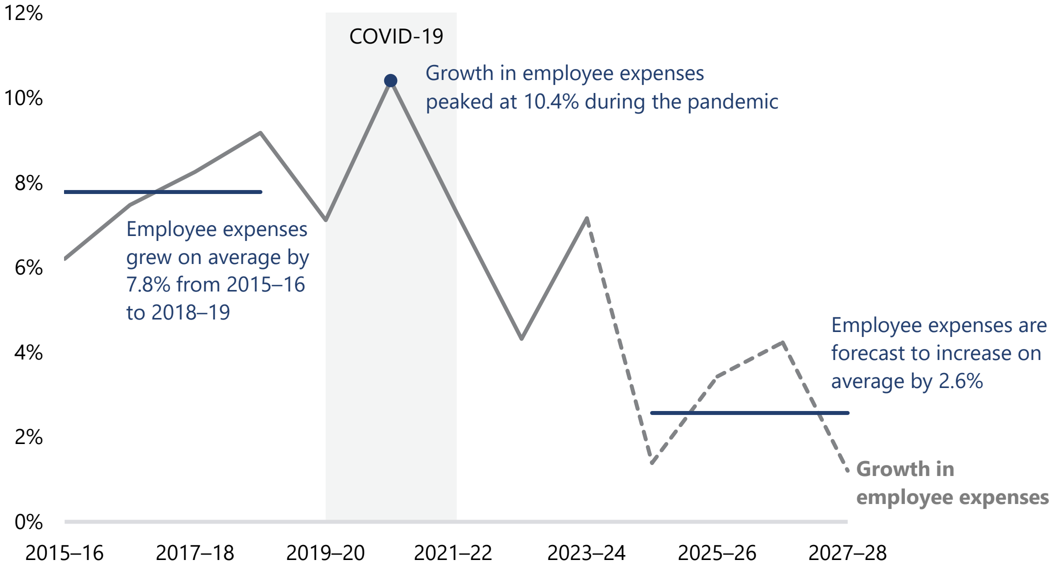
GGS employee expense has risen by 32.4 per cent from $27.2 billion in 2019–20 to $36.0 billion in 2023–24. Growth in employee expense peaked at 10.4 per cent in 2020–21 due to the government's pandemic response, however, has since gradually declined to 7.2 per cent in 2023–24.

The government forecasts it will grow by another 10.8 per cent over the next 4 years to $39.9 billion in 2027–28. This forecast is a modest annual increase of 2.6 per cent compared with the annual growth of 7.6 per cent over last 8 years.

Managing employee expense growth at forecast levels will be a challenge, particularly in a period of enterprise bargaining where several sector-based enterprise bargaining agreements (for example, for police, teachers, paramedics and nurses) either have been or are due for renegotiation in coming years at higher rates, which will likely increase pressure on employee expenses. This, combined with growing demand for public services driven by population growth, will add further strain on employee expenses.

The government's wages policy, established to set parameters around public sector enterprise bargaining, is expected to assist in managing some of these challenges.

Figure 19: Growth in GGS employee expenses



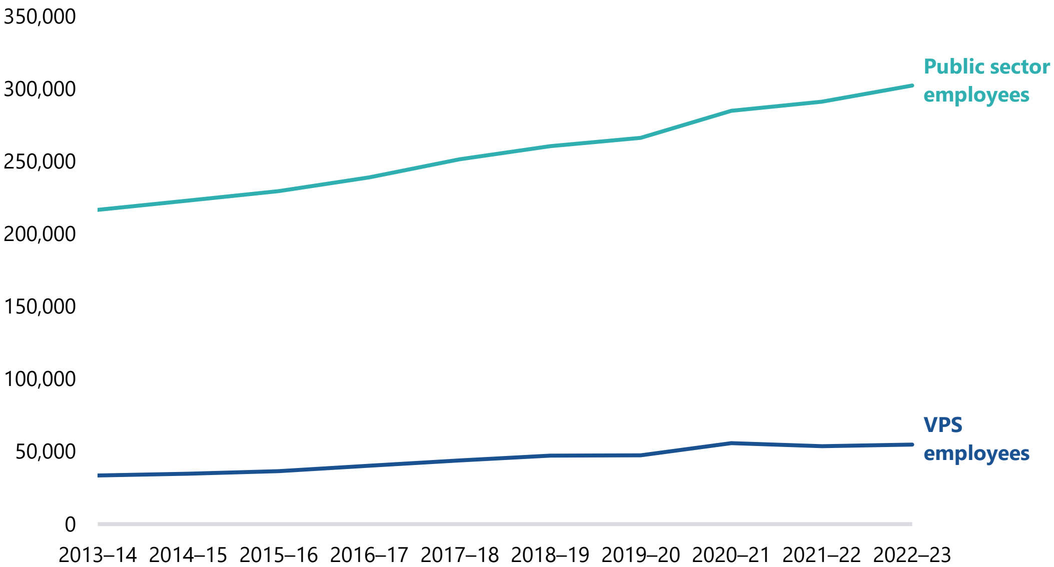
Note: Averages are shown as horizontal lines.
Source: VAGO, based on the AFR and state Budget.

Figure 20 shows that the number of Victorian Public Service (VPS) employees and all public sector employees increased over the 10-year period to 30 June 2023. At the time of writing this report, the Victorian Public Sector Commission had not released employee data for the year ended 30 June 2024.

The VPS grew by 64.0 per cent while all public sector employees grew by 39.5 per cent in that period.

Between 2018–19 to 2020–21, VPS FTE employees increased by 8,487, or 18.0 per cent, as the government responded to the COVID-19 pandemic. Following the COVID-19 pandemic, growth in VPS FTE employees has stabilised. There was 3.8 per cent decrease in FTE employees in 2021–22, followed by 2.1 per increase in 2022–23.

Figure 20: Number of FTE employees in the VPS public sector



Source: VAGO, based on the Victorian Public Sector Commission.

The government's Budget estimates of the last few years and in 2023–24 included implementing targeted cost-saving initiatives through staff reductions. If the benefits of these initiatives are not realised as planned, the employee cost will be greater than estimated and forecast targets will not be achieved.

The VPS

The VPS comprises of around 40 government departments, agencies and administrative offices.

Overall public sector

The overall public sector comprises of around 1,750 organisations, including 1,500 schools and 250 entities, such as hospitals, emergency services, water authorities, cemetery trusts, creative industry agencies and sport and recreation organisations. These agencies fall within both the GGS and public corporation sectors.

Expense management amid rising service demand and high inflation

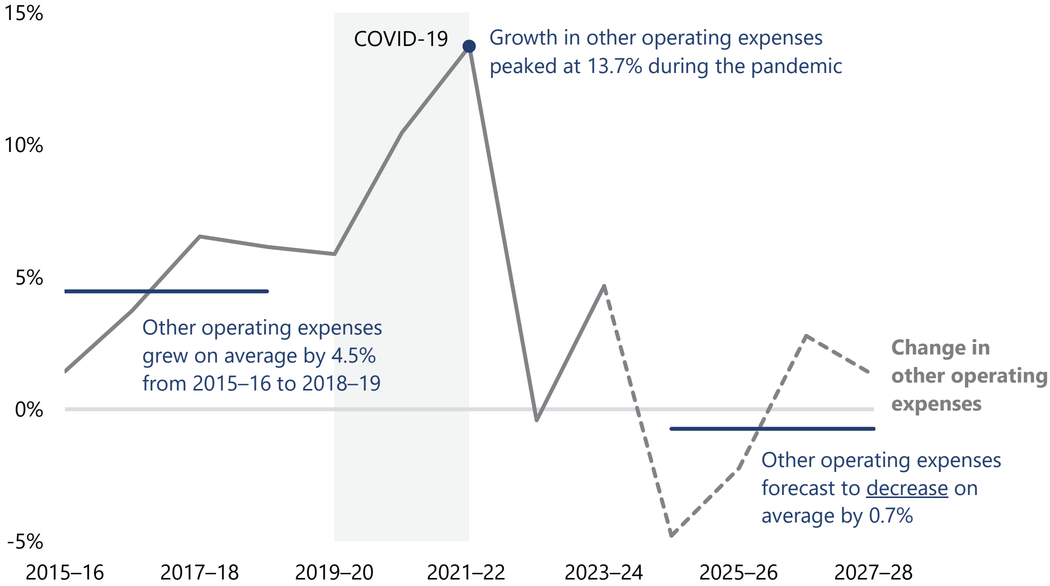
Cost management

Other operating expenses is the second largest component of GGS expenses, representing nearly 30 per cent of total expenses, or $29.1 billion, for 2023–24.

As shown in Figure 21, other operating expenses grew at an average rate of 4.5 per cent from 2015–16 to 2018–19. During the pandemic it peaked at 13.7 per cent per annum.

The government forecasts other operating expenses to reduce by an average rate of 0.7 per cent over the next 4 years to $28.2 billion by 2028.

Figure 21: GGS operating cost growth



Note: Averages are shown as horizontal lines.
Source: VAGO, based on the AFR and state Budget.

To achieve its financial objectives the government will need to ensure that the rate of growth in recurrent expenses falls and stays below revenue growth.

The government plans to reduce other operating expenses growth through various saving initiatives announced in past state Budgets. Realisation of these initiatives will be a challenge because of:

- unfavourable macro-economic conditions that accelerate expenses growth, including higher inflation and higher Victorian population forecasts increasing demand for public services
- financial discipline required by management of departments and agencies that face challenges from maintaining service delivery under constraints from previous saving initiatives and reduced funding from reprioritisation of programs and initiatives.

Some of the macro-economic conditions, such as higher inflation and population growth, may contribute to revenue and income growth.

The government will need to ensure relevant agencies, such as DTF, establish processes beyond current practices to monitor progress against these saving initiatives. This should help the government identify unexpected conditions and risks to both financial health and service delivery, allowing for timely change in approach.

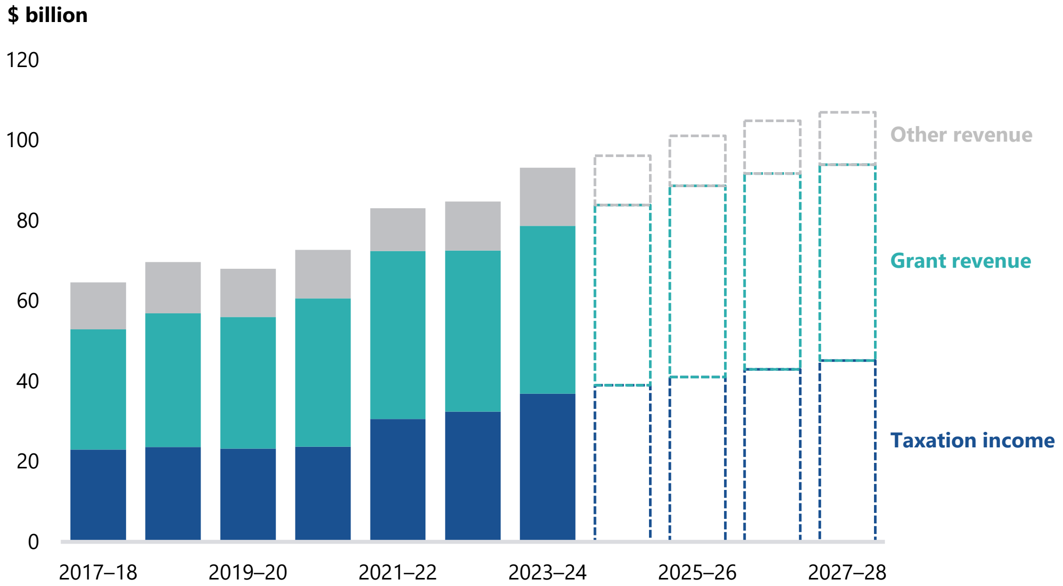
Limitations to new revenue and income streams

Sources for raising additional revenue and new cash inflows are limited

In the 2023–24 financial year, the GGS reported revenue and income of $93.1 billion. A major portion of this came from taxation income and grants from the Australian Government, accounting for 39.6 per cent and 44.9 per cent of the total respectively.

Revenue and income grew by 37.1 per cent, rising from $67.9 billion in 2019–20 to $93.1 billion in 2023–24.

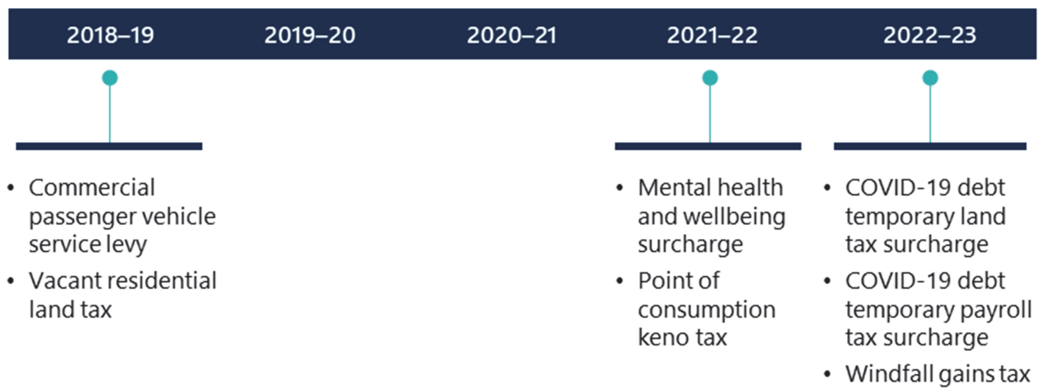
Figure 22: GGS revenue composition and growth



Source: VAGO, based on the AFR and state Budget.

Taxation income has grown by 59.2 per cent since 2019–20. The mental health and wellbeing surcharge and COVID debt levy contributed $0.9 billion and $3.1 billion in additional tax revenue in 2022–23 and 2023–24.

Figure 23: New taxes introduced by the government



Source: VAGO, based on the State Revenue Office Victoria.

Commercialisation opportunities are diminishing

The commercialisation of government assets and services has been a significant source of cash inflow in recent years.

Over the last 8 years, the government has commercialised or leased several assets and functions to private sector entities. Key transactions include:

- leasing the Port of Melbourne land, channels and infrastructure assets for an upfront payment of $9.7 billion in 2016–17
- commercialisation of Victorian Land Registry Services for $2.9 billion in 2018–19
- VicRoads modernisation joint venture arrangement for $7.9 billion in 2022–23.

While the receipt of $20.5 billion in funds from these arrangements has assisted the government in managing operating and investing cash needs, it has also lost some future cash inflows generated from these assets and services.

Unplanned and significant cost escalations of major infrastructure projects

Cost escalations of major infrastructure projects

The GGS outlaid $17.4 billion on infrastructure and capital assets this year, an increase of $1.1 billion compared to last year's $16.3 billion.

For the last 4 years, we have tracked the performance of major projects expected to cost $100 million or more. We are currently reviewing major projects that were complete and active at 30 June 2024 and listed in Budget Paper 4: State Capital Program as part of our limited assurance review Major Projects Performance Reporting 2024. This limited assurance review report is currently scheduled for tabling in 2025.

Through our reviews, we have consistently observed cost escalations in major projects. For example, the total estimated investment (TEI) of the Metro Tunnel Project was $10.9 billion when it first appeared in Budget Paper 4. However, as of 30 June 2024, the TEI is estimated to reach $12.6 billion, representing an increase of $1.7 billion.

The costs escalations in major projects can be attributed to several reasons both within and beyond the control of the state, including:

- staging of funding increases after projects develop more detailed plans
- redesigning or increasing the scope or capacity of a proposed project
- the impact of decisions about adopting procurement models
- unexpected price increases after a market engagement
- volatility in the construction industry and supply chains
- contract variations signed with private sector parties.

Costs escalations, regardless of their causes, may need additional funding.

In the 2024–25 state Budget the government committed to investing $208 billion in capital projects. This is a net increase of $7.9 billion compared to the same time last year.

In the 2024–25 state Budget, the government announced that the Suburban Rail Loop (SRL) East is expected to cost between $30.0 billion and $34.5 billion. The government has not yet fully disclosed the TEI, estimated expenditure and estimated completion date of the entire SRL.

If cost escalations in current and new major projects persist, it will further significantly strain the state's fiscal sustainability.

3.3 Emerging risks beyond the GGS and their impact

Why the financial sustainability of public corporations is important for the GGS and Victorians

Public corporations' financial sustainability

Public corporations in Victoria play a crucial role in providing services to Victorians and fulfilling the government's economic, social and public policy objectives. They provide services in sectors considered essential or strategic, such as transportation, utilities and public financial services.

Financial sustainability of PFCs is critical for the government's overall fiscal sustainability. It allows these corporations to continue providing essential services without disruption and improve the quality of services by way of investing in innovation and new development.

Non-sustainable financial corporations can add financial strain on the GGS's financial position because taxpayers' money is often used to support the financial health of these corporations. Further, fees and levies charged by these corporations to the public may increase adding financial burden to citizens.

There are several emerging risks in the public corporations space that require close attention by the government to avoid further sustainability challenges. They are discussed below.

Continued trend of rising insurance liabilities

Insurance liabilities to rose to $50.1 billion

Three of the 7 PFCs are insurers – the Victorian WorkCover Authority (WorkSafe), the TAC and the Victorian Managed Insurance Authority. These entities, which are not in the GGS, have a considerable influence on the operating result, balance sheet and cashflow outcomes of the state.

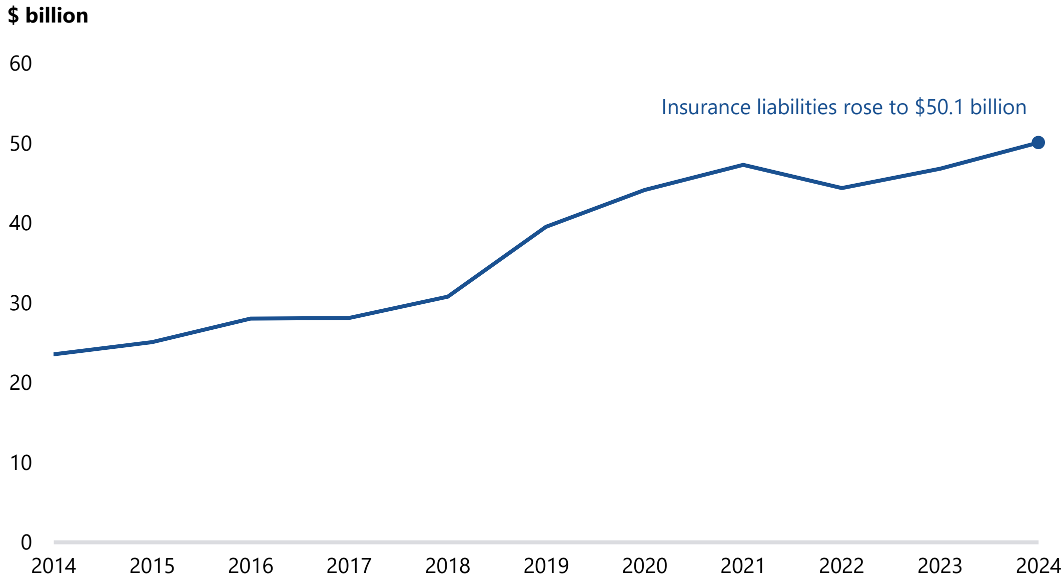
Transactions with these PFCs also have a significant impact on the GGS operating result, balance sheet and operating cash result outcomes in varying ways. The government:

- in recent years, has used taxpayers' money to support the financial sustainability of WorkSafe – as an example, WorkSafe received $1.3 billion from the government across 2020–2023 to support its financial sustainability
- sources income from these corporations through dividends, grants, taxation-equivalent payments, levies and capital repatriation that helps with the financial outcomes of the GGS – as an example, the TAC paid a $1.1 billion dividend to DTF this year.

At 30 June 2024, these insurers had $53.1 billion of total liabilities and held $53.3 billion of total assets. The majority of these assets were held to back insurance liabilities. Of those liabilities, $50.1 billion (94.5 per cent) related to outstanding insurance claims. Insurers paid $6.2 billion in claims during 2023–24 (compared with $5.4 billion in 2022–23).

Figure 24 shows that the value of the total outstanding insurance claim liabilities of the state continues to grow.

Figure 24: Total insurance claim liabilities at 30 June



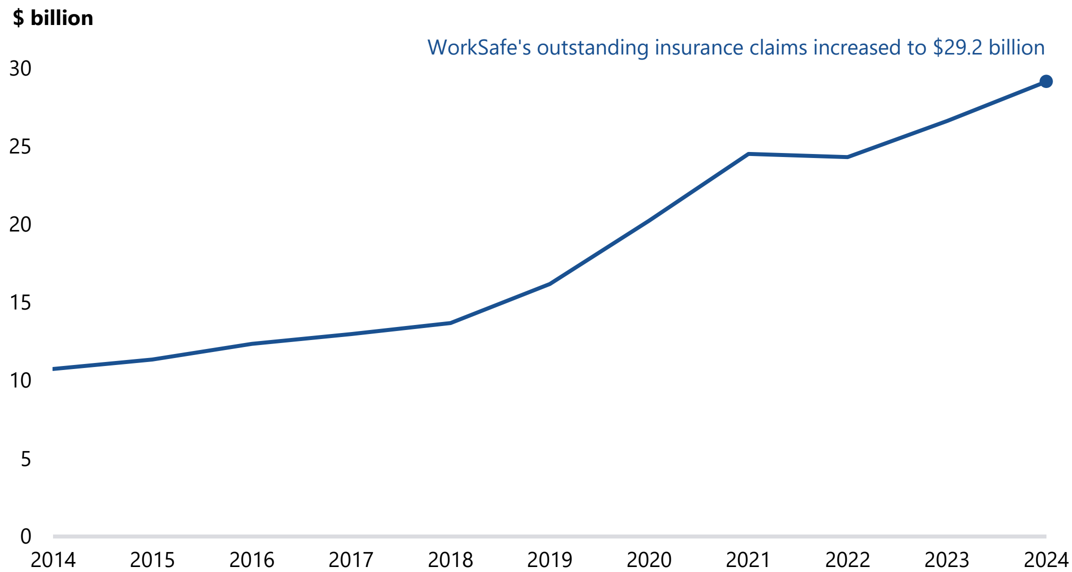
Source: VAGO, based on the AFR.

WorkSafe contributes 58.2 per cent to the state's insurance liability and remains the primary driver of the growth

WorkSafe is Victoria's workplace health and safety regulator. It manages the WorkCover insurance scheme and aims to reduce harm in the workplace and improve outcomes for injured workers.

Figure 25 shows that the value of WorkSafe's outstanding insurance claims has increased by more than 80 per cent since 2018–19.

Figure 25: WorkSafe's outstanding insurance claim liabilities at 30 June



Source: VAGO, based on data from WorkSafe's financial reports.

Weekly benefits paid to workers and common law claims are the major contributors to the significant growth of the WorkSafe claims cost and the outstanding insurance claim liabilities. Weekly benefit payments supplement wages when workers are unable to work due to mental or physical injuries. Common law claims arise where workers seek redress through the legal system.

In 2023–24 the liability increased by $2.5 billion (compared with $2.3 billion in 2022–23). The primary contributors to this increase were a 62 per cent increase in the liability for common law claims, offset by a 10 per cent decrease in the liability for weekly benefits for mental injury claims, and a 27 per cent decrease in the liability for weekly benefits for physical injury claims.

The decrease in claim liabilities for mental and physical injuries referred to above was a direct result of the WorkCover scheme reforms through the passing of the *Workplace Injury Rehabilitation and Compensation Amendment (WorkCover Scheme Modernisation) Act 2024* on 31 March 2024. This is discussed further below.

WorkSafe's financial sustainability is key to achieving its purpose

Financial sustainability is a key to achieving WorkSafe's purpose of reducing workplace harm and improving outcomes for injured workers. Rising claim costs from significant increases in claims and workers relying on the benefits for longer have deteriorated the financial sustainability of the WorkSafe scheme in recent years. This has been compounded by the gap between the premium revenue and claims cost (premium deficit).

In our past reports, we highlighted the challenges posed by adverse claims experience and the rising premium deficit, which significantly deteriorated financial sustainability of the scheme requiring the government's financial assistance. We emphasised the need for the government to take measures to ensure WorkSafe's long-term financial sustainability.

The long-term financial sustainability of insurers is measured using the insurance funding ratio, with a preferred range of 100 to 140 per cent for WorkSafe. WorkSafe's insurance funding ratio was 106 per cent at 30 June 2024 (compared to 105 per cent at 30 June 2023).

In response to financial sustainability challenges, the government:

- approved a substantial premium increase effective from 1 July 2023 raising the average annual premium by 41.7 per cent
- legislated and implemented the scheme modernisation reforms, effective from 31 March 2024.

The premium increase and the implementation of scheme modernisation reforms, further discussed below, are expected to help WorkSafe maintain its insurance funding ratio within the preferred range without additional government assistance.

Insurance funding ratio

Insurance funding ratio is a measure of assets against claim liabilities used as a measure of long-term financial sustainability for a scheme.

WorkCover reforms decreased claim expenses and liabilities by $1.2 billion

On 31 March 2024, the government passed the *Workplace Injury Rehabilitation and Compensation Amendment (WorkCover Scheme Modernisation) Act 2024*. With that, following key changes came into effect:

- new eligibility requirements for mental injury claims
- an additional whole person impairment requirement for workers to continue receiving weekly payments after the 130-week second entitlement period
- establishment of Return to Work Victoria for supporting injured workers' recovery, rehabilitation and return to work.

WorkSafe expects these reforms to initially stabilise the scheme's claims experience and return its financial performance to a sustainable level in the mid to long term.

The financial impacts of these reforms reduced the claim liabilities at 30 June 2024 and claim expenses for 2023–24 by $1.2 billion. This reduction primarily resulted from reassessment of claims incurred prior to 31 March 2024 that had not yet reached 130 weeks by that date under the new eligibility requirements.

Risks to achieving the 2035 unfunded superannuation funding target

What is the state's superannuation liability?

The state's public-sector-defined benefit superannuation plans are responsible for the liability for employee superannuation entitlements. These plans are not reported in the AFR because they are not controlled by the state.

The superannuation plans, which are principally operated for GGS employees, are not fully funded. The funding of these superannuation liabilities is the responsibility of the state and therefore a liability is recognised in the AFR for these obligations.

The state's liabilities include a superannuation liability of $18.2 billion at 30 June 2024.

In accordance with the requirements of Australian Accounting Standard AASB 119 *Employees Benefits*, this liability is valued using a discount rate based on Australian Government bond yields. However, the state's funding requirement is determined using the expected return on the superannuation fund's assets. On this basis, the state's actuarial service provider has estimated an unfunded superannuation liability lower than what is reported in the AFR, at $11.5 billion as at 30 June 2024. The government targets to fully fund this unfunded superannuation liability by 2035 by way of annual contributions, a key financial measure of the government.

The unfunded superannuation liability for funding purposes is lower than the superannuation liability reported in the AFR because the expected return on assets of the superannuation fund is currently greater than the Australian Government's bond yield.

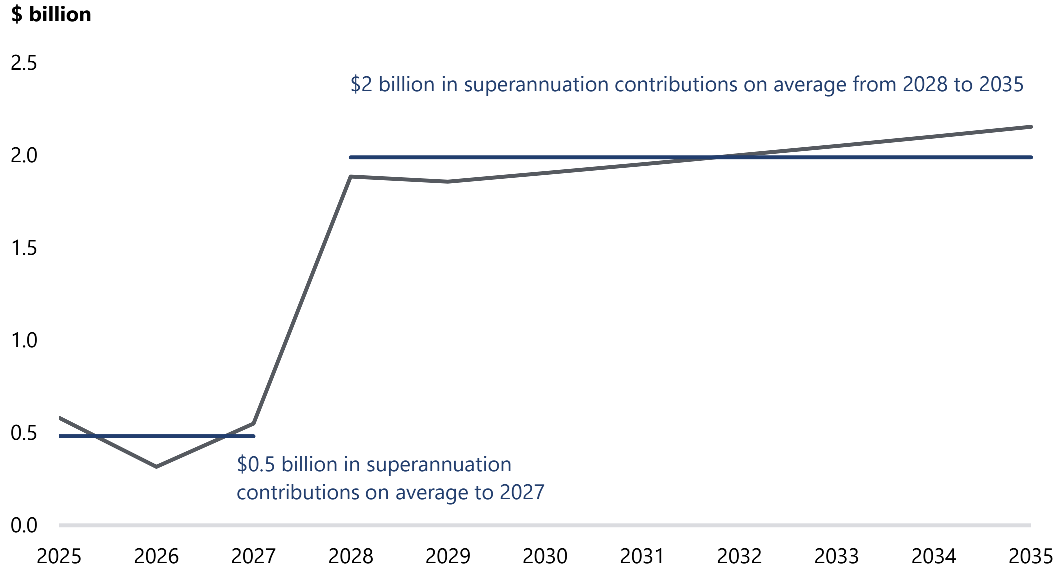
$17.3 billion is required to fully fund the liability by 2035

In the last 5 years the government has contributed around $0.8 billion each year to achieve the funding target. The government deferred annual contributions from 2023 to 2027 by $3.0 billion following the Victorian election in 2022, as outlined in Labour's Financial Statement 2022. The government did not explain why the contribution payments were varied and deferred. However, it keeps its commitment to fully fund the liability by 2035.

The government will need to contribute $17.3 billion (nominal value) from 2024 to 2035 to meet its fully funded commitment. These estimates are based on current assumptions used to determine funding requirements.

Figure 26 shows, more specifically, that under its revised contribution plan, the government plans to contribute approximately $0.5 billion per year over the next 3 years to 2027. This means its annual contribution will need to increase to approximately $2.0 billion from 2028 to meet the full funding target by 2035.

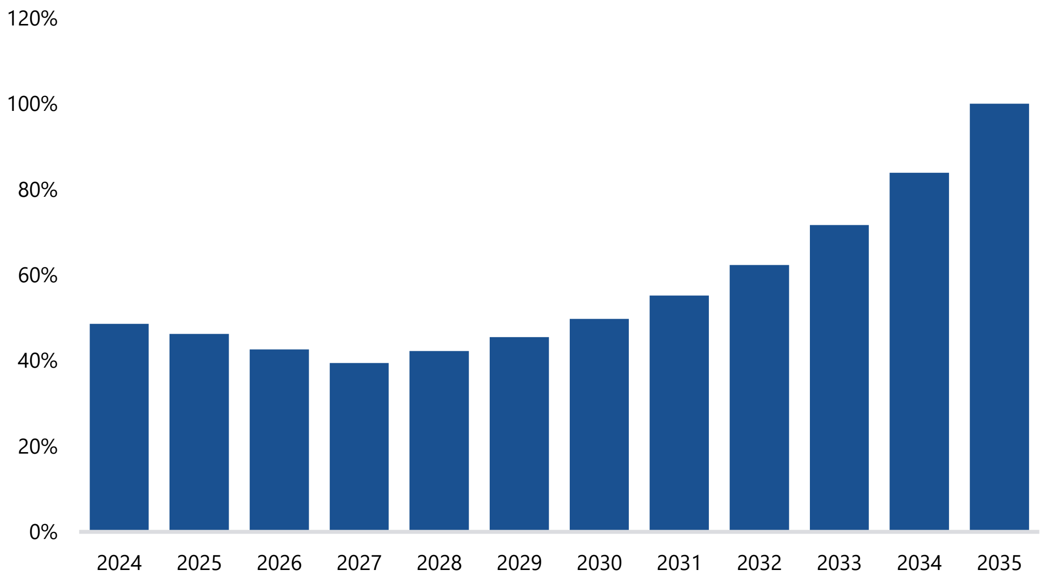
Figure 26: Projected annual superannuation contributions



Note: Averages are shown as horizontal lines.
Source: VAGO, based on DTF.

This contribution deferral will result in the funding position falling below 40 per cent on the funding basis by 2027 as shown in Figure 27.

Figure 27: Projected funding position of superannuation liability on the funding basis



Source: VAGO, based on DTF.

There are several significant risks to achieving this funding target. Rising employee expenses, service delivery costs and interest payments continue to strain the state's fiscal capacity and can compound the challenge of making ongoing contributions.

Furthermore, the current estimate of the liability is subject to external risks, such as the fund's investment performance, salary and pension increases. For example, a lower than expected investment return from the fund's assets would require more contributions from the government to fully fund the liability by 2035.

Nominal value

Nominal value is the value measured in terms of absolute money amount without taking inflation or other factors into account.

Funding position

Funding position shows the proportion of a superannuation fund's liability covered by the fund's assets. It is a measure of whether the fund has enough assets to pay out future benefits to its members.

4. Proper accounts and records

Snapshot

Material entities have adequate internal controls to prepare financial reports

DJCS failed to implement effective oversight of outsourced service provider

VicTrack continues to improve asset accounting

Many material entities' IT system controls have new and unresolved weaknesses

Conclusion

DTF implemented effective internal controls to support the preparation of a complete and accurate AFR.

VicTrack continues to make progress in improving its internal control framework that relates to asset accounting.

DJCS did not obtain assurance over an outsourced service provider's operations that manages systems and processes for distracted driver and seatbelt offences on its behalf. These systems and processes support accounting for fines income.

Significant weaknesses were identified in IT system controls across many material entities. Disappointingly, a number of prior-year IT control deficiencies remain unresolved, reflecting ongoing weaknesses in their control environments.

Adequate internal controls for financial reporting at material entities

Internal controls at material entities are adequate

We assess the internal controls at each material entity that ensure its financial report is complete and accurate and complies with relevant legislation. We report any significant issues to the relevant entity's management and its audit committee, as required under the Australian Auditing Standards.

We found that internal controls at material entities were generally adequate for financial reporting, with the exception of the matters outlined below.

DJCS – failure to implement effective oversight of outsourced service provider

Distracted driver and seatbelt traffic offence fines introduced in 2023–24

Changes to Victorian road rules and regulations came into effect on 31 March 2023. Changes included implementing camera detection of portable devices (includes mobile phones) and seatbelt-wearing offences. DJCS is responsible for administering the process under the state's road safety camera program.

There was a 3-month introductory period for the new camera-detected offences during which DJCS sent warning letters to offenders. DJCS commenced issuing fines for these offences on 1 July 2023, which it recognises as income in 'Note 4.3 Administered items' of its financial report.

Failure to oversight outsourced service provider

DJCS outsources the operation of camera technology, IT systems and processes used to detect, record and verify data for those offences to a service provider. The process involves the following steps:

- roadside cameras photograph approaching vehicles
- the cameras use artificial intelligence (AI) software to filter images and detect possible mobile phone use by the driver, or failure to correctly wear a seatbelt by the driver or front seat passenger – AI automatically rejects images where it does not see a potential offence
- an individual reviews each image accepted by AI and rejects clear non-offences (false positives)
- 2 individuals independently assess each potential offence against defined business rules, which are aligned to Victorian road rules and regulations
- Victoria Police, as the enforcement agency, reviews identified offences and approves the issuing of a traffic infringement notice
- information of the offences approved by Victoria Police is uploaded into the DJCS fines system and the department issues traffic infringement notices – it is at this point that fines income is recognised by DJCS.

In 2023–24, roadside distracted driver and seatbelt cameras photographed 12.2 million vehicles, of which approximately 0.11 million were approved by Victoria Police as committing an offence, where offenders were subsequently issued a traffic infringement notice. Images assessed as non-offences at the various stages in the process were deleted after a defined period.

During the year, DJCS did not obtain assurance over the outsourced service provider's operations as required by the *Standing Directions 2018 Under the Financial Management Act 1994*. This means it did not know whether the outsourced provider had maintained appropriate controls over its systems and processes to ensure all offences detected by the cameras were provided to Victoria Police to approve issuing traffic infringement notices and enable fines income recognition. This does not affect the validity of infringement notices issued by DJCS.

VicTrack – accounting for fixed assets and inadequate asset records

Continued asset investment in transport and planning

The state's investment in building, developing and replacing assets in the transport and planning sector continued. In 2023–24 the DTP invested $11.4 billion in assets ($12.8 billion in 2022–23). With respect to operational transport projects, DTP enters into the contracts, oversees the capital spending and then transfers the completed assets to VicTrack as the state's legal custodian of them.

Asset accounting is improving though further work is required

Historical asset accounting issues

In past reports, we have explained the significant shortcomings in asset accounting by DTP and VicTrack since 2019–20. The issues have included:

- an inability to identify individual assets in VicTrack's asset register
- delays in the recognition of assets, which means depreciation was not charged from when assets were first available for use
- no assessment of the nature of capital spending to make sure it could be recognised as part of an asset
- inadequate review of work-in-progress accounting records, resulting in stale work-in-progress amounts and asset write-offs
- asset disposals and replacements not identified and removed from the VicTrack asset register.

Progress to resolving these issues

DTP and VicTrack have devoted significant time and effort to resolve these issues. They have now implemented an asset collection and attribution framework that has been in place since the 2022–23 financial year. As part of our 2022–23 audit work, we confirmed the effective operation of this framework for most assets added since 2019. Some improvements remain to clarify and capture asset attributes for tracks and signals.

Further work to be completed to resolve legacy issues

While the work undertaken by VicTrack and DTP over the last 3 financial years and the new framework mean new assets are completely and accurately recorded, our testing found issues remain with information on the register predating 2019.

We would normally qualify a financial report for this matter. However, an additional qualification on this issue was not required because we already modified VicTrack's financial report for not complying with the leasing matter explained in Section 2.

This did not impact our opinion on the AFR because we concluded that the risk of a material misstatement in the AFR was low.

Accounting for asset write-offs and writedowns expected to be resolved in 2024–25

Significant write-offs and writedowns

As part of the valuation process, over $2.7 billion of asset value was written off from 2019–20 to 2020–21. The valuation process identified 2 issues:

- some maintenance-type works were incorrectly capitalised
- the valuer took a different approach to estimating fair value for an asset in a live operating environment that was different to the approach allowable under the Australian Accounting Standards.

A significant part of the write-offs related to level crossing removal projects, where construction occurs in an operating transport network.

Different approaches expected to be resolved in 2024–25

While we did not identify any material asset write-offs or writedowns during the last 2 financial years, the different approaches to measuring the current replacement cost for operational transport assets is still unresolved. The Australian Accounting Standards Board has issued authoritative guidance for estimating the fair value of assets for not-for-profit entities, which will apply to the 2024–25 reporting period. DTP has commenced consideration and discussion on the issue with the Valuer-General Victoria but further effort to resolve the different approaches will be required so that any changes can be implemented by the 2024–25 timeframe.

Department of Jobs, Skills, Industry and Regions – deficient controls for COVID-19 grant programs

Deficient controls for COVID-19 grant programs

In the *Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2022–23*, we commented on deficiencies in the Department of Jobs, Skills, Industry and Regions' (DJSIR) administration of COVID-19 grant programs. These included:

- its approach to verifying eligibility for the Business Costs Assistance Program (BCAP) and Licensed Hospitality Venue Fund (LHVF) was inconsistent with grant conditions authorised by the government and program intent
- design flaws in controls to detect and investigate potential fraud and error
- failure to provide full and frank advice to the government throughout the program
- post-payment investigation was not timely and there was no planned evaluation of the BCAP and LHVF programs.

We recommended that DJSIR appoints an independent evaluator to assess and report on the effectiveness of the BCAP and LHVF grant programs and whether value for money was achieved. The evaluation should identify lessons learnt and make recommendations for future programs.

Progress to resolving these deficiencies

During the last year, DJSIR completed a post-payment review of COVID-19 business support grants and engaged an external contractor to undertake an audit of grant programs assessed as higher risk. The audit:

- examined whether COVID-19 grant recipients that backdated their ABN and or GST registration were eligible for the funding
- gathered evidence on how grant funds were used.

Management received the final report from their external contractor in September 2024. We plan to provide an update in a future report to Parliament on any departmental outcomes that arise from this.

DJSIR has also developed a grants compliance framework that:

- describes the department’s key responsibilities when administering grants and grant programs under the *Financial Management Act 1994* and other legislation
- describes the authorising environment for managing and approving grants and identifies the key roles in the department that support the oversight and administration of grants and grant programs
- supports grant administrators to establish effective and efficient administrative controls and ensure that value for money outcomes are maximised
- sets out the mandatory controls and recommended best-practice standards to follow for meeting those obligations across the grant lifecycle.

WorkSafe – assessment of recovery of deferred tax asset

WorkSafe's tax arrangements

WorkSafe is required to pay income tax under the National Tax Equivalent Regime. Under this regime, it is able to use past tax losses to offset any future tax payable to the state.

The Australian Accounting Standards allow the recognition of deferred tax assets for tax losses.

Recoverability of deferred tax assets arising from tax losses

WorkSafe recorded a deferred tax asset of $2.6 billion at 30 June 2024 in its balance sheet, including $2.0 billion arising from unutilised tax losses.

In our report to Parliament for 2022–23, we raised an observation regarding the recognition of deferred tax assets arising from these unutilised tax losses. Such assets can only be recognised as assets when future profitability is probable. WorkSafe's profitability was dependent on Parliament passing legislation to reform the scheme, which had not occurred at the balance date last year.

On 31 March 2024, Parliament passed the WorkCover scheme reforms with 2 key changes to benefit entitlements for mental injury claims and weekly payments. Management estimated that these reforms, along with a substantial increase in the average premium rate to 1.8 per cent effective from 1 July 2023, would improve the profitability and ongoing financial sustainability of the scheme.

There are several uncertainties associated with the effectiveness of these reforms and consequential improvement to financial outcomes. In our reporting to management and those charged with governance, we have recommended management closely monitor the effectiveness of reforms and their impact on financial outcomes and reassess the recoverability of their deferred tax asset annually.

Operationalisation of machinery-of-government changes

Purpose of changes

On 1 January 2023, several changes to the machinery of government (MoG) came into effect following the November 2022 state election. The government decided to increase the number of departments in the VPS from 9 to 10. This resulted in setting up a new department – the Department of Government Services (DGS) on 1 January 2023.

The primary objective of this change was to improve how Victorians and businesses engage with the government and to accelerate digital transformation and corporate services reform across the VPS.

This was a significant reorganisation of government functions and service delivery, where many functions were moved into DGS from 4 other key departments. DGS was in a unique position because an existing structure was not in place for these government functions to move into.

With the establishment of DGS, certain corporate service functions of DTF and the Department of Premier and Cabinet (shared service clients) were centralised with DGS under a corporate shared services arrangement.

Status of the MoG change

During our audit of the DGS financial report for 2023–24, we observed the following with regard to the status of MoG implementation:

- transition and integration of some functions transferred from other departments were still in progress
- governance and assurance structures, like the audit committee and internal audit function, were not permanently established until May 2024

- well-defined shared service arrangements (service level agreements and service catalogues) were not established and implemented at 30 June 2024, despite the initial plan to have them in place within the first 12 months of operation
- internal controls and finance systems were being established during 2023–24 with some financial transactions still using financial systems of former departments
- an independent assurance process over the services provided to shared service clients was still being established, scheduled to be fully completed in the 2025–26 financial year.

Slower transition delaying realisation of benefits

It often takes time to operationalise a significant MoG change. While progress has been made over the last 18 months, it appears that more than 2 years will be needed to fully operationalise the change. This indicates that the VPS was not able to adapt to such a rapid reorganisation of this size within the short timeline imposed, of less than one month.

This slower transition may result in delays in achieving the intended objectives of enhancing engagement with the government, accelerating digital transformation and reforming VPS corporate services.

From an audit perspective, additional time and effort was required to gain assurance over the financial reports of DGS and its shared service clients.

The government holds the authority to reorganise its executive functions. However, rapid and unplanned MoG changes carry significant implications. A substantial MoG change like this requires considered planning, time and resources to implement to ensure realistic milestones are established for the realisation of expected benefits.

Recommendations

We made several recommendations to DGS in our reporting to management and those charged with governance from our observations, including finalisation of service level agreements and establishing a sound internal control framework and assurance process over the services provided to shared service clients.

We also recommend the Department of Premier and Cabinet works with other departments involved in this MoG change to conduct a post-implementation review and share the findings and lessons learnt with the government to improve planning, implementing and operationalising future MoG changes.

Various material entities – new and unresolved IT control weaknesses continue

Why IT controls are important

IT is integral to the operations and success of an organisation.

IT systems support critical business processes, store sensitive data and are essential for effective operations of any organisation. Effective IT controls reduce the risk of unauthorised access and changes to systems and help protect the underlying integrity of data.

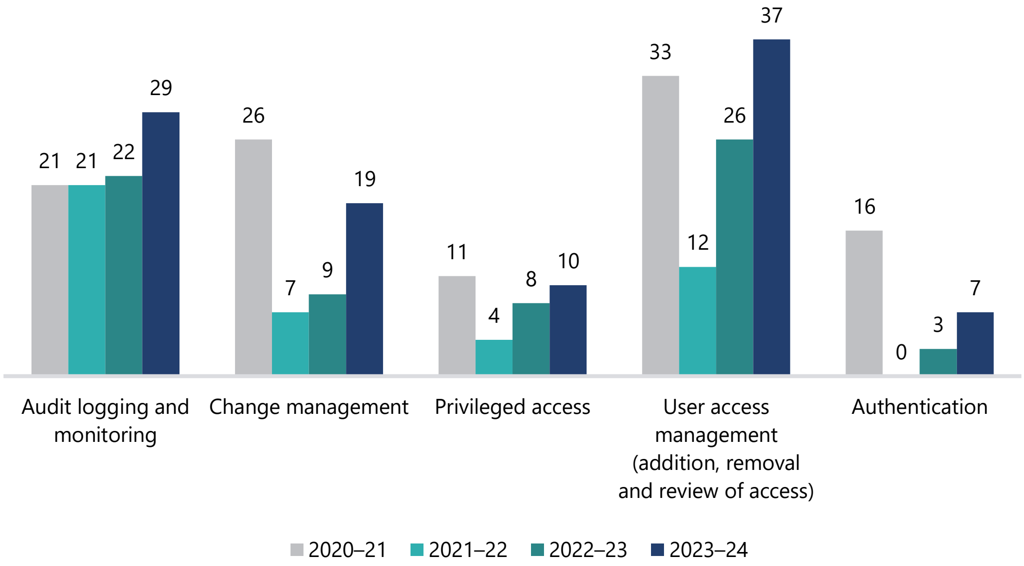
They are a prerequisite for the reliability of the systems used by the entities for financial reporting.

IT control deficiencies continue to rise

We continue to identify IT control deficiencies at many material entities. As illustrated in Figure 28, there has been a notable increase in issues identified from 2020–21 to 2023–24.

This increase can be attributed to an expansion in the systems included in our audit testing. Growing reliance on technology coupled with evolving auditing standard requirements have led to the increase in in-scope systems for our audits.

Figure 28: New and unresolved IT control deficiencies



Source: VAGO.

Common IT control deficiencies identified at the relevant material entities.

IT control deficiencies include …	Meaning …	This may result in …
audit logging and monitoring	system-generated audit logs were not always enabled to track critical and sensitive activities, including but not limited to changes to system user access, configurations, reports and master data. Where audit logging is enabled, we observed numerous instances where there is no active monitoring of these logs.	unauthorised or suspicious activities can go unnoticed or undetected that may impact the integrity of financial reports.
change management	ineffective change tracking, lack of proper change approval processes, inadequate testing before deployment and inadequate segregation of duties were identified.	unauthorised or improper changes made to critical systems or data, which may result in system outages, data corruption and errors in financial reports.
privileged access	employees assigned with only the minimum access necessary to do their job – is not consistently applied within and by material entities. We observed instances where employees were assigned system access well beyond what they require to complete their day-to-day tasks.	users with such access could misuse their accounts to gain access to sensitive systems and data.
user access management	inadequate user access reviews, failure to implement role-based access control, inconsistent or delayed termination of system access and granting of access without proper request or approval were identified.	poor management of user accounts can give individuals more access than needed, increasing the risk of accidental or intentional misuse of systems and data.

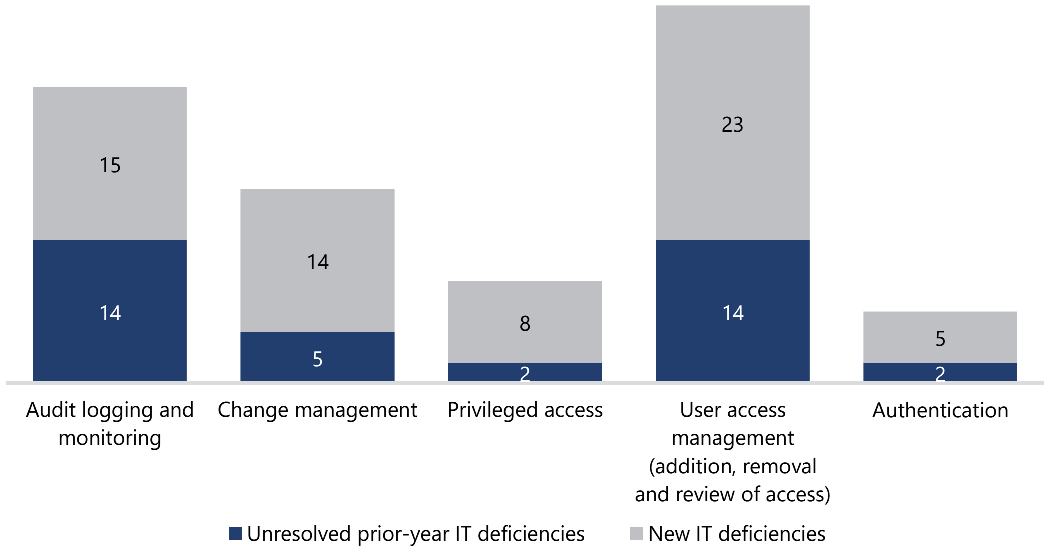
IT control deficiencies include …	Meaning …	This may result in …
authentication	weak password policies and password settings in the system as well as a lack of multi-factor authentication for some material entities are driving authentication issues.	weak authentication mechanisms make it easier for attackers to compromise user accounts by methods such as the guessing of passwords or tricking users into sharing such credentials with them.

Prior-year IT control deficiencies remain unresolved

Thirty-seven prior-year IT control deficiencies remain unresolved across many material entities, reflecting ongoing weaknesses in their control environments. Despite efforts to address these deficiencies, management struggle to fully implement the recommended controls.

Figure 29 shows a total of 102 new and unresolved prior-year IT control deficiencies.

Figure 29: New and prior-year IT control deficiencies in 2023–24



Source: VAGO.

Root causes of prolonged and rising IT control deficiencies

IT control deficiencies continue to occur and remain open for a prolonged period because of:

- competing priorities, funding constraints and staff turnover
- limitations of systems
- legacy applications making it difficult to put in place controls addressing new risks from program changes, access issues and cyber threats
- limited awareness by management of the risks and potential effects these deficiencies could have on operations
- untimely detection or remediation and limited oversight.

We have made several recommendations to relevant material entities to address these deficiencies through our reporting to management and those charged with governance.

Appendices

Appendix A: Submissions and comments

We have consulted with agencies named in this report, and we considered their views when reaching our audit conclusions. As required by the *Audit Act 1994*, we gave a draft copy of this report, or relevant extracts, to those agencies and asked for their submissions and comments.

Responsibility for the accuracy, fairness and balance of those comments rests solely with the agency head.

Responses received

Response provided by the Treasurer of Victoria

Treasurer of Victoria

Minister for Industrial Relations
Minister for Economic Growth

1 Treasury Place
GPO Box 4379
Melbourne Victoria 3001
Telephone: +61 3 7005 9474

D24/245226

Mr Andrew Greaves
Auditor-General
Victorian Auditor-General's Office (VAGO)

[redacted]

Dear Mr Greaves,

RESPONSE TO THE AUDITOR-GENERAL'S REPORT ON THE ANNUAL FINANCIAL REPORT OF THE STATE OF VICTORIA, 2023-24

Thank you for your letter on 31 October 2024, seeking my response to your report on the Annual Financial Report (AFR) of the State of Victoria: 2023-24 (the report) before its finalisation and transmission to Parliament.

The report confirms the issuance of a clear audit opinion on the financial statements of the State of Victoria and the General Government Sector (GGS) for the financial year ended 30 June 2024, providing reasonable assurance that the financial performance and position of the State of Victoria and the GGS as presented in the AFR is reliable.

This means Parliament and the Victorian community can depend on the information presented within the AFR to enhance their understanding of the state's financial outcomes and to promote informed decision-making.

The report highlights a significant improvement in the timing of completing and signing-off financial reports this year, with the median time for material entities to certify financial reports largely returning to pre-pandemic timelines over the past two years.

The report further provides an independent audit assessment of the financial outcomes and fiscal aggregates of the GGS for the year ended 30 June 2024. As the report notes, the State's fiscal strategy is underpinned by five steps:

- Step 1: Creating jobs, reducing unemployment and restoring economic growth.
- Step 2: Returning to an operating cash surplus.
- Step 3: Returning to operating surpluses.
- Step 4: Stabilising debt levels.
- Step 5: Reducing net debt as a proportion of the Gross State Product (GSP) by the end of the forward estimate period.

This is a balanced approach, ensuring the Government carefully navigates through the economic challenges facing the State. The recent 2024-25 Budget demonstrated that this strategy is working, with the economy performing well and the labour market strong.

VICTORIA State Government Australia

Response provided by the Treasurer of Victoria – *continued*

The report acknowledges the Government's achievement of step two by delivering an operating cash surplus in two consecutive years and notes that longer term fiscal sustainability requires close attention and management.

The report makes several recommendations to the Department of Treasury and Finance (DTF), with responses outlined in the table below:

Recommendation	Response
This year's recommendation	
1. Work with the government to: • better articulate its longer-term financial plan that prioritises the management of existing and emerging financial risks • use this long-term plan as a framework to anchor government decision-making in the allocation of public resources, to emphasise alignment with financial and economic strategies • transparently report this plan and ongoing progress against the plan to Parliament and the public, . 2 Enhance their public reporting to demonstrate progress against savings initiatives and efficiency dividends outlined in the state Budgets, and the realisation of their benefits.	**Noted** The five-step fiscal strategy provides a clear anchor for the State's long-term financial plan. DTF continues to work to further strengthen financial performance, accountability and transparency across Government.
Follow-up on prior-year recommendations	
1. Consider why quality issues with information provided by material entities arise and determine whether further training and guidance are required	**Agreed** DTF continues to place considerable effort into providing training and guidance to material entities and the broader public sector, including the provision of technical accounting training and the creation of various system tools and guidance material prior to the provision of information for the Annual Financial Report (AFR). DTF continues to look for further opportunities to provide training and guidance and has recently surveyed public sector entities to capture any feedback on further guidance and support which could be provided for the 2024-25 AFR.

Response provided by the Treasurer of Victoria – *continued*

2. Work with the government to set specific targets and precise timing of achieving its key financial measures and targets of net debt to gross state product and interest expense to revenue. 3. Work with the government to outline its debt management strategy including when and how the state will be able to start to pay down the debt that it has and plans to accumulate.	**Noted** The five-step fiscal strategy provides a clear anchor for the State's long-term financial plan. DTF continues to work to strengthen financial performance, accountability and transparency across Government. DTF continues to provide input for government deliberations and decision-making when setting fiscal strategy, budgets and financial targets.

Finally, I wish to thank you again for the opportunity to comment on the report.

Yours sincerely

[redacted]

Tim Pallas MP
Treasurer
Date: 18/11/2024

VICTORIA
State Government
Australia

Response provided by the Secretary, Department of Premier and Cabinet

Department of
Premier and Cabinet

1 Treasury Place
Melbourne, Victoria 3002 Australia
Telephone: 03 9651 5111
dpc.vic.gov.au

Mr Andrew Greaves
Auditor-General
Victorian Auditor-General's Office
Level 31, 35 Collins Street
MELBOURNE VIC 3000

BSEC-241100154

Dear Auditor-General

Thank you for inviting my comment regarding the recommendation to my department for the Proposed report *Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2023-24*.

The Department of Premier and Cabinet (DPC) accepts the report's recommendation to "undertake a post implementation review of the 2022 machinery-of-government change" as a joint responsibility of DPC and the Department of Treasury and Finance (DTF). My department will work with DTF on this review given their accountability for resource allocations to deliver the policy intent of machinery of government decisions, and its responsibility for the production and upkeep of the *Victorian public sector operating manual on machinery of government changes October 2016*. This work will be progressed during 2025.

I thank the Victorian Auditor-General's Office for their professionalism and collaborative approach to auditing my department's financial performance in accordance with the *Financial Management Act 1994*. This assists the community and Parliament to have confidence in agencies' financial management, and that the information provided to Parliament and the public about the management of finances and resources is clear, accurate and readily understandable.

Yours sincerely

[redacted]

Jeremi Moule
Secretary

..15 /..11 ./2024

VICTORIA State Government

Response provided by the Secretary, Department of Jobs, Skills, Industry and Regions

OFFICIAL

Department of Jobs, Skills, Industry and Regions

GPO Box 4509
Melbourne ,Victoria 3001 Australia
Telephone: +61 3 9651 9999

Ref: CSEC-2-24-25504

Mr Andrew Greaves
Auditor-General
Victorian Auditor-General's Office
Level 31, 35 Collins Street
MELBOURNE VICTORIA 3000

Dear Mr Greaves

PROPOSED REPORT – AUDITOR-GENERAL'S REPORT ON THE ANNUAL FINANCIAL REPORT OF THE STATE OF VICTORIA 2023-24

Thank you for your letter of 31 October 2024 inviting the Department of Jobs, Skills, Industry and Regions (the department) to provide a response to an extract of the Proposed report Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2023–24 (the report).

The department acknowledges the progress as outlined in the report, and notes that it has progressed the previously stated recommendation.

Thank you for the opportunity to comment on the extract of the proposed report.

Yours sincerely

[redacted]

Tim Ada
Secretary

14/11/2024

Response provided by the Secretary, Department of Justice and Community Safety

Department of Justice and Community Safety

Secretary

Level 26
121 Exhibition Street
Melbourne Victoria 3000
Telephone: (03) 9915 3759
www.justice.vic.gov.au

Our ref: 24111066

Mr Andrew Greaves
Auditor-General
Victorian Auditor-General's Office
Level 31, 35 Collins Street
MELBOURNE VIC 3000

Via email: [redacted]

Dear Mr Greaves

Thank you for your letter dated 31 October 2024 regarding your proposed *Report on the Annual Financial Report of the State of Victoria: 2023-24* (Report), and the invitation to provide a formal response.

I note that your proposed Report references the Department of Justice and Community Safety's (the department) reporting relating to distracted driver and seatbelt traffic offence fines introduced in 2023-24.

The department supports the need for good governance and management over all its systems and processes along with the work completed by VAGO in its financial audit to continuously improve governance and management mechanisms.

The department acknowledges the financial audit outcomes, noting that the issues identified have no impact on the legitimate distracted driver and seatbelt infringements approved and issued by Victoria Police throughout 2023-24.

In response to the financial audit outcomes, significant work is underway. The department has put in place measures to ensure annual assurance over the service provider is provided to the department and that they maintain appropriate controls over their systems. The department has also commenced work to implement stronger controls that will be reviewed as part of the 2024-25 financial audit and will ensure these controls continue to operate in compliance with privacy obligations.

As part of the 2023-24 financial audit, the department worked closely with VAGO to address these issues, and I thank your office for its ongoing commitment. The department looks forward to working in collaboration with your office to implement future improvements.

Thank you again for the opportunity to comment on your report.

Yours sincerely

[redacted]

Kate Houghton PSM
Secretary

13/11/2024

cc: [redacted]

Response provided by the Chief Executive, VicTrack

Our Ref: D/24/61159
7 November 2024

[redacted]
Director - Financial Audit
VAGO
Level 31/35 Collins Street
Melbourne VIC
3000

Dear Mr Kumara,

Re: Auditor-General's Report on the *2023-24 Annual Financial Report of the State of Victoria.*

Thank you for the opportunity for Victorian Rail Track (VicTrack) to provide comments to the *Auditor-General's Report on the 2023-24 Annual Financial Report of the State of Victoria*.

VicTrack continues to have a difference of opinion with the Victorian Auditor General's Office (**VAGO**) on the classification of its operating leases, which resulted in the adverse qualification first issued in 2019-20 for VicTrack and its consolidated entities.

VicTrack's position as lessor in relation to these leases as part of the 2023-24 financial statements has been informed by refreshed professional accounting advice and remains unchanged since the initial qualification.

There has been no contractual change in the franchise arrangements at the signing date that allows VicTrack to change this historical classification under the accounting standards.

We note that VicTrack's treatment as lessor is not connected to the position adopted by the Department of Transport and Planning **(DTP)** as lessee, as the adoption of the new Lease accounting standard treats lessor and lessee's differently.

Yours sincerely

[redacted]

Chris Olds
Chief Executive

VicTrack
Level 8, 1010 La Trobe St Docklands VIC 3008
GPO Box 1681 Melbourne VIC 3001
T 1300 VICTRACK (1300 842 872)
victrack.com.au

Appendix B:
Our audit approach

Our financial audits

We conduct our financial audits in accordance with the *Audit Act 1994* and the Australian Auditing Standards.

For each financial report, we evaluate the …	And design and perform audit procedures that …	And form an opinion …
risks of material misstatement – whether due to fraud or error	respond to these material risks	based on audit evidence that is sufficient and appropriate.
internal controls relevant to the audit	are appropriate in the circumstances	on the appropriateness of using the going-concern basis of accounting.
• appropriateness of accounting policies used and the reasonableness of accounting estimates and disclosures • overall presentation, structure and content of the financial report		on whether the report fairly represents the underlying transactions and events.

Our audit of the AFR

As part of our audit of the AFR, we also obtain:

- evidence about the completeness and accuracy of the financial information of the 30 material entities within the AFR
- an understanding of the consolidation process and evaluate the appropriateness, completeness and accuracy of consolidation adjustments, such as intra-agency and intra-sector eliminations.

Our independence

The Auditor-General is:

- an independent officer of the Parliament of Victoria
- appointed under legislation to examine, on behalf of Parliament and taxpayers, how the public sector manages resources
- not subject to control or direction of either Parliament or the government.

Our ethical obligations

The Auditor-General and VAGO must meet the ethical requirements of the:

- Australian Auditing Standards
- Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants*
- *Code of Conduct for Victorian Public Sector Employees of Special Bodies*

- *Public Administration Act 2004*
- *Standing Directions 2018 Under the Financial Management Act 1994*, which provides policies on accepting and provisioning gifts, benefits and hospitality.

Our costs

The cost of ...	Was ...	Which is funded by ...
our audit of the AFR	$423,000	DTF.
our audits of the 30 material entities	approximately $9.6 million	audited agencies.
preparing this report and its supporting dashboard	$395,000	parliamentary appropriation.

We do not provide any non-assurance services to our clients.

Appendix C:

Audit opinion on the AFR

Independent Auditor's Report

VAGO
Victorian Auditor-General's Office

To the Treasurer of the State of Victoria

Opinion	I have audited the consolidated financial report of the State of Victoria (State) and the Victorian General Government Sector (General Government Sector), which comprises the: • consolidated State and General Government Sector balance sheets as at 30 June 2024 • consolidated State and General Government Sector comprehensive operating statements for the year then ended • consolidated State and General Government Sector statements of changes in equity for the year then ended • consolidated State and General Government Sector cash flow statements for the year then ended • notes to the consolidated financial statements, including material accounting policy information • certification by the Treasurer and the Secretary of the Department of Treasury and Finance. In my opinion, the consolidated financial report presents fairly, in all material respects, the financial positions of the State and the General Government Sector as at 30 June 2024 and their financial performance and cash flows for the year then ended in accordance with the financial reporting requirements of Section 24 of the *Financial Management Act 1994* and applicable Australian Accounting Standards.
Basis for opinion	I have conducted my audit in accordance with the *Audit Act 1994*, which incorporates the Australian Auditing Standards. I further describe my responsibilities under that Act and those standards in the *Auditor's responsibilities for the audit of the consolidated financial report* section of my report. My independence is established by the *Constitution Act 1975*. My staff and I are independent of the State and the General Government Sector in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to my audit of the consolidated financial report in Victoria. My staff and I have also fulfilled our other ethical responsibilities in accordance with the Code. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.
Key audit matters	Key audit matters are those matters that, in my professional judgement, were of most significance in my audit of the consolidated financial report of the current period. These matters were addressed in the context of my audit of the consolidated financial report as a whole and in forming my opinion thereon, and I do not provide a separate opinion on these matters.

Level 31 / 35 Collins Street, Melbourne Vic 3000
T 03 8601 7000 enquiries@audit.vic.gov.au www.audit.vic.gov.au

<table>
<tr><th>Key audit matter</th><th>How I addressed the matter</th></tr>
<tr><td colspan="2">Recognition and measurement of transport assets
Refer to Note 4.1 Land, buildings, infrastructure, plant and equipment and Note 7.5 Fair value determination of non-financial assets</td></tr>
<tr><td>Significant spending on capital projects in the transport sector results in large additions to the State's asset base each year.

The State is ultimately responsible for ensuring proper accounts and records are maintained to sufficiently explain the financial impact of these assets on the financial performance and financial position of the State.

I considered this to be a key audit matter because:
transport assets are financially significant
capital projects in the transport sector are complex, and each project results in multiple assets being constructed
a significant degree of management judgement is required to:
determine individual assets within a project
determine which expenses should be capitalised
allocate capital expenses to individual assets
determine the fair value of individual assets.
multiple agencies are involved in the management and delivery of capital projects in the transport sector which makes the timely recognition and derecognition of assets challenging
Victorian Rail Track (VicTrack) is the custodial owner of a large portion of the State's transport assets. Significant asset accounting issues exist at VicTrack.</td><td>My key procedures included:
assessing management's process to identify individual assets within a project, and the costs directly attributable to those assets
assessing the results of the work undertaken by management to review work in progress balances and completed projects capitalised
reviewing management's assessment of the existence of assets, and the completeness and accuracy of asset records
reviewing the accounting treatment for asset additions, disposals and replacements against the requirements of Australian Accounting Standards
assessing the results of fair value assessments, challenging assumptions contained within, and investigating significant variances
assessing the potential impact of identified issues on the consolidated financial statements.</td></tr>
</table>

Key audit matter	How I addressed the matter
Recognition and measurement of service concession assets, liabilities and commitments Refer to Note 4.1 *Land, buildings, infrastructure, plant and equipment*, Note 4.2 *Other non-financial assets,* Note 5.1 *Borrowings*, Note 5.3 *Service concession arrangements* and Note 6.4 *Other liabilities*	

Service concession assets: land, buildings, infrastructure, plant and equipment – $46.8 billion
Service concession assets: intangible produced – $3.5 billion
Service concession arrangement liabilities – $7.5 billion
Service concession arrangements commitments – $52.5 billion (nominal value)
Service concession grant of a right to the operator (GORTO) liabilities – $20.2 billion
There are three types of service concession arrangements:
• arrangements where the State has contractual obligations to make payments and other contributions to the operators for the construction and operation of the assets
• arrangements where the State has granted the operators the right to charge the public directly for the use of the assets
• hybrid arrangements where the State has granted the operators the right to charge the public for use of assets and the State makes contractual payments and other contributions to the operator.
I considered this to be a key audit matter because:
• service concession assets, liabilities and commitments are financially significant
• the requirements of AASB 1059 *Service Concession Arrangements: Grantors* are complex, and their application requires significant management estimation and judgement
• service concession arrangements and the financial models used to value the assets, liabilities and commitments are complex
• a significant degree of management judgement is required to determine the key assumptions used in valuing the assets, liabilities and commitments
• extensive disclosures are required by Australian Accounting Standards which are critical to the users understanding of service concession assets, liabilities and commitments.
	My key procedures included:
	• reviewing material contracts, supporting schedules, financial models and professional accounting advice received by the State, where applicable
	• assessing the accounting treatment against the requirements of AASB 1059, and the reasonableness of management judgements made in the application of the standard
	• engaging appropriately qualified independent subject matter experts to review certain valuation methodologies and financial models and assess the:
	  ○ appropriateness of fair value methodologies
	  ○ reasonableness and consistency of assumptions
	  ○ reasonableness of inputs against underlying data and supporting documentation
	  ○ accuracy of models
	• reviewing all other material financial models and confirming the judgements applied by management to independent expert reports
	• assessing the completeness and accuracy of service concession assets, liabilities and commitments against the contracts and underlying financial models for each project
	• comparing the reasonableness of asset amounts against actual costs incurred
	• assessing the adequacy of financial report disclosures against the requirements of Australian Accounting Standards.

Key audit matter	How I addressed the matter
Valuation of defined benefit superannuation liability Refer to Note 6.5 *Superannuation*	

Defined benefit superannuation liability – $18.2 billion
The Emergency Services and State Super funds account for $17.3 billion (95.2 per cent) of the State's defined benefit superannuation liability (the liability). The Emergency Services Superannuation Board (ESSB) manage these funds.
I considered this to be a key audit matter because:
• the liability is financially significant
• the underlying model used to value the liability is complex
• a significant degree of management judgement is required to determine the method, the model and key assumptions used in valuing the liability
• a small adjustment to an assumption may have a significant effect on the total value of the liability
• ESSB has outsourced core member administration and fund accounting to an outsourced service provider. An independent assurance auditor was engaged by ESSB to report on the design, implementation and operating effectiveness of controls at the service provider
• extensive disclosures are required by Australian Accounting Standards which are critical to the users understanding of the valuation of the liability.
Management engaged an actuary to value the liability as at 30 April, then adjust the value of the liability to account for actual market performance and movements in key assumptions up to 30 June.
	My key procedures included:
	• gaining an understanding of the design and implementation of key controls over the outsourced arrangement, and then testing their operating effectiveness, including those:
	  ○ supporting the completeness and accuracy of membership data
	  ○ assisting with the management and oversight of the arrangement
	• obtaining the independent assurance auditor's report over the outsourced service provider's controls and:
	  ○ assessing the adequacy of the scope of work agreed between management and the assurance auditor
	  ○ assessing the professional competence and independence of the assurance auditor
	  ○ considering the relevance of the stated control objectives and controls covered by the assurance report
	  ○ assessing the testing performed by the assurance auditor and the results of the tests
	  ○ assessing the sufficiency and appropriateness of the audit evidence provided by the assurance report
	• assessing the professional competence and independence of the actuary
	• obtaining the actuarial report and year-end adjustments, and engaging an appropriately qualified independent actuary to assist in obtaining sufficient appropriate audit evidence for the liability and disclosures, including to:
	  ○ assess the appropriateness of the model used to value the liability
	  ○ review the reasonableness of membership data in the model by comparing it to the data in the service provider's system
	  ○ assess the appropriateness of management's selection and application of the method, significant assumptions and data used to value the liability
	  ○ challenge the reasonableness of key assumptions by comparing against accepted industry benchmarks
	  ○ assess the reasonableness of the reported liability value
	• assessing the adequacy of financial report disclosures against the requirements of Australian Accounting Standards.

Key audit matter	How I addressed the matter
Valuation of provision for insurance claims Refer to Note 6.6 *Other provisions*	

Provision for insurance claims – $50.6 billion
I considered this to be a key audit matter because:
• the provision for insurance claims is financially significant
• there are several insurance claim categories at the Victorian WorkCover Authority (WorkSafe), Transport Accident Commission and Victorian Managed Insurance Authority which make up the provision and must be valued
• the underlying models used to value the provision are complex
• the valuation of the provision is subject to significant management assumptions and estimation uncertainty
• a small adjustment to an assumption may have a significant effect on the total value of the provision
• on 31 March 2024, WorkSafe scheme reforms took effect under the *Workplace Injury Rehabilitation and Compensation Amendment (WorkCover Scheme Modernisation) Act 2024* (the Act). These reforms affect the assumptions and judgements made by management, which are essential for accurately valuing the provision
• extensive disclosures are required by Australian Accounting Standards which are critical to the users understanding of the valuation of the provision
• Management of each respective agency engaged actuaries to value the provision as at 30 June.
	My key procedures included:
	• gaining an understanding of the systems, processes and models that affect claims data and the provision valuation
	• testing the operating effectiveness of key controls supporting the underlying claims data used in the models
	• gaining an understanding of the changes to the WorkSafe scheme introduced by the Act and their financial impact
	• assessing the completeness and accuracy of the claims data used in the model by reconciling this data to underlying claims data in the insurers' systems
	• assessing the professional competence and independence of management's actuaries
	• obtaining management's actuarial reports, and engaging an appropriately qualified independent actuary to:
	  ○ assess the appropriateness of management's selection and application of the methods, significant assumptions including those used in applying WorkSafe reforms to value the provision
	  ○ assess the reasonableness of data and other inputs used in valuing the provision
	  ○ evaluate the appropriateness of the models used to value the provision
	  ○ challenge the reasonableness of key assumptions by comparing against claims history and accepted industry benchmarks
	  ○ assess the reasonableness of the reported provision value.
	• assessing the adequacy of financial report disclosures against the requirements of Australian Accounting Standards including disclosures relating to the WorkSafe reforms.

Other information

The Treasurer of Victoria is responsible for the Other Information, which comprises the information in chapters 1–3 and 5 of the 2023–24 Financial Report but does not include the consolidated financial report in chapter 4 and my auditor's report thereon.

My opinion on the consolidated financial report does not cover the Other Information and accordingly, I do not express any form of assurance conclusion on the Other Information. However, in connection with my audit of the consolidated financial report, my responsibility is to read the Other Information and in doing so, consider whether it is materially inconsistent with the consolidated financial report or the knowledge I obtained during the audit, or otherwise appears to be materially misstated. If, based on the work I have performed, I conclude there is a material misstatement of the Other Information, I am required to report that fact. I have nothing to report in this regard.

The Treasurer's responsibilities for the consolidated financial report	The Treasurer of Victoria is responsible for the preparation and fair presentation of the consolidated financial report in accordance with Australian Accounting Standards and the *Financial Management Act 1994*, and for such internal control as the Treasurer determines is necessary to enable the preparation of a consolidated financial report that is free from material misstatement, whether due to fraud or error. In preparing the consolidated financial report, the Treasurer is responsible for assessing the State and the General Government Sector's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless it is inappropriate to do so.
Auditor's responsibilities for the audit of the consolidated financial report	As required by the *Audit Act 1994*, my responsibility is to express an opinion on the consolidated financial report based on the audit. My objectives for the audit are to obtain reasonable assurance about whether the consolidated financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this consolidated financial report. As part of an audit in accordance with the Australian Auditing Standards, I exercise professional judgement and maintain professional scepticism throughout the audit. I also: • identify and assess the risks of material misstatement of the consolidated financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. • obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the State and the General Government Sector's internal control. • evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Treasurer. • conclude on the appropriateness of the Treasurer's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the State and the General Government Sector's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the consolidated financial report or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the State and the General Government Sector to cease to continue as a going concern. • evaluate the overall presentation, structure and content of the consolidated financial report, including the disclosures, and whether the consolidated financial report represents the underlying transactions and events in a manner that achieves fair presentation. • obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the State and the General Government Sector to express an opinion on the consolidated financial report. I remain responsible for the direction, supervision and performance of the audit of the consolidated financial report. I remain solely responsible for my audit opinion.

Auditor's responsibilities for the audit of the consolidated financial report (continued)	I communicate with the Treasurer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit. From the matters communicated with the Treasurer, I determine those matters that were of most significance in the audit of the consolidated financial report of the current period and are therefore key audit matters. I describe these matters in the auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, I determine that a matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

[redacted]

MELBOURNE
2 October 2024

Andrew Greaves
Auditor-General

Appendix D:
Results of material entity audits

Figure D1: Audit opinions issued for material entities

Entity	Benefit	Revenue ($ million)	Expenses ($ million)	Assets ($ million)	Liabilities ($ million)	Financial report certified	Audit opinion issued	Type
General government sector (GGS)								
Department of Education	Controlled	16,555.4	16,374.3	46,842.7	3,336.1	2/9/24	10/9/24	Unmodified
	Administered	5,130.1	5,027.5	59.6	0			
Department of Energy, Environment and Climate Action	Controlled	3,498.0	3,311.2	12,888.4	1,314.0	20/9/24	30/9/24	Unmodified
	Administered	1,684.7	1,744.6	5,083.4	3,193.1			
Department of Government Services	Controlled	799.1	705.6	1,370.2	153.7	24/9/24	2/10/24	Unmodified
	Administered	1,260.7	1,269.2	3,416.7	3,381.1			
Department of Families, Fairness and Housing	Controlled	6,398.0	6,999.7	40,495.4	1,933.1	13/9/24	30/9/24	Unmodified
	Administered	2,948.0	2,946.3	3.6	3.6			
Department of Health	Controlled	19,083.0	18,832.0	8,591.5	4,108.9	5/9/24	12/9/24	Unmodified
	Administered	14,909.5	14,900.2	509.6	509.6			
Department of Jobs, Skills, Industry and Regions	Controlled	3,617.1	3,504.9	1,625.4	771.6	17/9/24	20/9/24	Unmodified
	Administered	68.1	58.6	47.5	0.2			
Department of Justice and Community Safety	Controlled	10,205.5	10,143.4	8,771.2	3,295.1	14/10/24	18/10/24	Qualified
	Administered	1,536.2	978.1	2,529.8	760.7			
Department of Premier and Cabinet	Controlled	482.3	482.7	412.0	112.9	23/9/24	30/9/24	Unmodified
	Administered	20.7	20.7	9.9	10.0			
Department of Transport and Planning	Controlled	9,508.3	9,254.5	149,176.4	18,770.2	18/9/24	19/9/24	Unmodified
	Administered	4,812.6	4,635.1	48,754.5	12,330.1			
Department of Treasury and Finance	Controlled	398.6	398.4	231.6	156.4	23/9/24	30/9/24	Unmodified
	Administered	101,543.4	105,665.2	253,430.6	186,871.6			
Eastern Health	Controlled	1,562.7	1,666.6	1,992.6	595.7	12/9/24	20/9/24	Unmodified
Melbourne Health	Controlled	1,723.6	1,747.1	1,651.4	605.6	13/9/24	23/9/24	Unmodified
Monash Health	Controlled	3,066.5	3,396.3	4,287.2	1,145.6	5/9/24	20/9/24	Unmodified

Entity	Benefit	Revenue ($ million)	Expenses ($ million)	Assets ($ million)	Liabilities ($ million)	Financial report certified	Audit opinion issued	Type
National Gallery of Victoria	Controlled	208.0	147.9	4,826.8	60.8	30/8/24	3/9/24	Unmodified
Office of the Chief Commissioner of Police	Controlled	4,317.2	4,350.2	4,978.0	2,937.3	11/9/24	25/9/24	Unmodified
	Administered	76.7	75.8	74.1	71.5			
Suburban Rail Loop Authority	Controlled	131.4	131.0	2,829.1	203.0	29/9/24	30/9/24	Unmodified
The Royal Children's Hospital	Controlled	1,110.2	1,136.0	2,102.8	1,101.1	23/9/24	24/9/24	Unmodified
Victorian Gambling and Casino Control Commission	Controlled	47.4	47.9	22.0	10.3	11/9/24	17/9/24	Unmodified
	Administered	2,318.2	2,915.7	338.0	1,102.7			
Total GGS*		**219,021.2**	**222,866.7**	**607,352.0**	**248,845.6**			
Public non-financial corporations (PNFCs)								
Goulburn–Murray Rural Water Corporation	Controlled	185.1	281.0	5,260.8	732.9	28/8/24	3/9/24	Unmodified
Greater Western Water	Controlled	993.4	874.4	4,189.8	3,100.2	27/8/24	2/9/24	Unmodified
Melbourne Port Lessor Pty Ltd	Controlled	203.1	122.8	11,219.7	8,238.8	19/9/24	19/9/24	Unmodified
Melbourne Water Corporation	Controlled	2,040.3	1,785.5	18,238.7	10,263.4	30/8/24	13/9/24	Unmodified
North East Link State Tolling Corporation	Controlled	2.4	19.2	4,644.6	4,104.6	18/9/24	20/9/24	Unmodified
South East Water Corporation	Controlled	1,143.4	1,037.0	5,507.5	3,589.1	26/8/24	29/8/24	Unmodified
Victorian Rail Track	Controlled	211.1	1,307.1	48,290.3	3,858.0	5/9/24	12/9/24	Adverse
Yarra Valley Water Corporation	Controlled	1,238.7	1,064.4	6,459.0	4,675.0	27/8/24	9/9/24	Unmodified
Total PNFCs*		**6,017.5**	**6,491.4**	**103,810.4**	**38,562.0**			
Public financial corporations (PFCs)								
Transport Accident Commission	Controlled	4,062.8	2,596.0	20,016.6	18,474.6	29/8/24	6/9/24	Unmodified

Entity	Benefit	Revenue ($ million)	Expenses ($ million)	Assets ($ million)	Liabilities ($ million)	Financial report certified	Audit opinion issued	Type
Treasury Corporation of Victoria	Controlled	172.1	50.0	175,857.2	175,527.8	20/8/24	26/8/24	Unmodified
Victorian Managed Insurance Authority	Controlled	1,021.2	1,119.8	4,376.3	4,853.3	30/8/24	10/9/24	Unmodified
Victorian WorkCover Authority	Controlled	7,564.1	7,051.4	28,930.2	29,800.5	28/8/24	2/9/24	Unmodified
Total PFCs*		**12,820.2**	**10,817.2**	**229,180.3**	**228,656.2**			

Note: *Amounts include transactions between sectors. These transactions are eliminated on consolidation in the AFR.
Source: VAGO.

Appendix E:
VicTrack lease arrangements

Figure E1: Accounting for operational transport assets' lease arrangements

VicTrack is the legal custodian of the state's transport-related assets. It reported $48.1 billion of property, infrastructure, plant and equipment assets at 30 June 2024.

These assets include the operational transport assets, such as land, stations, tracks, rolling stock and signalling systems, that are collectively used to operate the state's transport network.

VicTrack leases all operational transport assets to DTP, which in turn provides train, tram and regional transport operators access to them. The lease between VicTrack and DTP is significantly below market terms and conditions, with only nominal amounts paid to VicTrack.

The table below shows the adopted accounting treatment for VicTrack, DTP and the AFR.

	VicTrack	DTP	AFR
Opinion type	**Adverse**	**Unmodified**	**Unmodified**
Adopted accounting treatment	VicTrack incorrectly recorded the arrangement as an operating lease under AASB 16 *Leases* because it believes it is exposed to substantially all the risks and receives the rewards from owning the assets.	DTP correctly recorded right-of-use assets under AASB 16 *Leases*. DTP disclosed in its financial report that it has the right to direct the use of the leased assets and obtains substantially all the economic benefits from their use.	A central adjustment was made on consolidation in the AFR to correct the inconsistent accounting treatment between DTP (a GGS entity) and VicTrack (a PNFC entity).
Impact	Leased assets and all associated transactions and balances should not have been reported in VicTrack's financial report. Instead, VicTrack should have reported a nominal finance lease receivable.	DTP again availed itself of temporary relief provided by the Australian Accounting Standards to record leases with significantly below-market terms and conditions at cost for 30 June 2024. This meant that for 2023–24, the assets and associated depreciation expenses were not reflected in the GGS*.	The fair value of the underlying assets and all associated transactions and balances were correctly reinstated at the State of Victoria level.

Note: *The Australian Accounting Standards Board has added a narrow-scope project to its work program to consider accounting for right-of-use assets under concessionary leases by not-for-profit entities. If the temporary relief from fair valuing these assets is removed, it is expected that these amounts will be fully reflected in DTP's and the GGS's financial reports. No change to this temporary relief occurred in 2023–24. This will adversely affect their net result from transactions because the depreciation expenses from the assets will also need to be recognised.

Source: VAGO.

Appendix F:
Financial measures and targets

Financial targets becoming more qualitative and less specific

Changes to financial targets during the pandemic

The government has changed its approach to setting measures and what its targets are over the last 10 years. In 2020–21, the government's focus on economic recovery after the COVID-19 pandemic led to the removal of the 'operating surplus' target and the introduction of the 'operating cash surplus' and 'interest expense to revenue' targets.

Targets have become less specific

Figure F1 shows the various measures the government has used and how they vary from specifically quantifiable targets to ones that allow for flexibility in response to economic conditions.

Figure F1: Changes to Victoria's financial targets over the last 12 years

Year	Operating cash surplus	Net debt to GSP	Superannuation liabilities	Interest expense to revenue	Operating surplus	Infrastructure investment
2024–25	A net operating cash surplus consistent with maintaining general government net debt at a sustainable level.	General government net debt as a percentage of GSP to stabilise and reduce in the medium term.	Fully fund the unfunded superannuation liability by 2035.	General government interest expense as a percentage of revenue to stabilise in the medium term.		
2023–24		General government net debt as a percentage of GSP to stabilise in the medium term.				
2022–23	A net operating cash surplus consistent with maintaining general government net debt at a sustainable level after the economy has recovered from the COVID-19 pandemic.					
2021–22						
2020–21						
2019–20		General government net debt as a percentage of GSP to be maintained at a sustainable level over the medium term.			A net operating surplus consistent with maintaining general government net debt at a sustainable level over the medium term.	
2018–19						
2017–18						
2016–17						
2015–16						

Year	Operating cash surplus	Net debt to GSP	Superannuation liabilities	Interest expense to revenue	Operating surplus	Infrastructure investment
2014–15 2013–14		General government net debt reduced as a percentage of GSP over the decade to 2022.			A net operating surplus of at least $100 million and consistent with the infrastructure and debt parameters.	Infrastructure investment of 1.3% of GSP (calculated as a rolling 5-year average).

Source: VAGO, based on the state Budget.

Challenges understanding these targets

Parliamentarians and the community may find it challenging to measure the financial performance of the government when the measures are more qualitative and less specific. Quantitative and specific measures help Parliament and the public hold the government accountable and improve transparency.

Appendix G: Abbreviations, acronyms and glossary

Abbreviations

We use the following abbreviations in this report:

Abbreviation	
VicTrack	Victorian Rail Track
WorkSafe	Victorian WorkCover Authority

Acronyms

We use the following acronyms in this report:

Acronym	
AFR	Annual Financial Report of the State of Victoria
AI	artificial intelligence
BCAP	Business Costs Assistance Program
CFO	chief financial officer
DGS	Department of Government Services
DJSIR	Department of Jobs, Skills, Industry and Regions
DJCS	Department of Justice and Community Safety
DTP	Department of Transport and Planning
DTF	Department of Treasury and Finance
FTE	full-time equivalent
GGS	general government sector
GSP	gross state product
ITE	income tax equivalent
IT	information technology
LHVF	Licensed Hospitality Venue Fund
MoG	machinery of government
PFC	public financial corporation
PNFC	public non-financial corporation
SRL	Suburban Rail Loop
TAC	Transport Accident Commission

Acronym	
TCV	Treasury Corporation of Victoria
TEI	total estimated investment
VAGO	Victorian Auditor-General's Office
VFF	Victorian Future Fund
VPS	Victorian Public Service

Glossary

This glossary explains key terms in this report:

Term	
Accountability	Accountability refers to the responsibility of public sector entities to achieve their objectives in the reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws and reporting to interested parties.
Adverse opinion	We make an adverse opinion when an entity's financial reports are misrepresented, misstated or do not accurately reflect the entity's financial health.
Asset	An asset is an item or resource controlled by an entity that will be used to generate future economic benefits.
Clear audit opinion	A clear audit opinion adds credibility to the financial report by providing reasonable assurance that reported information is reliable and accurate and complies with the requirements of relevant Australian Accounting Standards and applicable legislation.
Fiscal cash surplus/deficit	The cash surplus/deficit is calculated by: • net cashflows received from operating activities, which are the sum of cash received from sources, such as taxes and government grants, offset by cash spent on operating expenses, such as employee costs • plus net cashflows from investment in non-financial assets, being the sum of cash earned from investment activities, such as the sale of land and buildings, offset by cash spent on capital projects • less dividends received from public corporations.
Fiscal strategy	A fiscal strategy is a clear statement of the government's fiscal objectives and targets over a defined period. It sets out the government's short term and long-term fiscal strategies and objectives for managing its finances and existing and emerging risks. It also demonstrates how planned government policies will contribute to fiscal sustainability and macro-economic stability.
Fiscal sustainability	Fiscal sustainability is the ability of the government to maintain public finances at a credible and serviceable position now and into the future. Ensuring long-term fiscal sustainability requires governments to engage in ongoing monitoring and strategic forecasting of future revenue and expenditure, environmental factors and socioeconomic trends to remain financially resilient.
Funding position	Funding position shows the proportion of a superannuation fund's liability covered by the fund's assets. It is a measure of whether the fund has enough assets to pay out future benefits to its members.
Government bond	A government bond is a loan for a specified period with regular interest payments with repayment of face value in full at the maturity.
Insurance funding ratio	Insurance funding ratio is a funding ratio of available assets to estimated liabilities used to monitor the long-term financial sustainability of an insurance scheme.
Intergenerational equity	Intergenerational equity means fairly sharing economic costs and benefits of the government's fiscal policy decisions, such as taxation, public spending and borrowing across different generations.
Intra-sector or intra-entity transactions	Intra-sector or intra-entity transactions are financial transactions that occur between 2 entities in the same sector, or between 2 sectors of government. When an annual financial report is prepared, the accounts are adjusted so these transactions are not counted twice.
Key audit matters	Auditors may include a description of key audit matters in the auditor's report, as described in auditing standard ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*. Key audit matters are determined by the auditor as the matters of most significance to the audit. We voluntarily adopt key audit matter reporting for the AFR and material entities to enhance the value of our

Term	
	audit reports by providing greater transparency and insights about our audit process. Key audit matters are not opinions and are not necessarily adverse findings.
Limited assurance	We obtain less assurance when we rely primarily on an agency's representations and other evidence generated by that agency. However, we aim to have enough confidence in our conclusion for it to be meaningful. We call these types of engagements assurance reviews and typically express our opinions in negative terms. For example, that nothing has come to our attention to indicate there is a problem. See our assurance services fact sheet for more information.
Material	Omissions or misstatements of items are material if they could individually or collectively influence the economic decisions that users make on the basis of the financial report. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.
Material entities	Material entities are the entities that account for most of the state's assets, liabilities, revenue and expenses. In forming our opinion on the AFR, we focus on the financial transactions and balances of these entities.
Net operating balance	Net operating balance is revenue from transactions minus expenses from transactions. It is the part of the change in net worth that can directly be attributed to government policies and is a key measure of GGS financial performance and operating sustainability. It is also known as net result from transactions.
Nominal value	Nominal value is the value measured in terms of absolute money amount without taking inflation or other factors into account.
Off-balance sheet	Off-balance sheet commitments are assets and liabilities that an entity has committed to but not yet included in its balance sheet.
Outstanding insurance claim	An outstanding insurance claim is a claim that the insuring entity is responsible for paying in the future where the claim arises from an event that occurred on or before the valuation date. The liability includes an allowance for claims that have occurred but have not yet been reported to the insuring entity.
Overall public sector	The overall public sector comprises of around 1,750 organisations, including 1,500 schools and 250 entities, such as hospitals, emergency services, water authorities, cemetery trusts, creative industry agencies and sport and recreation organisations. These agencies fall within both the GGS and public corporation sectors.
Public corporations	Public corporations are state-owned entities or statutory authorities established under legislation. They include: • PNFCs that provide a wide range of goods and services while meeting commercial principles through cost recovery via user fees and charges • PFCs that deal with financial aspects of the state. They have the power to borrow, accept deposits and acquire financial assets.
Qualified opinion	We express a qualified opinion when we: • have obtained sufficient evidence that misstatements are material but not pervasive to the financial report • are unable to obtain sufficient evidence that the possible effects of undetected errors could be material but not pervasive to the financial report.
Reasonable assurance	We achieve reasonable assurance by obtaining and verifying direct evidence from a variety of internal and external sources about an agency's performance. This enables us to express an opinion or draw a conclusion against an audit objective with a high level of assurance. We call these audit engagements. See our assurance services fact sheet for more information.

Auditor-General’s reports tabled during 2024–25

Report title	Tabled
Results of 2023 Audits: Technical and Further Education Institutes (2024–25: 1)	July 2024
Building a Capable and High-performing Public Service Workforce (2024–25: 2)	August 2024
Protecting the Biosecurity of Agricultural Plant Species (2024–25: 3)	October 2024
Responses to Performance Engagement Recommendations: Annual Status Update 2024 (2024–25: 4)	October 2024
Auditor-General's Report on the Annual Financial Report of the State of Victoria: 2023–24 (2024–25: 5)	November 2024

All reports are available for download in PDF and HTML format on our website at https://www.audit.vic.gov.au

Our role and contact details

The Auditor-General's role

For information about the Auditor-General's role and VAGO's work, please see our online fact sheet About VAGO.

Our assurance services

Our online fact sheet Our assurance services details the nature and levels of assurance that we provide to Parliament and public sector agencies through our work program.

Contact details

Victorian Auditor-General's Office
Level 31, 35 Collins Street
Melbourne Vic 3000
AUSTRALIA

Phone +61 3 8601 7000
Email enquiries@audit.vic.gov.au