

PART 3: FISCAL OUTLOOK

OVERVIEW

The Australian Government's underlying cash surplus for 2006-07 is estimated to be \$11.8 billion, marginally stronger than the 2006-07 Budget forecast. In accrual terms, a fiscal surplus of \$10.4 billion is estimated for 2006-07. The fiscal outlook is for continuing underlying cash and fiscal surpluses in the forward years.

Table 5: Australian Government general government sector budget aggregates^{(a)(b)}

	Estimates(c)			
	2006-07		2007-08	
	Budget	MYEFO	Budget	MYEFO
Revenue (\$b)	231.7	231.9	240.7	242.7
Per cent of GDP	23.0	22.5	22.9	22.3
Expenses (\$b)	219.7	219.2	230.6	232.3
Per cent of GDP	21.8	21.3	21.9	21.4
Net operating balance (\$b)	11.9	12.7	10.1	10.4
Net capital investment (\$b)	1.6	2.3	0.2	0.5
Fiscal balance (\$b)	10.3	10.4	9.9	9.9
Per cent of GDP	1.0	1.0	0.9	0.9
Underlying cash balance (\$b)(d)	10.8	11.8	10.6	9.7
Per cent of GDP	1.1	1.1	1.0	0.9
<i>Memorandum item:</i>				
Headline cash balance (\$b)	37.5	21.0	10.7	17.6
	Projections			
	2008-09		2009-10	
	Budget	MYEFO	Budget	MYEFO
Revenue (\$b)	252.1	255.6	265.6	268.4
Per cent of GDP	23.0	22.5	23.0	22.7
Expenses (\$b)	240.9	242.5	252.6	252.7
Per cent of GDP	22.0	21.4	21.9	21.4
Net operating balance (\$b)	11.2	13.1	13.0	15.7
Net capital investment (\$b)	0.6	1.2	0.0	1.0
Fiscal balance (\$b)	10.6	11.9	13.0	14.7
Per cent of GDP	1.0	1.0	1.1	1.2
Underlying cash balance (\$b)(d)	11.2	11.8	12.0	14.0
Per cent of GDP	1.0	1.0	1.0	1.2
<i>Memorandum item:</i>				
Headline cash balance (\$b)	11.4	14.6	12.3	14.8

(a) All estimates are based on Government Finance Statistics (GFS) standards, but with goods and services tax (GST) revenue collected on behalf of the States and Territories netted off revenue and expenses.

(b) Budget estimates, including the per cent of GDP, are as published in Budget Paper No. 1, *Budget Strategy and Outlook 2006-07*.

(c) For the 2006-07 MYEFO, 2007-08 has moved from a projection to an estimates year.

(d) Excludes expected Future Fund earnings.

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Table 6 provides a reconciliation of the fiscal balance estimates between the 2006-07 Budget and the *Mid-Year Economic and Fiscal Outlook 2006-07* (MYEFO).

Table 6: Reconciliation of general government fiscal balance estimates^(a)

	Estimates		Projections	
	2006-07	2007-08	2008-09	2009-10
	\$m	\$m	\$m	\$m
2006-07 Budget fiscal balance	10,290	9,940	10,566	12,972
Per cent of GDP	1.0	0.9	1.0	1.1
Changes between 2006-07 Budget and MYEFO				
Effect of policy decisions ^(b)				
Revenue	-202	-1,609	-1,608	-1,753
Expenses	1,969	3,648	2,986	2,868
Net capital investment	159	134	106	307
Total policy decisions impact on fiscal balance	-2,330	-5,392	-4,700	-4,928
Effect of parameter and other variations				
Revenue	424	3,664	5,131	4,532
Expenses	-2,524	-1,883	-1,403	-2,792
Net capital investment	489	169	507	641
Total parameter and other variations impact on fiscal balance	2,459	5,378	6,028	6,683
2006-07 MYEFO fiscal balance	10,420	9,926	11,893	14,728
Per cent of GDP	1.0	0.9	1.0	1.2

(a) A positive number for revenue indicates an increase in the fiscal balance, while a positive number for expenses and net capital investment indicates a decrease in the fiscal balance.

(b) Excludes the public debt net interest effect of policy measures.

REVENUE

Total accrual revenue in 2006-07 is expected to be \$223 million higher than forecast at the 2006-07 Budget, comprising an additional \$323 million in non-tax revenue and a decrease of \$101 million in tax revenue.

The revised tax revenue estimates are driven by the flow on effects of a lower than expected revenue outcome in 2005-06 and downward revisions to expected revenue from capital gains from investors and petroleum resource rent tax, broadly offset by higher than expected revenue from higher forecasts of nominal economic growth in 2006-07.

Policy decisions since Budget have reduced revenue by \$202 million in 2006-07.

The Government announced details of the Simplified Superannuation package on 5 September 2006. This package will cost \$3.9 billion in revenue over the forward estimates. The revenue estimates in the 2006-07 Budget included an allowance for the package. The final package has now been incorporated into the estimates as a measure.

Other major policy measures reducing revenue over the four year period 2006-07 to 2009-10 include:

- \$53 million in 2006-07 (\$218 million over four years) owing to a decision to not proceed with planned increases in diesel excise and customs duty rates; and
- \$50 million in 2006-07 (\$350 million over four years) from an amendment to the investment rules for superannuation funds investing in instalment warrants.

A full list of revenue measures announced since the 2006-07 Budget is provided at Appendix A.

Detailed Australian Government general government sector revenue estimates for 2006-07, compared with the estimates published in the 2006-07 Budget, are provided in Table 7. Detailed cash estimates are in Table 12.

Table 7: Australian Government general government sector revenue

	2006-07			
	Budget \$m	MYEFO \$m	Change on Budget \$m	%
<i>Income taxation</i>				
Individuals and other withholding taxes(a)				
Gross income tax withholding	104,010	105,580	1,570	1.5
Gross other individuals	28,480	27,350	-1,130	-4.0
less: Refunds	16,790	16,790	0	0.0
Total individuals and other withholding taxation	115,700	116,140	440	0.4
Fringe benefits tax	3,720	3,730	10	0.3
Superannuation funds				
Contributions and earnings	5,890	6,450	560	9.5
Superannuation surcharge	680	520	-160	-23.5
Total superannuation taxation	6,570	6,970	400	6.1
Company tax	56,860	56,750	-110	-0.2
Petroleum resource rent tax	2,490	1,750	-740	-29.7
Income taxation revenue	185,340	185,340	0	0.0
<i>Excise and customs</i>				
Excise duty				
Petrol	7,310	7,110	-200	-2.7
Diesel	6,420	6,280	-140	-2.2
Other fuel products	450	610	160	35.6
Crude oil	470	580	110	23.4
Beer	1,760	1,780	20	1.1
Potable spirits	890	870	-20	-2.2
Tobacco	5,320	5,370	50	0.9
Total excise duty revenue	22,620	22,600	-20	-0.1
Customs duty				
Textiles, clothing and footwear	870	860	-10	-1.1
Passenger motor vehicles	1,300	1,140	-160	-12.3
Excise-like goods	2,160	2,170	10	0.5
Other imports	1,608	1,570	-38	-2.4
less: Refunds and drawbacks	300	230	-70	-23.3
Total customs duty revenue	5,638	5,510	-128	-2.3
Excise and customs revenue	28,258	28,110	-148	-0.5
<i>Other taxation</i>				
Wine equalisation tax	660	670	10	1.5
Luxury car tax	320	330	10	3.1
Agricultural levies	619	585	-34	-5.4
Other taxes	1,960	2,021	61	3.1
Other taxation revenue	3,559	3,606	47	1.3
Taxation revenue	217,157	217,056	-101	0.0
<i>Non-taxation</i>				
Sales of goods and services	4,846	4,984	138	2.8
Dividends	2,701	2,860	159	5.9
Interest received	3,717	3,581	-136	-3.7
Other non-taxation revenue	3,241	3,404	163	5.0
Non-taxation revenue	14,505	14,828	323	2.2
Total revenue	231,662	231,885	223	0.1

(a) The MYEFO estimate includes Medicare levy revenue of \$7,090 million in 2006-07.

The revenue estimates for 2006-07 and 2007-08 are constructed using the outcomes for 2005-06, information on revenue collections in the year to date and the revised economic forecasts for 2006-07 and 2007-08. Revenue estimates for the projection years – 2008-09 and 2009-10 – are based mainly on underlying trends in economic parameters and take no account of cyclical influences on economic activity. As at the 2006-07 Budget, key commodity prices are assumed to return to their long-run average level over the two projection years.

Total taxation revenue for 2006-07 is expected to be \$101 million lower than forecast at the 2006-07 Budget. Lower than expected revenue outcomes in 2005-06 for company tax and other individuals and downward revisions to expected revenue from capital gains and petroleum resource rent tax in 2006-07 are expected to be broadly offset by the effects of stronger than expected employment growth.

Estimated revenue from gross income tax withholding for 2006-07 has increased by \$1.6 billion since the 2006-07 Budget, in line with stronger than expected employment outcomes.

Superannuation contributions and earnings tax revenue has been revised up by \$560 million in 2006-07, in the light of the increased strength in the labour market and more buoyant conditions for superannuation fund earnings.

Company tax revenue in 2006-07 is expected to be \$110 million lower than the 2006-07 Budget estimate, reflecting a lower than expected outcome in 2005-06, partly offset by an increase in expected profits for 2006-07.

Expected gross revenue from other individuals tax has been revised down by \$1.1 billion in 2006-07, driven by a lower than expected outcome in 2005-06 and lower than expected growth in realised capital gains from investors.

Petroleum resource rent tax has been revised down by \$740 million in 2006-07 since the 2006-07 Budget, in the light of lower oil prices, higher than expected deductible costs – including wages and exploration – and lower than expected production.

Expected revenue from all other taxation in 2006-07 is broadly unchanged from Budget.

Non-taxation revenue in 2006-07 is expected to be \$323 million higher than the 2006-07 Budget estimate due in part from an increase in sales of goods and services by the Department of Defence.

EXPENSES

Estimated accrual expenses in 2006-07 have decreased by \$554 million since the 2006-07 Budget. This reflects a net decrease of \$2.5 billion due to parameter and other variations, partially offset by new policy measures of \$2.0 billion in 2006-07.

Table 8: Reconciliation of general government sector expense estimates

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
2006-07 Budget expenses	219,730	230,556	240,910	252,592
Changes between 2006-07 Budget and MYEFO				
Effect of policy decisions(a)	1,969	3,648	2,986	2,868
Effect of economic parameter variations				
Unemployment benefits	-507	-348	-382	-503
Prices and wages	-235	542	874	691
Interest and exchange rates	-60	-50	-94	-48
<i>Total economic parameter variations</i>	<i>-802</i>	<i>144</i>	<i>398</i>	<i>139</i>
Public debt interest	103	47	44	51
Programme specific parameter variations	-1,085	-1,309	-1,510	-1,717
Slippage in 2006-07 Budget decisions	0	0	0	0
Other variations(b)	-740	-764	-335	-1,264
Total variations	-554	1,766	1,583	76
2006-07 MYEFO expenses	219,175	232,322	242,493	252,669

(a) Excludes the public debt net interest effect of policy measures.

(b) The contingency reserve includes an allowance for the established tendency of existing government policy (particularly demand driven programmes) to be higher than estimated in the forward years. This allowance, known as the conservative bias allowance, is progressively reduced so that the budget year conservative bias is zero by the budget. As is standard practice, the conservative bias has been reduced at this MYEFO in the forward years from 2007-08 onwards.

Policy decisions announced since the 2006-07 Budget increase estimated expenses by \$2.0 billion in 2006-07 and include:

- \$522 million in 2006-07 (\$1.1 billion over three years) in funding for drought relief, including income support and interest rate subsidies to assist farmers and small businesses most affected by the drought;
- \$225 million in 2006-07 (\$1.3 billion over four years) for new and expanded listings on the Pharmaceutical Benefit Scheme (PBS), including Herceptin® for the treatment of early stage breast cancer (\$120 million in 2006-07);
- \$94 million in 2006-07 (\$1.1 billion over nine years) for Energy Initiatives that will provide cheaper fuel options through LPG excise concessions and further develop energy resources through investment in alternative fuels;

- \$82 million in 2006-07 (\$492 million over four years) to increase payments to healthcare providers treating veterans under the Gold Card and White Card arrangements;
- \$50 million in 2006-07 (\$473 million over five years) on measures to improve the retention and recruitment of Australian Defence Force personnel; and
- \$46 million in 2006-07 (\$3.4 billion over 11 years) for the establishment of the first of two light infantry battalions. A provision for the second battalion has been included in the Contingency Reserve.

A full list of expense measures announced since the 2006-07 Budget is provided at Appendix A.

Since the 2006-07 Budget, parameter and other variations have reduced estimated expenses by \$2.5 billion in 2006-07. This includes:

- a \$390 million reduction in expenses as a result of delays to defence acquisition projects. This reduction is offset by increased expenses in 2007-08 and 2008-09;
- a \$270 million reduction in expenses for the Pharmaceutical Benefits Scheme due to lower than expected expenditure against a number of drug groups (primarily chemotherapy, cholesterol lowering agents and blood pressure drugs);
- a \$214 million reduction in Newstart Allowance expenses as a result of a fall in the forecast number of unemployment benefit recipients reflecting improved labour market conditions;
- a \$192 million reduction in annual supplementary funding for government and non-government schools grants. This is due to a lower than anticipated increase in State and Territory expenditure on government schools, which is used to index the level of Australian Government funding each year;
- a \$151 million reduction in Disability Support Pension expenses primarily due to lower than expected customer numbers to date in 2006-07 based on trends over the previous two years;
- a \$127 million reduction in Job Network expenses resulting from a reduction in the estimate of Job Network provider activity for the remainder of the year; and
- a reduction in expense estimates following the inclusion of the provision for underspends in 2006-07. A provision is included each year at the MYEFO update to provide for the established tendency of departments and agencies to underspend their budgets in the current financial year.

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These reductions in expenses are partially offset by:

- a \$132 million increase in Defence expenses as a result of an increase in the non-farm GDP deflator, which is used to index Defence operating expenses;
- an \$80 million increase in Medicare Services expenses due to higher than expected expenditure across a range of medical services provided by General Practitioners and specialists; and
- a \$75 million increase in expenses in 2006-07 for Australian Technical Colleges reflecting the reprofiling of funds from future programme years. A major proportion of the increased expenses reflects the earlier than anticipated establishment of some colleges.

NET CAPITAL INVESTMENT

Estimated net capital investment in 2006-07 has increased by \$648 million since the 2006-07 Budget, partially reflecting new policy decisions of \$159 million, including:

- \$60 million in 2006-07 for additional construction costs at the Christmas Island Immigration Reception and Processing Centre;
- \$23 million (\$30 million over three years) to improve the capacity of the Australian Federal Police's International Deployment Group to respond to current and anticipated peace-keeping, peace restoration and capacity-building requirements;
- \$17 million (\$22 million over two years) to build a new system interface between the Department of Families, Community Services and Indigenous Affairs, Centrelink, and child care service providers to enable a more timely transfer of Child Care Benefit data; and
- \$11 million for the Australian Taxation Office to establish information technology systems to implement the Simplified Superannuation reforms (\$52 million over three years).

Table 9: Reconciliation of general government sector net capital investment estimates^(a)

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
2006-07 Budget net capital investment	1,642	174	602	38
Changes between 2006-07 Budget and MYEFO				
Effect of policy decisions(b)	159	134	106	307
Effect of parameter and other variations	489	169	507	641
Total variations	648	304	612	948
2006-07 MYEFO net capital investment	2,290	478	1,215	986

(a) Net capital investment is defined as net acquisition of non-financial assets.

(b) Excludes the public debt net interest affect of policy measures.

CASH FLOWS

In 2006-07, the underlying cash balance is expected to be a surplus of \$11.8 billion compared to an estimate of \$10.8 billion at the 2006-07 Budget.

Detailed Australian Government general government sector receipt estimates for 2006-07, compared with the estimates published in the 2006-07 Budget, are provided in Table 12.

Table 10: Summary of Australian Government general government sector cash flows (\$b)^(a)

	Estimates			
	2006-07		2007-08	
	Budget	MYEFO	Budget	MYEFO
Cash receipts				
Operating cash receipts	230.7	231.4	239.3	241.4
Capital cash receipts(b)	0.2	0.2	0.2	0.3
Total cash receipts	230.8	231.6	239.5	241.7
Cash payments				
Operating cash payments	214.7	213.6	224.2	225.9
Capital cash payments(c)	3.5	4.0	2.7	3.0
Total cash payments	218.2	217.6	226.9	229.0
Finance leases and similar arrangements(d)	0.0	0.0	0.0	0.0
GFS cash surplus(+)/deficit(-)	12.6	14.0	12.6	12.7
Per cent of GDP	1.2	1.4	1.2	1.2
less Future Fund earnings	1.8	2.2	2.0	3.1
Underlying cash balance(e)	10.8	11.8	10.6	9.7
Per cent of GDP	1.1	1.1	1.0	0.9
<i>Memorandum items:</i>				
Net cash flows from investments in financial assets for policy purposes(f)	24.9	7.0	-1.9	4.9
plus Future Fund earnings(g)	1.8	2.2	2.0	3.1
Headline cash balance	37.5	21.0	10.7	17.6
	Projections			
	2008-09		2009-10	
	Budget	MYEFO	Budget	MYEFO
Cash receipts				
Operating cash receipts	250.5	253.8	263.9	267.0
Capital cash receipts(b)	0.2	0.1	0.1	0.1
Total cash receipts	250.7	254.0	264.0	267.1
Cash payments				
Operating cash payments	234.2	235.9	247.1	247.0
Capital cash payments(c)	2.8	3.0	2.6	3.3
Total cash payments	237.0	238.8	249.7	250.3
Finance leases and similar arrangements(d)	-0.3	-0.6	0.0	0.0
GFS cash surplus(+)/deficit(-)	13.3	14.6	14.3	16.8
Per cent of GDP	1.2	1.3	1.2	1.4
less Future Fund earnings	2.1	2.8	2.3	2.8
Underlying cash balance(e)	11.2	11.8	12.0	14.0
Per cent of GDP	1.0	1.0	1.0	1.2
<i>Memorandum items:</i>				
Net cash flows from investments in financial assets for policy purposes(f)	-2.0	0.0	-2.0	-2.0
plus Future Fund earnings (g)	2.1	2.8	2.3	2.8
Headline cash balance	11.4	14.6	12.3	14.8

(a) Cash flows are derived from the accrual GFS framework excluding GST.

(b) Equivalent to cash receipts from the sale of non-financial assets in the GFS cash flow statement.

(c) Equivalent to cash payments for purchases of new and second-hand non-financial assets in the GFS cash flow statement.

(d) The acquisition of assets under finance leases decreases the underlying cash balance. The disposal of assets previously held under finance leases increases the underlying cash balance.

(e) Excludes expected Future Fund earnings.

(f) Under the cash budgeting framework, these cash flows were referred to as net advances.

(g) The earnings include the gross proceeds from the sale of Telstra to be transferred to the Future Fund. The Future Fund (excluding Telstra shares) is assumed to earn a rate of return initially equal to the yield on other term deposits held by the Australian Government then increasing to a rate consistent with the benchmark return specified in the Australian Government's investment mandate.

Major new policy decisions and parameter and other variations since the 2006-07 Budget have largely had the same impact on the 2006-07 underlying cash balance as the fiscal balance.

Table 11 provides a reconciliation of the variations in the underlying cash balance estimates.

Table 11: Reconciliation of Australian Government general government sector underlying cash balance estimates

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
2006-07 Budget underlying cash balance	10,828	10,628	11,225	12,019
Changes from 2006-07 Budget to MYEFO				
Effect of policy decisions(a)	-2,317	-5,455	-4,712	-5,010
Effect of parameter and other variations	3,316	4,489	5,331	6,987
Total variations	999	-966	618	1,977
2006-07 MYEFO underlying cash balance(b)	11,827	9,662	11,844	13,997

(a) Excludes the public debt net interest effect of policy measures.

(b) Excludes expected Future Fund earnings.

Total receipts in 2006-07 are expected to be \$763 million higher than forecast at the 2006-07 Budget, comprising \$591 million in non-tax receipts and \$172 million in tax receipts. Similarly to the revisions to the revenue estimates, the revisions to tax receipts are driven by the flow on effects of a lower than expected outcome in 2005-06, broadly offset by higher than expected tax receipts due to an upward revision to nominal economic growth forecasts.

Table 12: Australian Government general government sector receipts

	2006-07			
	Budget \$m	MYEFO \$m	Change on Budget \$m	%
<i>Income taxation</i>				
Individuals and other withholding taxes(a)				
Gross income tax withholding	103,420	104,830	1,410	1.4
Gross other individuals	26,810	26,260	-550	-2.1
less: Refunds	16,790	16,790	0	0.0
Total individuals and other withholding taxation	113,440	114,300	860	0.8
Fringe benefits tax	3,690	3,800	110	3.0
Superannuation funds				
Contributions and earnings	5,840	6,400	560	9.6
Superannuation surcharge	650	710	60	9.2
Total superannuation taxation	6,490	7,110	620	9.6
Company tax	56,130	55,770	-360	-0.6
Petroleum resource rent tax	2,490	1,560	-930	-37.3
Income taxation receipts	182,240	182,540	300	0.2
<i>Excise and customs</i>				
Excise duty				
Petrol	7,310	7,100	-210	-2.9
Diesel	6,420	6,280	-140	-2.2
Other fuel products	450	610	160	35.6
Crude oil	470	580	110	23.4
Beer	1,760	1,780	20	1.1
Potable spirits	890	870	-20	-2.2
Tobacco	5,320	5,370	50	0.9
Total excise duty receipts	22,620	22,590	-30	-0.1
Customs duty				
Textiles, clothing and footwear	870	860	-10	-1.1
Passenger motor vehicles	700	680	-20	-2.9
Excise-like goods	2,160	2,170	10	0.5
Other imports	1,600	1,550	-50	-3.1
less: Refunds and drawbacks	300	370	70	23.3
Total customs duty receipts	5,030	4,890	-140	-2.8
Excise and customs receipts	27,650	27,480	-170	-0.6
<i>Other taxation</i>				
Wine equalisation tax	660	660	0	0.0
Luxury car tax	320	320	0	0.0
Agricultural levies	619	585	-33	-5.4
Other taxes	1,700	1,775	75	4.4
Other taxation receipts	3,298	3,340	42	1.3
Taxation receipts	213,188	213,360	172	0.1
<i>Non-taxation</i>				
Sales of goods and services	5,008	5,280	272	5.4
Dividends	3,000	3,170	170	5.7
Interest received	3,498	3,477	-21	-0.6
Other non-taxation receipts	6,124	6,295	170	2.8
Non-taxation receipts	17,631	18,222	591	3.4
Total receipts	230,819	231,582	763	0.3

(a) The MYEFO estimate includes Medicare levy receipts of \$7,090 million in 2006-07.

NET DEBT AND NET WORTH

Net debt was eliminated in 2005-06, falling from a peak of 18.5 per cent of GDP in 1995-96. Since the 2006-07 Budget, the forecast level of net debt has fallen from -\$22.1 billion to -\$28.1 billion.

The estimates of net debt have changed since the 2006-07 Budget primarily as a result of changes to the technical assumptions regarding the expected financial asset composition of the Future Fund. These assumptions are for estimates purposes only and are not intended as a guide for the Future Fund Board of Guardians in finalising its investment strategy for the Fund. The net debt projections are therefore sensitive to the actual asset composition of the Fund.

As a result of the lower level of net debt, net interest payments will continue to fall in 2006-07 and beyond. Having peaked at \$8.4 billion in 1996-97, net interest payments are expected to fall to \$0.5 billion in 2006-07.

Australian Government general government sector net worth is expected to be -\$11.9 billion in 2006-07 compared with -\$12.0 billion at the 2006-07 Budget. Net worth over the forward estimates is expected to improve and, for the first time, is projected to be positive in 2008-09.

Table 13: Australian Government general government sector net worth, net debt and net interest payments

	Estimates			
	2006-07		2007-08	
	Budget	MYEFO	Budget	MYEFO
Financial assets (\$b)	147.1	149.2	163.0	164.1
Non-financial assets (\$b)	45.5	47.6	45.6	48.0
Total assets (\$b)	192.6	196.8	208.6	212.1
Total liabilities (\$b)	204.6	208.7	210.9	214.7
Net worth (\$b)	-12.0	-11.9	-2.3	-2.6
Net debt (\$b)(a)(b)	-22.1	-28.1	-24.7	-11.0
Per cent of GDP	-2.2	-2.7	-2.4	-1.0
Net interest payments (\$b)	0.5	0.5	0.3	0.0
Per cent of GDP	0.0	0.0	0.0	0.0
	Projections			
	2008-09		2009-10	
	Budget	MYEFO	Budget	MYEFO
Financial assets (\$b)	178.3	182.3	194.5	200.8
Non-financial assets (\$b)	46.2	49.3	46.3	50.3
Total assets (\$b)	224.5	231.6	240.8	251.1
Total liabilities (\$b)	215.7	219.6	219.1	223.1
Net worth (\$b)	8.8	12.0	21.6	28.0
Net debt (\$b)(a)(b)	-37.1	-26.6	-50.2	-42.3
Per cent of GDP	-3.4	-2.3	-4.3	-3.6
Net interest payments (\$b)	-0.2	0.2	-0.9	-0.8
Per cent of GDP	0.0	0.0	-0.1	-0.1

- (a) Net debt equals the sum of deposits held, advances received, government securities, loans and other borrowing, minus the sum of cash and deposits, advances paid and investments, loans and placements.
- (b) Includes the impact of the partial sale of the Australian Government's holding in Telstra and transfer of the Australian Government's remaining shares to the Future Fund. It is assumed that the Future Fund will increasingly be invested in equities until it reaches a portfolio equity allocation consistent with the benchmark return specified in the Australian Government's investment mandate.

REPORTING STANDARDS

The *Charter of Budget Honesty Act 1998* requires that the Mid-Year Economic and Fiscal Outlook (MYEFO) be based on external reporting standards, and that departures from applicable external reporting standards be identified.

The major external standards used for MYEFO reporting purposes are:

- the Australian Bureau of Statistics' (ABS) accrual Government Finance Statistics (GFS) publication, *Australian System of Government Finance Statistics: Concepts, Sources and Methods* cat. no. 5514.0, which in turn is based on the International Monetary Fund (IMF) accrual GFS framework; and
- Australian Accounting Standards (AAS), being the Australian Equivalents to International Financial Reporting Standards (AEIFRS) and AAS 31 *Financial Reporting by Governments*.

The MYEFO tables, with the exception of tables in Appendix B, do not include goods and services tax (GST) collections and equivalent payments to the States and Territories (the States). Under the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*, all GST receipts are appropriated to the States and thus are not available for expenditure by the Australian Government. Because the Australian Taxation Office collects GST as an agent for the States, GST receipts are not shown as Australian Government revenue. Estimates of GST receipts are provided in Table E2 of Appendix E.

ABS GFS requires that provisions for bad and doubtful debts be excluded from the balance sheet. This treatment has not been adopted because excluding such provisions would overstate the value of Australian Government assets in the balance sheet (and would, therefore, be inconsistent with the market valuation principle).

The AAS financial statements currently record IMF Special Drawing Rights (SDRs) as a liability. This is consistent with AAS. The GFS statements also record SDRs as a liability. However, in accordance with the IMF's GFS manual, IMF SDRs are not treated as a liability in ABS GFS although IMF treats them this way in some of its other documentation. As the statistical standard underpinning the GFS manual (the System of National Accounts 1993) is currently being updated and includes a proposal to treat SDRs as a liability, the current approach will remain in place at least until this update is finalised.

The GFS financial statements currently adopt the AAS treatment for circulating coins. Under this treatment revenue is recognised upon the issue of coins and no liability is recorded, as there is no legal obligation requiring coins on issue to be repurchased by

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the Australian Government. However, in ABS GFS, coins on issue are treated as a liability and no revenue is recognised. The treatment of coins on issue is listed for clarification as part of the update of the statistical standard referred to above and the current treatment will remain in place at least until the update is finalised.

Similarly, the GFS financial statements currently record education grants on the same basis as the AAS statements. Under this treatment the Australian Government's obligation to the States is recognised upon the annual Ministerial determination, usually occurring at the beginning of each funding year. However, in accordance with the latest guidance issued by the ABS, ABS GFS now recognises the obligation later in the year as monies are transferred to each State and Territory.

ABS GFS also requires defence weapons be treated as expenses. Defence weapons inventories are recorded as capital investment rather than expenses until such inventories can be reliably identified and measured. This treatment does not affect the underlying cash and fiscal balances.

Additional information on the reporting standards and budget concepts is provided in Appendix E.

BUDGET FINANCIAL STATEMENTS

The budget financial statements consist of an operating statement, balance sheet, cash flow statement and statement of other economic flows (reconciliation of net worth) for the Australian Government general government sector. The budget financial statements are based on GFS standards with the exception of the divergences discussed in Attachment A.

Table 14: Australian Government general government sector operating statement

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
Revenue				
Taxation revenue	217,056	227,555	240,123	251,922
Current grants and subsidies	0	0	0	0
Sales of goods and services	4,984	5,003	5,138	5,291
Interest income	3,581	3,896	3,648	4,584
Dividend income	2,860	2,812	3,343	3,338
Other	3,404	3,461	3,350	3,247
Total revenue	231,885	242,726	255,601	268,383
Expenses				
Gross operating expenses				
Depreciation	2,228	2,417	2,513	2,550
Superannuation	2,526	2,576	2,667	2,735
Salaries and wages	13,744	14,062	14,098	14,382
Payment for supply of goods and services	53,344	56,083	57,430	59,422
Other operating expenses	2,990	3,098	3,266	3,367
<i>Total gross operating expenses</i>	<i>74,832</i>	<i>78,236</i>	<i>79,973</i>	<i>82,455</i>
Nominal superannuation interest expense	5,725	5,869	6,163	6,371
Other interest expenses	3,996	3,862	3,712	3,674
Other property expenses	0	0	0	0
Current transfers				
Grant expenses	41,486	45,011	46,011	47,302
Subsidy expenses	7,326	7,795	8,281	8,214
Personal benefit payments in cash	80,830	86,203	92,665	99,883
Other current transfers	0	0	0	0
<i>Total current transfers</i>	<i>129,643</i>	<i>139,009</i>	<i>146,957</i>	<i>155,398</i>
Capital transfers	4,979	5,345	5,688	4,770
Total expenses	219,175	232,322	242,493	252,669
Net operating balance	12,709	10,404	13,108	15,714
Net acquisition of non-financial assets				
Purchases of non-financial assets	3,762	3,021	3,459	3,146
<i>less</i> Sales of non-financial assets	<i>184</i>	<i>255</i>	<i>143</i>	<i>72</i>
<i>less</i> Depreciation	<i>2,228</i>	<i>2,417</i>	<i>2,513</i>	<i>2,550</i>
<i>plus</i> Change in inventories	<i>680</i>	<i>129</i>	<i>344</i>	<i>338</i>
<i>plus</i> Other movements in non-financial assets	<i>259</i>	<i>0</i>	<i>67</i>	<i>124</i>
Total net acquisition of non-financial assets	2,290	478	1,215	986
Net lending/fiscal balance(a)	10,420	9,926	11,893	14,728

(a) The term fiscal balance is not used by the ABS.

Table 15: Australian Government general government sector balance sheet

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
Assets				
Financial assets				
Cash and deposits	2,014	2,244	2,029	1,993
Advances paid	22,775	24,543	26,350	27,964
Investments, loans and placements	67,316	50,159	64,294	77,596
Other non-equity assets	26,988	20,318	20,577	21,217
Equity(a)	30,063	66,841	69,075	72,073
<i>Total financial assets</i>	<i>149,156</i>	<i>164,104</i>	<i>182,325</i>	<i>200,843</i>
Non-financial assets				
Land	6,172	6,244	6,314	6,274
Buildings	15,070	15,370	15,969	16,324
Plant, equipment and infrastructure	9,609	9,741	9,983	10,209
Inventories	5,588	5,717	6,060	6,399
Heritage and cultural assets	7,702	7,715	7,725	7,741
Other non-financial assets	3,478	3,246	3,221	3,316
<i>Total non-financial assets</i>	<i>47,619</i>	<i>48,034</i>	<i>49,273</i>	<i>50,263</i>
Total assets	196,775	212,138	231,598	251,106
Liabilities				
Deposits held	300	300	300	300
Advances received	0	0	0	0
Government securities	57,923	59,842	59,984	59,260
Loans	5,381	5,406	5,099	5,094
Other borrowing	420	390	664	625
Superannuation liability	101,300	104,741	108,314	111,928
Other employee entitlements and provisions	8,171	8,390	8,708	9,068
Other non-equity liabilities	35,213	35,673	36,539	36,835
Total liabilities	208,709	214,743	219,608	223,110
Net worth(b)	-11,934	-2,605	11,989	27,996
Net debt(c)(d)	-28,081	-11,007	-26,626	-42,274

(a) Equity includes equity holdings of the Future Fund.

(b) Net worth is calculated as total assets minus total liabilities.

(c) Net debt equals the sum of deposits held, advances received, government securities, loans and other borrowing, minus the sum of cash and deposits, advances paid and investments, loans and placements.

(d) Includes the impact of the partial sale of the Government's holding in Telstra and transfer of the Government's remaining shares to the Future Fund. It is assumed that the Future Fund will increasingly be invested in equities until it reaches a portfolio equity allocation consistent with the benchmark return (excluding Telstra shares) specified in the Government's investment mandate.

Table 16: Australian Government general government sector cash flow statement^(a)

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
Cash receipts from operating activities				
Taxes received	213,360	223,528	235,599	247,778
Receipts from sales of goods and services	5,280	5,238	5,392	5,517
Grants and subsidies received	0	0	0	0
Interest receipts	3,477	3,664	3,402	4,326
Dividends	3,170	2,782	3,343	3,338
GST input credits received by general government	3,027	2,988	2,996	3,058
Other receipts	3,083	3,240	3,114	2,987
Total operating receipts	231,397	241,440	253,846	267,004
Cash payments for operating activities				
Payments for goods and services	-57,026	-59,840	-61,260	-63,313
Grants and subsidies paid	-51,638	-55,549	-56,593	-57,889
Interest paid	-3,948	-3,615	-3,560	-3,480
Personal benefit payments	-79,735	-85,287	-92,000	-99,370
Salaries, wages and other entitlements	-18,400	-18,996	-19,235	-19,693
GST payments by general government to taxation authority	-79	-81	-82	-85
Other payments for operating activities	-2,761	-2,572	-3,136	-3,153
Total operating payments	-213,586	-225,941	-235,866	-246,982
Net cash flows from operating activities	17,811	15,499	17,980	20,022
Cash flows from investments in non-financial assets				
Sales of non-financial assets	185	267	147	77
Purchases of non-financial assets	-3,967	-3,046	-2,977	-3,302
Net cash flows from investments in non-financial assets	-3,782	-2,779	-2,830	-3,226
Net cash flows from investments in financial assets for policy purposes	7,038	4,878	41	-2,048
Cash flows from investments in financial assets for liquidity purposes				
Increase in investments	-20,267	-19,281	-15,069	-13,982
Net cash flows from investments in financial assets for liquidity purposes	-20,267	-19,281	-15,069	-13,982
Cash flows from financing activities				
Advances received (net)	0	0	0	0
Borrowing (net)	-943	2,186	92	-589
Deposits received (net)	-20	0	0	0
Other financing (net)	232	-273	-429	-214
Net cash flows from financing activities	-730	1,913	-337	-803
Net increase/decrease in cash held	70	230	-215	-36

Table 16: Australian Government general government sector cash flow statement^(a) (continued)

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
Net cash from operating activities and investments in non-financial assets	14,029	12,720	15,150	16,796
Finance leases and similar arrangements(b)	-33	16	-551	30
GFS cash surplus(+)/deficit(-)	13,997	12,736	14,599	16,826
less Future Fund earnings	2,169	3,075	2,755	2,829
Equals underlying cash balance(c)	11,827	9,662	11,844	13,997
plus net cash flows from investments in financial assets for policy purposes	7,038	4,878	41	-2,048
plus Future Fund earnings	2,169	3,075	2,755	2,829
Equals headline cash balance	21,035	17,614	14,640	14,778

(a) A positive number denotes a cash inflow, a negative sign denotes a cash outflow.

(b) The acquisition of assets under finance leases decreases the underlying cash balance. The disposal of assets previously held under finance leases increases the underlying cash balance.

(c) The term underlying cash balance is not used by the ABS.

Table 17: Australian Government general government sector statement of other economic flows (reconciliation of net worth)

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
Opening net worth	-23,122	-11,934	-2,605	11,989
Opening net worth adjustments(a)	287	0	0	0
Adjusted opening net worth	-22,835	-11,934	-2,605	11,989
Change in net worth from operating transactions	12,709	10,404	13,108	15,714
Change in net worth from other economic flows				
Revaluation of equity(b)	205	-311	1,261	1
Net writedowns of assets (including bad and doubtful debts)	-2,434	-2,201	-1,971	-2,156
Assets recognised for the first time	178	18	19	30
Liabilities recognised for the first time	0	0	0	0
Actuarial revaluations	0	0	0	0
Net foreign exchange gains	-73	0	0	0
Net swap interest received	10	-51	-46	-41
Fair Value Gains Financial Instruments	348	1,279	2,248	2,455
Other economic revaluations(c)	-42	191	-24	5
Total other economic flows	-1,808	-1,075	1,486	294
Closing net worth	-11,934	-2,605	11,989	27,996

(a) Change in net worth arising from a change in 2005-06 outcomes.

(b) Revaluations of equity reflects changes in the market valuation of commercial entities. This line also reflects any equity revaluations at the point of disposal or sale.

(c) Largely reflects revaluation of assets and liabilities.

SENSITIVITY OF FISCAL EXPENSES AND REVENUE TO ECONOMIC DEVELOPMENTS

A guide to the sensitivity of the forward estimates of expenses and revenue due to variations in economic parameters in 2006-07 is provided in Table 18. It is important to note that the sensitivity analysis gives only a 'rule of thumb' indication of the impact on the budget of changes in prices, wages and other parameters. In each case, the analysis presents the estimated effects of a change in one economic variable only, and does not attempt to capture the linkages between economic variables that characterise changes in the economy more broadly.

Table 18: Sensitivity of fiscal expenses and revenue to changes in economic parameters

	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
Expenses				
Prices(a)	370	480	630	620
Wages	0	320	500	520
Federal Minimum Wage decision	0	90	170	240
Unemployment benefit recipients	120	240	250	260
Revenue				
Prices	20	130	150	150
Wages	870	1,770	1,790	1,910
Employment	840	1,710	1,720	1,840
Private final demand	100	290	300	310
Profits	120	460	500	540

(a) A change in the methodology used to estimate liabilities under the Commonwealth Superannuation Scheme and the Public Sector Superannuation Scheme means these estimates are now less sensitive to short-term changes in the CPI, compared to the estimates shown in previous MYEFO documents.

EXPENSES

On the expenses side, the sensitivity analysis of the estimates provides for the following assumptions about changes to four broad groups of parameters. An increase in any of the parameters considered will lead to an increase in expenses, and a decrease in any of the parameters will lead to a reduction in expenses.

Prices

All price growth rates are assumed to change by one percentage point in the March quarter 2007 and to remain unchanged subsequently, with all wage and salary growth rates left unchanged through the Budget and forward years.

- The effect of a change in prices is due to the indexation of Australian Government expenses (which impacts more in the forward years than the Budget year) and a one-off impact on the liabilities of the military superannuation schemes in 2006-07 (which in turn impacts on the defence superannuation interest expense).

Wages

All wage and salary growth rates are assumed to change by one percentage point in the March quarter 2007 and to remain unchanged subsequently, with all price growth rates left unchanged through the Budget and forward years.

- The effect of a change in wage and salary growth rates is largely due to the Government's commitment to maintain selected pensions at a minimum of 25 per cent of Male Total Average Weekly Earnings. The wages effect in Table 18 above does not include changes to wage and salary payments in Australian Government departmental expenses.

The Federal Minimum Wage decision

The Federal Minimum Wage increase determined by the Australian Fair Pay Commission (AFPC) is assumed to be \$2 per week higher in the Budget year and all forward years.

- Around \$60 billion of expenses in 2006-07, comprising agency departmental expenses, other Australian Government Own Purpose Expenses and Specific Purpose Payments to the States of a departmental expense nature, are indexed to weighted averages of movements in the Consumer Price Index and the Federal Minimum Wage decision.

Unemployment Benefit Recipients (Newstart Allowance and Unemployed Youth Allowance recipients)

The total number of recipients is assumed to change by 2.5 per cent in the Budget year and by 5 per cent in all the forward years.

REVENUE

On the revenue side, the sensitivity analysis of the estimates provides for the following assumptions about changes to five broad groups of parameters. An increase in any of the parameters considered will lead to an increase in revenue and a decrease in any of the parameters will lead to a reduction in revenue.

Prices

All price deflators are assumed to change by one percentage point at the start of the March quarter 2007, with wage deflators left unchanged.

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- A change in prices affects revenue primarily through changes in excise revenue and petroleum resource rent tax.

Wages

All wage and salary growth rates are assumed to change by one percentage point from the beginning of the March quarter 2007, with price deflators left unchanged.

- A change in wage and salary growth rates affects revenue through changes in gross income tax withholding and fringe benefits tax.

Employment

The level of employment is assumed to change by one percentage point from the beginning of the March quarter 2007, with no change in the composition of employment.

- A change in employment affects revenue through changes in gross income tax withholding.

Private final demand

The level of private final demand (consumption plus investment) is assumed to change by one percentage point from the beginning of the March quarter 2007, with no change in the composition of demand.

- A change in private final demand affects revenue primarily through changes in excise and customs duty collections.

Profits

The level of company profits is assumed to change by one percentage point from the beginning of the March quarter 2007.

- A change in the level of company profits affects revenue through changes in company tax collections.

TAX EXPENDITURES

Individuals and businesses derive financial benefits from various tax concessions. These concessions can be delivered in a variety of ways: by a tax exemption, tax deduction, tax rebate, reduced tax rate or by deferring a tax liability. Tax concessions can either reduce or delay the collection of tax revenue.

The benefits of most tax concessions could be delivered equally by direct expenditures. Hence tax concessions are an alternative to direct expenditure as a method of delivering government assistance or meeting government objectives. Accordingly, tax expenditures have an impact on the budget surplus or deficit, as do direct expenditures.

Table 19 provides aggregate tax expenditure estimates for the period from 2002-03 to 2009-10.

Table 19: Aggregate tax expenditures 2002-03 to 2009-10^(a)

Year	Superannuation \$m	Other tax expenditures \$m	Total \$m	Tax expenditures as a proportion of GDP (%)
2002-03 (est)	10,100	19,347	29,447	3.8
2003-04 (est)	13,540	20,015	33,555	4.0
2004-05 (est)	16,600	22,693	39,293	4.4
2005-06 (est)	18,080	24,064	42,144	4.4
2006-07 (proj)	17,255	24,064	41,319	4.0
2007-08 (proj)	20,250	26,420	46,670	4.3
2008-09 (proj)	22,230	27,692	49,922	4.4
2009-10 (proj)	23,940	28,756	52,696	4.5

(a) Preliminary estimates only — final estimates will be published in the *2006 Tax Expenditure Statement*.

Measured tax expenditures as a proportion of GDP are projected to fall from 4.4 per cent in 2005-06 to 4.0 per cent in 2006-07 mainly as a result of the impact of personal income tax rate reductions on the tax expenditure estimates. The ratio is projected to increase to 4.5 per cent by 2009-10 mainly because of changes in superannuation tax arrangements included in the *Simplified Superannuation* reforms.

Further detail on tax expenditures will be provided in the *2006 Tax Expenditures Statement*.

**SUPPLEMENTARY EXPENSE AND CAPITAL TABLES AND THE
CONTINGENCY RESERVE**

Expenses

Table 20 shows estimates of Australian Government general government expenses by function and sub-function for 2006-07 and the forward years.

Table 20: Estimates of Australian Government general government expenses by function and sub-function

	Estimates						Projections					
	2006-07			2007-08			2008-09			2009-10		
	Budget \$m	MYEFO \$m	Change on Budget %	Budget \$m	MYEFO \$m	Change on Budget %	Budget \$m	MYEFO \$m	Change on Budget %	Budget \$m	MYEFO \$m	Change on Budget %
General public services												
Legislative and executive affairs	830	873	5	948	993	5	777	820	6	784	843	8
Financial and fiscal affairs	4,109	4,649	13	4,076	4,700	15	4,117	4,848	18	4,211	5,008	19
Foreign affairs and economic aid	3,293	3,184	-3	3,957	3,895	-2	4,420	4,357	-1	4,525	4,720	4
General research	2,386	2,393	0	2,437	2,438	0	2,446	2,445	0	2,498	2,505	0
General services	639	717	12	639	709	11	640	690	8	653	701	7
Government superannuation benefits	2,551	2,526	-1	2,600	2,576	-1	2,690	2,667	-1	2,783	2,735	-2
Defence	17,871	17,025	-5	17,955	18,300	2	18,078	18,713	4	19,013	19,021	0
Public order and safety	3,286	3,393	3	3,326	3,483	5	3,370	3,557	6	3,450	3,671	6
Education	16,633	16,584	0	17,041	16,993	0	17,606	17,576	0	18,353	18,307	0
Health	39,838	39,708	0	41,991	42,003	0	43,635	43,631	0	45,459	45,428	0
Social security and welfare	91,756	91,349	0	95,807	96,331	1	99,991	100,462	0	103,788	104,141	0
Housing and community amenities	2,790	2,712	-3	3,026	3,127	3	2,631	2,647	1	2,314	2,391	3
Recreation and culture	2,627	2,731	4	2,549	2,692	6	2,513	2,630	5	2,534	2,608	3
Fuel and energy	4,804	4,935	3	4,958	5,183	5	5,290	5,523	4	5,304	5,515	4
Agriculture, fisheries and forestry	2,300	2,620	14	1,942	1,895	-2	1,588	1,415	-11	1,331	1,296	-3
Mining, manufacturing and construction	2,085	2,122	2	2,030	2,075	2	2,046	2,123	4	2,038	2,109	3
Transport and communication	3,552	3,608	2	4,023	4,083	1	4,166	4,223	1	2,649	2,703	2
Other economic affairs												
Tourism and area promotion	197	201	2	196	198	1	126	128	2	126	131	4
Labour and employment affairs	4,461	4,404	-1	4,416	4,415	0	4,414	4,531	3	4,503	4,687	4
Other economic affairs nec	959	1,005	5	948	987	4	957	966	1	965	966	0

Table 20: Australian Government expenses by function and sub-function (continued)

	Estimates						Projections					
	2006-07			2007-08			2008-09			2009-10		
	Budget \$m	MYEFO \$m	Change on Budget %	Budget \$m	MYEFO \$m	Change on Budget %	Budget \$m	MYEFO \$m	Change on Budget %	Budget \$m	MYEFO \$m	Change on Budget %
Other purposes												
Public debt interest	3,514	3,617	3	3,447	3,494	1	3,310	3,355	1	3,283	3,333	2
Nominal superannuation interest	5,784	5,725	-1	5,870	5,869	0	6,077	6,163	1	6,289	6,371	1
General purpose inter-government transactions	2,617	2,595	-1	2,671	2,695	1	2,624	2,647	1	2,547	2,608	2
Natural disaster relief	99	117	18	93	93	0	93	93	0	93	93	0
Contingency reserve	747	386	-48	3,611	3,095	-14	7,303	6,285	-14	13,099	10,777	-18
Total expenses	219,730	219,175	0	230,556	232,322	1	240,910	242,493	1	252,592	252,669	0

Contingency Reserve

The Contingency Reserve (other purposes function) is an allowance, included in aggregate expenses figuring, to reflect anticipated events that cannot be assigned to individual programmes in the preparation of the Australian Government budget estimates. The reserve is an estimating device used to ensure that the budget estimates are based on the best information available at the time of the MYEFO. It is not a general policy reserve.

While the reserve ensures that aggregate estimates are as close as possible to expected outcomes, it is not appropriated. Allowances that are included in the reserve can only be drawn upon once they have been appropriated by Parliament. These allowances are removed from the reserve and allocated to specific agencies for appropriation and for outcome reporting closer to the time when they eventuate.

The Contingency Reserve makes allowance in 2006-07 and the forward years for anticipated events, including the following:

- an allowance for the tendency for estimates of expenses for existing government policy to be revised upwards in the forward years;
- an allowance for the tendency for the estimates of expenses for some specific agencies or functions to be overstated in the budget year;
- commercial-in-confidence and national security-in-confidence items that cannot be disclosed separately;
- decisions made too late for inclusion against individual agency estimates;
- the effect on the budget and forward estimates of economic parameter revisions received late in the process and hence not able to be allocated to individual agencies or functions; and
- provision for events and pressures that are reasonably expected to affect the budget estimates.

FEDERAL FINANCIAL RELATIONS

In 2006-07, the States and Territories (the States) will receive GST revenue of \$39.3 billion and other payments from the Australian Government of \$28.3 billion, totalling \$67.6 billion as shown in Table 21.

Table 21: GST and Australian Government payments to the States, 2006-07

(\$m)	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	Total
(1) GST revenue to the States	10,999	8,515	8,012	3,945	3,562	1,566	763	1,979	39,342
(2) General revenue assistance	5	4	3	2	2	1	..	1	17
(3) Specific purpose payments	9,139	6,521	5,447	3,437	2,183	694	444	421	28,285
SPPs to the States	6,658	4,598	3,950	2,639	1,586	501	297	333	20,562
SPPs through the States	2,334	1,814	1,398	736	567	170	146	75	7,240
SPPs direct to local government	147	109	100	62	29	22	1	14	484
(4) Australian Government payments to the States and local govt (2) + (3)	9,144	6,524	5,451	3,438	2,185	694	444	422	28,303
(5) GST and total payments (1) + (4)	20,143	15,040	13,463	7,383	5,747	2,261	1,207	2,401	67,644
Per cent of GDP	2.0	1.5	1.3	0.7	0.6	0.2	0.1	0.2	6.6

GST revenue to the States

In accordance with the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations*, all GST revenue is paid to the States. This provides the States with a secure, growing and broad based revenue source to spend according to their own budget priorities. Table 22 is a reconciliation of the estimates of GST revenue between the 2006-07 Budget and the 2006-07 MYEFO.

Table 22: Reconciliation of GST revenue estimates

	Estimates		Projections	
	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
2006-07 Budget	40,000	42,210	44,440	46,670
Changes between 2006-07 Budget and MYEFO				
Effect of policy decisions
Effect of revenue recognition variations(a)	390	340	260	350
Effect of parameter and other variations	240	580	930	980
Total variations	630	920	1,190	1,330
2006-07 MYEFO	40,630	43,130	45,630	48,000

(a) Accrual estimates for GST revenue at the 2006-07 Budget were recognised using the Taxation Liability Method (TLM) of revenue recognition. Since the 2005-06 Final Budget Outcome, GST revenue has been recognised using the Economic Transactions Method (ETM) of revenue recognition. Refer to Appendix F of Statement 5 in 2006-07 Budget Paper No. 1 for an explanation of the different methods of revenue recognition.

A change in the recognition methodology for GST revenue has increased the GST revenue estimate for 2006-07 by \$390 million above the estimate provided at the 2006-07 Budget. This change in methodology only affects GST revenue estimated on an accruals basis, and does not affect GST receipts (cash collections) or the GST revenue to the States. GST revenue for 2006-07 has been revised up by a further \$240 million, primarily due to the higher than expected outcome for 2005-06.

Under the Intergovernmental Agreement, the Commissioner for Taxation estimates the likely level of GST receipts in June, prior to the end of each financial year. A balancing adjustment is usually made in the following financial year to ensure that the States receive the full amount of GST receipts for a financial year.

In 2006-07, the States will receive GST revenue totalling an estimated \$39.3 billion – \$212 million higher than estimated at the 2006-07 Budget. The upward revision reflects an increase of \$240 million in the estimate of GST receipts for 2006-07, offset by the recovery of a \$28 million overpayment in respect of 2005-06. Estimates of GST revenue to the States are shown in Table 23.

Table 23: GST revenue to the States, 2005-06 to 2009-10

	Outcome	Estimates		Projections	
	2005-06 \$m	2006-07 \$m	2007-08 \$m	2008-09 \$m	2009-10 \$m
GST revenue	38,884	40,630	43,130	45,630	48,000
less change in GST receivables	1,442	1,260	1,270	1,250	1,380
GST receipts	37,442	39,370	41,860	44,380	46,620
plus variation from Commissioner's determination(a)	28				
plus prior year balancing adjustment	-288	-28			
GST revenue to the States	37,182	39,342	41,860	44,380	46,620

(a) The Commissioner's determination for 2005-06 was \$28 million higher than the final outcome.

GST revenue to the States has grown strongly since its introduction, as shown in Table 24. The average annual increase since 2001-02¹ has been 8.2 per cent.

Table 24: GST revenue to the States, 2000-01 to 2006-07

(\$m)	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	Total
2000-01	7,258	5,099	4,658	2,375	2,279	988	473	1,226	24,355
2001-02	8,132	5,593	5,019	2,518	2,477	1,060	544	1,290	26,632
2002-03	9,080	6,365	5,888	2,910	2,859	1,247	616	1,515	30,479
2003-04	9,667	6,961	6,553	3,158	3,146	1,394	658	1,681	33,219
2004-05	9,884	7,346	7,329	3,624	3,293	1,435	680	1,730	35,323
2005-06	10,362	7,833	7,689	3,804	3,442	1,496	723	1,834	37,182
2006-07	10,999	8,515	8,012	3,945	3,562	1,566	763	1,979	39,342

1 As only 11 monthly activity statements, 3 quarterly activity statements, and no annual activity statements were payable in 2000-01, the calculated annual increase uses 2001-02 as the base year.

General revenue assistance

In the Intergovernmental Agreement, the Australian Government guaranteed that the budgetary position of each individual State would be no worse off than it would have been had the reforms in the Agreement not been implemented. The guaranteed minimum amount (GMA) is an estimate of the revenue that each State would have received under the previous system of financial assistance grants and if their own inefficient state taxes had not been abolished as part of the reforms.

For 2006-07, it is estimated that each State will receive more GST revenue than their GMA and, consequently, no State will require budget balancing assistance (BBA). Indeed, the States will receive a total revenue gain from the reforms of around \$2.0 billion above their GMA. These revenue gains are estimated to increase to around \$5.0 billion by 2009-10, as shown in Table 25.

Table 25: Revenue gains to the States as a result of reform, 2006-07 to 2009-10^(a)

(\$m)	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	Total
2006-07									
(1) GMA(b)	10,837	8,152	7,346	3,643	3,367	1,459	703	1,858	37,364
(2) GST revenue	10,999	8,515	8,012	3,945	3,562	1,566	763	1,979	39,342
(3) BBA (1) - (2)	0	0	0	0	0	0	0	0	0
(4) States' revenue gain (2) - (1)	162	363	666	302	195	108	60	121	1,978
2007-08									
(1) GMA	11,247	8,415	7,478	3,680	3,473	1,496	724	1,971	38,483
(2) GST revenue	11,906	9,138	8,400	4,139	3,763	1,621	809	2,086	41,860
(3) BBA (1) - (2)	0	0	0	0	0	0	0	0	0
(4) States' revenue gain (2) - (1)	659	722	922	459	290	125	85	115	3,377
2008-09									
(1) GMA	11,809	8,704	7,621	3,721	3,559	1,530	747	2,069	39,760
(2) GST revenue	12,903	9,765	8,744	4,317	3,938	1,674	852	2,187	44,380
(3) BBA (1) - (2)	0	0	0	0	0	0	0	0	0
(4) States' revenue gain (2) - (1)	1,094	1,061	1,122	596	380	145	105	118	4,620
2009-10									
(1) GMA(c)	12,593	9,035	7,925	3,850	3,684	1,568	782	2,173	41,609
(2) GST revenue	13,838	10,190	9,080	4,490	4,099	1,722	896	2,305	46,620
(3) States' revenue gain (2) - (1)	1,245	1,155	1,155	640	415	154	113	133	5,011

(a) Estimates from 2006-07 will be affected by variations in GMA components and GST revenue. Estimates from 2007-08 will be affected by recommendations by the Commonwealth Grants Commission on the distribution of GST provided to each of the States. Where GST revenue exceeds the GMA, no BBA is payable. As part of the agreement with the States to abolish the majority of the state taxes listed for review under the Intergovernmental Agreement, the Australian Government has extended the transitional period (in which BBA may be paid) from 30 June 2006 to 30 June 2009.

(b) As part of the agreement with the States to abolish the majority of the state taxes listed for review under the Intergovernmental Agreement, stamp duties on cheques, bills of exchange and promissory notes have been abolished in all States. The revenue foregone is included in the GMA from 2006-07.

(c) As part of the agreement with the States to abolish the majority of the state taxes listed for review under the Intergovernmental Agreement, all States will have abolished stamp duties on credit arrangements, instalment purchase arrangements, rental arrangements and leases by 1 July 2009. The revenue foregone is included in the GMA from 2009-10.

As no BBA is payable for 2006-07, general revenue assistance only consists of \$17 million in compensation payments to the States in respect of the cost of the Australian Government's decision to allow certain small businesses and non-profit organisations to pay their GST liability on an annual rather than quarterly basis (refer to 2004-05 Budget Paper No. 2). The compensation will ensure that the full financial impact of the decision is borne by the Australian Government and that there will be no impact on state budgets. Compensation payments for each year will be subject to an ex-post adjustment once final tax return data becomes available and the impact of the measure on GST revenue is known.

Specific purpose payments

The States receive substantial specific purpose payments from the Australian Government to help fund areas such as education, health, social security, housing and transport. These payments are a financial contribution to important areas of state responsibility which the Australian Government makes to pursue its own objectives.

In 2006-07, the States are estimated to receive \$28.3 billion in specific purpose payments (Table 26). Of this, \$7.2 billion is paid through the States, to be passed on to local governments and to others (for example, non-government schools), and \$484 million is paid direct to local governments.

Specific purpose payments have grown significantly since 2000-01, by an average of 7 per cent per annum, and are estimated to grow in aggregate by a further 5 per cent in 2006-07.

Table 26: Specific purpose payments, 2004-05 to 2006-07

(\$m)	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	Total
To the States									
2004-05	5,924	4,022	3,341	2,196	1,428	474	281	303	17,969
2005-06	6,402	4,421	3,648	2,500	1,514	501	286	342	19,613
2006-07	6,658	4,598	3,950	2,639	1,586	501	297	333	20,562
Through the States									
2004-05	2,139	1,643	1,219	659	506	152	128	69	6,515
2005-06	2,221	1,752	1,324	705	540	163	138	73	6,915
2006-07	2,334	1,814	1,398	736	567	170	146	75	7,240
Direct to local governments									
2004-05	90	78	54	43	22	10	6	7	311
2005-06	105	90	84	44	26	16	1	11	376
2006-07	147	109	100	62	29	22	1	14	484
Total specific purpose payments									
2004-05	8,154	5,742	4,614	2,898	1,955	637	415	379	24,795
2005-06	8,727	6,262	5,055	3,249	2,079	680	426	426	26,904
2006-07	9,139	6,521	5,447	3,437	2,183	694	444	421	28,285

Reform of state taxes

Implementation of the Intergovernmental Agreement has already delivered significant economic benefits as a result of abolishing a first tranche of inefficient state taxes from as early as 1 July 2000. The value of the revenue foregone from the abolition of these inefficient taxes is estimated to be \$3.9 billion in 2006-07 (Table 27).

The Australian Government has now agreed with the States on a schedule for the next tranche of state tax reform. The schedule provides for the abolition of all but one of the remaining taxes listed for review in the Agreement – these taxes were to be reviewed in 2005 to ensure that there was sufficient GST revenue to fund their abolition. The value of the revenue foregone from the second tranche of the abolition of state taxes is estimated to be a further \$0.6 billion in 2006-07 (Table 27), growing to \$1.7 billion by 2009-10.

Table 27: State tax revenues foregone as a result of reform, 2006-07^(a)

(\$m)	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	Total
<i>Tranche 1</i>									
Financial institutions duty	809	435	na	166	111	26	22	22	1,591
Debits tax	357	284	385	127	64	24	20	9	1,269
Quotable marketable securities duty	545	282	30	35	19	1	27	1	939
Accommodation taxes	105	na	na	na	na	na	na	11	115
Total	1,815	1,001	415	328	193	51	68	42	3,913
<i>Tranche 2</i>									
Mortgage duty	0	227	0	73	31	8	na	na	338
Rental duty	0	26	48	15	0	4	0	0	93
Lease duty	0	52	27	16	3	1	0	1	100
Non-quotable marketable securities duty	0	22	6	10	0	1	0	1	39
Cheque duty	na	na	na	6	3	na	na	3	12
Non-real business assets duty	0	na	0	0	0	0	1	0	1
Total	0	327	80	119	38	14	1	5	584

(a) A not applicable (na) indicates that the State did not levy that particular tax at the time of the Intergovernmental Agreement. A zero indicates that the State levies that particular tax, but has agreed to abolish it at a later date. Revenue foregone from the abolition of a tax is only included in the calculation of GMA (Table 25) once all States have abolished the tax.

Under the Intergovernmental Agreement, stamp duty on business conveyances of real property is also to be abolished, by a date to be determined jointly by the Australian Government and the States, on the basis that no State would be worse off in any year, compared with their likely financial position if reform had not occurred. This is the last remaining tax listed in the Intergovernmental Agreement which all of the States have agreed to abolish, but none have so far set out its timetable.