2006-07 BUDGET PAPER No. 1

BUDGET STRATEGY AND OUTLOOK 2006-07

CIRCULATED BY
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Notes

(a) The following definitions are used in this Budget Paper:

- 'real' means adjusted for the effect of inflation;
- real growth in expenses is measured by the non-farm Gross Domestic Product (GDP) deflator;
- the budget year refers to 2006-07, while the forward years refer to 2007-08, 2008-09 and 2009-10; and
- one billion is equal to one thousand million.

(b) Figures in tables and generally in the text have been rounded. Discrepancies in tables between totals and sums of components are due to rounding:

- estimates under $100,000 are rounded to the nearest thousand;
- estimates $100,000 and over are generally rounded to the nearest tenth of a million;
- estimates midway between rounding points are rounded up; and
- the percentage changes in statistical tables are calculated using unrounded data.

(c) For the budget balance, a negative sign indicates a deficit while no sign indicates a surplus.

(d) The following notations are used:

NEC/nec	not elsewhere classified
-	nil
na	not applicable (unless otherwise specified)
(e)	estimates (unless otherwise specified)
(p)	projections (unless otherwise specified)
$m	$ million
$b	$ billion

(e) The Australian Capital Territory and the Northern Territory are referred to as 'the Territories'. References to the 'States' or 'each State' include the Territories. The following abbreviations are used for the names of the States, where appropriate:

NSW	New South Wales
VIC	Victoria
QLD	Queensland
WA	Western Australia
SA	South Australia
TAS	Tasmania
ACT	Australian Capital Territory
NT	Northern Territory

(f) In this paper the term Commonwealth refers to the Commonwealth of Australia. The term is used when referring to the legal entity of the Commonwealth of Australia.

The term Australian Government is used when referring to the Government and the decisions and activities made by the Government on behalf of the Commonwealth of Australia.

Budget Strategy and Outlook 2006-07 is one of a series of Budget Papers that provides information to supplement the Budget Speech. A full list of the series is printed on the inside cover of this paper.

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After ten years of sound economic management the Australian Government has eliminated debt in net terms. The consequent reduction in debt servicing costs is producing on-going savings which can be applied to increased investment in physical and intellectual infrastructure.

The Future Fund is provisioning for the anticipated cost of the ageing of the population.

The Government will implement a further stage of tax reform that includes substantial cuts in personal taxes for low and middle-income earners, improvements to the international competitiveness of our top tax rates and enhancements to depreciation tax arrangements to improve business efficiency and competitiveness. In addition, a plan for substantial simplification and enhancement of Australia's superannuation system is being released.

The Government will continue its commitment to families through increasing the income test threshold for the maximum rate of Family Tax Benefit Part A to $40,000 a year and extending eligibility for the Large Family Supplement to families with three children.

The Government is increasing its commitment to health and medical research by providing additional funding to the National Health and Medical Research Council, along with a number of medical research facilities, and establishing an Australian health and medical research fellowship scheme.

The Government will also provide significant additional funding for road and rail infrastructure of $2.3 billion, including $800 million to accelerate duplication of the Hume Highway in southern New South Wales.

The Australian economy is forecast to continue to grow solidly, with GDP growth forecast to strengthen from 2½ per cent in 2005-06 to 3¼ per cent in 2006-07. Moderate inflation, low unemployment and strong business investment will provide a sound basis for sustained economic growth.

An underlying cash surplus of $10.8 billion is expected in 2006-07, with further surpluses projected for the three years following.

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STATEMENT 1: FISCAL STRATEGY AND BUDGET PRIORITIES

FISCAL OUTLOOK

The fiscal outlook for Australia continues to remain sound, with the Government forecasting a ninth budget surplus in 2006-07.

Ten years of fiscal and economic achievement has led to the elimination of Government debt in net terms. The consequent reduction in debt servicing costs has produced on-going savings which can be applied to investment in physical and intellectual infrastructure. The 2006-07 Budget advances a number of major initiatives. These include substantial cuts in personal taxes for low and middle-income earners, improvements to the international competitiveness of top marginal income tax rates, enhancements to depreciation tax arrangements to improve business efficiency and competitiveness, and a plan for substantial simplification and enhancement of Australia's superannuation system. The budget also continues the Government's commitment to families through increasing the income test threshold for the maximum rate of Family Tax Benefit Part A, investing significantly in health and medical research and providing significant additional funding for road and rail infrastructure.

An underlying cash surplus of $10.8 billion is expected in 2006-07 compared with an estimated surplus of $9.7 billion at the *Mid-Year Economic and Fiscal Outlook 2005-06* (MYEFO). Underlying cash surpluses continue to be projected across the forward estimates, helping to contain inflationary pressures in the economy and adding to national savings.

Table 1: Budget aggregates

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Underlying cash balance ($b)(a)	**13.6**	**14.8**	**10.8**	**10.6**	**11.2**	**12.0**
Per cent of GDP	1.5	1.5	1.1	1.0	1.0	1.0
Fiscal balance ($b)	**10.8**	**16.0**	**10.3**	**9.9**	**10.6**	**13.0**
Per cent of GDP	1.2	1.7	1.0	0.9	1.0	1.1

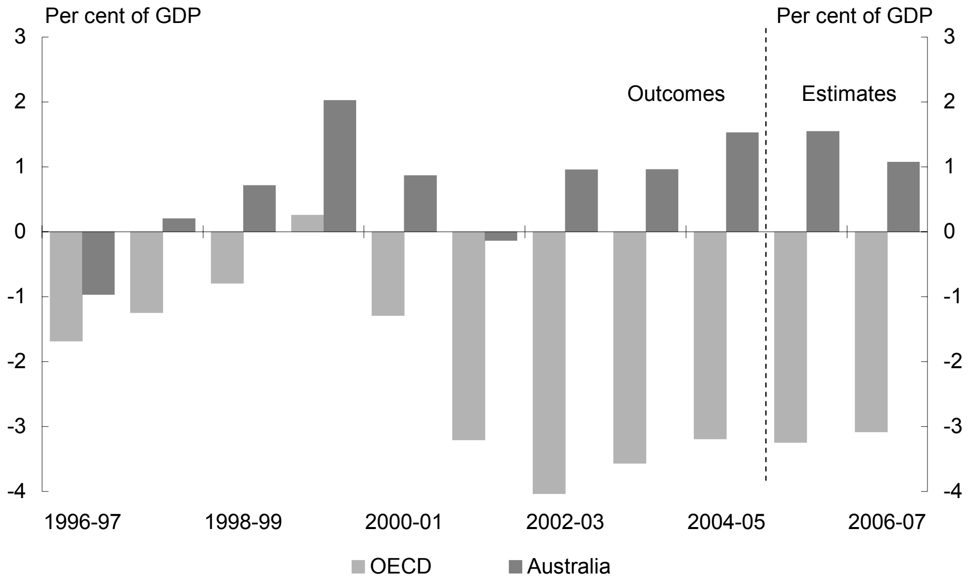
(a) Excludes expected Future Fund earnings from 2005-06 onwards.

In accrual terms, a fiscal surplus of $10.3 billion is now expected for 2006-07, compared to a surplus of $9.7 billion estimated at MYEFO.

Net debt has now been eliminated, after falling from a peak of 18.5 per cent of GDP ($95.8 billion) in 1995-96. Net debt servicing costs have fallen by 1.5 per cent of GDP in this period. Net worth is projected to become positive in 2008-09.

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

Chart 1: International comparison of budget balances



Source: OECD data are for the total general government sector and sourced from OECD Economic Outlook 78, December 2005. Australian data are for the general government sector and sourced from Statement 13.

ECONOMIC OUTLOOK

Prospects for Australian economic growth remain sound, particularly with strong growth anticipated for the world economy. Global growth is driving robust demand for Australian commodities and producing high commodity prices. This is generating a significant boost to the economy, with business investment set to grow strongly over 2006-07 and export growth likely to improve markedly. These developments are benefiting Australian businesses and households by supporting growth in national income.

Australia's GDP is forecast to increase by 3¼ per cent in 2006-07, up from 2½ per cent in 2005-06. Moderate inflation, low unemployment and an expansion in Australia's productive capacity will provide a sound basis for sustained economic growth.

Table 2 presents the major economic parameters used in preparing the budget. The parameters for 2005-06 and 2006-07 are forecasts while those for 2007-08, 2008-09 and 2009-10 are projections.

Table 2: Major economic parameters[(a)]

	Forecasts		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
Real GDP	2 1/2	3 1/4	3 1/2	3 1/4	3 1/4
Employment	2	1	1 1/2	1 1/4	1 1/4
Wage Price Index	4	4	3 3/4	4	4
CPI	3	2 3/4	2 1/2	2 1/2	2 1/2

(a) Year-average percentage change.
Source: Australian Bureau of Statistics (ABS) cat. no. 5206.0, 6202.0, 6401.0, 6345.0 and Treasury.

The projections from 2008-09 incorporate an employment growth assumption that has been adjusted down by ¼ of a percentage point to reflect the anticipated decline in labour market participation from the ageing of the population as identified in the *Intergenerational Report 2002-03*. The downward adjustment to employment brings projected real GDP growth down to 3¼ per cent from 2008-09.

Similar to the approach adopted for the 2005-06 Budget, the nominal GDP projections incorporate a technical assumption that iron ore and coal prices return progressively to their long-run average levels. The technical assumption has the effect of reducing nominal GDP growth in 2007-08 and 2008-09.

FISCAL STRATEGY

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

A medium-term approach to fiscal policy

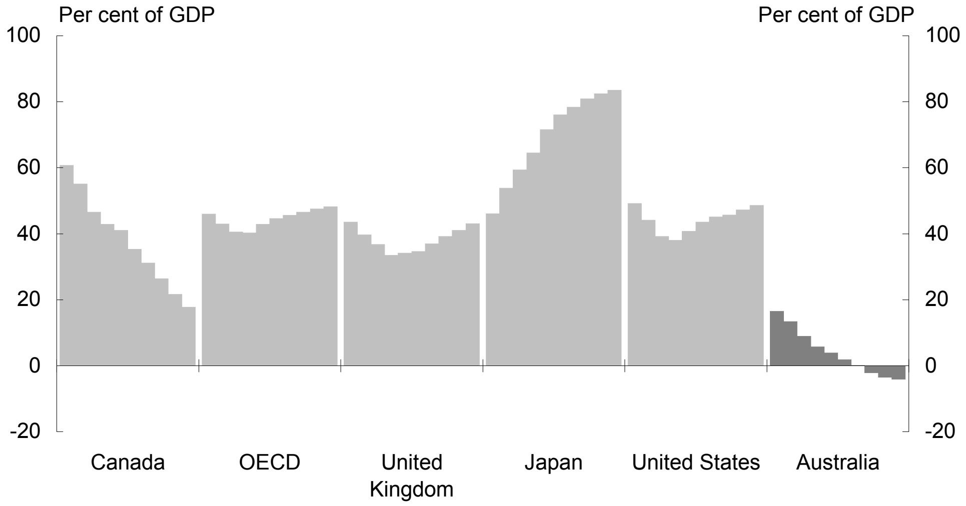
The primary objective of the medium-term fiscal strategy is to maintain budget balance, on average, over the course of the economic cycle. This helps deliver macroeconomic stability, encourages private investment in a low interest rate environment, entrenches low public debt and ensures that, over time,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

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

Consistent with the Government's fiscal strategy, this budget delivers a surplus in 2006-07 and surpluses over the medium-term. This will help contain inflationary pressures in the economy and will add to national savings. The fiscal strategy is complemented by a monetary policy framework which will continue to foster sustainable economic growth with low inflation and low interest rates into the future.

Sound economic management has seen the Australian economy enjoy output growth that has been one of the strongest and most stable on record. Since the recession of the early 1990s, Australia's GDP growth has averaged around 3¾ per cent per annum, having successfully navigated a number of major global shocks, including the east-Asian financial crisis in 1997, the global downturn in 2001, as well as severe drought conditions in Australia in 2002-03. During this period the Government has not only undertaken significant structural and taxation reform, but has also delivered a major reduction in the level of general government net debt. Australia is now one of only a few countries among the OECD with negative net debt (Chart 2).

Chart 2: General government net debt levels in selected countries (1998 to 2007)



Source: International data are sourced from OECD Economic Outlook 78, December 2005. Australian data are sourced from Statement 12. All data are for the total general government sector.

This transition to debt free status has enabled the Government to redirect expenditure away from interest payments on debt to spending on health, education and national security, while also investing for the future. Investing for the future has been a key theme of this Government. Central to this theme is the establishment of the Future Fund, in which funds will be gradually accumulated to meet the Commonwealth's superannuation liability — the largest liability on the Government's balance sheet, currently valued at around $96 billion.

The Government has established the Future Fund with an initial capital injection of $18 billion, with further contributions to be sourced from future budget surpluses and asset sales. In addition, Fund earnings are excluded from the underlying cash balance. These earnings will be retained within the Fund and hence are not available for recurrent Government spending. This means that fiscal policy will be tighter over future years than would otherwise be the case.

Maintaining budget surpluses over the forward estimates while our growth prospects remain sound represents a prudent response to an uncertain outlook, particularly in relation to the strength of the contribution provided by the terms of trade boost to revenues. This approach helps guard against the risks associated with a rapid unwinding of our fiscal position associated with a sharp fall in the terms of trade, by saving some of the additional income Australia is earning from the rest of the world. This fiscal policy approach also ensures that our public finances will be well positioned to meet future challenges flowing from demographic change and increasing demand for high quality health care.

BUDGET STRATEGY AND PRIORITIES

The last ten years of sound economic and fiscal management has delivered greater wealth, higher living standards and unprecedented prosperity to all Australians.

Ten years of fiscal and economic achievement provide the Government with the opportunity to implement a further stage of tax reform, along with new spending in a number of high priority areas including family assistance, mental health services, health and medical research, programmes for Indigenous Australians, road and rail infrastructure, national security and defence.

The tax reforms included in the budget include substantial cuts in personal taxes for low and middle-income earners, improvements to the international competitiveness of our top tax rates, enhancements to depreciation tax arrangements to improve efficiency and competitiveness and a plan for substantial simplification and enhancement of Australia’s superannuation system.

Personal income tax reform

The Government will reduce personal income tax by $36.7 billion (including the reduction in the fringe benefits tax rate) over four years. The tax cuts will increase disposable incomes for all Australian taxpayers, provide further incentives for individuals to participate in the workforce and improve the international competitiveness of Australia’s tax system. This builds on the substantial tax reform delivered in previous years’ budgets and provides households with the capacity to consolidate their financial position.

From 1 July 2006, the following changes will be made to the personal income tax scales:

- the 30 per cent threshold will increase to $25,001;

- the 42 per cent marginal tax rate will be cut to 40 per cent and the threshold will increase to $75,001; and
- the top marginal tax rate will be cut from 47 per cent to 45 per cent and the threshold will increase to $150,001.

Table 3: New personal tax rates

Current tax thresholds	Tax rate	New tax thresholds from 1 July 2006	Tax rate
Income range ($)	%	Income range ($)	%
0 - 6,000	0	0 - 6,000	0
6,001 - 21,600	15	6,001 - **25,000**	15
21,601 - 63,000	30	**25,001 - 75,000**	30
63,001 - 95,000	42	**75,001 - 150,000**	**40**
95,001 +	47	**150,001 +**	**45**

Low income earners will be further assisted through a substantial increase in the low income tax offset (LITO). From 1 July 2006, the LITO will increase from $235 to $600 and will begin to phase-out from $25,000. Those eligible for the full LITO will not pay tax until their annual income exceeds $10,000 (up from $7,567). Combined with the increase in the 30 per cent threshold to $25,001, this will improve the rewards from working for low income earners.

The Medicare levy low income phase-in rate will be reduced from 20 per cent to 10 per cent, ensuring more low income taxpayers pay a reduced rate of Medicare levy.

The fringe benefits tax rate will be reduced from 48.5 per cent to 46.5 per cent, effective from 1 April 2006.

Senior Australians will also benefit from these changes. Senior Australians eligible for the Senior Australians Tax Offset (SATO) and the LITO currently do not pay tax until an annual income of $21,968 for singles and $36,494 for couples (depending on the income received by each member of the couple). The tax cuts lift these income levels to $24,867 for singles and $41,360 for couples. The Medicare levy thresholds that apply to senior Australians will also be increased to ensure that they do not pay the Medicare levy until they begin to incur an income tax liability.

The 2006-07 Budget tax cuts ensure that more than 80 per cent of taxpayers face a marginal tax rate of 30 per cent or less. The increase in the top marginal tax rate threshold to $150,001 in 2006-07 will mean that around 2 per cent of taxpayers will be subject to a marginal tax rate of 45 per cent. Taxpayers will not reach the highest marginal tax rate until they earn more than three times average weekly earnings.

The 2006-07 Budget tax cuts build on the reform delivered in *The New Tax System* and the 2003-04, 2004-05 and 2005-06 Budgets. The overall effect has been to deliver a significant reduction in tax for all Australian taxpayers.

- Taxpayers earning $25,000 paid $4,522 in income tax prior to *The New Tax System* (excluding the Medicare levy) whereas taxpayers on that income will, from 1 July 2006, only pay $2,250; a reduction of around 50 per cent.

- Taxpayers on $65,000 paid $21,152 in income tax prior to *The New Tax System* (excluding the Medicare levy) whereas taxpayers on that income will, from 1 July 2006, only pay $14,850; a reduction of around 30 per cent.

- Taxpayers on $100,000 paid $37,602 in income tax prior to *The New Tax System* (excluding the Medicare levy) whereas taxpayers on that income will, from 1 July 2006, only pay $27,850; a reduction of around 26 per cent.

Chart 3 shows the percentage reductions in tax delivered by the Government, over a range of taxable incomes. In percentage terms the greatest tax cuts have been provided to low income earners.

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

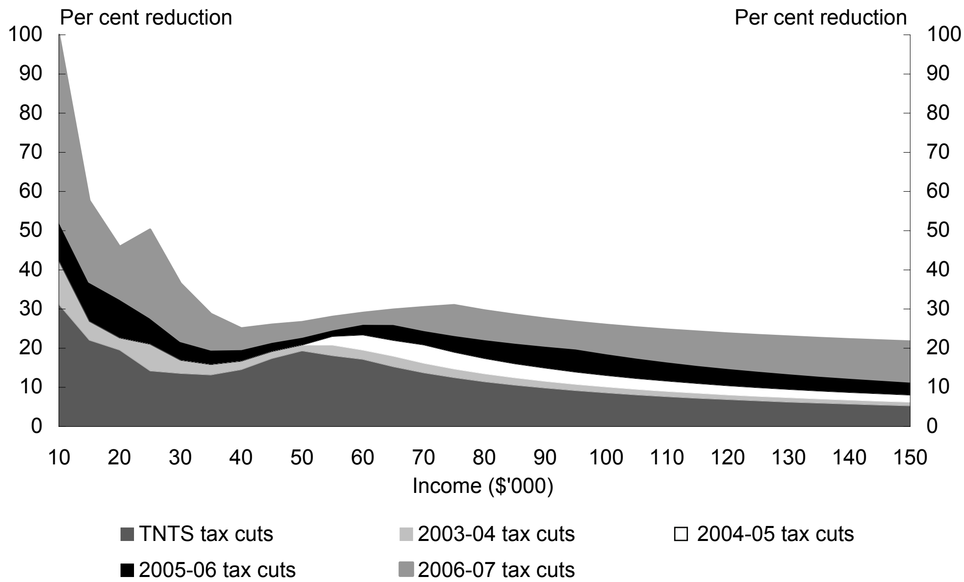
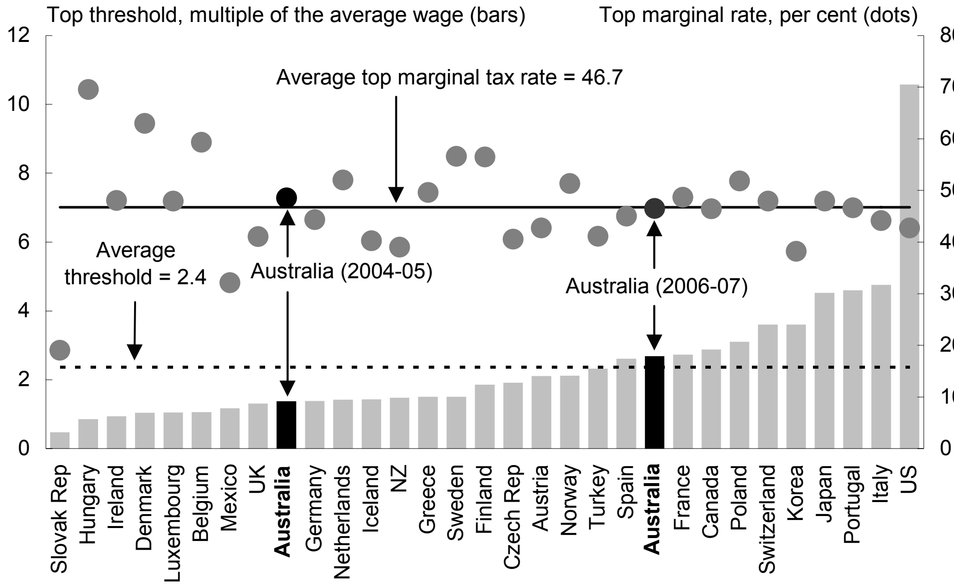


Chart 4 illustrates that the reduction in the top marginal tax rate and the increase in the threshold will improve Australia's competitiveness against other OECD countries. Australia's top marginal tax rate of 45 per cent, plus the Medicare levy, will be in line with the OECD average of 46.7 per cent and the increase in the top threshold will place Australia tenth highest in the OECD.

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



(a) The OECD average wage is for a worker engaged in full-time manual or non-manual labour across a range of industries.
Source: OECD Tax Database (preliminary data).

A plan to simplify and streamline superannuation

Australia's superannuation system is complex. Complexity confuses retirement decisions, clouds the incentive to invest in superannuation and imposes unnecessary costs. The Regulation Taskforce in its report 'Rethinking Regulation' recommended that the Government give high priority to comprehensive simplification of the tax rules for superannuation.

The current superannuation system has different arrangements for tax on contributions, earnings and superannuation benefits. Superannuation benefits tax is by far the most complicated. For example, a lump sum superannuation benefit may include up to eight different parts which can be taxed in seven different ways. If people cannot understand what they will receive from their superannuation in retirement, they will not have confidence in the system.

In this budget the Government releases a plan to simplify and streamline superannuation which includes a number of proposals to dramatically simplify the tax arrangements and restrictions that apply to Australians' superannuation benefits, encourage higher retirement savings and provide incentives to work.

Under this plan, Australians aged 60 and over who have already paid tax on their superannuation contributions and earnings would not pay tax on their superannuation benefits from 1 July 2007. The removal of benefits tax would sweep away the complexities retirees face when taking their benefits. Those contemplating retirement would not have to worry about, or pay for, professional advice on the tax implications of their superannuation benefits. As superannuation benefits would no longer be assessable income, there would be an incentive to continue to work while drawing down on superannuation as people will pay less tax on their work income. The preservation age will not be changed and people could still access their superannuation benefits before age 60, although they would be taxed on their benefits under new simplified rules. The plan also abolishes reasonable benefit limits (RBLs), introduces new streamlined rules for contributions, and gives individuals greater flexibility as to how and when they wish to draw on their superannuation in retirement.

As part of the superannuation reform there would also be reform of the pension assets test taper rate which would reduce from $3 to $1.50 per fortnight for every $1,000 of assets above the free area with effect from 20 September 2007. The current taper rate of $3 means that a retiree loses more age pension than they earn on their additional savings if they do not achieve a return of at least 7.8 per cent a year. This is a large disincentive to save for retirement.

Enhancing opportunities for business

The Government is committed to ensuring a supportive environment for business. Providing tax relief and reducing tariffs help in better positioning Australian businesses to perform domestically and compete in the global market.

Business taxation reforms

The Government will increase the incentives for Australian businesses to undertake the investment in new plant and equipment that is necessary for them to keep pace with new technology and remain competitive. The diminishing value rate for determining depreciation deductions will be increased from 150 per cent to 200 per cent (referred to as 'double declining balance'). This will apply to all eligible assets acquired on or after 10 May 2006. This measure, which will cost $3.7 billion over the next four years, will improve resource allocation by aligning depreciation deductions for tax purposes more closely with the actual decline in the economic value of assets. The changes will enhance the effectiveness of the uniform capital allowance regime introduced by the Government in 2001.

The Government will reduce taxes on small business by $435 million over four years. The changes will simplify and improve the alignment of thresholds and eligibility for a range of small business tax relief arrangements, including the Simplified Tax System, capital gains tax, the goods and services tax and pay as you go instalments. Changes to fringe benefits tax thresholds, at a cost of $40 million over four years, will reduce business compliance costs further. The Government will improve access to the small business capital gains tax relief arrangements for the owners of small businesses by replacing the current 50 per cent controlling individual test with a 20 per cent significant individual test and by increasing the net assets threshold for the relief arrangements from $5 million to $6 million. These changes will reduce compliance costs and allow more taxpayers to be eligible for the small business tax relief arrangements.

Venture capital and innovation

This budget includes measures to support the venture capital sector and encourage investment aimed at commercialising Australian research and development.

The Government will introduce an early stage venture capital limited partnership (ESVCLP) investment vehicle to develop further Australia's early stage venture capital sector and increase the provision of start-up capital for small, innovative firms. Investors in an ESVCLP will be exempt from tax on capital and revenue gains derived from ESVCLP investments. Amendments will also be made to improve the operation of the venture capital limited partnership investment vehicle.

The Government is also providing $200 million to establish up to ten new funds in a new Innovation Investment Fund programme round. Matching funding will be contributed by private investors. The new funds should assist in increasing the expertise of fund managers in the venture capital sector and provide more start-up capital to new companies, particularly those with a technology focus.

Heavy vehicle road user charge

The Government has decided not to proceed with an increase in the heavy vehicle road user charge recommended by the National Transport Commission. The recommendation to raise the charge reflected an increase in the National Transport Commission's estimate of the cost of road usage attributable to heavy vehicles. The Government's June 2004 *Securing Australia's Energy Future* statement assumed the charge would rise in line with road usage costs and this was reflected in the budget estimates. By not proceeding with the rise previously included in the estimates, the cost to the budget is $1.2 billion over four years.

Reducing tariffs

The Government is extending the Enhanced Project By-law Scheme to allow eligible capital goods that will be used in the power and water sectors to be imported duty free from 1 July 2006. This will reduce business input costs, improve the competitiveness of Australian industry, and promote opportunities for Australian business participation in large capital projects.

Protecting tax system integrity

The Government will introduce further measures to protect the integrity of the Australian taxation system. These measures will increase revenue by around $2.3 billion over four years.

- The Government will prevent some public sector superannuation schemes from improperly using pre-1 July 1988 funding credits. This measure will ensure that pre-1 July 1988 funding credits can only be used by superannuation schemes in circumstances consistent with the original policy intent. This measure will increase revenue by around $600 million over four years.

- The Government will require resident trustees to pay tax on distributions to non-resident trustee beneficiaries. This will ensure an appropriate amount of Australian tax is paid on such distributions and will increase revenue by around $800 million over four years.

- The Government will provide the Australian Taxation Office (ATO) with $81.6 million of additional resources over four years to maintain tax compliance by high wealth individuals and their associated entities. This is expected to increase revenue by $615 million over four years.

In addition, the Government has provided $305.1 million over seven years ($272.8 million of which is in the next four years) for investigations and prosecutions related to operation Wickenby which addresses alleged tax fraud involving the use of offshore entities. This is expected to increase revenue by $323 million over four years from active compliance and improved compliance behaviour by the relevant taxpayers.

Enhancing Defence capabilities

The defence of our country and its interests remains the highest priority of the Government.

In the Defence 2000 White Paper, the Government provided for around 3 per cent annual real growth in the Defence budget until 2010-11. Subsequently, this has been supplemented by additional funding for logistics and a range of other measures over recent years.

Consistent with the approach taken in the Defence 2000 White Paper, the Government will increase Defence spending by $10.7 billion between 2011-12 and 2015-16. This will provide 3 per cent annual real growth over the period, providing a firm basis for continued long-term planning. It will allow the Australian Defence Force (ADF) to continue to improve its capabilities, including acquisition of air warfare destroyers, large amphibious ships and new combat aircraft.

In addition, further key measures in the 2006-07 Budget include:

- $2.2 billion over six years to acquire new C-17 heavy airlift aircraft. These will enhance significantly the ADF's airlift capability, enabling rapid deployment of combat vehicles, helicopters and supplies. Australia's capacity to provide disaster relief will also be improved;

- $1.5 billion over ten years toward the development of a hardened and networked Army. This funding will be used to increase the size of the Army and to relocate a battalion to Adelaide. These initiatives will improve the sustainability of deployed land forces and enhance the Army's readiness for operations;

- $249.6 million over four years to improve recruitment and retention arrangements for permanent and reserve members of the ADF. These measures will include targeted bonuses for permanent members, improved remuneration for reserves and provision for the establishment of a High Readiness Reserve;

- $218.2 million over three years to provide an ADF contribution to a Netherlands-led Provincial Reconstruction Team (PRT) in Afghanistan. A further $57.6 million will provide for the deployment of Chinook helicopters to support the Special Forces Task Group and the initial stages of the PRT; and

- $392.7 million over three years to continue the ADF's contribution to stabilisation and reconstruction activities in Iraq.

National Security — Preventing Terrorism

As part of its broader national security strategy, the Government places a high priority on building the resources and capabilities of Australia's intelligence agencies. Airport and air transport security is also a particular focus for this budget, as is cooperation and capacity building with our neighbours.

Since 11 September 2001, the Government has made substantial investments in Australia's national security. Including measures in this budget, the Government has committed $8.1 billion over nine years from 2001-02 to new national security initiatives.

This budget provides an additional $1.5 billion over the five years to 2009-10 for intelligence, protective security, incident response capacity, regional cooperation and border security. A further $176.3 million is provided for intelligence measures in 2010-11. The *National Security — Preventing Terrorism* package includes funding out to 2009-10 comprising:

- $801.5 million for intelligence, including a commitment to increase staffing levels and technical capabilities for the Australian Security Intelligence Organisation, in response to the Taylor Review of that organisation's resources;

- $431.6 million for protective security, delivering the major part of the Government's response to the Wheeler Report into airport security and policing arrangements;

- $197.8 million for incident response capabilities, in particular to improve operational flexibility by funding Counter-Terrorism First Response teams at major Australian airports, as recommended by the Wheeler Report;

- $92.6 million for further capacity building in regional law enforcement and border control and increased cooperation across a number of Australian and regional security agencies; and

- $19.6 million for border security, including a further trial of unmanned aerial vehicles for Coastwatch.

Family assistance

Government spending on assistance to families with children has increased from $14 billion in 1996-97 to an estimated $28 billion in 2006-07 in recognition of the costs associated with raising children. Assisting families is an ongoing priority of the Government.

Families on lower incomes receive the highest rates of assistance. Through packages such as the $19 billion *More Help For Families* included in the 2004-05 Budget, the Government has increased the maximum rate of family assistance per child by 75 per cent from about $2,420 per child in 1996 to more than $4,200 in 2006 under Family Tax Benefit Part A.

In this budget, the Government is expanding eligibility for the maximum rate of Family Tax Benefit Part A. Currently, families start to have the maximum rate reduced once they earn more than $33,361 a year. The 2005-06 Budget provided an increase in this limit to $37,500 from 1 July 2006. This budget includes $993.3 million to further increase the limit to $40,000 from 1 July 2006 and allows more families to receive higher payment rates. It is expected that this measure will assist almost half a million families annually and provide increased payments of up to $9.62 a week. This means a single income family with two children will pay no net tax until their income rises above $48,065, after taking into account Family Tax Benefits.

In addition, the Government will extend eligibility for the Large Family Supplement of $248.20 to families with three children, with effect from 1 July 2006 at a cost of $496.7 million over four years. Currently, eligibility is restricted to families with four or more children.

Child care assistance

The Government recognises the importance of child care in assisting families to balance work and family commitments and enabling participation in the labour market by parents.

Building on previous Government initiatives that have almost doubled the number of child care places over the last ten years, the Government is removing the cap on the number of outside school hours care and family day care places, at a cost of $60.2 million. It is expected that this will generate an additional 25,000 places. This initiative brings outside school hours care and family day care into line with long day care, which is already uncapped.

New child care providers will be able to establish centres in areas of demand, without having to wait for a formal allocation of places, and existing providers will be able to expand more easily. This will make the child care sector more responsive to overall demand, and make it easier for parents to access child care places for their children.

Supporting older Australians and carers

The Government is committed to supporting older Australians and carers, recognising the important position they hold within our community.

To assist with the cost of household bills, the Government will provide by 30 June 2006 an additional one-off payment equal to the maximum rate of Utilities Allowance ($102.80) to each household with a person of Age or Service Pension age eligible for Utilities Allowance on 9 May 2006. A $102.80 payment will also be provided by 30 June 2006 to each self-funded retiree eligible for the Seniors Concession Allowance on 9 May 2006. This will cost $192.5 million.

The Government will also extend eligibility for the Utilities Allowance to cover recipients of Mature Age Allowance, Partner Allowance and Widow Allowance. These recipients will be paid by 30 June 2006 the same one-off payment applying to those currently eligible for Utilities Allowance. They will then receive Utilities Allowance every six months from September 2006 and beyond. This will cost $35.6 million.

The Government will provide $358 million for a lump sum payment to eligible carers in recognition of their contribution in caring for those with disabilities. Carer Payment recipients will receive $1,000 and recipients of Carer Allowance will receive $600 for each eligible person in their care. Those in receipt of both payments will receive both lump sum payments. In addition, those who receive both the Carer Allowance and either the Wife Pension or Department of Veterans' Affairs Partner Pension will receive both bonus payments. The bonus payments will generally be paid by 30 June 2006, be tax free and not treated as income when calculating social security payments.

The Government will also increase access to the Age and Service Pension for people who live on large blocks of land, have a 20 year connection to that land and for whom it would be unreasonable to realise the value of the land by selling or leasing it. From 1 January 2007, people in these circumstances will be able to exempt the entire value of land on the same title as their home from the Age and Service Pension assets test. This will cost $173.3 million over four years. Currently, only the home and an area up to two hectares is exempt.

Meeting our health care needs

In 2006-07, the Government will spend $47.6 billion on health and aged care, up from $20.2 billion in the Government's first budget in 1996.

Furthering the health and medical research effort

Health and medical research benefits all Australians through improved health outcomes. The Government is committed to continuing Australia's position as a world leader in this field. The Government's annual investment in health and medical research grants through the National Health and Medical Research Council (NHMRC) has more than tripled over the past decade, from $126.5 million in 1995-96 to $430.5 million in 2005-06. This budget provides an additional $905 million to health and medical research comprising:

- $500 million over four years for the NHMRC;
- $235 million for a number of medical research facilities to further their research, development and expansion projects; and
- $170 million to establish a new Australian health and medical research fellowship scheme, to attract and retain leading researchers and scientists.

This commitment will increase annual funding for health and medical research to over $700 million by 2009-10.

Council of Australian Governments' Mental Health package

Mental health conditions, such as schizophrenia, bipolar disorder and depression, directly reduce the wellbeing of sufferers and their carers, and have a broader effect on the prosperity of the community including through reduced workforce participation and productivity.

This year's budget provides an additional $1.9 billion over five years for a wide range of mental health services. Major elements include:

- an additional $538 million for increased psychologist and psychiatric services, and better general practitioner services, through reforms to Medicare;
- funding of $284.8 million for 900 new personal helpers and mentors to assist 53,000 people with a mental illness to navigate the health, welfare and employment systems;
- new respite care places to be delivered through the non-government sector, particularly for elderly parents who care for children with severe mental illness or an intellectual disability, at a cost of $224.7 million;

- funding of $191.6 million for new specialist mental health nurses to coordinate clinical care for people with more severe mental illness who are managed in primary care and by psychiatrists; and

- funding of $103.5 million for new tertiary education places and scholarships in mental health nursing and clinical psychology. The funding will also be used to increase mental health competencies and clinical training in mental health practice across the health workforce.

Investing in health care

The Government is investing in areas that underpin the health and aged care system to ensure Australians have access to high quality care. This includes funding the training of more doctors and nurses, prevention activities and the promotion of quality care for residents in aged care homes.

This budget provides:

- $240.8 million over five years to train more doctors and nurses as part of reforms through the Council of Australian Governments (COAG). This includes 400 new medical school places a year, 1,000 new higher education nursing places a year, and an increase in the Government's contribution to the cost of nurse clinical training from approximately $688 to $1,000 a year per full-time student. The States and Territories are expected to match this commitment to further strengthen Australia's health workforce;

- $79.5 million over five years for initiatives to address drug and alcohol abuse; and

- $58.3 million over four years to increase innovation and choice in private health insurance, and to increase consumer awareness of the incentives and benefits associated with private health insurance.

These initiatives build on the Government's $733.2 million commitment to the health system announced through COAG in February 2006, which includes a $250 million investment in promotion of good health, disease prevention and early intervention.

Road and rail infrastructure

A high quality land transport infrastructure network underpins Australia's productivity by providing for quick and seamless movement of goods and services to markets. In recognition of this, the budget provides for an additional $2.3 billion for roads and rail infrastructure. This new funding supplements the Government's $12.7 billion investment in land transport infrastructure between 2004-05 and 2008-09 under the Government's national land transport plan, AusLink, bringing total investment over the period to $15 billion. This compares with spending of $8.5 billion over the period 1994-95 to 1998-99.

The Government will provide $800 million to the New South Wales Government to accelerate duplication of the Hume Highway in southern New South Wales. Together with existing commitments, this funding will accelerate completion of the majority of unduplicated sections between Albury and Coolac.

The Government will also provide to the Queensland Government an additional $220 million for safety works on the Bruce Highway between Townsville and Cairns in support of far north Queensland's recovery from the effects of Cyclone Larry. The Government will also provide an extra $48 million to supplement its existing $80 million commitment to the Tully flood works project.

The Government will also provide:

- $234 million to the Western Australian Government for the Great Northern Highway;
- $160 million to the New South Wales Government for the Pacific Highway;
- $100 million to the South Australian Government for the Sturt Highway;
- $75 million to the Western Australian Government for further widening of the Eyre Highway;
- $60 million to the Tasmanian Government for the upgrade of the East Tamar Highway north of Launceston to Bell Bay;
- $30 million to the Northern Territory Government for the upgrade of the Victorian Highway to improve flood immunity; and
- $14 million to the Western Australian Government for the Great Eastern Highway.

In addition, the Government will invest a further $307.5 million in the Roads to Recovery Programme to improve the efficiency of Australia's regional road networks.

The Government will also invest an additional $270 million in the Australian Rail Track Corporation to improve rail track quality on the North-South rail corridor through targeted concrete resleepering.

Murray-Darling Basin Commission — boosting capital works

The Government is committed to restoring the health of the Murray Darling Basin for the benefit of the environment, irrigators, industry and the towns in the Basin.

In this budget, the Government will contribute $500 million to the Murray Darling Basin Commission. This funding will allow the Commission to:

- accelerate its capital programme;
- undertake additional projects under the Living Murray Environmental Works and Measures Programme; and
- participate in the Living Murray Agreement to deliver 500 gigalitres per annum for environmental water flows.

The Australian Government expects that all Commission parties will at least maintain their contributions in real terms for the next five years. The Government will seek agreement from the Commission to provide an ongoing identification of how these funds are spent.

Securing Borders against Illegal Foreign Fishing

The Government is committed to maintaining the integrity of Australia's borders, through combating illegal fishing.

Illegal fishing can pose serious risks such as the depletion of fish stocks, including endangered species, quarantine threats and the harbouring of illegal immigrants and prohibited goods.

The budget provides $388.9 million over four years to enhance Australia's surveillance and patrol capability in the exclusive economic zone of our northern waters. This increased capability will more than double the number of apprehensions each year and suppress the activities of vessels engaged in illegal fishing. The funding includes:

- $209 million to apprehend illegal fishing vessels and to transport, detain and prosecute their crew in order to provide a strong deterrent against illegal fishing;
- $64.4 million to construct dedicated facilities to destroy seized illegal fishing boats and properly manage the quarantine risks they pose;
- $43.4 million to enhance helicopter transport capability to rapidly deploy officers from relevant agencies to the sites of illegal landings or abandoned vessels and for charting and surveying work necessary to allow patrol vessels to navigate the Torres Strait and the northern Great Barrier Reef;
- $42.9 million to conduct surface and air surveillance over high risk areas and to engage Indigenous communities to report illegal fishing sightings;
- $19.6 million to expand the Joint Offshore Protection Command Headquarters to provide a more holistic and integrated assessment of maritime security threats and for preventative action to deter illegal fishing at its source through cooperation with Indonesia and within the region; and

- $9.6 million to enhance liaison, detection and response capabilities in Australia's northern waters.

In this budget, the Government is also committing $44.1 million over three years to maintain and enhance border controls at Australia's ports in response to the increased risk of avian influenza to both humans and animals in our region.

Child Support Reforms

The Government has announced a number of fundamental changes to the Child Support Scheme so that it better reflects the needs of a changing Australian society. These changes are designed to encourage shared parenting and aim to reduce conflict between parents, building on the Government's recent reforms to the family law system. The total cost of the reforms will be $877 million, with the first stage of reforms to commence from 1 July 2006.

The centrepiece will be a new formula to assess child support which better accounts for the capacity of both parents to meet children's needs, better reflects research on the costs of raising children and has greater regard to the costs of contact. The new formula will commence from 1 July 2008. The reforms also include revised Family Tax Benefit arrangements for separated parents.

Strengthening Indigenous Communities

The Government will support a range of new initiatives to help address the needs of Indigenous Australians. These include:

- $116 million over four years to improve Indigenous health. This includes an additional $55.2 million to help combat substance abuse, in particular petrol sniffing through the continued roll-out of Opal non-aromatic fuel, and additional funding of $39.5 million to expand access by Indigenous people to appropriate primary health care services;

- $126.5 million over four years to support compulsory Job Network registration for participants in the Community Development Employment Projects (CDEP) programme living in urban and regional areas and a time limit of one year's participation for new CDEP participants in urban and regional areas;

- $66.9 million over five years to improve education opportunities for Indigenous Australians, including through expanding the Indigenous Tutorial Assistance Scheme to include Year 9 students and vocational education and training students;

- $28.1 million over four years to improve the governance of Indigenous corporations and an additional $23 million to strengthen Indigenous community leadership and to assist communities to identify priorities and negotiate Shared Responsibility Agreements with the Government; and

- $20 million in capital to the Home Ownership Programme (enabling housing loans to be made to an additional 140 Indigenous families) and a further $107.5 million over four years for housing on Indigenous land, in support of proposed reforms to land tenure arrangements in the Northern Territory.

Better and fairer delivery of social services

A new health and social services access card

The Government distributes over $100 billion in health and social services benefits to more than 6.5 million individuals each year.

To ensure that those eligible are able to obtain Government benefits and services in a convenient, reliable and efficient manner, the Government has committed around $1.1 billion over four years to simplify service delivery through the introduction of a new access card for health and social services.

The new access card system, which will utilise smart card technology, will replace 17 existing health and social services cards and vouchers, including Medicare, Veterans' and Centrelink cards, and will reduce the need for people to go to offices, fill out forms and queue for service. Moreover, the new system will mean people no longer have to provide multiple identity documents each time they wish to apply for a different benefit. A one-off registration process will validate the identity of the applicant.

In addition to improving service delivery, the access card system is expected to deliver savings going forward as a result of reduced identity fraud and concession abuse, as well as reduced administration costs.

The access card will be phased in over two years, commencing in 2008. From early 2010, people will require an access card to obtain Government health and social services benefits.

Fraud and Compliance

This budget also includes a package of measures to minimise the risk of incorrect payments and reduce fraudulent activities, to protect the integrity of the social security system. The package, involving additional funding of $282.3 million over five years to assist service delivery agencies, builds on the existing fraud and compliance framework and is expected to lead to savings of $548.4 million, delivering net savings of $266 million over five years. Key elements of the package include:

- expanding the number and scope of investigations that can be undertaken by Centrelink officers to detect cases of serious social security fraud;
- strengthening information sharing and data-matching arrangements between agencies to prevent and detect fraud across multiple Government programmes;

- bolstering internal review activities to identify new and emerging compliance risks, and ensuring that the overall compliance framework is targeted correctly; and
- expansion of compliance activity in relation to the Child Care Support Programme and Child Care Benefit payment.

Investing in education

A high quality and responsive education system is vital to increasing skills which, in turn, boost labour force participation and productivity. In this year's budget the Government is delivering a range of initiatives to further improve Australia's education system.

Major additional initiatives in the 2006-07 Budget are:

- an extra $95.5 million over four years to increase capital funds for universities through the Capital Development Pool. This is in addition to specific funding in 2005-06 of $125 million for capital works at the Australian National University, including for the John Curtin School of Medical Research, and $12 million to expand the Centre for Transnational Crime Prevention at the University of Wollongong;
- raising the FEE-HELP loan limit for eligible full fee-paying students. For medicine, dentistry and veterinary science the limit will be increased to $100,000. For other courses the limit will be increased to $80,000;
- increased funding to New Apprenticeships Centres of $106.7 million over four years to enable increased contact by New Apprenticeships Centres with apprentices and their employers;
- an extra $34.9 million over four years to extend the Partnership Outreach Education Models pilot to offer national coverage. This will assist up to 3,000 disadvantaged young people with education, training or work annually; and
- an additional $40.8 million over four years to expand the eligibility criteria for the English as a Second Language — New Arrivals Programme.

Improving assistance for sport

The Government continues to provide significant assistance for sport.

This year's budget includes a further $54.3 million over four years for the Australian Institute of Sport. The measure will fund additional high performance coaching, better talent identification and development and new scholarship programmes, underpinned by improved sports science and medicine. This is in addition to the $52.3 million provided to the Australian Sports Commission in the 2005-06 Budget to support elite sport. These measures will help sustain Australia's international sports competitiveness and prepare Australian athletes for the 2008 Beijing Olympics.

Promoting sustainable development in the Asia-Pacific region

On 26 April 2006 the Government released the Aid White Paper, providing the strategic framework for Australia's overseas development assistance over the next decade. It follows the announcement of the Government's goal to increase development assistance to about $4 billion by 2010, conditional on strengthened governance and reduced corruption in recipient countries.

The Aid White Paper demonstrates the Government's commitment to poverty reduction, sustainable development and progress toward the Millennium Development Goals. It reaffirms the focus on the Asia-Pacific region and outlines several new initiatives for ensuring that Australia's aid dollars are effective in promoting sound economic development. In particular, the Government will work with developing countries through whole of government country development strategies and establish a new Office of Development Effectiveness.

In 2006-07, the Government will spend approximately $3 billion on official development assistance. This includes an additional contribution of $136 million to meet the costs of cancelling the debts of some of the world's poorest countries as part of the Multilateral Debt Relief Initiative. Australia is one of only a few countries to make an upfront financial contribution to the Initiative.

In addition, the Government will provide $442.5 million of new funding over five years for the Australian Scholarships programme. This increase will bring total programme funding to nearly $1.4 billion over five years providing more than 19,000 scholarships. A new component, the Australian Leadership Awards, will target future leaders in the Asia-Pacific region for advanced study. These scholarships will promote political and economic reform in the region and enable regional leaders to develop enduring connections with Australia.

STATEMENT 2: FISCAL OUTLOOK

This statement summarises the main budget aggregates for the Australian Government general government sector.

The fiscal outlook for Australia remains sound, with the Government forecasting an underlying cash surplus of $10.8 billion in 2006-07. Across the forward estimates the Government has maintained the budget in a surplus position after providing for substantial personal income tax cuts of $36.7 billion over four years commencing on 1 July 2006.

The Government's sound fiscal management has seen the elimination of net debt in 2005-06 and the prospect of positive net worth in 2008-09. Such sound fiscal policy, along with the financial assets accumulating in the Future Fund, leaves the Government well placed to deal with the budget pressures of an ageing Australia.

STATEMENT 2: FISCAL OUTLOOK

The fiscal outlook for Australia remains sound, with the Government forecasting its ninth budget surplus in the last ten years. Across the forward estimates period, the Government has maintained the budget in surplus after providing personal income tax cuts of $36.7 billion, $993 million for increasing the income test threshold for the maximum rate of Family Tax Benefit Part A, $905 million for funding on health and medical research and $2.3 billion additional funding for road and rail infrastructure.

BUDGET AGGREGATES

An underlying cash surplus of $10.8 billion is expected in 2006-07 compared with an estimated surplus of $9.7 billion at the *Mid-Year Economic and Fiscal Outlook 2005-06* (MYEFO). In accrual terms, a fiscal surplus of $10.3 billion is estimated for 2006-07 compared to the $9.7 billion at MYEFO. The fiscal outlook is for continuing underlying cash and fiscal surpluses in the forward years.

Table 1: Australian Government general government sector budget aggregates(a)

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Revenue ($b)	**206.6**	**222.9**	**231.7**	**240.7**	**252.1**	**265.6**
Per cent of GDP	23.1	23.3	23.0	22.9	23.0	23.0
Expenses ($b)	**195.7**	**206.0**	**219.7**	**230.6**	**240.9**	**252.6**
Per cent of GDP	21.9	21.6	21.8	21.9	22.0	21.9
Net operating balance ($b)	10.9	16.8	11.9	10.1	11.2	13.0
Net capital investment ($b)	0.1	0.9	1.6	0.2	0.6	0.0
Fiscal balance ($b)	**10.8**	**16.0**	**10.3**	**9.9**	**10.6**	**13.0**
Per cent of GDP	1.2	1.7	1.0	0.9	1.0	1.1
Underlying cash balance ($b)(b)	**13.6**	**14.8**	**10.8**	**10.6**	**11.2**	**12.0**
Per cent of GDP	1.5	1.5	1.1	1.0	1.0	1.0
Memorandum item:						
Headline cash balance ($b)	12.5	13.5	37.5	10.7	11.4	12.3

(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) Excludes expected Future Fund earnings from 2005-06 onwards.

VARIATIONS TO THE FISCAL BALANCE ESTIMATES

The upward revision of $0.6 billion in the 2006-07 fiscal surplus since MYEFO largely reflects higher than anticipated revenue from companies. This is partly offset by the impact of the Government's decision to provide additional tax relief and to increase the diminishing value rate of depreciation of eligible company assets acquired from 10 May 2006.

Table 2 provides a reconciliation of the fiscal balance estimates between the 2005-06 Budget, the 2005-06 MYEFO and the 2006-07 Budget.

Table 2: Reconciliation of 2005-06 Budget, 2005-06 MYEFO and 2006-07 Budget fiscal balance estimates

	Estimates		Projections	
	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m
2005-06 Budget fiscal balance	**7,410**	**7,458**	**8,003**	**9,022**
Per cent of GDP	0.8	0.8	0.8	0.9
Changes between 2005-06 Budget and MYEFO				
Effect of policy decisions(a)				
Revenue	-81	-129	-126	-141
Expenses	1,525	1,229	1,099	1,115
Net capital investment	230	59	-15	4
Total policy decisions impact on fiscal balance(b)	-1,836	-1,416	-1,210	-1,260
Effect of parameter and other variations				
Revenue	4,192	4,681	5,023	4,550
Expenses	-568	824	764	160
Net capital investment	-63	185	102	372
Total parameter and other variations impact on fiscal balance(b)	4,823	3,672	4,157	4,017
2005-06 MYEFO fiscal balance	**10,398**	**9,714**	**10,950**	**11,779**
Per cent of GDP	1.1	1.0	1.0	1.1
Changes between MYEFO and 2006-07 Budget				
Effect of policy decisions(a)				
Revenue	3	-6,952	-9,939	-10,727
Expenses	2,032	4,271	4,836	5,254
Net capital investment	57	398	191	244
Total policy decisions impact on fiscal balance(b)	-2,085	-11,621	-14,965	-16,225
Effect of parameter and other variations				
Revenue	4,239	11,181	12,309	13,071
Expenses	-3,052	-1,400	-1,542	-2,187
Net capital investment	-363	382	-104	245
Total parameter and other variations impact on fiscal balance(b)	7,654	12,198	13,955	15,012
2006-07 Budget fiscal balance	**15,966**	**10,290**	**9,940**	**10,566**
Per cent of GDP	1.7	1.0	0.9	1.0

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

Variations in revenue estimates

Total revenue for 2006-07 has been revised up by $4.2 billion since 2005-06 MYEFO. The upward revision represents the flow-on effect of stronger growth in expected revenue from companies and individuals in 2005-06, together with a stronger outlook for corporate profits in 2006. These upward revisions have been partly offset by the impact of the Government's decision to provide personal tax cuts (including the reduction in the fringe benefits tax rate) worth $6.6 billion in 2006-07, and $36.7 billion over the forward estimates and increasing the diminishing value rate for determining depreciation deductions at a cost of $3.7 billion over the forward estimates.

Other major policy decisions affecting revenue over the four year period from 2006-07 to 2009-10 include:

- the taxation of distributions to non-resident trustee beneficiaries which is expected to increase taxation revenue by $250 million in 2007-08 and $800 million over the forward estimates;

- the Government providing the Australian Taxation Office with an additional $82 million over four years to maintain tax compliance by high wealth individuals and their associated entities. This funding is expected to raise an additional $65 million in revenue in 2006-07 and $615 million over the forward estimates; and

- preventing some public sector superannuation schemes from improperly using pre-1 July 1988 funding credits. This is expected to increase taxation revenue by $150 million in 2006-07 and $600 million over the forward estimates.

Parameter and other variations are expected to increase revenue in 2006-07 by $11.2 billion, relative to the MYEFO forecasts. The strength in taxation revenue largely stems from the improvements in corporate profitability, bolstered by the flow-on effect of stronger outcomes in 2005-06.

Looking ahead, expected growth in nominal GDP remains supportive of continued strength in revenue, particularly from the corporate sector. In underlying terms, personal income is expected to continue to grow strongly on the back of solid growth in compensation of employees and the realisation of capital gains by investors.

Further detail on how the revised outlook for the economy has affected individual revenue heads over the forward estimates is provided in Statement 5. An analysis of the sensitivity of the taxation revenue estimates to changes in the economic parameters is provided in Appendix C.

Variations in expense estimates

Since MYEFO, estimated expenses for 2006-07 have increased by $2.9 billion reflecting the impact of new policy decisions of $4.3 billion partially offset by parameter and other variations of $1.4 billion.

Major policy decisions since MYEFO that have increased expenses include:

- $792 million in 2006-07 ($1.7 billion over four years) to acquire a new heavy airlift capability for the Australian Defence Force. The total cost amounts to $2.2 billion over six years;

- $242 million in 2006-07 ($993 million over four years) to expand the eligibility for the maximum rate of Family Tax Benefit Part A so that, from 1 July 2006, a family can earn $40,000 (up from $33,361 in 2005-06) without having their entitlement reduced;

- $178 million in 2006-07 ($1.1 billion over four years) for a range of national security measures under the *National Security — Preventing Terrorism* package;

- $137 million in 2006-07 ($971 million over four years) to introduce the health and social services access card, to provide more convenient and efficient access to Australian Government health and social services benefits;

- $136 million in 2006-07 to finance Australia's share of the Multilateral Debt Relief Initiative announced by G8 Finance Ministers in June 2005. The funding will enable up-front payment of Australia's contribution for the ten-year period 2006-07 to 2015-16;

- $133 million in 2006-07 ($1.9 billion over five years to 2010-11) for mental health reform measures including a major increase in clinical and health services available in the community; and

- $114 million in 2006-07 ($497 million over four years) to extend the Family Tax Benefit Part A Large Family Supplement to families with three children.

In 2006-07, parameter and other variations have decreased forecast expenses by $1.4 billion since MYEFO largely reflecting:

- a $287 million reduction in estimated Parenting Payment expenses largely due to a stronger labour market reducing the expected number of benefit recipients;

- a $260 million reduction in estimated Age Pension expenses, largely due to an increase in the number of part-rate pension recipients and a decrease in the population projection for people eligible to receive Age Pension;

- a $260 million reduction in expenses for the Pharmaceutical Benefits Scheme due to lower than expected growth in certain drug groups including anti-inflammatory, cholesterol lowering and psycho analeptic drugs;

- a $186 million reduction in Disability Support Pension payments, largely due to increased workforce participation resulting in a revised forecast of growth in recipient numbers;

- a $178 million reduction in Youth Allowance expenses, largely due to lower than estimated take up by new apprentices; and

- the regular draw-down of the conservative bias allowance[1] reducing estimated expenses in 2006-07 by around $1 billion.

The above decreases in expenses are partially offset by:

- a $200 million increase in 2006-07 due to the re-scheduling of the acquisition, maintenance and logistics support of defence weapon platforms originally planned to take place in 2005-06;

- a $190 million increase in spending on the Investing in Our Schools programme largely due to funding being brought forward from calendar year 2008 to calendar year 2006 to meet stronger than expected demand; and

- a $188 million increase in estimated civilian superannuation expenses, largely due to changes in demographics such as improved life expectancy of members.

In 2005-06, estimated expenses have decreased by $1 billion since MYEFO. This largely reflects parameter and other variations, including a $323 million reduction in civilian superannuation expenses and a $298 million reduction in estimated expenses for the Water Smart Australia and Raising National Water Standards programmes. These decreases have been partially offset by new spending of $2 billion, including $444 million for the Government's response to Cyclone Larry, $354 million for a one-off lump sum payment to eligible carers and $270 million for the Australian Rail Track Corporation to improve rail track quality on the North-South rail corridor.

More detailed information on expenses can be found in Statement 6. A full description of all policy measures since MYEFO can be found in Budget Paper No. 2, *Budget Measures 2006-07*.

Variations in net capital investment estimates

In 2006-07, forecast net capital investment has increased by $780 million since the 2005-06 MYEFO. This represents the combined effect of:

- new policy measures of $398 million, including $136 million for national security and counter-terrorism measures and $70 million for the upgrade of information technology systems for the Department of Immigration and Multicultural Affairs as part of the Government's response to the Palmer and Comrie reports; and

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1 The forward estimates include an allowance for the established tendency of existing Government policy (particularly demand driven programmes) to be higher than estimated in the forward years. To offset this, the contingency reserve includes an allowance based on past experience to preserve the overall integrity of the forward estimates. This allowance, known as the conservative bias allowance, is progressively reduced so that the budget year conservative bias is zero by budget night.

- parameter and other variations of $382 million, including $100 million for the purchase of items in the national medical stockpile delayed from 2005-06 as a result of increased worldwide demand for antivirals and personal protective equipment resulting from the spread of avian influenza in Europe, Asia and Africa, and $56 million for the re-scheduling from 2005-06 of capital works relating to the security upgrade of overseas missions.

In 2005-06, estimated net capital investment has decreased by $306 million since MYEFO, largely reflecting $100 million due to the above mentioned delay in the purchase of items in the national medical stockpile and $65 million relating to the above mentioned re-scheduling of capital works for the security upgrade of overseas missions.

CASH FLOWS

In 2006-07, an underlying cash surplus of $10.8 billion is expected, compared with the MYEFO estimate of $9.7 billion. While the 2006-07 cash balance has increased by $1.1 billion since MYEFO, the fiscal balance has increased by only $0.6 billion. This difference between the change in the underlying cash balance and the fiscal balance is largely attributable to increased superannuation expenses which do not have a cash impact and increased road funding where the cash impact occurs in 2005-06 but is expensed in 2006-07 to 2009-10.

Table 3 provides a summary of Australian Government general government sector cash flows.

Table 3: Summary of Australian Government general government sector cash flows[(a)]

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$b	$b	$b	$b	$b
Cash receipts					
Operating cash receipts	222.2	230.7	239.3	250.5	263.9
Capital cash receipts(b)	0.2	0.2	0.2	0.2	0.1
Total cash receipts	222.4	230.8	239.5	250.7	264.0
Cash payments					
Operating cash payments	204.6	214.7	224.2	234.2	247.1
Capital cash payments(c)	2.9	3.5	2.7	2.8	2.6
Total cash payments	207.5	218.2	226.9	237.0	249.7
Finance leases and similar arrangements(d)	0.0	0.0	0.0	-0.3	0.0
GFS cash surplus(+)/deficit(-)	**14.9**	**12.6**	**12.6**	**13.3**	**14.3**
Per cent of GDP	1.6	1.2	1.2	1.2	1.2
less Future Fund earnings	0.1	1.8	2.0	2.1	2.3
Underlying cash balance(e)	**14.8**	**10.8**	**10.6**	**11.2**	**12.0**
Per cent of GDP	1.5	1.1	1.0	1.0	1.0
Memorandum items:					
Net cash flows from investments in financial assets for policy purposes(f)	-1.4	24.9	-1.9	-2.0	-2.0
plus Future Fund earnings(g)	0.1	1.8	2.0	2.1	2.3
Headline cash balance	**13.5**	**37.5**	**10.7**	**11.4**	**12.3**

(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 from 2005-06 onwards.
(f) Under the cash budgeting framework, these cash flows were referred to as net advances.
(g) The earnings assume the gross proceeds from the sale of Telstra are transferred to the Future Fund. The Fund is assumed to earn a rate of return initially equal to the yield on other term deposits held by the Government then increasing to a rate consistent with the benchmark return specified in the Government's investment mandate. The earnings exclude capital gains which are reflected in the statement of other economic flows (Table B4).

Table 4 provides a reconciliation of the variations in the underlying cash balance estimates.

Table 4: Reconciliation of Australian Government general government sector underlying cash balance estimates

	Estimates		Projections	
	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m
2005-06 Budget underlying cash balance	**8,921**	**7,933**	**8,500**	**9,284**
Changes from 2005-06 Budget to MYEFO				
Effect of policy decisions(a)	-1,829	-1,427	-1,202	-1,252
Effect of parameter and other variations	4,360	3,196	2,836	2,693
Total variations	**2,531**	**1,769**	**1,634**	**1,440**
2005-06 MYEFO underlying cash balance	**11,452**	**9,702**	**10,134**	**10,725**
Changes from MYEFO to 2006-07 Budget				
Effect of policy decisions(a)	-5,171	-11,411	-14,212	-15,161
Effect of parameter and other variations	8,524	12,537	14,707	15,661
Total variations	**3,353**	**1,126**	**495**	**500**
2006-07 Budget underlying cash balance(b)	**14,805**	**10,828**	**10,628**	**11,225**

(a) Excludes the public debt net interest effect of policy measures.
(b) Excludes expected Future Fund earnings from 2005-06 onwards.

Headline cash balance

A headline cash surplus of $37.5 billion is now forecast for 2006-07 compared with a surplus of $36.2 billion at MYEFO. The increase in the headline cash surplus estimate since MYEFO largely reflects the increase in the underlying cash balance plus the inclusion of expected Future Fund earnings.

NET DEBT AND NET WORTH

Net debt has now been eliminated and with the budget remaining in surplus in the forward years, net debt is expected to stay below zero. From its peak of 18.5 per cent of GDP in 1995-96, net debt is estimated to fall to -$22.1 billion in 2006-07 (-2.2 per cent of GDP). Net worth is also expected to continue to strengthen and is projected to become positive in 2008-09.

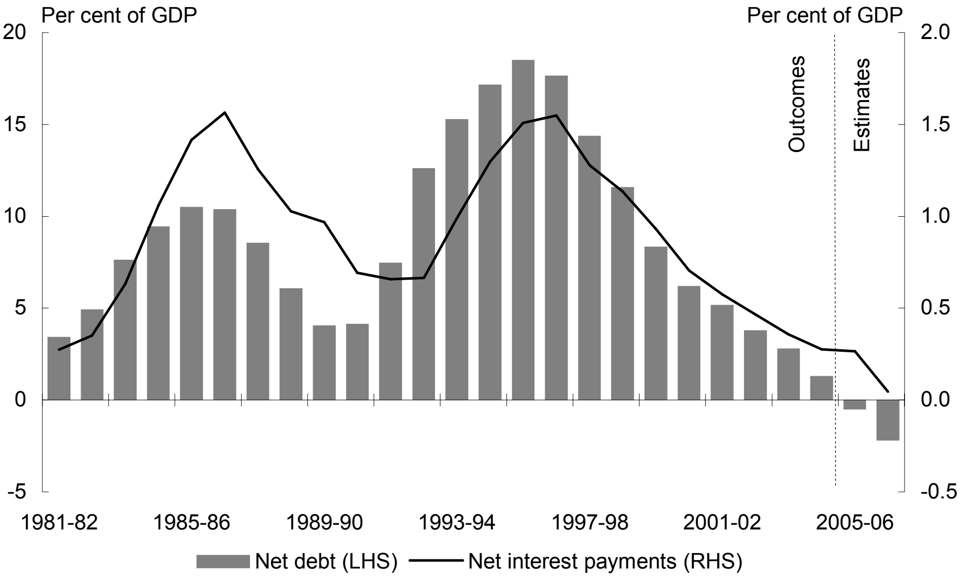
Table 5 and Chart 1 provide a summary of Australian Government general government sector net worth, net debt and net interest payments.

Table 5: Australian Government general government sector net worth, net debt and net interest payments

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$b	$b	$b	$b	$b
Financial assets	133.6	147.1	163.0	178.3	194.5
Non-financial assets	43.9	45.5	45.6	46.2	46.3
Total assets	**177.5**	**192.6**	**208.6**	**224.5**	**240.8**
Total liabilities	**201.5**	**204.6**	**210.9**	**215.7**	**219.1**
Net worth	**-24.0**	**-12.0**	**-2.3**	**8.8**	**21.6**
Net debt(a)(b)	**-4.8**	**-22.1**	**-24.7**	**-37.1**	**-50.2**
Per cent of GDP	-0.5	-2.2	-2.4	-3.4	-4.3
Net interest payments	**2.5**	**0.5**	**0.3**	**-0.2**	**-0.9**
Per cent of GDP	0.3	0.0	0.0	0.0	-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 further sale of the Australian Government's shareholding in Telstra and the establishment of the Future Fund. It is assumed that the Future Fund is initially invested in term deposits but will increasingly be invested in equities until it reaches a portfolio equity allocation consistent with the benchmark return specified in the Government's investment mandate.

Chart 1: Australian Government general government sector net debt and net interest payments



Source: Data are from ABS cat. no. 5501.0, Australian Government Final Budget Outcomes and Treasury estimates.

Over the forward years net debt is expected to fall further, primarily reflecting the assumption that the full sale of Telstra, Medibank Private and Snowy Hydro are achieved in 2006-07. Transfer of Telstra proceeds to the Future Fund has been adopted as an estimation assumption.

The net debt projections have changed since MYEFO largely reflecting assumptions regarding the financial asset composition of the Future Fund. The estimates assume the Fund is initially invested in term deposits and then gradually moves to a portfolio equity allocation consistent with the benchmark return specified in the Government's investment mandate. The assumptions are for estimates purposes only and are not intended to guide 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 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.

With the budget remaining in surplus, Australian Government general government sector net worth is expected to improve to -$12.0 billion in 2006-07 compared with -$16.9 billion at MYEFO. Net worth over the forward estimates is expected to continue to improve and, for the first time, is projected to be positive in 2008-09.

MEDIUM-TERM FISCAL OUTLOOK

Fiscal policy in a medium term setting

Since coming to office in 1996 the Government has adhered to a medium-term fiscal strategy that has delivered strong fiscal outcomes and supported economic growth. This strategy is based on the high level principles of fiscal management contained in the *Charter of Budget Honesty Act 1998* (the Charter). These principles require the Government to focus on financial and economic risks and the impact of fiscal decisions on future generations. For example, high debt levels reduce the ability of governments to respond to macroeconomic shocks and impose repayment burdens on future generations. With net debt now eliminated, investors and consumers have greater certainty about the stability of future government finances, thus creating an environment more conducive to investment and economic growth. The medium-term fiscal strategy provides the community with the same sound policy anchor that inflation targeting provides for monetary policy.

The Government's medium-term fiscal strategy ensures that budget commitments are affordable beyond the forward estimates period. Sound fiscal policy provides investors and consumers with confidence in the Government's fiscal intentions and ability to manage prevailing fiscal risks. The longer term fiscal risk was analysed in the Intergenerational Report 2002-03 (2002 IGR) and will be updated in future intergenerational reports that are required under the Charter.

Fiscal policy since the 2002 Intergenerational Report

The 2002 IGR raised community awareness of the demographic pressures Australia is likely to face over the long term. The 2002 IGR projected that if existing policies and demographic trends remain unchanged, a gradual fiscal adjustment of around 5 per cent of GDP would be required to meet these future commitments. The Government has subsequently introduced several policy measures designed to improve the sustainability of government finances and avoid costly burdens being placed on future generations. Moderate reforms today will reduce the need for drastic policy solutions in the future.

The Government has achieved strong fiscal outcomes over recent years which have allowed the Government to eliminate net debt and establish the Future Fund. Funding the Australian Government's superannuation liability now will reduce future pressures on the budget at a time when the budget will be facing the spending challenges associated with an ageing population.

In addition, the Government has taken steps to address the fiscal challenges posed by the 2002 IGR. These include increasing patient co-payments for the Pharmaceutical Benefits Scheme and requiring a mandatory 12.5 per cent price reduction for generic drugs. The Government has also taken steps to reduce the growth in the Disability Support Pension. While the cost of these programmes is higher today than originally projected in the 2002 IGR, these reforms have reduced their rate of growth.

Given the longer-term pressures identified in the 2002 IGR, previous budget papers have identified the importance of trends in population growth, work force participation and productivity growth in influencing economic outcomes and overall wellbeing. Policies to support economic growth through increased participation and productivity are essential to meet the demographic challenges.

Importantly for the fiscal strategy, the ageing population is expected to lead to lower labour force participation. The Government is taking steps to address this through initiatives such as the Welfare to Work package, which contained a comprehensive package of measures designed to increase incentives to enter the work force and reduce reliance on welfare. The unemployment rate is currently around the level projected in the 2002 IGR and participation rates in some groups have also been higher. The Government's workplace reforms provide the opportunity for even lower unemployment rates in the future.

Over the last four years, productivity growth has slowed to around the trend level projected in the 2002 IGR. Many of the Government's policies are aimed at improving productivity, such as a more flexible labour market flowing from the Government's Work Choices reforms and the tax reforms aimed at encouraging more efficient allocation of investment. The National Reform Agenda outlined at the February 2006 Council of Australian Governments also provides a framework for delivering further competition, regulatory and human capital reforms.

Continued strong economic and fiscal performance is essential over the medium term as the population ages. Responsible fiscal management, and the elimination of net debt, along with the introduction of several important policy measures in recent years aimed at increasing participation and productivity means that Australia is taking steps now to deal with the future challenges.

APPENDIX A: REPORTING STANDARDS

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

The major external standards used for budget 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 budget tables, with the exception of tables in Statement 9, 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 2 of Statement 8.

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 the 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 SDR's as a liability, the current approach will remain in place at least until this update is finalised.

Similarly, 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 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.

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. The update of the statistical standard is expected to change the treatment of defence weapons to assets and the current treatment will remain in place at least until the update is finalised.

Additional information on the reporting standards and budget concepts is provided in Statement 8.

APPENDIX B: 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 Appendix A.

Table B1: Australian Government general government sector operating statement

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Revenue					
Taxation revenue	208,085	217,157	226,076	236,741	249,452
Current grants and subsidies	0	0	0	0	0
Sales of goods and services	4,898	4,846	4,975	5,114	5,255
Interest income	2,386	3,717	3,457	4,005	4,647
Dividend income	4,321	2,701	2,866	3,058	3,228
Other	3,173	3,241	3,297	3,160	3,021
Total revenue	**222,864**	**231,662**	**240,671**	**252,078**	**265,603**
Expenses					
Gross operating expenses					
Depreciation	2,041	2,243	2,385	2,465	2,492
Superannuation	2,472	2,551	2,600	2,690	2,783
Salaries and wages	12,627	13,715	13,822	13,941	14,266
Payment for supply of goods and services	49,126	53,857	55,340	56,653	59,115
Other operating expenses	2,106	2,632	2,717	2,926	3,006
Total gross operating expenses	*68,372*	*74,998*	*76,864*	*78,675*	*81,663*
Nominal superannuation interest expense	5,583	5,784	5,870	6,077	6,289
Other interest expenses	4,084	3,900	3,833	3,678	3,634
Other property expenses	0	0	0	0	0
Current transfers					
Grant expenses	40,264	42,011	44,203	45,568	46,535
Subsidy expenses	6,343	7,268	7,523	7,953	7,870
Personal benefit payments in cash	77,332	81,108	87,303	93,684	102,261
Other current transfers	0	0	0	0	0
Total current transfers	*123,938*	*130,387*	*139,030*	*147,205*	*156,667*
Capital transfers	4,040	4,661	4,960	5,275	4,340
Total expenses	**206,018**	**219,730**	**230,556**	**240,910**	**252,592**
Net operating balance	**16,847**	**11,933**	**10,115**	**11,168**	**13,010**
Net acquisition of non-financial assets					
Purchases of non-financial assets	2,860	3,317	2,679	3,012	2,648
less Sales of non-financial assets	203	152	233	155	122
less Depreciation	2,041	2,243	2,385	2,465	2,492
plus Change in inventories	148	521	91	88	68
plus Other movements in non-financial assets	117	199	23	122	-63
Total net acquisition of non-financial assets	**881**	**1,642**	**174**	**602**	**38**
Net lending/fiscal balance(a)	**15,966**	**10,290**	**9,940**	**10,566**	**12,972**

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

Table B2: Australian Government general government sector balance sheet

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Assets					
Financial assets					
Cash and deposits	1,785	1,242	1,801	2,870	3,262
Advances paid	21,471	22,941	24,626	26,410	28,259
Investments, loans and placements	47,042	62,241	64,468	74,053	83,992
Other non-equity assets	19,758	20,010	20,244	20,564	21,877
Equity(a)	43,535	40,652	51,894	54,379	57,101
Total financial assets	*133,591*	*147,086*	*163,033*	*178,276*	*194,491*
Non-financial assets					
Land	6,089	6,112	6,099	6,069	5,991
Buildings	13,469	13,875	13,689	14,152	14,649
Plant, equipment and infrastructure	8,595	9,063	9,091	9,056	8,874
Inventories	4,625	5,146	5,236	5,324	5,392
Heritage and cultural assets	7,723	7,753	7,767	7,777	7,795
Other non-financial assets	3,361	3,546	3,694	3,825	3,572
Total non-financial assets	*43,861*	*45,493*	*45,575*	*46,204*	*46,273*
Total assets	**177,452**	**192,579**	**208,608**	**224,480**	**240,764**
Liabilities					
Deposits held	405	405	405	405	405
Advances received	0	0	0	0	0
Government securities(a)	59,547	58,356	60,164	60,237	59,428
Loans	5,264	5,293	5,318	5,008	4,994
Other borrowing	297	296	265	542	501
Superannuation liability	95,947	99,597	103,171	106,814	110,512
Other employee entitlements and provisions	8,001	8,207	8,372	8,599	8,878
Other non-equity liabilities	32,016	32,428	33,243	34,092	34,413
Total liabilities	**201,478**	**204,580**	**210,938**	**215,697**	**219,132**
Net worth(b)	**-24,026**	**-12,001**	**-2,330**	**8,783**	**21,632**
Net debt(c)(d)	-4,784	-22,075	-24,743	-37,140	-50,184

(a) Equity includes the valuation of the Telstra shareholding in 2005-06, which is valued at the average of the daily share price over a 90-day period

(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 further sale of the Australian Government's shareholding in Telstra and the establishment of the Future Fund. It is assumed that the Future Fund is initially invested in term deposits but will increasingly be invested in equities until it reaches a portfolio equity allocation consistent with the benchmark return specified in the Government's investment mandate.

Table B3: Australian Government general government sector cash flow statement[(a)]

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Cash receipts from operating activities					
Taxes received	204,469	213,188	221,974	232,477	245,056
Receipts from sales of goods and services	5,189	5,008	5,137	5,297	5,427
Grants and subsidies received	0	0	0	0	0
Interest receipts	2,275	3,498	3,316	3,787	4,379
Dividends	4,341	3,000	2,866	3,058	3,228
GST input credits received by general government	2,973	3,027	2,988	2,996	3,058
Other receipts	2,928	2,944	3,003	2,893	2,723
Total operating receipts	**222,176**	**230,665**	**239,284**	**250,508**	**263,872**
Cash payments for operating activities					
Payments for goods and services	-51,849	-57,615	-58,477	-59,745	-62,266
Grants and subsidies paid	-51,535	-52,052	-54,327	-55,674	-56,928
Interest paid	-4,810	-3,950	-3,619	-3,544	-3,451
Personal benefit payments	-76,343	-80,168	-86,472	-93,328	-102,072
Salaries, wages and other entitlements	-17,606	-18,437	-18,695	-19,049	-19,573
GST payments by general government to taxation authority	-86	-79	-81	-82	-85
Other payments for operating activities	-2,332	-2,406	-2,533	-2,774	-2,750
Total operating payments	**-204,561**	**-214,706**	**-224,204**	**-234,196**	**-247,125**
Net cash flows from operating activities	**17,614**	**15,959**	**15,080**	**16,312**	**16,747**
Cash flows from investments in non-financial assets					
Sales of non-financial assets	224	154	233	155	122
Purchases of non-financial assets	-2,939	-3,496	-2,695	-2,808	-2,577
Net cash flows from investments in non-financial assets	**-2,715**	**-3,342**	**-2,462**	**-2,652**	**-2,456**
Net cash flows from investments in financial assets for policy purposes	**-1,390**	**24,869**	**-1,923**	**-1,976**	**-2,028**
Cash flows from investments in financial assets for liquidity purposes					
Increase in investments	-12,346	-37,424	-12,144	-10,620	-11,092
Net cash flows from investments in financial assets for liquidity purposes	**-12,346**	**-37,424**	**-12,144**	**-10,620**	**-11,092**
Cash flows from financing activities					
Advances received (net)	0	0	0	0	0
Borrowing (net)	-1,754	-838	2,114	29	-684
Deposits received (net)	0	0	0	0	0
Other financing (net)	577	234	-105	-24	-95
Net cash flows from financing activities	**-1,177**	**-604**	**2,009**	**5**	**-779**
Net increase/decrease in cash held	**-15**	**-543**	**559**	**1,069**	**392**

Table B3: Australian Government general government sector cash flow statement[(a)] (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Net cash from operating activities and investments in non-financial assets	**14,899**	**12,617**	**12,617**	**13,659**	**14,292**
Finance leases and similar arrangements(b)	-12	-23	-6	-325	-6
GFS cash surplus(+)/deficit(-)	**14,888**	**12,594**	**12,611**	**13,334**	**14,286**
less Future Fund earnings	83	1,766	1,983	2,109	2,267
Equals underlying cash balance(c)	**14,805**	**10,828**	**10,628**	**11,225**	**12,019**
plus net cash flows from investments in financial assets for policy purposes	-1,390	24,869	-1,923	-1,976	-2,028
plus Future Fund earnings	83	1,766	1,983	2,109	2,267
Equals headline cash balance	**13,497**	**37,463**	**10,688**	**11,359**	**12,258**

(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 B4: Australian Government general government sector statement of other economic flows (reconciliation of net worth)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Opening net worth	**-31,979**	**-24,026**	**-12,001**	**-2,330**	**8,783**
Opening net worth adjustments(a)	-129	0	0	0	0
Adjusted opening net worth	**-32,108**	**-24,026**	**-12,001**	**-2,330**	**8,783**
Change in net worth from operating transactions	**16,847**	**11,933**	**10,115**	**11,168**	**13,010**
Change in net worth from other economic flows					
Revaluation of equity(b)	-6,561	1,711	1,399	1,515	1,607
Net writedowns of assets (including bad and doubtful debts)	-1,858	-2,071	-2,092	-1,854	-2,039
Assets recognised for the first time	8	26	18	19	30
Liabilities recognised for the first time	0	0	0	0	0
Actuarial revaluations	-1,716	0	0	0	0
Net foreign exchange gains	85	-1	0	0	0
Net swap interest received	138	110	86	74	58
Market valuation of debt	696	333	261	166	133
Other economic revaluations(c)	443	-17	-116	25	49
Total other economic flows	**-8,765**	**93**	**-445**	**-55**	**-163**
Closing net worth	**-24,026**	**-12,001**	**-2,330**	**8,783**	**21,632**

(a) Adjustments in opening net worth arise from a change in 2004-05 outcomes for the Australian Taxation Office and the Department of Defence and the impact of moving to new international accounting standards.
(b) Revaluations of equity reflects changes in the market valuation of commercial entities, including a change in the value of the Telstra shareholding which is valued at the average of the daily share price over a 90-day period in 2005-06 only. This line also reflects any revaluations at the point of disposal or sale.
(c) Largely reflects revaluation of assets and liabilities.

APPENDIX C: 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 C1. 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 C1: Sensitivity of expenses and revenue to changes in economic parameters

	2006-07 $m	2007-08 $m	2008-09 $m	2009-10 $m
Expenses				
Prices(a)	710	820	820	840
Wages	110	470	490	520
Unemployment benefit recipients	260	260	280	290
Revenue				
Prices	70	150	160	170
Wages	1,120	1,180	1,250	1,340
Employment	1,440	1,520	1,610	1,730
Private final demand	260	270	270	280
Profit	350	650	700	740

(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 budget documents.

EXPENSES

On the expenses side, the sensitivity analysis of the estimates provides for the following assumptions about changes to three 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 September quarter 2006, 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 superannuation interest expense).

Wages

All wage and salary growth rates are assumed to change by one percentage point in the September quarter 2006, 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. This effect on pensions is smaller in the budget year than in each of the forward years due to the timing of adjustments to pension rates. The wages effect in Table C1 above does not include changes to wage and salary payments in Australian Government departmental expenses.

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

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

REVENUE

Prices

All price deflators are assumed to change by one percentage point at the start of the September quarter 2006, with wage deflators left unchanged.

- A change in prices affects revenue primarily through changes in other excise.

Wages

All wage and salary growth rates are assumed to change by one percentage point from the beginning of the September quarter 2006, 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 September quarter 2006, 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 September quarter 2006, 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 September quarter 2006.

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

STATEMENT 3: ECONOMIC OUTLOOK

This statement presents the economic forecasts that underlie the budget estimates.

STATEMENT 3: ECONOMIC OUTLOOK

The Australian economy is expected to strengthen in 2006-07, with the world economy continuing to provide significant impetus to Australia's economic growth. Strong global demand for commodities is boosting business investment, supporting growth in corporate profits and household incomes, and establishing conditions favourable to increasing exports. Gross national expenditure growth is forecast to remain moderate, with growth in business investment offsetting slower growth in household consumption and a modest decline in dwelling investment. After a period of strength, employment growth is forecast to ease in 2006-07, and inflation is expected to remain moderate.

OVERVIEW

The **Australian economy** continued to record modest growth in the second half of 2005, with robust growth in business investment and moderate growth in household consumption offset by a fall in dwelling investment and sluggish growth in exports. Partial indicators point to a strengthening in activity in early 2006. Real GDP is forecast to grow by 3¼ per cent in 2006-07, up from 2½ per cent in 2005-06. The sources of growth are expected to continue to shift from the domestic sector to the external sector, although at a slower pace than anticipated in the *Mid-Year Economic and Fiscal Outlook 2005-06*.

Gross national expenditure is forecast to grow by 3½ per cent in 2006-07. Household consumption growth is expected to remain moderate, as households continue to experience a period of weaker growth in dwelling wealth. Dwelling investment is forecast to subtract marginally from GDP growth, but growth in business investment should continue to support economic activity. The outlook for export growth is positive, underpinned by the significant investment undertaken to boost productive capacity, particularly in the mining sector. Import growth is forecast to moderate from the recent strong rates of growth.

The combination of sharp increases in the prices of mineral commodity exports and moderate growth in the prices of many imported consumption and capital goods has significantly increased the purchasing power of Australian households and businesses. However, Australia's terms of trade are expected to change little in 2006-07 as commodity price growth eases, leading to lower growth in domestic income from external sources.

The current account deficit is expected to widen to 6¼ per cent of GDP in 2006-07. While the trade deficit is expected to be broadly unchanged in 2006-07, the net income deficit is forecast to increase in line with growth in the stock of net foreign liabilities. Net income payments to the rest of the world are expected to rise as increased dividends and retained earnings accrue to foreign investors in Australia's mining sector, and interest payments are made on a larger stock of net foreign debt.

Employment is anticipated to grow a little below trend in 2006-07, as the labour market responds to the recent weakness in GDP growth. The unemployment rate is expected to be around 5¼ per cent in 2006-07. Wage growth should remain solid, given continuing strong demand for labour in some sectors of the economy.

Inflation is forecast to remain moderate in 2006-07. Expected moderate growth in import prices, together with below-trend growth in household consumption, should see inflation remain contained. High oil prices and relatively strong unit labour costs are expected to partly offset these moderating influences on inflation.

The **world economy** is expected to continue to expand at a strong rate, with world GDP forecast to increase by 5 per cent in 2006 and 4¾ per cent in 2007. The positive global outlook reflects expectations for continued trend growth in the United States, strong growth in China, increasingly solid growth in Japan and a continuation of the moderate recovery underway in Europe.

On the domestic front, **household consumption** growth is forecast to strengthen slightly to 3 per cent in 2006-07. This is well below the growth rates recorded earlier this decade when households allowed consumption growth to run ahead of income growth, supported in part by the significant increase in dwelling wealth. With dwelling wealth having increased much more slowly over the past two years, debt servicing requirements increasing, and fuel prices remaining high, consumption growth is likely to remain moderate in the period ahead.

Dwelling investment is expected to fall by 1 per cent in 2006-07, following two years of small declines. The downturn in the current housing cycle is mild by historical standards, and the risk of a sharp fall in house prices appears to have largely abated. Underlying demand for new dwellings is expected to remain stable over the forecast period, with dwelling completions moving broadly in line with demand.

Business investment is expected to continue to be a major contributor to economic activity. After two years of exceptionally strong growth, business investment is forecast to grow by 8 per cent in 2006-07. The high level of activity in the mining sector and healthy corporate finances should see business investment remain at high levels.

Public final demand is forecast to grow by 3¼ per cent in 2006-07, reflecting strong growth in investment by all levels of government. Public consumption is expected to continue to grow at near trend rates.

Net exports are expected to subtract ½ of a percentage point from GDP growth in 2006-07, after subtracting 1 percentage point in 2005-06. Strong growth in non-rural commodity exports, coupled with improved conditions in the rural sector, should see exports grow by 7 per cent in 2006-07. Imports are also forecast to grow by 7 per cent in 2006-07, reflecting the moderation in household consumption growth.

The **terms of trade** reached their highest level in three decades in 2005. Non-rural commodity export prices are expected to be flat in aggregate in 2006-07 after increasing by around 25 per cent per annum in 2004-05 and 2005-06. As a result, the terms of trade are forecast to settle near their current high level.

The **current account deficit** is expected to narrow marginally in 2005-06, to around 6 per cent of GDP, before widening to 6¼ per cent in 2006-07. The trade deficit is expected to be 1¾ per cent of GDP in both 2005-06 and 2006-07. However, the net income deficit is forecast to widen in 2006-07 as strong mining profits result in increased dividends and retained earnings accruing to the rest of the world. Increasing world interest rates and a higher stock of net foreign debt are also anticipated to contribute to the widening net income deficit.

Employment growth is expected to moderate to 1 per cent in 2006-07, in line with the lagged effects of slower GDP growth in 2004-05 and 2005-06. Following a record high in mid-2005, labour force participation is expected to decline gradually over the forecast horizon. The unemployment rate is forecast to be around 5¼ per cent in 2006-07.

Wages are expected to continue to increase solidly, with the Wage Price Index forecast to grow by 4 per cent in 2006-07. The forecast slowing in employment growth in 2006-07 should have a dampening effect on wage growth, although continuing tight conditions in parts of the labour market, particularly those most affected by the mining sector, will prevent wage growth from slowing significantly.

Inflation is expected to remain moderate at 2¾ per cent in 2006-07. In the near term, the direct effect of higher oil prices is expected to continue to contribute to inflation. However, the cyclical upswing in productivity and slow growth in import prices should have a moderating influence on inflation.

In recent years, developments in the economy have been influenced by two very large price movements. The first was a prolonged boom in house prices until the end of 2003 and a subsequent period of little growth in prices. The second is a dramatic increase in the terms of trade stemming from very strong world demand for commodities that has not yet ended. Fortunately, the economy has adjusted remarkably well to these price changes, but some **risks** remain in the aftermath of these developments.

The boom in house prices prompted very strong consumption growth in 2003-04 and 2004-05. Since the end of 2003, house prices have shown only a small increase and consumption growth has moderated accordingly. The risk that house prices fall much further, at least in nominal terms, and trigger a significant weakening in consumer spending appears to have largely abated. Nevertheless, household borrowings have increased significantly and, consequently, debt servicing requirements have also increased. This has left the household sector, and the path of consumption growth, more sensitive to changes in labour market conditions and interest rates. Consumption may also be more vulnerable to adverse movements in external factors such as a further increase in oil prices or even a shock that affects confidence, such as a health or security concern.

High commodity prices have generated a significant amount of additional export income for Australia, although the dampening impact on the economy of flat house prices has helped to weigh against this stimulus. Past terms of trade booms have been associated with very rapid increases in wages and inflation. This scenario has not played out on this occasion, partly reflecting the benefits of a floating exchange rate, an independent monetary policy regime, and competitive labour and product markets (see also Statement 4). While the Australian economy has adjusted well to the dramatic increase in commodity prices, it may also need to adjust to a fall in prices at some stage. The timing and extent of any fall in commodity prices is uncertain and will depend, in part, upon the speed with which additional supply comes to market.

Wage rises associated with higher commodity prices have been confined to the geographical areas where mining operations are concentrated and in those industries most directly affected, such as in the mining and construction sectors. There does remain some risk that the higher wages paid in these sectors will spill over into increased wage demands in other sectors. However, while there has been some broadening in wage pressures more recently, wages still appear well-contained.

Oil prices remain high and volatile. The main effect of higher oil prices to date has been higher automotive fuel prices, which have increased by 20 per cent over the past year. There remains a risk that higher fuel prices, combined with solid wage outcomes, will feed into higher prices for other goods and services.

The forecasts for the rural sector are predicated on an assumption of average seasonal conditions in 2006-07. However, as is always the case, the timing and distribution of rainfall will have an important impact on the prospects for rural production and exports.

In terms of the world economy, the outlook remains positive, though a number of potential risks remain. These risks include global imbalances, high oil prices, increased financial vulnerability and a possible influenza pandemic. Current account imbalances have continued to widen despite favourable conditions for policy makers to undertake reforms. While these imbalances may persist for some time without significant adverse consequences, they increase the vulnerability of the world economy to destabilising changes in financing flows.

Table 1: Domestic economy forecasts[(a)]

	Outcomes(b)	Estimates	Forecasts	
	2004-05 year average	2005-06 year average	2006-07 year average	Four quarters to June 2007
Panel A - Demand and output(c)				
Household consumption	4.2	2 3/4	3	3
Private investment				
Dwellings	-1.5	-3	-1	2
Total business investment(d)	11.7	14	8	11
Non-dwelling construction(d)	7.7	14	6	8
Machinery and equipment(d)	15.4	15	9	13
Private final demand(d)	4.5	4 1/4	3 3/4	4 1/2
Public final demand(d)	4.3	3 1/4	3 1/4	2 1/4
Total final demand	4.4	4	3 1/2	4
Change in inventories(e)				
Private non-farm	-0.3	0	0	0
Farm and public authorities(f)	0.0	0	- 1/4	- 1/4
Gross national expenditure	4.1	4	3 1/2	4
Exports of goods and services	2.5	2	7	6
Imports of goods and services	12.0	6	7	9
Net exports(e)	-2.0	-1	- 1/2	-1
Gross domestic product	2.5	2 1/2	3 1/4	3 1/4
Non-farm product	2.6	2 3/4	3 1/4	3 1/2
Farm product	-0.5	-1	2	-1
Panel B - Other selected economic measures				
External accounts				
Terms of trade	10.0	10	0	-1 1/4
Current account balance				
$billion	-57.6	-56 1/4	-62 1/2	
Percentage of GDP	-6.4	-6	-6 1/4	
Labour market				
Employment (labour force survey basis)	3.0	2	1	1 1/4
Unemployment rate (per cent)(g)	5.3	5 1/4	5 1/4	5 1/4
Participation rate (per cent)(g)	64.0	64 1/2	64 1/4	64 1/4
Prices and wages				
Consumer Price Index	2.4	3	2 3/4	2 1/2
Gross non-farm product deflator	3.9	4 1/2	2 1/2	2 1/4
Wage Price Index	3.8	4	4	3 3/4

(a) Percentage change on preceding year unless otherwise indicated.
(b) Calculated using original data.
(c) Chain volume measures.
(d) Excluding transfers of second-hand assets between the public and private sectors.
(e) Percentage point contribution to growth in GDP.
(f) For presentational purposes, inventories held by privatised marketing authorities are included with the inventories of the farm sector and public marketing authorities.
(g) The estimates in the final column are the forecast rates in the June quarter 2007.
Source: Australian Bureau of Statistics (ABS) cat. no. 5206.0, 5302.0, 6202.0, 6345.0, 6401.0, unpublished ABS data and Treasury.

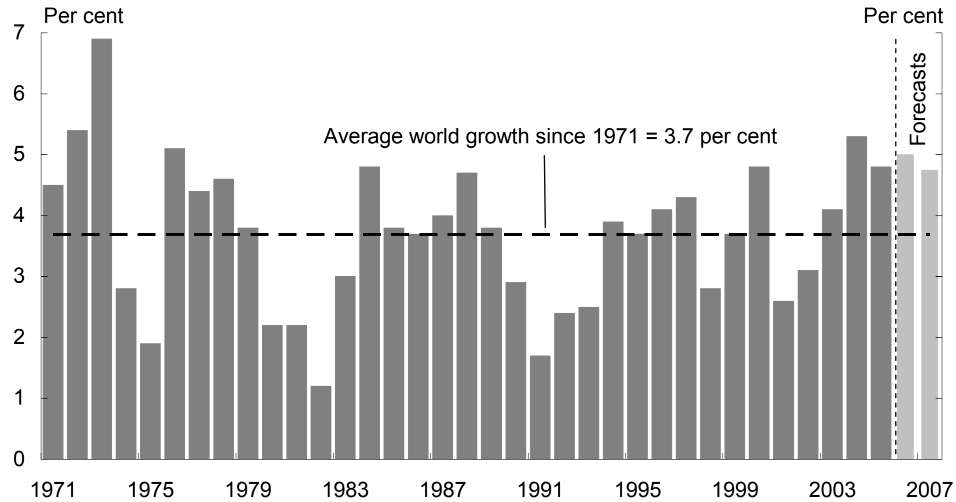
THE OUTLOOK FOR THE INTERNATIONAL ECONOMY

The world economy grew by 4.8 per cent in 2005, slightly below the 5.3 per cent recorded in 2004 (a 30-year high). Growth in 2005 was ¼ of a percentage point higher than expected at *Mid-Year Economic and Fiscal Outlook 2005-06*. A number of economies, including India, Russia and China, posted higher than projected outcomes in 2005.

Despite higher oil prices and the impact of natural disasters, such as the Asian tsunami, South Asia earthquake, and hurricanes Katrina and Rita, the world economy performed strongly in 2005. This resilience was underpinned by benign financial market conditions and strong corporate balance sheets. Over the course of the year, the pattern of growth across countries became more broadly based.

World GDP growth is forecast to continue to expand at a strong rate, by 5 per cent in 2006 and 4¾ per cent in 2007 (Chart 1). Following growth of 4.4 per cent in 2005, growth in Australia's major trading partners is expected to remain strong at 4½ per cent in 2006 and 4¼ per cent in 2007.

Chart 1: World GDP growth(a)



(a) World GDP growth rates are calculated using GDP weights based on purchasing power parity.
Source: International Monetary Fund and Treasury.

Economic growth has remained solid in the **United States**, despite the effects of natural disasters, tightening monetary policy and higher oil prices. Excess capacity continues to diminish, with capacity utilisation reaching its highest level in more than five years, and employment growth continuing at a solid pace.

The outlook for domestic demand in the United States remains positive, with business investment expected to be the key driver, supported in the United States by strong corporate profits and benign financial market conditions. A soft landing looks most probable, but a crucial issue in determining whether the United States economy slows to a sustainable pace remains the speed of the housing slowdown. While the housing market is expected to continue to slow, due to rising mortgage interest rates and a moderation in price growth (Box 1), continuing solid employment growth is likely to prevent a sharp slowdown. Consumption growth is also expected to slow, with the impact of a weaker housing market, higher debt servicing costs and high energy prices expected to offset positive momentum from growth in employment and wages. Higher government spending is anticipated, due to rebuilding in the aftermath of the hurricanes and the continuing costs of military activities in Iraq and Afghanistan.

Headline inflation has picked up in the United States during the last six months, reflecting the effects of higher energy prices. The labour market has tightened which, combined with slower productivity growth, may lead to upward pressure on wages and unit labour costs. However, to date underlying measures of inflation have remained in check and inflation expectations remain well-anchored.

Table 2: International GDP growth forecasts(a)(b)

	Actual	Estimate	Forecasts	
	2004	2005	2006	2007
United States	4.2	3.5	3 1/2	3 1/4
Euro area	2.1	1.4	1 3/4	2
Japan	2.3	2.7	3	2
China	10.1	9.9	9 3/4	9 1/4
Other East Asia(c)	6.2	5.0	5 1/4	5
Major Trading Partners	5.0	4.4	4 1/2	4 1/4
Total OECD	3.3	2.8	3	2 3/4
World	5.3	4.8	5	4 3/4

(a) World, OECD and euro area growth rates are calculated using GDP weights based on purchasing power parity. Calculations for major trading partners and other East Asia use export trade weights.
(b) 2004 estimate adjusted for the number of working days.
(c) Other East Asia consists of Korea, Singapore, Taiwan, Hong Kong, Indonesia, Malaysia, Thailand, and the Philippines.
Source: National statistical publications, IMF and Treasury.

The economic upswing in **Japan** appears to have consolidated, with growth accelerating to 2.7 per cent in 2005 due to strong domestic demand. Growth has been broadly based, in contrast with previous export-led upswings. Employment, corporate profits and bank lending have all risen, and recent partial indicators point to growth being sustained. Increasing confidence in the outlook has also seen the Nikkei stock market index rise by more than 45 per cent over the last year.

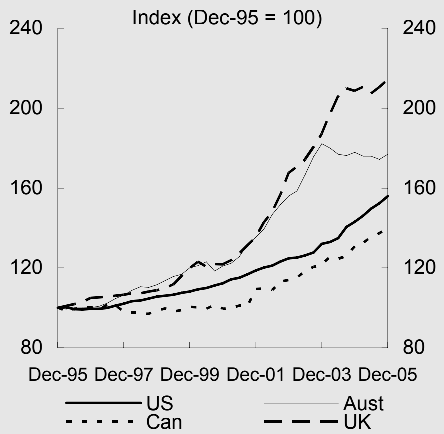
Deflation appears to have ended, with CPI inflation expected to be positive in 2006. The Bank of Japan has ended its quantitative easing policy, and adopted an inflation targeting monetary policy regime. However, official interest rates remain at zero per cent, and the timing and extent of the move to positive interest rates will be key decisions for policy makers in the coming period.

Box 1: International housing prices

Over recent years, house price appreciation has been one of the primary drivers of consumption growth in a number of economies around the world. Real house price growth has been driven by a range of factors including low interest rates and increasing disposable incomes.

Over the decade to December 2005 the growth in real (CPI adjusted) house prices in Canada, the United States and Australia was 40, 56 and 77 per cent respectively. The United Kingdom has experienced the strongest growth with median house prices growing by a very strong 114 per cent in real terms over the past ten years (Chart A).

Chart A: Median prices of existing homes

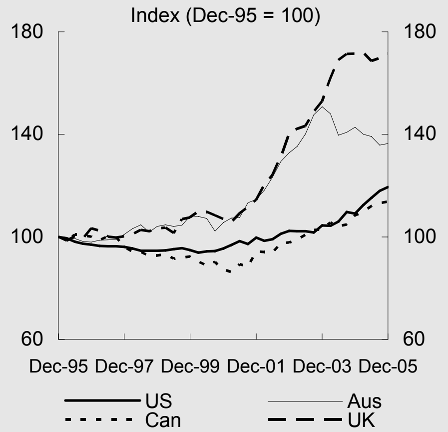


Source: Datastream and Treasury.

While not without shortcomings, the ratio of house prices to disposable income is often used as a simple indicator of housing affordability. Affordability has fallen in each of the four countries since December 1995.

Affordability has decreased the most in the United Kingdom, with the index of house prices to income rising by over 70 per cent in the period from December 1995 to December 2005 (Chart B). The smallest decrease in affordability was in Canada where the index rose by around 14 per cent over the same period.

Chart B: House price to income ratio



Source: Datastream and Treasury.

Australia's housing market was the first to experience a slowing of price growth, followed by the United Kingdom's housing market which has been unwinding over the past eighteen months.

There are fewer signs, mainly from non-price indicators, of a slowdown in the United States housing market and to date little sign of cooling in the Canadian market.

Real house prices appreciated in the year to December 2005 in the United Kingdom, Canada and the United States by 2.7, 7.0 and 8.9 per cent respectively. Over the same period real house prices in Australia fell by 0.5 per cent.

Growth in the **Chinese** economy continues to exceed expectations, with GDP growing by 9.9 per cent in 2005. China was the largest contributor to world growth in 2005. In December 2005 the level of Chinese GDP was revised upwards by 17 per cent, reflecting better measurement of the services sector. China's growth rate is estimated to have been around 10 per cent in each of the past three years.

Economic growth is likely to moderate in 2006, reflecting a lower contribution from the external sector. Growth in domestic demand picked up in late 2005 and is expected to remain strong. The sustainability of high investment growth rates remains a concern, although official data on industrial profits indicate an improvement in margins and strong profit growth.

Risks to the Chinese economy are centred on the success of Chinese authorities' efforts to pursue structural and financial sector reforms while maintaining macroeconomic stability. Financial sector reforms are continuing ahead of the opening up of the sector to foreign banks at the end of 2006, although it remains to be seen how foreign bank entry will affect lending. The management of China's large capital inflows and ongoing exchange rate developments could also affect the broader economic outlook.

Growth in the **rest of East Asia** moderated in 2005 compared to the previous year, with GDP in the region expanding by 5 per cent. After slowing in the first half of 2005, regional growth picked up, driven by rising exports and robust domestic consumption. The favourable global outlook is expected to continue to support growth, particularly the strengthening of demand for information and communication technology exports and stronger import growth in major regional economies such as Japan and China.

The outlook for growth in the **euro area** has remained broadly on track since MYEFO, despite the weak outcome in the December quarter. The expansion has been underpinned by strong credit growth, a depreciating real exchange rate, and strong corporate profits. Activity remains vulnerable to external factors, namely high oil prices and export demand, which affected net exports and household consumption in late 2005. Consumer sentiment remains weak. However, strong investment growth is expected given favourable financing conditions and improved competitiveness associated with the depreciation of the euro. Looking forward, growth is expected to pick up in 2006, and return to around potential in 2007.

Growth in the **United Kingdom** economy moderated in 2005 from the strong pace recorded in 2004. GDP increased by 1.8 per cent, with the deceleration driven by lower consumption growth in response to cooling house price growth (Box 1), monetary policy tightening and higher energy prices. The outlook is for growth to pick up in 2006 and 2007, with consumption growth rebounding as the housing market stabilises.

In addition to the country specific risks outlined above, there are a number of uncertainties associated with the outlook for the world economy. The main risks to the global outlook are global imbalances, high oil prices, increasing financial vulnerability and a possible influenza pandemic.

The recent broadening of world growth, with the consolidation of the Japanese recovery and signs of recovery in Europe, reduces the downside risk posed by previously unbalanced world growth. However, little progress has been made in addressing global imbalances despite improved conditions across a number of regions.

Current account imbalances have continued to rise, with a key component of those imbalances, the United States current account deficit, reaching a record 6.4 per cent of GDP in 2005. The rise in the United States' deficit has been driven by a surging trade deficit, which rose by US$106 billion in 2005. More than a third of the increase in the United States' trade deficit was due to an increase in the deficit with China. This has led to increasing protectionist sentiment and rising pressure from the United States for China to introduce further flexibility into its exchange rate regime. However, a more flexible Chinese exchange rate alone is likely to have only a limited impact on global imbalances and the United States' trade deficit.

While a gradual and orderly unwinding of global imbalances remains the most likely path of adjustment in the medium term, further policy measures are required to ensure this outcome. These policies include: greater focus on long term fiscal sustainability, particularly in countries facing demographic challenges in the near future; rebalancing the focus of activity in some economies from external to domestic demand; structural reforms to improve framework conditions for investment; and in other economies diversifying the industry structure to reduce their reliance on key industries or commodities, such as oil.

However, the longer the imbalances continue, the greater is the potential for a sudden adjustment, triggered by an increase in risk aversion, involving changes in financial asset prices and exchange rates. A sudden adjustment of this sort could have serious implications for global economic activity.

Another key risk to the outlook is the effects of increasing inflationary pressures. World inflationary pressures have remained relatively muted despite strong world growth and high energy prices. However, strong global growth has resulted in diminishing excess capacity, particularly in the United States' labour market. Monetary policy has tightened in a range of countries in response to the threat posed by potential inflationary pressures and as the economic recovery has strengthened and broadened.

While oil and other commodity prices have risen strongly, to date there has been little evidence of significant second-round effects in the major industrialised economies. In most major economies, core inflation is largely unaffected and inflation expectations remain well grounded. In part, this reflects competitive product and labour markets and the success of macroeconomic policy in establishing well-anchored inflation expectations.

However, high and volatile oil prices continue to weigh on the outlook. Recently, oil prices reached record highs of over US$70 per barrel due to market concern about developments in major exporting nations, namely Nigeria and Iran. While price rises between 2002 and early 2005 were largely the result of strong demand for oil, low spare capacity and supply disruptions in the second half of 2005 shifted the market's focus to supply side issues (Box 2).

Looking forward, given the low level of spare capacity there remains a risk of further supply side disruptions, particularly in the event of instability in key oil producing countries. Such disruptions, should they occur, may have a more pronounced impact than the demand driven rises experienced to date.

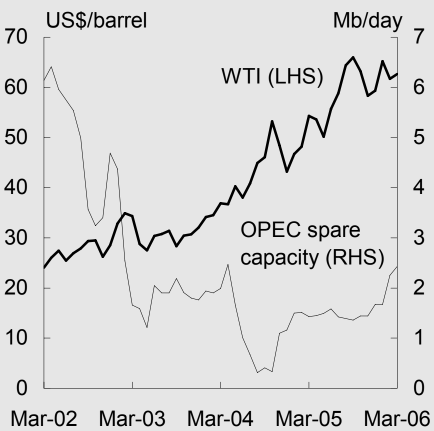
A further risk to the outlook stems from potential vulnerabilities in the global financial system. Financial institutions generally appear healthy and financial markets have performed relatively strongly in recent years. However, the continuing search for yield; the low level of credit risk spreads; high levels of household debt; and more complex financial products, have increased the exposure of the financial system to the negative impacts of an external shock. A shock that led to a reassessment of credit risk appetites or exposed weakness in risk management could have serious implications for real economic activity.

A possible avian influenza pandemic is another risk to the outlook. Whilst the likelihood of an avian flu pandemic is uncertain, potential scenarios indicate significant human and economic costs, particularly in developing countries. Governments and international bodies have expended significant efforts in order to prevent, and mitigate the potential impacts of, a pandemic. However, studies suggest that the most significant economic implications are likely to result from confidence effects, for which preparation is much more difficult.

Box 2: Impact of oil on inflation

Since 2002, West Texas Intermediate (WTI) oil prices have increased by nearly 200 per cent. Much of the increase can be attributed to rapid demand growth, principally from the United States and China. However, recent market concerns have concentrated on supply side factors, including low spare capacity in the Organisation of Petroleum Exporting Countries (OPEC) (Chart A).

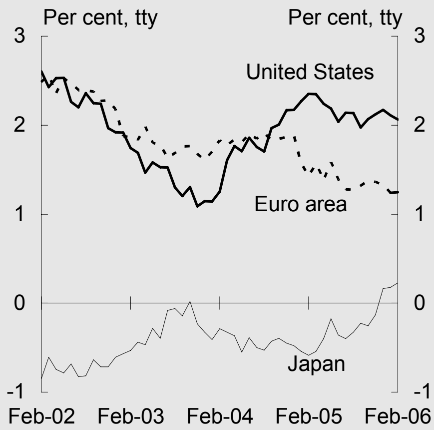
Chart A: WTI price and OPEC spare capacity



Source: Reuters, International Energy Agency.

Despite the rapid increase in oil prices, consumer prices in many of the large oil importing countries have not increased significantly. For example, over the last three years core inflation in the United States, the largest global consumer of oil, has averaged around 2 per cent (Chart B). Rising oil prices appear to have been absorbed by producers rather than being passed on to consumers, with producer prices in key regions increasing more rapidly than consumer prices.

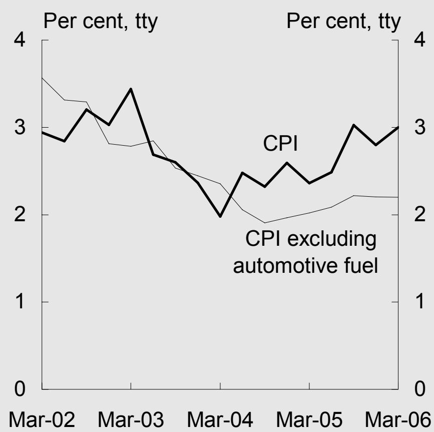
Chart B: CPI excluding food and energy



Source: OECD.

In Australia, higher fuel prices also do not appear to have flowed through to broader price inflation. Although fuel prices have recently been a significant contributor to headline inflation, the CPI excluding automotive fuel has grown at a relatively steady rate of around 2 per cent through the year since mid-2004 (Chart C).

Chart C: CPI excluding fuel



Source: ABS cat. no. 6401.0.

THE OUTLOOK FOR THE DOMESTIC ECONOMY

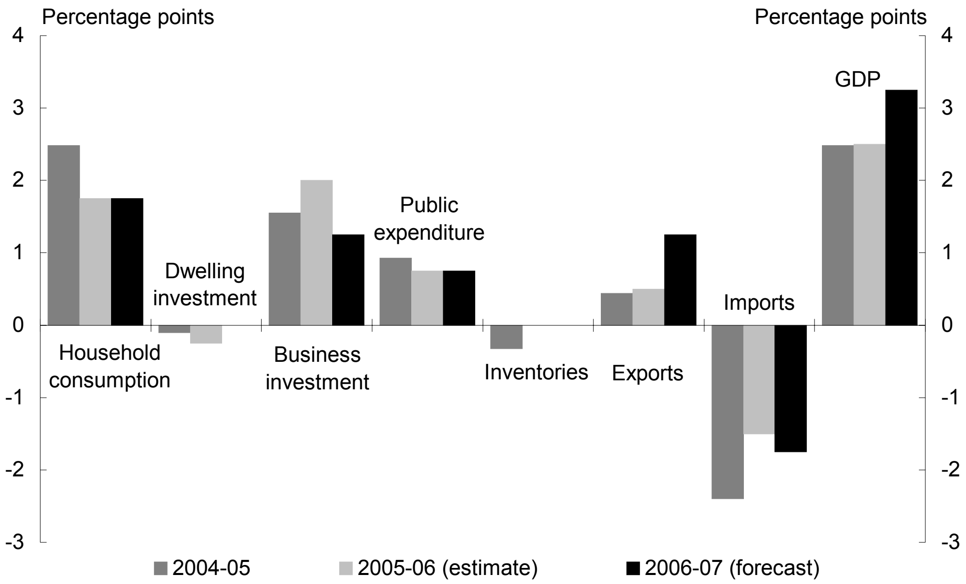
Key assumptions

The forecasts for the domestic economy are underpinned by several technical assumptions. The exchange rate is assumed to remain around the average level of recent months (a trade weighted index of around 63 and a United States dollar exchange rate of around 74 cents). Domestic interest rates are assumed to remain unchanged at current levels. World oil prices (West Texas Intermediate) are assumed to move in line with market expectations and remain above $US70 per barrel throughout the forecast period. The farm sector forecasts are based on an assumption of average seasonal conditions in 2006-07.

Demand and output

A shift in the balance of growth from households to the business and external sectors is changing the composition of demand and output. Household consumption is expected to grow at slightly below trend rates, following several years of strong growth. Dwelling investment experienced a mild downturn in 2005, and is forecast to remain weak for a while longer. In contrast, a favourable business environment and strong global demand should see business investment record its largest contribution to GDP growth in two decades in 2005-06, and further growth is forecast for 2006-07 (Chart 2).

Chart 2: Contributions to GDP growth[(a)]



(a) Excluding transfers of second-hand assets between the public and private sectors.
Source: ABS cat. no. 5206.0 and Treasury.

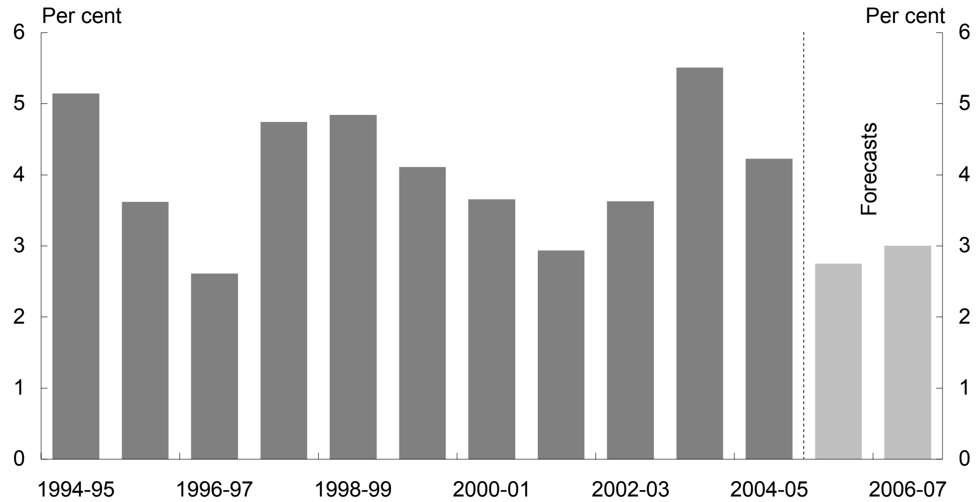
While an acceleration in mining investment has increased export capacity, a series of unanticipated disruptions to the supply chain have constrained export volumes for 2005-06. These include a number of cyclones in the Pilbara region of Western Australia and disruptions to transport infrastructure. In 2006-07, export growth should improve as additional capacity comes on stream and the benefits of better weather conditions in 2005 flow through to rural exports. Import growth is forecast to remain moderate, in line with below-trend growth in household consumption. This is expected to be partly offset by robust demand for capital imports from the business sector.

The non-farm economy is forecast to expand by 2¾ per cent in 2005-06 and 3¼ per cent in 2006-07. Despite a forecast contraction in the farm sector in 2005-06 for the year as whole, rural conditions have recently improved, with farm production increasing by around 8 per cent in the December quarter 2005. Nevertheless, a number of areas remain drought-declared which will continue to restrain growth in the farm sector. Rural production is forecast to grow by 2 per cent in 2006-07, on an assumption of average seasonal conditions.

Household consumption

Household consumption growth is expected to be a little below trend at 2¾ per cent in 2005-06 and 3 per cent in 2006-07 (Chart 3). This growth would deliver an increase in per capita consumption of around 1¾ per cent annually, but it would still represent a substantial slowing from the growth rates seen in 2003-04 and 2004-05.

Chart 3: Growth in household consumption



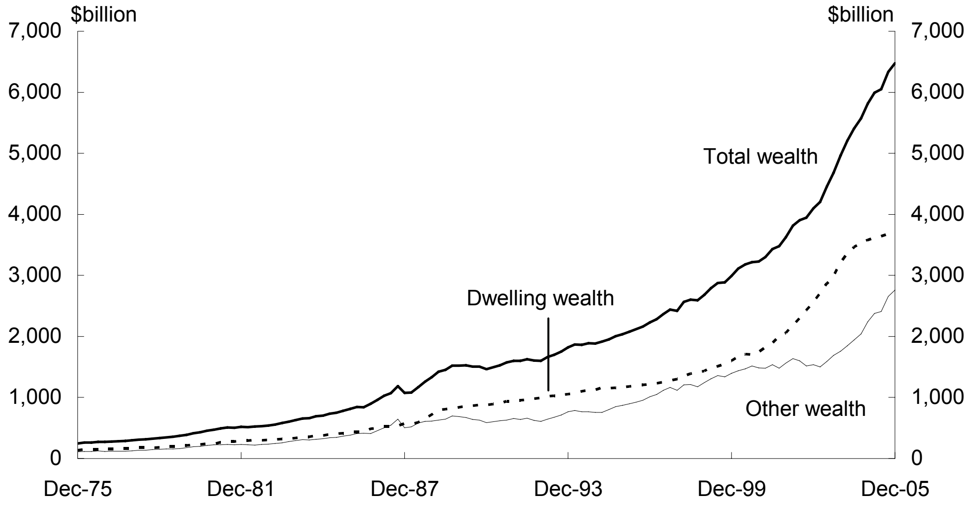
Source: ABS cat. no. 5206.0 and Treasury.

In the years since the early-1990s recession, household consumption spending has been supported by increases in household income associated with the falling unemployment rate. Over this period, the unemployment rate has fallen from a peak of nearly 11 per cent in 1992 to a three-decade low of around 5 per cent today. This long period of relative employment certainty, in combination with low interest rates, has given households the confidence to take on additional debt relative to their income, predominantly for expenditure on housing.

This increased willingness on the part of households to take on debt, and the related boom in house prices in the first part of this decade, has contributed to an increase in average household debt levels and a consequent increase in the household debt servicing ratio (the ratio of interest payments to disposable income) from around 7 per cent in the 1990s to 11 per cent currently. The debt servicing ratio for the household sector as a whole is likely to continue to increase for some time yet, as the debt taken on by new housing market entrants remains considerably higher than the average debt of those currently in the market.

The boom in house prices has contributed to a substantial increase in household wealth in recent years (Chart 4). Nominal household wealth has doubled over the past five years, with real household wealth growing by around 80 per cent over the same period on the back of rising dwelling and non-dwelling wealth. This increase in wealth supported consumption growth in 2003-04 and 2004-05. However, house prices have increased little since the end of 2003, and are assumed to remain unchanged in the forecast period, thus contributing to the more moderate forecast for consumption growth in 2005-06 and 2006-07.

Chart 4: Nominal household wealth



Source: Treasury.

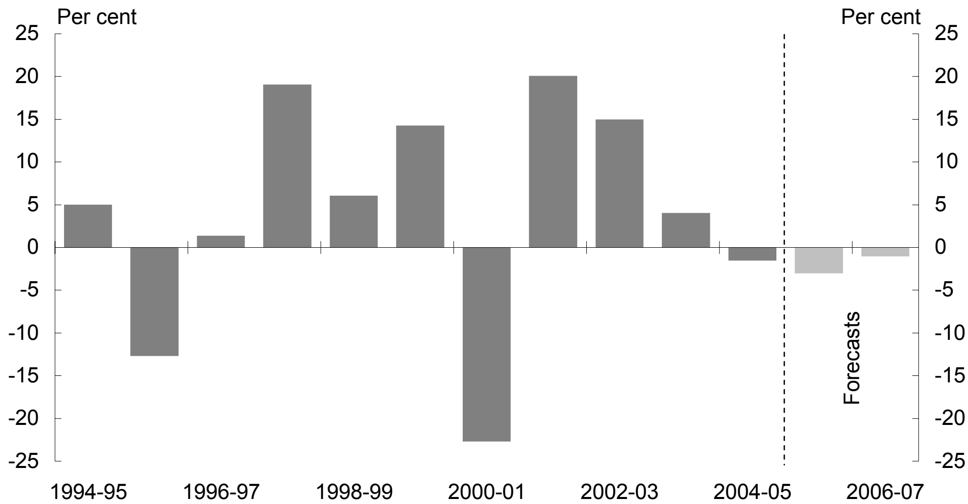
Another factor tending to lower consumption growth relative to recent years is lower forecast employment growth for 2006-07, which will tend to moderate growth in household labour income. But overall growth in household income is likely to remain solid once the effects of budget measures are taken into account. Recent increases in non-dwelling wealth, largely reflecting growth in the stock market, should also support consumption growth in the near term.

While the household sector in aggregate is expected to maintain near-trend consumption growth through 2006-07 despite higher debt servicing, some households are carrying considerably more debt as a proportion of their income than the average. The consumption decisions of these households will be especially sensitive to changes in labour market conditions and interest rates, and to adverse external shocks such as a further increase in world oil prices.

Dwelling investment

The mild downturn in housing construction that began in the latter half of 2004 is expected to continue, with dwelling investment forecast to fall by 3 per cent in 2005-06, and 1 per cent in 2006-07 (Chart 5).

Chart 5: Growth in dwelling investment



Source: ABS cat. no. 5206.0 and Treasury.

Leading indicators of housing construction are mixed — while dwelling approvals suggest weaker activity in the near term, housing finance data point to stronger activity. The picture remains mixed even within the finance data, with owner occupier finance for both established and new housing growing strongly since mid-2004, while investor finance has been weak. The inconsistency in the partial data suggests some uncertainty around the outlook for dwelling investment in the coming months, although any movement in housing activity is likely to be small.

There has been substantial variation in the housing market by State. The Western Australia housing market has been markedly stronger, while the New South Wales housing market has been weak.

Owner occupiers are expected to dominate activity in the housing market in the period ahead. Owner occupiers traditionally purchase a greater proportion of detached houses than investors, thus this segment of the market is expected to remain more buoyant than medium-density construction.

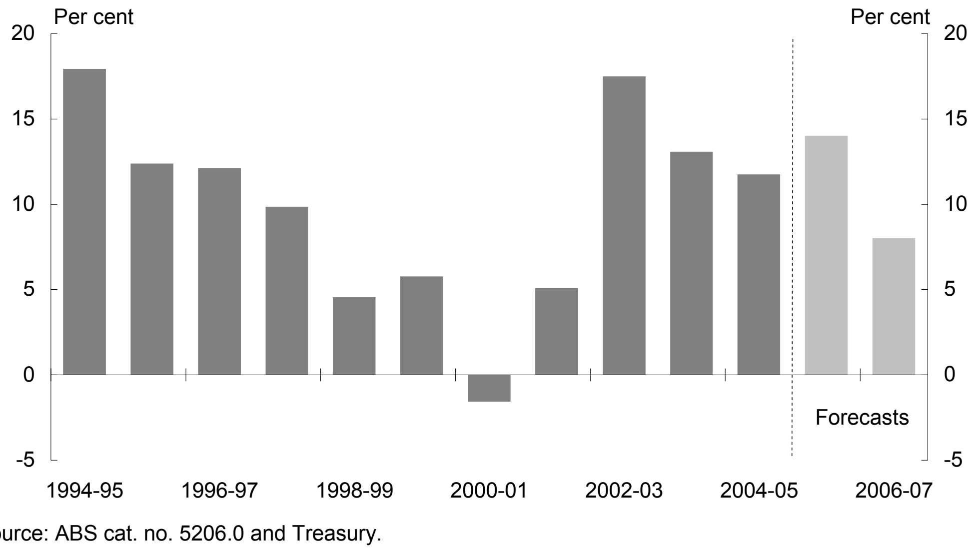
The adjustment to a period of low rental yields, little growth in house prices and an expectation that this may continue for some time is likely to continue to discourage investor activity in the housing market. Moreover, the current strength of the stock market and the possibility of further capital gains are increasing the incentive for investors to shift their capital out of housing.

Business investment

Business investment has been strong for a number of years, growing by 75 per cent over the past four years. This is set to continue, with new business investment forecast to increase by 14 per cent in 2005-06, before moderating to 8 per cent in 2006-07 (Chart 6).

Business conditions remain favourable. Profits are strong, capacity utilisation is high, the cost of capital and corporate debt levels remain low and ongoing demand for Australian commodities is stimulating investment in the resource sector.

Chart 6: Growth in new business investment



Source: ABS cat. no. 5206.0 and Treasury.

New machinery and equipment investment is forecast to grow by 15 per cent in 2005-06 and 9 per cent in 2006-07. The Australian Bureau of Statistics' *Survey of New Capital Expenditure and Expected Expenditure (CAPEX)* indicates that investment intentions have been strong across most industries. The first estimate of investment intentions for plant and equipment for 2006-07 was 6.2 per cent higher (in nominal terms) than the equivalent estimate for 2005-06, a strong result given the recent history of first estimates. Initial estimates of investment intentions for 2006-07 can only provide a broad indication of likely outcomes. While growth in machinery and equipment investment is expected to ease somewhat in 2006-07, it should remain at a high level.

Investment in non-dwelling construction is forecast to grow substantially in 2005-06, increasing by 14 per cent, before moderating to 6 per cent in 2006-07. Strong global demand for resources is expected to support investment activity, particularly in the mining sector. Over the past three years, more than $30 billion has been invested by the mining sector, with a number of major mining and infrastructure projects still in the pipeline. Non-residential building investment is expected to grow at a modest pace, with building approvals data indicating growth in the retail, office and other business premises sectors.

Inventories

Inventories are expected to subtract around ¼ of a percentage point from GDP growth in 2006-07, with private non-farm stocks forecast to remain broadly unchanged.

Farm and public authority inventories (including the inventories of privatised marketing authorities) are expected to be run down in 2006-07, as bumper crop harvests from the past few years enter the grain export system. Grain inventories are expected to reach record highs in 2005-06.

Public final demand

Public final demand is forecast to grow at a trend rate of 3¼ per cent in 2006-07, supported by strong growth in public investment. Following robust growth, public consumption is forecast to moderate in 2006-07.

Net exports

Net exports are expected to subtract 1 percentage point from GDP growth in 2005-06 and ½ of a percentage point in 2006-07. In 2006-07, export growth is forecast to strengthen to 7 per cent, with rural and non-rural commodities being the major contributors to the acceleration (Chart 7). Import growth is also expected be 7 per cent in 2006-07, around the same growth rate as expected for 2005-06, reflecting continuing growth in domestic demand.

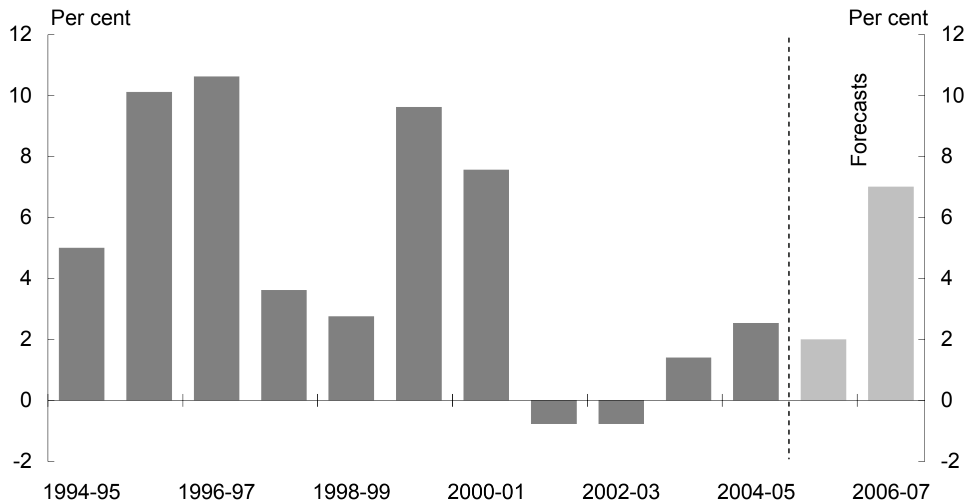
Export growth has been relatively weak since 2001-02, and remains significantly lower than the rates of growth recorded in the 1990s (Box 3). However, most categories of exports are expected to strengthen into 2006-07, especially non-rural commodities.

A number of factors constrained growth in non-rural commodity exports in the second half of 2005, including adverse weather conditions and temporary disruptions to transport infrastructure. In the early part of 2006, the cyclone season hampered the production and export of some commodities to a greater degree than normal, particularly for iron ore, oil and liquefied natural gas. In the absence of these temporary factors, growth is expected to pick up considerably in 2006-07.

The large scale and long lead times involved in new mining investment means that there is some uncertainty around the exact timing of forecast growth in non-rural commodity exports. The impact of the temporary factors described above also means that it is difficult to establish the underlying trend in export volumes. Nevertheless, the continuing strong world demand for commodities and an accounting of the likely increase in export volumes from mining investment already undertaken suggest that volumes will increase significantly in the next few years.

Growth in rural exports is expected to be relatively flat in 2005-06, but rise strongly in 2006-07. Following improved seasonal conditions in the second half of 2005, farmers are taking advantage of good pasture growth and lower feed costs to rebuild their herds. This is expected to reduce slaughtering rates in 2005-06, but facilitate increased production and exports in 2006-07. Following three years of strong grain production, cereal grains exports are also expected to make a significant contribution to the growth in rural exports in 2006-07.

Chart 7: Export growth



Source: ABS cat. no. 5302.0 and Treasury.

Other categories of exports are forecast to pick up 2006-07, although they are unlikely to grow at the strong rates experienced in the 1990s. Exports of elaborately transformed manufactures are forecast to grow moderately over the next two years, but are expected to continue to be hindered by a relatively high exchange rate and the increasing competitiveness of the manufacturing sectors in developing countries, such as China.

Service exports are forecast to improve modestly in 2006-07, after two years of little growth. Competition appears to have intensified in the global tourism industry, with factors such as increasing price competition in the short-haul airline market out of major Asian hubs reported to have adversely affected Australia's travel service exports. This may continue to constrain travel export growth in the near term.

Imports are forecast to increase by 7 per cent in 2006-07. Capital imports are expected to remain buoyant, reflecting the high level of business investment activity. However, below average growth in household expenditure is expected to have a moderating influence on imported consumption goods.

Box 3: Recent export performance

Export volumes have grown at an annual average rate of 0.6 per cent since 2000-01, well below the 20-year average growth rate of 5.9 per cent. There have been a number of contributing factors to the slowdown in exports, which have tended to play out sequentially over the last five years.

Exports were first affected by a slowdown in world economic activity around the turn of the decade.

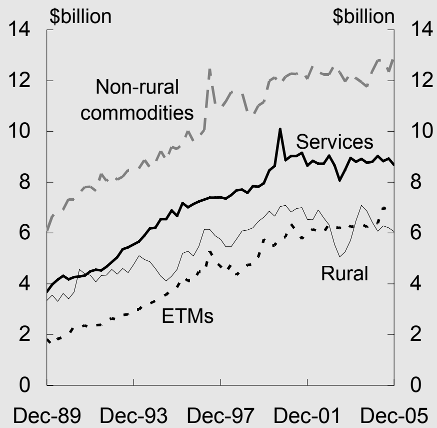
The terrorist attacks on the World Trade Centre and SARS added to the effects of the global downturn and depressed the global travel industry. This had particularly adverse effects on exports of services.

The drought of 2002-03, one of the worst on record, reduced rural exports significantly in the years that followed. The effects of the drought have gradually eased and favourable seasonal conditions since mid-2005 should support a recovery in rural exports.

The Australian dollar appreciated by more than 20 per cent over the course of 2003, and has remained at a relatively high level. This has constrained exports, particularly of services and elaborately transformed manufactures (ETMs), which are yet to recover.

Furthermore, ETM exports have been adversely affected by the global shift of manufacturing to emerging lower cost economies, particularly China. Looking ahead, this trend is likely to continue to affect ETM export growth.

Chart A: Major exports[(a)]



(a) Reference year for chain volume measures is 2003-04.
Source: ABS cat. no. 5302.0.

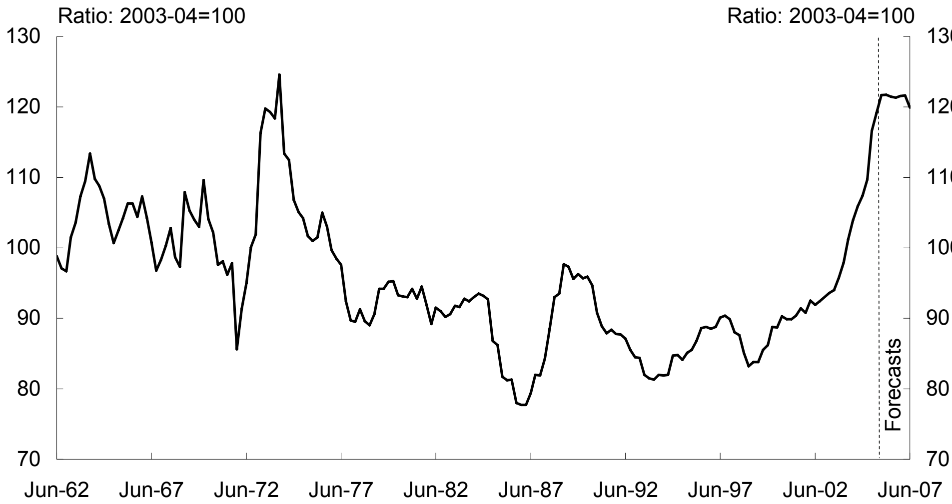
Weak commodity prices in the late 1990s were associated with reduced exploration and investment by the mining industry (see Box 2 from Budget Paper No. 1, *Budget Strategy and Outlook 2005-06,* Statement 3). This limited the extent to which the industry could respond to the recent growth in demand for commodities, given the long lead times to develop new mine capacity. Accordingly, the prices of many resource commodities rose, and Australia's resource export receipts increased. As new mining capacity comes on line over the next few years, non-rural commodity export volumes are expected to increase significantly.

The terms of trade

Australia's terms of trade are at a three decade high and this is boosting national income and generating significant benefits for the economy. Strong mining profits have supported the corporate sector and boosted investment activity. This has also increased Government revenue collections and generated additional income for the household sector through higher returns on mining and mining-related equity investments (Box 4).

Strong world economic growth, particularly in China, has fuelled the demand for commodities and pushed the price of some bulk commodities to record highs. The exceptional growth in the terms of trade over the past year has continued into 2005-06, but the terms of trade are forecast to remain flat in 2006-07 (Chart 8).

Chart 8: Terms of trade



Source: ABS cat. no. 5302.0 and Treasury.

As global supply is increased, commodity prices are expected to moderate somewhat as the substantial margins earned on these resources begin to be eroded. The price fall is expected to be less pronounced than in previous commodity cycles as ongoing demand, particularly from the rapidly expanding Chinese economy, may cause commodity prices to remain higher for longer than past cycles. It remains unclear how the timing of changes in global demand and supply will affect commodity prices (see also Statement 4).

Slow growth in import prices has also contributed to the rise in the terms of trade. The price of information and communication technology goods, in particular, has been falling for more than a decade. Tariff reductions on motor vehicles and textiles, clothing and footwear in 2005 should continue to exert downward pressure on import prices.

These terms of trade forecasts are based on the latest published ABARE commodity forecasts. This has been the long-standing approach used to generate forecasts for the terms of trade for the Budget. However, on this occasion, prices for a range of commodities have risen significantly in recent weeks. If these most-recent rises in commodity prices were sustained, they would imply somewhat higher terms of trade in 2006-07.

Box 4: Commodity prices and Australian incomes

The contract prices of some key Australian commodity exports, such as coal and iron ore, jumped sharply in early 2005. As a result, Australia's terms of trade have risen to their highest level since 1974. This has important effects on the Australian economy which are not directly captured in the most commonly cited measure of real economic activity, *real gross domestic product* (GDP).

Under most circumstances real GDP differs only slightly from measures of domestic income. However, when the terms of trade are rising strongly domestic income is boosted significantly relative to domestic production or real GDP.

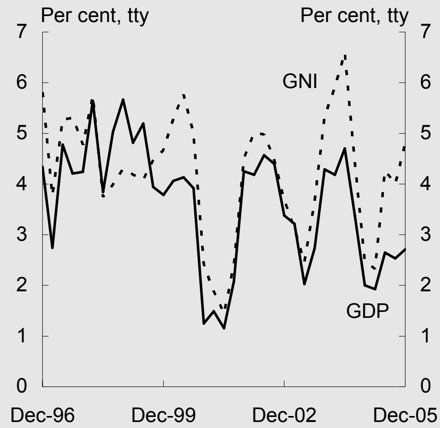
The Australian Bureau of Statistics compiles measures not only of real GDP but also of domestic and national income.

Real gross domestic income (GDI) adjusts real GDP for movements in the terms of trade. It shows how the recent rise in commodity prices increases the real income of Australia. This effect is expected to add around 2 percentage points to growth in domestic income in 2004-05 and 2005-06.

Real gross national income (GNI) adds primary income earned by Australians from working or investing overseas to GDI; and subtracts the primary income generated in Australia that accrues to foreigners. The difference between these represents the majority of the net income deficit in the balance of payments (deflated by the GDP deflator).

In 2004-05, a widening net income deficit has seen GNI grow around 1 percentage point slower than GDI but still more quickly than GDP.

Chart A: Real GDP and GNI

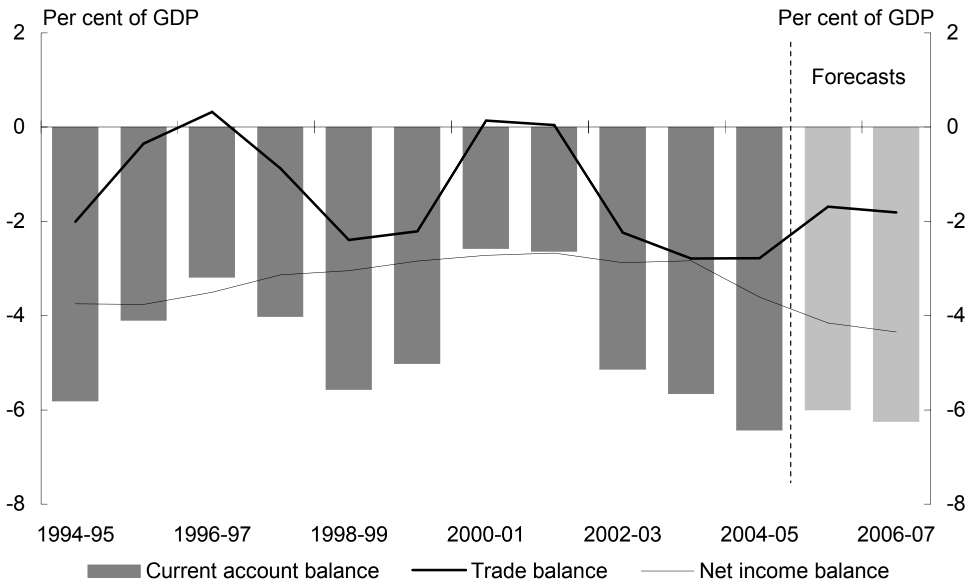


Source: ABS cat. no. 5206.0.

The current account

The current account deficit (CAD) is expected to be around 6 per cent of GDP in 2005-06, and 6¼ per cent of GDP in 2006-07. The trade deficit is expected to narrow to 1¾ per cent of GDP in 2005-06 and 2006-07. However, high commodity prices and increased interest payments to the rest of the world are expected to contribute to a widening of the net income deficit (Chart 9).

Chart 9: Current account balance



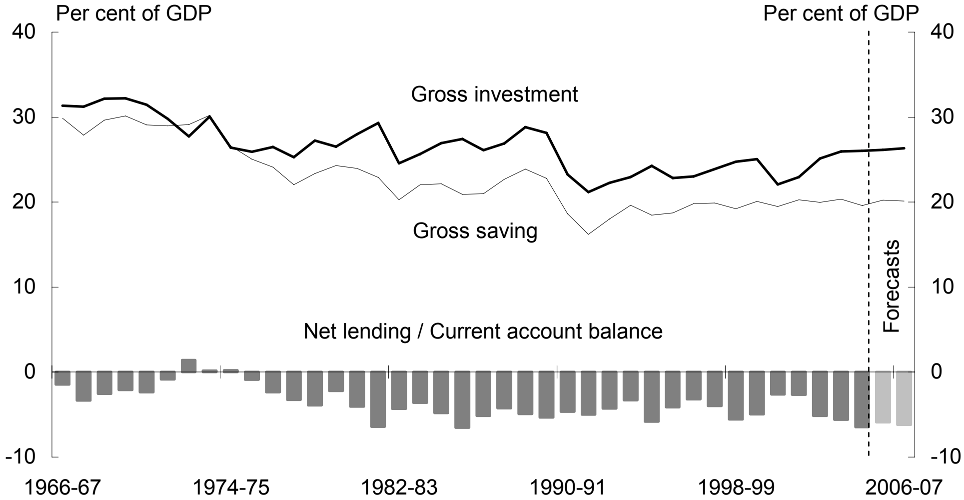
Source: ABS cat. no. 5302.0, 5206.0 and Treasury.

Equity income accruals to the rest of the world are expected to increase as a consequence of strong mining profits and the high degree of foreign ownership of the mining sector in Australia. In addition, net interest payments to the rest of the world are expected to increase with the stock of net foreign debt and as world interest rates increase.

From a saving and investment perspective, the deterioration in the current account reflects strong growth in investment. Since 2000-01, nominal investment has been increasing as a share of GDP, initially driven by strong dwelling investment but more recently by strong business investment. On the other hand, national saving has remained broadly stable as a share of GDP, in part because of support from the strong fiscal position of the government sector (see Statement 1). This conjunction of saving and investment outcomes has been an important reason why markets have been unconcerned at the deterioration in the CAD. Statement 4 includes an analysis of the international context and forces acting on the Australian economy that influence the CAD.

Over the forecast period, there should be a slight increase in business investment as a share of GDP while national saving is expected to be broadly stable (Chart 10).

Chart 10: Net lending and the current account[(a)]



(a) The net lending position is equivalent to the current account balance *plus* net capital transfers *less* net purchases of non-financial non-produced assets and statistical discrepancies.
Source: ABS cat. no. 5302.0, 5206.0 and Treasury.

Labour market, wages and prices

Labour market

The labour market remained strong in the first half of 2005, with employment growing quickly and the unemployment rate close to 5 per cent. Employment growth was particularly strong in Queensland and Western Australia. In the latter half of 2005, employment growth slowed.

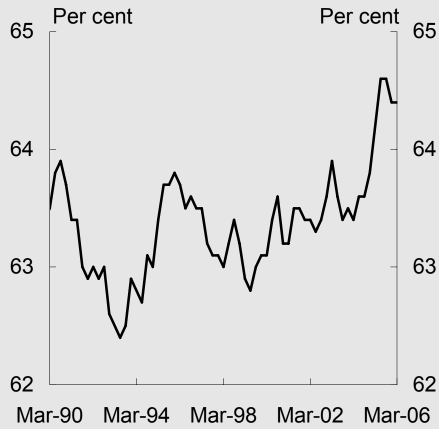
Employment is expected to grow by 1 percentage point in 2006-07, in line with the lagged effects of weaker GDP growth. However, the year-average figure masks a modest recovery from 2005-06, with employment expected to grow by 1¼ per cent through the year to the June quarter 2007. Forward-looking indicators such as job vacancies suggest some near-term strength in employment growth, although vacancies remain lower than a year ago.

The labour force participation rate reached a record level of 64.8 per cent in August 2005, supported by increased workforce participation across all age groups (Box 5). In the period ahead, the participation rate is expected to fall gradually and settle at around 64¼ per cent, as the weakness in employment growth encourages fewer people to enter the labour force. The unemployment rate is expected to be around 5¼ per cent in 2006-07.

Box 5: Labour force participation

After averaging around 63¼ per cent over the last decade, the participation rate has risen to a historically high level (Chart A). This increase has been associated with strong employment growth and rising wages, which in turn has drawn more people into the labour force.

Chart A: Participation rate



Source: ABS cat. no. 6202.0.

The increase in participation has occurred across most age groups, but was disproportionately large in groups with relatively low attachment to the labour force: older workers nearing retirement, and younger workers entering the workforce. These groups account for 45 per cent of the working age population, and yet they accounted for around 70 per cent of the rise in participation.

These recent changes have occurred against a backdrop of significant structural shifts in the labour force, which have manifested themselves in two key developments.

The first of these is the increase in female participation. A large portion of this increase occurred during the 1980s and was primarily driven by females aged 25 to 54 years. The ageing of this cohort has been gradually increasing the participation rates of older female age groups.

The second is the turnaround in male participation rates. After falling over the 1990s, the participation rates of older males began increasing earlier this decade — a pattern that occurred across most of the OECD. Much of the increase has been in full-time participation, and may be related to the ageing of the cohort of older men most affected by poor labour market conditions in the early 1990s and structural changes to the economy throughout the 1980s and 1990s.

The degree to which the most recent increase in participation persists will depend in part on economic conditions. In the latter half of 2005, a decline in the participation rate was accompanied by a fall in employment and below trend GDP growth. If the economy was to deteriorate significantly, it is likely that participation rates would fall further. Over the longer term, demographic factors will largely determine the size and growth of the labour force.

Wages

Wage growth is forecast to remain solid in the near term, as the effects of tight conditions in the labour market in 2004-05 flow through to wages. However, with employment growth forecast to moderate, the recent momentum in wage growth should ease in 2006-07.

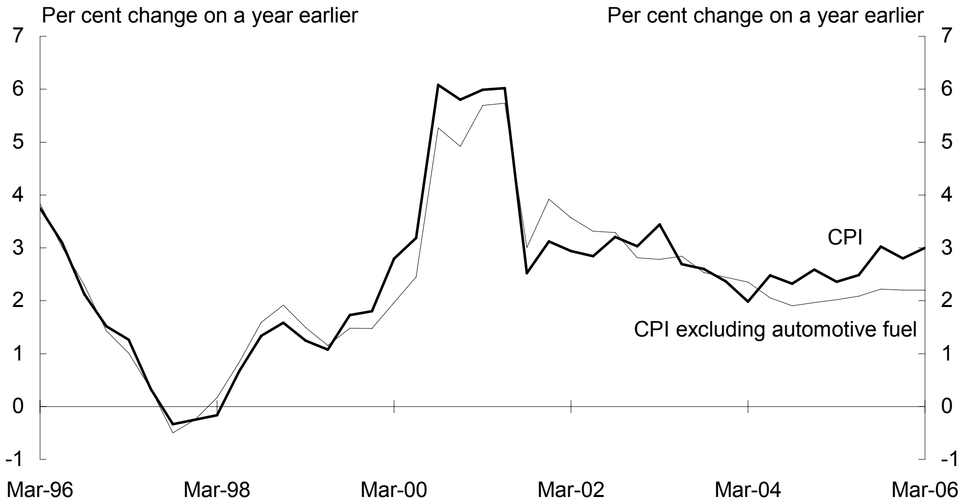
The Wage Price Index is forecast to increase by 4 per cent in 2006-07, similar to the growth expected for 2005-06. Businesses continue to report skill shortages, but to date this has not led to significant generalised wage pressures. Strong labour demand in the mining and mining-related sectors may see wages grow temporarily faster in those areas, but they are unlikely to have a noticeable impact on aggregate wage outcomes given the relatively low share of the mining sector in total employment.

There is a risk that strong wage growth in the mining, construction, health and education sectors over the past year may continue and lead to more widespread wage pressures.

Prices

Inflation has remained moderate for a number of years, despite rising oil prices and, in recent times, higher unit labour costs (Chart 11). This positive inflation outcome is due in no small part to low tradable inflation and well-anchored inflationary expectations.

Chart 11: Inflation



Source: ABS cat. no. 6401.0.

Looking ahead, inflation is forecast to remain moderate, despite a cyclical upturn in unit labour costs and further increases in fuel prices. The Consumer Price Index is expected to increase by 2¾ per cent in 2006-07, lower than the increase for 2005-06. Abstracting from the direct effects of fuel prices, inflation is forecast to be around 2½ per cent in the year to June 2006.

The pressure on inflation from unit labour costs is expected to dissipate with a cyclical upswing in productivity, which now appears to be underway. In contrast, with oil prices trading at record levels, fuel prices are expected to be a significant contributor to inflation in the near term. Fuel prices are forecast to contribute around ¾ of a percentage point to inflation in the year to June quarter 2006. In 2006-07, with oil prices assumed to remain steady, fuel prices are expected to have less effect on inflation.

Oil related increases in the price of some goods and services have already occurred (such as for airfares) but, to date, the indirect effects of higher oil prices on inflation have been mild. Nonetheless, with oil prices currently trading at record nominal levels, there is a risk of more widespread pass through of these costs to consumers. This has increased the likelihood of more significant second-round inflationary effects. The key risk to the outlook for inflation is the extent to which retailers can continue to absorb higher input costs into their profit margins. So far, the increased cost of labour, oil and raw materials has not resulted in any marked increase in retail consumer prices.

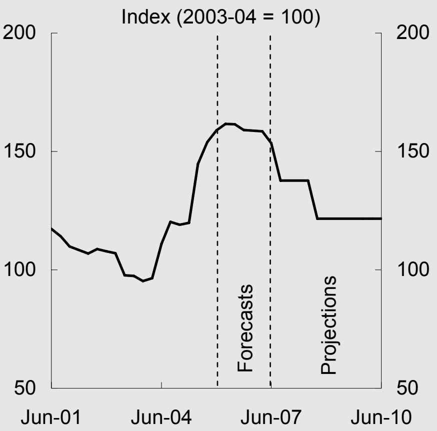
Tradables inflation is forecast to remain low, with the downward trend in the price of some tradable items, such as motor vehicles and computing equipment, expected to continue. Non-tradables inflation is expected to continue to decelerate, reflecting robust retail competition and the recent softening in consumer spending. After a prolonged period of strong growth, house purchase prices (project homes) are forecast to slow, in line with the expected moderation in unit labour costs and modest falls in new dwelling investment. House purchase is the largest component of the CPI, representing around 8 per cent of the basket.

Box 6: Nominal GDP projections

As foreshadowed in the 2005-06 Budget, growth in nominal GDP has been boosted by significant commodity price increases, particularly for iron ore.

Nominal GDP grew by 6.5 per cent in 2004-05, and is expected to increase by a further 7 per cent in 2005-06. However, these high commodity prices are eliciting a global supply response which is expected to see Australia's commodity export prices remain around current levels in 2006-07, resulting in a moderation in nominal GDP growth to 5½ per cent.

Chart A: Commodity prices



Source: ABS cat. no. 5302.0 and Treasury.

The global supply response is likely to continue well beyond the forecast horizon, creating the potential for commodity price falls. To account for this eventuality, it has been assumed that the prices of key commodities will return to a longer run level over the first two years of the projection period, 2007-08 and 2008-09 (Chart A).

As a result, the projections for nominal GDP growth in 2007-08 and 2008-09 are lower than average growth rates for nominal GDP. In 2009-10, nominal GDP growth is assumed to return to its average growth rate. Projected real GDP growth is unaffected by the technical assumption for commodity prices.

This methodology is consistent with the approach taken in the 2005-06 Budget.

There are considerable risks associated with the technical assumption for commodity prices, particularly given the uncertainty around the future demand for resources and the associated supply response.

STATEMENT 4: AUSTRALIA IN THE WORLD ECONOMY

This statement discusses a range of fundamental changes in prospect for the world economy, and their implications for Australia. It then discusses the strategies Australia is adopting in its economic engagement with the world to address and respond to these changes.

STATEMENT 4: AUSTRALIA IN THE WORLD ECONOMY

This statement examines Australia's place in the world economy. It begins by discussing some of the fundamental influences that are gradually changing the contours of the world economy. It focuses particularly on the far-reaching implications of the rising economic importance of China and India, before turning to the continuing process of globalisation, population ageing in both developed and developing economies, and possible exposure to adverse external shocks — in particular, terrorism, pandemics and threats to energy security. The statement therefore builds on Statement 4 in recent budgets, which have also examined fundamental global changes; in particular, the productivity-enhancing role of information and computer technology (2001-02) and the implications for Australia of population ageing (2003-04 and 2005-06).

The statement then turns to the strategies Australia is adopting in its economic engagement with the world to address and respond to these developments. The growing economic weight and influence of China and India, continuing globalisation, the evolving patterns of East Asian regionalism, as well as long-term security, resource and environmental concerns are placing new demands on international institutions and patterns of engagement — at the multilateral, regional, and bilateral levels. The statement discusses these issues with a focus on the strategic goals underpinning Australia's international economic engagement, the role of current activities in helping to achieve these goals, and the important challenges for the future.

CHANGES IN PROSPECT IN THE WORLD ECONOMY

China and India

Continuing strong growth in China and India is arguably the international economic development with the most far-reaching consequences for the global economy. China is already the world's second largest economy, and India the fourth largest. On plausible assumptions, it is possible that the size of China's economy could surpass that of the United States within fifteen years.[1] This shift in relative economic importance towards China, and potentially India, from the developed economies — Europe, Japan and to a lesser extent the United States — is already occurring and represents a major tectonic shift. As the metaphor suggests, the changing relative size of the key economies may sometimes see seismic disturbances with powerful economic implications. Managing these potential disturbances will be critical to maintaining an environment conducive to continued strong global growth.

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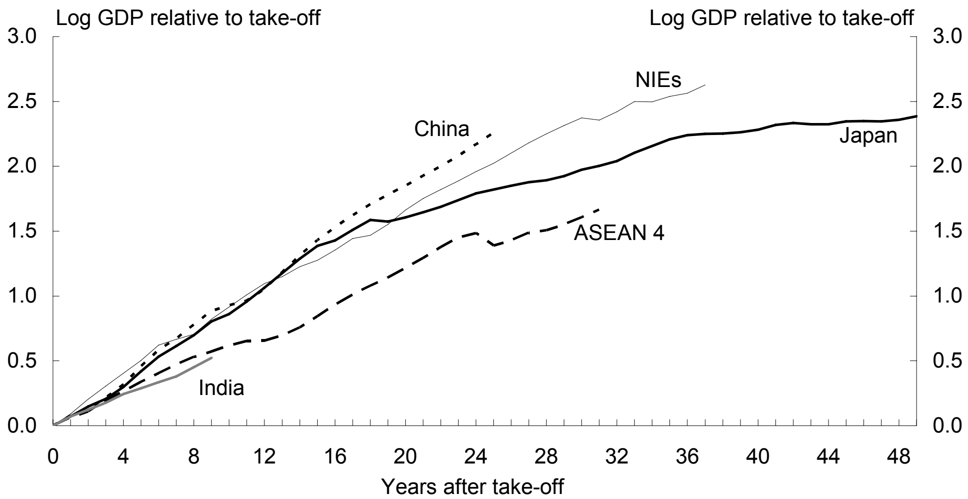
1 These estimates are on a purchasing power parity (PPP) basis. This is the preferred basis for comparing the relative size of economies because it uses a conceptually appropriate approach to estimating prices in both the traded and non-traded sectors of the economies, in contrast to comparisons based on market exchange rates.

Other large developing countries such as Brazil, Indonesia and Russia may also increase in economic importance in coming decades. We focus in this section on China and India because they are by far the most populous developing economies. As such, their continued rapid growth is of greatest importance for the global economy.

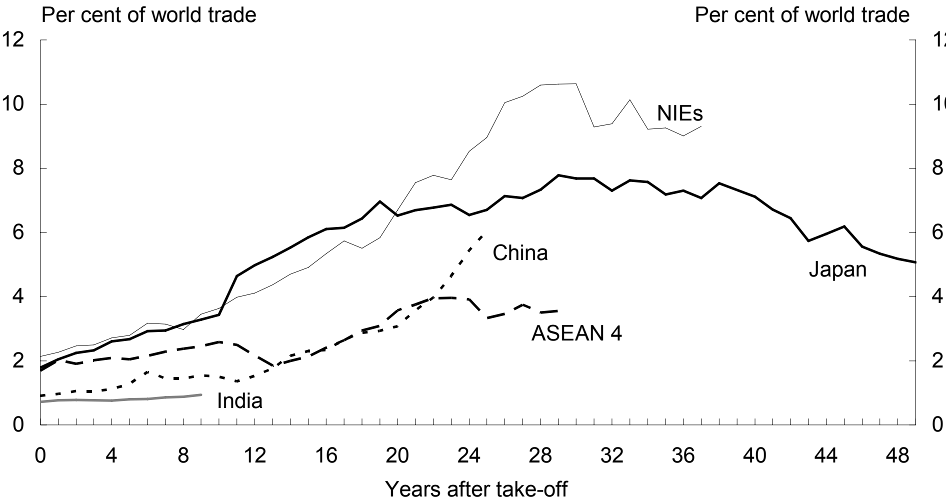
The recent growth rates of China and India have been very high relative to the standards of the developed economies but not dramatically different from those recorded in earlier decades by Japan, the East Asian newly industrialised economies (NIEs) (Hong Kong, Korea, Singapore and Taiwan), and ASEAN 4 (Indonesia, Malaysia, Philippines and Thailand) (Chart 1). China's share of global trade has thus far been less than Japan's (at comparable stages after take-off), but China's share is rising extremely rapidly and could soon surpass Japan's peak share of world merchandise trade during its rapid development (Chart 2). India's share of global trade remains small, but should grow strongly provided India continues to reform and open up its economy.

Chart 1: Growth after take-off



Source: IMF World Economic Outlook database, September 2005. Data shown are: Japan, 1955-2004, China, 1979-2004, NIEs, 1967-2004, ASEAN 4, 1973-2004, India, 1995-2004. Take-off is the first year when the country (or group) experienced at least 10 per cent annualised growth in the value of exports over the previous three years.

Chart 2: Share of world merchandise trade after take-off



Source: IMF World Economic Outlook database, September 2005. Data shown are for the same years as Chart 1.

The process of 'catch-up' in China and India is similar to that followed by Japan and the East Asian NIEs in past decades: moving towards the technologies, institutions and standards of living of the developed economies. The catch-up phase in China and India, however, may continue for longer because the gap between their productivity levels and those of the advanced economies is larger than was the case for their East Asian predecessors. This larger productivity gap arises primarily because the global productivity frontier has now moved further out than its position at the time of the rapid development of the other East Asian countries.

This line of argument suggests that China and India may continue to grow at around their recent average rates for quite some time to come, although they will undoubtedly experience inevitable bumps along the path to modernisation. Of course, bumps along the path to modernisation often require adroit policy responses — to ensure that they remain 'bumps' and do not evolve into something more serious and long-term. By similar logic, sustaining strong growth in these countries will depend on their continuing with internal reforms that will likely grow more demanding. For example, China will need to press on with improvements to fiscal sustainability, financial-sector reform, and reforms to its many remaining state-owned enterprises, and will also need to adjust to the inevitable appreciation of its real exchange rate. Much will depend on maintaining political and social stability through these processes of transition.

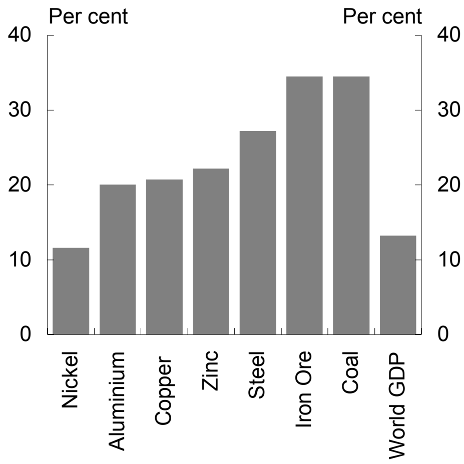
As discussed in more detail later in the statement, different demographic trends in the two countries will play an increasingly important role in their relative growth over time. China's working-age population is projected to begin to fall around a decade from now. By contrast, India is one of the few large economies projected to have a growing working-age population over the next 40 years and is projected to overtake

China as the world's most populous nation in the 2030s (United States Census Bureau 2005).

China's economy is large enough that its share of global demand for a range of commodities is already sizeable (Chart 3). Part of the reason for this, of course, is the sheer size of China's population — currently around 150 million more than all of the OECD countries combined (based on United Nations population projections for 2005).

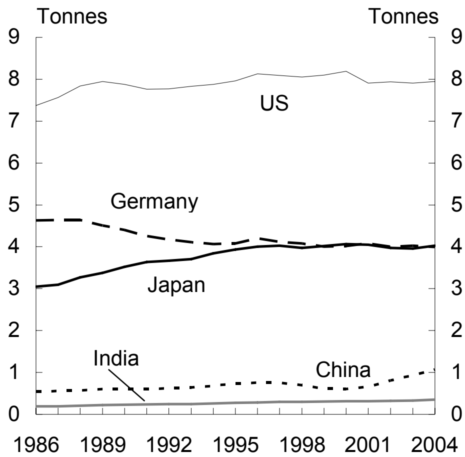
The effect of China and, to a lesser extent, India on world demand for imported forms of energy, especially crude oil, reflects the relatively high energy intensity of their economies (units of energy input per unit of output produced). China's consumption of energy per capita, however, is currently much lower than that of the advanced industrial countries (Chart 4), and the same is true of its consumption of metals. But as this per capita consumption rises, China may account for the majority of the world's growth in import demand for resource-intensive products for an extended period.

Chart 3: China's share of global consumption of materials



Source: Baffinland Iron Mines Corporation (2005), BP Global (2005), IMF (2005a), Morgan Stanley (2005), Richmond (2005). China's share of world GDP is at purchasing power parity exchange rates.

Chart 4: Energy use per capita



Source: World Development Indicators, BP Global (2005). Units are tonnes of oil equivalent per capita per annum.

The Chinese Government projects a doubling in energy use between 2000 and 2020. This projection may be conservative, however, given China's aim to quadruple its GDP per capita over this period (a goal economic historian and Nobel Laureate Robert Fogel regards as attainable; see Fogel 2006) and the recent experience that energy use has been growing faster than GDP (Sinton et al 2005). Even if China maximises the use of its domestic coal reserves and achieves sizeable improvements in energy efficiency, it is likely to have a rapidly growing demand for imported energy, especially oil for transport. In India as well, dependence on imported oil and other energy sources is likely to continue to rise.

Rising energy consumption in these countries will therefore have major implications for the balance of world energy supply and demand as well as for global efforts to restrain greenhouse gas emissions and hence climate change. International mechanisms aimed at containing global greenhouse gas emissions will clearly not be effective if they exclude these countries. This emphasises the need for mechanisms to promote the transfer of cleaner and more efficient energy technologies to developing economies, and for international agreements that aim to contain greenhouse gas emissions to include these countries as well as developed countries. Developing and deploying low-emissions technologies is a key focus of the recently established Asia Pacific Partnership on Clean Development and Climate, a collaboration between Australia, China, India, Japan, Korea and the United States, which together account for half of the world's energy use and greenhouse gas emissions.

Comparative advantage

Although China's future development is likely to involve progressively more capital-intensive production, its international trade will for a long time reflect its relative abundance of labour. That means China will continue to export mostly labour-intensive manufactures, and to import mostly raw materials, foodstuffs and capital-intensive manufactures.

A considerable literature modelling the implications for other economies of the likely further growth of China generally suggests that countries which specialise in labour-intensive manufacturing and assembly are most likely to be adversely affected by China's rise. By contrast, countries specialising in the production and export of components, capital goods and raw materials are more likely to be favourably affected.

The global effects of India's growth have so far been much less than those of China's, because India remains a relatively closed economy with only a small share of global trade in goods and services (Chart 2). If India continues to embrace globalisation and reform — which will support a continuation of its recent high growth rates — its trade will likely contribute increasingly to global growth.

One aspect of India's development that has attracted considerable attention is the outsourcing to India of services such as call centres and business data processing that were previously undertaken in developed countries. According to a McKinsey Global Survey, around 1.5 million services jobs were outsourced from developed countries (a number that includes all destination countries, not just India) in 2003 (The Economist 2005). Outsourcing is expected to grow rapidly (almost tripling by 2008 according to the McKinsey Survey), driven by advances in technology. Even the largest projections of jobs lost to outsourcing out to 2015, however, remain small relative to overall job turnover in the developed countries (OECD 2005).

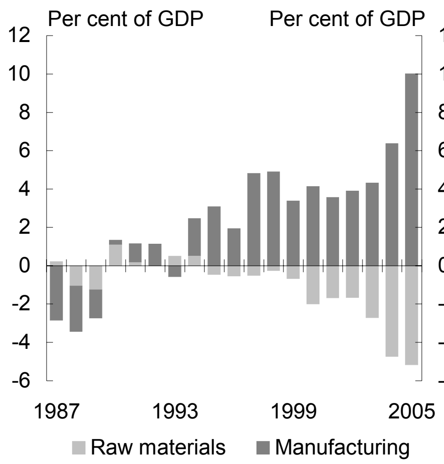
As is the case with opening up the economy to international trade, outsourcing enhances economic efficiency and generates net economic benefits for both source and destination countries. However, it imposes adjustment costs on those sectors of the economy, predominantly service sectors, that were previously insulated from overseas competition. Similar adjustments have been made by trade-exposed sectors of the economy over recent decades, in the process of reducing tariff and other barriers to trade, with widely accepted benefits for the economy.

Implications for Australia

The rise of China and other large developing countries presents opportunities for Australia to exploit its comparative advantage in natural resources and 'high-end' goods and services, although some more labour-intensive sectors are likely to face increasing competition.

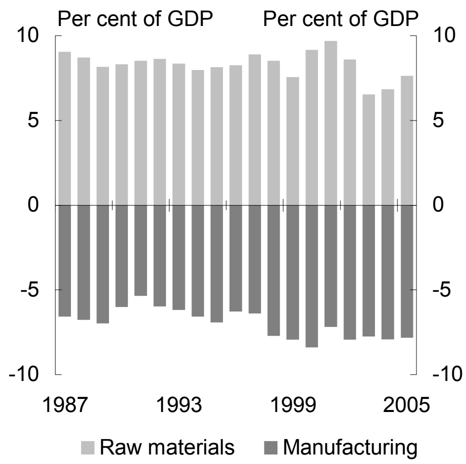
The complementarity of China's net exports and those of Australia is shown in Charts 5 and 6. China is a large net exporter of manufacturing goods, but a large net importer of raw materials, while Australia's net trade position in these two categories of goods is precisely the opposite.

Chart 5: China's net exports



Source: CEIC Asia Database.

Chart 6: Australia's net exports



Source: ABS cat. no. 5302.0.

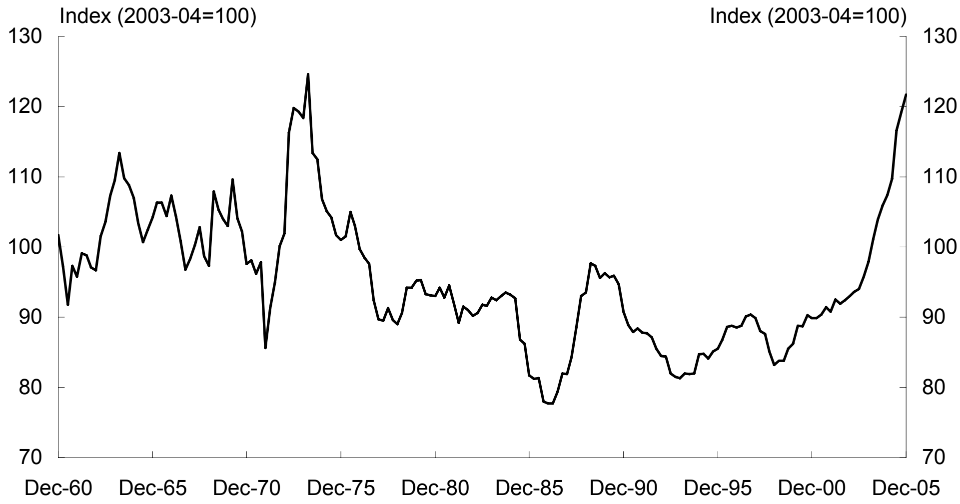
The additional demand for resources by China and other economies has manifest itself in a huge rise in Australia's terms of trade (the ratio of the prices we receive for our exports to the prices we pay for our imports) over recent years (Chart 7).

This huge change in relative prices has been absorbed by the Australian economy with minimal disruption, notwithstanding the heightened competitive pressures faced by many firms in both export and import-competing industries. In contrast, the previous similarly sized terms of trade boom in the early 1970s proved extremely disruptive, resulting in an inflationary boom that cast a long shadow over the economy (Gruen 2006).

In large part, the improved economic resilience in the face of the current terms of trade shock has been a consequence of improved institutional arrangements and the increased flexibility of the domestic economy. Of particular importance in this regard have been the floating of the exchange rate and the introduction of independent monetary policy. And the other crucial development — without which the first two would have been less effective — has been the increasing policy focus on the supply side of the economy — a focus on microeconomic reform. Industrial relations reforms and competition policy, in particular, have contributed significantly to macroeconomic stability both by allowing the exchange rate to act as an absorber of external shocks without generating inflationary impulses across the whole economy, and by reducing the need to resort to activist fiscal and monetary policy in an attempt to keep the economy on an even keel.

Having absorbed the huge rise in the terms of trade with minimal disruption to the aggregate economy, there are grounds for optimism that future volatility in the terms of trade can be similarly absorbed. The improved institutional arrangements and enhanced flexibility have reduced the vulnerability of the economy to the disruptive effects of sharp rises in the terms of trade. They should also do so were Australia to experience a sharp fall in the terms of trade at some time in the future.

Chart 7: Australia's terms of trade



Source: ABS cat. no. 5302.0.

Looking to the future, there are powerful economic influences tending to keep resource and energy prices high, and other powerful influences tending to reduce them. The most important influence tending to keep them high is the likelihood that a continuation of strong catch-up growth in the large developing economies will generate further increases in their energy and mineral needs over an extended period of time. This in turn would imply global resource requirements well in excess of existing capacity and continuing above-average rates of exploration and investment in the resource sector to meet these rising requirements.

The most important influences acting in the opposite direction, tending to reduce resource and energy prices, are the global demand and supply responses to the currently high prices. Over an extended period of time, these demand and supply responses can have a powerful moderating influence on prices, as was seen for example in the aftermath of the OPEC oil shocks of the 1970s. Furthermore, global responses to rising greenhouse gas emissions are also likely to reduce the rate of growth of energy demand below previous trend rates and put downward pressure on the prices received by resource suppliers over time.

Unfortunately, economists do not have an enviable track record predicting how powerful, but countervailing, economic influences will be resolved nor, in particular, the timing of their resolution. Given these unavoidable limitations with economists' crystal balls, it is worth discussing the main possibilities and their implications, at least in broad outline.

One possibility, which presumes no serious prolonged adverse developments that derail the catch-up process for the large developing countries, is that average prices for resources may remain relatively high — well above the average cost of production — for an extended period of time, especially given the size of the remaining productivity gap between the large developing economies and the advanced economies (Garnaut 2006). In that case, while there would undoubtedly be volatility in prices at times, Australia's terms of trade would continue at a relatively high average level for an extended period.

Were this outcome to eventuate, it would be outside the historical experience of the past several decades, as Chart 7 shows. It is therefore of interest to examine in some detail the implications for the Australian economy were the terms of trade to remain relatively high for an extended period.

To begin with, this would clearly have a strongly favourable effect on average Australian living standards. A long period of high resource prices would also generate a prolonged expansion of the resources sector, accompanied by a shift of capital and labour from other sectors of the Australian economy in response to higher average profits and employment opportunities in the resource sector. Capital and labour would likely be drawn out of some parts of manufacturing, and also parts of agriculture and services that are becoming increasingly tradeable.

Higher average returns in the capital-intensive resource sector for an extended period would raise the profit share of national income, and provide continuing stimulus for high levels of business investment in that sector. The implications for the current account deficit would depend on the response of national saving to the higher national income associated with the high level of resource prices (since the current account deficit is the excess of national investment over national saving). It is possible that the rise in investment would exceed the rise in saving, in which case the current account deficit would become larger, possibly for an extended period.

Such a development, should it occur, should not be cause for concern nor a sign that Australia was no longer able to compete in the global marketplace. It would instead be part of the process of Australia successfully reaping the broader economic benefits offered by the emergence of China, India and other large developing countries.

If these outcomes eventuate, the challenge will be to craft public policy with an eye to both distributional concerns and enabling the necessary adjustments to take place. There is a compelling case for helping to enhance individuals' capacity to adjust to economic changes that have adversely affected them, and hence an important role for education and training policies geared to this outcome. However, it would be counterproductive to provide trade protection or long-lived publicly funded economic support to sectors or firms that can no longer generate an economic return.

If we are at the early stages of a long-lived change in Australia's comparative advantage, this change is likely to generate significant reallocation of activity among major sectors of the economy; a reallocation that will be facilitated by the efficient functioning of product, labour and capital markets. On this score, Australia has achieved much in improving the functioning of its markets over recent years. For the economy to respond efficiently to a long-lived change in relative prices, however, will require a continued focus on improving the flexibility of the supply-side of the economy — that is on microeconomic reform. This will be particularly important in sectors relevant to enabling economic resources to reallocate with minimum disruption. In particular, pricing, competition and competitive neutrality issues in transport, energy and water need to be resolved to ensure both efficient infrastructure investment and service delivery.[2] Many policies designed to enhance flexibility clearly have important federal and state dimensions, and will therefore require cooperation between levels of government. The ambitious and broad-based reforms in the February 2006 Council of Australian Governments' National Reform Agenda represent an admirable example of such cooperation.

The future evolution of the terms of trade will also have implications for fiscal policy. At a time of strongly rising terms of trade, and hence strongly rising taxation revenues, there is a case for running larger-than-usual budget surpluses, because it remains unclear for how long the strongly rising taxation revenues will be sustained. This has been the strategy followed by the Australian Government, with the underlying cash surpluses over the most recent three years, 2002-03 to 2004-05, averaging 1¼ per cent of GDP, ½ per cent of GDP above the average over the previous five years.

If resource prices were to remain high on average for an extended period — which would, of course, only become apparent gradually over time — the case for continuing to run larger-than-usual budget surpluses would become progressively weaker. The budget strategy of balance over the cycle implies budget surpluses that are larger than

2 See Henry (2005) for more on reform issues in the transport, electricity and water sectors.

usual when macroeconomic conditions warrant it, but clearly cannot imply such surpluses at all times.

Having examined the implications for the Australian economy were resource prices to remain high on average for an extended period, it is worth also examining circumstances in which this outcome might not eventuate.

As argued above, continued strong catch-up growth by China, India and other large developing countries is a reasonable and plausible forecast, but it remains just that — a forecast. While the countries and country-groupings in Chart 1 have all experienced long periods of strong catch-up growth, the historical record also contains examples of countries that experienced a few short years of strong catch-up growth, after which they faltered.

The per capita output growth experiences of Korea and Brazil, for example, were strikingly similar in the first half of the 1970s. Moreover, important determinants of future per capita growth in these two countries, like saving and investment ratios to GDP and the behaviour of real wages, were also strikingly similar at that time. But while Korea continued strong catch-up growth after the early 1970s, Brazil did not (Sachs and Sundberg 1988). This example highlights the point that continued strong catch-up growth is not inevitable. Instead, it requires growth-enhancing economic policies and, at times, painful and unpopular adjustments in response to economic shocks which, for developing countries, can sometimes be hugely disruptive, both economically and socially.

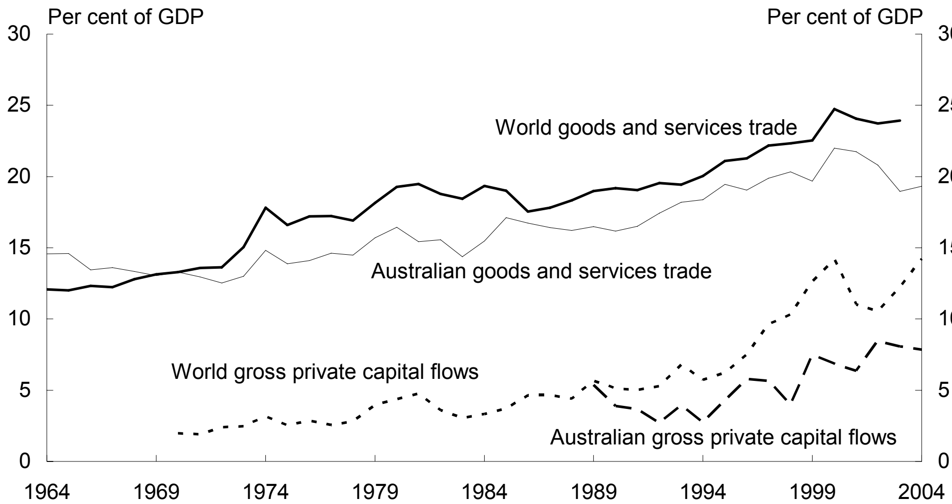
Developments across the rest of the globe are also relevant to whether resource prices remain high for an extended period, and whether China and India continue to grow rapidly for many years to come. As already mentioned, global demand and supply responses to the currently high resource prices may have a powerful moderating influence on prices, although with uncertain timing.

Furthermore, as also discussed above, continued strong catch-up growth in China and India will likely generate significant pressure for reallocation of activity among major sectors of the Australian economy. The size of the Chinese and Indian economies, especially if they continue to grow rapidly for an extended period, means that significant pressure for reallocation of activity among major sectors will be felt in many countries, not just Australia. Even if Australia responds flexibly to these challenges, there are no guarantees that others will do likewise — especially others whose economic welfare is seriously challenged by the rise of China and India. Inappropriate economic responses in other parts of the globe including, in particular, the rise of protectionism in any of its many guises, could do much to derail the process of long-term catch-up growth in China and India, with obvious deleterious implications for Australia and the world economy.

Continuing globalisation

The rise in the economic importance of China and India has been part, albeit an important part, of a process of continuing globalisation. A related manifestation of this process has been strong growth in international flows of goods and services and of capital, which have increased more rapidly than output over the past several decades (Chart 8). This has resulted partly from reductions in policy barriers to cross-border trade and capital flows, and partly from improvements in information and communications technology (ICT) and transport. This increase in economic integration has raised living standards by allowing countries to focus on producing and exporting those goods and services they can produce relatively more efficiently in exchange for those goods and services that others can produce relatively more efficiently. Financial integration allows savings to be invested where returns are expected to be highest and also enables risks to be better diversified.

Chart 8: World and Australian trade and capital flows



Source: ABS cat. nos. 5206.0 and 5302.0 and World Development Indicators. Trade is the average of exports and imports. Gross capital flows are the average of net foreign purchases of domestic assets and net domestic purchases of foreign assets.

While the increase in global integration to date has been substantial, there is scope for it to go further. This applies particularly to services, which account for two-thirds of world output but less than one-fifth of world trade. While the services share of world output has risen significantly, its share of world trade is no higher than it was in the 1960s. These trends suggest that neither improvements in ICT nor the recent growth of offshore outsourcing of some business services have thus far had a big aggregate effect on services trade.

There are now few remaining barriers to capital flows between developed countries (although foreign direct investment into developed countries is still sometimes restricted). Perhaps surprisingly, the allocation of international capital remains much less globalised than might have been expected. Notwithstanding a doubling since 1990, the share of foreign assets in portfolios across a group of developed economies remains only one-fifth of the share that would be expected in a world in which national borders represented no impediment to the movement of international capital (IMF 2005b). Developing economies are even less integrated into global capital markets, in part because of a lack of capital market development in those economies. Countries defined by the World Bank as low and middle income (having incomes per person less than about US$10,000 at market exchange rates) account for less than 10 per cent of gross private *cross-border* capital flows in recent years. Yet these countries account for 45 per cent of world GDP in terms of purchasing power parity and 20 per cent in terms of market exchange rates.

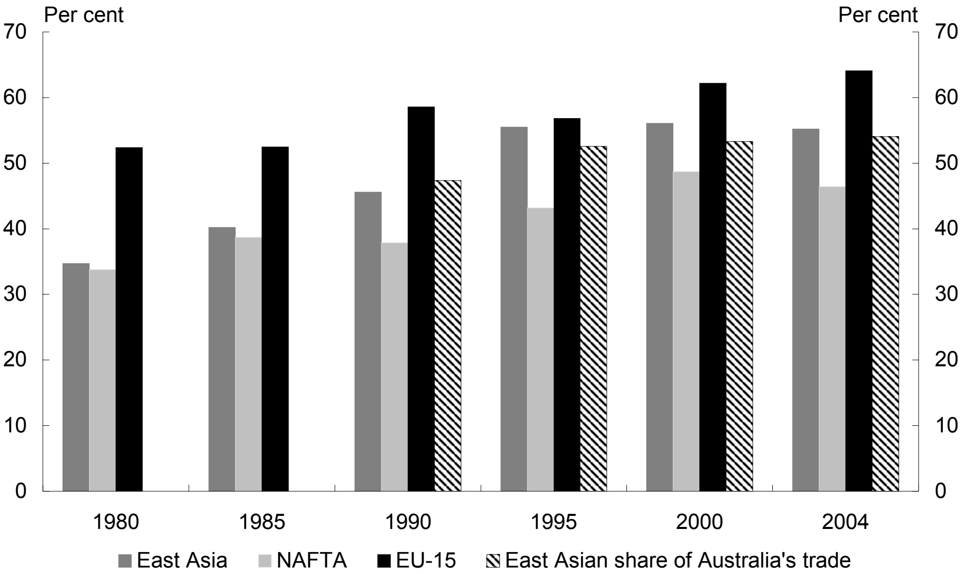
Cross-border capital flows are relatively small as shares of GDP because of both remaining policy barriers and 'home bias' on the part of investors. Home bias arises because investors usually know much more about the economic risks they face in their home countries than in other countries in which they may consider investing. But it also arises because of exchange-rate risk and differences in legal and regulatory systems. Many developing countries have explicit border barriers on some or all kinds of capital flows. Their integration into global capital markets is often further constrained by investors' perceptions of weak governance, low transparency and lack of policy and institutional credibility.

These observations suggest that while there is scope for much more international economic integration, the extent and pace of this integration are hard to predict. Further globalisation depends both on how far national governments liberalise policy barriers, and on whether pro-integration policies are supported by domestic policies and international arrangements to address 'behind-the-border' impediments and establish an environment in which cross-border transactions can flourish.

Regionalism

Trade for the three major economic regions of the world, Europe, North America and East Asia, has become increasingly intra-regional over time. Thus, for example, East Asia's intra-regional trade (trade between countries within the region) has risen from around 35 per cent of these countries' total trade in 1980 to 55 per cent in 2004, as Chart 9 shows. Trade *within* these regions, taken together, now accounts for over half of world trade. Australia has also been part of this trend, with a rising share of Australia's trade being undertaken with East Asia.

Chart 9: Intra-regional shares of total trade (exports and imports)



Source: ABS cat. no. 5368.0, Kawai (2005) and IMF Direction of Trade Statistics. East Asia comprises China, Japan, Korea, Hong Kong, Taiwan and the 10 ASEAN members.

Intra-regional integration has been accelerated by preferential liberalisation favouring intra-regional trade, both within the European Union (EU) and with the formation of the North American Free Trade Agreement (NAFTA). Integration within East Asia, including Australia, has been driven mainly by non-preferential liberalisation and economic complementarity. Even so, the intra-regional share of East Asia's trade is not far below that of the EU-15, as Chart 9 shows. East Asia's intra-regional integration has complemented its broader integration with the rest of the world, since much of the process has been driven by the development of intra-regional supply chains for the manufacture of goods for final sale in markets outside the region.

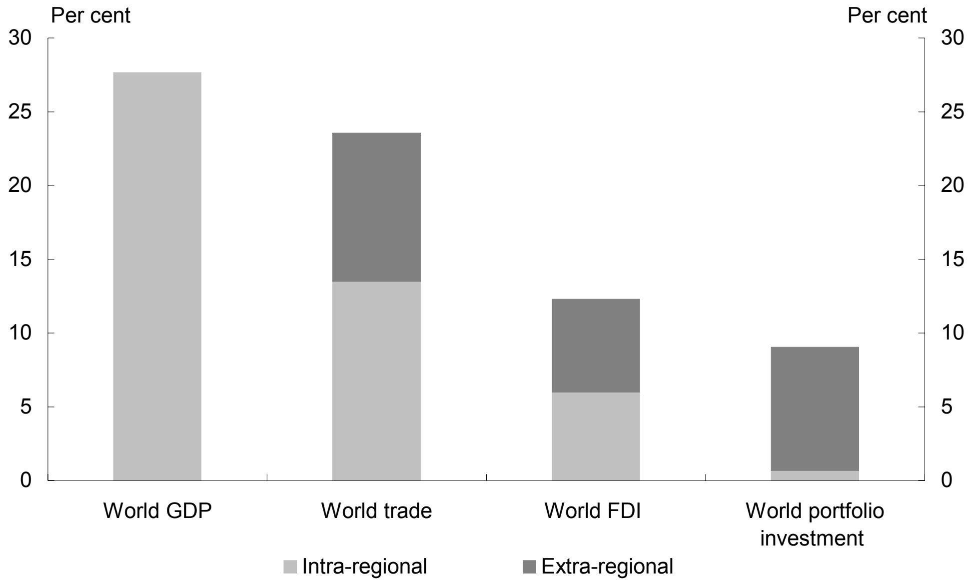
The situation in East Asia may, however, be changing. A number of preferential free trade agreements (FTAs) are under negotiation or consideration in the region, although their net economic benefits remain unclear, as discussed further below.

An equally important aspect of Asian regionalism has been a focus on regional financial cooperation with the aim of reducing financial vulnerabilities and better utilising the region's savings. In the Chiang Mai Initiative, the members of ASEAN+3 (the ten ASEAN countries plus Japan, China and Korea) have established a mechanism to provide mutual assistance in the event of future financial crises. Associated measures have been advanced in a range of forums to promote the development and integration of bond markets within Asia and the Pacific.

There appears considerable scope for further financial integration in East Asia, since international financial linkages remain much more limited than trade linkages. East Asia accounts for around one-quarter of world GDP and trade but only

12 per cent of foreign direct investment (FDI) and 9 per cent of portfolio investment (Chart 10). It is also notable that East Asia's intra-regional share of portfolio investment is very small relative to its intra-regional shares of trade and FDI. Australia's investment links with the region are also much more limited than our trade links. East Asia's share of Australia's inward and outward investment shrank during the Asian financial crisis, and has fallen further even after the region's recovery.

Chart 10: East Asia's shares, 2004



Source: CEIC Asia Database, Economist Intelligence Unit CountryData, IMF Coordinated Portfolio Investment Survey, World Development Indicators and the UNCTAD World Investment Report. Investment data are for total inward and outward investment stocks at year end. Intra-regional FDI based on intra-regional share of cumulative FDI flows for 1990-2002 (Kawai 2005).

Demographic change and labour mobility

Different demographic trends across the globe (discussed in Box 1) will be reflected in different patterns of labour force growth. Abstracting from net migration between regions, the total labour force in Russia, Eastern Europe, China and the high income countries taken together is projected to fall by around 30 million by 2025 and almost 250 million by 2050. By contrast, lower income countries will add around 800 million workers to the global labour force by 2025 and 1½ billion by 2050 (Holzmann 2005).[3]

3 In those countries with declining labour forces, there is projected to be a large rise in the number of people aged 65 and over, while in those with growing labour forces, it is projected that a 'demographic bulge' of young people will move into the working age population. The global population is projected to rise substantially — up by about 1.4 billion by 2025 and 2.6 billion by 2050 (United Nations Department of Economic and Social Affairs 2005).

These huge changes in labour supply will, in turn, likely lead to a gradual shift in the pattern of global growth from the high-income to the lower-income economies. As discussed earlier, while both China and India are projected to continue their strong economic growth and to increase significantly their shares of global output, China's more rapid ageing may gradually shift the balance between them.

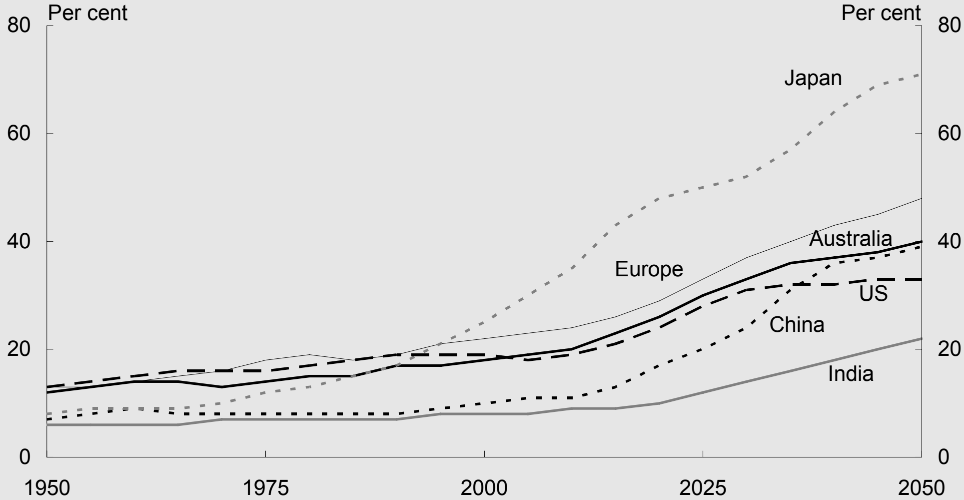
Box 1: Global demographic change

Populations across the globe are ageing because of declining rates of both mortality and fertility, which are in turn being driven by rising levels of development and improving health care. There is, however, significant diversity across countries in the rates at which these changes are occurring.

These demographic trends are manifesting themselves in rising old-age dependency ratios, which are projected to at least double for Australia, Europe, India, and Japan, but more than triple for China from now until 2050 (Chart 11). The United States old-age dependency ratio is also projected to rise but, with relatively favourable demographics, this rise is projected to be smaller than for other major countries and regions.

Chart 11: Old-age dependency ratios

Ratio of 65+ year olds to 15 to 64 year olds



Source: United Nations 2004 Revision Population Database, medium variant projections.

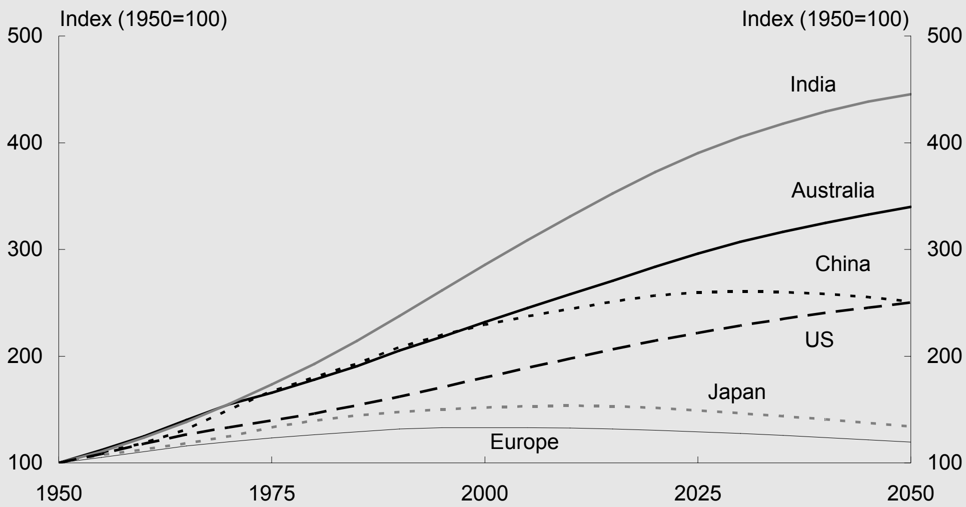
Increases in dependency ratios are projected to significantly raise government expenditures on both health and social security in both developed and developing economies. At the same time, slower economic growth — also due to population ageing — will make it difficult for many countries' governments to generate sufficient revenues to meet these projected higher levels of expenditure.

Box 1: Global demographic change (continued)

Differences in both demographic trends and openness to immigration will be reflected in sizeable differences in population growth rates across the globe (Chart 12). Due in large part to higher projected rates of immigration, population growth in Australia out to 2050 is expected to be faster than in all the other countries and regions in Chart 12 with the exception of India.

As the Chart shows, some countries and regions are expected to experience either declining or very slowly growing populations. For example, both Europe and Japan are projected to decline in population from now to 2050. China's population is projected to rise by around 10 per cent over the next quarter-century, before declining gradually after that.

Chart 12: Projected population trends[4]



Source: United Nations 2004 Revision Population Database, medium variant projections.

These changes in the global pattern of labour-force growth will generate pressures on the global economy, which may be resolved in a number of ways, including through changes in the flows of capital, people, and goods and services.

Capital mobility may be an important mechanism of adjustment to global demographic change. Internationally mobile capital should be expected to shift out of more-rapidly ageing economies into those with growing working age populations, including many developing economies and the United States. There will also be enhanced incentives to outsource business activities to lower-income countries to take

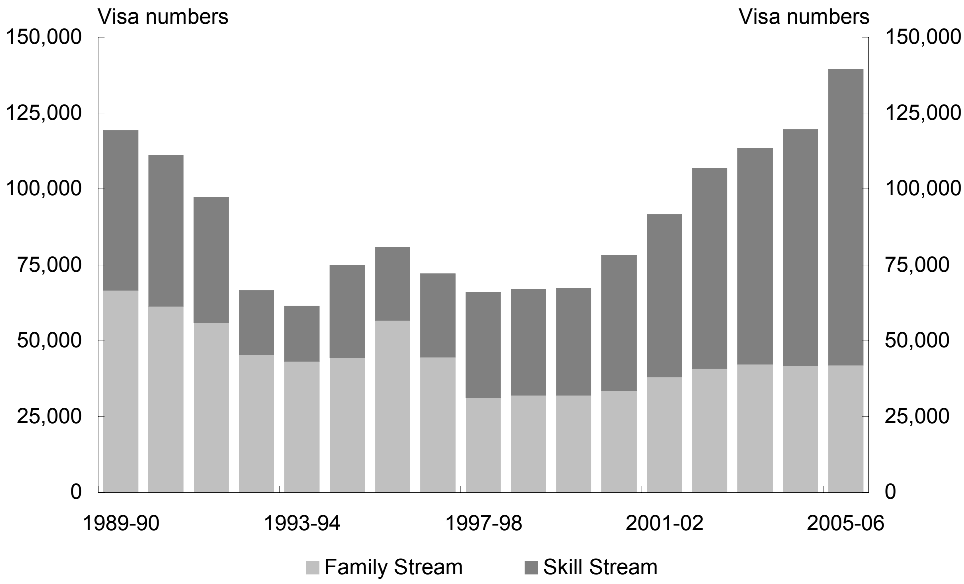
4 The projections shown for Australia differ slightly from those in the 2002-03 Intergenerational Report because they are based on slightly different assumptions.

advantage of labour cost differentials enlarged by the relative growth in labour supply in those countries.

Increased labour mobility might also be part of the adjustment process to demographic change, with at least some people moving from countries where labour is abundant to those where it is increasingly scarce, due to declining domestic labour forces. But increased immigration can only delay population ageing in developed economies since immigrants also age. Nevertheless, by delaying population ageing, increased labour mobility may give countries more time to fashion domestic policies that are more appropriate for an ageing population.

As these global demographic shifts play out over the next few decades, there is likely to be increased competition for skilled migrants as many developed countries seek to augment their labour forces via immigration programmes. This increased competition may gradually make it more difficult for Australia to attract skilled immigrants in the sort of numbers that have been attracted in recent years and may make it harder to retain skilled labour in Australia (Chart 13).

Chart 13: Composition of Australia's permanent immigration programme(a)



(a) Visa numbers for 2005-06 are planned rather than actual.
Source: Productivity Commission (2006).

Exposure to adverse external shocks

An increasingly integrated world can also generate enhanced vulnerability to international adverse shocks, although integration also enhances the possibility of international cooperation in responding to such shocks (as was the case with the global response to severe acute respiratory syndrome (SARS)), as well as increasing the scope to share risks through global financial markets. The most obvious new, or newly enhanced, possible adverse shocks include terrorism, disease epidemics or pandemics, and interruptions to energy supplies.

Terrorism

The direct economic impacts of even major terrorist attacks — through loss of life, damage to property and infrastructure, and disruption to financial and other markets — have so far been limited. The September 11 2001 attacks are estimated to have reduced United States annual GDP in the short term by only about ¼ per cent (Bruck and Wickstrom 2004). Such an estimate is clearly inherently speculative and cannot capture the impacts on wellbeing from loss of family and friends, trauma for survivors and a reduced sense of security.

In the longer term, the indirect costs of terrorism may be significantly greater. These costs arise from the deterioration in people's confidence about engaging in activities with perceived heightened terrorist risks, as well as from counter measures aimed at reducing those threats or perceptions. Some of these indirect costs — increased security, higher insurance premiums, and administration of financial and other counterterrorism regulations — are easier to estimate. The long-term cost of tighter security precautions in the wake of the September 11 attacks, for example, has been estimated to be as high as ¾ per cent of world GDP (Gupta et al 2002). And there are undoubtedly other costs associated with the threat of terrorism, which can be reduced by counterterrorist measures, although not eliminated.

Pandemics

Since late 2003, outbreaks of avian influenza have occurred in East Asia, Europe and the Middle East. This has raised concern at the prospect of a new pandemic if the avian influenza virus were to mutate to become highly infectious and lethal for humans — something the World Health Organization and other experts warn is possible.

In today's world of pervasive human mobility, a mutation of the virus which passed from human to human could spread rapidly and cause a pandemic, perhaps a global one. The counter measures needed to prevent this are not unprecedented, but would place enormous strains on public health systems for which few countries are as yet prepared.

Australia is, however, well-placed with preparatory measures including research, communication campaigns and enhancing the preparedness of regional neighbours. In addition, Australia has one of the largest stockpiles of anti-virals in the world and the Council of Australian Governments has agreed to develop an Australian Influenza Pandemic Prevention and Preparedness Action Plan (the National Action Plan) by mid-2006.

Unsurprisingly, the economic and social costs of a pandemic could be enormous. Kennedy, Thomson and Vujanovic (2006) estimate that a nationwide influenza pandemic could reduce Australian GDP by over 5 per cent in the first year. McKibbin and Sidorenko (2006) discuss a range of scenarios, and suggest that a 'severe' global pandemic could lead to the deaths of around 1 per cent of the world population and reduce GDP in the world's major economies by between 3 and 8 per cent in the first year. While such estimates are inherently speculative, they highlight the potentially extremely serious implications were a pandemic to occur.

Energy security

The world is heavily reliant on energy and, in particular, on the supply of oil. World oil demand is projected to increase by around 45 per cent over the next 20 years. Potential vulnerability is magnified by reliance on supplies from the Middle East, which already accounts for 30 per cent of world production — of which 11 per cent is from Saudi Arabia. This reliance on Middle East sources is projected to rise to 46 per cent by 2030.

Disruptions to oil supplies might arise from conflict involving key energy producers, unfavourable political shifts or major terrorist attacks. Because demand for oil is so unresponsive to price in the short run, disruptions that lead to only modest reductions in world supply could raise oil prices very substantially, at least for some time (National Commission on Energy Policy and Securing America's Future Energy, 2005).

INTERNATIONAL ECONOMIC ENGAGEMENT

The tectonic shifts reshaping the global economy have important implications not only for domestic economic policy but also for Australia's approach to international economic engagement.

Australia has a long and successful tradition of international economic engagement, and plays an active role in key global institutions such as the International Monetary Fund (IMF), the World Bank, the OECD and the G-20.[5] Australian leadership, commitment and expertise have supported the development of the Asia-Pacific Economic Cooperation (APEC) forum and other mechanisms of regional cooperation. And Australian engagement at the bilateral level has fostered a range of enduring and successful partnerships. The pattern and focus of Australia's international economic engagement, however, cannot remain fixed in the face of the far-reaching global and regional changes outlined earlier in this statement. Australia's engagement strategies,

5 The members of the G-20 are the finance ministers and central bank governors of Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom and the United States. The European Union, also a member, is represented by its Council presidency and the European Central Bank. The Managing Director of the IMF, the President of the World Bank and the chairs of the International Monetary and Financial Committee and Development Committee of the IMF and World Bank participate on an ex-officio basis. The G-20 member countries represent around 90 per cent of global GDP and around two-thirds of global population.

and the global and regional institutions it works through, must adapt to the challenges and opportunities posed by these changes.

This section focuses on three key issues:

- the strategic goals which underpin Australia's international economic engagement;
- how Australia's current engagement activities — at the multilateral, regional, and bilateral levels — help achieve these goals; and
- important engagement challenges for the future.

Before considering these issues, it is worth clarifying what is meant by the term international engagement. Put broadly, international engagement refers to Australia's efforts to persuade, negotiate with, cooperate with, learn from, and resolve differences with other governments, both directly, through bilateral relationships, and indirectly, through regional and multilateral institutions and agreements.

Australian governments since Federation have recognised the importance of effective international engagement. In an interdependent global economy, Australia will always be exposed to international risks and vulnerabilities — ranging from financial shocks or the slowdown of a major economy, to more recent threats such as terrorism or an influenza pandemic. While national efforts, including economic reforms to boost the flexibility and resilience of our economy, have played and will continue to play a central role in managing these risks, engagement with regional and global partners is also critical. It is only through effective engagement that sustained international attention and resources can be mobilised, cooperative strategies developed, and effective international rules and norms established, to deal with current and emerging regional and global challenges.

What, then, are the key strategic goals underpinning Australia's international economic engagement activities?

The overarching goal is to create a favourable international economic environment for Australia. Key elements of such an environment are:

- A stable, open and sustainably growing global economy — underpinned by effective, responsive and efficient rules-based institutions of global economic governance.
- Continued growth, development and stability in the Asia-Pacific region — and further progress in regional economic cooperation and integration.
- A network of strong, mutually supportive bilateral relationships with key strategic, commercial and development partners.

The following section examines the contribution of Australia's main engagement activities — at the multilateral, regional and bilateral levels — to these international objectives and discusses future challenges and directions.

Multilateral engagement

As a medium-sized, open economy dependent on access to global markets for goods, services, capital and labour, Australia has always had a strong stake in an open, rules-based and stable international economic system.

Through its multilateral engagement activities, the Australian Government works with other countries to: shape global trading and other rules; provide a range of global public goods including a stable global financial system; mobilise resources and expertise to support the development efforts of poorer countries; and manage challenges such as energy security, terrorism and the risk of an influenza pandemic.

This section outlines briefly three important vehicles of multilateral engagement: the World Trade Organization (WTO), the Bretton Woods Institutions (the IMF and the World Bank), and the G-20 forum of finance ministers and central bank governors.

The World Trade Organization

The WTO underpins the rules-based global trading system. The WTO's dispute resolution procedures and guiding principle of non-discrimination aim to ensure economic opportunity and fairness for all countries, regardless of economic size. Through a succession of negotiation rounds, the WTO (and its predecessor the General Agreement on Tariffs and Trade, GATT) has significantly reduced many barriers to global trade. As discussed earlier, the liberal trading system fostered by the GATT and WTO has, along with falling transport and communication costs, helped spur the process of international integration, and thereby generated expanding economic opportunities for Australia.

The scope and ambition of multilateral trade negotiations have widened significantly over recent decades. Early negotiating rounds of the GATT mainly involved a small group of developed countries and focused on lowering trade barriers for manufactured goods. The Uruguay Round, concluded in 1994, added the long-neglected areas of services and agricultural goods to the negotiation agenda and included a much wider range of countries. The current Doha Development Round of WTO talks is arguably the most ambitious on record. For the first time, large developing countries such as China, India and Brazil are playing a major role in negotiations.

These developments have increased considerably the potential global benefits of multilateral trade liberalisation (with estimates of potential gains ranging from US$18 billion to US$300 billion, depending on modelling techniques and assumptions about the coverage of the anticipated liberalisation). At the same time, they have added considerable difficulty and complexity to the negotiation task. In part, this is because of sensitivities associated with particular sectors, such as agriculture and services; in part, it is a reflection of the much wider, and more diverse, range of negotiating partners involved.

While Australia was an original contracting party to the GATT, Australia did not participate extensively in GATT negotiating rounds until the 1980s. Furthermore, it is important to bear in mind that the steps successive Australian governments have taken over recent decades to reduce protection for manufacturing industries have been undertaken on a unilateral basis to drive domestic competition, not as a result of trade negotiations. The key Australian objective for the Doha Round is to secure freer (and less distorted) trade in agricultural goods and services. To the extent that cuts to manufacturing tariffs are achieved, and they improve the export prospects of economies in East Asia, Australia — which supplies many of their inputs — will also benefit. Australia is already committed to further phase down its by-now-much-smaller manufacturing tariffs, and Doha Round commitments are unlikely to alter this timetable.

International Monetary Fund and the World Bank

The IMF and the World Bank were established after World War II to underpin the stability of the global financial system and mobilise resources for reconstruction and development. While the core responsibilities of these institutions remain unchanged, fundamental shifts in the global economy and financial markets, and the remarkable economic success of many Asian countries discussed earlier, have prompted these bodies to reconsider their roles and functions.[6]

In its early decades, the IMF fulfilled its mission by overseeing a system of fixed exchange rates with rules to prevent unilateral adjustment. When necessary, the Fund provided short-term financing support to countries experiencing temporary balance of payments difficulties; it would sometimes approve changes in exchange rates when they were assessed to be in 'fundamental disequilibrium'. As the fixed exchange rate system broke down and private capital flows increased, however, industrialised countries had less need to draw on Fund resources, and the Fund's lending activities increasingly focussed on emerging market and developing countries. Over this period, the Fund's surveillance of member countries' macroeconomic policies gradually expanded, together with its analysis of broader financial system risks and vulnerabilities. In today's world of more flexible exchange rates, sophisticated financial markets, still-growing capital flows, integrated economies and increasingly significant developing economies — many with potentially serious financial fragilities — a vigorous debate is taking place on how the Fund can best deliver on its core mission to promote the stability of the global financial system.

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6 See also Parkinson and McKissack 2003, Taylor, Tipping and McKissack 2004 and papers on the reform of the Bretton Woods institutions (Treasury Press Releases No. 6, 2005 and No. 2, 2006).

The risks posed by high and rapidly growing global imbalances are adding considerable urgency to this debate. While views differ on the causes of these imbalances and how long they can persist, it is a matter of economic logic that they cannot continue to grow forever. The question is, how will the needed adjustment unfold? In a highly integrated global economy, disorderly adjustment would cause considerable economic dislocation, and likely exacerbate already-mounting protectionist sentiments. An orderly adjustment, however, is unlikely to be achieved without concerted policy actions by the major economies. While the scope and direction of needed reforms are well known, disappointingly little progress has been made in implementing them — in part, this is a collective action problem, with each major economy reluctant to bear the possible costs of acting alone.[7] Achieving sustained progress in addressing global imbalances requires a strong multilateral response. Bilateral measures focusing on trade balances and exchange rates may pander to mercantilist sentiments, but will not, by themselves, resolve the underlying problem — which is a consequence of policies across a range of countries. Nor can the G-7, acting alone, engineer a solution, given the important role that emerging and developing economies must play in resolving imbalances. The IMF, through its surveillance activities, its planned multilateral consultation processes, and its policy advice, can support and guide the needed responses by national authorities.

The World Bank faces its own set of operational and strategic challenges. While its poverty-reduction mandate remains central, its operations continue to evolve in response to both experience and research on development. Persistent development failures, particularly in Africa but also in other regions including the Pacific, the success of some developing countries in accessing global capital markets, and increased scrutiny of Bank-supported projects, have required the Bank to examine critically its strategies, structure and effectiveness.

Successive Australian governments have played a leading role in setting the priorities and shaping the strategies of these organisations. Over the past decade, Australia has stepped up its efforts to support the reform and refocusing of these international financial institutions (IFIs). While these organisations have made some encouraging progress, reflected, for example, in the March 2006 IMF report on its medium-term strategy, Australia believes the international community must be more ambitious and comprehensive in reviewing the IFIs. The G-20 forum is well placed to support and influence this process.[8]

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7 Budget Statement 3 also discusses global imbalances and needed policy responses.

8 Indeed, as G-20 chair, Australia participated in the G-7 finance ministers' discussion on these issues in April 2006.

G-20

The G-20 forum was established in the wake of the financial crises that led to savage recessions in many emerging economies in the late 1990s. Taking a longer view, its formation can be seen as a response to the growing importance of China, India and other developing economies. The forum brings together the finance ministers and central bank governors of systemically important developed and developing countries to discuss current and emerging global economic challenges, ways to strengthen international economic governance, and shared economic policy priorities. The presence of the G-20 sends a powerful signal to other international institutions: if they fail to adapt to these challenges, including giving adequate voice to major emerging economies, they risk ineffectiveness and irrelevance.

Australia was represented at the first G-20 meeting in 1999 and has continued to play an important role in the group's short history. In late 2004, members adopted the G-20 Accord, a set of principles for sustained economic growth. In Beijing in November 2005, G-20 members proposed a 'roadmap' to shape future reform of the IMF and World Bank. In response to Australian suggestions, the G-20 has added demographic change and resource and energy issues to its agenda. In a speech delivered to a high-level forum in Los Angeles in January this year, the Treasurer outlined a vision for an 'energy freeway' linking Australia to major energy importers in the Asia-Pacific region, arguing that true energy security must be based on effective and transparent energy markets, strong regional cooperation and sound policy and regulatory frameworks at the national level.[9] Australia's hosting of the G-20 forum this year, which culminates in the ministers and central bank governors meeting in Melbourne in November, presents a valuable opportunity to advance this agenda.

Having outlined some of Australia's key multilateral engagement activities and priorities, it is appropriate to also look to the future. It would be desirable for multilateral institutions — and the rules and patterns of cooperation they foster — to play an increasing role in the future to underpin global growth, stability and sustainability. The historical record suggests that profound structural shifts in the global economy often generate opportunities for wealth creation but can also result in new sources of vulnerability and risk. Strong and effective multilateral institutions can play an important role managing these risks. Economic institutions like the IMF can help national governments deal with the policy challenges associated with the significant adjustment pressures they will face. The failure of national policy-makers to respond flexibly to the complex challenges posed by the rise of China and India, technological change and demographic pressures will result not only in missed economic opportunities; it could also spark a retreat from economic openness and the adoption of new forms of protectionism. As the period between the two World Wars amply demonstrated, there is nothing inevitable or unassailable about an open and

9 Both the G-20 Accord for sustained growth and the roadmap, the G-20 Statement on Reforming the Bretton Woods institutions, are available on the G-20 website, http://www.g20.org/. The Treasurer's speech is available at http://www.treasurer.gov.au.

stable global economic system. The founding purpose of the multilateral institutions discussed here — the GATT (the predecessor of the WTO), the IMF and the World Bank — was to restore a shattered international economy and hold in check the forces of protectionism and economic nationalism. Their task in today's world is no less urgent or important.

In fulfilling this task, these institutions must successfully negotiate three interconnected challenges. First, as mentioned above in relation to the WTO, key parts of the integration agenda are likely to be more complex and difficult than those in earlier periods. Liberalising 'behind-the-border' trade barriers, for example, is forcing trade negotiators to come to terms with a range of domestic policy constraints and sensitivities. In a world of integrated capital markets, the IMF's role in securing global financial stability requires an understanding of the structure, composition and interaction of national balance sheets. Second, as global institutions provide a greater voice to emerging economies, reaching a shared understanding on global challenges — let alone achieving consensus on common approaches — will become more difficult. Discussions and negotiations will involve a greater number of people, articulating a more diverse range of perspectives and concerns. This trend is already apparent, but will continue in coming years. It will pose particular challenges for developed economies like Australia, who will have to adapt their arguments and approaches to this new environment — and be prepared to respond to emerging economy priorities and concerns. The third challenge multilateral institutions are facing is greater demands from non-government groups — citizens, the media and interest groups — for greater transparency and accountability. While the steps multilateral institutions have taken to engage these groups should be welcomed, this needs to be balanced against their primary responsibility, which is to national governments. And in meeting this primary responsibility, greater transparency is not always appropriate. Instead, to be effective, peer discussions, surveillance activities and negotiations must take place with a degree of confidentiality. Successfully meeting these challenges will be critical to the future legitimacy, relevance and effectiveness of multilateral organisations.

Regional engagement

While Australia has global interests and engagements, our security and prosperity depend critically on the stability, growth and development of the economies of Asia and the Pacific. This section discusses APEC before turning to East Asian regionalism.

APEC

APEC is an integral part of the regional architecture of the Asia-Pacific. It is the only forum which enables Australian leaders and ministers to meet regularly with their counterparts from China, Indonesia, Japan, Korea, the United States and other Asia-Pacific economies. The APEC forum's 21 member economies represent around 40 per cent of the world's population, over half of global GDP and just under half of world trade. APEC's founding mission is to promote non-discriminatory free trade and investment in the Asia-Pacific region. In recent years, its agenda has broadened to include issues such as counter-terrorism, the risk of health pandemics and other security issues. APEC's wide membership, flexible agenda, consensus-style decision-making and lack of institutionalisation are important strengths, but also potential sources of weakness. APEC, more than most other forums, depends heavily on the commitment, skills, and vision of its members to achieve meaningful results.

Australia pursues three key economic objectives through APEC. The first is to promote unilateral trade and investment liberalisation by member countries — an objective enshrined in the Bogor Goals of free and open trade and investment in the Asia-Pacific by 2010 for industrialised economies and 2020 for developing economies. A second objective is to encourage APEC members to reduce 'behind-the-border' barriers to trade and to adopt a range of trade-facilitation measures. Behind-the-border barriers refer to domestic regulatory, competition and other restrictions which limit the productivity of member economies. With the reduction or removal of many tariffs and other border restrictions on foreign commerce, addressing domestic — or behind-the-border — barriers has become more pressing. A third objective is to boost APEC's role in fostering sound economic and fiscal policies, financial development and stability, and capital mobility through the APEC finance ministers' process.

In recent years, steps have been taken to invigorate these agendas. In 2005, APEC formally endorsed a structural reform agenda to pursue behind-the-border barriers, giving the officials-level Economic Committee a new role in coordinating structural reform activities. Under the finance ministers' process, Australia is co-sponsoring initiatives on insolvency reform, fiscal risk management and financial sector reform, with the aim of reducing medium-term structural risks in the Asia-Pacific region. Australia has become convenor of the APEC Investment Experts Group, which has been given the task of progressing APEC's investment liberalisation objectives. Australia's hosting of the APEC leaders' and ministers' meetings in 2007 provides an opportunity to achieve meaningful outcomes in these and other areas, and to secure APEC's standing and influence in the future.

East Asian regionalism

The trend towards increasing regionalism in East Asia, discussed earlier, is likely to continue for the foreseeable future. While EU-type integration is not on the agenda, East Asian countries' pursuit of regionally-based economic cooperation and integration initiatives is broadening and deepening. To date, growing regional integration has been largely a market-led process, driven by a range of factors. The most important of these factors have been: East Asian economies' outward-oriented development strategies and the associated strong demand for their manufactured exports from the United States and other industrialised economies, the emergence of region-wide supply chains and, in recent years, the rise of China as a focal point for regional economic activity. Government-led efforts have played a lesser role, although in recent years the pace, depth and ambition of regional cooperation initiatives have picked-up, led by the ASEAN+3 grouping and with the Asian Development Bank playing a supporting role.

Efforts to deepen and broaden regional integration are continuing. While the region's array of overlapping forums, including APEC, the East Asia Summit, and ASEAN+3 should be seen as an asset rather than a liability, care needs to be taken to avoid forum-overload and duplication of effort. Future regional integration efforts should be outward-looking — recognising the region's linkages with external markets — and supportive of the multilateral system. They should also be based on continued reform and liberalisation at the national level.

Australia's participation in the inaugural East Asia Summit (EAS) in Kuala Lumpur in December 2005 opened up a potentially valuable new avenue for this engagement. The EAS remains at a formative stage, with key questions concerning its role, focus, and operation yet to be settled. Nevertheless, this forum, if properly developed, could make a useful contribution to regional cooperation and integration efforts.

Australia has been a consistent supporter of regional integration and economic stability. In the wake of the Asian financial crisis, Australia and Japan were the only countries that pledged financial support for the three worst-affected countries, Indonesia, Korea and Thailand. The Treasurer has expressed support for the Chiang Mai Initiative and has signalled Australia's willingness to support its further development.[10] Australia was at the forefront of the international response to the 2004 Boxing Day tsunami, committing an initial $68 million for humanitarian assistance for Indonesia, Thailand, Sri Lanka and other affected countries, and announcing the $1 billion Australia-Indonesia Partnership for Reconstruction and Development (AIPRD).

Bilateral engagement

Australia's bilateral relationships are fundamental to the achievement of its economic engagement goals. Nation states remain the most powerful actors in international relations, notwithstanding the increasing importance of non-state actors, such as multinational corporations and non-governmental organisations, and the influence of multilateral and regional forums. Indeed, if multilateral initiatives are not supported by nation states, they cannot succeed.

Bilateral engagement between nation states is pursued for a number of reasons. Through regular contact and dialogue, ministers and officials can strengthen their understanding of other countries' policies and priorities. Bilateral economic agreements can sometimes achieve deeper levels of cooperation and integration than would be possible at the regional and multilateral levels. Bilateral diplomacy is often the starting point for regional and multilateral initiatives — indeed, by creative use of their bilateral networks, medium-sized countries like Australia can multiply their influence.

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10 See the Treasurer's address to the China-Australia Chamber of Commerce, 17 October 2005, available at http://www.treasurer.gov.au.

Australia's bilateral relationships will not be described in detail here. Suffice it to say that our strong alliance with the United States, deep and long-standing relationships with like-minded regional countries such as Japan, Korea and Singapore, traditional links with New Zealand and the United Kingdom, our crucial partnership with Indonesia, our deepening ties with China and India, and our engagement with key Pacific economies serve a range of important economic and security interests. Australia's bilateral engagement in recent years has been innovative, and has evolved in response to emerging opportunities and threats.

Australia's crucial relationship with Indonesia, for example, has been given new depth and impetus under the AIPRD, which is guided jointly by Indonesian and Australian ministers and officials. Under this partnership, a range of Australian Government agencies are forging close working links with their Indonesian counterparts.

Australian officials are also playing an important role in whole-of-government efforts to support development and reform in the Pacific. Officials have been deployed to Papua New Guinea, the Solomon Islands and Nauru to support fiscal management and economic reform efforts in these countries.

These initiatives represent a fundamentally new type of bilateral economic engagement. Under this approach, Australian policy advisers are working side-by-side with their regional counterparts in support of their efforts to build strong and effective institutions of economic governance. While traditional bilateral diplomacy remains as important as ever, the depth, complexity and range of official level contacts have increased markedly — a trend that opens up new opportunities for Australian influence, but also carries potential risks.

Bilateral free trade agreements

In recent years, the Australian Government has actively pursued preferential free trade agreements (FTAs). The first of Australia's four current FTAs was concluded with New Zealand in 1983 — the Closer Economic Cooperation (CER) agreement. This agreement initially focused on eliminating tariffs applying to trans-Tasman trade, but has been progressively expanded to include a wide array of integration issues, with the aim of creating a seamless market across both countries. The Government has recently concluded FTAs with the United States, Singapore and Thailand. FTAs are currently under negotiation with China, the 10 member countries of ASEAN, Malaysia and the United Arab Emirates. Australia and Japan are jointly studying the feasibility of a bilateral FTA.

Australia's interest in FTAs is part of a wider international trend. The WTO had received notification of 193 of these agreements in force as of 1 March 2006. The number of FTAs in the Asia-Pacific region has grown strongly: a recent APEC inventory available on its website lists 54 FTAs involving member economies, 38 being negotiated, and a further 6 under consideration. FTAs are entered into for a range of political, economic and strategic reasons. The slow pace of multilateral trade liberalisation is often cited as a motivation to conclude FTAs. Indeed, the Australian Government has stated that it will pursue FTAs which promise 'substantial economic and commercial benefits across all sectors faster than through multilateral reform'. Countries also seek FTAs for defensive reasons; to ensure that they are not excluded from networks of such agreements that one day might coalesce into trading blocs. In the view of some analysts, this competitive dynamic is one of the factors driving the proliferation of FTAs in the Asia-Pacific region.

By definition, FTAs are both liberalising (by removing trade barriers between the contracting parties) and restrictive (by retaining external barriers against excluded countries). As a general rule, FTAs that are comprehensive in scope, eliminate internal trade barriers most rapidly, cut external barriers over time (under wider regional or multilateral initiatives), and avoid restrictive rules of origin, will generate the highest net benefits for participating countries and do the least harm to excluded countries and the multilateral trading system. Australia and other countries that have embraced FTAs stand to reap important benefits from the deeper and faster liberalisation they offer, particularly in areas such as services and investment which have yet to be decisively dealt with in the WTO. Balanced against this must be recognition of the potential systemic costs of FTAs. The proliferation of FTAs in the Asia-Pacific region, for example, could create a complicated and costly business environment for traders and investors. Overlapping rules of origin, moreover, could stifle the development of region-wide supply networks — networks which are playing an important role in East Asian integration and the growth of China. FTAs can also divert attention and political commitment from the rules-based multilateral trading system — a system that open, medium-sized economies like Australia depend on so heavily. To this end, Australia is working with others in APEC to promote greater transparency, simplicity and consistency in Asia-Pacific FTAs.

CONCLUSION

This statement has discussed a range of fundamental changes in prospect for the global economy. It has focused in particular on the continuing rise in the economic importance of China and India, but also on the continuing process of globalisation, population ageing in both developed and developing economies, and the possibility of exposure to adverse international shocks like terrorism, pandemics or threats to energy security.

These prospective changes in the global economy will present both opportunities and challenges for the Australian economy in coming years. Australia's success in responding to them will depend, to a considerable extent, on maintaining high quality domestic policies and institutions; in particular, on the extent to which they support a flexible, innovative economy while at the same time providing an environment that enables individuals to adjust successfully to economic or other changes that have adversely affected them.

Over coming years, Australia's international economic engagement strategies will also play an important role in shaping our external environment. The fundamental shifts taking place in the world and our region promise expanding economic opportunities, but at the same time have sharpened existing vulnerabilities and given rise to new threats. The actions taken by the international community over the next decade, at both the global and regional levels, will play an important part in determining whether these fundamental shifts are successfully negotiated, or result in conflict and instability.

Australia's international engagement strategies are well placed to help influence these agendas. Efforts to encourage the IMF and World Bank to give major emerging economies greater voice and influence directly assist our regional engagement goals. A stronger multilateral trading system can help reduce the systemic risks posed by proliferating bilateral FTAs. Australia's network of bilateral relationships can help us project influence in regional and global forums.

Australia's hosting of the G-20 forum this year and APEC in 2007 provides an unparalleled opportunity to influence and help shape global and regional responses to the fundamental shifts described in this statement.

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STATEMENT 5: REVENUE

This statement contains details of the estimates of Australian Government revenue.

The Australian Government is providing additional personal tax relief of $36.7 billion over four years and is increasing the diminishing value rate of depreciation of eligible company assets acquired from 10 May 2006.

The revenue estimates have been revised up since the *Mid-Year Economic and Fiscal Outlook 2005-06* (MYEFO), reflecting stronger growth in expected revenue from companies and individuals in 2005-06, together with a stronger outlook for corporate profits in 2006.

Information about GST revenue is provided in Budget Paper No. 3, *Federal Financial Relations 2006-07*.

STATEMENT 5: REVENUE

OVERVIEW

Relative to the *Mid-Year Economic and Fiscal Outlook 2005-06* (MYEFO), total revenue for 2006-07 is expected to be higher, reflecting stronger growth in expected revenue from companies and individuals in 2005-06, together with a stronger outlook for corporate profits in 2006. Strong underlying growth in revenue has been partly offset by policy decisions in this budget. Personal income tax cuts of $36.7 billion (including a reduction in the fringe benefits tax rate) over four years will commence on 1 July 2006. These tax cuts are in addition to those announced in the 2005-06 Budget. The Government will also be increasing the diminishing value rate of depreciation of eligible company assets acquired from 10 May 2006, at a cost of $3.7 billion over the forward estimates.

Revenue forecasts[1] for 2005-06 and 2006-07, together with projections for the period from 2007-08, are provided in Table 1.

Table 1: Total Australian Government general government revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Total taxation revenue ($b)	**194.1**	**208.1**	**217.2**	**226.1**	**236.7**	**249.5**
Real growth on previous year(%)	6.2	2.6	1.9	3.3	3.7	3.4
Per cent of GDP	21.7	21.8	21.5	21.5	21.6	21.6
Non-taxation revenue ($b)	**12.5**	**14.8**	**14.5**	**14.6**	**15.3**	**16.2**
Real growth on previous year(%)	-0.8	13.5	-4.2	-0.2	4.1	3.3
Per cent of GDP	1.4	1.5	1.4	1.4	1.4	1.4
Total revenue ($b)	**206.6**	**222.9**	**231.7**	**240.7**	**252.1**	**265.6**
Real growth on previous year(%)	5.8	3.2	1.5	3.1	3.8	3.4
Per cent of GDP	23.1	23.3	23.0	22.9	23.0	23.0

1 All revenue estimates in this statement are reported on an accrual basis unless otherwise specified. An overview of the tax system is provided in Appendix A. Detailed estimates on a cash basis are provided in Appendix D. Commentary on accrual and cash taxation revenue and on revenue recognition issues more generally is provided in Appendix F. A historical time series of receipts outcomes is provided in Appendix H of this statement.
The revenue estimates in this statement exclude GST revenue, which is collected by the Australian Government and provided in full to the States and Territories. A discussion of GST revenue is provided in Budget Paper No. 3, *Federal Financial Relations 2006-07*.

Total revenue as a percentage of GDP is expected to decrease over the forward estimates, from 23.3 per cent of GDP in 2005-06 to 23.0 per cent in 2009-10. Taxation revenue is expected to decrease from 21.8 per cent of GDP to 21.6 per cent.

VARIATIONS IN THE REVENUE ESTIMATES SINCE THE 2005-06 BUDGET

Table 2 is a reconciliation of this budget's revenue estimates with those at the 2005-06 Budget and the 2005-06 MYEFO.

Table 2: Reconciliation of total Australian Government general government revenue estimates from the 2005-06 Budget and the 2005-06 MYEFO

	Estimates		Projections	
	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m
Revenue at 2005-06 Budget	**214,511**	**222,882**	**233,405**	**245,326**
Changes between 2005-06 Budget and MYEFO				
Effect of policy decisions	-81	-129	-126	-141
Effect of parameter and other variations	4,192	4,681	5,023	4,550
Total variations	4,111	4,552	4,896	4,409
Revenue at 2005-06 MYEFO	**218,622**	**227,434**	**238,301**	**249,735**
Changes between MYEFO and 2006-07 Budget				
Effect of policy decisions	3	-6,952	-9,939	-10,727
Effect of parameter and other variations	4,239	11,181	12,309	13,071
Total variations	4,242	4,228	2,370	2,343
Revenue at 2006-07 Budget	**222,864**	**231,662**	**240,671**	**252,078**

Total revenue for 2005-06

Since MYEFO, estimated total revenue for 2005-06 has been revised up by $4.2 billion, largely reflecting strong growth in company profits, strong capital gains for investors and robust growth in full-time employment.

Total revenue for 2006-07

Total revenue for 2006-07 has also been revised up by $4.2 billion since MYEFO. The upward revision represents the flow-on effect of stronger growth in expected revenue from companies and individuals in 2005-06, together with a stronger outlook for corporate profits in 2006.

These upward revisions have been partly offset by the impact of the Government's decision to provide additional personal tax relief and to increase the diminishing value rate of depreciation of eligible company assets acquired from 10 May 2006.

Effect of policy decisions

Policy decisions since the 2005-06 MYEFO are expected to reduce taxation revenue by around $7.0 billion in 2006-07 and around $39.1 billion over the forward years.

The Government's decision to provide additional personal income tax relief will reduce revenue by $6.4 billion in 2006-07, and $35.9 billion over the forward estimates period.

From 1 July 2006, the 30 per cent threshold will increase to $25,001; the 42 per cent marginal tax rate will be cut to 40 per cent and the threshold will increase to $75,001; and the top marginal tax rate will be reduced from 47 per cent to 45 per cent and the threshold will increase to $150,001.

The Government's personal tax cuts package includes changes to the low income tax offset (LITO). From the 2006-07 income year, the LITO will increase from $235 to $600 and will begin to phase out from $25,000. From 1 July 2006, the Medicare levy low income phase-in rate will also be reduced from 20 per cent to 10 per cent, ensuring that more low income taxpayers pay a reduced rate of Medicare levy.

In addition, the fringe benefits tax rate will be reduced to 46.5 per cent, effective from 1 April 2006, with a cost of $870 million over the forward estimates.

Reducing the top marginal rate and increasing the top threshold will improve Australia's competitiveness compared with other OECD countries. From 2006-07, the top marginal tax rate will apply to only around 2 per cent of taxpayers.

The budget also contains a number of other major policy decisions.

- Increasing the diminishing value rate for determining depreciation deductions under the diminishing value method from 150 per cent to 200 per cent for eligible assets acquired on or after 10 May 2006, with a cost to revenue of $3.7 billion over the forward estimates period.

- Taxing the distributions to non-resident trustee beneficiaries, which is expected to increase taxation revenue by $250 million in 2007-08 and $800 million over the forward estimates.

- Funding the Australian Taxation Office with an additional $82 million over four years to maintain tax compliance by high wealth individuals and their associated entities. This funding is expected to raise an additional $65 million in revenue in 2006-07 and $615 million over the forward estimates.

- Preventing some public sector superannuation schemes from improperly using pre-1 July 1988 funding credits. This is expected to increase taxation revenue by $150 million in 2006-07 and $600 million over the forward estimates.

A detailed description of the policy decisions is provided in Budget Paper No. 2, *Budget Measures 2006-07*. A summary of revenue policy decisions since the 2005-06 MYEFO is provided in Table 3.

Table 3: Revenue policy decisions since the 2005-06 MYEFO

Major policies	2006-07 $m	2007-08 $m	2008-09 $m	2009-10 $m	Total $m
Personal income tax cuts(a)	-6,385	-9,205	-9,830	-10,435	-35,855
Fringe benefits tax - reduction in rate	-260	-195	-205	-210	-870
Uniform capital allowance - diminishing value rate	-500	-900	-1,100	-1,200	-3,700
Taxation of trusts - distributions to non-resident trustees	-	250	270	280	800
Tax compliance - high wealth individuals and associated entities	65	145	190	215	615
Superannuation - ensuring appropriate use of pre-1 July 1988 funding credits	150	150	150	150	600
Other policy decisions	-22	-184	-202	-261	-669
Total revenue policy decisions	**-6,952**	**-9,939**	**-10,727**	**-11,461**	**-39,079**

(a) The personal income tax cuts and related reduction in the fringe benefit tax rate total $36.7 billion over four years.

Effect of parameter and other variations

Parameter and other variations are expected to increase revenue in 2005-06 by $4.2 billion, and revenue in 2006-07 by $11.2 billion, relative to the MYEFO forecasts.

Parameter variations

Taxation revenue growth has been revised up to 4.4 per cent in 2006-07.

The strength in taxation revenue largely stems from further improvement in corporate profitability, bolstered by the flow-on effect of stronger outcomes in 2005-06.

Looking ahead, expected growth in nominal GDP remains supportive of continued strength in revenue, particularly from the corporate sector. In underlying terms, personal income is expected to continue to grow strongly on the back of continued strength in compensation of employees and the realisation of capital gains by investors.

Further detail on how the revised outlook for the economy has affected individual revenue heads over the forward estimates is provided later in this statement. An analysis of the sensitivity of the taxation revenue estimates to changes in the major economic parameters is provided in Statement 2.

Other variations

Taxation collections to the end of the March quarter 2006 imply that the end of year outcome for taxation receipts will be 9.0 per cent above 2004-05 levels. This compares with MYEFO expectations of 7.3 per cent.

The strength in taxation collections observed since MYEFO largely reflects the cumulative effect of earlier rises in the terms of trade on corporate profits and labour market outcomes.

ESTIMATES OF REVENUE

Total revenue

Total revenue for 2006-07 is expected to increase by $8.8 billion, 3.9 per cent higher than estimated taxation revenue for 2005-06. Of this, taxation revenue is expected to increase by 4.4 per cent ($9.1 billion) and non-taxation revenue is expected to decrease by 1.9 per cent ($274 million).

The increase has resulted primarily from higher estimated revenue from companies (up $6.4 billion) and individuals (up $810 million). The revenue estimates for 2005-06 and 2006-07 are provided in Table 4. Descriptions of the revenue heads are provided in Appendix C.

Table 4: Australian Government general government revenue

	Estimates		Change on 2005-06	
	2005-06	2006-07		
	$m	$m	$m	%
Income taxation				
Individuals and other withholding				
Gross income tax withholding	103,830	104,010	180	0.2
Gross other individuals	26,410	28,480	2,070	7.8
less : Refunds	15,350	16,790	1,440	9.4
Total individuals and other withholding taxation	114,890	115,700	810	0.7
Fringe benefits tax(a)	3,660	3,720	60	1.6
Superannuation funds				
Contributions and earnings	5,390	5,890	500	9.3
Superannuation surcharge	1,030	680	-350	-34.0
Total superannuation funds	6,420	6,570	150	2.3
Company tax	50,480	56,860	6,380	12.6
Petroleum resources rent tax	1,970	2,490	520	26.4
Income taxation revenue	**177,420**	**185,340**	**7,920**	**4.5**
Excise and customs				
Excise duty				
Petrol	7,280	7,310	30	0.4
Diesel	6,240	6,420	180	2.9
Other fuel products	220	450	230	104.5
Crude oil	330	470	140	42.4
Beer	1,730	1,760	30	1.7
Potable spirits	810	890	80	9.9
Tobacco	5,290	5,320	30	0.6
Total excise duty	21,900	22,620	720	3.3
Customs duty				
Textiles, clothing and footwear	830	870	40	4.8
Passenger motor vehicles	1,258	1,300	42	3.3
Excise-like goods	1,810	2,160	350	19.3
Other imports	1,603	1,608	5	0.3
less : Refunds and drawbacks	330	300	-30	-9.1
Total customs duty	5,171	5,638	467	9.0
Excise and customs revenue	**27,071**	**28,258**	**1,187**	**4.4**
Other taxation				
Wine equalisation tax	660	660	0	0.0
Luxury car tax	320	320	0	0.0
Agricultural levies	607	619	11	1.9
Other taxes	2,007	1,960	-47	-2.3
Other taxation revenue	**3,594**	**3,559**	**-35**	**-1.0**
Taxation revenue	**208,085**	**217,157**	**9,072**	**4.4**
Non-taxation				
Sales of goods and services	4,898	4,846	-52	-1.1
Interest received	2,386	3,717	1,330	55.7
Dividends	4,321	2,701	-1,621	-37.5
Other	3,173	3,241	68	2.2
Non-tax revenue	**14,779**	**14,505**	**-274**	**-1.9**
Total revenue	**222,864**	**231,662**	**8,798**	**3.9**

(a) See fringe benefits tax description in Appendix C.

Box 5.1: Revised revenue recognition methodology

Accrual accounting was introduced by the Australian Government in the 1999-2000 Budget. The AAS and GFS standards for accrual accounting (refer to Appendix A in Statement 2 for an explanation of these reporting standards) require that taxation revenue be recognised in the reporting period in which the taxpayer earns the income that is subsequently subject to taxation — this is known as the Economic Transactions Method (ETM). But the standards also permit government reporting using an alternative approach when the ETM approach would generate unreliable measures of taxation revenues.

Because ETM is an unreliable measure for several significant revenue heads — and these account for the majority of total revenue — all taxation revenue has been recognised in all accrual budget-related documentation since the 1999-2000 Budget using the Tax Liability Method (TLM). Under TLM, taxation revenue is accounted for at the time a taxpayer makes a self-assessment or when an assessment of a taxation liability is raised by the relevant authority.

Commencing with this budget, the Government has adopted ETM revenue recognition for all revenue heads where the measurement issues are not material, but will retain TLM revenue recognition where ETM measurement issues may be material. Consequently, the taxation revenues that will continue to be recognised on a TLM basis are:

- individuals and other withholding taxation;
- company income taxation; and
- superannuation taxation.

Further details about taxation revenue recognition are provided in Appendix F.

Revenue estimates by revenue head

Income taxation revenue

Individuals and other withholding taxation

Estimated revenue from individuals for 2005-06, 2006-07 and the projection years is provided in Table 5. Estimated revenue from individuals in 2006-07 is expected to increase by $810 million (0.7 per cent), reflecting solid labour market outcomes and moderate growth in personal investment income, partially offset by personal income tax cuts.

Table 5: Individuals and other withholding taxation revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Individuals and other withholding						
Gross income tax withholding	98,250	103,830	104,010	109,540	116,620	124,870
Gross other individuals	24,003	26,410	28,480	29,670	32,000	34,770
less: Refunds	13,734	15,350	16,790	18,690	19,970	21,260
Total	**108,519**	**114,890**	**115,700**	**120,520**	**128,650**	**138,380**
Includes Medicare levy(a) revenue of:	6,105	6,560	6,950	7,410	7,840	8,330

(a) Medicare levy for 2004-05 is an estimate.

Gross income tax withholding

Gross income tax withholding (ITW) revenue is expected to increase by $180 million (0.2 per cent) in 2006-07, reflecting the continuing strength in compensation of employees partially offset by the Government's decision to provide additional personal income tax relief.

Gross other individuals

Gross revenue from other individuals is expected to increase by $2.1 billion (7.8 per cent) in 2006-07.

This increase reflects expected personal investment income from capital gains from continued strength in the share market, partially offset by the effect of additional tax cuts.

Income tax refunds for individuals

Refunds for individuals are expected to increase by $1.4 billion (9.4 per cent) in 2006-07.

Refunds are generally related to movements in revenue from ITW and gross other individuals in the previous year.

Medicare levy

Revenue from the Medicare levy is expected to increase by $390 million in 2006-07. Movements in revenue from the Medicare levy are generally consistent with growth in personal taxable income.

Fringe benefits tax

Estimated revenue from fringe benefits tax for 2005-06, 2006-07 and the projection years is provided in Table 6.

Table 6: Fringe benefits tax revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Fringe benefits tax(a)	3,476	3,660	3,720	3,810	3,920	4,050

(a) See fringe benefits tax description in Appendix C.

Revenue from fringe benefits tax is expected to increase by $60 million (1.6 per cent) in 2006-07. The revised estimate for 2006-07 reflects the reduction in the tax rate to 46.5 per cent.

Superannuation funds

Estimated revenue from superannuation funds for 2005-06, 2006-07 and the projection years is provided in Table 7.

Table 7: Superannuation funds revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Superannuation funds						
Contributions and earnings	5,083	5,390	5,890	6,400	6,950	7,560
Superannuation surcharge	1,326	1,030	680	110	40	30
Total	**6,410**	**6,420**	**6,570**	**6,510**	**6,990**	**7,590**

Superannuation funds taxation

Taxation revenue from superannuation contributions and earnings income is expected to increase by $500 million (9.3 per cent) in 2006-07, reflecting strong earnings growth.

Superannuation surcharge

Revenue from the superannuation surcharge is expected to decrease by $350 million (34.0 per cent) in 2006-07, reflecting the effect of its abolition. While the abolition of the surcharge extinguishes future liabilities from accruing, allowance has been made over the forward estimates period in relation to the identification of liabilities which accrued prior to 1 July 2005.

Company and other related income taxation

Estimated revenue from companies for 2005-06, 2006-07 and the projection years is provided in Table 8.

Table 8: Company and other related income taxation revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Company tax	43,106	50,480	56,860	59,400	59,950	61,800
Petroleum resource rent tax	1,465	1,970	2,490	3,250	3,740	4,000
Total	**44,570**	**52,450**	**59,350**	**62,650**	**63,690**	**65,800**

Company income taxation

Company tax revenue is anticipated to increase by $6.4 billion (12.6 per cent) in 2006-07, largely driven by strength in the finance, insurance and mining industries.

With business conditions remaining favourable, profit growth is expected to remain strong through 2006-07. In particular, Australian mining companies have benefited from a surge in external demand for bulk commodities — particularly from China. However, as detailed in Statement 3, supply chain disruptions and adverse weather conditions affected the ability of Australian mining companies to fulfil their contracted export volumes in 2005-06. In 2006-07, it is anticipated that these temporary factors will abate and additional capacity will come on stream — boosting both company profits and company tax revenue in the budget year.

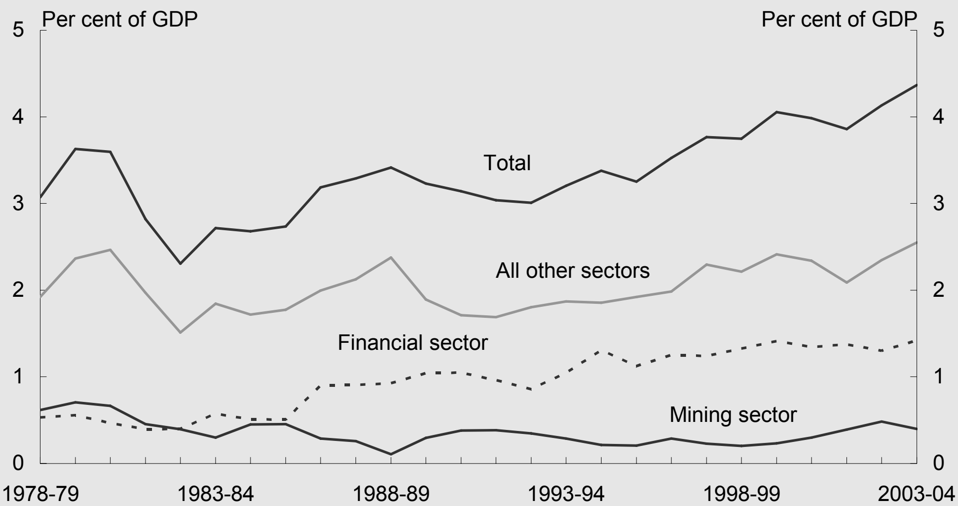
The company tax revenue estimates over the projection years of 2007-08, 2008-09 and 2009-10 reflect a technical assumption that coal and iron ore prices will return to long-term average levels over the first two years of the projection period (see Box 6 in Statement 3).

Box 5.2: Some observations on trends in company tax collections

The strength of company tax collections has been highlighted in previous budgets, and it continues to be a major contributor to the strength in forecast revenue in 2006-07. This strength has been underpinned by Australia's long economic expansion and the consequent strong growth in corporate profitability.

Company profits have been growing faster than GDP. Company taxation revenue has also been increasing as a proportion of GDP — Chart 1. At an industry level, profits in the financial sector and, more recently, the mining sector, have grown faster than the rest of the corporate sector. Reflecting this, these industries made significant contributions to the growth in company taxation revenue as a proportion of GDP.

Chart 1: Company tax revenue



Source: Treasury estimates using ATO *Taxation Statistics* and ABS cat. no. 5206.

In previous budgets, attention was drawn to a number of other factors which have also contributed to the growth in revenue. These include the privatisation of major Government Business Enterprises, growth in capital gains derived by companies, the dividend imputation system and more effective compliance activities of the Australian Taxation Office.

This box contains some further observations on the impact of developments in the corporate income base on trends in company taxation revenue. These developments include the interaction of the high inflation environment of the 1980s with company tax payment arrangements and the high corporate debt-servicing ratios that prevailed in the 1980s and early 1990s.

Box 5.2: Some observations on trends in company tax collections (continued)

The effective corporate tax rate

The strength of company taxation receipts has seen the effective corporate tax rate (measured as the ratio of company income tax paid to gross operating surplus) rise in recent years. It is currently not far above its long-run average — Chart 2.

Chart 2: The effective corporate tax rate

Source: ABS cat. no. 5206.

One factor contributing to the rise in the observed effective corporate tax rate has been reforms to company tax payment arrangements.

Until the late 1980s, a company's taxation liability was due for payment entirely in the year following the year of income, providing companies with a taxation deferral advantage relative to other taxpayers. Consequently, in an environment of profit growth, the effective tax rate measured one year's tax liability over the next year's higher income. The deferral advantage had the effect of artificially lowering the effective tax rate in the 1980s.

Payment system reforms since the late 1980s have brought forward the timing of the payments, so that they are now broadly contemporaneous with the year of income, and the effective tax rate is higher as a consequence.

Company debt-servicing ratio

Trends in the debt-servicing ratios of corporations can also help to explain movements in the effective company tax rate, and in particular its unusually low level through the 1980s and into the 1990s.

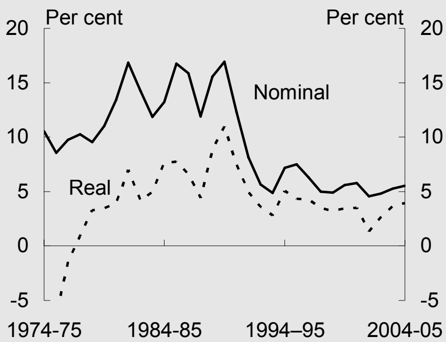
Nominal and real interest rates rose sharply in late 1970s and remained high, by current standards, until the return to a low inflation environment in the early 1990s — Chart 3. At the same time, corporate debt levels were also rising, with this

Box 5.2: Some observations on trends in company tax collections (continued)

trend accelerating sharply over the second half of the 1980s, following financial deregulation, before a subsequent period of debt reduction in the early 1990s — Chart 4. These developments saw the debt-servicing ratio of corporations jump sharply in the 1980s and remain high until the early part of the 1990s — Chart 5.

Chart 3: Nominal and real interest rates

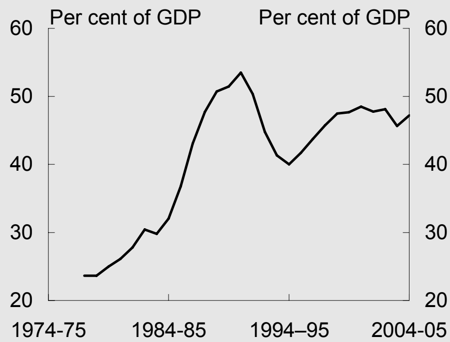
90 day bank bill rate



Source: RBA Bulletin and Treasury estimates.

Chart 4: Corporate debt indicator

Bank-intermediated corporate debt

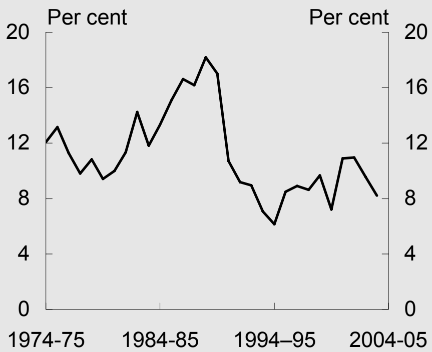


Source: RBA Bulletin and ABS cat. no. 5206.

The high levels of the corporate debt-servicing ratio in the 1980s and early 1990s had the effect of depressing the effective corporate tax rate over this period, since the interest costs of debt finance are generally deductible in calculating taxable income. As the gearing of corporations returned to more sustainable levels, and interest rates fell in line with the resumption of low inflation, the corporate debt-servicing ratio fell in the 1990s, unwinding the earlier depressing effect on the effective corporate tax rate — Chart 6.

Chart 5: Corporate debt-servicing ratio[(a)]

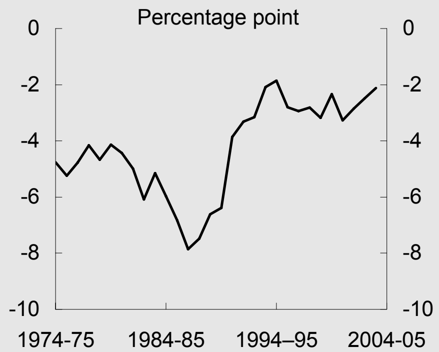
Net interest payments to corporate GOS



(a) Non-financial corporations.
Source: Treasury estimates using ATO *Taxation Statistics* and ABS cat. no. 5206.

Chart 6: Impact of debt[(a)] on company tax

Contribution to effective corporate tax rate



(a) Non-financial corporations.
Source: Treasury estimates using ATO *Taxation Statistics* and ABS cat. no. 5206.

Petroleum resource rent tax

Estimated revenue from the petroleum resource rent tax is expected to increase by $520 million (26.4 per cent) in 2006-07, reflecting the impact of higher expected profitability of offshore petroleum projects from higher oil prices in Australian dollars.

Excise and customs revenue

Estimates for 2005-06, 2006-07 and the projection years are provided in Table 9 for excise and customs revenue.

Table 9: Excise and customs revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Excise duty						
Petroleum and other fuel products						
Petrol	7,371	7,280	7,310	7,400	7,490	7,590
Diesel	6,164	6,240	6,420	6,650	6,860	7,080
Other fuel products	147	220	450	470	520	510
Total	13,682	13,740	14,180	14,520	14,870	15,180
Crude oil	668	330	470	310	200	120
Beer	1,653	1,730	1,760	1,790	1,820	1,850
Potable spirits	741	810	890	970	1,070	1,180
Tobacco	5,237	5,290	5,320	5,340	5,360	5,380
Total excise duty	21,981	21,900	22,620	22,930	23,320	23,710
Customs duty						
Textiles, clothing and footwear	966	830	870	930	990	760
Passenger motor vehicles	1,397	1,258	1,300	1,370	1,440	1,190
Excise-like goods	1,697	1,810	2,160	2,290	2,410	2,550
Other imports	1,793	1,603	1,608	1,718	1,839	1,958
less : Refunds and drawbacks	306	330	300	300	300	300
Total customs duty	5,548	5,171	5,638	6,008	6,379	6,158
Total	**27,529**	**27,071**	**28,258**	**28,938**	**29,699**	**29,868**

Excise duty

In 2006-07, revenue from excise duty on petroleum is expected to increase by $30 million (or 0.4 per cent), which is a decline in real terms. Excise from other fuel products is expected to increase by $230 million (104.5 per cent) in 2006-07. This arises principally from recent fuel tax changes which apply the full rate of excise which is netted off by a credit scheme. This head records the revenue. The credit scheme is recorded in expenses. While revenue increases, so do expenses.

Revenue from crude oil excise duty is expected to increase by $140 million (42.4 per cent) in 2006-07, reflecting the effect of higher estimated oil prices on desired production levels.

Other excise revenue is expected to increase by $140 million (1.8 per cent) in 2006-07, reflecting higher estimated revenue from beer and the ready to drink category of alcoholic beverages.

Customs duty

Customs duty revenue is expected to increase by $467 million (9.0 per cent) in 2006-07, reflecting solid growth in expected imports.

Other taxation revenue

Revenue estimates for 2005-06, 2006-07 and the projection years are provided in Table 10 for the wine equalisation tax, the luxury car tax, agricultural levies and other taxes.

Table 10: Other taxation revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Wine equalisation tax	693	660	660	670	690	710
Luxury car tax	302	320	320	340	360	380
Agricultural levies	584	607	619	614	605	424
Other taxes	2,068	2,007	1,960	2,024	2,137	2,249
Total	**3,647**	**3,594**	**3,559**	**3,648**	**3,792**	**3,763**

Total other taxation revenue is estimated to decrease by $35 million (1.0 per cent) in 2006-07.

Revenue from the wine equalisation tax and the luxury car tax is expected to remain unchanged from 2005-06 levels, reflecting underlying demand in both those markets.

Revenue from agriculture levies in 2006-07 is also expected to be largely unchanged from the 2005-06 levels.

Other taxes are expected to decrease by $47 million (2.3 per cent) in 2006-07, largely reflecting the phasing out of the aircraft noise levy for Sydney Airport and the stevedoring levy.

Non-taxation revenue

Revenue estimates for 2005-06, 2006-07 and the forward years are provided in Table 11 for the various categories of non-taxation revenue. Item descriptions are in Appendix C.

Table 11: Non-taxation revenue

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Sales of goods and services	4,388	4,898	4,846	4,975	5,114	5,255
Dividends	3,176	4,321	2,701	2,866	3,058	3,228
Interest received	1,621	2,386	3,717	3,457	4,005	4,647
Other non-taxation revenue(a)	3,271	3,173	3,241	3,297	3,160	3,021
Total	**12,455**	**14,779**	**14,505**	**14,595**	**15,338**	**16,151**

(a) Includes all other non-taxation revenue collected by the Australian Government agencies.

Non-taxation revenue is expected to decrease by $274 million (1.9 per cent) in 2006-07, largely reflecting decreased dividend income as a result of the sale of Telstra. This is partially offset by interest and dividends earned by the Future Fund. The fund received its seed funding of $18 billion in May 2006 and the estimates assume that the proceeds from the Telstra sale will be transferred to the Future Fund.

APPENDIX A: AUSTRALIA'S TAX SYSTEM

AUSTRALIA'S TAX SYSTEM COMPARED WITH THE OECD

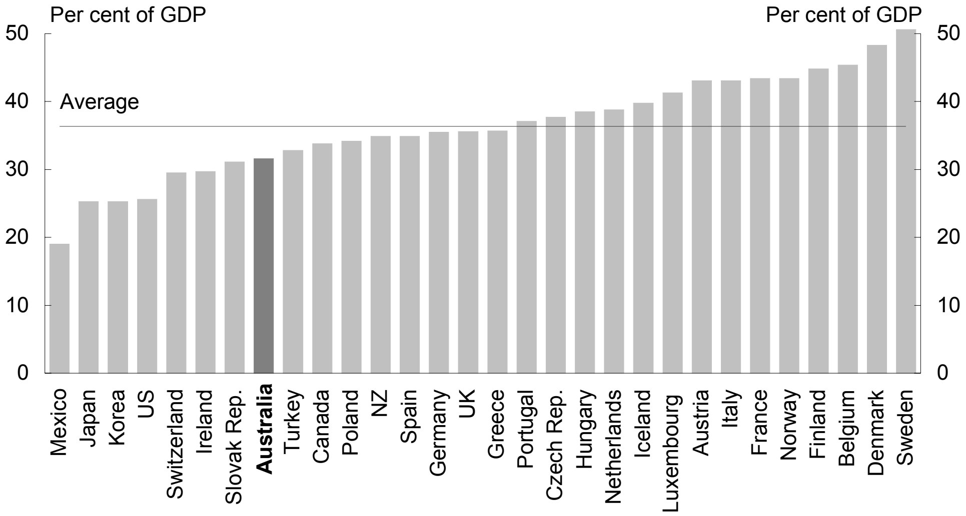
The analysis in this section includes the tax systems of all levels of government combined — national, state and local. Comparisons are provided with the tax systems of other OECD economies.

Tax burden

Australia has a low tax burden, both currently and historically. In 2003, Australia had the eighth lowest tax burden of the OECD countries (Chart A1) and has typically ranked in the bottom third of countries for the period since 1965.

- Australia's tax burden as a proportion of GDP is 31.6 per cent, which is below the OECD average of 36.3 per cent.

Chart A1: Total tax burden for OECD countries, 2003[(a)]

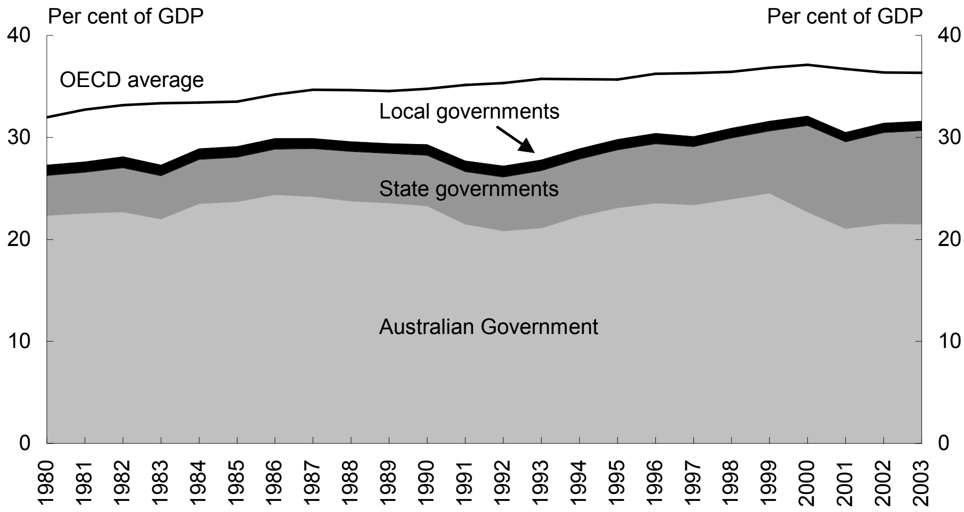


(a) The OECD's measure of the tax burden is the total taxation revenue of national, state and local governments expressed as a percentage of gross domestic product. For Australia, the data are for the 2003-04 financial year, the latest year where comparable international data are available.
Source: OECD *Revenue Statistics*, 2005.

While the total tax burden for Australia has been relatively steady over recent years, the tax burden of the Australian Government has fallen while the tax burden of the states has increased (Chart A2).

Chart A2: The Australian tax burden by government sector

Total taxation revenue as a proportion of GDP, 1980-2003



Source: OECD *Revenue Statistics*, 2005.

The tax burden of Australia's state governments increased from 6.1 per cent of GDP in 1999 to 8.5 per cent of GDP with the introduction of the goods and services tax in July 2000. The goods and services tax replaced a range of state government taxes and grants from the Australian Government. Since 2000, the tax burden of the state governments has increased by a further 8 per cent (or 0.7 percentage points), taking the state government tax burden to 9.2 per cent of GDP in 2003.

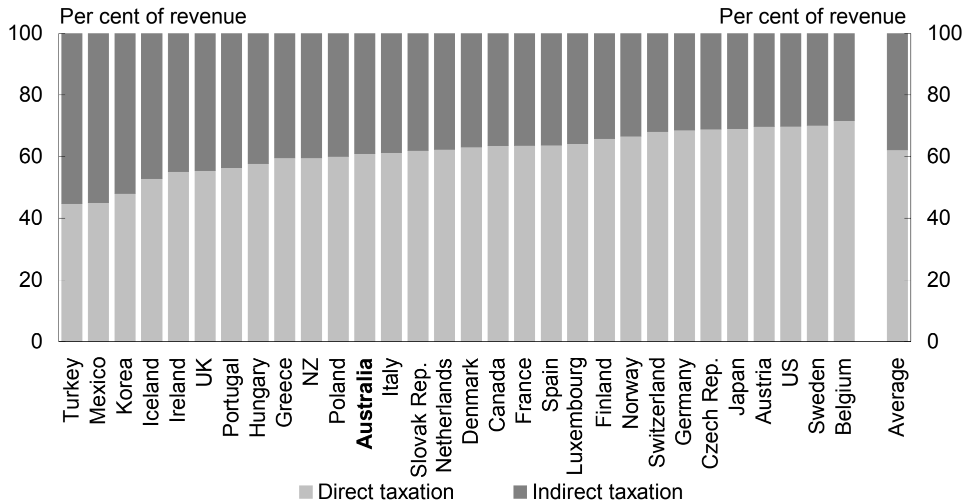
Tax mix

The Australian tax mix is broadly similar to most OECD countries (Chart A3), although there are a few distinguishing features.

- Like most other advanced countries, Australia raises the majority of its taxation revenue (60.9 per cent in 2003) from direct taxation levied on incomes — wages, salaries, payrolls and profits. This is below the OECD average of 62.2 per cent. Japan (69.0 per cent) and the United States (69.8 per cent) have a higher reliance on direct taxation than Australia.

- The remaining 39.1 per cent of Australia's taxation revenue is derived from indirect taxation — including the goods and services tax (value added tax), excise and customs duty, and property taxes. The OECD average is 37.8 per cent.

Chart A3: Direct and indirect taxation revenue as a proportion of total taxation revenue for OECD countries, 2003

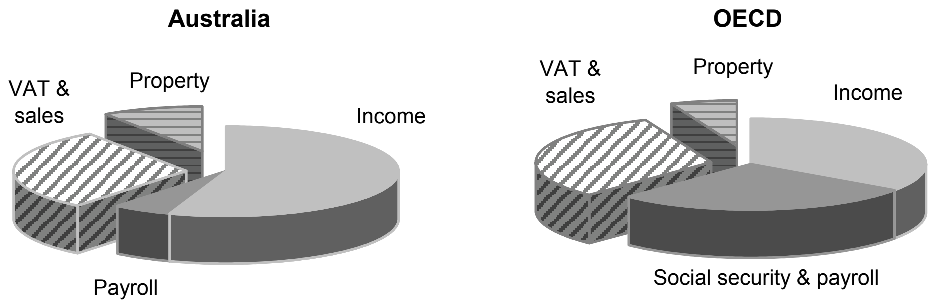


Source: OECD *Revenue Statistics*, 2005.

When income taxes, payroll taxes and social security taxes are taken together, the share of Australia's direct taxes in total taxation is broadly comparable with the OECD average (Chart A4). However, for a significant number of countries, social security taxes are now the largest source of direct taxation revenue.

Chart A4: Australia's tax mix compared with the OECD average

Direct and indirect taxation revenue as a proportion of total taxation revenue, 2003



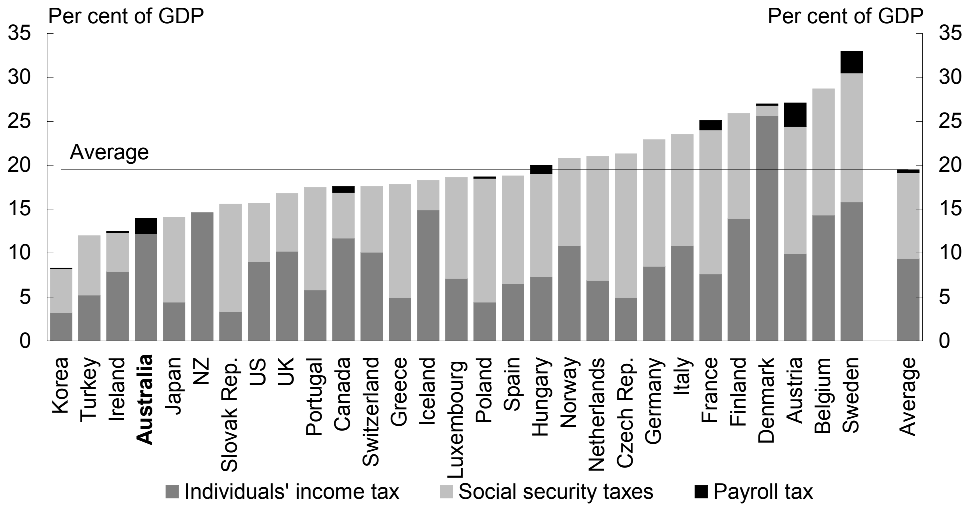
Source: OECD *Revenue Statistics*, 2005.

- Social security taxes are payments to institutions of general government that are earmarked to provide social security benefits. They usually consist of two components — one withheld from employees' wages and the other paid by employers. Both components are treated by the OECD as a tax on the income of individuals because they form part of an employee's remuneration.

- Examples of social security benefits funded through social security taxes include: unemployment insurance benefits and supplements; accident, injury and sickness benefits; old age, disability and survivors' pensions; family allowances; reimbursements for medical and hospital expenses; and provision of hospital or medical services. Australia funds these types of government programmes through general taxation revenue rather than a specific social security tax.

Australia has the fourth lowest level of direct taxation on individuals and payrolls in the OECD (Chart A5). Australia's tax burden (14.0 per cent of GDP) is significantly lower than the OECD average (19.5 per cent).

Chart A5: Components of direct taxation in respect of individuals and payrolls, 2003



Source: OECD *Revenue Statistics*, 2005.

AUSTRALIAN GOVERNMENT TAXES

The analysis in the previous section included the tax systems of all levels of government combined. This section includes just the taxes of the Australian Government — that is, it excludes taxes imposed by state and local governments.

Tax mix

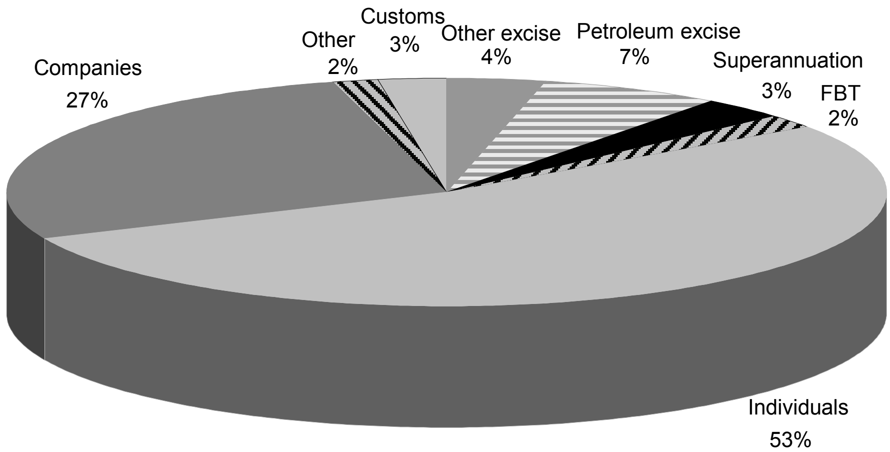
The Australian Government's main source of revenue is through the raising of taxes on income. These represent around 85 per cent of total taxation revenue (Chart A6).

- Of this, 53 per cent of total taxation revenue is sourced from personal income taxes. A further 3 per cent comes from taxes levied on superannuation and 2 per cent from taxes on fringe benefits payments.

- Company income taxes account for 27 per cent of total taxation revenue.

Most of the remaining taxation revenue is accounted for by excise and customs duties, which contribute 13 per cent of total taxation revenue.

Chart A6: Australian Government tax mix, 2006-07



Personal income tax distribution

The personal income tax system is progressive in nature. The intent of a progressive tax system is for the tax burden to be borne by those individuals who are best placed to bear it, while those individuals who have limited means bear relatively little or no tax.

- For the 2003-04 income year (the latest year for which tax return data is available from the ATO), 50 per cent of personal income tax was collected from the 14 per cent of taxpayers who were in the top marginal tax bracket, and 63 per cent of the tax burden was collected from the 24 per cent of taxpayers who earned more than $52,000 in taxable income.

- In comparison, the 23 per cent of taxpayers who earned less than $21,600 in taxable income paid only 3 per cent of the tax burden.

- The 53 per cent of middle income tax payers (in the $21,600 to $52,000 income range) paid only 34 per cent of the tax burden.

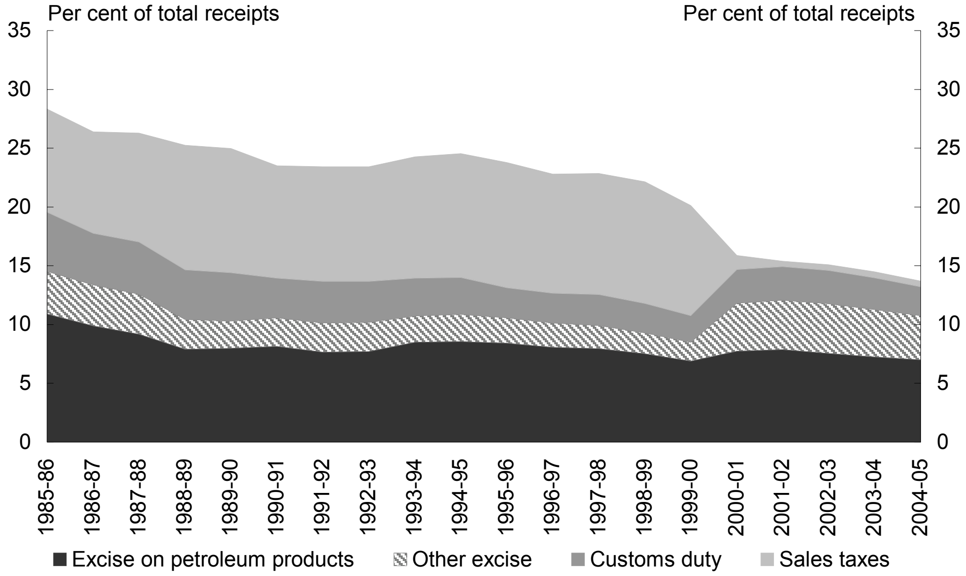
Company income tax distribution

Most company income tax is paid by a relatively small group of large companies. For the 2003-04 income year (the latest year for which tax return data is available from the ATO), around three-quarters of company income tax was collected from the 3 per cent of incorporated taxpayers which earned more than $10 million in total income.

Indirect taxes

The share of indirect taxes in total revenue is in long term decline because some of the indirect tax bases do not grow as quickly as the income tax bases and also because of policy decisions taken by governments to reform the indirect tax bases (Chart A7). With the abolition of wholesale sales tax, the removal of indexation from petroleum excise and trade liberalisation, indirect taxation revenue is expected to continue to decline in relative importance for the Australian Government.

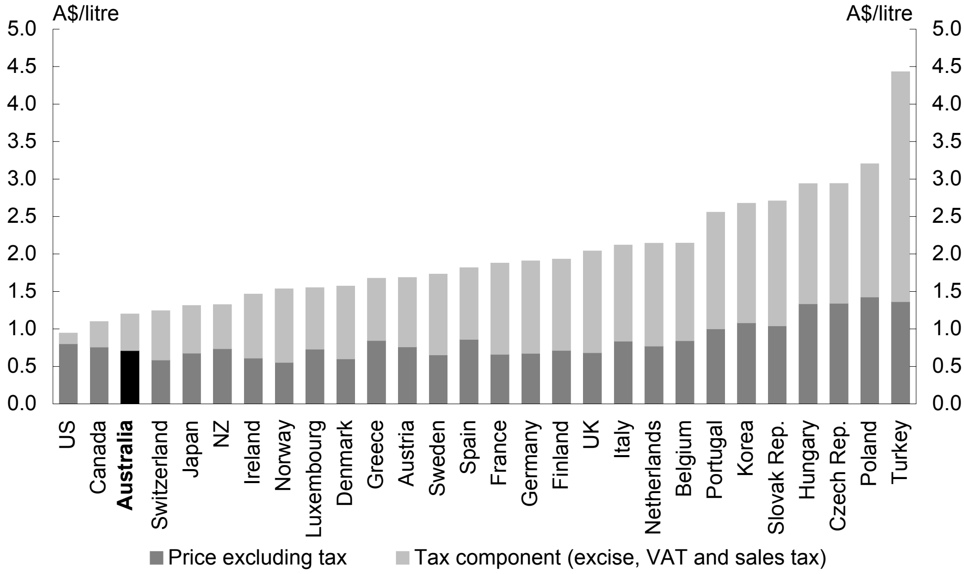
Chart A7: Australian Government indirect taxes



The rate of excise duty on unleaded petrol in Australia is 38.1 cents per litre. It has been at this level since the indexation of petrol rates to the consumer price index (CPI) ceased in March 2001. The impact of nominal tax rates on unleaded petrol, combined with the impact of general consumption taxes (VAT, GST and sales taxes), is shown in Chart A8 for OECD countries. Under this combined measure, which illustrates the total tax impost on consumers, the average level of tax included in petrol prices for the OECD countries shown was A$1.15 per litre in the last quarter of 2005. In comparison, the level of tax included in unleaded petrol prices in Australia for this quarter was less than half this amount at A$0.49 per litre — the third lowest of the OECD countries for which comparable data are available.

Chart A8: Unleaded petrol prices[(a)]

OECD countries, fourth quarter 2005



(a) Converted to Australian dollars using OECD Purchasing Power Parities. Data is for the fourth quarter of 2005 or the latest available. Data for Iceland and Mexico was not available.
Source: Australian Treasury estimates based on International Energy Agency data.

APPENDIX B: NET TAX THRESHOLDS

The impact of taxes on Australian households should be assessed alongside the level of assistance going to families from the government, either as offsets to tax or through direct payments.

Since 1996, the Government has substantially increased the level of Family Allowance and Family Tax Benefit provided to families (from around 1.3 per cent of GDP to 1.8 per cent of GDP in 2005-06). In particular, the Government has increased the real disposable income of families through the introduction of measures such as the Family Tax Benefit and the Baby Bonus, which will increase from $3,000 to $4,000 from 1 July 2006.

One way of illustrating the combined effect of cash transfers and tax for families is by showing the change in the real net tax threshold. The net tax threshold is the point at which taxes paid begin to exceed cash transfers received. Table B1 shows that the net tax threshold will have increased by more than 38 per cent in real terms between 1996-97 and 2006-07 for a range of families.

Table B1: Increases in real net tax thresholds for families[a], 1996-97 to 2006-07

	Real net tax threshold		
Family type(b)	1996-97	2006-07	Per cent change
Sole parent	$34,594	$48,065	38.9
Single income couple with children	$34,021	$48,065	41.3
Dual income couple with children (75:25 split)	$34,650	$51,829	49.6
Dual income couple with children (60:40 split)	$34,749	$50,910	46.5
Dual income couple with children (67:33 split)	$34,703	$51,808	48.1

(a) The net tax threshold is the level of private income at which income tax paid first exceeds cash benefits received. Dollar amounts are calculated in 2005-06 prices.

(b) Families are assumed to have two children — one aged 3 years and the other aged 8 years. The numbers in brackets represent the wages of each working adult in the family, expressed as a proportion of average weekly ordinary time earnings for full-time employees (AWOTE).

APPENDIX C: DESCRIPTION OF THE REVENUE HEADS

Income taxation

Individuals and other withholding taxation

These revenue heads broadly cover all personal income tax. A schedule of the personal income tax rates for the period covered in this budget is provided in Table C1.

Gross income tax withholding

Gross income tax withholding includes all taxes withheld from payments made under the Pay-As-You-Go (PAYG) withholding system and amounts withheld because no Tax File Number or Australian Business Number was quoted. It also includes applicable Medicare levy revenue.

The bulk of ITW revenue arises from taxes withheld from wage and salary income, but also includes all other withholding taxes levied on natural resource payments, dividends, interest and royalties paid to non-residents, and payments to Australian indigenous groups for the use of land for mineral exploration and mining. These taxes are often withheld from companies, rather than individuals, but are not separately identified from other PAYG revenues.

Gross other individuals

Gross revenue from other individuals consists of income tax paid by individuals other than that collected through the PAYG withholding system, and includes applicable Medicare levy revenue. It comprises:

- PAYG instalments paid directly by individuals — that is, not withheld by employers; and
- debit assessments on income tax returns.

Taxpayers in this category derive their income from many sources, including:

- profits from small unincorporated businesses, primary production and investment activities;
- wages and salaries (when PAYG withholding credits are insufficient to meet the tax liability on assessment); and
- capital gains.

Most revenue from other individuals is collected directly from the taxpayer through the PAYG instalment system. Individuals with annual tax liabilities of $8,000 or more and individuals who are registered for the GST will generally make quarterly payments. Individuals who have annual taxation liabilities of less than $8,000 and are not registered for the GST have the choice of making quarterly payments or an annual payment.

Income tax refunds for individuals

A final assessment of the income tax liabilities of individual taxpayers is normally made on the basis of returns lodged after the end of each financial year. Refunds from the ATO are made where tax credits to an individual exceed their final liability on assessment. Conversely, when tax credits are insufficient to meet the final tax liability, taxpayers are required to make an additional payment for the difference.

Medicare levy

Medicare is the scheme that gives Australian residents access to public health care. To help fund the scheme, resident taxpayers pay a Medicare levy. The amount of levy paid is based on an individual's taxable income and is normally calculated at 1.5 per cent of taxable income, but this rate may vary depending on circumstances. An individual may be exempt from the levy or it may be reduced if the taxpayer has a low income. Individuals and families on higher incomes who do not have an appropriate level of private hospital cover may also have to pay the Medicare levy surcharge, which is calculated at an additional 1 per cent of taxable income.

Low income tax offset

The low income tax offset provides targeted tax relief to low income earners. The LITO is claimable on assessment and reduces a taxpayer's tax liability.

Table C1: Personal income tax rates[(a)]

	From 1 July 2003		From 1 July 2004		From 1 July 2005		From 1 July 2006	
	Taxable income	Per cent	Taxable income	Per cent	Taxable income	Per cent	Taxable income	Per cent
Residents	$0–$6,000	Nil	$0–$6,000	Nil	$0–$6,000	Nil	$0–$6,000	Nil
	$6,001–$21,600	17	$6,001–$21,600	17	$6,001–$21,600	15	$6,001–$25,000	15
	$21,601–$52,000	30	$21,601–$58,000	30	$21,601–$63,000	30	$25,001–$75,000	30
	$52,001–$62,500	42	$58,001–$70,000	42	$63,001–$95,000	42	$75,001–$150,000	40
	> $62,500	47	> $70,000	47	> $95,000	47	> $150,000	45
Non-residents	$0–$21,600	29	$0–$21,600	29	$0–$21,600	29	$0–$25,000	29
	$21,601–$52,000	30	$21,601–$58,000	30	$21,601–$63,000	30	$25,001–$75,000	30
	$52,001–$62,500	42	$58,001–$70,000	42	$63,001–$95,000	42	$75,001–$150,000	40
	> $62,500	47	> $70,000	47	> $95,000	47	> $150,000	45
Medicare levy	$0–$15,529	Nil	$0–$15,902	Nil	$0–$16,284	Nil	$0–$16,284	Nil
for singles(b)	$15,530–$16,788	20% of > $15,529	$15,903–$17,191	20% of > $15,902	$16,285-$17,604	20% of > $16,284	$16,285-$19,157	10% of > $16,284
	> $16,788	1.5	> $17,191	1.5	> $17,604	1.5	> $19,157	1.5
		Amount		**Amount**		**Amount**		**Amount**
Low Income	$0-$21,600	$235	$0-$21,600	$235	$0-$21,600	$235	$0-$25,000	$600
Tax Offset	$21,601-$27,475	less 4% of > $21,600	$21,601-$27,475	less 4% of > $21,600	$21,601-$27,475	less 4% of > $21,600	$25,001-$40,000	less 4% of > $25,000
	> $27,475	Nil	> $27,475	Nil	> $27,475	Nil	> $40,000	Nil

(a) These standard income tax rates can be offset by a range of concessional arrangements, including the senior Australians tax offset, the spouse tax offset, the low income tax offset and the mature age worker tax offset.
(b) These standard Medicare levy rates apply to singles. Different concessional and penalty rates apply in certain circumstances.

Fringe benefits tax

Fringe benefits tax is paid on non-salary benefits provided by employers to employees which are provided in place of, or in addition to, the salary and wages of employees.

The tax is payable by employers and is assessed on the value of the fringe benefits provided to employees or their associates. From 1 April 2006, fringe benefits tax will be levied at 46.5 per cent of the grossed-up taxable value of benefits, as calculated under the fringe benefits tax rules.

Following a reclassification in Government Finance Statistics reporting standards, fringe benefits tax now includes revenue collected from employees of Australian Government agencies.

Taxation on superannuation funds

These taxes cover all income taxes generally paid by superannuation funds on behalf of their members on their contributions and earnings. A schedule of the superannuation funds tax rates for the period covered in this budget is provided in Table C2.

Table C2: Superannuation funds tax rates

	From 1/7/2004 Per cent	From 1/7/2005 Per cent	From 1/7/2006 Per cent
Superannuation funds			
Complying funds	15	15	15
Non-complying funds	47	47	45(a)
Superannuation surcharge			
Surcharge rate	12.5	0	0
Lower surcharge threshold	$99,710	-	-
Upper surcharge threshold	$121,075	-	-

(a) See measure description for personal tax cuts (consequential changes) in Budget Paper No. 2, *Budget Measures 2006-07*.

Superannuation funds taxation

Like companies, superannuation funds are taxed through the PAYG instalment system, but generally at a concessional rate of 15 per cent in relation to taxable contributions received, capital gains and investment income. Only two-thirds of a capital gain is included in assessable income if the asset is held for at least 12 months.

Superannuation surcharge

The surcharge is levied on the surchargeable contributions of a superannuation fund member whose adjusted taxable income exceeds the superannuation surcharge lower income threshold in a financial year.

Surchargeable contributions include employer contributions, certain rolled-over 'golden handshakes' and tax deductible personal contributions made to superannuation funds. A termination payment surcharge applies to certain 'golden handshakes' retained as cash.

The surcharge was abolished with effect from 1 July 2005. It does not apply for the 2005-06 and later financial years. However, assessments of surcharge and amended assessments continue to be issued in respect of the 2004-05 and earlier financial years. Interest will still accrue on any surcharge debt an individual has incurred.

Company and other related income taxation

These revenue heads broadly cover all income taxes paid by corporate type entities. A schedule of the company income tax rates for the period covered in this budget is provided in Table C3.

Table C3: Company and other related income tax rates

	From 1/7/2004	From 1/7/2005	From 1/7/2006
	Per cent	Per cent	Per cent
Company tax	30	30	30
Petroleum resource rent tax	40	40	40

Company income taxation

Company income taxation includes all income taxes paid by companies, including incorporated and unincorporated associations, limited partnerships and some public unit trusts.

Generally, every resident company that derives assessable income (including capital gains), whether sourced within or outside of Australia, and every non-resident company that derives assessable income from Australian sources, is required to pay company tax.

Company income taxation has been collected through the PAYG instalment system since the financial year beginning 1 July 2000. This system replaced the provisional tax and company tax instalment systems. Under the PAYG instalment system, most company taxpayers now pay their liability through four quarterly instalment payments and a balancing payment five months after the final instalment, although some small companies are able to make an annual payment.

Petroleum resource rent tax

Petroleum resource rent tax is levied at a rate of 40 per cent on economic profits in respect of offshore petroleum projects other than some of the North-West Shelf production and associated exploration areas, which are subject to excise (included in excise on petroleum and other fuel products) and royalties. The amount paid is deductible from a company's total profit when determining its company tax liability.

Excise and customs duty

Excise duty

The major categories of excisable products are petroleum and other fuel products, crude oil, oils and lubricants, tobacco and alcoholic beverages. Equivalent duties on identical imported products are imposed through, and reported under, customs duty.

Petroleum and other fuel excise includes excise on petrol, diesel fuel, biodiesel, aviation gasoline, aviation kerosene, fuel ethanol, fuel oil, heating oil and kerosene. It is imposed at specific rates per litre of product.

- Petrol includes unleaded petrol and lead replacement petrol (which replaced leaded petrol but is taxed at the unleaded petrol rate).

- All revenue from excise duty on aviation gasoline and aviation kerosene contributes to the funding of aviation activities undertaken by the Civil Aviation Safety Authority. The rates of excise applying to aviation fuels are adjusted, as necessary, depending on the funding requirements of those activities.

Crude oil excise provides a return to the community for the exploitation of its natural resources. The crude oil excise regime applies to:

- production from offshore fields in the North-West Shelf production licence areas that are not subject to petroleum resource rent tax; and

- production from onshore fields and fields in coastal waters.

The rate of excise varies according to the quantity of crude oil sold, the sale price of the crude oil, and the dates of discovery and development of the oil field.

Other excise is derived from beer, spirits, other alcoholic beverages (other than wine) and tobacco products.

- For beer, spirits and other alcoholic beverages, excise is imposed on the alcohol content. The excise rate on beer in containers greater than 48 litres (draught beer) is lower than for other beer.

- Excise is imposed on a *per stick* basis for cigarettes that do not exceed 0.8 grams (actual tobacco content) and on a *per kilogram* basis for other tobacco products.

Wine is not subject to excise, but is subject to the wine equalisation tax.

Excise indexation

The excise rates for petroleum products and oils and lubricants are no longer indexed. Excise indexation for petroleum products was removed in March 2001.

The rates of duty for other excisable products are adjusted every August and February in line with half yearly CPI movements (Table C4). If the change in the CPI is negative, the excise rate is not reduced. Instead the decline is carried forward to be set off against the next positive CPI movement.

Table C4: Excise rates

Commodity	Rates applying from 2 Aug 2004 $	Rates applying from 1 Feb 2005 $	Rates applying from 1 Aug 2005 $	Rates applying from 1 Feb 2006 $
Petroleum and other fuel products (per litre)				
Unleaded petrol	0.38143	0.38143	0.38143	0.38143
Ultra low sulphur diesel	0.38143	0.38143	0.38143	0.38143
Other diesel	0.40143	0.40143	0.40143	0.40143
Aviation gasoline(a)	0.03114	0.03114	0.03114	0.02854
Aviation kerosene(a)	0.03151	0.03151	0.03151	0.02854
Fuel oil(b)	0.07557	0.07557	0.07557	0.07557
Heating oil and kerosene (for burner use)(b)	0.07557	0.07557	0.07557	0.07557
Fuel ethanol	0.38143	0.38143	0.38143	0.38143
Biodiesel	0.38143	0.38143	0.38143	0.38143
Greases (per kilogram)	0.05449	0.05449	0.05449	0.05449
Oils and lubricants, excluding greases (per litre)	0.05449	0.05449	0.05449	0.05449
Beer (per litre of alcohol over 1.15 per cent)				
Draught beer, low strength	6.09	6.16	6.24	6.33
Draught beer, mid strength	19.12	19.35	19.60	19.89
Draught beer, high strength	25.02	25.32	25.65	26.03
Other beer, low strength	30.49	30.86	31.26	31.73
Other beer, mid strength	35.53	35.96	36.43	36.98
Other beer, high strength	35.53	35.96	36.43	36.98
Other beverages, not exceeding 10 per cent alcohol content	35.53	35.96	36.43	36.98
Potable spirits (per litre of alcohol)				
Brandy	56.21	56.88	57.62	58.48
Fruit brandy, whisky, rum and liqueurs	60.20	60.92	61.71	62.64
Other spirits, exceeding 10 per cent alcohol content	60.20	60.92	61.71	62.64
Cigarettes, cigars and tobacco (tobacco content of 0.8 grams or less per stick)	0.22353	0.22621	0.22915	0.23259
Tobacco products (per kilogram)	279.41	282.76	286.44	290.74

(a) Aviation fuel rates were reduced to $0.02854 per litre with effect from 1 November 2005.
(b) Excise rates for these fuels will increase to $0.38143 on 1 July 2006.

Customs duty

Customs duty is imposed as a percentage of the value of the imported good and/or on a volumetric basis (where duty is applied per unit of quantity) for excise equivalent products. In general, other dutiable goods attract a general tariff rate of 5 per cent.

Tariffs on passenger motor vehicles and textile, clothing and footwear account for around one-third of the total duty collected. Approximately 40 per cent of customs duty revenue is derived from duty imposed on imports of petroleum products, tobacco, beer and spirits, which is akin to excise duty on these items.

Table C5: Tariff rates

	Applying before 1 January 2005 Per cent	Applying from 1 January 2005 Per cent	Applying from 11 May 2005 Per cent
General tariff	5	5	5
Passenger motor vehicles	15	10	10
Textiles clothing and footwear			
Clothing and finished textiles	25	17.5	17.5
Cotton sheeting, fabric, carpet and footwear	15	10	10
Sleeping bags, table linen and footwear parts	10	7.5	7.5
Tariff concession order			
Consumer goods	0	0	0
Other (business inputs)	3	3	0

Other taxation

Wine equalisation tax

All wines, meads, perries, ciders and sakes are subject to a wine equalisation tax (WET) of 29 per cent on the wholesale value of the goods. The tax was introduced as part of *The New Tax System* to offset the removal of the previous wholesale sales tax on wine and the application of the goods and services tax. The WET was set at a rate to ensure that the price of cask wine need only increase by the estimated general price rise.

Unlike alcohol excises, the wine equalisation tax is an *ad valorem* tax. It is calculated at a rate of 29 per cent of the final wholesale price or, in certain other permitted circumstances, of a nominal wholesale value calculated as 50 per cent of the retail price, or alternatively at the average wholesale price for identical wine.

From 1 October 2004, a rebate has been payable on the first $290,000 in wine equalisation tax paid annually by any producer or producer group. This rebate will increase to $500,000 from 1 July 2006.

Luxury car tax

The luxury car tax was introduced as part of *The New Tax System* to maintain a tax differentiation between luxury vehicles and other vehicles sold in Australia.

The luxury car tax applies at a rate of 25 per cent for every dollar over the luxury car threshold. The current luxury car threshold is $57,009. The threshold is indexed annually using the motor vehicle purchase component of the CPI, which is composed of observed price movements for new vehicles sold in Australia.

Agricultural levies

Agricultural levies and charges are used to fund industry activities, such as research and development, marketing and promotion, residue testing, and animal health programmes.

The need for a levy is usually identified by the industry itself and the levy is generally collected at the first point of sale of the primary produce or point of further processing.

All levies and charges are paid into the Consolidated Revenue Fund without deduction and then disbursed to fund the relevant programme.

Other taxes

The major contributors to this category are the passenger movement charge and import processing and depot charges administered by the Australian Customs Service.

Other contributors include broadcasting licence fees, which are payable by all commercial radio and television licensees and are calculated as a percentage of licensees' gross earning for the previous year. Other taxes also include the Superannuation Guarantee Charge and the Universal Service Obligation levy.

Non-taxation revenue

Sales of goods and services

This category consists of revenue from the direct provision of goods and services by the Australian Government general government sector, including reimbursement of GST administration costs received from the states.

Dividends

The main sources of dividends are the Australian Government's business enterprises, the Reserve Bank of Australia (RBA) and the Future Fund. Dividend payments from the RBA can be volatile, as they are sensitive to movements in interest rates and the exchange rate.

Interest

Interest from other governments

This category mainly consists of revenue from the States for interest on General Purpose and Specific Purpose borrowings.

The Australian Government receives interest payments from the States in respect of General Purpose borrowings made on behalf of the States under the State Governments' Loan Council Programme (and from the Northern Territory in respect of advances made under similar General Purpose capital assistance arrangements). Payments relating to these advances are made, in turn, by the Australian Government to bond holders.

Interest from the States on General Purpose borrowings is declining as a result of the June 1990 Loan Council decision that the States and Territories make additional payments to the Australian Government each year to facilitate the redemption of all maturing Australian Government securities issued on their behalf. The reduction in interest revenue from the States is matched by a reduction in public debt interest expenses.

The Australian Government also receives interest on Specific Purpose borrowings to the States, including on advances made under the Commonwealth-State Housing Agreements, States (Works and Housing) Assistance Acts, Northern Territory Housing Advances, and by the Australian Capital Territory on debts assumed upon self-government.

Interest from other sources

This item includes interest income on Australian Government cash balances and on other financial assets including assets held by the Future Fund. It excludes swap transactions entered into as part of the Australian Government's debt management strategy, as they are reported separately in the Statement of Other Economic Flows under Government Finance Statistics standards. The Australian Office of Financial Management is responsible for the management and reporting of the Australian Government's net debt portfolio.

Other sources of non-taxation revenue

Other non-taxation revenue includes petroleum royalties paid by producers operating in the Timor Sea and the North-West Shelf oil and gas fields, Child Support Trust Revenue (collected by the Child Support Agency) and seigniorage from circulation coin production.

APPENDIX D: FORWARD ESTIMATES

Table D1: Australian Government general government revenue (accrual basis)

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Income taxation						
Individuals and other withholding taxes						
Gross income tax withholding	98,250	103,830	104,010	109,540	116,620	124,870
Gross other individuals	24,003	26,410	28,480	29,670	32,000	34,770
less: Refunds	13,734	15,350	16,790	18,690	19,970	21,260
Total individuals and other withholding taxation	108,519	114,890	115,700	120,520	128,650	138,380
Fringe benefits tax(a)	3,476	3,660	3,720	3,810	3,920	4,050
Superannuation funds						
Contributions and earnings	5,083	5,390	5,890	6,400	6,950	7,560
Superannuation surcharge	1,326	1,030	680	110	40	30
Total superannuation taxation	6,410	6,420	6,570	6,510	6,990	7,590
Company tax	43,106	50,480	56,860	59,400	59,950	61,800
Petroleum resource rent tax	1,465	1,970	2,490	3,250	3,740	4,000
Income taxation revenue	**162,975**	**177,420**	**185,340**	**193,490**	**203,250**	**215,820**
Excise and customs						
Excise duty						
Petrol	7,371	7,280	7,310	7,400	7,490	7,590
Diesel	6,164	6,240	6,420	6,650	6,860	7,080
Other fuel products	147	220	450	470	520	510
Crude oil	668	330	470	310	200	120
Beer	1,653	1,730	1,760	1,790	1,820	1,850
Potable spirits	741	810	890	970	1,070	1,180
Tobacco	5,237	5,290	5,320	5,340	5,360	5,380
Total excise duty revenue	21,981	21,900	22,620	22,930	23,320	23,710
Customs duty						
Textiles, clothing and footwear	966	830	870	930	990	760
Passenger motor vehicles	1,397	1,258	1,300	1,370	1,440	1,190
Excise-like goods	1,697	1,810	2,160	2,290	2,410	2,550
Other imports	1,793	1,603	1,608	1,718	1,839	1,958
less: Refunds and drawbacks	306	330	300	300	300	300
Total customs duty revenue	5,548	5,171	5,638	6,008	6,379	6,158
Excise and customs revenue	**27,529**	**27,071**	**28,258**	**28,938**	**29,699**	**29,868**
Other taxation						
Wine equalisation tax	693	660	660	670	690	710
Luxury car tax	302	320	320	340	360	380
Agricultural levies	584	607	619	614	605	424
Other taxes	2,068	2,007	1,960	2,024	2,137	2,249
Other taxation revenue	**3,647**	**3,594**	**3,559**	**3,648**	**3,792**	**3,763**
Taxation revenue	**194,150**	**208,085**	**217,157**	**226,076**	**236,741**	**249,452**
Non-taxation						
Sales of goods and services	4,388	4,898	4,846	4,975	5,114	5,255
Dividends	3,176	4,321	2,701	2,866	3,058	3,228
Interest received	1,621	2,386	3,717	3,457	4,005	4,647
Other non-taxation revenue	3,271	3,173	3,241	3,297	3,160	3,021
Non-taxation revenue	**12,455**	**14,779**	**14,505**	**14,595**	**15,338**	**16,151**
Total revenue	**206,605**	**222,864**	**231,662**	**240,671**	**252,078**	**265,603**

(a) See fringe benefits tax description in Appendix C.

Table D2: Australian Government general government receipts (cash basis)

	Actual	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Income taxation						
Individuals and other withholding taxes						
Gross income tax withholding	97,304	103,230	103,420	108,900	115,940	124,150
Gross other individuals	22,554	24,930	26,810	27,940	30,180	32,840
less: Refunds	13,734	15,350	16,790	18,690	19,970	21,260
Total individuals and other withholding taxation	106,123	112,810	113,440	118,150	126,150	135,730
Fringe benefits tax(a)	3,703	3,830	3,690	3,780	3,890	4,020
Superannuation funds						
Contributions and earnings	5,014	5,350	5,840	6,350	6,890	7,500
Superannuation surcharge	1,233	920	650	100	40	40
Total superannuation taxation	6,248	6,270	6,490	6,450	6,930	7,540
Company tax	40,404	49,800	56,130	58,620	59,170	61,010
Petroleum resource rent tax	1,459	1,970	2,490	3,250	3,740	4,000
Income taxation receipts	**157,937**	**174,680**	**182,240**	**190,250**	**199,880**	**212,300**
Excise and customs						
Excise duty						
Petrol	7,330	7,280	7,310	7,400	7,490	7,590
Diesel	6,131	6,240	6,420	6,650	6,860	7,080
Other fuel products	147	220	450	470	520	510
Crude oil	668	330	470	310	200	120
Beer	1,653	1,730	1,760	1,790	1,820	1,850
Potable spirits	739	810	890	970	1,070	1,180
Tobacco	5,220	5,290	5,320	5,340	5,360	5,380
Total excise duty receipts	21,888	21,900	22,620	22,930	23,320	23,710
Customs duty						
Textiles, clothing and footwear	966	830	870	930	990	760
Passenger motor vehicles	866	650	700	770	840	630
Excise-like goods	1,697	1,810	2,160	2,290	2,410	2,550
Other imports	1,789	1,590	1,600	1,710	1,830	1,950
less: Refunds and drawbacks	306	330	300	300	300	300
Total customs duty receipts	5,012	4,550	5,030	5,400	5,770	5,590
Excise and customs receipts	**26,900**	**26,450**	**27,650**	**28,330**	**29,090**	**29,300**
Other taxation						
Wine equalisation tax	682	660	660	670	690	710
Luxury car tax	298	320	320	340	360	380
Agricultural levies	584	607	619	614	605	424
Other taxes	1,775	1,752	1,700	1,770	1,851	1,943
Other taxation receipts	**3,339**	**3,339**	**3,298**	**3,394**	**3,507**	**3,456**
Taxation receipts	**188,176**	**204,469**	**213,188**	**221,974**	**232,477**	**245,056**
Non-taxation						
Sales of goods and services	4,373	5,189	5,008	5,137	5,297	5,427
Dividends	3,838	4,341	3,000	2,866	3,058	3,228
Interest received	1,400	2,275	3,498	3,316	3,787	4,379
Other non-taxation receipts	6,174	6,125	6,124	6,224	6,044	5,904
Non-taxation receipts	**15,784**	**17,930**	**17,631**	**17,543**	**18,186**	**18,937**
Total receipts	**203,960**	**222,400**	**230,819**	**239,517**	**250,663**	**263,994**

(a) See fringe benefits tax description in Appendix C.

APPENDIX E: CHANGES SINCE MYEFO

Table E1: Reconciliation of 2005-06 general government revenue (accrual basis)

	Estimates		Change on MYEFO	
	MYEFO $m	Budget $m	$m	%
Income taxation				
Individuals and other withholding				
Gross income tax withholding	102,030	103,830	1,800	1.8
Gross other individuals	25,110	26,410	1,300	5.2
less : Refunds	15,000	15,350	350	2.3
Total individuals and other withholding taxation	112,140	114,890	2,750	2.5
Fringe benefits tax(a)	3,470	3,660	190	5.5
Superannuation funds				
Contributions and earnings	5,280	5,390	110	2.1
Superannuation surcharge	1,410	1,030	-380	-27.0
Total superannuation funds	6,690	6,420	-270	-4.0
Company tax	48,740	50,480	1,740	3.6
Petroleum resources rent tax	2,130	1,970	-160	-7.5
Income taxation revenue	**173,170**	**177,420**	**4,250**	**2.5**
Excise and customs				
Excise duty				
Petrol	7,210	7,280	70	1.0
Diesel	6,260	6,240	-20	-0.3
Other fuel products	170	220	50	29.4
Crude oil	480	330	-150	-31.3
Beer	1,690	1,730	40	2.4
Potable spirits	790	810	20	2.5
Tobacco	5,300	5,290	-10	-0.2
Total excise duty	21,900	21,900	0	0.0
Customs duty				
Textiles, clothing and footwear	790	830	40	5.1
Passenger motor vehicles	1,350	1,258	-92	-6.8
Excise-like goods	1,700	1,810	110	6.5
Other imports	1,522	1,603	81	5.3
less : Refunds and drawbacks	300	330	30	10.0
Total customs duty	5,062	5,171	109	2.2
Excise and customs revenue	**26,962**	**27,071**	**109**	**0.4**
Other taxation				
Wine equalisation tax	660	660	0	0.0
Luxury car tax	310	320	10	3.2
Agricultural levies	599	607	8	1.4
Other taxes	2,077	2,007	-70	-3.4
Other taxation revenue	**3,646**	**3,594**	**-52**	**-1.4**
Taxation revenue	**203,777**	**208,085**	**4,308**	**2.1**
Non-taxation				
Sales of goods and services	4,900	4,898	-2	0.0
Dividends	4,318	4,321	4	0.1
Interest received	2,319	2,386	67	2.9
Other non-taxation revenue	3,307	3,173	-134	-4.1
Non-taxation revenue	**14,845**	**14,779**	**-66**	**-0.4**
Total revenue	**218,622**	**222,864**	**4,242**	**1.9**

(a) See fringe benefits tax description in Appendix C.

Table E2: Reconciliation of 2006-07 general government revenue (accrual basis)

	Estimates		Change on MYEFO	
	MYEFO $m	Budget $m	$m	%
Income taxation				
Individuals and other withholding				
Gross income tax withholding	107,720	104,010	-3,710	-3.4
Gross other individuals	25,850	28,480	2,630	10.2
less: Refunds	15,960	16,790	830	5.2
Total individuals and other withholding taxation	117,610	115,700	-1,910	-1.6
Fringe benefits tax(a)	3,540	3,720	180	5.1
Superannuation funds				
Contributions and earnings	5,620	5,890	270	4.8
Superannuation surcharge	410	680	270	65.9
Total superannuation funds	6,030	6,570	540	9.0
Company tax	52,210	56,860	4,650	8.9
Petroleum resources rent tax	2,270	2,490	220	9.7
Income taxation revenue	**181,660**	**185,340**	**3,680**	**2.0**
Excise and customs				
Excise duty				
Petrol	7,280	7,310	30	0.4
Diesel	6,500	6,420	-80	-1.2
Other fuel products	150	450	300	200.0
Crude oil	440	470	30	6.8
Beer	1,710	1,760	50	2.9
Potable spirits	850	890	40	4.7
Tobacco	5,390	5,320	-70	-1.3
Total excise duty	22,320	22,620	300	1.3
Customs duty				
Textiles, clothing and footwear	840	870	30	3.6
Passenger motor vehicles	1,252	1,300	48	3.8
Excise-like goods	1,710	2,160	450	26.3
Other imports	1,658	1,608	-50	-3.0
less : Refunds and drawbacks	300	300	0	0.0
Total customs duty	5,160	5,638	478	9.3
Excise and customs revenue	**27,480**	**28,258**	**778**	**2.8**
Indirect taxation				
Wine equalisation tax	730	660	-70	-9.6
Luxury car tax	340	320	-20	-5.9
Agricultural levies	608	619	11	1.8
Other taxes	2,088	1,960	-128	-6.1
Other taxation revenue	**3,766**	**3,559**	**-207**	**-5.5**
Taxation revenue	**212,906**	**217,157**	**4,251**	**2.0**
Non-taxation				
Sales of goods and services	4,855	4,846	-9	-0.2
Dividends	2,464	2,701	237	9.6
Interest received	3,858	3,717	-141	-3.7
Other non-taxation revenue	3,350	3,241	-109	-3.2
Non-taxation revenue	**14,527**	**14,505**	**-22**	**-0.1**
Total revenue	**227,434**	**231,662**	**4,228**	**1.9**

(a) See fringe benefits tax description in Appendix C.

Table E3: Reconciliation of 2005-06 general government receipts (cash basis)

	MYEFO	Budget	Change on MYEFO	
	$m	$m	$m	%
Income taxation				
Individuals and other withholding taxes				
Gross income tax withholding	101,430	103,230	1,800	1.8
Gross other individuals	24,060	24,930	870	3.6
less: Refunds	15,000	15,350	350	2.3
Total individuals and other withholding taxation	110,490	112,810	2,320	2.1
Fringe benefits tax(a)	3,440	3,830	390	11.3
Superannuation funds				
Contributions and earnings	5,300	5,350	50	0.9
Superannuation surcharge	1,300	920	-380	-29.2
Total superannuation taxation	6,600	6,270	-330	-5.0
Company tax	48,210	49,800	1,590	3.3
Petroleum resource rent tax	2,130	1,970	-160	-7.5
Income taxation receipts	**170,870**	**174,680**	**3,810**	**2.2**
Excise and customs				
Excise duty				
Petrol	7,210	7,280	70	1.0
Diesel	6,260	6,240	-20	-0.3
Other fuel products	170	220	50	29.4
Crude oil	480	330	-150	-31.3
Beer	1,690	1,730	40	2.4
Potable spirits	790	810	20	2.5
Tobacco	5,300	5,290	-10	-0.2
Total excise duty receipts	21,900	21,900	0	0.0
Customs duty				
Textiles, clothing and footwear	790	830	40	5.1
Passenger motor vehicles	740	650	-90	-12.2
Excise-like goods	1,700	1,810	110	6.5
Other imports	1,519	1,590	71	4.7
less: Refunds and drawbacks	300	330	30	10.0
Total customs duty receipts	4,449	4,550	101	2.3
Excise and customs receipts	**26,349**	**26,450**	**101**	**0.4**
Other taxation				
Wine equalisation tax	660	660	0	0.0
Luxury car tax	310	320	10	3.2
Agricultural levies	599	607	8	1.4
Other taxes	1,756	1,752	-4	-0.2
Other taxation receipts	**3,325**	**3,339**	**14**	**0.4**
Taxation receipts	**200,544**	**204,469**	**3,925**	**2.0**
Non-taxation				
Sales of goods and services	5,144	5,189	45	0.9
Dividends	4,318	4,341	24	0.5
Interest received	2,170	2,275	104	4.8
Other non-taxation receipts	6,333	6,125	-208	-3.3
Non-taxation receipts	**17,965**	**17,930**	**-35**	**-0.2**
Total receipts	**218,509**	**222,400**	**3,890**	**1.8**

(a) See fringe benefits tax description in Appendix C.

Table E4: Reconciliation of 2006-07 general government receipts (cash basis)

	MYEFO	Budget	Change on MYEFO	
	$m	$m	$m	%
Income taxation				
Individuals and other withholding taxes				
Gross income tax withholding	107,090	103,420	-3,670	-3.4
Gross other individuals	24,830	26,810	1,980	8.0
less: Refunds	15,960	16,790	830	5.2
Total individuals and other withholding taxation	115,960	113,440	-2,520	-2.2
Fringe benefits tax(a)	3,560	3,690	130	3.7
Superannuation funds				
Contributions and earnings	5,600	5,840	240	4.3
Superannuation surcharge	380	650	270	71.1
Total superannuation taxation	5,980	6,490	510	8.5
Company tax	51,300	56,130	4,830	9.4
Petroleum resource rent tax	2,270	2,490	220	9.7
Income taxation receipts	179,070	182,240	3,170	1.8
Excise and customs				
Excise duty				
Petrol	7,280	7,310	30	0.4
Diesel	6,500	6,420	-80	-1.2
Other fuel products	150	450	300	200.0
Crude oil	440	470	30	6.8
Beer	1,710	1,760	50	2.9
Potable spirits	850	890	40	4.7
Tobacco	5,390	5,320	-70	-1.3
Total excise duty receipts	22,320	22,620	300	1.3
Customs duty				
Textiles, clothing and footwear	840	870	30	3.6
Passenger motor vehicles	650	700	50	7.7
Excise-like goods	1,710	2,160	450	26.3
Other imports	1,656	1,600	-56	-3.4
less: Refunds and drawbacks	300	300	0	0.0
Total customs duty receipts	4,556	5,030	474	10.4
Excise and customs receipts	**26,876**	**27,650**	**774**	**2.9**
Other taxation				
Wine equalisation tax	730	660	-70	-9.6
Luxury car tax	340	320	-20	-5.9
Agricultural levies	608	619	11	1.8
Other taxes	1,733	1,700	-33	-1.9
Other taxation receipts	**3,411**	**3,298**	**-112**	**-3.3**
Taxation receipts	**209,357**	**213,188**	**3,832**	**1.8**
Non-taxation				
Sales of goods and services	5,032	5,008	-24	-0.5
Dividends	2,763	3,000	237	8.6
Interest received	3,522	3,498	-25	-0.7
Other non-taxation receipts	6,347	6,124	-222	-3.5
Non-taxation receipts	**17,665**	**17,631**	**-34**	**-0.2**
Total receipts	**227,022**	**230,819**	**3,798**	**1.7**

(a) See fringe benefits tax description in Appendix C.

APPENDIX F: TAXATION REVENUE RECOGNITION

There are different methods of accounting for taxation revenue. Each method of revenue recognition results in estimates and outcomes which may be significantly different to those produced using other methods.

Accrual accounting was introduced by the Australian Government for the 1999-2000 Budget. Prior to then, all estimates and outcomes were reported on a cash basis, but cash recognition still plays a role in budgeting and outcomes reporting — both accrual and cash taxation revenue estimates and outcomes are reported in the budget papers. Furthermore, there are also different methods for recognising accrual revenue.

This appendix provides an explanation of the different revenue recognition methods which apply to the various taxation revenue heads.

Revenue recognition methods

Cash revenue recognition

Under cash recognition, taxation revenue is accounted for at the time a taxation payment is received by the relevant authority. The receipt may be a different amount than the taxation liability and result in a subsequent amended (refund or debit) assessment. The payment may also be received in a different period from which the taxation liability relates.

Cash recognition remains a useful method under accrual accounting because of its use in the cash flow statement and to provide additional information about the structure of taxation revenues. Cash data is also available over a much longer period — accrual data is only available since 1999-2000 — and is therefore often used for time series analysis.

Accrual revenue recognition

The AAS and GFS standards for accrual accounting (refer to Appendix A in Statement 2 for an explanation of these reporting standards) require that taxation revenue be recognised in the reporting period in which the taxpayer earns the income that is subsequently subject to taxation — this is known as the Economic Transactions Method (ETM). However, the standards also permit government reporting using an alternative approach when there is an inability to reliably measure taxation revenues using the ETM approach.

ETM revenue is not a reliable measure for several significant revenue heads — individuals and other withholding taxation, company income taxation and superannuation taxation. As these revenue heads account for the majority of total revenue, accrual taxation revenue has always been recognised using the Tax Liability Method (TLM) rather than ETM.

Under TLM, taxation revenue is accounted for at the time a taxpayer makes a self assessment or when an assessment of a taxation liability is raised by the relevant authority. This method retains some elements of cash revenue recognition — for example, revenue is recognised when cash payment occurs prior to an assessment being raised.

For the major income taxation revenue heads, the point of recognition under ETM and TLM can sometimes be in different periods — for example, a taxation return lodged in October 2005 for the 2004-05 income year, and which results in a new taxation liability or a refund, would be recognised in the 2004-05 income year under ETM and in 2005-06 for TLM. In this case, ETM requires that outcomes for 2004-05 include an estimation of liabilities likely to be identified in subsequent periods. TLM outcomes do not incorporate this estimation, as only identified taxation liabilities are reported. Consequently, aggregate TLM revenue outcomes are usually known with relative certainty, although there can be estimation issues involved in allocating aggregate revenue between different heads of revenue.

In addition, AAS and GFS treat prior period adjustments to ETM revenue outcomes differently. GFS requires that a time series of outcomes is maintained, such that prior year outcomes are continually adjusted as new information comes to light. In contrast, AAS requires that prior period adjustments are not back-cast, and instead are reflected in the current period results. This difference in treatment reflects the different purpose in each of the standards:

- GFS ETM data may be more accurate over the long term, and may therefore be better for economic analysis, but has the disadvantage of constantly being revised; whereas

- AAS ETM outcomes are finalised at the end of each financial year, and this greater level of certainty may be better for budgeting and reporting.

Implementation of accrual revenue recognition

For the years 1999-2000 to 2005-06, all accrual taxation revenue has been recognised on a TLM basis. Commencing with the 2006-07 Budget, ETM revenue recognition has been adopted for all revenue heads where the measurement issues are not material. This generally occurs where the economic activity, the identification of the liability and the receipt of the payment all occur with little or no lag — and consequently, the ETM and TLM (and cash) recognition methods produce consistent results.

TLM revenue recognition will continue to be used if ETM measurement issues may be material. At present, this is limited to individuals and other withholding taxation, company income taxation and superannuation taxation, but this will be reviewed periodically. ETM estimates and outcomes are inherently more volatile for these revenue heads, mainly because they incorporate the estimation of significant levels of liabilities likely to be recognised in future periods. This additional level of estimation would increase the likelihood of differences between the revenue estimates and outcomes, with consequential impacts on the budget balances. This greater level of uncertainty would make the implementation of fiscal policy more problematic than if these revenue heads continue to be recognised using TLM.

Differences between the accrual and cash taxation revenue estimates

Table F1: Estimates of taxation revenue on an accrual and cash basis

	2005-06	2006-07	2007-08	2008-09	2009-10
	$b	$b	$b	$b	$b
Tax revenue (accrual)	208.1	217.2	226.1	236.7	249.5
Tax receipts (cash)	204.5	213.2	222.0	232.5	245.1
Difference (accrual less cash)	**3.6**	**4.0**	**4.1**	**4.3**	**4.4**
Memorandum items:					
Deferred company tax payments	-0.4	0.0	0.0	0.0	0.0
ACIS(a)	0.6	0.6	0.6	0.6	0.6
Other	3.4	3.4	3.5	3.7	3.8
Total	3.6	4.0	4.1	4.3	4.4

(a) Automotive Competitiveness and Investment Scheme.

Automotive Competitiveness and Investment Scheme

The Automotive Competitiveness and Investment Scheme (ACIS) operates by providing customs duty credits to exporters of Australian automotive products. The credits can be offset against future customs duty on specific imports.

Under accrual accounting, an expense is recognised when the ACIS credits are issued. The later redemption of the credits results in an increase in the difference between the accrual and cash estimates for customs duty revenue, because the customs duty accrual revenue is recognised at the point of credit redemption but no cash is received. ACIS credits account for $600 million of the difference between the accrual and cash estimates in 2006-07.

Deferred company tax payments

The PAYG arrangements for companies and superannuation funds (introduced as part of *The New Tax System*) better align tax payments with the period in which income is earned. In the absence of transitional arrangements, this would have created an overlap of tax payments, because payments of tax obligations for 1999-2000 (under the previous payment arrangements) and PAYG instalments for 2000-01 (under the new payment arrangements) both occurred during 2000-01. For a medium-sized company, for example, there would have been six payments due, instead of the usual four.

The Government implemented transitional arrangements to assist these taxpayers move to the new PAYG system, by allowing them to spread some of their tax payments in interest free instalments for up to five years. While the full amount of the tax obligations was included in accrual revenue for 2000-01 (the year in which the liabilities were recognised), the cash estimates will continue to be affected for the five year period.

While the impact of these deferred payments has been to increase the cash taxation receipts estimates by around $355 million in 2005-06, it has no impact of the accrual estimate in that year.

Other

This category consists of other timing differences between the recognition of accrual and cash revenue and instances where revenue has been recognised but payment is no longer expected to be received. For example:

- *receivables* arise where taxation liabilities are recognised in one period, but the taxpayer is not expected to pay the liability until a later period;
- *remissions* occur where taxation liabilities are recognised, but circumstances are taken into account and the Commissioner of Taxation reduces the amount of various penalties and interest required to be paid;
- a taxation liability may be *written-off* where the previously recognised revenue is no longer expected to be received; and
- a *credit amendment* may be issued where a taxation assessment is amended (for example, where a court decision leads to a change in the interpretation of the taxation laws).

To the extent that revenue includes taxation assessments for which payment may not be received, expenses are recognised (that is, in respect of *remissions* and *write-offs* of bad and doubtful debts). The higher revenue is offset by these expenses, leaving the fiscal balance unaffected.

APPENDIX G: TAX EXPENDITURES

This appendix contains an overview of the cost of tax expenditures provided to taxpayers through the tax system.

Tax expenditures provide a benefit to a specified activity or class of taxpayer. They can be delivered as a tax exemption, tax deduction, tax offset, reduced tax rate or deferral of a tax liability. The Government can use tax expenditures to allocate resources to different activities or taxpayers in much the same way that it can use direct expenditure programmes. For this reason, and noting their direct impact on the fiscal balance, these concessions are generally called tax expenditures.

The data reported in this appendix is consistent with tax expenditure data reported in the *2005 Tax Expenditures Statement* published in December 2005. Several considerations need to be taken into account when analysing tax expenditure data (see section 2.1 of the *2005 Tax Expenditures Statement* for a detailed description).

Table G1 contains estimates of total tax expenditures for the period 2002-03 to 2009-10.

Table G1: Aggregate tax expenditures

Year	Superannuation $m	Other tax expenditures $m	Net value of tax expenditures $m	Tax expenditures as a proportion of GDP %
2002-03 (est)	10,395	19,268	29,663	3.8
2003-04 (est)	14,000	19,854	33,854	4.0
2004-05 (est)	14,405	22,454	36,859	4.1
2005-06 (proj)	15,890	23,117	39,007	4.1
2006-07 (proj)	16,585	24,340	40,925	4.1
2007-08 (proj)	18,005	25,008	43,013	4.1
2008-09 (proj)	19,285	26,119	45,404	4.1
2009-10 (prelim)	20,621	26,980	47,601	4.1

Table G1 shows that measured tax expenditures as a proportion of GDP are projected to be steady at around 4.1 per cent between 2004-05 and 2009-10.

Table G2 is a list of the major tax expenditures in 2005-06.

Table G2: Major tax expenditures 2005-06

	$m
Large positive tax expenditures	
Concessional taxation of funded superannuation	15,520
Capital gains tax discount for individuals and trusts	4,390
Exemption of Family Tax Benefit Parts A and B, including expense equivalent	2,470
Senior Australians' Tax Offset	1,840
Tax offset for recipients of certain social security benefits, pensions or allowances	1,330
Application of statutory formula to value car benefits	1,140
Exemption of certain income support benefits, pensions or allowances	900
Exemption of 30 per cent private health insurance refund, including expense equivalent	890
Deduction for gifts to approved donees	800
Concessional rate of excise levied on aviation gasoline and aviation turbine fuel	780
Tax offset for low income earners	660
Exemption from excise for 'alternative fuels'	630
Large negative expenditures	
Higher rate of excise levied on cigarettes with less than 0.8 grams of tobacco	-1,355
Accelerated depreciation allowances for plant and equipment	-890

APPENDIX H: RECEIPTS HISTORY AND FORECASTS

Table H1: Australian Government receipts (cash basis)[(a)] [(b)]

	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06(est)	2006-07(est)
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Income taxation												
Individuals and other withholding												
Income tax withholding	59,970	64,521	69,366	75,170	81,055	75,009	78,983	84,134	89,638	97,304	103,230	103,420
Other individuals	10,078	11,820	12,119	13,103	13,370	13,226	16,290	17,436	19,935	22,554	24,930	26,810
less: Refunds	8,285	8,808	9,525	10,325	10,946	10,989	10,637	11,651	12,325	13,734	15,350	16,790
Total individuals and other withholding	61,763	67,533	71,959	77,948	83,478	77,246	84,636	89,919	97,247	106,123	112,810	113,440
Fringe benefits tax	3,031	3,163	3,168	3,289	3,656	3,492	3,632	3,459	3,590	3,703	3,830	3,690
Superannuation funds												
Contributions and earnings	1,634	2,595	2,746	3,630	3,243	4,110	3,550	3,865	4,502	5,014	5,350	5,840
Superannuation surcharge			347	286	577	690	824	975	1,050	1,233	920	650
Total superannuation funds	1,634	2,595	3,093	3,916	3,820	4,800	4,373	4,840	5,551	6,248	6,270	6,490
Company tax	18,252	19,173	19,406	20,734	24,453	31,582	27,230	32,752	36,101	40,404	49,800	56,130
Petroleum resource rent tax	791	1,308	907	419	1,184	2,379	1,361	1,712	1,168	1,459	1,970	2,490
Income taxation receipts	**85,470**	**93,773**	**98,534**	**106,306**	**116,592**	**119,498**	**121,233**	**132,681**	**143,657**	**157,937**	**174,680**	**182,240**
Excise and customs												
Excise duty												
Petroleum and other fuel products	10,224	10,543	10,895	10,974	11,189	11,919	12,386	12,866	13,231	13,608	13,740	14,180
Crude oil	13	9	16	31	219	526	393	417	309	668	330	470
Other excise	2,612	2,739	2,663	2,614	2,670	6,572	6,837	7,450	7,539	7,612	7,830	7,970
Total excise duty	12,849	13,291	13,574	13,619	14,078	19,017	19,616	20,733	21,079	21,888	21,900	22,620
Customs duty	3,124	3,289	3,637	3,634	3,771	4,584	4,625	4,982	5,038	5,012	4,550	5,030
Excise and customs receipts	**15,973**	**16,580**	**17,211**	**17,253**	**17,849**	**23,601**	**24,241**	**25,715**	**26,117**	**26,901**	**26,450**	**27,650**
Other taxation												
Wine equalisation tax						524	640	669	704	682	660	660
Luxury car tax						171	220	261	335	298	320	320
Agricultural levies					551	451	550	586	603	584	607	619
Other taxes	14,943	15,462	16,475	17,545	15,986	2,096	1,020	1,104	1,192	1,775	1,752	1,700
Indirect taxation receipts	**14,943**	**15,462**	**16,475**	**17,545**	**16,537**	**3,242**	**2,431**	**2,620**	**2,834**	**3,339**	**3,339**	**3,298**
Taxation receipts	**116,386**	**125,815**	**132,219**	**141,104**	**151,313**	**146,698**	**148,343**	**161,418**	**173,023**	**188,176**	**204,469**	**213,188**

Table H1: Australian Government receipts (cash basis)[a] (continued)

	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06(est)	2006-07(est)
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Non-taxation												
Interest received	1,403	1,126	1,139	682	995	1,140	918	982	1,056	1,400	2,275	3,498
Dividends and other	3,899	4,089	3,610	4,659	13,782	13,276	13,623	14,102	13,257	14,895	15,655	14,133
Non-taxation receipts	**5,302**	**5,216**	**4,749**	**5,341**	**14,777**	**14,416**	**14,541**	**15,084**	**14,313**	**15,784**	**17,930**	**17,631**
Total receipts	**121,688**	**131,031**	**136,968**	**146,444**	**166,089**	**161,114**	**162,884**	**176,503**	**187,336**	**203,960**	**222,400**	**230,819**

(a) Figures up to and including 1998-99 are based on the old Commonwealth Budget Sector cash accounting framework. Figures from 1999-2000 are on an Australian Government general government GFS basis.

(b) Taxation and non-taxation receipts in 2004-05 are different to those amounts reported in Table D2. This is because some levies that were previously classified under non-taxation receipts are now included in taxation receipts. The table also reflects the ABS's reclassification of the fringe benefits tax in GFS (see Appendix C).

Table H2: Major categories of receipts as a proportion of gross domestic product (cash basis)[(a)]

	Taxation receipts														Non-taxation receipts				
	Income tax									Other taxation receipts									
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	FBT	Super funds	Companies	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	Total other tax	Total tax receipts	Interest	Dividends and other	Total non-tax receipts	Total receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1976-77	10.5	2.7	1.4	11.8	-	-	3.0	-	14.8	1.2	1.4	1.2	6.1	20.9	1.7	0.2	1.9	22.8
1977-78	10.4	2.4	0.9	11.9	-	0.0	3.0	-	14.9	1.3	1.3	1.1	5.9	20.8	1.7	0.3	2.1	22.9
1978-79	9.9	2.1	0.9	11.1	-	0.0	2.6	-	13.7	1.8	1.5	1.2	6.5	20.1	1.6	0.3	2.0	22.1
1979-80	10.1	2.2	0.9	11.4	-	0.0	2.6	-	14.0	2.4	1.3	1.2	6.8	20.8	1.4	0.3	1.7	22.5
1980-81	10.3	2.3	0.8	11.8	-	0.0	3.1	-	14.9	2.7	1.2	1.2	6.9	21.8	1.4	0.3	1.7	23.5
1981-82	11.0	2.2	0.8	12.4	-	0.0	2.9	-	15.3	2.4	1.1	1.2	6.7	22.0	1.4	0.3	1.7	23.7
1982-83	11.3	2.2	1.1	12.5	-	0.0	2.6	-	15.1	2.6	1.1	1.1	7.1	22.2	1.5	0.5	2.0	24.1
1983-84	10.8	2.1	1.1	11.9	-	0.0	2.2	-	14.1	2.8	1.0	1.1	7.4	21.4	1.4	0.6	2.0	23.5
1984-85	11.2	2.3	0.9	12.8	-	0.0	2.4	-	15.2	2.8	0.9	1.3	7.7	22.9	1.4	0.7	2.1	25.0
1985-86	11.5	2.6	1.3	13.0	-	0.0	2.4	-	15.4	2.8	0.9	1.3	7.8	23.1	1.4	1.0	2.4	25.5
1986-87	11.7	3.1	1.3	13.8	0.2	0.0	2.4	-	16.4	2.6	0.9	1.2	7.5	23.8	1.3	1.1	2.4	26.2
1987-88	11.2	3.1	1.3	13.3	0.3	0.0	2.8	-	16.3	2.3	0.9	1.1	7.3	23.6	1.1	0.8	1.9	25.5
1988-89	11.6	2.8	1.4	13.3	0.3	0.0	2.8	-	16.4	1.9	0.6	1.0	6.7	23.1	1.0	0.3	1.4	24.5
1989-90	11.2	2.6	1.5	12.8	0.3	0.1	3.3	0.0	16.5	1.9	0.6	1.0	6.5	23.0	0.9	0.3	1.2	24.1
1990-91	11.0	2.8	1.7	12.5	0.3	0.3	3.5	0.1	16.6	2.0	0.6	0.8	6.2	22.8	0.8	0.4	1.2	24.0
1991-92	10.7	2.2	1.9	11.4	0.3	0.3	3.2	0.2	15.4	1.7	0.6	0.8	5.7	21.1	0.7	0.6	1.3	22.4
1992-93	10.5	1.9	1.8	11.0	0.3	0.3	3.0	0.3	15.0	1.7	0.5	0.8	5.4	20.4	0.6	0.7	1.3	21.7
1993-94	10.4	1.9	1.5	11.2	0.3	0.3	2.8	0.2	14.7	1.9	0.5	0.7	5.7	20.4	0.4	1.0	1.5	21.9
1994-95	10.7	1.9	1.6	11.4	0.6	0.4	3.2	0.2	15.8	1.9	0.5	0.7	6.0	21.7	0.4	0.6	1.0	22.7
1995-96	11.2	1.9	1.6	11.9	0.6	0.3	3.5	0.2	16.5	2.0	0.5	0.6	6.0	22.5	0.3	0.8	1.0	23.5
1996-97	11.4	2.2	1.6	12.4	0.6	0.5	3.5	0.2	17.2	1.9	0.5	0.6	5.9	23.1	0.2	0.7	1.0	24.0
1997-98	11.6	2.1	1.6	12.5	0.5	0.5	3.4	0.2	17.1	1.9	0.5	0.6	5.8	22.9	0.2	0.6	0.8	23.7

Table H2: Major categories of receipts as a proportion of gross domestic product (cash basis)[(a)] (continued)

	Taxation receipts														Non-taxation receipts			
	Income tax									Other taxation receipts								
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	FBT	Super funds	Companies	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	Total other tax	Total tax receipts	Interest	Dividends and other	Total non-tax receipts	Total receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1998-99	11.9	2.2	1.7	12.8	0.5	0.6	3.4	0.1	17.5	1.8	0.4	0.4	5.7	23.2	0.1	0.8	0.9	24.1
1999-00	12.1	2.1	1.7	12.9	0.6	0.6	3.8	0.2	18.1	1.8	0.4	0.4	5.4	23.5	0.2	2.1	2.3	25.7
2000-01	10.9	1.9	1.6	11.2	0.5	0.7	4.6	0.3	17.3	1.8	1.0	1.0	3.9	21.3	0.2	1.9	2.1	23.4
2001-02	10.7	2.2	1.4	11.5	0.5	0.6	3.7	0.2	16.5	1.7	0.9	0.9	3.7	20.2	0.1	1.9	2.0	22.1
2002-03	10.7	2.2	1.5	11.5	0.4	0.6	4.2	0.2	16.9	1.7	1.0	1.0	3.7	20.6	0.1	1.8	1.9	22.5
2003-04	10.7	2.4	1.5	11.6	0.4	0.7	4.3	0.1	17.1	1.6	0.9	0.9	3.5	20.6	0.1	1.6	1.7	22.3
2004-05	10.9	2.5	1.5	11.9	0.4	0.7	4.5	0.2	17.7	1.6	0.9	0.9	3.4	21.1	0.2	1.6	1.8	22.8
2005-06 est	10.8	2.6	1.6	11.8	0.4	0.7	5.2	0.2	18.3	1.5	0.8	0.8	3.1	21.4	0.2	1.6	1.9	23.3
2006-07 est	10.3	2.7	1.7	11.2	0.4	0.6	5.6	0.2	18.1	1.5	0.8	0.8	3.1	21.1	0.3	1.4	1.7	22.9

(a) Figures up to and including 1998-99 are based on the old Commonwealth Budget Sector cash accounting framework. Figures from 1999-2000 are on an Australian Government general government GFS basis.

Table H3: Major categories of receipts as a proportion of total receipts (cash basis)[(a)]

	Taxation receipts														Non-taxation receipts		
	Income tax									Other taxation receipts							
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	FBT	Super funds	Companies	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	Total other tax	Total tax receipts	Intrest	Dividends and other	Total non-tax receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1976-77	46.0	11.7	6.0	51.8	-	-	13.1	-	64.9	5.2	6.3	5.4	24.5	91.8	7.4	0.8	8.2
1977-78	45.3	10.5	4.0	51.9	-	0.0	13.1	-	65.0	5.7	5.9	4.8	23.8	91.0	7.6	1.4	9.0
1978-79	44.8	9.3	4.0	50.0	-	0.0	11.8	-	61.8	8.3	6.6	5.3	27.0	91.1	7.4	1.5	8.9
1979-80	45.1	9.6	3.8	50.9	-	0.0	11.4	-	62.4	10.7	6.0	5.2	28.1	92.4	6.4	1.2	7.6
1980-81	43.7	9.7	3.3	50.1	-	0.0	13.3	-	63.4	11.4	5.1	5.1	27.6	92.8	6.1	1.1	7.2
1981-82	46.4	9.2	3.5	52.2	-	0.0	12.3	-	64.6	10.1	4.5	5.0	26.6	92.8	5.9	1.3	7.2
1982-83	46.9	9.1	4.4	51.7	-	0.1	10.8	-	62.5	10.8	4.5	4.5	27.6	91.9	6.1	2.1	8.1
1983-84	45.9	9.1	4.9	50.7	-	0.0	9.3	-	60.0	11.7	4.3	4.7	29.2	91.4	6.0	2.6	8.6
1984-85	44.7	9.4	3.6	51.2	-	0.0	9.6	-	60.8	11.4	3.7	5.0	28.7	91.8	5.5	2.7	8.2
1985-86	45.0	10.3	5.2	51.0	-	0.0	9.4	-	60.4	10.9	3.6	5.0	28.3	90.8	5.3	3.9	9.2
1986-87	44.6	11.8	5.0	52.6	0.7	0.0	9.1	-	62.5	9.9	3.5	4.4	26.4	90.9	4.9	4.2	9.1
1987-88	44.0	12.0	5.1	52.2	1.1	0.0	10.8	-	64.0	9.2	3.4	4.5	26.3	92.5	4.4	3.0	7.5
1988-89	47.3	11.3	5.8	54.4	1.1	0.0	11.6	-	67.1	7.9	2.5	4.2	25.3	94.5	4.2	1.3	5.5
1989-90	46.4	10.8	6.1	53.1	1.2	0.4	13.5	0.0	68.2	8.0	2.3	4.1	25.0	95.2	3.6	1.2	4.8
1990-91	45.8	11.6	6.9	52.2	1.3	1.1	14.4	0.3	69.3	8.2	2.4	3.4	23.5	95.0	3.4	1.6	5.0
1991-92	47.8	9.8	8.3	50.9	1.4	1.2	14.4	0.9	68.9	7.7	2.5	3.5	23.4	94.1	3.2	2.7	5.9
1992-93	48.5	8.8	8.2	50.8	1.4	1.6	13.7	1.5	69.0	7.7	2.5	3.5	23.4	94.1	2.6	3.3	5.9
1993-94	47.6	8.6	7.1	51.1	1.4	1.2	12.6	1.1	67.3	8.5	2.2	3.2	24.3	93.3	2.0	4.6	6.7
1994-95	46.9	8.6	7.2	50.3	2.5	1.7	14.1	0.8	69.4	8.5	2.3	3.1	24.5	95.7	1.6	2.7	4.3
1995-96	47.5	8.3	6.8	50.8	2.5	1.3	15.0	0.6	70.2	8.4	2.1	2.6	23.8	95.6	1.2	3.2	4.4
1996-97	47.5	9.0	6.7	51.5	2.4	2.0	14.6	1.0	71.6	8.1	2.1	2.5	22.8	96.0	0.9	3.1	4.0
1997-98	48.8	8.8	7.0	52.5	2.3	2.3	14.2	0.7	71.9	8.0	1.9	2.7	22.8	96.5	0.8	2.6	3.5

Table H3: Major categories of receipts as a proportion of total receipts (cash basis)[(a)] (continued)

	Taxation receipts														Non-taxation receipts		
	Income tax									Other taxation receipts							
	Gross ITW	Gross other individuals	Refunds	Total individuals & w'holding	FBT	Super funds	Companies	PRRT	Total income tax	Petrol & other fuel products	Other excise	Customs duty	Total other tax	Total tax receipts	Intrest	Dividends and other	Total non-tax receipts
	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%	%
1998-99	49.4	8.9	7.1	53.2	2.2	2.7	14.2	0.3	72.6	7.5	1.8	2.5	23.8	96.4	0.5	3.2	3.6
1999-00	46.9	8.0	6.6	50.3	2.2	2.3	14.7	0.7	70.2	6.9	1.6	2.3	20.9	91.1	0.6	8.3	8.9
2000-01	46.6	8.2	6.8	47.9	2.2	3.0	19.6	1.5	74.2	7.7	4.1	2.8	16.9	91.1	0.7	8.2	8.9
2001-02	48.5	10.0	6.5	52.0	2.2	2.7	16.7	0.8	74.4	7.8	4.2	2.8	16.6	91.1	0.6	8.4	8.9
2002-03	47.7	9.9	6.6	50.9	2.0	2.7	18.6	1.0	75.2	7.5	4.2	2.8	16.3	91.5	0.6	8.0	8.5
2003-04	47.8	10.6	6.6	51.9	1.9	3.0	19.3	0.6	76.7	7.2	4.0	2.7	15.7	92.4	0.6	7.1	7.6
2004-05	47.7	11.1	6.7	52.0	1.8	3.1	19.8	0.7	77.4	7.0	3.7	2.5	14.8	92.3	0.7	7.1	7.7
2005-06 est	46.4	11.2	6.9	50.7	1.7	2.8	22.4	0.9	78.5	6.3	3.5	2.0	13.4	91.9	1.0	7.0	8.1
2006-07 est	44.8	11.6	7.3	49.1	1.6	2.8	24.3	1.1	79.0	6.3	3.5	2.2	13.4	92.4	1.5	6.1	7.6

(a) Figures up to and including 1998-99 are based on the old Commonwealth Budget Sector cash accounting framework. Figures from 1999-2000 are on an Australian Government general government GFS basis.

STATEMENT 6: EXPENSES AND NET CAPITAL INVESTMENT

Statement 6 presents estimates of general government expenses and net capital investment on a Government Finance Statistics (GFS) accrual accounting basis. The statement includes information on the allocation of Australian Government funds to the various functions of government. These functions are based on an international standard classification of functions of government that is incorporated into the GFS framework.

The first part of this statement provides information on trends in expense estimates while the second part presents trends in net capital investment estimates. Estimates are on an Australian Government general government sector basis.

Statement 6 focuses on short to medium-term expense trends and their underlying determinants. Consistent with this emphasis, much of Statement 6 explains year-on-year changes across the forward estimates.

Further information on portfolio and agency expenses, capital movements, major outputs and administered items may be found in the respective Portfolio Budget Statements.

The main trends are:

- general government expenses are forecast to rise from 21.6 per cent of gross domestic product (GDP) in 2005-06 to 21.8 per cent of GDP in 2006-07 and then increase to 21.9 per cent of GDP in 2009-10;
- in 2006-07, the social security and welfare, health, defence and education functions together account for approximately 76 per cent of total expenses with social security and welfare accounting for approximately 42 per cent of total expenses;
- in real terms, the strongest growth across the budget and forward estimates is occurring in the health, social security and welfare, general public services, education and other purposes functions, with growth in other functions either being largely stable or declining; and
- net capital investment in 2006-07 largely reflects increased investment in construction projects, security enhancements, refurbishment and relocation of various overseas missions, and increased Defence Housing Authority property holdings.

CONTENTS

STATEMENT 6: EXPENSES AND NET CAPITAL INVESTMENT

OVERVIEW

Australian Government general government expenses are expected to grow in real terms in 2006-07 and over the forward estimates period to 2009-10 (Table 1). Expenses are forecast to rise slightly from 21.6 per cent of gross domestic product (GDP) in 2005-06 to 21.8 per cent of GDP in 2006-07, and are projected to increase to 21.9 per cent of GDP in 2009-10. On a cash basis, payments remain at around 21.6 per cent of GDP over the budget and forward estimates.

Table 1: Estimates of expenses

	2005-06		2006-07	2007-08	2008-09	2009-10
	MYEFO(a)	Revised	Estimate	Projections		
Total expenses ($b)	**207.0**	**206.0**	**219.7**	**230.6**	**240.9**	**252.6**
Real growth on previous year(%)(b)	1.4	0.9	4.1	4.1	3.5	2.9
Per cent of GDP	21.6	21.6	21.8	21.9	22.0	21.9

(a) As published in the *Mid-Year Economic and Fiscal Outlook 2005-06*.
(b) Real growth is calculated using the non-farm gross domestic product (GDP) deflator.

GENERAL GOVERNMENT EXPENSES

Reconciliation of expenses since the 2005-06 Budget

Table 2 provides a reconciliation of expense estimates between the 2005-06 Budget, *Mid-Year Economic and Fiscal Outlook 2005-06 (*MYEFO*)* and the 2006-07 Budget, showing the effect of policy decisions and economic parameter and other variations.

Table 2: Reconciliation of expense estimates

	Estimates		Projections	
	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m
2005-06 Budget expenses	**206,081**	**214,806**	**225,400**	**236,568**
Changes between 2005-06 Budget and MYEFO				
Effect of policy decisions(a)	1,525	1,229	1,099	1,115
Effect of economic parameter variations				
Unemployment benefits	151	281	312	355
Prices and wages	243	1,221	1,141	971
Interest and exchange rates	64	93	64	97
Total economic parameter variations	*458*	*1,595*	*1,516*	*1,423*
Public debt interest	29	37	89	145
Programme specific parameter variations	-1,332	-594	-576	-422
Slippage in 2005-06 Budget decisions	1	0	0	0
Other variations	277	-214	-264	-985
Total variations	**957**	**2,052**	**1,863**	**1,275**
2005-06 MYEFO expenses	**207,038**	**216,858**	**227,263**	**237,843**
Changes between MYEFO and 2006-07 Budget				
Effect of policy decisions(a)	2,032	4,271	4,836	5,254
Effect of economic parameter variations				
Unemployment benefits	-23	172	132	165
Prices and wages	-139	-220	62	-50
Interest and exchange rates	-4	-172	90	73
Total economic parameter variations	*-167*	*-220*	*284*	*188*
Public debt interest	-14	-55	-167	-190
Programme specific parameter variations	-1,458	-1,316	-1,648	-1,574
Slippage in 2005-06 Budget decisions	-2	-4	-8	-39
Other variations	-1,412	195	-3	-571
Total variations	**-1,020**	**2,871**	**3,293**	**3,067**
2006-07 Budget expenses	**206,018**	**219,730**	**230,556**	**240,910**

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

Discussion of the major changes between the 2005-06 MYEFO and the 2006-07 Budget, shown in the above table can be found in Statement 2 (in the section titled Variations in expense estimates). Further information on expense measures can be found in Budget Paper No. 2, *Budget Measures 2006-07*.

Expense estimates by function

Table 3 sets out the estimates of Australian Government general government expenses by function for the period 2005-06 to 2009-10.

Table 3: Estimates of expenses by function

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
General public services	13,033	13,809	14,656	15,091	15,455
Defence	15,802	17,871	17,955	18,078	19,013
Public order and safety	2,804	3,286	3,326	3,370	3,450
Education	15,622	16,633	17,041	17,606	18,353
Health	37,620	39,838	41,991	43,635	45,459
Social security and welfare	86,372	91,756	95,807	99,991	103,788
Housing and community amenities(a)	2,321	2,790	3,026	2,631	2,314
Recreation and culture	2,699	2,627	2,549	2,513	2,534
Fuel and energy	4,013	4,804	4,958	5,290	5,304
Agriculture, forestry and fishing(a)	2,412	2,300	1,942	1,588	1,331
Mining, manufacturing and construction	1,847	2,085	2,030	2,046	2,038
Transport and communication	3,104	3,552	4,023	4,166	2,649
Other economic affairs	5,101	5,618	5,560	5,496	5,595
Other purposes	13,269	12,761	15,692	19,408	25,311
Total expenses	**206,018**	**219,730**	**230,556**	**240,910**	**252,592**

(a) There has been some reclassification of expenditure that was previously reported under the natural resources development sub-function (agriculture, forestry and fishing) to other primary functions.

Major movements within the estimates of expenses by function between 2005-06 and 2006-07, and across the forward estimates, include increases in the following functions:

- **Social security and welfare** due to the continued effect of indexation of payments together with the demographic and social factors that affect demand driven programmes;

- **Health** due to a continued growth in the use of medical and pharmaceutical services over the forward estimates period, increasing costs for the provision of medical services, a continuing trend towards newer and more expensive drugs under the Pharmaceutical Benefits Scheme and additional support programmes for mental health services;

- **Defence** due to continued funding increases associated with the Government's White Paper *Defence 2000 — Our Future Defence Force,* the Hardened and Networked Army — Phase 2 and Heavy Air Lift Capability, together with funding for major Australian Defence Force deployments, such as operations in Iraq and Afghanistan; and

- **Education** due to increased schools funding over the four year period 2005 to 2008 (calendar year) provided under the *Schools Assistance Act 2004* together with increased higher education funding reflecting increases under the *Our Universities — Backing Australia's Future* package and the Commonwealth Grant Scheme.

Estimates presented in Table 3 above are explained in greater detail for each individual function in the following pages.

General public services

Table 4: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Legislative and executive affairs	737	830	948	777	784
Financial and fiscal affairs	4,048	4,109	4,076	4,117	4,211
Foreign affairs and economic aid	2,929	3,293	3,957	4,420	4,525
General research	2,324	2,386	2,437	2,446	2,498
General services	524	639	639	640	653
Government superannuation benefits	2,472	2,551	2,600	2,690	2,783
Total general public services	**13,033**	**13,809**	**14,656**	**15,091**	**15,455**

Nature of expenses and major trends

The general public services function includes expenses relating to the organisation and operation of government. This includes: expenses related to the Parliament, Governor-General and conduct of elections; expenses related to the collection of taxes, and management of public funds and public debt; and assistance to developing countries including assistance initiatives in the Pacific, contributions to international organisations and the operations of the foreign service. It also includes: expenses related to research in areas not otherwise connected with a specific function; expenses related to overall economic and statistical services and government superannuation benefits (excluding nominal interest expenses on unfunded liabilities which are included under the nominal superannuation interest sub-function in the other purposes function).

Expenses within the function tend to fluctuate over the budget and forward estimates period partly due to factors such as the preparation for a federal election expected in 2007-08 and the Asia-Pacific Economic Cooperation conference in 2007 (legislative and executive affairs sub-function) and the 2006 Census (financial and fiscal affairs sub-function).

The increases in expenses in the foreign affairs and economic aid sub-function over the budget and forward estimates reflect the impact of the Government's goal to increase the level of Official Development Assistance to around $4 billion by 2010 and to forgive 80 per cent of Iraq's debt to Australia. Fluctuations in the foreign affairs and economic aid sub-function over the budget and forward years also reflect timing effects in Australia's contributions to multilateral development banks.

The increase in expenses from 2005-06 to 2006-07 in the general services sub-function arises primarily from a revision of Comcare's estimates for workers' compensation premiums and claims expenses taking into account recent actuarial reports and trends in 2005-06.

Defence

Table 5: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Defence	15,802	17,871	17,955	18,078	19,013
Total defence	**15,802**	**17,871**	**17,955**	**18,078**	**19,013**

Nature of expenses and major trends

Expenses in this function are within the Defence portfolio and support operations and delivery of navy, army, air and intelligence capabilities and strategic policy in the defence of Australia and its national interests.

Total annual expenses for the Defence function are estimated to rise by $3.2 billion over the period 2005-06 to 2009-10. In real terms, the growth in expenses for this function is 3.2 per cent a year on average.

The growth and pattern of expenditure is due to a number of factors. Firstly, there is the influence of significant funding increases for investments in capability announced by the Government in *Defence 2000 — Our Future Defence Force* (the Defence 2000 White Paper). Secondly, there are variations in funding levels for major Australian Defence Force deployments, such as the operations in Iraq and Afghanistan.

The remaining variation in expenses is largely due to additional funding being provided in this and previous budgets for logistics, Heavy Air Lift Capability and the Hardened and Networked Army — Phase 2 and military personnel costs and initiatives.

Public order and safety

Table 6: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Courts and legal services	741	870	895	926	932
Other public order and safety	2,063	2,416	2,431	2,445	2,518
Total public order and safety	**2,804**	**3,286**	**3,326**	**3,370**	**3,450**

Nature of expenses and major trends

Expenses for the public order and safety function support the administration of the federal legal system and the provision of legal services, including legal aid, to the community. Public order and safety expenses also include law enforcement and intelligence activities, as well as the protection of Australian Government property.

Expenses for the courts and legal services sub-function are expected to increase from 2005-06 to 2009-10 reflecting the growth in funding for the family law system announced in 2005-06, the refurbishment of the Sydney Law Courts and increased prosecutions relating to federal law.

Expenses for the other public order and safety sub-function are expected to increase by 3.5 per cent annually on average in real terms from 2005-06 to 2009-10 reflecting security and border protection measures. Key areas of growth include aviation security, intelligence capabilities and the response to illegal foreign fishers in Australia's northern waters. A significant component of the growth in intelligence capabilities is the increase in resources to be provided to the Australian Security Intelligence Organisation (ASIO). This follows the review of ASIO resourcing undertaken by Mr Allan Taylor AM in 2005.

Education

Table 7: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Higher education	5,199	5,361	5,492	5,630	5,765
Vocational and other education	1,543	1,607	1,629	1,649	1,681
Non-government schools	5,393	5,822	6,225	6,553	6,967
Government schools	2,898	3,215	3,068	3,124	3,280
Schools	*8,290*	*9,036*	*9,293*	*9,677*	*10,246*
Student assistance	475	486	498	530	548
General administration	1	2	1	1	1
School education - specific funding	114	141	129	120	112
Total education	**15,622**	**16,633**	**17,041**	**17,606**	**18,353**

Nature of expenses and major trends

Education expenses support the delivery of education services through: higher education institutions; vocational education and training providers (including technical and further education institutions); and government (State and Territory) and non-government schools.

Expenses under the student assistance sub-function include the ABSTUDY scheme, Assistance for Isolated Children and income support for students aged twenty-five years and over through AUSTUDY.

Total expenses for this function are estimated to increase by 6.4 per cent in real terms over the three forward years, 2007-08 to 2009-10, or 2.1 per cent annually on average, with expenditure on higher education and schools being the main drivers.

Funding for higher education continues to grow over the forward years, reflecting increases in expenditure under *Our Universities — Backing Australia's Future*, the Commonwealth Grant Scheme, increases to the number of higher education student places and scholarships, and additional funding for capital projects.

Growth in expenses relating to schools is largely driven by funding provided under the *Schools Assistance Act 2004* (the Act). Estimated Australian Government funding of $32 billion under the 2005-08 *Quadrennial Schools Funding Agreements* will be provided over the four-year period 2005 to 2008 (calendar year) through the Act. The remaining funding under this sub-function is largely made up of the *$1 billion Investment In Our School Infrastructure*, Australian Technical Colleges and Indigenous Education Strategic Initiatives. The estimated funding for government schools decreases from 2006-07 to 2007-08, mainly due to funding of $186 million for school infrastructure being brought forward from calendar year 2008 to calendar year 2006 to meet stronger than expected demand for funding under the initiative.

Health

Table 8: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Medical services and benefits(a)	16,329	16,879	17,600	18,375	19,157
Hospital services	1,588	1,710	1,753	1,793	1,831
Health care agreements	8,385	8,882	9,304	9,439	9,618
Hospital services and health care agreements	*9,974*	*10,592*	*11,058*	*11,232*	*11,449*
Pharmaceutical services and benefits	7,108	7,775	8,494	8,909	9,501
Aboriginal and Torres Strait Islander health	347	423	428	454	477
Health services	1,481	1,411	1,471	1,481	1,503
Other health services	1,572	1,775	1,897	2,061	2,208
Other health services	*3,054*	*3,185*	*3,368*	*3,542*	*3,711*
General administration	586	737	794	858	887
Health assistance to the aged	224	247	248	264	276
Total health	**37,620**	**39,838**	**41,991**	**43,635**	**45,459**

(a) The financial impact of premium growth on the forward estimates for the Private Health Insurance Rebate has been allocated to the contingency reserve.

Nature of expenses and major trends

The health function includes expenses relating to: medical services funded through Medicare and the Private Health Insurance Rebate (medical services and benefits sub-function); provision of in-hospital services to eligible veterans and their dependants (hospital services sub-function); funding under Australian Health Care Agreements between the Australian Government and the States and Territories (health care agreements sub-function); and the Pharmaceutical Benefits and Repatriation Pharmaceutical Benefits Schemes (pharmaceutical services and benefits sub-function).

The major purpose of health function expenditure is to ensure that all Australians have access to essential health services through a range of providers and without excessive price barriers.

While expenses related to health are likely to be a major, if not the major, contributor to the growth in Australian Government spending in the coming decades, total Government health spending is expected to remain at around 4 per cent of GDP over the budget and forward estimates years.

Total expenses for this function are estimated to increase by 10.0 per cent in real terms over the three forward years, or on average by around 3.2 per cent per annum in real terms.

Medical services and benefits funded through Medicare and the Private Health Insurance Rebate are the main contributors to health function expenses and are estimated to increase by 9.4 per cent in real terms over the three forward years, or on average by around 3.1 per cent per annum in real terms, making up around 42 per cent of total health expenditure in 2006-07 and across the forward estimates.

The hospital services sub-function has average annual growth in real terms of 1.1 per cent due to an ageing and increasingly frail veteran community requiring more hospital services. This average level of growth is increasing at a slower rate compared to last year due to declining client numbers in the veteran community.

The trend in the estimates for the health care agreements sub-function is driven by funding growth determined in the Australian Health Care Agreements, which cover the period 1 July 2003 to 30 June 2008.

While forecast expenses have been reduced over the forward estimates since the 2005-06 Budget, expenses for the pharmaceutical services and benefits sub-function continues to be one of the fastest growing health expenses and is forecast to grow at an average of 5.6 per cent per annum in real terms. This growth is driven by a combination of an ageing population and demand for newer and more expensive drugs.

Box 6.1: Pharmaceutical services and benefits

Table 8.1: Trends in major components of the pharmaceutical services and benefits sub-function

	2005-06	**2006-07**	2007-08	2008-09	2009-10
	$m	**$m**	$m	$m	$m
Pharmaceutical Benefits (Concessional)(a)	4,337	**4,544**	4,967	5,217	5,576
Pharmaceutical Benefits (General)(a)	1,072	**1,240**	1,383	1,496	1,635
Repatriation Pharmaceutical Benefits Scheme(b)	483	**485**	504	514	524
High Specialised Drugs(a)	527	**580**	638	695	749
Essential Vaccines	181	**175**	184	120	122
Other(c)	336	**566**	622	663	693
Sub-total administered items	6,936	**7,589**	8,299	8,705	9,298
Departmental expenses(d)	172	**186**	195	204	203
Total	**7,108**	**7,775**	**8,494**	**8,909**	**9,501**

(a) Since the 2005-06 Budget, there were significant variations to estimates for larger drug categories. For a detailed discussion of the Pharmaceutical Benefits Scheme, refer to Outcome 2 of Health and Ageing Portfolio Budget Statements 2006-07.

(b) Veterans' Pharmaceutical Services are covered under Outcome 2 of the Department of Veterans' Affairs (Defence Portfolio) Portfolio Budget Statements 2006-07. Since the 2005-06 Budget, there have been downward revisions to their forward estimates.

(c) Subsumed within Outcomes 1 and 2 of Health and Ageing Portfolio Budget Statements 2006-07. The ongoing increase in 2006-07 is due to the impact of the Community Pharmacy Agreement.

(d) Approximately 20 per cent of Medicare Australia (formerly Health Insurance Commission) departmental expenses and 14 per cent of Health and Ageing departmental expenses are allocated to this sub-function.

Social security and welfare

Table 9: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Assistance to the aged	29,776	31,704	33,685	35,619	37,647
Assistance to veterans and dependants	5,625	6,026	6,044	6,115	6,075
Assistance to people with disabilities	12,365	12,846	13,390	13,892	14,419
Assistance to families with children	26,407	27,878	28,538	29,345	29,670
Assistance to the unemployed	4,857	5,580	6,314	7,122	7,979
Assistance to the sick	86	85	87	88	87
Assistance to the unemployed and sick	*4,942*	*5,665*	*6,400*	*7,210*	*8,066*
Common youth allowance	2,190	2,273	2,279	2,299	2,316
Other welfare programmes	1,525	1,502	1,514	1,567	1,622
Aboriginal advancement nec	1,389	1,422	1,433	1,479	1,512
General administration	2,153	2,440	2,524	2,466	2,461
Total social security and welfare	**86,372**	**91,756**	**95,807**	**99,991**	**103,788**

Nature of expenses and major trends

The social security and welfare function includes pensions and services to the aged, services to the unemployed, assistance to people with disabilities, a variety of assistance to families with children, income support and compensation for veterans and their dependants, and advancement programmes for Aboriginal and Torres Strait Islander people.

Social security and welfare function expenses are estimated to total around $91.8 billion in 2006-07 and grow significantly over the forward years. The sub-functions contributing most to the growth over the forward years are the assistance to the aged and assistance to people with disabilities. The main driver of growth in these sub-functions is the indexation of payments, including maintaining the single rate of age and disability pensions at a minimum of 25 per cent of Male Total Average Weekly Earnings. The growth also reflects demographic and social factors such as the ageing of the population.

The assistance to families with children sub-function is expected to grow steadily at 2.6 per cent, in real terms, over the forward estimates. This sub-function includes the Family Tax Benefit, Parenting Payments and the Child Care Benefit as the most significant contributing programmes.

Lower estimates than in previous years for the sub-function for aboriginal advancement, not elsewhere classified, are due largely to a revision of the estimates for the payment to the Indigenous Land Corporation from the Aboriginal and Torres Strait Islander Land Account, which is paid in accordance with the *Aboriginal and Torres Strait Islander Act 2005*.

The general administration sub-function largely consists of Centrelink's operating costs and is expected to increase from 2005-06 to 2006-07 due to higher staffing numbers in Centrelink, largely due to the implementation of a number of new measures taking effect in 2006-07.

Housing and community amenities

Table 10: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Housing	1,629	1,670	1,725	1,787	1,823
Urban and regional development	202	209	185	138	137
Environment protection	491	911	1,116	706	355
Total housing and community amenities(a)	**2,321**	**2,790**	**3,026**	**2,631**	**2,314**

(a) There has been some reclassification of expenditure that was previously reported under the natural resources development sub-function (agriculture, forestry and fishing) to other primary functions.

Nature of expenses and major trends

The housing and community amenities function includes the Australian Government's contribution to the *Commonwealth-State Housing Agreement*, expenses of the Defence Housing Authority and various regional development and environment protection programmes.

Housing sub-function expenses are estimated to grow over the forward years mainly due to demand by Defence for the on-going upgrade and supply of housing stock. Growth in the housing sub-function over 2006-07 and 2007-08 is mainly due to the increased expenditure relating to Defence housing requirements, primarily in support of the personnel to be assigned to the Headquarters Joint Operation Command to be located in Bungendore, New South Wales.

The decrease in expenses in the urban and regional development sub-function from 2006-07 to 2008-09 primarily reflects the conclusion of the Sustainable Regions, Natural Disaster Mitigation and Bushfire Mitigation programmes.

There has been an increase in expenses under the environment protection sub-function due to the inclusion of expenditure under the three programmes that make up the Australian Government Water Fund (AGWF). The AGWF was previously reported under the natural resources development sub-function (agriculture, forestry and fishing function). The expenditure under this sub-function varies significantly from year-to-year due to the timing of the payment of grants, primarily under the largest AGWF programme, Water Smart Australia.

Expenses under the environment protection sub-function decrease between 2007-08 and 2008-09 largely due to the termination of funding for the Natural Heritage Trust (NHT) in 2007-08. A provision for the continuation of NHT has been included in the contingency reserve for 2008-09 and 2009-10. The remaining decrease reflects the termination in 2007-08 of some measures announced as part of the Climate Change Strategy and the conclusion of funding for the Water Wise Communities programme.

Recreation and culture

Table 11: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Broadcasting	1,251	1,277	1,288	1,308	1,329
Arts and cultural heritage	857	868	847	830	840
Sport and recreation	355	269	238	216	206
National estate and parks	236	213	176	159	158
Total recreation and culture	**2,699**	**2,627**	**2,549**	**2,513**	**2,534**

Nature of expenses and major trends

Recreation and culture function expenses support public broadcasting; the regulatory framework for Australia's broadcasting sector; cultural institutions; funding for the arts and the film industry; assistance to sport and recreation activities; and the management and protection of national parks and other world heritage areas. This function also includes expenses relating to the protection and preservation of historic sites and buildings, including war graves.

Total expenses for the recreation and culture function decrease slowly over the period from 2005-06 to 2009-10 with some fluctuation.

The broadcasting sub-function expenses increase over the forward estimates, in part due to increased resourcing for the Australian Broadcasting Corporation for Australian television content and the regional and local programming initiative, announced in the context of the Australian Broadcasting Corporation triennial funding arrangements.

Higher expenses in the sport and recreation sub-function in 2005-06 primarily reflect a direct payment to the Victorian Government to assist with costs associated with staging the Melbourne 2006 Commonwealth Games. It also reflects additional funding under the programme Building a Healthy, Active Australia — Active After-school Communities. This programme concludes in 2007-08, contributing to the declining trend over the forward years for this sub-function.

The national estate and parks sub-function expenses decrease due to completion of several small programmes. The decrease from 2007-08 is largely due to cessation of funding for the Natural Heritage Trust (NHT). A provision for the continuation of NHT has been included in the contingency reserve for 2008-09 and 2009-10.

Fuel and energy

Table 12: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Fuel and energy	4,013	4,804	4,958	5,290	5,304
Total fuel and energy	**4,013**	**4,804**	**4,958**	**5,290**	**5,304**

Nature of expenses and major trends

This function includes expenses for the Energy Grants Credits Scheme (EGCS), Cleaner Fuels Grants Scheme and the Fuels Sales Grants Scheme (FGCS), which are administered by the Australian Taxation Office. The Fuel Tax Credits (FTC) will replace the EGCS on 1 July 2006 and the FSGS will terminate at the end of 2005-06.

This function also includes expenses of the Department of the Environment and Heritage for programmes funded under *A New Tax System — Measures for a Better Environment* package, the *Climate Change Strategy* measures and the *Securing Australia's Energy Future* measures. These expenses increase in 2006-07 due to higher funding levels for several greenhouse related programmes, including the Low Emissions Technology Demonstration Fund and Solar Cities programme.

Also included within this function are expenses for programmes relating to the production of alternative fuels including ethanol and biodiesel, which are administered by the Department of Industry, Tourism and Resources and the Australian Taxation Office respectively.

Following the replacement of the EGCS with the FTC on 1 July 2006, this function is expected to have significant growth from 2006-07 due to the staged expansion of entitlements. This includes an increase in expenses in 2008-09 due to the extension of eligibility for 'off-road' business users. In addition, expenses increase in the forward estimates period due to the higher fuel tax credit payments flowing from the decision to freeze the road user charge for operators of heavy vehicles. An additional increase in expenses (fully offset by increased revenue) results from moving to a regime where all fuel attracts the full rate of excise or customs duty and a full tax credit is provided for business use other than as fuel (for example use in solvents, paints and the like). This continues to provide an effective excise-free outcome in these circumstances.

Agriculture, forestry and fishing

Table 13: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Wool industry	49	52	56	56	56
Grains industry	153	150	152	153	121
Dairy industry	111	93	85	79	55
Cattle, sheep and pig industry	135	146	147	147	146
Fishing, horticulture and other agriculture	285	490	322	245	227
General assistance not allocated to specific industries	414	423	403	399	367
Rural assistance	674	269	82	27	27
Natural resources development(a)	395	487	519	316	187
General administration	196	190	178	165	145
Total agriculture, forestry and fishing	**2,412**	**2,300**	**1,942**	**1,588**	**1,331**

(a) There has been some reclassification of expenditure that was previously reported under natural resources development to primary functions other than agriculture, forestry and fishing.

Nature of expenses and major trends

Agriculture, forestry and fishing function expenses support assistance to primary producers, forestry, fishing, land and water resources management, quarantine services and contributions to research and development.

Expenses within this function are expected to decrease by around 40 per cent between 2006-07 and 2009-10, reflecting expected decreases in expenditure on drought-related measures within the rural assistance sub-function. This reflects an assumed return to normal seasonal conditions in Australia and a consequent cessation of drought assistance outlays. The decrease is also attributable to the conclusion of the Tasmanian Community Forest Agreement Package (fishing, horticulture and other agriculture sub-function) and termination of funding in 2007-08 for the Natural Heritage Trust (NHT) and the National Action Plan on Salinity and Water Quality (NAP) (natural resources development sub-function). A provision for the continuation of NHT and NAP has been included in the contingency reserve for 2008-09 and 2009-10. In addition the decrease between 2008-09 and 2009-10 is partially due to reduced grains research and development (grains industry sub-function).

The overall decrease is partially offset by the additional funding for the Murray-Darling Basin Commission (natural resources development sub-function) over the period 2006-07 to 2010-11. In addition the increase in 2006-07 in the fishing, horticulture and other agriculture sub-function is a result of expenditure on the Fisheries Structural Adjustment package.

Other significant expenses on conservation and sustainable use and repair of Australia's natural environment are included in the environment protection sub-function (housing and community amenities function) and the national estate and parks sub-function (recreation and culture function).

Expenditure on the three programmes that make up the Australian Government Water Fund was previously reported under the natural resources development sub-function. They have now been reclassified to the environment protection sub-function (housing and community amenities function).

Mining, manufacturing and construction

Table 14: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Mining, manufacturing and construction	1,847	2,085	2,030	2,046	2,038
Total mining, manufacturing and construction	**1,847**	**2,085**	**2,030**	**2,046**	**2,038**

Nature of expenses and major trends

Expenses under this function relate to the manufacturing and export sectors, and are designed to improve the efficiency and competitiveness of Australian industries. Major expenses include programmes specific to the automotive, textiles, clothing and footwear (TCF) and pharmaceutical industries. Expenses also include Australian Government assistance to exporters through direct financial assistance for the development of export markets, information and promotional assistance, finance and insurance services, trade policy, programmes providing research and development assistance grants, and a programme of strategic investment incentives.

The introduction of a lower level of assistance under the new TCF Strategic Investment Programme (announced in the 2003-04 MYEFO) will be offset, in 2006-07, by higher grant payments under the Commercial Ready Programme, an increase in payments under the Pharmaceuticals Partnerships Programme, an expected increase in assistance under the Automotive Competitiveness and Investment Scheme, expected growth in the Research and Development Tax Concession Scheme and a continuation of funding for projects under the Strategic Investment Coordination process.

In 2007-08, a lower number of projects being funded under the Strategic Investment Coordination process has been partially offset by expected growth in the Pharmaceuticals Partnerships Programme.

In 2008-09, expenses increase due to expected higher grant payments under the Commercial Ready Programme and expected growth in concessions granted under the Research and Development Tax Concession Scheme.

The reduction in expenses from 2008-09 to 2009-10 arises from the conclusion of funding for the Pharmaceuticals Partnerships Programme and a reduction in the expected level of assistance under the Automotive Competitiveness and Investment Scheme, partially offset by expected growth in concessions granted under the Research and Development Tax Concession Scheme.

Transport and communication

Table 15: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Communication	622	705	638	613	331
Rail transport	301	107	169	176	0
Air transport	175	145	126	129	130
Road transport	1,619	2,206	2,697	2,853	1,789
Sea transport	217	238	248	250	252
Other transport and communication	170	151	144	146	147
Total transport and communication	**3,104**	**3,552**	**4,023**	**4,166**	**2,649**

Nature of expenses and major trends

Transport and communication function expenses support the infrastructure and regulatory framework for Australia's transport and communications sectors.

The increased expense in the communication sub-function between 2005-06 and 2006-07 is due to the telecommunications programmes Connect Australia and Metro Broadband Blackspots, which commenced in 2005-06. The overall decline in the sub-function from 2006-07 to 2009-10 reflects the conclusion of telecommunications and information technology initiatives, including the Telstra Social Bonus 2, the response to the Telecommunications Service (Besley) Inquiry, and the Building on IT Strengths, Metro Broadband Blackspots and the Connect Australia programmes.

The high level of expense in the rail transport sub-function in 2005-06 is due to the provision of $270 million to the Australian Rail Track Corporation for investment in the interstate rail network to improve the competitiveness of freight rail. The increasing expenses from 2006-07 to 2008-09 are due to rail expenses associated with the AusLink programme. These include the construction and upgrade of passing loops, communications systems and bridge over-passes on the inter-state rail networks, including the North-South rail line between Melbourne and Brisbane.

The high level of expense in the air transport sub-function in 2005-06 and 2006-07 is due to one-off aviation security initiatives, including grants for air cargo screening equipment, and a $28.5 million grant for the upgrade of the runway at Canberra International Airport.

The higher level of expense in the road transport sub-function from 2005-06 to 2008-09 is due to the AusLink programme. This includes an additional $1.7 billion in funding announced in the 2006-07 Budget for improvements to the national road network and an additional $307.5 million for improvements to local roads infrastructure. Further information can be found in the measures, *Investing in the nation's infrastructure — improving the national network* and *Investing in the nation's infrastructure — improving local roads*, under the Transport and Regional Services portfolio in the 2006-07 Budget Paper No. 2.

Funding for the second five-year plan of the AusLink programme from 2009-10 will be considered by the Government at a later date, so the 2009-10 projection for road transport is subject to change. The Road Safety Black Spot and the Roads to Recovery programmes are due to terminate in 2007-08 and 2008-09 respectively. The Government also provides untied funding to local governments through Financial Assistance Grants that are identified for roads — see the general purpose inter-government transactions sub-function (other purposes function).

The increased expense in the sea transport sub-function from 2006-07 is mainly due to the introduction of the national maritime towage and salvage arrangements. The arrangements provide for emergency maritime towage and salvage and will be administered by the Australian Maritime Safety Authority.

Other economic affairs

Table 16: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Tourism and area promotion	212	197	196	126	126
Vocational and industry training	650	755	796	826	850
Labour market assistance to job seekers and industry	2,058	2,278	2,253	2,201	2,230
Industrial relations	368	385	338	354	367
Immigration	905	1,043	1,029	1,032	1,057
Total labour and employment affairs	*3,980*	*4,461*	*4,416*	*4,414*	*4,503*
Other economic affairs nec	908	959	948	957	965
Total other economic affairs	**5,101**	**5,618**	**5,560**	**5,496**	**5,595**

Nature of expenses and major trends

The other economic affairs function includes expenses on tourism and area promotion, labour market assistance, immigration, industrial relations and other economic affairs not elsewhere classified.

Estimates for the labour market assistance to job seekers and industry sub-function reflect an overall increase in resourcing from 2006-07 to the Job Network, Work for the Dole and other work assistance programmes. The Government's Welfare to Work reform package announced in the 2005-06 Budget increased the expenditure on labour market assistance to job seekers.

The increase in the industrial relations sub-function in 2006-07 is a result of increased resourcing to the Department of Employment and Workplace Relations, Office of Workplace Services, Office of Employment Advocate, Australian Fair Pay Commission, Federal Court and Federal Magistrates Court to implement the Government's Workplace Relations reform package announced in the 2005-06 MYEFO.

Continuing growth in the vocational and industry training sub-function is due to an expected increase in apprenticeships/traineeships commencements and from a range of new initiatives targeting traditional trades and skill shortages generally, as a result of the Government's 2004 election commitments and the Commonwealth's contribution to the Council of Australian Governments' skills and training reforms.

The decline in 2008-09 in the tourism and area promotion sub-function reflects the conclusion of additional funding arrangements announced in the context of the 2003 White Paper on Tourism.

The variation in the immigration sub-function between 2005-06 and 2006-07 reflects an increase in resources for the Department of Immigration and Multicultural Affairs in response to the Palmer and Comrie Reports.

Other purposes

Table 17: Summary of expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Interest on Australian Government's behalf	3,629	3,514	3,447	3,310	3,283
Interest on behalf of states and territories	1	0	0	0	0
Interest received on Australian Government stock	0	0	0	0	0
Public debt interest	*3,629*	*3,514*	*3,447*	*3,310*	*3,283*
Nominal superannuation interest	5,583	5,784	5,870	6,077	6,289
General revenue assistance - states and territories	975	17	18	19	20
General capital assistance - states and territories	0	0	0	0	0
Debt assistance	220	0	0	0	0
Local government assistance	1,629	1,691	1,739	1,804	1,871
Revenue assistance to the states and territories	164	168	173	177	181
Assistance to other governments	668	740	741	624	475
General purpose inter-government transactions	*3,655*	*2,617*	*2,671*	*2,624*	*2,547*
Natural disaster relief	359	99	93	93	93
Contingency reserve(a)	42	747	3,611	7,303	13,099
Total other purposes	**13,269**	**12,761**	**15,692**	**19,408**	**25,311**

(a) Asset sale related expenses are treated as a component of the contingency reserve.

Nature of expenses and major trends

The other purposes function includes expenses incurred in the servicing of public debt interest, and assistance to the State, Territory and local governments. The function also includes items classified to natural disaster relief, the contingency reserve, and costs of asset sales.

The decline between 2005-06 and 2006-07 in general revenue assistance to the States reflects the cessation of National Competition Policy (NCP) payments and the removal of Budget Balancing Assistance (BBA) from the estimates from 2006-07 due to the expectation that the States and Territories will receive more GST revenue than their Guaranteed Minimum Amount and will not require BBA.

The NCP agreements only provide for payments to 30 June 2006. The Council of Australian Governments (COAG) has decided on a future National Reform Agenda. COAG agreed that, if funding is needed to ensure a fair sharing of the costs and benefits of reform, the Australian Government will provide funding to the States on a case-by-case basis once specific implementation plans have been developed. Payments to the States, and where appropriate, to local government, would be linked to achieving agreed actions or progress measures and demonstrable economic benefits.

There are no expenses in the debt assistance sub-function from 2006-07, reflecting the cessation of the agreed debt redemption arrangement between the Australian Government and the States in 2005-06.

The assistance to other governments sub-function includes payments to Western Australia for offshore petroleum royalties. Expenses in this sub-function fluctuate primarily due to variations in these payments. There is an expected increase in royalty payments to Western Australia in 2006-07. The reductions in expenses in 2008-09 and 2009-10 are due to the decrease in the estimated crude oil production volume from the North West Shelf project.

The natural disaster relief sub-function includes business assistance grants for the victims of Tropical Cyclone Larry, which are expected to conclude in 2005-06.

The increase in expenses in the contingency reserve from 2006-07 over the forward years is largely due to the conservative bias allowance — an allowance that compensates for the trend in expenses on existing Australian Government programmes to be underestimated by agencies in the forward years. There is also an increase in 2006-07 reflecting one-off asset sales expenses. The nature of the contingency reserve is discussed in more detail at Appendix B.

GENERAL GOVERNMENT NET CAPITAL INVESTMENT

Net capital investment comprises acquisitions of non-financial assets (including inventories) less non-financial asset disposals and depreciation.

Australian Government general government net capital investment is expected to rise in 2006-07 and remain positive, net of non-financial asset sales and depreciation, over the forward estimates period until 2009-10 (Table 18).

Table 18: Estimates of total net capital investment

	2005-06		2006-07	2007-08	2008-09	2009-10
	MYEFO(a)	Revised	Estimate	Projections		
Total net capital investment ($m)	**1,186**	**881**	**1,642**	**174**	**602**	**38**
Real growth on previous year(%)(b)	-	-	82.0	-89.5	242.0	-93.7
Per cent of GDP	0.1	0.1	0.2	0.0	0.1	0.0

(a) As published in the *Mid-Year Economic and Fiscal Outlook 2005-06*.
(b) Real growth is calculated using the non-farm gross domestic product (GDP) deflator.

Reconciliation of net capital investment since the 2005-06 Budget

A reconciliation of the 2005-06 Budget, 2005-06 MYEFO and 2006-07 Budget net capital investment estimates, showing the effect of policy decisions and economic parameter and other variations since the estimates were published in the 2005-06 Budget, is provided in Table 19.

Table 19: Reconciliation of net capital investment

	Estimates		Projections	
	2005-06	2006-07	2007-08	2008-09
	$m	$m	$m	$m
2005-06 Budget net capital investment	**1,020**	**617**	**1**	**-264**
Changes between 2005-06 Budget and MYEFO				
Effect of policy decisions	230	59	-15	4
Effect of parameter and other variations	-63	185	102	372
Total variations	**167**	**244**	**87**	**377**
2005-06 MYEFO net capital investment	**1,186**	**862**	**88**	**113**
Changes between MYEFO and 2006-07 Budget				
Effect of policy decisions	57	398	191	244
Effect of parameter and other variations	-363	382	-104	245
Total variations	**-306**	**780**	**86**	**489**
2006-07 Budget net capital investment	**881**	**1,642**	**174**	**602**

In 2006-07, forecast net capital investment has increased by $780 million since the 2005-06 MYEFO. This increase is due to the combined effect of new policy decisions of $398 million and parameter and other variations of $382 million.

Discussion of changes between the 2005-06 MYEFO and the 2006-07 Budget, shown in the table above, can be found in Statement 2 (in the section titled Variations in net capital investment estimates). Further information on capital measures since MYEFO can be found in Budget Paper No. 2, *Budget Measures 2006-07*.

Net capital investment estimates by function

Estimates for Australian Government general government net capital investment by function for the period 2005-06 to 2009-10 are provided in Table 20.

Table 20: Estimates of net capital investment by function

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
General public services	371	382	159	182	-58
Defence	-211	-10	-234	255	32
Public order and safety	135	109	26	3	1
Education	2	4	6	3	4
Health	98	201	11	-2	0
Social security and welfare	73	223	50	-4	-37
Housing and community amenities	72	214	36	37	6
Recreation and culture	76	110	18	2	-29
Fuel and energy	1	3	2	0	-1
Agriculture, forestry and fishing	19	42	5	3	1
Mining, manufacturing and construction	27	35	14	4	0
Transport and communications	57	16	1	-5	-15
Other economic affairs	138	183	52	0	-6
Other purposes	22	131	29	124	140
Total net capital investment	**881**	**1,642**	**174**	**602**	**38**

Net capital investment of $881 million is expected in 2005-06, largely reflecting — the construction of the Christmas Island Immigration Reception and Processing Centre and various other construction projects managed by the Department of Finance and Administration; investment by the Australian Nuclear Science and Technology Organisation in a new nuclear reactor; the acquisition of land and refurbishment/security upgrades of various overseas missions by the Department of Foreign Affairs and Trade; and investment in information technology by several agencies including the Australian Taxation Office, the Department of Employment and Workplace Relations and the Department of Veterans' Affairs.

Net capital investment is expected to rise between 2005-06 and 2006-07. Factors contributing to net capital investment, by function, include:

- **General Public Services** — the investment by the Department of Finance and Administration in its property portfolio, including construction of the Christmas Island Immigration Reception and Processing Centre and the National Portrait Gallery and security enhancements, refurbishment and relocation of various overseas missions by the Department of Foreign Affairs and Trade;

- **Housing and Community Amenities** — adjustments to the Defence Housing Authority's property portfolio including, increased inventory holdings due to fewer property sales, higher than anticipated finance leases and changes to Defence requirements affecting the Defence Housing Authority capital programme for construction and replacement of Australian Defence Force housing;

- **Health** — investment in pandemic influenza preparedness, including investment in anti-viral medication to protect against possible disease outbreaks such as avian influenza, infrastructure for Medicare Australia to establish the health and social services access card system and telephone counselling, self-help and support programmes for mental health services;

- **Social Security and Welfare** — the investment in information technology infrastructure for Centrelink including, enhancing the capability to detect and investigate social security fraud, opening additional Remote Area Service Centres, the establishment of the health and social services access card system and system changes for the Child Support Agency and Centrelink to implement the Child Support reforms;

- **Other Economic Affairs** — the development of information technology systems to ensure well trained and supported staff for the Department of Immigration and Multicultural Affairs;

- **Public Order and Safety** — investment by the Australian Security Intelligence Organisation in information technology, including expanding infrastructure to support growth in staff and operations and increasing technical and surveillance capability for counter-terrorism and counter-espionage related purposes, the relocation of state offices for the Australian Security Intelligence Organisation, and increased investment by the Australian Secret Intelligence Service to enhance counter-terrorism capabilities and help increase national security; and

- **Recreation and Culture** — increased capital for the Australian Broadcasting Corporation for replacing and updating its technical asset base, announced in the context of the Australian Broadcasting Corporation triennial funding arrangements. Also, revision to the Australian Broadcasting Corporation's estimates to reflect a delay in expenditure related to the digital television rollout from 2005-06 to 2006-07.

After 2006-07, net capital investment is expected to decrease. This results from the conclusion of various construction projects, as well as the progressive conclusion of the Department of Foreign Affairs and Trade's overseas mission upgrades and various information technology-based projects.

APPENDIX A: EXPENSE BY FUNCTION AND SUB-FUNCTION

Table A1: Estimates of expenses by function and sub-function

	Actuals	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
General public services						
Legislative and executive affairs	733	737	830	948	777	784
Financial and fiscal affairs	5,201	4,048	4,109	4,076	4,117	4,211
Foreign affairs and economic aid	2,863	2,929	3,293	3,957	4,420	4,525
General research	2,162	2,324	2,386	2,437	2,446	2,498
General services	638	524	639	639	640	653
Government superannuation benefits	2,386	2,472	2,551	2,600	2,690	2,783
Total general public services	**13,983**	**13,033**	**13,809**	**14,656**	**15,091**	**15,455**
Defence	**14,635**	**15,802**	**17,871**	**17,955**	**18,078**	**19,013**
Public order and safety						
Courts and legal services	660	741	870	895	926	932
Other public order and safety	1,689	2,063	2,416	2,431	2,445	2,518
Total public order and safety	**2,349**	**2,804**	**3,286**	**3,326**	**3,370**	**3,450**
Education						
Higher education	4,910	5,199	5,361	5,492	5,630	5,765
Vocational and other education	1,446	1,543	1,607	1,629	1,649	1,681
Non-government schools	4,990	5,393	5,822	6,225	6,553	6,967
Government schools	2,404	2,898	3,215	3,068	3,124	3,280
Schools	*7,394*	*8,290*	*9,036*	*9,293*	*9,677*	*10,246*
Student assistance	509	475	486	498	530	548
General administration	0	1	2	1	1	1
School education - specific funding	107	114	141	129	120	112
Total education	**14,365**	**15,622**	**16,633**	**17,041**	**17,606**	**18,353**
Health						
Medical services and benefits	14,891	16,329	16,879	17,600	18,375	19,157
Hospital services	1,386	1,588	1,710	1,753	1,793	1,831
Health care agreements	7,989	8,385	8,882	9,304	9,439	9,618
Hospital services and health care agreements	*9,375*	*9,974*	*10,592*	*11,058*	*11,232*	*11,449*
Pharmaceutical services and benefits	7,073	7,108	7,775	8,494	8,909	9,501
Aboriginal and Torres Strait Islander health	286	347	423	428	454	477
Health services	1,402	1,481	1,411	1,471	1,481	1,503
Other health services	1,713	1,572	1,775	1,897	2,061	2,208
Other health services	*3,116*	*3,054*	*3,185*	*3,368*	*3,542*	*3,711*
General administration	566	586	737	794	858	887
Health assistance to the aged	257	224	247	248	264	276
Total health	**35,564**	**37,620**	**39,838**	**41,991**	**43,635**	**45,459**
Social security and welfare						
Assistance to the aged	28,094	29,776	31,704	33,685	35,619	37,647
Assistance to veterans and dependants	5,982	5,625	6,026	6,044	6,115	6,075
Assistance to people with disabilities	11,453	12,365	12,846	13,390	13,892	14,419
Assistance to families with children	25,182	26,407	27,878	28,538	29,345	29,670

Table A1: Estimates of expenses by function and sub-function (continued)

	Actuals	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Social security and welfare (continued)						
Assistance to the unemployed	5,128	4,857	5,580	6,314	7,122	7,979
Assistance to the sick	91	86	85	87	88	87
Assistance to the unemployed and the sick	*5,219*	*4,942*	*5,665*	*6,400*	*7,210*	*8,066*
Common youth allowance	2,213	2,190	2,273	2,279	2,299	2,316
Other welfare programmes	1,141	1,525	1,502	1,514	1,567	1,622
Aboriginal advancement nec	1,336	1,389	1,422	1,433	1,479	1,512
General administration	2,346	2,153	2,440	2,524	2,466	2,461
Total social security and welfare	**82,966**	**86,372**	**91,756**	**95,807**	**99,991**	**103,788**
Housing and community amenities						
Housing	1,432	1,629	1,670	1,725	1,787	1,823
Urban and regional development	192	202	209	185	138	137
Environment protection	388	491	911	1,116	706	355
Total housing and community amenities(a)	**2,012**	**2,321**	**2,790**	**3,026**	**2,631**	**2,314**
Recreation and culture						
Broadcasting	1,163	1,251	1,277	1,288	1,308	1,329
Arts and cultural heritage	692	857	868	847	830	840
Sport and recreation	196	355	269	238	216	206
National estate and parks	214	236	213	176	159	158
Total recreation and culture	**2,264**	**2,699**	**2,627**	**2,549**	**2,513**	**2,534**
Fuel and energy	**4,369**	**4,013**	**4,804**	**4,958**	**5,290**	**5,304**
Agriculture, forestry and fishing						
Wool industry	56	49	52	56	56	56
Grains industry	124	153	150	152	153	121
Dairy industry	98	111	93	85	79	55
Cattle, sheep and pig industry	130	135	146	147	147	146
Fishing, horticulture and other agriculture	188	285	490	322	245	227
General assistance not allocated to specific industries	412	414	423	403	399	367
Rural assistance	321	674	269	82	27	27
Natural resources development(a)	312	395	487	519	316	187
General administration	174	196	190	178	165	145
Total agriculture, forestry and fishing	**1,816**	**2,412**	**2,300**	**1,942**	**1,588**	**1,331**
Mining, manufacturing & construction	**1,707**	**1,847**	**2,085**	**2,030**	**2,046**	**2,038**
Transport and communication						
Communication	510	622	705	638	613	331
Rail transport	174	301	107	169	176	0
Air transport	141	175	145	126	129	130
Road transport	1,629	1,619	2,206	2,697	2,853	1,789
Sea transport	194	217	238	248	250	252
Other transport and communication	124	170	151	144	146	147
Total Transport and Communication	**2,773**	**3,104**	**3,552**	**4,023**	**4,166**	**2,649**

Table A1: Estimates of expenses by function and sub-function (continued)

	Actuals	Estimates		Projections		
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m	$m
Other economic affairs						
Tourism and area promotion	218	212	197	196	126	126
Vocational and industry training	610	650	755	796	826	850
Labour market assistance to job seekers and industry	2,168	2,058	2,278	2,253	2,201	2,230
Industrial relations	388	368	385	338	354	367
Immigration	757	905	1,043	1,029	1,032	1,057
Total labour and employment affairs	*3,922*	*3,980*	*4,461*	*4,416*	*4,414*	*4,503*
Other economic affairs nec	759	908	959	948	957	965
Total other economic affairs	**4,899**	**5,101**	**5,618**	**5,560**	**5,496**	**5,595**
Other purposes						
Interest on Australian Government's behalf	3,869	3,629	3,514	3,447	3,310	3,283
Interest on behalf of states and territories	11	1	0	0	0	0
Interest received on Australian Government stock	0	0	0	0	0	0
Public debt interest	*3,880*	*3,629*	*3,514*	*3,447*	*3,310*	*3,283*
Nominal superannuation interest	5,005	5,583	5,784	5,870	6,077	6,289
General revenue assistance - states and territories	739	975	17	18	19	20
General capital assistance - states and territories	0	0	0	0	0	0
Debt assistance	0	220	0	0	0	0
Local government assistance	1,554	1,629	1,691	1,739	1,804	1,871
Revenue assistance to the States and Territories	160	164	168	173	177	181
Assistance to other governments	551	668	740	741	624	475
General purpose inter-government transactions	*3,003*	*3,655*	*2,617*	*2,671*	*2,624*	*2,547*
Natural disaster relief	77	359	99	93	93	93
Contingency reserve(b)	12	42	747	3,611	7,303	13,099
Total other purposes	**11,977**	**13,269**	**12,761**	**15,692**	**19,408**	**25,311**
Total expenses	**195,680**	**206,018**	**219,730**	**230,556**	**240,910**	**252,592**

(a) There has been some reclassification of expenditure that was previously reported under natural resources development sub-function (agriculture, forestry and fishing) to other primary functions.
(b) Asset sale related expenses are now treated as a component of the contingency reserve.

APPENDIX B: THE 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;
- 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.

The contingency reserve also includes expenses associated with the Government's major asset sales and associated administration costs.

STATEMENT 7: ASSET AND LIABILITY MANAGEMENT

This statement previously focused on debt management. With the elimination of government net debt and a new focus on net worth, this statement now covers the management of the major assets and liabilities on the Government's balance sheet and provides detailed information on Australian Government net debt and net worth.

STATEMENT 7: ASSET AND LIABILITY MANAGEMENT

The Australian Government balance sheet provides information on the Government's assets and liabilities and provides an indication of the sustainability of government finances. Maintaining a strong balance sheet ensures the Government has the capacity and flexibility to deal with longer term fiscal pressures.

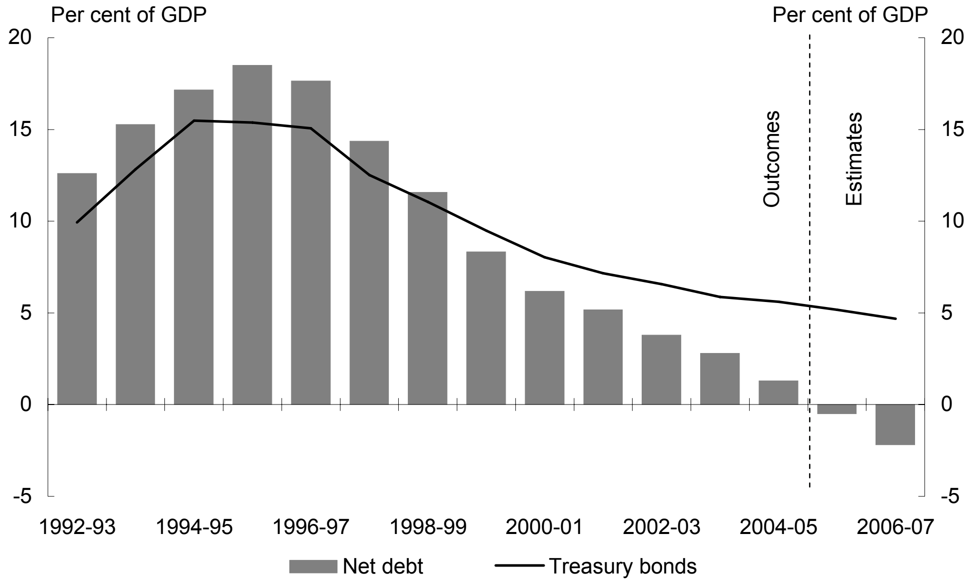
The balance sheet presents the Government's assets and liabilities, which contribute to the calculation of net debt and net worth. A detailed balance sheet for the Australian Government general government sector is provided in Appendix B of Statement 2 (Table B2).

NET DEBT AND NET WORTH

As a result of ten years of strong economic management, net debt was eliminated in April 2006 after falling from a peak of $95.8 billion (18.5 per cent of GDP) in 1995-96.

Net debt is expected to fall further below zero in 2006-07 and over the forward years. This means a build up in selected financial assets, reflecting continued budget surpluses and the assumption that the full sale of Telstra is achieved in 2006-07 (Chart 1).

Chart 1: Australian Government general government sector net debt and Treasury bonds on issue



Source: Data are from ABS cat. no. 5501.0, Australian Government Final Budget Outcomes and Treasury estimates.

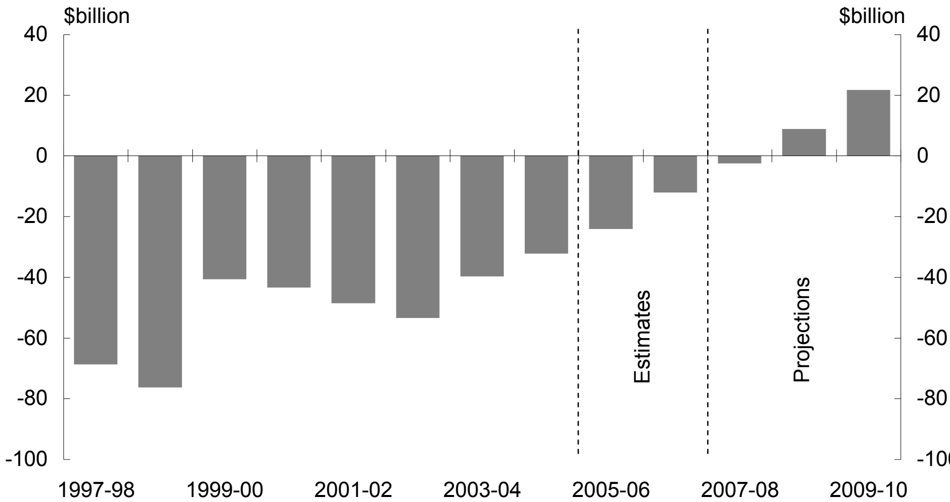
Australia's net debt position compares favourably to other industrialised countries. The ratio of Australia's total general government sector net debt to GDP is among the lowest in the OECD and is considerably less than in the United Kingdom, Japan and the United States (see Statement 1).

Net debt is a sub-set of the Government's broader financial portfolio. It includes financial liabilities such as government securities and other loans and borrowing and financial assets such as cash, deposits and other investments. Net debt is a common measure of the strength of a government's fiscal position and performance.

Net worth is a broader measure of the Government's overall financial position which incorporates the Government's non-financial assets, such as land and other fixed assets, as well as certain financial assets and liabilities not included in net debt, most notably accrued employee superannuation liabilities.

Australian Government general government sector net worth is expected to strengthen over the forward estimates with the establishment of the Future Fund. It is projected that by 2008-09 the Australian Government will have positive net worth (Chart 2).

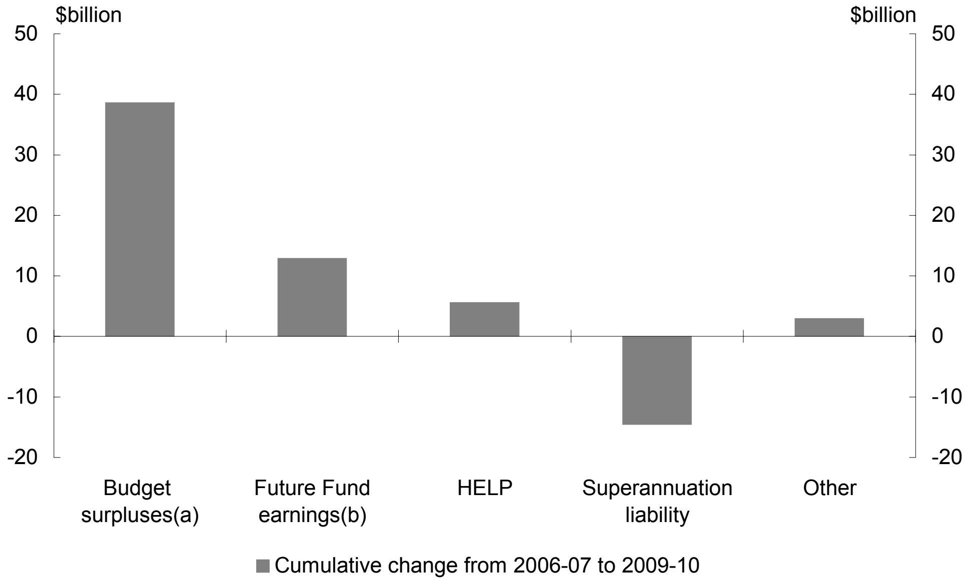
Chart 2: Australian Government general government net worth



Source: Data are from ABS cat. no. 5501.0, Australian Government Final Budget Outcomes and Treasury estimates.

The improvement in net worth is primarily driven by growth in budget surpluses, higher returns on investments in the Future Fund and increases in loans provided by the Higher Education Loans Program (HELP). These factors significantly outweigh growth in the Government's unfunded superannuation liability (Chart 3).

Chart 3: Contributions to net worth over the forward estimates



(a) Budget surpluses are assumed to reflect term deposits at the Reserve Bank of Australia.
(b) The transfer of seed capital and Telstra sale proceeds are excluded as they are financing transactions that do not impact on net worth.
Source: Treasury estimates.

The positive outlook for net worth and net debt means the Government is well placed to deal with future emerging fiscal pressures.

ASSET MANAGEMENT

The Australian Government holds a wide range of assets including investments in the Future Fund, term deposits at the Reserve Bank of Australia, higher education loans and non-financial assets such as land and buildings. Strong fiscal outcomes over recent years have contributed to both an increase in financial assets and Australian Government net worth.

The establishment of the Future Fund and possible sale of the Government's remaining share in Telstra in 2006-07 will have an impact on the size and composition of Australian Government assets.

Future Fund

The Australian Government established the Future Fund in 2005-06 with seed capital of $18 billion. The aim of the Future Fund is to fully offset the Government's unfunded public sector superannuation liabilities by around 2020, thereby allowing the budget to cater for the increased fiscal pressures arising from the ageing of the population.

The Future Fund will be invested in a broad range of financial assets and be managed by an independent statutory agency governed by an appropriately qualified board — the Future Fund Board of Guardians (the Board). Further contributions to the Future Fund will be made from future realised budget surpluses and asset sales.

The investment strategy adopted by the Board will have an impact on the Government's balance sheet. The recently appointed Board has not yet developed an investment strategy for the Future Fund, so standardised assumptions have been made about asset returns for the purposes of this budget, with assets invested in term deposits in the short term and progressively being invested in equities over the forward estimates. The actual impact on the forward estimates will depend on the investment strategy adopted by the Board.

Assuming the Board has a diversified holding of financial assets, net debt will be affected during the transition from the short to long term. This is because some of the Government's holdings of cash and fixed-interest securities will be converted into equities, which are not included in the calculation of net debt. Beyond the forward estimates period, the Future Fund is expected to contribute to improved net debt, largely due to compound growth from fixed interest and cash holdings within the overall asset portfolio.

Net worth over the forward estimates is likely to improve due to the establishment of the Future Fund. While transfers of funds between asset classes have no impact on net worth, the Future Fund is expected to improve net worth beyond the forward estimates due to an expectation of higher average returns through the Future Fund than under current arrangements.

Telstra

The budget estimates have been constructed assuming the full sale of the Government's remaining shares in Telstra in 2006-07. The estimates also assume that the sale proceeds will be transferred to the Future Fund. However, the Government has not made final decisions in relation to the sale, including the structure of the sale, the nature of securities to be sold, or the quantity of shares to be sold. The structure that is ultimately adopted may vary depending on market circumstances and expert advice provided at the time.

LIABILITY MANAGEMENT

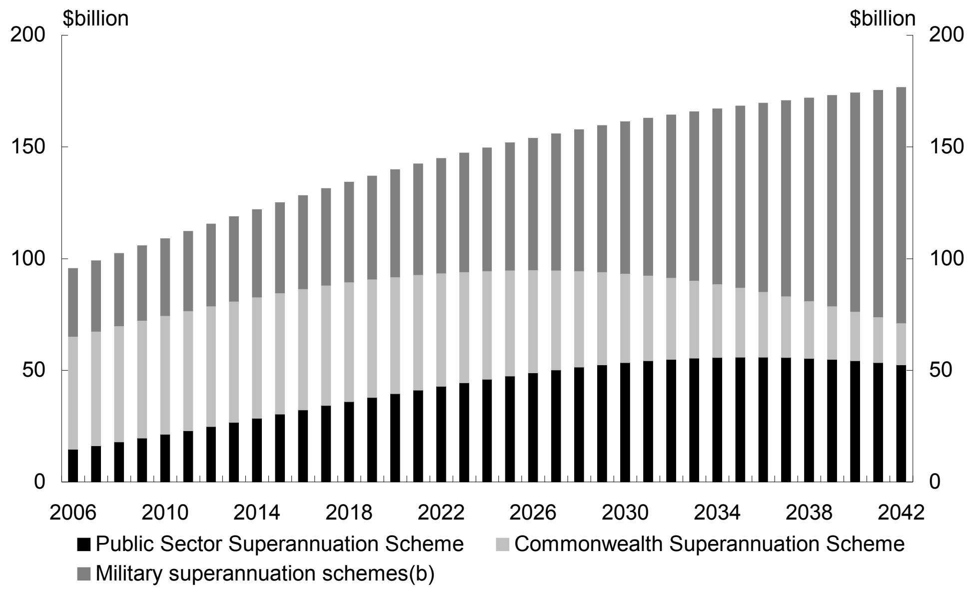
The major liabilities on the Australian Government's balance sheet are the Government's superannuation liability for public sector employees and government debt securities. In 2006-07, these liabilities are estimated to comprise more than three quarters of total Australian Government liabilities.

Public sector employee superannuation liabilities

Public sector employee superannuation entitlements are the largest financial liability on the Government's balance sheet. This liability relates to past and current public sector employees. It is currently valued at around $96 billion and is estimated to grow to around $140 billion by 2020.

The Australian Government has never fully funded its superannuation liability. However, in 1990 and 2005 the Australian Government closed the main civilian superannuation schemes to new members. From 2005 the Government began paying the superannuation liability for new civilians employed as they accrue, rather than growing the superannuation liability further. Funding employee superannuation entitlements as they accrue contributes to improved net worth over the medium term. Despite this, the existing superannuation liability is expected to continue to grow, largely due to growth in the military superannuation schemes and continued growth of entitlements accruing to existing members of the closed civilian schemes (Chart 4).

Chart 4: Public sector superannuation liability[(a)]



(a) The Public Sector Superannuation Scheme and the Commonwealth Superannuation Scheme (the main civilian schemes) and Military superannuation schemes form the dominant part of the Government's total unfunded superannuation liability.
(b) Includes the Military Superannuation and Benefits Scheme and the Defence Force Retirement and Death Benefits Scheme.
Source: Australian Government Actuary.

Further, the Government successfully negotiated the extinguishment of its liability with respect to Telstra and Australia Post superannuation in 2004. More recently, the Government has made an offer to the South Australian and Tasmanian Governments to extinguish the Australian Government's liability in respect of superannuation entitlements of former State Rail employees. Combined with the establishment of the

Future Fund, these initiatives are expected to reduce calls on the budget at a time when significant intergenerational pressures are likely to emerge.

Government securities — issuance in 2005-06 and 2006-07

In line with the public review of the Commonwealth Government Securities market in 2002-03, the Government will continue to issue debt, despite a strong fiscal position, in order to maintain liquid and efficient Treasury bond and Treasury bond futures markets.

Accordingly, the volume and timing of Treasury bond issuance takes account of the need to have an appropriate range of Treasury bonds available for inclusion in Treasury bond futures baskets. The programme maintains a pattern where new 5-year and 13-year Treasury bonds are launched in alternate years, with total issuance over two years of around $5 billion in each line.

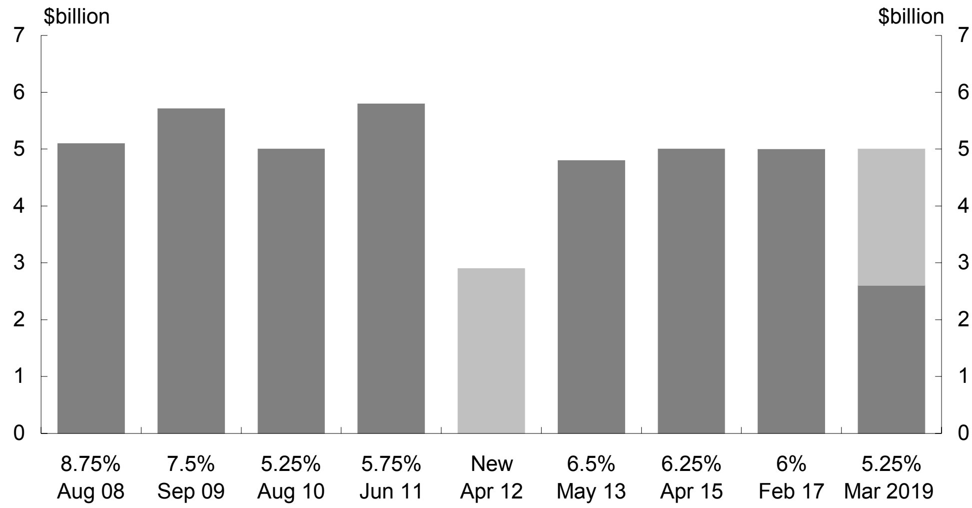
In 2005-06 one new stock was launched — the March 2019 Treasury bond. Issuance into this bond line commenced in January 2006 and is expected to reach $2.6 billion in the period remaining to 30 June 2006. Issuance in 2005-06 was also directed at building up the August 2010 and the February 2017 bond lines. The volumes on issue for both of these bond lines are now at their $5 billion target.

In the first half of 2006-07, issuance will be directed to building up the March 2019 Treasury bond. An additional $2.4 billion will be issued to bring the total volume on issue for this bond line to $5 billion by November 2006.

In December 2006, a new 5-year Treasury bond, an April 2012 bond line, will be issued to support the operation of the 3-year Treasury bond futures contract. It is planned that $2.9 billion of this bond will be issued during 2006-07. The remaining issuance necessary to bring this bond line up to $5 billion will be undertaken in the first half of 2007-08.

Total Treasury bond issuance during 2006-07 will be $5.3 billion, while scheduled maturities during this period, net of Australian Government holdings, are $6.1 billion. As a result, the total stock of Treasury bonds on issue, net of Australian Government holdings, will be around $47.3 billion as at 30 June 2007 (Chart 5).

Chart 5: Benchmark Treasury bonds outstanding expected at 30 June 2007[(a)]



(a) Treasury bonds on issue are net of Australian Government holdings. The October 2007 Treasury bond is excluded from the chart as it is not considered a benchmark bond line.
Note: The dark grey columns represent bonds outstanding at the beginning of the 2006-07 financial year. The light grey columns indicate new issuance in 2006-07.
Source: Australian Office of Financial Management and Treasury estimates.

STATEMENT 8: FINANCIAL REPORTING STANDARDS AND BUDGET CONCEPTS

This statement describes the financial accounting frameworks relevant to the Australian Government.

STATEMENT 8: FINANCIAL REPORTING STANDARDS AND BUDGET CONCEPTS

The *Charter of Budget Honesty Act 1998* requires that the budget be based on external reporting standards. Accordingly, the major external standards used in the budget are the Australian Bureau of Statistics' (ABS) accrual Government Finance Statistics (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 major fiscal aggregates (including the fiscal and underlying cash balances) are based on the accrual GFS framework.

The Charter also requires that departures from applicable external reporting standards be identified. These are disclosed in Appendix A to Statement 2, the introduction to Statement 9, and Note 1 in Statement 10.

ACCRUAL GFS FRAMEWORK

The GFS reporting framework is a specialised accounting and financial reporting system designed to support economic analysis of the public sector. It allows comprehensive assessments to be made of the economic impact of government and is consistent with international statistical standards (the *System of National Accounts 1993* (SNA93) and the International Monetary Fund's (IMF) *Government Finance Statistics Manual 2001*).[1]

The GFS conceptual framework is divided into a number of separate statements, each of which draws out analytical aggregates or balances of particular economic significance. Together, these aggregates provide for a thorough understanding of the financial position of the public sector. The GFS statements reported in the budget are the operating statement, balance sheet, cash flow statement and statement of other economic flows.

All GFS data are recorded as either stocks (assets and liabilities) or flows (classified as either transactions or other economic flows).

A transaction results from a mutually agreed interaction between economic entities. Despite their compulsory nature, taxes are transactions deemed to occur by mutual agreement between the government and the taxpayer. Transactions that increase or

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1 Additional information on the Australian accrual GFS framework is available in the ABS publication *Australian System of Government Finance Statistics: Concepts, Sources and Methods*, 2005 (cat. no. 5514.0).

decrease net worth (assets minus liabilities) are reported as revenues and expenses respectively in the operating statement.[2]

A change to the value or volume of an asset or liability that does not result from a transaction is an other economic flow. This can include changes in values from market prices, most actuarial valuations and exchange rates and changes in volumes from discoveries, depletion and destruction. All other economic flows are reported in the statement of other economic flows.

Under the accrual GFS framework, flows are recorded in the period in which they occurred. As a result, prior period outcomes may be revised where information arises that could reasonably be expected to have been known in the past, is material in at least one of the affected periods and can be reliably assigned to the relevant period(s).

GFS financial statements are contained in Statements 2 and 9.

Operating statement

The operating statement presents details of transactions in GFS revenues, GFS expenses and the net acquisition of non-financial assets (net capital investment) for an accounting period.

GFS revenues arise from transactions that increase net worth and GFS expenses arise from transactions that decrease net worth. GFS revenues less GFS expenses gives the GFS net operating balance. The net operating balance is comparable to the National Accounts concept of government saving plus capital transfers.

The net acquisition of non-financial assets (net capital investment) measures the change in the Australian Government's stock of non-financial assets due to transactions. As such, it measures the net effect of purchases, sales and consumption (for example, depreciation of fixed assets and use of inventory) of non-financial assets during an accounting period.

Net acquisition of non-financial assets equals gross fixed capital formation, less depreciation, plus changes (investment) in inventories, plus other transactions in non-financial assets.

Fiscal balance

The fiscal balance (or GFS net lending/borrowing) is the net operating balance less net capital investment. Thus, fiscal balance includes the impact of net expenditure

2 Not all transactions impact on net worth. For example, transactions in financial assets and liabilities do not impact on net worth as they represent the swapping of assets and liabilities on the balance sheet.

(effectively purchases less sales) on non-financial assets rather than consumption (depreciation) of non-financial assets.[3]

The fiscal balance measures the Australian Government's investment-saving balance. It measures in accrual terms the gap between government savings plus net capital transfers, and investment in non-financial assets. As such, it approximates the contribution of the Australian Government general government sector to the balance on the current account in the balance of payments.

Balance sheet

The balance sheet shows stocks of assets, liabilities and GFS net worth. Net debt is also reported in the balance sheet.

Net debt

Net debt is the sum of selected financial liabilities (deposits held, advances received, government securities, loans, and other borrowing) less the sum of selected financial assets (cash and deposits, advances paid, and investments, loans and placements). Net debt does not include superannuation or superannuation related liabilities. Net debt is a common measure of the strength of a government's financial position. High levels of net debt impose a call on future revenue flows to service that debt.

Net worth

The net worth of the general government sector is defined as assets less liabilities. For the public financial corporations and public non-financial corporations sectors, net worth is defined as assets less liabilities less shares and other contributed capital. Net worth is an economic measure of wealth, reflecting the Australian Government's contribution to the wealth of Australia.

Cash flow statement

The cash flow statement identifies how cash is generated and applied in a single accounting period. The cash flow statement reflects a cash basis of recording (rather than an accrual basis) where information is derived indirectly from underlying accrual transactions and movements in balances. This, in effect, means that transactions are captured when cash is received or when cash payments are made. Cash transactions are specifically identified because cash management is considered an integral function of accrual budgeting.

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3 The net operating balance includes consumption of non-financial assets because depreciation is a GFS expense. Depreciation also forms part of net capital investment, which (in the calculation of fiscal balance) offsets the inclusion of depreciation in the net operating balance.

Underlying cash balance

The underlying cash balance plus Future Fund earnings (GFS cash surplus/deficit) is the cash counterpart of the fiscal balance, reflecting the Australian Government's cash investment-saving balance. This measure is conceptually equivalent under the current accrual framework and the previous cash framework. For the general government sector, the underlying cash balance is calculated as shown below.

Net cash flows from operating activities

plus

Net cash flows from investments in non-financial assets

less

Net acquisitions of assets acquired under finance leases and similar arrangements[4]

equals

GFS cash surplus/deficit

less

Future Fund earnings

equals

Underlying cash balance

The Government is reporting the underlying cash balance net of Future Fund earnings from 2005-06 onwards because the earnings will be reinvested to meet future superannuation payments and are therefore not available for current spending. However, Future Fund earnings are included in the fiscal balance because superannuation expenses relating to future cash payments are recorded in the fiscal balance estimates.

Expected Future Fund earnings are separately identified in the Australian Government cash flow statement in Table B3, Statement 2 and Table 3, Statement 9.

Headline cash balance

The headline cash balance is calculated by adding cash flows from investments in financial assets for policy purposes and Future Fund earnings to the underlying cash balance.

4 The underlying cash balance treats the acquisition and disposal of non-financial assets in the same manner regardless of whether they occur by purchase/sale or finance lease — acquisitions reduce the underlying cash balance and disposals increase the underlying cash balance. However, finance leases do not generate cash flows at the time of acquisition or disposal equivalent to the value of the asset. As such, net acquisitions of assets under finance leases are not shown in the body of the cash flow statement but are reported as a supplementary item for the calculation of the underlying cash balance.

Cash flows from investments in financial assets for policy purposes include equity transactions and net advances.[5] Equity transactions include equity injections into controlled businesses and privatisations of government businesses. Net advances include net loans to the States, net loans to students under the Higher Education Loan Programme (HELP), and contributions to international organisations that increase the Australian Government's financial assets.

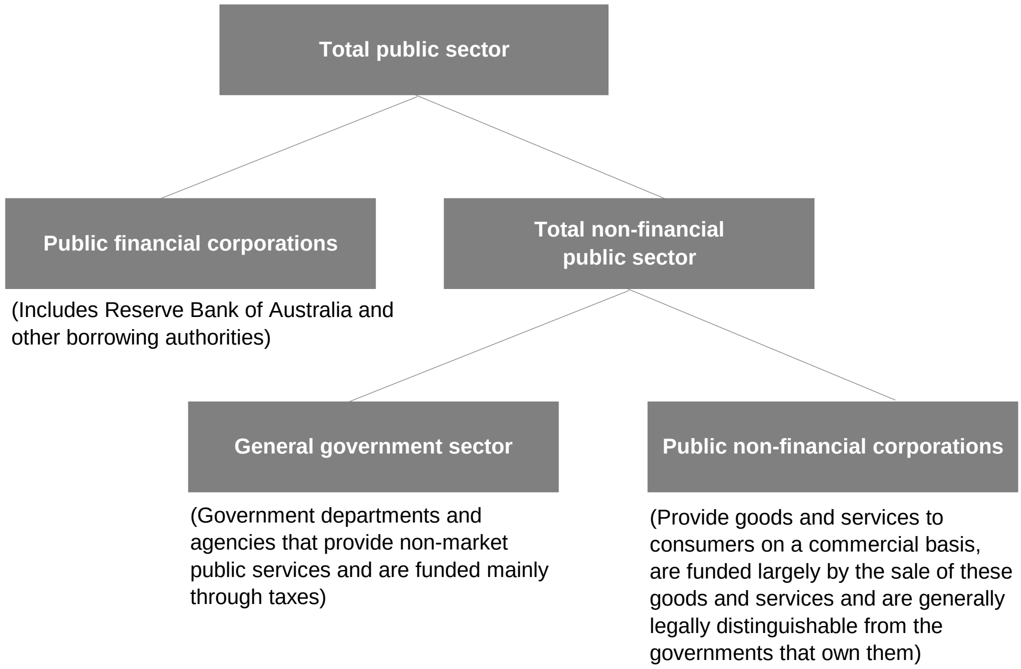
Statement of other economic flows (reconciliation of net worth)

The statement of other economic flows outlines changes in net worth driven by economic flows other than GFS revenues and GFS expenses. GFS revenues, GFS expenses and other economic flows sum to the total change in net worth during a period. The majority of other economic flows for the Australian Government general government sector arise from price movements in its assets and liabilities.

Sectoral classifications

To assist in analysing the public sector, GFS data are presented by institutional sector. GFS distinguishes between the general government sector, the public non-financial corporations sector and the public financial corporations sector, as shown in Figure 1.

Figure 1: Institutional structure of the public sector



5 Cash flows from investments in financial assets for policy purposes were called net advances under the cash budgeting framework.

Budget reporting focuses on the general government sector. The general government sector provides public services that are mainly non-market in nature, and for the collective consumption of the community, or involve the transfer or redistribution of income. These services are largely financed through taxes and other compulsory levies, although user charging and external funding have increased in recent years. This sector comprises all government departments, offices and some other bodies.

In preparing financial statements for the sectors all material transactions and balances between entities within the sectors are eliminated.

AUSTRALIAN ACCOUNTING STANDARD REPORTING FRAMEWORK

The AAS reporting framework, being the AEIFRS and AAS 31, requires the preparation of accrual-based general purpose financial reports, showing government assets, liabilities, income, expenses and cash flows. Reporting under this framework is intended to provide a consolidated overview of the financial performance and financial position of government.

There are four main general purpose statements that must be prepared in accordance with the AAS framework. These are:

- an income statement, which includes an operating result;
- a balance sheet, which shows net assets;
- a statement of changes in equity, which shows movements in equity; and
- a cash flow statement, which includes the net increase/decrease in cash held.

In addition to these general purpose statements, notes to the financial statements are required. These notes include a summary of accounting policies, disaggregated information and other disclosures required by AAS.

A full set of financial statements for the general government sector, with notes showing disaggregated information can be found in Statement 10.

RECONCILIATION OF GFS AND AAS AGGREGATES

There is a general consistency of treatment of the elements of financial statements between GFS and AAS. Both frameworks are based on the concept of economic events that give rise to stocks and flows. As a result, the definitions of stocks are broadly similar under the two frameworks and relate to the control of economic benefits, while flows are defined with reference to changes in stocks.

The GFS and AAS definitions of the scope of the public sector agree in almost all cases, with AAS 31 recommending the same segmentation of the public sector into general government, public non-financial corporations and public financial corporations sectors.

Transactions are generally treated in a similar manner by GFS and AAS; however, where GFS is a framework designed to facilitate macro-economic analysis, AAS is designed for general purpose financial reporting. The different objectives of the two systems lead to some variation in the treatment of certain items. This differing treatment relates predominantly to the definitions of revenues and expenses under the two frameworks.

In particular, revaluations of assets and liabilities are classified differently under the AAS and GFS standards. Major revaluations include write-downs of bad and doubtful debts (excluding those that are mutually agreed), changes in the valuation of superannuation liabilities, and gains and losses due to changes in foreign exchange rates and interest rates.

Under AAS reporting, valuation changes may affect income or expenses and therefore the operating result. However, under GFS reporting, revaluations are not considered to be transactions (that is, they are considered to be other economic flows) and accordingly do not form part of revenues or expenses. Therefore, most revaluations are not taken into account in the calculation of the GFS net operating balance or fiscal balance. However, revaluations still impact on GFS assets and liabilities, as can be seen in the statement of other economic flows.

Some of the major differences between the GFS and AAS treatments of transactions are outlined in Table 1. Further information on the differences between the two systems is provided in the ABS publication *Australian System of Government Finance Statistics: Concepts, Sources and Methods, 2005* (cat. no. 5514.0).

Table 1: Selected differences between AAS and GFS reporting standards

Issue	AAS treatment	GFS treatment
Asset write-downs	Treated as part of operating expenses.	Treated as revaluations (other economic flows), except for mutually agreed write-downs, and therefore not included in expenses.
Gains and losses on assets	Treated as part of operating income/expenses.	Treated as revaluations (other economic flows) and therefore not included in revenues/expenses.
Provisions for bad and doubtful debts	Treated as part of operating expenses and included in the balance sheet as an offset to assets.	Act of creating provisions is not considered an economic event and is therefore not considered an expense or included in the balance sheet. The Australian Government departs from this latter requirement (see Appendix A to Statement 2).
Interest flows related to swaps and other financial derivatives	Treated as operating income and expenses.	Treated as other economic flows and so not included in revenues and expenses.
Acquisition of defence weapons platforms	Treated as capital expenditure. Defence weapons platforms appear as an asset on the balance sheet. Depreciation expense on assets is recorded in the operating statement.	Treated as an expense at the time of acquisition. Defence weapons platforms do not appear as an asset on the balance sheet and no depreciation is recorded in the operating statement.
Valuation of assets and liabilities	Classes of assets and liabilities are measured using a range of methods. The predominant methods for valuing different asset classes include historic cost and market value.	Individual assets and liabilities are measured at current market value based on current market prices or a suitable proxy where market prices are not available.
Finance leases	Treats finance leases as if an asset were purchased from borrowings. That is, the lease payment is split into an interest component (which is shown as an operating expense) and a principal component. The asset and the liability are recorded on the balance sheet. This convention does not apply to the cash flow statement, which does not record the acquisition of the asset or the liability.	As per the accounting standard, except that the GFS cash flow statement includes the acquisition of the asset as a supplementary item for the calculation of the surplus/deficit and underlying cash balance.

The Australian Accounting Standards Board is currently drafting an AAS for financial reporting by general government sectors. This standard seeks to harmonise AAS and GFS and will involve changes to the presentation of government financial information. The standard should be finalised for the 2007-08 Budget.

Table 2 reconciles GFS revenue and expenses with their AAS counterparts.

Table 2: Reconciliation of GFS and AAS revenue and expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
GFS revenue (Statement 9)	**260,724**	**271,662**	**282,881**	**296,518**	**312,273**
less GST revenue for States and Territories	37,860	40,000	42,210	44,440	46,670
GFS revenue (Statement 2)	**222,864**	**231,662**	**240,671**	**252,078**	**265,603**
plus asset revenue recognised for the first time	258	226	218	119	130
plus foreign exchange gains	85	0	0	0	0
plus other economic revaluations	473	-27	-109	-215	-259
plus proceeds from the sale of assets	122	15	1,399	1,515	1,607
plus swap interest revenue	1,984	1,721	1,448	1,085	825
AAS income (Statement 10)	**225,786**	**233,597**	**243,628**	**254,583**	**267,905**
GFS expenses (Statement 9)	**243,328**	**259,080**	**272,091**	**284,635**	**298,522**
less GST grants to States andTerritories	37,100	39,130	41,300	43,480	45,670
less GST mutually agreed writedowns	210	220	235	245	260
GFS expenses (Statement 2)	**206,018**	**219,730**	**230,556**	**240,910**	**252,592**
plus actuarial revaluations	321	0	0	0	0
plus net writedown of assets/bad and doubtful debts	2,372	2,306	2,322	1,984	2,169
plus foreign exchange losses	0	1	0	0	0
plus other economic adjustments	-360	-360	-370	-380	-393
plus value of assets sold	0	-249	0	0	0
plus swap interest expense	1,846	1,610	1,361	1,012	766
plus defence weapons platforms depreciation	2,513	2,686	2,738	2,740	2,597
less defence weapons platforms investment	3,321	4,623	4,370	4,410	4,770
plus AusAid IDA/ADF expenses	0	0	260	233	233
plus ETM adjustment for expenses	0	0	0	0	0
AAS expenses (Statement 10)	**209,388**	**221,101**	**232,498**	**242,089**	**253,195**

Table 3 reconciles the AAS operating result to the GFS net operating balance and the fiscal balance (GFS net lending).

The AAS operating result is equal to AAS income less expenses. Similarly, GFS revenues less expenses equal the GFS net operating balance. Consequently, the reconciliation between the AAS operating result before extraordinary items and the GFS net operating balance relates directly to differences in the definitions of revenues and expenses which are shown in Table 2.

The second part of the Table 3 reconciliation shows the adjustment for net capital investment required to derive the fiscal balance from the GFS net operating balance.

As discussed previously, the fiscal balance is calculated as the net operating balance less net capital investment. This is a useful economic indicator as it represents the gap between government saving (less capital transfers) and investment, and so is included at the end of the GFS operating statement. In AAS there is no equivalent measure to the fiscal balance. That is, the AAS income statement stops at the operating result and includes no information on net capital investment.

Table 3: Reconciliation of AAS net operating result and fiscal balance

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
AAS operating result before extraordinary items (Statement 10)	**16,397**	**12,496**	**11,130**	**12,494**	**14,711**
Net differences from revenue and expense definitions	999	86	-340	-611	-960
GFS net operating balance (Statement 9)	**17,397**	**12,583**	**10,790**	**11,883**	**13,750**
less purchase of property, plant and equipment and intangibles	6,169	7,917	7,044	7,096	7,412
less assets acquired under finance leases	12	23	6	325	6
less other non-financial assets	138	199	23	122	-63
less increase in inventories	148	521	91	88	68
plus defence weapons platforms investment	3,321	4,623	4,370	4,410	4,770
plus proceeds from sales of property, plant and equipment and intangibles	224	152	233	155	122
plus depreciation and amortisation	4,554	4,930	5,123	5,205	5,089
less weapons depreciation	2,513	2,686	2,738	2,740	2,597
Fiscal balance (GFS net lending) (Statement 9)(a)	**16,516**	**10,940**	**10,615**	**11,281**	**13,712**
Impact of GST	-550	-650	-675	-715	-740
Fiscal balance (GFS net lending) (Statement 2)(a)	**15,966**	**10,290**	**9,940**	**10,566**	**12,972**

(a) The fiscal balance estimates in Statement 9 are higher than those presented in Statement 2, as explained in the introduction to Statement 9.

STATEMENT 9: GOVERNMENT FINANCE STATISTICS STATEMENTS

The financial tables presented in this statement are prepared in accordance with the Australian Bureau of Statistics (ABS) accrual Government Finance Statistics (GFS) framework.

The Australian, State and Territory governments have an agreed framework — the *Accrual Uniform Presentation Framework* — for the presentation of government financial information on a basis consistent with the ABS GFS publication. This statement presents Australian Government data on an ABS GFS basis, as required by the *Accrual Uniform Presentation Framework*, except for the departures (other than in relation to the treatment of goods and services tax (GST)) detailed in Appendix A to Statement 2.

In accordance with *Accrual Uniform Presentation Framework* requirements, this statement also contains an update of the Australian Government's Loan Council Allocation.

STATEMENT 9: GOVERNMENT FINANCE STATISTICS STATEMENTS

Financial tables presented in this statement are prepared in accordance with the Australian Bureau of Statistics' (ABS) accrual Government Finance Statistics (GFS) framework.

The tables include an operating statement, balance sheet and cash flow statement for the Australian Government general government, public non-financial corporations and total non-financial public sectors. A statement of other economic flows is also included for the Australian Government general government sector.

The Australian, State and Territory governments have an agreed framework — the *Accrual Uniform Presentation Framework* — for the presentation of government financial information on a basis consistent with the ABS GFS publication. This statement presents Australian Government data on an ABS GFS basis, as required by the *Accrual Uniform Presentation Framework*, except for the departures (other than in relation to the treatment of goods and services tax (GST)) detailed in Appendix A to Statement 2.

The only difference between the Australian Government general government sector statements in Statement 2 and this statement is the treatment of the GST. The clear policy intent of the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations* is that GST is collected by the Australian Taxation Office, as an agent for the States and Territories (the States), and appropriated to the States. Consequently, it is not shown as Australian Government revenue in other parts of this document. However, the tables in this statement show GST as taxation revenue and payments to the States as grant expenses.

As a result of the different treatments of GST related transactions, fiscal balance, net operating balance and net worth estimates in this statement differ from those reported elsewhere in this document. This difference represents the effect of GST revenue accrued but not yet received and, therefore, not yet paid or payable to the States (as GST obligations to the States are on a cash basis).[1] The cash flows presented in this statement include GST (except in respect to GST flows internal to the general government sector), whereas the cash flows presented elsewhere in this document do not. The GFS cash surplus/deficit is not affected and provides identical results under both treatments of GST receipts.

Transactions between the Australian Government general government and public non-financial corporations sectors are included in the relevant tables, but removed

1 Table 3 in Statement 8 shows the difference in the net operating and fiscal balance estimates resulting from the two treatments. The change in expenses when moving between the two GFS presentations of the estimates is less than the change in revenue.

from the total non-financial public sector tables as they are transactions internal to that sector.

Public access communication assets, computer software and other intangibles are recorded at historic costs, as market value information, or suitable proxies for market value, are not readily observable. This affects the public non-financial corporations sector balance sheet, but does not affect the general government sector balance sheet.

Statement 8 provides reconciliations between key GFS aggregates and their Australian Accounting Standards counterparts.

In accordance with *Accrual Uniform Presentation Framework* requirements, this Statement also contains an update of the Australian Government's Loan Council Allocation.

GOVERNMENT FINANCE STATISTICS STATEMENTS

Table 1: Australian Government general government sector operating statement

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
GFS revenue					
Taxation revenue	245,945	257,157	268,286	281,181	296,122
Current grants and subsidies	0	0	0	0	0
Sales of goods and services	4,898	4,846	4,975	5,114	5,255
Interest income	2,386	3,717	3,457	4,005	4,647
Dividend income	4,321	2,701	2,866	3,058	3,228
Other	3,173	3,241	3,297	3,160	3,021
Total GFS revenue	**260,724**	**271,662**	**282,881**	**296,518**	**312,273**
GFS expenses					
Gross operating expenses					
Depreciation	2,041	2,243	2,385	2,465	2,492
Superannuation	2,472	2,551	2,600	2,690	2,783
Salaries and wages	12,627	13,715	13,822	13,941	14,266
Payment for supply of goods and services	49,126	53,857	55,340	56,653	59,115
Other operating expenses	2,106	2,632	2,717	2,926	3,006
Total gross operating expenses	*68,372*	*74,998*	*76,864*	*78,675*	*81,663*
Nominal superannuation interest expense	5,583	5,784	5,870	6,077	6,289
Other interest expenses	4,084	3,900	3,833	3,678	3,634
Other property expenses	0	0	0	0	0
Current transfers					
Grant expenses	77,364	81,141	85,503	89,048	92,205
Subsidy expenses	6,343	7,268	7,523	7,953	7,870
Personal benefit payments in cash	77,332	81,108	87,303	93,684	102,261
Other current transfers	0	0	0	0	0
Total current transfers	*161,038*	*169,517*	*180,330*	*190,685*	*202,337*
Capital transfers	4,250	4,881	5,195	5,520	4,600
Total GFS expenses	**243,328**	**259,080**	**272,091**	**284,635**	**298,522**
Net operating balance(a)	**17,397**	**12,583**	**10,790**	**11,883**	**13,750**
Net acquisition of non-financial assets					
Purchases of non-financial assets	2,860	3,317	2,679	3,012	2,648
less Sales of non-financial assets	203	152	233	155	122
less Depreciation	2,041	2,243	2,385	2,465	2,492
plus Change in inventories	148	521	91	88	68
plus Other movements in non-financial assets	117	199	23	122	-63
Total net acquisition of non-financial assets	**881**	**1,642**	**174**	**602**	**38**
Net lending/fiscal balance(a)(b)	**16,516**	**10,940**	**10,615**	**11,281**	**13,712**

(a) The fiscal balance and net operating balance estimates in this table differ from those presented elsewhere in the Budget reflecting the treatment of the GST as an Australian Government tax.
(b) The term fiscal balance is not used by the ABS.

Table 2: Australian Government general government sector balance sheet appendix

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
GFS assets					
Financial assets					
Cash and deposits	1,785	1,242	1,801	2,870	3,262
Advances paid	21,471	22,941	24,626	26,410	28,259
Investments, loans and placements(a)	47,042	62,241	64,468	74,053	83,992
Other non-equity assets	22,470	23,073	23,662	24,361	26,060
Equity(a)	43,535	40,652	51,894	54,379	57,101
Total financial assets	*136,303*	*150,148*	*166,450*	*182,073*	*198,674*
Non-financial assets					
Land	6,089	6,112	6,099	6,069	5,991
Buildings	13,469	13,875	13,689	14,152	14,649
Plant, equipment and infrastructure	8,595	9,063	9,091	9,056	8,874
Inventories	4,625	5,146	5,236	5,324	5,392
Heritage and cultural assets	7,723	7,753	7,767	7,777	7,795
Other non-financial assets	3,361	3,546	3,694	3,825	3,572
Total non-financial assets	*43,861*	*45,493*	*45,575*	*46,204*	*46,273*
Total GFS assets	**180,164**	**195,641**	**212,026**	**228,277**	**244,947**
GFS liabilities					
Deposits held	405	405	405	405	405
Advances received	0	0	0	0	0
Government securities(a)	59,547	58,356	60,164	60,237	59,428
Loans	5,264	5,293	5,318	5,008	4,994
Other borrowing	297	296	265	542	501
Superannuation liability	95,947	99,597	103,171	106,814	110,512
Other employee entitlements and provisions	8,001	8,207	8,372	8,599	8,878
Other non-equity liabilities	32,470	32,883	33,698	34,546	34,867
Total GFS liabilities	**201,932**	**205,035**	**211,392**	**216,151**	**219,586**
Net worth(b)(c)	**-21,768**	**-9,393**	**634**	**12,126**	**25,361**
Net financial worth(d)	-65,629	-54,887	-44,942	-34,078	-20,912
Net debt(e)(f)	-4,784	-22,075	-24,743	-37,140	-50,184

(a) Equity includes the valuation of the Telstra shareholding in 2005-06, which is valued at the average of the daily share price over a 90-day period.
(b) The net worth estimates in this table differ from those presented elsewhere in the budget reflecting the treatment of GST as an Australian Government tax.
(c) Net worth is calculated as total assets minus total liabilities.
(d) Net financial worth equals total financial assets minus total liabilities. That is, it excludes non-financial assets.
(e) 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.
(f) Includes the impact of the further sale of the Australian Government's shareholding in Telstra and the establishment of the Future Fund. It is assumed that the Future Fund is initially invested in term deposits but will increasingly be invested in equities until it reaches a portfolio equity allocation consistent with the benchmark return specified in the Government's investment mandate.

Table 3: Australian Government general government sector cash flow statement[(a)]

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Cash receipts from operating activities					
Taxes received(b)	241,499	252,308	263,269	275,963	290,727
Receipts from sales of goods and services(c)	5,010	4,832	4,947	5,103	5,233
Grants and subsidies received	0	0	0	0	0
Interest receipts	2,275	3,498	3,316	3,787	4,379
Dividends	4,341	3,000	2,866	3,058	3,228
GST input credits received by general government(c)	0	0	0	0	0
Other receipts	2,928	2,944	3,003	2,893	2,723
Total operating receipts	**256,053**	**266,582**	**277,401**	**290,804**	**306,290**
Cash payments for operating activities					
Payments for goods and services(c)	-48,712	-54,480	-55,376	-56,643	-59,099
Grants and subsidies paid(d)	-88,635	-91,182	-95,627	-99,154	-102,598
Interest paid	-4,810	-3,950	-3,619	-3,544	-3,451
Personal benefit payments	-76,343	-80,168	-86,472	-93,328	-102,072
Salaries, wages and other entitlements	-17,606	-18,437	-18,695	-19,049	-19,573
GST payments by general government to taxation authority(c)	0	0	0	0	0
Other payments for operating activities	-2,332	-2,406	-2,533	-2,774	-2,750
Total operating payments	**-238,438**	**-250,623**	**-262,322**	**-274,492**	**-289,543**
Net cash flows from operating activities	**17,614**	**15,959**	**15,080**	**16,312**	**16,747**
Cash flows from investments in non-financial assets					
Sales of non-financial assets	224	154	233	155	122
Purchases of non-financial assets	-2,939	-3,496	-2,695	-2,808	-2,577
Net cash flows from investments in non-financial assets	**-2,715**	**-3,342**	**-2,462**	**-2,652**	**-2,456**
Net cash flows from investments in financial assets for policy purposes	**-1,390**	**24,869**	**-1,923**	**-1,976**	**-2,028**
Cash flows from investments in financial assets for liquidity purposes					
Increase in investments	-12,346	-37,424	-12,144	-10,620	-11,092
Net cash flows from investments in financial assets for liquidity purposes	**-12,346**	**-37,424**	**-12,144**	**-10,620**	**-11,092**
Cash flows from financing activities					
Advances received (net)	0	0	0	0	0
Borrowing (net)	-1,754	-838	2,114	29	-684
Deposits received (net)	0	0	0	0	0
Other financing (net)	577	234	-105	-24	-95
Net cash flows from financing activities	**-1,177**	**-604**	**2,009**	**5**	**-779**
Net increase/decrease in cash held	**-15**	**-543**	**559**	**1,069**	**392**

Table 3: Australian Government general government sector cash flow statement[(a)] (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Net cash from operating activities					
and investments in non-financial assets	**14,899**	**12,617**	**12,617**	**13,659**	**14,292**
Finance leases and similar arrangements(e)	-12	-23	-6	-325	-6
Equals surplus(+)/deficit(-)	**14,888**	**12,594**	**12,611**	**13,334**	**14,286**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) Includes GST cash receipts on an Australian Government tax basis, which is $10 million lower in 2006-07 than GST cash receipts measured on a State tax basis (as shown in Statement 10, Note 16).
(c) GST flows are excluded from these categories.
(d) Includes GST cash payments on an Australian Government tax basis.
(e) The acquisition of assets under finance leases decreases the surplus or increases the deficit. The disposal of assets previously held under finance leases increases the surplus or decreases the deficit.

Table 4: Australian Government general government sector statement of other economic flows (reconciliation of net worth)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Opening net worth	**-30,397**	**-21,768**	**-9,393**	**634**	**12,126**
Opening net worth adjustments(a)	**-129**	**0**	**0**	**0**	**0**
Adjusted opening net worth	**-30,526**	**-21,768**	**-9,393**	**634**	**12,126**
Change in net worth from operating transactions	17,397	12,583	10,790	11,883	13,750
Change in net worth from other economic flows					
Revaluation of equity(b)	-6,561	1,711	1,399	1,515	1,607
Net writedowns of assets (including bad and doubtful debts)	-1,731	-2,371	-2,412	-2,189	-2,394
Assets recognised for the first time	8	26	18	19	30
Liabilities recognised for the first time	0	0	0	0	0
Actuarial revaluations	-1,716	0	0	0	0
Net foreign exchange gains	85	-1	0	0	0
Net swap interest received	138	110	86	74	58
Market valuation of debt	696	333	261	166	133
Other economic revaluations(c)	443	-17	-116	25	49
Total other economic flows	**-8,639**	**-207**	**-763**	**-391**	**-516**
Closing net worth	**-21,768**	**-9,393**	**634**	**12,126**	**25,361**

(a) Adjustments in opening net worth arise from a change in 2004-05 outcomes for the Australian Taxation Office and the Department of Defence and the impact of moving to new international accounting standards.
(b) Revaluations of equity reflects changes in the market valuation of commercial entities, including a change in the value of the Telstra shareholding which is valued at the average of the daily share price over a 90-day period in 2005-06 only. This line also reflects any revaluations at the point of disposal or sale.
(c) Largely reflects revaluation of assets and liabilities.

Table 5: Australian Government public non-financial corporations operating statement

	Estimates	
	2005-06	2006-07
	$m	$m
GFS revenue		
Current grants and subsidies	302	84
Sales of goods and services	27,469	13,514
Interest income	136	88
Other	62	26
Total GFS revenue	**27,969**	**13,711**
GFS expenses		
Gross operating expenses		
Depreciation	3,940	1,595
Salaries, wages and other entitlements	6,512	3,956
Other operating expenses	13,829	6,808
Total gross operating expenses	*24,282*	*12,359*
Interest expenses	430	241
Other property expenses	2,426	868
Current transfers		
Tax expenses	1,761	684
Other current transfers	0	0
Total current transfers	*1,761*	*684*
Capital transfers	0	0
Total GFS expenses	**28,899**	**14,152**
Net operating balance	**-930**	**-441**
Net acquisition of non-financial assets		
Purchases of non-financial assets	5,568	2,380
less Sales of non-financial assets	29	19
less Depreciation	3,940	1,595
plus Change in inventories	35	38
plus Other movements in non-financial assets	535	2
Total net acquisition of non-financial assets	**2,169**	**806**
Net lending/fiscal balance(a)	**-3,100**	**-1,247**

(a) The term fiscal balance is not used by the ABS.
Note: The significant reduction in transactions in 2006-07 is due to the assumed sale of the Government's investment in Telstra.

Table 6: Australian Government public non-financial corporations balance sheet

	Estimates	
	2005-06	2006-07
	$m	$m
GFS assets		
Financial assets		
Cash and deposits	2,243	1,152
Advances paid	0	0
Investments, loans and placements	12	32
Other non-equity assets	5,033	933
Equity	466	513
Total financial assets	*7,755*	*2,630*
Non-financial assets		
Land and fixed assets	27,951	3,656
Other non-financial assets(a)	3,746	1,020
Total non-financial assets	*31,696*	*4,676*
Total GFS assets	**39,451**	**7,306**
GFS liabilities		
Deposits held	0	0
Advances received	0	0
Borrowing	16,130	681
Unfunded superannuation liability and other employee entitlements	2,119	967
Provisions (other than depreciation and bad and doubtful debts)(a)	3,675	414
Other non-equity liabilities	1,210	685
Total GFS liabilities	**23,134**	**2,748**
Shares and other contributed capital	**51,984**	**4,558**
Net worth(b)	**-35,667**	**0**
Net financial worth(c)	-67,363	-4,676
Net debt(d)	13,875	-502

(a) Includes the elimination of commercial taxation adjustments for future income tax benefits and deferred income tax.
(b) Net worth is calculated as total assets minus total liabilities minus shares and other contributed capital. The negative net worth recorded for this sector reflects a higher valuation of listed Australian Government corporations by the sharemarket than the value of net assets recorded by these corporations.
(c) Net financial worth equals total financial assets minus total liabilities minus shares and other contributed capital. That is, it excludes non-financial assets.
(d) Net debt equals the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.

Note: The significant reduction in balances in 2006-07 is due to the assumed sale of the Government's investment in Telstra. A zero net worth is recorded in 2006-07 as shares and contributed capital for the remaining non-financial corporations controlled by the Government are valued at net assets (a proxy for market value for unlisted corporations).

Table 7: Australian Government public non-financial corporations cash flow statement[(a)]

	Estimates 2005-06 $m	Estimates 2006-07 $m
Cash receipts from operating activities		
Receipts from sales of goods and services	29,662	14,381
Grants and subsidies received	207	52
GST input credit receipts	61	66
Other receipts	128	128
Total operating receipts	**30,058**	**14,628**
Cash payments for operating activities		
Payment for goods and services	-10,176	-5,336
Interest paid	-428	-245
Salaries, wages and other entitlements	-6,579	-4,046
GST payments to taxation authority	-1,295	-639
Other payments for operating activities(b)	-5,372	-2,240
Total operating payments	**-23,851**	**-12,507**
Net cash flows from operating activities	**6,207**	**2,121**
Cash flows from investments in non-financial assets		
Sales of non-financial assets	58	52
Purchases of non-financial assets	-5,573	-2,410
Net cash flows from investments in non-financial assets	**-5,516**	**-2,358**
Net cash flows from investments in financial assets for policy purposes	**0**	**0**
Cash flows from investments in financial assets for liquidity purposes		
Increase in investments	74	-70
Net cash flows from investments in financial assets for liquidity purposes	**74**	**-70**
Cash flows from financing activities		
Advances received (net)	0	0
Borrowing (net)	-1	-1
Deposits received (net)	0	0
Distributions paid (net)(c)	-2,443	-868
Other financing (net)	853	37
Net cash flows from financing activities	**-1,592**	**-832**
Net increase/decrease in cash held	**-827**	**-1,139**
Net cash from operating activities and investments in non-financial assets	**691**	**-237**
Finance leases and similar arrangements(d)	0	0
Distributions paid(c)	-2,443	-868
Equals surplus(+)/deficit(-)	**-1,753**	**-1,105**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) Other payments for operating activities includes the cash flow to the general government sector from public non-financial corporations distributions paid.
(c) Distributions paid comprise public non-financial corporations dividends to non-general government shareholders.
(d) The acquisition of assets under finance leases decreases the surplus or increases the deficit. The disposal of assets previously held under finance leases increases the surplus or decreases the deficit.
Note: The significant reduction in transactions in 2006-07 is due to the assumed sale of the Government's investment in Telstra.

Table 8: Australian Government total non-financial public sector operating statement

	Estimates	
	2005-06	2006-07
	$m	$m
GFS revenue		
Taxation revenue	244,089	256,441
Current grants and subsidies	0	0
Sales of goods and services	31,743	17,819
Interest income	2,523	3,805
Dividend income	1,397	1,462
Other	3,235	3,267
Total GFS revenue	**282,987**	**282,795**
GFS expenses		
Gross operating expenses		
Depreciation	5,981	3,838
Superannuation	2,589	2,679
Salaries and wages	19,140	17,672
Payment for supply of goods and services	58,943	58,581
Other operating expenses	2,359	2,778
Total gross operating expenses	*89,011*	*85,547*
Nominal superannuation interest expense	5,583	5,784
Other interest expenses	4,514	4,141
Other property expenses	2,426	868
Current transfers		
Grant expenses	77,364	81,141
Subsidy expenses	6,041	7,184
Personal benefit payments in cash	77,332	81,108
Other current transfers	0	0
Total current transfers	*160,736*	*169,433*
Capital transfers	4,250	4,881
Total GFS expenses	**266,521**	**270,653**
Net operating balance(a)	**16,466**	**12,141**
Net acquisition of non-financial assets		
Purchases of non-financial assets	8,428	5,697
less Sales of non-financial assets	232	171
less Depreciation	5,981	3,838
plus Change in inventories	183	559
plus Other movements in non-financial assets	652	202
Total net acquisition of non-financial assets	**3,050**	**2,448**
Net lending/fiscal balance(a)(b)	**13,416**	**9,693**

(a) The fiscal balance and net operating balance estimates in this table differ from those presented elsewhere in the Budget reflecting the treatment of the GST as an Australian Government tax.
(b) The term fiscal balance is not used by the ABS.

Table 9: Australian Government total non-financial public sector balance sheet

	Estimates	
	2005-06	2006-07
	$m	$m
GFS assets		
Financial assets		
Cash and deposits	4,028	2,394
Advances paid	21,471	22,941
Investments, loans and placements	47,131	62,273
Other non-equity assets	27,265	23,914
Equity	15,003	36,607
Total financial assets	*114,898*	*148,128*
Non-financial assets		
Land and fixed assets	68,451	45,604
Other non-financial assets	7,107	4,566
Total non-financial assets	*75,558*	*50,169*
Total GFS assets	**190,455**	**198,297**
GFS liabilities		
Deposits held	405	405
Advances received	0	0
Government securities	59,547	58,356
Loans	5,341	5,293
Other borrowing	16,428	977
Unfunded superannuation liability and other employee entitlements	106,068	108,770
Other provisions	8,448	5,065
Other non-equity liabilities	28,668	28,825
Total GFS liabilities	**224,904**	**207,690**
Shares and other contributed capital	**22,986**	**0**
Net worth(a)	**-57,434**	**-9,393**
Net financial worth(b)	-132,992	-59,563
Net debt(c)	9,090	-22,577

(a) Net worth is calculated as total assets minus total liabilities minus shares and other contributed capital. The negative net worth recorded for this sector partly reflects a higher valuation of listed Australian Government corporations by the sharemarket than the value of net assets recorded by these corporations.
(b) Net financial worth equals total financial assets minus total liabilities minus shares and other contributed capital. That is, it excludes non-financial assets.
(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.

Table 10: Australian Government total non-financial public sector cash flow statement[(a)]

	Estimates	
	2005-06	2006-07
	$m	$m
Cash receipts from operating activities		
Taxes received	239,750	251,611
Receipts from sales of goods and services(b)	32,753	18,559
Grants and subsidies received	0	0
Interest receipts	2,408	3,591
Dividends	1,449	1,797
GST input credit receipts(b)	0	0
Other receipts	2,891	2,944
Total operating receipts	**279,251**	**278,502**
Cash payments for operating activities		
Payments for goods and services(b)	-58,217	-59,723
Grants and subsidies paid	-88,428	-91,129
Interest paid	-5,238	-4,195
Personal benefit payments	-76,343	-80,168
Salaries, wages and other entitlements	-24,184	-22,482
GST payments to taxation authority(b)	0	0
Other payments for operating activities	-3,019	-2,724
Total operating payments	**-255,430**	**-260,422**
Net cash flows from operating activities	**23,821**	**18,080**
Cash flows from investments in non-financial assets		
Sales of non-financial assets	282	206
Purchases of non-financial assets	-8,512	-5,906
Net cash flows from investments in non-financial assets	**-8,231**	**-5,700**
Net cash flows from investments in financial assets for policy purposes	**-1,390**	**24,869**
Cash flows from investments in financial assets for liquidity purposes		
Increase in investments	-12,272	-37,494
Net cash flows from investments in financial assets for liquidity purposes	**-12,272**	**-37,494**
Cash flows from financing activities		
Advances received (net)	0	0
Borrowing (net)	-1,755	-839
Deposits received (net)	0	0
Distributions paid (net)(c)	-2,443	-868
Other financing (net)	1,430	271
Net cash flows from financing activities	**-2,769**	**-1,437**
Net increase/decrease in cash held	**-841**	**-1,682**
Net cash from operating activities and investments in non-financial assets	**15,590**	**12,380**
Finance leases and similar arrangements(d)	-12	-23
Distributions paid(c)	-2,443	-868
Equals surplus(+)/deficit(-)	**13,135**	**11,489**

(a) A positive number denotes a cash inflow; a negative sign denotes a cash outflow.
(b) GST flows are excluded from these categories.
(c) Distributions paid comprise public non-financial corporations dividends to non-general government shareholders.
(d) The acquisition of assets under finance leases decreases the surplus or increases the deficit. The disposal of assets previously held under finance leases increases the surplus or decreases the deficit.

Table 11: Australian Government general government sector taxation revenue by source

	Estimates	
	2005-06	2006-07
	$m	$m
Taxes on income, profits and capital gains		
Income and capital gains levied on individuals	119,580	120,100
Income and capital gains levied on enterprises	57,840	65,240
Income taxes levied on non-residents	0	0
Total taxes on income, profits and capital gains	**177,420**	**185,340**
Taxes on employers' payroll and labour force	305	280
Taxes on property	14	15
Taxes on the provision of goods and services		
Sales/goods and services tax	39,020	41,170
Excises and levies	22,679	23,396
Taxes on international trade	5,171	5,638
Other	0	0
Total taxes on the provision of goods and services	**66,870**	**70,204**
Taxes on use of goods and performance of activities	1,336	1,317
Total GFS taxation revenue	**245,945**	**257,157**

Table 12: Australian Government general government sector purchases of non-financial assets by function

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
General public services	794	770	701	627	586
Defence	608	686	665	1,116	854
Public order and safety	239	276	215	204	206
Education	14	17	21	19	20
Health	110	141	108	92	91
Social security and welfare	223	402	263	213	185
Housing and community amenities	95	25	19	19	18
Recreation and culture	279	339	246	235	208
Fuel and energy	5	8	6	6	5
Agriculture, forestry and fishing	39	74	39	38	34
Mining, manufacturing and construction	48	65	47	38	35
Transport and communications	104	53	44	39	29
Other economic affairs	284	383	274	241	236
Other purposes	19	77	30	124	141
General government purchases of non-financial assets	**2,860**	**3,317**	**2,679**	**3,012**	**2,648**

APPENDIX A: AUSTRALIAN LOAN COUNCIL ALLOCATION

Under Loan Council arrangements, every year the Australian Government and each State and Territory government nominate a Loan Council Allocation. A jurisdiction's Loan Council Allocation incorporates:

- the estimated non-financial public sector cash deficit/surplus (made up from the general government and public non-financial corporations sector balances);
- net cash flows from investments in financial assets for policy purposes; and
- memorandum items, which involve transactions that are not formally borrowings but nevertheless have many of the characteristics of borrowings.

Loan Council Allocation nominations are considered by the Loan Council, having regard to each jurisdiction's fiscal position and reasonable infrastructure requirements, as well as the macroeconomic implications of the aggregate figure.

As set out in Table 13, the Australian Government's 2006-07 Loan Council Allocation budget update is a $37,944 million surplus. This compares with its Loan Council Allocation surplus of $36,010 million endorsed by Loan Council on 31 March 2006.

Table 13: Australian Government's Loan Council Allocation budget update for 2006-07

	2006-07 Nomination $m	2006-07 Budget Estimate $m
General government sector cash deficit(+)/surplus(-)	-11,591	-12,594
Public non-financial corporations sector cash deficit(+)/surplus(-)	924	1,105
Non-financial public sector cash deficit(+)/surplus(-)	-10,667	-11,489
less Net cash flows from investments in financial assets for policy purposes(a)	24,649	24,869
plus Memorandum items(b)	-694	-1,586
Loan Council Allocation	**-36,010**	**-37,944**

(a) Such transactions involve the transfer or exchange of a financial asset and are not included within the cash deficit/surplus. However, the cash flow from investments in financial assets for policy purposes has implications for a government's call on financial markets.

(b) For the Australian Government, memorandum items include the change in net present value (NPV) of operating leases (with NPV greater than $5 million), over-funding of superannuation and an adjustment to exclude the net financing requirement of Telstra.

STATEMENT 10: AUSTRALIAN ACCOUNTING STANDARDS FINANCIAL STATEMENTS

This statement presents financial statements that have been prepared on an accrual basis in accordance with applicable Australian Accounting Standards (AAS), being the Australian Equivalents to International Financial Reporting Standards (AEIFRS) and AAS 31 *Financial Reporting by Governments*, except where departures from the standard are identified in Note 1.

A reconciliation between the Australian Government's general government AAS and Government Finance Statistics (GFS) revenue, expenses and operating results is provided in Statement 8.

STATEMENT 10: AUSTRALIAN ACCOUNTING STANDARDS FINANCIAL STATEMENTS

Table 1: Australian Government general government sector income statement

		Estimates		Projections		
		2005-06	2006-07	2007-08	2008-09	2009-10
	Note	$m	$m	$m	$m	$m
Revenues						
Taxation						
Income tax	3	173,760	181,620	189,680	199,330	211,770
Indirect tax	4	28,231	29,428	30,178	31,009	31,248
Fringe benefits tax		3,300	3,360	3,440	3,540	3,660
Other taxes		2,242	2,215	2,243	2,317	2,219
Total taxation revenue		**207,533**	**216,623**	**225,541**	**236,195**	**248,897**
Non-taxation						
Sales of goods and services		4,898	4,846	4,975	5,114	5,255
Interest and dividends	5	8,691	8,138	7,771	8,148	8,700
Other sources of non-tax revenue	6	3,502	3,415	3,462	3,325	3,185
Total non-tax revenue		**17,092**	**16,400**	**16,208**	**16,588**	**17,140**
Total revenue		**224,625**	**233,023**	**241,749**	**252,784**	**266,037**
Gains						
Net foreign exchange gains		85	0	0	0	0
Net gains from sale of assets(a)		99	0	1,384	1,499	1,588
Other gains		977	574	495	300	280
Total Gains		**1,161**	**574**	**1,879**	**1,799**	**1,868**
Income		**225,786**	**233,597**	**243,628**	**254,583**	**267,905**
Expenses						
Goods and services						
Employees	7	22,789	24,683	25,008	25,634	26,344
Suppliers	8	18,487	20,225	20,577	20,177	20,443
Depreciation and amortisation	9	4,554	4,930	5,123	5,205	5,089
Net write-down and impairment of assets and fair value losses		3,085	2,953	3,010	2,943	2,958
Net foreign exchange losses		0	1	0	0	0
Net losses from sale of assets(a)		0	196	0	0	0
Other goods and services expenses	10	7,649	7,695	8,643	9,112	10,086
Total goods and services		**56,564**	**60,682**	**62,362**	**63,072**	**64,919**
Subsidies benefits and grants						
Personal benefits		93,371	98,021	105,428	112,916	122,755
Subsidies		11,004	12,297	12,928	13,698	13,985
Grants	11	42,501	44,591	46,587	47,712	47,135
Total subsidies benefits and grants		**146,876**	**154,909**	**164,942**	**174,327**	**183,875**
Borrowing costs						
Interest		5,932	5,497	5,181	4,682	4,394
Other borrowing costs		17	13	13	8	7
Total interest and other borrowing costs		**5,949**	**5,510**	**5,194**	**4,690**	**4,400**
Total expenses		**209,388**	**221,101**	**232,498**	**242,089**	**253,195**
Operating result		**16,397**	**12,496**	**11,130**	**12,494**	**14,711**

(a) In the mid-year update of the 2005-06 Budget a profit on sale of assets of $27 billion was recorded in 2006-07. Due to the revaluation of financial investments to fair value in the budget, as disclosed in Note 1, profits or losses on sale are no longer recorded.

Table 2: Australian Government general government sector balance sheet

		Estimates		Projections		
		2005-06	2006-07	2007-08	2008-09	2008-10
	Note	$m	$m	$m	$m	$m
Assets						
Financial assets						
Cash		1,785	1,242	1,801	2,870	3,262
Receivables	12	32,069	33,910	36,473	39,391	42,606
Investments		89,829	102,349	115,880	128,002	140,714
Equity accounted investments		399	276	276	276	276
Accrued revenue		563	678	678	701	729
Other financial assets		17	18	18	18	18
Total financial assets		**124,663**	**138,472**	**155,126**	**171,258**	**187,606**
Non-financial assets	13					
Land and buildings		19,558	19,986	19,788	20,221	20,640
Infrastructure		40,031	42,459	44,219	45,854	47,845
Heritage and cultural assets		7,723	7,753	7,767	7,777	7,795
Intangibles		1,916	2,147	2,178	2,145	2,094
Investment property		851	872	976	1,083	1,101
Biological assets		0	0	0	0	0
Assets held for sale		65	63	56	65	65
Inventories		4,625	5,146	5,236	5,324	5,392
Other non-financial assets		4,596	4,216	3,269	2,194	1,609
Total non-financial assets		**79,364**	**82,641**	**83,488**	**84,665**	**86,542**
Total assets		**204,027**	**221,113**	**238,614**	**255,923**	**274,148**
Liabilities						
Debt						
Government securities		59,547	58,356	60,164	60,237	59,428
Loans		4,224	4,240	4,259	3,955	3,955
Leases		233	230	203	485	448
Deposits		405	405	405	405	405
Overdrafts		0	0	0	0	0
Other debt		1,099	1,113	1,115	1,105	1,087
Total debt		**65,508**	**64,343**	**66,146**	**66,187**	**65,323**
Provisions and payables						
Employees	14	103,948	107,803	111,543	115,412	119,391
Suppliers		2,680	2,571	2,569	2,532	2,512
Personal benefits payable		6,290	6,745	7,251	7,544	7,680
Subsidies payable		1,313	1,420	1,395	1,471	1,529
Grants payable	15	10,209	10,306	10,676	11,170	11,336
Other provisions and payables		11,529	11,391	11,358	11,380	11,362
Total provisions and payables		**135,970**	**140,237**	**144,792**	**149,509**	**153,809**
Liabilities associated with assets held for sale						
Total liabilities		**201,478**	**204,580**	**210,938**	**215,697**	**219,132**
Net assets		**2,549**	**16,532**	**27,676**	**40,226**	**55,016**
Equity						
Accumulated results		-55,956	-18,440	-7,311	5,193	19,905
Reserves		58,505	34,972	34,987	35,033	35,111
Capital		0	0	0	0	0
Total equity		**2,549**	**16,532**	**27,676**	**40,226**	**55,016**

Table 3: Australian Government general government sector statement of changes in equity

	Accumulated results		Asset revaluation reserve		Other reserves		Contributed equity/capital		Total equity	
	2005-06 $m	2006-07 $m	2005-06 $m	2006-07 $m	2005-06 $m	2006-07 $m	2005-06 $m	2006-07 $m	2005-06 $m	2006-07 $m
Opening balance										
Balance carried forward from previous period	-74,934	-55,956	16,939	16,741	21,505	41,764	0	0	-36,490	2,549
Adjustment for errors / entity adjustments	-1,014	-3	-222	0	-9	0	16	0	-1,230	-3
Adjustment for changes in accounting policy	23,127	0	na	na	na	na	na	na	23,127	0
Adjusted opening balance	**-52,822**	**-55,958**	**16,717**	**16,741**	**21,496**	**41,764**	**16**	**0**	**-14,593**	**2,546**
Income and expense										
Revenues and expenses recognised directly in equity										
Currency translation gain (loss)	na	na	na	na	0	0	na	na	0	0
Financial asset revaluations	na	na	-15	1,451	na	na	na	na	-15	1,451
Non-financial asset revaluations	na	na	68	33	na	na	na	na	68	33
Total revenues and expenses recognised directly in equity	0	0	53	1,484	0	0	0	0	53	1,484
Net operating result	**16,397**	**12,496**	na	na	na	na	na	na	**16,397**	**12,496**
Total income and expenses										
Transfers between reserves	-19,978	25,007	224	-9	19,754	-24,998	na	na	0	0
Dividends	0	0	0	0	0	0	na	na	0	0
Other movements	446	15	-253	-5	514	-5	-16	0	692	5
Closing balance	**-55,956**	**-18,440**	**16,741**	**18,211**	**41,764**	**16,761**	**0**	**0**	**2,549**	**16,532**

Table 3: Australian Government general government sector statement of changes in equity (continued)

	Accumulated results		Asset revaluation reserve		Other reserves		Contributed equity/capital		Total equity	
	2007-08	2008-09	2007-08	2008-09	2007-08	2008-09	2007-08	2008-09	2007-08	2008-09
	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m
Opening balance										
Balance carried forward from previous period	-18,440	-7,311	18,211	18,226	16,761	16,761	0	0	16,532	27,676
Adjustment for errors / entity adjustments	0	0	0	0	0	0	0	0	0	0
Adjustment for changes in accounting policy	0	0	na	na	na	na	na	na	0	0
Adjusted opening balance	**-18,440**	**-7,311**	**18,211**	**18,226**	**16,761**	**16,761**	**0**	**0**	**16,532**	**27,676**
Income and expense										
Revenues and expenses recognised directly in equity										
Currency translation gain (loss)	na	na	na	na	0	0	na	na	0	0
Financial asset revaluations	na	na	5	0	na	na	na	na	5	0
Non-financial asset revaluations	na	na	27	48	na	na	na	na	27	48
Total revenues and expenses recognised directly in equity	0	0	32	48	0	0	0	0	32	48
Net operating result	**11,130**	**12,494**	**na**	**na**	**na**	**na**	**na**	**na**	**11,130**	**12,494**
Total income and expenses										
Transfers between reserves	17	-2	-17	2	0	0	na	na	0	0
Dividends	0	0	0	0	0	0	na	na	0	0
Other movements	-18	12	0	-5	0	0	0	0	-18	7
Closing balance	**-7,311**	**5,193**	**18,226**	**18,272**	**16,761**	**16,761**	**0**	**0**	**27,676**	**40,226**

Table 3: Australian Government general government sector statement of changes in equity (continued)

	Accumulated results	Asset revaluation reserve	Other reserves	Contributed equity/capital	Total equity
	2009-10	2009-10	2009-10	2009-10	2009-10
	$m	$m	$m	$m	$m
Opening balance					
Balance carried forward from previous period	5,193	18,272	16,761	0	40,226
Adjustment for errors / entity adjustments	0	0	0	0	0
Adjustment for changes in accounting policy	0	na	na	na	0
Adjusted opening balance	**5,193**	**18,272**	**16,761**	**0**	**40,226**
Income and expense					
Revenues and expenses recognised directly in equity					
Currency translation gain (loss)	na	na	0	na	0
Financial asset revaluations	na	0	na	na	0
Non-financial asset revaluations	na	77	na	na	77
Total revenues and expenses recognised directly in equity	0	77	0	0	77
Net operating result	**14,711**	**na**	**na**	**na**	**14,711**
Total income and expenses					
Transfers between reserves	-1	1	0	na	0
Dividends	0	0	0	na	0
Other movements	2	0	0	0	2
Closing balance	**19,905**	**18,350**	**16,761**	**0**	**55,016**

Table 4: Australian Government general government sector cash flow statement

	Note	Estimates		Projections		
		2005-06	2006-07	2007-08	2008-09	2009-10
		$m	$m	$m	$m	$m
Operating activities						
Cash received						
Taxation	16	204,012	212,756	221,532	232,025	244,596
Sales of goods and services		5,204	5,008	5,137	5,297	5,427
Interest		4,308	5,240	4,844	4,956	5,251
Dividends		4,341	3,000	2,866	3,058	3,228
GST input credit receipts		2,973	3,027	2,988	2,996	3,058
Other		3,026	3,016	3,075	2,965	2,794
Total operating cash received		**223,849**	**232,048**	**240,441**	**251,297**	**264,354**
Cash used						
Payments to employees		19,953	20,843	21,228	21,720	22,321
Payments to suppliers		21,643	23,960	23,767	23,383	23,672
Subsidies paid		10,451	11,488	12,260	12,929	13,275
Personal benefits		92,382	97,082	104,596	112,560	122,565
Grant payments		44,559	44,321	45,487	46,204	46,701
Interest and other financing costs		6,744	5,513	5,278	4,834	4,402
GST payments to taxation authority		86	79	81	82	85
Other		7,144	7,717	8,591	8,999	10,013
Total operating cash used		**202,948**	**211,003**	**221,287**	**230,710**	**243,033**
Net cash from operating activities		**20,901**	**21,045**	**19,154**	**20,587**	**21,321**
Investing activities						
Cash received						
Proceeds from asset sales program		0	26,728	0	0	0
Proceeds from sales of property, plant and equipment and intangibles		224	154	233	155	122
Other net investing cash received		380	492	1,632	1,751	1,870
Total investing cash received		**604**	**27,373**	**1,864**	**1,907**	**1,991**
Cash used						
Purchase of property, plant and equipment and intangibles		6,188	8,120	7,066	7,217	7,347
Net loans, advances and HECS		1,238	1,697	1,758	1,859	1,911
Other net investing cash paid		12,798	38,361	13,776	12,372	12,962
Total investing cash used		**20,224**	**48,177**	**22,600**	**21,448**	**22,220**
Net cash from investing activities		**-19,620**	**-20,804**	**-20,735**	**-19,541**	**-20,229**
Financing activities						
Cash received						
Net cash received from currency issues		0	0	0	0	0
Other		459	81	59	37	26
Total financing cash received		**459**	**81**	**59**	**37**	**26**
Cash used						
Net repayments of borrowings		1,754	838	-2,114	-29	684
Other		1	26	33	44	43
Total financing cash used		**1,755**	**864**	**-2,081**	**14**	**727**
Net cash from financing activities		**-1,296**	**-784**	**2,140**	**23**	**-701**
Net increase/decrease in cash held	2	**-15**	**-543**	**559**	**1,069**	**392**

NOTES TO THE AAS FINANCIAL STATEMENTS

Note 1: External reporting standards and accounting policies

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

The financial statements included in this Appendix have been prepared on an accrual basis in accordance with applicable Australian Accounting Standards (AAS), being the Australian Equivalents to International Financial Reporting Standards (AEIFRS) and AAS 31 *Financial Reporting by Governments* (AAS 31).

AAS requires governments to prepare accrual based general purpose financial reports. This means that assets, liabilities, income and expenses are recorded in financial statements when transactions have an economic impact on the government, rather than when the cash flow associated with these transactions occurs. Consistent with AAS, an income statement, a balance sheet, a statement of changes in equity, and a cash flow statement have been prepared for the budget year and the three forward years.

The accounting policies in this appendix are generally consistent with the accounting policies in AAS. While the scope for financial reporting recommended in AAS 31 is the whole of government (that is, the Australian Government public sector), in accordance with the *Charter of Budget Honesty Act 1998*, the presentation covers the general government sector only. This appendix includes notes showing disaggregated information.

AAS would suggest the gross amount of goods and services tax (GST) be included in the Australian Government's financial statements. However, under the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations,* GST is collected by the Australian Taxation Office as an agent for the States and Territories (the States), and appropriated to the States. Therefore, accrued GST revenues and associated payments to the States are not recorded in the financial statements.

AAS seeks to recognise tax revenue when the economic event giving rise to the taxpayer's liability occurs. The budget and related outcomes adopt this treatment for measuring and recognising revenue of all categories of taxation. For individuals, company and superannuation revenue, such an estimation method is unreliable and tax revenue is recognised the earlier of when an assessment of a tax liability is made or cash payment is received by the Australian Taxation Office or the Australian Customs Service. This method is permitted under AAS when there is an inability to reliably measure taxation revenues at the time the underlying transaction or event occurs. Accordingly, for these categories of taxation revenue, there is a short lag between the time at which the underlying economic activity giving rise to the tax liability occurs and when the revenue is recognised. Longer lags occur for some elements of company and superannuation funds taxation. Further details are contained are Box 5.1 of Statement 5.

The new AEIFRS standard relating to superannuation is AASB 119 *Employee Benefits*. The expected impacts of applying this standard to the Australian Government's superannuation liability cannot be reliably determined at this point in time due to differences in interpretation in respect to the methodology used to calculate the discount rate. The Heads of Treasuries Accounting and Reporting Advisory Committee is currently reviewing cross jurisdictional consistency of interpretations and methodologies with the intention of seeking an interpretation from the Australian Accounting Standards Board.

Consistent with the market basis of valuation of assets adopted elsewhere in this document, the basis of valuation of the Government's investment in Telstra Corporation Limited and other Commonwealth entities under AAS, has changed from cost to fair value. The financial effect of this change is recognised in the Statement of Changes in Equity.

Note 2: Reconciliation of cash

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Operating result (revenues less expenses)	**16,397**	**12,496**	**11,130**	**12,494**	**14,711**
less **Revenues not providing cash**					
Foreign exchange gains	85	0	0	0	0
Gains from asset sales programme	0	0	0	0	0
Gains from sale of assets	99	249	1,384	1,499	1,610
Other	1,469	945	874	739	786
Total revenues not providing cash	**1,653**	**1,195**	**2,258**	**2,239**	**2,396**
plus **Expenses not requiring cash**					
Increase/(decrease) in employee entitlements	2,872	3,855	3,740	3,869	3,978
Depreciation/amortisation expense	4,554	4,930	5,123	5,205	5,089
Provision for bad and doubtful debts	352	423	452	490	525
Provision for diminution in value of assets	539	248	243	138	133
Losses from asset sales programme	0	446	0	0	0
Losses from sale of assets	0	0	0	0	19
Foreign exchange losses	0	1	0	0	0
Other	27	15	-16	12	23
Total expenses not requiring cash	**8,344**	**9,917**	**9,543**	**9,714**	**9,768**
plus **Cash provided by working capital items**					
Decrease in inventories	0	0	0	0	0
Decrease in receivables	0	0	0	0	0
Decrease in other financial assets	99	0	57	27	0
Decrease in other non-financial assets	0	314	967	1,122	365
Increase in benefits subsidies and grants payable	1,284	660	777	742	251
Increase in suppliers' liabilities	333	0	0	0	0
Increase in other provisions and payables	0	0	0	0	86
Total cash provided by working capital items	**1,716**	**974**	**1,800**	**1,890**	**703**
less **Cash used by working capital items**					
Increase in inventories	230	521	90	88	67
Increase in receivables	474	263	924	1,147	1,358
Increase in other financial assets	0	116	0	0	19
Increase in other non-financial assets	2,674	0	0	0	0
Decrease in benefits subsidies and grants payable	150	16	25	0	0
Decrease in other provisions and payables	375	128	21	1	0
Decrease in suppliers' liabilities	0	104	0	38	20
Total cash used by working capital items	**3,903**	**1,148**	**1,061**	**1,273**	**1,464**
equals *Net cash from/(to) operating activities*	20,901	21,045	19,154	20,587	21,321
plus Net cash from/(to) investing activities	-19,620	-20,804	-20,735	-19,541	-20,229
Net cash from operating activities and investment	**1,282**	**241**	**-1,581**	**1,046**	**1,093**
plus Net cash from/(to) financing activities	-1,296	-784	2,140	23	-701
equals Net (decrease)/increase in cash	**-15**	**-543**	**559**	**1,069**	**392**

Note 2(a): Consolidated Revenue Fund

The estimated and projected cash balances reflected in the statement of financial position for the Australian Government general government sector (Table 2) include the reported cash balances controlled and administered by Australian Government agencies subject to the *Financial Management and Accountability Act 1997* and the reported cash balances controlled and administered by entities, subject to the *Commonwealth Authorities and Companies Act 1997* (CAC Act), that implement public policy through the provision of primarily non-market services.

Revenues or monies raised by the Executive Government automatically form part of the Consolidated Revenue Fund by force of section 81 of the Australian Constitution. For practical purposes, total Australian Government general government sector cash, less cash controlled and administered by CAC Act entities, plus special public monies represents the Consolidated Revenue Fund referred to in section 81 of the Australian Constitution. On this basis, the balance of the Consolidated Revenue Fund is shown below.

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Total general government sector cash (Statement 10)	1,785	1,242	1,801	2,870	3,262
less CAC Agency cash balances	911	737	219	217	129
plus Special public monies	81	83	86	89	91
Balance of Consolidated Revenue Fund at 30 June	**955**	**588**	**1,668**	**2,742**	**3,224**

Further information on the Consolidated Revenue Fund is included in Budget Paper No. 4, *Agency Resourcing 2006-07.*

Note 3: Income taxation revenue

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Individuals and other witholding tax					
Gross income tax withholding	103,830	104,010	109,540	116,620	124,870
Gross other individuals	26,410	28,480	29,670	32,000	34,770
less Refunds	15,350	16,790	18,690	19,970	21,260
Total individuals and other witholding tax	114,890	115,700	120,520	128,650	138,380
Companies	50,480	56,860	59,400	59,950	61,800
Superannuation funds					
Contributions and earnings	5,390	5,890	6,400	6,950	7,560
Surcharge	1,030	680	110	40	30
Total superannuation funds	6,420	6,570	6,510	6,990	7,590
Petroleum resource rent tax	1,970	2,490	3,250	3,740	4,000
Total income taxation revenue	**173,760**	**181,620**	**189,680**	**199,330**	**211,770**

Note 4: Indirect taxation revenue

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Excise duty					
Petroleum and other fuel products	13,740	14,180	14,520	14,870	15,180
Crude oil	330	470	310	200	120
Other excise	7,830	7,970	8,100	8,250	8,410
Total excise duty revenue	21,900	22,620	22,930	23,320	23,710
Customs duty revenue	5,171	5,638	6,008	6,379	6,158
Other indirect tax revenue	1,160	1,170	1,240	1,310	1,380
GST	37,860	40,000	42,210	44,440	46,670
less transfers to States in relation to GST revenue	37,860	40,000	42,210	44,440	46,670
GST revenue	0	0	0	0	0
Mirror taxes	372	390	407	428	450
less transfers to States in relation to mirror tax revenue	372	390	407	428	450
Mirror tax revenue	0	0	0	0	0
Indirect tax revenue	**28,231**	**29,428**	**30,178**	**31,009**	**31,248**

Note 5: Interest and dividend revenue

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Interest					
Interest from other governments					
State and Territory debt	17	16	17	16	15
Housing agreements	170	166	162	158	153
Total interest from other governments	**187**	**182**	**179**	**174**	**168**
Interest from other sources					
Swap interest	1,984	1,721	1,448	1,085	825
Advances	19	26	27	27	27
Deposits	0	0	0	0	0
Bills receivable	6	6	6	5	6
Bank deposits	277	241	248	253	262
Indexation of HECS receivable and other student loans	378	387	394	455	522
Other	1,519	2,876	2,603	3,091	3,662
Total interest from other sources	**4,183**	**5,256**	**4,726**	**4,917**	**5,304**
Total interest	**4,370**	**5,438**	**4,905**	**5,090**	**5,472**
Dividends					
Dividends from controlled entities	4,312	2,465	1,676	1,765	1,838
Other dividends	9	235	1,190	1,294	1,390
Total dividends	**4,321**	**2,701**	**2,866**	**3,058**	**3,228**
Total interest and dividend revenue	**8,691**	**8,138**	**7,771**	**8,148**	**8,700**

Note 6: Other sources of non-taxation revenue

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Industry contributions	228	208	195	188	188
International Monetary Fund related revenue	23	15	15	15	15
Royalties	1,036	1,218	1,262	1,087	915
Seigniorage	125	101	106	103	103
Other	2,091	1,873	1,885	1,933	1,964
Total other sources of non-taxation revenue	**3,502**	**3,415**	**3,462**	**3,325**	**3,185**

Note 7: Employee expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Salaries and wages(a)	12,627	13,715	13,822	13,941	14,266
Leave and other entitlements	1,327	1,365	1,405	1,416	1,432
Separations and redundancies	42	48	40	44	40
Workers compensation premiums	0	1	2	10	4
Other (including superannuation)	8,792	9,555	9,739	10,222	10,602
Total employee expenses	**22,789**	**24,683**	**25,008**	**25,634**	**26,344**

(a) Salaries and wages do not include superannuation.

Note 8: Suppliers expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Supply of goods and services	16,308	17,943	18,244	17,786	18,014
Operating lease rental expenses	1,700	1,751	1,776	1,783	1,811
Other	479	530	558	608	618
Total suppliers expenses	**18,487**	**20,225**	**20,577**	**20,177**	**20,443**

Note 9: Depreciation and amortisation expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Depreciation					
Specialist military equipment	2,513	2,686	2,738	2,740	2,597
Buildings	586	604	623	646	657
Other infrastructure, plant and equipment	1,075	1,177	1,248	1,294	1,308
Heritage and cultural assets	43	44	46	47	47
Investment property	0	0	0	0	0
Total depreciation	**4,217**	**4,512**	**4,655**	**4,727**	**4,610**
Total amortisation	**337**	**418**	**468**	**478**	**479**
Total depreciation and amortisation expenses	**4,554**	**4,930**	**5,123**	**5,205**	**5,089**

Note 10: Other goods and services expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Health care payments	4,593	4,568	4,737	4,875	5,030
Development Cooperation Program	1,339	1,434	2,150	2,404	3,184
Other	1,717	1,692	1,756	1,833	1,872
Total other goods and services expenses	**7,649**	**7,695**	**8,643**	**9,112**	**10,086**

Note 11: Grants expenses

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
State and Territory governments	27,264	27,883	28,957	29,771	30,102
Non-profit organisations	1,575	1,698	1,720	1,764	1,779
Overseas	434	651	861	793	382
Private sector	1,982	1,797	1,513	1,379	1,208
Local governments	411	499	553	498	67
Multi-jurisdictional sector	6,081	5,942	6,053	6,205	6,365
Other	4,754	6,121	6,928	7,302	7,232
Total grant expenses	**42,501**	**44,591**	**46,587**	**47,712**	**47,135**

Note 12: Receivables

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Taxes receivable	10,726	11,792	13,054	14,495	16,132
Advances and loans	16,571	18,022	19,484	21,031	22,642
Other receivables	4,772	4,096	3,935	3,864	3,833
Total receivables	**32,069**	**33,910**	**36,473**	**39,391**	**42,606**

Note 13: Total non-financial assets

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Land and buildings					
Land	6,089	6,112	6,099	6,069	5,991
Buildings	13,469	13,875	13,689	14,152	14,649
Total land and buildings	**19,558**	**19,986**	**19,788**	**20,221**	**20,640**
Infrastructure					
Specialist military equipment	31,437	33,396	35,129	36,798	38,971
Other	8,595	9,063	9,091	9,056	8,874
Total infrastructure	**40,031**	**42,459**	**44,219**	**45,854**	**47,845**
Intangibles					
Computer software	1,753	1,982	2,019	1,998	1,957
Other	162	165	159	147	137
Total intangibles	**1,916**	**2,147**	**2,178**	**2,145**	**2,094**
Heritage and cultural assets	7,723	7,753	7,767	7,777	7,795
Total heritage and cultural assets	**7,723**	**7,753**	**7,767**	**7,777**	**7,795**
Investment properties	851	872	976	1,083	1,101
Total investment properties	**851**	**872**	**976**	**1,083**	**1,101**
Biological assets	0	0	0	0	0
Total biological assets	**0**	**0**	**0**	**0**	**0**
Assets held for sale	65	63	56	65	65
Total assets held for sale	**65**	**63**	**56**	**65**	**65**
Inventories	4,625	5,146	5,236	5,324	5,392
Total inventories	**4,625**	**5,146**	**5,236**	**5,324**	**5,392**
Other non-financial assets					
Prepayments	4,066	3,752	2,785	1,663	1,298
Other	530	464	485	532	312
Total other non-financial assets	**4,596**	**4,216**	**3,269**	**2,194**	**1,609**
Total non-financial assets	**79,364**	**82,641**	**83,488**	**84,665**	**86,542**

Note 14: Employee and superannuation liabilities

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Superannuation	95,504	99,105	102,631	106,225	109,899
Leave and other entitlements	4,185	4,205	4,183	4,256	4,350
Accrued salaries and wages	162	191	223	243	287
Workers compensation claims	1,562	1,589	1,638	1,638	1,662
Separations and redundancies	33	43	33	38	34
Workers compensation premiums	1,579	1,686	1,791	1,907	2,023
Other	923	983	1,045	1,106	1,137
Total employee and superannuation liabilities	**103,948**	**107,803**	**111,543**	**115,412**	**119,391**

Note 15: Grants payable

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
State and Territory governments	4,313	4,582	4,853	5,068	5,354
Non-profit organisations	59	59	59	59	59
Private sector	657	409	201	201	201
Overseas	1,110	947	1,112	1,277	1,054
Local governments	2	1	1	1	1
Other	4,068	4,308	4,450	4,565	4,668
Total grants payable	**10,209**	**10,306**	**10,676**	**11,170**	**11,336**

Note 16: Taxation receipts

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Total taxation receipts	241,484	252,276	263,239	275,933	290,715
less payments to States and Territories in relation to GST revenue	37,100	39,130	41,300	43,480	45,670
less payments to States and Territories in relation to mirror tax revenue	372	390	407	428	450
Taxation receipts	**204,012**	**212,756**	**221,532**	**232,025**	**244,596**

APPENDIX A: ADDITIONAL AGENCY STATISTICS

Table A1: General government expenses by agency

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	2,391	2,307	1,955	1,684	1,264
Grains Research and Development Corporation	131	136	140	144	116
Dairy Structural Adjustment Fund	45	35	24	15	0
Total	**2,566**	**2,477**	**2,119**	**1,842**	**1,380**
Attorney-General's					
Attorney-General's Department	663	849	805	800	790
Australian Customs Service	1,029	1,134	1,157	1,152	1,161
Australian Federal Police	914	1,019	1,031	980	987
Family Court of Australia	138	139	140	141	142
High Court of Australia	14	14	14	14	14
Total	**2,758**	**3,154**	**3,146**	**3,088**	**3,095**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	814	816	729	694	419
Australian Broadcasting Corporation	1021	1047	1054	1071	1088
Australian Communications and Media Authority	245	244	232	229	228
Australian Sports Commission	187	211	203	187	177
National Archives of Australia	69	69	69	69	70
National Gallery of Australia	47	48	49	49	50
National Library of Australia	69	69	69	69	70
National Museum of Australia	45	44	45	45	46
Special Broadcasting Service Corporation	239	229	229	234	237
Total	**2,737**	**2,777**	**2,678**	**2,647**	**2,383**
Defence					
Department of Defence	19,625	20,492	20,940	21,011	21,722
Defence Material Organisation	7,160	8,783	8,799	8,742	9,291
Defence Housing Authority	725	755	806	859	892
Department of Veterans' Affairs	10,481	10,860	11,039	11,231	11,342
Australian War Memorial	40	41	41	41	41
Total	**38,031**	**40,931**	**41,624**	**41,884**	**43,287**
Education, Science and Training					
Department of Education, Science and Training	19,405	20,434	20,950	21,536	22,354
Australian National Training Authority	0	0	0	0	0
Australian Research Council	596	587	592	607	620
Australian Nuclear Science and Technology Organisation	149	172	166	181	173
Commonwealth Scientific and Industrial Research Organisation	956	970	1,005	1,029	1,058
Total	**21,106**	**22,163**	**22,714**	**23,353**	**24,205**

Table A1: General government expenses by agency (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	25,211	26,837	27,948	28,798	29,755
Indigenous Business Australia	30	48	51	53	55
Comcare	610	324	333	341	352
Total	**25,851**	**27,210**	**28,332**	**29,192**	**30,162**
Environment and Heritage					
Department of Environment and Heritage	901	986	918	458	398
Bureau of Meteorology	228	231	237	239	240
Total	**1,129**	**1,217**	**1,155**	**696**	**638**
Families, Community Services and Indigenous Affairs					
Department of Families, Community Services and Indigenous Affairs	44,917	46,867	49,151	51,980	54,389
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	0	0	0	0	0
Total	**44,917**	**46,867**	**49,151**	**51,980**	**54,389**
Finance and Administration					
Department of Finance and Administration	5,750	6,288	6,033	6,166	6,331
Australian Electoral Commission	104	120	237	114	119
Future Fund Management Agency	1	8	8	8	8
Department of Human Services	1,333	1,736	1,916	1,884	1,882
Centrelink	2,294	2,564	2,650	2,607	2,604
Medicare Australia	438	619	691	730	729
Health Insurance Commission	147	0	0	0	0
Total	**10,067**	**11,334**	**11,534**	**11,508**	**11,673**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	949	996	1,005	1,048	1,034
AusAID	1,650	1,979	2,158	2,121	1,643
Australian Trade Commission	349	373	358	357	359
Total	**2,948**	**3,348**	**3,521**	**3,526**	**3,035**
Health and Ageing					
Department of Health and Ageing	38,867	41,661	44,106	45,973	48,108
National Blood Authority	574	636	667	706	747
Total	**39,441**	**42,297**	**44,774**	**46,679**	**48,855**
Immigration and Multicultural Affairs					
Department of Immigration and Multicultural Affairs	1,468	1,480	1,472	1,473	1,495
Total	**1,468**	**1,480**	**1,472**	**1,473**	**1,495**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	2,293	2,246	2,150	1,982	1,761
Tourism Australia	168	159	161	109	111
Total	**2,461**	**2,405**	**2,311**	**2,091**	**1,871**
Parliament					
Department of Parliamentary Services	161	159	161	163	161
Total	**161**	**159**	**161**	**163**	**161**

Table A1: General government expenses by agency (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	92	137	132	78	79
National Water Commission	34	404	606	544	204
Total	**127**	**542**	**738**	**622**	**283**
Transport and Regional Services					
Department of Transport and Regional Services	4,332	4,755	5,298	5,479	4,308
Civil Aviation Safety Authority	120	119	121	124	126
National Capital Authority	29	29	29	30	31
Total	**4,482**	**4,904**	**5,449**	**5,633**	**4,465**
Treasury					
Department of the Treasury(a)	1,317	366	358	359	361
Australian Bureau of Statistics	340	431	322	299	308
Australian Securities and Investment Commission	284	327	327	326	331
Australian Taxation Office(a)	12,947	13,664	13,943	14,342	14,530
Australian Office of Financial Management	5,705	5,133	4,817	4,331	4,058
Total	**20,593**	**19,922**	**19,768**	**19,657**	**19,587**
Small agencies	**3,223**	**3,500**	**3,558**	**3,633**	**3,704**
Whole of government and inter-agency amounts(b)	**-14,678**	**-15,586**	**-11,707**	**-7,581**	**-1,476**
Total expenses	**209,388**	**221,101**	**232,498**	**242,089**	**253,195**

(a) Excludes GST expenses consistent with the *Intergovernmental Agreement on the Reform of Commonwealth State Financial Relations*, whereby GST is collected by the Australian Taxation Office and appropriated to the States and Territories by the Department of the Treasury as agent for the States and Territories.

(b) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A2: Departmental expenses by agency

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	554	552	548	539	490
Grains Research and Development Corporation	131	136	140	144	116
Dairy Structural Adjustment Fund	0	0	0	0	0
Total	**685**	**688**	**688**	**682**	**606**
Attorney-General's					
Attorney-General's Department	190	220	195	189	181
Australian Customs Service	1,026	1,131	1,154	1,149	1,158
Australian Federal Police	914	1,019	1,031	980	987
Family Court of Australia	138	139	140	141	142
High Court of Australia	14	14	14	14	14
Total	**2,282**	**2,523**	**2,534**	**2,474**	**2,483**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	123	142	139	137	135
Australian Broadcasting Corporation	930	956	963	979	997
Australian Communications and Media Authority	74	85	86	84	82
Australian Sports Commission	187	211	203	187	177
National Archives of Australia	69	69	69	69	70
National Gallery of Australia	47	48	49	49	50
National Library of Australia	69	69	69	69	70
National Museum of Australia	45	44	45	45	46
Special Broadcasting Service Corporation	239	229	229	234	237
Total	**1,784**	**1,853**	**1,851**	**1,854**	**1,863**
Defence					
Department of Defence	17,007	17,860	18,227	18,210	18,829
Defence Material Organisation	7,160	8,783	8,799	8,742	9,291
Defence Housing Authority	725	755	806	859	892
Department of Veterans' Affairs	324	334	328	314	312
Australian War Memorial	40	41	41	41	41
Total	**25,256**	**27,772**	**28,201**	**28,166**	**29,365**
Education, Science and Training					
Department of Education, Science and Training	441	477	451	443	444
Australian National Training Authority	0	0	0	0	0
Australian Research Council	14	15	15	15	16
Australian Nuclear Science and Technology Organisation	149	172	166	181	173
Commonwealth Scientific and Industrial Research Organisation	956	970	1,005	1,029	1,058
Total	**1,560**	**1,634**	**1,637**	**1,668**	**1,690**

Table A2: Departmental expenses by agency (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	1,548	1,581	1,633	1,600	1,639
Indigenous Business Australia	30	48	51	53	55
Comcare	610	324	333	341	352
Total	**2,189**	**1,954**	**2,017**	**1,994**	**2,046**
Environment and Heritage					
Department of Environment and Heritage	376	374	353	276	272
Bureau of Meteorology	228	231	237	239	240
Total	**604**	**605**	**590**	**515**	**511**
Families, Community Services and Indigenous Affairs					
Department of Families, Community Services Indigenous Affairs	1,526	1,174	1,130	1,138	1,127
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	0	0	0	0	0
Total	**1,526**	**1,174**	**1,130**	**1,138**	**1,127**
Finance and Administration					
Department of Finance and Administration	387	784	383	356	358
Australian Electoral Commission	104	120	189	114	119
Future Fund Management Agency	0	0	0	0	0
Department of Human Services	483	636	788	739	712
Centrelink	2,294	2,564	2,650	2,607	2,604
Medicare Australia	438	619	691	730	729
Health Insurance Commission	147	0	0	0	0
Total	**3,853**	**4,723**	**4,700**	**4,546**	**4,522**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	706	791	802	845	832
AusAID	79	94	80	80	78
Australian Trade Commission	204	213	207	207	208
Total	**988**	**1,097**	**1,089**	**1,132**	**1,118**
Health and Ageing					
Department of Health and Ageing	569	605	587	585	588
National Blood Authority	9	10	10	9	9
Total	**579**	**615**	**597**	**594**	**597**
Immigration and Multicultural Affairs					
Department of Immigration and Multicultural Affairs	1,120	1,217	1,207	1,204	1,229
Total	**1,120**	**1,217**	**1,207**	**1,204**	**1,229**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	297	314	314	305	299
Tourism Australia	168	159	161	109	111
Total	**464**	**473**	**475**	**414**	**409**
Parliament					
Department of Parliamentary Services	120	122	123	125	127
Total	**120**	**122**	**123**	**125**	**127**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	80	124	118	65	65
National Water Commission	10	10	10	10	10
Total	**89**	**135**	**129**	**75**	**76**

Table A2: Departmental expenses by agency (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	224	221	216	217	218
Civil Aviation Safety Authority	120	119	121	124	126
National Capital Authority	19	19	19	19	19
Total	**364**	**359**	**356**	**360**	**363**
Treasury					
Department of the Treasury	142	141	131	127	128
Australian Bureau of Statistics	340	431	322	299	308
Australian Securities and Investment Commission	236	274	272	269	273
Australian Taxation Office	2,533	2,600	2,631	2,641	2,649
Australian Office of Financial Management	9	9	9	9	9
Total	**3,260**	**3,455**	**3,366**	**3,345**	**3,367**
Small agencies	**3,223**	**3,500**	**3,558**	**3,633**	**3,704**
Whole of government and inter-agency amounts(a)	**0**	**49**	**122**	**147**	**146**
Total departmental expenses	**49,946**	**53,945**	**54,369**	**54,067**	**55,349**

(a) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A3: Net capital investment by agency

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	499.8	-40.9	-147.0	-177.0	-67.0
Grains Research and Development Corporation	0.1	0.3	-0.2	-0.3	-0.2
Dairy Structural Adjustment Fund	0.0	0.0	0.0	0.0	0.0
Total	**499.9**	**-40.6**	**-147.2**	**-177.3**	**-67.3**
Attorney-General's					
Attorney-General's Department	12.8	26.0	-1.4	-3.5	-9.9
Australian Customs Service	33.0	25.5	1.4	-14.6	-2.0
Australian Federal Police	60.2	3.3	-3.4	-6.8	-8.2
Family Court of Australia	-0.8	-0.4	-0.5	-0.5	-0.4
High Court of Australia	-0.3	-0.5	-0.5	-0.6	-0.6
Total	**105.0**	**54.0**	**-4.3**	**-26.0**	**-21.1**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	-1.9	-1.7	3.9	72.3	-6.4
Australian Broadcasting Corporation	-20.0	22.5	10.5	7.5	-4.5
Australian Communications and Media Authority	-0.1	4.4	0.6	0.1	-1.9
Australian Sports Commission	40.5	9.9	-8.0	-7.9	-8.0
National Archives of Australia	1.3	15.3	12.0	12.0	16.7
National Gallery of Australia	12.1	19.9	-5.5	-5.2	-5.2
National Library of Australia	11.0	7.4	-1.0	-7.6	-7.6
National Museum of Australia	2.9	6.0	6.7	10.2	1.6
Special Broadcasting Service Corporation	-1.8	5.8	5.3	3.9	2.6
Total	**44.0**	**89.6**	**24.6**	**85.4**	**-12.7**
Defence					
Department of Defence	92.0	2,029.6	1,597.5	2,239.5	2,471.4
Defence Material Organisation	920.8	-7.1	-13.3	-11.8	-10.9
Defence Housing Authority	95.4	222.5	51.7	50.6	19.7
Department of Veterans' Affairs	9.7	8.8	8.8	6.0	13.7
Australian War Memorial	37.2	11.5	3.2	2.1	0.2
Total	**1,155.1**	**2,265.3**	**1,647.9**	**2,286.3**	**2,494.2**
Education, Science and Training					
Department of Education, Science and Training	-0.4	2.2	7.4	3.0	4.9
Australian Research Council	4.4	0.6	-0.6	-0.6	-0.7
Australian Nuclear Science and Technology Organisation	44.6	17.1	9.8	4.0	5.8
Commonwealth Scientific and Industrial Research Organisation	14.9	22.2	38.1	38.2	42.1
Total	**63.6**	**42.1**	**54.7**	**44.5**	**52.1**

Table A3: Net capital investment by agency (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	43.8	23.9	3.3	-11.0	1.2
Indigenous Business Australia	5.2	0.2	0.0	0.0	0.0
Comcare	-0.2	-0.3	-0.3	-0.3	-0.1
Total	**48.8**	**23.8**	**3.0**	**-11.3**	**1.0**
Environment and Heritage					
Department of Environment and Heritage	-1.7	0.6	-12.5	-13.4	-9.3
Bureau of Meteorology	13.1	11.7	15.0	5.2	4.6
Total	**11.4**	**12.4**	**2.4**	**-8.2**	**-4.7**
Families, Community Services and Indigenous Affairs					
Department of Families, Community Services Indigenous Affairs	168.7	8.1	-128.3	-1.3	-8.0
Aboriginal and Torres Strait Islanders Land Fund	0.0	0.0	0.0	0.0	0.0
Aboriginal and Torres Strait Islander Services	0.0	0.0	0.0	0.0	0.0
Total	**168.7**	**8.1**	**-128.3**	**-1.3**	**-8.0**
Finance and Administration					
Department of Finance and Administration	184.2	-92.2	105.4	46.2	-140.6
Australian Electoral Commission	-3.0	7.6	-1.2	1.3	5.0
Future Fund Management Agency	1.0	0.0	0.0	0.0	0.0
Department of Human Services	6.4	16.4	-3.2	-1.7	-7.5
Centrelink	42.9	147.5	27.4	-22.5	-43.0
Medicare Australia	129.8	4.8	-4.1	-4.9	-5.8
Health Insurance Commission	-131.9	0.0	0.0	0.0	0.0
Total	**229.4**	**84.1**	**124.3**	**18.5**	**-191.9**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	89.5	192.3	38.6	107.9	-34.6
AusAID	2.9	7.2	-1.7	-1.9	-0.5
Australian Trade Commission	13.5	16.2	3.1	-1.5	-1.5
Total	**105.9**	**215.7**	**40.0**	**104.5**	**-36.5**
Health and Ageing					
Department of Health and Ageing	6.9	158.0	-0.4	-8.1	-6.1
National Blood Authority	-5.8	27.7	1.5	1.2	1.3
Total	**1.1**	**185.6**	**1.1**	**-6.9**	**-4.8**
Immigration and Multicultural Affairs					
Department of Immigration and Multicultural Affairs	-5.1	390.3	21.6	-9.8	137.7
Total	**-5.1**	**390.3**	**21.6**	**-9.8**	**137.7**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	1.0	14.4	9.1	0.9	-3.9
Tourism Australia	4.1	0.0	0.1	-0.1	-0.2
Total	**5.1**	**14.4**	**9.2**	**0.8**	**-4.2**
Parliament					
Department of Parliamentary Services	-36.3	-20.9	-26.3	-30.2	-26.5
Total	**-36.3**	**-20.9**	**-26.3**	**-30.2**	**-26.5**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	12.8	8.6	-5.2	-1.7	-1.7
National Water Commission	0.4	-0.5	-0.5	0.2	-0.5
Total	**13.2**	**8.1**	**-5.7**	**-1.4**	**-2.1**

Table A3: Net capital investment by agency (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	2,191.6	-205.2	-689.9	-948.1	-313.8
Civil Aviation Safety Authority	4.1	-0.9	-1.2	-5.7	-3.8
National Capital Authority	9.2	3.9	4.0	3.4	1.1
Total	**2,205.0**	**-202.1**	**-687.0**	**-950.4**	**-316.5**
Treasury					
Department of the Treasury	-224.5	-29.9	0.4	0.4	-1.1
Australian Bureau of Statistics	26.4	9.4	-2.8	-2.7	0.0
Australian Securities and Investment Commission	3.9	8.6	-2.1	-1.6	-2.9
Australian Taxation Office	49.7	42.0	28.9	4.9	-5.2
Australian Office of Financial Management	-0.6	0.1	-0.5	-0.6	-0.1
Total	**-145.1**	**30.2**	**24.0**	**0.5**	**-9.3**
Small agencies	**398.4**	**206.8**	**88.5**	**67.5**	**43.9**
Whole of government and inter-agency amounts(a)	**-586.0**	**-90.1**	**-194.7**	**-208.7**	**-146.5**
Total net capital investment	**4,282.0**	**3,276.7**	**847.7**	**1,176.4**	**1,876.8**

(a) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A4: Capital appropriations by portfolio

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Agriculture, Fisheries and Forestry					
Department of Agriculture, Fisheries and Forestry	4	0	0	0	0
Grains Research and Development Corporation	0	0	0	0	0
Dairy Structural Adjustment Fund	0	0	0	0	0
Total	**4**	**0**	**0**	**0**	**0**
Attorney-General's					
Attorney-General's Department	14	28	8	7	0
Australian Customs Service	28	37	22	10	4
Australian Federal Police	64	38	36	20	8
Family Court of Australia	0	0	0	0	0
High Court of Australia	0	0	0	0	0
Total	**106**	**104**	**66**	**38**	**12**
Communications, Information Technology and the Arts					
Department of Communications, Information Technology and the Arts	2,001	5	8	2	0
Australian Broadcasting Corporation	0	14	13	11	0
Australian Communications and Media Authority	0	1	0	0	0
Australian Sports Commission	21	12	0	0	0
National Archives of Australia	0	0	0	0	0
National Gallery of Australia	4	22	4	4	4
National Library of Australia	7	5	7	1	1
National Museum of Australia	1	3	5	1	0
Special Broadcasting Service Corporation	6	5	4	3	3
Total	**2,040**	**67**	**41**	**22**	**8**
Defence					
Department of Defence	972	1,938	1,588	1,880	2,380
Defence Material Organisation	0	0	0	0	0
Defence Housing Authority	0	0	0	0	0
Department of Veterans' Affairs	6	3	2	1	1
Australian War Memorial	3	1	0	0	0
Total	**982**	**1,943**	**1,591**	**1,881**	**2,380**
Education, Science and Training					
Department of Education, Science and Training	9	2	4	3	5
Australian National Training Authority	0	0	0	0	0
Australian Research Council	0	0	0	0	0
Australian Nuclear Science and Technology Organisation	20	0	0	0	0
Commonwealth Scientific and Industrial Research Organisation	0	0	0	0	0
Total	**29**	**2**	**4**	**3**	**5**

Table A4: Capital appropriations by portfolio (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Employment and Workplace Relations					
Department of Employment and Workplace Relations	69	18	7	1	0
Indigenous Business Australia	14	57	38	42	33
Comcare	0	0	0	0	0
Total	**83**	**75**	**45**	**43**	**33**
Environment and Heritage					
Department of Environment and Heritage	7	5	0	0	0
Bureau of Meteorology	13	17	17	5	5
Total	**20**	**21**	**17**	**5**	**5**
Families, Community Services and Indigenous Affairs					
Department of Family and Community Services Indigenous Affairs	1	2	0	0	0
Aboriginal and Torres Strait Islanders Land Fund	0	0	0	0	0
Aboriginal and Torres Strait Islander Services	0	0	0	0	0
Total	**1**	**2**	**0**	**0**	**0**
Finance and Administration					
Department of Finance and Administration	1,730	1,131	1,058	1,225	1,093
Australian Electoral Commission	2	3	1	2	2
Future Fund Management Agency	0	0	0	0	0
Department of Human Services	0	9	6	1	0
Centrelink	57	95	29	0	0
Medicare Australia	1	14	3	0	0
Health Insurance Commission	4	0	0	0	0
Total	**1,793**	**1,251**	**1,097**	**1,229**	**1,095**
Foreign Affairs and Trade					
Department of Foreign Affairs and Trade	92	49	65	71	0
AusAID	36	29	15	8	6
Australian Trade Commission	9	8	5	0	0
Total	**137**	**87**	**85**	**79**	**6**
Health and Ageing					
Department of Health and Ageing	222	61	1	0	0
National Blood Authority	0	0	0	0	0
Total	**222**	**61**	**1**	**0**	**0**
Immigration and Multicultural Affairs					
Department of Immigration and Multicultural Affairs	36	116	47	29	20
Total	**36**	**116**	**47**	**29**	**20**
Industry, Tourism and Resources					
Department of Industry, Tourism and Resources	26	24	52	25	24
Tourism Australia	0	0	0	0	0
Total	**26**	**24**	**52**	**25**	**24**
Parliament					
Department of Parliamentary Services	0	14	11	11	12
Total	**0**	**14**	**11**	**11**	**12**
Prime Minister and Cabinet					
Department of Prime Minister and Cabinet	15	14	0	0	0
National Water Commission	0	0	0	0	0
Total	**15**	**14**	**0**	**0**	**0**

Table A4: Capital appropriations by portfolio (continued)

	Estimates		Projections		
	2005-06	2006-07	2007-08	2008-09	2009-10
	$m	$m	$m	$m	$m
Transport and Regional Services					
Department of Transport and Regional Services	35	104	6	5	5
Civil Aviation Safety Authority	0	0	0	0	0
National Capital Authority	2	2	2	2	2
Total	**37**	**106**	**8**	**7**	**7**
Treasury					
Department of the Treasury	118	68	49	37	25
Australian Bureau of Statistics	1	1	1	0	0
Australian Securities and Investment Commission	2	7	0	0	0
Australian Taxation Office	0	3	4	3	0
Australian Office of Financial Management	213,329	220,048	216,568	218,743	219,354
Total	**213,450**	**220,126**	**216,622**	**218,782**	**219,379**
Small agencies	**0**	**0**	**0**	**0**	**0**
Whole of government and inter-agency amounts(a)	**0**	**0**	**0**	**0**	**0**
Total capital appropriations	**218,982**	**224,012**	**219,686**	**222,155**	**222,985**

(a) Estimates of inter-agency transactions are included in the whole of government and inter-agency amounts. The entry for each portfolio does not include eliminations for inter-agency transactions within that portfolio.

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector

	Average staffing levels		
	2005-06	2006-07	Change
Agriculture, Fisheries and Forestry			
Department of Agriculture, Fisheries and Forestry	3,980	4,210	230
Australian Fisheries Management Authority	160	174	14
Australian Pesticides and Veterinary Medicines Authority	132	134	2
Australian Wine and Brandy Corporation	71	77	6
Biosecurity Australia	103	113	10
Cotton Research and Development Corporation	11	11	0
Dairy Structural Adjustment Fund	4	2	-2
Fisheries Research and Development Corporation	9	10	1
Forest and Wood Products Research and Development Corporation	7	7	0
Grains Research and Development Corporation	49	50	1
Grape and Wine Research and Development Corporation	12	12	0
Land and Water Resources Research and Development Corporation	42	42	0
Rural Industries Research and Development Corporation	24	25	1
Sugar Research and Development Corporation	8	8	0
Wheat Export Authority	15	4	-11
Total	**4,627**	**4,879**	**252**
Attorney-General's			
Attorney-General’s Department	981	1,126	145
Administrative Appeals Tribunal	161	166	5
Australian Crime Commission	505	514	9
Australian Customs Service	5,030	5,297	267
Australian Federal Police	4,770	4,793	23
Australian Institute of Criminology	47	45	-2
Australian Law Reform Commission	19	19	0
Australian Security Intelligence Organisation	1,003	1,088	85
Australian Transaction Reports and Analysis Centre (AUSTRAC)	130	183	53
Criminology Research Council	1	1	0
CrimTrac	70	87	17
Family Court of Australia	680	680	0
Federal Court of Australia	393	398	5
Federal Magistrates Service	123	149	26
High Court of Australia	100	100	0
Human Rights and Equal Opportunity Commission	92	98	6
Insolvency and Trustee Service Australia	260	265	5
National Native Title Tribunal	250	240	-10
Office of Film and Literature Classification	60	60	0
Office of Parliamentary Counsel	42	46	4
Office of the Director of Public Prosecutions	476	542	66
Office of the Privacy Commissioner	35	43	8
Total	**15,228**	**15,940**	**712**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2005-06	2006-07	Change
Communication, Information Technology and the Arts			
Department of Communications, Information Technology and the Arts	848	916	68
Australia Business Arts Foundation	29	24	-5
Australia Council	142	142	0
Australian Broadcasting Corporation	4,200	4,200	0
Australian Communications Media Authority	500	500	0
Australian Film Commission	276	279	3
Australian Film Television and Radio School	158	158	0
Australian National Maritime Museum	105	105	0
Australian Sports Commission	644	725	81
Australian Sports Anti-Doping Agency	53	59	6
Bundanon Trust	14	14	0
Film Australia	55	55	0
National Archives of Australia	452	452	0
National Gallery of Australia	228	222	-6
National Library of Australia	449	436	-13
National Museum of Australia	225	240	15
Netalert	6	3	-3
Special Broadcasting Service	790	798	8
Total	**9,174**	**9,328**	**154**
Defence			
Department of Defence - Military	51,189	51,091	-98
Department of Defence - Reserves	19,150	19,250	100
Department of Defence - Civilians	13,355	14,148	793
Defence Housing Authority	698	694	-4
Defence Materiel Organisation	4,426	4,620	194
Department of Veterans' Affairs	2,463	2,379	-84
Australian War Memorial	272	282	10
Total	**91,553**	**92,464**	**911**
Education, Science and Training			
Department of Education, Science and Training	2,060	2,145	85
Australian Institute of Aboriginal and Torres Strait Islander Studies	110	119	9
Australian Institute of Marine Science	168	162	-6
Australian Nuclear Science and Technology Organisation	855	860	5
Australian Research Council	70	75	5
Commonwealth Scientific and Industrial Research Organisation	6,030	5,860	-170
Teaching Australia - Australian Institute for Teaching and School Leadership Limited	16	20	4
The Carrick Institute for Learning and Teaching in Higher Education	11	15	4
Total	**9,320**	**9,256**	**-64**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2005-06	2006-07	Change
Employment and Workplace Relations			
Department of Employment and Workplace Relations	3,280	3,634	354
Australian Industrial Relations Commission and Australian Industrial Registry	227	227	0
Australian Building and Construction Commission	120	120	0
Australian Fair Pay Commission	5	20	15
Comcare	370	374	4
Equal Opportunity for Women in the Workplace Agency	20	20	0
Indigenous Business Australia	129	150	21
Office of Workplace Services	45	275	230
Total	**4,196**	**4,820**	**624**
Environment and Heritage			
Department of the Environment and Heritage	1,670	1,633	-37
Bureau of Meteorology	1,355	1,342	-13
Director of National Parks	275	272	-3
Great Barrier Reef Marine Park Authority	195	197	2
Office of the Renewable Energy Regulator	11	12	1
Sydney Harbour Federation Trust	47	47	0
Total	**3,553**	**3,503**	**-50**
Families, Community Services and Indigenous Affairs			
Department of Families, Community Services and Indigenous Affairs	1,857	2,336	479
Aboriginal Hostels Limited	385	409	24
Australian Institute of Family Studies	55	55	0
Indigenous Land Corporation	130	130	0
Torres Strait Regional Authority	50	50	0
Total	**2,477**	**2,980**	**503**
Finance and Administration			
Department of Finance and Administration	1,194	1,303	109
Australian Electoral Commission	748	763	15
Commonwealth Grants Commission	44	48	4
Commonwealth Superannuation Administration (ComSuper)	382	402	20
Future Fund Management Agency	2	13	11
Department of Human Services	4,815	5,817	1,002
Centrelink	22,900	25,285	2,385
Medicare Australia	4,830	4,797	-33
Total	**34,915**	**38,428**	**3,513**
Foreign Affairs and Trade			
Department of Foreign Affairs and Trade	3,199	3,328	129
AusAID	482	518	36
Australian Trade Commission	1,094	1,115	21
Australia-Japan Foundation	6	7	1
Australian Centre for International Agricultural Research	63	64	1
Total	**4,844**	**5,032**	**188**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2005-06	2006-07	Change
Health and Ageing			
Department of Health and Ageing	3,737	3,957	220
Aged Care Standards and Accreditation Agency	184	196	12
Australian Institute of Health and Welfare	192	197	5
Australian Radiation Protection and Nuclear Safety Agency	126	126	0
Food Standards Australia New Zealand	122	122	0
General Practice Education and Training Limited	29	31	2
National Blood Authority	40	40	0
National Institute of Clinical Studies Australia Limited	25	30	5
Private Health Insurance Administration Council	15	15	0
Private Health Insurance Ombudsman	8	8	0
Professional Services Review	20	30	10
Total	**4,498**	**4,752**	**254**
Immigration and Multicultural Affairs			
Department of Immigration and Multicultural Affairs	5,963	5,999	36
Migration Review Tribunal	174	174	0
Refugee Review Tribunal	190	190	0
Total	**6,327**	**6,363**	**36**
Industry Tourism and Resources			
Department of Industry, Tourism and Resources	1,817	1,852	35
Geoscience Australia	642	642	0
IP Australia	796	848	52
National Offshore Petroleum Safety Authority	34	36	2
Tourism Australia	252	252	0
Total	**3,541**	**3,630**	**89**
Parliament			
Department of Parliamentary Services	820	820	0
Department of the House of Representatives	166	166	0
Department of the Senate	159	158	-1
Total	**1,145**	**1,144**	**-1**
Prime Minister and Cabinet			
Department of the Prime Minister and Cabinet	475	564	89
Australian National Audit Office	300	300	0
Australian Public Service Commission	182	190	8
National Water Commission	42	48	6
Office of National Assessments	107	137	30
Office of the Commonwealth Ombudsman	145	137	-8
Office of the Inspector-General of Intelligence and Security	6	9	3
Office of the Official Secretary to the Governor-General	87	91	4
Total	**1,344**	**1,476**	**132**

Table A5: Estimates of average staffing level (ASL) of agencies in the Australian Government general government sector (continued)

	Average staffing levels		
	2005-06	2006-07	Change
Transport and Regional Services			
Department of Transport and Regional Services	1,210	1,339	129
Australian Maritime Safety Authority	141	143	2
Civil Aviation Safety Authority	696	675	-21
National Capital Authority	80	87	7
Total	**2,127**	**2,244**	**117**
Treasury			
Department of the Treasury	837	869	32
Australian Bureau of Statistics	2,832	3,300	468
Australian Competition and Consumer Commission	511	578	67
Australian Office of Finance Management	35	35	0
Australian Prudential Regulation Authority	572	582	10
Australian Securities and Investments Commission	1,472	1,578	106
Australian Taxation Office	21,529	20,538	-991
Corporations and Market Advisory Committee	3	3	0
Inspector General of Taxation	6	7	1
National Competition Council	20	15	-5
Productivity Commission	200	200	0
Royal Australian Mint	127	132	5
Total	**28,144**	**27,837**	**-307**
TOTAL (for all general government sector agencies)	**227,013**	**234,076**	**7,063**

(a) This table includes estimates of ASL provided by general government sector agencies. ASL figures reflect the average number of employees receiving salary or wages over the financial year, with adjustments for casual and part-time staff, to show the full-time equivalent. This also includes non-uniformed staff and overseas personnel.

STATEMENT 11: STATEMENT OF RISKS

A range of factors may influence the actual budget outcome in future years. The *Charter of Budget Honesty Act 1998* requires these factors be disclosed in a Statement of Risks in each Budget and Mid-Year Economic and Fiscal Outlook. This statement outlines the fiscal risks and the contingent liabilities which may affect the budget balances.

STATEMENT 11: STATEMENT OF RISKS

The forward estimates of revenue and expenses in the 2006-07 Budget incorporate assumptions and judgments based on the best information available at the time of publication. A range of factors may influence the actual budget outcome in future years. The disclosure of these factors in this statement increases the transparency of the fiscal projections and ensures they remain 'on-balance' estimates.

Events that could affect fiscal outcomes include:

- changes in economic and other parameters;
- matters not included in the fiscal forecasts because of uncertainty about their timing, magnitude and/or likelihood; and
- the realisation of contingent liabilities.

RISKS TO THE BUDGET — OVERVIEW

Economic and other parameters

The revenue and expense estimates and projections are based on a range of economic and other parameters. If the economic outlook were to differ from that presented in Statement 3, the revenue and expense estimates and projections would also change. Statement 3 discusses risks to the economic forecasts. Statement 2 discusses the sensitivity of revenue and expense estimates to changes in the major economic parameters.

Fiscal risks

Fiscal risks are general developments or specific events that may affect the fiscal outlook. Some developments or events simply raise the possibility of some fiscal impact. In other cases, some fiscal impact may be reasonably certain, but it will not be included in the forward estimates because the timing or magnitude is not known. Fiscal risks may affect expenses and/or revenue and may be positive or negative on revenue, expenses and/or the budget balance. Contingent liabilities are a specific category of fiscal risks.

Contingent liabilities

Contingent liabilities are defined by the accounting standard AASB 137, which came into effect on 1 July 2005. Broadly, they represent possible costs to the Australian Government arising from past events that the outcome of future events not within the control of the Government will confirm. Contingent liabilities include loan guarantees, non-loan guarantees, warranties, indemnities, uncalled capital and letters of comfort. These possible costs are in addition to those recognised as liabilities in the consolidated financial statements of the Australian Government general government sector.

The Australian Government's major exposure to contingent liabilities arises from legislation guaranteeing certain liabilities of Australian Government controlled financial institutions (the Reserve Bank of Australia and the Export Finance and Insurance Corporation) and the now fully privatised Commonwealth Bank of Australia. To help manage these exposures, strategies are in place which aim to ensure the underlying strength and viability of the entities, so that the guarantees are not triggered.

Another class of contingent liability is uncalled capital, which reflects a financial commitment to an institution where no promissory note is issued by the Australian Government. Uncalled capital is primarily associated with international financial institutions such as the International Bank for Reconstruction and Development, the Asian Development Bank, the European Bank for Reconstruction and Development and the Multilateral Investment Guarantee Agency. When promissory notes are issued, such as in the case of the International Monetary Fund, the amounts are recorded in the general government balance sheet, so contingent liabilities (or assets) are not shown for those amounts.

Details of fiscal risks and contingent liabilities

Contingent liabilities and other fiscal risks with a possible impact on the forward estimates greater than $20 million in any one year, or $40 million over the forward estimates period, are listed below.

Information on fiscal risks takes account of Parliament's decisions and other developments until the close of parliamentary business on 30 April 2006. In general, information on contingent liabilities is based on information provided by Australian Government departments and agencies and is current to 31 March 2006. However, in some cases other dates are used and are noted in the relevant section.

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

Table 1: Summary of material changes to Statement of Risks since 2005-06 Budget and Mid-Year Economic and Fiscal Outlook[(a)]

Fiscal risks — revenue	Status
Finance and Administration	
Asset sales — Telstra	Modified
Treasury	
General interest charge on Australian Taxation Office audit amendments affecting pre-2000 assessments	Deleted
Contingent liabilities — quantifiable	
Communications, Information Technology and the Arts	
Litigation	Deleted
Defence	
Indemnities	Modified
Finance and Administration	
Australian Industry Development Corporation	Modified
Foreign Affairs and Trade	
Export Finance and Insurance Corporation	Modified
Industry, Tourism and Resources	
Timor Sea Designated Authority — litigation	Deleted
Transport and Regional Services	
Maritime industry reform	Modified
Treasury	
International financial institutions — uncalled capital subscriptions	Modified
Reserve Bank of Australia — guarantee	Modified
Contingent liabilities — unquantifiable	
Attorney-General's	
Ocean surveillance	Modified
Education, Science and Training	
Australian Nuclear Science and Technology Organisation — make-good provision	New
Employment and Workplace Relations	
COMCARE liability for additional workers' compensation payments	New
Environment and Heritage	
Antarctic — make-good provision	New
Finance and Administration[(b)]	
Australian Industry Development Corporation — board members' and management indemnity	Consolidated
ASC Pty Ltd — Australian Government shareholding	Consolidated
ASC Pty Ltd — directors' indemnities	Consolidated
Australian Technology Group — directors' indemnities	Consolidated
ComLand Limited — directors' indemnities	Consolidated
ComLand Limited — site contamination	Consolidated

Table 1: Summary of material changes to Statement of Risks since 2005-06 Budget and Mid-Year Economic and Fiscal Outlook[(a)] (continued)

Contingent liabilities — unquantifiable (continued)	Status
Finance and Administration[(b)] (continued)	
Employment National Limited — board members' and Chief Executive Officer's indemnity	Consolidated
Indemnities relating to other former asset sales, privatisations and IT outsourcing projects	Modified
Potential claims relating to superannuation benefits	Modified
Sydney Airports Corporation Limited, Bankstown, Camden and Hoxton Park Airports — directors' indemnities	Consolidated
Telstra Corporation Limited — company, directors and senior executives' indemnities	New
Tuggeranong Office Park Pty Ltd — shareholder indemnity	Modified
Health and Ageing	
Guarantee Scheme for aged care accommodation bonds	New
Immigration and Multicultural Affairs	
Claim of unlawful detention on Nauru	Deleted
Industry, Tourism and Resources	
Liability for costs incurred in a National Liquid Fuel Emergency	New

(a) Risks appearing in this Statement but not listed in the table above are substantially unchanged since disclosed in Budget Paper No. 1, *Budget Strategy and Outlook 2005-06*, Statement 11 or in *Mid-Year Economic and Fiscal Outlook 2005-06*, Appendix D.
(b) Risks classified as consolidated risks are now reflected in the entry 'Indemnities relating to other former assets sales, privatisations and IT outsourcing projects'.

FISCAL RISKS — REVENUE

The Government's revenue and policy measure forecasts, like all forecasts, are subject to a margin of error. Over the past 20 years, the errors associated with the forecasts of cash receipts have not been significantly different from zero. Over this period, the average error was 0.9 per cent, with the errors varying around this average by 2.7 percentage points.

There are not enough observations to assess the forecasting performance for accrual revenue, however, in recent years revenue has grown more strongly than forecast. The revenue forecasting methodology has been adjusted from the 2005-06 Budget to align the revenue forecasts and projections more closely to recent experience (see Budget Paper No. 1, *Budget Strategy and Outlook 2005-06*, Box 1 in Statement 5).

While many of the forecasts are reported to the nearest million dollars for budget accounting purposes, they should not be interpreted as implying an equivalent level of forecast precision.

The general and specific risks influencing the accuracy of the revenue forecasts are outlined below.

General risks

The estimates and projections of revenue are subject to a number of general pressures that can affect taxation collections. These general pressures include tax avoidance, developments in communications technology and workplace arrangements, court decisions and Australian Taxation Office rulings. These pressures may result in a shift in the composition of taxation collected from the various tax bases and/or a change in the size of the tax base. The revenue forecasts include an appropriate allowance for these factors, given the data available.

Specific risks

Finance and Administration

Asset sales — Telstra

The forward estimates include the effect of the sale of the Australian Government's shareholding in Telstra, noting that the level of proceeds and costs will depend, inter alia, on the prevailing levels of world equity markets at the time of sale and that the timing and structure of the sale could be adjusted if circumstances are considered unlikely to provide an appropriate return to taxpayers.

Treasury

Renegotiation of withholding tax rates in certain Australian double tax treaties

The Australian Government is renegotiating its double tax treaties with several countries. Depending on the negotiated outcomes, changes to these treaties could have positive or negative revenue effects.

FISCAL RISKS — EXPENSES

Agriculture, Fisheries and Forestry

Exceptional Circumstances assistance for drought-affected farmers

Exceptional Circumstances assistance is available, subject to eligibility criteria, to drought-affected farmers by way of interest rate subsidies and/or income support. The forward estimates assume that there will be neither new drought declarations nor extensions of existing declarations. A continuation of adverse seasonal conditions or a return to severe drought conditions could result in higher than expected expenses for these forms of assistance. It is not possible to quantify the cost arising from such potential developments as this depends on the intensity, duration and scale of future drought conditions.

Health and Ageing

Immunisation funding mechanism

Future vaccine technology will result in new vaccines changing the profile of vaccine usage (for example, multivalent vaccines which combine several vaccines into one) and, as a consequence, could result in higher costs. It is not possible to quantify the potential fiscal risk arising from these factors.

Medicare Benefits Schedule and Pharmaceutical Benefits Scheme

From time to time items are added to, or removed from, the Medicare Benefits Schedule and Pharmaceutical Benefits Scheme. Major technological advances in medicines or medical procedures, shifts in Pharmaceutical Benefits Scheme usage patterns, or doctors' prescribing and charging practices may result in unexpected increases in expenses that exceed the provision in the forward estimates. It is not possible to quantify the potential fiscal risk arising from these factors.

Transport and Regional Services

Airservices Australia

On 31 August 2004, the Minister for Transport and Regional Services, pursuant to section 16 of the *Airservices Act 1995* (the Act), gave a direction to Airservices Australia to provide an operating control tower and approach radar control services in certain volumes of airspace. Section 16(4) of the Act provides that Airservices Australia may seek reimbursement from the Australian Government for any financial detriment it suffers as a result of complying with a direction. At this time, the quantum or nature of any financial detriment is uncertain, as is the nature of any consequent fiscal risk to the budget.

CONTINGENT LIABILITIES — QUANTIFIABLE

Defence

Indemnities

The Department of Defence (Defence) and the Defence Materiel Organisation (DMO) carry an extensive range of indemnities and undertakings, normally of a short-term nature, relating to business, training activities and other arrangements involving contracts, agreements and other Defence and DMO activities. Indemnities issued cover potential losses or damages for which the Australian Government would be liable.

There are 374 instances of contingencies that are unquantifiable and 197 instances of quantifiable contingencies to the value of $5.3 billion. While these contingencies are considered remote, they have been reported in aggregate for completeness.

Finance and Administration

Australian Industry Development Corporation

Under the *Australian Industry Development Corporation Act 1970* certain obligations of the Australian Industry Development Corporation (AIDC) are guaranteed by the Australian Government. As at 31 December 2005, AIDC's contingent liabilities, subject to Australian Government guarantee, were approximately $125 million in respect of guarantees and credit risk facilities.

In addition, AIDC had outstanding Australian Government guaranteed borrowings which totalled approximately $336 million as at the most current valuation of 31 December 2005. These borrowing obligations have been matched by AIDC's holdings of Australian Government guaranteed securities of similar value, largely eliminating the Australian Government's guarantee exposure. These securities were purchased on market by UBS Warburg and paid to AIDC as consideration for UBS Warburg's purchase of AIDC Limited's (a subsidiary of AIDC) financial assets. UBS AG, the international parent company that has taken over from UBS Warburg, manages this borrowing portfolio on behalf of AIDC. The UBS AG arrangement also provides a guarantee to cover any cash flow differences between the interest rate and maturity profiles of the matched borrowings and securities, together with any exchange rate movements in the borrowings. The Australian Government's contingent exposure to these borrowings is therefore negligible and is consequently recorded as zero.

Litigation

The Department of Finance and Administration is involved in litigation where a counter-claim for damages has been lodged against the Australian Government. The counter-claim, which will be vigorously defended by the Australian Government, seeks damages of $4.3 billion although the basis for this amount is yet to be fully provided.

Sale of Sydney Airports Corporation Limited

An indemnity has been provided to Southern Cross Airports Corporation as purchaser of the Sydney Airports Corporation Limited in the event of a liability arising under Chapter 3 of the *Duties Act 1997* (New South Wales) by reason of the sale of shares in Sydney Airports Corporation Limited constituting a relevant acquisition in a land-rich private corporation. In the event the liability arises it is estimated to be between $221.2 million and $282.8 million.

Foreign Affairs and Trade

Export Finance and Insurance Corporation

The Australian Government guarantees the due payment by the Export Finance and Insurance Corporation (EFIC) of money that is, or may at any time become, payable by EFIC to any body other than the Australian Government. The Australian Government also has in place a $200 million callable capital facility available to EFIC on request to cover liabilities, losses and claims. As at 30 April 2006, the Australian Government's total contingent liability was $3.0 billion, comprising EFIC's liabilities to third parties ($2.5 billion) and EFIC's overseas investments insurance, contracts of insurance and guarantees ($0.6 billion).

Immigration and Multicultural Affairs

Immigration detention services

The contract with GSL (Australia) Pty Ltd commenced on 1 September 2003, at which time the Australian Government agreed to limit GSL's exposure under the liability regime of the contract. While the general contract requires GSL to indemnify the Australian Government for certain claims of losses, the Australian Government has agreed to share the risk. Subject to certain conditions, GSL has been indemnified against claims of losses above a fixed amount to a capped amount. Where claims exceed the cap in any financial year, responsibility for the excess reverts to GSL.

A further limitation of liability has been provided in relation to loss or damage to Australian Government property or equipment as a result of the actions of detainees. Under the contract, GSL's liability for detainee damage is subject to an annual limit, unless claims of losses exceed an agreed cap.

Transport and Regional Services

Code Management Company — indemnity for the Code of Practice for the Defined Interstate Rail Network

The Code Management Company (CMC) is a company owned by the Australasian Railway Association whose members include all of Australia's major rail operators and track owners and representatives from smaller companies. The Australian Government has provided an indemnity to CMC against any loss or expense that occurred prior to the transfer of ownership from the Commonwealth relating to the correct use or application of the Code of Practice for the Defined Interstate Rail Network. The Code sets out a national approach to operational and engineering practices, including uniform standards for safe working, train operations and freight loading specifications. The indemnity is limited to an aggregate of $50 million for a period of six years from the date of transfer of ownership and expires on 15 July 2009.

Maritime industry reform

On 18 August 1998, the Australian Government provided a guarantee to cover borrowings made by the Maritime Industry Finance Company Limited to finance redundancy-related payments in the stevedoring and maritime industries. Outstanding borrowings covered by the guarantee are $92 million.

Treasury

Guarantees under the Commonwealth Bank Sale Act

Under the terms of the *Commonwealth Bank Sale Act 1995*, the Australian Government has guaranteed various superannuation and other liabilities amounting to around $12.8 billion. Of this amount, $9.3 billion was attributable to liabilities of the Commonwealth Bank of Australia at 30 September 2004 and $3.5 billion was attributable to liabilities of the Commonwealth Bank Officers' Superannuation Corporation at 30 June 2004.

International financial institutions — uncalled capital subscriptions

This contingent liability relates to the value of the uncalled portion of the Australian Government's shares in the International Bank for Reconstruction and Development (US$2.8 billion — estimated value A$3.9 billion), the Asian Development Bank (US$2.3 billion — estimated value A$3.2 billion), the European Bank for Reconstruction and Development (US$81.7 million plus €77.5 million — estimated value A$245.7 million), and the Multilateral Investment Guarantee Agency (US$26.5 million — estimated value A$37.0 million).

Reserve Bank of Australia — guarantee

This contingent liability relates to the Australian Government's guarantee of the liabilities of the Reserve Bank of Australia. It is measured as the Bank's total liabilities excluding capital, reserves and Australian Government deposits. The major component of the Bank's liabilities are notes (that is, currency) on issue. Notes on issue amount to $38 billion and the total guarantee is $51.6 billion.

CONTINGENT LIABILITIES — UNQUANTIFIABLE

Attorney-General's

Indemnities relating to the Air Security Officer programme

The Australian Government has entered into indemnity agreements with Australian airlines that agree to fly aircraft with Air Security Officers on board. The indemnity agreements limit the Australian Government's exposure to a maximum of $2 billion per incident. The indemnity applies to the extent that any loss is not covered by existing relevant insurance policies held by the airline and only applies where the airline(s) can prove that an action on the part of an Air Security Officer under or in connection with the Air Security Officer programme caused a loss.

Integrated Cargo System

In October 2005, the Australian Customs Service (Customs) implemented a new Integrated Cargo System for imports. Subsequent technical and business issues resulted in the delayed movement of some cargo. Customs has received claims for reimbursement of costs incurred by some importers in relation to the implementation of the new system. The extent of any potential liability cannot be quantified at this stage.

Native title agreements — access to geospatial data

The Australian Government has entered into agreements with State and Territory government bodies and/or their agents to access their geospatial data. The data is essential to support the National Native Title Tribunal in achieving its outcome. Under these agreements, the Australian Government provides indemnities against third party claims arising from errors in the data.

Native title costs

The Australian Government has offered to assist the States in meeting compensation costs associated with native title. The amounts that might be paid by the Australian Government will be subject to the terms of financial assistance agreements being negotiated with the States, and liabilities arising from the 1998 amendments to the *Native Title Act 1993*. The Australian Government's liability cannot be quantified due to uncertainty about the number and effect of compensable acts, both in the past and in the future, and the value of native title affected by those acts. Similarly, it is not possible to quantify the liability for compensable acts for which the Australian Government may be directly liable.

The Australian Government has also offered to assist the States with the costs of bodies performing native title functions under state legislation. The extent of this assistance will depend on the existence of such bodies, the timing of their recognition and the extent of their use.

Ocean surveillance

The Australian Government has entered into contractual arrangements with P&O Maritime Services for the provision of maritime charter services until June 2010 to facilitate the Australian Customs Service and the Department of Agriculture, Fisheries and Forestry armed patrols of Australia's exclusive economic zone.

The Australian Government has indemnified P&O Maritime Services against certain claims arising from the discharge of firearms or munitions, or where a steaming party is deployed to crew a seized vessel back to an Australian port.

Communications, Information Technology and the Arts

Art Indemnity Australia

Art Indemnity Australia is a programme through which the Australian Government indemnifies cultural objects loaned to exhibitions displayed in Australian museums and galleries. The exact amounts involved will vary with the exchange rate applying at the time any claim for loss or damage to an artwork or heritage object loaned from overseas is paid, and the extent of any loss or damage. Most of the Australian

Government risk in indemnifying exhibitions is insured through Comcover. Uninsurable risk continues to be borne solely by the Australian Government.

Defence

ADI Limited — HMAS *Westralia* indemnity

The Department of Defence is subject to claims by ADI Ltd for indemnity for uninsured losses relating to the fire on HMAS *Westralia*. This claim is under the 1999 deed of indemnity given by the Australian Government to Transfield Thompson-CSF Investments Pty Ltd now known as ADI Group Pty Ltd.

ADI Limited — officers and directors' indemnities

Under the sale agreements for ADI Limited, the Australian Government had agreed to indemnify the directors, officers and employees for claims and legal costs associated with assistance related to the sale of the Australian Government's shares in the company. The Australian Government has provided an indemnity to ADI Limited for uninsured losses relating to specific heads of claims.

ADI Limited — sale

ADI Group Pty Ltd has initiated litigation in relation to alleged non-disclosure issues associated with the sale of ADI Ltd by the Australian Government. A claim for damages by the purchasers was lodged in October 2005.

ASC Pty Ltd — Australian Government indemnities provided to Electric Boat Corporation under the services agreement

In early October 2002, the Department of Defence entered into a services agreement with Electric Boat Corporation (EB) and its subsidiary Electric Boat Australia (EBA) to provide technical and commercial support to ASC Pty Ltd as it transitioned from being a producer of submarines to an agency for Through-Life Support. EB/EBA staff commenced at ASC Pty Ltd on 14 October 2002. The initial services agreement ran for three years and the Australian Government has taken up the option to extend the agreement by a further three years. The extension has been incorporated into the Strategic Agreement for Through-Life Support of the Collins Class Submarines with ASC Pty Ltd.

Under this agreement, EB and EBA are provided with a warranty by the Australian Government and ASC Pty Ltd that the Australian Government and ASC Pty Ltd have the right to provide EB/EBA with confidential and other information and the Australian Government provides an indemnity to EB and EBA against claims arising from a breach of that warranty.

The Australian Government also indemnifies EB and EBA against claims arising from property loss or personal injury resulting from a defect in the operation or performance of a Collins Class submarine, other than caused by unlawful conduct, gross negligence or wilful misconduct of EB or EBA, against claims exceeding the greater of US$1 million or profit earned by EB under the agreement.

Decontamination of Defence sites

The Department of Defence is currently undertaking a large multi-year project to identify and quantify its land, building and infrastructure decontamination obligations. There is a significant number of contaminated sites where the estimated decontamination costs have not yet been quantified and may not be quantified for some time into the future.

HMAS *Melbourne* and HMAS *Voyager* damages claims

Former crew members of HMAS *Melbourne* have instituted legal proceedings against the Australian Government claiming damages for injuries allegedly caused by the HMAS *Voyager*/HMAS *Melbourne* collision on 10 February 1964. One hundred and twenty-seven claims remain current. Eighty-six of the current claims are statute barred under applicable state laws. In those cases, the plaintiffs will require an extension of time prior to progressing their claims for damages. A number of dependency claims arising from that collision have also been foreshadowed by the dependants of deceased former members of the crew of HMAS *Voyager*. Further claims are likely to be made in connection with the collision.

Litigation cases

The Department of Defence is involved in a wide range of litigation and other claims for compensation and/or damages that may result in litigation where the matters have yet to be finalised by negotiation or, where required, litigation. Various claims, the subject of cases that have yet to be heard, are part-heard or are subject to an appeal, await a decision on what (if any) damages and/or costs should be paid to the claimant. The litigated and non-litigated claims include common law liability claims and claims arising from complaints to the Human Rights and Equal Opportunity Commission. The litigation includes asbestos claims and claims from injury resulting from the F-111 Deseal/Reseal programmes. Claims have been received for damage caused by the use of Defence Practice Areas and from the presence of unexploded World War II ordnance. At any given point, there are about 400 claims. Presently, they have an estimated value in excess of $145 million. There is identified potential for claims within the above from known incidents of non-military asbestos exposure and the F-111 Deseal/Reseal project of some 130 claims with a value of some $30 million.

Military Superannuation and Benefits Scheme — indemnity

The Military Superannuation and Benefits Scheme (MSBS) provides occupational superannuation benefits for members of the Australian Defence Force. Much of the day-to-day administration associated with the MSBS is conducted by ComSuper. Under the *Military Superannuation and Benefits Act 1991* the actions of ComSuper and its Commissioner are deemed to be those of the Military Superannuation and Benefits Board (MSB Board). Defence has indemnified the MSB Board for certain specified claims that are made in relation to acts of ComSuper and/or its Commissioner that are not recoverable elsewhere.

Education, Science and Training

Australian Nuclear Science and Technology Organisation — indemnity

The Australian Government has indemnified the Australian Nuclear Science and Technology Organisation and its officers from liability that might be incurred from the conduct of activities authorised under the *Australian Nuclear Science and Technology Organisation Act 1987*. This indemnity is additional to commercial insurance covers obtained from the Comcover Insurance Pool and other insurers.

Australian Nuclear Science and Technology Organisation — make-good provision

The Australian Nuclear Science and Technology Organisation is required to recognise a provision associated with the decommissioning and restoration of assets, including the existing and new reactors. This requirement is mandated upon adoption of the Australian equivalents to the International Financial Reporting Standards.

The Australian Nuclear Science and Technology Organisation's liability cannot be quantified at this stage as work is still being undertaken to determine the quantum of the provision required.

Employment and Workplace Relations

Comcare liability for additional workers' compensation payments

The Federal Court's decision in *Comcare v Etheridge* [2006] has had the effect of increasing the Australian Government's liability to pay compensation under the *Safety, Rehabilitation and Compensation Act 1988* (the SRC Act) to some additional classes of workers for mesothelioma and similar diseases with a long latency period.

While the compensation amount involved in the particular case (including legal costs) has already been paid by Comcare, there is the potential for further liabilities to be identified in relation to other workers' compensation cases, either already accepted, or likely to emerge in the future.

Environment and Heritage

Antarctic — make-good provision

The Department of the Environment and Heritage is required to recognise make-good provisions for the future return to the original environmental condition of the Antarctic and sub-Antarctic territories over which Australia has control, in accordance with the conversion to the Australian equivalents to the International Financial Reporting Standards.

The Australian Government's liability cannot be quantified at this stage as work is still being undertaken to determine the exact quantum of this provision.

Finance and Administration

Indemnities for the Reserve Bank of Australia and private sector banks

Under agencies' contracts for transactional banking services, the Australian Government has indemnified the Reserve Bank of Australia and contracted private sector banks. These banks are indemnified against loss and damage arising from error or fraud by the agency, or transactions made by the bank with the authority of the agency.

Indemnities relating to other former asset sales, privatisations and IT outsourcing projects

Ongoing indemnities have been given in respect of a range of asset sales, privatisations and IT outsourcing projects that have been conducted by the Department of Finance and Administration (Finance), and the former Office of Asset Sales and Commercial Support and its predecessors. The probability of an action being made under one of these indemnities diminishes over time. Details of indemnities in respect of the other asset sales and privatisations have been provided in previous Budget and Mid-Year Economic and Fiscal Outlook papers, and previous annual reports for Finance and the Office of Asset Sales and Commercial Support.

Indemnities (including the year they were raised) are still current for: ADI Ltd (1998), Australian Airlines (1991), Australian Industry Development Corporation (1996), Australian Multimedia Enterprise (1997), Australian National Rail Commission and National Rail Corporation Ltd (1997 and 2000), Australian Submarine Corporation Limited (2000), Australian Technology Group (1986), ComLand Limited (2004), Bankstown Airport Limited (2002), Camden Airport Limited (2002), Commonwealth Accommodation and Catering Services (1988), Commonwealth Bank of Australia (1993 to 1996), Commonwealth Funds Management and Total Risk Management (1996 to 1997), Employment National Limited (2003), Essendon Airport Ltd (2001), Federal Airports Corporation's Airports (1995 to 1997), Home Loans Insurance Commission Ltd (1996), Health Insurance Commission (2000), Hoxton Park Airport Limited (2002), National Transmission Network (1999), Sydney Airports Corporation Limited (2001), Telstra (1996 and 1999), Wool International (1999). The Department does not currently expect any action to be taken in respect of these indemnities.

Potential claims relating to superannuation benefits

On 4 March 2005, the Supreme Court of the Australian Capital Territory found against the Commonwealth of Australia on a claim for negligence and breach of contract relating to superannuation benefits for a former employee of the Department of the Interior. This is considered to be a test case for several hundred named plaintiffs. There is potential for more claims to arise from other former employees depending on the terms of the final judgment. The Commonwealth's appeal was heard by the full bench of the ACT Supreme Court in February 2006. The judgment is expected to be handed down in June 2006.

Telstra Corporation Limited — company, directors and senior executives' indemnities

Certain indemnities have been provided to Telstra, its directors and selected senior executives in connection with their assistance in the preparation for the possible sale of the Australian Government's shares in Telstra. The indemnities cover liabilities that may arise from actions undertaken in support of the further sale of Telstra.

Tuggeranong Office Park Pty Ltd — shareholder indemnity

As part of the arrangements for Tuggeranong Office Park, the Australian Government can acquire the shares of the Tuggeranong Office Park Pty Ltd for $100 subject to certain conditions. In its capacity as purchaser of the shares, the Australian Government has issued a conditional indemnity to each shareholder for all 'losses, liabilities, costs, expenses and damages' incurred by virtue of their shareholding.

Foreign Affairs and Trade

Export Finance and Insurance Corporation — board members' and senior management indemnities

The Australian Government has provided certain indemnities to the Export Finance and Insurance Corporation (EFIC) board members and senior management to protect against civil claims and legal expenses for unsuccessful criminal claims relating to the implementation of EFIC's alliance/divestment of its short-term export credit insurance business.

Health and Ageing

Blood and blood products liability cover

A National Managed Fund (NMF) has been established which pools the liability risks associated with the supply of blood and blood products by the Australian Red Cross Blood Service (ARCBS) between the Australian Government, the ARCBS and the States and Territories. The NMF is covered by a Memorandum of Understanding (MoU) between the Australian Government, States and Territories, and the ARCBS. This will be amended to incorporate the operations of the Jurisdictional Blood Committee (JBC) and the National Blood Authority. The MoU provides for the parties to contribute to the NMF taking into account potential claims payments; the level of funds in the NMF and investment earnings; and a prudential allowance for liabilities incurred but not yet the subject of claims. If there are insufficient funds to cover claim costs, the JBC considers a report provided by the National Funds Manager to determine the level of funds required. Each party must contribute funds, as determined by JBC, in accordance with allocation provisions prevailing at the time. Under the MoU, the blood and blood products liability cover for the ARCBS remains in force until all parties agree to terminate the arrangements from an agreed date.

CSL Limited

CSL Limited is indemnified against claims made by persons who contract specified infections from specified products and against employees contracting asbestos-related injuries. CSL Limited has unlimited cover for most events that occurred before the sale of CSL Limited on 1 January 1994, but has more limited cover for a specified range of events that occurred during the operation of the Plasma Fractionation Agreement from 1 January 1994 to 31 December 2004. Where alternative cover was not arranged by CSL Limited, the Australian Government may have a contingent liability. Given the open-ended nature of some of the indemnities, damages and risk cannot be quantified. No similar indemnities have been given to CSL Limited in the new Plasma Products Agreement operating from 1 January 2005.

Guarantee Scheme for aged care accommodation bonds

A Guarantee Scheme has been established through the *Aged Care (Bond Security) Act 2006* and *Aged Care (Bond Security) Levy Act 2006*. Under the Guarantee Scheme, if a provider becomes insolvent or bankrupt and is unable to repay outstanding bond balances to aged care residents, the Australian Government will step in and repay the bond balances owing to each resident. In return, residents will assign their right to the Australian Government to pursue the defaulting provider to recover the accommodation bond money paid out. In the event the Australian Government cannot recover the full amount from the defaulting provider, it may levy all providers holding accommodation bonds to recoup the shortfall. It is not possible to quantify the Australian Government's contingent liability in the event that the Guarantee Scheme is activated.

Indemnity relating to smallpox vaccine

On 12 December 2002, the Australian Government took possession of an initial shipment of 50,000 doses of smallpox vaccine. This vaccine, to be used only in emergency situations, was the only type available for large-scale purchase and was manufactured using older style technology. The Government granted an indemnity to the manufacturer covering possible adverse events that could result from the use of the vaccine.

Medical Indemnity Exceptional Claims Scheme

In May 2003, the Prime Minister announced the Medical Indemnity Exceptional Claims Scheme to assume liability for 100 per cent of any damages payable against a doctor that exceeds a specified level of cover provided by that doctor's medical indemnity insurer, currently $20 million. These arrangements will apply to payouts related to either a single large claim or to multiple claims that in aggregate exceed the cover provided by the doctor's medical indemnity insurer, and will apply to claims notified under contracts-based cover since 1 January 2003.

Industry, Tourism and Resources

Liability for costs incurred in a National Liquid Fuel Emergency

The Australian Government has responsibility for the *Liquid Fuel Emergency Act 1984* administered by the Minister for Industry, Tourism and Resources. To coordinate Australian and State and Territory use of the powers under this Act in a national liquid fuel emergency, the Australian and State and Territory Governments have entered into an inter-governmental agreement (IGA). The IGA contains three areas where the Australian Government may incur expenses in the unlikely event of a national liquid fuel emergency. These relate to the direct costs of managing such an emergency, the potential for the Australian Government to reimburse the State and Territory Governments for the implementation costs of their response and the potential for compensation arising to industry from Australian Government directions under the Act.

Liability for damages caused by space activities

Under the United Nations Convention on International Liability for Damage Caused by Space Objects, the Australian Government is liable to pay compensation for damage caused to nationals of other countries by space objects launched from, or by, Australia. The Australian Government requires the responsible party for a space activity approved under the *Space Activities Act 1998* to insure against liability for damage to third parties for an amount not less than the maximum probable loss, up to a maximum of $750 million. Under the Space Activities Act, the Australian Government also accepts liability for damage suffered by Australian nationals, to a maximum value of $3 billion above the insured level.

Snowy Hydro Limited — directors' indemnities

The Australian Government has, together with the co-shareholder Governments of New South Wales and Victoria, indemnified the members of the board of Snowy Hydro Limited for liabilities arising from entering into agreements to implement corporatisation of the Snowy Mountains Hydro-Electric Scheme, and from liabilities to Snowy Hydro Limited at corporatisation. The indemnity will apply to liabilities arising within five years of corporatisation, and for which a claim is notified to the Governments within eleven years of the corporatisation date of 28 June 2002.

Snowy Hydro Limited — water releases

The Australian, New South Wales and Victorian Governments have indemnified Snowy Hydro Limited for liabilities arising from water releases in the Snowy River below Jindabyne Dam, where these releases are in accordance with the water licence and related regulatory arrangements agreed between the three Governments. The indemnity will apply to liabilities for which a claim is notified within 20 years from 28 June 2002.

The Australian, New South Wales and Victorian Governments will provide financial support to the company, if this is necessary, to avoid the company breaching its loan covenants to fund the cost of civil works required to address a cold-water pollution offence. The undertaking applies for seven years from 28 June 2002.

Transport and Regional Services

Assumed residual liabilities of the Australian National Railways Commission

The Australian Government under Schedule 3 of the *Australian National Railways Commission Sale Act 1997* assumed the residual liabilities of the Australian National Railways Commission. A writ of summons was filed in the High Court of Australia on 20 August 2004 and a statement of claim on behalf of 24 other plaintiffs was filed in the District Court of South Australia on 22 September 2005. The writ sought unspecified damages for personal injuries as a result of exposure to lead and other particles from trains carrying lead and zinc ore.

Maritime Industry Finance Company Limited — board members' indemnity

Indemnities for Maritime Industry Finance Company Limited board members have been provided to protect them against civil claims relating to their employment and conduct as directors.

Tripartite deeds relating to the sale of federal leased airports

Tripartite deeds apply to 12 federal leased airports (Adelaide, Alice Springs, Bankstown, Brisbane, Canberra, Coolangatta, Darwin, Launceston, Melbourne, Perth, Sydney and Townsville). The tripartite deeds between the Australian Government, the airport lessee company and financiers provide for limited step-in rights for the financiers in circumstances when the airport lease is terminated to enable the financiers to correct the circumstances that triggered such a termination event. These contingent liabilities are considered to be unquantifiable and remote.

Treasury

Housing Loans Insurance Corporation — guarantee

The Australian Government sold the Housing Loans Insurance Corporation (HLIC) on 12 December 1997 and has assumed all residual contingencies. The principal amount covered by the guarantee and the balances outstanding are unable to be reliably measured. The guarantee relates essentially to the HLIC's contracts of mortgage insurance and any borrowings approved by the Treasurer up to the time of sale.

Terrorism insurance — commercial cover

The *Terrorism Insurance Act 2003* established a scheme for replacement terrorism insurance covering damage to commercial property including associated business interruption and public liability. The scheme plans to accumulate approximately $300 million from reinsurance premiums paid to the Australian Reinsurance Pool Corporation (ARPC) to help meet administrative expenses and future claims. The Commonwealth guarantees to pay any liabilities of the ARPC, but the Treasurer must declare a reduced payout rate to insureds if the Commonwealth's liability would otherwise exceed $10 billion.

STATEMENT 12: TRENDS IN PUBLIC SECTOR FINANCES

This statement discusses trends in the fiscal balance, cash surplus, balance sheet data (net debt and net worth) and net interest payments for the non-financial public sector at the Australian Government and State/local levels of government, and also at the consolidated level. These indicators are discussed in greater detail in **Statement 8**.

This statement provides a broader context in which to consider developments in the Australian Government's budget.

For further information on the data used in the charts and tables in this statement, see Appendix B: Data. This statement uses the convention that references to the States include the Territories, and that the combined State and local government sector is denoted as the State/local sector and includes Territory governments unless otherwise stated.

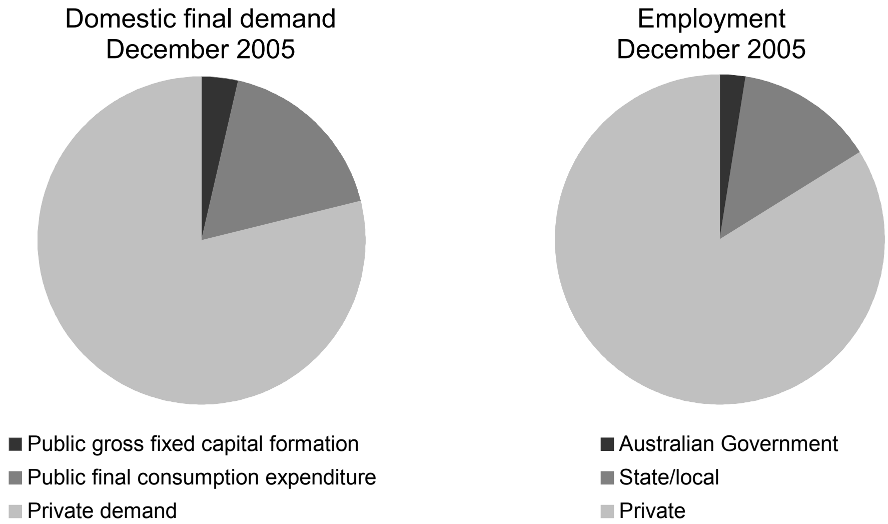
STATEMENT 12: TRENDS IN PUBLIC SECTOR FINANCES

SIZE AND STRUCTURE OF THE PUBLIC SECTOR

The size and structure of Australia's public sector provides a useful context for interpreting trends in the total public sector. The total public sector[1] constitutes a significant portion of the Australian economy (around 21 per cent of domestic final demand).

Domestic final demand (as shown in Chart 1) is made up of public final demand (which comprises public gross fixed capital formation and public final consumption expenditure) and private demand (consisting of private gross fixed capital formation and private final consumption expenditure). The Australian Government constitutes 39 per cent of public final demand, while the State/local level of government accounts for 61 per cent.

Chart 1: Contribution of public and private sectors



Sources: ABS cat. nos. 6248.0, 6202.0 and 5206.0.

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1 The total public sector includes the non-financial public sector (comprised of the general government sector and the public non-financial corporations sector) and the public financial corporations sector for the Australian Government and State/local levels of government.

There are significant differences in the roles and responsibilities of the two main levels of government. Major components of the Australian Government's expenses include transfer payments in relation to social security and welfare, and defence expenditure. Transfer payments, such as Australian Government income support payments, are not included in the Australian Government public final demand. Rather, these payments, along with payments that the Australian Government makes to the States and the private sector to assist in funding important services like education and health, are reflected in either State/local public final demand or private demand.

In terms of employment, the total public sector employs approximately 16 per cent of wage and salary earners (Chart 1). The State/local sector accounts for approximately 13.5 per cent of all wage and salary earners and for approximately 84 per cent of total public sector wage and salary earners. The Australian Government accounts for approximately 2.5 per cent of all wage and salary earners and for approximately 16 per cent of total public sector wage and salary earners. The State/local sector's larger share reflects that sector's major responsibilities for service delivery in the areas of education, health, transport and public order and safety.

FISCAL BALANCE

As outlined in Figure 1 of Statement 8, the total public sector is made up of the non-financial public sector (NFPS) and the public financial corporations sector. The NFPS is comprised of the general government sector and the public non-financial corporations (PNFC) sector.

The general government sector forms the majority of the NFPS (particularly in terms of revenue and expenses). The PNFC sector tends to be more important at the State/local level, where most PNFCs are concentrated.

The fiscal balance of the Australian Government general government sector is expected to be a surplus of 1.7 per cent of Gross Domestic Product (GDP) in 2005-06. The surplus is expected to be maintained at around 1 per cent of GDP over the forward estimates period.

The fiscal balance of the State/local general government sector is expected to be a deficit of 0.5 per cent of GDP in 2005-06, increasing to a deficit of 0.6 per cent of GDP in 2006-07. This projection is predominantly based on State 2005-06 mid-year reviews, since only the Northern Territory has released its 2006-07 Budget.

The consolidated[2] PNFC fiscal balance is expected to be in deficit in 2005-06 by 1.2 per cent of GDP. The decrease in consolidated PNFC revenue and expenses as a share of GDP in recent years is partly attributable to the privatisation of PNFCs by both the Australian and State/local governments.

Tables 1, 2 and 3 show general government, PNFC and NFPS fiscal balance data by level of government.

2 When combined, the Australian Government, State/local governments and universities are referred to as the 'consolidated public sector'.

Table 1: General government fiscal balance by level of government (per cent of GDP)[(a)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	26.0	26.7	-0.8	na	na	na	na	na	na
1997-98	25.4	25.7	-0.3	na	na	na	na	na	na
1998-99	25.0	24.1	0.6	17.1	16.3	0.3	37.1	35.3	1.0
1999-00	25.9	24.3	1.8	16.8	15.9	0.3	37.7	35.2	2.2
2000-01	23.5	22.9	0.8	16.7	16.2	-0.1	37.3	36.2	0.7
2001-02	22.1	22.7	-0.5	16.5	16.0	0.0	35.7	35.6	-0.4
2002-03	22.4	21.8	0.6	16.6	15.9	0.3	36.6	35.3	1.0
2003-04	22.4	21.8	0.6	16.9	15.8	0.5	37.1	35.3	1.2
2004-05	23.1	21.9	1.2	16.8	15.8	0.4	37.6	35.4	1.6
2005-06(e)	23.3	21.6	1.7	16.3	15.8	-0.5	37.0	34.6	1.3
2006-07(e)	**23.0**	**21.8**	**1.0**	**15.9**	**15.6**	**-0.6**	**36.3**	**34.8**	**0.5**
2007-08(p)	22.9	21.9	0.9	na	na	na	na	na	na
2008-09(p)	23.0	22.0	1.0	na	na	na	na	na	na
2009-10(p)	23.0	21.9	1.1	na	na	na	na	na	na

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(e) Estimates.
(p) Projections.
na Data not available.

Table 2: Public non-financial corporations fiscal balance by level of government (per cent of GDP)[(a)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	5.0	4.8	-0.1	na	na	na	na	na	na
1997-98	5.1	4.7	0.4	na	na	na	na	na	na
1998-99	4.6	4.3	-0.1	6.1	6.1	-0.5	10.6	10.4	-0.6
1999-00	4.0	3.6	0.2	5.7	5.4	0.3	9.6	9.1	0.5
2000-01	3.8	3.6	-0.1	5.5	5.2	0.2	9.2	8.8	0.1
2001-02	3.6	3.4	0.1	4.7	4.5	-0.2	8.3	8.0	-0.1
2002-03	3.1	2.9	0.3	4.5	4.4	-0.3	7.7	7.4	-0.1
2003-04	3.0	2.8	0.3	4.5	4.3	-0.3	7.6	7.2	0.0
2004-05	3.0	2.8	0.2	4.3	4.2	-0.4	7.4	7.1	-0.3
2005-06(e)	2.9	3.0	-0.3	4.3	4.3	-0.9	7.2	7.3	-1.2
2006-07(e)	**1.4**	**1.4**	**-0.1**	**na**	**na**	**na**	**na**	**na**	**na**

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(e) Estimates.
na Data not available.

Table 3: Non-financial public sector fiscal balance by level of government (per cent of GDP)[(a)]

	Australian Government			State/local			Consolidated		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	na	na	-0.8	na	na	na	na	na	na
1997-98	na	na	0.1	na	na	na	na	na	na
1998-99	28.9	27.8	0.5	20.8	19.9	-0.1	44.7	42.6	0.4
1999-00	29.2	27.1	2.0	20.5	19.5	0.6	44.8	41.6	2.6
2000-01	26.6	25.8	0.7	20.3	19.7	0.0	44.0	42.6	0.7
2001-02	25.1	25.5	-0.4	19.5	18.8	-0.2	41.7	41.2	-0.5
2002-03	24.9	24.1	0.9	19.5	18.6	0.0	42.0	40.2	1.0
2003-04	24.8	23.9	0.8	19.6	18.4	0.2	42.2	40.0	1.2
2004-05	25.5	24.1	1.4	19.5	18.4	0.0	42.7	40.0	1.4
2005-06(e)	25.6	24.0	1.3	18.8	18.4	-1.4	41.9	39.7	0.0
2006-07(e)	**24.1**	**22.9**	**0.9**	**na**	**na**	**na**	**na**	**na**	**na**

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(e) Estimates.
na Data not available.

CASH SURPLUS

General government sector

The Australian Government general government sector has been in surplus since 1997-98, with the exception of a small cash deficit of 0.1 per cent of GDP in 2001-02.

Panels A and C of Chart 2 show the large contribution of past Australian Government general government cash deficits to the consolidated NFPS cash deficit. Panel A of Chart 2 also illustrates the improvement in the Australian Government general government sector balance, culminating in the strong surplus outcomes of recent years.

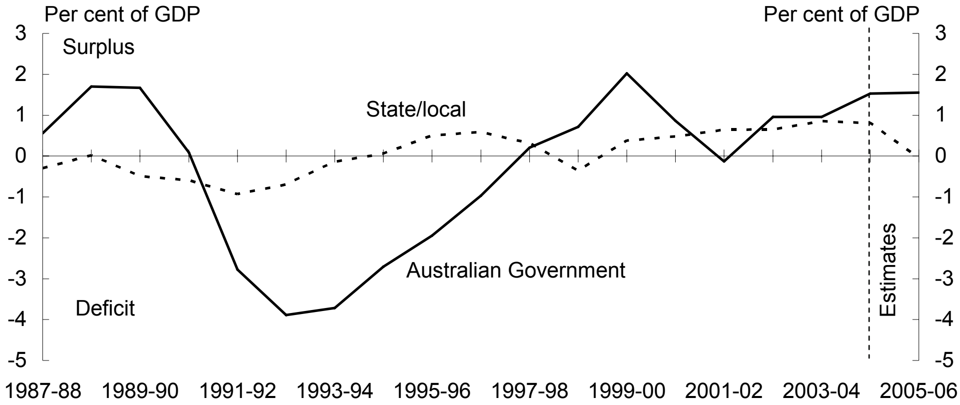
Panel A of Chart 2 also shows the sustained improvement in State/local general government balances through the mid 1990s. After the State/local cash deficit peaked at 0.9 per cent of GDP in 1991-92, deficits continued to be reduced until the State/local sector achieved a surplus in 1994-95. The State/local general government sector maintained a cash surplus each year from 1994-95 to 2004-05, with the exception of 1998-99. This improvement was initially due to payments restraint, helped by lower debt servicing charges and more recently by the strong growth in revenues related to the property market and GST. In 2005-06, the sector is expected to record a deficit of 0.1 per cent of GDP, which partially reflects the impact of a cooling property market in a number of States and planned increases in infrastructure spending.

Public non-financial corporations sector

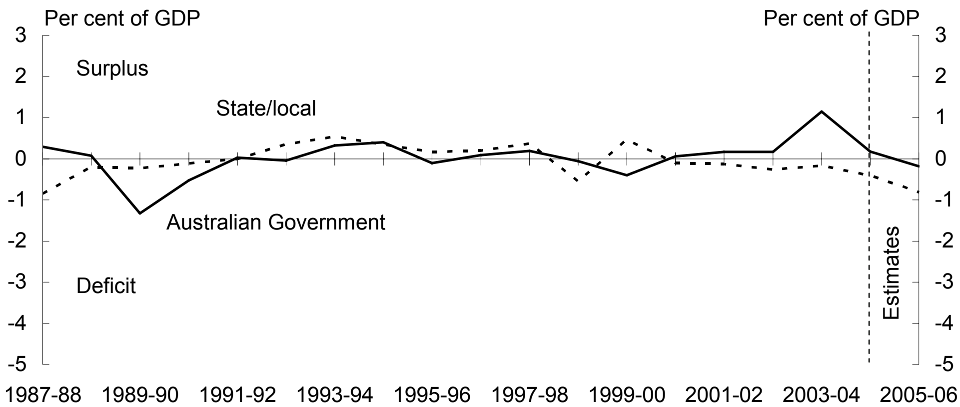
As shown in Chart 3, the consolidated PNFC sector maintained a cash surplus position through much of the 1990s but has often been in deficit in recent years. A deficit of 1 per cent of GDP is projected for the consolidated PNFC sector in 2005-06.

Chart 2: Cash surplus by sector and level of government

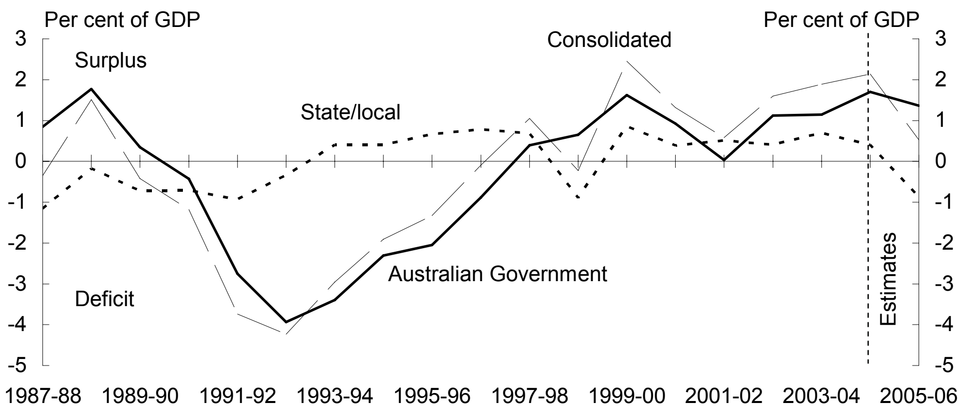
A: General government



B: Public non-financial corporations



C: Non-financial public sector

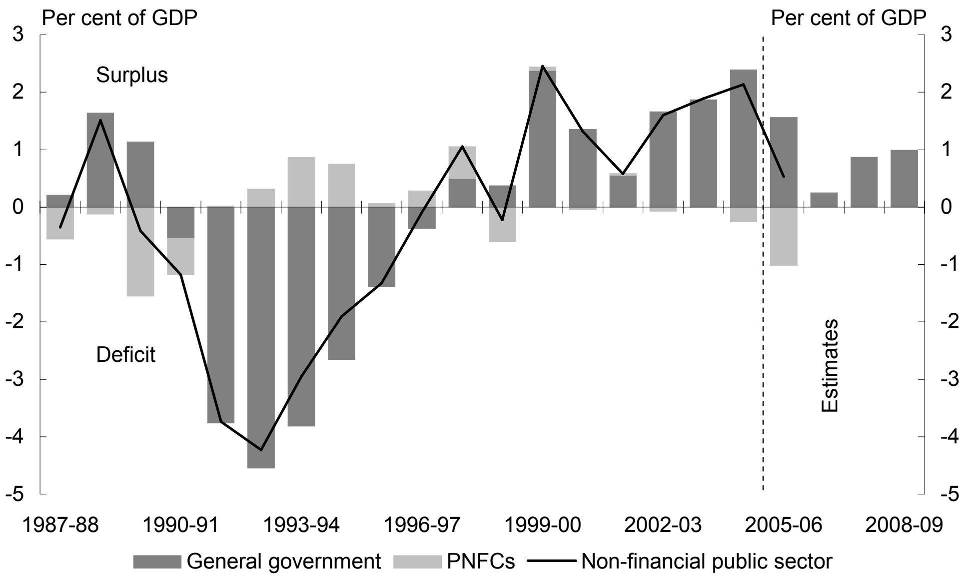


Non-financial public sector

It is estimated that the consolidated NFPS will achieve a cash surplus of 0.5 per cent of GDP in 2005-06.

Chart 3 illustrates that the consolidated NFPS was generally in a deficit position during the 1990s. The deficit peaked at 4.2 per cent of GDP in 1992-93 before moving into a surplus position in 1997-98. This primarily reflects Australian Government general government cash deficits in the early to mid 1990s. Since 1999-2000 the consolidated NFPS has remained in surplus due to consecutive surpluses in the consolidated general government sector. The deficit in 1998-99 is the result of one-off increases in State funding of superannuation liabilities.

Chart 3: Consolidated non-financial public sector cash surplus by sector[(a)]



(a) Data for the consolidated PNFCs and NFPS are only available to 2005-06, while general government data are available to 2008-09.

Receipts and payments

Chart 4 shows trends in general government cash receipts and payments at the Australian Government, State/local and consolidated levels. Due to its size, the general government sector is an appropriate focus for an assessment of public sector receipts and payments. It is also the sector through which governments primarily affect the level of private sector activity.

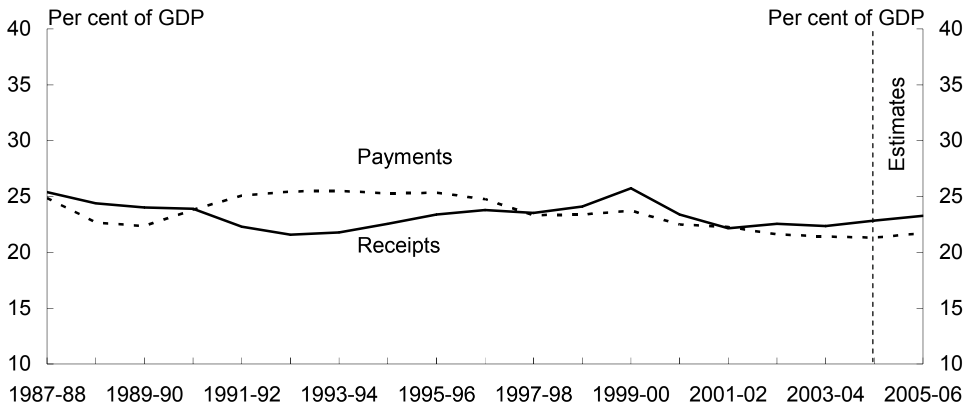
Estimates of Australian Government receipts and payments in Panel A of Chart 4 are net of GST receipts and show a decline in 2000-01 with the introduction of *The New Tax System*. In addition, consolidated general government receipts fell from 1999-2000 due to the Australian Government's tax reforms, which included significant personal income tax cuts and the abolition of a range of taxes at the State level, including financial institutions duty, stamp duty on quoted marketable securities and bank account debits tax.

The increases in both receipts and payments in 1998-99 for the State/local sector and in 1999-2000 for the Australian Government sector, shown in Panels B and A of Chart 4 respectively, were predominantly due to the move to an accrual accounting framework and the subsequent 'grossing' up of cash receipts and payments, whereas prior to this, some cash receipts were netted off payments.

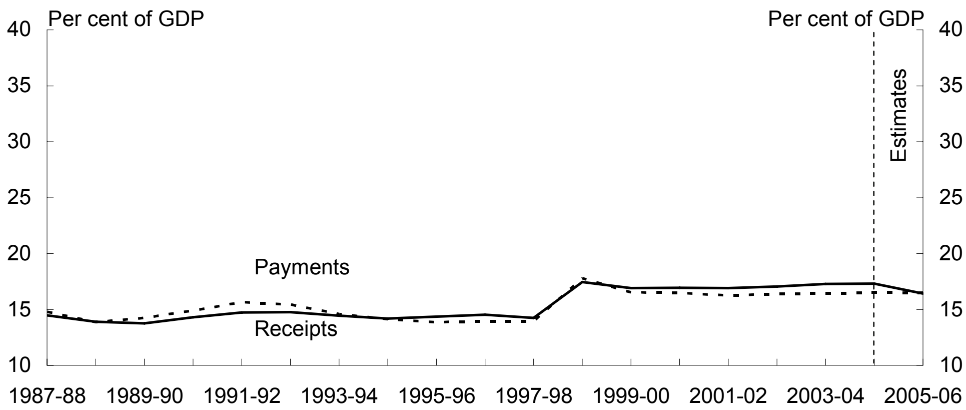
The PNFC sector is an important provider of economic infrastructure and contributes significant revenue to the general government sector, mainly in the form of dividends. State/local governments account for the majority of total PNFC sector payments, reflecting State responsibility for infrastructure and service provision in areas such as electricity, gas, water and public transport.

Chart 4: General government receipts and payments by level of government

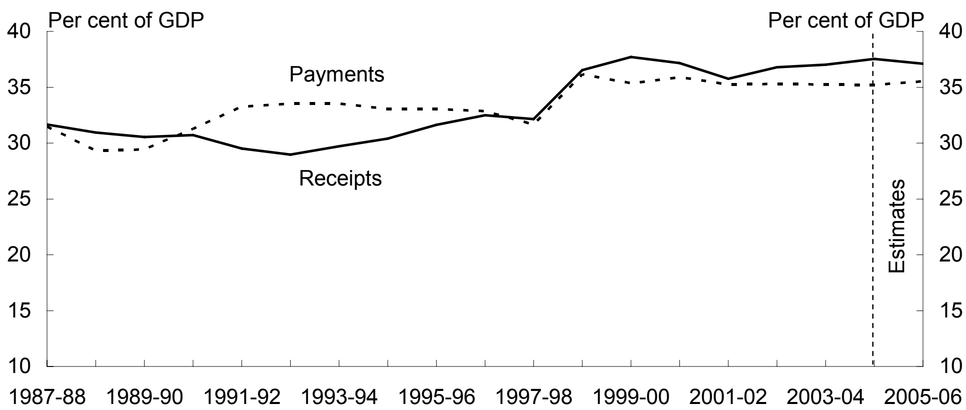
A: Australian Government



B: State/local



C: Consolidated



NET DEBT

Chart 5 shows a consistent decline in consolidated general government net debt as a share of GDP from a peak of 24.2 per cent of GDP in 1994-95. The consolidated general government sector recorded a level of net debt below zero in 2004-05 and its net debt levels are forecast to continue to fall over the forward estimates.

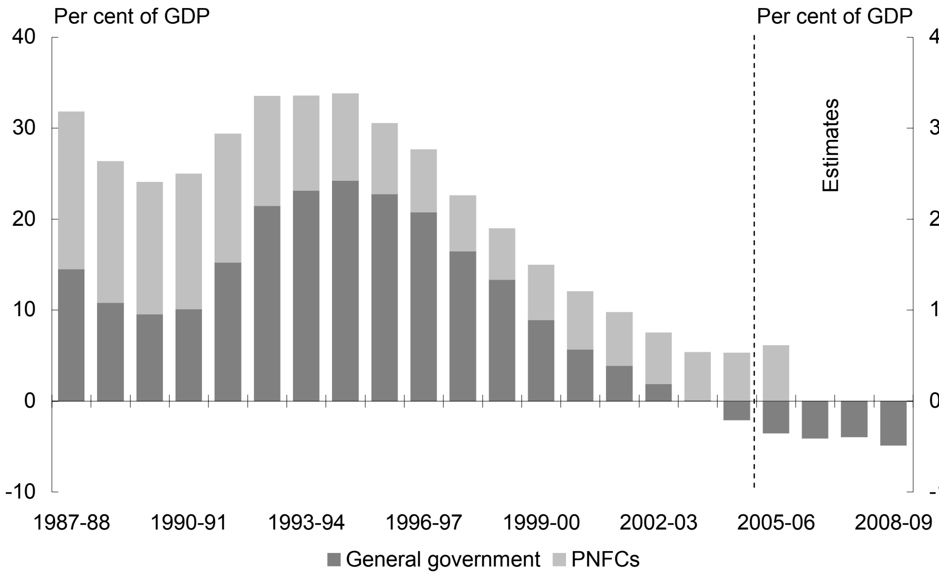
Charts 3 and 5 show the broad correlation between cash deficits and net debt levels. The financing of Australian Government cash deficits resulted in a substantial increase in general government net debt as a share of GDP over the early 1990s.

Chart 5 also shows the improvement in PNFC sector net debt as a share of GDP since the late 1980s, reflecting lower levels of capital expenditure, improved efficiency and privatisations. This moderated the deterioration in NFPS net debt as a share of GDP in the first half of the 1990s.

The subsequent improvement in NFPS net debt primarily reflects both the Australian Government and the State/local sector moving back into budget surpluses and the application of privatisation proceeds to debt retirement at both the Australian Government and State/local government levels.

PNFC privatisations during the 1990s occurred in two main sectors — electricity and gas (such as Victorian and South Australian electricity assets) and transport and communications (such as the partial sale of Telstra). Proceeds of asset sales have largely been used to reduce, or contain, the growth of general government net debt, resulting in ongoing savings in public debt interest.

Chart 5: Consolidated non-financial public sector net debt by sector (as at end of financial year)[(a)]



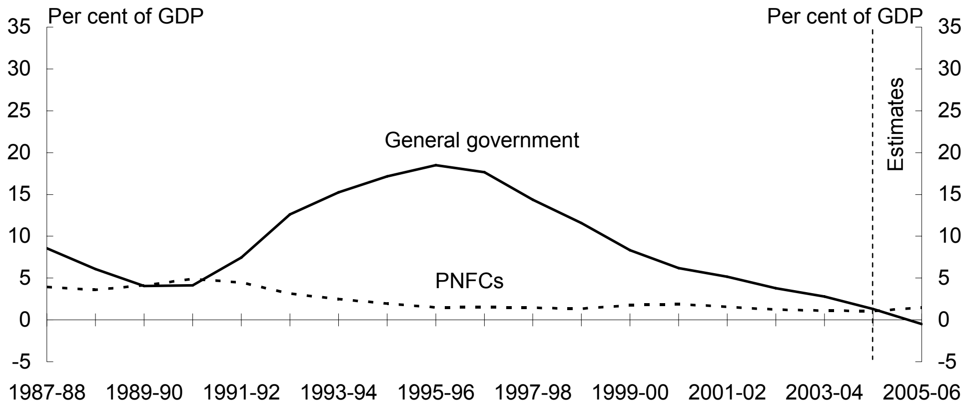
(a) Data for the consolidated PNFC and NFPS sectors are only available to 2005-06, while data for the general government sector are available to 2008-09.

As shown in Panel A of Chart 6, Australian Government general government net debt as a share of GDP grew from low levels in the late 1980s to a peak of 18.5 per cent in 1995-96. Since then, successive surpluses and asset sales (most notably the partial sale of Telstra) have improved Australian Government general government sector net debt, with net debt falling below zero in 2005-06.

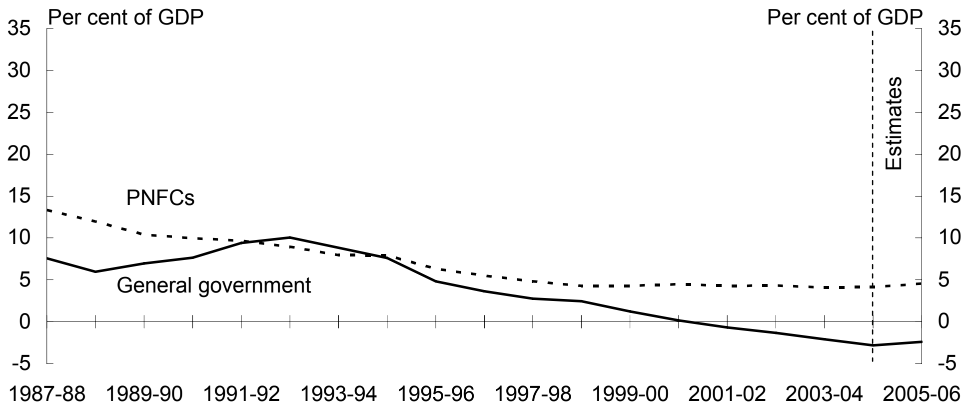
In contrast, State/local general government net debt grew more modestly in the early 1990s before declining from a peak of 10 per cent of GDP in 1992-93 to below zero from 2001-02. State/local net debt is estimated to be -2.4 per cent of GDP in 2005-06, as shown in Panel B of Chart 6. This improvement within the State/local general government sector reflects both the impact of asset sales and fiscal consolidation during the second half of the 1990s. However, most States are forecasting an increase in their levels of general government net debt in the forward years as they borrow to finance expenditure programs (for further information, see Budget Paper No. 3, *Federal Financial Relations 2006-07*).

Chart 6: Non-financial public sector net debt by level of government and sector (as at end of financial year)

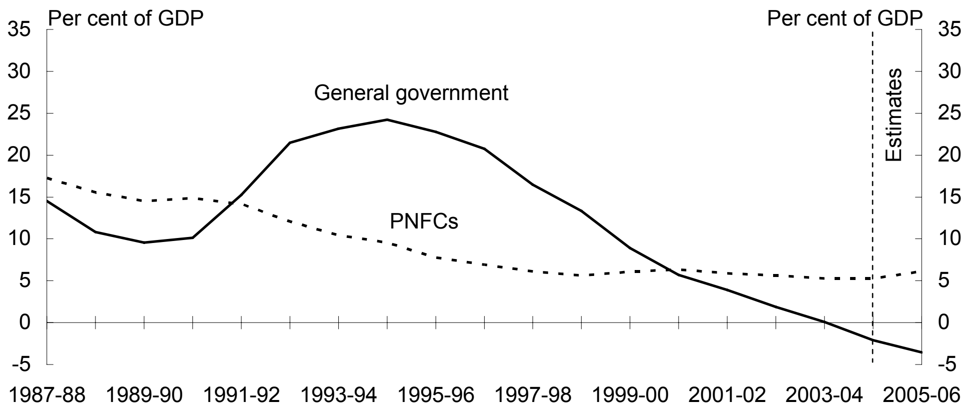
A: Australian Government



B: State/local



C: Consolidated



NET WORTH

The State/local general government sector is estimated to have a positive net worth of 59.1 per cent of GDP in 2006-07. State/local net worth has increased in nominal terms each year since 1998-99. However, net worth has not always grown at the same pace as the economy, and hence has not increased as a proportion of GDP. The Australian Government general government sector has historically recorded negative net worth. This difference primarily reflects the significant funding provided by the Australian Government to the States and to local government for capital works, with the resultant assets recorded in the balance sheets of the State and local governments.

Table 4: General government net worth by level of government (as at end of financial year)

	Australian Government(a)		State/local		Consolidated	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1996-97	-74,354	-13.6	na	na	na	na
1997-98	-68,544	-11.9	na	na	na	na
1998-99	-76,150	-12.5	362,391	59.6	304,300	50.1
1999-00	-40,552	-6.3	390,791	60.6	369,439	57.3
2000-01	-43,299	-6.3	405,658	58.8	382,459	55.5
2001-02	-48,429	-6.6	427,858	58.2	402,298	54.7
2002-03	-53,251	-6.8	470,098	60.1	440,928	56.3
2003-04	-39,595	-4.7	515,284	61.5	501,963	59.9
2004-05	-32,108	-3.6	571,722	64.0	567,466	63.6
2005-06(e)	-24,026	-2.5	575,991	60.3	582,347	60.9
2006-07(e)	**-12,001**	**-1.2**	**596,289**	**59.1**	**616,571**	**61.1**
2007-08(p)	-2,330	-0.2	na	na	na	na
2008-09(p)	8,783	0.8	na	na	na	na
2009-10(p)	21,632	1.9	na	na	na	na

(a) There is a break in the Australian Government net worth series between 1998-99 and 1999-2000. Data up to 1998-99 are sourced from the Commonwealth's Consolidated Financial Statements based on Australian Accounting Standards. Data beginning in 1999-2000 are based on the Government Finance Statistics (GFS) framework. For the general government sector, the major change across the break in the series is an improvement in net worth. This is primarily due to the move from valuing investments in public corporations at historic cost to current market value (which is calculated using the share price for listed corporations). This is partly offset by defence weapons platforms no longer being recorded as assets.

(e) Estimates.

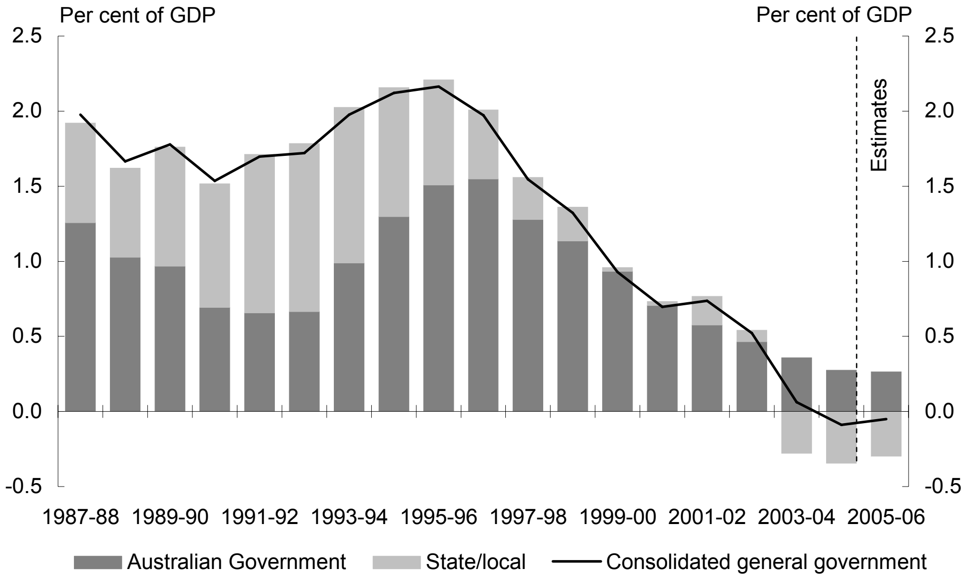
(p) Projections.

na Data not available.

NET INTEREST PAYMENTS

Consolidated general government net interest payments peaked in 1995-96 at 2.2 per cent of GDP due to the increased level of Australian Government general government net debt. Consolidated net interest payments are expected to reduce to -0.1 per cent of GDP in 2005-06 due to reduced Australian and State/local general government net debt since 1995-96 and lower interest rates in recent years.

Chart 7: General government net interest payments



APPENDIX A: SUPPLEMENTARY CASH TABLES

Table A1: Consolidated cash receipts, payments and cash surplus by institutional sector as a per cent of GDP

	General government			Public non-financial corporations			Non-financial public sector		
	Receipts	Payments	Cash surplus(a)	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus(a)
1987-88	31.7	31.5	0.2	3.9	5.7	-0.6	34.5	36.1	-0.4
1988-89	31.0	29.3	1.6	3.7	5.2	-0.1	33.7	33.6	1.5
1989-90	30.6	29.4	1.1	3.6	6.5	-1.6	33.1	34.8	-0.4
1990-91	30.7	31.3	-0.5	3.7	5.8	-0.6	33.2	35.8	-1.2
1991-92	29.5	33.3	-3.8	3.5	5.3	0.0	31.7	37.2	-3.7
1992-93	29.0	33.5	-4.6	3.5	4.8	0.3	31.1	37.1	-4.2
1993-94	29.7	33.5	-3.8	3.7	4.2	0.9	31.8	36.2	-3.0
1994-95	30.4	33.1	-2.7	3.3	4.4	0.7	32.3	36.0	-1.9
1995-96	31.6	33.0	-1.4	2.9	4.4	0.1	32.9	35.8	-1.3
1996-97	32.5	32.9	-0.4	3.0	4.0	0.3	33.4	34.9	-0.1
1997-98	32.2	31.7	0.5	2.9	3.6	0.6	33.5	33.7	1.1
1998-99	36.5	36.2	0.4	na	na	-0.6	na	na	-0.2
1999-00	37.7	35.4	2.4	na	na	0.1	na	na	2.5
2000-01	37.2	35.9	1.4	na	na	0.0	na	na	1.3
2001-02	35.8	35.3	0.6	na	na	0.0	na	na	0.6
2002-03	36.8	35.3	1.7	na	na	-0.1	na	na	1.6
2003-04	37.0	35.3	1.9	na	na	0.0	na	na	1.9
2004-05	37.5	35.2	2.4	na	na	-0.3	na	na	2.1
2005-06(e)	37.1	35.5	1.6	na	na	-1.0	na	na	0.5
2006-07(e)	**36.4**	**36.0**	**0.3**	**na**	**na**	**na**	**na**	**na**	**na**
2007-08(p)	36.2	35.2	0.9	na	na	na	na	na	na
2008-09(p)	36.3	35.1	1.0	na	na	na	na	na	na

(a) Future fund earnings have been excluded from the Australian Government cash surplus.
(e) Estimates.
(p) Projections.
na Comparable data not available.

Table A2: Non-financial public sector cash surplus by level of government as a per cent of GDP

	Australian Government(a)	State/local	Consolidated(a)
1987-88	0.9	-1.2	-0.4
1988-89	1.8	-0.2	1.5
1989-90	0.3	-0.7	-0.4
1990-91	-0.4	-0.7	-1.2
1991-92	-2.8	-0.9	-3.7
1992-93	-3.9	-0.3	-4.2
1993-94	-3.4	0.4	-3.0
1994-95	-2.3	0.4	-1.9
1995-96	-2.0	0.7	-1.3
1996-97	-0.9	0.8	-0.1
1997-98	0.4	0.7	1.1
1998-99	0.7	-0.9	-0.2
1999-00	1.6	0.9	2.5
2000-01	0.9	0.4	1.3
2001-02	0.0	0.5	0.6
2002-03	1.1	0.4	1.6
2003-04	1.1	0.7	1.9
2004-05	1.7	0.4	2.1
2005-06(e)	1.4	-0.9	0.5
2006-07(e)	**1.0**	**na**	**na**

(a) Future fund earnings have been excluded from the Australian Government cash surplus.
(e) Estimates.
na Data not available.

Table A3: General government net interest payments by level of government

	Australian Government(a)		State/local	
	$m	Per cent of GDP	$m	Per cent of GDP
1973-74	-306	-0.5	451	0.8
1974-75	-267	-0.4	474	0.7
1975-76	-389	-0.5	526	0.6
1976-77	-161	-0.2	555	0.6
1977-78	-106	-0.1	582	0.6
1978-79	126	0.1	609	0.5
1979-80	290	0.2	634	0.5
1980-81	444	0.3	801	0.5
1981-82	475	0.3	785	0.5
1982-83	654	0.4	1,034	0.6
1983-84	1,327	0.6	1,347	0.6
1984-85	2,462	1.1	1,405	0.6
1985-86	3,626	1.4	1,159	0.5
1986-87	4,387	1.6	1,493	0.5
1987-88	4,019	1.3	2,127	0.7
1988-89	3,722	1.0	2,158	0.6
1989-90	3,848	1.0	3,153	0.8
1990-91	2,834	0.7	3,364	0.8
1991-92	2,739	0.7	4,397	1.1
1992-93	2,912	0.7	4,901	1.1
1993-94	4,549	1.0	4,771	1.0
1994-95	6,310	1.3	4,182	0.9
1995-96	7,812	1.5	3,636	0.7
1996-97	8,449	1.5	2,515	0.5
1997-98	7,381	1.3	1,617	0.3
1998-99	6,901	1.1	1,376	0.2
1999-00	6,014	0.9	172	0.0
2000-01	4,855	0.7	191	0.0
2001-02	4,238	0.6	1,402	0.2
2002-03	3,641	0.5	602	0.1
2003-04	2,994	0.4	-2,331	-0.3
2004-05	2,463	0.3	-3,075	-0.3
2005-06(e)	2,535	0.3	-2,840	-0.3
2006-07(e)	**452**	**0.0**	**na**	**na**
2007-08(p)	303	0.0	na	na
2008-09(p)	-243	0.0	na	na
2009-10(p)	-928	-0.1	na	na

(a) There is a break in the Australian Government net debt and net interest payments series between 1998-99 and 1999-2000 (the first year of accrual budgeting). Up to 1998-99, Australian Government debt instruments are valued at historic cost. From 1999-2000 onwards, Australian Government debt instruments are valued at market prices, consistent with accrual GFS standards.
(e) Estimates.
(p) Projections.
na Data not available.

Table A4: Non-financial public sector net debt[(a)]

	General government						PNFCs		NFPS	
	Australian Government		State/local		Consolidated		Consolidated		Consolidated	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1987-88	27,359	8.6	24,201	7.6	46,410	14.5	55,293	17.3	101,703	31.8
1988-89	21,982	6.1	21,683	6.0	39,232	10.8	56,363	15.5	95,595	26.4
1989-90	16,121	4.1	27,672	7.0	37,989	9.6	57,794	14.5	95,783	24.1
1990-91	16,936	4.1	31,322	7.7	41,380	10.1	60,745	14.9	102,125	25.0
1991-92	31,132	7.5	39,167	9.4	63,525	15.2	59,011	14.2	122,536	29.4
1992-93	55,218	12.6	44,020	10.0	94,048	21.5	52,878	12.1	146,926	33.5
1993-94	70,223	15.3	40,693	8.8	106,439	23.1	48,021	10.4	154,460	33.6
1994-95	83,492	17.2	37,039	7.6	117,973	24.2	46,482	9.6	164,455	33.8
1995-96	95,831	18.5	24,981	4.8	118,053	22.8	40,135	7.7	158,188	30.5
1996-97	96,281	17.6	19,757	3.6	113,236	20.7	37,748	6.9	150,984	27.7
1997-98	82,935	14.4	15,937	2.8	95,122	16.5	35,371	6.1	130,493	22.6
1998-99	70,402	11.6	14,782	2.4	81,153	13.4	34,233	5.6	115,386	19.0
1999-00	53,768	8.3	7,970	1.2	57,501	8.9	39,135	6.1	96,636	15.0
2000-01	42,651	6.2	998	0.1	39,198	5.7	43,758	6.3	82,956	12.0
2001-02	38,024	5.2	-4,900	-0.7	28,638	3.9	43,262	5.9	71,900	9.8
2002-03	29,665	3.8	-10,423	-1.3	14,681	1.9	44,033	5.6	58,713	7.5
2003-04	23,421	2.8	-17,492	-2.1	839	0.1	44,103	5.3	44,942	5.4
2004-05	11,534	1.3	-25,026	-2.8	-18,802	-2.1	47,214	5.3	28,413	3.2
2005-06(e)	-4,784	-0.5	-23,114	-2.4	-33,823	-3.5	58,334	6.1	24,512	2.6
2006-07(e)	**-22,075**	**-2.2**	**-12,550**	**-1.2**	**-41,198**	**-4.1**	**na**	**na**	**na**	**na**
2007-08(p)	-24,743	-2.4	-9,502	-0.9	-41,494	-3.9	na	na	na	na
2008-09(p)	-37,140	-3.4	-8,121	-0.7	-53,215	-4.8	na	na	na	na
2009-10(p)	-50,184	-4.3	na	na	na	na	na	na	na	na

(a) Between 1997-98 and 1999-2000 there is a structural shift in the net debt series as jurisdictions moved from the cash GFS framework to the accrual GFS framework. Consistent with this framework, some jurisdictions value net debt at market prices, while other jurisdictions continue to value net debt at historic cost. Australian Government net debt is valued at market prices from 1999-2000.
(e) Estimates.
(p) Projections.
na Data not available.

APPENDIX B: DATA

The information in this statement is consistent with the Australian Bureau of Statistics (ABS) Government Finance Statistics (GFS) reporting framework for the public sector.

The clear policy intent of the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations* is that the GST is collected by the Australian Taxation Office, as an agent for the States, and appropriated to the States. The Australian Government accrual revenue and expenses and cash receipts and payments measures included in this statement therefore differ from ABS GFS measures by treating the GST revenue as State tax revenue.

Data are sourced from Australian Government Final Budget Outcomes and Australian Treasury estimates, the ABS 1997-98 Government Finance Statistics (cat. no. 5512.0), 2004-05 Government Finance Statistics (cat. no. 5512.0), the Northern Territory's 2006-07 Budget and other jurisdictions' 2005-06 mid-year reports. Net debt data prior to 1998-99 are sourced from the ABS 1998 Public Sector Financial Assets and Liabilities (ABS cat. no. 5513.0), and the ABS 1999-2000 Government Finance Estimates (ABS cat. no. 5501.0).

Australian Government budget aggregates, including net debt for 1999-2000 onwards, have been revised relative to the respective Final Budget Outcomes to ensure that data are consistent across the accrual period.

Due to methodological and data source changes associated with the move to an accrual accounting framework, time series data that use measures derived under both cash and accrual accounting should be used with caution. Statement 13 provides more information on specific factors affecting the comparability of data between years.

STATEMENT 13: HISTORICAL AUSTRALIAN GOVERNMENT DATA

This statement reports historical data for the Australian Government fiscal aggregates across the general government, public non-financial corporations and non-financial public sectors.

STATEMENT 13: HISTORICAL AUSTRALIAN GOVERNMENT DATA

Statement 13 provides historical data for the Australian Government fiscal aggregates across the general government, public non-financial corporations and non-financial public sectors.

Under the accrual Government Finance Statistics (GFS) framework, flows are recorded in the period in which they occurred. As a result, prior period outcomes may be revised where information arises that could reasonably be expected to have been known in the past, is material in at least one of the affected periods and can be reliably assigned to the relevant period(s).

Estimates up to and including 1998-99 are calculated on cash terms, while estimates from 1999-00 onwards are derived from an accrual framework. Due to methodological and data-source changes associated with the move to an accrual accounting framework, time series data that include measures derived under both cash and accrual accounting should be used with caution.

There are other structural breaks within the data set, prior to the shift to accrual reporting. Classification differences and revisions, as well as changes to the structure of the budget, can impact on comparisons over such an extended period.

Specific factors that affect the comparability of data between years include:

- classification differences in the data relating to the period prior to 1976-77 (which means that earlier data may not be entirely consistent with data for 1976-77 onwards);
- adjustments in the coverage of agencies included in the accounts of the different sectors. These include the reclassification of Central Banking Authorities from the general government to the public financial corporations sector in 1998-99, and subsequent back-casting to account for this change;
- consistent with the revised GFS treatment announced by the Australian Bureau of Statistics (ABS) (cat. no. 5501.0, released October 2002), the general government surplus measures in this statement, from 1998-99 onwards, incorporate the interest component of superannuation related payments by the Australian Government general government sector in respect of accumulated public non-financial corporations' superannuation liabilities;
- transfers of taxing powers between the Australian Government and the States;
- other changes in financial arrangements between the Australian Government and the State/local government sector; and

- changes in arrangements for transfer payments, where tax concessions or rebates are replaced by payments through the social security system. This has the effect of increasing both cash receipts and payments, as compared with earlier periods, but not changing cash balances. Changes in the opposite direction (tax expenditures replacing payments) reduce both cash payments and receipts.

Occasionally classification changes are made that require revisions to the historic series. Where appropriate, the changes are back-cast to 1999-00 to ensure that data is consistent across the accrual period. For example, the back-casting to account for the market valuation of net debt as discussed on page 2-12 of Budget Paper No. 1, *Budget Strategy and Outlook 2003-04*.

While approximate adjustments can be made to identify trends in budget aggregates on a generally consistent basis, the further back the analysis is taken, the more difficult the task becomes.

Table 1: Australian Government general government sector receipts, payments and underlying cash balance(a)

	Receipts(c)			Payments(c)			Future Fund earnings	Underlying cash balance(b)	
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	$m	Per cent of GDP
1973-74	11,890	10.4	20.1	10,829	3.8	18.3	-	1,061	1.8
1974-75	15,325	5.8	21.9	15,275	15.8	21.8	-	50	0.1
1975-76	18,316	3.6	22.4	19,876	12.8	24.3	-	-1,560	-1.9
1976-77	21,418	4.1	22.7	22,657	1.5	24.0	-	-1,239	-1.3
1977-78	23,491	0.8	22.8	25,489	3.4	24.7	-	-1,998	-1.9
1978-79	25,666	3.2	22.0	27,753	2.8	23.8	-	-2,087	-1.8
1979-80	29,780	6.0	22.5	31,041	2.1	23.4	-	-1,261	-1.0
1980-81	35,148	6.8	23.4	35,260	2.8	23.5	-	-112	-0.1
1981-82	40,831	2.8	23.6	40,394	1.4	23.3	-	437	0.3
1982-83	44,675	-1.7	24.0	47,907	6.6	25.7	-	-3,232	-1.7
1983-84	49,102	2.9	23.4	55,966	9.4	26.6	-	-6,864	-3.3
1984-85	57,758	11.8	24.9	63,639	8.0	27.4	-	-5,881	-2.5
1985-86	64,845	5.7	25.3	69,838	3.3	27.3	-	-4,993	-2.0
1986-87	73,145	5.2	26.1	75,392	0.7	26.9	-	-2,247	-0.8
1987-88	81,217	3.4	25.4	79,440	-1.9	24.8	-	1,777	0.6
1988-89	88,369	0.3	24.4	82,202	-4.7	22.7	-	6,167	1.7
1989-90	95,517	1.8	24.0	88,882	1.9	22.4	-	6,635	1.7
1990-91	97,705	-2.5	23.9	97,333	4.3	23.8	-	372	0.1
1991-92	92,966	-6.6	22.3	104,551	5.4	25.1	-	-11,585	-2.8
1992-93	94,448	0.4	21.6	111,484	5.4	25.5	-	-17,036	-3.9
1993-94	100,142	5.2	21.8	117,252	4.4	25.5	-	-17,110	-3.7
1994-95	109,720	8.6	22.5	122,901	3.9	25.3	-	-13,181	-2.7
1995-96	121,105	7.7	23.4	131,182	4.1	25.3	-	-10,077	-1.9
1996-97	129,845	5.5	23.8	135,126	1.4	24.8	-	-5,281	-1.0
1997-98	135,779	3.2	23.5	134,608	-1.7	23.3	-	1,171	0.2
1998-99	146,496	7.6	24.1	142,159	5.3	23.4	-	4,337	0.7
1999-00	166,089	na	25.7	153,030	na	23.7	-	13,059	2.0
2000-01	161,114	-7.1	23.4	155,143	-2.9	22.5	-	5,970	0.9
2001-02	162,884	-1.2	22.1	163,867	3.2	22.3	-	-983	-0.1
2002-03	176,503	5.1	22.5	169,017	0.1	21.6	-	7,486	1.0
2003-04	187,336	2.5	22.3	179,300	2.5	21.4	-	8,036	1.0
2004-05	203,960	4.8	22.8	190,344	2.1	21.3	-	13,616	1.5
2005-06(e)	222,400	4.3	23.3	207,512	4.3	21.7	83	14,805	1.5
2006-07(e)	**230,819**	**1.3**	**22.9**	**218,225**	**2.6**	**21.6**	**1,766**	**10,828**	**1.1**
2007-08(p)	239,517	2.9	22.8	226,906	3.1	21.6	1,983	10,628	1.0
2008-09(p)	250,663	3.7	22.8	237,329	3.6	21.6	2,109	11,225	1.0
2009-10(p)	263,994	3.3	22.9	249,708	3.2	21.6	2,267	12,019	1.0

(a) There is a break in the series between 1998-99 and 1999-00. Data for the years up to and including 1998-99 are consistent with the cash ABS GFS reporting requirements. From 1999-00, data are derived from an accrual ABS GFS reporting framework, with receipts proxied by receipts from operating activities and sales of non-financial assets, and payments proxied by payments for operating activities, purchases of non-financial assets and net acquisition of assets under finance leases. Due to associated methodological and data source changes, time series data that encompass measures derived under both cash and accrual accounting should be used with caution.

(b) Underlying cash balance is equal to receipts less payments less expected Future Fund earnings. For the purposes of consistent comparison with years prior to 2005-06, Future Fund earnings should be added back to the underlying cash balance.

(c) Receipts and payments outcomes since 1999-00 have increased from that reported in the 2005-06 MYEFO, following a reclassification of fringe benefits tax in GFS by the ABS (see Statement 5 Appendix C).

(e) Estimates.

(p) Projections.

na Not applicable, due to a structural break in the series.

Table 2: Australian Government general government sector taxation receipts, non-taxation receipts and total receipts[(a)(b)]

	Taxation receipts			Non-taxation receipts			Total receipts		
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP
1973-74	10,832	12.5	18.3	1,058	-7.8	1.8	11,890	10.4	20.1
1974-75	14,141	7.1	20.2	1,184	-8.2	1.7	15,325	5.8	21.9
1975-76	16,920	3.7	20.7	1,396	2.2	1.7	18,316	3.6	22.4
1976-77	19,714	3.8	20.9	1,704	8.7	1.8	21,418	4.1	22.7
1977-78	21,428	-0.1	20.8	2,063	11.3	2.0	23,491	0.8	22.8
1978-79	23,409	3.1	20.0	2,257	3.3	1.9	25,666	3.2	22.0
1979-80	27,473	7.2	20.7	2,307	-6.7	1.7	29,780	6.0	22.5
1980-81	32,641	7.5	21.8	2,507	-1.7	1.7	35,148	6.8	23.4
1981-82	37,880	2.7	21.9	2,951	4.2	1.7	40,831	2.8	23.6
1982-83	41,025	-2.7	22.0	3,650	11.2	2.0	44,675	-1.7	24.0
1983-84	44,849	2.4	21.3	4,253	9.1	2.0	49,102	2.9	23.4
1984-85	52,970	12.2	22.8	4,788	7.0	2.1	57,758	11.8	24.9
1985-86	58,841	4.6	23.0	6,004	18.1	2.3	64,845	5.7	25.3
1986-87	66,467	5.4	23.7	6,678	3.8	2.4	73,145	5.2	26.1
1987-88	75,076	5.2	23.5	6,141	-14.3	1.9	81,217	3.4	25.4
1988-89	83,452	2.4	23.0	4,917	-26.2	1.4	88,369	0.3	24.4
1989-90	90,773	2.5	22.8	4,744	-9.1	1.2	95,517	1.8	24.0
1990-91	92,739	-2.7	22.7	4,966	-0.3	1.2	97,705	-2.5	23.9
1991-92	87,364	-7.5	21.0	5,602	10.7	1.3	92,966	-6.6	22.3
1992-93	88,760	0.4	20.3	5,688	0.3	1.3	94,448	0.4	21.6
1993-94	93,362	4.4	20.3	6,780	18.3	1.5	100,142	5.2	21.8
1994-95	104,921	11.4	21.6	4,799	-29.8	1.0	109,720	8.6	22.5
1995-96	115,700	7.6	22.3	5,405	9.9	1.0	121,105	7.7	23.4
1996-97	124,559	5.9	22.8	5,286	-3.8	1.0	129,845	5.5	23.8
1997-98	130,984	3.8	22.7	4,795	-10.5	0.8	135,779	3.2	23.5
1998-99	141,105	7.4	23.2	5,391	12.1	0.9	146,496	7.6	24.1
1999-00	151,313	na	23.5	14,777	na	2.3	166,089	na	25.7
2000-01	146,698	-7.2	21.3	14,416	-6.6	2.1	161,114	-7.1	23.4
2001-02	148,343	-1.2	20.2	14,541	-1.5	2.0	162,884	-1.2	22.1
2002-03	161,418	5.6	20.6	15,084	0.7	1.9	176,503	5.1	22.5
2003-04	173,023	3.5	20.6	14,313	-8.3	1.7	187,336	2.5	22.3
2004-05	188,176	4.6	21.1	15,784	6.1	1.8	203,960	4.8	22.8
2005-06(e)	204,469	4.0	21.4	17,930	8.7	1.9	222,400	4.3	23.3
2006-07(e)	**213,188**	**1.8**	**21.1**	**17,631**	**-4.0**	**1.7**	**230,819**	**1.3**	**22.9**
2007-08(p)	221,974	3.3	21.1	17,543	-1.3	1.7	239,517	2.9	22.8
2008-09(p)	232,477	3.7	21.2	18,186	2.7	1.7	250,663	3.7	22.8
2009-10(p)	245,056	3.4	21.2	18,937	2.2	1.6	263,994	3.3	22.9

(a) There is a break in the series between 1998-99 and 1999-00. Data for the years up to and including 1998-99 are consistent with the cash ABS GFS reporting requirements. From 1999-00, data are derived from an accrual ABS GFS reporting framework, with receipts proxied by receipts from operating activities and sales of non-financial assets. Due to associated methodological and data source changes, time series data that encompass measures derived under both cash and accrual accounting should be used with caution.

(b) Taxation receipts outcomes for the period since 1999-00 have increased from that reported in the 2005-06 MYEFO. This is due to the inclusion of some levies previously classified under non-taxation receipts, and the reclassification of fringe benefits tax in GFS by the ABS.

(e) Estimates.

(p) Projections.

na Not applicable, due to a structural break in the series.

Table 3: Australian Government general government sector net debt and net interest payments[(a)]

	Net debt		Net interest payments(b)	
	$m	Per cent of GDP	$m	Per cent of GDP
1973-74	-1,851	-3.1	-306	-0.5
1974-75	-1,901	-2.7	-267	-0.4
1975-76	-341	-0.4	-389	-0.5
1976-77	898	1.0	-161	-0.2
1977-78	2,896	2.8	-106	-0.1
1978-79	4,983	4.3	126	0.1
1979-80	6,244	4.7	290	0.2
1980-81	6,356	4.2	444	0.3
1981-82	5,919	3.4	475	0.3
1982-83	9,151	4.9	654	0.4
1983-84	16,015	7.6	1,327	0.6
1984-85	21,896	9.4	2,462	1.1
1985-86	26,889	10.5	3,626	1.4
1986-87	29,136	10.4	4,387	1.6
1987-88	27,359	8.6	4,019	1.3
1988-89	21,982	6.1	3,722	1.0
1989-90	16,121	4.1	3,848	1.0
1990-91	16,936	4.1	2,834	0.7
1991-92	31,132	7.5	2,739	0.7
1992-93	55,218	12.6	2,912	0.7
1993-94	70,223	15.3	4,549	1.0
1994-95	83,492	17.2	6,310	1.3
1995-96	95,831	18.5	7,812	1.5
1996-97	96,281	17.6	8,449	1.5
1997-98	82,935	14.4	7,381	1.3
1998-99	70,402	11.6	6,901	1.1
1999-00	53,768	8.3	6,014	0.9
2000-01	42,651	6.2	4,855	0.7
2001-02	38,024	5.2	4,238	0.6
2002-03	29,665	3.8	3,641	0.5
2003-04	23,421	2.8	2,994	0.4
2004-05	11,534	1.3	2,463	0.3
2005-06(e)	-4,784	-0.5	2,535	0.3
2006-07(e)	**-22,075**	**-2.2**	**452**	**0.0**
2007-08(p)	-24,743	-2.4	303	0.0
2008-09(p)	-37,140	-3.4	-243	0.0
2009-10(p)	-50,184	-4.3	-928	-0.1

(a) There is a break in the net debt and net interest series between 1998-99 and 1999-00 (the first year of accrual budgeting). Up to 1998-99, Australian Government general government debt instruments are valued at historic cost. From 1999-00, Australian Government general government debt instruments are valued at market prices, consistent with accrual GFS standards.
(b) Excludes superannuation related interest flows.
(e) Estimates.
(p) Projections.

Table 4: Australian Government general government sector revenue, expenses, net capital investment, fiscal balance and net worth[(a)]

	Revenue(c)		Expenses(c)		Net capital investment		Fiscal balance		Net worth(b)	
	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP	$m	Per cent of GDP
1996-97	141,688	26.0	145,809	26.7	90	0.0	-4,211	-0.8	-74,354	-13.6
1997-98	146,820	25.4	148,646	25.7	147	0.0	-1,973	-0.3	-68,544	-11.9
1998-99	151,897	25.0	146,620	24.1	1,433	0.2	3,844	0.6	-76,150	-12.5
1999-00	167,158	25.9	156,492	24.3	-1,225	-0.2	11,892	1.8	-40,552	-6.3
2000-01	162,074	23.5	157,667	22.9	-1,168	-0.2	5,575	0.8	-43,299	-6.3
2001-02	162,956	22.1	166,758	22.7	-369	-0.1	-3,433	-0.5	-48,429	-6.6
2002-03	175,513	22.4	170,999	21.8	-219	0.0	4,734	0.6	-53,251	-6.8
2003-04	187,924	22.4	182,371	21.8	724	0.1	4,830	0.6	-39,595	-4.7
2004-05	206,605	23.1	195,680	21.9	147	0.0	10,778	1.2	-32,108	-3.6
2005-06(e)	222,864	23.3	206,018	21.6	881	0.1	15,966	1.7	-24,026	-2.5
2006-07(e)	**231,662**	**23.0**	**219,730**	**21.8**	**1,642**	**0.2**	**10,290**	**1.0**	**-12,001**	**-1.2**
2007-08(p)	240,671	22.9	230,556	21.9	174	0.0	9,940	0.9	-2,330	-0.2
2008-09(p)	252,078	23.0	240,910	22.0	602	0.1	10,566	1.0	8,783	0.8
2009-10(p)	265,603	23.0	252,592	21.9	38	0.0	12,972	1.1	21,632	1.9

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net worth is calculated as assets less liabilities.

(b) There is a break in the net worth series between 1998-99 and 1999-00. Data up to 1998-99 are sourced from the Australian Government's Consolidated Financial Statements based on Australian accounting standards. Data beginning in 1999-00 are based on the GFS framework. For the general government sector, the major change across the break in the series is an improvement in net worth. This is primarily due to the move from valuing investments in public corporations at historic cost to current market value (which is calculated using the share price for listed corporations). This is partly offset by defence weapons platforms no longer being recorded as assets and valuing debt at current market value.

(c) Revenue and expenses outcomes since 1999-00 have increased from that reported in the 2005-06 MYEFO, following a reclassification of fringe benefits tax in GFS by the ABS.

(e) Estimates.

(p) Projections.

Table 5: Australian Government general government sector accrual taxation revenue, non-taxation revenue and total revenue[(a)]

	Taxation revenue			Non-taxation revenue			Total revenue		
	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP	$m	Per cent real growth	Per cent of GDP
2000-01	152,080	na	22.1	9,994	na	1.4	162,074	na	23.5
2001-02	150,873	-3.1	20.5	12,083	18.1	1.6	162,956	-1.8	22.1
2002-03	163,957	5.4	20.9	11,556	-7.2	1.5	175,513	4.5	22.4
2003-04	175,838	3.6	21.0	12,085	1.0	1.4	187,924	3.4	22.4
2004-05	194,150	6.2	21.7	12,455	-0.8	1.4	206,605	5.8	23.1
2005-06(e)	208,085	2.6	21.8	14,779	13.5	1.5	222,864	3.2	23.3
2006-07(e)	**217,157**	**1.9**	**21.5**	**14,505**	**-4.2**	**1.4**	**231,662**	**1.5**	**23.0**
2007-08(p)	226,076	3.3	21.5	14,595	-0.2	1.4	240,671	3.1	22.9
2008-09(p)	236,741	3.7	21.6	15,338	4.1	1.4	252,078	3.8	23.0
2009-10(p)	249,452	3.4	21.6	16,151	3.3	1.4	265,603	3.4	23.0

(a) Taxation revenue outcomes for the period since 2000-01 have increased from that reported in the 2005-06 MYEFO. This is due to the inclusion of some levies previously classified under non-taxation revenue, and the reclassification of fringe benefits tax in GFS by the ABS.
(e) Estimates.
(p) Projections.
na Data not available.

Table 6: Australian Government cash receipts, payments and surplus by institutional sector ($m)[(a)]

	General government			Public non-financial corporations			Non-financial public sector		
	Receipts	Payments	Underlying cash balance(b)	Receipts	Payments	Cash surplus	Receipts	Payments	Cash surplus(b)
1988-89	88,369	82,202	6,167	4,177	6,035	257	91,544	87,188	6,424
1989-90	95,517	88,882	6,635	3,926	11,322	-5,261	98,387	99,081	1,374
1990-91	97,705	97,333	372	4,804	9,351	-2,139	101,315	105,476	-1,767
1991-92	92,966	104,551	-11,585	3,899	7,713	101	95,063	110,448	-11,484
1992-93	94,448	111,484	-17,036	4,385	7,819	-196	97,327	117,775	-17,232
1993-94	100,142	117,252	-17,110	5,178	6,476	1,482	103,065	121,457	-15,628
1994-95	109,720	122,901	-13,181	5,262	7,318	1,956	113,013	128,247	-11,225
1995-96	121,105	131,182	-10,077	4,927	8,190	-527	123,269	136,607	-10,604
1996-97	129,845	135,126	-5,281	4,782	7,373	473	131,512	139,385	-4,808
1997-98	135,779	134,608	1,171	6,238	7,923	1,119	139,560	140,006	2,290
1998-99	146,496	142,159	4,337	na	na	-353	na	na	3,984
1999-00	166,089	153,030	13,059	na	na	-2,594	na	na	10,465
2000-01	161,114	155,143	5,970	na	na	391	na	na	6,362
2001-02	162,884	163,867	-983	na	na	1,210	na	na	227
2002-03	176,503	169,017	7,486	27,386	26,105	1,280	na	na	8,766
2003-04	187,336	179,300	8,036	27,718	26,142	1,575	238,184	227,001	9,611
2004-05	203,960	190,344	13,616	29,621	28,071	1,550	257,897	241,489	15,167
2005-06(e)	222,400	207,512	14,805	30,115	31,868	-1,753	279,532	266,397	13,052
2006-07(e)	**230,819**	**218,225**	**10,828**	**14,680**	**15,785**	**-1,105**	**278,708**	**267,219**	**9,723**
2007-08(p)	239,517	226,906	10,628	na	na	na	na	na	na
2008-09(p)	250,663	237,329	11,225	na	na	na	na	na	na
2009-10(p)	263,994	249,708	12,019	na	na	na	na	na	na

(a) There is a break in the series between 1998-99 and 1999-00. Data for the years up to and including 1998-99 are consistent with the cash ABS GFS reporting requirements. From 1999-00 onwards, data are derived from an accrual ABS GFS reporting framework, with receipts proxied by receipts from operating activities and sales of non-financial assets, and payments proxied by payments for operating activities, purchases of non-financial assets and net acquisition of assets under finance leases. Due to associated methodological and data source changes, time series data which encompass measures derived under both cash and accrual accounting should be used with caution.

(b) These items exclude expected Future Fund earnings from 2005-06 onwards. Expected Future Fund earnings are shown in Table 1.

(e) Estimates.

(p) Projections.

na Data not available.

Table 7: Australian Government accrual revenue, expenses and fiscal balance by institutional sector[(a)]

	General government			Public non-financial corporations			Non-financial public sector		
	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance	Revenue	Expenses	Fiscal balance
1996-97	141,688	145,809	-4,211	27,431	26,015	-331	na	na	-4,542
1997-98	146,820	148,646	-1,973	29,618	26,999	2,360	na	na	387
1998-99	151,897	146,620	3,844	27,687	26,088	-816	175,682	168,806	3,028
1999-00	167,158	156,492	11,892	25,485	23,542	1,062	188,695	174,929	12,953
2000-01	162,074	157,667	5,575	25,869	24,762	-826	183,337	177,823	4,750
2001-02	162,956	166,758	-3,433	26,638	25,341	793	184,986	187,491	-2,640
2002-03	175,513	170,999	4,734	24,339	22,916	1,975	194,725	188,829	6,709
2003-04	187,924	182,371	4,830	25,449	23,444	2,143	207,628	200,070	6,973
2004-05	206,605	195,680	10,778	26,965	25,191	1,473	227,685	214,986	12,250
2005-06(e)	222,864	206,018	15,966	27,969	28,899	-3,100	245,127	229,211	12,866
2006-07(e)	**231,662**	**219,730**	**10,290**	**13,711**	**14,152**	**-1,247**	**242,795**	**231,303**	**9,043**
2007-08(p)	240,671	230,556	9,940	na	na	na	na	na	na
2008-09(p)	252,078	240,910	10,566	na	na	na	na	na	na
2009-10(p)	265,603	252,592	12,972	na	na	na	na	na	na

(a) The fiscal balance is equal to revenue less expenses less net capital investment. Net capital investment is not shown in this table.
(e) Estimates.
(p) Projections.
na Data not available.