

# 1 OVERVIEW – MEDIUM TERM FISCAL STRATEGY

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Framing a budget in an environment of falling revenues and continuing uncertainty is challenging. Queensland, like other economies around the world and in Australia, has been significantly impacted by the global economic downturn. Since the 2008-09 Budget, this downturn has stripped \$15 billion off the forward estimates of the State's key revenue streams of royalties, taxes and GST. Understandably this has had a significantly negative impact on Queensland's operating position, with the State forecasting deficits across each of the Budget and forward estimate years.

While current economic conditions prevail, the Queensland Government's objective is to continue to invest in infrastructure to sustain jobs. The 2009-10 Budget does this with a projected 2009-10 capital program of \$18.2 billion which is forecast to support 127,000 full-time jobs.

However, the Government also recognises the need to ensure the health of the Queensland economy in the medium and longer term and is cognisant of the part played by sound financial management and fiscal sustainability in supporting this growth. As a result, the Government has implemented a number of measures that are aimed at improving Queensland's fiscal position. Key initiatives in this Budget include:

- revised fiscal principles including a commitment to return to surplus
- abolition of the Queensland Fuel Subsidy Scheme
- further public sector efficiency measures which leverage off savings from the recent machinery of government changes
- reform to local government grants and subsidy programs
- revision to the Government's wages policy
- changes to procurement policy
- a comprehensive program of asset sales.

These are in addition to the following measures, announced since the 2008-09 Budget:

- Government-owned corporation reform
- closure of the defined benefits scheme
- taxation measures announced in December 2008.

The total value of these initiatives, excluding asset sales, is around \$5.4 billion over four years.

## FISCAL STRATEGY

### Revised fiscal principles

The unprecedented economic and financial conditions arising from the global financial crisis have had significant adverse effects on the State's financial position. In this environment, the Government has adopted a new fiscal strategy, setting out how it will restore Queensland's traditionally strong financial position, while maintaining services and continuing to deliver its commitments to the community.

To ensure the fiscal strategy is transparent and credible, the Government introduced the *Financial Accountability Act 2009* which, among other things, requires the Treasurer to prepare and table in the Legislative Assembly a *Charter of Fiscal Responsibility* giving details of the Government's fiscal objectives and the fiscal principles that support those objectives.

The Treasurer must report regularly to the Legislative Assembly on progress the Government has made against the outcomes stated in the Charter. This report will be tabled and published each year in the Budget papers, Mid Year Fiscal and Economic Review and Report on State Finances.

The fiscal principles of the Queensland Government are broadly based around three themes: fiscal sustainability; a competitive tax regime; and managing the State's balance sheet.

Since the 2008-09 Budget, the Queensland Government has taken a number of measures, totalling some \$5.4 billion over four years, to improve the State's financial position, including measures to reduce:

- the operating deficit, such as abolition of the fuel subsidy scheme, improving the efficiency of public sector service delivery and increasing revenue; and
- the level of debt, such as asset sales.

In addition to these measures, the wages policy for public sector employees will restrict expenditure growth, particularly in the years beyond the forward estimates.

## ***Fiscal sustainability***

Governments must balance the cost of their activities with the revenues raised by taxation, royalties and income from business activities. It is not sustainable for governments to borrow to fund recurrent expenses, as the resultant interest costs and repayment of debt will be borne by future taxpayers, at the expense of other government services or through higher taxes.

On the other hand, capital investment benefits users and society more generally over the life of the asset. It is therefore appropriate to borrow to fund capital investment, so that the costs of the investment are paid over the same time frame as the benefits that are realised.

### **Principle**

In the General Government sector, meet all operating expenses from operating revenue (where operating revenue is defined as total revenue from transactions and operating expenses are defined as total expenses from transactions less depreciation).

In this financial environment, fiscal discipline is important. Until it achieves an operating surplus, growth in state own purpose expenses (that is, excluding Commonwealth related expenses) will be limited to inflation and population growth. This is projected to be 4.75% in 2009-10.

### **Principle**

Growth in own-purpose expenses in the General Government sector to not exceed real per capita growth.

The approach to expenses growth, together with the impact of the large asset sale program not yet factored into the forward estimates, is aimed at achieving a net operating surplus in the General Government sector by 2015-16 and, depending on the strength of the recovery, possibly sooner.

Further details on expenses projections are contained in Chapter 7.

### **Principle**

Achieve a General Government net operating surplus as soon as possible, but no later than 2015-16.

## ***Competitive tax regime***

One of the Queensland Government's key fiscal objectives is to maintain a competitive tax environment. While the Government will raise sufficient revenue to meet the service and infrastructure needs of the people of Queensland, it is important that business has a low cost environment, to promote economic development and jobs growth.

### **Principle**

Maintain a competitive tax environment for business.

The competitiveness of a State's tax system is usually assessed by using one of the following measures:

- taxation revenue on a per capita basis
- taxation effort as assessed by the Commonwealth Grants Commission
- taxation revenue expressed as a percentage of gross state product (GSP).

Queensland's competitive tax position is confirmed on all three measures:

- per capita tax collections in Queensland in 2009-10 are estimated at \$2,087, compared with an estimated \$2,487 for the average of the other states
- Commonwealth Grants Commission data indicate that Queensland's taxation effort ratio was 85.6% of the standard for all states in 2007-08
- Queensland's tax collections were 4.46% of GSP in 2007-08, compared to 4.75% for the average of the other states.

The 2009-10 Budget and the Mid Year Fiscal and Economic Review include changes to transfer duty, payroll tax, land tax, casino taxes and motor vehicle registration fees. Details of these changes and other revenue items are provided in Chapter 6.

## ***Managing the State's balance sheet***

The provision of adequate levels of infrastructure is an ongoing challenge for a state such as Queensland that continues to experience higher levels of economic and population growth than the national average. In meeting this challenge, the Government funds capital expenditure well above the average of the other states and territories, in per capita terms.

As discussed above, Queensland funds its capital program primarily through borrowing, recognising the interest, operating and depreciation costs on the operating statement. It will also be necessary to borrow to fund operating deficits. While the balance sheet of the Queensland Government remains strong, the increased borrowing, coupled with a significant fall in revenue arising as a result of the global financial crisis has led to an increase in the ratio of net financial liabilities<sup>1</sup> to revenue, which is a measure used by financial markets to assess financial sustainability.

This ratio is expected to be 117% at the end of the 2009-10 financial year and to stabilise at below 130% after completion of the asset sales program.

### **Principle**

Stabilise net financial liabilities as a proportion of revenue in the Non-financial Public sector.

Queensland has a long history of setting aside funds to accumulate financial assets sufficient to meet future liabilities, the largest being for future employee entitlements, in particular superannuation. Queensland is therefore far better placed than other state governments to meet future accruing liabilities, as most other jurisdictions have substantial unfunded superannuation liabilities.

The State's policy of setting aside funds to meet future liabilities and reinvesting all earnings provides the capacity to manage cycles in investment markets without affecting the Government's ability to fund services to the community.

### **Principle**

Target full funding of long-term liabilities such as superannuation in accordance with actuarial advice.

Further information on balance sheet aggregates can be found in Chapter 8.

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<sup>1</sup> Net financial liabilities in this context is the term used by Standard & Poor's ratings agency and differs from that used in the Uniform Presentation Framework tables in Chapter 10.

**Table 1.1**  
**The fiscal principles of the Queensland Government**

Principle	Indicator	
<b>Fiscal sustainability</b>		
In the General Government sector, meet all operating expenses from operating revenue  (where operating revenue is defined as total revenue from transactions and operating expenses are defined as total expenses from transactions less depreciation)	<i>Operating Revenue<sup>1</sup></i> <i>(\$ million)</i>	<i>Operating expenses less depreciation</i> <i>(\$ million)</i>
	2009 10	36,373
	2010 11	37,444
	2011 12	38,930
	2012 13	40,327
Growth in own purpose expenses in the General Government sector to not exceed real per capita growth	<i>Growth in:</i>	<i>Own purpose expense<sup>2</sup></i>
	2009 10	4.75%
	2010 11	4.50%
	2011 12	4.50%
	2012 13	4.75%
Avg over FEs	4.63%	
Achieve a General Government net operating surplus as soon as possible, but no later than 2015 16	<i>Net operating balance (\$ million)</i>	
	2009 10	(1,954)
	2010 11	(3,459)
	2011 12	(4,090)
	2012 13	(3,290)
<b>Competitive tax regime</b>		
Maintain a competitive tax environment for business	<i>Taxation revenue per capita, 2009 10</i>	
	Queensland:	\$2,087
	Average of other states and territories:	\$2,487
<b>Managing the State's balance sheet</b>		
Stabilise net financial liabilities as a proportion of revenue in the Non Financial Public Sector	<i>Net Financial Liabilities/Revenue</i> <i>Non financial Public Sector</i>	
		<i>Before asset sales</i>
		<i>After asset sales</i>
	2009 10	116%
	2010 11	128%
2011 12	125%	
2012 13	130%	
Target full funding of long term liabilities such as superannuation in accordance with actuarial advice	As at last actuarial review (released June 2008), accruing superannuation liabilities were fully funded. The State Actuary reviews the scheme every 3 years.	
Notes:		
1. The reduction in revenue in 2010-11 reflects additional Australian Government funding in 2009-10 associated with initiatives such as the <i>Nation Building and Jobs Plan</i> .		
2. Superannuation interest costs have been normalised to reflect the assumed long run rate of return.		

## **Abolition of the Queensland Fuel Subsidy Scheme**

The Government has decided to cease the Queensland Fuel Subsidy Scheme from 1 July 2009, saving around \$2.4 billion over the next four years.

There are several compelling reasons to now abolish the fuel subsidy.

- The State's fiscal position makes the retention of the fuel subsidy scheme unsustainable. The Government would be required to borrow to continue to fund the fuel subsidy. To borrow for this purpose would run counter to the principle of intergenerational equity, as future generations would be required to fund the services consumed today.
- The Queensland Fuel Subsidy Scheme does not represent value for money to Queensland taxpayers. The scheme currently benefits interstate consumers and businesses purchasing retail fuel in Queensland or establishing a bulk end user fuel storage site in the State. The Pincus Inquiry into the effectiveness of the scheme, found that much of the diesel sold for commercial purposes is consumed outside the State. It also found that there was no practical way of preventing interstate businesses from benefiting from the fuel subsidy other than by abolishing it.
- The Pincus Inquiry recommended that the scheme be abolished if Government could not find a way to ensure the subsidy was being passed on. Evidence given to the Inquiry and an opinion from the Solicitor-General concluded that there is no perfect system to ensure that the subsidy is fully passed on. None of the submissions to the Inquiry or during public consultation identified workable options for improvement.

Further details on the cessation of the Queensland Fuel Subsidy Scheme can be found in Budget Paper 4 - Measures.

## **Further public sector efficiency measures**

In the 2008-09 Budget, the Queensland Government announced a public sector efficiency target of \$60 million in 2008-09, growing to \$80 million from 2009-10. Given the savings to be derived from the recently announced machinery of government reforms as well as the savings being realised through efficiency and productivity improvements in the areas of corporate overheads, travel, publication, marketing and communication costs, these targets have been increased to a total of \$280 million per year from 2009-10. These savings targets will not impact on front line service delivery.

## **Reform to local government grants and subsidy programs**

In 2006-07, the Government announced a program of \$700 million over five years for a suite of grants and subsidy programs to support local government to deliver the infrastructure for which they are responsible. To date, projects with a total subsidy value of \$880.5 million have been approved for construction. Of this total, \$388.5 million has already been paid to local governments.

Given the potential for efficiencies and savings being delivered through the Local Government Reform Program and the significant increase in grant and subsidy funding, the Government reviewed ongoing arrangements for funding of local government infrastructure.

As a result, the Government has decided to overhaul the current suite of local government grant and subsidy programs. The current programs will cease on 16 June 2009. Existing approved commitments will be met, subject to claims being lodged a maximum of three years from the date the application was approved.

Subsidy payments to local governments for street lighting will also cease. These funds are being redirected towards the increased funds allocated to the Pensioner Electricity Rebate Scheme.

A new \$45 million per annum local government infrastructure program will be introduced which will be more targeted. Through introducing revised funding criteria, the Government will ensure that subsidies are delivered to those councils and communities that have infrastructure projects that are ready to be delivered and do not have the financial capability to deliver the projects without assistance.

The \$2 million annual show subsidy scheme administered by the Department of Infrastructure and Planning will continue.

## **Taxation measures**

As a result of tight fiscal conditions brought about by the downturn in the global economy, the Queensland Government has decided to implement a number of taxation measures to enable it to continue to fund services to the community and maintain the capital program.

### ***Motor vehicle registration***

The Government will increase motor vehicle registration fees commencing 1 July 2009. These increases were detailed in the Mid Year Fiscal and Economic Review which, in addition, stated motor vehicle registration costs from 1 July 2009 will incorporate adjustments for the Consumer Price Index and changes to Compulsory Third Party premiums.

Further detail on this initiative can be found in Budget Paper 4 – Measures and the Mid Year Fiscal and Economic Review.

### ***Delay in abolition of transfer duty on core business assets***

The *Intergovernmental Agreement for the Reform of Commonwealth-State Financial Relations* (IGA), agreed by the Australian Government and all state and territory governments in 1999, required the abolition and review of a number of state taxes.

Following the review of duties listed in the IGA, a timetable for the abolition of the majority of these duties was announced in the 2005-06 Budget.

To date, the Government has completed all of the duty abolitions listed in this timetable in accordance with the timeframes agreed under the scheduled.

It was intended to halve duty on the transfer of core business assets from 1 July 2010, with full abolition from 1 January 2011. The 2008-09 Mid Year Fiscal and Economic Review extended this timeframe to 1 July 2012.

In light of the tight fiscal conditions, the abolition of this duty will now occur by 1 July 2013, in accordance with the timeframe included in the new *Intergovernmental Agreement on Federal Financial Relations*.

## **Casino gaming machines**

In order to reduce the disparity that exists between the tax rates applicable to gaming machines in casinos and those applicable to large clubs and hotels, the tax rate on gaming machine win on casino gaming machines will increase by 10% from 1 July 2009, to 20% at the Breakwater Island (Jupiters Townsville) and Reef (Cairns) casinos and from 20% to 30% at the Conrad Jupiters (Gold Coast) and Conrad International Treasury (Brisbane) casinos. At the same time, the concessional tax rate applicable to premium play at the Breakwater Island and Reef casinos will be removed. This initiative was announced in the Mid Year Fiscal and Economic Review.

## **Land tax**

As announced in the Mid Year Fiscal and Economic Review, from 1 July 2009, a 0.5% surcharge will apply where the aggregate value of all land (for land tax purposes) exceeds \$5 million. The surcharge will apply only to the portion of the value exceeding \$5 million. The surcharge is estimated to apply to around 2,000 of Queensland's 53,000 land tax payers (around 3.7%).

Further details on this initiative can be found in Budget Paper 4 – Measures and the Mid Year Fiscal and Economic Review.

## **Wages policy**

The Government is committed to maintaining wage increases as prescribed in the Memorandum of Understanding (MOU) with unions for all agreements covered by the MOU.

All other agreements that have expired or are due to expire by 31 December 2009, will have until 1 September 2009 to reach an agreement. Where an agreement is not reached by this date, and for agreements expiring after 31 December 2009, a new Government wages policy will apply which limits wage increases to 2.5% per annum until the Budget returns to surplus. The new policy will apply to Chief Executives, Senior Executives and Senior Officers and their equivalents from 1 July 2009.

## **Changes to procurement policy**

The Government considers a range of procurement options for delivery of major capital projects, including construct-only; design and construct; design, construct and maintain; alliance contracting; managing contractor model; public-private partnerships; and hybrid delivery models. To achieve optimal project outcomes, the procurement approach must be appropriate for the risks and issues each project is likely to face in practice.

In recent years, alliance contracting, where Government and its alliance partners share the risks and responsibilities in delivery the construction phase of a project, has featured significantly in certain areas of infrastructure delivery. While the Government will continue to consider alliance contracting where appropriate, in selecting procurement approaches for each major project, the Government will be particularly focused on driving competitive, value for money project delivery outcomes which reflect current market conditions.

### **Government-owned corporation reform**

As outlined in the Mid Year Fiscal and Economic Review, the Government has been working with its Government-owned corporations (GOCs) to improve their efficiency, effectiveness and accountability. The aim has been to provide GOCs with appropriate organisational structures and incentive frameworks to allow them to operate to their full commercial potential.

More information on this initiative can be found in the Mid Year Fiscal and Economic Review and in Chapter 5.

### **Closure of the defined benefit scheme**

Earlier this financial year the Government announced the closure of QSuper's defined benefit account to new members, effective from the date of announcement.

Before the closure of the scheme, Queensland was the only Government in Australia that still had a broad based, open defined benefit scheme. Other states and the Commonwealth all stopped offering defined benefit schemes over the past 15 years.

This action was taken to protect the current entitlements of existing defined benefit members and to ensure that the scheme's liabilities are not exposed to risks that flow from the decline in global equity markets.

## **Asset sales**

In order to protect the State's capital program while maintaining a prudent fiscal approach, the Government announced, on 2 June 2009, a significant infrastructure assets reform and sale program.

This program will involve:

- the sale of Forestry Plantations Queensland's softwood business and possibly its hardwood plantations
- the sale of Queensland Motorways Limited's (QML) business, incorporating a major upgrade of the Port of Brisbane Motorway
- the sale of the Port of Brisbane Corporation Limited's (PBC) business and assets
- the sale of QR Limited's (QR) above and below rail coal businesses and assets, along with Ports Corporation of Queensland Limited's Abbot Point Coal Terminal
- the intention to instigate negotiations with the Australian Government over the potential sale of other parts of QR's below rail network to the Australian Government-owned Australian Rail Track Corporation
- investigating options for the most appropriate way to offer the sale of Queensland Rail's bulk freight, intermodal, retail and regional freight services to the market.

In recognition of the complexity of the process and the need to undertake detailed planning in relation to appropriate sale structures, the Government envisages that the sales will be progressed in the market over the next three to five years. The sale program will deliver an estimated \$15 billion in sale proceeds, and result in approximately \$12 billion in required capital investment over the next five years being avoided. The staging of the asset sales will be influenced by the timing of the recovery in financial markets. The impact of the asset sales has not been factored into the Budget estimates.

## ***Economic impact***

The Government recognises the need to ensure that the Queensland economy emerges from the current economic conditions in a strong position to drive the future growth and job creation opportunities for both the State and national economies.

In this regard, the asset sales program has a strong export focus. The sale of QR's coal businesses provides an opportunity to further integrate coal export chains. The inclusion of Abbot Point Coal Terminal in the sales package is expected to further facilitate the integration of rail-to-port networks, and ensure that the objectives of port and rail infrastructure providers are more closely aligned.

Similar opportunities exist in relation to export infrastructure in South East Queensland. The sale of PBC, in conjunction with QML, the operator of key road infrastructure servicing the Port of Brisbane and the southern Queensland road network more generally, is expected to facilitate the development of both the Port of Brisbane and surrounding infrastructure.

In combination, the asset sales package is designed to encourage the private sector to play a more active role in providing and funding the key economic infrastructure which is essential in promoting economic growth.

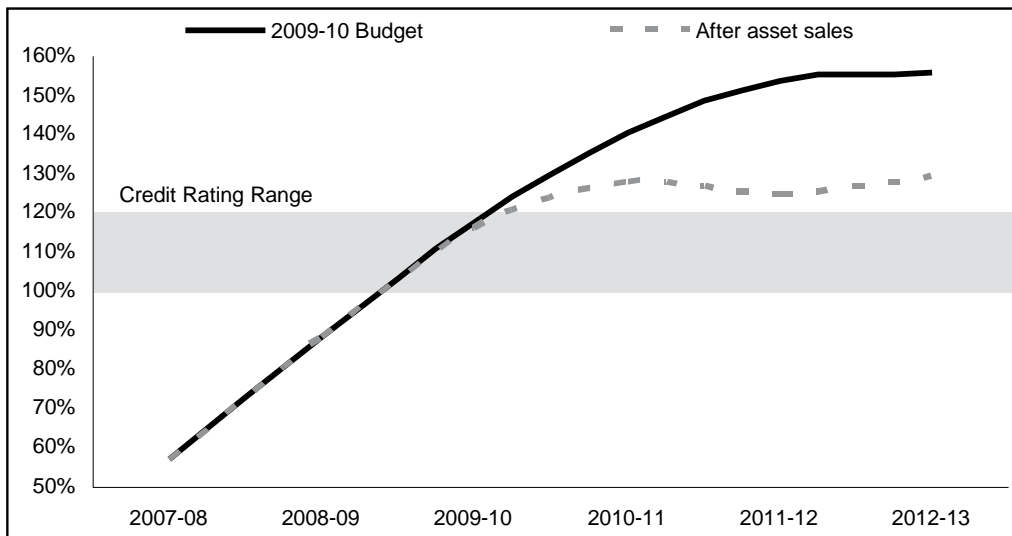
### ***Financial considerations***

The 2009-10 Budget focuses on supporting the continued delivery of key public infrastructure such as schools, hospitals and public transport, and the delivery of public services through these facilities.

The Government expects to forgo dividends and tax equivalent payments as a result of the asset sales. However, interest savings on sale proceeds and the additional capital expenditure of \$12 billion avoided as a result of the sales will benefit the Budget.

The following chart shows, on balance, the overall favourable impact the expected sale proceeds will have on one of the key credit rating ratios (net financial liabilities to revenue), after accounting for forgone revenue. Chart 1.1 indicates that the ratio stabilises at below 130% following these asset sales.

**Chart 1.1**  
**Net financial liabilities to revenue ratio, before and after asset sales**



Notes:

1. The figures in this chart assume the sales are completed by 2012-13.
2. Based on a broad range for AAA rated states.

The program of asset sales will play an important role in funding the Government's infrastructure program, reducing State debt and encouraging private sector provision of infrastructure. The sales are designed to realise value, reduce risk and obviate the need to further fund the significant ongoing capital requirements of these businesses, where the private sector can fund those requirements.

This will go a long way toward reducing the current level of indebtedness of the State and demonstrate to ratings agencies and financial markets the Government's willingness to reduce debt and return the State to a solid fiscal position. Post the current forward estimates, when the worst of the global economic crisis has passed, the Queensland Government will reduce the capital program to levels under \$10 billion per year and look at further policy measures to improve revenue and reduce expenditure to assist in bringing the net financial liabilities to revenue ratio back within a range comparable to other larger states.

Further detail about the restructuring and disposal processes is provided in Chapter 5.

## PATH BACK TO SURPLUS

Returning the Budget to surplus is a key element of the Government's revised fiscal principles. A return to surplus depends on economic and population growth in the State as well as on the policy decisions of Government.

The revised fiscal principle relating to the General Government net operating balance requires the Government to achieve a General Government net operating surplus as soon as possible, but no later than 2015-16. While Chart 1.2 below notionally indicates a deficit position for Queensland until 2016-17 (a year after the Australian Government has forecast to return to surplus), it is expected that the significant program of asset sales, which are not factored into the forward estimates, will make a positive contribution to the General Government sector and will assist in meeting this fiscal principle.

There also remains a high degree of uncertainty about the pace and path of recovery. Queensland's assumptions are for continuing deterioration in the fiscal position for a number of years before recovery in the final years of the forward estimates. While it is possible that the economy and hence fiscal position will deteriorate more dramatically than indicated in the chart below, Queensland's revenue estimates are more conservative than those used by other Australian states. This provides Queensland with more upside should the turnaround occur earlier or more favourably than anticipated.

**Chart 1.2**  
**General Government Sector Net Operating Balance, 2005-06 to 2016-17**

