LEGISLATIVE ASSEMBLY FOR THE AUSTRALIAN CAPITAL TERRITORY

SELECT COMMITTEE ON ESTIMATES 2018-2019

(Reference: Appropriation Bill 2018-2019 and Appropriation (Office of the Legislative Assembly) Bill 2018-2019)

Members:

MR A WALL (Chair)
MS T CHEYNE (Deputy Chair)
MS C LE COUTEUR
MS E LEE
MS S ORR

TRANSCRIPT OF EVIDENCE

CANBERRA

MONDAY, 18 JUNE 2018

Secretary to the committee:
Mrs N Kosseck (Ph 620 50435)

By authority of the Legislative Assembly for the Australian Capital Territory

Submissions, answers to questions on notice and other documents, including requests for clarification of the transcript of evidence, relevant to this inquiry that have been authorised for publication by the committee may be obtained from the Legislative Assembly website.

APPEARANCES

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Amended 20 May 2013

The committee met at 9.30 am.

Appearances:

Barr, Mr Andrew, Chief Minister, Treasurer, Minister for Economic Development and Minister for Tourism and Major Events

Chief Minister, Treasury and Economic Development Directorate
Nicol, Mr David, Under Treasurer
Miners, Mr Stephen, Deputy Under Treasurer, Economic, Budget and Industrial Relations
Vroombout, Ms Susan, Executive Director, Economic and Financial Group
Salisbury, Mr Kim, Executive Director and ACT Commissioner, Revenue Management
Goth, Ms Kathy, Director, Economic and Financial Analysis
Holmes, Ms Lisa, Director, Financial Framework Management and Insurance, Economic and Financial Group
McAuliffe, Mr Patrick, Director, Asset Liability Management, Economic and Financial Group

Independent Competition and Regulatory Commission
Dimasi, Mr Joe, Senior Commissioner

THE CHAIR: Good morning. Welcome to the second day of public hearings for the Select Committee on Estimates. The inquiry today will look at expenditure proposals for the revenue estimates, particularly at Chief Minister, Treasury and Economic Development Directorate, and particularly focusing on budget statements B dealing with treasury matters.

I trust, since everyone has done this more than once, that you are familiar with the pink privilege statement in front of you and that you are aware of its implications. This year we are trying to avoid opening statements.

Mr Barr: I have always taken that to heart. I rarely give opening statements. Those of you who have followed this would be aware that I am one of the few who never do; so fire away with your questions.

THE CHAIR: Let us get to the fun part straightaway: the surplus. There is a surplus that you have announced for the 2018-19 budget in forward estimates on the general government sector headline net operating balance. What is the acronym that you typically use? Save me repeating it several times. Is it HNOB?

Mr Barr: HNOB—headline net operating balance, yes.

THE CHAIR: It is the standard accounting concept of the headline net operating balance plus the superannuation return. The GGS net operating balance shows a deficit of $147 million in 2018-19. How is this deficit paid for in the future years?

Mr Nicol: The budget does not specifically go to how various surpluses are used or deficits are made up in future years. The budget simply records, based on the various indicators that are used, the state of the budget.

THE CHAIR: Will the net operating deficit then contribute to net debt?

Mr Nicol: The way net debt is calculated is essentially that we derive—net debt is essentially a cash concept; so it is how much cash we need to fund our operations, whether they be infrastructure investments or recurrent spending. If that total cash outlay is higher than our cash receipts, we have to borrow the difference.

The headline net operating balance is an accrual concept. It takes into account non-cash items such as depreciation, which is a substantial cost on our operating statement, but it requires no cash to fund depreciation, because it is just a change in the value of an asset. In respect of the headline net operating balance in and of itself, you cannot just use that figure to determine how much debt will change. You have to look at what the underlying cash position is.

That is done in two ways. One is to look at the operating cash balance, which is in strong surplus, principally because that does not take into account depreciation. Then you look at what decisions the government has made in terms of essentially capital investments. It is more complex than this, but basically if you take the net operating cash balance and the infrastructure investment, that determines your cash needs for the year.

THE CHAIR: What impact has the change in the discount rate to the superannuation return adjustment had on the net operating?

Mr Miners: It is going to be better.

Mr Nicol: Yes, the change in the discount rate essentially only changes the valuation of our superannuation liability, so it has no direct effect on our debt in that sense. It does have an impact on our operating statement and our liabilities as they are measured.

Whilst we dig out those figures, I will detail a little how that works. Under the accounting standards, we are required to value our liabilities at the end of each year. Our biggest liability is our superannuation liability, which relates to payments to past and present employees in our defined benefit funds, which were closed in 2005. For every employee who has joined since then, their super costs are met as they are employed. Funds are actually paid into an accumulation scheme fund of choice.

For those who are in defined benefit schemes, however, we make a lot of assumptions about the future liability for those people in terms of, when they retire, whether they will get pensions or lump sums. We make forecasts about what those costs will be. The way that is done is that we calculate essentially a cash flow for about the next 70 years. That is how long we think the liabilities will last, 70 to 80 years. Then we have to discount those back to a single value. The way you discount cash flows back is to use an interest rate on 30 June.

The accounting standards require us to use an actual rate at 30 June each year. We have some flexibility to determine what that rate is, but it has to be a rate on a bond or debt instrument that is close to the length of time that we are looking at. We use the longest commonwealth dated bond we can to define that rate. Last year it was 3.2 per cent, from memory.

In forming a budget, we make forecasts. We have assumptions about what various components of the budget will be. Previously, we used the discount rate assumption of six per cent, which is a long-term average. In the last three or four years, interest rates have been very low. So that has led to essentially an increase in the value of the liability. A lower interest rate—

THE CHAIR: Lower return, more to pay.

Mr Nicol: leads to a higher discount rate. One way of thinking of it is that if you invest an equivalent sum at prevailing interest rates, what would you need to invest to pay out that liability? As interest rates change, that liability will change. It is only a measured estimate of the value of the liability. So our real liability, in a sense, is the actual cash flows that we are going to face. The value of it changes. It is important but it does not actually drive any need to raise extra debt et cetera.

THE CHAIR: What is the current bond rate for the longest available commonwealth bond?

Mr Barr: 3.3 per cent.

Mr Nicol: 3.3 per cent.

THE CHAIR: Given that this budget was handed down less than a month prior to when the 3.3 per cent rate needs to be used, why have you chosen to go with the five per cent rate, given that obviously the impact is that it makes your budget look better?

Mr Nicol: Yes, we use what the commonwealth use because they are the same schemes. They cut their rate from six to five; so we have done the same thing. It is an assumption. It is a transparent assumption. It is clear what the effect to the budget is going to be using different assumptions. The question is not only what rate you should use this year, but what rate should you use going forward as well. Forecasting interest rates is a notoriously difficult thing to do. The further out you get, the harder it gets.

We have advised the government to take this approach, as the commonwealth has done. It is to use a long-term rate and not to try to forecast what is going to happen to interest rates in the formulation of the budget for this liability. Once the actual rate is known on 30 June, we use that for the accounts and the actual impact is easier—

THE CHAIR: Certainly, if the long-term bond rate is at 3.3 per cent, that is ultimately the market's forecast of what the long-term view of interest rates is?

Mr Nicol: As at today.

Mr Barr: Not over 30 years, though.

THE CHAIR: Pardon?

Mr Barr: At today, not over 30 years, though.

Mr Nicol: Today; interest rates can change. I agree; I do not think they will change back to five by 30 June. But I do not know what—

THE CHAIR: The economy is in crisis if they do.

Mr Nicol: I do not think the Reserve Bank is going to meet between now and 30 June. So they are not going to make a decision between now and 30 June—

THE CHAIR: Thus the term “crisis”.

Mr Nicol: But if you look at the history of interest rates as well, the Reserve Bank tends—I am not predicting anything; I do not—to move in cycles. Interest rates can change and I am not bold enough to predict and forecast changes in interest rates. That is why we use the straight long-term average. I would recommend doing that, whether interest rates are below the long-term average or above the long-term average.

MS ORR: Chair, I had a supplementary?

THE CHAIR: I have a couple of further questions and then I will go to you, Ms Orr, for a supplementary.

Mr Nicol: Mr Miners has the answer to your original question, which was: what is the impact of going from six to five?

Mr Miners: The impact of moving from the six per cent to the five per cent discount rate in 2018-19 is around $24 million; around $21 million in 2019-20; $18 million in 2020-21; and $15 million in 2021-22. That is the increase in expenses. They are all increases in expenses.

THE CHAIR: Is the headline net operating balance included in the audited consolidated annual financial statements with regard to the superannuation?

Mr Nicol: The superannuation liability is audited. The headline net operating balance is not audited but it is derived—everything in the headline net operating balance is derived from something that is audited by financial, by the auditor.

THE CHAIR: Have there been any discussions then with the Auditor-General around the inclusion of the superannuation return adjustment?

Mr Nicol: I would have to take that on notice. I cannot recall having an explicit discussion with the auditor. Just to clarify your question, chair, what we do on the headline net operating balance is we include a normalised return, assumed long-term return, on our superannuation provision account investments. That is a different question to the discount rate, the question we have just been talking about.

THE CHAIR: Yes.

Mr Nicol: Part of the government's policy is that by 2030—this has been a longstanding policy—it will build a fund to essentially fully meet the liabilities under its superannuation defined benefit schemes. The target date is 2030. That has now amassed $3 billion-odd worth of investments. Those investments generate a return, which is technically a revenue to the budget.

In setting the government's main fiscal target, which is the headline net operating balance, what the government has agreed to do and, again, this is a longstanding decision; it is not a decision of the—I can take on notice when the decision was made to approach it this way, but it has been a longstanding approach. It is essentially to ensure that the main fiscal target is not affected by changes in financial markets and changes in the return on the fund.

We assume a normalised return from our investments, a standard return. If the fund for the last two or three years has earned between 1½ and two times what our target is, if that had just flowed into the main fiscal aggregate, that would have produced quite a big increase in revenues and, therefore, a reduction in the deficit or even an increase in surplus.

Similarly, if markets had a bad year, if you did not take this into account, the main fiscal aggregate would go into deficit because the market fell by 10 per cent or whatever happened. So we normalise it. We assume a return on our funds invested of CPI plus 4.75. That is the amount we use to get that estimate.

The Auditor-General audits our financial statements. She does not audit the budget statements per se. I think in Victoria the auditor-general signs off on the budget statements. They do not audit them but they sign off on them. In no other states, to my knowledge, do auditors sign off on the budget statements.

But the headline net operating balance represents the government's fiscal aggregate, fiscal target, the best measure of the underlying state of the budget that we can produce.

MS ORR: Mr Wall in his question referred to a surplus. Chief Minister, I have heard you talk a lot about a balanced budget. I want to get a better understanding of what you see as the difference between the two.

Mr Barr: Essentially, within a band of headline and operating balance results it sits largely, depending on the jurisdictional vagaries, somewhere between plus or minus one per cent of total revenues. So there is often an argument about whether plus $1 would constitute a surplus and minus $1 would constitute a deficit. Both would constitute a balanced budget in the context of a $6 billion budget.

We will have these arguments—they are largely political or media driven—around what constitutes a balanced budget or a surplus budget. We have determined as a fiscal policy to seek balance. That means from time to time the budget will be on the positive side of the ledger where revenues will exceed expenditure. On other occasions, expenditure will exceed revenues. But we would seek to maintain that within a fairly narrow band, all other things being equal.

There have been times in the territory's fiscal history when all other things have not been equal. For example, in 2014 the Mr Fluffy situation was not a normal course of events and required an extraordinary response. Equally, the last couple of years before the global financial crisis could be described as boom times for government budgets, and the territory ran a surplus of $300 million in 2007-08 which, adjusted for today's dollars, would be a significantly higher amount given the relative size of the budget.

There is a long-run history of the headline net operating balance this century in the budget papers. They show a range of outcomes from a surplus as high as $300 million and deficits at an equivalent level, particularly in 2014. But our objective has been to return to a more balanced outcome where revenues and expenditures are more closely aligned.

MS ORR: You say your objective has been to get to a balanced budget. Why do you see that as important at this time?

Mr Barr: In a more normal set of economic circumstances and prevailing conditions in the economy, the territory should only be seeking to raise as much revenue as is necessary to deliver the widest range of government services of any government in Australia. To do significantly more than that would require a specific purpose—either saving for a large-scale infrastructure project or paying off a previous debt, which the government is doing in relation to Mr Fluffy.

The purpose of running surplus budgets over the next period is to ensure that by 2024 we have paid off that Fluffy loan. That was an important commitment we made when we took the loan out in 2014—that is, we would pay it back over 10 years. It is appropriate for us to run modest surpluses over this period in order to ensure we achieve that outcome as well as maintain our ability to provide the day-to-day services this community needs and to also maintain an ongoing infrastructure program to meet the territory's growing population.

MS ORR: What does the surplus mean for that longer budget outlook?

Mr Barr: Our endeavours over the last three or four years have been, as I say, to return the budget to balance and to keep it in that situation. We have, of course, made some very significant provisions in this year's budget for future spending, particularly on infrastructure but also on the recurrent side. This year's budget presents a balanced outcome in terms of revenues and expenditures in the current fiscal year and across the forward estimates as well.

MS LEE: Going back to the delightful acronym of HNOB, that does not include the acquisition of non-financial assets, which I understand are about $208 million this year. How is this net spending financed?

Mr Nicol: Can you give me the reference to the page number?

MS LEE: Page 4 in budget paper 3. Do you want to take that on notice?

Mr Nicol: Yes, I will take it on notice. I think it depends on where they are from.

MR COE: Have a look at the harmonised financial statements on page 316, on the second-bottom line, of $208 million. Is this, in effect, the capital that you are referring to? The capital goods? The capital expenditure?

Mr Nicol: Let me take that on notice. It is derived from a number of businesses in the ACT government. For example, a lot of that will be the SLA. It will acquire and sell assets. As to how they are treated, I will come back with an explanation.

MS LEE: Thank you. And does spending on non-financial assets contribute to debt?

Mr Nicol: As I said our net debt requirements are based on our cash requirements. So if cash revenues in a particular year are less than the cash outlays that go out the door, then, yes, we have to borrow to make up that shortfall. A purchase of non-financial assets will usually involve a payment of cash; it depends on the financial asset and on which business undertakes that purchase as to how it feeds into the general government balance sheet.

I do not think I can answer it from a single number; I have to look at the detail of the particular elements that feed into that. But I will see what we can do in terms of taking that on notice.

MS CHEYNE: I want to talk about the ACT as a diversified economy. A lot has been said about job creation and that one in seven new jobs has been in tourism. However, in their reports both last year and this year Pegasus asserted that our reliance on the commonwealth has not changed. I want to get a sense of whether we are really diversifying, and if so, how?

Mr Barr: There is one important point to make from the outset in that you can be more diverse within the non-commonwealth government sources of economic growth. So if a statement of diversity is interpreted as solely between the commonwealth government and everything else, you could be very narrowly based if your economy was the commonwealth government and the tourism industry only, for example. Our economy is not that.

Yes, the commonwealth is the main anchor of economic activity in the ACT, but the diversity of all of the other contributors to the territory economy continues. That is an important distinction to make. When I talk about diversity I do not just mean between the commonwealth government and all other economic activity; I am talking about how we can diversify that other sector of contributions of economic activity.

Perhaps the best example of this in that context is to look at the share of gross state product for each sector. Public administration and safety makes up 26.1 per cent of the territory's gross state product. Health care and social assistance is now 10.6 per cent, so a little more than a third of the commonwealth contribution. That is growing partially as a result of the NDIS and the transition of activity out of the commonwealth into that sector but also as a result of demographic change and growing demand for health care and social assistance services.

We have seen professional, scientific and technical services grow to be now 10.3 per cent of the territory's gross state product. To put a dollar figure on that, that is just under $4 billion annually in professional, scientific and technical services. It was the fastest growing category for the territory economy. Education and training at a little over $2.1 billion annually accounts for around 5.6 per cent of the territory's gross state product. The construction sector at a little under $2.3 billion is around six per cent of the territory's gross state product.

But across arts and recreation, financial and insurance services, information, media and telecommunications, transport, postal and warehousing, accommodation and food services, retail trade, wholesale trade, and electricity, gas, water and waste services, we are seeing diversification within those sectors and they are growing. That is an important objective for the territory.

If our economy was too narrowly based and it was just public administration and just, say, higher education and tourism, we would be very much at risk of two major factor decisions taken in a budgetary context by the Australian government and effectively the value of the Australian dollar in terms of the competitiveness of those industries internationally.

We have lived through this in the mining boom, for example. When the Australian dollar was very high it meant that those service export industries were not as competitive. With the lowering of the Australian dollar and the transition in the Australian economy away from the resource-based states and more economic activity happening in the services sector in south-eastern Australia the ACT economy has certainly benefited from that transition in Australia's economic activity.

Given that 99 per cent of our territory's exports are in the service sector, one could argue we are leading Australia's transition towards being a more service export-oriented economy. The areas where we have seen quite significant growth have included higher education, which grew by 25 per cent in the last fiscal year; the tourism sector has also been experiencing record growth.

But, importantly, for building on the territory economy's strength around exporting of government services, a lot of companies that come to Canberra in order to secure both Australian government contracts and ACT government contracts are also getting the business of exporting their services to other governments around the region and around the world. The practical examples of that include defence-aligned and cybersecurity-aligned companies winning contracts with the US government, with the Singaporean government, in New Zealand and across the region.

We are seeing a more diverse territory economy, greater levels of service exports and a wider range of industries operating in the territory. Renewable energy is another example of diversification of the ACT economy. Where 10 years ago we did not have a particularly large renewable energy industry, we are now growing that industry as a result of government policy that has supported that activity. It has achieved a certain policy goal in the territory but is also seeing an export focus internationally. We are also seeing activity from ACT-based companies in the Australian market in renewable energy, which is terrific.

That is a snapshot. For people who are more interested in the fine breakdown of every element of the territory's gross state product, that data is available on the treasury website. It is an annual snapshot. The most recent data is to June 2017. That will be updated in the coming months to give the outcome for the current fiscal year, once it is concluded. It is pleasing to see that those industries are growing and that the territory can offer more in terms of economic activity than just simply decisions of the Australian government.

MS CHEYNE: It is not going to change that the commonwealth is a major contributor to our economy, but having a greater mix of other sectors in our non-commonwealth side of things means we can weather external factors much better?

Mr Barr: Yes, indeed. We have almost zero control over what the commonwealth government does—almost zero. Through our friends and colleagues who represent the territory and through those who represent other states and territories but might have a certain fondness for the national capital, we may be able to influence some policy decisions of the Australian government, but by and large that is something that is beyond our control.

What we can seek to influence is the diversity of the balance of the territory economy, and we can seek through our own policy settings to encourage its growth and its diversity. That has been the focus of economic development policy for some time. That is a very simple proposition, particularly for the service export sector. That sector of the economy is bringing in money and wealth into our community and is creating good, long-term and sustainable jobs that are not reliant on decisions of the federal government. That is a good thing in the long term for the ACT.

MS CHEYNE: What are the sectors over the forward estimates that we want to grow, particularly those ones that are not reliant on commonwealth government decisions? Which ones are we putting a focus on?

Mr Barr: We have had a particular focus on the top five export earners for the territory. There are areas and opportunities for us to support the growth of those sectors. That includes higher education, government services, tourism, and professional, scientific and technical services. Each of those sectors has an opportunity to export. We support that through the economic development directorate. Obviously, we will have an opportunity to explore those programs and activities on Friday of this week, so I will park that one as an issue the committee can come back to and discuss in more detail.

The fact that our service export growth has been stronger than the Australian average over this decade and that the value of those exports has doubled is a pretty good indication of the right policy settings being in place, aided no doubt by the Australian dollar depreciating in value. The competitiveness of a number of those trade-exposed sectors has been improved as a result of that. Should the Australian dollar fall a little further—the indications are it probably will—that will only further enhance the competitiveness of those sectors. If we continue to see the current levels of growth, that will, in turn, contribute more to the ACT economy over the years ahead.

THE CHAIR: Treasurer, your explanation of what diversification looks like is clearly a change from what has typically been your argument—

Mr Barr: No, I do not think it is.

THE CHAIR: Largely, for the last two budgets, the statements have clearly said that diversification in the ACT economy was to achieve some independence from the influence of the commonwealth policy.

Mr Barr: This is exactly what I have outlined.

THE CHAIR: So whether, in the ACT economy other than commonwealth services, that 49 per cent is made up of just tourism or a thousand other industries, proportionally the commonwealth still plays the same part in the ACT economy and we are still just as susceptible to any change in commonwealth policy as we were five years ago.

Mr Barr: Well, no, because the commonwealth—

THE CHAIR: If 49 per cent of the economy is made up of either just tourism or if it is higher education, tourism, manufacturing, research and all the other services, 51 per cent of it is still ACT and commonwealth—

Mr Barr: Yes, but then you have to look at what are the capacities for those sectors to grow in the absence of growth at the commonwealth level. In the end, if we want a larger economy, we would need all parts of our economy growing.

THE CHAIR: Yes.

Mr Barr: That is accepted. Can we agree on that?

THE CHAIR: You just need a portion of that to grow and nothing to shrink.

Mr Barr: Yes, sure. The commonwealth have from time to time been in the business of shrinking.

THE CHAIR: Correct.

Mr Barr: Yes, okay. If they are not doing that—if they are just steady—then in order for our economy to grow, we need all of those other sectors to contribute to growth.

THE CHAIR: At least one of those other sectors to grow, yes.

Mr Barr: Sure, but given their relative size, if you assume everything else is constant and then only one sector growing would contribute to the total growth, yes, that is a hypothetical scenario that is unlikely to ever occur—

THE CHAIR: You are trying to break this down to a simplistic level, so—

Mr Barr: You will see a multitude of different elements of economic growth across the economy. Where we have the capacity to influence that, that would be the value of an economic development policy, would it not?

THE CHAIR: Yes, it would, but—

Mr Barr: Yes, it would. Okay, thank you.

THE CHAIR: But you have failed so far to increase the proportion of the economy that is not commonwealth dependent.

Mr Barr: That has not been a policy objective. The policy objective has been to grow the rest of the economy. I cannot control what the federal government does.

THE CHAIR: No, as I was saying, but the other portion has a—

Mr Barr: To take your argument to its logical conclusion, I would be an outstanding success if the commonwealth government halved its economic activity in the territory. Then the rest of the economy would be a greater share. But that would mean a smaller economy overall.

THE CHAIR: Yes, but the policy objective by you as Treasurer and Chief Minister several years ago was to increase the private sector portion of the economy compared to that of the commonwealth.

Mr Barr: No, it was to increase the private sector's contribution. I cannot influence the proportionality. That is determined by what happens in the commonwealth, which I do not control. But what I can seek to do, as economic development minister, is ensure that those areas of the economy where we have some influence are growing and we have in place the policies to support that. If the contribution of the commonwealth grew from $30 billion annually to $60 billion annually—

THE CHAIR: No, but your economic settings could grow the—

Mr Barr: we would have an economy that is $30 billion larger and, if the rest of the economy only grew by $15 billion, the commonwealth share would be greater but it would be a greater share of a bigger pie. In the end we cannot control that.

THE CHAIR: No, but the portion you can control is not growing at a rate faster than what the commonwealth is.

Mr Barr: Some elements of it are, obviously, as I have just outlined.

THE CHAIR: As a whole.

Mr Barr: I do not think the commonwealth grew by 24 per cent last financial year. The higher education sector did, in terms of its service—

THE CHAIR: Yes, but other sectors locally have shrunk and the average remains the same.

Mr Barr: No, they have not; they have grown. Other sectors of the economy have grown as well or else our economy would not have grown. Our economy is growing faster than that of any other state or territory at 4.6 per cent.

MS ORR: By getting growth in the non-commonwealth portions of the economy, how are we smoothing out any changes, particularly in the short-term of the ACT economy, that the commonwealth might make that would impact on us?

Mr Barr: We have limited capacity to do that, given the relative size. The ACT government is about 10 per cent of the total territory economic base. Where we can do that we have in recent times. That has been through running deficits to support the economy during those difficult periods. If we did not provide that injection of cash from the territory government into the economy there would be no other cash there. The economy would be commensurately smaller by whatever size of budget deficit we were operating during that period.

We are now in the period of more benign commonwealth policy settings. As I have observed over the last few budgets, they are not necessarily pouring huge amounts of additional money into the territory economy, but they have stopped cutting. In the absence of commonwealth cuts and just largely status quo from the commonwealth, we have seen these other sectors of the territory economy grow very strongly, all of which has fed into a growth in the territory's gross state product in the 2016-17 fiscal year of 4.6 per cent, which is higher than those of Victoria and New South Wales, and well above the territory's long-run average.

That is an encouraging sign, given that the commonwealth and the public sector were not significant contributors to that growth. That growth came in professional, scientific and technical services; it came in education; it came in a number of other sectors—a diverse range of sectors, dare I say, that have all contributed to the territory being the fastest growing economy in this nation. That surely is a good thing.

It would come as a surprise to many in the business sector that we would spend a huge amount of our time this morning bickering over which sectors have contributed the most. A growing economy is a good thing, I would have thought, particularly an economy growing as strongly as the territory's economy is now. That growth is broad based and that is a good thing for our community. Ultimately, I would have thought it was a shared objective in terms of public policy across all parties in this chamber.

THE CHAIR: I do not think there is any question about the commitment to seeing a diversified economy in the ACT, but clearly there is still some conjecture as to how you define and interpret that.

Mr Barr: Sure. Page 12 of budget paper No 3 outlines the public and private share of ACT state final demand. It shows the ACT government contribution, the Australian government contribution, and private expenditure, going back over the last six years. I draw the committee's attention to that table.

MS LE COUTEUR: I will move to a totally different subject: supplementary budget paper "Socio-economic analysis on taxation and concession policy". Remember, Alistair, you had a motion about rates? We amended it to ask for better analysis of the impact of rates changes. There are many examples of different households here.

The first thing to note is that the share of rates in their income ranges from 1.96 per cent for a Phillip couple up to 14.12 per cent for the Garran single pensioner. The interesting thing here is the difference between the rate concessions, utility concessions and vehicle concessions for everybody. This year the utilities concession is going up and the rates are staying fixed. Can you explain why we are putting more money into utilities and less into rates?

Mr Barr: Yes, utilities are a higher household bill than rates. They are growing faster at the moment.

MS LE COUTEUR: Is that the only reason? I thought the answer might possibly reflect the fact that not all households pay rates.

Mr Barr: That is also true.

MS LE COUTEUR: Is that relevant in your working out where to spend money on concessions?

Mr Barr: Yes.

MS LE COUTEUR: I note also that we have varying amounts for vehicle concessions and for public transport concession. Again, is the impact on different households, as well as the amount, looked at in these concessions?

Mr Barr: Yes.

MS LE COUTEUR: Will you consider extending the current public transport concessions, which are currently on their second one-year trial, to move out of trial phase into a commitment?

Mr Barr: Yes, we are certainly looking at that question. We have not yet resolved an outcome, but we are very happy to look at it, yes.

MS LE COUTEUR: Thank you. That is probably all I can get out of that one. It would be nice to have a real spreadsheet; that is my final comment on this question.

Mr Barr: It would be nice.

MS LE COUTEUR: A real spreadsheet, as opposed to a PDF, so that we can play with it as well. You guys have all the fun!

Mr Nicol: We can make that available.

Mr Barr: Sure. I do not think that is a major drama; yes.

MS LEE: I am looking at appendix H on page 399 of paper 3. It shows the key aggregates history. If you look at that table, what you see is the territory having moved from negative net debt until about 2011-12 into increasing net debt. It will move from an estimated net debt of $1.4 billion in 2017-18 to $2.1 billion in 2018-19 and then $2.6 billion in 2019-20. The question is: how can the territory be in surplus, leaving aside the discussion we have had about whether it is valid as a surplus, when net debt keeps rising?

Mr Barr: That reflects the territory's infrastructure program. We are borrowing for infrastructure.

MS LEE: Is the government's preferred definition of surplus meaningful if our net debt is continuing to rise in such large amounts?

Mr Barr: Absolutely, yes, because there is a difference between measuring our day-to-day activities versus our long-term infrastructure measures. If you wanted to, you could just use the pure cash, which is a surplus over the four years of about $2.1 billion, in terms of cash. But then we do have to depreciate assets and, of course, we do need to invest in infrastructure.

We are borrowing for some infrastructure investments. The rationale for that is, firstly, that it is very affordable to be in the market to borrow at the moment. Also, there are intergenerational equity questions. I do not think it is reasonable to ask one current generation, for example, over a single-year budget or even over a four-year budget estimates period to pay for infrastructure that will be in place for 20, 50 or 100 years. Examples of infrastructure that we have borrowed for are as diverse as a dam through to transport infrastructure, to building new hospitals, schools and road infrastructure.

There is a range. You can see the detail in the forward capital program. We have also, of course, borrowed $1 billion for the Mr Fluffy loan. That is a big part of the territory's net debt. We have an obligation to pay that off, as I mentioned in my earlier remarks, by 2024. That will be clearly a focus for future budget years. Do you want to add anything to that?

Mr Nicol: I only say that a budget is typically made up of a number of financial indicators. They measure things like debt, things like your operating balance, things like your liquidity. All of these are important to give a picture of the financial state of the budget. As the Treasurer said, that increase in net debt is driven by the government's infrastructure program. That is creating more assets for the balance sheet. So the debt there is matched by an increase in asset values.

Mr Barr: The good household analogy here is that we are renovating the territory's home. We are making it bigger and we are borrowing to undertake some of that activity. Previously, territory governments have funded infrastructure almost entirely off asset sales.

MS LEE: On Friday we saw an article in the paper—also the MBA gave some evidence about their concerns—about only 41 per cent of the capital expenditure having been spent on infrastructure. They called for a long-term infrastructure plan. What do you have to say to that?

Mr Barr: Yes, that 41 per cent figure, I think, related to the end of the March quarter of the current year. It will grow more over the balance of this fiscal year.

MS LEE: Sure.

Mr Barr: But, yes, the territory—

MS LEE: But I think the point was that it has not been spent. That is what they were concerned about.

Mr Barr: Indeed, yes, we have encountered some difficulties with some projects. So you do see a re-profiling of the infrastructure spend. I guess the basis for this has been capacity and supply side constraints in some projects. Others have had difficulty associated with planning approvals, weather or other events that have delayed their completion.

In some instances there is a distinction between physical completion of works and financial completion, which can lag by a quarter. This can mean that there will be physical completion in a fiscal year but fiscal completion in the following financial year. It is important to look at the capital works program as a rolling program.

But $750 million is around the cap for industry capacity in the territory at the moment. There are a couple of PPPs that are sitting on top of that that take that figure up closer to $1 billion annually. But that is around the supply side constraint that we have.

The other factors that are impacting on the territory's capacity in certain sectors of capital works relate to projects and programs underway in other states and territories. For example, as we are witnessing a very significant infrastructure program in Victoria and in New South Wales, our ability to import labour from those two jurisdictions in order to undertake projects in the ACT is severely limited because they are already engaged on projects in their home jurisdictions.

There is a capacity constraint within the territory economy. Hence we have shaped our forward infrastructure program to reflect that capacity constraint.

MS LEE: Does the government have plans to address the capacity issue to grow our local workforce?

Mr Barr: Yes, and that is clearly part of the agreement we have—

MS LEE: Is that reflected in the fact that CIT is going to have a reduction of 18 full-time staff?

Mr Barr: No, but they would be in areas not related to capital works. Obviously, the pipeline around skilled tradespeople in certain areas is a national challenge. Nevertheless the data I have seen shows that we have actually had some very high levels of completion of those trades in the ACT relative to other jurisdictions and we are seeing interest and demand in some of those sectors for growth.

But let us be clear that the pipeline to change this is a long-term one. We have signed a national partnership with the commonwealth in relation to skills. That does provide some additional resources to the territory in order to address some of these skill shortages. This will be an ongoing issue, not just for the ACT but for all states and territories.

I think it will be useful to get this data. You will see in the budget papers of New South Wales and Victoria that their programs are, by historic levels, extraordinary. This is the biggest infrastructure boom we have seen in this country for some time, driven by state and territory governments in large part. The commonwealth are also providing some additional resources, largely through equity into certain projects, but that is a whole other discussion.

Our expectation over the next few years is that it will continue to be difficult to attract labour into the territory from New South Wales and Victoria, and now even Queensland, given their state budget released last week. It has a series of very large infrastructure projects.

It is a hot market for big infrastructure in Australia at the moment. For long-suffering Australians who have felt a bit of an infrastructure deficit in recent times, it will be a good thing for the functioning of our cities and our economy. But it is a challenging period at the moment to be in the marketplace.

MS LEE: One of the other factors that you spoke about was planning approvals. Do you have any plans or initiatives in the pipeline to try and address this from that perspective?

Mr Barr: Yes, in terms of how we structure our own infrastructure program—it is relatively new; it has been in place for the last few years in terms of mapping out government infrastructure projects—the planning system is robust, if not always to the pleasure of proponents of particular projects—

MS LEE: I think that is pretty obvious.

Mr Barr: be they government projects or private sector sponsored projects. I do not think people should have any assumption that their projects will automatically be approved through the planning system. If you had that assumption, you would be naive. That reflects a balanced planning system.

Not every project, be it sponsored by the government or sponsored privately, will make its way through the planning system as quickly as every proponent would like. There would often be good reason for that because issues will be raised by stakeholders or by the community in relation to particular projects. That will be what it will be. Some projects are more controversial than others, undoubtedly, and that will always be the case.

MS LEE: I will not ask any questions about what you are going to do about the weather.

MS ORR: I have a supplementary. We were talking quite a lot there about the capital investment as part of the budget. What is the commonwealth's contribution to that in the wider context of the whole contribution? What is ACT doing and what is the commonwealth doing?

Mr Barr: The commonwealth has in its budget provided, I think, $40 million over the forward estimates period and a further $60 million outside the forward estimates period for Monaro Highway improvements. They required that the territory government match that contribution in order for it to go ahead; so we have done so.

They have also provided some funding, as I understand, for some of their own owned assets inside the territory. The National Gallery is an example there. I think they have about $12 million in their budget papers. They do provide some funding to the National Capital Authority to undertake largely repairs and maintenance rather than necessarily new asset building.

I will have to take on notice any other elements of directly funded commonwealth infrastructure. There is a small amount of local government grants and from memory there is a black spot road program that might be $1 million or so.

MS ORR: If you look at the infrastructure need as a whole, it is not a huge contribution?

Mr Barr: No. Black spots is about $1.43 million. They have contributed funding towards, I think, the roads to recovery program, which in 2018-19 is $1.4 million. There is $1.2 million as part of the bridges renewal program, and then there is funding from previous years continuing around water. We have had a partnership with the commonwealth around improving urban water. We have jointly funded some projects there. The details of this are in the federal relations chapter of BP3.

MS ORR: Just to clarify, within the whole infrastructure task, it is quite a small proportion.

Mr Barr: Yes, that is right.

MS ORR: A lot of it sounds like it is required for us to match it. It is conditional on our matching it.

Mr Barr: Generally speaking, yes, the commonwealth's approach to infrastructure funding has been to require matched funding from state and territory governments. I guess, relative to other jurisdictions, their investment inside the territory is not a significant part of our total infrastructure program, although you welcome every dollar as it contributes to improving the territory's infrastructure base.

THE CHAIR: What is the Monaro Highway funding going to be put towards?

Mr Barr: It is a very good question. The commonwealth did not have a particularly clear sense of it in terms of their announcement. They have written to us. We have written back agreeing and outlining that we have matched the funding. We will discuss how it can best be utilised, but that is probably something you can take up with the transport—

THE CHAIR: What is it that the territory would want to see, given that there is no certainty around what specific aspect of this 20-odd kilometres of road—

Mr Barr: I suggest that is probably best pursued with the transport minister as they will be dealing with the detail of that particular project going forward.

MR COE: Treasurer, you mentioned the 41 per cent until the beginning of this quarter, and that is likely to change in this quarter. What is actually going to change in this three-month period that is going to bump that up as a percentage, not just in dollar terms?

Mr Barr: That 41 per cent is 41 per cent of the year's program. For every extra dollar we spend beyond March, that will increase its percentage towards a maximum of 100. I do not think it is going to get to 100—I think the budget papers have been quite clear about a rollover into the next fiscal year—but every dollar that is spent in the final quarter—

MR COE: Sure.

Mr Barr: which traditionally has been the biggest spending quarter, partly because any new works cannot commence or go to market till the budget is passed, which is not until August. So the timing of our fiscal year and the timing of the budget do impact on the first quarter for any new works. It does not impact on ongoing works, which are the larger part of the territory's infrastructure program.

MR COE: In light of that, what has changed this year as opposed to previous years that has made this capital works program unachievable?

Mr Barr: I do not think there is much that has changed. We have not always hit our target each year.

MR COE: The rollovers are significant every year.

Mr Nicol: There are several reasons. I think the main difference this year is the tightness of the infrastructure market on the east coast of Australia, which added to delays. The other thing I would say is that with our system of appropriations, which we all know and respect, obviously, you appropriate a maximum amount. For each project, you cannot spend more than you appropriate. By and large, every project is going to spend up to 100 per cent, so every project is likely to be a little bit under with every delay: a weather event, planning delay or whatever. That is effectively built into the system.

My observation is that the projects spend to budget, by and large, in our infrastructure program; it is just that some of the time lines stretch out longer than we would initially like. The main difference this year, if there is a difference, I think, is the tightness of the supply market, starting to tighten up both labour and materials. Can I give you an example?

MR COE: Yes, but could you also, in that example, advise how you factored that into next year's program?

Mr Nicol: Yes. For example, we have come across instances where we might have certain building supplies ready to be delivered on a certain date to a project, but New South Wales comes along and buys 10 times as much and the factory bumps our order and supplies to New South Wales because they are a bigger contractor. That is one example of what we have seen.

MR COE: What projects have been affected by this?

Mr Nicol: That was a risk on the Manuka media centre. We were getting supplied with some concrete slabs from a factory. They phoned us up and said, "You are going to be delayed because New South Wales has come in." We went and negotiated with them and did a lot of arm-twisting, and I think we minimised the delay, but that is an example of what happens when the market is tight on the supply side.

In terms of what we have done, at an aggregate level we include a provision for an underspend, because we know that in aggregate we are not going to get the entire program out in the current financial year. We are not quite sure which project is going to be delayed by supply problems, planning issues or whatever, but we know that in aggregate we are going to be delayed.

The other thing we did this year, instead of rolling over a lot of the money from 2017-18 to 2018-19, was to roll it over to 2019-20. We do not want to create a bigger underspend problem for the current financial year. And generally, we know that if a project is delayed, it is very difficult to catch up.

Mr Barr: I think it is important in this to distinguish between physical completion and financial completion of projects. Projects are always physically complete before they are financially complete. The invoicing, paperwork et cetera will often extend at least a quarter after the physical completion, sometimes longer.

As we have a hard fiscal year reporting requirement, if a project is complete on 30 June it is in this fiscal year but if it is 1 July—there is one day difference—it is in the next fiscal year. That is a reality in terms of reporting. It can often be that financial completion is not achieved until some time after the physical works. And there will be warranty periods and defect periods for particular projects where money will be held back until certain remediation works are undertaken.

There are a variety of reasons why there is a gap between physical completion and financial completion.

THE CHAIR: Retention of funds would not normally contribute to that delay, though. That is factored in, isn't it?

Mr Nicol: It depends on what the cause of the difference is. For example, UCPH is complete, but we still rolled over funds from this year to next year to make sure we covered off any rectification works that may or may not be needed. A lot of that can happen as well.

Mr Barr: If they are not needed, the project comes in under budget.

Mr Nicol: It is under budget.

Mr Barr: Then you have all this money that is returned to the capital program, to the budget. And that does happen, too.

Mr Nicol: It does, yes.

Mr Barr: The media never report on that, of course. It is only the over-budget projects that are ever reported on.

MR COE: But in terms of financing, if you had planned to spend 100 per cent by 30 June, even if it was ambitious or it is just a reality that 100 per cent is never spent, what does that mean in terms of how you actually finance these? Have you, in effect, over-borrowed, or at least borrowed prematurely?

Mr Barr: Indeed. That is an excellent point, and one that we discuss regularly. That is why we have delayed borrowings many times in the territory. The territory's cash position has been so strong in recent times that we have not had to borrow in certain fiscal years when we planned to. That is why you see the net debt levels lower than were anticipated, if you go back and track year on year, because we have not had to go into the market to borrow.

MR COE: Or it has just happened six months later or 12 months later?

Mr Barr: Indeed, yes. Yes, that is right.

Mr Nicol: When we undertake a borrowing—a real borrowing rather than a forecast borrowing—we essentially monitor how much cash we have and do short-term cash forecasting. We have a target cash balance that we like to keep. As I said before, liquidity is an important measure of the solvency of any body, and one of my number one jobs is to make sure we have enough cash in the bank to meet our day-to-day needs.

MS LEE: That is pretty important.

Mr Nicol: Very important. Budgets are important, but that is also important. In one sense, often the cash drawdown is our first indication of our real activity levels, because we know before the project manager comes and tells us that we need to roll over some funds.

MR COE: Sure, but what percentage of the infrastructure spend do you think you are going to get to by 30 June, roughly?

Mr Nicol: I would have to take that one on notice.

MR COE: And what are the totals?

Mr Barr: I will know in about two weeks.

MR COE: Funnily enough. What is the total value of that program?

Mr Barr: It will be in the budget papers.

MR COE: Yes, that is right.

Mr Barr: We will fish it out for you.

MR COE: Yes, but we are going to be talking, are we not, of perhaps $100 million or $200 million that was expected to be spent that presumably you borrowed for?

Mr Nicol: Yes.

MR COE: That presumably you have borrowed for.

Mr Nicol: No, we will not have borrowed for it if our cash balance is sufficient.

MR COE: Has it therefore been held back from being invested?

Mr Barr: No.

MR COE: If you have not borrowed for it, and in effect you have the cash available—

Mr Barr: It would sit in the territory bank account.

MR COE: Yes, in the territory bank account. Could that not have been put into a short-term investment?

Mr Nicol: We do manage the territory bank account in short-term investments.

MR COE: Or even a medium-term investment?

Mr Nicol: Our objective is to try and keep the cash balance to a level that is sufficient to meet our forecast needs but not higher than we need. At the moment, as has been noted, in the borrowing situation, we are borrowing when we need more cash. Our borrowing rates are very competitive, so the cost of that is not high in terms of whether you borrow this month or next month. But by and large we keep our short-term cash at call so that when we need it we can call on it.

MR COE: I guess that is the point. If you have $100 million or $200 million that is at call that does not need to be, does that not in effect mean that there is forgone revenue?

Mr Nicol: I can ask Mr McAuliffe to come up. We try to keep a couple of months worth of cash, which, in a $6 billion a year budget, is closer to $400 million, to my recollection. We have a very good competitive rate from our bank, so it is not wasted. On that cash management side, I would prefer to defer borrowings than use that vehicle as an investment vehicle. We use the superannuation provision account as our medium-term/long-term investment vehicle. Mr McAuliffe, you might want to add some detail.

Mr McAuliffe: What Mr Nicol has said is pretty much right. The money does not just sit getting an overnight cash rate in the bank. We do have some external investment facilities that we utilise for that short to medium-term management as well as a very good rate with our current transactional banker which is above market rates at the moment. They are the decisions that we take up when we have that cash sitting around.

MR COE: But if you are still planning 100 per cent of the expenditure to happen by 30 June, surely that means there has to be an impact on either the borrowings or the investments?

Mr Nicol: No; we do not expect to spend 100 per cent of the program this year.

MR COE: Do you actually budget for it?

Mr Nicol: We budget for it, but—

MR COE: Otherwise what is the purpose of the document?

Mr Nicol: We budget for it, but we only borrow when our cash needs are necessary, when we need to borrow. We do that at an aggregate level; we do not do that at a project level. We monitor our cash drawdowns by our directorates for all purposes. We monitor our cash at bank. We know when our bonds are going to have to be renewed in the future, so we have to borrow for that. We keep a close look at the markets, because we do not want to be forced to go into borrowing in a market situation that is not ideal. There are certain times of the year that you do not go to the markets; at other times you do. We really borrow on our expected needs, and that is based on the cash in the bank in the short term.

We do budget for what is in the budget, in terms of spending. I should note, however, that we have a provision in the spending that in each budget we will underspend on capital. That is included; the calculation of our cash needs is derived based on that. We can get you the reference. Stephen, could you look up the reference to that page?

Mr Miners: The borrowing pages?

Mr Nicol: No. It is in our infrastructure spending.

Mr Miners: Yes, it is.

Mr Nicol: That is on page 202, table 5.2.1, the capital delivery provision there. We have assumed that even in 2018-19 we will underspend our capital provision by $148 million in aggregate, and our expected future borrowings are adjusted accordingly. But in relation to our actual borrowings, when you come around to it, we will only borrow when we need to borrow; we will not borrow if we have sufficient cash in the bank to meet all forecast expenses and cash needs for the next—

Mr McAuliffe: I think the reflection of what has happened with that re-profiling this year is shown in the 2018-19 borrowing numbers, where there are no new general government sector borrowings estimated to be required through the whole year.

Mr Nicol: I think in the last budget we forecast that we would have a $500 million—

Mr McAuliffe: Yes; I think it was something like that.

Mr Nicol: That has essentially been deferred for probably six months into the next financial year. That is how we manage our cash needs and link those cash needs to the budget.

MS ORR: Chief Minister, the first line of section 4.1 of budget paper 3 on page 183 states that the government's decisions about how the ACT budget is allocated sent a clear signal on our priorities and values. Can you elaborate on what is meant by that statement?

Mr Barr: The new spending initiatives are outlined in BP3 and they focus on health and education as well as our municipal service commitments around suburban services and transport. So around one in every $3 the territory invests on behalf of the community is invested in health care and one in every $4 is invested in education. Those two areas constitute more than half of annual expenditure in the territory.

On page 186 of BP3 we outline the estimated expense by function across general public services, public order and safety, economic affairs, environmental protection, housing and community amenities, health, recreation and culture, education, social protection, and transport. We report against those categories to be nationally consistent with various ABS reporting categories.

Mr Nicol: Yes, and they have changed substantially.

Mr Barr: Hence this new presentation and format for BP3.

MS ORR: What are the changes for?

Mr Miners: Basically, they have redone it right from the top, so all the major categories have moved around. In some cases it has meant breaking out some and in some cases it has meant collapsing them together. It is probably the most significant change to these classifications I have seen in my working time. So even the headings have changed in their titles. We can provide some more detail on that, if you like, but it has basically been rewritten to try and bring it more up to date. It has been a work in progress that has been going on for a couple of years to try and get them embedded, and this is the first time we have done it.

Mr Barr: In setting the budget revenue targets we have looked at what are the expenditure needs across a growing community and at our infrastructure program, our forward debt profile and our current spending needs and then looked to raise revenue that would balance with that. That is what we have achieved. The underlying principles behind this year's budget and indeed future budgets are to minimise the level of revenue necessary to meet the growing needs of the community.

There are, of course, alternative approaches to budgeting. You can seek to raise a whole lot less revenue, continue expenditure at a certain level and run large deficits. Equally, you can seek to reduce both revenue and expenditure and offer fewer services. Those options are available to the government of the day. It perhaps would come as no surprise to the committee that we have determined as a government that we would seek to meet the growing demand for health, education, transport, community services and local government services and through the various revenue lines ensure that those services were properly funded, have an infrastructure program that meets the needs of a growing city, and that is outlined in this budget, and run a balanced budget, leaving a small margin for any adverse economic circumstances that might arise, and hence a balanced budgeting approach.

MR STEEL: Going back to the discussion about the major sector contributors to economic growth, particularly tourism, one of the government and tourism sector's stated targets is to have $2.5 billion of overnight visitor expenditure every year. Are we on track to meet that target?

Mr Barr: Yes. We are a little under $2.2 billion at the moment. So on current trends we will reach that $2.5 billion by 2020 target. That was part of a national tourism sector approach agreed by all governments. I think Martin Ferguson was the tourism minister at the time who put that stretch target in front of the Australian tourism sector, tourism industry partners and state and territory government partners. We all signed up for what we thought at the time was a quite ambitious goal, and we have been performing very well against those targets, which is pleasing to see.

You highlighted the headline figure, but within achieving that are a range of other important metrics on the supply side, like increasing the number of hotel rooms, increasing the number of seats in the aviation sector into the marketplace. Singapore Airlines and Qatar Airways have between them got us there on their own, without adding in Tiger and other services that continue to expand. I think we are actually at our 2020 level now on aviation in 2018, with room for some more growth over the next 24 months.

We continue to want to invest in transport infrastructure to make it easier to move around Canberra, but we have also had a strong transport focus on making it cheaper and easier to get to and from Canberra both domestically and internationally. That undoubtedly is one of the supply-side factors that will support further growth in Canberra's tourism sector. I am sure we will discuss that in more detail on Friday.

MR STEEL: Will there be any more airlines coming soon?

Mr Barr: I have publicly indicated that I have continued to meet with both domestic and international airlines. In recent times that has included Jetstar and Tiger. I will meet with Virgin in Sydney next week. There have been some pretty significant changes in trans-Tasman alliances in the aviation sector. Virgin have been a strong partner for Canberra tourism over an extended period, and we certainly look to continue to work with them.

Following completion of the estimates period I will undertake my annual Asian investment tour, which has both a government bonds element and an economic and industry development element. I have secured a meeting with Hong Kong Airlines in Hong Kong in July, and we will begin some discussions with them. We have previously met with China Southern Airlines and China Eastern Airlines. China is the number one inbound tourism market for the ACT, so as a medium-term proposition, having a direct connection to China will help grow the tourism sector.

MR STEEL: Is it too early to measure the impact of the *Lonely Planet* accolade?

Mr Barr: It possibly is, although our friends at VisitCanberra may be able to give some more data on that—for the first quarter of the year, anyway—at estimates on Friday.

MR STEEL: And the impact of major events on the tourism sector?

Mr Barr: Yes, equally important. We have seen pretty strong numbers for both government and non-government events for the city. I do not have them in front of me today, but certainly we can explore that in more detail on Friday.

MS ORR: Are you open to taking requests for which airlines we would like in Canberra?

Mr Barr: I am happy to take any suggestions. There is certainly no harm in meeting with the airlines. In many instances the opportunities Canberra presents are not that well known for some of the international airlines. They are genuinely surprised at the core metrics of our market. But we also need to be realistic about the number of international carriers our city can support. The structure of international aviation agreements puts caps on the number of flights into the major Australian airports, and a way to enhance Australian services for a number of these international airlines is to also fly to a non-capped airport.

MS ORR: We are a non-capped airport?

Mr Barr: We are a non-capped airport, so the opportunity to have link or loop services with Sydney, given the proximity of the airports, is economically viable for airlines. It allows them to get an extra Sydney service at times, subject to the vagaries of slot allocation at Sydney airport, while also servicing the Canberra market. That is clearly the case with Qatar, but it could also be an opportunity together with a trans-Tasman link. The original Singapore Airlines connection was to serve both the New Zealand and Australian markets. The international agreements allow international airlines to carry passengers to and from, so that is another option to explore.

MS ORR: You mentioned China in the medium term as a possible market. Has anything been done on America?

Mr Barr: Yes. Qantas is the most likely partner there with American Airlines. There are some regulatory issues in relation to what level of co-sharing or revenue-sharing those entities are allowed to undertake, but an American Airlines-Qantas partnership hubbing through Auckland on to North America is a medium-term proposition. Canberra-Auckland could be serviced by a narrow-body aircraft then linking into a larger aircraft at Auckland.

Air New Zealand would be another potential airline in that regard, as their stated policy for the Australian market is to try and attract more Australians to fly deeper into North America by doing a smaller first step to Auckland and then being able to fly closer to the east coast rather than the traditional method by which Australians have dispersed through the US, which has either been through Los Angeles or Dallas-Fort Worth.

THE CHAIR: There has been a very public stoush between Canberra Airport and Qantas. What impact is that having on any prospective airlines coming to Canberra?

Mr Barr: It is difficult to assess in terms of other airlines, as it would be—

THE CHAIR: Do you hold a concern that it will potentially make selling Canberra to other airlines slightly harder given the reputational damage that may occur if they end up in a—

Mr Barr: It certainly would be preferable if airlines and airports could keep their robust commercial discussions around the board table rather than in the media, but it is what it is. Canberra Airport undoubtedly argue strongly around their own commercial interests, as you would expect from a privatised airport. I noted with some interest that the airline industry have expressed concern at the creation of private airport monopolies across the east coast in particular in that you had once publicly owned assets that were privatised but that there is not a huge amount of competition.

There is still only one airport you can land at in Sydney. There is only one airport you can land at in Canberra. In Melbourne you could arguably say there are two with Avalon, but whether that is necessarily a competitive arrangement remains to be seen. That is something that will play out in the aviation industry, and it raises an interesting public policy question about privatisation of what were publicly held monopoly assets.

MR COE: Regarding expenses, the budget states that there is a forecast of 3.8 per cent per annum over the next four years. That has increased based on last year's growth forecast, which was 2.7 per cent. Why are we seeing an increase of up to 3.8 per cent as opposed to what was forecast last year?

Mr Nicol: The budget aggregates are based on the sum of all spending across all directorates. It is not a top-down exercise where the government says that it will have a rate of growth of X-point-X per cent in any particular year. It is the result of all the cumulative decisions the government has made in regard to new initiatives, in regard to infrastructure spending.

Infrastructure directly does not hit expenses, but it does hit expenses through borrowing and financing. There will be other changes in there as well, such as depreciation. As assets are revalued and depreciation is reset for assets, that will change your expense profile. It is the aggregate of those expenses.

The other change, of course, will be the superannuation discount rate change from six to five, which adds $24 million to expenses. That will have slightly increased measured expenses. I am just trying to think if there are other—

MR COE: If you look at the chart on page 185 of BP3, does that fairly represent the increase in expenses that we are going to see?

Mr Nicol: That chart is affected very much by Mr Fluffy. It is the majority of the net costs for Mr Fluffy between the purchases, the sales and the demolitions of about $300 million. They hit mostly in 2014-15 and are spread over; so they are coming out.

MR COE: Given that in 2019-20, 2020-21 and 2021-22 there is that decrease, that fall-away, is that actually realistic?

Mr Nicol: The current forward estimates are based on, as I said, the forward projections of spending, and that is as a percentage of gross total product.

MR COE: Yes, noting that the forecast growth rate for the expenses is more than the overall economy growth rate as well.

Mr Miners: I am doing quick calculations, but do not forget the economic growth rate is a nominal number; so you need to add the inflation number to that as well. If you take the GSP plus inflation, you are actually up around six per cent. That is why it will continue to fall as a share of GSP.

MR COE: Okay. I turn to the large-scale generation certificates, which you can see on page 43. There is some discussion there on pages 43 and 44 about the handing over of these certificates to the commonwealth. Are you able to talk through the accounting impact of these certificates?

Mr Miners: There are two elements on both the revenue side and the expense side in terms of the accounting treatment. I should say that the treatment we follow in the ACT budget is exactly the same as the accounting principles require. The first thing is when the certificates are created, they create a revenue stream for the government. That is recorded as revenue. That comes on to the books at the time those assets are created and passed to the ACT. That happens immediately.

The next stage is then what actually happens to them. At the moment the government has a policy of surrendering those certificates. That happens at a point in time. When that happens, there is an expense equal to the value of those certificates, which occurs at the time of surrender.

That will not take place until that point of surrender. The way it is reported in the budget papers is that the government says it is holding on to them at the moment. The surrender will happen in the following year. I think 2019-20 is the first year of surrender. So there is an expense in that year, which is there. In the meantime they are valued at their current value and held in the accounts.

MR COE: But in terms of the actual cash impact, there is no cash impact at all?

Mr Miners: No.

Mr Nicol: No.

Mr Miners: Because they are held as an asset, basically.

Mr Nicol: The only cash impact would be if—

MR COE: As a non-financial asset.

Mr Miners: I will have to check where those actually sit.

Mr Nicol: We would have to check whether they are classified as a financial or not in that sense.

Mr Miners: Because they are treated as a revenue, I will have to check where the asset actually sits. I could not tell you off the top of my head.

MR COE: Yes.

Mr Nicol: The only possibility is if a government changed policy, decided not to surrender them and decided to sell them on the market instead. Then, obviously, the sale could generate a cash return, depending on what the price was at the time. That is the only way cash would come into it—through the transaction.

MR COE: But they are not valued at the current market; they are valued at the purchase price, are they not?

Mr Miners: No, we revalue them.

MR COE: You have revalued them?

Mr Nicol: The forward estimates of the budget do assume that their value will fall over the forward estimates. We have received advice that the current price, which is, I think, in the $80 range, will, according to our intelligence, potentially halve by mid-2020.

MR COE: So we are looking at going from, say, $70 million to $35 million and—

Mr Nicol: The price certificate will go from, we think, somewhere in the 80s to possibly somewhere in the 40s. That is what the budget is based on, anyway, but all these projections and forecasts are subject to uncertainty because it operates in a market.

THE CHAIR: We have a supplementary question on this from Ms Lee. However, noting the time, we will come back in 15 minutes after a morning tea break. We will then kick off with Ms Lee's supplementary.

Hearing suspended from 11.04 to 11.20 am.

THE CHAIR: Welcome back to the mid-morning session. We will kick off where we left off. Ms Lee had a supplementary question on the renewable energy certificates.

MS LEE: Perhaps you gave the entirety of your response on the large-scale generation certificates we were talking about before the morning tea break. The report that Pegasus provided to us, which is now publicly available, I understand, says:

> Given the current uncertainty in relation to the future development of the national electricity market, there is a risk that the Certificates will not realise the valuation applied when they were recognised in the Budget.

Do you have anything further to add to what we discussed before the morning tea break and/or in response to that statement from Pegasus?

Mr Miners: First, before I answer that specifically, can I just correct something? I think in my earlier answer I said that the first surrender of LGCs was in 2019-20. Apparently it is actually in 2020-21. My apologies for getting that date wrong.

In terms of the value, we treat the value of the certificates the same way we treat most assets. We do try and value it based on that market information as best as possible. That would include revaluing them, which is what we have done, and it does include then picking up the forwards, which has a reduction in their value moving forward to cover that risk. We feel that using market information is the best way to do that at this point rather than to make up a number ourselves.

THE CHAIR: The figure of $4.22 million in budget paper 3 for the components of government sector expenses shows that, as a proportion of expenses, health investment has actually decreased from 2017-18. Why has there been a reduction as a proportion of the budget in public health?

Mr Barr: Which page are you on?

THE CHAIR: It should be page 188, if my notes are correct. Yes. That graph shows health expenditure as 26 per cent of the budget. If you refer back to the 2017-18 table in budget paper 3 it shows that health had previously been at 27 per cent.

Mr Miners: Those charts represent a share of total spending. If you look at the functional tables on page 186 you can see the spending in the health function continues to rise in every year. It is a relative share; it is not a reduction in spending per se.

THE CHAIR: What would be spending then if it had remained at the 27 per cent mark?

Mr Nicol: Can we take that on notice?

THE CHAIR: All right.

Mr Nicol: I am also conscious that the functions have changed since last year. I do not know that health was affected seriously but it might have been.

THE CHAIR: Can you incorporate in that what change the functions have caused to that?

Mr Nicol: Yes. The other factor we will look at, and come back on, is if there is any one-off spending in 2017-18 that might have affected the percentage change. We will come back with all that information.

MR COE: We do hear from the Chief Minister semi-regularly that the share of health as a proportion of the budget is increasing.

Mr Nicol: Yes, and over time it will because its growth is generally higher, historically, than most other functions. Over time I expect it to be a bigger proportion of the budget. As I said the functions have changed slightly; so that might have had an effect. Also there are one-off factors, one-off spending. For example, the government gave additional funding to health in 2017-18 for an elective surgery blitz at the midyear review which can boost one year but does not flow through to the next year. It might not flow through. We will cover all those and give you an answer.

THE CHAIR: In regard to the significant changes to the expenses by function, how significantly have these changes altered the projections from previous budgets to the current budget?

Mr Miners: It will very much depend on the function. Some things have changed a lot; some have not. There are actually fewer functions than there were in the past. Some functions such as general public services have expanded quite a lot; so it would be very different.

Health and education are relatively untouched but, with some of the other purposes, have been amalgamated into general public services. It has got rid of a category; so that will be vastly different. Also, fuel and energy is now in economic affairs.

Some of that stuff which we had seen in housing and community amenities is now tucked in there. There are lots of those sorts of changes that have gone on, to the point where there is so much noise in it that it is not actually possible for us to go back and have a really good look at the previous years. It is quite a tricky thing to do.

THE CHAIR: There will be no comparison or longitudinal guidance given as to how those areas of government change?

Mr Nicol: At this point, no. We will have a look but it is quite a big job to—

THE CHAIR: When is that review likely or that work which you said—

Mr Nicol: I will be having a look in the next few months, and if we can do it we will publish something. If we cannot, we will be happy to give an explanation why we have decided not to.

THE CHAIR: And anything published is something that will be made public?

Mr Nicol: Yes.

MS LEE: We started talking about health. The budget states that with the health forecast the increase in expenses from 2018-19 is mainly due to "growth activity and costs for general hospital expenses". Could you provide some elaboration of or the underlying assumptions for this forecast? What growth activities do you foreshadow?

Mr Nicol: I can give you a brief introduction; then I suggest that that be raised in the health estimates. The government provides a general funding envelope for health which it allocates each budget, and there are three policy decisions for health funding. One is the speed of growth in the health funding envelope, which we can get you details on. I do not have the figures off the top of my head. It varies each year, I think.

MS LEE: Will you take that on notice?

Mr Nicol: Yes, we will take that on notice. The second set of decisions are what the government allocates each budget out of the envelope to health, and that will depend on the usual budget process. The third influence is the agreement we have with the commonwealth where the commonwealth funds a certain proportion, 45 per cent I think, of activity on a nationally efficient price. We forecast those activity levels going forward in order to calculate how much commonwealth funding we will receive each year.

A significant amount of effort goes into auditing those activity levels because they are related to a cash payment from the commonwealth. That is undertaken by the Independent Hospital Pricing Authority in consultation with all states and territories. Health can take you through the details of those far better than I can at this point.

THE CHAIR: Just while we are on the expenses by function, in regard to the change from what last year was recreation and culture to recreation, culture and religion, could you elaborate on the addition of "religion" and what the purpose of that is?

Mr Nicol: It is not something that we determined; it is determined by, essentially, the ABS in consultation with the IMF, I think. Is that right, Stephen?

Mr Miners: Yes, these are international standards.

Mr Nicol: We can try to find out some information. They do not look at the ACT per se when determining their functional classifications; they look at all governments. They have decided to incorporate that into that function for whatever reason. We can try and find out but I do not know.

Mr Miners: There is nothing I can add to that. I do not know.

Mr Nicol: There is nothing in particular in the ACT budget that I call religion, I do not think, or what the public calls religion. It is not anything of particular note for us. It is just what the function is called for all governments.

MS CHEYNE: What type of companies pay payroll tax in the ACT? What share of companies do not pay it at all?

Mr Nicol: The government has a payroll tax threshold of $2 million. Any companies under that threshold do not pay payroll tax. The big payers of payroll tax are the big national companies that operate in the ACT as well. They are generally all above the $2 million a year payroll.

MS CHEYNE: With big companies, do you mean banks?

Mr Nicol: Banks, retailers, big accounting firms—those sorts of businesses.

THE CHAIR: Universities.

Mr Nicol: Universities, yes. They are big enough to make the threshold.

Mr Barr: Utility companies are a good starting point. It you want actual individual company names, we cannot release that, of course. But go to the ASX200 list. There will be businesses in there. Not every business in the ASX200 will have activities in the ACT but a large number will, together with a range of multinational companies, some of whom do not pay much company tax because they have structured their affairs in such a way as to shift that taxation offshore. But they certainly are required to pay both land and payroll taxes in the territory. One could think of technology companies, large flat-pack furniture companies and others that would be captured within those tax lines.

Mr Nicol: In 2016-17, 91 per cent of ACT-based businesses did not pay any payroll tax and about 87.3 per cent of all businesses that operate in the ACT did not pay payroll tax in 2016-17.

MS CHEYNE: How is the $2 million threshold decided? Have we seen any evidence that the threshold is an obstacle to business creation or businesses wanting to be here?

Mr Nicol: The $2 million threshold is a government policy. It is a decision of government. I think the $2 million threshold is the highest in the country. Theory and some evidence would say to you that a higher threshold removes a potential impediment to business creation and business start-up. Most businesses start up with a lower wage threshold than that. We have seen quite strong business creation in the ACT.

Obviously, at any threshold level, it is going to be a question for the business to decide whether they continue to grow or not. I have not seen any evidence in particular that the threshold has operated in a way that has prevented businesses from growing. I think businesses, once they get to a payroll tax of $2 million, are starting to get to be a substantial business and face various costs et cetera. But it is part of the cost base of all businesses.

MR COE: Why was it increased a few years ago if it is inconsequential?

Mr Nicol: It has a cost on businesses, but that was a decision of government to essentially provide a more favourable investment.

Mr Barr: It is a policy choice. We have chosen to have a narrow tax base, as in we severely limit the range of companies who pay payroll tax by having that threshold. For example, in New South Wales, it is only your first $750,000 of payroll that is exempt. New South Wales captures a lot of small and medium-sized enterprises in the payroll tax net. They have a much broader tax base through that policy decision that they have taken as opposed to our rate for threshold.

MR COE: They do not accelerate at the rate of the ACT though, do they?

Mr Barr: In short, our policy choice has been to exempt about 90 per cent of businesses—particularly small and medium-sized enterprises—and tax the big players, the national and international players, at a higher level.

MR COE: If that were the case, why is it not a $10 million threshold or a $20 million threshold because those ones are going to have those sorts of payrolls?

Mr Barr: Sure. You would then need to draw a point at which you would narrow your tax base so much that, given the territory's size, it would be possible to see some businesses who you would rightly argue should be making a contribution in this tax line exempted. Yes, that is an arbitrary choice that was made.

MR COE: If you are trying to target the banks, all these big players—and given that it is not just incoming payroll here; it is payroll everywhere—surely you could have a significantly larger threshold and give real relief to small and medium-size businesses.

Mr Barr: To those big banks and multinationals?

THE CHAIR: No, to small and middle-size businesses.

Mr Barr: Mr Coe is moving into commentary rather than questions in that context. Nevertheless the policy position that the territory has chosen has been to have a significant difference between our threshold and that of New South Wales. As I say, unless New South Wales changes this in their budget this week, it is currently at a $750,000 exemption and we are at $2 million. Our rate is higher so we have a narrower base and we tax those bigger companies more.

When you look at the intersection of our higher threshold and our higher rate with New South Wales's lower threshold and lower rate, you see that a company would need to grow to have a payroll in the order of around $4 million, I think, before they pay more payroll tax in the ACT than in New South Wales. There is still substantive benefit for up towards 95 per cent of all businesses.

The remaining five per cent are those very large entities, particularly the multinational ones, who, as I say—and this has been the subject of considerable debate in this country—are able to structure their tax affairs in a way so that sometimes the only taxes they are paying in this country are to municipal and state governments. We are able to collect taxes from those particular businesses for the land they occupy in the territory and for their payroll contribution. They cannot avoid those taxes in the way that they have been able to structure their affairs to avoid other taxes.

That is a first principles taxation question, really. You fall on one side or the other of this particular debate. Both views are there for the public to see in terms of who should be making a contribution to taxation in this country and which taxes are easier to structure your affairs to avoid. We have taken the decision here to have a higher threshold and a higher rate of payroll tax to exclude most businesses. We have seen 2,000 more businesses operating in the territory now than three years ago. I think this policy setting is working for us. We will continue to pursue it.

A reason for raising the threshold over time is to ensure that wage price indexes that need growth in wages are taken into account. Whenever you set a threshold there will be an element of bracket creep. As wages rise—if you kept the threshold the same throughout time—you capture more businesses in the payroll tax net. That is one of the reasons why over the last seven budgets I as Treasurer have increased the threshold. I think it started at around 1.5 million when I was first Treasurer. It is now 2 million. That has more than accounted for wage price inflation over that period of time. But it would be a reason at some point in the future to revisit that threshold. At the moment, as we know, wage growth in this country is anaemic at around two per cent. That is one of the challenges that our economy faces

MR COE: Perhaps if there wasn't a six per cent tax on it they would have more money to give to staff.

Mr Barr: Should there be an increase in wages that is sustained over a period of time then the government would, at some point in the future, look again at that threshold. But at the moment it strikes the right balance between ensuring that all small and a large number of medium-size businesses in the ACT are exempt from paying any payroll tax at all.

Those medium-size businesses that do pay payroll tax pay comparatively less than they would if they were in New South Wales. It is only when a business grows to a very large size and has hundreds of employees that they pay more payroll tax in the ACT than in New South Wales. And that is as it should be. I am not in the business of giving the banks any more tax cuts at this point in time.

MS CHEYNE: If payroll tax were abolished, as some people have suggested, how much each year would we need to fill that gap? What sort of things would have to go up in order to fill that gap?

Mr Miners: Payroll tax in 2018-19 is forecast to be $522 million. You would need to find that equivalent amount in other taxes, reduce spending or borrow—one of those three things. The only sources you would have for that would be to increase our own source of taxation. You would either have to increase rates further or you would have to increase registration of vehicles. You could go to conveyance duty, which would be sort of contrary to current directions.

THE CHAIR: That is another tax that has been abolished but is not going anywhere.

Mr Miners: You would need to go to one of those other own source revenues to collect that amount.

THE CHAIR: How many businesses in the ACT currently receive either an exemption from payroll tax or are on a discounted schedule for payroll tax?

Mr Salisbury: Could I ask you to repeat the question?

THE CHAIR: How many businesses in the ACT either have an exemption from payroll tax or receive a discount to the payroll tax liability that they would otherwise have? Basically, how many entities over the $2 million payroll threshold are not paying the full rate of payroll tax?

Mr Salisbury: Is the question how many businesses in the ACT do not pay payroll tax?

THE CHAIR: No. How many have payroll in excess of $2 million but either have an exemption from payroll tax or receive a discount to the payroll tax levy?

Mr Nicol: I am not aware of any.

Mr Salisbury: I am not aware of any.

Mr Barr: There are two that I am aware of.

MR COE: These are sporting ones?

Mr Barr: These are the sporting ones. The Raiders and the Brumbies receive payroll tax exemptions or reductions as part of their performance agreement contracts with the government. I am not aware of any others, other than those two sporting teams. We will take that on notice. Generally speaking, there is not a policy of providing waivers to businesses in that regard.

Mr Salisbury: I clarify that they are waivers, not exemptions or discounts.

THE CHAIR: Is there a difference between a waiver and an exemption?

Mr Salisbury: Well, there is, yes.

Mr Barr: In legal terms, yes, there is. There is a line of tax waivers, you will see, in the budget papers, on that same table. The estimate for tax waivers in 2017-18 is $2.2 million.

THE CHAIR: How many entities are receiving a waiver? Is it just those two?

Mr Nicol: We will take that on notice. There might be one other.

Mr Barr: But that is tax waivers across the board—not just payroll.

Mr Nicol: We will take it on notice.

Mr Barr: It is in the order of half a million dollars for the sporting teams.

THE CHAIR: Yes, okay.

Mr Barr: The contracts are online and available. We have canvassed this, I think, before in estimates.

THE CHAIR: Things change. I have a question around the grouping for payroll tax purposes. It has been raised with me by a number of businesses that have expressed concern at the practices of grouping and how it is applied. What is the policy objective of grouping?

Mr Salisbury: The grouping rules try to group companies that have features like common control, common employees. Those companies, according to the grouping rules, are grouped for payroll tax purposes. If you had two firms that were both under the tax-free threshold, and they were grouped on the basis of control or common employees, they would be grouped together. They would be over the tax-free threshold, and they would come into the payroll tax net.

THE CHAIR: What consideration is given to whether or not the businesses are trading independently and in vastly different industries but may have a common director?

Mr Salisbury: It is a facts and circumstances test, but issues of control are fairly fundamental to the grouping principles.

THE CHAIR: So an individual might own two businesses—one in, say, hospitality, and the other one in, maybe, automotive—and the only commonality is the directors, but they would be grouped?

Mr Salisbury: Generally, yes.

THE CHAIR: Do you think that that is a fair application of the grouping policy? Would that not put what are two small businesses potentially at a competitive disadvantage to others simply because their owner is in two different marketplaces?

Mr Salisbury: That would be a correct application of the law. Whether that is the correct policy outcome is not a question I could answer.

THE CHAIR: How many entities in the ACT are grouped?

Mr Salisbury: I do have that number. It may take me a little while to find that in my briefing.

MS ORR: I could ask my questions while you are finding it.

THE CHAIR: Yes, Ms Orr.

MS ORR: Small business has come up quite a bit through this. Can you just refresh my memory? How many small businesses are operating in Canberra? Was it a metric that you put in there? Sorry; it was growth in small business, not how many small businesses. Was it 2,000 small businesses?

Mr Barr: There were 2,000 additional businesses in the last three years. The number will be in the order of 27,000, I think.

THE CHAIR: About 27,000 or 28,000.

Mr Barr: Yes.

MS ORR: Based on the information in front of you, is there any information on what industries those business are part of?

Mr Nicol: For those businesses that have more than 20 employees, which I have data for to hand, just over 20 per cent are in accommodation and food services; about 15 per cent in professional, scientific and technical services; and 11 per cent in retail trade. This is the number of businesses, not the number of employees.

MS ORR: Yes.

Mr Nicol: There are about nine per cent in administrative and support services; eight per cent in health care and social assistance; and eight per cent in construction. That is by numbers. Those are businesses with 20 or more employees.

MS ORR: So they are across a few fields. Obviously, compared to New South Wales and other jurisdictions, the payroll tax is part of helping small businesses establish in Canberra. What other policies does the government have in place to support small business?

Mr Barr: We have in this budget abolished commercial stamp duty on properties up to $1.5 million. That is about 70 per cent of all commercial property transactions that take place in the territory. They will, from 1 July this year, pay no stamp duty. Stamp duty is an up-front cost of doing business, so it will be cheaper to purchase commercial property in the ACT for small businesses.

Given that share of the total commercial market, up to $1.5 million in property value is a very pro small business measure contained in this year's budget. For businesses who choose where to establish, not only can they benefit from a higher payroll tax free threshold in the ACT—face no payroll tax charges here, as opposed to New South Wales—but they will not be taxed on the purchase of their commercial premises, for properties up to $1.5 million. That is another advantage for businesses to set up here.

There has been some commentary that businesses would move to New South Wales. If they were purchasing property in New South Wales to move into, they would be hit with a very large stamp duty bill, which would be a considerable cost of moving or relocating a business. What we have been seeing in recent times is in fact businesses relocating from New South Wales into the ACT in order to benefit from those lower tax rates, together with access to a skilled workforce, which is obviously a pretty fundamental element of business growth and success—the ability to attract and retain skilled people.

This, of course, varies across the nature of small businesses. Some require employees who are quite high up in the skills framework and others require less skilled labour. Nevertheless, the advantages that the ACT offers, in terms of establishment costs, payroll tax threshold benefits and access to a skilled workforce, combine to create an environment that has seen 2,000 new businesses establish in the territory over the last three years, and service exports grow by 22 per cent. At times those business are accessing international markets, which is terrific to see. And they are in a diverse range of industry sectors, as the Under Treasurer has identified.

You have a choice in how you go about raising revenue. Our choice has been to not tax small and medium-size businesses in the territory—either not to tax them at all or to tax them very lightly in terms of both their set-up and their ongoing costs—and to seek to support that end of the business spectrum.

I am happy to stand behind a value statement that the fast food giants, the big multinational tech companies, the banks and the ASX 200—all of those large businesses—can and should pay payroll tax in this jurisdiction. I will seek to structure our tax system in a way that supports small and medium-size enterprises not only to establish in the ACT but to grow. If they grow to a sufficient size that their payroll is more than $4 million or $5 million annually, they are a success story in the context of the ACT economy, and in that instance it is fair and appropriate that they make a contribution back to the community through payroll tax.

No-one enjoys paying tax. I do not meet many people who come cartwheeling up to me saying, “It is fantastic. I really appreciated paying tax this year.” But—

MS LEE: Is that a challenge?

Mr Barr: There are people who have taken up that challenge. Maybe not cartwheeling, Ms Lee, but since I have been making these statements, there have been some people who say, “Actually, I do not mind paying tax because I know it goes to contribute to a better community.” I agree with that sentiment.

The government’s philosophy around revenue and expenditure is to find that balance to ensure that we raise enough revenue to meet the needs of this community, to invest in the future of this community, and to do so in the simplest, fairest and most efficient way. As a result of these policies, we are in a period now of very strong economic growth, with the lowest unemployment rate in the nation, incredibly strong jobs growth and service export growth. It is a good time in the ACT economy historically.

The challenge for us over the next four or five years is to keep on working harder to ensure that these sorts of outcomes can continue: that we can drive unemployment lower, that we can see more new businesses established in the territory, and that we can continue to provide the services that this growing community needs. That is the basis on which we undertake our task of preparing the budget each year.

THE CHAIR: Mr Salisbury, can we just finish my previous question, please, if we have an answer?

Mr Salisbury: I have. There are 1,626 groups registered for payroll tax in the ACT, representing 2,595 individual entities.

THE CHAIR: Do you keep track of those entities within a grouping as to whether or not individually they are above or below the payroll tax threshold?

Mr Salisbury: Yes, we would. Yes.

THE CHAIR: Could you provide—I would imagine it is information that needs to be taken on notice—a breakdown of the number of entities inside those groupings that are otherwise exempt from the payroll tax, with the payroll under that $2 million threshold?

Mr Salisbury: Yes, certainly.

MS ORR: In relation to that last bit of evidence, Chief Minister, you mentioned that the payroll tax threshold and the stamp duty reduction for commercial businesses were some of the policies you were doing, but you also had other policies to support small business. I believe the policy innovation team in this budget has been expanded. Would that go towards supporting small business?

Mr Barr: Yes. There are a couple of initiatives on the regulatory reform side that are contained in the budget. These are two of the many areas of the interplay of regulatory systems, together with taxation arrangements and the availability of land, labour and capital, that go to informing business investment decisions.

On the regulatory side, there is an initiative particularly around the hospitality sector, in the cafe industry. That is a small business innovation that is a partnership between the ACT and the commonwealth. Through the budget, we have also just funded the ongoing work of the regulatory reduction area in order to streamline regulatory responsibilities. This is an opportunity for us, combining both the local and state government regulatory responsibilities that—

MS ORR: A benefit you cannot get anywhere else in Australia.

Mr Barr: Yes, indeed. That is an advantage for the territory, and in terms of both national and international investment interest, it is a real point of difference that navigating through a regulatory system does not require dealing with multiple levels of government, which a number of national and international businesses have expressed frustration at in the context of, for example, investing in Sydney, with the myriad of local government arrangements that are in play in that market, combined with the state government arrangements.

Sometimes it would be fair to say that local governments pursue an entirely different policy direction from state governments, and that has been commented on in the context of the City of Sydney, for example. The advantage we have is a consistent policy direction.

MR COE: Chief Minister, you said that you make no apologies for fast food giants paying payroll tax. If someone owns one Subway store, do they pay payroll tax?

Mr Barr: It will depend on the nature of the franchise arrangements in that context and whether there is a grouping provision, and it will depend on the legal structure of that particular circumstance.

MR COE: But if you have no problem with the multinational fast food chains—

Mr Barr: If you are part of a large international corporate structure and that is part of the business arrangements, I think it is reasonable that there is some tax paid, but in the example you give, it will depend, of course, on the nature of the legal arrangements around the—

MR COE: Sure. Say it is a corporate store and you own 80 per cent of the store, 90 per cent of the store or something along those lines, which I gather is a somewhat typical franchise arrangement. Then you have profit spreading as well and all sorts of other things. Do you think it is fair that the first person that business employs should attract the six per cent tax?

Mr Barr: If the legal arrangements and the structure of the franchise arrangements are such that you are part of a multinational chain and you benefit from all of the marketing and other elements that go with that particular business structure, then, yes, the law is the law. That is reasonable.

MR COE: I did not ask what is legal. I asked do you think it is fair.

Mr Barr: Yes. I have no issue with multinationals paying tax.

MR COE: Even if it is a local franchisee who personally has his house on the line?

Mr Barr: As I say, the circumstances of the franchise arrangement will obviously vary, depending on the nature of the multinational company. But the multinational company should pay tax, yes.

Mr Salisbury: If I can just—

THE CHAIR: Even if it is majority owned by a local franchisee?

Mr Salisbury: It will really depend on how many employees there are in the ACT as to whether they come under the threshold or go over the threshold. My experience with franchising is that if one owner runs a number of franchises in this jurisdiction, those two franchises may be grouped for payroll tax purposes. It is unlikely that we would group a single franchise in the ACT with the national network of franchises.

MR COE: So you could be part of a supposedly evil multinational network but not pay payroll tax if you own just one store and do not get to $2 million?

Mr Salisbury: That is correct, yes.

Mr Barr: It will depend on the legal arrangements associated with that particular franchise entity. Do I have a problem with Google, Facebook and some of those firms paying tax in this jurisdiction? No; I think they should. You are the one who is arguing to the contrary.

MS LE COUTEUR: This will be a different question. It relates to budget paper No 3, page 170. It deals with two items. The first is about renewing Higgins neighbourhood oval and the second is about more services and trees for our suburbs. Specifically, I want to ask about the budget treatment of living infrastructure. If you look at the Higgins oval, it has depreciation shown as an expense. If you look at the trees, they do not depreciate. I am interested in how you treat our living infrastructure.

Mr Nicol: We are getting into accounting principles here and detail that I might not be able to answer. But if it is a physical asset that clearly depreciates, if we can determine its useful life, we will give it a value and generally a depreciation schedule. Periodically we review the state of our assets and that may produce a different value and a different depreciation schedule.

MS LE COUTEUR: Trees are clearly physical assets that have a limited life.

Mr Nicol: Yes, and trees, our urban forest, are an asset that is on our balance sheet. I will have to take the question on notice, unless Mr Miners knows how they are depreciated. I think we probably depreciate them when a tree is removed or dies because a tree grows and matures. The accountants cannot value everything, I am afraid. I suspect we expense those costs when the tree dies or is removed.

Mr Miners: It is certainly something we would follow the standard accounting principles on. You may plant a tree and in the first year it actually grows; so it probably goes up in value for some time and then eventually holds that value for a long period of time. It has that value towards the end. It would be something we would follow the accounting standards or principles on. I can get the detail—

Mr Nicol: We can get the detail on how it is applied in practice.

MS LE COUTEUR: One of the things that I am interested in with respect to that is that we historically have underfunded the maintenance of trees in the ACT. It appears to be the fact that you do not allocate depreciation to them. Is this related in any way to the maintenance budgets that we have to keep them or not keep them in good nick?

Mr Nicol: No. In that case, essentially for most of our assets, I think there would be a correlation between assets that are more highly depreciated than their maintenance costs. But it is not a direct relationship. For example, generally a new asset will need less maintenance than a 30-year-old asset.

MS LE COUTEUR: Yes.

Mr Nicol: And the 30-year-old asset will be more depreciated than a new asset. But there is no direct correlation. Depreciation is the recognition of the expense of the capital value of an asset over time. That is how the capital investment side of the budget appears on the operating statement, through depreciation over time.

As the Chief Minister has said, for an asset that lasts for 50 years, you expense it over 50 years. It has a cost over 50 years, not the cash cost of acquiring the asset. The questions of maintenance and capital replacement are separate questions to depreciation.

Even with capital assets, some would argue that part of our depreciation expense, which is non-cash, can be used to cover the replacement of those assets. It does not work like that. A school might last 30 years and is depreciated over 30 years. You do not replace that school over 30 years. You replace it at the end as a one-off lump sum cost. They are separate in terms of both capital replacement and tree replacement and depreciation and maintenance and depreciation.

MS LE COUTEUR: When you are looking at providing the answer on notice, can you also look at the wetlands? The ACT has spent large sums of money on wetlands and associated water treatment things over the last few years. These are clearly very mixed assets—large holes in the ground but also there is living infrastructure. How do you deal with those?

Mr Miners: We can certainly take it on notice and have a good look at the detail. Certainly it would depend, again, on the nature of the assets. Some of those water treatment things are a clear asset. They depreciate and need replacing over time. They can be depreciated. Other bits are harder to value. I would need to go back and look at the details.

Mr Nicol: And maintenance also; that is a very good example. We are very much aware that the natural swales that are now part of our urban form are much more costly to maintain than a concrete creek that sort of makes up our older suburbs. Now budget is allocated to Transport and City Services and it is in their purview to determine how that is split in terms of meeting the maintenance of all of their infrastructure assets.

It is a question I would raise with them. At the end of the day it is a question for government as to how they allocate funds not only to maintenance of these sorts of assets but maintenance of more physical assets—schools, roads et cetera—as well as the balance between that and creating new assets and how that balance works over time.

Mr Miners: Certainly, maintenance is one of those factors that is taken into account in any decision on any assets that are there. The maintenance of those assets is considered.

Mr Nicol: I think we have some legacy assets pre-self-government that perhaps were often created under cash accounting, whereas under accrual accounting those sorts of things are much more obvious and are taken into account. As Stephen said, whenever we build new physical infrastructure, we build in a maintenance cost for that infrastructure. We recognise the depreciation costs according to the accounting standards et cetera.

MS ORR: Also on notice, can you provide the accounting standard that you use for trees?

Mr Nicol: Yes, certainly. I do not know the accounting standard for trees off the top of my head.

MS ORR: That is why I was happy for you to take it on notice.

Mr Nicol: Unless one of my experts can.

MS ORR: If anyone does, come and wow us, yes.

Mr Miners: The answer for trees is that they are actually treated as part of the value of the land, which is why they are not depreciated. So the trees are actually included as part of the value of the land. That is the accounting standard of doing that.

Mr Nicol: The public sector has many examples of difficult to apply accounting standards.

Mr Miners: Yes.

Mr Nicol: Some examples include things like the value of land under roads or the value of land in the lake that we are repossessing.

THE CHAIR: So was there any change to the valuation of trees when thousands were cut down along Northbourne Avenue for light rail?

Mr Nicol: I will have to take that on notice. In fact, I think we are planting more trees at the end of the project than we removed.

MS CHEYNE: Correct.

THE CHAIR: But obviously a number of fiscal years have passed since the removal of the said trees and the replacement.

Mr Nicol: I will have to take that on notice to see whether there was a change in the value of the land.

Mr Miners: It will depend on the net number of trees.

MS LE COUTEUR: Maybe an easier way to deal with an example along those lines would be after the 2003 bushfires, when an appreciably large number of trees were removed. Did we change the value of the land?

Mr Nicol: We can take that on notice. There is a difference in valuations between the urban forest and the non-urban forest, I think, and a difference between a commercial forest, which we did—

MS LE COUTEUR: Yes.

Mr Nicol: That were impacted—

Mr Barr: And were insured.

Mr Nicol: And were insured. That was to the tune of $40 million, I think—

MS LE COUTEUR: I am not particularly interested in the commercial forests.

Mr Nicol: Yes, I understand.

MS LE COUTEUR: They are clearly dealt with commercially. The other street trees, they are not a commercial forest. That is where—

Mr Nicol: We will take it on notice. I doubt we made a specific change to the asset values.

MS LE COUTEUR: We have the trees down as a capital expenditures. Obviously, I am totally in favour of it. I am just trying to make sure that we keep enough accounting that they can be loved and replaced as necessary.

Mr Miners: Certainly, the value of the trees that I have seen done is about the aggregate total. It will look at the number of trees we have. Some are cut down, some are replaced and some new ones are planted. There are new trees down Constitution Avenue. It will be the net effect of all those, not looking at the total number of trees, that determines the value.

MR COE: It is all very artificial, of course. Are there councils that are not bothering with this because to call something an asset that cannot be sold, does not derive an income and actually costs money to maintain is a bit of a stretch?

Mr Barr: Like a hospital or a school?

MR COE: That is exactly right. It goes to the accounting challenges of what really is an asset. If it cannot be sold and it is not productive, how do you—

Mr Nicol: I would argue—

Mr Barr: Trees are productive. Gee, there is a bold statement: "Canberra Liberals leader announces 'trees not productive'."

MR COE: There you go.

Mr Barr: I can see the press release right now.

MR COE: I am sure there are hundreds and thousands of people in Canberra that care a great deal.

Mr Barr: Yes, there probably would be.

MR COE: If it means that the tree in the backyard can be chopped down, I think they would be pretty excited to hear that media release.

Mr Barr: I will bear this in mind at any point I ever receive correspondence from a Canberra Liberals member regarding a tree.

MR COE: But if it cannot be sold and it is not deriving an income, it is not technically productive in an accounting sense, how do you get around that? And do other jurisdictions do the same thing?

Mr Nicol: I do not test how other jurisdictions apply the accounting standards. There are differences between public sector accounting and private sector accounting. We have a different reason for existence, and we are trying to apply as consistent a treatment as possible. We are creating assets, however, that produce benefit.

MR COE: I agree they produce benefit; it is just a matter of whether it is financial.

Mr Nicol: Certainly. That benefit goes to livability, supporting our economy and supporting our tax base. If you want to take a strict accounting economic perspective, you could say that if we have a livable city, we are going to be more attractive for businesses.

MR COE: That is an economic impact, not a financial impact.

Mr Nicol: No, but if you are treating the government as a business, our tax base depends on payroll, employment, growth et cetera; all of those things feed into that. I would probably end by saying that the accounting treatment of trees is probably not what triggers the interest and discussion and healthy debate about protecting trees and replacing them when they die. It is not whether they have depreciated or not; it is how they impact on the environment.

MR COE: The same could almost be said for roads that are not toll roads, for instance. Yes, they are an asset in that they cost money to replace and cost money to build, but they are not an asset that directly brings in revenue or can be sold.

Mr Miners: I think you would find that if Canberra did not have any roads, that would have a direct economic—

MR COE: Of course, but that is economic. It is economic, not financial.

Mr Miners: I think it is financial as well, because people would not live here. I think the link is fairly tenuous. Those things are part of the underlying activity. Yes, it is economic infrastructure, but that economic infrastructure provides for financial returns as well. The government does not collect money directly from the roads, but those roads create the economic environment that supports economic activity, supports businesses, supports all those things.

MR COE: As part of that net worth, are the credit agencies happy to take all that on board?

Mr Nicol: The credit agencies look at a lot of metrics. If you want to go into detailed questioning, Mr McAuliffe can answer some of those questions. If you are looking at it from a strict accounting financial perspective, the biggest asset any government has, which is not on any government's balance sheets, is its taxing power. I think the ratings agencies conceptually look at a government's taxing power, but they also look at the political environment in terms of deploying the taxing power: can the government and can the community afford a higher taxing regime?

The ratings agencies certainly go through some of the key factors. One is financial management and transparency. Do we adopt accounting standards? Do we use them? Are we audited? Is all of that at arm's length from the government? And it grades each institution on that.

MR COE: Is it net worth or is it mainly cash?

Mr Nicol: It would look at more the fiscal balance. It would certainly look at net debt and whether that is affordable.

MR COE: Yes.

Mr Nicol: That is net debt as a proportion of—

MR COE: But many of these assets would not necessarily go to it?

Mr Nicol: No, they would not. They would not say that we could sell $100 million worth of trees. That is certainly the case. They look at our ability to essentially finance our debt as and when it becomes due. As I said, that goes to our ability to tax and raise revenue, the strength of those revenues and our flexibility on the spending side. If there was a market event that disrupted, could we survive and how long could we survive? It is those sorts of questions.

MS LEE: Can I go back to the expenses by function raised earlier. We talked about health and recreation, culture and religion. Education talks about the significant growth in education in the forward estimates being as a result of enrolment growth and the operational costs of schools, in line with general wage and price inflation. That is at page 187. How have new schools and the expansion of schools been incorporated into this growth? How are they are treated?

Mr Nicol: The expansion of schools and new schools are capital investments, so this is the recurrent spending. As we build new schools, as we just talked about, depreciation will be incorporated into expenses by function. Essentially it is a policy process where, through the budget process, as in every other area of expenditure, the government looks at need and pressure. In the education system that pressure is particularly in north-side suburbs, where we are keeping up with the growth in population.

MS LEE: We have all seen the media about the capacity issues in our schools at the moment. That clearly has impacted on the timing of these announcements.

Mr Nicol: Indeed, and we have to design a process and policy decisions that are put to government to make those investments as best we can in advance of that growth. That will come to questions of expansions—when they happen, how fast they happen and what we have to do to get that in place so that school growth can be accommodated.

There is a lot of pressure on the north side and there are under-enrolments in the far south, so we have to deal with those from a policy perspective. I suggest you raise that with the Education Directorate because they are actively looking at that and they engage with us on those sorts of questions. There has been strong growth in public sector education enrolments, and that has been picking up over the last year or two. We expect further investments will have to be made in new schools in the medium term.

MS LEE: What are the other trends in terms of enrolment projections for the next couple of years and how will that change the operational costs?

Mr Barr: That is really for the Education Directorate. Treasury officials are not going to have that level of information.

MS LEE: It was only because the Under Treasurer was raising that you have been—

Mr Nicol: We do discuss it with education. We test their models and their growth and their demand, and we come to an agreed position on that. They have much more detail than I have to hand, but growth has accelerated.

MS LEE: Going to social protection, every category in table 4.2.1 has had an increase in expenses projected, except for social protection, which seems to be almost going backwards. Why is the government spending less on that and what is included in this category?

Mr Miners: Again, these are new categories so we are still, as I said, trying to work out exactly where things are moving in them. My understanding is that this now includes the housing and community amenities, which have had a large spike in spending through the housing renewal program. It will not be as high in 2018-19 as in 2017-18. It is more coming back towards base rather than a dip per se. But I can have another look at that and come back with further detail on notice.

MS LEE: Transport is set to grow by more than $57 million this year due to stage 1 light rail. That is close to $100 million more than last year and then to $392 million in 2021-22. Is this only light rail stage 1?

Mr Barr: That would also include further investments in the entire public transport network, including buses. My presumption is that transport would also capture transport-related expenditure in the forward estimates.

MS LEE: Does it include any of light rail stage 2 at all?

Mr Nicol: It includes design.

Mr Barr: It includes stuff that is already in train but not the operating costs.

MS LEE: So design and consultation and that kind of stuff, but not—

Mr Nicol: The government has not allocated that funding yet.

MS ORR: We have seen the creation of how many jobs in the last year?

Mr Barr: Certainly for calendar year 2017 it was around 10,000 additional jobs. We will get the 2018 data as we progress through 2018.

MS ORR: Do you have an idea of within which industries those jobs have been created?

Mr Barr: Yes; we can provide that data. The ABS will collect all of this information, so we can make that available.

MS ORR: My understanding is that jobs growth in the ACT has been quite strong in recent years. Am I correct in my understanding?

Mr Barr: Yes. When compared with our long-run average job growth and, indeed, job growth in other jurisdictions, yes, it has been a very strong period. We are seeing that jobs growth occur principally outside of the commonwealth public sector. We have contributed to that as the most diverse employer in the nation in terms of occupations. I do not think there is another employer in this country that would cover the range of industries and occupations that we do, with both the local government and state government responsibilities. So we have contributed to employment growth, as have the service export sectors. There has been strong growth in health and community services in recent times as well. We can provide detail for that.

Mr Nicol: Yes; I do not have it to hand. We have also had strong growth in our university sector, our education sector. Construction has been strong as well. Employment has been growing at above long-term trend for some time now. We expect it to moderate a little bit but still be very healthy into the medium term.

MS ORR: I want to find out a bit more about the benefits to small business. Regarding the key industry sector development initiative that has been announced in this budget, am I right in understanding that that goes towards jobs creation and small business support?

Mr Barr: Certainly there will be elements of that particular initiative. We can talk about that in some more detail on Friday when I appear in an economic development capacity. But that is certainly one element of the budget that goes to support our export efforts, together with business growth across the territory.

MS ORR: Budget paper No 2, page 71, says that we expect to see more jobs created in the knowledge-based industry. As well as this one, what industries do you see growing in the ACT?

Mr Barr: Undoubtedly professional, scientific and technical-related areas and ICT and cyber-related industries. I think there is further capacity for growth within the space economy. I was pleased to see an announcement from Senator Carr in relation to a decision our federal colleagues have made to headquarter the national space agency in Canberra, should there be a federal Labor government in time for that decision to be finalised. So that is a good outcome for the ACT.

We continue to engage with Dr Megan Clark, who is heading up this process for the commonwealth in relation to the development of the national space agency. I spoke with Dr Clark one evening last week. She was on the other side of the world, but we managed to coordinate a time to catch up, and we will be meeting again in July as part of that process. I think Senator Carr made the correct observation that the national headquarters for the agency has to be in Canberra in order to coordinate the more than 93 areas of commonwealth government activity that relate to the space industry. Any decision to locate that agency outside of Canberra would be done for base political reasons, rather than capability.

There is a role for every state and territory in our national space effort. Clearly the ACT will not be a launch site for satellites. It will not be an advanced manufacturing base; they are opportunities for other parts of the country. WA has a very significant radio radar that is of great value to the national space effort. Our capability in Canberra is through the ANU and the University of New South Wales Canberra, together with the defence department's space program that is all headquartered here in Canberra.

I think 2,000 of the 10,000 in the nation in the space industry are in Canberra, so we are a very significant player in what will be a new and emerging industry for this nation. I think we are well placed to play a role, but it is not a winner takes all gig. It should be seen not as an exercise in competitive federalism so much as cooperative federalism, in that there are opportunities for all states and territories.

It would be absurd to locate the headquarters outside of the national capital, given the capability that exists and the reason for being a national capital. But to do that does not mean that other states and territories will not have a significant role to play in it nationally, which is what needs to happen. I am pleased to have seen Senator Carr's announcement and pleased to have had very productive discussions with Dr Clark. I look forward to that continuing, because it will be an opportunity for the ACT.

MR COE: With regard to energy bills and particular rebates, are you expecting that the draw on the budget will increase significantly as a result of energy prices?

Mr Barr: Certainly we have made a provision to increase the general concession by a further $50. We have factored that into our forward estimates. However, it has been pleasing to see a level of competition at play within the electricity retail sector in the territory over the last period that has seen price reductions. I think ActewAGL is offering a 25 per cent reduction to customers who sign up to their arrangements, and Origin Energy also has some reasonably competitive deals in place at the moment. So we have seen the retailers seek to absorb a good part of that increase. In some instances, depending on which contractual arrangement a consuming household can sign up to, they can reduce their energy costs.

MR COE: Page 192 says that the rebate in 2018-19 is going to be 15.7 per cent. Last year's budget had 14.2 per cent. That is an increase of 10 per cent. However, people could experience more than that when you factor in the 20 per cent increase last year on energy prices. So, in effect, is it a bit ambitious to think that the total rebate is only going to be 15.7 per cent?

Mr Barr: The factors that would drive that would be an increase in the number of eligible concession card holders, together with the increase in the rebate itself. We have the capacity at the midyear review, should demand be tracking ahead of this projection, to supplement this particular community service obligation. And were that to be the case, we would supplement it, but we will wait and see. We will get the first half of the year's data. It is good to see the retailers competing for market share. The 25 per cent reduction would not reduce costs back to where they were pre the removal of the carbon tax. That has turned out to be a spectacularly unsuccessful policy in terms of keeping downward pressure on energy prices.

MR COE: There might be a few other factors at play.

Mr Barr: There may be a few, but we were all promised, were we not, that if you get rid of the carbon tax and electricity prices will fall? We have seen the exact opposite of that. Yes, there are a range of factors, but investment certainty is one of those. Fortunately in the ACT all parties are in agreeance with our 100 per cent renewable energy targets and the fact that we have been able to lock in a long-term, secure supply of renewable energy. We are all still in agreement on that, are we not?

MR COE: Can you please take on notice—

Mr Barr: Are we? Are we all still in agreement on that one?

MR COE: has there been an increase in the number of people—

MS LEE: Have not said otherwise, Mr Barr.

Mr Barr: Have not said otherwise. Thank you.

MR COE: Can you take this on notice: has there been an increase in the number of people accessing the scheme? How many applications were received for rebates during each of the last five years? How many rebates were approved or claimed during the last five financial years?

Mr Barr: I believe you have already asked a number of those questions on notice, so that data may already exist. We will be able to—

MR COE: I think there is a slight nuance to what I have just asked.

Mr Barr: We will look at information we have previously provided. We will look at where we are now and provide some further information to you.

MR COE: And the average value of the rebates would be useful as well.

THE CHAIR: We will suspend for lunch. The committee will resume at 2 pm.

Hearing suspended from 12.32 to 2 pm.

THE CHAIR: Welcome back to the afternoon session of estimates, continuing with the Treasurer, looking at the treasury budget estimates. In the vague schedule we have for this session, we are going to try to look at the Compulsory Third-Party Insurance Regulator and the statement of intent, as well as the lifetime care and support fund and output class 6 of treasury, which is revenue management.

MR COE: I would like to go to the revenue side of things first up. With regard to rates, at what point does a property become rateable after it has been purchased from the SLA?

Mr Nicol: I will get Mr Salisbury up to answer your question, Mr Coe.

Mr Salisbury: I caught the question on the way up. I think it was about how quickly after a block of land is sold it becomes rateable. I am not sure what the exact legal point is, but I would say that it becomes rateable very soon after it is sold.

MR COE: I think it is something we might have discussed before, but I just wonder whether there is any update on this. If a block is sold by the SLA or by the housing renewal team, is the sale price then the unimproved value?

Mr Salisbury: It is a good indicator of the unimproved value, but there may be a number of other factors that are taken into account.

MR COE: Are we talking about it being 10 to 15 per cent of that sale price?

Mr Salisbury: It is going to be pretty close to that sale price, generally.

MR COE: In the event that blocks are unable to be serviced for one reason or another, like Icon Water struggling to connect it up or Evo not being able to connect the block up, is that just a risk that the buyer takes on or can that be considered in whether rates are applicable?

Mr Salisbury: That issue very rarely comes across my desk—that people raise that issue when they object to rates. That is very rarely raised.

MR COE: When it is raised, what happens?

Mr Salisbury: Sorry?

MR COE: In the circumstances where it is raised that somebody is unable to connect to services as they expected to be able to, or Evo or Icon say that it is going to be nine months or 12 months before they can actually connect the block, is it fair that rates are charged even though the block is, in effect, unusable?

Mr Salisbury: In terms of the Revenue Office, rates would be chargeable from the date that the law requires. In terms of equity issues, I do not think we would make a call on that in the Revenue Office. That would be something that would go to objection, and we would see how the law applies. If the person involved is not happy with the outcome from the objection process, I guess they have the option to take that to ACAT. Alternatively, they could apply to the government for a waiver in those circumstances. I think they are the two options available.

MR COE: On that issue of a waiver, how many waivers for rates have been given in the last 12 months?

Mr Salisbury: In terms of the particular example you are referring to?

MR COE: No, just in general; just rates waivers.

Mr Salisbury: Rates waivers? I do not have figures on rates waivers. It is not a mechanism that we use generally—waivers for rates.

MR COE: Treasurer, can you remember signing off on any waivers?

Mr Barr: I do not believe so, no. But we will check the record.

Mr Nicol: I cannot recall any either, but we will check.

MR COE: Are there any sale contracts or any commercial negotiations that include reductions in rates?

Mr Nicol: Not that I am aware of.

Mr Barr: We will check.

Mr Nicol: We can check.

MR COE: Are there any historical ones, like the Canberra Centre or anything like that?

Mr Nicol: Not that I can recall. The last one I can recall where the rates arrangements were changed was with the airport, which went through specific legislation.

Mr Salisbury: In the time that I have been revenue commissioner, since 2012, I am not aware of any deals or arrangements that have taken place like that.

Mr Nicol: We will check.

MR COE: Thank you.

MS ORR: How many rateable properties are there in 2018-19?

Mr Barr: It is around 168,000, both residential and commercial. It has grown by about 25,000 over the last five years or so. We will check.

Mr Salisbury: That is a pretty good number. I will just double-check.

Mr Barr: Of course, we are releasing 17,000 new, so it will grow by at least a further 17,000 over the next four years, associated with that land release, plus whatever subdivision might occur, and growth in commercial rateable properties. Certainly the number of rateable properties is growing substantially each year. We have about 168,000 now, and we are releasing 17,000 more. That is 10 per cent growth over the next four years just from the land release program, let alone infill projects and the like that will increase the number of dwellings.

It is certainly the case that the territory's rateable base continues to grow. Obviously, we see the expenditure side of this clearly in terms of demand on services, but there is growth, and we have seen substantial growth, in the number of properties in the territory over that period, and that, of course, is reflected in future revenue growth. The total increase in revenue is both a function of growth in the total number of rateable properties and an increase in rates.

Similarly, on stamp duty, the fact that there are 25,000 more properties than there were five years ago is reflected in the level of turnover of properties overall. That is part of being in a growing economy.

MR COE: In terms of non-rateable properties, are we just talking about public housing properties?

Mr Barr: No; they are rateable.

MR COE: What are non-rateable properties then?

Mr Barr: Almost none.

MS LE COUTEUR: Charities? Churches? Are they non-rateable?

Mr Salisbury: There are a number of non-rateable properties that are community facilities, like scout halls and the like. In terms of the numbers, I can confirm that the total number was 167,993 properties.

Mr Barr: I was out by seven.

Mr Salisbury: I know.

Mr Barr: I will keep a closer eye on that growth figure.

MS ORR: We touched on this a bit, but I want to get more detail. Can you explain to me the difference between the growth in the total rates revenue and the growth in the amounts individual home owners pay, and how factors like the number of rateable properties and the value of individual properties affect this?

Mr Barr: The biggest impact is the number of properties. The value of properties really only impacts on the distribution within that broader collection. It really goes to what share of the total revenue pool is paid by each individual property. We have seen, for example, that land values have increased along the light rail route, so people who are along the light rail route are paying more rates as a result of that. People who are not on the light rail route are, comparatively speaking, paying less.

I think the variation across the districts saw some below the territory-wide average. For example, Weston Creek rate increases were lower than the territory average; north Canberra and Gungahlin were above the territory average. One of the factors there that is impacting on land values, as was predicted at the time, is the transport infrastructure.

MS CHEYNE: Let me go to stamp duty. People talk about it a lot. Following on from the rates discussion, one of the big centrepieces of the budget appears to be abolishing stamp duty for first homebuyers. Why was that decision taken, and what benefits does it have? Also, what impacts does it have on our overall revenue stream?

Mr Barr: It reflects a further step in what has been a multi-year policy approach to phase out stamp duty. It represents an acceleration of that program as it relates to the first homebuyer segment of the market. I would also note that we have continued the pensioner duty concession scheme in this budget. That targets two particular segments of the housing market, in addition to the ongoing program of reduction of duty rates across all property types in the territory.

Going to the figures, if we had just left the stamp duty rates where they were prior to reform, someone purchasing a $350,000 property would be paying $5,550 more in stamp duty; someone purchasing a $420,000 property would be paying $6,880 more; someone purchasing a $500,000 property would be paying $8,400 more; someone purchasing a $700,000 property would be paying $10,780 more; and at the high end of the scale, someone purchasing a $2 million property would be paying $22,150 more.

MS ORR: Chief Minister, can I check whether that is just at the point of conveyance? If you added that onto your mortgage, would you have compound interest on it?

Mr Barr: Certainly, yes. That is just the stamp duty component. Most people—not everyone, but most—borrow to pay the stamp duty. That is the tested market experience. It certainly is the case for first homebuyers, because in having to save for both a deposit and stamp duty there would be a considerable amount of saving that would be required for households in that circumstance. Not only is there an up-front saving, which is pretty critical in terms of cash flow for a first homebuyer, but there are lower mortgage repayments over the life of a loan.

THE CHAIR: There are also considerably higher servicing costs and rates on that property now going forward.

Mr Barr: You are providing the commentary as well as asking the questions. Yes, it is indeed. That is the trade-off. This is not a new topic; we have explored this every year for the last seven years. That is the trade-off. It is a question of the time value of money, is it not?

There are obviously going to be a range of views on this, but I do not think those who so easily dismiss a $10,000 saving now as being worthless are in the real world. Yes, there are ongoing costs associated with a tax mix switch. Yes, what we are doing is saying that rather than funding the territory's services out of the seven to nine per cent of the population who might transact in the residential property market in a given year, we will spread that cost across the entire rateable tax space and ask everyone to make a small contribution each year to the services that they consume each year, rather than saying that in one in every seven years, which is on average how often people move in Canberra, we will hit you for tens or thousands of dollars versus making smaller annual payments. That is the trade-off.

THE CHAIR: Treasurer, you are obviously giving figures on what you save on the purchase price, but has any modelling been done on the life of ownership expense difference, substituting for an average Canberra home the stamp duty component for increases in rates.

Mr Barr: Yes. That was part of the first range of modelling, and it is contained within the—

THE CHAIR: When was that last updated?

Mr Barr: A year ago? Maybe it was 18 months.

Mr Nicol: Two years ago.

Mr Barr: Two years ago. We will do a further set of modelling associated with the development of the next phase of tax reform. Obviously, the interest savings on the stamp duty borrowings are significant for households, as well as, as I say, the time value of money. Having to find $10,000 now versus having to pay several hundred extra each year over the next 25 years is a very different proposition for most. It is not for all: some people do have that sort of cash hanging around and may be able to pay stamp duty outright, but I do not think they are the majority of people in any equitable application of a tax system.

When you are designing something from scratch, would you seriously come in and design it so that you would raise a quarter of all own-source revenue from taxing people who buy a house? If you were designing a tax system from the start, you would not do that. I think everyone agrees with that: that you would not do that and that you would design another system. We do not have the benefit of coming in from scratch, but we do have the benefit, unlike other jurisdictions, of being able to make a transition over a period of time. That is what we have sought to do.

As the Prime Minister said on the *Insiders* program, last year I think, its political difficulty is 11 out of 10. But he, your leader, said that it was the right thing to do. That is interesting. But we will continue. My position on this is not going to change—I am going to surprise you! Having advocated for this for the last seven years, I am not suddenly going to go, “Everything we have done has been wrong.” We are going to continue this policy direction.

As I have indicated previously, we will look to bring new resources to the table to accelerate stamp duty reduction. We have brought such resources to the table in this budget for first homebuyers, and we have continued that approach for pensioners as well. It is up to the committee to make recommendations otherwise, but I presume you are not going to identify—I will be surprised if you are able to identify—two groups who are more worthy of receiving full or significant stamp duty concessions than first homebuyers and pensioners.

MR STEEL: I have a supplementary question. You raised modelling. Have you done some modelling on what, say, a stamp duty cost of $25,000 might be over the lifetime of the mortgage?

Mr Barr: Yes. We can certainly provide the committee with information on stamp duty on borrowings at various levels over various lengths of mortgage repayments. I am happy to do that.

MS ORR: Before I jumped in and interrupted you, you were explaining what stamp duty would have been if we had not started this. Did you have anything to add?

Mr Barr: Yes, I think that not only would we have seen rates revenue increase but if you had just gone back and left all the policy settings where they were in 2011 and just played that through over the last six or seven years then both rates and stamp duty would have increased over that time. Rates would have increased by less. Stamp duty would have increased significantly more. The house price inflation would have just pushed people into higher and higher stamp duty brackets; so they would have been forced to pay more and more stamp duty as house prices increased.

There is no system that seeks to raise the sufficient revenue that the territory needs that is more efficient to us than the broad-based land taxes that are rates and land tax. We do not have a tax line at our disposal that is more efficient, has the least economic impact and is simpler than that mechanism. That it is almost impossible to avoid paying that tax is a source of frustration for those who would seek to arrange their tax affairs in a way that they do not pay tax. There are some who undoubtedly structure their arrangements at the commonwealth, state and local level to achieve that outcome. If they do it within the law, I guess good luck to them. But there are plenty who do not, which is why the Revenue Office is always busy on the compliance side. It is because, unfortunately, there are some people who seek to avoid their legal liabilities in relation to taxation.

But there is not a better form of taxation available to our level of government. I note that when we look at the data in terms of taxation paid in the country at a local government level, at a state level and at a commonwealth level—there are chapters in the budget paper that go to the vertical fiscal imbalance that exists in this country—your average resident pays three to 3½ times as much tax to the Australian government as the average resident pays to the territory government.

Your own commissioned report, the Pegasus report, talks about states and territories taking responsibility for their own revenue raising. We take more responsibility than any other jurisdiction, other than Western Australia, at the moment for raising our own revenue. We do so out of necessity because we receive less from the commonwealth government. We can all have a whinge about that, but that ain't going to change. So we have to take responsibility for this. The Pegasus report talks about this sort of hard revenue challenge, about hard and soft revenue and all the rest. I am sure that I subscribe entirely to that philosophy because I think every little bit of revenue is hard.

As I say, no-one enjoys paying tax. But I have no doubt that at the end of this process, after you have sat here for two weeks, this committee will make a lot of recommendations about areas where we should spend more money. It falls upon this area of government to try to find the fairest, most efficient and simplest way to raise it. They are the philosophical underpinnings of the tax reform process. It is a long-term tax reform that will benefit the person who sits in this chair in 10 to 15 years time.

That will not be me, but I will wear the political pain, as I have over the last seven years, and will continue to do so whilst ever I sit in this role.

MR COE: Are you suggesting you are on the way out, Treasurer?

Mr Barr: Well, I certainly will not be still here in 2030. That would mean I would have had a career in this place of about 25 years, which I think is beyond anyone who has ever been a member of this place. I think the longest has been 20 years. I do not intend to set new records in that regard. But I am here today and I will be back next year. I will tell you that much.

MS CHEYNE: The abolition of the stamp duty applies to whatever property you want to buy, whereas the first home owner grants scheme was more about new properties. Why was that decision taken? I can see some obvious benefits if you want to decide for yourself where you are living. What broader benefits does that have and what was the reasoning behind it?

Mr Barr: There are a variety of competing public policy priorities around where you would direct government subsidy for particular outcomes. There certainly was a rationale around targeting particularly the first home owners grant into new construction in order at that time to provide a stimulus for both the territory economy and new housing construction. We certainly think it achieved that end.

But, as with everything in economics, it is a dismal science. You can get certain positive outcomes and then also have other side effects on a particular policy formulation. In this instance, what it did was to drive construction of a range of new properties but, particularly given of the nature of Canberra's development, into a smaller number of development fronts and housing types. The advantage of this model is that you remove the model of transition. If you remove some of the inflationary impact of the grant, having achieved a level of market stimulation through having the grant, you spread the opportunity for first homebuyers across a range of different locations and property types. That is the advantage.

The policy trade-off here was essentially around how we would bring new resources to the table to fast-track what has been a long-term policy objective: to remove stamp duty. The trade-off with the grant with the stamp duty concession also ends a pretty inefficient arrangement. It was sort of the left hand of government giving someone $7,000 in a grant and then the right hand taking it back in stamp duty. It is a bit of a money merry-go-round. This is a more efficient way of delivering the assistance that we want to give to first homebuyers. It diversifies both the location and property type that the concession applies to. But I think, importantly, it has to be delivered hand in hand with an increase in supply into the marketplace; hence the 17,000 additional dwelling sites.

I note the other major constraint on the supply side, particularly in areas that are close to existing employment centres and that are socially desirable, for whatever reason, for a segment of the market. The other big supply side constraint is planning zoning policies. I understand that is the subject of some further work, both within an Assembly committee and through the planning minister's housing choices work. I would hope for a successful outcome. I would hope that, if it is not bipartisan, then at least a majority of the Assembly will agree on some changes there that will also free up opportunity for new supply in this market segment in locations that are desirable for first homebuyers.

MS CHEYNE: Is that why the abolition of stamp duty for first homebuyers is not coming in until 1 July 2019? Is it intended perhaps to dovetail with some of that housing choices work?

Mr Barr: Certainly, that is a factor, together with—

MS CHEYNE: The land release?

Mr Barr: Yes, together with a transition to ensure that people who had made a series of plans around the existing arrangements were given time either to change their plans or to complete the transaction that they were intending to undertake. That is certainly a lesson that government has learnt over the years in terms of making changes like these—that giving a degree of advance notice can help in managing a transition and undertaking reform, rather than there being a big bang in one moment.

Gradually introducing a change tends to smooth out unanticipated market outcomes. Nevertheless, there is no absolutely perfect scenario whenever you make change. Someone will be unhappy. Some people will be very happy. There are very few reforms that government can introduce that upset no-one.

MS ORR: While we are on the topic of first homebuyers, how many additional first homebuyers will benefit from that abolition of stamp duty?

Mr Barr: I am checking. From memory, it is around 800, actually. We have—

Mr Nicol: Eight hundred.

Mr Barr: We have 800 additional. To put that in context, in the 2016-17 year we had 1,234 first home owner grant recipients and 1,252 homebuyer concession scheme recipients. Some of that could be people who qualified for both. Being able to add another 800 on to that is a pretty significant increase in the number of people that we can assist. It is taking the number from around the 1,200 mark up to 2,000 or thereabouts.

It varies from year to year in terms of the take-up of those programs, but at the moment in 2017-18 there have been about 1,500 first home owner grants and about 1,200 under the homebuyer concession scheme. I think both of those numbers will end up in 2017-18 exceeding the 2016-17 numbers. But it is, yes, a way that we can provide some significant additional assistance.

MS LE COUTEUR: My question is about valuations and how you value for residential rates. As I understand it, our rates are based on unimproved capital value. But of course most sales are for improved capital value because people do improvements. How do you actually calculate your unimproved value? Do you take the market value and subtract improvements?

Mr Nicol: I might ask Mr Salisbury to answer that question.

Mr Salisbury: Maybe I should start right back at the beginning in terms of how we build the rating base. I guess the territory is split up into a series of submarkets. For example, in a new suburb you might have two submarkets within that suburb: say, the houses in the valley and the houses on the hill. They might have broadly different values because some have got aspect and some do not. Typically when those blocks are sold, those values come into the rating network, as we spoke about earlier, and what we use from year to year is a mass appraisal process.

We choose a benchmark property in that subsector and we look at the movements in that subsector and then we look at how that property may have moved compared to what else has moved in that subsector. We then work out the difference in that value from year to year and apply that percentage increase across the whole subsector. We do that for every subsector in the ACT and that is what forms the basis of the rating for unimproved values from year to year.

THE CHAIR: How many subsectors are there?

Mr Salisbury: There would be over a hundred subsectors. I do not have the exact number with me.

MS LE COUTEUR: Where you would have particular difficulty is if the whole subsector does not move in the same direction. An easy example would be that with the light rail there is going to be a difference in movement if you are near a stop or not near a stop. When the inner north was built you certainly did not know where the light rail stops were going to be. Presumably that is not reflected in your subsectors?

Mr Salisbury: Where the relativities within a subsector get out of alignment, then we will go and have a look at that subsector as a zero base sort of approach. We will go and look at every single property and go through that process all over again. We will move away from the historical values and we will look at the new values and a new way to base that subsector, and we might even consider breaking that into a couple of subsectors for valuation purposes.

MS LE COUTEUR: When you are looking at redoing a subsector you will look at the market value and try and break it into capital value and improvements?

Mr Salisbury: Yes. Rather than using that mass appraisal process, which is a series of averaging calculations, we will try and do it property by property to get a sense of how a particular property has moved in the market, to rebase it.

MS LE COUTEUR: You basically do not really use the huge database that has been accumulated of sales of properties because they have got the market—

Mr Salisbury: We will, to establish the benchmark property, look at sales within that subsector to establish the benchmark value for that benchmark property and then we will adjust all the other properties based on the increase or decrease in that benchmark property.

MS LE COUTEUR: And that benchmark property would just be an average of a number of properties? Otherwise you have a situation such as: “I was living in the benchmark property but I decided to put a big extension on and when I sold it next year it was worth a lot more. That had nothing to do with the unimproved capital value; it had to do with the extensions I put on”.

Mr Salisbury: We look at the improved values, then we would deduct the improvements from that to find the unimproved value, to determine the unimproved value of it.

MS LE COUTEUR: The other thing that struck me is that obviously we have had a large sale of Mr Fluffy blocks and, anecdotally, in the inner north they have sold for way more than the reserve, whereas clearly there are also blocks that are still for sale in the outer suburbs. This would appear to me to be a market test of unimproved capital value because basically you removed the improvements in the Mr Fluffy blocks. How is this going to impact on our rateable values? This would seem to be significant. We have a thousand or so block market tests.

Mr Salisbury: In terms of the benchmark properties, in the subgroup the Mr Fluffy sales would be one of a number of sales that will be taken into account when we determine the benchmark valuation. Mr Fluffy properties might be one of a number of transactions that have happened in that particular subset, and that will be taken into account.

The thing about Mr Fluffy properties is that they are discounted by a scarcity factor as well, because they are generally unique properties because they are unimproved. There is a scarcity element and people often will pay a premium because there is a Mr Fluffy block which is levelled and ready to build on and it is generally, particularly in the inner north, a desirable location. There will be a premium that people will be prepared to pay for that vacant, cleared block and we will make an adjustment back so that the overall increases do not get out of alignment.

MS LE COUTEUR: I am obviously not totally understanding this, but you are basically saying there is a premium for getting an unimproved Mr Fluffy block—

Mr Nichol: In an existing urban area.

MS LE COUTEUR: All the rateable properties pretty much by definition are in existing urban areas. There are rural properties we pay rates on but—

Mr Nichol: I am comparing it to a new, greenfield suburb. There is a difference in values, we have noticed. I think the big difference is when people are looking at an established suburb and they are looking at the difference between buying a clean block and a block with a house on it. When you purchase that property with the house on it, it is a 30, 40, 50, 60, 70-year-old house, which you are paying something for in your market price. The market seems willing to pay more for a flat block where people can start again without having the overhead of that old property on the block.

MS LE COUTEUR: What I am saying is that, to someone with a very little brain, what they are paying for is the unimproved capital value when buying Mr Fluffy blocks, because that is what you get. What you are arguing—and I am sure it is true in some cases; I have certainly been told it is true—is that in some cases your block of land is worth less because it has improvements, so you will sell it for less than the unimproved capital value because the improvements are not wanted by a subsequent purchaser.

Mr Nicol: It is, I think, for two reasons: one, as Mr Salisbury said, there is a scarcity value. There are not too many cleared blocks in these established suburbs and we think the prices would be different if theoretically every block in a suburb was sold en masse. Secondly, people can, if they are avoiding the cost of buying an older house on a property, afford to spend more on the land to start again if someone is really looking to knock down and rebuild.

MS LE COUTEUR: There is always a scarcity value. Basically, in established suburbs all the houses are different and unique. From that point of view they all have a scarcity value of some sort. I cannot really see that the sales of the Mr Fluffy blocks are not reasonably representative of, in fact, the unimproved capital value, which I suppose I have not really grasped. Yes, they have a scarcity value but there is a scarcity value with all real estate.

Mr Nicol: I think the evidence that I have seen suggests that in some locations, not in all, even if you compare the prices that some of the Mr Fluffy blocks are going for—perhaps I should be careful about saying this too loudly—in terms of their relative price to someone buying an existing house and demolishing it and starting with a clean block, people are paying more for the Mr Fluffy vacant blocks straight off the bat.

MR COE: I guess the point is that in a year's time or two years time there are going to be two houses next to each other. One was a Mr Fluffy block and it has got a house on it. The other was not a Mr Fluffy block and has a house on it. They could have totally different valuations, could they not?

Mr Nicol: No. What Mr Salisbury is saying is that we normalise those. That is the process, to the extent that the blocks are comparable.

MS LE COUTEUR: Assuming the two blocks are comparable, the unimproved capital value of the house next door, which did not have a Mr Fluffy on it, will go up a bit, and the Mr Fluffy one, which sold for $800,000—whatever it was sold for—will have its unimproved capital value reduced to—

MR COE: $500,000 or $600,000.

MS LE COUTEUR: $500,000 or $600,000, and the one next door will go up from $450,000 to $500,000—is that what you are saying is going to happen?

Mr Nicol: Mr Salisbury can comment further but they will be, in the medium to long term, comparable in terms of rating unimproved values, if they are similar comparable blocks, no matter what they have been sold for in the past.

Mr Barr: And the examples you have used are very extreme indeed.

MR COE: No, not in Curtin or Deakin. In the Weston Creek suburbs you will have AUVs around the $350,000 mark, and then a block of land selling north of $350,000.

MS LE COUTEUR: This is one of the things that have been particularly hard for the people trying to buy back. They were given what seemed a quite reasonable price and told that they would be able to get it back for a bit less, around the unimproved capital value. This is only a minor point. I am really more concerned about what is going to happen in the long run with the valuations. If we are using unimproved capital value, then we have done the experiment and we have got a 1,000-block experiment. I cannot quite see how it does not—

THE CHAIR: That is a pretty reasonable sample size of what an empty block in Canberra is now worth, particularly in the inner suburbs. Surely that is going to have some impact on unimproved values for the remaining properties? It is not one or two empty blocks; it is—

Mr Nicol: It will to the extent of the proportion of the blocks that are sold. If there was a very desirable property with a very desirable aspect, and our grouping submarket analysis did not take that into account and someone paid over the odds for a particular property in a market—whether it was a Mr Fluffy or not; let us suppose it was not—we would not automatically assume that every other block in that submarket would go up by the same price. We are looking at a number of sales in the submarket to ensure that it is a representative increase.

Mr Barr: There would be somewhere between 12 and 15 times that volume of properties transacting every year. There is a much larger pool of data that is available to the Revenue Office. Whilst a sample of 1,000 is not insignificant, over the five-year time frame there will be 80 times that number of transactions occurring in the property market.

MR COE: Not for vacant blocks.

MS LE COUTEUR: But not of vacant land. And given that our system is currently based on—

Mr Barr: On vacant land, it will not be 80 times but it will certainly be a significant number more—but not always in the same locations, no. There is a whole lot of data coming into the system, I think is the important point to acknowledge here. If the line of questioning is suggesting that somehow Mr Fluffy sales are going to massively distort the underlying value—and that has certainly been asserted by others previously—that is not the case.

MS LE COUTEUR: I am concerned not that they are distorting it but that they are in fact really revealing that, if you look at unimproved capital values, we have not got them right and we are underestimating—

Mr Nicol: I do not think we are. I would only make the point that every property that is bought and sold has an underlying unimproved value as well. You should not just look at one type of sale to determine the unimproved value. A property with a house on it does have an unimproved value and an improved value.

THE CHAIR: But obviously the clearest measure of what the market is willing to bear as far as an unimproved value goes is a clear, vacant block of land.

Mr Nicol: I think what we were saying was that actually people are paying a premium for it, for whatever reason.

THE CHAIR: The fact that a number of properties are not achieving the reserve price would suggest that either the government are seeking to profit from this by setting a reserve price well above the unimproved value or they are not doing that.

Mr Nicol: I might ask Mr Miners to come up; he is on the committee that is overseeing the process. My understanding is that our clearance rates are on a par with what you would expect in the private market for auctions. That is a good thing; it suggests we are setting the reserves relatively well.

Mr Miners: The clearance rates we were getting at the initial auctions were around 50 per cent, which is pretty much what was anticipated at the time. That would suggest that we are pretty much in the ballpark with those prices. Subsequent to that, they go for sale over the counter, and they are then clearing. In a lot of cases, those properties have been clearing in one or two days after the auction, because people have come in and negotiated and accepted the reserve price.

I think the clearances we are getting are very good. Now we have sold getting up towards 600 properties, so there is not really a problem moving them on. The rest are coming through the process. In particular, some of that process has been delayed as you go through the first right of refusal; those properties would be sold either through the first right of refusal to the original owner or come onto the market for sale.

THE CHAIR: What proportion have been sold through the first right of refusal?

Mr Miners: It is very low.

Mr Nicol: It is under 100, I think.

Mr Miners: Yes.

Mr Nicol: We will pull that figure up.

Mr Miners: I have that data here.

MS LE COUTEUR: Would you be able to take on notice, for each suburb, the average of the unimproved capital value and the average that the blocks are being sold for?

Mr Nicol: Yes, we can do that.

MS LE COUTEUR: I want to get some idea of the relativities.

Mr Nicol: We can do that, yes.

MS LE COUTEUR: Thank you.

THE CHAIR: We will wait for that figure, and then we will move on.

Mr Miners: I will get that.

THE CHAIR: We will come back to it.

Ms LEE: I would like to change tack and ask a few questions about CTP. I do not know if you need to change any personnel.

Mr Nicol: Yes, we can do that.

MS LEE: How is the CTP regulator preparing for the implementation of the new scheme? What is their involvement in assisting to implement the scheme?

Ms Vroombout: The CTP regulator is assisting those who are developing the legislation with knowledge of how the existing scheme works and levering the contacts that we have as the CTP regulator with other jurisdictions who have implemented similar schemes. New South Wales, in particular, has recently implemented a similar sort of hybrid scheme.

MS LEE: Is the New South Wales legislation something that the regulator is looking at for our legislation?

Ms Vroombout: Not the regulator per se, but those who are—

MS LEE: Working on it?

Ms Vroombout: Those who are working on it, yes. The scheme is different from the one that is being implemented in the ACT, but it has some similarities. Some of the things that New South Wales have done in their legislation are useful points of comparison to look at. The CTP regulator is also helping with the design of the new ICT scheme required for the new scheme.

MS LEE: What are the priorities for the regulator in administering the scheme?

Ms Vroombout: The first one is assisting with the development of the legislation and the ICT system for the new scheme. More generally, other key priorities are working with the National Transport Commission and other CTP regulators around how CTP schemes deal with autonomous vehicles; working with peer-to-peer car-sharing companies that want to enter the ACT market; monitoring and reviewing a streamlined CTP premium filing process; continuing to monitor the scheme's performance; and contributing to targeted road safety initiatives. They are the six key priorities for the CTP regulator for 2018-19.

MS LEE: How will including at-fault claimants affect the cost of the scheme in the long run?

Ms Vroombout: The cost of the scheme or the regulator?

MS LEE: The scheme.

Ms Holmes: You are talking about the new proposed scheme which is being worked through?

MS LEE: Yes.

Ms Holmes: The scheme which was the chosen scheme by the jury has a number of elements. Yes, it is bringing in at-fault claimants, but there are also a number of other changes. It is substantially a totally different scheme. The chosen scheme, with all of the factors combined, means that there is likely to be a decrease in the premium on average to about $130, but ultimately it will depend on the detail. What went to the jury—

MS LEE: That is a decrease in premiums, isn't it?

Ms Holmes: Premiums, yes. Ultimately, the detail which went to the citizens jury and what they selected had the key principles, but as we work through legislation and as we go into the finer detail we will have to get it costed again. Whilst the $130 is the average and was the best information at that point in time, it will be refined as the legislation is worked through.

MS LEE: What was the regulator's involvement in the alternative schemes that were presented to the citizens jury?

Ms Holmes: The way the citizens jury worked was that the citizens jury, at the end of the second weekend, came out with the report which specified what their objectives were for an approved CTP scheme to best balance all road users. Based on those six objectives that they set, the stakeholder reference group then came into play. There was a scheme designer, a scheme actuary and other members of the stakeholder reference group. They then came up with a number of models which met the objectives set by the jury. That went back to the jury. They then selected their preferred scheme.

MS LEE: Prior to the citizens jury, did the regulator ever consult with or seek some advice from an actuary or any other designer about the current ACT scheme or other alternates?

Ms Holmes: In what sense?

MS LEE: Prior to going out before the citizens jury, did they end up doing other consultations with actuaries or other scheme designers?

Ms Holmes: On an alternative model? No, we did not.

Mr Nicol: I would say that as part of our annual reporting we do engage actuaries to describe the cost drivers of the current scheme as part of our statutory reporting responsibilities.

MS LEE: But there was nothing beyond that in terms of—

Mr Nicol: No. Not since the previous occasion the government debated CTP reform in the Assembly. How long ago was that? Six years?

Ms Holmes: It was 2011-12, I believe.

MS LEE: Why was that? Just because you did not have that policy direction?

Mr Nicol: Principally, yes. We did not have any indication from government at that point to undertake that sort of work. In terms of my own responsibilities, it would have been a costly exercise to engage actuaries for these sorts of things. You would only do it with some substantive suggestion that the government was looking to undertake some policy reform in any area, let alone this one.

MS ORR: Putting aside the new scheme because it is still in the future, how have CTP prices been up to date? What is the trend with CMOs?

Ms Holmes: Our prices specifically or premiums?

MS ORR: Premiums.

Ms Holmes: We have had a general trend since competition started in 2013 for the premiums to be reduced. I think they have been reducing on average since 2015. Compared to other jurisdictions we are one of the higher premiums.

MS ORR: Are you finding that that is flattening out or is it still decreasing?

Ms Holmes: The sorts of changes we are seeing when premiums are going down are small—less than $5.

Mr Nicol: I think the answer is yes. The competitors tested each other because they had to file premiums and go through an assessment process, and they found their level a little bit. With the subsequent announcement of price cuts and premium cuts you would get a response, and that response is getting smaller. It appears we are getting to a stage—it depends on underlying trends in accident rates and costs—where the premium has by and large settled.

Ms Holmes: When insurers do premium filings, or a request for the premiums, the role of the CTP regulator is to essentially do two tests: to look to see whether the premium they are requesting is fully funding what is expected in terms of claims and to see that those premiums are not excessive. An independent actuary looks at those elements for us and provides a report to us. On that basis it is the decision of the CTP regulator to accept or reject the premium.

Largely what drives the premiums is two factors: the number of claims coming through and the average costs of those claims. The insurers do not have the ability to set any premium they want; essentially it has to meet those two tests. As Mr Nicol indicated, they are finding a little bit of room at the moment, but there is not much. As I said, the actual cost of the scheme is what drives what the premiums are.

Mr Nicol: I agree with Ms Holmes. There is price competition between retailers and a bit of a retail margin there. We have eliminated that from the system with the introduction of competition. There are the cost drivers that Ms Holmes talked about in terms of the number of claims, average claim costs and those sorts of things, and the citizens jury went to those factors.

The third factor, which is probably outside our control, is the state of the general insurance market around the world—the cost of capital, how tight it is and so on. Those sorts of things are outside of our control. We can only control it to those two other factors. The competition was addressing the first one and the citizens jury is now going to the second.

MS ORR: Going back to the rates transitions, quite a bit has been made of the change to the unit calculation. Prior to this change, how had rates increases compared for houses and units?

Mr Nicol: Previously the methodology for calculating rates on any property was to get the unimproved value of the entire block. If the block had more than one property on it, more than one unit title on it, the value was divided into unit titles according to the unit titling methodology for any strata title body corporate. The ratings factors were then applied to those values. By and large, units had a significantly lower value than houses, which is appropriate.

Tax reform has also involved a rating system where rates increase as property values increase. That meant that houses which had higher unimproved values had higher rate increases than units which were lower value properties. In fact, we were at risk of having a situation where for a block that previously had one or two units on it and then had more units put on it the rates take went down because of the interaction of the two effects. That is how it works in theory. As to the numbers, do you guys have those on hand?

Ms Goth: It is hard to have an average number. If I understand the question correctly, it is about how average rates for units have changed since before the change in the calculation methodology to after. The change was driven by a review of the first stage of tax reform that was done after the first five years of tax reform to look at how the increases have played out across the board.

As a result of that review it was obvious that houses, on average having higher AUVs, were increasing at a much higher rate than units. Every unit was in the lowest category because of the reasons Mr Nicol explained. The increase now means that rates for units are increasing on average at a similar level to houses. Prior to the change in calculation methodology they were much lower than the average increase across the board for all residential properties.

Under the current methodology houses still increase at a higher rate than units in general, but the increase for units is much more on par with the average. So we are bringing units back up to be more on par with houses, but they are still significantly lower. We need to talk in averages because a lot of things feed into different AUVs, as we discussed earlier. It is hard to talk about a particular property, but we talk in general terms.

MS ORR: That is what I was getting to. Were houses doing a bit more of the tax burden work than units were under the old calculation. Is that a fair assessment?

Mr Nicol: That is a fair summation.

MS ORR: So the way it has been changed now is to capture much more equitably or fairly, or whatever word you want to use, the value of the land each property is sitting on?

Mr Nicol: I think there are two reasons, and that was first reason. The second reason was that as the government moves to increase densities we are going to have a lot more situations where the detached house will become a lower proportion of our housing types. We wanted a tax system that was sustainable so that, as we increased other denser housing types, the tax base was robust enough to continue to provide a revenue source that would provide the services that we need to provide for all residents.

MS ORR: As part of the broader discussion about this change, we have heard quite a lot of people—particularly people on fixed incomes, older Canberrans—talking about the cost of living. What are we doing through this budget to assist with that, particularly going to the unit and house rates?

Mr Barr: A range of concession and deferral schemes are in place. This budget has extended the eligibility to enter the deferral schemes.

Ms Vroombout: A general rates rebate will continue to apply, and that is $700 per annum. As the Chief Minister noted, the general rates age deferral scheme has been expanded in this budget by removing both the income and unimproved land value thresholds, which will mean it is available to many more older Canberrans.

MS ORR: Do you know what share of pensioners are on a full pension compared to a part pension? That goes to the eligibility, does it not?

Ms Vroombout: Both full and part pensioners are entitled to the concessions. I think around 40 per cent of all pensioners in the ACT are full pensioners and the other 60 per cent are part pensioners. But the concessions are available to both full and part pensioners.

MS LEE: On Friday we heard evidence from the Owners Corporation Network, and an economist who was giving some evidence was making comments about how with rates going up for units it makes it a very unattractive investment option in Canberra. That is one comment. The second is that the Pegasus report cites a discussion from the Housing Industry Association which has warned that the ACT government's policy to phase out stamp duty and replace it with rates will reach a point where residents of the ACT will seek relief from those increases by relocating to New South Wales. As the Minister for Economic Development and the Chief Minister for the ACT, does that concern you?

Mr Barr: If those dire predictions were to be realised and some people did move then that would be regrettable. However, it would be an extraordinarily irrational financial decision to do that, given the prevailing transactional costs associated with such a move. If you were to move to New South Wales, you would be paying stamp duty in New South Wales.

MS LEE: Yes, and that is exactly what Pegasus brought up in our briefing—that people would rather pay that one off and then be free from the rates.

Mr Barr: Sure. You would have to do a financial calculation of the fiscal cost of selling your property. What is the average real estate agent fee? It would $10,000 at least, and then you add the stamp duty you would pay in New South Wales, so that is probably another $25,000 to $50,000. So you are up to $35,000 to $60,000 before you have accounted for your moving costs. So you are up to about $70,000 now. You would have to be expecting to live for a very long time in order to be financially ahead as a result of the difference between rates in the ACT and those across the border compared to a transaction cost of somewhere between $50,000 and $70,000.

MS LEE: So if people are making those decisions it brings in to stark reality the rates increases.

Mr Barr: If anyone did it for financial reasons, they would probably be expecting to live well into their 100s in order to be financially better off. And if they were borrowing to pay for their stamp duty obligation on moving into New South Wales, that would also feed in to their annual costs. But not everyone is rational, Ms Lee.

MS LEE: As we all know.

Mr Barr: A rational person, particularly of a certain age, would take the duty deferral and the capital growth on their asset and have no outgoing costs and end up ahead. But some people will not do that. I absolutely guarantee that that would be the very first thing I would do, were I to reach that age and have that opportunity. It would be the most efficient and sensible and rational thing that you could do. But not everyone will do that, and I acknowledge that.

Can you design public policy to account for irrational decision-making? You can try, but it is pretty hard. It is not impossible, but it is hard. Some things are decisions of the heart; you are right. If people felt that strongly about the situation then we would certainly look to provide some counterarguments in terms of a conversation that could be had and show them the range of different options in front of them, rather than incurring all of that expense. I have only talked about the financial expense and not the dislocation that would come emotionally. Moving house is one of the more traumatic experiences in people's lives. I have done it a few times—it is a big and onerous task. I would not undertake it lightly, and I know most people do not.

But, in light of all that, if people were still determined to move because they felt that the few hundred dollars a year they would save in rates between this side of the border and another jurisdiction was worth it I would then encourage them to look at the other things they might value in their life. They might want high quality health services if they are of a certain age. They might want proximity to a range of social and community facilities that they may not have as readily in another jurisdiction.

Some people will leave Canberra because they do not like cold days like today; others will leave Canberra because they want to live closer to a beach; others will leave Canberra because their careers or family reasons might take them to other parts of the country. It would be difficult develop a tax system that takes into account all of the different factors that drive people's decision. It is clear that the transaction costs associated with moving are significant—stamp duties in other jurisdictions, real estate agent fees, the physical cost of a removalist or your own time in packing up everything and moving. I do not think it is something that is done on a whim.

THE CHAIR: On a commercial side though, Treasurer, it is clearly not the case where the rates are considerably higher this side of the border than they are on the other. As you put it, the inherent costs of transitioning from a commercial property on this side of the border to the other side of the border over a matter of four or five years can necessarily pay for itself.

Mr Barr: Except that there are land taxes on the other side of the border as well, for commercial, that we do not charge.

THE CHAIR: There are here.

Mr Barr: No, we have one payout.

THE CHAIR: You have exorbitant rates. Land tax and rates were combined.

Mr Barr: That is correct.

THE CHAIR: And they have exponentially increased since.

Mr Barr: That was done to simplify the system, and stamp duty has been significantly reduced. Again, you have a situation where a firm would have to make a decision based on the costs of acquiring new property. There would be a transaction tax on that unless they are moving to South Australia, which has similarly sought to remove taxes on commercial property transactions.

THE CHAIR: Ultimately you are relying on people doing maths and saying, "Look, we'll cop the hit here on the continual increases because it is prohibitively expensive to leave the jurisdiction."

Mr Barr: I assume that businesses would look at rates, payroll taxes and the absence of insurance taxes in this jurisdiction, which they would be paying if they were across the border. They would look at the total series of taxes. They would look at the availability of skilled labour, sources of capital as well as the underlying—

THE CHAIR: Cost of workers comp remits.

Mr Barr: That would be a factor too, as well as the underlying market conditions. It is going to be very difficult to be—

MR COE: Is it not the same market, the same access to labour, the same access to capital, if you are in Queanbeyan?

Mr Barr: If you are in Queanbeyan possibly, but not everyone would want to work in Queanbeyan who would work in Canberra. I do not know that many people who would say, “Right. I’m so attracted to the Queanbeyan lifestyle that I’m gonna go and work there as well.” There might be some. But there are also people who want to work and live in Canberra. The employees will say, “Well, where do I live and what are my transport costs?” That is a factor. If this massive move were on, then we would not have 2,000 additional businesses in the ACT. Our economy would be in reverse and Queanbeyan would be the boomtown of all boomtowns. It is not and that is not what has happened.

The real-life experience is that business is growing in the ACT. The number of businesses and the profits and revenue for businesses are increasing. Our population is increasing. In the end we can have all the doomsday speculation we want from various commentators, but it will be the real lived experience that will ultimately be what happens.

We have six years of experience now. We have seen it. If I had listened to this sort of commentary six years ago, where we would we be now? We would have thousands of fewer businesses operating in the territory. Our population would have gone backwards. Our economy would be smaller. None of that has happened in the first six years, and we are now into year seven of this reform.

If, all of a sudden, all the gains of the last seven years were reversed in the next seven years, that might present an argument for the government of the day to change course. But none of this has transpired. None of the doomsday scenarios have transpired to date. If it did happen then you would reassess. But it has not happened. In fact, it has gone the other way.

MS LE COUTEUR: My supplementary is about the rates deferrals. How would people know about them? I asked a question on notice probably about a year ago. At that time there had been only two age-based deferrals. How would people know about it? Have you ever sent out information to people who might be eligible? People on rates concessions might also be interested in deferrals.

Mr Salisbury: Information on the rates deferral is up on our website. Mostly when people contact the Revenue Office and they have a problem paying rates, that is the time when we raise the issue with them about the possibility of moving onto a rates deferral.

MS LE COUTEUR: Could I ask you to do a bit more education of your staff?

Mr Salisbury: Sure, yes.

MS LE COUTEUR: Because I have sent constituents in that direction and not had that result.

Mr Salisbury: Fair point. Absolutely. We might look to put something out in the rates notices.

MS LE COUTEUR: They were actually told the opposite.

Mr Salisbury: I will get advice on putting out information in the rates notices this year.

MS LE COUTEUR: Not everybody spends all their time looking at your website. I appreciate that if they were economically rational, Mr Barr, they would!

Mr Barr: That is a point well made. I accept that the interest in the revenue website would probably peak in this building and then move down. For those who have a need to access that information, it is there. But, yes, we can certainly do more in relation to promoting the availability of these particular schemes.

MS LE COUTEUR: Thank you.

Mr Barr: They have existed in the past. They will, I think, continue to exist in the future. And they should. Yes, it is possibly the most rational decision that you could make to do that.

Mr Salisbury: Can I jump in and recommend the ACT revenue website. It has recently had a revamp and a relaunch, and it is much more user-friendly than it once was.

MS ORR: I go back to the pensioners and the discounts. You said that everyone, whether they are on a full pension or on a part pension, is eligible for the discounts. Do they get the same amount of discount or is it pro rata?

Ms Vroombout: It is not pro rata, so they get the same amount.

MS ORR: If you are a pensioner, full or part-time, you are getting the full discount on it?

Ms Vroombout: Yes.

MS ORR: Okay, thank you. That is all I wanted to know.

MR STEEL: I was just going to suggest, rather than ask a question, that cameos be made available on the rates deferral so that people can get a better understanding of it, particularly with their increasing house prices.

Mr Barr: Yes.

Mr Salisbury: Yes, we can look at doing that.

MR STEEL: My question is on land tax. Who pays land tax, currently?

Mr Salisbury: Currently, where a property is rented, land tax applies to that property.

Mr Nicol: Residential.

Mr Salisbury: Residential.

THE CHAIR: Or if it is owned by a non-individual.

MR STEEL: Does that currently apply to commercial property?

Mr Salisbury: Residential properties.

Mr Barr: Yes, we abolished commercial land tax and rolled that into single rates.

THE CHAIR: It is not abolished; you combined it. Be transparent, please, Treasurer.

Mr Barr: Land tax was abolished. The revenue was rolled into the rates system in order to simplify it. That was, at that time, a request from the business community to simplify taxation arrangements with government so that they got one bill, not two. We accepted that recommendation at that time, to combine the two into one. That has not stopped some pretty gratuitous—

MR COE: Massive efficiency!

Mr Barr: From an administration side and from the business side, it meant one stream.

MR COE: I am sure many businesses are very grateful for that.

Mr Barr: I am not suggesting that it is the single greatest red tape reduction item in the history of the world, but it is not a bad thing. Surely you are not arguing we should go back to having two bills and two administrative systems?

THE CHAIR: Go back to the same rate; I think the business community would be welcoming it.

MR COE: Absolutely.

Mr Barr: Will we put all the stamp duties back up again? Is that where we are going?

MR COE: If somebody had already bought their business and bought their premises, and you did not grandfather it, exactly as Ted Quinlan said—

Mr Barr: That is one more view. If the committee wants to recommend that, the committee can recommend that.

MS ORR: What would happen if land tax were reduced? What would that mean for the services?

Mr Barr: Sorry, what if—

MS ORR: We have heard that services come from the revenue raised.

Mr Barr: Yes, this obviously is the substantive issue for people once they move beyond the immediate reflex, "Lower taxes; that is fantastic." What does that then mean? It means that other tax lines go up. Yes, we have had this debate. We have reduced certain tax lines, some of them to zero, and shifted our revenue base on to a more sustainable footing.

Yes, we could have a different debate about which taxes go up and down; or you can cut $500 million of expenditure out of the budget. That is essentially the long-term vision that was outlined by my opponent. It was to do that, or you run a budget deficit each year starting at $500 million. They are the options. You have to increase other tax lines, you reduce expenditure, you run deficits or you do some combination of the three. That is the only possible outcome of such an objective.

I am all for a good debate about the size of government, whether we ought to have a bigger government or a smaller government. We are always going to err on the side of a bigger role for government in the community. I do not think there is any doubt about that. That is not a contest, clearly. We will always deliver more health services, more education services, more community services, more public transport, more investment in the community than the other side of politics.

MR COE: Well, you will spend more.

Mr Barr: That is certainly the case. That has always been the case and presumably always will be. That is sort of business as usual. My reason for being in government is not to make government smaller and for it to do less. I do not hate the institution that I am part of. I actually value it and think it makes a difference to our lives. It makes for a better community. That is why we are here. I find absurd: people who run for office because they hate government and want to make it smaller and do less. That is a pretty woeful motivation to be involved in politics. But, anyway, there are some people like that. Good luck to them!

MS ORR: A lot of costs for business become tax deductible. Just out of interest, is there a tax deduction option on land tax for people who derive income from owning a property?

Mr Barr: Yes, that is right.

MS LE COUTEUR: You mentioned that it was very much more efficient commercially to have land tax and rates as one charge. Are you considering moving that efficiency into the residential sector?

Mr Barr: I guess there is a difference there in relation to—

Mr Nicol: Some properties being rented and some not.

Mr Barr: Yes.

MS LE COUTEUR: Yes.

Mr Nicol: So you would have to have two systems if you—

MS LE COUTEUR: It is just that, given what the Treasurer said, that was potentially the logical conclusion.

Mr Barr: Yes, but in this instance the difference is that all businesses previously paid rates and commercial land tax. It is not the situation in the residential sector that all pay both. That is the difference.

Mr Nicol: Assuming you maintained your current policy settings of having a land tax equivalent payment, you would either have a rates system for everyone and then a land tax system for renters, or you would have a rates system for everyone that had different rating factors for those who tended to rent their properties. It could actually get more complex doing it that way than having a separate tax one.

MR COE: I would like to go to the lease variation charge. I am wondering whether you are able to give an explanation as to why it is not bringing in the revenue that you expected it would.

Mr Barr: This year, not a particularly large number of large transactions. A range of concessions, rebates and the like have been applied.

MR COE: What does that tell you, either about the policy or about building activity?

Mr Barr: What that says is that we have been quite generous in some concessions in relation to the lease variation charge and that in this particular fiscal year certain large transactions did not occur. In other years they have. It will vary from year to year. But the fundamental principle of an unearned windfall gain not being taxed is not one that I am comfortable with. My view is that if a stroke of a pen increases the value of land so significantly then it is fair for the community to share in some of that value uplift.

If people do not believe that there is a value uplift, the only way to test that would be for the government to resume land for its current purpose, rezone it for a higher purpose and then sell it again. I guarantee you that there will be a difference between the before and after value if you allow for more development under the lease. If you do not believe in those principles of taxing and unearned windfall gain, that is fine. But this debate is the same debate we have had for the last seven years.

MR COE: Why were you generous, in your words, to give people concessions on this?

Mr Barr: We have done so historically around certain stimulus activities. We have done so to achieve higher environmental outcomes, and we have done so to achieve certain community and social outcomes.

MR COE: Is that generous or just applying the policy?

Mr Barr: The policy was generous in terms of giving concessions for those outcomes.

You could equally have determined not to or to have not given them at the levels that they were given. There will be a variety of views in the community, from one extreme, which is to give no concessions at all, to what I interpret is your line of argument: that no tax should be paid at all to vary a lease. Are you arguing that there should be no charges at all?

MR COE: Which ones in the last financial year have you been generous to—which developments?

Mr Barr: In the last financial year, the policy settings have included the tail end of an economic stimulus, environmental concessions and some for social purposes.

MR COE: But which projects have received—

Mr Barr: It is not project-specific. It was either a general stimulus remission or it related to certain environmental outcomes or certain social outcomes. It was not project—

MR COE: Which projects or developments were captured by this policy setting?

Mr Nicol: We could produce a list.

Mr Barr: Yes, that is—

MR COE: If you can produce a list and the number of—

Mr Nicol: I mean, subject to individual taxpayer privacy.

Mr Barr: I do not know because they are not set by individual project; they are set by certain outcomes. They apply to everyone via the stimulus measures or they apply for certain environmental performance benchmarks by a VAT remission instrument or they related, for example, to childcare centres and other social outcomes that, effectively, we were prepared to have the taxpayer subsidise to achieve that outcome. We can provide a breakdown within those different categories of how many remissions were utilised.

MR COE: And the value thereof.

Mr Barr: And the value, sure.

MR COE: Great. With regard to how the Revenue Office calculates these, does the Revenue Office actively keep an eye on lease variations, is it up to the property owner to report what variation has taken place or does the planning directorate automatically tell you?

Mr Nicol: The planning directorate, because obviously they have to approve a planning lease variation and then—

MR COE: And that has always been the case, that all notifications from the planning office for lease variations have been sent through to the Revenue Office?

Mr Salisbury: The Revenue Office gets notifications of lease variations from two sources within government. One is from the planning directorate and one is from the Land Titles Office. They are the formal mechanisms by which we get an indication of a lease change.

MR COE: Does that automatically trigger a revenue assessment by your office?

Mr Salisbury: What it will do will adjust or cause us to consider the unimproved value of that property.

MR COE: In instances where the Revenue Office has contacted lessees and said, “Actually, you had a lease variation several years ago; therefore you are going to get a backdated invoice,” why didn’t your systems pick that up at the time?

Mr Salisbury: From time to time a lease variation may go through that our systems do not pick up. That can be either system error or human error. We would look to rectify that by ensuring that the appropriate unimproved value applied to that property.

MR COE: Is there an onus on the property owner to notify the Revenue Office of a lease variation?

Mr Salisbury: I believe the court, in an ACAT matter, recently concluded that there was an obligation on the taxpayer to advise the Revenue Office.

THE CHAIR: How do they do that? What is the form they fill out?

Mr Salisbury: There is no form to fill out as such. It would be making contact with the Revenue Office if they had that declaration to make.

THE CHAIR: What other charges require someone to say, “Hang on, my circumstances have changed,” and opt in when it is a complete unknown? The land tax is a threshold question. Is it rented? They get the bill automatically.

Mr Barr: They have to tell us; they do not. What you just said there is not correct.

THE CHAIR: Sorry, they do not? My apologies. Okay; forget that. But this is a fairly substantial one. I guess the better question is: in how many instances does the Revenue Office believe that the change of purpose or the lease variation has not been applied to the unimproved value and the rates have not been charged at the right level?

Mr Salisbury: With any unimproved value that was affected by a lease variation, we would attempt to find that and make changes to it as appropriate.

THE CHAIR: Do you think it is appropriate that, for maladministration on the part of government, the private sector or the property holder has to carry the financial burden when you finally catch up with your maladministration?

Mr Salisbury: It really goes to an issue of tax administration. If different facts come forward, you would expect that the tax administration would ensure that the assessment or the unimproved value is correct. As new facts come forward, you would expect that the tax administration would catch up and ensure that tax is applied equally to everybody.

THE CHAIR: But don't you think that the government should accept some responsibility for maladministration? To refer to the case that you mentioned before that has recently been through the tribunal, a property holder got a retrospective rates adjustment notice of in excess of half a million dollars, to adjust five years or six years worth of rates simply because one arm of the government did not talk to the other? Half a million dollars!

For the benefit of other committee members, on commercial rental leasing terms, typically some of those on-costs are passed on to the tenant. It is a fairly punitive response from government to say, "We have stuffed up. Here is a half a million dollar bill," and completely disregard what other commercial arrangements may have been in place previously.

Mr Salisbury: I think the ACAT examined all those issues in some detail and concluded that the assessment had been made in accordance with the law.

THE CHAIR: How many more cases like this exist?

Mr Salisbury: I hope there are no more cases like this.

THE CHAIR: Are there any currently, other than the one that is being discussed, that the Revenue Office is currently seeking retrospective rates on?

Mr Salisbury: Not that I am aware of, no.

Mr Barr: During the break, chair, I might ask that you reflect upon the use of the word "maladministration". I do not think you meant it to mean what it actually means. Just look it up, have a look what it means, and reflect on whether that is what you meant when you accused the officials of that.

THE CHAIR: For clarity, there are obviously administrative processes in place, as officials have already mentioned today, where revenue receives information of varied leases from two arms of government and that administrative process did not occur.

Mr Barr: That may well be, but that is not maladministration.

THE CHAIR: Okay. For clarity's sake, that is the course of events that have occurred, and it has resulted in—

Mr Barr: I did not think it was deliberate; I think you have just misused a word.

THE CHAIR: That is okay. That has resulted, though, in a leaseholder receiving a bill in excess of half a million dollars simply because the wheels of government failed.

MS ORR: I know we are cutting into the tea break, but I have a very quick question.

THE CHAIR: I am guessing there are a few more questions in the revenue space beyond just one more supplementary?

MS ORR: Mine is pretty quick.

THE CHAIR: Have other members got further questions relating to revenue?

MS LE COUTEUR: I had one, but it was about the lease variation charge, which Mr Coe started with. Regrettably, we have wandered away a long way.

THE CHAIR: We might suspend briefly. If the officials that relate to the revenue management output class could remain, we will deal with those questions immediately after the break.

Hearing suspended from 3.37 to 3.51 pm.

THE CHAIR: We will kick on for the afternoon session; we are looking at the ICRC superannuation provision account and the territory banking account. I understand that there are a few more questions relating to revenue management when members return.

Chief Minister, I took your opportunity to reflect on the word "maladministration" during the break. In fact, yes, that is what I did mean. I am happy to table an excerpt from the *Macquarie Dictionary*. It says in relation to "maladministration", "maladminister" or "maladministrator":

> … to manage (especially public affairs) badly or inefficiently.

That is the definition I sought to imply.

Mr Barr: The Independent Commissioner against Corruption says that it is—

THE CHAIR: We do not have one of those in the ACT, Chief Minister.

Mr Barr: The Independent Commissioner against Corruption says that it is:

> … irregular or unauthorised use of public money, the substantial mismanagement of public resources, or the substantial mismanagement of official functions.

So to be clear—

THE CHAIR: And until such a definition is legislated in the ACT, I believe the *Macquarie Dictionary* definition stands.

Mr Barr: All right. I do not know about that, but just to be clear, you are not accusing anyone of corruption in any of these offices?

THE CHAIR: No. Poor administration.

Mr Barr: Okay. We can agree to disagree on that issue, but I just wanted to be clear that it was not reported in the media that you had accused officials of that, because I did not think you meant it in that regard.

THE CHAIR: No, not of corruption: of administering public affairs badly or ineffectively. I am happy to table that.

Mr Barr: You hold that view; I do not share it. Just so that the record is clear in that regard.

THE CHAIR: Okay. Ms Orr, did you have follow-up or further questions regarding the lease variation charge or other relevant revenue matters?

MS ORR: Yes, on revenue, speaking in broader terms. We have heard quite a bit about: "Let us not have this tax or that tax within the revenue." We are in the middle of quite a big tax reform agenda. What happens if we start fudging things? We have heard from Pegasus that we are in a good position to be raising our revenue to support what we need to be doing. What happens if we start going "Let's cut this; let's cut that"? For example, what happens if we cap the rate changes and say we are not going to change any more? Where does that leave the budget position?

Mr Barr: I guess it depends on where you would set a cap. We have an annual cap, and that is the basis on which the revenue collection for rates is currently set. That sets the amount, and we then distribute that amongst the ratepaying properties.

Mr Nicol: Technically, the government has agreed, at least across the forward estimates, both the stamp duty rates and the reduction to stamp duty rates and residential rates and commercial rate increases. If you froze it now, you would have to work out what that meant for future rate rises and future stamp duty rates. If you wanted it to have no effect on the budget, you would have to recalculate what a mutual freeze would mean. It is a technical process. You could do it, but that would be the result.

Mr Barr: The forward estimates have contained within them assumptions about the growth in the number of rateable properties. That is linked to the forward land release program, for example. You would also then be able to make certain assumptions about where stamp duty levels would need to be set.

For example, in 2011-12, prior to tax reforms, stamp duty revenue was $239 million. If the ACT had not undertaken the tax reform program and stamp duty revenue had grown at the same rate as in New South Wales during this period, the ACT would have collected $626.5 million in stamp duty in 2018-19. This is $351 million, nearly $352 million, from the actual stamp duty revenue forecast in 2018-19.

If we had not changed the tax policy settings at all, stamp duty would have increased from around $240 million to around $630 million, based on not having cut the rates. That is reflective of growth in properties and the higher tax rates that would have applied. Rates would also have gone up by the wage price index each year, so the total revenue take would be a different mix between stamp duty and rates, but both would have gone up in that time, reflecting the fact that the city and the economy are larger.

A question ultimately for the Assembly has been: of those revenue lines, which ones are the ones we want to collect the bulk of our revenue. Since 2012 the view has been to move away from the stamp duties towards the broad-based land taxes that we have now. That gives a great deal more predictability and stability in the revenue base. If you started changing that, you would need to do some pretty substantive modelling on what the implications would be in terms of future revenue and you would probably need to explain which areas you would cut if you were going to be collecting less revenue.

MS ORR: And that is because our revenue is going to fund services?

Mr Barr: Yes. For the ACT, at this level of government—at state and local government level—the revenue we collect is expended on services for the community. As I mentioned this morning, the little bit that is left over in terms of our balanced budgeting approach goes to fund future infrastructure or pay down debt, or a combination of the two.

MS LE COUTEUR: Last year the Assembly passed a Greens motion to do a full review of the suite of lease variation charges and remissions that apply to residential mixed-use developments. Where is the review up to?

Mr Nicol: I will ask the officer to come forward.

Ms Goth: The review is about to start. The charge came into play 12 months ago now, so it is timely to start looking at the impact of that review. That work is intended to be undertaken over the next six months so that there is ample time to have proper consultation with all relevant stakeholders and then work towards any changes being implemented in the 2019-20 budget.

MS LE COUTEUR: What consultation are you anticipating happening?

Ms Goth: The details are still to be worked through. We have put our focus into the budget so far. We are turning our mind to that review now. They will be worked through within government over the next few weeks, then there will be more details available on that.

MS LE COUTEUR: Will it be finalised well before the next budget?

Mr Barr: It will need to inform decisions for the next budget, as per the commitment. We would not want to pre-empt the outcome of the review.

MS LE COUTEUR: No, of course not.

Mr Barr: It may or may not recommend changes. It might recommend small ones; it might recommend large ones. We will see. But it needs to inform next year's budget; people are aware of the time frames. I am equally conscious that a lot of stakeholders do not have the resources and time to engage in the process as thoroughly as the government can, but we also need some data on which to base a discussion. I think we are at that point, or will be in the next couple of weeks. That will enable both a year's worth of data plus enough time to allow stakeholders to engage effectively and provide information in time for the 2019 territory budget.

MR COE: Mr Barr, you said earlier that people get windfall gains from lease variations. Is that the case for all lease variations?

Mr Barr: No, it will not be the case for all. There will be some where there is no increase in value or the variation adds additional potential uses that are of a lower economic order. For the most part, that is a rare thing, but it does happen. People do seek lease variations that do not increase the value, but then the charge does not apply. As it relates to a lease variation, as distinct from a lease variation charge, that distinction needs to be drawn.

MR COE: Are there occasionally applications to vary a lease to remove rights—for instance, if something has a GFA cap on it, to reduce that GFA?

Mr Barr: I guess that—

Mr Nicol: It is probably better to ask that question of our planning colleagues.

Mr Barr: Yes. I guess it could happen, in theory, but in terms of the specifics of approving a lease variation, that sits with the planners, not with the treasury side, yes.

MR COE: Sure, but I guess the relevance of this is that if something has a reduced value, does that mean that they can, in effect, reduce their rates, their unimproved value, by reducing the rights? If it goes the other way, if you get an uplift and your valuation goes up, does that mean that you can actually—

Mr Barr: I guess that in theory if someone were, say, to have acquired commercial land, paid a commercial price and then sought to vary the lease to remove all commercial uses—

MR COE: Remove uses, or remove some uses, or decrease the GFA.

Mr Barr: Yes, in theory—

Mr Nicol: I cannot—

Mr Barr: I cannot think of examples, but we will have a look.

Mr Nicol: In theory, you can—

Mr Barr: In theory I guess you could seek to do that, but we will inquire and see whether that has happened. But, generally speaking, most leases—the ones that are sought to be varied—were granted quite some time ago. One of the complexities is that they have not had a modern lease structure or information, as opposed—

Mr Nicol: And modern language.

Mr Barr: And modern language, as opposed to those that have been issued in more recent times. Look, it is an interesting theoretical question, and I am happy to—

MR COE: Does the government want to see more dual occupancies in Canberra?

Mr Barr: Dual occupancy has its place. With the right sized blocks and the appropriate planning controls, yes, there is certainly potential for dual occupancy to be part of the future housing mix options. That is the work that is being undertaken by Minister Gentleman and his directorate in relation to the housing choices policy paper.

There are some locations that are better suited than others and some block sizes that are better suited than others. Where it has not been possible to support dual occupancy, secondary residences of a certain size have been supported. The granny flat out the back sort of option is suitable for some blocks as well. But these are, I guess, questions of planning philosophy that might be better explored with that directorate.

MR COE: The reason I ask is just to make sure that, in effect, treasury's policies are in sync with the planning department's policies.

Mr Barr: Yes, the policies can be in sync, but that does not necessarily mean that an in sync policy means an unearned windfall gain. You can want to push a particular policy outcome and expect also that a fair and reasonable amount of tax would be collected to achieve that. It is not a case of, "We desire outcome A; therefore, everything else must fall away in order to achieve outcome A." In most instances, as it relates to land zoning and the property market, it would be the zoning restrictions that would be the biggest inhibitor to redevelopment and renewal, rather than tax arrangements as they are in this city at the moment.

MR COE: It has been put to me that RZ2 developments in Canberra are largely dead, especially dual occupancies, and that is because financially they do not stack up.

Mr Barr: It is interesting. I live in an RZ2 zone. I can say that there are still changes going on around where I live. Certainly, there was a lot of uptake of RZ2 rezoning and change that occurred. I think that zone came into effect at least 15 years ago. I look to my fellow planning nerd Ms Le Couteur to—

MS LE COUTEUR: Yes.

MR COE: It used to be called—it was the A10s and all of that—

Mr Barr: get a note on exactly when. It goes back to garden city variations and the like, does it not?

MS LE COUTEUR: Variation 2003, yes.

Mr Barr: Yes, so we are talking 15 years ago. RZ2 zones have changed in nature—I think we are straying into planning territory here now—but there certainly is an argument—

MR COE: It is relevant, though.

Mr Barr: Yes, there is an argument for more differentiation between the different planning zones and what is allowed and what is not. The principles that underpin RZ2 I think are reasonably sensible, that you would see a greater density closer to amenities, transport and the like.

What applied before this—this is going way back to when I was a much younger man; I did not need glasses in estimates and probably had more hair—was almost a free for all. If your block was bigger than 700 square metres, I think you could do a dual occupancy anywhere. There was quite a lot of concern at that time that that level of deregulation was too much.

Whether, 15 years on, the regulatory approach that was applied through that work in the early 2000s is now deemed to have served its purpose and it might be time for another look I guess is the subject of this planning work and the planning committee. But in the end, if it is to change, it will require a majority of members of the Assembly to change it. So you have a stake in it as much as Ms Le Couteur has.

MR COE: It is more a question of LVC. The RZ2 zones are already there. It just does not stack up to do a dual occupancy. It seems that the only RZ2 developments you see in Canberra are ones where there have been a couple of blocks consolidated and you get six units as opposed to getting a dual occupancy.

Mr Barr: Sure, that might be the case. It would probably go to a range of issues, including market demand for the particular product in a particular location—

MR COE: There is definitely a demand for townhouses.

Mr Barr: Yes, I know that on my drive home I have seen that there is a lot of advertising now along a particular road that I take. Yes, they are largely townhouses now; they are not—

MR COE: Yes, but they are usually a consolidation of two blocks, not dual occupancies. The specific question is: is the lease variation charge in effect restricting your government's stated policy outcome of densification in RZ2 areas?

Mr Barr: No, not according to how you have just described it. It might, and we can certainly look at this in the context of the review. It might be impacting on the type of densification, but it is not impacting on the densification because, as you observed, it might mean that there is block consolidation and more than one additional dwelling going on some of those sites. A little bit depends on the size of the original blocks as well. My personal experience in the part of Canberra I live in is not one filled with very large blocks. They are not 1,400 square metres in Dickson. They are a bit smaller than that.

MR COE: But they will still allow dual occupancies under the code.

Mr Barr: Some, yes. The place next-door to ours is a dual occupancy. They went from one dwelling to two. That is in an RZ2 zone. So, yes, you can have that sort of change. But then, go one street away, and there are two blocks that have been consolidated and they are building three townhouses.

MR COE: Is the government open to reconsidering the LVC on dual occupancies?

Mr Barr: Not the principle that there would be an LVC—

MR COE: Or the amount, then?

Mr Barr: That there would be an LVC—

MR COE: In the amount?

Mr Barr: You see, that is part of what the review process is going to look at. But it also has to be taken hand in hand with the planning review process in terms of what the rules will be—

MR COE: Even if you have the existing rules, are you open to reducing the LVC for dual occupancies?

Mr Barr: I think both have to be considered. If the policy objective is more dual occupancies, then the change that is necessary to achieve that will be both a zoning one and potentially an LVC—

MR COE: Not necessarily, because they do not stack up at the moment in RZ2 areas—

Mr Barr: I think it will, because depending on what size block you allow for a dual occupancy and what is—

MR COE: There are currently rules for that in RZ2.

Mr Barr: There are, but regarding the supply, RZ2 is a very, very, small element of the total footprint of available land in the territory. If the objective is more dual occupancies then you are going to have to both. That is what I am saying.

MR COE: But if you want more dual occupancies within walking distance of local centres, which is exactly what the RZ2 is meant to be, and you want densification around local centres—

Mr Barr: Yes, but not every suburb has an RZ2 zoning. When you go back to—

MR COE: That is right. That is because they are meant to be around local centres. So if you want to have densification around local centres—

Mr Barr: No, but there are suburbs that have local centres that do not have an RZ2 zoning around that local centre.

MR COE: Yes, they would be very few and far between.

Mr Barr: But they do exist.

MR COE: Possibly; I am not sure.

Mr Barr: Yes, they do.

MR COE: Why are there two zones at the moment? The government supposedly wants more dual occupancies then has a tax that restricts dual occupancies from going ahead. It just seems to me that you have got the planning department doing one thing and you have treasury doing something else, and you are at cross-purposes.

Mr Barr: You are welcome to that view. I do not agree with it. But in the context of the future, I suspect it will be the zoning changes—the Reserve Bank has concurred on this in their analysis of zoning impacts on dwelling types and housing affordability—that will make the biggest difference.

I am not in a position to pre-empt either that planning directorate work or, in fact, the position that the planning committee or indeed the Assembly will find ultimately on this question. As you all know, it requires at least one other dancing partner on the floor of the Assembly in order to get anything done. And one of your parties—

MR COE: I will give you a tip. I reckon if you reduce LVC, we are probably likely to put our hands up.

Mr Barr: There we go. Now I know what is needed to take you to the ball, Mr Coe, I will—

MR COE: That is right. I will be waiting for your invitation in the mail.

Mr Barr: consider that. I will consider that.

MR COE: I will be clicking send and receive every five minutes in anticipation.

THE CHAIR: I will defer my question to Mr Coe.

MR COE: Thank you.

MS ORR: Are we still with revenue?

THE CHAIR: If there are further revenue questions we can take them; otherwise we can delve into superannuation, treasury banking accounts and ICRC.

MS ORR: That is fine.

Mr Nicol: We do have the answer to that burning question about Mr Fluffy blocks.

Mr Miners: Basically, you were asking how many first right of refusals were in the system. There were 92 offers initially accepted. That does not mean they are going to translate into actually taking up the block. Of those, to this date 45 first right of refusal property offers have been exchanged and settled. The other 47 are in the system. They have either not been taken up or are still in the process of documentation. But, at this stage, 45 first-run refusal offers have been accepted, exchanged and settled; they own the block.

Mr Nicol: So that we can arrange witnesses, can you advise the order of the questioning?

THE CHAIR: How about we tackle the ICRC first? We have a change of officials. Mr Dimasi, can you please indicate that you are aware of the privilege statement on the pink sheet of paper in front of you?

Mr Dimasi: I am aware, yes.

MR COE: With regard to the latest determination of water prices, did the ICRC consider the service agreement that is in place with ActewAGL?

Mr Dimasi: The determination looked at everything, basically, and the agreements were examined, yes. I am not sure that I understand the question.

MR COE: Obviously there is a very expensive service agreement in place between Icon and ActewAGL for the delivery of various services?

Mr Dimasi: Yes. I understand your question now.

MR COE: Some of us in this place have questioned the value for money proposition of those contracts that are $25 million a year or thereabouts. Is it your role to actually investigate whether there is value for money there or do you see that as being just an input to get to your final decision?

Mr Dimasi: No. We need to be satisfied that the costs that lead into the composition of the tariffs, the prices, are efficient. We test all the cost components to ensure as best we can—and this is an imperfect science, of course—that they are efficient. We looked at the operating costs, we looked at the capital expenditure right through, and part of that was to look at those agreements, yes.

MR COE: When you look at those service agreements and the shared services contract for $27 million—and there are big agencies in the ACT government that are paying just a few million dollars, and what is really a relatively small organisation, Icon Water, is paying $27 million—how could that possibly be value for money if you benchmarked it against comparable services?

Mr Dimasi: First of all, there were some savings that were made from those agreements. Secondly, I guess the issue for us is to also have a look at existing contracts. We cannot disturb contracts that were properly entered into. In a forward looking way, it is getting some reassurance that whatever is in place is properly reviewed at the right time and that there is evidence presented to us that that is done in a way that gives value for money. We were satisfied at the end of the day that we had got the lowest possible cost that we could for those agreements, given the circumstances.

MR COE: You do not make a judgement on whether that contract should be in place or not; your role is to make sure that they are extracting as much value as possible out of the existing contracts?

Mr Dimasi: Correct.

MR COE: So you are not necessarily making a value judgement about whether it was right to sign that contact?

Mr Dimasi: Not whether or not to sign the contract. But, going forward, we would certainly be looking to ensure that with a contract, whenever it is renewed or whatever happens, the process that is in place delivers the most efficient outcome for the consumers in the ACT too. That is something that we would be always looking to do. I think we say that in the report, or words to that effect.

MR COE: And do you take a role in commenting on the government's dividend policy?

Mr Dimasi: No. That is a policy question for government. What we do, though—there is a whole cost of capital—is examine the whole issue of the cost of capital that is allowed and we, if you like, have a benchmark efficient firm where we determine the cost of capital, we determine the gearing ratio and we determine all the components that go in there. There is a rate of return that is allowed to the business, and that rate of return is benchmarked against what might be comparable businesses around the country bearing the same level of risk and the like. That then goes into getting the total costs and, from that, deriving the prices. What happens to that rate of return, whether that is then a proportion provided in dividends or whatever is done with it, is an issue between—

MR COE: The owner.

Mr Dimasi: the owner and the company. We do not get involved in that.

MS CHEYNE: The thing is that bills and prices are going up and that is being passed on to consumers, the ACT community. I want to get a better sense from you about the factors that are affecting this and are they local to the ACT or are they more regionally based or nationally based?

Mr Dimasi: This is for electricity?

MS CHEYNE: Yes.

Mr Dimasi: Not for water, because water bills went down.

MS CHEYNE: Water is okay but electricity? Heating is probably front of mind for me.

Mr Dimasi: Yes, absolutely. We have seen, unfortunately, two years of pretty significant price increases in electricity, and there is no getting around that. Our role as the regulator is to regulate ActewAGL Retail and to ensure that there is a standing offer for the consumers in the ACT that has some sort of control over it. The long and the short of it, though, is that some 87 per cent of all the costs that make up the bill are determined outside ActewAGL Retail's control. They are the network costs, the costs of distribution and transmission, carrying the electricity, all the poles and wires. They make up a very big proportion and they are regulated by the AER.

You have got the wholesale cost, and that is the cost of generating electricity, and that is where all the debates have been over the last couple of years—the big spikes in wholesale electricity prices. We have a national electricity market, and that is being largely determined outside the ACT. And there are some costs for delivering green objectives for renewables. The Clean Energy Regulator is involved in those and they have also contributed quite a bit this year.

There have been a number of these things that have come together, as we are seeing a fundamental change to the electricity sector, as more renewables are being utilised to generate power, and the structure of it changes. We saw a spike in electricity wholesale prices last year where the contract prices increased by over 100 per cent—112 per cent, I think it was. These are all external factors to the ACT.

What we do, though, is: try, as much as we can, to minimise the impact on ACT consumers by not allowing all that price to flow through instantaneously. The model that we use averages those wholesale price changes over a 23-month period. That means that you do not get that sudden huge surge but you do get an increase, and you get an increase this year as well. That is why we saw two years of price increases. We tried to smooth it out, flatten it a bit, not make it such a big increase.

We also did have a look at the actual costs that the retailer bears. Even though it is 13 per cent, it is still important. We reduced their margin because we did not think it was right to apply the existing margin to a much bigger cost base. So we reduced the margin. That was in the determination last year.

There was a debate about whether you should have headroom for competition, a CARC. It is called a competition allowance, CARC, and we did not allow that in the determination. This year what we did was not a full determination; it was just an adjustment. But there were additional costs that came through also from the AEMC which required some changes to allow the retailer to take over some of the metering functions, and that involved IT changes and various other changes.

ActewAGL Retail came to us with costs to be passed through, and what we did there was look at it. We decided some of those costs were actual capital costs, and they should have been capitalised over a five-year period. Again, that reduced the price increase, but I must admit that you have got them going down for a few more years as they are capitalised and worked out. There are a number of these very significant external factors at play here and we are doing the best we can to soften the blow, if you like, and smooth the price increases out to as little as we possibly can.

MS CHEYNE: Regardless, they are still a blow.

Mr Dimasi: But, regardless, they are still a blow, yes.

MS CHEYNE: Is there any relief in sight or is this the new reality?

Mr Dimasi: To state a forecast in the electricity sector is a very dangerous business.

I am also trained in economics. I will probably end up giving you "on the one hand" and "on the other hand" as well. If we are looking at the wholesale prices, they have stabilised and have started to come down. There is definitely some potential for light at the end of the tunnel there, but we have got to see what happens.

On the other hand, the wholesale costs are regulated by the AER. The AER's decision was challenged in the courts. It has been remitted to the AER to remake that decision. This year we only had an adjustment by CPI. That decision is still flowing through. The probabilities are that that decision will lead to higher costs down the track. On the one hand—I said I might use it; I did not mean to use it but there you go—the wholesale charges might go down, but on the other hand those electricity network costs might go up. As we are looking at it now, it is a bit hard to predict how it might go, but hopefully we will not see the price increases that we have seen in the past.

We also have seen a very large uptake in solar panels and that is also leading to some increased costs. Again, this is the national regulator. This is not a local issue. This is the national regulator. We have seen clearly a much bigger uptake than they had forecast. Even though the price has not gone up, the total cost has gone up and that is reflected in and has provided for some of the cost increases in our electricity price as well. You have got all these things and you need to predict each of them to see what might happen, to see where we might go. I am hopeful that we will not see this price increase that we have seen in the last two years, but I will not put it at greater than hopeful at this point in time.

THE CHAIR: What impact did the feed-in tariff that the retailers have to recoup have on the pricing determination?

Mr Dimasi: Very little. The feed-in tariff is adjusted through the network charges, and those network charges have not yet been adjusted. So we will wait and see. There were some minor timing adjustments in there, but that is all.

THE CHAIR: And did the energy industry levy contribute?

Mr Dimasi: We have a table that we can provide. You can see everything that was provided. The wholesale electricity price and the small-scale renewable were the two really big ones. The others all made small contributions. We can provide you the details. We have a table that can show you exactly the components of that increase. We will provide that to you on notice.

MS LE COUTEUR: I have a question about the territory superannuation provision and the territory banking account. As we are all aware, the banking royal commission has heard evidence of what it has described as appalling behaviour by a number of Australian financial institutions. Given that we have a responsible investment policy, has any action been taken under that policy with respect to the actions of the banks and other financial institutions?

Mr McAuliffe: Under our framework the sorts of issues arising through the commission will affect basically the ESG risk assessments that go on with those organisations. Certainly our provider that analyses all those companies is reviewing those ratings. But to date none of the ratings have shifted to the point where any of those organisations have been red flagged or have been made the lowest rating, to be excluded from our investments at this time.

MS LE COUTEUR: What about shareholder actions? I know AMP had its AGM. Did you vote for or against the remuneration report, given the circumstances?

Mr McAuliffe: I do not know, off the top of my head, but I can certainly have a look and let you know how our votes were cast.

MS LE COUTEUR: Thank you, because that would seem to be fairly egregious. Are you planning to change any votes for shares on future issues coming out of the banking royal commission?

Mr McAuliffe: As we have discussed in the past, we do not step in and make any voting decisions directly ourselves. We have always got our broad voting policy under consideration and we will probably have another look, once we get through this financial year, as to how the broad framework has been applied. If we think there should be any changes we can certainly recommend that.

Mr Barr: If the royal commission makes any recommendations in this area in relation to those who hold assets that are managed in the way ours are, and their relationship with the banking sector, we will respond to any recommendations that the royal commission makes. But, given that they are still taking evidence it would be pre-emptive until we have seen the conclusion of their investigations. But, should they make any recommendations in this area, we will consider them.

MS LE COUTEUR: I would have thought AMP was pretty straightforward and clear, but anyway. So the royal commission is the trigger point, and if the royal commission does not say anything you would not expect to vote your shares differently? Even if you do not divest, it would not matter?

Mr Barr: What do you mean? Vote differently in what regard?

MS LE COUTEUR: The one I am referring to is AMP, which in the last couple of months had its AGM.

Mr Barr: Most of the board and the chair were sacked as a result, were they not? They resigned.

MS LE COUTEUR: Yes, but there was also a remuneration report. They resigned; they did not hang around to be sacked, basically.

Mr Barr: So what are you looking for us to do?

MS LE COUTEUR: My question was: how did you vote on the remuneration report?

Mr Barr: How should we have voted, Caroline?

MS LE COUTEUR: Against it.

Mr Barr: Against it. So there should have been no remuneration for all executives?

MS LE COUTEUR: No. Corporate governance means that if shareholders vote twice against a remuneration report then the board spill will come up for vote again. So it does not actually change the remuneration straightaway.

Mr Barr: Has a board spill not occurred?

MS LE COUTEUR: No, not everybody. It almost has, but not everybody.

Mr Nicol: Our structure is very much that we do not try to look at every issue of every company. We engage an adviser, who will advise on the voting of our shares according to specified principles, including environmentally sustainable principles. I do not know how we voted on that; we will take it on notice and come back with an answer.

Under the process we have adopted, the behaviour of any company is monitored by our external adviser and that is fed into scores about how they are rated, not just for their good business practices but for socially, environmentally and operationally sustainable approaches. We will need to keep this under review to see that the process works as it is intended. We are not quite at the end of the process yet. Mr McAuliffe may want to talk about how often the ratings are reviewed on our companies, but I imagine it is not an instantaneous process. It is an ongoing process that may take some months.

MS LE COUTEUR: There is actually a fair chance you voted against the AMP remuneration.

Mr Nicol: I think there probably is.

MS LE COUTEUR: About 40 per cent of shareholders did.

Mr Nicol: I think there is probably a fair chance, so we will check.

MS LE COUTEUR: I am hoping that the answer, when it comes, will be yes.

Mr Nicol: It would be good if the processes we have put in train actually produced that result, rather than us having to intervene and direct it. Otherwise treasury would have to be a lot bigger than it currently is.

Mr McAuliffe: I can certainly provide that information, and whichever way our vote went I can provide the reasons as to why.

MS LE COUTEUR: When is the provider for the territory bank account up for tender next? And are you going to be looking at ESG issues as well as straight financial issues when you decide who the new provider will be?

Mr McAuliffe: I have to be careful what I say. A process is currently underway. The banking contract actually runs out at the end of this month, and some extension negotiations are currently being finalised. But a broader answer is that it is only the four major banks that can provide the services the government needs for transactional banking. The last time the tender was done there would have been some criteria around corporate responsibility and those sorts of things. They are certainly given a weighting in that process. Any future tender would presumably have that same sort of criteria.

Mr Nicol: I also add that changing our bank is a very costly and time-consuming process because all of our transactions are handled by our bank. It is not only having a bank account for our cash needs; it is everything from Access Canberra payments to all the parking facilities and all the linkages with our systems.

Mr McAuliffe: The last transition took probably the best part of 18 months.

MS LE COUTEUR: So it would be at least a year.

Mr Nicol: We have to do a lot of balancing here, and they are the sorts of issues we take into account in this process.

Mr Barr: One would hope that the royal commission that we apparently did not need might engender some industry-wide change.

MS LE COUTEUR: I think we can all agree with that, Mr Barr.

MS ORR: Pegasus noted in their report provided to the committee that the superannuation liability was estimated to grow but that there "is no indication that the ACT will have any difficulties in meeting its funded superannuation obligations". Is there anything you wanted to comment on in relation to that observation that it is growing? There does not appear to be any indication that we will have a problem with it.

Mr McAuliffe: Following on from this morning's discussion around that, the valuation itself has increased. That is because of a change in the discount rate that has been used to value the cash flows. But, as is also highlighted by Pegasus, that change in the discount rate did not make any change to the underlying cash flows projected. Our key focus is about those future cash flows. At present the budget provides an amount of appropriation to the super provision account to cover the cost of those payments. That way we can leave the rest of the cash in the account to be invested and, hopefully, grow, largely unencumbered by cash flow. I think Pegasus is right in that regard. We have a process in train to meet those cash flows.

Those cash flows are at risk, like everything. They are all going to depend on what happens with changing demographics in the main. For example, what is the effect of CPI on people that might take future pensions? How will wages growth impact on final benefits? There are a number of factors. At present, we are pretty reasonably comfortable with the assumptions that sit behind the projections.

Mr Nicol: I add: this is a liability that we have. There is nothing we can do to affect the liability. Closing the schemes in 2005 meant that the liability was not growing. We have to meet this cost irrespective of any actions the current government or future government might take. The question then becomes this: is the approach that we are taking the right one? I think Pegasus has commented in this regard and we think it is the right one. We are being prudent and building an asset of an equivalent amount to meet this over time.

We are not imposing at all on today's generation. It has been built over a period. It is our job to manage it very well and put appropriate governance over it to make sure it is managed properly, which, in my view, is the case. As Mr McAuliffe said, the budget is meeting the current cash needs of those pensioners. That leaves the fund in a relatively good place to have an eye to the longer term rather than have to liquidate assets to meet current liabilities. Most superannuation funds that have many members would have to not only invest for the long-term—for people who might be in their 20s and 30s—but also manage their affairs such that they have the cash available to pay out claims from members who might be in retirement age. We are managing that as well. I think we have put it in the best place we can.

Mr McAuliffe: I make one final point. The credit rating agency Standard & Poor's, in their last year's review—and it is one of the things that they often pick up—have effectively formed the same view as Pegasus. One of the things that they find is a key part of our framework: the funding plan strategy that we have got in place for the liability.

MR COE: With regard to the broader investments, does the superannuation account include any investments with Icon Water?

Mr McAuliffe: They are not a listed company, so we do not—

Mr Nicol: We don't own any equity.

Mr McAuliffe: Do not own equity. I mean, no.

MR COE: There is not?

Mr McAuliffe: No.

Mr Nicol: I do not think we would have any debt, direct debt or indirect debt, either.

Mr McAuliffe: No.

Mr Nicol: I think the answer is no.

MR COE: Yes; okay.

Mr Nicol: I cannot think of an avenue. We may own equity in a financial institution that—

MR COE: That deals with them? Yes. Sure, okay.

Mr Nicol: has lent to ACTEW or bought bonds from ACTEW perhaps. Maybe we get something indirect like that, but it is certainly not planned or part of the structure.

MR COE: Sure. Is there any indirect relationship with Jemena?

Mr McAuliffe: Not that I can think of offhand.

Mr Nicol: No. I do not even know Jemena's ownership status, to be honest.

MR COE: Yes. That is why I said "indirect dealings". Finally, is it possible that the superannuation provision account has got investments with any of ActewAGL's competitors?

Mr Nicol: That is more likely, I think.

Mr McAuliffe: Possibly.

Mr Nicol: Because Origin is listed. AGL is listed.

Mr McAuliffe: They may well be excluded under our responsible investment policy. For example, AGL, I think, is currently excluded under our framework.

Mr Nicol: But they would be very much passive investments as part of an index type thing.

Mr McAuliffe: That is right.

MR COE: So under your own investment rules you could not invest in a company such as ActewAGL if that was listed?

Mr McAuliffe: If they were a listed company on the stock exchange, they would fall into the broader pool of investments that would be considered and then—

Mr Nicol: Assessed.

Mr McAuliffe: Then the overall framework would apply to that, and then they may well be excluded.

Mr Nicol: And the government essentially owns 50 per cent of ActewAGL through Icon, so it is a direct investment rather than through the SPA.

MR COE: Is there any conflict in owning shares in competitors to ActewAGL?

Mr Nicol: I would say no, for three reasons. One is that it is very much a passive index; if we do own it, it is a passive index ownership. The second is that we obviously are not directly aware of it here, whether we do or how much, so we are not taking that into account in any decisions or advice we are giving to the government. And, thirdly, if we do, it is likely that the ACT is such a small proportion of that company's retail and customer base that it really does not come into play, I would have thought.

Mr McAuliffe: There is a list of all of our current direct shareholdings on our website, so you can see if there is anything there.

Mr Nicol: We will have a look, but, as Mr McAuliffe said, some of those companies are fossil fuels and—

Mr McAuliffe: We do not directly instruct any of our managers what to buy. That is the whole idea of it. We try to get a broad, diversified portfolio as best we can, by geographic area, by industry type.

Mr Nicol: That also supports the approach we have taken in terms of a policy framework for the voting of shares, not a direct direction to vote shares in a particular way. I do not think that was a big consideration, but it is a positive effect of that policy.

MR COE: Do you know, off the top of your head, whether the ACT government has any shares in any of the PPPs underway, in terms of the consorting partners?

Mr McAuliffe: We certainly have not got any direct. I do not know who the equity partners are, but we may own some shares in one of the equity partners through a listed company arrangement. That would be the only exposure.

Mr Nicol: It would be very small. I am trying to remember who the partners were. The constructor of the vehicles is a Spanish firm. The builder, I think, is a German firm. We have an Australian firm as a constructor. I think there is some Japanese equity. It is possible that if these companies are listed, we would have a very small shareholding. We can check. Again, it is not something that influenced any decision to choose one consortium over another. I suspect that we probably own shares in the other consortiums that bid for the projects if we own any in this one.

MR COE: While Mr McAuliffe is here, if I may go to something on a similar but different note: with regard to the dividend policy for Icon, and indirectly ActewAGL, is it correct that the government has a 100 per cent policy for ActewAGL?

Mr Nicol: That is correct, yes.

MR COE: How long has that been in place?

Mr Nicol: Certainly it has been in place for the just over five years I have been in this job. I do not know how far it goes before that. I will probably have to take it on notice and check. It is been a longstanding policy.

Mr Barr: For as far back as I can remember, probably in the history of self-government. If it is not the case—I am pretty sure it is—we will advise the committee.

MR COE: Is that ever up for review?

Mr Nicol: I think the government's current policy is that it reserves the right in any financial year to give relief of some description. It did make a change, I think, two years ago, whereby the contribution to profit from contributed assets which were non-cash was removed from the 100 per cent, so essentially we were not requiring—

MR COE: To get cash they did not have?

Mr Nicol: ACTEW to borrow. Yes; that is right. I think ACTEW's debt levels are within the accepted norms of business, so they are not high in that sense.

MR COE: Even though debt is increasing?

Mr Barr: As a proportion of revenue, I know that it is—

MR COE: I know it is a proportion, but debt is increasing, all the same.

Mr Nicol: It is, because it is investing and growing its business.

Mr Barr: It has a bigger asset base.

Mr Nicol: Yes. I would have to get details on it. It is debt metrics. Last time I looked, I think they were pretty stable as a proportion of their revenue.

MR COE: This might be a question for Icon, but can you say why the Icon dividend is considerably higher than what was forecast?

Mr Nicol: It probably would be best to ask Icon that.

MR COE: It is not because of government requests or anything?

Mr Nicol: No; it was exogenous.

MR COE: It is business as usual?

Mr Nicol: Yes. I think it was several factors. I am going from memory here. One was that they had higher water sales than they expected because it was a relatively dry season, which had revenue implications. I think they had some one-off transactions in the energy business in ActewAGL which produced a one-off gain this year. But they would be much better placed to give you the exact details.

Mr Barr: I understand they are first up tomorrow morning, so you will not have to wait long.

Mr Nicol: But was not a result of a government policy.

MR COE: One more sleep.

Mr Barr: One more sleep indeed; that is right. One more night to contemplate what you are wearing to the ball, Alistair.

MR COE: As long as you bring the LVC remission.

THE CHAIR: I have a couple of quick questions just to finish up. Can you explain why there is a preference for the fixed rate medium-term bonds to be issued until 2028 and then inflation-linked bonds beyond that?

Mr McAuliffe: The preference over—

THE CHAIR: Why is there a preference for fixed rate medium-term bonds to be issued up until 2028 and then inflation-linked bonds beyond that?

Mr McAuliffe: We have not actually undertaken any inflation-linked bond issuance for a number of years now. The short answer is that the demand for them is not there. They were undertaken in the early days and they were undertaken for Icon Water. It was all around a sort of natural hedge for their balance sheet because of the CPI linkages. That is why they were undertaken, but we have now moved towards the fixed rate bonds.

We are illiquid in the market; we do not go to the market all the time. What we are trying to do is make sure we have some nice regular issuance and that investors understand it. And we are trying to build out our yield curve. You will see that it is shown in our papers. You can see our curve just building at the maturities. What we tend to do is that each time we have a benchmark line we will go and issue for another couple near maturity. It gives us budget certainty around our costs and our estimates.

Mr Barr: We are not going back to any inflation. The reason there was one is historical.

Mr McAuliffe: That is historical. That is the maturity of it, sorry. And that is an annuity bond, so it actually pays down over time.

THE CHAIR: What are the plans, then, for bond issuance? What has been undertaken in the current fiscal year? And then looking forward to next year, what is the agenda?

Mr McAuliffe: For this current year the first of our medium term note bonds actually matured. They matured last week. We went to market a couple of months ago and we basically refinanced it with that 2028 maturity bond that you can see in the budget papers. That was largely just to refinance that. For the upcoming year, we do not have any new benchmark bond actually forecast. There is a table which shows that—

Mr Barr: It goes to the earlier discussion about the fact that we only borrow when we need to. However, we will continue to engage with the market. It is useful to have a wide range of players interested in purchasing ACT government bonds; it drives the price down. Mr McAuliffe and I are in Sydney next week and then in South-East Asia in July; between us we have about 15 bond meetings. It will be a good fun bond roadshow.

THE CHAIR: Typically, who is purchasing the bonds?

Mr McAuliffe: There is a range.

Mr Barr: It is a range, yes.

Mr McAuliffe: A range like asset managers, life insurance companies, superannuation funds. Whoever is managing a portfolio of fixed income securities will tend to look at whether our bonds fit into their portfolio at a point in time.

THE CHAIR: What transparency is there as to who is purchasing the bonds? Is that published on the treasury website?

Mr McAuliffe: No, because a lot of the time you do not see who the underlying bond holder is. Sometimes they are held through a custodian, so you do not actually see the underlying individual names.

Mr Barr: We can report, and I think we have reported, on domestic versus international; we can give that level of information.

Mr McAuliffe: I can certainly provide some statistics on some recent issuance around that mix between an offshore versus a domestic investor.

THE CHAIR: As a starting point, that would be handy.

Mr McAuliffe: And the types of investors that they are. It might be a bank balance sheet versus an asset manager, for example.

THE CHAIR: Unless there is a quick supplementary, we might draw a line there. Thank you, Treasurer and officials. In relation to the usual follow-ups to questions that were taken on notice, we ask that they be responded to within five days, the first day being tomorrow. A transcript of today's hearings will be provided for you in due course, as per usual.

The committee adjourned at 4.59 pm.