STANDING COMMITTEE ON
ESTIMATES AND FINANCIAL OPERATIONS

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
MONDAY, 22 JUNE 2009

Members

Hon Giz Watson (Chair)
Hon Philip Gardiner (Deputy Chair)
Hon Liz Behjat
Hon Ken Travers
Hon Ljiljanna Ravlich

Hearing commenced 2.32 pm

MARNEY, MR TIMOTHY
Under Treasurer, Department of Treasury and Finance,
sworn and examined:

The CHAIR: Welcome. On behalf of the committee I would like to welcome everybody to this public meeting. Before we begin, I ask Mr Marney to take either the oath or affirmation.

[Witness took the oath.]

The CHAIR: Thank you. Please state your full name and the capacity in which you appear before the committee.

Mr Marney: My full name is Timothy Michael Marney. I appear in my capacity as the Under Treasurer of the state of Western Australia and the CEO of the Department of Treasury and Finance.

The CHAIR: Thank you. You will have signed a document entitled "Information for Witnesses". Have you read and understood that document?

Mr Marney: I have.

The CHAIR: These proceedings are being recorded by Hansard. A transcript of your evidence will be provided to you. To assist the committee and Hansard, please quote the full title of any document you refer to during the course of this hearing for the record. Please be aware of the microphones and try to talk directly into them. I remind you that your transcript will become a matter for the public record. If for some reason you wish to make a confidential statement during today's proceedings, you should request that the evidence be taken in closed session. If the committee grants your request, any public or media in attendance will be excluded from the hearing. Please note that until such time as the transcript of your public evidence is finalised, it should not be made public. I advise you that publication or disclosure of the uncorrected transcript of evidence may constitute contempt of Parliament and may mean that the material published or disclosed is not subject to parliamentary privilege.

Mr Marney, we provided a letter inviting you to attend this committee hearing; I wonder if you would like to make an opening statement in response to that letter.

Mr Marney: The letter was quite specific in terms of the areas that you wanted to cover so I am happy to go straight into questions. In terms of an opening statement, the committee would be aware that the budget papers capture and seek to present as openly as possible the parameters that are used to formulate the budget projections across the out years. There has been some unprecedented volatility in some of those parameters in recent months and in the lead up to the budget. It is no surprise that the budget was framed in some fairly trying circumstances in that regard. The budget, in terms of the expenditure side, includes all the decisions of government that were communicated to me as Under Treasurer and I have sought to reflect those as completely as possible, where indeed government has taken such decisions.

The CHAIR: Thank you, Mr Marney. You may be aware that some of our committee members are relatively new to the Standing Committee on Estimates and Financial Operations. Consequently, questions today may range from more broad questions on the general budget process right through to specific details—in particular about the big picture economic issues facing the state. I will now simply throw the floor open to members who have questions.

Hon LJILJANNA RAVLICH: Thank you very much, Madam Chair.

Under Treasurer, I refer to page 17 of the 2009-10 budget overview and specifically to the net debt for the public sector. In 2008-09, we had a net debt level of $6.9 billion and by 2012-13 that is foreshadowed to increase to $19.1 billion, which is almost a tripling of debt.

First of all, could you outline what happened to state debt over the past decade by way of comparison to what we see happening now?

Mr Marney: I will have to refer to appendices in budget paper 3. In very broad terms, over the past decade the level of net debt, as at the end of each financial year, has roughly been in the $3.5 billion to $4.5 billion range. That level has been fairly consistent over the past decade.

Hon LJILJANNA RAVLICH: Can you now outline what options are available to the state government for the repayment of the $19.1 billion debt?

Mr Marney: I can outline the mechanics of how that all works. Essentially the net operating balance is one of the key mechanisms by which debt is repaid over time. Essentially, by running a surplus on day-to-day operations, that surplus is used to retire debt as and when the opportunity arises.

Hon LJILJANNA RAVLICH: What is the government's plan and time line for the repayment of the forecast $19.1 billion debt outlined in the budget papers?

Mr Marney: The government's plan is embodied in its suite of financial or fiscal targets that are required under the Financial Management Act. The plan in that respect, so much as debt is concerned, is to keep the net-interest-cost-to-revenue ratio below a level of five per cent: the government's plan and its fiscal strategy is focused on the burden of servicing the level of debt and how much of the state's day-to-day revenues goes to that interest cost. There is not an explicit target to reduce the aggregate level of net debt; the target is around the extent of burden that that level of debt puts on the day-to-day revenues—similar in many respects to the previous net-debt-to-revenue ratio which was the target of the previous government.

Hon LJILJANNA RAVLICH: In your opinion, how long will it take for net debt to be repaid? Also, what level of economic growth is required to deliver a budget surplus?

Mr Marney: Both are very simple questions with potentially very complex answers. How long does it take to pay off $20 billion? It depends on the policy settings. It depends how quickly you want to pay it off. It depends what surpluses you run; hence your question about the level of growth needed to run those surpluses. In terms of how one would assess that over time and how one would assess a reasonable duration for the repayment of $20 billion, one would have to look at what the average surplus has been over the past 15 years and then in very simple terms apply that to the level of debt.

Hon LJILJANNA RAVLICH: Have you got any idea?

Mr Marney: I have plenty of ideas. It is a question of whether they are valid and whether my opinion is valid. It is really a question for the government rather than for me as such. However, I posit that rule of thumb.

Hon LJILJANNA RAVLICH: Can you give us an idea what level of economic growth may be required to deliver the budget surpluses capable of making a significant and sustained impact on debt reduction?

Mr Marney: Whether a given level of economic growth has an impact on debt reduction depends on the revenue and expenditure decisions that a government takes in the context of that economic growth. Average economic growth in Western Australia is around 4.5 per cent per annum, so if you assume average levels of surplus to retire debt over a period of time, you would be looking at average economic growth to be able to achieve that: a growth rate of 4.5 per cent or thereabouts would generate capacity to have a decent structural and cyclical outcome in the budgetary setting.

[2.40 pm]

Hon KEN TRAVERS: I just want to go back. You made the comment in terms of the net-debt-to-revenue ratio and the new target was the net interest costs as a share of revenue. I guess my first question is: why was that chosen as the measure?

Mr Marney: It was a decision of government. If you are looking for an articulation of government's reasoning behind that, you would have to ask government. But, having said that, in pure economic terms, why would it be, from my perspective, a preferred measure? Because it is comparing one financial flow to another financial flow; that is, comparing the cost impost on a day-to-day basis of a level of debt with the capacity to pay that debt, being your day-to-day revenue flows, which gets around the problem of comparing a stock measure—that is, a level of net debt at the end of a given financial year—to a daily revenue flow, which is sort of mixing two concepts to an extent.

Hon KEN TRAVERS: I follow that to a degree, but once you start to bring in net interest rate costs, does that not add in a third factor which is outside the control of the state government—that is, what are the interest rates? You referred to the long-term average rate of growth for the state. If the long-term average interest rate was applied to the figures on page 14—I do not know if you have done the exercise on budget paper No 3 of what would occur if you applied the long-term average interest rate costs to those figures—what would that actually do to the net interest rate costs as a share of revenue?

Mr Marney: No, they have not been applied to any scenario around that. I guess, in any aspect of the budget in its construct, there are always elements that are outside government's direct control. In many respects, the key area of challenge in managing the budget is to deal with variations in parameters that are outside your control. The fact that they are outside your control does not mean that you put them to one side and just assume that that is someone else's fault. The state still needs to deal with those circumstances, whether it be global commodity prices, the exchange rate or interest rates. I guess the art of prudent budgeting is to ensure that your budget settings are such that they can deal with variations in those problems over time.

Hon KEN TRAVERS: How do our budget settings deal, then, with a dramatic increase in interest rates; in fact, not even a dramatic increase, but a return of interest rates from where they are currently to where their long-term average is? If you go to the chart on page 14 and look at the period during which the AAA credit rating was lost to this state, it was a period when the interest rate was approximately, on average, double what it currently is. If you have lots of money in the bank, that is fine in terms of debt, but if you have borrowings to the tune of about $19 billion, and if you return to the long-term average net interest rates, does that not then put us well above the upper limit of five per cent as the target limit?

Mr Marney: If you held all other factors in the budget equal, yes it would, but we are delighted to be dealing with only one varying parameter at a time. The key question is: what is it that would cause interest rates to increase to those levels? It would be, presumably, because of a strengthening in the domestic and international economies. In those circumstances, it would also be likely to expect that our revenue projections would be greater than those embodied in that particular parameter and, therefore, you would have variations in numerous aspects of that parameter, even if the level of net debt did not change. The fact that more than likely your revenue and your interest rate parameters would move would mean that they would probably offset each other. In any case, the job of government day-to-day midyear review and budgets is to deal with those movements and to seek to ensure that the state's finances remain within the fiscal targets that they have set for themselves.

Hon KEN TRAVERS: But is there not a problem that a lot of the borrowings will occur and a lot of the projects will commence in the next year and that once those projects have started, your options for not incurring those borrowings is gone? But if you do get, as many commentators are predicting, a lift in interest rates without necessarily a lift in the overall economic activity, does that not cause us a long-term problem for the state?

Mr Marney: It depends. If you restricted your responsive measures just to stopping capital projects, that would be a problem. But that is not the only fiscal tool the government has to play with.

Hon KEN TRAVERS: So, if you do not stop that, what are the other options to manage the budget?

Mr Marney: There is a whole suite of parameters and policies on both the expenditure and revenue sides of the budget. Obviously, if government was in a circumstance where interest rates had increased and it was looking at a breach of that particular self-imposed target then it would assess the relative merits of the various options before it.

Hon KEN TRAVERS: But what are some of the options?

Mr Marney: There are only two ways, really, that you can improve the state's balance sheet—either you raise more money or you spend less, or you do both.

Hon KEN TRAVERS: Is the sale of assets an option? That is certainly mentioned on page 14 as the way we returned the state to financial health in the past. Is that a third option?

Mr Marney: That is one way of raising revenue. It is off your balance sheet instead of your recurrent base.

Hon LJILJANNA RAVLICH: Under Treasurer, would you say that this is a prudent budget?

Mr Marney: I am not sure that I should be answering a question which requires an opinion.

Hon LJILJANNA RAVLICH: Purely from a professional viewpoint, I ask.

Mr Marney: Purely from a professional viewpoint, I think, in the circumstances, this is about the best you could do. These are very trying circumstances and I think we have seen other jurisdictions struggle with that quite significantly in terms of their budget settings, both in terms of the fiscal settings and the economic settings. With all the states now having released their budgets and the outlooks for their respective economies, I am far more comfortable with our settings than those of other jurisdictions.

Hon LJILJANNA RAVLICH: Can I just take you to the revenue growth? It seems that the revenue growth over the forward estimates is very weak, from $19.6 billion up to $22.4 billion. When you compare that to the net debt, quite clearly there is a severe mismatch in respect of that. I want to ask you a series of questions in respect to that. First of all, is it true that there is a risk that the level of economic growth required to deliver the budget surpluses capable of making a significant and sustained impact on debt reduction may in fact not be realised?

Mr Marney: I think the risk is that some of the key assumptions underpinning the budget parameters, rather than economic growth in aggregate, may deviate in reality from what is issued in the budget. That is where the clear risk is.

Hon LJILJANNA RAVLICH: Can I also ask: what is the probability of the level of economic growth required to deliver budget surpluses capable of making a significant and sustained impact on debt reduction also not being realised?

Mr Marney: It depends on what you view as the required level of economic growth.

Hon LJILJANNA RAVLICH: I would say that the required level of economic growth is such that it enables us to deal with this $19.1 billion deficit in a timely manner.

[2.50 pm]

Mr Marney: That level of growth is a subjective judgement. I can say that the budget parameters reflect our forecasts of decline in activity of 1.25 per cent in the current budget year, a further half a percentage point in the following year and growth of 3.25 per cent in 2011-12 and 2012-13. That remains below the state's long-term average growth.

Hon LJILJANNA RAVLICH: How much of the state's debt must be serviced by commercial returns?

Mr Marney: There is no specific requirement in that respect.

Hon LJILJANNA RAVLICH: What is the general rule of thumb, if there is such a thing?

Mr Marney: No, there is not. There has been a move to the net-interest-cost-to-revenue ratio because it gives the rule of thumb of how much of the day-to-day revenue that is raised is required to service that level of debt.

Hon LJILJANNA RAVLICH: Are we actually relying on the policy settings of the government to get us out of this $19 billion debt position? I imagine that a big part of that is the $7.6 billion over the forward estimates that also needs to be saved to reduce expenditure throughout the public sector. Can you advise me whether government agencies have been asked to redirect their capital works expenditure?

Mr Marney: In what respect?

Hon LJILJANNA RAVLICH: In respect to contributing to making that $7.6 billion saving over the forward estimates?

Mr Marney: The budget papers, particular budget paper No 3, articulate in full detail the construct of the savings measures. In budget paper No 3 are numerous references to the capital audit processes that looked at the major capital projects valued at over $20 million, from memory, across all agencies. The government sought to interrogate the departments to ensure that, in the context of the rapidly increasing projected debt, all those projects remained an imperative of government, given that many of those projects were introduced into the forward estimates by the previous government. A range of adjustments were made to the capital works program associated with that capital audit process, some of which resulted in the cancellation of projects. Some adjustments deferred or pushed back the time line of those projects. They are all detailed in the budget papers.

Hon KEN TRAVERS: Was that process done on the basis of cabinet making political decisions, or on the process of a cost-benefit analysis of each project?

Mr Marney: In reality, it is both. The Department of Treasury and Finance was asked to undertake a capital audit process, and we did that. We put a series of recommendations to government as part of that process based on not only our assessment of the relative benefit of the projects, but also our assessment of the realistic time lines associated with particular projects and the consequence of not proceeding with particular projects. Those recommendations were put to government in its budget process through its economic and expenditure reform committee and that committee then made its decisions. I assume that it would have its own criteria in that respect, one element of which would be its political imperatives.

Hon KEN TRAVERS: The reason I asked that is there was no funding in the budget for the Premier's stated number one economic project for the state—Oakajee. If it was done on a cost-benefit analysis, or even on a political basis, why would that not be in the budget? Is there a technical reason why it was not in the budget?

Mr Marney: Pretty much.

Hon KEN TRAVERS: And that was?

Mr Marney: That was because the specific nature and extent of government expenditure for that project is yet to be defined. On that basis, although it is flagged as a project that the government is committed to in principle, or to its concept, there is not the degree of costing of the project, or indeed articulation of the precise contractual or delivery arrangements of the project sufficient to enable incorporation of a specific figure into the budget.

Hon KEN TRAVERS: This is where I get confused about how the budget works. If I take you to the Main Roads budget, numerous projects would fit into that same category. They are road projects for which we do not know the full cost, the scope or whether we will receive commonwealth assistance, yet they are included in the budget.

Mr Marney: They are included because there is a great deal more certainty about those parameters.

Hon KEN TRAVERS: Does Roe Highway stage 8 have a greater degree of certainty than Oakajee? We had a briefing from Main Roads last week and its representatives said Main Roads was still not anywhere near understanding what the scope of the project is. The roadworks around Perth Airport, for which the state is also seeking commonwealth funding—I would have thought there was as much detail on those road works as Oakajee at this stage.

Mr Marney: I would argue that there is more detail about Main Roads original costings and concept of the project. There is certainly more detail around the ownership of the asset that flows from that project. That is probably a critical defining factor in the case of Oakajee in terms of who owns what out of that project, given the interaction between the commonwealth-state and private involvement.

Hon KEN TRAVERS: Has a state agreement not already been signed between us and OPR?

Mr Marney: Quite possibly. Whether or not that articulates specifically sufficiently to include a figure in the budget papers, I think the decisions, as communicated to me by the government, were that it did not have a specific figure in mind to provide as a provision for that project.

Hon KEN TRAVERS: Does that mean that the project may actually be greater than the figures that have been talked about? I think the federal government has put in $339 million for that project—correct me if I am wrong.

Mr Marney: It is about $339 million.

Hon KEN TRAVERS: That was about half the cost of the project. Are you saying that there are still enough vagaries about that project that we do not know whether that is the right figure and it could be higher?

Mr Marney: It could be more or it could be less. A decision from government is yet to be articulated to me.

Hon KEN TRAVERS: Has cabinet not made a final decision on what will happen at Oakajee?

Mr Marney: It has not made a final decision to allocate a defined sum of money to the Oakajee project. It may be that it has done that in concept and in principle in terms of the scope, but there are sufficient moving parts to the project that it is not possible for government, at this stage, to tell me what it wishes to spend on that project.

Hon KEN TRAVERS: So when the deal was made between the state and OPR, does that not identify the costs?

Mr Marney: Not to my knowledge, but that is a question for those who made the deal. I did not make the deals.

Hon KEN TRAVERS: Are you saying that the Northbridge Link does not have the level of degree of scope of what the cost of that project is relative to Roe Highway stage 8 or the road projects around the airport?

Mr Marney: It would seem on face value to be a pretty simple project, but I can guarantee that it is not. You might recall that a previous government put a tunnel in the vicinity of the Northbridge Link area not that long ago. There are some engineering complexities in the Northbridge hub project that we are yet to come to terms with. Having said that, again, the government has not yet clearly articulated to me how much it wishes to spend on a given scope for that project. Until such time as cabinet makes a decision and that decision is communicated to me, I cannot put it in the budget papers.

Hon KEN TRAVERS: By that, can we assume that the government has given you that level of detail of scoping for those projects that are allocated in the budget?

Mr Marney: The detailed projects in the budget papers are the projects for which the government has made a decision to allocate a certain amount of money to a given project. The scope and definition will vary from project to project.

[3.00 pm]

Hon KEN TRAVERS: Who does that then; is it you or the agency or the cabinet that makes those decisions? Surely the amount of money you put into a project is done on a bit more than the cabinet doing a back-of-an-envelope calculation.

Mr Marney: Obviously there is plenty of process behind the submissions to cabinet and how those projects are costed and estimated and so on. The government considers that, and when the government feels it has enough information to make a decision, then it will do so and communicate that decision. But if has gaps in its information set or gaps in terms of process in working through issues, whether it be with the private sector or with the commonwealth in terms of funding sources, then it is not unusual to hold back on a firm decision. As I am sure you have all witnessed, once you write a number into a set of budget projections, it is pretty much a done deal, but anyone wishing to draw that down will draw down the full amount of that, whether it be an agency or a private-sector partner or the commonwealth.

Hon KEN TRAVERS: Following that logic, you would not put a whole lot of other projects into the budget; that is the thing I find interesting.

Mr Marney: I think you will find there were not that many new projects added to the budget, so there were existing decisions of government to proceed with a particular project. Main Roads Western Australia is one agency that does its forward-year planning very well; it does it 10 years out. A lot of its approvals are in concept, but it knows it is going to build something, it will probably be largely black with white lines down the middle, and it knows where it is going to go, from A to B.

Hon KEN TRAVERS: Except it could not tell us that about Roe 8 last week in the estimates committee, but anyway that is another story!

Hon PHILIP GARDINER: Under Treasurer, in relation to the budget, the revenue is always difficult to predict and the costs are generally the ones you can hang your hat on, but as Hon Ken Travers has pointed out, it is the interest rate which is one of those costs which is not set. My question has two parts: in terms of the level of interest rates, what scope do you have to try to lock in those rates within the financial market context for the 12-month period of your budget, which of course is the period of risk; your exposure can affect what can happen there?

Mr Marney: The capacity to lock in for 12 months is very good. It is probably more the three-plus years horizon when it gets more difficult, particularly in the current environment whereby it is hard to get money in that longer term time frame. Therefore, 12 months out is fine, and we tend to have a portfolio of debt that we roll over on a pretty frequent basis to ensure that it is a pretty stable interest cost at least for that 12-month period in our accounts. It is really that three to five years and beyond period when the certainty in our interest cost goes up quite significantly.

Hon PHILIP GARDINER: In terms of the portfolio that you have over those three to five years, including the 12-month period, is that market now up to three to five years—for a government instrumentality of our standing, is that still difficult to cover out that far? Is it possible, or is it the margin for doing it too high?

Mr Marney: It is always possible; it is a question about at what price and whether or not you feel you are getting the best value you can. That is something that we assess every time we go to issue with debt security out that far. We assess whether the interest rate risk worth the premium that we are paying on that longer term paper, or should we just roll over a shorter term paper. That is fluid; it depends on the market and market sentiment on any given day. The main thing is, we have a continued presence in the market which means we have a reputation, if you like, as a reliable repayer of debt, and that comes back to issues of credit rating and having enough liquidity in the market so that there is confidence portrayed as to be able to exchange our paper.

Hon PHILIP GARDINER: In the context of the world financial markets, let us say, because that is what we are dealing in, really, do you see the way that you can manage your interest rate risks different to, say, how a corporation might manage its interest rate risks?

Mr Marney: Obviously a AAA credit rating helps in terms of reputation in the market. Probably the only difference to a corporation that we have is that we have numerous instrumentalities that rely on central government borrowing for their debt funding—power entities, water entities, public transport entities—all of which have differing maturity in their asset base and different investment requirements going forward. The capacity for us to manage that risk is through being able to aggregate the various debt requirements of those entities over time, their particular appetite in terms of timing of draw down of debt, being able to aggregate that, smooth that, and then package that, if you like, as a portfolio of debt we can draw from the market.

Hon PHILIP GARDINER: That is very similar to a corporation, really, because you find there is a central bank for each department in the same way that you just described.

Mr Marney: Yes, albeit there are not many corporations around that have got $20 billion per year turnover.

Hon PHILIP GARDINER: Yes, the size of debt; I understand.

Mr Marney: The turnover is a case in point. The level of debt is equal to one year’s expenditure, and an asset base and an economic base as prospective as that of the state of Western Australia.

Hon PHILIP GARDINER: But nonetheless, interest cost as a share revenue is a key performance indicator. Do you have a group, or person, in Treasury who is focusing on interest rate management, given the key performance indicators that are entrenched in the budget?

Mr Marney: We have that covered, I guess, from a couple of different perspectives. One is the operations of the Western Australian Treasury Corporation, which is a separate entity from the Department of Treasury and Finance. The corporation is run under a board governance arrangement, so it has a board of directors, and their job is to ensure that we are raising our debt at perhaps as low an interest cost as possible. That is entirely their role and the role of the Treasury Corporation. In addition to that, as the interface between fiscal settings and the debt requirements of the state, there is, within Treasury and Finance, a public sector finance committee that liaises with the Western Australian Treasury Corporation in terms of its debt issuance program and the state’s requirement of that program.

Having said that, the key issue in the net-interest-cost-to-revenue ratio is not managing the interest rate risk; it is managing the revenue and the expenditures that lead to the interest rate liability. That is where the challenge is and that is really what that indicator is—that target is intended to focus the government on.

Hon PHILIP GARDINER: Except with the expenditure, as I said, most of it is pretty well set. When I say “pretty well set”, it is much more controllable because you have got expenditure on capital or expenditure on wages and all that kind of thing.

Mr Marney: You were not here during the whole three per cent thing, were you?

Hon PHILIP GARDINER: No, I was not.

Hon KEN TRAVERS: I am happy to get back to that!

Mr Marney: It is great to hear that someone thinks expenditures in the state are controlled!

Hon PHILIP GARDINER: Once you set it in a budget, you have got much more control over expenditure than you have over revenue—I think you would agree with that, would not you? You have much more control over expenditure than revenue? Am I still caught on the three per cent, am I?

Mr Marney: No, run with that!

Hon KEN TRAVERS: We would like to think we could.

Hon PHILIP GARDINER: My real question is, the interest cost is still a significant uncontrollable expense, and where I was leading to, Under Treasurer, was that if it was that your people foresaw—and I know this is always about speculation, but you have to manage it, I am afraid—that there was going to be an interest rate rise because of burgeoning economic growth suddenly mushrooming and so on, do you have the risk management approvals in place to allow you to cover yourself against that risk of higher interest rates by entering the forward market stock markets and so on?

[3.10 pm]

Mr Marney: Certainly through entering the swap markets, we are able to manage those risks on a short-term basis. But if there is a sustained tightening cycle in interest rates, using derivative markets will hold us for only so long. At some point we will have to deal with that increase in interest rates. But it does give, if we like, a short-term cover to be able to address what are the root causes of that interest exposure, which is the level of debt and the level of expenditure in the state's fiscal settings. Yes, short term we are covered with enough time, hopefully, to then address some of the underpinning fundamentals as opposed to financial market parameters.

Hon PHILIP GARDINER: Has there been any history of using these derivative markets to try to protect the state against rising interest rates in the past?

Mr Marney: We tend to think of rising interest rates as in monthly Reserve Bank board meetings. But in actual fact, interest rates rise and fall on an hourly basis, so we are pretty much active in those markets on a day-to-day basis.

Hon PHILIP GARDINER: Okay. We might come back to that at a later time. In terms of the credit rating, roughly how much is the margin we would pay over, say, the commonwealth government paper for the same term, given the rating we currently have?

Mr Marney: I do not know what it would stand at today. In fact, I would have to go back to the last few weeks of performance of the paper to give you an accurate assessment. I am happy to provide that as supplementary information.

The CHAIR: If you could, that would be useful.

Mr Marney: It also depends on what we have in terms of an issuance profile in that area. The key point of your question being: in the current environment, what is our spread relative to that of the commonwealth?

Hon PHILIP GARDINER: This is more hypothetical I suspect and you may not wish to answer it: if we did not have the AAA credit rating and went down to the next level, what would be the difference in that margin?

Mr Marney: It is hard to predict what the markets reaction would be. In fact, it is hard to disentangle whether or not the market already assumes that subnationals in the Australian context are operating at a sub-AAA level. A case in point being that, when Queensland lost its AAA rating, we lost a significant margin in price at the same time. There is a degree of contagion in the market. It is very hard to say.

The CHAIR: I had a specific question regarding an item in *The Economic and Fiscal Outlook* on page 43 to do with health sector expenditure. The bit I refer to reads —

> Over recent years, the health system has experienced double-digit expense growth, with escalating demand for health services generating increases in inpatient, emergency department and outpatient activity. The costs associated with hospital services have grown significantly above the rate of growth in activity. Unabated, this trend in expense growth is financially unsustainable.

It states further on -

> The Government's decision to retain Royal Perth Hospital (RPH) as a tertiary hospital and major trauma facility will result in significant recurrent cost implications for the health system. Prior to this decision, it was intended to close RPH as a tertiary facility and transfer associated expenditures to fund the new Fiona Stanley Hospital. The health system will incur significant operating costs in 2013-14 from operating the 400-bed RPH trauma facility and the commissioning of the new 643-bed Fiona Stanley Hospital. These costs are yet to be determined or considered by Government.

Since we are about to contemplate legislation to enshrine this, I wondered if there was anything else you would add to that. It is fairly broad but I wonder whether there is some other guide to us. We must make a decision on this bill very shortly. What are the budgetary implications of trying to achieve both those things? Would the government have to look for cuts elsewhere in the health system to balance the books?

Mr Marney: I think the bottom line from those two paragraphs is that, at this point, I do not believe we have adequate funding in place for the retention of Royal Perth Hospital. The words did seem quite familiar when you read them out just then. They did appear over the weekend. It is a serious issue because, to be quite blunt, I do not know where the money is going to come from. It is a matter, as the paragraph points out, that the government is yet to quantify or consider. It may be that the Minister for Health has a plan. He has publicly articulated that this is achievable without additional impost on the budget. I have not been able to receive any assurance from the Department of Health that that is the case, but I am sure we will get together and discuss it and someone will let me know at some point. But I think it is an appropriate question for Parliament during the debate of that legislation. I cannot answer that question for you.

Hon KEN TRAVERS: Not to mention the need for growth at other hospitals such as Joondalup Health Campus in the same period.

The CHAIR: It struck me that we will need that information before we can make a genuine decision about whether to support legislation. That was a rhetorical question; it was not a question of you, Mr Marney.

Mr Marney: I took it as such, but nodded in agreement.

Hon LJILJANNA RAVLICH: Given that the minister has said that this can be achieved—he made that statement publicly. On page 42 of the *Economic and Fiscal Outlook* under "Health Sector Expenses" reference is made to the government's decision to retain Royal Perth Hospital as a tertiary hospital and major trauma facility. That will result in significant recurrent cost implications. The paragraph ends as follows —

> These costs are yet to be determined or considered by Government.

Either Treasury or the minister is correct, but you both cannot be correct. What is your response to that, firstly?

Mr Marney: I think it is an accurate statement to say that both parties cannot be correct.

Hon LJILJANNA RAVLICH: Is the Economic Audit Committee involved at all in working with the Minister for Health in helping him determine his position on this issue?

Mr Marney: No. This is not within scope of the economic audit as such, but it is part of normal ongoing interactions between the Department of Treasury and Finance and the Department of Health. As I pointed out, I have raised these concerns, obviously. The Department of Health has yet to confirm that the funding of Royal Perth Hospital on an operating basis under the government's commitment can be done within its existing resources.

Hon LJILJANNA RAVLICH: Have you consulted with the Minister for Health on this matter aimed at determining why there is such a variation between Treasury's and his position on this matter?

Mr Marney: Yes, and I do understand the difference in the position.

Hon LJILJANNA RAVLICH: Can you explain what his argument is as opposed to Treasury's argument on the variance in position on this matter?

Mr Marney: I think explanation of his argument is best done by him.

Hon LJILJANNA RAVLICH: That is a fair comment. What is your position on why you argue that there will be insufficient funds to meet the costs of operating both hospitals?

[3.20 pm]

Mr Marney: The reconfiguration of the health system came about as a consequence of the Reid report into the reform of the Western Australian health system. As part of that process there was a reconfiguration of beds across the metropolitan health system to try to get a better fit between the location of beds, the appropriate level of care that was required to have that delivered in an appropriate cost setting, and to also look at issues of duplication between particular sites. Since then, a lot of time and effort has gone into modelling the implications of the reconfiguration of the health system, including effort into understanding the recurrent cost implications of the various substantial capital projects that are currently underway. As part of that process, the expectations for recurrent expenditure across the system were optimised within a total-bed constraint. That bed constraint has not changed; therefore, if you suddenly add to the system the retention of some 400 beds that were previously anticipated to be lost from the system and to go elsewhere, then I cannot see how that does not have recurrent cost implications and that those implications cannot be significant. As I said, I have sought confirmation of the minister's position from the Department of Health and they do not concur with this view.

Hon LJILJANNA RAVLICH: In your opinion, do you think that the minister has locked himself into a corner by making an election commitment in respect to Royal Perth Hospital without fully comprehending the makeup, if you like, of the health system and the tertiary and secondary hospitals within it at the time he made that promise?

Mr Marney: It would be inappropriate for me to comment on the degree of comprehension of the minister at that point in time.

The CHAIR: Yes, that is slightly out of order.

Hon LJILJANNA RAVLICH: Okay, well can I ask you something a little closer to home; that is, how close are we to losing the AAA credit rating?

Mr Marney: Again, that is a matter of —

Hon LIZ BEHJAT: Conjecture.

Mr Marney: Yes, but it is even worse than that because the credit rating is something that, although the state adopts half a dozen fiscal parameters as its target, the rating agencies will look at in excess of 50 financial parameters. We sit down with them, usually once a year, in a full day of briefings and run through those various parameters. They take a number of months to then digest, query, question and interrogate those parameters before coming back to us with their eventual position, and there is no hard and fast rule. There is no "if you breach this level on a particular ratio, then you're done—you're a AA+ or you're a negative watch", so to judge how close we are or otherwise to losing AAA is a very difficult thing to do but what the rating agencies do rely on is that the government sets a series of fiscal targets for itself and it sticks to that plan.

Hon LIZ BEHJAT: On the health sector expenses, again on that same page, the very last line of that second paragraph states —

> These costs are yet to be determined or considered by Government.

Therefore, at the time of publication of the budget those costs were not available or, as far as you are concerned, not considered, but it does not mean to say that the money is not there somewhere to fully fund both the 400 beds in Royal Perth Hospital and the Fiona Stanley Hospital. So, today we cannot be going out of here saying, "Oh, look they don't have the money to do it; therefore, they can't meet that election commitment." Would you agree with that?

Mr Marney: I am glad I deliberated on these words fairly diligently. The fact that these costs are yet to be determined or considered by government remains a fact, so I do not know if there is something else in terms of system reconfiguration that the Minister for Health has in mind that may mean that there is zero impost on the state's budget—I do not know. Therefore, the, I guess, factual accuracy of that sentence remains.

Hon KEN TRAVERS: I am glad you reminded us about the three per cent hearings and I want to go back to that. On 24 March in one of those hearings you made the statement to a subcommittee of this committee —

> It is my view that the numbers as presented in the midyear review were financially unsustainable, yes.

That was your evidence to the committee. I guess my question is: are the numbers that are presented in the 2009-10 budget financially unsustainable?

Mr Marney: Are you capturing the gravity of the pause?

The CHAIR: I was thinking you might have nodded off actually!

Hon KEN TRAVERS: I was trying to work out how you get Hansard to record the pause!

Mr Marney: It is a very, very difficult circumstance. What I would say is that I think the budget did as much as it could to protect the state's finances. Although it would be nice to see a healthier structural position of the budget parameters, certainly every effort has been made to ensure that that would be the case. The environment we are in at the moment in terms of the volatility of some of the financial parameters and revenue parameters makes it extremely difficult but the measures that have been implemented, including what I would see as the successful implementation of the three per cent savings initiative—success based on the fact that over 97 per cent of that quantum was achieved—has been realised in the budget settings.

Hon KEN TRAVERS: I was going to say it has not been realised yet; it is in the budget to be realised but we have yet to see it materialise in many agencies.

Mr Marney: It is embodied in the expense limits that have been set for agencies, so in that respect it is done. That does not mean it is not difficult. There are plenty of hard measures in the budget, many of which are subject to criticism on a daily basis. So to say that everything has not been done that could possibly be done to ensure that that $19 billion debt figure is held down as much as possible—we have done our best. Are the budget aggregates sustainable? We have probably got a ways to go to get them to a sustainable position.

Hon KEN TRAVERS: One of the things is when you look at the key budget aggregates per what was in the midyear review and what is in the actual budget, the revenue is virtually unchanged and if anything has actually increased slightly over what was predicted in the midyear review. Expenses have actually grown, and you indicate you are confident about the three per cent but in the midyear review we were expecting a 12 per cent growth in expenses per the 2008-09 year, and in the actual budget you are now expecting that the actual outcome will be 13 per cent. Then when you go through all that, even though we have significantly downgraded the amount of capital works that we are doing, if anything has been reduced it is the asset investment program, but we are still actually ending up with the same or increased expenditure on recurrent expenditure. The net-debt-to-revenue ratio is up, which at that stage was the only measure we had in the midyear review.

Mr Marney: Is there a question in this?

Hon KEN TRAVERS: You say we have taken the measures, but what measures have we taken? That to me does not actually show any significant measures being taken, other than some capital works being deleted and others being brought forward.

Mr Marney: All you have to do is pick up a copy of *The West Australian* every morning and you can see the latest measure that is being attacked. There is about $7.6 billion worth of measures that were previously discussed embodied in the budget and that cuts across a range of areas—in some respects, across every agency in terms of their procurement spending and their spending on government vehicle fleet.

It cuts across areas of lower priority service delivery, and it cuts across areas of cost recovery for services, where people have discretion as to whether or not they consume those government services. To say that there is not much there is probably —

[3.30 pm]

Hon KEN TRAVERS: I guess I am talking about in aggregate terms.

Mr Marney: I am assuming you would support all the measures, then, if there is not enough there.

Hon KEN TRAVERS: This is what I cannot understand. In aggregate terms, you can talk about the $7.5 billion that is being cut, but the expense growth between the midyear review and this budget has not been cut, other than for some capital works projects, and even then, we have the Roe Highway. I hate to keep coming back to it, but it is a $550 million project; it is not an insignificant project. It has been brought forward. You have cut roads like the Collie Coalfields highway and replaced it with bringing forward Roe Highway stage 8. In aggregate terms, where are the cuts? We still have expense growth in 2011-12 of $21.739 million. The midyear review was predicting expenses of $20.356 million. The $7.5 million, you can talk about it, but it has just been replaced by other expenditure.

Mr Marney: The growth in expenses, again is articulated fully in the budget papers, and summarised in budget paper No 3, in some detail. A key component of that growth in expenditure is the implementation of election commitments and it is fair to say that some of the implementation costs have changed slightly from the midyear review. There are many moving parts to the expense base. While is easy for me, as Under Treasurer, to say that I would like to see a healthier set of numbers, I am not the one with the political contract with the electorate. The government made its commitments and it is implementing those commitments. That is the bottom line. I would like to say that Roe stage 8 is an explanation for that, but it is not, because it is a capital expense.

Hon KEN TRAVERS: That is on the capital side, but still in terms of the expenditure side, the three per cent savings were already factored into the midyear review, and the election commitments were factored into the midyear review.

Mr Marney: A big part of the growth in expense is in the area of salaries and a number of enterprise bargaining agreements have been entered into as well, police being the case in point, where the government settled a wage negotiation, and the budget had a provision for those negotiations.

Hon LJILJANNA RAVLICH: Just as a follow on from that—I am glad you raised it because I was going to go on to community service obligations, but I think I will follow up on this one—I assume that the wages policy is one of the assumptions on which the forward estimates are based, and a very important one also. The first question I want to put to you, Under Treasurer, is, does the additional cost of the new police agreement mean that there will now need to be an adjustment to the budget, or had the costs of the new agreement been budgeted before because it had been a variation, an increase upwards had been anticipated prior to the budget having been brought down? Is that clear? Do you now have to go and make an adjustment because you had had the government wages policy, and thought it would stick, but now a higher rate has been paid?

Mr Marney: The budget incorporated the offer that was on the table at the time of the budget, and I think that varied slightly from the government wages policy. The government actually articulated that the police agreement would not be subject to that policy, because it was the last on the previous wave of agreements, so it is likely that there will need to be some slight adjustment to the funding provided for the outcome of that EBA.

Hon LJILJANNA RAVLICH: If the police settlement is applied to nurses and public servants, what would be the additional unbudgeted cost?

Mr Marney: I have no idea, off the top of my head.

Hon LJILJANNA RAVLICH: Would it provide you with a problem in that the one of government's assumptions upon which this budget is based would be breached?

Mr Marney: It would obviously mean that expenses grow by more than is currently expected. If everything else is equal, then debt goes up.

Hon LJILJANNA RAVLICH: Did you model the various impacts of different wages policy across the budget, and in particular did you model what the additional cost would be over the forward estimates, for example, if the nurses' settlement is one per cent above the wages policy? Have you done that sort of modelling?

Mr Marney: Not across the board. We would do that normally in the process of providing advice to the government as each particular EBA comes up for renegotiation. We would ensure that the government has an understanding of the financial sensitivities associated with that round of negotiations.

Hon LJILJANNA RAVLICH: Given the importance of wages policy, and the fact that it is an assumption underpinning this budget at this stage, are you saying that Treasury has not provided modelling of how much a one per cent increase above the wages policy would mean in additional costs for nurses, public servants and teachers? Is that what you are saying?

Mr Marney: We have not done modelling on those specific occupations groups, no.

Hon LJILJANNA RAVLICH: Do you think it might be a good idea to do that modelling, given how tight this budget is?

Mr Marney: If I had people sitting around not doing much, then, yes, it would be very interesting. There are always very large components of the budget that are under active management. We would turn our mind to the active management of that sort of parameter as we head into those larger rounds of EBA negotiations. The forward estimates have assumptions for salaries growth across them, which reflect what we have modelled as the long-term growth trends in wages and salaries in total. There is some coverage in that respect, in that we do look at those long-term trends and factor them into the forward estimates.

Hon LJILJANNA RAVLICH: Have you factored in a little bit of fat in the event that, when the nurses, the public servants and the teachers meet with the government to settle their wages claim, they cannot reach agreement? Have you factored in, or just put in a little bit of extra fat as a bit of a buffer for the government?

Mr Marney: The short answer is no. The long answer is, why would you declare it?

Hon LJILJANNA RAVLICH: So you did!

Hon KEN TRAVERS: If he did, he would not tell us anyway!

Mr Marney: Let us be honest, if you are going into rounds of negotiations, you are not going to actually declare that you have got X hundred million up your sleeve.

Hon LJILJANNA RAVLICH: Just for the committee, not the public!

Mr Marney: Just between us!

The CHAIR: And the readers.

Mr Marney: That is why, in the out years, we do look at the longer term aggregate of wages—the full wages bill for the public sector—and we have that model through the forward estimates, rather than specific outcomes for specific occupational groups.

Hon PHILIP GARDINER: An easier blow-out to measure—the foreign exchange rate movement. To what extent has that changed the revenue at this stage, especially what is left outside the royalties for regions, in relation to the royalties and the earnings we are generating from the royalties?

Mr Marney: The exchange rate parameter is set out in the budget papers. For every one-cent variation in the exchange, there is a $55 million dollar variation in royalties receipts. If the exchange rate appreciates by one cent, we lose $55 million per annum in royalty revenue.

[3.40 pm]

Hon PHILIP GARDINER: Was the exchange rate set at 68c?

Mr Marney: Yes, 68.5c, and we are currently just above 10c over that.

Hon PHILIP GARDINER: So it is $550 million.

Mr Marney: That is correct.

Hon PHILIP GARDINER: It is easy in my position to say but it was difficult in that position at the time because who knows which way it is going to move, but it is a big variation. That does not mean today that it will all be back there in 12 months' time either, so it might all be fine depending how the royalties are calculated across time during the year. We have had a brief discussion on it. I suspect there may be ways of protecting that, which at this stage the Treasury has chosen not to pursue. Is there a time when you would consider pursuing the possible management of that risk when it could have a significant impact upon a year's budget result?

Mr Marney: I think the first question is: what is the implication of the budgeting assumption of using the six-week average as the assumed exchange rate for the next four-and-a-half years? If the exchange rate is buzzing around its long-term average, then that is not a problem, that is fine, but in the past 10 months we have seen the exchange rate vary 30 per cent down and then up. Normally we would have a natural hedge relationship between commodity prices and the exchange rate. So when commodity prices fall so too does the exchange rate, reflecting what we think is the fundamental economic relationship. We have seen those relationships breakdown and turn horrible in the past 10 months. It is in that sort of environment that we do start to think very seriously about hedging arrangements, but it is also the environment when it is probably too late to start thinking about hedging arrangements. The natural hedge over the long run has been our best bet. Over the past 15 years of my involvement in Treasury matters, we have examined this question on a handful of occasions, and each time we have come to the conclusion that the long-run relationships and natural hedge relationships are sufficient to protect the state. It is the circumstances of extreme volatility that we are experiencing at the moment when it does not work. Whether or not you enter hedge arrangements, it is too late to do that now. Once we come out of this current environment and the dust settles a bit, then we will be analysing it fairly intensively to know whether or not we could have done better in a counterfactual scenario had we taken out hedge arrangements in advance, but it is too late to do it now. The premium you pay is just not worth it.

Hon PHILIP GARDINER: Is that analysis that you have made, Under Treasurer, in the previous years a public document?

Mr Marney: I will have to go back and check. The last analysis I think would have been undertaken in about 1997. It is usually done as part of an expenditure revue committee-type process. It may be that it is not public, but I will check if I can take that on notice.

The CHAIR: Thank you. Mr Marney, I believe you need to be somewhere at four o'clock. Is that correct?

Mr Marney: I am having so much fun here I am prepared to stay a bit longer, but I think my parking meter runs out at half past four. Actually it runs out at five past four!

The CHAIR: Perhaps you might indicate how long you —

Mr Marney: It is fine.

The CHAIR: I just did not want to run you out of time.

Hon KEN TRAVERS: I just want to get a sense of how it operates to try to understand better the interaction of appropriations versus cash and the situation we are currently in. As I understand it, we have now run out of cash. We have used up all that remains of the existing loan appropriations, so the only cash we would now have is cash that comes in as receipts to the government.

Mr Marney: Yes.

Hon KEN TRAVERS: What is the current situation in that regard, and how do agencies manage that situation? I can understand that in terms of meeting what was expected we are about $225 million short of the amount of cash that we will require to see out this financial year. I guess I am trying to work out how individual agencies manage that situation. Does it mean they cannot expend the money that they would be getting under the Treasurer's Advance Authorisation Bill? If you could give us an understanding of it for dummies—appropriations versus cash?

Mr Marney: Yes. Basically, once the appropriation is authorised by Parliament, then we will strike agreement with relevant agencies on what is called a disbursement profile through the financial year. It is usually done fortnightly. That profile specifies how much agencies will be able to draw down out of the appropriation each fortnight to cover their expenses. In the current environment, where without the passage of the Loan Bill we will get very tight on cash, and in fact fall short, then we will look at where are the big chunks of disbursement between now and 30 June and what chunks of those can be managed, deferred or avoided in order to ensure that we do not run out of cash altogether. The short answer is that we manage the disbursements to the agencies in accordance with how much cash we have got left at the bank.

Hon KEN TRAVERS: Can you give us an example of the sort of payment you are talking about that you would have to defer? The agency may still appropriate it but just not pay it out. Is that what you are saying?

Mr Marney: No, it is Parliament that appropriates the money to the agencies.

Hon KEN TRAVERS: Sorry. When I said "appropriate", I should have said that the agency can still incur the expense but it just will not pay people for it.

Mr Marney: No, it may be that it cannot incur the expense. My hope would be that we do not get to that point and that in actual fact the Loan Bill proceeds through the Council. Whatever you can do in that regard would be much appreciated.

Hon KEN TRAVERS: I just get confused when the Treasurer says it is not that urgent, that is all; that you can all manage. That is why I am trying to understand how it all operates, to get a better understanding of what is the urgency.

Mr Marney: As I am sure you would appreciate, the fortnightly financial flows within the sector can be pretty substantial. If the Loan Bill does not pass and we run out of cash capacity, then we will look at those various flows and recommend adjustments to government in order to live within the cash pool that we have available. Now I cannot tell you exactly what particular items within those flows we would look at. That is really a matter that we would discuss with the government, and ultimately it would be its decision.

Hon KEN TRAVERS: I am trying to get a sense of an example of the sort of thing that you could defer the incurring of. Wages and salaries—short of laying off people between now and the end of the financial year—I cannot see that happening. Do you tell agencies that they cannot drive their motor vehicles for the next two weeks because they do not have the cash to pay for it?

Mr Marney: It may be that there are expenditures of agencies where timing—whether it is paid next week or the following week—does not matter. It may be that agencies have grants expenditures outside of the sector where five days does not make a difference. Those are the sorts of things we look at.

Hon KEN TRAVERS: That is where they are paying out a grant to some other agency, so they do not incur the expenditure until they have physically paid money out. Is that right?

Mr Marney: Yes.

Hon KEN TRAVERS: That would be grants to NGOs. Say it was to local government, does that then not have a potential flow-on ramification to budget management for those other agencies' meeting their cash flow for the end of the financial year?

Mr Marney: That is what we would look at pretty intensively. I guess the question of what would not be spent or what could be sacrificed in that process is really a question for debate in the upper house through this week on the Loan Bill. It is not something that, with respect, was a topic of this discussion this afternoon.

[3.50 pm]

Hon KEN TRAVERS: I am more interested in the bigger picture of how the financial arrangements operate. I thought I would get a clearer answer from you than I might from Chinese whispers from you through the minister representing the minister in terms of understanding how the process works and operates, without the specifics.

Mr Marney: In very broad terms, we will look at all the parameters that move within the disbursements over the next 10 days, and we will make sure every single one of those movements is absolutely drop-dead necessary. It may be that there are some grants to third parties in which we would test whether or not we could hold off on those grants. Agencies at any point in time have various creditors on their books, and whether they are being managed to reflect current circumstances is a question we would ask.

Hon LJILJANNA RAVLICH: Madam Chair, I wonder if could ask the Under Treasurer some questions in relation to expenses from government in relation to public corporations. On page 172 of budget paper No 3, *Economic and Fiscal Outlook*, reference is made to "Addressing the Sources of Spending Growth". It states on page 173 that the audit committee identified that Western Australia spends around 20 per cent more than other states on transfers, both as a percentage of general government expenses and per capita, and the audit committee, having looked at these transfers, found that the policy objective of transfers is generally ill-defined, resulting in poorly targeted and unevaluated expenditure. The audit committee also found that many of the existing transfers to individuals and households alter price signals in the market, resulting in perverse or unintended consequences that on occasions undermine other policy objectives. Therefore, the committee does not perceive these things to be particularly effective or, in fact, they can be quite dangerous, if one follows that reasoning. A whole range of these are listed on pages 280 and 281 in the same budget paper.

I refer in this instance to "Country Water, Sewerage and Drainage Operations", where the Under Treasurer will see that for 2009-10 an allocation of $351.3 million and that across the forward estimates it accounts for about $1.3 billion. However, we could equally be talking about some of the other community service obligation in terms of the general principles underlying these CSOs. In your view, given the policy parameters outlined by the government, can the future of CSOs be assured?

Mr Marney: It really depends on the policy in progress of government. The construct of CSOs—if I can make a distinction between a CSO payment versus a transfer payment.

Hon LJILJANNA RAVLICH: Yes.

Mr Marney: A community service obligation payment is a payment from central government to a public trading enterprise to reflect the cost impost on that trading enterprise of a noncommercial nature of community service obligations that the government wishes that trading enterprise to meet. For example, if government is of the view that electricity prices should be X, and the cost of those is X plus Y, the CSO makes up the difference. That is the government's policy decision. That is different to a transfer payment, which may be a payment to a household or an individual to subsidise the consumption of a particular public good. It may be water, electricity or whatever. In principle, CSOs are a sound tool to reflect the cost impost of government's decision making, and I would not see those disappearing from the colourful fiscal management landscape. With transfer payments, on the other hand, the Economic Audit Committee found there were a large number of transfer payments; indeed, the vast majority, in excess of 90 per cent, I think, of households receive some form of transfer payment or other, quite possibly without knowing it. Those payments have emerged over a long period of time with successive governments and successive policy settings. The point that the Economic Audit Committee was trying to make was that at some point we need to go back and have a look at those and ask whether they are consistent with, first, the policy settings of the current government and, second, if they are, is the transfer payment achieving that policy objective.

Hon LJILJANNA RAVLICH: When Western Power pays money into a fund that goes to subsidise the loss to Horizon Power for the power it distributes in regional areas, is that a transfer payment?

Mr Marney: It is not of the nature that the Economic Audit Committee was concerned about, in particular. The committee was saying that there are a range of these payments, and if there is a transfer payment under that definition it may be that it is valid and consistent with government's policy objectives. But the committee was saying that at some point we need to go back through this and have a look. The committee was not passing judgement as to whether or not they were robust.

Hon LJILJANNA RAVLICH: But they are currently being investigated with a view to assessing whether they should remain or should be handled in a different way?

Mr Marney: That is one of the varied elements of the committee's activities at the moment.

Hon LJILJANNA RAVLICH: Is it possible to get a list of the ones that they are looking at?

Mr Marney: The audit committee deliberations and recommendations are provided to cabinet and, as such, they are, if you like, deliberative documents and that is probably something that I would need to seek clearance from the Treasurer on, if the committee is happy for me to do that, and respond.

Hon LJILJANNA RAVLICH: That would be good.

The CHAIR: Thank you. That will be useful.

Hon KEN TRAVERS: I had a couple of questions on the structure of the budget and how it is prepared. Is appendix 5, which is the election commitments, intended to identify all of the commitments or only those that have received funding?

Mr Marney: I have a pretty black and white view of the world, as you would know. If an election commitment has a funding implication and it is a commitment that the government wants implemented, then it should be in that appendix. If it is not there, it is not funded and not being implemented. That may be for a number of reasons, one of which being it does not cost anything.

Hon KEN TRAVERS: No. There is one that I can think that has been deferred outside of the budget period, so it does not appear there. However, in terms of someone wanting to track through the budget to find the election commitments and whether they have been funded, where would I find that information? Should it be in there?

Mr Marney: Yes.

Hon KEN TRAVERS: Because there are some that are not. The Collie coalfields highway, of course, is not there.

Hon LIZ BEHJAT: What is missing?

Hon KEN TRAVERS: That is the problem! We have to work out what is missing; however, I know that the Collie coalfields highway is not in the budget. That is why I am trying to work out whether everything should be in there and whether there has been a funding allocation to that project.

Mr Marney: Every decision of government associated with an election commitment should be captured in budget paper No 3 in one form or another, whether it is in the appendix or the chapters on policy decisions.

Hon KEN TRAVERS: The other issue I raise goes into general budget paper issues, and is feedback to you about the new structure. With the change to capital works rather than the asset investment program, one of the things I find difficult is trying to track projects through there. There are some projects that have been taken out and turned into grants, so they suddenly appear under details of controlled grants and subsidies. I am not exactly sure why, but when we get to sport and recreation I will ask that question.

Mr Marney: The reasoning why—and this is the key underpinning of that change in definition—is if money is spent and it creates an asset on the state's balance sheet, then it is in the asset investment program. If money is spent and it does not create an asset on our books, it must be money that is given to someone else and someone else gets the asset; therefore, it is not in the capital program because we did not build anything, someone else did.

The fact that we fund it is a key consideration. You will find that most prominent probably in some of the road space—the state grants to local authorities to build a road, and it is a local road rather than a state road.

[4.00 pm]

Hon KEN TRAVERS: I guess the question for us as MPs, though, is: is there any way of having in the budget papers some sort of note that actually identifies those projects that have been deleted—that says they are no longer state projects and the money has gone to some other agency—so that we can track them? Also, the other thing that Main Roads does is change the title of the project, which makes it difficult if we are trying to follow a project from one year to the next. Is there any way of again having some sort of note that says, "The majority of the funding that was provided to X project is now captured in Y project"?

Mr Marney: I thought we had done some reconciliation between the two definitions. I am happy to explore that further, if required, and at least give you a stock take of those projects that were previously in and that are now out and classified differently, and where they are classified. I am happy to provide that. To respond in part to your concerns, and also to my own concerns, about tracking projects over time, under the new structure we now have a much better articulation of the—I almost said capital works program—asset investment program over the budget year, and now the forward estimates, to try to give that whole picture of spend. So hopefully that has come through as an improvement in the transparency of those settings.

Hon KEN TRAVERS: My next question relates to the new southern tertiary hospital, or Fiona Stanley Hospital as it is better known. My understanding is that the money in the account for that hospital is expected to fully fund that hospital. However, if interest rates remain low—that is, if they continue to remain at the level that they are at now—there may not be sufficient funds in that account to fund Fiona Stanley Hospital. Is that correct?

Mr Marney: That could well be the case. I think the original allocation to that account was $1.2 billion, consistent with the original budget setting for the project. Interest has then accumulated on the project account, which has covered most of the increase in budget to $1.749 billion. It may be that there is a shortfall.

Hon KEN TRAVERS: Right. That goes back to my earlier question about interest rates. If the budget is predicated on interest rates being at a certain level that would allow you to fund Fiona Stanley Hospital, but if interest rates do not reach that level, you will potentially have a shortfall in the funding for Fiona Stanley Hospital. It is again a bit of a chicken or egg situation, because you will either have to find more money to fund Fiona Stanley Hospital, or you will need to have higher interest rates, and that will have an impact on our net-debt-to-revenue ratio.

Mr Marney: The good news is if we do not meet the full funding from interest earnings, because interest rates are —

Hon KEN TRAVERS: Low, which is good.

Mr Marney: Yes, low, that will mean that our interest-cost-to-revenue ratio is going to be okay, which completely nullifies your previous conversation around the same issue.

Hon KEN TRAVERS: But then will you not have the problem that you will have to find additional capital expenditure to fund the shortfall?

Mr Marney: Yes. That is just another one of the myriad balls in the air at any one point in time.

Hon KEN TRAVERS: So your borrowings will need to go up. That is what I am trying get to.

Mr Marney: Yes.

Hon KEN TRAVERS: If we do maintain interest rates at the low level that the budget is predicated on, that may have other implications in terms of —

Mr Marney: Which is fully factored in. We use the same interest rate settings across all budget parameters that are sensitive to interest rates. Maybe I can alleviate a potential dark concern that we have manipulated the interest rate settings in the budget to get a particular outcome. They are based on Treasury Corporation’s forward projections of what it thinks it can borrow at over time. So we have not taken off half a per cent because it makes us look better, or whatever. It is straight down the line.

Hon KEN TRAVERS: I am not suggesting that there is any manipulation. I am just trying to get an understanding of the total picture. As I understand it, the margin between the interest rate you will receive and the interest rate that you will borrow at is expected to be around—I cannot quote the exact figure—a 1.5 per cent differential at the moment. In the out years, in terms of the assumptions that have been made, it drops to only about 0.5 per cent. Can you explain to us why there is that expectation that the margin between the interest received on your money—cash at bank—versus the interest that you pay will diminish so much over the four years?

Mr Marney: Essentially, it is going from a very unstable and volatile environment into an assumption of a steady state—that is, what has been our historic performance. That is the simple answer.

Hon KEN TRAVERS: So that 0.5 per cent is about the historic margin?

Mr Marney: That is my understanding, yes.

Hon LJILJANNA RAVLICH: The *2009-10 Budget Overview* states at page 13 —

> In order to provide the funding for the range of initiative contained in this budget, difficult decisions have needed to be made.

It goes on to say that these tough decisions have involved savings of $7.6 billion over the forward estimates. I would like to ask you a series of questions about that. I have already asked you about the redirection of capital works expenditure by agencies. Has Treasury instructed or asked agencies to identify surplus government land and/or assets that could be sold; and, if so, could Treasury provide a list of the land and/or assets earmarked for sale if those lists have been finalised?

Mr Marney: Yes. I think there is a target of $250 million worth of landholding sales to be realised over the forward estimates.

Hon LJILJANNA RAVLICH: That is over the forward estimates?

Mr Marney: Yes.

Hon LJILJANNA RAVLICH: Has Treasury asked agencies to identify those parts of their operations that could be privatised, or any functions that could be contracted out; and, if so, has there been any identification of functions that could be privatised or contracted out?

Mr Marney: That figure of $250 million relates to landholdings and physical assets. It does not relate to operations.

Hon LJILJANNA RAVLICH: Do you have a figure for operations?

Mr Marney: No, we do not.

Hon LJILJANNA RAVLICH: Are you working on one?

Mr Marney: No, other than the specific items that are identified in policy decisions within particular agencies. I think the Department of Transport would be a case in point, where there is a policy decision with respect to the greater use of private partners in the provision of licensing services. So there are pockets within the budget papers, but nothing global around an outsourcing target or a privatisation target in any form.

Hon LJILJANNA RAVLICH: Has Treasury asked agencies to reduce staff numbers over the next four years; and, if so, what ceiling has been set, and how many staff are expected to be shed over the forward estimates period?

Mr Marney: The staff numbers are detailed in the budged papers and matched to the financial statements and the expense limits set for agencies that are consistent with their appropriations. Those staffing numbers are provided by the agencies themselves and marry up with the overall budget capacity that they have.

Hon LJILJANNA RAVLICH: Do you have a figure for that?

Mr Marney: I do not have a figure as to what those particular FTEs across the agencies sum to. I suspect it is very close to 100 000.

Hon LJILJANNA RAVLICH: How much will that be reduced to—from 100 000 to whatsoever—over the next four years? What is the target cap?

Mr Marney: There is not a target reduction over the next four years as I understand it. There is a government policy decision at this point that stems from a cap for 2008-09.

Government is considering that issue in the context of the 2009-10 budget year. The FTEs are capped for each agency in the context of the FTE that they have articulated to Parliament as their FTE level for the budget year.

[4.10 pm]

Hon LJILJANNA RAVLICH: Can I just say that your answer is a little bit inconsistent with what is in this budget overview which talks about a saving of $7.6 billion over five years across government. It specifically refers to a ceiling on public sector employee numbers, yet you are telling us that there is a cap for 2009-10 but that there is not a cap across the forward estimates in terms of FTE numbers. That is not what is implied in this document. I ask whether it is possible for you to provide the committee with some explanation or if it is possible for you to give us the table target reduction over the forward estimates—either would be good.

Mr Marney: The $7.6 billion relates to expenses, and those expense savings are built into the budget numbers. The budget numbers have with them the FTE cap for each agency, so it is articulated in the budget papers.

Hon LJILJANNA RAVLICH: I do not want to waste three weeks doing the numbers. Treasury must have an up-to-date figure on how many public sector employees there are; what the target reduction is over the forward estimates; and—if we have 100 000 in 2009-10—how many FTEs we will have in 2012-13. I think that is a reasonable enough question.

Finally, the last —

The CHAIR: Can I just check if it is possible to provide that information?

Mr Marney: It is probably a reasonable enough question for the Public Sector Commissioner rather than the Department of Treasury and Finance. The Department of Treasury and Finance deals in expenses and dollars and the Public Sector Commissioner deals with the level of FTEs and the reporting of FTEs to Parliament. I am happy to provide a report on the 2009-10 level of FTEs embodied across —

Hon LJILJANNA RAVLICH: But surely the number of FTEs has a dollar figure attached to it and so from that point of view I find it hard to understand how this budget or parts of this budget could have been put together without an understanding of the FTEs across the whole —

Mr Marney: The FTE figures, as I have said, are articulated in each set of financial statements for each agency—so, yes, they do have an FTE associated with them. My recollection is that FTE is a 2009-10 figure only, because that is all we asked the agencies for. It may be that in the out years the agencies reserve flexibility to expend their expense limit through other means: other than wages and salaries and FTE. I can give you a figure for 2009-10 of the current number within the budget parameters.

Hon LJILJANNA RAVLICH: Finally, in terms of limiting expenditure, what private-public partnerships are anticipated to be entered into, and have you instructed agencies to provide you with possibilities in the respective agencies about what PPPs could be entered into as a way of reducing cost to government over the forward estimates?

Mr Marney: We have not instructed agencies but we are certainly actively looking for opportunities to partner with the private sector as a means of reducing our costs and getting better value for money out of taxpayers' dollars. We are doing that as part of our role in implementing government's policy settings around private sector involvement. We are exploring those opportunities in a number of areas and we will evaluate those opportunities in the context of that very question: is it best value for money for taxpayers' dollars? We are in the process of assembling a team that can do that in a robust way so that we do not—any of us—fall into the trap of pursuit of philosophy over outcome.

Hon LJILJANNA RAVLICH: Thank you.

Hon KEN TRAVERS: You mentioned earlier the 10 per cent reduction in the government car fleet. You suggested that it was one of the corrective measures incorporated into this budget. Is that correct?

Mr Marney: Yes.

Hon KEN TRAVERS: Off the top of your head, would you have what the four-year saving is expected to be for that?

Mr Marney: I think $60 million rings a bell but I would have to check on that.

Hon KEN TRAVERS: All right. Is it factored into the budget as being a four-year saving in each year or is there a reduced saving in the 2009-10 financial year?

Mr Marney: I am pretty sure that there is a discount in the current year.

The CHAIR: It would be good to find that figure.

Hon KEN TRAVERS: Yes.

Mr Marney: There are about four parameters: state fleet; procurement savings; the $250 million asset target mentioned before; and the 15 per cent reduction in grants. They have varying profiles in terms of cash flow, reflecting the difficulty in targeting and implementing those measures immediately.

Hon KEN TRAVERS: Are you able to tell us where they would appear in the budget papers?

Mr Marney: They would be in budget paper No 3.

Hon KEN TRAVERS: Certainly the provision of $250 million in land sales is separately identified as one of the corrective measures but those other three that you have mentioned do not seem to appear in the budget paper No 3.

Mr Marney: It should be in the policy decisions chapter, General Government Expenses, in budget paper No 3—expense policy decisions by portfolio. The headings are Procurement Savings and Grants Programs, both of which appear on page 83. At the moment those savings are held centrally, to be implemented and incorporated in agencies' budgets ahead of the midyear review.

Hon KEN TRAVERS: I am still trying to find the motor vehicle one and what it is in each year.

Mr Marney: I may have to provide that as supplementary information if I cannot find it quickly for you—but you should find everything covered in that chapter.

The CHAIR: Perhaps we might take it as supplementary information.

Mr Marney: I am sorry —

The CHAIR: No; that is okay.

Hon KEN TRAVERS: I am a little confused because a number of line items by agency in terms of media and consultancy savings and the like are factored in, but the motor vehicle fleet does not seem to be factored in; however, as far as you are aware, it is actually committed —

Mr Marney: Yes, it is committed. Although procurement savings, the transfer payments grants saving and the asset target are all disclosed in that chapter on page 83 of budget paper No 3, it may be, because of its in-and-out nature, that the fleet is captured elsewhere.

Hon KEN TRAVERS: I ask because when we asked agencies last week about that particular line item, I think two of them indicated that the only way they were aware of that was through media comment. They had not received any formal notification of it.

Mr Marney: That is correct.

Hon KEN TRAVERS: How do they achieve the savings then if they are not formally notified that they need to achieve them?

Mr Marney: What do you mean by "formally notified"?

Hon KEN TRAVERS: If it is for next year's budget, when will they be notified?

Mr Marney: Very soon.

Hon KEN TRAVERS: What does the savings on grants line item entail? What are we talking about in terms of savings of 10 per cent across grants—what grant programs across agencies?

[4.20 pm]

Mr Marney: It is exactly that; it is an examination of the various grants of agencies and an evaluation of the outcomes achieved from those various grants programs and a target level of savings applied to them. Again, that is work that we need to undertake with the agencies over the next few months to ensure that the raft of very good and high value for money grants that are provided by the sector are not damaged and that we actually focus on areas of grants which have not been examined for some time and may no longer be relevant in the current settings.

Hon KEN TRAVERS: So how was the 10 per cent arrived at?

Mr Marney: It was based on advice on what might be achievable through various aspects of better fleet management, including reconsideration of the lease length, taking into consideration the current circumstances in the second-hand vehicle market.

Hon KEN TRAVERS: And the 10 per cent grant?

Mr Marney: The grant was purely a look across the growth in expenditure historically and what was thought might be feasible in terms of a target level of reduction based on that history of growth.

Hon KEN TRAVERS: If you could explain a bit more detail about how that is actually arrived at, as to how you would determine that it is going to be 10 per cent rather than an eight per cent or a 15 per cent figure that you are seeking to reduce, if you have not done the detailed work as to which grants you can get rid of?

Mr Marney: Those aggregates are based on an assessment of the overall trends in those variables over a period of time.

Hon KEN TRAVERS: So are you saying it has been growing by 10 per cent?

Mr Marney: It has been growing pretty strongly.

Hon KEN TRAVERS: What sort of a growth figure?

Mr Marney: I do not have those records to hand and I certainly was not expecting to go into that level of detail in terms of —

Hon KEN TRAVERS: Maybe you should take that on notice.

Mr Marney: — the formative process of those policy decisions, and it is probably a matter that is better directed to the government rather than the Under Treasurer.

Hon KEN TRAVERS: And that is the question. Is it a figure of government or is it a figure of Treasury?

Mr Marney: Ultimately, it is a figure of government because it is a government decision.

Hon KEN TRAVERS: What I am trying to work out —

Mr Marney: Ask government where did they get it. Treasury advice.

Hon KEN TRAVERS: Yes. How was that figure determined, which is not necessarily a figure of government; it is a figure of someone sitting down and doing the process. If you tell me it was done in the cabinet without any sort of calculations outside of cabinet, that is fine; it is a decision of government. But if there was some process to arrive at that 10 per cent figure, I would be interested in knowing. You indicated that it has got to do with the growth in the past, so if you are able to take on notice what the growth figures in the past have been, that would be useful.

Mr Marney: I am happy to provide detail of the growth in both the vehicle fleet expenses, the number of vehicles and share with you where they are, if you like.

Hon KEN TRAVERS: I would be interested in both the fleet and the grant programs if you are able to give us that information on supplementary. And the $60 million per annum for the procurement, on what basis is that arrived at?

Mr Marney: Again, that is based on an analysis of our understanding of the procurement patterns and the data that we have through who buys what. Essentially, the common-use arrangements that are in place at the moment have aggressively pursued standardisation, aggregation and simplification of agencies' procurement in areas that run across numerous agencies; computers, for example. The Auditor General has been through that procurement reform process and confirmed that the original savings targets were met and in fact exceeded by that process. Having said that, the common-use arrangement suite of reforms applies to around $800 million or $900 million worth of procurements spent across the sector when our total spend on goods and services is more like $4 billion. There is a substantial body of expenditure within agencies that has not had those same principles of reform applied to it. On the basis of what has been achieved in the broader reforms and the analysis undertaken of procurement patterns, that figure was arrived at.

Hon KEN TRAVERS: Good luck.

Mr Marney: I think it is doable. I think a lot of agencies have not managed their own spend in a way that yields savings for the government. I think what many have done has been to realise savings and then buy more stuff. In the current circumstance, we are able to tighten up on that a little bit, and it is probably going to save us a whole bunch of money.

The CHAIR: Members, we might finish at 4.30 pm.

Hon LJILJANNA RAVLICH: Under Treasurer, I want to quickly touch on the working relationship that Treasury officials have with the Economic Audit Committee and ask you to give your opinion on the nature of that relationship. I am particularly interested in process.

Mr Marney: Any particular area of concern?

Hon LJILJANNA RAVLICH: No; I am just very interested in the process of how it works. I know a couple of Treasury officials sit on the Economic Audit Committee. Do they go off and do their own thing and then you have a combined meeting? My concern comes from the fact that in the Legislative Council estimates only last week, we had two ministers advise those hearings that the target savings in their portfolios were in fact imposed upon them by the Economic Audit Committee; that being the Perth city council parking levy and the landfill levy. What is particularly concerning to me is the minister who is responsible for the Perth city car park levy in fact made the point that he did not even realise that the increase for parking a motorcycle had increased by some 400 per cent. That sort of thing is concerning. What concerns me is that if this committee is taking a heavy hand and giving directives, if you like, to Treasury officials or ministers, or indeed anybody else, I think that there may well be some cause for concern. Really, I am just asking for your feedback in respect of process and that working relationship.

Mr Marney: Yes. Thank you for giving me a better sense of what the concern is. The Economic Audit Committee has no authority across government. It is purely an advisory body. It comprises six members—Catherine Nance, John Langoulant, Peter Shergold, Peter Conran, Mal Wauchope and myself. For administrative purposes, I am the chair of the committee. The committee has terms of reference approved by cabinet, and the committee members work with a secretariat which reports to me on various areas of analysis and policy work to address those terms of reference. The committee's task is to provide a report to government, and it did that as part of the budget process. It provided its report to the economic and expenditure reform committee. It is then in government's hands. It is cabinet that takes decisions as to what is implemented and what is not implemented. There are no instructions given by the Economic Audit Committee; it simply does not have that authority. I do not have that authority. It provided options to government as government requested through its terms of reference, and government then dealt with it as it saw most appropriate in the circumstance. The Economic Audit Committee does not have free rein to impose its will upon the public sector. I can assure you that appropriate structures of authority are in place governing the work of the Economic Audit Committee.

Hon KEN TRAVERS: Leading on from that, in the budget some of those decisions must have been taken by cabinet to factor in revenue, but the revenue streams are controlled. The one that Ljil referred to was the Perth parking management authority and the waste management levies. Any expenditure under those levies is controlled, but there was no corresponding addition to the budget for those controlled expenditures on the expenditure side, but the revenue side was factored in. Is that not slightly misleading? Is that not slightly misleading for anyone who uses those figures in terms of the overall budget picture not to have included it in expenditure, particularly for Perth parking where you get $16 million a year but there is no increased expenditure even though it is a controlled expenditure? You cannot just use that expenditure willy-nilly; you actually have to spend it on something else.

Mr Marney: I can assure you that we do not use any expenditures willy-nilly.

Hon KEN TRAVERS: But no expenditure is factored into it.

Mr Marney: In terms of how those revenues offset other expenditures, I will leave it to the relevant ministers to discuss.

Hon KEN TRAVERS: That is the problem.

Mr Marney: I cannot help you there.

The CHAIR: That is their problem, not the Under Treasurer's problem.

Hon KEN TRAVERS: They say, "We were just told the fee was going up and we are still working out what we are going to spend it on."

The CHAIR: I think we have had a very useful afternoon. Thank you, Mr Marney, for attending.

Mr Marney: Thank you. Always a pleasure.

Hearing concluded at 4.30 pm