

WESTERN AUSTRALIAN FUTURE FUND BILL 2012

EXPLANATORY MEMORANDUM

OVERVIEW

The Bill consists of 12 clauses that provide for the establishment and ongoing operation of the Western Australian Future Fund (Future Fund).

The objective of the Future Fund is to set aside and accumulate a portion of the revenue from the State's finite mineral resources for the benefit of future generations of Western Australians.

The broad framework for the Future Fund, as provided for in the Bill, is as follows:

- the Future Fund will be established with 'seed capital' from the Royalties for Regions Fund totalling an estimated \$1.04 billion over the period 2012-13 to 2015-16;
- from 2016-17 onwards, the Future Fund will be credited each and every year with a minimum 1% of the State's annual royalty income;
- earnings on the Future Fund balance will be retained and reinvested in the Future Fund over the first 20 years of its operation (i.e. to 30 June 2032);
- during this 20 year accumulation period, draw downs from the Future Fund are prohibited;
- the balance of the Future Fund at 30 June 2032 (indicatively estimated at around \$4.7 billion) will be maintained into perpetuity; and
- the income earned on the balance of the Future Fund after 30 June 2032 (indicatively estimated at around \$230 million per year) may be applied for the purpose of providing public works and other public infrastructure in the metropolitan and regional areas of Western Australia.

The Future Fund will be a Treasurer's special purpose account for the purposes of the *Financial Management Act 2006* (FMA), and will be administered by the Treasurer. Money standing to the credit of the Future Fund will form part of the Public Bank Account, and can only be invested in accordance with the FMA and associated regulations governing investment of the Public Bank Account. This restricts investment of the Future Fund to cash and various debt instruments of high credit quality.

The Bill also includes an entrenching or 'manner and form' provision at clause 10 outlining the required manner and form of any amendments to, or repeal of, the Future Fund Act during the 20 year accumulation period. This is designed to preserve and protect the intended purpose of the Future Fund.

CLAUSE NOTES

Outlined below is a brief description of each clause of the Western Australian Future Fund Bill 2012.

Clause 1: Short Title

When enacted, the Act will be cited as the *Western Australian Future Fund Act 2012*.

Clause 2: Commencement

Provides for sections 1 and 2 of the Act to come into operation on the day on which the Act receives the Royal Assent. The rest of the Act comes into operation on the day after the Royal Assent.

Clause 3: Terms Used

Defines terms used in the Act.

Clause 4: Purpose of Act

Outlines the purpose of the Act, which is to provide for the accumulation of a portion of the revenue from the State's mineral resources and other money for the benefit of future generations through the establishment of the Western Australian Future Fund.

Clause 5: Western Australian Future Fund

Clause 5(1) establishes the Future Fund for the purpose stated in section 4.

Clauses 5(2) and 5(3) establish the Future Fund as a Treasurer's special purpose account under the *Financial Management Act 2006* (FMA), to be administered by the Treasurer.

Clause 5(4) requires that the balance of the Future Fund is to be held in the Public Bank Account, as defined in the FMA. Money standing to the credit of the Future Fund is not to be invested other than in accordance with the FMA and associated regulations (regulation 5 of the *Financial Management Regulations 2007*) governing the investment of money in the Public Bank Account. This means that money standing to the credit of the Future Fund can only be invested:

- with authorised deposit taking institutions with a credit rating not lower than 'BBB-' or 'Baa3';
- in debt securities that are guaranteed by the government of the Commonwealth or of a State or Territory; and

- in debt securities issued in Australia by a corporation, subsidiary or institution with a credit rating not lower than 'A' or 'A2'.

Clause 6 Credits to Future Fund from Royalties for Regions Fund

In conjunction with clause 6(4), clause 6(1) authorises the immediate transfer of an amount of **\$297.7 million** from the Royalties for Regions (RfR) Fund to the Future Fund. This is the first instalment of the RfR 'seed capital' to be transferred to the Future Fund (totalling an estimated \$1.04 billion over the period 2012-13 to 2015-16). The \$297.7 million amount in clause 6(1) comprises:

- a \$25 million per annum efficiency dividend applied to the RfR Fund from 2009-10 to 2012-13 (\$100 million over the four years), equivalent to the 3% efficiency dividend implemented in the 2009-10 Budget;
- an unspent balance of \$97.7 million from 2009-10 that has been maintained in the RfR Fund since that time (in 2009-10, actual royalty income was below the budget forecast for that year, and the Government decided not to spend the RfR portion of the difference); and
- an amount of \$100 million, being the 25% RfR component of the forecast revenue from the increase in the royalty rate on iron ore 'fines' in 2012-13 (in the 2011-12 Budget, the Government announced that it would remove, in stages, the concessional royalty rate then applying to iron ore 'fines' (5.625%), with a 6.5% royalty rate applying in 2012-13 and the full 7.5% 'lump' iron ore royalty rate applying from 2013-14).

Subclause (2)(a) defines the amount to be transferred from the RfR Fund to the Future Fund on 1 July 2013. Based on current (2012-13 Budget) forecasts, this amount is currently estimated to total **\$259.8 million**, which comprises:

- the 25% RfR component of the forecast revenue from the increase in the iron ore 'fines' royalty rate to 7.5% from 2013-14 (subclause (2)(a)(i)). This is currently estimated to be \$234.8 million, with the actual amount to be transferred on 1 July 2013 to be based on the forecast increase in royalty revenue due to the increased royalty rate on iron ore 'fines' as estimated by the Under Treasurer at the time of the 2013-14 Budget; and
- a continuation of the previously mentioned \$25 million efficiency dividend on the RfR Fund in 2013-14 (subclause (2)(a)(ii)).

Subclause (2)(b) defines the amounts to be transferred from the RfR Fund to the Future Fund on 1 July 2014 and 1 July 2015. Based on current (2012-13 Budget) forecasts, these amounts are currently estimated to be **\$241.6 million** and **\$243.8 million** respectively. The actual amounts to be transferred on 1 July 2014 and 1 July 2015 will be based on the forecast increase in royalty revenue due to the increased royalty rate on iron ore 'fines' as estimated by the Under Treasurer at the time of the 2014-15 Budget and 2015-16 Budget respectively.

Clause 6(3) defines terms used.

Clauses 6(4) and 6(5) require that the above amounts transferred from the RfR Fund to the Future Fund are to be charged to the RfR Fund, credited to the Future Fund, and taken to be expenditure authorised under section 9 of the *Royalties for Regions Act 2009*.

Clause 7 Credits to Future Fund from Forecast Royalty Income

Clause 7(a) requires that in 2016-17 and each subsequent financial year, the Future Fund is to be credited with an amount equal to 1% of the forecast royalty income for that year.

Clause 7(b) provides a standing appropriation which authorises the transfer of the amounts described in clause 7(a) from the Consolidated Account to the Future Fund.

Clause 8 Additional Money Credited to Future Fund

Clause 8(1) provides that the Treasurer may credit to the Future Fund any amount in addition to the amounts provided for under sections 6 or 7. Depending on future economic and financial circumstances, this provides scope for a future government to, for example, allocate more (but not less) than 1% of the State's royalty income to the Future Fund. Any such amounts will require Parliamentary approval of the relevant appropriation item.

Subclause (2)(a) requires that income derived from the investment of money standing to the credit of the Future Fund, is to be credited to the Future Fund.

Subclause (2)(b) provides that the Treasurer may credit to the Future Fund any other money lawfully made available to the Future Fund. This covers potential contributions that may be made direct to the Future Fund (i.e. funds not charged to the Consolidated Account), including, for example, a contribution from a private entity.

Clause 9 Application of Future Fund

Clause 9(1) defines terms used.

Clause 9(2) requires that money credited to the Future Fund under sections 6(4) (i.e. the RfR 'seed capital'), 7 (i.e. the 1% of annual royalty income from 2016-17 onwards), 8(1) (i.e. any additional amounts credited to the Future Fund) and 8(2)(b) (i.e. any other money lawfully made available to the Future Fund), along with income derived on the balance of the Future Fund before 1 July 2032, must be held in perpetuity in the Future Fund and cannot be applied for any purpose. This means that the balance of the Future Fund at 30 June 2032 (indicatively estimated at around \$4.7 billion) will be preserved into perpetuity, and that only the income earned on the balance of the Future Fund after this date can be spent (see clause 9(3)).

Clause 9(3) provides that income earned on the Future Fund balance after 30 June 2032 (indicatively estimated at around \$230 million per annum) may be applied for the purpose of providing public works and other public infrastructure in the metropolitan and regional areas of Western Australia. This is the only purpose to which Future Fund earnings may be applied.

Clause 9(4) requires that the Treasurer and the Minister for Regional Development reach agreement on an appropriate division of the Future Fund's income between the metropolitan area and the regions, and the purposes for which the income is to be applied in the regions. The form of this agreement is not legislated.

Clause 9(5) allows the Minister for Regional Development to consult with the Western Australian Regional Development Trust in considering the application of the Future Fund in the regions.

Clause 9(6) provides that the Treasurer cannot give a direction in relation to the Future Fund under section 20 of the FMA. This means that the Treasurer cannot use section 20 of the FMA to transfer any of the cash balance in the Future Fund to the Consolidated Account, thereby ensuring the purpose of the Future Fund is preserved and protected over time.

Clause 9(7) provides that section 12 of the FMA does not apply to the Future Fund. Section 12 of the FMA allows the Treasurer to apply any money standing to the credit of the Public Bank Account to make any lawful payment. To ensure the purpose of the Future Fund is preserved and protected over time, clause 9(7) prohibits the application of section 12 of the FMA to the Future Fund.

Clause 10 Manner and Form of Amendment or Repeal during Accumulation Period

Clause 10(1) defines the term 'accumulation period', which is the period to 30 June 2032 during which the Future Fund's balance is accumulating and draw downs from the Future Fund are prohibited.

Clause 10(2) is an entrenching or 'manner and form' provision which requires an absolute majority of both Houses of Parliament to repeal or amend the Act during the accumulation period. An absolute majority constitutes one more than half the votes of the total number of members of each House, whether they are present or not.

Clause 10(3) provides that a future Bill that is in contravention of subsection (2) is of no effect as an Act.

This provision is designed to ensure that the Future Fund balance accumulates for the benefit of future generations (as intended), and is not able to be used for other purposes or otherwise be tampered with by future governments – unless the 'manner and form' requirements of subsection (2) are satisfied.

Clause 11 Annual Reporting

Clause 11(1) defines 'Department' as the department of the Public Service principally assisting in the administration of the Act. This is intended to be the Department of Treasury (Treasury).

Clause 11(2) requires that the Department (Treasury) must include information about the operation of the Future Fund during a financial year in its annual report for that year.

Clause 11(3) requires that the Department's annual report is also to include details of the expenditure, if any, from the Future Fund in the metropolitan area and regions of Western Australia for that year. It is noted that this requirement will not take effect before the 2032-33 financial year.

Clause 12 Regulations

Clause 12 provides for regulations to be made for giving effect to the purposes of the Act.