[P.P.4B

Government
of South Australia

Report

of the

Auditor-General

Supplementary Report

for the

year ended 30 June 2017

Tabled in the House of Assembly and ordered to be published, 29 May 2018

First Session, Fifty-Fourth Parliament

Consolidated Financial Report review: May 2018

By authority: W Hunter, Government Printer, South Australia

2018

General enquiries to:

Auditor-General
Auditor-General's Department
Level 9
State Administration Centre
200 Victoria Square
Adelaide SA 5000

www.audit.sa.gov.au

ISSN 0815-9157

Government of South Australia
Auditor-General's Department

Level 9
State Administration Centre
200 Victoria Square
Adelaide SA 5000
DX 56208
Victoria Square
Tel +618 8226 9640
Fax +618 8226 9688
ABN 53 327 061 410
audgensa@audit.sa.gov.au
www.audit.sa.gov.au

28 May 2018

The Hon Andrew McLachlan CSC
President
Legislative Council
Parliament House
ADELAIDE SA 5000

The Hon Vincent Tarzia MP
Speaker
House of Assembly
Parliament House
ADELAIDE SA 5000

Dear President and Speaker

Report of the Auditor-General: Supplementary Report for the year ended 30 June 2017 'Consolidated Financial Report review: May 2018'

As required by the *Public Finance and Audit Act 1987*, I present to each of you my Supplementary Report for the year ended 30 June 2017 'Consolidated Financial Report review: May 2018'.

Content of the Report

Part A of the Auditor-General's Annual Report for the year ended 30 June 2017 referred to audit work that would be subject to supplementary reporting to Parliament.

This Supplementary Report provides detailed commentary and audit observations on the 2016-17 Consolidated Financial Report.

Acknowledgements

The audit team for this report was Salv Bianco, Kenneth Anderson and Grace Lum.

We appreciate the cooperation and assistance given by staff of the Department of Treasury and Finance during the review.

Yours sincerely

Andrew Richardson
Auditor-General

Contents

1 Executive summary

1.1 Introduction

This Report provides our observations on the 2016-17 Consolidated Financial Report (CFR), in particular:

- the purpose of the CFR
- highlights of the CFR
- an overview of the CFR reporting frameworks
- the findings of our review of the CFR
- an analysis of the State's actual financial performance
- an analysis of the State's actual financial position.

The CFR fulfils the SA Government's consolidated financial reporting obligations under AASB 1049. It reports the SA Government's actual financial performance and position for the year. The 2016-17 CFR was published on DTF's website in January 2018.

The CFR incorporates both the whole of government financial report and the financial report of the general government sector.

The whole of government financial report gives a consolidated picture of the financial relationship between the SA Government as a whole and the 'rest of the world'. The whole of government reporting entity comprises the general government, PNFC and PFC sectors. Section 2 provides further details on the nature and activities of these sectors.

In preparing the whole of government financial report, transactions between the general government sector, PNFCs and PFCs are eliminated.

The State Budget focuses on the activity of the general government sector rather than the whole of government, but includes general government sector interactions with the PNFC and PFC sectors such as dividend receipts and community service obligation payments.

Commentary on the State Budget is provided in the Auditor-General's Supplementary Report for the year ended 30 June 2017 'State Finances and related matters: November 2017'.

1.2 Conclusion

1.2.1 The 2016-17 Consolidated Financial Report reported a net operating deficit and net lending deficit for the whole of government and reflects increased reliance on Commonwealth grant revenue

The 2016-17 CFR has some key highlights:

- The whole of government reported a $246 million net operating deficit for 2016-17, compared to a $436 million net operating surplus for the general government sector.

- The whole of government reported a net lending deficit of $3.588 billion in 2016-17.
- The State is increasingly reliant on grant revenue, with over half its revenue in 2016-17 coming from grants.

Section 1.3 provides further details on these highlights.

1.2.2 Our review of the Consolidated Financial Report did not identify any material misstatements or control deficiencies

There is no requirement under the *Public Finance and Audit Act 1987* or any other legislation to provide an audit opinion on the CFR, so I have not issued one.

I do, however, consider it valuable and consistent with wider public expectation that we review the credibility and validity of the financial information in the CFR. As a result, our 2016-17 review covered:

- the principles adopted in defining the economic entity
- DTF's controls and procedures for evaluating the reliability and validity of financial data provided by agencies
- processes for preparing the CFR
- compliance with legislation and accounting frameworks.

Our review also included sample testing to ensure that financial data provided by agencies for inclusion in the CFR was consistent with their audited financial statements, and evaluating the accounting policies and significant accounting estimates unique to the CFR.

We did not identify any material misstatements or control deficiencies. We did, however, identify opportunities to improve the way financial information is collected, validated and consolidated in preparing the CFR. They are outlined in section 1.4.

1.3 What we found

1.3.1 The whole of government reported a $246 million net operating deficit for 2016-17, compared to a $436 million net operating surplus for the general government sector

There was a $682 million difference between the reported operating results for the whole of government and general government sector.

This is mainly due to agency operating losses in the PNFC sector and the elimination of transactions between the general government sector and the PNFC and PFC sectors in the whole of government financial report (including land tax, Emergency Services levy and guarantee fees received by the general government sector from PNFCs). Section 4.2.2 provides further detail on these operating losses and eliminated transactions.

1.3.2 The whole of government reported a net lending deficit of $3.588 billion in 2016-17

The net lending deficit of $3.588 billion for the whole of government in 2016-17 is mainly due to the recognition of a $2.809 billion finance lease liability for the new RAH. It was recognised by the Central Adelaide Local Health Network Incorporated following commercial acceptance on 13 June 2017.

1.3.3 The State's net worth has increased by $4.677 billion

The total change in net worth for the whole of government in the Statement of Comprehensive Income is an increase of $4.677 billion. This is mainly due to the following other economic flows:

- an actuarial gain on defined benefit superannuation plans ($2.468 billion) arising from a change in assumptions used by the actuary to value plan liabilities
- an increase in asset revaluation reserves ($1.393 billion) mainly owing to a revaluation increment of $627 million on DECD buildings and improvements and a $335 million increase in the valuation of land under roads
- other net actuarial gains ($536 million) primarily driven by a MAC insurance claims provision adjustment ($515 million).

1.3.4 The State is increasingly reliant on Commonwealth grant revenue

Grant revenue is the largest revenue stream for the State. As a percentage of total revenue it has increased from 43% in 2012-13 to 51% in 2016-17. This is mainly due to growth in GST grants from the Commonwealth Government. Section 4.2.4 provides further detail on trends in grant revenue.

1.3.5 The actual net operating result for the general government sector in 2016-17 under AASB 1055 was $167 million better than budgeted

Figure 1.1 shows that the actual net operating balance and net lending/borrowing positions reflected in the 2016-17 Final Budget Outcome and the CFR for the general government sector were better than corresponding budget figures.

Figure 1.1: Budget and actual net operating balance and net lending/borrowing position for 2016-17 under UPF and AASs

	Net operating balance	Net lending/ borrowing
2016-17 Budget under UPF	$254 million surplus	$2.436 billion deficit
2016-17 Final Budget Outcome under UPF	$443 million surplus	$2.371 billion deficit
2016-17 Budget under AASB 1055	$269 million surplus	$2.422 billion deficit
Actual result in the 2016-17 CFR[1]	$436 million surplus	$2.378 billion deficit

The actual net operating surplus in the 2016-17 CFR is $436 million, compared to a budgeted surplus of $269 million in the 2016-17 Budget prepared in line with AASB 1055 requirements.

The difference between the actual and budgeted result was mainly due to:

- a higher than budgeted dividend from MAC
- an unbudgeted income tax equivalent payment from ReturnToWorkSA
- lower interest expenses resulting from changes in the timing of commercial acceptance of the new RAH.

These impacts were partly offset by downward revisions to GST grant revenue and National Partnership grants compared to the original budget.

The 2016-17 Budget Papers and Final Budget Outcome are presented on the UPF basis, while the budget figures in note 51 of the 2016-17 CFR are presented on the AASB 1055 reporting basis. Section 4.3.3 provides further detail on the differences.

1.3.6 The State's total assets and liabilities both increased significantly in 2016-17

Total assets increased by $9.704 billion (9%) to $113.997 billion, while total liabilities increased by $5.027 billion (8%) to $71.57 billion.

This is mainly due to an increase in SAFA's borrowings and investments and the recognition of new RAH buildings, machinery and equipment assets and corresponding finance lease liabilities in 2016-17.

Sections 5.1.2 and 5.1.3 provide further detail on the main variations in assets and liabilities from the prior year.

1 Note 3 of the CFR discloses the differences in actual results reported under the UPF and AAS reporting frameworks. The differences for both the net operating balance and net lending/borrowing position were immaterial in 2016-17 ($7 million).

1.3.7 Matters reflected in Independent Auditor's Reports for government agencies in 2016-17

As noted in section 1.2.2, an audit opinion is not provided on the CFR. However, a letter summarising the results of our review was provided to DTF in January 2018. It included any agency specific audit matters identified that would impact on the audit opinion for the CFR, if one was provided.

I noted in the letter that, while I had not modified my Independent Auditor's Reports for ReturnToWorkSA and the Lifetime Support Authority for 2016-17, I drew attention to the inherent uncertainty associated with certain liabilities of these entities.

1.4 What we recommended

We issued a management letter to DTF's Chief Executive in February 2018 outlining opportunities to improve the way financial information is collected, validated and consolidated in preparing the CFR. Our recommendations included:

- performing and documenting analysis to support whether certain agencies should be treated as controlled for CFR reporting purposes in line with AASB 10
- reconciling original budget figures in note 51 on budgetary information to the budget papers
- analysing material prior year variances and differences between the whole of government and general government sector reported results as part of the quality assurance process over the preparation of the CFR.

1.5 Response to our recommendations

DTF's response to our management letter indicated that appropriate action would be taken to address the matters raised, including:

- performing further work to establish whether the identified agencies are controlled entities of government and formally documenting the process performed to review and identify potential controlled entities
- reconciling each original budget line item in note 51 on budgetary information to the budget papers when preparing the 2017-18 CFR
- analysing material prior year variances and differences between the whole of government and general government sector reported results when preparing the 2017-18 CFR.

2 Background

AASB 1049 requires governments to prepare whole of government and general government sector financial reports.

The South Australian CFR for the year ended 30 June 2017 was prepared by DTF under AASB 1049 and comprises both whole of government and general government sector financial reports.

The whole of government reporting entity includes the general government sector, PNFCs and PFCs. The general government sector financial report reflects that sector's transactions with PNFCs, PFCs and non-SA Government sector entities.

The three government sectors are defined as follows:

- General government – all budget dependent departments and agencies providing services free of charge or at prices below their cost of production or service cost. These are the services that tend to be primarily financed through taxes and other charges, and for this reason this sector tends to be the focus of fiscal targets.
- PNFCs – trading enterprises mainly engaged in producing goods and services for sale in the marketplace at prices that aim to recover most or all of the costs involved. In South Australia this sector includes SAHT and SA Water.
- PFCs – bodies primarily engaged in providing financial services. This includes financial institutions such as SAFA, HomeStart Finance and Funds SA.

A listing of the entities controlled by the SA Government and their corresponding sector classification is provided in note 49 of the CFR.

In arriving at a consolidated result in the whole of government financial report, transactions between all government controlled entities are eliminated to present a consolidated picture of the financial relationship between the SA Government as a whole and the 'rest of the world'.

AASB 1049 requires financial reports to be prepared consistent with the principles and rules established by the ABS.[2] However, it is important to note that some technical differences remain between AASB 1049 and the UPF based on ABS Government Finance Statistics principles. The impact of these differences for the SA Government is immaterial, with a table reconciling the key aggregates provided in note 3 of the CFR.

[2] 'Australian System of Government Finance Statistics: Concepts, Sources and Methods', Australia, 2005, Australian Bureau of Statistics (Publication 5514.0).

3 Audit mandate, objective and scope

3.1 Our mandate

The Auditor-General has authority to review controls over the preparation of the CFR under section 36(1)(a)(iii) of the *Public Finance and Audit Act 1987*.

3.2 Our objective

The objective of this Report is to provide independent commentary and analysis on the actual financial performance and position of the whole of government.

The CFR is the only report that presents the consolidated activity of all government sectors. The CFR presents a picture of the financial relationship between the SA Government as a whole and the 'rest of the world'.

The Auditor-General's Supplementary Report for the year ended 30 June 2017 'State Finances and related matters: November 2017' focuses mainly on the estimated results and budget of the general government sector.

The Final Budget Outcome report only reflects actual outcomes against budget for the general government and PNFC sectors and, as it is prepared by DTF, does not reflect independent analysis.

3.3 What we reviewed and how

Our review in 2016-17 covered:

- the principles adopted in defining the economic entity
- DTF's controls and procedures for evaluating the reliability and validity of financial data provided by agencies
- processes for preparing the CFR
- compliance with legislation and accounting frameworks.

Our review also included sample testing to ensure that financial data provided by agencies for inclusion in the CFR was consistent with their audited financial statements, and evaluating the accounting policies and significant accounting estimates unique to the CFR.

3.4 What we did not review

Consistent with previous years, there is no requirement under the *Public Finance and Audit Act 1987* or any other legislation to provide an audit opinion on the CFR, so I have not issued one.

4 2016-17 Consolidated Financial Report financial performance

Key points

- The whole of government reported a $246 million net operating deficit for 2016-17, compared to a $120 million net operating deficit in the prior year.
- There is a $682 million difference between the whole of government and general government sector 2016-17 net operating balances, due mainly to agency operating losses in the PNFC sector and the elimination of transactions between the general government sector and the PNFC and PFC sectors in the whole of government financial report.
- Grants are a key revenue stream, representing 51% of total whole of government revenue in 2016-17.
- Employee expenses are the largest component of expenditure in 2016-17 at 39% and have remained steady as a percentage of total whole of government expenditure over the past two years.
- The State’s net worth has increased by $4.677 billion, primarily owing to the net actuarial gain on defined benefit superannuation plans and increases in asset revaluation reserves.
- The whole of government reported a net lending deficit of $3.588 billion in 2016-17, compared to a net lending deficit of $313 million in the prior year.
- The actual net operating result for the general government sector in 2016-17 under the AASB 1055 reporting basis was $167 million better than budgeted, mainly due to a higher than budgeted dividend from MAC, an unbudgeted income tax equivalent payment from RTWSA and lower interest expenses.

4.1 Analysis of variations with prior year

Figure 4.1 summarises the whole of government Statement of Comprehensive Income for the year ended 30 June 2017 and comparative prior year figures.

Figure 4.1: Statement of Comprehensive Income (whole of government)

	2016 $’million	2017 $’million
Revenue from transactions:		
Taxation revenues	4 088	4 037
Grant revenue	9 518	10 459
Charges for goods and services	4 954	4 507
Other	1 380	1 616
Total revenue from transactions	19 940	20 619

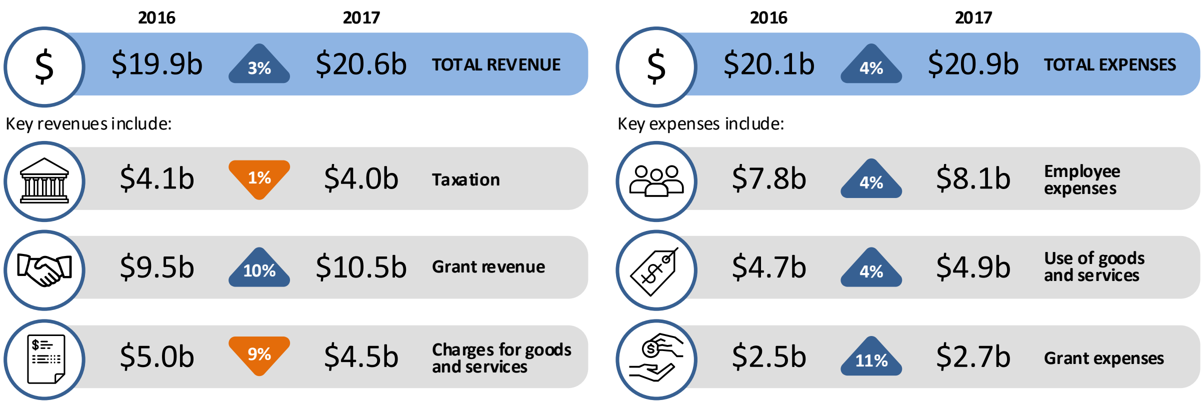
	2016 $'million	2017 $'million
Expenses from transactions:		
Employee expenses	7 797	8 098
Depreciation and amortisation	1 368	1 413
Use of goods and services	4 732	4 904
Grant expenses	2 454	2 736
Other	3 709	3 714
Total expenses from transactions	20 060	20 865
Net result from transactions – Net operating balance	(120)	(246)
Other economic flows – included in net result:		
Net actuarial gain (loss) on superannuation defined benefit plans	(2 683)	2 468
Other	(717)	884
Total economic flows included in net result	(3 400)	3 352
Net result	(3 521)	3 105
Other economic flows – other non-owner movements in equity:		
Changes in property, plant and equipment asset revaluation reserve	771	1 393
Other	633	(81)
Total other economic flows – non-owner movements in equity	1 404	1 312
Comprehensive result – change in net worth	(2 116)	4 418
Transaction with owners	-	259
Total change in net worth	(2 116)	4 677
Key fiscal aggregates:		
Net operating balance	(120)	(246)
Less: Net acquisition of non-financial assets	193	3 342
Net lending/borrowing	(313)	(3 588)

Note: Totals may not add due to rounding.

4.1.1 Modest increases in total revenue and expenditure

Figure 4.2 shows changes in revenue and expenditure between 2015-16 and 2016-17 for key items.

Figure 4.2: Analysis of variations in revenue and expenditure



Total revenue and expenditure increased modestly in 2016-17. Total revenue increased by $679 million (3%), while total expenditure increased by $805 million (4%).

4.1.2 Increase in total revenue mainly due to higher grant revenue, offset partly by lower charges for goods and services

The main variations in total revenue from the prior year were:

- grant revenue – increased by 10% or $941 million. This is mainly due to higher GST grant revenue from the Commonwealth Government, increased capital grants under the Intergovernmental Agreement on Federal Financial Relations and increased Commonwealth financial assistance grants received by the South Australian Local Government Grants Commission
- charges for goods and services – decreased by 9% or $447 million. This is mainly due to decreases in CTP premiums ($397 million) and SA Water rates and charges ($143 million). The State no longer receives CTP premiums following the transition to private insurer arrangements from 1 July 2016. The decrease in SA Water rates and charges is due to decreased water usage and a reduction in average prices owing to a regulatory pricing decision.

Part B of the Auditor-General's Annual Report for the year ended 30 June 2017 'Agency audit reports' provides further details on variations between years for individual agencies.

4.1.3 Increase in total expenses mainly due to higher employee and grant expenses

The main variations in total expenditure from the prior year were:

- employee expenses – increased by 4% or $301 million. This growth was due mainly to increases in salary and wages expenses of $290 million, primarily due to enterprise agreement increases and additional resources to implement child protection reform initiatives
- grant expenses – increased by 11% or $282 million. This is primarily due to an increase in financial assistance grants from the Commonwealth Government, on-passed to the South Australian Local Government Grants Commission, and increases in Department for Communities and Social Inclusion disability grants.

In 2016-17 enterprise agreement negotiations were finalised for nurses, Rail Commissioner's train operation drivers and maintenance employees, assistants to Members of Parliament, wages parity (weekly paid trade), and TAFE SA and SA Ambulance employees, and generally resulted in a 2.5% salary increase. DTF advised that these agreements, which were executed in 2016-17, were already well progressed at the time of the 2016-17 Budget and were not subject to the 1.5% wages policy introduced in the 2016-17 Budget.

Part B of the Auditor-General's Annual Report for the year ended 30 June 2017 'Agency audit reports' provides further details on variations between years for individual agencies.

4.1.4 Variations in other economic flows primarily attributable to actuarial gains and losses on superannuation defined benefit plans and changes in property, plant and equipment asset revaluation reserves

The main variations in other economic flows from the prior year were:

- net actuarial gain or loss on superannuation defined benefit plans – $2.468 billion gain in 2016-17 compared to $2.683 billion loss in the prior year. This is mainly due to an increase in the discount rate used to value the unfunded superannuation liability from 2.5% at 30 June 2016 to 3.1% at 30 June 2017, which decreased the unfunded superannuation liability
- other net actuarial gains (losses) – increased by $828 million to a gain of $536 million. This is primarily due to changes in actuarial assumptions for the MAC outstanding claims liability and the impacts of the increase in the discount rate adopted for valuing long service leave liabilities
- changes in asset revaluation reserve – increased by $622 million to $1.393 billion. This balance varies from year to year based on the revaluation cycles of individual agencies. The increments in 2016-17 primarily relate to DECD building and improvements and land under roads.

4.1.5 Transactions with owners attributable to receipts from private insurers under new Compulsory Third Party insurance arrangements

The capital returned under transactions with owners ($259 million) reflects the one-off receipt of fees from four private insurers for initial market shares under CTP insurance market reforms.

4.2 Trends in financial performance

4.2.1 The net operating deficit increased in 2016-17

The net operating balance in the Statement of Comprehensive Income is calculated as revenue from transactions less expenses from transactions. It is a summary measure of the ongoing sustainability of operations and excludes gains and losses resulting from changes in price levels and other changes in the volume of assets. It is the component of the change in net worth that is due to transactions and can be attributed directly to government policies.

Figure 4.3 shows the whole of government and general government net operating balances for the past five years.

Figure 4.3: Net operating balances

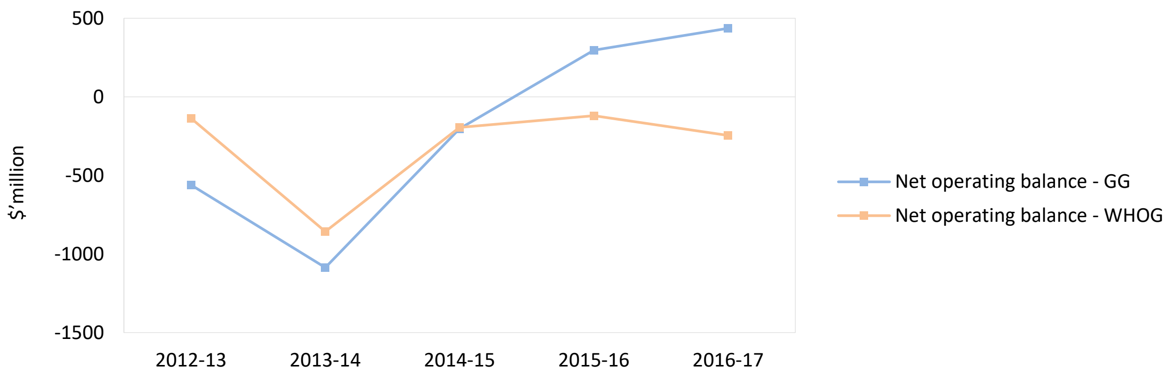


Figure 4.3 shows that following a trend towards surplus between 2013-14 and 2015-16, the whole of government net operating balance deficit increased in 2016-17.

The increase in the whole of government net operating deficit in 2016-17 contrasts with an increase in the general government sector net operating surplus over the same period.

4.2.2 The difference between the whole of government and general government sector net operating balances is $682 million

The net operating balance for the whole of government in 2016-17 was a deficit of $246 million. This compares to a $436 million net operating surplus for the general government sector, a $682 million difference.

The whole of government reported result reflects the elimination of all transactions between all government entities, thus only reporting transactions with the 'rest of the world'. The general government sector reported result only reflects the elimination of transactions that occur within the general government sector.

The resulting differences between the whole of government and general government sector are:

- the transactions the general government sector has with the PNFC and PFC sectors
- any transactions the PNFC and PFC sectors have with non-SA government entities.

The significant transactions the general government sector had with the PNFC and PFC sectors in 2016-17 are outlined in note 52 on related party transactions. The following revenue was received by the general government sector from the PNFC and PFC sectors:

- land tax received from SAHT ($180 million)
- income tax equivalents from PNFCs and PFCs ($181 million)
- guarantee fees from PNFCs and PFCs ($132 million)
- dividend revenue from MAC ($298 million)
- dividend revenue from SA Water ($193 million).

The impact of these revenue transactions on the general government sector net operating balance was partly offset by the following significant expense transactions paid by the general government sector to the PNFC and PFC sectors:

- interest loans expense paid to PFCs ($226 million)
- community service obligation payments made to SA Water ($136 million)
- fleet expenses paid to SAFA ($51 million)
- grants from the Department for Communities and Social Inclusion to SAHT ($162 million).

Dividends and income tax equivalents received by the general government sector are driven by the operating profits of the agencies in the PNFC and PFC sectors. As a result, a portion of the activity of PNFCs and PFCs is in effect reflected in the general government sector financial report as dividends and income tax equivalents revenue.

Operating losses in the PNFC and PFC sectors also drive differences between the whole of government and general government sector net operating balances. SAHT and the Urban Renewal Authority made operating losses in 2016-17.

4.2.3 The net lending/borrowing position has been highly variable over the past five years

The net lending/borrowing position is the net operating balance minus the net acquisition/ disposal of non-financial assets. A net lending balance (fiscal surplus) indicates that the public sector is contributing more than enough to finance its investment spending. A net borrowing (fiscal deficit) position indicates that the public sector's level of investment exceeds its level of savings.

Figure 4.4 shows the whole of government and general government net lending/borrowing position for the past five years.

Figure 4.4: Net lending/borrowing position

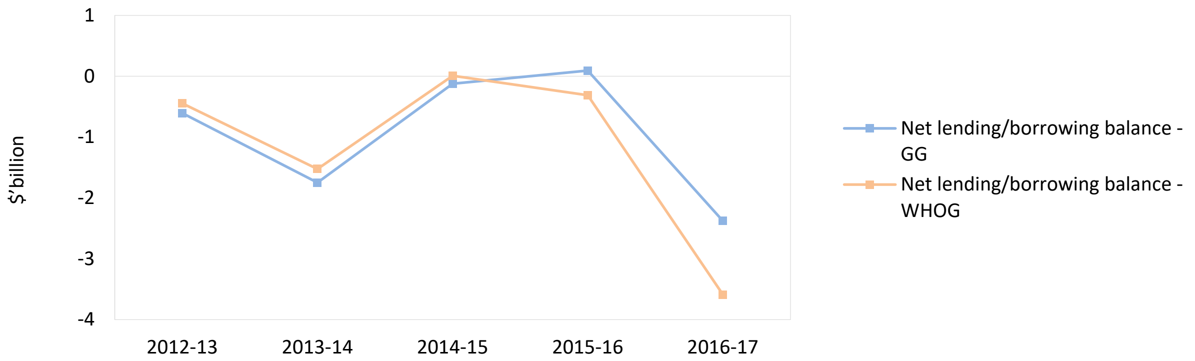


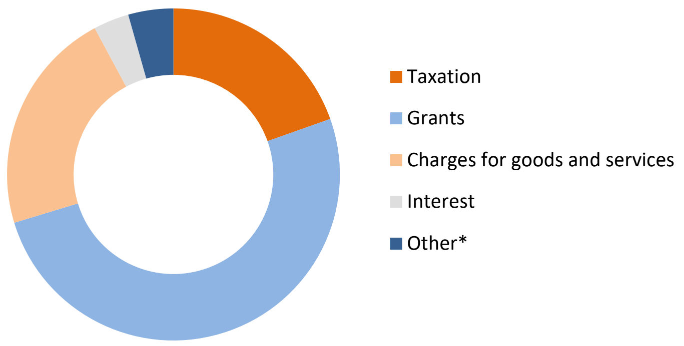
Figure 4.4 shows the high variability in the net lending/borrowing position over the past five years, with a significant net lending/borrowing deficit in 2016-17.

The net lending deficit of $3.588 billion for the whole of government in 2016-17 is mainly due to the recognition of the $2.809 billion finance lease liability for the new RAH. It was recognised by the Central Adelaide Local Health Network Incorporated following commercial acceptance on 13 June 2017.

4.2.4 The State is increasingly reliant on Commonwealth grant revenue

Figure 4.5 shows the composition of whole of government revenue in the 2016-17 CFR.

Figure 4.5: Composition of revenue

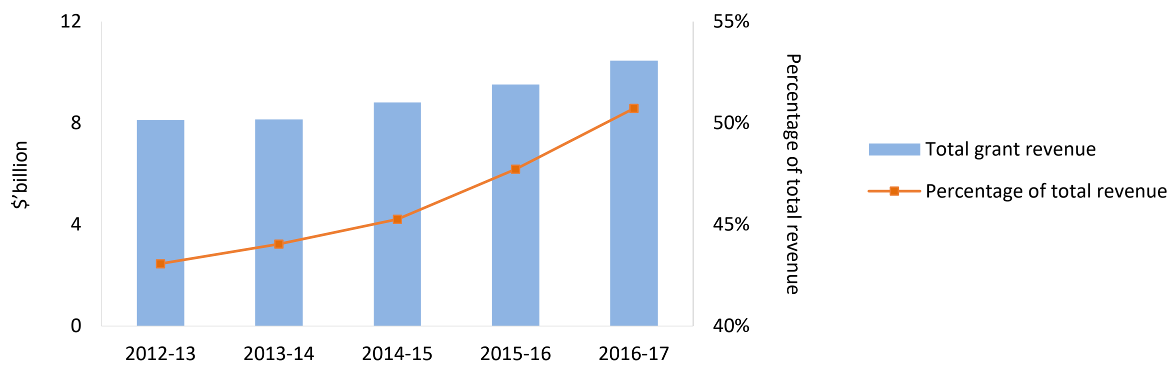


* Includes dividends and income tax equivalents and other revenues.

Figure 4.5 highlights that grant revenue, which is virtually all Commonwealth sourced, is the largest revenue stream for the State, representing more than half of total revenue from transactions in 2016-17.

Figure 4.6 shows the State's increasing reliance on grant revenue over the past five years.

Figure 4.6: Grant revenue as percentage of total revenue



Grant revenue, as a percentage of total revenue, has increased from 43% in 2012-13 to 51% in 2016-17.

This growth in grant revenue largely reflects growth in GST grants from the Commonwealth Government, with South Australia's share of the national GST pool increasing in 2016-17. The growth also reflects increased capital funding from the Commonwealth in 2016-17.

The other major revenue streams for the State are goods and services charges (22%) and taxation (20%).

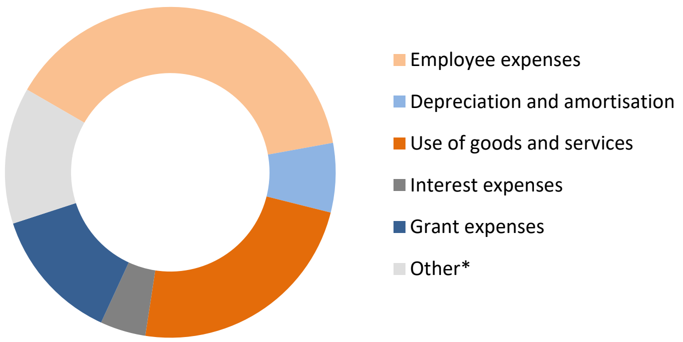
4.2.5 Taxation revenue decreased slightly in 2016-17 from the prior year

Taxation revenue was $4.037 billion in 2016-17, compared to $4.088 billion in the prior year. The 1% decrease is mainly due to a reduction in stamp duties and gambling taxes, driven by the phased abolition of a number property transfer stamp duties and a reduction in taxable gambling sales revenue compared to the prior year.

4.2.6 Employee expenses are steady as a percentage of total expenditure

Figure 4.7 shows the composition of whole of government expenses in the 2016-17 CFR.

Figure 4.7: Composition of expenditure



* Includes other superannuation expenses, superannuation interest cost and other expenses.

Figure 4.7 highlights that employee expenses are the largest component of expenditure for the State, representing 39% of total expenses from transactions in 2016-17. The other major components of expenditure are use of goods and services expenses (24%) and grant expenses (13%).

Figure 4.8 shows whole of government employee expenses over the past five years and those expenses as a percentage of total expenses.

Figure 4.8: Employee expenses as a percentage of total expenses

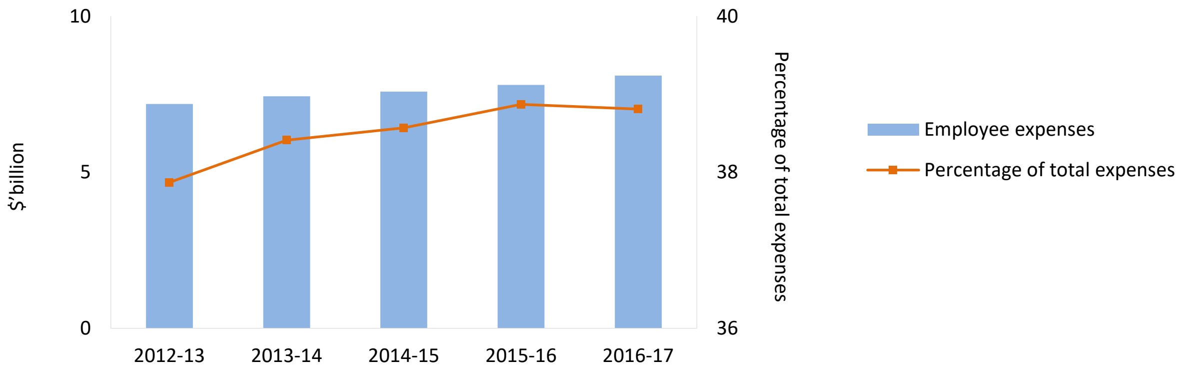


Figure 4.8 highlights that employee expenses as a percentage of total expenses trended marginally upwards between 2012-13 and 2015-16 and remained steady over the last two years.

Figure 4.9 shows the year on year percentage change in total whole of government employee expenses over the past five years.

Figure 4.9: Year on year percentage change in employee expenses

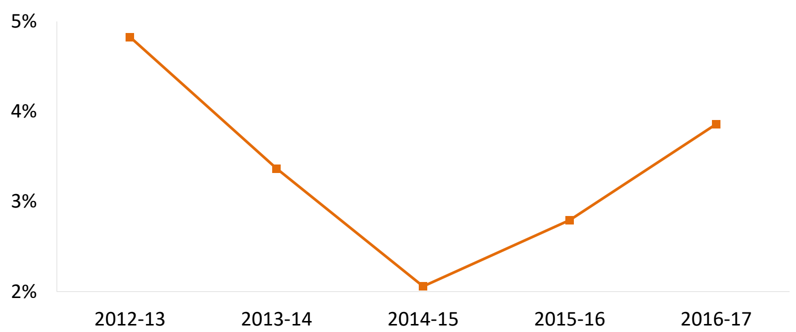


Figure 4.9 highlights that percentage year on year growth in employee expenses trended downwards from 2012-13 to 2014-15, but has trended up since then, mainly owing to enterprise agreement increases in 2015-16 and 2016-17 and additional resources to implement child protection reform initiatives in 2016-17.

Figure 4.10 shows the FTE employee numbers for the whole of government over the past five years.

Figure 4.10: Whole of government FTEs

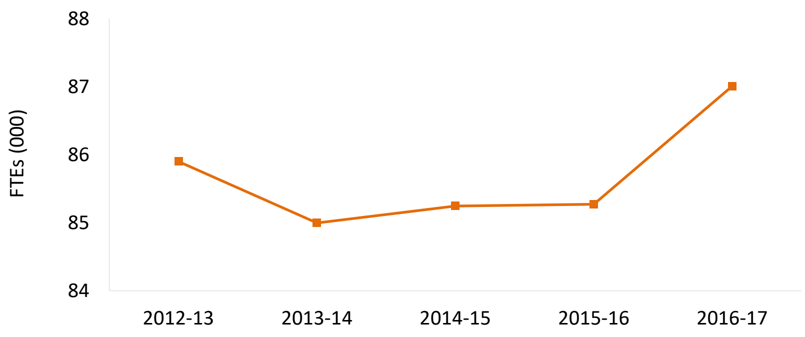


Figure 4.10 highlights that there has been a slight trend upwards in total FTE numbers since 2013-14 with a larger 2% increase between 2015-16 (85 272 FTEs) and 2016-17 (87 011 FTEs). The increase in FTEs in 2016-17 is primarily attributable to additional positions in the Department for Child Protection, DECD, health units and South Australia Police.

4.3 Further commentary and analysis

4.3.1 The State's net worth has increased by $4.677 billion

The total change in net worth for the whole of government in the Statement of Comprehensive Income is an increase of $4.677 billion. This is mainly due to the following other economic flows:

- an actuarial gain on defined benefit superannuation plans ($2.468 billion) arising from a change in assumptions used by the actuary to value the plan liabilities
- an increase in asset revaluation reserves ($1.393 billion) mainly owing to a revaluation increment of $627 million on DECD buildings and improvements and a $335 million increase in the valuation of land under roads
- other net actuarial gains ($536 million) primarily driven by a MAC insurance claims provision adjustment ($515 million).

Section 5.1.3 provides further detail on the assumptions and financial reporting requirements impacting the estimate of unfunded liabilities for defined benefit superannuation plans.

4.3.2 The whole of government reported a net lending deficit of $3.588 billion in 2016-17

The net lending/borrowing balance for the whole of government in 2016-17 is a net lending deficit of $3.588 billion, compared to a net lending deficit of $313 million in the prior year.

The net lending deficit in 2016-17 is mainly due to the recognition of a $2.809 billion finance lease liability for the new RAH. It was recognised by the Central Adelaide Local Health Network Incorporated, following commercial acceptance on 13 June 2017.

The section of Part B of the Auditor-General's Annual Report for the year ended 30 June 2017 titled 'Central Adelaide Local Health Network' provides more detail on the new RAH finance lease arrangements.

4.3.3 The net operating result for the general government sector in 2016-17 under AASB 1055 was $167 million more favourable than budgeted

Note 51 of the CFR provides a comparison of the original budget figures presented in line with AASB 1055 reporting requirements and the 2016-17 final outcome figures in the CFR.

The original budget figures in the 2016-17 Budget Papers are presented on the UPF basis. The UPF is based on the ABS Government Finance Statistics format. The Final Budget Outcome report produced by DTF reports on the final outcomes against the budget prepared under the UPF basis.

AASB 1055 requires that original budget information be disclosed in the CFR in line with AAS reporting requirements. As the SA Government does not present budgets on the AASB 1055 basis, a restated budget is presented in note 51 of the CFR to align with the accounting basis specified by the standard. Note 51 also outlines the variations between the AASB 1055 reporting basis and the UPF basis.

Figure 4.11 shows that the actual net operating balance and net lending/borrowing positions reflected in the 2016-17 Final Budget Outcome and CFR for the general government sector were more favourable than corresponding budget figures.

Figure 4.11: Budget and actual net operating balance and net lending/borrowing position for 2016-17 under UPF and AASs

	Net operating balance	Net lending/ borrowing
2016-17 Budget under UPF	$254 million surplus	$2.436 billion deficit
2016-17 Final Budget Outcome under UPF	$443 million surplus	$2.371 billion deficit
2016-17 Budget under AASB 1055	$269 million surplus	$2.422 billion deficit
Actual result in the 2016-17 CFR[3]	$436 million surplus	$2.378 billion deficit

The actual net operating surplus in the 2016-17 CFR is $436 million, compared to a surplus of $269 million in the 2016-17 Budget prepared consistent with AASB 1055 requirements.

The difference between the actual and budgeted result was mainly due to:

- a higher than budgeted dividend from MAC
- an unbudgeted income tax equivalent payment from ReturnToWorkSA
- lower interest expenses resulting from changes in the timing of commercial acceptance of the new RAH.

These impacts were partly offset by downward revisions to GST grant revenue and National Partnership grants compared to the original budget.

[3] Note 3 of the CFR discloses the differences in actual results reported under the UPF and AAS reporting frameworks. The differences for both the net operating balance and net lending/borrowing position were immaterial in 2016-17 ($7 million).

5 2016-17 Consolidated Financial Report financial position

Key points

- Total assets increased by $9.704 billion (9%) to $113.997 billion.
- The State's major assets are buildings, structures and land.
- Total liabilities increased by $5.027 billion (8%) to $71.57 billion.
- The State's major liabilities are borrowings and unfunded superannuation liabilities.
- The State's borrowings increased by $5.195 billion, mainly due to changes in SAFA's liquidity policy, the recognition of the new RAH finance lease liability and the Consolidated Account deficit in 2016-17.
- Unfunded superannuation liabilities decreased by $2.581 billion primarily as a result of an increase in the discount rate used to value the liabilities and increased rates of return on defined benefit plan assets.
- The State's net assets and net worth are $42.426 billion, which is a $4.677 billion increase from the prior year.

5.1 Analysis of variations with prior year

Figure 5.1 summarises the whole of government Statement of Financial Position for the year ended 30 June 2017 and comparative prior year figures.

Figure 5.1: Statement of Financial Position (whole of government)

	2016 $'million	2017 $'million
Assets		
Financial assets:		
Investments, loans and placements	11 856	14 429
Investments – other	20 795	23 620
Other	4 802	4 599
Total financial assets	37 453	42 648
Non-financial assets:		
Produced assets:[1]		
Buildings and structures	49 003	52 716
Other	4 322	4 997
Non-produced assets:[2]		
Land	12 779	13 032
Other	736	604
Total non-financial assets	66 840	71 349
Total assets	104 293	113 997

Liabilities	2016 $'million	2017 $'million
Borrowings	17 756	22 951
Unfunded superannuation liabilities	14 029	11 448
Superannuation fund deposits	24 209	27 178
Provisions (other than employee benefits)	5 306	4 830
Other	5 243	5 163
Total liabilities	66 543	71 570
Net assets	37 749	42 426
Equity		
Retained earnings	2 492	5 798
Reserves:		
Asset revaluation reserve	35 151	36 483
Other reserves	60	100
Financial assets available for sale reserve	46	46
Total equity (net worth)	37 749	42 426

Note: Totals may not add due to rounding.

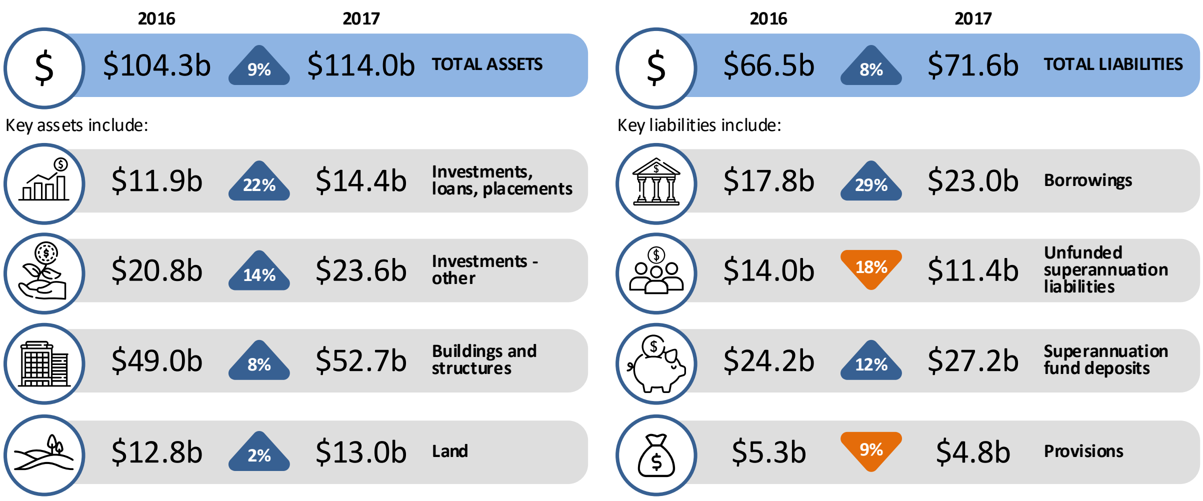
[1] Produced assets are non-financial assets that have come into existence as outputs from production processes.
[2] Non-produced assets are non-financial assets that come into existence other than through processes of production.

5.1.1 Significant increases in total assets and liabilities

Total assets increased by $9.704 billion (9%) to $113.997 billion, while total liabilities increased by $5.027 billion (8%) to $71.57 billion.

Figure 5.2 shows changes in assets and liabilities between 2015-16 and 2016-17 for key items.

Figure 5.2: Analysis of variations in assets and liabilities



5.1.2 Increase in total assets mainly due to increase in SAFA investments, growth in superannuation funds held under management by Funds SA and buildings and structures additions

The main variations in total assets from the prior year were:

- buildings and structures – increased by 8% or $3.713 billion. This is mainly due to the recognition of the leased building asset for the new RAH of $2.551 billion in 2016-17.
- investments– other – increased by 14% or $2.825 billion. This primarily reflects increases in superannuation funds held under management by Funds SA owing to improved investment market conditions in 2016-17 compared to the prior year
- investments, loans and placements – increased by 22% or $2.573 billion. This increase is mainly due to changes in SAFA's liquidity policy. SAFA sought to increase its liquidity to better align with market best practice and regulator and rating agencies' guidelines. To increase the amount of liquid funds available, new select line bonds were issued, with the proceeds placed in investments
- machinery and equipment – increased by 19% or $320 million. This is mainly due to the recognition of leased furniture, fixtures and equipment for the new RAH ($258 million).

Part B of the Auditor-General's Annual Report for the year ended 30 June 2017 'Agency audit reports' provides further details on variations between years for individual agencies.

5.1.3 Increase in total liabilities mainly due to increases in borrowings and superannuation fund deposits, offset partly by decreases in unfunded superannuation liabilities and provisions

The main variations in total liabilities from the prior year were:

- borrowings – increased by 29% or $5.195 billion. This increase is primarily attributable to changes in SAFA's liquidity policy, the recognition of the new RAH finance lease liability and the $618 million Consolidated Account deficit in 2016-17. SAFA sought to increase its liquidity to better align with market best practice and regulator and rating agencies' guidelines. New select line bonds were issued in order to increase the amount of liquid funds available
- superannuation fund deposits – increased by 12% or $2.969 billion. This is mainly due to the improved investment performance of superannuation funds managed by Funds SA in 2016-17 compared to the prior year
- unfunded superannuation liabilities – decreased by 18% or $2.581 billion. This is mainly due to a decrease in the estimated present value of the defined benefit obligation ($2.081 billion) and an increase in the fair value of the defined benefit plan assets ($500 million). The defined benefit obligation decreased primarily as a result of a movement in the discount rate used by the actuary to value the obligation. The discount rate was 2.5% at 30 June 2016 compared with 3.1% at 30 June 2017. The increase in the fair value of defined benefit plan assets is mainly due to increased rates of return in 2016-17 (12.4% in 2016-17 compared to 7% in 2015-16)

- provisions – decreased by 9% or $476 million. This is mainly due to a decrease in MAC motor vehicle compensation insurance claim provisions, resulting from payments made to settle claims in 2016-17 and changes to a range of assumptions in the actuarial calculations.

Part B of the Auditor-General's Annual Report for the year ended 30 June 2017 'Agency audit reports' provides further details on variations between years for individual agencies.

5.2 Trends in financial position

5.2.1 Net worth has trended upwards again after a dip in 2015-16

Net worth is an economic measure of wealth and provides an indication of a government's overall financial position. For the whole of government, net worth is calculated as total assets less total liabilities and shares/contributed capital.

Figure 5.3 shows the net worth for the whole of government over the past five years.

Figure 5.3: Net worth

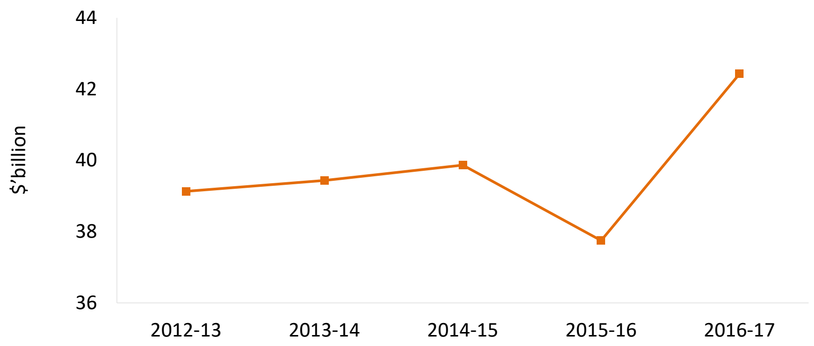


Figure 5.3 highlights that the net worth of the State has generally trended upwards over the past five years, except for a dip in 2015-16 that was mainly due to an increase in the unfunded superannuation liability that year arising from changes in actuarial estimates and assumptions.

The $4.677 billion increase in net worth in the Statement of Financial Position in 2016-17 is due to a $9.704 billion increase in total assets, offset by a $5.027 billion increase in total liabilities. Sections 5.1.2 and 5.1.3 provide further detail on the factors driving these increases.

5.2.2 Unfunded superannuation liability is a key driver of net worth

Figure 5.4 shows the unfunded superannuation liability, net worth and net worth excluding the unfunded superannuation liability over the past five years.

Figure 5.4: Unfunded superannuation liability and net worth

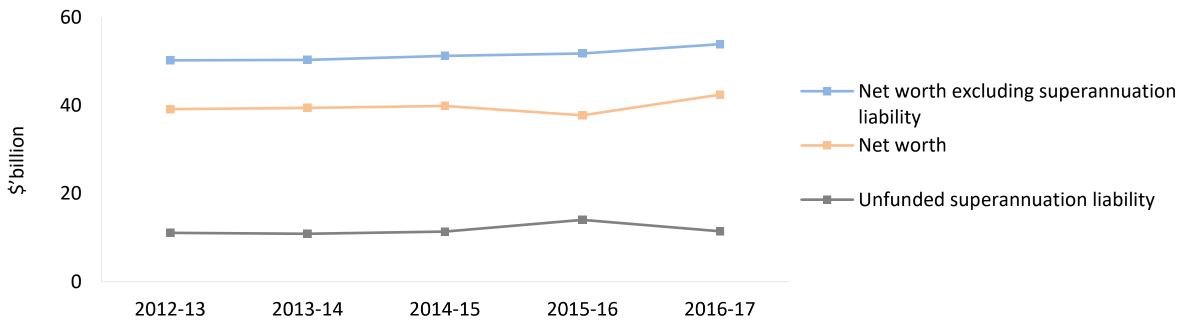


Figure 5.4 shows that the movement in net worth over the past five years has been the inverse of movements in the unfunded superannuation liability. It also shows that without the unfunded superannuation liability, there has been a slight trend upwards in net worth over the past five years.

The unfunded superannuation liability is a long-term liability to current and past members of closed defined benefit superannuation schemes. The 2016-17 Budget reported that while financial market volatility in the recent past has resulted in multi-billion dollar revisions to the value of the liability recorded on the balance sheet, there has been no material change in the actual expected payments to beneficiaries underlying the liability.

Unfunded superannuation liabilities are valued at points in time by discounting future superannuation benefit payments by a discount rate that reflects the prevailing risk-free interest rate, consistent with AAS requirements.

The SA Government reports that it remains committed to fully funding the superannuation liability by 2034.

Note 37 of the CFR provides further information on the actuarial calculation of the unfunded superannuation liabilities.

5.2.3 State assets primarily comprise buildings, structures and land

Figure 5.5 shows the composition of whole of government assets in the 2016-17 CFR.

Figure 5.5: Composition of the State's assets in the CFR

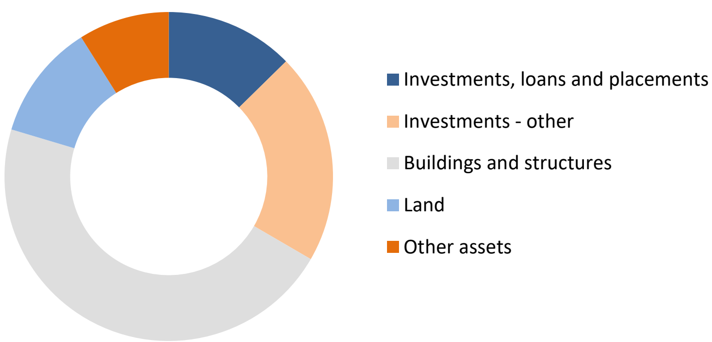


Figure 5.5 shows that the State's assets primarily comprise buildings and structures (46%), investments – other (21%), investments, loans and placements (13%) and land (11%).

Investments – other relates to superannuation investments held by Funds SA on behalf of members of the various State superannuation schemes. Funds SA has a corresponding liability to the members of these schemes that is reflected under superannuation fund deposits.

5.2.4 State liabilities primarily comprise borrowings and unfunded superannuation liabilities

Figure 5.6 shows the composition of whole of government liabilities in the 2016-17 CFR.

Figure 5.6: Composition of the State's liabilities in the CFR

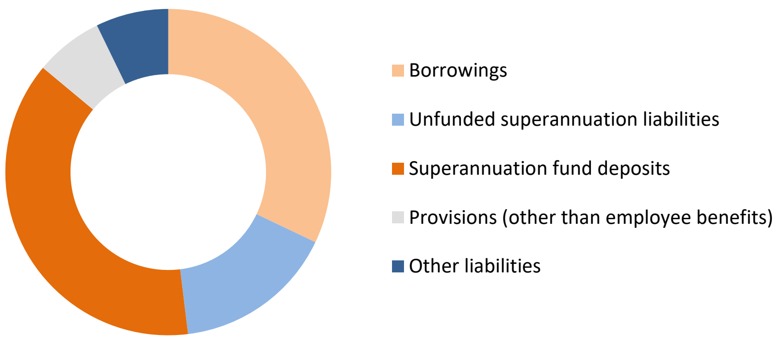


Figure 5.6 shows that the State's liabilities primarily comprise superannuation fund deposits (38%), borrowings (32%) and unfunded superannuation liabilities (16%).

The superannuation fund deposits relate to the funds invested by the various State superannuation schemes with Funds SA. Funds SA has a liability to the members of these schemes for the funds deposited. The corresponding superannuation fund investments held by Funds SA on behalf of members are reflected under assets in investments – other.

Figure 5.7 shows whole of government borrowings over the past five years.

Figure 5.7: Borrowings

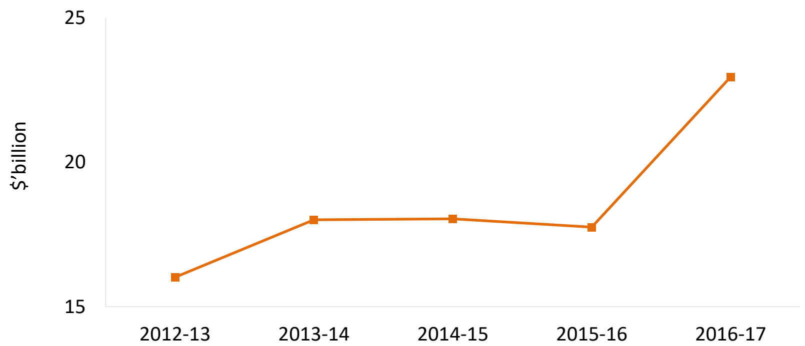


Figure 5.7 highlights that borrowings increased significantly in 2016-17 after remaining steady between 2013-14 and 2015-16. As outlined in section 5.1.3, this increase is mainly due to changes in SAFA's liquidity policy, the recognition of the new RAH finance lease liability and the Consolidated Account deficit in 2016-17.

5.3 Further commentary and analysis

5.3.1 $1.605 billion proceeds received from land services commercialisation after 30 June 2017

In August 2017 the Treasurer announced the outsourcing of lands titles services to Land Services SA (LSSA) for a 40-year concessional period. In October 2017 the SA Government received $1.605 billion in consideration from LSSA. The new arrangements for delivering State land registry and valuation services by LSSA then began.

The $1.605 billion receipt from LSSA will reduce the net lending/borrowing position and net debt in 2017-18 by $1.605 billion.

5.3.2 Land under roads was revalued as at 30 June 2017 by the Valuer-General resulting in a revaluation increment of $335 million

Land under roads is revalued by the Valuer-General on a triennial basis, with updates applied annually where movements in value are considered material. A triennial valuation was performed as at 30 June 2017.

An englobo valuation methodology was applied by the Valuer-General using the road network records of the Department of Planning, Transport and Infrastructure. This involved determining an englobo rate per square metre for regions throughout the State based on statutory site values, development classifications and local government area.

Based on the Valuer-General's estimate, land under roads was revalued to $2.496 billion, a $335 million revaluation increment on the 30 June 2016 carrying amount.

Appendix — Abbreviations used in this Report

Abbreviation	Description
AAS	Australian Accounting Standard
AASB 10	Consolidated Financial Statements
AASB 1049	Australian Accounting Standard AASB 1049 ‘Whole of Government and General Government Sector Financial Reporting’
AASB 1055	Australian Accounting Standard AASB 1055 ‘Budgetary Reporting’
ABS	Australian Bureau of Statistics
CFR	Consolidated Financial Report
CTP	Compulsory Third Party
DECD	Department for Education and Child Development
DEWNR	Department of Environment, Water and Natural Resources
DTF	Department of Treasury and Finance
FTE	Full-time equivalent
Funds SA	Superannuation Funds Management Corporation of South Australia
GST	Goods and services tax
MAC	Motor Accident Commission
PFC	Public financial corporation
PNFC	Public non-financial corporation
RAH	Royal Adelaide Hospital
ReturnToWorkSA	Return to Work Corporation of South Australia
SAFA	South Australian Government Financing Authority
SAHT	South Australian Housing Trust
SA Water	South Australian Water Corporation
UPF	Uniform Presentation Framework