Report of the Auditor-General

Auditor-General's Department

Report 3 of 2019

Consolidated Financial Report review

Government of South Australia

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18 March 2019

The Hon A L McLachlan CSC MLC
President
Legislative Council
Parliament House
ADELAIDE SA 5000

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

Dear President and Speaker

Report of the Auditor-General:
Report 3 of 2019 *Consolidated Financial Report review*

As required by the *Public Finance and Audit Act 1987*, I present to each of you Report 3 of 2019 *Consolidated Financial Report review*.

Content of the Report

The 2017-18 Consolidated Financial Report for the SA Government was published in January 2019. It fulfills the SA Government's consolidated financial reporting obligations under AASB 1049 *Whole of Government and General Government Sector Financial Reporting*. This report provides our observations and detailed commentary on it, including our recommendations for improving the way financial information is collected, validated and consolidated in preparing it.

Acknowledgements

The audit team for this report was Daniel O'Donohue, Bill Sierros and Sonia Yin.

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 2017-18 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 controls over the preparation 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 Australian Accounting Standard AASB 1049 *Whole of Government and General Government Sector Financial Reporting*. It reports the SA Government's actual financial performance and position for the year. The 2017-18 CFR was published on the Department of Treasury and Finance (DTF) website in January 2019.[1]

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, public non-financial corporation (PNFC) and public financial corporation (PFC) sectors. The nature and activities of these sectors is explained further in section 2.

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 Auditor-General's Report 1 of 2019 *State Finances and related matters*.

[1] *Consolidated Financial Report 2017-18*, www.treasury.sa.gov.au/budget/current-budget/previous-budgets/budget-2017-18, viewed March 2019.

1.2 Conclusion

Our review of the CFR 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.

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.

1.3 Key overall observations

1.3.1 The whole of government reported a $675 million net operating balance deficit for 2017-18, up from $246 million last year

The deficit increased because the increase in total expenses, mainly due to higher use of goods and services, employee and interest expenses, was higher than revenue growth, mainly from grant revenue.

1.3.2 The whole of government reported a net lending deficit of $825 million in 2017-18, down from $3.588 billion in 2016-17

The $2.763 billion decrease is due mainly to the recognition of $2.5 billion assets under financial lease relating to the new RAH in 2016-17.

1.3.3 The State is increasingly reliant on Commonwealth grant revenue, particularly GST revenue

Grant revenue is the largest revenue stream for the State. As a percentage of total revenue, it increased from 44% in 2013-14 to 52% in 2017-18. This is mainly due to growth in GST grants from the Commonwealth Government. Section 4.4.4 provides further detail on trends in grant revenue.

1.3.4 The State's total assets and liabilities both increased in 2017-18

Total assets increased by $5.357 billion (5%) to $119.451 billion, while total liabilities increased by $4.796 billion (7%) to $76.366 billion.

The increase in total assets is mainly due to:

- a $2.374 billion (10%) increase in other investments, which mainly relate to equities in listed and unlisted companies held by the Superannuation Funds Management Corporation of South Australia (Funds SA) and Return to Work Corporation of South Australia (RTWSA)

- a $1.726 billion (3%) increase in buildings and structures
- a $956 million (7%) increase in investments, loans and placements.

The increase in total liabilities is mainly due to:

- a $2.908 billion (11%) increase in superannuation fund deposits
- a $1.77 billion (223%) increase in other liabilities, of which $1.5 billion relates to unearned revenue arising from the land services commercialisation transaction.

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

1.3.5 Matters reflected in Independent Auditor's Reports for government agencies in 2017-18 included inherent uncertainty in some liabilities of the Return to Work SA Corporation of South Australia and the Lifetime Support Authority of South Australia

As noted in section 1.2, we do not provide an audit opinion on the CFR. However, we provided a management letter summarising the results of our review to DTF in January 2019. It included the agency specific audit matters we identified that would impact on the audit opinion for the CFR, if we provided one.

I noted in the letter that, while I had not modified my Independent Auditor's Reports for RTWSA and the Lifetime Support Authority of South Australia for 2017-18, I drew attention to the inherent uncertainty associated with their care, support and claim liabilities.

1.4 What we recommended

We issued a management letter to DTF's Chief Executive in January 2019 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 Australian Accounting Standard AASB 10 *Consolidated Financial Statements*
- moving significant accounting policies to the respective note to improve the understandability of the CFR
- ensuring the CFR includes, where material, all disclosures required under applicable accounting standards
- establishing a procedure outlining the scope, nature and timing of actuarial work to be undertaken in performing the unfunded superannuation liability calculations, including the roles and responsibilities of the staff involved.

1.5 Response to our recommendations

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

- performing further work to establish whether the identified agencies are controlled entities of government
- moving significant accounting policies to the respective note in the 2018-19 CFR
- reviewing its data collection procedures to obtain the necessary information to meet required disclosure requirements. Where DTF elects not to meet specific disclosure requirements, it will document the basis for this
- establishing a procedure outlining the scope, nature and timing of actuarial work to be undertaken in performing the unfunded superannuation liability calculations for 2018-19, including the roles and responsibilities of the staff involved.

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 2018 was prepared by DTF under AASB 1049 and includes 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 the South Australian Housing Trust (SAHT) and South Australian Water Corporation (SA Water).
- PFCs – bodies primarily engaged in providing financial services. This includes financial institutions such as the South Australian Government Financing Authority (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 Australian Bureau of Statistics (ABS).[2] However, it is important to note that some technical differences remain between AASB 1049 and the Uniform Presentation Framework 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.

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2 *Australian System of Government Finance Statistics: Concepts, Sources and Methods*, Australia, 2015, ABS (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 commentary and analysis on the:

- actual financial performance and position of the whole of government
- controls over the preparation of the 2017-18 CFR.

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.

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

Auditor-General's Report 1 of 2019 *State Finances and related matters* provides commentary on the 2017-18 State Budget estimated results and final budget outcome of the general government sector.

3.3 What we reviewed and how

Our review in 2017-18 covered:

- the principles adopted in defining the economic entity for the purposes of CFR reporting
- 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.

4 2017-18 Consolidated Financial Report financial performance

Key points

- The whole of government reported a $675 million net operating balance deficit for 2017-18, compared to a $246 million net operating balance deficit in the prior year.
- There is a $336 million difference between the whole of government and general government sector 2017-18 net operating balances, due mainly to agency operating surpluses in the PNFC and PFC sectors offset by the elimination of transactions between the general government sector and the PNFC and PFC sectors in the CFR.
- Grants are a key revenue stream, representing 52% of total whole of government revenue in 2017-18.
- Employee expenses are the largest component of expenditure in 2017-18 at 38% and have decreased as a percentage of total whole of government expenditure over the past two years.
- The whole of government reported a net lending deficit of $825 million in 2017-18, compared to a net lending deficit of $3.588 billion in the prior year. The $2.763 billion decrease was due mainly to the recognition of $2.5 billion of assets under finance lease for the new RAH in 2016-17.

4.1 Net operating balance

4.1.1 The net operating balance deficit increased in 2017-18

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.

The whole of government reported a $675 million net operating balance deficit for 2017-18, compared to a $246 million net operating balance deficit for 2016-17.

Figure 4.1 shows the whole of government and general government net operating balances for the past five years.

Figure 4.1: Net operating balances

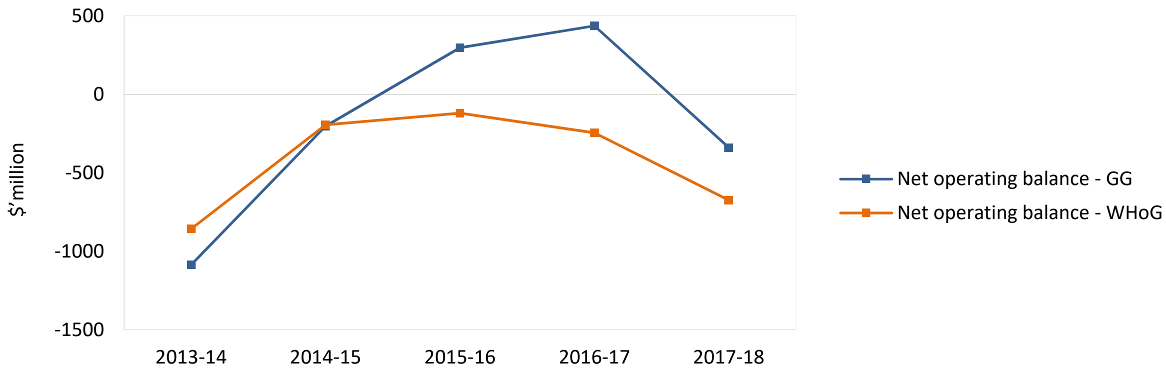


Figure 4.1 shows that following a trend towards surplus between 2013-14 and 2015-16, the whole of government net operating balance deficit has increased from 2016-17. Section 4.4 provides further detail about changes in revenues and expenditure.

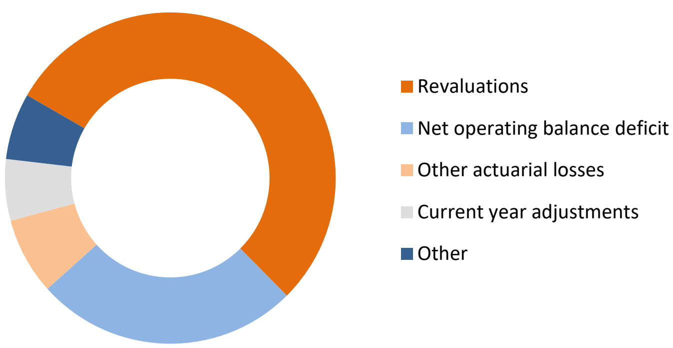
The $429 million increase in the whole of government net operating balance deficit in 2017-18 was less than the $775 million increase in the general government sector net operating balance deficit over the same period. The $346 million variance reflects increases in PNFC ($195 million) and PFC ($231 million) net operating balance surpluses, offset by a $79 million increase in consolidation eliminations. Refer note 2 to the CFR.

4.2 Total change in net worth

4.2.1 The State's net worth has increased by $561 million, mainly because of revaluations

Figure 4.2 shows the main drivers for the $561 million increase in net worth in 2017-18 for the whole of government in the Statement of Comprehensive Income.

Figure 4.2: Main reasons for net worth increase in 2017-18



The change in net worth is mainly the result of an increase in asset revaluation reserves ($1.42 billion). The main revaluation increments were $408 million on SAHT properties, $290 million on Department of Planning, Transport and Infrastructure roads and structures,

$117 million on Women's and Children's Health Network Incorporated land and buildings and $83 million on Southern Adelaide Local Health Network Incorporated land and buildings.

The change is net worth was also influenced by the net operating balance deficit ($675 million) and the following other economic flows:

- other net actuarial losses ($197 million) primarily driven by increases in the RTWSA Compensation Fund outstanding claims liability ($296 million), self-insured agencies workers compensation claims liability ($80 million) and long service leave liabilities ($66 million), offset by a $344 million decrease in Motor Accident Commission (MAC) insurance claim provisions
- current year adjustments – prior period ($157 million), the most significant relating to a $22 million adjustment by the Department for Environment and Water to recognise land dedicated as conservation parks in 2016-17
- other economic outflows ($145 million) primarily driven by write-offs of $38 million in SA Water purchased seasonal water allocations, $32 million in SA Water abandoned water and sewer infrastructure and derecognised capital works in progress, $21 million in SAHT assets demolished and $14 million in Central Adelaide Local Health Network Incorporated (CALHN) buildings derecognised.

4.3 Net lending/borrowing position

4.3.1 The net lending/borrowing position has varied significantly over the past five years

The net lending/borrowing position is the net operating balance less 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 4.3 shows the whole of government and general government net lending/borrowing position for the past five years.

Figure 4.3: Net lending/borrowing position

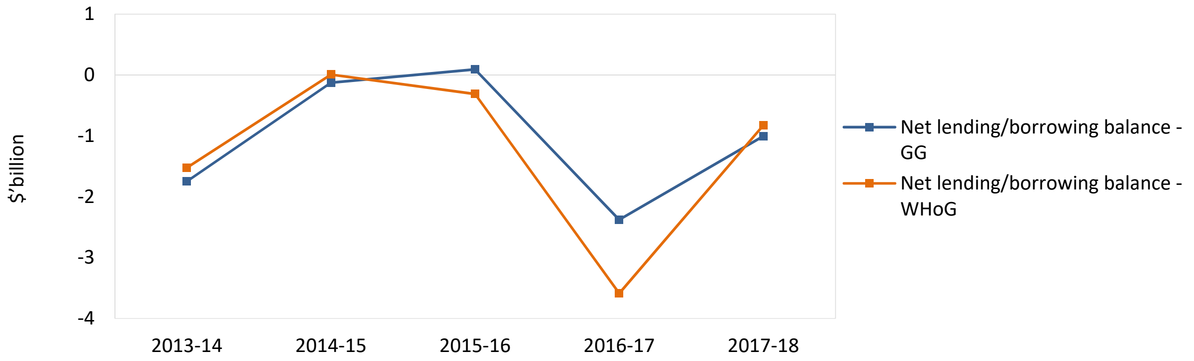


Figure 4.3 shows the significant variability in the net lending/borrowing position over the past five years, with a reduced net lending/borrowing deficit in 2017-18.

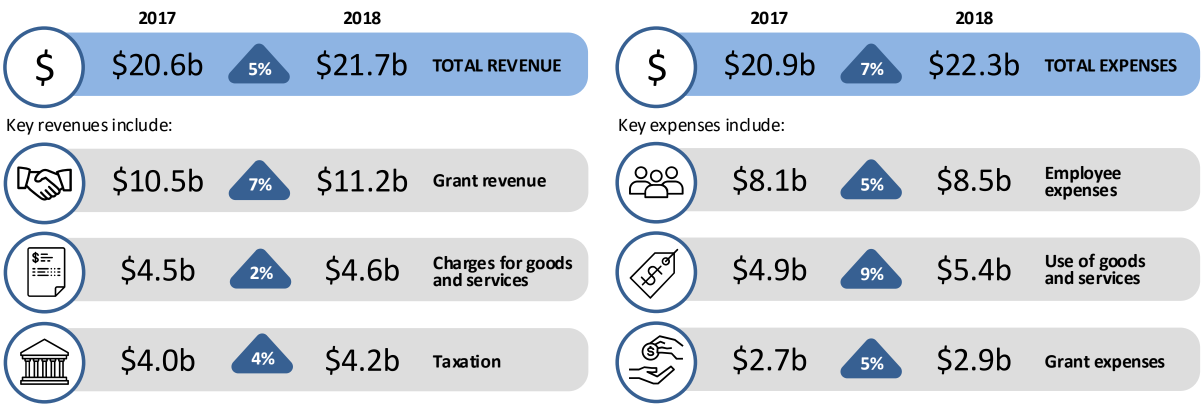
The net lending deficit of $3.588 billion for the whole of government in 2016-17 mainly reflected the recognition of $2.5 billion of assets under finance lease for the new RAH, recognised by CALHN following commercial acceptance on 13 June 2017.

4.4 Revenue and expenditure

4.4.1 Modest increases in total revenue and expenditure

Figure 4.4 shows changes in revenue and expenditure between 2016-17 and 2017-18 for key items.

Figure 4.4: Analysis of variations in revenue and expenditure



Total revenue increased in 2017-18 by $1.039 billion (5%). Total expenditure increased by a slightly higher $1.468 billion (7%).

4.4.2 Increase in total revenue mainly due to higher grant and taxation revenue

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

- grant revenue – increased by 7% or $724 million. This was mainly a result of higher GST grant revenue from the Commonwealth Government, increased capital grants under the Intergovernmental Agreement on Federal Financial Relations and specific purpose grants to the Department for Health and Wellbeing
- taxation revenue – increased by 4% or $143 million, mainly due to increases in taxes on employers' payroll and labour force ($83 million) and gambling taxes ($36 million), the reasons for which are explained in section 4.4.5.

Auditor-General's Report 5 of 2018 *Annual Report for the year ended 30 June 2018, Part B: Agency audit reports* provides further details on variations between years for individual agencies.

4.4.3 Increase in total expenses mainly due to higher use of goods and services, employee and interest expenses

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

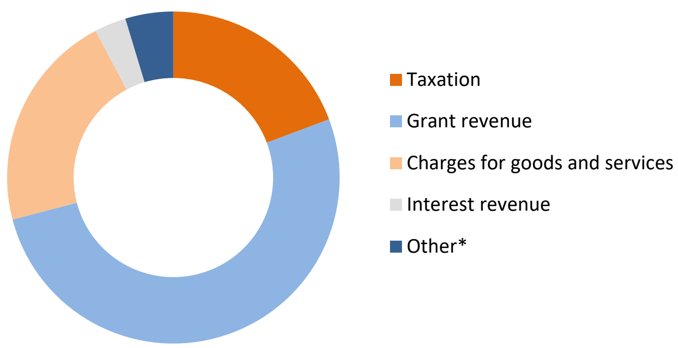
- use of goods and services – increased by 9% or $453 million. The increased expenditure mainly occurred in local health networks ($167 million), the Department for Child Protection ($119 million), the Department of the Premier and Cabinet (DPC) ($97 million) and DTF ($58 million). Increased expenditure included $82 million paid by DPC for short-term emergency electricity supply and $43 million in land title fees paid by DTF to Land Services SA (LSSA)
- employee expenses – increased by 5% or $414 million. This growth was due mainly to increases in salary and wages expenses of $349 million, primarily due to enterprise agreement increases and increases in FTEs
- interest expenses – increased by 31% or $285 million, mainly reflecting the full year impact of interest charges on the new RAH finance lease, recognised by CALHN following commercial acceptance on 13 June 2017.

Auditor-General's Report 5 of 2018 *Annual Report for the year ended 30 June 2018, Part B: Agency audit reports* provides further details on variations between years for individual agencies.

4.4.4 The State is increasingly reliant on Commonwealth grant revenue

Figure 4.5 shows the composition of whole of government revenue in the 2017-18 CFR.

Figure 4.5: Composition of revenue

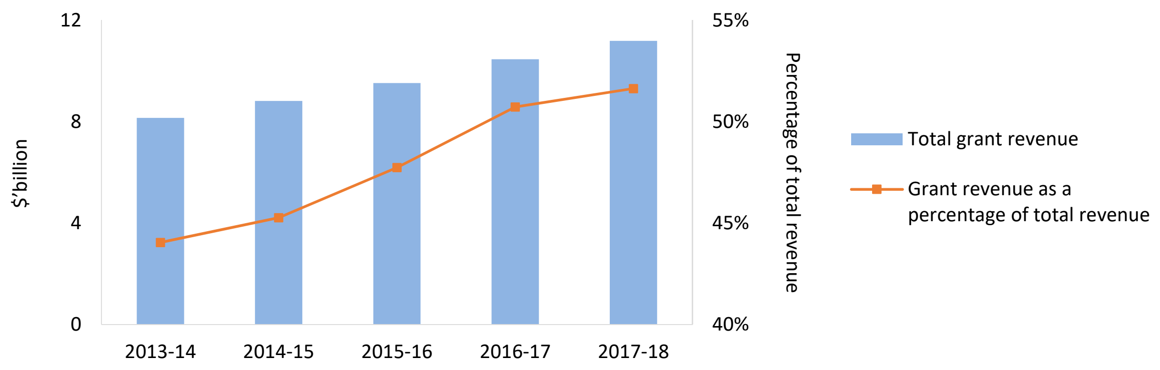


* Includes dividends and income tax equivalents and other revenues.

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 2017-18.

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

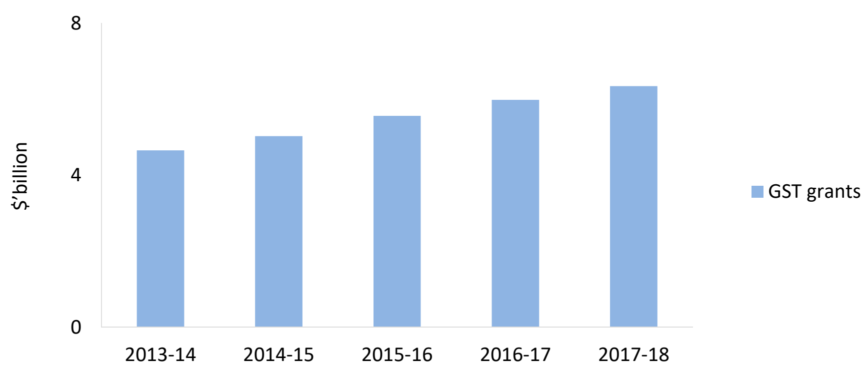
Figure 4.6: Grant revenue as a percentage of total revenue



Grant revenue, as a percentage of total revenue, has increased from 44% in 2013-14 to 52% in 2017-18. This largely reflects growth in GST grants from the Commonwealth Government, which made up 57% of total grant revenue in 2017-18.

Figure 4.7 shows the growth in GST grants over the last five years.

Figure 4.7: GST grants



The growth in grant revenue in 2017-18 also reflects increased capital funding from the Commonwealth in 2017-18.

The other major revenue streams for the State are goods and services charges (21%) and taxation (19%).

4.4.5 Taxation revenue increased modestly in 2017-18 from the prior year

Taxation revenue was $4.18 billion in 2017-18, compared to $4.037 billion in the prior year. The 4% increase is mainly due to:

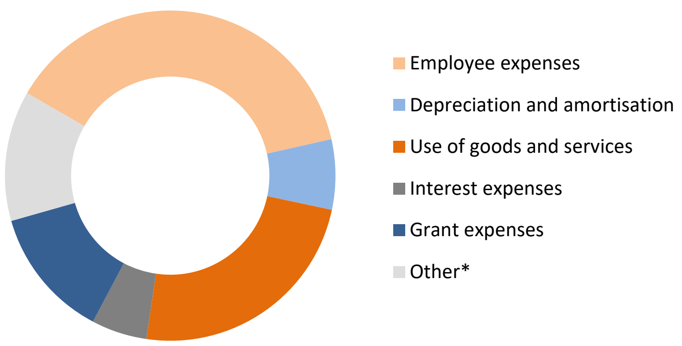
- a $36 million (10%) increase in gambling tax following the introduction of the new Betting Operations Tax from 1 July 2017

• an $83 million (7%) increase in taxes on employers' payroll and labour force, which reflected strong growth in taxable payrolls between 2016-17 and 2017-18 and growth in the number and size of employers liable for payroll tax.

4.4.6 Employee expenses as a percentage of total expenditure decreased in 2017-18

Figure 4.8 shows the composition of whole of government expenses in the 2017-18 CFR.

Figure 4.8: Composition of expenditure



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

Figure 4.8 highlights that employee expenses are the largest component of expenditure for the State, representing 38% of total expenses from transactions in 2017-18. The other major components of expenditure are use of goods and services expenses (24%) and grant expenses (13%).

Figure 4.9 shows whole of government employee expenses over the past five years and those expenses as a percentage of total expenses.

Figure 4.9: Employee expenses as a percentage of total expenses

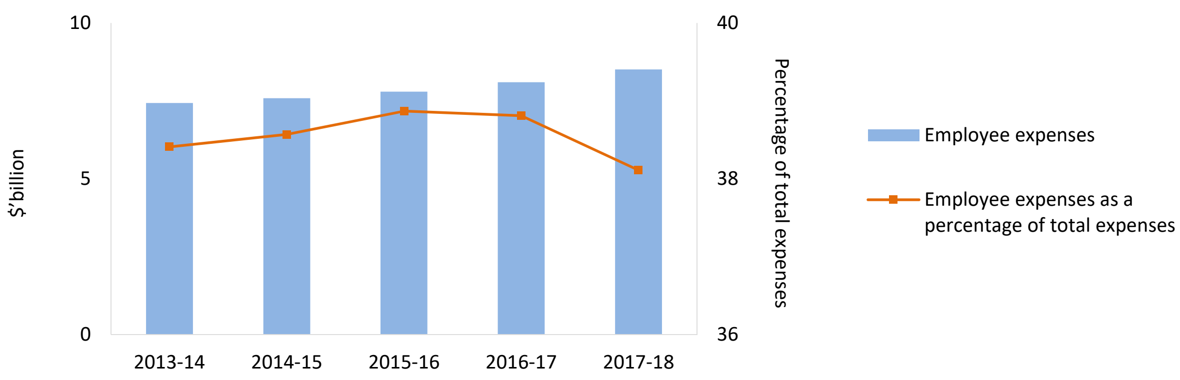


Figure 4.9 highlights that employee expenses as a percentage of total expenses trended marginally upwards between 2013-14 and 2015-16 before trending downwards from 2016-17.

Figure 4.10 shows the year on year percentage change in total whole of government employee expenses over the past five years.

Figure 4.10: Year on year percentage change in employee expenses

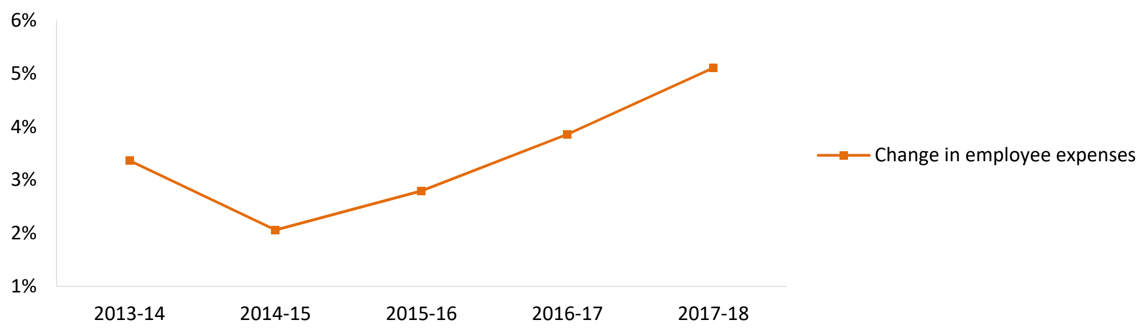


Figure 4.10 highlights that percentage year on year growth in employee expenses fell from 2013-14 to 2014-15, but has since trended up, rising to 5% in 2017-18 mainly owing to enterprise agreement increases and additional FTEs in each year since 2015-16.

Figure 4.11 shows the growth in FTE employee numbers for the whole of government over the past five years.

Figure 4.11: Whole of government FTEs

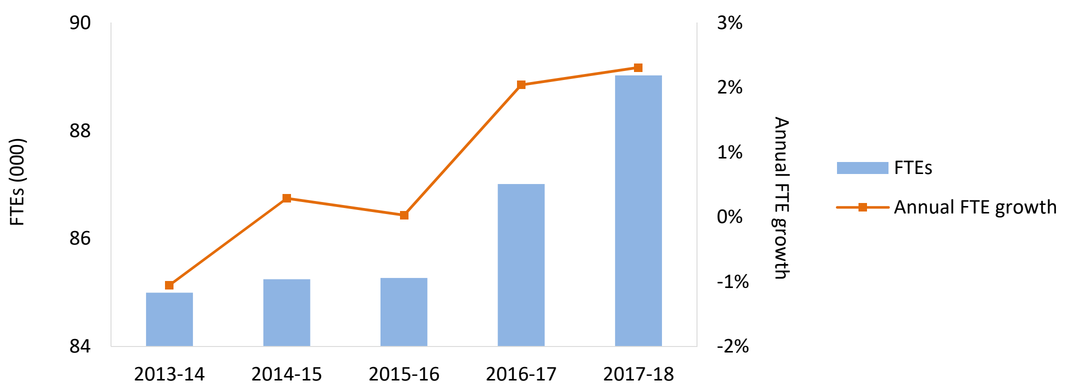


Figure 4.11 highlights that there has been an upward trend in total FTE numbers since 2013-14 reaching the highest level in 2017-18, with larger 2% increases between 2015-16 (85 272 FTEs), 2016-17 (87 011 FTEs) and 2017-18 (89 022 FTEs). The increase in FTEs in 2017-18 is primarily due to additional positions in local health networks, the Department for Education and the Department for Child Protection, offset by reductions in positions in the Department of Human Services and the Department for Health and Wellbeing.

4.5 Further commentary and analysis

4.5.1 Variations in other economic flows primarily attributable to actuarial gains and losses and gains and losses on financial assets and financial liabilities at fair value

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

- net actuarial gain (loss) on superannuation defined benefit plans – $82 million gain in 2017-18 compared to a $2.468 billion gain in the prior year. This is mainly due to a small decrease in the discount rate used to value the unfunded superannuation liability from 3.1% at 30 June 2017 to 2.9% at 30 June 2018, which marginally increased the unfunded superannuation liability
- other net actuarial gains (losses) – decreased by $733 million to a loss of $197 million. This is primarily due to changes in actuarial assumptions for the RTWSA Compensation Fund outstanding claims liability, MAC insurance claims liability and self-insured agencies workers compensation claims liabilities
- gains (losses) on financial assets or financial liabilities at fair value – decreased by $411 million to $84 million. This is mainly due to a $331 million decrease on revaluation of financial instruments and derivatives held by SAFA and a $102 million decrease on revaluation of financial assets under management by Funds SA, reflecting market valuations.

4.5.2 The difference between the whole of government and general government sector net operating balances is $336 million

The net operating balance for the whole of government in 2017-18 was a deficit of $675 million. This compares to a $339 million net operating balance deficit for the general government sector, a $336 million difference.

The whole of government reported result reflects the elimination of all transactions between all government entities, 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 2017-18 are outlined in note 52 of the CFR 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 ($190 million)
- income tax equivalents from SA Water ($58 million)

- guarantee fees from PNFCs and PFCs ($147 million)
- interest revenue on deposit accounts ($89 million)
- dividend revenue from MAC ($342 million)
- dividend revenue from SA Water ($139 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:

- loan interest paid to SAFA ($249 million)
- community service obligation payments made to SA Water ($144 million)
- fleet expenses paid to SAFA ($51 million)
- grants from the Department of Human Services to SAHT ($246 million)
- operating lease rental expenses paid by the Department of State Development to the Urban Renewal Authority for the use of technical and further education sites ($54 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 recorded the only significant operating loss for the PNFC and PFC sectors in 2017-18.

5 2017-18 Consolidated Financial Report financial position

Key points

- Total assets increased by $5.357 billion (5%) to $119.451 billion.
- The State's major non-financial assets are buildings, structures and land.
- The State's building and structures increased by $1.726 billion (3%) to $54.421 billion.
- The State's investments increased by $3.33 billion (9%) to $41.379 billion.
- Total liabilities increased by $4.796 billion (7%) to $76.366 billion.
- The State's major liabilities are superannuation fund deposits, borrowings and unfunded superannuation liabilities.
- The State's superannuation fund deposits increased by $2.908 billion (11%) to $30.086 billion.
- The State's other liabilities increased by $1.77 billion, primarily due to the land services commercialisation transaction which has resulted in unearned revenue of $1.5 billion being recognised as a liability.
- The State's net assets and net worth are $43.085 billion, which is a $561 million increase from the prior year.

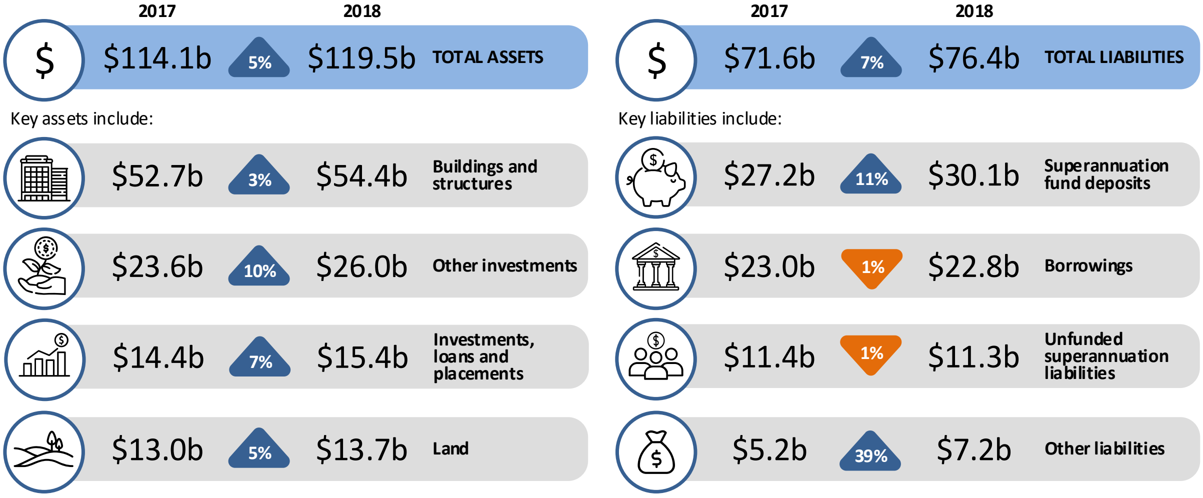
5.1 Assets and liabilities

5.1.1 The State's total assets and liabilities both increased in 2017-18

Total assets increased by $5.357 billion (5%) to $119.451 billion, while total liabilities increased by $4.796 billion (7%) to $76.366 billion.

Figure 5.1 shows changes in assets and liabilities between 2016-17 and 2017-18 for key items.

Figure 5.1: Analysis of variations in assets and liabilities



5.1.2 Increase in total assets mainly due to growth in superannuation funds and buildings, structures and land additions, offset by a decline in non-financial assets held for sale

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

- other investments – increased by 10% or $2.374 billion. This primarily reflects increases in superannuation funds held under management by Funds SA owing to strong investment performance
- buildings and structures – increased by 3% or $1.726 billion. This is mainly due to additions of $1.548 billion (mainly relating to the road network, bus and rail tracks) and revaluation increments of $848 million (mainly relating to the road network, buildings and water, sewerage and drainage assets), offset by $1.189 billion in depreciation charged for the year
- investments, loans and placements – increased by 7% or $956 million. This is mainly due to strong investment performance, revaluing investments at market value and additional funds invested by RTWSA, MAC, Lifetime Support Authority of South Australia and Funds SA
- land – increased by 5% or $599 million. This is mainly due to the revaluation of land held by SAHT ($361 million) and the Department for Education ($69 million)
- non-financial assets classified as held for sale – decreased by 98% or $788 million. This is mainly due to the sale of the Techport Australia Common User Facility and associated assets and the MAC Direct Property Portfolio in 2017-18.

Auditor-General's Report 5 of 2018 *Annual Report for the year ended 30 June 2018, Part B: 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 superannuation fund deposits and other liabilities

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

- superannuation fund deposits – increased by 11% or $2.908 billion. This is mainly due to the strong investment performance of superannuation funds managed by Funds SA
- other liabilities – increased by 223% or $1.77 billion. This is mainly due to a $1.577 billion increase in unearned revenue, which is primarily due to the land services commercialisation transaction that has resulted in unearned revenue of $1.5 billion being recognised as a liability.

Auditor-General's Report 5 of 2018 *Annual Report for the year ended 30 June 2018, Part B: Agency audit reports* provides further details on variations between years for individual agencies.

5.1.4 State assets primarily comprise buildings, structures and land

Figure 5.2 shows the composition of whole of government assets in the 2017-18 CFR.

Figure 5.2: Composition of the State's assets in the CFR

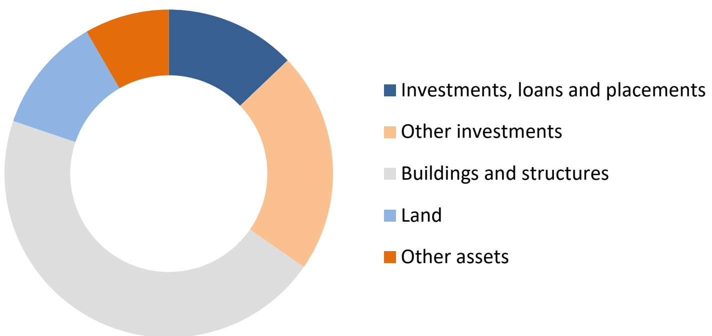


Figure 5.2 shows that the State's assets primarily comprise buildings and structures (46%), other investments (22%), investments, loans and placements (13%) and land (11%).

Other investments mainly relate 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.

5.1.5 State liabilities primarily comprise borrowings and unfunded superannuation liabilities

Figure 5.3 shows the composition of whole of government liabilities in the 2017-18 CFR.

Figure 5.3: Composition of the State's liabilities in the CFR

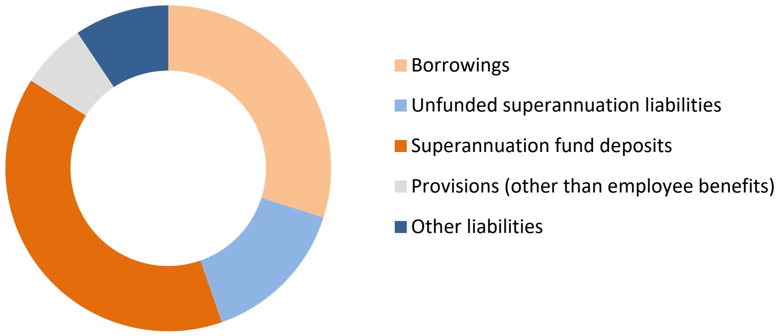


Figure 5.3 shows that the State's liabilities primarily comprise superannuation fund deposits (39%), borrowings (30%) and unfunded superannuation liabilities (15%).

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 other investments.

Figure 5.4 shows whole of government borrowings over the past five years.

Figure 5.4: Borrowings

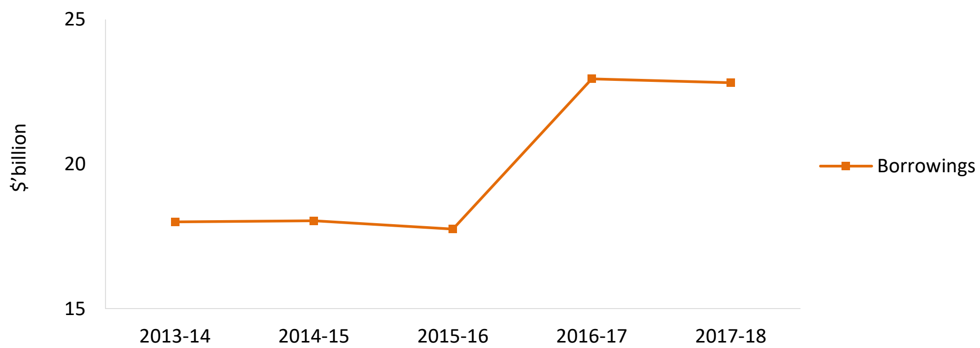


Figure 5.4 highlights that borrowings remained steady in 2017-18 after a significant increase in 2016-17.

The $5.195 billion increase in 2016-17 was due mainly to changes in SAFA's liquidity policy, the recognition of a $2.809 billion finance lease liability for the new RAH 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 bonds were issued to increase the amount of liquid funds available.

5.2 Further commentary and analysis

5.2.1 Net worth has continued to trend upwards

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

Figure 5.5: Net worth

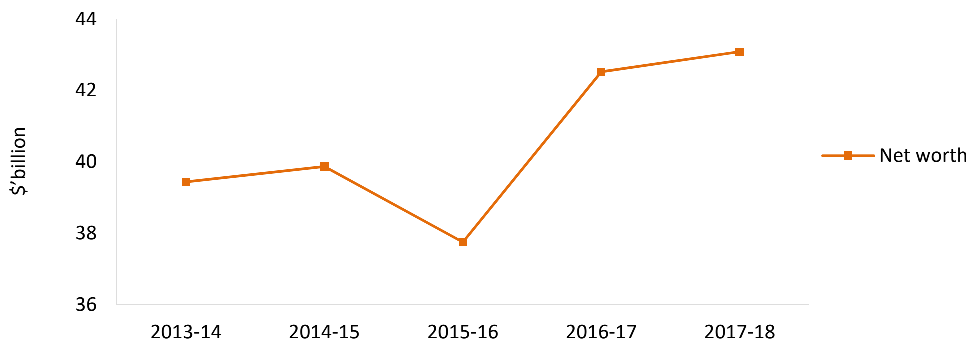


Figure 5.5 highlights that the net worth of the State has generally trended upwards over the past five years, except for a dip in 2015-16 that was mainly due to an increase in the unfunded superannuation liability that year arising from changes in actuarial estimates and assumptions.

The major drivers behind the $561 million increase in net worth in the Statement of Financial Position in 2017-18 are discussed in sections 5.1.2 and 5.1.3.

5.2.2 Unfunded superannuation liability is a key driver of net worth

Figure 5.6 shows the unfunded superannuation liability, net worth and net worth excluding the unfunded superannuation liability over the past five years.

Figure 5.6: Unfunded superannuation liability and net worth

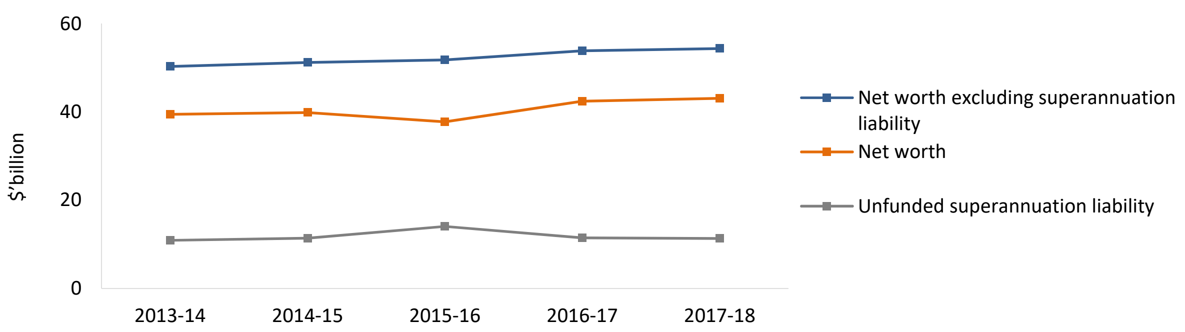


Figure 5.6 shows that the movement in net worth over the past five years has been the inverse of movements in the unfunded superannuation liability. It also shows that without the unfunded superannuation liability, there has been a slight trend upwards in net worth over the past five years.

The unfunded superannuation liability is a long-term liability to current and past members of closed defined benefit superannuation schemes. The 2017-18 State 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.[3]

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 Australian Accounting Standards 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 $1.605 billion proceeds received from land services commercialisation in October 2017

In August 2017 the Treasurer announced the commercialisation of lands titles and valuation services to LSSA for 40 years. 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 principles of Australian Accounting Standard AASB 1059 *Service Concession Arrangements: Grantors* and industry practice were applied to account for the transaction.[4]

Accordingly, the following was recognised in the CFR for the transaction:

- cash proceeds of $1.605 billion from LSSA
- revenue of $27 million representing a part-year recognition of proceeds in 2017-18 on a straight-line basis
- a liability of $1.498 billion at 30 June 2018 reflecting the unearned revenue arising from the cash proceeds received
- a liability of $80 million at 30 June 2018 reflecting the possible repayment to LSSA if the SA Government does not proceed with commercialisation of another State registry or award an additional seven years on the contract.

The overall impact of the transaction was a $27 million reduction in the 2017-18 net lending/borrowing position and $27 million increase in net worth at 30 June 2018.

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3 2017-18 Budget Paper 3 *Budget Statement*, page 66.

4 Further detail on the transaction is included in Auditor-General's Report 5 of 2018 *Annual Report for the year ended 30 June 2018, Part B: Agency audit reports*, pages 461-464.

Appendix – Abbreviations used in this Report

Abbreviation	Description
AASB 1049	Australian Accounting Standard AASB 1049 *Whole of Government and General Government Sector Financial Reporting*
ABS	Australian Bureau of Statistics
CALHN	Central Adelaide Local Health Network Incorporated
CFR	Consolidated Financial Report
DPC	Department of the Premier and Cabinet
DTF	Department of Treasury and Finance
FTE	Full-time equivalent
Funds SA	Superannuation Funds Management Corporation of South Australia
GG	General government
GST	Goods and services tax
LSSA	Land Services SA
MAC	Motor Accident Commission
PFC	Public financial corporation
PNFC	Public non-financial corporation
RAH	Royal Adelaide Hospital
RTWSA	Return to Work Corporation of South Australia
SAFA	South Australian Government Financing Authority
SAHT	South Australian Housing Trust
SA Water	South Australian Water Corporation
WHoG	Whole of government


Summary sale