

Chapter 3 **Fiscal Strategy**

Overview This chapter outlines the Territory Government's fiscal strategy, including medium-term fiscal objectives and financial targets. The fiscal strategy provides a sound fiscal management framework to ensure sustainable service provision, continued investment in infrastructure and a competitive tax environment that supports economic growth.

The 2007-08 Fiscal Strategy remains unchanged from that set out in the 2006-07 Budget and aims to ensure substantial service provision particularly in the areas of health, education, community safety and investment in infrastructure. The importance of a strong financial position is paramount for a jurisdiction such as the Territory with a limited revenue base but high expenditure requirements.

As discussed in Chapter 2, the contribution towards the Territory's superannuation liability for 2006-07 results in an underlying cash outcome, operating result and fiscal balance. The Territory will adopt these underlying targets from 2006-07 as its primary Budget measures.

The Government's medium-term fiscal objectives and projected achievements against targets are:

- **Sustainable Service Provision**

Target: General government net operating balance by 2012-13.

Assessment: Operating surplus predicted for all years.

- **Infrastructure for Economic and Community Development**

Target: Maintain total public sector infrastructure investment at appropriate levels and achieve a general government net lending balance by 2012-13.

Assessment: Increased capital investment in 2007-08 of \$629 million and continuing high investment over forward years.

Assessment: Fiscal balance continues on a trend to surplus with a small net borrowing of \$10 million by 2010-11.

- **Competitive Tax Environment**

Target: Ensure Territory taxes and charges are competitive with the average of the states.

Assessment: Taxation revenue per capita of \$1765 in 2007-08, second lowest, after Tasmania, and significantly lower than the average of the states at \$2341.

- **Prudent Management of Liabilities**

Target: Net debt plus employee liabilities as a proportion of total revenue to fall.

Assessment: Net debt plus employee liabilities to revenue ratio continues to fall over the forward estimates to 110 per cent by 2010-11.

Fiscal Principles

The *Fiscal Integrity and Transparency Act* (FITA) requires the Treasurer to deliver a fiscal strategy statement at the time of each Budget which specifies the Government's medium-term fiscal objectives and key fiscal indicators. Under the FITA, the fiscal strategy statement must be based on principles of sound fiscal management to:

- formulate and apply spending and taxation policies having regard to the effect of these policies on employment, economic prosperity and the development of the Territory economy;
- formulate and apply spending and taxing policies so as to give rise to a reasonable degree of stability and predictability;
- ensure that funding for current services is provided by the current generation; and
- prudently manage financial risks faced by the Territory (having regard to economic circumstances), including the maintenance of Territory debt at prudent levels.

These financial management principles underpin the Territory's fiscal strategy.

Sustainable Service Provision – Target: General Government Net Operating Balance by 2012-13

The expected cash outcome for 2006-07 has improved due to continued growth in economic activity resulting in increased mining royalties and stamp duty on conveyances, along with the effect of timing of capital payments for the Darwin Waterfront Development. These factors have resulted in an improvement of \$105 million in 2006-07. This has enabled a contribution of \$60 million to be made towards the Territory's superannuation liability and results in an underlying deficit of \$11 million. All other years' cash targets remain unchanged, with a return to balance still expected in 2008-09 and a surplus of \$34 million projected for 2010-11.

Table 3.1 compares the cash targets set in the 2006-07 Budget, with the revised 2007-08 Budget targets.

Table 3.1: General Government Cash Outcome

| | 2006-07 Estimate | 2007-08 Budget | 2008-09 | 2009-10 | 2010-11 |
|-------------------------|---------------------|-------------------|---------|---------|---------|
| | Forward Estimates | | | | |
| 2006 Cash Targets (\$M) | - 56 | - 40 | 0 | 17 | na |
| 2007 Cash Targets (\$M) | - 11 | - 40 | 0 | 17 | 34 |

Source: Northern Territory Treasury.

The net operating balance for 2006-07 and forward years, as shown in Table 3.2, represents an increase in all years on the estimates in the 2006-07 Budget. This is due to higher goods and services tax (GST) revenue, together with an upward revision to own-source revenue as a result of increased economic activity, particularly for mining royalties and stamp duty on conveyancing. These increases have been partially offset by the initiatives introduced as part of the 2007-08 Budget, together with an increase in unfunded superannuation expenses following a recent actuarial reassessment.

As a proportion of total revenue, Table 3.2 shows that the net operating balance is estimated to be better in 2006-07 and 2007-08 with improvement of revenue, coupled with ongoing spending restraint. By 2010-11 the projected \$38 million surplus means that the ratio improves to 1.04 per cent.

**Table 3.2 General Government
Net Operating Balance**

| | 2006-07 | 2007-08 | 2008-09 | 2009-10 | 2010-11 |
|---|----------|---------|-------------------|---------|---------|
| | Estimate | Budget | Forward Estimates | | |
| 2006 Net Operating Balance (\$M) | 17 | - 18 | - 15 | 4 | na |
| 2007 Net Operating Balance (\$M) | 31 | 29 | 8 | 15 | 38 |
| 2007 Net Operating Balance as a Proportion of Total Revenue (%) | 0.96 | 0.85 | 0.23 | 0.43 | 1.04 |

Source: Northern Territory Treasury.

Table 3.3 shows the ratio of the Territory's net operating balance to revenue compared with the average of the states.

**Table 3.3: State and Territory
Net Operating Balance as
a Proportion of Revenue
– General Government**

| | 2005-06 | 2006-07 | 2007-08 |
|------------------------------|------------|------------|------------|
| | Actual | Estimate | Budget |
| | % | % | % |
| New South Wales | 2.4 | - 1.1 | 0.8 |
| Victoria | 2.6 | 1.1 | 1.1 |
| Queensland | 2.6 | 1.1 | 1.1 |
| South Australia | 1.8 | 0.1 | 0.9 |
| Western Australia | 14.0 | 10.1 | 8.3 |
| Tasmania | 3.4 | - 3.1 | - 2.2 |
| Australian Capital Territory | - 6.5 | - 4.0 | - 4.4 |
| State Average | 5.7 | 1.1 | 1.6 |
| Northern Territory | 0.7 | 1.0 | 0.9 |

Source: Northern Territory Treasury and state budget, mid-year and outcome reports.

The projected cash position and operating balance continue to indicate that the accrual target of an operating balance by 2012-13 remains realistic.

Infrastructure for Economic and Community Development – Target: Maintain Infrastructure Investment at Appropriate Levels and Achieve Fiscal Balance by 2012-13

Capital investment is a large component of the Government's budget strategy to meet both the Territory's social and economic requirements.

The provision of adequate levels of infrastructure is an ongoing challenge for the Territory due to both its remoteness and its stage of development, relative to the other states.

Net lending (fiscal balance) provides a measure of the Territory's investment balance (that is, as a lender or a borrower). Net lending includes the effect of both capital and operating transactions after excluding the effect of depreciation.

Consistent with the net operating balance revised estimates, the fiscal balance shows improvement since the 2006-07 Budget in all years and is trending towards a balanced position.

When comparing against other jurisdictions, Table 3.4 shows the Territory's net lending to revenue is projected to be marginally better than the average of the states in 2007-08.

Table 3.4: State and Territory
Net Lending (+)/ Borrowing (-)
as a Proportion of Revenue
– General Government

| | 2005-06 | 2006-07 | 2007-08 |
|------------------------------|--------------|--------------|--------------|
| | Actual | Estimate | Budget |
| | % | % | % |
| New South Wales | - 1.1 | - 5.3 | - 3.2 |
| Victoria | - 1.2 | - 2.7 | - 2.6 |
| Queensland | 8.2 | - 6.5 | - 6.5 |
| South Australia | 0.7 | - 1.8 | - 2.6 |
| Western Australia | 11.4 | 4.4 | 1.7 |
| Tasmania | 2.3 | - 3.0 | - 1.3 |
| Australian Capital Territory | - 6.7 | - 10.5 | - 6.4 |
| State Average | 2.5 | - 3.6 | - 3.2 |
| Northern Territory | - 1.7 | - 2.2 | - 2.9 |

Source: Northern Territory Treasury and state budget, mid-year and outcome reports.

The fiscal balance deficits indicate that capital spending in all years is greater than the depreciation expense, which is consistent with a developing economy such as the Territory. The effect of the Territory's substantial capital investment associated with the Darwin Waterfront Development in 2006-07 and 2007-08 remains evident in Table 3.5. As a proportion of total revenue, net lending is estimated to be - 2.9 per cent in 2007-08 improving to -0.3 per cent by 2010-11. As with the net operating balance, the trend of improvement over the forward estimates would indicate that the Territory's aim of a balanced position by 2012-13 will be achieved.

Table 3.5: General
Government Net Lending (+)/
Borrowing (-)

| | 2006-07 | 2007-08 | 2008-09 | 2009-10 | 2010-11 |
|--------------------------------------|----------|---------|------------------|---------|---------|
| | Estimate | Budget | Forward Estimate | | |
| Net Lending (+)/Borrowing (-) (\$M) | - 71 | - 96 | - 41 | - 32 | - 10 |
| As a Proportion of Total Revenue (%) | - 2.2 | - 2.9 | - 1.2 | - 0.9 | - 0.3 |

Source: Northern Territory Treasury.

When considering capital investment in the Territory, it is more appropriate to look at the non financial public sector. It better reflects the complete picture of Government spending on infrastructure projects, and includes the Power and Water Corporation which will be investing approximately \$600 million over 2007-08 and forward years in the essential services of electricity, sewerage and water.

Table 3.6 presents the estimates for infrastructure investment for 2006-07 to 2010-11. The government's capital investment, including the Darwin Waterfront Development, comprises purchases of non financial assets (including construction and capital items), assets acquired under finance lease (to include the Convention Centre) and capital grants to non-government organisations. It excludes repairs and maintenance.

**Table 3.6: Capital Investment
– Non Financial Public Sector**

| | 2006-07 | 2007-08 | 2008-09 | 2009-10 | 2010-11 |
|-------------------------------------|------------|------------|------------------|------------|------------|
| | Estimate | Budget | Forward Estimate | | |
| | \$M | \$M | \$M | \$M | \$M |
| Purchases of Non Financial Assets | 419 | 506 | 426 | 390 | 405 |
| Assets Acquired Under Finance Lease | 48 | 34 | 1 | 1 | 1 |
| Capital Grants | 83 | 89 | 115 | 105 | 103 |
| Total | 549 | 629 | 542 | 495 | 509 |

Source: Northern Territory Treasury.

The high investment in 2006-07 and 2007-08 remains attributable to the Darwin Waterfront Development. In all other years, capital expenditure is still significantly higher than historic levels due to ongoing infrastructure requirements in the Territory and the investment of approximately \$600 million by the Power and Water Corporation. Further information on capital works projects is included in *Budget Paper No. 4*.

Competitive Tax Environment – Target: Ensure Territory Taxes and Charges are Competitive with the Average of the States

The Government is committed to maintaining a competitive tax environment to encourage increased levels of business activity in the Northern Territory.

As part of the 2007-08 Budget, the Government has announced further revenue measures to build on economic and employment growth and has confirmed the removal of certain taxes under the national tax reform agreement.

In the 2005-06 Budget, the Government committed to the abolition of a number of stamp duties as part of the national tax reform. Most of these stamp duties have already been abolished, with stamp duty on hiring arrangements to be abolished from 1 July 2007.

The Government's remaining commitment to national tax reform is the abolition of stamp duty on business property conveyances (excluding land) from 1 July 2009.

A more detailed analysis of these revenue initiatives is provided in Chapter 4 of this Budget Paper.

In order to assess the competitiveness of the Territory's tax system, the following measures are utilised:

- taxation revenue per capita; and
- taxation effort as assessed by the Commonwealth Grants Commission (the Commission).

Taxation revenue per capita is a simple summary measure that affords comparability with other jurisdictions.

Table 3.7 shows that the Territory's tax collections per capita for 2007-08 are estimated at \$1765, compared with \$2341 for the average of the other states. This also highlights that the Territory in 2007-08 is expected to collect the second lowest per capita tax revenues, after Tasmania.

The Territory's 2005-06 actual of \$1810 reflected large one-off stamp duty transactions in that year. The 2006-07 and 2007-08 estimates continue to show an increase in economic activity, however at a lower base.

**Table 3.7: Taxation Revenue
Per Capita – General
Government**

| | 2005-06 | 2006-07 | 2007-08 |
|------------------------------|---------------|---------------|---------------|
| | \$ per capita | \$ per capita | \$ per capita |
| New South Wales | 2 326 | 2 442 | 2 541 |
| Victoria | 2 130 | 2 183 | 2 220 |
| Queensland | 1 817 | 2 028 | 2 172 |
| Western Australia | 2 520 | 2 671 | 2 655 |
| South Australia | 1 912 | 2 016 | 2 058 |
| Tasmania | 1 436 | 1 483 | 1 571 |
| Australian Capital Territory | 2 373 | 2 510 | 2 672 |
| State Average | 2 143 | 2 264 | 2 341 |
| Northern Territory | 1 810 | 1 724 | 1 765 |

Source: State and territory outcome reports, state and territory budget papers; ABS Cat. No. 3101.0.

Although taxation per capita is a useful comparative measure, it is limited in that it does not make any allowances for differences in states' capacities to raise revenue.

A more sophisticated measure of tax competitiveness is the Commission's analysis of 'tax effort', which adjusts for the extent to which a particular state's capacity to raise revenue is above or below average. Table 3.8 details the Territory's revenue-raising capacity and effort expressed as a percentage of the Australian average in 2005-06, the latest year assessed by the Commission.

**Table 3.8: Northern Territory
Revenue-Raising Capacity
and Effort 2005-06
Australian Average
= 100 per cent**

| | Capacity ¹ | Effort ² |
|--|-----------------------|---------------------|
| | % | % |
| Total Taxation | 82 | 111 |
| Total Own-Source Revenue | 94 | 99 |
| Total Taxation plus Royalties and Public Safety User Charges | 92 | 101 |

¹ Northern Territory's capacity to raise revenue compared to the Australian average.

² Northern Territory's revenue effort compared with the Australian average, given the capacity available.

Source: Commonwealth Grants Commission 2007 Update.

The Commission's assessment shows that the Territory's total tax effort in 2005-06 was above the Australian average. This is due to a number of large one-off stamp duty transactions in that year. Arguably a better comparative measure for 2005-06 is taxation combined with mining royalties and public safety user charges.

On this basis, the Territory's tax effort (101 per cent) remains slightly above the Australian average and the third lowest, after Tasmania and Queensland. This, together with the per capita measure, demonstrates that the Territory continues to provide a competitive tax environment for Territorians.

Further interjurisdictional comparisons of individual tax revenue measures and a more detailed synopsis of the methodology used by the Commission are provided in Chapter 8 of this Budget Paper.

Prudent Management of Liabilities – Target: Net Debt and Employee Liabilities as a Proportion of Total Revenue to Fall

This element of the fiscal strategy aims to ensure that debt is prudently managed, taking into consideration service delivery needs and investment in infrastructure required to promote social wellbeing and economic growth. The measures of net debt and net debt plus employee liabilities provide the means of assessing the Territory's performance against this target.

Net debt for the non financial public sector is projected to increase until 2009-10, in line with the contributions to the Darwin Waterfront Development, before declining to \$1742 million in 2010-11, below the 2001-02 level of \$1753 million. This improvement has been achieved even with record levels of capital investment in infrastructure in all years.

When compared to the states, the Territory's net debt for the non financial public sector remains higher due to the greater requirement for infrastructure investment. This is highlighted by Chart 3.1, which shows the Territory's net debt as a proportion of revenue against the states for the 2005-06 outcomes.

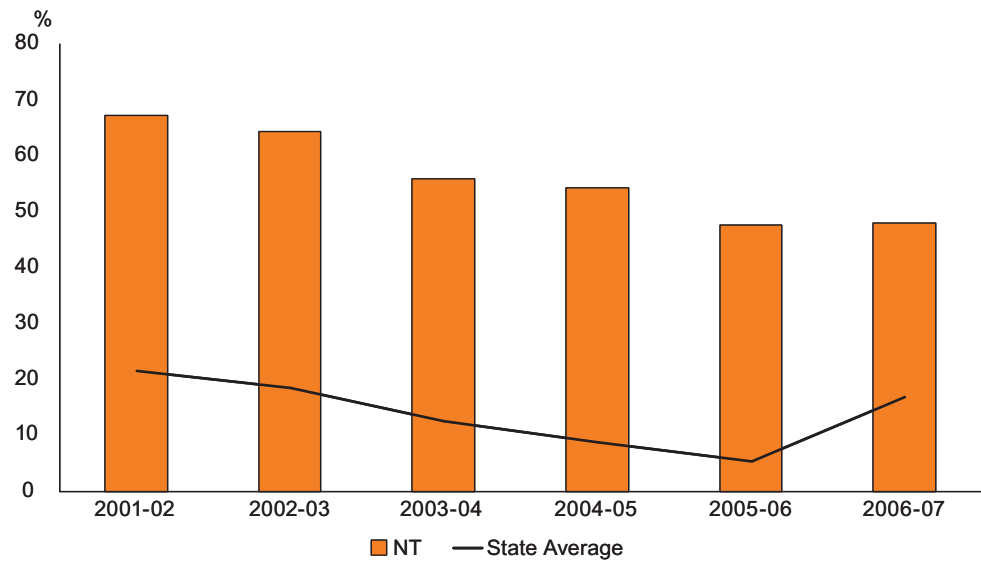
Chart 3.1: State and Territory
Net Debt to Revenue
– Non Financial Public Sector
2005-06 Outcomes



Source: State and territory outcome reports.

Chart 3.2 also compares the level of Territory debt with the average of the states for 2001-02 through to 2006-07 and shows the Territory is beginning to improve, relative to the states.

Chart 3.2: Historical State and Territory Net Debt to Revenue – Non Financial Public Sector



Source: State and Territory outcome reports, state and territory budget papers.

Net debt plus employee liabilities is a broader measure than net debt in that it encompasses unfunded employee liabilities, consisting largely of unfunded superannuation which is a major liability for the Territory and most states.

The level of net debt plus employee liabilities as a percentage of revenue for the non financial public sector is expected to fall. This is as a direct result of successive cash surpluses through to 2005-06 and the improving projected outcomes over the forward estimate period. The improving trend is despite the updated superannuation actuarial assessments and scheme revaluations in 2006, which have resulted in increases in the Commonwealth Superannuation Scheme liabilities for 2006-07.

Table 3.9 shows the effect of the Government's continuing commitment to prudently manage debt and employee liabilities while maintaining service provision. This highlights that the level of net debt plus employee liabilities as a percentage of revenue will continue to drop from the 2006-07 estimate of 116 per cent to 110 per cent in 2010-11. This represents a significant reduction on the 134 per cent recorded in 2001-02.

Table 3.9: Northern Territory Net Debt and Employee Liabilities – Non Financial Public Sector

| | 2006-07 Estimate | 2007-08 Budget | 2008-09 Forward Estimate | 2009-10 Forward Estimate | 2010-11 Forward Estimate |
|---|---------------------|-------------------|-----------------------------|-----------------------------|-----------------------------|
| Net Debt (\$M) | 1 578 | 1 693 | 1 748 | 1 749 | 1 742 |
| Net Debt to Revenue (%) | 44 | 45 | 45 | 44 | 42 |
| Net Debt plus Employee Liabilities (\$M) | 4 196 | 4 382 | 4 481 | 4 537 | 4 578 |
| Net Debt plus Employee Liabilities to Revenue (%) | 116 | 116 | 115 | 114 | 110 |

Source: Northern Territory Treasury.

Further information on budget aggregates and financial projections that underpin the Territory's fiscal strategy are included in Chapter 2 of this Budget Paper.