

# Budget Operations Framework

For Victorian Government Departments

Updated February 2017



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and Finance

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# Introduction

## Purpose

The Budget Operations Framework (BOF) serves to assist Victorian Government Departments in understanding and applying the financial and legislative framework that underpins budgeting and funding processes.

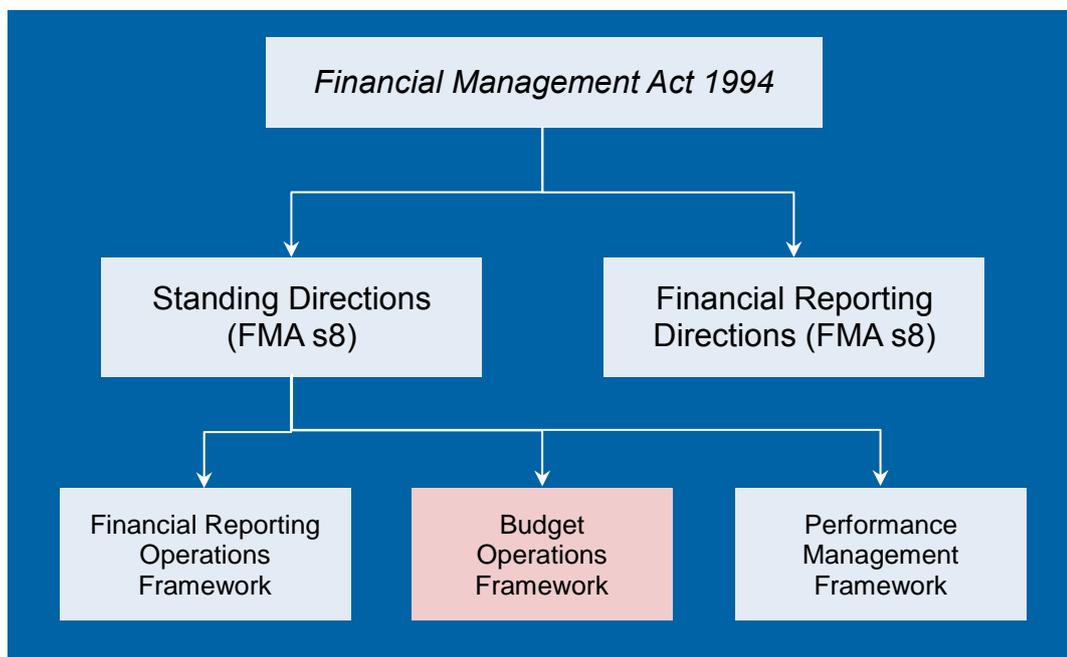
The BOF includes mandatory requirements for Departments on specific budget and funding topics. It also includes extensive guidance material.

## Legal status

The BOF is issued by the Deputy Secretary, Budget and Finance Division at the Department of Treasury and Finance (DTF), and mandated for Departments by direction of the Minister for Finance in the *Standing Directions of the Minister for Finance 2016* (Standing Directions)<sup>1</sup>.

The following diagram illustrates how the BOF fits into the broader financial management framework for Victorian public sector agencies:

Figure 1: The Budget Operations Framework within Victoria's Financial Management Framework



<sup>1</sup> See Standing Direction 4.3.

## Application and compliance

The BOF applies to all Victorian Departments.<sup>2</sup>

The Accountable Officer of each Department must ensure that the BOF is applied by the Department.<sup>3</sup>

Applying the BOF requires complying with its mandatory requirements (refer to the information provided under 'Structure' below).

Departments are subject to the compliance requirements set out in the Standing Directions in relation to the BOF. This includes public attestation of compliance in annual reports from 2017-18. Refer to the Standing Directions for more information, in particular Direction 5.1.

The *Financial Management Act 1994* (FMA) requires Departments and Victorian public sector entities to comply with requirements in relation to financial management. While the Standing Directions only mandate the BOF for Departments, other entities subject to aspects of the FMA are expected to comply with its related requirements. For example, an agency that is subject to the Capital Assets Charge should comply with BOF 3.2 (Capital Assets Charge). The expectation is that agencies using public resources should manage and account for those resources transparently, consistent with stated government policies and, as far as possible, consistently with other agencies.

Other agencies are not bound by the BOF, but may voluntarily adopt it where relevant.

## Commencement, DTF role and currency

The BOF formally commenced on 1 July 2016. This version of the BOF is being released in February 2017 and is **effective immediately**.

The BOF supersedes a number of Budget and Financial Management Guidances (BFMGs) previously issued by DTF under the *Standing Directions of the Minister for Finance 2003* (2003 Directions). The BFMGs were discontinued on 1 July 2016, along with the 2003 Directions.

DTF manages and implements the BOF on behalf of the Deputy Secretary, Budget and Finance Division. To ask a question or provide feedback on the BOF, email [financial.frameworks@dtf.vic.gov.au](mailto:financial.frameworks@dtf.vic.gov.au)

The BOF may be amended and re-issued from time to time. Departmental CFOs will be notified of any new releases of the BOF. Please also check the DTF website to ensure you are working with the latest version.

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<sup>2</sup> 'Department' is defined as having the same meaning as para (a) of *department* in section 3 of the FMA.

<sup>3</sup> Refer to Direction 4.3.

## Structure

The BOF consists of two components:

- mandatory requirements; and
- non-mandatory guidance material.

This document is divided into the following chapters:

- Setting the context for the State's Budget;
- The legislation supporting the State's resource management framework;
- The State's appropriation framework;
- Mechanisms available to manage departmental funding levels;
- Accrual budgeting concepts;
- Asset funding and management policies;
- Other budget policies
- Concepts and mechanisms underpinning budget and financial management; and
- Guidance on estimates updates.

An additional section sets out relevant attachments.

The chapters are presented as follows:

### 1. Example chapter one

#### 1.1 Example section one

Mandatory requirements EXAMPLE SECTION	
<b>1.1.1 Mandatory requirement example one</b>	Explanatory detail about mandatory requirement one, including: <ul style="list-style-type: none"><li>(a) specific provisions, requirements and directions; and</li><li>(b) additional related requirements</li></ul>
<b>1.1.2 Mandatory requirement example two</b>	Departments must apply mandatory requirement two.

#### Guidance

Guidance information which is non-mandatory in nature. This section attempts to assist the reader in gaining a broader understanding of the mandatory requirements laid out above. In certain sections, there are examples and worked examples provided in the attachments section.

# Definitions

Term	Definition
<b>Additions to the Net Assets Base (ATNAB)</b>	An appropriation that provides for an increase in the net capital base of a Department's statement of financial position.
<b>Administered item</b>	An item that will generally be characterised by the relevant Department lacking the capacity to benefit from that item in the pursuit of the Department's objectives, and the Department lacking the capacity to deny or regulate the access of others to that benefit.
<b>Appropriation</b>	An authority given by the Parliament to draw certain sums out of the Consolidated Fund, now or at some future point in time, for the purposes stated, up to the limit of the amount in the particular Act.
<b>Capital Assets Charge (CAC)</b>	A charge levied on the written-down value of controlled non-current physical assets in a Department's balance sheet which aims to attribute to agency outputs the opportunity cost of capital used in service delivery.
<b>Carryover</b>	Occurs where an annual appropriation amount for the previous year was not applied and where the Treasurer has approved the application of this amount in the next financial year, under section 32 of the FMA. Special or standing appropriations are not impacted by the carryover provisions.
<b>Competitive neutrality</b>	Involves achieving a fair market environment by removing or offsetting any competitive advantages or disadvantages due to public ownership of the government business.
<b>Consolidated Fund</b>	The Government's primary financial account, established by the FMA, that receives all Consolidated Revenue under the <i>Constitution Act 1975</i> and other monies as defined in section 9 of the FMA.
<b>Contributed Capital</b>	The recognition and reporting of the investment by the State in Departments and their portfolio agencies, as reflected in a Department's financial statements.
<b>Controlled item</b>	Generally refers to the capacity of a Department to benefit from that item in the pursuit of the entity's objectives and to deny or regulate the access of others to that benefit.
<b>Department</b>	Has the same meaning as para (a) of <i>department</i> in section 3 of the FMA.
<b>Depreciation</b>	The systematic allocation of the cost of a tangible asset over its useful life.
<b>Depreciation equivalent asset investment funding</b>	The quantum of funds equal to actual depreciation expense which is provided to a Department as output revenue for asset investment within its portfolio.
<b>Equity investment in controlled entities</b>	Refers to the Government's equity investment in a Department and other controlled entities of the State, in its capacity as owner (Refer to Contributed Capital also).
<b>Financial Management Act 1994 (FMA)</b>	One of the key pieces of legislation underpinning the Financial Management Framework of Victoria. The purposes of this Act are: <ul style="list-style-type: none"> <li>(a) to improve financial administration of the public sector;</li> <li>(b) to make better provision for the accountability of the public sector; and</li> <li>(c) to provide for annual reporting to the Parliament by Departments and public sector bodies.</li> </ul>

Term	Definition
<b>Long service leave equivalent</b>	The quantum of funds equal to actual long service leave expense, which is provided to a Department from output revenue for paying out long service leave entitlements drawn down by employees.
<b>Long service leave expense</b>	Recognises long service leave accrued by employees during the reporting period. Referred to as a non-cash cost.
<b>National Partnership payments (NPs)</b>	A type of Commonwealth grant for a specific purpose (i.e. paid by the Commonwealth to support the delivery of specific projects, facilitate reforms, or reward jurisdictions that deliver on nationally significant reforms). Refer also to Specific Purpose Payments (SPPs).
<b>Outputs</b>	Are products or services produced or delivered by a Department/agency for external customers.
<b>Payments on behalf of the State (POBOS)</b>	An appropriation that provides for payments to be made on behalf of the State. The Department making the payment has no direct control with respect to the quantity of outputs delivered.
<b>Price</b>	The amount that Government is prepared to pay for the provision of an output with specified measurable attributes and other attributes.
<b>Provision for Long Service Leave</b>	An obligation (liability) of a Department to its employees for accrued outstanding long service leave.
<b>Public Account</b>	The Government's principal bank account. All cash transactions relating to the Consolidated Fund, the Trust Fund and Advances under sections 36 and 37 of the FMA are processed through the Public Account.
<b>Special Appropriations</b>	Used for ongoing payments that need to be made independently of the Government's annual budget priorities. Special Appropriations represent a standing authority and do not lapse each year as annual appropriations do. They instead remain in force until the relevant legislation providing for the special appropriation is amended or repealed by Parliament.
<b>Specific Purpose Payments (SPPs)</b>	A type of Commonwealth grant for a specific purpose. National Specific Purpose Payments (National SPPs) are paid annually by the Commonwealth in key service delivery sectors. Refer also to National Partnership payments (NPs).
<b>State Administration Unit (SAU)</b>	The SAU serves two primary functions: <ul style="list-style-type: none"> <li>(a) as a mechanism for recording transaction flows and balances within the Public Account; and</li> <li>(b) a means of capturing certain relationships and balances between the Government (with DTF as the 'corporate head office') and Departments (such as Contributed Capital balances).</li> </ul>
<b>Surplus/deficit</b>	Arises when the operating revenue generated by a Department is greater/less than the Department's operating expenses for a particular accounting period. This is also known as the net result from transactions (net operating balance).
<b>Temporary Advance</b>	An advance provided by the Treasurer under section 35 of the FMA to a Minister to enable him/her to meet urgent claims in the current budget year before parliamentary sanction is obtained.

Term	Definition
<b>Treasurer's Advance</b>	An annual appropriation to the Treasurer to meet urgent expenditure claims that were unforeseen at the time of the Budget. Amounts advanced under this authority are reported to and sanctioned by the Parliament in a subsequent year's Annual Appropriation Bill.
<b>Trust accounts</b>	Separate accounts in the Trust Fund, which contain moneys set aside for specific purposes. The specific purpose for the establishment of each Trust Account is defined by the Minister, pursuant to sections 19 or 23 of the FMA, or is contained in a separate statute.
<b>Trust Fund</b>	Forms part of the State's Public Account, along with the Consolidated Fund. The Trust Fund encompasses a number of specific purpose accounts for funds that are not subject to parliamentary appropriation.
<b>User charges</b>	Receipts that satisfy the following criteria: <ul style="list-style-type: none"> <li>(a) the receipt originates from payments made voluntarily for goods and services provided; and the payments made; and</li> <li>(b) the benefits gained by the user can be clearly linked to the cost of providing the products and services.</li> </ul>
<b>Warrant</b>	A written authority to spend specified sums during the financial year from the Consolidated Fund which must be signed by the Treasurer, the Auditor-General and the Governor (refer to section 93 of the <i>Constitution Act 1975</i> and section 17 of the FMA).
<b>Working accounts</b>	A trust account facility (under section 23 of the FMA) designed to provide Departments with direct access to user charge receipts for those activities conducted on a cost recovery or commercial basis separately from core Departmental operations.

## Setting the context for the State's Budget

Governments collect and spend public money to provide essential goods and services to the community. To undertake this process, legal authority is required from Parliament.

### Legislative context for the collection and appropriation of public monies

The *Constitution Act 1975* (the Constitution), together with other legislation, establishes a framework for the collection of public money (revenue), the prudent management of finances, and the spending of public money (expenditure).

The Government collects revenue through taxes, fees for services, sales of assets, and other receipts (e.g. Commonwealth GST grants). The Constitution and the *Financial Management Act 1994* (FMA) prescribe that generally all such revenue must first go into the Consolidated Fund.<sup>4</sup>

Section 92 of the Constitution provides the power for Parliament to appropriate revenues from the Consolidated Fund. This revenue may be appropriated to specific purposes as directed by Parliament.

Parliament may only appropriate public money on the initiative of the Government. In particular, the Constitution:

- requires that any money Bill be preceded by a message from the Governor<sup>5</sup>;
- requires that an Annual Appropriation Bill must deal only with appropriation<sup>6</sup>; and
- permits expenditure to be incurred only on warrants from the Governor.

### The State Budget

In order to request Parliament to appropriate money from the Consolidated Fund for the upcoming financial year, the Government develops the annual State Budget, detailing how appropriation will be spent. The Budget has two components:

- **Appropriation Bills** – to use public money from the Consolidated Fund, the Government must pass an Appropriation Bill through Parliament. This Bill outlines the amount of public money appropriated to each Department for outputs, assets, payments on behalf of the State, and other appropriations specified in the Bill. A separate Appropriation Bill is also submitted for the Parliament itself.
- **Budget papers** – these are required by the FMA to detail the goods and services that are to be delivered with the appropriation. The Budget papers also describe the Government's fiscal strategy, the overall budget position of the State and the objectives of each Department's service delivery.

The Budget forms the basis of accountability for financial and performance management for each Department.

### The role of Cabinet and Cabinet committees in the Budget process

Cabinet is the principal decision making body of the Government. It consists of all Ministers of the Crown and the Cabinet Secretary. The Premier, as the leader of the Government, is the chairperson of Cabinet.

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<sup>4</sup> The Consolidated Fund may be viewed as a set of bank accounts owned and operated by Government. Together, the Consolidated Fund and the Trust Fund make up the Public Account.

<sup>5</sup> Refer Section 63 of the *Constitution Act 1975*.

<sup>6</sup> Refer Section 64 of the *Constitution Act 1975*.

Each Government will designate a committee responsible for making budget decisions on behalf of Cabinet. This committee is responsible for considering all output, revenue, asset investment and financing proposals submitted by Departments on behalf of Ministers for the development and delivery of the State Budget. This committee usually comprises the Premier, Treasurer, Minister for Finance, and potentially, a number of other Ministers.

The Department of Treasury and Finance (DTF) supports this committee in its budget deliberations by providing:

1. process management and secretariat support; and
2. information, advice and recommendations to support its decision-making, in conjunction with the Department of Premier and Cabinet.

Portfolio Ministers are responsible for recommending the initiatives they would like to be funded to this Cabinet committee. Once the committee finalises their decisions based on the submissions of portfolio Ministers and the Government's overall priorities and objectives, DTF proceeds with the preparation of the State Budget papers.

### **Tabling of the Budget**

Usually on the first Tuesday in May each year, the Treasurer introduces the Appropriation Bill to Parliament to appropriate public money, in addition to the annual State Budget papers. These documents provide a statement of Victoria's budget position, details how the Government will spend the public money it expects to collect over the next year, and requests approval from the Parliament to use public money for that year.

# The legislation supporting the State's resource management framework

While the Constitution provides broad powers for government to use public money, there are laws that specifically govern the use of that money and the accountability processes that government is obliged to satisfy.

The three principal pieces of legislation that underpin the State's resource management frameworks are the:

- Financial Management Act 1994 (FMA);
- Audit Act 1994; and
- Annual Appropriation Acts.

## **The *Financial Management Act 1994***

The FMA is a key piece of legislation underpinning the financial management framework in Victoria. It administers the use of public money and the accountability processes and secondary legislation that departments and public entities must comply with.

Its key elements:

- relate to the financial administration of money coming into the hands of the Government;
- prescribe the collection, management and expenditure of, and the subsequent accounting and reporting to the Parliament for money, public property and other property;
- establish and define the scope of the Public Account, including the Consolidated Fund and the Trust Fund; and
- include financial responsibility and budget management provisions.

Section 40 of the FMA relates to the Government's commitment to output management by providing that a separate statement must accompany the annual Appropriation Bills, detailing:

- the goods and services produced or provided by each Department;
- a description of the funds available to each Department during the period;
- the estimated receipts of the Department; and
- such other information as the Minister determines.

These requirements are met through the content of the annual Budget papers, in particular Budget Paper No. 3 (*Service Delivery*) and Budget Paper No.5 (*Statement of Finances*).

## **The *Audit Act 1994***

The Auditor-General is an independent officer of the Victorian Parliament, appointed under the *Constitution Act 1975* to conduct and report on financial and performance audits in the Victorian public sector.

The *Audit Act 1994* (the Act) governs the powers and functions of the Auditor-General. The Act establishes the legislative framework governing the ongoing role and functions of the Auditor-General. This Act identifies the statutory powers and responsibilities of the Auditor-General. It provides the authority for the Auditor-General to:

- conduct annual financial statement audits of public sector agencies;
- review and report on the estimated financial statements;
- undertake performance audits within the public sector which encompass assessments of the economy, efficiency and effectiveness of the management of public resources by the government or individual government agencies;
- examine the use of public grants received by both private and public sector organisations; and
- determine the efficiency, effectiveness and economy of the services or functions that are delivered through contracts with private or not-for-profit providers (associated entities) through 'follow-the-dollar' performance audits.

### The annual Appropriation Acts

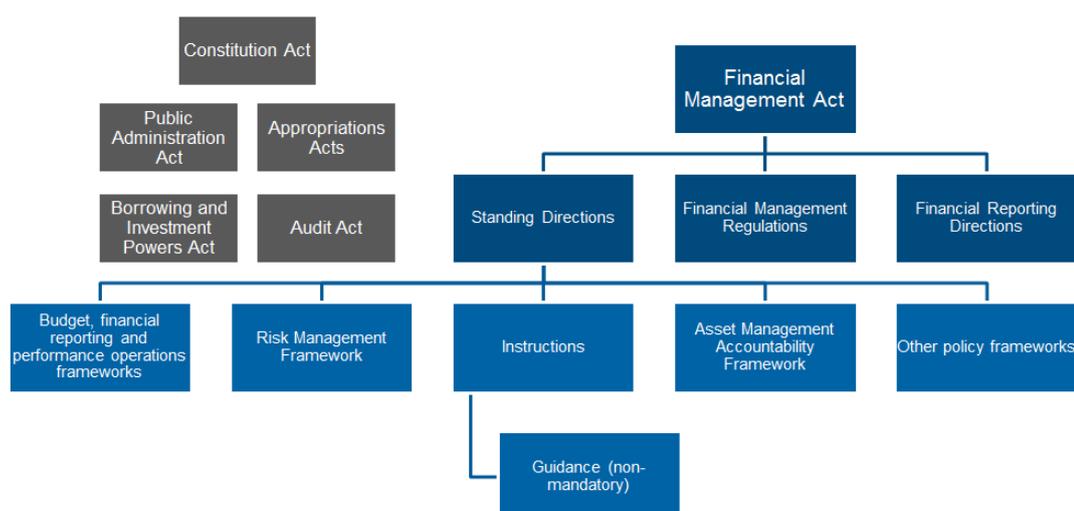
An appropriation is an authority given by the Parliament to draw certain sums out of the Consolidated Fund, now or at some future point in time, for the purposes stated, up to the limit of the amount in the particular Act. It authorises the Government to use money from the Consolidated Fund, but it also restricts the expenditure to the particular purpose specified by the appropriation.

The Appropriation Act is issued annually and:

- provides the Treasurer the authority to commit money from the Consolidated Fund, up to a specified amount; and
- sets out how much of that specified amount may be applied to each Department and the purpose(s) for which that funding is provided.

### Further legislation

The above legislation is also supported by the *Public Administration Act 2004* and the *Borrowing and Investment Powers Act 1987*. The diagram below depicts how the various legislation interact:



### **The *Public Administration Act 2004***

The *Public Administration Act 2004* (PAA) reflects the State Government's objective that the fundamental role of the public service is to serve the public interest. The PAA demonstrates the Government's commitment to:

- sustain an effective and impartial public service;
- protect public employment from politicisation by reaffirming and promoting the principles of merit and equity;
- promote the highest standards of public service conduct and integrity thereby strengthening public confidence and trust in government;
- drive further improvements in the integrated delivery of government services;
- promote career opportunities in the public sector by ensuring a more coherent approach to workforce management and professional development;
- ensure the public sector workforce is capable of delivering high quality services to the Victorian community, both now and into the future;
- promote standards of good governance in public entities; and
- clarify the accountability relationship of public entities to a responsible Minister who, in turn, is accountable to Parliament.

### ***Borrowing and Investment Powers Act 1987***

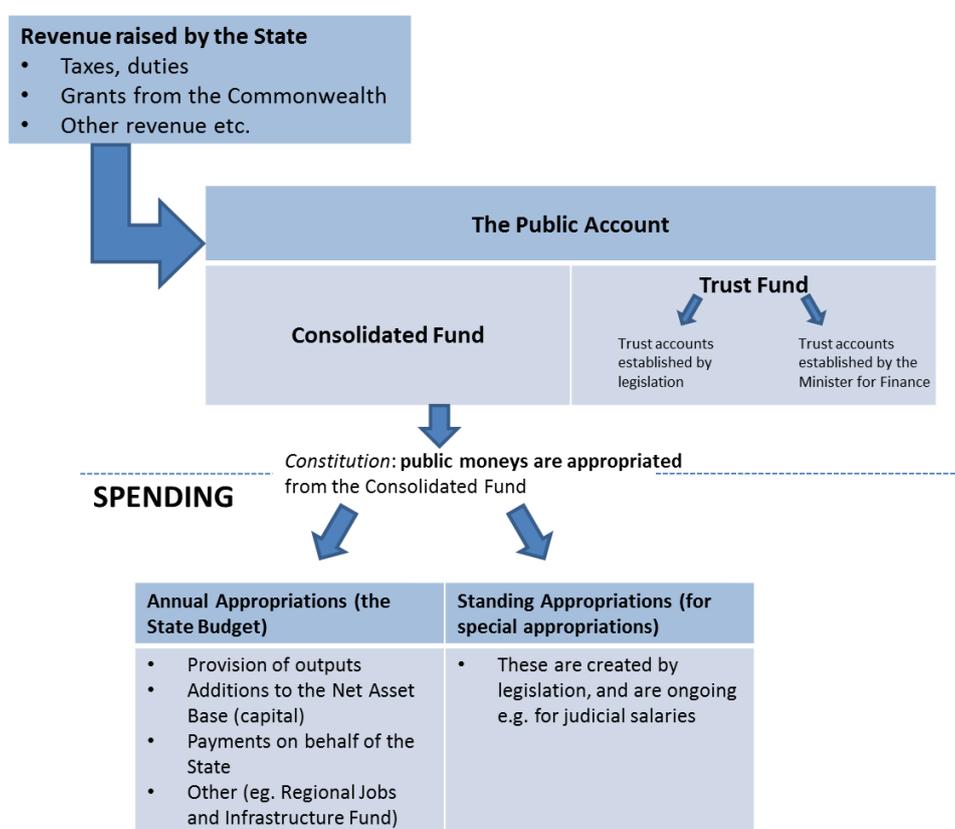
The purpose of the *Borrowings and Investment Powers Act 1987* is to provide statutory authorities with the power to borrow and invest in a wide range of financial products, and to access the financial arrangements required to effectively manage their debt and investment portfolios.

# The State's appropriation framework

## The framework at a glance

Financial management is concerned with the sourcing, distributing and management of public money, to ensure funds are used appropriately and efficiently. Effective financial management allows for the continued delivery of public goods and services.

The diagram below illustrates the State's appropriation framework. This framework ensures accountability and transparency, so it is clear how public money is being used. The *Constitution Act 1975* and the *Financial Management Act 1994* (FMA) provide clear rules for how money is managed and accounted for.



In legislation, and supporting the State's financial management framework, are the concepts of:

- the Public Account;
- Consolidated Fund (including warrants); and
- the Trust Fund.

These concepts are explained below.

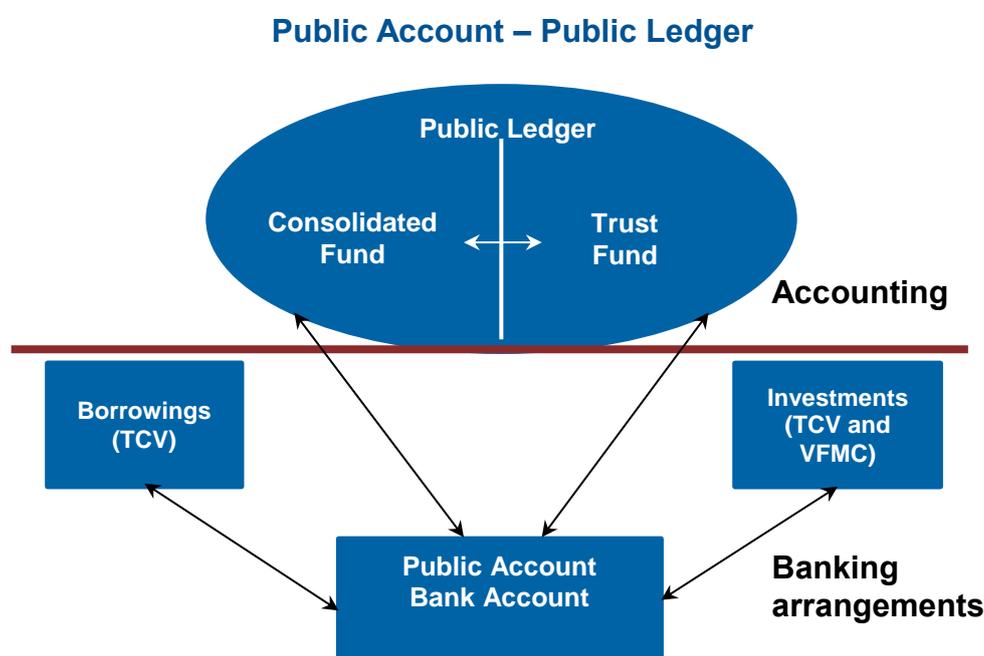
## The Public Account

The Public Account is the Government's official bank account. The Public Account holds the cash balances of the Consolidated Fund and the Trust Fund. The State's financial transactions are primarily conducted through the Public Account.<sup>7</sup>

**Accounting arrangements** – comprise a centrally managed account which is linked to Departmental bank accounts (generally via the mechanism known as the State Administration Unit (SAU) – refer to Section 5.1 for more information).

**Banking arrangements** – are determined by the State's cash and banking arrangements, and is the net of its investments and borrowings held by the Treasury Corporation Victoria and the Victorian Funds Management Corporation.

These representations of the Public Account are illustrated below:



## The Consolidated Fund

The Consolidated Fund is the Government's primary financial account in the Public Account. Under the Constitution, the Consolidated Fund receives all consolidated revenue from which payments, appropriated by Parliament are made.

### Issuing monies from the Consolidated Fund

Parliament appropriates money on a Departmental basis annually from the Consolidated Fund for the following purposes:

- to produce or procure goods and services (output provision);
- to produce/buy capital items (asset investment);
- to make payments on behalf of the State; and
- as specified by other legislation.

<sup>7</sup> There are also funds known as the non-public account. These are generally bank accounts that sit with statutory and other agencies, and these are operated independently outside the Public Account.

## Warrants

The Appropriation Acts provide Government with a record of what it is legally entitled to draw down from the Consolidated Fund during a given year. Warrants are the legal instrument required to draw down the **actual** funds from the Consolidated Fund.<sup>8</sup>

Each year's Appropriation Act therefore requires a warrant to be prepared and authorised before funds can legally be drawn down from Consolidated Fund.

If the original warrant is insufficient, a new warrant is required to draw down on any additional monies appropriated from the Consolidated Fund in any given year. This requirement is applicable in some instances where supplementation to budgets is sought by Departments – for example under sections 10 or 33 of the FMA.

Chapter 1 provides further guidance on when a warrant is required to be prepared. DTF prepares each warrant, which are signed by the Treasurer, counter-signed by the Auditor-General and then approved by the Governor. Until this occurs, no funds may legally be drawn down from Consolidated Fund.

## The Trust Fund

In the Public Account, the Trust Fund encompasses a number of accounts for funds that are not subject to parliamentary appropriation, such as:

- accounts created by legislation for specific purposes;
- accounts to record specific purpose payments from the Commonwealth for on-passing by the State to third parties; and
- accounts facilitating the receipt and disbursement of private funds held by the State in trust.

Trust accounts are operated by Departments. Unlike the Consolidated Fund, no appropriation or warrant is required to authorise spending from a trust account.

More information on how to set up, manage and close trust accounts is provided in Section 1.2.

## Appropriations

### Annual Appropriations

Departmental annual appropriations are made on an accrual and global basis for each Department. From this global allocation of funds Departments are responsible for, and manage their own budgeting and expenditure, including budgeting for their portfolio agencies.

Global appropriations provide Departments flexibility to adjust to pressures and to respond to changed circumstances within the spending limit provided. However, significant changes to output delivery<sup>9</sup> and/or new policy decisions require approval from the Government.

These Departmental appropriations, and similar appropriations for the Parliament, are set out in Schedule 1, Part 1, of the respective Appropriation Acts that are issued each financial year.

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<sup>8</sup> Under section 93 of the *Constitution Act 1975* and section 17 of the FMA.

<sup>9</sup> Note that the Performance Management Framework (Requirement 5.1) allows the relevant portfolio Minister to approve changes of up to 5 per cent between outputs. Changes greater than 5 per cent, or the establishment of new outputs, require approval from the Minister for Finance.

## Treasurer's Advance

As part of the annual Appropriation Act, a Treasurer's Advance (TA) is appropriated to be applied at the Treasurer's discretion to meet any urgent or unforeseen claims. A schedule of items of expenditure is submitted for Parliamentary authority in a subsequent year's Appropriation Bill. Refer to Section 1.3 for more information on TA.

## Section 29 *Financial Management Act 1994* - Annotated Revenue

The Appropriation Act also provides for the application of section 29 of the FMA, whereby Departments on behalf of their relevant Minister may apply to the Treasurer to retain certain types of revenue/receipts from third parties. This is covered in more detail in Section 1.1.

## Special Appropriations<sup>10</sup>

A special appropriation is a provision within an Act that provides authority to spend money for particular purposes, for example, to fund a particular project or function.

Examples of special appropriation in the FMA are section 28 (borrowing against future appropriation) and section 33 (access to previously appropriated amounts).

Special appropriations are separate from global annual appropriations and are created under specific legislation.<sup>11</sup> They are often ongoing in nature, until such time as the legislation is modified or repealed. Special appropriations can also include one-off appropriations for specific amounts or amounts with sunset clauses (clauses that have a fixed life).

A number of factors may be taken into account in determining whether an annual or special appropriation may be used in particular circumstances. Generally, a special appropriation may be used when:

- it is important to demonstrate the independence of an entity from parliament and the executive by providing for automatic payment of the remuneration of its officeholders (for example, the salaries of judges and the Auditor-General are included in the *Constitution Act 1975*);
- it is desirable to create a legal entitlement which is to be provided in all instances that satisfy specific criteria;
- it is considered necessary to demonstrate the State's ability to meet its financial obligations independently of parliamentary approval of funds (for example, the repayment of loans); or
- other unique circumstances exist that would be difficult to accommodate in annual Appropriation Bills.

The Public Account disclosure in the Budget papers provides a list of estimated special appropriation expenditure for the year. Note that increases in special appropriation expenditure beyond these estimates do not require Government approval. However, additional warrant will be required.

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<sup>10</sup> Sometimes referred to as 'standing appropriations'.

<sup>11</sup> For example, judicial salaries have a special appropriation to ensure their salaries are not at the discretion of the Government, maintaining the separation of powers.

## Other funding sources

A Department's revenue base may also consist of funds received and held outside the Public Account (such as third-party revenue held in separate bank accounts by schools). In addition, other general government sector portfolio agencies are created on a 'stand-alone' basis such that they are able to generate and retain certain additional revenues without the requirement to pay it to the Consolidated Fund. However, these agencies are generally reliant on appropriated funds transferred from their department to deliver the Government's outputs or services (such as hospitals, TAFEs and certain transport-related entities).

Government-owned businesses which generate their own operating revenue (such as water authorities) are subject to a different set of governance oversight and are outside the scope of this Budget Operations Framework.

## General framework concepts

### The concept of appropriation limits

'Appropriation limits' are the maximum amounts able to be legally drawn from the Consolidated Fund for any given item of appropriation. These limits are set by the appropriation amount included in the Appropriation Act.

However, Departments should note that:

- appropriations do not of themselves limit the operating expenses incurred by Departments;
- expenses incurred by Departments will give rise to liabilities and obligations which Departments are legally bound to meet as payments fall due, regardless of whether they have access to sufficient appropriations to meet these obligations; and
- once appropriation limits have been reached, the Government is legally unable to commit additional funding to meet payments related to a Department's expenses.

### Accountability mechanisms

A Department's Minister(s) and Secretary are accountable to the Cabinet and Parliament for ensuring that the Department's resources are sufficient to enable it to meet all payments as and when they fall due.

Therefore, Departments retain responsibility for monitoring the extent of application of appropriations, even though this is determined by the Minister for Finance's certification, and the Treasurer's application of revenue (refer to the *Performance Management Framework* for further guidance).

# 1. Mechanisms available to manage departmental funding levels

This section outlines the mechanisms available to Departments to manage their funds under existing legislative arrangements, and in accordance with the principles of the *Performance Management Framework*. Possible arrangements include:

- (a) The retention of fees and charges revenue from the delivery of outputs, Commonwealth grants for specific purposes, and receipts from the disposal of surplus assets under section 29 of the *Financial Management Act 1994* (FMA) arrangement (refer to Section 1.1 for more information); and
- (b) A trust account arrangement – circumstances when a trust account arrangement may be suitable are outlined in Section 1.2.

## Supplementary funding from within existing funding arrangements

The annual budget is the primary planning mechanism for determining the level and priorities for government spending. The budget process allows the Government to assess all competing proposals and make informed decisions about the allocation of the limited funding available.

Under the *Performance Management Framework*, Government agrees to pay a Department a fixed price for the delivery of outputs at predefined levels of quantity, quality and timeliness (performance targets). Government will generally not increase the price it pays for outputs for the coming budget year once the budget has been set. Departments are expected to manage the expenses associated with the delivery of the agreed outputs within this annual funding envelope.

However, Government may agree to provide budget supplementation to Departments outside of the normal budget process, under the following conditions:

- Outputs - Government will consider increasing the funding provided to Departments in exceptional circumstances, such as where Government agrees (between budgets) to a change in the quantity, quality and timeliness characteristics of an output;
- Assets - where Government requires a Department to undertake additional asset investment; or
- Payments on Behalf of State (POBOS) - where Government approves variations to POBOS, with the form of compensation determined and approved by the Treasurer.

Under the *Performance Management Framework*, the final amounts earned by and paid to Departments are certified by the Minister for Finance and applied by the Treasurer at the end of the financial year. They are determined using evidence submitted by the Department on the progress of their output and capital programs.

## Sources of supplementary funding

The source of the additional funding, if approved, will be determined by the Treasurer taking into account the requirement to manage the overall parliamentary appropriation authority available to the Government. Some of these funding sources will require the preparation of additional warrant.

Possible sources of funding may include (with references within the Budget Operations Framework (BOF)):

- (a) supplementation through a Treasurer's Advance under the Appropriation Act. An additional warrant is **not** required (refer to Section 1.3 of the BOF);
- (b) supplementation through a Temporary Advance under section 35 of the FMA. A warrant is **not** required (refer to Section 1.4);
- (c) borrowing against future appropriation under section 28 of the FMA (this is a Special Appropriation provision). A warrant is required for this request (refer Section 1.5);
- (d) carryovers of unused prior years appropriations under section 32 of the FMA. A warrant is **not** required (refer to Section 1.7);
- (e) access to balances in a Department's State Administration Unit (SAU) inter-entity account (which may comprise accumulated surpluses, or appropriation provided in prior years for specific accrued liabilities such as long service leave or accumulated depreciation equivalent). All of the prior years' SAU balances are accessible under section 33 of the FMA and a warrant is required. This is a Special Appropriation provision (refer Section 1.8);
- (f) access to a Public Account advance under section 37 of the FMA. A warrant is **not** required for this request as it is not a drawdown from Consolidated Fund (refer to Section 1.9); and
- (g) payments of awards for salaries and related costs under section 3(2) of the annual Appropriation Act. A warrant is required for this request.

Each of these mechanisms require the approval of the Treasurer or relevant Cabinet committee. Departments should not assume an application to access one of these funding sources will guarantee receipt of that source of funding.

The conditions and processes for applying for most of these sources of supplementary funding are detailed in Sections 1.3 to 1.9.

## Other mechanisms for varying funding

**Transfer of appropriation within a department** - Departments may also request transfers to or from other appropriation items (purposes) for that Department, with the approval of the Treasurer under section 30 of the FMA. Refer to Section 1.6 for more information.

**Machinery of government changes** – The Government may choose to transfer administrative responsibilities and appropriation authority between Departments, under administrative arrangements ordered by the Governor in Council under the *Administrative Arrangements Act 1983*. Refer to the *Victorian public sector operating manual on machinery of government changes* issued October 2016 for more information.

## 1.1 Appropriation of certain revenue and asset proceeds – section 29 of the FMA

### Mandatory requirements SECTION 29 FMA - APPROPRIATION OF CERTAIN REVENUE AND ASSET PROCEEDS

#### 1.1.1 Commonwealth grants provided for specific purposes

- (a) Payments from the Commonwealth for specific purposes may be accessed through a section 29 agreement, or by utilising section 10 of the FMA. Departments should speak to their DTF contact to discuss these options before submitting a request.
- (b) For Commonwealth expenditure accessed via a section 29 agreement, if access to those funds is required beyond a financial year, the balance may be made available in the following year (subject to a Department meeting the section 32 FMA carryover requirements).
- (c) The carrying over of a section 32 carryover (i.e. into a second year) is not permitted under the FMA. Departments must only recognise/claim what they have drawn down and spent to this point in time. However, Departments may apply for access to the remaining funds by submitting a request to the Treasurer or as part of a Budget bid for the relevant Cabinet committee to consider.
- (d) An application for a special appropriation to access Commonwealth funds under section 10 of the FMA is appropriate if one or more of the following conditions apply:
  - (i) it is a new Commonwealth agreement established during the year; or
  - (ii) if it is likely that funds will be required to be accessed beyond the next financial year.
- (e) Departments must ensure that funds from the Commonwealth have been deposited with DTF before accessing the appropriation.
- (f) If the output or asset investment is delivered by the State for less than the funds provided by the Commonwealth, the excess funds may only be applied to finance activities that are outlined in each Commonwealth agreement. Departments are to liaise with the Commonwealth on the application of any excess funds.

#### 1.1.2 User charges

- (a) A Department wishing to establish a section 29 agreement for user charges (fee for service) must lodge a request with DTF.
- (b) Eligible user charge estimates must be agreed with DTF on an unchanged policy basis, i.e. each agreement shall be based on the expected level of receipts from the implementation of existing policies at current prices (for guidance on setting prices, refer to the *Cost Recovery Guidelines*).
- (c) Unless the service is new and unfunded, the agreed estimate will be deducted from the gross appropriation to arrive at a net appropriation to which section 29 applies.

## Mandatory requirements

### SECTION 29 FMA - APPROPRIATION OF CERTAIN REVENUE AND ASSET PROCEEDS

#### 1.1.3 Asset sales

- (a) A Department wishing to retain the proceeds earned from disposal of an asset or class of assets must lodge a business case with DTF regarding the disposal, and request the relevant Cabinet committee or Treasurer's approval for annotation of the proceeds to their Additions to the Net Asset Base (ATNAB) appropriation.
- (b) The impact on the balance sheet from the asset disposal and revenue retention must be discussed with a relevant DTF officer (before finalisation of the business case).
- (c) Departments must consider the *Victorian Government Land Sales Financial Framework* regarding the retention of receipts from land sales.

## Guidance

Under normal circumstances, money received by the State for any purpose must be credited to the Consolidated Fund (under section 9 of the FMA).<sup>12</sup>

However, section 29 of the FMA provides the legislative authority, in conjunction with the Appropriation Act, for amounts received relating to certain receipts / revenue to be credited or annotated to a departmental appropriation item. Section 29 'deems' these amounts to be appropriated for the purposes of those items.

Access to these amounts are subject to a section 29 agreement between the relevant Minister making the request, and the Treasurer.

The types of revenue (receipts) that may be considered in a section 29 agreement are:

- Commonwealth specific purpose grant revenue;
- specific purpose revenue from Municipal Councils;
- revenue from outputs (relating to user charges but excluding regulatory fees); and
- *receipts* from asset sales.

### Establishment of section 29 agreements

The following steps should be followed in developing section 29 agreements:

- Departments are to advise DTF in writing of the amount and nature of the revenue they wish to be annotated to the Department's appropriation, and complete a schedule listing each revenue item for inclusion in the agreement to support the request. This schedule comprises three columns:
  1. the previous year's **Revised Revenue Estimate** amount – this is the outturn estimate, or total actual revenue (if known) for the revenue item;
  2. the **Agreed Revenue Base** amount – this is the amount (agreed between the relevant Minister and the Treasurer) that would be reinstated to a Department's base appropriation if the section 29 arrangement was terminated at a later date (i.e. the 'unchanged policy base' amount); and

<sup>12</sup> Unless by or under an Act it may be paid into another fund (such as an account in the Trust Fund, or an account operated by a statutory authority).

3. the **Agreed Revenue Estimate** amount – this is the total amount estimated to be received under the agreement in the given financial year. This amount should be reviewed and agreed each year as part of each section 29 agreement.
- The relevant Minister then submits a formal request to the Treasurer seeking his agreement.
  - The Treasurer may then choose to approve (or not approve) each revenue item proposed for inclusion in a section 29 agreement.

Other things to note about section 29 agreements:

- such agreements only apply to Departments;
- the agreements increase a Department's annual appropriation by the *actual revenue recognised* (or in the case of asset sales – the *actual receipt of the cash*) rather than the estimated amount noted in an agreement;
- for user charges, any increases in revenue that are the result of the application of competitive neutrality principles may be retained by the Department (i.e. on an unchanged policy basis); and
- the appropriation item must specify 'section 29 of the **Financial Management Act 1994** applies' in the Appropriation Act for a given year, otherwise an agreement cannot apply.

All section 29 agreements must be renewed on an annual basis.

**Regarding user charges** - When a section 29 agreement for user charges is reached as part of the Budget process, the appropriation for the particular item in the Appropriation Act is reduced by the amount estimated to be received from the source of revenue identified in the section 29 agreement.

### Where estimated revenue is exceeded

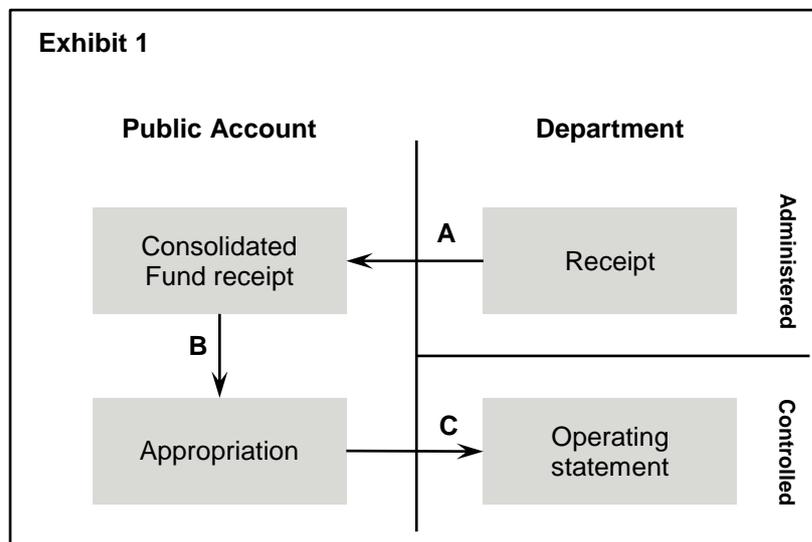
As a general rule, if a Department exceeds the agreed revenue estimate, the appropriation is increased to the value of the additional revenue and is available to the Department. This revenue may be used for any purpose consistent with the appropriation item and the Department's agreed objectives and/or asset investment program.

However, there are different types of revenue arrangements under section 29 of the FMA:

- **Commonwealth specific purpose grant revenue, and specific purpose revenue from Municipal Councils** - Departments should not claim revenue under a section 29 arrangement if those funds are not needed in the year to meet costs incurred. If access to excess revenue from these sources of funds is required in the following financial year, Departments may apply for carryover of these funds subject to the approval of the Treasurer (refer Section 1.7 of the BOF).
- **Revenue from outputs (relating to user charges)** – in some cases, Departments could exceed the revenue estimate for user charges but will not have spent the additional revenue by the end of the year. For example, if there is an over-collection of user charges relative to the expenditure incurred, this may result in a surplus which will accrue in a Department's SAU inter-entity account. Departments may then apply for access to these surpluses in a subsequent year subject to the approval of the Treasurer (refer Section 1.8 of the BOF).
- **Receipts from asset sales** – Departments may only draw down on the actual cash received from an asset sale and only to the extent required in the current year to fund cash outflows for approved investments. Any unspent receipts at year end are then subject to section 32 carryover.

## Accounting for section 29 revenue

The accounting treatment for the recognition of section 29 revenue flows are documented in the diagram below:



**Step A:** All cash received by a Department is recognised as administered and is required under section 9 of the FMA to be paid into the Consolidated Fund. Normal accounting standards are applicable in relation to revenue recognition by the State.

**Step B:** If the revenue relates to user charges, Commonwealth grants, and/or sales of non-current physical assets, and a section 29 agreement is in place, the relevant appropriation item is increased accordingly.

**Step C:** The Treasurer may apply the appropriation. The Department then recognises the revenue as controlled.<sup>13</sup>

## Additional information on specific Section 29 revenue classes

### Specific purpose payments from the Commonwealth (Mandatory requirement 1.1.1)

#### Eligibility

The Commonwealth Government provides grants to the States for specific purposes under section 96 of the Commonwealth Constitution.

Section 29 agreements for Commonwealth grants received for specific purposes are arranged at the start of each financial year, or upon the receipt of the grants from the Commonwealth.

<sup>13</sup> It should also be noted that for section 29 to be applicable, there must be a provision included against the relevant item in Schedule 1 of the annual Appropriation Act. If such a provision is not included in the Appropriation Act then section 29 cannot be applied in the financial year covered by the Appropriation Act.

There are currently two types of tied Commonwealth grants for specific purposes: Specific Purpose Payments (SPPs) and National Partnership Payments (NPs).<sup>14</sup> These grants are received into the Consolidated Fund first (with the exception of Health Reform grants) and then appropriated.

Commonwealth grants that do **not** qualify for a section 29 agreement include:

- grants provided for on-passing paid directly into a trust account, including the *National Health Reform Agreement*, which is subject to a separate process; and
- general purpose grants paid into the Consolidated Fund.<sup>15</sup>

Not all specific purpose payments are for State budget programs. A substantial proportion of these are for on-passing to other parties such as non-government schools and local government authorities. In such cases the State simply acts as a vehicle for distributing the Commonwealth funds via a trust account in the Trust Fund. In addition, a number of other relatively small Commonwealth grants are paid direct to specific trust accounts in the Trust Fund and similarly are not subject to appropriation.

### Application

Commonwealth grants received for specific purposes (SPPs or NPs) that are paid to the Consolidated Fund are to be included in section 29 agreements. Commonwealth grants that are paid directly into a trust account are excluded from such arrangements.

### User charges (Mandatory requirement 1.1.2)

#### Eligibility

A section 29 arrangement for user charges may be established to provide departments with access to revenue they generate from the sales of goods and services (outputs).

Section 29 agreements for user charges are not mandatory. Such arrangements are only established by agreement on an annual basis between the relevant Minister and the Treasurer.

User charges need to be carefully distinguished from other forms of revenue such as regulatory fees (also classified in accounting terms as user charges), fines, dividends, interest and taxes as these are not eligible for retention. Care needs to be taken in making this distinction, as in some cases there is a fine line between regulatory fees and other user charges.

The following criteria should be used in determining whether a revenue item is a valid *user charge*:

- the revenue should stem from payments made voluntarily for goods and services provided; and
- the payments made and the benefits gained by the user can be clearly linked to the provision of the products and services.

*Regulatory fees* on the other hand are characterised by one or more of the following:

- they are compulsory and serve primarily as an instrument of government policy;
- they generally reflect the granting of a privilege or right to undertake a regulated activity.

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<sup>14</sup> Refer to [https://www.coag.gov.au/the\\_federal\\_financial\\_relations\\_framework](https://www.coag.gov.au/the_federal_financial_relations_framework) for more details.

<sup>15</sup> These are GST grants, GST transitional grants and national competition policy payments

## Application

Section 29 agreements are based on the principle of applying current prices.

The 'Current price' of the base amount does not automatically mean existing prices are indexed by the forecast Consumer Price Index (CPI). Depending on the nature of the service, this may need to be determined on a case-by-case basis.

Departments should also refer to DTF's *Cost Recovery Guidelines* for more information.

## Goods and Services Tax

Under the provisions of the *Commonwealth A New Tax System (Goods and Services Tax) Act 1999*, fees and charges paid to a government department are deemed to be subject to the Goods and Services Tax (GST).

Departments should refer to Division 81 to identify any Victorian Government fees and charges that are excluded from GST.

Given that Victorian public sector Departments and agencies are registered separately for GST purposes, they should regularly review the fees and charges, as they will individually be responsible for the management and remittance of GST to the Australian Tax Office.

Note that when preparing a section 29 agreement, the revenue items that comprise the agreement will be **exclusive** of GST.

## Receipts from asset sales (Mandatory requirement 1.1.3)

### Eligibility

The cash proceeds from the sale of Departmental controlled (not administered) physical assets may be accessed through a section 29 agreement.

The Treasurer must agree to:

- the proposed sale of the particular asset or class of assets; and
- the amount derived from the sale to be annotated to the Department's ATNAB appropriation if only a portion of the proceeds are to be annotated.

A Department wishing to use a section 29 agreement for asset sales, should include any proposal to dispose of assets or class of assets in their Budget funding business cases for new asset investment.

Departments are encouraged to think broadly about possible opportunities for asset disposal as part of any asset initiative development.

Departments should also refer to the *Victorian Government Land Sales Financial Framework* when considering land sales opportunities.

### Application

Timing issues associated with accessing the proceeds of sale will be unique to each situation. Where the proceeds of sales are to be applied to asset replacement there may be a need to arrange an advance of funds to cover the period before sale proceeds become available.

Other issues may include:

- the change of accounting treatment regarding the asset (e.g. a non-current physical asset may have a different value when converted to asset held for resale);
- the estimate of anticipated proceeds;
- the impact of actual proceeds being different to the estimate;
- responsibility for the costs associated with the disposal; and
- interest by other agencies in acquiring the asset in question.

Discussions will be held with each Department on the configuration of balance sheets in the context of budget formulation. At this time, the options for asset disposal and the opportunity for the retention of proceeds will be discussed and tested.

Departments should also refer to the *Victorian Government Land Sales Financial Framework* for specific policies regarding the retention of receipts from land sales.

## 1.2 The Trust Fund and trust accounts

### Mandatory requirements THE TRUST FUND AND TRUST ACCOUNTS

#### 1.2.1 Creation of a trust account

- (a) If a trust is being created as a result of legislation, a Department must inform DTF about its impending creation and advise DTF once it is established to process the requirements to administer and report on the trust.
- (b) If a trust is proposed to be set up using the Minister for Finance's powers under the FMA, the relevant Minister should submit a letter of request to the Minister for Finance, who will then consider the trust being proposed.

#### 1.2.2 Review of trust accounts

- (a) A Department must maintain and periodically review its trust accounts to determine if there is a continued need for the trust account and that the appropriate amounts are in it.

#### 1.2.3 Specific requirements relating to the Treasury Trust Fund

- (a) New arrangements must not be set up in the Treasury Trust Fund unless it is for its original purpose (i.e. the recording and accounting for unclaimed and unidentified moneys held by Departments).<sup>16</sup>
- (b) Departments must undertake a regular review of their activity in the Treasury Trust Fund to ensure that inappropriate balances do not build up in the Treasury Trust Fund.
- (c) Moneys left unclaimed in the Treasury Trust Fund after a period of seven years must be transferred by the Department to the Consolidated Fund.
- (d) In certain circumstances, monies appropriated for one Department may be transferred to and held in the Treasury Trust Fund by a second Department in order to deliver services on behalf of that originating Department. Any excess monies held as at 30 June each year must be remitted back to the originating department on that date and repaid to the Consolidated Fund.

#### 1.2.4 Closure of trust accounts

- (a) A Department must close a trust account when the purpose for which it was created no longer exists.
- (b) Money standing to the credit of a trust account that is closed, must, on direction of the Minister for Finance, be credited to another trust account, or to the Consolidated Fund.

## Guidance

### The Trust Fund and trust accounts

The Trust Fund forms part of the State's Public Account as a separate and discrete component. Part 4 of the FMA (sections 19 to 23) covers legislation regarding the Trust Fund.

<sup>16</sup> DTF is currently undertaking work to facilitate trust account arrangements that will allow a Department to transfer funding to another Department. DTF will advise when this arrangement is in place.

Trust accounts in the Trust Fund may be established by:

- (a) an Act of Parliament, under legislation for a specific purpose<sup>17</sup>, or
- (b) the Minister for Finance, under section 19(1) of the FMA (defining the purpose for which they are established), following a request from a Department.

A trust account established by a statute will be restricted to the purposes set out in that statute.

Trust accounts are usually established for the use of a single Department, although in some instances a trust account may be accessed by more than one Department, or may be generic in nature.

The Trust Fund comprises the following types of accounts:

- **State Government trust accounts** established to record the receipt of certain State funds and their disbursement for specified purposes. These include trust accounts established to record the receipt and disbursement of State revenues which are hypothecated (through special appropriations) to particular purposes, e.g. gaming revenue is hypothecated for the provision of health services;
- **Commonwealth and joint Commonwealth and State accounts** established to record the receipt and disbursement of specific purpose payments from the Commonwealth Government which are on-passed by the State to other organisations (such as non-government schools and local government). These accounts are generally established to comply with Commonwealth legislation or specific agreements with the Commonwealth;
- **Specific purpose operating accounts** established to essentially quarantine commercial activities in Departments from the rest of the Department's business. They incorporate:
  - (a) specific purpose trust accounts established under Section 19 of the FMA;
  - (b) working accounts established pursuant to Section 23 of the FMA; and
  - (c) trust accounts established under specific legislation;
- **Treasury Trust Fund, agency and deposits accounts** – Some of the larger accounts in this category are the Victorian Government Solicitor's Trust Account, Estate Agents Guarantee Trust Account, Conservation Agency Trust Account, Finance Agency Trust Account, and Public Works Agency Trust Account. Revenue in Treasury Trust Fund includes unidentified money and un-presented cheques;
- **Suspense accounts** established for accounting purposes;
- **Working accounts** established for departmental commercial and service units; and
- Accounts established to facilitate the receipt and disbursement of private funds held by the State in trust. These moneys may include bequests, donations, prizes, scholarships and research grants. This is generally in the form of a true trust, which can be either administered or controlled by the State and mostly involves management of money provided by a member or members of the public for a specific purpose.

The specific purpose for the establishment of each trust account is either defined by the Minister for Finance (pursuant to section 19 of the FMA) or is contained in a separate statute.

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<sup>17</sup> For example, the *Conservation, Forests and Lands Act 1987* provides for the Conservation, Forests and Lands Stores Suspense Account (Section 22(1)); and the Conservation, Forests and Lands Plant and Machinery Fund (Section 23(1)).

## Criteria to consider when requesting the creation of a trust account

A Department should consider the following criteria when requesting the creation of a new trust account:

### Criteria 1 – Purpose of the proposed trust account

- What is the purpose of the intended trust (it must be clearly explained)?
- Could an existing trust account be used for the required purpose?
- Given the flexibility of the appropriations framework, would a section 29 arrangement suffice?

### Criteria 2 – A need to quarantine/set aside the money from the rest of the Department's operations

- Are the moneys being held in trust for a third party? Is it likely to be a long-term arrangement?
- Is there legislation that prescribes such an arrangement be set up (e.g. pursuant to a Commonwealth Act)?
- Are there other agreements or arrangements in place that require the need to have such moneys separated in the Public Account?
- Are existing financial management systems unable to be used to separate the third party transactions from core Departmental business to negate the requirement for a separate trust account?

Departments should also consult with DTF at the earliest opportunity to determine the appropriateness of any proposed trust account arrangement.

### Investment of money in trust accounts

Section 21 of the FMA provides that the Minister for Finance may invest money standing to the credit of a trust account. The making of such investments is dependent upon whether a business case exists for interest on credit balances to be retained in the Trust Fund. However, the Minister's discretion does not apply where the crediting of interest is provided for in specific legislation.

### Management of moneys in trust accounts

Trust accounts must not be overdrawn at any time. Commitments to expenditure may only be made from a trust account where there is sufficient cash available in the trust account to cover the expected payments.

If a payment is required to be made which would result in a trust account becoming overdrawn, an advance or other legally available source of funds should be sought as soon as practicable prior to the payment being made so that an overdrawn situation does not result. If there are financial investments in the trust fund, these are only considered to be available to pay expenditure if fully liquid (e.g. at-call investments). Note that it is not appropriate to incur an interest expense on funds obtained to cover any shortfalls in a trust account without the Treasurer's agreement.

### **Accounting for trust accounts**

Each specific trust account is identified by a unique trust authority (i.e. the third segment of the Whole of Government chart of accounts) and contains ledger accounts which can potentially record revenue, expenses, investments, assets and liabilities (i.e. the full range of natural accounts) for certain Departmental activities.

### **Renaming of trust accounts / Change in purpose of trust accounts**

Trust accounts may be renamed to better reflect their purpose. The approval of the Minister for Finance is not required for this to occur, although DTF should be notified of the details of the intended change. However, ministerial approval is required should the purpose of a Trust Fund change, unless that changed purpose has been legislated.

### **Process for the closure of a trust account**

The FMA allows the Minister for Finance to make a direction to close a trust account where appropriate. However, a trust account established by statute may be closed by further legislation, or by the means, if any, specified in the statute.

### **Reporting on trust accounts**

For reporting purposes trust accounts fall into two categories:

- **Controlled trust accounts:** where the responsible Department can make decisions about how the funds are used; and
- **Administered trust accounts:** for which decisions about how the funds in the accounts are used are made outside the Department. The Department's responsibility for these trust accounts is limited to processing the trust account's receipts and payments.

The assessment of whether a trust account is deemed to be controlled or administered is entirely the responsibility of the Department concerned. As such decisions will be subject to audit review, they should consult with their relevant director at the Victorian Auditor General's Office in the determination of the appropriate classification.

The financial transactions and balances of accounts in the Trust Fund are reported in the financial reports of the administering departments.

A high level summary of these transactions and balances is also included in the State's Annual Financial Report. Departments are required to report on both categories of trust accounts in their audited financial statements.

## Specific trust accounts – further details

### Departmental working accounts

Departmental working accounts in the Trust Fund provide a means of giving Departments direct access to user charge receipts for those activities conducted on a commercial basis separately from core Departmental activities. The legislation governing the establishment and operation of Departmental working accounts is set out in section 23 of the FMA.

The main requirements for a Departmental working account are that:

- the activity is undertaken by a discrete business unit, operating to a business plan and producing its own set of accounts;
- the charges applying to the activity comply with the *Competitive Neutral Pricing Policy*; and
- provision is made for a dividend on any profit component, to be repaid to the Consolidated Fund.

### The Treasury Trust Fund

The Treasury Trust Fund was originally established under the *Audit Act 1958* to facilitate the recording and accounting for unclaimed and unidentified moneys held by Departments.<sup>18</sup>

However over time, the interpretation of the possible uses of the Treasury Trust Fund appear to have exceeded the original intended purpose of the account. The Auditor-General in particular has made comments in published reports about the use of the Treasury Trust Fund.

Therefore, the use of the Treasury Trust Fund is being strictly monitored by DTF.<sup>19</sup> Specific requirements relating to the Treasury Trust Fund are detailed in the Mandatory requirements of this section.

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<sup>18</sup> With the repeal of the Act in 1994, the FMA includes provision for the continuation of all existing trust funds and, now provides the legislative authority for the continuing operation of the Treasury Trust Fund consistent with its original purpose.

<sup>19</sup> Departments at times are required to provide funding to other departments in the delivery of Government objectives. DTF is currently working on the establishment of a dedicated trust to facilitate this.

## 1.3 Treasurer's Advance for urgent and unforeseen claims

### Mandatory requirements TREASURER'S ADVANCE (TA)

#### 1.3.1 Process and requirements for Treasurer's Advance requests

- (a) A Department must discuss all Treasurer's Advance funding requests with DTF, including advising of the quantum of the funding sought, prior to any correspondence being prepared in relation to the request.
- (b) In preparing a letter from a Minister to the Treasurer seeking a Treasurer's Advance, a Department must ensure that the letter includes:
  - (i) the reasons for the funding request, including whether the request is urgent and unforeseen;
  - (ii) the quantum of the funding sought;
  - (iii) confirmation that there are no other sources available to fund the request;
  - (iv) how the funding request aligns with Government objectives;
  - (v) any proposed adjustments to output and financial performance targets arising from the request; and
  - (vi) any funding variations previously approved by the Treasurer or the relevant Cabinet committee for the program or output seeking an advance.

#### 1.3.2 Reporting on Treasurer's Advance expenditure

All expenses and obligations to which any Treasurer's Advance is applied must be reported in the financial year in respect of which the advance(s) was made.

#### 1.3.3 Restrictions on Treasurer's Advance

Any unapplied component of a Treasurer's Advance in a given year lapses at the end of the year. Departments are not permitted to carry over a Treasurer's Advance to the following year.

## Guidance

### Definition

The Treasurer's Advance (TA) represents a specific appropriation made available to the Treasurer each year as part of the annual Appropriation Act, to meet any '... urgent claims that may arise before Parliamentary sanction is obtained'. Parliamentary sanction is obtained through the tabling in a subsequent financial year's annual Appropriation Bill, which includes a schedule outlining all payments made against TA in that previous financial year.

Additional warrant is **not** required to access TA.

## Conditions

TA capacity is limited to the amount that appears in Schedule 1 of the Appropriation Act under DTF. As such, the Treasurer will initially only provide approval in-principle for successful funding requests. The final source of funding for this supplementation will be reviewed by DTF and confirmed by the Treasurer towards the end of the financial year, taking into account total TA capacity and other available sources of Departmental appropriation authority.

TA may be applied to output or asset funding requests. This is determined by the Treasurer informed by advice from DTF.

## Reporting

Accountability for use of the TA is also met through the presentation of a summary of each year's expenditure in the State's Annual Financial Report which is tabled in the Parliament after the end of each financial year.

## Application and assessment process

A Minister may apply for budget supplementation from TA by submitting a letter of request to the Treasurer.

Each request is assessed by DTF and advice is provided to the Treasurer. The Treasurer will then determine whether or not to fund the request.

*Please note the following:*

For new policy decisions made by Cabinet or a sub-committee that requires a TA, refer to Section 4.2 Central Contingencies for guidance on such requests.

A TA request is for funding in the current financial year only. If changes in funding are required in the other forward estimates years, this should be foreshadowed in the TA request and a submission should then be made as part of the annual budget process.

## Approval notification

The Treasurer will provide return correspondence to the Minister making the request.

DTF will also advise the Department on the following if the funding request is approved:

- (a) the source of the funding;
- (b) the revenue limit; and
- (c) adjusted output and financial performance targets (if relevant).

## 1.4 Supplementation under section 35 of the FMA

### Mandatory requirements SUPPLEMENTATION UNDER SECTION 35 OF THE FMA

#### 1.4.1 Process and requirements for requests for supplementation under section 35 of the FMA

In preparing a letter from a Minister to the Treasurer seeking supplementation from section 35 of the FMA, a Department must ensure that the letter includes:

- (a) the reasons for the funding request;
- (b) the quantum of the variation sought;
- (c) confirmation that there are no other sources available to fund the request;
- (d) how the funding request aligns with Government objectives;
- (e) any proposed adjustments to output and financial performance targets arising from the request; and
- (f) any funding variations previously approved by the Treasurer or the relevant Cabinet committee for the program seeking the supplementation.

#### 1.4.2 Reporting on supplementation under section 35 of the FMA

All expenses and obligations to which any Section 35 of the FMA is applied must be reported in the financial year in respect of which the supplementation was provided.

#### 1.4.3 Restrictions on section 35 of the FMA

If any component of a section 35 FMA supplementation in a given year remains unapplied (i.e. unspent) at the end of the financial year, it may only be carried over to the following year with the approval of the Treasurer (FMA section 35 (4)).

## Guidance

### Definition

Section 35 of the FMA authorises the Treasurer to issue funding out of the Public Account to enable a Minister to meet urgent claims in the current budget year. Such urgent claims for Budget supplementation may include funding required for additional output and asset investment initiatives approved by the relevant Cabinet committee.

Parliamentary sanction is required for this funding pursuant to the specific wording of section 35 itself. This is addressed in a subsequent year's Appropriation Bill (section 7). Therefore, because it is technically an advance from the Public Account until such time as approved by Parliament, a warrant is **not** required for supplementation under section 35 of the FMA.

In a single budget year, the Treasurer is only authorised under section 35 to issue temporary advances of up to 0.5 per cent of the total amount appropriated by the annual Appropriation Act (the main bill) for that year.<sup>20</sup>

<sup>20</sup> The Appropriation Bill for Parliament is not included in the calculation. Section 35 of the FMA does not appropriate the amount, it is section 7 of a subsequent year's Appropriation Bill (the main Bill) that does so. Since the following year's appropriation is submitted to the Parliament before the end of the financial year, the amounts presented for ratification are delayed until the following year's Bill. There is no equivalent schedule in the Bill for Parliament.

## Conditions

The Treasurer will initially only provide approval in-principle for successful funding requests under section 35. The final source of funding for this supplementation will be reviewed by DTF at the end of the financial year, taking into account other available sources of appropriation authority.

## Reporting

Accountability for use of section 35 is also met through the presentation of a summary of each year's expenditure in the State's Annual Financial Report which is tabled in Parliament after the end of each financial year.

## Application and assessment process

A Minister may apply for budget supplementation from section 35 by submitting a letter of request to the Treasurer.

Each request is assessed by DTF and advice is provided to the Treasurer. The Treasurer will determine whether or not to fund the request.

## Approval notification

The Treasurer will provide return correspondence to the Minister making the request.

DTF will also advise the Department on the following if the funding request is approved:

- (a) the source of the funding;
- (b) the revenue limit; and
- (c) adjusted output and financial performance targets (if relevant).

## The difference between a Treasurer's Advance and supplementation under section 35 of the FMA

A Treasurer's Advance and supplementation under section 35 of the FMA provide the Government with two sources of (almost identical) additional funding to supplement the Budget in a given year. The key difference is that the Treasurer's Advance appropriation is accounted for in the budget estimates and the Annual Appropriation Bill (under the Treasury and Finance portfolio), whereas funding legally available under section 35 is generally not included in the estimates.

In practice, this has meant section 35 has been used to fund capital expenditure (which does not impact the operating statement), while Treasurer's Advance is usually reserved for operating (output) expenditure. Note there is nothing specifically mentioned in the FMA or elsewhere precluding section 35 being used to fund operating expenditure, or to prevent TA from being used to fund capital expenditure.

DTF will determine the final funding sources and seek approval from the Treasurer accordingly to use this section of the FMA.

## 1.5 Borrowing against future appropriation – section 28 of the FMA

<b>Mandatory requirements</b> <b>BORROWING AGAINST FUTURE APPROPRIATION (SECTION 28 OF THE FMA)</b>	
<b>1.5.1</b>	<b>Process and requirements for section 28 ‘Borrowing against future appropriation’ requests</b>  In preparing a letter from a Minister to the Treasurer seeking supplementation from section 28 of the FMA, a Department must ensure that the letter includes: <ul style="list-style-type: none"><li>(a) the reasons for the funding request, including how the request aligns with the specific requirements of section 28. Specifically:<ul style="list-style-type: none"><li>(i) why it is considered prudent and advantageous to expend the money in the current financial year; and</li><li>(ii) why the benefit of that allocation will accrue, or continue, in the next financial year;</li></ul></li><li>(b) the quantum of the additional funding sought;</li><li>(c) that there are no other sources available to fund the request (or demonstrate that there is an inability to redeploy existing resources to meet assessed requirements);</li><li>(d) how the funding request aligns with Government objectives;</li><li>(e) any proposed adjustments to output and financial performance targets arising from the request; and</li><li>(f) any funding variations previously approved by the Treasurer or the relevant Cabinet committee for the program seeking the advance.</li></ul>
<b>1.5.2</b>	<b>Reporting on section 28 ‘Borrowing against future appropriation’ expenditure</b>  All expenses and obligations to which any section 28 of the FMA is applied must be reported in the financial year in respect of which the advance(s) was made.

### Guidance

#### Definition

Section 28 of the FMA enables the bringing forward of funding from future appropriations to the current year. Under the FMA, the Governor in Council, on the recommendation of the Treasurer, may approve an allocation to a Department in addition to their annual appropriation amounts.

Section 28 supplementation is deemed a special appropriation and a warrant is required.

## Conditions

For a section 28 request to be approved, the legislation states that the Treasurer must not recommend the allocation to the Governor in Council unless the Treasurer is 'satisfied that this allocation is for a prudent and advantageous purpose in the current financial year, and that the benefit will accrue, or continue, in the next financial year'. Typically, this may apply to new capital projects or to capital projects which have been brought forward for continuation or completion. A successful justification for expenditure on outputs would be more difficult to sustain.

Under section 28 an amount issued must not exceed an amount equal to three per cent of the Department's total (gross) annual appropriation for the year. The total available for all departments is 0.5 per cent of the total annual appropriation for that year.

## Reporting

Accountability for use of section 28 is also met through the presentation of a summary amount in the State's Annual Financial Report, which is tabled in Parliament after the end of each financial year.

## Application and assessment process

A minister may apply for budget supplementation from Section 28 of the FMA by submitting a letter of request to the Treasurer.

Each request is assessed by DTF and advice is provided to the Treasurer. The Treasurer will determine whether or not to recommend the funding proposal to the Governor in Council for approval.

## Approval notification

The Treasurer will provide return correspondence to the minister making the request. DTF will also advise the Department on the following if the funding request is approved:

- (a) the source of the funding;
- (b) the revenue limit; and
- (c) adjusted output and financial performance targets (if relevant).

## 1.6 Transfers between items of Departmental appropriation – section 30 of the FMA

Mandatory requirements TRANSFERS BETWEEN ITEMS OF DEPARTMENTAL APPROPRIATION (SECTION 30 OF THE FMA)	
<b>1.6.1 Process and requirements for section 30 appropriation transfers</b>	<p>In preparing a letter from a Minister to the Treasurer seeking agreement to transfer amounts between its own appropriation items under section 30 of the FMA, a Department must ensure the letter includes:</p> <ul style="list-style-type: none"><li>(a) the reasons for the request;</li><li>(b) the quantum of the variation sought;</li><li>(c) that there are no other sources or mechanisms available;</li><li>(d) how the request aligns with Government objectives;</li><li>(e) any proposed adjustments to output and financial performance targets arising from the request; and</li><li>(f) any other variations previously approved by the Treasurer or the relevant Cabinet committee for the programs affected.</li></ul>
<b>1.6.2 Reporting on section 30 FMA expenditure</b>	<p>All expenses and obligations to which any section 30 transfer is applied must be reported in the financial year in which the transfer was made.</p>

### Guidance

#### Definition

Section 30 of the FMA enables a Minister, with consent from the Treasurer, to transfer an amount from one appropriation item to another in the current year, up to the limit appropriated in that year.

Warrant is **not** required for a section 30 request.

#### Conditions

For a section 30 request to be approved, the relevant Minister must demonstrate:

- that the appropriation being transferred is no longer required for its original purpose for which it was appropriated, and
- that there are insufficient funds available in the appropriation (where the funds are being transferred into) to fund the initiative/project.

## **Reporting**

Accountability for use of section 30 is also met through the presentation of a summary amount in the State's Annual Financial Report which is tabled in Parliament after the end of each financial year.

## **Application and assessment process**

Transfer requests must consist of a letter from the relevant portfolio minister addressed to the Treasurer.

Each request is assessed by DTF and advice provided to the Treasurer. The Treasurer will determine whether or not to consent to the request.

## **Approval notification**

The Treasurer will provide return correspondence to the Minister making the request.

DTF will also advise the Department if the transfer request is approved.

## 1.7 Carryover (of unused appropriation) – section 32 of the FMA

### Mandatory requirements SECTION 32 CARRYOVER (UNUSED APPROPRIATION)

#### 1.7.1 Process and requirements for requests for carryover of appropriation

In preparing a letter from a Minister to the Treasurer seeking permission to carryover unspent appropriation under section 32 of the FMA, a Department must ensure the letter includes:

- (a) the quantum of the carryover sought (for any output, ATNAB and POBOS appropriation);
- (b) the reasons for the carryover request. This must include an explanation of why the carryover is sought, as well as information to justify its approval. Explanations must also include the identification and details of specific programs or projects that have resulted in the request;
- (c) any proposed adjustments to output and financial performance targets arising from the request; and
- (d) the application of any prior year's carryover on the programs or projects that form part of the request.

The Treasurer shall determine if the carryover request will be approved.

#### 1.7.2 General carryover approval conditions and limits

- (a) Carryovers into the following budget year can only be considered where the appropriation has not already been applied.
- (b) Any unapplied appropriation not approved for carryover will lapse.
- (c) Section 32 does not permit a Department to carry forward a carryover from a preceding year.

#### 1.7.3 Specific conditions for carryover for output appropriation

- (a) Unless the Treasurer approves otherwise, Departments may only carryover the unapplied provision of output appropriation up to three per cent of the total (gross) appropriation for that item.
- (b) Any carryover request cannot exceed the difference between revenue certified and total appropriation provided in a financial year.
- (c) A carryover request shall not be granted if the Department's revenue for the year has been fully certified.

## Guidance

### Definition of carryover

A carryover arises when amounts appropriated annually for Departments or the Parliament, which remain unapplied at the end of one financial year, are approved by the Treasurer for application in the following financial year (i.e. amounts are 'carried over' and deemed added to the appropriation for the following financial year). This approval is granted under the authority of section 32(1) of the FMA.

Special or standing appropriations are not impacted by the carryover provisions.

Warrant is **not** required for a section 32 request.

### General carryover guidance

#### Provision of output appropriation

Where a Department has delivered less than its budgeted quantity of outputs, but the outputs actually delivered have been provided in the budgeted unit cost, the Department may apply to the Treasurer for approval for the remainder of the appropriation to be carried over to a subsequent year.

DTF will assess any requests for carryover against the Department's revenue certification claim and the Government's priorities to ascertain whether the request is reasonable.

#### Additions to the net asset base (ATNAB) appropriation

Where a Department's capital investment program has not been progressed as originally budgeted for, a Department may seek the Treasurer's approval to carry over the unapplied appropriation specific to the delayed projects.

Appropriation associated with a capital project that is to be discontinued is not usually eligible for carryover. The unapplied appropriation associated with such projects normally lapses, unless the Treasurer authorises otherwise.

Requests for carryover of unapplied appropriation for additions to the net asset base are considered on a case-by-case basis.

#### Payments made on behalf of the State (POBOS) appropriation

A Department may apply to the Treasurer for a carryover related to the deferral of any payments made on behalf of the State.

Requests for carryover of unapplied appropriation for payments made on behalf of the State are considered on a case-by-case basis.

### When should carryover apply (or not apply)?

A Department's carryover request will be considered and assessed on a case-by-case basis by DTF.

There are certain types of expenditure which, as a general rule, DTF would not support for carryover. Such examples include:

- funding for initiatives that the Government has decided should not continue;
- employee expenses for ongoing employees; and
- funding for the awarding of legal costs (where the outcome is not yet determined).

Departments should discuss any potential carryover items with DTF that may be contentious before submitting a formal carryover request.

### **Contrasting carryover with the definition of a surplus**

Where a Department *fully delivers* the outputs funded by provision of output appropriations, and the corresponding operating expenses are less than its revenue, the difference is recognised as a surplus on the provision of outputs.

Departments retain this surplus in their SAU receivables account in accordance with Section 2.1, and may apply to use it in a future financial year to increase the quantity or quality of outputs provided, subject to the approval of the Treasurer.

In contrast, a carryover implies that a Department has been unable to use the full appropriation amount in its output delivery, so there has been *under-delivery* of the output. It is the Government's prerogative whether or not to fund the output shortfall in the following financial year, or potentially to apply the funds to the delivery of an additional output initiative.

### **Update of budgets with carryover estimates**

Departments should include any forecast appropriation carryover estimates in their annual budgets. They should also review and, if required, revise appropriation carryover estimates during each update of the Budget.

## 1.8 Access to previously appropriated amounts under section 33 of the FMA

**Mandatory requirements**  
**ACCESS TO PREVIOUSLY APPROPRIATED AMOUNTS UNDER SECTION 33 OF THE FMA**

**1.8.1 Applications of section 33 of the FMA**

A Department may apply for access to previously appropriated amounts under section 33 of the FMA for one of the following:

- use of prior years' surpluses;
- Long Service Leave (LSL) funding accumulated in prior years;
- payment of outstanding creditors or other accrued obligations; or
- depreciation equivalent funding accumulated in prior years (for funding asset investment only).

**1.8.2 Process and requirements for section 33 of the FMA**

In preparing a letter from a Minister to the Treasurer or the relevant Cabinet committee to access one of the sources of funding in 1.8.1 under section 33 of the FMA, a Department must ensure the letter includes:

- (a) the reasons for the funding request;
- (b) the quantum of the funding sought;
- (c) how the purpose of the funding request aligns with Government objectives; and
- (d) any proposed adjustments to output and financial performance targets arising from the request.

**1.8.3 Reporting on section 33 FMA expenditure**

All expenses and obligations to which any section 33 of the FMA is applied must be reported in the expenses and payments of the financial year in which the amount was made available.

### Guidance

#### The use of section 33 of the FMA

Section 33 of the FMA is the enabling authority (special appropriation) to access the accumulated balances of a Department's SAU receivables account, and requires the Treasurer's approval to access the Consolidated Fund.

Warrant is required for section 33 requests.

For specific guidance on when section 33 of the FMA may be utilised, please refer to the following sections:

- departmental surpluses (Section 2.1);
- depreciation equivalent balances (Section 2.2), and
- LSL equivalent balances (Section 2.3).

## 1.9 Public Account Advances – section 37 of the FMA

### Mandatory requirements PUBLIC ACCOUNT ADVANCES (SECTION 37 OF THE FMA)

#### 1.9.1 Process and requirements for section 37 Public Account Advance requests

In an application by a Minister to the Treasurer for advances from Section 37 of the FMA, the Department must prepare a letter to support the application with information including:

- (a) the reasons for the request;
- (b) the quantum of the amount sought;
- (c) that there are no other sources available to fund the request;
- (d) how the funding request aligns with Government objectives;
- (e) any proposed adjustments to output and financial performance targets arising from the request;
- (f) supporting cash flow projections over the forward estimates and the proposed source of funds to meet the repayment schedule with expected timeframes; and
- (g) any funding variations previously approved by the Treasurer or the relevant Cabinet committee for the program seeking the advance.

#### 1.9.2 Reporting on section 37 Public Account Advance requests

All expenses and obligations to which any section 37 of the FMA is applied must be reported in the financial year in respect of which the advance(s) was made.

## Guidance

### Definition

Section 37 of the FMA enables the advancing of funds from the Public Account, to be repaid at a later point in time.

Warrant is **not** required for a section 37 request as it is not a drawdown from the Consolidated Fund.

### Conditions

The Treasurer's approval is required for a section 37 Public Account Advance, which will provide the authority to draw down on the funds.

Such an advance may be used as temporary (short-term) funding pending receipt of other revenues, including future year appropriations in the following circumstances (not a definitive list):

- to pay the outstanding bills of a Department or public body; or
- to bring forward funding of an investment or initiative that realises savings at a later point in time.

Repayment of the advance is required, and interest may be charged on such advances.

Departments should also review and, if required, revise estimates during each update of the Budget, noting the Treasurer's approval is required for any deviations from the agreed repayment schedule.

## 2. Accrual budgeting concepts

### 2.1 Departmental surpluses

#### Mandatory requirements DEPARTMENTAL SURPLUSES

##### 2.1.1 Application of Departmental surpluses

A Departmental operating surplus on the provision of outputs may be applied at the discretion of the Department, provided the following conditions are met:

- (a) a request for access to surpluses must outline the intended use of the surplus;
- (b) the surpluses must be applied for a purpose consistent with Government objectives; and
- (c) the use of Departmental surpluses is one-off in nature and must not give rise to any future year commitment or customer expectations of future commitment.

### Guidance

Output appropriation is provided to Departments by government as payment for the production of agreed services and outputs.

Under this funding model, government pays a 'price' to Departments (recognised as revenue) for delivery of outputs. If a Department produces outputs for less cost than the revenue provided, it records a surplus on these outputs, which is included in the balance of the Department's State Administration Unit (SAU) inter-entity account. The Department may apply to the Treasurer to access and apply that surplus to other spending proposals under section 33 of the FMA. This is intended to act as an incentive to Departments for delivering services for less than the agreed 'price'.

The range of purposes to which a surplus may be applied is not limited as long as Departments comply with the broad parameters set out in the Mandatory requirements.

This guidance should be read in conjunction with Section 1.8 (Access to previously appropriated amounts under section 33 of the FMA). Note a warrant is required to access surpluses generated in prior years.

### The contrast with carryovers

Carryover occurs when an annual appropriation amount for the previous year was not applied and the Treasurer has approved the application of this amount in the following year. This implies under-delivery of the outputs concerned, whereas a surplus is the difference in appropriation revenue achieved above the cost of delivery of an output.

## 2.2 Depreciation and depreciation equivalent

### Mandatory requirements DEPRECIATION AND DEPRECIATION EQUIVALENT

#### 2.2.1 Depreciation equivalent for asset revaluations

Departments may apply for an increase in its depreciation equivalent (appropriation) funding, to account for an increase in depreciation expense as a result of asset revaluations, by submitting a request to the Treasurer.

#### 2.2.2 Depreciation equivalent for portfolio agencies

If informed by a decision of the Government, a Department may transfer depreciation equivalent funding for approved capital projects in portfolio agencies as a capital grant expense to the agency concerned. The receiving agency will recognise the grant as revenue.

#### 2.2.3 Depreciation on administered assets

- (a) Depreciation on an administered asset must be recorded in a Department's administered entity.
- (b) A Department must not include depreciation on an administered asset in Departmental controlled operating costs for budgeting or reporting purposes.
- (c) Depreciation equivalent asset investment funding does not apply to the acquisition of an administered asset.
- (d) If an administered asset is required to be replaced or enhanced, funding must be sought as part of a submission.

## Guidance

### Definition of depreciation equivalent

Depreciation equivalent is the amount of appropriation revenue equal to actual depreciation expense for a given year. As depreciation is a non-cash expense, this amount remains undrawn in the Consolidated Fund, but is initially recognised notionally for the Department in its SAU receivable account until expended on approved capital investment items.

### What is the purpose of depreciation equivalent?

The purpose of depreciation equivalent revenue is to preserve the net asset value of the portfolio department by providing a source of asset investment funding. Both the Appropriation Act (section 5) and section 33 of the FMA for accumulated prior year unspent balances require that expenditure can only be made on fixed assets.

Under accrual budgeting principles, depreciation equivalent is one of the primary sources of funds available for asset investment, along with:

- proceeds of net asset sales (generally accessed under a section 29 agreement); and
- Additions to the Net Asset Base (ATNAB) appropriation funding.

Other sources of funding include Commonwealth (section 29 agreement) or other third-party revenues (generally through ATNAB or revenue of portfolio agencies such as TAFEs or hospitals).

Refer to Section 3.1 (Asset Funding) for more information on the funding of assets, and **the order in which the fund sources should be accessed**.

There is no direct link between depreciation equivalent and the renewal and replacement requirements in a Department's physical asset base. However, the intent of depreciation equivalent is to be a primary contributor to sustain asset investment requirements.

### How does a Department access its depreciation equivalent balance?

A Department may only access depreciation equivalent to fund approved asset investment programs determined by the Government.

**Current year's depreciation equivalent revenue** - may be accessed by a Department to fund approved asset investment.

**Prior year's depreciation equivalent balances** - a Department may submit a request to the Treasurer to access this balance in its SAU account under section 33 of the FMA.<sup>21</sup>

For instructions on the application of a section 33 request, please refer to section 1.8 (Access to previously appropriated amounts under section 33 of the FMA).

Note that where a Department has prior years' depreciation equivalent balances available, these balances should be applied to asset investment before accessing their ATNAB appropriation.

### Depreciation on administered assets

Administered assets are managed by a Department on behalf of the State. Departments should maintain accounting records of depreciation on administered assets in the same way as their controlled assets.

However, depreciation on administered assets is not associated with Departmental output delivery, therefore it is not included in output costs.

When an administered asset is to be replaced or enhanced, an amount for asset investment should be sought as part of the overall appropriation for administered items.

### Transfer of depreciation equivalent to agencies

As a general rule, depreciation equivalent revenue should **not** be applied to government controlled agencies outside the general government sector.

### Impact of asset revaluations

As part of an asset revaluation process, the accumulated depreciation associated with the asset being revalued is 'written back' into the accounts. There is no impact however on the existing depreciation equivalent balances in a Department's SAU inter-entity account.

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<sup>21</sup> Section 33(2) of the FMA only permits depreciation equivalent balances to be used to fund asset investment.

## Other information on depreciation equivalent

### What is the difference between depreciation and depreciation equivalent?

Depreciation expense refers to the non-cash expense charged to an entity's accounts to represent the allocation of an asset's cost over its useful life. As this expense has no associated cash outflow, the depreciation equivalent revenue included as part of a Department's output appropriation funding remains in the Consolidated Fund. Being part of the revenue earned by a Department for the year, it is recorded as a receivable in the Department's SAU inter-entity account, pending draw down from the Consolidated Fund for approved asset investment purposes.

### What is the difference between *accumulated* depreciation and depreciation equivalent?

There is no direct link between accumulated (i.e. unspent) depreciation equivalent in the SAU (which is an asset), and accumulated depreciation which captures the written-down value of assets in the Balance Sheet (a contra-asset).

## Relevant materials

### Attachments

- Attachment 3: Depreciation Equivalent – Asset investment funding sourced from provision of outputs appropriation diagram

### Financial Reporting Directions

- FRD 119A *Transfers through Contributed Capital*

## 2.3 Long service leave and long service leave equivalent

### Mandatory requirements LONG SERVICE LEAVE AND LONG SERVICE LEAVE EQUIVALENT

#### 2.3.1 Valuation of balances of accumulated long service leave

- (a) The accumulated long service leave (LSL) provision must be estimated in accordance with the reporting provisions set out in AASB 119. Therefore any variation to the liability must be brought to account as a revaluation of the liability at 30 June each year, split between its components of 'transaction' and 'other economic flows'.
- (b) The gain or loss on revaluation of the LSL provision must be included in 'Other Economic Flows' in the Departmental operating statement.

#### 2.3.2 Inclusion of estimated annual long service leave expense in output costs

Estimated annual LSL expense (i.e. the amount expensed as a transaction in a Department's controlled operating statement) must be included in calculating the total estimated output costs of a Department.

#### 2.3.3 Long service leave equivalent (LSL equivalent)

- (a) A LSL equivalent amount is recognised in the SAU inter-entity account when an actual LSL expense is first recognised.<sup>22</sup>
- (b) Any revaluation or write back of LSL which has been classified as an 'Other economic flow' does not change the LSL equivalent amounts in the SAU inter-entity account.
- (c) LSL equivalent accumulates as a financial asset in a Department's SAU inter-entity account, until used to fund LSL payouts.

#### 2.3.4 Transfer of long service leave balances between Departments

- (a) When employees are transferred between Departments *as a result of a machinery of government change*, the accumulated liability and the full amount of LSL equivalent must be transferred between the two Departments.
- (b) For all other transfers of employees between Departments (e.g. due to job transfers, promotions etc.), only the accumulated liability is transferred between the two Departments. The LSL equivalent is not transferred

#### 2.3.5 Funding of long service leave when long service leave equivalent is exhausted

- (a) Departments must ensure sufficient LSL equivalent is included in its budgeting processes, to cover any expected up-coming LSL payouts.
- (b) When a Department's expected LSL payouts in a particular budget year is estimated to exceed the funds available in its SAU inter-entity account, Departments may seek additional supplementation by providing a submission to the relevant cabinet committee for consideration.

<sup>22</sup> This **excludes** any subsequent recognition of gains or losses on revaluation of the LSL provision arising from the changes in present value resulting from the discount (bond) rate applied.

## Guidance

### Long service leave provision

Accumulated LSL provisions for employees are a liability on each Department's balance sheet. The LSL entitlement expense starts to accumulate when an employee completes a pre-qualifying period with a Department. In each accounting period an operating expense is recognised, which progressively increases the corresponding accumulated liability.

Generally, under existing public sector employment conditions, employees are entitled to three months LSL after 10 years of service and can be accessed on a pro-rata basis after seven years of service.

LSL represents an obligation (or a liability) of the Department to its employees and any LSL outstanding at the end of each reporting period is accrued.

Theoretically, the LSL entitlement starts when an employee commences with a Department. However, in practice, an LSL expense is financially recognised when an employee completes a pre-qualifying period of service (although generally the legal obligation to pay out LSL does not commence until an employee has achieved seven years' continuous service).

### Long service leave equivalent

The component of a Department's revenue stream, equal to actual LSL expense incurred by an employee, becomes the amount of LSL equivalent available to a Department, recognised in its SAU balance. This amount is set aside notionally in the Consolidated Fund for the purposes of paying out LSL when required.

### Drawdown of cash to fund long service leave payouts

Cash payments for LSL, regardless of the period to which the liability relates, will be met by drawing against the LSL equivalent balance in the SAU inter-entity account. It may be some years before payment is due, and in that time the balance in the SAU inter-entity account should have increased sufficient to cover the amount due in cash. If, because of an unexpected demand for LSL payouts, there is insufficient LSL equivalent balance available, the Department will need to apply for additional funding to cover the expected cash shortfall.

Payment to employees will draw down against the Department's LSL provision when:

- employees choose to use their LSL entitlement after it matures (through the taking of leave, or via a monetary payout); or
- employees cease employment with the Victorian Public Service and their employment agreement entitles them to a monetary payout of part or all of their accrued benefit.

Departments do not need to apply to access LSL equivalent accumulating in the SAU inter entity account to pay out LSL unless the drawdown of cash for this purpose leaves the SAU closing balance at 30 June lower than the year's opening balance at 1 July. In this latter case, approval is required under section 33 of the FMA to access the prior year's SAU balance.

For instructions on the application of a section 33 request, please refer to Section 1.8 (access to previously appropriated amounts under section 33 of the FMA).

## Transfers of employees between Departments

Transfers of employees between Departments may be effected as an annual adjustment covering net transferred entitlements of all transferred employees.

### Relevant materials

#### Attachments

- Attachment 4: Pro-forma journal entries for LSL transactions
- Attachment 5: Diagrammatical representation of long service leave funding flows (DEDJTR as the example)

#### Accounting standards

- AASB 119 *Employee Benefits*

#### Financial Reporting Directions

- FRD 17B *Wage Inflation and Discount Rates for Employee Benefits*

## 3. Asset funding and management policies

### 3.1 Asset funding

#### Mandatory requirements ASSET FUNDING

##### 3.1.1 Asset investment proposals considerations

A Department's asset investment proposal must demonstrate that the proposed asset investment is the most effective and efficient means of delivering the Department's outputs, and meets Government objectives.

The proposal should also consider:

- (a) any alternatives such as leasing, outsourcing and/or private provision; and
- (b) the implications on output provision performance (quantity, quality, timeliness, revenue and expense) of the investment.

##### 3.1.2 Order of funding for approved asset investment programs

A Department's approved asset investment program must be funded from the following sources in the specified order below:<sup>23</sup>

- (a) any funds provided by the Commonwealth towards specific projects;
- (b) the unspent depreciation equivalent receivable held in the SAU inter-entity Account;
- (c) net proceeds of asset sales; and
- (d) additional Additions to the Net Asset Base (ATNAB) appropriation funding.

##### 3.1.3 Asset replacement

A Department must not replace an asset unless doing so is consistent with a Department's approved overall asset investment plan and Government priorities.

### Guidance

This guidance serves to provide Departments direction on the policies and processes regarding the funding of asset investment.

This guidance should also be read in conjunction with the Asset Management Accountability Framework (AMAF). The framework seeks to ensure that public assets are managed with consideration for their whole lifecycle costs and to optimise service delivery outcomes. The framework establishes a number of mandatory requirements and provides guidance on good practice for asset management.

#### Departmental investment prioritising and approval

Departments are expected to allocate sufficient funding to maintain their assets within their allocated budget. Where service delivery objectives can be improved through additional investment, funds can be sought through the budget process for consideration against other investment priorities.

<sup>23</sup> With written approval from DTF, a Department may vary the order in which these funding sources are applied.

Departments should consider using the Investment Management Standard (IMS) to help develop and prioritise investment proposals. The IMS is a collection of simple ideas and practices that help organisations direct resources to deliver the best outcomes.

### Content of asset investment proposals

Asset investment proposals should be supported by a business case that includes sufficient documentation and analysis to support the proposal. The investment lifecycle and High Value High Risk guidelines provide comprehensive guidance to assist in the development of a business case.

Departments must ensure any funding proposals for asset investment have considered:

- alternative funding sources that may offset the cost of a proposal, provided the funding source is relevant to the proposal being considered<sup>24</sup>; and
- that any contingencies calculations included in a proposal are well-developed and robust.

These asset investment proposals are assessed by central agencies, with recommendations made to Cabinet advising which asset investment proposals to approve.

### Cabinet process

Cabinet assesses Departmental asset submissions on a whole-of-government basis, to inform the Government's asset investment program.

Each Department's asset investment proposals will then be evaluated and approved by the relevant Cabinet committee on a project-specific basis.

The approval of the Treasurer is required if a Department wishes to re-cashflow the Total Estimated Investment (TEI) of a project across the forward estimates.

The approval of the relevant Cabinet committee will be required if a Department wishes to substitute another project in place of one that has been approved.

Decisions regarding major asset refurbishment, replacement, purchase or construction of new assets will be based on an assessment of whether such expenditure is the best way for the Department to meet its future output delivery commitments.

### DTF's role in determining asset funding decisions

As part of its role advising the Government on investment decisions, DTF will consider the robustness of supporting information. For asset funding proposals, this may include information derived from Asset Information Management Systems and asset strategies (e.g. a case for funding where there is existing asset stock may include information on the stock condition and how the proposal is consistent with the Department's asset management strategy).

### Funding of approved asset proposals

Asset investments can be funded from a variety of sources, that should be drawn down in following order:

- a) **Commonwealth funds for specific projects:** if such funds are received, these must be applied against these projects as the priority source of funding;

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<sup>24</sup> While Departments may take into account the existence and extent of hypothecated revenues when preparing asset investment proposals, the decision to allocate hypothecated revenues to particular investment projects rests with Government.

- b) **Depreciation equivalent in the SAU inter-entity Account:** these funds comprise the balance held by each Department in its SAU inter-entity account for current and prior years' unspent depreciation equivalent revenue (refer to Section 2.2 for more information);
- c) **Net proceeds from asset sales:** these proceeds may be used to fund asset investment, provided they have been subject to a section 29 FMA agreement. Where a purchase of a new asset involves the trade-in of an existing asset, the use of the proceeds from the trade-in to fund the assets will require section 29 approval (see Section 1.1 for more information); and
- d) **Additions to the Net Asset Base (ATNAB) appropriation funding:** should the first three sources be insufficient to fund the Department's approved investment program, the provision of additional ATNAB appropriation by Government may be required.

The order of the drawdown of funds used to fund asset investment is also listed in the Mandatory requirements of this section.<sup>25</sup>

### Departmental asset investment program

Asset investment proposals approved by Government form part of a Department's overall asset investment program.

A Departments' asset investment spending during any Budget year will consist of:

- the first year's expenditure on new major asset investments approved by the relevant Cabinet Committee to be started in the Budget year; and
- estimated annual cash flows for those assets approved by Government in previous years' investment programs.

### Recognition of the operating costs associated with assets

Operating costs associated with the holding of assets include depreciation expense and Capital Assets Charge (CAC). Departments should recognise the impact of these operating costs in asset proposals, and throughout the life of the asset.

The inclusion of depreciation expense on controlled assets in output costing and pricing recognises that assets have a finite working life, and enables funds to be allocated (via depreciation equivalent) to finance the acquisition of new or replacement assets to meet future service delivery plans.

The CAC recognises the cost to Government of the capital invested in the assets (see Section 3.2 for more information on CAC).

### Managing growth in asset base

Where additional capital funding is approved that leads to a material increase in the total value of depreciable assets held by a Department, Departments are responsible for ensuring output revenue remains sufficient to meet the costs of the management of the assets that supports the delivery of outputs.

This may be achieved by:

- agreeing with Government that additional outputs will be produced from additional revenue from appropriations;
- increasing revenue from non-appropriation sources; or
- negotiating increases in output prices.

<sup>25</sup> A Department may also use its retained surpluses on the provision of outputs to fund asset investment, subject to the provisions of approval under section 33 of the FMA.

## 3.2 Capital Assets Charge

### Mandatory requirements CAPITAL ASSETS CHARGE

#### 3.2.1 Capital Assets Charge levy rate

A Department must apply a Capital Assets Charge (CAC) levy rate of eight per cent on the budgeted written down value of controlled non-current physical assets of the Department and its portfolio (general government sector) agencies, as per the amount in Budget Paper No. 5 *Statement of Finances*.

#### 3.2.2 Charging of Capital Assets Charge to actuals

A Department must apply the CAC at one-twelfth of eight per cent of the budgeted written down value of controlled non-current physical assets (as per Budget Paper No. 5), each month.

#### 3.2.3 Capital Assets Charge allocation across outputs

CAC must be allocated across a Department's outputs as part of Departmental budgeting processes.

### Exemptions to the Capital Assets Charge

#### 3.2.4 Administered assets

A Department must not include administered assets in the calculation of the non-current physical assets base on which the CAC is charged, as these assets do not contribute to output delivery.

#### 3.2.5 Financial and intangible assets

Financial assets (which include cash, investments and deposits with the SAU inter-entirety account), and intangible assets, are *not* subject to CAC.

#### 3.2.6 Exempt controlled physical assets

The following specified assets are currently exempt from the CAC:

- (a) the declared road network controlled by VicRoads encompassing:
  - pavement and earthworks;
  - sound barriers;
  - bridges;
  - traffic signal control systems; and
  - construction in progress.
- (b) national parks;
- (c) cultural collections and structures; and
- (d) motor vehicle finance lease assets held under the whole-of-government Standard Motor Vehicle Policy.

## Guidance

### What is the Capital Assets Charge?

The Capital Assets Charge (CAC) is a charge (operating expense) levied on the written down value of controlled non-current physical assets of a Department (i.e. the Department and its general government sector portfolio agencies detailed in its balance sheet). The charge aims to facilitate the full costing of outputs by attributing to agency outputs the opportunity cost of capital used in service delivery.

Departments are appropriated the amount of CAC appropriation funding equal to eight per cent of the budgeted written down value of controlled non-current physical assets of the Department and its portfolio (general government sector) agencies, to fund the CAC expense.

The CAC policy is subject to periodic review by DTF.

### Capital Assets Charge cost allocation across outputs

CAC is paid by a Department as a whole, and each Department is responsible for allocating CAC expenses across its outputs and to its internal divisions and portfolio (general government sector) agencies.

To ensure prices are not distorted, the proportion of total Departmental CAC that should be included in the cost of each output should reflect as closely as is practical the proportion of Departmental non-current physical assets that are used in the production of the output.

### Potential variations to the Capital Assets Charge

There may be circumstances where the CAC amount to be charged on a monthly basis by a Department is different to what is required as per Mandatory requirement 3.2.2. Situations where this may occur could include machinery of government changes. Departments must discuss such situations with DTF to determine whether adjustments to the CAC amount are necessary.

### Impact of revaluations and variations in asset base

Departments should manage their asset base effectively, and carry out timely asset revaluations in accordance with accounting standards. Such revaluations may affect the amount of CAC payable by a Department in future periods.

### Construction-in-Progress

The CAC shall apply, unless otherwise exempt, to Construction-in-Progress (CIP), in the years following the commencement of the construction:

- Year 1 of construction – no CAC applies; and
- Year 2 onwards – recognise prior year's construction amounts for the purposes of applying CAC.

## 4. Other budget policies

### 4.1 Hypothecation arrangements

#### Mandatory requirements HYPOTHECATION ARRANGEMENTS

##### 4.1.1 Instructions on hypothecation arrangements

Departments must discuss with DTF any proposal it considers could potentially be funded through a hypothecation arrangement, and must demonstrate how the proposal meets the five criteria set out in this section.

### Guidance

#### Definition

Hypothecation is the linking of specific expenditure requirements with particular revenue sources, either through legislation (hard hypothecation), or through government policy alone (soft hypothecation). There may be some instances where such an arrangement is desired in directing certain revenue streams towards a particular program or initiative, such as the hypothecation of revenue from roads safety initiatives towards the funding of roads infrastructure (through the Better Roads Victoria Trust Account).

#### Comment on hypothecation arrangements

As a general rule, unless otherwise determined by the Government, expenditure is not tied to specific revenue sources, in order to provide the Government with maximum flexibility in the way it chooses to allocate resources to meet its objectives. Also, depending on their design, hypothecation arrangements may also lead to less scrutiny being placed on projects, services or programs, and may lead to an inefficient and ineffective allocation of resources if Government priorities change over time.

If a hypothecation arrangement is to be considered, departments should consider a soft hypothecation arrangement. These arrangements are more flexible, can be amended through Government policy, and are typically broader in their application. The revenue for such hypothecation arrangements should flow through to the Consolidated Fund, and not to trust funds or other accounts.

#### Criteria to consider before consulting with DTF

The following five criteria must be considered in determining whether or not a proposed hypothecation arrangement is suitable:

##### Criteria 1 – Clear superiority over alternative arrangements

A proposed hypothecation arrangement must explain:

- why a hypothecation arrangement is superior in the set of circumstances;
- what alternative arrangements have been considered;
- the reasons why the alternative arrangements have not been deemed suitable for adoption; and
- what differences in outcomes alternative arrangements would likely produce.

## **Criteria 2 – Links to whole-of-government priorities**

A proposed hypothecation arrangement must consider the following questions with regards to whole-of-government priorities:

- What key Government priority does the proposal hope to achieve and how will it do this?
- Are the proposed spending initiatives likely to remain a Government priority over the next four to five years?
- What flexibility is there to adapt the funding to any future changes in Government priorities?

## **Criteria 3 – Clear link between revenue sources and expenditure**

A proposed hypothecation arrangement must demonstrate a clear link between the new revenue source and proposed expenditure.

## **Criteria 4 – Stable expenditure streams and revenue source**

A proposed hypothecation arrangement must:

- state the anticipated size and timing of the expenditure and revenue streams, and how the streams will vary over time; and
- explain any risks associated with the forecasting of the revenue and expenditure streams.

## **Criteria 5 – Regular review process**

All hypothecation arrangement proposals must incorporate a formal review mechanism and sunset clause.

## 4.2 Central contingencies

### Mandatory requirements CENTRAL CONTINGENCIES

#### 4.2.1 Process and requirements for requests to access central contingencies

In requesting access to funding from central contingencies for previously approved Government funding decisions, a Department must ensure the request documentation includes:

- (a) the reasons and context for the request;
- (b) the quantum of the funding sought;
- (c) reference to the Government decision to support the request;
- (d) how the funding request aligns with Government objectives;
- (e) any proposed adjustments to output and financial performance targets arising from the request; and
- (f) any funding variations previously approved by the Treasurer or the relevant Cabinet Committee for the program or output.

#### 4.2.2 Reporting on expenditure from central contingencies

All expenses and obligations to which any funding from central contingency is applied, if related to funding from the Treasurer's Advance, must be reported in the financial year in which the funding was provided.

#### 4.2.3 Restrictions on central contingencies

Any unapplied component of funding from central contingency from a Treasurer's Advance in a given year lapses at the end of the year. Departments are not permitted to carry over contingency funding sourced from Treasurer's Advance to the following year.

## Guidance

### Definition

Central contingencies are provisions established by government for future expenditure which have not yet been allocated to specific departments. These contingencies are held and managed by DTF.

Government may set aside central contingencies to provide for:

- service growth;
- new initiatives in future budgets;
- Government decisions which for various reasons, are not recorded in the relevant Department's or agency's financial statements at that time;
- future cost pressures; and
- urgent and unforeseen expenditure.

Central contingencies for outputs and assets are outlined in the notes of the estimated financial statements and are categorised by 'decisions made but not yet allocated' and 'funding not allocated to specific purposes'.<sup>26</sup> Treasurer's Advance may form a part of the central contingencies.

### **Application and assessment process**

A Minister is required to submit a request to the Treasurer or relevant Cabinet committee to request release of budget funding for a specific project, initiative or policy that is held in a central contingency.

Advice is provided by DTF to the Treasurer or the relevant Cabinet committee, who will decide whether to approve the release of the central contingency to the Minister.

### **Approval notification**

Departments shall be advised if the release from the central contingency is approved.

### **Reporting**

Accountability for use of the TA, within the context of the central contingencies, is also met through the presentation of a summary of each year's expenditure in the State's Annual Financial Report which is tabled in the Parliament after the end of each financial year.

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<sup>26</sup> Output contingencies are disclosed in Note 12 (c), Chapter 1, Budget Paper 5. Asset contingencies are disclosed in Note 20 (c), Chapter 1, Budget Paper 5.

## 5. Concepts and mechanisms underpinning budget and financial management

### 5.1 The State Administration Unit

#### What is the State Administration Unit?

The concept of the State Administration Unit (SAU) was developed with the introduction of accrual output budgeting and management in the late 1990s.

The SAU was set up for the following purposes:

- as an accounting mechanism for capturing and recording transaction flows and balances in the Public Account; and
- a means of capturing certain relationships and balances between the Government (with DTF as the 'corporate head office') and Departments (such as Contributed Capital balances).

Note the SAU is not a separate legal entity in its own right.

#### The components of the State Administration Unit

The SAU consists of three components:

1. SAU inter-entity accounts;
2. SAU branch ledger; and
3. SAU head office/central component.

#### 1. The SAU inter-entity account(s)

This SAU component is most relevant to Departments.

The SAU inter-entity account comprises each Department's **appropriated but unspent (not yet drawn down)** funds that are available to it in the Public Account, sourced from non-cash expenditure (such as depreciation and long-service leave) or liabilities for expenditure not yet paid for i.e. accrued expenses.

In the State's ledger the SAU inter-entity transactions are effected through three receivables accounts:

- Account 45000 – SAU Inter-Entity (Consolidated Fund);
- Account 45500 – Trust Fund Inter-Entity (Trust Fund); and
- Account 46000 – Public Account Advances FMA.

These accounts are used in each Department's **controlled** entity.

Departments are required to submit a quarterly dissection report to DTF to explain the movements and balances in its SAU inter-entity accounts (refer to Section 5.2 for more information).

## 2. The SAU branch ledger

This SAU component records the administered transactions of each Department, such as:

- payments on behalf of the State (various amounts in the annual Appropriation Act or grants on-passed through the trust fund from the Commonwealth to an entity outside of Victorian Government);
- the amount invested by government in its controlled entities (other than the core Departments); and
- revenue received on behalf of the State and paid to a central agency (such as taxes revenue).

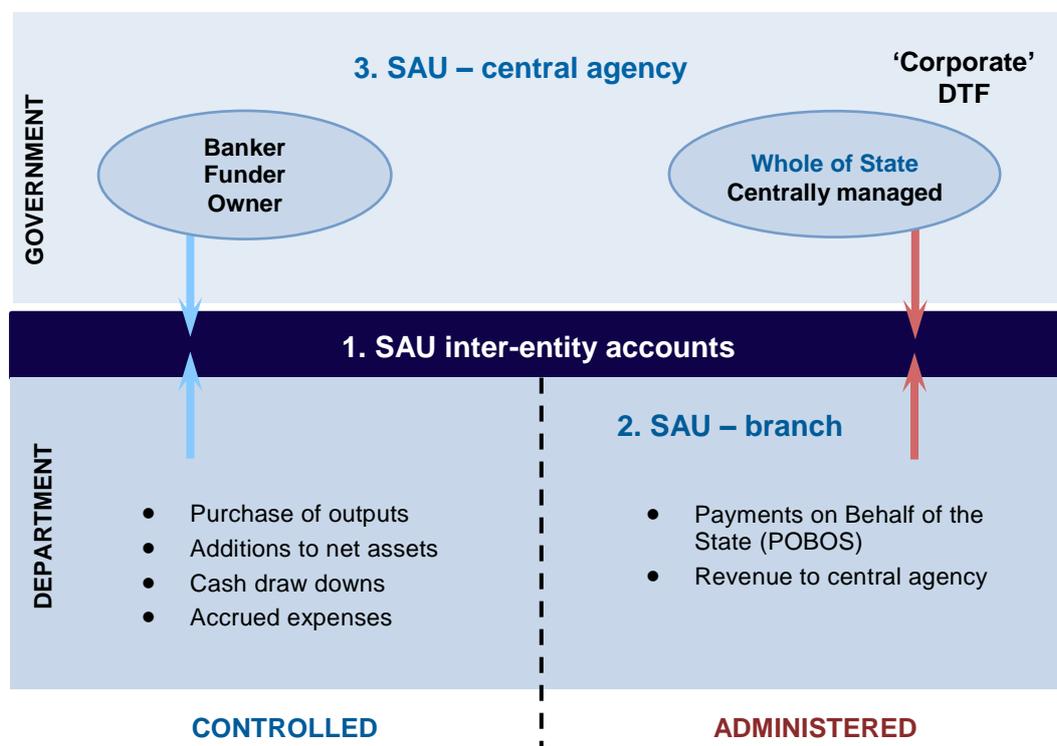
In the State's ledger, the SAU branch ledger is represented in Department's accounts by the x100 entity in each Department.

## 3. The SAU head office/central agency component

This SAU component records the transactional flows between Departments and the Public Account. It may also record transactions that do not functionally or operationally belong to a particular Department.

In the State's ledger, this component of the SAU is represented by the entity 9200 'State Administration Unit'. This component is visible to, and maintained centrally by DTF. Departments are generally not involved in the workings of this component of the SAU.

The three components of the SAU are also represented diagrammatically below:



## How the three components of the State Administration Unit interact

The following section seeks to explain the SAU's workings through a hypothetical set of transactions.

Transaction/event	Entity	Account	Amount
Receipt of taxation revenue by DTF (administered entity)	7100 (SAU branch ledger)	6xxxx (Revenue)	-1000
Submission of tax revenue to Consolidated Fund (via SAU)	7100 (SAU branch ledger)	90500	+1000
Receipt of taxation revenue by the SAU	9200 (SAU central agency)	70570	-1000
Recognition of funds in the State's bank account	9200 (SAU central agency)	10230 (Bank)	+1000
<b>Funds appropriated for expenses (cash items)</b>			
Drawdown from bank account	9200 (SAU central agency)	10230 (Bank)	-200
Transfer to Department	9200 (SAU central agency)	86500	+200
Appropriation drawn down by Department	Controlled Dept. Entity	71200	-200
Expense incurred	Controlled Dept. Entity	86000	+200
<b>Funds appropriated for expenses (non-cash items)</b>			
Drawdown from bank account	9200 (SAU central agency)	10230 (Bank)	-400
Transfer to Department	9200 (SAU central agency)	86500	+400
Appropriation drawn down	Controlled Dept. Entity	71200	-400
Increase in Departmental SAU Inter entity account	Controlled Dept. Entity	45000 (SAU Inter-entity account)	+400
Depreciation expense incurred	Controlled Dept. Entity	81xxx	+400
Recognition of accumulated depreciation (contra-asset)	Controlled Dept. Entity	2xxxx	-400

## Relevant materials

### Attachments

- Attachment 2: *The history of the establishment of the State Administration Unit*

## 5.2 The SAU inter-entity account dissection

<b>Mandatory requirements</b>	
<b>STATE ADMINISTRATION UNIT (SAU) – INTER-ENTITY DISSECTION</b>	
<b>5.2.1</b>	<b>SAU inter-entity account dissection requirements and time frames</b>
(a)	The SAU inter-entity account dissection must be undertaken twice a year. <sup>27</sup>
(b)	The SAU inter-entity account dissection must be certified by the relevant Chief Financial Officer (CFO) and forwarded to DTF.
(c)	The certification must be provided in accordance with the time frames advised in DTF Information Requests.
(d)	The dissection must separately identify: <ul style="list-style-type: none"><li>• appropriations by Parliament;</li><li>• the drawdown of cash by Departments;</li><li>• appropriation funded accruals;</li><li>• unspent depreciation equivalent;</li><li>• unspent long service leave (LSL) equivalent; and</li><li>• surplus on the provision of outputs.</li></ul>
<b>5.2.2</b>	<b>Specific end of year requirements</b>
(a)	The SAU inter-entity account dissection must be provided to the Auditor-General's Office and DTF as part of the end of year process, together with the final draft of the Department's annual report.
(b)	The date for delivery of the dissection to the Auditor-General's Office must be negotiated between each Department and its auditors.
<b>5.2.3</b>	<b>Machinery of government changes requirements</b>
	When machinery of government changes occur, the SAU inter-entity account dissection must be updated by affected Departments as at the date of the machinery of government change. A copy of the dissection must then be provided to DTF in a timely manner.
<b>5.2.4</b>	<b>Resolution of issues</b>
(a)	Departments must resolve all issues/variances identified by DTF in a timely manner.
(b)	DTF must provide all necessary assistance to Departments in clarifying and understanding the issues involved.

<sup>27</sup> This coincides with the Mid Year and Annual Financial reporting requirements. A Departmental CFO may decide to complete inter-entity account dissections at more frequent intervals for internal management and control purposes.

## Guidance

The SAU inter-entity account comprises each Department's appropriated but unspent (not yet drawn down) funds and other amounts that are available to it in the Public Account. This may include balances payable from the Consolidated Fund or cash held by central agency on behalf of Trust Accounts in the Trust Fund.

Specifically, the SAU dissection seeks to account for a Department's:

- appropriations by Parliament;
- the drawdown of cash by Departments in accordance with the appropriate parliamentary authority;
- appropriation-funded accruals (such as employee entitlements and payables);
- unspent depreciation equivalent;
- unspent LSL equivalent; and
- surplus on the provision of outputs.

### The SAU inter-entity dissection – template and additional notes

Departments are required to submit a regular dissection report to DTF to explain the movements and balances in this account. This is required to satisfy legal, audit and budget monitoring requirements.

The SAU dissection template is provided in *Attachment 1* for use by Departments.

For more information on how to populate the SAU dissection template, please contact your usual DTF contact.

### Reporting on the SAU inter-entity account (account 45000) dissection

The SAU inter-entity account balance dissection must be reconciled to the relevant financial statements to ensure the integrity of the information provided.

The SAU inter-entity account is considered a current receivable amount in the financial statements, as it is expected Departments will draw down on the bulk of their appropriations within a 12-month period. Consequently, there is no requirement to re-measure this receivable to present value terms.

Note inter-entity account 45500 represents cash held in relation to Trust Accounts and is available on demand to settle trust fund payables. As such, it is reported as Cash at Bank in departmental financial statements.

## Relevant materials

### Attachments

- Attachment 1: *SAU dissection template*

## 6. Guidance on estimates updates

### 6.1 Policy vs non-policy journal entries

As part of the annual Budget and Budget Update processes, Departments may submit budget journal entries to update their budget estimates in the State Resource Information Management System (SRIMS) for approval by DTF.

When submitting these journal entries to SRIMS, Departments must identify whether a journal entry submitted is either 'policy' or 'non-policy' in nature.

**Policy journal:** A policy journal will allow a Department to post variations to appropriation accounts. Following a Government decision to introduce a new program or project, a policy journal will reflect the adjustment of appropriation as necessary. These journals should be able to source a Cabinet committee, Treasurer or Ministerial decision that underpins the estimate change. Policy decisions also include decisions to provide a Department with additional budget supplementation.

Examples of SRIMS policy journals include:

- decisions from Budget deliberations;
- Treasurer's Advance decisions; and
- Section 37 Public Account advances.

Departments can only increase their appropriation by applying for budget supplementation and receiving approval from the Treasurer or the relevant Cabinet committee.

**Non-policy journal:** A non-policy journal does not allow for a variation of appropriations.

Examples of non-policy SRIMS journals include:

- reallocations between expense accounts;
- changes to third party revenue estimates; and
- asset revaluations/devaluations.

## 6.2 Process for the creation of the fourth year estimates in SRIMS (rollover)

### Guidance

The Budget process involves the creation of the Budget year and the creation of three years of forward estimates, commencing after the newly Budgeted year, to assist with budget management. As each year's Budget is created in SRIMS, the final year of the forward estimates rolls forward to two years out, rather than three years out.

As such, a new estimates year is added each year, to the end of the last existing estimates year. This is known as creating the rollover year.

This process in SRIMS typically occurs in October/November (after the finalisation of the State's Annual Financial Report). These estimates are intended to capture the known funding for programs relevant to the State in that particular financial year.

### Explanation of the forward estimates

The 'forward estimates' consist of the current year, plus the following year plus three additional years.

For example, the current forward estimates consist of the following years:

Current year	Next Budget Year	Budget Year + 1	Budget Year + 2	Budget Year + 3
2016-17	2017-18	2018-19	2019-20	2020-21

Once the 2017-18 budget year commences (1 July), it becomes the new current year, the budget years get 'rolled forward' by one, which then creates the requirement for the new budget year (i.e. the rollover year).

Current year	Budget Year	Budget Year + 1	Budget Year + 2	Budget Year + 3 (rollover year)
2017-18	2018-19	2019-20	2020-21	2021-22

### The rollover creation process

Currently, the rollover and creation of a new estimates year is carried out by DTF each year as part of the Budget Update process in November.

This involves the following steps:

1. DTF copies over the estimates (movements) from the previous year into the new year created in SRIMS.
2. DTF then processes journal entries to adjust these estimates for any Departmental Funding Model (DFM) indexation and General Efficiency Dividend (GED). These adjustments are applied to each department's appropriation revenue item, with the associated expense amount for the new year allocated to the Indexation Adjustment Account (86999).
3. Departments are then required to submit journals for items that need to be adjusted and also to reallocate the amount from the Indexation Adjustment Account to appropriate expense accounts.

## Timing

The revised rollover process commences in October (post finalisation of the Annual Financial Report), and is usually completed by the end of January.

### List of items to consider in a rollover process

Below is a list of items for Departments to consider when completing a rollover and creation of the new forward estimates year. Note this is not an exhaustive list and is intended to be a guide only.

Item	Comments
Ensuring the removal of sun-setting initiatives	DTF will review all journal entries to ensure that lapsing programs have not been reinstated.
Changes to Special Appropriation: Examples include Hypothecated revenue, Judicial Salaries and Electoral Commission appropriation	DTF will check the amounts posted are reasonable in terms of growth over the forward estimates (relative to actuals and existing forward estimates) and will request an explanation if the estimates look significantly different to what is expected.  Note some special appropriations substantially vary in accordance with the underlying purpose (e.g. Electoral Commission).
Commonwealth grants and associated expenditure/capital	These adjustments will be reviewed on a case-by-case basis.
Indexation for any fixed price items (e.g. contracts)	Department should have a record of all fixed price items. DTF will check the reasonableness of indexation applied.
Employee entitlements	Departments must check the entitlements on the balance sheet are reasonable, and advise DTF on the validity of the estimate.  Departments may need to review the number of pay periods for estimate year to determine if a 27th pay is applicable.
Any movements in current and non-current items	Departments are required to check for items that are split between current and non-current that appear to fluctuate between years, e.g. finance leases.
Any revaluations to balance sheet	Refer to FRD 103E which outlines the asset revaluation schedule for departments.
Any asset purchases or sales	
Trust fund cash balances and associated revenue and expenses	Departments should ensure any movements in cash balances align with movements in interest revenue and expense accounts.
Reallocation of DFM/GED balance from Indexation Adjustment Account (86999) to the appropriate expense accounts.	Once adjustments have been made, the account should be zero.
Any (other) items from the Long-term Commitments database	

# Attachments

## Attachment 1: SAU dissection template

The State Administration Unit (SAU) dissection is required to be completed on the spreadsheet template provided below.

The template consists of five tabs:

- Statement C1 – Dissection of Departmental SAU inter-entity balances within the Consolidated Fund (controlled entities);
- Statement C2 – Reconciliation of Controlled SAU to appropriation;
- Statement C3 – Reconciliation to Departmental operating statement;
- Statement C4 – Reconciliation to Departmental financial statements; and
- Statement A1 – Reconciliation of Administered SAU to appropriation.



SAU Dissection  
updated 13 July 2017

Please also note the following about the SAU dissection:

- Only the controlled entities within a Department require both a dissection (refer *Statement C1*) and reconciliations. However, a reconciliation of movements in the Administered Entity SAU inter entity account to appropriations is also required (refer *Statement A1*);
- As Trust Fund transactions do not flow through the Consolidated Fund, these are not included in *Statement C1*, but are included in *Statement C4*; and
- Reconciliations of Controlled and Administered Appropriations in the SAU are required – refer to *Statement C2* (controlled) and *Statement A1* (administered).

## Attachment 2: The history of the establishment of the State Administration Unit

One of the most significant financial management reforms in the late 1990s was the move from cash to an accrual-based appropriation budgeting and reporting regime. The Public Ledger Operating Statement began to reflect revenues earned, regardless of whether cash has been received, and expenses incurred, but not necessarily paid (or payable) in cash.

Under these reforms, the concept of the State Administration Unit (SAU) was established, and became operational on 1 July 1998. The SAU formalises arrangements between Departments and DTF as the 'Corporate Office' for the State of Victoria from an accounting and reporting perspective following the introduction of accrual output budgeting and management.

At any given time, the balance held in each Department's SAU inter entity account represents appropriated funds available to that Department which have not been drawn. This can result in substantial financial assets being available to Departments, which represent the value of appropriations that have been applied but for which money has not been drawn from the Consolidated Fund.

### Purpose of the SAU dissection:

For Victorian Government Departments, to:

- manage the application of appropriation funding provided;
- ensure legislative and administrative requirements are met;
- identify and verify unspent depreciation equivalent to be applied against asset initiatives during the current year, and in the out years, contained in the forward estimates;
- identify unspent levels of long service leave (LSL) equivalent to be applied to fund future draw downs on the provision for LSL;
- identify and verify the surplus on the provision of outputs, which will be available for application against future initiatives, following the Treasurer's approval, and
- identify Departmental obligations to pay employee entitlements, creditors and other commitments since 1 July 1998, for which output appropriation has been certified but not drawn.

For DTF to verify that:

- legislative and administrative requirements have been met;
- the unspent component of the depreciation equivalent is available for future application towards asset investment/replacement when formulating the forward estimates, and
- the surplus on the provision of outputs is available for application against initiatives to be approved by the Treasurer.

### Attachment 3: Depreciation equivalent – Asset funding sourced from provision of outputs appropriation diagram

Operating Statement for the Provision of Outputs for the Department. Authority codes between 002005 and 002220	Amount \$		Balance Sheet	Amount \$	Comment
Revenue			SAU Inter-entity Account 45000		
			SAU Inter-entity Account opening balance	200,000	SAU Inter-entity Account opening balance covering prior-years depreciation equivalent per SAU Inter-Entity Dissection Statements
			Current year actual depreciation expense equivalent	50,000	Department receives appropriation for the provision of outputs which is deposited in its SAU in-entity account.
			<b>Total Available depreciation Equivalent</b>	<b>250,000</b>	
Appropriation for the Provision of Outputs- Accounts 71050 to 71200	-1,000,000		Appropriation covering current year other output expenses.	950,000	
<b>Total Appropriation Revenue for the Provision of Outputs received during the current year.</b>	<b>-1,000,000</b>		<b>Total Appropriation funding available in the SAU Inter-entity account</b>	<b>1,200,000</b>	
Expenses (Outputs)			Payments SAU Inter-entity Account payments comprising:		
			Payment for Property Plant and Equipment (Additions to the Net Assets Base) from previous years depreciation equivalent	-200,000	Payment for property plant and equipment from previous year's depreciation equivalent. In this instance, the Treasurer's approval under S.33 of the <i>Financial Management Act 1994</i> is required.
Depreciation (includes amortisation) – Accounts between 81000 and 81950.	50,000		Payment for Property Plant and Equipment (Additions to the Net Assets Base)	-50,000	Payment for property plant and equipment from current year's depreciation equivalent.
Other Expenses – Accounts between 80100 and 80985 and between 82000 and 90800	950,000		Payments for Output Expenses	-950,000	Normal payments for output expenses from the Provision of Outputs appropriations.
<b>Total Expenses</b>	<b>1,000,000</b>		<b>Total draw-downs from the SAU Inter-Entity Account</b>	<b>-1,200,000</b>	
<b>Total operating result</b>	<b>0</b>		<b>Total Balance in the SAU Inter-entity Account</b>	<b>0</b>	

## Attachment 4: Pro-forma journal entries for long service leave (LSL) transactions

### 1. Accruing of long service leave by employees

The provision for long service leave (LSL) progressively increases as a result of accumulating LSL expense.

- Dr** Long service leave expense (other than revaluation of Present Value of LSL) – account 80500 (transaction flows)
- Dr** Long Service leave expense – gains (losses) on revaluation account 80550  
(Annual appropriation authority codes must not be used with this account).
- Cr** Long service leave provision (Liability)

Departments receive funding for the payment of LSL (Other than revaluation of Present Value of LSL – account 80550) as part of the revenue received for the delivery of outputs. This revenue is recorded in the form of a deposit in the SAU inter entity account.<sup>28</sup>

- Dr** SAU inter entity account LSL (Asset)
- Cr** Revenue for outputs (Revenue)

### 2. Recognition of long service leave resulting from previous employment outside the Victorian budget sector

Employees in the Victorian Public Service (VPS) may have a period of service with a previous employer that was outside the VPS but is still recognised for LSL purposes.

- Dr** Long service leave expense (Expense)
- Cr** Long service leave provision (Liability)

### 3. Pay out of leave: employee resigns, retires or takes a payout in lieu of leave

Upon resignation, retirement or by request, an employee receives a payment in lieu of LSL if he/she is recognised as having seven or more years of service and has not fully drawdown on his/her available LSL entitlement:

- Dr** Long service leave provision (Liability)
- Cr** Cash at bank (Asset)

Cash at bank would be reimbursed from the SAU inter-entity account:

- Dr** Cash at bank (Asset)
- Cr** SAU inter-entity account LSL (Asset)

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<sup>28</sup> Appropriation revenue is not provided for LSL gains/(losses) on revaluation due to changes in the present value resulting from the discount (bond) rate applied.

#### **4. Employee resigns or retires – no pay out of leave provision as a result of not accruing a sufficient entitlement to a payout under their conditions of employment**

An employee who resigns or retires is not entitled to receive a payment in lieu of LSL if they are not recognised as having at least seven or more years of service and is not entitled to pro rata payment in lieu of LSL upon cessation of employment.

In this situation the LSL provision is written back against LSL expense and no reduction is made to the deposit with the SAU inter entity account.

- Dr** Long service leave provision (Liability)
- Cr** Long Service Leave expense (Expense)

#### **5. Deposits accrued in the SAU inter entity account are sufficient to fund long service leave**

It is expected that there will generally be sufficient SAU deposits accrued to fund LSL as it falls due for payment. Accordingly the following transactions would normally apply:

- Dr** Long service leave provision (Liability)
- Cr** Cash at bank (Asset)

Cash at bank would be reimbursed from the SAU inter entity account as follows.

- Dr** Cash at bank (Asset)
- Cr** SAU Inter entity account LSL (Asset)

Refer Attachment 5: Representation of long service leave funding flows for an illustration how the SAU inter-entity Account is funded for LSL expense.

#### **6. Deposits accrued in the SAU inter-entity account are insufficient to fund long service leave over the long term**

There may be occasions where deposits accrued in the SAU inter entity account will be insufficient to pay LSL over the long term due to some unforeseen condition arising. There are two specific times when this can occur:

1. there is an increase in the number of staff taking LSL in a particular year; or
2. due to the age profile of staff in a Department, a significant number of staff who have accrued LSL fall due for retirement.

For both conditions noted above:

Reduction in liability (provision for long service leave)

- Dr** Long service leave provision (Liability)
- Cr** Appropriation<sup>29</sup>
- Cr** SAU balance (to the extent that existing balances are available)

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<sup>29</sup> This example assumes that additional output appropriation has or will be made available.

**7. The transfer of an employee's accrued service leave entitlement when that employee secures employment outside of a Department to an organisation not covered by agreements for the transfer of LSL funding**

Circumstances may arise where an employee secures employment outside a Department and their accrued LSL provision is recognised by the new employer. Unless employment arrangements exist for the payment of LSL on a pro rata basis upon resignation the following applies:

- Dr** Long service leave provision (Liability)
- Cr** Long service leave expense (Expense)

**8. Long service leave accruals for salaries paid from Special Appropriations or Trust Funds**

Normally salaries and employee entitlements will be funded out of output revenue. However, there will be some cases where the source of funds will be either from special appropriations or trust funds. In these circumstances it will be necessary to charge LSL expense against the Special Appropriation or trust fund with a corresponding increase in the SAU inter-entity account.

(a) Long service leave is accrued

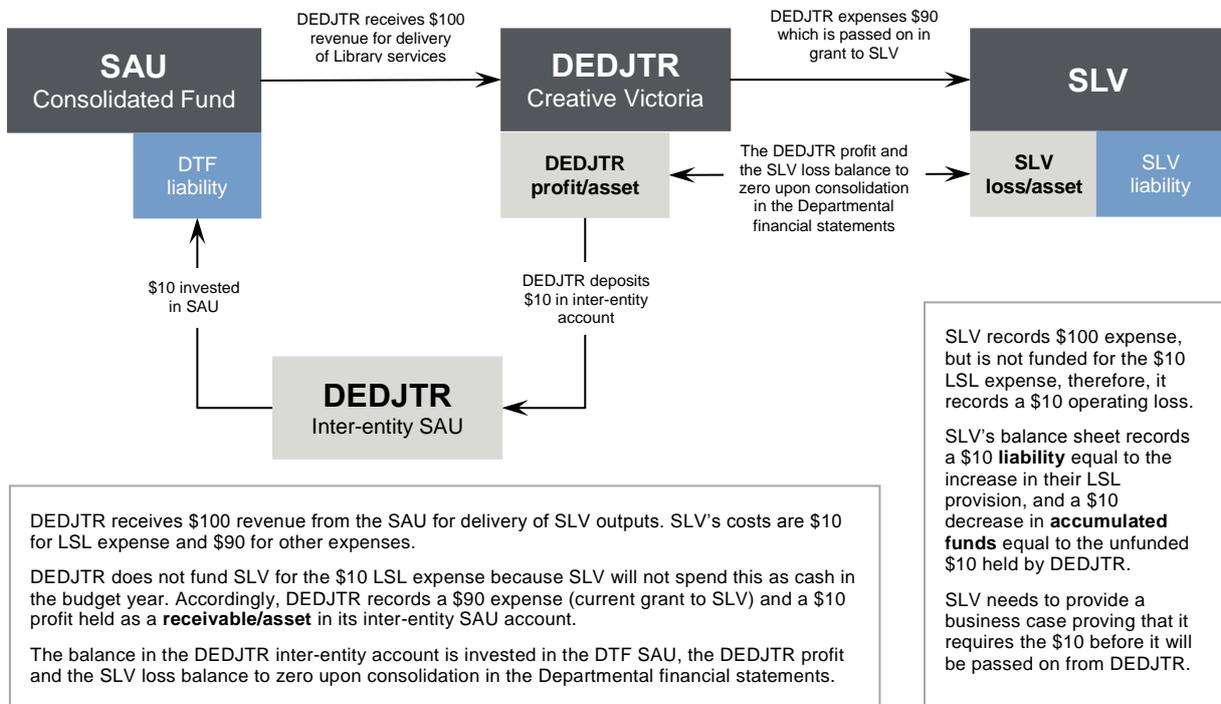
- Dr** Long service leave expense (Expense)
- Cr** Long service leave provision (Liability)

(a) Transfer of funds equal to long service leave expense into the SAU inter-entity Account

- Dr** SAU inter-entity account LSL (Asset)
- Cr** Special Appropriation (Revenue)

## Attachment 5: Representation of long service leave funding flows

(Department of Economic Development, Jobs, Transport and Resources (DEDJTR) and State Library Victoria (SLV) used in this example)







Treasury  
and Finance