

# **CHARTER OF BUDGET HONESTY POLICY COSTING GUIDELINES**

ISSUED JOINTLY BY THE SECRETARIES  
TO THE TREASURY  
AND THE DEPARTMENT OF FINANCE  
UNDER PART 8 OF  
*THE CHARTER OF BUDGET HONESTY ACT 1998*  
*2021*

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# CONTENTS

|   |           |
|---|-----------|
| <b>INTRODUCTION .....</b>   | <b>1</b>  |
| <b>PART 1 – COSTING OF ELECTION COMMITMENTS: ROLES OF THE SECRETARIES AND THE PARLIAMENTARY BUDGET OFFICER.....</b> | <b>2</b>  |
| <b>PART 2 – COSTING PROTOCOLS AND METHODS .....</b>   | <b>4</b>  |
| <b>PART 3 – PROCESS FOR ELECTION COSTINGS.....</b>  | <b>8</b>  |
| <b>APPENDIX A – BUDGET TREATMENT OF RELEVANT BALANCE SHEET TRANSACTIONS .....</b>                                   | <b>11</b> |
| <b>APPENDIX B – COMMONLY USED TERMS .....</b>   | <b>15</b> |
| <b>APPENDIX C – PRO-FORMA REQUEST FOR COSTING AN ELECTION COMMITMENT .....</b>                                      | <b>17</b> |
| <b>APPENDIX D – PRO-FORMA PUBLIC RELEASE OF COSTING.....</b>  | <b>20</b> |

## INTRODUCTION

The *Charter of Budget Honesty Act 1998* (the Charter) outlines arrangements under which the Secretaries to the Treasury and the Department of Finance (the Secretaries) may be requested to cost election commitments during the caretaker period prior to a general election. The Charter also allows for the Secretaries to jointly issue written guidelines recommending approaches or methods to be used in the preparation of such costings.

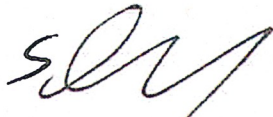
The *Charter of Budget Honesty Policy Costing Guidelines* (the Guidelines) outline the process for submitting and preparing policy costings. The Guidelines focus on matters directly relating to the methods and approaches as required by subclause 30(1) of the Charter.

Information on the role of the Parliamentary Budget Office (PBO) can be accessed from the [PBO website](#).

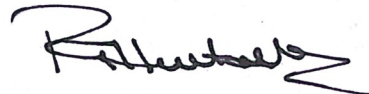
The Guidelines are consistent with the robust methods and approaches established by the Treasury and Finance for the preparation of policy costings outside of a caretaker period.

These Guidelines are similar to those released prior to the 2019 Election with the inclusion of additional information on the costing of guarantees.

We are releasing these Guidelines to provide all parties with appropriate notice of the arrangements for costing election commitments during a caretaker period.



Dr Steven Kennedy PSM  
Secretary to the Treasury



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Secretary of the Department of Finance

# **PART 1 – COSTING OF ELECTION COMMITMENTS: ROLES OF THE SECRETARIES AND THE PARLIAMENTARY BUDGET OFFICER**

The Charter outlines arrangements under which the Secretaries to the Treasury and the Department of Finance may be requested to cost election commitments during a caretaker period. The Parliamentary Budget Officer (the Officer) may also be requested to cost policies in the caretaker period. This part outlines the differences in the roles of the Secretaries and the Officer.

## **The Secretaries**

Part 8 of the Charter sets out the arrangements for the costing of election commitments by the Secretaries. These provisions relate to the costing of publicly announced policies, referred to as election commitments, of the Government, the Opposition and minority parties, and apply only during the caretaker period. The obligations of the Charter are independent of, but have precedence over, the caretaker conventions.

During the caretaker period, the Secretaries may be asked by the Prime Minister, the Leader of the Opposition or the Leader of a minority party<sup>1</sup> to cost their publicly announced policies.<sup>2</sup>

The approach and costing conventions used by the Secretaries when undertaking costings are outlined in Part 2 of these Guidelines. The procedures for submitting costings to the Secretaries and for the public release of costings are outlined in Part 3.

## **The Parliamentary Budget Officer**

Subsection 64J(2) of the *Parliamentary Service Act 1999* (the Act) provides that during the caretaker period, the Officer will prepare election policy costings upon request from a Parliamentary party or a sitting independent member of Parliament seeking re-election.

When requested to prepare a policy costing, the Officer must use approaches and costing conventions recommended in the most recent guidelines issued under the Charter.<sup>3</sup> With the agreement of the Secretaries, the Officer may issue alternate written principles, which then must be made publicly available.<sup>4</sup>

In the absence of principles issued by the Officer, the PBO must use these Guidelines as the basis for the preparation of policy costings.<sup>5</sup>

All requests to cost election policies made to the Officer by a Senator or Member of Parliament *within the caretaker period* must be made publicly available by the PBO.<sup>6</sup>

Further information on the role and functions of the PBO is available on the [PBO website](http://www.aph.gov.au/pbo).<sup>7</sup>

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<sup>1</sup> Clause 3 of Schedule 1 to the Charter defines 'minority party' as a recognised non-Government party of at least 5 members.

<sup>2</sup> Subclause 29(2) of Schedule 1 to the Charter.

<sup>3</sup> Clause 64G of the Act.

<sup>4</sup> Subsection 64G(3) of the Act.

<sup>5</sup> Subsection 64G(2) of the Act.

<sup>6</sup> See sections 64L and 64LA of the Act.

<sup>7</sup> <http://www.aph.gov.au/pbo>.

### **Prohibition against duplicate costings**

Subclauses 29(1A) and (1B) of the Charter and subsections 64J(3) and (4) of the Act prohibit Parliamentary parties from seeking duplicate costings of the same, or a substantially similar, policy from both the Secretaries and the Officer during an election campaign.

Section 64K of the Act requires the Officer to first ask the Secretaries whether a request has been made to prepare a costing of the same or substantially similar policy by the Secretaries under clause 29 of the Charter. If such a request has already been made to the Secretaries, the Officer must not prepare the requested costing.

## **PART 2 – COSTING PROTOCOLS AND METHODS**

The Charter, under clause 30, details how the policy costings are to be prepared. It provides for the Secretaries to issue written guidelines (this booklet) recommending approaches or methods to be used in preparing costings.<sup>8</sup>

### **DIVISION OF RESPONSIBILITIES**

The Charter divides responsibility for costings between the Secretaries:

- the Secretary to the Treasury is responsible for costing policies affecting taxation revenue; and
- the Secretary of the Department of Finance is responsible for costing policies that affect government outlays and expenses and non-taxation revenue.<sup>9</sup>

Policies that have implications for both taxation revenue and expenses will be jointly costed by the Secretaries. The costings for these policies will separately identify the revenue and expense components.

### **SECRETARIES' OBLIGATIONS IN COSTING POLICIES: CLARITY AND TIMELINESS**

The Secretaries will aim to be clear, transparent and timely in costing policies. In undertaking policy costings, the Secretaries will:

- endeavour to provide their best estimate of the full cost of a policy (including departmental expenses where requested and feasible);
- cost policies in a manner consistent with methodologies used to prepare the Budget statements and fiscal reports required under the Charter;
- cost Government, Opposition and minority party policies in a consistent manner;
- only provide financial costings, and not provide policy advice or assessments of the economic impact of policies; and
- produce a self-contained written report on the costing that fully justifies the published costings.

The Secretaries will endeavour to complete and release a costing within five business days of receiving a request. However, this may not be possible in the case of complex costing requests where data is difficult to obtain, or where more detailed information needs to be provided by the party. In such cases, a public statement to that effect will be made by the relevant Secretary at the outset, or when it becomes clear that the costing cannot be completed within the time frame. Where additional information is required, the five days will exclude the time taken to obtain the additional information.

For requests made after polling day, where the caretaker period extends after that day, the Secretaries are to publicly release costings as soon as practicable after the request is received.<sup>10</sup>

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<sup>8</sup> Subclause 30(1) of Schedule 1 to the Charter.

<sup>9</sup> Subclause 30(2) of Schedule 1 to the Charter.

<sup>10</sup> Paragraph 31A(3)(c) of Schedule 1 to the Charter.

## **COSTING VARIABLES**

Policy costings will focus on the effect of a policy on the Australian Government's key Budget aggregates (both cash and accruals) and include both the estimated cost and savings associated with the proposal. The estimates of the policies will show both the impact on the underlying cash balance and the fiscal balance in current dollars, as well as the impact on the headline cash balance as appropriate.

A request for a policy costing should fully outline the design features of the policy to be costed. It will assist in the preparation of costings if detailed information is provided on the assumptions that parties may have used in making their own assessments regarding the cost of policies. If necessary, in order to fully cost a policy, the relevant Secretary may request, in writing, more information from the Prime Minister, the Leader of the Opposition or the Leader of a minority party.<sup>11</sup> Appendix C contains a pro-forma indicating the information normally required for a costing to be prepared.

Estimates are provided for the current financial year and the forward estimates period using the most recent set of published estimates under the Charter as the benchmark. For election costings, these will be the forward estimates published in the Pre-Election Economic and Fiscal Outlook (PEFO). The financial years used in costings ends in June. Where necessary, full year, part year and one off effects will be distinguished in the advice.

Where revenue and expense costs are likely to be significantly different beyond this forward estimates period – for example, because the measure is not scheduled to commence or reach 'maturity' until after the forward estimates period – it may be necessary to include a statement about the financial impact of the policy beyond the forward estimates.

In the case of costing a policy package, both the cost of individual components and the overall cost of the package will be undertaken and, where feasible to do so, the effect of one component of a package on another will be taken into account and reported.

While costings will generally be the Secretaries' best assessment of the cost of a policy, in cases where assumptions are particularly uncertain, Secretaries may choose to publish costings as a range of possible outcomes.

### **Public Debt Interest<sup>12</sup>**

Costings will generally not account for the impact on Public Debt Interest (PDI) payments, unless it is an explicit policy objective to affect the level of interest payments, or the policy involves transactions of financial assets (such as loan schemes). PDI costings will normally assume no change to the debt management strategy.

Further information on the budget treatment of balance sheet transactions, including government investment funds and financial asset transactions can be found in Appendix A.

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<sup>11</sup> Subclause 30(3) of Schedule 1 to the Charter.

<sup>12</sup> PDI is the cost of servicing the stock of Australian Government debt incurred to meet budget financing and other borrowing requirements.



## **Departmental expenses**

Departmental expenses will be included where analysis of the policy shows that these are material. Existing programs/policies of a similar nature will be used as a guide to determining these expenses.

## **COSTING ASSUMPTIONS**

### **Consistency and transparency of costing assumptions**

Any economic data or forecasts used in costings will be consistent with the most recent publicly released estimates. The PEFO will be the basis of the economic parameters used in costing election commitments.

Other assumptions used in costings (for example, the numbers of people making use of a particular rebate or estimates of taxable incomes) will be the most appropriate available, based on the best professional judgment of the Secretaries.

The nature of assumptions used will be made clear by the Secretaries when publicly releasing costings and any caveats associated with the assumptions will be outlined. To maintain consistency, assumptions used in one policy costing will generally be used again for costing similar policies.

### **Direct behavioural and broader economic effects**

Policy costings will take into account the direct behavioural impact of a policy change when this is expected to be material to the costing. Direct behavioural impacts are the changes in the behaviour of individuals, businesses or organisations that are directly affected by a policy change, as well as the impacts on closely related industries where relevant.

Information on direct behavioural responses to a policy change is drawn from a variety of sources. These include previous experience for similar policy changes; academic and other studies of response effects or price elasticities; input from consultations or submissions; econometric modelling and studies; behavioural economics studies or trials, and sensitivity analysis estimating the scope for variations and taking a point estimate within the range.

For some policy costings, direct behavioural responses are not factored into the costing either because of a lack of information or an expectation that the magnitude of the behavioural response will be small. Both the inclusion of a behavioural response and the extent of the response in a policy costing can involve judgement.

There are also occasions where policy changes have broader economic or 'second-round' impacts. These impacts occur when a policy change has flow-on effects to the aggregate economy. Second-round impacts can include changes at the aggregate level in investment, wages, employment, prices and/or industry structure.

As a general rule, policy costings only take into account the direct behavioural effects of a policy change, and do not include broader economic or 'second-round' effects. Second-round effects are generally not included in costings for a range of reasons, including uncertainty in estimating the magnitude and timing of the effects and because generally it will be reasonable to assume that the second-round effects are likely to be small relative to the direct financial impact of a measure. Second-round effects are also likely to take longer to arise than the immediate costs of a new policy proposal, and often may not occur within the forward estimates' timeline.

Second-round effects have occasionally been included and separately identified in costings. Examples include: the 1994 *Working Nation* policy; the 1999 *Review of Business Taxation*; the 2000 *New Tax System*; the 2005 *Welfare to Work* package; and the 2010 *Stronger, Fairer, Simpler* package. These packages included estimates of second-round effects because the broad-based nature of the packages meant that they were expected to produce unambiguous second-round benefits for the whole economy rather than shifting resources from one activity to another. Moreover, the magnitude and timing of the reforms meant that the second-round effects were likely to be measurable over the forward estimates timeframe.

## **COMMONWEALTH BODIES' ASSISTANCE IN PREPARING COSTINGS**

The Charter allows the Secretaries to request an Australian Government body (for example, other government departments or agencies) to provide information to assist in the costing.<sup>13</sup> An Australian Government body is required by the Charter to comply with such a request in time to allow the information to be taken into account in the preparation of the policy costing, unless it is not practicable for the body to do so, or where providing the information would contravene another law of the Commonwealth.<sup>14</sup> The Secretaries will ensure consultations take place with other relevant departments or agencies, at senior management level, as a matter of course in producing a costing, so as to help ensure the assumptions chosen are the most appropriate. However, the final responsibility for the assumptions used will remain with the Secretaries.

## **FURTHER INFORMATION REQUIRED FOR THE COMPLETION OF COSTINGS**

If the Secretaries consider that further information is required, they may request information from the Prime Minister, the Leader of the Opposition, or the Leader of the relevant minority party, as appropriate, in writing.<sup>15</sup> The Secretaries will endeavour to ask for such additional information within two business days of receiving the costing request. Further discussion between the Treasury and/or Finance officials and advisers in the offices of the Prime Minister or the Leader of the Opposition or the Leader of the relevant minority party may be necessary as part of that process. Additional information provided in such discussions should be followed up in writing and forwarded to the Secretaries.

Requests for clarification will be noted in the final costings advice where the information materially affects the costing outcome.

## **VARIATIONS IN COSTINGS FROM THOSE SPECIFIED BY PARTIES**

Where there is a difference between a costing request and the publicly released policy, the Secretaries will seek to clarify the difference by seeking further information as outlined above. If that is not possible, the costing will be based on information provided in the costing request.

The difference may be due to variations between the assumptions made by the parties and those made by the Secretaries. Where a costing uses different assumptions to those specified in a party costing request, the costing advice will explain the reason for using those different assumptions.

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<sup>13</sup> Subclause 32(1) of the Schedule to the Charter.

<sup>14</sup> Subclause 32(2) of the Schedule to the Charter.

<sup>15</sup> Subclause 30(3) of Schedule 1 to the Charter.

## **PART 3 – PROCESS FOR ELECTION COSTINGS**

### **REQUESTS FOR COSTINGS**

During the caretaker period, the Secretaries may be asked by the Prime Minister, the Leader of the Opposition or the Leader of a minority party to cost their publicly announced policies. The processes are the same whether the request is made before polling day or after polling day, where the caretaker period extends beyond that date.

A request from the Leader of the Opposition or the Leader of a minority party is to be provided to the Prime Minister, who may then refer it to the responsible Secretary. The Secretaries are not obliged or authorised to take action in relation to any request, unless the Prime Minister has referred the request to them.

Clause 29 of the Charter details how requests for the costing of election commitments are to be made. A request is to:

- be in writing;
- fully outline the policy to be costed, giving relevant details; and
- state the purpose or intent of the policy.<sup>16</sup>

Upon receiving a request from – or through – the Prime Minister, the relevant Secretary (or Secretaries jointly) will issue a press release to inform the public they have been asked to cost a policy. The press release will broadly outline the policy to be costed.

### **Timelines for submitting costing requests**

Policy costing requests should be submitted to the Secretaries during business hours. Business hours for the purpose of these Guidelines are the weekday hours from 8.30 am to 5.30 pm. Requests received by Secretaries outside of these hours will be taken as having been received the next business day, unless otherwise specifically agreed in advance with the relevant Secretary. These timing conventions will apply to both the public release of information regarding the request, as well as the commencement of work on the costing.

In addition, policy costing requests should be received by the Secretaries no later than 5.30 pm on the sixth business day prior to polling day for the election (that is, Thursday in the penultimate week before the election), to enable the public release of the policy costings by 5.30 pm on the Thursday before polling day for the election. This will allow time for costings to be publicly scrutinised before polling day. Should requests be received later than the specified time, the Secretaries will endeavour to cost the policy and release the costing. However, it may not be possible to complete the costing in time for release on the Thursday before polling day for the election.<sup>17</sup> The Secretaries will send a letter and issue a press release early in the caretaker period reminding parties of the submission deadline.

### **WITHDRAWAL OF REQUESTS**

The Prime Minister, Leader of the Opposition or Leader of a minority party may withdraw a request at any time. A withdrawal by the Prime Minister must be in writing to the Secretaries. A written withdrawal by the Leader of the Opposition or Leader of a

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<sup>16</sup> Appendix C contains a pro-forma of the information normally required to complete a costing.

<sup>17</sup> See subclause 31(3) of Schedule 1 to the Charter.

minority party is to be given to the Prime Minister, who will then notify the Secretaries of the withdrawal. The responsible Secretary will issue a press release as soon as practicable after receiving notice of the withdrawal and no later than the close of business on the last business day before polling day.

Policy costings may also be deemed withdrawn by the responsible Secretary.<sup>18</sup> Where a policy costing is not possible, the Secretaries will issue a press release, as soon as practicable and no later than the close of business on the last business day before polling day, stating reasons why the policy cannot be costed.

Where the caretaker period extends past polling day, and where costing requests made after polling day cannot be completed, a similar press release will be issued as soon as practicable after the end of the caretaker period.

The non-release of a policy costing may be due to:

- time constraints that prevent the policy being costed before polling day or the end of a caretaker period;
- insufficient information about the policy to allow the Secretaries to cost it properly; or
- insufficient data available to cost the policy reliably.

Once a policy costing has been withdrawn the Secretaries are not obliged or authorised to take any further action in relation to it on or after the date of withdrawal unless it is resubmitted.<sup>19</sup>

### **Resubmission of a deemed withdrawal of a policy costing request**

Where a policy costing request has been deemed to have been withdrawn by the Secretaries under subclause 31(3) of the Charter due to insufficient information or time before polling day, and the caretaker period for that general election subsequently extends beyond polling day, the parties may re-submit the request to either the Secretaries (under clause 31A of the Charter) or to the Officer (under section 64J of the Act) so that the policy may be costed and released before the end of the caretaker period.

## **PUBLIC RELEASE OF COSTINGS**

When policy costings are to be publicly released, a copy will be provided to the Parliament House offices of the Prime Minister, the Leader of the Opposition and the Leader of a minority party. A copy of the relevant costing will be provided to the requesting party first. Shortly after the delivery of the costings, they will be publicly released on the joint Treasury/Finance election costings website, [www.electioncostings.gov.au](http://www.electioncostings.gov.au).

### **Contents of published policy costing**

When a policy costing is published, it will include:

- the costing request;
- any request for further information made by the Secretaries; and

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<sup>18</sup> Subclause 31(3) of Schedule 1 to the Charter.

<sup>19</sup> Paragraph 31(3)(c) of Schedule 1 to the Charter.

- any further information forwarded to the Secretaries or obtained in discussions with parties.<sup>20</sup>

The policy costing will also include the following:

- an outline of the specific costing methodology and assumptions used (including any economic and behavioural assumptions) in sufficient detail to allow an understanding as to how the costing was determined;
- the estimates of the policy's impact on the underlying cash balance and the fiscal balance in current dollars, as outlined in Part 2;
- an explanation detailing any significant differences between the assumptions specified in a party costing request and those used in a Treasury/Finance costing; and
- where the Secretaries consider it appropriate, a sensitivity analysis which shows the extent to which changes in assumptions could produce different costing estimates.

Appendix D outlines the pro-forma that will be used by the Secretaries when releasing a policy costing.

## **ELECTRONIC SUBMISSION AND WITHDRAWAL OF REQUESTS**

Requests and withdrawals of policy costings may be submitted electronically following the normal processes. The Prime Minister may submit written requests via email to the Secretaries. Requests from the Leader of the Opposition or Leader of a minority party may be submitted via email to the Prime Minister who may then refer it to the Secretaries. The Secretaries are not obliged or authorised to take action in relation to any request, unless the Prime Minister has referred the request to them.

Requests for further information and responses to them may also occur electronically.

## **SECURITY ARRANGEMENTS**

Security arrangements for handling of policy costings will be similar to those applied at Budget time and the confidentiality of the costings will be protected until they are publicly released.

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<sup>20</sup> Subclause 29(2) of the Charter.

## **APPENDIX A – BUDGET TREATMENT OF RELEVANT BALANCE SHEET TRANSACTIONS**

### **DRAWDOWN OF GOVERNMENT INVESTMENT FUNDS (EXCLUDING THE FUTURE FUND)**

The Government's investment funds (the Funds) (excluding the Future Fund which is addressed separately below) are reported on the Government's balance sheet as financial assets consisting of cash and investments.

These funds do not directly impact on the fiscal or underlying cash balance until a decision is made to make non-financial asset investments or grants outside the General Government Sector (GGS) from the specific fund. Earnings from the Funds have a positive impact on both the fiscal and underlying cash balance. Payments from the funds that are not classified as equity or loan principal repayments impact on both the underlying cash and fiscal balance. This is consistent with the budgetary treatment of other payments.

A decision to create a new fund involves increasing gross debt or reducing holdings of other assets, with a corresponding increase in PDI costs (or reduction in the interest earnings); wholly or partially offset by fund earnings, which will depend on the investment mandate.

A decision to close one or more of the funds would not directly result in a reduction in the underlying cash balance or fiscal balance for the Budget. This is so because either the relevant cash and investments would still be reported as assets on the balance sheet (if investments are retained) or if the remaining funds were used to reduce the borrowing requirements there would be no change to net assets. Indirectly, the underlying cash and fiscal balances will be impacted by closing the fund to the extent that any reduction in PDI is larger or smaller than the reduction in earnings from the Funds.

Where a decision is taken to close a fund, or reprioritise expenditure from a fund, the costing would consider the viability of effectively revoking grant payments that have been publicly committed or those set out in contractual arrangements. These projects are often very difficult and/or expensive to unwind and this may affect the quantum available, if any, as a save from the closure of the relevant fund.

#### **Example: Implications for the Budget of a Government investment fund (hypothetical)**

The Government decides to set up a \$1 billion Fund to invest in a variety of projects across the country. The Fund is a separately administered financial asset instead of being aggregated into cash reserves or other financial assets. The initial establishment of the Fund will have no impact on the fiscal or underlying cash balance as no payment or flow of receipts results from this decision.

Any costs associated with the management of the Fund would be recorded as an expense/payment and any interest earnings on the funds would be recorded as revenue/receipt inflows (noting that any borrowings required to establish a fund's balance would lead to an increase in public debt interest outlays). Both would therefore impact on the fiscal and underlying cash balance.

The next year the Government decides to spend \$600 million over two years on projects. These grants would be recorded as an expense/payment in the relevant years, and would impact on the fiscal and underlying cash balance. The following year the

Government decides to spend \$300 million over three years on additional projects. These grants would also affect the fiscal and underlying cash balance.

The Government decides to close the Fund with \$100 million remaining. The \$100 million will continue to be reported as a financial asset (assuming it is held in cash and not used to reduce borrowing), with no direct impact on the fiscal and underlying cash balance.

| \$ million  | FB/UCB<br>Yr 1 | FB/UCB<br>Yr 2 | FB/UCB<br>Yr 3 | FB/UCB<br>Yr 4 | FB/UCB<br>Yr 5 | Total<br>FB/UCB<br>impact | Financial<br>assets total |
|---|----------------|----------------|----------------|----------------|----------------|---------------------------|---------------------------|
| Fund established —<br>recorded as distinct asset                      | 0.0            | 0.0            | 0.0            | 0.0            | N/A            | 0.0                       | 1,000.0                   |
| Commit to \$600m of<br>projects / 2yrs                                | N/A            | -300.0         | -300.0         | 0.0            | 0.0            | -600.0                    | 400.0                     |
| Commit to \$300m of<br>projects / 3yrs                                | N/A            | N/A            | -100.0         | -100.0         | -100.0         | -300.0                    | 100.0                     |
| Close Fund — assets<br>reported in total assets but<br>not separately | N/A            | N/A            | N/A            | 0.0            | 0.0            | 0.0                       | 100.0                     |

Note: Depending on the timing of payments, fiscal balance and underlying cash balance may or may not be equivalent in individual years. This example does not include the costs of setting up the fund or any interest earnings in the fiscal and underlying cash balance numbers.

## FUTURE FUND

The general principles applying to the investment funds (above) also apply to the Future Fund. The total balance of the Future Fund is reported on the Government's balance sheet as financial assets consisting of cash and investments.

From 1 July 2020, the net earnings of the Future Fund have been included in the underlying cash balance, as from this date, consistent with *Future Fund Act 2006*, the Fund can be drawn down if a government so determines to meet superannuation payments. The current Government's policy is to defer drawing down from the Future Fund until at least 2026-27.

## LOANS

Loans, as financial assets, do not have a direct impact on the underlying cash balance. However, there will be an impact on the underlying cash balance and fiscal balance as a result of net interest costs.

Interest repayments on loans have a positive impact on the underlying cash balance and fiscal balance, which will either be partially, wholly or more than (depending on the relative interest rates of the loan and Commonwealth financing costs) offset by the PDI costs associated with any debt raised to fund the proposal.

The repayment of loan principal will have no direct net impact on the underlying cash balance as it is replacing one financial asset (a loan) with another (cash). It must be probable that the funds will be repaid for the full payment to be considered a loan.

### Commercial loans

If loans are made by the Government on terms equivalent to those that the borrower could obtain in the marketplace then these loans would be treated as commercial loans.

Such loans will typically have an overall positive impact on the underlying cash balance and fiscal balance as any PDI costs (or interest earnings foregone) would be less than the interest repayments. Net Debt is not affected by the Government's provision of a Commercial Loan as the debt incurred from providing the loan is offset by the increase in financial assets.

As the loan is a financial asset transaction, the direct effect on the level of PDI will be costed with the proposal. The second round effects of such loans on public debt interest rates as a result of increasing risk on the Commonwealth's balance sheet would not normally be costed.

### **Concessional loans**

If loans are made by the Government at more favourable terms than the borrower could obtain in the marketplace, then these loans would be treated as concessional loans. The concession provided may be in the form of lower market interest rates, longer loan maturity or grace periods before the payment of the principal and/or interest.

The concessional component of these loans (that is, the opportunity cost of the value forgone in providing the loan at a discounted rate) will have an upfront negative impact on fiscal balance and net debt. These impacts are unwound as loan repayments are received over the life of the loan, which has a positive impact on revenue, fiscal balance and net debt.

Whether or not such loans have an overall positive impact on the underlying cash balance, fiscal balance and net debt will depend on the extent of the concession. In some cases, the PDI costs (or reduction in interest earnings) associated with the financing of these proposals will exceed the total amount of the interest repayments.

The non-concessional component of the loan will be treated as a financial asset on the Government's balance sheet. Both the borrowing, or reduction in financial assets, and loan are included in the calculation of net debt and net debt will be increased by the concessional component of the loan. As with commercial loans, the effect the concessional loan has on the level of PDI would be included in the costing.

## **INVESTMENTS IN ENTITIES OUTSIDE THE GENERAL GOVERNMENT SECTOR**

The Government may also make investments in entities outside the general government sector. Government owned commercial corporations that produce goods and services are referred to as a Public Non-Financial corporations while corporations mainly engaged in financial intermediation and provision of auxiliary financial services are referred to as Public Financial corporations.

An entity is a public corporation if it meets all of the following criteria:

- it operates under the Government's control. Control is defined by the ability to determine general corporate policy by appointing appropriate directors. This is generally determined by holding more than 50 per cent of the shares of the entity. However, the Commonwealth may also obtain control of an entity with less than a 50 per cent holding by way of legislative or regulatory powers;
- it produces goods and services or provides financial services for sale in the market; and



- it provides such goods and services on a commercial basis, and is funded largely by the sale of these goods and services.

Investments into these corporations can take the form of an equity injection or a loan.

An investment would be regarded as an equity injection if the Government exercises control over the investment, such as being able to sell its investment without unreasonable impediments and there is reasonable expectation of recovery of the investment. Therefore, the entity must be able to generate a revenue stream that at least covers its costs and generates a real rate of return (i.e. above the long-term inflation target).

An equity injection from the Government to a corporation would have no direct impact on the underlying cash and fiscal balances as it is a financial investment. There would be an ongoing indirect impact on the underlying cash and fiscal balances reflecting the difference between dividends received from the corporation and the interest paid by the Government on borrowings to finance the equity injection (or forgone interest if financed from an asset). The equity injection would be treated as a financial asset on the Government's balance sheet. As equity is not a net debt asset, net debt will increase reflecting borrowings or lower cash reserves.

A loan would be treated in the way as discussed above. A payment to a corporation would only classify as funding as a loan where there is a contractual arrangement covering the loan period and interest rates. There should be a reasonable expectation that the funds would be repaid and the corporation can service the loan, otherwise it will be classified as a grant. A grant from the Government to the corporation would reduce fiscal balance and the underlying cash balance directly when paid.

## **GUARANTEES**

A guarantee is a promise by the Commonwealth to reimburse a lender if a borrower defaults. Contractual guarantees are financial liabilities with an impact on the fiscal balance, and net and gross debt (and underlying cash balance when paid). If a payment is probable for a contractual guarantee it has an impact on the underlying cash balance in the year the payment is expected.

Non-contractual (e.g. legislated) guarantees are liabilities if they are reliably measurable and it is probable that a payment will be made. Liabilities have an impact on the fiscal balance, and net and gross debt. As with contractual liabilities, if a payment is probable for a non-contractual guarantee it has an impact on the underlying cash balance in the year the payment is expected.

If the Government charges a fee to the recipient for providing the guarantee (known as a guarantee fee), those fees improve the underlying cash balance, fiscal balance and net and gross debt.

Where the financial impacts of a guarantee are unable to be quantified, the guarantee would still be disclosed in the Budget papers in the Statement of Risks.

## **APPENDIX B – COMMONLY USED TERMS**

Policy costings often make reference to common terms that arise in the context of budget updates published either outside of the caretaker period or in the PEFO. This Appendix seeks to aid understanding of these terms.

### **Measures**

Measures are defined as decisions of the Government that have a real or potential impact on the fiscal and underlying cash balances in the current year, forward estimates period, or beyond. Measures can comprise:

- new policy decisions;
- changes to, or the extension of, existing policy; and
- alterations to eligibility criteria or assistance rates (other than by legislated indexation).

Measures are classified as expense, capital or revenue, and can include both spending and saving components. Measures are either ongoing or terminating. Ongoing measures continue indefinitely (until a decision is made to cease or alter the program). Terminating measures end on a date set out in the initial policy and a further decision is required to continue the program beyond this date.

### **Contingency Reserve**

The Contingency Reserve (CR) is an allowance, included in aggregate expenses, principally to reflect anticipated events that cannot be assigned to individual programs in the preparation of the budget estimates. The CR is designed to ensure that aggregate budget estimates are based on the best information available, and are as close as possible to expected outcomes at the time of the release of an economic and fiscal outlook. The CR is not a general policy reserve.

Allowances included in the CR are not appropriated and can only be drawn upon once the relevant appropriation legislation has been passed by Parliament. These allowances are removed from the CR and allocated to specific entities for appropriation closer to the time when the anticipated events eventuate.

In addition to allowances for anticipated events, the CR may also include: measures that reflect decisions taken but not yet announced by the Government, Government decisions that were either made too late in the estimates process for inclusion against individual entity estimates, or are commercial-in-confidence or national-security-in-confidence and therefore cannot be disclosed explicitly in portfolio estimates.

### **Conservative Bias Allowance**

One of the largest components of the CR is the conservative bias allowance (CBA). This is an allowance for the tendency for estimates of expenses for existing Government policy to be revised upwards over time. This is of particular importance for demand driven programs where precise cost estimates are difficult.

The allowance is set as a percentage of total general government sector expenses (excluding GST payments to the States). The rates applied across the Budget and forward estimates are reviewed periodically by Treasury and Finance. The CBA is

reduced for earlier forward estimate years as program estimates are progressively updated, thereby decreasing the bias.

Drawdowns (which are reflected as reductions) of the conservative bias allowance are treated as parameter variations and are consistent with long standing practice. Such adjustments do not realise any actual budgetary savings, nor offset Government spending measures, as the CBA is always reduced to zero prior to the commencement of the budget year. That is, the CBA does not affect the accrual level of government spending – it is only a device to improve the accuracy of the forward estimates.

### **Other allowances that may be included in the CR**

Allowances may also be made for other anticipated events including for:

- underspends in the current financial year reflecting the tendency of budgeted expenses for some bodies or functions not to be met;
- programs that are yet to be renegotiated with State and Territory governments;
- economic parameter revisions on the budget and forward estimates received too late in the process to be allocated to individual entities or functions; and
- events and pressures that are reasonably expected to affect the budget estimates.

## APPENDIX C – PRO-FORMA REQUEST FOR COSTING AN ELECTION COMMITMENT<sup>21</sup>

| Name of policy   |  |
|--|--|
| Person requesting costing<br>(Prime Minister/Leader of the Opposition/Leader of a minority party):   |  |
| Date of public release of policy:  |  |
| Link to the publicly released policy:  |  |
| Date of request to cost the policy:  |  |
| Summary of policy (please attach copies of relevant policy documents):   |  |
| Intention of policy:   |  |
| Certification that this, or a substantially similar costing request, has not been submitted to the Parliamentary Budget Office:  |  |
| <b>Description of policy</b> ( <i>note: where the request to cost a proposal differs from the announced policy, the costing will be on the basis of information provided in the costing request</i> )  |  |
| <b>What are the key assumptions that have been made in the policy including:</b>   |  |
| Is the policy part of a package?<br><i>If yes, list and outline components and interactions with proposed or existing policies.</i>  |  |
| Where relevant, is funding for the policy to be demand driven or a capped amount?  |  |
| Will third parties (for instance the States/Territories) have a role in funding or delivering the policy?<br><i>If yes, is the Australian Government contribution capped, with additional costs to be met by third parties, or is another funding formula envisaged?</i> |  |
| Are there associated savings, offsets or expenses?<br><i>If yes, please provide details.</i>   |  |

<sup>21</sup> An electronic version of this pro-forma can be found at [www.electioncostings.gov.au/templates](http://www.electioncostings.gov.au/templates).

**Description of policy** (note: where the request to cost a proposal differs from the announced policy, the costing will be on the basis of information provided in the costing request)

**What are the key assumptions that have been made in the policy including:**  
(continued)

Does the policy relate to a previous budget measure?

*If yes, which measure?*

If the proposal would change an existing measure, are savings expected from the departmental costs of implementing the program? Will funding/cost require indexation?

*If yes, list factors used.*

What are the estimated costs each year? Are these provided on a cash or fiscal basis?

Are the revenue and/or expense costs likely to be significantly different beyond the forward estimates period?

*If yes, why?*

What assumptions have been made in deriving the expected financial impact in the party costing (please provide information on the data sources used to develop the policy)?

Has the policy been costed by a third party?

*If yes, can you provide a copy of this costing and its assumptions?*

What is the expected community impact of the policy?

How many people or businesses will be affected by the policy?

What is the likely take up?

What is the basis for these impact assessments/assumptions?

*Note: it will be up to the professional judgment of the relevant Secretary as to whether these assumptions are adopted in a Treasury or Finance costing of the policy.*

|   |  |
|---|--|
| <b>Administration of policy</b>   |  |
| Who will administer the policy (for example, Australian Government entity, the States, non-government organisation, etc.)?  |  |
| Should departmental expenses associated with this policy be included in this costing?<br><i>If no, will the Australian Government Entity be expected to absorb expenses associated with this policy?</i><br><i>If yes, please specify the key assumptions, including whether departmental costs are expected with respect to program management (by policy agencies) and additional transactions/processing (by service delivery agencies).</i> |  |
| Intended date of implementation.  |  |
| Are there transitional arrangements associated with policy implementation?  |  |
| Will the policy be ongoing or terminating*?   |  |
| If terminating:<br>What is the intended date of termination?<br>Are there any transitional arrangements associated with the conclusion of the policy?   |  |
| List major data sources utilised to develop policy (for example, ABS cat. no. 3201.0).  |  |
| Are there any other assumptions that need to be considered?   |  |

\* Ongoing policies continue indefinitely (until a decision is made to cease or alter the program). Terminating measures end on a date set out in the initial policy and a further decision is required to continue the program beyond this date.

## APPENDIX D – PRO-FORMA PUBLIC RELEASE OF COSTING<sup>22</sup>



### PUBLIC RELEASE OF (INSERT YEAR) ELECTION COMMITMENT COSTING

|  |  |
|--|--|
| <b>Name of proposal costed:</b>                              |  |
| <b>Costing Identifier:</b>                                   |  |
| <b>Summary of costing:</b>                                   |  |
| <b>Ongoing or Terminating (including date)<sup>(a)</sup></b> |  |
| <b>Person making the request:</b>                            |  |
| <b>Date costing request received:</b>                        |  |
| <b>Date of public release of policy:</b>                     |  |
| <b>Date costing completed:</b>                               |  |
| <b>Additional information requested (including date):</b>    |  |
| <b>Additional information received (including date):</b>     |  |

(a) Ongoing policies continue indefinitely (until a decision is made to cease or alter the program). Terminating measures end on a date set out in the initial policy and a further decision is required to continue the program beyond this date.

#### Financial implications (outturn prices)<sup>(b)</sup>

| Impact on                           | 20xx-xx | 20xx-xx | 20xx-xx | 20xx-xx | 20xx-xx |
|-------------------------------------|---------|---------|---------|---------|---------|
| Underlying Cash Balance (UCB) (\$m) |         |         |         |         |         |
| Fiscal Balance (\$m)                |         |         |         |         |         |

(b) A positive number for the fiscal balance indicates an increase in revenue or a decrease in expenses or net capital investment in accrual terms. A positive number for the UCB indicates an increase in revenue or a decrease in expenses or net capital investment in cash terms.

<sup>22</sup> An electronic version of this pro-forma can be found at [www.electioncostings.gov.au/templates](http://www.electioncostings.gov.au/templates).

|  |
|--|
| <p><b>Where relevant, state that the proposal has been costed as a defined or specified amount.</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p>  |
| <p><b>Where relevant, include separate identification of revenue and expense components.</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p>   |
| <p><b>Where appropriate, include a range for the costing or sensitivity analysis.</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p>  |
| <p><b>Qualifications to the costing (including reasons for the costing not being comprehensive).</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p>   |
| <p><b>Where relevant, explain effects of departmental expenses.</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p>  |
| <p><b>Where relevant, explain the reason for any significant differences between the assumptions specified in a party costing request and those used in a Treasury or Finance costing.</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p>   |
| <p><b>Other comments (<i>including reasons for significant differences between the estimated impact on the fiscal and underlying cash balances</i>).</b></p> <p><b>Where relevant, include an explanation of the medium-term implications of the proposal.<sup>(c)</sup></b></p> <p>&lt;Insert text or 'Not applicable'.</p> |

(c) Information on the medium term implications will be provided if the cost of the policy is expected to be significantly different beyond the forward estimates period. The medium term is considered to be the 7 years after the current forward estimates

|   |
|---|
| <p><b>Background information</b></p> <p><b>Costing methodology used:</b></p> <p>&lt;Insert text using headings below or insert 'Not applicable' and remove the headings&gt;</p> <ul style="list-style-type: none"> <li>• <b>Costing techniques.</b></li> <li>• <b>Policy parameters.</b></li> <li>• <b>Statistical data used.</b></li> </ul> <p><b>Behavioural assumptions used (as appropriate):</b></p> <p>&lt;Insert text or insert 'Not applicable'&gt;</p> |
|---|