

DEFENCE

CHAPTER SEVEN BUDGETED FINANCIAL STATEMENTS

BUDGETED FINANCIAL STATEMENTS

Budgeted Statement of Financial Performance

Budgeted Statement of Financial Position

Budgeted Statement of Cash Flows

Capital Budget Statement

Non-Financial Assets - Summary of Movement

**Schedule of Budgeted Revenues and Expenses Administered
on Behalf of Government**

**Schedule of Budgeted Assets and Liabilities Administered
on Behalf of Government**

Schedule of Budgeted Administered Cash Flows

Notes to the Budgeted Financial Statements

Table 7.1: Budgeted Statement of Financial Performance⁽¹⁾

2004-05 Projected Result		2005-06 Previous Estimate	2005-06 Budget Estimate	Variation	2006-07 Forward Estimate	2007-08 Forward Estimate	2008-09 Forward Estimate
\$'000		\$'000	\$'000	%	\$'000	\$'000	\$'000
REVENUES							
15,808,399	Appropriations from Government	15,299,062	15,977,721	4.4	16,019,324	16,859,110	17,302,046
262,789	Sales of goods and services	261,074	186,682	-28.5	189,900	193,628	196,904
-	Interest	-	-	-	-	-	-
142,680	Revenue from asset sales	40,000	95,063	137.7	5,792	5,108	4,410
-	Net gain on foreign exchange	-	-	-	-	-	-
600,000	Assets now recognised	100,000	30,000	-70.0	12,500	-	-
72,046	Other	50,434	186,159	269.1	189,030	192,624	197,478
16,885,914	Total revenues	15,750,570	16,475,625	4.6	16,416,546	17,250,470	17,700,838
EXPENSES							
6,592,915	Employees	6,824,772	6,587,528	-3.5	6,715,586	7,079,248	7,753,641
5,967,209	Suppliers	5,878,121	6,946,746	18.2	6,783,916	7,182,546	6,856,493
1,266	Grants	1,275	1,275	-	1,301	1,327	2,246
3,134,337	Depreciation and amortisation	2,844,827	2,771,838	-2.6	2,829,735	2,925,358	3,028,104
800,000	Write-down of assets	130,000	60,000	-53.8	47,500	30,000	30,000
142,680	Value of assets sold	40,000	95,063	137.7	5,792	5,108	4,410
-	Other	-	-	-	-	-	-
16,638,407	Total expenses	15,718,995	16,462,450	4.7	16,383,830	17,223,587	17,674,894
31,446	Borrowing cost expense	32,075	32,075	-	32,716	26,883	25,944
216,061	Net operating result	(500)	(18,900)	3,680.0	-	-	-
EQUITY INTEREST							
36,612,889	Accumulated surpluses at 1 July	38,297,280	38,738,194	1.2	33,867,354	33,978,924	34,096,634
38,738,194	Total available for appropriation	38,399,260	33,867,354	-11.8	33,978,924	34,096,634	34,096,634
	Change in accounting policy						
	Capital withdrawal						
38,738,194	Accumulated surpluses as at 30 June	38,399,260	33,867,354	-11.8	33,978,924	34,096,634	34,096,634

Note

1. Cross-reference to Table 2.8 in Chapter Two – Resourcing.

Table 7.2: Budgeted Statement of Financial Position⁽¹⁾

2004-05 Projected Result \$'000	2005-06 Previous Estimate \$'000	2005-06 Budget Estimate \$'000	Variation \$'000	2006-07 Forward Estimate \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000
ASSETS						
Financial assets:						
87,584	87,584	77,584	-11.4	77,584	77,584	77,584
906,785	769,699	787,252	2.3	743,609	679,486	602,117
994,369	857,283	864,836	0.9	821,193	757,070	679,701
Non-financial assets:						
9,943,336	9,830,668	9,894,468	0.6	9,838,616	9,779,975	9,715,903
36,078,454	37,211,919	34,681,656	-6.8	34,163,418	33,792,696	33,832,538
254,313	234,129	131,592	-43.8	129,432	127,363	125,285
26,010	26,010	26,010	-	26,010	26,010	26,010
4,519,866	4,583,100	-	-100.0	-	-	-
689,681	689,681	2,345,795	240.1	4,541,137	6,693,640	8,848,849
51,511,660	52,575,507	47,079,521	-10.5	48,698,613	50,419,684	52,548,585
52,506,029	53,432,790	47,944,357	-10.3	49,519,806	51,176,754	53,228,286
LIABILITIES						
Debt:						
354,336	339,856	339,856	-	324,436	308,076	290,776
354,336	339,856	339,856	-	324,436	308,076	290,776
Provisions and payables						
1,912,764	2,044,994	1,754,288	-14.2	1,697,876	1,617,808	1,645,257
1,017,313	1,017,313	448,489	-55.9	471,823	495,157	518,491
407,723	407,723	407,723	-	407,723	407,723	407,723
3,337,800	3,470,030	2,610,500	-24.8	2,577,422	2,520,688	2,571,471
3,692,136	3,809,886	2,950,356	-22.6	2,901,858	2,828,764	2,862,247
48,813,893	49,622,904	44,994,001	-9.3	46,617,948	48,347,990	50,366,039
EQUITY						
1,899,469	3,047,414	2,950,417	-3.2	4,462,794	6,075,126	8,093,175
8,176,230	8,176,230	8,176,230	-	8,176,230	8,176,230	8,176,230
38,738,194	38,399,260	33,867,354	-11.8	33,978,924	34,096,634	34,096,634
48,813,893	49,622,904	44,994,001	-9.3	46,617,948	48,347,990	50,366,039
Represented by:						
1,940,881	1,975,139	1,772,256	10.3	1,830,496	1,891,745	1,967,580
50,565,148	51,457,651	46,172,101	10.3	47,689,310	49,285,009	51,260,706
2,244,886	2,316,480	1,793,870	22.6	1,764,382	1,719,940	1,740,298
1,447,250	1,493,406	1,156,480	22.6	1,137,476	1,168,824	1,121,949

Note

1. Cross-reference to Table 2.9 in Chapter Two – Resourcing.

Table 7.3: Budgeted Statement of Cash Flows⁽¹⁾

2004-05 Projected Result \$'000		2005-06 Previous Estimate \$'000	2005-06 Budget Estimate \$'000	Variation %	2006-07 Forward Estimate \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000
OPERATING ACTIVITIES							
15,808,399	Appropriations from Government	15,299,062	15,977,721	4.4	16,019,324	16,859,110	17,302,046
285,389	Sales of goods and services	278,144	196,660	-29.3	200,004	203,932	207,388
-	Interest	-	-	-	-	-	-
886,389	Net GST refund	873,761	287,007	-67.2	296,921	314,384	316,168
70,046	Other	48,434	184,659	281.3	187,530	191,124	195,978
248,537	Cash transfer from Official Public Account (receivables)	55,100	34,681	-37.1	43,643	64,123	77,369
17,298,760	Total cash received	16,554,501	16,680,728	0.8	16,747,422	17,632,673	18,098,949
6,678,223	Employees	6,781,449	6,523,786	-3.8	6,660,428	7,041,606	7,726,192
6,088,583	Suppliers	5,970,859	7,282,131	22.0	7,281,256	7,613,212	7,324,889
1,266	Grants	1,275	1,275	-	1,301	1,327	2,246
109,276	Inventory	111,713	-	-100.0	-	-	-
31,446	Other	32,075	32,075	-	32,716	26,883	25,944
378,278	Cash transfer to Official Public Account (receivables)	-	-	-	-	-	-
13,287,072	Total cash used	12,897,371	13,839,267	7.3	13,975,701	14,683,028	15,079,271
4,011,688	NET CASH FROM/(TO) OPERATING ACTIVITIES	3,657,130	2,841,461	-22.3	2,771,721	2,949,645	3,019,678
INVESTING ACTIVITIES							
Cash received:							
142,680	Proceeds from sales of property, plant and equipment	40,000	95,063	137.7	5,792	5,108	4,410
142,680	Total cash received	40,000	95,063	137.7	5,792	5,108	4,410
Cash used:							
3,069,680	Purchase of specialist military equipment	3,361,372	3,407,930	1.4	3,807,755	4,109,488	4,571,845
614,541	Purchase of property, plant and equipment	597,404	565,062	-5.4	466,715	441,237	452,992
731,310	Inventory purchases	747,614	-	-100.0	-	-	-
4,415,531	Total cash used	4,706,390	3,972,992	-15.6	4,274,470	4,550,725	5,024,837
(4,272,851)	NET CASH FROM/(TO) INVESTING ACTIVITIES	(4,666,390)	(3,877,929)	-16.9	(4,268,678)	(4,545,617)	(5,020,427)
FINANCING ACTIVITIES							
Cash received:							
393,286	Equity appropriation	1,023,740	1,121,148	9.5	1,512,377	1,612,332	2,018,049
393,286	Total cash received	1,023,740	1,121,148	9.5	1,512,377	1,612,332	2,018,049
Cash used:							
13,607	Repayments of debt	14,480	14,480	-	15,420	16,360	17,300
-	Capital use charge	-	-	-	-	-	-
268,741	Capital withdrawal	-	70,200	-	-	-	-
282,348	Total cash used	14,480	84,680	484.8	15,420	16,360	17,300
110,938	NET CASH FROM/(TO) FINANCING ACTIVITIES	1,009,260	1,036,468	2.7	1,496,957	1,595,972	2,000,749
(150,225)	Net increase/(decrease) in cash held	-	-	-	-	-	-
237,809	Cash at 1 July	87,584	87,584	-	77,584	77,584	77,584
-	Opening Balance Transfer to DMO	-	-10,000	-	-	-	-
87,584	CASH AT 30 JUNE	87,584	77,584	-11.4	77,584	77,584	77,584

Note

1. Cross-reference to Table 2.10 in Chapter Two – Resourcing.

Table 7.4: Capital Budget Statement

2004-05 Projected Result \$'000		2005-06 Previous Estimate \$'000	2005-06 Budget Estimate \$'000	Variation %	2006-07 Forward Estimate \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000
CAPITAL EXPENDITURE							
3,069,680	Purchase of specialist military equipment	3,361,372	3,407,930	1.4	3,807,755	4,109,488	4,571,845
614,541	Purchase of property, plant and equipment	597,404	565,062	-5.4	466,715	441,237	452,992
3,684,221	Total capital payments	3,958,776	3,972,992	0.4	4,274,470	4,550,725	5,024,837
Funded from:							
393,286	Equity injection	1,023,740	1,121,148	9.5	1,512,377	1,612,332	2,018,049
3,210,055	Operating receipts	2,895,036	2,826,981	-2.4	2,756,301	2,933,285	3,002,378
80,880	Net capital receipts	40,000	24,863	-37.8	5,792	5,108	4,410
3,684,221	Total capital funding	3,958,776	3,972,992	0.4	4,274,470	4,550,725	5,024,837
CAPITAL RECEIPTS							
-	Proceeds from the sale of specialist military equipment	-	-	-	-	-	-
142,680	Proceeds from sales of property, plant and equipment	40,000	95,063	137.7	5,792	5,108	4,410
-	Other capital receipts	-	-	-	-	-	-
61,800	Less: capital withdrawal	-	70,200	-	-	-	-
80,880	NET CAPITAL RECEIPTS	40,000	24,863	-37.8	5,792	5,108	4,410

Table 7.5: Non-financial Assets – Summary of Movement

Revised Budget Year 2005-06	Land	Buildings	Other IP&E	Specialist Military Equipment	Software	Other Intangibles	Heritage and Cultural	Total
	\$'000	\$'000	%	\$'000	\$'000	\$'000	\$'000	\$'000
GROSS VALUE								
Gross value as at 30 June 2005	2,654,167	10,365,600	56,436,990	8,176,042	299,881	158,589	26,010	78,117,279
Gross value – additions	-	225,349	3,407,930	337,960	-	1,753		3,972,992
Gross value – revaluations								-
Gross value – disposals				-95,063				-95,063
Gross value – write offs			-60,000					-60,000
Gross value – adjustments			-2,206,135	-317,772	-42,301	-78,270		-2,644,478
Gross value – other movements			30,000					30,000
Gross value –as at 30 June 2006	2,654,167	10,590,949	57,608,785	8,101,167	257,580	82,072	26,010	79,320,730
								-
ACCUMULATED DEPRECIATION/AMORTISATION								
Accumulated depreciation/amortisation as at 30 June 2005	-	3,076,431	25,449,323	3,085,255	119,551	84,606	-	31,815,166
Depreciation/amortisation on assets held at beginning of the year		274,217	2,131,863	361,855	3,842	61		2,771,838
Accumulated depreciation/amortisation on assets disposed through year								
Accumulated depreciation/amortisation as at 30 June 2006	-	3,350,648	27,581,186	3,447,110	123,393	84,667	-	34,587,004
Net book value 30 June	2,654,167	7,240,301	30,027,599	4,654,057	134,187	(2,595)	26,010	44,733,726

Table 7.6: Schedule of Budgeted Revenues and Expenses Administered on Behalf of Government

2004-05 Projected Result \$'000		2005-06 Previous Estimate \$'000	2005-06 Budget Estimate \$'000	Variation %	2006-07 Forward Estimate \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000
	Revenues administered on behalf of Government						
55,100	Interest and dividends	15,276	17,776	16.4	21,579	27,689	27,689
678,405	Other	686,475	683,975	-0.4	682,475	682,475	682,475
733,505	Total revenues administered on behalf of Government	701,751	701,751	-	704,054	710,164	710,164
	Expenses administered on behalf of Government						
2,429,100	Military benefits	2,530,100	2,530,100	-	2,530,100	2,630,100	2,630,100
9,250	Subsidies	9,250	9,250	-	9,250	9,250	9,250
-	Other	-	-	-	-	-	-
2,438,350	Total expenses administered on behalf of Government	2,539,350	2,539,350	-	2,539,350	2,639,350	2,639,350

Table 7.7: Schedule of Budgeted Assets and Liabilities Administered on Behalf of Government

2004-05 Projected Result \$'000		2005-06 Previous Estimate \$'000	2005-06 Budget Estimate \$'000	Variation %	2006-07 Forward Estimate \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000
	Assets administered on behalf of Government						
-	Cash	-	-	-	-	-	-
1500	Receivables	4,369	1000	-77.1	500	-	-
1,258,883	Investments	1,258,883	1,258,883	-	1,258,883	1,258,883	1,258,883
100,000	Non-financial assets	95,000	105,000	10.5	110,000	115,000	120,000
1,360,383	Total assets administered on behalf of Government	1,358,252	1,364,883	0.5	1,369,383	1,373,883	1,378,883
	Liabilities administered on behalf of Government						
30,100,000	Military benefits	31,000,000	31,000,000	-	32,000,000	33,000,000	34,000,000
-	Other	-	5,000	-	5,000	5,000	5,000
30,100,000	Total liabilities administered on behalf of Government	31,000,000	31,005,000	0.0	32,005,000	33,005,000	34,005,000
	Represented by:						
1,500	Current assets	4,369	1,000	-77.1	500	-	-
1,358,883	Non-current assets	1,353,883	1,363,883	0.7	1,368,883	1,373,883	1,378,883
-	Current liabilities	-	-	-	-	-	-
30,100,000	Non-current liabilities	31,000,000	31,005,000	0.0	32,005,000	33,005,000	34,005,000

Table 7.8: Schedule of Budgeted Administered Cash Flows

2004-05 Projected Result \$'000		2005-06 Previous Estimate \$'000	2005-06 Budget Estimate \$'000	Variation %	2006-07 Forward Estimate \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000
OPERATING ACTIVITIES							
Cash received:							
1,407,779	Cash from the Official Public Account	1,639,350	1,625,981	-0.8	1,543,850	1,643,850	1,644,350
55,100	Interest and dividends	15,276	17,776	16.4	21,579	27,689	27,689
678,405	Other	696,475	683,975	-1.8	682,475	682,475	682,475
2,141,284	Total cash received	2,351,101	2,327,732	-1.0	2,247,904	2,354,014	2,354,514
Cash used:							
1,398,529	Military benefits	1,630,100	1,616,731	-0.8	1,534,600	1,634,600	1,635,100
9,250	Subsidies	9,250	9,250	-	9,250	9,250	9,250
733,505	Cash to the Official Public Account	701,751	701,751	-	704,054	710,164	710,164
-	Other	-	-	-	-	-	-
2,141,284	Total cash used	2,351,101	2,327,732	-1.0	2,247,904	2,354,014	2,354,514
-	Net cash from/(to) operating activities	-	-	-	-	-	-
-	Net (decrease)/increase in cash held:	-	-	-	-	-	-
-	Cash at the beginning of the reporting period	-	-	-	-	-	-
-	Cash at the end of the reporting period	-	-	-	-	-	-

NOTES TO THE BUDGETED FINANCIAL STATEMENTS

Note 1 – Key Accounting Policies

1.1 Budgeted Financial Statements Overview

Budgeted financial statements have been included to show the planned financial performance over the 2005-06 budget year, and each of the following forward years from 2006-07 to 2008-09.

Budgeted statements of financial performance, financial position and cash flows, and a budgeted capital statement are provided to show the revenues, expenses, assets, liabilities and equity of Defence. These budgeted statements contain estimates prepared in accordance with the requirements of the Government's financial budgeting and reporting framework.

Budgeted financial estimates are provided for both *departmental* and *administered* financial items. *Departmental*, or controlled, financial statements are those statements which include revenues, expenses, assets and liabilities over which Defence has discretion, responsibility and authority. Departmental financial statements represent the financial performance of Defence in delivering its outcomes.

Administered financial estimates include revenues, expenses, assets and liabilities that Defence administers on behalf of the Government, but over which Defence does not have management control. These typically include military superannuation benefits.

1.2 Comparative figures and variations

In recognition of the budget development and scrutiny process, variations identified in the budgeted financial statements are between the previous estimate for 2005-06 as provided in the *Portfolio Additional Estimates Statements 2004-05* and the budget estimate for 2005-06, unless otherwise noted. The projected result for 2004-05 is also included in these budgeted financial statements for comparative purposes.

1.3 Rounding

Unless otherwise stated, the convention used in these budgeted financial statements is to round amounts to the nearest \$'000. Totals are the sum of unrounded figures.

1.4 Budgeted Departmental Financial Statements and Schedule of Budgeted Administered Activity

Note that the term '*budgeted financial statements*' and '*statements*' are used interchangeably.

Under the Government's accrual-based budgeting framework, and consistent with Australian Accounting Standards, transactions that agencies control (Departmental transactions) are separately budgeted for and reported, compared to transactions that agencies do not have control over (Administered transactions). This ensures that agencies are only held fully accountable for the transactions over which they have control.

- Departmental expenses include employee and supplier expenses and other administrative costs, which are incurred by Defence in providing its goods and services.
- Administered items are revenues, expenses, assets and liabilities that are managed by Defence on behalf of the Government according to set Government directions of which Defence does not have management control. These include military superannuation contributions, payments received from the United Nations and foreign governments, bank interest and dividends paid by the Defence Housing Authority.

1.5 Appropriations in the accrual budgeting framework

Under the Government's accrual budgeting framework, separate annual appropriations are provided for:

- departmental price of outcomes appropriations (representing the Government's funding for outcomes from agencies);
- departmental capital appropriations (representing investments by the Government for either additional equity in or loans to agencies);
- administered expense appropriations (representing estimated administered expenses relating to an existing outcome, a new outcome or a Specific Purpose Payment to the states); and
- administered capital appropriations (represent increases in administered equity through funding non-expense administered payments).

Special appropriations fund the majority of payments from the Consolidated Revenue Fund (especially those that are entitlement driven or involve transfers to state and territory governments).

1.6 Basis of Accounting

The Budgeted statements have been prepared in accordance with:

- the Financial Management and Accountability Orders under the authority of section 63 of the *Financial Management and Accountability Act 1997*;
- Australian Accounting Standards and Accounting Interpretations issued by the Australian Accounting Standards Board; and
- Consensus Views of the Urgent Issues Group.

The Budgeted Statements of Financial Performance and Financial Position have been prepared on an accrual basis and are in accordance with the historic cost convention, except for certain assets which, as noted (refer to items 1.15 and 1.16), are at valuation. Except where stated, no allowance is made for the effect of changing prices on the results or financial position.

Revenues and expenses are recognised in the Statement of Financial Performance when, and only when, the flow or consumption or loss of economic benefits has occurred and can be reliably measured.

Administered revenues, expenses, assets and liabilities and cash flows reported in the Schedules of Administered Item are accounted for on the same basis and using the same policies as for departmental items, except as otherwise stated.

1.7 Changes in Accounting Policy

The accounting policies used in the preparation of these budgeted financial statements are consistent with those used in the preparation of the *Portfolio Budget Statements 2004-05*.

1.8 Revenue

Revenues from Government

Departmental outputs appropriation for the year are recognised as revenue, except for certain amounts which relate to activities that are reciprocal in nature, in which case revenue is recognised only when it has been earned.

From 2002-03, Defence elected to operate on an 'as required' draw-down basis that has resulted in undrawn appropriations that will be reflected as a receivable. This receivable is available for draw-down to meet future obligations.

Other Revenue

Revenue from the delivery of goods and the rendering of services is recognised by reference to the stage of completion of contracts or other agreements to provide goods or services. The stage of completion is determined according to the proportion that costs incurred to date bear to the estimated total costs of the transaction. Revenue from disposal of non-current assets is recognised when control of the asset has passed to the buyer.

1.9 Transactions with Government

Equity Injection

Equity injection represents an additional contribution to Defence by the Government, which is over and above the revenue from the Government for the price of outcomes. Equity injections are used entirely to fund capital expenditure.

1.10 Employee Benefits

Defence's workforce comprises two employment components: Australian Public Service (APS, ie civilians) and Australian Defence Force (ADF, ie military) personnel. Employee benefits for each workforce component are based on the relevant employment agreements and legislation.

Liabilities for services rendered by employees are recognised at the reporting date to the extent that they have not been settled.

Liabilities for wages and salaries (including non-monetary benefits), annual leave and sick leave are measured at their nominal amounts. Other employee benefits expected to be settled within 12 months of the reporting date are also measured at their nominal amounts. The nominal amount is calculated with regard to the rates expected to be paid on settlement of the liability.

Leave

The liability for employee benefits includes provision for annual leave and long service leave. No provision has been made for sick leave as all sick leave is non-vesting and the average sick leave taken in future years by employees of Defence is estimated to be less than the annual entitlement for sick leave. The leave liabilities are calculated on the basis of employees' remuneration, including Defence's employer superannuation contribution rates to the extent that the leave is likely to be taken during service rather than paid out on termination.

The liability for long service leave is determined by reference to the work of an actuary. The estimate of the value of the liability takes into account attrition rates and pay increases through promotion and inflation.

The liability for annual leave for APS employees reflects the value of total annual leave entitlements of all such employees and is recognised at the nominal amount. All annual leave for APS employees is current. The liability in respect of annual leave for ADF personnel reflects an estimate of the total value of annual leave entitlements. The liability is recognised as the best estimate of the nominal amount required to settle the obligation as at the reporting date. All annual leave for ADF is current.

Superannuation

Permanently-appointed APS employees and Defence contribute to the Commonwealth Superannuation Scheme or the Public Sector Superannuation Scheme (PSS). These schemes are defined benefit superannuation plans for APS employees. No liability is shown for APS superannuation in the Statement of Financial Position as the employer superannuation contributions by Defence fully extinguish the accruing liability, which is assumed by the Commonwealth, and is reported by the Department of Finance and Administration, with the administration being conducted by ComSuper. For APS employees who are not

members of the Commonwealth Superannuation Scheme or Public Sector Superannuation Scheme, Defence makes an employer superannuation contribution to their nominated fund.

The Defence Force Retirement and Death Benefits Scheme and the Military Superannuation Benefits Scheme are defined benefit superannuation plans for ADF members. ADF employer superannuation contributions, pension payments, Defence Force Retirement and Death Benefits Scheme member contributions and the provision for unfunded superannuation are reflected in the Schedules of Administered Items

Military Workers' Compensation

The Military Rehabilitation and Compensation Bill 2003 and the Military Rehabilitation and Compensation (Consequential and Transitional Provisions) Bill 2003 passed by the Parliament on 1 April 2004, provide for the establishment of the new Military Rehabilitation and Compensation scheme. The new scheme significantly reforms the existing arrangement of two separate military compensation schemes under multiple sources of legislation including the *Veterans' Entitlements Act 1986* and the *Safety Rehabilitation and Compensation Act 1988*. Effective from 1 July 2004, the Department of Veterans' Affairs is the single administrative body for all forms of ADF compensation under the old and the new schemes.

Employee Workplace Agreements

As a result of workplace agreements in place for Defence employees, a number of pay increases for both APS and ADF personnel are due to be paid in ensuing years. The current military agreement is for a period of 18 months from 6 May 2004 until 3 November 2006. The remaining pay rises are 2 per cent from 2 June 2005 and 1.5 per cent from 9 March 2006. The APS Certified Agreement expires on 31 December 2006. The remaining pay rises are 2 per cent from 2 June 2005 and 2 per cent from 12 January 2006. Remuneration for executives (being members of the Senior Executive Service or equivalent) is subject to individual agreements.

1.11 Asbestos-related Disease Exposure

An inter-departmental committee chaired by the Department of Finance and Administration commissioned an actuarial study on the nature and extent of the Government's liability for Asbestos-Related Diseases. The Actuarial Assessment of the Government Asbestos-Related Disease Exposure report, which was finalised in October 2003, involved collecting extensive data on individual Government claims, modelling the various sources of claims and conducting interviews with various Government agencies involved in managing the claims.

The provision is based on the best estimate of Defence's potential exposure, consistent with the requirement of Australian Accounting Standards Board 1044, Provisions, Contingent Assets and Contingent Liabilities. In making the best

estimate of the consideration required to settle the provision, the Actuary has applied independent expertise and has used existing historical data, as well as similar claims elsewhere. The estimate represents the present value of future compensation payments on both future reported claims and currently open claims, including defendant legal costs. In the financial statements, Defence is required to present the full liability as well as disclosing the asset.

1.12 Cash

Cash means notes and coins held, as well as any deposits held at call with a bank or financial institution. Changed cash management procedures during 2002-03 required Defence to adopt an 'as required' draw-down approach to appropriations. This has reduced the amount of cash held by Defence. Undrawn appropriation is represented as a receivable from the Commonwealth.

1.13 Acquisition of Assets

Assets are recorded at cost of acquisition except as stated below. The cost of acquisition includes the fair value of assets transferred in exchange and liabilities undertaken. With the exception of specialist military equipment, assets acquired at no cost or for nominal consideration are initially recognised as assets and revenues at their fair value as at the date of acquisition, unless acquired as a consequence of restructuring of administrative arrangements. In the latter case, assets are initially recognised as contributions by owners at the amounts at which they were recognised in the transferor agency's accounts immediately prior to the restructuring.

1.14 Property, Plant and Equipment including Land, Buildings and Infrastructure

Asset Recognition Threshold

Purchases of property, plant and equipment are recognised initially at cost in the Budgeted Statement of Financial Position where they meet the capitalisation threshold. Individual items will be capitalised where the individual value is equal to or exceeds \$10,000. Grouped assets will be capitalised for items of homogenous nature within a single class where the individual item values equal or exceed \$2,000 and the class group value equals or exceeds \$50,000.

Asset valuation

From 1 July 2002, Commonwealth agencies and authorities are required to use the cost basis (for specialist military equipment and intangibles) or the fair value basis (for other, infrastructure, plant and equipment) to measure Property, Plant and Equipment. The shift from the deprival method of valuation to fair value occurred gradually over a three-year period. Fair value essentially reflects the current market value of an asset.

Revaluations

In accordance with Schedule 1 of the Financial Management and Accountability (Financial Statements 2003-2004) Orders and Australian Accounting Standards Board 1041 Revaluation of Non-Current Assets, all non-current assets are valued on the fair value basis from 1 July 2002, with the exception of specialist military equipment, which is currently valued on the basis of historical costs.

Property, plant and equipment, except for assets under construction and specialist military equipment with values greater than established revaluation thresholds, are revalued progressively in successive three-year cycles. All current progressive revaluation cycles commenced on 1 July 2002 and will conclude by 30 June 2005.

Assets within each class acquired after the valuation of the asset type in the current revaluation cycle are reported at cost for the duration of the cycle unless significant changes in the value of the asset have occurred, in which case the asset will be subject to revaluation or indexation.

Assets under construction are not revalued but are accounted for at cost. In addition to reviewing expenditures from the point of rollout into service, assets under construction expenditures are now also considered on a whole-of-life basis.

All valuations are conducted by an independent qualified valuer.

Depreciation and Amortisation

Depreciable property, plant and equipment assets are written-off to their estimated residual values over their estimated useful lives to Defence using, in all cases, the straight-line method of depreciation from the time they are first held ready for use. Leasehold improvements are amortised on a straight-line basis over the lesser of the estimated useful life of the improvements and the unexpired period of the lease.

Depreciation and amortisation rates (useful lives) and methods are reviewed at each reporting date and necessary adjustments are recognised in the current, or current and future reporting periods, as appropriate. Residual values are re-estimated for a change in prices only when assets are revalued.

Asset Disposals

The gain or loss on disposal of property, plant and equipment is determined as the difference between the carrying amount of the asset at the time of disposal and the proceeds of disposal.

New disclosure requirements from 2002-03 require the proceeds from asset sales to be separately disclosed from the net book value of assets sold. Therefore, the gross position is disclosed in the Budgeted Statement of Financial Performance.

1.15 Inventory

Defence does not ordinarily hold inventory for sale. Sales recorded represent disposal of inventory, surplus to requirements, and minor fuel sales. Inventory has been brought to account at weighted average cost since 2001-02.

Costs incurred in bringing each item of inventory (primarily explosive ordnance and general stores) to its present location and condition, that are capable of being allocated on a reasonable basis, are assigned on a weighted average cost basis.

Previously, as historic cost was not available in all instances, inventory was brought to account at average cost, replacement cost or at last purchase price.

Inventory is considered obsolete based upon the nature of current inventory levels and expected usage of such assets in the achievement of Defence's Outcomes.

1.16 Investments

Investments held on behalf of the Commonwealth are included as administered assets and are brought to account as the value of the Commonwealth's share as at 30 June 1997 of the net assets of the entity, except where there has been a return of equity to the owner (the Government). This is a requirement of the Finance Ministers' Orders. Administered investments in controlled entities are not consolidated because their consolidation is relevant only at the whole-of-government level.

1.17 Taxation

Defence's activities are exempt from all forms of taxation except fringe benefits tax and the goods and services tax (GST). Defence is able to claim input credits for goods and services tax incorporated within the costs of assets and supplies purchased by Defence.

Revenues, expenses and assets are recognised net of GST except:

- where the amount of GST incurred is not recoverable from the Australian Taxation Office (in these circumstances GST is recognised as part of the cost of acquisition of the asset or part of the item of expense); and
- for receivables and payables (which are shown inclusive of GST in the Budgeted Statement of Financial Position).

1.18 Leases

A distinction is made between finance leases which effectively transfer from the lessor to the lessee substantially all the risks and benefits incidental to ownership of leased non-current assets and operating leases under which the lessor effectively retains substantially all such risks and benefits.

Where a non-current asset is acquired by means of a finance lease, the asset is capitalised at the present value of minimum lease payments at the inception of the lease and a liability recognised for the same amount. Leased assets are amortised over the period of the lease. Operating lease payments are expensed on a basis which is representative of the pattern of benefits derived from the leased assets.

1.19 Bad and Doubtful Debts

The provision for bad and doubtful debts is based on an analysis of the expected realisation of outstanding debts and write-off experience from prior years. Bad debts are written-off as they are identified. No provision is made for the Australian Government or Foreign Government debtors as they are deemed to be collectable.

1.20 Insurance

Defence has insured for key insurable risks through the Government's insurable risk-managed fund called Comcover. Workers compensation for civilians is insured through the Government's Comcare Australia. Defence meets the benefit costs for military compensation on an emerging cost basis.

1.21 Schedule of Budgeted Administered Activities

Administered revenues, expenses, assets, liabilities and cash flows are disclosed in the Schedules of Administered Items and related notes.

Except where otherwise stated below, administered items are accounted for on the same basis and using the same policies as for departmental items, including the application to the greatest extent possible of Australian Accounting Standards, Accounting Interpretations and Urgent Issues Group Consensus Views.

Administered appropriations received or receivable from the Official Public Account are not reported as administered revenues or assets respectively. Similarly, administered receipts transferred or transferable to the Official Public Account are not reported as administered expenses or payables. These transactions or balances are internal to the Administered entity.

Accounting policies that are relevant to administered activities only of Defence are disclosed below.

Administered Revenue

All administered revenues are revenues relating to the core operating activities performed by Defence on behalf of the Commonwealth. Administered revenues comprise military superannuation contributions, payments received from the United Nations and foreign governments, bank interest and dividends paid by the Defence Housing Authority.

Administered Expenses

All administered expenses are expenses relating to the core operating activities performed by Defence on behalf of the Commonwealth. Administered expenses comprise unfunded military superannuation benefits, ADF housing subsidies, ADF retention benefits and foreign exchange losses.

Administered Investments

Each Commonwealth department is required to show an Administered investment in each *Commonwealth Authority and Company (CAC) Act 1997* entity within their portfolio. These administered investments should be valued at the Commonwealth's ownership interest in the net assets of those CAC entities, fixed at a notional acquisition date of 30 June 1997.

Military Retention Benefits

Certain categories of ADF personnel who are members of the Military Superannuation Benefits Scheme and have had 15-years of service receive retention benefits as an incentive for continued service. From 1 July 2002, retention benefit payments are recorded as prepayments instead of expenses. The change has been made to recognise the nature of these payments.

Military Superannuation

The Defence Force Retirement and Death Benefits Scheme (DFRDB) and the Military Superannuation Benefits Scheme (MSBS) are defined benefit superannuation plans for ADF members. ADF employer superannuation contribution revenue, pension and lump sum payments, the provision for unfunded DFRDB and MSBS superannuation and DFRDB member contribution revenue are reflected in the Schedules of Administered Items.

The DFRDB is a fully unfunded scheme but the MSBS is a partly-funded scheme. MSBS member contributions are paid into the MSBS fund that is controlled by the MSBS Board and are therefore not reflected in the Schedules of Administered Items. The Commonwealth on behalf of the MSBS Fund makes funded benefit payments to members of the scheme and the Commonwealth is reimbursed by the MSBS fund for these payments.

The Australian Government Actuary estimates the unfunded provisions and expected future cash flows as at 30 June each year. These estimates are reflected in the Schedules of Administered Items. The Australian Government Actuary completes a full review of the unfunded liabilities (a long-term cost report) every three years. The most recent long-term cost report was completed as at 30 June 2002. ComSuper administers MSBS and DFRDB benefit payments on behalf of Defence. These payments are made using Defence Special Appropriations.

Note 2 – Summary of Estimated Special Account Balances

Table 7.9: Summary of Estimated Special Account Balances⁽¹⁾⁽²⁾

	Opening Balance 2005-06 2004-05	Receipts 2005-06 2004-05	Payments 2005-06 2004-05	Adjustments 2005-06 2004-05	Closing Balance 2005-06 2004-05
	\$'000	\$'000	\$'000	\$'000	\$'000
Services for Other Governments and Non-Agency Bodies – <i>Financial Management and Accountability Act 1997⁽³⁾</i>	113,927 <i>93,927⁽⁴⁾</i>	100,000 <i>115,500</i>	75,000 <i>95,500</i>	-	138,927 <i>113,927</i>
Defence Endowments – <i>Financial Management and Accountability Act 1997⁽³⁾</i>	276 <i>266</i>	35 <i>45</i>	30 <i>35</i>	-	281 <i>276</i>
Fedorczenko Legacy Fund – <i>Financial Management and Accountability Act 1997⁽³⁾</i>	148 <i>151</i>	5 <i>2</i>	12 <i>5</i>	-	141 <i>148</i>
Other Trust Monies – <i>Financial Management and Accountability Act 1997⁽³⁾</i>	21,856 <i>9,356</i>	22,000 <i>29,500</i>	9,000 <i>17,000</i>	-	34,856 <i>21,856</i>
Young Endeavour Youth Program – <i>Financial Management and Accountability Act 1997⁽³⁾</i>	565 <i>878</i>	655 <i>724</i>	550 <i>1,037</i>	-	670 <i>565</i>
Total Special Accounts	136,772 <i>104,578</i>	122,695 <i>145,771</i>	84,592 <i>113,577</i>	-	174,875 <i>136,772</i>

Notes

1. 2005-06 budget in bold.
2. 2004-05 projected result in italics.
3. These are Departmental special accounts.
4. The Services for Other Governments balance includes money relating to Comcare. As Defence does not have a Ministerial determination for Comcare, it cannot be disclosed separately in this note to the financial statements.