

DEFENCE

CHAPTER SEVEN

BUDGETED FINANCIAL STATEMENTS

BUDGETED FINANCIAL STATEMENTS

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Methods of Presenting the Defence Budget

There are three main ways of presenting the Defence budget. All three methods are consistent and are used for different purposes. The Defence budget is presented below in each of the three ways.

METHOD 1: DEFENCE RESOURCING

The Defence resourcing method excludes administered appropriations, which are administered on Defence's behalf by other organisations. This method includes total funding appropriated by the Government to Defence plus net capital receipts and Defence's own-source revenue. It is based on Australian Accounting Standards (accrual basis). Method 1 is used in the Defence Portfolio Budget Statements and also in the Commonwealth Budget Paper 4 (Appropriation Bills).

The Defence resourcing method is derived as follows.

	2006-07 \$'000	Reference
Appropriation from Government for price of outputs	17,063,404	Table 2.1, Serial 1
Appropriation for equity injection	1,937,879	Table 2.1, Serial 2
Own-source revenue	594,645	Table 2.1, Serial 4
Net capital receipts	23,192	Table 2.1, Serial 5
Total Department Resourcing	19,619,120	Table 2.1, Serial 7

Method 1 is commonly used to measure movements in Defence's funding allocations against the previously agreed budget and forward estimates allocations. It is used in presenting the 2000 Defence White Paper commitment, and to compare methods in Defence funding since then.

METHOD 2: UNDERLYING CASH BALANCE IMPACT

Method 2 is the sum of Defence cash flows from operating activities and net capital investment, including both departmental and administered expenditure, and is used by the Treasury to describe the Defence budget in terms of underlying cash impact. It is a measure of spending rather than resourcing, and is an estimate of the net impact of Defence spending on the whole-of-government cash balance. This number is derived on an Australian Bureau of Statistics government finance statistics cash operating payments basis, adjusted for net proceeds of asset sales returned to the Government.

A figure of \$17,409 million is used in the Treasury budget overview and the Treasurer's budget speech and is derived as follows:

	2006-07 \$m	Reference
Underlying cash baseline	16,111	
Heavy airlift – acquisition component	792	Table 2.3, serial 15
Hardened and Networked Army – Phase 2	24	Table 2.3, serial 1
Operation Catalyst - Contribution to Multinational Force	310	Table 2.3, serial 3
Operation Slipper – Reconstruction Task Force to Afghanistan	92	Table 2.3, serial 4
Reserve Remuneration Review	36	Table 2.3, serial 5
Naval Aviation Logistics Funding	26	Table 2.3, serial 6
Enhancement of Australia's Fisheries and maritime surveillance	5	Table 2.3, serial 12
Rationalisation of the ADF Command and Control structure	-6	Table 2.3, serial 13
Broadening the Efficiency Dividend	-4	Table 2.3, serial 16
Coastal Surveillance – Increased Patrolling of Maritime Approaches	24	Table 2.3, serial 17
Total Defence Funding⁽¹⁾	17,409	

Note

1. This is an underlying cash figure provided by the Department of Finance and Administration.

The important distinction between methods 1 and 2 is that the latter approach describes estimates of spending in a cash sense, rather than appropriations from the Government which include funding for accrual items such as depreciation.

METHOD 3: DEFENCE FUNCTION

Method 3 includes only expenses that have a direct impact on the fiscal balance and excludes superannuation, which is recorded in the superannuation function. This method is derived using the Government finance statistics accrual expense approach and is used in Statement 6 of Commonwealth Budget Paper No. 1. It also includes investment in specialist military equipment but excludes depreciation of specialist military equipment and intra-government flows such as fringe benefits tax payments to the Australian Taxation Office. It is derived as follows:

	2006-07 \$m	Reference
Defence AAS expenses ⁽¹⁾	17,860	Table 7.1
DMO AAS expenses	8,749	Table
Administered expenses	56	Table 5.7.1, retention benefits + housing subsidies
Investment in specialist military equipment	4,623	Table 7.6
Specialist military equipment depreciation	-2,686	Table 7.6
Intra-Government transfers	-10,495	Department of Finance and Administration
write down of non-financial assets	-235.	Table 7.1
Total Defence Function Expense	17,871	Statement 6, Budget Paper No. 1

Note

1. Australian Accounting Standards 31 – Financial Reporting by Governments.

Table 7.1: Budgeted Departmental Income Statement⁽¹⁾

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
INCOME							
Revenue							
16,133,541	Revenue from Government	16,362,110	17,063,404	4.3	17,424,698	17,498,316	18,089,342
535,361	Goods and services	258,130	530,482	105.5	536,974	547,251	559,406
-	Interest	-	-	-	-	-	-
87,891	Other Revenue	228,076	65,663	-71.2	64,958	64,657	79,926
16,756,793	Total Revenue	16,848,316	17,659,549	4.8	18,026,630	18,110,224	18,728,674
Gains							
-	Net gain on foreign exchange	-	-	-	-	-	-
250,000	Reversals of previous asset write-downs	72,500	200,000	175.9	200,000	100,000	100,000
-	Net gains on sale of assets	-	-	-	-	-	-
250,000	Total Gains	72,500	200,000	175.9	200,000	100,000	100,000
17,006,793	Total Revenues	16,920,816	17,859,549	5.5	18,226,630	18,210,224	18,828,674
EXPENSES							
6,299,616	Employees	6,549,692	6,609,082	0.9	6,742,406	7,039,455	7,487,515
7,003,260	Suppliers	6,885,384	7,649,136	11.1	7,821,025	7,582,329	7,872,486
6,675	Grants	5,201	5,592	7.5	1,304	1,304	1,304
3,145,023	Depreciation and amortisation	3,336,323	3,336,323	-	3,409,595	3,434,486	3,314,258
18,163	Finance Cost	32,716	20,412	-37.6	20,799	21,144	21,605
514,056	Write-down of and impairment of assets	107,500	235,000	118.6	230,000	130,000	130,000
-	Net losses on sale of assets	-	-	-	-	-	-
20,000	Other	4,000	4,004	0.1	1,501	1,506	1,506
17,006,793	Total Expenses	16,920,816	17,859,549	5.5	18,226,630	18,210,244	18,828,674
-	Net operating result	-	-	-	-	-	-
EQUITY INTEREST							
35,743,047	Accumulated surpluses at 1 July	35,581,258	35,571,664	0.0	35,683,234	35,800,944	35,800,944
35,571,664	Total available for appropriation	35,692,828	35,683,234	0.0	35,800,944	35,800,944	35,800,944
-	Change in accounting policy	-	-	-	-	-	-
-	Capital withdrawal	-	-	-	-	-	-
35,571,664	Accumulated surpluses as at 30 June	35,692,828	35,683,234	0.0	35,800,944	35,800,944	35,800,944

Note

1. Cross-reference to Table 2.6 in Chapter Two – Resourcing.

Table 7.2: Budgeted Departmental Balance Sheet⁽¹⁾

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation \$'000	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
ASSETS							
Financial assets:							
161,249	Cash	161,249	161,249	-	161,249	161,249	161,249
499,094	Appropriation receivable	438,251	455,451	3.9	405,451	350,451	290,451
256,235	Other receivables	256,235	256,235	-	256,235	256,235	256,235
916,578	Total financial assets	855,735	872,935	2.0	822,935	767,935	707,935
Non-financial assets:							
10,945,697	Land and buildings Infrastructure, plant and equipment	10,906,161	10,982,127	0.7	10,856,956	11,182,520	11,264,079
36,450,883	Intangibles	29,578,070	38,216,881	29.2	39,727,201	41,312,320	43,419,964
309,774	Heritage and cultural	306,148	306,210	0.0	302,646	299,082	295,518
800,459	Inventories	800,459	800,459	-	800,459	800,459	800,459
3,738,313	Other	4,150,815	4,169,043	0.4	4,384,941	4,717,275	5,003,035
489,816		8,604,028	289,816	-96.6	289,816	289,816	289,816
52,734,942	Total non-financial assets	54,345,681	54,764,536	0.8	56,362,019	58,601,472	61,072,871
53,651,520	Total assets	55,201,416	55,637,471	0.8	57,184,954	59,369,407	61,780,806
LIABILITIES							
Debt:							
243,710	Leases	228,290	228,990	-	211,930	490,230	452,890
2,631	Other interest bearing liabilities	2,631	2,631	-	2,631	2,631	2,631
246,341	Total debt	230,921	230,921	-	214,561	492,861	455,521
Provisions and payables							
1,550,302	Employees	1,532,896	1,493,890	-2.5	1,427,945	1,477,763	1,525,726
584,885	Suppliers	608,219	608,219	-	631,553	654,887	678,221
527,606	Other	527,606	527,606	-	527,606	527,606	527,606
2,662,793	Total provisions and payables	2,668,721	2,629,715	-1.5	2,587,104	2,660,256	2,731,553
2,909,134	Total liabilities	2,899,642	2,860,636	-1.3	2,801,665	3,153,117	3,187,074
50,742,386	Net assets	52,301,774	52,776,835	0.9	54,383,289	56,216,290	58,593,732
EQUITY							
4,559,862	Contributed equity	5,998,086	6,482,741	8.1	7,971,485	9,804,486	12,181,928
10,610,860	Reserves	10,610,860	10,610,860	-	10,610,860	10,610,860	10,610,860
35,571,664	Retained surpluses or accumulated deficits	35,692,828	35,683,234	0.0	35,800,944	35,800,944	35,800,944
50,742,386	Total equity	52,301,774	52,776,835	0.9	54,383,289	56,216,290	58,593,732
Represented by:							
788,677	Current assets	811,296	817,871	0.8	840,599	872,730	908,178
52,862,843	Non-current assets	54,390,120	54,819,600	0.8	56,344,355	58,496,677	60,872,628
1,707,087	Current liabilities	1,701,517	1,678,628	-1.3	1,644,024	1,676,798	1,707,932
1,202,047	Non-current liabilities	1,198,125	1,182,008	-1.3	1,157,641	1,476,319	1,479,142

Note

1. Cross-reference to Table 2.7 in Chapter Two – Resourcing.

Table 7.3: Budgeted Departmental Statement of Cash Flows⁽¹⁾

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
OPERATING ACTIVITIES							
16,133,541	Appropriations from Government	16,362,110	17,063,404	4.3	17,424,698	17,498,316	18,089,342
545,339	Sales of goods and services	268,234	540,586	101.5	547,278	557,735	570,047
-	Interest	-	-	-	-	-	-
287,007	Net GST refund	296,921	296,291	-	314,384	316,168	381,329
86,391	Other	226,576	64,163	-71.7	63,458	63,157	78,426
86,445	Cash transfer from Official Public Account (receivables)	43,643	43,463	-	50,000	55,000	60,000
17,138,723	Total cash received	17,197,484	18,008,717	4.7	18,399,818	18,490,376	19,179,144
6,235,874	Employees	6,494,534	6,553,924	0.9	6,690,641	6,989,637	7,439,552
6,620,785	Suppliers	6,347,578	7,022,330	10.6	7,122,136	6,874,288	7,212,366
6,675	Grants	5,201	5,592	7.5	1,304	1,304	1,304
20,324	Finance Costs	32,716	20,412	-37.6	20,799	21,144	21,605
-	Inventory	-	-	-	-	-	-
20,000	Other	4,000	4,004	0.1	1,501	1,506	1,506
87,200	Cash transfer to Official Public Account (receivables)	-	-	-	-	-	-
12,990,858	Total cash used	12,884,029	13,606,262	5.6	13,836,381	13,887,879	14,676,333
4,147,865	NET CASH FROM/(TO) OPERATING ACTIVITIES	4,313,455	4,402,455	2.1	4,563,437	4,602,497	4,502,811
INVESTING ACTIVITIES							
Cash received:							
83,363	Proceeds from sales of property, plant and equipment	5,792	38,192	559.4	122,208	69,210	6,799
83,363	Total cash received	5,792	38,192	559.4	122,208	69,210	6,799
Cash used:							
3,420,757	Purchase of specialist military equipment	3,969,944	4,522,933	13.9	4,370,480	4,409,902	4,769,820
485,608	Purchase of property, plant and equipment	466,708	585,446	25.4	572,908	716,213	766,876
1,198,499	Inventory purchases	1,236,199	1,239,727	0.3	1,214,641	1,342,193	1,313,016
5,104,864	Total cash used	5,672,851	6,348,106	11.9	6,158,029	6,468,308	6,849,712
-5,021,501	NET CASH FROM/(TO) INVESTING ACTIVITIES	-5,667,059	-6,309,914	11.3	-6,035,821	-6,399,098	-6,842,913
FINANCING ACTIVITIES							
Cash received:							
972,080	Equity appropriation	1,369,024	1,937,879	41.6	1,588,444	1,880,401	2,379,642
972,080	Total cash received	1,369,024	1,937,879	41.6	1,588,444	1,880,401	2,379,642

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
	Cash used:						
14,480	Repayments of debt	15,420	15,420	-	16,360	36,400	37,340
-	Capital use charge	-	-	-	-	-	-
176,964	Capital withdrawal	-	15,000		99,700	47,400	2,200
191,444	Total cash used	15,420	30,420	97.3	116,060	83,800	39,540
780,636	NET CASH FROM/(TO) FINANCING ACTIVITIES	1,353,604	1,907,459	40.9	1,472,384	1,796,601	2,340,102
-93,000	Net increase/(decrease) in cash held						
254,425	Cash at 1 July	161,249	161,249	-	161,249	161,249	161,249
-176	Other Movements						
161,249	CASH AT 30 JUNE	161,249	161,249	-	161,249	161,249	161,249

Note

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

Table 7.4: Departmental Statement of Changes in Equity – Summary of Movement (Budget Year 2006-07)

	Accumulated results \$'000	Asset revaluation reserve \$'000	Other reserves \$'000	Contributed equity/capital \$'000	Total Equity \$'000
Opening balance as at 1 July 2006					
Balance carried forward from previous period	35,571,664	10,610,860	-	4,559,862	50,742,386
Adjustment for changes in accounting policies	111,570	-	-	-	111,570
Adjusted opening balance	-	-	-	-	-
Income and expense					
Income and expenses recognised directly in equity	-	-	-	-	-
Gain/loss on revaluation of property	-	-	-	-	-
Sub-total income and expense	-	-	-	-	-
Net operating result	-	-	-	-	-
Total income and expenses recognised directly in equity	35,683,234	10,610,860	-	4,559,862	50,853,956
Transactions with owners	-	-	-	-	-
Distribution to owners	-	-	-	-15,000	-15,000
Returns to capital	-	-	-	-	-
Dividends	-	-	-	-	-
Returns on capital	-	-	-	-	-
Restructuring	-	-	-	-	-
Other	-	-	-	-	-
Contribution by owners	-	-	-	-	-
Appropriation (equity injection)	-	-	-	1,937,879	1,937,879
Other	-	-	-	-	-
Restructuring	-	-	-	-	-
Sub-total transaction with owners	-	-	-	1,922,879	1,922,879
Transfers between equity components	-	-	-	-	-
Closing balance as at 30 June 2007	35,683,234	10,610,860	-	6,482,741	52,776,835

Table 7.5: Departmental Capital Budget Statement

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
CAPITAL EXPENDITURE							
3,420,757	Purchase of specialist military equipment	3,969,944	4,522,933	13.9	4,370,480	4,409,902	4,769,820
485,608	Purchase of property, plant and equipment	466,708	585,446	25.4	572,908	716,213	766,876
3,906,365	Total capital payments	4,436,652	5,108,379	15.1	4,943,388	5,126,115	5,536,696
Funded from:							
972,080	Equity injection	1,369,024	1,937,879	41.6	1,588,444	1,880,401	2,379,642
2,909,422	Operating receipts	3,061,836	3,147,308	2.8	3,332,436	3,223,904	3,152,455
24,863	Net capital receipts	5,792	23,192	300.4	22,508	21,810	4,599
3,906,365	Total capital funding	4,436,652	5,108,379	15.1	4,943,388	5,126,115	5,536,696
CAPITAL RECEIPTS							
	Proceeds from the sale of specialist military equipment						
83,363	Proceeds from sales of property, plant and equipment	5,792	38,192	559.4	122,208	69,210	6,799
-58,500	Other capital receipts Less: capital withdrawal	0	-15,000		-99,700	-47,400	-2,200
24,863	NET CAPITAL RECEIPTS	5,792	23,192	300.4	22,508	21,810	4,599

Table 7.6: Non-financial Assets – Summary of Movement

Revised Budget Year 2006-07	Land	Buildings	Other IP&E	Specialist Military Equipment	Software	Other Intangibles	Heritage and Cultural	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
GROSS VALUE								
Gross value as at 30 June 2006	3,864,390	10,613,559	8,543,145	59,187,771	420,254	122,698	800,459	82,751,817
Gross value – additions	-	336,042	247,554	4,622,933	-	1,850	-	5,208,379
Gross value – revaluations	-	-	-	-	-	-	-	-
Gross value – disposals	-	-32,400	-5,792	-	-	-	-	-38,192
Gross value – write offs	-	-	-57,500	-177,500	-	-	-	-235,000
Gross value – adjustments	-	-	-	-	-	-	-	-
Gross value – other movements	-	-	-	200,000	-	-	-	200,000
Gross value –as at 30 June 2007	3,864,390	10,917,201	8,727,407	63,833,204	420,254	124,548	800,459	88,687,463
ACCUMULATED DEPRECIATION/AMORTISATION								
Accumulated depreciation/amortisation as at 30 June 2006	-	3,532,252	3,529,125	27,750,908	157,239	75,939	-	35,045,463
Depreciation/amortisation on assets held at beginning of the year	-	267,212	377,246	2,686,451	3,842	1,572	-	3,336,323
Accumulated depreciation/amortisation on assets disposed through year	-	-	-	-	-	-	-	-
Accumulated depreciation/amortisation as at 30 June 2007	-	3,799,464	3,906,371	30,437,359	161,081	77,511	-	38,381,786
Net book value 30 June 2007	3,864,390	7,117,737	4,821,036	33,395,845	259,173	47,037	800,459	50,305,677

Table 7.7: Schedule of Budgeted Revenues and Expenses Administered on Behalf of Government

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
	Income administered on behalf of Government						
70,060	Interest and dividends	21,579	76,912	256.4	68,517	68,444	67,752
660,500	Other	682,475	659,000	-3.4	659,000	659,000	659,000
730,560	Total income administered on behalf of Government	704,054	735,912	4.5	727,517	727,444	726,752
	Expenses administered on behalf of Government						
2,608,000	Military benefits	2,606,100	2,622,000	0.6	2,703,000	2,791,000	2,883,000
10,000	Subsidies	10,000	10,000	-	10,000	10,000	10,000
	Other						
2,618,000	Total expenses administered on behalf of Government	2,616,100	2,632,000	0.6	2,713,000	2,801,000	2,893,000

Table 7.8: Schedule of Budgeted Assets and Liabilities Administered on Behalf of Government

2005-06 Estimated Actual \$'000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
Assets administered on behalf of Government							
Financial Assets							
-	Cash	-	-	-	-	-	-
3,215	Other Receivable	3,225	3,215	-0.3	3,215	3,215	3,215
	Appropriation						
31,551,000	Receivable	32,632,990	32,638,000	0.0	33,760,000	34,928,000	36,156,000
1,258,883	Investments	1,258,883	1,258,883	-	1,258,883	1,258,883	1,258,883
32,813,098	Total Financial Assets	33,895,008	33,900,098	0.0	35,022,098	36,190,098	37,418,098
84,632	Non-financial assets	89,632	84,632	-5.6	84,632	84,632	84,632
32,897,730	Total assets	33,984,730	33,984,730	-	35,106,730	36,274,730	37,502,730
Liabilities administered on behalf of Government							
31,551,000	Military benefits	32,638,000	32,638,000	-	33,760,000	34,928,000	36,156,000
9,883	Other	9,883	9,883	-	9,883	9,883	9,883
31,560,883	Total liabilities	32,647,883	32,647,883	-	33,769,883	34,937,883	36,165,883
EQUITY							
(3,418)	Accumulated results	(3,418)	(3,418)	-	(3,418)	(3,418)	(3,418)
1,258,883	Reserves	1,258,883	1,258,883	-	1,258,883	1,258,883	1,258,883
81,382	Capital	81,382	81,382	-	81,382	81,382	81,382
1,336,847	Total Equity	1,336,847	1,336,847	-	1,336,847	1,336,847	1,336,847
32,897,730	Total Equity and Liabilities	33,984,730	33,984,730	-	35,106,730	36,274,730	37,502,730
Represented by:							
87,847	Current assets	92,857	87,857	-5.4	87,857	87,857	87,857
32,809,883	Non-current assets	33,891,873	33,896,873	0.0	35,018,873	36,186,873	37,414,873
1,401,263	Current liabilities	1,456,493	1,456,493	-	1,506,548	1,558,655	1,613,439
30,154,620	Non-current liabilities	31,191,390	31,191,390	-	32,263,335	33,379,228	34,552,444

Table 7.9: Schedule of Budgeted Administered Cash Flows

2005-06 Estimated Actual ‘000		2006-07 Previous Estimate \$'000	2006-07 Budget Estimate \$'000	Variation %	2007-08 Forward Estimate \$'000	2008-09 Forward Estimate \$'000	2009-10 Forward Estimate \$'000
OPERATING ACTIVITIES							
Cash received:							
1,506,000	Cash from the Official Public Account	1,529,100	1,545,000	1.0	1,591,000	1,633,000	1,665,000
70,060	Interest and dividends	21,579	76,912	256.4	68,517	68,444	67,752
660,500	Other	682,475	659,000	-3.4	659,000	659,000	659,000
2,236,560	Total cash received	2,223,154	2,280,912	2.1	2,318,517	2,360,444	2,391,752
Cash used:							
1,496,000	Military benefits	1,519,100	1,535,000	1.0	1,581,000	1,623,000	1,655,000
10,000	Subsidies	10,000	10,000	-	10,000	10,000	10,000
730,560	Cash to the Official Public Account Other	704,054	735,912	4.5	727,517	727,444	726,752
2,236,560	Total cash used	2,233,154	2,280,912	2.1	2,318,517	2,360,444	2,391,752
	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 2006-07 budget year, and each of the following forward years from 2007-08 to 2009-10.

Budgeted Income statement, Balance sheet 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 2006-07 as provided in the *Portfolio Additional Estimates Statements 2005-06* and the budget estimate for 2006-07, unless otherwise noted. The estimated actual for 2005-06 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:

- Finance Minister's Orders, being the Financial Management and Accountability Orders (Financial Statements for reporting periods ending on or after 1 July 2005);
- Applicable Australian Accounting Standards and Accounting Interpretations issued by the Australian Accounting Standards Board (AASB); and
- Consensus Views of the Urgent Issues Group.

The Budgeted Income statement and Balance sheet 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 Income statement 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 Australian Accounting Standards Board has issued replacement Australian Standards to apply from 1 July 2005. The new standards are the Australian Equivalents to International Financial Reporting Standards (AEIFRS). The changes in accounting policies under AEIFRS are applied retrospectively as if the new policy had always applied, except in relation to the exemptions available under AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards.

Changes in specific accounting policy have been identified in this note under their appropriate headings.

1.8 Revenue

Revenues from the Australian 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.

Defence operates on a just in time draw-down basis that has resulted in undrawn appropriations at year end being reflected as a receivable. This receivable is available for draw-down to meet future obligations.

Other Revenue

Revenue from the sale of goods is recognised upon delivery of the goods to the customer. Revenue is recognised from services at the time the service is provided. Revenue from disposal of non-current assets is recognised when control of the asset has passed to the buyer.

Receivables

Receivables for goods and services expected to be settled within 12 months of the reporting date are recognised at the nominal amounts, less any provision for doubtful debts. Receivables expected to be settled more than 12 months after the end of the reporting date are measured at their net present value. The collectability of receivables is assessed periodically with provision being made for impairment.

1.9 Transactions with the Australian Government

Equity Injection

Equity injection represents an additional contribution to Defence by the Australian 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 and are recognised directly into equity in that period.

Other Distributions to Owners including Repayments of Appropriations

The Finance Minister's Orders require that distributions to owners be debited to Equity, unless in the nature of a dividend.

1.10 Employee Benefits

Defence's workforce comprises two employment components: Australian Public Service (APS, i.e. civilians) and Australian Defence Force (ADF, i.e. 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 expected to be settled within 12 months of the reporting date are measured at their nominal amounts. The nominal amount is calculated with regard to the rates expected to be paid on settlement of the liability. Employee benefits expected to be settled more than 12 months after the end of the reporting date are measured at the present value of the estimated future cash outflows to be made in respect of services provided by employees up to the reporting date.

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 liability for annual leave for APS and ADF employees reflects the value of total annual leave entitlements of all such employees and is recognised at the nominal amount or discounted to the present value for non-current amounts.

Separation and Redundancy

Provision is made for separation and redundancy benefit payments. Defence has developed a detailed formal plan for the terminations and has informed those affected that the terminations will be carried out.

Superannuation

Permanently-appointed APS employees and Defence contribute to the Commonwealth Superannuation Scheme (CSS), the Public Sector Superannuation Scheme (PSS), the PSS Accumulation Plan and other superannuation schemes held outside the Commonwealth. The liability for staff CSS, PSS and the PSS Accumulation Plan superannuation benefits is recognised in the financial statements of the Australian Government and is settled by the Australian Government in due course.

Defence makes employer contributions to the Australian Government at rates determined by an actuary to be sufficient to meet the cost to the Government of the superannuation entitlements of the department's employees.

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 contributions, pension payments, DFRDB member contributions and the provision for unfunded superannuation are reflected in the Schedule of Administered Items.

Superannuation on-costs have been added to the provisions for annual leave and long-service leave in respect of both APS and ADF employees.

1.11 Asbestos-related Disease Exposure

The responsibility for the administration of common law claims in relation to Asbestos Related Disease Exposure was transferred from the Department of Defence to Comcare, with effect from 1 July 2005. An amount has been recognised in the department's financial statements in respect of Defence's estimated liability for the military personnel component of Asbestos Related Disease Exposure.

1.12 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 and recognised at the lower of the fair value of the leased asset and the present value of minimum lease payments at the commencement of the lease term. A liability is recognised at the same time for the same amount.

Non-current assets acquired under a finance lease are depreciated/amortised over the useful life of the asset. Lease payments are allocated between the principal component and the interest expense.

Operating lease payments are expensed on a basis which is representative of the pattern of benefits derived from the leased assets.

Lease incentives taking the form of 'free' leasehold improvements and rent holidays are recognised as liabilities. These liabilities are reduced by allocating lease payments between rental expense and reduction of the liability

1.13 Bad and Doubtful Debts

The provision for bad and doubtful debts is based on an analysis of the expected realisation of outstanding debts. 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.

1.14 Borrowing Costs

Borrowing costs are expensed as incurred.

1.15 Cash

Cash means notes and coins held, as well as any deposits held at call with a bank or financial institution. Cash is measured at the nominal amount.

1.16 Acquisition of Assets

Assets are recorded at cost on 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 and Intangible assets (where no active market exists), 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.

1.17 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 Balance Sheet where they meet the capitalisation threshold.

Individual items will be capitalised where the individual value is equal to or exceeds \$2,000. Grouped Specialist Military Equipment assets will be capitalised for items of homogenous nature within a single class where the individual item values equal or exceed \$1 and the class group value equals or exceeds \$50,000.

Revaluations

Land, buildings, plant and equipment are measured and disclosed at fair value.

The carrying value of non-current assets have been assessed at 30 June 2006 by independent qualified experts or management. The fair value of non-current assets not subject to an external valuation in any given year are reviewed by management and the carrying amounts adjusted where they are materially different from fair value as determined by management.

With the exception of Specialist Military Equipment, Assets Under Construction, and Intangibles, from 1 July 2004 Defence moved to a 5-year external revaluation cycle.

In accordance with the Finance Minister's Orders, Specialist Military Equipment is carried at deemed or actual cost.

Assets Under Construction are not revalued but are carried 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.

Depreciation and Amortisation

Non-current assets having limited useful lives are systematically depreciated/amortised over their estimated useful lives in a manner that reflects the consumption of their service potential on a straight-line basis.

Heritage assets are generally anticipated to have very long and indeterminable useful lives. The service potential of heritage and cultural assets has not in any material sense been consumed during the reporting period.

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

Decontamination and Restoration Costs

Where a legal or constructive obligation exists to restore an asset back to its original condition, the net present value of estimated restoration costs are capitalised and added to the cost of the underlying asset and depreciated over the asset's useful life. As such, a corresponding provision is recognised for the restoration obligation costs. When discounting is used, the carrying amount of the provision is adjusted to reflect the unwinding of the discount and this is recognised as a finance expense.

Decontamination costs associated with properties listed for disposal are recognised as a provision separate to the valuation of the property. This provision offsets against the overall value of the property. The decontamination costs are determined on the basis of remediation surveys and technical assessments. When decontamination costs are recognised, the corresponding entry is an expense of the period of recognition. The cost of decontamination work carried out is cleared against the provision.

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.

Impairment of Non-Current Assets

Non-current assets carried at cost or fair value, which are not held to generate net cash inflows, are assessed for indications of impairment. Where indications of impairment exist, the recoverable amount of the asset is estimated and compared to the asset's carrying amount. If the recoverable amount is less than its carrying amount, the carrying amount is reduced to the recoverable amount and the reduction is to be shown as an impairment loss expense.

1.18 Inventory

Defence's inventory is for its own consumption and it does not ordinarily hold inventory for sale. If sales are made they represent disposal of inventory surplus to requirements and minor fuel sales.

Inventors held for distribution are measured at the lower of cost and current replacement cost. The cost of inventories are to be assigned using the weighted average cost formula (In 2004-05 inventory no longer required was valued at net realisable value).

Defence has implemented a policy to identify and provide for potential excess stocks.

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.

1.19 Intangibles

Defence's intangibles primarily comprise externally acquired and internally-developed computer software for internal use. Intangibles with gross values greater than \$150,000 are capitalised.

Acquired intellectual property may form part of the acquisition of particular tangible assets and in such cases is reflected in the value reported for Property, Plant and Equipment in the Budgeted Balance Sheet.

Defence carries intangible assets at cost or, where an active market exists, at fair value (in 2004-05 intangibles were held at cost).

The service potential of non-current intangible assets is reviewed annually. If an intangible asset is regarded as being impaired, the asset is written down to reflect its remaining service potential. Intangible assets are assessed annually for impairment.

Intangibles are amortised on a straight-line basis over their anticipated useful life.

1.20 Investments

Investments held on behalf of the Australian Government are included as administered assets and are brought to account as the value of the Australian Government'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.

1.21 Foreign Currency

Transactions denominated in a foreign currency are converted at the exchange rate on the date of transaction. Foreign currency receivables and payables are translated at the exchange rate current as at the balance date.

1.22 Taxation

Defence's activities are exempt from all forms of taxation except fringe benefits tax and the goods and services tax (GST).

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

- where the amount of GST incurred is not recoverable from the Australian Taxation Office; and
- for receivables and payables (which are shown inclusive of GST in the Budgeted Income statement).

1.23 Insurance

Defence has insured for key insurable risks, excluding workers compensation, through the Government's insurable risk managed fund, called 'Comcover'. Workers compensation is through Comcare.

1.24 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.

Revenue collected by Defence, for use by the Australian Government rather than Defence, is Administered Revenue. Collections are transferred to the Official Public Account maintained by the Department of Finance and Administration. Conversely, cash is drawn down from the Official Public Account to make payments under Parliamentary appropriations on behalf of the Australian Government. These transfers to and from the Official Public Account are reported as adjustments to the administered cash held by Defence on behalf of the Government and reported as such in the Budgeted Statement of Cash Flows in the Schedule of Administered Items and in the Administered Reconciliation Table. Thus the Budgeted Schedule of Administered Items largely reflects the Australian Government's transactions, through Defence, with parties outside the Australian Government.

Administered Revenue

All administered revenues are revenues relating to the core operating activities performed by Defence on behalf of the Australian Government. Administered revenues mainly 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 Australian Government. Administered expenses mainly comprise unfunded military superannuation benefits, ADF housing subsidies and ADF retention benefits.

Administered Investments

Defence reports the Australian Government's capital investment in the Defence Housing Authority. It is measured at fair value and is subject to impairment.

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. Retention benefit payments are initially recorded as prepayments and written down over the period of service.

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 Budgeted 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 Budgeted Schedules of Administered Items. The Australian Government on behalf of the MSBS Fund makes funded benefit payments to members of the scheme and the Australian Government 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 Budgeted Schedules of Administered Items. The Australian Government Actuary completes a full review of the unfunded liabilities (a long-term cost report) every three years.

NOTE 2 – SUMMARY OF ESTIMATED SPECIAL ACCOUNT BALANCES

Table 7.10: Summary of Estimated Special Account Balances⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾

	Opening Balance	Receipts	Payments	Adjustments	Closing Balance
	2006-07	2006-07	2006-07	2006-07	2006-07
	<i>2005-06</i>	<i>2005-06</i>	<i>2005-06</i>	<i>2005-06</i>	<i>2005-06</i>
	\$'000	\$'000	\$'000	\$'000	\$'000
Services for Other Governments and Non-Agency Bodies – Financial Management and Accountability Act 1997 ⁽⁵⁾⁽⁶⁾	29,120 <i>155,428</i>	35,497 <i>30,209</i>	37,660 <i>156,517</i>	- -	26,957 <i>29,120</i>
Defence Endowments – Financial Management and Accountability Act 1997	289 <i>285</i>	40 <i>26</i>	37 <i>22</i>	- -	292 <i>289</i>
Fedorczenko Legacy Fund – Financial Management and Accountability Act 1997	156 <i>154</i>	8 <i>6</i>	5 <i>4</i>	- -	159 <i>156</i>
Other Trust Monies – Financial Management and Accountability Act 1997	288 <i>7,793</i>	1,889 <i>2,429</i>	1,902 <i>9,935</i>	- -	275 <i>287</i>
Young Endeavour Youth Program – Financial Management and Accountability Act 1997	847 <i>827</i>	792 <i>784</i>	700 <i>764</i>	- -	939 <i>847</i>
Total Special Accounts	30,700 <i>164,487</i>	38,226 <i>33,454</i>	40,304 <i>167,242</i>	- -	28,622 <i>30,699</i>

Notes

1. 2006-07 revised estimates in bold.
2. 2005-06 estimates in italics.
3. The 2005-06 figures above include approximately \$6,000 for interest earned on the Official Public Account.
4. The 2006-07 figures above include approximately \$30,000 for interest earned on the Official Public Account.
5. The Services for Other Governments balance includes money relating to Comcare.
6. With the prescription of DMO on 1 July 2005 Defence has transferred \$125,909,667.45 from Services for Other Governments and Non-Agency Bodies.

