Defence Housing AUSTRALIA

Defence Housing Australia

AASB Submission Paper

Date	14 May 2009
Subject	Submission paper – Exposure Draft 174 (ED 174)

Purpose

The purpose of this submission is to provide comment on ED 174 '*Amendments to Australian Accounting Standards to facilitate GAAP/GFS Harmonisation for Entities within the GGS*', with specific reference to whether the Exposure Draft is appropriate for application to for-profit entities within the General Government Sector (GGS).

Comment on Exposure Draft 174

Defence Housing Australia (DHA) understands that ED 174 is the second phase of a broader initiative undertaken by the Australian Accounting Standards Board (AASB) to pursue the harmonisation of Government Finance Statistics (GFS) and Generally Accepted Accounting Principles (GAAP) reporting. The objective of the AASB is to achieve an Australian Accounting Standard for a single set of Government reports which are auditable and comparable.

Whilst appreciating the importance of the comparability of financial statements, DHA notes that its objectives and operational functions, as a GBE, are significantly different to that of the majority of GGS entities.

DHA operates as a commercial entity within the residential property market. DHA borrows funds from the Department of Finance and Deregulation at market rates however the majority of DHA's funds are derived from external revenue sources. DHA does not provide goods and services free of charge or at prices that are not economically significant and DHA does not redistribute income. DHA seeks to achieve an appropriate rate of return on capital employed and in doing so operates in the commercial sector with its own set of governance arrangements and performance expectations.

DHA targets against a variety of Key Performance Indicators, including Earnings Before Interest and Tax, Profit Before Tax and Net Operating Surplus after Income Tax. These are to be clearly distinguished from indicators such as Net Appropriations and Net Operating Surplus/Deficit as relevant to many GGS entities.

DHA manages approximately 17,400 properties across Australia, representing around $7.6 billion worth of housing stock. Approximately 63% of these homes are owned by private investors and leased back to DHA primarily through a Sale and Leaseback Program. In order to sustain DHA's extensive capital funding program, DHA must focus on the attractiveness of the Sale and Leaseback product to individual and institutional private investors. Furthermore, DHA needs to remain attractive to potential commercial consortium partners to continue to deliver its Defence mandate.

Comparability to other GGS entities is therefore not a key focus for DHA. Reporting in line with other GGS entities satisfies neither an operational nor a financial reporting need. This was confirmed at the recent Roundtable meeting held in Canberra where representatives from both the Department of Finance and Deregulation and the Australian Bureau of Statistics were in agreement with the notion that DHA's reporting needs are markedly different to that of the wider GGS reporting group.

On the basis that DHA operates predominantly within the private sector and GGS entities report for the purpose of government transparency and government resource allocation, DHA questions the benefit to be obtained from the harmonisation of for-profit financial reports with those of the wider GGS community.

Further to this, it is relevant to reflect on the AASB's *Statement of Accounting Concepts 2 (*SAC 2*)*, and the original purpose of financial reporting. SAC 2 outlines the purpose of financial reporting as being the communication of relevant and reliable information to its users. It encourages the dissemination of information useful to users for making and evaluating decisions about the allocation of resources. The Finance Minister's Orders also require Government entities to present all disclosures necessary to give a true and fair view of their results, which meet their stakeholders' information needs and *are reflective of their operations.*

ED 174 has the potential to hinder DHA's ability to appropriately reflect its operational activities and financial achievements. The presentation of the Statement of Financial Position on a liquidity basis and the Statement of Comprehensive Income in the form of transactional and economic flows provides DHA private investors with information that is neither comparable to that of its competitors nor particularly reflective of its financial objectives.

Accounting implications of ED 174 amendments

For the last three years, DHA has applied *AASB 140* and, through the enabling items in the Finance Minister's Orders, *AASB 116*, to account for its investment properties at cost. This facilitates a better understanding of DHA's property holdings and makes the setting of targets and reporting of achievements more transparent.

Implicit in ED 174, in particular the insertion of Aus 83.1 and Aus 83.2 item (d), is the assumption that investment properties are carried at fair value by GGS entities.

Should ED 174 and the harmonisation process proceed as described, the insertion of Aus 83.1 and Aus 83.2 would potentially require DHA to change its accounting treatment of investment properties from that of cost to fair value. With a move to fair value, DHA would be required to alter its Dividend Policy and also review its capacity to borrow. Profitability would be determinate on market values as opposed to actual performance and as a result Key Performance Indicators such as Return on Equity and Return on Capital Employed would become increasingly volatile when used to report to shareholders.

Such a shift would therefore be significant for DHA, creating not only disclosure implications but also issues relating to measurement and recognition and analysis thereon.

In approaching the Exposure Draft, the AASB noted that because the amendments are consistent with the current requirements in AASB 101 and AASB 107, there would be no reason to prevent a for-profit entity such as DHA from complying with the amendments.

Although the ED 174 amendments are in keeping with the spirit of AASB 101 and AASB 107, DHA urges the AASB to consider the secondary accounting implications identified above, in their assessment of the Affected Entities outlined in Item BC6 of ED 174.

Conclusion

In summary, DHA notes the following:

The varied and often commercial nature of for-profit entities within the GGS is such that the relevance of financial reporting harmonisation is potentially minimal and in some instances unfavourable.

ED 174 has the potential to hinder DHA's ability to appropriately reflect its operational activities and financial achievements and therefore departs from one of the fundamental principles of financial reporting.

Although drafted with a view to remain consistent with AASB 101 and 107, there are potential secondary accounting implications of the amendments, when they are applied to for-profit entities. DHA therefore recommends the AASB reconsider the Affected Entities as outlined in Item BC6 of ED 174.

As a result DHA does not believe it is appropriate for the proposals as outlined in ED 174 to apply to for-profit entities within the GGS. DHA has alternative recommendations that will negate the unfavourable outcomes outlined above and propose the AASB consider these, outlined below.

DHA Recommendations

In light of the above considerations, DHA would recommend the establishment of a primary and secondary reporting regime.

Under the primary regime, for-profit GGS entities would be permitted to nominate the application and presentation of key accounting policies. This is in line with all other for-profit entities and would ensure the necessary comparability with key competitors.

Under the secondary regime, for-profit entities within the GGS would be required to prepare a secondary set of accounts for consolidation purposes. This may or may not be used to facilitate the comparability as intended by the harmonisation initiative.

DHA believes there is a need for multiple sets of accounts for for-profit entities and reiterates the importance of the ability to prepare a set of accounts that enable the dissemination of information to its users.

APPENDIX 1

DHA Background

Defence Housing Australia (DHA) was established under the *Defence Housing Australia Act 1987*.

DHA's main function is to provide adequate and suitable housing and relocation services for, and housing services to, members of the Australian Defence Force (ADF) and their families, and officers and employees of the Department of Defence (Defence) and their families, to meet the operational needs of the ADF and the requirements of Defence.

As a Government Business Enterprise (GBE) operating under the *Government Business Enterprises Act 1995*, DHA has two Shareholder Ministers, the Minister for Defence and the Minister for Finance and Deregulation. Additionally, DHA qualifies as a GGS entity by virtue of an Australian Bureau of Statistics ruling under the Government Financial Statistics (GFS). As a result, DHA produces two sets of annual accounts, one in relation to its for-profit status, the other, not-for-profit accounts, in relation to its being part of the GGS.

DHA operates under the Finance Minister's Orders for Financial Reporting, as required by the *Commonwealth Authorities and Companies Act 1997*, and complies with the Australian Accounting Standards.

DHA has become a key player in the Australian residential property market. DHA compares itself with competitors such as Stockland and Australand and places significant emphasis on its private sector presence. As a commercial entity, DHA submits income tax to the Australian Taxation Office and also complies with Fringe Benefits Tax and Goods and Services Tax Legislation.