Australian Government
Australian Office of Financial Management

AOFM

ANNUAL REPORT
2013-14

Australian Office of Financial Management

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Annual Report 2013-14

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Australian Government
Australian Office of Financial Management

3 October 2014

The Hon Joe Hockey MP
Treasurer
Parliament House
CANBERRA ACT 2600

Dear Treasurer

I have pleasure in presenting the Annual Report of the Australian Office of Financial Management for the year ending 30 June 2014 for presentation to the Parliament.

The Report has been prepared in accordance with guidelines approved on behalf of the Parliament by the Joint Committee of Public Accounts and Audit.

Yours sincerely

Rob Nicholl

Rob Nicholl
Chief Executive Officer

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AOFM

ITS ROLE

The AOFM supports and advances Australia's economic growth and stability, and the effective operation of its financial markets, through issuing debt, investing in financial assets and managing that debt and those investments for the Government

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REVIEW BY THE CHIEF EXECUTIVE OFFICER

Context

Core to the AOFM's responsibilities are financing the Government's budget requirements (through debt issuance), managing its daily cash balances in the Official Public Account (OPA) and managing the Commonwealth Government Securities (CGS) portfolio. Sharply changing market conditions and appreciable shifts through the year in the financing task combined to present challenges in achieving the 2013-14 issuance task while balancing cost and risk considerations. There were times throughout the year when the broader longer-term objective for the portfolio of issuing longer-dated maturities was challenged by weekly issuance judgments that needed to take account of prevailing demand for shorter-dated bonds. By year end however, there had been sufficiently consistent strong overall demand for CGS to facilitate smooth absorption of a large issuance programme ($87 billion in gross terms). Opportunities were also taken to further extend the Treasury Bond and Treasury Indexed Bond yield curves.

CGS yields rose over the early part of the year and this trend continued into the middle of the year, being most pronounced during November 2013 to January 2014. Although the United States (US) Federal Reserve had in early 2013 signalled an intention to adjust its accommodative monetary policy stance, it did not announce a wind-down of its asset buying programme until December of that year. Speculation about the impact it would have in global bond markets led to a general market sell-off. Yields and currency levels in emerging markets were particularly impacted around this time. As CGS yields tend to track changes in US Treasury bond yields, the increase in CGS yields during this period was consistent with global events. As had been the case the previous year, market expectations about a prolonged period of low RBA cash rates 'anchored' short-dated CGS yields relative to the large rises for longer dated securities. Together, these influences resulted in a steeper yield curve. Through the second half of the financial year, bond markets 'rallied' in response to weak US GDP data and expectations of continued very weak economic growth across most of Europe. As a result, 10-year CGS yields were around 70 basis points lower by June 2014 compared to what had been observed in December 2013.

At the end of the financial year, CGS yields remained at historically low levels and management of the debt portfolio though the year was again progressed through extending both the length of the yield curve (this time to around 20 years) and the duration of the portfolio.

Market engagement consistently indicates that a sovereign issuer that is transparent and consistent in its operations, and uses market feedback and engagement with investors to determine its issuance pattern and market development decisions, is highly regarded by investors. The AOFM remains mindful of these operational considerations.

Issuance to support the financing task

The Government's budget financing requirement in 2013-14 was fully met with the issuance programme effectively having been completed around the announcement of the 2014-15 Budget. As regular supply through weekly competitive tenders of bonds is recognised as an important feature of the AOFM's operations, issuance was continued (at lower weekly tender volumes) until the end of the year; resulting in around $4 billion in pre-funding for the 2014-15 financing task.

Gross Treasury Bond issuance for the year totalled approximately $80 billion, most of which went into existing bond lines to enhance liquidity. The AOFM understands that liquidity is a core determinant of investor preferences when investing in sovereign bond markets and the CGS market enjoys a reputation for strong liquidity relative to its size (particularly amongst offshore investors). The CGS market exhibits a diversity of investor types (and a wide geographic spread of them) and has attracted strong 'price making' competition amongst a large number of (intermediary) banks.

In terms of market development, favourable market opportunities were used to establish three new Treasury Bond lines: October 2018 and April 2026 maturities (to support the 3-year and 10-year Treasury Bond futures contracts); and an April 2033 maturity (to extend the yield curve and establish a 20-year benchmark). The two longer maturities were launched via syndication, and both deals attracted very strong demand, with total bids received in each case substantially in excess of the volumes issued.

For Treasury Indexed Bonds, gross issuance for the year totalled approximately $7 billion. To further develop this market, a new August 2035 maturity was established to extend the length of the real yield curve (to around 20 years). In addition, a new November 2018 maturity was issued and this will provide the AOFM with additional issuance flexibility in the short end of the indexed curve.

The AOFM is committed to regular engagement with the market and once again, it took account of prevailing market conditions and information from financial market contacts about investor demand in selecting the bond lines to issue each week. Other factors of significance for issuance decisions were relative yield considerations, increasing the liquidity of outstanding bond lines, and the need to manage the maturity structure of the debt portfolio in order to maintain refinancing risks at acceptable levels.

The AOFM is aware that striking the right balance between maintaining flexibility in its issuance task and transparency in its approach, is an important contributing factor to the success of its operations. In this regard, the AOFM continued to update the market through the year with respect to changes to the issuance programme, while not revealing market sensitive decisions until an appropriate time had been determined.

Portfolio management and outcomes

The AOFM continued throughout 2013-14 with its aim of increasing the duration of the debt portfolio.

A longer average term to maturity of new issuance was again targeted with the aim of continuing to increase the weighted average term to maturity of the portfolio as a whole. The weighted average term to maturity of the stock of nominal bonds outstanding at the end of the year was just under six years. This compares with around five years in June 2010.

The issuance of Treasury Bonds with relatively long terms to maturity in a historically low interest rate environment is a cost-effective means of reducing risk in the portfolio by giving greater certainty around future debt servicing cost outcomes and reducing refinancing risk. With a large issuance programme, there was always the possibility that volatile market conditions would limit the proportion of the total programme that could be issued into long bonds. However, sufficient periods of favourable market conditions and steadily growing interest by investors for longer dated CGS combined to allow for the overall portfolio objective to be further progressed.

Residential mortgage-backed securities

Although the AOFM has ceased investment in new RMBS, it continues to manage the existing portfolio to maturity.

Australian RMBS market conditions continued to strengthen throughout 2013-14. The AOFM took four opportunities to sell RMBS notes, totalling around $872 million, with the aim of supporting price discovery in the secondary market or to adjust the portfolio in line with the Treasurer's Directions regarding the programme. These sales resulted in a gain on disposal over the amortised face value of the notes sold.

Registry services for CGS

The AOFM is now responsible for oversight of the registry services for CGS. This has involved the procurement of debt registry services to support securities exchange trading of CGS, and to replace the existing domestic debt registry service provided by the RBA. Registry services to support exchange-traded CGS became operational during 2012-13, while work to transition the domestic debt registry services provided by the RBA to a new service provider was successfully completed in February 2014.

Looking ahead

The 2014-15 Budget indicated that fiscal policy settings will result in declining issuance programmes over the forward estimates period. The outlook for declining issuance will generate speculation on the part of investors as to what the outright size of the CGS market will be once a return to Budget surpluses has been achieved. An important part of the AOFM's engagement with investors is to reinforce policy undertakings by successive governments to support liquidity in the CGS market.

The CGS market has undergone a marked transformation in a relatively short period of time. Growing interest in CGS has supported the AOFM's objective of issuing longer dated maturities and gradually extending the yield curve. We understand that this also assists broader financial market development for Australia.

The AOFM remains mindful of the need to consider further sustainable market developments, for both the Treasury Bond and Treasury Indexed Bond markets, and an important step will be to consolidate the 20-year Treasury Bond benchmark. Issuing new maturities in support of the 3-year and 10-year futures market contracts remains a priority, as does the need to monitor liquidity and how that may be affected by the outstanding size of individual bond lines. We will also continue to assess the prospect of further successfully extending the nominal and indexed bond yield curves and will be monitoring domestic and offshore interest for longer CGS duration to assist in making this judgement.

There is unlikely to be significant new central bank and sovereign wealth fund demand for CGS in the near term because around 75 per cent of the world's 30 largest institutions, from this group, now participate in the CGS market. While new institutions periodically commence investing in the market, they are now usually small to medium sized reserve managers and so their impact on demand, while positive, is not large. However, a steadily growing interest from fund managers continues. Our investor engagement efforts are taking this into account and we remain aware of the need to meet with new and potential new investors in order to support the objective of increasing the diversity of the CGS investor base.

Rob Nicholl
Chief Executive Officer

AOFM

PART 1
AOFM OVERVIEW

AOFM OVERVIEW

Role, function, outcome and programme structure

The Australian Office of Financial Management (AOFM) is responsible for the management of Australian Government debt. The AOFM also manages the Government's cash balances and invests in financial assets.

The AOFM's debt management activities include the issuance of Treasury Bonds and Treasury Indexed Bonds. To support the efficient operation of the markets for these debt instruments, it maintains a securities lending facility that allows financial market participants to borrow the bonds from the Reserve Bank of Australia (RBA).

The AOFM's cash management activities include the issuance of Treasury Notes for short-term funding, and investments in term deposits with the RBA.

The AOFM's investment management activities include managing investments in Australian residential mortgage-backed securities (RMBS) under the Government programme that supported competition in lending for housing. Under the direction of the Treasurer, the AOFM has made no new investments in RMBS since April 2013.

The AOFM is part of the Treasury portfolio. It is accountable to the Secretary to the Treasury and to the Treasurer, and through the Treasurer to the Parliament and the public. However, it is a prescribed agency under the *Financial Management and Accountability Act 1997* and maintains its own accounts separately from those of the Treasury. AOFM staff are employed under the *Public Service Act 1999*.

For budgetary purposes, the AOFM's activities comprise of one programme directed to achieve the following outcome on behalf of the Australian Government: the advancement of macroeconomic growth and stability; the effective operation of financial markets through issuing debt and investing in financial assets; and managing debt, investments and cash. The AOFM aims to manage its net debt portfolio at least cost, subject to an acceptable level of risk. It also issues bonds taking into account the Government's policy objectives to support the Commonwealth Government Securities market.

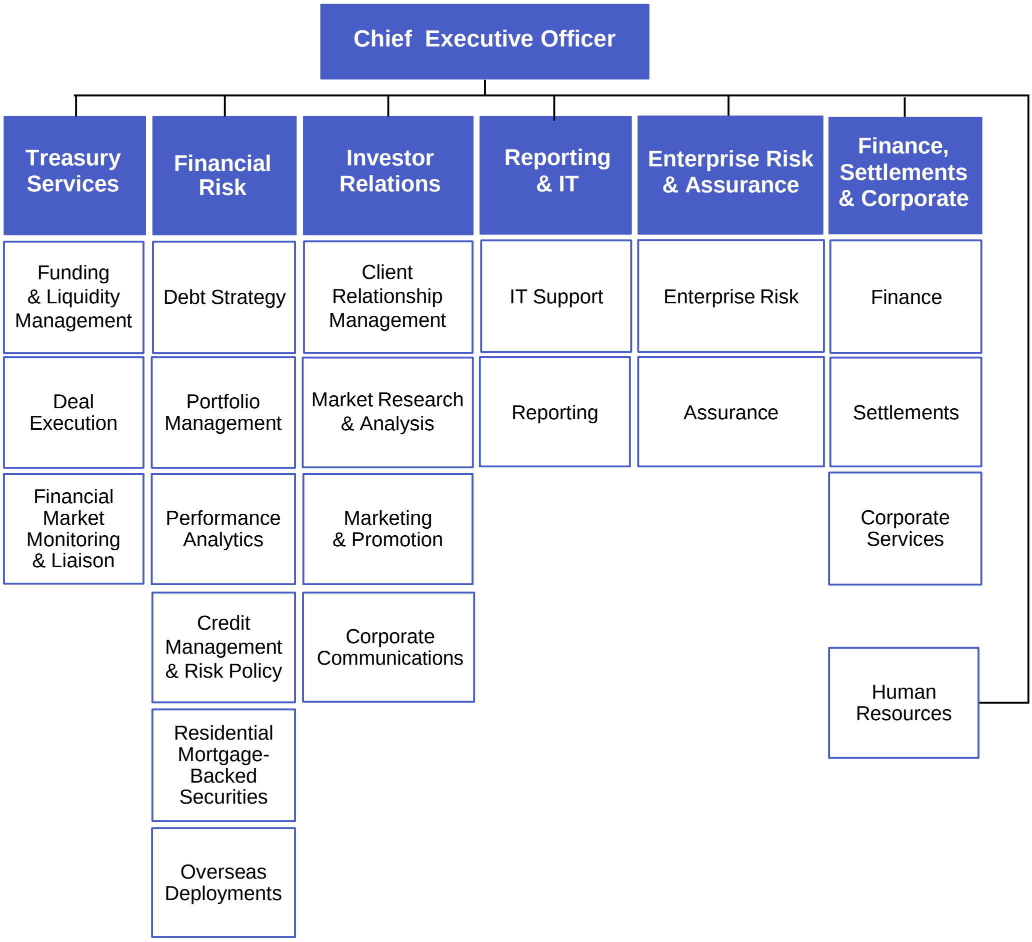
Organisational structure

During 2013-14, the AOFM operated using six groups supported by a human resources manager. Roles and responsibilities within the Office were structured to ensure an appropriate segregation of duties and reporting lines. The six groups were:

- Treasury Services;
- Financial Risk;
- Investor Relations;
- Reporting and Information Technology (IT);
- Finance, Settlements and Corporate; and
- Enterprise Risk and Assurance.

In addition, the AOFM supports the Australian Government's aims to transfer knowledge and skill to developing countries through foreign aid related avenues. In 2013-14, AOFM staff members worked on programmes organised by AusAID and Department of Foreign Affairs and Trade under the *Strongim Gavman Program* in Papua New Guinea and the *Solomon Islands Economic and Public Sector Governance Program* in the Solomon Islands. Both programmes offer these governments support for their debt and cash management activities.

Figure 1: AOFM organisational structure



AOFM

PART 2

OPERATIONS AND PEFORMANCE

OPERATIONS AND PERFORMANCE

Introduction

The principal functions of the AOFM are:

- issuance of Commonwealth Government Securities (CGS) to support the Government's financing task (including maturing debt) and in accordance with broader Government policy objectives (such as promoting liquidity);

- managing the Government's daily cash balances through borrowings and investments;

- undertaking investments in financial assets according to policy directives, or as part of broader portfolio management;

- developing risk assessments that support the effective cost management of the debt and asset portfolios; and

- where appropriate, supporting the efficient operation of the Australian financial system through its debt issuance choices.

This section outlines the activities undertaken in 2013-14 and reports on AOFM performance against these functions.

Treasury Bond and Treasury Indexed Bond issuance

Objective

One objective of Treasury Bond and Treasury Indexed Bond issuance is to raise monies to fund the Australian Government Budget.

Another objective is to support the efficient ongoing operation of Australia's financial system. This second objective is achieved in the following ways:

- Treasury Bonds, Treasury Indexed Bonds and Treasury Bond futures are used by financial market participants as benchmarks for the pricing of other capital market instruments and to manage interest rate risk; and

- the existence of active and efficient physical and futures markets for sovereign debt strengthens the robustness of the financial system and reduces its vulnerability to shocks.

Achieving the objective

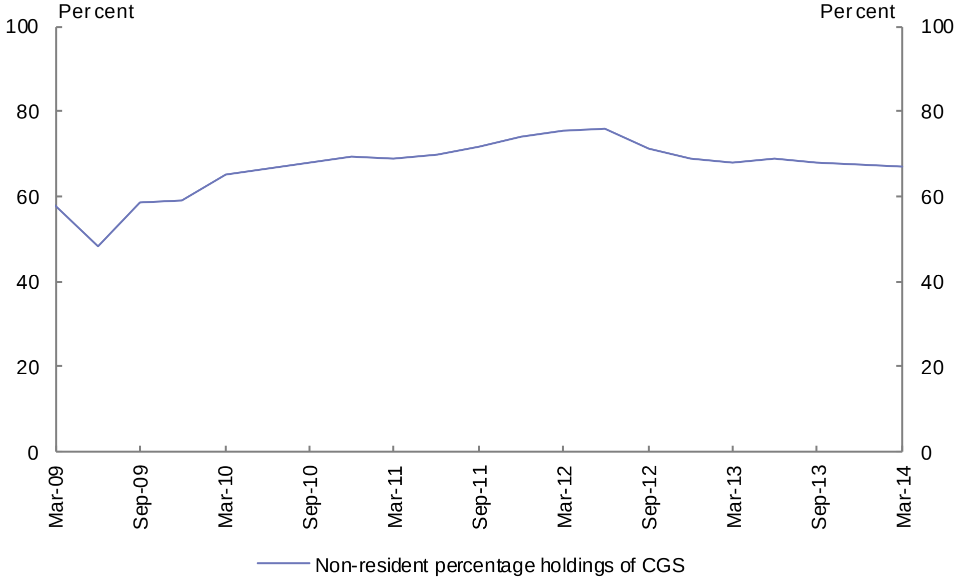
The 2013-14 debt issuance programme was successfully completed in the context of continued strong investor demand for CGS. The length of the yield curve was extended to around 20 years, and liquidity was built in several new and existing lines.

In August 2013, the Reserve Bank of Australia (RBA) reduced the target cash rate to a record low 2.50 per cent. Over the course of 2013-14, CGS yields ended the year relatively unchanged; however, there was significant variation in yields within the year. In the first half of 2013-14, CGS yields moved higher, and the yield curve steepened, in line with United States (US) Treasury yields in the lead up to the announcement by the US Federal Reserve of its 'tapering' programme of quantitative easing — which it commenced in December 2013. US Treasury yields subsequently fell in January due largely to the expectation that the terminal Fed funds rate may be lower than anticipated. While in Europe, financial markets expected the European Central Bank to maintain rates at record low levels for longer amid low inflation and growth forecasts.

The higher yields on Australian bonds relative to other similarly rated sovereign bonds were attractive to offshore investors, especially in the second half of 2013-14. The strong offshore demand for CGS resulted in the 10-year spread to US Treasury yields contracting sharply to near seven-year lows in June 2014.

Non-resident holdings were on average around 70 per cent of the total CGS outstanding during 2013-14. The proportion of CGS held by offshore investors has been relatively steady during recent years, as illustrated in Chart 1.

Chart 1: Non-resident holdings of Commonwealth Government Securities



Treasury Bonds

Gross Treasury Bond issuance for the year totalled approximately $80 billion. The bulk of issuance was into existing bond lines in order to enhance their liquidity and in turn, the attractiveness of the CGS market. This was particularly important to international investors. In addition, three new Treasury Bond lines were launched in 2013-14:

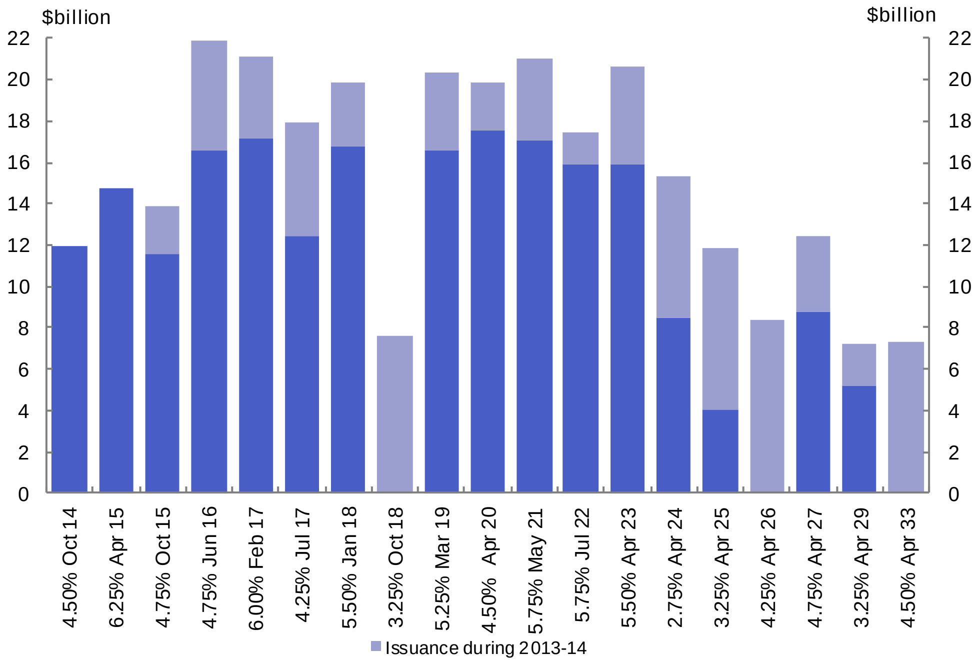
- a new bond line with a maturity date in April 2026 was opened in order to support the operation of 10-year Treasury Bond futures contracts;
- a new bond line with a maturity date in October 2018 was opened in order to support the operation of 3-year Treasury Bond futures contracts and to assist in reducing the amount outstanding in future years in surrounding bond lines, which will make it easier to manage maturity of those bonds; and
- a new April 2033 bond line was issued to increase the length of the yield curve to around 20 years.

In selecting the bond lines to issue each week, the AOFM took account of prevailing market conditions; information from financial market contacts about investor demand; relative value considerations; the aim of increasing the liquidity of outstanding bond lines; and the need to manage the maturity structure to limit refinancing risk. Two tenders were held most weeks, typically comprising a tender of a long-dated bond line and a tender of a short-dated bond line, with the amount being offered at each tender in the range between $600 million to $1.5 billion.

Chart 2 shows the Treasury Bonds outstanding as at 30 June 2014 and issuance during the 2013-14 financial year.

During the year, the total volume of Treasury Bonds outstanding increased by around $57 billion, to $290 billion. At the end of the year, there were 15 Treasury Bond lines with over $10 billion on issue.

Chart 2: Treasury Bonds outstanding as at 30 June 2014 and issuance in 2013-14



Treasury Indexed Bonds

Gross Treasury Indexed Bond issuance for the year totalled $7.29 billion.

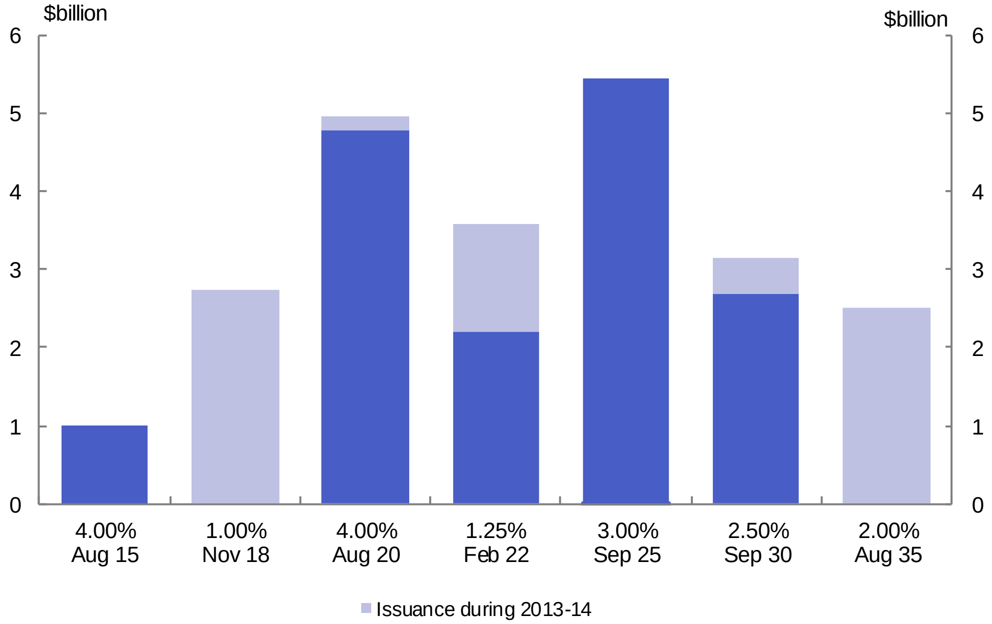
Tenders for the issue of Treasury Indexed Bonds were conducted twice a month, in most months. The volume of each line outstanding, relative yields and other prevailing market conditions were all considered in the selection of which line to offer. Following consultation with indexed bond market participants, tenders for the issue of Treasury Indexed Bonds were held on a multiple price basis rather than a single price basis from July 2013.

There was one syndicated offer of a new Treasury Indexed Bond maturing in August 2035, which extended the length of the real yield curve. In addition, a new Treasury Indexed Bond maturing in November 2018 was issued by tender. The new bond provides the AOFM with additional issuance flexibility in the short end of the curve and supports market development.

Holders of the August 2015 Treasury Indexed Bond were given the opportunity to convert their holdings in that bond to the November 2018 bond. The conversion offer revealed investor support for the new 2018 maturity and was well subscribed, with $2,039 million face value of the August 2015 bond converted to the November 2018 bond. The conversion offer allowed the new 2018 bond line to be quickly built up to a liquid size and for investors to exit the 2015 bond, which due to its short remaining period to maturity is of limited use as an inflation hedge.

Chart 3 shows seven Treasury Indexed Bond lines and amounts outstanding as at 30 June 2014, together with issuance during the 2013-14 financial year.

Chart 3: Treasury Indexed Bonds outstanding as at 30 June 2014 and issuance in 2013-14



Domestic debt registry services

In 2012-13, debt registry services were procured to support the securities exchange trading of CGS and to replace the domestic debt registry service provided by the RBA.

Work to transition the domestic debt registry service to the new service provider was completed in February 2014.

Commonwealth Government Security Buyback Facility

The RBA closed the small investor bond facility in May 2013. From February 2014, small investors were able to sell their holdings of CGS back to the Australian Government via the Commonwealth Government Security Buyback Facility (Buyback Facility). The Buyback Facility is operated by Computershare Investor Services Pty Limited under a contract managed by the AOFM on behalf of the Australian Government.

Performance

Funding the Budget

The Government's budget financing requirement in 2013-14 was fully met, together with around $4 billion in pre-funding for 2014-15.

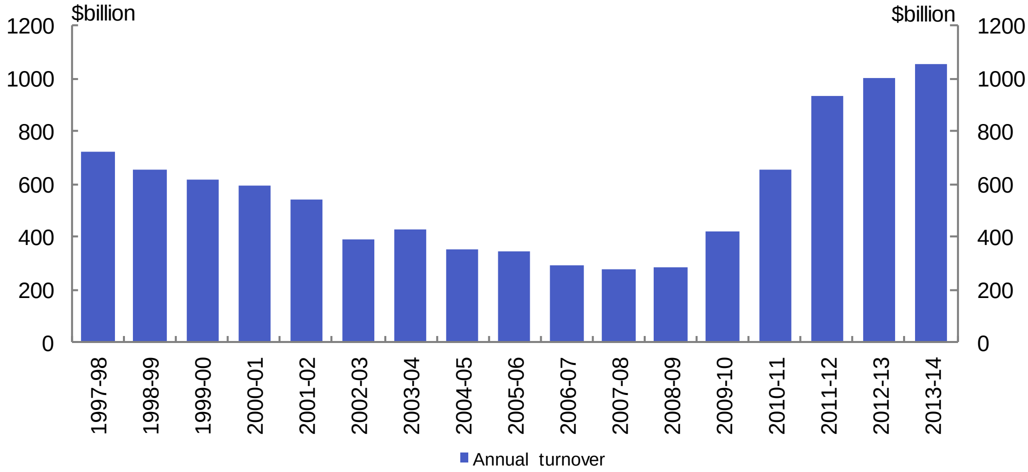
The budget underlying cash deficit for 2013-14 was higher than estimated at the time of the 2013-14 Australian Government Budget due to lower than forecast taxation revenue and increased spending, which included a grant payment of $8.8 billion to the RBA to increase the RBA's capital reserve. The larger than expected budget financing task was managed primarily by increasing Treasury Bond issuance.

Market liquidity and efficiency

The Treasury Bond and Treasury Indexed Bond markets operated smoothly throughout 2013-14 with liquidity again being maintained throughout the year.

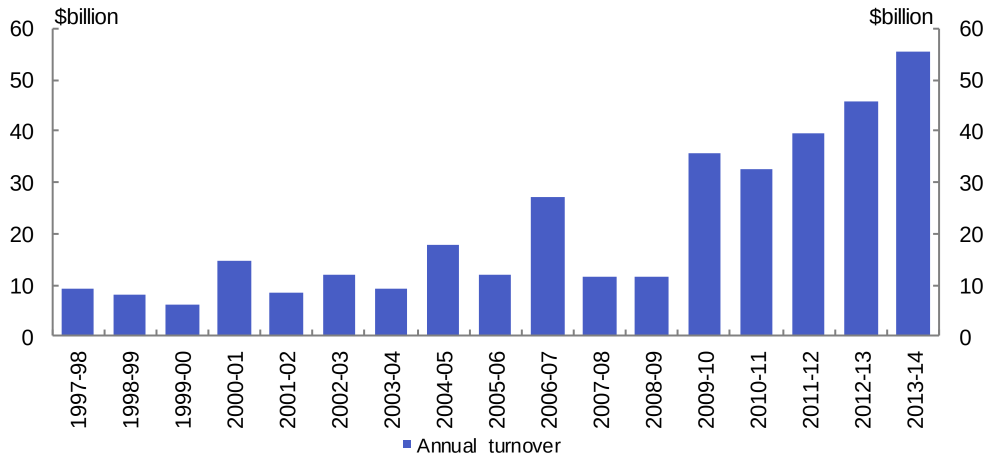
Financial market liquidity has a range of interpretations, however one indicator of liquidity is turnover in the secondary market. Charts 4 and 5 show the evolution of total secondary market turnover from 1997-98 through to 2013-14. Turnover has steadily increased since 2008-09 and was around $1,050 billion per annum in 2013-14 for Treasury Bonds (5 per cent higher turnover than in 2012-13) and $55 billion per annum for Treasury Indexed Bonds (21 per cent higher than in 2012-13). Strong liquidity is attractive to investors and reflects favourably on a sovereign bond market.

Chart 4: Treasury Bond secondary market turnover



Source: Based on data sourced from the Australian Financial Markets Association.

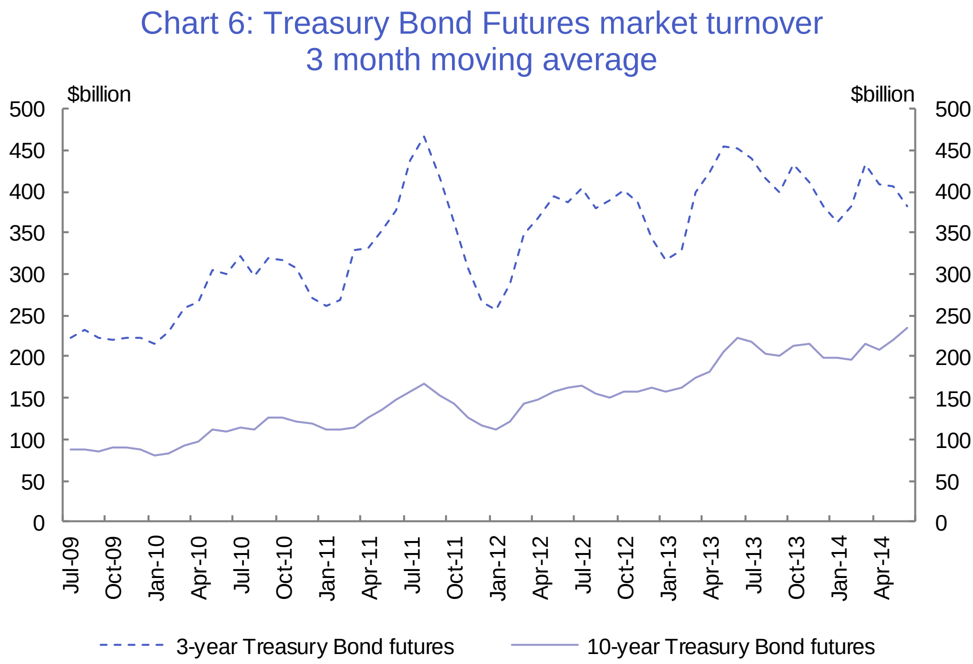
Chart 5: Treasury Indexed Bond secondary market turnover



Source: Based on data sourced from the Australian Financial Markets Association.

Turnover in the Treasury Bond futures market is significantly higher than in the underlying Treasury Bonds. The 3-year Treasury Bond futures contract is amongst the 10 most traded interest rate futures products in the world.[1] Treasury Bond futures continued to display strong liquidity in 2013-14 with the turnover of 3-year Treasury Bond futures contracts increasing by 1 per cent over the previous year and turnover of the 10-year contracts increasing by 20 per cent. Turnover in recent years is illustrated in Chart 6. All Treasury Bond futures contract close-outs in 2013-14 occurred smoothly.

1 Source: Australian Securities Exchange.



Source: Based on data sourced from the Australian Securities Exchange.

The AOFM's securities lending facility allows market participants to borrow Treasury Bonds and Treasury Indexed Bonds for short periods when they are not otherwise available. This enhances the efficiency of the market by improving the capacity of intermediaries to make two-way prices and reducing the risk of settlement failures and supporting market liquidity.

Continued settled market conditions during the year resulted in a relatively low usage of the securities lending facility. The facility was used 18 times for overnight borrowing in 2013-14 compared with 14 times during 2012-13 and 66 times during 2011-12. The face value amount lent in 2013-14 was approximately $135 million compared with $225 million in 2012-13.

Efficiency of issuance

The AOFM used competitive tender, syndication and a conversion offer as the means by which issuance of CGS was undertaken in 2013-14. The use of competitive tenders remains the mainstay of the AOFM's issuance operations.

Tenders held during 2013-14 were well supported. Table 1 summarises the results of Treasury Bond tenders conducted during the year. The results are shown as averages for each half-year and grouped by the maturity dates of the bonds offered.

Table 1: Summary of Treasury Bond tender results

Period	Maturity	Face value amount allocated ($m)	Weighted average issue yield (%)	Average spread to secondary market yield (basis points)	Average times covered
July - December 2013	Up to 2019	17,100	2.9707	-0.56	4.12
	2020 - 2033	18,700	4.0420	-0.01	3.04
January - June 2014	Up to 2019	14,400	3.1501	-0.64	4.48
	2020 - 2033	16,900	4.0324	-0.38	3.84

The average ratio of the volume of bids received to the amount of stock on offer was 3.82 for Treasury Bonds in 2013-14, a slight decrease from 3.99 in 2012-13. The average tender size in 2013-14 of $780 million was higher than previous years due to the large issuance programme. Shorter-dated bond tenders generally received a greater volume of bids.

The strength of bidding at tenders was reflected in issue yield spreads to the secondary market. At most Treasury Bond tenders, the weighted average issue yields obtained were below prevailing secondary market yields.

The average ratio of the volume of bids received to the amount of stock on offer was 4.56 for Treasury Indexed Bonds in 2013-14, an increase from 3.43 in 2012-13. At most tenders, the weighted average issue yields were below prevailing secondary market yields.

Full tender details are available in Part 5 of this annual report.

Cash management

Objective

The AOFM manages the daily cash balances of the Australian Government in the Official Public Account (OPA).[2] The AOFM's primary objective in managing these balances is to ensure that the Government is able to meet its financial obligations as and when they fall due. Other objectives are to minimise the cost of funding the daily cash balances and to invest excess cash balances efficiently. In minimising cost, the AOFM seeks to avoid any use of the overdraft facility provided by the RBA.[3]

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2 The Official Public Account is the collective term for the Core Bank Accounts maintained at the RBA for Australian Government cash balance management.

3 The overdraft facility is more costly than equivalent short-term borrowing (for example, issuance of Treasury Notes). The terms of the facility provide that it is to cover only temporary shortfalls of cash and is to be used infrequently and, in general, only to cover unexpected events.

Achieving the objective

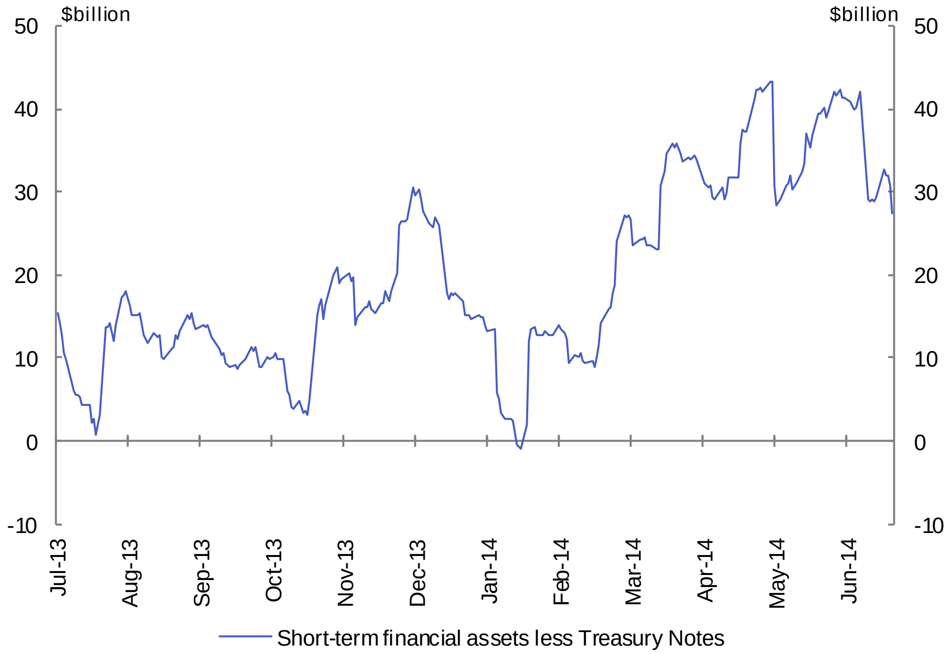
Achieving the cash management objective involves undertaking appropriate short-term investments and debt issuance.

Cash balances not required immediately were invested in term deposits at the RBA, with the magnitudes and tenors of the term deposits determined by the AOFM. Maturity dates of term deposits were selected to efficiently finance large outlays. Interest rates for term deposits at the RBA reflect the rates earned by the RBA in its open market operations.

Treasury Notes are issued to assist with management of the within-year funding requirement. The volume of Treasury Notes on issue ranged from zero to $10 billion during 2013-14.

The size and volatility of the within-year funding requirement are indicated by changes in the short-term financial asset holdings managed by the AOFM, after deducting Treasury Notes on issue. Chart 7 shows movement in the funding requirement in 2013-14.

Chart 7: Within-year funding requirement 2013-14



Performance

The objective of meeting the Government's financial obligations as and when they fall due was met, with the overdraft facility provided by the RBA accessed only twice in 2013-14 (in September 2013 and June 2014, with the facility cleared the next business day).

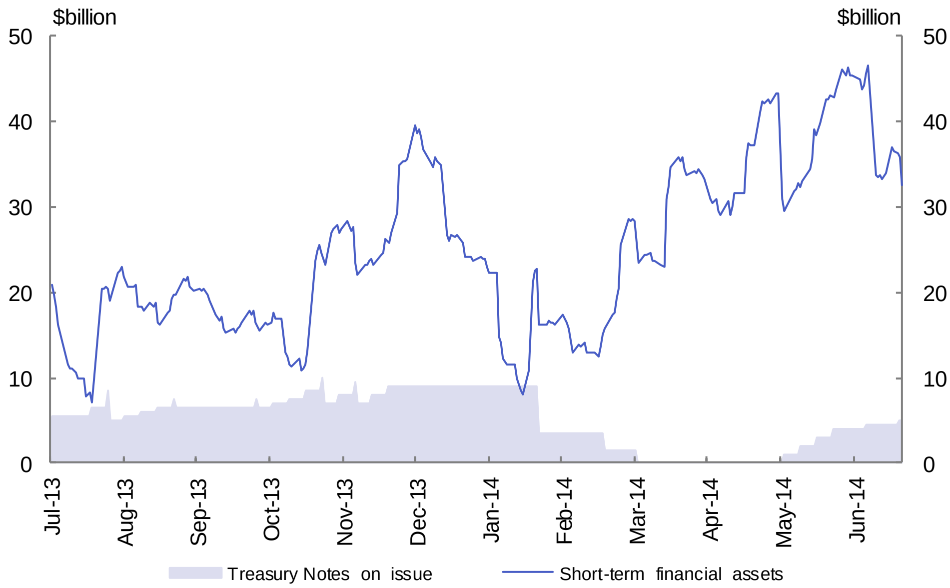
During 2013-14, the AOFM placed 304 term deposits with the RBA. The stock of term deposits fluctuated according to a range of factors influencing the AOFM's cash portfolio management needs and decisions. Term deposits ranged from a minimum of $6.5 billion in July 2013 to a maximum of $46.1 billion in June 2014.

The average yield obtained on term deposits during 2013-14 was 2.53 per cent, compared with 3.11 per cent in 2012-13. The decrease in average yield reflects the lower average level of interest rates that prevailed during 2013-14.

A total of $19.5 billion of Treasury Notes were issued in 2013-14 (in face value terms). The tenders were well supported with an average coverage ratio of 3.85. Yields averaged around 19 basis points less than bank bill yields of corresponding maturities (compared to 14 basis points less than bank bill yields in 2012-13). Yields were on average around three basis points lower than Overnight Indexed Swap rates for corresponding tenors. Details are available in Part 5 of this annual report.

The movement in total short-term financial asset holdings managed by the AOFM (OPA cash balance plus term deposits with the RBA), together with the volume of Treasury Notes on issue, during 2013-14 are shown in Chart 8.

Chart 8: Short-term financial asset holdings and Treasury Notes on issue 2013-14

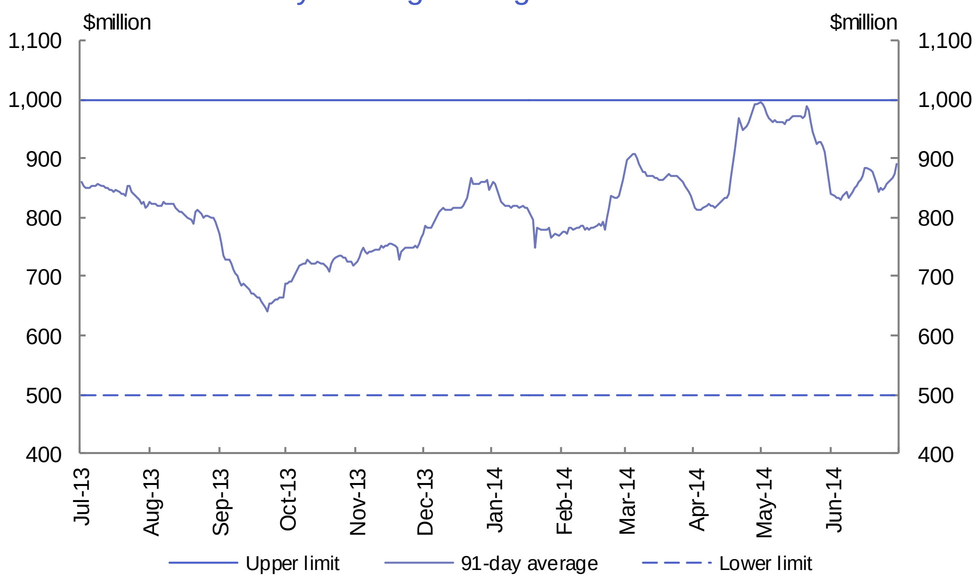


In undertaking its cash management activities, the AOFM was required to maintain the 91-day moving average of the daily OPA cash balance within operational limits. In 2013-14, these limits were the same as applied in recent years, with operational upper and lower limits of $1,000 million and $500 million respectively. There is also a Ministerially approved upper limit of $1.5 billion.

The 91-day moving average OPA cash balance was maintained within operational limits, and within the Ministerial limit, throughout the year.

Movements in the 91-day rolling average OPA cash balance over the year are shown in Chart 9.

Chart 9: 91-day moving average cash balance 2013-14



Minimising debt servicing costs subject to acceptable risk

Objective

In managing the Commonwealth's debt portfolio, the AOFM seeks to minimise debt servicing costs over the medium term at an acceptable level of risk, by which is meant an acceptable level of variability in debt servicing cost outcomes. As debt servicing costs have an impact on the Budget, a greater degree of confidence in estimated cost outcomes is taken to be preferred over alternative outcomes. The AOFM also seeks to maintain liquid bond lines to facilitate the issuance of debt at acceptable cost and to manage the refinancing risk that arises when bond lines mature, while also managing the impact of its issuance on the CGS market.

In order to meet its objective, the AOFM uses cost and risk measures that appropriately reflect the costs and risks faced by a sovereign debt manager. The primary cost measure used is historic accrual debt service cost. This includes interest payments made on CGS, realised market value gains and losses, capital indexation of indexed debt and the amortisation of any issuance premiums and discounts. Total accrual debt service cost can be expressed as a percentage of the stock of debt outstanding to provide the effective yield of the portfolio. This measure of cost is the most appropriate in circumstances where financial assets and liabilities are intended to be held or, in the AOFM's case, to remain on issue until maturity. The use of an historic accrual debt service cost measure excludes unrealised market value gains and losses.

An alternative measure of cost is 'fair value', which takes account of unrealised gains and losses resulting from movements in the market value of physical debt and assets. Debt service cost outcomes are presented in the AOFM's financial statements on this basis. A comprehensive income format is used that allows revenues and expenses on an historic basis to be distinguished from the effects of unrealised market value fluctuations, that is 're-measurements'. Fair value is useful in circumstances where it is possible that changes in market value may be realised in the future.

Variability in cost outcomes, or risk, can be measured in several ways. The AOFM calculates and compares several metrics to assess risk. In general, an acceptable level of risk can be characterised as an acceptable level of variation in cost outcomes over time. Debt issuance decisions made today have an impact on the variability of future cost outcomes because of their influence on the maturity profile of the portfolio, and hence the amount of debt that needs to be refinanced and therefore 're-priced' through time.

Achieving the objective

The AOFM influences the cost and risk profile of the portfolio primarily through its decision making on the composition and maturity structure of the debt securities it issues. These decisions are framed through an annual debt issuance strategy approved by the Treasurer, which identifies the overall scale of the issuance task and its breakdown into different instrument classes. Within these broad strategy parameters, the AOFM separately determines issuance weightings (specified as a range) applicable to different segments of the yield curve. Operational issuance decisions such as determining if, when, how much and what lines to issue each week, are made by the AOFM over the course of the year and are influenced by a range of factors including general market conditions, relative value considerations and feedback from market intermediaries. It is the AOFM's standard practice to regularly test the ongoing suitability of its overarching strategy with the AOFM Advisory Board, which is chaired by the Secretary to the Treasury. Strategic decision-making regarding the portfolio is supported by an ongoing research programme focused on exploring the cost and risk characteristics of alternative portfolio structures and issuance strategies. Informed by this research and related judgments, the AOFM continued to lengthen the nominal debt portfolio in 2013-14.

Chart 10: Treasury Bond issuance average yield and term to maturity

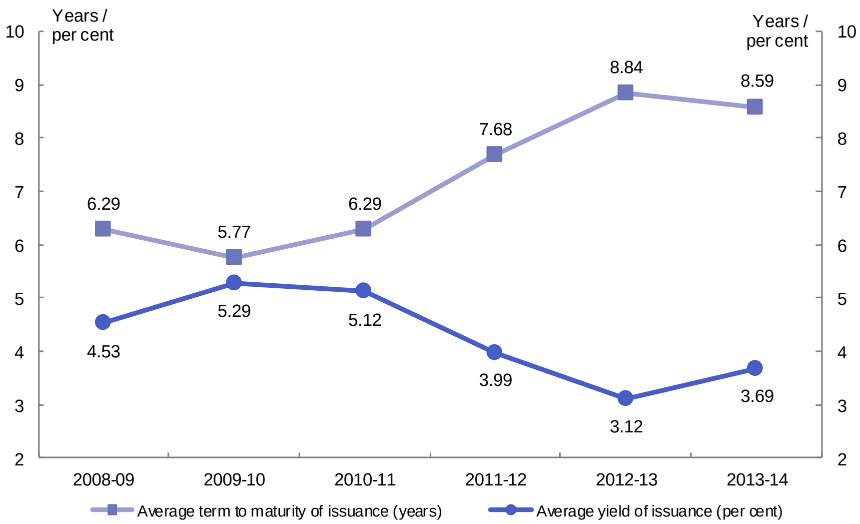


Chart 10 shows that the AOFM's issuance of Treasury Bonds undertaken in 2013-14 had an average term to maturity of 8.59 years and a funding cost of 3.69 per cent. This had the effect of simultaneously lengthening duration and average term to maturity while lowering the effective cost of funds on the Treasury Bond portfolio as a whole. All else being equal, longer-dated issuance reduces uncertainty in future funding costs, however, this will typically come at a higher cost than short-dated issuance.

Chart 11: Treasury Bond portfolio modified duration, average term to maturity and cost of funds

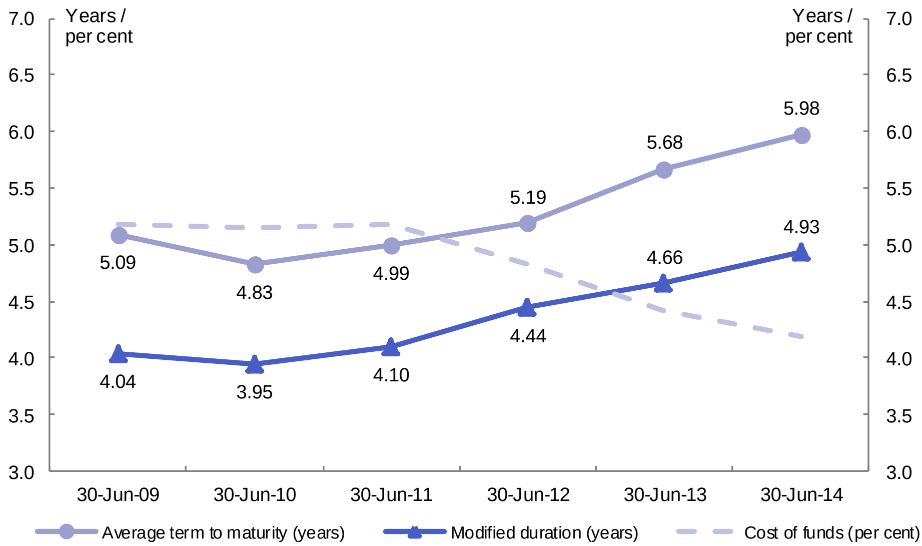
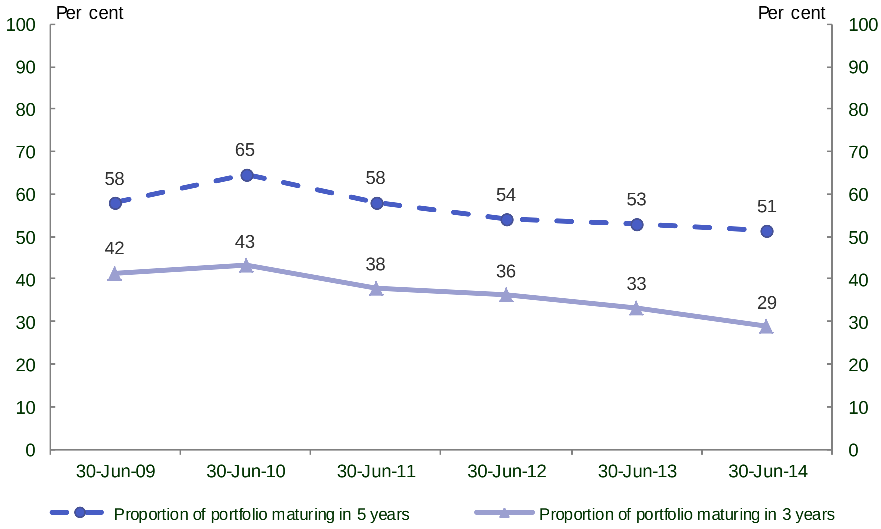


Chart 11 shows how both duration and average term to maturity of the Treasury Bond portfolio increased throughout 2013-14 by 0.3 years to 5.98 years and 4.93 years respectively. Meanwhile, the average yield on new issuance lowered the effective cost of funds on the Treasury Bond portfolio from 4.41 to 4.19 per cent. This outcome was influenced by several factors, not least the continuing favourable funding environment with low outright yields and strong investor demand for CGS.

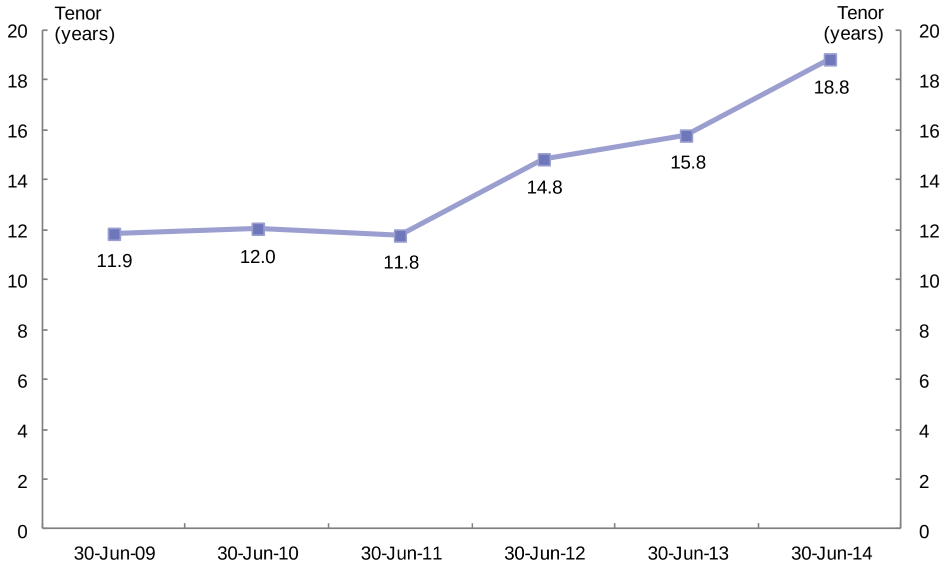
By lengthening issuance in a low interest rate environment, the AOFM has been able to cost-effectively reduce the inherent risk levels of the portfolio. That is to say, the AOFM now has greater certainty around future debt servicing cost outcomes (because funding has been locked in over a longer time horizon), while future gross borrowing programmes will be generally smaller as less issuance will need to be allocated to refinancing maturing debt. Chart 12 demonstrates the progressive decline in refinancing risk in terms of the proportion of the Treasury Bond portfolio maturing within 3- and 5-year windows.

Chart 12: Treasury Bond maturity profiles



A key component of the AOFM's lengthening strategy in 2013-14 was the launch of the new April 2033 bond line. The new line represented the third consecutive year where the AOFM has extended the yield curve, as shown in Chart 13. Notably, the issuance of the 2033 bond line established a new 20-year benchmark for the nominal CGS curve. The AOFM will maintain this benchmark and intends to adopt a pattern of issuing slightly beyond 20 years in order to allow time for successive bond lines to roll in before being replaced. The creation of a 20-year benchmark and the resulting pattern of maturities across the curve will reduce the need to separately maintain a 15-year benchmark.

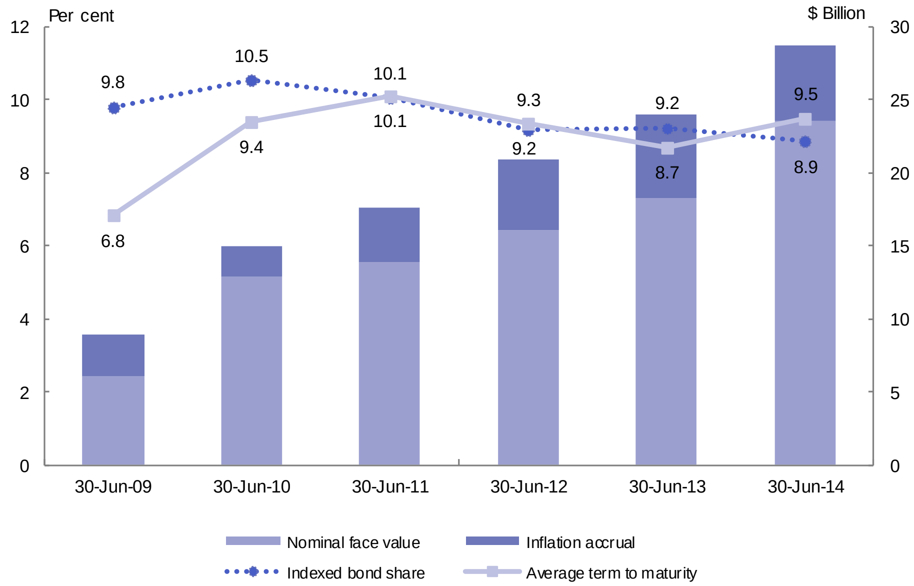
Chart 13: Longest active Treasury Bond line



The AOFM's alternative long-term funding instruments to Treasury Bonds are Treasury Indexed Bonds. Indexed bonds, with a capital value adjusted periodically with changes in the Consumer Price Index, typically attract a different class of investor to nominal bonds and are a source of diversification in the AOFM's funding base. The AOFM re-commenced issuance of indexed bonds in 2009-10 following an extended period of absence from this segment of the market. It has issued regularly in the period since. Indexed bonds now comprise around 9 per cent of the long-term funding base. While the indexed portfolio has been relatively stable as a share of total debt, in absolute terms the stock of indexed bonds has been growing steadily (as shown in Chart 14).

Chart 14 shows that the average term to maturity of Indexed Bonds is currently around 9.5 years, which is broadly in line with the average across the last five financial years (since the AOFM re-entered the market). There were two significant events during the year: the extension of the curve with a new 2035 indexed bond line, and an offer for investors to convert existing 2015 holdings into the newly issued 2018 bond line. There was a strong take-up of the conversion offer, with around $2 billion face value of 2015 indexed bonds being converted into holdings of 2018 indexed bonds. This has reduced the refinancing task for the 2015 bond line to just over $1 billion in face value terms.

Chart 14: Treasury Indexed Bond volume, average term to maturity and share of long-term funding base



Performance

Reducing debt servicing cost at an acceptable level of risk

The debt servicing cost[4] of gross debt managed by the AOFM in 2013-14 was $13.58 billion. This represented a cost of funds of 4.42 per cent for the financial year. Table 2 provides further details of the cost outcomes for the combined portfolio by instrument and portfolio for 2012-13 and 2013-14.

The debt servicing cost of gross debt increased in dollar terms by $1.36 billion compared to the previous year. This was due to an increase in the average volume of debt on issue from $266.65 billion in 2012-13 to $307.28 billion in 2013-14. In percentage terms however, the funding cost of gross debt declined by 16 basis points (4.58 per cent to 4.42 per cent) during 2013-14. This improvement was principally driven by the issuance of new bonds through the year at yields that were below the average of pre-existing (and maturing) debt. Lower rates also reduced the yield on funds invested in term deposits from 3.11 to 2.53 per cent and RMBS investments from 4.62 to 4.15 per cent.

4 Debt servicing cost includes net interest expenses (measured on an accruals basis and includes realised gains and losses on the disposal of assets or liabilities) plus foreign exchange revaluation gains and losses (now minimal). Unrealised changes in the market valuation of domestic debt and assets are not part of this measure.

The return on gross assets for the period was just over $1 billion, an increase of $214 million compared to 2012-13. The interest income from RMBS actually declined as the portfolio matured and sales were made. Income from state housing advances normalised in 2013-14 after declining sharply last year due to a Government decision to waive $320 million in state housing advances.[5]

The net servicing cost of the combined portfolio of debt and assets was $12.53 billion. This was higher in dollar terms compared to 2012-13, due to the volume of debt on issue being higher over the course of the year. The 2013-14 net servicing cost represents 4.59 per cent of the combined debt and asset portfolio. This was an improvement on the 2012-13 result of 4.79 per cent, which confirms that significant cost savings were achieved during 2013-14 by taking advantage of the low interest rate environment. The reduced servicing cost in percentage terms was complemented by an increase in asset returns, in particular the earnings on state housing advances returning to normal levels.

The difference between the return on gross and net CGS debt narrowed to 17 basis points in 2013-14 from 21 basis points in 2012-13. This was despite higher average term deposit holdings and lower returns through the year, which would normally have increased the gap. The fact that it has narrowed can be primarily attributed to the impact of the 2012-13 waiver of a component of the state housing advance balances, which inflated the gap in that year.

5 State housing advances are loans that reside in the AOFM's administered balance sheet. The waiver of this debt generated a realised loss in 2012-13, equivalent to the book value of the loans at disposal, of $284 million. See *2012-13 AOFM Annual Report*, page 27.

Table 2: Commonwealth debt and assets administered by the AOFM

	Interest expense		Book volume		Effective yield	
	2012-13	2013-14	2012-13	2013-14	2012-13	2013-14
	$ million		$ million		per cent per annum	
Contribution by instrument						
Treasury fixed coupon bonds	(10,570)	(11,811)	(228,365)	(274,666)	4.63	4.30
Treasury inflation indexed bonds	(1,174)	(1,650)	(22,872)	(27,661)	5.13	5.97
Treasury notes	(481)	(122)	(15,411)	(4,942)	3.12	2.46
Foreign loans (a)	(1)	(0)	(5)	(6)	18.44	6.89
Gross physical CGS debt	(12,225)	(13,583)	(266,654)	(307,275)	4.58	4.42
Term deposits with the RBA	500	608	16,060	23,996	3.11	2.53
Investments in bank paper	-	-	-	-	0.00	0.00
Term investments (c)	-	-	-	-	0.00	0.00
RMBS investments	478	321	10,345	7,729	4.62	4.15
State Housing Advances	(135)	128	2,532	2,455	-5.32	5.20
Gross assets	843	1,057	28,937	34,180	2.91	3.09
Net CGS debt	**(11,383)**	**(12,527)**	**(237,717)**	**(273,094)**	**4.79**	**4.59**
Contribution by portfolio						
Long-Term Debt Portfolio	(11,745)	(13,462)	(251,243)	(302,332)	4.67	4.45
Cash Management Portfolio	19	486	649	19,054	2.89	2.55
RMBS Portfolio	478	321	10,345	7,729	4.62	4.15
Housing Advances Portfolio	(135)	128	2,532	2,455	-5.32	5.20
Total debt and assets	**(11,383)**	**(12,527)**	**(237,717)**	**(273,094)**	**4.79**	**4.59**
Re-measurements (b)	11,668	(3,671)				
Total after re-measurements	**285**	**(16,198)**	**(237,717)**	**(273,094)**		

Note: Sub totals and totals are actual sum results, rounded to the nearest million dollars. Effective yields are based on actual results before rounding, rounded to two decimal places. Book volume is a through the year average.

(a) Interest expense and effective yield on foreign loans incorporates foreign exchange revaluation effects.

(b) Re-measurements refer to unrealised gains and losses from changes in the market valuation of financial assets and liabilities.

Movements in market interest rates increased the market value of the portfolio in 2013-14. As a result, unrealised losses from re-measurements amounted to $3.67 billion. This compares to a gain of $11.67 billion in the previous year. The re-measurement loss was primarily driven by a $2.99 billion increase in the market value of Treasury Bonds, which constitute the vast majority of the portfolio. As the bond prices driving these re-measurements move in opposite directions to bond yields, it can be seen that the same favourable, low interest rate environment that prevailed through 2013-14 was also the driver of this negative re-measurement impact.

As re-measurement items are highly volatile from one year to the next, they have no bearing on the AOFM's debt issuance strategy. Indeed were the AOFM to adopt a strategy designed to minimise the 'noise' from re-measurements, issuance would be limited to only very short-term debt securities, for example Treasury Notes, creating a portfolio structure that would maximise expected variability in debt servicing costs when measured in cash, accrual and public debt interest terms while also maximising exposure to refinancing risk. In practice, the AOFM has been seeking to reduce refinancing risk by allocating a greater proportion of issuance to long dated lines. In 2013-14, over half of all new issuance was allocated to maturities underpinning the 10-year Treasury Bond futures contract or longer maturities.

Residential mortgage-backed securities

Objective

The Australian residential mortgage-backed securities (RMBS) market is acknowledged as a critical source of funding for smaller mortgage lenders. The global financial crisis that started in 2007-08 reduced the availability of funding through the Australian RMBS market, which limited mortgage lenders' access to funding.

During the period October 2008 to April 2013, the AOFM was directed to invest up to $20 billion in eligible RMBS.

On 10 April 2013, the Treasurer directed the AOFM to cease investment in new RMBS, but the Direction continued to allow the AOFM to consider sale opportunities. The AOFM has since been managing the existing portfolio to maturity and has sold RMBS to assist with price discovery or to adjust the portfolio in line with the Directions.[6]

Achieving the objective

The Australian RMBS market continued to strengthen throughout 2013-14 following on from the relatively buoyant conditions of 2012-13. Prime RMBS issuance for the year reached the highest volumes since 2008 and, as further indication of strong investor demand, several transactions were oversubscribed and up-sized. Other positives included relatively strong offshore demand and tightening margins. Consistent with the Treasurer's Directions issued in April 2013, the AOFM continued to manage the existing portfolio and undertook periodic sales to assist with price discovery and/or to adjust the portfolio in line with Directions. Sales undertaken in 2013-14 are summarised in the following table.

6 Full details of each Direction are available on the AOFM website, http://aofm.gov.au.

Table 3: RMBS divestments for 2013-14

TRANCHE	AMORTISED FV ($m)	CLEAN VALUE ($m)	GAIN ($m)
Oct-13			
IDOL 2011-1 A1	99.71	100.51	0.80
IDOL 2012-1 A1	75.80	77.14	1.34
Feb-14			
APOLLO 2011-1 AB	61.08	63.00	1.92
APOLLO 2012-1 AB	16.50	17.50	1.00
CONQUEST 2010-2 AB	4.97	4.99	0.02
FIRSTMAC 1-2009 AB	40.50	40.62	0.12
FIRSTMAC 1-2010 AB	21.36	21.58	0.22
HBS 2011-1 AB	17.87	18.06	0.18
PINNACLE 2010-1 AB	10.63	10.74	0.11
PROGRESS 2010-1 AB	26.94	27.15	0.20
PROGRESS 2012-1 AB	29.33	30.78	1.45
RESIMAC 2009-2 AB	9.11	9.15	0.04
RESIMAC 2011-1 AB	9.05	9.08	0.03
TORRENS 2010-3 AB	14.07	14.15	0.07
TORRENS 2011-1 AB	27.37	27.50	0.13
WIDE BAY 2009-1AB	0.74	0.74	0.00
WIDE BAY 2010-1 AB	21.81	22.08	0.27
Mar-14			
CHALLENGER 2009-1 AB	13.73	13.74	0.01
LIBERTY 2010-1 AB	10.38	10.40	0.02
FIRSTMAC 2-2011 AB	11.16	11.70	0.54
FIRSTMAC 1-2012 AB	12.61	13.40	0.79
Jun-14			
PINNACLE 2010-1 A2	74.75	75.50	0.75
GBS 4 A1	37.00	37.40	0.40
LIGHT TRUST 3 A3	176.38	178.00	1.62
BARTON 2011-1 A2	49.54	50.10	0.56
Total	**872.41**	**885.00**	**12.59**

Note: Clean Value provides a measure of market value, adjusting for any accrued interest that has yet to be paid.

In February and March 2014, the AOFM divested the entirety of its mezzanine or AB note holdings, which made up slightly more than five per cent of the overall portfolio, or $359 million, in amortised face value terms. Due to the relatively high coupon margins on some of these notes, and the improvement in valuations for this type of note in particular, the AOFM booked a gain on disposal of around 1.99 per cent of the amortised face value of the notes sold. In June 2014, further improvements in market conditions enabled the AOFM to divest a cross section of RMBS from the credit union and building society sector, with weighted average lives between 2.0 years and 4.2 years. In this case, the sale of around $338 million of notes was sold to produce a gain on disposal of around 0.98 per cent of their amortised face value.

In summary, conditions in 2013-14 allowed the AOFM to sell a total of around $872 million in RMBS notes, with a gain on disposal of around $12.6 million, or 1.44 per cent of the amortised face value of the notes sold. This compares with sales between March 2010 and the end of 2012-13, in which the AOFM sold a total of around $629 million worth of notes, in amortised face value terms, with an associated gain on disposal of $5.3 million, or 0.84 per cent of the value of the notes sold.

Performance

Due to both sales and capital amortisation, the book value of the portfolio reduced in size from $9.1 billion to $6.0 billion over the course of the financial year. Furthermore, the average margin over the one month bank bill rate (weighted by each of the AOFM's investments) for the book outstanding as at 30 June 2014 fell by six basis points over the financial year to 127 basis points, due largely to the divestment of all remaining higher yielding mezzanine notes.

Interest income in 2013-14 was $308.4 million. In addition, sales through the year contributed a further $12.6 million in incremental income. Total accrual income of $321.0 million represented an annualised return of 4.15 per cent on the portfolio's average book value of $7.7 billion.

Losses or gains in the mark-to-market value of the portfolio change with prevailing conditions and therefore vary at any particular point in time. These are not realised returns and so are excluded from the accrual returns, but are included as re-measurements within the AOFM's comprehensive accounting treatment.

The RMBS securities held by the AOFM are valued using indicative 'bid' margins for secondary market trading as estimated by an independent valuation service provider. The RMBS portfolio was valued at $6.1 billion as at 30 June 2014. The cumulative unrealised gain on the portfolio was $32 million as at the end of the financial year, an improvement of around $15 million over the year before.[7] Thus, the total return on the RMBS portfolio for 2013-14, including re-measurements, was around $336 million, or around 4.35 per cent of the portfolio's average book value.

Further information on the AOFM's investments in RMBS up to 30 June 2014 is available in Part 5 of this annual report.

Investor relations

Objective

The AOFM investor relations activities contribute to meeting the budget financing task in a cost effective manner by focusing on growth and diversification of demand for CGS.

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7 Were the AOFM to use 'mid' rates for valuation purposes, the cumulative unrealised gain would be expected to be around $40 million to $45 million higher. When sales have been undertaken, they have typically been achieved at levels that are better than mid-market, from the AOFM's perspective.

This involves informing and updating new and existing institutional investors about the Australian economy, the CGS market and the AOFM's issuance activities. The strategy also focuses on managing the relationships with existing long term investors as well concentrating on potential or new investors, thus encouraging further diversity in the investor base.

A diverse investor base can benefit the CGS market through added liquidity from trading supporting issuance and achieving a lower cost of borrowing through a higher and more stable aggregate demand. The CGS market continues to attract a wide range of investors from across different geographies, sectors and investment policies.

Outcomes

The AOFM continued to maintain an understanding of investors' mandates, strategies and perceptions regarding the CGS market through market engagement. Engagement with investors was achieved via a range of regular activities such as one-on-one meetings, presentations and through group forums (typically 'roundtable' events). These activities are summarised in Table 5.

Table 5: Summary of investor relations activities in 2013-14

Activity	Details
Conferences, speaking engagements and investor roadshows	15 events.
Approximate total audience size: Large Presentations	400 attendees.
Individual meetings	124 investor meetings.
Hosted roundtable/small presentations	3 presentations with 27 investors.
Individual cities visited	27 cities.
Two AOFM staff members travel on each overseas trip	CEO, Head of Investor Relations, Director of Financial Risk, Head of Portfolio Strategy and Research, Senior Analyst from Investor Relations, Senior Dealer from Treasury Services.
Hosting banks: Investor roadshows	ANZ, Barclays, Citi, Commonwealth Bank of Australia, Deutsche Bank, JP Morgan, Royal Bank of Canada, UBS, Westpac.
Hosting banks at Australian Government Fixed Income Forum, Tokyo	ANZ, Citi, Commonwealth Bank of Australia, Daiwa Securities, Deutsche Bank, JP Morgan, Nomura, UBS, Westpac.

Consistent with past years, the AOFM visited a range of centres of international financial importance, meeting with investors familiar to the AOFM as well as new and potential investors. Opportunities to present or speak at investor conferences continued to prove an efficient means of updating the market.

In 2013-14, the AOFM undertook more investor related visits and presentations than the previous year, holding around 20 per cent more meetings. Overall, this resulted in the AOFM holding 124 face to face meetings through the year (with 34 of these as 'first time' investor engagements), 26 more than in 2012-13. The regions visited were throughout Europe, the US and Asia. Table 6 provides a timeline of the investor engagement activities undertaken during the year.

Table 6: Timeline of investor engagement activities in 2013-14

Period	Details
September 2013	South East Asia: 18 investor meetings.
October 2013	Paris: OECD Sovereign Debt Managers Conference, 1 luncheon presentation to 12 attendees. United Kingdom/France/Luxembourg: 13 investor meetings.
November 2013	North Asia: 23 investor meetings. Sydney: CBA Fixed Income Conference, 1 presentation to 80 attendees, participated in the Kanga News Round Table. China: 4 investor meetings.
December 2013	Tokyo: Australian Government Fixed Income Forum, 1 presentation to 53 attendees. Sydney: 1 investor meeting.
February 2014	Sydney: Westpac Inflation Linked Roundtable with 9 attendees. Hong Kong: Official Monetary and Financial Institutions Forum Conference, 1 paper given, 2 investor meetings. Paris: OECD Sovereign Debt Managers Conference. Middle East stopover: 1 investor meeting. Sydney: ANZ Central Bank and Sovereign Wealth Fund Conference, 1 presentation to 100 attendees, 4 investor meetings.
March 2014	Canberra: Deutsche Bank Investor Mission, 1 presentation to 30 attendees.
March/April 2014	Northern/Eastern Europe: 17 investor meetings.
May 2014	North America: 26 investor meetings.
June 2014	Sydney: Australian Business Economists luncheon, CEO speech to 100 attendees. Sydney/Melbourne/Brisbane: 15 investor meetings.

A new activity undertaken by the AOFM this year was to hold the Australian Government Fixed Income Forum (Forum) in Tokyo. The event was hosted by the AOFM at the Australian Embassy in December 2013, and included presentations from the state government issuers of New South Wales, Victoria, Queensland and Western Australia. Tokyo represents the single largest concentration of investors in the CGS market.

The Forum was opened by the Australian Ambassador to Japan, and proceeded with presentations by the AOFM's CEO, the CEOs of the larger state borrowing authorities and senior officials from the Treasury and the RBA. In arranging the event, the AOFM was supported (logistically) by nine banks that also attended. Based on a survey held on completion of the Forum and on feedback received in the following days, the investors rated the Forum very highly.

Chief Executive Officer Rob Nicholl presents to Australian Government Fixed Income Forum in Tokyo, Japan

Public Register of Government Borrowing

The *Guarantee of State and Territory Borrowing Appropriation Act 2009* requires the AOFM to publish a register recording the beneficial ownership, by country, of all CGS and any Australian State or Territory government securities guaranteed by the Commonwealth.

The Act does not contain any mechanisms to compel the provision of information to the AOFM by the beneficial owners of these securities or persons holding these securities on their behalf. Nominee and custodial services firms have not provided information to the AOFM due to their fiduciary and contractual obligations to clients. Many investors wish for their holdings to remain confidential for commercial reasons.

This situation limits the information available to the AOFM to form an opinion on the extent of beneficial ownership of the securities. Without detail on the country of beneficial ownership, information on the holdings of nominee/custodial firms alone provides a very limited indicator of 'offshore' CGS ownership.

During 2013-14, the AOFM published the register each quarter and following the latest update, the register contains monthly data up to 30 June 2014. The register indicates that around $335.2 billion of CGS, together with State and Territory securities guaranteed by the Commonwealth, were on issue at year end. Country of ownership could be identified for $103.1 billion or 30.8 per cent, of which $55.5 billion was identified as Australian and $47.6 billion was recorded as held offshore. Country of beneficial ownership could not be identified for around $232.1 billion or 69.2 per cent. Most of this unidentified component was held by nominee/custodial firms.

The Australian Bureau of Statistics (ABS) also collects and publishes information on the holdings of securities. The legal powers provided to the Australian Statistician enable the ABS to obtain information from nominee/custodial firms on security holdings; however, there are also set confidentiality requirements that can constrain how and to what extent the ABS publishes such information at the country specific level.

The quarterly ABS publication *5302.0 Balance of Payments and International Investment Position, Australia* indicates that 68.0 per cent of Commonwealth Government Securities were held by non-residents as at June 2014.[8]

The annual ABS publication *5352.0 International Investment Position, Australia* provides information on the country of domicile for portfolio investment in debt securities. This information covers a broader range of debt securities, issued in Australia and overseas, than that covered by the AOFM register (that is, State and Territory securities not guaranteed by the Commonwealth, as well as debt securities issued by financial intermediaries such as banks and those issued by companies).

The publication estimates that there was $969.6 billion of this foreign portfolio investment in debt securities at 31 December 2013. The survey indicated the country of investor domicile breakdown as: the United States, $264.2 billion; United Kingdom, $175.2 billion; Japan, $45.2 billion; Hong Kong, $18.2 billion; Switzerland, $14.1 billion; Singapore, $12.8 billion; Luxembourg, $11.9 billion; Netherlands, $3.9 billion; Germany, $2.9 billion; Belgium, $2.6 billion; France, $2.5 billion; New Zealand, $2.4 billion; Thailand, $1.1 billion; Bermuda, $0.4 billion; Saudi Arabia, $0.3 billion; South Africa, $0.1 billion and China, $0.1 billion. The remainder of holdings were attributed to international bond markets, were unspecified, or were not published for confidentiality reasons.

Information technology operations

The AOFM upgraded its server and switching infrastructure both at its primary and disaster recovery sites during 2013-14. The replacement of this equipment provides the AOFM with improved functionality, additional bandwidth and greater resilience to the core network. The upgrade of this equipment will provide a reliable and resilient platform for growth.

8 Note this does not cover Commonwealth guaranteed securities issued by the State and Territory governments under the Act.

Enterprise risk

The AOFM's Enterprise Risk Management (ERM) framework enables the AOFM to consolidate, evaluate, prioritise and monitor risks from an organisational perspective, and to provide relevant and timely information to the CEO, Executive Group and the Audit Committee in support of their governance and decision-making roles.

Enterprise risks encompass the AOFM's strategic, portfolio and operational risks.

- Strategic risks are managed by the Executive Group and impact on the AOFM's medium to long term strategies.
- Portfolio risks involved in debt issuance, investment and portfolio management are managed pursuant to the AOFM's Financial Risk Management Framework.
- Operational risks relate to business-as-usual activities of the AOFM, and generally arise when opportunities or failures present in relation to internal processes, people, systems, or from external events.

The AOFM manages risks subject to its risk appetite, and cognisant of its business context. The AOFM maintains a culture of prudence and awareness, together with high ethical standards, which are reinforced by regular in-house training and adherence to the Australian Public Service Code of Conduct and the Australian Financial Markets Association (AFMA) Code of Conduct.

Responsibility for the design, implementation and maintenance of risk and assurance activities resides with the Enterprise Risk and Assurance Group. It maintains the AOFM's ERM framework and supports the business in understanding and implementing the framework.

Key enterprise risk activities undertaken in 2013-14 included:

- review and implementation of annual and quarterly enterprise risk assessment processes;
- further integrating the ERM framework into business processes across the AOFM; and
- reviewing the AOFM's risk appetite against the risks identified in its risk register.

The ERM framework is complemented by assurance activities (refer below), which together support the CEO in meeting his obligations to maintain a sound system of risk management and internal control.

Assurance

The AOFM's compliance with external obligations and internal controls and procedures is monitored internally, and these activities are complemented by the use of internal audit services.

Key assurance activities undertaken in 2013-14 included:

- auditing the control effectiveness of: contract management; debt issuance, confirmation and settlement processes; human resources (operational and payroll); the registry services associated with retail exchange trading of CGS (post-implementation); and the domestic debt registry service formerly provided by the RBA;
- internal assurance reviews of the control effectiveness over authorisations, procedures and systems involved in the CGS tender processes (deal capture, settlement and reporting); and change management processes relevant to maintaining the AOFM's treasury system;
- an external review of AOFM compliance with the Government's Protective Security Policy Framework;
- preparation of the annual Certificate of Compliance to test the AOFM's compliance with the financial management framework under the *Financial Management and Accountability Act 1997* (FMA Act);
- implementation of an annual compliance assurance plan, with monthly reporting provided to the Executive Group and quarterly reporting provided to the Audit Committee;
- enhancement of the Assurance framework (discussed below); and
- coordinating the transition from the arrangements and delegations under the FMA Act to the *Public Governance, Performance and Accountability Act 2013*.

In July 2013, the AOFM commenced a project to develop and implement an Assurance framework. The Assurance framework seeks to provide assurance in regard to the effective and/or efficient operation of the governance arrangements, risk management and/or control environment of the AOFM. Critical to achieving this is the ability of the framework to provide timely and relevant information to key stakeholders and risk owners to enable them to have confidence in the design and operation of the controls implemented to manage risk.

The Assurance framework is aligned with the ERM framework to facilitate a risk-based approach to assurance activities, and to assist the CEO in meeting his risk management and internal control obligations. The framework has been modelled on better practice, whilst being scaled to meet the needs of the AOFM. The concept for the Assurance framework was endorsed by the Audit Committee in June 2014, with final approval and implementation to occur in the first quarter of 2014-15.

Settlement operations

The AOFM is a low transaction volume, high transaction value environment. In 2013-14, it settled around $55.6 billion of payments of interest and principal on CGS, around $676 billion in financial asset acquisitions (including term deposits with the RBA) and repurchased prior to maturity over $5.1 billion of CGS. The AOFM also ensures that all administered receipts are settled promptly and correctly by its transaction counterparties.

In 2013-14, the AOFM settled all payment obligations on time for its debt and investment management activities. The AOFM did not need to seek compensation from counterparties because of a failure to settle payment obligations in line with their contractual obligations.

In February 2014, the AOFM assumed the roles of settlement and paying agent for CGS in Austraclear. These roles had been previously performed by the RBA on behalf of the AOFM. However, the AOFM and the RBA have an agreement where settlement activities in Austraclear will be performed by the RBA in the event that the AOFM is unable to do so. The Stand-in agreement also covers activities in Austraclear relating to the purchase and sale of assets.

Agency financial performance

The AOFM recorded an operating surplus on agency activities of $1.60 million for the 2013-14 financial year, comprising total revenue of $12.36 million and expenses of $10.76 million. The surplus in 2013-14 was largely due to lower than anticipated operating costs.

As at 30 June 2014, the AOFM was in a sound net worth and liquidity position, reporting net assets of $25.75 million, represented by assets of $28.12 million and liabilities of $2.37 million.

As at 30 June 2014, the AOFM had unspent appropriations totalling $25.57 million of which $0.10 million was held in cash. Unspent appropriations are available to settle liabilities as and when they fall due and for future asset replacements and improvements.

Cooperation with other debt managers

In 2013-14, the AOFM continued to support the debt management activities of the Papua New Guinea and the Solomon Islands governments. One staff member is seconded to each of these countries to help develop cash and debt management capabilities. In August 2013, debt management officials from the three countries met in Honiara to discuss their experience with debt management over the year and their progress in capacity development.

In May 2014, a senior official from the AOFM met with officials responsible for sovereign debt management from the Canadian Department of Finance and the Bank of Canada in Ottawa.

The sharing of information and perspectives with other sovereign debt managers has contributed positively to the AOFM's knowledge and in particular, has enhanced the AOFM's portfolio research programme.

AOFM

PART 3
MANAGEMENT AND ACCOUNTABILITY

MANAGEMENT AND ACCOUNTABILITY

Corporate governance

The Secretary to the Treasury (Secretary) has responsibility for specific authorities over the AOFM's activities and is responsible for advising the Treasurer on Government policy relating to debt management and investment activities. The Secretary approves detailed debt management and investment policies, approves policy limits and addresses any breaches of those limits. In discharging his responsibilities, the Secretary is advised by the Chief Executive Officer (CEO) and the AOFM Advisory Board.

The CEO of the AOFM is responsible for the day-to-day management and direction of the AOFM. The CEO exercises powers authorised by the Treasurer and the Secretary for debt creation and issuance, investment, portfolio management and management of the AOFM's staff. The CEO has final responsibility for all aspects of the financial management of the AOFM (which is treated separately from the financial management of the Treasury as the AOFM is a prescribed agency under the *Financial Management and Accountability Act 1997* (FMA Act)). The AOFM reports to the Treasurer on issues pertaining to the management and performance of the portfolio, prepares this annual report for presentation to the Parliament and provides information about its activities on its website.

AOFM Advisory Board

The AOFM Advisory Board provides advice to the Secretary on debt management policy and the operational strategy and performance of the AOFM. The Board does not possess executive powers or decision-making authority. The Advisory Board members as at 30 June 2014 were:

- Dr Martin Parkinson PSM, Secretary to the Treasury, Chair;
- Rob Nicholl, CEO, AOFM;
- Rosemary Huxtable, Deputy Secretary, Budget Group, Department of Finance;
- Paul Bide, Consultant;
- Carol Austin, Consultant;
- Nigel Ray, Executive Director, Fiscal Group, the Treasury; and
- Peter Warne, Consultant.

The Advisory Board met on three occasions in 2013-14.

Senior management committees

Several senior management committees operate to assist the CEO in the management of the AOFM and to facilitate communication, coordination and the assessment of risk and compliance management.

Executive Group

The Executive Group advises the CEO on policies and procedures governing the conduct of AOFM operations. Its activities include the review and assessment of the AOFM's risk exposures; monitoring compliance obligations; determining and monitoring the implementation of HR policies; overseeing and advising the CEO on significant work health and safety matters; overseeing the corporate planning process, including internal and aggregate resourcing needs; and advising the CEO on significant corporate matters as they may arise.

Portfolio Strategy Meeting

During 2013-14, regular Portfolio Strategy Meetings were conducted with the purpose of advising the CEO on operational debt policy and financial risk management issues, as well as reviewing deal execution and general financial market conditions. Its membership comprises of the CEO, Director of Financial Risk, Head of Treasury Services, Head of Investor Relations and Head of Reporting and Information Technology (IT), together with other senior staff holding relevant functional responsibilities.

Cash Management Meeting

A meeting is held each week to review the Government's cash position and short to medium term cash flow projections including expected funding needs. The meeting is attended by the CEO, Head of Treasury Services, Director of Financial Risk, Head of Investor Relations, together with other staff from the Treasury Services Unit with responsibility for cash management.

Information Technology Steering Committee

The Information Technology Steering Committee advises the CEO on overall IT system design, structure and security, and monitors IT service availability and security related incidents. It also oversees current and planned IT projects and operations. Its membership comprises of the CEO, Head of Reporting and IT, Chief Financial Officer, Financial Risk Practice Leader, IT Security Advisor, and IT Technical Specialist.

Security Committee

The Security Committee performs an oversight role in respect of security management within the AOFM. Its membership comprises of the CEO, Agency Security Advisor, and IT Security Advisor. The head of the Treasury Security Team is invited to attend ex officio to assist in security harmonisation.

Other elements of the governance framework

Other elements of the AOFM's governance framework include:

- formal delegations, authorisations and directions from the Treasurer of powers under various Acts that provide the legal authority for the conduct of the AOFM's debt and cash portfolio management and related investment activities;
- formal delegations from the Minister for Finance through the *Financial Management and Accountability (Finance Minister to Chief Executives) Delegation 2013*;
- formal delegations from the CEO to staff through the *Chief Executive Instructions* and internal financial delegations;
- financial risk policies, including an Annual (Debt Management) Remit approved by the Secretary;
- annual corporate and business group plans to support delivery of the AOFM's outcome and programme as stated in the *2013-14 Treasury Portfolio Budget Statement*;
- human resource policies and procedures to establish the expectations and obligations of staff in relation to values, ethics and performance;
- enterprise risk and assurance frameworks, including an enterprise risk register and compliance assurance plan to support oversight of the management of risks, operation of controls and compliance with obligations; and
- a fraud risk assessment and fraud control plan that comply with the *Commonwealth Fraud Control Guidelines* and include appropriate fraud prevention, detection, investigation reporting and data collection procedures and processes.

The AOFM has taken all reasonable measures to optimise the management of risks, including to minimise the risk of fraud. Risks are managed within a risk appetite and tolerances established under the Enterprise Risk Management (ERM) framework. This is achieved through the implementation of a framework of internal policies (for matters including, but not limited to, procurement, security and conflicts of interest), internal controls, and within a culture that embraces a heightened level of mindfulness and awareness of the AOFM's obligations and commitments, consistent with the AOFM's governance and legislative frameworks.

Audit

Audit Committee

The AOFM Audit Committee reviews, monitors and recommends improvements to the risk management, internal control and financial reporting processes. Through quarterly meetings, it oversees the audit and assurance programmes, making its assessments based on the information and reports it receives from the AOFM and auditors.

Key activities during 2013-14 included:

- reviewing the operation of the AOFM's risk and internal control environments, including implementation of the ERM framework and enhancement of the Assurance framework;
- endorsement of the AOFM's 2013-14 internal audit plan;
- monitoring actions taken by the AOFM in response to matters raised by auditors and other assurance providers;
- advice on the preparation and review of the AOFM's financial statements;
- monitoring progress of major agency projects; and
- reviewing the AOFM's *Public Governance, Performance and Accountability Act 2013* transition readiness.

Membership as at 30 June 2014 comprised:

- Peter Warne, independent member of the AOFM Advisory Board (Chair);
- David Lawler, independent member;
- Matthew King, General Manager, Financial and Facilities Management Division, Corporate Strategy and Services Group, the Treasury (from March 2014); and
- Samantha Montenegro, Chief Risk and Compliance Officer, AOFM.

Other representatives from the Treasury included Robert Ewing (November 2013 meeting).

The Audit Committee met on four occasions during 2013-14.

External observers at audit committee meetings included the Australian National Audit Office (ANAO) and its outsourced provider (KPMG), and the AOFM's internal auditor (Deloitte Touche Tohmatsu until November 2013, and PricewaterhouseCoopers from December 2013). The AOFM Chief Financial Officer is an invited attendee. The AOFM CEO regularly attends meetings.

Internal auditor

Internal audit coverage is determined using a structured approach to provide comfort around significant risks, processes, systems and regulatory requirements where assurance is determined to be a priority for that period. The Audit Committee endorses the internal audit strategy for CEO approval.

The AOFM's internal auditors undertook the following audits during 2013-14:

- contract management;
- a post-implementation review of retail exchange trading of Commonwealth Government Securities (CGS);
- human resources (operational and payroll);
- debt issuance, confirmation and settlements processes; and
- a post-implementation review of retail exchange CGS registry services.

Internal audit concluded that the control environment within the AOFM was mature, as demonstrated by the nature and type of findings reported. Recommendations made were aimed at enhancing the efficiency and design of the current control environment. The internal auditors also found that the AOFM had appropriate processes in place to ensure that audit recommendations were actioned in a timely manner. At 30 June 2014, recommendations had either been implemented or were in the process of being implemented in accordance with agreed timelines.

Business continuity arrangements

The AOFM has comprehensive business continuity and pandemic plans to ensure that its critical activities can continue in the event of a major disruption or the outbreak of a pandemic. These arrangements include the provision of back up of full IT and related business services that can be implemented when the AOFM's office accommodation is not able to be used, or when AOFM staff are not available to perform key tasks. Business continuity plans were updated and tested during 2013-14.

In addition to business continuity plans, there is also an IT disaster recovery plan which sets out the processes required to restore critical IT-reliant functions in the aftermath of a significant disruption; and an Emergency Procedures Manual to provide for incidents including, but not limited to, those articulated in the Government's Protective Security Policy Framework.

Judicial decisions

In 2013-14, no matters relating to the AOFM were the subject of judicial proceedings, administrative tribunal hearings or consideration by the Commonwealth Ombudsman.

External reports on agency operations

There were no reports in 2013-14 on the operations of the AOFM by the Auditor-General (other than the report on financial statements); a Parliamentary committee; or the Commonwealth Ombudsman.

Management of human resources

Meeting workforce needs

The AOFM was created with a view to building a specialised agency focused on financial operations employing targeted skills in both investment and debt management. The AOFM people systems were designed to stabilise this niche workforce and align it with the wider financial industry. So, although a public sector entity, the AOFM operates in, and orientates its work to, the finance sector. The core business of the AOFM requires close interface with financial market participants and wholesale financial market intermediaries. Financial market operations and concepts affect all roles in the AOFM and these skills contribute to the AOFM's success.

Eighty-six per cent of AOFM staff have degree qualifications, with 23 per cent holding higher degrees and 19 per cent holding double degrees. Forty-two per cent have professional qualifications related to their role with the AOFM. The retention rate for 2013-14 was 93 per cent, with an average annual retention rate of 91 per cent over the previous five years.

The AOFM is developing a workforce plan to meet medium-term strategic challenges. The plan will be completed and implemented during the next reporting period.

Training and development

The AOFM performance management system sets the main framework to consider training and development activities during each performance cycle. In 2013-14, all staff participated in some form of internal or external training and $4,307 per full-time equivalent (FTE) was paid to external providers for the period. Of the 4.6 days per FTE invested in skill development, 2.5 days per FTE were external courses, 0.5 days were invested in study, and the balance was spent on training in-house. Including participant time, the AOFM's commitment to training and development activity in 2013-14 represented 4.7 per cent of gross salary.

The AOFM workforce

At 30 June 2014, the AOFM employed 39.7 FTE staff under the *Public Service Act 1999*. Table 1 shows this workforce by broadband classification.

Table 1: Operative and paid inoperative staff as at 30 June 2013 and 2014

	Ongoing				Non-ongoing				
	Full-time		Part-time		Full-time		Part-time		
Classification	**Male**	**Female**	**Male**	**Female**	**Male**	**Female**	**Male**	**Female**	**Total**
2014									
AOFM1	0	2	0	1	0	0	0	0	**3**
AOFM2	17	10	0	3	0	0	0	0	**30**
AOFM3	5	1	0	0	0	0	0	0	**6**
AOFM4	1	0	0	0	0	0	0	0	**1**
CEO	1	0	0	0	0	0	0	0	**1**
Total	**24**	**13**	**0**	**4**	**0**	**0**	**0**	**0**	**41**
2013									
AOFM1	1	2	0	1	0	0	0	0	**4**
AOFM2	15	11	0	3	0	1	0	0	**30**
AOFM3	5	1	0	0	0	0	0	0	**6**
AOFM4	1	0	0	0	0	0	0	0	**1**
CEO	1	0	0	0	0	0	0	0	**1**
Total	**23**	**14**	**0**	**4**	**0**	**1**	**0**	**0**	**42**

Note: AOFM broadband classifications are linked to Australian Public Service classifications as follows: AOFM1 corresponds to APS1 to APS4, AOFM2 corresponds to APS5 to EL1, AOFM3 corresponds to EL2 and AOFM4 covers higher level EL2.

Three staff were involved in overseas missions during the year and of these, one was still on deployment at the end of 2013-14. Two positions were staffed to support capacity building in sovereign debt management in Papua New Guinea and the Solomon Islands. These positions are arranged under the *Strongim Gavman Program* and the *Solomon Islands Economic and Public Sector Governance Program* respectively.

Changes to senior management

There were no changes to senior management.

Other staffing changes

Four ongoing staff were recruited during 2013-14. This represents replacement for staff turnover.

There were three staff departures during the year, two of whom were ongoing staff. All of these staff took up positions in the private sector, and two of them went to roles elsewhere in the finance industry. Staff departures represented 7.0 per cent of average staffing levels in 2013-14 (7.2 per cent in 2012-13, and 14.2 per cent in 2011-12 — this latter figure was misreported last year).

Employment arrangements

All non-SES staff have terms and conditions set by the *AOFM Enterprise Agreement 2011-2014* which was negotiated under the Australian Public Service Bargaining Framework.

The CEO has his terms and conditions set by the Secretary through a determination made under subsection 24(1) of the *Public Service Act 1999*.

Remuneration

Pay rates as at 30 June 2014 are shown in Table 2. These rates are set in accordance with the enterprise agreement and take account of relevant market rates. The AOFM set a conservative benchmark against financial services organisations using data provided by the Financial Institutions Remuneration Group. These data cover a wide range of public and private sector financial institutions, including banks, corporate treasuries and State debt management agencies. AON Hewitt provided independent advice in applying the data to the AOFM.

Table 2: AOFM salary ranges

	30-Jun-14	
	Band Low	Band High
Classification	$	$
AOFM1	39,912	72,940
AOFM2	70,896	144,688
AOFM3	168,666	210,833
AOFM4	226,849	283,562

Remuneration within the range for the classification depends on individual performance ratings. Performance appraisals balance what is achieved (outputs) with how those results are obtained (behaviours). Performance-linked bonuses are not paid.

Non-salary benefits provided to staff principally comprise superannuation and support for professional development through study assistance, short courses and payment of job-relevant professional society membership fees. A mobile phone, Blackberry, laptop, or other mobile device may be provided where there is a business need. Executive remuneration is reported in Note 13 of Part 4: Financial Statements.

Work health and safety

Health, wellbeing and safety services are provided by the Treasury under a Service Level Agreement. The AOFM has one Health and Safety Representative who assists staff in accordance with the *Work Health and Safety Act 2011*.

Work health and safety is a standing agenda item at Executive Group meetings.

Flu vaccinations and health assessments were made available to staff in 2013-14. Counselling and related support is available under an Employee Assistance Programme provided by Optum. Additional online resources are provided to all staff to assist with safety and health promotion.

There were no compensable injury claims in 2013-14.

There have been no notices or investigations under Part 10 of the *Work Health and Safety Act 2011.*

Disability reporting

The *National Disability Strategy 2010-2020* sets out a 10 year national policy framework to improve the lives of people with disability, promote participation and create a more inclusive society. A high level two-yearly whole-of-government report will track progress against each of the six outcome areas of the Strategy and present a picture of how people with disability are faring. The first of these reports will be available in late 2014, and can be found at www.dss.gov.au.

Consultants

During 2013-14, eleven new consultancy contracts were entered into involving total actual expenditure of $162,664. In addition, four ongoing consultancy contracts were active during 2013-14, involving total actual expenditure of $91,287. This is summarised in Table 3.

Annual reports contain information about actual expenditure on contracts for consultancies. Information on the value of contracts and consultancies is available on the AusTender website at www.tenders.gov.au.

The AOFM engages consultants where it requires specialist expertise or when independent research, review or assessment is required.

Prior to engaging consultants, the AOFM takes into account the skills, experience and resources required for the task, the skills available internally, and the cost-effectiveness of engaging external expertise. The decision to engage a consultant is made in accordance with the FMA Act and related regulations, including the *Commonwealth Procurement Rules* (CPRs), and relevant internal policies.

Table 3: Consultancy contracts

	2011-12	2012-13	2013-14
Number of consultancy contracts			
New contracts	7	15	11
Ongoing contracts	3	3	4
Expenditure (including GST)			
New contracts	$106,910	$93,060	$162,664
Ongoing contracts	$239,480	$175,160	$91,287

Purchasing

The AOFM's purchasing activities comply with legislative requirements and Government policy, in particular the CPRs.

The CPRs are applied to the AOFM's activities through the *Chief Executive Instructions* and supporting internal policies and procedures.

ANAO access clauses and exempt contracts

Three contracts were let during the reporting period in excess of $100,000 that did not provide for the Auditor-General to have access to the contractor's premises.

One contract was for the syndicated issuance of $2.1 billion of Australian Government Treasury Indexed Bonds (August 2035) in September 2013. The AOFM appointed Westpac Banking Corporation, Deutsche Bank AG (Sydney Branch) and Merrill Lynch (Australia) Futures Ltd as joint-lead managers for the issue.

The second contract was for the syndicated issuance of $5.9 billion of Australian Government Treasury Bonds (April 2033) in November 2013. The AOFM appointed ANZ Banking Group Ltd, Citigroup Global Markets Australia Pty Ltd and UBS AG (Australia Branch) as joint-lead managers for the issue. The AOFM appointed Deutsche Bank AG (Sydney Branch), J.P. Morgan Australia Ltd and Westpac Banking Corporation as co-managers for the issue.

The third contract was for the syndicated issuance of $7.0 billion of Australian Government Treasury Bonds (April 2026) in March 2014. The AOFM appointed Westpac Banking Corporation, Deutsche Bank AG (Sydney Branch), Citigroup Global Markets Australia Pty Ltd and UBS AG (Australia Branch) as joint-lead managers for the issue.

ANAO access clauses were not included in the contracts as the AOFM maintains all relevant information in relation to the contracted services. Under these contracts, $24.75 million (including GST) was paid.

No contract or standing offer has been exempted from being published in the Purchasing and Disposals Gazette on the basis that it would disclose exempt matters under the *Freedom of Information Act 1982*.

AOFM

PART 4
FINANCIAL STATEMENTS

Australian National
Audit Office

INDEPENDENT AUDITOR'S REPORT

To the Treasurer

I have audited the accompanying financial statements of the Australian Office of Financial Management for the year ended 30 June 2014, which comprise: a Statement by the Chief Executive Officer and Chief Financial Officer; Statement of comprehensive income; Statement of financial position; Statement of changes in equity; Statement of cash flows; Schedule of commitments; Administered schedule of comprehensive income; Administered schedule of assets and liabilities; Administered reconciliation schedule; Administered schedule of cash flows; Administered schedule of commitments; and Notes to and forming part of the financial statements, comprising a summary of significant accounting policies and other explanatory material.

Chief Executive Officer's Responsibility for the Financial Statements

The Chief Executive Officer of the Australian Office of Financial Management is responsible for the preparation of financial statements that give a true and fair view in accordance with the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997*, including the Australian Accounting Standards, and for such internal control as is necessary to enable the preparation of financial statements that give a true and fair view and are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on the financial statements based on my audit. I have conducted my audit in accordance with the Australian National Audit Office Auditing Standards, which incorporate the Australian Auditing Standards. These auditing standards require that I comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Australian Office of Financial Management's preparation of the financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Australian Office of Financial Management's internal control. An audit also includes evaluating the appropriateness of

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the accounting policies used and the reasonableness of accounting estimates made by the Chief Executive Officer of the Australian Office of Financial Management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Independence

In conducting my audit, I have followed the independence requirements of the Australian National Audit Office, which incorporate the requirements of the Australian accounting profession.

Opinion

In my opinion, the financial statements of the Australian Office of Financial Management:

(a) have been prepared in accordance with the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997,* including the Australian Accounting Standards; and

(b) give a true and fair view of the matters required by the Finance Minister's Orders, including the Australian Office of Financial Management's financial position as at 30 June 2014 and its financial performance and cash flows for the year then ended.

Australian National Audit Office

Michael J. Watson
Group Executive Director

Delegate of the Auditor-General

Canberra
22 August 2014

AUSTRALIAN OFFICE OF FINANCIAL MANAGEMENT

Statement by the Chief Executive Officer and Chief Financial Officer

In our opinion, the attached financial statements for the year ended 30 June 2014 are based on properly maintained financial records and give a true and fair view of the matters required by the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997,* as amended.

Signed

R Nicholl
Chief Executive Officer
22 August 2014

Signed

P Raccosta
Chief Financial Officer
22 August 2014

Statement of comprehensive income

for the period ended 30 June 2014

	Notes	2014 $'000	2013 $'000
NET COST OF SERVICES			
EXPENSES			
Employee benefits	4A	**6,940**	6,481
Supplier expenses	4B	**3,435**	2,913
Depreciation and amortisation	4C	**377**	380
Write-down and impairment of assets	4D	**6**	2
Total expenses		**10,758**	9,776
LESS:			
OWN-SOURCE INCOME			
Revenue:			
Sale of goods and rendering of services	5A	**473**	516
Other revenue	5B	**411**	383
Total revenue		**884**	899
Total own-source income		**884**	899
Net cost of services		**9,874**	8,877
APPROPRIATION FUNDING			
Revenue from government	5C	**11,479**	11,409
Total appropriation funding		**11,479**	11,409
Surplus (deficit)		**1,605**	2,532
Total comprehensive income		**1,605**	2,532

The above statement should be read in conjunction with the accompanying notes.

Statement of financial position
as at 30 June 2014

	Notes	**2014 $'000**	2013 $'000
ASSETS			
Financial assets:			
Cash and cash equivalents		**100**	100
Receivables	6A	**25,551**	28,664
Total financial assets		**25,651**	28,764
Non-financial assets:			
Property, plant and equipment	7A,7C	**554**	588
Intangibles	7B,7C	**967**	153
Other non-financial assets	7D	**952**	84
Total non-financial assets		**2,473**	825
Total assets		**28,124**	29,589
LIABILITIES			
Payables:			
Supplier payables	8A	**89**	237
Other payables	8B	**200**	183
Total payables		**289**	420
Provisions:			
Employee provisions	9A	**1,945**	1,849
Other provisions	9B	**140**	136
Total provisions		**2,085**	1,985
Total liabilities		**2,374**	2,405
Net assets		**25,750**	27,184
EQUITY			
Retained surplus		**23,858**	22,253
Contributed equity		**1,892**	4,931
Total equity		**25,750**	27,184

The above statement should be read in conjunction with the accompanying notes.

Statement of changes in equity

for the period ended 30 June 2014

	2014 $'000	2013 $'000
RETAINED SURPLUS		
Opening balance	**22,253**	19,721
Changes for period:		
Comprehensive income	**1,605**	2,532
Total retained surplus	**23,858**	22,253
CONTRIBUTED EQUITY		
Opening balance	**4,931**	4,525
Changes for period:		
Contributions by government:		
Capital injection - departmental capital budget	**408**	406
Distributions to owners:		
Return of capital	**(3,447)**	-
Total contributed equity	**1,892**	4,931
Total equity	**25,750**	27,184

Statement of cash flows

for the period ended 30 June 2014

	Notes	**2014 $'000**	2013 $'000
OPERATING ACTIVITIES			
Cash received:			
Appropriations - recurrent		**10,971**	9,181
GST received		**5**	20
Goods and services(a)		**649**	584
Cash used:			
Employees		**(6,832)**	(6,315)
Suppliers		**(4,137)**	(2,874)
GST paid		**(7)**	(12)
Transfers to Official Public Account(a)		**(649)**	(584)
Net cash from (used by) operating activities	11	**-**	-
INVESTING ACTIVITIES			
Cash used:			
Purchase of property, plant and equipment		**(1,167)**	(294)
Net cash from (used by) investing activities		**(1,167)**	(294)
FINANCING ACTIVITIES			
Cash received:			
Appropriations - contributed equity		**1,167**	294
Net cash from (used by) financing activities		**1,167**	294
Net increase (decrease) in cash held		**-**	-
Plus cash held at the beginning of the reporting period		**100**	100
Cash at the end of the reporting period	11	**100**	100

The above statement should be read in conjunction with the accompanying notes.

(a) Non-appropriation receipts are required to be returned to the Official Public Account. They increase the AOFM's available appropriation under section 30 and section 31 of the *Financial Management and Accountability Act 1997* and when subsequently drawn down for use by the AOFM they are recorded as appropriations (recurrent).

Schedule of commitments

as at 30 June 2014

	2014 $'000	2013 $'000
BY TYPE		
Commitments payable:		
Operating leases(a)	**222**	728
Other commitments(b)	**4,401**	1,666
Total commitments payable	**4,623**	2,394
Commitments receivable:		
GST recoverable on commitments	**(8)**	(1)
Total commitments receivable	**(8)**	(1)
Net commitments by type	**4,615**	2,393
BY MATURITY		
Commitments payable:		
Operating leases:		
One year or less	**26**	288
From one to five years	**196**	440
Over five years	**-**	-
Total operating leases	**222**	728
Other commitments:		
One year or less	**1,675**	1,480
From one to five years	**2,726**	186
Over five years	**-**	-
Total other commitments	**4,401**	1,666
Commitments receivable:		
GST recoverable on commitments:		
One year or less	**(2)**	(1)
From one to five years	**(6)**	-
Over five years	**-**	-
Total commitments receivable	**(8)**	(1)
Net commitments by maturity	**4,615**	2,393

Note: Commitments are GST inclusive and where an input tax credit is available to the AOFM, the recoverable GST is reported in Commitments receivable.

(a) Operating leases are effectively non-cancellable and comprise:

Nature of lease	**General description of leasing arrangement**
Lease for office accommodation	• The lease term is for 15 years less one day with no option to renew and lease payments are subject to review on each second anniversary of the lease commencement date (22 December 2000).
Motor vehicle leases	• The novation of lease rental payments over motor vehicles.

(b) Other commitments relate to contractual obligations for the provision of consultancies and contractors, payroll services, market data and news services and service agreements with other parties, including Commonwealth bodies.

Administered schedule of comprehensive income

for the period ended 30 June 2014

	Notes	2014 $'000	2013 $'000
Income before re-measurements			
Interest revenue	17A	**1,044,272**	1,121,487
Other revenue	17B	**349**	40
Total income before re-measurements		**1,044,621**	1,121,527
Expenses before re-measurements			
Grants	18A	**20**	21
Interest expenses	18B	**13,389,975**	12,225,143
Supplier expenses	18C	**23,819**	12,145
Total expenses before re-measurements		**13,413,814**	12,237,309
Gains (losses) before re-measurements			
Net foreign exchange gains (losses)	19A	**78**	(500)
Net realised gains (losses) on financial instruments	19B	**(181,753)**	(278,572)
Total gains (losses) before re-measurements		**(181,675)**	(279,072)
Surplus (deficit) before re-measurements		**(12,550,868)**	(11,394,854)
Re-measurements			
Net market revaluation gains (losses)	20	**(3,670,817)**	11,667,953
Total re-measurements		**(3,670,817)**	11,667,953
Surplus (deficit)		**(16,221,685)**	273,099
Total comprehensive income		**(16,221,685)**	273,099

The above schedule should be read in conjunction with the accompanying notes.

Administered schedule of assets and liabilities
as at 30 June 2014

	Notes	2014 $'000	2013 $'000
ASSETS			
Financial assets:			
Cash and cash equivalents		**622**	622
Investments (under FMA section 39)(a)	21A	**33,175,900**	29,272,165
Receivables	21B	**2,106,076**	2,177,119
Accrued revenue	21C	**383**	394
Total financial assets		**35,282,981**	31,450,300
Total administered assets		**35,282,981**	31,450,300
LIABILITIES			
Interest bearing liabilities:			
Commonwealth Government Securities	22A	**351,288,481**	285,754,725
Other	22B	**93**	93
Total interest bearing liabilities		**351,288,574**	285,754,818
Payables:			
Accrued expenses	22C	**31**	214
Total payables		**31**	214
Total administered liabilities		**351,288,605**	285,755,032
Administered net assets		**(316,005,624)**	(254,304,732)

The above schedule should be read in conjunction with the accompanying notes.
(a) FMA = *Financial Management and Accountability Act 1997*.

Administered reconciliation schedule

for the period ended 30 June 2014

	2014 $'000	2013 $'000
Opening administered assets less administered liabilities	**(254,304,732)**	(241,667,356)
Administered income and expenses:		
Administered income before re-measurements	**1,044,621**	1,121,527
Administered expenses before re-measurements	**(13,413,814)**	(12,237,309)
Administered gains (losses) before re-measurements	**(181,675)**	(279,072)
Re-measurements - net market revaluation gains (losses)	**(3,670,817)**	11,667,953
Administered transfers (to) from Australian Government:		
Special appropriations (unlimited)	**736,734,699**	935,905,474
Transfers to OPA	**(782,213,805)**	(948,815,864)
Change in special account balance	**(101)**	(85)
Closing administered assets less administered liabilities	**(316,005,624)**	(254,304,732)

Administered schedule of cash flows

for the period ended 30 June 2014

	Notes	2014 $'000	2013 $'000
OPERATING ACTIVITIES			
Cash received:			
Interest receipts		**1,026,687**	1,102,879
Other		**2,247**	40
GST refunds		**1,749**	873
Cash used:			
Interest payments		**(15,023,529)**	(12,655,597)
Other		**(27,917)**	(12,805)
Net cash from (used by) operating activities	23	**(14,020,763)**	(11,564,610)
INVESTING ACTIVITIES			
Cash received:			
Capital proceeds from deposits		**669,050,000**	831,350,000
Capital proceeds from residential mortgage-backed securities		**3,075,297**	2,287,118
Repayments from advances and loans		**88,675**	100,248
Cash used:			
Acquisition of deposits		**(676,000,000)**	(837,000,000)
Acquisition of residential mortgage-backed securities		**-**	(160,000)
Net cash from (used by) investing activities		**(3,786,028)**	(3,422,634)
FINANCING ACTIVITIES			
Cash received:			
Capital proceeds from borrowings		**108,126,825**	113,474,440
Other receipts		**1,490**	62
Cash used:			
Repayment of borrowings(a)		**(44,842,317)**	(85,576,784)
Net cash from (used by) financing activities		**63,285,998**	27,897,718
TRANSACTIONS WITH OFFICIAL PUBLIC ACCOUNT			
Cash received from Official Public Account:			
Appropriations		**736,734,660**	935,905,433
Special accounts		**-**	19
Cash to Official Public Account:			
Appropriations		**(782,213,805)**	(948,815,864)
Special accounts		**(62)**	(62)
Net cash from (to) official public account		**(45,479,207)**	(12,910,474)
Net increase (decrease) in cash held		**-**	-
Plus cash held at the beginning of the reporting period		**622**	622
Cash at the end of the reporting period		**622**	622

The above schedule should be read in conjunction with the accompanying notes.

(a) Includes redemption of debt issued on behalf of the States (where relevant).

Administered schedule of commitments

as at 30 June 2014

	2014 $'000	2013 $'000
BY TYPE		
Commitments payable:		
Other commitments(a)	**1,452**	1,950
Total commitments payable	**1,452**	1,950
Commitments receivable:		
Other commitments(a)	**(86)**	(133)
Total commitments receivable	**(86)**	(133)
Net commitments by type	**1,366**	1,817
BY MATURITY		
Commitments payable:		
Other commitments:		
One year or less	**457**	643
From one to five years	**995**	1,307
Total commitments payable	**1,452**	1,950
Commitments receivable:		
GST recoverable on commitments:		
One year or less	**(28)**	(44)
From one to five years	**(58)**	(89)
Total commitments receivable	**(86)**	(133)
Net commitments by maturity	**1,366**	1,817

(a) As at 30 June 2014 the AOFM had no open transactions under its securities lending facility (30 June 2013: nil).

Notes to and forming part of the financial statements

for the period ended 30 June 2014

Note 1: Summary of significant accounting policies

1.1 Basis of preparation of the financial statements

The Australian Office of Financial Management (AOFM), a 'prescribed agency' under the *Financial Management and Accountability Act 1997* (Commonwealth), is a specialised agency responsible for the management of Australian Government debt and financial assets. The AOFM operates on a not-for-profit basis. The financial statements cover the AOFM as an individual entity and are for the reporting period 1 July 2013 to 30 June 2014. They are required by section 49 of the *Financial Management and Accountability Act 1997*, and are general purpose financial statements prepared on a going concern basis.

The financial statements have been prepared in accordance with:

- the Finance Minister's Orders (FMOs) (Financial Statements for reporting periods ending on or after 1 July 2011) made under section 63 of the *Financial Management and Accountability Act 1997* and as amended by the Finance Minister's Amendment Orders;
- Australian Accounting Standards, including Interpretations issued by the Australian Accounting Standards Board (AASB) that apply for the reporting period; and
- other authoritative pronouncements of the AASB, which includes the *Framework for the Preparation and Presentation of Financial Statements*.

The financial statements have also been prepared having regard to guidance produced by the Department of Finance including estimates memoranda, finance briefs, finance circulars, financial management guidance series and accounting guidance notes. The AOFM has made the following departures from this guidance:

- *Finance Brief 31 (Revised) – AASB 7 Financial Instruments: Disclosures Standardisation of market risk sensitivity analysis* advises the use of standard parameters produced by the Department of Finance to determine a reasonably possible change in interest rates for market sensitivity analysis. The AOFM prefers to use a 1 per cent change in interest rates, as it is easily scalable while still being reasonably possible.

Since 2005 the AASB has adopted International Financial Reporting Standards issued by the International Accounting Standards Board (IASB) for the purposes of setting Australian Accounting Standards. In some instances the Australian Accounting Standards are modified for the private and public not-for-profit sectors.

The financial statements have been prepared on an accruals basis under the historic cost accounting convention, as modified by the revaluation of certain classes of financial assets and financial liabilities, certain classes of property, plant and equipment and employee entitlements.

The financial statements are presented in Australian dollars, and values are rounded to the nearest thousand dollars unless disclosure of the full amount is specifically required by the FMOs.

Liabilities and assets which are unrecognised in the Agency Statement of Financial Position or the Administered Schedule of Assets and Liabilities are reported in Note 12 (departmental) and Note 24 (administered).

The continued existence of the AOFM in its present form, and with its present outcome and programme, is dependent on government policy and on continuing appropriations by Parliament for the AOFM's administration and activities.

1.2 Significant accounting estimates and judgments

Subject to one exception, no accounting assumptions or estimates have been identified that have a significant risk of causing a material adjustment to carrying amounts of assets and liabilities within the next reporting period. The residential mortgage-backed securities (RMBS) held by the AOFM are fully amortising instruments. The repayment of principal on each RMBS security is dependent on the payment priorities set out in the issuance documentation and the timing of principal repaid on each RMBS security may vary over its life and cannot be precisely forecasted. For valuation purposes, the repayment profile is estimated to produce a weighted average life for each security. The weighted average life represents a measure of the estimated point in time in which a holder of a security will receive (in undiscounted terms) repayment of 50 per cent of the principal invested. The weighted average life of each security is estimated, including on the basis of actual repayment history where available. The estimated weighted average life is an important factor in the valuation of RMBS securities.

1.3 Statement of compliance with International Financial Reporting Standards

In some circumstances compliance with Australian Accounting Standards will not lead to compliance with International Financial Reporting Standards. Paragraph 16 of AASB 101 *Presentation of Financial Statements* requires that where an entity's financial statements comply with International Financial Reporting Standards, then such compliance shall be made in an explicit and unreserved statement in the notes to the financial statements.

These financial statements and associated notes do not fully comply with International Financial Reporting Standards, due to the application of not-for-profit provisions in AASB 116 *Property, Plant and Equipment* relating to the accounting treatment arising from revaluations.

(a) New Australian Accounting Standards applicable to the reporting period

During 2013-14 the AOFM adopted all applicable Australian Accounting Standards that became effective during 2013-14.

AASB 13 *Fair Value Measurement* became operational in 2013-14 and has had a material effect on the financial statements by requiring new disclosures to assign a 3 level hierarchy for assets and liabilities measured at fair value.

(b) New Australian Accounting Standards applicable in future reporting periods

A number of revised or new Australian Accounting Standards have been issued that are effective for future reporting periods. With the exception of AASB 9 *Financial Instruments* (effective for the 2017-18 financial year) the revisions are not expected to materially affect the AOFM's assets, liabilities, revenue or expenses.

AASB 9 Financial Instruments

The IASB has been progressively replacing the current standard for the measurement and recognition of financial instruments (IAS 39 *Financial Instruments: Recognition and Measurement* (in Australia AASB 139)) with a new standard IFRS 9 *Financial Instruments* (in Australia AASB 9).

AASB 9 currently contains the requirements for the recognition and measurement of financial assets and liabilities and their de-recognition and general hedge accounting. The requirements for amortised cost and impairment, and macro hedge accounting are expected to be incorporated into the standard at a later stage.

Financial assets

Currently, the AOFM classifies its administered financial assets into the following categories: financial assets at fair value through profit or loss; and loans and receivables (which requires measurement at amortised cost). The AOFM determines which classification applies to each class of financial assets on the basis of how it manages the assets and assesses the performance of the financial assets. Where the AOFM's management monitors cost and risk in mark-to-market terms (and not necessarily only in those terms) the AOFM designates the relevant financial assets at fair value through profit or loss.

All of the AOFM's administered financial assets, with the exception of loans to the State and the Northern Territory Governments, are designated at fair value through profit or loss. Loans to the State and the Northern Territory Governments are measured at amortised cost.

AASB 9 establishes new principles for determining the accounting treatment for financial assets. AASB 9 requires that where the business objective of the entity is to hold the instrument to collect its contractual cash flows (rather than trading to earn capital profits) and those contractual cash flows are in the nature of principal and interest on the principal outstanding, the financial asset is to be carried at amortised cost. Otherwise a financial asset is to be carried at fair value through profit or loss. In addition, an entity can elect to carry a financial asset at fair value where carrying it at amortised cost would create an accounting mismatch. Where an entity's objective for holding a financial asset changes so too should the accounting treatment, where relevant. The sale of a financial asset for portfolio management, credit or liquidity reasons may not represent a change of purpose from one of collection of contractual cash flows to one of trading to earn capital profits. Under AASB 9, derivatives are deemed to be held for trading to earn capital profits, and accordingly must be carried at fair value through profit or loss.

The AASB has issued Exposure Draft 230 *Classification and Measurement: Limited Amendments to AASB 9*. The proposed changes seek to clarify the accounting treatment for financial assets, including the creation of a new category of fair value through other comprehensive income. The amendments that may follow after completion of consultations on the exposure draft may have a significant impact on the accounting treatment of AOFM's financial assets. Accordingly, the AOFM will make an assessment of the impact of AASB 9 on its financial assets after that time.

Financial liabilities

Currently, the AOFM classifies its administered financial liabilities into the following categories: financial liabilities at fair value through profit or loss; and other financial liabilities (which requires measurement at amortised cost). The AOFM determines which classification applies to each class of financial liability on the basis of how it manages and assesses the performance of the financial liability.

All of the AOFM's administered financial liabilities, with the exception of debt on allocation to the State and Northern Territory Governments, are designated at fair value through profit or loss. Debt on allocation to the State and Northern Territory Governments is measured at amortised cost.

The classification requirements for financial liabilities remain largely unchanged in AASB 9 from AASB 139. Furthermore, except in limited circumstances (which are not applicable to the AOFM), AASB 9 prohibits the revocation of a previous designation of a financial liability as measured at fair value through profit or loss. Accordingly, the

AOFM will be required to maintain its existing accounting treatment for those financial liabilities it holds when AASB 9 becomes operative.

For financial liabilities carried at fair value through profit or loss, AASB 9 has adopted a revised disclosure for the presentation of unrealised fair value gains and losses due to own credit risk. These changes require the gain or loss to be apportioned between changes in credit risk (recognised in other comprehensive income) and other changes (recognised in profit or loss).

AASB 1055 Budgetary Reporting

From 2014-15 the AOFM will need to disclose budgetary information and variances of actuals from budget and explanations of significant variances.

1.4 Departmental and administered items

Departmental assets, liabilities, revenue and expenses are those items that are controlled by the AOFM and used or incurred to deliver goods and services to the Government, including:

- computers, plant and equipment;
- liabilities for employee entitlements;
- receipts deemed appropriated under the *Financial Management and Accountability Act 1997*; and
- employee expenses and other administrative expenses.

Administered assets, liabilities, revenue and expenses are those items which are controlled by the Government and managed or overseen by the AOFM on behalf of the Government. These items include debt issued to finance the Government's fiscal requirements, investments of funds surplus to the Government's immediate financing needs and investments in residential mortgage-backed securities to support competition in the residential mortgage market and to meet government policy objectives.

The purpose of separating administered and departmental items is to enable assessment of the administrative efficiency of the AOFM in providing services to support the Government.

Administered items are identified separately in the financial statements by shading.

1.5 Revenue (Departmental)

The revenue described in this note is revenue relating to the departmental activities of the AOFM.

(a) Revenue from Government — output appropriations

Amounts appropriated for departmental outputs for the year (adjusted for any formal additions and reductions) are recognised as revenue. Appropriation receivables are recognised (at their nominal amounts) for output appropriations that have not been drawn by the AOFM and have not lapsed.

Under the Government's 'net cash appropriation framework' the AOFM receives an output appropriation equivalent to budgeted expenses less depreciation, amortisation and make good expenses.

(b) Resources received free of charge

Resources received free of charge are recognised as revenue when, and only when, a fair value can be reliably determined and the services would have been purchased had they not been donated. Use of those resources is recognised as an expense.

(c) Other revenue

Revenue from the rendering of a service is recognised by reference to the stage of completion of contracts or other agreements to provide the service. Other revenue includes amounts received and receivable for salary packaging arrangements for staff and transfers of annual leave and long service leave entitlements from other government agencies.

1.6 Transactions with the Government as owner (Departmental)

(a) Equity injections

Amounts which are designated as 'equity injections' for a year (less any formal reductions) are recognised directly in Contributed Equity in the Statement of Financial Position in the financial year that the appropriation takes effect.

Appropriation receivables are recognised (at their nominal amounts) for equity injections that have not been drawn by the AOFM and have not lapsed.

For 2013-14 the AOFM received a capital injection of $0.408 million (2012-13: $0.406 million) under the Government's 'net cash appropriation framework'. Under this framework, the AOFM is provided with capital funding in the form of an equity injection for the replacement of departmental property, plant and equipment and computer software.

(b) Distributions to owners

Distributions to owners are deducted from Contributed Equity unless the distributions are in the nature of a dividend. Dividends are deducted from Retained Surplus in the Statement of Financial Position.

In 2013-14, $3,447,050 in unspent departmental appropriations was returned to the Budget due to the repeal of annual appropriations from 1 July 1999 through to 30 June 2010 by the *Statute Stocktake (Appropriations) Act 2013* (2012-13: $nil).

1.7 Employee benefits (Departmental)

Liabilities for services rendered by employees are recognised at the end of the financial year to the extent that they have not been settled.

(a) Salaries

Outstanding salaries, and superannuation in relation to those salaries, are recognised at their nominal (undiscounted) amounts.

(b) 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 the AOFM is estimated to be less than the annual entitlement for sick leave.

The AOFM obtains advice from the Australian Government Actuary on the valuation of its leave liabilities. Leave liabilities are calculated on the basis of employees' remuneration at the end of the financial year adjusted for expected increases in remuneration effective from 1 July.

Long service leave employee benefits and annual leave benefits are measured at the present value of the estimated future cash flows to be made in respect of all employees at the end of the financial year. In determining the present value of the long service leave liability, the AOFM commissions an annual actuarial assessment by the Australian Government Actuary of the anticipated attrition rates and pay increases through promotion and inflation. The Australian Government Actuary has recommended the application of the shorthand method, as prescribed by the FMOs, for determining the present value of the long service leave liability.

(c) Superannuation

Staff and contractors of the AOFM contribute to the Commonwealth Superannuation Scheme (CSS: a defined benefit scheme), Public Sector Superannuation Scheme (PSS: a defined benefit scheme), Public Sector Superannuation Accumulation Plan (PSSap: an accumulation scheme) and other nominated schemes.

The AOFM makes employer contributions to the CSS and PSS superannuation schemes at rates determined by an actuary to be sufficient to meet the current cost to the Government of the superannuation entitlements of its employees. The liability for defined superannuation benefits payable to an employee upon termination of employment with the Australian Government is recognised in the financial statements of the Department of Finance and is settled by the Australian Government in due course. This defined benefit liability is reported by the Department of Finance as an administered item. The AOFM accounts for its contributions to the CSS and PSS as if they were defined contribution plans.

An on-cost liability, based on actuarial assessment, has been recognised for employer superannuation contributions payable on accrued annual leave and long service leave as at the end of the financial year. Employer superannuation contributions are payable on leave benefits that are taken during service, but are not payable on leave benefits paid out on termination.

1.8 Leases (Departmental)

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

The AOFM holds operating leases only. Operating lease payments are charged as an expense as they are incurred over the lease term.

1.9 Cash (Departmental)

Cash means notes and coins held and any deposits held at call with a bank. Deposits held with a bank that are not at call are classified as investments. Cash is recognised at its nominal amount.

1.10 Financial instruments (Departmental)

The AOFM recognises a financial asset or financial liability in its Statement of Financial Position when and only when it becomes a party to the contractual provisions of the instrument. A financial asset is de-recognised when the right to receive cash flows from the financial asset has expired or substantially all the risks and rewards of ownership have been transferred to another party. A financial liability is de-recognised when the obligation in the contract is discharged, cancelled or has expired.

The AOFM classifies its departmental financial assets as loans and receivables. Loans and receivables primarily comprise amounts due from other parties for the reimbursement of staff costs associated with staff secondments. Loans and receivables are initially recognised at fair value and are subsequently measured at amortised cost. Amounts due from the Official Public Account (OPA) for undrawn departmental appropriations are not financial instruments as they are not contractually based.

Financial liabilities represent trade creditors and accruals and are recognised at the amounts at which they are expected to be settled.

Departmental financial assets and financial liabilities are predominantly denominated in Australian dollars, are non-interest bearing and their fair values approximate their carrying values. Accordingly, the AOFM is not exposed to interest rate risk or significant exchange rate risk on its departmental financial instruments. The AOFM's maximum exposure to credit risk on departmental financial assets approximates their carrying values. The AOFM's exposure to credit risk on its departmental financial instruments is immaterial.

1.11 Property, plant and equipment (Departmental)

(a) Asset recognition threshold on acquisition

Purchases of property, plant and equipment are recognised initially at cost in the Statement of Financial Position, except for purchases costing less than $1,000 ($500 in 2012-13), which are expensed at the time of acquisition. The asset recognition threshold is applied to each functional asset, that is, items or components that form an integral part of an asset are grouped as a single asset.

(b) Revaluations

Basis

Following initial recognition at cost, valuations are conducted with sufficient frequency to ensure that the carrying amounts of assets do not materially differ from the assets' fair values as at the reporting date, in accordance with AASB 116 *Property, Plant and Equipment*.

Fair value has been determined as depreciated replacement cost for leasehold improvements and market selling price in an active market for computers, plant and equipment.

Revaluation adjustments are made on a class basis. Revaluation increments for a class are credited directly to a revaluation reserve in Equity, except to the extent that they reverse a previous revaluation decrement of the same asset class, in which case they are credited as revenue directly through the Statement of Comprehensive Income. Revaluation decrements for a class of assets are recognised as an expense directly through the Statement of Comprehensive Income, except to the extent that they reverse a previous revaluation increment for that class, in which case they are debited directly to a revaluation reserve in Equity. Upon disposal, any revaluation reserve relating to the asset sold is transferred to Retained Surplus.

For all assets, excluding leasehold improvements, any accumulated depreciation or amortisation as at the revaluation date is eliminated against the gross carrying amount of the asset. For leasehold improvements, accumulated amortisation on revaluation is restated proportionately in accordance with the gross carrying amount of the asset.

Property, plant and equipment assets are classified in a three level valuation hierarchy which is disclosed at Note 10. Transfers between levels are deemed to occur at the end of the reporting period following a revaluation of the asset class.

Frequency

Property, plant and equipment assets are formally revalued every three years. All property, plant and equipment assets were revalued as at 31 March 2012.

Assets acquired after the commencement of a revaluation are not captured by the revaluation.

Conduct

All valuations are conducted by an independent qualified valuer.

(a) Impairment

All property, plant and equipment assets were assessed for impairment at the end of the financial year. No allowance for impairment was required.

(b) Depreciation

The depreciable value of property, plant and equipment assets is written off over the estimated useful lives of the assets to the AOFM using the straight-line method of depreciation. Leasehold improvements are depreciated on a straight-line basis over the lesser of the estimated useful life of the improvements and the unexpired period of the lease. The depreciable value of property, plant and equipment assets is based on a zero residual value.

Depreciation rates (useful lives) are reviewed at least annually and, if required, the remaining useful life of an asset is adjusted. Adjustments are recognised in the current, or current and future, reporting periods as appropriate. During 2013-14 the AOFM extended the useful lives of a number of assets. The financial impact of the change was a reduction in the depreciation charge for 2013-14 of $11,500.

Depreciation expenses have been determined by applying rates to new depreciable assets based on the following useful lives:

Sub-class of depreciable asset	**2014**	2013
Leasehold improvements	lease term	lease term
Computers	3-5 years	3-5 years
Office equipment	5 years	5 years
Furniture	10 years	10 years

The aggregate amount of depreciation allocated to each class of asset during the reporting period is disclosed at Note 4C.

1.12 Computer software (Departmental)

Purchases of computer software are recognised at cost in the Statement of Financial Position except for purchases costing less than $10,000, which are expensed at the time of acquisition.

An item of software represents:

- a software licence granted for greater than 12 months; or
- a developed software application.

Developed software is recognised by capitalising all directly attributable internal and external costs that enhance the software's functionality and therefore service potential.

Software assets are amortised on a straight-line basis over their anticipated useful lives, being three to ten years (2012-13: three to five years). Software assets are carried at cost and are not subject to revaluation.

An impairment assessment was made as at the end of the financial year and an impairment allowance was not required.

1.13 Taxation (Departmental)

The AOFM is exempt from all forms of taxation except for Fringe Benefits Tax (FBT) and the Goods and Services Tax (GST).

Revenue, expenses, assets and liabilities 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 (where GST is applicable).

Receipts and payments in the Statement of Cash Flows are recorded at their GST inclusive amounts.

All supplies provided by the AOFM are input taxed under the GST legislation. In accordance with applicable GST regulations the AOFM is entitled to a reduced input tax credit (equal to 75 per cent of the GST paid) on some purchases, such as security transaction services, which are applied in making input taxed supplies. From 1 July 2012 non-commercial supplies provided by government agencies are GST-free.

1.14 Reporting of administered activities

Except where otherwise stated, administered items are prepared on the same basis of accounting and using the same policies as for departmental items, including the application of Australian Accounting Standards.

1.15 Exemption from FMOs

Section 17.2 of the FMOs provides an exemption to the AOFM from presenting its Administered Schedule of Comprehensive Income, and associated notes, in accordance with the Annexure to the FMOs. Instead, the AOFM is required to comply with AASB 101 *Presentation of Financial Statements* for presenting its Administered Schedule of Comprehensive Income.

Paragraph 85 of AASB 101 encourages reporting entities to adopt a presentation for reporting revenue and expenses that is most relevant to users in understanding the entity's financial performance.

With the adoption of fair value through profit or loss measurement for certain classes of financial assets and financial liabilities the AOFM presents its administered revenue and expenses into two categories:

- surplus (deficit) before re-measurements; and
- re-measurements.

The category 'surplus (deficit) before re-measurements' records a financial result that is consistent with an accruals (or amortised cost) basis of accounting under the historic cost accounting convention and is most relevant to the AOFM's role in managing its debt portfolio whereby debt and other financial instruments are predominately issued and held to maturity (and with portfolio restructuring a rarity and performed primarily for portfolio management, credit or liquidity purposes, rather than for profit making purposes). Where a financial asset is sold or a financial liability is bought back prior to maturity, the realised gain or loss, calculated on an amortised cost basis, is recognised within this category. Realised and unrealised foreign currency gains and losses are also included in this category.

The category 're-measurements' provides information on the unrealised changes in the market valuation of the portfolio of administered financial assets and financial liabilities during the financial year. This is relevant for assessing changes in financial risk exposures and changes to the value of transactions managed from year to year. The revaluation effect will net to zero over the life of a financial instrument.

1.16 Recognition and de-recognition of financial instruments

The AOFM recognises a financial asset or financial liability in its Administered Schedule of Assets and Liabilities when and only when it becomes a party to the contractual provisions of the financial instrument. A financial asset is de-recognised when the right to receive cash flows from the financial asset has expired or substantially all the risks and rewards of ownership have been transferred to another party. A financial liability is de-recognised when the obligation in the contract is discharged, cancelled or has expired.

The AOFM accounts for purchases and sales of financial instruments on a trade date basis, that is, the date on which transactions are executed. Depending on the transaction type this may be several days prior to settlement.

1.17 Classification and measurement of financial instruments

The AOFM classifies its administered financial assets into the following categories: financial assets at fair value through profit or loss; and loans and receivables. The AOFM classifies its financial liabilities in the following categories: financial liabilities at fair value through profit or loss; and other financial liabilities. See Note 25A for further details of the AOFM's financial instrument categories.

The AOFM has determined the classifications on the basis of how it manages and assesses the performance of its financial assets and financial liabilities. Where the AOFM's management monitors cost and risk in mark-to-market terms (but not necessarily only in those terms), the AOFM has classified the relevant financial assets and liabilities at fair value through profit or loss.

(a) Non-derivative financial assets at fair value through profit or loss

This category comprises short-term Australian dollar denominated deposits and Australian dollar denominated residential mortgage-backed securities. Under section 39(2) of the *Financial Management and Accountability Act 1997*, the AOFM invests public money to manage the balance of the Official Public Account (OPA) and to support the residential mortgage market.

These assets are measured at fair value on initial recognition and at fair value on subsequent measurement. Changes in carrying value are attributed between changes in amortised cost of the asset and other changes.

Changes in carrying value attributable to amortised cost are recognised in Interest Revenue in the Administered Schedule of Comprehensive Income. Where a security is acquired at a premium or discount to its par value, the premium or discount is recognised at that time and included in the carrying value of the asset. The premium or discount is amortised over the life of the security using the effective interest rate method and recognised in Interest Revenue. Other changes in carrying value (including unrealised changes in valuation due to a change in interest rates) are recognised in Re-measurements in the Administered Schedule of Comprehensive Income.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The AOFM classifies a financial asset as a loan and receivable (as opposed to a financial asset at fair value through profit or loss) in circumstances where the cost and risk of the asset is not managed in mark-to-market terms.

Currently, this category comprises debt on allocation to, and advances made to, the State and Northern Territory Governments.

Until July 1990, the Australian Government borrowed on behalf of the State and Northern Territory Governments and allocated a portion of the proceeds of its Treasury Bond raisings to those Governments to fund the redemption of previous allocations of raisings. Until 1986, the Australian Government also borrowed on behalf of the State and Northern Territory Governments to raise new borrowings. In addition to Treasury Bond allocations, there are outstanding balances on stock issued by the States prior to 1 January 1924 and taken over by the Australian Government in 1927 (under the original Financial Agreement Act). The States and the Northern Territory are responsible for meeting all obligations as to interest and principal on the debt on allocation to them in accordance with the provisions of the *Financial Agreement Act 1994* (the current agreement). As at 30 June 2014 approximately $8 million of perpetual debt with no fixed maturity date issued by New South Wales and Victoria remained outstanding under the arrangements governed by the *Financial Agreement Act 1994* (30 June 2013: $8 million). All other debt has been redeemed. Redemption of the perpetual debt is at the discretion of the relevant State.

In addition to debt governed by the *Financial Agreement Act 1994*, from 1945 to 1989 the Australian Government made concessional advances to the State and Northern Territory Governments under Commonwealth-State financing arrangements, which were not evidenced by the issue of securities (namely, housing advances and specific purpose capital advances). On 26 June 2013, the Minister for Finance approved pursuant to section 34(1)(a) of the *Financial Management and Accountability Act 1997* the waiver of $320 million (in face value terms) of housing advances owed by the South Australian Government with effect on 30 June 2013. The accounting loss arising from this waiver is reported at Note 19. The principal value of these advances outstanding from the State and Northern Territory Governments (for which the AOFM is responsible for administering) was $2,366 million as at 30 June 2014 (30 June 2013: $2,455 million).

Loans and receivables are measured at fair value on initial recognition and at amortised cost on subsequent measurement using the effective interest rate method. Changes in carrying value, including amortisation of premiums or discounts, are recognised in Interest Revenue in the Administered Schedule of Comprehensive Income.

For financial assets measured at amortised cost, interest revenue earned but not yet received is recognised in Accrued Revenue in the Administered Schedule of Assets and Liabilities.

(c) Non-derivative financial liabilities at fair value through profit or loss

Currently this category comprises all Commonwealth Government Securities (CGS) debt with the exception of debt on allocation to State and Northern Territory Governments and overdues. CGS primarily comprises Treasury Bonds, Treasury Indexed Bonds and Treasury Notes.

These liabilities are measured at fair value on initial recognition and at fair value on subsequent measurement. Changes in carrying value are attributed between changes in amortised cost of the liability and other changes. Changes in carrying value attributable to amortised cost are recognised in Interest Expense in the Administered Schedule of Comprehensive Income. Where a security is issued at a premium or discount to its par value, the premium or discount is recognised at that time and included in the carrying value of the liability. The premium or discount is amortised over the life of the security using the effective interest rate method and recognised in Interest Expense. Other changes in carrying value (including unrealised changes in valuation due to a change in interest rates) are recognised in Re-measurements in the Administered Schedule of Comprehensive Income.

For Treasury Indexed Bonds, the principal value appreciates over time with the consumer price index (the Weighted Average of Eight Capital Cities All-Groups Index) in line with a six-month lagged consumer price index. As future inflation rates are uncertain, an estimate of the Australian Government's future redemption cost on maturity is not disclosed in the financial statements. Capital accretion is recognised in Interest Expense over time.

There are no options available to either the Australian Government or the holder of the securities to exchange or convert CGS. There are also no options to either party for early redemption.

(d) Other non-derivative financial liabilities

This category comprises perpetual debt on allocation to State and Northern Territory Governments and overdues (debt that has reached maturity but has not been claimed by the investor).

These liabilities are measured at fair value on initial recognition and at amortised cost on subsequent measurement using the effective interest rate method. Changes in carrying value are recognised in Interest Expense in the Administered Schedule of Comprehensive Income.

For financial liabilities measured at amortised cost, interest incurred but not yet paid is recognised as Other Interest Bearing Liabilities.

1.18 Fair value estimation of financial instruments

Where a financial instrument is traded in an active market, fair value is based on quoted market rates for the financial instrument as at the end of the financial year. Where market rates are unavailable because a financial asset or financial liability is not traded in an active market, valuation techniques are used, including quotes for similar instruments and discounted cash flow analysis. Fair value measurement requires maximising the use of market observable inputs and minimising the use of unobservable inputs. Where markets are distorted or illiquid, with pricing not necessarily reflective of underlying credit and cash flow fundamentals, assumptions may be necessary to derive the fair value of a financial instrument.

Fair value is synonymous with market value and represents the estimated exchange equivalent price using relevant inputs from reference markets and valuation techniques. Fair value is determined on the presumption that the reporting entity is a going concern and is operating in an active market under normal conditions, without any intention or need to liquidate, curtail materially the size of its activities or undertake transactions on adverse terms.

Financial instruments are classified in a three level valuation hierarchy which is disclosed at Note 25G. Transfers between levels are deemed to occur at the end of the reporting period.

(a) Non-derivative financial instruments at fair value

The fair value of Treasury Bonds is based on discounted cash flows using a zero coupon curve valuation methodology created from observable market rates. The zero coupon curve is based on market yields of the most liquid Treasury Bond lines as at the end of the financial year.

The fair values of Treasury Indexed Bonds are based on observable market quotes for each issue.

The fair value of term deposit investments with the RBA is based on a zero coupon curve using the overnight cash rate and overnight indexed swap rates. These yields reflect a default free credit risk. The valuation approach for Treasury Notes is largely equivalent.

For residential mortgage-backed securities each issue is modelled to determine its weighted average life, which is tested and compared against other sources where available. Fair value is determined using the weighted average life, market quotes (where available) and assumptions based on credit quality considerations.

As the secondary market for the Australian Government's foreign currency denominated debt is largely illiquid, the valuation approach for foreign currency denominated debt is based on deposit and swap rates in each relevant foreign currency.

1.19 Other significant administered accounting policies

(a) Revenue

All administered revenue is revenue relating to the activities performed by the AOFM on behalf of the Australian Government.

Interest revenue is earned on loans to State and Northern Territory Governments, residential mortgage-backed securities and term deposits. Interest is credited to revenue as it accrues and is calculated on an amortised cost basis using the effective interest rate method.

Net interest earnings on securities lending transactions are reported as revenue when received.

(b) Grants

Under the *Financial Agreement Act 1994*, the Australian Government assists the State and Northern Territory Governments to redeem maturing debt on allocation to them. Payments made under these arrangements are recognised in grants expenses as and when they fall due and payable.

(c) Borrowing costs

In accordance with section 21.1 of the FMOs borrowing costs are expensed as incurred. Under AASB 123 *Borrowing Costs*, borrowing costs directly attributable to a qualifying asset may be capitalised or expensed by a not-for-profit public sector entity. A qualifying asset is an asset that takes a substantial period of time to get ready for its intended use or sale. The AOFM's borrowing programme does not specifically raise funds for qualifying assets.

(d) Cash

The AOFM maintains a number of administered operational bank accounts with the Reserve Bank of Australia (RBA) and the National Australia Bank. Interest is not paid on these accounts. Deposits are recognised at their nominal amounts.

(e) Securities lending facility

The AOFM has a securities lending facility available for Treasury Bonds and Treasury Indexed Bonds. The facility is operated by the RBA and is governed by the terms and conditions of an agency agreement between the RBA and the AOFM. The purpose of the facility is to enhance the efficiency of the bond market by allowing bond market participants to borrow Treasury Bonds and Treasury Indexed Bonds (generally for a period of no more than several days) when they are not readily available from other sources in the market.

The securities lending facility operates by entering into two simultaneous repurchase agreements with the party wishing to borrow securities — a repurchase agreement (the sale of securities to the party and agreement to buy them back at a future time at an agreed price) and a reverse-repurchase agreement (the purchase of securities from the party and agreement to sell them back at a future time at an agreed price). The net effect of these two transactions is that the Australian Government holds securities as collateral, and not cash, for securities loaned to bond market participants.

The exchange of securities is market value matched subject to a 2 per cent initial margin imposed by the AOFM for credit risk mitigation purposes. There is provision for making margin calls after initial exchange where the securities pledged as collateral by the other party fall in value relative to the Treasury Bonds or Treasury Indexed Bonds loaned under the facility. The repurchase and reverse-repurchase agreements are at-call, that is, they do not have set terms.

Interest is payable under the facility where lending is overnight. Interest is not payable on intra-day lending. The interest rate payable by the other party is the RBA target cash rate. The interest rate payable by the AOFM is the target cash rate less a margin. Net interest earnings of the Australian Government are reported as revenue when received. The temporary sale of CGS under the facility is recorded off-balance sheet. See Note 27 for details of transactions undertaken during the financial year under the facility.

(f) Foreign currency

Transactions denominated in a foreign currency are converted at the exchange rate at the date of the transaction. Foreign currency receivables and payables are translated at the exchange rates current as at the end of the financial year.

Net foreign exchange gains and losses (both realised and unrealised) arising from foreign currency transactions are reported in the Administered Schedule of Comprehensive Income.

Note 2: Objectives and activities of the AOFM

The AOFM manages a portfolio of debt and financial assets on behalf of the Australian Government. It issues Treasury Bonds and Treasury Indexed Bonds to finance projected budget deficits. It also manages the Government's cash in the Official Public Account (OPA) which is surplus to immediate requirements by making investments in term deposits. It uses these instruments, together with the issue of Treasury Notes, to manage the within-year financing task. It undertakes the administration, financial and operational risk management, and financial reporting of its portfolio of debt and assets. In managing its portfolio and undertaking these tasks it seeks to minimise accrual debt servicing costs over the medium term at an acceptable level of risk.

Financing the budget

For many years debt issuance by the AOFM was undertaken solely with the objective of maintaining the Treasury Bond and Treasury Bond futures markets, as successive budget surpluses removed the need to borrow to fund the Budget. The forecast Budget outlook changed in the *Updated Economic and Fiscal Outlook* published on 3 February 2009 and the objective of issuance changed to funding the Budget. Since this time, the AOFM has significantly increased debt issuance and intensified its promotional activities with investors (including overseas investors) and intermediaries.

Portfolio management

The cost and risk of the debt portfolio is managed through debt issuance and investment activities.

Cash management

The AOFM manages the overall level of cash in the OPA to ensure that the Government is able to meet its financial obligations as and when they fall due. To this end, it makes short-term borrowings by issuing Treasury Notes. It also invests in term deposits with the Reserve Bank of Australia (RBA).

The OPA is recorded in the Department of Finance's financial statements and is not reported by the AOFM. The AOFM holds continuing balances of short-term assets to allow it to respond flexibly and quickly to swings in cash requirements.

Investments in residential mortgage-backed securities

In September 2008, the Government announced that the AOFM would invest $4 billion in residential mortgage-backed securities (RMBS) to support competition in the Australian residential mortgage market. The initiative was extended in October 2008 and again in November 2009 to a total programme of up to $20 billion. In April 2013, the Government announced that due to improvements in market conditions, the

AOFM would not make any new investments in RMBS. The AOFM invested $15.5 billion in RMBS over the life of the programme.

The AOFM continues to hold investments in RMBS purchased prior to April 2013 and to monitor conditions in the RMBS market. It sells its holdings from time-to-time to assist with price discovery in the market.

Trading of depository interests in Commonwealth Government Securities

In November 2012, the *Commonwealth Inscribed Stock Act 1911* and *Corporations Act 2001* were amended as part of the Government's Competitive and Sustainable Banking Package to enable trading of depository interests in Treasury Bonds and Treasury Indexed Bonds on financial markets in Australia. Ownership of a depository interest provides the retail investor with beneficial ownership of the underlying bond including the right to receive principal and interest.

The AOFM facilitated the establishment of infrastructure to allow these financial products to trade on the Australian Stock Exchange (ASX), where they are called Exchange-traded Treasury Bonds and Exchange-traded Treasury Indexed Bonds. Trading commenced on 21 May 2013.

The trading, settlement and administration of these financial products are governed by the *Corporations Act 2001*, market integrity rules made by the Australian Securities and Investments Commission, ASX market rules and contractual arrangements between the AOFM and the ASX (the financial market operator) and the AOFM and Computershare Investor Services Pty Limited (the registry provider).

Legislation

The AOFM's borrowing and portfolio management activities comply with applicable legislative requirements. The key legislative mechanisms that governed these activities during the reporting period were as follows:

- the *Commonwealth Inscribed Stock Act 1911*, which represents the Australian Government's primary vehicle for the creation and issuance of domestic stock, including Treasury Bonds, Treasury Indexed Bonds and Treasury Notes. It also provides a standing authority to the Treasurer to borrow in Australian currency;
  - on 10 December 2013, the *Commonwealth Inscribed Stock Amendment Act 2013* received royal assent. The Act includes an amendment to the *Commonwealth Inscribed Stock Act 1911* to remove the legislative limit on borrowing. The requirement for the Treasurer to issue a direction as to the maximum face value of stock that may be on issue under the Act remains in place. On 11 December 2013 the Treasurer issued a new direction under section 51JA of the Act permitting the AOFM to borrow up to $500 billion.

- the *Loans Securities Act 1919*, which includes provisions relating to overseas borrowings, and provides authority to enter into swaps, securities lending, repurchase agreements and other financial arrangements;
- the *Financial Agreement Act 1994*, which formalises debt consolidation and redemption arrangements applying since 1 July 1990 between the Australian Government and the States and Territories; and
- section 39 of the *Financial Management and Accountability Act 1997*, which gives the Treasurer the power to invest public money in authorised investments.

Note 3: Financial risk management

The AOFM is exposed to financial risks arising from its portfolio of financial assets and liabilities comprising interest rate risk, inflation risk, exchange rate risk, liquidity and refinancing risk, credit risk and prepayment risk. These risks are controlled within a financial risk management framework that includes directions from the Treasurer and policies and limits approved by the Secretary to the Treasury and overseen by the CEO and senior management of the AOFM. The Secretary to the Treasury is advised by Treasury, the AOFM CEO and the AOFM Advisory Board.

Timing mismatches between the Australian Government's receipts and expenditures cause large fluctuations in the volume of short-term assets and liabilities held by the AOFM, and thus in the overall size of its net portfolio, relative to the gross volume of debt outstanding. To provide stability in the management of the longer term component of its debt, long-term financing and short-term financing are managed through separate portfolios, the debt portfolio and the cash management portfolio. In addition, the AOFM's investments in residential mortgage-backed securities and advances to State and Northern Territory Governments (which were made under previous Commonwealth-State financing arrangements and were not evidenced by the issue of securities) are held in separate portfolios.

(a) Interest rate risk

Interest rate risk represents the risk to debt servicing cost outcomes and investment return outcomes and to the value of debt and financial assets caused by changes in interest rates. The AOFM largely holds its debt and assets until maturity. Accordingly, the primary measure used to assess cost and return is the accruals basis of accounting under the historic cost accounting convention. Market value measures (which include unrealised changes in the valuation of financial assets and financial liabilities due to changes in interest rates) are considered to be secondary.

Debt portfolio

The AOFM manages the interest rate structure of the debt portfolio through the choice of instruments and bond series in issuing debt. The cost and interest rate risk of the debt portfolio is regularly measured and reported to senior management, the Secretary to the Treasury and the AOFM Advisory Board.

Cash management portfolio

The cash management portfolio holds a fluctuating portfolio of short-term investments and liabilities. Given the short tenor of the financial instruments in this portfolio, the level of interest rate risk is considered to be low.

Residential mortgage-backed securities

Interest earned on residential mortgage-backed securities comprises a floating interest rate (based on the one-month BBSW rate) plus a fixed margin set at the time each investment is acquired. The AOFM monitors movements in these interest rates as part of its management of the overall portfolio.

See Note 25B for details of the AOFM's interest rate risk profile.

(b) Inflation risk

The AOFM currently has seven series of Treasury Indexed Bonds on issue. These instruments have their principal value indexed against the (all Groups) Australian Consumer Price Index (CPI). The interest is a fixed real rate of interest payable on the accreted principal value. Accordingly these debt instruments expose the AOFM to inflation risk on interest payments and on the value of principal payable on maturity. There is a six month lag between the calculation period for the CPI and its impact on the value of interest and principal.

(c) Exchange rate risk

Exchange rate risk arises from debt denominated in a foreign currency. Only a small residual amount of such debt remains in the AOFM's portfolio and the AOFM seeks to repurchase this debt when available on acceptable terms. The volume of foreign currency debt remaining is monitored by senior management.

See Note 25C for details of the AOFM's exposure to foreign exchange risk.

(d) Liquidity and refinancing risk

The AOFM manages liquidity risk by maintaining sufficient cash and short-term investments to ensure that the Government can meet its financial obligations, both planned and unplanned, as and when they fall due. The AOFM manages the daily volume of cash in the OPA by monitoring the projected daily transactions of major spending and revenue agencies, undertaking investment of funds that are surplus to immediate cash requirements and by issuing Treasury Notes. The 91-day rolling average balance of the OPA is kept within a limit set by the Treasurer and the Minister for Finance. The AOFM also has access to an overdraft facility with the RBA. The overdraft facility is not to be used in normal day-to-day operations but only to cover temporary, unexpected shortfalls of cash and it has a limit of $1 billion. Should circumstances arise for the overdraft to exceed this limit, Ministerial approval is required.

The AOFM seeks to control refinancing risk by issuing along the entire yield curve. This creates a range of short-dated and mid-to-long-dated exposures that balance cost and refinancing patterns. In formulating its annual debt issuance strategy the AOFM considers the volume of debt in any one line and the maturity structure (including the number of bond lines and the maturity gaps between lines) of its debt. The AOFM CEO approves the debt issuance programme.

Senior management monitors the daily balance in the OPA, holdings of short-term assets and short-term and long-term debt issuance activity.

See Note 25D for details of the maturity profile of AOFM's cash flow obligations arising from its financial liabilities as at year end.

(e) Credit risk

The AOFM's investment activity is made in accordance with legislative limits, delegations and directions from the Treasurer and policies and limits established by the Secretary to the Treasury. Section 39 of the *Financial Management and Accountability Act 1997* and associated regulations specify authorised investments. Directions from the Treasurer further limit the class of acceptable assets. The Secretary to the Treasury sets class and individual issuer exposure limits, including credit rating requirements.

The AOFM CEO approves the individual issuer names eligible for investment and from time to time may impose further restrictions on class and individual issuer exposure limits. Eligible investments and their limitations are as follows:

Eligible investment classes	**Limits framework for 2013-14**
Securities issued or guaranteed by the Commonwealth, a State or Territory.	Class limit of zero.
AAA rated or equivalent debt securities issued or guaranteed by the government of a foreign country in Australian dollars.	Class limit of zero.
AAA rated or equivalent debt securities issued by a financial institution or supranational in Australian dollars.	Class limit of zero.
Bank accepted bills of exchange and negotiable certificates of deposit rated at least A1 or equivalent issued in Australian dollars by an authorised deposit taking institution, where the remaining term to maturity is no more than 12 months.	Class limit of zero.
Commercial paper issued in Australian dollars rated at least A1+ or equivalent where the remaining term to maturity is no more than 12 months.	Class limit of zero.
Eligible investment classes	**Limits framework**
Deposits with the Reserve Bank of Australia.	No limits apply.
AAA rated or equivalent residential mortgage-backed securities issued in Australia.	As of 9 April 2013, this class is no longer eligible for new investments.

See Note 25E for details of the AOFM's exposure to credit risk.

Residential mortgage-backed securities (RMBS)

The AOFM no longer makes new investments in RMBS, however, it continues to hold securities purchased prior to 9 April 2013. The credit quality of RMBS derives from the underlying quality of the mortgage assets and structural enhancements such as lenders' mortgage insurance, liquidity facilities, and the issue of different classes of securities. At the time of acquisition, each RMBS security must meet a range of eligibility criteria set by the AOFM, including AAA (or equivalent) credit rating by at least two ratings agencies and denomination in Australian dollars. Mortgages backing the securities must be secured by an insurable prime mortgage over Australian residential property and meet various limits, including mortgage loan size and loan-to-value ratios. Each mortgage pool must be subject to independent review to provide assurance that the eligibility criteria have been met. The AOFM monitors the performance of each RMBS issue through a monthly report by the issuer on mortgage portfolio characteristics as well as conducting due diligence on RMBS issues from time to time. In the event that an investment made ceases to meet the specific eligibility requirements, the AOFM may continue to hold the security until maturity or it can be sold at an acceptable price.

As at 30 June 2014 all RMBS securities held by the AOFM were rated at AAA or equivalent.

Other assets and credit exposures

The AOFM has a credit risk exposure on its advances to the State and Northern Territory Governments. This risk is regarded as minimal.

To protect the Australian Government's financial position with respect to securities lending arrangements, the market value of the collateral securities taken from counterparties is at least 2 per cent greater than the market value of the Treasury Bonds or Treasury Indexed Bonds lent. The AOFM has the right to seek additional collateral if there is a decline in the market value of the collateral securities relative to the lent securities.

(a) Prepayment risk

All RMBS currently held by the AOFM are fully amortising, pass through instruments. This means that the principal collections from the underlying portfolio of mortgages are repaid to the holders of the securities thereby reducing the principal outstanding on them.

Principal and interest on the underlying loans are received by the servicer and paid to an issuer bank account. On a scheduled basis, typically monthly, in accordance with a set priority of payments (a 'cash flow waterfall'), the cash collected is used to pay any taxes, fees and expenses of the issuer, and interest and principal due on each class of outstanding RMBS. Due to the pass through nature of the RMBS, the repayment of principal is dependent upon the timing of principal repayments on the underlying mortgages and the operation of the cash flow waterfall. Accordingly, the rate at which principal is repaid varies over time and the actual date that the securities will be repaid in full cannot be precisely determined (this is referred to as prepayment risk).

The AOFM monitors the performance of each RMBS issue through a monthly report by the issuer. The report provides details of cash received from payments on the underlying mortgages, payments made, the rate of the loan principal repayments ahead of scheduled principal payments and the estimated weighted average remaining life of the securities.

Note 4: Expenses

	2014 $'000	2013 $'000
Note 4A: Employee benefits		
Wages and salaries	**5,570**	5,215
Superannuation	**1,049**	939
Leave and other entitlements	**90**	130
Other employee expenses	**231**	197
Total employee benefits	**6,940**	6,481
Note 4B: Supplier expenses		
ANAO - notional audit fee	**320**	303
Corporate support services	**553**	53
Market data services	**537**	634
Operating lease rentals(a)	**288**	286
Depository and transaction services(b)	**139**	125
Travel	**366**	302
Workers compensation premium	**12**	7
Other	**1,220**	1,203
Total supplier expenses	**3,435**	2,913
Supplier expenses are made up of:		
Provision of goods - related parties	**29**	2
Provision of goods - external parties	**25**	67
Provision of services - related parties	**1,364**	885
Provision of services - external parties	**2,017**	1,959
Total supplier expenses	**3,435**	2,913
Note 4C: Depreciation and amortisation		
Depreciation of property, plant and equipment:		
Computers, plant and equipment	**107**	116
Leasehold improvements	**109**	104
Amortisation of intangibles:		
Computer software	**161**	160
Total depreciation and amortisation	**377**	380
Note 4D: Write-down and impairment of assets		
Computers, plant and equipment - disposed	**2**	2
Computer software - disposed	**4**	-
Total write-down and impairment of assets	**6**	2

(a) Amounts relate to minimum lease payments only. Novated lease payments from salary packaging of motor vehicles are disclosed in 'other employee expenses'.

(b) From 29 June 2011, costs and expenses incurred in relation to issuing and managing debt are made against an administered appropriation.

Note 5: Income

	2014 $'000	2013 $'000
Note 5A: Sale of goods and rendering of services		
With related entities:		
Staff secondments to other agencies	**473**	516
Total sale of goods and rendering of services	**473**	516
Note 5B: Other revenue		
Resources received free of charge - ANAO audit services	**320**	303
Other	**91**	80
Total other revenue	**411**	383
Note 5C: Revenue from government		
Appropriations - departmental output	**11,479**	11,409
Total revenue from government	**11,479**	11,409

Note 6: Financial assets

	2014 $'000	2013 $'000
Note 6A: Receivables		
With related parties:		
Goods and services	**73**	141
Appropriations receivable(a):		
Output	**23,183**	25,311
Equity injection	**-**	162
Departmental capital budget	**2,290**	3,049
Tax and other	**5**	1
Total receivables	**25,551**	28,664
Receivables are expected to be recovered in:		
No more than 12 months(b)	**2,920**	7,139
More than 12 months	**22,631**	21,525
Total receivables	**25,551**	28,664
Receivables are aged as follows:		
Not overdue	**25,551**	28,664
Overdue	**-**	-
Total receivables	**25,551**	28,664

(a) Appropriations receivable are appropriations controlled by the AOFM but held in the OPA under the Government's 'just-in-time' drawdown arrangements.
(b) Includes appropriations repealed. See Note 28B for further details.

Note 7: Non-financial assets

	2014 $'000	2013 $'000
Note 7A: Property, plant and equipment		
Computers, plant and equipment:		
Gross value - at fair value	**366**	183
Accumulated depreciation	**(66)**	(15)
Net value - at fair value	**300**	168
Gross value - at 2012 valuation (fair value)	**266**	279
Accumulated depreciation	**(177)**	(132)
Net value - at 2012 valuation	**89**	147
Total computers, plant and equipment	**389**	315
Leasehold improvements:		
Gross value - at fair value	**67**	66
Accumulated depreciation	**(35)**	(16)
Net value - at fair value	**32**	50
Gross value - at 2012 valuation (fair value)	**1,071**	1,071
Accumulated depreciation	**(938)**	(848)
Net value - at 2012 valuation	**133**	223
Total leasehold improvements	**165**	273
Total property, plant and equipment	**554**	588

No indicators of impairment were identified for property, plant and equipment assets.

All revaluations are independent and are conducted in accordance with the revaluation policy stated at Note 1.11. The 2012 valuations were conducted by an independent valuer, the Australian Valuation Office. As at 30 June 2014, the AOFM had cumulative net revaluation losses of $13,137 for leasehold improvements and $69,850 for computers, plant and equipment which were recognised as expenses in the Statement of Comprehensive Income.

Note 7: Non-financial assets (continued)

	2014 $'000	2013 $'000
Note 7B: Intangibles		
Computer software (purchased):		
Gross value - at cost	**4,245**	3,342
Accumulated amortisation	**(3,278)**	(3,189)
Total intangibles	**967**	153

No indicators of impairment were identified for intangible assets.

The following tables reconcile the opening and closing balances of property, plant and equipment, and intangible assets.

	Leasehold improvements 2014 $'000	Computers, plant and equipment 2014 $'000	Computer software (purchased) 2014 $'000	Total 2014 $'000
Note 7C: Reconciliation of opening and closing balances				
As at 1 July 2013				
Gross book value	**1,137**	**462**	**3,342**	**4,941**
Acc depreciation/amortisation	**(864)**	**(147)**	**(3,189)**	**(4,200)**
Net book value 1 July 2013	**273**	**315**	**153**	**741**
Additions:				
By purchase	**1**	**183**	**979**	**1,163**
Depreciation/amortisation charge	**(109)**	**(107)**	**(161)**	**(377)**
Disposals:				
Gross book value	**-**	**(13)**	**(76)**	**(89)**
Acc depreciation/amortisation	**-**	**11**	**72**	**83**
Net book value 30 June 2014	**165**	**389**	**967**	**1,521**
As at 30 June 2014				
Gross book value	**1,138**	**632**	**4,245**	**6,015**
Acc depreciation/amortisation	**(973)**	**(243)**	**(3,278)**	**(4,494)**
Net book value 30 June 2014	**165**	**389**	**967**	**1,521**

Note 7: Non-financial assets (continued)

	Leasehold improvements	Computers, plant and equipment	Computer software (purchased)	Total
	2013	2013	2013	2013
	$'000	$'000	$'000	$'000
Note 7C: Reconciliation of opening and closing balances (continued)				
As at 1 July 2012				
Gross book value	1,053	290	3,335	4,678
Acc depreciation/amortisation	(760)	(33)	(3,046)	(3,839)
Net book value 1 July 2012	293	257	289	839
Additions:				
By purchase	84	176	24	284
Depreciation/amortisation charge	(104)	(116)	(160)	(380)
Disposals:				
Gross book value	-	(4)	(17)	(21)
Acc depreciation/amortisation	-	2	17	19
Net book value 30 June 2013	273	315	153	741
As at 30 June 2013				
Gross book value	1,137	462	3,342	4,941
Acc depreciation/amortisation	(864)	(147)	(3,189)	(4,200)
Net book value 30 June 2013	273	315	153	741

	2014	2013
	$'000	$'000
Note 7D: Other non-financial assets		
Prepayments	**952**	84
Total other non-financial assets	**952**	84
Other non-financial assets are expected to be recovered in:		
No more than 12 months	**952**	83
More than 12 months	**-**	1
Total other non-financial assets	**952**	84

No indicators of impairment were identified for other non-financial assets.

Note 8: Payables

	2014 $'000	2013 $'000
Note 8A: Supplier payables		
With related entities:		
Trade creditors and accruals(a)	**22**	33
With external parties:		
Trade creditors and accruals(a)	**67**	204
Total supplier payables	**89**	237
Supplier payables are expected to be settled in:		
No more than 12 months	**89**	237
Total supplier payables	**89**	237
Note 8B: Other payables		
Salaries and wages	**166**	150
Superannuation	**28**	32
Tax and other	**6**	1
Total other payables	**200**	183
Other payables are expected to be settled in:		
No more than 12 months	**200**	183
Total other payables	**200**	183

(a) Settlement is usually made net 30 days.

Note 9: Provisions

	2014 $'000	2013 $'000
Note 9A: Employee provisions		
Annual leave	**448**	452
Long service leave	**1,291**	1,197
Superannuation	**206**	200
Total employee provisions	**1,945**	1,849
Employee provisions are expected to be settled in:		
No more than 12 months	**361**	339
More than 12 months	**1,584**	1,510
Total employee provisions	**1,945**	1,849
Note 9B: Other provisions		
Make-good on leasehold premise(a)	**140**	136
Total other provisions	**140**	136
Other provisions are expected to be settled in:		
More than 12 months	**140**	136
Total other provisions	**140**	136
Reconciliation of movements in other provisions:		
Opening balance	**136**	136
Re-measurement	**4**	-
Closing balance	**140**	136

(a) In accordance with the terms of its lease agreement for office accommodation, the AOFM is required to restore its leased premises to original condition at the conclusion of the lease in 2015. The AOFM has made a provision to recognise this obligation.

Note 10: Non-financial assets carried at fair value

Note 10A: Fair value measurements

The following table discloses the quality of significant inputs used to determine the fair value of non-financial assets measured at fair value as at year end, by assigning a three level hierarchy to those valuations.

		Carrying value at the end of the reporting period using		
	Last revalued	Level 1 inputs(a) 2014 $'000	Level 2 inputs(b) 2014 $'000	Level 3 inputs(c) 2014 $'000
Computers, plant and equipment	Mar-12	-	389	-
Leasehold improvements	Mar-12	-	-	165
Total		-	389	165

(a) The fair value is determined using unadjusted prices in active markets for identical assets.
(b) The fair value is determined using inputs, other than quoted prices included within Level 1 that are observable for the asset either directly or indirectly.
(c) The fair value is determined using unobservable inputs for the asset.

Note 10B: Valuation technique and inputs for level 2 and level 3 fair value measurements

The following table discloses the techniques and significant inputs for level 2 and level 3 fair value measurements.

	Category (Level 2 or Level 3)	Carrying value $'000	Valuation technique	Inputs used
Computers, plant and equipment	2	389	Market approach	Reference to recent market evidence of comparable items in second-hand markets
Leasehold improvements	3	165	Depreciated replacement cost	Current gross replacement cost per sq. metre
				Consumed economic benefits (unobservable input)

(a) Level 3 fair value measurements — sensitivity of inputs

Leasehold improvements — the depreciated replacement cost valuation technique estimates the gross cost to replace the service potential of the asset using observable market inputs (current replacement cost), *less* the estimated economic benefits consumed by the AOFM over the expected useful life of the asset. The gross replacement cost has been determined by an independent qualified valuer using industry based costing guidelines.

The consumed economic benefits is an unobservable valuation input, and was determined by the AOFM and an independent qualified valuer using professional judgement regarding physical, economic and external obsolescence factors.

(b) Level 3 fair value measurements — sensitivity analysis for non-financial assets

The significant unobservable input in relation to leasehold improvements is the consumed economic benefits of the asset represented by the estimated useful life of the asset to the AOFM. A significant increase (decrease) in this input would result in a higher (lower) net fair value.

The current property lease is for 15 years less one day and expires on 21 December 2015. There is no renewal option within the lease. Accordingly the AOFM is depreciating its leasehold improvements over a useful life period that will cease at the end of the contracted lease term. The AOFM may negotiate a new lease and continue to use its leasehold improvements beyond December 2015. A change to the lease term may have a material impact on the depreciated replacement cost of leasehold improvements. Each 1-year extension in the useful life of leasehold improvements equates to approximately a $70,000 increase in net fair value.

Note 10C: Reconciliation for level 3 fair value measurements

The following table reconciles the opening and closing balances of level 3 fair value measurements.

	Leasehold improvements 2014 $'000	Total 2014 $'000
Opening balance	273	273
Total gains (losses) recognised in net cost of services(a)	(109)	(109)
Purchases	1	1
Sales	-	-
Transfers into Level 3	-	-
Transfers out of Level 3	-	-
Closing balance	165	165

(a) These gains (losses) are presented in the Statement of Comprehensive Income under depreciation and amortisation.

Note 11: Cash flow reconciliation

The following table reconciles the AOFM's operating cash flows as presented in the Statement of Cash Flows to its net cost of services presented in the Statement of Comprehensive Income.

	2014 $'000	2013 $'000
Net cost of services	**(9,874)**	(8,877)
Add revenue from Government	**11,479**	11,409
Adjustments for non-cash items:		
Depreciation and amortisation	**377**	380
Write-down and impairment of assets	**6**	2
Property, plant and equipment and intangibles accruals	**4**	10
Repeal of appropriations	**(3,447)**	-
Change in receivables for DCB(a)	**(759)**	112
Adjustments for changes in assets:		
(Increase) decrease in receivables	**3,113**	(2,938)
(Increase) decrease in other non-financial assets	**(868)**	(27)
Adjustments for changes in liabilities:		
Increase (decrease) in employee provisions	**96**	147
Increase (decrease) in other provisions	**4**	-
Increase (decrease) in other payables	**17**	18
Increase (decrease) in supplier payables	**(148)**	(236)
Net cash from (used by) operating activities	**-**	-

(a) DCB = Departmental Capital Budget.

The following table reconciles cash and cash equivalents reported in the Statement of Cash Flows to items that comprise cash and cash equivalents in the Statement of Financial Position.

	2014 $'000	2013 $'000
Items in statement of financial position		
Financial assets - cash and cash equivalents	**100**	100
Total items in the statement of financial position	**100**	100
Total as per statement of cash flows	**100**	100

Note 12: Contingent liabilities and assets

Unquantifiable contingencies

The AOFM is not aware of any unquantifiable contingencies as of the signing date that may have an impact on its operations.

Remote contingencies

The AOFM has indemnified a number of contractors providing goods and services under contract for losses incurred by the contractor due to, amongst other things, the AOFM's failure to observe certain terms of contract, or for wrongful, unlawful or negligent acts committed by the AOFM. The AOFM is not aware of any event that has occurred that may trigger action under the indemnities.

Furthermore, under a number of contracts, the contractor's liability to the AOFM for losses arising from certain circumstances is capped. The AOFM has assessed that the likelihood of significant losses above the liability cap is remote.

Note 13: Executive remuneration

Remuneration means any money, consideration or benefit including wages, salaries, accrued leave entitlements (excluding superannuation on-costs), superannuation contributions (including notional contributions made to defined benefits schemes at a rate determined by the Department of Finance), the cost of motor vehicles, housing, commuting, fringe benefits tax and allowances. Remuneration does not include reimbursement of out-of-pocket expenses incurred for work related purposes. Where the AOFM is not entitled to an input tax credit, remuneration includes the non-recoverable GST amount. AOFM employees are not eligible to receive performance bonuses.

Remuneration expenses (on an accruals basis) for officers in the senior executive service

Actual remuneration expensed during the financial year(a)	**2014** **$**	2013 $
Short-term employee benefits:		
Salary and other short-term benefits	**332,531**	306,026
Annual leave accrued	**26,406**	26,406
Total short term employee benefits	**358,937**	332,432
Post employment benefits:		
Superannuation(b)	**46,930**	44,366
Total post employment benefits	**46,930**	44,366
Termination benefits:		
Separation payments	**-**	-
Total termination benefits	**-**	-
Other long-term benefits:		
Long service leave(c)	**9,152**	8,521
Total other long-term benefits	**9,152**	8,521
Total senior executive remuneration expenses	**415,019**	385,319

(a) Excludes officers not in the Senior Executive Service on acting arrangements in positions that are Senior Executive Service positions, and Senior Executive Service officers not employed for the full year whose total remuneration was less than $195,000 for the year.

(b) Superannuation contributions are paid into the employee's superannuation scheme at a rate determined by the Department of Finance. The contributions made by the AOFM into a defined benefit scheme do not necessarily correspond with the officer's benefit under the scheme which is governed by legislation.

(c) The value of the long service leave provision at the end of June is determined based on advice from the Australian Government Actuary. The valuation includes the use of a discount rate to equate the expected future payments of the benefit to a net present value. The discount rate is determined based on differences between future expectations of long-term salary increases and the long-term bond rate. Changes from year to year in the discount rate used to value long service leave have an impact on the level of remuneration reported for a financial year. As at 30 June 2014 the discount rate was 97.7 per cent (30 June 2013: 97.6 per cent).

Note 13: Executive remuneration (continued)

The following table discloses the number (on a headcount basis) and reportable remuneration of senior executive service (SES) officers for the reporting period.

Average reportable remuneration paid (on a cash basis) to officers in the senior executive service

	Senior executives	Reportable salary(a)	Contributed superannuation(b)	Reportable allowances(c)	Bonus paid	Total
	2014	**2014**	**2014**	**2014**	**2014**	**2014**
	No.	**$**	**$**	**$**	**$**	**$**
Total reportable remuneration						
$375,000 to $404,999	**1**	**350,245**	**46,715**	**-**	**-**	**396,960**
Total	**1**					
	2013	2013	2013	2013	2013	2013
	No.	$	$	$	$	$
Total reportable remuneration						
$375,000 to $404,999	1	339,606	44,300	-	-	383,906
Total	1					

(a) ‘Reportable salary’ is the average actual gross payments paid (less any bonuses paid) and reportable fringe benefits (at the net amount prior to ‘grossing up’ for the purposes of deriving taxable value of fringe benefits) for senior executives in that reportable remuneration band during the reporting period as per each individual’s payment summary.
(b) The ‘contributed superannuation’ amount is the average actual superannuation contributions paid to senior executives in that reportable remuneration band during the reporting period, excluding salary sacrificed to superannuation which is reported in reportable salary.
(c) ‘Reportable allowances’ is the average actual allowances paid to senior executives in that reportable remuneration band during the reporting period as per each individual’s payment summary.

Note 13: Executive remuneration (continued)

Average reportable remuneration paid (on a cash basis) to other highly paid staff during the reporting period

The following table discloses the number (on a headcount basis) and reportable remuneration of officers not in the SES who had reportable remuneration of $195,000 or more for the reporting period.

	Highly paid staff	Reportable salary(a)	Contributed superannuation(b)	Reportable allowances(c)	Bonus paid	Total
	2014	**2014**	**2014**	**2014**	**2014**	**2014**
	No.	**$**	**$**	**$**	**$**	**$**
Total reportable remuneration						
$195,000 to $224,999	**1**	**185,647**	**38,862**	**-**	**-**	**224,509**
$225,000 to $254,999	**4**	**212,793**	**36,567**	**860**	**-**	**250,220**
$255,000 to $284,999	**3**	**224,267**	**39,368**	**4,282**	**-**	**267,917**
$345,000 to $374,999	**1**	**296,034**	**58,695**	**-**	**-**	**354,729**
Total	**9**					

	2013	2013	2013	2013	2013	2013
	No.	$	$	$	$	$
Total reportable remuneration						
$225,000 to $254,999	4	204,017	31,192	-	-	235,209
$255,000 to $284,999	3	226,150	34,259	-	-	260,409
$315,000 to $344,999	1	277,513	47,953	-	-	325,466
Total	8					

(a) 'Reportable salary' is the average gross payments (less any bonuses paid) including salary sacrificed to superannuation and reportable fringe benefits (at the net amount prior to 'grossing up' for the purposes of deriving the taxable value of fringe benefits) for staff in that reportable remuneration band during the reporting period as per each individual's payment summary.

(b) The 'contributed superannuation' amount is the average actual superannuation contributions paid to officers in that reportable remuneration band during the reporting period, excluding any salary sacrificed to superannuation which is reported in reportable salary.

(c) 'Reportable allowances' is the average actual allowances paid to officers in that reportable remuneration band during the reporting period as per each individual's payment summary.

Note 14: Remuneration of auditors

Financial statement audit services are provided free of charge to the AOFM. The fair value of the audit services provided by the Australian National Audit Office was:

	2014 $'000	2013 $'000
Remuneration of auditors	**320**	303

Auditors' remuneration is disclosed inclusive of GST.

No other services were provided by the Auditor-General.

Note 15: Average staffing level

The average staffing level (paid only) for the AOFM during the year was:

	2014	2013
Average staffing level	**42**	40

Note 16: Compensation and debt relief in special circumstances

	2014 $'000	2013 $'000
Departmental		
No 'Act of Grace' payments were made during the reporting period (2012-13: nil).	**-**	-
No waivers of amounts owing to the Government were made pursuant to subsection 34(1) of the *Financial Management and Accountability Act 1997* during the reporting period (2012-13: nil).	**-**	**-**
No payments were made under the 'Defective Administration Scheme' during the reporting period (2012-13: nil).	**-**	-
No payments were made under section 73 of the *Public Service Act 1999* during the reporting period (2012-13: nil).	**-**	-
No payments were made under ex-gratia programs during the reporting period (2012-13: nil).	**-**	**-**

	2014 $'000	2013 $'000
Administered		
No 'Act of Grace' payments were made during the reporting period (2012-13: nil).	**-**	-
No waivers of amounts owing to the Government were made pursuant to subsection 34(1) of the *Financial Management and Accountability Act 1997* during the reporting period (2012-13: 27)(a).	**-**	320,000
No payments were made under the 'Defective Administration Scheme' during the reporting period (2012-13: nil).	**-**	-
No payments were made under section 73 of the *Public Service Act 1999* during the reporting period (2012-13: nil).	**-**	-
No payments were made under ex-gratia programs during the reporting period (2012-13: nil).	**-**	-

(a) On 26 June 2013, the Finance Minister waived 27 loans with a total face value of $320 million made to the South Australian Government between 1956 and 1981 under Commonwealth-State financing arrangements.

Note 17: Administered income before re-measurements

	2014 $'000	2013 $'000
Note 17A: Interest revenue(a)		
Loans to State and Territory Governments:		
State and Territory debt	**239**	239
Advances	**127,738**	149,072
Investments (under FMA section 39):(b)		
Deposits	**607,854**	499,531
Residential mortgage-backed securities	**308,441**	472,645
Total interest revenue	**1,044,272**	1,121,487
Note 17B: Other revenue		
Securities lending and other revenue	**349**	40
Total other revenue	**349**	40

(a) Recognised using the effective interest rate method.
(b) FMA = *Financial Management and Accountability Act 1997*.

Note 18: Administered expenses before re-measurements

	2014 $'000	2013 $'000
Note 18A: Grants		
Public Sector:		
State and Territory Governments(a)	**20**	21
Total grants	**20**	21
Note 18B: Interest expenses		
Commonwealth Government Securities interest:(b)		
Treasury Bonds	**11,806,154**	10,569,738
Treasury Indexed Bonds	**1,460,836**	1,173,938
Treasury Notes	**121,751**	480,768
Other debt	**946**	678
Total Commonwealth Government Securities interest	**13,389,687**	12,225,122
Other interest costs	**288**	21
Total interest expenses	**13,389,975**	12,225,143
Note 18C: Supplier expenses(c)		
Registry and other costs	**756**	998
Syndication fees	**23,063**	11,147
Total supplier expenses	**23,819**	12,145

(a) Grants represent Commonwealth contributions into the Debt Retirement Reserve Trust Account — see Note 28G.
(b) Recognised using the effective interest rate method.
(c) From 29 June 2011 the *Commonwealth Inscribed Stock Act 1911* was amended to provide an appropriation to meet the costs and expenses of issuance and sale of stock, and the cost of managing stock issued under the Act. Previously these costs were met through departmental appropriations. In addition, on 17 November 2012 the Commonwealth Inscribed Stock Act was amended to provide an appropriation to meet costs and expenses arising from depository interests in stock issued under the Act.

Note 19: Administered gains (losses) before re-measurements

	2014 $'000	2013 $'000
Note 19A: Net foreign exchange gains (losses)		
Foreign currency denominated loans and securities	**78**	(500)
Total net foreign exchange gains (losses)	**78**	(500)
Note 19B: Net realised gains (losses) on financial instruments(a)		
Waiver of South Australian loans by the Minister for Finance	**-**	(283,863)
Sale of residential mortgage-backed securities	**12,576**	5,291
Repurchase of debt	**(194,329)**	-
Total net realised gains (losses) on financial instruments	**(181,753)**	(278,572)

(a) Total net realised gains (losses) on financial instruments represent the total proceeds paid or received from a sale or termination, less the amortised cost carrying value using the effective interest method at the time of sale or termination.

Note 20: Administered re-measurements

	2014 $'000	2013 $'000
Net market revaluation gains (losses)(a)		
Commonwealth Government Securities	**(3,686,211)**	11,498,357
Deposits	**(40)**	13
Residential mortgage-backed securities	**15,434**	169,583
Total net market revaluation gains (losses)	**(3,670,817)**	11,667,953

(a) Net market revaluation gains (losses) represent the unrealised fair value gains (losses) on the portfolio of administered financial assets and financial liabilities. Changes in the carrying value of financial assets and financial liabilities are attributed between changes in the amortised cost carrying value and other changes in carrying value. Changes attributable to amortised cost are recognised in revenue before re-measurements or expenses before re-measurements. Other changes in carrying value (including due to a change in interest rates) are recognised as administered re-measurements. Where a financial asset is sold or a financial liability is repurchased during the financial year, the cumulative unrealised market value gain or loss at that time is reversed against administered re-measurements. The revaluation effect will net to zero over the life of a financial instrument, either at maturity or on termination prior to maturity.

Note 21: Administered assets(a)

	2014 $'000	2013 $'000
Note 21A: Investments (under FMA section 39)(b)		
Designated at fair value through profit or loss:		
Deposits	**27,116,335**	20,159,143
Residential mortgage-backed securities	**6,059,565**	9,113,022
Total investments (under FMA section 39)	**33,175,900**	29,272,165
Investments maturing:(c)		
Within one year	**27,300,967**	20,641,049
In one to five years	**5,485,300**	7,201,441
In more than five years	**389,633**	1,429,675
Total investments (under FMA section 39)	**33,175,900**	29,272,165
Note 21B: Receivables		
At amortised cost:		
Loans to State and Territory Governments:		
Principal	**2,373,934**	2,462,609
Balance of special account(d)	**(843)**	(742)
Unamortised net discounts	**(267,015)**	(284,748)
Total receivables	**2,106,076**	2,177,119
Receivables maturing:(e)		
Within one year	**2,337**	1,815
In one to five years	**31,315**	28,795
In more than five years	**2,072,424**	2,146,509
Total receivables	**2,106,076**	2,177,119
Receivables are aged as follows:		
Not overdue	**2,106,076**	2,177,119
Overdue	**-**	-
Total receivables	**2,106,076**	2,177,119
Note 21C: Accrued revenue		
Accrued interest on loans to State and Territory Governments	**383**	394
Total accrued revenue	**383**	394
Accrued revenue maturing:		
Within one year	**383**	394
Total accrued revenue	**383**	394

(a) Where the amortised cost accounting convention is applied, the value of a financial asset is disaggregated and recorded against several financial statement classes (for example, the principal value of a financial asset is classified separately to coupons receivable on the asset).
(b) FMA = *Financial Management and Accountability Act 1997*.
(c) The maturity profile is based on contractual maturity dates, with the exception of residential mortgage-backed securities. For residential mortgage-backed securities the maturity profile is based on the weighted average life of each investment.
(d) Refer to Note 28G for special account balances.
(e) Loans to State and Territory Governments are composed primarily of credit foncier loans. The maturity profile is based on the maturity date of each loan and disregarding principal repayments prior to that time.

Note 22: Administered liabilities(a)

	2014 $'000	2013 $'000
Note 22A: Commonwealth Government Securities		
Designated at fair value through profit or loss:		
Treasury Bonds	**313,875,056**	253,157,332
Treasury Indexed Bonds	**32,418,652**	27,092,922
Treasury Notes	**4,974,038**	5,483,361
Other debt	**6,926**	7,408
Total designated at fair value through profit or loss	**351,274,672**	285,741,023
At amortised cost:		
Other debt	**13,809**	13,702
Total Commonwealth Government Securities	**351,288,481**	285,754,725
Commonwealth Government Securities maturing:(b)		
Within one year	**32,583,532**	28,742,733
In one to five years	**137,239,754**	115,592,451
In more than five years	**181,465,195**	141,419,541
Total Commonwealth Government Securities	**351,288,481**	285,754,725
Note 22B: Other		
Interest payable on other debt (at amortised cost)	**93**	93
Total other	**93**	93
Other maturing:		
Within one year	**93**	93
Total other	**93**	93
Note 22C: Accrued expenses		
Costs and expenses on CGS and depository interests	**31**	214
Total accrued expenses	**31**	214
Accrued expenses maturing:		
Within one year	**31**	214
Total accrued expenses	**31**	214

(a) Where the AOFM applies fair value accounting to a financial liability, the aggregate value of the financial liability is recorded against a single financial statement class. Where the amortised cost accounting convention is applied, the value of a financial liability is disaggregated and recorded against several financial statement classes (for example: the principal value of a financial liability is classified separately from coupons payable on the liability).

(b) The maturity profile is based on contractual maturity dates.

Note 23: Administered cash flow reconciliation

The following table reconciles cash as per the Administered Schedule of Assets and Liabilities to the Administered Schedule of Cash Flows. It also reconciles the surplus (deficit) reported in the Administered Schedule of Comprehensive Income to net cash flows from operating activities reported in the Administered Schedule of Cash Flows.

	2014 $'000	2013 $'000
Reconciliation of cash and cash equivalents as per administered schedule of assets and liabilities to administered schedule of cash flows		
Cash and cash equivalents as per:		
Administered schedule of cash flows	**622**	622
Administered schedule of assets and liabilities	**622**	622
Difference	-	-
Reconciliation of comprehensive income to net cash from operating activities		
Surplus (deficit)	**(16,221,685)**	273,099
Adjustments for non-cash items		
Amortisation and capital accretion of debt instruments	**(1,046,085)**	(844,618)
Amortisation of net discounts on Loans to State and Territory Governments	**(17,733)**	(20,799)
Net (gain) loss on sale of financial instruments	**181,753**	278,572
Net foreign exchange (gains) losses	**(78)**	500
Re-measurements	**3,670,817**	(11,667,953)
Debt Retirement Reserve Trust Account contributions and interest payments(a)	**39**	42
Other	**220**	-
Adjustments for cash items		
Capital accretion costs on repurchase of debt	**(1,329,288)**	-
Accrual adjustments		
Interest accruals on debt instruments	**742,489**	414,188
Interest accruals on financial assets	**(1,029)**	2,145
Accrued expenses	**(183)**	214
Net cash used by operating activities	**(14,020,763)**	(11,564,610)

(a) Debt Retirement Reserve Trust Account contributions and interest payments increase the balance of the Debt Retirement Reserve Trust Account (see Note 28G) but comprise a notional payment only.

Note 24: Administered contingent liabilities and assets

Unquantifiable contingencies

The AOFM is not aware of any unquantifiable contingencies as of the signing date that may have an impact on its operations.

Remote contingencies

(i) The Government has indemnified agents of foreign currency denominated loans issued by the Australian Government outside Australia against any loss, liability, costs, claims, charges, expenses, actions or demands due to any misrepresentation by the Australian Government and any breach of warranties. The AOFM is not aware of any event that has occurred that may trigger action under the indemnities.

(ii) In the unlikely event of default by a borrower of Treasury Bonds or Treasury Indexed Bonds under the securities lending facility, the AOFM would be in a position to sell the securities pledged by the borrower to offset the increased liability to the Government. As at 30 June 2014 there were no open transactions under the AOFM's securities lending facility (30 June 2013: nil).

Note 25: Administered financial instruments

Note 25A: Categories of administered financial assets and liabilities

Under Australian Accounting Standards a financial instrument must be measured at fair value on initial recognition. After initial recognition the accounting treatment for a financial instrument is dependent on the category under which the financial instrument is classified. The following table illustrates the AOFM's financial instruments by category:

	2014 $'000	2013 $'000
Administered financial assets		
Cash	**622**	622
Loans and receivables (at amortised cost):		
Loans to State and Territory Governments	**2,106,076**	2,177,119
Accrued interest on loans to State and Territory Governments	**383**	394
Total loans and receivables (at amortised cost)	**2,106,459**	2,177,513
Fair value through profit or loss (designated by the AOFM):		
Investments	**33,175,900**	29,272,165
Total fair value through profit or loss (designated by the AOFM)	**33,175,900**	29,272,165
Carrying amount of financial assets	**35,282,981**	31,450,300
Administered financial liabilities(a)		
Fair value through profit or loss (designated by the AOFM):		
Treasury Bonds	**313,875,056**	253,157,332
Treasury Indexed Bonds	**32,418,652**	27,092,922
Treasury Notes	**4,974,038**	5,483,361
Other debt	**6,926**	7,408
Total fair value through profit or loss (designated by the AOFM)	**351,274,672**	285,741,023
Other financial liabilities (at amortised cost):		
Other debt	**13,809**	13,702
Interest payable on other debt	**93**	93
Total other financial liabilities (at amortised cost):	**13,902**	13,795
Carrying amount of financial liabilities	**351,288,574**	285,754,818
Net financial assets	**(316,005,593)**	(254,304,518)

(a) Accrued expenses have been excluded from disclosures relating to financial instruments.

Note 25: Administered financial instruments (continued)

Note 25B: Interest rate risk

The AOFM's exposure to interest rate risk and corresponding weighted average effective interest rates from financial instruments is set out below. The maturity profile is based on contractual maturity dates except for residential mortgage-backed securities in which the maturity profile is based on the weighted average life of each security. Those financial instruments with a fixed interest rate expose the net debt portfolio to changes in fair value with changes in interest rates, whilst those financial instruments at floating interest rates expose the net debt portfolio to changes in debt servicing costs with changes in interest rates. The extent to which the AOFM can match the repricing profile of its financial assets with those of its financial liabilities is limited by the differences in the volumes and the need for assets to be available for cash management or other purposes.

	Fixed interest rate	Floating interest rate	Non interest bearing	Total	Weighted average interest(a)
	2014 $'000	2014 $'000	2014 $'000	2014 $'000	2014 %
Financial assets					
Cash	-	-	622	622	-
Loans to State and Territory Governments	2,106,456	-	3	2,106,459	5.88
Deposits	27,116,335	-	-	27,116,335	2.48
Residential mortgage-backed securities	-	6,059,565	-	6,059,565	3.93
Total financial assets	**29,222,791**	**6,059,565**	**625**	**35,282,981**	
Financial liabilities					
Treasury Bonds	313,875,056	-	-	313,875,056	4.22
Treasury Indexed Bonds(b)	32,418,652	-	-	32,418,652	2.21
Treasury Notes	4,974,038	-	-	4,974,038	2.51
Other debt	14,997	-	5,831	20,828	3.66
Total financial liabilities	**351,282,743**	**-**	**5,831**	**351,288,574**	
Net financial assets	**(322,059,952)**	**6,059,565**	**(5,206)**	**(316,005,593)**	

(a) Interest rates are nominal interest rates with the exception of Treasury Indexed Bonds (which are real interest rates).

(b) Treasury Indexed Bonds have their principal value indexed against the (all groups) Australian Consumer Price Index. The interest is a fixed real rate of interest payable on the accreted principal value. Accordingly these instruments expose the AOFM to cash flow risk on interest payments and on the value of principal payable on maturity or on redemption prior to maturity.

Note 25: Administered financial instruments (continued)

Note 25B: Interest rate risk (continued)

	Maturing in				
	1 year or less	1 to 5 years	5 years or more	Total	Weighted average interest(a)
	2014	2014	2014	2014	2014
	$'000	$'000	$'000	$'000	%
Financial assets					
Cash	622	-	-	622	-
Loans to State and Territory Governments	2,720	31,315	2,072,424	2,106,459	5.88
Deposits	27,116,335	-	-	27,116,335	2.48
Residential mortgage-backed securities	184,632	5,485,300	389,633	6,059,565	3.93
Total financial assets	27,304,309	5,516,615	2,462,057	35,282,981	
Financial liabilities					
Treasury Bonds	27,603,663	132,346,383	153,925,010	313,875,056	4.22
Treasury Indexed Bonds(b)	-	4,886,445	27,532,207	32,418,652	2.21
Treasury Notes	4,974,038	-	-	4,974,038	2.51
Other debt	5,924	6,926	7,978	20,828	3.66
Total financial liabilities	32,583,625	137,239,754	181,465,195	351,288,574	
Net financial assets	(5,279,316)	(131,723,139)	(179,003,138)	(316,005,593)	

(a) Interest rates are nominal interest rates with the exception of Treasury Indexed Bonds (which are real interest rates).

(b) Treasury Indexed Bonds have their principal value indexed against the (all groups) Australian Consumer Price Index. The interest is a fixed real rate of interest payable on the accreted principal value. Accordingly these instruments expose the AOFM to cash flow risk on interest payments and on the value of principal payable on maturity or on redemption prior to maturity.

Note 25: Administered financial instruments (continued)

Note 25B: Interest rate risk (continued)

	Fixed interest rate	Floating interest rate	Non interest bearing	Total	Weighted average interest(a)
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 %
Financial assets					
Cash	-	-	622	622	-
Loans to State and Territory Governments	2,177,510	-	3	2,177,513	5.88
Deposits	20,159,143	-	-	20,159,143	2.76
Residential mortgage-backed securities	-	9,113,022	-	9,113,022	4.16
Total financial assets	22,336,653	9,113,022	625	31,450,300	
Financial liabilities					
Treasury Bonds	253,157,332	-	-	253,157,332	4.45
Treasury Indexed Bonds(b)	27,092,922	-	-	27,092,922	2.75
Treasury Notes	5,483,361	-	-	5,483,361	2.72
Other debt	15,480	-	5,723	21,203	3.70
Total financial liabilities	285,749,095	-	5,723	285,754,818	
Net financial assets	(263,412,442)	9,113,022	(5,098)	(254,304,518)	

	Maturing in				
	1 year or less	1 to 5 years	5 years or more	Total	Weighted average interest(a)
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 %
Financial assets					
Cash	622	-	-	622	-
Loans to State and Territory Governments	2,209	28,795	2,146,509	2,177,513	5.88
Deposits	20,159,143	-	-	20,159,143	2.76
Residential mortgage-backed securities	481,906	7,201,441	1,429,675	9,113,022	4.16
Total financial assets	20,643,880	7,230,236	3,576,184	31,450,300	
Financial liabilities					
Treasury Bonds	23,253,507	109,862,880	120,040,945	253,157,332	4.45
Treasury Indexed Bonds(b)	-	5,722,304	21,370,618	27,092,922	2.75
Treasury Notes	5,483,361	-	-	5,483,361	2.72
Other debt	5,958	7,267	7,978	21,203	3.70
Total financial liabilities	28,742,826	115,592,451	141,419,541	285,754,818	
Net financial assets	(8,098,946)	(108,362,215)	(137,843,357)	(254,304,518)	

(a) Interest rates are nominal interest rates with the exception of Treasury Indexed Bonds (which are real interest rates).

(b) Treasury Indexed Bonds have their principal value indexed against the (all groups) Australian Consumer Price Index. The interest is a fixed real rate of interest payable on the accreted principal value. Accordingly these instruments expose the AOFM to cash flow risk on interest payments and on the value of principal payable on maturity or on redemption prior to maturity.

Note 25: Administered financial instruments (continued)

Note 25C: Foreign exchange risk

Foreign exchange risk arises from debt the AOFM holds in foreign denominated currencies and represents the risk to debt servicing costs and the value of the net debt portfolio caused by a change in foreign exchange rates. Currently the AOFM's foreign exchange risk arises from contractual obligations on foreign currency loans and securities. The AOFM's exposure to foreign exchange risk is not material.

The Australian equivalent principal value of foreign currency loans and securities is disclosed in the following table:

	2014 AUD $'000	2013 AUD $'000
FOREIGN CURRENCY DENOMINATED LIABILITIES		
Current:		
Pounds sterling	**94**	85
Japanese yen	**4**	4
Swiss francs	**61**	58
Euros	**8**	8
Total current	**167**	155
Non-current:		
United States dollars	**5,649**	5,737
Total non-current	**5,649**	5,737
Total foreign currency denominated liabilities	**5,816**	5,892
FOREIGN CURRENCY DENOMINATED ASSETS		
Current:		
Pounds sterling	**4**	3
Total current	**4**	3
Total foreign currency denominated assets	**4**	3

Note 25: Administered financial instruments (continued)

Note 25D: Contractual maturities of financial liabilities

The following table discloses the undiscounted value of the contractual maturities of financial liabilities as at the end of the financial year, including estimated future interest payments.

	Less than 1 year	**1 to 2 years**	**2 to 5 years**	**5+ years**	**Total**
	2014 $'000	**2014 $'000**	**2014 $'000**	**2014 $'000**	**2014 $'000**
Treasury Bonds	**40,686,693**	**48,164,585**	**114,935,532**	**171,434,219**	**375,221,029**
Treasury Indexed Bonds(a)	**795,447**	**2,720,216**	**4,918,428**	**27,455,961**	**35,890,052**
Treasury Notes	**5,000,000**	**-**	**-**	**-**	**5,000,000**
Other debt(b)	**473**	**473**	**6,122**	**-**	**7,068**
Total	**46,482,613**	**50,885,274**	**119,860,082**	**198,890,180**	**416,118,149**
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000
Treasury Bonds	34,356,551	37,198,614	97,965,336	131,366,849	300,887,350
Treasury Indexed Bonds(a)	791,959	791,959	7,140,302	21,572,817	30,297,037
Treasury Notes	5,500,000	-	-	-	5,500,000
Other debt(b)	480	480	6,698	-	7,658
Total	40,648,990	37,991,053	105,112,336	152,939,666	336,692,045

(a) The interest payments and principal value are indexed against the (all groups) Australian Consumer Price Index (CPI). There is a six month lag between the calculation period for the CPI and its impact on the value of interest and principal. Interest payments and principal value on redemption are projected at the CPI for the March quarter and held constant thereafter.

(b) Perpetual debt and overdue debt have been excluded from this analysis.

Note 25: Administered financial instruments (continued)

Note 25E: Credit risk

The following table sets out the AOFM's credit risk by asset class and credit rating as at 30 June. In the table, where a counterparty has a split rating between the rating agencies, the AOFM's exposure to the counterparty is allocated to the lower credit rating.

The AOFM's assets are of strong credit quality. The AOFM's exposure to credit risk under the securities lending facility and its repurchase agreements as at year end is zero.

S&P or Fitch long-term rating **Moody's long-term rating**	**AAA** **Aaa**	**AA+** **Aa1**	**AA** **Aa2**	**Total** **Total**
	2014 **$'000**	**2014** **$'000**	**2014** **$'000**	**2014** **$'000**
By instrument				
Cash(a)	**622**	**-**	**-**	**622**
Loans to State and Territory Governments	**1,107,789**	**1,175,057**	**237,114**	**2,519,960**
Deposits(a)	**27,116,335**	**-**	**-**	**27,116,335**
Residential mortgage-backed securities	**6,059,565**	**-**	**-**	**6,059,565**
Total	**34,284,311**	**1,175,057**	**237,114**	**35,696,482**
	2013 $'000	2013 $'000	2013 $'000	2013 $'000
By instrument				
Cash(a)	622	-	-	622
Loans to State and Territory Governments	1,582,076	739,484	238,008	2,559,568
Deposits(a)	20,159,143	-	-	20,159,143
Residential mortgage-backed securities	9,046,951	66,071	-	9,113,022
Total	30,788,792	805,555	238,008	31,832,355

(a) Cash and deposits are held with the RBA. The RBA does not issue debt in the wholesale market and accordingly does not have a credit rating. However, as Australia's central bank it is deemed to have the same credit rating as the Australian Government.

Note 25: Administered financial instruments (continued)

Note 25F: Residential mortgage-backed securities

Since September 2008, the AOFM has acquired a portfolio of AAA rated (or equivalent) residential mortgage-backed securities with a face value of $15,463 million.

Details of residential mortgage-backed securities acquired by the AOFM since the Government announced this initiative in September 2008 are contained in the following table. In April 2013, the Government announced that the AOFM would not make any new investments in RMBS.

	Opening balance	Amount invested	Principal repayments	Sales	Invested as at year end
	$'000	$'000	$'000	$'000	$'000
Financial year					
2008-09	-	6,203,420	(179,281)	-	6,024,139
2009-10	6,024,139	2,819,540	(850,664)	(73,790)	7,919,225
2010-11	7,919,225	4,349,220	(1,438,640)	-	10,829,805
2011-12	10,829,805	1,930,430	(1,509,050)	(50,000)	11,201,185
2012-13	11,201,185	160,000	(1,771,242)	(510,585)	9,079,358
2013-14	**9,079,358**	**-**	**(2,177,699)**	**(885,000)**	**6,016,659**
Total		**15,462,610**	**(7,926,576)**	**(1,519,375)**	

Note 25: Administered financial instruments (continued)

Note 25G: Net fair values of administered financial assets and liabilities

	Principal value(a)	Total carrying amount	Aggregate net fair value
	2014	**2014**	**2014**
	$'000	**$'000**	**$'000**
Administered financial assets (recognised)			
Cash	**622**	**622**	**622**
Loans to State and Territory Governments(b)	**2,373,091**	**2,106,459**	**2,519,117**
Deposits	**27,100,000**	**27,116,335**	**27,116,335**
Residential mortgage-backed securities	**6,016,659**	**6,059,565**	**6,059,565**
Total financial assets (recognised)	**35,490,372**	**35,282,981**	**35,695,639**
Administered financial liabilities (recognised)			
Treasury Bonds	**290,936,151**	**313,875,056**	**313,875,056**
Treasury Indexed Bonds	**28,721,400**	**32,418,652**	**32,418,652**
Treasury Notes	**5,000,000**	**4,974,038**	**4,974,038**
Other debt	**19,458**	**20,828**	**20,828**
Total financial liabilities (recognised)	**324,677,009**	**351,288,574**	**351,288,574**
Net financial assets (recognised)	**(289,186,637)**	**(316,005,593)**	**(315,592,935)**
	2013	2013	2013
	$'000	$'000	$'000
Administered financial assets (recognised)			
Cash	622	622	622
Loans to State and Territory Governments(b)	2,461,867	2,177,513	2,558,826
Deposits	20,150,000	20,159,143	20,159,143
Residential mortgage-backed securities	9,079,358	9,113,022	9,113,022
Total financial assets (recognised)	31,691,847	31,450,300	31,831,613
Administered financial liabilities (recognised)			
Treasury Bonds	233,539,500	253,157,332	253,157,332
Treasury Indexed Bonds	23,951,312	27,092,922	27,092,922
Treasury Notes	5,500,000	5,483,361	5,483,361
Other debt	19,438	21,203	21,203
Total financial liabilities (recognised)	263,010,250	285,754,818	285,754,818
Net financial assets (recognised)	(231,318,403)	(254,304,518)	(253,923,205)

(a) Comprises the face value of financial instruments, with the exception of Treasury Indexed Bonds where the inflation adjusted capital value at the end of the financial year is included in the principal figure.

(b) Loans to State and Territory Governments are recognised at amortised cost. These transactions are not traded and, especially for those with the longest terms to maturity, a direct market benchmark to underpin fair value measurement does not exist. In estimating aggregate net fair value, the AOFM based its valuation from data on Treasury Bonds.

Note 25: Administered financial instruments (continued)

Note 25G: Net fair values of administered financial assets and liabilities (continued)

The following table discloses the quality of significant inputs used to determine the fair value of all financial assets and financial liabilities measured at fair value as at year end, by assigning a 3 level hierarchy to those valuations.

	Level 1(a)	Level 2(b)	Level 3(c)	Total
	2014 $'000	**2014 $'000**	**2014 $'000**	**2014 $'000**
Administered financial assets (measured at fair value only)				
Deposits	**-**	**27,116,335**	**-**	**27,116,335**
Residential mortgage-backed securities	**-**	**6,059,565**	**-**	**6,059,565**
Total assets at fair value	**-**	**33,175,900**	**-**	**33,175,900**
Administered financial liabilities (measured at fair value only)				
Treasury Bonds	**286,271,393**	**27,603,663**	**-**	**313,875,056**
Treasury Indexed Bonds	**32,418,652**	**-**	**-**	**32,418,652**
Treasury Notes	**-**	**4,974,038**	**-**	**4,974,038**
Other debt	**-**	**6,926**	**-**	**6,926**
Total liabilities at fair value	**318,690,045**	**32,584,627**	**-**	**351,274,672**
	2013 $'000	2013 $'000	2013 $'000	2013 $'000
Administered financial assets (measured at fair value only)				
Deposits	-	20,159,143	-	20,159,143
Residential mortgage-backed securities	-	9,113,022	-	9,113,022
Total assets at fair value	-	29,272,165	-	29,272,165
Administered financial liabilities (measured at fair value only)				
Treasury Bonds	253,157,332	-	-	253,157,332
Treasury Indexed Bonds	27,092,922	-	-	27,092,922
Treasury Notes	-	5,483,361	-	5,483,361
Other debt	-	7,408	-	7,408
Total liabilities at fair value	280,250,254	5,490,769	-	285,741,023

(a) The fair value method is determined using unadjusted quoted prices in active markets for identical financial instruments.
(b) The fair value is determined by price quotations in non-active markets for identical financial instruments, or from price quotations in an active market for similar assets or liabilities or from other inputs that are observable by market data. The fair value is estimated by using inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices).
(c) The fair value is determined from inputs not based on observable market data. This includes significant adjustments to observable market data.

Note 25: Administered financial instruments (continued)

Note 25H: Movement in commonwealth government securities on issue (face value)

	Opening balance	Issuance	Maturities/ Redemptions	Other	Closing balance
	2014 $'000	**2014 $'000**	**2014 $'000**	**2014 $'000**	**2014 $'000**
Treasury Bonds	**233,539,500**	**80,000,000**	**(22,603,349)**	**-**	**290,936,151**
Treasury Indexed Bonds(a)	**18,319,000**	**7,288,930**	**(2,076,577)**	**-**	**23,531,353**
Treasury Notes	**5,500,000**	**19,500,000**	**(20,000,000)**	**-**	**5,000,000**
Other debt(b)	**19,438**	**-**	**(123)**	**143**	**19,458**
Total	**257,377,938**	**106,788,930**	**(44,680,049)**	**143**	**319,486,962**
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000
Treasury Bonds	205,387,900	53,750,000	(25,598,400)	-	233,539,500
Treasury Indexed Bonds(a)	16,069,000	2,250,000	-	-	18,319,000
Treasury Notes	12,500,000	53,500,000	(60,500,000)	-	5,500,000
Other debt(b)	19,038	-	(127)	527	19,438
Total	233,975,938	109,500,000	(86,098,527)	527	257,377,938

(a) The inflation adjusted capital accretion for Treasury Indexed Bonds is excluded from these amounts.
(b) This includes foreign currency denominated amounts. Changes in value due to foreign currency translation are shown in the 'Other' column. The foreign currency denominated face value is restated into Australian dollars using end of year exchange rates.

Note 25I: Movement in investments held (face value)

	Opening balance	Purchases	Maturities/ Redemptions	Other	Closing balance
	2014 $'000	**2014 $'000**	**2014 $'000**	**2014 $'000**	**2014 $'000**
Deposits	**20,150,000**	**676,000,000**	**(669,050,000)**	**-**	**27,100,000**
Residential mortgage-backed securities	**9,079,358**	**-**	**(3,062,699)**	**-**	**6,016,659**
Total	**29,229,358**	**676,000,000**	**(672,112,699)**	**-**	**33,116,659**
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000
Deposits	14,500,000	837,000,000	(831,350,000)	-	20,150,000
Residential mortgage-backed securities	11,201,185	160,000	(2,281,827)	-	9,079,358
Total	25,701,185	837,160,000	(833,631,827)	-	29,229,358

Note 26: Market risk sensitivity of administered financial instruments

AASB 7 *Financial Instruments: Disclosures* requires each entity with financial instruments to present a market risk sensitivity analysis for each type of market risk exposure arising from financial instruments held. Market risk represents the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market prices.

The main types of market risk the AOFM's portfolio of debt and financial assets is exposed to are domestic *interest rate risk* and domestic *inflation risk.* Moreover, by generally issuing/buying and holding to maturity, the market risk most relevant to the AOFM's activities is the risk of fluctuations to future interest and principal cash flows arising from changes in interest rates and inflation. The risk of fluctuations in the fair value of the AOFM's net debt portfolio is of a secondary order.

Accordingly, the AOFM has focused its market risk sensitivity analysis on an accruals (or amortised cost) basis of accounting under the historic cost accounting convention, as it provides the best predictive value of future cash flows (and hence costs and returns) arising from the AOFM's portfolio of debt and financial assets.

(a) Interest rate risk sensitivity analysis

Domestic interest rates impact on debt servicing costs when the AOFM enters the primary market to raise new borrowings or refinance maturing debt. When the AOFM borrows to repay maturing debt, there is a risk that debt servicing costs will change due to the interest rate on the new debt being higher or lower than the interest rate on the maturing debt. Furthermore, when the AOFM enters the market to raise new borrowings the interest cost locked-in will be dependent on the absolute level of market interest rates at that time.

Australian dollar denominated residential mortgage-backed securities investments provide for the AOFM to receive interest at a floating interest rate plus a fixed margin set at the time each investment is acquired. When interest rates rise (fall), investment return will also rise (fall).

As the manager of the Government's liquidity, the AOFM holds a fluctuating portfolio of Australian dollar deposits. These investments have fixed interest rates and given their use for cash management purposes they have short terms to maturity (generally no more than a few months). When these investments mature and new investments are made the return may change due to re-investment at higher or lower interest rates.

Note 26: Market risk sensitivity of administered financial instruments (continued)

Under previous Commonwealth-State financing arrangements the Australian Government made concessional Australian dollar loans to the States and the Northern Territory. These loans are of a fixed interest credit foncier nature. Changes in market interest rates do not cause changes in future cash flows of interest or principal.

At 1 July 2014, if domestic interest rates had experienced an immediate 100 basis point parallel upward (downward) movement across the yield curve, and if that change were to persist for the 12 months to 30 June 2015, with all other variables held constant, the effect on the AOFM's operating result before re-measurements (calculated on an accruals basis) and equity position for the year ended 30 June 2015 would be as follows:

Operating result sensitivity to changes in domestic interest rates(a) (calculated on an accruals basis)

		-1%		+1%	
Change in interest rates from 1 July 2014 for 12 months to 30 June 2015	Carrying amount as at 30 Jun 2014 $'000	Impact on profit 2014-15 $'000	Impact on equity 2014-15 $'000	Impact on profit 2014-15 $'000	Impact on equity 2014-15 $'000
Financial assets					
Cash	**622**	**-**	**-**	**-**	**-**
Loans to State and Territory Governments	**2,106,076**	**-**	**-**	**-**	**-**
Deposits	**27,116,335**	**(267,610)**	**(267,610)**	**267,610**	**267,610**
Residential mortgage-backed securities	**6,059,565**	**(50,684)**	**(50,684)**	**50,684**	**50,684**
Financial liabilities					
Treasury Bonds	**313,875,056**	**269,308**	**269,308**	**(230,082)**	**(230,082)**
Treasury Indexed Bonds	**32,418,652**	**-**	**-**	**-**	**-**
Treasury Notes	**4,974,038**	**39,521**	**39,521**	**(39,521)**	**(39,521)**
Other debt	**20,828**	**-**	**-**	**-**	**-**
Total increase (decrease) in accrual result (before re-measurements)		**(9,465)**	**(9,465)**	**48,691**	**48,691**

(a) Changes in nominal interest rates only.

Note 26: Market risk sensitivity of administered financial instruments (continued)

The corresponding figures for the previous 12 months are as follows:

Operating result sensitivity to changes in domestic interest rates(a) (calculated on an accruals basis)

Change in interest rates from 1 July 2013 for 12 months to 30 June 2014	Carrying amount as at 30 Jun 2013 $'000	-1% Impact on profit 2013-14 $'000	-1% Impact on equity 2013-14 $'000	+1% Impact on profit 2013-14 $'000	+1% Impact on equity 2013-14 $'000
Financial assets					
Cash	622	-	-	-	-
Loans to State and Territory Governments	2,177,513	-	-	-	-
Deposits	20,159,143	(200,589)	(200,589)	200,589	200,589
Residential mortgage-backed securities	9,113,022	(78,629)	(78,629)	78,629	78,629
Financial liabilities					
Treasury Bonds	253,157,332	214,172	214,172	(185,293)	(185,293)
Treasury Indexed Bonds	27,092,922	-	-	-	-
Treasury Notes	5,483,361	48,740	48,740	(48,740)	(48,740)
Other debt	21,203	-	-	-	-
Total increase (decrease) in accrual result (before re-measurements)		(16,306)	(16,306)	45,185	45,185

(a) Changes in nominal interest rates only.

(b) Inflation risk sensitivity analysis

The AOFM currently has seven series of Treasury Indexed Bonds on issue. These instruments have their principal value indexed against the (all Groups) Australian Consumer Price Index (CPI). The interest is a fixed real rate of interest payable on the accreted principal value. Accordingly these debt instruments expose the AOFM to cash flow risk on interest payments and on the value of principal payable on maturity or on redemption prior to maturity. There is a six month lag between the calculation period for the CPI and its impact on the value of interest and principal. As the CPI increases, debt servicing costs and the principal payable on maturity also rises.

Note 26: Market risk sensitivity of administered financial instruments (continued)

At 1 July 2014, if the CPI were to experience an immediate 1 per cent increase (decrease) and that change were to persist for 12 months to 30 June 2015, with all other variables held constant, the effect on the AOFM's operating result before re-measurements (calculated on an accruals basis) and equity position for the year ended 30 June 2015 would be as follows:

Operating result sensitivity to changes in the consumer price index (calculated on an accruals basis)

Change in CPI from 1 July 2014 for 12 months to 30 June 2015	Carrying amount as at 30 Jun 2014 $'000	-1% Impact on profit 2014-15 $'000	-1% Impact on equity 2014-15 $'000	+1% Impact on profit 2014-15 $'000	+1% Impact on equity 2014-15 $'000
Financial assets					
Cash	**622**	**-**	**-**	**-**	**-**
Loans to State and Territory Governments	**2,106,076**	-	-	-	-
Deposits	**27,116,335**	**-**	**-**	**-**	**-**
Residential mortgage-backed securities	**6,059,565**	**-**	**-**	**-**	**-**
Financial liabilities					
Treasury Bonds	**313,875,056**	**-**	**-**	**-**	**-**
Treasury Indexed Bonds	**32,418,652**	**314,875**	**314,875**	**(309,272)**	**(309,272)**
Treasury Notes	**4,974,038**	**-**	**-**	**-**	**-**
Other debt	**20,828**	**-**	**-**	**-**	**-**
Total increase (decrease) in accrual result (before re-measurements)		**314,875**	**314,875**	**(309,272)**	**(309,272)**

Note 26: Market risk sensitivity of administered financial instruments (continued)

The corresponding figures for the previous 12 months are as follows:

Operating result sensitivity to changes in the consumer price index (calculated on an accruals basis)

		-1%		+1%	
Change in CPI from 1 July 2013 for 12 months to 30 June 2014	Carrying amount as at 30 Jun 2013 $'000	Impact on profit 2013-14 $'000	Impact on equity 2013-14 $'000	Impact on profit 2013-14 $'000	Impact on equity 2013-14 $'000
Financial assets					
Cash	622	-	-	-	-
Loans to State and Territory Governments	2,177,513	-	-	-	-
Deposits	20,159,143	-	-	-	-
Residential mortgage-backed securities	9,113,022	-	-	-	-
Financial liabilities					
Treasury Bonds	253,157,332	-	-	-	-
Treasury Indexed Bonds	27,092,922	273,606	273,606	(279,657)	(279,657)
Treasury Notes	5,483,361	-	-	-	-
Other debt	21,203	-	-	-	-
Total increase (decrease) in accrual result (before re-measurements)		273,606	273,606	(279,657)	(279,657)

Assumptions and methods used

(a) Interest rate risk sensitivity analysis

Interest rate risk sensitivity has been measured assuming that for the next 12 months domestic interest rates are 100 basis points higher and lower across the entire yield curve than those observed as at year end. The analysis was performed as follows:

- the sensitivity of debt servicing costs for the next 12 months on Treasury Bonds comprised the difference between:
  - debt servicing costs on the planned issuance programme to refinance maturing debt and to raise new borrowings for the next 12 months at the observed or estimated market yield for the relevant line of stock as at year end; and

Note 26: Market risk sensitivity of administered financial instruments (continued)

  - debt servicing costs on the planned issuance programme to refinance maturing debt and to raise new borrowings for the next 12 months at yields that are 100 basis points higher and lower than the observed or estimated market yield for the relevant line of stock as at year end;

- the sensitivity of debt serving costs for the next 12 months on Treasury Notes comprised the difference between:
  - debt servicing costs on Treasury Notes held at the end of the financial year for the full 12 months at the observed or estimated rate as at year end; and
  - debt servicing costs on Treasury Notes held at the end of the financial year for the full 12 months at yields 100 basis points higher and lower than the observed or estimated rate as at year end. The 100 basis point shift is applied from the date the positions held as at year end mature and is held constant at that level thereafter;

- the sensitivity of returns for the next 12 months on residential mortgage-backed securities comprised the difference between:
  - the return at the relevant reference market interest rate at the end of the financial year (being the one-month BBSW rate plus specific fixed margin set for each security at the time of acquisition); and
  - the return at a yield that is 100 basis points higher and lower than the relevant reference market interest rate as at year end plus the fixed margin for each security. The 100 basis point shift is applied from the date of the first rate re-set after the end of the financial year and is held constant at that level thereafter;

- the sensitivity of returns for the next 12 months on term deposits comprised the difference between:
  - the return on term deposits held at the end of the financial year for the full 12 months at the relevant reference market interest rate (being the relevant Overnight Indexed Swap (OIS) rate) as at year end; and
  - the return on term deposits held at the end of the financial year for the full 12 months at a yield that is 100 basis points higher and lower than the relevant OIS rate as at year end. The 100 basis point shift is applied from the date of the first re-investment after the end of the financial year and is held constant at that level thereafter.

Note 26: Market risk sensitivity of administered financial instruments (continued)

(b) Inflation risk sensitivity analysis

Inflation risk sensitivity has been measured assuming that for each quarter in the next financial year the CPI is 1 per cent higher and lower (when compared to the year before) than in the base case. The analysis was performed as follows:

- the sensitivity of debt servicing costs for the next financial year on Treasury Indexed Bonds comprised the difference between:
  - debt servicing costs for the next financial year on the basis that inflation persists at the average rate experienced in the financial year (base case); and
  - debt servicing costs for the next financial year on the basis that the CPI index is higher and lower by 1 per cent than the assumed base case level for each quarter.

(c) Other assumptions and methods used

For the purposes of calculating sensitivity analysis, it has been assumed that the AOFM will issue $63,500 million of Treasury Bonds and $3,500 million of Treasury Indexed Bonds during the 2014-15 financial year (2013-14 assumptions: $50,000 million and $4,000 million respectively). It is also assumed that the volume of Treasury Notes outstanding as at 30 June 2014 of $5,000 million will remain at these levels for the full 12 months to 30 June 2015 (2013-14 assumption: $5,500 million). It is assumed that the volume of term deposit investments will remain at levels as at 30 June 2014 of $27,100 million for the full 12 months to 30 June 2015 (2013-14 assumption: $20,150 million). Residential mortgage-backed securities will have a principal repayment rate based on an estimated cash flow waterfall for each issue acquired. During 2014-15 the AOFM will make no further investments in RMBS consistent with the Treasurer's direction (2013-14 assumption: nil) and no sales are assumed (2013-14 assumption: nil). Interest earned on investments is assumed to be returned to the OPA when received and not re-invested.

The sensitivity analysis does not consider possible adjustments that the AOFM might make to the composition of its portfolio in response to the assumed interest rate changes.

(d) Fair value sensitivity

The fair value sensitivity of the net debt portfolio (excluding loans to State and Territory Governments, which are measured on an accruals basis) to changes in domestic interest rates as at 30 June 2014 was $180.3 million per basis point (30 June 2013: $135.8 million per basis point). This means that a 1 basis point (or

0.01 per cent) parallel increase (decrease) in interest rates across the yield curve would result in a favourable (unfavourable) change in fair value of $180.3 million.

Note 27: Securities lending facility

The AOFM has a securities lending facility for Treasury Bonds and Treasury Indexed Bonds, operated by the RBA. The purpose of the facility is to enhance the efficiency of the bond market by allowing bond market participants to borrow Treasury Bonds and Treasury Indexed Bonds when they are not readily available in the market. Bonds are lent on an intra-day or overnight basis. Where bonds are lent overnight the AOFM receives interest income. The following table details the security lending transactions completed during the year:

	Number of transactions	Number of transactions	**Face value loaned**	Face value loaned
	2014 No.	2013 No.	**2014 $'000**	2013 $'000
Treasury Bonds:				
December 2013	**-**	3	**-**	81,005
June 2014	**-**	1	**-**	9,500
October 2014	**1**	1	**70,000**	11,500
April 2015	**6**	6	**426,800**	131,200
June 2016	**-**	-	**-**	-
February 2017	**-**	-	**-**	-
July 2017	**-**	-	**-**	-
January 2018	**1**	-	**75,000**	-
March 2019	**4**	-	**266,200**	-
April 2020	**8**	-	**178,000**	-
May 2021	**13**	-	**511,700**	-
July 2022	**-**	1	**-**	30,000
April 2023	**2**	-	**80,000**	-
April 2024	**3**	-	**277,000**	-
April 2025	**1**	-	**180,000**	-
April 2027	**1**	-	**46,000**	-
Treasury Indexed Bonds:				
August 2015	**1**	-	**30,000**	-
August 2020	**-**	1	**-**	40,000
February 2022	**-**	5	**-**	81,700
September 2025	**-**	-	**-**	-
September 2030	**-**	2	**-**	90,000
Securities lent	**41**	20	**2,140,700**	474,905
Lending comprised:				
Overnight:				
Treasury Bonds	**17**	10	**502,900**	183,205
Treasury Indexed Bonds	**1**	4	**30,000**	41,700
Intra-day:				
Treasury Bonds	**23**	2	**1,607,800**	80,000
Treasury Indexed Bonds	**-**	4	**-**	170,000
Securities lent	**41**	20	**2,140,700**	474,905

Note 27: Securities lending facility (continued)

	2014 $'000	2013 $'000
Income on overnight lending(a):		
Treasury Bonds	**58**	16
Treasury Indexed Bonds	**3**	4
Total income on overnight lending:	**61**	20

(a) Income on loan transactions is recognised when received and is reported at Note 17B.

In 2013-14 no security lending transactions were open at the start of the financial year (2012-13: nil). In 2013-14 no security lending transactions were outstanding at the end of the financial year (2012-13: nil).

Note 28: Disclosures of appropriations

Note 28A: Annual appropriations

Outcome 1 — The advancement of macroeconomic growth and stability, and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government

Annual appropriations

	Appropriation Act		FMA Act				
	Annual appropriation	Appropriation reduced (c)	Section 30	Section 31 (GST ex)	Total appropriation	Appropriation applied	Variance(d)
	2014 $'000	2014 $'000	2014 $'000	2014 $'000	2014 $'000	2014 $'000	2014 $'000
Departmental							
Ordinary annual services(a)(b)	**11,893**	**(6)**	**15**	**634**	**12,536**	**(12,138)**	**398**
Total departmental	**11,893**	**(6)**	**15**	**634**	**12,536**	**(12,138)**	**398**
Administered							
Ordinary annual services							
Outcome 1	**10**	**(10)**	**-**	**-**	**-**	**-**	**-**
Total administered	**10**	**(10)**	**-**	**-**	**-**	**-**	**-**

(a) Amounts presented in this table exclude GST where the GST is recoverable from the ATO.

(b) Amounts under Ordinary annual services include capital budget appropriations of $0.408 million which are recognised directly in Contributed Equity in the Statement of Financial Position.

(c) Reductions are presented in Note 28C. This administered reduction is legally affected under *Appropriation Act (No. 1) 2013-14* when the AOFM's annual report is tabled in Parliament.

(d) The variance is explained by lower than anticipated costs of undertaking additional issuance activity.

Note 28: Disclosures of appropriations (continued)

Note 28A: Annual appropriations (continued)

Outcome 1 — The advancement of macroeconomic growth and stability, and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government

Annual appropriations (continued)

	Appropriation Act		FMA Act				
	Annual appropriation	Appropriation reduced(d)	Section 30	Section 31 (GST ex)	Total appropriation	Appropriation applied	Variance(e)
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000
Departmental							
Ordinary annual services(a)(b)(c)	11,867	-	-	584	12,451	(9,475)	2,976
Total departmental	11,867	-	-	584	12,451	(9,475)	2,976
Administered							
Ordinary annual services							
Outcome 1	10	(10)	-	-	-	-	-
Total administered	10	(10)	-	-	-	-	-

(a) Amounts presented in this table exclude GST where the GST is recoverable from the ATO.

(b) Amounts under Ordinary annual services include capital budget appropriations of $0.406 million which are recognised directly in Contributed Equity in the Statement of Financial Position.

(c) The 2012-13 Mid-Year Economic and Fiscal Outlook (MYEFO) announced targeted savings for the 2012-13 year of which the AOFM's share was $52,000. The Finance Minister made a determination to reduce the appropriation by $52,000 on 5 August 2013. As the reduction in the appropriation was not reflected at law on 30 June 2013, this figure does not include the $52,000 reduction and is consistent with the 2012-13 Budget. However, as the reduction was announced by the Government before 30 June 2013, the appropriation revenue recognised in the Statement of Comprehensive Income, the unspent appropriation disclosed at Note 28B and appropriation receivable disclosed at Note 6 reflect the reduction.

(d) Reductions are presented in Note 28C. This administered reduction is legally affected under *Appropriation Act (No. 1) 2012-13* when the AOFM's 2012-13 annual report is tabled in Parliament.

(e) The variance is explained by lower than anticipated costs of undertaking additional issuance activity.

Note 28: Disclosures of appropriations (continued)

Note 28A: Annual appropriations (continued)

Outcome 1 — The advancement of macroeconomic growth and stability, and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government

Departmental Capital Budget(a)

	Appropriation Act			Appropriation applied		
	Annual capital budget	Appropriation reduced(c)	Total capital budget	Non-financial assets(b)	Other purposes	Variance
	2014 $'000	**2014 $'000**	**2014 $'000**	**2014 $'000**	**2014 $'000**	**2014 $'000**
Departmental						
Ordinary annual services - departmental capital budget	**408**	**-**	**408**	**(1,167)**	**-**	**(759)**
Total departmental	**408**	**-**	**408**	**(1,167)**	**-**	**(759)**
	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000	2013 $'000
Departmental						
Ordinary annual services - departmental capital budget	406	-	406	(294)	-	112
Total departmental	406	-	406	(294)	-	112

(a) The AOFM does not receive administered capital budget funding.
(b) Amounts presented in this table exclude GST where the GST is recoverable from the ATO.
(c) Reductions are presented in Note 28C.

Note 28: Disclosures of appropriations (continued)

Note 28B: Unspent annual appropriation

Outcome 1 — The advancement of macroeconomic growth and stability, and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government

	2014 $'000	2013 $'000
Unspent departmental annual appropriation(a)		
Appropriation Act 2 2000-01 (a)	**-**	162
Appropriation Act 1 2006-07	**-**	-
Appropriation Act 3 2006-07	**-**	-
Appropriation Act 1 2007-08	**-**	-
Appropriation Act 1 2008-09	**-**	-
Appropriation Act 1 2009-10 (a)	**-**	3,285
Appropriation Act 1 2010-11 (b)	**-**	5,636
Appropriation Act 1 2011-12 (b)	**653**	7,433
Appropriation Act 1 2012-13	**12,399**	12,106
Appropriation Act 1 2013-14	**12,521**	-
Total	**25,573**	28,622
Represented by:		
Cash at bank	**100**	100
Appropriation receivable - output	**23,183**	25,311
Appropriation receivable - equity injection	**-**	162
Appropriation receivable - departmental capital budget	**2,290**	3,049
Total	**25,573**	28,622

(a) On 1 July 2013 the *Statute Stocktake (Appropriations) Act 2013* commenced. This Act repeals all annual Appropriation Acts from 1 July 1999 through to 30 June 2010. On this day the AOFM returned $3,447,050 in unspent departmental appropriations to the Budget.

(b) From 1 July 2014 these appropriations were no longer available for use. Further details are provided at Note 32.

	2014 $'000	2013 $'000
Unspent administered annual appropriation		
Appropriation Act 1 2012-13	**-**	10
Appropriation Act 1 2013-14	**10**	-
Total	**10**	10

Note 28: Disclosures of appropriations (continued)

Note 28C: Reduction in administered items

The AOFM receives an annual administered appropriation of $10,000 to meet potential payments that may arise on certain overdues that matured some time ago and an alternative appropriation source does not exist. The unspent and uncommitted funds arising from this appropriation are returned to the Budget on an annual basis.

For 2013-14 the AOFM received an appropriation authority of $10,000 in *Appropriation Act (No. 1) 2013-14* for this purpose. Section 11 of *Appropriation Act (No. 1) 2013-14* creates an automatic reduction to the appropriation on tabling of the AOFM's annual report in Parliament where it identifies that an administered appropriation is no longer required, either in full or part.

The following table specifies the reduction in the annual administered appropriation for the AOFM. It reduces the AOFM's annual administered appropriation of $10,000 appropriated in *Appropriation Act (No. 1) 2013-14* to nil.

Outcome 1 — The advancement of macroeconomic growth and stability, and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government

	2014 **$0.00**
Reduction in administered items	
Total administered items appropriated 2013-14	**10,000.00**
Less administered items required by the agency as per Appropriation Act, section 11:	
Appropriation Act (No. 1) 2013-2014	**0.00**
Total administered items required by the agency	**0.00**
Total reduction in administered items - effective 2014-15	**10,000.00**

Note 28: Disclosures of appropriations (continued)

Note 28D: Administered special appropriations (unlimited amount)

The following table details administered special appropriations applied by the AOFM:

	2014 $'000	2013 $'000
Australian National Railways Commission Sale Act 1997, section 67AW		
Purpose: payment of principal and interest on former debts of the National Railways Commission	**-**	-
Commonwealth Inscribed Stock Act 1911, section 13AA		
Purpose: payment of principal and interest on money raised by Stock issued under the Act and principal and interest due to holders of depository interests in Stock issued under the Act	**55,593,579**	98,731,954
Commonwealth Inscribed Stock Act 1911, section 13A		
Purpose: payment of costs and expenses incurred in relation to issuing and managing debt and issuing and managing depository interests	**25,750**	12,805
Commonwealth Inscribed Stock Act 1911, section 13B		
Purpose: payment of costs and expenses incurred in repurchasing debt prior to maturity	**5,112,705**	-
Financial Agreement Act 1994, section 5		
Purpose: debt redemption assistance and payment of interest to bond holders on behalf of the States and Northern Territory on public debt under the Act	**278**	283
Financial Management and Accountability Act 1997, section 28		
Purpose: refunds of monies received by the Australian Government	**1,899**	-
Financial Management and Accountability Act 1997, section 30A		
Purpose: payments of recoverable GST	**-**	-
Financial Management and Accountability Act 1997, section 39(9)		
Purpose: to make investments in the name of the Commonwealth of Australia	**676,000,000**	837,160,000

Note 28: Disclosures of appropriations (continued)

Note 28D: Administered special appropriations (unlimited amount) (continued)

	2014 $'000	2013 $'000
Loans Redemption and Conversion Act 1921, section 5		
Purpose: payment of principal, interest and costs of converting loans made in accordance with the Act	**-**	-
Loans Securities Act 1919, section 4		
Purpose: payment of principal and interest on money raised by stock issued under the Act	**488**	432
Loans Securities Act 1919, section 5B		
Purpose: payment of money under a swap or repurchase agreement and any expenditure in connection with the negotiation, management or service of, or a repayment under, any such agreement	**-**	-
Loans Securities Act 1919, section 5BA		
Purpose: payment of money to enter into securities lending arrangements	**-**	-
Moomba-Sydney Pipeline System Sale Act 1994, section 19		
Purpose: payment of principal and interest on former debts of the Pipeline Authority	**-**	-
Snowy Hydro Corporatisation Act 1997, section 22		
Purpose: payment of principal and interest on former debts of the Snowy Mountains Hydro Electricity Authority	**-**	-
Treasury Bills Act 1914, section 6		
Purpose: payment of principal and interest on money raised by issuance of Treasury Bills	**-**	-
Total	**736,734,699**	935,905,474

Note 28: Disclosures of appropriations (continued)

Note 28E: Special appropriations (refund provisions)

Section 28 of the *Financial Management and Accountability Act 1997* provides for repayments of monies received by the Australian Government where no other appropriation exists to refund the monies received. In 2013-14 the AOFM used $1,898,608 of this appropriation (2012-13: $nil) to refund counterparties for overpayment of monies relating to RMBS securities and other payments made in error to the AOFM.

Note 28F: Special appropriations (FMA section 39)

Investment of public money:	**2014 $'000**	2013 $'000
Special appropriations under section 39 of the FMA Act in face value terms		
Amount invested brought forward from previous period	**29,229,358**	25,701,185
Investments made during the year	**676,000,000**	837,160,000
Investments redeemed during the year	**(672,112,699)**	(833,631,827)
Amount invested carried to the next period (at face value)(a)(b)	**33,116,659**	29,229,358

FMA = *Financial Management and Accountability Act 1997*.
(a) See Note 25I for details of investments held and Note 17 for details of investment income.
(b) See Note 2 and Note 3 for details on the framework under which investments are made.

Note 28: Disclosures of appropriations (continued)

Note 28G: Special accounts (Administered)

Debt Retirement Reserve Trust Account (DRRTA)

Establishing Instrument — *Financial Management and Accountability Act 1997*, section 21.

Purpose —to fund the redemption of the State and Territory debt governed by the *Financial Agreement Act 1994*. Monies standing to the credit of the DRRTA are applied to repurchase debt of the States and the Northern Territory.

	2014 **$'000**	2013 $'000
Balance brought forward from previous period	**742**	657
Appropriation for reporting period	**20**	21
Interest amounts credited	**19**	21
Other receipts:		
State and Territory contributions	**62**	62
Available for payments	**843**	761
Total increase	**101**	104
Payments made:		
Debt repayments	**-**	(19)
Total decrease	**-**	(19)
Balance	**843**	742
Balance represented by:		
Cash - held in the Official Public Account	**843**	742
Total balance carried to the next period	**843**	742

Note 28H: Assets held in trust (Administered)

Monies standing to the credit of the Debt Retirement Reserve Trust Account are held on behalf of the States and Northern Territory. These monies are held for the purposes prescribed by the *Financial Agreement Act 1994*.

Details of balances, payments and receipts in relation to the Debt Retirement Reserve Trust Account are provided in Note 28G: Special accounts (Administered).

Note 29: Reporting of outcomes

The AOFM delivers a single outcome — the advancement of macroeconomic growth and stability, and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government.

	Outcome 1	Outcome 1
	2014	2013
	$'000	$'000
Expenses		
Administered	**13,413,814**	12,237,309
Departmental	**10,758**	9,776
Total expenses	**13,424,572**	12,247,085
Own-source income		
Administered		
Interest	**1,044,272**	1,121,487
Other	**349**	40
Gains (losses)	**(3,852,492)**	11,388,881
Total administered	**(2,807,871)**	12,510,408
Departmental		
Other(a)	**564**	596
Total departmental	**564**	596
Total own-source income	**(2,807,307)**	12,511,004
Net cost/(contribution) of outcome	**16,231,879**	(263,919)

(a) Excludes resources received free of charge from the ANAO.

Note 30: Net cash appropriation arrangements (Departmental)

The following table reports the amount of depreciation and amortisation expenses for which the AOFM no longer receives revenue appropriations.

	2014	2013
	$'000	$'000
Total comprehensive income excluding expenses previously funded through revenue appropriations(a)	**1,982**	2,912
Less: depreciation/amortisation expenses previously funded through revenue appropriation	**(377)**	(380)
Total comprehensive income as per the Statement of Comprehensive Income	**1,605**	2,532

(a) From 2010-11, the Government introduced net cash appropriation arrangements, where appropriations for depreciation/amortisation expenses ceased. The AOFM now receives a separate capital budget appropriation.

Note 31: Compliance with statutory conditions for payments from the consolidated revenue fund

Section 83 of the Constitution provides that no amount may be paid out of the Consolidated Revenue Fund except under an appropriation made by law. The Department of Finance provided information to all agencies in 2011 regarding the need to conduct risk assessments in relation to compliance with the statutory conditions on payments from special appropriations, including special accounts. Non-compliance with statutory conditions on payments may constitute a breach of section 83 of the Constitution.

On 2 July 2013 the AOFM received further advice from the Department of Finance in relation to possible breaches of section 83 of the Constitution for what it called certain 'generic' payments. These are payments made by agencies pursuant to the *Remuneration Tribunal Act 1973*, the *Long Service Leave (Commonwealth Employees) Act 1976* and section 30A of the *Financial Management and Accountability Act 1997*.

The AOFM undertook a risk assessment for the 2013-14 financial year. No breaches of Section 83 were identified and the overall risk of a breach was considered low.

The Australian Government continues to have regard to developments in case law, including the High Court's most recent decision on Commonwealth expenditure in *Williams v Commonwealth [2014] HCA 23*, as they contribute to the larger body of law relevant to the development of Commonwealth programmes. In accordance with its general practice, the Government will continue to monitor and assess risk and decide on any appropriate actions to respond to risks of expenditure not being consistent with constitutional or other legal requirements.

Note 32: Events occurring after reporting date

On 1 July 2014 the substantive provisions of the *Public Governance, Performance and Accountability Act 2013* (the PGPA Act) commenced. On this day the PGPA Act replaced the *Financial Management and Accountability Act 1997* (the FMA Act) as the law governing the financial management of Commonwealth agencies. To support transition to the PGPA Act, on 1 July 2014 the *PGPA (Consequential and Transitional Provisions) Act 2014* also commenced. It establishes certain transitional or saving arrangements, including that the FMA Act continues to apply to 2013-14 annual financial statements and their audit by the Auditor-General.

In addition, on 1 July 2014 the *Public Governance, Performance and Accountability (Consequential Modification of Appropriations Acts) Acts 2014* commenced. To support the transition to the PGPA Act, the Acts contain consequential amendments to the 2012-13, 2013-14 and 2014-15 Appropriation Acts to replace references to or reliance on provisions in the FMA Act with equivalent provisions in the PGPA Act. Accordingly, only those Appropriation Acts commencing after 30 June 2012 are available for use by agencies from 1 July 2014. Appropriation Acts commencing prior to 1 July 2012 are not available to agencies and legislation is currently in Parliament to repeal these Acts.

There have been no significant events occurring after the reporting date that materially affect these financial statements.

AOFM

PART 5
OTHER INFORMATION

OTHER INFORMATION

Funding

Table 1 places the AOFM's asset and liability management activities in 2013-14 in the context of budget financing for the Australian Government and in particular as it covers the General Government Sector. Flows managed by the AOFM are shown in purple.

Table 1: General Government Sector funding requirement and funding sources

Source of funds	Actual 2013-14 ($billion)	Use of funds	Actual 2013-14 ($billion)
		Headline budget balance	**52.5**
Debt issuance[a]		**Debt redemption[a]**	
Treasury Bonds	82.1	Maturing Treasury Bonds	22.6
Treasury Indexed Bonds	7.5	Early CGS debt repurchases	3.7
Total	**89.6**	Treasury Notes (net)	0.6
		Total	**27.0**
		Financial assets	
		Change in deposits at RBA	7.0
		Change in other general government sector investments	0.8
		Total	**7.7**
		Other applications of funds	
		Other financing (net) [b]	2.4
		Total	**2.4**
Total	**89.6**	**Total**	**89.6**

(a) Cash flows rather than face value of securities.
(b) Includes other general government sector flows not elsewhere classified.
Not all totals may sum exactly due to rounding.

Agency resource statement and resources for outcomes

Table 2: AOFM resource statement

		Actual available appropriation 2013-14 $'000	Payments made 2013-14 $'000	=	Balance 2013-14 $'000
Ordinary annual services					
Departmental appropriation(a)(b)		40,347	14,774	(c)	25,573
Receipts from other sources (s30 & s31)(d)		649	649		-
Total departmental		40,996	15,423		25,573
Administered expenses					
Outcome 1		10	-		10
Total administered		10	-		10
Total ordinary annual services	**A**	41,006	15,423		25,583
Other services					
Departmental non-operating		162	162	(c)	-
Total other services	**B**	162	162		-
Total available annual appropriations (A+B)		41,168	15,585		25,583
Special appropriations non-capital					
Commonwealth Inscribed Stock Act 1911		15,889,716	15,889,716		-
Financial Agreement Act 1994		278	278		-
Financial Management and Accountability Act 1997		1,899	1,899		
Loans Securities Act 1919		489	489		-
Subtotal		15,892,382	15,892,382	-	-
Special appropriations capital					
Commonwealth Inscribed Stock Act 1911		44,842,317	44,842,317		-
Financial Management and Accountability Act 1997		676,000,000	676,000,000		-
Subtotal		720,842,317	720,842,317	-	-
Total special appropriations	**C**	736,734,699	736,734,699	-	-
Total appropriations excluding special accounts (A + B + C)		736,775,867	736,750,284		25,583
Special Accounts					
Debt Retirement Reserve Trust Account					
Opening balance		742	-		-
Appropriation receipts		20	-		-
Non-appropriation receipts to special account					-
Interest amount credited		19	-		-
State and Territory contributions		62	-		-
Payments made		-	-		-
Total Special Account	**D**	843	-	-	843
Total net resourcing and payments for AOFM (A + B + C + D)		736,776,710	736,750,284		26,426

(a) Actual available appropriation comprises *Appropriation Bill (No.1) 2013-14* plus carried forward appropriation balances as at 1 July 2013.
(b) Includes capital budget appropriation for 2013-14 of $0.408 million.
(c) Payments made include appropriations returned to Budget on 1 July 2013 of $3.447 million.
(d) Receipts received under sections 30 and 31 of the *Financial Management and Accountability Act 1997*.

Table 3: Expenses and resources for Outcome 1

Outcome 1: The advancement of macroeconomic growth and stability and the effective operation of financial markets, through issuing debt, investing in financial assets and managing debt, investments and cash for the Australian Government	**Budget(a) 2013-14 $'000**	**Actual Expenses 2013-14 $'000**	**Variation $'000**
Programme 1.1: Australian Office of Financial Management			
Departmental expenses			
Departmental appropriation	10,807	10,055	752
Expenses not requiring appropriation in the Budget year	803	703	100
Administered expenses before re-measurements			
Ordinary annual services (Appropriation Bill No.1)	10	-	10
Expenses not requiring appropriation	188,571	194,329	(5,758)
Special appropriations expenses			
Commonwealth Inscribed Stock Act 1911	13,452,771	13,413,053	39,718
Loans Securities Act 1919	864	483	381
Financial Agreement Act 1994	20	278	(258)
Total for Programme 1.1	13,653,846	13,618,901	34,945
	2013-14	**2013-14**	
Average staffing level (number)	**42**	**42**	**-**

(a) The Budget figure for 2013-14 is the estimated actual 2013-14 expenses, reported in Table 2.1 of the Portfolio Budget Statements 2014-15.

Grant programmes

Under the *Financial Agreement Act 1994*, the Commonwealth is required to contribute to the Debt Retirement Reserve Trust Account to assist the State and Northern Territory Governments to redeem maturing debt on allocation to them. Monies standing to the credit of this Account are held for the purposes prescribed by the *Financial Agreement Act 1994*.

The contributions made by the Commonwealth are accounted for as grants in the AOFM's financial statements.

Advertising and market research

During 2013-14, the AOFM made no payments to market research organisations, polling organisations or direct mail organisations.

The AOFM incurred expenditure of $5,991 in campaign advertising to promote Australian Government debt to investors. This was paid to Universal McCann (a division of Mediabrands Pty Ltd) for the placement of advertisements.

The AOFM incurred nil expenditure during 2013-14 to media advertising organisations for staff recruitment.

Freedom of information

Agencies subject to the *Freedom of Information Act 1982* (FOI Act) are required to publish information to the public as part of the Information Publication Scheme (IPS). This requirement is in Part II of the FOI Act and has replaced the former requirement to publish a section 8 statement in an annual report. Freedom of Information (FOI) matters in respect of the AOFM are handled by the Treasury and all documents disclosed in response to FOI requests (other than personal or business information that would be unreasonable to publish) are published on the FOI Disclosure Log of the Treasury website. The Treasury reports on AOFM's FOI requests in an annual submission to the Office of the Australian Information Commissioner (OAIC) for inclusion in the OAIC's annual report. In 2013-14, the AOFM received one FOI request.

An agency plan showing what information is published in accordance with the IPS requirements, including material relevant to the AOFM, is accessible from the Treasury's website at www.treasury.gov.au.

Ecologically sustainable development

The AOFM's operations have an impact on the environment typical of office operations generally. Procurement and facilities management services are provided to the AOFM by the Treasury under a Service Level Agreement. Information on the environmental impact of these services is published in the Treasury's Annual Report.

Structure of the AOFM's portfolio

The assets and liabilities managed by the AOFM and held on its administered balance sheet in 2013-14 were Commonwealth Government Securities (Treasury Bonds, Treasury Indexed Bonds, Treasury Notes and other securities), term deposits placed with the Reserve Bank of Australia, residential mortgage-backed securities (RMBS) and housing advances to the States under the various Commonwealth-State Housing Agreements.

For financial and risk management purposes, these assets and liabilities are allocated between four portfolios: the Long-Term Debt Portfolio, the Cash Management Portfolio, the RMBS Portfolio and the Housing Advances Portfolio. This allocation recognises the different objectives, risks and management approaches required in each area.

The **Long-Term Debt Portfolio** contains debt denominated in Australian dollars and in foreign currencies. It includes all Commonwealth Government Securities, other than Treasury Notes, which are issued for cash management purposes.

As no borrowings have been undertaken in foreign currencies since 1987, the Long-Term Debt Portfolio holds only a small residual amount of foreign currency debt.

The **Cash Management Portfolio** is used to manage within-year variability in the Australian Government's financing requirement due to differences in the timing of Government payments and receipts. It contains all the assets and liabilities not held in the other three portfolios.

The **RMBS Portfolio** contains residential mortgage-backed securities purchased by the AOFM.

The **Housing Advances Portfolio** comprises loans for public housing made by the Commonwealth to the States and Territories. These loans, which were not evidenced by the issue of securities, were made under previous Commonwealth-State financing arrangements. The last of these loans is due to mature on 30 June 2042.

Residential mortgage-backed securities portfolio

The AOFM's investments in residential mortgage-backed securities up to 30 June 2014 are shown in Table 4.

Table 4: AOFM's RMBS investments up to 30 June 2014

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
14-Nov-08	21-Nov-08	FirstMac	FirstMac Mortgage Funding Trust Series 2-2008	Class A1	0.7	1M BBSW + 1.25%	132.00
14-Nov-08	21-Nov-08	FirstMac	FirstMac Mortgage Funding Trust Series 2-2008	Class A2	3.5	1M BBSW + 1.50%	325.00
14-Nov-08	21-Nov-08	FirstMac	FirstMac Mortgage Funding Trust Series 2-2008	Class AB	5.0	1M BBSW + 1.80%	39.00
17-Nov-08	09-Dec-08	Members' Equity Bank	SMHL Securitisation Fund 2008-2	Class A1	2.8	1M BBSW + 1.30%	500.00
04-Dec-08	12-Dec-08	Challenger	Challenger Millennium Series 2008-2 Trust	Class A	2.8	1M BBSW + 1.35%	481.00
04-Dec-08	12-Dec-08	Challenger	Challenger Millennium Series 2008-2 Trust	Class AB	4.5	1M BBSW + 1.75%	19.00
10-Dec-08	15-Dec-08	RESIMAC	RESIMAC Premier Series 2008-1	Class A2	1.5	1M BBSW + 1.20%	280.00
10-Dec-08	15-Dec-08	RESIMAC	RESIMAC Premier Series 2008-1	Class A3	4.5	1M BBSW + 1.40%	204.75
10-Dec-08	15-Dec-08	RESIMAC	RESIMAC Premier Series 2008-1	Class AB	4.5	1M BBSW + 1.70%	15.25
06-Mar-09	26-Mar-09	CUA	Series 2009-1 Harvey Trust	Class A1	3.6	1M BBSW + 1.40%	350.00
13-Mar-09	18-Mar-09	Bendigo and Adelaide Bank	TORRENS Series 2009-1 Trust	Class A2	4.2	1M BBSW + 1.35%	475.00
23-Mar-09	30-Mar-09	AMP Bank	Progress 2009-1 Trust	Class A2	4.0	1M BBSW + 1.30%	425.00
03-Apr-09	21-Apr-09	Bank of Queensland	Series 2009-1 REDS Trust	Class A1	4.2	1M BBSW + 1.30%	500.00
09-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class A1	0.1	1M BBSW + 0.90%	14.50
09-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class A2	0.9	1M BBSW + 1.20%	164.70
09-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class A3	3.2	1M BBSW + 1.40%	283.00
09-Apr-09	20-Apr-09	Liberty Financial	Liberty Prime Series 2009-1	Class AB	4.0	1M BBSW + 1.65%	37.80
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class A2	0.5	1M BBSW + 1.00%	38.20
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class A3	1.5	1M BBSW + 1.30%	152.50
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class A4	4.3	1M BBSW + 1.45%	289.00
15-Apr-09	24-Apr-09	Challenger	Challenger Millennium Series 2009-1 Trust	Class AB	4.4	1M BBSW + 1.70%	20.30
11-May-09	14-May-09	Members' Equity Bank	SMHL Securitisation Fund 2009-1	Class A2	3.7	1M BBSW + 1.35%	500.00
21-May-09	28-May-09	RESIMAC	RESIMAC Premier Series 2009-1	Class A2	0.5	1M BBSW + 1.00%	10.00
21-May-09	28-May-09	RESIMAC	RESIMAC Premier Series 2009-1	Class A3	2.9	1M BBSW + 1.40%	435.00
21-May-09	28-May-09	RESIMAC	RESIMAC Premier Series 2009-1	Class AB	4.1	1M BBSW + 1.70%	13.80
01-Jun-09	05-Jun-09	FirstMac	FirstMac Mortgage Funding Trust Series 1-2009	Class A3	2.9	1M BBSW + 1.40%	458.00
01-Jun-09	05-Jun-09	FirstMac	FirstMac Mortgage Funding Trust Series 1-2009	Class AB	5.0	1M BBSW + 2.20%	40.62
09-Jul-09	16-Jul-09	Wide Bay Australia	WB Trust 2009-1	Class A1	0.5	1M BBSW + 1.10%	16.00
09-Jul-09	16-Jul-09	Wide Bay Australia	WB Trust 2009-1	Class A2	3.5	1M BBSW + 1.40%	282.50
09-Jul-09	16-Jul-09	Wide Bay Australia	WB Trust 2009-1	Class AB	5.4	1M BBSW + 1.60%	1.00
14-Jul-09	28-Jul-09	Australian Central Credit Union	Light Trust No. 2	Class A1	4.0	1M BBSW + 1.30%	190.00
20-Aug-09	04-Sep-09	Suncorp Metway	APOLLO Series 2009-1 Trust	Class A3	3.6	1M BBSW + 1.30%	499.20
28-Aug-09	11-Sep-09	Greater Building Society	GBS Receivables Trust No. 4	Class A1	4.3	1M BBSW + 1.35%	190.00

Table 4: AOFM's RMBS investments up to 30 June 2014 (continued)

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
14-Oct-09	21-Oct-09	Liberty Financial	Liberty Prime Series 2009-2	Class A2	1.0	1M BBSW + 0.90%	35.00
14-Oct-09	21-Oct-09	Liberty Financial	Liberty Prime Series 2009-2	Class A3	3.3	1M BBSW + 1.40%	58.50
14-Oct-09	21-Oct-09	Liberty Financial	Liberty Prime Series 2009-2	Class AB	4.0	1M BBSW + 1.65%	6.30
21-Oct-09	28-Oct-09	RESIMAC	RESIMAC Premier Series 2009-2	Class A2	3.3	1M BBSW + 1.40%	38.10
21-Oct-09	28-Oct-09	RESIMAC	RESIMAC Premier Series 2009-2	Class AB	3.5	1M BBSW + 1.95%	18.30
10-Nov-09	24-Nov-09	FirstMac	FirstMac Mortgage Funding Trust Series 2-2009	Class A2	3.5	1M BBSW + 1.40%	195.40
10-Nov-09	24-Nov-09	FirstMac	FirstMac Mortgage Funding Trust Series 2-2009	Class AB	5.0	1M BBSW + 1.95%	19.74
22-Jan-10	29-Jan-10	AMP Bank	Progress 2010-1 Trust	Class AB	5.2	1M BBSW + 1.80%	36.00
09-Feb-10	17-Feb-10	Bank of Queensland	Series 2010-1 REDS Trust	Class A	3.1	1M BBSW + 1.30%	250.00
25-Feb-10	10-Mar-10	CUA	Series 2010-1 Harvey Trust	Class A1	2.9	1M BBSW + 1.35%	143.00
05-Mar-10	15-Mar-10	Members' Equity Bank	SMHL Securitisation Fund 2010-1	Class A	2.6	1M BBSW + 1.35%	250.00
17-Mar-10	24-Mar-10	Bendigo and Adelaide Bank	TORRENS Series 2010-1 Trust	Class A	2.8	1M BBSW + 1.35%	123.00
26-Mar-10	31-Mar-10	IMB	Illawarra Series 2010-1 RMBS Trust	Class A	3.0	1M BBSW + 1.35%	157.50
12-May-10	17-May-10	RESIMAC	RESIMAC Premier Series 2010-1	Class A	2.4	1M BBSW + 1.65%	10.00
28-May-10	09-Jun-10	Suncorp Metway	APOLLO Series 2010-1 Trust	Class A2	6.0	1M BBSW + 1.10%	300.00
02-Jul-10	14-Jul-10	Members' Equity Bank	SMHL Securitisation Fund 2010-2E	Class A3	5.7	1M BBSW + 1.10%	250.00
08-Jul-10	20-Jul-10	Bendigo and Adelaide Bank	TORRENS Series 2010-2 Trust	Class A3	3.0	1M BBSW + 1.10%	19.50
08-Jul-10	20-Jul-10	Bendigo and Adelaide Bank	TORRENS Series 2010-2 Trust	Class A4	5.8	1M BBSW + 1.10%	476.50
23-Jul-10	04-Aug-10	MyState Financial	ConQuest 2010-2 Trust	Class A2	1.5	1M BBSW + 1.40%	20.00
23-Jul-10	04-Aug-10	MyState Financial	ConQuest 2010-2 Trust	Class A3	5.0	1M BBSW + 1.30%	139.25
23-Jul-10	04-Aug-10	MyState Financial	ConQuest 2010-2 Trust	Class AB	3.7	1M BBSW + 1.85%	10.75
11-Aug-10	18-Aug-10	Liberty Financial	Liberty Prime Series 2010-1	Class A2	3.3	1M BBSW + 1.25%	90.00
11-Aug-10	18-Aug-10	Liberty Financial	Liberty Prime Series 2010-1	Class AB	4.0	1M BBSW + 1.65%	10.40
18-Aug-10	27-Aug-10	Bank of Queensland	Series 2010-2 REDS Trust	Class A2	6.2	1M BBSW + 1.10%	497.60
26-Aug-10	02-Sep-10	Macquarie Bank	PUMA Masterfund P-16	Class A3	6.3	1M BBSW + 1.15%	247.50
06-Sep-10	09-Sep-10	FirstMac	FirstMac Mortgage Funding Trust Series 1-2010	Class A3	4.7	1M BBSW + 1.30%	164.00
06-Sep-10	09-Sep-10	FirstMac	FirstMac Mortgage Funding Trust Series 1-2010	Class AB	3.6	1M BBSW + 2.20%	26.77
23-Sep-10	28-Sep-10	Members' Equity Bank	SMHL Securitisation Fund 2010-3	Class A2	6.1	1M BBSW + 1.10%	290.00
14-Oct-10	20-Oct-10	ING Bank (Australia)	IDOL Trust Series 2010-1	Class A2	7.5	1M BBSW + 1.10%	250.00
10-Nov-10	18-Nov-10	Australian Central Credit Union	Light Trust No. 3	Class A3	5.4	1M BBSW + 1.20%	243.50
19-Nov-10	25-Nov-10	RESIMAC	RESIMAC Premier Series 2010-2	Class A2	4.8	1M BBSW + 1.25%	148.00
26-Nov-10	03-Dec-10	Police and Nurses Credit Society	Pinnacle Series Trust 2010-T1	Class A2	7.2	1M BBSW + 1.25%	96.50
26-Nov-10	03-Dec-10	Police and Nurses Credit Society	Pinnacle Series Trust 2010-T1	Class AB	6.7	1M BBSW + 2.00%	14.60

Table 4: AOFM's RMBS investments up to 30 June 2014 (continued)

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
10-Dec-10	16-Dec-10	Bendigo and Adelaide Bank	TORRENS Series 2010-3 Trust	Class A5	4.6	1M BBSW + 1.10%	395.00
10-Dec-10	16-Dec-10	Bendigo and Adelaide Bank	TORRENS Series 2010-3 Trust	Class AB	4.7	1M BBSW + 1.80%	20.00
15-Dec-10	21-Dec-10	Wide Bay Australia	WB Trust 2010-1	Class A2	6.6	1M BBSW + 1.25%	81.20
15-Dec-10	21-Dec-10	Wide Bay Australia	WB Trust 2010-1	Class AB	6.2	1M BBSW + 2.00%	23.00
17-Mar-11	24-Mar-11	Members' Equity Bank	SMHL Securitisation Fund 2011-1^				0.00
07-Apr-11	14-Apr-11	Community CPS	Barton Series 2011-1 Trust	Class A2	6.5	1M BBSW + 1.25%	90.90
08-Apr-11	13-Apr-11	Liberty Financial	Liberty Prime Series 2011-1	Class A2	4.0	1M BBSW + 1.30%	50.75
15-Apr-11	20-Apr-11	Macquarie Bank	PUMA Masterfund P-17	Class A2	5.6	1M BBSW + 1.15%	157.50
13-May-11	19-May-11	RESIMAC	RESIMAC Premier Series 2011-1	Class A	2.9	1M BBSW + 1.25%	170.00
13-May-11	19-May-11	RESIMAC	RESIMAC Premier Series 2011-1	Class AB	2.4	1M BBSW + 1.75%	22.00
20-May-11	27-May-11	AMP Bank	Progress 2011-1 Trust	Class A2	5.8	1M BBSW + 1.15%	138.00
10-Jun-11	17-Jun-11	ING Bank (Australia)	IDOL Trust Series 2011-1	Class A1	3.6	1M BBSW + 1.10%	206.00
11-Jul-11	14-Jul-11	Heritage Building Society	HBS Trust 2011-1	Class AB	5.5	1M BBSW + 1.95%	21.60
14-Jul-11	21-Jul-11	Bendigo and Adelaide Bank	TORRENS Series 2011-1(E) Trust	Class A3	6.6	1M BBSW + 1.20%	195.00
14-Jul-11	21-Jul-11	Bendigo and Adelaide Bank	TORRENS Series 2011-1(E) Trust	Class AB	5.6	1M BBSW + 1.75%	27.50
12-Oct-11	19-Oct-11	Members' Equity Bank	SMHL Securitisation Fund 2011-2	Class A	3.0	1M BBSW + 1.25%	175.25
12-Oct-11	19-Oct-11	Members' Equity Bank	SMHL Securitisation Fund 2011-2	Class AB	5.3	1M BBSW + 2.10%	25.25
28-Oct-11	04-Nov-11	Bendigo and Adelaide Bank	TORRENS Series 2011-2 Trust	Class A2	6.3	1M BBSW + 1.50%	163.75
28-Oct-11	04-Nov-11	Bendigo and Adelaide Bank	TORRENS Series 2011-2 Trust	Class AB	6.3	1M BBSW + 2.50%	26.25
11-Nov-11	18-Nov-11	ING Bank (Australia)	IDOL Trust Series 2011-2	Class A1	2.7	1M BBSW + 1.35%	146.50
11-Nov-11	18-Nov-11	ING Bank (Australia)	IDOL Trust Series 2011-2	Class A2	5.0	5.50%	50.00
23-Nov-11	08-Dec-11	Suncorp Metway	APOLLO Series 2011-1 Trust	Class A2	5.9	1M BBSW + 1.50%	250.00
23-Nov-11	08-Dec-11	Suncorp Metway	APOLLO Series 2011-1 Trust	Class AB	5.9	1M BBSW + 2.50%	63.00
20-Dec-11	22-Dec-11	FirstMac	FirstMac Mortgage Funding Trust Series 2-2011	Class A3	7.0	1M BBSW + 1.65%	87.70
20-Dec-11	22-Dec-11	FirstMac	FirstMac Mortgage Funding Trust Series 2-2011	Class AB	5.7	1M BBSW + 2.75%	11.70
29-Mar-12	12-Apr-12	ING Bank (Australia)	IDOL Trust Series 2012-1	Class A1	3.2	1M BBSW + 1.45%	200.00
13-Apr-12	23-Apr-12	Members' Equity Bank	SMHL Securitisation Fund 2012-1	Class A3	2.8	1M BBSW + 1.50%	123.50
17-May-12	29-May-12	AMP Bank	Progress 2012-1 Trust	Class A	3.4	1M BBSW + 1.55%	195.65
17-May-12	29-May-12	AMP Bank	Progress 2012-1 Trust	Class AB	5.9	1M BBSW + 2.85%	30.78
01-Jun-12	14-Jun-12	RESIMAC	RESIMAC Premier Series 2012-1	Class A2	2.4	1M BBSW + 1.65%	137.00
02-Aug-12	09-Aug-12	FirstMac	FirstMac Mortgage Funding Trust Series 1-2012	Class A2	6.1	1M BBSW + 2.10%	129.10
02-Aug-12	09-Aug-12	FirstMac	FirstMac Mortgage Funding Trust Series 1-2012	Class AB	6.1	1M BBSW + 3.00%	13.40
24-Aug-12	30-Aug-12	AMP Bank	Progress 2012-2 Trust^				0.00

Table 4: AOFM's RMBS investments up to 30 June 2014 (continued)

Pricing date	Settlement date	Issuer	Issue name	Tranche	Expected WAL* at closing (years)	Coupon (per cent)	Original face value ($m)
30-Aug-12	12-Sep-12	Suncorp Metway	APOLLO Series 2012-1 Trust	Class AB	5.9	1M BBSW + 3.00%	17.50
13-Sep-12	25-Sep-12	Members' Equity Bank	SMHL Securitisation Fund 2012-2^				0.00
27-Sep-12	10-Oct-12	ING Bank (Australia)	IDOL Trust Series 2012-2^				0.00
02-Nov-12	15-Nov-12	People's Choice	Light Trust No. 4^				0.00
12-Dec-12	18-Dec-12	FirstMac	FirstMac Mortgage Funding Trust Series 3-2012^				0.00
							15462.61

* Weighted average life.
^ The AOFM final allocation was zero.

Tender results for debt issuance

Table 5: Treasury Bond tender results — 2013-14

Tender date	Coupon and maturity	Face value amount allocated ($m)	Weighted average issue yield (%)	Spread to secondary market yield (basis points)	Range of bids accepted (basis points)	Times covered
3-Jul-13	4.75% 21-Apr-2027	700	4.1034	-0.03	0.50	3.06
5-Jul-13	4.75% 15-Jun-2016	700	2.8000	-1.21	0.00	5.73
10-Jul-13	3.25% 21-Apr-2029	700	4.3592	-0.08	1.50	1.54
12-Jul-13	5.50% 21-Jan-2018	700	3.0150	-1.50	0.00	3.34
17-Jul-13	2.75% 21-Apr-2024	700	3.8634	-0.50	1.00	3.59
19-Jul-13	4.75% 15-Jun-2016	700	2.6643	-1.00	0.50	4.84
26-Jul-13	5.50% 21-Apr-2023	700	3.7607	-0.18	0.50	3.30
31-Jul-13	4.75% 21-Apr-2027	700	4.0550	-0.95	0.00	3.15
2-Aug-13	4.25% 21-Jul-2017	700	2.8100	-1.02	0.00	5.20
7-Aug-13	3.25% 21-Apr-2025	1,000	3.9026	0.81	2.00	2.69
9-Aug-13	4.75% 21-Oct-2015	700	2.4218	-0.32	1.00	3.16
14-Aug-13	5.50% 21-Apr-2023	800	3.8382	-0.18	1.00	3.21
16-Aug-13	6.00% 15-Feb-2017	800	2.8700	-0.50	0.00	3.40
21-Aug-13	3.25% 21-Apr-2025	800	4.1682	0.20	1.50	2.27
23-Aug-13	5.50% 21-Jan-2018	800	3.1984	-0.34	0.50	3.74
28-Aug-13	2.75% 21-Apr-2024	800	3.9792	0.92	2.00	1.71
30-Aug-13	4.25% 21-Jul-2017	800	2.9680	-0.24	0.50	3.94
4-Sep-13	4.75% 21-Oct-2015	800	2.7138	-0.36	1.50	3.89
6-Sep-13	5.75% 15-May-2021	800	3.9592	0.22	1.00	2.50
11-Sep-13	5.50% 21-Apr-2023	800	4.1828	0.78	1.50	1.94
13-Sep-13	4.75% 15-Jun-2016	800	2.9085	0.15	0.50	4.39
18-Sep-13	4.75% 21-Oct-2015	800	2.7867	0.16	1.00	3.39
20-Sep-13	5.50% 21-Jan-2018	800	3.1923	0.19	1.50	4.15
25-Sep-13	4.75% 15-Jun-2016	800	2.7614	0.64	1.50	4.02
27-Sep-13	3.25% 21-Apr-2025	800	4.0866	0.22	1.50	2.46
2-Oct-13	5.50% 21-Apr-2023	800	3.9018	0.18	2.00	2.52
4-Oct-13	4.25% 21-Jul-2017	800	3.0694	-0.31	0.50	4.14
9-Oct-13	2.75% 21-Apr-2024	800	4.0683	0.07	1.00	4.36
11-Oct-13	4.75% 15-Jun-2016	800	2.9456	-0.69	1.00	4.28
16-Oct-13	4.50% 15-Apr-2020	800	3.7951	-0.22	1.00	3.01
18-Oct-13	5.75% 15-Jul-2022	800	3.9728	-0.47	0.50	3.59
25-Oct-13	2.75% 21-Apr-2024	800	4.0137	0.37	1.00	2.88
30-Oct-13	3.25% 21-Apr-2025	800	4.0754	0.29	1.50	2.59
1-Nov-13	5.75% 15-May-2021	800	3.8000	-1.49	1.00	4.27
6-Nov-13	3.25% 21-Apr-2029	600	4.6000	-0.36	0.00	4.53
8-Nov-13	4.25% 21-Jul-2017	1,000	3.1431	-3.94	2.50	3.58
13-Nov-13	5.50% 21-Apr-2023	800	4.1965	0.31	1.00	4.73
15-Nov-13	6.00% 15-Feb-2017	800	3.0545	-0.05	1.50	3.89
22-Nov-13	4.75% 15-Jun-2016	800	2.9681	-0.19	0.50	5.40
27-Nov-13	4.50% 15-Apr-2020	800	3.7061	-0.24	1.00	4.29
29-Nov-13	5.25% 15-Mar-2019	800	3.5060	-0.40	0.50	4.15
4-Dec-13	5.75% 15-Jul-2022	800	4.1615	-0.10	1.00	2.25
6-Dec-13	3.25% 21-Oct-2018	1,500	3.5738	N/A	3.00	3.13
11-Dec-13	3.25% 21-Apr-2025	800	4.4572	0.07	1.00	2.47

Table 5: Treasury Bond tender results — 2013-14 (continued)

Tender date	Coupon and maturity	Face value amount allocated ($m)	Weighted average issue yield (%)	Spread to secondary market yield (basis points)	Range of bids accepted (basis points)	Times covered
13-Dec-13	6.00% 15-Feb-2017	700	3.0148	-0.27	0.50	4.79
15-Jan-14	5.75% 15-May-2021	800	3.8919	-0.37	1.00	3.86
17-Jan-14	3.25% 21-Oct-2018	1,500	3.3257	-0.04	1.50	1.98
24-Jan-14	4.75% 21-Apr-2027	800	4.3331	0.19	1.50	2.12
29-Jan-14	2.75% 21-Apr-2024	800	4.0912	0.24	1.00	2.60
31-Jan-14	5.25% 15-Mar-2019	800	3.3288	-0.19	1.00	3.66
5-Feb-14	3.25% 21-Apr-2025	800	4.1550	-0.26	0.00	5.06
7-Feb-14	6.00% 15-Feb-2017	800	2.9785	-0.40	0.50	4.79
12-Feb-14	2.75% 21-Apr-2024	800	4.2041	-0.34	0.50	4.41
14-Feb-14	5.50% 21-Jan-2018	800	3.2157	-0.68	1.00	4.56
19-Feb-14	3.25% 21-Apr-2025	800	4.2344	-0.31	0.50	4.63
21-Feb-14	5.25% 15-Mar-2019	800	3.4661	-0.64	1.00	3.94
26-Feb-14	5.75% 15-May-2021	800	3.7850	-0.76	0.50	4.80
28-Feb-14	4.25% 21-Jul-2017	800	2.9647	-0.58	1.00	5.16
5-Mar-14	5.50% 21-Apr-2023	800	3.9609	-0.66	0.50	4.55
7-Mar-14	3.25% 21-Oct-2018	800	3.3869	-0.99	1.00	4.58
14-Mar-14	6.00% 15-Feb-2017	800	2.8861	-0.77	1.00	4.82
19-Mar-14	2.75% 21-Apr-2024	700	4.0891	-0.64	1.00	3.88
21-Mar-14	3.25% 21-Oct-2018	700	3.3988	-1.25	0.50	5.20
26-Mar-14	3.25% 21-Apr-2025	700	4.2036	-0.39	0.50	2.73
28-Mar-14	4.25% 21-Jul-2017	700	3.1050	-0.45	0.00	4.19
2-Apr-14	4.50% 21-Apr-2033	700	4.7100	-0.92	0.00	4.85
4-Apr-14	4.75% 15-Jun-2016	700	2.8621	-1.04	0.50	5.79
9-Apr-14	4.75% 21-Apr-2027	700	4.2885	-0.15	1.00	3.49
11-Apr-14	5.75% 15-May-2021	700	3.6982	-0.52	0.50	4.08
16-Apr-14	3.25% 21-Oct-2018	1,000	3.2885	-0.40	0.50	3.12
30-Apr-14	3.25% 21-Apr-2025	700	4.0311	-0.07	1.00	4.87
2-May-14	5.25% 15-Mar-2019	700	3.2795	-0.85	0.50	5.08
7-May-14	4.25% 21-Apr-2026	700	4.0050	-0.31	1.00	4.88
9-May-14	4.50% 15-Apr-2020	700	3.3622	-0.38	0.50	3.95
14-May-14	2.75% 21-Apr-2024	700	3.8081	-0.43	0.50	4.12
16-May-14	3.25% 21-Oct-2018	700	3.1196	-0.54	1.00	4.62
21-May-14	4.25% 21-Apr-2026	700	3.8257	-0.18	0.50	2.87
23-May-14	4.25% 21-Jul-2017	700	2.8800	-0.67	0.00	4.54
28-May-14	4.75% 21-Apr-2027	700	3.9479	-0.11	1.00	3.02
30-May-14	3.25% 21-Oct-2018	700	3.0600	-0.74	0.50	5.93
4-Jun-14	4.50% 21-Apr-2033	700	4.3157	-0.97	2.00	3.53
6-Jun-14	3.25% 21-Apr-2025	700	3.8594	-0.56	0.50	4.28
11-Jun-14	3.25% 21-Apr-2029	700	4.2055	-0.47	1.00	2.61
13-Jun-14	3.25% 21-Oct-2018	700	3.1114	-0.51	0.50	4.26
18-Jun-14	2.75% 21-Apr-2024	700	3.7393	-0.40	0.50	3.17
20-Jun-14	5.25% 15-Mar-2019	700	3.0436	-0.79	0.50	4.35
Average over year to June 2014				-0.37	0.86	3.82
Average over 3 years to June 2014				-0.24	0.99	3.62
Average over 10 years to June 2014				-0.06	1.07	3.71

Table 6: Treasury Indexed Bond tender results — 2013-14

Tender date	Coupon and maturity	Face value amount allocated ($m)	Weighted average issue yield (%)	Spread to secondary market yield (basis points)	Times covered
16-Jul-13	1.25% 21-Feb-2022	200	1.2550	-3.00	8.98
20-Aug-13	2.50% 20-Sep-2030	200	1.9539	-1.11	3.08
10-Sep-13	1.25% 21-Feb-2022	200	1.5989	-2.11	3.72
29-Oct-13	1.25% 21-Feb-2022	200	1.3483	-0.67	3.38
12-Nov-13	2.50% 20-Sep-2030	150	2.0900	-1.50	3.51
26-Nov-13	1.25% 21-Feb-2022	200	1.6139	-2.61	5.22
10-Dec-13	2.50% 20-Sep-2030	100	2.0690	-1.10	4.92
11-Feb-14	2.00% 21-Aug-2035	200	2.1635	-1.65	3.74
25-Feb-14	1.25% 21-Feb-2022	200	1.4460	-2.40	5.36
11-Mar-14	4.00% 20-Aug-2020	200	1.2667	-2.33	4.51
25-Mar-14	1.25% 21-Feb-2022	200	1.4017	-1.83	3.45
8-Apr-14	2.00% 21-Aug-2035	100	2.0712	-2.38	3.69
29-Apr-14	1.00% 21-Nov-2018	500	0.9530	N/A	3.96
20-May-14	1.25% 21-Feb-2022	200	1.0660	-1.90	4.36
10-Jun-14	1.00% 21-Nov-2018	200	0.7363	-3.37	5.34
24-Jun-14	2.00% 21-Aug-2035	100	1.6138	-2.62	5.77
Average over year to June 2014				-2.04	4.56
Average over 3 years to June 2014				-0.38	3.92

Table 7: Treasury Note tender results — 2013-14

Tender date	Maturity	Face value amount allocated ($m)	Weighted average issue yield (%)	Range of bids accepted (basis points)	Times covered	Spread to OIS (basis points)	Spread to BBSW (basis points)
18-Jul-13	25-Oct-13	1,000	2.4824	6.0	6.27	-11.35	-25.69
25-Jul-13	25-Oct-13	1,000	2.3805	3.0	5.30	-17.33	-35.42
25-Jul-13	08-Nov-13	1,000	2.3969	3.0	4.41	-13.79	-32.97
1-Aug-13	25-Oct-13	500	2.3413	4.0	4.51	-13.39	-28.75
8-Aug-13	08-Nov-13	500	2.3460	4.0	3.66	-9.67	-25.44
15-Aug-13	25-Oct-13	500	2.3539	6.0	4.71	-11.06	-26.75
22-Aug-13	08-Nov-13	1,000	2.3483	5.0	4.74	-11.72	-24.87
26-Sep-13	24-Jan-14	500	2.3539	10.0	5.41	-7.71	-22.67
26-Sep-13	21-Feb-14	500	2.3506	8.0	6.21	-6.33	-23.22
3-Oct-13	24-Jan-14	500	2.3856	4.0	3.88	-6.82	-18.82
10-Oct-13	24-Jan-14	500	2.4086	7.0	3.88	-4.76	-17.83
17-Oct-13	21-Feb-14	1,000	2.4602	4.0	2.94	0.02	-13.64
24-Oct-13	24-Jan-14	1,000	2.4484	7.0	3.13	-3.16	-15.02
24-Oct-13	21-Feb-14	500	2.4599	6.0	4.62	-2.01	-14.87
31-Oct-13	24-Jan-14	1,000	2.4688	2.0	2.99	-1.12	-12.47
7-Nov-13	24-Jan-14	1,000	2.4755	6.0	2.90	-1.45	-10.47
7-Nov-13	07-Mar-14	500	2.4831	5.0	3.56	-0.69	-11.42
14-Nov-13	24-Jan-14	500	2.4799	4.0	2.28	-1.01	-10.24
14-Nov-13	07-Mar-14	500	2.4765	3.0	2.93	-0.71	-11.46
21-Nov-13	24-Jan-14	500	2.5110	3.0	2.50	2.10	-7.34
21-Nov-13	07-Mar-14	500	2.4996	3.0	2.93	1.35	-8.52
8-May-14	08-Aug-14	500	2.4814	5.0	5.03	-1.86	-20.16
8-May-14	24-Oct-14	500	2.4709	19.0	4.09	-2.91	-23.80
15-May-14	08-Aug-14	500	2.5104	4.0	2.92	1.04	-17.19
15-May-14	24-Oct-14	500	2.5107	4.0	2.61	1.07	-19.64
22-May-14	08-Aug-14	500	2.5302	4.0	3.05	3.02	-15.14
22-May-14	24-Oct-14	500	2.5367	4.0	2.85	3.67	-16.86
29-May-14	08-Aug-14	500	2.5588	2.0	2.46	6.88	-12.21
29-May-14	24-Oct-14	500	2.5622	2.0	2.34	7.22	-14.08
12-Jun-14	08-Aug-14	500	2.4706	12.0	5.69	-2.94	-19.77
26-Jun-14	24-Oct-14	500	2.4979	7.0	4.68	0.68	-22.60
Average over year to June 2014				5.35	3.85	-3.38	-18.69
Average over 3 years to June 2014				7.17	4.72	0.47	-22.13

Glossary

Accrual cost

A method of accounting based on recording revenue and expenses when they are incurred, regardless of when cash is exchanged.

Bank Bill Swap Reference Rates (BBSW)

Reference rates for bank bills accepted by approved banks published each business day by the Australian Financial Markets Association.

Basis point

One hundredth of one per cent.

Bid-ask spread

The difference between the price (or yield) at which a market maker is willing to buy and sell a particular financial product or instrument.

Book value

(Also known as carrying amount). The amount at which an asset or liability is recognised in the balance sheet. Under a fair value methodology, measurement is by reference to current market rates. Under an historic cost methodology, measurement is by reference to market value rates at the time the original transaction was conducted. The AOFM's assets and liabilities are measured at fair value, except for Australian Government advances to State and Territory governments for public housing, which are measured at historic cost.

Bullet security

A security that repays principal owing to investors as a lump sum at a predetermined future date.

Cash Management Portfolio

The Cash Management Portfolio is a part of the overall portfolio of assets and liabilities managed by the AOFM. It contains short-term assets and liabilities and is used to manage the within-year variability in Government cash flows.

Commonwealth Government Securities (CGS)

Debt obligations of the Commonwealth evidenced by the issue of securities or, nowadays, issued as inscribed stock. CGS on issue are predominantly Treasury Bonds, Treasury Indexed Bonds and Treasury Notes but also include small residual amounts of Australian Savings Bonds, Peace Saving Certificates and War Saving Certificates.

Coupon rate

A rate of interest paid on a bond, which is fixed for a specified period (usually the term of the bond). In the case of Treasury Bonds coupon interest is payable semi-annually, while for Treasury Indexed Bonds it is paid quarterly. In each case, the coupon rate is set on the date of announcement of first issuance of the bond line.

Credit risk

The risk of counterparty default creating financial loss. Credit risk is contingent on the combination of a default and there being pecuniary loss. The AOFM faces credit risk in relation to its investment transactions.

Credit spread

The difference in yields between securities of different credit qualities. The credit spread reflects the additional net yield required by an investor from a security with more credit risk relative to one with less credit risk.

Discount

An amount by which the value of a security on transfer is less than its face (or par) value.

Discounting

Calculating the present value of a future amount.

Duration

Duration (expressed in years) represents the 'effective term' of a bond. It is the weighted average life of a bond or a portfolio of bonds. The weights are the relative cash flows associated with the bond or portfolio (the coupon payments and principal), discounted to their present value. See also modified duration.

Exposure

The amount of money at risk in a portfolio. Exposure to a risk is calculated by measuring the current mark-to-market value that is exposed to that risk.

Face value

The amount of money indicated on a security, or inscribed in relation to a security, as being due to be paid on maturity.

Fixed rate

An interest rate calculated as a constant percentage of the face value or notional principal and generally payable quarterly, semi-annually or annually. Treasury Bonds pay a fixed coupon rate semi-annually.

Floating rate

An interest rate that varies according to a particular indicator, such as the BBSW (the Bank Bill Swap Reference Rate). For example, the floating leg of an interest rate swap may provide for the interest paid to be reset every six months in accordance with the BBSW.

Foreign Debt Portfolio

The non-domestic currency component of the Long-Term Debt Portfolio. Following the elimination of the foreign currency derivatives exposure, this portfolio now consists of a single US dollar denominated loan that was issued in the 1980s.

Funding risk

The risk that an issuer is unable to raise funds, as required, in an orderly manner and without financial penalty. For the Australian Government, funding risk encompasses both long-term fund raising to cover future Budget needs and the short-term mismatches in the timing of Government payments and receipts.

Futures basket

A collection of like financial products or commodities, grouped together, that are used to define the benchmark for pricing a futures contract. For example, 3-year and 10-year Treasury Bond futures baskets consist of collections of Treasury Bond lines that have an average term to maturity of approximately three and ten years respectively.

Futures contract

An agreement between two parties that commits one party to buy an underlying financial instrument or commodity and another (counter) party to sell a financial instrument or commodity at a specific price at a future date. The agreement is completed at a specified expiration date by physical delivery or cash settlement, or alternatively is offset prior to the expiration date. In Australia, standardised futures contracts are traded on the Sydney Futures Exchange. Futures contracts traded on the Sydney Futures Exchange include contracts for 3-year and 10-year Treasury Bonds.

Historic cost

Basis of measurement where an asset or liability is recorded at fair value on initial recognition and, after initial recognition, by amortisation of the initial value using market rates at the time the transaction was conducted that gave rise to the asset or liability.

Interest

The charge for borrowing money, usually expressed as an annual percentage rate. For the AOFM financial statements, interest cost is the coupon payment (where relevant) adjusted for the amortised cost carrying value of a debt security. Where a debt security is issued at a premium or discount to its principal value, the premium or discount at issuance is recognised in amortised cost carrying value and amortised over the life of the security using the effective interest method. This amortisation is recognised in the interest cost.

For Treasury Indexed Bonds, the change in its amortised cost carrying value includes capital accretion of the principal due to inflation. As capital accretion occurs, it is also recognised in the interest cost.

Interest rate risk

The risk that the value of a portfolio or security will change due to a change in interest rates. For example, the market value of a bond drops as interest rates rise.

Issuance

The sale of debt securities in the primary market.

Kangaroo bonds

Australian dollar denominated bonds issued in the Australian capital market by foreign borrowers.

Liquidity

The capacity for a debt instrument to be readily purchased or sold. A liquid market allows the ready buying or selling of large quantities of an instrument without significant movement in price.

Liquidity also refers to the ability to meet cash payment obligations.

Liquidity risk

The risk that a financial instrument will not be able to be readily purchased or sold.

Long-Term Debt Portfolio

The Long-Term Debt Portfolio is a part of the overall portfolio of assets and liabilities managed by the AOFM. It contains ongoing domestic and foreign currency liabilities and assets.

Market risk

The risk that the price (value) of a financial instrument or portfolio of financial instruments will vary as market conditions change. In the case of a debt issuer and investor such as the AOFM, the principal source of market risk is from changes in interest rates.

Market value

The amount of money for which a security is traded in the market at a particular point in time.

Modified duration

A measure of the sensitivity of the market value of a debt security to a change in interest rates. It is measured as the percentage change in the market value of a debt instrument in response to a one percentage point change in nominal interest rates. Portfolios with higher modified durations tend to have more stable interest costs through time, but more volatile market values. Modified duration is related to duration by the equation:

$$\text{Modified duration} = \frac{\text{Duration (years)}}{1 + \text{yield to maturity}}$$

At times, 'modified duration' is abbreviated to 'duration', and desirably only in contexts where this will not lead to confusion.

Nominal debt

Debt that is not indexed to inflation. Treasury Notes and Treasury Bonds are examples of nominal debt.

Nominal interest rate

Interest rate that does not take account of the effects of inflation (in contrast to the 'real' interest rate).

Operational risk

The risk of loss, whether direct or indirect, arising from inadequate or failed internal processes, people, systems or from external events.

Overnight cash rate

The interest rate charged on overnight loans between financial intermediaries. The Reserve Bank of Australia manages the supply of funds available in the money market to keep the cash rate as close as possible to a target set by the Bank Board as an instrument of monetary policy.

Overnight Indexed Swap (OIS)

A fixed for floating interest rate swap in which one party agrees to pay another party a fixed interest rate in exchange for receiving the average overnight cash rate recorded over the term of the swap. The term to maturity of such swaps is typically between one week and one year. Financial market participants enter into overnight indexed swaps to manage their exposures to movement in the overnight cash rate.

Overnight indexed swaps are quoted by reference to the fixed interest rate leg of the swap. For example, the 3 month OIS rate is the interest rate for the fixed leg of an overnight indexed swap with a term to maturity of 3 months. Interest rates for term deposits placed by the AOFM with the RBA are set by reference to quoted rates for overnight interest swaps.

Physical debt

Securities that give rise to debt, in contrast to derivatives (which give rise to a contingent liability). Treasury Bonds, Treasury Indexed Bonds and Treasury Notes represent physical debt.

Present value

An amount that represents the value today of a payment to be received (or made) in the future. If the opportunity cost of funds, or discount rate is 10 per cent, the present value of \$100 to be received in two years is $\$100 \times [1/(1 + 0.10)^2] = \$82.64$.

Primary market

The market where securities are issued for the first time and where the sale proceeds go to the issuer. For example, the primary market for Treasury Bonds is when the bonds are sold at tender by the AOFM on behalf of the Australian Government.

Real interest rate

The interest rate that has been adjusted to take account of the effects of inflation. For example, if the coupon interest rate on a bond is 6.5 per cent and the inflation rate is 3.0 per cent then the real rate of interest on that bond is 3.5 per cent.

Repurchase agreement (Repo)

An agreement under which the seller of a security agrees to buy it back at a specified time and price.

Repricing risk

The risk that interest rates will have increased when maturing debt needs to be refinanced.

Residential mortgage-backed security (RMBS)

A debt instrument issued by a special purpose vehicle to finance the securitisation of a pool of loans that is secured by residential mortgages.

Risk premium

The difference between the return available on a risk-free asset and the return available on a riskier asset.

Secondary market

The market where securities are bought and sold subsequent to original issuance. Investors trade securities between themselves in the secondary market.

Securities lending

An activity whereby securities are lent to a financial market participant for a fee.

Securities Lending Facility

A facility established by the AOFM in 2004 that uses repurchase agreements to lend Treasury Bonds and Treasury Indexed Bonds to market participants for short periods. The facility is operated by the Reserve Bank of Australia on behalf of the AOFM. It supports the efficient operation of these markets as it facilitates trading by enabling dealers to obtain specific lines of stock when they are not readily available from other sources.

Securitisation

The process of converting a pool of assets into marketable financial instruments. The rights and obligations relating to the assets are assigned or transferred to a special purpose vehicle (typically a trust), which issues securities to pay for the assets. The cash flow from the asset pool is used to service the securities and any other costs of the special purpose vehicle.

Semi-government bond

A bond issued in the Australian capital market by Australian State or Territory governments.

Short-dated exposure

The proportion of a portfolio that will have its interest rate reset in the short-term. A portfolio with a high short-dated exposure will tend to have more volatile annual interest payments than a portfolio with low short-dated exposure.

Special purpose vehicle (SPV)

A financial trust established for a special purpose. A special purpose vehicle used in an Australian RMBS transaction is typically a bankruptcy-remote trust established for the sole purpose of acquiring a pool of mortgages from a mortgage lender and then issuing RMBS to finance those mortgages.

Spread

The difference between two prices or yields.

Swap

A financial transaction in which two counterparties agree to exchange streams of payments occurring over time according to predetermined rules.

Tender

A method of issuance whereby debt is sold through auction. The amount, coupon and maturity date of the stock are announced by the issuer. Registered participants then bid for their desired amounts of stock at interest rates at which they are prepared to buy. Bids are accepted from lowest interest rate (yield) upward until the issue amount has been filled. Stock is therefore allocated in order of lowest yield (and highest price).

Tenor

The tenor of a financial instrument is its remaining term to maturity.

Term deposit

A deposit held at a financial institution that has a fixed term. These are generally short-term with maturities ranging anywhere from a month to a few years. When a term deposit is purchased, the lender (the customer) understands that the money can only be withdrawn after the term has ended, or after having given a predetermined number of days' notice.

Term premium

The margin over the expected path of cash rates that investors require as compensation for having invested at greater terms to maturity.

Treasury Bond

A medium to long-term debt security issued by the Australian Government that carries an annual rate of interest (the coupon rate), which is fixed over the life of the security and payable in six monthly instalments (semi-annually) on the face, or par, value of the security. The bonds are repayable in full at face value on maturity.

Treasury Indexed Bond

A security issued by the Australian Government for which the capital value is adjusted periodically according to movements in the Consumer Price Index. Interest is paid quarterly at a fixed rate on the adjusted capital value. At maturity, investors receive the adjusted capital value of the bond — that is, the initial face value as adjusted for inflation over the life of the bond. Interest Indexed Bonds, another form of indexed bond, were also issued by the Commonwealth Government in the past but these have all now matured.

Treasury Note

A short-term debt security issued by the Australian Government at a discount and redeemable at par on maturity. The interest payable on the notes is represented by the difference between their issue value and their par or face value. Treasury Notes are issued to cover short-term mismatches between the Australian Government's payments and receipts. They are used in circumstances in which cash holdings may be temporarily low such as changes in the AOFM's holdings of term deposits with the Reserve Bank of Australia; soon after a large maturity; or at long intervals ahead of large revenue collections.

Two-way price

A price (or yield) at which a market-maker is prepared to both buy and sell a particular financial product or instrument. That is, the simultaneous quoting of a bid and an offer.

Yield

The expected rate of return expressed as a percentage of the net outlay or net proceeds of an investment.

Yield curve

Graphical representation on a specific date of the relationship between the yield on debt securities of the same credit quality, but different terms to maturity. When securities with longer terms to maturity have a higher yield than securities with shorter terms to maturity, the curve is said to have a positive slope. In the opposite case, the slope is said to be negative or inverse.

ACRONYMS

AASB	Australian Accounting Standards Board
ADIs	Authorised Deposit-taking Institutions
AFMA	Australian Financial Markets Association
ANAO	Australian National Audit Office
AOFM	Australian Office of Financial Management
APS	Australian Public Service
AUD	Australian dollar
BBSW	Bank Bill Swap Reference Rates
CEO	Chief Executive Officer
CGS	Commonwealth Government Securities
CPI	Consumer Price Index
EL	Executive Level (APS Classification)
FBT	Fringe Benefits Tax
FMA Act	*Financial Management and Accountability Act 1997*
FMO	Finance Minister's Orders
GDP	Gross Domestic Product
GFC	Global Financial Crisis
GST	Goods and Services Tax
HR	Human resources
IT	Information technology
OECD	Organisation for Economic Co-operation and Development

OIS	Overnight Indexed Swap
OPA	Official Public Account
RBA	Reserve Bank of Australia
RMBS	Residential Mortgage-backed Security
SES	Senior Executive Service
TIB	Treasury Indexed Bond
US	United States of America
USD	United States dollar

INDEX OF COMPLIANCE WITH REQUIREMENTS

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