AARNet Pty Ltd Financial Report and Directors' Report 2017

for the year ended 31 December 2017

ABN 54 084 540 518

aarnet

CONTENTS

DIRECTORS' REPORT

Your Directors present their report on the Company, AARNet Pty Limited ("AARNet"), for the year ended 31 December 2017.

The following persons were Directors of AARNet during the whole of the financial year and up to the date of this report:

Emeritus Professor Gerard Sutton AO
Chair of the Board and Chair of the Nomination and Remuneration Committee

Mr Chris Bridge

Dr Christine Burns

Professor Annabelle Duncan

Mr Rob Fitzpatrick
Member of the Audit, Finance and Risk Committee

Mr Chris Hancock
Chief Executive Officer

Mr Jeff Murray

Mr John Rohan
Deputy Chair of the Board, Chair of the Audit, Finance and Risk Committee and member of the Nomination and Remuneration Committee

Professor Deborah Terry

Emeritus Professor Mark Wainwright AM
Member of the Audit, Finance and Risk Committee and the Nomination and Remuneration Committee

Dr David Williams

Professor John Dewar was appointed a director on 23 March 2018, being the date of this report.

PRINCIPAL ACTIVITIES

AARNet is a not-for-profit, proprietary company in which 38 Australian universities and the Commonwealth Scientific and Industrial Research Organisation (CSIRO) have an equal shareholding.

AARNet's principal activity is the provision of internet and advanced telecommunication and network services to its shareholders ("Members") and to other relevant organisations. Services are provided in accordance with the AARNet Access Policy in order that Members and other customers may:

a) use AARNet's internet and other telecommunications facilities and services to provide educational programs and conduct research activities in an efficient and cost effective manner; and

b) collaborate with other parties (nationally and internationally) in furtherance of research and education objectives.

OTHER ACTIVITIES

In addition, AARNet:

a) facilitates the construction of connections (fibre tails) to the AARNet backbone and between campuses and other locations to facilitate services for Members and customers;

b) provides applications and services which operate across the AARNet network supporting teaching and research activities;

c) assists Members and other customers with network design, engineering and consulting services to optimise the end-to-end performance, robustness and resiliency of campus, data centre and cloud networks via the AARNet network;

d) participates in the design and deployment of advanced network infrastructure in partnership with network organisations in Australia and internationally, to develop national and global research and education networks; and

e) makes representations to all levels of government on policy, legislation and programs to improve the telecommunications facilities and services available to its Members and other customers.

DIVIDENDS

AARNet's constitution prohibits the payment of dividends or other distributions to its shareholders. Accordingly, no dividends have been paid, declared or recommended either during the financial year or in the period since that year ended (2016: nil).

REVIEW OF OPERATIONS

Network Performance

During the year AARNet's network services again provided high levels of performance and availability. In particular:

a) average network availability at 99.95% was slightly lower than in 2016 (99.982%) but was in line with AARNet's target for network availability (99.95%); and

b) the volume of traffic carried across the network increased by 23.8% (2016: 38.7%).

For over ten years, AARNet has experienced very significant growth in the traffic carried across the network. For the five years up to and including 2017, the average compound annual growth in traffic received by AARNet's Members was 38.2% pa.

Despite this significant and sustained growth in traffic, the amounts paid by Members for the carriage of this traffic, in the form of subscriptions, access and traffic charges, grew by an average of only 1.08% pa over the same five year period. In 2017, Members' subscriptions and related charges actually reduced by 0.4% from 2016 (see further commentary below).

Including traffic for non-member Customers, the volume of traffic carried by AARNet for all users has increased at an average compound rate of 43.8% over the five years to 2017.

However, in 2017 the rate of growth (for all users), while still significant, was 23.8%, which was below the five-year average rate (43.8% pa). AARNet believes the slower rate of growth is due, in part, to the transition of some traffic to virtual private networks and private optical circuits – traffic carried across these services is not counted as a component of general network traffic.

Network Expansion

During 2017 AARNet continued to invest to upgrade to the capacity of the AARNet network and to expand the geographic reach of the network's fibre footprint.

Overall spending on communication assets (including network infrastructure and equipment) was $13,574,599 during the year which was slightly higher than the $12,741,600 invested in 2016 (refer to note 20 to the financial statements).

During the year AARNet also substantially upgraded international capacity into South East Asia through the establishment of additional 2 x 10Gbps services from Perth to Singapore and Sydney to Singapore via Guam.

Domestic capacity was also upgraded in a number of areas of the network. In particular, capacity between Brisbane and key locations along the Sunshine Coast and into North Queensland was upgraded to provide multiple 100Gbps services along this route.

For a number of years AARNet has provided its Members and other large customers with substantial capacity between their campuses and cloud service providers. In 2017 a number of our smaller customers also began moving their services into the cloud, with the effect that AARNet continued to see growing demand for connections to data centres and commissioned a growing number of services to provide these connections.

Indigo Consortium

AARNet is a member of the Indigo consortium which is currently constructing a submarine fibre optic cable to provide capacity between Sydney and Perth as well as Perth to Singapore.

This is the first time AARNet has participated in this type of consortium and also the first time it has engaged in construction of this type of infrastructure. Indigo is scheduled to commence service during 2019 and, when it is commissioned, will provide AARNet with significantly enhanced capacity to connect with research networks in Asia as well as improved capacity and network resilience between the east and west coasts of Australia.

Further details about AARNet's participation in the project can be found at aarnet.edu.au/network-and-services/the-network/indigo-project.

Other Services

AARNet offers a range of other services to Members and other customers. Broadly, these services fall into three categories:

- **Infrastructure Services**, where AARNet facilitates the construction of fibre to provide network services to locations not yet connected to the network;
- **Transmission services** providing point-to-point capacity enabling Members and customers to link together geographically diverse campuses, or to provide dedicated high-speed capacity between user facilities and third party data centres; and
- **'Above the network' services** which directly support the delivery of teaching and research outcomes (including Zoom, a video conferencing/meeting service offered in conjunction with Zoom Inc and Cloudstor, a service which is optimised for the storage and sharing of research data sets).

New services were commissioned in each of these categories during 2017. Notably, AARNet expanded the portfolio of services included in Above the network services by partnering with Panopto Inc to host the Panopto service on the AARNet network in Australia. Panopto is a video recording, management and streaming service which is used by many universities around the world as a teaching and research resource.

Subscriptions and Telecommunications Revenues

AARNet's Members pay subscription and related fees for connection to the network and carriage of data across the network (to research and education facilities in Australia, international research and education networks, and to the general internet). These charges form the largest component of AARNet's revenues.

During 2017 Members' subscription and related charges were 0.4% lower than in than in 2016 despite the growth in Members' traffic (both on-net and off-net) discussed above.

The reduction reflects lower charges for access services and reductions to the Peering Charge element of the Member subscriptions.

	2017 $	2016 $	Increase
Members: Subscription, Traffic and Access	40,399,463	40,551,073	(0.4%)
Non-Member: Subscription, Traffic and Access	16,097,666	14,493,953	11.1%
Other Services	13,901,773	13,076,531	6.3%
Telecommunications Revenue	70,398,902	68,121,557	3.3%

Non-Member subscriptions continued to grow strongly with 2017 revenues up 11.1% on the previous year. This reflects continued growth in Non-Member customers connected to the network as well as traffic growth from existing customers.

Growth in other telecommunications services (available to both Members and non-members) rose by 6.3% over 2016. Within this amount, revenues from transmission services increased strongly but the overall growth in this area was reduced by two one-off factors:

a) a new cost sharing model with Members and customers for use of a third-party network used to provide services to a significant regional area; and

b) an accounting adjustment whereby the recognition of revenues from a particular service was changed to an accrual basis from a cash basis.

Overall, subscriptions and service revenues increased by 3.3% from 2016.

Infrastructure Revenues

Infrastructure service fees (income from the provision of new fibre infrastructure, where AARNet retains ownership of the fibre) again rose significantly in 2017 (23.1%) reflecting the value of infrastructure projects completed and brought into service – including projects which completed in the latter part of 2016 contributing a full year's revenue in 2017.

	2017 $	2016 $	Increase
Infrastructure Service Fees	10,158,604	8,254,361	23.1%
Infrastructure Project Construction Revenue	1,829,763	1,891,714	(3.3%)
	11,988,367	10,146,075	18.2%

Revenues from infrastructure construction and allied activities (such as services to relocate infrastructure or design and construction activities where AARNet does not retain ownership of the infrastructure created) reduced by 3.3%, however, this income stream is significantly lower than the Infrastructure service fee arrangements, and overall infrastructure revenues were 18.2% higher in 2017 than 2016.

Telecommunication Expenses

The largest category of operating costs, Telecommunication Expenses were in line with costs incurred in the previous year. Within the category, AARNet experienced increases in transmission costs but these were offset by savings in maintenance charges and other costs.

Employee and Administration Costs

During the latter part of 2016, and again in 2017, AARNet increased the number of people employed in our Product Development, Service Desk and Infrastructure Development Teams. The additional headcount, was planned to support the development, commissioning and operation of new services (including new transmission services, new "above the network" services) as well as expanding our Infrastructure team to enable AARNet to roll out more AARNet owned infrastructure to reduce reliance on leased capacity on key network routes.

The additional headcount resulted in growth in Employee Benefits costs in our Infrastructure team of 36% and 21% in the rest of the company.

The increased headcount also contributed to some increase in administration costs, however the increase in Administration – Telecommunications costs is principally driven by costs associated with a significant project designed to re-engineer and streamline internal processes related to provisioning new services. These costs will continue in 2018, and the project will allow AARNet to support ongoing growth in the range and number of services it provides, along with ongoing growth in the number of non-member customers connected to the network.

Depreciation and Amortisation Charges

Depreciation and Amortisation charges, inclusive of depreciation on equipment, depreciation on infrastructure and amortisation of Indefeasible Rights to Use (IRUs) totalled $17,909,198 in 2017 which was 2.4% higher than 2016 ($17,496,079).

Within these totals depreciation charges on infrastructure increased by 11% over 2016 reflecting additional infrastructure brought into service in 2017 and the latter part of 2016. This increase was partially offset by reduced amortisation charges on IRUs driven by strength in the Australian Dollar during 2017 (which lowered the expected total value of IRUs in service; the value on which amortisation is calculated).

Finance Costs

AARNet has significant contractual commitments requiring it to make foreign currency denominated payments (mainly United States Dollars) for international transmission capacity (including the commitments for capacity under IRUs referred to in the previous section). These commitments, many of which extend for periods in excess of five years, are included in note 2(b) to the financial statements.

In order to hedge the exposure to exchange rate fluctuations with respect to these commitments (and other payments required in foreign currencies), AARNet arranges forward foreign currency purchases, purchases foreign currency options and maintains holdings of foreign currency balances. These arrangements are discussed in note 24 to the financial statements.

For the last few years, these arrangements have contributed to AARNet recognising a foreign exchange gain – such a gain usually arises when the Australian dollar weakens against the US Dollar. During certain periods in 2017, the Australian dollar strengthened against the US Dollar which had the effect of reducing the Australian Dollar value of the outstanding commitments that AARNet was committed to paying, while, at the same time, reducing the value of the hedging arrangements in place against those commitments.

Consequently, during 2017, AARNet recorded a loss of $2,336,325 on foreign currency contracts compared to a loss of $322,683 in 2016 (refer note 10 to the financial statements). These losses are non-cash items and are offset by reductions in the Australian dollar equivalent of the amounts AARNet has paid, or expects to pay, for charges (which may be capital or expense items) denominated in US Dollars.

ACCUMULATED SURPLUS AND RESERVES

In 2017 AARNet recorded a net surplus of $15,472,662 (2016: $21,376,178).

In the Board's view, it is prudent for AARNet to generate a surplus in order that investments in network capability and services may be funded without calling on Members to contribute further equity to the company.

Surpluses earned by AARNet cannot (by virtue of the terms of AARNet's constitution) be distributed to the shareholders.

Surpluses earned in recent years, aided by conservative financial management, have therefore been accumulated into significant holdings of cash and investments. In 2016 and 2017 a significant portion of these funds were used to:

a) secure the extension of the IRU arrangement for AARNet's national backbone network;

b) Invest in the Indigo consortium constructing submarine fibre capacity (as described above).

In addition, AARNet intends to use further funds to:

a) finance investments in:

    (i) infrastructure and equipment to expand the reach, capability and resilience of AARNet's network; and

    (ii) technology to enhance the delivery of services AARNet delivers to Members and other customers.

b) supplement Members' subscriptions and other income in future years; and

c) defray part of the significant financial commitments in respect of non-cancellable operating leases (principally rights to use the traffic paths of fibre cable systems operated by other telecommunication carriers) which, at year end, were $120,715,519, refer note 2(b) to the financial statements.

NET ASSETS

Net assets at 31 December 2017 were $216,492,799 (2016: $200,780,478). The increase represents the surplus for 2017 plus the change in value of available-for-sale financial assets during 2017.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

Except for the matters discussed under the heading "Review of Operations" there were no significant changes in the Company's state of affairs during the financial year ended 31 December 2017.

MATTERS SUBSEQUENT TO THE END OF THE FINANCIAL YEAR

AARNet is party to an agreement with several other organisations to jointly construct and operate a submarine telecommunications cable between the east coast of Australia and Guam. AARNet believes this agreement became binding in March 2018, subsequent to the end of our financial year, and that construction will begin in 2018. Consequently, AARNet is now obliged to invest in the construction of the infrastructure concerned and this expenditure is not reflected in the amounts shown in note 2(a) to the financial statements.

When completed, this infrastructure will provide AARNet with a high capacity route to Guam where connections to key South East and Northern Asian regions are available. This will enable AARNet to offer high capacity services to Asian destinations, provide an east coast route to Asia (providing diversity for the routes from the west coast) and significantly expand AARNet's capacity to carry research and education traffic into Asia, which is increasingly becoming a key source and destination for such traffic.

Except for the matter referred to in the preceding two paragraphs and the matters discussed under the heading "Review of Operations", no other matter or circumstance has arisen since 31 December 2017 that has significantly affected or may significantly affect:

a) AARNet's operations in future financial years;

b) the results of those operations in future financial years; or

c) AARNet's state of affairs in future financial years.

LIKELY DEVELOPMENTS AND EXPECTED RESULTS OF OPERATIONS

While the rate of traffic growth has slowed in the last two years, AARNet expects network traffic will continue to grow at significant levels during 2018.

In addition, investment in the Indigo submarine cable system will continue throughout 2018, although the system is not expected to commence service until 2019.

ENVIRONMENTAL REGULATION

AARNet's operations are not adversely affected by any significant environmental regulation. AARNet believes its greenhouse gas emissions are substantially below the thresholds that are subject to the reporting requirements of either the Energy Efficiency Opportunities Act 2006 and the National Greenhouse and Energy Reporting Act 2007.

INSURANCE FOR OFFICERS

During the financial year, AARNet paid a premium of $30,274 (2016: $28,394) in respect of liability insurance for the Company's Directors and Officers. The liabilities insured against are costs and expenses that may be incurred in defending civil or criminal proceedings that may be brought against the Directors and Officers in their capacity as Directors and Officers of AARNet, and any other payments arising from liabilities incurred by the Officers. It is not possible to apportion the premium between amounts relating to the insurance against legal costs and those relating to other liabilities.

No known liability has arisen under these indemnities to the date of this report.

AGREEMENT TO INDEMNIFY OFFICERS

Under the terms of its Constitution, AARNet provides indemnity to persons who are, or have been, an officer or auditor of AARNet, but only to the extent permitted by law and to the extent that the officer or auditor is not indemnified by Directors' and Officers' liability insurance maintained by AARNet. The indemnity is against liability incurred by that person as an officer or auditor of AARNet to another person and for costs and expenses incurred by the officer or auditor in defending such proceedings.

Separately, AARNet and each director of AARNet have entered into a Deed of Indemnity under which AARNet indemnifies each director against any liability:

a) to a third party (that is, other than to AARNet) unless the liability arises out of conduct involving a lack of good faith, and

b) for legal costs incurred in successfully defending civil or criminal proceedings.

No known liability has arisen under these indemnities as at the date of this report.

AUDITOR

A copy of the Auditor's Independence Declaration as required under s.60-40 of the Australian Charities and Not-for-profits Commission Act 2012 is included on page 10 of this financial report.

PricewaterhouseCoopers continues in office as auditor of the company.

This report is made in accordance with a resolution of Directors.

Emeritus Professor GR Sutton AO	Mr CM Hancock
Director	Director
Sydney	
23rd March 2018	

AUDITOR'S INDEPENDENCE DECLARATION

pwc

Auditor's Independence Declaration

As lead auditor for the audit of AARNet Pty Ltd for the year ended 31 December 2017, I declare that to the best of my knowledge and belief, there have been no contraventions of any applicable code of professional conduct in relation to the audit.

Scott Walsh
Partner
PricewaterhouseCoopers

Sydney
23 March 2018

PricewaterhouseCoopers, ABN 52 780 433 757
One International Towers Sydney, Watermans Quay, Barangaroo, GPO BOX 2650, SYDNEY NSW 2001
T: +61 2 8266 0000, F: +61 2 8266 9999, www.pwc.com.au
Level 11, 1PSQ, 169 Macquarie Street, Parramatta NSW 2150, PO Box 1155 Parramatta NSW 2124
T: +61 2 9659 2476, F: +61 2 8266 9999, www.pwc.com.au

Liability limited by a scheme approved under Professional Standards Legislation.

STATEMENT OF SURPLUS

	Notes	2017 $	2016 $
Services revenue	8	82,387,269	78,267,632
Other revenue	9	3,469,645	3,806,604
Grants and contributions received	9	536,161	572,146
Total revenue		**86,393,075**	**82,646,382**
Telecommunications expenses		(18,964,895)	(18,886,274)
Depreciation and amortisation - Telecommunications	10	(10,294,042)	(10,633,367)
Employee benefits expense - Telecommunications		(15,469,888)	(12,793,017)
Administration - Telecommunications		(8,805,657)	(6,969,159)
Infrastructure project construction		(3,148,751)	(2,302,455)
Depreciation and amortisation - Infrastructure projects	10	(7,615,157)	(6,862,715)
Employee benefits expense - Infrastructure Development Group		(2,993,170)	(2,207,844)
Administration - Infrastructure Development Group		(657,143)	(282,175)
Other expenses (including finance costs)	10	(2,971,710)	(333,198)
Total expenses		**(70,920,413)**	**(61,270,204)**
Net surplus		**15,472,662**	**21,376,178**
Movement in the fair value of available-for-sale financial assets		**239,659**	**(138,836)**
Total comprehensive surplus for the year		**15,712,321**	**21,237,342**

BALANCE SHEET

	Notes	31 December 2017 $	31 December 2016 $
ASSETS			
Current assets			
Cash and cash equivalents	11	23,566,326	18,493,901
Receivables	13	36,747,108	40,355,449
Derivative financial instruments	24	-	390,323
Accrued income	14	597,039	1,327,689
Held-to-maturity investments	16	35,500,000	32,562,666
Total current assets		96,410,473	93,130,028
Non-current assets			
Receivables	19	-	212,245
Available-for-sale financial assets	18	12,825,223	11,366,442
Held-to-maturity investments	17	33,237,788	24,183,045
Derivative financial instruments	24	-	15,465
Other financial assets- Non-controlling investment in Smart Services CRC Pty Ltd		1	1
Property, plant and equipment	20	87,683,386	83,094,086
Indefeasible Rights to Use traffic paths	21	75,746,689	82,476,159
Total non-current assets		209,493,087	201,347,443
Total assets		**305,903,560**	**294,477,471**
LIABILITIES			
Current liabilities			
Payables	3	10,148,411	13,608,311
Derivative financial instruments	24	700,888	-
Provisions	6	4,738,680	3,267,426
Other liabilities		193,548	184,308
Income in advance	4	48,930,900	47,164,504
Total current liabilities		**64,712,427**	**64,224,549**
Non-current liabilities			
Income in advance	5	23,005,799	28,625,227
Derivative financial instruments	24	1,229,649	-
Provisions	7	462,886	847,217
Total non-current liabilities		**24,698,334**	**29,472,444**
Total liabilities		**89,410,761**	**93,696,993**
Net assets		**216,492,799**	**200,780,478**
EQUITY			
Contributed equity	22	39,039	39,039
Reserve (accumulated unrealised gain/loss on investments)	23	588,857	349,198
Retained earnings	23	215,864,903	200,392,241
Capital and reserves attributable to members of AARNet Pty Ltd		216,492,799	200,780,478
Total equity		**216,492,799**	**200,780,478**

STATEMENT OF CHANGES IN EQUITY

	2017 $	2016 $
Total equity at the beginning of the financial year	**200,780,478**	179,543,136
Changes in the fair value of available-for-sale financial assets, net of tax	**239,659**	(138,836)
Net surplus for the year	**15,472,662**	21,376,178
Total recognised surplus and expense for the year	**15,712,321**	21,237,342
Total equity at the end of the financial year	**216,492,799**	200,780,478

STATEMENT OF CASH FLOWS

	Notes	2017 $	2016 $
Cash flows from operating activities			
Receipts from members and customers (inclusive of goods and services tax)		**92,152,847**	85,458,170
Payments to suppliers and employees (inclusive of goods and services tax)		**(59,300,557)**	(47,800,074)
		32,852,290	37,658,096
Interest paid		**-**	(2,491)
Net cash inflow from operating activities	12	**32,852,290**	37,655,605
Cash flows from investing activities			
Payments for property, plant and equipment		**(17,406,467)**	(12,914,717)
Payments for Indefeasible Rights to Use traffic paths (intangible assets)		**(192,335)**	(20,465,200)
Payments for available-for-sale financial assets		**(4,222,870)**	(2,919,420)
Payments for held-to-maturity investments		**(101,375,661)**	(64,343,611)
Proceeds from sale of available-for-sale financial assets		**3,229,342**	3,121,950
Proceeds from held-to-maturity investments		**89,425,000**	52,340,000
Dividends received		**553,833**	397,104
Interest received		**2,201,293**	2,280,206
Proceeds from sale of property, plant and equipment		**8,000**	962
Net cash outflow from investing activities		**(27,779,865)**	(42,502,726)
Net increase/(decrease) in cash and cash equivalents		**5,072,425**	(4,847,121)
Cash and cash equivalents at the beginning of the financial year		**18,493,901**	23,341,022
Cash and cash equivalents at end of year	11	**23,566,326**	18,493,901

NOTES TO THE FINANCIAL STATEMENTS

1. BASIS OF PREPARATION

These general purpose financial statements have been prepared in accordance with Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board and the Australian Charities and Not-for-profits Commission Act 2012. AARNet Pty Ltd is domiciled in Australia and is a not-for-profit entity for the purpose of preparing the financial statements. The registered address of AARNet Pty Ltd is Level 2, Building 1, 3 Richardson Place, North Ryde, NSW, 2113.

Historical cost convention

The financial statements have been prepared on a historical cost basis, except for the following: available-for-sale financial assets, financial assets and liabilities (including derivative instruments), certain classes of property, plant and equipment and investment assets that are measured at fair value.

Income tax

AARNet is exempt from income tax under Section 50-5 of the Income Tax Assessment Act 1997 and therefore, no provision for income tax is included in these financial statements.

2. COMMITMENTS AND CONTINGENCIES

(a) Expenditure and capital commitments

	31 December 2017 $	31 December 2016 $
Within one year	**20,496,787**	2,732,371
Later than one year but not later than five years	**8,746,604**	1,368,709
Later than five years	**148,238**	199,325
	29,391,629	4,300,405

(b) Lease and capacity commitments: AARNet as lessee

	31 December 2017 $	31 December 2016 $
Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows:		
Within one year	**7,451,125**	7,735,376
Later than one year but not later than five years	**47,068,560**	46,223,865
Later than five years	**66,195,834**	74,866,175
Commitments not recognised in the financial statements	**120,715,519**	128,825,416

(c) Contingent Liabilities

AARNet's bankers have issued bank guarantees in favour of the Company's landlords and a third-party contractor with total face value of $1,064,584 (2016: $549,469).

3. CURRENT LIABILITIES - PAYABLES

	31 December 2017 $	31 December 2016 $
Current liabilities		
Trade payables	**2,855,890**	5,081,764
Other payables	**7,292,521**	8,526,547
	10,148,411	13,608,311

Trade payables and accruals are expected to be paid within 30 days.

These amounts represent liabilities for goods and services provided to AARNet prior to the end of the financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

Accounting Policy

The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to AARNet for similar financial instruments.

4. CURRENT LIABILITIES - INCOME IN ADVANCE

	31 December 2017 $	31 December 2016 $
Infrastructure projects	**16,784,255**	14,979,243
Other	**1,369,742**	1,296,242
Infrastructure service fees	**5,986,271**	4,175,960
Subscriptions	**24,790,632**	26,713,059
	48,930,900	47,164,504

Accounting Policy

The Accounting Policy for Income in Advance is described in note 8.

5. NON-CURRENT LIABILITIES - INCOME IN ADVANCE

	31 December 2017 $	31 December 2016 $
Infrastructure service fees	**19,243,926**	24,308,000
Infrastructure projects	**1,719,016**	1,962,278
Other deferred income	**2,042,857**	2,354,949
	23,005,799	28,625,227

Accounting Policy

The Accounting Policy for Income in Advance is described in note 8.

6. CURRENT LIABILITIES - PROVISIONS

	31 December 2017 $	31 December 2016 $
Employee benefits	**4,619,539**	3,267,426
Make good provision	**119,141**	-
	4,738,680	3,267,426

Accounting Policy

Wages and salaries and annual leave

Liabilities for wages and salaries, including non-monetary benefits and leave entitlements expected to be settled within 12 months of the reporting date, are recognised in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled.

7. NON-CURRENT LIABILITIES - PROVISIONS

	31 December 2017 $	31 December 2016 $
Employee benefits	**342,823**	608,013
Make good on leased premises	**120,063**	239,204
	462,886	847,217

Movements in provisions

Movements in each class of provision during the financial year, other than employee benefits, are set out below:

2017	Make good on leased premises $
Non-current liabilities - Provisions	
Carrying amount at start of year	239,204
Decrease in provision recognised	(119,141)
Carrying amount at end of year	120,063

2016	Make good on leased premises $
Non-current liabilities - Provisions	
Carrying amount at start of year	239,204
Movement during the year	-
Carrying amount at end of year	239,204

Accounting Policy

Employee benefits

These are liabilities for long service leave and annual leave not expected to be settled wholly within 12 months after the end of the period in which the employees render the related service. They are therefore recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the end of the reporting period using the projected unit credit method.

Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using market yields at the end of the reporting period of corporate bonds with terms and currencies that match, as closely as possible, the estimated future cash outflows. Re-measurements as a result of experience adjustments are recognised in the Statement of Surplus.

Make good on leased premises

Provisions for make good costs on leased premises are recognised when AARNet has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.

8. SERVICE REVENUE

	2017 $	2016 $
Telecommunications		
Members: Subscription, Traffic and Access	**40,399,463**	40,551,073
Non-Member: Subscription, Traffic and Access	**16,097,666**	14,493,953
Other Services	**13,901,773**	13,076,531
	70,398,902	68,121,557
Infrastructure & service agreements		
Infrastructure service fees	10,158,604	8,254,361
Infrastructure project construction revenue	1,829,763	1,891,714
Space		
	82,387,269	78,267,632

Accounting Policy

Subscriptions, Traffic and Telecommunications Services

Revenue from services delivered under a subscription charging arrangement is recognised over the period to which the subscription relates. Revenue from provision of other telecommunications services is recognised upon delivery of the services to the user.

Infrastructure and Service Agreements

Where a customer engages AARNet to provision infrastructure and deliver services to the customer across that infrastructure, with the infrastructure becoming the property of AARNet (referred to as a Service Agreement) revenue is recognised over the term of that Service Agreement.

Revenue from the provision of infrastructure where the infrastructure becomes the property of the customer is recognised on the percentage of completion method unless the outcome cannot be reliably estimated. Where a contract outcome cannot be reliably estimated amounts are recognised as revenue equal to the costs in the project to date.

In some cases the provision of infrastructure may involve the receipt of contributed assets - these contributed assets are accounted for as described in note 9.

Discounts and Taxes

Amounts disclosed as revenue are net of any discounts or taxes paid.

Income in Advance

Amounts received or due and receivable in respect of future subscription periods or for services which have not been delivered are recorded as Income in Advance and appear as a liability (refer notes 4 and 5).

Income in Advance is classified as either a current liability or a non-current liability depending on when the relevant subscription expires or the related service is expected to be delivered.

9. OTHER REVENUE, GRANTS AND CONTRIBUTIONS RECEIVED

In 2017 and 2016 AARNet recorded significant amounts of Other Revenue, Grants Received and Other Contributions.

These amounts are a material component of the surplus recorded by the company.

	2017 $	2016 $
Interest	2,126,636	2,190,033
Dividends	528,390	455,137
Gain on foreign currency transactions	-	279,512
Gain on Available-For-Sale Financial Assets	225,594	487,362
Other income	589,025	394,560
Other Revenue	3,469,645	3,806,604
Grants and Contributions received	536,161	572,146

Grants and Contributions Received

This item includes amounts received by AARNet by way of grants and contributions where AARNet does not supply a service to the organisations providing the funding.

Accounting Policy

Interest and Dividend Income

Interest and dividend income is recognised as it accrues and dividends are recognised as revenue when the right to receive payment is established.

Foreign Currency Contracts

At year end, Foreign Currency Contracts are recognised at fair value as described in note 24 (see Derivative Financial Instruments). Realised and unrealised gain or losses on such contracts are taken into account each year in the Statement of Surplus. AARNet does not apply hedge accounting.

Contributed Assets

Contributed assets (including the contribution of funds by government agencies or other persons to facilitate the construction of infrastructure for the AARNet network) are recognised at fair value when title and control of the asset passes or when the conditions to receive or retain funding are met.

10. EXPENSES

	Notes	2017 $	2016 $
Depreciation			
Office equipment		**817,034**	556,798
Leasehold improvements		**148,584**	139,143
Communication assets		**9,955,384**	8,998,018
Software		**66,391**	87,399
Total depreciation	20	**10,987,393**	9,781,358
Amortisation			
Intangibles - Indefeasible Rights to Use traffic paths	21	**6,921,805**	7,714,721
Total depreciation and amortisation		**17,909,198**	17,496,079
Other expenses (including finance costs)			
Interest and finance charges paid/payable		**-**	2,491
Loss on foreign currency contracts		**2,336,325**	322,683
Loss on foreign currency transactions		**635,385**	-
Loss on disposal of assets		**-**	8,024
Total other expenses		**2,971,710**	333,198
Loss on sale of available-for-sale financial assets		**68,248**	228,363
Rental expense relating to operating leases			
Minimum lease payments - premises		**1,148,152**	1,052,077
Superannuation expense		**2,324,579**	1,813,164

Loss of Foreign Currency Contracts

The company hedges a significant proportion of its exposure to foreign currency movements (refer note 24) and does not apply hedge accounting. The accounting policy adopted with respect to derivatives and hedging activities is described below. During 2017 movements in the Australian dollar produced a loss (including realised and unrealised loss) on the hedging instruments held during and as at the end of the year of $2,336,325 (2016: $322,683).

Unisuper Defined Benefit Division

Employer superannuation contributions for certain of AARNet's employees are held by the Unisuper Defined Benefit Division (DBD) which is a defined benefit plan under superannuation law but is considered a defined contribution plan under accounting standard AASB 119.

AARNet is not legally obliged to make additional contributions to the DBD in respect of any deficiency within the DBD. Accordingly, no provision has been made in AARNet's accounts for any potential shortfall in the DBD.

Accounting Policy

Depreciation and Amortisation

The accounting policy for depreciation and amortisation is described in notes 20 and 21 respectively.

11. CURRENT ASSETS - CASH AND CASH EQUIVALENTS

	31 December 2017 $	31 December 2016 $
Current assets		
Cash at bank and in hand (AUD)	**9,685,550**	8,704,812
Cash at bank (USD and EUR)	**7,578,080**	2,553,143
Deposits at call - all denominated in AUD	**6,302,696**	7,235,946
	23,566,326	18,493,901

Cash at bank and on hand

Cash at bank and on hand is held at interest rates varying between 0.00% and 1.36% (2016: 0.00% and 1.16%). During the year, cash is transferred to or from term deposits to meet liquidity requirements.

Deposits at call

Interest bearing deposits at call attracted interest rates between 2.33% and 2.51% (2016: 2.57% and 2.75%). These deposits have an average maturity of 181 days.

Bank guarantee and credit facilities

AARNet has a $1,200,000 Bank Guarantee Facility provided by the National Australia Bank. AARNet has drawn on this facility to provide bank guarantees in favour of the landlords for leased premises and a third party contractor. AARNet has an unsecured credit card facility of $300,000.

Accounting Policy

For the purpose of presentation in the statement of cash flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, bank overdrafts and other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

12. RECONCILIATION OF NET SURPLUS TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	2017 $	2016 $
Surplus for the year	**15,472,662**	21,376,178
Depreciation and amortisation	**17,909,199**	17,496,079
Dividend income	**(528,390)**	(455,137)
Interest received	**(2,201,293)**	(2,280,203)
Net gain on sale of investments	**(225,594)**	(487,362)
Net amortised interest income	**(41,417)**	(23,551)
Net (gain)/ loss on sale of assets	**(8,000)**	8,024
Decrease/ (increase) in trade receivables	**3,800,249**	(2,388,963)
Decrease in accrued income	**705,208**	320,692
Decrease in prepayments and other debtors	**20,337**	565,308
Decrease in derivative financial instruments	**2,336,325**	106,371
Increase/ (decrease) in trade payables	**(1,630,127)**	2,457,383
Increase in other operating liabilities	**9,240**	135,042
Increase in provisions	**1,086,923**	595,585
Increase/(decrease) in income received in advance	**(3,853,032)**	230,159
Net cash inflow from operating activities	**32,852,290**	37,655,605

13. CURRENT ASSETS - RECEIVABLES

	31 December 2017 $	31 December 2016 $
Trade receivables	**33,716,530**	37,516,779
Provision for impairment of receivables	**(255,000)**	(255,000)
	33,461,530	37,261,779
Prepayments and Other Debtors	**3,285,578**	3,093,670
	36,747,108	40,355,449

Trade Receivables

Trade receivables are due for settlement no more than 30 days from the date of recognition.

At 31 December 2017, trade receivables included balances of $95,599 (2016: $453,877) which are past due but not impaired or considered uncollectable. These amounts have been outstanding for more than 90 days. These relate to a number of customers for whom there is no history of default.

Prepayments and Other Debtors

Payments for goods and services which are to be provided in future years are recognised as prepayments. Other debtors generally arise from transactions outside the usual operating activities of AARNet. Interest is not normally charged.

Fair Value

Due to the short-term nature of these receivables, their carrying amount is assumed to approximate their fair value.

Accounting Policy

Trade receivables are recognised at fair value, less provision for impairment.

Collectability of trade receivables is reviewed on an ongoing basis. Debts which are known to be uncollectible are written off. A provision for impairment of trade receivables is established when there is objective evidence that AARNet will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 60 days overdue) are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. Cash flows relating to short-term receivables are not discounted if the effect of discounting is immaterial. The amount of the provision is recognised in the Statement of Surplus in Administration - Telecommunications expenses.

The carrying value less impairment provision of trade receivables is assumed to approximate fair value due to the short-term nature of the receivables.

14. CURRENT ASSETS - ACCRUED INCOME

	31 December 2017 $	31 December 2016 $
Current assets		
Infrastructure projects	**49,042**	324,655
Other	**157,391**	470,912
Accrued interest receivable	**390,606**	532,122
	597,039	1,327,689

15. FINANCIAL ASSETS AND INVESTMENTS

AARNet holds financial assets and investments (other than prepayments or trade receivables) including

- Held to maturity investments (see notes 16 and 17)
- Available for sale investments (note 18)
- Derivative financial instruments (shown on the Balance Sheet)

Accounting Policy

Held-to maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that management has the positive intention and ability to hold to maturity. If AARNet were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available-for-sale. Held-to-maturity financial assets are included in non-current assets, except for those with maturities less than 12 months from the end of the reporting period, which are classified as current assets.

At initial recognition, AARNet measures a held-to-maturity investment at fair value plus transaction costs that are directly attributable to the acquisition of the investment. Held-to-maturity investments are subsequently carried at amortised cost using the effective interest method.

If a held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, AARNet may measure impairment on the basis of an instrument's fair value using an observable market price.

Purchases and sales of financial assets are recognised on the date on which AARNet commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and AARNet has transferred substantially all the risks and rewards of ownership.

Available-for-sale financial assets

Available-for-sale financial assets are held at fair value with gains and losses recognised in other revenue. Debt or equity securities that are not held to maturity are recognised as available-for-sale securities. They are included in non-current assets unless the investment matures or management intends to dispose of the investment within 12 months of the end of the reporting period.

At each reporting period, AARNet assesses whether any available-for-sale securities are impaired. Impairment exists if one or more events have occurred which have a negative impact on the security's estimated cash flows which can be reliably estimated.

If available-for-sale financial assets are impaired, the cumulative loss - measured as the difference between the original cost and the current fair value, less any impairment charge previously recognised in the Statement of Surplus - is removed from other revenue and recognised in the Statement of Surplus.

Impairment losses on equity available-for-sale instruments previously recognised in the Statement of Surplus are not reversed in subsequent periods. If the fair value of a debt security which has been impaired increases, due to an event which has occurred after the impairment was recognised, the impairment charge is reversed through the Statement of Surplus.

When securities classified as available-for-sale are sold, the accumulated fair value adjustments recognised in other revenue are reclassified to the Statement of Surplus.

Derivatives and hedging activities

Derivatives are initially recognised at cost on the date a derivative contract is entered into and are subsequently remeasured to their fair value at each reporting date.

AARNet has entered into forward exchange contracts which are economic hedges for foreign currencies to be traded at a future date but do not satisfy the requirements for hedge accounting. Any changes in fair values are taken to the Statement of Surplus immediately.

Fair value measurements

AARNet measures and recognises the following assets and liabilities at fair value on a recurring basis:

- Available-for-sale financial assets; and
- Derivative financial instruments.

AASB 13 Fair Value Measurement requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The following table presents the company's assets and liabilities measured and recognised at fair value at 31 December 2017 and 31 December 2016:

31 December 2017	Level 1 $	Level 2 $	Level 3 $	Total $
Assets				
Available-for-sale financial assets				
Equity securities	**5,901,795**	**-**	**-**	**5,901,795**
Bonds	**6,923,428**	**-**	**-**	**6,923,428**
Total assets	**12,825,223**	**-**	**-**	**12,825,223**
Liabilities				
Derivative financial instruments	**-**	**1,930,536**	**-**	**1,930,536**
Total financial liabilities	**-**	**1,930,536**	**-**	**1,930,536**

31 December 2016	Level 1 $	Level 2 $	Level 3 $	Total $
Assets				
Derivative financial instruments	-	405,788	-	405,788
Available-for-sale financial assets				
Equity securities	5,658,047	-	-	5,658,047
Bonds	5,708,395	-	-	5,708,395
Total assets	11,366,442	405,788	-	11,772,230

The fair value of financial instruments traded in active markets (such as available-for-sale financial assets) are based on quoted market prices at the end of the reporting period. These instruments are included in level 1.

The fair value of financial instruments that are not traded in an active market (such as derivative financial instruments) are determined using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2.

16. CURRENT ASSETS - HELD-TO-MATURITY INVESTMENTS

	31 December 2017 $	31 December 2016 $
Debt securities (fixed and floating rates)	**1,000,000**	2,987,666
Term deposits	**34,500,000**	29,575,000
	35,500,000	32,562,666

17. NON-CURRENT ASSETS - HELD-TO-MATURITY INVESTMENTS

	31 December 2017 $	31 December 2016 $
Debt securities (fixed and floating rates)	**33,237,788**	19,683,045
Term deposits	**-**	4,500,000
	33,237,788	24,183,045

18. NON-CURRENT ASSETS - AVAILABLE-FOR-SALE FINANCIAL ASSETS

	31 December 2017 $	31 December 2016 $
Non-current assets		
Debt securities (fixed and floating rates)	**6,923,428**	5,708,395
Equity securities	**5,901,795**	5,658,047
	12,825,223	11,366,442

19. NON-CURRENT ASSETS - RECEIVABLES

	31 December 2017 $	31 December 2016 $
Prepayments	**-**	212,245

20. NON-CURRENT ASSETS - PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvements $	Office equipment $	Communication assets $	Software $	Total $
At 1 January 2016					
Cost or fair value	2,206,095	5,331,932	126,522,473	1,056,556	135,117,056
Accumulated depreciation	(1,554,602)	(4,256,649)	(49,073,805)	(912,973)	(55,798,029)
Net book amount	651,493	1,075,283	77,448,668	143,583	79,319,027
Year ended 31 December 2016					
Opening net book amount	651,493	1,075,283	77,448,668	143,583	79,319,027
Additions	234,367	538,231	12,741,600	51,209	13,565,407
Disposals	(5,540)	(3,450)	-	-	(8,990)
Additions (financial leases)	-	-	632,981	-	632,981
Disposals (financial leases)	-	-	(632,981)	-	(632,981)
Depreciation charge	(139,143)	(556,798)	(8,998,018)	(87,399)	(9,781,358)
Closing net book amount	741,177	1,053,266	81,192,250	107,393	83,094,086
At 31 December 2016					
Cost or fair value	2,426,981	5,818,235	139,026,289	1,107,765	148,379,270
Accumulated depreciation	(1,685,804)	(4,764,969)	(57,834,039)	(1,000,372)	(65,285,184)
Net book amount	741,177	1,053,266	81,192,250	107,393	83,094,086

	Leasehold improvements $	Office equipment $	Communication assets $	Software $	Total $
Year ended 31 December 2017					
Opening net book amount	741,177	1,053,266	81,192,250	107,393	83,094,086
Additions	100,431	1,854,413	13,574,599	47,250	15,576,693
Depreciation charge	(148,584)	(817,034)	(9,955,384)	(66,391)	(10,987,393)
Closing net book amount	693,024	2,090,645	84,811,465	88,252	87,683,386
At 31 December 2017					
Cost	2,527,412	7,656,237	152,406,631	1,155,015	163,745,295
Accumulated depreciation	(1,834,388)	(5,565,592)	(67,595,166)	(1,066,763)	(76,061,909)
Net book amount	693,024	2,090,645	84,811,465	88,252	87,683,386

Communication Assets- Finance Leases

AARNet provides other parties with rights to use components of AARNet's fibre and other infrastructure in return for that party providing AARNet with similar rights to use components of its fibre and infrastructure.

These arrangements are in the nature of two separate finance leases with each party acting as lessor and lessee. Each lease is treated as settled when both sides of the swap agreement come into force. Consequently, there is no lease finance cost or outstanding lease liability arising in respect of such transactions.

Assets in the course of construction

Included in the carrying amounts of the assets shown above are assets that were in the course of construction as at the end of the reporting period. The relevant amounts are as follows:

	31 December 2017 $	31 December 2016 $
Communication assets	12,729,760	8,938,581
Office equipment	113,616	104,579
Total assets in the course of construction	12,843,376	9,043,160

Accounting Policy

Acquisition

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to AARNet and the cost of the item can be measured reliably.

Fibre and Infrastructure Swaps

AARNet may enter into arrangements granting other parties the right to use AARNet's fibre or infrastructure in return for receiving rights to use fibre or infrastructure owned by the other party ("swaps"). Where such swaps involve significant values of assets, AARNet records an asset disposal in respect of the assets used by the other party at the carrying value of the relevant assets at the time the swap becomes effective. AARNet then recognises an asset of equivalent value, being the right to use the fibre or infrastructure of the other party.

Unincorporated Joint Operations

AARNet accounts for interests in unincorporated joint operations by recognising its share of the assets and liabilities held or owed by the joint operation along with its share of the expenses incurred by the joint operation.

Where the assets held within the joint operation include assets in the course of construction, AARNet's share of those assets is included in the values for assets in the course of construction shown in this note.

Depreciation

Property, plant and equipment is depreciated using the straight-line method to allocate cost, net of residual value, over each item's estimated useful life, as follows:

Leasehold improvements	10 years
Office equipment	3 years
Leased communication assets	5 - 6 years
Leased office equipment	3 years
Communication assets	3 - 20 years
Software	2 - 3 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period; such adjustments may result in a revised useful life shorter than that shown above.

Impairment of Assets

Assets that are subject to depreciation or amortisation are reviewed for indicators of impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. As a not-for-profit entity, value in use is calculated on the basis of the depreciated replacement cost, which represents the current replacement cost of an asset less, where applicable, accumulated depreciation calculated on the basis of such cost to reflect the already consumed or expired future economic benefits of the asset.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). The company has only one cash generating unit.

Gains and Losses

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the Statement of Surplus.

21. NON-CURRENT ASSETS - INDEFEASIBLE RIGHTS TO USE TRAFFIC PATHS (INTANGIBLE ASSETS)

	Total $
At 1 January 2016	
Total payments	143,350,382
Accumulated amortisation on a straight line basis	(73,624,702)
Net book amount	69,725,680
Year ended 31 December 2016	
Opening net book amount	69,725,680
Additions	20,465,200
Amortisation charge	(7,714,721)
Closing net book amount	82,476,159
Total payments	163,815,583
Accumulated amortisation on a straight line basis	(81,339,424)
Net book amount	82,476,159
Year ended 31 December 2017	
Opening net book amount	82,476,159
Additions	192,335
Amortisation charge	(6,921,805)
Closing net book amount	75,746,689
At 31 December 2017	
Cost	164,007,918
Accumulated amortisation	(88,261,229)
Net book amount	75,746,689

AARNet's intangible assets are indefeasible rights to use (IRU) capacity on traffic paths across communication infrastructure owned by other parties.

During the year, additions totalled $192,335. These additions were the result of recognising further payments for Indefeasible Rights to Use traffic paths.

Accounting Policy

The value of each IRU is amortised from the date each right become available for service and will continue to be amortised over the term of the right, which varies from 10 to 28 years. The longest remaining amortisation period is 20 years.

Impairment

IRUs are also subject to impairment review as described in note 20.

22. CONTRIBUTED EQUITY

	2017 Shares	2016 Shares	2017 $	2016 $
Ordinary shares				
Fully paid ordinary shares	78	78	39,039	39,039

Movements in ordinary share capital

Date	Details	Number of shares	$
1 January 2016	Opening balance	78	39,039
31 December 2016	Balance	78	39,039
31 December 2017	Balance	78	39,039

AARNet's shareholders are 38 Australian Universities and the Commonwealth Scientific and Industrial Research Organisation (CSIRO). Each shareholder holds two ordinary shares.

Holders of ordinary shares are entitled to one vote per share on resolutions put before the members. Holders of ordinary shares are not entitled to dividends and have no right to receive any distribution during a winding up.

23. RETAINED EARNINGS AND RESERVE

Retained earnings

Movements in retained earnings were as follows:

	2017 $	2016 $
Balance 1 January	**200,392,241**	179,016,063
Surplus for the year	**15,472,662**	21,376,178
Balance 31 December	**215,864,903**	200,392,241

Reserve - accummulated unrealised gain/loss on investments

Movements in reserve were as follows:

	31 December 2017 $	31 December 2016 $
Balance 1 January	**349,198**	488,034
Changes in the fair value of available-for-sale financial assets	**239,659**	(138,836)
Balance 31 December	**588,857**	349,198

24. FINANCIAL RISK MANAGEMENT

AARNet's activities are exposed to a variety of financial risks including:

a) Market risk (including currency risk, interest rate risk and equity price risk);
b) Credit risk; and
c) Liquidity risk.

This note explains the Company's level of exposure to these risks, how these risks could affect the Company's future financial performance and how AARNet manages the impact of these risks.

AARNet's overall risk management program focuses on managing its liquidity and seeking to minimise potential adverse effects on financial performance. The Board, through the Audit, Finance & Risk Committee, is responsible for setting the overall objectives for risk management and provides specific policies where necessary.

The day to day risk management is carried out by identifying, evaluating and hedging financial risks. This is the responsibility of the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) and they are supported by operating management.

a) Market risk

(i) Currency risk

AARNet operates equipment at international locations and deals with certain suppliers in foreign currencies and is impacted by changes in foreign exchange rates. The Company is primarily exposed to changes in the US dollar (USD) and to a smaller extent, the Euro (EUR). AARNet currently has monthly requirements in excess of USD200,000, for the purchase of international communications capacity and other services. These requirements are expected to increase over time.

Currency risk is measured using sensitivity analyses and cash flow forecasting, summarised below.

Currency risk is managed by holding foreign currency, entering into forward foreign exchange contracts and purchasing options to acquire foreign currency. At year end, AARNet held USD5,807,611 (AUD7,440,980) in USD denominated bank accounts and EUR89,324 (AUD137,100) in a EUR denominated bank account. AARNet's risk management policy is to hedge at least 60% of anticipated short-term cash flows (mainly for the purchase of capacity to the USA) in USD.

The following table summarises the sensitivity of the Company's financial assets and financial liabilities to foreign exchange risk for the year.

		-100 bps		+100 bps	
At 31 December 2017	Carrying amount $	Surplus $	Equity $	Surplus $	Equity $
Cash and cash equivalents	23,566,326	(842,009)	(842,009)	688,916	688,916
Trade Receivables	33,716,530	-	-	-	-
Derivative financial instruments (liabilities)	(1,930,536)	214,504	214,504	(175,503)	(175,503)
Trade payables	(2,855,890)	2,285	2,285	(1,869)	(1,869)

		-100 bps		+100 bps	
At 31 December 2016	Carrying amount $	Surplus $	Equity $	Surplus $	Equity $
Cash and cash equivalents	19,143,901	(283,683)	(283,683)	232,104	232,104
Trade Receivables	37,516,779	-	-	-	-
Derivative financial instruments (assets)	405,789	(45,088)	(45,088)	36,890	36,890
Trade payables	(5,081,764)	69,482	69,482	(56,849)	(56,849)

(a) Market risk (continued)

(ii) Interest rate risk

AARNet's main interest rate risk arises from its cash at bank, cash in deposits and held-to-maturity investments.

The Company's interest rate risk is monitored using sensitivity analysis and is reviewed by management and the company's external investment consultant.

The following table summarises the sensitivity of the Company's financial assets and financial liabilities to interest rate risk for the year.

		-10%		+10%	
		Interest rate risk			
At 31 December 2017	Carrying amount $	Surplus $	Equity $	Surplus $	Equity $
Financial assets					
Cash and cash equivalents	23,566,326	(90,674)	(90,674)	159,882	159,882
Held-to-maturity investments, term deposits	34,500,000	(345,000)	(345,000)	345,000	345,000
Held-to-maturity investments, floating rate notes	34,237,788	(342,378)	(342,378)	342,378	342,378

		-10%		+10%	
		Interest rate risk			
At 31 December 2016	Carrying amount $	Surplus $	Equity $	Surplus $	Equity $
Financial assets					
Cash and cash equivalents	19,143,901	(111,861)	(111,861)	165,908	165,908
Held-to-maturity investments, term deposits	33,425,000	(334,250)	(334,250)	334,250	334,250
Held-to-maturity investments, floating rate notes	22,670,711	(226,707)	(226,707)	226,707	226,707

(iii) Available-for-sale assets (price risk)

AARNet's equity price risk arises from holding available-for-sale assets such as equity instruments, listed bonds and hybrid investments.

Price risk is measured and using sensitivity analysis and is monitored by management and the company's external investment consultant.

The following table summarises the sensitivity of the Company's financial assets and financial liabilities to price risk for the year.

		-1%		+1%	
		Other price risk			
At 31 December 2017	Carrying amount $	Surplus $	Equity $	Surplus $	Equity $
Financial assets					
Available-for-sale financial assets	12,825,223	(128,252)	(128,252)	128,252	128,252

		-1%		+1%	
		Other price risk			
At 31 December 2016	Carrying amount $	Surplus $	Equity $	Surplus $	Equity $
Available-for-sale financial assets	11,366,442	(113,664)	(113,664)	113,664	113,664

b) Credit risk

Credit risk arises where a debtor fails to make contractual payments to AARNet as and when they fall due. AARNet is exposed to credit risk on its holdings of cash and cash equivalents, term deposits, corporate bonds and loan notes, hybrid securities and derivative financial instruments. Further credit risk arises from credit exposures to customers in the form of outstanding receivables and committed transactions.

AARNet's credit risk is mainly managed through the following measures:

Credit risk source	Management
Bank deposits and derivative financial instruments	• Principally deal with highly rated financial institutions.
Investments in hybrid loan notes and bonds	• Bound by an approved investment policy which stipulates minimum ratings or other criteria for investment funds. • Investment decisions based on recommendations from a licensed investment advisor.
Customers	• Assessment of credit quality of the customer, taking into account its financial position, past experience and other factors. • Invoicing in advance for significant portion of income.

c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash to meet the needs of the business. Management monitors AARNet's liquidity and cash and cash equivalents on a rolling forecast expected cash flow basis. This analysis is prepared in Australian Dollars.

AARNet's Board periodically considers longer range financial forecasts (5+ years) provided as part of the normal course of its deliberations. The Board also considers the expenditure commitments disclosed in note 2 when assessing the liquidity of the Company.

25. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies.

Often, this involves estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(i) Useful life of intangible assets

The Director's have assumed in the ordinary course of business that AARNet's customers will continue to use AARNet's services into the forseeable future. The useful economic lives assigned for intangible assets are based on the contractual terms agreed for each Indefeasible Right to Use.

(ii) Useful life of assets

AARNet is the owner of a significant amount of assets and infrastructure. Estimates are made as to the useful life of these assets which can affect the amount of depreciation and amortisation expense during the year.

26. DIRECTORS

The Directors of AARNet Pty Ltd during the financial year were:

Chairman - non-executive
Emeritus Professor Gerard Sutton AO*

Executive Directors
Mr Chris Hancock, CEO

Non-executive Directors
Professor Annabelle Duncan
Dr Christine Burns
Mr Chris Bridge
Dr David Williams
Professor Deborah Terry
Mr Jeff Murray
Mr John Rohan*
Emeritus Professor Mark Wainwright AM*
Mr Robert Fitzpatrick*

*Denotes independent director

27. KEY MANAGEMENT PERSONNEL DISCLOSURES

Key management personnel compensation

The key management personnel are those who had authority and responsibility for planning, directing and controlling the activities of AARNet, directly or indirectly, during the year. The remuneration for key management personnel including directors is as follows:

	31 December 2017 $	31 December 2016 $
Short-term and long-term employee benefits	**2,533,016**	2,356,145
Post-employment benefits	**290,976**	327,489
	2,823,992	2,683,634

Transactions with key management personnel

A director, Emeritus Professor MS Wainwright AM, is Chair of Smart Services CRC Pty Ltd. AARNet owns one share and makes in-kind contributions to this company. Subsequent to year-end, Smart Services CRC Pty Ltd applied for voluntary deregistration.

Several directors (Messrs CM Bridge, J Murray and Dr C Burns) are members of the Council of Australian University Directors of Information Technology (CAUDIT) to which AARNet provides payroll bureau services. AARNet receives no consideration for this service.

During 2017 a Director, Mr Robert Fitzpatrick, provided consulting services to the company in return for remuneration of $54,750.

Other directors represent, act for, or hold offices at certain AARNet's shareholders and customers. AARNet provides services to these shareholders on arm's length terms.

28. REMUNERATION OF AUDITORS

PricewaterhouseCoopers

Audit and other assurance services

	2017 $	2016 $
Audit and other assurance services		
Audit and review of financial statements	**211,000**	208,000
Other assurance services		
Audit of special purpose finance reports	**-**	3,500
Total remuneration for audit and other assurance services	**211,000**	211,500
Taxation services		
Taxation Services	**112,389**	10,165
Other services		
Remuneration for advisory services	**69,030**	115,000
Total remuneration of PricewaterhouseCoopers	**392,419**	336,665

29. OTHER SIGNIFICANT ACCOUNTING POLICIES

New, revised or amending Accounting Standards and Interpretations adopted

AARNet has applied the following standards and amendments for the first time for their annual reporting period commencing 1 January 2017:

- AASB 2016-2 Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107, and
- AASB 2017-2 Amendments to Australian Accounting Standards – Further Annual Improvements 2014-2016 Cycle

The adoption of these amendments did not have any impact on the amounts recognised in prior periods and will also not affect the current or future periods.

AARNet has not early adopted any standards that have been issued but are not yet effective.

Foreign currency translation

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Surplus.

Leases

Leases of property, plant and equipment where AARNet, as lessee, has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's inception at the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in other short-term and long-term payables. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to the Statement of Surplus over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the asset's useful life or over the shorter of the asset's useful life and the lease term if there is no reasonable certainty that AARNet will obtain ownership at the end of the lease term.

AARNet may, as described in note 20, enter into arrangements which are considered off-setting finance leases. Such leases are considered to be settled immediately after coming into effect with the result that no finance cost, or finance income is recognised, and no finance liability or receivable remains outstanding. Assets acquired under such arrangements are depreciated over the shorter of the asset's useful life or the lease term.

Leases in which a significant portion of the risks and rewards of ownership are not transferred to AARNet as lessee are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the Statement of Surplus on a straight-line basis over the period of the lease.

Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of associated GST, unless the GST incurred is not recoverable from the Australian Taxation Office (ATO). In this case it is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables (except accrued expenses) are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the Balance Sheet.

Cash flows are included in the Statement of Cash Flows on a gross basis. The GST component of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

Comparative figures

Comparative figures have been adjusted to conform to the presentation of the financial year, where required.

New Accounting Standards and Interpretations not yet mandatory or early adopted

For the annual reporting period ended 31 December, 2017, Australian Accounting Standards and Interpretations that have recently been issued or amended but are not yet mandatory have not been early adopted by AARNet. AARNet's assessment of the most relevant new or amended Accounting Standards and Interpretations are set out below.

AASB 9 Financial Instruments (AASB 9)

This standard is applicable to annual reporting periods commencing on or after 1 January 2018. The standard replaces all previous versions of AASB 9 and replaces AASB 39 Financial Instruments: Recognition and Measurement. AASB 9 introduces a number of changes with the main changes being:

- new classification and measurement models for financial assets
- new impairment requirements that use an 'expected credit loss' ('ECL') model to recognise an allowance
- new simpler hedge accounting requirements are intended to more closely align the accounting treatment with the risk management activities of the entity.

AARNet will be applying AASB 9 from 1 January 2018.

AARNet (with assistance from engaged advisors) has completed a preliminary assessment on AASB 9 and is currently understanding the financial statement impact of this new standard. The key impact identified to date is the potential broader application of hedge accounting to foreign currency risk management activity for significant asset transactions with foreign currency risk exposure. The application of hedge accounting will align the recognition of the hedge instrument with the asset on the Balance Sheet, with the gain/loss incorporated into the cost of the underlying asset. After reviewing its current foreign currency arrangements AARNet has determined there is no material impact of applying the new hedge accounting rules. AARNet has also determined that the change in measuring impairment loss for its financial assets is not material. As such AARNet has determined there is no significant impact arising from the transition to AASB 9.

AASB 15 Revenue from Contracts with Customers (AASB 15)

This standard is applicable to annual reporting periods commencing on or after 1 January 2018. The standard provides a single standard for revenue recognition. The core principle of the standard is that an entity will recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The concept of control replaces the existing requirements to consider when the 'risks and rewards' pass to the customer as the trigger point to recognise revenue.

AARNet will be applying AASB 15 from 1 January 2018.

AARNet (with assistance from engaged advisors) has completed a preliminary assessment on AASB 15 and is currently understanding the financial statement impact of this new standard. The key impacts identified to date are in respect of the classification of charges for dark fibre and the timing of revenue recognition for establishment fees for fibre tails. The impact of these changes will defer revenue over a longer period of time than under the current standard. The magnitude of the financial impacts on transition and on the comparative financial year is yet to be determined, as a result, at this time AARNet cannot make a reasonable quantitative estimate of the effects of the new standard.

AASB 16 Leases (AASB 16)

This standard is applicable to annual reporting periods commencing on or after 1 January 2019, with an opportunity for early adoption in conjunction with AASB 15. The standard replaces AASB 117 Leases and for lessees will eliminate the classification of operating leases and finance leases. The new standard requires the lessee to recognise its leases in the statement of financial position as an asset (the right to use the leased item) and a liability reflecting future lease payments. Depreciation of the leased asset and interest on lease liability will be recognised over the lease term.

DIRECTORS' DECLARATION

In the Directors' opinion:

(a) the financial statements and notes set out on pages 8 to 25 are in accordance with the Australian Charities and Not-for-profits Commission Act 2012, including:

  (i) complying with Accounting Standards and other mandatory professional reporting requirements, and

  (ii) giving a true and fair view of the entity's financial position as at 31 December 2017 and of its performance for the year ended on that date, and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of Directors.

Emeritus Professor GR Sutton AO
Director

Mr CM Hancock
Director

pwc

Independent auditor's report

To the members of AARNet Pty Ltd

Our opinion

In our opinion:

The accompanying financial report of AARNet Pty Ltd (the Company) is in accordance with Division 60 of the *Australian Charities and Not-for-profits Commission (ACNC) Act 2012*, including:

1. giving a true and fair view of the Company's financial position as at 31 December 2017 and of its financial performance for the year then ended
2. complying with Australian Accounting Standards and Division 60 of the *Australian Charities and Not-for-profits Commission Regulation 2013*.

What we have audited

The financial report comprises:

- the balance sheet as at 31 December 2017
- the statement of changes in equity for the year then ended
- the statement of cash flows for the year then ended
- the statement of surplus for the year then ended
- the notes to the financial statements, which include a summary of significant accounting policies
- the directors' declaration.

Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial report* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Company in accordance with the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

Other information

The directors are responsible for the other information. The other information comprises the information included in the Company's annual report for the year ended 31 December 2017, including the directors' report, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the financial report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and *Australian Charities and Not-for-profits Commission (ACNC) Act 2012* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Company to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/auditors_responsibilities/ar4.pdf. This description forms part of our auditor's report.

PricewaterhouseCoopers

Scott Walsh
Partner

Sydney
23 March 2018

PricewaterhouseCoopers, ABN 52 780 433 757
One International Towers Sydney, Watermans Quay, Barangaroo, GPO BOX 2650, SYDNEY NSW 2001
T: +61 2 8266 0000, F: +61 2 8266 9999, www.pwc.com.au
Level 11, 1PSQ, 169 Macquarie Street, Parramatta NSW 2150, PO Box 1155 Parramatta NSW 2124
T: +61 2 9659 2476, F: +61 2 8266 9999, www.pwc.com.au