



Australian Government
Department of Finance

Jane Halton PSM
Secretary

Our Ref: SEC0011527

Ms Jeanette Radcliffe
Secretary
Senate Standing Committee on Community Affairs
Legislation Committee
PO Box 6100 Parliament House
CANBERRA ACT 2600

Dear Ms Radcliffe

Following the recent Senate Community Affairs Legislation Committee hearing of 13 February 2015 into the *Aboriginal and Torres Strait Islander Amendment (A Stronger Land Account) Bill 2014*, we enclose our supplementary submission providing the additional information requested from the Department of Finance at that hearing.

Following discussions with the Committee Secretariat a revised deadline of Wednesday, 25 February 2015 was granted to my department.

During the committee hearing on 13 February 2015, Senator Siewert requested a copy of legal advice sought by my Department on matters related to the purchase of the Ayers Rock Resort. The Department is not in a position to provide a copy of the legal advice. It is legal advice to the Australian Government and, following established precedent, would not be appropriate to disclose.

Please contact Mr Lembit Suur, First Assistant Secretary, GPMR Taskforce on (02) 6215 3244 if the department can be of further assistance in the committee's inquiry.

Yours sincerely

Jane Halton
Secretary

 February 2015

Department of Finance
Supplementary Submission to the Senate Community Affairs Legislation Committee
on the Aboriginal and Torres Strait Islander Amendment (A Stronger Land
Account) Bill 2014 – February 2015

Executive Summary

The Senate Community Affairs Legislation Committee (the Committee) invited the Department of Finance (Finance) to provide a supplementary submission elaborating further on issues discussed at the hearing. The submission primarily addresses the questions taken on notice, being the provision of additional information regarding the use of the four high level terms in items 11 and 13 of the *Aboriginal and Torres Strait Islander Amendment (A Stronger Land Account) Bill 2014* (the Bill) and provides suggested amendments to items 3 to 7 of the Bill to ensure the total real value of the Land Account is maintained.

High level terms

Sections 11 and 13 of the Bill use the terms “good governance, transparency, financial accountability and ethical procurement”. The Explanatory Memorandum (EM) accompanying the Bill does not define these terms with respect to either section and, in fact, it introduces other terms such as accountability (versus financial accountability).

Accordingly, this supplementary submission addresses the use of the four terms in sections 11 and 13 of the Bill, which of themselves do not enhance stronger governance of the Indigenous Land Corporation (ILC) and, at a statutory level, introduce terms that are indeterminate in their meaning and possibly obscure what is required.

In introducing the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), the Parliament has established a set of common and defined statutory concepts that go to corporate governance, including those required of the ILC Board. It is important to note that the implementation of the PGPA Act has required some additional duties of the ILC Board, as the accountable authority, that were not in existence under the *Commonwealth Authorities and Companies Act 1997*. These relate to the duty to promote the proper use and management of public resources for which the [ILC Board] is responsible (section 15), promoting the financial sustainability [of the ILC] (section 15) and the duty to establish systems of internal control and risk management oversight (section 16). These new duties place higher obligations on Boards. The terms “proper use” and “public resources” are defined in section 8 of the PGPA Act. The other terms have commonly understood meanings in accounting, auditing and financial management practice.

The amendments in the Bill introduce new and additional statutory obligations on the ILC Board by using terms that are not defined in the legislation and do not have commonly understood meanings. It is unclear as to whether these terms complement, inter-relate or override the statutory concepts in the PGPA Act. This is why we say in our earlier submission that these terms “disrupt the coherence” of the current framework.

It is not clear why separate and additional obligations or principles need to be introduced for the ILC Board to have it stand apart from the general obligations of other Commonwealth boards. The two ILC submissions do not explain why these terms have been selected and what they hope to achieve, other than to say that they will “mandate higher and different standards of corporate governance for the ILC”. If the meaning of these terms is unclear, notwithstanding the intention, it is unlikely that their introduction into the Bill will result in higher standards of corporate governance.

At the Committee hearing held on 13 February, members of the Committee asked whether defining the terms would assist in their application. While we have indicated that this would assist, the question remains as to the relevance of the use of the terms,

particularly in the context of how these terms are intended to complement or override the well understood and accepted governance concepts contained within the PGPA Act.

The difficulties in applying these terms are explained individually in more detail below:

Good Governance

The Macquarie Dictionary defines *governance* as “1. government; exercise of authority; control. 2. Method or system of government or management.” The addition of the qualifying adjective “good” does little to help explain what is required of people subject to the use of the term *good governance* in legislation, given that the Macquarie Dictionary definition has 30 possible meanings of “good”.

The term *good governance* is used in different ways by various regulatory bodies. The Australian Securities and Investment Commission (ASIC), the Australian Government’s regulator of Australian companies, addresses the subject of governance for registered companies at (<http://asic.gov.au/regulatory-resources/corporate-governance/>). ASIC states:

“There are many sources of regulatory and best practice guidance on corporate governance, including:

- *the ASX (including the ASX Corporate Governance Council)*
- *the Australian Institute of Company Directors*
- *the Governance Institute of Australia*
- *the Financial Services Council*
- *the Australian Council of Superannuation Investors.*

The judgements of various Australian courts are another important source of guidance on corporate governance – particularly directors’ duties.”

Further examination of the references given above includes:

The ASX, Australia’s principal stock exchange, has a Corporate Governance Council which has (27 March 2014) released a 44 page document entitled *Corporate Governance Principles and Recommendations* (referred to at <http://www.asx.com.au/regulation/corporate-governance-council.htm>). Under Listing Rule 4.10.3, ASX listed entities are required to benchmark their corporate governance practices against the Council’s recommendations and, where they do not conform, to disclose that fact and the reasons why. The rule gives a listed entity the flexibility to adopt alternative corporate governance practices, if its board considers those to be more suitable to its particular circumstances, subject to the requirement for the board to explain its reasons for adopting those alternative practices.

The Australian Institute of Company Directors (AICD), on its web site at <http://www.companydirectors.com.au/Director-Resource-Centre/Governance-and-Director-Issues/Guiding-principles-of-good-governance>, describes its own 10 high level guiding principles of good governance. The introduction to these 10 principles caveats their presentation as follows:

Corporate governance refers to the framework of rules, systems and processes put in place to control and monitor – or “govern” – an organisation. Good governance underpins good conduct and the good judgement of those who are charged with running an organisation. ... It must be acknowledged there is no “one size fits all” good practice solution for effective governance. ... The Guiding Principles are intended to provide companies of all sizes and types with starting point or guide for the development or review of their own corporate governance arrangements, taking into account their particular circumstances.

Transparency

It is not clear what *transparency* means in the context of the Bill. *Transparency* is another high level term that has no specific application as a standard. There are levels of transparency that can apply, therefore the application is necessarily varied in its effect and the simple use of the word does not describe the obligation that the Bill seeks to apply under the *Aboriginal and Torres Strait Islander Act 2005* (ATSI Act).

The PGPA Act, through defined reporting obligations, sets a standard level of transparency expectations that apply to all Commonwealth entities. The ATSI Act also prescribes additional specific reporting requirements on the ILC, as does the *Freedom of Information Act 1982* and the *Work Health and Safety Act 2011*. The application of a principle of transparency, without detailing specific requirements in the Bill or explaining expectations in the Explanatory Memorandum, could arguably enable the ILC and its Board to claim that it meets the transparency principle in the Bill without any changes to its conduct.

Financial Accountability

Financial accountability is another term that is not descriptive of the obligations placed on a Commonwealth entity or an Australian government official beyond a high level concept encompassing a number of possible obligations with respect to resource management.

Financial accountability is not a defined term in the Australian accounting standards, though public accountability and accountability are defined in the Australian Accounting Standards Board glossary. The definition of public accountability is “accountability to those existing and potential resource providers and others external to the entity who make economic decisions but are not in a position to demand reports tailored to meet their particular information needs”. This definition only covers financial statements, which is narrower than their intended meaning under the PGPA Act.

High quality financial statements are seen as integral to good governance and an important analytical tool for assessing financial sustainability (particularly in the public sector), but neither term is formally defined under accounting standards or government finance statistics.

Ethical Procurement

The introduction of a statutory duty to act in accordance with the *principle of ethical procurement* is also problematic because it not a term that has a common meaning and, therefore, could be interpreted inconsistently over time or between decision makers among the ILC Board and its employees.

The Macquarie Dictionary defines two general meanings of *ethical*; the first being “relating or dealing with morals or the principles of morality” and the second being “in accordance with the rules or standards for right conduct or practice, especially the standards of a profession”. The difficulties of understanding precisely what is meant by *ethical* become clear when allied with a particular form of procurement, that of investment. While “ethical investment” is now a more commonly used term, it describes a variety of decisions that are made on grounds of preferences of a group of like-minded investors to be used in purchasing shares. However, not everyone aspires to the same set of ethics, so the rules for purchasing investments vary from fund to fund.

Viewed more narrowly, the Commonwealth Procurement Rules (CPRs) issued under the PGPA Act deal with “ethical behaviour” in the context of Australian Government procurement. The CPRs codify a widely accepted set of rules that require Australian Government employees to behave ethically when undertaking procurements. Ethical

behaviour, the CPRs state, identifies and manages conflicts of interests, and does not make improper use of an individual's position¹.

ILC is currently not subject to the CPRs, but promoting "ethical behaviour" standards that apply broadly to its procurement activities could be easily established by prescribing ILC as a prescribed corporate entity under section 30 of the PGPA rule. Twenty other corporate entities, including CSIRO, ANSTO and the Australian War Memorial are prescribed corporate entities.

If the ILC does not wish to be bound by the standards that relate to the Commonwealth procurement rules, then it is not clear what the Bill is seeking to achieve by using the term "ethical" in the context of procurement. For example, whether it relates to conduct of officials, the considerations they take into account in reaching decisions, or the types of assets that can be procured. On a practical level, the absence of a clear definition of the term *ethical procurement* may pose unintended consequences or risks for the ILC Board if the term were to be interpreted too broadly, too narrowly or inconsistently.

Conclusion

The terms *good governance*, *transparency*, *financial accountability* and *ethical procurement* express high level concepts that have different meanings according to personal interpretation and context. In the context of legislation, we consider these concepts are not sufficiently understood or defined to provide a clear understanding of the statutory obligations that would, as a consequence, be visited upon the ILC or its Board.

The ILC is a corporate Commonwealth entity for purposes of the PGPA Act. It is obligated to follow the resource management framework principles that are imposed by the PGPA Act on all Commonwealth entities (and also Commonwealth companies) and it is not clear how, or if, these concepts or principles in the Bill will improve or complement the ILC's overall governance arrangement.

If the Parliament considers it necessary to set the ILC apart from the general governance standards that apply to Commonwealth entities, as stated in the hearing, Finance has no objection to specific and additional provisions that might strengthen the governance of ILC. However, we do not support provisions that do not strengthen governance, that might conflict with other legislative obligations, do not give clarity to the legislative obligations of ILC, or even detract from clarity by causing confusion.

We respect the statutory independence of the ILC, however, we caution that, with respect to general principles of governance, all Australians have a right to expect consistent behaviour and accountability from the Australian Government as a whole.

For instance, section 17 of the Bill establishes an Audit and Risk Committee membership that is inconsistent with section 17 of the *PGPA Rule 2014*. The Bill restricts the ILC's Audit and Risk Committee membership to members of the ILC Board whereas the PGPA Act, from 1 July 2015, requires a majority of independent members, who can be sourced either from the entity's Board or from outside the entity. The ability to access independent audit committee members from outside the entity itself is considered a valuable assurance process for the Board. This is of particular importance when entities need to manage significant entity risks like those posed by the operations of ARR.

A final point to make is that if we had been approached by ILC, prior to the drafting of this Bill, we would have been able to work through the governance issues and develop arrangements that meet the desired objectives of the Bill.

¹ The CPRs at page 17 identifies some behaviours considered to be ethical in the context of Australian Government procurement activities. The list is not exhaustive however.

Maintaining the real value of the Land Account

As requested by the Committee on 13 February 2015, this further supplementary submission from Finance provides additional information on:

1. the impact of amended additional payment arrangements from the Aboriginal and Torres Strait Land Account (the Land Account), as outlined in the ILC's supplementary submission to the Committee, *Aboriginal and Torres Strait Islander Amendment (A Stronger Land Account) Bill 2014 Submission 1 - Supplementary Submission* (undated);
2. the need for a further amendment to the draft Bill to deliver the intended real growth in the Land Account over time; and
3. the need to amend certain dates in the ILC supplementary submission to ensure the proposed changes are not retrospective.

1. Proposed changes relevant to the Land Account - Replacement of Items 3 to 7 (incorporating the ILC supplementary submission's proposal)

Proposal Provisions

The ILC's supplementary submission to the Committee suggests replacing Items 3 to 7 in the Bill, with the following amendment to the existing legislation (in bold and underlined):

*On the first business day in December in a financial year (the current year) beginning on or after 1 July 2011, an amount is to be paid to the Indigenous Land Corporation, out of the Land Account, if the actual capital value of the Land Account for the current year exceeds the real capital value of the Land Account for the current year. The amount to be paid is an amount equal to **half** the excess.*

Finance Analysis

This amendment would result in half of any amounts in excess of that required to maintain the real value of the Land Account in any year being transferred to the ILC, with the other half retained by the Land Account.

- Assuming the target investment returns are achieved (Consumer Price Index plus 2.6 per cent per annum), this arrangement would be likely to preserve the real capital value of the Land Account as shown in Table 1 attached.

This proposed amendment would mitigate the risk, created in the draft Bill, of an erosion in the real value of the Land Account. It does this by retaining the existing mechanism which specifies that an additional payment to the ILC will only occur if the real capital value of the Land Account is maintained (the 'benchmarking mechanism').

2. The need for a further amendment to the draft Bill to deliver the intended real growth in the Land Account over time

The proposed amendment by the ILC would not result in the Land Account growing over time. This is because there is no mechanism to stop funds retained by the Land Account in one year being paid out in a subsequent year. If the intent is for the Land Account to grow over time, consideration could be given to achieving this with an additional clause, which requires the excess funds retained by the Land Account to be added to the benchmark against which future excess returns are measured. If the provisions of the Bill were changed in this way, then the retained excess plus the existing capital in the Land Account indexed by the indexation factor would become the new benchmark below which no additional payments to the ILC would be made, as indicated in Table 1.

3. The need to remove certain dates in the ILC supplementary submission to ensure the proposed changes are not retrospective

Finance also notes that the alternative arrangements included in the ILC's supplementary submission could be retrospective. This is due to a commencement date of "...on or after 1 July 2011...". In order to prevent this retrospectivity, Finance suggests any revised payment arrangements commence on the first day of the financial year beginning immediately following the enactment of the Bill. Table 1 assumes no retrospectivity.

These suggested amendments would assist in achieving the objectives identified in the Explanatory Memorandum of the Bill, which is to preserve and grow the Land Account's real capital value over time.

TABLE 1

Comparison of Finance proposed and existing additional payments models

Current method	Base Year (\$m)	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14	Year 15
Actual Capital Value (s.193(5))	1995.0	2046.8	2098.1	2150.6	2204.3	2259.4	2315.9	2373.8	2433.2	2494.0	2556.3	2620.2	2685.7	2752.9	2821.7	2892.3
Investment performance	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%
Investment income (assumed)	101.7	104.4	107.0	109.7	112.4	115.2	118.1	121.1	124.1	127.2	130.4	133.6	137.0	140.4	143.9	147.5
Less statutory payment to ILC (s.193 (2))	-49.9	-51.1	-52.4	-53.7	-55.1	-56.5	-57.9	-59.3	-60.8	-62.3	-63.9	-65.5	-67.1	-68.8	-70.5	-72.3
Real Capital Value(s.193(4))	1995.0	2044.9	2096.0	2148.4	2202.1	2257.1	2313.6	2371.4	2430.7	2491.5	2553.7	2617.6	2683.0	2750.1	2818.9	2889.3
Additional payment to ILC (s.193(3))	0.0	-2.0	-2.1	-2.2	-2.2	-2.3	-2.3	-2.4	-2.5	-2.5	-2.6	-2.7	-2.7	-2.8	-2.9	-2.9
Indigenous Land Corporation (ILC) method (as per supplementary submission to the Committee - undated)	Base Year (\$m)	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14	Year 15
Actual Capital Value (s.193(5))	1995.0	2046.8	2099.1	2152.2	2206.3	2261.6	2318.3	2376.3	2435.7	2496.6	2559.0	2623.0	2688.6	2755.8	2824.7	2895.3
Investment performance	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%
Investment income (assumed)	101.7	104.4	107.1	109.8	112.5	115.3	118.2	121.2	124.2	127.3	130.5	133.8	137.1	140.5	144.1	147.7
Less statutory payment to ILC (s.193 (2))	-49.9	-51.1	-52.4	-53.7	-55.1	-56.5	-57.9	-59.3	-60.8	-62.3	-63.9	-65.5	-67.1	-68.8	-70.5	-72.3
Indexation Factor (s.193(5C))	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025
Real Capital Value(s.193(4))	1995.0	2044.9	2096.0	2148.4	2202.1	2257.1	2313.6	2371.4	2430.7	2491.5	2553.7	2617.6	2683.0	2750.1	2818.9	2889.3
Additional payment to ILC (s.193(3))	0.0	-1.0	-1.6	-1.9	-2.1	-2.2	-2.4	-2.4	-2.5	-2.6	-2.7	-2.7	-2.8	-2.9	-2.9	-3.0
Finance method (re-benchmarking)	Base Year (\$m)	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14	Year 15
Actual Capital Value (s.193(5))	1995.0	2046.8	2099.1	2152.7	2207.6	2264.0	2321.8	2381.2	2442.0	2504.4	2568.5	2634.2	2701.6	2770.7	2841.7	2914.4
Investment performance	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%
Investment income (assumed)	101.7	104.4	107.1	109.8	112.6	115.5	118.4	121.4	124.5	127.7	131.0	134.3	137.8	141.3	144.9	148.6
Less statutory payment to ILC (s.193 (2))	-49.9	-51.1	-52.4	-53.7	-55.1	-56.5	-57.9	-59.3	-60.8	-62.3	-63.9	-65.5	-67.1	-68.8	-70.5	-72.3
Indexation Factor (s.193(5C))	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025	1.025
Re-benchmarked real capital value (s.193(4))	1995.0	2044.9	2097.0	2150.5	2205.4	2261.7	2319.4	2378.6	2439.4	2501.7	2565.7	2631.3	2698.5	2767.6	2838.4	2911.0
Additional payment to ILC (s.193(3))	0.0	-1.0	-1.0	-1.1	-1.1	-1.2	-1.2	-1.3	-1.3	-1.4	-1.4	-1.5	-1.5	-1.6	-1.6	-1.7
Difference in real capital value	Base Year (\$m)	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14	Year 15
Real Value of the Land Account - indexed to CPI	1995.0	2044.9	2096.0	2148.4	2202.1	2257.1	2313.6	2371.4	2430.7	2491.5	2553.7	2617.6	2683.0	2750.1	2818.9	2889.3
Current Method - change in real value	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ILC Proposed Method - change in real value	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Finance Proposed Method - change in real value	0.0	0.0	1.0	2.1	3.3	4.5	5.8	7.2	8.7	10.3	11.9	13.7	15.5	17.5	19.5	21.7

Note 1: For illustrative purposes, the statutory payment and the real capital value are indexed to 2.5%, and the rate of return from investments is assumed at the target investment performance of 5.1%.