

SHAREHOLDER MINISTERS

Introduction

- 3.1 Shareholder Ministers, with support from their departments, represent the Government's ownership interests in GBEs. The *1997 Governance Arrangements for Commonwealth Government Business Enterprises* (1997 Governance Arrangements) and the CAC Act outline responsibilities of both Ministers and boards.
- 3.2 Shareholder Ministers are responsible for ensuring that boards receive appropriate policy direction. Boards and management of GBEs, however, have significant independence and autonomy and are free from day-to-day Ministerial oversight in the conduct of their duties.
- 3.3 Some of the key responsibilities of shareholder Ministers include:
 - providing GBEs with their mandate and objectives;
 - proposing changes if necessary to GBE corporate objectives;
 - selecting and removing GBE directors;
 - agreeing with GBE boards on the optimal capital structure, the estimated dividend policy and financial targets of GBEs; and
 - assessing the financial performance of GBEs.
- 3.4 This chapter will examine the joint Ministerial shareholder arrangement which applies to the majority of GBEs. Some groups have suggested that the involvement of portfolio Ministers could lead to conflicts of interest in relation to their industry policy and regulatory responsibilities. The joint

shareholder model will be assessed against alternative shareholder arrangements.

- 3.5 In addition, the chapter will examine the relationship between Ministers and GBE boards. Some groups suggest that there should be a clearer expression of the relationship between Ministers and boards.
- 3.6 The final section of the chapter will examine the effectiveness of the Department of Finance and Administration (DoFA) in scrutinising the performance of GBEs. The skill base and ability of DoFA to conduct this work will be examined.

The existing model for shareholder control

- 3.7 The 1997 Governance Arrangements set out principles relating to the joint Ministerial shareholder arrangements. Under section 1.2, 'the Commonwealth's ownership interest is represented by two "Shareholder Ministers", the portfolio Minister and the Finance Minister.' DoFA indicated that the Minister for Finance and Administration 'generally takes a lead role in GBE financial matters, with the portfolio Minister focusing on operational issues.'¹
- 3.8 The joint Ministerial shareholder model does not apply to some of the more recently established GBEs. The government determined that the Minister for Finance and Administration as the sole shareholder was most appropriate in the cases of the Sydney Airports Corporation Ltd, Essendon Airport Ltd and Employment National Ltd. The ANAO notes that the sole shareholder model was introduced to address a 'perceived conflict of interest as the portfolio Minister is also the regulator or purchaser of services from the company'.² Similarly, DoFA commented that the arrangement 'allows the portfolio Minister to focus primarily on regulatory or industry policy issues, and the Minister for Finance and Administration, as shareholder, to pursue the objective of value maximisation.'³

1 Department of Finance and Administration, *Submission*, p. S29.

2 Australian National Audit Office, *Submission*, p. S9.

3 Department of Finance and Administration, *Submission*, p. S33.

The appropriateness of the joint Ministerial shareholder arrangement

3.9 The inquiry evidence focused on the appropriateness of continuing with the joint Ministerial shareholder model or removing the portfolio Ministers from their shareholder responsibilities and having the Minister for Finance and Administration as sole shareholder. DoFA indicated that there were advantages in both models. In support of the joint shareholder model, DoFA stated:

Although some duplication of effort has arisen from the introduction of the joint shareholder arrangements, having the Minister for Finance and Administration as shareholder has enhanced the balance between the government's regulatory, industry policy and financial perspectives. This has resulted in greater efficiency and effectiveness in GBE oversight.⁴

3.10 DoFA, however, also noted that the sole shareholder model 'also has some advantages, in particular where clarity is required with respect to the government's shareholder objectives and expectations for GBEs.⁵ The Australian Society of Certified Practising Accountants (ASCPA) supported a sole shareholder model commenting that 'corporate governance would be improved further if Ministerial accountabilities were separated.'⁶

3.11 Telstra, in relation to its own corporate objectives, was concerned that at the broad government level there exists a perceived conflict between the government's industry regulatory functions and its share owner interests. Telstra indicated that a sole shareholder arrangement was not a solution to this matter. However, when Telstra was pressed to comment on the administrative merits of a sole versus joint Ministerial shareholder arrangement it commented that 'at an operational level, the one shareholder Minister would bring some streamlining and some operational efficiencies for us and may work more effectively in that sense.'⁷

3.12 Australia Post indicated that the joint Ministerial shareholder arrangements were working effectively. Australia Post suggested that a useful balance has been struck between the Finance Minister focusing on shareholder value and the portfolio Minister, for example, focussing on certain performance standards for community service obligations (CSOs).

4 Department of Finance and Administration, *Submission*, p. S27.

5 Department of Finance and Administration, *Submission*, p. S33.

6 Australian Society of Certified Practising Accountants, *Submission*, p. S95.

7 Mr Graeme Ward, Telstra, *Transcript*, p. 96.

Australia Post, however, acknowledged that 'there can be an appearance of a conflict of interest where a Minister has regulatory responsibilities and also has shareholder responsibilities.'⁸

- 3.13 Department of Communications, Information Technology and the Arts (DoCITA) which is the portfolio shareholder department for both Australia Post and Telstra supported the joint Ministerial shareholder arrangements. DoCITA commented that the system is working well and there is only minimal additional workload placed on Australia Post and Telstra.⁹
- 3.14 The Humphry Report examined the Ministerial shareholder arrangements which applied under the *1993 Accountability and Ministerial Oversight Arrangements for Commonwealth GBEs*. Under these arrangements, the portfolio Minister was the shareholder Minister. The Minister for Finance could, after consulting with the portfolio Minister, request financial information from GBEs. The Humphry Report stated that the 'requirement that the portfolio Minister balance the shareholder interests in GBEs, with the other relationships that the Government has with its GBEs, places that Minister in an extremely difficult position because of the potential for conflicts of interests'.¹⁰
- 3.15 Humphry drew attention to certain areas of potential conflict. The first arises from the tension between the Government's interest in delivering CSOs versus the Government's interest as a shareholder. Under this example, the Government as a contractor of CSOs has an incentive to deliver the CSOs at the lowest cost, while from another perspective the Government has an interest in maximising the rate of return of the entity.¹¹
- 3.16 Humphry suggests a further concern arises with the creation of an 'incentive for portfolio departments to use GBEs to deliver their programs as implicit CSOs'.¹² The creation of implicit CSOs arises from not requiring GBEs to price efficiently or allowing the GBE to cross-subsidise certain consumers. Humphry concluded that this outcome could be seen as an advantage for portfolio agencies but a disadvantage for the Government because it would 'adversely affect the profitability of the GBEs resulting in lower dividend streams and a less valuable asset'.¹³

8 Mr Gerry Ryan, Australia Post, *Transcript*, p. 119.

9 Mr John Neil, Department of Communications, Information Technology and the Arts, *Transcript*, pp. 74–75.

10 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 4.

11 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 17.

12 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 18.

13 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 18.

- 3.17 A further potential conflict arises when a portfolio agency is a major consumer of a GBE's products and services. For example, the Department of Defence is a major consumer of the products and services of its GBEs, Australian Defence Industries and the Defence Housing Authority.¹⁴ Again, in this example, the portfolio agency has an incentive to minimise the cost of goods and services purchased but on the other hand it should be seeking to maximise the rate of return of the entities.
- 3.18 The Productivity Commission (PC) indicated that the former Industry Commission had previously considered the potential for conflicts arising from the role of the portfolio Minister but could not reach a clear preference. The PC reported that potential conflicts could also exist with the Minister for Finance in relation to pricing policy versus dividends.¹⁵
- 3.19 Humphry noted that the financial results of a number of GBEs, during the period of his review, suggested that more emphasis in practice was placed on servicing the need of the portfolio and/or the portfolio's constituency, and less emphasis on GBEs performing efficiently and generating appropriate rates of return. In relation to rates of return on assets, Humphry stated:
- Most GBEs, apart from Telstra and Post in the past few years, have not generated a level of return commensurate with the value of assets invested in the entity and the risks involved.¹⁶
- 3.20 In view of potential conflict issues, Humphry raised the possibility of removing the responsibility for the shareholder function from the portfolio Minister and giving the responsibility to an economic Minister in addition to the Minister for Finance and Administration. Humphry stated that this 'arrangement has considerable merit, however submissions from portfolio departments strongly supported continuation of the portfolio Minister's shareholder role.'¹⁷ One of the reasons for continued involvement of the portfolio Minister relates to the Administrative Arrangements Orders (AAOs) which places GBE enabling legislation under the relevant portfolio Minister.¹⁸
- 3.21 In relation to AAOs, Humphry suggested they 'have given rise to public and Parliamentary expectations that, for example, the Minister for Communications and the Arts be accountable for matters such as Telstra's

14 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 18.

15 Mr Gary Banks, Productivity Commission, *Transcript*, p.139.

16 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 20.

17 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 4.

18 Commonwealth of Australia, Gazette, Special, Administrative Arrangement Order, No. S514, Thursday, 22 October 1998.

universal service obligations and the impact of industry policy on Telstra'.¹⁹ The ANAO stated:

The Administrative Arrangement Order does not discuss the issue of the joint shareholder model. The Order outlines that, where there is enacting legislation for a GBE, then this legislation is the responsibility of the Portfolio Minister. The Administrative Arrangement Order does not explicitly mention the Portfolio Minister's status as shareholder. The Minister for Finance and Administration does not have enacting legislation responsibilities for any GBEs. The only reference in the Order to shareholding responsibilities relates to the Department of Finance and Administration's role to provide advice to the shareholders of Commonwealth GBEs.²⁰

3.22 The ANAO noted some of the dilemmas that Humphry faced in arriving at the joint Ministerial shareholder model and commented that it was 'a pragmatic response to the situation.'²¹ In addition, the ANAO suggested that the role and influence of the Finance Minister was increasing with consequent loss of influence by portfolio Ministers.

3.23 In 1995 the Joint Committee of Public Accounts (JCPA) examined Ministerial oversight arrangements.²² The JCPA's examination showed that there was general support for portfolio Ministers continuing to have GBE shareholder responsibilities. There were two reasons for this conclusion. First, was the view that it was more effective to have communication between a GBE and one department. Second, it was suggested that if the Minister for Finance was the sole shareholder then there would be too much focus on financial issues. For example, the Civil Aviation Authority commented that a 'sole focus on commercial performance might jeopardise its emphasis on safety.'²³ The JCPA stated:

A portfolio Minister brings to his or her responsibility for GBEs a greater understanding of the policy issues relating to the GBEs' operations than would be possible with a single Minister for GBEs or if all GBEs were the responsibility of the Minister for Finance.²⁴

19 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 21.

20 Australian National Audit Office, *Submission*, p. S??.

21 Mr Ian McPhee, Australian National Audit Office, *Transcript*, p. 30.

22 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, AGPS, Canberra, 1995.

23 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 280.

24 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 277.

3.24 The JCPA, in relation to the Ministerial oversight arrangements, concluded that 'the current arrangements for Commonwealth GBEs were working well and appeared to be preferable to any other considered.'²⁵ It is important to note, however, that when the JCPA made this conclusion, the then Department of Finance (DoF) had a significant GBE oversight role. This responsibility derived from *the 1993 Accountability and Ministerial Oversight Arrangements for Commonwealth Government Business Enterprises*. DoF commented that it was already assessing financial performance 'against as consistent a set of criteria as a single agency can hope to achieve internally.'²⁶ The then Industry Commission agreed with this assessment and stated:

By virtue of powers associated with expenditure and control of public moneys, the Minister for Finance also has certain interests in the activities of all Commonwealth GBEs such as dividend policies, returns on investment, finance arrangements and overall commercial viability. In effect, the portfolio Ministers and the Minister for Finance perform the role of shareholder Ministers, having joint responsibility for the commercial performance of GBEs.²⁷

Conclusions

3.25 In 1995 the then Industry Commission (IC) commented that the relationship between government and GBEs is one of the key factors influencing enterprise performance. The Committee agrees with this assessment and that is why the Ministerial oversight arrangements are being revisited in this inquiry.

3.26 In 1995 the Joint Committee of Public Accounts concluded that it was appropriate that portfolio Ministers should continue to have GBE shareholder responsibilities. While the *1993 Accountability and Ministerial Oversight Arrangements for Commonwealth GBEs* did not indicate that the Minister for Finance was a shareholder Minister, the role of the Minister for Finance was significant. The IC suggested that the Minister was in effect a shareholder Minister. The 1997 Governance Arrangements for

25 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 282.

26 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 279.

27 Industry Commission, *Ministerial Oversight of Government Business Enterprises*, Supplementary Submission to the Joint Committee of Public Accounts inquiry into the commercialisation of public sector operations, March 1995, p. 4.

Commonwealth GBEs formerly recognised the Minister for Finance and Administration as a shareholder Minister.

- 3.27 The Commonwealth's ownership interests in its GBEs is represented, in most cases, by two 'Shareholder Ministers', the portfolio Minister and the Minister for Finance and Administration. Three recently formed GBEs namely, Employment National, Sydney Airports Corporation and Essendon Airport have the Minister for Finance and Administration as their sole shareholder. This course was taken to address a perceived conflict of interest in the case that the portfolio Minister has regulatory functions and/or is a purchaser of services from the GBE.
- 3.28 A key consideration during the inquiry was the perceived conflict that exists with the continuation of portfolio Ministers as shareholder Ministers. While Telstra and Australia Post did not report any concerns with the joint shareholder model, both suggested that there were merits in a sole shareholder arrangement.
- 3.29 The Committee notes that the Humphry Report dealt with this issue and, after arguments raised by portfolio departments, took the position of including portfolio Ministers in the joint shareholder model. However, this is no reason to ignore the persuasive arguments that prevail for removing portfolio Ministers from their current GBE shareholder responsibilities.
- 3.30 The potential for conflicts of interest relating to the different roles of portfolio Ministers continues to exist. The Government has recognised this very fact when it chose to have the Minister for Finance and Administration as the sole shareholder for Sydney Airports Corporation, Essendon Airport, and Employment National. In these cases, the Department of Finance and Administration justified the sole shareholder model on the grounds that it would allow portfolio Ministers to focus primarily on regulatory and industry policy issues and the Minister for Finance and Administration, as shareholder, to pursue the objective of value maximisation. On the grounds of consistency, these reasons could be applied to the other GBEs that continue to have their portfolio Minister as shareholder.
- 3.31 For example, there are persuasive reasons why the Minister for Employment Services, as the purchaser of employment services, is not a shareholder Minister for Employment National. On what grounds then does the Minister for Defence, as a consumer of services from the Defence Housing Authority, continue to remain as a shareholder Minister?

- 3.32 In addition, the Committee notes the concerns raised by Humphry relating to the incentive to deliver CSOs at the lowest cost yet also seeking to maximise the rate of return of the entity. The incentive to deliver implicit CSOs was also part of this discussion.
- 3.33 It is essential that the operational settings for GBEs are such that they maximise the efficiency and effectiveness of the entity and help generate appropriate rates of return. As suggested in the evidence, the influence of the portfolio Minister could compromise these objectives.
- 3.34 One of the arguments put to Humphry for the continued inclusion of the portfolio Minister in the shareholder arrangements was the expectations created by the Administrative Arrangement Orders (AAOs). Humphry reported that portfolio departments claimed that the existing AAOs gave rise to public and Parliamentary expectations that, for example, the Minister for Communications and the Arts is responsible for matters such as Telstra's universal service obligations (USOs). The Committee does not consider the AAOs to be an insurmountable obstacle to removing the portfolio Minister from GBE shareholder responsibilities. Again, an issue of consistency arises as the AAOs are not set in concrete and are often the subject of change with the creation of a new Ministry. At the same time, portfolio Ministers would continue to be responsible for policy and regulatory functions where relevant.
- 3.35 The Committee notes that there is a public perception that because GBEs are under government ownership the portfolio Minister can direct GBEs separate from the board and management. For example, Members of Parliament and Senators receive constituency inquiries regarding Telstra services. As Telstra is still under majority government ownership, there is a public perception that the Government has the power to direct it on day-to-day operational matters. This is not the case and the continued involvement of the portfolio Minister as a shareholder Minister may be perpetuating these public perceptions.
- 3.36 In view of these issues, the Committee recommends that all portfolio Ministers be removed from their GBE shareholder responsibilities but remain as the responsible Minister under GBEs' enabling legislation. The Government's shareholder interests in GBEs should be represented by, and be the responsibility of, the Minister for Finance and Administration.

Recommendation 2

- 3.37 **That all portfolio Ministers be removed from their government business enterprise shareholder responsibilities, but remain as the responsible Minister under GBEs' enabling legislation. The Government's shareholder interests in GBEs should be represented by, and be the responsibility of, the Minister for Finance and Administration.**

Ministers and Boards

- 3.38 The relationship between Ministers and boards can influence the efficiency and effectiveness of GBEs. It is generally understood that Ministers exercise strategic control consistent with their accountability to Parliament and the public. Boards, in turn, determine and approve corporate strategy and give guidance to senior management for the day-to-day operations of the entity. However, the separation of responsibilities is not always understood and this confusion can lead to inefficiencies.
- 3.39 The relationship between Ministers, boards and management can be complex. The CAC Act seeks to prescribe certain roles and responsibilities for shareholder Ministers and boards. First, the CAC Act sets out that a responsible Minister or Ministers is responsible for an authority or company.
- 3.40 The relevant sections in the CAC Act which link the duties of directors with the needs of shareholder Ministers include:
- sections 9 and 36²⁸ which require directors to prepare an annual report and give it to the responsible Minister by the deadline for the financial year;
 - sections 16 and 41 which require directors to:
 - ⇒ keep the responsible Minister informed of the operations of the authority and its subsidiaries; and
 - ⇒ give the responsible Minister such reports, documents and information in relation to those operations as the responsible Minister requires;

28 Section 9 refers to Commonwealth Authorities and section 36 refers to Commonwealth Companies. The remaining dot points are divided in this way.

- ⇒ give the Finance Minister such reports, documents and information in relation to those operations as the Finance Minister requires;
 - sections 15 and 40 which require the responsible Ministers to be notified of significant events; and
 - sections 28 and 43 which provides responsible Ministers with the power to notify directors of general government policies which are to apply to the Authority or Company. The responsible Minister is obliged to consult the directors before notifying them of the policies.
- 3.41 The ANAO draws attention to the point that there is no provision in the CAC Act that gives responsible Ministers the 'power of direction in relation to the actual operations of the particular CAC'.²⁹ However, as the ANAO indicates, the power of direction may exist, for example, in an organisation's enabling legislation. For example, section 49 of the *Australian Postal Corporation Act 1989* provides for the Minister to give written directions to the board. In the event of this happening, section 49(3) requires the Minister to table a copy of the direction before each House of Parliament within 15 sitting days. The *Telstra Corporation Act 1991*, under section 9, provides a similar power of Ministerial direction in relation to Telstra. Similarly, in the event that the Minister gives a written direction to the Telstra board, section 9(5) requires the Minister to table the direction in both Houses of Parliament.
- 3.42 The Government's GBE policy arrangements are set out in the 1997 Governance Arrangements. Section 1.3 sets out the guiding principles of the governance arrangements. In particular, this section states that 'shareholder Ministers exercise strategic control consistent with their accountability to the Parliament and the public.'³⁰
- 3.43 As part of exercising strategic control, shareholder Ministers receive a GBE's corporate plan at least once a year. Under section 2.3 of the 1997 Governance Arrangements, shareholder Ministers 'will include (if necessary) proposed changes to the corporate plan to better reflect the Government's policies and objectives for the business.'³¹ Corporate plans, and subsequent updates, are confidential to Ministers, their advisers and Departments.
- 3.44 In addition to the power of Ministers to exercise strategic control of GBEs, there is also the capacity for the Auditor-General to conduct performance

29 Australian National Audit Office, Principles and Better Practices, *Corporate Governance in Commonwealth Authorities and Companies, Discussion Paper*, 1999, p. 9.

30 *Governance Arrangements for Commonwealth Government Business Enterprises, 1997*, pp.2-3.

31 *Governance Arrangements for Commonwealth Government Business Enterprises, 1997*, p.5.

audits of GBEs. Section 16(2) of the *Auditor-General Act 1997* states that the 'Auditor-General may conduct a performance audit of a Commonwealth authority that is a GBE, or any of its subsidiaries, if the responsible Minister, the Finance Minister or the Joint Committee of Public Accounts and Audit requests the audit.'³² Section 17(2) of the Auditor-General Act provides the same power to conduct performance audits in relation to Commonwealth companies. The Auditor-General advised that, to date, he 'has not been requested to undertake a performance audit of a Commonwealth GBE under the provisions of the Auditor-General Act'.³³

- 3.45 In relation to New South Wales (NSW) government entities, the Chief Executive Officer of the Australian Institute of Company Directors, Mr Ian Dunlop, indicated that a critical governance issue is the extent of board power, and whether board responsibilities are adequately defined. Mr Dunlop commented that due to political linkages and structures a 'board is in an unenviable position if it is constrained in what it can and can't do'.³⁴ In a recent press article, the NSW Auditor-General commented that there is still confusion over whether boards or Ministers are running government entities.³⁵
- 3.46 In 1997 the NSW Auditor-General conducted a performance audit into corporate governance in organisations in the NSW public sector.³⁶ The NSW Auditor-General noted that governance relationships are more complicated in the public sector compared to the private sector. This was because the number of individuals and entities involved in decision-making has complicated relationships. More importantly, the NSW Auditor-General noted that 'the roles, responsibilities and accountabilities of each party often have not been clearly defined, either in the organisational/governance model, legislation or in the day-to-day operations.'³⁷ The NSW Auditor-General stated:

The principle underpinning the criteria regarding the relationship between the board, the Minister, CEO and central agencies is that the framework for the board and its decision-making processes should allow the board full and effective control over the

32 *Auditor-General Act 1997*, p. 10.

33 Australian National Audit Office, *Submission*, p. S11.

34 Mr Ian Dunlop, *Australian Financial Review*, Weekend, 8–9 May 1999, p. 28.

35 Mr Tony Harris, NSW Auditor-General, *Australian Financial Review*, Weekend, 8–9 May 1999, p. 28.

36 Audit Office, New South Wales, *Corporate Governance, Performance Audit Report*, Vols, 1–3, June 1997.

37 Audit Office, New South Wales, *Corporate Governance, Performance Audit Report*, Volume One: in principle, June 1997, p. 17.

organisation it is 'governing'. This means that there should be a separation of powers and concomitant responsibilities between the board, the Minister and the CEO. To ensure that these conditions are met, these powers and responsibilities should be set down in legislation.³⁸

3.47 The NSW Auditor-General suggested that the framework for a separation of powers between Ministers and boards should include:

- the Minister's ability to issue direction in regard to a board's activities should be subject to clear limits;
- the Minister should not be able to give directions to the board in terms of the exercise of the board's statutory powers and duties;
- any Ministerial Directions to the board in regard to its activities should be in writing and publicly reported;
- there should be clear and agreed provisions for boards to refuse these Ministerial Directions; and
- where Ministerial Directions are imposed, there should be agreed provisions for boards to seek compensation for implementation of Ministerial Directions.³⁹

3.48 At the Commonwealth level, Mr Richard Humphry addressed issues relating to the relationship between government and GBEs. He drew attention to the tensions that exist in relation to the delivery of CSOs and the government's competing pressures of being both a provider and consumer of goods and services. These issues are discussed in more detail in the next section.

3.49 In evidence to the inquiry, Blake Dawson Waldron (BDW) commented that 'whilst the principles underlying effective corporate governance are increasingly well defined, in practice the various relationships can be complex'.⁴⁰ BDW identified a range of factors which could limit the extent to which boards in the public sector could add value. These include:

- the board's limited role in setting strategic directions;
- the government's ability to control and direct the decision making of many boards;

38 Audit Office, New South Wales, *Corporate Governance, Performance Audit Report*, Volume One: in principle, June 1997, p. 24.

39 Audit Office, New South Wales, *Corporate Governance, Performance Audit Report*, Volume One: in principle, June 1997, p. 24.

40 Blake Dawson Waldron, *Submission*, p. S142.

- blurred roles and responsibilities between Ministers, boards and CEOs for securing organisational performance;
 - the board's lack of power over how its resources are controlled;
 - uncertainty as to the extent to which boards are responsible for the consequences of their decision making;
 - inadequate board power over the appointment and accountability of their chair and CEO; and
 - lack of transparency in board appointment processes.⁴¹
- 3.50 DoFA did not provide detailed information on the relationship between Ministers and boards. DoFA noted that the governance arrangements 'are designed to encourage open communication' between Ministers and boards which 'has facilitated a strengthening of relationships between the parties'.⁴²
- 3.51 In 1995 the Joint Committee of Public Accounts (JCPA) examined Ministerial oversight arrangements.⁴³ The then Department of Finance (DoF) reported to the JCPA that 'it is evident that there has been some misunderstanding by some members of GBEs [boards] about the requirement for consultation on an ongoing basis with responsible Ministers about proposals of a strategic nature'.⁴⁴ In addition, the JCPA cited an academic study which concluded that 'the incorporation of GBEs under the Corporations Law creates an 'uncertain relationship' between Ministers and boards'.⁴⁵ In response to these concerns, DoF, in 1995, stated:
- Guidelines are being developed, in the light of experience to date, to assist directors to better understand their obligations under the GBE accountability arrangements to notify responsible Ministers about significant initiatives which directors propose to undertake. It is proposed that relevant sections in the CAC Bill be used to develop and promulgate the guidelines.⁴⁶

41 Blake Dawson Waldron, *Submission*, pp. S142–143.

42 Department of Finance and Administration, *Submission*, p. S28.

43 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, AGPS, Canberra, 1995.

44 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 159.

45 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 160.

46 Joint Committee of Public Accounts, *Report 336 – Public Business in the Public Interest: An Inquiry into Commercialisation in the Commonwealth Public Sector*, 1995, p. 160.

3.52 The ANAO, in a 1999 better practice guide, discussed the relationship between Parliament, Ministers, boards and CEOs and concluded that:

...there is no common set of principles to guide responsible Minister(s) in their relationship with CAC bodies. There is also little guidance in the CAC Act as to the nature of the relationship between the responsible Minister(s) and a CAC body.⁴⁷

3.53 In view of this finding, the ANAO proposed that the 'functions and powers of the key participants should be defined in the enabling legislation and other governing legislation.'⁴⁸ Alternatively, the ANAO proposed that 'memorandums of understanding of a Board Charter could be agreed to ensure that roles and responsibilities are adequately defined'.⁴⁹

Conclusions

3.54 The public sector corporate governance framework is subject to more complexity than exists in the private sector. This is an outcome of the relationships that exist between Parliament, Ministers, boards and CEOs. In this section, the focus is on the relationship between Ministers and boards. A number of organisations have drawn attention to the fact that there are no principles to guide the relationship between Ministers and boards relating to GBE performance. The NSW Auditor-General suggested that, in NSW, there is still confusion over who is running government entities – Ministers or boards. In view of this, the NSW Auditor-General suggested that a framework should be created to define the separation of powers between Ministers and boards, and that this framework should be set down in legislation. In particular, the NSW Auditor-General proposed that any Ministerial directions to boards in regard to their activities should be in writing and publicly reported.

3.55 The Committee notes that in the event that the Minister gives written directions to the boards of Telstra or Australia Post, then these written directions must be tabled in both Houses of Parliament within 15 sitting days. The power of the Minister to provide written directions to the boards of Telstra and Australia Post and the need to report these

47 Australian National Audit Office, Principles and Better Practices, *Corporate Governance in Commonwealth Authorities and Companies, Discussion Paper*, 1999, p. 9.

48 Australian National Audit Office, Principles and Better Practices, *Corporate Governance in Commonwealth Authorities and Companies, Discussion Paper*, 1999, p. 19.

49 Australian National Audit Office, Principles and Better Practices, *Corporate Governance in Commonwealth Authorities and Companies, Discussion Paper*, 1999, p. 19.

directions to Parliament is set out in section 49 of the *Australian Postal Corporation Act 1989* and in section 9 of the *Telstra Corporation Act 1991*.

- 3.56 In the case that Ministers have the power to direct GBE boards, there is increased accountability and transparency if written directions are made public and subject to scrutiny. The Committee concludes that all GBE boards in their relationship with Ministers should be under a similar arrangement to Australia Post and Telstra. That is, all Ministerial directions to GBE boards should be in writing and publicly reported. Therefore, the Committee recommends that the Minister for Finance and Administration amend the 1997 Governance Arrangements for Commonwealth Government Business Enterprises to include a section that all Ministerial directions to GBE boards should be in writing and tabled in both Houses of Parliament within 15 sitting days.
- 3.57 The Committee emphasises the importance of the existing arrangements whereby Ministers have the power of Ministerial direction in relation to the strategic direction of GBEs and matters in the public interest. At the same time, the Committee supports the increased accountability and transparency that exists through the power of the Auditor-General to conduct performance audits of GBEs. While the Auditor-General, to date, has not been requested to conduct a performance audit of a GBE, this mechanism remains a powerful tool for government and Parliamentary scrutiny of GBEs.

Recommendation 3

- 3.58 **That the Minister for Finance and Administration amend the 1997 Governance Arrangements for Commonwealth Government Business Enterprises to include a section that all Ministerial directions to GBE boards should be in writing and tabled in both Houses of Parliament within 15 sitting days.**

The Department of Finance and Administration and portfolio agencies

- 3.59 The shareholder departments, including DoFA and a range of portfolio agencies, provide their Ministers with research, analysis, advice and recommendations regarding the performance and future directions of their GBEs. The key components of this process include the quality and effectiveness of communication, the skills and expertise of financial analysis of GBEs, and the need for external financial advice.

- 3.60 Analysing the work of and commenting on the future directions of GBEs is a challenging task. The 14 GBEs provide a wide range of goods and services and some operate in challenging and diverse markets. The key question focuses on the ability of a small group of public servants to monitor effectively this diverse range of functions. For example, postal economics and developments in the telecommunications markets are highly complex and dynamic systems. In relation to electricity production, the Snowy Mountains Hydro Electric Authority commented that the product price can be subject to 48 price variations every day. In this case, the risk management involved is complex and it is suggested that only appropriately skilled staff are in a position to grasp the complexities of the market and the industry.
- 3.61 In view of these considerations, the following sections explore aspects of agency performance in monitoring and assessing GBE performance.

Communication

- 3.62 There was no evidence that the communication between GBEs and shareholder departments was ineffective. Employment National reported that communication between itself and the shareholder departments was very effective.⁵⁰ This included regular communication at the management level and twice yearly meetings between the Board and the Minister for Finance and Administration.
- 3.63 Similarly, the Defence Housing Authority reported that it 'has a close working relationship with the Shareholder Ministers and their offices.'⁵¹

Skills and expertise

- 3.64 The Humphry Report recommended that a GBE unit should be established within the Finance Department and be responsible for providing commercially focused advice on GBEs to shareholder Ministers.⁵² This was based on the advice of a number of GBEs and portfolio departments that there is 'a preference for the shareholder relationship to be managed through a single point of contact within the Government.'⁵³ In addition, Humphry commented on the need for financial and economic advice:

50 Mr Rodney Halstead, Employment National, *Transcript*, p. 14.

51 Defence Housing Authority, *Submission*, p. S120.

52 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 22.

53 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 22.

Establishing such a group would have the added advantage of consolidating, in one portfolio, the scarce resources such as economic, financial and industry understanding, that have the capacity of protecting the Commonwealth's interest as shareholder.⁵⁴

3.65 DoFA acted on Humphry's recommendation and created a Commonwealth Shareholder Advisory Unit (CSAU). Staff employed in the CSAU have financial and analytical skills, and have vocational experience in banking, finance, small business, information technology and the public sector.⁵⁵ DoFA stated:

Of the 12 analysts we currently have employed, all have undergraduate degrees in relevant fields such as commerce and accounting, economics or the law; five are certified practising accountants; three have graduate diplomas in applied finance from the Securities Institute of Australia, and we have one master of law in corporate finance. We have five staff members who are currently completing postgraduate studies, and that is encouraged. All staff members are encouraged to take ongoing professional development training.⁵⁶

3.66 DoFA advised that the staffing level in the CSAU will be increased to 16 at the end of September 1999.⁵⁷

3.67 The Department of Communications, Information Technology and the Arts (DoCITA), as the portfolio department for both Australia Post and Telstra, commented that DoFA was professional and providing relevant and effective advice to Ministers.⁵⁸ Medibank Private confirmed that from the questions and analysis undertaken, DoFA seems to 'have the skills and understanding of commercial accounting and financial analysis.'⁵⁹

3.68 As mentioned earlier, the ANAO confirmed that it will be conducting a multi-agency performance audit of *Agencies Monitoring of the Performance of GBEs* during 1999–2000.⁶⁰ In particular, the ANAO noted that DoFA has created a centralised GBE monitoring unit which would be subject to scrutiny as part of the performance audit. The ANAO stated:

54 Humphry, R., *Review of GBE Governance Arrangements*, March 1997, p. 22.

55 Ms Megan Coombs, Department of Finance and Administration, *Transcript*, pp. 90–91.

56 Ms Megan Coombs, Department of Finance and Administration, *Transcript*, pp. 90–91.

57 Ms Megan Coombs, Department of Finance and Administration, *Transcript*, p. 91.

58 Mr John Neil, Department of Communications, Information Technology and the Arts, *Transcript*, p. 79.

59 Mr Michael Whelan, Medibank Private Ltd, *Transcript*, p. 60.

60 Mr Ian McPhee, Australian National Audit Office, *Transcript*, p. 37.

The proposed audit would review agencies' implementation of the 1997 GBE governance arrangements seeking to identify the effectiveness of the new governance arrangements in providing appropriate performance information to the Government and whether the current GBE monitoring system effectively informs Government.⁶¹

External financial advice and independent assessment of GBE corporate plans

3.69 In 1997–98 the Auditor-General conducted a performance audit entitled *Government Business Enterprise Monitoring Practices*.⁶² The ANAO commented that 'portfolio agencies have varying degrees of understanding of such matters as the key economic drivers of individual GBEs, where those GBEs sit in the economic cycle, the maturity of the industry in which they operate and the threats to their future performance'.⁶³ The ANAO noted that, at times, departments have used external advisers to conduct specific reviews.

3.70 In addition, the ANAO reported that the quality of the information that was provided to portfolio agencies in corporate planning information was improving, however there was concern that risk management information was 'still largely unreflected in the information provided to agencies'.⁶⁴ In view of these findings, the ANAO recommended that:

...portfolio departments periodically commission an independent assessment of the corporate plans of GBEs within their portfolio to provide objective assurance to Ministers and the Parliament on an important element of the governance framework.⁶⁵

3.71 This recommendation was agreed to by the then departments of Communications and the Arts, Transport and Regional Development, and the Department of Defence. The recommendation was agreed with qualification by the Treasury and the then Department of Finance.

61 Australian National Audit Office, *Performance Audit Work Program, 1999–2000*, August 1999, p. 85.

62 Australian National Audit Office, *Government Business Enterprise Monitoring Practices, Selected Agencies*, Audit Report No. 2, 1997–98.

63 Australian National Audit Office, *Government Business Enterprise Monitoring Practices, Selected Agencies*, Audit Report No. 2, 1997–98, p. 23.

64 Australian National Audit Office, *Government Business Enterprise Monitoring Practices, Selected Agencies*, Audit Report No. 2, 1997–98, p. 24.

65 Australian National Audit Office, *Government Business Enterprise Monitoring Practices, Selected Agencies*, Audit Report No. 2, 1997–98, p. 24.

- 3.72 The issue of independent assessment of GBE corporate plans was raised in public hearings. DoCITA indicated that it was not aware of any corporate plans being subject to independent assessment, although financial assessment is the responsibility of DoFA.⁶⁶
- 3.73 DoFA indicated that it had commissioned independent assessments on some aspects of GBE performance on a case by case basis. This has included assessments of Australia Post's business drivers, a capital review of Health Services Australia, and capital structure reviews to assess whether GBEs have appropriate debt equity structures. DoFA, however, had not sought independent assessment of any GBE corporate plans.⁶⁷
- 3.74 The Department of Health and Aged Care (DHAC) confirmed that it was not the sole source of advice to Ministers. DHAC determines whether issues are outside its sphere of expertise and, if so, may 'engage one of the top four accounting groups.'⁶⁸
- 3.75 Mr Richard Humphry suggested that there was nothing inappropriate in portfolio agencies seeking independent assessment to test whether a corporate plan is competitive.⁶⁹
- 3.76 Telstra was the most opposed to having its corporate plans subject to independent assessment. Telstra stated:

We would be deeply disturbed by that. Having made the point that a three-year corporate plan is not commercial practice, to have it seen by somebody else in addition to the two ministers is a bit of an anathema to us, I would have to say. We would not welcome such a development, and really it is in the reverse direction from our submission.⁷⁰

66 Mr John Neil, Department of Communications, Information Technology and the Arts, *Transcript*, p. 79.

67 Ms Megan Coombs, Department of Finance and Administration, *Transcript*, p. 90.

68 Mr John Reynolds, Department of Health and Aged Care, *Transcript*, p. 62.

69 Mr Richard Humphry, *Transcript*, p. 111.

70 Mr Graeme Ward, Telstra, *Transcript*, p. 100.

Conclusions

- 3.77 Executive government has a challenging task in scrutinising GBE performance. Shareholder Ministers, with support from their departments, have the responsibility for protecting the Commonwealth's interest as shareholder.
- 3.78 In 1997 Humphry, in recognising the complexity of examining the financial performance of GBEs, recommended that a GBE unit should be established in the Finance Department. The Department of Finance and Administration (DoFA) acted on this advice and created the Commonwealth Shareholder Advisory Unit (CSAU). At September 1999, the CSAU consisted of approximately 16 staff with a range of experience in banking, finance, small business, information technology and the public sector. The Committee commends DoFA for establishing the unit and, based on advice, ensuring that it is staffed with qualified and experienced officers.
- 3.79 The Committee maintains that the CSAU should continue to strive for excellence and be adequately resourced to achieve its primary objective of assisting the Minister for Finance and Administration to protect the Commonwealth's interest as GBE shareholder. The Committee notes that the Australian National Audit Office will be conducting, during 1999–2000, a multi-agency performance audit of *Agencies Monitoring of the Performance of GBEs*. As part of this performance audit, the CSAU will be subject to scrutiny. The CSAU should consider this an opportunity to enhance its processes and confirm its credentials in GBE monitoring. The Committee supports the Auditor-General in initiating this audit, and may, depending on the findings, revisit the issue of agency monitoring of GBEs.
- 3.80 The final issue under consideration is the proposal that portfolio departments commission an independent assessment of GBE corporate plans. This was a recommendation in the Auditor-General's performance audit entitled *Government Business Enterprise Monitoring Practices*, Audit Report No. 2, 1997–98. While certain departments agreed with this recommendation, no department, to date, has sought an independent assessment of its GBEs' corporate plans. On the merits of the proposal, Telstra indicated that it was 'deeply disturbed' by the prospect that its corporate plan would be subject to independent assessment.
- 3.81 The merits of supplementing DoFA's financial scrutiny of corporate plans by seeking independent analysis is weighed against security and treatment of commercially sensitive information. In the case of Telstra, the additional task would be selecting an appropriate organisation that would

have sufficient knowledge of the telecommunications industry to conduct a valid analysis.

- 3.82 In view of some of the concerns by GBEs about independent assessment of their corporate plans, the Committee considers this to be a non-obligatory tool for use by shareholder Ministers. The process for analysing GBE corporate plans should be at the discretion of the Minister for Finance and Administration. At the same time, it is clear that Ministers have a key responsibility to ensure that the Commonwealth's interests are protected while at the same time being held to account by the Parliament.