



COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

Reference: Review of the Auditor-General's Reports 1996-97

CANBERRA

Monday, 3 February 1997

OFFICIAL HANSARD REPORT

CANBERRA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

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Senator Crowley
Senator Mackay
Senator Watson
Senator Woods

Mr Anthony
Mr Beddall
Mr Broadbent
Mr Laurie Ferguson
Mr Fitzgibbon
Mr Georgiou
Mr Griffin
Mrs Stone
Mr Vaile

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Present

Mr Somlyay (Chair)

Senator Gibson	Mr Beddall
Senator Short	Mr Broadbent
	Mr Laurie Ferguson
	Mr Georgiou
	Mrs Stone

The committee met at 11.52 a.m.

Mr Somlyay took the chair.

CHAIR—I will now open today's public hearing, which is the second in a series of quarterly hearings to examine the reports of the Auditor-General tabled in the financial year 1996-97. Today we will be taking evidence on three reports: audit report No. 13, *Tax debt collection*; audit report No. 15, *Management of food provisioning in the Australian Defence Force*; and audit report No. 17, *Workforce planning in the Australian Defence Force*.

I remind you that the hearings today are legal proceedings of the Parliament and warrant the same respect as proceedings of the House itself. The giving of false or misleading evidence is a serious matter and may be regarded as a contempt of Parliament. The evidence given today will be recorded by *Hansard* and will attract parliamentary privilege. I refer any members of the press who are present to a committee statement about the broadcasting of proceedings; in particular, I draw the media's attention to the need to report fairly and accurately the proceedings of the committee. Copies of the committee's statement are available from the secretariat staff present at this meeting.

I now welcome representatives from the Australian National Audit Office and the Australian Taxation Office to the first session of today's hearings.

BARRETT A.M., Mr Patrick Joseph, Auditor-General for Australia, Australian National Audit Office, GPO Box 707, Canberra, Australian Capital Territory 2600

BUTLER, Mr David Edward, First Assistant Commissioner, Small Business Income, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory

CAHILL, Mr Matthew Leo, Audit Manager, Tax/Customs Branch, Performance Audit, Australian National Audit Office, National Circuit, Barton, Australian Capital Territory

GARDNER, Mr Robert Marshall, Director, Debt Collection, Withholding and Indirect Taxes, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory

HIGHFIELD, Mr Richard Francis, Second Commissioner of Taxation, 2 Constitution Avenue, Canberra, Australian Capital Territory

McPHEE, Mr Ian, National Business Director, Performance Audit, Australian National Audit Office, Centenary House, 19 National Circuit, Barton, Australian Capital Territory 2600

MULLIGAN, Mr Rory, National Coordinator, Debt Collection, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory

WHITE, Mr Peter Frank, Executive Director, Tax/Customs Branch, Performance Audit, Australian National Audit Office, National Circuit, Barton, Australian Capital Territory

CHAIR—Thank you. In this first session of today's public hearing, the committee will examine the main issues raised in the Auditor-General's report No. 13. Firstly, I would like to acknowledge the spirit of cooperation which I understand exists between the ATO and the ANAO during this audit. The Auditor-General found there was scope for improvement in the performance of ATO debt collection and that enhancements were needed to ATO debt collection business systems.

The JCPA will take evidence today on the ATO's implementation priorities for enhancement of business systems. We will also examine the ATO on its responsibility to treat tax payers equitably and in accordance with the law. Does the ATO wish to make a brief opening statement to the committee before we proceed to questions?

Mr Highfield—Yes, I would, Mr Chairman. We will just set a bit of context. Debt collection is a major program of the ATO requiring around 1,200 staff, dealing with an inventory of work that moves cyclically between 250,000 and 290,000 cases and

representing around \$4 billion of tax outstanding. To put this in context, the ATO will collect some \$105 billion in 1996-97 from around 10 million tax paying businesses and individuals.

The ANAO's report clearly evidences that over the last five years there has been a downwards trend in the size of the ATO's debt collection inventory relative to the size of the overall revenue base. Notwithstanding that, there have been some improvements. The ATO accepts that there is further scope to improve. The ANAO's report provides a range of recommendations on suggestions to improve debt collection performance and its management. We have responded positively to all of the recommendations and work is already under way, or about to commence, on most of them. We will be reporting direct to the Department of Finance on our progress with the recommendations.

From our perspective the audit was conducted professionally, and progression of its recommendations should appreciably improve the efficiency and effectiveness of the debt collection program. In addition to progressing the audit office's recommendations, we have recently commenced an international benchmarking initiative on debt collection work involving tax authorities in the United States, Canada, the United Kingdom, Japan and New Zealand. We will also be benchmarking these activities shortly against some Australian public and private sector organisations.

However, at a more strategic level, the ATO has concerns that one of the factors that impinges on tax payment compliance and the cost of compliance to taxpayers is the large number of different tax collection mechanisms that we have to separately administer. Each has its own design elements, business rules, separate systems and associated overheads. This issue was highlighted in the report of the Small Business Deregulation Task Force entitled *Time for business*.

With these concerns in mind and with the Treasurer's endorsement, the ATO will be exploring over the next few months a range of ideas covering simpler, less costly and, hopefully, more effective tax collection mechanisms. Thank you.

CHAIR—Thank you. I will invite the audit office to make an opening statement as well.

Mr McPhee—Thank you, Mr Chairman. By way of background, the topic was clearly of interest to the ANAO because of the significant amount of revenue managed by debt collection each year. For example, in 1995-96 over 360,000 cases, involving about \$16.5 billion, were referred to debt collection. The effective collection of these debts is a significant issue for the ATO, taxpayers and, of course, the federal budget.

Within the tax office, the debt collection role is to collect all overdue tax debts as quickly and as effectively as possible. There are over 1,200 tax offices; that is, about seven per cent of the ATO's staff engaged in recovering tax debts from taxpayers who fail

to pay their tax on time. As you would appreciate, the management of the debt recovery process is a complex and sensitive activity involving the maximising of the collection of outstanding revenue while ensuring fair and equitable treatment to debtors.

Tax debt collectors are required to apply a broad array of rules, policies and laws in a number of jurisdictions in addition to assessing the taxpayer's capacity to pay his/her debts. Within this context, the audit examined the key aspects of the debt collection process, including the identification of outstanding debts, the setting of priorities and the management of collection activities. In addition, areas that support this process, including performance information and research activity, were reviewed. Also, as part of the audit, better debt collection practices in the private sector, which were relevant to the tax office's operations, were identified.

I might also note that the audit focused on the collection of tax debts. Therefore, our analysis did not include debts arising in the Child Support Agency. We are about to commence an audit of the Child Support Agency, which will include a review of that agency's debt collection practices.

Overall, the audit found that opportunities exist for more timely, efficient and effective recovery of outstanding debt. This primarily involves the enhancement of business systems to assist the collection of outstanding debts. For example, improving the business systems so that they automatically generate different collection activities based on the identified risks associated with debts is a private sector better practice which will improve the tax office's effectiveness in collecting debts. Such improvements would also effectively increase staff resources available to pursue these outstanding debts where individual attention and expertise would prove most productive.

Further, improving the ability of the business system to automatically impose penalties would be of particular benefit, given that the ANAO found that there is a significant risk that late payment penalties are not being imposed in accordance with the legislation. There is a considerable financial benefit to the Commonwealth in the tax office reducing the in-built delays in the recovery process, particularly the time taken to refer outstanding debt to the debt collection area. The ATO should also improve performance information to enhance its management of recovery activity as well as conduct research into the client profile of debtors and the cost of collection activities. This will ensure that the tax office has the necessary information to select the most cost effective collection practices.

Overall the tax office was very supportive of the audit, including seconding an experienced debt collection officer to join our audit team. The audit office made 29 recommendations which were accepted by the tax office. The audit identified potential for significant financial gain to the Commonwealth that would result from the tax office implementing these recommendations. Our analysis suggests that a combination of minor improvements in the timeliness and effectiveness of debt collection would provide a net

benefit to the Commonwealth of around \$140 million per annum. We consider this estimate of savings each year as conservative.

In my view, Mr Chairman, the value of the report is that it presents a very useful basis on which the tax office can address the key strategic areas for improvement in its debt collection operations. This should result in a substantial ongoing financial benefit to the Commonwealth and better ensure equitable treatment of tax debtors.

In closing, I would also like to mention that, as part of our commitment to adding value to public administration, the office is now considering a financial control and administration audit of accounts receivable across the APS which would have regard to debt collection practices. Peter White and Matt Cahill are the senior audit staff who were involved with the audit, and we are available to respond to your questions. Thank you.

CHAIR—Thank you Mr McPhee. Mr Broadbent, I believe you want to put a question.

Mr BROADBENT—In reading the report, it is very clear to me that the small business sector does not seem to be getting the same net benefit or justice that those who have greater debts do. It has come out of this report that there are no deals for small business and there are deals done for those with higher amounts of debt. What have you done to get some justice and fairness back to the small business debtors?

In the debt collection process, it is a fact that for those with larger debts the remissions are greater than they are for those with smaller debts. The larger the debt, the fewer funds that are going back from that, whereas the smaller debts seem to be paid more quickly by small business. Is there an equity problem here with small business against the rest of the debt collection?

Mr Mulligan—The tax office does not accept that we are treating large business any differently from small business. I will just give you a couple of reasons why.

Mr BROADBENT—Or a large debt or small debt—and am I doing the right thing by transferring that to large business and small business?

Mr Mulligan—We actually give priority to large debts over small debts. There are instances where some of our large debts are based on estimates. We have to take a fair amount of time to contact the taxpayer and ascertain what the exact amount of the debt is. In terms of our collection processes, we use essentially exactly the same practices for large debts as well as medium debts.

For instance, we will be contacting the taxpayer, confirming whether or not that they have in fact made the payment. It could be in the mail for instance, they could have sent us a cheque, or they may be having payment problems. After contacting the taxpayer

we may enter a payment arrangement. The same approach is used irrespective of whether it is a large debt, a small debt, whether it is a large business or a small business or even for an individual.

The techniques that we use are the same for whether it is a large debt or a small debt or a large taxpayer or a medium taxpayer, whether in small business or a sole trader or whatever. Our policies for the collection of debts do not draw any distinction between large businesses and small businesses and also between large debts and small debts.

Obviously, in terms of return of dollars to the revenue, we will give priority to larger debts first as opposed to an insignificant debt. I do not know whether that answers your question, but I think we can flesh it out a bit more if you want some more information.

Mr BROADBENT—I am concerned that the tax office does not have any regard for small business. A phone call from a tax office or an address from small business to the tax office or from the tax office back to the small business frightens the pants off small business, but big business are not too concerned about you. They will deal with you when the time comes.

Mr Mulligan—I think there is probably a difference between whether or not we deal directly with the individual who conducts the business. Obviously, with a large business, their address for service and the like is invariably a firm of accountants or a tax agent or whatever. They have considerable familiarity with working with the tax office, they are aware of our policies and the like. In relation to small business, the biggest problem that we have is that taxpayers do not contact us. We do not in any way act in a draconian manner, although I accept that some people perceive that we do.

If a taxpayer contacts us, we will treat them exactly the same as anybody else. Where we have difficulty is, where taxpayers—and this is particularly prevalent particularly with some small businesses who do not have the confidence of an accounting firm—are reluctant to talk to us. If a taxpayer is having problems with meeting their accounts on time, we are quite willing to enter into payment arrangements and the like.

I think in the last six months we have had something like 65,000 of them. We are not adverse to accepting payment over time. We are also not adverse to remitting additional tax for late payment if the circumstances are such that they meet our policy guidelines. Again—and I keep coming back to this—I am not quite sure where you are coming from.

Mr BROADBENT—It comes back to this after hearing your response. It is clear from the audit report that small business pays all of the debt under legislation, including the fines that are on top of their late payment, but it is negotiated with the bigger firms as to whether they pay all of that fine—whereas the small businesses pay all of it. Is there

not some place for negotiation? There is none under legislation, however, the smaller debts pay all of the fine whereas the larger debts do not necessarily pay all of the fine.

Mr Mulligan—The legislation is the same for all taxpayers—large, medium, small or individuals. In relation to the policy for the remission of additional tax, the policy is also the same. We have just reviewed our policy. We consulted with the private sector, with the accounting and the law societies and the like. The policy is relatively stable and has not had any significant changes for at least five years that I am aware of.

In relation to the application of policy, the tax office has to work with the information that is in front of it. I would suspect that if there is a difference between large and small, it is probably because the large actually ask for a remission of additional tax whereas the small may not be doing so. I am not in a position to confirm whether that is the case. It is just speculation.

The small businesses have exactly the same opportunities for raising the situation if they are having trouble with, for instance, a major client who does not pay their account on time and they are short on cash in order to meet their bills. Our guidelines suggest that they can remit additional tax, in whole or in part, in those circumstances, provided they have taken appropriate arrangements to mitigate the impact of the client not meeting their bill on time. Again, I am not sure where you are coming from.

Mr BROADBENT—Thank you for that answer but is there a case for the tax office to have a better relationship with small business in Australia?

Mr Butler—Generally speaking?

Mr BROADBENT—Yes, in general.

Mr Butler—My area of responsibility in tax is, as I said when I was introducing myself, small business. We have a range of consultative forums where small business people are involved in directions and planning, those sorts of things. The small business deregulation task force, of which the government is yet to respond to, certainly sets an agenda of looking at the way the tax system administers the tax system for small business. Certainly, that is the area of focus for me and the people in my business line in the tax office.

Mr BROADBENT—The fact is that from the report and from other backgrounds that we were looking at investigating, it is very clear that small business feels, and certainly I feel, that big business is getting a better go as far as paying their remissions is concerned than small business is. Perhaps that is one area that has come out of the report from the Audit Office that we should be looking at as a community to making sure there is some fairness and equity in our approach to all businesses.

The guy who misses his group tax and does not pay it till three days later pays a fine. Where there is a major debt, that is negotiated, and that is not fair.

Mr Highfield—There is an additional point that I should make in relation to your first question and that is the fact that most of the debt attributable or applicable to large business is, in fact, subject to dispute. That is subject to dispute because there are legal or technical issues that go behind the nature of that debt where from a taxpayers perspective there may be valid grounds to conclude that the taxpayer took a legitimate course of action, hence the dispute and the lapse of time that will take place until that issue is resolved.

What we find, particularly in our large business area, is that upwards of 80 percent of the debt is subject to that dispute and it well may be in the end if some allowance is made for that dispute, if the taxpayer is found to be correct, then a situation would arise where part of that debt would not attract any late payment penalty. That may be a factor that influences the sort of quantitative observations that are made in the Auditor-General's report.

Mr BROADBENT—Have you the facility to have profiles on your clients? Your clients are nearly the whole of Australia and we have many hundreds of thousands of small businesses and many thousands of large businesses. Has the Australian Tax Office got the ability to distinguish between a one-off late payment that should not deserve a fine and a consistent late payer, or have you not?

Mr Highfield—You will recall that the Audit Office report made quite a reference to the notion of risk profiling and certainly it is within our capability to do that sort of profiling and identify or differentiate between taxpayers in terms of their previous history. I cannot say today that we are systematically doing that in all of our systems because we are simply not. It is one of the recommendations and it is an issue that is getting consideration as we redesign our business systems. Once that is established and implemented it would give us a capacity to differentiate between first time offenders and habitual late payers, which I think was the point of the question.

Mr Butler—And the people in between those two extremes as well.

Mr BROADBENT—I want to know whether you have physically got the ability to make that an order of priority. I daresay that the relationship with your clients would be enhanced if one of your 1,200 officers knew what the background of the particular item was, as we do with social security and other areas of government activity.

Mr Highfield—Our debt collection areas are already structured around client segments and part of our overall approach to risk management would ensure or aim to ensure that those resources are directed to taxpayers that we perceive to be greatest at risk in terms of default on payment. What we need to build now, and this is evident from the

recommendations, are systems that directly support that kind of outcome. I can tell you in relation to the specific recommendations that that is one area that is getting attention already from a research viewpoint with a view to establishing profiling mechanisms.

Mr BROADBENT—The dollars that we are talking about here—

Mr Mulligan—Until about a year ago, our COMPACT system, which is our debt collection system, recorded payment details for a period of about 15 months. About a year ago we changed the parameters so we can now record payment history details for a period of three years. That will give us a much greater amount of data which we can analyse as part of the work which Mr Highfield mentioned a couple of moments ago. Currently this data is still being accumulated because we are now only 27 months into a 36-month maximum term. We will have that data for a period of three years shortly which will enable us to make our research much more authoritative and stronger than it currently is.

Mr BROADBENT—I asked you the question as a point of equity as well. If I am paying my tax and somebody else is not paying theirs it is, again, unfair on the small business as against larger business. One general question: you have approximately 1,200 officers that are involved in debt collection as the report says. Do you dedicate those 1,200 officers to debt collection or are they pulled off to do other work at different times?

Mr Butler—Essentially they are dedicated to debt collection. Generally speaking, each business line has its own debt collection area and they are staff who are actually on that full time. I say essentially because there might be a particular branch office where, if the inquiry counter got particularly busy on a day for whatever reason, they might for an hour or so help out on the inquiry counter. But their job is primarily debt collection and that is what they are focused on.

Mr BROADBENT—Do you agree that the report says that they are not benchmarked against private industry or international best practice?

Mr Mulligan—We are in the process of doing that now, Mr Chairman. As Mr Highfield mentioned before, we are doing international benchmarking against five other revenue authorities around the world. We are about to start doing the domestic benchmarking in the next couple of weeks. Going back to the point you made before about whether they are engaged full-time, in our withholding tax arena the debt collection staff are part of a multifunctional team. If I can just pick an arbitrary figure of 100 for the purpose of discussion, debt collection may have 100 normal staff allocated to these debt collection teams. They would not be doing debt collection work only. But on the other hand, the other members of the client service teams would also be doing debt collection work so there is the equivalent of 100 staff members who are doing that work.

In the other two areas which Mr Butler referred to before—small business and individuals—the staff are dedicated on debt collection work only.

Mr BROADBENT—There is a view in the community from small business that they do not get a fair go as against big business. I am sure you are well aware of that. Actually this report points out a few places where that may be the case. I would like to think that the Australian Tax Office addresses itself to that issue and says, ‘Look, are we being fair overall?’. I know you have your processes; I know you would agree that you try to treat everybody the same way but it is the outcomes that we are looking for here, not necessarily the rules that are in place.

CHAIR—The committee recognises that your job is to collect the revenue. Did I hear correctly; did you say that 60,000 requests for repayment schedules were approved by the ATO?

Mr Mulligan—In the first six months of this year I think we have had roughly 60,000 payment arrangements. In other words people will pay their debts over time with the full agreement from the Tax Office.

CHAIR—How many requests for repayment schedules were refused?

Mr Mulligan—We do not record information for that long.

CHAIR—As local members and senators we do not see those people who successfully make arrangements. We only see those people who have problems. You mentioned the word ‘policy’ a number of times. Could you outline for the committee the ATO’s policy with regard to small businesses who get into difficulties in hard times when they are not getting money owed to them and they cannot pay their tax. What is the attitude of the ATO in making arrangements with those people to pay their tax? Or do they just close them down and bankrupt them and that means that other people down the line do not get paid? Have you ever made a study of what the result is to revenue of the chain reaction?

Mr Butler—With small business, we certainly are not trying to put people out of business. We would like to see small businesses exist and grow. Our approaches are to really look for ways of finding common ground—and Mr Mulligan can go into some more detail if you wish—but to find common ground where a tax liability can be met over a period of time. To take action to liquidate a company or to bankrupt a small businessperson would be, in our view, a fairly extreme step to take. It would be a last resort. We would do our best to balance the need to collect the revenue that we have to collect against the desire to see a small business continue in business, making sure that payments are met within an appropriate period of time. We would find that balance to help small business continue to exist, yet still collecting the revenue that is payable. As I said, we would see things like liquidation and bankruptcy as really last resorts—‘all else has failed’ type actions.

CHAIR—Are your branch officers aware of that?

Mr Butler—Oh, most definitely, yes.

CHAIR—Everyone of us sitting here has had instances, and mine as recently as three or four weeks ago, when a taxpayer offered a repayment schedule to the office to pay it by the end of January and could not get through on the telephone. Tax did not want to talk to that person. What you are saying is admirable but it is not being applied in practice.

Mr Butler—We handle approximately 300,000 cases per year in the debt collection area nationally. We would like to think we get it right in most of those cases but certainly where people are aggrieved by a particular decision we are only too happy to revisit that. I am sorry to hear that that sort of thing happened. From what you said it certainly seems a reasonable outcome to pay a debt off by the end of January, not knowing the history of the case. But certainly we are not here to shut people off; we are here to try to find ways of reaching that common ground.

CHAIR—But the importance for the ATO is that if a debt can be recovered by a person being given time to pay it back, then there is a chance the ATO will protect the revenue—that you might get paid.

Mr Butler—Certainly.

CHAIR—If you bankrupt that business nobody gets anything.

Mr Highfield—As Mr Mulligan said, our first recourse is always to consider the taxpayer's financial circumstances and capacity to pay. We have already negotiated 60,000 payment agreements in the first six months of this financial year from taxpayers who have come forward and we have been able to negotiate particular arrangements.

CHAIR—But you cannot tell me how many you refused.

Mr Highfield—According to Mr Mulligan those statistics are not available but that is not to say they may not be kept. There may well be some taxpayers who, simply because of a very poor payment history, we have difficulty in negotiating payment arrangements with. In the past they may have failed to honour agreements. I am not suggesting that your client was in that particular situation but I would be surprised—and it would really be against administrative approaches—if we just outright refused a payment arrangement which was no more than four weeks for a debt for a taxpayer who did not have a prior history that concerned us.

CHAIR—Bear in mind I prefaced my question by the statement that it was your job to protect the revenue so I do acknowledge that.

Mr Mulligan—If I could just add something to what Mr Highfield just said, the

statistics that I have show that we have finalised roughly 56,000 payment arrangements and we currently have 73,000 in place at the end of December. We are not averse to entering into these payment arrangements.

CHAIR—We do not see the good ones.

Mr Mulligan—I accept that.

CHAIR—Nobody rings me up and says they have not got a problem and they are well.

Mrs STONE—I have other examples which mirror Mr Somlyay's almost exactly: people about to be bankrupt and about to be sold up. We rescued them in the last 24 hours before they were to leave their businesses and walk out, with no history of failure to pay tax before.

Mr Mulligan—It is obviously very awkward to talk about these cases without knowing the identity of the taxpayer. We are extremely loathe to bankrupt people. We do not actually keep statistics of people who we put into liquidation or bankruptcy. We have only stats of those taxpayers who are in liquidation or are bankrupt—not who caused it to occur. But I know anecdotally that the number of taxpayers we place in liquidation or in bankruptcy has been declining for about five or six years. It is, as the Chairman has correctly stated, a counterproductive approach if there is any avenue open for the taxpayer to trade their way out.

We have not done any studies, in answer to your question before, about the flow-on effect to other areas of the community or the employment prospects in an industry. We are very loathe to putting people into bankruptcy. Whether we like it or not, we have a lifelong relationship with taxpayers, unlike in the private sector where you can decline to trade with somebody. They will be paying tax all their lives. It is pointless for us to penalise or punish someone. We are here to try to encourage compliance.

In a lot of cases where we actually make people bankrupt, they have not spoken to us at all. You would be surprised at the number of taxpayers who will not talk to us for any reason at all. They will virtually wait until the door of the court before they will make an approach and put their financial situation on the table.

So the message I hope I am conveying to the committee is that if your constituents are having this problem they should talk to us. The vast majority of people we have trouble with about debt collection are those who will not talk to us.

CHAIR—Their tax agents ring us and say that you will not answer the phone, that they cannot get hold of tax and that tax has made up its mind to go through with the prosecution and that is it.

Senator GIBSON—Mr Highfield, in your introduction you mentioned 250,000 to 290,000 cases and I think debts of \$4 billion to \$5 billion. How do you reconcile that with the number in the audit report, which is \$16 billion? What is the explanation?

Mr Highfield—If you refer to page 57 of the audit report, the \$16 billion-odd refers to the value of cases that are referred during a year for debt collection action. The figure of \$4 billion broadly approximates to the net amount of tax that is outstanding at any point in time.

Senator GIBSON—I have been talking to a few people in the professional debt collection business and they have told me that within their industry the Tax Office for the last five or six years has been regarded as a bit of a joke. To give evidence of that—this is the reputation in the industry—they said that, first, the Tax Office does not chase arrears and, second, it is not using the courts, whereas in the normal debt collection business probably about one-third of all cases end up in the courts with a writ or some order being issued. Is this true?

Mr Highfield—The statistics are in the report. The evidence is there of the number of cases and the amount of tax outstanding relative to the revenue base. If all of those things were true, in my view you would see a lot more cases outstanding and a lot more tax outstanding. The reality is that, over the six years detailed in the report, there has been a downward trend in the number of cases—that is quite evident—and the amount of tax outstanding has stabilised around \$4 billion.

You said we do not go to court; we just quoted to you the fact that we enter into payment arrangements with a lot of our clients. There are other situations where we have to enter into perhaps garnishee actions through a pay-as-you-earn employer because we are having difficulty in getting the debt. In the area of personal taxpayers, non payment of debt for income earned by unemployed taxpayers is high in terms of numbers of cases but low in terms of relative debt. Nevertheless, it forms part of our workload. So there is a variety of those situations.

I suspect also that the private sector would welcome an opportunity to do some of this work, so it will make certain observations to you. I have, in fact, had discussions with one firm of debt collectors to get a feel for the sorts of services they offer. It may well be that into the future we, from the viewpoint of testing the productivity and effectiveness of our own programs, test our performance against what external collection agents provide.

Senator GIBSON—So you have not run any trials yet, but you are thinking about doing so?

Mr Highfield—No, not yet. I am aware of one revenue authority overseas that is running a trial at the moment.

Senator GIBSON—Given the criticism in the report about your business systems not being up to scratch, it would seem to me that, in the short term, making arrangements particularly for chasing the smaller end of the debt cases may be a sensible way to go.

Mr Highfield—It is something to consider, but there are privacy issues that you would need to take into account. It is a bit of a fine line to explore before you go down the track of saying, ‘We will outsource some of this particular work.’ We cannot action all the cases we have at any one point in time and there are delays in actioning some cases. That is simply because of the size of the inventory. What I would say is that, with adoption of the recommendations in this report, I would think we could make further inroads into that inventory.

Senator GIBSON—To go back to past perceptions of your performance in the debt collection business, I had heard stories from within that industry that apparently there had been a directive from the tax office with regard to debt collection, dating from around 1989 or 1990, that basically said to not go too hard on debtors—to negotiate with them and accept any offers made from the debtor—and that that has only been changed in recent times. Is that fair comment?

Mr Mulligan—I am not aware of that directive. If it is around, it is—

Mr Butler—Superseded! Certainly, it is a balance between collecting the money that is due to be paid, trying to keep people in business and not being seen to be too soft. It is really a juggling act, in many ways, to manage this part of the program.

Mr Mulligan—We do not issue directives to go easy of debtors for the simple reason that it is not our money. It is the parliament’s money. It is the first I have heard of that, Senator, so you have caught me a bit on the hop. In terms of your comments before about legal action, we are reluctant to initiate legal action. It is a very cost-inefficient way of collecting money. There are obviously filing fees and the like; the debt that we will collect is still going to be the same, irrespective of whether we incurred that money. If the person goes bankrupt, which may be the ultimate course if that is the appropriate outcome for that case, historically our dividend from bankruptcy is one or two cents in the dollar. Legal action is our last resort.

I am aware that, historically, we did do a lot more legal activity. But, as Mr Highfield mentioned, we are still reducing the amount of debt and cases without using that particular activity. The way we are going about it—and I quoted the statistics before—is that we are going into the payment arrangements; we are using exactly the same techniques as the private sector. I should mention that if it is a case where legal action is appropriate, and bankruptcy or liquidation is appropriate, then we will do it. We do not win too many friends by doing it, for fairly obvious reasons, but the facts speak for themselves in a lot of cases.

Mrs STONE—The Auditor's report found that the finance delegations for writing off irrecoverable revenue at the ASO4 level, which is a fairly junior level, range from no ability to do that to \$250,000 in different branches. That raises a number of issues on the variation of responsibility between people at the same public sector level. It also is a concern to us that you do in fact review each of those remissions that are made by officers. Do you ensure that they are made strictly according to a policy? Do you analyse them at law? What we are saying is: if some ASO has chosen to write off \$250,000 worth of debt owed, is it ever a case that you are concerned about the legality of that action? And what is the reason for that variation? Is it something to do with where the officers are located? There are a number of questions there but, in particular, we are concerned at the extent that you review those levels of delegation. Can you assure us that each of those delegations made at that level are strictly according to the laws?

Mr Highfield—Just broadly—and I will hand over to my colleagues—I share your concern about inconsistent allegations. My understanding is that there is a major project to bring those into line. There is no valid reason, in my view, to have different delegations between different regions. I can only assume that for some local purposes, which I cannot explain here to you today, for some reason different officers have somehow moved to vary those delegations. My understanding is—and Mr Mulligan can confirm this—that we are implementing consistent delegations across the country. In relation to the review of the application of those delegations, I think you could provide the answer as well.

Mr Mulligan—The differences arose when the Australian Taxation Office split its debt collection area from one unit into three or four and the positions moved from one central unit—and I use that term for ease of discussion—into four separate units. When the positions went, there were different powers given to different people and there was a rationalisation. It was recognised coincidentally, during the course of the audit, that there were discrepancies and all of those discrepancies have been removed in a revised delegation that was signed by the Minister for Finance late last year.

In terms of how we go about debt collection, writing off outstanding debts which are uncollectable: the approach is—and this is consistent Australia wide—that the action officer will prepare a report. It is then reviewed by another officer at a more senior level, normally at the manager level, who will approve the write-off. The write-off is then actioned and appropriate documentation is kept. This is an area which is part of the annual internal audit cycle. Not all write-offs are checked for fairly obvious reasons, given the volume, but a sample of them are checked by our internal audit area in every office around Australia—that is my understanding.

So there are appropriate schedules kept, there are procedures that everyone has to follow and the policy in relation to write-offs was also refined and brought together into one document as part of the policy manual review last year. As I see it, the policy has been ratified and consolidated into the one document, the procedures are consistent and have been for a number of years about checking internally and then checking by internal

audit area and our procedural documentation has been reviewed as well.

Mrs STONE—And you have never found any inconsistencies in those write-offs, say, up to \$250,000 where you have been concerned with why a write-off has been given?

Mr Mulligan—It has to be, as I said, vetted by the manager.

Mrs STONE—So that is where your check comes in: the manager within the office would approve—

Mr Mulligan—It is a multi-tiered check. You have got the manager who has to vet. The managers are at a much more senior level—ASO6 level—and they vet all write-offs in their particular section and, unless they sign it off as being appropriate, it does not get actioned.

Mrs STONE—Okay. Perhaps you have changed lately, but when the audit was done, there was a generic prompt sent out to those in arrears with their taxation and you are moving, I understand, towards sending out a more flexible or targeted debt reminder statement. Now that presumably will require more staff effort, more time. How are you going to cope with that, given that at the coalface you have a lot of junior officers who are the bane of our lives as constituent representatives?

Our complaint from our members is that they cannot get through on the phone lines, there is a different person every time they ring, the staff turn over very quickly, often they cannot get detailed answers—even when their accountants make approaches on their behalf, they get a very, very difficult time at that local office. So my concern is: if you are going to go away from generic instruments towards something more specific, more targeted, how are you going to do that within your current staff resources?

Mr Highfield—Most of these are computer assisted, so the generic advice that we issue at the moment is done entirely by computer process and there is no human intervention in the actual production of that notice.

You might recall that, in relation to an earlier question, I said that as part of our work around risk profiling, we would be enhancing the computer systems to better differentiate between different taxpayers and their history, and taking those factors into account in terms of deciding what type of letter we send to the taxpayer. Again, our approach to doing that would be one of building computer systems that would support that sort of decision making and the generation of letters to taxpayers based on that information that we have, So we would be largely computerised.

Mrs STONE—But you still have to have more people to input that data, don't you?

Mr Highfield—No, the data would not be input. The data is captured as part of our normal administrative processes. We can establish, for example, histories about taxpayers' payment compliance simply by looking at what has happened in the past and recording particular flags or indicators on records.

Mrs STONE—So you are interrogating your own data, in fact, about the cases that are in debt?

Mr Highfield—Yes.

Mrs STONE—At the moment, it takes between 17 and 68 days to get a debt collection notice. With your new systems, do you expect to bring that down to a consistent benchmark of, say, what number of days before people get a debt collection notice?

Mr Highfield—In terms of days, we generally focus on larger debts. First of all, the audit identified that we should advise and approach taxpayers sooner than what we currently are doing anyway. So, as a general rule, I would envisage a bringing forward of the point in time at which we make our first contact with taxpayers. That contact, or the timing of it, would be dependent, I would think, on the size of the debt because, generally, when you send out a notice, it initiates a response from the taxpayer or you are expected to make some intervention with the taxpayer.

Simply in terms of the numbers at different times of the year, you cannot do all of that at the same point in time so you stagger your advices to taxpayers and you spread your work. But we would focus on the larger debts. What I am suggesting is, in line with the sorts of recommendations in the report: a general move for earlier contact, but differentiating our actions based on what we know about the taxpayer, which we can automatically take account of in that first contact process.

Mr Butler—I would add, too, that there will be cases where we do not know the current location of a particular person and it might take us some time to find the person to send the notice out—and that could add to the delays from time to time.

Senator SHORT—On the point about computerisation—I think we talked about this in a different capacity a few months ago—as I understand it, there has been little scope for the computer system to take account of the question of whether it is a first offence, a minor offence or whether it has been a multiple offender in the actual notification that you send out to the taxpayer?

Mr Highfield—I think I have responded along those lines in earlier answers today, Senator. But I also said that, in terms of moving forward on the recommendations in here, we would be building into our advice processes an ability to differentiate and take into account—

Senator SHORT—How far down the track are you on that?

Mr Highfield—We are actually doing the research within the different client segments at the moment to identify the factors that we should take into account. Mr Mulligan, earlier on, mentioned the fact that we are now storing more payment information and history. We are looking at what other factors we should take into account: for example, whether a taxpayer is in business or not; what sort of income they receive; is it subject to collection at source? So there are a range of factors that you can take into account, not just one. Even the age of the taxpayer or the sex of the taxpayer could be relevant to the advice that you take.

So what we are doing at the moment is the research to identify those attributes that you may want to take into account in a profiling system. That work is under way at the moment. And, because we also have moving in parallel with that at the moment a major systems redevelopment of our income tax system for which there are a number of releases planned in the latter half of 1997 and in early 1998 we would expect that our work in the area of risk profiling could be factored, in part, into that modernisation activity.

Senator SHORT—I want to go back to a point that I think Mr McPhee pointed out, that seven per cent of the total staff of the ATO is in the area of debt collection. How does that compare with past years? Have you gone up or down as a proportion?

Mr Highfield—I suspect that in the early 1990s—I would have to check this out—there would have been a numerical decline but around 1994-95 there was a new deficit reduction strategy which saw us change the work of some of our staff and put more staff on to debt collection work. There would have been an increase around that period, and most of that would be there now. There have been, as you know, ongoing efficiency dividends which we are obligated to meet. That is about all I can point to in terms of general numbers. Twelve hundred, which is the figure being quoted here both by us and the Audit Office, would represent a slight increase on what we had in the early 1990s.

Mr Butler—Some of that shift was as a result of doing things better in other areas to allow staff to move across to debt collection. We certainly see it as an important area.

Senator SHORT—Yes. This 1,200 is a bit higher than you had in the early 1990s but your total numbers have come down, haven't they ?

Mr Butler—Yes.

Senator SHORT—So that would mean that the proportion of your total staff engaged in debt collection would have risen?

Mr Butler—Yes.

Senator SHORT—You said you were doing some bench marking now in this area. Do you know, at this stage, how that seven per cent compares with other countries?

Mr Highfield—No. We are just in the information gathering stage at the moment. We have just made our first formal contacts over the last few weeks with those revenue authorities. That information gathering will occur over the next few months so it would be probably three or four months before we had that basic information about debt collection programs of other revenue authorities.

Mr Butler—From past experience, we just need to be cautious too and make sure we compare apples with apples when we do those international comparisons because other revenue authorities may call people different things and structure themselves differently.

Senator SHORT—Thanks.

CHAIR—How does the Tax Office treat moneys owing in terms of revenue forecasts?

Mr Highfield—The general revenue estimating process basically starts from an historical basis. That is, you look at what you have achieved at a particular point in time. In terms of looking forward, you then have to make allowance for projections of economic activity, the impact of changes in legislation—

CHAIR—Who does that, you or Treasury?

Mr Highfield—Treasury has primary carriage for the Commonwealth budget revenue forecasts. However, on the ground the process is one where the ATO and Treasury work closely together. We provide, I guess, a more practical viewpoint of what is happening on the ground that may be relevant to the forecasting activity. But in terms of the actual forecasting activity you have an historical base; you have economic parameters; you have to take account of the likely impacts of legislation; you have to take into account the likely impacts of changes in administrative procedures; you have to take into account the likely impact of new compliance activities; you have to take into account, potentially, any changes in compliance behaviour; and, based on last week's events, you have to take into account what may be happening in the external world on tax planning matters.

All of those factors, from my experience, are not subject to precise quantitative processes and there is an element of judgment that has to be exercised when formulating the estimates. As I said, we do that process in conjunction with Treasury. There is a major process pre-budget and there is a mid-year review activity which occurs in December-January each year, and we use those processes to arrive at estimates of the revenue.

CHAIR—You mentioned a deficit reduction program in 1994 and increasing the debt collection staff. Did it work?

Mr Highfield—From the evidence that we were able to gather we were able to demonstrate there was a positive revenue impact. That would have been factored into the budget forecast, but we are talking about \$100 million, or \$200 million in a revenue pool of about \$96 billion.

CHAIR—Are we not talking about \$16 billion outstanding debt at any one time?

Mr Highfield—Over a period of a year. At any point in time the net value of debt outstanding is around \$4 billion, some of which is in dispute, some is subject to litigation, bankruptcy, or insolvency action. A fair proportion is subject to payment arrangements.

Mrs STONE—We have had delegations telling us of writing off debt cases, and so on. I am interested in whether you have got a standard set of criteria for determining what is uneconomic to pursue in the way of a debt. We also have from the auditor's report some information about the fact that the bigger your debt the more likely you are to be able to get away with it. The smaller debtors seem to be more likely to have to pay their penalties. So, how do you go about assessing whether a debt is uneconomic to pursue and, in fact, are there any written criteria, or policy, that applies right across the board?

Mr Butler—Just before we answer, I will clarify that. In the larger debt cases you do not get away with not paying the debt. It is asserted that you pay a lesser penalty in an additional tax related payment. You still pay the debt itself.

Mrs STONE—So, there is a smaller penalty if you are a bigger debtor, compared with—

Mr Butler—That is being asserted, or suggested. I do not have the figures in front of me but, certainly, there is not any claim that they do not actually pay the tax that they should pay.

Mrs STONE—Perhaps, Mr Cahill would be able to help us there.

Mr Cahill—In terms of our risk assessment, I can refer you to page 32 of the report. In terms of late payment penalties, we found that there was a trend that where a penalty had been imposed, the rate of remission grew from 19 per cent to 44 per cent. This poses a possibility that there was a risk that penalties were being used for negotiation.

Mrs STONE—And that was related to the size of the debt?

Mr Cahill—It was related to size of the debt.

Mrs STONE—So, that is—

Mr Butler—I just want to make clear one more thing about the payment. The tax is the primary tax. They still pay that. It is the additional tax related payment—

Mr Cahill—These were cases that were finalised by payments, so they had been finalised in terms of payment on account. It was a matter of whether penalty had been imposed. It was just a pure count of cases that had been finalised.

Mrs STONE—So, we are talking about two issues here. Firstly, there is the business about negotiating penalties. Let me stick to that issue first then: how you assess whether a debt is uneconomic to pursue?

Mr Butler—Mr Mulligan can elaborate on the procedures we have in place for that.

Mr Mulligan—I am going to go to your question in a roundabout way for a deliberate reason. With write-offs, essentially, there are three categories, but I will only talk about two. One is debt that is irrecoverable at law. This is, essentially, where a person has been made bankrupt and discharged and there is no prospect that we will ever be paid. As soon as the person is discharged the debt is finalised, so it is written off at law. The debt cannot be re-raised, and the taxpayer walks away and starts life afresh.

The second category, which is the one that you are focusing on, is the debt that is uneconomic to collect. The term ‘write-off’ is probably inappropriate for those who are not familiar with it, apart from those inside the tax office. Instead of writing it off, as the term is traditionally used in the private sector and the commercial world, in essence, we just park the debt over in a corner. If there is any subsequent activity on that particular taxpayer’s account, the debt can immediately be re-raised. There is no preclusion in any law of our initiating further activity on that particular account. So, it is more a question of it as deferring activity on that account. The revenue—

CHAIR—Is there a time limit on that?

Mr Mulligan—There is no statute of limitations in respect of taxation debts. So, the debt is parked over at the side and we can re-raise it. Most of the cases that we have where we write off debt as uneconomic to collect is where someone has, say, moved house—voluntarily, or otherwise—and we just cannot trace that person. We will write him or her off as uneconomic. It is just pointless chasing someone, or annoying everybody else trying to find data as to the taxpayer’s current whereabouts.

Occasionally, we have taxpayers who say that they cannot afford to pay the debt at that particular time but they will at some future time. We may write it off as uneconomic to collect at that point in time, and it is based on the facts of each individual case. If the debt is fairly small, it is obviously a lot harder to justify writing it off as uneconomic to collect than if, say, the debt is much larger. Ultimately, it gets down to a general fact

situation.

The guidelines we use are those published by the Department of Finance and they have been replicated in our policy manual. Essentially, they talk generically about what the return is on investment of effort of a number of dollars to collect. It is a subjective judgment. There may be some differences between individual officers in how they exercise those guidelines but, ultimately, as I said before, the debt is still on our books. It may not be current until there is further activity on the account, at which point in time the debt is reviewed to see whether it is economic to collect. If it is, we will proceed to recover it; if it is not, we will then re-write off the debt again and put it back. As I have said, we will park the debt in the corner.

Mrs STONE—I would like to pick up that second point we have raised then in that question—the bit about the difference in penalties negotiated for larger or smaller debts. Obviously, the bigger debts have more leverage, it would seem, in attracting a smaller penalty for late payment. Is that because they are better represented by accountants, or barristers, or whatever? I mean, why is there that differential between the smaller debt and the larger debt which the Auditor-General picked up?

Mr Mulligan—The factors which differentiate between a lower debt and a larger debt are infinite. I expect that if you were to engage in larger trading activities, you are obviously exposed to much greater risks. It may also be the case that they presented their case a bit better. I do not know.

Mrs STONE—I would dispute that. If you were a single person, or two-person operation, then there would be an impact of debt substantially greater for you, perhaps, than if you were part of a large corporation.

Mr Butler—I think that Mr Highfield mentioned earlier that a lot of the larger debt cases revolve around factors in some sort of dispute as to the debt, the nature of the debt, whether the assessment is on a correct legal basis, and those sorts of things. In those cases that brings about a different result from the case where the person who has a real debt that he or she does not dispute just takes too long to pay it off. There are some differences around that.

Mrs STONE—So, the bigger debt burden is more likely to be disputed—is that what you are saying—compared with the smaller business with the smaller tax?

Mr Butler—That is the usual outcome.

Mr Highfield—Many of those debts arise from, for example, audit action which we have undertaken where the taxpayer is contesting, say, the assessability of the particular income item, or the deduction of a certain expense item. I do not know exactly the data that Mr Cahill's team analysed, but those sorts of factors could influence the

outcome.

CHAIR—I think that we have pretty well covered the report now. Summing up from the point of view of this committee, I think that we understand and support the Tax Office in its collection of revenue and the need to protect the revenue base. We want to see the Tax Office being consistent. We do not like to hear from our constituency questions about why the Tax Office does not pursue the big fellows, but pursues the small fellows. We hear that all the time. We would like to think that they get equal and consistent treatment across the board irrespective of which Tax Office—whether it is Chermside or Box Hill. That was one of the things we found in our report—I think, 326. The main problem with this Audit Report is the inconsistency that occurs across the board.

Mr Barrett—I would like to make an obvious comment to finalise these proceedings. I think that this hearing has shown, and the Audit Report was trying to indicate, as well, two things. Firstly, there is the importance of performance information because that is important for management. It is also important for the parliament and for the taxpayers.

And, secondly, concerning information to taxpayers, I think that we have witnessed many times that it is not just the question of equity and legality, it is the question of perception, and I think that that is another issue as part of performance information. Certainly in terms of transparency, in terms of making available information to individual taxpayers, I think that, while you might argue about the revenue base, et cetera, failure to take advantage of one's legal rights should be redressed in some way. In a sense that is by information to taxpayers as opposed to a medium or large corporation that has got the resources to adequately inform itself and knows how it can get redress or remission or whatever have you. So knowledge of that is the important aspect.

It is an important point in the report, and it has been taken up by the committee today, that whatever the reasons for the time taken to deal with the larger taxpayers, the fact is that arithmetically the savings are significant to the extent to which either the administrative processing or resolution of the issue can be done in one day, two days, et cetera—or done in a shorter time—and obviously that is where the big bucks are. So quite clearly that is an area that it is important to look at. I would have to say that 100 per cent vetting of ASA4 delegations seems to me to raise a real question of the level of delegation. That needs to be looked at.

Finally, in terms of taxation liability review, as a taxpayer I always thought that if the Tax Office had made a mistake it was not unlimited. If you make a mistake of course it is.

CHAIR—Does the ATO want to respond to that? It has no final comments?

Mr Highfield—The only thing I was going to say is that I will undertake to ensure

that the committee's comments are brought to the attention of all debt collection staff.

Mr Butler—Just a point of clarification: 100 per cent vetting of cases, as Mr Mulligan said, was a particular type of case of writing off rather than all cases they deal with.

Luncheon adjournment

[2.03 p.m.]

ACHARYA, Ms Shampa, Senior Director, Defence Branch, Australian National Audit Office, GPO Box 707, Canberra, Australian Capital Territory

McPHEE, Mr Ian, National Business Director, Performance Audit, Australian National Audit Office, Centenary House, 19 National Circuit, Barton, Australian Capital Territory 2600

MINCHIN, Mr Tony, Executive Director, Australian National Audit Office, GPO Box 707, Canberra, Australian Capital Territory

BAKER, General John Stuart, Chief of Defence Force, Australian Defence Force, Russell Offices, Canberra, Australian Capital Territory

CAMPBELL, Brigadier James Kenneth Hunter, Director General Logistics, Australian Defence Force, Anzac Park West, Canberra, Australian Capital Territory

HADDAD, Brigadier Peter Francis, Director General Engineering and Logistic Policy, Army Headquarters, Russell Offices, Canberra, Australian Capital Territory 2600

ROBINSON, Captain Boyd Chapman, Director Supply Policy—Navy, Royal Australian Navy, CP3-1-02, Campbell Park, Australian Capital Territory 2600

TYLER, Air Commodore Christopher Alan, Director General Information Management and Logistics—Air Force, Australian Defence Force, Russell Offices, Canberra, Australian Capital Territory

CHAIR—I declare the meeting open, resuming from this morning. I welcome representatives from the Audit Office and from Defence. Do you have any comments to make on the capacity in which you appear?

Brig. Campbell—I am representing the headquarters of the Australian Defence Force.

CHAIR—In this session of public hearings, the committee will examine the main issues raised in the *Audit report No.15 1996-97: Management of food provisioning in the Australian Defence Force*.

The Auditor-General found that there was no ADF policy on food provisioning and there was no system for measuring performance of food provisioning in the ADF and comparing performance across the three services. The report also claimed that army's entitlement based ration procurement led to significant wastage. The JCPA will examine

today the potential for efficiencies in food provision in the ADF as well as the level of concern in the ADF in relation to the costs and standard of food provision. I would like to offer Defence the opportunity to make an opening statement. Does the Chief of the Defence Force wish to make a brief statement to the committee?

Gen. Baker—Yes, Mr Chairman. I appreciate the opportunity to be part of your review of the Auditor-General's report on the management of food provisioning in the Australian Defence Force. From my viewpoint, the report is welcome and timely. The issues raised are directed at improving the effectiveness of the administrative arrangements for the provision of food to the ADF and build on internal reviews of food provisioning. In particular, the issue of the absence of an overarching defence policy on ADF food management is being addressed. The defence efficiency review, now under way, has also identified food provisioning as an area for potential saving.

I note that the report addresses food provisioning and catering support in the base environment. Defence is required to retain certain levels of uniform members to undertake food provisioning in support of deployments and operations.

The cost of providing food stuffs to ADF members has attracted some attention, particularly in respect of costing variations between the services and in terms of potential savings through greater use of the commercial support program initiatives. Defence does recognise that costs associated with military operated food provisioning are higher than CSP costs. Action is being taken to reduce these costs where practical and viable to do so.

The report comments on ways to achieve efficiencies through changes to work practices—in particular, through improved collection and evaluation of performance information using both internal and external benchmarking practices. Performance measures and benchmarking for military operated food provisioning is being addressed in the development of the ADF food provisioning policy, taking cognisance of work practices developed in the CSP in-house bid.

With regard to CSP food provision, the report drew a number of conclusions pertaining to CSP practices. I note that the contractors already provide cost and other performance information on catering contracts. Furthermore, the quality of new CSP contracts is continually improved as existing contracts are reviewed.

In terms of ADF work practices, the report recommends that it would be appropriate for the army to adopt a demand driven system similar to that utilised by the navy and air force for on base rations provision. As noted in the report, army has commenced trials of such a demand driven system. However, the extent of the potential savings will not be known until these trials are complete.

I value the ANAO findings on food provisioning in the ADF, and we have already begun a wide range of actions to address them. We have here today the experts from

Headquarters ADF and each of the services, who should be able to address any of the issues or questions that you care to raise. Thank you.

CHAIR—Mr McPhee, would you like to make a statement on behalf of the Australian National Audit Office?

Mr McPhee—Yes. Our decision to examine food provisioning was not prompted by any perceived deficiencies in this area of ADF activity. Rather, it was chosen because it was assumed to involve significant expenditure by the three services in feeding large numbers of personnel. As well, there have been recent changes in the area as a result of the commercial support program. Food is also obviously important for the health and wellbeing of members of the ADF and for their combat readiness.

We found that food provisioning costs the Department of Defence about \$100 million a year in terms of the actual procurement of food and, while reasonably well managed, there is scope for worthwhile improvements in efficiency and effectiveness. For example, Defence could improve current arrangements by reducing duplication stemming from separate initiatives by the services and by further rationalising their food provisioning activities with guidance from ADF Headquarters.

Defence have acknowledge the usefulness of the report and agreed to almost all of the recommendations. Even before the report was completed, the audit had prompted action by Defence, in particular by the logistics policy group, which is currently reviewing ADF food provisioning policy, as General Baker has indicated.

We suggest that to improve management of food provisioning, Defence should focus on the following five key areas. The first area is policy guidance and coordination. Without an overarching ADF policy on food provisioning, the services have pursued their own initiatives and have different procedures. There are risks that procedures are not aligned to ADF objectives and may not be cost effective or best practice.

The second area is performance information and benchmarking. The ADF would benefit from having a system for measuring the performance of food provisioning and comparing it across the three services. There would also be benefit from comparing in-house costs with those of CSP contractors. The average daily cost of providing an officer with meals in the military mess is about three times the cost of what it is in the CSP mess.

The third area is the Army's entitlement based rationing. There could be savings of around \$4 million a year on the basis of our estimates if Army adopted a demand driven system for procuring food instead of the entitlement system based on the number apparently entitled to meals. The fourth area is food management arrangements in Darwin. Given the ADF's moves to northern Australia, Defence needs to address inefficiencies that have arisen with management of rations purchased for the three services in Darwin.

The final area is in CSP contract administration. In view of inconsistencies in contract specification of standards for catering and performance measurement, there would be advantages in coordinating catering contracts. Also, training for staff involved in negotiating, preparing and managing CSP contracts could be more effective.

Other areas for improvement that were noted by the report are as follows: firstly, establishing common contracts for fresh food in the same locality; secondly, separate identification of operational and reserve stocks of combat ration packs; thirdly, listing of components of combat ration packs; and, fourthly, separate performance information on the catering component of contracts that provide common base support services.

Our audit found that there are significant savings to be made in the area of food provisioning through improved management. In addition to this saving of \$4 million a year, which I referred to earlier, the move away from the entitlement system carries potential savings from reducing the volume of administration involved in maintaining the system. There is also the possibility for savings from the amalgamation of local food supply contracts. The other recommendations in the audit also contribute to the more cost effective management of food provisioning with potential for further savings from reduced administrative duplication.

Tony Minchin and Shampa Acharya were the senior audit staff involved with the audit. Mr Chairman, we would be happy to respond to any questions from the committee.

CHAIR—Thank you, Mr McPhee.

Mr GEORGIU—I would like to get a fix on the total cost of food provisioning. The audit office estimates the purchase of food and some other elements of the contract system is costing \$100 million. First, does Defence agree with that? Second, what is the estimate of the all-up cost of provisioning in the ADF? On a quick look, labour costs, et cetera, at minimum seem to add a fivefold increase in food costs. Can I have an estimate for food provisioning in the ADF all up?

Brig. Campbell—The estimate that auditors provided in the report is the best estimate that is available to Defence at the moment. We are in the process of refining our figures to determine the full cost of providing rations. As is indicated in the report, the costs do not include the costs of labour. Were they included, as you have indicated in your question, the cost doubtless would be higher. I do not have the answer to that question in detail and will take it on notice if that is your wish.

Mr GEORGIU—I would like to have some sort of ballpark figure. The figures that Defence provided indicate that in the case of Navy, for example, the rations component is around \$10. The total cost of meals per officer is roughly 12 times that. I am after some sort of feeling for what it actually costs to put that food on the table so that people can eat it.

Brig. Campbell—As to the cost that is referred to—I hope I am referring to the right section of the report—where there is a comparison between the cost of providing a meal in a commercial support program mess and the cost of providing a meal in a non-commercial support program mess, the principal difference in cost arises in the area of manpower, noting that mess staffing levels in non-commercial support program messes are based on needs commensurate with members required in uniform.

To give the committee one example, the costing components associated with non-CSP messes included the full recovery costs associated with military manpower in those messes. I will give the committee a feel for the magnitude of cost. The average salary for a private equivalent in Navy, Army or Air Force is \$25,000. When we take into account the full recovery costs for that one person, those costs go to anywhere between \$85,000 to \$80,000 per person. That is the way we assess the difference between a non-CSP and a CSP activity to make sure that the full value of savings are realised across the portfolio.

Mr GEORGIU—I am still going to press this issue. Page 10 of report No. 5 says:

Food provisioning does not attract a high priority in Defence, because it is routine and accounts for only a small proportion of the Defence budget.

It is quite important in assessing what is happening to actually understand what you multiply that food figure by to get an estimate of what it actually costs to feed the defence force.

I would say I am puzzled if you do not have a feel—is it \$500 million or \$600 million?—for the sorts of factors you have to multiply your rations number by to get the total cost number. Is it a factor of 12 in messes? If you halve that, it is six. If you multiply \$100 million by six, you get over half a billion dollars. Between \$600 million and a billion dollars is not a small component of the defence budget; it is a fairly significant component of the Defence budget.

Brig. Campbell—I am not endeavouring to suggest that it is not an important matter. Indeed, from the opening comments that have been made we are elevating the importance of this subject to the attention of the members who are here this afternoon. As to the specific costs of providing a ration, the purpose of providing that information in respect of labour costs was to indicate that a component of labour cost carries with it a number of overheads which are spread across other elements of activity in the Department of Defence.

It is not possible to give you a ballpark figure for the cost of providing a ration, just as it would not be possible to provide a ballpark figure here this afternoon for the provision of catering services. I will be happy to take that question on notice, if I may, and we will do our best to gain a fulsome response, rather than try to assess what the

answer might be.

Mr GEORGIU—Just for the purposes of this discussion however, would it be absolutely out of the ballpark to say that we are talking about costs of between \$500 million and \$1 billion to actually get fresh food that costs in the order of between \$75 million and \$100 million onto the table where people can eat it?

Gen. Baker—I do not have a figure because our chart of accounts is not structured in that way. The figure of \$500 million to me sounds extremely high. I would think somewhere between \$100 million and \$200 million. Again, I think you need to be careful about costs. The way we cost for CSP purposes, the service mess, bears little relationship to the actual cost of doing it. If you cost a private cook at \$80,000 a year, it actually costs us far less than that.

Secondly, it is necessary to recognise also that, as we move down our new policy, most of the food provisioning will be done under CSP, except where there is a military requirement to have people in uniform. Again, there is a factor in there which is not cost driven. I am sorry, but because our chart of accounts is not structured that way, I cannot give you a precise figure. But my estimate off the top of my head—and it is no more than that—would be something of the order of \$150 million to \$200 million.

Mr GEORGIU—There is \$100 million essentially in fresh food and it takes half of that amount to convert into food on the table with overheads, depreciation and napery. What the cost of meals in in-house messes indicates—certainly in the Navy's case anyway—is that the cost of rations is \$9.69 and the total cost of in-house meals per officer is \$121, which is a factor of roughly 12. If you look at the commercial operators, it is a factor of roughly five between the rations allocation and the food. Being modest, I only multiplied the \$100 million for food by five, rather than by 10 or seven. This is a very important issue and I have raised this before with audit. I am a bit puzzled about why audit did not get the full costings out.

Can I just go onto another matter, which is the issue of wastage in the purchasing and allocation of an entitlement base system. The estimate is that about 37 per cent of people entitled actually take their meal. Let us call it 40 per cent for the sake of argument. What happens to the other 60 per cent of fresh food? Is it cooked? Is it served? What happens?

Brig. Haddad—I will take that question. Firstly, I would like to make the point that the Army has recognised the need to move to a demand based system. That certainly applies in all of our CSP messes at the moment and will apply in the rest of the messes with effect from July this year.

As for the gap, there are a number of components. One is certainly wastage, that is, the inability of the catering staff to accurately forecast the numbers who are actually

going to attend. There is an element there which on my assessment—and it is a rough judgment—is probably in the order of 20 to 30 per cent of the total entitlement because the population is quite variable as to whether they turn up for a meal or not.

Another element of that surplus goes into a cross-subsidy for those who actually choose to dine. For example, the entitlement for breakfast is one egg per person. Those who come and dine invariably have more than one egg, so the catering staff use the surplus as a means of cross-subsidising the actual diners. They also use some of the surplus material for supporting activities which are not strictly within the entitlement regime, that is, providing morning and afternoon teas to entitled people. So that takes up some of the surplus. There is also an element in there of judgment by the catering staff where they under order, based on the fact that they know they have surplus stock on their shelves.

Those are the four components in my view of what happens in relation to the surplus that exists. I would like to repeat my point; we do recognise that the entitlement based system has a large element of waste embodied in it and we intend moving away from that to a demand system.

Mr GEORGIU—How do you maintain control? If you get 40 per cent usage and the cook decides to give people two eggs rather than one or three eggs rather than one, how do you actually maintain control of or accountability for this system? I understand what you are saying, but I am asking, how do you actually know what is happening?

Brig. Haddad—In aggregate there is control; in detail there is not. In other words, there is a judgment on providing additional food for each of the consumers who turn up to dine. That judgment is made by the catering staff supporting that particular customer base. They know that the feeding pattern of their customer base is such that they provide surpluses in some circumstances. That is a question of judgment. In aggregate, the control is there, but there is not control in detail.

Mr GEORGIU—Can you tell us about the control in aggregate? How is the control in aggregate managed?

Brig. Haddad—The control in aggregate is managed by the accounting system that takes account of the numbers of diners, the numbers who are entitled to dine and the internal control mechanisms that exist within each of the catering facilities to make sure that there is not fraud, abuse or theft of the product that is being supplied.

Mr GEORGIU—Basically, if you have 100 people entitled to dine, since the cooks are working on an entitlement system they cook 100 meals.

Brig. Haddad—No.

Mr GEORGIU—This is where I get lost.

Brig. Haddad—The cooks do not cook 100 meals. They have an entitlement, for example, of 100 so they draw 100 rations and there are number of components to that ration base. There are fresh rations and there are dry rations. They have greater flexibility with the dry rations because they last longer; fresh rations have a limited time life. They make a judgment on the basis of the numbers of people they expect to turn up on that particular day for that particular meal. That is quite volatile, given the population that we are feeding. They make an allowance for insurance to make sure that everyone gets adequate food provided and the balance is not cooked at that particular time. The balance is used for those purposes I described earlier in my response.

Mr GEORGIU—It is purchased, people make an estimate and people buy the extent of their rations. They then make an estimate of how many of those rations they will actually need, given their local knowledge of people's preferences. Then the fresh food is wasted if it is not used, because it is actually bought, if I understand you correctly.

Brig. Haddad—No. The element of waste occurs for food that is prepared but then a customer does not turn up to consume that food. That is where the wastage occurs. Also remember that I made the point that there is some judgment applied by the catering staff to under order when they already have stocks of food available. The balance that is provided as fresh food is then used and cooked for other meals. The food that is not prepared, is not wasted. Some of the food that is prepared, but then not consumed, some of that is wasted if it cannot be re-used in other meals.

Mr GEORGIU—What do you mean, other meals? Tomorrow's meal or tomorrow's breakfast?

Brig. Haddad—The example that is mentioned in the audit report is the use of bubble and squeak for breakfast. In other words, something is cooked for the previous night, it is not consumed that previous night but is able to be reconverted to something that is acceptable to the customer base for use at another meal. Now that is only a small element of the total food that is able to be used in that way. Most of it unfortunately, if it is prepared and then not consumed, is wasted.

Mr GEORGIU—And your estimate of that is 30 per cent?

Brig. Haddad—Without a quantitative basis for that judgment, I estimate that up to 30 per cent of the ration entitlement goes in that way, because the cooks do not want to be caught out with a fluctuation in the demand base. It is quite volatile, given the age of the people who turn up, particularly in soldiers' messes. If there is football match on that night, they do not come. They go and watch the football somewhere else. There is volatility in the demand.

Mr GEORGIU—I have one last question on this one. If the turn-up is 37 to 40 per cent, there is a 30 per cent wastage. The rest in your view is allocated to the 40 per cent of people who actually turn up to eat. Is that right?

Brig. Haddad—Yes. In a general sense, that is the way. It is transferred to other purposes. The supplementation I talked about and the provision of additional food in the form of morning teas or suppers. That is where it is diverted to.

Mr GEORGIU—The bottom line is that you have indicated that there is a reasonable amount of judgment involved in cooking things. What has prevented that degree of judgment being used to adjust the actual purchasing of provisions on entitlement rather than a judgment about what is necessary?

Brig. Haddad—There is an element of that already. That is why I said the catering staff apply a judgment by underordering to reflect what they have already got on the shelf. That is only a small part of the total demand. This is a system of rationing that has applied in the army for a long time and therefore people have grown comfortable with the idea. I stress that we have recognised that it does involve waste and it is not the most cost-effective way of providing that support and we have already made the judgment to migrate to a demand based system. The only reason we have not changed so far is that we have linked the change of this with a revision of the rations scale, in other words, the nutritional requirements of the people who we are feeding, and that is what has caused the delay. However, the decision has now been made to go ahead with this new basis of provisioning and that will be applied with effect from July 1997.

Mr GEORGIU—This picks up on something that General Baker said. I want to understand the demand for uniformed personnel. This is mentioned in the audit report and I am totally ignorant of how that works, what the requirement is, et cetera. An explanation of that would help us.

Gen. Baker—In calculating the number of people we require in uniform, we calculate that on the basis of operations, not on peacetime, in-barracks support. Clearly, if you want to send a ship to sea or a battalion from barracks out into the field where they need to eat in the field, you take your catering and cooking staff with you. You need them in uniform, essentially. To support those numbers of people in uniform you need a structure within the defence force which guarantees that you develop cooking supervisors, clerks and all the rest of it. There is a way of calculating the number of people required in uniform. In peacetime, rather than having them sit waiting for operations, you put them to work. In some installation ashore you will find we will need to retain cooks and mess staff in uniform, even though we know it would be cheaper to do that by contract.

Mr GEORGIU—So that is the notion of requirement.

Gen. Baker—It is our capacity to go to war, essentially, is what it is all about.

Mr GEORGIU—How many equivalent full-time people is that requirement for? How many people do you reserve against these activities or you commit to these activities?

Gen. Baker—I do not have the numbers for mess staff and cooks with me. We have developed that for each of the services and we can find it for you, but it works out nearly two to one. For every one we require in the field you need two in peacetime so that you can give people rest and relief from operations. You do not want your Navy cooks to spend their whole life at sea, for example. It is about two to one.

Mr GEORGIU—Later on could we get some numbers—

Gen. Baker—We can give you an estimate of the catering staff required for all of the defence force in the present MOU calculations.

CHAIR—General Baker, when you are preparing your budget bids to go to cabinet, how do you work out a food component?

Gen. Baker—Each of the services work out a component. Essentially, it is based on changes from a historical base and an entitlement.

Air Cdre Tyler—At each base, within each command structure, people estimate what they are going to need for the next year for food, for CSP, for fuel and for every component that is costed to the service. That is aggregated in the command level and it is aggregated at service headquarters and questioned and eventually an allocation is made.

CHAIR—Is there anywhere you have to report on whether that allocation was accurate? Do you measure expenditure against the allocation?

Air Cdre Tyler—Each year in the financial system those figures are reviewed for looking for instances where there might have been underexpenditure or where there were tendencies towards overexpenditure.

In the Air Force, as far as catering goes, within Air Command, which is the operational side of the Air Force, the cost of meals per plate is checked monthly and trends are monitored on that.

CHAIR—Shouldn't going through that procedure give you the figures that Mr Georgiou was asking for?

General Baker—We have fairly accurate figures for food provision. Coming back to the question asked by Mr Georgiou, the allocation is about \$50 million a year as set out in the report. The difficulty is that our chart of accounts is not structured in a way that you can say how much it cost to put that food on the table.

CHAIR—You are moving to accrual accounting, aren't you, in Defence?

General Baker—It is more than accrual accounting, it is a change to our chart of accounts. Under the management system that we have been operating the food is produced by the logistic organisations and the contracts are let and the expenditure is measured. But the facilities are provided by somebody else, the personnel to do it are provided by another element of the service and it is not structured in such a way that you can closely calculate the actual cost of doing it.

Under our new accounting procedures, what I am looking to do under a new chart of accounts is enable us to sense what it costs us to do in a lot of things and Air Force is one of the leading test beds and trial organisations for this structuring of our accounts in such ways as we can make better management decisions on the resources of the Defence Force. I suspect we will progressively introduce that over the next few years. Accrual accounting is part of that but it is not the totality of it. There is a lot more to it than that.

Mrs STONE—Following on my first question relating to the issues Mr Georgiou was raising, in the report the army procures rations according to the entitlements of officers who are on base and so on and Brigadier Haddad has explained how you manage to rationalise that in terms of wastage. But is it not also the case that you subsidise the cost of operating the officers' and sergeants' messes with this system. If that is the case, when you move to more demand based catering, as you do now in the weekends and on some bases—and I understand that works very well—what is going to happen to those sergeants' and officers' messes which will not have that cross-subsidisation facility any more? Will it mean adding additional costs to those officers' and sergeants' contributions? Will they contribute more for their food?

Brig. Haddad—Mr Chairman, I will take that one. The Army CSP messes have a cost outcome very similar to the other two services. Really what the demand-based rationing system is seeking to do is to place the food component into the same dimension as the others. I am confident that the scale, as has been developed, will meet the needs of the customer base. If those customers in a mess believe that because of this approach they are missing out on a privilege that they are used to then those costs will have to be met by the mess members rather than, as at the moment, a cross-subsidy. That is exactly what occurs in the CSP run mess where there is a very strict cost regime and a demand based system.

Mrs STONE—I see, so it will be an increased salary component?

Brig. Haddad—No. It will not be an increased salary component. It will be under a local arrangement. For example, if the living-in mess members believe that they need to have morning and afternoon tea available to them then that will be met as a direct cost to them on a local basis.

Mrs STONE—I see. At the moment you ask for, I understand, your ration forecasts several months ahead from the lieutenants or whatever especially for the fighting units who go into the field. That is a very flexible sort of thing. I understand at the moment that often the problem is that those forecasts are inaccurate or, indeed, they are not made at all in the rush and hurly burly of life. While the rations are drawn for the field, the in-field rations are more than taken care of. No one remembers to tell the poor old warrant officer catering that there will not be 40 in the mess that night. How is your shift to demand based catering going to cope with those communications problems?

Brig. Haddad—In the field the population in theory is not as volatile as it would be back in the barracks where individuals make a decision whether they wish to come to a meal or not. A demand based system for field deployment has exactly the same characteristics as an entitlement one.

Mrs STONE—Yes, but my concern, Brigadier Haddad, is how are you going to get that forecasting of the demand for field versus on-base rations. It is the forecasting that is the problem at the moment.

Gen. Baker—When the force goes to the field there is no volunteering. We know exactly how many are going and where they will be, and they are invariably exercising hard and hungry.

Mrs STONE—I understand that people are not necessarily letting the mess know.

Gen. Baker—But I think you need to understand the difference between the forecasting system and the purchasing system, except for combat rations, which we will put aside for one moment. Fresh rations are purchased very much these days locally to meet the actual entitlement of the numbers deployed. The forecast is only a general guide for funding and for staffing rather than for actually purchasing the ration. We have progressively moved from a situation where rations are bought centrally and stored and delivered out at an Army depot to one of much more local purchase and a much tighter, shorter time frame of delivery. Most of those problems would be overcome. The problem in the field is simple. We know exactly how many we have got and where they will be, and they are all hungry.

Mrs STONE—I understand the field rationing, as your report suggests, was not the focus of the report and it is efficient. My concern was the relationship between letting the base mess know that there would be that number of people not there for food.

Gen. Baker—Again, from a day-to-day problem, most base messes know exactly what is happening to the people in that base in terms of those that will be out on exercises and so forth. That is fairly well predictable.

Mrs STONE—You are reviewing a policy on the provisioning. Are you looking at

things like the timeliness of meals—when they are served—and the dress codes, for example? I am not just talking about officers, but for the general private soldier as well where it might be that the meals are served earlier than the people want to eat, say, at 5.30 in the afternoon. It might be that they do not want to get into certain sorts of clothing to attend a meal. I am not suggesting the Army, Navy or Air Force should change that requirement but, rather, that that might be the disincentive for people to present for their mess meals and instead to ring up Dial-a-Pizza.

Brig. Campbell—The review of the policy referred to has much more to do with a move away from an entitlement base system to a demand driven system. In terms of the way that we will approach that problem, we have already determined that many of the elements of this new policy will move us more towards the best practice which is referred to in this report. It would, however, be important for me to point out that there are still many categories of customers who are fed in base areas whom we do not necessarily wish to provide a degree of discretion to, particularly junior people who are under training in recruit training areas. They will still conform to set meal times and also be required to wear uniform, both as a element of their training and because training schedules are such that we cannot afford that degree of flexibility.

However, when we move to base areas the situation that you have described already prevails. There is a degree of flexibility in respect of meal hours across the three services and there is also a relative degree of discretion, as determined by base commanders, in respect of the standard of dress that will apply. But just as clubs and other activities have minimum standards of dress, I would foreshadow that minimum standards of dress will also be maintained in military activities for quite some while to come.

Mrs STONE—How do you therefore explain the 30 to 40 per cent who fail to come to their mess meals when they are on base and it is part of their entitlement?

Brig. Campbell—I think Brigadier Haddad covered the issue relatively well before. It is a question of the more modern lifestyle that these young people lead. My practical experience with them has been that, whilst we and catering staff do their very best to determine who will be there, a change of decision at a moment's notice before the meal is due to start can be what causes them to go somewhere else.

Mrs STONE—Are you, though, taking on board on those bases what the response of the recipients of the meals is to that catering service as part of your review?

Brig. Campbell—Yes.

Mrs STONE—They are being consulted, so you can look at things like timeliness and so on?

Brig. Campbell—Yes, we will be looking at that. We will take this review as it is

being presented and examine all of the elements of that review to try and make sure that we present the best service available.

Mrs STONE—Okay, I have more questions I want to pursue. I understand that while there is no stated policy of nutritional standards and so on—you cannot perhaps refer immediately to a manual of salt, fat, sugar and so on—but is there, in fact, an operational standard that you have informally?

Gen. Baker—Yes, there is. There is quite a lot of detailed research and work done on the minimum nutritional standards required by all members of the Defence Force tied to their activity levels. And indeed, the Army rations scale is deliberately constructed to ensure that someone who eats the full range of meals gets the calorie intake necessary for what we expect of them. So there is a basis there. The problem is that, in barracks, of course, McDonald's is very popular.

Mrs STONE—That is right.

Gen. Baker—But in the field it is not the same problem.

Mrs STONE—The audit report they referred to the potential problem of allergies, allergic responses to field, is it the case that the Defence Force screens out people with potential allergies or allergies to foods, or is that, in fact, a real problem?

Gen. Baker—I think the statement is probably a bit overdrawn in the audit report. In part, because of the medical history of people, we should know what their allergies are, and certainly the medical staff know what the contents of the ration packs are. But there is always, I guess, a possibility of people over time developing an allergy that we were not aware of before. But I do not believe it is a big problem, because we have full medical history of all of our people.

Mrs STONE—Right. On the issue of the private contractors—CSP they are called, are they not?—there has been some resistance in some services to them. Can you outline for us—whichever service, or perhaps General Baker—why they are resisted in some categories or some areas of the Defence Force?

Gen. Baker—I think that there are a number of reasons. You put yourself in the position of someone who has decided to join the Defence Force, decided that catering and cooking is his forte and sees his career structure disappearing because all of his functions are going out to contract. So there is a bit of a cultural challenge, and that is understandable.

I think there was also a concern in the early days that the standard of cooking and catering across the Defence Force, which has improved remarkably over the last 10 or 15 years, would go backwards because contractors would put profit ahead of quality of

service. I think some of that has been misplaced and, indeed, proper contract supervision and management have preserved reasonable standards of delivery. But it is largely, I think, that cultural problem of people feeling insecure about their futures.

Mrs STONE—So it is not a logistic issue or—

Gen. Baker—I think there are a range of issues associated with keeping enough capability in uniform to go to war, but I think the real problem with it is people seeing their jobs disappearing.

Mrs STONE—I notice there is reference in the document in a number of places to catering or provisioning being not necessarily low status but not a high priority area, and we have associated that with the cost of catering. But is it sometimes, or is it any sense a reflection of the status of the catering corps compared to, say, fighting units or flying units or whatever, so that, in terms of communication, where policies are of great concern, there is a lack of ability for those issues to be brought forward?

Gen. Baker—It is difficult to answer the last question. There is no doubt that the glamour parts of the ADF are the combat elements and the combat units—and may it always be so because the last thing I want is a group of people in the ADF who are not warriors. And automatically, I think, there are some trades that do not have the same glamour and the same appeal. But nonetheless, if you go back over 20 years, the change of standards of food preparation and delivery in the defence forces has been one of our great achievements. And any decent commanding officer will insist upon having high quality cooking and catering staff because it is so important to the people he commands. But it is obviously not the same as being a fighter pilot.

Mr GEORGIU—Can I say that I was reconciled about 10 minutes ago to the fact that we would get the data on all-up cost. I should be reconciled because, having heard the development, I am not sure that we are at one. All I want is a ballpark figure of what it costs for Defence in the same sort of way as Defence could give the cost of meals in house messes. That sort of thing.

Gen. Baker—We will give you a range of figures of what we estimate costs to be and what CSP costs look like and so forth. We can do that.

Mr GEORGIU—I would just like to say again that the ratio between the cost of rations and the cost of meals is that the cost of providing the meals after the rations are there is between six and 10 times the cost of the rations. That is why I just want to get that straight.

The other thing is: you were talking, General, about concerns people being displaced for jobs and the audit report notes that when there is an issue of transferring in-house catering which involves civilians potentially to external caterers, Defence is under

some sort of constraints in terms of consultation and negotiation with the unions and others. Can the committee be advised on those constraints?

Gen. Baker—I think the recommendation of the audit report is that we should do away with in-house bids for catering contracts. It is one of the recommendations with which I totally disagree for four reasons.

First of all, I want the cheapest way of providing the best service to our people and we are not contracting out for religious reasons; we are doing it because I want to save money. That is reason one, if the in-house option is cheaper, I want to take it.

Secondly, we do owe it to our people, I believe, to give them a chance to compete for the jobs and we do have some undertakings with the unions that we will consult with them in that process. Part of that consultation is to allow them to make an offer.

Thirdly, by having an in-house option, you ensure that you have got the best possible competition between private industry and Defence. I think it helps you get a cheaper overall price at the end.

Fourthly, our experience has been that by looking at the in-house options we have been able to achieve internally about a 30 per cent saving across the board. These are generalised figures. Now I believe that, in doing the in-house option, we have learnt not only in terms of catering but a whole range of other administrative support functions: how to manage our internal structures and systems a lot better so that we get ongoing savings, not only in catering but in all the other areas, because the people involved transfer that knowledge to other areas.

So I think there are strong reasons for continuing in-house bids. I think over time that will become more and more difficult to do, because as we transfer most of this out into private industry, we will not be able to recover the situation.

Mr GEORGIU—I thought that what the audit was recommending was that the in-house option should be made a matter of judgment rather than be obligatory. Have I misunderstood?

Mr Minchin—Yes, that is correct. The discussion on page 31 is the relevant page. We did have a recommendation on this on one occasion, but in view of Defence's comments, we deleted the recommendation there. We still put it in as an area that is worth having a look at. It is as you say: we see no point in having it as a mandatory requirement to have in-house bids when they had so little prospect of success.

Mr GEORGIU—Following your point, were there any other recommendations that you had and then deleted because Defence did not like them?

Mr Minchin—It was not so much that they did not like them; it is just that they seemed to have a fairly reasonable response. There seemed no point in our proceeding with that recommendation. But we still had the discussion in case it was of interest to the parliament.

Mr McPhee—We do have a due process which raises the issues and we put them to the agency for comment. And in the interaction we are convinced from time to time about their position. So we modify our initial position.

Mr BROADBENT—On the same issue, General Baker, I misunderstood you before: you said you were against in-house bids but you actually meant you were against the recommendation—

Gen. Baker—Yes, that in-house bids cease.

Mr BROADBENT—You said that competitive tendering, as we are now calling it, which goes into in-house bids, would transfer to other areas and therefore that knowledge. Is there any structure that you are putting together, as we are doing in local government across parts of Australia, where they are actually documenting the process of the in-house bid? Are you doing that?

Gen. Baker—Yes, we are. It is all fully documented and quite substantial.

Mr BROADBENT—And it is fully understood by the Defence Force that a competitive tender is not compulsory within the Defence Force at this stage? Is that correct?

Gen. Baker—It is not compulsory but in most instances under CSP, of course, those presently doing the job are keen to keep the job and they are keen to have—

Mr BROADBENT—I fully understand the arguments, having been through it for two years. What I am putting to you is that it is not compulsory within the Defence Force at the moment to go through the process of competitive tendering.

Gen. Baker—It is not compulsory but it will normally happen because of the benefits of doing it.

Mr BROADBENT—I know what you are doing but it is not compulsory and it is certainly not compulsory to accept any bid that is put forward.

Gen. Baker—We go through an evaluation of all the bids and make a deliberate decision on best value for money and other criteria.

Mr BROADBENT—My question is: if the private sector has no opportunity and

there is no intention to outsource a particular delivery of a service within the Defence Force, are you not sending a message to private contractors, 'We are never going to accept your bid'?

Gen. Baker—No, I do not believe so. There are some functions which obviously cannot be done by private contractors. Combat is the classic one. We have, I think, a fairly wide distinction between what we call core and non-core. Those core functions are those that we judge should not go out to contract because we require that capability in uniform so we can go to war. All the administrative support and non-core functions will eventually be offered up for contract.

Mr BROADBENT—Explain to me then how, if under a core proposal all you are doing really, General, with due respect, is an assessment of the service, it is not a competitive tender.

Gen. Baker—No, in terms of a core proposal, what I am saying is that there are some functions of the Defence Force which are simply not suitable for contract. We are not going to contract out the provision of an infantry battalion, surely. That is just not on the table.

Mr BROADBENT—I have read Machiavelli. The contracting out of a military battalion usually does not work.

Gen. Baker—Of course it does not, so why do it?

Mr BROADBENT—I coming back to the processes such as the provision of food for the ADF. If the particular service is not going to be contracted out because you have said we need to keep a core provision, in case of war, of the talents we need within the Australian Defence Force, if that is the case I am trying to establish how you get a competitive contract area because there are not those listed that put in a competitive contract.

Gen. Baker—No. I think catering is a good example. We have calculated how many catering staff—cooks and mess staff—we require in uniform. Throughout the Australian Defence Force in each of the services we decide where those will best be positioned and placed. That means the other positions are available and up for contracting out. We are progressively working through that process of contracting out base support functions which are considered non-core and we will continue to do so.

Mr BROADBENT—That is different from looking at an in-house bid and going through the process of an in-house bid for a non-core function, or a base supply function as you called it then, as against a private contractor. Do you go through the process, when you have decided that non-core activity, where the in-house bid gets a chance?

Gen. Baker—Yes. For all non-core activities which would go out to commercial contract the opportunity is available for the unit concerned to put in an in-house bid. It is there. Now it is up to them whether they take it up or not and in most cases I suggest they will.

Mr GEORGIU—I would just like to ask Mr Minchin or Mr McPhee something apropos the last point that was raised about recommendations. I think the response was that sometimes you get persuaded out of something because the arguments look fairly compelling that you should not proceed. In paragraph 7.18, does that mean you were persuaded out of the recommendation but not out of the observation?

Mr McPhee—We basically had in mind, in paragraph 7.20, doing an audit of the CSP. We figured that we would pick up this issue at that time.

Mr GEORGIU—So, in the light of Defence's arguments, you did not make it a recommendation, but you were not sufficiently moved to change your observation?

Mr McPhee—Yes, that is right. From time to time, we do not always make recommendations. In some cases—

Mr GEORGIU—No, I appreciate that, I just wanted clarification.

Mr Minchin—The issue of in-house bids was really bigger than just catering contracts and, therefore, one to be raised in a larger audit for CSP.

Mrs STONE—There are two issues here, basically. The first is, with your food provisioning, have you looked at the ADF taking responsibility overall rather than single service chiefs having responsibility? I mean that differently to having the triservice coordination. I mean a single ADF catering function which might give more career opportunities for individuals and perhaps economies of scale and cost efficiencies.

Gen. Baker—I think there is a whole range of ways of doing business. It is important to understand that the ADF has grown up as three separate services which, in recent years, we have started to bring together into a joint process. Headquarters ADF is now only 11 or 12 years old, and we are progressively reviewing this. There is a nice balance to be struck between leaving the services to get on with their business and devolving functions, versus centralising them in Canberra. It is my wish to minimise the centralisation by giving strong policy direction and allowing the services to get on with it, as free as we can. In all of these areas, we will continually examine the best way of doing business, but I have some resistance about centralising everything in Headquarters ADF.

Mrs STONE—But not to everything, just catering? You have a particular resistance to catering?

Gen. Baker—Yes, but if you do it for catering, you might as well do it for vehicle repairs, for fuel supply, for logistics. Where do you stop? I think the policy ought to be the other way: we have a strong, endorsed, central policy process that allows us to devolve the functions as far as we can, and we encourage commanders et cetera in the field to achieve local coordination. So that is the philosophy but, clearly, there are some things where a higher degree of coordination might be a cost benefit.

Mrs STONE—In relation to the Glenn report which came out a couple of years ago and, some 13 years ago, the so-called Tooth report, what has inhibited progress since those two reports were tabled, which said basically the same thing as this current report?

Gen. Baker—Mr Chairman, can we leave that to the next agenda item?

Mrs STONE—Too big?

Gen. Baker—No it is not, but I think we will address Glenn and that consequence in the next item.

Mrs STONE—All right.

Mr GEORGIU—I would like to ask two questions, if possible, about the single service logistics management. What were the problems in terms of Darwin?

Gen. Baker—Essentially we had a single service agreement in Darwin where Air Force provided the food for the three services. With the increase of people in the north in moving the army to the north, the system has outgrown the original agreement we had between the services. It needs to be renegotiated.

For example, at one stage, by far the largest consumer of rations in Darwin was the Air Force at RAAF Base Darwin, but now the largest consumer is Army, so is Army paying Air Force a proper proportion of the bill for food in Darwin? They are the sorts of issues. How many extra staff has Air Force had to put on to support Army, versus doing Air Force's? So there is a whole range of issues in there. I think what we will find in Darwin under the new command arrangements is that most of the administrative support in Darwin will be done in future under joint arrangements. That is still under study; it still has a way to go.

Mr GEORGIU—My last question is about the response to the recommendations. This relates to the previous question about what has happened since the Tooth report, but I understand we are leaving that. A lot of the responses to the recommendations seem to be of the order of 'Agreed, and then we will think about it.' And this is a theme. For example, let me give you recommendation number 3:

The ANAO recommends that the three Services develop cost-effective performance indicators of

food provisioning services, including indicators relating to the cost of providing the service, to assist with management decision-making, consistent with HQ ADF policy guidance (refer to Recommendation No. 1).

The defence response is 'Agreed', and the addendum is 'To be addressed as part of the development of an ADF food provisioning policy.' Does that mean that this will be implemented, not addressed? You are not going to come out with, 'Having addressed it, we do not like it.' That is actually a commitment to having cost-effective performance indicators of food provisioning services. Okay, enough about that. Maybe it is just a stylistic issue.

The other thing is the ADF food provision policy time line. When can we see that chugging out the other end?

Brig. Campbell—It is a task we have undertaken to complete, together with many of the other policy development tasks, during the course of this year, Mr Georgiou.

Mr GEORGIU—Okay, so by Christmas at least.

Brig. Campbell—Yes.

Mr BROADBENT—Will that include, Brigadier, an assessment of in-house bids? Having regard to the fact that you actually do not have accurate costings, I just wonder how you could work out an in-house bid, if you have not got accurate costings now.

Brig. Campbell—It is quite separate commercial support program policy, which is developed within the department, to deal with both the way we would approach, from a tactical perspective, how we would offer services to industry. By that I mean whether we offer catering contracts by themselves, or whether we offer the delivery of catering services as part of the provision of an array of base services. That particular approach is alluded to in the report, and the fact that catering costs are included as part of the total of base services is one of the reasons we are having difficulty in dissecting some of the detail that this committee seeks.

Mr BROADBENT—I can imagine you would. In other words, in regard to rubbish removal—another name was used—the first time you find out what it costs is actually the first contract that comes in, the real costs.

Brig. Campbell—No. In the sense that it is quite common best commercial practice at the moment to offer a contract for an array of services, and to acknowledge in that offer that those services might be provided as individual components at either a greater or lesser cost than the contractor had anticipated, then you allow, within the total of the contract price, the contractor the flexibility to manage his costs against the bottom line. What does not change is the bottom line cost for the contract, although the individual components may vary, either because we vary our demand for seasonal reasons in the case of foodstuffs costs, where there can be variation, or for other demand reasons, for

instance, exercises where entire components of military population move from one area or another. So what we have tried to do, from a strategic CSP policy point of view, is provide industry with flexibility consistent with what they find in the normal marketplace.

Mr BROADBENT—Please do not think that I am coming from a position of criticism. I believe defence force is quite different to local government or any other service that is provided in the broader community. It might be better if we choose other language for the processes that you are going through, rather than the compulsory competitive tendering or competitive tendering or in-house bids. Perhaps those terms should be eliminated from what you are trying to put in place, which is reasonable management of the defence force, rather than benchmarking yourself against private or other industries.

CHAIR—Right. We might conclude on that note with that report. I think maybe down the track some of the committee might be interested in visiting your defence establishment and having a look at the catering. If we are impressed with it, we might let you tender for our catering in this place.

[3.19 p.m.]

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CHAIR—I welcome representatives from the Australian National Audit Office and the Australian Defence Force to the third session of today's hearing. In the third session of this public hearing, the committee will examine the main issues raised in *Audit Report No. 17 1996-97: Workforce Planning in the Australian Defence Force*. The Auditor-General found that there was considerable scope to improve effectiveness and efficiency in the workforce planning in the ADF and to make savings in salary costs. The JCPA wants to investigate at this hearing the potential role of the Headquarters ADF in improved management and co-ordination of the workforce planning function and to review the way in which workforce requirements are determined. General Baker, do you wish to make an

opening statement?

Gen. Baker—Yes. Ladies and gentlemen, I welcome this opportunity to address the committee on the subject of workforce planning. It is a topic of great importance and one of my foremost concerns for the future of the ADF. Accordingly, it is one of my highest priorities. I say this not only because of the substantial share of the defence budget expended on personnel, their training and support, but also because of some other aspects.

The quality of the men and women of the ADF is one of our greatest assets. I think this has been demonstrated over recent years in the international and domestic acclaim for our peacekeeping efforts and, more recently, in the successful rescue of yachtsmen in the Southern Ocean. In the future, as our technological edge inevitably wanes, our capability advantage on the battlefield will rest even more squarely on the training, skill and commitment of our people. We demand a lot from them. In the future, we are likely to demand even more.

I think our workforce planning processes are the least developed of all our planning systems. I think there are some reasons for this, given the complexity of the issues involved, our lack of tools or levers to manage and the rapid changes which are taking place throughout the ADF.

I am concerned about our future ability to attract and retain the high calibre of personnel we need to meet the future demands of the ADF, given competition from private industry, the growing expectations of youth and changing social attitudes in general. Accordingly, I was very pleased when I was advised that the ANAO initiated the performance audit of our workforce plan. I was looking for that external review to provide a fresh look at the problem—some new initiatives and possible techniques and suggestions to add to the already extensive work which has been under way and which continues within the defence organisation.

I must say from the outset that my high hopes for this audit have been somewhat dashed by the outcome. It may be that, given the complex and demanding issues, my expectations were far too high. Solutions to our workforce planning problems are not yet readily apparent, but committee members should be in no doubt that implementation of all of the recommendations in this report—and we pretty much intend to do them all—will not fix the fundamental problems that we face.

In essence, the audit focus of this report is on the mechanics of the problem, not the key strategic management issues involved. It suggests a precision which, at present and probably for the future, is unattainable and unrealistic. The fundamental problem that we in the ADF face is that, within present practice and regulations, we have few tools to manage the strength of an all-volunteer force, particularly in periods of rapid change.

It is important to accept that there are a number of key aspects to this. Firstly, an

all-volunteer force is a great asset. I do not want people in the ADF who have no desire to be there. Secondly, there is very little scope for lateral recruiting to overcome the wastage of most skill groups within the ADF. Thirdly, because of that, we need to grow our own experience, leaders and managers. It is important to understand the time lag involved in that. For a unit commander, it is perhaps up to 20 years; for senior NCOs, it is perhaps 10-15 years.

So recruiting simply to replace wastage does not fix the problem. Yet varying recruiting rates with wastage is about the only tool available to the personnel managers of the ADF. Wastage rates within the ADF vary over time with direct correlation to economic cycles, and we can demonstrate that. I think anyone who could predict economic cycles with any accuracy is unlikely to be in the ADF.

Interestingly, the ADF is one of the few organisations which continues to train its staff in times of recession. Therefore, the ADF is particularly vulnerable in times of economic upturn. In many ways there is no way in which the ADF can compete with the private sector. Pilots are a particular case in point.

If we are to keep the ADF young and vigorous, some wastage is desirable, but it is important to understand that the desired wastage rate is not uniform across the ADF workforce. For example, for employment with high physical demands such as infantry, youth—and hence a reasonable turnover—is desirable. The average age of an infantry battalion might fall best in the mid- to high-20s. On the other hand, in those employment categories with expensive, costly training and lesser physical demand, greater experience and lower turnover is desirable. Unfortunately, it is those people with greater training whom we wish to keep the longest, and it is those whom private industry finds the most attractive.

I simply quote these issues to illustrate a number of key aspects of ADF workforce planning. Firstly, it is not an exact science, rather it is a bit of an art in which there will always been imbalances between the available and the desired workforce. Secondly, we will always be subject to external influences beyond our control, such as the economic cycle. We cannot hope to eliminate undesirable variations in wastage rates, but we should aim to dampen down the amplitude of change. Our present management practice of recruiting to replace wastage is highly inefficient. It leads to constant and wide variations in intakes, with great turbulence in the whole training system and with very high associated costs.

Because we are essentially a closed workforce, glitches in our personnel profiles take years to work through the whole system. Clearly, I think we need to take a whole series of actions which go well beyond the proposals in the audit report—and I stress that most of the recommendations in the audit report we will pick up and run with—but they will not solve the problem.

Firstly, we need to give personnel managers—primarily the service officers and service chiefs—better tools and levers for managing the strength of the service. Secondly, our management should focus on retention rather than recruiting, but by retention, I include the ability to both retain and waste out people to meet service requirements. Thirdly, we need workforce planning strategies which recognise the real limitations of our position and the nature of the ADF.

To meet these needs, there is an extensive program of action in train. I come back to where I started. People with the right training and experience will provide a capability edge as nations around this region achieve parity in equipment terms. It was for this reason that in 1994 we commissioned a review of the ADF personnel policy strategies. That was the Glenn report entitled *Serving Australia: the Australian Defence Force in the 21st century*. This was completed in October 1995 and now forms the basis for the ADF personnel strategy. I think comments contained in that report relevant to this hearing have been distributed to the committee.

Coincident with the submission of that report, it was decided that a work force cell be established in headquarters ADF to direct and coordinate strategic work force planning issues. That group was formed from February last year. They produced, as one of their first tasks, a discussion paper on the conceptual framework of work force planning. That has been accepted by the Chiefs of Staff Committee. With effect from last month, the work force planning cell from the civilian side of the organisation was combined with the military cell. This action accords with our philosophy to manage our total work force as far as we can in a holistic manner.

Consistent with the observations and recommendations contained in that Glenn report and the paper on work force planning, a new defence personnel information system is being put in place. This will aggregate personnel data from the program to support key decision makers and senior planning staff. This is leading to an appraisal of the information requirements to support work force and personnel planning and a dictionary of common definitions.

With effect from last month, a new directorate of defence personnel research has been formed to undertake research on external and internal factors likely to impact upon work force and personnel planning. For the first time a strategic work force plan and a personnel plan are being produced. I hope the first edition of these documents would be available mid-year, but they will be very much a first edition because we have a lot to learn. Personnel and capability development divisions within Headquarters ADF are working more closely together to develop cost of capability guidelines to ensure that work force and personnel factors are given far more consideration at every stage of the capability development process.

A far more holistic and sophisticated assessment of personnel options is currently

being undertaken to better manage the work force. Some of the projects include the following. We are looking for more flexible employment practices, characterised by phases of a career where the number and length of phases will differ between professional streams and where ideal separation rates are modelled. This permits timely management intervention if separation trends vary too greatly from the ideal; not in bulk terms but directed specifically to employment categories. We are looking for a wider range of work practices such as part-time work and job sharing to provide greater flexibility to work force planners and managers and also to members, and these recognise the changing work and career patterns of all Australians.

We need to look at a more competitive remuneration for the officer corps based on work value, rank and skill. We are already developing such a system for the other ranks. We need a reassessment of career management in the ADF to have regard to individual expectations, changing career patterns and changing organisational requirements, not least of which is CSP. We need reappraisal of the existing work force controls such as limited tenure promotion, management initiated early retirement, redundancy provisions, retention bonuses and the level of approval for such initiatives. In particular, we need to provide the chiefs of our services with better levers. We also need to think how ongoing changes in industrial policies will be implemented within the ADF.

I welcome the opportunity to touch on a few of the complexities of the work force issues facing the ADF. The performance audit recommendations will be implemented. Indeed, the program we already have in place is rather comprehensive and it picks up most of the things that the audit report itself recommended. That said, much remains to be done to achieve a work force planning and personnel management system which meets my expectations and the needs of the ADF. The audit by itself will not fix our problem. Thank you, Mr Chairman.

CHAIR—Thank you. Mr McPhee?

Mr McPhee—Thank you, Mr Chairman. The work force planning in the ADF was chosen for audit because of the significant cost of personnel—some \$4 billion a year, or over 40 per cent of the defence budget—and the importance of personnel in performing the defence function, which General Baker has articulated so well.

Work force planning has not been subject to previous audit coverage. Auditing all three services was intended to provide some better practice findings which could be used across the ADF. The objective of the audit was to assess the work force planning systems used by ADF with a view to identifying better practice and making recommendations where appropriate to promote overall effectiveness of planning systems. The main issues were the management of the work force planning function and the determination of work force requirements. The scope of the audit was not intended to be—nor was it—as broad as General Baker may have wished. We would be happy to talk a bit about our planning processes if you wish later on.

The audit concentrated on the full-time military work force, but also included the issue of the flexibility available for military units to employ reserves or civilians where appropriate.

Overall, we found that operational work force planning was being conducted in a satisfactory manner. It is a complex task, as General Baker has indicated, which the individual services were pursuing diligently. However, in our view there was considerable scope to improve effectiveness and efficiency. Savings in salary costs should also be possible. The department responded positively to the report, stating that it provides a good summary of how work force planning is conducted within the ADF and makes some useful suggestions as to how the ADF might improve procedures and practices.

We suggest defence should focus attention on the following key areas. Firstly, the establishment system, which we observed to be inflexible and, sometimes, inefficient and ineffective. The ANAO recommended a reduction of emphasis on establishment controls together with more reliance on financial controls to manage work force usage while retaining central control of the military work force structure. However, this was the only recommendation disagreed with by the department, because of concerns that it would add to administrative complexity and not be consistent with central control of the military work force.

We were informed that there were not always clear cost benefit analyses to support decisions on work force requirements for new capabilities. We recommend that a coordinated approach be taken, along the lines introduced by the air force, to define the costs—including work force costs—of introducing a new capability. Further, the audit looked at the issue of structural overlay. This is the requirement—driven by the closed nature of the military work force system—for additional people in junior ranks to maintain the strength of senior ranks into the future. Structural overlay is particularly high in Navy—80 to 1000 sailors. This indicates the potential for reducing structural overlay which currently costs about \$40 million per year for Navy alone.

We noted that Navy is facing a work force requirement which reduces then rises again, as new ships are brought into service. Navy is proposing to smooth the required work force levels by retaining additional people—or around 2,000 person years—at a cost of some \$120 million. Navy commented that only a part of the dollar figures referred to by this office could be realised as a saving, and we fully accepted that point. We propose that steps also be taken to improve the accuracy of a key element of work force planning, namely the prediction of wastage. Tony Minchin and Graham Smith were the audit staff who were involved in the audit, and we would be happy to respond to the committee's questions.

CHAIR—Thank you.

Mr GEORGIU—I will start off with a brief question on the first

recommendation on Army concentrating the management of all work force planning, other than resourcing, in policy division. The response is agreed in principle, which always makes me a bit uncertain about what that means. The further comment is that the spirit of the recommendation is thought to be in place currently. What does that response actually mean—that you are going to do it, or not?

Col. Hay—The management work force planning situation within Army essentially has two functional elements to it. I would also argue that those functional elements are common to the other services. They are the determination of the liability or the requirement to have people in Army and, secondly, the provision of people to actually fill what we call those establishment positions.

Army has structured itself within army headquarters to separate those two functions, because they are discrete. I think what ANAO is alluding to in their report is that they should in fact be integrated or combined into one organisation. Whilst we agree in principle with that idea, the way in which we actually conduct the process of work force planning involves a great deal of interaction between those two functional elements. Therefore, we believe that the principle of the recommendation is actually in place, that we do conduct work force planning as they are suggesting, but the organisational boundaries that we have placed around the two functions are discrete, rather than combined and integrated, which may be the spirit of their recommendation.

Mr GEORGIU—So the recommendation says ‘unify them’. You are saying that they are actually separate but operating in an integrated fashion and that actually executes the outcome that ANAO intended?

Col. Hay—Yes, that is correct. The other aspect to it is that some of the components of those two discrete functions actually perform other roles than just work force planning. Therefore, organisationally it is Army’s preference to retain the current structure rather than to combine the two functions.

Mr GEORGIU—Could I ask for ANAO’s comment: is Army really doing what you think you want Army to do?

Mr Smith—The reason for the observation was that there seemed to be a fairly complex method of achieving that coordination, which we do not doubt is occurring. We are happy to take Army’s recommendation at face value and, in due course, we might do a follow-up and try to evaluate more carefully how the coordination to achieve the objective is achieved.

Mr GEORGIU—So, in essence, you accept Army’s response?

Mr Smith—My first preference was the initial recommendation. But, if that is Army’s response, I guess we accept that on face value, and we will look at it again later

when we come to a follow-up audit.

Mr GEORGIU—So you do not really agree, but you are willing to wear it at this stage until you go back and have a look at it?

Mr Smith—Yes.

Mr GEORGIU—There is a substantial conflict on recommendation 4(b) on page xxvii, regarding the allocation of:

personnel resources (in the form of a single monetary allocation covering regulars, reserves and civilians) to sub-program managers . . .

The defence response is a very strong negative. How significant is the recommendation in ANAO's view?

Mr Smith—It was part of our group of recommendations in recommendation 4, which we thought was a solution to the problems which we observed with the establishment system. We recognised in the preamble that it is complex. We felt this was a solution which would achieve that objective. Defence have disagreed with that component. As has been said earlier, our point is always to raise issues and suggest ways forward, but it is up to departments to implement. Again, we can come back later to see whether the root cause has been addressed.

Mr McPhee—Our position is to try to get some of the decision making down at their command level and to do that to the extent practicable. Because, if I could quote General Baker on the value of devolution, if you can do that—and leave the centre to determine policy—that is great. General Baker said clearly that there are exceptions. This is probably one, in his view. The idea is to try to address some of the bureaucratic arrangements which we have in place and to put up an alternative proposal for the department's consideration.

Mr GEORGIU—Am I wrong in saying that Defence is almost totally negative on that? It seems like a very strong rejection of a recommendation.

Gen. Baker—From a personal viewpoint, I am happy to allow the service chiefs to manage their work force in the way they believe is best, provided they deliver. That is fine, provided it is an open system and you can go and buy what you want. But the Defence Force itself is a closed system and, unless that work force is generated centrally and controlled centrally, you lose all aspects of control. We are constantly trying to predict our requirements 10 and 15 years ahead. That is what drives much of the work force planning. I admit we are not good at it because we do not have the controls. But it does inhibit, in some ways, how much you can devolve. I think there is a balance somewhere between what the audit office is saying and our present practice. I am keen to devolve as

far as I can.

One of the complications in personnel planning all the time is that we are operating within two sets of controls: one is numbers; the other is money. If we could just go out and buy battalion commanders off the street tomorrow, it would be easy, but you cannot. The only other organisation that has the limitations that we have is probably the Catholic Church, and they are not doing much better either. It is the problem with having a closed work force—you have to grow your own. It creates problems as to how far you can devolve control.

It is all very well a battalion commander saying, 'I want ten cooks and only three riflemen.' That is fine, but we would not be able to give it to him unless we started to produce years ago. I think our systems are bureaucratic, over structured and too slow. We need to improve it. To that extent I think the audit office is right, but we have to find that balance.

Mr Barrett—As I said before, we are not in the business of telling Defence how to run the Defence Force. I would stress that that recommendation relates to subprogram managers, which is a pretty high level. In fact, I would argue that the subprogram managers are pretty essential, particularly in the defence context.

So I agree with the General that it is a question of balance. But we have now had a lot of experience in the private sector and in the public sector for a number of years, where greater flexibility to managers has paid off. It paid off very handsomely in terms of not only getting the right people in the right job but encouraging people to come in on the flexible conditions that are available.

It seems to me that there is a range of positions in the Defence Force where I think flexibility would be the key to getting people in and not having the stringent controls. We all know that stringent controls come at a cost. I then make a distinction, as General Baker made a distinction, between those people who are key to the Defence Force at the end of the day, where he does have problems in not having a market out there. That is not what we are talking about. What we are talking about is the subprogram managers, where there is a degree of flexibility.

I think that when you talk to people—including base commanders, as I have done over the years—you can tell that the crying need is, as they have said in relation to other managers, for more flexibility. If they only had greater flexibility, they would be able to produce greater efficiency. If we are talking about blue sky thinking, about manpower planning in the future, then I think you have to open your mind towards greater flexibility for people who are actually paid to manage. That is the basic point from where we come.

Mr Smith—I will add a little bit to that, Mr Chairman. I certainly support what Mr Barrett has said and emphasise that what was in our thinking here was more the

support units where there was potentially more flexibility between military civilians and reserves. We might almost also point out that we understand what we are proposing is a little bit similar to arrangements with the non-service programs where, if a nominated service is supposed to provide a particular uniformed officer—say, to Headquarters ADF—and if they cannot provide that particular uniformed officer, then we understand that HQ ADF would be entitled to ask for funds to fill that position by other means. That is a similar approach to what we are recommending for the other subprogram managers.

Senator GIBSON—From an industry perspective, which is where I come from, I support what Mr Barrett was saying. There have been great returns in the private sector from delegation, pushing responsibility as far down the line as possible. In some industries there are a lot of specialties that are not available in the marketplace and you have to train yourself. I know of a company where that applied.

But, in pushing this 4(b) recommendation, in having that sort of regime in place in the private sector, there was also great pressure on those managers to cooperate together, to go across several entities or some subprograms to make sure that the planning is in place and to make sure that there are the replacements and the people coming through in an overall aggregate sense. So I am not sure that I agree with the Defence Force.

Gen. Baker—If you can explain to me where you get a ship's captain, a fighter pilot, a maritime patrol officer or a battalion commander off the marketplace, without starting to prepare him and train him 15 or 20 years ago, I will agree with you. But the simple fact is it takes us 15 years to train a senior NCO. Now you have to keep an overall control because there will always be a gap between your ideal manpower structure and what you have actually got and you need to manage that. I am not averse to devolving the function in terms of managing the people that we have, I am quite happy to do that, but you cannot have people at the lower level suddenly deciding that next week they want 10 battalion commanders when you have only had a system of training three. Even if they approve it, you cannot give it to them. Now this is the problem in a closed system, you do not have the same flexibility.

Let me go further by saying it is all of those areas that you can do in the commercial world which are the subject of CSP and are slowly being processed out of the Defence Force. We will have, in future, difficulties in attracting people to keep our technical expertise alive and we will need to have relationships with industry which are quite different to now. But that is not the central core of our manpower problem which is a time delay between wastage and filling that position with experienced people.

Senator GIBSON—Is this largely at the senior level?

Gen. Baker—It is at most levels. And it varies between rank, between trade specialty and with the nature of your employment category.

Senator GIBSON—In rejoinder, can I say that in running paper machines—again—you need 15 years experience. It had to be in-house because they were not available in the marketplace.

Gen. Baker—That is all right. You have the opportunity though, if you want to retain someone, of upping his wage to keep him in the system. We do not have that and that is one of our limitations—we do not have manpower control. That is what complicates our whole process and that is what I am saying we need to do.

Senator GIBSON—Okay, so you need better flexibility?

Gen. Baker—Better manpower control. Our only manpower control is when someone leaves we recruit someone to replace him. That recruit is at the bottom of the tree.

Mr BROADBENT—My question is to General John Baker. Buying a manager from an international company cannot be done in the Defence Force. You can, but it might be totally inappropriate. Also, I have a comment to Pat Barrett: I hope you give the lecture you have just given this group to DSS and Veterans Affairs' within a couple of weeks. I would appreciate that greatly.

General Baker, my questions stem from your opening remarks. You said you do not want anybody in the Defence Force that does not want to be there on a voluntary basis, and whilst I can understand your position, and that would be the position of most managers in every organisation across Australia, however, I want to put to you a couple of things to get your comments. One would be that a voluntary or involuntary group of people for one or two years of reasonable training or semi-training would give you a pool of people that, having regard to the changing social attitudes that you have put forward, would educate that pool of people—voluntary or involuntary people—to open up the opportunities for your recruiting of a wider range of people. That may make a difference in the long run to the glitches that you face, if you have a greater pool of people to draw from.

Secondly, regarding the lateral recruiting, I take it that is a remark in regard to the closed shop process or the closed market that you are in?

Gen. Baker—On the first question, I am keen that anyone in Australia who wants to serve in the Defence Force should have the opportunity to do so. I regard that as a fundamental requirement. And the system for doing that is not only full-time but you can also do it part-time. It is my hope, in the future, that we will break down the distinction between full-time and part-time training so that people can move freely between full-time and part-time training. I think that accords with the changes in social developments that are occurring. Under previous arrangements, when someone had to change his lifestyle and did not want to be posted interstate—for family reasons or other reasons—he had one

option, and that was to leave the Defence Force. So we got rid of him or her. I would like to be a little more flexible in the future.

I think we will need to increase our lateral recruiting in specialist fields. As we go down the commercial support program there will be some things in engineering, maintenance and logistics that we will no longer have the workload within the ADF to generate our own experts. Aircraft engineering is a classic example. More and more, the deep maintenance of our aircraft is put out to commercial enterprise, and the less opportunity we will have of training the senior aircraft engineers in-house and giving them their experience for the Air Force. So we will need to come to some accommodation with industry, either by seconding people in uniform to industry or by coming to some new arrangements. Because when we deploy for operations, we will want some of those people in the field. So there are those sort of problems.

Medics are another example. It is becoming increasingly difficult to attract and retain medical officers in the Defence Forces. There are enough problems elsewhere. Not only that, medical officers in the Defence Force spend their whole time training on fit, young people who have sprained ankles and things like that. They do not get the level of experience required by their own profession to keep themselves eligible for civilian practice. So we cannot afford to keep doctors, in their own interests, in the Defence Force for 30 years like we used to. So we have to find a new way of dealing with that.

We will deal with those sorts of circumstances provided we get different levers to control it and different policies. It requires, in essence, a rewrite of the Defence Act to do the sorts of things we have in mind. They are all the sorts of things that impinge upon work force planning. Because, unless you have those mechanics and regulations that allow you to do those things, you can do all the planning that you like and it will not work. That is part of our problem.

CHAIR—Have these things been looked at by the review?

Gen. Baker—We started this in 1994, when I became aware of the long-term problems with personnel in the Defence Force, and that is what gave rise to the Glenn review. That was the start of this basis. We are doing a lot of work internally to look at how we can restructure and rearrange, but it really comes down to changing the whole way we go about doing our business. That is going to be a long-term process and will require amendments to the Defence Act, and other regulations will need to be put in place.

I pointed out to the ongoing defence efficiency review that this is the top of my priority list, and they have to do something about helping us jump this hurdle. It is a very important issue as far as I am concerned, and it is a long-term one.

Mr BROADBENT—Have you chosen not to comment on a base of voluntary or involuntary people in the Defence Force?

Gen. Baker—I do not want involuntary people. We are not a social engineering agency; we are not there to change people's attitudes. The great strength of the ADF is that wherever we have gone, the people who have gone with us—and this is in recent years—are people who have wanted to be there. They were volunteers and they were committed to what they were doing. You did not spend two-thirds of your time administering a bunch of malcontents. I might say that it is not a criticism of all of those who went to Vietnam as national servicemen, because they all virtually volunteered to go. They performed magnificently. But there is a whole range of administrative overheads in looking after people who do not want to be there. It is not my priority for developing the capabilities we need—

Mr BROADBENT—I used the words 'voluntary' and 'involuntary' on purpose. Is there a case for a country to develop a bank of young people over a two-year period—an opportunity to voluntarily—

Gen. Baker—There is a system called Reserves. We get the flexibility to offer people full-time and part-time training, and we can build up that bank for people who volunteer to do it. I think we almost have the flexibility to do that now, but we do not have the financial cover to do it. We need to change our priorities in that sense. So there are a lot of issues associated with it that go well beyond manpower. On present government projections, we could only do that at the expense of developing capabilities elsewhere. It is a question of where your priorities lie in the present strategic circumstances.

Mrs STONE—You have talked about the fact that you are limited with the tools that you have to manage. You have identified what those limitations are in terms of being able to predict socio-economic circumstances, your closed shop and so on. Then you mentioned strategies that you have at your disposal now, or perhaps you do not, but you are aiming to achieve flexible employment practice by the sound of it, a wider range of work practices, negotiable incomes and so on.

I am wondering, what sort of work are you doing now to identify why you have got the separations that you have? Most of us who have anything to do with the Defence Forces can immediately list 15 reasons why when young men's wives get to a certain stage they exit the force and so on. Have you got that data now and have you identified how in a matter of months you could very quickly change some of the problems?

Gen. Baker—We have. We do a lot of research and a lot of post-separation or separation interviews. The problem comes down to a number of areas. Firstly, we are in the stage of two income families becoming the norm. It is very difficult for spouses of members of the Defence Force who are shifted regularly throughout the country. Even if they find a job, they generally go to the bottom of the totem pole. I have seen spouses whose members have served 20 or 30 years, who finish up with virtually no superannuation for example because they are constantly shifting.

As we increase the level of education, training and stature of people in the Defence Force, more and more of the spouses are professional people in their own right, with their own careers, their own ambitions and their own desires. The Defence Force lifestyle is difficult. It is recognised that one of the greatest disadvantages faced by service families is the education of children and the constant move around. There is a perception if not a reality that it is a great disadvantage to the children. More and more we are seeing people shift to do their jobs and leave their families behind which has a whole series of implications that flow from it. Your mind is only half on the job if your kids are sick 10,000 miles away.

Certainly when I grew up you joined the Defence Force and you expected to stay there for the rest of your life. We plan our systems around that expectation. In fact, less than two per cent of ADF members serve to retiring age, yet all our systems are structured around lifetime service. Youths these days—and I speak to a lot of them at recruiting centres and the Defence Force Academy—say to me, ‘We’ll give you 10 years and then we’ll go and do something else’. So there is a changing social expectation of youth and we have not adjusted our systems to dealing with that.

I think there is a lot of research and a lot of analysis to be done, but the primary reason is economic. You can trace it. In periods of recession, the Defence Force retention rate improves; in periods of economic upturn, people are bought. It is very difficult to keep a young pilot in the air force who is offered three times his wage by the Saudis to go and serve for three or four years in Saudi Arabia. How do you keep him? We have no leverage. You have a technician who has done 15 years training and he has been career managed to give you a long-term capability in electronics. He comes to you and says, ‘That company is offering me twice as much’. We cannot even offer him a three per cent increase in salary. There is no way we can keep them. You cannot expect these kids under the social pressures today to serve on. That is our problem. We need to fundamentally change and give our managers the levers to control their work force.

How do we deal in the future under enterprise agreements in the ADF? I think there are some complicated issues there that we need to deal with. It is not just now. It has been changing for the last five years, but they pose particular problems for an organisation such as ours that we need to learn to cope with. I am not saying we should not do it. I am saying we have to change and learn and we have not been good at that. But they are the fundamental problems. You can do all the planning you like, but if you do not have the levers to manage it, what is the point?

Mrs STONE—So it is a regulatory straitjacket you are talking about, which is a major problem to deal with.

Gen. Baker—Yes. Particularly in a closed work force environment where the decisions you make now will have an effect 20 years later.

Mrs STONE—More women are serving, for example, and they tend to be marrying male service personnel, but the army, navy and air force do not necessarily choose to put them in the same place as married couples. There are those sorts of issues that happen, too, which do not require regulation.

Gen. Baker—There are not too many ships at Tindal, yet that is our problem. If you have got a fighter pilot who is married to a girl in the navy who is a principal warfare officer and likes to be at sea, you have a problem when one goes to Tindal and the other one does not. What is concerning me is, increasingly, as we go more and more joint, what we are finding at the Defence Academy is the cadets from one service are going out with the cadets not of their own service but of a different service.

Mrs STONE—Yes, that was the point I was making.

Gen. Baker—And the inter-service marriages are increasing tremendously.

Mr BROADBENT—And the divorces.

Gen. Baker—No. I think we do face some very serious problems in that respect.

Mr GEORGIU—I would just like to continue with the theme of recommendation and response. Can I just go to recommendation 4(a) on page 27, where audit recommends that each service:

(a) set an overall uniformed target strength that takes into account demands from sub-program managers, future requirements, structural constraints and financial constraints;

This is after significant discussion of establishments and establishment control, and Defence says:

Agreed—the ADF operates on this principle;

Is there a degree of two parties missing one another about what is recommended and what is agreed? Does audit believe that the ADF does operate on this principle?

Mr Smith—I think there is a little difference. We feel that there are a number of targets. There is the sum of the establishments, the personnel entitlements of the various units, but they do not necessarily add up to the total amount of personnel resources that are funded. That is one difference. There is also an attempt to meet the future requirements, but I do not know that that is explicitly taken into account in that system either. I guess what we are suggesting is there should be some attempt for a synthesised overall target structure which takes those things into account. That is my explanation of what the recommendation intended.

Mr GEORGIU—And it is not your empirical observation that this is the way the system operates in principle?

Mr Smith—Yes, that is correct.

Mr GEORGIU—Because there does seem to be a degree of A saying something and B saying, ‘Yes, that is what we are doing’, but the two do not meet. Is that the case in this one? Essentially what audit is doing is actually asking for a different sort of approach towards management of manpower and is quite explicitly attacking establishment control. When you negotiated this, did you both think that you were agreeing on it?

Gen. Baker—Mr Chairman, I do not have any problems with subparagraph (a). I think we need to do that. We can do it better. But we agree, we would like to be able to do that. What we do not agree with is subparagraph (b); that is where the difference comes. So there is a whole bunch of recommendations here.

Mr GEORGIU—And there is not a world of difference between the intent of (a) and the principle of (b). I cannot address that beyond that particular point.

Gen. Baker—Yes.

Mr BROADBENT—Are we drawing close to a close? I have a more general question for General Baker. Sir, you have virtually called today, in my opinion, for a comprehensive review to allow some more flexibility with the levers for the Australian Defence Force Headquarters. A lot of these recommendations and the implementation of them will form part of that review, or do they just raise the issues further?

Gen. Baker—My view is that the recommendations in this do not address the fundamental issues. You can have all these recommendations, and we will implement virtually all of them, but they will not solve the fundamental problem. Therefore we need a totally different approach, which I am proposing. I was hoping to get a lot more new ideas out of this external review but that has not come about. I do not say that as a criticism, because it is a very difficult, complex problem.

We can implement all of these recommendations and it really will not fix the problem that I see for the ADF into the future. That is the point I am trying to leave with the committee. You should not say, ‘If we implement this, the problem is fixed.’ It is not. That is what I am trying to say.

Mr BROADBENT—What processes have ADF Headquarters got in order to move to the concerns that you have?

Gen. Baker—We have a whole series of initiatives in process. It started with the Glenn review to look at all the background, to try and give us some steers. We have

formed some new organisations, we have a policy planning paper that has been considered and agreed in principle by the Chiefs of Staff Committee, we have put in place some research organisations, we are putting in place common personnel reporting systems, et cetera. We need to go further and this why it is one of my highest priorities to get our work force planning processes upgraded to a strategic process—it is one of the weaknesses we have in our defence planning systems at the moment.

CHAIR—Is this problem shared by defence forces overseas?

Gen. Baker—I think it is shared in various degrees. If you doubled everybody's salary tomorrow, the problem would temporarily go away. It is a bit difficult to compare our conditions with those of the major forces overseas. We need a uniquely Australian solution to this, because we are dealing with an Australian community which is different from most others. But no militaries, other than those who do it compulsorily, have an effective manpower planning system—and those that do it compulsorily do not have effective manpower. So you can take your choice.

Mr BROADBENT—But many of those that do it in a compulsory way have an immediate threat also, don't they?

Gen. Baker—You change the strategic circumstances of Australia, then, and my view would change. But under present strategic circumstances, an all volunteer force is what we are talking about.

Mr BROADBENT—It is great to hear, General Baker, that you are saying 'flexibility' already.

Gen. Baker—I have been saying it for years.

CHAIR—That concludes our hearing for today. I would like to thank the people from Defence and also from the Audit Office for participating. I think this hearing leaves more questions than it does answers, so we will have a careful look at the whole subject.

Resolved (on motion by Mrs Stone):

That the committee authorises publication, including publication on the parliamentary database, of the proof transcript of the evidence given before it at public hearing this day.

Committee adjourned at 4.13 p.m.