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JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

Friday, 31 May 2002

Members: Mr Charles (*Chairman*), Ms Plibersek (*Deputy Chair*), Senators Colbeck, Crowley, Hogg, Murray, Scullion and Watson and Mr Ciobo, Mr Cobb, Mr Georgiou, Ms Grierson, Mr Griffin, Ms King, Mr King and Mr Somlyay

Senators and members in attendance: Senators Colbeck and Watson and Mr Charles, Mr Ciobo, Mr Cobb, Ms Grierson, Ms King and Ms Plibersek

Terms of reference for the inquiry:

Review of Auditor-General's reports, first and second quarters 2001-02.

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Committee met at 10.35 a.m.

CHAIRMAN—I open today's public hearing, which is the first in a series of hearings to examine reports tabled by the Auditor-General in the financial year 2001-02. This morning, we will be taking evidence on two audit reports: audit report No. 3, *The Australian Taxation Office's Administration of taxation rulings*; and audit report No. 22, *Personnel security—management of security clearances*.

The committee has received submissions from the Department of Immigration and Multicultural and Indigenous Affairs and AusAID. We will be running today's session for each report in a round-table format. I ask participants to observe strictly a number of procedural rules. First, only members of the committee may put questions to witnesses if this hearing is to constitute formal proceedings of the parliament and attract parliamentary privilege. If other participants wish to raise issues for discussion, I ask them to direct their comments to me, and the committee will decide if it wishes to pursue the matter. It will not be possible for participants directly to respond to each other. Secondly, given the length of the program statements, comments by witnesses should be relevant and succinct. May I emphasise those last two words. Third, I remind witnesses 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. Finally, I refer any members of the press who are present to the 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 this committee statement will be available from the secretariat staff.

BOND, Mr Michael John, Assistant Commissioner, Advice Infrastructure Branch, Office of Chief Tax Counsel, Australian Taxation Office

FOSTER, Mr Phillip Leslie, Deputy Chief Tax Counsel, Office of Chief Tax Counsel, Australian Taxation Office

MEREDITH, Mr Tom, Assistant Commissioner Public Rulings, Australian Taxation Office

CRONIN, Ms Anne, Executive Level 2, Australian National Audit Office

HANSEN, Mr Jon, Executive Level 1, Australian National Audit Office

McPHEE, Mr Ian, Deputy Auditor-General, Australian National Audit Office

WHITE, Mr Peter, Executive Director, Performance Audit Services Group, Australian National Audit Office

CHAIRMAN—The audit report being considered in the first segment is audit report No. 3, the *Australian Taxation Office's Administration of Taxation Rulings*. I welcome representatives from the Australian National Audit Office and from the Australian Taxation Office to today's hearings. With regard to audit report No. 3, the ATO's administration of tax office rulings, does Mr Foster have a brief opening statement he would like to make?

Mr Foster—Yes, thank you, Mr Chairman. I do have just a brief statement that I would like to make. First of all, let me say we welcome the opportunity to be here and to appear before the committee. We would like to inform the committee of the improvements the ATO is making in the administration of the taxation rulings system. We are well down the path of a comprehensive improvement program. This follows two in-depth reviews that have been conducted. The first was the internally commissioned review by Tom Sherman. The second was the ANAO performance audit. The recommendations arising from each of those reviews complement each other. Hence, we were in a position to readily accept all 12 recommendations from the ANAO report.

The improvement program that we have got under way has been given high priority and was recently affirmed by the Commissioner of Taxation in a speech he gave on 4 April to an international tax conference. To facilitate the ATO's improvement program in this area, a new branch has been created within the tax office. This branch gives a stronger focus to the development and maintenance of the infrastructure for technical decision making, especially the binding advice area. I would like to briefly outline the improvements that we have made since the audit.

CHAIRMAN—Can you make that very brief, please, Mr Foster.

Mr Foster—Yes, certainly. I will focus on the private rulings, because I think that is the area that the ANAO raised first. At the time of the ANAO audit, private ruling improvements arising

from the Sherman review were in the design stage. While the ANAO is supportive, and said so in its report, it indicated that the ATO will need to remain focused and resolute. This we have done. Many improvements have now been implemented. We consider that these overcome many of the concerns expressed in the audit report. They improve the integrity and transparency and complement procedures already in place for the processing and quality assuring of private rulings. We now publish all private rulings in a form that does not identify taxpayers in the register of private binding rulings, which is accessible to the public via our web site. We subject all officers approving private rulings to a demanding accreditation process to ensure they have the necessary skills to perform their role.

We have a core production process from receipt to issue, including unique identifiers and secure archiving. We have a better integrated IT system, with the ability to extract more performance data. We have a greatly expanded database of precedent interpretive decisions to assist our staff in providing accurate and consistent advice. The database is also accessible to the community through our web site. We have an electronic manual to ensure that staff understand what is expected of them when processing requests. All of these provide the foundation upon which we can implement the ANAO recommendations, which we are currently doing.

One of the things I should point out to the committee is that, to implement three of the four major recommendations the ANAO made, we had to further develop our IT system. Given the size of that task, it is something we are doing in stages. The next stage will happen in a few months later this year. Another major initiative we have undertaken is that we have now taken a more concentrated approach in the way we actually decide interpretive issues. We have refocused what we had in our centres of expertise to cover all areas of the law and, as a result of refocusing those centres around the technical decision making areas, we have in fact a fewer number of people making decisions. That will improve the quality of the decisions and will help us expand the database that we have.

Finally, we are using the Professional Excellence Forum, which was suggested by the ANAO to ensure that we remain focused on delivering the outcomes. The forum comprises senior tax office as well as private sector members from the tax profession and the small business and business community. I am happy to answer any questions along with my colleagues.

CHAIRMAN—Thank you very much, Mr Foster. Would you mind tabling your entire statement after the hearing so that we can have it on the public record.

Mr Foster—Certainly.

CHAIRMAN—Mr McPhee, do you have a brief opening statement?

Mr McPhee—Thank you, Mr Chairman. I too am happy to table my statement. Mr Foster has obviously given a fairly comprehensive statement of the tax office's actions since the audit. We felt, in particular, that it was the area of private rulings that needed quite serious attention by the tax office. The Audit Office points out the particular areas where attention was needed. We were pleased to see the tax office agree with the recommendations we made and responded very positively to the recommendations. Thank you, Mr Chairman.

CHAIRMAN—Thank you, Mr McPhee. Mr Foster, one of the issues commented on by ANAO in respect of the public rulings was timeliness of those rulings. I think the committee has already earlier this morning expressed some concern at what seemed like very long delays in the development of public statements. Can you comment on the timeliness?

Mr Foster—Perhaps Tom Meredith, the assistant commissioner of the public ruling branch, can comment on it.

Mr Meredith—Certainly it is one of the things that we are concerned about. We have been, particularly in the area I manage, looking very closely over the last 12 months at the ways in which we can improve the timeliness of public rulings. I believe personally that we are improving the timeliness. Obviously there are issues that we need to have regard to. It is perhaps best if I explain first that usually our public rulings are dealing with very controversial and grey areas of the laws. Unfortunately, that is the nature of the product. With some of the public rulings that we put out, we go through a very long consultation process.

Sometimes there are difficulties in actually establishing a better view of the law. That is what we are seeking to do; we are seeking to put out a product that provides guidance to taxpayers, that provides a better view of the law that is consistent with the underlying policy of the law. Nevertheless, we acknowledge it, and we are taking action to improve the timeliness of our public rulings processes. We have consulted in particular with external members of our public rulings panels. A number of suggestions made by those members have been incorporated into our processes. I am not sure that I can add much more to that, Mr Chairman.

CHAIRMAN—Thank you very much for that. I can assure you that at least I, in participating in our inquiry into the rewriting of the capital gains tax law in plain English, am more than well aware of some of the difficulties you face in the legality of a word in a statement and in interpretation by various people who are very experienced in applying tax law. We understand some of the difficulties.

Mr Meredith—I will make one additional comment. Particularly in the last two to three years there has been an increased pressure on the public rulings process following the introduction of the GST and following the introduction of a number of major tax reforms, which have put a great deal of pressure on our rulings process to make sure that we have advice out there to enable the community to comply with the law.

CHAIRMAN—Thanks for that. I have one other question and then I will let my colleagues get stuck into you, because they have a range of questions. I would like to know whether you have any impression yet of how the new office of the inspector-general is likely to affect your public relations role with respect to the public binding rulings?

Mr Foster—It is a new office. I read with interest the documentation that came out as part of the consultative process this week. I think as a general proposition the tax office and the commissioner are quite warmly receiving that kind of initiative. I do notice in the documentation that private and public rulings are something they would be offering some suggestions on. As people in the tax office concerned with the administration of those systems, we would welcome any good ideas that would come from whatever source there. More specifically around the inspector-general, I think it is just really too early to get too involved in

what it might or might not do. My understanding is that there are several months of consultation around the way the process may develop. I do not think I can add anything further to it.

Ms PLIBERSEK—Amongst many of the problems that were identified that were related to private rulings, there was one of consistency. I wonder whether you have made any changes to your information technology systems or other systems that would allow for greater consistency in issuing private rulings?

Mr Foster—I might comment briefly. I will ask Mike Bond to comment in more detail. One of the structural things we are doing is that we are now requiring, in an area of the law where there is no precedent in existence, them to be forwarded off to our centres of expertise as a specialist team in that area of the law.

Ms PLIBERSEK—And that did not exist at the time of the audit?

Mr Foster—It existed at the time of the audit in this respect: The origin of the centres of expertise were to put the ATO view together around the business tax reform topics. So it was basically new business tax reform law and nothing else. It works quite well in the narrowness of that. What we have done now is expanded that across the whole field, including GST, excise and superannuation. We now have those separate centres identified. They will be in full production and operational by the end of June. That is causing anything where there is not a precedent to come to a smaller group of experts. So that helps us a lot on consistency. Where there is a precedent, and that precedent can be identified by a unique identifier, our business line operatives must be able to sight that precedent before they can give advice. So we have a two-staged kind of an approach there. But Mike Bond can give you more detail on the IT side of it.

Mr Bond—Certainly. First of all, I support what Phil says. It is a fairly good summation of what is happening. Basically, we have got two groups of people, if you like—people who can apply precedents. In other words, the question comes in and they say, ‘What is the answer to that?’ Have we got something in a similar case that we have already given an answer on? If so, we match it and send out a response. If not, we escalate it into the centre of expertise. The centre of expertise is resolving those cases. But we are leveraging that. We are not just saying, ‘That’s beaut.’ The case goes out. We capture that information on a database of precedents, which we call ATO interpretive decisions. So our aim is to build and build that database not only for our staff but also for some guidance for the community. So it is dropped on to our *ATOassist* web site as well.

Ms PLIBERSEK—Does that database have a historical component as well? Are you putting all the precedents on the database, or did you mean that just as new rulings are made they go on to the database?

Mr Bond—It is always difficult. This database has been going for about three or four years. I suppose in the early days there were not too many decisions put on this particular database. In some ways, we are looking at it prospectively. But as to how we might capture it historically, it is a case where, if a request comes in and there is no precedent, people say, ‘Well, we probably don’t know the answer to that at any rate.’ We will say, ‘Put it on at any rate. Put it on the database.’ We are trying to build a solid database going forward. But in some ways it does look back.

Mr Foster—Is it worth mentioning the numbers that we have put?

Mr Bond—At the moment, we have got around 1,300 interpretive decisions on that database. That has built up considerably. When the ANAO was looking at this with Tom Sherman, I think it was around 300.

Senator WATSON—Were you not concerned at the audit findings that, of those rulings that were taken to appeal either through the AAT or the courts, 28 per cent produced adverse comment or more? Firstly, what is your reaction? Secondly, how have you responded to reduce that? I mean, sending matters to centres of technical excellence may, in a sense, convey an interpretation of law, but not necessarily with the degree of clarity that it is understood by the ordinary lay person whom it affects.

Mr Foster—Senator, you address your comments to public rulings?

Senator WATSON—Public rulings, yes.

Mr Foster—Again, Tom Meredith can explain it in a bit more detail. We are always conscious of getting the maximum clarity in public rulings. The fact of the matter is that some of them do deal with very complex notions, so it is always a challenge for us to get the expression right.

Where a matter in a public ruling is overturned by a court, we obviously go back, examine the public ruling and withdraw, amend, vary or whatever we have to do. I do not want to say that we can get every technical decision in a public ruling right; we cannot. It is the fact that the courts have different views of the world around some of those interpretive issues. But, wherever possible, with the process that we use through the drafting stage, the public consultation and the reconsideration by our public panels, which include a number of external recognised tax experts, we produce what I think is judged to be rulings of high quality. I am not saying we cannot do better. Inevitably, people are going to have different views so there is always going to be some element of the courts finding against what we might do.

Mr Meredith—Basically, I support what Mr Foster has said. It needs to be pointed out that the ANAO has acknowledged that the ATO has a well-developed public rulings system—which draws on the expertise of ATO staff with detailed knowledge of tax law, on industry and community group experts and academics, and on the general public—and that we do provide a high quality product. Nevertheless, as I said earlier in an answer to the Chairman, the simple fact is that a lot of our public rulings are dealing with controversial issues, with grey areas of the law. Not everybody agrees with our final conclusions on these matters. The purpose of the ATO is to put out this advice to assist the community to comply with the tax law. We put out what we consider to be the better view of the law that is consistent with the underlying policy of the law that we are interpreting. Nevertheless, there are always going to be cases where the courts disagree with our view of the law.

I have one further comment to make in relation to the comments on the study that was undertaken on behalf of the ANAO. Some of those adverse comments were not directed at whether we got the answer right or wrong; some of them were criticising the way in which we were articulating what part of a taxation ruling was a public ruling for the purpose of the Taxa-

tion Administration Act and what was not. Since the decision in Bellinz several years ago, we have taken steps to make sure that we do clarify that. In fact, the ANAO recognised and actually commended our efforts to improve the clarity of the content of public rulings after that decision.

Senator WATSON—Where you discover, in your process of establishing a public ruling or as a result of an adverse comment from the courts, that perhaps the law as proclaimed in the legislation should have been clarified because it is not clear and that is why your people have had some difficulty in expressing a clear public ruling, what procedure do you have of referring that back to the relevant minister or to the parliament?

Mr Meredith—That is one of the processes that we do have in place. Where there is a decision of the court which we consider, for example, is not consistent with the underlying policy and rejects our interpretation of the law, that is something that we do bring to the attention of the government, to ascertain whether or not the government, whichever government that happens to be, wishes to make any changes to the law in that respect.

Senator WATSON—You have suggested that you pass that on to the government. What is your mechanism, though, for informing the parliament? Do these sorts of things get reflected in the commissioner's annual report or do you put out publications? What is the procedure? Parliament also needs to be told when it has passed legislation that is unclear, ambiguous or difficult to comply with. We are interested in making sure that the law is fair and equitable. You have said that you have a process for getting back to government. But what is your process for ensuring that there is some action taken, for example, through a reporting mechanism to the parliament?

Mr Foster—Senator Watson, when we find something where there is some lack of certainty or clarity with the law exposed through the procedures we have been talking about, we go back to one of the Treasury ministers and report to them. We do not have a process, as such, to report to the parliament. To be quite honest with you, I have not thought about it in those words before.

Senator WATSON—You can see the problem, though.

Mr Foster—Yes, I do. They have a new law —

Senator WATSON—Parliament has passed a law that it believes is clear and is intended to produce the results that are explained through the explanatory memorandum. However, as a result of your expertise or as a result of court interpretation, there is a difficulty. I perceive that there is a need for parliament also to be informed about the difficulties that the parliament has created by virtue of the wording that it has passed in legislation.

Mr Foster—I understand and appreciate the point that is being made. But at the moment there is no process that we are aware of. We rather just take things back via the Treasury ministers.

Ms PLIBERSEK—I want to ask a question based on Senator Watson's first question about the 27 per cent of rulings that are appealed. What proportion of all of the rulings you give are

appealed? Senator Watson said that 27 per cent of the rulings that are appealed are found to have negative comments. What proportion of all of the rulings you give are appealed?

Mr Meredith—I do not think we can give any statistics on that.

Ms PLIBERSEK—Could you take a guess, from your experience? Is it very small, or reasonable?

Mr Meredith—It would only be a small percentage of our rulings that are actually ever litigated. Off the top of my head—I hope I am not misleading you—I believe that there would only be a small percentage of rulings that we put out that are taken to the court. Obviously, the ones that are brought to my attention. But we have a large number of public rulings out there. The system of binding rulings has been in place for some 10 years. I am not in a position to answer you.

Mr Bond—What might help—and again, I cannot guarantee the accuracy of the actual percentage—is that I recall something the tax office did a while back, looking at favourable versus unfavourable private rulings; that is, how many were favourable and how many were unfavourable to the taxpayer. That was running at around 70 per cent favourable to 30 per cent unfavourable. If you extrapolate that out, I think it supports Tom's point.

Ms PLIBERSEK—So 30 per cent of the rulings might be unfavourable.

Mr Meredith—I think Mr Bond was talking about private rulings.

Mr Bond—Yes. So 30 per cent might be unfavourable. Most taxpayers probably accept that. Those that do not, then want to go forward. I am in some ways trying to support Mr Meredith's statement.

Mr Meredith—My experience, from talking to people outside the tax office is that the vast majority of taxpayers accept the ATO's view of the law as expressed in a public ruling. Obviously, there are always the margins.

CHAIRMAN—Is that because you are bigger than they are?

Ms PLIBERSEK—It is because they are right.

Mr Meredith—That is because we have such a good process for putting out product rulings, Mr Chairman. Basically, the majority of people are keen to do what they consider is the right thing in terms of their taxation obligations. Our taxation rulings, both public rulings and private rulings, are there for that purpose: to assist taxpayers to comply with the law.

Ms GRIERSON—You mentioned, Mr Foster, that you were setting up a Professional Excellence Forum. What role will they have in responding to rulings that do attract adverse comment or are challenged in law? Will they have a role in that? Will they report on that in any way?

Mr Foster—First of all, the Professional Excellence Forums have been in existence for some time. We have been using that as a sounding board in improving the general technical quality of our work, not just for rulings; we use them in a wider range of things. We get the benefit of some quite good private sector experts there.

Ms GRIERSON—So you have not shaped that in any way in response to this report?

Mr Foster—No. We are using that as the vehicle to make sure that we carry through the things that we have to improve as a result of the report. We are using that as, if you want, a steering committee or a guidance committee to make sure that we push on with the reforms and that we report back to them. On the question of taking adverse technical matters to them, no, we do not—because they are not a technical advisory committee as such.

Ms GRIERSON—I see. So they are not legal experts et cetera?

Mr Foster—They have a different hat on. Some of the individuals there are quite well-known legal experts. Others are more business focused. But we do not use them in that forum for their technical expertise.

Ms GRIERSON—You also said that as part of your improvement program you had set up a new branch.

Mr Foster—Yes.

Ms GRIERSON—Could you tell me what the resourcing is of that, what their priorities are at the moment, and how they will review that or report on that.

Mr Foster—Michael Bond is the assistant commissioner of that branch. He might like to tell you exactly what he is doing.

Mr Bond—It is a question I am often asked at the centre. It is a new branch. We have three major aims with the branch. We are all about infrastructure in the tax office to get the right decisions made—correct, accurate and consistent et cetera. To do that, we basically have three arms in the branch. The first arm looks at work practice and process. You can imagine in the tax office that there are a considerable number of people. There are a number of business lines in the way we are structured. We are trying to make sure that there are some core practices and processes in place so that we can have a corporate control over the production of rulings and other things.

The second stream looks at the technology side. As Mr Foster mentioned in his opening statement, we have basically done some work on our systems already. We have made them more integrated, as the ANAO wished, and we are taking further steps now to improve those systems once more. The third stream is a stream that has, in some ways, two roles. There is a resource of eight or nine who are purely involved in publishing private rulings, this initiative that we have undertaken since the ANAO—

Ms GRIERSON—Taking those up to 1,300.

Mr Bond—No. They are the ATO interpretive decisions. With the publishing of private rulings, for every ruling that comes in, once we respond, we sanitise the response and pop that on a register. That is a little different from the ATO interpretive decisions. That is in the thousands at the moment. So it has that role. The other important role which we are currently resourcing, now that we have got better systems and have the ATO interpretive decisions on a database and have the public register of private binding rulings, we now have the ability to start trawling that information to see what trends et cetera are showing up. We might use that to improve compliance practices et cetera.

Ms GRIERSON—That is the quality assurance?

Mr Bond—That is another aspect. One of my roles is as the corporate assurer of technical quality in the ATO. We do that by examining on a random basis a number of decisions that have been made during the year. We actually do this twice a year. We apply a rigorous test to those decisions. We involve people external to the ATO in that.

Senator WATSON—I refer to the billing systems. We have a \$310 application fee, which includes the GST. In addition, further work is billed at the rate of \$155 per hour, including the GST. For the past 12 months, can you give us an example of what would be the typical minimum fees that you collect from people who apply for private rulings, and also, if you would not mind, the maximum fee? Does it run into tens of thousands of dollars? Secondly, are people using the system rather than using their lawyers as a cheap method—or an expensive method—of getting interpretive advice?

Mr Foster—We do not charge a fee for our rulings.

Mr Meredith—We never have.

Senator WATSON—The billing process is that a \$310 fee is paid by the taxpayer on application.

Mr Foster—Is that for FOI or is it AAT?

Senator WATSON—For a ruling, as I understood it. I might be wrong.

Mr Meredith—We do not charge.

Mr Foster—We certainly do not charge a fee.

Mr Meredith—It was one of the recommendations of the Ralph review. But that has never been implemented.

Senator WATSON—Where does this figure come from?

Mr Meredith—Are you reading from the report?

Senator WATSON—Yes.

Mr Meredith—What page are you reading from?

Senator WATSON—Page 269, re systems supporting user charging fee base ruling.

Mr Foster—It could have been for overseas countries.

Senator WATSON—When a ruling has reached the draft stage?

Ms Cronin—That is the system in New Zealand, I think.

Mr Foster—That is the table that compares different structures in different countries.

Senator WATSON—I see. So you do not charge at all for your rulings?

Mr Foster—No, we do not. Mr Meredith mentioned that the review of business tax did comment on that. There was a suggestion in John Ralph's report that some consideration might be given to charging. That has never been acted upon. So certainly we do not charge at all for any of our advice.

Senator WATSON—So, in a sense, taxpayers would come to you with quite a complex business arrangement that was skirting almost on tax avoidance, which could require hundreds of hours of your work to produce a ruling.

Mr Meredith—Some of the requests we get in the large business area are very complex issues. They do take considerable resources to provide a response. On the other hand, the purpose of the private rulings system is to provide certainty to taxpayers. Where a large corporate is entering into a complex arrangement, they need to have some certainty that the tax office is not going to come and audit them two or three years down the track and say, 'I'm sorry. That's not the appropriate tax treatment.'

Senator WATSON—Could you give us some idea of the range of costs that you incur in producing these rulings? I think we need to look at this, as a parliament.

Mr Bond—In fact, Senator, that is the very issue that the ANAO itself asked. It is certainly at the larger end that the question is currently being focused. We do not have consolidated information. As Mr Foster said, we have accepted the ANAO recommendation. Part of that systems development, which comes on stream late this year, will give us that ability to capture the costs of a private ruling.

Mr Meredith—That is for individual private rulings.

Mr Bond—And we can aggregate it, of course.

Senator WATSON—You cannot take it on notice and give us some idea of the range of costs?

Mr Meredith—At this stage, I would be very sceptical that we have that data available to us. We may have aggregate costs in relation to our private rulings. But I think that is about the extent of the analysis that we could provide at the moment.

Senator WATSON—The tax office is embarking on a program at this time of the year, seeking out those promoters who are involved in tax avoidance schemes. Are there any patterns where these sorts of people regularly put up these so-called ‘devious’ schemes for your assessment in the ruling system?

Mr Foster—We do have a system of what we call product rulings. It is a form of public ruling. If a person wants to market an arrangement, they do make an application to us and we consider that application. If we find that the arrangement has no objectionable features, we do issue a product ruling. That is the item that is quoted often in newspaper advertisements as ‘Approved by the ATO—product ruling No. X’. I am not quite sure how many we have issued this year. Tom might have some more detail, but my guess would be that it is probably under 100.

Mr Meredith—So far this financial year, we have issued 120 product rulings. That is up to 15 May this year.

Senator WATSON—You also issue a system of taxation alerts.

Mr Foster—The taxation alerts are a bit different.

Senator WATSON—How often are your applications for rulings bordering on taxation alert arrangements? I am wondering how often these promoters are pushing the rulings system to the limits.

Mr Meredith—The best way to answer that is to say that, if a ruling application comes in dealing with an arrangement that has the features of a product, that is a private ruling that I anticipate would be escalated. There are, of course, a lot of products that are being marketed that the tax office does not see. We generally see, in terms of product rulings, the products for which the promoters do not anticipate any difficulties with the tax office. They are the ones who come along to us because they want the assurance, when they go out to their potential investors, to say, ‘Look. The tax office agrees with the taxation treatment that we are telling you that you will be entitled to if you invest in this project.’

Senator WATSON—I am interested for you to take on notice the cost to the tax office of producing some of these more expensive rulings. For example, you can categorise it: over \$1,000, over \$10,000, or over \$100,000.

Mr Foster—In the product ruling market there is a reasonably small number.

Senator WATSON—I am just talking about generally.

Mr Foster—We do them in specialist areas. We could probably get some data manually. It would be an approximation. It would be probably be near enough for the kind of thing you are asking.

Mr JOHN COBB—Do you only give public rulings arising out of a change in the legislation? What prompts it? If enough people are inquiring on a particular subject privately, does that prompt you to give a public ruling?

Mr Foster—Yes, it would. That is one of the improvements that we are making, within better management of the system. If we had a significant number of people coming individually and wanting a private ruling, it is a far more economical approach to issue a public ruling so that you can address it at that level rather than coming down to the individual type of thing. But we issue public rulings not just in respect of new law; it might be in respect of a new business practice that is emerging, where we have to do something to explain how that works. It might be as a result of a court decision. There can be a whole range of different reasons. We do in fact invite external people to nominate areas where they think we should issue public rulings. We just do not do them all ourselves. We constantly ask the consultative groups we work with to come up with ideas, areas of concern or areas where the administration would benefit by a public ruling.

Mr Meredith—I will add to Mr Foster's comments. The other trigger for public rulings is where we identify a compliance gap. For example, if we are out undertaking audits and we come across an area of the law where people quite clearly are misinterpreting or misapplying the law, then we will issue a public ruling. We did several—I cannot remember exactly how many—a number of years ago. We put out a lot of what we call 'occupational' rulings. They were all public rulings, but they dealt with the sorts of expenditure that people in particular occupations, such as nurses, could claim deductions for.

Mr JOHN COBB—Generally speaking, is there any reason why a public ruling should be more complicated than a private one?

Mr Meredith—Yes. Because the public rulings deal with the application of the law to arrangements in general. As I say, some of those arrangements can be quite complex. The vast majority of our private rulings come into our personal tax area. They are generally not of a complex nature and can be dealt with fairly readily. The public rulings system is used basically as the flagship of the ATO interpretive advice. It provides advice on complex areas of the law and rather more detailed transactions.

Mr JOHN COBB—So you will not do a public ruling in more detail and more carefully simply because the consequences to Treasury out of the public ruling are not there with a private one?

Mr Meredith—I am sorry. I did not quite understand the question.

Mr JOHN COBB—The point is that a private ruling is exactly that. If it is favourable to a taxpayer, for example, it is really only going to cost the Treasury what that one person owes.

Mr Meredith—That is exactly right, yes.

Mr JOHN COBB—Does that influence how carefully you do it?

Mr Meredith—It certainly does. The private rulings system is, I guess, an exercise in legislative risk management. The whole purpose of the law ensuring that the taxpayer to whom the private ruling is directed is the only person who is entitled to rely on that and get the benefit of it is exactly that—because of the risk of an error of law being made in relation to that private ruling. It is restricted in an economic sense, a dollar sense, to the taxpayer who is in receipt of that private ruling; whereas the public ruling goes out and applies to the community at large.

Mr JOHN COBB—So you would never refer a ruling you have already made privately to someone else? You would never refer a ruling you have made in one situation to another?

Mr Meredith—Firstly, we would not be permitted to actually use a private ruling that has been given to a particular individual to refer that to someone else. If someone else with similar circumstances comes in and asks the same question, in the normal process, the person who is preparing the private ruling should actually be able to identify that there was a private ruling or a number of private rulings that have dealt with the same issue and should provide the same answer.

Mr JOHN COBB—Conversely, if one taxpayer finds out from another one or an accountant et cetera about a ruling, can he use that ruling? He cannot?

Mr Meredith—No. That is the way the law operates. The law provides that a person, be it an individual or an entity, company or trust, can come and ask for a private ruling about the application of the taxation law to an arrangement that that particular entity is entering into. When the private ruling is provided to that entity, the protection that is provided by that private ruling is limited to the taxpayer who receives the private ruling.

Mr Foster—One thing we are doing in connection with that style of private rulings is converting them into what we call ATO interpretive decisions and publishing the decision in a way that does not identify the taxpayer at all. So it puts into the public domain our view of that type of transaction. But it does not put it in as an individual person type of thing.

Mr JOHN COBB—That is something that is sent out to all accountants et cetera, is it?

Mr Foster—It is on our web site.

CHAIRMAN—Didn't duplicating private decisions cause you to come to grief on tax avoidance issues like the Budd plan?

Mr Meredith—I am not sure whether 'duplicating' is the—

CHAIRMAN—They were identical decisions on identical plans, because it was the same promoter. When you got a few of them, somebody woke up and realised that something was wrong.

Mr Meredith—The people who are probably more able to provide an answer in relation to those sorts of arrangements are not in the room at the moment. Nevertheless, what I understand happened with some of the private rulings that were issued in relation to some arrangements was that they were then used inappropriately to convince people that the tax office had

approved arrangements that were not necessarily even the same as the arrangements referred to in the private rulings.

CHAIRMAN—That is certainly my understanding of the issue in a public sense.

Senator COLBECK—Page 22 of the report at clause 35 mentions that there have been identified numerous problems in reports since 1996 and that there has been an incremental system put in place to improve the process. Clause 37 comes to the challenge. What is your confidence in the capacity to meet the challenge?

Mr Bond—I can answer that. I think we have great confidence. We refer you to the opening statement made by Mr Foster. We have not in this instance been saying, ‘We are going to do it.’ We have actually come and said, ‘We have done it.’ We have put in place better systems to capture the information. We have put in place stronger databases et cetera. We have put in place professional accreditation to make sure that people authorising rulings have the appropriate skills and qualifications et cetera. We have done that but we are not stopping there. We are going further with systems improvement. We are going further with that corporate approach to setting precedent that Mr Foster talked earlier about, with centres of expertise et cetera. So we are moving along.

Senator COLBECK—So we can confidently look forward to a smaller volume, next time we come back to have a look?

Mr Bond—A smaller report?

Senator COLBECK—Yes, hopefully.

Mr Foster—I certainly hope so. What has happened since both the Sherman report and the ANAO report has certainly been a far more focused attitude within the tax office on this matter. That is evidenced by the fact that I have sought and obtained additional resources for new branches. We have got a very high priority in our IT system-build plans at the moment for building these types of systems, engaging the Professional Excellence Forum, and subjecting ourselves to a large degree of external reporting back through that committee. Certainly from the commissioner’s point of view, he has established it both in the current year and again for next year as one of the top ATO priority areas. That is to make sure that we get the taxation rulings systems working the way they should work. We are very much dependent on making sure that it all works. While it is true there have been incremental improvements going on since probably 1992 when the system set off, it has never had the internal degree of importance and emphasis that it has now. That was simply brought into focus by the reports that we have had.

CHAIRMAN—Mr Foster, is that an advertisement for our processes in this town of using the Australian National Audit Office to do performance audits of agencies and publicising them, and therefore putting pressure on agencies to look at particular areas? Assuming you will probably say yes, I will ask you this: why did you not have internal procedures which would have picked up these issues yourself?

Mr Foster—That is a good question. We did have internal procedures that were identifying some of the difficulties. The incompatible IT systems and recording systems was certainly

something we were aware of. The cost and the resources and the time to fix some of them are quite immense. They have to compete for priority with a lot of other things within the organisation. What we did was this: The commissioner commissioned Tom Sherman to do a review of where we were with private rulings. That work basically highlighted the fact that we had to do something. We totally changed the emphasis within the organisation in this area. We have now got within the Office of Chief Taxation Counsel some quite focused and dedicated branches. For instance, the corporate governance around private and public advice will not work through the business lines now; it will work through the Office of Chief Taxation Counsel. So we will have more of a whole ATO approach to the issue. But the system that we have been working with over the past two years is getting better every quarter. But there is still going to have to be more time in it.

CHAIRMAN—Ms Grierson and Ms King, I ask you to make the questions succinct and the officers to keep the answers even more succinct, because we are out of time.

Ms GRIERSON—With regard to corporate governance, in the conclusion in that chapter of the report, there was criticism that it was an inefficient process and an inadequate form of control because of the lack of guidance to staff in terms of manuals and also your rulings. It said that the manuals were incomplete and the guidance was dispersed. So what have you done? Who has that responsibility and how have you responded to that criticism? How can we expect to see—other than the changes you have already spoken about—more certainty?

Mr Meredith—I had that responsibility at the time the ANAO was conducting its review. Mr Bond now has responsibility. The ATO advice manual has been updated to include process improvements to date. It has been linked to our relative practice statements, which are our instructions to staff, and to procedural materials. It is now available in electronic form. It is supported by an electronic alert facility, so that staff can be quickly advised of changes to practices and processes. We have a process in place to continuously enhance the manual and maintain its currency. They are all of the aspects that the ANAO was concerned about.

Ms KING—I have a quick question. Were there any inconsistencies in the recommendations of the Sherman review and those of the ANAO? You said they were quite complementary. Were there any other areas that the Sherman review looked at or recommended that the ANAO did not, or are they all exactly the same?

Mr Meredith—You might have to ask the ANAO that.

Mr Bond—I would have said that the ANAO was very supportive of all that Mr Sherman asked for. In fact, they used two particular words when they said that we must remain ‘focused’ and ‘resolute’ in implementing Mr Sherman’s recommendations. That is tantamount to saying that they were right on side.

Ms KING—Did Sherman go further than the ANAO?

Mr Bond—No. Personally, I do not think so. The ANAO’s brief was to look at the whole taxation rulings system, whereas Mr Sherman’s brief was mainly to look at the private rulings systems.

Mr Meredith—We did commence implementing the recommendations of the Sherman report during the course of the ANAO audit, and that was reflected in the report.

CHAIRMAN—In order to wind up, Mr McPhee and colleagues, you have heard what our friends from the ATO have proffered today. Would you like to comment?

Mr McPhee—It sounds pretty positive. I think the ATO has always viewed the audit process pretty positively. The constructive approach with which they are trying to address some fairly major issues within the organisation is to be applauded. There are no issues from us.

CHAIRMAN—Mr McPhee, I was going to say on behalf of the committee that we have always found the ATO to be extremely cooperative and willing to move forward on these issues that we think are important. We will now hear from the next set of witnesses.

[11.37 a.m.]

CLEMENT, Mr Trevor Frederick, Assistant Secretary, Policy and Services Branch, Attorney-General's Department

TYRIE, Mr Ed, Director, Protective Security Co-ordination Centre, Attorney-General's Department

COLLINS, Mr George David, National Manager, Intelligence Branch, Australian Customs Service

BONIGHTON, Mr Ron, Acting Deputy Secretary, Intelligence and Security, Defence Security Authority, Department of Defence

CHARLES, Mr Michael Paul, Director, Personnel Security and Training, Defence Security Authority, Department of Defence

MCCARTHY, Ms Margot, Head, Defence Security Authority, Department of Defence

FLEETON, Mr Mark, Assistant Director General, Resources Branch, Australian Agency for International Development

ROBERTS, Mr Michael, Agency Security Adviser, Australian Agency for International Development

ZABAR, Mr Joe, Manager, Staffing, Australian Agency for International Development

FLYNN, Ms Cathie, Director of Security, Department of Immigration and Multicultural and Indigenous Affairs

HANNAH, Ms Cheryl, Chief Information Officer, Business Solutions Group, Department of Immigration and Multicultural and Indigenous Affairs

BONNEY, Mr William Graham, Audit Manager, Australian National Audit Office

McPHEE, Mr Ian, Deputy Auditor-General, Australian National Audit Office

RUNDLE, Mr Richard Bruce, Executive Director, Business Assurance Services, Australian National Audit Office

CHAIRMAN—We have now come to the second audit report to be examined in this morning's public hearing. I remind witnesses 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. The audit report being considered in this session is audit report No. 22, *Personnel security—management of security clearances*.

I welcome to today's hearing representatives from the Australian National Audit Office, the Attorney-General's Department, AusAID, the Australian Customs Service, the Department of Defence and the Department of Immigration and Multicultural and Indigenous Affairs. I would like to make it clear from the beginning that, to the best of my knowledge, Mr Charles and I are not related.

We have severe time restraints but I am bound by custom to ask each of the departments whether you wish to make a brief opening statement. If you do, if it is more than about 35 seconds, I am likely to get agitated. We will start with Mr Tyrie.

Mr Tyrie—Mr Chairman, I can provide a copy of our opening statement. It will take me longer than 35 seconds to read; maybe a minute and a half.

CHAIRMAN—Could you table it?

Mr Tyrie—Of course.

CHAIRMAN—Mr Fleeton from AusAID?

Mr Fleeton—We have provided a submission which summarises our status against the recommendations.

CHAIRMAN—For which we thank you. Mr Collins from Customs?

Mr Collins—I provided a brief submission this morning.

CHAIRMAN—Thank you very much. Mr Bonighton from Defence?

Mr Bonighton—We have provided a submission. We have a short opening statement, which we will table, if we may.

CHAIRMAN—Thank you very much. Ms Hannah from Immigration?

Ms Hannah—We also tabled an opening statement.

CHAIRMAN—Thank you very much. Mr McPhee?

Mr McPhee—We are happy to do the same and table our opening statement, Mr Chairman.

CHAIRMAN—That is excellent. Having dispensed with all that, this is a broad issue that the committee is very interested in, particularly considering events of September 11 and the on-the-ground clearance procedures that now are associated with our security against terrorism. Certainly, it must also be an important part of those procedures that our personnel, both within departments and in contracted companies, do have adequate security clearance that we are sure

is right, and that we get it right 99.9 per cent of the time so that we do not put ourselves at risk, by having inadequate procedures for clearing people, about knowing things which the general public is not entitled to have access to.

The audit found shortcomings in relation to management, resourcing and operation of personnel security and, in particular, was critical of the backlog in reassessing those who have been cleared once but are due to be reassessed. I think we know from some well-publicised cases both here and abroad of people who go off the rails after a period of time, who were once properly assessed and cleared. Would you each like to tell us briefly about what you are doing regarding each of those issues.

Ms McCarthy—Defence is increasing its vetting staff by a total of 50 per cent. Those people will be coming on board progressively over the next few months. We hope to be able to make good inroads into our backlog in re-evaluations. We are very conscious of the issues you raised with regard to the importance of re-evaluation to our assurance about people's ability and capacity to look after classified information. In addition to the vetting process, we are, as part of our training and awareness strategy, reinforcing to supervisors and managers their role in observing the behaviour of people in the workplace and the importance of alerting security officials to any concerns they may have about people in the workplace.

CHAIRMAN—Ms Hannah?

Ms Hannah—From Immigration's point of view, we have certainly valued the opportunity to have that assessment done independently. It was very useful to us. We have implemented the re-evaluation and revalidation processes. It is something that Immigration takes very seriously and always has done. Where it is warranted, we have put in additional after-care arrangements. In some cases, where revalidation has taken place, we have also made a note that, because of the changed circumstances of the individual or something, this perhaps is not exactly how we would have liked it. We have put a shorter than three-year period into looking again at that particular individual, bearing in mind the sort of comments that you made earlier. It is certainly something that I, as the delegate, am very conscious of. We have been probably more diligent since September 11 because of the things that have happened with heightened security awareness. We have been back through all the re-evaluations to check them and to make sure that we are on track with it.

Mr Collins—Customs has provided an additional \$415,000 for personnel security vetting resources. When we started the project—and this is specifically for security reviews—we had 342 needing clearance or review. At the end of April it was down to 64. I am sure by the end of this month—we do not have the figures—it will be far less than that.

CHAIRMAN—Very good.

Mr Fleeton—AusAID does not have an issue of a backlog at the moment. We have about eight clearance reviews that are due to be renewed. We started action on all those eight before they fell due to be reviewed. So we do not have that issue.

Mr Tyrie—Mr Chairman, I will put my comments in context first. Firstly, as the director of the PSCC and therefore head at the present time of the Protective Security Policy Committee, I

might say that the Protective Security Policy Committee, which has 15 agencies as members, reviews, and continually reviews, the Protective Security Manual. At the present time, it is undertaking a review of part D of the PSM in order that it remains within the context of the environment in which people are expected to work.

The second aspect of addressing you is in my capacity as the head of the PSCC, with responsibility also for the departmental security unit, which has under it the Australian Security Vetting Service—the departmental security unit, with 70 agencies contracted to the ASVS to carry out personnel security vetting. We have at the present time about 369 cases from the 70 agencies. Within the department we have some 97 cases. But we do not have what could be described as a backlog at present.

Ms PLIBERSEK—I think Ms McCarthy is probably the appropriate person to ask: in February this year, you were asked a series of questions in Senate estimates about the backlog and the processing time. I think it was mainly by Senator West. At that stage you were talking about the increase in the number of case officers to begin to address this problem. The first included in the Senate estimates were actually of quite significant concern. I notice that in the case of one type of negative vetting there was a backlog at that stage of 10,969 people. In respect of positive vetting, there were 451 initial clearances and 211 re-evaluations in progress. There were 845 re-evaluations due but not yet initiated. Can you tell me first of all whether there has been any significant dent made on those backlogs? Secondly, at that time you were not able to give us the backlog in length of time. I am curious whether now you are able to tell us what the length of time is for the backlog.

Ms McCarthy—We have yet to make a significant dent in those figures. Our recruiting action is still in train. At the time of estimates we had recently run our national advertising campaign. The recruitment round, which is not only for vetting staff but for other staff to supplement our security resources, is coming to a close over the next month. We expect new people to come on board in about August-September. There will then be, in line with the requirements of the Commonwealth Protective Security Manual, a training investment that will need to be made. It is government policy that vectors cannot undertake security clearances until they have been adequately trained. Unfortunately, although there are new resources coming on, we have yet to make a significant dent.

In terms of the time we think it will take to bring the backlog down that we spoke about at estimates, we hope that our backlog of initial clearances—that is, people who cannot yet start their job in Defence until they have received their clearance, which currently stands at around 1,100—will be well under control in the first quarter of next year. But we estimate that it may take 18 months from now to get the re-evaluation backlog under control, which, as you rightly pointed out, is significant and is of concern to us.

One of the factors in the very large backlog of re-evaluations relates to a new requirement in the Commonwealth Protective Security Manual that was issued in 2000, which for the first time mandated minimum standards across the Commonwealth. The life of a secret clearance was reduced from 10 years to five, for very good reasons, obviously. Immediately on issue of that, as you would appreciate, our re-evaluation load increased very sharply. It is our hope that we are effectively risk managing that re-evaluation backlog through practices in the workplace to

ensure that supervisors are taking account of their environment and the behaviour of the people working with them.

Ms PLIBERSEK—In respect of those initial clearances, where people cannot start work until they receive an initial clearance, do you find a significant number of people actually change their minds and get another job while they are waiting for their clearance?

Ms McCarthy—I do not think that is our experience. I might just check with my colleague Mr Charles.

Mr Charles—No. It certainly does happen, particularly when you have graduates, for example, who have a range of jobs to go to. We do lose some at that time. But at the lower levels, no—this is anecdotal, I am afraid—there are not significant numbers.

Ms PLIBERSEK—With that backlog for negative vetting of close to 11,000—I do not know your systems well enough to understand what happens with those people while they are waiting for vetting. Presumably, they can start on some limited duties until the negative vetting occurs. What is the situation?

Ms McCarthy—This is for re-evaluations? The people due for re-evaluation continue to perform their duties. Again, we are risk managing the implications of that. By virtue of having been cleared initially, they are aware of their responsibilities and they have received the appropriate briefings into the appropriate sensitive areas of information with which they deal. The risk, of course, as the chairman pointed out, is that their life circumstances may have changed in the period. But they are continuing to do their work.

Ms PLIBERSEK—This is a question for you, but other people might like to comment on this. In respect of people's personal circumstances changing, do you ever have people coming to you and saying, 'I'm sorry. I'm going through a crisis. I'm not sure that I really should have the level of clearance that I've got'?

Ms McCarthy—We certainly do. In fact, I withheld an initial clearance last year on the basis of, among other things, the person's frank and, from our point of view, very welcome—we commended the person—admission that they did not feel they were able to work with this level of information. We commended that person in writing for their frankness. One of the important aspects of the training we provide our vectors is to help them develop interview techniques that draw out that level of frankness. We also have people coming to us volunteering the changes in their life circumstances.

Ms PLIBERSEK—Did anyone else want to make a comment on that issue that was identified?

Mr Collins—From Customs' perspective, people do volunteer changes in their circumstances. But we have had no experience of anyone coming to us and offering or making a claim that they are not suitable.

Ms PLIBERSEK—This is my final question. Ms McCarthy, the number of almost 11,000 people is a very substantial number to have as a backlog. I am not quite sure how an

organisation can allow it to get to that extent before you talk about contributing valuable resources. Is there any explanation for that?

Ms McCarthy—I should say that I am bound to tell you that the number has increased since we last spoke. The number now stands at around 13,900. Re-evaluations are coming due every day, obviously on the anniversary of the person's clearance. With regard to how we came to this situation, I would have to say that in an organisation as large and complex as Defence, there are many competing priorities. Different issues come to prominence and are afforded greater or lesser emphases at different times.

Some unfortunate events of the last couple of years in relation to some high-profile security incidents, which have exercised the whole of the Commonwealth, have led to an increased emphasis on this area. All I can say is that I am glad that now we are being given a higher level of resourcing. But there are many competing priorities. Fortunately, security is being given a high priority at this time.

Mr Bonighton—I will add to that. There is a very high level of operational tempo that Defence is working at at the moment. This means that we get a lot more people at very short notice with security clearance requirements. Our hopes of dinting this rapidly—it is going to take us a little bit longer than we had hoped.

CHAIRMAN—Can you put this in context for me. I want to follow up. That 13,000-odd—how many are total personnel?

Mr Bonighton—We are looking at 108,000.

Ms McCarthy—That includes contractors with clearances.

CHAIRMAN—So 13,900 out of something over 100,000?

Mr Bonighton—Yes.

CHAIRMAN—So you are talking about 14 per cent?

Mr Bonighton—Yes. I guess what happens is that, because of the rotational requirements for some of the units, these occur more often than they would have in the past.

CHAIRMAN—Is that total personnel, or personnel requiring some kind of security clearance? My understanding was that with Defence—am I right or wrong—about 80 per cent of your personnel require some kind of security clearance?

Ms McCarthy—I think it is probably a higher number than that. Everyone, for example, who needs access to our internal restricted communications network needs a restricted clearance. That is a very low level of clearance, but nevertheless it is a level of clearance. That 108,000 is not an exact figure. A high proportion of people in Defence need some level of access to national security classified information, even if only at that very low level of restricted information.

CHAIRMAN—I had not thought of this, but I would like to follow it up. I remember visiting the Australian Submarine Corporation, the ASC, in Adelaide. They stripped me of my camera and would not let me even take the camera on the premises. The commanding officer of the submarine that I hitched a ride on for a few days gave it back to me. Navy seemed to have an entirely different view of security than did the Australian Submarine Corporation. I am not cleared for anything. Can you comment on that? You were not there, obviously.

Ms McCarthy—I expect Australian Submarine Corporation would have been particularly concerned to protect national security classified material in development in terms of the submarine project and commercial-in-confidence material. With regard to the submarine, I cannot comment on the commander's comfort with giving you back your camera. Perhaps he had a high level of confidence that you would use that appropriately.

CHAIRMAN—They even took pictures for me.

Ms PLIBERSEK—Of all the operating systems.

CHAIRMAN—Everything.

Ms McCarthy—They are very proud of their work, Chairman.

CHAIRMAN—And justifiably so.

Ms McCarthy—We do not, as a matter of course—I will be corrected by my colleague if I am wrong—clear members and senators as such on the basis that, by virtue of the democratic process, you have been entrusted with the confidence of the electorate.

CHAIRMAN—That is very nice, Ms McCarthy.

Ms KING—I have three questions. The first is to Ms McCarthy. You have said that your staffing is to increase by 50 per cent. Can you tell me what numbers that involves?

Ms McCarthy—That is an increase of around 30, from 60 to around 90.

Ms KING—To the Attorney-General's Department, can you tell me a little bit more about the review of part D of the *Protective Security Manual*. How is it being tightened? What are the areas that were seen to be inadequate?

Mr Clement—All of the PSM is looked on as a living document, so each part is under constant review. Part D, or personnel security, was subject to a personnel security review all on its own. It was a separate exercise a number of years ago. It was the result of an extensive study tour right around the world to look at best practice—not just Australian best practice but international best practice.

One of the frustrations being dealt with in the PSM and part D at the moment is that each level of security clearance has a separate pack requiring the subject to fill it out. But a lot of information is consistent through all of the packs. The review of part D is looking at simplifying

that process wherever possible, not watering down any of the standards—in fact, tightening a number of them. The shift from 10 years to five years for the validity of a clearance is one example of toughening it up—but to try to standardise the pack so that there will be a single pack of information required with little supplements of additional information as you move up through the security classification levels. It is a review to bring it into line with best practice and to try to streamline and simplify the process for the subject who is undertaking the vetting process.

Ms KING—In terms of the monitoring of this system overall, what sort of resourcing do you put into that? Can you tell me a little about that monitoring system and the role you play?

Mr Tyrie—Perhaps I will comment first. Within the department, we face a similar problem to Defence, though on a far lesser scale. One of the issues that is contributing to the problem is that IT systems and information management systems have not kept abreast of the changes in policy. The policy decision to change the period of the validity of a secret clearance from 10 to five years must have had an enormous impact on Defence as against other agencies. What is being developed at the present time is the connection between the systems that manage the protective security clearance regime and the human resource, so that the review of a clearance is flagged six months prior to it falling due. Mr Clement might like to add to that.

Mr Clement—With regard to the resources going into reviewing part D, the policy section within my branch has nine positions. Part D is just one of the parts we are looking at at the moment. We are reviewing part B, risk management, and part G, investigations.

Ms KING—My question was more about the system overall as opposed to the review.

Mr Clement—The system as across government?

Ms KING—Yes.

Mr Clement—Part of the review of the Inspector-General of Intelligence and Security, Mr Blick, a couple of years ago was the requirement for the Protective Security Policy Committee to report to government annually on the status of security across government. For the PSM to do that, we needed to go out and survey every department. We did that last year. That report is yet to go forward to government. But what it achieved was that, for the first time, it allowed us to develop a picture of the status of security across government. We did not have that before. Before September 2000, when the current PSM was endorsed by our cabinet, the PSM was a set of best practice guidelines that were referred to secretaries. It encouraged them to adopt them. There was no compliance—no mandatory requirement to do that. September 2000 changed that and moved the PSM to minimum mandatory standards.

Ms KING—So how many staff do you have in your area that are responsible for the survey? You put the monitoring down to the survey?

Mr Clement—The survey itself: we had three officers working for a number of months exclusively on the survey.

Ms KING—Okay. That is fine.

Mr Clement—It is just one of many tasks in the section.

Senator COLBECK—It appears that for some that have been subjected to this process it has been a wake-up call and perhaps a reinforcement of knowledge of an existing problems for others. Some of you have indicated that you are going to increase resources to catch up with the backlog. But it is clear from the report that generally there has been insufficient resource allocated to managing the issue. We have had heard from Defence that they have made some actions to deal with it. In the longer term, what are the strategies that you have in place to maintain these review processes at an acceptable level? Those who have not responded might like to indicate that.

Ms Hannah—Immigration and Multicultural and Indigenous Affairs has a departmental security committee, which is part of what is required under the PSM. We have recently gone through a process of reviewing the membership and the chairing of that committee with a view to increasing the strength of the monitoring and evaluation component of it. It is directly linked now into our board of management, which is all of our division heads, our CFO, and chaired by our secretary. So I, as chair of the departmental security committee, will have a direct line of reporting into the board to explain what we are doing, how we are monitoring. It will give me an opportunity to continue to make sure that the resourcing level that is set for this is lined up with the requirements that have increased quite dramatically over the last two years for our department.

Mr CIOBO—My first question is to Ms McCarthy with respect to Defence about the 14,000. In the Defence Security Authority, do you do all your own internal revalidations of security clearances, or do you outsource some of that to, for example, vetting services? Or is it all done internally by the defence department?

Ms McCarthy—We do not outsource any of our negative vetting. We have a small number of professional service providers assisting in the positive vetting process. That is a higher and more thorough level of clearance that is undertaken by a cell within the Defence Intelligence and Security Group.

Mr CIOBO—In terms of having a backlog of 14,000 people, is that a failure of your management controls to allow that to happen? I recognise what you said in terms of the PSM dropping from 10 to five years. I do not understand how it can reach such a significant proportion of people, even taking into account competing priorities.

Ms McCarthy—I think a high proportion of the problem relates to resourcing. I guess an understanding of the level of resourcing required is a facet of management control. It would be true to say that we have not in the past afforded this as high a priority as we might, but are now doing so.

Mr CIOBO—With regard to part B of the PSM, does Defence have an up-to-date risk assessment?

Ms McCarthy—We are currently developing a Defence security plan based on risk assessment principles. The first stage in that is a very high level document covering the whole of Defence. For that plan to be meaningful, it obviously needs to be cascaded down across the

13 groups because they each face slightly different risks and threats. So while that is not in place yet, we are working on that at the moment. Just this week, we brought on another staff member, whose time will be almost exclusively devoted over the next few months to working with other parts of Defence on that plan.

Mr CIOBO—Is the development of that plan a consequence of the ANAO report, or is that something you started prior to that?

Ms McCarthy—We had for some years undertaken a yearly threat assessment for Defence, but that is slightly different from a Defence security plan. Our action on that plan is more a consequence of the requirements of the Protective Security Manual than of the ANAO audit. The Protective Security Manual preceded the ANAO audit.

Mr CIOBO—Is that now being tied back into personnel security arrangements that you have got, so that there is a coordination between the two?

Ms McCarthy—Certainly it will be important. We recognise the need for the security plan to address all aspects of security, be it personnel security, physical security or information security. So it will certainly take into account personnel security as an important area of risk.

Mr CIOBO—If there has been an increase of 2,000 people since February, I take it you would know over the next few months whether it is now going to plateau, or is that backlog still going to increase, given that, as you said, every day there are anniversaries of initial clearances? What is the trend going forward?

Ms McCarthy—The trend, unfortunately, prior to having our people fully trained and fully productive, will be upwards. So our priority, once we bring these new people on board, will be to get them trained as quickly as we possibly can, without sacrificing the quality of that training of course, so that they can start working on the backlog. There is obviously light at the end of the tunnel, but the problem will not be fixed —

Mr CIOBO—You would know, though, how many people are coming to be revalidated over coming months. Given your time frames for the training of staff, where is it going to peak—at 16,000 or 17,000?

Ms McCarthy—I do not have that figure immediately to hand as to where it might peak. Our understanding of this problem is likely to be enhanced—and this is something that the ANAO audit addresses—when our overall human resource management database is connected to our personnel security management database. That will allow us, for example, to take off our system people who are coming up on our personnel security management database as due for re-evaluation but who may have in fact left the service. But we cannot predict exactly what the impact of that connection will be, only that we will have an even clearer view of the challenge ahead of us.

Mr JOHN COBB—On the face of it, these figures are not good. Are these things prioritised within the numbers? Nobody has more respect for our armed forces than me, and I have more respect for them than to think that they did not have responses worked out on things that can happen in Australia prior to September 11. So for the people with the knowledge of how we

would respond to a situation, would their clearances be prioritised? Can you assure us that, while these total numbers are obviously not good, the people in the most important positions, with the knowledge that would be incredibly dangerous if it went out, are not part of these numbers? Similarly, with Immigration: the people who actually make the decisions of who comes in and who does not—are they prioritised against the total numbers we are talking about? I guess Customs is probably not much less important, but it is more a case, I suppose with you, of the people physically doing the checking rather than the decision makers, so it is probably a bit harder to prioritise. Can I assume that the people in the really important positions are done?

Ms McCarthy—We are looking at ways of prioritising effectively, in just the way you have stated, those re-evaluations when we have resources available to be cutting down that backlog. We will be drawing on some work that the positive vetting area has been doing. They are conscious of their own backlog, which in absolute numbers is much smaller. They are conscious of the need to prioritise those re-evaluations, so they are developing a checklist of subjective and objective measures that will enable us to determine who should be re-evaluated first. We have not fully worked that out yet; it is obviously something that we will need to do in short order.

Mr JOHN COBB—But do you take my point? Whether a soldier in the field is vetted is a different thing to whether the person is who works out how we respond to a situation. The people at the top who do matter: can we assume that they are cleared?

Ms McCarthy—We can assume that everybody in Defence who currently has access to national security classified information has had an initial clearance. The re-evaluation is obviously of concern in relation to whether their circumstances have changed. In relation to the soldier in the field, it is not automatically the case that we would not be concerned if, for example, they had access to very sensitive intelligence material. We would be equally interested in re-evaluating them.

Mr JOHN COBB—We can assume, then, that at least the people who are the most important are the ones you will fix up first?

Ms McCarthy—We will endeavour certainly to make sure that happens. We will do that.

CHAIRMAN—Would Customs and Immigration like to answer their portion of Mr Cobb's question.

Ms Hannah—I am happy to do that. Immigration does not have a backlog. First of all, I would like to put that on the record. Secondly, we do not have the difficulties that face an organisation of the size and scale of Defence. However, we do have some extremely sensitive positions in our organisation. I can assure the committee that we have the proper clearance processes in place. There is nobody operating at that level who does not have appropriate clearance.

Mr Collins—Customs does have a priority scale for clearances. That is considered by the Customs security committee, which meets every six months and looks to see whether that priority scale is still appropriate. Generally, it stays pretty much the same. But the higher level clearances—for instance, top secret for SES officers—is our highest priority. It works down

from that according to operational requirements and any other factors. Like Immigration, we do not have a backlog as such. I think we have a separation rate of around five or six per cent. Assuming they are replaced, we have the resources to maintain our level of service and our clearance processing.

CHAIRMAN—ANAO's recommendation No. 4 said that organisations should adopt better practice, contract management principles and standards in outsourced security clearance and vetting service arrangements. Defence has already told us that they do not utilise outsourcing.

Ms McCarthy—Except in the positive vetting area, a very small number of professional service providers.

CHAIRMAN—Can I ask each of you whether you have accepted ANAO's recommendation and what have you done about it?

Ms Hannah—Yes, we have. We were doing it prior to the recommendation. But we certainly accept the recommendation.

Mr Collins—Customs has, but we do not use outsourced arrangements very much at all, only for some particular clearances.

Mr Fleeton—AusAID does all its clearances in-house.

CHAIRMAN—You would be more represented overseas by contractors than by AusAID agents, by personnel, wouldn't you?

Mr Fleeton—Yes, we would have more contractors than AusAID staff.

CHAIRMAN—Overseas.

Mr Fleeton—Yes.

CHAIRMAN—Importantly, you put them through security clearance processes that you would put your own officers through?

Mr Fleeton—No, because they generally will not be required to have access to national security information.

CHAIRMAN—Why am I surprised?

Mr Fleeton—AusAID contractors overseas administering projects in the health or education area, for example, have a specific task, which is to work in that area with their counterparts to achieve developmental objectives. They generally do not have, to my knowledge, a requirement to have access to national security material.

CHAIRMAN—You are saying that they do not have access to information that could be considered to be a security risk?

Mr Fleeton—That is right.

CHAIRMAN—Thank you.

Mr Tyrie—We apply best practice principles in our organisation, being responsible for the development of the policy. In order to get across this, one has to understand the changes that have taken place. The Blick and Blunn reports and September 11 have changed the security environment markedly.

CHAIRMAN—Tell me about it!

Mr Tyrie—The PSCC has been at the centre not only of the protective security policy with regard to the PSM but counter-terrorism coordination and the management of security. From my perspective looking over all of the agencies and their performance in this area, one of the reasons that the Protective Security Policy Committee developed the survey was annually to survey what was going on. We have had the first survey. We have not yet dealt with the results of that survey because it is before go for the cabinet's consideration at the present time. We need some of these things to wash through the system so that we can get a truer picture of what is going on.

CHAIRMAN—Thank you for that.

Ms PLIBERSEK—I want to ask some questions of the auditors. It might be quicker than asking every department in turn. Mr Cobb asked about how presumably the people with more access to more sensitive information are re-evaluated first. In paragraph 2.9 of your report, it says that the audit found a need for improvement in the integration of the threat risk management processes within the personnel security function in four of the six organisations audited. It seems to indicate to me that that is not the case, that there is not necessarily a priority given to people who either might have access to more sensitive information or have other risk factors. In your audit process, is that what you found? Can you reassure Mr Cobb, or did you find that you could not reassure him, given what you have seen?

Mr Rundle—The comment that led to 2.9 was in fact talking about wider understandings of risk management being applied specifically to the clearance process. We were not looking at the setting of priorities within personnel clearance.

Mr Bonney—That is right. I can confirm that we did come across processes for prioritising security clearances in a couple of the agencies. Immigration and Customs were the two that come to mind. We did not necessarily look for it. It happened that we came across it in those two.

Ms PLIBERSEK—We have focused a little on this backlog. I did not want to unfairly paint one department as having a more serious problem than any other if that is not the case. In your evaluation of all seven organisations—I know that Immigration has said they do not suffer that problem—did you find that backlog problem in other organisations?

Mr Bonney—Yes. The backlog was a common problem.

Ms PLIBERSEK—What I mean to ask more properly is: Defence are talking about quite a high proportion of their staff that require security clearance—was the proportion as high in other areas, or significant, in your view?

Mr Bonney—The problem of the backlog was highest in Defence. It was also very high in two of the other agencies, who unfortunately are not here today.

Ms PLIBERSEK—Can you tell us who they are? In the report we have all been very cagey about who is not doing what. Given that we all know who is in the report now, can you tell us which agencies had a problem with that?

Mr Bonney—The chairman tells me that I can tell you. The Australian Taxation Office had a very high proportion of backlogs. It was somewhere in the vicinity of 40 per cent.

Ms PLIBERSEK—40 per cent?

Mr Bonney—35, 40 per cent. This is in reviews.

Ms PLIBERSEK—Is that making you feel better, Ms McCarthy?

CHAIRMAN—But 40 per cent of 10 is one hell of a lot less than 40 per cent of 100,000.

Mr Bonney—That is of the security clearances; that is not of their total number of staff. Of the total number of staff, something like 10 per cent have a security clearance because of the nature of the information they deal with.

CHAIRMAN—They are doing better than Defence, then.

Ms PLIBERSEK—Slightly, yes. And the other organisation was?

Mr Bonney—The National Crime Authority also had a very high proportion, somewhere in the vicinity of 40 per cent.

Ms PLIBERSEK—But that 40 per cent would be of a significant proportion of their staff?

Mr Bonney—Of their staff numbers; that is right.

Ms PLIBERSEK—Of their staff numbers, what proportion would require security clearance?

Mr Bonney—Nearly 100 per cent.

Ms PLIBERSEK—Most of them. So 40 per cent of most of them?

Mr Bonney—Yes.

Ms PLIBERSEK—Thank you.

Mr Rundle—In mitigation, not particularly defending them, they have very strong risk management practices contributing to a lot of the other areas, so it does not necessarily mean that they have a large exposure as a result of that backlog.

CHAIRMAN—Thank you for that, or you might have left us with the wrong impression.

Ms GRIERSON—I want to take on that issue. It seems that, post September 11, the duty of care to one's employees has now increased markedly so that these security checks and processes are much more vital. Are you satisfied now that each department has a process in place or a strategic target in place to respond to that? Are you seeing evidence that that is actually happening posthaste?

Mr Rundle—We do not have information since the audit which covers that period to be able to help you, I am sorry. But the information coming out of the survey that is being conducted by Attorney-General's may contribute information that assists.

Ms GRIERSON—I will return to the outsourcing. Everyone has a high reliance on that now. The report found that only one organisation actually formally had written into their contract for outsourcing that there was a requirement for security clearances before that contract could be put into effect, and warning of a lead-in time. Have all the organisations now put in their contract in a formal way that contractors will be required to have a security clearance to take up the position or project?

Mr Tyrie—Certainly the Attorney-General's Department has.

Ms GRIERSON—Other departments?

Mr Fleeton—AusAID contractors working in AusAID formally have that in their contracts.

Mr Collins—That is the case for Customs.

Ms Hannah—It has been and is the case for Immigration.

Ms GRIERSON—So that means that, of all these organisations, all of them had to change bar one. I am assuming that everyone has actually made that alteration to their contract, because the finding was that only one organisation at the time formally had that. I will leave that with you. Thank you.

CHAIRMAN—To try to finish this thing up, I have a question that you could help us with. Audit found that organisation-specific security indicators should not replace but rather supplement the generic indicators. In terms of interdepartmental transfers, do you think that a central coordinating agency might be helpful in moving people from one agency to another and transferring their security clearances?

Mr Tyrie—It is an issue that has been before the security policy committee at a number of its meetings. The portability of security clearances is an issue which has not been resolved. In my view, it is just commonsense that if the minimum standard is reached in the PSM with regard to

a security clearance, and that is the standard for the Commonwealth, then it should be accepted across the Commonwealth. The matter of coordinating that has not been resolved yet, but I think there is a general acceptance that that should—

CHAIRMAN—Wouldn't you be a logical agency to perform that function?

Mr Tyrie—Logical, yes.

CHAIRMAN—Is there anybody here who has a major disagreement with what Mr Tyrie has said, that we should be able to transfer security clearances and that the Attorney-General's might be a clearing house? Does that make sense?

Mr Collins—We agree in principle but we—

CHAIRMAN—You reserve your right?

Mr Collins—What I was going to say was that we reserve the right to ask supplementary questions, being a law enforcement agency.

CHAIRMAN—I knew you would say that.

Senator WATSON—That would not infringe the privacy provisions, would it—shuffling these around various departments?

CHAIRMAN—How could it? Does ANAO have any winding-up comments with regard to the questions we have asked and the answers we have received?

Mr McPhee—Thank you, Chairman. I think the hearing today has been useful to say that the issue of security clearance processes should be on the radar screen of those in agencies charged with governance. They should at least review their own position. It is obvious some agencies are fairly well placed; others have the job ahead of them. Where there are backlogs and other issues, they obviously need an active strategy to get on top of the backlogs et cetera. I think it has been very useful.

CHAIRMAN—Thank you all for coming and participating in this rather broad-brush inquiry.

Proceedings suspended from 12.33 p.m. to 2.06 p.m.

BOWEN, Mr Eric Phillip, General Manager, Budget Group, Department of Finance and Administration

CAMPBELL, Ms Kathryn, Group Manager, Budget Group, Department of Finance and Administration

HUTSON, Mr Jonathan, Acting General Manager, Business Services Group, Department of Finance and Administration

JACKSON, Mr Barry Raymond, Branch Manager, Property Management Branch, Department of Finance and Administration

CRONIN, Mr Colin Douglas, Executive Director, Performance Audit Services Group, Australian National Audit Office

McPHEE, Mr Ian, Deputy Auditor-General, Australian National Audit Office

PALMER, Ms Barbara Alison, Director, Performance Audit Services Group, Australian National Audit Office

CHAIRMAN—We now come to the third audit report to be examined in today's public hearing. I remind witnesses 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.

The audit report being considered in this session is Audit report No. 4: *Commonwealth estate property sales*. I welcome representatives of the Australian National Audit Office and the Department of Finance and Administration to today's hearing. Thank you for coming today. This was undoubtedly a difficult audit, conducted under difficult circumstances. While the committee is certainly interested in asking some very detailed questions about why some decisions were made regarding the divestment of some government owned properties, perhaps, for me at least, one of the more succinct issues is where we go on in terms of the relationship between DOFA and the Australian National Audit Office. I would be remiss if I did not bring up this issue at the beginning of this public hearing. I have to say that this committee is concerned at what appeared to us last year to be a poisonous relationship between the two authorities. We did not appreciate it and we do not think it is in the interests of the Commonwealth that it continue. Would Mr Bowen and Mr McPhee have any comment on that, please?

Mr McPhee—Thank you, Chairman. I think we both agree that the relationship was not good at that particular time. We have talked about that. I am certainly positive that we are in better shape now. Certainly the relationships we see through the audits we are currently doing are much better than they were during this difficult time. I would just add that this was obviously a sensitive audit, a high profile audit and a high profile government property sales program. It is understandable there will be sensitivities when we are doing audits of departmental administration relating to policy advice and the consequences, if you like, of some government

decisions. It would also be remiss of me not to say that there will be sensitivities from time to time, and I would not say they just relate to our colleagues in Finance; they relate to other agencies as well. We certainly see relationship management as an important part of the way we work. We will be doing the best that we can to manage the relationship. Certainly it is my clear understanding that Finance will be doing the same.

Mr Bowen—Chairman and members, I would endorse what my colleague Mr McPhee has said. This was a difficult audit, I think, for both the Audit Office and for the department of finance. At times we will have legitimate genuine differences of view about issues. We have in the past, and I expect that there will, from time to time, be differences. However, what we are both working to achieve—I know the Audit Office is; I know that we are too in Finance—is the more difficult the issues become, the more we have to talk and interact to make sure that we narrow the amount of difference between us. On this particular audit, I was going to make a few opening remarks, if I have an opportunity at some stage.

CHAIRMAN—You will, absolutely. I just got in first.

Mr Bowen—You did; your prerogative. Our full intention is to do everything we can possibly do to have a good relationship. In fact, in the period since this audit—and it is now some considerable time; I just cannot remember how long, but a lot of water has gone under the bridge since then—I would think our relationships have improved. In a conversation I had in the last week or two with the Auditor-General, Pat Barrett, we both remarked that Finance and ANAO have much more in common than we have in difference. We have a mutual interest in most of the issues that the Auditor-General gets into.

CHAIRMAN—Okay. I want to make a brief comment, then I will ask you to make very brief opening statements. In this past week, I, by happenstance, had as a luncheon partner a head of a Commonwealth agency who told me how much he appreciated the work that this committee does. During the conversation he said that one of the things his agency had found extremely valuable was that, in working with ANAO, he found how well they could work together and that it allowed them to improve their processes and their procedures and to become more effective. He said, ‘We just don’t have a confrontational attitude with respect to Audit. We look forward to them coming in and we look forward to the results. If they say we did something wrong, so what—who’s perfect?’ I thought I would pass that on, for whatever it is worth, because I thought it was good anecdotal advice. Mr Bowen, would you have a brief opening statement? And I mean brief.

Mr Bowen—Very brief, Mr Chairman, and I endorse your last comment wholeheartedly. It is quite noticeable in this case that Finance disagreed with each of the recommendations in the report. I would have to say in some cases that was a fine line. There were genuine differences in our views on the methodology that was applied in some parts of the report. On some of the recommendations I think Finance’s disagreement was more a statement that it was already implementing the proposals put forward by Audit.

I think I have already said that there was a high level of dialogue and we will continue to have that with ANAO. On this particular audit, while it may not come through in the report, there was a high level of interaction between the officers of ANAO and Finance. Finance did provide a significant amount of written comment. However, where Finance could have done

better was in providing a much more fulsome final response in a consolidated, comprehensive way to the section 19 report. I know we have been criticised for not having done that. I do not think that will happen again.

Finally, I want to pick up on one point, which you may well raise but I would like to mention it. There is an implication in the report, maybe a misunderstanding, that Finance had or has a view that it did not have what I would call a whole of government responsibility for protecting the interests of the Commonwealth. Without getting into detail at this point, in fact within the body of the report there is a fulsome comment correctly attributed to Finance where we have explained what we meant by the statement that DOFA was not charged with the role of protecting the overall interests of the Commonwealth. On page 89 in the quotes, the second sentence is the covering sentence:

The overall interests of the Commonwealth were considered in the development of the Commonwealth's property principles and their implementation.

But I do not want it left on the record in any way that Finance does not believe it has a whole of government responsibility for value for money decisions. We do, and we treat that responsibility very seriously.

CHAIRMAN—Thank you for that, because that was my first question. Mr McPhee, do you have a brief opening statement?

Mr McPhee—I have an opening statement which I am happy to table in view of the tight timing on this inquiry.

CHAIRMAN—Thank you very much; we accept that statement as tabled. I have a question to Mr Bowen on the 15 per cent hurdle rate, which was a major difference between DOFA and ANAO. There are two parts to the question. First, why did DOFA dogmatically stick with such a high rate of return? I wish I could get that on my properties. Second, have you changed your mind?

Mr Bowen—The hurdle rate is a rate adopted by government. It was not open to Finance to arbitrarily change or take a view on a particular hurdle rate that had been adopted by the government. The government adopted that rate in 1996 when interest rates, the cost of funds, were substantially higher than they are today. It applied a risk premium to that cost of funds to arrive at a rate between 14 and 15 per cent—it was actually a band. The government has recently, in the latest budget in fact, adopted a revised hurdle rate. That is a rate of 11 per cent. That rate is aligned with the government's capital use charge rate and it is the rate that the government has said it will use in determining the appropriateness of long-term investment decisions.

CHAIRMAN—But did not the government accept the 15 per cent based on DOFA advice? Is not the 11 per cent and, in fact, the capital use charge based on DOFA advice?

Mr Bowen—Finance advises the government on matters such as that, of course, and we will continue to do that. But we cannot discuss the nature of our advice to government in public forums.

CHAIRMAN—Do you have any comment, Mr McPhee?

Mr McPhee—Certainly in terms of our audit mandate we would see it is quite legitimate for us to look at the advice provided by departments to government to assess, in our view, the accuracy or the quality of that advice and to comment publicly on that. In this report we have done so. We certainly do not feel constrained in that part of our mandate.

CHAIRMAN—I would not have thought that this committee was constrained either.

Ms PLIBERSEK—I want to clarify: Mr Bowen, are you saying that you may or may not have advised the government that a 15 per cent hurdle rate was reasonable and more recently you may or may not have advised them that a different hurdle rate is appropriate? You are not prepared to tell us whether DOFA gave the government that advice?

Mr Bowen—It is not normal for a public servant to reveal the nature of his or her advice to government. It is a well-established convention that public servants do not do that.

Ms PLIBERSEK—I will ask the question differently then. Where do you think the government may have got the impression that a 15 per cent hurdle rate was a good idea?

Mr Bowen—I am in no way saying that Finance did not advise. We advise on those sorts of things. But it is really quite inappropriate for me to disclose what our advice is to government. If the government wishes to disclose that, that is the government's prerogative, but it is not my prerogative.

Ms PLIBERSEK—Surely, though, it is fundamental, for us to work out whether this process was appropriately handled, to know whether—

CHAIRMAN—It does not matter who is in government, kid, that is the way it goes. That is the system. It has been that way for a long time.

Mr Bowen—I will be as helpful to you as I possibly can, but I cannot disclose the nature of our advice, as much as I might like to.

Ms PLIBERSEK—The Auditor-General's report suggests that that figure was arrived at after advice from the Department of Finance and Administration. Are you contesting that?

Mr Bowen—No. I have said we advised on those things, yes. We have recently advised again. What I am not saying is exactly what we advised. What I can tell you is how the 11 per cent has been derived. I am quite happy to tell you that. I am happy to tell you to the extent that I personally can—I was not there at the time—how the 15 per cent was derived. But you appreciate my position. I cannot reveal a confidence of what we actually advised the government.

CHAIRMAN—That is okay. I am with you. I will ask one more question. Then I will shut up and let my colleagues have a go at all of you. The audit report leaves me with the impression

that the government did not get value for money out of this process, which is the subject of this audit. Would you concur with that view, Mr Bowen?

Mr Bowen—I will answer that question in this way. The government adopted a hurdle rate of return. At the point of adopting that hurdle rate of return, it made a value for money judgment. That value for money judgment was this: it would not retain property, unless there was a public interest reason for doing so, that had an internal rate of return of less than the hurdle. So by the government's standard of a hurdle rate, the fact that properties that were sold did not achieve the hurdle rate meant that by definition the government achieved value for money under its criteria.

Ms KING—What period lapsed between the adoption of the 15 per cent hurdle rate and the actual divestment of the bulk of the properties? You said there were significant changes in the economic circumstances in that period.

Mr Bowen—Perhaps I will take the factual issue of the time difference and the amount of properties sold.

Ms Campbell—The Commonwealth property principles with the hurdle rate were established in 1996. Properties were sold from that time onwards and are continuing to be sold now.

Ms KING—So it is only now in this budget, in 2002, that the hurdle rate has been changed, despite there being significant changes in interest rates and economic circumstances during that period?

Mr Bowen—I did not quite catch the question.

Ms Campbell—The Commonwealth property principles have been changed in this budget to reflect those changes in interest rates and economic circumstances.

Mr Bowen—Can I just butt in for one moment. Could you restate the question? Are you talking this current financial year or next year?

Ms KING—In this budget it changed.

Mr Bowen—In the coming year?

Ms KING—Sorry, for the coming year. I said the 2002 budget. I did not say for which financial year. Given that you cannot tell us what advice you provided, I would like to ask a general question about that advice. Would you provide advice to government in relation to changes in interest rates and the impact that they may have on the hurdle rate?

Mr Bowen—From time to time we would provide that type of advice, yes.

Ms KING—How regularly would you do that?

Mr Bowen—I do not know that I can answer that. We are constantly providing advice to government on financial matters, both on our initiative on and on request.

Ms KING—In terms of advice in relation to how the hurdle rate is working, you would provide that as well in a general sense?

Mr Bowen—As required, yes.

Ms KING—As required. Am I still correct in saying that from 1996 to now, 2002, the hurdle rate remained at 15 per cent for that entire period—despite your advice, perhaps?

Mr Bowen—I did not say that. We can tell you that the hurdle rate has remained over that five-year period, yes.

Ms KING—I note that in particular—I have a particular interest in this—the Bendigo property sold for well below its initial valuation. To what extent is each property formally revalued at the time it is being prepared for sale? Did this have any impact on the decision?

Ms Campbell—The original valuations that were provided to the Commonwealth Property Committee were based on proposed leases and did not often take into consideration detailed due diligence of the properties. After detailed due diligence, it became apparent in a number of cases that the value was going to go down. Sometimes that was due to the physical nature of the property or also because the properties were not fully occupied by the Commonwealth—or any tenant, for that matter. I do not have at hand the Bendigo property, but we can see whether we have some material so that we can provide a little more comment on that property.

Ms KING—Were decisions changed on the basis of the due diligence, if the due diligence gave you information that was different from your initial valuation?

Ms Campbell—If the internal rate of return was still below 15 per cent, the property was sold.

Ms KING—Thank you.

Senator WATSON—In terms of a quartile type of presentation in relation to the hurdle rate of 15 per cent, can you give us the proportion of properties disposed of in each of the four categories?

Mr Bowen—Senator, you said ‘four categories’?

Senator WATSON—We are talking about a quartile type presentation, where the presentation would be in relation to the highest, the medium and then the lowest et cetera. I am just interested to see, in terms of that hurdle rate of 15 per cent, where the disposals occurred. Did most of the disposals occur at 10 per cent, 15 per cent? Did it happen between, say, 13 and 15 per cent? That sort of analysis would tend to worry me a bit and would confirm very strongly that the hurdle rate was far too high.

Mr McPhee—Senator Watson, on page 42 of the report there is some analysis that goes to that question.

Mr Cronin—At 12 per cent, for argument's sake, we would have retained something like 69 per cent of the properties by value.

Senator WATSON—You would have retained what they disposed of?

Mr Cronin—Yes.

Senator WATSON—69 per cent?

Mr Cronin—At a hurdle rate of 12 per cent, we would have retained 69 per cent and only sold 31 per cent.

Senator WATSON—But what actually did you sell?

Mr Cronin—If you move across to the 15 per cent, you will see that we sold 99 per cent by value. Essentially, everything that was put up for sale was sold.

Senator WATSON—Yes, but I want a clearer percentage in terms of these quartiles. Say that 13 to 15 per cent could be the top quartile. The next one would be, say, 11 to 12, or something like that. That is what I am interested in. I want to see whether—

Mr Cronin—We could construct that for you, Senator.

Senator WATSON—From what Mr McPhee has just told me, on trying to interpret it, it would appear that a lot of them are right up near the margin; is that right?

Mr Cronin—Yes.

Senator WATSON—So we have not been erring on the side of conservatism in terms of holding properties?

Ms PLIBERSEK—We have, or we have not?

Senator WATSON—We have not. We have been letting it go. This analysis is really critical for the Public Accounts appraisal of this. As the Chairman said, in terms of property developers, you might be looking for higher figures. But the government really is not in the business of property development. Certainly the cost of borrowings is a lot less than 15 per cent.

Mr Bowen—The cost of borrowing is very low. However, the government's view was that there is risk associated with holding property. That is our view; there is risk associated with holding property.

Senator WATSON—Minimal risk.

Mr Bowen—The other view the government had was that it was not necessarily in the business of owning property but in the business of using its resources in the best way to deliver services to the Australian people.

Senator WATSON—Absolutely right.

Mr Bowen—The government adopted this hurdle rate. The sales program flows from that.

Senator WATSON—I am not against a hurdle rate: the problem is with the level that hurdle rate is pitched at and the ability to vary that from time to time. In my view, and perhaps in Ms King's view, it should not have been static for such a long time; am I correct?

Ms KING—You are quite correct.

Ms PLIBERSEK—The risks associated with owning property would be predominantly that interest rates go through the roof; is that right?

Mr Bowen—There are other risks. There is an interest rate risk. There are facilities risks. At worst, of course, you have a September 11 risk, which we did not think about at that time, I am sure.

Ms PLIBERSEK—No. Presumably the buildings are insured, though.

Mr Bowen—They are insured for a range of things, yes. But there is also the risk that your business changes.

Ms PLIBERSEK—Sure.

Mr Bowen—In fact, many of the Commonwealth properties that have been sold have been occupied either by only a very tiny proportion of Commonwealth agencies or by private sector occupants.

Ms PLIBERSEK—There is a risk associated with renting, as well, isn't there?

Mr Bowen—Yes.

Ms PLIBERSEK—Depending on how good your contracts are—I am not looking at you at all, Mr McPhee, nor at the Audit Office—there can be quite substantial increases written into rental agreements.

Mr Bowen—There certainly can be. They can be as high as—very high.

CHAIRMAN—Were you trying to say 'as high as Centenary House,' Mr Bowen?

Mr Bowen—No. We are having a very good relationship.

Ms PLIBERSEK—Mr Bowen, you could use as another example the Australian Geological Survey Organisation building which, far from saving money, could cost the taxpayer a loss of \$95 million at the present value over 20 years. It is a pretty substantial loss, isn't it?

Mr Bowen—If that calculation is correct. Again, it comes down to the value of the funds and how that calculation is done. I am not sure whether here is the place to go through the technicalities of that calculation. But that property under that lease would still be sold today or tomorrow under the new hurdle rate that applies for next financial year.

Ms PLIBERSEK—What about the Department of Foreign Affairs and Trade facing a rent increase of 35 per cent to \$22.7 million, barely three years after the government sold the R.G. Casey building for \$217 million? Again, that is a fairly substantial risk that was not taken into account when the initial contract was written, I guess.

Mr Bowen—I will defer to Mr Jackson, who is familiar with the detail of that.

Mr Jackson—Whilst you are correct in saying that the new owner sought an increase of 38 per cent for R.G. Casey House, the end result was an increase—once it had gone through the appropriate negotiation clauses within the lease regarding rental increases—of \$6 per square metre.

Ms PLIBERSEK—Which is a total of?

Mr Jackson—It is approximate but indicative. It went from approximately \$350 to \$356 per square metre.

Ms PLIBERSEK—Which is a total of what per annum for what you use of the whole building?

Mr Jackson—When the rent is done, it is at \$350 per square metre per annum for that building.

Ms PLIBERSEK—I know. But what is the total, then? The figure we have got is \$22.7 million for what the Department of Foreign Affairs and Trade leases.

Mr Jackson—I believe that is what is the new owner sought to have. But the actual result would not be in that order.

Ms PLIBERSEK—It would be in what order, then? It would be about what?

Mr Jackson—That would be a question for DFAT. I am not totally familiar with what their current rental status is, I am sorry.

Mr Bowen—To put it into perspective, if that is the figure—and I accept what my colleague says—that is a very low percentage, six on 300.

Mr Jackson—It is two per cent or thereabouts.

Ms PLIBERSEK—So they sought 38 per cent but they got two per cent?

Mr Jackson—That is correct.

Ms PLIBERSEK—The other one was Discovery House, which is supposed to have a break-even point after only eight years. Have you had any further information about that?

Mr Bowen—While people are looking up the Discovery House details, I would say that this is a real area of genuine difference, I guess, in our methodological approaches. We do not accept that break-even methodology. Discovery House—

Ms Campbell—For Discovery House, the internal rate of return was 9.73 per cent at the time it was sold.

Ms PLIBERSEK—It was getting 9.73 per cent.

Ms Campbell—That is below the hurdle rate then and now and for 2003.

Ms PLIBERSEK—What I am curious about is that it is a sale and lease-back arrangement and that the Auditor-General's report suggests that after eight years there is a break-even point.

Mr Bowen—As I said, that is on one analysis. Our analysis would not show that. It would show that it was a value for money decision and that in fact it would still be a value for money decision based on a 10 per cent or a 9.5 per cent hurdle.

Ms PLIBERSEK—But your value for money decision, whether it is a 15 per cent hurdle rate or the lower 11 per cent hurdle rate, is not a methodological decision; it is an ideological decision, really, isn't it?

Mr Bowen—Well, no. The concept of a hurdle rate is not ideological.

Ms PLIBERSEK—But setting a high hurdle rate is.

Mr Bowen—The commercial property market, on average, for property trusts now would be yielding somewhere between eight and 12 per cent. I think I am right in saying that.

Mr Jackson—That is right.

Mr Bowen—As for what the government is saying by accepting a rate of 11 per cent, I will tell you what the methodology for that is. It is the 10-year average of the 10-year bond rate, to get a bit of stability into it. You are not investing by hopping into the market and hopping out. They are long-term decisions, whether you buy or whether you sell and rent. The government has adopted a rate which is based on that 10-year average of the long-term bond rate. It has added to that a premium for risk based on the 10-year average of the premium obtained in the equity market. It is not perfect, but it is a good approximation for a risk weighting on a broad spectrum of activity. That has resulted in the rate of 11 per cent.

Ms PLIBERSEK—Was the calculation the same basic one for the 15 per cent?

Mr Bowen—I believe the 15 was done on a slightly different basis. But both applied the capital asset pricing model that the ANAO recommends, in concept at least. But it was slightly different, in that it was more the interest rates at the time. We have now looked at a 10-year average, which we think is a better way to apply it for the future.

CHAIRMAN—Could we test that?

Ms PLIBERSEK—Yes. I would like to.

CHAIRMAN—Could we have a comment from the Audit Office on the most recent statements, please.

Mr McPhee—Mr Bowen said that perhaps the approach may not be perfect. We might agree with that. We may have some technical differences about the approach that has been adopted. In the main, and broadly, it is a reasonable approach to adopt. We would not quibble with the differences: that is what I am saying.

Ms PLIBERSEK—Can I clarify that? You wouldn't quibble with the way that the current 11 per cent rate of return has been calculated? Or you wouldn't quibble with—

Mr McPhee—I think we would not quibble with the outcome. We would have a slightly different approach to calculating the rate, if you asked us for a technical view. In terms of the outcome that has been achieved—that is, the 11 per cent—we would be within a per cent of it. I do not think it is worth arguing about.

Ms PLIBERSEK—You did quibble with the 15 per cent, didn't you?

Mr McPhee—Yes, exactly.

Ms PLIBERSEK—With the rate or with the calculation?

Mr McPhee—It was the calculation—and the resultant outcome, of course.

Mr JOHN COBB—I do not have a problem with the issue of R.G. Casey and what have you. But when you look at those three on page 107, with the agreement to rent above market to that extent, the implication is that the increased rent would have thrown it out to a reasonable extent on your 11 per cent. Certainly when you look at what is there, it does. What conditions were placed on the lease-back arrangements regarding future rent increases by the new owners?

Mr Jackson—The lease—and I am using AGSO as an example—contains a commercial escalation clause that identifies how future rent increases will occur. It is a combination of fixed escalator rates, CPI and market reviews. It also determines how that market review shall occur and what CPI rate shall be used. Those items were agreed in the negotiations with the tenants of the AGSO building, being AGSO themselves, who had engaged their own independent advisers to assist them.

Mr JOHN COBB—The figure of \$22 million might have been mentioned earlier. That is obviously over 10 years on R.G. Casey, which you were referring to. On a per annum basis, the figures over 10 years look to be one heck of a lot of money to me.

Ms PLIBERSEK—I am sorry, Mr Cobb. If you are asking about the figure that I was quoting before, my understanding is that the rent increase sought was an increase of 38 per cent to \$22.7 million per year, barely three years after the building was sold for \$217 million.

Ms Palmer—They were the facts available at the time of the report: the owner had sought an increase.

Ms PLIBERSEK—Yes. I am just clarifying it for Mr Cobb, with regard to what I was quoting before.

Mr CIOBO—I have a couple of questions about the hurdle rate of 15 per cent. I see there are three limbs to that: a rate of 6 per cent, a property risk premium of six per cent and then three per cent for what you term as the suboptimal nature of the current Commonwealth property portfolio. In what way is it suboptimal? Further, with regard to the determination of those percentages, is there an element of it that is really trying to measure the intangible? How long is a piece of string? Is that one of the principal causes of conflict, perhaps, in terms of the methodological approach to this type of thing?

Ms Campbell—I am sorry. I did not understand the last part of your question.

Mr CIOBO—With respect to the assignment of those percentages of the six, the six and the three, on page 39, is there a proportion of it that is a measurement of the intangible? You might try to value goodwill or something like that in a commercial sense—I cite that as an example—and so there is some disagreement about how you actually get down to those percentages.

Mr Bowen—This was, of course, put in place in 1996.

Ms Campbell—In 1996, when the Commonwealth property principles were being established, for the Commonwealth properties in question it was considered that there would be quite a large capital maintenance required on those properties in the coming years. There were no formal leases in place. There was no knowledge of adherence to local government regulations. They had been built by the Commonwealth on Commonwealth land, without reference to local and state government authorities.

Mr CIOBO—Was that because it was by shield of the Crown or something?

Ms Campbell—That is correct. There was some uncertainty about the asset that was being considered. My understanding is that it was considered in that context.

Mr CIOBO—What I am trying to determine is this. When you have the three elements of that hurdle rate of 15 per cent, is the disagreement that has occurred a consequence of a disagreement about what each of the three limbs should actually be, or is it over the fact that it is these three limbs? Do you understand what I am saying? Is the disagreement over the percentage, or over the actual inclusion of these elements?

Mr Jackson—We agree fully with a risk-free rate of six per cent. That is given to you by the market. We disagree with the risk premium being the market as a whole. The market as a whole risk premium includes everything from low value risk, such as property, through to dot.coms. That gives you the market risk. We would say that property has a specific risk associated with it. We would say that you should use the market risk and apply the beta factor, which is for property. There is some debate on the beta factor, but it would appear to be in the order of 0.5. Instead of using six, we would have said you should use the specific attributes of property, which meant that people require a lower than market return—because they did not have in that portfolio things like dot.coms and high risk things. We are not aware of why you would actually add on to this another three per cent, which is the third limb. We have not seen that in terms of the application of investment criteria in the Commonwealth. If we look at the literature that has been available in the Commonwealth in terms of discounted cash flow analysis stretching back to the 1970s, this is something that is not in accordance with that. We looked at the principles put out in the 1987 guidance issued by the then Department of Finance. We have followed that. That is the same approach that Access Economics followed in their two reports.

Mr CIOBO—Why use the six per cent, then, and why include that third limb of three per cent—given, as you phrase it, the suboptimal nature of the current portfolio?

Mr Bowen—This is what was done at the time.

Mr CIOBO—Sure.

Mr Bowen—Clearly there are different views about it. Ms Campbell has pointed out that the property portfolio at the time was not your blue ribbon—she did not use those words—property trust.

Mr CIOBO—Mr Bowen, are you saying that it was because previously the shield of the Crown had applied and a large investment was required to maintain facilities that you went above the 0.5, which might have been the average beta risk factor for property, to six? Is that also the reason why the three per cent is in there? Is that what are you saying?

Mr Bowen—My understanding of the way this was constructed is that the additional risk associated with the portfolio is reflected in that three per cent.

Mr CIOBO—Okay. Thank you.

Ms PLIBERSEK—I want to ask some questions about the actual arrangements that were made regarding the sales of some of the buildings and so on. We spent \$20.6 million on sales advisers, legal advisers, marketing and other consultants up to April 2001. That is a fairly significant figure. It includes over \$5 million for sales advisers, a figure which the audit report specifically cites as possibly too high. I am curious: if there was already a sales panel of seven real estate agents to manage the property sales, why was it necessary to appoint a sales adviser? What are the implications of having a sales adviser from the same firm contracted to sell packages 1 to 4 and 5 to 6?

Mr Bowen—There are a number of issues in your questions. Let me start and then I will hand over to Ms Campbell. These were very large packages and very large sales. They were not

your average sale of a residential property, which at times can become quite complex but, clearly, not anywhere near the magnitude of the complexity associated with these commercial properties, including getting them to a point where they were appropriate for sale both in a physical and commercial sense. So, yes, the fees in absolute terms are large, but in percentage terms they were well within the bounds that you would normally expect in an asset sale of that size and complexity.

Ms Campbell—I think you asked why a sales adviser was appointed when there was already a panel. Sometimes the sales advisers were appointed off that panel. They were just directly taken off. The panel was established as a generic panel to try to address most properties. When we were selling some of the properties, some of them had quite specific needs. It was sometimes assessed that the advisers on the panel were not best able to sell those properties. That was when some other sales advisers were sought.

Ms PLIBERSEK—Okay. There are a number of other questions I want to ask. However, it is three minutes to 3 o'clock. If I read you some questions, can you get back to us with the answers and take them on notice? Is that all right?

Mr Bowen—We can. I take it that we will get a transcript of this so that we can get them accurately. Or you could give them to us later, if you like.

CHAIRMAN—Of course. Mr Bowen, it will be on the Internet by next Thursday, I imagine.

Ms PLIBERSEK—No. I think that Hansard are saying that there will be a 10-day delay because of Senate Estimates and so on, probably. What I will do is give the questions to the secretariat and ask them to write to you.

Mr Bowen—That would be fine, yes.

Ms PLIBERSEK—Given my previous question, I would like to know why you rejected recommendation No. 2 in particular. There were several instances where, for example, one of the legal firms offered a discount for fees over the threshold of \$900,000 for packages five and six to reflect the experience gained in the earlier sales. The engagement for services was approved on that basis. However, a discounting arrangement was not reflected in contractual documents. I would also like to know why you decided to proceed with the property sales at Rockhampton, Bendigo and Wagga Wagga, when the revised valuation was much lower than the valuations used in the initial decision to divest the properties. To what extent did you use the criteria for AGSO property sales to select the successful tenderers? Why were bids accepted from non-conforming tenderers? I could just go on and on, but I think that is probably enough for the moment.

Mr Bowen—We would love to answer them now, but I appreciate the time constraints. We will be very happy to take them on notice.

Ms PLIBERSEK—Thank you. I appreciate that.

Ms KING—I have a question that I can put on notice as well, but I think Senator Watson has a question.

Senator WATSON—I checked with the Reserve Bank. Currently, as at 30 May 2002, the 10-year benchmark is something like 6.205.

Mr Bowen—Yes.

Senator WATSON—It has been quite low for quite a few years.

Mr Bowen—Yes.

Senator WATSON—I am a bit worried about the 10 per cent that you gave us.

Mr Bowen—10 per cent?

Mr Jackson—11 per cent.

Senator WATSON—That is what you are talking about.

Mr Bowen—No. The 11 per cent comprises two parts. It is a 10-year average of the long-term bond rate, which is slightly higher. It is about 7.3, I think.

Senator WATSON—That would be about right.

Mr Bowen—On top of that is a risk premium of 3.7 per cent—

Senator WATSON—Which we are querying in the case of some buildings. What we are trying to impress upon you is that for some buildings it might be okay, but for a lot of Commonwealth properties, the risk premium, I would submit, is quite low.

Mr Bowen—All I can say to you is that this is based on external research, but it is also the figure that the government has adopted as its hurdle rate.

Senator WATSON—The people who produced this information for Finance at the time, are they the same people who are defending the policy now?

Mr Bowen—No. I do not think so. In our advice, we have used publicly available material this time.

Senator WATSON—This time?

Mr Bowen—Well, we have not commissioned specific work is what I am saying. We have relied on publicly available work.

Senator WATSON—That is in determining your lower rate to 11 per cent?

Mr Bowen—Yes.

Senator WATSON—Obviously, there was some change in methodology compared with when the 15 per cent was set?

Mr Bowen—There is a slight change in methodology. We have simply adopted a capital asset pricing model using the risk-free rate on a long-term basis plus a market risk premium.

Senator WATSON—The audit report was dated August 2001, wasn't it?

Mr Bowen—Yes.

Senator WATSON—So you have recognised the issues raised by that audit?

Mr Bowen—We have. In our response to recommendation 1, which talks about the way in which the Audit Office would recommend that we go about the methodology, we indicated that we had reviewed the approach. The government had not taken a decision at that time, but it now has. Our approach is now much closer, I think it is fair to say, to the Audit Office recommended approach.

Senator WATSON—So a change in methodology does reflect the Audit Office's analysis and report?

Mr Bowen—We would say that it does and that it is quite consistent, within bounds at least, with it, yes.

Senator WATSON—It just raises this question: why was it not within the knowledge or ability of Finance to recognise that much earlier than before the Audit Office came in? It has obviously been quite a sea change.

Mr Bowen—It is a change, whether it is a sea change. It does reflect different market conditions now and a different portfolio, a different risk profile.

Ms KING—I would like to put a question on notice too, given the time frame. In both the sale of the R G Casey Building and the Bendigo Commonwealth Offices, in the original leases there were separate clauses in relation to payment between the agencies and DOFA. Why did DOFA transfer, in the case of R G Casey, the DFAT obligation to the private sector when it sold the R G Casey Building? That would also apply to the Bendigo building as well. Can you take that on notice, please. It is contained in paragraph 4.10 and 4.11 of the audit report.

Mr Bowen—We will.

CHAIRMAN—Does DOFA have any final comments to make?

Mr Bowen—I do not think so. We will be happy to take these questions on notice.

CHAIRMAN—I assume that if the secretariat has further questions you would not mind answering them.

Mr Bowen—We would not mind at all, no.

CHAIRMAN—We would appreciate that so that we do not have to bring you back again. ANAO, do you have any final comments to make, Mr McPhee?

Mr McPhee—No, thank you, Mr Chairman.

CHAIRMAN—We thank you very much for your attendance today.

Mr Bowen—Our pleasure. Thank you.

[3.06 p.m.]

CAINE, Mr Grant Douglas, Senior Director, Performance Audit, Australian National Audit Office

LEWIS, Mr Michael Kenneth, Executive Director, Performance Audit Service Group, Australian National Audit Office

McPHEE, Mr Ian, Deputy Auditor-General, Australian National Audit Office

ARCHER, Ms Alison Louise, Director, Heritage Assistance and Projects, Department of the Environment and Heritage

KEEFFE, Mr Kevin, Assistant Secretary, World Heritage, Australian Heritage and Education Branch, Department of the Environment and Heritage

GOSLING, Ms Karen Ann, General Manager, Cultural Development Branch, Department of Communications, Information Technology and the Arts

THORPE, Ms Rhonda Vivien, Assistant General Manager, Federation Fund, Cultural Development Branch, Department of Communications, Information Technology and the Arts

CHAIRMAN—We now come to the last audit to be examined in today's public hearing. I welcome to today's hearing representatives from the ANAO, the Department of Communications, Information Technology and the Arts and the Department of Environment and Heritage. I remind witnesses that these hearings 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. The audit report being considered in this session is Audit report No. 11 2001-02: *Administration of the Federation Fund program*. Ladies and gentlemen, thank you very much for coming to talk to us today. Ms Gosling, do you wish to make a brief—I overly emphasise the word 'brief'—opening statement?

Ms Gosling—Yes, I do, Mr Chairman. I will be brief.

CHAIRMAN—If it is pages, then I will stop you. I would prefer that we had Hansard record your statement.

Ms Gosling—It is about a page and a half.

CHAIRMAN—We would need about a minute or less.

Ms PLIBERSEK—You are able to table your comments in full, if you want to.

Ms Gosling—I do not have them in a form to give to Hansard. That is fine. I will decline from making an opening statement.

CHAIRMAN—We really want to ask you questions. Mr McPhee?

Mr McPhee—I will table a one-page statement.

CHAIRMAN—Thank you very much. We will accept that. I am not trying to deprive you of your democratic right. We have limited time. We will have lots of questions and we would prefer to ask questions.

Ms Gosling—I understand.

CHAIRMAN—Thank you very much. One of the questions that I have—and I do not know whether either of the departments can answer this or if ANAO have any clues—is that no Commonwealth department has a responsibility for monitoring the collective performance of the Federation Fund projects against the program's objectives. The Audit Office did comment in their report that it made it difficult for them to come up with a performance audit. Would either of you or both of you care to comment?

Ms Gosling—I can only reiterate the situation. After the projects were selected, the administration was divided between various departments. We have been getting on with the job of administering the projects for which we are responsible. In relation to one of the programs, the Federation Community Projects program, we have full responsibility for that program in DCITA.

CHAIRMAN—We had a look at that. Our Audit report No. 26, recommendation 2, recommended that the Department of Communications, Information Technology and the Arts implement its draft guidelines for the administration of grant programs. Have you done that?

Ms Thorpe—We have guidelines for the administration of the Federation Fund projects.

CHAIRMAN—No. For the administration of grants programs.

Ms Thorpe—For the department?

CHAIRMAN—Yes.

Ms Thorpe—My understanding is that the department has had draft guidelines in place for some time that have been with the executive. The department has also been waiting—

CHAIRMAN—No, not draft programs. We understand that you have draft programs. That is not what we recommended. We recommended that you get on and implement them so that they are no longer in draft.

Ms Gosling—They are not fully implemented, Mr Chairman. In some respects we have been waiting for the ANAO best practice report on grant administration as well: the *Better Practice Guide*.

CHAIRMAN—Do you have a comment, Mr McPhee?

Mr McPhee—The *Better Practice Guide* is due out very shortly.

Mr Lewis—It has in fact been launched.

Ms Gosling—And our guidelines are not far away. It seemed that it would be appropriate to take into account any further advice from the Audit Office before they were released.

CHAIRMAN—Thank you. We are getting there. The second recommendation was recommendation No. 3, which said:

We recommend that, after making grant decisions, all applicants, successful or otherwise, should be notified of the decision as soon as possible in writing ... advised of relevant appeal processes and provided with guidance for improving subsequent applications.

Have you any idea what you have done with that recommendation or are likely to do?

Ms Thorpe—No. We would have to take that on notice to give you a correct answer.

CHAIRMAN—My understanding from this audit report is that, with respect to the Federation Fund program that we are discussing today, it was many months after the positive decisions were made that the negatives were advised. Is that true?

Ms Thorpe—I was not there at the time, so I am not sure, but that may well be the case.

CHAIRMAN—That is what it said in the audit report. Mr McPhee, is that right?

Mr McPhee—That is correct, Mr Chairman.

CHAIRMAN—I have to tell you that it is a personal concern of mine. That recommendation reflects some of my words. When we ask people to put forward ideas for projects for capital funding—whatever program it comes under and whoever is in government it matters not—those that win get the money and they go on and use the money on whatever it is for. Those that lose all too frequently are advised late. When they are advised, they are simply advised, ‘You lost,’ rather than being provided with guidance on why they lost and what they might do better next time to have a better chance. Many programs are ongoing, as you well know. Obviously this one is not. We are not going to have another federation for a while, at least not in my lifetime, anyway.

Ms PLIBERSEK—Until we join with New Zealand and New Zealand becomes part of Australia.

CHAIRMAN—So you can understand that that is a concern.

Ms Gosling—Yes, Mr Chairman.

CHAIRMAN—Let us return to the overall program. I suppose it is an executive decision, not a department decision. The fact that there is no overall administration of this program is something that concerns me. Tell me the degree to which you have followed up on the projects under your control.

Mr Keeffe—We in the Department of the Environment and Heritage have our own program management system, with which we comprehensively evaluate the projects. You will notice that the draft report pointed out the standard funding agreement. We are quite keen on following up those evaluations. We can give you fairly comprehensive reports on how they are going. But I will defer to Ms Archer, who has day-to-day management responsibility.

Ms Archer—We monitor all our projects through our schedules in our agreements, which are very comprehensive and have reporting milestones all the way through. We have done that right through the life of all the projects—all of which are coming to conclusion now. We also have included evaluation criteria, for which they have to provide us with detailed reports right up to their final reports. They allow us to test the performance of the grants against the broad objectives of the program.

CHAIRMAN—So if someone came to you with a safety concern about one of the lifts at No. 4 Treasury Place in Melbourne, what would you have done about it?

Ms Archer—I would refer them to the managing agency, which was not mine.

CHAIRMAN—I see. Mr McPhee, if we were the agency that referred that complaint to the department, the department referred it on to the managing agent—

Ms Archer—The grant managing agency would be DCITA.

CHAIRMAN—How do we then go about getting assurance that our safety concern has in fact been looked at? Have we any recourse but to ask the Audit Office to do an audit of that lift at No. 4 Treasury Place in Melbourne?

Mr McPhee—I guess it depends very much on the feedback mechanism the agencies have to get feedback on that particular request to the project manager. In terms of the special audit, I would not like to receive a request to investigate how a particular lift is going but perhaps a broader scope audit would be appropriate.

CHAIRMAN—Then I will change my question slightly. If this committee had reasons to have concerns about the whole safety aspect of No. 4 Treasury Place, would it be proper for us to ask ANAO to consider auditing the factors surrounding safety associated with that building?

Mr McPhee—I certainly think the committee could ask us. Our first step would be to see what actions the managing agency had taken to address them. Our focus is very much on departmental or agency administration. If we could not get the answers there, of course we would speak—and may anyway—to the project manager. But we would hope that the agencies

themselves have arrangements in place to be able to manage those sorts of situations. They may have experience already that could bear on this, Mr Chairman.

CHAIRMAN—My colleagues have questions. I want to finish this scenario for a particular purpose, however. I understand that neither of your departments is administering the Abt Railway project in Tasmania. Is that correct?

Ms Thorpe—We are not.

Ms Gosling—No.

Ms PLIBERSEK—I think it is Transport and Regional Services, but I am not entirely sure.

CHAIRMAN—I wanted it on the record, thank you.

Ms PLIBERSEK—I have questions for the ANAO that relate to the report. One of the ways that you analysed the break-up of the funding was according to electorate. I was curious about what happens when you take the ACT out of that break-up of Labor and coalition electorates. The ACT, during the time that a lot of these decisions were being made, was facing an election campaign. In some ways, I guess you could say that there are two Labor seats but there was a very important Senate battle being fought there.

If you took out the \$174 million that went to the ACT, including the \$146 million that went to the National Museum, there were five other projects worth a total of \$28 million. How does that affect the balance of Liberal seats and so on, if you treat the ACT as a separate proposition, given the Senate battle that was going on there? Would that make the value of the approved projects about \$528 million to Liberal electorates, if you treat it as a Liberal marginal Senate position, and \$371 million to Labor electorates? It is quite a substantial difference, is it not?

Mr Lewis—It would obviously change the proportions.

Ms PLIBERSEK—The House of Representatives seats are not the only seats that governments are interested in winning, of course.

Mr Lewis—That is correct. But I am not sure that we have actually done that sort of analysis at this stage.

Ms PLIBERSEK—I was also curious that there were 21 projects approved immediately before the caretaker period. Did you want to comment on that?

Mr Lewis—We did cover that in the report. There was a large number of projects approved just before the caretaker period commenced.

Ms PLIBERSEK—You will not have looked at how many were scheduled to open or were opened during the federal election campaign, such as the NIDA theatre and so on, which incidentally was opened before it was ready.

Mr Lewis—We did not do any analysis of openings. We did an analysis of projects that were announced during the election campaign.

Ms PLIBERSEK—What was the proportion of those projects announced during the election campaign? Was it about half?

Mr Lewis—That sounds about right. We suggested that—picking up a point that the Chairman made—letting unsuccessful applicants know early on was important. We said that whilst the timing of announcements is very much up to the government—that is within their purview—it would be better if projects were announced as soon as possible after the decision is made.

Ms PLIBERSEK—So there were two electoral cycles affected by this, were there not? There was the 1998 election, when some of the announcements were made, and then there was the 2001 election, when a whole lot of completed projects were opened. If you plotted a map of the announcements of the projects and then the openings, you would probably find the dots bunched up around election time, would you not?

Mr Lewis—I could not comment because we have not done that sort of analysis, I am afraid.

Senator COLBECK—When you put together the agreements that were used between you and the agency conducting the projects, were those contracts standard agreements that you would have used under any other projects that you would be undertaking, or were they specific to these particular projects?

Ms Archer—Ours was specific to the project but was based on a model agreement that we had within the department already. We added to it the specifics in terms of the objectives of this particular program so that those objectives were reflected in the deed of agreement. In our case, it was actually based on the Natural Heritage Trust deed.

Ms Gosling—In our case, there is a standard form of grant deed. It has attached to it a schedule that is very much tailored to the specific project. It sets out the objectives and the milestones that the grantee has to meet as well as the payment schedule et cetera.

Senator COLBECK—So there would have been specific milestones and arrangements that would have to have been met as the project progressed for things like payment and things of that nature?

Ms Gosling—Yes.

Senator COLBECK—What monitoring of those milestones was undertaken specifically by the departments as opposed to the reporting process that was provided by the project proponents?

Ms Archer—We programmed our management of each of the grants and followed up close to the time that reports were due, to check that they had completed those stages of the projects. We had various checks that they had to provide at different stages, particularly in the planning

stages, where we chased that documentation and so on. So we monitored it very closely through each of those stages—through correspondence and, in a lot of cases, visits.

Ms Thorpe—Each of our projects is the responsibility of a project manager, who monitors in a similar way to Environment in terms of when reports are coming due; they liaise with the project to ensure that things are going ahead. Where problems came to light either we worked with the grantee through letters and phone calls or, when necessary, we visited them to try to assist them to keep progressing. We withheld their payments, where necessary, until we had had satisfactory reports provided that covered the appropriate milestone and we had been convinced that the project had been moving forward.

Senator COLBECK—Would those program managers have had specific experience in the type of project that they were involved in administering or supervising?

Ms Thorpe—It would vary. Some of my staff have come from a project management background in terms of other programs within the department. Others might not have had that, but they have had the guidelines and senior staff have worked with them so that they understood what they were meant to be looking for. A senior person has been overseeing the whole program to ensure that nothing fell through the cracks and that the staff understood what they were meant to be doing.

Mr Keefe—For Environment, we have got much the same approach except we do have a specialised area of our division that deals with program grant management. In that section, which now reports to me—it is only a recent change—we have work plans in place with the individual project managers that include as an assessment criterion their monitoring of grant programs that are performing adequately.

Senator COLBECK—So there was active follow-up and assessment of the reports that came into your departments rather than just taking the word of the project proponent?

Ms Gosling—Very much so in our case. In some situations, we have gone back to the grantee and asked for additional information or sought clarification of particular issues—how funding has been allocated et cetera.

Mr Keefe—Quite a deal of interaction with the project managers, with individual project proponents querying the information and assessing it. We are quite experienced in running other projects like this and ensuring that all targets and milestones are met. So it is the standard work practice to do so. It does take a lot of time. Not in these project cases, but some project proponents are somewhat tardy or a bit vague in what they return. So we have to keep chasing them up.

Senator COLBECK—How many of the projects that your departments have administered would have had significant time overruns?

Ms Archer—I do not have a specific proportion. There were a fair few that had early lags in the planning phases. We had to push them along to get them over the planning stage. Once the work started, they seemed to catch up quite a lot. We are now in a position where all work is basically completed.

CHAIRMAN—When is Federation Square going to catch up?

Ms Archer—I could not comment on it. It is not one of mine. Sorry.

Ms Gosling—Similarly with us, I could not give you a figure on that. But we had a similar experience in the early stages in terms of just getting the planning right for some of the projects. Over time, as they got under way, we found that they had generally caught up. We have a small number of projects that are still under way. We are working very closely with those grantees to try to move them along. I have some figures on each of the programs, if that is helpful, in terms of how many are completed or ongoing.

Senator COLBECK—What would be the scale or the extent of the time overruns, as an average to the scheduled completion date?

Ms Gosling—It is difficult. With each of the three programs, the major projects and the Federation Cultural and Heritage Projects Program—and we have the electorate based projects as well—there has been a variety of factors that have influenced the overruns with each of those separate programs.

Senator COLBECK—I am more interested in the major projects.

Ms Gosling—With the major projects, we have a couple where we are working with state governments and where we are not providing the full funding. We are a partial contributor to the funding. Either we are working on a major construction site or we are working, for example, with the Queensland Heritage Trails Network around the state of Queensland. It is made up of 31 individual projects around Queensland. Queensland are managing the projects. They are trying to secure recurrent funding for those projects from other sources, be it from private sources or local councils. They are trying to get a sense of ownership at a community level for those projects. So those projects have experienced some difficulty or there have been a handful that have had some delays because of trying to make sure that they have a secure financial footing before they are actually progressed. There really has been a variety of factors. In most cases, it is where we are providing part of the funding, I would say.

Senator COLBECK—In a circumstance where the project is predominantly or wholly funded by the federal government, how many of them would have significant time overruns, and what would be the scale of those time overruns?

Ms Gosling—I would have to take that on notice. I do not have that level of detail at my fingertips.

Ms Archer—In terms of the major projects that we administer—and there is only a very small number—Centennial Park, Moore Park, St Andrew's and Oddfellows Hall are all finished. The Belgenny Farm project was terminated. Those moneys were moved into the Sydney Harbour Federation Trust, which is an ongoing project that ceases to be a Federation Fund project from 1 July this year, as I understand it. I have not managed it. It is a long-term project.

Ms Gosling—Sorry, Senator, my colleague has actually pointed out to me that, in answer to your question, the answer would be that there is one major project that is still experiencing some delay where we, the Commonwealth, are the sole funder. There have probably been another three or four, where there might have been a delay of some months, that are actually moving forward, where we were the sole funder. So it has been a fairly small proportion of the number of projects overall.

Ms KING—You have now completed an audit into the major projects component and a separate audit into the cultural and heritage projects. Have you done any analysis of the community projects at all? Are there any plans to do so?

Mr Lewis—No. We have not done any audits in that area. It is certainly not planned at this stage.

Mr CIOBO—I have a question for Communications, Information Technology and the Arts. You developed comprehensive guidelines, as I understand it, in terms of risk identification and management but these were not endorsed by senior management. Why is that the case?

Ms Gosling—I am not sure what guidelines you are actually referring to. There have been a couple of sets of guidelines that we have used in guiding the management of the projects. One set of guidelines, the contractual issues paper, is actually referred to in a case study in the audit report on page 96. That has certainly had endorsement. In relation to the broader departmental guidelines, as I mentioned before, those guidelines are in draft and we are waiting. We wanted to clarify that there was nothing in the *Better Practice Guide* that is coming from the Audit Office. We wanted to tie into that, but they are certainly under way and not far away.

Mr CIOBO—Do you think the fact that they are still in draft form had any impact on the project management?

Ms Gosling—No.

Ms Thorpe—No, because we have project guidelines for the program, and a lot of thought was put into it within the actual division. It was an oversight in not getting senior management endorsement on them. But the program managers still knew what they had to do.

Ms Gosling—It was really an adoption of them on a departmental wide basis, and we have used them in guiding the management of this program.

Mr CIOBO—Environment and Heritage, you did not develop guidelines in terms of the actual project, did you? Did I read that correctly?

Ms Archer—No. We did not have specific guidelines for the program. We used both the ANAO *Better Practice Guide* and the departmental grants administration guidelines. We also conducted risk assessments based on a model we developed for the program.

Mr CIOBO—Based on that model, how effective do you think that was?

Ms Archer—It was actually extremely valuable. We assessed the risks associated with the projects across the board. On that basis, we picked projects which we felt had a slightly higher risk in terms of project management. We adjusted our management of them accordingly.

Mr CIOBO—I will ask both departments, then: what strategies did you have in place basically to ensure accountability was maintained, especially for small group participants, with respect to value for money and accountability across the board?

Ms Archer—We had all these sorts of appropriate checks in our project administration. We had requirements of independent audits of financial expenditure throughout the project, which required the receiving agency to go out and provide us with independently audited statements to show that the money they had received had been spent on the project appropriately. They had to break that down to a great deal of detail. That was done not just at the end but right through the project at various stages. They also had to provide us with other degrees of evidence in terms of the outcome reports, photographs and documentation of works carried out. In our case, they were all place-related heritage outcomes. We also had checks in place with our planning processes with both state bodies and with other heritage advisers on site, as well as our own visits, to make sure that they were complying with all the statutory requirements. They were some of the checks. There were probably an awful lot more.

Ms Thorpe—We had some similar ones. We also have annual audit requirements on our larger projects. Our projects are basically culturally based. They have had to comply with a range of cultural requirements, including plans for the development of their collections and ensuring that they comply with federal and state responsibilities—such as getting Heritage Commission approval, where necessary, and a range of those sorts of things—so that we know they understand how to manage their collections in an ongoing way and not simply how to build a building.

They have had financial accountability because all of the projects have to come to me. I make sure that the project managers have effectively taken into account all the various items for each milestone before they have been paid, discussing them with the grantees where there were any issues of noncompliance. Sometimes we have had to wait for a significant amount of time to ensure that we got what we wanted. In some of the major projects where we felt they perhaps were not going to complete their buildings to the required standards, or where they were not going to have enough other money to complete, they have had to demonstrate that other money was available. We have had state governments demonstrating that they would ensure that the rest of the money would be put into finished projects to the standard we had agreed. So then we were reasonably confident that we were getting the outcomes that the money had been given for.

Ms KING—You may not be able to answer this. I note that the Fort Queenscliffe project is not to go ahead because the Defence department is going to retain that property. It states in the footnotes of the appendices on page 115 that the funding involved has been reallocated but that the decision has not been announced. I assume they have been. Can you tell me what they are? Do you know?

Mr Caine—Sorry. We are not aware of the actual announcement.

Ms Thorpe—They have been announced. I cannot actually give them to you. The Department of the Prime Minister and Cabinet knows them. I would not want to guess because I might get them wrong. But I certainly am aware that the announcement has been made.

Ms KING—I assume that it would have been, given the timing of the report.

Ms PLIBERSEK—I have a question for the Audit Office team. Several weeks ago there were some reports in the Tasmanian media that suggested that the Audit Office had particular concerns about the Abt Railway arising from this report. Can you tell me whether this report has any particular mentions of that project?

Mr Lewis—No, I do not believe so, but we do mention it along with all the other projects.

Ms PLIBERSEK—Along with all the other projects, yes.

Mr Lewis—When we were looking at the management of the project by the department of transport, we did look at that particular project. There were some concerns regarding payments and the like. The department was also concerned about progress and payments and the like. The project was one of the projects that we looked at. We were satisfied that the department had acted correctly to protect the Commonwealth's financial interests. There are other issues to do with the Abt Railway concerning safety and the like that we are aware of and which have been brought to our attention. We have forwarded those concerns to the department of transport and have been following up on some of those issues.

CHAIRMAN—I will clarify that. It was about a year ago that two constituents came to me—both were professional engineers, had extensive railway qualifications and had long times on Puffing Billy—with very serious concerns about Abt Railway. On their behalf, I wrote to the Auditor-General and referred the following issue to him. The Audit Office then forwarded it on to the department of transport. So if anybody expressed concerns to the Audit Office, it was me as a local member. I was responding to my constituents. For the record, I still have those concerns, and I have more concerns today than I did in the beginning.

Ms PLIBERSEK—It is also the case, is it not, that Senator Brown contacted you with some concerns but that, following provision of detailed information by the state government and the Tasmanian rail safety regulator, no further action was deemed necessary by the ANAO?

Mr Lewis—That is correct, yes.

Mr Caine—We also received advice from the department of transport, which reviewed the information from the Tasmanian government.

Ms PLIBERSEK—The Tasmanian government has obviously acknowledged that there are safety concerns there because they are not running the railway at the moment. Your interest in it, however, is not relating to its safety at all; your responsibility goes to seeing whether Federation Fund money has been appropriately spent and appropriately accounted for. I wonder whether you could confirm whether that is the case.

Mr Lewis—That is correct. There are obviously safety concerns, such as those expressed by the chairman or Senator Brown. We want to make sure that the railway is as safe as possible and that Commonwealth departments are discharging their responsibilities.

Ms PLIBERSEK—It is not going to be safe if it is not running. If it is not running because it is not finished, then by definition it is not safe. Is that not the case?

Mr Lewis—I do not know why it is not running. Whether it is a safety concern or the fact that it is not finished—

Ms PLIBERSEK—I think they are doing remediation work along the length of the railway and there is some additional construction that is not complete at the Strahan end of the railway.

Mr Lewis—Yes. That is correct. I was there on holiday a few weeks ago.

Ms PLIBERSEK—It is a beautiful part of the country.

Mr Lewis—I saw it myself. Those sorts of issues are really beyond the scope of the audit.

Ms PLIBERSEK—So this report does not go to those issues at all?

Mr Lewis—No.

Ms PLIBERSEK—Thank you.

Senator WATSON—I am concerned that the intention for which the money was applied has been fulfilled. I would have thought your job is not complete if you just satisfy yourself about the progress and the propriety of the payments rather than see that the intention for the project has been substantially fulfilled and met on time.

Mr Lewis—That is quite correct, Senator. The Commonwealth funding was provided to provide part of the infrastructure for the total project. It was a joint government-private sector project. Commonwealth funding was provided for particular purposes, such as the restoration of the locomotive, the track and perhaps the railway carriages. That is what the funding was provided for. As far as I am aware, that is what has been purchased with the money provided. There are obviously other issues that have caused delays with this project. I understand that it is still not completed. Certainly in terms of the funding that has been provided by the Commonwealth, as far as we know, it has been spent for the intended purpose. I think the department requires a sign-off from the state Auditor-General to that effect.

Ms PLIBERSEK—Isn't it also the case that the deed of grant conditions not only require this annual statement from the Tasmanian Auditor-General but also require the provision of regular reports to the Commonwealth officers prior to payment of funds, in accordance with the milestones, and that there is an existing payment outstanding because the project has not, in fact, been completed? Is that your understanding?

Mr Lewis—That is our understanding.

Ms PLIBERSEK—Would that be a common form of a deed of grant condition? Would that be common to a lot of projects? Have you encountered delays in the completion of other projects?

Mr Lewis—It is quite common. That is the normal form of contract. A lot of them are slightly different, but that is the general idea. There have been other projects that have been delayed.

Ms PLIBERSEK—Can you tell us about some of those?

Mr Caine—Names do not roll off the top of my head. There were some minor delays with some Environment and DCITA projects. They were certainly not of the magnitude of the current one.

Mr Lewis—In appendix 1 of the report, we give a snapshot of the progress of a number of projects and when they are expected to be completed. The program was designed so that not all projects would necessarily be completed by the end of 2001, but it was expected that they would be substantially completed. There have been delays in a number of those projects. Obviously when we are auditing these things, we look to see whether or not payments have been made in advance of milestones.

Ms PLIBERSEK—Has that been the case on any project?

Mr Caine—No, not to any real extent. At the margins, there might have been some payments made. Some parts had been completed and advanced further while other parts had not been quite up to the stated milestones, so it was really a discretionary decision by the department to say whether or not, on balance, progress was sufficient to warrant this amount of payment, be it in full or a part payment of a milestone. Overall, no, they were not really paid in advance. May I also point out to the committee figure 4 on page 104. It shows in total the lags in payments for the program, which is indicative of how continual delays have been experienced over the entire program. In most cases, the delays in those payments reflect delays in achieving milestones. Therefore, payments have been delayed.

Ms PLIBERSEK—I ask the Audit Office another question. Much of this decision making process, as the report points out, was done inside cabinet. Are you clear as to whether the decision making was formally done by a subcommittee of cabinet?

Mr Lewis—It was not a formal subcommittee; it was more of an ad hoc committee.

Ms PLIBERSEK—With consistent membership or changing membership?

Mr Lewis—It was pretty consistent.

Ms PLIBERSEK—Did you have access to any paperwork from this? For the most part you would not because it is a cabinet subcommittee. Did you have any access to any of the rationale behind any of the decision making process undertaken by that subcommittee?

Mr Lewis—No. We had no access to the deliberations of the committee. We did seek advice from the Prime Minister, who was the chair of that committee. He provided us with a response, which I think we have provided in the report. We had access to the actual decision itself. As I said before, we did not have access to the deliberations.

CHAIRMAN—Notwithstanding your answer to Ms Plibersek before about funding and having to approach some tests, is it also not true that a percentage of completion is often in the eye of the beholder? I remind you of ANAO's audit reports on the Collins class submarines and on the Jindalee over the horizon radar. Do I need to go on in terms of projects where the money has been spent before the project has actually been completed? Is it not true that many times we get caught out overpaying for contracts without completion?

Mr Lewis—Absolutely.

CHAIRMAN—Thank you for that. Mr McPhee, I ask that the ANAO contact the department of transport and ask whether safety and completion concerns have been satisfied and follow-up and advise this committee, if you would.

Mr McPhee—Certainly.

Ms PLIBERSEK—If you are going to do that for one project, would it not be wise to do it for all the outstanding projects—if you are saying that there are overruns with more than one project?

Mr McPhee—We could certainly do it. An alternative could be for the secretariat to seek advice, based on the schedule, from all of the agencies involved. We could do it, if you like, but it is really subsequent information to the audit. We are happy to do it in one or two cases, but I am a bit concerned about the resource usage for the totality of them.

Mr Lewis—It may be that PM&C is still collecting these six-monthly reports. Perhaps the secretariat could write to PM&C and get an update, if that would help.

Ms PLIBERSEK—Could you give us an idea of how many you think might be outstanding?

Mr Lewis—We do not know at the moment.

Ms PLIBERSEK—Take a guess. Is it half a dozen or 200?

Mr Lewis—I really have no idea.

Mr McPhee—We could perhaps be guided by the other two agencies here in terms of proportion.

Mr Keefe—All our projects are complete.

Ms Gosling—Out of the major Federation Fund we have got a total of 17 projects. There are still seven ongoing. With the Federation Cultural and Heritage Projects we had 28 projects, and four are ongoing.

Ms PLIBERSEK—Are they running according to schedule, or are they behind time?

Ms Gosling—Not all of the projects are. A couple are behind schedule, yes.

Ms Thorpe—They were behind time.

Senator COLBECK—I want to ask a further question of ANAO: how many projects in the process of your review displayed safety concerns through the reporting process with the departments?

Mr Caine—The only one that came to our attention was the Abt Railway.

Senator COLBECK—I am a little disappointed that all the departments are not here and available for questioning this afternoon. That has restricted our capacity to review the process to an extent that I might have liked.

CHAIRMAN—I have been negligent. Do either of the departments or ANAO have any concluding statements to make before we wind this up?

Mr McPhee—No, Mr Chairman.

Ms Gosling—No, Mr Chairman.

Ms Archer—No, Mr Chairman.

CHAIRMAN—It has been a long and interesting day. I thank our witnesses and colleagues and the secretariat. I also thank Hansard.

Resolved (on motion by **Ms Plibersek**):

That this 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 3.54 p.m.