COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

Reference: Review of Auditor-General's reports-Audit Report No. 4, 2003-04

MONDAY, 8 MARCH 2004

CANBERRA

BY AUTHORITY OF THE PARLIAMENT

INTERNET

The Proof and Official Hansard transcripts of Senate committee hearings, some House of Representatives committee hearings and some joint committee hearings are available on the Internet. Some House of Representatives committees and some joint committees make available only Official Hansard transcripts.

The Internet address is: **http://www.aph.gov.au/hansard**

To search the parliamentary database, go to:
http://parlinfoweb.aph.gov.au

JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

Monday, 8 March 2004

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

Senators and members in attendance: Senators Scullion, Murray and Watson, and Mr Charles, Ms Grierson and Ms Plibersek

Terms of reference for the inquiry:

To inquire into and report on:

ANAO Audit Report No. 4 of 2003-04, plasma fractionation

WITNESSES

Committee met at 10.45 a.m.

BORDONARO, Mr Paul, General Manager Bioplasma, CSL Ltd

COCHRANE, Mr Warren John, Group Executive Director, Performance Audit Services Group, Australian National Audit Office

DAVIES, Mr Philip, Deputy Secretary, Department of Health and Ageing

HOLBERT, Ms Frances Elizabeth, Executive Director, Performance Audit Services Group, Australian National Audit Office

LOUDON, Mr Michael, Assistant Secretary, Manager, Procurement Branch, Department of Finance and Administration

MORAUTA, Dr Louise, First Assistant Secretary, Acute Care Division, Department of Health and Ageing

CHAIRMAN—Ladies and gentlemen, thank you for coming this morning. I open today's public hearing, which is the second in a series of hearings to examine reports tabled by the Auditor-General in the 2003-04 financial year. This morning we will be taking evidence on Audit Report No. 4: *Management of the extension option review: plasma fractionation agreement*. We will run today's session using a roundtable 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 will 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 to respond directly to each other.

Second, given the length of the program, statements and comments by witnesses should be relevant and succinct—and I emphasise 'succinct'. 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 a committee statement about the broadcasting of proceedings. In particular, I draw to the media's attention the need to report fairly and accurately the proceedings of the committee. Copies of this committee statement are available from secretariat staff.

I welcome representatives from the Australian National Audit Office, the Department of Health and Ageing, the Department of Finance and Administration and CSL Ltd. You will understand what we are discussing. Do any of the representatives wish to make a very brief opening statement before we proceed with questions? No? Thank you.

One of the reasons we are here is that in October 2000 we tabled our report No. 378 which focused on the plasma fractionation agreement review and we made two recommendations. One

of those was that ANAO conduct an audit, and they have done that. We are here to review that audit as part of the formal requirement in our act that defines that this committee report to parliament on every audit by the Auditor-General. I simply imprint that on people's minds to make them aware—if they are not aware already—of the seriousness with which we review these kinds of issues. In reviewing that agreement, this committee had ANAO do an audit report. They have done it and we are here to discuss that audit report. The second recommendation we made—recommendation No. 9 of report No. 378—states:

The Committee recommends that the Chief Executive Officer of the Department of Health and Aged Care assess the skill base and training needs of its contract managers, and ensure that appropriate legal and technical advice is readily available to them.

I have a letter dated 8 March 2001 from Michael Wooldridge, who was the Minister for Health and Ageing at the time, regarding this recommendation. Essentially it is advice from the minister, and so it is policy. Among other things, it states, 'The department has taken a number of steps to improve its contract administration in the area of blood and blood products.' These include a number of things, and the second dot point states, 'Raising staff awareness of relevant documentation, such as the department's chief executive instructions and the Department of Finance and Administration's *Competitive tendering and contracting: Guidance for managers*.'

It is my understanding that, in considering whether to extend the CSL contract for blood fractionation products beyond 30 June this year for a further five years or to negotiate a new contract, the department decided unilaterally—without discussing the issue with CSL—to not extend the contract and to enter into negotiations for a new shorter term or other contract. In doing so, it did no cost benefit analysis whatsoever, despite the fact that, in responding to our recommendation, the minister said that it would take note of DOFA's *Competitive tendering and contracting: Guidance for managers*, which requires that contracts be tested for value for money for the Commonwealth. Can Health and Ageing tell us why it did not proceed with competitive tendering prior to making the decision and advising CSL? You also then advised the minister and therefore PM&C at the last minute.

Dr Morauta—Perhaps I might go to a few of your lead-up points, Mr Chairman. The matter we are looking at here is the decision not to renew the agreement. That was the advice we gave the minister. The question of what happened next—that is, after the decision not to renew—was not the subject of advice at the same time. That was the subject of separate advice and separate processes. I just want the committee to be clear on that.

CHAIRMAN—Let me be clear: do you consider that a decision not to extend a contract means that the Department of Finance and Administration's guidelines that state it should be based on a cost benefit analysis need not be followed?

Dr Morauta—At the time we had some legal advice which suggested that the guidelines were not completely clear but, in any event, we placed great importance on the economic and financial issues around the decision or recommendation not to renew the contract. So, whether or not we were bound in that matter, we took a measured approach to that question of economic and financial consequences.

CHAIRMAN—Pardon me if I border on being rude, but I would have thought, even regarding minutiae of legal opinions, that logic and commonsense would tell you that when you are dealing with hundreds of millions of dollars of public funds a year any decision regarding extending a current contract which involves consideration of whether there will be some kind of a new contract, either with the same company or with someone else, would be based on whether or not this was to the benefit of the purchaser.

Dr Morauta—I believe that is the case and that is what we did. On pages 49 to 50 of the report, the main disadvantages of extending the PFA are noted and they are all in what you might call the economic financial area. The current pricing arrangements were not the most advantageous available to the Commonwealth; the current—

CHAIRMAN—Hang on. That is fascinating. Based on what cost benefit analysis?

Dr Morauta—Based on the fact that this was a 10-year contract which was struck at a completely different point in the history of the market and based on the history of the relationship with CSL.

CHAIRMAN—So you tested the market for these products and felt that there was some chance you would get a better price for product?

Mr Davies—We were not in the situation—

CHAIRMAN—I would have thought that was called cost benefit analysis.

Mr Davies—The situation is less one of testing the market than one of being aware of developments in the environment. I think there are a number of references in the report to the fact that the market for the manufacturing and supply of blood plasma products is changing and has changed significantly and is likely to change even more rapidly over the coming years. So I think the point we are making here is less that we went out to a competitive tender but more that we were mindful of the impact that changes in the market would have on the pattern of demand, and hence supply in the Australian market, and the fact that the original PFA was not conducive to us as a nation capturing the benefit of those changes in the marketplace.

CHAIRMAN—Could I ask DOFA their view of this issue?

Mr Loudon—The requirements are, as you mentioned, in relation to an analysis of: what is the best way forward under value for money?

CHAIRMAN—That is essentially saying ‘cost benefit analysis’.

Mr Loudon—It can take different forms, including cost benefit analysis as a proportion of the decision making process. The issue for us in the guidance, particularly with contract options, is that that was part of a process of evaluating what value for money meant and that that should be set out when moving forward for a decision. It does not necessarily mean market testing in itself but that the criteria on which you are going to evaluate value for money should be set out—that is one of the major portions of the guidelines—and then you evaluate against that criteria. That could include—as Health has mentioned and as is in the report—an analysis based on market

conditions and the changes in market conditions. But, in itself, that may not be sufficient, depending upon the size, risk and profile of the procurement.

CHAIRMAN—This committee views its recommendations and the responses to the recommendations—and the follow-through on what people say they are going to do—extremely seriously. Is it the department's view that Health and Ageing did not follow DOFA guidelines in this instance?

Mr Loudon—Well, let me—

CHAIRMAN—Do you want me to find what you told us in writing?

Mr Loudon—We disagreed that the Commonwealth procurement guidelines did not cover the extension of options. I think there was some discussion in the report and in the process of the audit—

Ms PLIBERSEK—And in the FMA.

Mr Loudon—and also in section 44 of the FMA Act in relation to the fact that, in our opinion, very clearly the guidelines were designed to encompass what we thought was a value for money decision in the extension of the contractual option. So you had already entered into a contract, it had obligations and you would assess that. We do not describe the nature of that assessment, but we would expect that value for money is assessed as part of that, yes.

CHAIRMAN—CSL—again, continuing on with the first basic question after your listening to all these statements—were you at any point brought into discussion with Health and Ageing regarding a contract extension?

Mr Bordonaro—No.

Ms PLIBERSEK—This is a question for Health. Basically, you are saying that you thought you could probably get these products cheaper elsewhere. Is that the assessment you made?

Dr Morauta—No; cheaper than the arrangement we had with CSL under the current agreement.

Ms PLIBERSEK—Or under a new contract. Why in that case wouldn't you start negotiations with CSL a bit earlier so that you could use the potential contract renegotiation as a leveraging point? I do not understand why you would not renew the option but also, at the same time, not start negotiations until so close to the expiry of the contract.

Dr Morauta—Because the government had not taken a decision to have a new contract with CSL. The only decision they took was not to renew the previous one. As you can see from the US FTA announcement, governments were obviously considering a wider range of options than just going with CSL, so the wider range of options had to be tested before a decision was taken.

Ms PLIBERSEK—Don't you give CSL an enormous advantage in negotiating new contracts if you leave things so late in the piece?

Dr Morauta—Not if you decide to negotiate with somebody else or use another process.

Ms PLIBERSEK—So you did not use any of the information that you considered during the steering committee processes as a basis on which to talk to CSL at all?

Dr Morauta—No. CSL has confirmed and we confirm and the report confirms that we did not discuss the extension of the PFA with CSL. We discussed lots of other things with them. We have an ongoing operational relationship with them, and we also were working at the time on some minor changes to the PFA which we subsequently agreed with them.

Ms PLIBERSEK—But you not only did not use it to discuss the extension; you did not use it to discuss any renegotiation. That is what is a little surprising to me.

Dr Morauta—No, the extension. We did renegotiate the 10-year contract. We renegotiated that during this period.

Ms PLIBERSEK—Now you have, but we are talking about 2002; at that time you were not using any of the process that you were going through to talk to CSL concurrently about a renegotiation of a contract.

Dr Morauta—Of the current contract or an extension of it?

Ms PLIBERSEK—Of a renegotiated contract, not an extension.

Dr Morauta—We did discuss and reach agreement with CSL on some changes to the current PFA.

Ms PLIBERSEK—When did you reach agreement with them?

Dr Morauta—I do not know.

Mr Bordonaro—Mr Chairman, the deed of contract variation was executed in January 2003, which varied the existing agreement.

Ms PLIBERSEK—Can Health explain to me why, when the deadline for exercising the option was 23 June, the steering committee advice to the minister did not arrive until 11 June 2002?

Dr Morauta—The department went through a number of processes in considering the recommendations it would make and made the recommendations on a timeframe which enabled the minister to take the decision.

Ms PLIBERSEK—But there was a subsequent piece of advice from the steering committee to the minister on 20 June. Is that right?

Dr Morauta—Yes.

Ms PLIBERSEK—So the minister did not think the 11 June advice was adequate and asked for more information?

Dr Morauta—I cannot speak on behalf of the minister.

Ms PLIBERSEK—Was the steering committee asked for more information?

Dr Morauta—No, I do not think so.

Ms PLIBERSEK—Do you know why the subsequent 20 June advice was given?

Dr Morauta—I think that would be a question for the minister's office to answer.

Ms PLIBERSEK—You provided the advice; do you know why you provided the advice?

Dr Morauta—I think we might have provided the same advice.

Ms PLIBERSEK—You provided it twice. Did they lose the first advice?

Dr Morauta—I cannot comment on that.

Ms PLIBERSEK—Was it additional advice or was it the same advice again?

Dr Morauta—My understanding is that it was the same advice.

Ms PLIBERSEK—So the minister's office had two weeks to make a decision about whether they accept your advice or not. Do you think that was an adequate timeframe in which to allow the minister to make a decision about spending over $100 million a year?

Dr Morauta—Yes.

Ms PLIBERSEK—You think two weeks is enough time. So, in December 1999, when the ANAO advised that early planning would be necessary in deciding whether to exercise this option, you were not inclined to start the process then of drafting this advice?

Dr Morauta—That is a completely different point.

Mr Davies—Perhaps I can just come in at this point. The report does go into—and our response in appendix 1 explains this in detail—the fact that the Stephens Review of the blood sector should be seen as part of a much broader process of addressing the issues, including those raised by this committee at the end of 1999. So to say that we did not pick up the issue until the steering committee first met I think is to ignore the quite considerable body of work that was undertaken in the interim period.

Ms PLIBERSEK—This question is to the ANAO. In your view, if people were faced with this possible decision about whether to exercise an option or not and there was another body of policy work being decided concurrently, would it be good to take the precaution of starting to

examine whether to exercise the option a little earlier than six months before the option runs out rather than to wait until the policy work is completed in the hope that that would give you firm guidance about whether the option should be exercised or not?

Mr Cochrane—I think it is pretty clear in our report that we felt that things were left too late. Because of that late start, there was late consultation with the major players at the end of the day. Just given the size of the contract, our experience in other departments is that there would have been a lot larger lead time—even allowing for the Blood Review. I think the Blood Review reported before the steering committee was formed.

Ms PLIBERSEK—Indeed. The Blood Review was in March 2001 and the steering committee was formed in December 2001. Is that right?

Mr Cochrane—Yes.

Ms PLIBERSEK—That is quite a time lag. Would Health like to discuss why there was such a time lag—if you say that you were waiting for the results of the Blood Review before making any decisions?

Mr Davies—I think the report of the Blood Review was actually agreed and published a couple of months later, if I remember rightly. I may be wrong, but that is my recollection of the chronology.

Dr Morauta—It was released in June.

Mr Davies—It was released in June; thank you. The steering committee first met formally in December?

Dr Morauta—Yes, but work commenced within the department prior to the formal gathering of the steering committee on the matters that were to be considered by the steering committee.

Mr Davies—As I am sure you can imagine, a reasonable amount of preparatory work goes on before the first formal meeting of that committee.

Ms PLIBERSEK—And none of that preparatory work could have been done before the release of the report?

Mr Davies—There was work going on concurrent with the deliberations of the Stevens committee and the publication and consideration of its report that could be considered to be preparatory work. I do not think there is a point where we fire a starting pistol and say, 'This is now preparatory work from the steering committee.' The whole body of knowledge within the relevant areas of the department could be deemed to be preparatory work—a lot of working papers prepared for the Stephens Review, for example.

Ms PLIBERSEK—But specifically about whether to exercise the option on the contract or not?

Mr Davies—I would not know what the level of detail would be but, in view of the fact that the whole decision whether to extend or not was set against the context of an evolving blood sector—developing science and developing technologies—I think again it is not easy to say whether a particular deliberation was relevant to an issue or not. I do not think it is a black and white issue. It is all building a body of knowledge amongst officials.

CHAIRMAN—I want to follow up briefly on two of those answers. Could CSL tell us if the 'late' decision—that is, late in our view and in ANAO's view—to not extend the contract put CSL under some pressure regarding the future of their business?

Mr Bordonaro—Reading the recommendations that came out of the Stephens Review in June 2001, it would be my view that CSL expected there to be a second agreement at some time and therefore that the first agreement would not be extended. So in CSL's thinking we were expecting that the current agreement would not be extended.

CHAIRMAN—In your view, that then included the possibility that you would not have the business?

Mr Bordonaro—There was a possibility of that, because obviously out of Stephens came the recommendation that there would be a second agreement. It was a very comprehensive review done by what I would describe as very eminent Australians. In CSL's thinking, obviously there is always a possibility of anything, but we did believe that the probability was that there would be a second agreement.

CHAIRMAN—Health and Ageing, you spoke before about the FTA with the United States affecting the timing and relevance of this issue then, and that it still does. Can you tell us when those negotiations formally started and when Health and Ageing started to take a potential FTA with the United States into account?

Dr Morauta—I am sorry, Chairman; I did not say that that was what was being considered at the time. I said that, when the government made announcements about the US FTA, it moved into the public domain that the question of alternative arrangements had been considered by the government. I did not say that it was the US FTA at that time which influenced their thinking. But the government were looking at all the options, as I am sure anybody would want them to, at the time they came to look at what would happen next.

CHAIRMAN—Why muddy the waters by throwing that in when it has absolutely nothing to do with this inquiry whatsoever?

Dr Morauta—I thought it might be helpful because it indicated a direction of thinking.

CHAIRMAN—I see. If tomorrow, unbeknown to the department, the government announces that it has commenced negotiations with the USSR for an FTA in which we are going to throw open to consideration our whole public health system, would you have taken that into account a couple of years ago?

Mr Davies—Perhaps I can add to what my colleague has said. The reference to the free trade agreement—and, indeed, I am sure, a wholly hypothetical free trade agreement with the Soviet

Union—is merely an illustration of the fact that this is an environment where things change; it is not a stable environment. I have referred to some of the scientific and technological changes. My colleague has referred to some of the geopolitical contextual changes. Unlike the period covered by the first PFA, which was certainly scientifically fairly stable, the blood sector and the environment in which it operates have become more unstable. So I think my colleague's reference to the FTA was more by way of an illustration of a general principle than to suggest a specific causal relationship.

CHAIRMAN—In making the decision not to extend the existing agreement with CSL, did you take into account that you might use either some potential competitor or overseas markets to put competition into the equation with CSL and therefore get a better value for money outcome for the Commonwealth?

Mr Davies—Another of the contextual issues is the question of government policy on the self-contained nature of the Australian blood system. I think I am right in saying that the Stephens Review made some reference to the possibility of changes in that environment. But there is a counterview which argues for maintenance of what is currently the government's policy setting that very much restricts the ability for overseas players to enter this market.

Senator WATSON—I have a number of questions for the Department of Health and Ageing. You highlight the economic and financial benefits and also the changing nature of the market as two of the principal reasons why you chose a particular course of action. Given that the rationale for your course of action was basically that you felt it was better value for money to change the nature of the contract rather than to continue it, could you outline how each of the principles underlying value for money—that is, efficiency and effectiveness, accountability and transparency, ethics and industry development—were achieved in your particular proposal? That is my first question. You spoke of economic and financial benefits and the changing nature of the markets. In relation to the first one, value for money, please tell us about the four factors underpinning that philosophy.

Dr Morauta—I think the efficiency and effectiveness one is very much at the heart of those three points that were taken into account. The question was: is the government likely to get the best value out of a contract that was signed 10 years ago in the context of a sale in a privatisation exercise and when the market is changing so rapidly? That is the connection to efficiency and effectiveness that we saw in our deliberations.

Senator WATSON—But how was the market changing? You have made general statements, but we need to know: what changes in the market were affecting this contract?

Dr Morauta—Many countries have switched the treatment of haemophilia largely to non-plasma based product. They are using what is called recombinant or synthetic product. In other OECD countries, this change has by and large occurred. It was possible that there would be a policy change in Australia which would switch most treatment for haemophilia to a different kind of product. That would then completely change what it was that governments were going to purchase from CSL and it would sit quite poorly with the provisions of the 10-year PFA.

Senator WATSON—But there had not been a change in policy, had there? You were presuming there would be a change in policy.

Dr Morauta—It was a possibility that needed to be taken into account in considering this matter.

Mr Davies—In a sense, it is a risk management issue whereby extending the contract in its original form with CSL would have effectively locked us in, notwithstanding any possible future changes in government policy on the use of recombinant products. To extend the contract would have locked us into paying for, if not actually using, what in many countries would be regarded as an outmoded product.

Senator WATSON—You have answered the first factor. What about accountability and transparency?

Dr Morauta—We believe that our recordkeeping and accounting processes met this standard, but perhaps the chair would like to ask ANAO whether they thought the recordkeeping and so on were appropriate.

CHAIRMAN—ANAO, could you respond to that?

Mr Cochrane—I will let my colleague answer in a general sense. But clearly we would have liked to have seen some of this decision making transferred into the financial analysis around the contract.

Ms Holbert—In terms of what the committee did, there was meticulous recordkeeping of all of the things they were doing. Our concern was with what was not there.

Senator WATSON—What was not there?

Ms Holbert—As we discussed earlier, on the financial side of things we would have expected a lot more consideration of what the potential costs of alternatives were. The analysis that was relied on was a scenario analysis taking into account some of these things that Health are mentioning at the moment in terms of possible changes in the market, but without measuring that against what else you might be able to get and what the pricing might be in the absence of purchasing such products.

Senator WATSON—In terms of ethics?

Dr Morauta—I think the processes were appropriate. We did consider at a number of junctures specific ethical issues which required debate in the committee. So I think there was a very appropriate consideration of ethical matters.

Senator WATSON—Despite the fact that there was very little consultation with CSL at this level?

Dr Morauta—That, in fact, was one of the points where we felt there was an ethical issue involved, which was that we considered that to consult with CSL might place CSL in an advantageous position against potential competitive suppliers in the market before a decision had been taken about how to proceed.

Mr Davies—Page 87 of the report states:

... the Department considered that it should not give a potential advantage to one supplier over other potential suppliers in the industry.

Senator WATSON—At the same time, if you are talking about the changing nature of the market, surely you should have given CSL some indication of your thinking so that they could have responded accordingly; otherwise they operate from a position of status quo rather than having the potential to meet your new requirements, your new demands, if you think this is going to be a permanent shift.

Mr Davies—CSL are an organisation of sufficient scale and competence that they would be fully abreast of developments in the marketplace. I cannot speak for CSL obviously, but I would assume that, in their own modelling and strategic planning, they would be aware of these issues without our bringing them to their attention.

Senator WATSON—But that is a presumption on your part in terms of the hypothesis that you were playing with between yourselves.

Mr Davies—In our dealings with the private sector, we have to assume—and rightly so—that the private sector is able to address its own interests.

Senator WATSON—In terms of your decision making in meeting that value for money criterion, where does industry development fit in?

Dr Morauta—I could be corrected by others who understand these guidelines better than me, but I think the issue there is that, if you have a process which compares people with an Australian presence to those with a non-Australian presence in some process, then consideration has to be given to how different suppliers bidding in a procurement exercise can contribute to Australian industry development. I think that is what that means.

Senator WATSON—You talk about value for money and you said that the Australian price is something like 75 per cent of the prices in European markets and 60 per cent in other commercial markets, so it would appear that the Commonwealth is already getting pretty good value for money. How are you going to improve on it, considering that CSL is a monopoly supplier? Who else would you go to?

Dr Morauta—I think negotiations are occurring currently between the National Blood Authority and CSL about prices for the forthcoming new agreement. I am not sure that it would be appropriate for me to discuss that matter here.

Senator WATSON—But you talk about getting better value for money, it being in your long-term interest not to continue the current arrangement and that the record shows that Australian prices average 75 per cent of prices in Europe and 60 per cent of those in other commercial markets. So it would appear to me that we seem to be getting pretty good value for money, even though we are dealing with a monopoly. But you say that you could go elsewhere. Where are you going to go to get comparable products?

Dr Morauta—The value for money consideration is not just about absolute price but about the conditions under which prices are triggered, the mix of product that is required and also, in the case of the PFA, the provision that CSL revenue must be no less than the revenue received in a previous year. So the value for money of a contract is a mix of price and other considerations.

Senator WATSON—I know. But we are still not getting much information; we are still talking in generalities. Where is this other supplier that you keep referring to? There is the possibility of going to another supplier; where is this other supplier?

Mr Davies—The existence and identity of another supplier depends largely on the products that we are seeking to purchase. For the current blood plasma based products, there is no other domestic supplier. There is obviously the possibility of another supplier entering the Australian market or what is known in the business as toll fractionation, which is exporting Australian plasma for fractionation overseas in a protected environment and reimporting it for use here. Both those options would clearly take time to implement, but they are possibilities.

Senator WATSON—But isn't CSL involved in both of those?

Mr Davies—CSL is present in Australia.

Senator WATSON—And engages in this work?

Mr Davies—CSL, I understand, also performs toll fractionation for other countries. If we stay with CSL then toll fractionation is not an issue. But if we again hypothesise a shift towards recombinant products, non-blood based products, obviously the number of potential suppliers increases significantly.

Senator WATSON—You have not articulated very clearly the changes in the product mix. Again, you have given us generalities, but you have not come down to the specifics which we are looking for. CSL does seem to be reasonably competitively priced, according to the information that we have. But you disagree, because you think you might go elsewhere but you do not know where you are going—and that is a worry. It is all very well to say these things, but we have to be convinced about the authenticity of these other suppliers and their reputations.

Dr Morauta—They were only part of the story. Apart from renewing the PFA, the other two main options were a new contract with CSL or going to another supplier. The way that might be structured or pursued was a matter that was still under consideration.

Senator WATSON—You say that, apart from discussions on extension issues beyond 2004, there was quite good dialogue relating to strategic management and operational matters. If what you tell me now was really the case, it really throws into doubt some of your bona fides. CSL advised ANAO:

The ANAO Report outlines the lack of effective communication between [Health] and CSL for 'ongoing operations and for strategic purposes'.

Taking out the extension issue, which I can understand, there is a lot of inconsistency, which worries me.

Mr Davies—I am sorry; do you mean inconsistency between our view and that of the ANAO?

Senator WATSON—The ANAO's position obviously was based on information that you gave them in terms of communication, because that is where they got their advice from. So was there really this close level of consultation and communication, or was there not?

Mr Davies—Between ourselves and CSL?

Senator WATSON—Yes.

Mr Davies—We consider that, throughout the life of the contract up to and since the announcement of the decision not to extend, we have maintained a very good and productive working relationship with CSL, as befits commercial partners. I cannot speak for CSL on that matter, but that is certainly our view.

CHAIRMAN—Does CSL agree with the statement that has just been made?

Mr Bordonaro—Very much so.

Senator WATSON—On the other hand, you have obviously withheld a little bit of information from them, because you believe that there are other suppliers. But you have not told me who those other suppliers are going to be or under what circumstances they will supply.

Mr Davies—The opportunities for other suppliers to enter this market are driven to some degree by the government's policy in two areas. One is the self-sufficiency in the Australian blood derived products, and the second is the substitution of blood derived products by recombinant products. Until those policy issues are resolved, we do not know what it is that we are going out to buy and, therefore, we do not know who the alternative suppliers are. But, in a more general sense around the industry, there are numerous other companies that have the technology to supply blood based products and/or are currently supplying recombinant products around the globe. I do not know the identity of those companies to the degree that I can recite them to the committee today, but they certainly exist.

Senator WATSON—In what is purported to be the Australian product, is there the degree of clinical accuracy—because, again, CSL prices are consistently significantly below imported prices?

Dr Morauta—That was not a matter we were deciding. We were starting at the broader question of how the government should proceed on procurement. Clearly, if the government came to an exercise where it was buying these products overseas, the question of clinical quality and safety would be very important.

Senator WATSON—But you say that you have no idea of what your product mix is likely to be. So wouldn't you frame the contract in the light of possible changes in the product mix?

Mr Davies—That is precisely the rationale for not extending the previous contract. The decision that was announced in 2003 does not require us to take the business away from CSL.

The decision announced in 2003 was merely that we would not exercise the option to roll over the previous contract with CSL.

Ms GRIERSON—You have tried to fill in some gaps for us, and the gaps that we have perceived come from the ANAO directly when they state that they found:

... a lack of detailed work undertaken during the Steering Committee process to clarify the contract's terms including analysis of potential for benefits to the Commonwealth from continuation of the existing terms ...

Do you agree with the statement that there was a lack of detailed work undertaken?

Dr Morauta—No.

Ms GRIERSON—ANAO, would you like to clarify what you mean by 'a lack of detailed work undertaken'?

Mr Cochrane—It is largely within the area that we were talking about before in terms of having a proper financial analysis done on the alternatives available to the department in purchasing products.

Ms GRIERSON—Health would suggest to us that extending the option would mean that they could not change or vary it in any way. Would Finance accept that?

Mr Loudon—Without knowing the detail of the contract arrangements and of the exercising of the option, it is hard to say. Whether it is better to base negotiations on an existing contract or completely start from scratch is the issue that we would say the value for money equation needs to look at.

Ms GRIERSON—My view from reading the reports would be that the Blood Review suggested that CSL should be the preferred partner in this agreement and in the supply of blood products but with a view to perhaps having a different contract with different terms. However, Finance and I think ANAO would have known that the option of extending it, if you could marry both those needs together, was a financially attractive one to the Commonwealth. Would you agree with that?

Mr Loudon—I might need to clarify it, but I will answer and then see whether it makes sense. In making a decision on whether to extend or not, you would look at the attractiveness of using the current contract. I think that would be our opinion.

Ms GRIERSON—If you could have got up the deal that you wanted with any changed conditions in it, do you think that could have been exercised?

Mr Loudon—As I said, it probably would be a starting point to look at whether the existing contract could be negotiated to suit future requirements. I do not have the detail to be able to answer that.

Ms GRIERSON—ANAO, do you have a view on whether that could have been possible, or do you just feel perhaps that was not pursued at all?

Mr Cochrane—We say that there were no discussions with CSL. Clearly in this audit we are not looking at whether the department should have renegotiated another contract or let the extension occur. We are looking at the extension in itself and saying that the extension decision needed to be based on a proper analysis. That analysis probably would also support the decision of whether you were going to renegotiate with CSL or, indeed, take on some other supplier.

Ms GRIERSON—CSL, do you feel that you could have continued negotiations with the Department of Health and Ageing or with the National Blood Authority to have renewed that option within terms that everyone would have been happy with?

Mr Bordonaro—This is only a view, but it perhaps would have been difficult.

Ms GRIERSON—Were you ever asked?

Mr Bordonaro—No, we were not asked or consulted, and this is an opinion only. Everything is doable, but it probably would have been difficult.

CHAIRMAN—Could you clarify that? It would have been difficult to make any changes to an extended existing contract?

Mr Bordonaro—There might have been some very, what I would describe as, difficult issues to agree in terms of variation to that agreement.

CHAIRMAN—Would those difficulties extend to a new contract?

Mr Bordonaro—That is what is happening now.

Ms GRIERSON—In that interim period during which the option expired and you now have a short-term contract, have your costs increased through there being uncertainty for your Australian providers or overseas providers? Because of this uncertainty, have you had to renegotiate contracts down the line or set up different arrangements that have cost you more?

Mr Bordonaro—Dealing with overseas suppliers is a constant issue that we are involved in. I do not believe that there has been any need to renegotiate existing agreements with any of them because of this particular issue. Costs are going up and there are currency and various other factors. It is very difficult to say that uncertainty caused by the non-extension has directly caused issues where we have had to work with overseas suppliers to renegotiate costs; no.

Ms GRIERSON—Department of Health and Ageing, who was on the steering committee that reviewed that position?

Mr Davies—The steering committee referred to throughout the document?

Ms GRIERSON—No, your steering committee that reviewed whether you would take up that option or set up a new contract and which then advised the minister for health.

Mr Davies—I think it is documented. On the four-person steering committee were SES officers from the department, including the TGA.

Ms GRIERSON—So they were all internal departmental personnel, not anyone from the industry, the wider sector—stakeholders particularly?

Mr Davies—Not on the committee. But, as the report explains, the committee through the task force obviously made extensive use of expert consultants.

Dr Morauta—And the Blood Review had given parties in the sector the opportunity to comment on those two terms of reference that referred to the PFA.

Ms GRIERSON—CSL, do you envisage that that contract will be long term, or do you have any idea of what term that contract will extend over?

Mr Bordonaro—There is no clarity at this stage as to what the term of the new agreement would be, no.

Ms GRIERSON—Finance, do you have a view on that?

Mr Loudon—No, I am afraid I do not.

Ms GRIERSON—Do you think the negotiated US FTA, which opens our market up to tender in 2007, will limit the life of that contract?

Mr Loudon—I am not familiar with the new arrangements; they are outside of our realm.

Ms GRIERSON—It is nice to see that the department of health might make an input on that.

Mr Davies—I have a correction for the record: the free trade agreement does not signal necessarily an opening up of our market; it merely signals that a review of that issue will be undertaken.

Ms GRIERSON—When would a review be undertaken?

Dr Morauta—By no later than 1 January 2007.

Ms GRIERSON—If you made recommendations regarding that, they would impact on contracts.

Mr Davies—I am sorry; I thought you said that the FTA had made a decision that the market would be opened up.

Ms GRIERSON—I thought it would go to a tender.

Mr Davies—No. The FTA merely initiates a review—

Ms GRIERSON—With the view of going to a tender process.

Mr Davies—That is a possible outcome of it. I put that purely to correct the facts.

Ms GRIERSON—That helps; thank you. I am left with great doubts because extending the option, which I think would have been financially very advantageous to us, was not pursued and not investigated—given that the Blood Review said that CSL were the preferred partner for the Commonwealth and they thought it should continue. Page 83 of the report states that the Blood Review concluded that Australia's future plasma fractionation needs would be best met through the national facility operated by CSL Ltd. I can only say that, although they had some recommendations about changing it to a new contract, they certainly still did signal that the national facility that was existing under the direction of CSL should continue.

Mr Davies—I would take the opportunity to refer you to paragraph 3.9 on page 47 of the ANAO report where it actually explains that the Blood Review noted that it supported the 'establishment of a new, shorter-term plasma fractionation agreement rather than an extension of the current one'. A decision in June 2003—

Ms GRIERSON—Did they give any reasons for that?

Mr Davies—I believe that is elaborated in the paragraph you were quoting from earlier. The issue we are discussing here is whether or not to extend the previous contract. Therefore, the decision made is exactly aligned with that recommendation of the Blood Review.

Ms GRIERSON—Yes. We know that but we do not feel that the financial side of that negotiation was at all tested, and that is our only concern. It was not tested. The financial costs of that option were not reviewed against another new contract and you did not look at the benefits that would have flowed, or not flowed, from either contract. We are just concerned that that option certainly does not seem to have been thoroughly investigated; therefore, we cannot be assured that we are going to get the best financial deal. Yet we all would agree with you that value for money in this case would have some very major issues attached to it, considering the health needs of Australia.

Mr Davies—I am sorry. I thought the specific line of your questioning was that the department had acted in a way that was inconsistent with the recommendation of the Blood Review. I was merely trying to point out that the Blood Review did indeed recommend non-extension.

Ms GRIERSON—And that should have been costed. That is my major point. I would have thought negotiations with CSL should have taken place to see whether the two needs—a contract that gave you some new options and the best financial position for the Commonwealth—could have been married together. But those negotiations did not take place and those costings were not put on the table. ANAO are concerned that procurement policies and guidelines be applied to options as well as to contracts and we should see that they are applied. If they were, we would know that your decision making was fully accountable and we could all accept that. I will leave it at that.

CHAIRMAN—Health, do you believe that audits add value to your processes and operations?

Mr Davies—Very much so.

Dr Morauta—Very much so.

CHAIRMAN—Do you think this committee and its reports add value to your processes and your organisations?

Mr Davies—Again, very much so.

Dr Morauta—Yes.

CHAIRMAN—Health, before you decided to accept the Blood Review holus-bolus without doing a cost benefit analysis—that is what everybody else thinks you did, even though you do not think so—did you take legal advice to determine whether or not product mix was an important consideration of the current contract?

Dr Morauta—I do not think it was around product mix, but we did establish that the terms of the current contract were that the option to extend was to be on the same terms and conditions as the existing contract. So I think the legal advice we took was about the nature of the contract.

CHAIRMAN—You keep bringing up the potential for the Commonwealth to change its mind about whether or not you use whole blood products or what the product mix will be in any particular treatment procedure. I wonder if you took legal advice on whether or not the current contract precluded any changes in that degree of product mix. Evidently you did not.

Dr Morauta—No. I think we took advice on the provisions of the contract which would go to what happens if there is a change. I am sorry, when you first asked the question, I was not clear what it was about. We took legal advice on the terms and conditions of the current contract and what that meant.

CHAIRMAN—If we have further questions about that, will you mind if we put them to you in writing?

Dr Morauta—No.

Senator WATSON—Did the audit examine any probability analysis of the various options or alternatives that the Department of Health and Ageing had been referring to?

Ms Holbert—What we saw was a scenario analysis where the department were testing against the provisions of the contract as it currently stood and against their interpretation, based on their legal advice of that contract, of what various changes to the product mix would mean, and they then determined that the contract was not in the best interests of the Commonwealth. We are saying that there was no pricing of any alternatives and we had an additional problem in that we had conflicting legal advice as to whether or not Health's understanding of how the terms of the PFA worked was correct.

Senator WATSON—You say there was a probability analysis but it did not extend to the price consequences of each of those alternatives?

Ms Holbert—There was no costing because you can only get the costing if you have price information about alternatives. What they were looking at—

Senator WATSON—They did not have price information about alternative products?

Ms Holbert—Yes. The scenario analysis was that, if you assume the PFA means that you cannot give CSL less than they have had in the previous year and if you then decide there are whole areas of product you no longer wish to take, you will be overpaying for the product you do take. That was the scenario analysis conducted by Health. We are saying that, if that is the case, there is no other information to say what the price of the remaining products will be, or, if you are going to an alternative supplier, what the prices of those will be. So, although the scenario analysis was there, we felt it was insufficient.

Senator WATSON—Incomplete and inadequate for the decision that was finally made.

Ms Holbert—We felt it was insufficient to make the recommendation.

CHAIRMAN—Finance, what are the recognised procedures for assessment of best value for money when agencies are striking agreement with private sector service providers?

Mr Loudon—It is a big question.

CHAIRMAN—Be fairly brief.

Mr Loudon—This will be brief. It depends upon the actual instance. In relation to value for money, there are a number of influencing factors on what the costs of the process will be: how large the contract is, what the risk profile is. Those analyses would need to be done. Another factor is the nature of the market, which has been a big issue this morning.

CHAIRMAN—In relation to the first thing you said, do you believe that Health undertook to accomplish what you believe the guidelines encompass in this instance?

Mr Loudon—It is difficult for us to judge. We did not have the in-depth analysis that the ANAO had. We did come in at the end of the process. I know that the department asked for additional information in relation to the financial and economic analysis that was undertaken for the decision making. We are still of the view that we would want to see the information that was put together by Health. But their view of what was necessary to make the decision was obviously different to what ours continues to be.

CHAIRMAN—Finance, you promulgated a procurement circular entitled ‘Evaluating options in procurement contracts’. The guidelines state that sufficient time be set aside and all that. Do you think Health allowed sufficient time to undertake the evaluation processes in the issue we are discussing?

Mr Loudon—Again, based on the information that has been provided to us on whether the process commenced and when it commenced, it is difficult to say, but it seemed that the decision was late in the making and that was in short one of the reasons we wanted to be more explicit in our guidance.

CHAIRMAN—Does ANAO concur with that view?

Ms Holbert—Yes.

CHAIRMAN—That circular spells out the requirement to evaluate programs on a whole-of-life basis. Finance, in your view, was the evaluation of the plasma fractionation agreement alternatives sufficiently rigorous?

Mr Loudon—Again, we did not see the evaluation, but we pointed our whole-of-life basis very much to say it included all extensions of options. So the life of the current contract, including the extension and whether that met the whole-of-life basis, included all of the costs that could be identified.

CHAIRMAN—ANAO, in your view, was the evaluation of the agreement alternatives sufficiently rigorous?

Mr Cochrane—No.

CHAIRMAN—ANAO, you view effective communication between parties as a prerequisite to good contract management. Do you think the absence of discussions in this instance between the agency and the supplier—that is, Health and CSL—allowed effective communication to take place?

Mr Cochrane—It is a long question. We think the two of them should have been communicating.

Ms PLIBERSEK—You do not think that would have advantaged CSL in future negotiations?

Mr Cochrane—It is a mystery why you cannot talk to them about the extension on the one hand but you can talk to them about a renegotiated contract. Where the disadvantage comes for other players in the market is a bit of a mystery to me.

CHAIRMAN—Health, because there was so little time available to the minister to consider her options, was she effectively compelled to agree with her department's advice and agree to the rejection of the extension option?

Dr Morauta—I cannot answer that question. It is a matter for the minister.

CHAIRMAN—Does Finance have a view?

Mr Loudon—No.

CHAIRMAN—You have no view?

Mr Loudon—Well—

CHAIRMAN—You might have a view but you are not willing to state it?

Mr Loudon—It is up to each department and their minister's office to work out what is sufficient time.

CHAIRMAN—Does ANAO have a view?

Ms Holbert—Our view was that it seemed to occur very late. The minister got her first briefing on 11 June suggesting she write to the Prime Minister. On 20 June she got another briefing saying, 'You need to make the decision yourself.' The decision had to be made on 21 June.

CHAIRMAN—ANAO, what measures would you recommend be adopted to prevent another area or another agency repeating Health's very late management of the assessment of the PFA extension option?

Mr Cochrane—Compliance with the new Finance guideline would be a good start.

CHAIRMAN—Did you understand that question, CSL? Do you have a response to that?

Mr Bordonaro—Not really, no.

Ms GRIERSON—CSL, would you agree that you were in a win-win situation: being able to renew an extension option that was satisfactory to you and also being the person who negotiated a new contract that was acceptable?

Mr Bordonaro—At the time of course we did not know that. The only thing we really had was the recommendation that came out of Stephens. There was no certainty at that time as to who was going to win or lose.

CHAIRMAN—During this inquiry today, Health has frequently referred to the Stephens Review, the Blood Review, and has accepted its recommendations. Finance and ANAO, in your experience, does the government always accept recommendations of independent committees?

Mr Cochrane—No.

CHAIRMAN—I can guarantee that the government does not always accept our recommendations. I must admit that we have a better strike rate than anybody else around this place—that is my view—but the government does not always say yes. I just say that for whatever it is worth. I thank Health, Finance, ANAO and CSL for coming today. I understand CSL had some initial reluctance to appear, but we appreciate your being here because you have added value to these discussions. I would like to thank the observers, the secretariat, my colleagues and, last but not least, 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 11.59 a.m.