COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

**Reference: Contract management in the Australian Public Service**

FRIDAY, 31 MARCH 2000

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**JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT**

**Friday, 31 March 2000**

**Members:** Mr Charles *(Chair)*, Mr Cox *(Deputy Chair)*, Senators Coonan, Faulkner, Gibson, Hogg, Murray and Watson and Mr Andrews, Mr Brough, Mr Georgiou, Ms Gillard, Mr Lindsay, Ms Plibersek, Mr St Clair, Mr Somlyay and Mr Tanner

**Senators and members in attendance:** Senator Hogg and Mr Charles, Mr Cox and Ms Gillard

**Terms of reference for the inquiry:**

To inquire into, and report on the management of Commonwealth contracts focusing on:

- the adequacy of contract specifications including the design and framing of the initial contract documentation;
- the adequacy of mechanisms for ensuring management accountability and facilitating Parliamentary scrutiny of contracts, including the method by which the Auditor-General is given access to the accounts of contractors;
- quality assurance and performance monitoring of contracts—adequacy of documentation of contract deletions, side agreements, and amendments;
- risk allocation and risk management
- levels of accreditation and expertise of contract management personnel; and
- the extent to which corporate memory is being preserved in agencies to a level sufficient to protect Commonwealth interests.

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**FOX, Ms Julie, Principal Legal Officer, Legal Services Branch, Corporate Services Division, Department of Health and Aged Care**

**GUNN, Ms Stephanie, Assistant Secretary, Corporate Development Branch, Corporate Services Division, Department of Health and Aged Care**

**TOMKINS, Mr Neville, First Assistant Secretary, Corporate Services Division, Department of Health and Aged Care**

**CHAIRMAN**—The Joint Committee of Public Accounts and Audit will now take evidence as provided for by the Public Accounts and Audit Committee Act 1951. I declare open this public hearing of the Joint Committee of Public Accounts and Audit inquiry into contract management in the Australian Public Service. Today the JCPAA will take evidence from the Department of Health and Aged Care, the Department of Immigration and Multicultural Affairs and the Department of Defence. Before swearing in witnesses, I refer members of the media who may be present at the hearing to the committee's statement about the broadcasting of proceedings. In particular, I draw the media's attention to the need to fairly and accurately report the proceedings of the committee.I welcome representatives of the Department of Health and Aged Care to today's hearing. Thank you very much for your submission and thank you for coming today. Do you have a brief opening statement you would like to make or will we start asking questions about your submission.

**Mr Tomkins**—We will make an opening statement. Thank you, Mr Chairman, and the committee for the opportunity to appear before the committee and to also supplement the comments which we have made in our submission. The Department of Health and Aged Care has dedicated resources over the last several years to improving the skills, knowledge and expertise of those departmental staff involved in contract management. We have taken the opportunity, through this, to develop a particular approach, and that approach is to ensure that all

of our staff understand the importance of good contract management. It is essential that the tender and procurement process as well as the negotiation of any contract with the department is done professionally. Our staff must also meet legislative and regulatory requirements. Accordingly, the department has centralised the development and provision of advice, support and training for contract management. The day-to-day management of the contracts is the responsibility of the respective divisions. The centralised resources work very closely with departmental staff to improve their knowledge of the appropriate processes. They also raise with staff some of the common issues to address within a contract.

I will briefly outline the department's framework for effective contract management. The department has formalised its framework through various instruments such as, firstly, our Chief Executive Instructions, commonly referred to as CEIs, and these instructions are provided under the Financial Management Act. Drawn from that, the department has developed a quite comprehensive list of procedural rules. We also have standard contracts. We have also put in place and continue to further develop a comprehensive range of training programs and, further to that, specific technical assistance to our staff.

The framework also covers issues such as, firstly, how to manage the procurement process; secondly, advice on the development of a statement of requirement; thirdly, quality assurance programs; and fourthly, the exploration of ethics relating to contract management. The department's objective for this framework is to ensure the actual process of contract management is very explicit and is understood by both parties from the very beginning. It also ensures that the contract implementation phase is able to focus on delivering outcomes based on the establishment of a trusting and transparent relationship. Thank you, Mr Chairman.

**CHAIRMAN**—Thank you. One of the things that this committee is interested in is particularly the circumstances that you have outlined where you have gone to a central procurement unit, which I understand gives advice but does not drive the contracts or the purchase orders or the contract negotiations themselves. At what dollar value do they become involved, or do they simply only respond to requests?

**Mr Tomkins**—The answer to that is that the actual day-to-day management of the contract remains the responsibility of the line divisions. The purpose of the central units—and we have two of those—essentially is to be able to advise and to support but they do not actually manage the contract itself.

**CHAIRMAN**—We understand that, but what triggers their involvement?

**Ms Gunn**—If a tender is to be released, the area of the department that provides that tender number provides a recommendation that they talk with the area that provides the advice on procurement, so in the process of the development of an RFT staff are encouraged to go through to the area that provides them with all of that advice and training.

**CHAIRMAN**—If a section or an area of your responsibility is going to place a contract for service provision that is worth, let us say, several hundred thousand dollars over several years, are they required to go to the central unit or do they only go if they decide they would like to?

**Ms Gunn**—There is no formal mechanism requiring them to go to the Unit. However, the advice that those units give is around the standard contracts, the standard procedures. Most people now involved in the divisions in procurement activities have participated in training provided by the department. That provides a series of checklists, guidance, steps to follow. A number of divisions have their own procedural rules that must be followed in accordance with the requirements expected by the various heads of those divisions.

**Mr Tomkins**—In other words, there is no dollar amount that triggers the involvement of the central advisory units. However, we are trying to develop a culture where the staff managing contracts feel as though they are strongly supported by the central units and, indeed, that they are encouraged to first seek the support and the advice of those units.

**CHAIRMAN**—You might think about that. How do you ensure consistency if you have one group dealing in major contracts that does not go to the central unit and does not adequately have in place a systematic examination of risk analysis so that risk is taken into account when a contract specification is agreed on, and when the negotiations take place with the private sector or wherever the tenders or offers are going to come from, and then that knowledge is passed down to the contract manager who is going to manage the contract in order to make sure that those areas of risk identified in the specification stage are transferred to the contract manager, so he or she understands that there may be some areas of risk that have already been identified way back in the beginning when you wrote the specification and that that gets transferred into continuous monitoring of that particular area of the contract so you make sure that risk is mitigated?

**Mr Tomkins**—We certainly have given thought to that. I wonder if I may, in response, talk about two issues: firstly, our standard contract for services—and we do have copies here for the committee, if you are interested—and, secondly, our framework for risk management. Our framework is in fact outlined in our Chief Executive Instructions, which do have the force of law, and also in our procedural rules. The department has also spent quite a considerable amount of time developing two booklets and, if I may, I will submit these booklets for evidence. We do not have sufficient copies here; we are reprinting them. The first one is about risk management in the department and the other one, which gets to the very essence of your question, Mr Chairman, is *Planning for risk management.*

**CHAIRMAN**—We would like those and that example of the standard contract, too, thank you.

**Mr Tomkins**—May I talk for a moment about the standard contract?

**CHAIRMAN**—Yes.

**Mr Tomkins**—It goes without saying that the department does have a standard contract for services and also a standard contract for consultancies. The department also has a standard short-form contract for small and non-complex arrangements. It is important that I outline the intention behind the contract: firstly, to assist in complying with the Financial Management Act and also with the accountability framework, which I think gets to the issue that you have raised with us;

secondly, to protect the interests of the Commonwealth; and, thirdly, to provide staff with guidance and to ensure common and important issues are addressed.

We do have sufficient copies to hand over to you, and the key clauses in the contract cover issues such as task and required outcomes, key personnel and responsibilities, the protection of Commonwealth information, intellectual property rights, dispute resolution mechanisms and accountability. I should also say that the department has a range of terms and conditions to cover funding arrangements.

**Senator HOGG**—In your standard contract, do you have anything about confidentiality or commercial-in-confidence? Do you have a standard provision there?

**Mr Tomkins**—Yes, we do.

**Senator HOGG**—What would have been the origin of that particular provision? Was it something drafted internally within your department or was it something that you picked up from another department or somewhere else?

**Mr Tomkins**—If I could refer you to the clause, it is clause 15 in our standard form contract. The person who would be best placed to answer that is Julie Fox.

**Ms Fox**—The contract was drafted within the department but with advice from the Australian Government Solicitor. It is similar to, although there are differences from, the more standard Australian Government Solicitor style of contract that you would see. There are two places where we would address commercial-in-confidence as an issue but, principally, the clause which is there at the moment—it is clause 10 on disclosure of information—is not drafted on the assumption of contractor commercial-in-confidence but from the perspective of Commonwealth commercial-in-confidence. There is no starting assumption of contractor commercial-in-confidence.

**Senator HOGG**—What about contractor commercial-in-confidence where that may apply?

**Ms Fox**—The standard form is drafted not to make that assumption, so that would be a negotiated process.

**Senator HOGG**—So it would be fair to say that your contract works from the assumption that everything you are contracting out is subject to scrutiny. It may well be that there is something, such as a piece of intellectual property that the contractor owns, that they do not want made known and then that becomes the subject of further discussions when the contract is being negotiated. Is that a fair assumption?

**Ms Fox**—Yes, although I would make it a little stronger. The subject of scrutiny is strongly supported by clause 15, which sets out the accountability regime with which the department would expect to deal with contractors. There we have made clear that the arrangements, subject to scrutiny, are not only for audit or internal audit purposes, but for external audit and even for parliamentary committee purposes and the like. It is premised on accountability.

**CHAIRMAN**—If you have read our report on Commonwealth procurement policy and practice, then you would know that we approve of your central agency, which is something we did not find much of, I must admit, two years ago. It seems to have proliferated throughout agencies. Maybe our report had something to do with it, maybe not, but it is pleasing to see. The committee has noted other examples in other departments and agencies where at least they have some minimum trigger that requires the individual officials, groups or agencies to go back to that unit under some minimum circumstances, which tends to assure some consistency of action across the unit.

On this business of risk, I have asked others and I will ask you: we understand that risk management means you are going to take risks, and we understand that the old culture of the Commonwealth Public Service was one of risk aversion and doing everything possible and having the number of people required to try to make sure that nobody ever made a mistake. That is not the real world and there is a different culture now. We have moved on to more modern management thinking. We understand that you cannot manage risk if there is no risk—that is, if you are going to transfer all the risk to someone else. So, if you are taking risks from time to time, there will be a failure. To what extent do this committee, with its interrogations, and other committees like Senate estimates tend to make you more risk averse?

**Mr Tomkins**—I guess I can respond best to that by talking about our approach generally to the allocation of risk in contract management. In that context, when allocating risk within the contract framework, the department's starting point is that risk should be borne by the party most able to control it. It is normal practice that the price tendered by contractors reflects their assessment of that risk. However, the final allocation is a negotiated position, based on the agreement between the parties.

**CHAIRMAN**—In standard contracts or in general do you ever ask for unlimited liability?

**Ms Fox**—Yes.

**CHAIR**—You do?

**Ms Fox**—We ask for unlimited liability. That would be the starting point in the contract, to the extent that a contractor is being paid to perform a service or deliver a good.

**CHAIRMAN**—How can a contractor insure if it is unlimited liability?

**Ms Fox**—Liability is never unlimited. There is a process to identify responsibility for liability and, to the extent that actions have caused damage, it was foreseeable that that damage would be the result of those actions, that you are responsible for it, that will set a limit on your liability. So we tend to avoid language such as 'unlimited liability', because you identify the scope of liability based on your risk assessment.

**Mr Tomkins**—I want to add to Ms Fox's comments by saying that there is flexibility around this. I do understand the context of your question, Mr Chairman. I wonder if I can share with the committee a recent example that, if the department feels that such a position is unreasonable then, yes, we are prepared to negotiate a different position. We have a current example in the

department that relates to the development of a particular IT system. The department's original position was challenged by the successful tenderer. We engaged in discussions with that tenderer to identify and explore the nature of the risks. The outcome of that was that the contract was subsequently adjusted. So I want to suggest that there is an element of flexibility in how we approach that issue of allocation of risk.

**CHAIRMAN**—If you put out a specification for tender for consultancy services of the order of $50,000, let us say, and you require the successful contractor to accept an unlimited personal liability clause which could run to heaven only knows how many hundreds of millions of dollars, how can you expect to get a competitive price on a $50,000 contract? Is that what you do?

**Ms Fox**—We do not actually have a clause that positively requires unlimited liability. The way risk is dealt with would be to assume that the consultant is being paid to do a professional job. To the extent that they fall below that performance level and the Commonwealth is exposed to liability, to the extent that they could be said to be responsible for that, they are asked to indemnify the Commonwealth. If, for example, the $50,000 consultancy was in a high risk developmental area and if it was not reasonable to expect that, firstly, they might be able to insure for that exposure, then that would be a basis on which we could negotiate a sharing of risk and a moderation of price.

**CHAIRMAN**—I think I may not have expressed myself well. Let us take a hypothetical. In a consultancy the consultant obviously has to have a public liability insurance policy. One of the consultants happens to be in your offices and leaves a filing cabinet bottom drawer open. A Commonwealth employee comes by and falls over the filing cabinet drawer and winds up in the morgue.

**Ms Fox**—In those circumstances, it is quite likely the Commonwealth would find itself in circumstances of strict liability, either as an employer within the workplace or—

**CHAIRMAN**—There would be little question that the consultant would be liable for their actions in negligence. Do you require them to have unlimited public liability insurance or do you place a limit on it at $10 million or whatever?

**Ms Fox**—We usually ask for a minimum level. How you identify that level would be on the basis of a risk assessment.

**CHAIRMAN**—You stated that new versions of standard contracts now include a specific clause enabling access to Commonwealth documents for the Auditor-General. Is that in line with the standard advice out of DOFA?

**Ms Fox**—Yes, that is clause 15. The Auditor-General, or any of their staff, could be authorised in writing by the project officer. There is no limitation on who could be authorised to gain access under the contract.

**CHAIRMAN**—Have you had any flack from any tenderers or proposed contractors over such a clause?

**Mr Tomkins**—No, to the best of my knowledge. In this context I would support the views expressed yesterday by Warren Cochrane of the Audit Office in this area. There has been a concern about how the department does express this issue, but the department's position remains that of enabling the project officer to have access or authorise another person, such as a person from the Auditor-General's office, to gain access.

**CHAIRMAN**—So the Audit Office does not automatically have right of access to documents and premises under the terms of your contract?

**Mr Tomkins**—That is correct. Clause 15 in that contract gives the departmental project officer and any person authorised by that officer access to the relevant premises. It is not automatic but there is provision for it to be enabled.

**CHAIRMAN**—We might point out to you that, if you had a project officer who was acting fraudulently and you were not aware of it, he might under some circumstances wish the auditor not to have access in order to find out what the heck was going on.

**Mr COX**—At least it might slow him down.

**CHAIRMAN**—It might.

**Mr Tomkins**—I would hope that the department never faces those sorts of circumstances. I think that is a good point. The department is prepared to take that on notice and re-examine whether there might be a clause.

**CHAIRMAN**—For what it is worth, we support it. In fact, we have recommended in our report on the Collins class subs that there be a legislative provision for the auditor to have automatic right of access to any contract of records and contract of premises if he requires them. We do not expect that to happen more than once in a blue moon. At least it is our collective view that having such a right would improve public perception of Commonwealth government accountability.

**Mr COX**—The only thing I would add to that is that you could fairly readily change clause 15 to say that 'The Contractor agrees to give to the Auditor-General and the project officer ...' and then just continue on with the rest of the clause. One of the things we are very interested in are contracts for the administration of human services because they raise particular issues. Is the Aged Care Standards and Accreditation Agency Ltd a Commonweath body?

**Ms Gunn**—It is a Commonwealth body, but in terms of its actual status, I could chase that up for you straightaway.

**Mr COX**—But it is owned by the Commonwealth?

**Ms Gunn**—As far as I am aware, yes.

**Mr COX**—It is a limited liability company, according to the submission.

**Ms Gunn**—Yes. Sorry, I thought you were questioning what we had written.

**Mr COX**—Can you tell us a little bit about how it operates and what it does?

**Mr Tomkins**—We are not the people best placed to be able to answer those questions. The reason there is some reluctance on our side is because we are aware that we do want to give factual and accurate information to the committee. I wonder if I may take those questions on notice and get back to you?

**Mr COX**—It is not that important now that we have established that it is in fact Commonwealth owned.

**Ms GILLARD**—Sorry, I have not been here for all of your presentation, but just looking through the standard contract I note that really all of the information confidentiality clauses run the Commonwealth's way, if I can use that expression, in terms of the vesting of intellectual property and the ability of the Commonwealth to end up as the ultimate owner of certain records and material. One of the issues we have been pursuing during the course of this inquiry is the question of commercial-in-confidence. The issue has really been to what extent the Commonwealth and/or the persons with which it contracts seek to keep information outside the public domain by describing it as commercial-in-confidence. Has it been your experience in dealing with the contracts you administer that there is a demand from contractors to have certain bodies of information defined as commercial-in-confidence?

**Mr Tomkins**—Perhaps if I can respond to that question and ask Ms Fox to add to it. Over the course of the last 12 months the department has in fact revised its standard contract. It has been drafted in a way that does not assume commercial-in-confidence status. Of particular note, and I draw us back to clause 15 of the standard contract, under which the department can request a contractor's attendance at Senate legislation committees. The contractor cannot address the committee by virtue of not being an officer of the Commonwealth. However, they can provide advice to officers appearing before the committee. For all other parliamentary committees, the contractor could address the committee and answer questions put to them. I am trying to answer your question in a very broad context and now we can go to more specifics.

**Ms GILLARD**—Just before you do move, have you had contractor resistance to the imposition of those requirements, those sorts of public accountability requirements? Have you had people say they are not prepared to do that or change their minds about whether or not to tender for the work?

**Mr Tomkins**—I am not aware of any particular sources of resistance. I would have to say that the contractors are becoming increasingly aware of the need to work closely with the department and through that to address the issues of accountability to the parliament. I guess what I am saying is that I have personally observed a growing level of awareness of the need for accountability back to the parliament. I would not say that there is absolutely no concern whatsoever, but I do sense a growing acknowledgment of the need for full and open accountability.

**Senator HOGG**—One of the other issues we have been pursuing is the issue of corporate memory. I note in your submission–and I must say you get the prize of the week for jargon in terms of this particular sentence:

The Department is adopting learning organisation principles which encourage the sharing of experiences to inform improvements in management practices.

As I say, it is highly jargonised. Then you go on to say:

The Department has recently established a knowledge centre within its highly regarded library.

Could you put that into plain English for us as to what you are doing in terms of corporate memory? One of the concerns we have with the outsourcing of work is that corporate memory is being lost within the departments and, whilst it might not be of significance at this stage, as the outsourcing continues there will be a further loss in the corporate memory and therefore the outsourcer may well end up dictating the terms rather than the department. That is taking a longer term view of it. You might say, 'Well, that is not happening currently,' and we accept that. One of our concerns is the protection of corporate memory and the training programs that you have in place to ensure that officers of the department who are dealing with the contracts have the corporate memory, in effect, to be able to deal with the contractors in the outsourcing areas on a level playing field.

**Mr Tomkins**—May I respond and then pass over to my colleague, Ms Gunn. As a department, we are acutely aware of the loss of corporate memory. What we try and do is build the organisation's capability so that we can negotiate and manage contracts in the best possible way. We do that through various mechanisms. For example, in our corporate governance structures we ensure that if we do not have the relevant expertise in-house we buy it in. There are numerous recent examples that I have been involved with where we have acknowledged that we do not have the appropriate skills and therefore we contract those in. Secondly, the department does have a very comprehensive training program. Thirdly, the department has, I think, gone to great lengths to ensure that we have central bodies of expertise. It is in that area where I would like my colleague to elaborate.

**Senator HOGG**—Just before we proceed, what efforts are you taking to review the skills that you have at your disposal to ensure that the skills are there? What review processes do you have?

**Mr Tomkins**—We do have a process of accreditation. Perhaps it is not as well developed as we might otherwise want it to be. I also want to acknowledge—

**Senator HOGG**—Could I just interrupt there? Is this going to be an expanding area for you in the future then, if it is not as well developed?

**Mr Tomkins**—It has been over the course of the last two to three years and it will continue to be as we continue to market test a range of our activities. The short answer is yes.

**Ms Gunn**—I have just a couple of points to follow on from Neville. Importantly, In our individual performance development schemes, we are looking at the development that, as a core competency, staff must be trained in and must be competent and good at that issue around

contract management and project management. We believe that, over time—it is not going to happen overnight—that will see an improved management of the processes in the department.

To pick up a couple of other questions, very quickly: our IT outsourcing is a good example of the movement of memory from those that developed to those that then manage. The people who were involved with the negotiation, the nitty-gritty, exactly what was required, are now responsible for the management of that. Importantly then what the department is doing is a number of system responses to ensure that the information does not just stay in their head but that it exists in electronic document management systems as well, so that we have a system that, across the department, is a continual repository of that information over time.

**Mr Tomkins**—To finalise our response to that: the department has recently embarked on quite a comprehensive program of organisational alignment. Within that context we are looking very closely at a management model for the organisation, and within that we are clarifying much more points of accountability, and roles and responsibility. That links to what Ms Gunn spoke about, which is our performance development scheme and, core to that, some skills and some competencies. There are two in particular which I would like to finish on—project management and also contract management. The executive and senior management in our department have acknowledged the need for us to continue to develop our capability as an organisation in that area.

**Senator HOGG**—Thank you. Just one final question on the issue of commercial-in-confidence or confidentiality: do you have any idea how often in, say, the past 12 months or two years, at either Senate estimates or other inquiries conducted by committees of the parliament—whether they be joint committees or other House of Representatives committees—commercial-in-confidence has been an issue?

**Mr Tomkins**—To the best of my knowledge, I am not aware of any particular circumstance.

**CHAIRMAN**—Can we go back to the issue that the senator was pursuing. You did mention your new IT outsourcing contracts. We are talking about corporate memory and skills. When you are developing your specification—that is, deciding what information you want produced by the computer programs and what processes they are to follow—is that developed by management?

**Mr Tomkins**—I am sorry, I do not understand the question.

**CHAIRMAN**—Your information technology program is about a number of things, I would think. Part of it is delivering services and part of it is keeping track of what is happening within the department for reporting purposes. Is that correct?

**Mr Tomkins**—Yes.

**CHAIRMAN**—So you have management reports that tell you periodically your performance against certain standards, which I hope is going to wind up in your annual report. Is that right?

**Ms Gunn**—Yes, in terms of the IT security reports that are being produced. There are a number of reports that are produced in relation to the performance of the IT system. Is that what you mean?

**CHAIRMAN**—Performance of what?

**Ms Gunn**—I am sorry, I am still not quite sure if I understand the question.

**CHAIRMAN**—Dollars per person treated and so on. You might, for instance, track the effectiveness of the 30 per cent Commonwealth rebate on private health insurance uptake. Would that be a management tool? I would have thought it was. I would have thought your minister would really want to know that.

**Mr Tomkins**—Absolutely.

**CHAIRMAN**—If I were managing the department I would certainly want to know whether or not we were getting value for money out of the 30 per cent rebate.

**Mr Tomkins**—Absolutely. I agree with you, Mr Chairman. The issue which I am a little bit confused about is the context of IT outsourcing. That type of analysis—and also policy advice—remains a core function within the department. What has been outsourced in the IT context is in fact our infrastructure and not that type of analysis.

**CHAIRMAN**—Okay. Then the question was inappropriate.

**Mr COX**—I do not think they are doing that kind of analysis. I do not think they can afford to.

**CHAIRMAN**—That is a political statement, Mr Cox, and not one based on sound engineering advice.

**Ms GILLARD**—Why collect information that is not going to affect policy, anyway?

**CHAIRMAN**—With the greatest respect, Ms Gillard, I would have thought that it would.

**Ms GILLARD**—I think we have convincingly proved it does not.

**CHAIRMAN**—You said the department's audit committee directs an internal audit program. That is good; we like that. Before that, you talked about an audit and fraud control branch. Who drives examination of contract management performance and risk management and risk performance? Is that the internal audit committee or the audit and fraud control branch?

**Mr Tomkins**—There are two sources. The first is that, as part of good contract management, issues around the performance must be continually monitored by the line divisions—in other words, the actual staff involved in the management of that project. Secondly, there are occasions when the executive of the department does authorise the examination of particular contracts, and it is a member of the executive that chairs the audit committee.

**CHAIRMAN**—Do you build any buildings?

**Mr Tomkins**—The organisation itself does not build buildings. But, from time to time and in particular program areas, the department may contract for the construction of buildings.

**CHAIRMAN**—Oh, very good. Ha, we found one!

**Senator HOGG**—It's taken us a long time.

**CHAIRMAN**—We have found somebody who is still building buildings.

**Mr Tomkins**—I would not want to disappoint you, Mr Chairman, but we actually fund the construction of the buildings. We do not contract directly.

**CHAIRMAN**—That is all right. That is what we are looking for. I understand you do not have any personnel that go out and swing a hammer or lay bricks.

**Mr Tomkins**—That is correct.

**CHAIRMAN**—What branch of the department does have construction or building activities? In other words, you build and own the buildings?

**Mr Tomkins**—From memory, it would be the Office for Aboriginal and Torres Strait Islander Health.

**CHAIRMAN**—Do you simply fund the construction activities?

**Ms Fox**—We do not place the contract for the construction to be undertaken. We fund an organisation who then places a construction contract.

**CHAIRMAN**—So you do not write the specifications?

**Ms Fox**—No.

**CHAIRMAN**—Okay. Then you cannot answer my questions. Thank you very much for your submission and for the additional information that you have provided us. Is it the wish of the committee that the documents entitled *Planning for risk management*, *Risk management in the Commonwealth Department of Health and Family Services* and *Standard contract for services* presented by the Department of Health and Aged Care be taken as evidence and included in the committee's record as exhibits 29, 30 and 31? There being no objection, it is so ordered.

**Proceedings suspended from 10.19 a.m. to 10.30 a.m.**

**DANIELS, Ms Yole, Acting Assistant Secretary, Corporate Strategy and Support Branch, Department of Immigration and Multicultural Affairs**

**FREEMAN, Mr Philip, Director, Purchasing Reform and Accounting Services, Department of Immigration and Multicultural Affairs**

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

**McMAHON, Mr Vincent, First Assistant Secretary, Corporate Governance Division, Department of Immigration and Multicultural Affairs**

**METCALFE, Mr Andrew, Acting Secretary, Department of Immigration and Multicultural Affairs**

**PAGE, Mr David Julian, Acting First Assistant Secretary, Multicultural Affairs and Citizenship Division, Department of Immigration and Multicultural Affairs**

**CHAIRMAN**—I welcome representatives of the Department of Immigration and Multicultural Affairs to today's hearing. Thank you very much for coming and thank you for your submission. Do you wish to make a brief opening statement?

**Mr Metcalfe**—Mr Chairman and committee members, thank you very much for the opportunity to address you this morning. The Department of Immigration and Multicultural Affairs has delivered a significant range of services under third party arrangements for a number of decades. These include major and sensitive services such as the adult migrant education program and immigration detention, to name just two. In fact, over 40 per cent of the department's budget, covering a wide range of activities, is now outsourced. The significant change in the 1990s has been the change in the character of many of the contractual arrangements; that is, some of the traditional service providers are being replaced by others in open market competition, such as Australasian Correctional Services replacing the Australian Protective Services in providing immigration detention, or service providers themselves have reconfigured to deliver services under business models, such as state adult migrant English program providers.

In delivering services for the Commonwealth, the department deals with two distinct groups of service providers. There is the normal commercial market, where our requirements are likely to be highly specified, where there is a clear understanding of the services required and where services provided are measurable through specific performance measures. There are also community service providers, typically involving a significant voluntary element. They tend to lack both organisational and commercial sophistication. These service providers work under contract management arrangements to deliver broadly defined services. This means that while the needs are recognised by the government, the actual delivery and the form of delivery are, to a large extent, determined by the service providers themselves.

The department's further submission, as requested by the committee, merges commentary on these two quite different types of contract management. The committee has had some exposure to the latter group through its previous examination of ANAO report No. 29, *Provision of Migrant Settlement Service by DIMA*, on which the committee, I understand, has commented in its just published report No. 373.

The move to a broader range of contractual arrangements is posing significant challenges for the department. Contract management requires the development of an appropriate set of skills in our staff. This is identified and highlighted in the departmental work force analysis report of last year, which is entitled *Staff at their best*. We have put in place initiatives to increase contract management skills. There is a focus by the department's central purchasing reform unit on the training and advisory services for areas managing contracts. There is no doubt that in the early stages of outsourcing arrangements the department lacked expertise in managing some contracts. However, I equally believe that we have learnt well from our experiences in dealing with the private sector and we are now much better equipped to manage an outsourced environment.

It is pleasing to note that the ANAO concluded in February that, after looking at management systems and practices in forms, printing, distribution and translation services, there were no material contract weaknesses. Given similar results in two other agencies, the ANAO concluded that their initial findings did not warrant a full performance audit as a follow-up at that time. Both my colleagues and I will be very happy to answer questions from the committee.

**CHAIRMAN**—I noted in your submission—and you mentioned it just now as well—that 43 per cent of the current year's department budget is managed under contract arrangements. With such a high degree of outsourcing, how do you assure accountability of both the service provider and the contract agency, if it happened to be for supply of goods, to you and then your accountability to parliament? How do you manage that process now?

**Mr Metcalfe**—I will make some general comments, and Mr McMahon or others may wish to follow-up. It is obviously a matter for the development of each contract to ensure that there is appropriate accountability to the department. We have provided to you details of our standard contract, which is the basis for much of our contractual work. We have much more highly specific contracts in some areas. For example, there is the one I am personally most familiar with in relation to detention services. The accountability comes through a range of measures, but we aim to work very carefully and closely with our contract partners. For example, in the detention services area, this means that there are requirements for regular meetings to monitor performance under the contract. Indeed, a system of rewards and sanctions is applied on a quarterly basis to the service provider, following a review of their performance. There are doubtless numerous examples in other areas of contract management.

In terms of accountability to the parliament, the department of course is subject, very properly, to the full range of accountability measures, both through the Audit Office, which in turn reports to the parliament, and through the regular Senate estimates processes. We are highly accountable to our own minister and to the government, as well as the parliament. In addition, some of our areas are subject to further accountability and performance measures. We are clearly involved within government in annual budget cycles and have developed clear measures of performance and outputs and outcomes under new budget arrangements. Similarly, beyond direct financial

accountability there is performance accountability through a range of bodies—I will again use the example of the detention services contract—such as the Ombudsman, the Human Rights and Equal Opportunity Commission and the Joint Standing Committee on Migration—all of which maintain a very significant interest in that issue and regularly undertake inquiries into it. That is a small illustration of some of the accountability measures that we demand of contract partners and that are demanded of us, very properly, by the parliament and other bodies. Mr McMahon or Mr Page may want to add a little bit of detail to that, if that would help.

**Mr McMahon**—Just very briefly, we have put some time into making sure that there are reasonably sophisticated reporting mechanisms within a lot of our contracts. The reporting mechanisms have often increased the amount of information that we have had available to us for basic management purposes relative to where we were before. A trivial example is stationery and associated stores worth many millions in our organisation. When we put the contract out, a key part was actually coming to a firm understanding of what we were using throughout the department. I think Mr Metcalfe referred to performance measures. In a number of cases before when we have gone out to contract, there have been no performance standards in place within the organisation. But, by going out to the outsourcing arrangements, we have been forced to actually specify in considerable detail the levels of performance.

I would also note that we have tried, and are interested in pursuing more, actually attaching the draft contract to the tender. This provides quite distinct advantages in respect of the post-tender negotiation process, but it also provides a fairly high level of transparency in what we are doing. I think we have mentioned in the submission that, as a standard clause, we require contractors to provide access to documents to the ANAO. We also ensure that the ANAO has access to premises.

**CHAIRMAN**—We thank you for that.

**Mr Page**—Mr Chairman, perhaps I could take the opportunity to give an example of what Mr Metcalfe meant by distinguishing between contracts that are under the market competitive tender arrangement and the sorts of contracts we have with funded agencies at the community level. The distinction you have made between management information required to satisfy ourselves that those agencies are fulfilling the contract and producing the service creates a different type of performance requirement from what the parliament might require. In fact we frequently have difficulty in persuading community organisations to give us data which we need solely for the purpose of meeting requests from parliament.

Those requests come in a range of forms—through individual MPs or through Senate estimates committees wanting particular details about an agency that they are aware of—but mostly it is because parliament wants aggregated data across the whole range of a community program. We have 308 separate service agreements and each of those has performance measures relating to the service to be delivered, but it does not follow that the 308 different agencies see themselves as part of a group on which we have to report to parliament.

**CHAIRMAN**—Let us try an example of what I am asking about in terms of accountability to parliament. This committee considers the annual report to be an ideal vehicle to tell us your performance in the various segments of your operation against targets that you set and/or

performance against some financial criteria—in other words, how much it costs to deliver a service per person or per transaction or per whatever. If we go back to an area which you may not like me to revisit, that of migrant settlement, the auditor found some deficiencies in consistency between the various states in overstays. We would consider that that might be a reasonable performance measure in terms of expenditure on migrant resettlement expenditure. Would it be your intention to report in the annual report on overstays and by location?

**Mr Page**—Perhaps I could respond to that question and give some further information at the same time. I think when the committee was looking at that issue in August, that preceded the situation we are now in in having released a request for proposal, a form of tendering, in November. The issue of how long people are allowed to stay in on-arrival accommodation will shift as a result of the successful outcome of that tender process from 1 July. I think the committee was specifically concerned that we appeared to be allowing people to stay for 26 weeks in Sydney and for 13 weeks in Melbourne.

**CHAIRMAN**—It is true.

**Mr Page**—Under the new proposal the issue shifts. I cannot say it goes away entirely, but the issue shifts for the department because the contractor, whoever it turns out to be, will be required to take over the cost of accommodation for people who have to stay for longer than four weeks. It does not follow that the people will be evicted from the accommodation but it is an incentive for the contractor to find suitable alternative and more permanent accommodation for the residents.

**CHAIRMAN**—Are you shifting risk?

**Mr Page**—That is a form of shifting risk.

**CHAIRMAN**—I was pleased to read in your submission that you now have a central purchasing unit providing an advisory role to various agencies across your operation, which I believe did not exist last time we talked to you about purchasing policy and practice. In using the services of that central unit, is there some dollar level of contract that triggers their involvement or are they only there in an advisory role?

**Mr McMahon**—They are available for advice on any level of contract. It may well be that for some minor contracts, particularly if they are repeat contracts where the area itself has confidence in dealing with the contracts, they may not be consulted. In general, we encourage and enforce widespread consultation with them for the overwhelming majority of contractual issues.

**CHAIRMAN**—‘Enforce’?

**Mr McMahon**—Yes. For example, if I, the secretary, the deputy secretary or the executive heard that a contract was being pursued, one of the first questions that we would ask would be whether or not it had a sign-off, not in a formal sense but in respect of consultation and agreement, with the central purchasing reform area. If the answer were no, then almost certainly

there would be considerable discomfort in respect of signing a contract that had not gone through that process.

**CHAIRMAN**—How large is that organisation?

**Mr McMahon**—In respect of the people actually providing advice, I think there are five people.

**CHAIRMAN**—And levels of accreditation?

**Mr McMahon**—They are not formally accredited as such, to my knowledge. They have undergone various levels of training. They have considerable experience in respect of contract dealing. Many of them have had longstanding financial and purchasing responsibilities.

**CHAIRMAN**—Going back to performance—and this goes to risk management as well—when you go to write the specification for a contract, whether it is for building maintenance services or IT, or whether it is outsourcing service provision, and you identify, in terms of risk management, the areas which could have some risk attached to them, some would have higher levels of risk than others. Having done that, the specification and the contract documents are then transferred to a contract and that contract is given to someone to manage the contract itself. How do you ensure transfer of that initial risk assessment to the final contract or project manager?

**Mr McMahon**—I do not really believe that we operate in two distinct stages in respect of the way we do it. For example, in drawing up the specifications it would probably be done in a line area, but that line area would be consulting with the centralised purchasing reform group to ensure that it is getting adequate advice in respect of the drawing up of those specifications. It also would be accessing a centrally held body of legal advices to ensure that there is finetuning. It is also picking up the accumulated corporate understanding of contractual and other issues in respect of the standard contract which, as I said in our submission, is a store of corporate knowledge. When the contract goes to tender, we almost always have a member from the Corporate Governance Division, and normally from that particular area, who is involved in the tender process as well to give us assurance throughout that process. So there is a significant overlap in the processes which results in no formal handover.

The other issue is that it is really the specification of the performance criteria and the expectations under the contract that actually define the risk in many cases. What initially may be a conceptual exercise about the risk actually gets translated into quite detailed contract performance issues that are then measured. One of the key issues I mentioned earlier is that we do insist upon monitoring arrangements taking place under the contracts. In other words, we look for systems to be put in place fairly rapidly by the contractor in many cases.

**CHAIRMAN**—Following on from what you have just said, in your submission you said that you adhere to the Financial Management Accountability Act, the relevant chief executive instructions and the Commonwealth procurement guidelines. I am pleased to see that. It is the first time I have seen that in a submission as I recall. In evaluating performance as the contract proceeds, one of the concerns that we had in the purchasing inquiry, which was dictated by a response from private industry, was that there were times when the Commonwealth procurement

guidelines talked about not only value for money but maximising ANZ content of the outcomes of procurement. Sometimes departments did not check that what had been tendered was supplied in terms of ANZ content, for instance. In your new procedures would that get picked up as a performance indicator and be tested by the project manager?

**Mr McMahon**—The answer is that we believe our broad contractual arrangements do comply with that requirement and some of the major contracts that we are party to and not necessarily running ourselves, like our cluster 3 IT. I do recall that it was specifically built into it. We would like to think that we do evaluate and monitor all aspects of a contract. I have to say though, quite frankly, that I do not recall that particular aspect ever having been an issue.

**CHAIRMAN**—You cannot recall a tender saying, '65 per cent of what we deliver will be ANZ content'?

**Mr McMahon**—I do not recall that we have ever pulled up a contractor in respect of a failure to provide adequate local content.

**CHAIRMAN**—Okay, but the question was: do you actually check at the end of the delivery to make sure that you got what they promised in the first place?

**Mr McMahon**—I believe we do. I would have to take that on notice. We basically go through all our performance measures. To the extent that it is reflected in a contract, it would be a matter of course for us to do so.

**CHAIRMAN**—Okay.

**Ms GILLARD**—Following up issues that Mr Page was addressing before, when you are dealing with your contract arrangements, how do you deal with the question of commercially sensitive or commercial-in-confidence information? Do you have a standard clause that deals with those questions?

**Mr Page**—For the grant type contracts that I was referring to we do not have a commercial-in-confidence concept in that set of arrangements because, unlike the market driven competitive tendering version of contract, they are in effect partnerships to produce services that are absolutely essential to the government's settlement service arrangements and policies.

Therefore, the distinction that I would draw between one form of contract and another is that in the competitive tendering concept the purchaser specifies what is to be done and has a fair idea, as Mr Metcalfe's opening remarks indicated, of what should be done, and the supplier gives best value for money. In the arrangements that I am referring to, it is the other way around. The agencies relating to particular community interests that involve the settlement of migrants identify needs with which the government agrees. They are needs to be addressed and we are interested in contributing to the service that an agency is proposing. Consequently, the legally enforceable service agreement that we draw up with that agency assumes an agreement on the continued service to a set of end users. Therefore, that is our overarching purpose and it informs the way in which we manage and administer those contracts. In terms of whether the content of the contracts has been available, I think we have freely given to various parliamentary

committees the standard contract. I do not recall a case in which we have then been asked to provide the accompanying work program, but we have certainly given, very freely, information about a particular service. The arrangements that are embedded in the service agreement ensure that we can get any information we require for any purpose.

**Ms GILLARD**—And the information that is available includes the quantum of the grant moneys that is being provided under those agreements?

**Mr Page**—Indeed, yes.

**Ms GILLARD**—To look more broadly at contracts not of that nature, if I can define it that way: how do you deal with contractors in a more commercial setting who raise the question of protecting commercially sensitive information?

**Mr McMahon**—Are you asking in respect of access to information by the parliament?

**Ms GILLARD**—Yes. One of the things we have been discussing with departments—it varies, depending on the setting—is an issue about information being taken out of the public domain because it is described as commercial-in-confidence. There are some categories of information that we would all agree need to be taken out of the public domain. If you are contracting with someone who has genuinely got a trade secret or some form of unique intellectual property, then it is fair that they get to protect that. But the concern of the committee has been that the description of what is commercial-in-confidence flows much more widely than that and on occasions it could be used as a tool just to defeat legitimate public inquiries, rather than there being any truly valid commercial reason for the protection of that information.

**Mr McMahon**—We are well acquainted with that issue, because it has come up a number of times in respect of Senate estimates examination. I do not know whether all the parties on the other side would agree, but I think we have walked our way through it quite well over time. One formula which I think has broadly satisfied the interests of parliamentary scrutiny is the release to the parliamentary committees of the majority of the contract, but just removing those sections of the contract which will go to the heart of the commercial sensitivity. In other words, the response in respect of commercial sensitivity has not been a blanket, 'No, you can't see the contract.' We have had a number of concerns over time, in particular about either compromising the firm or the Commonwealth's own best value for money position: sometimes it would be damaging if it got into the public domain what we were paying for, because in the next tender arrangements we would want to see the price come well below, not just be matched at, that level. Having said that, I think I mentioned earlier that we do like to try to publish some deeds and some draft contracts, obviously at that time without the relevant commercial information—putting the actual contract into the tender, because it provides considerable protection for the Commonwealth and the potential contractor.

**Mr Page**—Mr Chairman, may I qualify a statement I made just now? I said we could get information for any purpose. I meant financial accountability. I should have said that we do allow agencies to protect confidential private client data, so I have qualified my generalisation.

**CHAIRMAN**—You are required by statute to do that, yes.

**Ms GILLARD**—It is not an issue about that individual client data as such. Just in respect of your answer, I think there are varying views as to what, if any, market distortion you cause by releasing prices after a successful tender round. The general view seems to be taken by departments—Job Network, that sort of thing—that you do distort the market by releasing price information, but there is an equally compelling view that you get the best performance in markets when people have got the best sorts of information and that a tenderer who knows what the successful price is has got an incentive to bid under that price next time round. Or, if there is a premium being paid in certain regional areas, the fact that that is disclosed might encourage more firms to bid in those areas because the prices are higher. I do not know if you have got a response to that debate.

**Mr McMahon**—My response to that would be that it probably relates to individual circumstances of contracts. I think they are both legitimate views.

**CHAIRMAN**—Could I pose a hypothetical. Sometimes it is the best way to get there. If you had a contract to supply a building, I assume you would have no reluctance in disclosing the contract price for the building, because it is going to be different than any other building that is ever going to be built. Is that correct?

**Mr Metcalfe**—Speaking hypothetically, I think the answer is probably yes.

**CHAIRMAN**—I can tell you that the Department of Housing and Construction, as a matter of course, would publish the accepted tender prices.

**Mr Metcalfe**—I just wonder whether that would disaggregate builders' margins and other aspects which might in fact—

**CHAIRMAN**—Total tender price for the contract.

**Mr Metcalfe**—So it would not be disaggregated.

**CHAIRMAN**—But the department would have never known builders' margins, with respect.

**Mr Metcalfe**—Yes.

**CHAIRMAN**—I would think even the most publicly declared individual on this committee would not think it was reasonable to ask the contractor to disclose to the public how much money they thought they were going to make out of the contract.

**Mr Metcalfe**—We can probably move out of the hypothetical and move into a specific example, Mr Chairman. As the committee may be aware, we do not build buildings—

**CHAIRMAN**—I was going to ask you that.

**Mr Metcalfe**—but we certainly engage with our detention services contractor in their providing buildings which ultimately are owned by the Commonwealth. I am specifically talking about detention centres. We are doing that right at the moment in a construction project at

Woomera in South Australia. I think the levels of cost associated with provision of those detention centres has been well put on the public record, and indeed will be through various budget documents and whatever. They will be broad costs, not highly detailed costs. For example, we have been talking for some time about the cost of providing additional detention accommodation at Woomera and there have been some fairly specific figures used in that public discussion of the issue.

**CHAIRMAN**—But then, to continue the hypothetical, if we asked Mr Page to tell us the cost per resident of resettlement services in New South Wales, Victoria, South Australia, Queensland, Western Australia and Tasmania you might have some reluctance?

**Mr Page**—I do not know. The contract has not been let as yet, and therefore we do not know which providers or what set of arrangements will occur from 1 July. But in terms of your comments about the annual report, I would think that we should be able to give disaggregated data about different locations, and presumably the costs would vary according to differences of location and infrastructure rather than because of the tendering arrangements.

**CHAIRMAN**—Can I go back to building, Mr Metcalfe? I understand you do not want—

**Mr Metcalfe**—We have a contract with Australasian Correctional Management, who are half owned by Thiess.

**CHAIRMAN**—You have a contract with whom?

**Mr Metcalfe**—We have a contract with Australasian Correctional Management, which is the company that is contracted to us to supply detention services. That company is half owned by Thiess Constructions, so we have contractual arrangements with ACM and with Thiess for the provision of construction of detention facilities right at the moment at Woomera.

**CHAIRMAN**—And who writes the specifications and produces the drawings?

**Mr Metcalfe**—We develop specifications in terms of broad requirements for numbers of people to be detained.

**CHAIRMAN**—Is it a functional specification?

**Mr Metcalfe**—There is a functional specification for the quality of building and the purposes for which the detention centre will be put.

**CHAIRMAN**—But they are not detailed specifications of the number of layers of bricks and height of walls?

**Mr Metcalfe**—The very detailed specifications are developed by the company and subject to agreement by the department. In that iterative process with this particular project, for example, where we are having to do this quickly because of the fact that more and more people are arriving who need somewhere to stay, we routinely employ the services of a firm of quantity surveyors to assist us in ensuring that we are understanding what is being put to us and that we

are achieving value for money through that project and a quality of construction that is appropriate.

**CHAIRMAN**—In going back to risk and migrant services—I am sorry to keep pounding on that one, but it is fresh in the mind so it is easy to address; and it is not my intent to embarrass anybody—the question is generally this issue of risk and whether or not the Commonwealth Public Service is risk averse or is in fact accepting now that risk management means that you are taking some risk. There will be some areas of some contracts where there is more risk than in some areas of other contracts, and I think we understand that when you say that you are going to take a risk—which implies efficiencies—from time to time there will be a failure?

**Mr Metcalfe**—Yes.

**CHAIRMAN**—My question is: to what extent does this committee, through its inquiries, Senate estimates committees and other parliamentary committees tend to make you more risk averse?

**Mr Metcalfe**—I might answer in the broad, Mr Chairman, and I am sure my colleagues will have something to say. I think that we regard it as a fact of life that committees like this committee, Senate estimates committees and other accountability processes exist. That is just a reality. It is hard to speculate whether or not that makes us more risk averse. At the end of the day, our legislative obligations under the Financial Management Act are clear in that, in dealing with these issues, we need to search for value for money. I think we accept that in some areas of some contracts risk does exist. As Mr McMahon indicated earlier, the task in developing those contracts is understanding what we want, identifying where the risk is and seeking to appropriately deal with that risk.

If the question that you are driving at is whether the existence of accountability measures is making us more risk averse and therefore do we pay more as a result, I do not have a simple answer to that. We operate in the system that we operate in, both from a legislative and an accountability point of view. We accept that, increasingly, the department is becoming more comfortable with the need to manage risk. We have certainly lifted the level of skills associated with contract management. It is reassuring to hear your comments that, if you are in a risky environment, occasionally something is going to go wrong. At the end of the day you need to be comfortable that that is not the end of the world, that that is an accepted component of operating in a commercial area. It is a very interesting question. I do not know that I can give you an absolutely precise answer as to whether or not, somewhere deep in my consciousness or in other people's consciousness, we tend to be a bit more risk averse because we are going to be answering these questions.

**CHAIRMAN**—I cannot tell you that when something goes wrong, we will not ask you about it.

**Mr Metcalfe**—I absolutely accept that you will ask us about it and I hope we have got the right answers. Sometimes the answer might be, 'Look, we took our eye off the ball.' I hope that is not the case because we are trying very hard to deal with it. We accept that there is

accountability if something goes wrong, in the same way that we hope there is praise if something goes right.

**CHAIRMAN**—It would be nice from time to time when something does go wrong to hear someone come before this committee and say, ‘Look, we stuffed up, but we’ve now got in place procedures to make sure we don’t do that one again.’

**Mr Page**—Mr Chairman, may I give a version of that?

**CHAIRMAN**—Nobody ever says, ‘Look, we stuffed up.’

**Mr Metcalfe**—We are taking the opportunity. This is a somewhat cathartic hearing.

**Mr Page**—This is not admission of a stuff-up—

**CHAIRMAN**—No.

**Mr Page**—but admission of the stimulus that committees such as this do give to contract management. Therefore, you can look at the issue, as you put it, of departments being risk averse because of the existence of committees like this or you can look at it from the point of view of the inspiration that questions from you and others give us which improves the standard. That is why I wanted to intervene. Since we were here in August and the issue of a risk management strategy for the area covering community grants and the migrant resource centre network was raised, we have been stimulated by the committee to produce a revised version of a business plan that covers those areas and a parallel risk management strategy. Within that risk management strategy, we have begun to identify risks that previously we described as embedded in our guidelines. I am trying to describe a result which is part of a healthy interaction between officials and the parliament.

**CHAIRMAN**—We have been very pleased, particularly over the last three days, to note how many departments have gone to a centralised purchasing unit. Considering what we found when we did the purchasing inquiry, it has been delightful to see that that has occurred.

**Mr McMahon**—There is a question of being risk averse, but there is also the question of risk avoidance. What we have learned over a period of time is that we have got smarter, without doubt, in respect of our contract management. We have been able, with a growing sophistication in dealing with the market, to eliminate a lot of risk that was there in respect of some of our early dealings with the market. I think we can avoid risk and still undertake risk management because some of the risk management issues may go to the management of the contract.

**CHAIRMAN**—We thank you for your submission and for coming and talking to us today.

[11.17 a.m.]

**CONROY, Air Vice Marshal Raymond John, Head, Systems Acquisition, (Aerospace), Defence Acquisition Organisation, Department of Defence**

**FITZGERALD, Mr John Thomas, Director General, Contracting Policy and Operations Branch, Department of Defence**

**GAIREY, Mr Mark Christopher, Acting First Assisting Secretary, Capital Equipment Program Division, Department of Defence**

**KEARNS, Dr Graham, Head, Industry Procurement Infrastructure Division, Department of Defence**

**LAMACRAFT, Rear Admiral Richard, Head, Systems Acquisition (Maritime and Ground), Defence Acquisition Organisation, Department of Defence**

**NOBLE, Mr James McCallum, Acting Head, Systems Acquisition (Electronic Systems), Defence Acquistion Organisation, Department of Defence**

**ROCHE, Mr Michael John, Under Secretary, Defence Acquisition Organisation, Department of Defence**

**CHAIRMAN**—Welcome. Thank you for your submission and for coming to talk to us again today on this most important area. We understand from your report that you are currently reviewing your procurement and project management systems and activities which have been the subject of a good deal of detailed questioning by this committee over some considerable period of time. One of the systemic questions that we have tended to ask all the departments and agencies that have come before us so far in this inquiry is related to the issue associated with risk analysis, risk management and project management itself. I think it goes to the heart of the whole area surrounding contract management. You are currently undertaking an inquiry, which I understand you will report to the minister on soon. Is that right?

**Mr Roche**—Yes.

**CHAIRMAN**—I noticed in that inquiry that you are giving serious consideration to the processes by which you establish the project specifications in the first instance and sign off on them and, as part of that process, you identify specific areas of risk and hopefully rate them. Then, through whatever procedure, you transfer the specifications into a contract with a contractor and then the contract goes to a contract or project manager or team or whatever. I guess there are really two questions in one: first, do you now recognise that there are some areas in your major purchasing where, because of your preliminary risk analysis, you understand that you must write the contract specifications differently in one section of the contract than in others; and, second, do you transfer the corporate knowledge that was inherent in developing a specification, which then led to the contract, to the project management team so they are well aware of the risks inherent that were identified all the way back in the initial specification stage and so they keep track of the contractor's performance in those areas specifically of risk? That is

a long question! I am sorry about that, but I did not know how to make it shorter. We would like to know your thinking, even if you cannot tell us exactly what you are going to do, Mr Roche.

**Mr Roche**—We can share that. I am just thinking about where to start. The review that we are undertaking, what we call acquisition reform, is really a cradle to grave job. So it does cover the process from the very first blush of capability development right through to life support and eventual disposal. I think the minister has already announced that there is a review being undertaken of Support Command Australia, and we are looking to see whether that might be brought into a closer alignment with the Defence Acquisition Organisation.

We have identified the fact that there is room for improvement in the way that we define capability. We have discussed with the minister a number of specific proposals along those lines, but broadly we are looking to expose that process to industry much earlier. One of the problems that I think has been raised with us is that industry does not get involved early enough and is not able to give us good information on risk, the potential for innovation, cost drivers, schedule drivers and so on. So what we are trying to do is establish integrated project teams much earlier, with representation from the Defence Acquisition Organisation and with representation from the support area and logistics. All three areas—capability, purchasing and support—will come together in a team that will more or less stay together for the life of the project. That team would then be able to canvass, at a much earlier stage than we do now, projects with industry to get input on risk. I agree with you that risk is an area where we need to be doing more and we need to identify that risk up front. We believe that by using these integrated project teams and by involving industry and by doing more funded study earlier on, we can better identify risk. We will flow that into the purchasing process by virtue of the fact that the team will flow through into the purchasing process.

There will be some shift in membership, but I would imagine it would drag through some of the original capability people. The original acquisition people would flow through into the acquisition process and, of course, the logistics people would still be there. That is how we see the information being transferred into the purchasing part of the process.

We do agree with you that we need to tackle different areas of risk in different ways. One of the things we have done in the past is to look at a project as a whole in terms of risk and define something as a risky project or not, whereas the truth is that most projects have risky bits in them and some bits that are a much lower risk. We do agree that we need to tackle that quite differently in a contractual sense.

I was going to say at the outset that we are working on this reform now. The sand is shifting in relation to our submission. One of the things that we are doing at the moment that did not get much airplay in our submission is that we are involved in a full-scale review of DEFPUR 101. That is the general purchasing contract. One of the key areas we are looking at is the treatment of risk in that contract and specific parts of projects.

**CHAIRMAN**—If we could get the specific. It is pretty old hat now, but let us say that you were going to write the specification for a contract for Collins class submarines today. You knew I would get onto that.

**Mr Roche**—I wonder if I could be difficult and ask whether we could not use a more current example, something like AEW? There is a very good example there.

**CHAIRMAN**—We are not familiar with that. You can go to that in a minute but I want to ask my specific question. If we take as a given that it would be reasonable today to place a contract on a fixed price basis for construction of submarines—including batteries, diesel engines, periscopes, torp tubes and all the rest of it—development of blue sky software for a combat control system might be somewhat different from building the whole of a submarine and fitting it out with batteries and diesel engines et cetera. Would you think that in this review you might be more likely to split such a contract into two parts, one being for a fixed price for the supply of goods and some services and the other being a development contract?

**Mr Roche**—I do not think that the sole difference between the two of them would be fixed price versus development contract. I think we would deal with them quite differently in a contractual sense. Yes, there would be likely to be more pricing flexibility in relation to the delivery of software systems. A more significant issue in relation to the software systems is that, because it is developmental and evolutionary, you would be putting much more thought these days into how you might specify the overall architecture, bus design and interface specifications for a combat system, without getting too hung up on the level of processor or whatever was going to drive the thing. We would be looking to trying to define a lot more modularity at an early stage.

**CHAIRMAN**—Are you trying to say that what you might be trying to define better was what outcome you want from the system—in other words, what you wanted to be able to do rather than precisely how it does it?

**Mr Roche**—That also. I was taking an intermediate path. We are moving down the path of functional specifications and outputs based specifications. But at some stage you still need to include in the contract a more precise technical definition of how you are going to actually achieve the job because you cannot build every single requirement into your output or your functional specification. We would be looking to something that was performance based for the system, but we would also want to go down a level or two into defining overall architectures and so on.

**Mr COX**—Might we be helped by you telling us what you are going to do with airborne early warning and control aircraft?

**Mr Roche**—I was going to use that simply to draw out the example of different levels of risk, and that is based on a Boeing 737-700 airframe, which is virtually nil risk. There may be some slight aerodynamic risk from the things that are mounted on it externally. Some of the hardware already exists and is proven and can be put together, so that may be a higher risk than the airframe but is still not a great risk. When you move into the software, which is the nub of the system and which has not been done in this particular form before, you are again moving into a higher level of risk. I would be looking to a contract that treated those different parts of the proposal in different ways, and we would be monitoring and managing them differently, rather than having just the one.

**CHAIRMAN**—In considering the software portion of the contract, is it a consideration that it might be a joint development? In other words, Air Force and Defence might involve themselves closely in working with the contractor to evolve the system in a cooperative venture?

**Mr Roche**—I might ask Ray Conroy to speak to that. I would say that there is certainly going to be a large element of our input into the requirements, but whether we end up developing with them is another matter.

**Air Vice Marshal Conroy**—We intend to place total system performance responsibility on the prime contractor to deliver the functional performance that we write into the contract. Before we enter into that contract, however, we are in the process of conducting what we call a final systems design review, which is the specification of the aircraft as Boeing intended, in order to produce a product that meets those functional specifications. To test whether they have actually delivered the functioning product, obviously, we are not going to just sit back and take their word of honour that it will perform in accordance with what we expected from the outset.

We have contracted an Australian based independent validation and verification team, an industry team, on our behalf to conduct some of that test and evaluation. Some of the test and evaluation will be so complex that we have placed a foreign military sales contract with the United States Air Force, specifically with Electronic Systems Command, to assist us in verifying and testing, and ensuring that we know what it is we are getting. In subsequent service, a system like this will constantly evolve. We know that, and we will set in place processes for that evolution in service, but that latter aspect will not be part of the contract that we are negotiating at the moment.

**CHAIRMAN**—I am reminded of JORN and a flawed process where the main contractor could not sign off with the subcontractor with respect to software development and the A to D converter drivers out of the bunkers, and Defence would not sign off with Telecom. We had this huge stalemate that ultimately led to a four-plus years delay—or six, or whatever it was that we were going to wind up with—in the process because nobody worked together, it seems to me. We had this stand-off between Air Force and Defence, and the contractor and the subcontractor. So nobody was pulling together, and we had one lot of software being written off a million miles away and, as it turns out, my understanding is that they overwrote the codes so significantly that it will not fit on a 24-hour clock, so now we are going back and rewriting the blessed thing to make it fit into the time available. All these tensions are inherent, and then there are these tensions between Defence and this committee—and, I assume, between Defence and Foreign Affairs, Defence and Trade, Senate estimates and everything else. There are millions of words written in our newspapers and stories shown on television saying that we have not performed. I would like to be assured that somehow we can get the contractors, suppliers, Defence and the services arm trying to achieve the same outcome.

**Mr Roche**—Mr Chairman, perhaps I can respond to that. I certainly hope we do not have any difficulties with this committee. We are very conscious of the need to work more closely with industry, but I am cautious about going the whole way in the sense of working in integrated project teams for delivery purposes because, at the end of the day, it is the contractors who are saying to us that they can deliver a product to us at a given price. We have to do everything in our power to make sure that that can happen. We have to avoid placing unnecessary difficulties

in their way, but at the end of the day it is their responsibility and if we go completely in with them then we muddy that responsibility.

I think we can go a fair way towards partnerships. We have some good examples of early work on integrated project teams, and we also have some good examples of partnerships that do seem to be working. That is about as far as I would want to go, rather than to move into joint development. As soon as we move into joint development there is an equal sharing of the risks of the project, and that is not necessarily the way it is intended to be at the outset.

**Ms GILLARD**—I have some questions on another sort of contract management issue, not an acquisitions issue. I actually have some questions about a contract agreement entered into by the Defence Estate Organisation. As I am sure you are aware, the RAAF Williams-Point Cook site has been identified as surplus to Defence requirements and is marked for disposal in the next financial year. In the course of preparing for that disposal, the Defence Estate Organisation has entered into some airfield use agreements with the aircraft operators that fly out of Point Cook. In that agreement, because they do not want to spend maintenance money on the airfield, which is understandable given that they are preparing for disposal, the Commonwealth does not warrant or represent that the airfield is or will remain suitable for an operational airfield.

So what the Commonwealth is providing to the aircraft operator is less than would be provided to them at a commercial airfield where, presumably, the airfield operators are prepared to warrant that it is up to standard as an operational airfield and will continue as an operational airfield. Notwithstanding that what the Commonwealth is providing is less than is provided at a commercial airfield, the pricing structure for a single landing by a private aircraft at Point Cook is almost 40 times higher than the pricing structure to land at Moorabbin. Indeed, it is more expensive for a single landing at Point Cook than to land at either Tullamarine or Sydney airport during peak periods. Could you explain to me why that pricing structure has been adopted?

**Mr Roche**—Unfortunately, we do not have anyone here from the Defence Estate Organisation. I will have to take that on notice, Mr Chairman. I really do not have access to the detailed answer to that.

**Ms GILLARD**—Could you take that on notice. Secondly—and we have been talking here about the question of risk management over the past few days with each of the departments appearing before us—one of these agreements was entered into with the Royal Victorian Aero Club in respect of aircraft that it operates and its club members operate. That club is a non-profit incorporated association. The original position of the Defence Estate Organisation was that it required each of the directors of that non-profit incorporated association to give unconditional, unlimited and continuing personal guarantees.

As you would imagine, persons who are involved in non-profit associations might have some reluctance to execute a document like that. After a series of fairly vexed negotiations, the Defence Estates Organisation agreed to withdraw that requirement in exchange for a $500 increase in the security deposit. I would like an explanation as to how, from any point of view, the move from the requirement of unconditional, unlimited and continuing personal guarantees to $500 extra dollars can be justified as an appropriate risk management approach? I would be very interested in the explanation for that.

**Mr Roche**—It would be safer for me not to comment on that. We will provide you with a written answer.

**CHAIRMAN**—We will look forward to your advice. I have been asking department officials all week if you build buildings. We know Defence builds buildings. On the very first day of public hearings we held on this inquiry we interviewed the Master Builders Association, the Royal Australian Institute of Architects and the Institution of Engineers, and I believe all of them talked to us about what they perceived as a shifting of risk by the Commonwealth, by the Public Service. The way they described it was that when we had a Department of Housing and Construction and the Commonwealth really built lots of buildings, generally speaking a specification was developed, drawings were developed and, along with those documents going out to tenders, there was also a bill of quantities produced by a quantity surveyor, and that that took some of the risk out of tendering because each of the tenderers did not have to individually take off every brick, every piece of four-by-two timber, every nail and every bracket, et cetera. In effect, they accused the Commonwealth of risk shifting. Can you tell us how you approach your building contracts?

**Mr Roche**—Again, I regret that we do not have someone here from the DEO, so I am not in a position to provide you with a detailed answer on that. I will have to provide you with the written answer.

**CHAIRMAN**—You understand that the nature of the question is in association with risk shifting. We have been trying to identify whether or not the practices they refer to do exist and whether they are significant. We have been unable to find any answer so far. On project management, which also includes paying people for what they do, I note in your submission that you say:

> a resource management framework managing on an accrual and output basis, with supporting resource allocation and management systems—

good bureaucratic-speak—

> and contract payment according to achievement against project objective;—

I understand that that is using the earned value management system. My question is: to what extent are you now or do you intend to incorporate cost to complete in your analysis of contract payment?

**Mr Roche**—I will ask Mr Gairey to respond to that.

**Mr Gairey**—Under the earned value framework, one of the tools that is delivered, if you like, or one of the measures that is delivered is cost to complete. We are moving to a regime where, for the majority of our larger contracts, the payment mechanism is based on a mixture of predefined milestones and earned value. I do not recall the figures, and maybe somebody can help me with those, but we do require for contracts of specific value that an earned value management system is in place as part of the contract management mechanism, and for lesser value contracts a lesser form of earned value management. So we are in a better position now

than we were some years ago to actually have visibility of the sort of information you are talking about. Maybe somebody can remind me of the figures.

**Mr Fitzgerald**—I think the figures were $50 million for R&D contracts and $100 million for production contracts as the threshold at which we call up earned value or cost schedule control systems. I would need to confirm that. It is something of that order.

**CHAIRMAN**—I will get back to the nitty-gritty of the question again. I should not keep going back to major project failures in the past but I do note that both JORN and Collins—and you mentioned them in your submission—are excellent examples of how not to pay for a contract. We kept paying and paying and paying, and the costs to complete never really got examined adequately, to the point that we paid for almost all of the combat control system software and we are never going to get it. Likewise on JORN, we paid because they had done lots of work but did not examine in detail that critical little bit. You may have spent 97 per cent or reached 97 per cent earned value, but if you have another 50 per cent of the work yet to do, you should not have been paid 97 per cent of the contract value. It is just that simple.

**Mr Roche**—I think what Mr Gairey was saying was that we do include cost to completion in the earned value system, but we are looking these days at a mixture of earned value and milestones. The problem with the earned value system, if there is one, is the ability to open large numbers of packages of work and work on a very broad front but not necessarily achieve anything with all the packages that have been opened. You build in milestones as well as a check that they are actually achieving some progress, plus you have to keep your eye looking at that cost to completion.

**Mr Gairey**—Further, if we go back and look at the submarines JORN, neither of those projects as initiated used earned value or cost schedule control systems as part of the payment arrangements, hence management of the contracts.

**CHAIRMAN**—I accept that.

**Mr Gairey**—The version of cost schedule control or earned value management system that the submarine projects used omitted cost to complete as a parameter.

**CHAIRMAN**—But you will recall that this committee asked Defence on Collins why it did not step up the analysis of what had been agreed. At one point you ran two systems in parallel. Why not use the earned value as an indicator? We were told that the old system was fine and everything was jake. Then, at the end, we found out that was not jake and the cost to complete was quite substantial.

**Mr Gairey**—I think it is a fact of history that the Collins class did not have an earned value system or a cost schedule control system as its management mechanism, as we would currently understand it. The cost schedule control system was something that was added after the event and was intended not as a management mechanism for the contract but as a separate check. Unfortunately, the contractual arrangements in the case of Collins did not allow the information extracted from that system to be used for purposes other than maintaining the accreditation of their cost schedule control system.

**CHAIRMAN**—I point out for whatever it is worth that, in terms of public accountability transparency, over a long period of time, apparently the relationship between this committee and Defence has been less than satisfactory because we have asked questions about those systems and the answers we have got have been such as to lead us to believe that everything was hunky-dory and then we have found out that it was not. I mention this only to try to say to you that we need a more transparent relationship between Defence and this committee, and then perhaps you will not have us on your back so much, for whatever it is worth.

**Air Vice Marshal Conroy**—Mr Chairman, can I give you an example of how we are managing these types of issues in contemporary times compared with the past?

**CHAIRMAN**—Thank you.

**Air Vice Marshal Conroy**—I have got a contract with BAe Systems to deliver the lead-in fighter, the Hawk aircraft. It is a 75 per cent earned value, 25 per cent milestone contract, by and large—in the order of over $800 million. I have a milestone coming up in July. I have to have seven aircraft delivered online at Williamtown. My contract has liquidated damages if that milestone is not achieved; there is provision for that. The contract also makes provision to cease all earned value payments if that milestone is not met. So it is pretty severe. We are also in a very intense partnering arrangement. The end result we are after is aeroplanes online, not cash payments in particular.

**CHAIRMAN**—I understand you are always reluctant to drive the contractor broke. We understand that.

**Air Vice Marshal Conroy**—But the contract does allow me to cease all earned value payments if that milestone is not met.

**CHAIRMAN**—We have asked all the departments and agencies that have appeared before us over these three days about their attitude to the Auditor-General having automatic right of access to contractor records and, if necessary, contractor premises where Commonwealth goods are located. Defence continues to say—and in your submission you continue to say—that it is unnecessary to specifically stipulate the requirements of the Audit Act and conditions of a particular contract. We are increasingly finding it difficult to understand your position, particularly in light of our discussions with other departments and agencies where more than a majority—almost every one—have now included the standard provisions that DOFA put out, as requested by the Auditor-General and this committee to be included in contracts. We are finding it increasingly difficult to support your contention that it is unnecessary, undesirable or both.

**Mr Roche**—I came to this a little late. I joined Defence in November and I think that the position had already been put to you. I do have to say that I agree with the Defence position in some respects. I have no difficulty with access by the Audit Office to contractors' records and, if necessary, contractors' premises where the contractor is carrying out a function that would ordinarily be carried out by government. I know there is a concern on the part of parliament about outsourcing. Where a function that would be considered to be the provision of a community service normally provided by government is put into the private sector, it is not

acceptable necessarily for that to be put beyond public scrutiny. So I see that there is a difference in that case.

I think there is a case for access where, because of the nature of the project, the Commonwealth may have entered into some sort of cost-plus arrangement. I would see that as being no different from a normal commercial arrangement where, if I am entering into a cost-plus arrangement with a supplier, I seek independent access to verify the contractor's claims. But if I am simply buying some Ford sedans for my vehicle fleet, I cannot, for the life of me, see the basis of a requirement that I build into that contract access by the Auditor-General to the premises and records of the Ford Motor Company.

**Mr COX**—I hardly think that that is what we are suggesting. What we are talking about is the Auditor-General being able to examine major Defence suppliers' records—for example, in circumstances where there is evidence of fraud.

**Mr Roche**—If there is evidence of fraud, my view is that the proper way to deal with that is through the police. The difficulty is in deciding what would qualify specially for this inspection by the Auditor-General. But the case that has been put to me so far is a general requirement in Defence contracts for access by the Auditor-General. Very much of what we do relates to the acquisition of supplies that I do not believe should involve the contractor entering into any other levels of scrutiny over and above what would be normal in a commercial transaction.

**Mr COX**—If it is just malfeasance in terms of the performance of a contract, it is not something that the police would have an interest in, but it may involve a large waste of public money and that would be something that the Auditor-General might very well want to have an investigation into. He might want to determine, for example, whether the malfeasance was by the department or by the contractor.

**Mr Roche**—We are continually exhorted to be more like the private sector in our approach, to be more efficient and to strive for best practice, benchmark performance and so on. I do not see evidence of this sort of access in the private sector. I think that in the case of a particular project we might have the debate, but for the normal acquisition of supplies I do not see that it is appropriate. When you start adding these extra requirements on to contractors, that is when you start getting prices increased for dealing with the Commonwealth. What is the purpose of the Auditor-General's access? Is he able to do the equivalent of an efficiency audit? What protections are there for data that the Auditor-General takes from these people? Will he publish the data and so on? Our view is that if it is the view of the parliament, after listening to all the arguments, that the Auditor-General should have this access in the generality of cases—not in the specific cases that I have mentioned, where I would concede the point quite readily—the appropriate way to do it is through the Auditor-General's own act. The protections that are in there for the people that you are giving him access to should be spelt out at the same time.

**CHAIRMAN**—Mr Roche, I will give you three examples of why we think it is important, the first point being a generality. There is, rightly or wrongly, a public perception that, as governments sell off what are deemed to be commercial activities and outsource many of the activities that formerly the Public Service itself performed, there is a reduction in public accountability. That is one of the things that we are trying to test, in a sense, with this inquiry.

Personally—I can’t speak for my colleagues—I am pleased with an awful lot that I hear, quite frankly. Many departments have told us they now are examining performance against standards that they never had set before, much less the ability to examine them.

**Mr Roche**—Should we respond?

**CHAIRMAN**—No. Let me finish. So public perception is part of the issue. If we can say to the public, ‘The Auditor has access to the contractor records in the rare event that he deems he needs it—and remember that he is under constraint of a budget as well, and this all costs money,’ it is a matter of trying to tell the public that the Commonwealth and its Public Service and the parliament’s committees are not trying to hide information from the public. That is number one.

As No. 2, I remind you of the insurance case on the Collins project, with which you may not be familiar, Mr Roche. Had the Auditor had access, we might well have found out where the heck our $2.4 million went. You may say that is not a lot of money but we considered, and still do consider, that it was serious. As No. 3, back on Collins again and/or JORN: there were deficiencies in the payment systems themselves and so, realistically, in both those instances the Commonwealth paid for more than was there. The auditor had no right of access to contractor records to see how much really was left to be spent. Cost to complete is an issue I come back to over and over. So we have one generality and two instances in point.

**Mr Roche**—In relation to the first one, I do agree with you. I made the point earlier that, where a function which has a particular public service/community service nature about it is outsourced, there may well be a case for the Auditor-General to have access. To go to a specific example: if the provision of advice on people’s claims or entitlements to a social security benefit were outsourced, should that be subject to scrutiny by the Auditor-General? My instinct is to say yes, that the community would not unreasonably expect that.

In the case of the second case you quoted, the insurance case—and I do understand the difficulty and the frustration the committee feels about that one—I do believe that is more of a commercial issue which should have been tackled commercially. The data should have been there on our side to answer those questions.

**CHAIRMAN**—Sure, but it wasn’t?

**Mr Roche**—It would have been more effective for the Auditor-General to have had access to the Australian Submarine Corporation to have resolved that. But it should have been capable of being resolved from our data, as should have your third case. The issue is that if you are going to give the Auditor-General access to large contracts as a matter of routine—and you are saying that you do not want to do it in the case of vehicle fleet acquisition but you do want to do it in the case of JORN or Collins, and there are going to be a whole lot of grey cases in between times—where do you want the Auditor-General to stop? Because it is not dealt with in the legislation, there is no real limit on the documentation and material he might seek. It has been a while since I read the Auditor-General’s Act, but I would bet there is very little control over what he does with the data in terms of reporting on it. There is a whole heap of stuff there that he would have access to that would be considered to be very much commercial-in-confidence. It might mean in

the end that if you do want to give that access to the Auditor-General, you might find that you have a lot more shell companies tendering for your business.

**CHAIRMAN**—A statement by the Auditor-General said that, in the ANAO's experience, they had found that almost without exception the relevant issues of principle could be explored in an audit report without the need to disclose the precise information that could be regarded as commercial-in-confidence.

**Mr Roche**—That is an assurance, Mr Chairman.

**CHAIRMAN**—Can you imagine the outcry, Mr Roche, if the Auditor-General went in and looked at Boeing's books because they happened to be supplying us with aircraft and then told the world what their cost to manufacture some component was, resulting in some other organisation getting a commercial advantage in manufacturing that component? I would have thought that would have been huge. You are essentially saying that our Audit Office is not responsible.

**Mr Roche**—No, not at all. I am saying that if you want to do something that is not a standard commercial practice and goes well beyond a commercial practice in the acquisition or in the contracting for supplies or goods and services, then you should spell out with some precision in the legislation what access the Auditor-General is to have and what safeguards there are. I do not believe it is satisfactory to work off an assurance from the Auditor-General. I know the Auditor-General well and have the greatest regard for his assurances, but if I were somebody that was being given unlimited access by the Auditor-General, if I were a company dealing with the Commonwealth, I would definitely want to know what my rights were, what the Auditor-General could look at and what he could do with the information he took. I think it is perfectly reasonable.

**CHAIRMAN**—How did the United States defence establishment come to the conclusion that their audit investigations should have the automatic right of access to all contractor records? Do we have such a huge defence establishment that we cannot support such an initiative?

**Mr Roche**—We have come to different conclusions to the United States in a number of areas. In many respects I would say that what the Commonwealth is doing in financial management reform and in public sector reform is well ahead of the United States. I am not really sure that they are a good model for us in this.

**CHAIRMAN**—Good try!

**Dr Kearns**—I think it might be worth adding, Mr Chairman, that many of the United States Defense Department contracts have been cost-plus.

**CHAIRMAN**—But not all of them.

**Dr Kearns**—No, but they do come from a very heavily cost-plus environment.

**CHAIRMAN**—And increasingly they are not. It is my understanding and I think yours too, that they are moving away from cost-plus contracts but that they have not removed that requirement.

**Dr Kearns**—My point is that the arrangements they have put in place have their origins in that particular contracting environment, and that is very different from the environment in which we operate here.

**CHAIRMAN**—We are telling you that you are now operating in an environment where public trust is an important consideration. This committee believes strongly—it has put it in writing, so I can speak for every member of the committee—that we would increase public trust in public accountability if we allowed the Auditor-General automatic right of access. Anyhow, we are just beating it to death and not getting anywhere.

**Mr COX**—I think we should go on with this a bit further. Defence is the only agency that has been before us that suggests it is a problem. We have asked all of the other agencies who have included those sorts of terms in their contracts what the reaction of their suppliers was. Those agencies have said that certainly they had to explain to their suppliers what it meant but their suppliers then did not have any problem with it. We asked if they said they did not have any problem with it but it would cost them. They said they had never had problems of that nature. So it is Defence all by itself out on its lonesome on this. It is a deepening suspicion of mine that Defence finds it enormously convenient to have the audit trail end at the interface between Defence and the contractor because in the circumstance such as the one that the chairman described the auditor is unable to pursue possible malfeasance where Defence perhaps conveniently does not have records.

**Mr Roche**—I do not believe it is reasonable to draw those inferences or to say that we are making any judgments about the Auditor-General. What we are saying is that we are being exhorted more and more to become more efficient and more effective in our acquisition processes. We are being told there is best practice out there in the commercial world. What you are suggesting here is something that is quite foreign to the commercial world. It is not happening in the commercial world. You are suggesting a blanket approach in our contracts to access by the Auditor-General in all contracts and even down to fleet purchases. Even though you say not fleet purchases, there has been no suggestion made as to where the line would be drawn, and where the supplier of normal goods and services to a range of people may have to be subject to an investigation by the Auditor-General.

**Mr COX**—I would not put the emphasis on the word ‘blanket’. I would put the emphasis on circumstances where there is evidence of malfeasance or fraud which is the only reason the Auditor-General would have an incentive to go and have a look.

**Mr Roche**—I guess we are going to have to agree to disagree on that. I am not uncomfortable about Defence standing alone if we believe that our view is right. What I do not understand is why the parliament would not consider it appropriate to change the Auditor-General’s act to make this quite explicit. The sort of thing we are talking about does involve potential privacy issues. It certainly involves commercial confidentiality issues. I do not understand why you recommend the route of trying to provide the access by a variety of contract modifications rather

than by very clear-cut and explicit law that includes conditions on how far he may go and safeguards for the information that is taken.

**Mr COX**—A substantial part of the reason we are having an inquiry is so that we are able to make some substantial recommendations in this area. We are looking for substantial issues that departments can raise that would help give us some guidance as to how we might frame those recommendations so it deals with the actual concerns and not airy-fairyness, red herrings and blanket opposition.

**CHAIRMAN**—Mr Roche, the answer to your question is very simply that we have so recommended and we were advised yesterday that cabinet is considering that.

**Mr Roche**—We would be happy if you would consider a further supplementary submission from us on the sorts of things that might be in this legislation.

**CHAIRMAN**—We are simply trying to encourage you to do what other departments have agreed to do which both we and the Auditor-General recommended some time ago. But we went further as a result of Collins and recommended that the legislative provision be put in place. I suspect your minister might oppose that in cabinet. We have no idea of the outcome, but we have so recommended.

**Mr COX**—We would like a further submission on the substantial issues if you are able to put your mind to it and provide one.

**Mr Roche**—We would be happy to provide that because our position is not one of blanket opposition. I think it is unreasonable to characterise it as that. Our position is that there are some cases where we would most certainly agree with the committee's view and there are other cases where we would consider it less appropriate. We might have a go at teasing out that spectrum, if we could, in a further note.

**Mr COX**—That would be excellent.

**CHAIRMAN**—Thank you for coming and for your submission.

**Mr Roche**—I trust that our relationship is going to be rather—

**CHAIRMAN**—It is always robust.

**Mr Roche**—Not robust but more productive with the committee. We do understand that we may have been seen as being a little insular in the past. We are certainly trying our best to be more open both with the people we deal with in industry, parliamentary committees and internally.

**CHAIRMAN**—I would have thought the adjective was 'insufficient'.

Resolved (on motion by **Mr Cox**):

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 12.11 p.m.**