

Chapter 6

The A2 Dairy Marketers project

Background

6.1 On Sunday 29 August 2004, the day the federal election was announced, the Hon De-Anne Kelly MP, then Parliamentary Secretary to the Minister for Transport and Regional Services, approved a \$1.27 million grant under the Regional Partnerships Program. The grant was to test herds for A2 milk-producing cows and establish an A2 milk processing plant on the Atherton Tablelands, Qld. The funding was to be used for a joint venture between A2 Dairy Marketers Pty Ltd (A2DM – the proponent), Mungalli Dairy Pty Ltd and several Atherton Tablelands dairy farmers. The grant approval was announced during the election period on 8 September 2004 and A2DM went into voluntary administration on 4 October 2004—after only five months of trading and less than a month after the grant was announced. Approval of the grant was then withdrawn.

6.2 This chapter examines A2DM, the history of its applications for funding under the Sustainable Regions and Regional Partnerships Programs, the actions taken by various bodies and individuals in the application process, and the overall impact of the proposed A2DM project, the grant announcement and its subsequent withdrawal, on the Atherton Tablelands dairy industry.

6.3 The A2DM project draws out some serious concerns with the administration of both the RPP and the SRP, including: advice from an advisory committee being ignored or not acted upon; ministers or parliamentary secretaries expediting projects at the expense of a full assessment being undertaken; the role and influence of ministerial advisers on the programs; and the adequacy of due diligence processes.

A2 milk

6.4 All cows' milk contains a type of protein called beta-casein, two variants of which are β -casein A¹ ('A1') and β -casein A² ('A2'). Cows usually produce milk containing both A1 and A2, although the levels of each protein vary considerably between and within breeds and up to one in four cows do not produce A1 at all.¹ A2 milk refers to cow's milk that does not contain the A1 protein, and is produced by selectively milking cows that do not produce A1.² Cows can be genetically tested to determine whether they produce the A1 casein, at a cost of about \$25 per test.³

1 K. Tailford, C. Berry, A. Thomas and J. Campbell (2003) 'A casein variant in cow's milk is atherogenic', *Atherosclerosis* 00 (2003) 17, p. 3; *Committee Hansard*, 13 April 2005, p. 71.

2 L. Edmiston (2004) 'Doubts over benefits of new milk', *The Courier-Mail*, 1 July 2004, p. 10.

3 Mr Strazzeri, *Committee Hansard*, 13 April 2005, p. 86.

6.5 A2 milk patents are based on studies that suggest a connection between consumption of A1 and type 1 diabetes, vascular disease and neurological disorders. However, this connection has not been proven in humans and many independent scientific and medical groups have said there is no strong scientific evidence to back up these claims.⁴ The worldwide holder of A2 milk patents is New Zealand company A2 Corporation Ltd.

A2 Dairy Marketers Pty Ltd

6.6 This section provides a brief outline of A2DM's operations outside the Atherton Tablelands, from the company's establishment until the time it went into voluntary administration.

6.7 A2 Dairy Marketers Pty Ltd (A2DM) was established by Brisbane businessmen Mr Lindsay Stewart and Mr Phil Roberts. The company was registered on 12 November 2003 and Mr Stewart and Mr Roberts were appointed company directors on the same day. Mr Stewart, Mr Roberts and their wives were the only shareholders, and commenced the company with \$2 start-up capital.⁵

6.8 In evidence given to the Committee, Mr Stewart said the other A2DM director was Mr Chris Saddler, a stock agent. However, the Committee has been unable to establish that Mr Saddler was ever legally appointed as a director. Mr Stewart's evidence indicated that Mr Saddler was responsible for supply of A2 milk, Mr Roberts was primarily responsible for the administrative and financial aspects of the company and Mr Stewart was the marketing specialist. Mr Greg Little, managing director of a milk distributor, was also involved in managing the distribution and logistics functions of A2DM.⁶

6.9 A2DM entered into a licence agreement on 22 December 2003 with A2 Corporation Ltd to sell A2 milk anywhere in Australia and to access patents for the testing of cows and milk. As part of the agreement, A2DM was required to pay the A2 Corporation a royalty of 10.75 cents per litre of A2 milk sold.⁷

6.10 In late 2003, A2DM engaged a public relations consultant and an advertising agency. Mr Stewart told that Committee that the advertising agency, Cooe Advertising, recommended that A2DM employ a government liaison consultant, and suggested Mr Ken Crooke, a director of the Asia Pacific Corporation (a government

4 L. Edmiston (2004) 'Doubts over benefits of new milk', *The Courier-Mail*, 1 July 2004, p. 10.

5 Mr Stewart, *Committee Hansard*, 13 April 2005, pp 31 and 68.

6 Mr Stewart, *Committee Hansard*, 13 April 2005, pp 34-35.

7 Mr Stewart, *Committee Hansard*, 13 April 2005, pp 41 and 46; licence agreement between A2DM and A2 Corporation Ltd, dated 22 December 2003, in A2DM liquidator's documents, received 8 April 2005.

relations consulting firm).⁸ Mr Crooke's role in relation to A2DM's applications for funding is discussed later in the chapter.

6.11 A2DM commenced trading in south east Queensland on 1 May 2004.⁹ The launch was accompanied by a marketing campaign that included extensive television advertising. Mr Stewart told the Committee that A2DM could not fulfil its supply obligations from the first day:

At the launch of the company we were promised by one director, who was in charge of the supply of A2, that we would have 25,000 to 30,000 litres per day. On saying that, we put a heavy marketing campaign together to justify that. When we launched he had 6,000 litres, so the company was in a situation where we had back orders and things like that, which I sometimes said was a good thing because it was creating demand, but it was a panic mode. We had sales there that we could not deliver because of promises or lies by directors.¹⁰

6.12 The A2 milk sold in south east Queensland was sourced from dairy farmers located in the Gympie area. A2DM paid a farm gate price of 50c per litre for the five months it traded, and sold the milk for between \$4.09 and \$4.29 per two litre bottle.¹¹

Financial situation and legal action against A2DM

6.13 A2DM appears to have been in a tenuous financial situation from the time it began trading in May 2004. Between June and August 2004, A2DM was late paying its contracted southern Queensland A2 milk suppliers and could not pay its suppliers out of the operation of the business.¹²

6.14 Mr Stewart told the Committee that several times at board meetings he had raised concerns that the company's accounts were not accurate:

We employed a full-time accountant and were under the directorship of Phil Roberts, who was mainly in charge of the funding and the office arrangements, because I was travelling, launching the product and things such as that. So I would attend the board meetings, and the minutes will show that there were a couple of times where I did raise the question about finance and the capabilities of the people that were running A2.¹³

6.15 Queensland Health met with A2DM in late May 2004 and questioned the corporation's use of health claims in its A2 milk advertising campaign. A2DM's

8 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 47.

9 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 33.

10 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 34.

11 Mr Stewart, *Committee Hansard*, 13 April 2005, pp 71-72.

12 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 37.

13 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 34.

website and advertising campaign made claims that A2 milk reduces the risk of heart disease, diabetes and neurological disorders such as autism that have been linked by some studies to A1.¹⁴ In September 2004, A2DM was convicted and fined \$15,000 by the Brisbane Magistrate's Court for making misleading health claims in breach of the *Food Act 1981*. A spokesperson for Queensland Health said that 'the [Queensland] Government was compelled to take action because A2 Dairy Marketers had inferred ordinary milk was unhealthy'.¹⁵

6.16 A2 Dairy Marketers went into voluntary administration on 4 October 2004 and a liquidator was appointed on 11 November 2004. At the time it went into administration, A2DM had a debt of \$126,146.11 to the Department of Agriculture, Fisheries and Forestry for the 11c per litre Dairy Industry Adjustment Levy (DIAL), incurred between May and September 2004.¹⁶ A2DM also owed Dairy Australia \$82,480.59, which probably related to an unpaid research and development levy.¹⁷

A2DM's applications for SRP and RPP funding

6.17 This section outlines the events leading up to the announcement of the RPP grant to A2DM to establish an A2 milk processing plant on the Atherton Tablelands. It also examines the involvement of various stakeholders, including politicians, a ministerial adviser, the Atherton Tablelands Sustainable Region Advisory Committee (ATSRAC), the Far North Queensland Area Consultative Committee (FNQACC) and DOTARS.

The expression of interest for SRP funding

6.18 Evidence to the Committee suggests that Mr Crooke (A2DM's government liaison consultant) and the A2DM directors had some preliminary meetings and discussions with ATSRAC members and staff during May 2004 regarding possible SRP funding to test cows and establish an A2 milk processing plant in the Atherton Tablelands. These meetings and discussions are outlined in more detail below.

6.19 Although there may have been earlier contact with the executive officer of ATSRAC,¹⁸ the Committee received evidence that the first time A2DM made written representations regarding the possibility of RPP or SRP funding was in a letter from Mr Stewart to the Hon John Anderson MP, then Deputy Prime Minister and Minister for Transport and Regional Services on 10 May 2004. The letter requested

14 L. Edmestone, 'Doubts over benefits of new milk', *The Courier-Mail*, 1 July 2004, p. 10.

15 S. Dwyer quoted in ABC Queensland, 'Court fines dairy distributor over milk claims', 30 September 2004.

16 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 39.

17 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 40. For further information about A2DM's financial status, refer to A2DM liquidator's documents, received 8 April 2005.

18 Mr Crooke, email to Mr Saddler, 6 May 2004, in A2DM liquidator's documents, received 8 April 2005.

information on the availability of 'government assistance schemes' such as RPP and SRP and 'urgent consideration of a proposal to fund the establishment of a production facility to process A2 milk on the Atherton Tablelands'.¹⁹

6.20 Mr Stewart's letter also highlighted A2DM's willingness to pay a farm gate price of 50 cents per litre – significantly higher than the incumbent processor and a possible boon to the drought and deregulation affected Atherton Tablelands dairy industry. The letter referred to a discussion between Mr Stewart and Ms Wendy Armstrong of the minister's office and foreshadowed A2DM's meeting of 17 May with then ATSRAC Executive Officer, Ms Yvonne Tunney (as discussed below).²⁰

6.21 In an email of 6 May 2004, Mr Crooke also stated that he had scheduled a meeting on 17 May with Ms Tunney to discuss a possible application for SRP funding. The email said:

Behind the scenes I have opened the door a little and it should be possible for us to have a suitable letter tabled at the next meeting of the Committee (scheduled for May 28th/29th). At this stage they would only look at a brief concise description of what A2 wants to do.²¹

6.22 On 20 May 2004, Mr Stewart sent Ms Tunney a draft letter to be presented to the ATSRAC meeting scheduled for 28 and 29 May. The letter was almost identical to Mr Stewart's letter of 10 May to Mr Anderson. It contained background information about A2 milk and requested support to test cows and consideration of a proposal to establish a processing facility.²² Ms Tunney replied to Mr Stewart on the same day, providing some feedback on the letter and suggesting it include information about the contribution A2DM and other project partners would make to the project.²³

6.23 Mr Stewart revised the letter according to Ms Tunney's comments and sent the revised letter, dated 26 May 2004, to then ATSRAC Chairman Mr Peter McDade. The amended letter outlined 'investment options' for establishing an A2 milk processing plant, including a joint venture with Cuda Brothers dairy, located on the Atherton Tablelands.²⁴

19 Mr Stewart, correspondence to Minister Anderson, 10 May 2004, in A2DM liquidator's documents, received 8 April 2005.

20 Mr Stewart, correspondence to Minister Anderson, 10 May 2004, in A2DM liquidator's documents, received 8 April 2005.

21 Mr Crooke, email to Mr Saddler, 6 May 2004, in A2DM liquidator's documents, received 8 April 2005.

22 Mr Stewart, email to Ms Tunney, 20 May 2004, in A2DM liquidator's documents, received 8 April 2005.

23 Ms Tunney, email to Mr Stewart, 20 May 2004, in A2DM liquidator's documents, received 8 April 2005.

24 Mr Stewart, correspondence to Mr McDade, 26 May 2004, in A2DM liquidator's documents, received 8 April 2005.

6.24 Mr McDade told the Committee he had a preliminary meeting with Mr Crooke, Mr Roberts, Mr Saddler and one other A2DM representative whose name he could not recall on 26 May 2004 to discuss the possibility of a future A2DM application for SRP funding.²⁵ The meeting was initiated by Mr Crooke and took place in Brisbane.²⁶

6.25 Mr McDade said there was no mention of politicians during the meeting.²⁷ Rather, the A2DM representatives were more interested in the processes and timeframes for SRP applications:

They were asking, 'What sort of time limits do we have on the processes here?' I explained our processes to them and said: 'You know, we cannot rush things through. This is government money. It is a public program. But, if you get something to my executive officer and it is in a suitable form, then I will ask the committee to consider whether it is appropriate to consider it as an expression of interest.'²⁸

6.26 ATSRAC considered Mr Stewart's letter of 26 May at its meeting of 28 and 29 May and resolved that A2DM be invited to submit a detailed expression of interest (EOI). On 11 June 2004, Ms Tunney emailed Mr Stewart and invited him to lodge an EOI by 16 July to be considered at ATSRAC's meeting of 6 August.²⁹ She also provided some guidance about the information that would need to be included:

...whilst we won't need detailed business plans etc at EOI stage we will need to see some detailed budget information and indication of future viability/sustainability.³⁰

6.27 A2DM completed an expression of interest form for \$100,000 of SRP funding to subsidise farmers to test cows for the A2 protein.³¹ ATSRAC considered the form at its meeting of 6 August 2004 and declined to accept it as an expression of interest for SRP funding because it did not address the criteria of the SR program or ATSRAC's criteria for an expression of interest.³² The ATSRAC minutes indicated the matters ATSRAC took into consideration when deciding not to accept the expression of interest:

25 Mr McDade, answer to question on notice, received 14 April 2005.

26 Mr McDade, *Committee Hansard*, 13 April 2005, p. 150.

27 Mr McDade, *Committee Hansard*, 13 April 2005, p. 151.

28 Mr McDade, *Committee Hansard*, 13 April 2005, p. 151.

29 Ms Tunney, email to Mr Stewart, 11 June 2004, in A2DM liquidator's documents, received 8 April 2005.

30 Ms Tunney, email to Mr Stewart, 11 June 2004, in A2DM liquidator's documents, received 8 April 2005.

31 A2DM expression of interest for SRP funding, undated, in A2DM liquidator's documents, received 8 April 2005.

32 Mr McDade, *Committee Hansard*, 13 April 2005, p. 150.

The Committee considered a number of issues and aspects of the A2 Milk Marketing project including:- Impacts of A2 Milk initiative and possible establishment of processing facility in the Tablelands region—how would the existing processor and industry be impacted?

Consideration of regional dairy industry initiative—this has been developed through long-term planning since deregulation and the Advancing Grow Malanda forum supported by ATSRAC in October 2003.

No indicated financial input from A2 apart from in-kind—the ATSRAC criteria have always considered a commercial entity should contribute at least 50% of future actual cash contributions to any project.

There is no information on what would occur past the initial testing—there are references to a processing facility but no firm indication how this might be established.

There is no information as to the market situation or supply chain development process.

The issues of competitive neutrality in relation to the existing industry are not addressed.

ACTION: ATSRAC endorsed decline of the Expression of Interest as the proposal does not address the criteria of the program.³³

The application for RPP funding

6.28 A2DM also made an application for funding under the Regional Partnerships Program. The suggestion of applying for RPP funding appears to have originated from a meeting of 11 June 2004 between the parliamentary secretary, Mr Stewart, Mr Roberts and Mr Crooke. Ms Leslie Riggs, then Assistant Secretary of the DOTARS Regional Communities Branch, was involved in the meeting by teleconference, as was a DOTARS project officer.³⁴ Mr Stewart told the Committee that the parliamentary secretary called the DOTARS officers and asked about appropriate channels to provide federal government funding for an A2 milk processing plant on the Atherton Tablelands. It appears that this was the first time DOTARS became aware of the project.³⁵

6.29 The local ACC, which is based in Cairns, was first notified about the possibility of A2DM making an RPP application via an email on 15 June 2004 from the DOTARS office in Townsville. The same email alerted FNQACC to the parliamentary secretary's particular interest in the project.³⁶

33 Mr McDade, *Committee Hansard*, 13 April 2005, pp 150-151.

34 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 52.

35 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 55.

36 Mr Vieira, *Committee Hansard*, 13 April 2005, pp 98, 112-113.

The first proposal for RPP funding

6.30 In an email to Mr Stewart dated 21 June 2004, Mr Crooke claimed that he had managed to fast-track the application process:

After some further 'negotiation' had been successful in cutting out the first phase of the Cairns application, the requirement to submit a brief to the [FNQACC] board, and with the board then considering whether to invite a full application, we have been invited to go direct to the full application. However they have asked for it to be in Cairns by close of business, Wednesday, 23 June.³⁷

6.31 The Committee has been unable to ascertain who Mr Crooke's 'negotiations' were with. Neither Mr Robert Blanckensee, FNQACC Chair or Mr Tomas Vieira, FNQACC Executive Officer could recall having contact with Mr Crooke.³⁸

6.32 Mr Stewart sent an incomplete RPP application form to Mr Vieira on 22 June 2004 requesting funding for a joint venture between A2DM and Cuda Brothers Dairy for a milk processing plant at the Cuda family dairy at Tolga. The proposal contained background information about A2 milk and A2DM's operations, information about the Atherton Tablelands dairy industry, the potential benefits of an A2 milk processing plant, a brief marketing strategy and information about the company structure. Stage one of the proposal involved testing 3,500 cows at \$30 a head, and stage two involved establishing the milk processing facility in partnership with the Cuda family.³⁹

6.33 Mr Vieira said that he first met with Mr Stewart on 6 July 2004. Mr Vieira described the purpose of the meeting as being to provide feedback and advice as to how the application might be strengthened.⁴⁰ At the meeting, Mr Vieira assisted Mr Stewart to develop the application and suggested it needed stronger regional partnership elements. It appears that A2DM then revised the proposal and changed partners so as to broaden the project and include more local ownership.⁴¹

The application

6.34 A2DM lodged an RPP application directly with DOTARS on 9 July 2004⁴² for a partnership between A2DM, Mungalli Dairy and local dairy farmers for funding to subsidise the farmers for the testing of A2 cows and establish an A2 milk

37 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 98.

38 Mr Blanckensee and Mr Vieira, *Committee Hansard*, 13 April 2005, p. 99.

39 Mr Stewart, correspondence to Mr Vieira, 22 June 2004, in A2DM liquidator's documents, received 8 April 2005; A2DM incomplete RPP application, undated, in A2DM liquidator's documents, received 8 April 2005.

40 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 98.

41 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 115.

42 Mr Yuile, *Committee Hansard*, 14 April 2005, p. 76.

processing plant at Mungalli Dairy. The Committee was unable to obtain evidence regarding the reasons A2DM lodged the application directly with DOTARS rather than submitting it to FNQACC after Mr Vieira had provided advice on the original proposal.

6.35 Mr Stewart told the Committee that the Atherton Tablelands operation was intended to be entirely separate from A2DM and that funding was to be conditional on transferring a cleanskin company owned by Mr Stewart and Mr Roberts, Star International Group, into the ownership of all project partners.⁴³ This funding condition is discussed below in relation to due diligence assessment.

6.36 A meeting regarding the possible A2 grant was held on 31 July 2004 between the parliamentary secretary (who chaired the meeting), representatives of A2DM, Mr Vieira and nine or ten local dairy farmers.⁴⁴ Mr Joe Strazzeri, one of the dairy farmers who attended the meeting, recalled that the parliamentary secretary:

...gave us a briefing and promised that she would do something about it, because she wanted us to be able to negotiate for prices and get better returns...She gave a commitment that she would look into the grants and see what she could do. That is all we knew, as farmers. After that, we went home.⁴⁵

6.37 Mr Vieira described his role at that meeting as examining the viability of the existing Atherton Tablelands dairy industry and gauging whether A2DM's project had the support of local farmers.⁴⁶ He told the Committee the meeting of 31 July was the first time he became aware the application had changed from its original form as a partnership between A2DM and Cuda Bros Dairy:

I think that is where I learned of the change—when we talk of the change—with Mungalli's addition. I thought that was a great move because at least that meant greater local ownership in the project.⁴⁷

6.38 As it is unusual for a minister or parliamentary secretary to attend meetings in relation to an RPP application, the Committee asked whether FNQACC was encouraged to accept the project by the parliamentary secretary:

Senator O'BRIEN—Was it clear from the meeting that Parliamentary Secretary Kelly wanted the project to succeed or get up?

Mr Vieira—My understanding or my feeling was that, yes, she would have liked to support the dairy farmers on the tablelands.⁴⁸

43 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 78.

44 Mr Strazzeri, *Committee Hansard*, 13 April 2005, p. 83.

45 Mr Strazzeri, *Committee Hansard*, 13 April 2005, p. 90.

46 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 100.

47 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 127.

48 *Committee Hansard*, 13 April 2005, p. 128.

Fast-tracking of the application process

6.39 The parliamentary secretary and others have been reported as stating that the A2DM application for RPP funding was fast-tracked.⁴⁹ Although DOTARS witnesses claimed that all due diligence checks normally carried out at that stage had been passed,⁵⁰ it appears that political pressure led DOTARS to bypass the advice of the ACC and due diligence checks that should have uncovered A2DM's financial problems and the legal action being taken against it by a state government.

6.40 Dr Gary Dolman, then Assistant Secretary of DOTARS Regional Communities Branch, provided the following observations about the fast-tracking of RPP applications:

There are...occasions when time critical projects are sought to be fasttracked. Generally, that is at the request of the proponent, where they say they need the money within a certain time. As the ACC said, it is the experience of other ACCs that, where we are asked to try and fast-track an assessment, which means doing the same amount of work on the assessment but doing it more quickly, we do try and do that where there is seen to be a good reason, a good case for doing so—where there is a community need to have the money quickly.⁵¹

6.41 DOTARS witnesses told the Committee that the application made by A2DM passed through the initial due diligence tests that are applied to all projects. The due diligence process commenced on 9 July 2004, when the application was received by the Department, and was completed on 27 August, when DOTARS provided advice to the parliamentary secretary.⁵²

6.42 In assessing the application, DOTARS sought background information about A2DM's proposal from Mrs Lyn O'Connor, an independent consultant and advocate for the Atherton Tablelands dairy industry, who in evidence to the Committee said she had provided DOTARS and FNQACC with feedback on various RPP applications.⁵³ Mrs O'Connor described to the Committee the sense of time pressure associated with the A2DM project:

During my previous contact with DOTARS, the dialogue and time frames around seeking and providing input have been reasonable. With the A2 project, there was a different climate and a sense of haste and pressure.⁵⁴

49 L. Taylor, 'Nats' milk plan turns sour', *Australian Financial Review*, 1 December 2004, pp 1, 7.

50 Ms Riggs, correspondence, received 12 July 2005, p. 3.

51 Dr Dolman, *Committee Hansard*, 14 April 2005, pp 78-79.

52 Dr Dolman, *Committee Hansard*, 14 April 2005, p. 76.

53 Mrs O'Connor, *Committee Hansard*, 13 April 2005, pp 2, 4.

54 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 3.

6.43 The Committee was also concerned as to whether FNQACC was pressured to provide comments on the application within a reduced timeframe. DOTARS and FNQACC witnesses could not recall the date the application was sent to FNQACC through the TRAX system for comment. Committee members asked whether the ACC was asked to provide comments in less than the normal timeframe, and Dr Dolman told the Committee that the ACC was asked by the DOTARS officer that attended the FNQACC meeting of 6 August to provide comments within the ten day timeframe set out in the internal procedures manual.⁵⁵

6.44 However, as discussed in relation to Tumbi Creek, the Regional Partnerships Internal Procedures Manual states that this timeframe does not apply to applications submitted directly to the Department and not prepared in conjunction with the ACC.⁵⁶ As the A2DM application was submitted to DOTARS and the revised application was not prepared in conjunction with FNQACC, it stands to reason that the ACC should have had a longer time frame to examine the application.

FNQACC advice on the application

6.45 The Committee was concerned to understand the rationale for FNQACC's recommendation about the A2DM application and the extent (if any) to which the ACC should have undertaken a due diligence assessment.

6.46 FNQACC's Executive Officer Mr Tomas Vieira and Chair Mr Robert Blanckensee made it clear to the Committee that while the ACC had made a strong recommendation to DOTARS that further research should be undertaken before the project was approved, due diligence was not the responsibility of ACCs and they were not resourced to undertake it. Mr Blanckensee said the ACC believed its role was to 'provide the reconnaissance information for the department and the minister for their consideration'.⁵⁷ However, Mr Blanckensee and Mr Vieira were informally aware through their relationship with ATSRAC that a request for SRP funding existed and that ATSRAC did not support it.⁵⁸ This prompted the ACC to delve '...a little deeper than normal into finding out what was happening...'⁵⁹

6.47 Both Mr Vieira and Mr Blanckensee commented on the 'disjunction in the information flow' that can occur when applications are submitted directly to DOTARS rather than developed in conjunction with the ACC.⁶⁰ They explained that it is preferable for the ACC to work with the proponent to address any deficiencies in an

55 Dr Dolman, *Committee Hansard*, 14 April 2005, pp 78-79.

56 DOTARS, *Submission 14*, Attachment E, Regional Partnerships Programme Internal Procedures Manual September 2004, p. 58.

57 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 120.

58 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 104.

59 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 102.

60 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 126.

application before it is submitted and before the ACC is required to provide comments to DOTARS:

When the process goes the way this one has, it has come through a different channel. When we are working with the ACC or the proponent, we are trying to say, 'This project has legs but you need this, this and this.' We are making sure all the i's are dotted and all the t's are crossed so that the considerations can be made.⁶¹

6.48 The FNQACC received a briefing on the A2DM application from Mr Vieira at its meeting of 6 August 2004.⁶² At the meeting, members discussed 'the composition and benefits of A2 milk, as well as the product's 'niche' market and impact on current dairy farmers'.⁶³ Subsequent to the meeting, Mr Vieira disseminated the application to FNQACC members and requested their comments. The ACC made some judicious comments about the application, as recorded in the TRAX system on 26 August. Mr Blanckensee summarised the ACC's concerns as follows:

...at the time, you have to remember that the Atherton Tableland was still suffering in the grips of a drought that had virtually crippled the area. It saw milk production sink to probably an all-time low. The other concern we had was that, if you throw a competitor into such an economic situation as we had there, which was very depressed, you may have enough to sink the other organisation. I believe that Dairy Farmers was on a knife edge with regards to the critical level of production...I do not think that we would all be happily sitting around the table here with the \$1.3 million being given to one organisation while 134 permanent jobs disappeared from the region. I do not think we would have been doing our job if we had not brought that to the attention of people.⁶⁴

6.49 Mr Blanckensee explained FNQACC's decision to give the project a rating of 3 (medium priority) by saying that it fitted the TRAX description of 'medium priority' and met a number of the criteria in the strategic plan, because it would have an overall benefit to the region. It was not rated a high priority because ACC members thought the timing was wrong and extra work needed to be done before the project should proceed.⁶⁵ Mr Blanckensee also observed:

At face value the project looked as if it could have had potential for the region and could have delivered the panacea that we needed for the dairy industry. The concern we had was that if it went ahead it might have

61 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 126.

62 Mr Vieira, *Committee Hansard*, 13 April 2005, p. 112.

63 FNQACC Minutes 6 August 2004, p. 5, in FNQACC minutes and recommendations, received 1 April 2005.

64 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 105.

65 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 129.

destroyed the dairy industry, because we would have seen another organisation go under.⁶⁶

6.50 FNQACC's overall recommendation was that the project warranted further investigation by DOTARS, but '[u]ntil the competitive neutrality issue is clarified, FNQ ACC Inc. members cannot recommend this project any higher than 3'.⁶⁷

The question of due diligence

6.51 The Committee is concerned that due to political pressures to process the application within a short timeframe, a proper due diligence process was not undertaken by the department. The department's explanation was unconvincing and inadequate:

It is true that the department did do the normal internal due diligence assessment for this project. The details of that assessment involved confirming the company's registration, its GST registration and ABN. It involved reviewing the business plan that was provided by A2 Milk and also cash flow forecasts. It also involved checking the development approval.⁶⁸

In other words, the department's assessment was superficial and hasty.

6.52 Mrs O'Connor, the local dairy industry expert who provided DOTARS with some advice about the A2DM application, expressed some concerns about the lack of information DOTARS had regarding the application:

Was it to be directed towards shares, testing, purchase of plant and equipment? How does that fit within the guidelines? I certainly have a lot of questions which I believe the department should have had time to consider fully. I do not need the answers to them, but the department certainly should have them.⁶⁹

6.53 It appears that A2DM provided little in the way of financial data to support its application for RPP funding, and the information provided was restricted to internally generated cash flow projections and forecasts for the Atherton Tablelands operation.⁷⁰ Mr Stewart said the company was not required to provide current financial statements and the only financial information he can recall being requested to provide by

66 Mr Blanckensee, *Committee Hansard*, 13 April 2005, p. 130.

67 FNQACC TRAX comments on A2 Milk Processing project, 26 August 2004, in FNQACC minutes and recommendations, received 1 April 2005.

68 Dr Dolman, *Committee Hansard*, 14 April 2005, p. 90.

69 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 3.

70 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 58.

DOTARS was '...the financial spreadsheets and our projection on supply of, I think, 40,000 litres per day up here'.⁷¹

6.54 DOTARS told the Committee that it wrote to A2DM on 28 July 2004 to request further information, including information relating to processing equipment, details of the 40 jobs that were claimed to be created by the project, competitive neutrality information relating to the processing plant at Malanda, development approvals for the processing plant, and the guarantee they would provide to farmers regarding the farm gate price. DOTARS received the additional information on 5 August 2004.⁷²

6.55 Mr Stewart told the Committee that DOTARS did not ask any questions about the referees for the project in A2DM's application.⁷³ The referees were listed as Mr Saddler, Mr Dick Schroder, owner of Cooloola Milk (A2DM's south east Queensland milk processing agent) and Mr Kevin Kelly, owner of Cooee Advertising. None of the referees was independent of A2DM.⁷⁴ The Committee also heard that A2DM did not have a written agreement regarding the A2 milk processing plant with Mungalli Dairy at the time the grant was applied for or announced.⁷⁵

6.56 Mr Stewart told the Committee that DOTARS had not asked any questions about A2DM's operations in southern Queensland, its inability to pay farmers or its supply problems. Mr Stewart's evidence was that it was not necessary for DOTARS to seek information about A2DM's current financial status, because the Atherton Tablelands A2 milk processing plant was to be an entirely separate operation:

I always believed that the operation up here in Cairns or in the tableland region was seen as a different operation so, with the financials and things, alarm bells did not go off—it was projections as well as a new identity that was commencing this.⁷⁶

6.57 The Committee believes A2DM's financial situation and operations in south east Queensland were highly relevant to the viability of the RPP project and should have been investigated by DOTARS. For example, the proponent was A2DM and the managers of the new company proposed to receive the funding, Star International Group, were to be the same as the directors of A2DM. The new company was also to use the same marketing strategy and produce the same product as A2DM's southern Qld operation. The fact that much of the proponent's contribution was to be in-kind management expertise also made the directors' record in running other companies relevant.

71 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 38.

72 Dr Dolman, *Committee Hansard*, 14 April 2005, pp 77-78.

73 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 44.

74 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 43.

75 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 78.

76 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 39.

6.58 As outlined above, FNQACC submitted its comments on the project to DOTARS on 26 August 2004, with an overall recommendation of 3 but with the caveats that the project was worthy of further research and that competitive neutrality issues in particular should be investigated before the project proceeded.⁷⁷ DOTARS witnesses told the Committee that the due diligence process was completed on 27 August 2004. This suggests that the ACC's recommendation was ignored.

'After the fact' due diligence

6.59 The Committee is concerned that in relation to this and other grants, proper due diligence checks were not carried out prior to grants being approved or announced. The 'due diligence' assessment carried out prior to the department making its recommendation to the minister appears to only be a compliance check, and meant that the department neglected to provide fundamental information to the decision maker about the viability of the project.

6.60 DOTARS appeared to suggest to the Committee that such neglect was appropriate. The rationale given was that no public funds had been expended because the actual funding of the project was conditional on a full due diligence assessment of the new company that was to be created to accept the grant.⁷⁸ For example, Mr Yuile told the Committee that:

...funding was conditional on the confirmation of cofunding, an independent viability assessment of the project and the establishment of the new company, Star International Group, which was partially owned by local dairy farmers. As committee members would be aware, the proponents of the application recently went into liquidation and, as the conditions attaching to the grant were not met, no grant moneys have or will be paid.⁷⁹

6.61 This 'after the fact' due diligence, by making funding subject to conditions to be met after the approval, has allowed applications to be expedited so that the political benefits of announcements can be achieved. This practice has damaging effects not only on the proponent, but also on project partners, the local industry and community. As discussed below, this is particularly relevant in this case where dairy farmers assumed that the announcement of project approval meant that the project would proceed.

6.62 The Committee was also concerned by evidence from Mrs O'Connor that suggested DOTARS was still undertaking investigation into the application on the day of the grant announcement—nine days after the application had been approved:

77 FNQACC TRAX comments on A2 Milk Processing project, 26 August 2004, in FNQACC minutes and recommendations, received 1 April 2005.

78 Dr Dolman, *Committee Hansard*, 14 April 2005, p 80-81.

79 Mr Yuile, *Committee Hansard*, 14 April 2005, pp 76-77.

My last contact with the department, when they were still asking relevant questions in the process of rigour and due diligence, was actually around midday on 8 September. The media alert went out that afternoon.⁸⁰

6.63 If the treatment of the A2DM application represents normal practice as claimed by DOTARS, the Committee is extremely concerned about the laxity of evaluation processes.

DOTARS lack of awareness of legal action

6.64 It is of concern to the Committee that funding was approved for a project where the proponent had legal action pending against it, particularly considering the action was being taken by a state government body. Mr Stewart told the Committee he never advised the department or the ACC that A2DM was the subject of legal action over misleading advertising and DOTARS never asked about the legal action.⁸¹

6.65 The Committee considers it highly inappropriate that Mr Stewart or the other A2DM directors did not advise DOTARS of the legal action, particularly given that it impacted on the viability of the media strategy on which the project's cash flow projections were based.⁸² The Committee is also concerned that the department's routine compliance checks did not reveal legal action pending against the proponent.⁸³

The offer of funding

6.66 The letter of 2 September 2004 from Parliamentary Secretary Kelly to Mr Stewart, advising A2DM that its application for RPP funding had been approved, is somewhat ambiguous in relation to the actual recipient of the funding. The letter is addressed to Mr Stewart as Director of A2DM and states:

I am pleased to advise you that I have approved partial funding under Regional Partnerships of \$1,268,300 (GST Inclusive) to the A2 Dairy Marketers Pty Ltd for your A2 Milk Processing project.⁸⁴

6.67 There is no mention of the other project partners - Mungalli Dairy and the several dairy farmers – other than to say that funding for the project had been approved subject to confirmation of additional cash support from A2DM and other

80 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 12.

81 Mr Stewart, *Committee Hansard*, 13 April 2005, pp 59 and 60.

82 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 60.

83 DOTARS became aware of the legal action against A2DM on 26 August 2004 – see Ms Riggs, correspondence, 22 June 2005.

84 Parliamentary Secretary Kelly, correspondence to Mr Stewart, 2 September 2004, in A2DM liquidator's documents, received 8 April 2005.

partners, and 'satisfactory resolution of company structure between Mungalli Dairy, yourself and individual dairy farmers'.⁸⁵

6.68 DOTARS witnesses explained this by saying the full conditions of the grant were outlined in a follow up letter on 24 September from DOTARS to Mr Stewart, and would have been outlined in the funding agreement.⁸⁶ The Committee suggests that the letter of offer may have more appropriately addressed to all project partners, indicating that their joint application had been approved subject to the satisfactory resolution of a company structure.⁸⁷

6.69 Given that A2DM was the proponent but a separate company was intended to be the grant recipient also raises the question of whether there was a breach of the RPP guidelines, which state that third parties seeking funding on behalf of others are not eligible to apply for funding.⁸⁸

Timing of the grant approval and announcement

6.70 DOTARS gave evidence that the A2DM application was approved by the parliamentary secretary on 29 August and announced on 8 September 2004. However, when Mrs O'Connor met with Minister Anderson and Senator Boswell on 3 September 2004 at a National Party dinner in Innisfail, she raised the issue of the A2DM grant to, in her own words, check:

That they look at the whole picture and that they address any of the weaknesses or concerns in the application or the environment around it very carefully...My whole aim in the discussion was saying, 'Are you are aware of it? Please be careful and please help us manage the impact.'⁸⁹

6.71 Mrs O'Connor told the Committee that Senator Boswell and Mr Anderson took note and said they would follow the issue up. The following week Mrs O'Connor received a call from a person claiming to be from Mr Anderson's office, who said that A2DM had not made an application for RPP funds.⁹⁰ Mrs O'Connor said:

Personally, I was aware of the application being in the system. Why else is DOTARS communicating with me regarding regional impacts and concerns? Why am I being involved in their due diligence in providing industry background if there is not an application? We are all obviously

85 Parliamentary Secretary Kelly, correspondence to Mr Stewart, 2 September 2004, in A2DM liquidator's documents, received 8 April 2005.

86 Dr Dolman, *Committee Hansard*, 14 April 2005, p. 82.

87 Senator O'Brien, *Committee Hansard*, 14 April 2005, p. 83.

88 DOTARS, *Submission 14*, Attachment D, Regional Partnerships Guidelines, p. 6.

89 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 10.

90 Mrs O'Connor, *Committee Hansard*, 13 April 2005, pp 10-11.

very disillusioned about that. The advice provided back to me, early in the week after 3 September, was that there was no application.⁹¹

6.72 This suggests that the grant was, in fact, approved *after* the election had been announced—during the caretaker period. If this is the case, it would be contrary to the government's guidance document on caretaker conventions, which counsel that the government avoids entering major contracts or undertakings, particularly those that require ministerial approval, during the period preceding an election.⁹² It would also contradict the department's evidence to the Committee.⁹³

The role of Mr Crooke

6.73 As noted previously, Mr Crooke arranged meetings between A2DM and members of the Queensland Government and the Australian Government. Mr Crooke also liaised with FNQACC and ATSRAC on A2DM's behalf. However, he later took a position as media adviser to the parliamentary secretary, giving rise to allegations of conflict of interest.

6.74 Mr Stewart described Mr Crooke's role as initially being to explain to members of the government: '...the story of A2, the benefits to Dairy Australia and those types of things'.⁹⁴ One of Mr Crooke's objectives, as set out in the Asia Pacific Corporation's *Proposal for A2 Corporation – Government and media relations strategy* signed by Mr Crooke and dated 18 February 2004, was:

... To explore the prospect for financial assistance from industry support schemes offered by State and Federal Governments e.g. Research and Development Grants; assistance under the Federal Government Sustainable Regions Programme.⁹⁵

6.75 Mr Stewart told the Committee that Mr Crooke organised and attended several meetings between A2DM and members of the Australian Government, including a meeting in early April 2004 with the Hon Warren Truss MP, then Minister for Agriculture, Fisheries and Forestry. Mr Stewart described the purpose of this meeting as being '...just to explain the way we were going to go about A2 and promote it. It was to advise the government out of courtesy'.⁹⁶

91 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 11.

92 Department of the Prime Minister and Cabinet, *Guidance on caretaker conventions*, July 2004, p. 4.

93 DOTARS, *Revised RPP tables*, received 11 May 2005, p. 24.

94 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 48.

95 Asia Pacific Corporation, *Proposal for A2 Corporation – Government and media relations strategy*, 18 February 2004, in A2DM liquidator's documents, received 8 April 2005.

96 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 49.

6.76 As discussed earlier in the chapter, Mr Stewart, Mr Roberts and Mr Crooke met with the parliamentary secretary in her Brisbane electorate office on 11 June 2004. The meeting was organised by Mr Crooke. Mr Stewart said that Mr Crooke advised him approximately three weeks after the 11 June meeting that he was going to work for Parliamentary Secretary Kelly as her media adviser.⁹⁷

6.77 Concerns have been raised in other forums because Mr Crooke was not asked to provide a written statement of personal interests or a declaration of conflict of interest form when commencing employment on the parliamentary secretary's staff. However these matters were not pursued in evidence to this Committee. The parliamentary secretary also faced allegations in the House of Representatives on 2 December 2004 of conflict of interest and breaching the Ministerial Code of Conduct by approving a grant for a company that had employed a member of her staff as a political lobbyist.⁹⁸ Indeed, the Prime Minister acknowledged in the House of Representatives that Parliamentary Secretary Kelly did breach the Ministerial Code of Conduct.⁹⁹

6.78 The Committee is unable to make an assessment of the conflict of interest allegations on the evidence before it. However, it would be highly inappropriate had Mr Crooke continued his involvement with the proponents after he became an adviser to the parliamentary secretary.

Impact of the A2DM grant announcement

6.79 The announcement of the \$1.27 million dollar grant to A2DM and its subsequent withdrawal had a negative impact on the already fragile Atherton Tablelands dairy industry. Following sustained drought and the deregulation of the dairy industry in 2004, the Atherton Tablelands dairy industry was in a tenuous position. It had one major processor, which bought the majority of milk from the estimated 105 local dairy suppliers.¹⁰⁰ One submission to the inquiry said:

No doubt you are now well aware of the hardship & stress experienced by dairy farmers & their families with the advent of deregulation and the subsequent price wars between processors resulting in unsustainable farm gate milk prices & greater profits for the processors & retailers, more particularly, the main super markets, so it is not surprising that a number of Atherton Tableland dairy farmers strongly supported the concept of another processor coming into play especially as they were being offered 40c—50c / litre...¹⁰¹

97 Mr Stewart, *Committee Hansard*, 13 April 2005, p. 58.

98 *House of Representatives Hansard*, 2 December 2004, pp 75-87.

99 The Hon John Howard MP, Prime Minister, *House of Representatives Hansard*, 9 December 2004, pp 80-81.

100 Mrs O'Connor, *Committee Hansard*, 13 April 2005, pp 15-16.

101 Mr Bell, *Submission 41*, p. 1.

6.80 The announcement of the grant with its implication of government support for the project had instilled confidence in local farmers that the project was viable and would go ahead. This encouraged a number of farmers to invest in testing their herds for, or purchasing, A2 cows. Several more spent time and money adjusting their business plans towards producing A2 milk.¹⁰² Mrs O'Connor articulated the influence perceived government support can have on business decisions:

I assume, perhaps wrongly, that, when strong government support is being provided to a project, or is perceived to be being provided to a project, farmers may be less careful than perhaps they otherwise would be.¹⁰³

6.81 This led to an inflated market price for A2 cows, which sold for approximately \$400-\$500 more than their usual price. Mr Strazzeri, a local dairy farmer for the past 32 years, told the Committee that, after attending an auction in May 2004 and seeing A2 tested cows sell for \$1,100 - \$1,200 that would normally be worth \$600-\$700, he and his son had paid a premium for A2 tested cows:

One fellow who had been tested—Mr John Jones—had his cows for sale...So we purchased 34 head of dairy cattle from him, which were A2 tested. I have all the proof here, with the numbers of the cows and so on.

Senator CARR—How much did they cost?

Mr Strazzeri—They cost \$1,000 each.

Senator McLUCAS—How would that compare with the going price of an A1 cow?

Mr Strazzeri—The same fellow sold the rest of them for \$600.

Senator McLUCAS—So you paid a premium of \$400?

Mr Strazzeri—I paid \$400 more than I should have.¹⁰⁴

6.82 The Committee received evidence about the effects of the grant withdrawal:

Some farmers spent considerable sums of money on the strength of the proposed grant. De-anne Kelly was adamant that the money was available and that we could confidently go ahead with our preparations for supplying A2 milk. One farmer went straight out and spent \$30,000 [p]urchasing A2 positive cows. These people should be compensated for the expense incurred on the strength of a political promise of funds that in hindsight were only ever intended to be used for political purposes.¹⁰⁵

6.83 In evidence to the Committee, Mrs O'Connor made a recommendation aimed at avoiding these market distorting effects by making it clear that the announcement of a grant does not necessarily mean that the grant will be awarded:

102 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 6.

103 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 6.

104 *Committee Hansard*, 13 April 2005, pp 87-88.

105 Mr Bell, *Submission 41*, p. 3.

Firstly, at the announcement of a grant, especially when it involves other stakeholders, it should be clearly stated that the announcement is only a step in the process. Further due diligence should continue and the project should not be a goer until contracts have been executed by both the applicant and the minister.¹⁰⁶

Conclusion

6.84 The Committee believes the government must consider delaying grant announcements until all conditions of the grant have been met in full. A2DM's application was received by DOTARS on 9 July 2004, FNQACC's advice was provided to DOTARS on 26 August, DOTARS provided advice to the parliamentary secretary on 27 August and the project was approved on 29 August. This stands in stark contrast to the many projects that remain unconsidered by DOTARS or the minister several months after an application has been received and recommendations passed on by the ACC.

6.85 The case of A2DM raises serious concerns about the administration of the Regional Partnerships Program. In particular, it exposes the risks inherent with fast-tracking applications and failing to heed an area consultative committee's warning that a project application required more investigation and development. The Committee is also extremely concerned that A2DM funding was approved and the announcement was made before proper probity and due diligence checks were undertaken.

6.86 The Committee believes that the government must accept responsibility for expressing support for projects that are ultimately doomed to fail, and the consequences that reach beyond the proponent throughout the local community and industry—even in cases where no public funding was expended.

6.87 The Committee is appalled that projects of questionable merit and sustainability are fast-tracked at the expense of regionally-worthy projects supported and developed by local ACCs, which are often rejected by the delegate with little explanation or simply stuck at the departmental or ministerial level for months.

106 Mrs O'Connor, *Committee Hansard*, 13 April 2005, p. 3.

