

The Senate

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Rural and Regional Affairs and  
Transport Legislation Committee

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Australian Wool Innovation Limited -  
Application and expenditure of funds  
advanced under Statutory Funding  
Agreement dated 31 December 2000

February 2004

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# EXECUTIVE SUMMARY

## Chapter 1: Conduct of the inquiry

The Committee adopted the inquiry following concerns about the management of AWI during 2001 and 2002; in particular, concerns that some AWI activities might be in breach of the Statutory Funding Agreement which controls how AWI applies Wool Levy Funds and Commonwealth Matching Funds (grants towards wool industry research and development).

## Chapter 2: The AWI Statutory Funding Agreement

The wool levy is compulsory, enforced by Commonwealth law. The money is handed over to AWI, a Corporations Law company. Accountability mechanisms are in place so that the Commonwealth can be satisfied that the company is using the money appropriately for the benefit of woolgrowers. The *Wool Services Privatisation Act 2000* provides that the Minister may enter a contract to pay AWI the wool levy and matching R&D funds; but before doing so the Minister must be satisfied that the contract includes adequate provisions to ensure that the money is spent in the allowed ways.

This contract is the AWI Statutory Funding Agreement (SFA). The agreement sets conditions on AWI's use of the Wool Levy Funds and the Commonwealth Matching Funds. It includes conditions on planning and reporting to allow oversight by AFFA. The key conditions are:

- Wool Levy Funds may only be used for specified activities, and only 'for the benefit of Australian woolgrowers'.
- Commonwealth Matching Funds may only be used for eligible wool industry research and development as defined in schedule 4 of the agreement.

## Chapter 3: AWI's structure and strategic plan

AWI was established as a subsidiary of Australian Wool Services, which was chaired by Mr Rod Price. Professor Vizard (a former AWI director) argued that this caused some confusion about which chair (AWS or AWI) was running the company.

The founding managing director of AWI, Mr Dorber, was appointed by Mr Price. There is no evidence on what executive search procedure led to this appointment, and it appears that the process was not transparent. The AWI Board was involved only to approve Mr Price's choice. In the Committee's view it would have been prudent for AFFA to take a greater interest in this appointment.

The strategic and operating plans mandated by the SFA were not finalised to AFFA's satisfaction until almost 18 months after AWI's establishment. It is unfortunate that it took so long. The Committee believes that in future agreements of this type AFFA should exert greater oversight over the strategic planning process. Arguably an unsatisfactory planning process would be an early warning of other possible problems which should lead AFFA to want closer oversight.

#### **Chapter 4: Concerns about AWI's management and corporate governance, 2001 and 2002**

From late 2001 WoolProducers (a growers representative body) became concerned about the direction of AWI. The main concerns were about project priorities; the board's skills and involvement in decision-making; and (in WoolProducers' view) inadequate performance measures and internal accountability controls. Professor Vizard, then an AWI director, had similar concerns.

AFFA gave evidence that at the time it regarded these concerns as matters of project priority or management style, which AWI should resolve internally, rather than breaches of the Statutory Funding Agreement. In the Committee's view some of the matters went beyond project priorities or management style, and should have been of concern to both the department and the minister.

A number of transactions in 2002, particularly in the second half of 2002, caused particular concern. They have been the subject of a 'forensic review' commissioned by the new (post November 2002) AWI Board. This review identified a significant number of unusual or poorly substantiated payments, payments which may be inconsistent with the SFA, and project management issues.

On the weight of evidence the Committee concludes that concerns about AWI management and corporate governance, especially in the second half of 2002, were completely justified. The examples, especially in the second half of 2002, show a pattern of behaviour in breach of good corporate governance standards.<sup>1</sup>

The Committee notes particularly that in the leadup to the October 2002 election of directors, AWI campaigned on behalf of sitting directors at company expense. In the Committee's view this was most improper. The Committee notes advice from the Australian Government Solicitor that it was probably a breach of the Corporations Act.<sup>2</sup>

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<sup>1</sup> Senator Cherry disagrees with this paragraph and has provided supplementary comments.

<sup>2</sup> Senator Cherry disagrees with this paragraph and has provided supplementary comments.

### **Recommendation 1 (paragraph 4.83)**

**The question whether AWI used company money to campaign for sitting directors during the 2002 Board election, in breach of Corporations Law, should be referred to the Australian Securities and Investments Commission.**

The Committee notes Mr Dorber's view that AWI may spend its independent income freely - including, for example, on agri-political activity. In the Committee's view a levy-funded body like AWI should not be allowed to spend *any* money, however sourced, on agri-political activity.

### **Recommendation 2 (paragraph 4.149)**

**The Statutory Funding Agreement should have a condition that all the company's expenditure (not only the expenditure of 'the Funds') should be controlled by the Statutory Funding Agreement.**

## **Chapter 5: AFFA's oversight of AWI in 2001 and 2002**

AFFA argued that complaints about AWI in the first half of 2002 were more about project priorities and management style than breaches of the SFA; and that project priorities and management style were a matter for AWI to resolve internally. AFFA argued that the more serious concerns raised in the second half of 2002 would in any case not have been revealed by auditing until the end of the 2002/03 financial year.

The Committee acknowledges AFFA's considerable efforts during 2001 to obtain a satisfactory AWI strategic plan. Nevertheless, it is unfortunate in retrospect that AFFA did not act more energetically on the particular concerns about AWI management which began to be raised from February 2002. It was not necessary to wait for a regular audit. AFFA, if it reasonably believed there might be a breach of the SFA, had the right to demand an additional audit report or opinion at any time at AWI's expense.

The Committee believes that AFFA failed to properly pursue the issue of AWI's understanding of and compliance with the SFA given the fundamental difference between AFFA and the AWI Managing Director as to what the company's accountability obligations actually were.

### **Recommendation 3 (paragraph 5.36)**

**The Minister should direct AFFA to pursue compliance and other reports pursuant to all Statutory Funding Agreements.**

The Committee notes the need for orderly risk management in AFFA's oversight of bodies like AWI. If problems occur there should be protocols so that the level of supervision can be increased in a timely way which, at each stage, balances the risk involved, the administrative workload which supervision implies for AFFA, and the policy goal of allowing the company to manage its affairs with reasonable autonomy.

The Committee comments on the argument, which Mr Dorber put at the time, that ‘the direct accountability of AWI [is] to its shareholders.’ This argument cannot be used as an excuse for failure to comply with the SFA. The SFA is a contract. If AWI fears that the contract is not in the company’s best interests, it does not have to sign it. By signing, AWI asserts that the net effect of the contractual rights and obligations (which include the accountability obligations) *is* in the company’s best interests.

The Committee disagrees with the suggestion by Mr Taylor, secretary of AFFA, that ‘ASIC is the appropriate body if you have any concerns in terms of governance for a Corporations Law company’. This is not an adequate response. AWI’s shareholders have a dual role: they are shareholders protected by the Corporations Law like any other shareholders; but they also, through the levy, provide their company’s income. Because the levy, by government policy, is compulsory, there is a separate duty on government to ensure that the money is used not only legally in the Corporations Law sense, but also prudently for the benefit of levy payers. That duty lies with AFFA.

## **Chapter 6: AWI and AFFA responses since November 2002**

AWI submitted that since the election of the new Board in November 2002 AWI and the Commonwealth ‘have worked, and continue to work, closely and cooperatively to ensure that the company complies with its obligations in the SFA.’

The new Board commissioned a ‘forensic review’ into AWI expenditure in 2001 and 2002. AFFA has obtained advice from the Australian Government Solicitor on possible breaches of the SFA or the Corporations Act, and is considering its possible responses.

In the last year AWI has also obtained a report on compliance with the SFA for the 2002/2003 year; and a Review of Performance which, under the SFA, must be available to shareholders before a Wool Poll.

AFFA advised that it is renegotiating the SFA with a view to strengthening accountability and reporting arrangements. AWI said it accepts this ‘without reservation’.

### **Recommendation 4 (paragraph 6.18)**

**The Minister should give consideration to referring any breaches of the Corporations Act by AWI to the Australian Securities and Investments Commission.**

### **Recommendation 5 (paragraph 6.18)**

**Prior to a new SFA being agreed with AWI the Minister should review the effectiveness of remedies for breaches of the agreement currently available through the *Wool Services Privatisation Act 2000*.**

## **Chapter 7: Comments on the statutory funding agreement model**

The chapter summarises relevant discussion in AFFA's 2002 *Review of the Corporate Governance of AFFA Portfolio Agencies*. The committee agrees with its recommendations on AFFA's oversight of bodies like AWI.

The Committee particularly notes and approves the review's implication that AFFA's oversight should not be limited to SFA compliance viewed narrowly. It should consider:

- whether the body is achieving its public interest purpose;
- whether it is obtaining value for money; and
- whether its internal corporate governance is satisfactory.

Arguably the special position of a body such as AWI implies standards of corporate governance additional to those implied by the Corporations Act. The Committee suggests that statutory funding agreements should reflect these special requirements. The Committee notes the ASX Corporate Governance Council's *Principles of Good Corporate Governance and Best Practice Recommendations*. (March 2003). The Committee suggests that AFFA should consider incorporating these into accountability conditions of agreements as relevant.

The Committee makes some suggestions for the provisions of statutory funding agreements. The Committee notes that the SFA prohibits 'agri-political activity' as defined; but the Australian Government Solicitor doubted whether the definition included 'internal' activity of the sort which AWI indulged in before the 2002 Board election (as opposed to the 'external' activities of trying to influence government or public opinion). In the Committee's view the definition of 'agri-political activity' should be amended to clarify that it includes internal as well as external political activity.

### **Recommendation 6 (paragraph 7.16)**

**The definition of 'agri-political activity' should be amended to explicitly include internal as well as external political activity.**

### **Recommendation 7 (paragraph 7.19)**

**The SFA should incorporate a requirement mandating that expenditure be consistent with the strategic plan, the operational plan and the R&D Guidelines.**

### **Recommendation 8 (paragraph 7.28)**

**The Minister should give consideration to incorporating conditions in existing and future Statutory Funding Agreements as suggested by recommendations 2, 6, 7 and other relevant suggestions in this report.**



# CHAPTER ONE

## Conduct of the Inquiry

### Background

1.1 During consideration of 2003-04 Budget Estimates of the Department of Agriculture, Fisheries and Forestry (AFFA) in May 2003, the Committee raised concerns about the administration of Australian Wool Innovation Limited (AWI), and AWI's compliance with its Statutory Funding Agreement with the Commonwealth.<sup>1</sup> The Statutory Funding Agreement sets conditions under which AWI receives Wool Levy Funds and Commonwealth Matching Funds towards wool industry research and development and certain other activities for the benefit of woolgrowers (more details are in chapter 2). The concerns related mostly to the period between the creation of AWI as a Corporations Law company on 1 January 2001 and the election of a new Board on 31 October 2002.

1.2 During the Budget Estimates hearing the Committee could not question AFFA officials about an April 2003 'forensic review' of AWI's financial operations by PricewaterhouseCoopers, since it was confidential at the time.<sup>2</sup> In order to pursue this and other matters at more length, on 26 May 2003 the Committee resolved to inquire into:

- (a) the administration and operation of the Statutory Funding Agreement dated 28 December 2000, between the Commonwealth of Australia (represented by the Minister for Agriculture, Fisheries and Forestry), Australian Wool Innovation Pty Limited and Australian Wool Services Limited;<sup>3</sup>
- (b) the expenditure and application of funds paid to Australian Wool Innovation Pty Limited under the terms of that agreement; and
- (c) other relevant matters arising from the reference.

1.3 The Committee adopted the inquiry of its own motion under Senate Standing Order 25(2)(b), which allows legislation committees to inquire into the performance of the departments allocated to them.

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1 Senate Rural and Regional Affairs and Transport Legislation Committee: consideration of Budget Estimates, *Committee Hansard*, 26 May 2003, p.9ff.

2 PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003

3 The correct date of the Statutory Funding Agreement is 31 December 2001. AWI was created as a subsidiary of Australian Wool Services on 1 January 2001. It became a public company limited by shares when demerged from AWS on 1 May 2002.

## Conduct of the inquiry

1.4 The Committee advertised the inquiry in *The Australian* and wrote to a number of key stakeholders inviting submissions. The Committee received and made public 18 submissions (see Appendix 1). The Committee also ordered AWI to provide the PricewaterhouseCoopers April 2003 forensic review mentioned at paragraph 1.2. After considering the review the Committee decided it was in the public interest to make it public. Its findings are mentioned further in chapter 4.

1.5 The Committee held four public hearings (see Appendix 2), and heard evidence from AFFA, AWI, WoolProducers (a woolgrowers' peak interest group), Mr Colin Dorber (former AWI Managing Director) and Associate Professor Andrew Vizard (a former AWI Board member). Mr Dorber appeared once before the Committee and made three written submissions. Ms Maree McCaskill (former Chair of the AWI Board) made a written submission on behalf of herself and three other former Board members. The Committee twice invited Ms McCaskill to give evidence but on each occasion she advised that she was unable to attend on the day proposed. This was despite early statements reported in the media that Ms McCaskill was happy to defend the old board's actions in any forum.<sup>4</sup>

1.6 Submissions and transcripts of the hearings are available at the parliament's website ([www.aph.gov.au](http://www.aph.gov.au)).

## Focus of the report

1.7 The focus of the report is accountability in public administration. Is the statutory funding agreement model suitable for ensuring proper accountability when compulsory levies are handed over to a Corporations Law company? Were concerns about the corporate governance of AWI justified? Did AFFA oversee AWI adequately during its controversial first two years? What improvements can be suggested for the future?

1.8 The report is not about how much the Wool Levy should be, or what the direction of wool industry research and development should be, or whether AWI is carrying out the recommendations of the Future Directions report adequately.<sup>5</sup>

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4 ABC Country Hour Western Australia, 6 June 2003.

5 'The Future Directions report' = The Wool Taskforce [Chairman: the Hon I. McLachlan AO], *Diversity and Innovation for Australian Wool*, July 1999.



# CHAPTER TWO

## The AWI Statutory Funding Agreement

### Background

2.1 Compulsory levies or taxes have been exacted from woolgrowers since 1936-37 to fund research and development (R&D) and promotion. In more recent years successive Commonwealth governments have contributed a matching R&D funding to rural R&D corporations, up to 0.5 per cent of the gross value of production.

2.2 From 1994 to 2000 the wool tax and matching R&D funding was directed to the Australian Wool Research and Promotion Organisation (AWRAP), a statutory authority created by the *Australian Wool Research and Promotion Organisation Act 1993*. In 1999, following industry dissatisfaction with the performance of AWRAP, a 'Future Directions Taskforce' report recommended that AWRAP should be replaced with a Corporations Law company limited by shares owned by woolgrowers. On 8 August 2000 the Commonwealth announced that AWRAP would be privatised in the way suggested, and would have two subsidiaries: one to take over the commercial development of the Woolmark, and the other to manage research and development using the proceeds of the wool levy. The aim of the new structure was to 'reduce government involvement in industry affairs and provide levy payers with a greater say in their industry's future.'<sup>1</sup>

2.3 The privatisation was effected by the *Wool Services Privatisation Act 2000* (the Privatisation Act). On 1 January 2001 AWRAP became Australian Wool Services Ltd (AWS), a public company limited by shares owned by woolgrowers. Its subsidiaries were TWC Holdings Pty Ltd for commercial development of the Woolmark and Australian Wool Innovation Ltd (AWI) for research and development. On 30 April 2002 AWI demerged from AWS and since 1 May 2002 it has operated as an independent company.

2.4 The wool tax, which had been collected by the Australian Taxation Office and remitted to AWRAP, was replaced with a wool levy collected by AFFA and remitted to AWI. The wool levy is 2 per cent of the gross value of production. AWI shareholders (who number about 37,000) have voting rights in proportion to the Wool

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1 The Hon. Warren Truss, *New Wool Industry arrangements announced*, Press Release, 8 August 2000.

Levy they pay.<sup>2</sup> Additionally, the Commonwealth provides matching contributions for eligible R&D expenditure by AWI.

2.5 The Committee has previously reported on the legislative changes that gave rise to the establishment of AWI.<sup>3</sup>

2.6 The Wool Levy is compulsory, enforced by Commonwealth law. The Commonwealth gives the money to AWI, a Corporations Law company. Accountability mechanisms are in place so that the Commonwealth can be satisfied that the company is using the money appropriately. As AFFA put it: 'AFFA is accountable, through the Minister, to the Parliament for expenditure of monies appropriated by Parliament.'<sup>4</sup> The Privatisation Act provides that the Minister may enter a contract to pay AWI the wool levy and matching R&D funds; but before doing so the Minister must be satisfied that the contract includes adequate provisions to ensure that the money is spent in the allowed ways.<sup>4</sup>

2.7 This contract is the Statutory Funding Agreement (SFA).<sup>5</sup> The agreement sets conditions on AWI's use of the Wool Levy Funds and the Commonwealth Matching Funds. It includes conditions on planning and reporting to allow oversight by AFFA. It was made between the Commonwealth, AWI and AWS on 31 December 2000. It was to operate for three years. It has been temporarily extended so that negotiations over a new agreement can include consideration of the findings of this report.

2.8 Nothing stops AWI from earning income from other sources, and this other income is not subject to the accountability controls of the SFA.<sup>6</sup> In 2002-2003 AWI's

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2 AWRAP, *Statements of Financial Performance for the six months ended 31 December 2000*, p.46. The Wool Taskforce [Chairman: the Hon I. McLachlan AO], *Diversity and Innovation for Australian Wool*, July 1999, p.99. Wool Services Privatisation Bill 2000, explanatory memorandum, p.2. Hon. Warren Truss, *New Wool Industry Arrangements Announced*, press release 8 August 2000; *Australian Wool Services Launched*, press release 19 December 2000. Submission 13, AWI, p.10. AWI Constitution, clause 5.3.

3 Senate Rural and Regional Affairs and Transport Legislation Committee, *Report on Australian Wool Research and Promotion Amendment (Funding and Wool Tax) Bill 2000*, June 2000; *Report on Wool Services Privatisation Bill 2000*, October 2000.

4 *Wool Services Privatisation Act 2000*, s31.

5 Department of Agriculture, Fisheries and Forestry, *Statutory Funding Agreement between the Commonwealth of Australia, Australian Wool Innovation Pty Limited and Australian Wool Services Limited*, 31 December 2000.

6 AWI's constitution has an objects clause listing activities of similar tenor to the eligible activities listed in clause 5 of the SFA; and the activities must 'in each case be for the benefit of Australian woolgrowers'. However this is advisory, not mandatory: an act of the company is not invalid merely because it is contrary to or beyond the objects: *Corporations Act 2001*, s125.

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revenue was \$60 million from levies, \$16 million from the Commonwealth, and \$5 million from interest and royalties.<sup>7</sup>

2.9 Research and development and promotion done in this way, through a contract between the Commonwealth and a Corporations Law company owned by producers or levy payers, is a significant part of current agricultural R&D. In 2002-2003 there were five companies of this type: they received about \$122.4 million in industry levies for research and development and \$76 million in Commonwealth matching funds for research and development.<sup>8</sup> Overseeing these companies is an important administrative responsibility of AFFA.

### **General provisions of the Statutory Funding Agreement**

2.10 The main provisions of the Statutory Funding Agreement relevant to the inquiry are:

2.11 Clause 3.1: the Commonwealth must pay AWI Wool Levy Funds ('Category A Funds') and Commonwealth Matching Funds ('Category B Funds'). The Commonwealth Matching Funds are a grant towards eligible research and development: they are paid in arrears and may not exceed 0.5 per cent of the gross value of eligible wool. The two categories together are 'the Funds' as noted below.

2.12 Clause 4: AWI must establish accounting systems, procedures and controls to ensure that the Funds are spent only in accordance with the SFA; that dealings with the Funds are properly authorised and accounted for; and that an auditor is able to readily verify that the Funds have been used only in accordance with the agreement.

2.13 Clause 5.1: AWI may apply Wool Levy (Category A) Funds only to certain activities. These are listed in Appendix 5 of this report. All activities must be 'for the benefit of Australian woolgrowers'. They include:

- R&D activities (clause 5.1(b)) and managing intellectual property arising from R&D activities (clause 5.1(e));
- 'providing wool industry services not otherwise widely commercially available to woolgrowers' (clause 5.1(f)); and
- various administrative activities including remunerating directors, employees and consultants.

2.14 Clause 5.2: Commonwealth Matching Funds are provided to reimburse AWI for expenditure on eligible wool industry R&D 'for the benefit of Australian woolgrowers

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7 Australian Wool Innovation Ltd, Annual Report 2002-2003, p.4.

8 AFFA, additional information, 23 December 2003.

and the Australian community generally’, as defined in schedule 4 of the SFA (see Appendix 6 of this report).

2.15 The slightly different, though overlapping, conditions of use for the Wool Levy Funds and the Commonwealth Matching Funds reflect the fact that the Wool Levy is paid by woolgrowers and should be applied for the benefit of woolgrowers, while the Commonwealth Matching Funds are a grant from the public treasury specifically to fund research and development.

2.16 Clause 5.3: In determining how to spend the Funds AWI must have regard to the Company’s strategic plan and operations plan (these plans are mandated by other clauses of the agreement, noted below); the Government’s R&D priorities as communicated by the Minister from time to time; and the ‘Levy Principles and Guidelines’ issued by AFFA. Generally under clause 5.3, AWI must apply the Funds in a manner that is ‘...efficient, effective and ethical’.

2.17 The AFFA ‘Levy Principles and Guidelines’ are copied as Schedule 2 of the SFA. They mostly deal with rules for proposing new or changed levies. However there are some points relevant or implicitly relevant to the expenditure of levy money. For example, ‘Statutory levies are not to be used to fund agri-political activities’; ‘The proposed levy must relate to a function for which there is significant market failure’; and ‘The body managing expenditure of levy monies must be accountable to levy payers and to the Commonwealth’.

2.18 Clause 5.5: AWI may not spend any of the Funds on grants or financial assistance to a body that represents wool growers.

2.19 Clause 5.6: AWI may not spend any of the Funds on on ‘agri-political activity’. This is defined as:

‘political campaigning or funding, developing, designing, resourcing or participating in activities intended to exert political rather than advisory influence on government policies or in activities intended to exert political influence on public opinion.’

2.20 Clause 6.1: This gives conditions under which the Commonwealth may suspend or reduce payments if AWI breaches the agreement, among other reasons.

### **Provisions on planning, reporting, and audit**

2.21 Clause 16: AWI must give the Commonwealth a strategic plan which covers issues such as

- the objectives and priorities of the company;
- a corporate governance statement outlining the directors’ responsibilities in terms of planning;
- proposed outcomes and performance indicators; and

- 
- broad resource allocation for the life of the plan.

2.22 Clause 17: AWI must give the Commonwealth each year an operating plan which shows intended operations, R&D programs to be undertaken, and budgets.

2.23 The SFA does not give the Commonwealth the power to direct the contents of the plans or to veto them. However AFFA advised that it was consulted by AWI during the development of the plans (see chapter 3).

2.24 Clauses 18 and 19: AWI must give the Commonwealth a copy of its annual report and other reports relating to the expenditure of the Funds that the Commonwealth requires from time to time.

2.25 Clause 20: Before a Poll AWI must undertake a performance review and have it externally audited, and make the review and the audit available to the Commonwealth and to levy-payers. (A 'Poll' is a three-yearly poll of wool levy payers, mandated by the Privatisation Act, for the purpose of recommending to the Minister what the rate of wool levy should be.)

2.26 Clause 21: The Commonwealth, if it reasonably believes that AWI may be in breach of the agreement, may examine company records and question staff.

2.27 Clause 22: AWI must give the Commonwealth a copy of its audited financial reports at the same time it is required to give it to shareholders. Clause 22.2 contains an additional requirement that 'the auditor audit and report on the Company's compliance with its obligations under this Agreement in relation to the Funds.' A matter of comment in this inquiry was that AWI did not provide the clause 22.2 audit for the years ending 30 June 2001 and 30 June 2002.

2.28 Clause 22.3 allows the Commonwealth at any time to request an additional audit report or opinion on any matter relevant to compliance with the agreement if the Commonwealth suspects a breach.

### **Relationship with Corporations Law**

2.29 The controls of the SFA are additional to those which apply to AWI by virtue of the *Corporations Act 2001*. The Corporations Act sets out the minimum standards expected of directors and officers of corporations. The following points summarise the duties of a director:

- Directors must act at all times in good faith in the best interests of the company. This requires that directors give proper consideration to whether a course of action is in the interests of the company and must honestly believe that it is in the company's best interests.
- Directors must avoid conflicts of interest by putting the interests of the company before their own personal interests.

- Directors must disclose to the board any personal interests which they have that relate, or may relate, to the affairs of the company or to any matter to be considered by the company.
- Directors must act with a high degree of care, skill and diligence in their role as a director of the company.
- Directors must exercise their powers only for the purposes for which they were conferred under the constitution of the company and not for any collateral or ulterior purpose.
- Directors must not improperly use their position or any information obtained through their position to gain any advantage for themselves or someone else or to cause any detriment to the company.
- Directors must ensure that the company does not enter any transactions with a party that is a ‘related party’ within the meaning of the Corporations Act without first obtaining approval of the members of the company. A ‘related party’ of a company includes the directors, their spouses and certain relatives.
- Directors must not engage in any conduct that may result in the concealment, destruction or falsification of any books or records of the company.
- Directors must not allow the making of any statement in a document required to be prepared under the Corporations Act that is false or misleading in a material particular.<sup>9</sup>

### **Comment**

2.30 A number of AWI activities in the calendar years 2001 and 2002 were queried, either at the time or subsequently, as likely breaches of the SFA. These are dealt with in chapter 4. Most of the concerns were over whether they were eligible activities within the terms of clause 5 (Wool Levy Funds) or Schedule 4 (Commonwealth Matching Funds).

2.31 Recommendations on how this and similar agreements might be improved, in light of AWI’s experience, are in chapter 7.

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9 AFFA, additional information 29 August 2003, AGS advice to AFFA 5 August 2003, p.4-5.

# CHAPTER THREE

## AWI's structure and strategic plan

3.1 The committee considered key questions concerning the relationship between AWI and AWS, the appointment of the AWI managing director, and the development of the strategic plan required by the Statutory Funding Agreement.

### AWI established as a subsidiary of AWS

3.2 AWI and The Woolmark Company (TWC) were established on 1 January 2001 as subsidiaries of Australian Wool Services (AWS). AWS was chaired by Mr Rodney Price and AWI by Ms Maree McCaskill. Directors of AWI were initially appointed by Mr Price, and 'ratified by the AWS Board'.<sup>1</sup> The *Wool Services Privatisation Act 2000* contemplated the demerger of AWS and AWI, and the demerger was completed on 30 April 2002. Before demerger all non-executive directors of TWC and AWI were also directors of AWS. Ms McCaskill explained:

A major recommendation from the Task Force Report not accepted, was the company structure. Instead, the Commonwealth sensibly proposed a holding company with two subsidiaries that would in a short time de-merge and stand-alone... Until April 2002, AWI and TWC were subsidiaries of Australian Wool Services (AWS), chaired by Mr Rodney Price. Under Australian corporate law, all non-executive directors of TWC and AWI were also directors of AWS. "A" Class Directors were on the boards of AWS and AWI and "B" Class directors were on the boards of AWS and TWC. In practical terms this meant AWI and TWC were under the complete scrutiny and control of AWS. The AWI Board regularly provided reports and updates on the performance of the company to Mr Price and the [AWS] Board.<sup>2</sup>

3.3 Former AWI director Professor Andrew Vizard argued that the establishment of AWI as a subsidiary of AWS resulted in some 'confusion about which chair was running the company':

In my view, the proper board for running the company clearly was the AWI board. I was concerned in the first several months of AWI's formation that there seemed to be confusion about which chair was running the company. At various times, at various board meetings, I would be asking Mr Dorber, 'Under whose instructions are you doing that?' and it would perhaps be under Mr Price's instructions that such and such had occurred. I made it quite clear that my position was that the chair of AWI, Ms McCaskill, should be responsible for Mr Dorber—that view was supported, I think, by

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1 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.3.

2 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.1.

all directors—and that, if there were any conversations that had to be had between AWS and AWI, they would best be performed through a chair-to-chair relationship rather than from the managing director through to the AWS chair. That, as a principle, was agreed. I also remember that this was still an ongoing issue for me as late as September 2001.<sup>3</sup>

### **The AWI Constitution: difficulty of nomination to the Board**

3.4 The AWI constitution was developed in late 2000 by consultation between AFFA, AWRAP, a Woolgrowers Advisory Group nominated by the industry to represent growers in the transition to the privatised structure, and the ‘Interim Advisory Board’, appointed by the Minister in May 2000, which became the founding Board of AWS.<sup>4</sup>

3.5 An element of the Constitution which became controversial during the leadup to the October 2002 Board election was the prerequisites for standing for election as a director. To be eligible to contest the election by right, a candidate had to be nominated by 5 per cent of shareholders - which, according to AWI at the time, required 1,830 signatures. WoolProducers commented that ‘the general convention for a Corporations Law company is no more than 100 shareholder signatures to nominate.’<sup>5</sup> The Board could accept nominations without these signatures but, though asked, did not do so.

3.6 The Minister for Agriculture, Fisheries and Forestry, the Hon Warren Truss, was quoted in *The Land* (19 September 2002), as saying:

At the time the new structure was put in place a deliberate decision was made by the industry to make it hard for challengers to overthrow the incumbent board because there was a perception the industry was suffering an inability to attract quality directors due to almost annual coups.<sup>6</sup>

3.7 WoolProducers argued before this inquiry that the AWI constitution was ‘unhealthily defensive...’

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3 Prof. A. Vizard, *Committee Hansard*, 28 August 2003, p. 67.

4 Mr P. Sutton (AFFA), evidence to Senate RRAT Legislation Committee inquiry into Wool Services Privatisation Bill 2000, 8 September 2000, p.5. Hon. W. Truss, Minister for Agriculture, Fisheries and Forestry, *Truss announces next stage in wool reform process*, media release 1 May 2000.

5 Submission 1, WoolProducers, p.34.

6 Submission 1, WoolProducers, p.36. Mr Truss shortly afterwards issued a statement to correct any impression that his words indicated support for the sitting Directors. *Australian Wool Innovation Board election process*, media release 24 September 2002.



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...It actively militates against shareholders simply and easily nominating candidates not to be on the board but merely to be on the ballot paper.<sup>7</sup>

3.8 Others argued that the system worked: when concerns about AWI management arose, the complainants were able to obtain a change in the board through the democratic process: at the election of 31 October 2002 five of the six directors facing election were replaced. Professor Vizard said:

In a most difficult period the integrity of the system has come through. In that process there is often a little bit of serendipity involved, and perhaps there was here as well. Within a very short period—and remember this company was formed only two years ago—we have virtually a completely new board, a new CEO and a new CFO. The system was able to recognise that something was wrong and completely change it within quite a short period of time. Personally, I would think that that is quite a positive for the current system rather than a negative.<sup>8</sup>

3.9 AFFA also stressed that disagreement about management priorities within AWI ‘is an appropriate thing to be resolved, *as it ultimately was*, at the election process.’ (emphasis added)<sup>9</sup>

3.10 WoolProducers gave evidence that:

WoolProducers... were able to overcome for shareholders this very difficult and obstructive process by obtaining in excess of 12,000 signatures to ensure that all growers had a choice at the 2002 election. The cost to woolgrowers and their representative organisations to do this is estimated at about \$45,000.<sup>10</sup>

3.11 WoolProducers argued that the ability to achieve change in this way was ‘a very near thing’:

**Mr Campbell**—... the structure that was suggested has actually worked. It was a very near thing though because of the defensive nature of the constitution that was given to AWI. If we had not been able to raise a lot of signatures, the necessary changes may not have been made.

**Senator O’BRIEN**—Was that an accident? You are alleging that there was a potential for the problems of AWI, as you see them, to have been insoluble but for the existence for your organisation.

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7 Mr S. Campbell (WoolProducers), *Committee Hansard*, 28 August 2003, p.55.

8 Prof. A. Vizard, *Committee Hansard*, 28 August 2003, p.80

9 Mr M. Taylor (AFFA), *Committee Hansard*, 17 September 2003, p.114.

10 Submission 1, WoolProducers, p.35

**Mr Campbell**—I think that is correct.<sup>11</sup>

***Comment***

3.12 The Committee agrees with WoolProducers that the 5 per cent requirement for nomination to the Board was too onerous. It was fortuitous that there was a growers' organisation like WoolProducers with the resources needed to pursue change within the system.

3.13 The Committee notes that for the 2003 election the board, at its discretion, required only 100 nominators, and at the annual general meeting on 21 November 2003 the AWI constitution was amended to entrench this.

**Appointment of AWI's Managing Director**

3.14 The Committee heard evidence of concerns about the appointment in early 2001 of AWI's founding Managing Director, Mr Colin Dorber.

3.15 Professor Vizard described his recollection of the appointment:

...this appointment was formally confirmed at an AWI board meeting of 30 January 2001... That was the first time I had heard Mr Dorber's name... During the phone board meeting, following a brief overview of the nature of the contract that had been signed by Mr Dorber and AWI, the chair put a resolution to the effect that Mr Colin Dorber be appointed as managing director. I remember that I stated that I was in no position to ratify such an important decision since all I knew about the candidate so far was his name. In particular, I remember I stated that I would need to have, at the minimum, a copy of Mr Dorber's CV and an overview of the appointment process before being able to ratify that decision. I also voiced my opinion that since nested in this decision was an implicit agreement that the company was to move to Sydney from Melbourne—with consequent loss of staff and increase in costs—this also required proper and full assessment before ratification.

After some further discussion, it was agreed that the board would be supplied with a copy of Mr Dorber's CV and that this was to be circulated immediately along with a signed letter of employment. Despite my position that there was insufficient information to pass such a resolution, the resolution was put to the vote and passed. Mr Dorber's CV and the letter of appointment were provided to me by AWS the following day. At the next AWI board meeting of 16 February 2001, Mr Dorber's appointment was discussed further. The board resolved as follows—and since there has been some other possibly conflicting evidence, I will read out the exact resolution as recorded in the minutes of that meeting:

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11 Mr S. Campbell (WoolProducers), *Committee Hansard*, 28 August 2003, p.43.

*Mr Rodney Price, Chairman of AWS Ltd is to be asked to prepare a one-page summary concerning the process adopted leading to the appointment of the Managing Director. The board indicated that information concerning the process (not the selection of the ultimate appointee) was sought. This was as a consequence of direct representations to a number of Directors by 'stakeholders'. Action: Chair—ASAP.*

That summary was never tabled whilst I was a director. So, to answer your question, I am not privy to how Mr Price selected that process because that piece of information was never tabled, despite being asked for by the board.<sup>12</sup>

3.16 The submission of four former AWI directors said that Mr Dorber 'was recruited through an executive search process conducted by Mr Price...'

I do not have any reason to doubt the competence of Mr Price or his extensive high—level corporate experience and ability to search and select an appropriate Managing Director... Directors Vizard, Patten and Murphy wished to be advised on the process for the appointment of the Managing Director. Mr Price described it in detail during the first meeting in February 2001.<sup>13</sup>

3.17 AFFA explained that it was not involved in Mr Dorber's appointment:

**Senator FERRIS**—Would the department have had any interest in the skill base of Mr Dorber or the process under which he was appointed—for example, in any executive search that might have taken place? Did the department in any way have any involvement in the appointment of Mr Dorber?

**Mr Mortimer**—I am not aware that the department was involved; indeed, I would expect that the department was not involved. Essentially the board of the company made that decision. Generally speaking, boards of corporations do not seek the advice of the department on these appointments.<sup>14</sup>

3.18 Mr Dorber said he was not privy to the details of the selection process conducted by Mr Price:

**Senator FERRIS**—How was it [your appointment] approved at the AWS board?

**Mr Dorber**—I do not know; I was not a member of that board... The only meeting I was present at was a board meeting of AWI Ltd when directors

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12 Prof. Andrew Vizard, *Committee Hansard*, 28 August 2003, pp.58-9.

13 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.1.

14 Mr D. Mortimer (AFFA), *Committee Hansard*, 23 June 2003, p.11.

Vizard and Patten demanded an explanation as to how I had been appointed. I said, ‘Go and ask Mr Price. How would I know?’<sup>15</sup>

### 3.19 WoolProducers criticised the method of appointment:

There is absolutely no public evidence that, prior to the appointment of the former CEO, the former board of AWI ever identified the skills required for that position, used this list of skills to conduct the widest possible national and international search or that the board interviewed or canvassed any range of candidates for the position.

It is an absolutely fundamental activity of any business group to write a strategic plan and then find a CEO who culturally, intellectually and competently is able to reflect the business direction of the company. If these processes did not occur, it is a major failure in corporate governance by the former board.<sup>16</sup>

### ***Comment***

3.20 No evidence was offered on the details of the executive search process which resulted in the appointment of Mr Dorber. The Committee notes the uncontradicted evidence of Professor Vizard that the Board never received the details it requested. The Committee shares the concern of WoolProducers that, on the face of it, it does not seem that it was a transparent process.

3.21 In respect of AFFA’s ‘hands-off’ approach in respect of this appointment: the Committee acknowledges the policy goal that AFFA should not micro-manage privatised R&D companies under the heading of oversight. There is no mention in the SFA of any role for AFFA in the appointment of the CEO, and as such AWI was under no legal obligation to report to AFFA in any respect on this matter. Nevertheless, in the Committee’s view it would have been prudent for AFFA to take a greater interest in this appointment.

3.22 This is firstly for a pragmatic reason: the inaugural Managing Director of a new company such as AWI could well have a special influence - particularly as AWI had had an almost complete turnover of staff from AWRAP days. Secondly, there is a reason of principle relating to AFFA’s duty of oversight: AFFA, whether or not it feels the need to be interested in the identity of the appointee, ought to satisfy itself that such an important appointment is done with due process and diligence. The company’s commitment to due process at this early stage would be a token of its commitment to good corporate governance generally.

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15 Mr C. Dorber, *Committee Hansard*, 26 June 2003, p.36.

16 Mr S. Campbell (WoolProducers), *Committee Hansard*, 28 August 2003, p.42.

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## Development of AWI's strategic plan and operating plan

3.23 The Statutory Funding Agreement required AWI to make a strategic plan and an operating plan and to provide them to the Commonwealth. The Agreement briefly addresses matters which should be covered, but it does not give the Commonwealth a power to direct the detailed contents of the plans, or a power of veto.<sup>17</sup> However AWI and AFFA did consult during the development of the plans, as shown below.

3.24 Mr Dorber told the Committee that 'within three months of commencing operations the board met and adopted a strategic plan and an operating plan for the first two years...'

Every concept proposal and project proposal was required by board dictate to be measured against that strategic and operating plan.<sup>18</sup>

3.25 It is clear both from the evidence of AFFA officers and from documents provided to the committee that this work was inadequate. AFFA described the correspondence which followed:

- 29 May 2001: AWI supplied the 'final draft' strategic plan.
- 7 June 2001: AFFA 'raised a number of issues regarding the lack of detail provided in the plan and requested a copy of the final strategic plan. The Department also indicated that it would be happy to provide comments on the operational plan. Specific comments provided on the draft strategic plan included the need for the plan to:
  - define long-term strategic programs and broad directions of research and innovation;
  - identify Government R&D priorities;
  - clarify linkages between objectives, strategies and outputs;
  - link performance indicators to planned activities;
  - allocate funds to the objectives and strategies;
  - identify in a transparent manner the way in which levy money and matching contributions will be spent;
  - provide other inclusions such as a governance statement on directors' responsibility for planning and reporting; and

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17 Statutory Funding Agreement, clauses 16&17.

18 Mr C. Dorber, *Committee Hansard*, 26 June 2003, p.25.

- include means to ensure faster adoption of R&D outcomes.’

3.26 At this point the draft strategic plan lacked the most basic requirements. AFFA’s description of the relevant correspondence continued:

- 16 July 2001: AWI supplied for review a draft Strategic Plan and Operating Strategy.
- 24 September 2001: AWI supplied a ‘Statement of Corporate Intent’, and sought ‘formal confirmation from the Commonwealth that the materials provided thus far will be accepted as meeting and discharging the Company’s [reporting] obligations to this point in time.’
- 17 October 2001: AFFA advised continuing concerns:

In relation to the expectations for the Strategic Plan (SFA, section 16), AWI’s current plan would probably meet minimum expectations, but I welcome your intention to refine it further in the future. As regards expectations for the Operating Plan (SFA section 17), much more specific information is required than has been provided in the ‘Statement of Corporate Intent’ and ‘Operating Strategy’ submitted by AWI. Without wanting to direct AWI as to the fine detail, I can say that there is a need for greater specificity in projected expenditure for projects areas in 2001-02, clear linkages between projects and the Strategic Plan and the Government’s R&D priorities and adequate performance indicators.

- 26 October 2001: A consultant advised AFFA that she had been engaged to develop AWI’s strategic and operating plans.
- 14 November 2001: AWI asked for ‘urgent advice as to what additional information is required’, since ‘all of these documents have been subject to a most exhaustive development process, and have subsequently been formally ratified by the AWI Board.’ Mr Dorber suggested that AWI was not adequately resourced to change the existing documents, but proposed ‘to incorporate the many additional matters identified by your officers in the ongoing post July 2002 development program of AWI.’ He again sought agreement that the materials provided satisfied the SFA for the year ending 30 June 2001.
- 5 February 2002: AFFA agreed that the documents provided ‘represent an adequate response to the requirements of our Statutory Funding Agreement [for the year ending 30 June 2001].’
- 14-15 March 2002: AFFA officers participated in AWI’s Strategic Planning Forum.
- 8 May 2002: AFFA met the AWI Managing Director to discuss the draft Strategic Plan, and offered to review the draft and provide comments.

- 27 May 2002: AFFA commended progress on the Strategic Plan.
- 26 June 2002: AWI provided the Strategic Plan 2002-2007 and Operating Plan 2002-2003. The Minister acknowledged these on 12 August saying that in his opinion they met the requirements of the Statutory Funding Agreement.<sup>19</sup>

### 3.27 Professor Vizard regretted the delay in finalising the strategic plan:

...the element that was missing was the very strong strategic plan which would delineate those areas to which funding would be applicable and would therefore be the blueprint for how it would be funded and would clarify that it was all in line with what was required by both the company and the Commonwealth. That strategic plan was still not complete—still not there—at the time of my resignation [in June 2002].<sup>20</sup>

### 3.28 The Committee was interested in the reasons for this prolonged process. Mr Taylor, Secretary of AFFA, said:

Early in the history of AWI, I wrote to Mr Dorber about some issues we had about the way in which both the strategic and operational plans were being developed. That related to the 2001-02 year. We had a number of discussions. My colleagues also had discussions and liaised with AWI's consultants in this matter. We subsequently put a lot of energy into the development of the arrangements for the 2002-03 year. That was done principally because we were part of the way through the 2001-02 year.

I think it is fair to say that, in the preparation of the 2002-03 year framework that sits with the statutory funding agreement—the strategic and operational plans—AWI were much improved on what they did in 2001-02, in their first, fledgling year. That has not been an unusual experience with others, but we certainly did want to put pressure on the way in which they developed those strategic and operational plans and frameworks for both the way in which they communicated with their shareholders—the wool producers of Australia—and the way in which they complied with the expenditure of funds in terms of the wool levy.<sup>21</sup>

### ***Comment***

3.29 The Committee notes that the strategic and operating plans were not finalised to AFFA's satisfaction for almost 18 months after AWI's establishment. It is unfortunate that it took so long. Regrettably the Secretary, Mr Taylor, advised the committee that

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19 AFFA, additional information 29 August 2003, p.4ff & attachments.

20 Prof. A. Vizard, *Committee Hansard*, 28 August 2003, p.69.

21 Mr M. Taylor (AFFA), *Committee Hansard*, 17 September 2003, p. 111.

such a delay is not uncommon.<sup>22</sup> The Committee believes that in future agreements of this type AFFA should exert greater oversight over the strategic planning process. Arguably problems in the strategic planning process would be an early warning of other possible problems which should lead AFFA to want closer oversight. Agreements could usefully include conditions such as:

- a deadline for completion of the strategic plan [the AWI SFA required it only ‘as soon as possible’];
- an obligation to provide a draft strategic plan to the Commonwealth;
- an obligation to take into account the Commonwealth’s comments on the draft.

3.30 Whether the Commonwealth should have a greater power to direct the contents of the plan, or to veto a plan that it does not regard as satisfactory, should be a matter for further consideration. The Committee acknowledges that a balance needs to be struck between the needs of Commonwealth oversight and the policy goal of greater industry autonomy.

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22 Mr M. Taylor (AFFA), *Committee Hansard*, 17 September 2003, p. 111.



# CHAPTER FOUR

## Concerns about AWI's management and corporate governance, 2001 and 2002

### WoolProducers' concerns from late 2001

4.1 According to Mr Campbell, president of WoolProducers, WoolProducers first became concerned about the direction of AWI's management in November 2001:<sup>1</sup>

There were a range of matters that became publicly visible that concerned us: design awards; the Shear Express announcement; and on 29 January [2002], an announcement about Woodlots in a press release. There was a range of activities that made us uncomfortable and a lack of focus by the board. As a shareholders association, we were trying to get them to focus on performance measurement and we wrote to them about that in November [2001]. We did not receive a very favourable reply ....<sup>2</sup>

4.2 On 4 February 2002 WoolProducers wrote to Mr Truss, Minister for Agriculture, Fisheries and Forestry, raising concerns about a number of AWI activities. These were:

- National Woodlot Advisory Service: 'The project duplicates services already widely commercially available and clearly fails to address AWI's key obligations under the Commonwealth Statutory Funding Agreement, guidelines for use of compulsory levy funds, and their published strategic plan...'
- AWI funding of Global Design Awards: 'Distancing any promotional activities from R&D was the clearly indicated preference of woolgrowers post-Goulburn, hence The Woolmark Company (TWC) now exists in its own right... Unlike TWC, AWI has no means in place by which to measure the performance of any 'promotional funds' spent by AWI... This activity also does not address the core business of a company in receipt of statutory levy funds, namely market failure research....'
- Shear Express: '...the CEO of AWI is to assume the Chair of the Shear Express Board. It is our view that the review of this project as an R&D investment for growers and AWI may only be properly conducted if AWI as an investing party is at arms length from the Board or management of Shear Express...'

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1 WoolProducers advised that it is a subscription funded growers' representative organisation with about 14,000 members. Submission 1, p.3.

2 Mr S. Campbell (WoolProducers), *Committee Hansard* 28 August 2003, p.44.

- Performance measurement: ‘It is critical that transparent and readily available information is provided to levy payers before the next wool poll. To date, WoolProducers have requested this information from AWI on two occasions and are yet to receive a reply. The performance measures that AWI has released in public are contradictory, confused and inconsistent.’
- Involvement of the Board: ‘WoolProducers are concerned that appropriate accountability and a system of internal controls have not been put in place by the Board of AWI... There is great concern amongst members that substantial funds are able to be expended by the CEO without full knowledge of the Board... As there was no public process sponsored by the AWI Board or the AWI Board Chairperson of which we are aware, which resulted in the appointment of the current CEO, this abrogation of responsibility clearly started early in the business life of AWI.’<sup>3</sup>

4.3 Mr Taylor, Secretary of AFFA, gave evidence that at the time AFFA regarded these concerns as matters of project priority or management style, which AWI should resolve internally, rather than breaches of the Statutory Funding Agreement.<sup>4</sup>

### ***Comment***

4.4 The Committee considers that the final two issues raised by Woolproducers did not necessarily relate to project priorities or management style and should have been of concern to both the department and the minister.

4.5 The penultimate issue of concerns in Woolproducers’ letter to the minister asserted a lack of clear and accountable reporting arrangements. These matters go directly to the issue of the appropriate use of funds provided through grower levies and from consolidated revenue. Such reporting arrangements are essential to enable AFFA and more importantly the minister to be satisfied funds are being spent in accordance with the conditions imposed through the SFA.

4.6 It is the committee’s view that the final issue put to the minister by Woolproducers also required urgent investigation. Any concern that there was no effective accountability through the board to both the minister and levy payers and that there was no system of internal controls in place should have been quickly and fully investigated. If those concerns were established as fact the integrity of the relationship between AWI, growers and the minister through the SFA, and proper accountability for millions of dollars of growers’ and taxpayers’ funds, would have been at risk.

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3 Submission 1, WoolProducers, attachment C.

4 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2002, p.119ff.

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## Board's skills and involvement in decision-making

4.7 WoolProducers argued that the former AWI Board did not have an 'appropriate skills mix to conduct their business independently':

Boards must have adequate knowledge of the company business internal to the Board so that they can effect judgement independent of dependence on management, according to OECD guidelines for Board governance. Additionally, the problem became larger and more urgent subsequent to the resignation of Directors Vizard and Patten from the Board. Mr Patten's resignation [in March 2002] left the Board particularly weak in corporate financial experience. The former Board only addressed this matter in the leadup to the AGM in 2002 by two very late additional appointments and under considerable public pressure by WoolProducers and others.<sup>5</sup>

4.8 The submission of four former Board members argued that the Board did have appropriate skills:

Up until de-merger the directors of AWI were selected and appointed by Mr Rodney Price and ratified by the AWS Board. Each director was selected for their knowledge, experience and skills in varying categories that would be of significant advantage to a "start up" research, development and innovation company... Prior to de-merger, the skill sets of both TWC and AWI were examined carefully by the Chair of AWS to ensure that the Boards had balanced expertise. It was determined that AWI lacked the skill of international fibre marketing and TWC needed an enhanced accounting skill. A meeting of the AWS Board was held and the decision was made to swap directors, with John Patten moving to TWC and Don Nelson moving to AWI... The existing directors appointed two new Board members to the Board of AWI after de-merger. These appointments were made after an extensive search to identify a woolgrower that was not agri-politically aligned or involved who had experience "off farm" and preferably further down the wool pipeline. That position was filled by Peter Sykes ... The other position was for an internationally renowned scientist who had credibility in genetics and that position was filled by Professor Alan Trounson.<sup>6</sup>

4.9 On the TWC/AWI swap of directors (March 2002), Professor Vizard was concerned that 'the board should have had an opportunity to actually be involved in the discussion and submit a collective view on the mix of board skills and experience necessary...':

We had no such opportunity. I put forward the view that this was actually a return to something that we were trying to avoid. Previously in AWRAP

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5 WoolProducers, additional information: *List of Corporate Governance Concerns*, tabled 28 August 2003, p.4.

6 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.3-4.

there was a belief that directors got the position by having an old school tie sort of club approach, and what we wanted was a completely transparent system of appointment of directors. I did not think that this was such an appointment. Again, I felt that giving the board no opportunity to be involved in that discussion was a clear and fundamental departure from best practice corporate governance and the responsibility that directors have to help ensure that the best possible candidates with the most appropriate range of skills and talents are recruited to boards.<sup>7</sup>

#### 4.10 WoolProducers commented on this matter:

This internal manoeuvring of Directors between companies is, again, inconsistent with governance practices expected and deserved by compulsory shareholders.<sup>8</sup>

#### 4.11 The submission of four former Board members denied that the Board was inadequately involved in decision-making:

From February 2001 until June 2002 (when Mr Vizard resigned), each Board meeting was attended by all directors... Most Board folders were in excess of a thousand pages of written material to consider. The diligence of the directors was palpable and it is highly defamatory of the directors that they should have had their diligence and careful attention to the governance of the company besmirched by such innuendo. No decisions were ever made by two directors. The full Board was expected to, and did, participate in all such matters.<sup>9</sup>

#### 4.12 Mr Dorber stressed that ‘...the board had access to everything: the staff, the accounts, the committees, me. There were no rules about who you could or could not talk to.’

#### 4.13 On the other hand, Professor Vizard said: ‘Mr Dorber stated to the Board in February 2002 that there were 200 projects, and very few of those 200 would have come to the board with any detail.’<sup>10</sup>

#### 4.14 A point of concern to some was that the Managing Director was delegated to spend up to \$2 million without the approval of the Board. WoolProducers argued that this was excessive:

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7 Prof. Andrew Vizard, *Committee Hansard* 28 August 2003, p.62.

8 WoolProducers, additional information: *List of Corporate Governance Concerns*, tabled 28 August 2003, p.1.

9 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.3.

10 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.25. Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.68; similarly p.76.

To examine the absurdity of this, with an annual spend of about \$70 million, an MD in this position at AWI could in fact spend the entire company budget within 35 projects.<sup>11</sup>

#### 4.15 Professor Vizard's recollection of this was:

The proposal was put forward on the basis that in this interim period there would be considerable need for some rapid decision making by the managing director.... I remember I expressed concern about the size of that and thought it was probably excessive. After some discussion, it was agreed that the \$2 million would stand; however, it would be subject to review in January 2002. To my knowledge, that review did not occur.<sup>12</sup>

4.16 Mr Dorber stressed that 'in practice, there was nothing that did not go to the board. There was no project that I did not run past the board formally or informally.'<sup>13</sup>

4.17 The Committee notes that the post-November 2002 Board has reduced the Managing Director's spend limit from \$2 million to \$500,000.<sup>14</sup>

4.18 Professor Vizard argued that Board was handicapped in considering projects in the absence of a 'strong strategic position':

One of the big elements that was missing, in my opinion, through this whole process and should be driving decisions on investment in R&D was a strong strategic position. As I have said previously, the strategic portfolio for investment, particularly on on-farm projects, had not been developed whilst I was a board member.<sup>15</sup>

### **Concerns about evaluation of projects**

4.19 One of the concerns about AWI's management during the relevant period was its approach to the selection of projects. There are two related matters:

- Were all projects consistent with clause 5 or schedule 4 of the Statutory Funding Agreement?
- Were some projects undertaken or rejected unwisely or without due process despite the fact that they complied with the SFA?

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11 Submission 1, WoolProducers, p.38.

12 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.59.

13 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.25.

14 Submission 13, AWI, par. 4.1.

15 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.75.

4.20 If SFA-controlled money is spent contrary to the conditions of the SFA, this should obviously be a concern to government. If the money is spent pursuant to the SFA, but in a manner inconsistent with good governance practice, this is more problematic for government..

4.21 Mr Dorber described AWI's project evaluation under his management:

Within three months of commencing operations the board met and adopted a strategic plan and an operating plan for the first two years. Every concept proposal and project proposal was required by board dictate to be measured against that strategic and operating plan.<sup>16</sup>

4.22 He described the Innovar project evaluation system:

One of the earliest things we did was to implement the Innovar concept project and proposal assessment model... It is a very effective model, and it was used in every instance, including on the famed and poorly named woodlot project. Those records were placed in front of the board so that, when they made a decision, they had the original project proposal, the Innovar score sheets, the reports of the project officer and the program manager, and my recommendations arising from that.<sup>17</sup>

4.23 Professor Vizard thought that this system was sound and 'allowed for an objective assessment of programs', but he did not think that it was always used properly:

My problem was not necessarily with that as a concept but at times I had quite a deal of difficulty as to whether it was being conducted and, when it was being conducted, whether it was being conducted properly.... I notice Mr Dorber said in his statement that the Innovar program was used on all projects. I know that is incorrect.<sup>18</sup>

4.24 Professor Vizard commented on the National Woodlot project, which was one of the matters that prompted WoolProducers' letter of 4 February 2002 to the Minister, Mr Truss:

The project was never presented to the board for approval or comment prior to its public release [on 29 January 2002] .... When the project was made public I looked at the details that were publicly available and became concerned. I contacted the chair seeking that this project be discussed at the next board meeting of 21 February 2002. I remember that, at that meeting, Ms Murphy and I raised a series of concerns regarding this project.... The board resolved that management rigorously review this project within its

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16 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.26.

17 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.20.

18 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.66.

first year of operations. Despite the evidence given by Mr Dorber, I was never privy to any Innovar process involved in that project, if it did exist.<sup>19</sup>

4.25 Another contentious project was the Wool Profit Map. Professor Vizard:

By this Innovar process, which is documented here and was tabled at the May 2001 board meeting, it came out as one of the highest ranked projects. Nevertheless, Mr Dorber recommended that it be discontinued. I remember questioning Mr Dorber at the time and asking, ‘Why would you recommend discontinuing this project when it is one of the highest ranked projects that we have?’ Mr Dorber explained, to the best of my memory, that there were some other concerns with the project, which I could not quite understand, and that the analysis had been done using an old weighting system of the Innovar method so subsequently, that ranking could be wrong. I said, ‘Which particular weightings are incorrect and if you reweight it, does it still come out?’ but I got no satisfactory answer. So I left it at that but the project was discontinued.<sup>20</sup>

4.26 Mr John Grant, a director of Innovar Pty Ltd, said of the Wool Profit Map: ‘the scoring was completely ignored and the project dropped.... The basis for this project being dropped was never publicly made clear.’<sup>21</sup>

4.27 The new AWI Board argued that ‘the Innovar scoring system to which Mr Dorber has referred in his evidence is a useful tool but it can only be applied to some on-farm projects, which make up less than 40% of AWI's projects’:

[5.53] It has no application to off-farm projects, such as a project to develop more efficient wool spinning processes. Mr Dorber's claim that it was '*used for almost every project and concept assessment from approximately May 2001*' is not true. There is no evidence that the scoring system nor any other objective appraisal methodology was ever applied to the following projects:

- (a) 'Million Dollar Movie';
- (b) European Wool Awards;
- (c) Farmhand appeal donation;
- (d) donation to the Charles Sturt University's Somerville Collection; and
- (e) '*Woodlot*' project.<sup>22</sup>

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19 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.66.

20 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.73.

21 Prof. A Vizard, additional information: papers tabled at hearing 28 August 2003: comments of Mr J. Grant, p.1.

22 Submission 13, AWI, p.27.

4.28 In reply Mr Dorber denied that ‘the Innovar scoring system does not have any application to "off farm" projects’:

It was the only system available pending the development of a new tool. It was not ideal at the time Mr Dorber was in office but it was his view, and that of his board, that it was adequate. The matters referred to in paragraph 5.53 [of AWI's submission 13 quoted directly above] with respect to specific examples as to the applicability of the scoring system is a distortion of the true circumstances, noting that over 300 projects were on foot.<sup>23</sup>

4.29 The Committee notes the comments on project evaluation and management in of AWI's May 2003 *Review of Performance*:

Strategic Plan implementation has started but, at April 2003, AWI is more project than Strategic Plan driven... The expenditure patterns also suggest more project rather than Plan driven investment over 2002...

Most AWI managers identify that project busyness was dominant over 2001 and 2002 and that it is vital to shift more of managers' time to project management, review and delivery of R&D results....

The restructure and relocation in March 2001 were significant factors. Staff recruitment and procedure development began in 2001. Then 2002 saw about eight months of AWI consolidation and direction identification through strategic planning, with impressive efforts by most managers and associated staff to advance systems and project handling. New uncertainty developed in the latter part of 2002. This was settled by March 2003. Many issues discussed during this Review are now receiving systematic attention.<sup>24</sup>

4.30 The comments above go to how well AWI prioritised projects. All projects, of course, had to be consistent with the Statutory Funding Agreement. On this the November 2003 audit of AWI's compliance with the SFA for the 2002/2003 year commented:

It is noted that there appeared to be no formal assessment of projects meeting the requirements of the SFA, prior to approving the projects. In a small number of cases there was formal documentation as to whether the projects fell within the strategic objectives of AWI.<sup>25</sup>

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23 Submission 16, Mr C. Dorber, p.13.

24 Dr S. Welsman, *Review of Performance - Summary 2003*, Australian Wool Innovation Ltd, p.9,16.

25 AWI, additional information 9 January 2004: PricewaterhouseCoopers report on AWI's compliance with Statutory Funding Agreement, 25 November 2003.



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## Status of Directors Vizard and Murphy, March 2002

4.31 Professor Andrew Vizard was a director of AWS and AWI, appointed 1 January 2001. In October 2001 he was elected to the Board of AWS and (or so he thought) consequently to the Board of AWI. On or about 11 March 2002 Mr Dorber told Professor Vizard that, according to legal advice, in fact he had been elected to the board of AWS but not AWI; his status as a director of AWI was still ‘appointed 1 January 2001’; therefore, he would have to face election to AWI again in 2002, according to the rule in the AWI constitution that the directors who have served longest since their last election or appointment face election in rotation. Ms Trish Murphy was in the same position.

4.32 WoolProducers described the situation thus:

Four Directors stood for election at the AWS AGM 2001. The pre-meeting information made it clear that the two ‘A’ class Directors facing reelection, Directors Murphy and Vizard, would become Directors of AWI if they were successfully reelected to the Board of AWS.

The belief of all participants in the AGM process (standing Directors and voters) was that the A-Class Directors were facing an election where their AWI Directorship was at risk.

The company failed to complete tasks subsequent to the AGM in 2001 that would have ensured that the AWS Directors elected at the meeting (Dr Vizard, Ms P. Murphy) were properly installed as the Directors of AWI.<sup>26</sup>

4.33 The submission of four former AWI Board members said similarly:

Prior to the de-merger of the companies in April 2002, due diligence was carried out and in March 2002 the AWI solicitors discovered that the declarations of directors at the AWS AGM had not been done correctly.<sup>27</sup>

4.34 If it were judged that Professor Vizard and Ms Murphy had been elected to AWI in October 2001, then Ms McCaskill and Mr Staley would face election in 2002.

4.35 Legal advice to AWI on 26 February 2002 noted that this matter could be solved in the following way:

If Patricia Murphy and Andrew Vizard are removed from office as Directors of AWI and immediately reappointed prior to the Demerger, then neither

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26 WoolProducers, additional information: *List of Corporate Governance Concerns*, tabled 28 August 2003, p.1.

27 Submission 9, Ms M. McCaskill & 3 other former AWI directors, pp.2-3.

will be required to retire by rotation at the first AGM held after the Demerger.<sup>28</sup>

4.36 Professor Vizard stressed that there was no constitutional reason why they had to face election twice running: ‘Our retirement and subsequent reappointment to AWI could have been, and should have been, recorded at that [2001] AWS AGM.’<sup>29</sup>

4.37 Professor Vizard described his attempts to solve the problem:

Despite repeated attempts by me to obtain a response from Mr Dorber to my requests [for copies of relevant legal advice and related documents], it was not until 3 April [2002] that I finally received a reply—some 23 days after I requested an immediate response. The response consisted of copies of two emails of legal advice that Mr Dorber had received, dated 26 February and 14 February. Although this reply was an incomplete response to my request, it did show that Mr Dorber had been given exactly the same legal advice as I had—that is, at the time Mr Dorber had received the advice for the anomalous situation, he had also received advice on how the anomaly could be fixed by the board of AWS recording the retirement and subsequent reappointment of Ms Murphy and me to the board of AWI...

What particularly concerned me about this was that, despite several conversations with me about this issue, Mr Dorber had never informed me that he had received such advice nor had he provided the board with the legal advice he had received. On the day that I received Mr Dorber’s response, 3 April, I contacted AWI lawyers instructing them to properly document the retirement-reappointment process required to fix the anomaly so that it could be presented to the board for a decision. Late that day, the lawyers rang back saying that they had discovered a problem. Under the process of demerger, that day—the same day I had finally received a response from Mr Dorber—was the very last day on which the resignation and reappointment of Ms Murphy and I could be recorded. I immediately contacted Ms McCaskill suggesting that AWI request AWS to send out a circular resolution so that the directors of AWS could vote on the issue immediately. Ms McCaskill later informed me that evening that the chair of AWS, Mr Price, had declined the request to circulate such a resolution.

A few days later, on Monday, 8 April, AWI legal advisers contacted me stating that they had reviewed the legal situation and had discovered that, in fact, a solution to the anomalous situation still existed. The recording of the retirement and subsequent reappointment of directors Vizard and Murphy could still occur, although through a slightly different process. However,

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28 Prof. A. Vizard, additional information tabled at hearing 28 August 2003, item F: email from R. Feenaghty to C. Dorber, 26 February 2002. Similarly Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.2.

29 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.63.

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owing to the forthcoming demerger of AWI and AWS, this window of opportunity would also expire on 1 May 2002.

I rang the chair, asking that the election of directors be added as an agenda item at the next board meeting on 18 April 2002. At that meeting the matter was discussed. The AWI board voted to reject pursuing the legal solution that was outlined, with Ms Murphy and I voting in favour; the chair, directors Dorber and Nelson voting against and director Staley abstaining.<sup>30</sup>

#### 4.38 Ms Murphy commented:

I supported the concept that shareholders had rightly or wrongly understood themselves to be voting for A and B class directors rather than AWS directors in the election of 2001. I supported the notion that all should be done to legally rectify this problem. I accepted the legal advice tabled on the issue and was disappointed at the result of a resolution to overturn this position.<sup>31</sup>

#### 4.39 WoolProducers argued that this episode was a serious failure of corporate governance:

The Board failed to elect Directors to AWI in 2001. The Directors failed to advise shareholders of this fact at the time....

When this major process error was detected, and solutions noted, the Board actively chose not to advise all shareholders of the nature of the problem immediately it was detected, or of any solutions to the problem.

The Directors then actively voted not to effect a solution to present unelected, appointed-only Directors in normal rotation.

As a consequence this ensured for the moment that the appointed, unelected, then-Chair Marie McCaskill did not face election at the forthcoming [October 2002] AGM.<sup>32</sup>

#### 4.40 Professor Vizard too argued that this was ‘an issue of corporate governance’:

I was concerned in trying to maintain shareholders’ rights. The AWI shareholders believed that they had already had their opportunity to vote on Ms Murphy and me and would be rightfully seeking an opportunity to express their opinion about other directors in proper rotation. In my opinion,

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30 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.63-4.

31 Submission 14, Ms P. Murphy, p.1.

32 WoolProducers, additional information: *List of Corporate Governance Concerns*, tabled 28 August 2003, p.1.

the board [at the meeting of 18 April 2002] voted against trying to maintain the integrity and intent of the system.<sup>33</sup>

#### 4.41 Mr Dorber said:

Claims that the former AWI board failed to disclose a 'failed AGM' in respect of the election of certain directors is untrue...The facts are that, when I identified to the then board deficiencies surrounding the demerger process because of oversights in the constitution of AWI Pty Ltd, subsequently AWI Ltd, those matters were reported immediately to the board, subjected to immediate legal investigation and disclosed in a timely and proper manner to shareholders.<sup>34</sup>

4.42 In their evidence to this inquiry four former AWI Board members and Mr Dorber did not dispute that shareholders had understood themselves to be voting for AWI directors through the system of A and B class AWS directors in the 2001 election. They did not suggest that it was right that Professor Vizard and Ms Murphy should have to stand for election twice running. They did not offer any comment on why the Board, on 18 April 2002, rejected the solution (removing and reappointing them) that would have avoided this. However the Committee notes that in a media release on 1 July 2002, responding to media comments about Professor Vizard's resignation from the AWI Board on 14 June, Ms McCaskill said:

To accept the option of removing and then reappointing directors would have denied shareholders the chance to exercise their democratic right.<sup>35</sup>

4.43 As well, Mr Dorber at the time was reported as saying he voted against the resignation/reappointment option because 'it would remove transparency from the process and it would look a bit smelly and it was a bit late.'<sup>36</sup>

#### ***Comment***

4.44 The Committee notes the uncontradicted evidence that all concerned believed that the 2001 election was an election of AWI directors. The Committee agrees with Professor Vizard that in light of this 'commonsense would indicate that Ms McCaskill and Mr Staley, as the longest-serving AWI directors, would be standing [in 2002].'<sup>37</sup> The comments of both former Board members and Mr Dorber accept that the

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33 Prof. Andrew Vizard, *Committee Hansard* 28 August 2003, p.63-4.

34 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.11.

35 AWI, *AWI Board takes strategic decisions for the Australian wool industry*, news release 1 July 2002.

36 *Vizard tells: why I quit*, *The Weekly Times*, 26 June 2002, p.1,4. Submission 1, WoolProducers, attachment U.

37 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.62.

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Vizard/Murphy problem was unanticipated and unintended. The solution to the problem - for them to resign and be reappointed before demerger - was straightforward, as shown in legal advice to AWI in February 2002.

4.45 The Committee considers that in the circumstances it would have been appropriate to put this solution into effect. Ms McCaskill's explanation at the time of why the Board refused to do so ('to accept the option of removing and then reappointing directors would have denied shareholders the chance to exercise their democratic right') is unconvincing. The essence of the Vizard/Murphy problem was that the shareholders *had* exercised their democratic right at the appropriate time, but this had not been recognised.<sup>38</sup>

4.46 It is the Committee's view that resignation/ reappointment should not be used as a tactic to avoid facing a timely election. However this was not and is not at issue. Resignation/ reappointment was a solution to a one-off problem, and was possible only before demerger. It could not be repeated, because the AWI constitution since demerger provides that an appointed Director must face election at the following annual general meeting.

4.47 Against these matters, it should be noted that four of the six non-executive directors of AWI needed to face election in 2002. Mr Staley (a former AWI director) commented:

Due to the extraordinary, untrue and vindictive comments from a minority of shareholders and the rural press, my fellow non-executive director, Mr. Don Nelson and I decided to submit ourselves for re-election at the November 2002 annual general meeting even though we were not required to submit to re-election until November 2004.<sup>39</sup>

### **Conduct of the Board election, October 2002**

4.48 The Committee considered two matters:

- claims that the Board deliberately obstructed external nominations to the Board;
- claims that AWI improperly used the company's money to campaign on behalf of sitting directors.

#### ***Whether AWI obstructed nominations to the Board***

4.49 WoolProducers argued that the sitting Board deliberately obstructed external nominations to the Board at the October 2002 election.

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38 Senator Cherry disagrees with paragraph 4.45 and has provided supplementary comments.

39 Submission 7, Mr M. Staley, p.2.

4.50 Under the AWI constitution at the time a person other than a retiring director was eligible for election if the person was nominated by 5% of the shareholders. The Board could at their discretion accept nominations without this condition.

4.51 WoolProducers claimed that AWI delayed releasing the rules of the election for five weeks in July 2002:

[This] left shareholders only a further five weeks to the deadline to comply with the rules by obtaining 1,830 (5% of shareholders) signatures to nominate an alternative candidate..... The rules were also made as difficult as possible. Shareholders were unable to put five nominee names on one form, consequently the number of signatures to be collected in total became 1,830 multiplied by five....<sup>40</sup>

4.52 WoolProducers asked the Board to accept five nominees without the signatures. The regular Board meeting at which this could have been considered (16 September) was only three days before the close of nominations. On 16 September the Managing Director told press that no announcement would be made until after the close of nominations. By that time WoolProducers had already gathered the signatures, and the Board never considered the request.<sup>41</sup>

4.53 On 20 September Ms McCaskill said in a news release that AWI required the signatures in order to 'comply with the constitutional requirements... We have done nothing more than to observe the established requirements, something that we are legally required to do.'<sup>42</sup>

4.54 On 16 October 2002, in a fullpage advertisement in the Weekly Times which commented on the WoolProducers' candidates' election platform, AWI said:

The rule requiring 5% of shareholder signatures for nominees to stand for election was included in the AWI constitution as part of the demerger of AWI and was not imposed by the current Board. It was implemented to ensure stability for the Board and to avoid continual coups by a small percentage of shareholders.<sup>43</sup>

4.55 When questioned about this at the 31 October 2002 Annual General Meeting, Ms McCaskill at some points suggested that the outcome was simply unfortunate timing:

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40 Submission 1, WoolProducers, p.34.

41 Submission 1, WoolProducers, p.35.

42 AWI, *Government supports AWI approach to candidate endorsement*, news release 20 September 2002.

43 *Who's pulling the wool over whose eyes?* The Weekly Times, 16 October 2002, p.11. Submission 1, WoolProducers, attachment L. The advertisement also appeared in The Land on 17 October 2002.

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...The board did not have the opportunity to consider the request... because by the time of that first board meeting after the request was made, AWI was already on notice that the candidates intended to obtain the support of 5% of the shareholders...

The entire dates [of board meetings] for the whole of 2002 were locked in at the beginning of the year, so there is no conspiracy theory, I'm really sorry.<sup>44</sup>

4.56 At the same meeting Ms McCaskill at other times suggested that it was a deliberate decision of the Board (although, as noted, the Board never considered WoolProducers' request):

The constitution that AWI operates under was in existence before the board of AWI was appointed. It was put together after considerable consultation with some advisory groups pre the incarnation of Australian Wool Innovation. And that advisory group, which did consist of the old Wool Council and some of the state farm organisations, were in fact part of the group that were insistent upon the 5 per cent rule. So, it is the view of the Directors of AWI that for this annual general meeting we would, in fact, adhere to the constitution....

It was consistent with the rules and the spirit of the constitution that the board required those candidates to be supported by the requisite number of shareholders.<sup>45</sup>

### ***Comment***

4.57 The Committee believes that the former Board was deliberately unhelpful to the WoolProducers nominees. Regardless of the schedule of regular Board meetings, it would not have been hard to call a special Board meeting by teleconference to consider WoolProducers' request.

4.58 Ms McCaskill's claims that applying the 5% rule was a matter of 'adhering to the constitution' or 'observing the legal requirements' were seriously misleading. The constitution included *both* the 5% rule and the facility for the Board, at discretion, to waive it. It contained no presumption about which course the Board should take.

4.59 Nor does the Committee accept that applying the 5% rule was necessary to adhere to the spirit of the constitution. If the aim of the 5% rule was to prevent

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44 Submission 1, WoolProducers, attachment Z, transcript of 31 October 2002 AWI annual general meeting, p.89,100.

45 Submission 1, WoolProducers, attachment Z, transcript of 31 October 2002 AWI annual general meeting, p.49,89; see also Mr McLachlan, p.105.

‘continual coups by a small percentage of shareholders’, this could hardly be said to apply to nominees from a peak interest group with a claimed membership of 14,000.<sup>46</sup>

### ***Whether AWI campaigned for sitting directors***

4.60 WoolProducers and the new AWI Board argued that AWI under the former management had improperly used the company’s money to campaign on behalf of sitting directors at the October 2002 election.

4.61 The submission of four former AWI directors claimed that:

Every part of the election process was subjected to legal scrutiny. No election related material was published, unless it had been signed-off in advance by Mallesons. The legal firm representing AFFA, Minter Ellison, have already twice confirmed that the entire process was exercised with due diligence and care.<sup>47</sup>

4.62 According to the new AWI Board, ‘during the period immediately prior to the election of directors in October 2002, Mr Dorber actively campaigned for the re-election of the existing board at AWI’s expense...’;

He engaged a freelance journalist to ask specific questions at a speech given by Ian McLachlan at the Victorian Rural Press Club. He also engaged a communications company specifically to assist in the campaign to have the sitting directors re-elected. The board believes that this expenditure was not for the benefit of AWI or woolgrowers but for the benefit of the sitting directors.<sup>48</sup>

[He had]... regular correspondence in the months leading up to the election with both John Roydhouse, the principal of Rural IT & Web Pty Ltd, and the members of AWI’s Wool Advisory Group concerning how the profiles of the current members of the Board with woolgrowers should be enhanced and how those woolgrowers should be discouraged from voting for Mr McLachlan’s team.<sup>49</sup>

4.63 Claims of improper behaviour in relation to the 2002 Board election rest on three matters:

- payment to David Everist, journalist, to ask questions at a press luncheon;

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46 Senator Cherry disagrees with paragraphs 4.57 to 4.59 and has provided supplementary comments.

47 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.3.

48 Submission 13, AWI, par.1.6. Mr B. Van Rooyen (AWI), *Committee Hansard* 28 August 2003, p.82.

49 Submission 17, AWI, p.4.



- payment to i2K Communications for consultancy services;
- advertisements in the rural press.

4.64 The SFA prohibits use of the Funds for 'agri-political activity'.

*David Everist*

4.65 AWI paid Mr David Everist, a freelance journalist, \$638 to ask questions of Mr McLachlan (a WoolProducers' candidate) at a Victorian Rural Press Club luncheon on 18 October 2002. In evidence Mr Dorber at first denied, but later admitted, that he had suggested particular questions.<sup>50</sup>

*i2K Communications*

4.66 AWI paid i2K Communications \$13,003.85 in October and November 2002. In an email to Board members and 13 others (20 September) the consultant introduced herself by saying:

I have been retained to assist with the campaign for the re-election of the current AWI Board. Part of the brief is to improve third party exposure for the Board members and AWI issues in all states. I plan to be in touch with the members of the advisory group and the board this weekend to discuss a communications strategy...

4.67 Mr Dorber replied by email on 21 September saying, 'Good one Claire.'

4.68 In an email to Mr Dorber, Ms McCaskill and Mr John Roydhouse (23 September) the consultant said, among other things:

1. Use WAG [Wool Advisory Group] members to endorse Board members....
2. ...we need to get the media interviewing Board members in each state about issues (eg, processing, genetics etc, - not politics)... One WAG member suggested any projects which touched on the drought would be well received and attract attention - I think he has an excellent point...
3. Any political interviews to be handled by the chair - don't think we can run the risk of putting other up....
5. Use agents group to influence producers - apparently there is a list of agents floating about in AWI. Possibly need to call a briefing for these guys in the next week or so before other group gets to them...

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50 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.44. Mr S. Campbell (WoolProducers), *Committee Hansard* 28 August 2003, p.53. Submission 16, Mr C. Dorber, p.7. AWI, submission 13, p.19-20; submission 17, p.4. PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.14.

7. Advertising - open to suggestion here, but I would not advocate running provocative ads at this stage...

4.69 In a further email to Mr Dorber, Ms McCaskill and Mr John Roydhouse on the same day the consultant said, among other things:

...I agree board members should not be publicly campaigning for re-election. However they can be out there talking about issues and projects.... Ads which complement other communications - such as WAG letters etc. in profiling the board I think have some value.<sup>51</sup>

4.70 In context, it is most likely that 'board members should not be publicly campaigning for re-election' should be read as a consequence or further specification of the statement 'Any political interviews to be handled by the chair - don't think we can run the risk of putting others up...' <sup>52</sup>

#### *Advertisements in rural press*

4.71 In an email to Board members and Wool Advisory Group members (2 October 2002), Mr Dorber said:

...a national advertising campaign will also be undertaken. The most efficient manner would be to run a series of advertisements in the Rural Press publications two weeks immediately prior to the AGM... budget is \$7,500 for this purpose ... this is a defensible level of expenditure, consistent with our responsibility to shareholders.<sup>53</sup>

4.72 In the Weekly Times (16 October) and The Land (17 October) appeared a full page advertisement 'Who's pulling the wool over whose eyes?'<sup>54</sup> This was placed by AWI, apparently at a cost of \$4,895.<sup>55</sup> It sets 'WoolProducers' candidates policy statements' against 'What AWI is doing'.

4.73 The AWI comments are mostly rebuttals of the accusations implicit in the WoolProducers statements. However they include what could arguably be seen as a

51 Submission 13, AWI, attachment 4. PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.10.

52 Submission 13, AWI, attachment 4. PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.10. AWI, additional information 13 January 2004.

53 PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.10.

54 *Who's pulling the wool over whose eyes?* The Weekly Times, 16 October 2002, p.11. Submission 1, WoolProducers, attachment L.

55 PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.47.

few direct attacks on the WoolProducers' candidates, such as that italicised below. For example:

<b>Wool Producers Candidates Policy Statement</b>	<b>What AWI is doing</b>
4. The candidates will respect the Constitution in spirit and practice....	The current Board complies with the AWI Constitution....
2. The candidates will only be responsible to AWI shareholders...	The AWI Board works hard to represent all shareholders.... <i>The same cannot be said of the 'Shareholders' Candidates', who are in reality the candidates of the Wool Producer growers group.</i> [emphasis added]

4.74 Mr Dorber defended placing this advertisement:

This document was, on the advice of Mallesons Stephen Jaques, necessary to publish in view of the serious attempt by some wool producers to undermine the then AWI Board by making accusation which, if substantiated, would have amounted to breaches of the SFA and/or corporate governance.<sup>56</sup>

4.75 A full page advertisement appeared in The Land (17 October) disparaging the 'Shareholders candidates.' It was attributed to 'concerned wool producers.' WoolProducers claimed that their inquiries at the newspaper had found it was paid for by AWI.<sup>57</sup>

4.76 In relation to the advertisements, the new AWI Board commented that there may be a fine line between 'putting out the true facts' and electioneering:

We questioned those advertisements and the expenditure and the answer in one case was given that it was to correct statements made by the opposing nominees, which were 'defamatory'. In other words, it was an attempt to set the record straight, so it came under the heading of putting out the true facts in the marketplace. The reality is that once you get involved in doing those things you really do immediately go over the edge and can be criticised for spending company funds on electioneering.<sup>58</sup>

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56 Submission 16, Mr C. Dorber, p.18.

57 *Remember the days when the Wool Board was stacked with wool producers?* The Land, 17 October 2002. Submission 1, WoolProducers, p.21 & attachment K.

58 Mr B. Van Rooyen (AWI), *Committee Hansard* 28 August 2003, p.100.

4.77 Mr Dorber denied that his conduct in relation to the election campaign was not in the best interests of AWI:

Mr Dorber did not lead a campaign for the re-election of the existing Board. Mr Dorber did not promote the Board members nor undermine other candidates. Mr Dorber did vigorously promote the successes of the company under its then Board as directed.....<sup>59</sup>

4.78 The post November 2002 Board has resolved that any campaigning for re-election must be undertaken at the directors', rather than at AWI's, expense.<sup>60</sup>

### ***Comment***

4.79 The Committee accepts that AWI may use company money to advise shareholders about the company's activities, or to encourage shareholders to participate in an election, providing it is done in a way that is impartial to the outcome of the election.

4.80 It is the Committee's view, however, that the previous board authorised improper expenditure on a campaign to assist the re-election of the sitting directors.

4.81 In reaching this conclusion the Committee is most influenced by these points:

- The i2K emails are unambiguous;
- 'Who's pulling the wool over whose eyes?' included not only matters of information but also direct attacks on the WoolProducers' candidates.

4.82 The Australian Government Solicitor, in advice to AFFA, noted that legal precedent suggests that using the company's money for election campaigning would breach the Corporations Law duty to act in the best interests of the company and for a proper purpose, and would involve improper use of the directors' position to gain an advantage for themselves. In the precedent judgment, 'even though the directors acted honestly and in good faith in what they believed to be the best interests of the company, their primary purpose was to secure their own re-election to the Board. As such, they had misused their authority as directors.'<sup>61</sup>

4.83 The Committee believes this expenditure benefited sitting directors and not woolgrowers. The use of the company's money to campaign for sitting directors was

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59 Submission 16, Mr C. Dorber, p.6-7.

60 Submission 13, AWI, par.1.5.

61 AFFA, additional information 29 August 2003: AGS advice 5/8/03, p.16. *Advance Bank Australia v FAI Insurances Ltd*, (1987) 9 NSWLR 464.

improper. The Committee recommends that this matter be referred to the Australian Securities and Investments Commission.<sup>62</sup>

### **Recommendation 1**

**The question whether AWI used company money to campaign for sitting directors during the 2002 Board election, in breach of Corporations Law, should be referred to the Australian Securities and Investments Commission.**

4.84 The question also arises whether the election-related expenditure was contrary to the SFA as being funding of 'agri-political activity'. The SFA defines 'agri-political activity' as:

'political campaigning or funding, developing, designing, resourcing or participating in activities intended to exert political rather than advisory influence on government policies or in activities intended to exert political influence on public opinion.'<sup>63</sup>

4.85 The Australian Government Solicitor, in advice to AFFA, felt that it is unclear whether the SFA definition of 'agri-political activity' is intended to apply only to 'external' political activity intended to affect government and public opinion; or whether it applies also to 'internal' political activity intended to influence company members' vote in a election of directors. AGS concluded:

We doubt that it could be confidently concluded that the use of Funds for election campaigning by the then AWI Board was prohibited on the basis that it was Agri-political activity within the meaning of the SFA.<sup>64</sup>

4.86 The Committee recommends in chapter 7 that the definition of 'agri-political activity' should be amended to explicitly include internal as well as external political activity. This should also seek to provide some guidance to directors on what is legitimate defence of the interests of the company against unwarranted attacks, and what is campaigning. This can be a very grey area.

### **Matters in PWC Forensic Review: mostly late 2002**

4.87 Following the 31 October 2002 annual general meeting, the new AWI Board commissioned a 'forensic review' of a number of AWI transactions. This was done by

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62 Senator Cherry disagrees with paragraphs 4.79 to 4.83, but endorses recommendation 1.

63 Statutory Funding Agreement, clause 1.

64 AFFA, additional information 29 August 2003: AGS advice 5/8/03, p.14.

PricewaterhouseCoopers (PwC) and investigated 28 issues identified by AWI management.<sup>65</sup> The review highlighted the following 'key issues':

- six 'unusual or poorly substantiated payments';
- three payments 'which may be inconsistent with the SFA'; and
- four payments 'regarding projects which were poorly documented, or exhibited weaknesses in standard controls and procedures'.

4.88 Most of these occurred in the second half of 2002, although most only came to public notice in June 2003. PwC's findings were summarised in a letter to AWI shareholders of 5 June 2003, and the actions suggested in the review have been the basis of actions taken by AWI during 2003.

4.89 It should be noted that the PwC report carries a heavy disclaimer. Given the fact that the report has been submitted by AWI at the request of the Committee, and its evidence is referred to in subsequent pages, the Committee believes that it would be prudent to re-produce the disclaimer:

For the purposes of preparing this report, reliance has been placed on the representations, information and instructions provided to us. We have not sought to verify the accuracy or completeness of the information made available to us, nor have we conducted any procedures in the nature of an audit of the information or assumptions therein in any way, other than has been specifically stated in this report.

The report has been prepared subject to the provisions and qualifications stated herein, for the use of Minter Ellison, and its client, Australian Wool Innovation Limited ("AWI"). The firm, its partners, its agents and servants specifically deny any liability whatsoever to any other party who may use or rely on the whole, or any part, of this report or to the parties to who it is addressed for the use, whether in whole or in part, for any other purpose that that herein set out. This report should not be used for any other purpose without the firm's prior written consent.

This report included the results of tests designed to highlight unusual transactions or 'profiles' in data provided to us by AWI. We stress that the transactions and profiles identified in the report are merely the result of our analysis, and are not necessarily indications that fraud or errors have occurred. The testing we perform cannot detect all cases of fraud and nothing in this report is intended to imply this.

This report is prepared based on the information made available to us up to the date of this report and we reserve the right to amend our opinions, if

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65 PricewaterhouseCoopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003.

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necessary, based on factual information that comes to our attention after that date.

Given the nature of AWI's business, the information set out in this report is sensitive and should be treated confidentially and with care.<sup>66</sup>

4.90 AWI's letter to shareholders of 5 June 2003 has been criticised in some evidence to this inquiry as an attempt to defame the first AWI board. For example:

It would appear from the disclaimer that the very people who wrote the report might have concerns with regard to its outcome through not having access to all the information? The review report is not available for release so therefore as shareholders we have to believe the disclosure letter but with many unanswered questions and much doubt about the real facts and the intent of the current AWI Board's actions... What it [AWI] has done is deliberately tried to defame the organisation and the first Board.<sup>67</sup>

4.91 The submission of four former AWI Board members commented:

Perhaps of greater interest to this Committee should be the expenditure of wool growers levies on legal fees and this campaign to discredit [former] directors, including the extraordinary letter to shareholders from Mr McLachlan with a large disclaimer from PwC at its foot, effectively removing them from any inferences he drew. This amounts to a breach of governance on behalf of the current Board and should be investigated. At the very least the full Board should stand for election in November.<sup>68</sup>

4.92 The new AWI Board advised:

Ultimately, the board considered that its duty of disclosure compelled it to release a summary of PwC's major findings. However, it did so in a way that disclosed only issues rather than naming individuals.<sup>69</sup>

4.93 AWI argued that the June 5 letter to shareholders 'not only accurately represents what appears in the PwC report but was expressly approved by PwC before it was sent.'<sup>70</sup>

4.94 At the time the full review was confidential. This Committee has made it public.

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66 Price Waterhouse Coopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.2.

67 Submission 6, Ms M. Gibbins, p.1.

68 Submission 9, Ms M. McCaskill & 3 other former AWI directors, p.7.

<sup>69</sup> Submission 13, AWI, p.13.

70 Submission 13, AWI, p.29.

4.95 PwC matters which were mentioned in evidence to this inquiry are described below.

***Unusual or poorly substantiated payments***

4.96 PwC said: ‘We have identified several examples of payments to directors, employees and vendors which are unusual, have not been properly explained, or are not sufficiently supported by documentation made available to us. The total amount of these payments is approximately \$270,000.’<sup>71</sup>

*Mr Dorber’s ShearExpress directors’ fees (November 2002)*

4.97 PwC reported that Mr Dorber was paid \$24,062.50 as ShearExpress director’s fees on 15 November 2002, although he had earlier told the ShearExpress Board that ‘...his duties as Chairman of ShearExpress fell within his duties as Managing Director of AWI, and accordingly he would not seek remuneration for his position.’ (ShearExpress Board minutes, 10 April 2002). PwC commented and recommended:

The payment of directors fees to Mr Dorber appears to contradict ShearExpress Board Minutes.

Determine what, if any, legal action can be taken for recovery of total Director’s fees of \$24,062.50 paid to Mr Dorber.

Obtain legal advice as to the appropriateness of payment of Directors fees when contrary to employment contract.<sup>72</sup>

4.98 Mr Dorber, in evidence on 26 June 2003, did not believe he had been paid. However in a supplementary submission he acknowledged that he had been paid, acknowledged a ‘moral obligation’ to return the money, and said he had returned it.<sup>73</sup>

*Advance payments of directors’ fees (March 2002)*

4.99 PwC reported that four directors and the Managing Director were each paid \$15,450 on 25 March 2002 as an advance of their directors’ fees for the year 2002-03. PwC commented and recommended:

These payments may be considered as directors’ loans which should have been disclosed in the accounts. AWI auditors have advised they were unaware of the payments, which were not disclosed in the accounts.

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71 Price Waterhouse Coopers, *Australian Wool Innovation Ltd: Forensic review of financial operations, Final Report*, April 2003, p.4.

72 PwC Forensic Review, p.17-18.

73 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.52; submission 16, p.9. AWI’s comments are at submission 13, p.21-22, & submission 17, p.5.



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Obtain legal advice as to whether there is a recovery from the Directors for the advance payment of fees received for 2002/2003, where directors have not served the full term.<sup>74</sup>

4.100 Mr Dorber argued that ‘the payments referred to relates to an FBT rebatable allowance, paid only after the Chief Financial Officer sought and received written advice from PricewaterhouseCoopers about the processes for such payments. It was entirely proper.’ AWI submitted in August 2003 that ‘all other former directors of AWI [other than Mr Dorber and Ms McCaskill] have settled any outstanding debts to the company.’<sup>75</sup>

*Ms McCaskill’s travel costs (October 2002)*

4.101 PwC reported that on 6 October 2002 Ms McCaskill travelled with her son to Shanghai for a Wool and Wool Textile Conference. On 8 January 2003 AWI paid Gentry Travel \$11,777.12 for two return business class tickets. On 25 November 2002 Ms McCaskill received \$5,788.56 by electronic funds transfer from AWI as reimbursement for one business class airfare. PwC commented and recommended:

The payment to Ms McCaskill appears very unusual as it is a direct payment, not an expense reimbursement.

... obtain legal advice as to whether there is a recovery from Ms McCaskill for

- the cost of the business class flight for her son totalling \$5,888.56;
- the \$5,788.56 paid to Ms McCaskill for a reimbursement of the business class airfare which was invoiced and paid by AWI.

Conduct a review of Internal Controls in relation to expense reimbursement.<sup>76</sup>

4.102 Ms McCaskill’s submission did not refer to this matter. The new AWI Board advised that it is ‘continuing to pursue that claim.’ Mr Dorber submitted that ‘any wrongdoing on the part of Mr Dorber is denied.’<sup>77</sup>

*Contract with Mr John Roydhouse (October 2002)*

4.103 This relates to a contract to develop an education program. PwC reported:

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74 PwC Forensic Review, p.17.

75 Mr C. Dorber, *Committee Hansard* 26 June 2003, p. 14. Submission 13, AWI, p. 22. See also Mr Dorber, submission 16, p.10; AWI, submission 17, p.5

76 PwC Forensic Review, p.15.

77 Submission 13, AWI, p.24. Submission 16, Mr C. Dorber, par.40.

- On 11 October 2002 Mr John Roydhouse (Rural IT & Web Pty Ltd) contracted with AWI to develop and implement an education programme. Contract value was \$220,000 (including GST) and \$55,000 was paid on signing.
- P. Comyn, AWI's Program Manager Education and Adoption, wrote in an internal memo (5 February 2003) that 'he was disappointed with the documentation presented by Mr Roydhouse. Project report was meaningless and there was no evidence written or verbal to suggest that work of any substance had been done...'
- Following a review of deliverables by senior management it was agreed to terminate the contract.

#### 4.104 PwC commented and recommended:

Obtain legal advice as to whether there is a recovery of \$55,000 first instalment payment for the education programme.<sup>78</sup>

4.105 This matter should not be confused with an earlier contract with Mr Roydhouse for website design, which was also mentioned in evidence. The website contract was made on 24 September 2002 and was for \$195,076.

#### *Payments to Peter Anderson & Co (September to November 2002)*

4.106 This relates to a June 2002 contract of \$11,000 with Peter Anderson and Co. (PAC) to review the management of Ovine Johne's Disease. PwC reported:

- AWI paid PAC \$11,000 on 18 July 2002. Four further payments totalling \$44,000 were made between September and November 2002.
- On 5 March 2003 Mr Anderson advised PwC that:
  - the additional payments above the original contracted value of \$11,000 were due to the additional time spent in meetings with wool growers and other persons within the wool industry on the OJD issue;
  - on termination of the employment of the former Managing Director he ceased work on the OJD project;
  - he had reported his findings verbally to the former Managing Director.

4.107 PwC commented and recommended:

The payments to Peter Anderson beyond that agreed in contract are poorly substantiated. It is not possible to determine value of services provided as reporting was verbal.

Obtain legal advice as to whether there is any possible recovery for the additional four invoice payments of \$44,000 for the OJD review....<sup>79</sup>

4.108 According to the new AWI Board:

- PAC's lawyers confirmed that the extra payments totalling \$44,000 were made pursuant to a 'verbal agreement';
- PAC's lawyers did not dispute AWI's claim that Mr Anderson had stated that PAC reported verbally to Mr Dorber and was 'not required to document its findings.'
- PAC has refused to reveal details of its work to the current Board.<sup>80</sup>

4.109 Mr Dorber submitted that '...Anderson did receive some payments, but payments were always made on a full disclosure basis, and with the approval of the then Board of AWI.'<sup>81</sup>

*Termination payments to Luke and Holly Dorber (November 2002)*

4.110 PwC reported:

- Luke Dorber, the Managing Director's son, started employment with AWI on 27 August 2001 at a salary of \$47,500. On 3 May 2002 his salary was increased to \$86,000. On 25 November 2002 he received a termination payment of \$94,649.18 gross (\$64,031.66 net of tax).
- Holly Dorber, the Managing Director's daughter, started employment with AWI on 11 March 2002, part time. From 1 July 2002 her salary was increased to \$35,000 since she would work full time to 3 September 2002 and then revert to three days a week. On the payroll records she was always classified as a casual employee. On 25 November 2002 she received a termination payment of \$37,989.17 gross (\$25,704.96 net of tax).

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79 PwC Forensic Review, p.21-2.

80 Submission 13, AWI, par.5.58. Similarly Submission 17, AWI, p.6.

81 Submission 16, Mr C. Dorber, p.14. See also Mr C. Dorber, *Committee Hansard* 26 June 2003, p.5; AWI, submission 17, p.6.

#### 4.111 PwC commented and recommended:

The termination payments to Luke and Holly Dorber appear unusually high in reference to their employment periods....

Obtain legal advice as to whether any action lies for recovery of termination payments.

Conduct a review of internal controls in relation to approval and payment of termination payments, salary increases, bonuses and other employee entitlements.<sup>82</sup>

4.112 Mr Dorber advised that he terminated Luke and Holly Dorber because of his fear that they would be discriminated against under new management; he was advised that an industrial commission would regard the terminations as unfair and might award the maximum available amount of six months salary; and he regarded a termination payment of 12 months salary as reasonable as ‘a payment for unfair dismissal and a payment for discrimination.’<sup>83</sup>

#### 4.113 The new AWI Board commented:

While the new board discussed the matter with Mr Dorber at its first meeting [November 2002] and expressed the view that it is an unwise practice to employ one’s relatives in a public company, it advised him no decision was being taken as to his children’s continued employment with AWI. Notwithstanding this advice, Mr Dorber unilaterally took the decision to retrench his own son and daughter .... the level of the termination payments made to each of his children was excessive.<sup>84</sup>

4.114 In the case of Holly Dorber, AWI noted that at the time of her termination she was working casually two days per week and due to finish in December 2002.<sup>85</sup>

#### 4.115 Mr Campbell of WoolProducers commented on the redundancy payments:

It takes rather a lot to set me back on my heels. Given that so many of our constituents are in drought, have debt and are still obliged to meet their compulsory two per cent levy payments, I am absolutely horrified.<sup>86</sup>

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82 PwC Forensic Review, p.28-29.

83 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.41.

84 Submission 13, AWI, par.5.36.

85 Submission 13, AWI, p.23; submission 17, AWI, p.5.

86 Mr S. Campbell (WoolProducers), *Committee Hansard* 28 August 2003, p.52.

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***Payments which may be inconsistent with the SFA***

4.116 PwC said: ‘There are several examples of payments made by AWI which may be inconsistent with the Statutory Funding Agreement.’<sup>87</sup> (This would be because they are not among the eligible categories of expenditure noted in clause 5 and schedule 4 of the Statutory Funding Agreement.)

*Donations and sponsorships*

4.117 PwC noted donations and sponsorships of \$9,360 to the NSW Sports Council for the Disabled for 104 children and carers to attend ‘Movie Mania’ (November 2002); \$100,000 to Charles Sturt University towards the establishment of a museum to house the Somerville fossil and rock collection (September 2002); \$251,931.07 to the Royal Society of Arts to fund Student Design Awards (November 2001 and December 2002); and \$4,033.20 worth of books to Cromer High School (first half of 2002). PwC recommended that AWI obtain legal advice as to whether the use of funds was consistent with section 5 of the Statutory Funding Agreement.

4.118 The Cromer High School books were Shakespearian plays.<sup>88</sup>

4.119 Mr Dorber defended these payments in several ways:

- The activity, properly viewed in context, was within the terms of the SFA relating to wool innovation (Charles Sturt University: ‘the project involved a major program in wool education’; Royal Society of the Arts: ‘these payments relate to use of innovative wool (Australian content).’)<sup>89</sup>
- The payment related to ‘corporate citizenship’ and ‘creating the identity of AWI within the community’ (NSW Sports Council for the Disabled).<sup>90</sup>
- No breach of the SFA occurred because payment was from the non-government component of AWI funds: ‘No claim was (or would have) been submitted for matching Commonwealth Funds for this expenditure.’ (NSW Sports Council for the Disabled)<sup>91</sup>

4.120 The Committee considers that Mr Dorber’s claims in relation to this expenditure stretch the bounds of credibility.

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87 PwC Forensic Review, p.5.

88 Submission 13, AWI, p.16.

89 Submission 5, Mr C. Dorber, p.15.

90 Submission 17, Mr C. Dorber, p.4.

91 Submission 5, Mr C. Dorber, p.15.

4.121 In relation to Cromer High School, Mr Dorber referred to a 'pilot wool education program':

An agreement was reached that a donation would be made to the Cromer Campus for use as determined by the school in return for the direct participation by the campus in the development of the pilot program.<sup>92</sup>

4.122 The new AWI Board advised that 'there is no evidence in AWI's records of any agreement of the nature described by Mr Dorber.'<sup>93</sup>

#### *Payments relating to the 2002 Board election*

4.123 PwC reported that payments totalling \$13,003.85 were made to i2K Communications in October and November 2002. AWI staff indicated to PwC that there is no evidence of the substance of the work performed. PwC commented and recommended:

i2K work product identified by PricewaterhouseCoopers may be two advertisements disparaging the election of 'shareholders candidates'. No other work product identified by PricewaterhouseCoopers or AWI staff.

Obtain legal advice as to whether the use of funds to assist with the campaign for the reelection of the board is inconsistent with section 5 of the Statutory Funding Agreement - Applications of Funds, noting that the stated use of funds was also to improve exposure of AWI issues.<sup>94</sup>

#### *Project management issues*

4.124 PwC identified a number of examples of payments to employees, consultants and contractors regarding projects which were 'poorly documented, or exhibited weaknesses in standard controls and procedures.'<sup>95</sup>

#### *Advance of \$550,000 for a film (June 2002)*

4.125 PwC reported that \$550,000 was paid to Line Communications as a 50 per cent upfront payment for a film to promote the Australian wool industry. PwC recommended: 'Review advance payment policy.'<sup>96</sup>

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92 Submission 17, Mr C. Dorber, p.4.

93 Submission 17, AWI, p.3.

94 PwC Forensic Review, p.10-11.

95 PwC Forensic Review, p.5.

96 PwC Forensic Review, p.20.

4.126 The new AWI Board commented: ‘...the issue of concern to the new board was that the contractor, a sole trader without any material asset backing, had been advanced \$500,000 of the contract amount upon execution of the contract without any form of security over that sum to protect AWI.’<sup>97</sup>

4.127 Mr Dorber commented: ‘This payment was made against a formal contract after a tender process. The nature of the payment for work of this kind is standard practice for the type of work.’<sup>98</sup>

*Advance to European Wool Awards (April and June 2002)*

4.128 PwC reported that payments totalling \$404,560.41 were made to Interlaine in April and June 2002 as an advance of 50% of the payment for the 2002/2003 European Wool Awards. PwC recommended:

Conduct a review of the advance payment policy.

Conduct a review of the performance of Interlaine.

Conduct further investigations concerning the agreement with Interlaine.

Conduct a review of the sponsorship policy.<sup>99</sup>

*Payment of bonuses to senior staff (November 2002)*

4.129 PwC reported that bonuses totalling \$228,000 net of tax were paid to seven senior AWI staff on 25 November 2002. Four other staff were each paid \$10,000 net of tax during November. PwC commented and recommended:

Conduct further investigations including review of staff appraisals; interviews with AWI staff to ascertain bonus criteria.

Bonus payments should be referred to a remuneration committee for approval.

Conduct a review of internal controls in relation to approval and payment of bonuses.<sup>100</sup>

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97 Submission 13, AWI, p.18. See also submission 16, Mr C. Dorber, p.22; submission 17, AWI, p.7.

98 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.16.

99 PwC Forensic Review, p.23-4.

100 PwC Forensic Review, p.26.

4.130 The new AWI Board said that the payments were made without reference to the Chair or the Board, and this was one of the issues which caused the majority of the Board to lose confidence in the managing director.<sup>101</sup>

4.131 Mr Dorber argued that ‘all payments comply with a Board approved policy and were within the published delegation to the MD. No impropriety of any kind occurred....’<sup>102</sup>

### **Farmhand donation, October 2002**

4.132 In October 2002 AWI paid \$500,000 to the Australian Red Cross’s Farmhand drought relief appeal. This became controversial in the leadup to the October 2002 AWI annual general meeting. AFFA and the Minister wrote to AWI in October and November seeking confirmation that the payment was consistent with the SFA. The Red Cross later refunded the money when it became clear that it could not accept conditions which AWI would have to impose if the payment was to be allowable under the Statutory Funding Agreement.<sup>103</sup>

4.133 WoolProducers claimed that ‘it is widely believed that the intent of this donation was to influence the public perception of the McCaskill Board in the minds of drought-affected woolgrower shareholders who would be deciding on their choice of AWI Directors.’<sup>104</sup>

4.134 Mr Dorber admitted that it was ‘poor judgment’ to make the donation before formal agreement on the conditions, but he denied that the payment was a breach of the SFA: firstly because ‘the Farmhand grant was conditional upon specific requirements that were consistent with AWI goals’; secondly, for the same reason as that noted above in relation to the NSW Sports Council for the Disabled, viz: ‘In order to breach the SFA a claim for funds must have been made in accordance with schedule 1, paragraph 2 of the SFA. No claim had been made and no request for reimbursement to the Commonwealth had been submitted.’<sup>105</sup>

4.135 The Committee comments on the second point at paragraph 4.136.

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101 AWI, *Committee Hansard* 28 August 2003, p.88.

102 Submission 5, Mr C. Dorber, p.14.

103 Mr D. Banfield (AFFA), Senate RRAT Legislation Committee, consideration of Budget Estimates, supplementary hearing, 20 November 2002, p.49. Mr C. Dorber, *Committee Hansard* 26 June 2003, pp.53-54. Submission 5, Mr C. Dorber, p.3.

104 Submission 1, WoolProducers, p.18.

105 Submission 16, Mr C. Dorber, pp.7-8.



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## Comment

### *Whether AWI may spend Wool Levy money freely*

4.136 At several points Mr Dorber argued that no breach of the SFA can occur unless reimbursement is sought under the Commonwealth Matching Funds provision. For example, see paragraph 4.119 above in relation to the donation to the NSW Sports Council for the Disabled, and paragraph 4.134 in relation to the Farmhand donation. Similarly:

As the statutory funding agreement requires the retrospective payment of moneys spent on RDI, it is physically impossible, even if that [Farmhand] payment had gone ahead, for there to be a breach of the statutory funding agreement unless a claim had been made to the Commonwealth for matching funds. No breach occurred.<sup>106</sup>

4.137 This would mean in effect that AWI could spend Wool Levy money with complete freedom. This is the implication of Mr Dorber's statement, for example: 'We even had some informal discussions with government about ending the Commonwealth matching grants because of our belief that the wool industry wanted freedom from the government forever.'<sup>107</sup>

4.138 The Committee agrees with the new AWI Board that this is untenable.<sup>108</sup> The SFA is clear in its terms. Wool Levy money may be spent only as shown in clause 5; Commonwealth Matching Funds may be spent only as shown in schedule 4. Whether a particular activity at the margin satisfies these tests may be a matter of opinion; but it is undeniable that the tests must be applied.

4.139 To suggest that AWI may spend in any way it likes, providing it does not seek reimbursement under the Commonwealth Matching Funds provision, ignores the fact that the money AWI spends in this way is mostly Wool Levy money (since the Wool Levy is three quarters of AWI's income).

4.140 The accountability obligations apply to Wool Levy money just as much as to Commonwealth Matching Funds because the Wool Levy is compulsory: exacted by law and appropriated by Parliament.

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106 Mr C. Dorber, submission 5, p.15; submission 16, p.7-8; *Committee Hansard* 26 June 2003, p.53.

107 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.31. Similarly p.22: 'The statutory funding agreement deals particularly with the Commonwealth's matching funds... Its primary interest is in guarding the Commonwealth's interest in making sure that the Commonwealth's share of the money is spent only on the matters listed in schedule 4.'

108 Submission 13, AWI, p.16.

4.141 As a related matter the Committee notes Mr Dorber's statement in the rural press in March 2002:

Also the [Woodlot] program was not grower funded but government funded, he said. AWI receives a federal R&D contribution of \$13million and, in line with the Government's increasing emphasis on natural resource management, AWI will continue to direct as much of that funding component as possible towards resource management and sustainability development, he said.<sup>109</sup>

4.142 Here the idea seems to be that AWI may spend 'government money' (Commonwealth Matching Funds) in any way that is consistent with government policy. This also is obviously untenable as it is clearly contradicted by the restrictions in schedule 4 of the SFA.

4.143 The Committee finds it extraordinary and irresponsible that the former Managing Director of AWI could have held these perverse views of the SFA for nearly two years without either the AWI Board or AFFA seeking to clarify the matter.

***Whether AWI may spend its independent income freely***

4.144 Mr Dorber suggested that AWI is free to spend as it likes providing it uses its independent income (\$5 million in 2002-03):

But it [AWI] could spend money on agri-political activity, provided that was not either Commonwealth money or levy funds. For example, a board of the company could spend the \$24 million of funds that I negotiated from the sale of the properties in any way that corporate law permitted it to, without referral to this agreement or to the Commonwealth.<sup>110</sup>

4.145 It is true that the SFA only controls 'the Funds' (Wool Levy and Commonwealth Matching Funds). However, to argue that AWI may spend independent income as it likes disregards the objects of the company as shown in its constitution, which are essentially the same as the objects shown in clause 5 of the SFA.

4.146 Furthermore, in the Committee's view it is wrong to pretend that other source income can be quarantined in this way. Excluding the Commonwealth Matching Funds, AWI's income is over 90 per cent sourced from the Wool Levy. All expenditure that is not to be claimed from the Commonwealth Matching Funds should therefore be regarded as 90 per cent funded by the Wool Levy, and accordingly all should conform to the requirements of the SFA.

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109 *Dorber challenges survey but changes imminent*, The Land, 14 March 2002.

110 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.23.

4.147 In any case, independent income from interest and royalties is a return on investment funded by woolgrowers. If it is not to be given back to woolgrowers as a dividend, it should be reinvested under the same conditions, for the benefit of woolgrowers, as shown in the SFA.

4.148 In the Committee's view a levy-funded body like AWI should not be allowed to spend *any* money, however sourced, on agri-political activity.

4.149 The SFA, to avoid doubt on this point, should have a condition that *all* the company's expenditure (not only the expenditure of 'the Funds') should be controlled by the SFA.

## **Recommendation 2**

**The Statutory Funding Agreement should have a condition that all the company's expenditure (not only the expenditure of 'the Funds') should be controlled by the Statutory Funding Agreement.**

### ***Whether AWI may spend 'for the benefit of woolgrowers' generally***

4.150 At times Mr Dorber seemed to imply that to satisfy the Statutory Funding Agreement it is enough that the expenditure is for the benefit of woolgrowers. For example:

The referenced payments with respect to Cromer High School and the NSW Sports Council for the Disabled (and indeed a payment to the Bathurst Museum, care of Charles Sturt University) were for the benefit of Australian wool growers. Mr Dorber concurs with the opinion of the Board that the SFA requires that payments must be spent efficiently, effectively and ethically and the for the benefit of Australian woolgrowers and maintains that the reference payments were in accordance with the SFA.<sup>111</sup>

4.151 In fact it is necessary but not sufficient that expenditure be for the benefit of Australian woolgrowers. Expenditure must be for the benefit of Australian woolgrowers *and* must satisfy of the categories of clause 5.1 or schedule 4 of the SFA.

### ***Whether AWI may spend on 'corporate citizenship'***

4.152 Mr Dorber justified a donation to the NSW Sports Council for the disabled on the grounds that it related to 'corporate citizenship' and 'creating the identity of AWI within the community' (NSW Sports Council for the Disabled).<sup>112</sup>

4.153 The issue is similar to that above. However beneficial it may be to 'create the identity of AWI within the community', expenditure is not allowed unless it satisfies

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111 Submission 17, Mr C. Dorber, p.4-5.

112 Submission 17, Mr C. Dorber, p.4.

one of the categories of clause 5.1 or schedule 4. The Australian Government Solicitor commented:

There is no basis in the SFA to support the making of any donations by AWI or members of the Board on behalf of AWI unless the application of the Funds would be in relation to the purposes otherwise set out in clause 5.1 of the SFA.<sup>113</sup>

***Comment on AWI's management during the period***

4.154 On the weight of evidence the Committee is satisfied that concerns about AWI management and corporate governance, especially in the second half of 2002, were justified. The examples, especially in the second half of 2002, show a pattern of behaviour not consistent with good corporate governance.

4.155 In reaching this conclusion the Committee is most influenced by:

- the conduct of AWI in relation to the 2002 election of directors;
- the cumulative impact of the matters in the PwC forensic review; in particular, matters such as the Roydhouse contract, the Anderson contract, and the Luke and Holly Dorber termination payments;
- the Board's behaviour in the Vizard/Murphy election matter;
- the failure to apply project evaluation methodology completely or consistently.

4.156 Some of these matters concern possible breaches of the SFA and/or the Corporations Law. More of them concern behaviour which does not involve breaches of the SFA, but is arguably inappropriate in other ways. For example, the Anderson contract matter (see paragraph 4.106) does not show any breach of the SFA (since the subject Ovine Johne's Disease is related to wool research); but to spend \$44,000 on a verbal contract to provide verbal reports (the wisdom of which is now lost to the company with the departure of the former Managing Director) is arguably not a prudent use of the company's money.

4.157 In the Committee's view AFFA, in supervising AWI and similar bodies, ought to be concerned not only with possible breaches of the SFA narrowly viewed, but also with possible failings of corporate governance more broadly. AFFA's 2002 *Review of Corporate Governance of Portfolio Bodies* supports this view when it says:

In a pragmatic, political environment, the Minister/Parliamentary Secretary may be called upon to answer for the actions of the company:

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113 AFFA, additional information 29 August 2003, AGS advice 5 August 2003, p.22.

- if it does not achieve the public interest purposes underlying the Government's motivation in promoting its establishment;
- if it fails to comply with the terms of its contractual obligations to the Commonwealth;
- if it misappropriates or fails to secure value for money in its use of funds provided by the Commonwealth;
- if its internal corporate governance is less than required....<sup>114</sup>

4.158 Despite Mr Dorber's three written submissions and extensive verbal evidence the Committee believes that WoolProducers were entirely justified in their continuing concerns about the way in which AWI was being administered.<sup>115</sup>

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114 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.44-45.

115 Senator Cherry disagrees with paragraphs 4.154 to 4.158 and has provided supplementary comments.



## CHAPTER FIVE

### AFFA's Oversight of AWI in 2001 and 2002

5.1 This chapter describes how AFFA supervised AWI in 2001 and 2002. It describes how AFFA and the Minister dealt with complaints about AWI from a grower group (WoolProducers) and a former AWI Board Member (Professor Andrew Vizard). The question is whether AFFA acted on concerns about AWI in a timely way, and what if anything AFFA could reasonably have done to avoid the problems that arose.

#### Development of AFFA's oversight of AWI

5.2 A core issue for AFFA's oversight of the SFA is clause 5: the Funds are to be used only as allowed by the agreement. Mr Dorber told the Committee that to show this he had focussed on giving AFFA as much information as possible:

AWI unilaterally introduced a system whereby we took schedule 4 of the statutory funding agreement and we itemised every dollar spent, line by line, against each of the sections of section [schedule] 4... We then sent that spreadsheet, which ran to hundreds of pages, to the Commonwealth, with a certificate signed by me saying that the moneys had been spent in accordance with the statutory funding agreement and defining every expenditure item.<sup>1</sup>

5.3 Mr Dorber said that this arrangement was altered at AFFA's request:

That happened for some months and then the Commonwealth said, 'What we want from you is a single piece of paper—a certificate—signed by the managing director, certifying truthfully that the retrospective claim for matching capped funding has been spent in accordance with the statutory funding agreement.'<sup>2</sup>

It was a massive amount of information, they did not have the resources to check it and their attitude was, 'You're a corporate entity; it's your responsibility.'<sup>3</sup>

5.4 The new AWI Board advised that 'internal inquiries have not revealed that AWI has any documents relating to a request by AFFA for AWI to reduce the amount of information provided in satisfaction of its reporting obligations under the SFA.'<sup>4</sup>

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1 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.24.

2 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.24.

3 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.28.

5.5 On AFFA's approach to oversight generally, Mr Dorber said:

The key message consistently returned to AWI by the department was—and I might add this was said to my face by Minister Truss—that the government had stepped away from the day to day management of this business and that what the government sought was for the wool industry get on with the game and do what it was required to do.<sup>5</sup>

5.6 AFFA described its 'three level' approach to oversight: the strategic plan, the operating plan and the government's research priorities.

There is a higher level strategic plan—typically a five-year strategic plan—which provides the big picture, and then there is the annual operating plan... the third [element] was actually the research priorities. You have an operating plan, but it is not something that is prepared in a vacuum; it is built around and linked to the government's articulated research priorities.<sup>6</sup>

5.7 AFFA argued that if these are correctly in place government should not need to be involved in assessing individual projects:

The planning and reporting interests that the department has are very different from the project assessment methodology that you have just alluded to, which are matters for the company itself to develop and apply. We would not normally, by any stretch of the imagination, be involved in that level of project assessment.<sup>7</sup>

5.8 An exchange of correspondence in late 2001, in context of negotiations over the strategic plan, alluded to the general working relationship between AFFA and AWI. It appears that Mr Dorber thought AFFA's accountability requirements went beyond an appropriate level of scrutiny:

**AFFA to AWI, 17 October 2001**

...The expected standards for planning, setting objectives and reporting against them remain the same as those required of the statutory authorities.

**AWI to AFFA, 14 November 2001**

...In your letter [of 17 October 2001] you also refer to the establishment of AWI as a Corporations Law Company. Your statement 'However, despite these changes in the ownership structure, the essential elements of accountability and transparency in the application of statutory levies, which

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4 Submission 13, AWI, p.2.

5 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.18.

6 Dr C. Samson (AFFA), *Committee Hansard* 23 June 2003, p.16.

7 Dr C. Samson (AFFA), *Committee Hansard* 23 June 2003, p.16.



largely fund AWI's activities to the Minister of the day, **remain unchanged**. The expected standards for planning, setting objectives and reporting against them **remain the same as those required of the statutory authorities**.' (bold emphasis is mine).

These statements are crucial to AWI's interpretation of its responsibilities to Government. Whilst AWI management is committed to a very strong relationship, I must record that the words I have highlighted are significantly at odds with the instructions I have received from both the AWI Board and the AWS Board. In particular, the Chairman of the AWS Board, Mr Rodney Price and the legal and other consultants engaged in the formal negotiations with Government for the establishment of AWS and its related entities, have emphatically and repeatedly emphasised the direct accountability of AWI to its shareholders, and the significant differentiation in the role it is now engaged upon, in respect of research development and innovation, when measured against the delivery of that role as a former Statutory Corporation of Government.<sup>8</sup>

#### **AFFA to AWI, 5 February 2002**

... As a Commonwealth Department AFFA is accountable, through the Minister, to the Parliament for expenditure of monies appropriated by Parliament. Monies raised through the wool levy and the additional monies paid as matching R&D funds fall into this category. Accordingly they are subject to the same level of scrutiny and accountability as other public monies and to do so effectively with respect to private companies, AFFA has contractual relationships with them requiring robust, performance-oriented planning and reporting systems to be in place so that we can collectively respond to the needs of the Minister, particularly in regard to his Parliamentary obligations.<sup>9</sup>

5.9 AFFA's efforts to obtain a satisfactory AWI strategic plan are described in chapter 3. As to concerns about management at this time, AFFA commented:

**Mr Taylor**—...What we were looking at the beginning of 2002 was certainly reputable people on the board and reputable processes but a need in our view to improve the consultation with respect to the strategic and operational planning framework. We certainly saw that they had processes in place for the proper keeping of accounts and the proper preparation of financial information. So there was no reason to suggest in any shape or form that, in terms of the management of funds, they had other than proper procedures in place.

**Dr Samson**—...we were working virtually continuously with AWI to ensure that, from what was admittedly a fairly low base, we were satisfied

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8 AFFA, additional information 29 August 2003: letter AWI-AFFA 14/11/2001, pp.6-8.

9 AFFA, additional information 29 August 2003: letter AFFA-AWI 5/2/2002, pp.1-2.

that there was ongoing improvement in their planning and reporting regime.<sup>10</sup>

### **Comment**

5.10 The Committee agrees with AFFA that AFFA, through the Minister, is accountable to Parliament for the expenditure of not only Commonwealth Matching Funds (which are direct grant for R&D) but also Wool Levy Funds. This is because the levy on growers is compulsory - a compulsion which only government can enforce. The privatised structure aims to make it most likely that the money will be well spent according to the industry's needs; but as long as government wishes to enforce the levy, government cannot escape final responsibility for the outcome. The Committee notes with concern Mr Dorber's evidence noted at paragraph 5.5 that the Minister, Mr Truss, suggested a lower standard of accountability.<sup>11</sup>

### **AFFA oversight of AWI audit reports**

5.11 The SFA provides that 'the Company ... must give the Commonwealth a copy of its audited financial report for the year at the same time as the Corporations Law requires it to be given to members' (clause 22.1). AFFA advised that AWI provided its audited financial statements to June 2001, and for 2001/2002, and these disclosed no cause for concern about possible non-compliance with the SFA.<sup>12</sup>

5.12 Clause 22.2 of the SFA also requires AWI to obtain, as part of the financial audit, a report on 'the Company's compliance with its obligations under this Agreement in relation to the Funds'. AWI did not do this for the years ending 30 June 2001 and 30 June 2002.

5.13 In relation to the 2000/2001 year, AFFA said that 'AWI had only been operational for about 3 months ... Due to the comparative short term of operation the Department did not pursue a compliance statement.'<sup>13</sup>

5.14 In relation to the 2001/2002 year, Mr Dorber, when asked about the missing clause 22.2 report, said:

I understand from the auditors that the writing of the annual report and that component of it was exclusively their responsibility.... The only people who

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10 Mr M. Taylor & Dr C. Samson (AFFA), *Committee Hansard* 17 September 2003, p.118.

11 Mr C. Dorber, *Committee Hansard*, 26 June 2003, p.18.

12 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.118.

13 AFFA, additional information 29 August 2003: answers to questions, pp.7-8.

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could tell you why the precise words are not published there are the auditors themselves. What I can tell you is that the compliance did take place.<sup>14</sup>

#### 5.15 AWI advised:

The board understands that the auditors met with Mr Dorber and AWI's Chief Financial Officer to discuss this in the context of the statutory audit. PwC has advised the new board that Mr Dorber requested that the auditors only conduct the statutory audit.<sup>15</sup>

5.16 AFFA explained that the clause 22.2 compliance report for 2001/2002 would properly have appeared in the annual report which AFFA received only after the 31 October 2002 annual general meeting. AWI did provide certain additional information pursuant to schedule 3 of the SFA (matters which the annual report should cover) on 29 August 2002. AFFA advised that in the covering letter to this information:

The former Managing Director noted that it had established an internal audit committee in 2001 and in relation to an internal audit report 'Although not a formal requirement of the statutory funding agreement AWI will supply you with a copy of the internal report in due course.' ... The internal report mentioned in the letter was not provided.<sup>16</sup>

5.17 AFFA advised that it did not follow up the lack of a clause 22.2 compliance report with AWI immediately after the 31 October 2002 AGM, because:

With a new board and management team in place and clear signals from the new AWI Board that it was taking a serious look at its reporting and corporate governance obligations, the specific matter of the missing SFA compliance audit statement was not pursued at that time.<sup>17</sup>

5.18 As to whether the SFA compliance audit would in any case have helped avoid 'alleged irregularities' in the second half of 2002, the Australian Government Solicitor, in advice to AFFA, commented:

We note that a number of the alleged contraventions of the SFA occurred after June 2002. To the extent that this was true they would not have been addressed in the audited financial report for the financial year 2001/02.<sup>18</sup>

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14 Mr C. Dorber, *Committee Hansard* 26 June 2003, p.18.

15 Submission, 13, AWI, p.30.

16 AFFA, additional information 29 August 2003: answers to questions, p.8.

17 AFFA, additional information 29 August 2003: answers to questions, p.7-8.

18 AFFA, additional information 29 August 2003: AGS advice 5/8/03, p.32.

5.19 In April 2003 AWI obtained a ‘forensic review’ of past financial operations, as described in chapter 4. In May 2003 AWI produced a ‘Review of Performance’ as required by clause 20 of the SFA (AWI must procure a Performance Review Report and make it available to levy payers before a Wool Poll). In November 2003 AWI obtained the clause 22.2 compliance report for the 2002/2003 financial year (details are in chapter 6). AWI advised that it does not propose to obtain a clause 22.2 report retrospectively for the 2001/2002 year.<sup>19</sup>

### **Concerns of WoolProducers, February 2002**

5.20 WoolProducers became concerned about AWI’s management in late 2001 and early 2002. WoolProducers wrote to the Minister on 4 February 2002 (details are in chapter 4). AFFA described its action on this:

- 11 February 2002: Minister’s office asked AFFA for an urgent brief. Briefing prepared for a possible meeting between the Minister and WoolProducers on 13 February. Minister’s office advised that the meeting scheduled for 13 February had been postponed.
- 1 March 2002: Final briefing was provided to the Minister.<sup>20</sup>

5.21 In this briefing AFFA advised:

Given its business relationship with AWI, it is neither practical, nor indeed appropriate for the Government to seek to influence AWI’s expenditure on a project-by-project basis. While projects undertaken by AWI are required by the Government to come within the Company’s charter, there may well be examples where individual projects do not have 100% industry support. In these instances, it is not the role of Government to be drawn into this debate. Rather, if woolgrowers have concerns, they are able to exercise their rights as shareholders of the company under the Corporations Law.

That said, the Government is of course aware of the need for statutory funds to be applied properly and accounted for. The Statutory Funding Agreement provides appropriate accountability measures....

5.22 AFFA’s view was that the matters noted in WoolProducers’ letter were not breaches of the SFA.<sup>21</sup>

5.23 Mr Campbell of WoolProducers said: ‘We received no formal reply from Mr Truss’s office on any of the matters that were raised. There were informal discussions,

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19 Submission 13, AWI, p.30.

20 AFFA, additional information 8 October 2003: answers to questions, p.1.

21 AFFA, additional information 8 October 2003, p.2.

which tended to centre on: the wool industry should go in there itself and solve the problems.<sup>22</sup>

5.24 On 19 June 2002 WoolProducers met with AFFA officials and the Minister. Mr Campbell recalled:

**Mr Campbell**—...We expressed our concerns. We had verbal assurances that, really, it was a semiprivatised company and that the wool industry would have to go and solve these problems....

**Senator O'BRIEN**—What did the minister actually say at the meeting?

**Mr Campbell**—I would return to what I said. He has tended to say in regard to the AWI problem that the wool industry has to go and solve it. By which he meant: it is a semiprivatised company—for instance, why don't you stand directors or not elect directors, as the case may be?<sup>23</sup>

5.25 In evidence to this inquiry AFFA repeated its view that WoolProducers' concerns at that time were really more a disagreement about project priorities and management style - matters which, AFFA argued, AWI should resolve internally. They did not disclose breaches of the SFA which AFFA could have acted on.<sup>24</sup>

5.26 AFFA stressed that through this period it was active in obtaining a satisfactory AWI strategic plan (details are in chapter 3):

The Department was aware of some concerns within industry about several matters, particularly the management style of AWI, selection of projects for funding also the perceived lack of progress being made in the development of its strategic and operating plans. As indicated previously, the Department was actively engaged with AWI on planning and reporting and the management style and the selection of projects are matters for the company board.<sup>25</sup>

5.27 AFFA stressed that the questionable matters raised in the 2003 PwC Forensic Review occurred later (from September 2002), and only became known when AFFA obtained PwC's review in June 2003. AFFA argued that on the one previous occasion when there was serious doubt about whether a project was allowable - the Farmhand

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22 Mr S. Campbell (WoolProducers), *Committee Hansard* 28 August 2003, p.44.

23 Mr S. Campbell (WoolProducers), *Committee Hansard* 28 August 2003, p.44.

24 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.119ff.

25 AFFA, additional information 8 October 2003, p.2.

donation, October 2002 - AFFA acted promptly by writing to AWI seeking assurances that the donation met the requirements of the SFA.<sup>26</sup>

## Concerns of Professor Vizard

5.28 Professor Vizard, then a director of AWI, raised concerns about AWI with Mr Taylor, the secretary of AFFA, on 22 February 2002. Mr Taylor recalled:

I had certainly had earlier discussions with Dr Vizard in which he had indicated that he was unhappy personally with the way in which the CEO operated.... But I think importantly, Senator, I did not have—nor did he convey to me—anything of substance that I could have taken action on.... We had no evidence, and no-one provided us any evidence, to indicate anything that would require legal action. Nor did any of my discussions with Dr Vizard before his resignation indicate that.<sup>27</sup>

5.29 Professor Vizard resigned as a director of AWI on 14 June 2002. In his letter of resignation to the Chair he mentioned three particular matters:

- ‘The recent review of the Managing Director’s performance was conducted in the absence of any normal measures of performance... an operating environment at the board level in which constructive criticism of performance was, in the end, aggressively discouraged.’
- ‘The decision of the board to reject a process to correct a clear potential serious error in the mechanics of the last AWS Annual General Meeting...[concerning the election of Directors Vizard and Murphy, discussed in chapter 4]
- ‘Following the resignation of Mr Patten from AWI, the board of AWI had no opportunity to submit a collective view on the mix of board skills and experience necessary...’<sup>28</sup>

5.30 Professor Vizard asked for this letter to be confidential, and knowledge of it became public only in October 2002 when it was leaked to the rural press.<sup>29</sup> However in June Professor Vizard gave an interview to the Weekly Times which, as published, dealt with the second and third of the points above (but not the first), and other concerns which he held:

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26 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.116ff. AFFA, additional information 8 October 2003, p.3.

27 AFFA, additional information 8 October 2003, attachment 1. Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.114.

28 Prof. A. Vizard, *Committee Hansard* 28 August 2003, p.56.

29 *Can of Worms*, The Weekly Times, 16 October 2002, p.1.

- lack of investment by AWI in genetic research;
- lack of discussion at board level on controversial projects such as forestry and revegetation;
- decisions to spend money on marketing initiatives such as fashion parades and assisting wool mills with promotion; the concern being that it was uncertain whether these fell within AWI's strategic guidelines.<sup>30</sup>

5.31 The question arises whether Professor Vizard's concerns and his subsequent resignation, in context, should have aroused more concern in AFFA. The Committee questioned Mr Taylor on this matter:

**Senator FERRIS**—Dr Vizard clearly raised with you some issues that were of great concern to him at the time. He subsequently resigned. Did it not occur to you that he had resigned based on concerns that must have developed further from the conversation he had with you? Did you think to give him a call to discuss those?

**Mr Taylor**—I would have thought Dr Vizard, given the Corporations Act, rather than responding to me would have responded to the Australian Securities and Investments Commission. That is the appropriate body if you have any concerns in terms of governance for a Corporations Law company.<sup>31</sup>

## Comment

5.32 The Committee notes AFFA's argument that complaints about AWI in the first half of 2002 were more about project priorities and management style than breaches of the SFA; and that project priorities and management style were a matter for AWI to resolve internally. AFFA argued that the more serious concerns raised in the second half of 2002 would in any case not have been revealed by auditing until the end of the 2002/03 financial year. However it is clear that WoolProducers' concerns reflected a wider range of issues including performance measurement and the involvement of the Board (see paragraph 4.2).

5.33 The Committee acknowledges AFFA's considerable efforts during 2001 to obtain a satisfactory AWI strategic plan. Nevertheless, it is unfortunate in retrospect that AFFA did not act more energetically on the particular concerns about AWI management which began to be raised from February 2002. Given the newness of the hybrid public/private model under which AWI was operating, AFFA should have acted more energetically in establishing clearer lines of accountability, reporting and consultation. In particular, if AFFA reasonably believed that there might be a breach

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30 *Vizard tells: why I quit*, The Weekly Times, 26 June 2002, p.1,4. Submission 1, WoolProducers, attachment U.

31 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.114.

of the SFA, it did not need to wait for a regular audit, but had the right to demand an additional audit report or opinion at any time at AWI's expense.<sup>32</sup>

5.34 There had already been warning bells: firstly, the problems over the strategic plan; secondly AWI's letter of 14 November 2001 which said: '...the words I have highlighted [to do with AFFA's understanding of AWI's accountability obligations] are significantly at odds with the instructions I have received from both the AWI Board and the AWS Board.' This suggested strongly that problems with AWI might not be merely the teething problems of a new organisation, but appeared to reflect a fundamental disagreement about what the accountability obligations should mean. This needed to be sorted out.

5.35 As well, the very fact that there could be such serious disagreement about whether particular projects met the definitions of allowable activities should have suggested that some clarification of the definitions would be desirable.

5.36 The Committee believes that AFFA failed to properly pursue the issue of AWI's understanding of and compliance with the SFA given the fundamental difference between it and the AWI Managing Director as to what the company's accountability obligations actually were.

### **Recommendation 3**

**The Minister should direct AFFA to pursue compliance and other reports pursuant to all Statutory Funding Agreements.**

#### ***Need for orderly risk management***

5.37 The policy goal in establishing companies like AWI to replace statutory authorities is that the body should be more responsive to its industry and, correspondingly, that the government should take a 'hands-off' role in its detailed affairs. Yet, because the levy which funds the company is compulsory, the government cannot escape ultimate responsibility for how well the money is spent.

5.38 In this situation, the essence of the 'hands-off' approach is risk management. One of the lessons of the AWI experience is the need for better mechanisms to react quickly to potential problems. If problems occur there should be protocols so that the level of supervision can be increased in a timely way which, at each stage, balances the risk involved, the administrative workload which supervision implies for AFFA, and the policy goal of allowing the company to manage its affairs with reasonable autonomy. The planning and reporting provisions of Statutory Funding Agreements should be devised to take this role. The Committee has suggested that AFFA should strengthen its role in approving strategic and operating plans (see paragraph 3.29).

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32 AWI Statutory Funding Agreement, clause 22.3.



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***Whether duty to shareholders conflicts with accountability to government***

5.39 In respect of AWI's argument that 'the direct accountability of AWI [is] to its shareholders' (letter of 14 November 2001: see paragraph 5.8 above): the Committee contends that this argument cannot be used as an excuse for AWI's failure to comply with the SFA. As AFFA noted, the SFA is a contract. If AWI fears that the contract is not in the company's best interests, it does not have to sign it. By signing, AWI asserts that the net effect of the contractual rights and obligations (which include the accountability obligations) *is* in the company's best interests.

5.40 In any case, the Committee finds it hard to imagine that full compliance with the SFA could be against the company's best interests. Thorough strategic and operational planning and performance reporting are arguably to the benefit of any large company.

***Whether ASIC is the appropriate body for complaint***

5.41 The Committee disagrees with Mr Taylor's suggestion that 'ASIC is the appropriate body if you have any concerns in terms of governance for a Corporations Law company' In the Committee's view this is not an adequate response. AWI's shareholders have a dual role: they are shareholders protected by the Corporations Law like any other shareholders; but they also, through the levy, provide their company's income. Because the levy, by government policy, is compulsory, there is a separate duty on government to ensure that AWI acts not only legally in the Corporations Law sense, but also prudently for the benefit of levy payers, according to the Statutory Funding Agreement. That duty lies with AFFA.

5.42 The duty of protecting levy payers' interests lies with AFFA, and even where the legal responsibility for corporate governance falls under ASIC, AFFA should be proactive in drawing concerns to ASIC's attention.

5.43 The same applies in relation to the expenditure of the Commonwealth Matching Funds (research and development grants) under schedule 4, except that in that case the funds are provided by taxpayers at large, and the duty to ensure that they are well spent lies towards taxpayers at large, not only towards Wool Levy payers.

5.44 The Committee notes that this is also the conclusion of AFFA's June 2002 *Review of Corporate Governance of Portfolio Bodies*:

...the practical and political reality is that, if the corporate governance of a Corporations Act entity within the AFFA portfolio becomes a matter of contention, it will likely not be sufficient for the Minister or Parliamentary Secretary to simply respond to comment or criticism by saying that the matter is one for ASIC. This is particularly the case where coercively

extracted producer levies are being provided to the company by the Commonwealth.<sup>33</sup>

The Review of Corporate Governance of Portfolio Bodies is considered further in chapter 7.

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33 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.51.

# CHAPTER SIX

## AWI and AFFA Responses Since November 2002

### New AWI Board, November 2002

6.1 A largely new Board of AWI was elected on 31 October 2002. AWI detailed how the new Board has acted to improve the governance of AWI:

The board has worked very closely with management to strengthen governance procedures and to improve controls. Since the election, the new board has substantially reduced management's delegations so that the board can exercise control over the company's operations, improve the transparency of AWI's monthly financial reports and resolve that, as a matter of priority, all projects should be covered by formal contracts prior to being acted on. We have also promulgated an advance payments policy, which provides guidelines on how the company is to process advance payment requests made by research providers. Importantly, we have also resolved that any campaigning for re-election must be undertaken at the directors' and not the company's expense. We have formed the remuneration and appointments committee of the board, which sets policy on remuneration issues for the company...<sup>1</sup>

6.2 The new AWI Board praised AFFA's diligence in overseeing the Statutory Funding Agreement since November 2002:

Within days of the election of the current board on 4 November 2002, the Minister wrote to Mr McLachlan, seeking clarification of the donation of \$500,000 to the Farmhand Appeal and urging high standards of corporate governance. Since that time there have been a number of meetings and correspondence at both ministerial/board and department official/management level. Senator Troeth has also been involved in some of these meetings.

During these discussions, which have been frank and co-operative, AWI has provided the Commonwealth with information about its operations and explained what action it has taken on identified problem areas. The Commonwealth has communicated clearly its expectations of AWI throughout this period.<sup>2</sup>

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1 AWI, *Committee Hansard* 28 August 2003, p.81.

2 Submission 13, AWI, pp.10-11.

## PricewaterhouseCoopers forensic review, April 2003

6.3 The new Board commissioned from PricewaterhouseCoopers a special ‘forensic review’ of AWI financial operations.<sup>3</sup> Its findings were summarised in a letter to shareholders in June 2003. It disclosed a number of unusual or poorly substantiated payments, possible breaches of the Statutory Funding Agreement, and project management issues (details are in chapter 4). AWI advised that it has acted in response both to improve management controls and to investigate possible recovery of money ‘where legally or commercially appropriate.’<sup>4</sup>

6.4 AFFA referred the PwC forensic review to the Australian Government Solicitor for advice on possible breaches of the SFA and possible actions in response. AGS advised that a number of the matters, if true, disclose breaches of the SFA. Some may also disclose breaches of the Corporations Act (for example, use of the company’s money to promote the re-election of sitting directors).

6.5 AGS advised that possible remedies under the *Wool Services Privatisation Act 2000* or the SFA (for example, suspend levy payments) would be excessive in relation to the breaches alleged and counterproductive to the shareholders of AWI and the continued relations between the Commonwealth and AWI. AGS recommended that the Minister should write to AWI asking to be kept informed about the progress of investigation into the PwC forensic review matters; and asking AWI to notify the steps it is taking to ensure that the Funds are used only for permissible purposes. AGS noted that pursuing any remedy for breaches of the Corporations Act would be a matter for AWI or the Australian Securities and Investments Commission to pursue: it could not be done by the Commonwealth.<sup>5</sup>

6.6 The Minister wrote to AWI in the suggested terms on 12 August 2003. AWI advised the Committee that ‘we are getting our response audited by PricewaterhouseCoopers to provide a level of comfort that what is being said in that response is in fact happening.’<sup>6</sup>

6.7 AFFA advised the Committee that it was ‘not ruling out or in’ further action in relation to the PwC matters.<sup>7</sup>

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3 PricewaterhouseCoopers, *Australian Wool Innovation Limited - Forensic Review of Financial Operations, Final Report*, 16 April 2003. See discussion of this report and the letter to shareholders at paragraphs 4.89 to 4.94.

4 AWI letter to shareholders, 5 June 2003, p.3. Similarly Mr B. Van Rooyen (AWI), *Committee Hansard* 28 August 2003, p.89.

5 AFFA, additional information 29 August 2003: AGS advice 5/8/03, p.37-38.

6 AFFA, additional information 8 October 2003, p.3; 30 October. Mr L. Targ (AWI), *Committee Hansard* 28 August 2003, p.90.

7 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.108.

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## **AWI's Review of Performance, May 2003**

6.8 Under clause 20 of the Statutory Funding Agreement, AWI must make a Review of Performance, and make it available to shareholders, before a Wool Poll. This was done by a consultant and published in May 2003. Some of its key findings were:

- The AWRAP to AWS-AWI restructure did bring about 'substantial change' and producer control of wool R&D activities, but on balance and to date, R&D performance has not been enhanced.
- AWI transparency on decisions and operations has been less than demonstrated by AWRAP in formal communications of later years, and less than levels expected by stakeholders.
- AWI was both criticised and praised on consultation during 2001 and 2002.
- AWI has focussed primarily on R&D over 2001 and 2002 but perceptions that AWI needs to be the industry leader also seem to influence AWI style, reactions and priorities at times.
- The targets set out in the Strategic Plan 2002-2007 and in the Operating Plan 2002-2003 for projects are a significant advance for AWI and for shareholders, and are mostly useful.
- Informative efficiency measures are still to be developed. They need to be more refined than comparisons of overheads or numbers of people, although these should be clearly reported.
- AWI has met most of the obligations in the SFA, and is working to meet them all in 2003.
- There has been progress in implementation of parts of the Operating Plan but overall this has been slower than projected.
- Much R&D and corporate activity is underway, but performance in the form of delivery of benefits to woolgrowers is not, as yet, widely identifiable at project or AWI level.
- AWI's Strategic Plan 2002-2007 and Operating Plan 2002-2003 both met Statutory Funding Agreement requirements plus Government and industry consultation and content expectations.
- Neither the AWS Annual Report 2001 nor the AWI Annual Report 2002 met Statutory Funding Agreement requirements, or woolgrower shareholder expectations, in spirit or form.

6.9 Under clause 20(b) of the SFA AWI was obliged to procure an external opinion of the Review by the company's auditors. PricewaterhouseCoopers expressed the opinion that the review process was appropriate and 'led to an open and frank

assessment of AWI's performance.' PwC noted that they were not qualified to comment on the outcomes of scientific projects or matters that relate to scientific activities.<sup>8</sup>

### **Special audit of compliance with the SFA**

6.10 On 25 November 2003 AWI obtained an auditor's report, as required by clause 22.2 of the SFA, on compliance with the SFA for the 2002/2003 year. This reviewed a sample of AWI projects 'to determine the criteria against which the projects were assessed (in particular whether there was any formal evidence of assessment against SFA compliance) and whether the objective of the project appeared in compliance with the SFA.' The review did not involve analysing the prudence of business decisions made by directors or management.

6.11 The report noted a number of possible breaches of the SFA, most of which were those noted in PricewaterhouseCoopers' April 2003 forensic review. Otherwise it noted:

We found that the payments selected were for projects whose objectives appeared to meet the purposes for expenditure for 'Funds' as specified in the SFA.

It is noted that there appeared to be no formal assessment of projects meeting the requirements of the SFA, prior to approving the projects. In a small number of cases there was formal documentation as to whether the projects fell within the strategic objectives of AWI.

6.12 The report could not express an opinion on whether the use of the Funds was 'efficient, effective and ethical' (clause 5.3 of the SFA):

Due to the scientific nature of the expenditure of AWI and the highly subjective nature of what is efficient, effective and ethical, we are unable to express an opinion as to whether the Funds were spent in a manner that was efficient, effective and ethical.<sup>9</sup>

6.13 AWI advised that it has no plans to seek a clause 22.2 retrospectively for the 2001/02 year:

Due to the scientific nature of the expenditure of AWI and the highly subjective nature of what is efficient, effective and ethical, we are unable to

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8 AFFA, additional information 13 January 2004: PwC clause 20 review, 11 September 2003.

9 AWI, additional information 9 January 2004: PricewaterhouseCoopers report on AWI's compliance with Statutory Funding Agreement, 25 November 2003.

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express an opinion as to whether the Funds were spent in a manner that was efficient, effective and ethical.<sup>10</sup>

6.14 The Committee notes the comment of the May 2003 *AWI Review of Performance*:

Statutory Funding Agreement obligations: AWI has met most of the obligations in the SFA, and is working to meet them all in 2003. Processes are being further developed to ensure systematic assessment of compliance with the SFA in decisions to apply the Funds, and for full annual reporting in the spirit and terms of the SFA.<sup>11</sup>

### **Renegotiation of the SFA**

6.15 The Statutory Funding Agreement was to expire on 31 December 2003. It has been temporarily extended so that the negotiations can take account of the findings of this report. AFFA advised that it would negotiate with a view to reinforcing accountability and reporting arrangements.<sup>12</sup> However AFFA argued that the basic structure is sound:

The Department considers that the arrangements put in place by the Parliament have been demonstrably robust in identifying and remedying problems within the company. The arrangements recognise that it is not practicable for the Commonwealth to seek to manage the day-to-day operations of an industry owned company. It is appropriate for the company to be owner and operated by industry, and for it to continue to work in partnership with the Government to deliver agreed outcomes for industry and taxpayers alike.<sup>13</sup>

6.16 AWI submitted that it accepts foreshadowed amendments to strengthen governance and reporting requirements 'without reservation'. However it also argued strongly that the basic structure is sound:

AWI believes that the necessary mechanisms to ensure the proper use of funds by AWI and its accountability to stakeholders, as well as adequate remedies, are already in place. It is difficult for AWI to see how the agreement could undergo fundamental amendment and still be effective for

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10 AWI, additional information 9 January 2004: PricewaterhouseCoopers report on AWI's compliance with Statutory Funding Agreement, 25 November 2003.

11 AWI (Dr S. Welsman), *Review of Performance: summary 2003*, p.16.

12 Mr M. Taylor (AFFA), *Committee Hansard* 17 September 2003, p.125.

13 AFFA, additional information 8 October 2003, p.4.

both the company itself, its shareholders, the Commonwealth and the Australian wool industry.<sup>14</sup>

#### 6.17 WoolProducers agreed:

WoolProducers believe it is not the structure of the wool industry service organisations, not the Agreement, that has been responsible for what has occurred over the past two years... Rather it has been the application of that structure that was in a large part removed from woolgrower shareholders by those that were initially appointed to oversee the companies. WoolProducers believe that greater care should have been given to the initial appointments.<sup>15</sup>

#### 6.18 The new AWI Board argued that a co-operative approach to ensuring SFA compliance is best, and praised AFFA's approach:

It is AWI's submission that co-operation between the Commonwealth and AWI is the most effective way of achieving compliance, not only with the express provisions of the SFA, but also with its intent. Indeed, AWI suggests that the Minister and his department have acted in the most appropriate manner in deciding to allow the corporate model to work and by engaging in direct dialogue with AWI. Any other approach, such as imposing a team of auditors, would have been unlikely to have led to such a successful resolution and would certainly not have done so without major business interruption to AWI and/or a cost to innocent woolgrowers.<sup>16</sup>

### **Recommendation 4**

**The Minister should give consideration to referring any breaches of the Corporations Act by AWI to the Australian Securities and Investments Commission.**

### **Recommendation 5**

**Prior to a new SFA being agreed with AWI the Minister should review the effectiveness of remedies for breaches of the agreement currently available through the *Wool Services Privatisation Act 2000*.**

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14 Submission 13, AWI, pp.11-12.

15 Submission 1, WoolProducers, p.7.

16 Submission 13, AWI, par. 3.5, 3.6.



# CHAPTER SEVEN

## Comments on the Statutory Funding Agreement Model

7.1 A balance needs to be found between the needs of accountability and oversight and the policy goal of greater industry ownership of R&D bodies. In the Committee's view the basic structure of Corporations Law company answering for the use of public money through a statutory funding agreement allows this, but requires strengthened accountability procedures. The Committee suggests that continuing refinement of AFFA's oversight processes will be necessary to prevent the problems of AWI recurring in either AWI or other similar bodies. The Committee makes some miscellaneous suggestions for SFA provisions below.

### **AFFA's oversight of portfolio bodies: 2002 review**

7.2 Oversight of levy-funded R&D companies such as AWI is an important responsibility of AFFA. In 2002 AFFA commissioned a review of the corporate governance of AFFA portfolio agencies. One of its topics was:

... the management of deeds of agreement with industry-owned companies that AFFA funds; including:

- addressing whether the Minister is a “shareholder”, stakeholder or interested bystander (particularly given the bulk of monies are appropriated by Parliament); and
- advising on the most appropriate way of managing the arrangements so that the Minister and Parliament are fully informed on the use of public monies  
....<sup>1</sup>

7.3 The Review recommended the following basic principle concerning AFFA's role in ensuring good corporate government among portfolio agencies (which, in this context, includes companies like AWI):

- that it is the individual portfolio agency that should be primarily responsible for ensuring the quality of its own corporate governance. AFFA should not undertake corporate governance tasks that should more properly be performed within the agency; and
- AFFA has a quite separate portfolio corporate governance role the purpose of which should be:

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1 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.9.

- to support portfolio Ministers and the Parliamentary Secretary in acquitting their accountability and responsibility for the corporate governance of AFFA portfolio agencies;
- to reinforce, support and promote the assumption by portfolio agencies of their primary responsibility for their own corporate governance;
- to foster best-practice corporate governance amongst portfolio agencies; and
- to monitor compliance by portfolio agencies with their corporate governance responsibilities, and facilitate redress where necessary.<sup>2</sup>

7.4 The Review notes that Government has no power over companies such as AWI except ‘a fundamental and pragmatic power... the right to withhold future funding.’ However Government does have a stake in the performance of the company, in that -

In a pragmatic, political environment, the Minister/Parliamentary Secretary may be called upon to answer for the actions of the company:

- if it does not achieve the public interest purposes underlying the Government’s motivation in promoting its establishment;
- if it fails to comply with the terms of its contractual obligations to the Commonwealth;
- if it misappropriates or fails to secure value for money in its use funds provided by the Commonwealth;
- if its internal corporate governance is less than required; or
- if it loses favour with its industry constituency, particularly where it is funded by compulsory levies on that group.

The prospect of the Minister/Parliamentary Secretary being held to account in these circumstances means that it is essential that there be a close focus on the content of the AFFA portfolio corporate governance role as it particularly affects these bodies.<sup>3</sup>

7.5 The Review comments on AFFA’s relationship with bodies like AWI:

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2 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.12.

3 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.44-45.

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Where a portfolio agency is, or is proposed to be, a private, industry-owned company, AFFA's involvement will principally be based in contract... there will be far more limited capacity to issue mandatory directions or, ultimately, to abolish and replace the agency.

In these circumstances, the development of the various deeds of agreement and their management day-to-day assume a heightened importance.... there is necessarily a more demanding task in setting and maintaining AFFA's portfolio corporate governance role in relation to private, industry-owned agencies.<sup>4</sup>

7.6 The Review proposes a checklist of AFFA's responsibilities in relation to such bodies.<sup>5</sup> It comments specially on the proposed responsibility to 'appraise conformance with obligations under the *Corporations Act*'. The question is whether AFFA has any role in this regard:

In our discussions with some senior officers, it was suggested that AFFA has no role at all in relation to whether or not a private, industry-owned company is complying with its corporate governance obligations under the *Corporations Act*. In contrast, a number of other officers, and notably the Parliamentary Secretary, did think that AFFA had some legitimate role in this regard. We think the latter view is the correct and preferable one.

There is no question that primary responsibility for regulating the corporate governance of a *Corporations Act* company rests with the Australian Securities and Investments Commission ("ASIC"). Nevertheless, we consider that the practical and political reality is that, if the corporate governance of a *Corporations Act* entity within the AFFA portfolio becomes a matter of contention, it will likely not be sufficient for the Minister or Parliamentary Secretary to simply respond to comment or criticism by saying that the matter is one for ASIC. This is particularly the case where coercively extracted producer levies are being provided to the company by the Commonwealth.

Accordingly, we recommend that AFFA regard its role in this regard is as follows:

- to remain observant and identify any emerging corporate governance issue;
- to take such issues up with the relevant company to ascertain whether or not there is in fact any matter for concern; and

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4 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.49.

5 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.49-50.

- where concern does arise, to consider what action should be taken including exercise of powers under the contractual arrangements with the company; withdrawing statutory designation under levy legislation, withholding levy payments, and referring matters for investigation by ASIC<sup>6</sup>

7.7 The Review recommends that AFFA should have a settled procedure for handling complaints about the corporate governance of portfolio agencies.<sup>7</sup>

7.8 The Committee has recommended at paragraph 6.18 that the Minister refer any breaches of the Corporations Act by AWI to the Australian Securities and Investments Commission.

### ***Comment***

7.9 The review was not commissioned in response to AWI's problems, but the problems which arose in AWI shortly afterwards show that the review was timely. The Committee supports its recommendations.

7.10 The Committee particularly notes the suggestion that AFFA's oversight should not be limited to SFA compliance viewed narrowly (paragraph 7.4 above). It should include:

- whether the body is achieving its public interest purpose;
- whether it is obtaining value for money;
- whether its internal corporate governance is satisfactory.

7.11 The Committee agrees. A body might comply with its statutory funding agreement and still fail these tests. This should be a matter of concern. AFFA should develop oversight procedures which will allow it to test these points.

### **Miscellaneous comment on SFA provisions**

7.12 These suggestions are phrased to relate to AWI, but they would apply equally to other similar agreements.

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6 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.51.

7 Mallesons Stephen Jaques, *Review of the Corporate Governance of Portfolio Bodies, Final Report Volume 1*, report for Department of Agriculture, Fisheries and Forestry, June 2002, p.61.

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### ***Standards of corporate governance***

7.13 Arguably the special position of a body such as AWI implies standards of corporate governance additional to those implied by the Corporations Act. For example, the fact that activities compensate for market failure means that many activities will not yield clearly predictable or quantifiable returns which can be used to prioritise them. This implies the need for more sophisticated performance indicators than a purely commercial company might need, and more trust in the judgment of management and directors in choosing investments.

7.14 The Committee suggests that statutory funding agreements should reflect these special requirements. The Committee notes the ASX Corporate Governance Council's *Principles of Good Corporate Governance and Best Practice Recommendations*. (March 2003). The Committee suggests that AFFA should consider incorporating these into accountability conditions of Statutory Funding Agreements as relevant.

### ***Prohibition on 'agripolitical activity'***

7.15 The SFA prohibits 'agri-political activity' as defined (clause 5.6). The Australian Government Solicitor, in advice to AFFA, felt that it is unclear whether the SFA definition of 'agripolitical activity' is intended to apply only to 'external' political activity intended to affect government and public opinion; or whether it applies also to 'internal' political activity intended to influence company members' vote in a election of directors. AGS concluded:

We doubt that it could be confidently concluded that the use of Funds for election campaigning by the then AWI Board was prohibited on the basis that it was Agri-political activity within the meaning of the SFA.<sup>8</sup>

7.16 In the Committee's view the definition of 'agri-political activity' should be amended to clarify that it includes internal as well as external political activity.

### **Recommendation 6**

**The definition of 'agri-political activity' should be amended to explicitly include internal as well as external political activity.**

### ***Whether the SFA should control all company expenditure***

7.17 The Committee has recommended that the SFA should have a condition that all the company's expenditure (not only the expenditure of 'the Funds') should be controlled by the agreement (see paragraph 4.144ff).

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8 AFFA, additional information 29 August 2003: AGS advice 5/8/03, p14.

***Whether expenditure should have to follow the strategic plan***

7.18 The SFA requires that in spending the Funds the AWI must ‘have regard to’ the strategic plan, the operational plan and the R&D Guidelines (clause 5.3).

7.19 The Committee believes that the SFA should incorporate a requirement mandating that expenditure be consistent with the strategic plan, the operational plan and the R&D Guidelines.

**Recommendation 7**

**The SFA should incorporate a requirement mandating that expenditure be consistent with the strategic plan, the operational plan and the R&D Guidelines.**

***Whether market failure should be a condition of all projects***

7.20 With some AWI projects a point of contention has been, whether the project really compensates for market failure (for example, WoolProducers’ concern about the Woodlot project noted at paragraph 4.2).

7.21 The SFA has no general condition that particular projects should be restricted to cases of market failure. The AFFA ‘Levy Principles and Guidelines’ imply it (‘the proposed levy must relate to a function for which there is significant market failure’); but strictly speaking the Guidelines relate to rules for proposing new or changed levies, not expenditure of levy money in detail.

7.22 The Committee suggests that AFFA should clarify its intentions in this regard. Whether each particular project should have to prove market failure formally should be a matter for further consideration.

***Whether financial auditors can comment on technical matters***

7.23 Clause 20 (Review of Performance) and clause 22 (audit of compliance with the SFA) attempt to obtain independent review by involving the company's auditor.

7.24 However there are difficulties where the financial auditors have to report on compliance with the agreement in relation to technical matters. In its audit report pursuant to clause 20, PwC understandably felt unable to comment on the outcomes of scientific projects.

7.25 The Committee suggests that a better way to achieve independent review would be for reviews of performance or SFA compliance to be done by an independent expert agreeable to AWI and AFFA.

***‘Efficient, effective and ethical’***

7.26 AWI must apply the SFA Funds in a way that is ‘efficient, effective and ethical’ (clause 5.3).

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7.27 This is a worthy goal, but it is not a practical decision criterion, because it is not capable of objective definition. The Committee notes that PricewaterhouseCoopers, in its report on SFA compliance for 2002/2003, felt unable to comment on whether the use of the Funds was ‘efficient, efficient and ethical’ because of the subjective nature of the terms. ‘Efficient, effective and ethical’ would have to be defined more closely if this condition is to have practical effect. A requirement that the Funds must be spent in accordance with a strategic plan which has clear goals and performance measures would probably achieve the same practical effect.

***‘For the benefit of Australian woolgrowers’***

7.28 This term is used in clause 5.1 of the SFA (permissible uses of the Wool Levy Funds) and schedule 4 (permissible uses of the Commonwealth Matching Funds) Like ‘efficient, effective and ethical’, it is hard to define. For example, it has not prevented debate over whether AWI’s donations to charity are permissible uses as being good corporate citizenship. The Committee notes in this regard that the condition ‘for the benefit of Australian woolgrowers’ is additional to the conditions in clause 5.1; it is not freestanding. A proposed use of the Wool Levy Funds must match one of the terms of clause 5.1 *and* be for the benefit of Australian woolgrowers.

**Recommendation 8**

**The Minister should give consideration to incorporating conditions in existing and future Statutory Funding Agreements as suggested by recommendations 2, 6, 7 and other relevant suggestions in this report.**

**Senator Bill Heffernan  
Chairman  
Rural and Regional Affairs and Transport Legislation Committee**





# **SUPPLEMENTARY COMMENTS**

**by Senator John Cherry**

This Inquiry is about the administration and the operation of the Statutory Funding Agreement between the Commonwealth and AWI, and the expenditure and application of funds under that agreement. It is not supposed to be an exercise in denigrating former or current employees or directors of AWI.

While I am happy to sign up to the recommendations in the majority report touching on the public administration issues raised by AWI's brief history, and recommendations referring the evidence to the relevant authorities for investigation, I am not happy to sign up to sweeping 'conclusions' that reflect adversely on the performance of individuals based on incomplete evidence.

For that reason, I have declined to support the conclusions made by the Committee in Chapter 4 (paragraphs 4.45, 4.57 to 4.59, 4.79 to 4.83, and 4.154 to 4.158). The conclusions reached by the Committee may or may not be correct, but I do not believe that the Committee has taken sufficient evidence to make such broad conclusions on the performance of AWI or its directors. Much of the evidence of an adverse nature has not been addressed by those affected by it. Nor have the paper trails been followed to their conclusion. Further, the Committee has taken no evidence from experts in corporate governance or ASIC to establish appropriate benchmarks against which such matters should be judged.

This Inquiry has taken evidence from the new board of AWI, the Woolproducers organisation, a former director of AWI who ultimately fell out with the old board, and subpoenaed a highly critical forensic audit commissioned by the new board. Against that, it has taken evidence (once) from the former AWI chief executive Col Dorber, declining his request for a second appearance, but accepting his three detailed supplementary submissions. It requested the former AWI chair to appear on two occasions, but she declined, citing other business commitments. A mutually convenient date for her appearance was never found. The board also received submissions from three other former AWI directors but took no evidence from them. It received submissions from several directors of the Australian Wool Growers Association and other wool producers but, again, took no evidence from them.

I am of the firm view that our evidence gathering is incomplete for the Committee to make serious adverse findings against the performance of individuals. To make findings based on incomplete evidence affects the credibility of the Committee's report, leaving its report unbalanced and vulnerable to assertions of it being a 'kangaroo court'. Natural justice and due process should dictate that the Committee either complete its investigations or make no adverse findings.

Having said that, I believe that is not in the public interest, or in the interests of AWI or woolgrowers to have allegations and counter-claims left unresolved. I believe that a proper, genuine independent review should be conducted into the various claims made to this Committee, with full access to AWI records and current and former AWI directors and staff.

### **Recommendation:**

**That AFFA, with the agreement of the current and former directors of AWI, appoint an independent person expert in corporate governance, to investigate the various matters raised with the Committee, with such report to be released publicly to settle the matters once and for all.**

### **Historical background to the AWI dispute:**

This inquiry has become the latest forum in the long fight between the two ‘camps’ in the wool industry. On the one side has been the WoolProducers organisation and the new board of AWI. On the other side have been the ‘rebel’ woolgrowers in the Australian Woolgrowers Association (AWGA) and the old Board of AWI. The events covered in this report covered the period leading up to and following the hotly contested board elections of 2002 which resulted in woolgrower-shareholders splitting roughly evenly between the two camps. This reflected the deep divisions that have been evident in the wool industry about its future direction for a long time.

AWI itself grew out of the wool growers rebellion against the old wool industry leadership represented by the board of the former Australian Wool Research and Promotion Organisation (AWRAP). In November 1998, woolgrowers rebelled against the AWRAP and the industry leadership, recording a 74% vote of no confidence at its annual general meeting. The Board of AWRAP resigned, and a “Future Directions Taskforce” report recommended that AWRAP should be replaced with a Corporations Law company limited by shares owned by woolgrowers. The March 2000 Wool poll saw woolgrowers support a reduction in the levy from 4% to 2%, with the allocation for marketing and promotion effectively deleted.”<sup>1</sup>

AWI was established as a separate subsidiary on January 1 2001, with a formal demerger effected on 30 April 2002. WoolProducers, in their evidence to the Committee, said that they started ‘being concerned’ about AWI from late 2001 on. Such ‘concerns’ did not surprise some submitters. Australian Wool Growers Association director Marion Gibbins argued:

‘Right from the beginning of its operation, the new AWS and AWI organisations were seen to be different to the previous research organization and its predecessors. With a totally new team of operators, the excitement and challenge coming from AWI to make Research, Development and

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<sup>1</sup> For further discussion see RRAT Report “The Australian Wool Research and Promotion Organisation Amendment (Funding and Wool tax) Bill 2000 report April 2000

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Innovation have the relevance as set out in the “McLachlan report; for the profitability of wool growers was sure to create discomfort for the previous beneficiaries of compulsory woolgrower funding.”<sup>2</sup>

As 2002 progressed, relations between AWI and WoolProducers clearly deteriorated. The board found itself criticised in the rural media, with one former director referring to the "extraordinary, untrue and vindictive comments from a minority of shareholders and the rural press".<sup>3</sup> Representative organisations and individuals would ultimately fund \$45,000 to support the WoolProducers-preferred candidates for the AWI board elections held in late 2002. As the election approached, the campaign by WoolProducers against AWI's board continued. WoolProducers President Simon Campbell was quoted in the “Financial Review” as saying:

“We believe there has been a consistent failure on the part of the current executive team to observe standards of transparency and accountability that is required of a body that is charged with spending the tax on wool producers.”<sup>4</sup>

The Board sought to respond to these continuing attacks, but, in doing so, appears to have crossed the line of using company funds to support its own re-election as opposed to defending the company's good name. While I recognise that the dotted line between 'campaigning' and 'defence' is a difficult one to determine, the question of whether AWI directors crossed it should be investigated by ASIC. That investigation should also cover whether the letter sent to shareholders by the current AWI Board on 5 June 2003 ‘summarising’ the PwC report and arguing that the previous board was challenged at the AGM “on the basis that there had been inadequate corporate governance by the previous board”<sup>5</sup> was a further piece of pre-emptive campaigning ahead of a possible challenge at the 2003 AGM. The submission from the four former directors of AWI certainly saw it as such, arguing that the letter aimed to 'discredit directors' and:

“This amounts to a breach of governance on behalf of the current Board and should be investigated. At the very least, the full Board should stand for election in November.”<sup>6</sup>

The current board of AWI defends the letter, arguing that its ‘duty of disclosure compelled it to release a summary of the PwC’s major findings.’<sup>7</sup>

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<sup>2</sup> Marion Gibbins submission p.1

<sup>3</sup> Submission from Michael Staley

<sup>4</sup> “Riding into battle on the sheep’s back” AFR 25/10/2002

<sup>5</sup> Letter from I McLachlan to AWI members 5/6/2003 p.2

<sup>6</sup> Old board of AWI submission p.7

<sup>7</sup> AWI submission 11/8/03 p. 13

The frustration of the former directors with the campaign against them during 2002 is evident in their submissions to this Inquiry. Agri-politics is a tough business and, at times can get very robust. But, given that AWI was in its first two years of operation, some argued that the first Board was never given a fair opportunity to prove itself. It is particularly noteworthy that all directors agreed to face election in 2002, as the former directors put it:

"A decision was made by the Board to offer all positions for election despite not being required to do so. This was done as an act of good faith in the performance of the Board and the company."<sup>8</sup>

Other wool grower organisations, including the Australian Wool Growers Association, remained strongly supportive of the Board's direction. Chairman of the Australian Association of Stud Merino breeders, Mr Wal Merriman, also a member of the then AWI's wool advisory group, was reported as saying that the current board had been truly innovative, commercially focussed and transparent.<sup>9</sup> The Managing Director of Australia's largest wool buyer, Itochu Wool, was quoted in the media stating that the then AWI board 'is doing a phenomenal job' and growers should 'give them a chance', dismissing the WoolProducers campaign as 'an unelected rehash of the now defunct Wool Council of Australia'.<sup>10</sup>

In the end, wool growers split down the middle in supporting and opposing the old board of AWI. The 2002 AGM showed strong support for the old AWI Board. The former six former directors attracted slightly higher support among growers than the WoolProducers team at the 2002 AGM, averaging 3460 votes per director (51%) compared to 3324 for the five challengers (49%). However, when the formal poll was counted with votes weighted for wool tax payments (i.e. with larger producers receiving more weight), support for the former board fell to an average of 220,597 votes (falling to 214,872 if the director backed by both sides is deleted), while the support for the new board members averaged 247,932 votes.<sup>11</sup>

I have been very critical of the 'weighting' of votes in agri-political organisations based on effectively the size of farm. Given such polls concern the collection and spending of compulsorily collected funds, it is the Democrats' firm view that "one vote – one value" principles should apply to elections of agricultural bodies (including Dairy Australia and Meat and Livestock Australia). Interestingly, had that rule applied to AWI in 2002, four of the old board directors would have been re-elected (McCaskill, Sykes, Trounson and Murphy) along with two of the WoolProducers candidates (McLachlan and Van Rooyen). With votes weighted to favour large producers over smaller one, the WoolProducers-endorsed team, swept all five

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<sup>8</sup> McCaskill submission p.2

<sup>9</sup> "Stud breeders back AWI board" "The Land" 11/9/2002

<sup>10</sup> "Stick with AWI team, Itochu urges" "The Land" 15/10/2002

<sup>11</sup> Figures provided by the ASX to AWI

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positions that they contested (the sixth position going to director Sykes endorsed by both teams).

Nor have assertions of corporate governance failings finished with the election of the new Board in 2002. Several submissions to this Inquiry have made various assertions against the current board's management as well, covering expenditure decisions,<sup>12</sup> the protection of intellectual property,<sup>13</sup> and the 5 June letter to shareholders.<sup>14</sup>

Given the deeply political background to the AWI dispute, it is my view that the Committee should tread carefully, seek to avoid further impugning the reputations of those involved, and focus instead on the public administration issues that hybrid public-private bodies like AWI raise.

### **Public administration issues:**

The Democrats firmly believe that public bodies should adhere to the highest standards of corporate governance. As the main Committee report highlights, the 'hybrid' public-private model used for AWI (and earlier used for Meat and Livestock Australia) raises some concerns in a public administration and accountability sense. Many of these issues were canvassed in AFFA's June 2002 *Review of Corporate Governance of Portfolio Bodies* and are considered in detail in Chapter Seven of the Committee's report. The recommendations made by the Committee are sensible ones which will help to clarify the proper relationship between 'hybrid' producer bodies and the Commonwealth.

I do not underestimate the task that faced the first board on AWI in establishing a new organisation, negotiating a new strategic plan, and developing new consultative arrangements with wool producers while dealing with an increasingly hostile agri-political environment. Nor do I underestimate the task faced by the current board in rebuilding confidence in AWI. It is inevitable that some mistakes will be made, but good corporate governance arrangements, departmental oversight and clear accountability to producer/shareholders should act to minimise mistakes and ensure ready correction. But, at the end of the day, when an organisation is dealing with \$80 million of levies collected under compulsion of law from wool growers, the tolerance for mistakes should be at the lowest possible level.

It should also be noted that the structure of AWI was a direct result of decisions taken by the Government and industry representatives in 2000 and 2001. As discussed in the main report, some of the elements which were subsequently criticised (e.g. lower level of oversight by AFFA, making challenges to the board more difficult, change in R&D direction from previous body) were direct consequences of direct policy decisions

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<sup>12</sup> M. Gibbins submission.

<sup>13</sup> Submission by M. Staley

<sup>14</sup> Submissions by McCaskill, S. Coppock and M. Gibbins

taken prior to AWI's establishment. The Committee has recommended some changes in these policy settings. That is not a reflection, in my view, on the former management of AWI. Rather, it is a reflection on the policy framework within which AWI was to operate.

Given the newness of the hybrid public/private model under which AWI was operating, the Democrats believe that AFFA should have acted more energetically and earlier in establishing clearer lines of accountability, reporting and consultation. The recommendations in this report will clarify these relationships and ensure that proper accountability for compulsorily collected levy funds to the Commonwealth Parliament is more apparent in the future.

Senator John Cherry

# APPENDIX ONE

## SUBMISSIONS

<b>Submission Number</b>	<b>Author</b>
1	WoolProducers
2	Mr Vanne Tompf
3	Mr Alix Turner
4	Mr Hans Huebner
5	Mr Colin Dorber
6	Ms Marion Gibbons
7	Mr Michael Staley
8	Mr Jim Kennedy
9	Ms Maree McCaskill
10	Mr Stuart Coppock
11	Mr Christophe Mujagic
12	Mr Colin Dorber - Supplementary Submission
13	Australian Wool Innovation Limited
14	Ms Patricia Murphy
15	Mr Alix Turner – Supplementary Submission
16	Mr Colin Dorber – Supplementary Submission
17	Australian Wool Innovation Limited - Supplementary Submission
18	PricewaterhouseCoopers





# **APPENDIX TWO**

## **WITNESSES**

**Canberra, Monday, 23 June 2003**

**Department of Agriculture, Fisheries and Forestry**

Mr Gavan Cattanach, Manager, Science and Innovation Policy

Mr David Mortimer, Executive Manager, Food and Agriculture

Dr Cliff Samson, Executive Manager, Rural Policy and Innovation

**Canberra, Thursday, 26 June 2003**

**Mr Colin Dorber (Private Capacity)**

**Canberra, Thursday, 28 June 2003**

**Australian Wool Innovation Ltd**

Mr Brian Van Rooyen, Deputy Chairman and Chairman of Finance and Audit Committee

Mr Leslie Targ, Company Secretary and General Manager, Commercial

**Associate Professor Andrew Vizard (Private Capacity)**

**WoolProducers**

Mr Simon Campbell, President

Mr Duncan Fraser, Honorary Treasurer

Miss Sharon Turner, Executive Director

**Canberra, Wednesday, 17 September 2003**

**Department of Agriculture, Fisheries and Forestry**

Mr Gavan Cattanach, Manager, Science and Innovation Policy

Dr Cliff Samson, Executive Manager, Rural Policy and Innovation

Mr Michael Taylor, Secretary

Mr Greg Williamson, Acting Executive Manager, Food and Agriculture



## APPENDIX THREE

### TABLED DOCUMENTS

Documents submitted during hearings and accepted as evidence of the Inquiry.

Date	Submitted by	Title/Subject	Pages
26/6/03	Mr Colin Dorber	Volume of documents – material produced by Mr Colin Dorber while Director of AWI.	208*
26/6/03	Mr Colin Dorber	Statement No. 1: <i>Response to Issues in the Senate</i> , dated 26 June 2003	4
26/6/03	Mr Colin Dorber	Statement 2: <i>Further response to specific issues raised in the Senate Committee concerning: the Hon. Peter Anderson of Peter Anderson and Company Pty Ltd, claims of reporting concerns raised by AFFA Departmental Officers; Administration of the Statutory Funding Agreement</i> , dated 26 June 2003	7
26/6/03	Mr Colin Dorber	AWI Limited: Financial Authorities (Board approved financial/management delegations for AWI Limited), current as at 1 July 2002	13
26/6/03	Mr Colin Dorber	Correspondence between Mr Colin Dorber and Mr Michael Taylor, AFFA, Mr Gavan Cattanagh, AFFA, Senator the Hon. Judith Troeth, Mr David Hawker, MP and the Hon. Warren Truss, MP.	11
26/6/03	Mr Colin Dorber	AWI Limited Operating Plan 2002-3	33
26/6/03	Mr Colin Dorber	AWI Limited Strategic Plan 2002-7	49
26/6/03	Mr Colin Dorber	AWI Limited Annual Report 2001-2	65
28/8/03	Mr Simon Campbell, WoolProducers	<ol style="list-style-type: none"> <li>1. List of Corporate Governance Concerns</li> <li>2. Potential Breaches of the Statutory Funding Agreement</li> <li>3. Letter to Mr Simon Campbell from Mr Col Dorber, dated 9/11/01 regarding correspondence between</li> </ol>	<p style="margin: 0;">4</p> <p style="margin: 0;">2</p> <p style="margin: 0;">1</p>

		AWI Limited and WoolProducers 4. Email to Ms Sharon Turner from Mr Colin Dorber, dated 4/2/02 regarding communications between AWI and WoolProducers 5. Letter to Committee from Mr Simon Campbell (WoolProducers) dated 26/08/03 re Parliamentary Privilege – Protection of Witnesses	1 2
28/8/03	Professor Andrew Vizard	<b>Document A:</b> Resignation letter, dated 12 June 2002 <b>Document C:</b> AWI Recommendations of Appointment, dated 29 January 2001 <b>Document B:</b> Correspondence from Ms Maree McCaskill to Mr Colin Dorber, dated 22 February 2002 <b>Document E:</b> Email to Mr Col Dorber from Prof. Andrew Vizard re Board Appointment, dated 13 March 2002. <b>Document F:</b> Email to Prof. Andrew Vizard from Mr David Lewis regarding directors and demerger, dated 3 April 2002. <b>Document G:</b> Submission from Mr John Grant, Director, Innovar Pty Ltd, dated 15 August 2003.	3 2 1 1 2 2
17/9/03	Mr Michael Taylor, Secretary, AFFA	1. Letter from Australian Government Solicitor to Mr Gavan Cattanach, Manager, Science and Innovation Policy, AFFA, dated 15 September 2003, regarding AWI Limited. 2. Copy of an email from Mr Lex Morey (various recipients), dated 7 November 2001, titled <i>Matching contributions proforma</i> with a one-page attachment.	5 2

\* accepted as confidential evidence

## APPENDIX FOUR

### ADDITIONAL INFORMATION

Additional information accepted as public evidence of the inquiry.

Type:

A. Answers to questions put by the Committee

C. Miscellaneous further comment

D. Miscellaneous documents

Dated	Type	From	Topic
2/7/03	C	Hassall & Associates	comment on Mr Dorber's evidence 26/6/03
13/8/03	D	AWI	letter and attachments: PwC report to AWI 7/5/03: classification of expenses; PwC report to AWI 7/5/03: projects approved and without contracts; PwC report to AWI 16/4/03: <i>Australian Wool Innovation Ltd: Forensic Review of Financial Operations</i>
26/8/03	D		letter from Ms McCaskill to Chair, n.d.; from Ms McCaskill to Chair, 26/8/03; from Chair to Ms McCaskill, 26/8/03
26/8/03	C	WoolProducers	comment on Mr Dorber's submission 7/8/03
26/8/03	D	WoolProducers	protection of witnesses
29/8/03	A	AFFA	answers to questions from 23/6/03 hearing, attachments
	D	AFFA	AGS advice to AFFA 5/8/03: Australian Wool Innovation Ltd: Compliance with Statutory Funding Agreement

	D	AFFA	AGS advice to AFFA 5/8/03: AWI projects approved without executed contracts in place
	D	AFFA	AGS advice to AFFA 15/8/03: possible remedies under the Statutory Funding Agreement
	D	AFFA	Mallesons Stephen Jaques, <i>Department of Agriculture, Fisheries and Forestry: Review of the Corporate Governance of Portfolio Bodies: Final Report</i> , June 2002
	D	AFFA	AGS advice to AFFA 15/9/03
8/9/03	D	AWI	letter and attachment: Deed of Release between AWI and Mr Dorber, 11 December 2002
8/10/03	A,C	AFFA	answers to questions from 17/9/03 hearing, comment
30/10/03	A	AFFA	further advice in answers to questions from 17/9/03 hearing
23/12/03	C	AFFA	statistics on AFFA R&D corporations expenditure, 2002-3
9/1/04	D	AWI	25/11/02 letter PricewaterhouseCoopers to AWI: audit of compliance with Statutory Funding Agreement
13/1/04	D	AFFA	PricewaterhouseCoopers audit of AWI's Review of Performance, 11/9/03
13/1/04	D	AWI	emails to/from i2K Communications, 23/9/02

## **APPENDIX FIVE**

### **Extract from AWI Statutory Funding Agreement, 31 December 2000**

#### **Application of the Funds**

5.1 The Company may spend or otherwise apply the Wool Levy Funds only for or in relation to:

- (a) investigating and evaluating the requirements for R&D and innovation in relation to the wool industry;
- (b) R&D and innovation activities in relation to the wool industry;
- (c) facilitating the dissemination, adoption and commercialisation of the results of R&D and innovation in relation to the wool industry;
- (d) managing the Funds and risks related to the Company's expenditure and ongoing funding;
- (e) managing, developing and exploiting Intellectual Property arising from R&D activities;
- (f) providing wool industry services not otherwise widely commercially available to woolgrowers (including, but not limited to, activities in relation to animal health and welfare, market access initiatives, product and industrial marketing, wool quality assurance, chemical and pharmaceutical residues standards compliance, economic and non technical research);
- (g) collaborating with government and with government departments and agencies, both Federal and State, in relation to animal health and welfare, crisis and issues management, regulatory activities and other activities that may be necessary or convenient for the improvement of the productivity or the performance of the Industry;
- (h) maintaining a register of shareholders of the Company and, for so long as the Company is a Subsidiary of AWS, a register of A Class Shareholders of AWS;
- (i) holding an annual general meeting of the Company and, for so long as the Company is a Subsidiary of AWS, an annual general meeting of the A Class Shareholders of AWS;
- (j) maintaining a record of names and addresses of all Levy Payers and their voting entitlements on a Poll;

- (k) conducting a Poll in accordance with the Act and the Poll Regulations;
- (l) paying costs incurred by the Commonwealth or by AWS or any of its subsidiaries, in connection with the privatisation of AWRAP, the transition from a 4% Wool Tax to a 2% Levy or the transition from an organisation with the objects conferred on AWRAP by the Australian Wool Research and Promotion Organisation Act to an organisation with the objects conferred on the Company by its constitution;
- (m) payments to the Commonwealth in accordance with clause 3.4;
- (n) complying with obligations imposed on it under this Agreement or the Act;
- (o) such other purposes as may be approved by the Commonwealth in writing from time to time;
- (p) paying remuneration and allowances to directors, employees, consultants and agents of the Company or, for so long as the Company is a Subsidiary of AWS, of AWS and in meeting administrative, operating or capital expenses (including, but not limited to, lease costs and legal and other professional expenses) reasonably necessary or appropriate to be incurred by the Company to support its activities in relation to paragraphs (a) to (o) above;
- (q) the repayment of money borrowed by the Company, and the payment of interest and other financing costs incurred in relation to money borrowed by the Company, for purposes related to an activity referred to in paragraphs (a) to (p),

in each case for the benefit of Australian woolgrowers.



## **APPENDIX SIX**

### **EXTRACT FROM AWI STATUTORY FUNDING AGREEMENT, 31 DECEMBER 2000**

- 5.2 Commonwealth Matching Funds must be paid to the Company only to reimburse the company for amounts already spent by the Company on Eligible R&D Activities as specified in Schedule 4.

#### **SCHEDULE 4**

##### **R & D Activities**

##### **1. R & D Activities**

23.1 An activity will be a 'research and development activity' for the purposes of the Act if it is for, or in relation to, R&D related to the wool industry for the benefit of Australian woolgrowers and the Australian community generally.

23.2 Without limitation to paragraph 1.1., examples of activities which may be determined to be R&D Activities are:

- (a) a R&D project;
- (b) the training of people to carry out wool research and development;
- (c) the investigation and evaluation of the requirements for R&D in relation to the wool industry, and, on the basis of such investigation and evaluation, the preparation, reviewing and revising of R&D plans;
- (d) the carrying out, and the coordination and funding of the carrying out of wool industry R&D activities;
- (e) the monitoring, evaluating and the reporting to Commonwealth and the industry, on the R&D funded by the Company;
- (f) facilitating the dissemination, adoption and commercialisation of the results of R&D or of practices or technological developments that have been designed or adapted to improve the operation or efficiency of the wool industry;

- (g) the dissemination of information related to any aspect of wool industry R&D, whether electronically, by print or by any other means;
- (h) improving the accountability for expenditure upon R&D activities in relation to the wool industry;
- (i) the development in the wool industry of an awareness of the contribution that can be made by R&D in improving its efficiency and competitiveness;
- (j) such other activities as may be approved by the Commonwealth in writing from time to time;
- (k) any activity incidental but considered important to an activity referred to in paragraphs (a) to (j);
- (l) engaging directors, employees, consultants and agents of the Company and, for so long as the Company is a Subsidiary of AWS, of AWS and in meeting administration, operating or capital expenses (including, but not limited to, lease costs and legal and other professional expenses) reasonably necessary or appropriate to be incurred by the Company to support its activities in relation to paragraphs (a) to (k) above.