EDOs of Australia

EDOs of Australia
ABN 85 763 839 004
C/- EDO Northern Territory
7 Searcy Street
DARWIN NT 0800
www.edo.org.au
T: 08 8981 5883

Submission on Governance and operation of the Northern Australia Infrastructure Facility (NAIF)

7 August 2017

EDOs of Australia (formerly the Australian Network of Environmental Defender's Offices) consists of eight independently constituted and managed community legal centres located across the States and Territories.

Each EDO is dedicated to protecting the environment in the public interest. EDOs:

- provide legal representation and advice,
- take an active role in environmental law reform and policy formulation, and
- offer a significant education program designed to facilitate public participation in environmental decision making.

EDO ACT (tel. 02 6243 3460)
edoact@edo.org.au

EDO NSW (tel. 02 9262 6989)
edonsw@edonsw.org.au

EDO NQ (tel. 07 4028 3739)
edonq@edonq.org.au

EDO NT (tel. 08 8981 5883)
edont@edont.org.au

EDO QLD (tel. 07 3211 4466)
edoqld@edoqld.org.au

EDO SA (tel. 08 8359 2222)
edosa@edo.org.au

EDO TAS (tel. 03 6223 2770)
edotas@edotas.org.au

EDO WA (tel. 08 9420 7271)
edowa@edowa.org.au

Submitted to:

Senate Standing Committee on Economics

economics.sen@aph.gov.au

For further information please contact:

EDOs of Australia: [redacted]

Governance and operation of the Northern Australia Infrastructure Facility (NAIF)

EDOs of Australia (**EDOA**) is a network of community legal centres that specialise in public interest environmental law. We have written extensively on environmental assessments, approval processes and institutional governance at the national level and in each Australian jurisdiction. Because of its local relevance to Northern Australia, this submission has been prepared primarily by the Environmental Defenders Office Northern Territory and the Environmental Defenders Office QLD.

We welcome the opportunity to provide the Standing Committee on Economics with our analysis and recommendations for reform of the governance and operations of the Northern Australia Infrastructure Facility (**NAIF**). The NAIF is established under the *Northern Australia Infrastructure Facility Act* 2016 (Cth) (**the Act**). As recognised in the NAIF's *Environmental and Social Review of Transaction Policy* 2016, "some economic infrastructure projects have the potential to result in significant environmental and social impacts". As such the operations of the NAIF, and the legislation under which it operates is of relevance to the EDOA.

Our comments on the Inquiry's terms of reference are set out below:

a. the adequacy and transparency of the NAIF's governance framework, including its project assessment and approval process;

Because the NAIF's functions are guided by the *Northern Australia Infrastructure Facility Investment Mandate Direction* 2016 (**the Investment Mandate**) there is some overlap between this term of reference and term of reference (b) below.

General transparency

The NAIF's governance framework is characterised by a stark lack of transparency. Despite the existence of the Investment Mandate, few mechanisms exist that would allow meaningful assessment of whether the NAIF is appropriately applying the Investment Mandate in any given case.

The functions of the NAIF are set out at section 7 of the Act:

> **7 Functions of Facility**
>
> *(1) The functions of the Facility are:*
>
> *a. to grant financial assistance to States and Territories for the construction of Northern Australian economic infrastructure; and*
> *b. to determine terms and conditions for the grants of financial assistance; and*
> *c. as agreed between the Facility and the States and Territories, to provide incidental assistance to the States and Territories in relation to financial arrangements and agreements related to the terms and conditions of the grants of financial assistance.*

Section 9(3) of the Act requires the NAIF to "take all reasonable steps to comply with the Investment Mandate".[1]

The NAIF is governed by the NAIF Board (**the Board**) established by section 13 of the Act. The Board is charged with the responsibility of ensuring the proper, efficient and effective performance of the NAIF's functions.[2] Within the scope of the Investment Mandate, the Board has the power to decide policies and strategies to be followed by the NAIF.[3] To date 10 published policies are publicly available.

It is noted that the power of the Board to devise policies and strategies is a general one. There is no requirement for example for specific policies to be developed by the Board relating to an investment strategy or benchmarking or standards to be used to measure the performance of the investments approved by the NAIF. This can be directly contrasted with the requirements imposed on the Clean Energy Finance Corporation by virtue of section 68 of the *Clean Energy Finance Corporation Act* 2012 (Cth)

Recommendation 1: The Act is amended to require the NAIF to make and publish specific policies for risk management, investment strategies and standards for assessment of investments.

Absence of reporting requirements & public disclosure

Despite the requirements set out in the Investment Mandate (the adequacy of which are addressed below), there are no effective mechanisms to assess whether the NAIF's actions are taken in accordance with the Investment Mandate in relation to any given proposal.

The Board is obligated to take minutes of its meetings and keep a record of its decisions.[4] However the minutes of meetings and the decisions made are not publicly available. The Board is required to prepare an Annual Report.[5]

Currently information on assessment processes is not made publicly available.[6] Additionally the NAIF also refuses to publish its Risk Appetite Statement, which is a crucial component in understanding the criteria by which the NAIF measures risk, including, presumably, environmental risks.[7] The principles of ecologically sustainable development (**ESD**) provide a well-established legal framework to integrate and consider environmental risks and impacts of decision-making alongside other social and economic factors.[8] All Australian

1 We note that the Act does not impose any reporting requirements on the Board where it becomes aware that the Investment Mandate has not been complied with. This directly contrasts with the comparable s 67 of the Clean Energy Finance Corporation Act (Cth) 2012.

2 See s 14(1)(b) of the Act

3 See section 14(1)(a) of the Act

4 See section 26-27 of the Act

5 See section 42 of the Act

6 We note that the only limitation on publishing information is to the extent that such publication would conflict with commercial confidentiality – see section 17(2) of the Act.

7 This is of even greater concern, when coupled with the fact that elegibility for the board is not contingent upon members having demonstrated any skills in environmental or social impacts

8 See for example *Environment Protection and Biodiversity Conservation Act 1999* (Cth), ss. 3-3A; *Sustainable Planning Act 2009* (QLD) s. 3; *Environmental Planning and Assessment Act 1979* (NSW) s. 5(a)(vii); National Strategy for Ecologically

jurisdictions have agreed to embed ESD in decision-making on project assessment and land use planning.[9]

In addition to the above, there are no provisions/requirements in the Act, the Investment Mandate or the various policies for:

- Public notification of, and ability to comment on, proposed decisions to offer a financing mechanism.
- The NAIF to provide reasons for their decision to offer, or not to offer a financing mechanism.[10]
- Consideration of ESD and its principles in NAIF decision-making.
- Merits review of decisions to offer a financing mechanism.

While we recognise the desirability for flexibility in the NAIF's application of the Investment Mandate, that flexibility should not obviate the need for rigorous reporting standards and public accountability. As a publicly owned and accountable entity the NAIF must act appropriately and be seen by the public to be operating in a manner that is consistent with the Investment Mandate and more broadly, consistent with the law. The lack of review mechanisms and formal reporting requirements in the Act, the Investment Mandate and the NAIF's policies create a significant barrier to good governance, corruption prevention and public confidence in the management of significant sums of public funds.

We note that the NAIF's *Interim Corporate Plan* refers to independent reviews of the NAIF's governance arrangements, which have found them to be 'best practice'. As far as we can tell, those reviews are not publicly available.[11]

Recommendation 2: The Act is amended to at a minimum require:

- public notification of (and corresponding public comment period) a proposed decision to offer a financing mechanism;
- consideration and application of ESD principles in making funding decisions; and
- the NAIF to publish reasons for their decision to offer, or not to offer, a financing mechanism

Apparent conflict between the Investment Mandate and policies

---

Sustainable Development (1992); Intergovernmental Agreement on the Environment (1992). ESD principles are defined to include the precautionary principle; biodiversity and ecological integrity as a fundamental consideration; intergenerational and intra-generational equity; full environmental costing and the polluter pays principle.

9 *Intergovernmental Agreement on the Environment* (1992) section 3.4. For example:

> *the parties agree that environmental considerations will be integrated into Government decision-making processes at all levels by, among other things:*
>
> 1. *ensuring that environmental issues associated with a proposed project, program or policy will be taken into consideration in the decision making process;*
> 2. *ensuring that there is a proper examination of matters which significantly affect the environment; and*
> 3. *ensuring that measures adopted should be cost-effective and not be disproportionate to the significance of the environmental problems being addressed.*

10 See s 4 Investment Mandate.

11 https://naif-gov-au.industry.slicedtech.com.au/wp-content/uploads/2017/07/FINAL-Corporate-Plan-2016-17.pdf, at p 8-9

In relation to the approach the Board takes to environmental and public interest considerations during project assessment and approval, the Governance framework is let down by the approval of policies which are inconsistent with the Investment Mandate.

At section 17, the Investment Mandate requires that the NAIF "have regard to Australian best practice government governance principles and Australian best practice corporate governance for Commercial Financiers when performing its functions, including developing and annually reviewing policies with regard to:

a) environmental issues;
b) social issues; and
c) governance issues.

The requirement that the NAIF have regard to Australian best practice government governance and best practice corporate governance for Commercial Financiers is not operationalized in any of the NAIF's published policies. In fact, the polices seem to urge an approach that is not best practice.

The NAIF's *Environmental and Social Review Transaction Policy* fails to make any mention of climate change or ESD principles. In relation to regulatory, environmental, social and Native Title requirements it treats them broadly, stating:

> *The Board considers its regulatory, environmental, social and Native Title requirements are met when expert regulatory, environmental, social and Native Title due diligence reviews on which NAIF has reliance confirms (or otherwise) that all relevant approvals have been obtained.*[12]

The Policy (and the Investment Mandate –s 15) states that the Board may make an investment decision prior to a project receiving all such approvals.[13]

It is difficult to reconcile the approach articulated in the *Environmental and Social Review Transaction Policy* with either the best practice requirements at s 17 of the Investment Mandate or the mandatory requirement that the Board consider the public interest of a project.

An accurate assessment of public benefit will be exceedingly difficult without the benefit of considering things like an environmental assessment report. This will be particularly true of projects, which, because they exceed the $50 million threshold, will be subject a cost benefit analysis by virtue of the NAIF *Public Benefit Guideline.*[14]

Rejection notice & consideration by the Minister

The grounds upon which the Minister can reject the provision of financial assistance - following a decision of the NAIF to grant financial assistance - are confined by section 11(5) of the Act. Those grounds could be usefully expanded to include, for example, if the provision of financial assistance would have the effect of breaching an international agreement to which Australia is a party.

12 NAIF Environment and Social Review of Transaction Policy 2016, p 2.

13 See s 15 of the Investment Mandate. Also, noting that funding will not be provided until review of the approvals required has been achieved to the satisfaction of the Board.

14 See NAIF Public Benefit Guideline, p 3

b) the adequacy of the NAIF's Investment Mandate, risk appetite statement and public interest test in guiding decisions of the NAIF Board:

The Investment Mandate, risk appetite statement and public interest test are patently inadequate mechanisms for guiding decisions of the Board. Each of the documents should include clear criteria and unambiguous definitions as well as requirements for public consultation to adequately guide the decisions of the Board. A high level of public scrutiny and involvement is required to ensure that decisions are truly in the public interest and that the NAIF is a responsible investor of public funds. Finally, to ensure that the levels of investment return and public policy outcomes are commensurate with assumed risk the Investment Mandate should include portfolio benchmark return requirements.[15]

When assessing NAIF loan applications, the NAIF is likely to experience inherent difficulty when attempting to apply any useful public interest test within the context of a high risk appetite.

The investment mandate introduces two potentially conflicting mandatory criteria that project proponents need to meet:[16]

1. the project will be of public benefit; and

2. the project is unlikely to proceed, or only at a much later date, without NAIF financial assistance.

Without appropriate qualification, the need for a public subsidy potentially undermines the public benefit if it encourages the NAIF to invest in projects that are high risk and low return. This is of particular concern given the broad decision-making discretion, limited transparency and lack of requirements to direct funding consistently with positive environmental outcomes or minimal adverse impacts.[17]

The Productivity Commission has identified that the level of actual assistance conferred by a NAIF concession is difficult to quantify as are the contingent liabilities incurred by the NAIF:

> *Concessions may be lower interest rates, longer loan periods and different repayment arrangements to those required by the private sector, such as repayment holidays. The level of assistance conferred by the concession is difficult to quantify, especially when several types of concession are combined. The largest component is usually the value of the interest rate discount, where the 'grant equivalent' depends mainly on the size of the loan and the difference between the market interest rate and the rate charged under the facility. The contingent liabilities incurred by the NAIF, which convert to real liabilities if the firms find themselves unable to repay or refinance their loans, are particularly difficult to quantify (Australian Government 2016b).*[18]

15 Clean Energy Finance Corporation Investment Mandate Direction 2016 (Cth) s7.

16 Northern Australia Infrastructure Facility Investment Mandate Direction 2016 (Cth) s 7(2)(a), Schedule 1.

17 For example, to encourage environmental improvement or green infrastructure that in turn improves 'ecosystem services' (benefits that nature provides to humans, which are often invisible to traditional cost-benefit analysis) and climate resilience of human settlements and ecosystems.

18 Productivity Commission, Trade and Assistance Review 2015-16 (July 2017) 42.

This emphasises the difficulty in capturing all of the factors that increase the public cost of the project; for example, impacts on the labour market if one project or industry is favoured over another, loss of jobs in competing industries or States in declining markets, and the value of the benefit itself to a proponent in terms of market advantage.

The public benefit guidelines do not appear to assist Board members to accurately recognise the inherent difficulties raised above when assessing the public benefit of a project.

The public benefit criteria is not a suitable public interest test

Under the Investment Mandate, the Board must only grant financial assistance to Proponents who demonstrate the proposed Project will be of 'public benefit'[19]. This is not a public interest balancing test as suggested by the TOR; it is a cost benefit analysis.[20]

A 'public interest' test is a three-step process involving:

1) Identifying public interests in favour;
2) Identifying public interests against; and
3) Determining where the balance lies.

There is no clarification in the Investment Mandate on what is meant by public benefit, and no mention of public benefit in the *Northern Australia Infrastructure Facility Act 2016.* Thus, the NAIF Board had broad discretion in determining the public benefit test before publishing its Public Benefit Guideline (**the Guideline)** in June 2017.

The Guideline reiterates that NAIF will only approve Projects that will be of public benefit. Public benefits are defined in the Guideline as '*benefits of the Project not captured by the Project Proponent*.[21]' The Guideline purports to outline how the Board will assess the public benefit of a Project prior to making its decision[22]. However, this is not provided in any useful detail. The Guideline only stipulates that the Board must be provided with a Public Benefit Analysis (**PBA**) from the Proponent. No indication is given as to how the PBA is then assessed and relied upon in the decision-making process.

Under the Guideline, the Board is only to approve projects that have '**net public benefit**', meaning the benefits of the Project are greater than the costs, excluding benefits received and costs borne by the Proponent[23].

Where the proposed NAIF Investment is $A50 million or greater (such applications are to be given preference under the Investment Mandate[24]), the Board will require a Cost Benefit Analysis (**CBA**) of the Project's Public Benefit. This CBA can be based on both qualitative and quantitative data. The Guideline stipulates that, at a minimum, the following three types of impacts that generate benefits and costs should be included:

- **Impacts on the economy and productivity**;

19 Northern Australia Infrastructure Facility Investment Mandate Direction 2016 Schedule 1.

20 Compare this to the public interest balancing test in Freedom of Information Act 1982 (Cth) s 11B.

21 Public Benefit Guideline, 3 Background.

22 Public Benefit Guideline, 1 Purpose.

23 Public Benefit Guideline, 4 Policy

24 Northern Australia Infrastructure Facility Investment Mandate Direction 2016 Schedule 2

- **Impacts on individuals; and**
- **Impacts on the community[25].**

The CBA must involve 'aggregating the impacts on members of the community' and where possible, 'consider a range of possible scenarios in addition to the base case.'[26]

We are very concerned that the Public Benefit Guideline contains no requirement to expressly consider the potential harm that a project will have on the environment. The current approach is inconsistent with the ESD principle of assessing the full environmental costs of decisions through 'improved valuation, pricing and incentive mechanisms'.[27] The economic cost of environmental impacts (quantitative and qualitative) should be expressly included as a public interest factor. An associated policy should set out the methodology for assessing the economic costs of environmental impacts,[28] and include a default social cost of carbon, as applied in other jurisdictions.[29]

Where the proposed Project is valued at over $A100 million, NAIF must consult Infrastructure Australia and may also consult with Government stakeholders and independent experts on the analysis provided. There are no indications of what constitutes a consultation for these purposes.

Issues with Public Benefit Guideline

Process undertaken by the Proponent

The process for producing a PBA is undertaken by the Proponent alone. This raises concerns with reliability, transparency and impartiality of the result. As Richard Mulgan noted when discussing the role of government bodies in disclosing information under freedom of information legislation, 'it is appropriate that the government should not act as a judge in its own cause but should refer the decision to an independent body.[30]' Analogy can be drawn with Proponents analysing the public benefit of their own Proposed Projects.

The information used to generate the PBA is sourced solely by the Proponent. There is a significant risk that factors in the Proponent's favour will be overstated and overweighted in the PBA.

---

25 Public Benefit Guideline, 4 Policy

26 Public Benefit Guideline 4 Policy

27 See *EPBC Act 1999* (Cth) s. 3A(e). See also *Intergovernmental Agreement on the Environment* (1992) at 3.5.4 on improved valuation, pricing and incentive mechanisms: '*environmental factors should be included in the valuation of assets and services'.* Available at: http://www.environment.gov.au/about-us/esd/publications/intergovernmental-agreement.

28 See, for example, State of Queensland (2003) Environmental Economic Valuation: An introductory guide for policy-makers and practitioners. See also NSW Government (2015) *Guidelines for the Economic Assessment of Mining and Coal Seam Gas Proposals*.

29 For example until recently the USA Environmental Protection Agency had a standard social cost of carbon to be used in evaluating policies fixed at $US37 per tonne, see High Country Conservation Advocates, Wildearth Guardians, and Sierra Club v United States Forest Service & Ors (2014) USDC Colorado, before Judge R.Brooke Jackson. See also Tol, R. (2012) "On the uncertainty about the total economic impact of climate change", Environmental and Resource Economics, vol. 53, no. 1, pp. 97-116.

30 Richard Mulgan, 'Perspectives on the Public Interest' (2000) 95 (March 2000) Canberra Bulletin of Public Information 5, 9

For Projects falling under the $A50 million threshold, the Guideline provides no instruction or indication as to what factors are to be considered when generating the PBA. A Public Benefit need only 'be clearly demonstrated to the satisfaction of the Board.[31]' The Proponent is left with the discretion to decide which type of impacts are to be included, and therefore, exercises a level of control over the form the PBA will take.

The risk of an imprecise and skewed PBA is heightened by the lack of review mechanisms provided for in the Guideline. At no stage in the process of generating a PBA or CBA is there chance for objective review of the information provided. For example, there is no requirement for independent peer review of the economic assessment. There is no opportunity for public submission, denying third parties with relevant insights an opportunity to contribute to improvement of a PBA. There is also no requirement for publication of the PBA, which is given only to the Board for the purposes of making the Investment Decision.

Transparency, community engagement, public submission processes and provision for merits review of a decision are essential components of an anti-corruption regime.[32]

Methods used to calculate impacts under PBA

The Guideline provides no guidance as to the methods or models used to calculate the impacts under the PBA or CBA. There is an inherent risk that unreliable models and unrealistic assumptions will be adopted to produce analyses that then form the base of the PBA. The Productivity Commission cautions '[h]istory suggests that there is *systemic* 'optimism bias' in assessments of the spillovers and flow-on effects, not least in how much employment is generated.'[33]

This was the case in *Adani Mining Pty Ltd v Land Services of Coast and County Inc. & Ors*[34] where the economic assessment methodology relied upon in the proponent's Environmental Impact Statement was found to be deficient. One key aspect of the economic assessment was the estimated production of Queensland jobs from the Project. Under the initial Input Output (IO) modelling, it was estimated that 10,000 full time Queensland jobs per annum would be generated by the mine alone at peak operation. When economic experts reviewed the modelling and addressed deficiencies in the IO method as part of the court process, the average annual employment was only increased by 1,206 full time Queensland jobs. The Court found that "*Overall, my conclusions about the financial and economic evidence are that the applicant has overstated certain elements of the benefit of the mine both in the EIS and in the evidence before this Court*".[35] The large discrepancy between the two results demonstrates how sensitive economic assessments are to the modelling techniques, input data and underlying assumptions used. It also demonstrates the benefit of public transparency and interrogation by independent experts (in this case including the Courts). If appropriate economic models are not adopted, this can have a drastic influence on the final outcome, and can detract from the reliability of the economic assessment.

31 Public Benefit Guideline 4 Policy

32 See for example, Independent Commission Against Corruption (NSW), *Anti-corruption stafeguards in the NSW planning system* (2012).

33 Productivity Commission, Trade and Assistance Review 2015-16 (July 2017) 43.

34 [2015] QLC 48

35 At paragraph [575].

There is no guidance in the Public Benefit Guideline on how to conduct the analysis - how to calculate, weight or compare competing impacts. Any reliance on a CBA may be inaccurate if stringent analysis was not undertaken during its production.

Risk Appetite Statement

We are unable to provide detailed comment on the adequacy of the NAIF's risk appetite statement (**RAS**) in guiding decisions of the Board as it is not publicly available. The NAIF's position on provision of the RAS is stated on its website:

> *The RAS is not a public document as it describes in detail the manner in which NAIF's risk appetite and tolerances (qualitative and quantitative) are established and controlled.*
> *Despite being high level, the information that is available on the NAIF website regarding the NAIF's RAS raises some significant red flags in terms of identifying potential conflicts between the chosen level of 'high financing risk tolerance' and the public interest harm caused by adoption of that risk.*

Relevantly, NAIF has identified that:

> *NAIF has a high financing risk tolerance to complement and encourage ("crowd in") private sector participation in financing a Project, which may include a high risk tolerance for concessions in relation to tenor, pricing, repayment terms, cash flow priority, and willingness to partner with Commercial and other financiers.*[36]

In its most recent Trade and Assistance Review, the Productivity Commission identifies that '[t]he risk for the NAIF is more likely to be that some infrastructure projects will fail to cover their operational costs, let alone meet their loan servicing and repayment obligations.'[37]

Some public commentary suggests that this type of issue could arise with respect to Adani's proposed North Galilee Basin Rail Project. Concerns have been raised over the Adani groups significant liquidity issues, the fact that the proponent of the rail line (Carmichael Rail Network Pty Ltd) operates in an off-shore tax haven and claims by the company that it simultaneously requires, but does not need a NAIF loan.[38]

In any event, the NAIF Board should be required to ensure that the risk appetite of the NAIF NAIF accurately reflects the public appetite for risk. The Board must consider whether its risk appetite will protect the public. The current mechanisms have allowed the Board to set a high risk appetite without public consultation. It is completely inadequate then for the Board to assess the *actual* risk to the public interest by virtue of a CBA or PBA submitted by the proponent for the loan. In contrast, it is usual for shareholders (not stakeholders) to set the risk appetite in commercial investment funds:

---

36 Northern Australia Infrastructure Facility, Risk Management Framework (2016) http://www.naif.gov.au/risk-management-framework/.

37 The Productivity Commission 2017, Trade and Assistance Review 2015-16 (July 2017) 44.

38 Mark Ludlow, 'Adani's $16.5b mine has $3b shortfall,' Australian Financial Review (Sydney), 6 June 2017 http://www.afr.com/news/politics/adani-approves-165b-carmichael-mine-20170606-gwl9h7; Michael Koziol, 'It's not critical': Adani says it doesn't even need controversial $1 billion government loan,' Sydney Morning Herald (Sydney), 5 December 2016 http://www.smh.com.au/federal-politics/political-news/its-not-critical-adani-says-it-doesnt-even-need-controversial-1-billion-government-loan-20161205-gt425r.html.

Recommendation 3:

That the NAIF Act be amended to require:

1. a positive return on all investments as a criteria for the grant of financial assistance;
2. public consultation process on development of the Risk Appetite Statement or that the Risk Appetite be restricted to low-medium risk investments;
3. include public consultation at each phase of the assessment process; and
4. independent peer review of economic analysis provided by development proponents.

That the investment mandate be amended to include:

1. portfolio benchmark return requirements;
2. the risk appetite statement; and
3. consideration of environmental impacts and ESD principles as part of any public benefit analysis.

c) processes used to appoint NAIF Board members, including assessment of potential conflicts of interest;

i. Skills and expertise

The threshold for eligibility to sit on the Board is far lower than is appropriate. The Act requires a person to have "experience or expertise in one or more of 8 broad fields.[39] By contrast, for a person to be appointed to the Board of the *Clean Energy Finance Corporation* the Minister is required to be satisfied that a person has:

a) substantial experience or expertise; and
b) professional credibility and significant standing,

in one or more of a variety of different fields as specified.[40]

As a further comparison, appointment to the Board of the Northern Territory Environment Protection Authority requires the Administrator to be satisfied that a person has "skills, knowledge and experience" in a range of different fields.[41]

In addition to the above, we note that despite indigenous engagement being one of 7 mandatory criteria that a project must meet to be eligible for financial assistance under the Investment Mandate, there is no requirement that a Board member demonstrate skill, knowledge or experience in this area before becoming eligible to sit on the Board.[42] Nor is experience with indigenous issues or engagement a field which is deemed relevant to a person's eligibility.[43]

39 See s 15, the Act

40 See s 16, Clean Energy Finance Corporation Act 2012 (Cth)

41 See s 10, Northern Territory Environment Protection Authority Act 2012 (NT)

42 See Schedule 1 to the Investment Mandate.

43 See s 15(4) of the Act

Recommendation 4: The Act be amended to impose a higher threshold for Board members' balance of skills and expertise and members' eligibility, similar to that found in the *Clean Energy Finance Corporation Act* 2012 (Cth).

Recommendation 5: The Act be amended to require the NAIF Board have an Indigenous member. Or, alternatively, require that the Board include a person recognised by Aboriginal and Torres Strait Islander communities as having skills, knowledge and experience working with Aboriginal and Torres Strait Islander people on community engagement, community development or other such relevant issues.

ii. Assessment of conflicts of interest

Part 5 of the Act provides for the establishment of the Board, its functions and the way it conducts its business. Section 15 provides for the appointment of members to the Board. Nothing in the Act specifically provides for the management of conflicts of interest, either actual or perceived.

Despite this, the relevant provisions of the *Public Governance, Performance and Accountability Act* 2013 (Cth) (**PGPA Act**) will apply to the Board and staff of the NAIF.[44] We note that one consequence of the application of the PGPA Act to the NAIF is that the Minister has the power to terminate the position of a board member should they contravene their obligations under ss 25-29 of the PGPA Act.[45]

Notwithstanding the application of the PGPA provisions, and the recent introduction of the NAIF's policy on conflicts of interest, the Act would benefit from the introduction of specific provisions relating to conflicts of interest. This would be consistent with the approach taken to managing conflicts of interest arising for members of the Future Fund Board of Guardians.[46] Division 8 of the *Future Fund Act* 2006 (Cth) provides for specific provisions for the management of conflicts.

To manage conflicts or potential conflicts, that Act:

- imposes a positive statutory duty on board members to inform other board members where a material personal interest arises.[47]
- Allows members to declare a standing interest.[48]
- Restricts voting in certain circumstances.[49]
- Allows for Ministerial declarations in relation to conflicts.[50]

A particular conflict of interest of concern arises where a board member has, or may have, a material personal interest in the outcome of a NAIF decision. The high risk of corruption resulting from any failure to declare an interest underscores the need for clear protective

44 See section 25 - 29 of the PGPA Act.

45 This is in addition to any power the Minister may have to terminate a Board member pursuant to s 21 of the Act.

46 See section 70, Future Fund Act 2006 (Cth)

47 See section 68, Future Fund Act 2006 (Cth)

48 See section 68, Future Fund Act 2006 (Cth)

49 See section 71, Future Fund Act 2006 (Cth)

50 See section 72, Future Fund Act 2006 (Cth)

legislative provisions in this regard. To this end, offence provisions should be in place to protect the public from misuse of public funds for personal gain by board members.

Finally, we note that the superannuation industry has perhaps the most stringent legislative requirements for addressing conflicts of interest.[51] Of interest is the requirement for Registrable Superannuation Entities to maintain a publicly available register of *"relevant duties and relevant interests"*.[52] Applying a similar obligation to the Board would greatly enhance transparency associated with the NAIF and as a corollary would increase the public's confidence in it. Conversely, It is difficult to see why applying an obligation of that nature would be onerous or unreasonable.

Recommendation 6: That the Act is amended to introduce specific provisions relating to conflict of interests and how they are managed. Management of conflicts of interest should be adequately set out in legislation and regulations, and not subject to excessive discretion.

Recommendation 7: That the Act is amended to include offence provisions for Board members or officers who misuse public funds for personal gain.

Recommendation 8: That the Act be amended to impose a statutory requirement for the NAIF Chairperson maintain and make publicly available an up-to-date register of interests for the Board.

d) the transparency of the NAIF's policies in managing perceived, actual or potential conflicts of interest of its Board members;

The NAIF has recently introduced *Conflicts of Interest Policy* in June 2017.[53] The policy applies to conflicts of interests generally and is complemented by more specific policy guidance contained within other policies and procedures (some of which are publicly available, others which are not).[54]

The policy guidance while generally satisfactory is let down by the absence of mandated requirements – either in policy or legislation - for Board members make public notification of their relevant interests. In our view the rationale that lies behind the strict requirements on disclosure of interests for directors of public companies should apply equally to Board members of the NAIF, namely:[55]

- Board members of the NAIF will be privy to detailed information about the financial/social and environmental aspects of a company that applies for finance. That information will far exceed that available to shareholders or the general public; and

- Board members of the NAIF could be motivated / or be perceived to be motivated to make investment decisions based on their personal interests.

51 See for example Prudential Standard SPS 521 made under the Superannuation Industry (Supervision) Act 1993 (Cth).

52 See Prudential Standards SPS 521.

53 NAIF Conflict of Interest Policy

54 See p 3, NAIF Conflict of Interest Policy.

55 See section 205G of the Corporations Act 2001

The provision of a public register of interests will increase public confidence in the NAIF and assure the public that investment decisions are motivated only by application of the Investment Mandate. For example, the NSW Auditor-General recently recommended that State's Planning Assessment Commission (**PAC**) publish an online summary of interests of PAC members, in addition to existing requirements for managing conflicts of interest.[56]

We also note that none of the policies appear to feature the consideration of conflicts before an appointment is made, for example, to the Board or as CEO. Appointment procedures (or statutory requirements) should be put in place requiring an incoming person to disclose all relevant interests prior to taking up the appointment.

At section 3.3 of the *Conflicts of Interest Policy* the use of information barriers is heavily relied on as the predominant tool for the control of conflicts of interest that have been identified. Information barriers, also known as 'Chinese walls', are commonly used in an attempt to prevent disclosure of confidential information within organisations, particularly where a member of the organisation has a potential or actual conflict of interest with part of the organisation's business. However, they are not always an appropriate or effective way of managing these risks.

In the South Australian Supreme Court in *Pradhan v Eastside Day Surgery Pty Ltd*,[57] Bleby J was very critical of the use of information barriers in small firms particularly, stating:

> *It will only be in very rare cases, if at all, that a "Chinese wall"…will be sufficient protection. There will always be a risk that some confidential information will be inadvertently revealed across the wall…This is particularly so where there is an attempt to place an information barrier between people who are accustomed to working with each other, and it likely to be almost impossible in a relatively small firm.*[58]

While the large size of organisations and compartmentalised operations within organisations *can* be factors that improve a barrier's chance of success,[59] even in large firms information barriers can be ineffectual in managing the potential risk of conflicts of interest.[60]

According to the NAIF Corporate Plan 2016-17, the NAIF has "access" to 120 FTE staff, however, that majority of those are actually Efic [1]staff to which the NAIF has access. As far as we can determine the NAIF itself actually only employs 10.6 people (FTE). In relation to the Board, the NAIF website notes it is made up of a group of seven people and, under the Act 2016, quorum for a board meeting is four members where the board is six or more people (it is currently seven).[61] If members are excluded from discussions and/or votes due to conflicts of interest, there is increased risk that a quorum cannot be met.

---

56 NSW Audit Office (2017), *Assessing major development applications*, available at: http://www.audit.nsw.gov.au/publications/latest-reports/performance/assessing-major-development-applications/recommendations/3-recommendations.

57 (1999) SASC 256.

58 Ibid, at [52].

59 Fruehauf Finance Corporation Pty Ltd v Feez Ruthning (1991) 1 Qd R 558.

60 Ibid; Newman v Phillips Fox (1999) WASC 171.

61 Northern Australia Infrastructure Facility Act 2016, s24(a).

As noted above, where the effectiveness of information barriers have been scrutinised by courts, it has commonly been seen as unrealistic to expect a small group of people, working closely together, to maintain strict confidentiality with each other.

Considering the size of the NAIF, both its board and staff, information barriers are likely to be an ineffective measure to adequately manage conflicts and perceived conflicts[2].

e) the adequacy of the *Northern Australia Infrastructure Facility Act* 2016 and Investment Mandate to provide for and maintain the independence of decisions of the Board;

In our view, the Act fails to sufficiently provide for and maintain the independence of decisions of the Board.

The Minister's powers to appoint NAIF Board members, control the assessment process through the Investment Mandate and ultimately to veto a grant of financial assistance fetter the powers of the Board and prevent it from exercising independence.

Concerns about the independence of the NAIF have led to the inclusion of the NAIF as a potential performance audit topic for the Australian National Audit Office on the program entitled *Northern Australia Infrastructure Facility.*[62] Additionally, the Productivity Commission recently concluded that 'the lack of transparency to date and the promotion of certain projects by politicians (in the absence of credible supporting investment data) has raised concerns about the viability of future investments under the NAIF.'[63]

We support additional mechanisms in the Act to protect the NAIF from political influence and to ensure that the NAIF makes decisions based on the merit of an application against the eligibility criteria. These should include specific criteria in the NAIF Act, supported by clear definitions for terms such as 'public benefit' and 'relevant regulatory, environmental and Native Title approvals'.[64]

Recommendation 9: That the Act be amended to include the criteria for a grant of financial assistance to a State or Territory, the role of a proponent and the requirements for applications for grants of financial assistance.

f) the status and role of state and territory governments under the NAIF, including any agreements between states and territories and the Federal Government.

There is a distinct lack of transparency around how NAIF delivers finance through the Queensland, Western Australian and Northern Territory Governments. This lack of transparency extends to the nature, structure and purpose of agreements between States and Territories and the Federal Government, including the impact on a grant of financial assistance if a State or Territory exercises its veto power under subsection 13(4) of the Investment Mandate.

62 Letter from Auditor-General for Australia to Wayne Swan MP, 19 July 2017 https://www.anao.gov.au/work/request/northern-australia-infrastructure-facility.

63 The Productivity Commission 2017, Trade and Assistance Review 2015-16 (July 2017) 45.

64 Northern Australia Infrastructure Facility Investment Mandate Direction 2016 (Cth) s 15.

The lack of transparency has resulted in the States and Territories themselves failing to clearly communicate their role under the NAIF. Queensland in particular has failed to disclose the nature of its role as a conduit of NAIF grants by virtue of its requirement to be the recipient of any grant of financial assistance pursuant to sub section 7(1) of the Act for Adani's North Galilee Basin Rail Project.[65]

The Commonwealth's legal power to fund projects through the NAIF is granted by section 96 of the Constitution. Under the grant power, the Commonwealth may grant financial assistance to a State or Territory for particular projects, but only if the assistance passes first to the State or Territory.[66] Despite this, Queensland's Treasurer, has stated that 'any project financing approved by the independent NAIF board will flow between the Federal Government and a project proponent.'[67]

Relevantly, the NAIF's decision-making power set out in section 7 of the Act provides that:

> *(1) the functions of the Facility are*
>
> > *(a) to grant financial assistance to States and Territories for the construction of Northern Australia economic infrastructure; and*
> > *(b) to determine terms and conditions for the grants of financial assistance; and*
> > *(c) as agreed between the States and Territories, to provide incidental assistance to the States and Territories in relation to financial arrangements related to the terms and conditions of the grants of financial assistance.*
>
> *(2) The Facility has the power to do all things necessary or convenient to be done for or in connection with the performance of its functions.* [68]

The powers in subsection 7(2) are bound by the Minister's power to give, by legislative instrument, directions to the NAIF about the performance of the NAIF's functions.[69] These directions are stated in the Investment Mandate.[70] In carrying out its functions, the NAIF must take all reasonable steps to comply with the Investment Mandate.[71]

---

65 Curtis Pitt, 'Northern Australia Infrastructure Facility' (Media Statement, 29 May 2017).

66 The High Court has determined that it is not necessary that the grant benefit the State or Territory directly: A-G for Victoria, ex rel Black v Cth (DOGS Case) (1981) (State Aid Case) 146 CLR 559.

67 Curtis Pitt, 'Northern Australia Infrastructure Facility' (Media Statement, 29 May 2017), cf information from the NAIF website stating "[t]he Queensland, Northern Territory and Western Australian Governments will work with the NAIF through the on lending of NAIF investments to project proponents. The involvement of the states and territory will help to maximise the gains from infrastructure investment in northern Australia."

68 NAIF Act s 7.

69 NAIF Act s 9(1).

70 NAIF Act s 9(2).

71 NAIF Act s 9(3).

Read on its face, section 7 of the Act empowers the NAIF to provide grants of assistance and incidental assistance *to* States and Territories. This power does not extend to the grant of assistance to a project proponent, unless it is necessary or convenient to be done in connection with the performance of its functions.[72]

Power to 'veto' the provision of funding to a Project

Subsection 13(4) of the Investment Mandate specifies the power of a state or territory government to prevent the NAIF from providing funds to a project by notifying that financial assistance should not be provided to a Project.

This subsection specifically states:

> *'(4) The Facility must not make an Investment Decision if at any time the relevant jurisdiction provides written notification that financial assistance should not be provided to a* ***Project****.'*

Section 4 of the Investment Mandate provides for the following definitions:

> ***Project*** *means the infrastructure activity that is the subject of the* ***Project Proponent's Investment proposal.***
>
> ***Project Proponent*** *means the entity responsible for a Project.*
>
> ***Investment Proposal*** *means the application submitted by a Project Proponent.*

The power under subsection 13(4) of the Investment Mandate to 'veto' the provision of funds to a project may therefore be used for a single application by a proponent for a project that is an infrastructure activity. However, this power is only provided as a 'direction' of the Investment Mandate 'about the performance of the NAIF's functions' per subsection 9(1) of the Act. The NAIF must only take 'all reasonable steps' to comply with this direction. This places some uncertainty as to whether or not the NAIF must ultimately comply with a direction provided under subsection 13(4).

Terms and conditions imposed or agreed for provision of financial assistance

The NAIF may, under subsection 7(3) of the Act, 'determine terms and conditions for the grants of financial assistance.' Also, under subsection 7(4) a function of the NAIF is 'as agreed between the NAIF and the States and Territories, to provide incidental assistance to the States and Territories in relation to financial arrangements and agreements related to the terms and conditions of the grants of financial assistance'. These subsections therefore give the NAIF the power to determine terms and conditions for grants either without agreement with a state or territory jurisdiction, or by entering an agreement with a state or territory government with respect to the provision of financial assistance.

The NAIF Confidentiality Policy, dated February 2017, refers to a 'Master Facility Agreement' having been entered into between the NAIF and the relevant states and territory and the Federal Government.[73]

---

72 NAIF Act s 7(2).

73 Confidentiality Policy, Australian Government and Northern Australia Infrastructure Facility, February 2017, p4, https://naif-gov-au.industry.slicedtech.com.au/wp-content/uploads/2017/04/NAIF-Confidentiality-Policy.pdf.

The Queensland Government has publicly confirmed it has entered into such an agreement,[74] which may be an agreement for incidental assistance made under subsection 7(4) and which appears to affect the operation of the provision of financial assistance for Queensland projects.

As the Master Facility Agreement is clearly a key document determining the terms and conditions of grants of financial assistance (the primary function of the NAIF facility) public access to this agreement is necessary for accountability and good governance.

Recommendation 10: That the Act is amended to include the requirement for any agreement/s under section 7 to be made publicly available, regarding either the provision of financial assistance to States and Territories, or related to the terms and conditions of such grants.

74 Media Statement, Treasurer and Minister for Trade and Investment, Hon Curtis Pitt, 29 May 2017, http://statements.qld.gov.au/Statement/2017/5/29/northern-australia-infrastructure-facility.